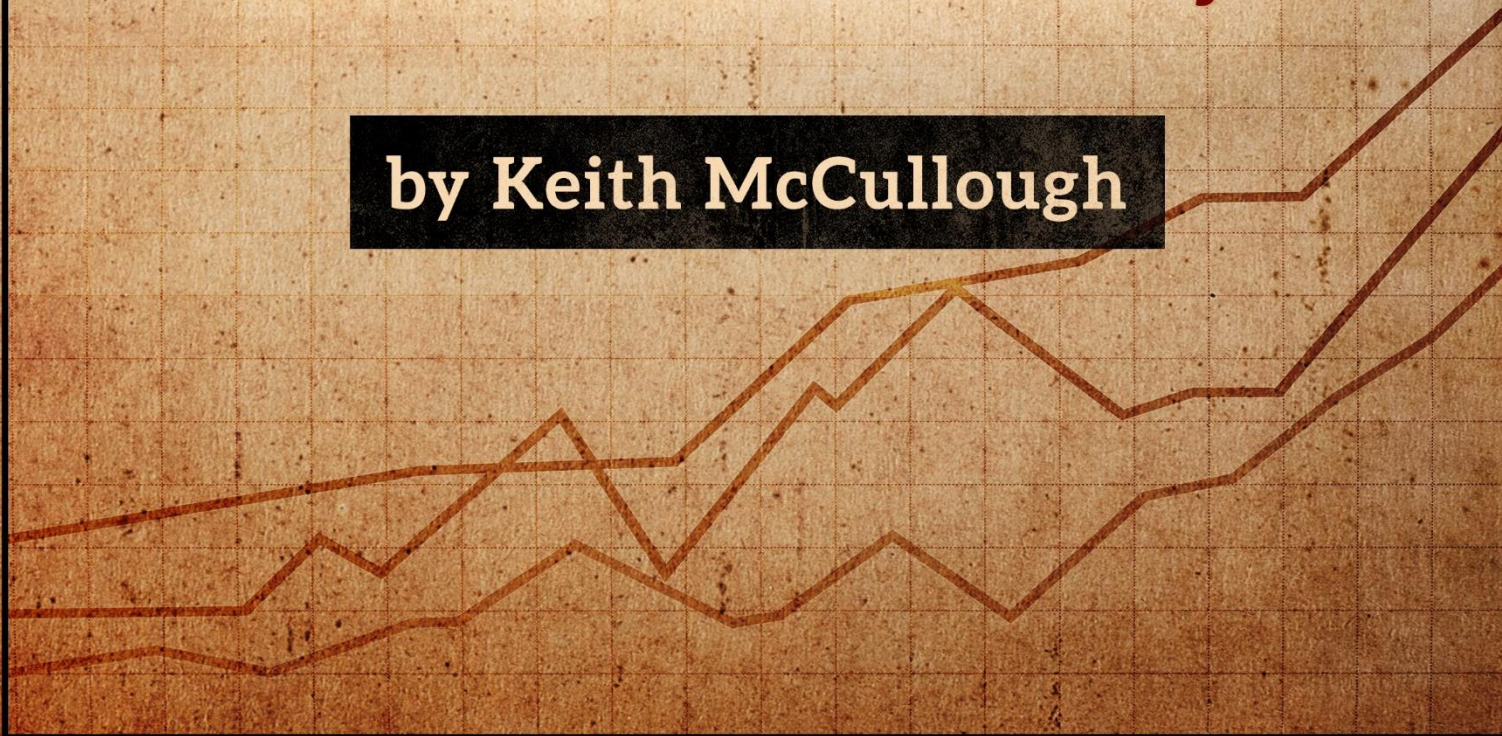




MASTER THE MARKET

*A Hedge Fund Manager's
Guide to Process and Profit*

by Keith McCullough



Praise For “Master The Market” & The Author...

“This book is an essential read for any person interested in investing and learning from a true expert that has proven his track record by following a strict process, unparalleled data analysis, and a solid method. I have known Keith McCullough for almost two decades and he is one of the brightest minds in finance and economics.

We come from a similar background in hedge fund asset management, and he provides a unique perspective that may assist readers, ranging from experienced investors to those who want to start to understand the reality of markets and the economy, in a clear and helpful way. In this book, Keith debunks many of the myths repeated by mainstream financial services while offering highly valuable advice and the methodology that can help readers invest in the most profitable way and secure their financial future. A must read.”

-Daniel Lacalle, PhD, Chief Economist at Tressis and Fund Manager, Author of Escape from The Central Bank Trap

"I run a \$1 billion hedge fund, and I rely on Keith's research and insights every day. Hedgeye is like an outsourced research arm, with top analysts and—most importantly—amazing quantitative macro insights. No one works harder than Keith to help investors compete against the Wall Street machine. He has a top quantitative mind and a rebel heart.”

-Dan Rasmussen, Founder & Portfolio Manager at Verdad Capital

“Discipline, rigor, resilience, consistency, and putting your teammates ahead of yourself are the hallmarks that the best athletes and best hedge fund managers both possess.

Keith McCullough embodies all of these. His breadth and depth of knowledge can help any investor trying to improve their performance returns. This is a must read for the curious minded.”

-Dr. Gio Valiante, Performance Coach & Psychologist, Former Head Performance Coach at Point 72 Asset Management

“Keith is one of a very rare breed. Indeed, it is almost extinct now on Wall Street. The laborious maximus insists on actually doing THE WORK, rather than taking the received wisdom as gospel. It is not easy to be a data grunt and can often result in periods of extreme unpopularity. But, for these determined creatures, getting at the truth is more important than cocktail party invitations. Keith embodies all these unique characteristics, but with one additional facet. Not only does he do the work, but he graciously shares his process with any who will listen. That magnanimity makes him an absolute blessing.”

-Stephanie Pomboy, Founder of MacroMavens

“In my nearly three decades working in financial services with private wealth, C-level executives, and institutions, I’ve rarely encountered an individual as focused and determined as Keith McCullough and the team he captains. Hedgeye’s commitment to protecting investors from significant financial downturns through its rigorous, data-driven approach is unparalleled.

Keith is a rare breed. He has a relentless drive to deliver truth in an industry often swayed by financial incentives. It’s refreshing and absolutely necessary. The diverse range of innovative products Hedgeye has created empowers the community to craft personalized risk management strategies, prioritizing capital preservation above all.

Having engaged with Keith personally over the years, I can attest to his profound dedication not just in business, but also in life. His core values of honesty, trust, loyalty, and integrity extend beyond work to his family and friends, inspiring excellence in everyone around him. It's impossible not to champion such integrity and drive.”

Mitchel Krause, Managing Principal & CCO at Other Side Asset Management

“Unlike the rest of us, Keith McCullough lives and breathes markets. Where I may see only numbers on a screen, Keith can sense, behind the digits, the racing hopes and fears of speculators; and, behind those, he can map out the topography of invisible supply and demand curves that extend across continents.

So when he explains what and when to buy or sell, don’t imagine an algorithm you can translate into your order bot. Imagine rather learning, from this master teacher, a new way to think about trading as an art and trading as a way of life. When Keith teaches the art, he uses simple parables and brilliant rules of thumb to help you gain confidence. (My favorite: how to use fighter pilot John Boyd’s OODA loop to refresh your market take each morning.)

And when he teaches the way of life, this hardscrabble Xer has the humility to be honest: Any trader sometimes gets it wrong; what the pro knows, and the amateur doesn’t, is how to minimize the damage.”

-Neil Howe, Historian, Economist, and Demographer, Author of numerous acclaimed books including his latest “The Fourth Turning Is Here”

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Foreword

By Mike Taylor

This book is brief and concise. It has figures and tables. You will need a pen to take notes. You will need to review it three times and it is also the most important investing guide you will ever read.

My name is Michael Taylor, Troglodyte with a keyboard. I am the PM of PINK, a healthcare-focused ETF. I have been a PM in the investment arena for the past 25 years, most of which was spent at Citadel and Millennium, the biggest Hedge Funds on Earth. And I ran a multi-billion dollar book with a big team of (super-star) analysts. Before that, I developed drugs as a Scientist.

Keith jokingly calls me “the biggest name in healthcare that you’ve never heard of.” And unless you’re “in the business” you’ve probably never heard of me. We are a silent bunch for one reason: We are forbidden from talking publicly while under contract.

Though I have survived for decades, if not excelled, in many ways, I am an investor just like you, fearful I would fail at every turn and relieved when the portfolio finished green. To this day, I am unsure if by luck or skill, I never had a down year. Through the years, I have crafted and adopted an arsenal of tools that has seen me through to the other side, the most significant of which is the Hedgeye Process. I owe much of my returns and, frankly, my professional survival to Hedgeye.

Back in early 2008, I knew little of Hedgeye and Keith McCullough when he walked into the Connecticut office of Diamondback Capital (now defunct) with a slide deck on Risk Management. I was a newly minted Healthcare PM of a small book (\$140mn), rolling into the shitstorm that was 2008. I had a newborn baby and one on-the-way. My white-knuckled Troglodyte hands knew I had to navigate this. But how? I was on a trial-by-fire journey to figure it out before I got fired. This is the life of a Hedge Fund PM: survival in a foxhole.

My expectations for Keith were low. Every Tom Dick and Harry rolls into my office pitching their solution, all day, every day. And I listen. I have to listen. I wanted to see Keith because he had a “new way” to predict macro transitions and moreover, he was “one of us,” a former PM at a Hedge Fund. I recall the slide deck was rough – an almost home-made print job: No gloss. And then I caught a whiff of the ozone: this was REAL RESEARCH; fresh, gritty and new.

Keith was different. He was a successful PM displaced by the vicissitudes of Wall Street. Lots of PMs were in the same boat, but few can pivot to make lemonade from lemons. Coming from the Buy Side, Keith was positioned to produce unique and refreshing research.

Most investors don’t understand the depravity, conflict and banality of “Old Wall Street Research.” It is total and complete shit. You (the investor) are easy pickings, and your pile of cash is minded by a sociopathic narcissist that thinks of you as a Muppet. Nobody on the Sell Side is a successful PM, critical or ethical. Sell Side research analysts are 99% of the time, dullards who could not cut it on the Buy Side. Research from the Sell Side is inherently compromised by banking deals, as their ‘real’ job is to stuff your face with new paper and tell you “The price target is higher,” full-stop.

That Hedgeye slide deck turned out to be a magical goldmine waiting to be unearthed. In short, Keith disaggregated economic history to describe a back-tested system of four “Quads” that delineated the economic cycle. It was news to me. Nobody had done that before in such a concise way, explaining what to buy, when to buy and more importantly, when to sell.

“SELL” is a word the Sell Side does not use, for good reason: They get FIRED when they say “SELL.” And I realized right there: Keith is a knuckle-dragging Troglodyte just like me, with brilliant analysis that works. My first thought: The Sell Side was going to assassinate him. My second thought: My God I like this guy. I became one of Keith’s first clients and soon a devotee of the Hedgeye Process.

Over the recent decade, Hedgeye has expanded to include all the verticals: Government Policy, Financial Policy, Demographics and very importantly, Micro. Micro means individual stocks and this is an area where Hedgeye excels. The team that Keith & Company have built is nothing short of astounding. It is rare, very rare.

As a PM who has built teams, I confess, it is extremely difficult to assemble and retain top talent: They all have >140 IQ’s, are from the top Universities, expect to make millions and are A+ type personalities. In short, they’re all Gladiators in the making. These Analysts are hard to find, hard to keep and sometimes, frankly, hard to work with.

But has Keith assembled a dream team of Pros for every industry vertical. From Tech to Industrials, China to REITs, Hedgeye has it all. Every one of these analysts would prosper at a hedge fund and, to our benefit, they share their work with the world through Hedgeye. Hedgeye’s hit rate on buy/sell calls is astonishingly high and the research product is deep and rich. A great feature that separates Hedgeye’s research from the rest are “SELL” calls or more importantly, “SHORT.” Hedgeye is the only research outfit I have ever seen that says, “short that stock.” This is something you will never see from Old Wall Street.

Fifteen years later, my process has changed for the better. Hedgeye is the first thing I read in the morning, followed up with Hedgeye’s video productions – “The Call” and the “Macro Show.” I put CNBC on “mute,” and it stays that way all day long.

Hedgeye grew from a daily macro note to a comprehensive, all-encompassing product, predicting macro trends world-wide and micro (single stocks) with 40 Analysts. As the influence and weight of Hedgeye grew, “Old Wall” has tried in earnest to silence the message. Keith has been “cancelled” by the mainstream media as the lone voice calling the Sell Side what it is: frauds. Hedgeye is forcing a seismic change on the Old Wall, forcing them to face the truth: Their Research Sucks.

This book is an owner’s manual to the Hedgeye Process, more importantly, a process to Protect and Prosper. Use it wisely. Use it often. It has been an honor to assist Keith and Hedgeye on this journey.

Lastly, I am like many of you, a paying client of this marvelous product.

-Michael Taylor

INTRODUCTION

The Journey Begins Now: Becoming A Full Cycle Investor

In late 2007, I experienced one of the most jarring experiences of my life.

I got fired.

It's easy to say now but, looking back, it was the best thing that ever happened to me. It's why I built Hedgeye. Thank you for downloading this book, because I'm here to teach you everything I've learned in over two decades working on Wall Street. It's my sincere hope that my experiences and what I've learned will help make you a more resilient, confident and successful investor.

My final day in the hedge fund business was Friday, November 2, 2007.

At the time, I worked as a Portfolio Manager at Carlyle-Blue Wave. The Carlyle Group — already well known around the world for its private equity prominence — was pushing into the hedge fund business. Its new hedge fund arm was called Blue Wave. I was a Managing Director and Partner, the firm also gave me a seat on the hedge fund's Investment Committee. I thought I was on top of the world!

Then, in the summer of 2007, the Carlyle-Blue Wave Credit team blew up. It was an early warning sign on many levels – of the coming Great Financial Crisis.

One-by-one, people around me lost their jobs.

By mid-2008, Carlyle had closed Carlyle-Blue Wave forever, but I'd been long gone by then. I was bearish on the U.S. economy throughout the Summer of 2007 and, even as the economy ebbed closer and closer to the Great Recession, I was early to the short side by a few months (the US Stock Market peaked in November of 2007).

On the morning of what turned out to be my last day in the business, I ducked out of our Midtown office, right before noon, and walked down Fifth Avenue to buy a new pair of black loafers.

The soles of the ones I had on weren't exactly worn out and might have even lasted me another six months, but with my son Jack due to be born in the coming week, I felt it was time to start the next chapter of my life.

So did my bosses at Carlyle-Blue Wave.

Later that afternoon, I was informed that I was being let go. My days trading a “book” for a hedge fund were over. I packed up my things—all of my personal belongings, books, files, and notebooks into a cardboard box, but I left my old shoes in the office. When those dusty loafers were mailed to me a month later, I had already forgotten about them.

But I smiled.

Five days after being fired, my son was born. Nothing sharpens the mind like the existential feeling of being a new father with no job! As I started thinking about what to do next, the seminal moment came when my mom asked me, "How do you change the world with your job?"

My mom asked me that question while we were standing at our lake house in Thunder Bay, Ontario, right on Lake Superior. Building that house for our family was the first thing I did when I started building a successful career on Wall Street.

When I was growing up, my father was a firefighter, and my mom was a teacher. My parents gave me everything they had. It was my parents who instilled in me the work ethic that created all these opportunities – from a knuckleheaded hockey player to captaining Yale's hockey team, to opportunities on Wall Street and ultimately landing at Carlyle-Blue Wave.

While I was never the smartest investor or hockey player, no one outworked me. In the rink, I earned the name "Mucker," a physical player, a grinder. (In the 1996-1997 season, I led the Yale hockey team in scoring and penalty minutes).

That's why, back on Lake Superior after I'd been fired, I started to think about how to respond to my mom's question, "How do you change the world with your job?" I didn't have an answer at the time. Her words stuck with me.

And, as the words rattled around in my thick skull, I did what I always do. I got to work. Out of that, Hedgeye was born in 2008.

Remember, Hedgeye was born around the time the U.S. economy tipped into its greatest downturn since the Great Depression. It's worth remembering the devastation of the Great Recession and how it impacted hard-working Americans. The stock market lost more than 50% of its value from the October 2007 peak to the trough in March 2009. The U.S. Government Accountability Office reported that American retirement plans lost about \$2 trillion in the 15 months between October 2007 and December 2008, which was approximately a 20% decline.

The bursting of the housing bubble caused home prices to fall 30% on average from their peak in 2006 to their nadir in 2009, wiping out trillions of dollars in household wealth. The unemployment rate in the U.S. nearly doubled from about 5% in December 2007 to 10% in October 2009.

Making matters worse, the Financial Crisis exposed the worst of Wall Street: rampant conflicts of interest, a lack of accountability and opaqueness. Complex slicing and dicing of subprime mortgages into an alphabet soup of financial products (MBS and CDOs) that, when combined with easy money Fed policy, created an environment of excessive risk. As with all great crashes in financial market history, excessive leverage amplifies the fallout.

Unfortunately, a lot of Americans got caught up in the carnage.

I tell you this story today because, back when I was bearish and got fired in the summer of 2007, I'd made the classic mistake of being right on my market outlook, but wrong on the timing.

What I didn't fully appreciate at the time was that the market didn't care what I thought it should do. The market was on its own timetable, and I needed to #GetBetter at predicting those precise tipping points.

In the almost two decades since I was fired from Carlyle, my analyst team and I have built our entire risk management process around not screwing that up again. We don't get every call right. But I'd humbly submit that we've built a risk management framework that enables investors to be more right than wrong.

For example:

- *In early 2008, we signaled investors should go to 85% cash.**
- *In April of 2009, we went bullish on US Stocks.†*
- *In 2016, we went long US Stocks.‡*
- *In October of 2018, we signaled buy Bonds and short US Stocks.§*
- *In early 2020, we called for another US stock market crash***
- *Later in 2020, we went back to bullish on Global Equities.††*
- *In January of 2022, we warned investors ahead of a -25% crash in US.‡‡*

I'm leaving out a lot of other important examples, like getting long Commodities in June 2020 when the Fed said inflation was “transitory” and before Copper ripped 60%+. We also nailed a series of highly tactical calls in the time between the European Debt Crisis of 2010-2011 to the Fed-induced “taper tantrum” of 2013.

You get the point. We're proud of our wins. But, then again, we expect to win.

More important, I'm proud of how my teammates and I follow a repeatable process that generates these money-making outcomes for our subscribers.

The secret to our success isn't about gazing into a crystal ball to discover an obvious future. Despite what you'll hear from always confident “experts” on Wall Street TV, financial markets are inherently uncertain. Successful investors must embrace this uncertainty.

The only way to combat uncertainty is to have a rules-based, repeatable process. A repeatable process allows the investor to make high-probability bets over time. Beyond that, a repeatable process enables investors to be more right than wrong and have the humility to change your mind when the facts change.

This is important. When your process tells you that the outcome you are positioned for is now less likely, you don't argue with the data. You change your positioning. I've seen too many investors with a weak investing process fall in love with their positions. Unable to change their minds, these investors become trapped by their own “intelligence.”

I'd put the Hedgeye process up against any successful buy-side hedge fund in the world. Many of these world-class investing organizations already pay us six figures or more for access to our process. (Currently, institutional Hedgeye subscribers manage more than \$10 trillion in assets under management.)

While certain hedge fund managers are forced to focus on the end of day, week, and month performance of their business, I don't have to do that with either the business I'm building or my own personal wealth. If you can personally rotate your hard-earned capital across *Asset Classes*, *Sector Styles*, and *Factor Exposures*, ***The Game*** of compounding returns never ends.

* [Early Look: 85% Cash](#)

† [Early Look: The Great Recession](#)

‡ [Early Look: Quad 2](#)

§ [Early Look: Q&A for QA](#)

** [Early Look: Re-Entering Quad 4](#)

†† [Early Look: Volatility Breakdowns = Bullish](#)

‡‡ [Early Look: Trending VOLATILITY](#)

That's why I call our investment *#process* **Full Cycle Investing**. It's not beholden to Wall Street's daily, weekly or monthly performance problems. All that matters is preserving, protecting and compounding your portfolio over the big fluctuations in the economic cycle.

How is Hedgeye, of all businesses, becoming one of the *longest-term* risk management and investment processes anyone can follow? A: Wall Street consensus investing continues to become more concentrated and *shorter-term*.

Since consensus 60/40 and American 401k portfolios have never been more concentrated, that amplifies the absolute panic you've been seeing on both the upside and downside since 2020.

The manifestation of super-short-term "hedging" and speculative options trading have very obviously amplified this part of *The Game*. Since 2021, *0DTE* (Zero Days to Expiration) *Options* have bubbled up to greater than 50% of *The Game's* daily options flow! Since zero days is the ultimate short-term game, this provides those of us playing the **Full Cycle Investing** game major longer-term opportunities.

Now that I've completely stirred the *Old Wall Street* pot, let me do some more of that asking you some important questions?

- A) Would you prefer a concentrated or diversified portfolio?
- B) Would you prefer to take on 10-30% *Drawdown Risk* in your portfolio or not?
- C) Would you prefer your portfolio's pile to be at all-time highs this morning or not?

To be crystal clear, I used to play *The Game* on the end of day, week, and month performance rules. While I made a pile doing that A) I was doing it with OPM (other people's money) at hedge funds and B) I was a very concentrated investor.

As an older man with a much larger pile, I don't want to do it that way with my own money.

So, let's separate what some of you are paid to do while running other people's money versus the *Full Cycle Investing* game I'm playing which A) prioritizes **#P3** (preserving & protecting **#ThePile**) so that B) I can compound returns...

And now you can start to "see" why Hedgeye's longer-term vision is starting to become more obvious to more people.

Again, that's why we call our go-anywhere Macro approach, with its emphasis on risk management, Full Cycle Investing. This proven process combines...

- Proprietary and quantitative-based risk management signals
- Top-down Macro analysis; along with
- Bottom-up fundamental research

By the end of this book, I'll have laid out this entire process and will likely have convinced you to become a Full Cycle Investor. Hedgeye is here to help you get the big moves in markets right.

First and foremost, we help preserve and protect your portfolio.

The opportunities that come from preserving and protecting your wealth are underestimated by most investors. Investors going through large drawdowns of their capital can't redeploy it when compelling opportunities appear. These investors are too busy cleaning up yesterday's mess to proactively identify the next big market move.

All of this boils down to the idea that you've worked too damn hard to lose -20%, -30% or -50% of your hard-earned capital.

Q: *Do you know what your portfolio has to be up to recover from a -20% drawdown?*

A: 25%

Let's take a more extreme example of this drawdown math. Someone who invested in Bitcoin at the 2021 peak lost -78% by the time Bitcoin bottomed. That requires a +354% return just to get back to breakeven. If you bought the 2021 peak, it took almost 3 years for Bitcoin to get back to breakeven. Surely, there was something better to do with your money over that painful period where cryptocurrencies were finding a bottom!

Making poorly-timed investing decisions can have a profound impact on your wealth. It can also affect the well-being of your family. At the end of the day, investing is about compounding. A catastrophic error like buying the peak in Bitcoin takes you out of the game.

DRAWDOWN	PERCENT CHANGE TO GET BACK TO BREAKEVEN
-10%	+11%
-20%	+25%
-30%	+43%
-40%	+67%
-50%	+100%
-60%	+150%
-70%	+233%
-80%	+400%
-90%	+900%

One of the biggest problems for anyone actively managing their own money is the inability to distinguish between skill and luck. Unchecked, our monkey brains have evolved to attribute every successful outcome to skill.

Meanwhile, bad results are attributed to factors outside our control. This line of thinking—judging your decision based on the results—doesn't evaluate your actual decision-making process. You can make a bad (lucky) decision that generates a successful outcome and make a good (skill-based) decision that's a loser.

World Series of Poker winner and former professional poker player Annie Duke explains this concept in her book, "Thinking in Bets: Making Smarter Decisions When You Don't Have All the Facts." Duke calls this phenomenon "resulting." Resulting," Duke explains, refers to the cognitive bias where people judge a decision based on its outcome, rather than on the quality of the decision at the time it was made.

"Resulting" leads people to create overly simplistic narratives about why success or failure happened. If the outcome is good, the decision was good; if the outcome is bad, the decision was bad. This can distort learning and growth, as it prevents a clear understanding of how decisions impacted outcomes independently of luck or external variables.

The top performers in *The Game* accept that the world is filled with uncertainty, but place high-probability bets when the odds are in their favor. It's important to note that the world's best investors expect their edge relative to the broader market to be a success rate of between 55% and 65%.

Another way of saying that is these investors expect to be wrong 45% to 35% of the time. And that's for pros playing at the highest level! This is a far cry from the certainty you hear on mainstream finance TV, where the line of questioning is always, "are you all-in?" on a particular trade.

What the pros know (and what I intend to convince you of in this book), is that the compounding effect of high-probability decision making is how the best investors preserve, protect and grow their wealth.

In other words, the best way to combat "resulting" is to have a repeatable decision-making process for investing. Your decisions need to be surgical. You need a decision-making process for when to get into an asset class and when you'll get out.

This latter point is very important: A lot of people are very effective in convincing you to get into an asset, but who gets you out?

Wall Street convinces most investors to buy and hold something by pitching the comfort of long-term averages. That's just Wall Street collecting fees and taking your money. Sure, over the long-term, the S&P 500 goes up 6-7% annually on average after adjusting for inflation. But while the long-term average could be a useful starting point, it doesn't provide the whole picture. Just because something happens 80% of the time under a particular set of historical conditions doesn't mean that pattern will repeat in the future. "What matters is the particular, not the average," is a fantastic quote by the father of fractal math Benoit Mandelbrot in his seminal book *The Misbehavior of Markets*.

There's a very real cost to owning something for the long-term and weathering those painful periods where that asset class goes down -10%, -20%, -30% or more in your face.

Let's take a quick example. You're about to retire, a -20% correction is coming, and you just can't see it. This isn't theoretical either. The classic 60-40 portfolio, where stocks make up 60% and bonds 40% of a total portfolio, is supposed to be diversified. But, in 2022, those 60-40 portfolios were down -17%.

Here's another example. Target date funds are designed to "lower risk the closer you are to retirement." Target Date Funds, regardless of how close you were to retirement, were down -13% to -20% in 2022. In 2022, the median return for a target date fund designed for someone retiring in 2025 was down -15.4%. I want to emphasize this point. This fund was designed for someone retiring in just 3 years and it fell -15.4% in 2022!

That doesn't sound like "lowering risk the closer you are to retirement" to me.

IS THIS DIVERSIFICATION?

Wall Street's "diversified" 60-40 portfolio of stocks and bonds has been struggling since late 2021.



Source: FactSet

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Most investors aren't equipped with the right tools needed to navigate the business cycle. The inevitable jumps up or down can periodically tilt the odds in your favor where you can either buy every damn dip in risky assets OR get the hell out and put your precious capital into more promising opportunities.

Drawdowns are painful.

The long-term averages aren't signal.

Think about an earthquake. In preventing a catastrophe, seismologists have developed a series of real-time, precise tools (seismographs and accelerometers) to spot early warning signs then issue signals. The average of what's happened in the past isn't predictive.

There's a better way to invest that provides peace of mind and generates long-term success. At Hedgeye, we monitor markets every day to identify when an asset starts to shake and then break.

Rest assured that there are particular points in market and cycle time when particular moves matter. When you get those signals, you don't ask questions. You act.

What I'll teach you in the pages to come is my repeatable risk management process for doing exactly that. I'll explain why I developed this process over the past two and a half decades.

Importantly, all of the tools we've developed and decision-making frameworks in this book are born out of past (often painful) mistakes. I'll share stories of those mistakes to illustrate why the Hedgeye process is a #BetterWay to invest.

A quick word of caution but also a challenge. The process I'm about to teach you is not going to be easy. There are no shortcuts to investing success. If you're not looking to #GetBetter each and every day, if you're not trying to preserve, protect and grow your precious capital, if you don't want hedge fund quality insights relied upon by the world most successful institutional investors, I strongly recommend you rethink that as you read this book.

But if you are interested and committed to #GettingBetter each and every day, if you're excited to preserve, protect and grow your capital, if you want to get investing insights that are battle-tested by the best hedge funds in the industry, then this book is for you.

By the time you're done reading this book, I'm going to convince you of this: Hedgeye is the **first and only risk management service for the self-directed investor**.

What you don't know yet is that "risk management," done the Hedgeye way, is a lifestyle. It's not just a way of thinking about markets, but also a way of approaching your life. That might sound weird when you first read it. But managing your money properly and safely, without large drawdowns, allows you to compound your hard-earned capital and unlock unlimited possibilities for your family.

I know the impact that the Hedgeye process has on our subscribers and their families. We get emails all the time from the hard-working people of #HedgeyeNation thanking us for protecting and growing their capital so they can...

- Send their kids to college
- Provide a comfortable retirement for their elderly parents; or
- Build wealth with confidence in order to plan for an even brighter future

Those letters from Hedgeye subscribers give me hope.

I've heard too many horror stories from people who have tried "investing newsletter services" from so-called Wall Street "gurus." It's human nature to be tempted by these get-rich-quick schemes. But I guarantee those newsletters leave you unprepared the next time the stock market crashes.

Drawdowns like this are unacceptable here at Hedgeye. Since 2008, we have never missed preparing the hard-working people of #HedgeyeNation for a major U.S. market crash. I'm proud of that. I know it enables hard-working people like you to prepare your family for a better future.

That's why we're not a newsletter business selling stock picks. We're a risk management service teaching you a process and a #BetterWay to invest.

Wall Street has sold a lot of people a lot of BS narratives over the years. Rest assured, there's a lot of money being spent perpetuating those narratives. You're going to unlearn those bad habits. I'm going to teach you the Hedgeye process. I've lived this process day in/day out for more than 15 years now. I know it's a recipe for long-term success in markets. Believe in yourself and join me on this journey.

Before we get started, I'll leave you with a final quote from legendary NFL coach Bill Walsh. Walsh created the "West Coast Offense," which completely revolutionized the way football is played. During his tenure as San Francisco 49ers head coach from 1979 to 1988, he led the team to three Super Bowl victories. *When you focus on the process of making great decisions, Walsh said, "the score takes care of itself."*

It's time to become a Full Cycle Investor. Let's do this.

-Keith McCullough
Founder & CEO, Hedgeye Risk Management
Stamford, CT

CHAPTER SUMMARY

A Framework For Investing Success

- The opportunities that come from preserving and protecting your wealth are underestimated by most investors.
- Investors going through large drawdowns of their capital CAN'T redeploy it to compelling opportunities.
- Drawdowns are painful: If you have a -20% drawdown of your capital, you need to be up +25% to get back to breakeven. A -50% drawdown requires +100% growth to get back to breakeven
- "Resulting" refers to the cognitive bias where people judge a decision based on its outcome rather than on the quality of the decision at the time it was made.
- The long-term averages aren't signal.
- Embrace uncertainty: Most investors aren't equipped with the tools needed to navigate the business cycle.
- The inevitable jumps up or down of the business cycle and market prices can periodically tilt the odds in your favor where you can either buy every damn dip in risky assets OR get the hell out and put your precious capital into more promising opportunities.

Recommended Reading & Viewing

- Keith McCullough: "[How A Pro Constructs A Portfolio And Invests Over The Full Investing Cycle](#)"
- Hedgeye University: [Master the Market → Learn The Hedgeye Process](#)
- Annie Duke, "Thinking In Bets: Making Smarter Decisions When You Don't Have All The Facts"
- Benoit Mandelbrot, "The Misbehavior of Markets: A Fractal View of Financial Turbulence"

The Hedgeye Toolkit

- Since you're just getting started, you might be interested in a subscription to the [Early Look](#), my daily, 5-minute market strategy note.
- Email support@hedgeye.com to discuss investment research options with a trained Customer Service representative.

CHAPTER 1

The Game Has Evolved. Have You?

It feels like a lifetime ago now, but I was finally given the opportunity to run money in 2002.

My maiden visit to Jon Dawson's Southport, Connecticut, hedge fund shop was in the spring of 2000. In the late 1980s and early 1990s, Dawson embraced growth stocks, and he added talented analysts and new funds to his tent. His core strategy was classic long/short equity, with a disciplined value-oriented bent, despite his gravitation toward growth.

Dawson's shop managed around \$1 billion when I joined, at that time a humongous pile on which to be earning 2 & 20. Dawson and gifted energy Portfolio Manager Tony Giammalva were supported by a team of a dozen or so analysts and execution traders. Additionally, Dawson had opened a small New York office run by Dawson's 26-year-old protégé, a University of Florida graduate named Russell Herman. On January 1, 2000, Herman had launched a new hedge fund under Dawson called the Southport Millennium Fund.

When I visited the Southport office for the first time, I didn't expect a group of 20 or so people sitting around quietly in a three-story former factory that had been partially converted into office space. Dawson wore a button-down shirt, denim pants, and cowboy boots. His spacious office, decorated with photos spanning a long career rubbing shoulders with corporate America, was on the second level, just off the trading floor.

When Dawson wanted to do a trade, he opened the door of his window-enclosed office and shouted out the order to his traders sitting just outside, loud and deliberate, piercing the otherwise laid-back aura.

I learned a lot, particularly from Russell Herman out of Dawson's New York office. Herman constantly crunched numbers and pored over filings. He followed the market like a true old-fashioned stock operator, a dying breed with algorithms and MIT programmers and PhDs taking a firm hold on the market. Herman didn't use computer programs to trade. I'll never forget the day I looked into his office and saw Herman pressing a blank sheet of paper up to the computer screen on an angle like a crude slide ruler in an attempt to measure a set of closing price data.

The game of investing has changed dramatically since I joined Dawson-Giammalva in 2000. Back then, when Herman dove into a stock, he knew everything, every angle, who else owned it, how the options were being priced, and who owned the options. If he saw something worth chasing after, Herman would assign me or one of the other sector analysts to dig deeper. He used the Street for meetings. Herman played the game, and he knew how to play it, having learned from one of the best.

The prevailing *modus operandi*, passed down to him by Dawson, was this: You did more management meetings than anyone else, and you built out the best possible models to forecast earnings. Between kick-ass models (factoring together key business drivers, like operating margins, projected sales, etc.) and an exhaustive amount of one-on-one meetings, preferably with the CFO or COO, doing whatever it took to fill

in the blanks short of explicitly asking, you nailed down whether a company would hit its numbers. That's how you earned your "2 & 20."

By any measure, you'd say I'd been successful as an analyst. Then, the next level of the game came calling. Fast forward two years and by the start of 2002, Herman gave me responsibility for a "carve-out" percentage of the Southport Millennium Fund. Although informal, non-audited, and only a small piece of the overall fund, it was still tens of millions of dollars. Frankly, I was both nervous and thrilled to be playing with live ammo. More than anything, I was excited for a clear-cut, put-up-or-shut-up opportunity to prove myself. My chance to make it as a hedge fund manager, or to embarrass myself, had arrived.

Now that I was running a piece of Herman's Southport Millennium fund, I worked longer and harder than I ever have in my entire life. I got up earlier, too. I was always up by 5:30 a.m., but now I started to whittle my wake-up time down into the 4:45 a.m. vicinity. Never later than 5 a.m.

I traveled more, attended, impossibly, more conferences, more management meetings. I was a road warrior, a freakishly frequent flyer; seriously, I must have done 200 management meetings in 2002. (I would set a personal record two years later with 256 meetings in a 12-month period.) I engrossed myself in the markets (and not just my narrow sector) with an invigorated fervor.

I read everything I could get my hands on. Papers, magazines, biographies, white papers, anything that told me about the world beyond my reach, challenged my assumptions. I used plane trips to catch up on materials I collected like a pack rat in freebie canvas conference bags.

I clung to the concept that only harder work could separate me from the rest of the pack.

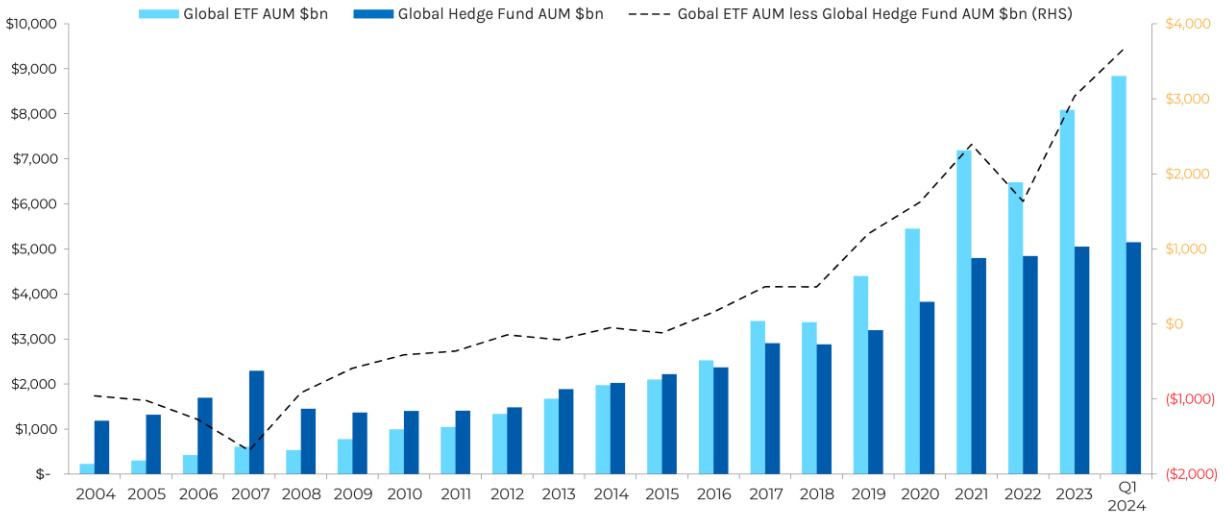
What I didn't realize at the time was that the active management industry was at its peak. The style of investing practiced by Dawson-Giammalva back then was about to be completely upended.

The chart below is from the Hedgeye Macro team which I lead. It captures and explains the rapidly evolving investment landscape over the 20+ years since my days at Dawson-Giammalva.

In 2023, the assets under management in listed Exchange Traded Funds (ETFs) surpassed \$7 trillion globally, topping global hedge fund assets by over \$2.1 trillion. You might be wondering how this has changed the game of investing. Well, to put it simply, **the asset management industry has been overtaken by "passive" ETF strategies at the expense of active managers.**

STOCK-PICKING HAS GIVEN WAY TO FACTOR-PICKING

ETF assets under management (i.e. “passive flows”) surpassed \$7 trillion globally as of Q3 2023, topping global hedge fund assets by \$2.1 trillion.



Source: Bloomberg, BarclayHedge, JPMorgan

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Active management involves portfolio managers making investment decisions to outperform a specific benchmark index through research, market forecasting, and security selection. In contrast, passive management, or indexing, aims to replicate the performance of a specific index, such as the S&P 500. The key differences between the two approaches lie in cost structure, trading activity, and performance goals. Active funds have higher costs and aim to generate higher returns, influenced by market timing and manager decisions. Passive funds aim to hug their benchmark and are therefore offered at a low-cost.

There's more to this story.

JPMorgan estimates that 90% of U.S. equity trading volume is happening systematically, meaning based on a pre-programmed set of criteria that AUTOMATICALLY causes a trade to happen. That could be based on an ETF rebalancing, market maker hedging activity, market neutral hedging strategies, etc.

All of this trading, based on rules, not active managers placing bets on a company's growth prospects, obviously changes how markets trade day-to-day. Funds, like Dawson-Giammalva, that were solely focused on analyzing company “fundamentals” have had to upgrade their investment processes or die. Many funds died.

You can see in the chart above that, around the Great Financial Crisis of 2007-2008, active management hit its peak relative to the small, but growing, assets under management for passive ETFs. In 2016, ETF assets finally eclipsed the size of global hedge fund assets for the first time. The growth of ETFs has continued unabated since then, while the pace of hedge fund growth has slowed. Since 2015, total ETF AUM has increased 240%. Meanwhile, net inflows to ETFs relative to Hedge Funds has increased 1,285% since 2016.

All of this might sound complicated, but just imagine something I call *The Machine*. In this simplified scenario, *The Machine* is a rules-based trading engine that's just buying and selling based on a particular set of criteria. *The Machine's* trading flows are so massive that it's influencing the direction of the stock market in a profound way.

If you're wondering how to make money on this phenomenon, this trading of *The Machine* ... good. If you can hack into the factors that trigger *The Machine* to buy or sell and you can accurately predict those factors, well, then you've got a magic money printer.

That's why Hedgeye Risk Management exists.

I gained a finer appreciation for how *The Machine's* rules-based trading impacts the stock market at Magnetar Capital. I joined Magnetar when Falconhenge Partners – the hedge fund I started with Harry Schwefel (now Point72's co-CIO) – started attracting the attention of larger players in the industry. We were approached by these larger hedge funds who dangled in front of Harry and I the opportunity to run significant sums of money.

Timing and size are everything in this business. Back in 2006, the magnetic pull of the economics of such a large pool was too powerful to resist. That pitch had been made to us by Ross Laser, the co-founder of Magnetar Capital. Laser and Magnetar's co-founder, ex-Citadel star trader Alec Litowitz, were creating one of the most talked-about hedge funds in the business.

By the second quarter of 2006, around its one-year anniversary, Magnetar was coming up on the \$3 billion mark, remaining in explosive growth mode, attracting money and industry talent in neutron - star-worthy fashion. Magnetar was attempting to create one mother of a "Multi Strategy" hedge fund, comprising a wide range of a dozen or so separate strategies, dabbling in standard and exotic asset classes, scouring markets in every corner of the planet.

The fund mixed merger arbitrage, in which Litowitz specialized at his former employer Citadel, along with other forms of arbitrage, as well as long/short global equity, long-only equity, event driven strategies, distressed credit, private placements, direct lending, and PIPEs (Private Investments in Public Equities). It even embarked on a reinsurance industry strategy, setting up a Class 3 Bermuda company, Pulsar Re, to take advantage of opportunities caused by the fallout in the reinsurance industry following Hurricane Katrina.

Magnetar was also a major investor in asset-backed instruments called collateralized debt obligations, or CDOs. Some of these CDOs comprised pools of mortgage streams, and some of those streams including debts pegged to riskier than normal borrowers, mortgages known as subprime.

Using his prime broker contacts at Morgan Stanley Magnetar's Laser spied our little Falconhenge and our +6% first quarter and approached us about the possibility of Magnetar's pulling in our entire team to help round out its long/short equity platform handling consumer-retail stocks. Surely the hedge fund industry was getting ahead of itself if a firm like Magnetar was coming after us despite our firm only having existed for exactly one quarter, or maybe talented PMs just were not in abundance. The Wall Street universe has always revolved around an unending quest for talent. We took Magnetar's offer.

Ross Laser ran the Magnetar business while Litowitz ran the book. Litowitz, a highly skilled merger arbitrage trader had been promoted from PM into the hybrid role of PM/Leader of Other Traders. He gave it his best, and was hands on in this regard, always asking questions of his PMs, getting us to defend our positions in terms he could understand.

Litowitz was, in a way, sort of the flip side to my first hedge fund teacher, Russell Herman. Herman looked into stocks and charts and fundamentals and balance sheet clues and wanted the beat of the Street, wanted to hear what management was saying; Litowitz looked at computer-driven models, numerical patterns. He taught me how to analyze the risk factors associated with stocks that were outside what I normally considered being retail risk factors. So, while I understood how a highly publicized food poisoning incident could leave a

restaurant chain's share price heaving, what Litowitz showed me was how to analyze risks using purely agnostic statistical factors such as liquidity, volatility, and volume and a host of others that I'm sure he'd prefer I didn't disclose.

"So what's your bet?" Litowitz would ask me.

He wanted to know price objective, timing, upside and downside, and he wanted it in cold stark numerical conveyances. Litowitz didn't care about what management had to say, he didn't follow stories or sentiment. He was purely a numbers guy. Although when it came to stocks there was one thing Litowitz had in common with Herman — they both always wanted to know who else owned it.

When I was at Magnetar, I was one of many portfolio managers. I wasn't inside of a fundamental long, short book that Jon Dawson was running. I was running a book amongst many other managers, not unlike how it works at Citadel. And because Magnetar was born out of Citadel, everyone had to obey the same quantitative limits and quantitative rules.

Magnetar pioneered many techniques now considered "best practices" by today's hedge fund industry — particularly how to operate market neutral and manage factor exposure risk. These are risk management policies that can dramatically impact market flows. The proliferation of these strategies, combined with the concentration of hedge fund assets at market-neutral platforms, has made financial markets more sensitive to Macro risks than ever before.

In my early days running a long-short portfolio at Magnetar, a risk management policy set by the firm would often neuter me out of positions. I began to develop what would become my Risk Range™ Signaling process and a rate-of-change based Macro framework to stay ahead of those changes.

The idea was: Could I front-run *The Machine's* flows by developing a repeatable risk management framework?

It was yet another question bubbling around in my mind in those days. The answer to that question was a resounding yes, but with a BIG asterisk. §§

§§ Yes, but you'd have to work your ass off and hire a huge team of analysts to build that process. Challenge accepted.

CHAPTER SUMMARY

A Framework For Investing Success

- In 2023, the assets under management in listed Exchange Traded Funds (ETFs) surpassed \$7 trillion globally, topping global hedge fund assets by over \$2.1 trillion.
- JPMorgan estimates that 90% of U.S. equity trading volume is happening systematically, meaning based on a pre-programmed set of criteria that AUTOMATICALLY causes a trade to happen.
- All of this trading, based on rules and not active managers placing bets on a company's growth prospects, obviously changes how markets trade day-to-day.
- Imagine something we'll call "The Machine." In this simplified scenario, The Machine is a rules-based trading engine that's just buying and selling based on a particular set of criteria.
- If you can hack into the factors that trigger The Machine to buy or sell and you can accurately predict those factors, well, then you've got a magic money printer.

Recommended Reading & Viewing

- Keith McCullough & Tier 1 Alpha: "[A Masterclass on Modern Market Structure: Inside Options, Flows & Volatility](#)"
- Hedgeye University: [Master the Market → Learn The Hedgeye Process](#)
- Edward Thorp, "A Man For All Markets"

The Hedgeye Toolkit

- I'm proud of the team of analysts we've assembled at Hedgeye. You can listen to my team of 40+ analysts and I discuss our favorite stock ideas with a subscription to [The Call @ Hedgeye](#).
- Email support@hedgeye.com to discuss investment research options with a trained Customer Service representative.

CHAPTER 2

Hope Is Not A Risk Management Process: My GIP Model

Something happened to me in the first quarter of 2005 that convinced me that maybe I was not in over my head, that likely I was as good as any hedge fund manager out there.

Wal-Mart was hosting an investor gathering in China for PMs and analysts from all over the world to come and get a first-hand overview of the big picture as it related to the future of the Bentonville, Arkansas-based retail monstrosity and its symbiosis with China where most of the cheap goods it sold were being made.

I boarded a Cathay Pacific flight to Hong Kong, the first leg of the journey, and happened to notice that a few rows ahead of me in first class was one of the biggest, best-known hedge fund managers in the world. I'll call him "The Giant."

I watched him on and off for pretty much the whole 14-hour flight. While I devoured the contents of multiple canvas bags overstuffed with reading material, there's *The Giant*, sprawled out like he's in his home theatre, shirt open, shoes off, stuffing his face with all the free caviar the stewardesses could feed him (and free caviar wasn't all you got when you flew Cathay Pacific to Asia; there was also wine, shrimp, cheese, sweets).

This guy, *The Giant*, watched movies and racked out. Meanwhile, I read, researched, and worked. I came away that night convinced *The Giant* was weak, and that if this was how the biggest and best hedge fund managers rolled, well, I shouldn't worry ever again about how I measured up. I wasn't just as good. I was better.

For me, investing has never been about being the smartest guy in the room. It's always been about getting up at 5 a.m., putting two feet on the floor and doing the hard work most people are unwilling to do.

One of the goals I had when I set out to do this book was to inspire people to be more involved in the investing decisions that would impact the lives of their families. If a hockey player named Mucker from Thunder Bay can do this, anyone can. Or at least you might get to a point where, with some help, you can take a role that goes beyond just hoping the market moves in your favor.

Hope is not a risk management process.

Since that experience with *The Giant*, I've learned that there's a framework for success that most of the world's best intuitively know through experience. I'll share these principles with you because you need to be thinking about them as you discover how to perform at the highest level.

There are five ways to win, according to my friend and one of the world's top performance coaches, Dr. Gio Valiante. Dr. Gio has witnessed and helped orchestrate more success stories than most. He's worked with some of the world's highest performing golfers, championship football teams and hedge fund managers, including the title of Head Performance Coach for Steven Cohen's Point72 Asset Management.

Dr. Gio has a fantastic framework for understanding how you, the self-directed investor, can gain an edge in financial markets. His framework is called, “There Are 5 Ways To Win.”

Here they are:

1. You have outstanding **TALENT**
2. You **WORK HARDER** than those with more talent (all-in).
3. You have a **DIFFERENTIATED** perspective (Unique View).
4. You have a rigorous, disciplined, repeatable **PROCESS**.
5. You **HIRE** to effectively compensate for above deficiencies.

Look closely at that list again.

Be brutally honest with yourself. Identify your strengths and weaknesses. As you progress through this book, think about how you might amplify your strengths and correct your weaknesses by structuring your investment process around those strengths and weaknesses.

Yes, you can do this.

Why do I believe you can do this? Because I’m invested in your success. I’m not only predicting a rise in the ranks of self-directed investors, I’m banking on it. I’ve been building a business around it for more than 15 years now. My thesis is this: Individuals have to get more involved and take back the reins from industry people who get paid to keep them in the dark.

Wall Street, through its rational self-interest, is waking up to the reality that more investors are demanding the ability to manage their own money. Major brokerages like Charles Schwab, TD Ameritrade, E*TRADE, and Fidelity all announced the elimination of commissions for online stock, ETF, and options trades back in 2019. By 2020, most other major brokerages followed suit, making commission-free trading a standard offering.

That’s a good start. It means you can actively trade your own portfolio without incurring costly commissions. That’s an edge over large institutional investors who, to move large sums of money around, still need to pay prime brokers.

What else can you do to tilt the odds in your favor?

For that, I need to tell you more about the hedge fund I co-founded, Falconhenge Partners, and how we stumbled on the beginnings of what would ultimately become Hedgeye’s global Macro framework.

My final years working on the fundamental long-short side at Dawson-Herman, I was running a consumer fund. One of the best analysts I worked with at the time was an analyst by the name of Harry Schwefel. He played hockey at Harvard. Today people in the industry know Harry as the co-CIO at Point72, working alongside Steve Cohen. But back then, Harry and I were just two up-and-comers that left Dawson to start our own hedge fund.

When we launched Falconhenge Partners fundraising efforts forced us to write how we’d generate excess returns. We wrote:

Our Mission: To Manage a High Conviction, Highly Concentrated Portfolio. Process driven, cash flow focused. Our proprietary modeling and valuation process uncovers undervalued cash flow opportunities that are out of favor with conventional consensus.

Our value with a catalyst approach was the investment style that dominated in Q4 of 2006 — that quarter was one of the best I had ever had with my quarterly return in the high teens.

The main point for Harry and I was our process. We called that process, the “Pods.” There were three things we cared about in this framework:

- Pod #1: The rate of change of **Revenue Growth**
- Pod #2: The rate of change of either **Cash flow** or **Earnings Growth** (depending on the company)
- Pod #3: **Capital Allocation**, or a company’s free cash flow returns on invested capital.

We would always evaluate companies in terms of the year-over-year rate of change, scoring each company across all three Pods. A company was either accelerating or decelerating across each of these three Pods. It was simple logic, but not easy to implement in practice. If we could predict these inflection points: Companies decelerating were shorts and companies accelerating were longs. That’s how we did it for every single company model we built.

As I progressed in my career, I became more and more Macro focused. I started to think about using the Pods to predict how countries might perform economically.

I got tired of modeling companies in a way that couldn't tell me what the forward outlook was from a macro perspective. No matter how great an analyst was at bottom-up company modelling, I constantly saw these analysts getting blindsided by Macro. I would get that wrong too, and I didn't like being wrong.

I started to build a global macro overlay to analyze companies from a top-down perspective. Once I combined that with the bottom-up company view, it was magic. This seemed intuitive enough to me at the time. I just fundamentally couldn't understand why people weren't applying a repeatable process like this.

This all gets easier to understand when you think about it in the context of a particular company. Think about a global company like Nike, for example. From a macro perspective, don’t you want to know what the dollar’s impact might be on Nike? How might the rise or fall of the U.S. dollar impact Nike's upcoming quarter? How might that impact Nike's European business? What happens to Nike if global growth is decelerating?

These all seemed like logical questions to ask. It was an intuitive conclusion that you should have a rate of change, top-down macro process while overlaying the bottom-up company research. I started to think of the world as one big sine curve that has an amplitude – accelerations and decelerations. Think of a sound wave. Louder sounds have a higher amplitude. If the amplitude is too loud, you can blow your ears out and permanently damage your hearing.

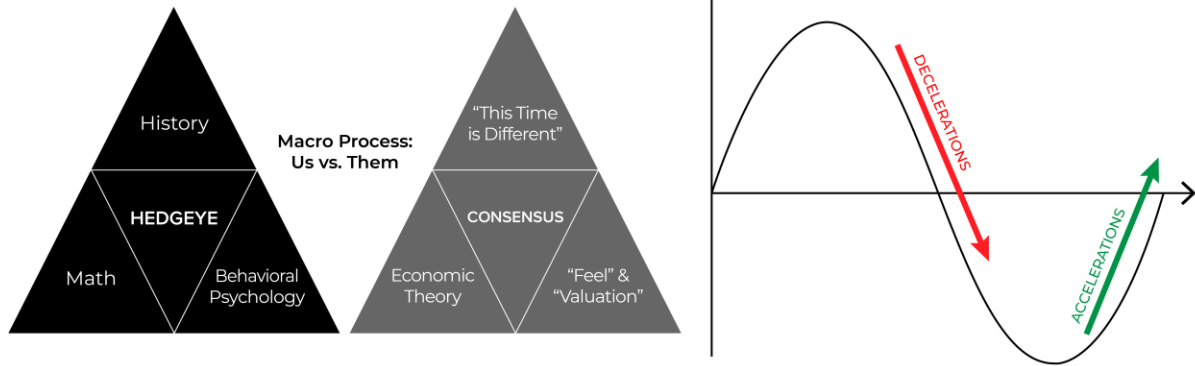
The economy is no different really. An economy can have a wide amplitude - growing rapidly then falling off a cliff when growth fails to keep up over the ensuing years. When the economy falls off a cliff, you better be sure you don’t cause permanent damage to your capital.

The best way to think about it is there's no fixed end point, you’re just looking at where a country is on the continuum of their growth trajectory. People who are modeling things bottom up, don't quite like that. They want it to be linear.

That's the opportunity, having an apolitical and data-driven view of top-down Macro and bottom-up Fundamental was, and still is, highly differentiated.

OUR PROCESS IS DIFFERENTIATED BECAUSE WE FOCUS ON FACTS

Rate of change accelerations and decelerations are facts, not opinions.
This helps spot inflections in key asset classes 3-6 months ahead of consensus.



At Falconhenge, this answer was staring me right in the face. The goal was to have a process to trade what was directly in front of you, as opposed to what I might want to see.

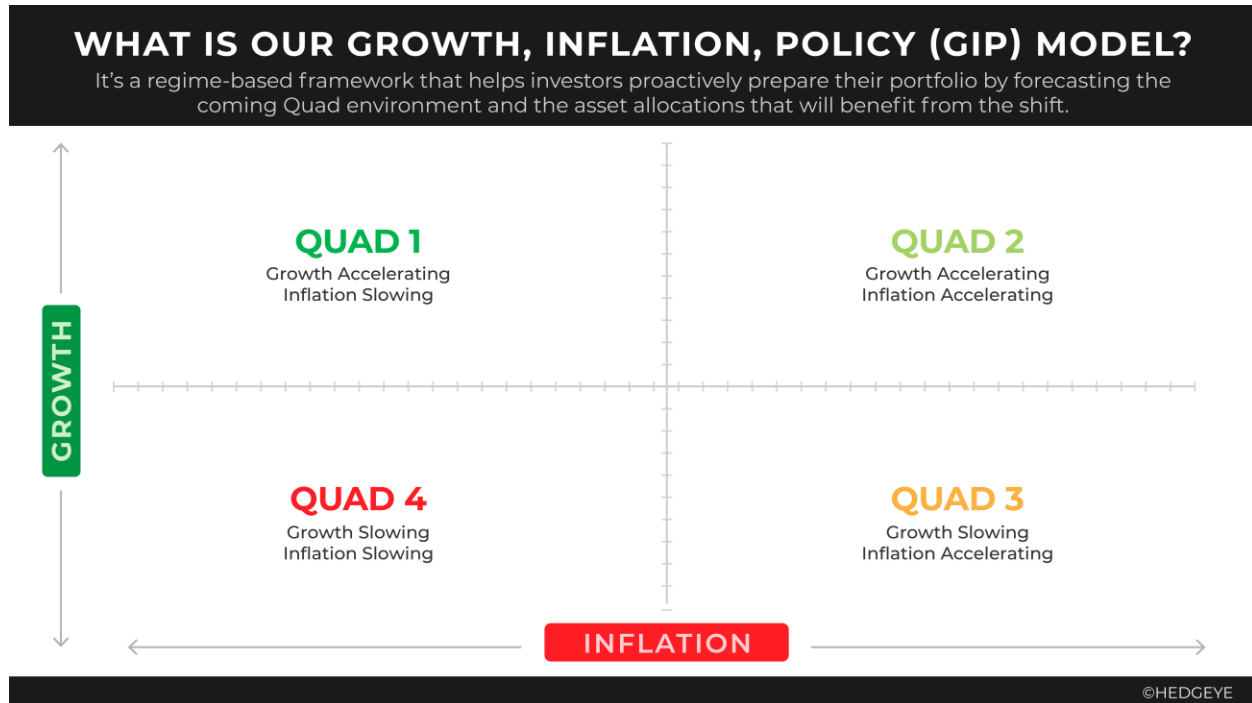
The question became how do I adapt the “Pods” to Macro. What I came up with was a four Quadrant framework. At the country level, instead of the rate of change of revenue, we have *GDP*. And instead of company cash flow or the rate of change of margins, we have *inflation*.

The final twist, because we’re obviously not analyzing the returns on invested capital of governments, was to look at the central bank policy response to these rates of change of growth and inflation.

What came out of this thought process was something beautiful. At Hedgeye, we call it our “Growth, Inflation, Policy” model (or GIP model for short).

Let’s sum all this up simply and succinctly.

We find two factors to be most consequential for forecasting future financial market returns: economic growth and inflation. We track both on a year-over-year rate of change basis to better understand the big picture then ask the fundamental question: **Are growth and inflation heating up or cooling down?**



From there, we get four possible outcomes, each of which is assigned a “quadrant” in our Growth, Inflation, Policy (GIP) model and the typical government response as a result (neutral, hawkish, in-a-box or dovish):

- Growth accelerating, Inflation slowing (QUAD 1);
- Growth accelerating, Inflation accelerating (QUAD 2);
- Growth slowing, Inflation accelerating (QUAD 3);
- Growth slowing, Inflation slowing (QUAD 4).

The chart we use at Hedgeye today is above.

After building this base of knowledge, we can now select what we like (and don’t like) based on our historical back-testing of the different asset classes that perform best in each of the four quadrants. Below is a chart that lays out precisely what we like and don’t like when an economy is in each of the four quadrants.

This chart should serve as a starting point for making better investment decisions.

The key point here is that this investment framework is based on a back-tested reality. If we get the rates of change of growth and inflation right, we’re able to front run what Wall Street and the Fed will do next. Over time, we’ve proven that. Hedgeye is consistently 3 to 6 months ahead of Wall Street.

BEST & WORST PERFORMING ASSET CLASSES BY QUAD REGIME

We've back-tested the performance of all asset classes by Quad to help investors make money as the Macro regime changes.

Quad 1: Goldilocks	Quad 2: Reflation	Quad 3: Stagflation	Quad 4: Deflation
Best Asset Classes: Equities, Credit, Commodities, FX	Best Asset Classes: Commodities, Equities, Credit, FX	Best Asset Classes: Gold, Commodities	Best Asset Classes: Fixed Income, Gold, USD
Worst Asset Classes: Fixed Income, USD	Worst Asset Classes: Fixed Income, USD	Worst Asset Classes: Credit	Worst Asset Classes: Commodities, Equities, Credit, FX
Best Equity Sectors: Tech, Consumer Discretionary, Materials, Industrials	Best Equity Sectors: Tech, Consumer Discretionary, Industrials, Materials	Best Equity Sectors: Utilities, Tech, Energy, Industrials	Best Equity Sectors: Consumer Staples, Utilities, REITS, Health Care
Worst Equity Sectors: Utilities, REITS, Consumer Staples, Financials	Worst Equity Sectors: Telecom, Utilities, REITS, Consumer Staples	Worst Equity Sectors: Financials, REITS, Materials, Telecom	Worst Equity Sectors: Energy, Tech, Industrials, Financials
Best Equity Style Factors: High Beta, Momentum, Cyclical, Secular Growth	Best Equity Style Factors: Secular Growth, Momentum, Cyclical Growth, Small Caps	Best Equity Style Factors: Secular Growth, Momentum, Mid Caps, Low Beta	Best Equity Style Factors: Low Beta, Dividend Yield, Quality, Defensives
Worst Equity Style Factors: Low Beta, Defensives, Value, Dividend Yield	Worst Equity Style Factors: Low Beta, Value, Dividend Yield, Defensives	Worst Equity Style Factors: Small Caps, Dividend Yield, Value, Defensives	Worst Equity Style Factors: High Beta, Momentum, Cyclical, Secular Growth
Best Fixed Income Sectors: BDCs, Convertibles, HY Credit, EM \$ Debt	Best Fixed Income Sectors: Convertibles, BDCs, Preferreds, Leveraged Loans	Best Fixed Income Sectors: Munis, EM \$ Debt, Long Duration Treasuries, TIPS	Best Fixed Income Sectors: Long Duration Treasuries, Medium Duration Treasuries, IG Credit, Munis
Worst Fixed Income Sectors: TIPS, Short Duration Treasuries, MBS, Medium Duration Treasuries	Worst Fixed Income Sectors: Long Duration Treasuries, Medium Duration Treasuries, Munis, IG Credit	Worst Fixed Income Sectors: BDCs, Preferreds, Convertibles, Leveraged Loans	Worst Fixed Income Sectors: Preferreds, EM Local Currency, BDCs, Leveraged Loans

Source: Hedgeye GIP Model Market History Back-Tests, Quarterly expected values since 1Q98. Total Return indices.

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And from the Pods, the Quads were born.

The above is the evolved form of the Hedgeye Macro process that I started to develop back in the Falconhenge days. Since then, our Macro team has built predictive tracking algorithms to forecast growth and inflation for the U.S. and the top 50 economies around the world. All told, the scope of our Macro research today covers 90% of global GDP. It's a daily grind and we love it.

But back then, while Harry and I were still toiling away at Falconhenge, the early days of combining a top-down Macro process with fundamental, bottom-up stock research started to generate some fascinating ideas. While fundraising, many potential investors we met with were still skeptical.

Sure enough, one day I found myself seated across from none other than *The Giant*. I half expected him to belch caviar on me. He sat slumped back behind a conference table, leaning back in his chair, hands crossed behind his head, his tie flipped back over his shoulder, looking at me with a vague sense of knowing who I was and sounding like every other hedge fund guy, asking me "so, what's your best idea?"

First of all, the tendency for industry members to frame everything into "best ideas" on the one hand is sort of useful, makes sense. On the other hand, it's the exact same question everyone else is asking, parroting, unoriginally what they think is the expected language of the realm.

But since I was looking to make an impression (*The Giant* by this time had certainly made one on me) and seeing as I had fairly recently attended the annual Prospectors & Developers Association of Canada expo at the Metro Toronto Convention Centre, one of the largest, most important gatherings of mining industry executives from all over the world, I was bullish on mining, and told *The Giant* as much.

Turns out, I said, one of the richest gold mines in the world operated in Red Lake, Ontario, just north of Thunder Bay where I had contacts on the ground, guys in the industry that my brother knew. *The Giant* gave me a look that said I know you, you're that retail guy from Jon Dawson's shop, what the Christ do you know about mining stocks? And then, in a gruff, gravelly tone, he just blurted it out: "Mining stocks? What do you know about mining stocks?"

My back stiffening up, and speaking in brisk sound bites, I went on the offensive, rattling off some macroeconomic trend observations (global inflation, rising commodities prices, demand for raw materials in China) but it was clear to me he wasn't hearing any of it.

What did I know about mining? *The Giant's* disdain infuriated me to no end. Here I had told him of one of the most informative research trips I had ever taken — I had done a sort of mining industry immersion, met all the main players — and I had sources on the ground miles from a mining hub, what did I know — what did he think he could possibly know about mining sitting here one block from Park Avenue?

Anyway, I told him my best ideas were Freeport-McMoRan Copper & Gold (NYSE: FCX) and Phelps Dodge Corp (former ticker: PD) and thanked him for his time. When I left the office, I was practically running a fever. *The Giant* passed on the investment opportunity. Within the year, FCX and PD announced they were merging in a deal valued at \$26 billion. I would later find out FCX became one of *The Giant's* single biggest positions.

Top-down Macro and bottom-up fundamental analysis was clearly a winning combination.

CHAPTER SUMMARY

A Framework For Investing Success

- Individual investors have to get more involved and take back the reins from industry people who get paid to keep them in the dark.
- There are five ways for investors to win, according to one of the world's top performance coaches Dr. Gio Valiante: Talent, Work Harder, Differentiated Perspective, Process, Hire.
- Bottom-up, fundamental analysis (PODS) focuses on the rate of change of the following variables: Revenue Growth, Cash Flow or Earnings Growth and Capital Allocation (free cash flow returns on invested capital)
- Top-down, Macro analysis (QUADS) focuses on the rate of change of the following variables: Country's Economic GDP Growth and Inflation Growth (with a central bank's corresponding policy response)
- Four quadrant Growth, Inflation, Policy Model:
 - Growth accelerating, Inflation slowing (QUAD 1);
 - Growth accelerating, Inflation accelerating (QUAD 2);
 - Growth slowing, Inflation accelerating (QUAD 3);
 - Growth slowing, Inflation slowing (QUAD 4).
- Our Macro team has built predictive tracking algorithms to forecast growth and inflation for the U.S. and the top 50 economies around the world. All told, the scope of our Macro research today covers 90% of global GDP.
- Top-down Macro combined with bottom-up fundamental analysis is a winning combination.

Recommended Reading & Viewing

- Keith McCullough, "[14-Minute Macro Masterclass: Building A Go-Anywhere Macro Portfolio](#)"
- Hedgeye University: [Master the Market → Learn The Hedgeye Process](#)
- Dr. Gio Valiante, "Fearless Golf: Conquering the Mental Game"
- Philip Tetlock, "Superforecasting: The Art and Science of Prediction"

The Hedgeye Toolkit

- The process we've built at Hedgeye is second to none. If you're interested in stock ideas, I curate a list of long and short ideas and my analysts provide fundamental updates with [Investing Ideas](#). If you're interested in macro asset allocation, [ETF Pro](#) gets you my favorite ETF ideas.
- Email support@hedgeye.com to discuss investment research options with a trained Customer Service representative.

CHAPTER 3

Numbers Don't Lie, People Do: My Risk Range™ Signals

Most of my major leaps forward in building a better investment process are born out of past mistakes. I'll give you an example.

A retail company I followed fairly closely in 2000, and into the summer of 2001, was Pacific Sunwear of California (former ticker: PSUN), an Anaheim - based seller of surf clothes, shades, and sandals.

But could they sell board shorts in the heartland? Was it a fad or for real?

Every major sector has its conference circuit, and I began to attend these events, usually put on by a sellside analyst from a major bulge bracket firm. Just as Frank Quattrone and Credit Suisse First Boston (CSFB) put on a massive technology conference at The Phoenician in Scottsdale, Arizona — golf, booze, and shoulder rubbing couched under the guise of riveting panel discussions on industry trends — all the banks did some sort of conference. The major banks would all put on elaborate sector conferences, including retail. Lehman Brothers, for example, put on one of the biggest retail conferences every spring.

These types of events usually featured management teams from household name companies. In spring of 2001, at one such event, I sat down with PSUN's Chief Merchandising Officer, Timothy Harmon, an upbeat, curly-haired fellow. Because of his permanently gelled curls, I mentally assigned him a nickname that meant no disrespect, but which amused me: Perma-fro. He met with me and one other hedge fund analyst (a "2-on-1"). I came away from the conversation with the impression that PSUN's sales in their second quarter (the company's prior fiscal year that year ended February 4, 2001) were actually going to be closer to rad than gnarly.

My fellow hedge fund analysts all agreed PSUN's future looked bright, or rather we agreed to agree on what we just heard. I believe even more favorable sentiment was bandied about later that night over cocktails: "We like PSUN," one hedge fund analyst declared to another who replied, "We like it, too." Hedge funds cherish privacy and go to great lengths to stay out of the public eye, but the notion that hedge funds are secretive is something of a myth. Many hedge fund managers like to share their ideas, and they like to copy other managers' ideas because a group hug can drive the share price up in a sort of self-fulfilling prophecy, which CEOs love.

Who else owns it? That's a question most hedge fund managers ask first and foremost. This clubby, influential New York City/Connecticut area hedge fund sphere was sometimes referred to as the hedge fund mafia.

Sufficiently impressed with my own "research," I began to speak up loudly about the company at our morning meetings, and on my recommendation, Dawson and Herman were both buying up PSUN ahead of their first quarter earnings announcement scheduled for later that May. All they wanted to know from me, was PSUN going to hit its numbers? Yes, I told them, I had just met with management.

I had learned that if you want to get a hedge fund Portfolio Manager's attention, tell him or her you just met with management. A week or so after I met with Perma-fro, Pacific Sunwear announced that its COO had resigned and that sales at stores open at least a year decreased 4.1 percent for the four weeks ended May 6. Chairman and Chief Executive Greg Weaver said in a statement: "April was disappointing."

The stock got hammered, and Dawson and Herman questioned my call, but since I had just met with management, I countered that the stock was still looking good — the negativity was overboard, business was on the upswing, and they'd do better in their second quarter. They would grow in the second quarter over the same period a year earlier. PSUN, I was sure, would shine.

Later that July, as I prepped for the daily morning call with the whole firm on the squawk box, during which I knew I'd be asked again about Pacific Sunwear because its June sales numbers were coming out, I saw an item come over the Reuters tape that made my heart jump. PSUN missed; June sales had sucked. The stock sold off.

The phone rang. It was Jon Dawson, and he was not happy. Before he hung up on me, I heard him yell to his traders to "sell!" He was selling at a loss. I felt like an idiot.

PSUN fell about \$2.50 that day from the open. We'd been gobbling it up, long, for weeks. Perma-fro had played me. I was a lemming. From that experience I learned a few things: One, stocks don't lie. People do.

And two, if you just go along with what everybody else thinks, if you confuse popular consensus for an honest research process, you're setting yourself up for failure. I'd been drawn in by the guidance game, by hedge fund groupthink syndrome. That whole system had failed me. Yet Herman and Dawson never held the PSUN fiasco over my head, and we moved on; they gave me the chance to take shots and miss. As my idol Wayne Gretzky once said, "You will miss 100 percent of the shots you don't take."

While that holds true, there's nevertheless a distinct line in the hedge fund business between a few missed shots and outright poor performance.

Out of every painful experience comes growth. I can't say I developed my Risk Range™ Signaling process as a direct result of getting burned by PSUN and Perma-fro, but experiences like this (there have been many over the years) stick with you.

The point that I learned from PSUN - "numbers don't lie, people do" - is something that's been burned into my brain. **Over the years, I've built a rules-based process to minimize painful mistakes like this.**

Before I describe my Risk Range™ Signaling process, I need to tell you about the ideas of a genius mathematician by the name of Benoit Mandelbrot. Mandelbrot (1924-2010) was a Polish-born French-American mathematician best known for his work in developing the field of fractal geometry. He was born on November 20, 1924, in Warsaw, Poland, to a Lithuanian Jewish family. In 1936, his family emigrated to France to escape the growing anti-Semitism in Poland.

Mandelbrot's early work spanned various fields, including economics, fluid mechanics, and information theory. Simply put, Mandelbrot was a mathematical genius whose ever-curious mind frequently got him in trouble with purveyors of conventional wisdom.

In 1958, Mandelbrot joined the research staff at IBM's Thomas J. Watson Research Center in New York, where he began to explore the concept of self-similarity in mathematical objects. His work led to the development of fractal geometry, a branch of mathematics that studies complex shapes that can be split into parts, each of which is a reduced-scale copy of the whole.

A classic example of “self similarity,” as Mandelbrot calls this reduced-scale copy concept, is a stalk of broccoli. A smaller stalk of broccoli broken off from the larger whole looks like a reduced-scale copy. Mandelbrot developed a statistical process for identifying patterns in complex systems that applied to everything from natural phenomena (snowflakes, earthquakes, lightening bolts), biology and, most importantly for us, financial markets.

In his book *The Misbehavior of Markets*, Mandelbrot describes his first foray into financial markets with the study of cotton prices. Mandelbrot was shocked to discover that his findings challenged conventional economic theory. The “Efficient Market Hypothesis” backstops much of conventional wisdom in finance. It suggests financial markets are efficient and that price changes are evenly distributed along a bell curve. As Mandelbrot diligently plugged cotton prices into IBM’s state-of-the-art computing power an interesting finding jumped off the page. “There were too many big price jumps to fit the bell curve,” Mandelbrot wrote.

Mandelbrot discovered that cotton prices exhibited “fat tails” and greater peaks, indicating a higher likelihood of extreme changes than would be generally predicted by standard economic theory. “Big gains and losses concentrate into small packages of time,” Mandelbrot wrote.

If you think deeply about Mandelbrot’s findings, this has profound implications for investors. If extreme price movements (up and down) tend to cluster together, then the smart investor had better have a process before they “buy the dip.” A so-called “cheap” stock could get a lot cheaper.

My Risk Range™ Signals were built on the basis of Mandelbrot’s fractal math.

The Risk Range process and my Trade-Trend-Tail model was developed while I was working as a portfolio manager at Magnetar Capital in the mid-2000s. As a highly quantitative-based risk management shop, the Magnetar team was second-to-none back then. I developed my Risk Range process to try to stay ahead of and front run big changes that the risk systems started to spit out, things that would run counter to my positioning.

Remember, Magnetar pioneered techniques now considered “best practices” – how to operate market neutral and manage factor exposure risk. As we reviewed earlier, JPMorgan estimates that 90% of U.S. equity trading volume happens automatically based factor-based index investing or market-neutral risk management practices.

As Mandelbrot might have predicted, since these rules-based trading strategies are so prevalent, rising market volatility can exacerbate down moves as automatic selling is triggered. Conversely, falling market volatility can cause a cascade of buying from these rules-based strategies. All of this is to say that there’s money to be made identifying “forced” buying or “forced” selling.

I’ll say this again, financial markets are more sensitive to Macro risks than ever before.

That’s why my Risk Range™ Signaling process is so important. It’s a multi-factor, multi-duration model that can be used to identify breakouts or breakdowns across any asset that ticks.

Here’s how it works.

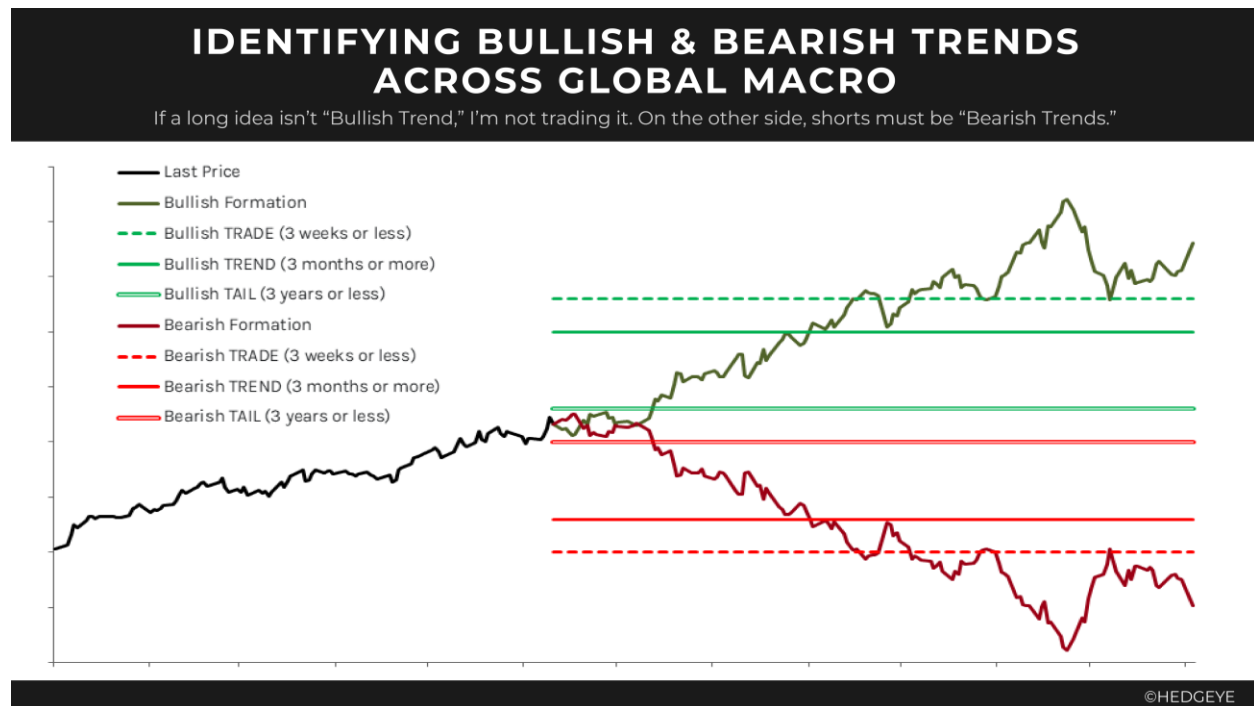
My quantitative Risk Range process uses price, volume and volatility at the index or ticker level to generate a probable range for that security over the short to intermediate-term. For example, if you’re looking at the S&P 500, the Risk Ranges suggest where you want to be buying (at the low end of the probable range) and selling (at the top end of the range). Importantly, these ranges move intraday as an asset’s price, volume and volatility changes, meaning they’re dynamic. This allows me to make high probability decisions in real-time.

Using the underlying price, volume and volatility of an asset, this proprietary signal also suggests critical thresholds, across different durations to help you identify Bullish and Bearish “phase transitions” – effectively helping you identify breakouts and breakdowns across specific assets. I generate these probable buy low, sell high ranges across durations to be able to tell whether an asset is breaking out or breaking down.

Here are those durations:

- "Trade" is a duration of 3 weeks or less
- "Trend" is a duration of 3 months or more
- "Tail" is a duration of 3 years or less

An asset that is bullish across all three of my durations – Trade, Trend and Tail – is a safer asset to “buy the dip” than a stock that’s breaking down.



Armed with a completely quantitative tool, it's a lot harder to be fooled by the likes of PSUN or Perma-fro these days. Sure, Hedgeye analysts still feed me tickers they're bullish or bearish on based on bottom-up, fundamental company analysis. But I plug those tickers into my Risk Range™ Signaling process and I have a completely agnostic, quantitative view on whether an asset is breaking out or breaking down.

I'd put our risk management process up against any buy-side firm out there.

In fact, if you aren't measuring and mapping global economic data like we do, and interpreting it through the lens of our Risk Ranges, what are you doing to effectively manage Macro risk?

A fractal approach to markets is going to beat the hell out of the alternative all day. Now that you understand my Risk Range™ Signals and GIP model let's talk about the next skill most investors don't pay enough attention to: **Position sizing**.

CHAPTER SUMMARY

A Framework For Investing Success

- Most of my major leaps forward in building a better investment process are born out of past mistakes. Build a rules-based process to minimize painful mistakes.
- The “Efficient Market Hypothesis” backstops much of conventional wisdom in finance and suggests financial markets are efficient and that price changes are evenly distributed along a bell curve.
- Mathematician Benoit Mandelbrot identified "fat tails" and greater peaks in markets, indicating a higher likelihood of extreme changes than predicted by economic theory.
- “Big gains and losses concentrate into small packages of time,” Mandelbrot wrote.
- JPMorgan estimates that 90% of U.S. equity trading volume happens automatically based factor-based index investing or market-neutral risk management practices.
- Since these rules-based trading strategies are so prevalent, rising market volatility can exacerbate down moves as automatic selling is triggered.
- Falling market volatility can cause a cascade of buying from these rules-based strategies.
- There’s money to be made identifying “forced” buying or “forced” selling.
- My Risk Range™ Signaling process is a multi-factor, multi-duration model used to identify breakouts or breakdowns across any asset that ticks.
- My quantitative Risk Range process uses price, volume and volatility at the index or ticker level to generate a probable range for that security over the short to intermediate-term. This allows me to make high probability decisions in real-time.

Recommended Reading & Viewing

- Keith McCullough, “[The Macro Playbook](#)”
- Hedgeye University: [Master the Market → Learn The Hedgeye Process](#)
- Benoit Mandelbrot, “The Misbehavior of Markets: A Fractal View of Financial Turbulence”
- Herbert Simon, “Models of My Life”

The Hedgeye Toolkit

- If you want buy low, sell high levels for 30+ major asset classes (ex. S&P 500, Gold, Tesla (TSLA) & more), you might be interested in [Risk Range™ Signals](#). If you’re interested in a turbocharged list of stock picks (chose via my Risk Ranges), check out [Signal Strength Stocks](#).
- Email support@hedgeye.com to discuss investment research options with a trained Customer Service representative.

CHAPTER 4

Dealing With Mistakes: Position Sizing Principles

Ever since the Pacific Sunwear fiasco I made it a habit not to consort with my hedge fund brethren during conference events or following 3-on-1 meetings, which put a CEO or CFO in a room with three analysts or PMs at a time. These meetings were starting to become the norm because of how many hedge funds were paying for access to management — they couldn't all be accommodated. If, after a meeting ended, I saw that one of the other analysts or PMs was even remotely looking in my direction I simply pretended to be on the phone.

Sometimes, when a group of buysiders approached me to “pick my brain” (confirm that my takeaway jibed with theirs) I just began talking to myself as if I were sporting the world's most inconspicuous hands-free device, an absurd, not at all sly, but nevertheless effective antidote to poisonous groupthink. Yet for all of my efforts at nurturing self-discipline and to steadfastly stand apart from the hedge fund mafia crowd, there were times when I fell right into the honey traps of life in the hedge fund bubble.

In the middle of the summer of 2005, I was part of a small group of analysts and PMs invited by a major bank to an exclusive golf outing at the world-renowned Bandon Dunes Golf Resort out on the majestic, jagged Oregon coastline, billed as the best golfing anywhere this side of Scotland. Golf heaven.

At this time, I still had a significant long position at Dawson-Herman in Nike and a short one in Reebok International (NYSE: RBK). I might have noticed all of the Adidas golf shoes in the pro shop and on the links, but if I didn't, it may have been because by day's end I had a cigar the size of a striped bass lodged in my teeth and an unlimited array of vintage Scotch whiskeys. Not much was on my mind as my hedge fund brethren and I sat around a fire pit outside the restaurant, looking out on a vast expanse of beautifully manicured landscaping, like a group of turn-of-the-century industrialists.

Sufficiently gassed up, feeling as if this one time I could sleep in, I set my alarm for 5:30 a.m. instead of my usual 2:30 a.m. West Coast routine. I woke up hung over, beyond parched, my mouth tasting as if a smoldering campfire had been emptied into it. No matter how much I gagged or spit or coughed or gargled or brushed my teeth, I couldn't lose the sludge-like film that permeated my tongue and throat. The phone was ringing off the hook but I didn't answer — I couldn't talk. Finally, I answered. It was Dawson. Reebok was being acquired by Adidas-Salomon AG. My short position was getting clobbered! What should they do, what the heck happened, where the hell have you been? Reebok, taken out, and not only was I short, not only did I not see it coming, I didn't even know it was happening now. I had no access to a computer or a television, or my cell phone, and most cruelly, no ability to formulate sentences.

I tried to mumble something, but what came out was the unmistakable sound of a cat spitting up a hairball. This was an ultimate crushing. Somewhere a French Canadian deejay spun a K.C. and the Sunshine Band 45-inch record and gyrated hyperactively in my honor. I can still taste that stogie. The one time I decide to sleep in, I get jumped. But I couldn't beat myself up too much. The merger would have gone down regardless of

whether I was up crazy-early. No one held it against me. I'd make it through this earnings season, shake off the Dunes debacle.

Losses hurt. If you're investing as long as I have you've got plenty of scars. **Over the years, I've found the best way to minimize losses when they inevitably happen is to have a rules-based process.** A series of rules that you always abide by takes the sting out of mistakes. When you lose (and you will) you know precisely what to do next.

It's freeing to follow your process, take your lumps and move on to the next play. You can't afford to do otherwise. If you remember performance coach Dr. Gio's five ways to win, most of us aren't going to win by being more talented than Wall Street. When my team wins, we win on hard work and differentiated process.

Below I'm going to teach you my rules-based process for...

1. Establishing a Core Position & Sizing That Position Properly
2. When To Buy The Damn Dip In A Core Position
3. When To Get Out of a Core Position

Mistakes like the PSUN fiasco or the Reebok acquisition have taught me valuable lessons. What I've found over the years is that investors who panic about a position do one or all three of the following.

1. They haven't properly thought through their position sizing rules.
2. They haven't considered the reasons they'd get out of a position once they're in.
3. Once a mistake has been made, they set aside their better judgement and double down on failure.

I've learned all of this the hard way (i.e. lost money) over the past two-plus decades. It's my aim that by sharing these hard-learned lessons, it will make you a more informed investor.

The below isn't going to be easy to swallow. It's not a fast-food cheeseburger. Sorry, but it's time to eat your vegetables. The next time you open your investment portfolio, think about these principles, start to develop your own rules and abide by them.

You'll thank me later.

Key Principles of Position Sizing

Position sizing refers to the percentage of total capital allocated to a particular investment. As I said, I've been doing this for a long time and I've developed a series of rules that are amplified by the Hedgeye process to help me better manage risk.

First things first, Minimum and Maximum Position Sizes. It's essential to your investing discipline to establish minimum (MIN) and maximum (MAX) position sizes for different asset classes *before* entering a trade.

The way I do it is as follows:

- **Commodities:** MIN 1%, MAX 4%
- **Equities:** MIN 2%, MAX 6%
- **Fixed Income:** MIN 3%, MAX 10%
- **Single Stocks (Longs):** MIN 1%, MAX 3% and (Shorts): MIN 0.5%, MAX 2%

The Position Sizing framework above is generalized. I base the actual minimums and maximums for each asset on the volatility of that particular asset. For instance, Commodities are the most volatile so a smaller MIN and MAX position size is prudent. Specifically, Bitcoin is one of the most volatile assets on the planet. I classify cryptocurrencies as Commodities and size those positions accordingly.

Again, each investor should set up their own position sizing rules before they enter any trade.

MY FRAMEWORK FOR POSITION SIZING

All investors should define their minimum and maximum position sizes. Then, use our Risk Range™ Signals to incrementally add to or subtract from a position within those min/max ranges.

Dynamic Asset Allocation	Max	Min	Long-Short Equity Allocation	Long	Short
Foreign Currency	12%	4%	Maximum	6%	3%
Fixed Income	10%	3%		4%	2%
Equities	6%	2%	Minimum	2%	1%
Commodities	4%	1%			
Options	1-2%	-			

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Alright, so you've got an investment idea, you've established a position, you're abiding by my position sizing guidelines and that asset falls in value.

The next question is...

When Do You Buy The Damn Dips And Stay In?

My answer to that question rests heavily on my quantitative-based Risk Range™ Signals. As you know, my Risk Ranges generate a probable range for an asset based on its price, volume and volatility. These ranges suggest where you want to be buying (at the low end of the probable range) and selling (at the top end of the range).

So back to the question: *When Do You Buy The Damn Dips And Stay In?*

Here's my answer:

- A. When a market (or security's) price is signaling Bullish on both my TRADE and TREND durations
- B. When my Risk Range™ Signal is signaling a series of Higher Lows and Higher Highs
- C. When that ticker is nearing the LRR (low-end of the Risk Range™ Signal)

Those are the best dips to buy.

Less good set-ups have the following attributes:

- A. Bullish TRADE and TREND ... but with
- B. Higher Lows and Lower Highs in the Risk Range™ Signal

Those positions fall towards the bottom of my Long Only Asset Allocation.

IDENTIFYING BULLISH & BEARISH TRENDS ACROSS GLOBAL MACRO

If a long idea isn't "Bullish Trend," I'm not trading it. On the other side, shorts must be "Bearish Trends."



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What happens after we buy the damn dips?

- A. We either make money ... or
- B. We lose money

And that last point about "losing money" brings up the very next critical question...

When Do You Get Out of a Core Position?

- A. When you get stopped out?
- B. When your process tells you to get out?
- C. When you've made so much money that you just decide to get out?

For me, the answer is rarely C).

It's generally B) ... and if I really screw something up, it's A).

Getting "stopped out" means you're losing so much money that you have to stop it. Abandon ship! I used to run with a -12% stop loss rule. Now I use 6%, but that's AFTER I've gone to my MAX position (see position size rules above).

Getting stopped out is easy to understand. But how about B) "WHEN your #process tells you to get out"? Since my risk management #process is both disciplined and rules-based, that's an easy answer for me too:

- A. If something signals Lower-Highs in my Risk Range™ Signal, I start to reduce the SIZE of the position
- B. If something signals Lower-Highs and breaks immediate-term TRADE support, I take the position to my minimum (see position size rules above)
- C. If something signals Lower-Highs, breaks TRADE, and then breaks intermediate-term TREND, I'm out

So, let's recap and simplify things...

- If something breaks TRADE and TREND support, I'm #out
- If something is for sale and holds TRADE and TREND support (with High-Highs and Higher-Lows in my Risk Ranges), I'm buying it
- If I'm buying or selling, I'm usually doing so in increments of 50-150bps of my capital

I slipped another important point in there with bullet C). Contrary to the “all-in” investment talk on CNBC, it's always smart to buy incrementally in basis points of capital. (One basis point is one-hundredth of a percent or 0.01%, so if a position moves from 2.00% to 2.25% that's an increase of 25 basis points.)

Why do I buy in increments of 50-150bps of my capital?

At the low end of my Risk Range™ Signal an asset has more probable upside than when it's closer to the top end of the Risk Range™. Remember, the goal is to buy low, sell high. In other words, the amount of capital I'll deploy incrementally into a position depends on an asset's Risk Range™ set-up.

So here are a few more rules:

- A. When something is breaking down on my immediate-term TRADE duration, add less aggressively to that position when it's down
- B. When something breaks TRADE and a potential TREND breakdown is implied in my Risk Range™ Signals, do NOT buy more
- C. When snow is yellow, do not eat

I'll ask one final question here: How about YOUR Rules?

- A. Have you already established MIN and MAX position rules, by Asset Class?
- B. Have you already established how many basis points you'll buy and sell incrementally?
- C. If or when you violate your established rules, why are you doing that?

If you haven't thought through each of the questions above, I have three suggestions:

1. Read and re-read my suggestions above
2. Think about how you'd implement my suggestions above into your own investing process
3. Subscribe to Hedgeye

Again, the best way to minimize mistakes is to follow your rules-based process for WHEN to get in and out of a position.

The next few chapters will give you a better appreciation for why Macro matters, the issues with current financial media and how to weaponize your investment process with Hedgeye's risk management process.

CHAPTER SUMMARY

A Framework For Investing Success

- Over the years, I've found the best way to minimize losses when they inevitably happen is to have a rules-based process.
- A series of rules that you always abide by takes the sting out of mistakes. When you lose (and you will) you know precisely what to do next.
- Example of Position Sizing Minimums and Maximums: Equities: MIN 2%, MAX 6%;
- I base the minimums and maximums for each asset on their volatility. For instance, Commodities are the most volatile so a smaller MIN and MAX position size is prudent.
- If something breaks TRADE and TREND support, I'm #out
- If something is for sale and holds TRADE and TREND support (with High-Highs and Higher-Lows in my Risk Ranges), I'm buying it
- If I'm buying or selling, I'm usually doing so in increments of 50-150bps of my capital

Recommended Reading & Viewing

- Keith McCullough & Portfolio Manager Mike Taylor, "[Two Pros Talking Shop: Winning Strategies in Today's Market](#)"
- Hedgeye University: [Master the Market → Learn The Hedgeye Process](#)
- Robert Coram, "Boyd: The Fighter Pilot Who Changed the Art of War"
- Daniel Kahneman, "Thinking Fast & Slow"

The Hedgeye Toolkit

- There are two daily HedgeyeTV broadcasts you might be interested in. For Macro, join me every trading day on [The Macro Show](#). For stock pickers, join my entire research team and I daily on [The Call @ Hedgeye](#).
- Email support@hedgeye.com to discuss investment research options with a trained Customer Service representative.

CHAPTER 5

Conflicts of Interest

Since I started Hedgeye in 2008, I've been sidelined from virtually every single mainstream financial media outlet. That might sound ridiculous, but I can assure you it's not.

The timeless, dirty little secret about Wall Street is this: It's all about the money. Media is no different. Any financial "news" outlet that suggests it provides actionable insights for the average investor is lying. It's all about collecting advertising dollars (and maintaining access to the rich and powerful).

My firm couldn't be more different than the Old Wall and its media. I refuse to compromise when it comes to Hedgeye's core principles of transparency, accountability and trust. Our North Star is truth. We have no conflicts of interest. We get paid if our subscribers save and make money. Full stop.

It's sad to say this, but speaking the truth often gets me into trouble. If the cost of exposing frauds, cheats, and liars is getting banned from the mainstream media, I'll make that trade all day.

And now, two stories.

I'll never appear on CNBC ever again.

But, when Hedgeye was a startup in 2008, we needed to get the word out about our research. Perhaps naively, I became a CNBC contributor in 2010.

In these early days, appearing on the "leading business news channel" was a positive for Hedgeye. Sure, I would occasionally be instructed to be "less combative" on air. That was fine.

They had their bosses to answer to. I had mine: The Market. And I'd never hold my tongue if market prices or the facts in front of me were giving me a signal.

As my analyst team grew, the potential for conflict between my team and Wall Street grew as well. Back in 2010, Hedgeye had fewer than 10 total employees, but we were growing fast. Today, we employ more than 40 analysts, covering thousands of companies and have a payroll fast approaching 100 total employees. It was just a matter of time before I had a dust-up with someone else at CNBC.

As Hedgeye's CEO, I was ready for that. I would never stand idly by while someone publicly disparaged one of my analysts. I've always been a Mucker, in hockey and in business. If that meant going hard into the corners to win the puck for my team or call out nonsense live on air, so be it.

Enter Jim Cramer.

My last appearance on CNBC was sometime in 2013, so it took a full three years before we couldn't stand each other. Our Energy analyst at the time was a young guy named Kevin Kaiser. At the time, Kaiser's big call was warning investors about accounting shenanigans at **Linn Energy** (LINE) toward the end of March

2013. Kaiser argued the stock was worth about \$15, when it was trading a little under \$40, or more than -60% downside.

It was a big call and Kaiser had done the real hard work. LINE was a Master Limited Partnership (MLP), a tax-advantaged corporate structure that traditionally attracts individual investors looking for a mix of above-average yield and safety. Oil and gas exploration and production (E&P) MLPs typically acquire and operate older producing oil and gas fields with low decline rate fields (approximately 10% per year). These fields tend to throw off decent revenues and, since the MLP does not pay corporate income taxes, the company distributes excess cash flow to its unit holders.

These so-called “upstream” MLPs typically grow through acquisition of producing fields, rather than through expensive and capital-intensive exploration. Simply, E&P MLPs are in the cash flow business, and the MLP structure mandates them to distribute the majority (+90%) of their excess cash flows to unit holders.

Back then, there were 11 publicly-traded upstream MLPs in the US. LINE was the largest with a \$19 billion enterprise value.

Kaiser wrote the following:

“LINE may be the tip of a very large iceberg. Investors who are enjoying above-average returns from high-yield MLPs should look under the hood. While it is too early to say this whole business model is in jeopardy, LINE looks like a company trying to stay ahead of the curve by taking advantage of a series of accounting strategies. We do not mean to imply that there is anything improper about what LINE is doing. It should be enough warning for investors that their books are not transparent. Accounting rules have been so distorted by Congress and lack of clear regulation that no one needs to break the law in order to pull the wool over investors’ eyes.”

In a 57-minute presentation titled, “Where There’s Smoke, There’s Fire,” Kaiser explained the thesis in 55 slides. The thesis was threefold:

- *“We believe LINN’s business model is unsustainable.”*
- *“We estimate that LINN’s actual Distributable Cash Flow (DCF) during 2006-2012 may have been as much as 70% lower than the amount LINN reported.”*
- *“Investors are mistaken in valuing LINN like a midstream MLP or REIT. We believe that LINN should be valued like an E&P company - based on the underlying assets.”*

It was a masterful presentation by Kaiser on a large, battleground stock.

This didn’t sit well with Cramer. He was long the stock in his charitable trust and advised people to buy it in his Action Alerts product. A public battle ensued.

Cramer actually called Hedgeye “unscrupulous” and went so far as accusing us of violating the 1934 Securities Exchange Act in an article on his website and Twitter. “I did not know you were allowed to have bear raids since the ’34 act allegedly banned them,” Cramer wrote on June 17, 2013. “But I guess there is a LINE carve out!! Ha!”

He also attacked Kaiser’s work, not based on anything having to do with Hedgeye’s analysis, but because Kaiser was too young, according to Cramer. “My good friend Doug Kass has shown me the resume of the ‘expert’ ringleader attacking LINE. Almost 3 years experience! What a pro!!,” Cramer wrote. Cramer also hosted Linn Energy’s CEO on his “Mad Money” show to defend his company.

So, what happened after Cramer smeared Hedgeye and told investors to stay long Linn Energy? LINE shares completely evaporated. In 2016, the company filed for Chapter 11 bankruptcy. In other words, a donut.

Before Linn went bankrupt, we made a few more friends along the way. Most notably, billionaire investor Leon Cooperman, in a 2,000 word letter to the editor of Barron's, claimed Kaiser, as quoted by Barron's journalist Andrew Bary, was "wrong." Cooperman wrote, "we believe strongly that the distortions of the three Barron's articles will not, in the end, carry the day."

Here's an excellent excerpt from Mr. Cooperman's letter:

"We believe that this newly raised issue of a potentially large 2016 tax liability at Linn is a straw man erected by Bary and his short sources. Any investors who are concerned about such an eventuality should also be worried about the hobgoblins in their bedroom closet. Omega Advisors is comfortable with our investment in Linn Energy; we are convinced of the professionalism and integrity of the company's management; we are optimistic about the company's future growth and financial performance; and we believe strongly that the distortions of the three Barron's articles will not, in the end, carry the day."

You can read the entire Cooperman letter [here](#) with Hedgeye's point-by-point rebuttal.

Omega Advisors, Cooperman's fund, was Linn Energy's largest outside investor with 3.05% of the company's shares worth more than \$200 million. Mr. Cooperman was obviously defending what was Omega's fifth-largest position at the time, but we'd like to let the record show that Omega's views did not "carry the day." Hedgeye's research did.

Linn Energy = \$0 per share

Nice work, Jim and Leon. #Booyah

The sad part about the CNBC, Jim Cramer and Leon Cooperman dust-up is that a lot of investors followed Cramer and Cooperman into the Linn Energy buzzsaw. Cramer called himself "Mr. Linn Energy." We agree, Jim. Mr. Bankrupt.

The fact that Jim Cramer is still on television is beyond me.

Many readers will remember March 11, 2008. That's when Mad Money host Jim Cramer told a viewer, "Bear Stearns was fine!" at \$62 per share. Shortly thereafter, the investment bank (which was heavily exposed to subprime mortgages) was mercy folded into JPMorgan Chase (read: bailed out) at \$2 per share. Incidentally, Jim Cramer still has a job despite this egregious advice and hundreds more just like it. Moral of the story? From tulips to subprime mortgages, Wall Street always knows how to make a buck off unsuspecting retail investors.

Why is present day Financial Media in shambles? Let's quickly revisit the blossoming of an industry that has (to put it simply) screwed over so many workers and families.

In the mid-90's, the democratization of finance began with promise. Rather than getting gouged by boiler room stock jockeys, internet-based brokerage houses brought investing to an entire generation of self-directed retail investors with ads telling Americans to "Boot your broker."

The 'retail investor' community was born.

This was quickly followed by the Dot Com boom and the resulting bust. Retirement plans were dashed, fortunes were lost while IPO-crazed investment bankers lined their pockets.

In a fitting preamble for what was to come, an entire industry was rising around stoking investor FOMO for the next get-rich-quick stock pick. CNBC rode the retail investor wave to prominence throughout the mid-to-late 90s and early-2000s, as Jim Cramer began regular appearances on that network.

A mere 8 years later, the “democratization of finance” had once again gone awry. This time Wall Street peddled teaser rate mortgages to subprime borrowers and under the guise of promoting the American dream.

All of this came crashing down yet again. But not before a massive bull market run in stocks that was propped up by stock pumping media outlets that couldn’t admit the dopamine days were done.

We take risk management very seriously at Hedgeye. That’s why it makes our skin crawl when people like Cramer toot horns and yell “Buy, buy, buy!” to hundreds of thousands of investors every day. That’s NOT a risk management process.

Our repeatable, risk management process is designed to proactively prepare you for the next big market move. When we’re wrong, we own it, we know exactly why, and rest assured we won’t (and don’t) stay wrong for long. Every day we reserve the right to change our mind and get on the right side of the market based on the data we track.

- That’s why we run predictive tracking algorithms that are fed data every single day to spot inflections in economic growth and inflation.
- That’s why we employ a research team of 40+ fundamental research analyst + 15 Software Engineers and Data Scientists, monitoring every aspect of U.S. equities
- That’s why I developed a quantitative Risk Range™ Signaling process to identify bullish and bearish TRENDS across all asset classes in Global Macro

It’s the singularity of this process that keeps us on the right side of the grass every day. Don’t let your portfolio get killed by bad “advice” purveyed by unaccountable entertainers on Mainstream Media.

Second story. I was kicked off Fox Business because approximately \$140 million in equity value evaporated into thin air.

Let me explain.

I began appearing on Fox Business in 2014, eventually finding myself sitting next to respected business journalist and host Maria Bartiromo. For the next year, I’d spend two to three days a week seated next to Maria, offering my insights on the markets and scrapping with Wall Street strategists live on air.

At the time, I respected Maria. In her two decades at CNBC, she became the first woman to report from the floor of the New York Stock Exchange. Maria was a savvy, financial journalist who worked hard and was well-prepared to interview major business leaders and policymakers.

At first, sitting next to Maria was a breath of fresh air. As I understand it, she enjoyed my combative, no-nonsense style. Sure, occasionally, a high-profile guest would appear on the show and I’d be instructed to, “Let Maria do the talking here,” which I generally understood to mean, “Shut the hell up, Keith.”

That was fine by me. It was Maria’s job to delicately question these “masters-of-the-universe.” In the world of business journalism, asking hard questions while preserving access to the wealthy and powerful is an art I have no interest in ever learning. Two things feed financial media: Access to the big names in investing and advertising. If you push too hard on big marquee guests, they don’t come back on air. If you can’t attract industry talent, viewers don’t watch. If viewers don’t watch, you can’t generate ad revenue.

I didn’t care about all that. I wouldn’t waste a second of my precious time on politicians and policymakers, whose whole job is to tell their story on national television, not present facts and truth. So, when I was instructed to “Let Maria do the talking,” I sat patiently, watching the pre-market or pushed send on market

strategy notes that outlined key takeaways from my morning process. Back on camera, if Maria asked for my opinion, I gave it. That was the relationship. We had a rapport that made great TV, for a while at least.

At Hedgeye, we cover every aspect of the equity market, from Retail to Industrials to Global Tech and everything in between. Our 40+ analysts do their bottom-up, fundamental research within each of those sectors and identify a handful of the best 15 to 20 long and short stock ideas. Our Institutional clients – big asset management shops and hedge funds – pay us six figures annually to access all our analysts’ “Best Ideas.” I’m proud to say that when our analysts publish a new “Best Idea” long or short that the most successful managers in the business pay attention. Hedgeye research can move markets.

Around noon on December 14, 2015, our Financials team pushed send on an email. The subject line read, “Best Ideas Call Invite | WisdomTree (WETF) - Not So Smart Beta.” My last appearance on “Mornings With Maria” was just 21 days later.

I’m certain those two events are connected. I didn’t realize my Financials team, by publishing that WisdomTree short call on December 14, 2015, had just ended my relationship with Maria Bartiromo.

Shortly after Christmas, I was at a dinner party with some staffers from Fox Business, including Maria. The party was fine, but the vibe Maria gave me was ice cold. After the party, I messaged Hedgeye’s VP of Media and PR Dan Holland to see if I was missing something.

“Something just doesn’t feel right,” I told Dan. Dan replied that he’d look into it. Sure enough, weeks went by with no call from Fox Business to join Maria’s show. No big deal, we were building HedgeyeTV at the time and had just launched “The Macro Show” the previous summer which I hosted providing Macro insights and actionable takeaways before the market opened each morning.

Still, we were curious to understand what happened. We eventually pieced it together.

In the immediate aftermath of Hedgeye’s short call on WisdomTree, the stock fell like a stone. The stock had peaked in August 2015. One of our Financials analysts at the time, Jonathan Casteleyn, surgically laid out his short thesis that December in a 60-page slide presentation to Institutional clients. He wrote, “The company has too much reliance on ‘two’ few products.”

Casteleyn continued...

- *“Two-thirds of the company’s AUM resides in two products the HEDJ and the DXJ.”*
- *“Both HEDJ and DXJ are dependent on Dollar strength for returns... which has put in a 3 standard deviation move within a 10-year period something that isn’t likely to continue.”*
- *“Our analysis finds consistent underperformance across most of its strategies.”*
- *“Our 2017 estimates are -25% below the Street and we see a high probability of the firm missing Consensus’ lofty expectations.”*

It was classic rate-of-change based Hedgeye analysis. I was proud of the work this analyst had done.

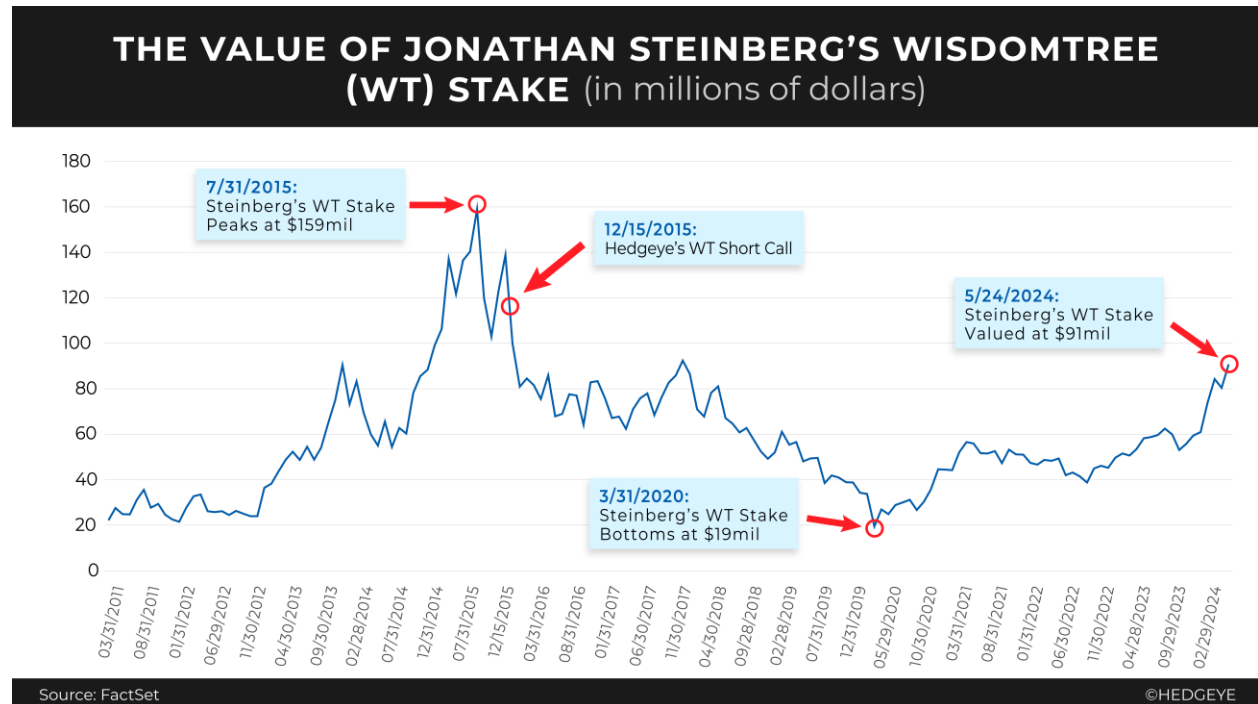
WisdomTree’s CEO Jonathan Steinberg presumably didn’t share my appreciation for the key takeaways from our analyst’s research. He definitely didn’t like that WisdomTree shares fell -30% in just one month after Hedgeye’s short call on the company.

My analyst was clearly on to something in saying that shares of WisdomTree were overvalued. From the peak in WisdomTree’s share price in the Summer of 2015 to its 2020 lows, the value of Steinberg’s personal stake in WisdomTree would fall from \$159 million to \$19 million. That’s a drop of \$140 million in Steinberg’s personal stake in less than 5 years. That must’ve been a gut punch for him.

Did I mention that Jonathan Steinberg is married to Maria Bartiromo?

Let's state the obvious here. Conflicts of interest aren't new. Power and money amplify the stakes. And, in the aggressive, zero-sum competition for trillions of dollars in investor funds that is the asset management business, the stakes could not be higher.

I have a lot more to say about this, which brings us to the final chapter.



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- Our 40+ analysts do their bottom-up, fundamental research within each of those sectors and identify a handful of the best 15 to 20 long and short stock ideas.
- I developed a quantitative Risk Range™ Signaling process to identify bullish and bearish trends across all asset classes in Global Macro
- The combination of bottom-up fundamental research and top-down Macro risk management is a winning formula. As I like to say, "It's the singularity of this process that keeps us on the right side of the grass every day."
- Our repeatable, risk management process is designed to proactively prepare you for the next big market move. When we're wrong, we own it, we know exactly why, and rest assured we won't (and don't) stay wrong for long.
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- Don't let your portfolio get killed by bad "advice" purveyed by unaccountable entertainers on Mainstream Media.

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- Hedgeye University: [Master the Market → Learn The Hedgeye Process](#)

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CHAPTER 6

Risk Happens Slowly, Then All At Once

Before I was fired from Carlyle-Blue Wave for being “too early” on the GFC, I had an unlimited travel budget and doors opening up for me as never before, but on some gut level my whole regimen was less satisfying.

This went beyond my losing money, which, let’s face it was humiliating and something I wasn’t used to. But I still gave the job my all, taking a 4:03 a.m. train to get in by 5:15 a.m., first one in the door. I tuned out the backlash I was getting over my negative posture on the markets. If anyone in my office shared my beliefs, they weren’t vocal about it. I didn’t care. I ignored the media hype surrounding the mere words “hedge fund manager” and didn’t worry about how much money I stood not to make that year if things continued.

I certainly enjoyed making money as much as the next guy, but there had always been more intangible rewards that came with trading a book, the thrill of the hunt, I suppose. Or maybe it was proving others wrong. What always motivated me most were people telling me I couldn’t do something. You can’t play for the Thunder Bay junior hockey team, you’re not ready. You can’t follow mining stocks, you’re a consumer - retail guy. You can’t do macro, you’re not Ray Dalio. You can’t time the market, you’re no smarter than the rest of the pack.

Now my peers were mocking me behind my back, some were openly mad at me. I felt I was putting my career at risk by speaking up in investment meetings against the hysteria in the markets, the bubble in our very industry, and what’s more, I don’t think I even cared. I never cared what people thought about me. I’d always been a “chirper” on the ice, and if people didn’t appreciate it, that was their problem.

I knew from studying the life of my grampa Alphonse that being able to ignore what everyone else thinks was the reason he ever started his many business ventures because all of his friends and family told him he couldn’t do it. I had just read David Nasaw’s book about Andrew Carnegie. The great steel titan, I’d learned, used to leave the United States for long stretches, retreating to the rural hills of Scotland to relax in a giant castle and fish in the loch, but also to think about the world differently from his industrialist rivals. Then he would kick their asses because he knew what was coming.

I think I know what’s coming.

Today, the media is so entwined with the interests of the rich and powerful that corporate interests are overrepresented in reporting.

For the media, it’s all about the money, outlets have tethered their business model to advertising revenue. Since that revenue is generated from the corporations they’re supposed to cover, expose and hold accountable, most reporting is effectively bought and paid for by somebody.

I think there’s a not-so-quiet revolution bubbling beneath the surface.

Journalists are leaving traditional media platforms. Social media has enabled these “content creators” to capture a loyal follower base. They’re launching subscription services and creating independent newsletters to monetize their loyal followings. Unshackled by the moderating power of corporate interests, we’re seeing a blossoming of different opinions, viewpoints and experiences.

The current environment is not without its drawbacks. “Audience capture” describes when a content creator or social media influencer tailors their message to what their audience wants to hear, potentially compromising their own identity or goals.

Where is the media landscape headed? What I’d like to see is a return to the Muckraker generations of old. In the early 1900s, Ida Tarbell was a pioneering investigative journalist who played a pivotal role in exposing the ruthless business practices of John D. Rockefeller's Standard Oil Company. Her work helped usher in the Progressive Era of reform in the early 20th century.

Tarbell's interest in Standard Oil stemmed from her personal experiences. Witnessing her father's oil business struggle against Standard Oil's aggressive tactics in the 1870s fueled her determination to expose their wrongdoings.

In 1902, Tarbell embarked on a meticulous investigation of Standard Oil for McClure's magazine. Her 19-part series, published between 1902 and 1904, rigorously documented Standard Oil's anti-competitive practices. She unearthed evidence of secret deals with railroads, predatory pricing to drive competitors out of business, and ruthless tactics to control the entire oil industry.

Tarbell's exposé, later compiled into the book "The History of the Standard Oil Company," became a national sensation. It ignited public outrage against Standard Oil's monopolistic practices and helped lay the groundwork for the Sherman Antitrust Act's enforcement against the company. Though Rockefeller himself remained wealthy, Standard Oil was eventually broken up into 34 separate entities in 1911 by the Supreme Court, a decision heavily influenced by Tarbell's investigative work.

Tarbell's work became a hallmark of investigative journalism, earning her the label "muckraker" – a term she disliked but which reflected the era's focus on exposing corruption and advocating for reform. Her work on Standard Oil is considered a landmark achievement in American journalism.

Would Ida Tarbell have a Substack today? Maybe.

She would find like-minded company at Hedgeye.

At the same time, Wall Street’s entire business model is conflicted, compromised and constrained. Sell-side analysts aren’t paid to tell the truth. According to FactSet broker ratings, over the past 20 years, less than 10% of the S&P 500 companies tracked by Wall Street each year were rated “sell,” despite the U.S. economy entering multiple bear market crashes and two full-blown recessions over that period. There’s a reason for that. These analysts are paid to help the investment banking side of the business generate fees and make sure institutional and retail investors are always in buy mode.

Combine Wall Street’s conflicted, compromised and constrained business model with a mainstream media incentivized to parrot Wall Street BS and you have a recipe for disaster. The average investor doesn’t know that the whole system is stacked against them.

My goal with Hedgeye has been to aggregate the best-of-the-best analysts on Wall Street covering every aspect of financial markets. We identify longs and shorts. We expose frauds, cheats and liars.

Our subscribers get to listen in to our morning Independent Research team meeting, save and make money on our research and analysis, and learn from our analyst research team every step of the way (covering Retail, Financials, Energy and everything in between).

I always thought of Hedgeye as a world-class hedge fund you could see inside. If you could look inside that world-class hedge fund what would you see? That's Hedgeye.

Using this analogy, the way to think about it is, I'm the portfolio manager or Risk-Manager-In-Chief and my analysts are feeding me Macro and Stock ideas that all flow into my process. You get to listen in, learn our Full Cycle Investing process and make your own decisions. We're building something that doesn't exist on Wall Street: Hedge fund quality research for all investors.

You get a front row seat inside my day. Here's what that looks like...

- The Macro team feeds me economic and critical market data before 5 a.m. ET each day.
- At 5 a.m. ET, I'm already up analyzing that data, interpreting that data through my Risk Range™ Signals across asset classes.
- I send key takeaways from this process to subscribers and institutional investors by 6:30-7:00 a.m. ET (in my Risk Range™ Signals, Early Look and Top 3 Things).
- My fundamental, bottom-up equity research team joins me on "The Call @ Hedgeye" at 7:45 a.m. ET. This is our daily, morning firm meeting. You listen in as my team discusses the most actionable, timely topical stocks and themes in each Sector. I provide top-down Macro commentary filtered through my Risk Range™ Signals process.
- At 9:00 a.m. sharp, I'm on "The Macro Show," having ingested all of this information across my process and 40+ analysts and I'm LIVE with you, explaining the actionable takeaways impacting the investing landscape over the days, weeks and months ahead.

You can get access to all of this before the market even opens. This doesn't include my intraday signals (from my coaching notes and intraday signals in *Real-Time Alerts* to a sneak peek inside my actual long-only ETF account in *Portfolio Solutions*).

Since I made the decision not to appear on Fox Business or CNBC, Hedgeye has been quietly building out the infrastructure to go direct to institutional and retail investors alike. We're successfully charting paths to reach you, the investing public, directly. In markets, risk happens slowly, then all at once. The same holds true for Old Wall Street and its Media.

I really appreciate you taking the time to read this eBook. Again, since it's officially us vs. them, we're always in guerrilla warfare marketing mode at Hedgeye. If you've enjoyed what you read, I have two small asks of you...

1. **Feel free to share this book** with anyone you think could benefit from the investment insights I've provided.
2. **Subscribe to Hedgeye** if you're interested in accessing actionable investment insights from my team every single day.

On that latter point, we have research for every single type of investor. If you'd like to discuss becoming a Hedgeye subscriber with a trained Customer Service representative, email support@hedgeye.com.

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- We have research that fits the needs of every single type of investor. If you'd like to discuss becoming a Hedgeye subscriber with a trained Customer Service representative, email support@hedgeye.com.

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Appendix: Keith's Coaching Notes

We have compiled below a list of Hedgeye CEO Keith McCullough's favorite "Coaching Notes." These Coaching Notes are a hand-picked selection of his Keith market strategy note the [*Early Look*](#) that he wanted to share with readers of "Master The Market." These Early Look "Coaching Notes" are examples of the practical application of the Hedgeye process and great supplemental materials to "Master The Market."

- [Narrowing Risk Ranges](#): What does a narrowing in Keith's Risk Range mean for an asset? Less volatility.
- [Gold: Front-Running The Fed & Flows](#): Keith explains his process of reviewing the Risk Range Signal set-up for an asset within the context of the economic set-up (i.e. our forecasted Quads).
- [Signal Strength Decision-Making](#): An asset that is developing "Signal Strength" on Keith's Risk Range™ Signals is "Bullish on both my TRADE and TREND durations and signaling higher-highs in my Risk Range™ Signal"
- [Bought More QQQ, Bitcoin, etc](#): Keith reviews how a shifting in the economic set-up (i.e. our forecasted Quads) is informing his decision to buy specific assets (in this case, Tech and Bitcoin)

Investors interested in an *Early Look* can review what's included [here](#). Email support@hedgeye.com to discuss investment research options with a trained Customer Service representative.

Acknowledgements

This book is about sharing my experiences, and the lessons learned from nearly a quarter century on Wall Street. I've spent nearly 16 of those 25 years building Hedgeye alongside my teammates. That's why there are two groups of people I need to thank because, without their support, this book would not be possible.

I would like to thank my family and my firm:

Ishmael Asad, Marina Bacino, Nicholas Balch, Joshua Balch, Patrick Barber, Daniel Biolsi, Michael Blum, Kerrie Brinckerhoff, Jamie Bruno, Christopher Chang, Forrest Chang, Bennett Cheer, Gene Cleaves, Matthew Cooper, Jack Cromwell, Scott Deming, Christian Drake, Augustine Ekpoudom, Jeffrey Esser, Emily Evans, Ian Fignon, Casey Flavin, Christian Ford, Andrew Freedman, Brandon Gastelo, Eric Gendron, Paul Glenchur, Phyllis Goldberg, Geoff Gregoire, Jane Hamilton, Alexander Handler, Dan Holland, Neil Howe, Kevin Hurley, Sean Jenkins, Daryl Jones, Todd Jordan, Katelyn Kozlowski, Alexander Ledda, Drago Malesevic, Sam Marshall, Callie McCullough, Cheryl McCullough, Cole McCullough, Jack McCullough, Jenine McCullough, John McCullough, Laura McCullough, Liam McCullough, Lucy McCullough, Reese McCullough, Ryan McCullough, Vivianne McCullough, Brian McGough, Regina McGough, Robert McGroarty, Jeremy McLean, Robert Milburn, Matthew Moran, Daniel New, Brett Novak, Anthony Parsio, Kevin Peel, Howard Penney, Arianna Petillo, Ben Pirko, Ryan Ricci, Robert Rich, Jason Rogers, Gregg Ruais, Puneet Saini, David Salem, Diego Scataglini, Daniel Seltzer, Grace Shay, Moshe Silver, Rob Simone, Frank Slezak, Joshua Steiner, David Talbott, Tom Tobin, Ryan Tucker, Jose Valcourt, Fernando Valle, Teri Van Noy, Jay Van Sciver, Emma Vlasic, Tanya Waite, Felix Wang, Ryan Wilson, Hayley Wolff, Ethan Yee and William Zegras.

A special thanks to my *Diary of a Hedge Fund Manager* co-author Rich Blake.

About the Author

Prior to founding Hedgeye Risk Management in 2008, Keith built a successful track record as a hedge fund manager at the Carlyle-Blue Wave Partners hedge fund, Magnetar Capital, Falconhenge Partners, and Dawson-Herman Capital Management.

For many years, Keith was a regular market guest across financial media including CNN and Fox Business, as well as a contributor for CNBC and Bloomberg. Disappointed by the conflicts of interest and quality of Establishment Media, Keith launched HedgeyeTV in 2014 and hasn't looked back.

In addition to producing a wide array of written Macro research (covering the top 50 global economies), Keith hosts his own show, "The Macro Show" weekday mornings as well as "The Call @ Hedgeye," which features the firm's entire 40+ analyst research team discussing their favorite long and short stock ideas.

Keith also hosts the acclaimed interview series "Real Conversations" which features in-depth conversations with the world's top investors, strategists and thinkers.

The goal behind Hedgeye's investing research platform has always been to push the boundaries of financial research and provide data-driven, conflict-free, hedge-fund quality research to all investors.

Keith is the author of the popular book, "[Diary of a Hedge Fund Manager](#)" and founder of private equity firm, Seven7. He began his career as an institutional equity sales analyst after earning an economics degree from Yale University. While at Yale, he captained the men's ice hockey team to a Division I Ivy League Championship.

Hedgeye has come a long way since Keith started the firm in 2008 alongside his cofounders. The firm now provides research to institutional investors across the globe who collectively manage over \$10 trillion in assets.