

**Nick:** Good morning. Today is Saturday, the 27th of April. We've had an exciting week and a very exciting week coming up next week. So let's have a look at what happened last week. Everything in the real economy continues to be extremely strong. Some people thought that GDP was slightly weak. It wasn't. It was quite, quite strong.

The the only weakness was in inventories, which basically means that we need to restock, which will make the next GDP even stronger. So there is nothing out there that's showing us any kind of weakness. Is there, Andy?

**Andy:** No, yeah, the employment number on Thursday was finally below 212, which has been sitting at for a while now, 207 in terms of nonfarm payrolls sorry, not nonfarm payrolls, jobless claims and so, yeah, the economy is, as we've been describing for ever Strong economy, inflation holding and staying above target and markets have begun to accept that.

**Nick:** Yes, and that was actually reflected in the pricing of the of the auctions that we had last year. Sorry, last week, twos, fives and sevens, they cheapened up the curve and they, the auctions went okay, nothing to write home about, but they, they got them off and now, that they're still underwater.

And every single auction comes out and within a couple of days, it's underwater. So people must be getting quite fed up with with buying bonds at negative carry and losing money either on the carry and or on, on the reval. So. The situation is completely unchanged, but what could change and change the situation is the QRA and the FMC next week.

And that's what we should concentrate on.

**Andy:** Sure. I just want to review briefly what happened last week though. There were some big market moves equities fell a couple of percent and then rallied back. That was mostly earnings. If you look at the earnings MEDA's earnings were showed that Zuckerberg is willing to spend and the stock was punished for it.

Things like that happened earlier in the follow up the prior week, like, like Netflix, those stocks stayed down. And even Microsoft and Google were interesting to observe after the market bounced On Thursday, it's simply oversold, led by semiconductors. Microsoft's earnings were, very good as were Google's Microsoft on the other hand closed below where it opened before the sell off.

So by and large, Microsoft didn't really do much. In fact, Trade it down for the week and Google was an exception. It did very well, but I would say the earnings were not being rewarded in the same way as they had been the last quarter. And so we run into next week where the first of the semiconductors AMD shows up and semiconductors have rallied a lot.

All of the semis are back near their highs and that shows to me some, when the market feels like it is not vulnerable to a further sell off, market participants rush to the stocks that have done the best. And so, and that's less and less the Mag 7 and more and more narrow to semiconductors.

**Nick:** And, as I keep on saying, as soon as the bond stabilize, people come into, buy equities and wish them back up towards the highs, it seems to be a repetition of the same old story that we've seen for quite some time.

**Andy:** Right. And I just want to say one last thing about last week, before we move on, the BOJ did not surprising us at all did end up being fairly well, as dovish as they could be.

They didn't change the rate and they didn't change the bond buying patterns in an extremely curt statement. And. Currency's really moved a lot for the week, the yen went from 1.53ish at the lows to 1.54ish to peaking at 1.5834 on the close. So, yen weakness is a story that is Very important, and some believe that there's some sort of, willingness to by the treasury to help in the yen weakness as it leads into the QRA.

We think there's nothing to that story, but it does come in, so we lead up to the QRA and the FOMC meeting next week. What do you think? Nick,

**Nick:** I think it's going to be a boring Q. R. A. Because I don't think there's any need for Janet to change anything at all. It was pre announced during the last Q. R. A.

That things should Be it should remain roughly as they are going forward for quite some time I see nothing that has changed since they made this announcement What three months ago? Nearly now That would lead them to change that of course they could but I just see no reason for it So the central case has to be that coupons and bills will be maintained at roughly the same kind of proportion, which is 25%.

And. We just trundle on what are the consequences of that? It just the same amount of issuance. Now, first of all, we should say that a lot of people are

talking about sizable reductions in the TGA. Why would they do that? I don't get it. The TGA is there for a purpose, right? Andy, it's a stated purpose of the treasury to have enough river reserves.

In case of market disruptions to last a certain period of time, if she were to reduce the TGA, that would be going. Straight against policy, wouldn't it? Yeah, I think

**Andy:** we should step back for viewers who are new to us and viewers who still need the refresher. There's really three things that Janet the Treasury can do in the Q.

R. A. One thing they can't do much about is the budget deficit. It's going to be what it's going to be. And perhaps tax revenues are going to be above their estimate. Perhaps they're going to be below their estimate, but the spending is fixed. So she really can't do much. She has to finance that deficit.

The only thing she can do is choose the composition. Which is more coupons, less coupons, more, and bills are the plug. We think she will choose the same amount of coupons. As in the last quarter and the other thing she can do is reduce issuance. Thus reducing the need for both coupons and bills and she can reduce issuance by spending some of her checking account. Which is what Nick was describing the treasury general account the tga that account has a little under a trillion dollars in it and it has risen in the last two years for very good reasons.

We all paid our taxes. And so had they expected that? Of course they had expected that, and for that reason, their financing needs are only 200 billion for all of Q2, even though we run a budget deficit of 400 billion quarterly, if you annualize it. And we have to pay back the fed 180 billion. So, the normalized amount of issuance is about 580 billion each quarter, but we only plan on issuing 200 billion this quarter because our checking account is going to, was filled up.

By our, by the tax receipts we had and will be reduced by the paying back of the Fed and the budget deficit. And so it's going to go, it's almost a trillion now. And by June 30th, it'll be down to their target of 750 billion. So that. Is not that shouldn't be factored into the market at all. What Nick's describing is in the first half of 2022, 2023, because of the debt ceiling, the government reduced its issuance sizably because it was not allowed to issue more debt and spent its treasury general account from 750 billion, where it is targeted now down to practically zero.

That was against their own policy for prudent cash management. They did it because they had no other choice, but many market participants are expecting the Fed, the treasury to use that account. To pump the economy, which would require them violating their own internal policy for safe management of their cash account for no reason except political reasons, not because there's a debt ceiling, but because they just want to.

And so let me tell you briefly that about that policy back in September 11th, 2001 we found out that for 5 days, the government couldn't issue that. No, the markets were closed because of a market disruption event. The tragedy of September 11th we couldn't issue bills and we had to continue to honor our obligations on bills and coupons that were maturing and to spend to send checks to social security and all the other places we sent checks to.

And so we developed a policy on that, which is in a market disruption event, the treasury must keep on hand five days worth of spending, assuming it cannot issue so as not to bankrupt the country or cause a default or have its citizens not get its money. And so that's the reason why the treasury general account is kept in at its current level.

It's five days worth of spending. Yes. 750 billion gets spent every five days. Of course, we issue to cover that, but that's the policy. And so we don't think there's any chance she messes with that policy for political gains. And so that's the one pump. The second pump is the probably the more likely thing is she could change her and we don't think it's likely she could change the issuance to reduce coupons and reduction of coupons has in the past and would in the future.

Going today result in asset price rallies. So we're going to pay attention to that as well as any monkey business. She may pull, cause we don't know what she'll actually do. We met that she may pull with the TGA.

**Nick:** Well, I'm going to nail my colors to the mast and I'm going to say that the TGA drawdown that you've just so well described is extremely unlikely.

I would give it a 0 percent chance. I think the repercussions would be. Large in terms of confidence in a treasury secretary who is so overtly political, I think the dollar and gold would actually spike in different directions. I, the dollar down and gold up. And I just don't see any. Any gain, any particular gain immediately from doing so.

So I will say the odds of that are close to zero.

**Andy:** Yeah. So I would say to add to that, I agree completely. She's not going to do it. However, she is a political operative and every treasury secretary in history has been in the business of making sure the administration wins the next election. The question is, why shoot your bill today?

The S& P is at 5, 100 up 20 percent from the lows and 5 percent for 5, 6 percent for the year. Interest rate, 10 year interest rates are at 475 ish. The GDP is strong and projected to be 3.9 percent next quarter and strong this quarter. Inflation is heading in the right direction and unemployment is 3.

8%, extremely tight. What gain, what can she win by pumping today? Now, that's it. She is a political operative and at 4, 500 on the S and P and some negative employment prints in in June or July. And she has another shot at the pump on July 31st. And I believe she could then, but she has no incentive to do it today.

**Nick:** I absolutely agree with you there. There's just no risk reward in the calculation for her. And even if The scenario that you've just described of S and P's down at 4, 500 and so on. I think the TGA is the least likely way to do it simply because it's so overtly political. The bills coupon makes you can justify for whatever, for whatever reason, just reducing the ability of the country to, honor its obligations to me is just.

A ridiculous way to to go about it. In any case, we will post a table of what we think the most likely outcome of the TGA is and what the likely market reaction is. So you can sit and as soon as we've seen it, we've naturally send you an email and decide what to do. I think the, this is going to be a boring one.

We hope. And therefore volatility probably will go down and that will be the most likely path that we will choose to hedge our exposure. But otherwise, what do you think, what do you think the the Fed's reaction is going to be? Is that going to be a boring FOMC as well?

**Andy:** Well, What are they going to do?

They can't do much. They have no, they're not pulling any levers. They're not going to change the interest rate. It's going to be the same as it is today. They, and so it'll be all talk. And the talk will lean hawkish probably, they're losing, they're not losing confidence about the path of inflation, but there, there's nothing in the recent data that would give them more confidence.

And they're certainly not getting more confident at best. They're staying. Slightly less confident, but they're not losing confidence. They're just slightly less confident. And so, it modestly hawkish outcome. It makes sense. We're going to pay attention to whether they taper cutie or not. Our sense is that they continue to discuss it and do not announce a particular date when they're going to taper quantitative tightening.

But regardless, the quantitative tightening taper is small as a small factor in our market view, relative to the composition of data. Of treasury issuance from the QRA, and I do want to tell you about that table briefly. We'll provide you a grid, essentially, of how much gross issuance the treasury does in coupon bonds, which is all they'll tell us.

And that gross issuance will tell us whether they've decreased coupon bond issuance, kept it the same, which is our expectation, or increased, which is unlikely, but possible for some minor technical reasons. Anyway, we'll provide that chart and it'll give you a sense of where we think you should do things depending on the outcome, and then we'll confirm that with an email in the morning.

Your view on the Fed, Nick?

**Nick:** My view is that the pricing has is 99 percent that they do nothing in June. And I see no upside for pal to confirm to a hundred percent. What does he gain by doing that? So he will keep his options open. He might say something slightly hawkish. And that is that he has lost more confidence because the PC data on Friday was slightly higher than expectations because of the revisions of the previous months.

So he has absolutely no reason to say he's more confident about inflation going down to target because the data just does not support it. And therefore he. Could be slightly hawkish, but I don't think the reaction of the market is going to be that great because we all know that he's not going to hike and that we are a long way away from the fed deciding that the next move is going to be equilateral, i.

e. they could hike or they could cut and that data for them to make that kind of decision won't be around for at least a couple of months and therefore no upside for from him being extremely bearish. And that, that outcome would be very bearish if he said, Oh, no, we could hike just as easily as we could cut.

Now that would actually move rates quite a bit, certainly at the very short end, and that would hit all assets very hard.

**Andy:** I think some of the FOMC members are. Would be certainly no FOMC meet member at this stage would say, yeah we really are going to cut aggressively, but there are a few that's think that hiking is a possibility.

I don't think Powell in the press conference will provide that type of guidance. He'll leave that to the. June meeting where the scp will once again be done and we'll see what the individual fed members Think and without question if the data stays where it is They're going to reduce the number of cuts in 2024 and the market's already there.

**Nick:** Yeah, absolutely So to sum it all up qra, we will know something on monday morning We will know most, in fact, everything by Wednesday at 8 30 in the morning. Eastern standard time. You will most probably get an email from us Monday, but certainly Wednesday, and then we'll decide how to change our portfolio.

If any changes need to be made. Absolutely. Thanks for listening. Speak to you next week. And now let's have a look at the portfolio. So on Friday, all our options either expired or we close them out as advised. And this is the result. We are at 35 percent in equities, about 20 percent in bonds, 10 percent in gold and commodities and 35 percent effectively in cash.

And I think this is a prudent way to go into the QRA and the FOMC. We think that not a lot will change, and if it doesn't, the likelihood is that we sell some out of the money calls for one month against our equity position, because if everything stays the same, it's extremely unlikely that we're going to sell.

Equity pricing can improve substantially and we'll probably sell some calls against our bond portfolio as well because the likelihood is that bond prices can't do very much better either. That will be stability for the next month at least until the let's call it the June FOMC or until the pricing or sorry, until we find out what the CPI is for next month, which is two or three weeks away.

So for quite some time, the market is unlikely to do very much in any case. I've written that down in the order entry. We naturally have no orders but be prepared for an email anytime next week. We will most likely send you one on Monday if something happens which is unforecastable at the moment in the first part of the QRA.

but certainly you'll get one on Wednesday and we will tell you what we are doing to the portfolio or everything is updated the broker statements are uploaded the monthly performance and also the weekly performance chart it's all in there we think we are in a comfortable place where we don't need to do very much and we can react to facts And the facts will come next week.

And finally, an administrative point. If you ever have an urgent market question after you've received an email and you don't understand what it means or anything like that, please send me an email. To Nick at to graybeards. com rather than putting up a question in the comments section Simply because I only look at the comment section once every day once every two days Because I assume that it's nothing urgent, but if you have therefore an urgent question Please email me rather than posting a question here.

This is all for next week. Wish you a wonderful weekend and tomorrow, next week is definitely going to be exciting. So be prepared to receive an email from us and act on

it.

