Nick: Good morning, ladies and gentlemen. Today is the 15th of June, another Saturday, another episode of Two Gray Beards, after a very eventful week for both the U. S. and Europe especially, and we'll talk about that in detail. So Andy, do you want to go through the FOMC and what you made out of it?

Andy: Yeah, sure. You know, it was very interesting.

The FOMC was more hawkish than I was and I was and we were and I was pretty hawkish. You know, it was a fairly big surprise that the feds dot plot eliminated the the FOMC. To cuts went from 3 cuts to 1 cut in 2024. Now, in practice, they just pushed it out to 2025, but they did reduce that by 1 cut as well, which.

Is consistent with them thinking that they are not yet done with battling inflation and also notice, notice increased the long term run rate to 2. 8%, which was a surprise also hawkish and that was built on data, which gave, which they moved their inflation points. forecast for poor PCE to 2.

8, which has risen by 40 basis points since December when they were extremely dovish. The GDP forecast didn't change. It remained where it was. And so all in all, it looked to me to be a, you know, a quite hawkish dot plot showing that the committee has really decided that they're going to basically be on pause for a while, not hike, but be on pause for a while.

And then Chairman Powell at the press conference, who just can't help himself from being dovish. Almost, almost all the time. I mean, there's rare occasions like the Jackson Hole 2022 meeting where he dropped the mic and was, there will be pain. Of course there wasn't. But he actually supported the hawkishness, which, you know, is unusual for him.

Now, he wasn't hawkish per se, but he wasn't He didn't follow his tendencies and be extremely dovish. And that what's interesting about that is we had basically a month now with one exception in the non farm payrolls data and the income growth that associated with that we've had weak data and that morning and incorporated into their dot plot or allowed to be incorporated into their dot plot by the members, they had a.

ice cold CPI number. And it's possible, not certain, but possible. They had an inkling of what the PPI number would be the next day, which was also ice cold, creating a PCE, which is their preferred measure, Chord PCE measure that could be very close to zero for July. Sorry, sorry. When it's released at the end of June for The data from May.

So all in all, if you look at all those things, they remained hawkish knowing that they were going to get a very favorable set of inflation data. A

Nick: couple of points I'd like to make about the year end PCE target of that they moved up to 2. 8%. For that target to be met because of base effects, you really need to have a monthly PCE now, from now until the end of the year, which is sub 2%.

So, you are really, look, and that annualizes to somewhere around two and a quarter. Which is not very far away from the, their actual target. And I think that that is why the market took it not hawkishly because yes, the dot plots were hawkish, but I don't think the overall impression the market got was that they were looking for any sign of acceleration of inflation.

And therefore, that still means that at worse. That they are on hold. There is absolutely the market is assigning is zero probability or as close to zero. It makes no difference to them having to hike. Or even thinking about hiking from now until year end. And that is why, you know, even the short end did slightly better.

But I think the real news and the real reason why, why the bond market did better and equities Marked time was because of what happened in Europe. And I think we should talk about the European situation because it's potentially very, very serious and it would completely reverse any kind of position that the Fed might currently have because the implications could be that great.

So what I would like to say about the situation in Europe is this, it's. much graver potentially than Brexit because it's a political situation that goes to the heart of the functioning of the EU. The UK was never central to the EU. France, Germany and Italy are the three founding countries and they are politically the central axis around which all EU politics are based.

Reverberate. Now what we saw this week as a result of Macron's decision to call early elections having lost the election really badly is basically a credit crisis, not a risk off crisis, but a credit crisis. I, we had The OATs in France and the BTPs in Italy to a certain extent, and much less so in, in Spain or Portugal as, as the periphery completely blow out and blow out to levels that we haven't seen since the Euro crisis of 2011 2012.

That is very worrying because the potential implications for France. having a populist government that increases the budget deficit and breaks all the EU rules and therefore politically says to the, shows the middle finger to the EU, are possibly quite great. Much greater than Brexit for sure. And that is why you had a very bad reaction in European equities, and you had a very bad reaction in European bonds.

And I'm absolutely sure that a great proportion of the money that flowed out of Europe and European bonds and equities came into US equities, the safety of US equities, And the safety of us bonds and that's probably why the bonds reacted so much more Then one would have expected them to react as a result of the FOMC.

That I think is the current situation and how it evolves is going to be very, very interesting for all asset prices. Anything you'd like to add, Andy?

Andy: Yeah, I mean, I guess the question is what's changed and what are the odds and things of that nature? And I completely and totally agree that the

gravity of the situation is high. And what I mean by that is, you know, it would have significant effects if the EU or the Euro itself were to Were to fall apart in some way. The consequences are, you know, what we'll see as time goes on, but the consequences would be great. And the question is should we do anything about that?

And is there, is it likely, and I would just reiterate that it is not likely that a populist government if elected would then succeed in creating enough. Pressure to withdraw from the euro. Very unlikely. But anything's possible. And so you have to just be aware of that and measure the gravity of the situation versus the probability and we'll get some data on that and we'll see how markets act as that happens and we'll have your back as it relates to, you know, our thoughts.

Nick: Absolutely. Now we'd like probably to stress that while. Say two weeks ago, the probability of the euro falling apart was zero. Now it's 1%, 2%. It's not 10%, 20%, 30%. So the last thing we'd like to get You know, so leave you with is an impression that we are thinking that it's doom and gloom. We don't It's just that the market has assigned a probability To that happening which might be too high or too low But it's still a very low probability and that is why the market whenever it's uncertain what does it do it buys volatility the volatility spread between european equities and The vix in the us has blown out By 500 600 basis points and he was always trading car And these things are the things that make markets These are opportunities that we might be able to exploit over the course of the next couple of weeks For your information.

We have the first round of the French election is going to be on Sunday, the 30th of June, and the second round is on Sunday, the 7th of July. So by the 30th of June, we will have an idea. And on the 8th of June, I think we will know what is happening and the markets will naturally react accordingly. But the high level That we'd like to leave you with impression is that it's very unlikely that the European situation calms down tomorrow.

It won't calm down until the 8th of July and therefore the likelihood of the US market being able to rip away in the course of the next two or three weeks is very low. And that is why I will say later on that one of the possibilities is to overwrite the calls that we have. But in any case, our portfolio, I think, is extremely well positioned for whatever might happen.

We have 540 calls, and therefore we have a 2 percent or so on that position. We have Three to five year duration roughly in our bond portfolio Which means that if things blow up that part of the portfolio Will perform very well because let's not kid ourselves the fed wrote The dot plots according to the data they had when they reach those conclusions If a very bad situation develops in europe the likelihood of a european recession becomes quite high And therefore that impinges on the dot plots that the fed has the likelihood of them easing Would go up exponentially if something bad were to happen in Europe and therefore the part of the curve that we have is going to perform much, much better than the long duration part of the curve.

Andy: Right. You know I, I, and that's what we've been Tweaking our portfolio to reflect that limited upside in equities while still remaining long and taking some profits and some of the high flyers. And. Selling the little bit of TLT we had and placing it in sensible things for the outcome that we have.

I think that's the way you want to be positioned with the circumstances as they are at the moment. Nick, what do you think about the slowdown itself though? You know, we've had this slowdown of data. Do you have any insight on that? I'm struggling to have an insight?

Nick: Yeah, no, I, I, All I can see and rely on really is the price action.

We have the Dow stocks, which are the, let's call them the old economy stocks at zero for the year, i. e. no return. Then we have the Russell, which is down approximately 3%. So the market does seem to be believing this story of a slowdown and with the European situation that might be getting exaggerated.

But the data is showing a little bit of a slowdown now whether that is enough to bring the fed or make the fed cut Earlier than they would like to I think most houses have agreed that they're penciling in the september area to to to do the first cut I would find that unlikely because september is the You last meeting before the election.

So I find it unlikely that for, for political. considerations they would do that. I think it's either July, and that becomes, that is, you know, getting more unlikely by the day unless stuff happens. And then you have November itself, which is the day after the election. I think they would much prefer to cut The day after an election than the month before again for optics No other reason but it to me it all depends now how badly things develop in europe because Let's face it, if Europe goes into recession, how far can the U.

S. be? It's such a big part of the world economy and the, and the SBX, most of, and the Dow, especially stocks are so tied in with world trade and Europe being such a large proportion of world trade, it, you know, the U. S. is not an island and cannot remain an island for very long. At the moment, people are doing the obvious trade, which is selling the stocks for safety and buying SBX with it.

And that will probably be the way for the next week or so. But if things really go wrong in Europe, then the SBX will not be able to sell. You know, hold on to these gains and we really will have a slowdown. I have no particular insight into whether we're having a slowdown at the moment or not, but we do have retail sales next week, which could give us a further hint.

Andy: Yeah. Yeah, we'll, we'll look at the data. You know, the data is fairly light next week. We have two auctions and retail sales. And I think there's some PMI data, maybe. Yes. The. When you look at all that data, we're not going to get a ton of information. So it is going to focus on the things that we're seeing that we've just referred to in terms of France and so on.

You know, to me, there's still this idea. We've seen slow down stocks that suffer and slow down, slow underperforming. We've seen stocks tech stocks and Nvidia in particular continue to outperform. And so my question is. Is there an economy in an economic outcome? Let's assume we either have the potential of this slowdown extending or reversing.

And to the extent that it extends, it seems to me that we're going to continue to see underperformance of the economically sensitive old economy stocks and outperformance of the Big cap tech. And if it reverses, that's when you could get a broadening, but I don't think that's going to constrain people from chasing, chasing big cap tech.

So, you know, it seems like big cap tech is positioned to be having, to have a asymmetric out continued asymmetric outperformance until it's not. And that until it's not phase just has, there's no, it's not obvious that that's happened. So, you know, I think that's where things are and we'll just continue to chop along the way.

But to think that you're going to get that these economically sensitive old economy stocks are good value here seems you know, you're better off somewhere else.

Nick: Exactly it. I think the portfolio is very well positioned for either outcome and we will see which which comes out Thank you very much indeed.

Thanks everyone. Bye. So what did we do last week? Well if as you saw we Moved our 520 calls up to 540. So we've put a lot of money away and we only have a 1. 2 percent risk to the whole portfolio by having these calls. And if we are exercised and we are currently above that strike price, these would be our allocations.

We took some profit, of course, in the XLK and put it into to work at SPY. That's probably the wrong move, but you know, we had so much money in it, I thought we'd take it. And finally, we sold all our TLT and we have instead SHI and IEI. So we are somewhere in the three to five year area in terms of duration, which we think is probably the most appropriate for now.

Naturally, the positions have updated everything, including the order entry. There are basically no limit orders for now. But what we would like to do, and we'll send you an email when that happens, when the market conditions allow, is buy some FEZ. calls or sell some puts we will see what is the most interesting thing to do at the time and we naturally will advise you but we wouldn't put more than five to ten percent of the portfolio in FEZ.

There should be a considerable bounce if things turn out well. On the other hand, if things turn out badly, it's gonna be very bad Indeed. So otherwise, the only thing really that makes any sense is to overwrite the SBY calls that we have at the five 50 to 5 55 strike level to June 29th. IE. the day before the French election, which is on the 30th, but we'll send you an email most probably Monday or Tuesday if the market rallies a little bit and we can get a reasonable price for those calls.

Otherwise, all the broker statements are updated as always, as is the monthly performance and all the weekly performance charts as well. Nothing more to say really about the positions, we are very happy, we have optionality, we have the duration we like, and we have a reasonably balanced portfolio. Not a lot that we really need to do now, those things that I mentioned in the order entry are really sort of How shall I put it?

They are cherries on the cake as it were. And finally just a quick word about what to have ready for the new 1 million dollar account which we will start in September. Now A lot of people have asked me about this and really what is indispensable is that you have a margin broker account, not a cash only type because that means that you can't sell at the same time as you buy something.

So, And that creates difficulties for you. So you can't swap USFR for TLT, for example, without leaving a day in between or whatever. And that is a difficulty. And not an IRA of any type because there are far too many restrictions for all the bells and whistles that we will introduce over time. And therefore an IRA account is just a waste of time and money for you.

So. The preferable add ons, but which are not indispensable because you can use other instruments. The preferable one really is a futures account because of the easier execution of the strategies that will be available to you. via futures. Now, I will always try to give you, for example, in SBX, let's say, you can do SBX options at one basis, or you can do futures options at another price, which is the same basis as the SBX.

I will try to explain it as much as possible, but really it would be much easier if you had a futures account and then you could just follow along in the futures. The risk is the same. The risk in futures is not higher. Then the risk in the SPX cash options. So that should not really be a worry for you at all.

And the other one, which I was not quite sure whether to put in the preferable or in the indispensable. is the ability to naked short options. And for that, you need certain permissions in your account, which you might not currently have. But I think you would definitely be worthwhile having it, because otherwise you are limiting yourself to many you know, Not being able to execute many strategies, not that it's going to make that much difference for you in percentage terms of return per year, but it's just a very annoying thing if you can't follow along and not a strategy.

And Simply because you don't have that permission in your account. Get that permission. It's very simple. It doesn't take that long. It might involve you taking a brief test. But on the other hand, if you don't know the answers to those questions, then you probably should not sell the product. Options naked.

And that is about it. We will definitely start in September. Can't promise it's going to be the first of September, but that is what I think you should have in order to make sure that the extra money you'll be paying for this is not a complete waste of money. Thank you very much indeed. Have a wonderful weekend.