Nick: Good morning. Today is Saturday the 21st of September and we've had the first cut of the year. It was a surprise 50. Surprise for us, but I guess not to a lot of people. So Andy, what'd you make of it? And what, what shall we do with a fed that's obviously going to be more dovish than we expected, even though the data is not really justifying the level of dovishness.

Andy: Yeah. I think it's important to note that the front end of the yield curve, which is the most sensitive. part of the, to the Fed. Obviously there was a very, the very, very front of the curve was, was had about a 70 percent chance of going 50 basis points. And so it adjusted a tiny, tiny amount, a few basis points, basically a few ticks.

The longer part of the short end of the yield curve didn't care at all. And so the short end of the yield curve has already been pricing a Fed that is expected to cut a lot. And so they told us they're going to cut a lot. So in that, in that way, there wasn't much news. For the markets to digest the dot plot.

And then the press conference and then subsequently the Waller interview on CNBC all suggested a Fed that is highly confident that inflation has been tackled. is highly con pretty highly confident, frankly, that the economy is okay. But, two things are important to note. Their, their reaction to weakening jobs data or, based on Waller's interview, further weakening in inflation below target is going to cause them to cut but they are data dependent.

So they're leaning to more cuts than they've shown data dependent. And so the market didn't really move because it had already priced a Fed that is that way, which is leaning toward more cuts than is currently On their dot plot and is already in pricing. And so what does that mean? It means that one, they may or may not be right about the economy.

And, you know, they're just like anybody else in terms of making those guesses. And two, they are pretty clear that they are going to significantly cut rates over the next 6 to 12 months. And what does that mean? Well, I think there's a school of thought that says the Fed is late to these cuts.

The economy is much worse than the Fed thinks. And that's bad. That means we're going into a recession. That means that equity should sell off. And bonds are a buy. That's not the school of thought we're in at all. We don't see that weakening data. And we, from the Fed's words and from the Fed's dot plots and from the Fed's Anything they say and from the actual hard data, there's nothing to be afraid of that.

We're about to go into a minute imminent recession my own personal opinion is We've been seeing market pricing in a significant easing in financial conditions since the inflation data in july And

that easing is working through the market and is now being supported by a Fed that's not going to stand in its way. And all of those things are supportive of the economy. And so in synthesis of that, that's better for stocks. I

Nick: think it's very fair to say that unless the data is strong going forward, they're going to cut 25 in November and in December.

If the data is weak, you can forget about 25s. They're going to do at least 50 in November. In both occasions, so you're looking at a fed funds rate, which at worst is going to be 425 unless the data is really, really strong and could actually be, you know, 375 by year end and certainly down towards the 3 percent area.

Sometime in 2025, whether it's early 2025 or late 2025, we can argue about that, but, you know, 100 basis points of cuts by the end of this year, if the data turns weak is certainly not out of the question. And therefore, that tells you that the short end of the curve. Is going to be okay ish and the long term, long part of the curve depends entirely on how strong the economy is.

And it's entirely possible that the long end backs up more than is priced in at the moment, but it's certainly not going to do that unless it's until it has seen NFP and most probably the next set of CPI numbers. So at the moment, we're in a period where period of uneasy stability, I would say there should be some switching out of long term bonds and into equities until we see some weak numbers and then the whole thing could unravel and completely change.

But for the time being, certainly we have a Fed put ie the the the equity market is expecting the fed to act very fast and very strongly on any kind of weak data, which protects the downside slightly in equities Of course if we go into recession You know, not much is going to be protected there, but that is the situation that we're in.

I really can't see a very much alternative to a situation in which equities have an uneasy stability all the way into the election. What do you think? I mean, I think the election is now going to be the bigger concern for the equity market rather than. The economy itself.

Andy: Yeah, I mean, I think we're both in agreement that the odds of a choppy market are high and the odds of a big move in one direction or another.

And by the way, that would be. bonds up stocks down or stocks up bonds down is pretty unlikely. In the next, you know, as you said, through the election you know, you only have one NFP and one inflation cycle before the next fed meeting, they get the NFP the day before while they're meeting and we have the election, but you know, October doesn't give a lot of grist.

It certainly doesn't give a, you know, What we mentioned is a surprisingly hot bit of data would obviously be bad for bonds and good for stocks and but it's not going to change the Fed. They're doing 25 for probably 2 to 4 meetings at least, probably more, and they could do 50 on weak data. So the strong data isn't going to cause the bond market to reverse until it's many, many.

months of strong data. And the weak data is going to cause the 50 basis points to be cut in both November and December. And so the question that one has to ask when they're thinking about equities, I agree that the, the most important takeaway is the Fed is ready and willing to ease. The question is, will they ease fast enough?

Will they need to ease faster? I guess is the question. And then will they ease faster? We already know the answer. Yes. So the Fed put will only work if the data is weak enough for them to cut, but not so weak that they can't cut enough spot on

Nick: spot on.

Andy: And to be honest, we have one data point.

Nick: That's all we can do now is go from data point to data point and then act accordingly after that data point.

Not much else that anyone can do. So what's going to happen next week to change what we've said? Not a lot because all we have is very few. Very few real economic data. We have some global PMIs and we have weekly claims again. What strikes me is that weekly claims just are not Weakening to the extent that would suggest that inflate that and rather a recession is imminent.

We now have a recession probability of nearly 50 percent according to certain models and weekly claims just aren't justifying that. So I think that to be afraid or to be very afraid of a recession at the moment is just wrong.

Andy: Yeah, I mean, I look at

GDP,

I look at retail sales as, you know, where we are, GDP is printing 3 percent for Q3 so far.

By the way, to clear out the next week's data, we'll also get PCE and we'll get the final second quarter GDP, which is obviously extremely stale. But we will get the PCE for Q3. August, which we know will be low because of what the CPI and PPI components have already told us. So that is not really market moving data, but it will happen.

But the point being that GDP is killing it. Fed's there to support the economy. Bond yields, mortgage rates, municipal bond financing, corporate bond financing, and equity levels are very attractive for financing growth or consumption. And the wallet of those who can spend, there's always a set of pop, the population that's struggling in every environment, but at the macro level, the wealth of the private sector is high.

And that's not what, and by the way, lastly, there's no credit problems on the horizon. Certainly no public private sector credit problems on the horizon. And so that all adds up to a very unlikely imminent recession.

Nick: I would agree. The only other thing that we haven't mentioned is that we have twos, fives and sevens for about 180 odd billion dollars.

And that is going to be the first test of how the market sees. The feds policy, and I reckon they're probably going to do quite well. I mean, the auctions are going to get bought. I really see no reason why anybody would start selling off the bond market to any great extent at the moment, apart from preparation for the auctions and then choppiness, choppiness into NFP next you know, in two weeks time, right?

Andy: Yeah. I mean, we're fairly conservatively priced. We'll have some.

You know, when I look at this, I say, you know, this is good for equities, bad for bonds. But are you going to chase equities here? We had a big rally on Thursday. And a little sell off on Friday. It was all part of the expiration week. And. It doesn't seem to me that there's an obvious rally of 5 percent or sell off of 5 percent that we need to think about.

So why chase?

Nick: Yeah. No, I think that we are in a period of uneasy stability until we see the next set of really important economic numbers. And that's all we can say and that's all we can do. Act accordingly. Absolutely. See you next week. See you next week.