Nick: And hello there today is the 28th of September quarter end coming up on Monday and let's see what we think about what happened last week Andy. I think that probably the biggest news was China and what China did to try and reflate its economy. First, do you think it's enough and do you think it really matters for the U.

S.? Here's the question.

Andy: Yeah, I mean, the way the way I think of China right now is it's a sort of long drawn out great financial crisis like ours in 2007 and 2008, where the economy got overlooked, significantly over levered, overbuilt many speculators and banks were heavily invested in real estate and it's the unwinding of that leverage has been depressionary, essentially, because There has been inadequate policymaker action, and, you know, it's been a dream of, of bulls on the Chinese economy to foreigners bulls for them to see.

Meaningful and there's been lots of jumps and starts on it to see meaningful policymaker action. And there was meaningful policymaker action that started with the the PBOC, the central bank who lowered interest rates, short term interest rates announced plans to lower both deposits for people who will have the money at the banks.

And mortgages, more importantly, by 50 basis points. And there were you know, sort of significant loan offerings to banks who would then package those and offer them to investors, both domestic and foreign to buy stocks. And, you know, those are, those are reasonable monetary easings when you have an economy that is not in the midst of a depression.

What's. What I think and what I think most think is what's required when you have a, you know, the classic Keynesian view would be what you need is monitor fiscal stimulus and the fiscal package came toward the end of the week and it was small it was, you know, this is an 18 trillion economy with a one point, you know, a 2 trillion problem in their, on their hands, you know, 8 to 10 percent of GDP sort of problem on their hands.

And you know, they did 2 percent of GDP in terms of announcements and the money will go largely to the middle class and the poor. And. It's inadequate for the economy to really rebound. But in situations like this, speculators shoot first and aim later. And the Chinese stock market had a huge rally.

You know, it's now outperforming the S and P this year.

Nick: Yes, you know, it, it absolutely had a huge rally. The question is, is that good for the U. S., for the U. S. market or not? And really the U. S. market is different from most other markets, isn't it? Because it's a very self contained market. What happens abroad tends to affect it least, both to the downside And as we saw last week, what did the S and P do where he was up less than half a percent?

So really, the S and P was not impressed by this and didn't think that this was going to reflate the world economy to any great extent. And neither did the price of oil, which actually ended down on the week again. So are we really does, does what China did change our view? In any way about what is happening in the US economy, and I guess from what you're saying and what I think the answer is No, as far as the US is concerned But it probably makes us slightly more bullish about international commodities Which we talk about Have started shifting into out of the US and into international commodities equities.

Sorry.

Andy: Yeah. I mean, I think that's right. You have the spec, the speculative pump of the Jack, the Chinese market next week, it's closed broadly though the U S ETFs will keep trading likely. So there could be continued sort of The last oomph of a 30 percent move but it's not something you would want to chase because it's unclear to us whether the economic impact is going to be enough to self sustain consumption in China, given their deleveraging.

So. You talk about the U. S. and the impact. It's probably going, if there is a big consumption boom in in, in China, their trade partners, their, their, in the place where they import stuff from are going to be the most impacted. So places like Europe and Japan would probably benefit well before the United States.

Demand for commodities, you know, Commodity demand is for institution is for industrial consumption and real estate consumption. Neither of those things are what are being targeted by the stimulus. So to us, it seems unlikely that you're going to see a meaningful impact on inflation. You're going to get some consumption, which is inflationary domestically.

But that's what their goal is. Exporting it to the rest of the world is unlikely. Maybe a little tick up in. Global growth.

Nick: Yeah. So what we're basically saying is that China has no big effect on the US and certainly the way they have structured this package, the totality of this package, it's probably going to benefit most, I don't know, Louis Vuitton.

And they're going to be buying, you know, sort of Louis Vuitton bags They're not really going to be buying anything else that is significant for the u. s and therefore the u. s market reacted least and Almost, you know sort of yawned at the at the china news, which is as it should be I think What else happened?

What do you think the pce was probably the most important thing that happened last week and You Nothing much came of that the the bond market yawned at the news that it was rounded down to 0. 1 as opposed to 0. 2 because we all know where the P. C. is going to be I just keep on having this feeling that inflation and especially after the data that we had in in Europe on Friday where inflation actually went negative month over month and is Headed to below the ECB target now, so we're probably going to get more ECB cuts and that was reflected in the local bond markets.

I just keep on getting the feeling that much the same thing could happen in the U. S. and that by the first half of next year. We could be at the fed's target and therefore what they have promised us the cuts they've promised us in the dot plots Are going to be realized and maybe even faster than they promised.

Do you agree with that view? Do you have a counter

Andy: view to that? So I I so it's a question of term and how quickly all this happens I do disagree I think the economy is so you didn't mention the jobless claims that was

Nick: Yeah, they, they're always fine though. Every week we look for weaker jobless claims.

And every week they are exactly in line

Andy: Right, which to me represents an economy that is and I think you agree and I think we've been saying this absolutely no sign of weakness No, so the the point on it on inflation to me is I don't know what inflation is going to do I think the economy is fine and the fed is cutting into a strong economy and that generally is is inflationary and gold is taking that message in a big way.

Stocks even are taking that message in a fairly big way. The bond market is being held down by expectations of cuts. And I don't disagree with you that if we start to see disinflation, further disinflationary numbers from what we are seeing, that the cuts that are priced in will be realized, but it's, and I think it's important to note that since the.

Since Jackson Hole basically, but certainly since the FOMC meeting, pretty much every governor except Bowman has been speaking from the same hymn book, and that's that they're on a path, they're data dependent, and that data, and their bigger concern is the jobs market. However, which to me is not, shouldn't be their concern, and shouldn't be why they're cutting because the economy is strong.

And there's no sign of weakness in the job market, but they've mentioned that only Waller most recently was concerned about disinflation like you are and That tells me that Any hot inflation, inflation number, and we're bound to get one that's above expectation. You know, these numbers shift around, they're unpredictable is going to be ignored.

And any cold number is going to be supported. So it's going to take a number of hot inflation numbers to to turn the sentiment and the market pricing around regarding inflation. And it's hard to think that that's going to happen really soon. I would say that one interesting point is that spot oil is about to drop below forward oil, which is a Inflationary signal, it means oil prices are, instead of what it has been for a number of years as the economy has weakened, spot oil has been above forward oil, which signals disinflation because the market expects oil to be lower in the future.

That's shifting. I don't know when it'll turn, but with an economy that is strong with the cuts that are priced in already affecting every market that borrows and lends and with a very dovish Fed, I, I'm, I'm more six months out optimistic about the economy and unfortunately optimistic about inflation, not accelerating, but not coming down to target.

Nick: I get where you're coming from. I think that this is precisely the wrong time to be adding risk, simply because there are so many unknowns and unknowables. First of all, the most important one being the election, because monetary policy, potentially, and fiscal policy, certainly, are going to be very different.

You know, if one candidate wins over another and we will discuss that much closer to the to the election. No point in doing that Now, I just know that from experience, from bitter experience most of the time is that when the market like

US equities finds itself at a point where it has very limited upside, it tends to probe the downside.

And I think that all the people who bought equities last week and the week before on some Chinese news Or you know the strong economy or whatever news are going to regret it in the next few weeks before the election You know, we we what do we see on friday? We saw that volatility rose for absolutely no reason at all and that's another sign so i'm I am really very cautious here about all markets whether they be bond markets or Whether they be stock markets, I think that we are priced for perfection in both markets And we are unlikely to get perfection because perfection doesn't exist as we all know So what can happen next week to derail this wonderful?

Everything is going up rally inequities and bonds. Well, we have NFP of course, but right. So months.

Andy: So in terms of what's coming Monday, we're going to have month end and it's slightly bullish bonds in terms of just inflows and duration extension that happens pretty much every month. Bonds have also underperformed.

So bonds are likely to be bought. An equity sold for rebalance pressures, but there's some fairly technical things, which I won't go into in this video regarding a very large options trade that expires on the close. So it's very unpredictable. We could either rally a lot or sell off a lot on. So, you know, we'll communicate if either of those two things happen.

But the market, as Nick said, is is a little skittish regarding the next month. And again, I agree completely. This is not the time to be committing new money to any asset market, given the Uncertainty and what the market is telling you is that they are uncertain. So the rest of the week, you know, is going to be secondary jobs, data, some other secondary data, and then the big.

NFP data, and that's going to be a focus of the Fed and has been a focus of most of the governors, except as I mentioned, Waller, about seeing any weakness in the job market. Consensus is about 1. 140, 000 jobs, 160, 000 jobs, and the unemployment rate is not expected to change. What do you think happens next week?

Nick: I think if NFP is hot, let's say, let's say 175 plus, the bond market will probably let's see, it'll bear, bear flatten, i. e. the two year note will suffer by 15 basis points or something like that. It's very unlikely that the market prices in less than the two cuts that would be promised by the Fed for 2024.

That's almost an impossibility and it'll always keep a little bit of a cushion just in case they go 50. I think one month worth of data is not going to be enough to change anyone's mind about the the employment situation. It's going to need several months of strong numbers for people's opinion to change.

The market would react much more to cold data, say 100, 110 or even lower if the number is lower than 100, I expect the market to price in immediately to 50 basis points cuts for 2024. Which basically means that's another 20 to 25 basis points on the, at the very short end, about 20. So there's more room for rallies than there is for, for falls.

And in case of a cold number, then the market would bull steepen. So the short end would go go up in price more than the long end. And that tends to be true. Supportive of equities, but in any case, it would be a bonds over equities kind of move because equities are very, very fully priced. And you could get a I wouldn't sell that.

I wouldn't say that they're going to sell them very hard, but they're certainly going to sell them by a percent or so, certainly relative to bonds, because it, it, it just gives you that little bit of extra pricing in bonds that you have to price in a little bit of odds of a recession. Now, I don't think that we're going to have a recession.

I think that's Completely the wrong thing to to think about, but I think at the moment very Very small odds of a recession are being priced in the bond market It's more of an inflation story rather than a recession story So bonds will do better than equities. I believe on a Very cold number and the colder the more bonds rally and that tends to support equities But certainly I don't think that they'll be going up in that scenario.

They'll be unchanged to down

Andy: Yeah, it's interesting. You know, our view on the economy is heading toward, you know, we have slightly different views on how we get there, but heading toward target on inflation and strong growth that favors equities over bonds. But at the same time, both Nick and I are at the, of the belief that we have this great uncertainty in the next month.

Volatility is very high, which indicates markets are uncertain, and there's limited upside to equities given its pricing. So for me, the point on the employment number is that what Nick described as a bull steepener in a cold number and a bear steepener in a hot number, the transmission bear flattener, sorry, the transmission mechanism to equities is one of equities pricing on their multiple.

Because a cold number, if it's extrapolated to a recession, is bad for earnings, but a cold number, if it's not extrapolated to earnings, that earnings are fine, but allows the Fed to cut more than they want, is supportive of equities. And so, I think equities are priced here, mostly resting on the rate cuts, and not resting on economic strength.

Thank you. So, I would think, for that reason, bull steepener is supportive of equities, bear, bear flattener is bearish equities, and that the economic, the earnings pass through of those numbers, which are contra to those things are going to be ignored. And so I agree you might get a little but basically the point being that on a hot number It's stocks over bonds in a cold number.

It's bonds over stocks But at current pricing neither of those things are attractive enough to add risk

Nick: on as we said in the beginning, you know Precisely the wrong time to be adding much risk to your portfolio. Great Thank you very much indeed and speak to you next week. See you next week nick