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Nick: Hello. Good morning, and today is the 3rd of May already. We had a very interesting week. A lot of things that we didn't think would happen did happen, but the one thing that is the overarching theme, and I think that we are correct in, is that if there is going to be weakness in the data, it's going to come.

After the, in the second half of this month and sometime in at the beginning of June. So that is the timeframe that we are looking at, simply because all the data that we've getting been getting so far, and we are talking about employment, including the NFP, is all data that pertains to. The month of March or the first part of April, and what does it tell us?

It tells us that employers are not adding jobs, which is perfectly normal because in a period of uncertainty, the first thing you do is you scale back on adding new jobs, but you wait until you get much more solid. Indications of what is ahead before you continue hiring or firing. And what we are not seeing is the firing as yet.

We could see that, but only as I've said in the second part of this month. Otherwise, what did we have? Of data last week that we found slightly surprising. Well, the negative GDP print was slightly surprising, but it was mostly technical factors. IE consumption was solid and all the bits that matter for the stock market were pretty solid.

W one can't say that one can see anything but a technical recession coming out of the GDP data. The BOJ was actually pretty dubbish in its deliberations, which was slightly surprising because market participants thought the BOJ would be slightly more hawkish, and that actually leads us into what the FMC will do next week.

We think it'll probably be as hawkish as dovish as the BOJ. But one more important factor that we got on Friday that got very little press or discussion so far is Trump's budget proposal for 2025, and that was far more. Fiscally conservative than was predicted IE. What he wants to do is he wants to increase substantially the defense spending, but at the expense of a lot of other discretionary items.

So, which would result in what will probably be the. One of the highest fiscal retrain retrenchments in modern political history. So that budget is probably dead on arrival, but it gives us their intention what Trump 2.0 wishes to achieve.

What do you think, Andy? What does Trump 2.0 wish to achieve with these budget proposals, which are pretty damn draconian?

Andy: Yeah. Yeah, I mean I think that the funny thing, and I think markets are expecting a Trump 1.0, which is one in which tariffs are actually a lot smaller. But there are some, the fiscal side is doesn't really do any cuts and taxes are cut on the, and so the deficit rises and borders are secure.

That's standard. So Trump 2.0 is one in which borders are secured and global trade is reshaped through tariffs which are sizable. And as it relates to the budget news that we got on Friday that the Trump administration through its elimination of.

Muscle and bone of the US government shrinks the footprint of the US government in a meaningful way except for the things that they're, they have a priority on. For instance, the budget had a 65% increase in Homeland Security, total Trump 2.0. And so I. Shrinking the expenditure side is the big difference between Trump 2.0 and Trump 1.0.

And they didn't pivot at all. In fact, they were quite strong on their shrinking the size of the government. It's not gonna pass, and there's gonna have, there's gonna be implications of that, which we'll talk about at another time. Probably leaning toward raising taxes on the most unpopular.

Populist entity, which is the wealthy, but we'll come to that at another, in another ti at another time. This is gonna be a multi-month negotiation reconciliation, which itself is a shrinking of the government expenditures. They hope to have by July 4th. And yet there's no sign that will pass yet.

So a lot of this is in the sausage making and there's not gonna be any real news on it, but it is important that they released a budget that was, meaningfully different than Trump 1.0 and very consistent with everything the president has told us for months. One last point that I think is important in that context.

The Saudis last week were made a statement, which you can take it for what it is that they could survive very low oil prices for a very long time. Oil sold off on that. And. Y. Putting that in context of the Trump administration's policies as expressed by Secretary Besant. They want deficit reduction.

So that's the expenditure cut bit and they want real growth. We haven't heard much about that because that's been dr. That's drive being driven by, deregulation, which we have yet to see a lot of details on, but it's also driven by the third leg, which is if you make oil prices low enough, people can spend their money, both industrial and consumption on things other than oil and the last.

And so that's good for real growth. And then the last thing in the bessant 3, 3, 3 plan is. Lowering oil prices and it seems perhaps, and Trump is heading toward the Mideast to meet with the Saudis and others in the weeks to come. It seems that the opec, we'll talk about Russia maybe, I don't know, but at least the Saudis are talking oil down and that was a surprise to me and is.

Not a surprise. It was part of the plan, but the timing of it was impactful on the market and is a supporter of the entire Trump agenda. And so what you have to look at is what does that all mean? Well, expenditures are coming down. That's bad for real growth. Deregulation has yet to happen. That's good for real growth when it happens.

Immigration is. Very active, and that's bad for real growth and tariffs are all sorts of happy talks since the Trump administration paused and extended the deadline for tariff implementation by 90 days, and the Happy Talk continued this week with rumors of China being willing to come to the table.

Those I think are, should be heavily discounted until we actually see something. But all the other deals looking good from the administration, not really. The rest of the world didn't really support that. They're looking good, but they're at least talking. So leading into next week, we have the FOMC meeting.

We have a series of auctions. We have some data, but not the primary data, and we have expectations of. Tariff deals and I think that's the lead in to next week. What do you think happens next week?

Nick: Well, as far as the FOMC, I think that's an easy call. They're gonna do nothing, and they are probably going to be slightly more dovish than the market expects.

Simply because there is no mileage in being hawkish. The worst thing that could possibly happen to the Fed is that they are hawkish, and two weeks later, the data completely negates them and makes them look like fools. So that is not something that. Powell is very good at IE. He's not very good at being hawkish in his presses, in any case, even when he should be.

And, but what he won't do is take the chance that he is made an absolute fool by the data only two weeks after an FOMC meeting. And in any case, we all know that when employment starts going. Because employment is in the rear view mirror, as it were. The fed is automatically behind the curve and he knows that.

So why would he take the chance and be hawkish when you know everyone is telling him that the possibility of weaker data is actually in the second half of May or the first half. Of June. He won't do that. And therefore I think the markets, the bond markets are going to be supported throughout the first part of next week.

We came off on Friday because of the auctions. We have the threes, tens, and the thirties. But I think from Wednesday on, we start rallying. Into the FOMC and outta the FOMC. Very unlikely that he is anything but neutral to the dovish side. I just can't see why he can take the chance

Andy: of that. The one thing that I would say on that is, what does dovish mean?

It means cautious. It doesn't mean, hey, we're cutting in, we're starting a cutting cycle in June. I don't think he can bring the committee with him to that point though. There are certainly close to half that are doves, but why also ease into that when you can just say we are concerned or cautious.

So I think it's a very narrow spectrum of dovish to neutral. We're not talking about. Super dovish and we're not, and we're certainly not talking about a hawkish outcome somewhere in that narrow range of data. But we are a little concerned versus, Hey Jo, June is a live meeting that we're really want you to start pricing in.

And frankly I agree completely on the back end of the curve pricing down against, auctions coming, but the front end of the curve really reversed in a major way last week. At one point last week, early in. I think it was Thursday. There were over 110 basis points of cuts priced in for for 2025.

And now they're only 70 ish, five ish, priced in for 2025. So that's a big reversal. An entire rate cut, 25 basis point rate cut got taken out within. 24 hours of Thursday through Friday's close. We're leading into A-F-O-M-C meeting in which the Fed is likely to lean, is neutral to dovish, and yet pricing in the front end of the curve is as hawkish as it's been in a while.

So, there might be an opportunity short term to be long, short dated stuff, but that's not really why we're here at two Gray Beards. What I would be concerned about. Is an outcome. So again, I real Nick and I both really discount any hawkish outcome, but an overly dovish outcome would concern me.

Because that would, to me be a good for equities bad, but very bad for the long end. To front run to say essentially that the tariff related inflation is either not going to happen because deals get done. Or is going to happen, and we're gonna completely look through that and cut aggressively would be bad to me for the long end of the bond market and very good for the front.

But we'll see. We don't expect that sort of deviation.

Nick: No the odds of that happening are, again, so slight. It's not worth considering really. The, there is absolutely no upside in him doing that because he has another meeting in June, so in four weeks he'll be able to correct anything. He gets wrong now, so why stick his neck out?

He'll have all the data. He actually needs to make a decision in June and move in June if necessary. So absolutely no need for him to stick his neck out. I completely agree. Maybe we should have a few words about this big rally with Ed inequities, because I certainly didn't expect it to go this far.

And what is the market discounting and where would we be wrong or why would we be wrong? In being so, I would say conservative and stroke concerned about the valuation of the start market. What would you say, Andy?

Andy: Well, you look at the pricing first. The pricing is now 22 pe on relatively strong expected future earnings.

The earnings themselves. Last week, which we got a lot of Microsoft and Meta were, who are pretty immune to tariffs showed their strong, their resilience and those stocks drove most of the rally this week. Apple and Amazon who are. In the crosshairs of tariffs reported poorly and a apple at least sold off a fair amount.

And so I think it's mixed. It's not atypical that this sort of thing happens during earning seasons as you get this sort of dispersion leading to an overall equity rally. And so the question is it unusual? To get this, it's it surprised me. I started shorting for my alpha account lower and continue to short a little bit more, a little bit more.

But I don't see a lot of upside for equities. What, how would we be wrong? AI would be even stronger than expected. Nvidia shows great strength in its earnings and, AI takes off. The Trump administration announces some unexpected, extremely optimistic deregulation that would be make us wrong.

The Trump administration does reverses its tariff policy and accepts very modest. Deals on tariffs to versus what they had in mind. Meaning drops the 10% across the board, tariffs drops significantly. Any a adversarial relationship with China? I think the happy Talk is pretty strong on those sort of things.

So maybe not much wrong if something like that happened. And then of course I now given the terror, given what is. Being reconciled within the mandatory expenditures and being the entire administration, every cabinet member signed off on this budget and you know that's a bureaucracy that's gonna be pushing for that budget for many months.

I don't see any reversal coming on the government, the fiscal side. I guess the last thing is Powell could be, as we said, very unlikely, but Powell could be very dovish and those are the types of things that I would look for to say, Hey, we got this wrong. But does that mean I chase probably not at 22 forward PE and 10% earnings growth?

Probably not.

Nick: Yeah. No I agree with you. Everything you've said is absolutely right. And the idea that one should chase when the macro is actually so strongly against these levels. It just, it's is repugnant to me. So, the best one can do is say, okay, the next couple of weeks before the data has a chance to really hit this market.

We are unlikely to go down too far, but you never know. And that's the thing where we got outta the market or we hedged far too soon. But that does not mean that we are wrong. I've never seen a a market we just bottoms and never retests. Certainly the only one that I can think of is Covid, but that's a completely different story.

For the market to keep on going here, I think Trump would have to give up most of his policies, and I really don't see that he is in any mood to do that or has any reason to do that. Why would he drop the tariffs? They're the central plank. His policy, particularly now, why would he do, why the

Andy: equity markets are so strong?

Nick: Correct. So the stronger the equity market is, the more he's actually emboldened to play, to, to play as tough as possible in the negotiations and get the best possible deal of what he or what he considers the highest possible deal. From the tariffs and the highest possible revenue from them. Yeah. It just doesn't make any sense that he would drop his policies now.

Andy: Right. I guess the two things that come to mind in terms of looking at the last six, the four months, the year to date, performance of any investment, if you didn't own gold, your returns are basically like cash. There's, sure. If you. Entered the year in cash and you bought the lows, and then you rode the lows to where you are.

You've done great. But that's alpha. If you entered the year in cash in s and p in bonds, in anything but gold today, you look at your statement, it would've all been the same. You wouldn't have had the same as cash. What do you do today? Well, I guess you have to look on whether you own enough gold.

Thankfully. Our original subscribers have owned gold for a long time, and we've been hesitant to get our new subscribers that are using leverage into gold at these prices. But bottom line, if you didn't have gold, you missed it. And so when you look at your portfolio with gold here. Ca, you're basically where you were year end, and you say, where do you want to be allocated?

I still struggle with adding gold here. I don't have a desire to be long. A lot of assets relative to cash, given what cash is paying, and I favor bonds over equities.

Nick: Yep. Can't disagree. I I certainly favor the the middle part of the curve. The five sevens area, three five sevens over the twos, all the tens and thirties.

I I still dislike. Duration the high duration I am afraid of, I, I just can't invest in it. But if things really do change and the economy starts getting really hit in, in, let's call it June time, then duration will certainly perform very well and much, much better than equities. But we'll see that in the data, and then we'll act accordingly.

Andy: We've One last thing we've also talked about and believe that there are secular flows out of US assets, which are massively over owned by everyone. To the rest of the world. Developed markets, em isn't my thing, but developed markets and that will weaken the dollar. There's been a re retrace of that, but the secular change is extremely important and an ongoing headwind to US dollar strength and US asset on outperformance and that.

Whether it's a temporary retracement is what our expectation. I don't see that changing.

Nick: No, I'm, I would agree with you and that's certainly something that our portfolio reflects because we do have quite a high allocation in what we have to international equities, and they're doing much, much better than US equities.

And that some of it is attributable to the weakness of the dollar, but even if you don't take the dollar into account, they are certainly outperforming the US equity performance, however good it might have been for the last one or two weeks. Right. Thank you very much Andy. I'll speak to you next week and if there's anything that we need to do after the FOMC because we got our expectation wrong, we'll send you an update straight away.

Thanks everyone. Bye.