

## 2 Gray Beards Week 171

**Nick:** Hello and good morning everyone. Today is the 11th of April. Let me try and summarize what I think is going on and then Andy, maybe you can criticize my thought process and tell us what you think is happening. First of all, I don't think that the conflict in Iran is anywhere near over, but what has happened in the past week is that people got excessively short, and then we had the ceasefire and the CTAs had to chase.

The bond market is now, I dunno, something like 15 basis points in real, yields lower than it was at its worst, and that enable equities to rally some, but also we have earnings coming up and we all know that those are going to be. Absolutely excellent, and that prompted a huge amount of short covering in equities, not so much in bonds, and I've been expecting equities through outperform bonds all week, and they did.

What happens next in my view is that we have a second round of failed negotiations with Iran. And that basically means that we are not going to make new highs in equities, but who the hell knows we could get a possible deal. I doubt it very much, and here we have to play the odds. I think the odds of a deal are no higher than 20%, but if we do get a deal, we will probably have a further leg higher.

But even that leg higher, I think fails eventually simply because bond yields are not high enough to get the, to get us to buy them, and while they continue to go higher over time, I think equities are going to be facing a very strong headwind and they're not going to be able to maintain whatever level they get to.

I think they're topping at the moment. They could easily go higher, but I think that the prudent thing to do is to remain hedged. And wait for the second leg lower because those are the higher odds. What do you think, Andy? How? How is my thinking? Possibly wrong.

**Andy:** Yeah. So, I mean, markets fluctuate. I think the, the most important thing about whether you're right or wrong is markets move up and down, you know, that's the game.

But you know, my, the way my takeaway for what's happened is, you know, two weeks ago last. On the 28th, I was absolutely pounding the table that we

were gonna have a sell off on Monday that was mechanically associated with significant negative gamma in the market, and that we were gonna have a very, uh.

Sharp rally through Tuesday which has extended on, which is exactly what happened, and saying I was nothing but a buyer. Now, that was at 6,300 on the SPX, that was at two year yields that were up over 4%. That was with 30 year yields that were, as Nick rightly said. Real yields at their local peak. So it was easy to buy assets into that sort of mechanical selling and then let it rally.

So we rallied. We rallied a little bit farther than I expected, which is totally typical in these big negative gamma situations, and we found ourselves towards 6550, 6600 on the S and P.

And then we got resolution. No, we didn't get resolution. We got the announcement of a potential ceasefire that is a potential beginnings to a lasting deal, and the market gapped what? Little over 2%, 2.4%. And then has flatlined since. So for me, I have to just look at, so that's what happened. We're up 500 points from when I was pounding the table to buy.

Am I pounding the table to buy right now? Absolutely not. Like no cr, that'd be crazy. Nothing has really actually happened at all, right? Nothing. So now. Up 500 points. Am I a aggressive seller? Yeah. I'm starting to sell a little bit and, and buy some puts in my alpha account on equities. Bonds really haven't done much though, you know, they did come off their, they, they've rallied a little bit.

The auctions were pretty good. The central banks sort of priced in some hot, some significant amount of hikings, particularly in the UK during all this episode, but have sort of come back down to what looks like mostly a pausing policy. But for me, stepping back and saying what's different about the market, the big difference is persistently high.

Oil prices expected for the next year, not persistently low oil prices, persistently high oil prices. And listen, I'm not an expert on what's happening in the Gulf by any means whatsoever. I'm just looking at markets and trying to logic through all this. It seems like there's going to be tight supply for a period of time, even in the most optimistic of peace outcomes.

And as long as oil remains significantly elevated for this, for 2026 you see inflation is printing high. If that doesn't really matter so much, what matters is me and you and the world are spending an extra 101% of GDP just on energy. That we can't spend on everything else, and that is a significant negative growth

hit that is not gonna be resolved with a ceasefire and probably isn't gonna be resolved even with the most optimistic peace outcomes.

So that said. The more peace outcomes happen, the more likely asset markets stay elevated. But to what end? The conditions for growth, the conditions for employment, the conditions for central bank easing, the conditions for now with add on a persistent, persistently elevated energy price. Yeah. Just make my thesis of why I didn't wanna be long.

A lot of equities up here a month ago, even stronger. So I think it's very simple that you should be looking to, to lighten up equities and. If bonds offer a significant real yield, and we've given you levels on that, begin to extend what is relatively short duration, interest rate exposure to longer dated interest rate exposure, and that's sort of where I fit.

**Nick:** Yeah, so really we haven't moved our position at all as a result of price movements this week. We are just saying the same thing, but at different levels. That's all. Yeah. Is there anything, is there anything else that we. Need to look for forward to next week. That could change our mind. Apart from the negotiations outcomes

**Andy:** we're gonna get negotiations uh, just my own point of view on that.

I think the sides are extremely far apart and at the same time, if they want to get, get, say they made a deal, they'll say they made a deal. But do I think that that ends the. Controversy in the Middle East for that's been ongoing for 47 years. Absolutely not. Do I think it even ends the controversy for the next month?

Probably not. So I'm not particularly optimistic. On the other hand, I hope we get some really great news coming from the. Negotiations. For one, I like great news and pieces good for another. It lets me sell the crap out of the market into any rally associated with that, which is what I will be doing.

**Nick:** Okay, so we've got that. Let's talk about economic data, which we keep on telling you is very unreliable. We had CPI, it was slightly better than the worst outcome that could have been. But does that mean anything for us? Do we change our mind in any way? We have PPI next week, and that will let us calculate PCE with a 99% accuracy kind of thing.

We have home sales, but otherwise we are data light. Is there anything that's gonna come out next week that's gonna change our mind apart from the peace negotiations, data wise? I don't think so. Right.

**Andy:** So data has been, to me, a trying to extrapolate market moves based on the last four to six months of data has been a fool's errand.

A combination of tariffs on, tariffs off, um, the war, general lack of, of the, the closure of the government for an extended period of time. Ha has all led to significant. Turmoil and the data, which already has, which already is not something I spend a lot of time extrapolating my market view from to begin with.

Right now it's even more so, and now you have this, you know, this oil impact. So yeah, I don't think you're gonna get much from the data. The CPI, to me was somewhat reassuring if you think the Fed needs to cut. Um, but also the headline was just a joke, but that's just oil. So when I look at next week's data, no, I don't see anything that's gonna change our outlook.

What I think you have to do is think about what would change your outlook. And so there are big things coming. The big things that are coming are. AI and whether it'll generate ROI the Fed what the war plan will be. Will they ease into inflation? That's what Trump wants. Fiscal Can Trump do anything on the fiscal standpoint issuance?

Who's gonna be issuing what? Those are the big things that are on the runway, not what the CPI number is gonna be. And so those are the things that I'm looking for. And yes, I could change my mind if I saw an environment where the tr, the Fed, the treasury and the administration all get very easy.

It'll destroy the dollar, making the bull case really to be, in other currencies, equity markets. But, and will probably cause a steepening in the yield curve, but for equities. Yeah. I, I could imagine getting super long equities if, a bunch of unexpected policy decisions are made.

**Nick:** Like what? Like the QRA, is that what you're talking about?

That's coming end of

**Andy:** this month. We're marked. We have, you know, we have these budget stuff. We, we didn't talk about this. We had \$1.5 trillion of military spending proposed for in the most recent budget release. We had \$200 million of immediate budget support for the military that was proposed and then withdrawn on Friday.

You know, there's lots of fiscal stuff that's going. The sim and tariffs have yet to, could run off completely in July unless reengaged and to reengage tariffs, you're gonna see a lot of policy decisions that have to come out if they don't reengage tariffs. The deficit is blowing out. You know, we, they depend on \$300 billion of tariff revenue that SCOTUS has kicked to the curb and shrunk dramatically that needs to be replaced.

Or we have three, or we have a hundred basis points of deficit to GDP increase. Just because of tariffs. So the tariffs have to come. If they don't come, you've got this massive deficit. That would be a big deal. But the deficit, because it's growing and because. The budget, the, like the, the proposed budget is big.

If it could pass, which you may not be able to, is gonna demand more issuance from treasury this quarter, and we'll find out about that in early May. And when we find out, we'll find out whether they're gonna start demanding investors increase auction size on long dated coupon treasuries, which will expand risk premiums, et cetera.

We've talked about this. Endlessly, we'll find

**Nick:** out. And that will be very negative equities.

**Andy:** It could, it's negative assets and yeah, it could be negative e equity though, if they do it with massive deficits, that's less negative equities and more negative bonds. So

**Nick:** there's lots, it's going to be negative US equities relative to the rest of the worlds.

**Andy:** Sure. Absolutely. So yeah, I mean I think that's this war has been nice and interesting and you know, I don't know what we achieved. Maybe we achieved something. We'll see, we don't know. We traded the market. Okay. During that war. Maybe it's over. Probably not, but let's see. But the big picture. Is what's fiscal doing?

What's monetary doing? What are the pricing? What's the pricing of assets? And whether will AI deliver on its promises? And with those big things, to me, there's a lot of headwinds coming that by the could be tailwinds depending on what the policymakers decide, of course. But we're looking at those and those start coming in early May.

**Nick:** Really, you would've thought that they will try to do absolutely everything they can to help the market going into the midterms.

**Andy:** Yeah. Which is interesting. You've thought, interesting. If, if, if, if Besson wants to save the 10 year, the only way to save the 10 year is to not sell any. That's also happens to save equities, but it crushes the dollar.

So he can't save the one thing, so they wanna save the midterms? Maybe, maybe not. I don't know. Maybe they've given up. Maybe they think they've got it. I don't know. But if your view is that they're trying to save the midterms, it's really pretty straightforward.

**Nick:** Sell

**Andy:** the dollar. If you wanna save stock and bonds, sell the dollar and buy gold.

'cause those are your only choices. You can't save both the stock and the bond market. And you can't save the stock market without saving the bond market. To do that, you have to crush the dollar and that's the only choice. So to me, being short dollars, being in rest of world equities is a much better way of owning equities, but we'll see.

**Nick:** Understood. Right. Let me go through my bit and see where we are with the portfolio and we are going to basically sit out now until early May. When we get the information that we need to make our big moves. Thank you, Andy. See you next week.

**Andy:** See you next week, Nick.