2 Gray Beards Week 172

Nick: Hello, and today is the 18th of April Now. Incredible week. Last week, Andy, wasn't it a, a squeeze of such major proportions that I haven't seen that in ages, not since the nineties really, of that kind of, uh, percentage move. So what can we say? What is the current state of play? The economic numbers are just flatlining.

There is absolutely no change in the economy. It's neither accelerating nor decelerating. Unemployment numbers are flat, completely flat, which is. Incredible in itself, the PPI was very, very slightly better than the worst expectations, but it's hardly good news that prices are only going up as opposed to skyrocketing up.

PCE, we have PPI, we have CPI. So we know what it's going to be. It's not going to be brilliant and it's not going to be horrific. The data continues to be a very low quality though, doesn't it? And it doesn't really tell us very much about what is going to happen in the future. If we completely disregard this major, major squeeze that happened and we can, you know, so we can address later why we think it happened.

But no one knows really what should our portfolio look like. Really, we have to disregard all these stupid. Headlines about what is going on in the Gulf and what is not going on on in the Gulf. I've said many times what I think is going on in the Gulf, and that is that no one is really running Iran.

You have factions which are battling, and one faction is coming out with one narrative, and the other faction is coming up. Out with the opposite narrative. But before that is absolutely concluded. We dunno which faction is going to win and therefore we don't know what's going to happen. The straight of ous fact is still blocked and ships are still not going through it.

While this persists, what should our portfolio look like and. What can we, I mean, when should we change it? Yeah. What is going to be our trigger? And I don't think our trigger to change it is going to be until the next two or three weeks. The facts that emerge from those two or three weeks come out?

Andy: Yeah, I mean, I think we have to start with what would you, you don't know anything.

You just know what's currently in the market, what the prices are, what the economic conditions are, and this high level of uncertainty. What would your portfolio look like? And for me, it's very simple. I would want less risk than I norm. You know, we, we all tweak what we think the right portfolio is, and we're certainly pro, we provide our consensus, right?

Portfolio, and I provide my own portfolio and Nick has his own portfolio and, you know, we all save in different ways and most of them are okay. Like the big, the big differences are not that big. The high level thing I, I think right now for portfolios is that prices really matter, but at current prices, I want less risk oh, that means I want more cash.

So let's, let's just start with there, and then there's a question of what do I want? And for me, three weeks ago, I wanted many, much more stock. Now I want much less stock. I still want less US assets than I've ha wanted for years and years and years. And I want more rest of world assets. I want more industrial assets than I normally do.

I want more military assets than I normally do in terms of stocks. But I mostly want less risk and less stocks. Then it comes to bonds and you know, I personally, from what I do, own more bonds than what two G GB owns because I like the anti-growth nature of bonds. But it does ha what you own in bonds for the last multiple years hasn't mattered at all.

It's just never mattered. You know, they never go up a lot and they never go down a lot. And so what that means is bonds and cash have been acting like the same thing for many years. And so any diversification I've been, I've, I've had relative to two gray beards portfolio has been essentially non-existent.

In

Nick: terms of performance?

Andy: Yeah, in terms of performance, like it's just cash. Like cash is fine. So you know, for two gray beards, we don't own any bonds and so that makes me wor, the only thing that makes me worried about is there's gonna be a time to own bonds and you don't wanna own stocks when you own bonds, if we were ever to like get in a position, and this was exactly what we were talking about in March, we never got, we got to a level where I cared on stocks, but we never got to a level where we both care on bonds. There's gonna be a time to buy both stocks and bonds in size, but bonds just don't offer that right now.

So then the question is, okay, so I want to own stocks. Well, I don't right now, but if I did want to own stocks, do I have to own bonds as a hedge? At the right price. I really wanna own bonds as a hedge. But today what's important is bonds don't offer attractive real yields relative to what our target is.

Meh. Stocks have massively rallied and are pricing in 17% earnings growth and 23 per and 23 times multiple. That means I don't wanna own as much of them and there's great uncertainty. So I don't want, I wanna own more cash. And so when I look at our portfolio today, I think it's about right.

Nick: And what more can we say about, how we should change the portfolio and when we should change the portfolio.

Andy: So I think that's gets to some, you know, we had a disagreement. I wanted, I was pounding the table. We had to be a buyer. We ended up selling you for you. By the way. I think we should just frame this. Nick owns Nick's a guy who has a variety of investment accounts.

He has two accounts that we trade in two gray beards. They're his accounts. He is, he's ultimately the decider. I give him my input, he decides totally good, happy with that relationship, that's, that works the. Point being that those two accounts have different purposes. One is mostly a very conservative, two, two gray beards, original, very conservative wealth management product with low risk and low leverage.

And the other is much more of an alpha product in which we are taking levered bets, which sometimes don't work out. And this one, for instance, what we disagreed. Nick decided it didn't work out. That happens. It happens all the time. It happens to me all the time. It happens to Nick all the time. It's gonna happen to you all the time.

Let's move on. Now we look at our existing portfolios. The two gray beards squared portfolio is pretty low equity exposure, so we need a plan for that. The um. Even relative to both Nick and I's View, it's pretty low equity. The two gray beards original portfolio is about where Nick and I think equity should be.

Our equity exposure should be, so the not much needs to be done there. So now what's the plan, Nick? What do you think we should be doing to get our portfolios to the place where we want them?

Nick: It's, uh, it's, it's a very tough one. I think the, uh, I think this whole year is going to be a year of up, down, up, down, and really very muted.

Long term return be returns. So I don't expect equities to offer more than very low single digits in terms of returns for the whole year. I think that that means that you have to diversify away from the indices and go into sectors, and I think that you have to actively trade at levels. Now, regardless of where one Hedges, one has to recognize that at this kind of level, and as you rightly said, prices really do matter.

You are reflecting more than, that is possible earnings growth of, you know, in the high double digits with a multiplier of 23. When real, I mean when real rates are 2.6, 2.7, and I think they, there's every chance that they get worse. Is unrealistic, and if it's unrealistic, you don't chase you. You wait for the thing to come back.

Now how do you wait for the thing to come back is something that we can discuss. But overall. When I look at everything that I own, apart from the two GB portfolios, I am now at these levels. I am net short of equities. So I'm just giving you a an overall, an honest overall of where I am at. I would hate to be any longer of equities in either portfolio than we are at the moment because I just think that what happened, and let me give you my idea of what happened, I think that people got far too, uh, going into this.

It's interesting. I think people were hedged. Okay, so let's start with that. If people were hedged and then they started getting short. By the time we got to the lows, people got very short. And then they started not just covering but covering their shorts, first of all. And then the administration actually did.

Very interesting things in terms of the timing of when they released the, uh, the good news in inverted commas about the negotiations with Iran and so on, and they really made everyone not only cover their shorts, but also the people who had co uh, sold a lot of calls. They just, the gamma just exploded on them at various times.

That was certainly a major contributing factor that I did not recognize. I did not think, A, that it would matter, and B, I didn't think that the timing was really that important. It turned out to have been very important, my mistake, but you know, you live and learn. We've had, I dunno how many quarters of of the JPM caller expiry where nothing happened.

And, but this time it really did matter because of the technical situation that we were in. I got it wrong. The market then exploded through that, and then the CTAs were forced to cover something like 80 billion a day. And there were no sellers. It wasn't that the market was going up because people were buying, yes, they were buying to cover not to get longer, but they just weren't any sellers of the stock.

Why do I think there weren't any sellers now that, that's a more interesting point. I think that when you reallocate between bonds and equities, you have to decide which one you want to own. I think everyone's recognized that bonds at the moment, at these yields are not hedging anything. As Andy said, nah, you know, it, it's neither fish nor foul.

I'm, I'm neither happy with the yield they give, nor am I unhappy. I would be happy at 3% real. I would be very unhappy at 2.5% real, but that's neither here nor there. People were just not buying bonds and therefore. The fact that the big people who own equities for beta IE, you know, you're talking about the ETFs, the BlackRocks, the, the Vanguards and so on.

They just weren't selling. They weren't supplying to the market at any price because they did not need to reallocate. And I think you had this technical situation, which just caused this massive. Huge runup. Now the runup is over, I think. I think the CTAs from all the data that are looked at no longer need to buy.

And people will now start looking at earnings and it's very noticeable that all the earnings, all the stocks that have had earnings so far haven't moved. If anything, they've moved down. They certainly haven't moved higher, certainly in the financials

Andy: and certainly under anybody who reported earnings has underperformed the broader market.

Nick: Yeah. And that tells me, and I dunno if and agrees that the squeeze is over and any squeeze. Normally retrace is at least 50%, so it went from 6,300 to 7,100. If you take 50% of that, that's at least a 400 point move back, and that is what I personally look for in the next 2, 3, 4 weeks. Andy, what are your thoughts on what I just said?

Andy: Well, as I said, I mean, I think you have to decide what you wanna do and what you're, what you're really solving for. For me, solving for a long only portfolio in which you're trying to extract the best risk adjusted return for beta, your job is to be less risky. And so you wanna own less equities, less bonds, less gold, less commodities, more cash.

And so I think two two gray beards original is well positioned, given that today at this very moment. On the other hand, I also am pretty aggressive, like not only was was I pound, like when I pounded the table on February, on March 28th to buy, that was worked out well now. I'm pounding the table for at damp spring to be selling assets and going short for alpha and so two gray beards.

Original, two gray beards squared. Got it wrong, was early and wrong, but now is in the position I want. Now again, it's next. Next money you'll do. No,

Nick: no, no. We are both in the position we want now. Right, right. Okay.

Andy: But that's great. That's, we're in the position we want in both accounts, and so to me, that's the answer.

Nick: Right. What are we looking for next week? Nothing really, because the data is very sparse. Retail sales, usual jobless claims like

Andy: happens maybe.

Nick: Sorry,

Andy: twos, five sevens.

Nick: Yeah. I mean, they'll go fine. You know, it, it's above it. It's above funding. It, it'll go three, four basis points one way or the other.

Andy: Uh, are we gonna get washes? Senate testimony. That's a possibility.

Nick: Who knows?

Andy: The Fed, the, the various Fed Talk guys, Waller made a fair, I think a fairly important speech. Even Moran has been my run is being changing his tune a little bit. The doves are getting less dovish to me.

Nick: Yeah.

Andy: I don't know. I think it's a, it's an interesting question. We'll see. I mean, I think, I think the answer on wars is, he's going to get through and he's gonna do everything he can to make sure not to make any waves. But at the same time, he's probably gonna be on the Dover side when he actually meets.

We'll see if it actually happens. There's still some technicalities on whether they meet, but he's scheduled to. So that's one thing. Earnings, we'll get some more earnings, but none of the major big guys, that's important, I guess. But data is, is light.

Nick: But what is gonna make us change our views is going to be the QRA if they start, changing that.

But are the odds high of that? That's, I mean, before first week of next month,

Andy: before that, we get the fed's not gonna cut. It's not gonna hike, it's

Nick: not gonna do anything.

Andy: And it's has no dots. And, um, it's. Powell's last meeting unless he, it's, unless it's not as chair. So he may get some applause, but at the same time, we don't have a new confirmed chair by then.

Maybe we will by then. Who knows? So that might be, you know, there might be some press conference. Well,

Nick: let, let me rephrase then. What would make you want to go major long equities at this price?

Andy: At this price?

Nick: Yeah.

Andy: Uh

Nick: oh. Higher because they'll be higher. Sure. If you need to buy 'em,

Andy: I'll be pretty clear.

At this price, it's going to take a lot. Um, but the things that I'm looking at are, I've done a fair amount of work with experts and I have some skills at this level as well, but experts on what the potential levers are from the fi, the fiscal side. I don't think it's possible that we get a highly stimulative reconciliation.

I think they're very focused on the D on funding the DHS, which is currently not being funded, and so. It's just because it's not being funded doesn't mean the money isn't being spent. It's just a technicality. So no change to the fiscal side. If they pass a skinny reconciliation that funds the DHS, um.

They could expand it. Now, I don't think there's any possibility that they did, but you know, a highly leased front front loaded stimulus would be a reason to buy equities. The QRA, which is in May, oh, sorry. Shockingly, if the Fed did cut or signal the cutting cycle, that would be a reason to buy stocks.

Frankly, it would be a better reason to sell the crap out of the dollar and buy European stock, uh, global stocks. But it would be a good reason to buy stocks. Some AI miracle would be a good reason to buy stocks. Some stocks. Some stocks, maybe not all stocks. The QRA which is May 4th and, and sixth where we get the data, uh, they could.

Cancel coupon auctions. That'd be a good reason to buy stocks. It'd be a great reason to sell the crap out of the dollar.

Nick: But these are all extremely low probability events, aren't they?

Andy: Right. Which means I'm happy to be short. All the things I can think of. I can think of dozens of things that are possibilities, that are low probability possibilities of why I would wanna own stocks today.

And I can think of very few reasons except momentum investor. Animal spirits and momentum that could cause stocks to rally from here.

Nick: Gotcha. Okay. So next week. Very light as we said. And really, no, no real urgency to change the portfolio at the moment. Good. I'll speak to you next week and that'll be my bit Next.

Andy: Great

Nick: call. Bye.

Andy: Thanks.