Brent Johnson: A big dollar rally could drag stocks higher with it

June 6th 2019

Erik: Joining me next is Santiago Capital founder, Brent Johnson. Brent is extremely well known for his dollar milkshake theory which, in my opinion, along with Jeff Snider's dollar squeeze theory, is really one of the most insightful explanations of what's been going on with the dollar index and the reason that we've seen so much strength in the dollar, even when interest rate differentials would seem to suggest otherwise.

I want to refer our listeners, before we get into the interview with Brent, to a couple of previous episodes. We've had Brent on – not in his own feature interview; this will be Brent's first feature interview today – we had him almost as a rebuttal to Luke Gromen's last feature interview.

The link to that interview, including Luke Gromen's very dollar bearish story along with Brent's dollar bullish rebuttal, you can find that in your Research Roundup email or on our home page at macrovoices.com next to Brent's picture. Also, Brent recently did an All Stars appearance for MacroVoices where we talked a little bit about the dollar.

Brent, I think that since we have not had you on the program as a feature interview guest before, I'd like to just do a quick recap of your Dollar Milkshake theory. What is this all about? And why is it that you think about the US dollar index a little differently than most analysts who tend to think that, really, the value of the dollar has everything to do with interest rate differentials. And a lot of analysts really don't see some of the other aspects that you believe are driving the dollar.

Brent: Thanks again for having me, Erik. Always happy to talk to you and your listeners.

I'll go through the Milkshake theory pretty quickly. There's a lot of info out there on it for those of you who want to have a deeper dive.

But, essentially, the Dollar Milkshake theory is kind of a play on a movie about where this guy was drinking up the oil of his next door neighbor by using a straw.

What I mean by that is that over the last (let's call it) 10 years, the central banks took out their monetary syringes and they pushed down on their plungers, which is the interest rates, and they flooded the global market with liquidity. They printed yen, they printed yuan, they printed dollars, they printed euros, they printed British pounds, etc. etc.

So there was this big pool of capital out there. And that went on from (let's call it) 2010 to 2015 (for lack of a better time period).

And then at the end of 2015, the US got rid of its syringe and they stuck a straw down into this milkshake, that I call it. We've got this currency milkshake out there and the US stuck their straw down in there by raising interest rates.

So now, rather than pushing down on their syringes, they're lifting up on their syringes and they're sucking that capital up into the US economy. As that happened, the dollar started to get stronger.

It hasn't broken out yet. In some cases, I would argue that the Milkshake theory is only just getting started. Some people think it's at its end. I really don't even think it's really started yet.

But that higher differential in US interest rates versus the rest of the world, and the fact that our domestic economy, at least on a relative basis, has been stronger than other domestic economies, has pulled capital into the US. And as we move forward, I think that that continues.

Now that doesn't mean that things are good here. It doesn't mean that the US economy is accelerating. It doesn't mean it's hitting on all cylinders (for lack of a better analogy). It just means it's better than everywhere else.

And for those who argue that it's not better than everywhere else, I ask why was the US able to raise interest rates nine times when Japan has made modern monetary theory their national pastime and Draghi has never raised once in 10 years? So the fact that we were able to do nine of them and nobody else could even do one, to me, kind of validates what I'm saying.

Now, again, it doesn't mean that the global economy is strong. It just means that on a relative basis we are stronger than anybody else.

And I think that that continues. And I think as that continues, it pulls capital into the US and it makes the US markets on a relative basis better than everywhere else.

Erik: Now, Brent, when I've talked to you about this theory before – and I agree with you, by the way, I think the dollar is definitely getting ready to break out and I expect it to move much higher. There are a lot of people who disagree strongly with us on that. And they've made their arguments, and that's great.

But, boy, if you're us and you think the dollar is moving higher, and one of the views that you and I have both had is that all the people that want to get excited about gold, and I think gold is going to be the asset to be long, in the long run. But I haven't felt like it's time yet. I think the dollar goes higher and gold goes lower before this is all over.

Well, boy, look at the last couple of weeks in gold, Brent. It looks like, to a lot of people, the market is starting to prove us wrong with a breakout that I didn't expect in gold. I thought we might get a little breakout above that down-sloping trend line that's been in play for several months. Only because so many people think the Fed is maybe getting ready to pivot back to a more accommodative cutting cycle as opposed to a hiking cycle.

But I didn't expect it to go this high.

Now, as we are speaking on Wednesday morning, we are flirting with $1,350, which has been, for four or five years now, that has been the level that has capped gold. So a lot of people think it's about to break out above $1,350. And that would seem to prove us wrong.

What do you think about the message we're getting from gold here?

Brent: Yeah, it's been quite a couple of weeks for gold. And I kind of go with what you said. I was expecting a little bit of a bounce. I didn't expect it would be this high.

But I'll tell you, I have not changed my opinion.

And, before I answer this question specifically, I just want to say that, listen, I'm a huge believer in gold. There may be a handful people out there who have put out more work than I have on why everybody should own gold on their portfolio, and I still believe that.

I just don't happen to think it's going to pay off right now, even despite this short-term bounce. I actually bought some puts on the minors earlier this morning, kind of as a short-term trade, because I think this is a little bit overdone in the short term.

So I do think that gold is going to pull back.

Now, I might be wrong. And, here's the thing. I don't mind being wrong. I've been wrong many times in my life. I'll be wrong many more times going forward. That's the nature of this business. Nobody is going to be in this business for 20 years and not get it wrong on several occasions.

One of the key things is when you get it wrong not to lose too much money. So I own gold. I don't expect it to pay off now.

I thought this morning provided an opportunity to make a little short-term trade, which I entered. But if I lose money on that trade, I'll make money on my long-term gold thesis and it will be fine.

But I just think that the dollar hasn't even really broken out yet. And I think when the dollar finally breaks out, I think that that's going to at least initially be bad for gold.

Now, we've spoken before, and we've talked about how eventually I think that there will be enough chaos out there that both gold and the dollar will rise together versus all other currencies. I don't think we're there yet. We might be.

And, like I said, if I'm wrong and gold keeps going up, that's fine. I'll say I was wrong and I'll move forward. But, in the short term, I think gold is a little bit overdone here. I'd be a little bit careful chasing it.

Erik: Yeah, I couldn't agree with you more. I have not dared to short it here. But I expect what's likely to happen is $1,350 or $1,360 – in there somewhere – that's where the very, very strong resistance level has been.

And, certainly, if we see a decisive breakout above that level, it's time for me to rethink my view and buy some gold too. But so far I'm not expecting that to happen. And, exactly as you say, the beauty of these markets, once you get the process down it's okay to be wrong, as long as you've got a plan for what to do next.

Let's move on to bond yields. A lot of people thought, boy, we were going to hit that 3.10 on the 10-year, and it was just going to be all over after that, and we couldn't go anywhere but higher in bond yields.

Now we've got moving down to crashing. Crashing is maybe a little bit of an exaggeration but, boy, collapsing bond yields.

What's going on? Is this about a recession signal? Or is there more to this story?

Brent: I think it's a little bit of both. I think that, listen, the smartest guys I know are all bullish rates. Or they've all been telling me that rates are going to go much lower and perhaps to zero, and to be buying bonds over the last 6 to 12 months.

And I give them credit; they've been right. It's been a great call.

I have exposure to short-term bonds. I have never loaded up on the long-term or anything and I haven't made a killing by owning bonds in the last year. But that's okay. That's a trade that I'm okay sitting on the sideline and letting somebody else make money.

I completely understand the argument for rates going much lower. I'm just not convinced it's going to happen. And I think it's actually possible that we're seeing somewhat of a low in rates being made now.

Now, again, if I'm wrong, that's fine. I don't have a problem being wrong on that. It's just that if you look up the interest rates probabilities on Bloomberg, the market is saying there is a 99% chance of a rate cut in the next seven months.

And, listen, that is not a contrarian trade. Rates going lower is not a contrarian trade right now. It’s very much the consensus right now. In fact, them not cutting would be a very contrarian stance.

Now what ends up happening? I’m not sure. I actually don’t think that they’re going to raise. Now, if I’m wrong on that, again, fine. I’ll adjust and we’ll go from there.

But I’m not sure that cutting rates does what they think it will do. The stock market, US markets, are within 2% or 3% maybe 4% of their all-time highs. Inflation is around 2%, give or take a little bit. Unemployment is extremely low. I’m not sure that they
need to cut.

Again, I understand the argument for rates going lower, but I just don’t think that the Fed needs to cut. And here’s the thing if they do cut.

Let’s just stand back and think about what a rate cut tells you. A rate cut by the Fed, when the market is near its all-time high, inflation is low, and unemployment is low tells you that, behind the scenes, somewhere that you can’t see, things are really bad. And to me that’s a very bearish signal that the Fed would be sending to rest of the world.

Now there’s two things from this.

If you send out that negative signal, does that really help markets or does it hurt markets? Well the dollar would probably, at least initially, go down on that news. So, from a headline perspective, maybe it provides a little bit of a down-push on the dollar and that provides a little relief for the people who are having trouble getting dollar funding.

But what are the other central banks going to do if we cut? Remember, Japan has been doing QE or modern monetary theory moves for 20 years now. The ECB has been doing it for 10. Nobody can get off zero except for the US. Are they, after everything they’ve done, and now the Fed comes in and cuts, do you think those guys are just going to sit there and do nothing?

I think as soon as we cut Japan probably cuts. And maybe Europe goes even more negative. I just don’t see this being a huge thing where the US rates are all of a sudden falling, the rest of the world is raising, and the dollar just goes to zero.

I actually think that if the Fed were to cut and the dollar were to fall on that headline, I think it would be an incredible, incredible buying opportunity.

I mentioned to you in January, Erik, that I am so convinced the dollar is going higher over the next couple of years I’m in the middle of setting up a vehicle to actually play this theory. And we literally are just launching this month. I am looking across the board at all these different opportunities and I just cannot believe that they exist.

Erik: Brent, I want to jump on that and talk about little bit more specifically what are these opportunities that you're looking at? We've talked about a view that we share, which is the dollar is headed higher.

Are you just talking about being long the dollar? Or is there more to the story?

Brent: Well, there's a little bit more to the story. But I'll tell you, Erik, I really think the whole world is the dollar story right now. As goes the dollar so goes the world.

And, as we've discussed before, I think ultimately the dollar goes much higher before it goes lower. And the knock-on effects of the dollar going higher, I think, create a lot of disruption in the market.

And, because the dollar is not expected to go as high as I think it is, the pricing of some trades out there is very favorable for those who do think it's going to go that high.

As an example, if you look at currencies – like the yen or the Australian dollar, or even the Swiss franc, the euro – because of the wide differential in rates, the option pricing to buy puts versus these other currencies', puts on these other currencies versus the dollar are very favorable.

You can go out and buy a 2- or 3-year put on the euro or the yen and outlay a very small amount of premium to buy a very large exposure should that reverse or should the dollar strengthen versus them.

And the US dollar, for all its flaws – and, believe me, I agree it is very flawed – but for all its flaws, it is still the world reserve currency. It is still used for a huge percent of the world's trade and trade finance.

Not only that, but a number of countries have gone out there and borrowed in dollars. The rest of the world, not the US, the rest of the world owes 11 trillion in dollars. So there is still huge demand for the dollar.

So when the US has rates significantly higher than the rest of the world, and the rest of the world is, in many places, negative rates, the pricing for that to reverse – because I do believe it will reverse. Now, whether it reverses next month or next year, I don't know. I think it happens sooner than many people think it does.

But if you give yourself a two-year window for this to happen, the pricing on some of these puts versus the dollar are really spectacular.

Erik: Brent, I want to move on to the stock market. Because if I think about the way most people think about relationships between markets and macroeconomic theory, they would say, okay, this Brent Johnson fellow...

He's very, very bullish the dollar. Dollar rallies tend to go with stock market crashes. And, furthermore, he's not particularly saying that the dollar's strength is about a strong economy. He says it's other factors. So not a really strong US economy, dollar moving higher. Sounds like this guy must be a super stock bear.

But that's actually not the case. Please explain why you have a theory that this dollar rally might actually be the catalyst that causes stocks to move much higher.

Brent: I'll tell you, out of all the parts of this theory that I get challenged on, this is the one. There are a number of people out there who can understand the dollar getting stronger. They often will come back to me and say I just don't get the hot stocks going higher part of it.

And my thought is that, if I'm sitting in somebody else's shoes and I'm not in the US – let's say that I'm in Italy as an example – and I'm managing some kind of a pension fund or an endowment or even just a very large portfolio. Now, say whatever you have to say about the US economy. Criticize it as you will. Fine. I'll accept that.

But then compare it to the Italian economy. Now, do you honestly think that the Italian economy is better than the US economy? I have a hard time getting to that one. Especially with their banking system, which everybody knows is (for the lack of a better word) insolvent.

Now, you also have the potential for Italy, with their government, to not play nice with the rest of the EU. And so you're sitting there looking at, as an asset manager in Italy, and trying to figure out where to place your assets.

You can buy European sovereign that's giving you a negative yield. Or you can buy a US Treasury that's giving you 2% or 2.5%. To me that's not such a bad idea. Because if the euro goes lower and the dollar goes higher, then you get your 2% or 2.5% coupon and you get the dollar strengthening. All of a sudden maybe you're at a 4% or 5% return.

Well then you also go out there and you look and you say, okay, what about equities? Do I want to buy an Italian or a Spanish or a UK blue-chip company? Or do I want to put my money in a big blue-chip US company?

I've used the example of Phillip Morris before. And I always use that because I think it is a very big company, it's got a great management team, it's product is somewhat recession proof, and it pays like a 4% dividend.

So if I'm sitting in Italy, and I am looking around where to put money, and I can buy US blue-chip, and the dollar goes up by 4% or 5% versus the euro, and I get a 4% or 5% dividend on top of it, all of a sudden I'm at 8% or 9% return. That's not so bad, right?

I use the Italian example, but I think it exists for somebody in Australia, I think it exists for someone in Canada, I think it exists for someone in Japan, I think it exists for someone in Spain.

I think it's kind of a global thing.

Again, it's a relative world and I think that when things start to break that the US will be seen as a relative safe haven.

This leads into why I said earlier in this conversation that I'm not even sure that the Milkshake theory has really gotten started yet. And that is because the dollar hasn't really broken out yet. And the rest of the world, even though they're not growing gangbusters, they haven't really started breaking down yet.

I think when other markets start to break down, and they start to realize that their economies are in worse shape than they think that they are, and they start looking for safe havens, that's when I think the flows are going to start coming back into the US. And I think that that can push US equities higher.

I saw a chart yesterday and it showed all the flows that have been going out of equities over the last, I think, four or five months. And it's a huge number (I don't have it right in front of me).

And I was thinking, okay, we've had this huge outflow from equities and yet they're still within 3%-4 % of the all-time highs. What happens when those flows come back? Or what happens if the flows just stop leaving?

So I think that there is an opportunity for the US equities to go higher. Not because things are good but, in some ways, because things are bad. And that's kind of how it ties in to the Milkshake theory.

Erik: Well, I think that's extremely insightful, Brent, because I have been bearish on US stocks. But if there is one theory that I've heard that really explains to me why I should think about a serious upside risk in stocks, it's exactly what you've described.

I guess the way I would put it is there's never, ever, in all of recorded monetary history been a time when we had dual bubbles in both sovereign bonds and in stocks created by 10 years of accommodative central bank policy. That's never, ever happened before. We're in uncharted territory.

And any assumption that we might have about what happens when things start to turn south – normally what happens in most markets is the stock market goes down dramatically and the money flows into the bond market, because the bond market was probably already depressed at that point.

But the bond market is not depressed at this point. It's at all-time highs, all time low yields or close to it, within a percent of being a 35-year low.

So when you get people panicking, the idea of let's sell all of our stocks – say you're in Europe

and you've got both European stocks and US stocks in your portfolio. Things are getting bad, it's time to panic, let's sell all of the interest that we have in stocks – that's ownership in productive companies that actually produce a profit – and let's instead throw the money into negative-yielding sovereign debt in a currency block which a lot of people think is collapsing.

It's not necessarily true that people are going to exit stocks and go into sovereign bonds in their own countries the way it's always worked in the past, because these circumstances are so different, and nobody knows what's going to happen.

So I certainly don't interpret what you're saying as any kind of certainty that the stock market is going to go way up. But if it does, I think this is probably the explanation.

It's the same thing that so many people have said to me about gold. I've expressed a real skepticism that it's not time yet for gold. And I really think that I'm right about that in US dollars. If you are a European investor and your savings are in euros, the time to get into gold was a long time ago.

It's a whole different game and you've got to understand that that's really big. There is a risk that the European Union is beginning to fall apart. And if it starts to look like it's really falling apart, that's going to create a mass panic exodus.

And it's an exodus from what into what? We don't know because the dynamics are completely different.

Have you found any corollaries or examples in history where you had a situation where there was a setup like this? Where maybe the economy is finally turning south but you're going into a situation where any flight capital coming out of stocks would have to go into what's already a bond bubble? Out of stocks and into the safety of negative-yielding sovereigns?

Brent: And that's why I say – listen, there's that famous saying, there's nothing new under the sun, right? This has probably happened before. I don't have a good example off the top of my head.

But, I just look at now and I say there's no real easy answer here. And, listen, there's this theory that's gone around for the last two or three or maybe four years where they would talk about TINA when talking about the stock market, which means There Is No Alternative.

And I always kind of hated it. Because there is always, you can always sit on the sideline. You don't have to invest.

Unless you're a manager of a mutual fund or an endowment or some institution, you don't have the ability to go to the sideline. Your mandate says you are invested. Where are you going to place the money? So you do actually have to put your money somewhere. And I don't believe that people are going to continue to plow their money into a negative-yielding bond.

Now, could I be wrong? Of course I can be wrong. But, as I look around, I have a hard time believing that's the case.

And you mentioned something when you were just talking there that made me think of something else regarding bonds.

I don't have a big desire to get into the big bond debate. I completely understand the argument for yields going lower. And very, very smart people believe that that's where it's going. Again, I'm kind of willing to sit on the sideline and let that trade go by.

But if I had to take the argument on the other side and I had to challenge the view, this is one thing that I think people may be forgetting or overlooking.

Part of the reason that a lot of people think interest rates are going lower is there is very low inflation. And the prospects for inflation don't look great.

So if I was going to argue for the upside of inflation, this is how I would start it.

As part of my whole worldview, I've said before that I think the rest of the world, as the dollar gets stronger, the rest of the world is going to experience deflationary effects because of all the dollar debt that they owe and the dollar funding that they need.

But maybe I should have said more of a stagflationary as opposed to pure deflationary.

Because, if you look around the world, especially in emerging markets, food makes up an incredible amount of the cost of daily budgets or daily living expenses. And I think I can make a case where food prices 12 to 18 months from now might not only be higher but could be significantly higher. And that leads to inflationary effects.

And if we start to get those and that starts to percolate up, then maybe the Fed has a harder time continuing to drop rates. You know, if there starts to be some inflationary effects, now they've got to start taking that into consideration.

Here's how I would argue it.

In China they have I guess I would call a hat-trick of problems in their food industry. They've got the Asian swine flu, which I promise you is a bigger issue than even the people who are out there ahead of it are saying it is.

There is the army worm which is now hurting their grain crops.

And then, last week, they had a bird flu outbreak. So now it's attacking their poultry.

Now, for the biggest country in the world to potentially go into a food shock trying to feed all their citizens, that's a big problem. And you're already starting to see that lead to higher prices in substitutes such as beef. That's on the meat side of things.

But let's talk about the grain side of things. Again, they have the army worm problem in China. Now, in the US, we've had some severe storms in the spring. A large percent of the farmable land in the Midwest has not even been planted because they can't get into their fields to plant.

And there's still standing water. And the banks of the Mississippi have flooded. We've had the biggest floods along the Mississippi in, like, 100 years. So the crop production 6, 12, 18 months from now could be constrained, or the supply of grain could be constrained.

Now all of a sudden you've got rising food prices because demand is still there. We've still got all the people but we've got less supply. And now you start to get social unrest in these countries where food prices are going up but their earnings aren't going up and their wages aren't going up.

It was five or six years ago where we had the Arab Spring uprisings across the Middle East and North Africa. It all started because of food prices.

So I just think that it's a fascinating world right now. I'm not convinced that inflation is as contained as many people would say it is. And I think that we could start to see some real, not just social but geopolitical, knock-on effects of what's going on.

And when that happens, I think the dollar in the US gets capital flows as a result.

Erik: I want to talk about the long-term view that you've described associated with the Dollar Milkshake theory where you've said that there could be – and I want to be careful.

You have not predicted that this is a certainty to happen. You've just said there is plenty of possibility for a really, really big move in the dollar index to all-time highs, say 125-plus on the dollar index.

Here is my problem with that. I'm going to make a little bit of a crazy analogy.

If you were a structural engineer, and you told me you've done some analysis and you're convinced that the Brooklyn Bridge is going to collapse, and the cars driving across it, everybody is going to be killed as a result of this horrible thing, I'd say, well, that's a big prediction. Let's see what your data is. I can believe that that's possible. It's an old bridge.

But if you told me that what's going to happen is the bridge is going to collapse and then, for the next two months, all day long, cars are going to drive off of it and everybody is going to die, I would say, Brent, you're crazy. They would close the road.

I guess what I'm not seeing here is there is so much risk to the global economy if the dollar really, really starts to take off. Let's say above 110 on the dollar index, for the sake of a round number.

That would cause so many problems with so many countries and major corporations around the world, foreign companies that have borrowed in US dollars that would suddenly be unable to repay their debts. It would make US exports next to impossible because nobody would be able to afford them. It would cause so much damage, it seems to me like they would close the road and it wouldn't go any higher.

What I mean by that is some equivalent to the Plaza Accord, back in I think it was '85, when there was an agreement explicitly for governments to work together to suppress the dollar.

It seems to me that, for any theory that involves the US dollar moving above 110 on the dollar index, there has got to be some analysis of when they at least try to close the road and what happens.

So how do you think this would play out? At some point is there a Plaza Accord? What happens?

Brent: Very good question. Ultimately I do think that there will have to be some kind of a Plaza Accord. I think the dollar will have to get revalued lower. I've said before that I actually that, when that happens, the Plaza Accord will be welcomed and the rest of the world will beg us to devalue the dollar because they will need it even more than we do.

And, listen, Trump is a very, very big part of all of this. Now, Trump hates that we have this strong dollar. And he's come out several times and said he wants a weaker dollar.

But why does Trump want a weaker dollar? Trump wants a weaker dollar because he wants the stock market to go higher. Well, if the stock market is going higher, I think his concern about the dollar kind of goes to the backburner. And he's more worried about other things and worried about other fires that he's got to put out.

And if we get back into a situation where the dollar is going higher, it creates pressure on other economies. The capital flows from those other economies into the US and the US stock market goes higher.

That, perhaps, keeps Trump happy. Maybe happy is not the right word. I don't think the guy is ever happy. But maybe that keeps him from continually jawboning down the dollar.

But I do think that, as we go along this road, there are going to be attempts to counteract the dollar. This is not going to be a smooth ride from dollar 98 to dollar 150. It will be extremely scary. It will be extremely volatile. I think there will be periods where the dollar really spikes and it will pull back hard. And it will spike again and it will pull back hard.

Let's go back 10 years to 2008. You made the comment that the world just doesn't work with the dollar going to 120, 130, 140. Well, the world didn't really work with the DOW going from 18,000 to 6,000 either, but it happened anyway.

If you look through the summer of 2008 and into the fall of 2008 and then into the spring of 2009, the markets would go down. The monetary authorities, the central bankers, the governments would come out and they would institute policies. They would ban short selling, they would do some stimulus plan, they would cut rates. And the markets would rally a little bit. And then pretty soon you're back to reality.

And the markets would crash again. And they'd come out and they'd say something else or they'd institute some other policy. And markets would bounce a little bit and then back to reality. And it goes down again.

So I do think, to your point, there will be cops that will approach the bridge and tell people don't drive off the bridge. But, then, I don't know that those cops are going to be able to stop it, to be honest, until they put up road barriers and completely shut the whole thing down.

I mentioned to somebody before that my theory is not called the Glass of Milk theory. It's called the Milkshake theory. And there's going to be a lot of shaking going on.

And even if I'm right, Erik, even if I get this right, there are going to be moments of pure terror for me along the way – and everybody else. This is not a nice smooth ride to the endgame.

Listen, this is going to be crazy. I guess that's the best way I can say it. To think it's going to be anything other than crazy I think is naïve. Even if I get part of it right and I'm able to make money on it, it doesn't mean that it's going to come without some real white-knuckling along the way.

Erik: Now, I want to ask you how in the long term your theories eventually meld together with others. Because a lot of our listeners are familiar with Luke Gromen's view.

And, at first glance, it would seem that you and Luke just polar opposites who see the world in a completely different way and just can't agree. Because Luke has been hugely dollar bearish. And he is (I think) right now, tactically still long the dollar. But he's waiting for it to reverse. He thinks it's imminently upon us. And he thinks that the road is much, much lower.

So most casual observers would assume that you guys never see eye to eye.

Personally, the way I see it, is I am absolutely convinced that Luke is going to be proven right. I just think you're going to be proven right first. I think Luke has the story exactly right. He's just early.

I want to know what you think about that.

Luke's view is basically that the US dollar is going to lose its hegemony over the global financial system, probably lose its reserve currency status, and fade into the sunset very similar to the pound sterling, which used to be the world's global reserve currency.

The currency never went away. We've still got the British pound, but it is nowhere close to the importance that it used to have in the global financial system. And it devalued a long way along the way.

Do you think that Luke's got that wrong? Or do you think he's just way early to expect those things to happen?

Brent: I think a couple of things. And I say this every time I get this question. I like Luke. I actually consider him a friend. If I bumped into him in the airport and we had to sit there and hang out before we each caught our flights, I would enjoy that two hours.

So I don't have a problem with Luke's criticism of my theories or our debates or however you want to define that. I think it's actually, maybe, perhaps a mutually beneficial thing because there's times I probably make him think about things he hadn't thought of and vice versa. He definitely makes me think about things that I haven't thought of.

I think you're largely correct on how to define our views. I think he is really early. But I do think, ultimately, a lot of the things that he is talking about will come to pass.

Part of the reason that I perhaps come back against him as strongly as I do is that I actually manage money for individuals. So when I'm investing and we're going over results, I'm sitting there looking the person in the eye talking to them about how their results have gone and how this is personally going to affect them.

That's a little different than managing money institutions where you never actually see the people that it affects. And it's a little different than writing research where you're not actually placing money in the market.

And my experience has been that everybody says they're a long-term investor and they're in it for the long term – until it goes against them. Mike Tyson said everybody has a plan until they get punched in the mouth. And I think there's real truth to that.

The reason I bring that up is, if you are seeing what Luke is talking about and you are placing your assets for 5 to 10 years down the road, and you don't mind – you have to be really honest with yourself here – you don't mind getting punched in the mouth really hard over the next couple of years, then sure. Then you place your assets for the dollar getting weaker because 5 or 10 years from now it will be a lot weaker, I think.

But I think it's very possible in the next (call it) two years, the dollar just pummels everybody. And I don't know a lot of people who can withstand the pummeling. They say they can. But when they start getting hit, they want to get out.

Not only that, but I think there is a great, great number of opportunities to play the move in the dollar over the next couple of years. And I just want people to know that, even though Luke might be right in the long term, it's possible that he's wrong in the short term. And that it's possible that I'm right in the short term.

I want people to go in with eyes open and understand that the move before the dollar going to zero could very well be going back to all-time highs. And I would hate for them to get shook out of their long-term trades if they weren't prepared for that.

Erik: Brent, you said earlier that there is a possibility that foreign capital flows could drive equity markets much higher. Now, we talked about that in terms of how it is plausible for the mechanism to operate.

In the current environment, where we're seeing what to me are a lot of recession signals and bearish stock signals, is that mechanism strong enough to overcome the bearish factors? Or is it maybe a setup that we're going to see a bear market that I think is coming? That maybe still it's a short-lived cyclical bear market and there's still another wave higher?

Or is it really that you think stocks are headed higher from here, right now?

Brent: Last fall in Q4, and specifically the very end of December, I was pretty aggressively buying equities. And that turned out that we were fortunate that that was the right call and we had a very good first (call it) four months of the year. And, just being prudent, we took down exposure a little bit and bought some puts in early May, which has really helped us out.

I just think that the next three or four months are pretty uncertain, let's just say it that way. And I think prudence says to just be careful for the next two or three months until we get some more visibility on what's actually going to happen.

I think that the dollar breaking out is going to be the key to the US market maybe moving higher, the US equities moving higher, when that starts to cause problems abroad.

I actually think the dollar is going to break out later in the fall, but it could be as soon as next month.

There's a couple of things that I'm looking at that tell me we're not going to have to wait another year to see what the dollar does. Because we were fortunate to have a good first part of the year, we kind of have the luxury of being a little careful over the next three or four months. So we're going to be careful.

And I should always caveat this: My mind could change later today based on what I see.

But, as of right now, I think it's probably likely that equities consolidate, maybe go up and down over the next two or three months. Perhaps we have a volatile summer while we're trying to figure out which way to go. But ultimately, just to be clear, I ultimately do think that we are going to see higher highs before we see significantly lower lows in equities.

Erik: I want to come to a very similar question, but let's go back to gold now. You and I, I think, both agree here. As we're speaking Wednesday morning, we're flirting with that $1,350 level. So far, it's been rejected pretty aggressively. But of course anything is possible.

Let's suppose, Brent – going back to your statement that your mind can change very quickly – let's suppose that, by the time our listeners hear this interview about 36 hours from now on Thursday evening, that we have seen a breakout in gold and we've got a daily close over $1,400.

At that point, is it time to just throw in the towel and say okay we got the gold call wrong? It turns out that the move is on to the upside and it seems like the dollar and gold are going to move up together and it's time to roll with it and increase your gold holdings?

Or is that a signal that, okay, it's gotten ahead of itself and it's about to reverse, maybe as the dollar comes off of a low?

Brent: That's a very good question because I'm sure there's a lot of people out there who are wondering this exact thing right now. I would be very, very, very careful chasing it at $1,400 right now. If it were at $1,400 by the end of the week, that would be a pretty strong sign that we're looking at a breakout.

But even if we have a breakout, I think we'll probably come back and test the $1,360-$1,375 area before then moving back to about $1,400 again and up to $1,500 or whatever it is.

I've seen too many times people buy these breakouts (quote unquote) only to see gold pull back $50-$60 in a very short period of time.

I would suggest that listeners do this: Go back and look at a chart of gold last year versus this year, year-to-date. Now, they are not exact but they are very similar.

In 2018 we had a big run-up in the spring, we had a pullback in May. Gold then popped back to $1,315 or $1,320 right ahead of the Fed meeting in June. And by the end of June we were at $1,250.

So it's not exactly like that this year, but it's pretty similar. I mean, you just don't know where we're going to go. This is part of the reason why, for the last six or seven years, I've been

encouraging people to just buy some gold and forget about it.

Now, I don't think it's going to pay off yet, but I think you should own it. Hopefully, people listening already have some gold in their portfolio.

If you already have some gold in your portfolio, you don't have to chase it here. If it goes to $1,400, be patient. When it pulls back to $1,370 or something like that, then maybe start adding. But I wouldn't be buying if I wake up tomorrow morning and gold is at $1,400. I'm not going to be adding until at least the end of the month. I would wait and see where we're at two or three weeks from now.

Erik: Brent, earlier in this interview you mentioned that you were in the process of launching a special-purpose fund to pursue the opportunities that you see relative to the dollar index.

Now, just to explain to our listeners, because that fund is only available to accredited investors, Brent is not really at liberty to make any specific representations about the investment strategy and so forth. But what I do want to ask, Brent, is just what is the approximate timing? And, for the accredited investors who are qualified to invest and learn more about that, how should they contact you in order to find out more about what you're up to?

Brent: I think it's important to start off and say, listen, this isn't something for everybody. We designed this – I'm partnering with Keith Dicker of Icecap Asset Management to launch this vehicle. And we're doing it because we both have very similar businesses where we manage money for high-net-worth individuals.

We see the dollar getting stronger as the biggest single factor influencing global markets over the next two or three years and it has the potential to impact markets extremely negatively, especially for investors outside the United States.

It's very difficult to protect against these types of moves in separately managed accounts for individuals. We wanted to have a vehicle through which we could put some of our clients' capital in there to help protect against the potentially negative effects of a stronger dollar but then also capitalize on what we see as incredible opportunities as the dollar does get stronger.

It's not for everybody, but we think it plays an extremely important part of an overall diversified portfolio. And if somebody wants to learn more about it, I'm available at brent@santiagocapital.com. Happy to discuss in more detail.

Erik: Well, Brent, it's great to finally get you on the show for a full-length feature interview. I look forward to having you back. And in the meantime we're going to have you every few weeks at MacroVoices All Stars to get an update on some of these views.

Patrick Ceresna and I will be back as MacroVoices continues, right here at macrovoices.com.