Title

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Erik: Joining me now is Diego Parrilla, the portfolio manager with Quadriga Asset Managers. And a good friend and co-author with our good friend Daniel Lacalle. Daniel and Diego co-authored *The Energy World is Flat: Opportunities from the End of Peak Oil* published in 2014. And Diego is the sole author of *The Anti-Bubbles: Opportunities Heading Into Lehman Squared and Gold's Perfect Storm*.

Diego prepared an excellent slide deck to accompany today's interview and I strongly encourage you to download it. Registered users will find the download link in your Research Roundup email. If you're not yet registered, just go to our home page at macrovoices.com and look for the red button that says Looking for the Downloads? next to Diego's picture.

Diego, thanks so much for joining us. I want to go ahead and jump right in with the investment thesis that you focus your work around. Of course, you co-authored that book with Daniel Lacalle with respect to *The Energy World is Flat: Opportunities from the End of Peak Oil*. And your new book is called *The Anti-Bubbles*. Tell us what those are about.

Diego: Thanks Erik. *The Energy World is Flat* presented a highly contrarian view of the world. We're looking at 2014, we have $120 oil. We had the consensus view of peak oil which was looking at $200.

And there we came in with a thesis that was arguing for the flattening of the energy world, which had two major implications. One was the convergence across energies with big losers such as oil. And secondly the convergence across regions, the globalization with big losers such as natural gas, or in this case LNG.

Now, the combination of these powerful forces, the flatteners, effectively led to the variable convergence, the flattening of the energy world, which we argued $30 to $50 oil was a reasonable target that probably sounded like science fiction to a lot of people at the time.

It didn't take too long for some of these flattening forces to take force, especially with OPEC sort of folding, and we saw what happened. So I guess that being a contrarian, being a bit of a chess player, being early in the game, identifying more forces.

As an engineer, I do look at the world more as equilibriums, balances, forces. And sometimes you find these sort of big imbalances that it's a matter of when, not if, that things will happen.

So some of these forces are more obvious. Some of them might be slow grinding. Some of them might be driven by paradigm shifts like, obviously, technology and other game changers. But eventually it's a matter of when, not if, that these dynamics play out.

And sometimes they turn out to show the emperor has no clothes. There are massive winners and massive losers in the process. So I found this process incredibly powerful, as I always said, but I knew it.

And teaming up with Daniel was fantastic. He came in more from the energy equities world, perhaps, and me from the energy commodities. We tend to share views. But very often we also found ourselves looking at a square and a circle, thinking this is what's going on. And it turns out, talking to each other, we are looking at a cylinder. So we were both correct.

It really brought this perspective and the analysis and the views after we finished the book to a different level. So I learned so much through that process that I kept that discipline of writing. I guess my brain looks for these sort of relationships.

And the second book reflects this thinking. It's a similar framework in the sense that I'm looking at imbalances, I'm looking at forces.

This time around, the book is more focused on the macro space. And it goes hand in hand with the strategies and the fund that I manage.

But the common theme is we're looking at, effectively, highly contrarian investment pieces, the challenges, the status of the world. And perhaps it might be a bit early, but the processes in both cases not only survive but are actually being reinforced.

So, in this sense, the second book, which is very relevant to today's world and dynamics, it's also bringing and coining the concept of the anti-bubble, which I think could be very helpful for the listeners.

Erik: What is the anti-bubble? Please explain that concept.

Diego: Perhaps it is best to start with the definition of a bubble. And I like to borrow George Soros' definition. He talks about bubbles as assets that are artificially expensive based on a belief that perhaps is very deeply entrenched in people's minds but it happens to be false, what he calls a misconception.

So we could debate at length today whether, I don't know, bitcoin is going to change the world or not. It's out of scope. But certainly the belief that it might do can drive certain valuations. For other people, it might be a very different world. And, to be honest, only time will tell.

But to a certain extent, certainly beliefs can actually distort reality. So, in that sense, the concept of the anti-bubble is born from a generalization of George Soros' framework.

And perhaps the first I mentioned the concept, led to the fact that misconceptions not only distort reality through artificially high prices, which we call bubbles.

You could also have artificially low prices and valuations, which I define as the anti-bubble. So we're looking at, effectively, assets that are grossly artificially cheap, based on a belief that happens to be false, where it's a matter if when, not if, that they will go up.

Now, there is a second dimension that is important. And it is the fact that bubbles and anti-bubbles are somewhat like distorted mirror images of the same misconceptions. They are effectively two reflections of the exact same process.

So, by construction, once the misconception is understood and the bubble bursts it's the exact same catalyst and climbing as the anti-bubble goes up – because they are effectively the exact same process.

So I called it anti-bubble, a bit like an anti-virus or an anti-missile. It is a defense mechanism against the bubble. As I say, which is pretty close to a perfect hedge because they are the same process.

But there is also a third dimension that is relevant and it is the fact that these bubbles and anti-bubbles are also interrelated. There is some sort of a symbiotic relationship between them. They feed on each other.

So if you look, for example, at what in my view are clear bubble/anti-bubble relationships, such as the S&P and the VIX, they are not independent processes. One might argue that some of the artificially high valuations in the S&P are partially driven by artificially low VIX, whether it's in the form of complacency, whether it's both for qualitative and quantitative reasons, which we can discuss in more detail.
Either way, the interesting thing and the opportunity – or the ironic thing we could argue as well – is that nobody wants to buy puts in the S&P at 3,000 and 12 vol, yet everybody seems to be rushing to buy that insurance when the S&P is at $2,400 and the VIX is at 40.

So, in that sense, what we see is a great opportunity. In fact, the market is willing to give us the insurance the cheapest when we need it the most. There is an element here of risk premia, where we are being compensated for taking the other side of complacency and panic.

So, in that sense, the anti-bubble has these three dimensions of value, of hedge, and of risk premia, which effectively lead us to tremendous opportunities. There is a wider framework.

And I guess the question here is focus on the beliefs and focus on the misconceptions because they are the ones that will actually give you the clue. And, again, looking back and looking forward and where the opportunities might lie.

Erik: Diego, when I hear you talking about beliefs and misconceptions, what immediately comes to my mind is this notion which a lot of people call the central bank put. The idea that, hey, it doesn’t really matter what happens, what goes wrong, because the Fed’s got our back.

We’ve seen for the last 10 years they are going to come riding to the rescue with more accommodative monetary policy, they’re going to rescue the market. We don’t need to be worrying about buying those puts that you’re talking about on the S&P because the Fed’s got our back.

I think this has got to be the greatest complacency bubble in the history of the world. Everybody is just convinced nothing can go wrong. And I think valuations are out of sight.

Does that come into your thinking? And how does that play in?

Diego: 100%. I would argue the central bank put is central to – it’s perhaps one of the biggest beliefs, in my view, misconceptions that has been shaping global markets for a long time.

And linking it back to OPEC, for example, in the first book, there was this very widely held belief that in the OPEC put, you remember this idea that oil was perfectly, would hold at such high prices because Mommy and Daddy (Saudi and OPEC) were infallible, in full control. Whereas the reality was quite different.

At the end of the day, Saudi needs X dollars per barrel. Rather, they need, let’s say, $100 for fiscal and other big issues that they may need to finance. And whether that’s produced with one barrel at $100 or two at $50 or four at $25, they still need that money.

But, nevertheless, there was this perception that they could just cut production and be fully in control, which obviously wasn’t the case. In fact, this relationship, this equilibrium breaks. And, once it breaks, then it actually collapses, because then it brings this race to the bottom.

So I think, obviously with the benefit of hindsight, that’s pretty obvious. In the energy book we were challenging that put. And in fact we were looking at this as one of the sources of risk and game changers.

I think we have a similar dynamic here. The central bank put, I would describe it as the belief – it might be a misconception – that central banks and governments are infallible and in full control. And they can print and borrow their way out of problems without any adverse consequences.

Now this is, I think, flawed. And it feeds into arguably two sub-beliefs that are very important. The first one is the belief that monetary policy has no limits. And the second one is the idea that fiscal policies have no limits.

And we have seen this belief being played out. It takes many names. It takes “never fight the Fed.” It’s Draghi’s “whatever it takes.” It’s “PBOC in China is in control.”

We have seen the relentless bullying and financial bullying with not only playing by the rules, which I would argue that bringing interest rates to zero and to some extent QE and printing money was within the rules. But actually breaking into what, in my view, was just one step too far, which is negative interest rates and what's to come in the form of helicopter money and other things that I believe we will certainly see. In fact they are already happening. They just accelerate.

And the central bank put – again, you mentioned and we agree, it's central. And it, I would argue, has two main implications. The first one is complacency and the perception that there is no risk. But, even if there was, don't worry because if things go wrong Mommy and Daddy will come and rescue us.

But the second one is arguably even more dangerous, which is the financial bullying. You know, in Europe, facing negative interest rates, we are literally being told we are pretty stupid just saving money or holding your cash.

And this drives, I guess, a second wave which is also critical in the process – it might be even more complex and complicated because they feed on each other – which is what I would define as the complacent desperate search for yield.

Erik: Diego, as we talk about these complacencies and so forth, I think, as you said, a huge one is this idea that we can have negative interest rates.

We haven't talked about modern monetary theory yet. But I think there is this desperate search for yield and this complacency that people don't think if they keep searching for yield, that they're eventually going to introduce risk that's going to come back and bite them.

So how does that factor into your whole thinking about all this?

Diego: This is very important. I guess the complacency and the financial bullying, and we've been incentivized or perhaps rather forced to take more risk. We've been building the house to the roof.

Once upon a time, we would go to the market and say, hey, I want to take X amount of risk, how much do you pay me for it? We're in a situation now where we say, listen, I want my 5%, tell me what I need to do.

And what we've done is, really, take incremental risk in each and every single dimension you can think of.

The first one and perhaps critical is term premia. It's the bubble in duration, it's fixed-income government bonds, it's lending for longer and longer for lower and lower yields.

And we've seen 30-year bonds now negative. We've seen, obviously, this thirst for duration

with 100-year Austrian bonds. A process that has been driven by this combination of thirst for yield and also artificially high demand from governments in the form of QE and other benchmarks, etc.
I would argue that this is the epicenter of the problem but not the problem itself.

Things really start going wrong where, effectively, we go into the second dynamic, which is the credit risk premia. So, obviously, with negative yields in AAA bonds, we are going down the chain, with perhaps investment grade and then it's high-yield and obviously emerging markets, lending to weaker and weaker credits for longer and longer for lower and lower yields. And creating what I think is a major bubble across the spectrum, including high-yield and zombies and everything else.

This distortion of the fixed-income market and credit markets leads into the third wave, which is equity risk premia. The put called parity relationship, it's broken with negative yields.

You're discounting highly complacent expectations with artificially cheap interest rates, artificially low. You're looking at artificially low inflation. You're looking at so many things that impact buybacks, that impact the valuations.

Which lead us to investors wanting to capture the liquidity premiums. Whether it's private equity, with higher and higher valuations and more leverage, or private credit, where we have effectively shadow banking with lending all over the place and disguised very often as Fintech. But this is stuff that is happening of the system and unregulated and very dangerous.

Liquidity, as we'll come back to, is one of the major issues. We've seen already people gating. We've seen a lot of the issues with the repo and many other ways in which liquidities are wider-term, but it's critical in what's to come.

And then that brings us to leverage. Of course, I want my 5%. My mom used to earn that in Europe for 5% with one-year AAA unlevered bonds not that long ago. Today she would have to go to BBBs 10 to 15 years ex-time levered.

So this process, if you add on top of that what I think is effectively a case of gross mis-selling, these income strategies (quote, unquote) where people are selling short volatility strategies in multiple ways. And these guys, these income strategies – it's very different if I own a house in Miami and I rent it. What I collect is indeed income. But if I am selling hurricane insurance on your house, what I collect is not income. It is insurance premiums at the expense of insurance liability.

So you have a Fed 2018 VIX hurricane come, and people were completely wiped out.

So what's happening here, the conclusion and these two forces, the central bank put, and the desperate search for yield are sort of feeding on each other. This complacency, this financial bullying, this desperation for yield, are leading to what I would summarize as from risk-free interest to interest-free risk.

That nice little concept we have in the textbooks – has now given way to a world where we are literally doing insane things like locking in negative yields for incredibly long times.

So what it has done is it's created, in my view, this series of perilous synchronous bubbles which I would argue that, after years and decades, has taken us to a point where I would argue they are too big to fail. And this is technically a new paradigm which brings tremendous risks – and I would argue also opportunities for investors.

Erik: And how do you translate too big to fail? Obviously, these institutions that are not allowed to fail even when they should, because it is feared by regulators that they are too big to fail. Someday they are going to fail and there's nothing that's going to be done about it.

So when you say there are opportunities for investors, do you mean that you're speculating they will eventually fail? Or are you talking about how to profit from the fact that regulators are likely to keep them propped up as long as they can?

Diego: Well, I would argue that obviously too big to fail takes different forms. You know, 2008 it was all about the banks, it was all about keeping the systemic risk of Lehman – it's almost a lose-lose or a win-win. You need to keep them alive, otherwise the system collapses. But if you keep them alive, then you are incentivizing the wrong behavior.

But the reality is, too big to fail is now a much broader term. We're talking about China being too big to fail. We're talking about the duration being too big to fail. We're talking about these zombies in Europe being too big to fail. Which means you can't hike rates.

We're talking about all these massive bubbles that we've built that go way and beyond institutions. That's where the Lehman squared is more like Lehman cubed in terms of the challenges that we're facing.

And, to me, the fourth quarter in 2018 was an inflection point. I think this process of normalization of monetary policy, where there was a perception that, after all these years of excess and low rates and QE and increased debt, we could just turn things around and normalize things – it became pretty clear to the Fed and the rest of the world that that's just not going to be possible.

A lot of people forgot about this. It's not even a year ago, but we saw GE amongst others being on the brink of collapse, with the implications it would have had. And I think the Fed realized that it was a lot closer.

I mean, this increase in volatility, this increase in correlations, this increase in enforced liquidation, which was starting to have an impact in liquidity, was pretty close to becoming a major liquidity event. We've barely dodged the bullet and what could have been also a reflexive move.

And I think what we are seeing today, again, I'm particularly worried. And I think China is a great example of what might come. But the reality with too big to fail is they simply cannot fail. And, as a result, they will be transformed.

So if I look at the macro picture, if I had to summarize it very quickly, I would argue that all these years of money printing and debt haven't really solved the problems. All we've done is it has delayed, enlarged, and, to a certain extent, transferred these problems across currency wars. "Beggar thy neighbor."

Now we are in a situation where all these dynamics which are contagious, complacent, etc., have led to bubbles which are so large that we can't let them collapse.

Therefore, we are going to see a very, very preemptive central banks all over the world sending rates to zero, including the Fed, effectively paving the way for massive fiscal expansion with expenditures and debts and MMTs that will never be paid back and will be effectively extended to maturity. They'll be whatever, but they'll never be paid back. And we have clearly a problem medium term, longer term of inflation.

So we are now – the problem of bubbles that are too big to fail effectively means that we are in the process of transforming these bubbles into inflation.

Now, there is plenty of room for miscalculation here. There are plenty of risks. The losers are pretty obvious, to some extent. But there are also anti-bubbles in the process. And there are also widow makers to be honest.

I would argue that #1 of the rules of the investment game is that they will change the rules. So if you play the game thinking, oh, inflation is the end game, therefore rates will go up I should short bonds – long bonds – I think you might find yourself in deep trouble. Because the new enemy is bubbles. It's not inflation.

So they're going to let inflation run. And it will also feed through the currency, which is what they want.

But you're not going to see – the rules of the game are changing. And this, again, opens a complex world that is becoming increasingly polarized between extremes of either these bubbles completely implode, until what would be catastrophic in terms of the potential size and impact, or we transform those into a different problem. Today inflation is seen as the lesser evil. I'm sure our grandparents would disagree.

So in that sense the damage is done. I think it would be foolish to think that everything that we've done is something you can just get out nicely. This is something that is compounding these problems and is extremely polarized. And it's accelerating.

So, yes, there are lots of risks. But there are also anti-bubbles and other opportunities in this framework. Although, as I always say, I hope I'm wrong because it is not a pretty picture.

Erik: Diego, as we take this – first of all, I couldn't agree more with you on this big picture. And I think, as you say, they are going to change the rules. They are going to take desperate measures in order to keep things propped up. And it's probably going to result in a whole bunch of government spending and a whole bunch of bond issuance and so forth.

One of the conclusions that I come to is, it's hard for me to see how gold doesn't benefit stupendously from this. And there's lots of ways this could go down. But it's hard for me to see how they bail things out and change the rules without eventually resulting in a major increase in the US dollar per ounce value of gold.

I'm guessing that you agree with that, from the title of your book including "gold's perfect storm." Are we on the same page there? And how does that play into your thesis?

Diego: We are 100% on the same page. I think gold is part of the checkmate of these dynamics. There are very clear processes. I think it's worth discussing how we get to this checkmate.

And I think China is a good example. So China is a country that operates under either a semi-open or semi-closed system. It does trade with the world, but it does it in a way where there's lots of rigidities on the exchange rate, and monetary policy and other manipulations.

So what's been happening is they know what they need to do. But in reality, every time they've faced a crisis, they've done three things. They've printed money, they've lent that money, and they've created implicit guarantees on people.

So if you are about to bail out, whether you are a broker or a construction company, suddenly you are state-owned. Or whatever else.

Now this money that has been printed and lent that can't leave the system, it effectively finds its way like water into two main buckets: infrastructure and real estate – where there is another bridge to nowhere or a ghost city or whatever.

So you have this dynamic where all of this monetary and fiscal abuse ends up a bit like Spain where I'm originally from, of finding its way to these bubbles. We're talking about real estate. And this is not my numbers. This is the main investment banks who owe $40 trillion of real estate bubble. So I would argue this is definitely too big to fail.

Because if you actually think about, okay, what would happen if these bubbles failed and what is the process, you think about the asset values going down, the developers going down, your collateral at the bank, your wealth effect, the banking assets, liabilities, the lending etc. The house of cards collapses.

So what's going to happen is, in the case of Spain, we left these countries like Palermos –

I mean, China obviously has other issues. Three percent of the wealth of the Chinese is in equities – think about it – it's all brick, it's other forms of wealth.

So if that shoe fell, this is pretty major. So it's not going to fall. It's not going to fall because it shouldn't fall. It's not going to fall because they will keep those housing prices in yuan artificially high.

Now that doesn't mean that those houses will stay high in dollars or euros or yen or whatever. So the degree of freedom – and this is very, very important to understand – the way in which China blows up is through the currency fund, so currency devaluation manipulation etc, which we're not talking about a small 5% move. We're talking about a major move. Technically, it's more of the same.

And, as a European, I would argue that part of the 2012 crisis came from the US QE in 2008 extending the euro up to 1.50, and along with it the euro/yuan, to which the Chinese currency was pegged.

So, as a European, I have sympathy for Draghi who walks into the office and say hey, man, I need to defend myself. And Europe came in and not only did QE in another form. It actually had to go way bigger and way farther with negative rates as part of this contagious process. Which then led to China doing stuff in August '15 and January '16 etc.

So this circle eventually brings us to a situation where, why are we doing currency wars? What are the benefits and risks? And I think it's important to understand that there are obviously positives and negatives.

Well, start with the negatives. You have certain bubbles. You have inflation because, if the yuan is 20% weaker, then oil in yuan is 20% more expensive.

Now this is more than offset in the case of China by the benefits, which is, oh, I am a cheap labor, I'm competitive, I'm a cheaper economy to produce, therefore people send their factories, they do the investment, the spending, and the economic activity, employment etc.

So China is balancing these two forces of the negatives of inflation and bubbles with the positives of others until you get trade wars.

Because trade wars are very critical. It's a new phase and it's very much a defense mechanism against currency wars.

We need to understand, when you have beggar they neighbor, when someone is misbehaving and sending you the crisis in the way of artificially cheaper production costs and whatever, at the end of the day, Mr. Trump, whether you like him or not, he basically looks at this and says, hey, General Motors, I didn't bail you out so that you could produce in China. I bailed you out so you could produce in Chicago and Detroit. So you know what? By law you're not going to be able to do this.

And, by the way, Apple. I know you don't owe me anything. But, to be honest, if you want to produce 20% cheaper in China, I'm going to tariff you by 20%.

So all trade wars are doing is neutralizing these currency wars. And the important thing to understand is that then the emperor has no clothes. Because economies that have been effectively trying to print and borrow their way out of the problems, through beggar thy neighbor, find that they are left with the bubbles and the inflation. And they have no benefit.

And then you have Venezuela and then you have Argentina.

So the flip between China from a perceived world power to a complete Ponzi is, in my view, more fragile than people think. And, to some extent, it might fall by its own weight. Or it might be triggered by some of these dynamics.

So, in this sense, going back to gold, if I look at the currencies around the world – and this is a marathon race – you would ask me, Diego, who is going to win the race or who is going to lose the race? I would think this is an easy call. I think gold will win the race. And people like Venezuela or Turkey or Argentina will lose the race.

It is less clear to me whether the dollar, the euro, or the yen, how they will peg in this race. But my contrarian view – because, believe it or not, a view that gold and the dollar are both up happens to be a contrarian view – and it gives you opportunities also to structure trades with very, very attractive risk/reward.

So I do think gold will be a big winner and it's a critical part of this process of printing and borrowing your way out of currency and trade wars.

Erik: Diego, I couldn't agree more with you on the big macro picture. But I know our listeners will thank me if I ask you to translate that now to portfolio construction. How do we take all of these big picture ideas and translate them what to invest in?

Diego: Great question. Warren Buffett has two rules of investment. He talks about don't lose money. And rule #2, don't forget rule #1.

Which sounds great and very wise, but I think it's somewhat cynical in the approach because many of the long-only people will face very significant losses during a Lehman scenario or others.

So I do agree with him, but this is a game of capital preservation first and foremost. And I think what he means is you need to compound on that capital preservation. To some extent, cash might help you there in the short run. But I think there are much more efficient ways to do this.

So let me, perhaps – this is a global audience, so let me take an example using a portfolio as if it was a soccer team, a football team. And, trust me, it has quite deep messages.

The first point I would make – and this is for the listeners just to reflect on – is many people think that investing is a game where you win by scoring goals. It's all about making money, right? And in investing my money I want to make money. I want to make capital gains, I want to make income gains.

It's this mindset of strikers. It's all about scoring goals.

Whereas, in reality, whether it's the case in football or basketball or any sport, there is also a very important aspect of the game, which is playing defense. In fact, I think that in order to win you must first not lose. And, to me, it's all about capital preservation and compounding on that.

So when you build a portfolio – the first thing we need to be aware of is that some people might be playing by the wrong rules. They think it's all about scoring goals. And, as a result,we have 10 or even 11 strikers.

So your equities, your credit, your high yield, your EM, your commodities, your private equity, private debt, venture, real estate, the whole lot is designed to go and make me money.

So I think in that sense, when you look at the team, there are some hidden risks, particularly one which I define as the risk of false diversification.

False diversification is confusing the fact that you have a lot of stuff in your portfolio – some Argentina, some oil, some Amazon, whatever – thinking that I'm actually diversified. When, in reality, it's all one trade, all one big trade.

And I think we don't need to go that far. I would ask investors – and I'm not trying to be clever or anything – I'm just saying, hey, how did your portfolio do in the last quarter in 2018? How did you do? Were you as diversified as you thought you were? Were you running more risks than you thought?

And the answer probably is that many have been caught into this perceived or artificial low volatility game, which is perhaps the most important anti-bubble in the system. An asset that is grossly artificially cheap, in volatility and the perception of risk, but also artificially low correlations.

So you have a portfolio that, for a while, looks like it has no risk, low volatility, low correlation. But when things go wrong, you get volatilities going exponentially higher and correlations increasing to +1 or -1, effectively resulting in exponential growth in value at risk and risk-adjusted measures.

What it means is you have this forced liquidation, everybody has the same trade, and this compounds. So I think this is a major concern. And I would actually urge investors to look at their portfolios and watch carefully for that possibility of only strikers and looking at their false diversification.

Now, if you look at the rest of the team, going back, some people told me, Diego, my defender is cash. And I would argue, keeping the football analogy, the soccer analogy, that cash is not really a defender.

Cash is a striker in the bench. You have money set aside, which you're holding there waiting for the opportunity to buy another striker. But it's not going to make you money necessarily. It's kind of there. And it works just like if you had a striker, if you leave him there for a few matches it's okay. You leave it there for a few years, you're going to have a problem with inflation.

And then we have what I call Beckenbauer. Those who are old enough and fluent enough in soccer will know he is one of the Michael Jordans, one of those amazing footballers from Germany in the 70s, a captain, a great defender. And he has done, effectively –

The German bund has been an incredible defender for the portfolio, but Franz Beckenbauer is now 73 years old. There is very limited room, in my view, with already 30 years at deep negative rates – well, negative rates – that it will have significant room for defending.

And this is a major problem, because this whole concept of 60/40 balanced portfolios, the idea that my equities, if they ever fall, my bonds are there with my 5% yield to protect me. In Europe, it's certainly not the case and, for that matter, in Japan.

And the thought that rates are going to go to -5 I think is ludicrous. I think you will see zero to -1 in the sweet spot of negative rates. I think Germany is more likely to borrow $5 trillion at -1 than $1 trillion at -5.

So what it brings us, just compounding the problem and putting it in perspective, is not only we were playing the game by the wrong rules, which is we think we only will win by scoring goals. We are playing with 11 strikers. By the way, many of them very expensive.

This mindset that you win by having 11 Ronaldos where that's not necessarily the case, with cash that is suffering from long-term inflation, and bunds that are suffering –

Obviously, in the US I think Treasuries have a role to play. They are arguably one of the very few markets in the world that has AAA dollar and room to actually make gains in duration. So I think Treasuries should play and have still room to play.

But it actually creates the urge for us to find defenders. To balance back those portfolios. And I do agree that gold has a big role to play.

But I'd like to elaborate on a couple of more people, because this is about educating the listeners and investors. And I think – again, I'm not in possession of the truth, but let's look at a piece of the puzzle that is generally viewed as a defender, which are trend followers, CTAs.

And so very often it is understood. They did well in 2008. But in reality, if you actually ask yourself, okay, what position is this CTA playing in the pitch? What am I asking this guy to do?

The reality is that we're basically telling the trend follower, hey, when I am attacking, go and score all the goals for me. In fact, in a situation like today, where markets, the trends have been very strong, where volatility is very low, effectively they're playing at the very top and they are all in and properly levered.

Unfortunately, when the team counterattacks, we're telling the players, listen, run really, really fast, put the gloves on and do all the saves. And then, by the way, when we attack again, go and run and score the goals for me.

What sounds totally stupid in the football pitch somehow sounds feasible for some people or rational in the portfolio. It is not.

Some of these perceived defenders are not currently defenders. In fact, they are pretty much the opposite. And I think this is important to understand.

Because sometimes in the industry you have a lot of frustration with, okay, I bought this strategy, I thought I had a defender and it turned out I had a guy in offside or a red card or whatever.

So I think in that sense the portfolio needs to look at strategies that are going to behave the way we expect them, the way they are meant to. And, in that sense, I am the goalkeeper of the portfolio.

I run a strategy that believes strongly in gold. It believes in Treasuries. But perhaps the key asset that will provide the very, very explosive and highly predictable payouts is financial insurance, is options.

And, here, I think there are tremendous opportunities to achieve what I would argue is almost the Holy Grail, which is artificially cheap premium with very low carry potentially, even positive, and very explosive returns when you need them. And this is part of the construction that I would look at clearly.

Before we get, perhaps, into some trade examples if you're interested, I would just complete the picture by saying be careful with credit.

Credit is an asset class that, in this end game where we are either going into a major blow-up or inflation, unfortunately credit is going to be bad in both. You will lose if there is a big credit event. But I really don't know what your 94 euros will buy you in 30 years with inflation kicking in. So those gains, those principle repayments that you will get in a long time with inflation, I think they are not going to do that much.

So if you want to play with strikers, I think selective equities will do better, at least in an inflation scenario. I think real assets like real estate, while they might look quite expensive, I think they have a role to play more in the midfield.

But certainly my focus and what I do is goalkeeping. And in particular I think these three assets (gold, Treasuries, and financial insurance) have a lot of value to add.

Erik: Diego, I can't thank you enough for a fantastic interview. Unfortunately in the interest of time I'm not going to be able to take you up on your offer to get into specific trade examples.

But for the benefit of our listeners who may want to follow up with you and learn more about what you do at Quadriga Asset Managers, please tell us first of all what business you're in and how people can contact you.

Diego: Thank you so much for the opportunity. It's been a pleasure.

I'm a portfolio manager. I run a series of strategies. I'm the goalkeeper. We have an offshore strategy with daily liquidity, which has the support from large institutional investors.

We are in advanced discussions and a process to launch also a US onshore solution. So in that sense what we do is differentiate it in the way it's constructed and likely to perform. And it uses those building blocks I discussed: it's precious metals, Treasuries, and financial insurance.

I am reachable directly on my email. Perhaps it's easier for people to look me up in Twitter and then I can link them up.

On Twitter I am @ParrillaDiego and at Quadriga Asset Managers I am diego.parrilla@quadrigafunds.es.

It will be my pleasure. We don't run retail strategies. We work at the accredited level. But certainly very happy to continue the dialog and the education, hopefully preventing some mistakes or potential accidents. And hopefully contributing to creating those large returns when we need them.

Thank you again for the opportunity and I look forward to continuing the dialog.

Erik: Okay, and for the benefit of the accredited investors in our audience who are qualified to invest in your funds, what is the Twitter handle and email address again?

Diego: Twitter is @ParrillaDiego and my email address is diego.parrilla@quadrigafunds.es.

Erik: Well thanks so much for a great interview. Patrick Ceresna and I will be back as MacroVoices continues, right here at macrovoices.com.