MACRO Voices
with hedge fund manager Erik Townsend

Julian Brigden: Hyper-Financialization Is The New Inflation

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Erik: Joining me now is MI2 Partners founder Julian Brigden. Julian prepared an excellent slide deck to accompany this week's interview listeners. You'll find the download link in your research roundup email. If you don't have a research roundup email, just go to our homepage macrovoices.com. Look for the red button above Julian's picture that says, looking for the downloads.

Julian, it's been a long time. Like last time I spoke with you, you said something nobody else was saying, which is get ready, put your seatbelt on inflation is gonna get serious. And everybody thought you were crazy. What has happened as one of the people who saw this coming, how has it played out? And how's it gone differently perhaps than you were expecting?

Julian: So, I mean, to be honest, it's been more powerful than we thought. And more persistent than we thought. We wrote at the start of 2021, the first report, we wrote, I think the fifth of January or something 2021, that inflation would be the most important variable of the year and indeed, it was. But kind of we got to the beginning of '22 and end of '21, we were expecting some base effects to kick in. And then just things continued. And I think the problem is Erik is that we've started this process, should I think of sort of non-linearity, right? I mean, the world, we're very used to a world, companies, central banks, and it was interesting listening to the Sintra conference where we had Powell, Bailey, and Lagarde on. And it's really worth listening to, if your readers can listen to this. You know, they talked about the world structurally changing now, right? Structurally changing. And I think, we're so used to as market participants since the Great Moderation started in the mid 80s, this kind of period of relatively benign, relatively predictable, relatively forecastable, if you want to call it the nice sine wave around the long term trend of economic growth, where, your grower kind of two and a half and central banks come in and cap a little bit and we roll over to sort of half and then they cap it a little bit on the bottom. We kind of stay in this is predictable. So this increasingly volatile world where things just don't respond in the way that you had thought, right?

And even we who said we were extraordinarily aggressive on the inflation story, we're caught out by just how powerful these forces appear to be, because base effects should have started away on inflation starting really at the end of the last year, and didn't and so something else is totally going on. So then you have to sort of step back and go what is it? So is it companies just deciding after 30 years of never being able to push through price increases to go like, screw it, now we can jam through it? I think there's an element of that, right? Or is it just all these normal relationships that we assumed that would happen? Break down? I mean, there's a great chart. So as you can see from the next slide on page two, you can see this excess stimulus model, where you look at the breakout of inflation, right? And you can, you can take this thing back to 1926 I think, that's quite a long time, not even you and I have that old Erik. And you look at a range of typically inflationary tops being between max between like 5.4 and 6.4% base CPI in the US. If you break that, the lowest next print that we saw, was 9.4. And the average was over 13%. And there's been very few periods of that Erik. But the point is, it's material, right?

So things have just totally broken down and the world isn't acting normally. I think it was I said, I think that Sintra conference call was hugely important. Because all three central bank governors, all acknowledged that this concept that we are necessarily returning back to that nice benign world where you had globalization, high productivity, all of those factors weighing continuously on inflationary pressures, maybe over for quite some time. And I think that is material. So look, I can see some signs of benign inflation or should we say, peaking inflation, okay. In the US some, but I think there are, I don't think it's necessarily the case that it's a guaranteed and in fact, we've got some models that suggest and maybe I'm being a bit too cute, but they go back to the 1960s. But if I look at the size of the stimulus, and I think this is really the key point here, and you can look at that the next slide, and you can see that. You can see that if I look at the stimulus and the size, it was five times bigger than anything that we've seen in postwar history Erik and it suggests when you use it to try and forecast inflation, it doesn't see a peak until Q4. Right now, I don't want to get too cute on this. But you can see it's actually measuring what they call detrended core CPI. So is looking at the change over running baseline. So in actual fact, that peak is where it shows sort of five or six on the right hand side of the screen is actually a nine and a half. But the point is, is even if some of these other factors start to weigh in, I think we're looking at extraordinary inflation pressures and high sticky inflation pressures, probably well into Q4. And the implications for other assets are pretty damn clear, I'm afraid.

Erik: Julian, I was expecting you to tell me that inflation was going to be the really big thing to pay attention to, because I know you've been on top of the inflation story for a long time. You actually told me off the air that hyper financialization is the thing to keep your eye on. Okay, what's hyper and what.

Julian: What's hyper financialization and call it what you will but financialization I think Is this painful situation that we have in the US. And there's, I think, a couple of factors behind it. But I think the, you know, in a way, it's an epitome of extreme capitalism. We've moved to this situation Erik where company CEOs are no longer paid to produce anything right? They weren't actually until recently paid even to produce a profit. I think we might have all seen that meme going around, where I think it's from that great HBO series, what they did on Silicon Valley, where the guy's like, well we're going to make a profit and the venture capitalist guys like: Don't you dare! Don't you dare make any revenue, right? So the, anyway, the point is CEOs are remunerated just simply to do one thing. And they are shepherds of a stock price. That's the job.

The job is to 10 the stock price, drive the stock price higher. That is it. So the problem is that when the stock price starts to fall, it elicits a response function, whether it's in terms of employment cutting, and we've seen signs of that already, right? We've seen all these, these sorts of long duration companies that you know, sort of the names that were in, peace of mind by like Cathie wood and her fund started to lay people off or cut back hiring. And the other place, you typically see that manifestation come through is in capex. So what tends to follow is that as we start to see these things, the next shoe to drop, and it's, it's strange, because this is one of the best economic leading indicators we can use are the PMIs. So you would thin Erik, that in a world where you asked the question, which comes first, the chicken or the egg, right, if you think of it in economic market terms. I mean, really, the chicken should be the real economy, right? The real economy should dictate the level of corporate profits, the level of inflation, and those should feed through into equity markets or bond markets, etc, etc. That should be logically how this thing happened.

It actually isn't. It's actually the chicken is the equity market and egg is the real economy because of this feedback loop between the behavior of CEOs. So what's happened is that once you bring stock prices through tighter financial conditions, which Jay Powell has explained to us is how monetary policy works for the system. And old macro gets like me and you all along, it starts to elicit a chain reaction. And I think the next chain reaction that we're going to see is a significant drop in the level of some of these confidence metrics, things like the PMIs. We've got ISO manufacturing on Friday. And I think people are going to be shocked at the imminent risk of a recession because I think we are moving rapidly to that point. Right. In fact, if you we have a chart that we look at, you can see on slide three, this slide here, it shows you corrections in the S&P, and while we aren't there yet, right, we have not dropped 30%. If you go back and you take this chart back. And you can see it goes back 90 years with the exception 1987, which Erik, I know you were and I were both around for. Maybe in our very young days, but we were around four, which was really not a bear market per se, it was really a function of market terms, you'd call it a negative gamma kind of Flash Crash, caused by this misheld belief in portfolio insurance. So they can synthetically create kind of puts, until it didn't work, and the market crash, but it was really more of a flash crash, it wasn't really a true economic bear market and it corrected quite quickly. But with the exception of ‘87, every single 30% decline in stocks has given you a recession. And the problem is, once you get to that 30% down doesn't mean you stop at 30% down, because then it's a function of how bad the recession is.

Erik: Julian, I want to go back to that point you just made of it doesn't mean you stop when you get to 30% down because I keep reading more and more commentary, where people saying, well, it's unclear as to whether the bottom is in, or maybe there's just one more flush down and maybe 3600 on the S&P, but it can't go any lower than that, then it will be all clear. I'm sort of like, why do you think that? Why can't it go lower? And what am I missing?

Julian: No, I look at some metrics Erik, and I think there's a lot of validity in them. You know, two that I tend to look at look at the VIX. And then I look at the, its a little bit more complicated the cross correlation between stocks in the S&P, right? So if you start with the VIX, and you can see that on slide four, you can look at if you look at this to the history of the VIX, it's a bit of a strange beast, in that it tends to sort of trade in bands. Okay, it tends to trade in four bands. And those four bands, if you kind of look at them, let's take band one, you know, it's almost the inverse of I can ever get this one, right defcons, right? So, you start off in band one. And that's kind of between 10 and 30. And that's completely normal. Okay, you move into band two, and two is sort of 30 to upper so lets use 37-38. You move to band 3, 48 to 53 on the top side. And then you go into move band four, and that's kind of Armageddon. And if you go back and you look at the last 30 years, there's only three occasions actually where we've gotten the band for the two bad ones, obviously with the global financial crisis, COVID, and then the bund tantrum actually interesting in 2015, where bond yields doubled or jumped 1% from zero. The other ones though, we tend to your point Erik we don't seem to see that sort of cathartic, blow off move in vol and bottom in the market until at least you've got into band three, right? Where you're pushing that upper 40s to lower 50s kind of level.

And then you've got things like, *volmageaddon*, the end of QE1, but you can go back into the sort of height of the dotcom crash in 2001 and 2000. And then the broader market in 2002 right? We have not even got into the bottom of band 2, 37-38. So to me, that just tells me that the pros have been extraordinarily well hedged. Right, extraordinarily well hedged. The second one is this cross correlation between stocks in the S&P and that's kind of important because the higher the correlation goes towards one, the more and more difficult it is for long-short equity hedge funds to balance their book, like because when correlations go to one, the reason that we've hedged, everything is going down in the same direction. So typically, at sort of market bottoms, you tend to see correlation vols in like 70 to 80, maybe 90. Once again, we're not even close. So I kind of look at this, and I think, boy oh boy, you know, people may be very bearish, but they're either hedge or there's is another element, which is what I really fear. And that is the pros are bearish. But they aren't positioned particularly that way. And retail sure as hell isn't positioned that way. Because they've just been told over the last decade, buy the dip, buy the dip, buy the dip, buy the dip, and most recently, that you know, bonds are trash in a inflationary environment. And so I'm fearful that we just don't have the conditions for a low and the really what has to happen for that those conditions to come in is that retail has to be taken to the woodshed and shot through the forehead.

Erik: And does that mean that that's coming and if so, what would be the catalyst to bring it about?

Julian: I'm fearful that it is coming. I am fearful that it is coming because I don't, you know, to go back to that financialization argument, Erik right. If the Fed is intent on slowing the economy down, which they are, and Powell needs to see, he doesn't want to see it, but he keeps giving those subtle hints, may require, you know, we might have to see pain, right? Then he's got to tighten financial conditions. He's explained that. That's how monetary policy sending signals to the economy. And the one element that still is really high and sort of isn't contributing to that real tightening of financial conditions, because it's the sort of five metrics in a financial conditions index, roughly. So the short term interest rate, long term interest rates, the currency, credit spreads, and equities. The one bit that is not pulling its weight still is stocks right? So if stocks don't go down, stocks try to rally, then the economy, because of that financialization probably won't slow down as much as you think. And then the federal have to keep pushing on rates until stocks get it. So one way or another stocks have to go. And I think the next shoe to drop on stocks is earnings right? We've seen a P rerating as bond yields have risen, the discount factor has risen. I think the shoe that has yet to drop is the earnings downgrade. And I think that we'll start to realize, people start to realize that when we start to get this acceleratively weak economic data, which I think we're on the cusp of seeing a good start as soon as Friday with these ISM manufacturing.

Erik: Julian, I want to run a hypothesis past you that a listener sent me because I've been saying that very similar to what you just said, which is, look, we've seen a very orderly sell off so far. We haven't seen the panic, we haven't seen the fear. We haven't seen the capitulation. What a listener sent me was a very interesting thought. He said look, maybe what's going on here is when you see those things, that's the less experienced, younger retail investor panicking. That's the reason we're taught to look for those things. Maybe we're looking in the wrong place, because what younger, less experienced retail investors invest in these days is crypto. And guess what crypto is showing plenty of signs of fear, panic, and capitulation. So could it be that the reason we're not seeing fear, panic, and capitulation in the stock market is because the demographic which is vulnerable to having that experience is in the crypto market instead?

Julian: I think that's fair. I think that's fair. So I think that is you've taken those guys out and you've shot right, but they're the millennials, right? They control a fraction of the wealth. Who controls the wealth Erik? The boomers. They have not been trading crypto, what are they trading? They're trading stocks, how they trading stocks? Well, if they're wealthy, they've got a registered investment advisor. Like they got a broker. A broker has told them to get out. Those guys haven't been trained to tell them to get out. Right? So it's when these guys and I can tell you in conversations I've had with wealth managers, and private family offices. They are all gagging for a rally. So they can try and get out. No one saw this coming. No capitulation. Now, maybe they don't capitulate. But it's kind of hard to see that because a lot of these guys are coming up to retirement, right. So you got to imagine, if you got a rally that they'd be sellers on a rally. Right? Same as pension funds, right? I mean, if you're a pension fund, and you just got given, you just caught the Hail Mary pass because you are underwater in terms of your funding equities have risen. And now and you were long, a lot of equities, and now you can go and sell those equities and go and lock it in decent bond yields. Wouldn't you do that? So I just think, minimum, there's a hell of a lot of supply on the top side. Worst case, they just haven't capitulated yet.

Erik: You mentioned bond yield so let's move on to that because, you know, with this inflation situation, a lot of people are saying, okay, seems like Jay Powell wants to be the new Paul Volcker. So we're headed to 20% interest rates. But wait a minute, Paul Volcker said before he died, that that approach that he took in the early 1980s would never work today, because we've got so much more debt to contend with. So what is going to happen with respect to bond yields? It seems like the prescription here is increase treasury yields as much as possible to fight inflation. But now we've got a situation where increasing those treasury real yields could crash everything. And I guess the corollary to that question is, where does it leave high yield?

Julian: So I think, yeah, I mean you're right. I mean, we're not going to get rushed back to Paul Volcker type levels. And it doesn't mean that we can't do say the damage that Paul Volcker did. But I don't think, you know, my analogy is we're not really in the 70s yet because of the dollar. That was the real thing that drove the extended inflation that we got. But people forget that the real inflation that led to the 70s started in the late 60s. And that's kind of where I think we is much more analogous period historically. And back then the Fed was trying to do their best to try and fight this inflation. And I think Jay Powell, he told us, his intent to try and do his best he's, you know, to use that space girded his loin. And he's prepared to fight to do this. And he made it as did Legarde and as did Bailey, they all made it very, very clear on this video call this morning on this conference that they spoke to this morning to the ECB, that the biggest risk was not the pain. The biggest risk was letting inflation get out of the jar, kind of thing that's a bit late.

So there's a big difference, though, right? There's a big difference what central banks say and what markets price. I mean, the market has been much more aggressive at pricing in rate moves than the Fed and the Fed, I think all the other central banks, and it's part of the game, right? You kind of hope that the market does a lot of your work for you in using forward guidance. And so maybe at the end of the day, you don't have to fully deliver that in terms of actual rate hikes. That's how tightening financial conditions works. And we've seen that so bond markets really kind of priced in an awful lot. The question is going to be though, what happens next? So if growth, as I said, I think inflation is certainly going to move higher in the Eurozone, I think in the US, it's going to be at best sticky, maybe even still slightly higher. That's going to make things very difficult to balance, I think it's going to make things very difficult for the central banks to back off. But if you start to get materially weaker data in terms of growth Erik, what the bond market is going to start to do is go aha, okay. I know you say, you know, which is where the Fed is that the terminal rate, the highest rate that rates are gonna go okay is 3.8. You're not getting there mate. You're not gonna get there, because I know, I can smell already. But by the time you get anywhere close, you'll have shanked the equity market, and the real economy will be down the plug hole okay. So the market, I think is starting to bet on that. And you can see that really at the front end of the bond market, right, in kind of the two year, Euro dollar sector, two year yields. That's what the market is beginning to smell.

And that's actually what typically happens Erik ahead of a recession. Okay. So, I know a lot of your guys are interested in the equity market. But please, please, please, never listen to an equity guy pontificating about the bond market, because they wouldn't understand it if it bit them in the ass okay? You constantly hear things on CNBC. When guys go, these commentators who aren't even market participants, they're journalists in most cases, saying things like, oh well, you know, the curve inversion is a sign of the bond market pricing in a recession. So in other words, two year yields are higher than 30-year yields or 10-year yields, right. That's the inverted curve. That's totally wrong. The curve inversion, particularly in that in this type or this point in the cycle is the bond market, anticipating central bank hikes, okay. And longer term yields either fall or remain anchored as those front yields move higher because central banks are moving to deal with inflation, I don't have to be that concerned about my yields further out, because I know the central bank is doing the right thing to maintain the value of my bonds by tackling inflation. But what actually happens right before the recession is actually called the bull steepener. The bull steepener is a bull market move because the bond market is rallying, yields are falling, okay, is when two yields fall relative to the long end. So the curve steepens, but it's because bond yields at the front drop, and that's where the bond market as I said goes through that guessing game where they go. I know what you think you're doing Federal Reserve or ECB, you think you're gonna get rates to this level. You're not because I could already see the cracks are starting to form in the economy. And so that's where I think we're at that phase. I think it's still difficult because of this background inflation. But if the data is sufficiently weaker, which I fear it's going to be, then the front end of the bond market will start to look through the inflation data and go look. At some point, I know even if it drags on for another three to six months, this inflation will wane because we'll be in a deep, ugly recession. Okay and I know that central banks never gonna get there.

Erik: Julian for most of the 20 teens, I kept telling myself that the trade of the century when it was time was going to be shorting junk bonds. Except I tried too many times too early and lost money each time. Is it finally time to short junk bonds?

Julian: It's kind of difficult because of the tools that you have available. So in late November, we put on a trade in HYG. And it was a put spread on HYG. We said it was a super, super cheap hedge. And it was, and it was a blowout trade area coming out. We got it in on incredibly, incredibly good levels. Thing was barely off the highs. And the problem is that that's probably the easiest thing to trade. And it's moves a long way. Right? It's moved mostly on the back of duration. So in other words, the bond market move, because it's been very, you know, credit bonds or high yield has two elements has the duration element, just like a regular sovereign bond. And then it also has the credit spread. I do think that there's now a significant risk that the credit spread component Erik starts to move. It's quite difficult to play that, given how much HYG has already moved. I mean, there's some you know, these other things you can start to play. I just think at this point, the better trades you slot equities.

Erik: Now inflation has moved exactly as you predicted it, what surprised a lot of people is precious metals, gold is really languishing here. We haven't seen a big move up. We got the geopolitical pop when the war broke out between Russia and Ukraine. That's pretty much retraced now. As we're speaking on Wednesday, we're just moved today below all of the cluster of moving averages, charts not looking good. How can that be when inflation is such a problem?

Julian: I mean, precious metals are not really a hedge on inflation. And they're non yielding right? So they're not really a great inflation hedge. What they're really good hedge on is lack of central banking, which often goes hand in hand with inflation, but at the moment isn't. I mean if you look at gold, it tends to be inversely correlated to bond yield. Right, and got a tough central bank here. So, it's a tough one to own in that kind of environment. I mean, frankly, I think it's done remarkably well to hold in as well as it should. I mean, if you look at the move in, you can see that in five, if you look at here 10-year yields against gold, you can see that really, gold has held up remarkably well. It's inversely correlated has been since oh nine very closely to those bond yields. Held up remarkably well in this move and bond yields from like one and a half to three and a half at the highs, right? To be honest, it probably should be down at 1400 bucks, all lower. So it's done well and I think that's because there's other you know, non-economically sensitive buyers coming through.

But when precious metals do remarkably well, is when the dollar tends to weaken. Right? And the dollar won't weaken until the Fed is forced in a corner and has to capitulate on because either we've got super deep recession, and bond yields or high, relatively and they are forced to come in and kind of save those two bits of the economy. It's this dilemma which we think we're coming to face, which is basically called the impossible Trinity in economic terms. You've got three variables. In this case, it's the equity market, the bond market, and the currency. Which two do you save? Because you can't control all three. Right? We think the Fed if we're right about this next leg of the equity market falling Erik, let's say we do dotcom type burst, you know, by the time this thing is down, it's down. The S&P is down 30 plus percent, the NASDAQ is down 40% or worse, or worse. You know, bond yields are say very sticky still, because we still got that background benign inflation. And that's not inconceivable, right? Remember guys, we've seen this before.

If you look at slide six, you'll see a period where in the late 60s bond yields rose, and stocks fell. right can happen because inflation is rising. But I think, at some point the Fed will capitulate, they'll have to. When they do, that's when I think the dollar goes, We're not there yet. But when that happens, that's when you really load up on precious metals and particularly silver. It's just as I said, it's really a precious metals and not so much as an inflation play, not when the central banks are trying to be tough to address it, when precious metals come to their own is when you've got weak ineffective central banks or central banks that are forced to make unpleasant choices, where they're looking at these three variables in which two do they save. Not there yet.

Erik: Julian, I'm tempted to ask you, okay, what's the magic number on the s&p where you start buying? Because the bottom is in, of course, most of our listeners are smart enough to know it's not quite that simple. But let's talk in terms of analogues to other bear markets. What are the signs we would look for? Or how would we tell when the bottom really is in or approaching? Because it sounds like you and I both agree, we're not there yet. How do you know when you are there? And how do you know when it's time to start buying?

Julian: So I think, as all those other various signs that we talked about, like the capitulation signs, Erik and I think, you know, we'd sort of agree that basically we aren't there yet. I think, the other thing is to look at analogies in history, and I think the one that was that is most close to this is the dotcom bubble, right? And the reason I say that is I think we've had one of these periods of what I would call exceptionalism. They happen kind of all around the world but the US is typically prone to them because it's the reserve currency and that's periods where you get currency strength that are associated with equity market strength and equity market outperformance. So, if you kind of look at the US from sort of 95 to 2002, you had a period of dollar strength and a period of relative outperformance of the US equity market versus the rest of the world. And that obviously led to the dotcom bubble. And the reason for that is very simple. Foreigners basically get two for one, right? It's a classic to first trade, right, you can buy the currency and you can buy the equities and both of them outperform.

And this one has actually run arguably twice as long really started in 2011 with earnest since 2014. And once again, this incredible powers sucked in money into the US and it truly is reflexive in that kind of Soros sense of the word Erik right whether purchase of the asset actually leads to an outperformance and underpins the performance of that asset itself. So it becomes self perpetuating until it kind of isn't. So I think that that relationship needs to start breaking down for us just to have a chance to see that this is over. But if you look at dotcom period, the important thing to remember is that whole process took time to burst Erik right? So we kind of burst the NASDAQ in March of 2000. The S&P pretty much held in until September of 2000. And then the Dow really until May of 2001. So a full 14 months after and if you know, and I know this probably will have upset some of your listeners, hopefully they will have taken some lessons from it. But I constantly tweet about Cathie wood, right? I mean I think you know, she's been a horse for a single course. Right? She's done, she did exceptionally well in free money and playing long duration stocks. And I do not believe that her fans will come back for a number of years. And I don't think you're gonna see your money back at the highs for a decade. But the chart pattern, and I'll call it that where you compared the price faction of Cathie Woods fund, and you can see it in in slide seven. You compare Cathie Woods fund, against the NASDAQ in 2000. Miss the same chart, Erik, I mean, it's literally the same chart. So if you say Cathie Woods fund was that and that burst in February of last year, right. It's about now that you should be expecting to see the weakness in the equity market. And we have, like, the question is, how far does this run because in 2000, these corrections were brutal made. I mean, you remember this? I mean, this was not a 30% when we're all done, walk away. You know, that's great. That's fine, right? I mean, the NASDAQ dropped 77%. It didn't base until two years later, the S&P dropped 72% and even the Dow which was the big market back then dropped 56%.

Julian Bridgen I mean, I think arguably this market has gone on for twice as long as those, I think, the dynamics are hugely dangerous. So I'm in no rush, I don't think you have to be, as I said, with this inflationary backdrop, I think it's gonna be very difficult for central banks, even if growth starts to stumble, it's going to be very difficult for central banks to say they won't stop if growth goes weak enough, but to come in with another bout of QE or something, right, or to give you rate cuts, I think that's going to be very very difficult to do. And I think the risks are of a growing of a very ugly recession, potentially because there's financialization on the back of that. And so I'm not saying that we're gonna go down 77%-72% on the S&P but 40% isn't inconceivable, Erik. And that's why I don't think you need to be in a rush, because the only reason why you need to be in rush last decade is you were trying to anticipate a Fed coming to your rescue. That was it. But you've got those big sharp bounces. But often, equity markets aren't like most of the equity market prior to a world like that, right? I mean, you least had six to eight months where the market kind of stabilized. Right and then started to move higher. I mean, the NASDAQ made its slow in October of 02, right? It was pretty much unchanged for another year. So you had plenty of time to kind of think about it, there was no V-shaped bottom. So I just, I don't know whether anyone needs to be in a rush right now.

Erik: I just want to interject for anyone who's not familiar, Cathie Wood is the manager of the ARK funds. She's known as one of the biggest cheerleaders for stocks like Tesla, and other companies whose new paradigms and in her analysis mean that they don't necessarily need to have the types of earnings that are normally associated with profitable companies and so forth. I was trying to be gentle, what are you laughing at?

Julian: Take a step back and you actually listen to that. It is and you're absolutely right. That's her monologue, right? But it's a bizarre monologue to convince you to put money into something right?

Erik: Well, it sounded good to a lot of people when those stocks were going up. She was saying, don't worry about earnings. It's a new paradigm. It's a different kind of system. You don't have to worry about the old normal. It doesn't apply here, because it's a different kind of company. And that worked for a while, didn't it? She made it did work.

Julian: She did extraordinarily well right? It's just cynical old bosses like us have seen it before right? We heard the same thing in the dotcom bubble, right? Don't look at this. You know, look at it against revenue, look at it, x times sales, look at it this, right?

Erik: If that doesn't work out, we'll just make up for it with volume. That was my favorite one. Let's move on Julian, final question. First of all, I'm with you. I don't think this is over yet in the equity market. I don't think there's any reason to rush in and start buying the bottom because I don't think we've seen the bottom yet. But hold on. You're saying it could be quite a while. So what do you do to make money now? Where is the trade? It sounds like you're saying it's a little bit late to get on the short side of this market. What do you do?

Julian: Well, it is not necessarily too late. I mean, if we're right, we still got in percentage terms a lot further to go, right? So if you've been sitting here, and that water started to feel a little hot, doesn't mean you can't try and raise some cash, remember! I mean, unless you're getting new chunks of cash in, you need to have some cash to take advantage of those lows, right? That's the fallacy of a lot of brokers right? They say you can't time the market, which is bizarre, because there's a whole bloody industry that does it, and does make lots of profit out of it. And then they said, because you'll never get back in well, the trick is, obviously to get back in but, you know, they're the ones who are incapable of telling you to get back in, not you. So I think as I said, I think there's potentially Erik some opportunities to be had at the very front end of the bond market. The kind of two years. But I really really don't think so that it is wrong having cash for a while. I mean, I really really think it's important to have cash.

Erik: But you are Mister inflation Julian... Normally, cash and inflation...

Julian: Sit with it for six months, right? And you get 5% erosion.

Erik: Or you could buy sriracha sauce with it!

Julian: Yeah! Let's say you put it in two year treasuries and they don't go down, they don't go up. You earn 1% and then you've got erosion of four. Okay. We've seen those intraday in the NASDAQ really? I mean, you can't take that. I genuinely think you can. I think I mean, I would say, maybe corporate high yield. But as I said, I think the next shoe to drop for that is actually the credit spreads. Credit spreads are pretty tight actually. Credit spreads are remarkably tight. If you take something like triple C's against B's, Erik, they about 400 basis point. If we're going into anything close to a real recession, right? Let's say ISM significantly under 50. Those things should be 600 basis points. So I can't even tell you that I think there's an advantage. I mean, I really think at the moment, I mean, precious metals aren't bad, they're not gonna go too far. I don't think that, you know, gold is quite heavily owned, but it's got a bit. Silver, I think, could come down a little bit. It's not going to go down as much. I think, personally I'm long quite a few things that I want to be long but I have shorts against them. And the reason is simple. This is if you go and you look at that and you know, look at slide eight, this is a final slide, you'll see the growth/value S&P chart, right, going back to dotcom period. And you can use anything I mean, this is S&P growth-value, but you could use US-emerging markets. You could use tech- mining, metals, energy. Whatever those ratios, they're all basically the same. Tech, the US growth has utterly outperformed the rest of the world, just like it did into the dotcom bubble.

Now, I think we're halfway through the correction in that ratio. But as you know, Erik, ratios can correct one of two ways. Okay there's the nice correction. All right. So let's say US tech goes nowhere and mining metals, Europe, emerging markets, you know, energy rises, right? So the ratio corrects, the nice way. And then there's the nasty way. And the nasty way is everything drops but just tech drops the most, the US drops the most. The problem is like, this is like I always love this one. This is like the fund manager who says to you, I beat the index. He's like, oh great. Yeah, the index down 20 and im down 10. Cheers mate, you just lost me 10% of my money right? That's the problem with the nasty phase, right, and the nasty phase persists until the central banks blink. That was the lesson of dotcom bubble until the Fed blinked and the dollar started to weaken, initiating the next raise wave of inflation and reflation. You got the nasty correction, I think we're in that phase. So unless you can shut hold ratios, where you're long this and short that. And even that can be difficult. Cash is not a bad thing. I mean, I want to buy silver at some point, I think I'm gonna get it probably in the mid 19s in a blow off, because I don't think it's very heavily owned Erik but it's owned. And when you get that VaR event, right? We talked about that big spike in vol, the big spike in cross correlations, where everything just pukes. Even the stuff that you want to own is going to go down. So cash is fine.

Erik: Well Julian, I can't thank you enough for a terrific interview. But before I let you go, I want to talk a little bit about what you do at MI2 Partners. Now you cautioned our listeners earlier in this interview, not to let guys that do nothing but stocks try to lecture you on the bond market. You have for decades now been an institutional macro advisor talking about the big picture of all of these asset classes. Give us a little bit of a sense of what you do there and how our listeners can follow your work.

Julian: Right! So MI2 Partners has been around now for 11 years. So we survived that threshold of 10, which is you know, kind of the last point where companies, startups tend to fold if you make it past that age you're pretty much golden. So fingers crossed. And you can visit us at mi2partners.com. You can express your interest if you want to see the research, there's ways to sign up or you could just reach out to support@mi2partners.com. And then we have as you've talked about in the past Erik, this joint ventures we have with Raul at real vision called Macro Insiders. And we shoot the shit with each other basically once a month and we send institutional research to clients. And we've made different types of that. I think it is hugely important for clients, but many times we start to agree and now it's kind of one of these times we're getting a bit closer. And there's actually a special on at the moment so I think if you go to the real vision site or they look on my Twitter which is the other way to follow me. So if you don't want to pay for anything and you just want to follow the freebies @JulianMI2 on Twitter and I'm also on LinkedIn if you prefer that. But yeah, that's kind of how you can follow us. And we don't just want to pontificate Erik, we try and pay people money right. We are not just an economist by any stretch of the imagination. We try and get real trading profits.

Erik: Patrick Ceresna and I will be back as MacroVoices continues right after this.