



MACRO Voices
with hedge fund manager Erik Townsend

Marko Papic: Investment Implications of Geopolitics Around The Globe

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Erik: Joining me now is Marko Papic, partner and chief strategist for [Clocktower Group](#). Marko is a geopolitical expert, and that's what we're going to focus on. Marko, obviously, we used to say, well, everything that's on everybody's mind is Russia/Ukraine almost seems like it's been forgotten in the wake of Israel/Gaza. But let's start with Russia/Ukraine, is the intention of the US and the EU to kind of push this under the rug and tells Zelenskyy it's time to negotiate, or is that an incorrect message?

Marko: You know, that's such a great question. And first of all, I just want to thank you for having me on the show. It's a great question because it gets right to the heart of what I do for a living. And the framework that I employ, to sort of generate geopolitical alpha for investors. No, it's not in their intention. It is not preference, I think the preference of the European Union, various member states in the United States of America is to continue to push against Russian attempts to expand the sphere of influence. But preferences of policymakers are not diagnostic. They're not relevant for investors. They're not relevant for us as analysts, what matters are material constraints that constrain policymakers from getting their way, from getting their preferences. And this is why, I think that the entire industry of geopolitical research or geopolitical analysis that tries to convince its clients, many of them in the asset management industry, that getting closer to policymakers is the way to generate alpha. In other words, I will tell you what I heard at a cocktail party in Washington, DC, and then you'll make some money off of it. That entire business model, I think, doesn't really make sense. Because both politicians and policymakers, they don't get what they want, they don't get to pursue their preferences. And the reality on the ground, is that there are severe material constraints for continuing this conflict on both sides. By the way, we can talk about what the constraints are on Russia's side, being pretty incompetent in war might be an obvious one. But from the western perspective, I mean, what you're seeing is a real turn in terms of political appetite, by the median voter, in both Europe and the US to continue the endless conflict in Ukraine. And I think that that's a real big risk to the policymakers in Europe, in the US in perpetually continuing to support Ukraine, in its attempts to recover the lost territories to Russia. And so yeah, I would say that we're at the end of the line. And I think that over the next 12 to 18 months, the pressure on Kyiv to negotiate some sort of a ceasefire is going to increase, not a peace deal. I just want to mention that before you follow up, because I can probably guess that you are going to ask me that I don't think that anyone will ever be able to convince Ukrainians that, you know, to sue for peace and to give up these territories. But there are ways to avoid having to do that, we can agree to

disagree for a very long time, in terms of territorial arrangements. And that has been the case in many conflicts around the world that did end.

Erik: Well, let's come back to what you said about material constraints, because the political sentiment until recently, was: look, until the end, no matter what it takes, keep on sending weapons, support equipment and so forth to Ukraine. Now, one side of this is that that political sentiment or the public support for that is waning. But it seems to me there's another side of that, which is, although you can print more dollars out of thin air, you can't print tanks, and missiles and so forth, they have to be manufactured. And obviously the defense industry is going to benefit from having to replace the ordinance and so forth that have already been used up. But what about the ability of continuing to support this war? Do we have enough stockpile of weapons and bombs and missiles and everything to keep doing this? Or are we at a point where we're already risking the US and European national security by using up so many of our own weapons that we don't have enough to defend ourselves and something else happened?

Marko: Well, a lot of great points that you brought up, and it is that is indeed a material constraint. Now, first of all, I don't think you're risking US security. You know, unless Canada and Mexico decide to engage in a land war, the US is probably defending its security by engaging a strategic rival like Russia and land war far, far away. So as far as I'm concerned, it would probably make sense to send 100% of stockpiles over to Ukraine and the US will be fine. The issue is that you do need to engage the defense industry, and you need to incentivize them to produce more because we're already running out of not all weapons systems, but some certainly, we are beginning to run out. And so the issue is, why hasn't that been done? And the answer is that, and this is not a politically correct answer, and I'm going to anger a lot of people by saying it. But the truth of the matter is that Ukraine is just not that existential to the West. It just isn't. And I don't say that because of what politicians are saying in the press. But because of their behavior, clearly, Ukraine is not existential to the West, because clearly, the defense industries of the West have not been ramped up the way that was done, for example, in WWI, WWII. And let me maybe make it more specific, independence of Ukraine may be existential to the West, but that was already gained. In other words, that was already accomplished, effectively, March of 2022. Within a month of this conflict, the Russians effectively acknowledged the day of lost, their initial foray into northern Ukraine. And they withdrew on March '23, they basically, you know, a month after the war started, they said, Oh, we accomplished our first phase of the war. No, you didn't, you're just saying you're lost, and you're trying to put a face on it. So basically, within a month of this war, what was existential to the West was accomplished, which is like we will have an independent Ukraine that will not be controlled by Russia, there will not be some puppet government.

And so now the conflict is over something else. It's over at the Oblast in the east, which are populated mainly by Russian speakers. Donetsk, Luhansk, Kherson. and of course, Crimea. And Kyiv's control over those Oblast, over those states, is just not that existential to really anyone other than Ukraine. It's optional, it's a luxury. And that's why you're not seeing the ramping up of defense industry to prolong this war to let Ukraine "win," because as far as the West is concerned, and by West I mean, like Italy, Germany, France, United States, Canada,

the West has already won. Ukraine is independent, Moscow doesn't control Kyiv. And so now, it's much more of a luxury to continue the conflict for territorial integrity of Ukraine.

Erik: So what does this mean for US defense industry? Obviously there's a lot that's already priced, and it's a little bit too late to go buy defense stocks, because you heard about a war in Ukraine. What should we expect next? And what are the investable, actionable strategies that we can pull away from this Russia Ukraine situation?

Marko: Well, at the end of last year, I told our clients that they should definitely invest for the long term in European defense industry. I think that's the one that is going to ramp up because I think you will see continued expansion of European defense budgets. I think Ukraine was a watershed moment from that perspective. And some of the biggest gains in terms of market performance were in Europe and their defense competence. And so I think that is, is that fully priced in? Not necessarily, I think there's still a lot of doubt whether European countries will be able to boost their defense spending as percent of GDP, I actually think it will happen. And I think that Europeans will be quite protectionist about how they do that. So this idea that they will continue to do America's bidding as they did during the Cold War, by buying American defense systems, I mean, that's just not going to happen. And so I think that if you're looking for an opportunity, that some sort of long term geopolitical beta, I think that that would be the play here, not American companies, but European ones.

Erik: And where do you see this conflict in Ukraine going from a resolution standpoint? We've heard initially, a bunch of reports that said: Okay, it's time for the US and EU to kind of push Zelenskyy to the negotiating table, make a deal, come up with some kind of truce agreement, put this thing behind us. But then just in the last week or so I've seen a couple of statements out of US policy makers saying no, that's not our position. We are staying with this. It's going to continue. But as I go back to your material constraint thing, I don't see any political will to send US soldiers put US boots on the ground and put American lives at risk there. I hate to say this so bluntly, but it seems to me that Ukraine has already almost run out of fighting age men in their own population, unless someone else is willing to send boots on the ground. I don't understand how this war could continue any further than it already has. Am I missing something there?

Marko: I think in the US, look, the big story here, you know, and I know we're going to cover this today, is the US election. So you've got basically 11 months left to supply Ukraine with enough material, because there's a pretty high probability that there is 180 degree turn in US policy after November 2024. In my view, Donald Trump is the front runner in this election. And his probability of victory is probably underestimated at the current juncture for a number of different reasons, including the strength of the US economy at this moment. And so, if you're a Western planner, you cannot ignore American election. And so you have these 12 months. And I think that's what you're seeing. The Biden administration is basically saying: look, we need to provision Ukraine with funding in particular. And the unsaid part of that statement is because there may not be any more funding after November 2024. And so by the way, it's not just the US election, you know, you had a Polish election this year, and Poland is at the frontline of West

sort of the France challenge to Russia. Polish election, ahead of the election, the incumbent party abrogated a trade deal with Ukraine to satisfy its farmers, so if Poland is willing to play politics, instead of geopolitics, if Poland is willing to take short term political goals over strategic goals, then why would you expect any other country in the world to take the big picture perspective here? It's clear that every single western country is starting to lose this sort of enthusiasm it had in February of 2022. And again, that's not because we're myopic, or because we're short sighted. It's because Donetsk and Luhansk just do not matter, for big picture geopolitics. You know, and again, it's unfortunate to say that if you're Ukrainian, and I say that with caution and humility, but the reality is that the West already won, it weakened Russia, it embroiled in a Forever War, where they're going to have to staff a million men with weapons on this front line for a very long time, that's going to continue to drain Russia's budget. And most importantly, Kyiv is held by Western allies, it's free, it controls vast majority of Ukraine. As far as the West is concerned, these are ancillary goals, their luxury. And so I think that you will continue to see erosion of support. Dutch election is another one, you're starting to hear French president Macron make statements about this as well that are you know, talking about the end game. So I think the writing is on the wall and by the way, as market is concerned, as far as markets are concerned, this conflict has not really mattered, I would argue since September of 2022. Forget defense stocks for a second. Oil prices, commodity prices, wheat prices, European currency, European energy costs, European industrials relative to American industrials, all of those trades are gone, because the markets decided in September of 2022, that this is a frozen conflict. And quite frankly, this time the market got it right.

Erik: Let's move on to the Israel/Gaza conflict, which obviously is the hot one. Now, where is this headed? IDF has said as they have re escalated after the ceasefire ended or a ceasefire broke down is perhaps more accurate, that this will probably take at least a year. That's probably more than some people were bargaining on. Do you agree with that? Where's it headed? And who's likely to get involved?

Marko: Well, I don't think it will take a year because I don't think Israel has a year. And I say that because from my reading of Israel's history, what gives Israel its unique military technological advantage over its rivals and neighbors in the region is its status as a Western country, based on a form of Western small L of liberalism. I don't mean in the American context, like progressive liberalism, I mean, you know, nation state building process that took part in the 19th and 20th century. And you have a state that's effectively recognized by everybody in the West as carrying on these Western European liberal ideals. And this is really important for Israel, because it depends on this technological and military advantage, because of its connectivity with the rest of the world. And so, when you see a turning public opinion, which is, as you know, documented and empirical, and it's not just college campuses, it's significant. When you see it turn the public opinion against Israel, I think that is a material constraint. I think that no Israeli government can ignore that turning public opinion. And quite frankly, I think this is exactly what Hamas wanted. I think Hamas has been wildly successful. And not because of the casualties on October 7, but because of the subsequent Israeli retaliation, this is precisely what Hamas wanted. Israel is literally following their enemy's playbook. Because the idea here is to showcase to the world that Israel is somehow doing something wrong, other than defending

itself. And so I think that Israel, the IDF doesn't have a year, I think they have less than a year, and they're going to have to wrap up this conflict fairly quickly, or risk turning global public opinion further against Israel, which is an existential risk.

Erik: I just want to make sure that I understood what you just said, it sounded like you're saying that Hamas wanted to see Israel, essentially disgrace itself in the eyes of the global community, by overreacting or by initiating a campaign that would be perceived as genocidal by the rest of the world, and that they were set up for that to happen by Hamas, essentially putting itself at risk, like a suicide bomber that's, sacrificing itself, in order to cause Israel to be disgraced on the public stage, in the eyes of the rest of the world. Is that what you meant?

Marko: Yeah. And just to be clear, I'm not saying that this is an objective reality, I think that Israel has a great case to argue that it is defending itself, and that the context of Gaza, which is a highly urban, high density population area, makes it very difficult for them to kind of do what America did in Afghanistan, or Iraq. So the objective reality is something else. But certainly, I think this was Hamas's point, this is what they wanted, they got exactly what they wanted. And by the way, this is exactly the playbook that al Qaeda followed against the US. I mean, you can literally read Osama bin Laden speeches, where he literally said, we attack them, so they would come here, bring their war to us. So they would put American troops on Muslim lands. That's what we want, we want them here. And America did the same thing. America retaliated after 911. The difference between the United States and Israel however, and this is very important to understand is that, the US was and is in many ways a global hegemonic, it gets to make strategic mistakes, it gets to make them because it has preponderance of power. And because those mistakes are less relevant to the United States, which has its own industrial capacity, its own technological superiority. Israel doesn't. And this is the tragedy of great power politics in a way this is the tragedy of geopolitics, big countries get to make mistakes, small countries don't, they have to be much more cognizant of their material constraints. And so I think that Israel will have to adjust that forecast of the IDF, I would argue that by mid-January, this conflict, you know, Israeli operations in Gaza are going to have a much lower intensity, I don't doubt that they're going to continue to occupy parts of Gaza for a year or maybe longer. So maybe that statement by the IDF will technically proved to be correct. But I think from the perspective of the global public opinion, I think that by mid-January, this will look a lot more different than it looks now. And I'm willing to come back on your show and be proven wrong, obviously.

Erik: What do you think the outcome will be for the people who reside in Gaza? Obviously, they've been displaced from North Gaza into South Gaza. Now they're being told to get out of South Gaza. They can't leave Gaza completely. There's been some talk of trying to, to move them out to Egypt, although it sounds like the Egyptians are not exactly rolling out the welcome mat for that. What happens to the people, the civilian people of Gaza, as this conflict eventually reaches some kind of conclusion?

Marko: You know, I have no idea. And I have no idea because I've spent really no time thinking about your question. And that's because there's one truth about the Middle East. And that's that pretty much none of the big players in the Middle East or any players for that matter.

really care what happens to the Palestinians. That doesn't mean that I don't care. I'm just saying that it is pretty clear to me from the reading of history since 1947 that nobody actually cares what happens to the Palestinians, Jordan might be the one country that stands against that. But, you know, Arab nations that surround Israel have never really taken any real serious efforts to defend the interests of the Palestinians. And I don't think that will change. And so I don't really know what happens to them. But I also don't think that it will be relevant for the broader markets. And just as a reminder to the listeners who are going like, whoa, this guy is extremely callous. You know, I only focus on geopolitics from a market perspective. So rarely will I really spend any time thinking about purely geopolitical, political or, for that matter, human normative moral issues. And so on that question, I just don't have an answer.

Erik: Well, I understand your point that many of the governments in the region may not care about the Palestinians. But I think that the message is overwhelmingly clear that the rest of the world in terms of the general population is having a stronger reaction than almost anybody expected, saying, wait a minute, what about the Palestinians, they care very much about whether there is a genocide risk, and if the Palestinian people are going to be sacrificed completely. It seems to me that that is an unexpected event that some of the governments which as you say, are very callous and don't care about the Palestinians, are going to have to cope with and that they were maybe not planning on? What are their investable implications of that?

Marko: I don't think so. But what I would say is that, yeah, you're right, you're correct. And obviously, the reaction of the West in particular, is this big material constraints to Israel. So I guess you're right. I mean, it does matter. I think it's going to be very difficult for Israel to, for example, forcibly expel Palestinians out of Gaza. But I also, I really disagree with the notion that that was ever a plan. I'm sure you can, you know, we can all find somebody in Israel or Israel's government or security services, saying something like that. But that's just without Egypt's acquiescence, that would have been impossible to do anyways, I think that pushing these people out of Gaza was never really the plan. But at the same time, I mean, it does look objectively like retaliation, heavy handed retaliation for October 7 event whilst part of the plan. And that in of itself, I think, is running afoul of global opinion.

Now, in terms of the region, I'll give you a scenario that will sort of prove me wrong, and would create a sustainable risk in the region from this event that, that would be if a population in one of the neighboring countries really started to become agitated by the events. And obviously, the only country I can think of as being really relevant from that perspective is Egypt. If you had some sort of a popular unrest in Egypt against the current government, that demanded a much more forceful response to Israel's actions. Now, that's something we'll be able to see. We'll be able to sort of monitor over a long period of time, it's not happening right now. But that is a potential way in which popular reaction in the region to the events could become investment relevant. Iran? Iran has been very careful in how in response to the events in Gaza, I think, for probably two reasons. One, it's been warranted by the US that they will retaliate against Iranian involvement. And there's historical precedent for Iran, such as the 1988 Operation Praying Mantis, it learned what American retaliation looks like. It does not want to get Americans

involved until, Iran-Saudi detente in 2022, actually gave Iran some real strategic wins in Iraq and in Yemen. So Iran does not want to retaliate, to sort of West's or Israel's behavior, by impacting the global source of oil, which is Saudi Arabia. And so you've seen Iran tell its various proxies, including Houthis in Yemen, not to target Saudi facilities as retaliation for West support of Israel. And I think that's an important point that nobody really mentions that Saudis and Iranians solved a lot of their problems back in 2022. The only thing Americans basically kind of know about that deal is that it was "negotiated by China." But the much bigger significance is that that detente is actually holding in this stressful environment.

Erik: Let's talk a little more about the risk of this Israel/Gaza conflict escalating to a regional war, which was the great concern so many people had initially. It seems like other than Iran, the other Arab states really don't want to see that happen. Iran has been the standout that's been boldest in its statements. And I guess I have to go back to what you said earlier about Russia/Ukraine. I think you're right that a lot of the real intention of the West was not so much to help Ukraine as was advertised, but rather to damage Russia militarily, because that was their strategic objective. It seems to me that the US also has a strategic objective, potentially, I don't know. But it seems like they may have an objective to damage Iran militarily. And I noticed something like just this past weekend, the missile attacks on some merchant vessels operating in the Red Sea. You know, what really happened, as far as I can tell is there were some missile attacks on some civilian merchant vessels and a US destroyer responded to distress calls from those vessels in order to see what was happening, yet the headline came out, as Houthis attack US warship with drones, which I'm not sure that was quite accurate. It makes me wonder if the agenda that in the Russia/Ukraine conflict was to strategically damage Russia's military, if the US has a strategic objective to damage Iran's military capability.

Marko: Maybe later, not ahead of the election, you know, I think that the White House is extremely focused on not causing oil prices to go higher. So I will be very surprised if there was an intention with 12 months to go to do that. So I would say no, I don't think that that's what the intention is. But I will say this regional war thesis was from October 7 onwards, like the number one forecast by a lot of geopolitical forecasters, a lot of them assigned pretty high probability to that happening. And I do think that there's an option where it happens, I would think that Israel is more likely to make this a regional war than Iran, by for example, pursuing some strategy to create standoff distance between themselves in Hezbollah and Iranian proxies in Syria or Lebanon. So I can see Israeli military incursion into those two as an example of how this widens, but Iran really is constrained. And I want to really emphasize that, as I said earlier, they don't want US to be involved. US involvement would significantly impair Iranian capabilities, US has overwhelming military superiority over Iran. And more importantly, again, that Iran-Saudi Arabia detente really limits what Iran can do. In the past, they've expressed their anger at the West, by allowing their proxies or they themselves targeting Saudi energy facilities. That was a way to kind of rattle the cage of the West, you know, hey, we can increase oil prices. Iran can't really do that anymore, because they got what they wanted from their deal with Saudi Arabia in 2022. And so what you're actually seeing from Iran is just a lot of rhetoric, a lot of like, strong words, but very little actual things.

Erik: Well, let's go a little deeper on that. Maybe I'm misinterpreting this. But it seems to me that the rhetoric has been incredibly strong from Iran, what they've said is, we promise you United States that you're going to pay a very heavy price for having enabled what Israel is doing, we're going to get you for this, essentially, was the subtext. And the reason that that concerns me quite a lot is, it seems to me if you're sitting in Iran, and you've literally got half of the US Navy parked in your front yard with all of its weapons pointed at you, you're not going to take immediate action against the US Navy, that would be obviously suicidal. What you might do, though, is taking advantage of a wide open US southern border, and move your terrorists into the US and start planning the next 911 sized terror event on US soil, it seems to me if your rhetoric is you just wait, we're going to get even with you where you're going to pay a very heavy price for this. That to me logically would be what they might be planning. And maybe I'm just paranoid. Is that something we should be concerned about?

Marko: I'm going to fade that risk. I think Iran is completely and utterly just talking a lot of hot, hot air and again, willing to come back here in six months to the show and eat a lot of crow. But let me give you a little data point here. Before COVID became a thing, something else happened in early 2020. The United States of America assassinated, General Soleimani, who was the head of the Al Quds Force of the IRGC. He was also one of the most senior basically people in all of Iran, very popular. He was a hero of the country, rumored to be the next presidential candidate, by the way. This is like Petraeus level notoriety. And the US killed him while he was on the diplomatic mission to see Iraqi leadership. Iraq, of course, being a nominal ally of the US. He was just killed in Iraq by the United States. So this is a really serious event, early 2020, I believe it was January 2020. This happened. What did Iran do as retaliation? So again, this isn't something happening in Gaza, to Palestinian people who are not Iranians, you know, this is the United States of America, killing one of the most prominent members of Iranian leadership. Iran basically did nothing.

Today, they did rocket attacks against two military bases of the United States. But they were so pre planned and basically telegraphed to the US that there were just some injuries, like injuries, nobody died. I suspect they have no evidence that they called US and told them precisely when they would hit them, which part of the base would be hit. So what I'm trying to say here is like, look, we can infer from Iranian behavior, that they are clearly very cautious when it comes to rattling America's cage. And so I would say that most of their rhetoric is intended for domestic audience, and that they actually have no intention of doing anything of significant measures because again, they go back to 1988. For listeners read up about it, Google it, Operation Praying Mantis, Iran was very, very frustrated with US support from Iraq at the time. And they mined the Persian Gulf, one of those mines impacted a naval vessel, the United States in 48 hours, effectively sunk the entire Iranian navy. You know, and I don't think Iranians have forgotten that wrath of the US, the US is not going to put boots on the ground in Iran, it's not going to lose men and women in fighting Iran, the US will bomb Iran from 30,000 feet and walk away. And that's not something Iran wants to experience.

Erik: Let's move on to the next geopolitical risk event, which is Venezuela and Guyana, Venezuela has threatened to annex the oil rich regions of Guyana. This is a conflict that some of

our listeners may not even be aware of. So why don't we start with what's going on there? What's happening? And why is it happening?

Marko: Oh, man, you're really pushing me here, you're like, this is like Carmen Sandiego, all around the world. Look, what's happened here is something really interesting. I mean, Guyana, basically, is a recent entry into the global oil production club, and they have increased their oil production from like, 70,000 barrels to 200,000, in 12 months and 24 months. And they're looking at potentially being in the million barrel club very, very quickly. And they're right next door to Venezuela, which I'm sure most of your listeners know, is effectively an impoverished country, where the government has all intents and purposes, destroyed the economy. And suddenly, the next door neighbor, suddenly finds all this oil. This is just the land grab by Venezuela, it's claiming. It's claiming that the maps that create a ground up, are basically wrong and have been wrong throughout history. It's claiming two thirds of Guyanese territory, by the way, it's two thirds. It's not like a small region. And they just had a referendum in Venezuela to kind of like rubber stamp, a military operation against your neighbor. And what does this mean for all of us? I mean, again, I look at geopolitics from an investor perspective. So obviously, the big picture here is that we're going to have a first serious military conflict in Latin America, like since the war between Paraguay, Brazil and Argentina in like the 19th century, I don't know. But it's not going to have any impact on global markets. That's what I would say. And the reason for that is like Guyana just doesn't produce those millions, yet. They produce about 200,000 barrels. So this isn't going to really impact global supply and demand of oil, number one. Number two, Venezuela's oil itself, its own production has been significantly impaired over the years due to their domestic economic mismanagement. And number three, I think this is a real desperate attempt by the Maduro regime to stay in power. Because they're wildly unpopular. And so yeah, there could be a conflict in Latin America, Brazil could get involved on behalf of Guyana to prevent this from happening. I think if there is a war between Brazil and Venezuela, Venezuela will lose very quickly. And, you know, that's a high risk for Maduro in taking this action because obviously, it could backfire domestically.

What should your listeners take from this from a big picture perspective, though? You know, the big picture perspective here is that we are in a world where the frequency of geopolitical conflict is very high. And we're going to stay in that world. There's a lot of this kind of like revanchism happening, settling of scores of these conflicts that were frozen for hundreds of years, either because of the cold war set up between Soviet Union and the US, or because of American hegemony, where the US was basically in charge from 1985 to sometime into 2010s. We're now in a completely different world, what I call a multipolar global environment. And in that environment, when nobody's really in charge, a country like Venezuela decides to invade his neighbor. And I think that we will start seeing more and more of these events globally.

Erik: The next big one is one that hasn't happened yet. But a lot of people are worried about, which is the risk of China invading Taiwan. How big of a risk is that? And what would the market implications be?

Marko: So that's the one that I definitely would not say, I mean, your listeners at this point are probably seeing like, wow, this guy's a one trick pony. Every time something happens in the world, you just face the risks? Well, you know, if China invades Taiwan, well, we've got a problem. Markets would definitely think, global markets, S&P 500 would likely be impacted by that. We do have a very important event, the January 13, Taiwanese presidential election, very interesting election. Similar to the US, there's multiple candidates, the pro sovereignty party, the DPP Democratic Progressive Party, their candidate William Lai, is likely going to win the election. I hesitate to call it a pro Independence Party, because it's not fair. TPP will not proclaim independence, but they are pro sovereignty from China. So they are very closely aligned with the US. The current President, President Tsai has, you know, obviously been very close to the Biden and the Trump administrations, if they continue to be in power that will definitely irk Beijing. Interestingly though, William Lai is polling terribly. He's polling in the 30s. So why is he going to win? Well, because the more sort of like conciliatory vote is split between two different parties, three candidates, in fact, the two main ones are KMT, Kuomintang, and TPP, which is the Taiwan's People's Party, a new party. And so the reason I mentioned this is because it's important to understand that if the current incumbent party stays in power, they don't have a popular mandate for independence, they don't have a popular mandate for even continuing the level of close relations with the US they had over the last administration, because they will only have a mandate support of about 35% of the public. So that's the first thing I want to mention.

The second thing I want to mention is that President Xi visiting the US and meeting Biden in San Francisco was a big concession by Beijing. It seems to me that China is so focused on internal politics and internal economic situation which is deteriorating, that they don't want to rattle the cage with the US, they want a temporary détente, a pause, if you will. And so I think that the tensions at least in the immediate term, let's say, over the next 12 to 36 months are actually going to be lowered over Taiwan. I think that strategic rivalry between China/US still remains the most important geopolitical question over the next decade. But China is basically saying to the US, listen, we're going to take our toys and go home, we don't want to play this game right now.

Erik: Let's go back to the material impacts and where the risk factors are, because something I just do not understand about this China/Taiwan situation, if you start the first part of this story, if you were reading it in a history book, would go something like this: There was a pandemic in 2020 and in the course of navigating that pandemic, the whole world realized something really scary and interesting, which is that we are completely and totally dependent on China for almost all of our prescription drug manufacturing. And we're completely and totally dependent not just on Taiwan, but on one specific company in Taiwan, for the lion's share of the semiconductor manufacturing, which is the absolutely essential ingredient to almost all electronics, computers, anything high tech, it's almost impossible to build it without semiconductors that come from Taiwan. So when we noticed all of these things, if I was writing the history book chapter, I would have to believe the next paragraph goes, we recognize these risks and the US government immediately took action to mitigate them by taking the following actions, except there haven't been any reactions, what the heck is going on here?

Marko: It's really tough, Erik, I mean, it's very, very difficult. It's not like pressing a button, and we suddenly have alternatives to a lot of these supply chain issues you're pointing out. I mean, let's take the chip building point, you can go to the US Department of Labor website, and just take a look at what's happened to our supply of highly skilled manufacturing labor in the semiconductor space. It's that specific, there is an actual data point, and it's collapsed since the 90's. So the TSMC plant in Arizona as an example, which both the Trump and the Biden administration have touted as a solution to a lot of these problems, let's get TSMC to build a plant in the United States. I mean, it's a disaster. Books are going to be written five years from now about what an absolute boondoggle that that plant is going to be. And there's a lot of reasons for that. It's not just that we don't have supply of labor in the United States to actually build these things. It's also that there's no wider supply chain, then we're going to be wildly expensive. We apparently put in in Arizona, I don't know why we put in Arizona, I think we put in Arizona, because it's a purple state and somebody wants to cut a ribbon of this factory ahead of an election. Because I can tell you this, that highly sophisticated chip that's produced in Arizona is going to have to be put on a bed of a truck sent to Long Beach, California, and then put on a ship so it can go back to Taiwan, where it can be integrated into a piece of electronics. So I think the US government is trying to modify the supply chains, it just takes a long time.

Now the good news, though, is that here in the US, everyone's hysterical about the US addiction to China, from a supply chain perspective, but nobody's talking about how absolutely addicted China is to global demand. So while they have the supply chain, actual physical components of the supply chain, we have the demand. And see, China thought that they would have the demand, they thought that their middle class story was the story of the 2020s or the 2030s. Well guess what? China from an economic perspective is where the United States was in 2009 cannula. They are facing a private sector deleveraging moment. They're in a balance sheet recession, as Richard Koo would call it, they are facing their secular stagnation. And so the C, the consumption component of their GDP equation is going to be permanently impaired. As far as the current policymakers in China are concerned for the next seven years. How long did it take us to resolve our secular stagnation from 2008 until when? 2017 to 2020, depending how you see it. So that's where China is actually considerably constrained. And I think it gives the US a lot more time. Because I don't think China is going to start a war. While it's absolutely addicted to the global demand story, which means that American households and European households are what pays for GDP growth in China. And as long as that's the case, I think that they will hesitate to play politics with supply chains, which by the way, Erik, we have empirical evidence that I'm right. What is it? China has hesitated to retaliate to any of the American tariffs, sanctions, export restrictions, you know, they said, like, oh, we'll put some export controls on various materials in rare earths. But those are not automatic. They will basically choose which companies in China get to export some of this stuff. But to this day, China's not retaliated in any way to the American export control sanctions and tariffs, just think about that. There's a reason they haven't retaliated, and it's because they're afraid that it will impact their economy far more than it impacts the US or Europe.

Erik: Let's move on to what you already said is the big one. It's an election year in the United States. And I don't think this election really bears much resemblance to any other that I can remember because what you're hearing now, from the people who oppose Donald Trump is, not we don't like this guy. It's not we think you shouldn't vote for our guy. Instead, it's the end of civilization will happen if Donald Trump is reelected. We've actually seen some rhetoric in you know, Senators that are tweeting saying that the comments that Democrats have made this week are a stealth call for assassination. Now, whether or not that's true or not, I don't know. But the notion that we have Congressmen in the United States, who are publicly making the statement that the other side has called for an assassination of their candidate. I don't remember anything like that ever happening in my lifetime in US politics before. Seems to me like this is more emotionally charged than anything we've ever dealt with.

Marko: Look, I think that US election will be the biggest macro event of 2024. You know, it took us 54 minutes or sorry, 47 minutes to get to this, we saved the best for the last. But what I would say is that there is no bigger political geopolitical issue for investors. Why? Because you're right, Erik, a large group of Americans, like I would say, half of Americans do believe that a Trump presidency 2.0 will be the end of the Republic. And why does that matter? Oh, and by the way, and this election will be the most unprecedented, I think, in US history since the 19th century, because I believe there will be more than one viable third party run. I think Joe Manchin is going to run, I think Liz Cheney has just today, December 5, said that she's contemplating running, and you have Kennedy who's miraculously polling double digits around 10%. So what you could have is a situation where Donald Trump or Joe Biden wins this election with about 35% of the vote. By the way, can you imagine what that would look like from 2024 to 2028? If we have an administration that only carried 30-35% of the popular vote, can you imagine how little confidence the government, the public will have in that White House? The second issue is that you could have a situation with third party candidates when Electoral College votes, and then neither candidate gets to 270 votes. And then you have the House of Representatives decide the President, again, extraordinary things will happen this year.

So why does this matter? I think it matters, because I don't think the Fed will ignore this reality. And this real risk. And again, this is not a popular view. I think a lot of professional investors who have cut their teeth over the last 40 years, reading Fed statements, taking them seriously thinking about the FOMC and the Fed as a catalyst for markets, they're going to douse gasoline over themselves and light themselves on fire right now, because I'm about to say something that's heretical in American financial industry. You know, in our epistemic community, it's not nice to say that the Fed is political. It's improper, well, you know what, sorry, but it's about to get political. Because I do believe that the Fed is part of that establishment elite consensus, and the view in that group. And by the way, this isn't just Democrats and Liberals. This is also many, many centrist Republicans who believe that the Trump 2.0 presidency will be a real game change. And so I think it's just ridiculous to think that the FOMC will do anything but cut rates in 2024, no matter what happens to the economy. Now, I happen to be slightly bearish about the US economy. For example, this is a low conviction view, but my view is that we're going to have a shallow recession in first half of 2024, actually not in the latter. But see, my view is then that the Fed will cut rates by far more than 125 basis points, it's currently priced in the OAS curve,

far more, it will cut rates 3-4%, in order to mitigate the political effects of that recession. Now, if your view, as a listener is like, well, I don't think a recession is a risk in 2024, I think the recession risk is just out of the market at all, then you should not bet against the current pricing in the market of 125 basis points worth of cuts, I can actually see the Fed using whatever data gets as an excuse to become lenient in 2024. So that's why I think this election matters.

Erik: And let's talk about the investment implications of that. Certainly, gold would be one benefactor of the Fed, cutting more than expected, cutting more than consensus expectations. What are the other investable strategies there?

Marko: Well, I think whether there's a recession or not, matters for you on a tactical basis. So January, February, I probably want to be bearish on US equities in anticipation of a recession, right? But if you have my view on the lenient Fed, then the endpoint is the same. In other words, we made round trip to all-time highs, but we will get to all-time highs by the end of next year. That will be the implication, in other words, if you close your eyes, we will be somewhere much higher than 5000 and the S&P 500 By the end of next year. Why? Because the Fed is going to respond with leanings. I also think that the dollar will be weak. If we are correct, obviously, that's the flip side of your gold call, which I agree with. And if that's the case, if you have a lenient Fed, if you have weak dollar, then I think emerging markets and commodities should do actually pretty well. And this is interesting because a lot of folks out there have soured on emerging markets. A lot of institutional investors that I work with closely, don't want to be in emerging markets and have expected emerging markets to do very poorly because of high rates in the US, and also because of dollar strength. And quite frankly, both commodities and emerging markets have held up quite well, despite hawkishness in the Fed and despite China's economic weakness. And I think that that's telling you that emerging markets are like a coiled spring. And if the US monetary policy becomes populist, effectively responding to political risks domestically, then I think that investors and institutional investors will start seeking those returns outside of the US. So that might be a story for 2024.

Erik: And I just want to make sure I understood your round-trip comment, you're suggesting there's a possibility of a very significant downdraft in markets, we might see equities sell off badly in the beginning of the year. You're simply saying that we're going to get back up to new all-time highs, no matter what, even if there is a significant bear market before that happens?

Marko: So very low conviction view, but yeah, I don't think it will be significant bear market because when I look at the data right now, I think if we do have a recession in the first half of 2024, it will be a CapEx and government spending induced recession. Now those two are 30% of US GDP, you know, 70% of US GDP is the households. Households, in my view, a controversial view, but it's been right so far, households are far healthier than people have expected them to be. So what I would expect is the market can react to this CapEx induced recession, very shallow recession, like a 2001, for example, maybe stocks go down 20% in the first quarter, second quarter, but by the end of the year, I think that we've reached all-time highs. This isn't that different, by the way, from investment bank forecasts. I mean, if you go through all the different investment bank research, I think the majority of them are saying \$5000 SPX, by

the end of 2024. My contribution to this sort of exercise, if you will, end of the year exercise would be to say that I would expect the year to end higher than \$5000, because of this leniency of the Fed.

Erik: Marko, to summarize this whole discussion of US politics, what are the main points that our listeners should take away from this?

Marko: There's a problem in supply and demand in US politics. And what I mean by that is that the supply right now is Democrats, Republicans, those are your two options. The demand from the public is clearly for something else. And so what I would say, maybe not in the 2024 election, but I do think that this decade, we will have another party realignment in US politics, the first one since the 19th century, the sort of a fourth party realignment, most listeners are going to scoff at that and say: No way, the barriers of entry are too high. But, you know, that will be my highly controversial view. And I think that ultimately in the long term, will be good for the US because I think the median American is a centrist. I think the median American is reasonable and wants solutions. And I think that you will get those maybe not this election, but potentially the next.

Erik: Well, Marko, I can't thank you enough for a terrific interview. Before I let you go, though, please tell our listeners a little bit more because you guys are not just a research firm, [Clocktower Group](#), you're an asset manager. Tell us a little bit more about what you do there and how out interested listeners can contact you.

Marko: So we are in asset management, we work with a very large institutional investors, we do macro seeding, so we seed discretionary macro hedge funds for a living. That's our tradition. That's sort of the historical background that we come from. And then we also do some private, illiquid markets as well. And for anyone who wants to find out more about what we do just go to [clocktowergroup.com](#) is probably the best way to go about it. I'm also on Twitter so they can search for me on Twitter and I occasionally do post some little snippets of wisdom but, you know, maybe not wisdom, but I definitely don't post all of my views and my investment calls so that's reserved for clients.

Erik: Patrick Ceresna, Nick Galarnyk and I will be back as MacroVoices continues right here at [macrovoices.com](#)