MacroVoices Episode 545

Feature Interview with Michael Howell

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Michael: This everything bubble will inevitably come to an end, and you're starting to see signs that liquidity is rolling over, and therefore we've got to accept the fact that after every bubble comes a bust

Erik: That was Michael Howell. I'm Eric Townsend, and this is Macro Voices, the free weekly podcast targeting professional finance and sophisticated private investors.

Episode 545 was produced on August 13th, 2026. Michael and I will discuss the 65-month global liquidity cycle, where we stand in that cycle currently, and what comes next. Michael agrees with my view that gold has probably bottomed and is likely to rally from here. So we'll also discuss precious metals, inflation, and where Fed policy is headed longer term.

Patrick: And I'm Patrick Ceresna. Let's dive into this interview.

Erik: You probably know Michael as the founder of Cross-Border Capital and the publisher of the Capital Wars Substack. There's also another business there, which is Global Liquidity Indices that we're gonna talk quite a bit about. Michael, it's great to get you back on the show.

It's been six months or so. Let's dive right into the slide deck that you prepared. Listeners, you'll find the slide deck linked in your Research Roundup email. If you don't have a Research Roundup email, just go to our homepage, macrovoices.com. Click the red button above Michael's picture that says, "Looking for the downloads."

Let's go ahead and dive right into it, talk about the liquidity cycle and so forth. Where do you wanna start?

Michael: First, Eric, thanks for the invitation. It's always a great pleasure to be on your podcast. I think the best thing to start with is the global liquidity picture. That's the, the lens that we look at markets through.

Global liquidity is the key driver of asset markets. Money drives markets, basically, and that's really our thesis. And so what we do is we monitor the flow of money through world financial markets. And in the slide deck, there's a, a chart there which shows the global liquidity cycle. We focus in this particular slide on the advanced economies for reasons that will be probably apparent later that China is doing something very different.

But essentially what that's saying is the liquidity cycle has peaked, and by that we mean that the growth rate of liquidity is falling. The absolute level of liquidity in dollar terms is still elevated, but it's the growth rate which is really critical for asset pricing, and that's rolling over. And I think the, the thing to bring out of that is, or two things to bring out of that, one is that this is a regular five to six-year cycle, as you can see or those that have got the slide deck will be able to see.

It's a very regular cycle. The cycle bottomed in late 2022, and it peaked at the end of 2025, and it's now starting to come off quite noticeably. The second point to note is that the reason that liquidity cycle is coming down is not really because central banks are tightening yet. That is a story that is unfolding and yet to come.

It's much more because the real economies are strong, and they are dragging liquidity out and effectively crowding out the financial sector increasingly. And it really comes down to a very simple point that all money that is anywhere must be somewhere. And effectively if it's in the real economy, it's not in financial markets and vice versa.

We've had, the blaze of performance from asset markets and now it's the turn of the real economy. It's as simple as that

Erik: Now, if I'm reading this global liquidity cycle chart on page three correctly, it looks like not only has liquidity already peaked, but w- looks like we're more than halfway through the down cycle and maybe almost getting closer to the next rebound cycle, at least in terms of the, the Y-axis.

But on the X-axis, we're not there yet. How do you reconcile that? Are, are we close to a bottom or are we far from a bottom? I could interpret it either way.

Michael: You're right. The way that I would see it is that the liquidity cycle per se is unlikely to bottom within the next six months. It's much more likely to be a twenty twenty-seven event.

And if I had to venture a, a time, I would say sometime around the middle to later in twenty twenty-seven. That would be the normal timeline. It's possible that things could concertina, and we may get a, an earlier rebound, but I think that's unlikely. Not least because the big monetary authorities, namely the Federal Reserve, is still a long way from aggressively tightening, but I think that is upcoming.

I think the Fed is gonna have to do something much more explicit, and we may know that before the end of the month after the Jackson Hole speech.

Erik: I actually thought that the title of your slide deck might be more telling than the slides themselves. You say Warsh versus the markets. Kinda feels to me like that's really the theme that we've been handed here is a president who's absolutely passionate about getting a Fed chair installed who's gonna do nothing but cut, and I think we got a guy who might be inclined to do something different.

So is this an impossible setup? How should we think about what comes next in Kevin Warsh finding his relationship with Donald Trump, so to speak?

Michael: I think it's gonna be a pretty unhappy relationship if that's what Trump is expecting, and probably is. The fact is that central banks don't control interest rates.

They may think they do, but the market controls interest rates, and it's the long end which drives the short end not vice versa as the textbooks tell us. And the plain fact is that if bond yields are rising, which they clearly are, and I would argue that that rise in bond yields, which is a global phenomenon with the exception of China, is all about strong nominal GDP growth.

That's what tends to drive the underlying level of interest rates. That's why they're moving up, and that is putting a lot of pressure on the front end of the term structure. And the plain fact is that the Federal Reserve can't resist that very easily. It can do various tricks, and they've already used up a lot of those tricks.

But to keep the repo markets liquid after pushing so much funding into the front end of the market will mean rapid monetary growth or an expanding Fed balance sheet. Those are presumably now ruled out. So barring some some, clever tricks from Scott Bessent, which could mean that A lot of the deficit is being funded at the margin by more and more bills.

We're due higher interest rates. That must be coming, or higher policy interest rates. That has to come.

Erik: Michael, it seems like all indications are that rates are headed higher, but at the same time, we have a president who is absolutely passionate about wanting to see lower rates. And I'm not sure that he understands whether the dog wags the tail or the tail wags the dog.

So what should we expect here?

Michael: I think it's gonna resolve by rates are gonna have to go up. That's what the markets are saying. If you look at what's happening at the front end of the curve in the US, the two-year Treasury note, which has always been a fantastic predictor of policy rates, is elevated.

It's already broken through SOFR rates. It's suggesting that we're heading for higher policy rates in the next few months, and in fact, the, the market is already discounting that. That, that's clear. But we're probably treading a path which to my estimation looks remarkably like late 2021, early 2022.

That was a period with of some considerable unhappiness for investors. And you've got to recall through that period, the S&P dropped 25% and Bitcoin dropped 75%. Now some of that drop in crypto is already in the bag, you, you get the idea here that markets, asset markets, risk asset markets don't like central banks that are tightening.

And this is, I think, inevitable given the given the backdrop for the economy. And my view is the economy is a lot more, is a lot stronger, a lot more robust than than many people would envision.

Erik: Michael, let's move on to page four, the history of asset bubbles. When's the next one? What should we be buying or selling in order to profit from it?

Michael: I think the fact is we're already seeing the asset bubble. This is the everything bubble that has been fueled by again, more liquidity. And I think the, one of the interesting points is to try and understand how the liquidity mechanism works, and it's something which is running-- It may have been originally triggered by central bank easing, but it's running now out of their control.

And the problem is that the financial system creates liquidity endogenously because after an initial liquidity shock, which may come from the central banks, asset prices rise, collateral levels increase. We live in a financing system now where collateral is the mainstay or the backstop for all credit and all loans.

Something like 80% of all lending now in the world economy is collateral based. So if collateral values rise you've got more ability to borrow, and then more liquidity goes in the system, and this is why you see this recurring sequence of liquidity booms and busts. Now, history shows, and this is what the slide deck is indicating, that every previous bubble that we've shown there has had, as a root cause, a big expansion in liquidity, and it's no surprise that we're getting it again.

Even if you drill down into the bubbles that we've seen in in some of the emerging Asian markets like Korea, you've got to accept the fact that Korean liquidity has been skyrocketing higher. And this is just the reality of how markets work. This everything bubble will inevitably come to an end, and you're starting to see signs that liquidity is rolling over, and therefore, we've got to accept the fact that after every bubble comes a bust.

Erik: You mentioned a few minutes ago that China seemed to be an exception to the rule in terms of what was happening with global liquidity cycles and so forth. This is a message, Michael, I've been getting from several of our recent guests, saying China's in a special category all of its own. And that worries me, 'cause it feels like we're seeing a bifurcation of the economy where China's kind of branching off.

And frankly, it makes me fear that we're headed toward a war scenario and that we're seeing the financial markets essentially anticipate that there will be a a forced bifurcation of those economies by military circumstances. Am I crazy to think that?

Michael: No, I don't think you're crazy to think that. I think that's the way that the world is evolving, and I think that you can see certainly in the liquidity data, signs that China is definitely out of step and maybe moving almost exactly oppositely to where the US is.

Now, the legacy that China has has had is that it's been struggling to try and maintain the value of the yuan for several years against what has been a strong dollar. And what they have done is they've basically maintained a very tight liquidity policy through much of that period. That Tight liquidity reinforced the debt problem in China.

It created debt deflation. The backdrop that we're now seeing in the Chinese economy is lackluster growth very weak inflation, if not disinflation or deflation, and we're seeing the debt burdens grow. And if you look at the Chinese government bond market, it's the only bond market where yields are dropping and yields are down at one point seven percent, which is a great contrast to everywhere else.

Now, that backdrop, it needs to be resolved. The Chinese economy can't stomach debt for much longer, this degree of debt, and they basically have to devalue debt domestically. In other words, that means devaluing the yuan within the Chinese economy. Now, I stress the internal nature of that devaluation.

China has capital controls, as it has large Forex reserves, and it has compliant state banks, and they can probably manage if you like, a, a bifurcated exchange rate regime, maintaining a stable yuan/US dollar externally while trying to devalue the yuan internally. And my reckoning has been that is all about, or that is the story of why gold is going up and going down.

The cycle in gold is all about Chinese devaluation. China is embarking on, I think, a, a significant liquidity expansion. It will need its economy to grow. That economic growth will further fuel world economic activity, and it will boost commodity prices globally. And I think that's the regime we're in. I think one needs to understand the differences in these cycles.

So what you're seeing is strong growth in Western economies, as we know already. That is fueling commodity markets. They've had a tremendous run over the last 12 months, but there's been still more to go. And now we're getting a further stimulus likely coming through from China, and I think the increase in the gold price, particularly in the last 10 days, is indicating the fact that China is turning on the money taps again

Erik: This change in the direction of gold in the last 10 days has definitely caught my attention.

Feels to me like the correction is over, the new move higher is on. Do you agree with that? And if not, why not?

Michael: 100%. There's a, a chart that you can see in the pack, or if those are the listeners who have got the pack, if you go on to slide 21 there is a chart there which looks at PBOC liquidity and the gold bullion price.

Now, what I've tried to indicate in that chart is that the two series are very closely correlated. In other words, the rise in the gold market, and in particular, the breakaway of gold from its normal axis of real interest rates, which was a very clear feature in early 2022, was not anything about, Russia or whatever the, the excuse was.

It was much, much more about the fact that PBOC, the People's Bank, started to turn on the liquidity tap quite aggressively. And if you look at the chart, you'll see there's actually quite a compelling correlation, both going up when liquidity is expanding, and then more recently when liquidity has come down with a bump.

Now, it may now be being restored once more, but I think that gyration is very important. Now, for those that are more or maybe those who are less persuaded by this chart, there is another one which looks at changes on the following slide, which is shown in terms of weekly changes. And there's actually even I think even a stronger case for saying that there is a connection between these two data series.

And as the People's Bank started to increase liquidity, we signaled the gold market was likely to rebound, and it looks like it has. And very interestingly if you look at the yuan gold price, in other words, the gold price denominated in Chinese yuan, it's bottomed exactly on its trend line at about 27,000 yuan And that's the thing to look at, not the dollar gold price because China and the Shanghai Gold Exchange is now the marginal pricer of gold worldwide, eclipsing COMEX and London.

And that's where we need to look. It's Asian demand that's fueling gold not Western demand, and we need to understand the People's Bank. Now, there is a chart which I've got a little bit earlier, I think it's slide 19, which looks in a lot more detail at what is going on. Now, this is an interesting conjecture.

I'm not saying I've got any insight here, but I'm, it's purely proof by association. And this is looking at daily, a daily print of the People's Bank's balance sheet which we've constructed by looking at their open market operations and various other liquidity injections. And what that chart on slide 19 shows is that the People's Bank, after a long expansion of liquidity, effectively turned the money taps off on March the 2nd, and you saw liquidity declining quite noticeably.

That money tap was turned on almost exactly to the day that the MOU was signed. Regardless of whether it's a fragile MOU or not, that seemed to be a turning point. And ever since that that date, Chinese liquidity has expanded again, and with that, the gold market has gained more traction. And I think that this is the beginning of a further and maybe longer stimulus from China because they need it.

Believe me, the economy needs some stimulus.

Erik: Let's go a little deeper on this because I know a lot of our listeners will be tempted to get back into this gold market on the long side and speculate on higher prices. But it seems to me, as you said, China has been the key to all of this, and it seems to me that what's going on right now is, eh, maybe things are getting better, but maybe not.

And I think that there's plenty of room for a re-escalation of the Hormuz conflict as we realize that maybe President Trump didn't have this negotiated quite as well as he thought he did. If the Hormuz conflict heats up again, does that potentially kill the gold rally and put us into lower lows, or has something changed that's going to be, I'll say, immune to those politics that would cause us to wanna get long gold in size?

Michael: I think there are, the way that I would express it, Eric, is to say this, is that the gold price is going up now because of China's historic debts, and the liquidity injection that we've seen from the People's Bank is all about trying to devalue the yuan internally, and that is what's driving gold up. And as we know, crypto, one of the other obvious monetary hedges, is illegal in China, so any buying of of protection against liquidity expansion or money printing really is gold, and we know that Chinese retail have a huge appetite for the gold market.

So what I would say is that the course of gold follows what happens from the People's Bank. So the first thing one needs to look at is what the People's Bank is doing in terms of its liquidity injections into markets. If they fade off again, and let's never say never, but if they do fade off again then the gold market is gonna be challenged.

If they keep running, which I suspect they probably will, then gold continues to get a bid. Now, I think that it's important to draw a distinction between gold and precious metals, which are the obvious monetary hedge for many, but particularly for Asians. They tend to like those instruments, they're traditional monetary hedges.

And crypto, which has really been the monetary hedge of choice of maybe many people in the West, or particularly younger generations in the West. Now, crypto is much more attuned to global liquidity, and particularly Federal Reserve liquidity, than it is PBOC liquidity. By definition the PBOC shouldn't have any effect on crypto, and the evidence suggests that it doesn't really have much effect.

But it's really global liquidity and Fed liquidity which really matters. Now, if we're correct and we're seeing this fading off of global liquidity and the Federal Reserve under pressure to tighten, then it's no great surprise that crypto is under a cloud and gold has been outperforming, and that's really the story we think is likely to continue.

In the longer term, both assets are gonna go up, but I think we've got to be we've got to acknowledge the cycles here, and those cycles are moving very differently.

Erik: Michael, I pulled you out of order a little bit there because I was very curious to get your thoughts on gold. Let's go back to where we left off on the slide deck at page six.

Tell me what's going on with the world's global liquidity cycle. What causes the cycle to go down, and how much further does it have to go?

Michael: Okay. The slide that you refer to, which is on page six, is looking at the difference between global liquidity, which if you recall, is basically money which is flowing through world financial markets, and what's happening in the real economy.

So let's think of those as two very distinct spheres of liquidity. The orange line on the chart is looking at our global liquidity index, which is measuring the financial uses of liquidity. And the black line is the world business cycle, which I've basically calculated by looking at all the major headline business surveys worldwide, the Japanese Tankan, the ISM in the US, the IFO in Germany, et cetera, the INSEAD in France, weighted them by GDP, and put together an index of w- of the world business cycle.

Now, if you look at that chart, you'll see that those two cycles are moving completely asynchronously. In other words, what is when there is a trough in global liquidity, there is a peak in the world economy, and similarly vice versa. And it comes back to the point I made earlier on, that is, all, all money that is anywhere must be somewhere, and if it's in the real economy, it's not in financial markets, and similarly vice versa.

Now, what that chart indicates is that the turning point, the inflection downwards in global liquidity coincides with an upward move in the world business cycle. That was occurring from around late 2025, but it looks like it's accelerated recently. Vis evidence, look at the latest jump in the US ISM or the Philly Fed surveys or whatever.

Those are clearly indicating some strong pickup in world economic activity, and that is draining markets of liquidity. Now, that would suggest that we're late in the investment cycle. The investment cycle, as the name suggests, is a cycle. It goes up and goes down, and the fact is that liquidity is falling.

It's got further to fall, and we're only probably let's say 60% of the way through a fall, a likely fall in liquidity. But bear in mind, this is a rate of change and not a level. Momentum, as I keep saying, is very important to asset pricing. But if you take a look a little bit further maybe in the presentation, and if we take a look at slide 16, we try and put this into context into an asset allocation framework.

Now, what that diagram, schematic diagram on slide 16 tells us is that the liquidity cycle is very distinct, maybe not surprisingly from the economic cycle. One morphs into the other, so the liquidity cycle leads the economic cycle. Liquidity will spill over probably through wealth effects, et cetera, into a stronger real economy.

And you can see on the chart that the lead time is probably, some- somewhere around about 15, 18 months lead time between a liquidity peak and a real economy peak. So it would suggest that the real economy is still gonna, real economy worldwide is still gonna be expanding well into 2027, maybe early 2028, and that will be further boosting commodity demand.

And what this is really saying as well is that we're really in that spot between the peak of liquidity and the peak of the real economy, which is basically telling us two things. One is that, as I just said, commodity markets look good, but in terms of financial assets, you ought to be moving more defensively.

And that is an environment where bond yields tend to rise where defensive stocks increasingly outperform, and that's really where we're positioned.

Erik: And I notice on page 16, you've got a 60-month periodicity on the sine wave here. I thought it was 65 on the earlier chart.

Michael: I think it is, but that's broadly trying to I think that's, that comes into the category of being approximately right rather than approximately right and precisely wrong.

But it's a, it's about those sort of levels. I wouldn't put too much credence on that. 60-month is just, we're just saying about around five to six years.

Erik: Tell me about the asset allocation cycle on page 17.

Michael: Yeah, the asset allocation cycle really just derives from that. It just embellishes that rather further, and what it says is that if you look at that asset allocation cycle, we tend to think, as the right-hand side says, in terms of sort of broad regimes.

So we think of calm or speculation or turbulence or rebound. As the name suggests, turbulence is not a great place to be. Speculation gives you a flavor of where we are right now, which is saying that you can make returns, but volatility is gonna be high, so the quality of those returns is poor. And I think you know it's no great surprise that a lot of asset managers are actually down this year, despite the fact that the big indexes are up, and that's showing what a struggle it's been.

And then if you go to the earlier phase of calm, which is when the cycle is above average and expanding, that's when equity markets generally do well, and you just want to hold beta through that phase. And equities generally perform and everything goes up. And that's clearly the phase we've been in for quite some time over the last two years, but that phase has really come to an end.

One's got to be a lot more selective now. The commodity markets, as I foreshadowed, really, they tend to be dominant around the peak of the cycle, and that's pretty much where we are. The other thing to say is that you would typically expect to see in the downswing of a liquidity cycle a bear flattening in yield curves, and that's certainly what we've had worldwide right up until the last FOMC presser, where it seemed to be that the yield curve in the US started to steepen.

But I think that was really a reflection of the policy mix or the policy statements that really came out of the FOMC, particularly with Chair Warsh emphasizing the fact that, A, he wanted markets to do tightening for him, in other words, bond yields went up, and secondly, he was gonna maintain liquidity at the front end of the curve, emphasizing the ample bank reserve regime, and that is r- a recipe for a steepening curve.

Now, clearly, he's fighting the markets in this because the markets want to flatten the curve, but we'll see how how far he gets, and that's why we entitled this, Chair Warsh versus the markets.

Erik: Obviously, the the $64 million question is knowing when we're at the moment where you shift from turbulence to rebound mode.

What are the signs to watch for?

Michael: I think the signs we tend to look at, we look at a range of factors a bit. One of those would be what the actual liquidity data is telling us. Are you getting an inflection at all? The second thing we begin to look at is what sort of stocks are performing in different phases of the cycle.

We'd add to that what the yield curves are doing. So you'd expect after an inflection, almost immediately after an inflection, that you would begin to get a bull steepening in yield curves, and that's another factor to wa- to watch out for. And at that stage, you would also expect to see some serious damage, in other words, falls in prices in commodity markets.

They won't come out of this very well. Now, there may be compelling arguments to say that the trend in commodities is now a lot higher because of the background of competition with China and arguably capital wars between the major powers. That may well be a strong underlying trend, but we must recognize the cycle as well because cycles are clearly very important to investment and often they can spoil the party.

But generally, those are the sort of things we'd be looking at and I would say we're a long way from that point yet.

Erik: Page 18 begins a series of slides titled Has China's Great Debasement Ended? I'm quite curious. Has it ended? And what, talk us through this.

Michael: This is the point about gold Eric.

This is really saying that China needs to expand liquidity. It's got a huge debt problem. It's trying to, if you like, have its cake and eat it in the sense that normally if you expand liquidity, your currency will will fold. As I've argued that if China can basically keep that liquidity expansion internally to China, it can devalue domestic debt in other words, to raise the level of prices and wages in China relative to the value of nominal debt.

If they succeed at doing that, they will manage to erode their debt problem or progressively erode their debt problem. But it will come at the cost of a devaluation which will be expressed in a much, much higher gold price. Now, if you assume, and we're assuming this, that they can maintain the level of the yuan-US dollar cross, then that means that gold prices in US dollar terms are gonna skyrocket as well.

And I would think that would be pretty close to the top of my list of of conviction trades, certainly over the medium term. That's what I think is gonna happen. Going gold just simply has to go up. Not just because, as I hinted or said earlier on, that it's all about China's historic debts that is driving gold now, but it's the West's future debts.

In other words, the the likely huge expansion in debt GDP ratios right across the advanced world as aging demographics. You know the story as well as me. Defense spending, government procurement, all these elements basically drive spending and we're taxed out. They need to take on more debt, and that is likely to be the result.

And as a result of that, more and more of that debt will be monetized and the gold price will go up. So you've got many reasons why gold looks an attractive, very attractive asset right now. But as I, as said earlier on, I think that it's not just gold, it's commodity markets that are worth looking at.

What we've been seeing so far this year is a very clear outperformance of industrial metals against gold. You see the normal commodity cycle unfolding in front of us, where it's gold and precious metals that kick the thing off. Industrial metals then come through, then foodstuffs, and then energy tends to be towards the back end of the cycle.

And I think it's energy which is a really interesting play right now because so many people argue with great conviction that oil prices are probably even now too high and are gonna come down. I just don't buy it. I think oil prices are gonna go up significantly. I'm very invested in energy stocks because I think this is a great area to be in.

Erik: I want to come back to energy in just a minute, but before we leave gold, let's just talk about what happens next. We've seen a 30% correction on gold. Do you think we've got a setup now for a, a big rally into year-end where we get back to new all-time highs? Or is it gonna be a slower Slog than that?

What do you think?

Michael: I wouldn't want to bet on new all-time highs by year-end, but I think that the trend is in place. There's a chart in the pack that I alluded to earlier on, on slide 20, which looks at the gold price in Chinese yuan, which in my view is the better metric to watch because China is driving this price now.

And if you look at that chart, what I've put on there are various price levels that I have historically assumed that the Chinese were targeting, rightly or wrongly, but they seem to match up. And the trend line has basically held, and that trend line, as I suggested, at 27,000 is exactly where the gold price in yuan bounced off.

It seems to be climbing higher. If you look at the pace of that trend, it would seem unlikely by year-end that you would break out to new all-time highs. But I would figure we might even get close. So I think that's something to watch. And I think the other thing which would reinforce that story is whether silver is outperforming gold.

And another confirmation sign that I tend to look at is whether silver, which is a high beta play, is rising faster than the gold price. And if that's the case, that would suggest that sentiment is coming back into the precious metals.

Erik: And what are those indicators showing you right now?

Michael: They, I think they're hinting we may be near a turn.

It looks as if silver, but we're only talking about a matter of a few trading days, but it looks as if silver is starting to claw its way back and beginning to outperform. And that would, if you like, reinforce this, this thesis. But like everything else in investing, you've got to look at many indicators and try and join the dots.

And sometimes those dots join up quite well, and sometimes they don't. At the moment, they are joining up.

Erik: Let's move back to your comments about energy prices and talk about where they're headed next. I agree with you, but I'll play devil's advocate and just say, okay, there's a lot of people who think that, we've basically had the Strait of Hormuz closed.

As soon as we get this situation under control, what's going to happen is you've had the UAE leave OPEC with the intention of basically producing as fast as they can. A lot of people think that oil prices will basically crash as everybody starts producing again, just as soon as we resolve this Strait of Hormuz crisis.

That's not my view at all, but that's the view that competes with yours. So what do you have to say to that?

Michael: Yeah, I think the starting point is to say what is to come back to fundamentals and try and argue what drives commodity markets. And in my view, and this is probably a very simple view, but I tend to hold there are two moving parts, Eric.

One of those is the currency of denomination, so let's say that's the dollar, and the other is some real exchange ratio that tells us a lot about the relative extraction costs of maybe two metals or two commodities. Now, if you take gold and oil, on page 15, there's a chart which shows the gold-oil ratio.

Now, what I've done there is I've done two things. One of those is to draw that red line, which is the gold-oil ratio on the right scale in log terms. So there's a little bit of mathematical manipulation. But I've done that so I could compress the gold-oil ratio and fit it into the long-term liquidity cycle, which you can see overlaid on that chart, the sine wave that actually was extracted from an earlier chart looking at how global liquidity moved.

That, as I said, is a five to six-year cycle. Now You probably don't need to squint too much of the chart or go too much boss-eyed to work out or to see that those cycles pretty much overlap, and in other words, that as the global liquidity cycle rises, the gold-oil ratio also rises, and as the global liquidity cycle drops, so the gold-oil ratio falls.

Now, what's the mechanism there? The two things that I would argue are that number one, you tend to find that as liquidity increases, it fuels precious metals that are a mon- obvious monetary inflation hedge, and so the gold price tends to go up with the beginning of the liquidity cycle. Then, as you start to see liquidity faltering, the faltering in liquidity which causes the inflection is all about money being shipped into the real economy.

So that downswing is largely explained by the fact that the real economies are strong, and therefore commodity demand is picking up, and therefore the oil market tends to be very buoyant. So in the upswing, the gold-oil ratio is pushed up by rising gold, and in the downswing it's pulled back by rising oil.

And if you look at those cycles, it's been very regular. Now, if you then do a statistical analysis of the data on the red line, the gold-oil ratio, it is shown to be strongly mean-reverting, and there is very limited evidence of any trend in that data. There's a mild uptrend, but nothing which is too, over the long term, since nineteen seventy at least, there's nothing which is particularly compelling.

Now, we saw in the COVID crisis exactly the same development of the gold-oil ratio spiking, and then within two or three years, it actually mean reverted again. And I would argue that we're looking at the same setup once more. Now, if you believe, and this is where one has to hold onto one's chair a little bit, but if you believe that the gold market is underpinned at four thousand dollars an ounce, maybe it's higher, who knows, but let's assume it's four thousand dollars an ounce, and we take the long-run average gold-oil ratio historically, which has been around about twenty times.

In other words, the ratio of an ounce of gold to a barrel of oil is about twenty times, and you divide that ratio into the gold price. What you find as a result is a two hundred dollar a barrel oil price. Now, that may be way, way off the scale, and I fully accept that, but I think let's just play around with the numbers.

We're just triangulating here, so it's not really a projection. It's just saying, what if? So if you believe that gold-oil ratio is stable, and history is very much on the side because this is a real exchange ratio based on relative extraction costs of those of those two minerals, then you've got to say that if it's not twenty times Maybe it's 30 times, maybe we accept that, and then but you still get an oil price of $135 a barrel, so substantially above where we are now.

So all I'm doing is triangulating and saying what if, and recognizing the fact that gold is probably going up, at least on my estimation, and the gold-oil ratio has shown very long run stability.

Erik: You've made a very persuasive argument in favor of higher oil prices and also in favor of higher bond yields.

I agree with you on both scores, and I think that those are self-reinforcing. You get higher oil prices, it tends to be inflation-inducing that results in higher bond yields and so forth. So it all makes sense to me, but hang on a second, Michael. If we get to substantially higher bond yields, we're gonna bankrupt the US government's ability to service its debt.

What happens then?

Michael: I think equally, yes. Th- these are tricky moments because the other thing to throw into that, Eric, is that if oil prices do jump, that's normally been an ending feature of bull markets. What we're saying here is that you've got rising bond yields, not good. You've got rising, potentially rising energy prices, not good, and therefore one ought to be scaling back beta exposure within equities and risk asset markets, and that's pretty much where we are.

Now, if you come back to the mechanics of what's driving the bond markets and where we're gonna end up, I'd suggest you take a look at a chart I put on slide 24 Five, which is looking at the drivers of the US bond market. Now, what that is illustrating is in black, the black line there is showing the four-year moving average of NGDP, which means nominal GDP, so that's the real bit plus the inflationary element on top, and this is a four-year rolling average of that growth rate.

Now, what I've put on top of that four-year moving average is the 10-year bond, 10-year US Treasury bond risk-adjusted, so I've just taken off an estimate of term premium on that for those that are wonkishly inclined. But it's really telling us the underlying level of interest rates over that 10-year period.

And you'll see those two lines really match very closely, and the only period they didn't was actually in the beginning of the period where you saw the Treasury Fed or up until the point where you got the Treasury Fed Accord, where after World War II controls and yield curve manipulation, the Treasury was basically...

sorry, the Fed was allowed by the Treasury to set monetary policy more independently, and then you see the bond market and nominal GDP aligning, more correctly through this period. What we're seeing now is a period whereby nominal GDP, the growth rate is accelerating. I would argue it's somewhere between a six to eight percent range.

I think the huge fiscal spending in the US, the AI boom, and the effects of de-globalization on CapEx and inventory build are driving nominal GDP higher. That means both higher inflation and stronger activity growth. But that is pulling up bond yields, and you can see from the extrapolation that it's not impossible to see the 10-year bond testing six percent yields, in the not too distant future.

So that's clearly gonna be a constraint. How does the Treasury get around that? I think it's a difficult one, and this is a, a problem that I wouldn't like to have But it basically means that if they if they want to fund, they may have to go to the front end of the curve. We've got a situation where right now 22% of outstanding debt in the US federal debt is Treasury bills, so it's very short-dated government paper.

That may go up. It could go up. The Treasury have indicated that they, or originally indicated they had a preference for a range of between 15 and 20. That's now been exceeded, and it may go up to levels that we last saw in the early 2000s, which were nearer 30%. That would be significant to the markets if they did that.

It would be really bad for the dollar, in my estimation, and it would cause the gold market to shoot up. Never say never. Scott Bessent has clearly come out against that policy in the past. The fact is that when push comes to shove, that's the policy he has been employing over the last couple of years.

So he's been following the Janet Yellen line of funding through the bill market, and that almost behoves the Federal Reserve to keep liquidity at the front end of the curve ample, which is what they say they want to do.

Erik: Michael, let's tie the Japanese yen into this. It seems like the yen has been a factor in quite a few of these trades.

What's controlling what here? Is it t- tail wagging the dog, or is the dog wagging the tail here?

Michael: I think again, if you look at what's happening in Japan, is that bond yields are rising after a period of yield suppression. The Japanese are stepping back and letting the long end of the market reprice properly.

If you take a look at a slide on page 28, it basically shows what's happening to the 10-year JGB bond, which is the orange line, is catching up with nominal GDP growth in Japan. And the shaded area of that chart is where they had basically a yield suppression policy, which was the yield curve control or QQY policies as well.

Now, what you can see is that underlying economic growth in Japan, nominal n- nominal GDP is over 4%, and that would suggest the long bond there, or the 10-year JGB rather should be there closer to 4% than 3%. And clearly it's climbing. Now, the Japanese authorities are trying to hold that down by keeping short-term interest rates low.

They're reluctant to raise rates. This is a story that we could equally put to Fed Chair Warsh. Again, if he doesn't raise interest rates, what are the consequences? And the consequences are a, a yen sell-off, and that yen sell-off is gonna keep going until they decide that they're gonna tighten monetary conditions.

And this is the problem that we have, is that if you don't if you don't address these problems and you keep funding at the short end, this is basically monetization by, in writ large. Banks buying government debt, which- whichever stripe, be it bills or bonds or notes, is monetization. And the huge issuance of debt in all these economies is being sucked up by the banks, and they're effectively printing money, and this monetization is causing currency turmoil in, certainly in the case of the yen.

And what they need to do is to raise rates But they aren't doing that, and that's a lesson for for the US. This is what could go wrong.

Erik: Michael, final question, speaking of the US and what could go wrong. Where do we stand in the Fed's in the US Federal Reserve's hiking cycle, and what should we expect as the next policy decision?

Is it a Fed hike or a cut?

Michael: I'm-- my view is 100% that it's gonna be a rate hike. If you take a look at slide 30, which starts to delve into what's happening in the US markets, what we chart there is SOFR overnight rates, which is the black line. That's the nearest thing to Fed policy rates, Fed funds.

It's really the, the rate that is the main financing rate in the repo markets, the overnight rate. And the orange line is the two-year Treasury note yield, which has always been a particularly good predictor of what's gonna happen to policy rates. I ran this data through AI, for what it's worth, and I said, "How accurate is the two-year note as a predictor of policy rates?"

And the answer that came back from the AI model was it's correct 85% of the time. And that's on the upside and the downside. So what this is indicating is that rates are gonna go up. And if you take a look at the following chart, what that shows is SOFR rates, that spread of SOFR less two-year yields for this cycle in orange and for the 2020, '23 cycle in black.

As I recall, if you go back to the end of '21 on that chart and look at what is happening, that big drop in the black line signals a tightening of monetary conditions in the US, and that was a big sell-off between January and October of 2022. And we're maybe not going as fast down that cliff edge, but we're certainly starting to move.

We're hovering over it, and that's clearly the threat. And if you put that everything together, the slide on page 33 is then looking at Fed tightening cycles. And what we've done is to look at the existing cycle, and this is looking at everything, throwing everything into mix, looking at our liquidity data for what the Fed is doing, what the Fed balance sheet's doing, et cetera.

That's the do- the broken dotted line, and that is following a path that looks remarkably similar to the average cycle over the 1985, 2025 period shown in orange. And if that is true, we've got at least another six months of intensified tightening by the Federal Reserve to go before there is any hint of an inflection.

Erik: Michael, I can't thank you enough for a terrific interview. But before I let you go, please tell our listeners what you do at Global Liquidity Indices, what services are on offer there, and where people can follow your work.

Michael: Great. Thanks, Erik. Yeah. GL Indexes is basically the company which is supplying data.

We produce indexes and data on liquidity worldwide. We cover 90 countries. We have recently expanded that into a daily nowcast of liquidity for all of those countries. If you think liquidity is important, that we have the data to show it or to prove it, and that's what GL Indexes does. The other hat we wear is Capital War Substack.

That is a regular report or series of regular reports. We write about three reports every week on providing data and narrative about what's happening in markets.

Erik: Thanks, Michael. Now it's time for Patrick Ceresna and Massil Beguenane to join for our Macro Voices Market Desk segment, which begins with Patrick turning Michael Howell's market outlook into a risk-defined trade.

Patrick, where's the trade?

Patrick: Thanks, Eric. So for this week's Trade of the Week, I wanna focus on gold. Now, Michael clearly remains structurally bullish gold, but tactically he thinks the correction may be approaching an inflection. So when I'm thinking about a trade construction, I had to think about timeframes.

In this case, my focus is on the interim tactical opportunity, looking for the next leg higher. So what I love about this opportunity when using options on gold is that gold has a steep right tail skew. That means calls are relatively expensive the farther you go out on the strikes. That lets us sell the expensive upside volatility to subsidize the call we're buying.

Better payoff structure than simply buying the call out, right? And that's why today I wanna put this on as a traditional bull call spread. So our trade thesis is that gold will continue recovering for the next two months, and particularly I wanna target that April high on the GLD near four hundred and fifty dollars.

I also wanna make sure I give it enough time by looking at an option that's about two months out into the future. So let's look at the trade mechanics. The GLD, which is the SPDR Gold Shares ETF, is trading around four hundred and five dollars at the time of this recording. Now, I wanna focus on that October 16, 2026 expiration, which gives us about 65 days in the trade.

Now, I wanted to buy a four hundred and ten dollar strike call option, which is about five dollars higher than where we're currently trading, which costs around fifteen dollars. Now, I wanna then subs- subsidize the cost of that call by selling that four hundred and fifty dollar strike call, which is currently bid four dollars and fifty cents.

That gives us a net debit cost of about ten dollars and fifty cents on a forty dollar wide spread. So just, again, to put that into simple terms, we're risking about ten dollars to make about thirty if we are right. That's a, a very close to a three-to-one payoff Now the max payoff, of course, is if the GLD in the next two months is able to make it up to the $450 strike.

But what I love about this trade is there's a very defined downside. The premium which we paid for the spread. So with the fact that the GLD has already rallied close to 40, $50, there's all sorts of downside volatility that can happen, retesting lows, and this gives us that defined structure. So we're using that rich right tail volatility in our favor, that defined risk and being capital efficient.

So for tactical traders looking to participate in Michael Howell's bullish gold follow through, the skew lets us build a defined risk structure with almost three to one upside. That's Where's the Trade?

Erik: Patrick analyzes and trades the markets every day over at Big Picture Trading. Macro Voices listeners can sign up for a free two-week trial at bigpicturetrading.com.

Now back to Patrick and Massil.

Massil: Yeah, I love it, Patrick. What's cool about gold is that it's still just turning out this move, so there's a lot of room to run on the upside, even the short term here. But let's turn to the equity markets here. What are we watching?

Patrick: Let's dive into this S&P 500 because last week we had that explosive move to the upside that cleared the S&P 500 to a fresh all-time high.

What is impressive about the last week is that the bulls have been more or less able to maintain that elevated level, which is price acceptance. The-- we've normally if that kind of an explosive liquidity event was not sustainable, we would have seen very deep mean reversion sending us back to, let's say, seventy-five hundred on the S&P, and that's simply not happening.

We're literally bouncing along fifty-two week highs. And so right now the the market structure is surprisingly bullish, and and the bulls are a hundred percent in the driver's seat on the short-term trend. That means if there was any short-term catalyst that breaks this to a fresh new high out of this one-week trade range, we could even see eight thousand within a week or two on the upside.

So during this summer doldrums, the bull trend is the path of least resistance. Now I wanna make one note about where it would turn bearish. And this is where I think that the bulls actually have their edge because it would take a substantial decline in the tune of about four hundred S&P points to start doing this the technical price damage that would potentially trigger systematic selling and potentially reverse the trend.

In other words the bulls can easily absorb a two hundred S&P point pullback, it'd be bought on dip and just be an opportunity to trade that upside. So right now, the bulls have a lot working in their favor. Now that could quickly change in September, but right now that's where we're at.

Massil: And the positioning data does back it up.

Quick reminder for listeners, this COT report does reflect positioning as of Tuesday, August fourth. So anything after that, you'll have to wait for tomorrow's release to see this week's changes. But on equities, the data that stands out the most is that the Nasdaq is still lagging, and you can obviously see that in the chart.

But the Dow and the S&P, fresh new highs, but the tech-heavy Nasdaq just hasn't joined. Look at the positioning data. The SPX speculators is sitting at the ninety-sixth percentile of positioning on the one-year basis, while the Dow is even more extreme at ninety-ninth percentile. But the Nasdaq, still near zero.

Now, if you go to the market deep dive, you'll see that the Nasdaq positioning went short another twenty-five thousand contract, and that took the net short thirty-five thousand contracts. What's cool about this is that it's all new shorts coming into the market, not positioning that changed of, current positioning.

When you compare that to the SPY They're only down nine thousand contract shorts, and the Dow is even positive at six thousand contracts long. So we're pretty net-net on those two assets. So to me, the real question is, do the semis and even the tech as a whole finally come back and participate in this rally?

What do you think about that, Patrick?

Patrick: The observation I would make there is a lot of that short positioning in the Nasdaq could very well be a long-short pairing against people that are way overextended on semiconductor and Mag Seven exposures. Now, what is interesting is that bullish impulse that we did see at the end of July that drove this rally was very well led by the hyperscalers and these Mag Sevens ripping to the upside.

But what is notable here is the lack of participation in this rally in the semiconductor space. Now, certainly they h- were huge leaders on the upside, and they are clearly where the money is rotating out of at this stage. Overall, if the S&P is heading to eight thousand on the upside, it is going to need the Mag Sevens participating, and so watching whether or not they will be bought on dip here and continue to press is gonna be huge in terms of whether or not the S&P has the fuel to get to that eight thousand round number.

All right, now I wanna move on and talk about this US dollar. Now, over the last two weeks, the US dollar's been mean reverting its prior bullish trend. Now, overall, we actually are structurally still in a bull trend on the dollar. Now, one of the biggest drivers of why this move happened was the big yen intervention in Japan.

And that drove that US dollar yen to drop from the one sixty-four handle all the way down to one fifty-five. And that really was this burst. But now what we've seen is the US dollar yen has now fifty percent retraced. We're basically rallied back about half of that huge intervention loss.

And so we're now actually a really interesting inflection point. If the US dollar is going to continue to weaken we should see the yen once again rally here and the US dollar to break down against this. And as well, we should see that correspondingly shown on the Euro USD chart. And I think that it won't take more than a week or two to find out whether or not the US dollar is meaningfully reversed or whether this will be one big buy on dip.

Massil: And you're totally right, Patrick. The whole story is in the yen pair because we saw extreme positioning on the short side in the yen for the better part of two, three, four years even. And that yen intervention forced a bunch of those short sellers out of the market. A hundred and eighteen thousand contract move in just one week on the long side.

That's not only the biggest weekly change across all markets on the COP report, but it represented twenty-five percent of open interest that shifted just like that. That's one in four traders being forced out of their position. And that obviously explained the violent move that we saw just two weeks ago after the intervention.

Now, even with that huge move, yen positioning is actually still net short, so more short covering is still possible. So I'm super excited to see what's gonna happen over the next few weeks. Now let's move on to crude oil

Patrick: Interestingly, crude oil has actually been quiet here over the last few days. We've really settled in around that fifty-day moving average and really we have not seen any big explosive move.

Clearly, the situation in the Middle East continues to be fragile and certainly, there's big debates as to who's really in control and how much oil's actually flowing through the strait. The one thing I would generally conclude is that things are clearly not back to normal and the oil markets continue to be stressed.

That to me implies that there's lots of room for the fair value of oil to be at an elevated level. I think that as we beat this eighty level, there's a very reasonable chance that we're going to stay in the eighty-plus dollar area with lots of room if on a headline-driven scenario where we can make it back to the ninety-dollar level where we were just trading a couple weeks ago.

And so generally I think oil has room to strengthen and I don't really see the scenario where oil heads back to the June low near sixty-five dollars.

Massil: Yeah. Positioning has largely stayed the same here on crude oil, whether you look at the WTI or the Brent. But I wanna talk about gold 'cause we've seen a big move in precious metals this past week.

What do you see here?

Patrick: A lot of people are very excited about this breakout, a 10% move in gold very quickly. Clearly, we already talked about it during the where's the trade. But what I'm certainly gonna be watching here on gold is how do the traders behave when we inevitably have a little bit of profit-taking.

If this was a meaningful turn in the, the bull trend in gold, we should see all dips being bought, moving averages defended, and generally the price action remaining structurally accumulative. Overall, it was a very strong breakout. The first real sustained period above the 50-day moving average since late April's bounce.

And so it'll be very interesting to see whether this is in fact the inflection point for the potential beginning of a new gold run.

Massil: Yeah. On the positioning side, gold moved to neutral territory, but silver remains underowned. Like here, large speculators are near the zeroth percentile on the positioning for the last 12 months.

So if this is a turn in precious metals as a whole, we're still in the first inning of this move. Now, listeners, if you wanna see what I'm seeing, don't forget to visit cotsignal.com so we can start following the data along with us. Now, Patrick, is there any other markets that were super interesting this week?

Patrick: Listen, we gotta quickly touch on uranium. Now for the last three months, uranium has been completely dead. On the future side, we were trading basically between the $85 to $87 level flat-lining. And f- for the first time in three, four months, we're actually seeing the uranium market upticking.

And what's particularly interesting is that when all the mining stocks came to life a few weeks ago the uranium stocks up- turned up during that time. W- in the URA, which represents the basket of uranium producers, we had almost a 25% trough-to-peak rally here over the last two weeks. This has allowed the uranium stocks to reclaim their 50-day moving average and potentially have turned the trend.

Now the one week like this does not make a new trend, but it is the first time we've seen some positive price action since early second quarter. One-- we're gonna definitely be watching whether this is that key turn point for a new accumulation cycle to begin. And Mass, while we've gotten most of the major assets out of the way, what else caught your attention on the COT reports?

Massil: For sure. Look at what's happening on the bond side. Look at the two year and the 10 year. When you look at the one-year range, the two year's sitting at the hundredth percentile of positioning. But when you go to the middle end of the curve to the 10 year, we're seeing it at the zeroth percentile of the range, just the complete opposite.

So you've basically got two very different stories depending on where you look at the yield curve. What's your read on that?

Patrick: It's clearly just all about central banks because the, the two-year note is very closely linked to the Fed path and whether or not Warsh is going to be raising interest rates.

It's very interesting. We had just weak jobs data and now an inflation number that came in line. What's interesting is when you look at Fed funds futures, clearly the idea of a September rate hike is slowly being walked back. We were at a greater than a fifty/fifty chance that Warsh was gonna raise here in September, and now there's almost a two-thirds probability that they're not gonna move at all.

What makes this particularly interesting is that there's only three Fed meetings this year left, and if they don't move in September, then the October meeting is literally within one week of the election. So there would need to be some very clearly sharp data for the Fed to feel like they're gonna move into a political election.

And therefore the-- what all that would be left would be a potential Christmas rate hike. What-- even though the current Fed funds futures are giving the most probable outcome that there's going to be one full rate hike this year, if they don't move here in September, I think that a lot of stir traders are gonna start walking back that the Fed may even move at all.

And so this makes it super interesting because the two-year note, like you were highlighting, has had substantial short covering as a lot of the gross shorts are closing, as many feel that the Fed is much closer to the end of this hawkish cycle, or at least it's starting to be priced that way. But that's not what we're seeing on the long bonds.

The thirty-year yield is almost at five and a quarter and continuing to press highs as the long bond continues to just have a vicious downtrend and and the shorts continue to pile in on on pressing that long bond. It'd be very interesting to see whether or not we get a bull steepening, but clearly the way traders are positioning at the front of the curve versus at the back is dynamically different.

All right, Mass, let's wrap up with just touching on the positioning pulse. What else caught your attention on those COT reports?

Massil: All right, the market that I'm watching this week is wheat because there's a pretty interesting setup building here. Now, I want you to look at the market deep dive on the wheat on cotsignal.com, and that's the first chart on the top right, right?

When you're looking at contracts, you would've seen that large speculators went from basically flat to about 15,000 contracts net short in just one week. But the part that I really care about is how we got there. We saw roughly 11,000 fresh new shorts come into this market. So this isn't just people getting out of longs.

You've actually got new money coming in and betting that wheat goes lower. But here's where the timing matters. As I said earlier, the COT data only captures positioning as of last week, from Tuesday, August 4th. So all of these new shorts were put on before this latest escalation in the Black Sea. And for anybody that doesn't know, just two days ago, we had reports of attacks on major Russian grain infrastructure, and Russia right now controls 22% of global wheat exports.

So if you start disrupting Russian exports, that can become a global wheat problem pretty quickly, comparable to the lead-up to the 2022 Russia-Ukraine War. Just yesterday, we saw the price react to the news, which helped wheat futures hold its 50-day moving average and is also bouncing right off the fib zone.

Now, the way that I'm looking at this is that you got traders getting more bearish on wheat at the exact same time that the risk to physical supply is going up. So if the Black Sea situation gets worse, those same traders who just sold wheat may suddenly have to buy it back. Now, I'll be keeping a close eye on this market myself.

If you wanna follow positioning behind it, it's all on cotsignal.com. It's free, and it's updated every single Friday.

Patrick: You know what's also interesting is that same type of a chart pattern is there on the soybeans and on corn. And so the entire ag space is certainly looking like it's setting up for some sort of food shortages and potential bullish price action.

It's certainly something I wanna keep watching. All right so that's where we're gonna wrap things up, and that's this week's Trading Desk. I'm Patrick Ceresna.

Massil: And I'm Massil Beguenane. See you next week

Erik: And a reminder, as a Macro Voices listener, you're entitled to a two-week free trial of Big Picture Trading, where you can watch Patrick analyze and trade the markets live every single day at bigpicturetrading.com.

No credit card is required to sign up and there's nothing to cancel. I'm Eric Townsend and this is Macro Voices. We'll see you next week.

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