

Gratuitous Specs

How about some end-of-summer provocations? We have two. Neither should be expected to happen but both have a greater-than-zero percent probability of occurring in the coming months (despite Senate Majority Leader McConnell saying the second one has zero chance). Both would be high impact events.

First, a diplomatic-military solution to a vexing problem: Russia bombs and neutralizes North Korea. It then hands oversight of the country to China and/or NATO, with the exception of a sovereign military bases it keeps for itself (a la Guantanamo). Imagine Kim's (very brief) surprise. Imagine China's pique amid new checks on formerly uncontested power. Imagine Russia's reinstatement into the community of nations and its new global soft power. Imagine Putin's glory and Trump's fabulous parade of historic proportions down Fifth Avenue. Imagine the deflationary impact on Korean body massages.



Second, the US House of Representatives blocks raising the debt ceiling. The Freedom Caucus and more conservative Republicans decide they have a better chance of reelection by favoring voters in their districts over corporate donors (i.e., government contractors). Their calculus is that they would not be able to successfully stand for reelection in 2018 if they have not repealed Obamacare AND have agreed to let the federal government sink deeper into debt. They will tell their voter bases that payments to government contractors will be curtailed rather than curtailing social security payments or letting the US default on its debt obligations.

Both scenarios are identifiable tail events, but we would not bet the farm on either of them occurring. Given that the potential payoff is greatly asymmetric, a small bet on rising volatility or a directional bet in certain sectors may be warranted for those already leaning that way and willing to speculate.

Paul Brodsky
Macro Allocation Inc.
PostModern Partners

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