Richard:	00:01:58	Welcome.
Adam:	00:01:58	Happy Friday.
Richard:	00:01:59	Happy Friday, boys.
Mike:	00:01:59	Happy Friday.
Richard:	00:02:00	Welcome, Alex
Alex:	00:02:01	Thank you. Thank you for having me.
Mike:	00:02:04	And before we start, because I think we're going to jump in pretty quickly, I think everyone wants to get to the discussion part. But disclaimer, this isn't investment advice. It is for educational, informational purposes only. And with that, I'll kick it over to you guys.

Backgrounder

Adam:	00:02:22	Okay. Well, let me just very briefly introduce our guest, Alex Gurevich, who obviously needs very little introduction for most people on this broadcast, I'm sure. Alex is the author of two incredible books on trading. One is *The Next Perfect Trade*, and the other is *The Trades of March 2020*. And so I'm sure we're going to want to get into both the historical experience that informed the writing of those books. And of course, we're going to dive into some of the incredible dynamics that are in play right now and driving markets and maybe get Alex's insights into how people might want to position and manage risk and maybe harvest opportunities at the moment. But before we get started, Alex, can you maybe just give us a couple minutes of background and where you come from and how you got into this nasty business?
Alex:	00:03:27	Well, my educational background is mathematics. I've always wanted to be a mathematician. And that was one of my gateway drugs. And my other gateway drug is that I was always interested in competing, academic competitions and strategy games. I grew up in Russia. I left Russia in 89 when I was in the middle of college. But back then, of course, I learned to play chess and I competed in chess. And then I started to play the Japanese and Chinese game Go, very serious and compete in that. And then later I learned poker and a whole bunch of other strategy games. And that really combined with my analytical approach to make kind of a perfect setup to have a Wall Street mind, so to say. It was very natural for me to think of like, oh, what can I do with strategy? Oh, financial markets, that's a perfect place to be. So, my natural path was always to be a mathematician. I got my PhD in the University of Chicago. And it would be a subject for a whole separate podcast to

discuss how you choose career paths end up on Wall Street versus academia. I made the choice to go on Wall Street, partially because I felt I found my measure in academia and I've proven myself there. And I've had good results and good kind of traction there. But I also knew, like, where is my floor and where is my ceiling so to say. And I felt I want to go and try this other thing. And I was interested not on being a quantitative analyst. I was interested really to trade. So, I wanted to implement strategy. I was very adamant that I would not like equations on Wall Street … Nothing wrong with people to do that. I have some friends who did extremely well doing that. It's just not what I wanted to do ever.

And I started at Bankers Trust … Deutsche Bank. I made one move to Chase for my senior job. My starting jobs were basically customer fixing … desks, I had some encounters with various, less liquid derivative transactions like index swaps, like I really got into asset swaps. And I started municipal index swaps, for example, and I did bond options, including even mortgage and agency and some exotic options. So, in Deutsche Bank, various, wide range of trades. I know that my first senior job at Chase when I ran the … franchise, and then launched the agency bond asset swap franchise. I actually started trading them as a package in 2001 at Chase, which became JPMorgan Chase. And did this for a few years I started. Then I went to proprietary side and global macro portfolio. I'm doing very, very abbreviated career version. And this is when I was running a global macro portfolio as part of the global currency and commodities group JP Morgan, this is where really my strategy started to coalesce.

And when I later went on my own and started to do various things on my own, over time, I started to articulate the strategy more and more and be more and more rigorous about how I implemented, and eventually I wrote a book about it. The first book, you mentioned, *The Next Perfect Trade*. I wrote most of that in 2014. It came out in 2015. And it's been very relevant when it came out, because some of the patterns I observed there are very interestingly manifesting now. So, there will be stuff to talk about there. I soon thereafter, I started to take client money again, and launched my current firm, HonTe Investments.

And the experiences of 2020 led me to writing another book, *The Trades of March 2020*, which is just basically trying to have this fly on the wall view of what it's like to descend into the case of pandemic for financial markets. Kind of the idea was of that book, this is the book, and I'm sure you'll bring it up more, but I just wanted to show you *The Trades of March 2020*, … best seller. The idea of this book is to kind of let aspiring traders be like medical students being led in the operating room. You can really see blow by blow what is happening, you can read the trade chatter with all the curses, all the screw ups. That was their kind of intention.

But it's also, I think, interesting to my peers, because they can compare notes. And it's interesting to broad audience who's just interested what the hell is going inside hedge funds is beyond what movies show you. I think my book is really unique in this way, because of the transcripts that I use that people can see fruitfully, like without any bias what is really going on inside. And now we're on to the new crisis and I'm to navigate the next big thing

The Next Perfect Trade

Adam: 00:08:30

Okay. Well, let's go right there. Because you mentioned something from *The Next Perfect Trade*, and that you are seeing patterns right now that align with some of the frameworks that you laid out in that book. So, what was the general premise of *The Next Perfect Trade*? And then how do you see some of the patterns that you were talking about in that book playing out currently?

Alex: 00:09:00

Okay. So, this is a good place to start. The general premise of the book, *The Next Perfect Trade*, that there are certain parameters that you can judge trades …. because very often we say like, oh, that was a great trade, we made so much money or this was terrible. I lost money, right? But how do we actually go through the trade -- trade selection process has to happen before you know the outcome. And *The Next Perfect Trade* was really focused on the trade selection process. And I try to identify factors which are as non-speculative as possible.

And full disclaimer, we're speculators, we're going to speculate. I always tell my investors I'm not there to hold your assets. I'm here to buy low and sell high. Doesn't matter what your time horizon. It could be 20 years or two months, you're still a trader. If you're trading, you're a trader. You buy low, selling high. So, as soon as you speculate, how do you turn the odds in your favor, how do you try to be house versus, like in a casino versus the gambler. And there are certain parameters that tend to turn trades in your favor.

And I was going through chapter by chapter in the book *The Next Perfect Trade*, and one of the important parameters of this chapter was historical patterns. Things happen in certain patterns, like certain things lead to certain things. They don't have to repeat, but much more often, I'm surprised about how they repeat versus how they don't repeat. Much more often, I'm surprised when you think like, oh, this time is different, it ends up being no different than the time when you get surprised, but it's different. And both surprises happen. So, what I find is that the odds are very strongly skewed when you observe, this is just one chapter out of like 15 chapters in the book, right, … But odds are very strongly skewed when you observe certain things. And there are certain things that are observable in the current markets, which I used, also successfully in 2018.

So, my book, the next book, *The Trades of March 2020*, I set a little bit of background for how I was thinking -- what I was thinking about in 2020. And early

2018, I started to observe signs of late cycle, various patterns that repeated in the past. As markets go, economy goes on the life cycle and market is about to roll over into the recession or slowdown … for me, I don't trade GDP, GDP is not an asset by itself. I generally care about what happens to interest rates, more than anything. I come from a background of interest rates. For me, that's bread and butter. Equities are sometimes harder to gauge. And it's very hard to be short equities because stocks on average go up. And it would be in short just … to be squeezed again and again. But fixed income has been good, because you can just say like, okay, what kind of things show that interest rates are about to go down? And I saw a lot of that while price was still hiking in 2018, I saw a lot of the indicators.

Richard: 00:12:09 Give us some of those specifics if you wouldn't mind like, are you looking at the repo market? Are you looking at the shape and the slope of the interest rate curve? Walk us through some of the features that you're watching.

Alex: 00:12:20 Well, I'll focus on things which are actually repeating today, if you don't mind. One of the interesting, like the sharp rise in oil prices, has been -- and there's been a debate on Twitter and people like doing yes or no one sharp rise in oil prices as foreshadowing of recession. And again, if I told you this today, and it's the first time I did work on it, it would be spurious. But I did that work in 2018. And I wrote in my investor letter in 2018, showing how rising oil prices has a pattern of foreshadowing recessions. So, that's for example, one thing. Another paradoxically, strong employment, very strong employment, very tight labor markets typically foreshadow recessions. And there is a logic there, because once the labor market's tight, you cannot grow anymore. Now there is some argument whether the labor market is now tight or not. Because some people say it's tight, but it's not really tight, it's because of low participation. But it acts as if it's tight and in the past, that was foreshadowing lower interest rates.

Yield curve, it's a little -- I have a little different attitude towards yield curve, it's definitely to be looked at. And I did notice the fact that whenever yield curve goes inverted, like my one of my favorite saying, whenever yield curve is inverted, it's not inverted enough. So, right now, the market shows easing in 2023-2024. Whenever that shows that, not only it will occur, but there'll be much more … price. I don't know precedence on market aggressively and continuously price easing didn't happen. How that pressures works.

But my theory, I'm a little cautious of the yield curve indicator, because I think, long ago, I made this example, if you're falling off the 20th floor of a building, flying by the 10th floor is a really good leading indicator that you're going to hit the ground. You should already be knowing that you're falling. When yield curve invert, you should already know that something's off here. So, there are disjointed equity price actions like disconnecting between different equity markets and sectors re-diverging from each other is also a sign of late cycle, for example for me. And I don't know, would you agree or disagree? People here probably know more about equities than I do, but it feels like there's some sector divergence happening

Adam: 00:14:55 But they definitely see some rotation.

Alex: 00:14:56 Yeah. It's a difficult -- I'm a little cautious with those statements because it's so easy to make a statement, there's some rotation, because there's always some rotation, right? But some, the feel of it., this is more art and science here, the feel of it is late cycle-ish for me. So, those are the type of examples. I don't want to spend a ton of time on this, because I've been pounding on this indicator for a while. But my interest rate momentum indicator is flashing absolute red for stock market.

Adam: 00:15:29 Red you said?

Alex: 00:15:29 Red? Yes, like very negative predict -- I've never been -- seen my favorite indicator being basically as negative for stock market as it's been in my career.

Adam: 00:15:42 What indicator is that?

Alex: 00:15:45 The difference between 10 year yield today and two years ago and today, very simple. Has the 10 year yield risen or fallen over the last two years. And the theme of that chart and what is also very relevant, that I published the chart first time in my first book in 2015 and I saw the amazing theme. And then since then, and I charted it, and since then the theme continued to be amazing. So, add kind of the current theme, 70 years of data, which I could not have known now confirming my pattern. And the pattern has been amazing because think about this what like if you think what happened, 2013-2014 taper tantrum rates have risen. 2015-2016, two years later, we're having industrial recession and Brexit and correction markets.

What happens in 2016? Rates have fallen. What happens for the next two years, 2016 to 2018? We're have a rising stock market. What happens in 2018? Rates have risen versus 2016. What happens next two years? We're starting to have trouble with stock market long before COVID, 2018 was heading for a kind of correction then we're having COVID bear market. What happens in 2020? Rates have fallen. What happens next two years? Extremely bullish stock market. What do we have now? Rates have risen.

Energy Intensity and Recessionary Risk

Adam: 00:17:11 So, let me just pull on a couple of the indicators that you have mentioned here. Let's start with a rapid rise in oil prices, and we've observed the same phenomenon the same pattern where a 50% year over year or greater than 50%

year over year, rise in oil prices, rise in gasoline prices has pre-dated recessions and stock market corrections in the past. Some of the sell side analysts have been putting out decks that show that there's been such a decline in energy intensity over the last decade or two, especially in Western markets where you just need fewer units of energy inputs. So, in other words, fewer barrels of oil or gasoline, three units of natural gas to produce the same amount of GDP growth. And therefore, the rapid rise in gasoline and energy prices may not have the same recessionary causal impacts this time around. So, maybe just let's knock down a few of the more common arguments against some of these more commonly recognized indicators of recessionary risk. So, any thoughts on that, the decline in energy intensity, and the fact that that may not trigger recession in this case?

Alex: 00:18:38 I don't think I have the power to knock down those arguments. There is definitely a decline in energy intensity. And they're also compared to decades ago, US has less, has become less centric, has less energy dependence, we're actually not energy dependent, right? We could export energy, we don't have to import energy. All of those factors are so, and all those factors could be adjusted. But I want to go back to my earlier point, patterns have higher chances of repeating than otherwise. And what I'm thinking that it's not necessarily that the energy is dragging on global economies, it's just the kind of conditions that cause the rise of energy are typically concurrent with pre-recessionary conditions. It's like what's going on in the pipelines of the world, which causes energy to spike, is usually the type of things that go on before the growth rolls over. That's my kind of justification. I'm not going to --

The mechanics of how, where the oil price on itself is going to cause the recession in the United States. In some sense, I don't see that mechanics. I'm not going to -- I don't think by itself that's recession. I think you could even argue it's inflationary because we have a lot of like, energy producers and their bonds will do better and whatever. But the sharp rise, it may be even that the sharp rise on energy for example leads to quick restructuring of energy demand and energy industry, that it leads to subsequent sharp decline in energy and we can talk about this. For example, I put an increasingly high probability an absolute crash on energy in the next couple of years and we can talk about why. And that could be the recessionary situation, because there's a saying that the best cure for high oil prices is high oil prices, because we will start producing more, rethinking the infrastructure. I mean, other countries start increasing production, increasing domestic production, energy independence, and then two-three years later, you have prices way lower than the forward curve implies. Not brave enough to be short oil, necessarily here, because the … is already very strong. So, you have to be very brave to short different oil. But the possibilities, how that plays out are rising.

Richard: 00:20:53 To the extent that you don't necessarily see sometimes fundamental reasons why some of these patterns do repeat themselves, to what extent do you think that there is a component of self-fulfilling prophecy to some of these things? Like, the behavior of investors once they see a certain price dynamic will then lead them to act in a certain way. So, how do you think about that continuum between fundamental dynamics at play versus sort of behavioral/expectation reasons?

Alex: 00:21:29 That's a good question. There might be some aspects of self-fulfilling prophecies. Most of the indicators I don't think are self-fulfilling prophecies. Because even again, in my first book, I talked about the fact that I called the negative predictive power of interest rate futures. What I meant by that is, the more interest rates are projected higher in the future, the lower they're actually likely to be, and converse. So, when we were in 2020, the rates were like zero, zero, zero forever. That was a little bit of hindsight, an excellent predictor that actually hiking will start much earlier than people realize. And right now, hike, hike, hike is an excellent predictor that rates will be zero in 2023, which is my central view currently, by the way.

Adam: 00:22:19 So, is it just that the market now is conditioned to do the work of central bankers in advance of the central bankers actually needing to raise rates and/or run off their balance sheets? What is the underlying dynamic there that causes this, changes in rates to be such an inverse indicator of what to expect going forward?

Alex: 00:22:52 You know, I think a lot of this has to do with the kind of human conditioning, which is even for smartest humans, and very hard to avoid. And even I'm often subjected to that conditioning, even though I talk about this, and I'm very aware of this. It's a conditioning that people very much have the feel that the environment that is currently now will persist further. It's a very fundamental, strong feeling. Like when, for example, if there is like a COVID wave, we're like, okay, let's hunker down, this is where the COVID is worst. While for example, with the height of COVID wave that's already where, it's going to come over and come off, right.

And it's been like, a lot of those things during pandemic. The example I gave, actually, in my second book, was, if you walk on the beach, and there's a narrow strip of land, and you see the wave coming in, waves coming in and out, and you want to run through this without getting wet. Now, if you're going to wait for the wave to start receding, you're going to start running, the wave will come in as you're running and get you wet. What you should do, you should start running when the wave is still at the high, knowing that it's going to start receding as you're running. And you'll run in the gap of time when it starts receding.

So, it's very hard to think about this this way in the markets. So, what happens is, people are saying things like inflation is high and the labor market is hike, hike, hike, usually it's at a time when those things are already things of the past. That is currently my, again, possibly flawed but biased, or if you wish, my bias towards the situation. I think this whole inflationary scare is a thing of the past. That's something that did happen and worrying about -- and to me, like I feel like I'm in some kind of weird, insane world that people are talking about worrying about inflation right now. I think the worry should be very different right now, but they are worried about inflation and they are pushing up their interest rates. And I think that, as it all has happened before, it will happen the other way.

Mike:	00:24:55	Isn't it the very fact that that you have to have the overreaction in order back to zero? You have to have the inflationary impulse, you have to have this supposed reaction and potential error in policy to then have to unwind it all the way back down to a zero rate once it's realized that the inflation may have been transitory, in some sense, right? You've miss-timed the running of -- your running across the wave a little bit.
Alex:	00:25:24	Yes. And I think the economy's going to get slashed in -- Well, not necessarily, but I think the odds have heightened to us all getting slashed by this. Yes. What is interesting about this environment that I don't even know if they don't get the rates very high. Because I don't think, usually things look like they do now at the beginning of a hiking cycle. Like inverted yield curves, usually would come much later. Again, I'm not really a huge expert on studying this, but things are beginning to look like usually at the beginning of the hiking cycle, financial conditions seemed pretty loose. Dollar was, for example, in 2004, we started hiking cycle, dollar continued to weaken from 2004 to 2007. Gold had an enormous rally nothing like -- we're talking about gold rallying last few weeks, that's like nothing. That's just noise. Up $20, down $20. Goldman went $300 to eventual height of like $1,800 in the following decade. There was nothing like that going on right now. Silver went almost up to $50 and then it's back down. So, we're not seeing any of these dynamics, we're not seeing any of the dynamics. And there was nothing like 2004-2005, interestingly, market was very cautious about pricing hikes. They weren't hiking prices more than the market price. Now market started to get really aggressive about pricing hikes. It's a very deep -- and those usually, like, when market, because first market usually resist, no, no, no, they're never going to hike. Maybe like once or twice. And then like, okay, we're going to hike. 2006-2007, that's when eventually like, okay, bond market sells off and gives up, right? And that's what happens afterwards, great recession, right.
Richard:	00:27:11	And there's an argument to be made that tighter monetary policy doesn't necessarily help inflation when the source of inflation comes from a lack of supply of certain goods for a moment, and particularly heightened energy prices, right? There's no such thing as hiking interest rates in order to cure higher oil prices. So, I wonder if you might comment on that. And maybe, to what extent this might be

a political move, given that the inflationary button has been pressed. And the US President's popularity suffers from this. And as always, there's a political component to all this, or there tends to be.

Alex: 00:27:52 Yeah, that's a very good point. I totally agree. I've been talking about this a lot. It seems completely preposterous to me that the Fed is trying to, to me, like my logic, but some people disagree with me. So, just keep in mind, it's just one person's perspective. My logic, it seems completely preposterous that Fed is trying to solve supply chain inflation by raising rates, because there are several dynamics going on there. Let's assume for a second that people are really hurting from inflation, right. And politically, they have to appear to be doing something. But the remedy to this is saying like, okay, you have hard time buying things. So, we'll make it even harder for you to buy stuff. We'll hurt you even more. Then you'll stop buying it. And then maybe prices will come down. This logic seems to be very perverse to me. It doesn't make any sense.

And as for spiraling inflation argument, I just don't know, I don't think we'll have enough evidence of this inflationary spiraling or not. And however, even when people, like kind of people hurting from inflation, people don't like when prices go up, that's painful. But what is interesting, what was pointed out to me that real wages on the bottom percentage of population is actually quite positive rolls of real wages. So, actually, this last two years have been an equalizing event and it might have helped wealth and income inequality that a lot of people are complaining about actually inflationary event typically do. So, this is against paradox that people -- this is not a political statement left or right. This is more like people for a while, it was almost like consensus. People were saying, well, inequality is an issue. Now we're having a pattern that was diminishing this inequality. And now people are saying let's raise rates and crush this pattern. Just nothing really makes…

Adam: 00:29:50 Well, I'm not sure that the pattern is addressing inequality. Allowing incomes in the bottom decile to rise by15 or 20%, while the S&P rises by 50 to 100%, and housing prices also rise by 50%. I think the bottom decile is still dramatically behind in terms of their ability to pursue the American Dream. So, it is nice to see that the lowest wage earners are catching up a little bit after two or three decades of falling further and further behind. But I think we have a long way to go. And one thing that the very least you can say, about a more hawkish Fed is that it will deflate current global asset bubbles, and therefore, potentially put assets within reach, productive assets with attractive yields in reach of millennials and Gen Z's, and allow for household formation for millennials and Gen Z's, who currently are completely priced out of any options for shelter in most US, Canadian, and many European cities.

So, I actually just to turn that into a bit of a question, I'm just wondering whether maybe the Fed decides if they're a little bit more dovish on rates, and instead, they may move to maybe preserve rates a little lower than the market is currently anticipating, but allow for more aggressive balance sheet runoffs. Have you contemplated this?

Alex: 00:31:33

Yes. I've been thinking a lot about this. So, on your question, yes, your argument, first of all, the first part of the argument, yes, it makes sense. And you could argue back and forth on this. All I was just trying to say that if the rise in real wages on the lower percentile is a desirable thing, then you should take care not to stop this process if you think this process is desirable. And I don't even know if you can make political arguments for the desirable or not. But I'm just saying like, if you want it to be desirable, if it's desirable that real wages on the lower end actually rising, then maybe you want to preserve the environment. That's all I'm trying to say. Right.

What to do with … I have given a lot of thought on this. And actually, as a matter of fact, I'll confess I was a little blindsided. Part of the reason for that policy makes absolutely no sense. For me, it seems to me completely unhinged. And I'm not a person to criticize the Fed. I actually think that they're doing their best. So, they might be seeing things I don't see. And they have their own arguments. I don't think like I'm not one of those people who say they're like clueless they're detached. They're smart people trying to do their best. That's just not often what I would have done. But again, my job as a trader is not to figure out what I should do, but how to capitalize on what they actually do. Right?

With this caveat, it makes a ton of sense, it would -- again, if you put me in their seat, knowing what I know now, and I probably would have known more in that seat, I would just say like no raising rates. Maybe like 25 basis point hike, just to stabilize money markets and very aggressive balance sheet unwind. Why do you want to raise interest rates on your own liability, which is the Fed's reserve? And to your point, it might work better to deflate asset prices. And honestly, if they really wanted to deflate something like real estate, probably the best way to do this would be to change tax policies not to raise rates. The best way would be to like kill some of the real estate deductions. Right? I'm not talking about the mortgage deduction, but a lot of other things.

Mike: 00:33:36

Change the mortgage structures, 30-year mortgages …

Alex: 00:33:40

Tax the resale of primary residence. Change maybe abolish 1031 Rule. It's like this. There's a lot of things they can do, which I think would be hard politically, but on the other hand, if that's the objective, what I'm saying, right, if the objective is specifically to deflate and more affordable things you could do on the policy side, not necessarily on the monetary side, right. That's all I'm trying to say. And to your point, it would make total sense for me to run off the balance sheet because they kind of almost like committed themselves to not being able to reduce the balance sheet. They're saying they will but they won't, because if you hike rates and then you have a recession, you cannot start reducing - how much balance sheet reduction are they going to reduce it by like 100 billion dollars and then they have to go that way again. That's like ever-ending trap.

And also what happened to good old LIFO, Last In First Out? We started by cutting rates and building balance sheets. So, let's unwind balance sheet and raise rates.

Adam: 00:34:42 Exactly. Yes.

Alex: 00:34:43 And I don't know why the thinking is and I honestly anticipated the thinking to be more that way. And I was blindsided by the fact that they -- not blindsided, but I was surprised by the fact that they chose to be very aggressive in terms of projecting hiking without being aggressive at all about they were very kind of slow and methodical about tapering and then about, they could have tapered much faster this time, right? What are they doing? They were like buying bonds, this winter still, while their inflationary concerns. If their concerns is inflation, why are you buying bonds still? Right? I think it just really kind of seems a little weird to me. Like, I think they just start laying off the balance sheet aggressively now right.

Adam: 00:35:27 Exactly.

Richard: 00:35:29 Yeah. Alex, I want to pull on the thread that you were mentioning earlier about fiscal policy. So, you might argue that the hike, the rise in oil prices acts as an indirect tax for consumers, income tax in general. And I'm sure we're going to get into it later in the conversation about what's going on in Russia and Ukraine. But to linger just on the uncertainty around energy prices right now, you also have this dynamic where people have been discussing this more and more about this fiscal cliff that is approaching. The *Build Back Better Plan* did not pass in Congress. There's no prospect, especially if there's a sweep in the midterms for any meaningful fiscal expansion to happen. So, if you consider that we are already facing this fiscal headwind in the US with the addition of the energy uncertainty, isn't there a case to be made that the Fed should actually be considering slowing down or even reversing course, with regards to their rhetoric to soften the blow that is likely to come if these things do materialize?

Alex: 00:36:37 That definitely would make sense to me, and that's why I would favor being very patient rate hikes and just be front load run over the balance sheet, because that's something like you can kind of soften the things with that. What I think is going to happen now is they're going to hike rates, they possibly will have a chance to start running off the balance sheet. They're going to have to pause the hikes very quickly, maybe it'll get one or two hikes this year. And then, but the balance sheet runoff will be late started and running in the background. And it's like, back to my wave analogy, there'll be off-phase. And that balance sheet runoff might come in late, might cause enough of a continuing tightening of financial conditions, in addition to the fiscal issues that you just mentioned.

And it's kind of the same argument where the energy cost serves as attacks or not, or whether like a general fear factor is a -- like, look at COVID slowing us down, but who knows, maybe the war in Europe has also kind of caused some caution on people in terms of traveling, might be some kind of negative. Typically, wars are inflationary, but there could be a component of a negative growth shock there too. So, between all the shocks, yeah, that's why I'm kind of biased to think that we're going to be easing in not that distant future.

Richard: 00:37:59 If Mr. Powell doesn't stumble into another policy error like 2018.

Alex: 00:38:06 Well, he will .

Mike: 00:38:08 The easing is in response to the policy.

Alex: 00:38:11 There is a tool that I used in my book too, I think it's Grant William said it. Fed always hikes till they break something. So, we cannot count on them to preemptively get very dovish, I think they're in the corner, but they will be hawkish relative to where they should be. And they will have to be … before the reality. Now, a very strong sell off in stock market will change. Remember what I said earlier about the zeitgeist, that feeling of persistence, when stock market is down, it's much easier to convince yourself psychologically. So, imagine there's a day that NASDAQ is down two and a half percent, versus the day when NASDAQ is up two and a half percent. Really, it's only a 5% difference, not that big right, one day move.

But on the day when NASDAQ is down two and a half percent, it's much easier even for me to convince myself that the economy is going into recession. It's a very subtle psychological condition that's happening. So, if the Fed, not because they're trying to prop stock market and save rich people in some kind of corrupt way that people often talk about, it's just a psychological conditioning. They see assets getting weaker. Eventually it spills into things which are more in their purview like funding. They see funding getting tighter here and the credit spreads going wide, assets going weaker. Then it's easier for them to find the pretext to become more dovish. Then next time they see a mixed economic number they'll say a-ha, maybe we can stop, right?

At first their reaction is, their first reaction is like, oh, stock market corrected 10%. Who cares, right? That's not our purview. That's fine. It was overvalued anyway. This is their first line of thinking and we cannot really get them to think otherwise. As a matter of fact, let's talk about like Powell put, the Greenspan put. I was not always surprised of how much this put exist, but how much it does not exist. If you look at the actual timing on action, they don't react to the stock market. They still tightened in 2018, in December 2018. They still tightened them May 2020 when they were corrections happening in stock markets. They need to see that and a combination of some economic data. But it will bias them to be more responsive to economic data. That's what I'm trying to say.

Fed Errors and Stein's Law

Adam: 00:40:32

The challenge over the last decade or so has been that the response of the Fed when they do decide that they're going to pivot QE two, QE three, Operation Twist, etc., it drives moves in asset prices that are so asymmetrically out of proportion to the upside relative to what they're willing to tolerate on the downside, right? So, this is one dynamic that I think is really -- has this strange trap property to it for the Fed, where they are willing to institute stimulus measures that drive asset prices higher by 50 to 100%, over a 15 to 24 month period. And then they react when markets drop by 15 to 20%, right. So, you're correcting a small fraction of the damage that you did on the upside. But you're not allowing -- the balloon just keeps --you've got this massive increase in the size of the balloon, you get a minor contraction, and then you get this massive asymmetric support again, right?

The question for me is, A, can this dynamic go on forever, can market PEs go to maybe back to 2000 levels? Or maybe to where we saw the Nikkei in 1989? Can cap rates on real estate go to, from 3% to 2% to 1%. I guess invoking Stein's law, which is, if something can't go on forever, it'll stop, right? This type of dynamic seems to me to be unsustainable and is now an opportunity for the Fed to acknowledge these errors of the last 10 years, and at least allow their balance sheet to run off, allow some of the air to come out of the asset bubble, keep rates low, and do what they can to kind of preserve economic growth. So, it sort of stumbles along still, right. Do you think that might be on the minds of some central bankers here?

Alex: 00:42:54

Well, let me first address the first thing that I have that you said about this whole thing, which I did notice this pattern a lot too. Yes, we get like 100% growth in stock market. And that's okay. And then 20% correction, that's panic. I'm totally -- and one argument that can be made, that overall economic growth, at least in the United States are so fragile that it kind of relies on this continuously running stock market. And when the stock market, even flat stock market is not good enough. And as the more you get higher, the more like a lot of debt and financialization leverage and economic growth. So, economic growth has to grow that thing so fast that when you get like, you can sustain small and small corrections without a hit to growth. Maybe we -- possibly COVID let us get a, like delivered us a little bit and let us get out of this dynamic being so sensitive. But again, patterns tell us that corrections need to grow slow down very often, right? But that is the first argument. And the second argument -- Sorry, your question was about? Can you repeat the last portion of your question? Sorry.

Adam: 00:44:12

Yeah, it was just do you think that some central bankers are now -- are beginning to look at asset prices as actually a fundamental problem that needs to be addressed now, because they've already kicked the can? There's been a series of policy errors that have now painted them into a corner. If they repeat this again, maybe they will never be able to escape from this corner without such dramatic repercussions that it would be so unpalatable for everybody.

Alex: 00:44:43

Well, yeah, I'm sure they're asking those questions, first of all, and I just wanted to tie in -- the reason I asked you to repeat, I wanted to tie in what I was saying before with what I'm saying now to make sure I didn't lose my thread. So, you brought up earlier like where can PE, right? What is sustainable and what is not? My problem with this is and there's, again, two warring ideas. One of them when I talk about historical patterns. If historical patterns say that this is not sustainable, every once in a while, valuations run ahead, and people make an argument why this time that's sustainable, and you always end up buying stock market 70% cheaper if you are courageous enough.

And I kind of believe that last year, I believe it now that we'll buy stock market most likely, much cheaper than it is today in the next couple of years. There will be a moment when you can buy cheaper. I used to do those polls in 2018. I would like poll people and say, in 2017, like, raise your hands if you think in the next five years, you can buy stock market cheaper than today. And almost everybody said yes. And I was like, why long? Right? Why didn't you wait till you buy cheaper, right? So, that was my position. It's still happened to be kind of my position. But it is important to also understand that historical pattern is almost the only thing we'll have to guide us with respect to valuations.

There is no rule what PE should be. What is the PE of gold? What is the PE of Bitcoin? If we're starting to think of mega caps, like the Googles and Amazons of the world is just a store of value, then as long as they're not -- like, if they were losing money, that would be unsustainable, probably. But they can sustain it for a long time, but not forever. But if they're actually making a little bit of money. And they're beginning to be dominant, and the stock remains liquid. Or they could say, Ok - Google stock better than treasuries, right? Let's just -- who cares if they yield one and a half percent and treasuries yield 50 cents, right? Why not? You can very easily make those arguments. What happened in 2001, this is my perception of the reality of 2000, then PEs get out of control, valuations get out of control. And because the people …, they … by supply.

People started to pour IPOs in the market, and they basically choked the money demand with IPOs, the demand with IPOs. And they're like, oh, I can just get five guys together or whatever, and say, we're going to start our company, which has no business plan, but we're going to do something and put the call. Sell it $100 million. Well, people start doing it till eventually the market get over supplied.

Now, is this the environment we're seeing right now? In some sense, not so much, because what happened between 2000 and now, we went through very much this super winner takes all economy. So, actually starting like a small search engine company is really not a very good business.

Richard: 00:47:45 Yeah, that makes sense.

Alex: 00:47:47 Yeah, go ahead.

Richard: 00:47:49 No, I was just wanting to, you mentioned, you framed the conversation surrounding tech mega caps as a potential store of value. So, that just made me curious to think a little bit more about your investment and trading framework and how you sort of operate in the global asset class scale. And then I thought this might be a good way for us to shift gears into talking a little bit about your book. And for that, if you could set the stage into some of the asset classes and instruments that you look at and that you trade in, and then maybe walk us through a little bit about from a 30,000 foot view, what happened in March 2020 from your view.

Alex: 00:48:27 Okay. Well, that's a very broad question, but I'll see what I can do in the next few minutes. So, first of all, I do global macro, which means I basically can dabble in anything I want to dabble in. Obviously, I cannot be an expert in everything. So, I probably do less research, kind of individual stocks or credits, I cannot know anything about them. If I like gold, I might buy gold, or I might buy gold mining index, right? Will I buy individual gold miners? Well, maybe if I like some research on them. But it's not kind of my core -- I don't come to my whatever meetings internally and say like, hey, I like this company, which does this widget, we'll see if you can buy them. I look more about like asset classes.

And what is important about my approach, I don't feel that I have to do all this like short or long stock markets, short or long Euro, short or long interest rates. I don't have to have a view on any of the core macro assets. I could have no view on the Euro on any given moment. What I try to do, I try to find places where I have, according to my criteria, skewed odds in my favor and focus on those and whenever I can, build a balanced portfolio out of those trades. Now when crisis like pandemic hit, obviously you hedge your positioning before that and I talk a lot about my book about how we can position, why we position certain ways and also certain ways that you can on occasion have kind of a free crisis protection options or really cheap crisis protection options, and I've used them a lot in 2020.

Setup was not as favorable for me, for example, this time. Things that you would need to buy, you would want to buy, if you were thinking about the war getting out of hand in Europe, were not free. Even if you had that view, right? It wouldn't be cheap or free to protect yourself against that situation right now. But in 2020, it was cheaper for you to protect yourself against pandemic, and when it's cheap or free, I do it, right. But when the crisis actually does happen, the most important challenge of the trader is to just kind of leave behind what you had before crisis in a sense, like, okay, those are the positions. We made money and we lost money. We got lucky and we made money and we got unlucky and we lost money, and now we have a new portfolio. And what should we do with this portfolio throughout crisis?

I talk a lot about -- I'm maybe straying a little bit from your question, but it's a good segue into this. In the book, in my book, *The Trades of March 2020*, I used a poker analogy. If you're on a winning night, like you're up money, you're feeling good about your game, you're feeling relaxed, you have time to go get yourself a drink, and go to the bathroom, freshen your face. Maybe it's a long poker session, but you're winning, you will have the advantage. I think this was also, what is the movie, Hustler about fools, right. And they also show like one guy keep playing and drinking and another guy's like taking a break, relaxing and… right. So, this is how you win by starting with a winning hand. It's much harder if crisis blindsides you, if you're under pressure, and this time, like your portfolio was not well prepared for it.

And honestly, it's 50/50, you're not going to be -- in my career, whenever such incidents happen, sometimes it's favorable, sometimes it's unfavorable. You cannot be always -- you're not going to be so lucky that every time there's something unpredictable happens in your position and direction. So, if it's a guess you, you have to take your losses, right and then you think like, okay, so what do I do next, what positions do I hold to, what new I can put on and how to take advantage of it. And the key -- so, I made a subtitle for my book, for my pandemic book, *A Shield Against Uncertainty*. What I meant by this is that, like how those environments are very uncertain. We knew how uncertain it was during the pandemic. Nobody knew how bad it is, how it's going to spread, what are going to be the policy responses, we really didn't know what was happening.

And right now we really -- there's a lot of theorizing about geopolitical situation. But people like projecting anything from peace talks and ceasefire within 24 hours to nuclear war, right? It was having such a wide range of possibilities. Honestly, I don't think anybody knows a really clear answer of what's going to happen, even on a very short horizon. And markets are gyrating with this mood swings. The idea what I did in the pandemic times and what I'm trying to do now and what I think other traders trying do now is to perceive what it is that we can kind of see through this event, what things are certain. Are there any bets that in every reasonable scenario will eventually converge? Because there are some things that don't have to converge.

Like, for example, will Russian economy recover? Like, will Russia become reintegrated in the world community? You can make odds on it, but there is no specific reason or belief Russia could go the way of like Iran and Venezuela, right, after this war. It's possible. There are precedents to such things happening, right? Or it could be somehow negotiated settlements and changes and basically kind of be put back, put behind us in a year or two. Right? All of those are possibilities. Hard to bet on that. What's going to happen to oil prices in the next few weeks? Very hard to imagine. But just as during COVID I thought, well, oil prices went very low. But two, three years from there, one or the other way, pandemic will pass. So, the forward oil contracts to me when I was looking at 2020 to 2023 oil, I was like, well, it's going to normalize to like $60, right?

Now, I did not think and I didn't bet on it going to 110, I wish I did, of course. But that's not my -- what I was speculating on. I was just thinking that it's going to go from 35 to 65, back to normal, whichever way the pandemic will play out. Because what I knew during the pandemic, this is what I talked about, the mantra was that pandemic will pass, liquidity will stay. During pandemic, we knew that the policymakers will keep adding liquidity till it becomes successful. And that was the game to play in March and after March 2020. So, that's the game I tried to play. Not bet on how quickly liquidity will arrive, what's going to happen to the virus, but the fact that eventually there will be enough liquidity and things that benefit from it will go up? How do we play it now? It's hard to tell. But obviously, like we're in it, how do you play it now? What do you look at?

With energy, my guess that energy will normalize to some trends which are fundamental to it before this crisis. But there could be some changes because Europe can move to more energy independence, many countries can increase production, people will like to decouple if Russia is allowed to sell energy again, they might sell more than before for economic recovery. There is all those things that could be looked at. So, I actually think that long term perspective for energy became more negative than they were two months ago. But it's a hard bet to make. I'm kind of betting on the fact that Europe will restabilize and come back, possibly with less energy dependence, but most likely with …, they're pretty fiscally aggressive and they're fiscally aggressive as military budgets are going up. They'll have more fiscal expenditures.

So, I think there's some opportunities in that world, like just kind of your Europe stabilizing and possibly European stock markets doing better then on a relative basis, possibly Euro doing bad on the crosses going forward, Euro and pound. I think. For example, there are defensive things if you think it's hard to judge, like where you think Euro/Swiss or Euro/Yen should be, those defensive crosses. So people are panicking, they're selling Euro to bank Swiss franc. But if you really think about this, one way or another, the situation will resolve. So, if you don't think Swiss franc belongs at 100, if you think it belongs at 105, and 110, if you buy it now, sooner or later the situation will resolve. And then Euro/Swiss will go to that … place.

If you think that Euro/Yen belongs at 135 rather than 125, again, once the situation will resolve one way or another, it'll normalize. Of course, they're off-chance scenarios of very severe escalation, nuclear incidents, or maybe even just a really protracted war, which something like replay of the Great Northern War of early 1700s, when whole northern Europe gets pulled into something. Yeah, you can look at those outlier scenarios. Just as with pandemic, we could say like, what if COVID gets so bad that we're shut down for five years, right? But we have to take our chances. Those are clearly low probability scenarios. Like there is no argument and the likelihood is one way or another, with whatever the fate will be of the Ukraine or Russia, situation will stabilize in Western Europe. So, there might be potential for bets there on that long horizon bets.

Russia/Ukraine and Capital Allocations

Richard: 00:58:01

So, sketch out for us if you wouldn't mind your base case scenario for what you're witnessing right now. I guess how you believe the current conflict will resolve itself, what kind of equilibrium we're going to find ourselves in and what that means for capital allocations?

Alex: 00:58:19

Well, first as I said, it's very difficult for me to say how this conflict will be resolved. And honestly, I was the worst predictor of this conflict so far, because I really couldn't see the all-out war happening. I know it was one of those like, we've had all this game, we've had all the research people lay out scenarios, including the one that's happening, that was gamed. But it seemed such a low probability, because just as I said, like if people know something, I don't know. But just as what central bankers earlier we discuss, doesn't make sense what they're doing. So, completely leaving the humanitarian and ethical side of the moral side of it aside, strategically, what is happening was befuddling to me.

And I'm trying to find some now post-facto strategic rationales for what various parties are trying to accomplish and why they're trying to do this certain ways. Kind of like what negotiating tactics they're planning to use to get out of this. And there are several parties here. There's the West, there's Russia, there's Ukraine, there might be some other more subtly involved parties, right? China and so on, right, how they're all going to untangle this. Because I think everybody wants to untangle at some point. But again, maybe that's the wrong assumption. Maybe somebody doesn't want to untangle at all. Maybe somebody wants a 20 year war. It's hard to -- like there you can definitely see various paths of resolution.

I was surprised with the military developments. I was surprised, most people were surprised by the fierceness of fighting and the fierceness of resistance in Ukraine. Many people thought maybe that Ukraine will just play possum if these things happen. Or many people, including myself, would think that if incursions were to occur, they wouldn't be so broad and will just be restricted to certain areas. So, the whole thing just spun out into something that, honestly, I would give less than 1% chance probability if you asked me just a few weeks ago, and the different paths to resolution, right? People just could suddenly negotiate ceasefire and find some kind of solution that allows everybody to save face. You could have Russia gain significant military gains, and then negotiate itself out of it and say, okay, well, now we're there. Now we're going to give us this and we're going to pull back right?

Mike: 01:00:48 Are there any of those sort of cheap, free hedges that are available out there? Or are they evolved past at the moment?

Alex: 01:00:59 It's hard to be cheap or free. Honestly, I will be, right now, if there was something free, I probably wouldn't be talking about this right now on the broadcast. Full disclosure, if there was something very subtle, huge misprice, I would probably be first loading up on this and then …

Mike: 01:01:17 Yeah, you'd want to get your position on and then you'd tell everybody.

Alex: 01:01:21 And I not really want to talk my book, I don't try to do this very much. I don't believe in putting position on and then getting other people involved. I'd rather prefer because I don't want other speculators on my positions, because they only going to mess me up. I just want to put position on and wait for normal economic forces to resolve. Where I think opportunities lies on the fact that various things are priced for various levels of Armageddon. And that was through every crisis, through September 11, through global financial crisis. I mentioned that in my books, … about it during COVID. What you try to do is always sell whatever is priced, and everything is hunky-dory, and buy whatever is priced as if it's the end of the world. That is kind of the approach, right? You think about, huh, there are some interesting opportunities in markets, which are somewhat niche markets. Things that are of just in my opinion, for example, there is markets, which has priced as if rates will never go up at all in the world, like I'm going to be zero forever.

And there are things which are priced in such a way that, oh, it's really, rates are really high, and everything's great. So, there is like all this disconnect. Opportunities may lie within disconnect, and opportunities may lie within things, which I think have a very high probability of snapping back. Like what I mentioned, for example, Euro crosses, like Euro/Swiss. I think it just has a good opportunity of snapping back and I'm just using it as an example. But it's not free. You could go five 10% against you. I just think like, five years from now assuming I see the world in which there is no war in Europe going on, hopefully, right. And I see the world in which Europe actually potentially is in a zero interest, in negative interest rate policy. I'm seeing Euro carrying positively against currencies like Swiss Franc and being a little stronger.

Mike: 01:03:22 So, you're seeing some economic growth then.

Alex:	01:03:24	I'm looking to something like one point level against dollar because that seems to be the kind of historical magnet for Euro.
Adam:	01:03:30	Well, yeah, the PAYGO idea in Europe is thawing. Right? Like, you're starting to see even the most hawkish fiscally austere German central bankers and government representatives, talking about the need for pretty substantial fiscal balance sheet expansion, right. They're talking about pretty substantial investments in defense. And once you begin to open the door to deficit spending, I think we're going to find that once there's a foot in the door, that there's going to be a lot of appetite for more fiscal expansion. And that that will, once the Germans open the door to deficit spending and fiscal stimulus, then I mean, obviously, Southern Europe, has been chomping at the bit for the ability to loosen the purse strings. And I'm sure France would be happy to follow suit. And so if Germany is already making moves in that direction, there certainly is an argument that, yes, we're going to see much looser purse strings, some pretty substantial amount of deficit spending, major escalation and economic growth in Europe, potentially relative to the US, and that could be positive for the Euro crosses.
Alex:	01:05:01	Yes. And I generally believe that fiscal expansion, deficit spending is actually good for domestic currency for developed markets, because a lot of people have this knee-jerk reaction, oh, there's a deficit and that's bad for the currency. But the reality is the US situation, yes, US story would be like we have a deficit so we issue more bonds. Well, someone has to buy them and to buy them there to buy dollar. And assuming that they're not all hedging, right? They start on incremental, it creates actually buyers for those extra bonds, which is kind of an extra dollar product to make. So, it drives capital account surplus. That has been my kind of assumption, maybe it is not very differentiated, because I'm not an economist, but I felt like, historically, fiscal expansion is actually good for domestic currency. And I think, in Euro, fiscal expansion would be good for getting off negative rate policy which I don't think anybody really wants to stay at. But other countries, like Switzerland attract much deeper in the negative rate policy. And now we're in a hurry to get off it with Euro/Swiss at 100.
Richard:	01:06:10	Yeah. To stay in this sort of the three larger currencies, I guess the euro, the dollar and the yen. And to borrow from … and the idea of the cleanest dirty shirt, right, currencies are a relative game, obviously. And because we're all in this debt overhang period, what does that mean for the ability to continue down this road of deficit spending? And are we looking at debt monetization? Are we looking at MMT? Is this where we're headed in terms of policy directions? And what does that mean for this relative, cleanest dirty shirt currency game?
Alex:	01:06:54	Well, I think when it comes to debt, I might be a little bit of a closet MMT-er, not really, MMT-er, but like a tiny bit of MMT in the closet. I just don't think that sovereign debt is a big issue for countries which have not, don't have like for debt

and other currencies. So, they don't have countries like US or Europe, which don't really have, especially Japan, which have no fear of balance of payments crisis, they can fund on their own currency, it's not as much of an issue. And an issue is kind of chickens come to roost is when you have inflation. And even the hardest core MMT people agree with this, but you have to deal with inflation. But to me, yes, but to me, they already won that game, because it seems you can issue the debt, and then buy back 1/3 of it or half of it with the central bank. You kind of won the game because what happens next, if people -- if you have inflation problem, all you have to do is just sell your balance sheet. And you can solve the inflation problem.

Richard: 01:07:59

But who's buying your balance sheet unless you're resorting to capital controls and financial repression and forcing, I guess, insurance companies and reinsurance companies to own your government debt, because it's the perceived collateral that they need to build their balance sheets with?

Alex: 01:08:16

Well, it almost doesn't matter who is buying it, because say you need to sell hundred billion 10 year notes, and you might not sell them directly. It could be through runoff, right. But you just put them on the market and say like, okay, buy them. So, maybe they'll buy them cheaper, but at some point, they'll clear. Now, will rates rise? Well, no kidding. If we're fighting inflation rates will rise. If you're doing it for the purpose of fighting inflation, yes, the outcome of it will force - the yield could long term or temporarily go up. Now the history shows that there's increasing supply doesn't actually cause yields to go up.

But even if they did, it would be like, rates shoot up. We're fighting inflation, we tighten financial conditions, rates went up. Right? But it's actually not what even happens necessarily. Like if you needed supply of treasury bonds that did not really correlate very strongly with interest rates historically, or if anything correlated negatively with interest rates.

Global Equity Markets Today

Adam: 01:09:15

Interesting. Can we maybe shift to equities a little bit? Because I don't know. I'd love to hear your thoughts on what you're seeing in global equity markets. And what I think I've noticed in this correction so far, is that it's had much more of the character that we, those of us who kind of grew up and observed markets in the 90s and early 2000s and mid-2000s came to expect, where we had these sort of rolling tops, and these more sort of staged drawdowns with big bear market rallies. But we haven't seen a massive spike in credit spreads. The credit markets certainly don't seem like they're panicking.

VIX until and I didn't look at it today, but until certainly yesterday, the day before, we're still seeing VIX well below 40. Any thoughts on the character of this current equity market move? And I mean, you've already sort of stated that some of your other signals are flashing red for equities, but maybe comment on the character of the current equity market correction, and in the context of some of your other signals, maybe what investors might expect over the next few months?

Alex: 01:10:40 Well, for me, this has a feel what is happening in the US market, kind of the, in general, just intuitive feel, it has a feel of a *grinding bear market*. Which is something we actually hadn't seen for a while. Because we've had a few sharp stock – well, we've had COVID. Before COVID, there was a really sharp and also precipitous sell off in end of 2018. There were some corrections in like 2015-2016, but none of them had that feel of grinding bear market. And I wonder the last grinding bear market was in 2008, and even that was really hectic. But I think that probably portions of 2018 would feel like that, right? The 2007-2009 bear market, which was very severe, obviously, and protracted, a lot of chaos. But right now it almost feels like you want something pre those times, some kind of like a phenomena that -- another 21st century market.

Adam: 01:11:38 Yeah, like a 1990 recession style or …

Alex: 01:11:41 Yeah, it feels like a 20th century market right now, which is, by the way, somewhat supports the narrative that we're in a different world because inflation is higher, right. But that feel of grinding bear market is actually not even that familiar to me, at least not in the recent years. And I could be totally wrong, but that kind of thing when you just -- Yeah. You see in the past, like it's a sell off and you … bounce base and you like good back the bull market. And now it's like, not maybe it just keeps…

Mike: 01:12:14 So, a 70-style, you've got inflation, you've got an oil price shock, I don't know. Is that sort of what you're -- a decade long, lots of vol, down lots then recover, but never break out to new a high, down again?

Alex: 01:12:30 Yeah, something like that. What is interesting, there were some similarities between what happened in 74 and what happened in the Great Recession of 08, like the blow out and credit spreads and blow outs and things like what actually happened back then too, and the magnitude of stock correction. But the environment was still very different. Yes, it maybe -- I haven't traded in the 70s. But it's very hard to get a good feel, just looking at charts of how it felt. It's always easy to compare with the days that you traded even if obviously you can nowadays look at charts 100 years back. But there is this feel of something different this time that this is a grinding bear market. That's my current assumption.

Richard: 01:13:17 Yeah, the main difference with the 1970s is that we left the gold standard in the 1970s. And since then, we've been in an economic model, a global economic model that leans on the US dollar heavily. So, to pull on that a little bit, the US dollar cycle has been sort of one of the main drivers of relative asset class performance. And so the last 10 to 12 years, we've observed US dollar being very strong. And then the US 60/40, being sort of the dominant, the only game in town, along with US real estate, and so on. And then now all of a sudden, we're seeing inflation, and more dispersion across asset class returns. What are your thoughts on that? And if you could comment on the US dollar, specifically, and to what extent do you think that perhaps sanctions and not to get into the merit of the sanctions themselves, but the more the US dollar becomes weaponized, the more it drives other countries to seek alternatives from the US dollar, and how that might play out from an asset class perspective?

Alex: 01:14:23 Well, there's a lot there to cover. But yes, to most of it. One thing, just to go back to what you said, at the very beginning of this portion, when you talked more about comparing 70s to the current environment. I just want to make one comment about this and about the changes. One thing that is very different right now is a very different demographic situation. We don't have a huge amount of people entering the labor force like in the 70s. So, the growth potential is much worse. So, we're kind of facing this but with much worse potential growth. But as you say, economy dollar has -- there is no like gold standard or anything like this. There is a kind of new world order, there is complete globalization and now possibly some partial deglobalization.

I'll be honest, I find myself very conflicted on the dollar. I find that it's hard to play the dollar right now, because there is almost, like my bias, first off to 2020 do we short dollar, because I was foreseeing the cycle similar to 2004-2007. I thought we'd have kind of like a slow way to get to tightening in a very slow, reluctant way and precious metals will go up dramatically. I was not talking gold 1,900, I was talking gold 3,000, right. I was thinking that dollar will weaken broadly too, more likely than not, and that was kind of my bias. I thought the emerging markets will do well, obviously, they did horrifically badly. I thought they would do well, like I said as they did in 2004-2006. And I had to kind of reposition and rethink my thesis and start being a little bit more pro dollar when I realized that, well, it looks like they're going to be really hawkish.

However, what is interesting is that dollar actually sells off at the end of the hiking cycle. So, we could have a correction on the dollar. I still think that long term, I'm probably positive on precious metals. It's similar like, when all is good and done, like this hawkish periods. Precious metals are not so much about inflation, it's about liquidity. Maybe right now, it will tighten but in the long run central banks will probably err on the side of providing liquidity. And precious metals will probably do well. Or at least the upside is just if you think about like even silver going to zero versus silver going to $50-$60 which I think is a very reasonable target that the risk/reward is skewed favorably to precious metals to hold on for a long time.

So, there are, however, dollar versus Euro, I think, actually risk/reward is slightly skewed towards Euro being at some point hitting 120, and will it carry -- of course, obviously, there is a negative carry on being long Euro. So, by the time it gets there maybe it'll be just the same as kind of a wash, right? But I don't think -- if you think that rates in US are not going to go as high -- what I'm having trouble with, for example, think about dollar versus Euro is because if you make an assumption that the hikes will be as aggressive as they are you probably want to actually long dollar, against currencies which are not hiking so much. But maybe you can still short dollar against some other currencies, which are pretty aggressive like New Zealand and Australia, right? If you think that the economies roll over, however, you want to short those currencies because they are very …

Basically, I can paint so many pro and con arguments. I wish I could tell you -- I know people who are very bullish on dollar here, I wish I could tell you all in, this is my view. I'm not so much centering my, right now, for me, like Euro is more interesting right now, because I feel it's definitely … because of this war, but I don't feel it's a long term damage to where Euro's going to be. But I don't see why this war five years from now, how this war will affect the Euro. I think like this war will affect the Euro if anything positively in terms of where it's going to be five years from now.

Adam: 01:18:27 How do you hedge the -- I mean, I think your central thesis is that, whatever, two years from now, three years from now, five years from now, this conflict will have passed. And there'll be some reversion to equilibrium. How do you hedge the less likely case of moving to disequilibrium, or substantial escalation here? First of all, what might substantial escalation look like? And then how do you potentially hedge your wealth and your life against some of those scenarios?

Alex: 01:19:13 So, this is a complicated question, because you have to be really careful what it is that you're hedging. For example, if you're worried, like if you're a typical person who wants economic growth to be stronger, like you have your house, your business, whatever, and you're worried about lower economic growth, I think we are at the place where risk parity, which was kind of for a while put on hold now is back. I think betting on lower interest rates is a good hedge against things rolling over. But you have to be careful about that because we'll, for example, just as escalation in Europe and kind of inflationary shocks from it, not be ameliorated by interest rates because you could have interest rates continue rising.

You might want to have some bets which actually perform well in inflation and rising interest rates. You might have to cover more than just two scenarios here, what I'm trying to say. You can think about like, okay, excess liquidity hedges are typically hard assets, cryptocurrencies, precious metals, hedges against strong, very aggressive … kind of being with it. It's vice versa, strong dollar, right, being stronger. But there are also some -- to hedge that and to hedge real escalation of war, I'm afraid you need to go to municipal markets. You need to say like, okay, well, I see some interesting opportunities in municipal markets. For example, I look for misprices on municipal markets in the event that rates actually do go up.

So, you could make some interesting trades there, which most people are not available, right? If you want to bet on escalation of war and buy defense contractors, so somebody like, anything to do with nuclear security or something, right? You might have to get creative here. It's not simple, what I'm trying to say. You might have to get creative because what are they going to do now, short ruble? Too late, right? If you are smart enough to short ruble several weeks ago, if you saw that this is going to get out of control and the ruble was like high 70s or something, maybe risk/reward case that gets out of control, ruble is going to lose 30-40% of its value. Kudos to you, right. But it wasn't a cheap bet because ruble was carrying positively.

Normally, it's like Russia is a country with no external debt, no public debt at all. There is normally no pressure on Russian currencies whatsoever. The only pressure is capital flight, people converting the rubles into dollars to buy assets overseas, that's the only real outflow, everything else is inflows, right? So, it's not a cheap and easy bet. But if you were courageous enough to break how to catch through this, I think rates offer good isometric opportunities. Because as I say, I think US rates are a good opportunity. And maybe Australia and New Zealand rates are good opportunities, because I think there will be zero, two-three years from now, with or without escalation. And I think escalation of war will not cause rates to actually go higher. But it might cause them to go lower just because of the panic.

But on the other hand, you can win this game even without the war, I think. So, that's why I like having some bets on rates being lower two-three years from now, in this group of countries and maybe converging -- and rates in Europe meanwhile, normalizing. So, I can see a scenario where, for example, rates are zero both in the US and Europe, two-three years from now. It's an extreme kind of convergence, because probably events that will cause US rates to go to zero will cause Europeans to stay negative, but kind of -- I see the convergence basically. I see some convergence there more likely. And those could be interesting, but how to make money on extreme escalation of war? I mean, probably precious metals will do well in extreme escalation of war.

Adam: 01:23:20

Are you surprised at how -- I've been looking at the implied vol on gold and I was shocked to see that even far out of the money, but like, but near the money the implied vol on gold is in the low 20s. And, I mean, that seems like potentially fairly cheap insurance at the moment to buy some out of the money, exposure to gold or maybe to silver, to precious in general. Just wondering whether or not you've been seeing that and whether you're ...

Alex: 01:23:58

Well, I think this is not a bad idea, because and I've been thinking in those terms in general, like looking for various options in the world. So, wherever -- because when the price is dislocated, severely, but the option price is not going super high, the areas were optional is very high, no option. ... where it went up, but not as catastrophically higher as it might have, right? When there is a ... because one of the two things will happen, either things will keep getting worse and more catastrophic, in which case the volume will stay high or at least there will be big snapback to normal pricing level, which will be a big move, right? So, in either case, either you get a big move, which could be a grinding move, but at least it'll be directional, right? Or you'll have a continuous chaos in which either case it's okay to own options.

So, yes, I'm looking for some of the options strategies. Vol is not cheap, but where you see vol reasonable just from that perspective, you're thinking like vol gold is vulnerable -- if you think that in normalization process vol is very vulnerable for downside, why don't buy options, why hold gold, right? And chances are basically what we're saying is like either you get -- when you get killed on options, whether you don't see a big move, and you don't see a lot of volatility, right. When you see like slow grind to your strike. What I think is more likely, in many cases, not just precious metals right now is some kind of sharp, original either continued chaos and volatility or sharp normalization of various things. For example, if war get somehow resolved. And eventually vol will die, but before it dies, it probably will work for you.

Adam: 01:25:41

Yeah, so straddles on some assets where the market is not really pricing in vol the same way as its pricing it in certain areas. Like it's tough to buy a straddle on equities here, right, or even on rates given where implieds are on rates, but I think ...

Alex: 01:26:00

Yeah, rates have all gotten very high. And this is .... I talk a lot about this in my book, because in 2018, I start my book with discussions I had with John Burbank about buying calls on the Euro dollar futures. And those calls were so much cheaper. We kind of revisited recently this conversation with him and the calls are so much more expensive, so much more expensive now than it was in 2018. Same thing, just so much less lucrative. Sorry, I'm just interjecting.

Options Across Asset Classes

Richard: 01:26:35

I wanted to kind of get a sense when it comes to expressing these views, you're talking about options a little bit. You've talked a little bit about the cash position. So, if you wouldn't mind kind of walk us through when you're talking about options, are these over the counter, any of the exotics, do you use swaps and futures? Are they asset class dependent? How do you think about that? And what are some of the instruments that you're using to express your views across asset classes?

Alex: 01:27:00 So, my bias is towards … instruments. Whenever I can I use futures. Or if I use over-the-counter instruments it's usually the most simplest ones I can find. I wrote about this a lot in my first book. I really want to avoid unnecessary complexity. I really hate any kind of like exotic knockouts, … options, I almost never do any of this stuff because it just adds many ways things can go wrong for you. Ideally, I want to just put the vanilla directional trades, and hold it till it makes money. Because with options, there's a lot of ways to be wrong. People buy an option and be right about the direction. But either things might not go the right direction, or they might not go fast enough or might not go far enough.

So, there's three ways to lose money except just one, if you're holding the vanilla. Now imagine that it's some kind of reverse knockout option, now you have yet another way to lose money. So, it went fast and further now and in the right direction, but too far. So, now you have four ways to lose money on options. With everything you're jeopardizing your original good trading idea with more and more layers. And of course, you pay a lot of good offers. I think people really do not comprehend how much they pay to the street for doing exotic trades. I used to be an option trader, I used to be on the other side of that. And as many and I think there's a strong pattern. People who come from sell side and they used to do option trades for clients, they don't want to use …

And it's not because bank's pricing is bad. It's just that you observe how clients do with those options. And you see that they actually often don't do well on those options, right? It's not that banks are competitive. They do what they can but they take money and like the more complex your structure, every leg of the -- every -- this little kink of the structure makes more money you have to pay to do it. It's like becoming a gambler instead of a casino because you're paying away the rate.

Adam: 01:29:00 Yeah. On the theme of losing money or like having many ways to lose money on a trade, maybe let's wrap up because we're almost at 90 minutes and just valuing your time. Maybe wrap up with just a discussion about how you manage the risk of the trades that you put on and just risk management in general. Like, how do you acknowledge when the trade is wrong, or when it's moving against you or when the situation has changed? How do you exit? Maybe talk a little bit about that.

Alex: 01:29:32 Well, that's always like a paramount subject of investment strategies. And risk management is something that you always think you've figured out how to do it until you realize that you have not. That's like, getting your risk management policy is like an ongoing struggle in life. And what I tend to do, I tend to differentiate between strategy for trade and risk management for the portfolio. That is, if I evaluate a trade, my primary, I think how I'm going to trade this asset? Is it like a long term trade, is there a stop? Is there an exit? And depending upon what asset it is, and what I'm thinking it could have very different patterns of how I'm going to plan to trade it. My sizing will be actually, usually I'm going to do some stress analysis, how big can this trade be, depending on my conviction, and so it doesn't blow off up my portfolio.

Now, I do not have a principle that every trade should have a stop. The paramount risk management comes at the portfolio level. Because if you're losing money, you typically have to reduce risk, because you just have less capital to work with. And we have certain formulas for risk reduction right now in place, in terms of how our risk limits change. There is some flex on that, certain things that are flexible, certain things are less flexible, right? Certain, like different parameters that we'll look at. Certain ones that need to be followed very rigorously. But for me, it's about the portfolio, not about the trade. Like, if I have a portfolio of selling trades, and some of them are up money and some of them down money, I don't want to be automatically stopping out of trades down money just because they happen to be down money. I've had a lot of trades that I just had to hold for a long time before they made money. And that was just as simple as that. However, so to me, it's all about not preserving portfolio.

However, with trades, individual trades, I find it's very useful to stick to your original strategy and not overthink it. For example, if you told yourself, this is my stop, and this is my profit level, I am very big believer to observe those regardless of anything that happens and hold them till you reach those levels, regardless of anything happens. Which is contrary to a lot of advice about being involved. The common advice is be nimble, like take the new information, now you can change your mind. This is whole thing about -- I brought it up in some other discussions, strong opinions lightly held. And I was just like, I want to be the opposite. I actually want to have weak opinions strongly held. I totally disagree with the series of strong opinions lightly held.

I think it should be weak opinions in a sense, it shouldn't be overly committed to any trades. But once you do them, for me, it works to just stick with them. Because when new information comes the whole market adjusts. And the price of it adjusts. … before it was -- than it was originally. The best work you're going to do is the research and thinking that I do before putting the trade on or as you develop the trade and build it up. And if you came up with certain levels to stop out of it, for example, it's probably for a good reason. So, do not take new information and say no, I'm not going to stop out of this trade because of new information.

And conversely, don't say like, oh, I don't need to take profits here because now this company is doing really well. They have great earnings. I'm not going to take profit on it. But the whole reason why you bought this company is because you thought it was going to have great earnings. Now it has great earnings, so where is your edge? Right? So, now why you're in it, right? That's how I'm thinking about it. So, stick with individual trades whenever possible. My recommendation, I'm not saying I'm always perfect about this. My recommendation's stick with strategy. And with portfolio, because how you're going to risk manage your portfolio, how much risk depending on how big your portfolio is and what is the path of your portfolio? How much risk you can have on it. And that will basically answer all your questions.

End miniriff here

Adam: 01:33:31 Beautiful.

Mike: 01:33:32 Well said.

Adam: 01:33:33 Yep. Well, I mean, we've covered a huge amount of ground here. It's more than I feel equipped to summarize in 30 seconds to end this off. But does anyone else have any other ground they want to cover? Or can we release Alex with our sincere thanks here?

Richard: 01:33:52 We'll leave it for round two when we have Alex back on the show. And we can talk about what's happening in the world maybe later this year. We'll keep those questions for then. Alex, thank you so much. You've been very generous with your time. This is great.

Adam: 01:34:05 Let's make sure to remind everybody about Alex's two books. Right? So, the first one is *The Next Perfect Trade* and also *The Trades of March 2020*, which we've reviewed a little bit here today, especially in the current context, which was fantastic. Also, Alex, where can everybody find you?

Alex: 01:34:25 So, I'm easy to find on Twitter. In fact, my initial and last name, A Gurevich 23, @AGurevich23. Honestly, if you just Google Alex Gurevich, it's a very common name, but I think I'm the first one that comes up, though it is extremely a common name so don't be confused by that, you could find. And also I have a corporate website like the name of www.honteinv.com, It'd be like HonTe Investments. You could also find it through Twitter or any other way but that's our corporate website. It's for accredited investors. But there is some stuff that is more -- people can read kind of broadly. And there are some people who are actually interested in investing would have to be accredited in certain ways.

Richard: 01:35:15 What does HonTe mean? Does it stand for anything? Is it an acronym?

Alex:	01:35:19	It's a Japanese term for true move, patient, strategic move, coming from the game of Go.
Richard:	01:35:28	I like it.
Alex:	01:35:29	HonTe.
Mike:	01:35:30	We didn't even get to chat about Go and the fact it's been solved.
Alex:	01:35:35	Oh, that was a big event in my life I can assure you.
Mike:	01:35:38	Yeah. Amazing.
Richard:	01:35:41	All right, boys.
Adam:	01:35:42	All right. Well, Alex, thank you so much. And thanks, everyone, for tuning in. Make sure to tune in next week. I actually don't have the list of guests. Does anyone know who's up next week?
Mike:	01:35:52	Wow.
Adam:	01:35:53	…
Richard:	01:35:54	I have to pull the agenda.
Adam:	01:35:56	Alex, it's been fantastic. Yeah, yeah, that's right. All right. Thanks, everyone. Have a great weekend.
Richard:	01:36:02	Have a great weekend. Bye, all. Thanks, Alex.
Mike:	01:36:05	Thanks, Alex.
Alex:	01:36:06	Thanks for having me on. Thank you.
Adam:	01:36:08	Thank you.