



- 1) A vicious tug-of-war will continue to ensue this week between the bulls and the bears around the 50 and 100 day moving averages in the S+P 500 (cash). On Friday, the bears successfully smashed through the 100 day only to then witness the market rallying and then retesting that figure at least 3 times. The market did close over that upward sloping figure, but the bears continue to smell blood given the psychological damage done to a number of groups on fundamental fears as to how business models will be disrupted by AI. The bulls will take solace in the closing figure and will attempt to gain further traction essaying for a close over the 50 day (6894) which would produce significant short-covering.
 - a. At some point this year, history tells us that the bears will win a major war. The average intra-year drawdown during the midterm elections is 18%. Therefore, expect a nasty equity correction at some point this year. The drawdown tends to be most pronounced in the 3rd quarter which makes sense. The largest historical drawdowns were in 2002 and 1974. No matter how popular a president, the Administration at the time almost always loses seats. Even Ronald Reagan, after winning 49 states in the 1984 triumphant reelection, lost 5 seats in the 1986 midterms. President Trump lost 40 seats in the 2018 midterms. (As an aside, the Republicans actually gained 2 Senate seats in 2018, increasing their majority.)
- 2) Please note the significant decline in the yield on the 10 year this week, falling from 4.22% to 4.06%, an incredible move. Mathematically, such a decline in yields should be viewed as a positive for equities based on discounted cash flow models. From a fundamental standpoint, this decline comes as no surprise to the Miller Tabak Economist, Paul Shea, based on his views on inflation. "Inflationary concerns have been quickly dispelled by the data," as he has been writing for months. Shea has been predicting for months a meaningful decline in the yield on the 10 year in 2026 , which was perceived by most as bordering on lunacy when first stated. His target for the yield on the 10 year by Christmas is 3.75%.

- a. Shea notes in his report this week entitled "The Labor Market Remains Frozen" (your inbox late Wednesday USA/early Thursday EU/UK) that while the household survey on employment was "undeniably excellent," all of the other evidence is "pointing in the wrong direction." Aside from private education and healthcare, employment in the rest of the labor market has "declined for eleven of the past thirteen months." We are now in a "waiting game" as to whether hiring or layoffs will accelerate; this "low-hire low-fire" environment may continue.
 - b. Shea also espouses the view and is "confident" that the widening 10-2 year Treasury spread is "not useful" for forecasting the US economy. It mostly reflects a series of the Trump Administration's policies that have elevated term premiums. The Fed's switch to a large balance sheet with ample reserves has "permanently" reduced the yield curve's usefulness.
- 3) Continuing with the theme of the impact of the fixed-income market on equities, HYG, one of this writer's most important indicators for reasons enumerated on multiple occasions, remains relatively quiet, above both its upward sloping 50 and 200 day moving averages. The Index successfully tested the lows of mid to late December and continues to act as a balm for equity investors' nerves.
 - 4) This writer has been noting since early December that the Transpos, after lagging badly for most of 2025, began displaying positive relative performance across all industry sectors that are components of the Index. The Transpos are up over double-digits y/t/d despite a stumble this week related to AI-disruptions for the logistics oriented companies, namely CHRW, EXPD, and RXO. The argument can certainly be made that the Transpos are a significant beneficiary of higher cap ex due to the newly enacted accelerated depreciation allowance as well as the economy being stronger than most observers had been predicting.
 - 5) Relative to the SMH, which many investors including this writer believe to be the most important etf in the equity market, there were wild price movements with the etf shrugging off a price decline early this past week to close higher on the week. Fundamentally, the gargantuan increases in capex announced by the hyperscalers should be most beneficial to the components of this etf, as reflected in the price action.
 - 6) Small cap investors continue to relish the outperformance of the RUT vs. the SPX. Clearly, there has been a mean-reversion trade in view of the questioning of the AI/megacap story. Furthermore, bulls on the small-caps are emphasizing the potentially better earnings growth for these US-focused companies rather than those with global exposure. Moreover, investors appear focused on companies that use AI to boost productivity instead of those companies building AI.

- 7) Markets outside the USA continue to display excellent relative and absolute performance. This writer has been harping on the strength of the Nikkei following the election of Takaichi (aka Mrs. Thatcher) and her stunning victory on her recent gamble with the snap Election. Given that the Nikkei is up 13% y/t/d, the Index is certainly entitled to some back-and-fill, but the fundamentals suggest continued strength. Also note the EEM etf is up 13% as well y/t/d. A softer US\$ and easier global financial conditions are key components of this move as well as the view that the markets are relatively cheap vs. developed markets.
- 8) Physical gold/digital gold: It is difficult to state reasons that there should be a substantial pullback in GLD other than the reversion to the mean argument and the fact that some investors were disappointed with the data presented two weeks ago by the World Gold Council indicating that purchases by central banks and sovereign wealth funds had declined approximately 20% in 2025. Bulls are instead concentrating on the continued massive holdings of stablecoin issuers which are required to have either gold and/or Treasuries underlying the amount of stablecoins that have been issued and will continue to be issued. Secretary Bessent has recently stated that he envisions the stablecoin market expanding from its current \$300 BB to \$3 Tr "soon." After a disastrous week for crypto, a rally ensued on the belief that \$60,000 is a fundamental low point for bitcoin as that is the cost to miners of minting. For there to be further upside momentum, there needs to be a resolution of the intense fight that has prevented the passage of the Clarity Act in Congress.
- 9) For non-US citizens reading this piece, I wish to offer an apology as a US citizen for the awful behavior this week between Pam Bondi and certain members of the Congress. It was an embarrassment for both sides of the aisle.

Jeff

Have a productive week and enjoy the rest of the long weekend.

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