MILLER TABAK + CO., LLC

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1) Grappling with the conundrum of whether or not Bessent has lost the confidence of investors is the obvious and most compelling issue facing investors for the foreseeable future. The Financial Times, a constant critic of this Administration, ran front page headlines this weekend—"US Bond Intervention Backfires"/"Faith in Greenback Rattled"/"Bessent Under Pressure" relative to the skepticism that has evolved following Bessent's statements that the US Treasury would "at least" double its purchases of long-term government debt beginning September 9th from $2bb to $4bb. Bonds immediately rose in price with the 30 year yield declining 4 bps from its 20 year high. However, this reversed itself in a "New York minute." The next day he then promised to "bring equilibrium" to the $43Tr market. The yield on the 30 year closed the week 4 bps (4.27%) down from the high yield of 5.31% but the 10 year yield closed at its high tick. What else Bessent might draw from his "toolkit" (his word) as a balm is yet to be seen and one can be certain that Warsh will be grilled on the issue this week in Jackson Hole.

2) A plethora of issues now face equity investors. First, the bears smelled an equity route given the bond markets reaction to Bessent's comments. Instead, while the S+P 500 closed down 1.8% on the week, and to the chagrin of the bears, commodities, gold and digital assets all rallied smartly. Granted, the announcement by the SEC of new digital asset regulations and the revived notion that The Clarity Act will be brought to the Senate Floor after Labor Day added to the reasons FBTC and CRCL each rallied 22%, but SCCO was up 17%, FCX 15% and GLD 5%. One suspects the momentum shift to these names will continue unless there is a better view of what Bessent will accomplish. Secondly, if yields stay at these levels or move higher, all equity investors must deal with the adverse consequences of using such yields in any discounted cash flow model for valuation. Thirdly, will Bessent be able to convince investors that he is "America's top bond salesman," providing the marketplace with proof that there will be an "increased focus on fiscal consolidation" and that there is a "very good chance" that the US has hit the peak of its government deficits.

3) The bears will focus on the fact that the US deficit now exceeds $40Tr with daily interest of $2.7bb making it very unlikely that Bessent can "bring about equilibrium." Moreover, these higher buybacks of the amount of long-term bonds will almost certainly force Treasury to issue more short-term debt, leaving the department exposed to fluctuations in rates. It must go noticed that Bessent in 2024 criticized then-Treasury Secretary Janet Yellen for pursuing a similar policy. Furthermore , the bears are virtually laughing out loud at the idea that Vice-President Vance's planned fraud crackdown will improve the expense to revenue ratio for the US government, as Bessent has suggested.

4) There is a chance that the Fed could compound these issues by raising rates in September, which the Miller Tabak Economist, Paul Shea, labelled as "Madness" in his most recent report. Shea, who was virtually the only economist on Wall Street to get the July jobs report correct as well as the recent CPI data, sent a brief note to clients this week emphasizing that Warsh is not "looking through" an energy price spike and needs instead to worry that high yields are creating a concerning fall in demand. This would of course dovetail with the earnings report from WMT this week. Shea also notes that, to play devil's advocate, he will assume inflation does require a response. Yet bond markets are not pricing in one or two short-lived hikes, but rather they are "pricing in a 400 bps fed funds rate 5-10 years out, but neutral is likely closer to 300."

5) The action in the US$ has also unnerved investors as lack of confidence in the greenback meshes with what has occurred in bonds. Using the DXY, this index has fallen from a high of 101.80 in late June to a low of 98.56 this week before closing the week at 98.80. A more positive view is that a weaker dollar aids EU investors in the US and the decline in the DXY has been orderly. The fear of course is that a gyrating yen would cause a meaningful reduction in the carry trade. Scanning several AI sources, there is no comprehensive "global carry-trade position" with which to quantify this because the trade is often implemented with FX swaps, forwards, options, structured products and prime-broker financing rather than visible cash borrowings. The yen traded in a narrow range this week so this remained out of focus. Interestingly, the AUD/JPY ratio often viewed as a proxy for risk on/risk off in equities increased this week.

6) Regular readers of Sunday Comments know my most important indicator for the direction of equities is HYG. Given the headlines in the govvie market this week, there was little discussion of the high-yield market. From an equity standpoint, bulls can take solace in the fact that HYG closed only slightly lower this week and did not eradicate the lows of the previous two weeks. Moreover, the 50 day moving average returned to an upward sloping position, barely, but the 200 day is still downward sloping. A return to an upward sloping 200 day and a close in HYG above that figure would turn this writer decidedly bullish on equities. Contrariwise, a move below the 79.1-79.37 level would be definitively bearish.

7) After a stunning rally in the private credit stocks which took, for example, APO up 23% from the late June lows to the close a week ago Friday, this group notably retreated this week. There is clearly a knee-jerk reaction in this group to government bond yields which in reality has little to do with the excellent fundamental backdrop upon which all of the management teams have commented in their earnings' calls.

8) An important theme on which I have written extensively this year is the contention by the bears that the market will ultimately succumb to its historic 18% correction witnessed in all but 2 of the Post World War II mid-term Election years. One is reading more about this now as appears all but certain the Republicans will lose the House, paralyzing Washington for the next two years. However, as chronicled by this writer, thus far we have instead witnessed week by week intense corrections group by group and even name by name rather than the overall market and I continue to believe this will continue to be so. One can just site a few of the myriad of stocks that have suffered the pain of an 18% correction while the market marched merrily to new highs—MU, WMT, META, TPR, ULTA, GOOGL. The bears are vociferously arguing that that the VIX is showing utter complacency—it finished below the y/e close a week ago and advanced only slightly this week—but the same argument could have been made months ago. Given how quickly minds are changed by the "theme of the week," I contend that this group by group name by name correction will continue rather than happening to the overall market. I have sited numerous times in the past what happened in the mid-term elections relative to losses for even Reagan, certainly the most popular post-WWII President. The only 2 times that a President did not lose House seats in the mid-terms were Bush in 2002 (+8) and Clinton in 1998 (+4) but this was after Clinton's devastating beating in 1994 when he lost 54 House seats,

Jeff

Have a productive week.

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