

Positioning remains relatively static from the previous monthly update as the themes are largely intact. The recent announcement of Kevin Warsh to replace Jerome Powell as Fed Chairman has garnered quite a bit of headline talk. Some refer to him as hawkish and others dovish. My take is that his opinions are strong, but loosely held. In his previous stint at the Fed, he was in favor of quantitative easing during the crisis, but wanted it quickly unwound. The bottom line for me is that he is quick to react in either direction. Of course, nothing will truly happen until May if he makes it through the confirmation hearing.

The US economy continues to grow at a relatively rapid pace with recent GDP at 4.4%. The turning of the calendar to 2026 brings with it the new tax incentives and spending initiatives from the OBBB. A combination of easy monetary policy, big government spending, and increasing capital expenditures (especially in AI world) should give the overall economy a strong tailwind. It is difficult to be negative the stock market with cheap energy and strong spending. Without an exogenous event, the overall world economy should continue to hum along.

While not a new position, the short in the British pound continues to be a staple. The British government remains between the proverbial rock and a hard place. They need to keep tax revenues high to offset their increasing public debt, but also need to find a way to push their economy to expand further. All the while, their energy policy has rendered them into the position of trying to lift a bucket while standing in it. There is a little bit of headway on the energy front, but nothing close to the radical changes necessary to provide the country with cheap energy. When you add in the political problems, it certainly points toward a weakening pound.

Nothing has changed regarding the yield steepening trend in the US. The continued tax/spend or tax less/spend (depending on who holds office) continues unabated. With the US government adding ~\$1 trillion in new debt every 180 days, the long end of the curve should continue moving toward more policy risk, thus higher rates. The front end is anchored to inflation expectations and unemployment. Both of these have stabilized in recent months indicating no real need for the Fed to do much in the short-term. The current spread has the 10 yr note ~0.70% over the 2 yr. Over time, that should move out to 1.5%.

Sincerely,



Stephen Davis
February 10, 2025

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