Deutsche Bank's Ozan Tarman and Aditya Singhal on Understanding the Macro Risks | Odd Lots

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SUMMARY

The podcast episode features a discussion on current market dynamics, particularly focusing on the challenges and strategies traders face amidst conflicting headlines and economic indicators. The guests, Ozan Tarman and Aditya Singhal from Deutsche Bank, emphasize the importance of having a structured perspective when trading and the impact of macroeconomic factors, including AI developments and geopolitical tensions.

- *Traders are navigating a complex market with conflicting headlines, making it essential to adopt a long-term view across asset classes.*
- *The concept of "empty buses" suggests that many investors are not fully engaged in the market, leading to potential opportunities.*
- *Earnings growth, particularly in tech, is a key driver of market resilience despite economic challenges.*
- *The geopolitical landscape, including U.S.-China relations and the Russia-Ukraine conflict, significantly influences market sentiment and positioning.*
- *AI is a major narrative driving stock market rallies, with both the West and China investing heavily in technology.*
- *The podcast highlights the increasing relevance of Chinese financial assets, including government bonds, as investors reassess their portfolios.*
- *The need for the West to build its manufacturing capabilities is underscored, especially in light of competition from China.*
- *Upcoming UK elections and their potential impact on fiscal policies are also discussed, with a focus on the implications for market stability.*

Someone needs to make like
a motivational poster that says, 'Lord give me the confidence of an equity
investor trading on an Axios headline.' Yeah, like I feel like that would
that would sell out. Yes. We have one open. Yeah. Okay. Generally we, we have no choice. If you were to look at the rates
market, for example. Yeah, as an example. Right. There was, Six
Sigma event that happened within it. At some point the pricing gets to a level
where it doesn't make any rational sense.

Okay. So you start to look at that on

a, on a more structured basis, and you start to ignore
the noise in the middle. And whether we like it or not, we have to
operate with that kind of philosophy. So you take one side or the other. It's very difficult to trade the headline because it's impossible, because as of now you had two conflicting headlines and you can get caught out. So most people
have come to that understanding.

So you've taken a perspective or a view
that either this is going to get resolved or you believe it's
not going to get resolved. There's a way of expressing it
within the five asset classes where you might get the most convexity. Similarly, if it gets resolved, there are certain things that actually might work which haven't yet worked. So you take those sides
and you just sit and wait. Hello and welcome to another episode
of the Odd Lots podcast.

I'm Tracy Alloway and I'm Joe Weisenthal. Joe, our live show in London,
recorded May 7th at Wilton's Music Hall. A lot has happened since then. in markets, it’s
hard to have a markets conversation that you know isn't out of date
within like a minute or two. Yeah. But but I think this one,
this one carries on. I think this one is still relevant. Well, you know, I have to say, I always feel a little anxious about recording markets episodes because of this very phenomenon.
But this is true for a live.

And our recording shows
that by the time it comes out, who knows how much all have changed.
This is why you should go to the. This is why you should get this exactly
where I was going to go. It's actually good to record markets
episodes of the live show because it's like, all right, you create an inducement
to get people in to buy a ticket. But again,
you know, with a lot of these things, like how traders are digesting
this particular moment in time, sure.

The headlines
and the prices on the screen change, but there are certain like principles and frameworks for understanding what's going on that will be sort of useful regardless
of what's happened in the meantime. You mentioned frameworks, and that is
the perfect framing for this discussion. So we indeed had the perfect guests. We spoke to someone
who's been on quite a few times before. One of our favorites for letting us know what the big money is actually thinking about and trading.

We spoke with Ozan Tarman He is, of course, vice chair of Global

Macro over at Deutsche Bank. We also spoke to his colleague,
someone who hasn't been on the show before,
but who has quite a reputation as one of Deutsche Bank's star
bond traders. Aditya Singhal
he is the head of EM, trading across rates FX and credit at Deutsche Bank. So take a listen. Let's start with the obvious question. Lines on the chart. Keep going up.

Despite
what would seem to be some challenges to the global economy,
to put it mildly. Why? First of all, even when I walked
in, I was checking for you guys. It wasn't like that 15 minutes ago
when, we're now recording this at 733. Exactly. 20s. And when, one agency claimed that, Operation
Freedom was back on that, President Trump
could try to open the Hormuz by force. S&P and oil S&P didn't like that at all. Oil was surging
higher than Al-Jazeera denied.

So we're all calmer again. But, bottom line is why we keep going
higher despite everything that Javier and Lorcan said
is because busses are empty. When I say busses are empty,
you know, I only I don't only talk to my, portfolio managers about men
on the street, to my college classmates. One of them was like,
what do you mean? Busses are empty? That means investors don't have it. The analogy is a bit like, closer to April 2nd, April
9th of last year when we had the big tariff shock billboard
up, we thought that it would be the end of the end of the end of the year,
end of the markets.

And then President Trump, stepped back. Yeah. And the markets never looked back. I mean, similar coincidence or not,
March 31st is the is the first time, he claimed through Wilshire Journal
that he would separate state of foremost and operation that the two could go separately. None of that happened. But that was the first,
big breath market took. And on April 9th, exactly the same day,
the big first postponement came, I said, you're not going to do
anything for two weeks.

And since then, markets never looked back. The historic led by tech
Nasdaq and S&P rally. And you know, I talked to a lot of people
a lot of, you know, key ladies, guys, honestly,
maybe three, 4 or 5 people really believed in this rally since April, April 1st,
April 9th. That's one big part of it. But it can't be all positioning

also fundamentals right. Earnings. Yeah. Again head of sales. One of my legendary researchers
Jim Reed just today, he was on Bloomberg as well,
talking about earnings in Q4 of last year, just 13% growth, Q1 record is biggest
in five five years, led by take 24%.

That engine keeps us keeps us going. Yeah. The earnings are what they are. So, here's something, Caruso Ozanne came in
and he gave us the latest headlines. Thank you. Because I haven't
I hadn't been looking at on my job. Yeah. You didn't
look at his phone for 15 minutes. Yeah, yeah, it's a record. You know, I mean, how do traders deal with the market in which they're
just the sheer number of headlines? How would you and how do they know
what to take seriously?

And like, you know, what's real? What's not real? Like, how are they
how are they ingesting news? So from a trading perspective,
yeah, fundamentally five asset classes. Right. So you have a thematic view and you have
rates of credit equities and commodities. And a lot of people are, fixated or
are mandated or asset class or say, right. So they, they have no choice
but to stick within that kind of regime. And, and then, of course, are you
if you're a real money investor or a hedge fund or if you are, a sell side trader,
just depending on how you are positioned.

Right. It's not really it's difficult
to get in and out. Right. So thematically, you have to take a structural long
term view, see what every asset class is pricing on that particular view and,
define an upside. Downside kind of scenario. And based on the liability profile
you have. And that how you define that
is the function of the money you have. Or what kind of drawdowns are acceptable. You take a particular position
and you let it play out.

So in this kind of environment
this is difficult. So what is the upcoming
kind of positive news that you can you can rely on to the market? Right. Today if you were to sit here today
you say, okay, so the fact that not much action has happened in the last,
3 to 4 weeks within the street, means that at some point or the other,
the resolution will come. Pakistan is is mediating, as we can see,
there's been enough talks happening.

So you assume that resolution should come. That's what the market is.

Pricing theoretically. You also have a situation with Russia
which is developing, right, Russia-Ukraine war,
which could be positive also. And then you have, the visit, the US visit to China,
which also has the atom positive. Now of course, there's a lot of it isn't the price per se,
but fundamentally speaking, as a trader, you position yourself and,
and then you just choose, you know, at some point to, close it to the time,
get out.

That all make sense to me. But, like, are traders
sitting there with a truth social window open,
like the literally congestion of news? How do you do it? I'm just getting the messages from you. Yeah, right. Just kidding. Well, someone needs to make,
like a motivational poster that says, Lord, give me the confidence
of an equity investor or trading on an Axios headline. Yeah. Like I feel like that would
that would sell out. Yes. We have one open. Yeah.

Okay. I just, I genuinely we,
we have no choice. But but fundamentally,
it's, it's it's like this. Right. So you, you make up, you see what's so so we had, if you were to look at the rates market, for example, just as an example. Right. There was, a Six Sigma event
that happened within it, at some point the pricing gets to a level
where it doesn't make any rational sense. Okay. So you start to look at that on
a, on a more structural basis, and you start to ignore
the noise in the middle and whether we like it or not, we have to
operate with that kind of philosophy.

So you take one side or the other. It's very difficult to trade the headline
because it's impossible, because as of now,
you had two conflicting headlines and you can get caught out. So most people
have come to that understanding. So you've taken a perspective or a view
that either this is going to get resolved or you believe it's
not going to get resolved. There's a way of expressing it
within the five asset classes where you might get the most convexity.

Similarly, if it gets resolved, there is
certain things that actually might work which haven't yet worked. So you take those sides
and you just sit and wait. You know, you mentioned, irrationality
just then, which means we should talk about AI, right? Because all of the stock market rally
at this point essentially seems to be a bet on AI. What are you hearing from your clients? I was on on
how comfortable they feel with us. Well,
just two days before the yuan war began, we were in West Palm

Beach and Miami with us as well, visiting clients and then the whole talk
of at least that town.

But the US in general
was, that famous 3D piece, the other comedian snaps,
something big is about to happen. How, in 12 to 18 months, 50% of white collar jobs could be wiped out. And what that could mean for, for rates,
that in itself is very, very telling. Right. And because of that,
and one source claims numbers, if you remember us, ten years, that Friday before the bombs came in close at 393. Okay.

And one of my more famous friends
clients sends me a message on that Friday night bond. Is the new gold 393 top. They close then, it on more happens. Not that surprising, but of course the
how it played out is very, very surprising. War elation hikes getting priced in for people completely pushed aside the slowdown job growth labor part of it and then started completely focusing
on the equity the growth of the AI engine.

Again,
if you just go back to January, February, we were quote unquote happy
because the thing was building out. It was a rally,
but it was a rally led by Russell as well. Would it be? Oh, yeah. Oh, it's like a long time ago
Magnificent Seven was forgotten. And now, Lord, behold, on the some of us,
thank God, have three months memories. Now, now you're complaining about. Oh, it's all about seven stocks. The breadth is to two.

We're just fighting ways. You try to, fight and wrestling. We wrestle with the rally. But. So back to your question at the moment. Yeah. The Kool-Aid is to believe that this I,
Ron, may have another 1 or 2 years, to go pull to the John's public, one of definitely my, more famous
friends clients today claimed that that's the case
and made the 1999 technology. So either you swim
if that's or try to feed it.

You know, this is the other thing. All right. So we talk about the,
you know, these very worrisome scenarios, the price surge in oil,
but very worrisome scenarios about deep shortages
in various commodities. And that's one reason to be worried. But then there's this other thing
that basically, you know, the disinflation is stalled out. If arguably it's going
in the other direction, rates around the world, in, you know, we're
I think, you know, there was some sort of what was UK
30 year, the highest since 1998.

Yeah. So again, just intuitively, you would say these things compound each other and should really take the wind out of the sails of risk appetite. And yet. So how is it that like, even like, you know, what we see going on and selling a how does the selling and sovereign bonds mix into this market, in their view? So let me, let me take this to actually give you a thematic kind of how to take care of things. Right?

Okay.
Just just to give a perspective. Right. So ultimately, there is only one thematic view that matters for the next few years. Right? And that is, if you would, as you, you have China in China, allied countries, and you have the West. Right? If you were to take China and China line countries, right, and they were in space, what does West need theoretically, in both manufacturing and services? And if you go to the reverse route, what is and if the West was in space, what is China and China aligned countries need both in manufacturing and services?

And the reason I'm bringing to this point is because I want to give a perspective. So what happened right in the last many years. So this microphone, for example, right. This most of the materials in here comes from China. Right? China aligned countries almost 90% right. Manufacturing capacity. The world is 55% right now China link. But some places almost 90 to 95%. Take an example of cobalt cobalt refining oil in China. Now in the past what happened was they would give you this microphone and you would give them dollars or pounds or euros or whatever it is.

So they hold that. So China holds that. What is the most rational thing for them to do? The most rational thing for them to do was to buy your land with that money. But you said no. Then they said, I'll buy equities. You said no to that, to then they said, what? You know what? I'm going to buy the commodities that you might need in the future. We said, fine, do it. Which is what China did for years.

Then here's the interesting thing you said in return, let me send you my services. So let me sell you fine wine. Let me send you the Gucci. You know more, you know, phenomenal bags, top educational service, education, education and a lot of other things. And then also services, services, whether it's, Microsoft Excel or whatever it is. Right. Sure. But now what's happening is you have that side of the world which is also building their own services.

Tax. So tourism is now onshore. They started building their own cars up the chain value chain. So you're getting to a stage where if you expand this,

you kind of thematic view, you in the West have to literally build
all of it from ground up. So if you assume China was in space, they can still disrupt
the services sector, but they can't disrupt the manufacturing
sector theoretically anymore because you can
you will have to build it all up.

So if you want cobalt and if they say no, you have to refine it
minute refine it. You need to have companies that refine it. You need to have the engineers
that that do that work. And fundamentally, that's what
the fundamental paradigm of the world is. So when you talk about sovereign
debt, yeah, any holding of or any equity holding, ultimately the creditor is
China and China allied countries. They are the creditor in the West,
and we are the debtor.

And this is only increasing. So if you believe the wizard,
what is the ultimate objective
agenda of the Wizard of, of the US? To China is to balance the current account
to some extent. That's one agenda. And there's of course there are certain other aspects to it,
but fundamentally that's what defines the the kind of make shift
of the next kind of year to three years. And whether we like it or
not, we have to build this.

I want to come back to China versus the US on
AI in just a second, but I definitely want to also ask this question
because we are in London, how big a deal are the UK elections? From your respective perches, the local
elections that are happening tonight is important
because basically the UK and abroad, there is for the past two years at least,
a big fight between fiscal dominance leaves, ten years, 30 years, more
importantly, 30 years, around the world.

Will they get more out of out of control
since we are in London, will we have the the Liz Truss two moment or, will financial repression mean meaning
emerging markets style Treasury and central bank for working more closely
together, especially on issuance, issuing less on the,
long end, more on the short end, taking a name, taking a risk. But, making sure that ten and 30 years
are under the leash, in fact, a really key investor less so much as in a smaller roundtable.

What happens if all four of them? This was probably August. This before back to school September races
began. Us, France, Japan and UK,
if all of them had their trust moments. And then September. Damien
I remember I was talking about this. Yes, it happened,

but only four hours in the gilt market. That was it. I remember that little mini moment. So now there is an excitement again, you know, because UK has a different risk
premium. Net international investment
portfolio i.e.

has a budget deficit
and the current account deficit has to be nice to the foreigners
because they will buy your, our are that question marks on what this local election
may mean for the government. Will there be a change there
or in the Chancellor? Will somebody more to the left come in
all these are, on the question mark. Famous last words. My feel is, for the moment, still,
the financial repression, will win. We won't have the trust the moment two,
but obviously we they will need a little bit of luck, for the Iran situation
to continue to calm down because, unlike the Truss moment, Truss moment one now, all of this is happening for reasons
much beyond the UK.

Joe, I am impressed that we always managed
to schedule these macro conversations for maximum event risk between when
we record and when it actually publishes. So we have the UK elections, everything happening with Iran
and we have non-farm payrolls tomorrow. There's so much going on
and we just apologize in advance. This is why people should buy tickets
to the event. That's right. If you have to hear this conversation
on the podcast feed, who knows, it could be out of date.

But those who are here
don't have that issue. Is Emma ification of Western policymaking. Is that a
is that an apt characterization of it? Setting aside specific,
you know, elections here or there, you hear that term
ramification of and is that apt? It again, it depends. Right. So it's country to country. In this again paradigm, you have this so so let's
the legalistic UK is an example.

Let's elaborate further. Real rates are reasonably high. The country's gone
through a difficult situation. We could see what happened with oil,
the pass through effect. But it's happening
pretty much everywhere else in the world. You have, current account, which matters
mostly in most countries, including UK. You have an input factor of energy and you have an output factor of services
effectively that you said. So depending on where you are in
the world, which country you depending on who you are, if you have a situation

where you are an energy importer.

And your exports are highly dependent on effective services,
which are getting disrupted. Courtesy. Yeah. You're in trouble. Alongside if you are an importer
of manufacturing also or goods again you're in trouble. So this adjustment will happen. So you have to have allies. You have to have people who you do
a quid pro quo with. And that adjustment
is what we are seeing effectively. And markets are finding a true balance
of risk premium along side.

Well, okay. So on this point, two things you've said
which sound very rational on stage, having a series of allies,
I don't know if those are stable. And then also,
you know, this aspiration to balance the, you know, balance the current account
between the US and China. And sounds nice, but like,
do you think like you. Yeah. Again, it sounds nice. Are there actually any real prospects of
moving the dial on that kind of thing? So, again, I don't want to comment here.

This is in terms of our house view, but, but I'll give you a general perspective
on the same example. If you were to get West in space and ask
China, what does it need from the West? Yeah, it's not much. Yeah,
I've heard apart from Boeing and Airbus by parts, if you were to just look it
from that perspective. So you there is a desire and maybe there is and they will oblige. I do think there is certain things like are for example, agricultural products that could benefit,
that has certain aspects.

But fundamentally,
unless we choose within the West to build the whole manufacturing stack, it's going to be very difficult
to keep this current account balanced. Yeah. And on top of it, the biggest worry and
again, I'm maybe jumping on this point is when people talk about the fact that
the West is investing in the CapEx type, that the West is investing in
the key is not what the West is doing. The key is to understand
what China is doing in it, understand what they are doing with the deep sea version for models
to glorify the Hawaii clusters.

I can go on with an optical computer,
quantum computing. There are many more things
that they are actually investing a lot in, which effectively becomes a true competition
and a cost factor reduction. If there is a risk,
that is the risk to watch out for, right? It's not to study what we are doing here
because we will find ways to keep evolving. But you have, yeah, an ecosystem there

which is actually quite, quite well versed
and also has a lot of capital behind it.

And, you know,
there was somebody who was quoted that most of the engineers today actually
are like, yeah, that part of the world. Wait, another sorry. Go ahead. Another thing
that the market miscalculated, right? Right after Trump got elected
the second time. December 24th January 25th. By far the big consensus rate
besides the US ten years going to 550. You know, everybody being
the long was to buy these the other few options strikes at 775. Everyone I knew was buying dollars.

You know there you go.
And they keep going. Yeah. And what happened is it's the stock
the start currencies were on CNN. So that shows you even though some people
are really into saying markets are never wrong, you're wrong. That can be very, very wrong itself. So we are all human beings and certainly
that can make markets very wrong itself. One more Asian country
that we need to talk about to bring you right to the markets,
Japan. Right.

So to your question, high in oil,
higher rates, why doesn't this thing bring down equities. Why are these no why is this guy
all is on sending messages busses empty. Nobody's buying it.
It can be quite frustrating right? That Thursday Friday
it almost happened because, you know, it just feel itchy,
and looked like it would break 162. Looked like, us it would continue
to sell off, Hormuz again. Question mark. There was there wasn't a detente. And then, just like the rate check of,
at the beginning of the year, one of my closest friends
on not on our trading floor, but on the sector, I had heard this
big Irish voice, you know.

You know, this is in fact, New York
calling in on behalf of Bank of Japan. I'm like, what's going on with this guy? And because he was shouting around
because they they want to make sure that, you know, public information,
they told the three banks that they called would let others know that they were
watching similar this time around. They didn't call. Bank of Japan itself came
and they punted for risk parity. What does that mean?

They punted for lower volatility,
common waters, and stable rates. The moment, they push down

yen, dollar yen, lower yen, stronger U.S rates, calmed down, equities
got a bit, etc., etc. so it's always or tug of war on one side. Respect the camp. Mostly central banks
trying to keep things calm and on the other side
sometimes my dear fast money friends looking for more 2022 like years Christmas come early
every Friday, another 50 basis point sell off on TV, us ten years
higher volatility, etc. etc.

and I'll stay in the middle
and try to decide which one is right. Can't you just tell your fast money
friends to calm down for a little bit? They usually listen to me a detail. I want to go back to what you were saying about U.S versus Chinese AI models, because if we think about
how much the stock market rally is actually dependent on AI at the moment,
and how much of the AI story is dependent on this idea that, like,
well, the West has these amazing, more sophisticated, albeit
more expensive models for which the, you know,
Tam is basically the entire world, and you're arguing
that actually that's not the case.

And China's models are perfectly suited
for its own needs. Elaborate on that. How are you as a sort of trader, evaluating these models? How much of your day basically is now
just trying to figure out AI? So it's a very, very good question. And the key here is, is to understand what are you currently. There is a whole
there is a very strong narrative. Yes. Also a very strong use case. Now the valuation stack was as a forward earnings kind of multiple.

Right. If you were to look at it
right, sees that there is going to be a huge CapEx investment within the Western
stack for the next 3 or 4 years. And that's what's created
this rally within various companies. And the second order effect companies. China is doing something similar. It's very clearly said in the West that
they are effectively using Nvidia chips. And Nvidia is just a companies,
just to give an example, but just their chips to train the models.

In reality, now they have Huawei chips,
which are pretty much parallel or comparable to H100 processors. The big problem,
and that the West is not appreciating is, is that the reason West
is investing so much in CapEx is because they want to effectively get
to superhuman intelligence very quickly. So almost everybody's saying, okay, you have a model
that has 7 trillion parameters. Now we go to 15, maybe 25, 50
and it becomes self-learning and it's reinforcement.

But the reality is
you have things like distributing the AI. You have things like which is actually
being worked on in the West. You have also things
which are very different, which is something
as simple as quantum computing. Or I would say optical GPUs. Right, is another concept.
Please read about it. So you have currently, there was a there
was a narrative in the West where you had GPUs of Nvidia and
you got a copper connector between them.

Now you have optical compute phones
or optical phones effectively, that have done very well
in the last many kind of months. So this narrative will remain right. Having said that, if you keep an eye on what's going on on the other side of the world,
also use case in terms of actual uptake of usage, because it's not like I'm
going to run five different AI models together. I'm going to probably converge to one
at some point, will eventually cause
some kind of a problem in the future.

The second thing that you have to keep
an eye on is also robotics. That's the other aspect,
which is going to be the second narrative that is actually going to start
within the Western stack, which is the Elon
Musk revolution of Optimus. And again, something to keep an eye on
what's happening in China within it versus what's happening in West,
and how deficient is West on it? Just real quickly because we have like
a minute left, you're talking about, okay, this microphone
that we're talking to almost certainly, the majority of it or all of it
probably made in, China.

How much do you see
clients or people that you talked to purchasing Chinese financial assets,
including Chinese government bonds, which more and more people
are talking about, not just the safe haven, but a safe haven
that's done well in a diversifier. And how much is that becoming a meaningful
part of portfolio construction? It can grow. I mean, already it's happening
with, effects. But, you know, people, first,
denial, then anger, then acknowledgment. Right there. They realize that a free trade
train has moved.

To your question, government
bonds, Chinese. Let's say it's, just 2 or 3 years ago,

even when I went to, Singapore and Hong Kong's of the world,
people were either fearing, claiming, being very confident
that China was an investable. Yeah, I remember and deep inside I was saying,
if Chinese aren't investable, you know your future in Singapore and Hong
Kong. I turned out to be correct. Right. But it turns out, it
it it starts with effects, but there is still a lot more room to go
in, Chinese equities and Chinese bonds.

That boss is also not fooled. Okay. All right. Lots of empty busses around. Ozan and Aditya thank you so much for coming on Odd Lots Really appreciate it. That was our conversation. Recorded live in London on May 7th.
I'm Tracy Alloway. You can follow me @tracyalloway And I'm Joe Weisenthal
You can follow me @thestalwart Follow our producers Carmen Rodriguez
@carmenarmen, Dashiel Bennett @dashbot
and Cale Brooks @calebrooks and Kevin Lozano
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