



WHO IS MORE BELIEVABLE: CENTRAL BANKS OR INTEREST RATE MARKETS?

Agenda: Central Banks vs Markets

	Fed Reverses Q2, floods with liquidity	Fed pauses start of Q2, tentatively reversing in 3Q 2023	Fed pauses Q2 2023, tentatively reversing in Q4 2023	Fed pauses Q3 2023, watches for Q4 2023
Fed Funds rate	2.25	4	5	5.25
Earnings				
Current 2023	2.5%	2.5%	2.5%	2.5%
Current 2024	10%	10%	10%	10%
Revision to forecasts 2023	-5.0%	-7.0%	-10.0%	-10.0%
Revision to forecasts 2024	5.0%	-5.0%	-7.5%	-10.0%
New 2023	-2.5%	-4.5%	-7.5%	-7.5%
New 2024	15%	5%	3%	0%
Valuation				
Current STM P/E	15.3	15.3	15.3	15.3
In one year, STM becomes NTM				
NTM in one year, no price change	15.3	17.3	18.4	18.9
Target P/E in one year (16.8 currently)	20	18	16	14
Price change	30.4%	3.9%	-12.9%	-25.9%
S&P Target	5,430	4,328	3,625	3,086
US P/E	22.6	20.4	18.1	15.8
Inflation	2	1.5	1	0.5
Aussie 10y Bonds now	3.60%	3.60%	3.60%	3.60%
Aussie 10y Bonds +1y	3.50%	3.00%	2.50%	2.00%
Change in 10y Bonds 1 year	3.9%	8.3%	12.9%	17.7%
Weighted Bond change	2.9%	6.2%	9.7%	13.3%
Factors	Value & cyclicals	Quality & Growth	Quality	Quality
AUD	0.85	0.75	0.7	0.65
Probabilities	10	35	35	20
Weights				
Stocks	90	60	50	30
Bonds	2	35	45	65
Cash	8	5	5	5

Scenario 1: Fed reverses quickly

- Yields tumble initially
- Wild risk-on rally, buy growth, cyclicals
- DXY smashed
- EMs, commodities fly
- Yields rebound just as fast as sticky inflation freaks out markets
- End point either global rebound and resumption of disinflation...
- Or, sticky inflation and rebound, and crash as Fed forced back in.
- 10% probability

Scenario 2: Fed pauses soon, starts cutting by Q3

- Yields tumble
- Corporate profits fall modestly on big margin squeeze but multiple expansion lifts stocks somewhat anyway
- Buy quality
- DXY falls but not so far
- EM rally persists, commodities struggle
- 35% probability

Scenario 3: Fed pauses soonish, starts cutting by Q4

- Yields plateau then tumble some more
- Stocks fall. Corporate profits down moderately on big margin squeeze and multiple expansion delayed
- Buy quality/defensives
- DXY remains firm
- EM rally peters out, commodities fall
- 35% probability

Scenario 4: Fed keeps raising rates, pauses for rest of 2023

- Yields rise then crash into 2024
- Stocks fall hard. Corporate profits down big on top and bottom line pressures
- Buy quality/defensives
- DXY rises anew
- EM falls, commodities fall
- 20% probability

Viewer question of the week:

Will the Fed lead the market in 2023 or follow it?

Drop your answers in the comments

Agenda: Implications for markets

- Inverted yield curve signalling recession
- Stocks expensive given declining earnings prospects
- Inflation has lowered level of Fed “put” and needs a commodities bust
- DXY bull market to make it worse. AUD to continue falling
- Eventual capitulation of stocks

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