

PALOS

The Palos Perspective

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CONTENTS

Gold is the "Topic du Jour"	1
Disclaimer & Contacts	4

A Macro Market View by Hubert Marleau

Gold is the "Topic du Jour"

Gold's breakneck rally gained unabated momentum this week, rising more than 5% to surpass the \$4,200 mark. I took the opportunity to sell my remaining holdings of small gold exploration plays, but retained all of my cash-flow-producing gold stocks, my reasons for lightening up these positions having been given in last week's missive.

Gold was the hot "topic du jour" at the IMF and World Bank meetings among the finance elite. The bottom line here is that the move toward it is on the one hand a manifestation of political concerns and on the other an application of political pressure. Meanwhile, pressure is building for the IMF to sell a portion of its own large gold reserves to generate funds for foreign aid.

What Took Place in the week ended October 17?

On Sunday, the S&P's 500 futures bounced back strongly, rising 1.6% after President Trump backpedalled on his threats to impose an additional 100% tariff on Chinese imports and export controls on any and all critical software in response to President Xi's threat to dramatically expand China's rare earth export controls, saying that he can also play the same game too. Investors were heartened, however, by comments from Trump in a social-media post: "Don't worry about China, it will all be fine!"

On Monday, investors bought the dip, rallying the S&P 500 to 6655, up 1.6%, amid a softer tone on trade relations between the US and China that appeared to have emerged. The broader markets were not as enthusiastic, the DXY advancing to 99.28 and gold to \$4,129.

On Tuesday, the market opened deep in the red as investors watched the U.S. and China spar over trade, but managed to recover in the afternoon sufficiently to recover their morning losses. First,

A Macro Market View by Hubert Marleau

three big money market banks posted better-than-expected results as dealmaking, corporate lending, and trading fueled profits. Second, Powell announced publicly that the Fed will soon stop trimming its balance sheet, offering no push-back against rate-cut expectations, and said that the monetary authorities have a good handle on the economy. The S&P 500 fell marginally to 6644, down only 0.16%.

On Wednesday, US stocks finished mostly higher in a choppy manner, lifting the S&P 500 0.4% to 6671, buoyed by encouraging earnings from Bank of America and Morgan Stanley.

On Thursday, the S&P 500 fell 0.6% to 6629 led by the financial sectors, as investors grew nervous about cracks in the regional private credit space, pushing sharply the CBOE Volatility Index fear index above 25, its highest level since the tariff-fretting days of April 2025, and potentially implying that this pullback might not be a buying opportunity for retail dippers.

On Friday, stocks clawed their way back, shrugging off concerns about the banking industry for two reasons. First, it seems like there are only a few cockroaches and therefore not an infestation. Second, loan losses are par for the course: they affect rates of return on diversified portfolios of loans and usually do not trigger a wide-credit crunch. (Interestingly, the reaction in the high-yield junk bond market was muted: credit spreads in the bond market were lower than the previous week.) Meanwhile, the retail dippers were back in the market, focusing their optimism on Bessent, who was scheduled to meet his Chinese counterpart to reduce trade tensions and on an increase in the Atlanta Fed's GDP growth estimate to 3.9%. Indeed, the two best early warning signs of a recession are showing no signs of a slump: budgets for takeout dinners are holding up well while going out to restaurants and bars were up 6.5% over the past 12 months.

The Near-Term Stock Market Outlook:

Last week. I wrote: "A period of consolidation is likely after a 3-year run, but the equity rally is underpinned by solid earnings; and that should support the market. Citigroup and Goldman Sachs

A Macro Market View by Hubert Marleau

said: 'S&P 500 earnings are expected to grow 8.8% year-over-year in Q3, on sales growth of 6.4%.' According to Seaport Research Partners, those numbers may prove to be too low. FactSet published on Friday that analysts are projecting annual earnings growth for the S&P 500 of 14% from the end of 2025 through 2027."

Of the 51 companies that have reported so far this third quarter season, 82% have beaten expectations by an average 6.3%, according to Tom Lee, head of research at FundStrat.

There is some evidence that the market is tiring: retail confidence to buy-on-dips seems to be topping out, suggesting that a pullback may be in the cards as speculation in the hot tech sector is being expunged. I view this low conviction around equities as a contrarian positive. Why? There is no economic evidence that assures that either a deep or a long pullback looms, for the broader uptrend remains intact. The AI-driven productivity surge is real, suggesting that the US economy is in the midst of a deflationary boom. In this connection, those productivity gains that we are currently witnessing significantly reduce the probability that the AI-boom will pop.

Moreover, a series of factors - the length of the shutdown, the imposition of tariffs, the slowing growth of the money supply and the risk to maximum employment are pushing monetary policy towards the neutral state, that being a policy rate of 3.50% and an end to quantitative tightening.

In an email message from Tom Lee, late Thursday evening, he reiterated his call that the S&P 500 will finish the year at 7000. Meanwhile, Edward Yardeni, a believer that the U.S. economy is in the midst of an unprecedented productivity boom, believes that the S&P 500 will get to 10,000 by the end of 2029, with forward earnings per share rising to \$455.

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