BEHIND THE MARKETS PODCAST: A DISCUSSION WITH WARREN PIES FROM 3FOURTEEN RESEARCH

Wisdomtree EU
02 Dec 2021

Warren Pies, Founder and Strategist at 3Fourteen Research joined regular host Jeremy Schwartz, Global CIO at WisdomTree, on the Behind the Markets podcast.

Introduction and Background

It was interesting to start by hearing a bit about Warren's background. He started out as an attorney, and then he transitioned over to research on markets at Ned Davis Research. His focus there was predominantly on commodities and real assets, and he left after Ned Davis Research wanted to stop focusing on commodities coverage. He started 3Fourteen Research about a year ago.

Who is 3Fourteen Research

3Fourteen takes a more advanced, quantitative approach to building different models. The firm's 'high level' asset allocation view is that the next 25 years in the markets will look very different from the 25 years that we have experienced. Investors were well served by the 60/40 equities/fixed income approach for the past 25 years—but this may not work as well in the coming period.

What is the model telling us today?

Warren discussed one of 3Fourteen's key models, which includes 17 different assets. The drivers of the model include:

1. Trend
2. Correlation
3. Volatility

The current positioning is taking a very clear stance on 'short duration.' One way this can be seen is that the longer-term Treasury bond exposure is only at about 1%. Equity exposure is roughly neutral, at about 40%, but within this exposure the model has shifted more towards small caps and the value factor. The main shift was out of bonds and into real assets—notably real estate, bitcoin and gold are at the highest levels that were seen in the model since the pandemic began.

Notable research with big implications for equities vs. bonds

Warren cited a piece that 3Fourteen put out looking at the relationship in terms of returns for stocks vs. bonds. He took the 100 worst days from the last 25 years, based on equity returns, and saw that bond returns were positive on 83 of these days—a great ratio of success as a possible hedge. If one did the same exercise, but looked instead at the period 25 years prior to 1998, during the same type of days—the worst 100 for equity returns—bonds only had positive returns on 35 of them.

Two simple variables account for a lot of the movement of stocks and bonds: economic growth and inflation. Over the past 25 years, inflation was largely removed from being a real concern for investors. There was a huge trend toward globalisation which led to much lower inflation, particularly in durable goods. Cheaper durable goods prices effectively pulled the Consumer Price Index lower over this time, improving the prospects for bond returns generally.

What are some of the best hedges if people are concerned with Inflation?

Warren thinks that oil will merit special consideration as an inflation hedge in the coming years. He cited how we have seen the 'shale revolution' since about 2014, driving prices lower. However, going forward there hasn't been much further capital investment in oil, and yet the demand for oil is expected to keep going up in the coming years. After the supply and demand balance normalises in the next six to nine months, Warren's view is that the focus will eventually start to recognise that green energy is great, but oil demand shrinking to zero is not in the immediate future even if the mix of how people get energy is evolving more and more toward cleaner sources.

What about gold & crypto?

3Fourteen also looks at gold and crypto. Towards the end of the discussion, Warren discussed his view that bitcoin has been taking investor flows away from gold. Warren believes that bitcoin has a great use case for wealthy individuals stuck in closed economies, who want to take their wealth to countries with strong property rights, like the United States. Bitcoin has been rising, and so has the dollar, and this is one possible explanation, at least in part.

You can listen to the full episode below.

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