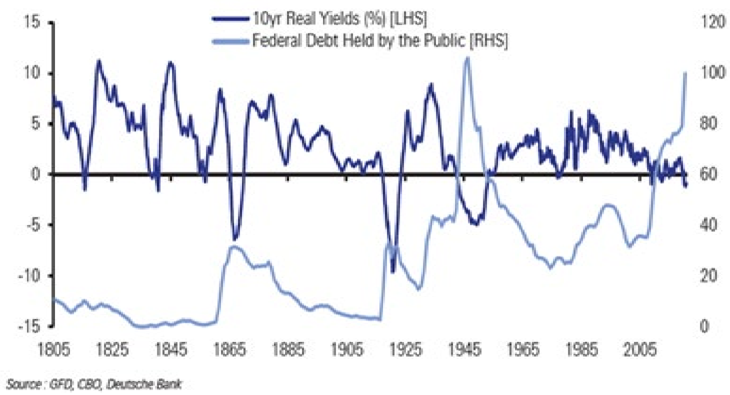
Fixed Income – Chasing Zeroes

As Federal debt continues to climb to higher and higher levels, you have to wonder how far we are from the markets imposing consequences. Many have expecting the bond vigilantes to appear over the last 12 months as government spending skyrocketed, but these revered characters may be more myth than reality. The yield on the 10-Year U.S. Treasury Bond has surged to 1.50% in recent days for the first time since January 2020. However, what is surprising to many is that the inflation-adjusted yield, or real yield, is actually falling. This is because inflation expectations are rising faster than the yields, primarily being driven by the dramatic rise in Federal debt. Investors might be collecting higher interest payments on debt, but it is being more than offset by an increase in prices. Expect to see the dollar come under weakness if Federal spending does not decline soon.



Technical – Hockey Stick Speculation

If there was ever a chart as a precursor to a bubble or mania, it might be a chart of Call Options. The chart has been gradually trending higher for 30 years, but in 2020 we saw spikes in volume that were unprecedented. The latest data suggests demand for speculating in stocks is at historic levels as the chart would make even Bitcoin envious. When investors buy “Call” options, they are paying for the right to purchase a stock at a pre-determined price in the future. For example, a year ago you could buy Tesla calls giving you the right to purchase the stock at $150/share when it was trading at $133/share for the next year. You might have paid $20/share for the call option, giving you a profit of $530/share today even after the $50/share price decline today. This is clearly being driven by speculators, which tends to end poorly for those entering late in the game.