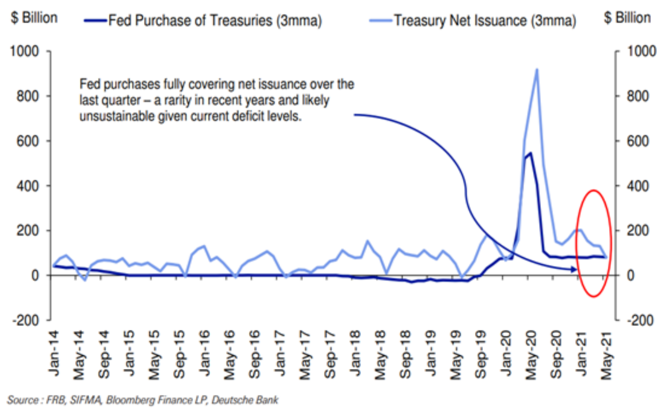
Fixed Income – Last Buyer Standing

You would not be alone today in questioning who is willing to buy U.S Government debt at the current yields, given where inflation is now and is expected to go in the future. How do you make financial sense out of buying a bond that does not mature for 30 years that yields 2.1%, when many are forecasting that inflation may average 4% over that same period? For example, $100,000 invested today in a 30-year Treasury would only retain $30,821 in purchasing power at maturity if inflation averaged 4%. If your assumption for inflation is 3%, you still are left with only $41,200 in real terms at maturity. A 10-year Treasury today will lose more than 25% in real terms at maturity with just 3% inflation. As the chart demonstrates, among the only parties willing to lock in these losses is the Fed.



Technical – Running out of Margin?

One of the data points market technicians keep close tabs on is margin debt on the S&P 500. History suggests that when margin debt peaks then retreats, it creates pain for investors long in the stock market. We are at the highest margin levels in history, just exceeding $1 trillion in June, doubling in just 18 months. Margin works wonderfully when stock prices are rising, but forces selling when stocks begin to decline. Just as margin creates artificial demand when markets are rising, they create artificial selling in a downturn. Margin levels peaked in 2000, 2007, and 2018 in advance of large stock market declines. Those hoping peak levels of margin will no longer be a leading indicator for the stock market may find themselves disappointed. Historically, the stock market does not sell off until margin starts its decline, so the bull market may have a bit more room to run.