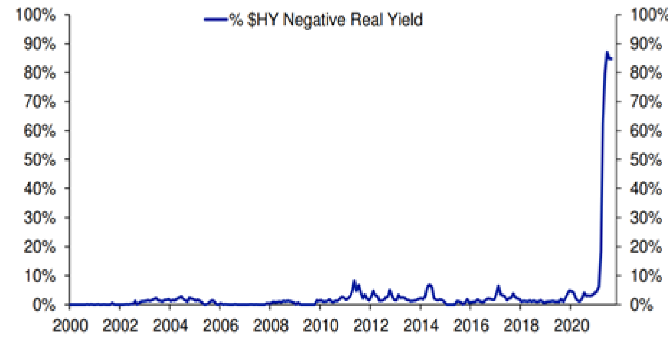
Fixed Income – Stupidity on Display

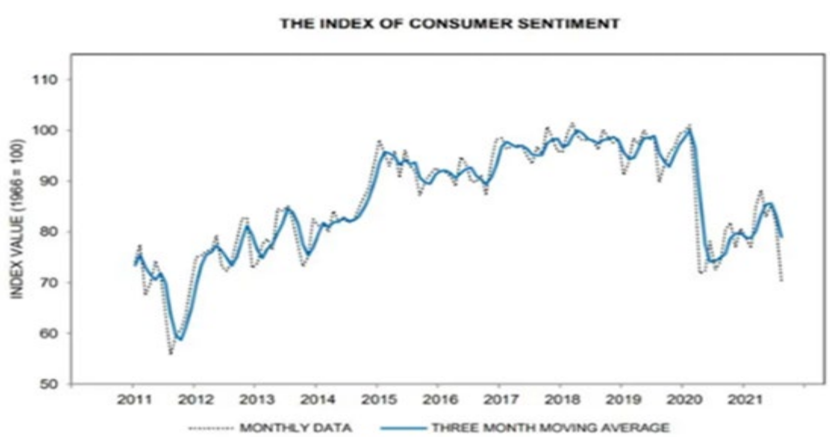
High yield data goes back more than 25 years and the average real yield has been just a tick below 4.50% per annum, motivating some investors to take on some credit risk. It may still make sense for tactical investors to own high yield, but buying it at a negative real yield seems crazy. Historically somewhere between 0% and 3% of non-investment grade bonds trade at a negative yield, but this is the "new era" of investing, boldly (and stupidly) going where no investors have dared to go before. Today a stunning 85% of US high yield is trading at a negative real yield. At the end of 2020, less than 4% of these bonds traded at a negative yield. Even if inflation went back to 50% above the Fed's target of 2% (3% for those in Rio Linda), an astonishing 35% of junk bonds would have negative real yields.



Source : Bloomberg Finance LP, Deutsche Bank

Technical – Sad Sentiments

While many talking heads continue to tout the current strength of the US economy, signs are appearing that suggest this is more wishful thinking than reality. The trends in Consumer Sentiment have a very strong correlation to changes in GDP over time. It will likely only take the threat of a contraction in GDP for markets to react from all-time highs in the wake of the ongoing pandemic. It is telling that confidence is waning at a time of peak corporate earnings, peak economic growth, and peak fiscal stimulus. Equity market cheerleaders are proclaiming we are in a goldilocks environment and investors have nothing to be concerned with. Intuitively, many investors are realizing the bears might not be that far off. With stimulus programs expiring and the Fed announcing they will taper bond purchases, caution makes sense.



Source: University of Michigan