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Freak show

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Despite massive ongoing debt monetization being deployed by the Fed, ECB and Bank of Japan, it's not enough to keep global interest rates totally docile amidst the ongoing proliferation of debt being spun out form literally every corner of the planet. Especially from the corporate and public sectors. Combined, the Fed and the ECB, by themselves, are still engineering a stated QE tack that amounts to over $220-billion per month of freshly conjured-up "money." The Bank of Japan is a moving target as its being steered by its so-called "*yield curve control"* policy. This means theoretically, that the Bank of Japan can buy (monetize) whatever if it takes (zero-to -infinity) in order to cap the rate on the 10-year Japanese Government Bond (JGB) at zero. But the Bank of Japan is also buying, "*huge amounts of relatively risky assets such as (passive stock and securitized real estate investments) as part of efforts to revive growth and achieve its elusive 2% inflation target,"* according to a Bloomberg report published in early December of last year. The Bank of Japan, via its ongoing and relentless market-propping efforts, has also finally become the largest single owner of Japanese stocks. Between the BOJ and Japan's massive *Government Pension Investment Fund,* the two now own an unnatural proportion of Japan's publicly traded stock— the world's third largest stock market. Citing Satoshi Okumoto, chief executive officer at Fukoku Capital Management Inc., in a recent Bloomberg report, he laments, '*Regardless of which whale is larger, the dominant presence of these two public entities has raised concerns over their influence on market prices. The combination of a state-run institution, the BOJ, and the country's representative public pension fund, the GPIF, buying up local equities feels distorted.*

Index	Feb. 28 2021	YTD%
S&P 500	3811	+1.46%
Dow Industrials	30932	+1.01%
Nasdaq Composite	13192	+2.36%
Value Line Arithmetic	8714	+10.12%
Russell 2000	2201	+11.44%
U.S. Dollar Index	90.88	+1.05%
Gold (ounce)	$1729.90	-8.65%
Silver (ounce)	$25.45	+0.06%
Amex Gold Bug Index	250.44	-16.42%
Oil (NYM Lt Sweet/barrel)	$61.50	+26.75%
30 Year Treasury Yield	1.65%	+0.53%
10 Year Treasury Yield	1.46%	+0.53%
2 Year Treasury Yield	0.15%	+0.02%

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Jim Gant, founder of *The Interest Rate Observer* and former credits market beat writer for *Barron's* explained during a recent CNBC interview how the 10-year U.S. Treasury bond, perhaps the world's most critical price-setting component which transmits its influence for how prices get set across all global asset markets has essentially become corrupted by central banks' non-price sensitive buying of it via their ongoing interventions. Grant asked rhetorically, what sounds more attractive, to borrow at 3% for 30-years or to own a 10-year Treasury bond yielding 1.6%? Without saying it, Grant basically explained how over ten relentless years of central bank radicalized interventions it has delivered us the increasingly clear freakish market deformities that would be more suitable for a carnival side show.

But as we know, it's not just the U.S. Fed. It's basically the entirety of global markets being squeezed, manipulated, muscled and cajoled by this cabal of unnatural, *non-price sensitive* voracious buyers of global assets. If anyone can foresee a path for how these huge and intrusive market propping entities can ever return real price discovery back to the markets themselves without them crashing, I'd love to hear from you. But in the interim, it's getting freaky. And as we've seen in recent weeks, even what would have once been considered an almost imma-

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terial nudge higher in interest rates is seemingly causing significant angst throughout global markets. Either way, I now believe that these central banks are inclined to do almost anything within their powers to quarantine price discovery from their bizarre and distorted freak show markets to protect their massive and mutant asset bubbles. However, I believe at some point they will lose control as the peculiarity of their increasingly radicalized intrusions will eventually prompt a rush to the exits in a gesture akin to, "*Okay...I've seen enough, I'm out here!*"

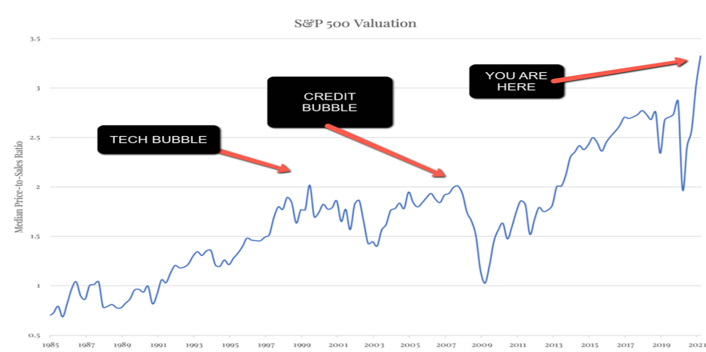
It appears that the highs of mid-February for the Nasdaq's fad and meme favorites are going to continue to act as significant overhead. Those highs also coincided with perhaps the most ostentatious display of unhinged speculation that I have witnessed in my nearly 30-year career. That includes even the very late stages of both the dot-com bubble in 2000 and the real estate/credit bubbles 2007. But on top of that, we have also seen the 10-year yield move from 1.1% to 1.7%, a level that once reached transitioned the prevailing market narrative from, "*No worries, rising rates are just an indication of the looming robust recovery,*" to "*Oh my god, what if money is no longer free and what does that mean for an economy hooked on cheap debt and hooked on all of the market's bubbles which it has spawned*?"

With that said, there is no chance that the Fed and its complicit cabal of serial bubble blowing, wealth cleaving global central banks can seriously contemplate easing off the gas pedal. Not only will they never run out of sufficiently concocted political cover, no matter how logically challenged, to keep on doing what they're doing. But the global economy will continue to be impeded by world record levels of debt relative to GDP and the subsequent siphoning of economic capital necessary just to service this world's all-time record debt-to-GDP albatross. Central banks will never arrive at the self-implicating conclusion that the world's economy is sluggish because their policies have fomented this world record proliferation of debt now sapping the global economy's vitality. Instead, they will look no further than the mere sluggishness, and conclude that all it needs is just more of the same.

Yet, to a degree central bankers are at least somewhat aware of just how precarious of a situation they have fashioned for themselves, the global economy and its political implications. We now have a global economy that has become predominantly dependent on asset bubbles, and whatever modest portion of those bubbles actually trickles down to the lower half of global wage earners and pensioners. These bubbles and the continued nourishing and servicing of these bubbles has moved to the forefront influencing monetary policy decision making even as policy makers continue to allude to *real economic factors* as being their true guiding light, no matter how disingenuous their data mining appears to be to anyone subjected to spiraling healthcare, food, education and real estate costs. In recent weeks, Fed members have specifically clung to their mutilated and hedonically adjusted official "inflation" data, the Consumer Price Index (CPI) to make their case for why the cost of living is still "*too low*', while ignoring the more obvious spiraling cost spike distortions taking place in the real economy for everyone to see and feel. By the way, how did paying too little for life's essentials ever become something that must be eradicated and now the centerpiece of Fed policy? Fed mouthpieces describe "inflation" in such an innocuous way that leaves us asking: *Are they describing my cost of living or something else? Or, do I no longer know the meaning of inflation?* This is even as these same bubble blowing central bankers simultaneously dismiss their officially sanctioned government tabulation on unemployment and instead points to data that again lends political cover for their true policy—propping up their massive asset bubbles. In other words, the Fed is going to mine for whatever data provides them with the most convenient political cover for protecting their now death-defying asset bubbles. And as they get more and more boxed-in, their justifications for doing what they will keep on doing anyway will only come into greater conflict with that of the physical world and things we can witness with our own two eyes feel with our own two hands.

In his recent shareholder letter, Warren Buffet alluded to "*market illusions*" as being emblematic of almost every prior extended business and credit cycle. This is clearly pertinent in today's environment, an environment which I have described as approaching *maximum gullibility*. As testament to this extreme level of gullibility are the myriad of ridiculous and shaky themes of today's market environment which passes as "investing." Last spring and summer's chase of bankrupt Hertz (HTZGQ) and JC Penny's respective bankrupt equity stubs counts as an obvious case. Meme stocks such as the clear and obvious mutant GameStop (GME) ordeal and Reddit flash crowd manipulations of incredibly flawed and fundamentally challenged entities are another. SPAC-o-rama is yet another. By mid-March, the volume of new Specialty Purpose Acquisition Companies (SPACs) had already surpassed last year's record issuance of these so-called blank check IPOs. The price of Bitcoin recently surpassed $60,000 per that *delusive virtual bubble coin*, and a non-fungible token (NFT) of a piece electronic art was sold for $69-million by a living artist. Virtually everything now seems to be the same trade, whether it be a meme stock, an electronic coin or token or a detached garage near Toronto—recently listed for over half-a-million.

I haven't even mentioned anything about fundamentals. Those might be even more ominous than the more intangible, "*it might be a bubble when*," attributes described above. But let's at least scratch that surface. Below is a chart of the median *Price-to-Sales* ratio of the S&P 500. At 70% more expensive today, by that valuation metric, than the 2x median price-to-sales ratio reached at the peak of the tech bubble and also the credit bubble, I believe, tells us that market illusions are thriving.



Median Price-to-Sales ratio of the S&P 500, 1985-Current (Source: The Felder Report)

Remember, when you ponder what the above chart might be telling us, corporate revenues are the purest numbers on a corporation's income statement. Corporations have a difficult

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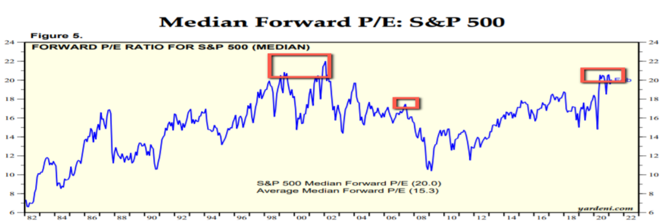
time applying aggressive accounting techniques aimed at puffing-up top line revenues, even though its possible. Not so the further you scroll down the income statement. They only become less pure the further down the corporate income statement you get and by the time you arrive at the *earnings after taxes* line, in all likelihood, as it concerns American finance and accounting, circa 2021, there are plenty of "*promotional techniques and "imaginative" accounting maneuvers,"* that have taken place in between as Buffet describes in his latest investor letter. For that reason, comparing the current median *Price-to-Sales ratio* of today to that of the prior two epic bubbles may be the purest apples-to-apples comparison we can get. If that's the case, is 70% more expensive than a market that eventually crashed roughly 50% reason enough to have some concerns pertaining to its fundamental underpinnings?

Even as the current "forward" median *price-to-earnings* ratio of the S&P 500 is not quite as extreme as the year-2000 peak, there are other factors, or props, which if we were to recalibrate today's environment so that it would be a fair apples-to-apples comparison with that of the year 2000, even today's median forward *Price-to-Earnings* multiple would likely be substantially above that of the tech bubble's peak level. Particularly the excess earnings being generated today strictly due to the differential in prevailing and artificially suppressed interest rates and hence the lower cost of debt financing vis-à-vis that of the 2000 tech bubble. Also, the less than genuine boost of EPS (earnings per share) today, due to massive corporate share buybacks, much of which have also been financed by adding artificially cheap debt to corporate balance sheets and reducing the number of shares outstanding. Alas, in the year 2000, S&P 500 firms spent $196-billion on share buybacks, or roughly 1.53% the total market-cap of the S&P 500 in that year. By 2018, S&P 500 companies were spending $875-billion on share buybacks, amounting to roughly 3.6% of the S&P 500's total market-capitalization. The current era's increased use of accounting gimmickry, in my opinion, also inflates the "E" and thus tamps down the key valuation ratio known as *Price-to-Earnings* or P/E of the broader market. Also, according to a 2019 report in CFO magazine, 97% of companies in the S&P 500 reported using non-GAAP (Generally Accepted Accounting Principles) accounting. This compares to 59% using the more loose form of accounting reporting back in 1996. Combined, given all the variables being used to goose the "E" for earnings, the denominator in the *Price-to-Earnings* ratio calculation, this is also conspiring to suppress that key valuation metric today relative to the year-2000 bubble. Its probably safe to say that if not for the three wind-aided variables helping to inflate "E" (earnings), today's P/E ratio is actually much higher than what occurred at the bubble's peak in 2000.



Median Forward P/E ratio of S&P 500, 1982-Current (Source: Yardeni Research)

Per a recent report from Christopher Cole of Artemis, he had determined that due just to the acute leverage of corporate balance sheets, earnings attributable to the artificially low interest rate environment today, accounts for roughly half of all prevailing net corporate earnings relative to what U.S. corporations would be earning if rates were normalized akin to the pre-2008, pre-central bank radicalization interest rate environment. Cole's analysis did not even attempt to account for the circular dependence of aggregate economic demand which is also dependent on stocks staying bubbly (i.e. the consumption wealth effect), which itself is dependent on those puffed-up corporate earnings which again, are further dependent on those artificially suppressed debt costs. Again, its easy to see how the artificially suppressed and the manipulated strangle hold on global interest rates gratis of the central banks is literally the lynch-pin holding this era's bubble monstrosity all together.

Going forward, the Fed is going to have to strike an awkward balance which will also entail outright gas-lighting of the more obvious inconsistencies we can witness with our own two eyes as it attempts to explain to its sponsored speculating community why higher interest rates is deemed to be an encouraging sign for more robust economic growth expectations, even as it will eventually become all to obvious and clear that the global economy, now so incredibly soaked with debt and leverage cannot tolerate higher interest rates. One of the Fed's key accomplice central banks, the European Central Bank (ECB), recently illustrated how that dichotomy is impossible to explain without defying simple logic. Like the Fed, the ECB has been insisting that it has been implementing all kinds of grotesque price discovery obliterating policy all in the name of trying to achieve *higher inflation.* Again, higher *inflation* is supposedly good. Wink, wink. We've expended significant time trying to explain how the Fed, ECB and BOJ have effectively hi-jacked the very definition of *inflation* to mean rising prices that are generally good for business conditions, but somehow being able to perfectly dissect that from effectively meaning a *rising cost of living for everyone else*, especially those that don't own a significant portfolio of stocks, sovereign and junk bonds and real estate. Oh, and now I guess even Bitcoin and non-fungible tokens. And now that its collective sovereign bond markets recently began signaling that indeed, higher inflation might just be on its way, as they claim to have been desirous of all along, and as yields in Germany went from negative to almost positive, the ECB reacted by speeding-up its bond buying via its current QE program in an attempt to again overturn that inflationary signal emanating from its bond market. The ECB's prompt attack on the burgeoning re-awakening of Europe's bond market price discovering was akin to saying, "*We need more inflation, but if the bond market begins to act as if more inflation is on the way, we will tamp-down that market mes-*

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saging, so that we can keep doing what we're doing all in the name of trying to flatter more inflation. And the reason we can keep doing so is because bond yields are not telling us that inflation is a burgeoning problem. Its akin to killing the town crier because you don't like what he's warning the townspeople of.

So, watching these central bankers inexplicable maneuvers amidst more grotesque and undeniable characteristics and instances of market deformities is going to become quite a juggling act and even more of a verifiable freak show.

Perhaps as testament to what stage of this bubble era we have arrived, during the recent bizarre run-up in shares of GameStop (GME), from under $20 per share at the end of last year to a high of $483 per share by late January, it was short-sellers who were singled-out as among the primary culprits. Not the carnival barking huckster, pump and dump sell-siders who are always there giving each other high-fives somewhere late in every euphoric business and credit cycle. Again, I've spent considerable ink over the years defending the general purpose and attributes of short selling, per se, and how they have historically served a vital purpose for a properly functioning market as well as having been credited with uncovering numerous instances of fraud, embellishments and fertile fallacies even as there are indeed instances where there are abuses that occur. But far less the number of abuses that proliferate on the long side. Again, find me one dedicated short-seller that ever rose to the level of abusive prominence and who inflicted near the investor losses that comes even close to rivaling Lehman Brothers, Enron, WorldCom, the lax lending environment of the credit crisis era subprime debacle or Bernie Madoff? Name one. You can't. The massive frauds, abuses and fertile fallacies are almost always fashioned as can't lose propositions where the perps are basically conspiring to inflate dubious themes. Like today.

They always say a bell never rings at the top of any bull market. But near the top, there are always an abundance of carnival barkers seemingly at every corner tempting us with things once never imaginable. Step right up folks. It's the freak show.

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