Twitter Thread by a h

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#irrationalebullience If you want to understand the nature of this asset bubble and the epic capital mis-allocation at it’s heart, look no further than rates. CB’s only tool to push an uber-levered financial system that is highly interconnected through derivatives
(1/N)

away from it’s natural convergence path towards collapse is to create opposing forces to push it towards divergence. Meaning: force, through financial repression, market participants to rely on price continuation, in a way that makes it self-fulfilling.
(2/N)

The tool used is rates as it is the basis off of which all other financial assets are priced. Today any buyer of $UST across the curve up to 30Y is guaranteed a loss given reals are negative throughout. So the only hope of escaping this GUARANTEED loss
(3/N)

is to angle for capital gains, i.e a continuous move downwards in real rates to push for some capital gains in real terms. The longer the financial repression lasts, the further investors are pushed out the maturity and credit risk curves.
(4/N)

Here are examples to understand what exactly is happening. If an investors buys a 5 Y UST he is guaranteed to lose almost 2% in real terms, so making that up in capital gains is much harder given the v short duration.
(5/N)

That investor can buy a 30 Y instead where his real loss is only 20 bp and the duration increases the convexity so his odds of capital gains are much higher. That’s for duration. Credit risk works the same. As opposed to duration investors take an idiosyncratic risk
(6/N)

in exchange of an improved yield. Except, this divergent market feeds on itself. And just like 30 Y UST are a GUARANTEED loss despite the massive duration risk, 40% of all IG index at par trades at real yields lower than -50 bp.
(7/N)

By construct, the loss guarantee keeps being pushed out the curves. This is clearly not a boring Fixed Income issue. It concerns all financial assets. Only it's easier to see in rates as it is a mathematical asset. Knowing the real rate is just a matter of calculus.
(8/N)

But this guarantee of loss have long migrated towards other financial assets. The most obvious being equities, cryptos and PMs. Only it is less obvious to see the certainty of loss in these assets because they are not mathematical but narrative driven.
(9/N)

Nevertheless any keen observer would have seen that by now, the only justification for equities' valuations is: « but the ERP » for $GOLD « hyperinflation is coming = reals are v negative » and cryptos « fuck this shit »
(10/N)

Now the problem is, when you race down to the bottom, you keep price momentum going short term but the positioning at the end of duration, credit risk, esoteric assets and shitequities ensures catastrophic losses. Just like in rates, these losses are GUARANTEED.
(11/N)

Now if you are wondering where you are in this roadmap to destruction, answer is : in the acceleration phase. Only a month ago, 35% of all IG at pars where yielding reals lower than -50 bp. That's a big move in a month. Where should you be by now?
(End)