



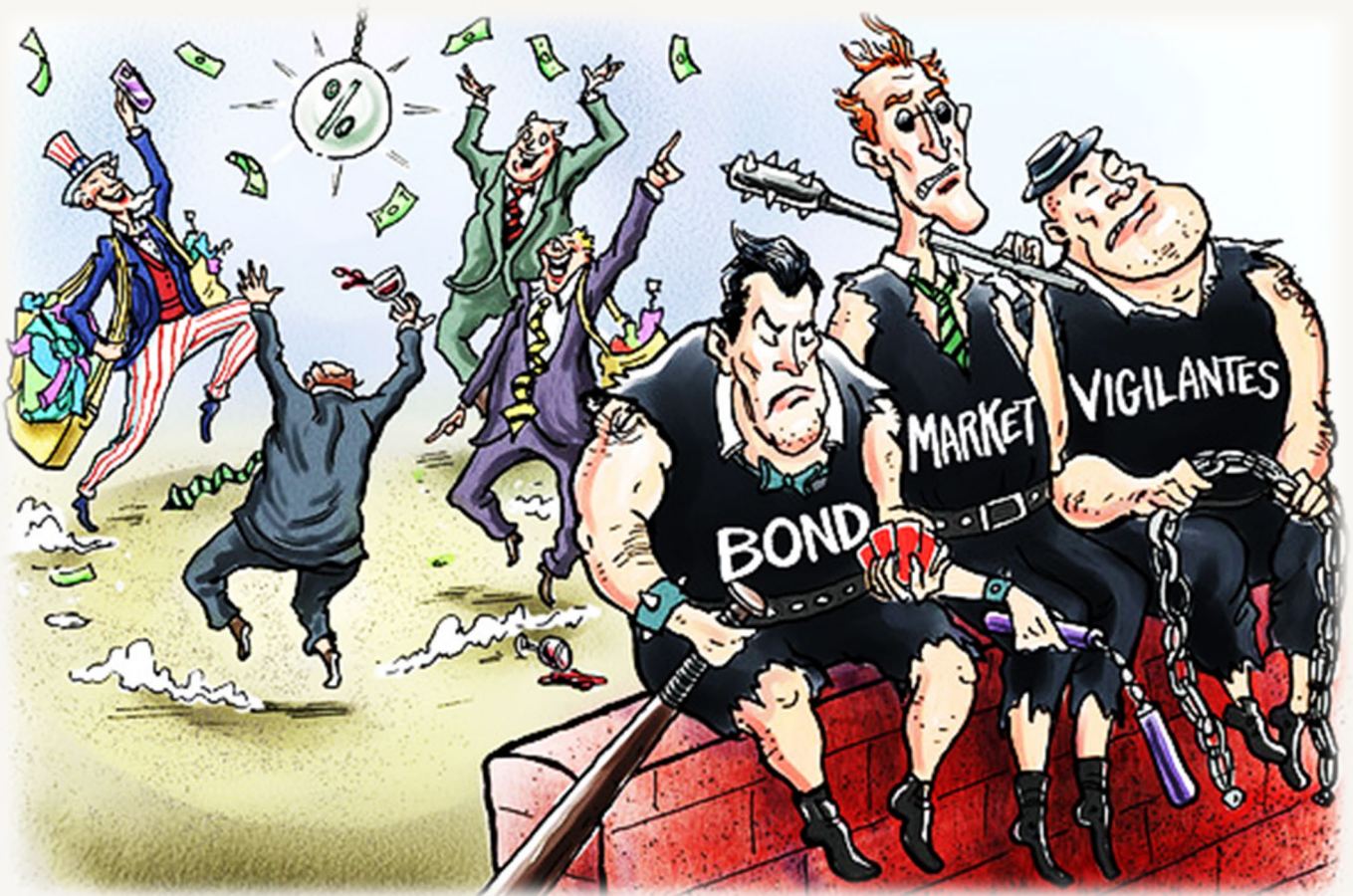
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Baron Point Research
The Bond Bear Market Meets the Fact of Life Cast Reunion 2022
September 26, 2022

Baron Point issue research describing current intermediate term trends and topics we find interesting. This research is intended to complement the regular Monthly Fact Sheets which include our monthly return updates.

If you have any comments please feel free to email us at info@baronpoint.com or call +1 (212) 248-2733 x701.



Source: The Wall Street Journal, a Dow Jones & Company



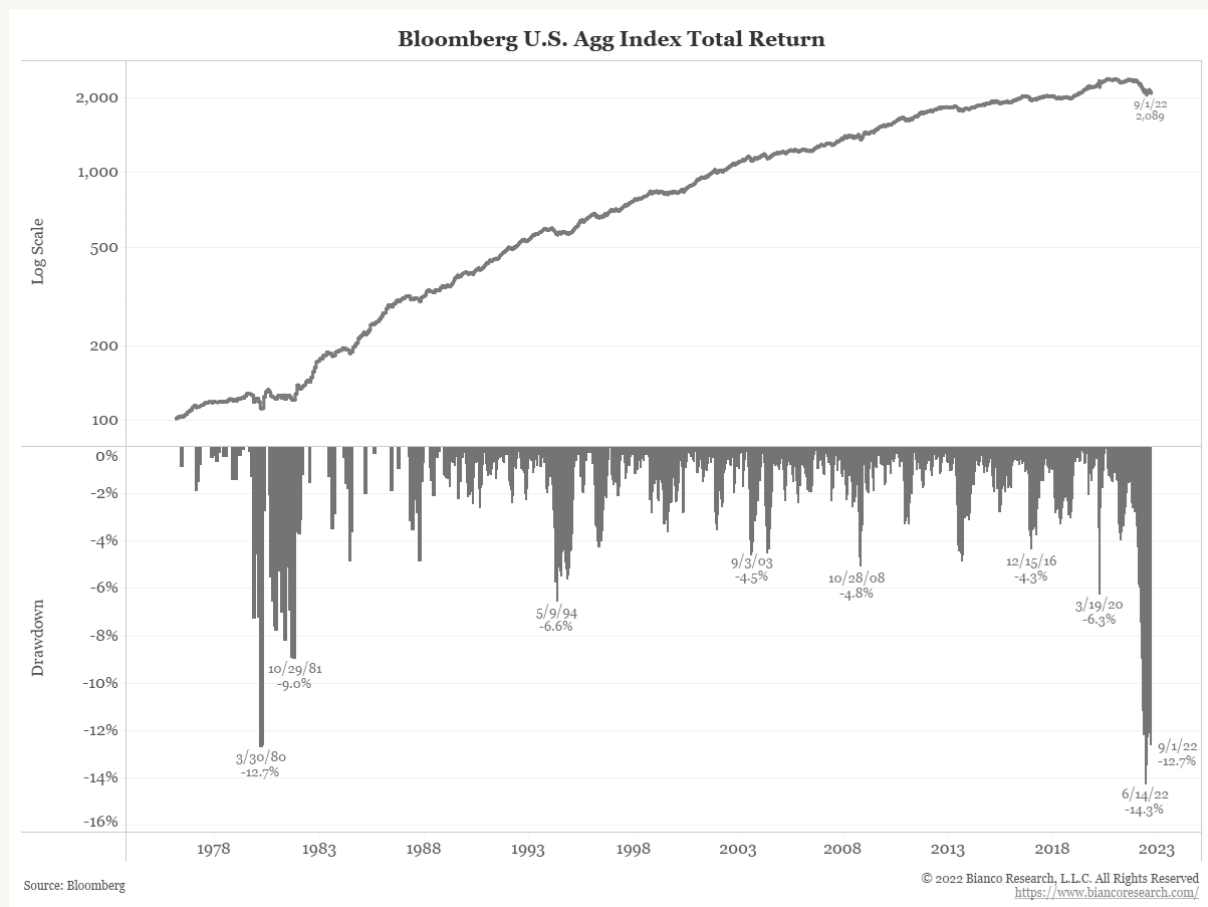
'If the bond market does not function, then no other market functions, really'

- Ben Emons, Managing Director,
Global Macro Strategy at Medley Global Advisors



The Bond Bear Market of 2022 By Baron Point Financial

Global bond markets are stuck in what we consider is one of their greatest bear markets ever! This year, we have already touched a new low point, and are on course for one of the worst bond market performances since at least 1926. Below is a chart of the Bloomberg U.S. Aggregate Index (formerly the Lehman and Barclays Agg.), showing data from 1976 for U.S. investment-grade bonds. This chart is courtesy of Bianco Research, with the data ranging back to 1976 for U.S. investment-grade bonds.



While U.S. investment-grade bonds are generally regarded as one of the most safe and liquid asset classes in the world available to investors; once liquidity dries up during a financial shock, just about all asset classes tend to follow bonds down. Metallica has a song for it called, Seek and Destroy!

So, let us now examine the iShares 3-7 Year Treasury Bond ETF (“IEI”) compared to nearly 97 years of history for a perspective of this year’s Fed monetary policy actions. As a reference source, we used data supplied by Ibbotson Associates for U.S. Treasury “Intermediate Notes”, with total losses including coupon interest from 1926 – 2022. 96 years and 9 months of data was considered.



As of Friday, September 23, 2022:

- The IEI is down **-10.74%**. That is 109% more than any full year versus Intermediate Notes since 1926;
- The T-Note Intermediate Futures are down **-14.74%**, year-to-date;
- iShares Core U.S. Aggregate Bond ETF (“AGG”) is down **-14.8%**, year-to-date; and the
- iShares 20+ Year Treasury Bond ETF (“TLT”) is down **-26.8%**, year-to-date;

For perspective, the worst long-term U.S. bond annual loss was -14.9%, during the prior 100-year flood, which suddenly now seem to occur every decade or so. According to the Ibbotson Associates data, the last great bear market in bonds occurring in 2009 during the Great Recession.

Congratulations policy makers, we touched another record in the 97-years old data series, with global bonds having done even worse.

The economy was fine, until the Fed took a bat to it

The problem we face in America is not economic. It is a Fed/political issue. As we outline above, save for the Great Recession, the U.S. Bond/Intermediate Note markets have never acted this poorly, according to 96 ¾ years of data.

The current situation is created by a bumper crop of politicians in power and policy makers at the Fed that think they can change reality. Shall Einstein’s theory of special relativity and the scientific method be next on the list?

As noted above, T-Note Intermediate Futures are down -14.74%, as of Friday, September 23, 2022. Here is how the U.S. Treasury Intermediate Notes index did, annually, in the other down years according to the Ibbotson Associates data:

1932 -2.32%	1994 -5.14%*
1955 -0.65%	1999 -1.77%
1956 -0.42%	2009 -2.40%
1958 -1.29%	2013 -2.01%
1959 -0.39%	2021 -3.35%
1969 -0.74%	2022 -??

Notice no losses in the inflation years of 1970 - 1982, and all the way up from 1970 until 1993

*** Largest annual decline in data series from 1926**



Too fast, too fast for love

In 1994 the Fed raised rates 6 times and a total of +2.5%, it was the most Fed Fund rate increases in a year since 1979.

Date	Fed Action	Federal Funds Rate
September 4, 1992		3.0%
February 4, 1994	+0.25%	3.25%
March 22, 1994	+0.25%	3.50%
April 18, 1994	+0.25%	3.75%
May 17, 1994	+0.50%	4.25%
August 16, 1994	+0.50%	4.75%
November 15, 1994	+0.75%	5.50%

This Mötley Crüe at the Fed in 2022 has raised rates 5 times and a total of +3.0% so far, and they are calling for more aggressive action before the year is finished.

Date	Fed Action	Federal Funds Rate
March 16, 2020		0.00%
March 17, 2022	+0.25%	0.50%
May 5, 2022	+0.50%	1.00%
June 16, 2022	+0.75%	1.75%
July 27, 2022	+0.75%	2.50%
Sept 21, 2022	+0.75%	3.25%



Is it the Puntrooskie, 1988 FSU v Clemson?

Is the Fed calling a Puntrooskie (RIP Bobby Bowden)? I was at the game. It worked; Look it up, Bobby fooled them!

In the current case, the U.S. government is trying to fool the American people with what American football teams call a silent count. The U.S. government does not want “money supply” constraints to hamper its spending habit, which is out of control, and this has contributed to inflation. Inflation is more pervasive than directly raising taxes on the people. Worse, inflation hits the poorest and the middle class in America the hardest. We all have to eat, heat and cool our homes, and we wear clothes, especially in the North in the winter. As my late Uncle used to say, all that matters, son, is food, shelter, and clothing yourself, the rest of the stuff is ego.

Below, takes a look at the rapid increase in the M2 measure of the money supply. M2 has soared to US\$ 21.71 trillion since COVID-19 hit the U.S., up about 25% from a year ago. This is the fastest growth on record.

YCHARTS

US M2 Money Supply

21.71T USD for Jul 2022

Level Chart





Milton Friedman taught us to watch M2, because nominal economic growth and inflation tends to track M2 broadly over time.

However, in this installment of Young Frankenstein (RIP Gene Wilder and Madeline Kahn), they actually tell us its different this time! They say it, don't look here, it doesn't matter, really? According to Fed Chairman, Jerome Powell, "When you and I studied economics a million years ago, M2 and monetary aggregates seemed to have a relationship to economic growth," but, "right now ... M2 ... does not really have important implications. It is something we have to unlearn I guess." Ah, the Abby Normal jar.



I wonder what Chairman Powell thinks of Joseph Schumpeter's writings? Does anybody sense some "creative destruction" occurring, globally? As a concept, we find it to be a key principle in understanding the logic of globalization. I suppose they took the classic book off the syllabus for globalization 101 class this semester?

At the same time as M2 balloons, U.S. interest rate yields are moving to multiyear highs with the 10-year note touching 3.69% on Friday (September 23, 2022). The **next test for the 10-year note could be the last cycle high of 4.01%**, which we saw for one day on April 5, 2010. As for interest rates in Europe, BofA research informed us on Friday, September 23, 2022, that government-bond rates in the U.K., Germany, and France rose at the fastest clip since the 1990s.



There is likely a very simple explanation to the poor play calling by the Fed. That is they took a bet to get inflation up from 1.7% to a 2% target, and they lost the cycle, because this is a route.



King Dollar the Undisputed Inflation Hedge Champion of the World, 2022

A potentially crowded trade setting up includes King Dollar, the undisputed inflation hedging champion of the current cycle.



We discuss why we think King Dollar grabbed Gold's belt, in "The 2022 Gold Conundrum Investment Bank Manipulation or Strong U.S. Dollar?, Summer Edition II", published July 18, 2022. Please contact us at info@baronpoint.com if you are interested in reading more on that subject.



A simple real-time hedging experiment with King Dollar is a lucky position I call my own life's happy circumstances. In terms of the USD as an inflation hedge, I can report, the trade has worked well!

I spend as much of my time as possible in Bangkok, Thailand. I have lived in six world cities throughout my business career, and this one is the best on Earth. However, we make our money in USD.

King Dollar and the USD to THB cross rate since May 2021 has kept inflationary costs in check here in the City of Angels with the cross rate adding +15.7% to purchasing power. This same cross has worked just about in every port of call made for our business, from the Middle East to Ho Chi Minh City!

It's good to be the King (Mel Brooks).





But Uncle Joe and Auntie Yellen, for the love of God, unemployment is a lagging indicator!

Interest rates have been discussed above, now let's turn our attention to the current recession, inflation, and employment in America.

As David Rosenberg of Rosenberg Research tweeted on September 22, 2022, "The die is cast. The Conference Board's LEI fell 0.3% in August and is down six months in a row at -5.3% SAAR. This has a 100% track record of predicting recessions back to 1959. Same pattern we saw from June-November '07. Recession started in January."

In trading we call this a **confirming indicator**. We already clocked a **second negative GDP number in 2Q2022**, and the GDP recession signal has now been confirmed by the **Conference Board LEI**. So, we agree with Mr. Rosenberg's tweet. We cannot deny it, or simply listen this recession away at a White House press briefing, **we embrace it**. Hey, kids, don't disturb Uncle and Auntie, let them enjoy their time on the La-Z-Boys, sooner or later they will wake up and agree we now have *both* inflation and a recession in America.

Look both ways before you cross the street, because the intersection of a recession, occurring with a bear market in stocks, is a particularly nasty intersection for bulls. I'm tryin' to walk a straight line. On sour mash and cheap wine (AC-DC). (Please contact us at info@baronpoint.com if you are interested in reading our extensive Bear Market Stock Market study 1800 — 2022).



Leading us to the strong labor markets sound bite monotony we have to hear, over and over, from the podium of policy makers. The current leadership in America tell us that labor markets are strong. However, people have to work harder, today, to pay bills in the real economy. How else does a family cover the increase in cost when inflation, if using 1980 methodologies as its measure, is +16% in America?

Hey Mon, what you mean you only have two jobs?

In the case of the bear market in bonds, some of the smarter credit analysts we follow indicate that the bond crash we have experienced this year, likely means that credit spreads could expand more before we see lows in the stock market. We too tend to agree with this thesis.



Despite stocks showing some relative price strength in their price pattern to investment-grade bonds, we agree that with this level of bond cabin depressurization, now putting pressure across asset classes, it means it is time to **wear the mask!**



Which leads us to a seemingly missed season of the facts of life. Did all the PhDs at the Fed possibly forget to pay attention during the entire 1929 Stock Market Crash and the Great Depression PBS channel series? Does nobody have the courage to stand up and reveal that data to the American people? Is everybody at the working level just keeping their mouth shut and falling in line, so they keep their job? Is Congresswoman Rashida Tlaib for real when debating in an uneven match against Jamie Dimon and then calling for a bank run on checking accounts at JP Morgan Chase when she lost her way on her teleprompter?

Come on now people, sing it with us, “Rock the boat, don’t rock the boat baby, tip the boat, don’t tip the boat over.”

How did a similar fact pattern play its way out to a conclusion?



To consider, I had to walk down the street and visit our Uncle Trader Vic this week. He gave me some startling information. August 1929, before the October stock market crash, the unemployment rate was practically at ZERO percent. To be specific, according to NBER, it was 0.04%. August 1929 is the month the NBER classified as the top of the economic cycle looking back before the Great Depression.

The Fed raised rates in the lead up to the crash, and then found it a good idea to again raise them in December 1929, after the market broke. By June 1930, or 10 months later, the unemployment rate was about the same as today in the U.S., or 3.77%. However, by December 1930, one year after raising rates, unemployment jumped to 11.89%.



Finances Now on a Sound Basis

A year later in 1932 unemployment climbed to 19.1%, and at its peak, unemployment ballooned to 23%.

But Uncle Vic, the stock market crashed in October 1929, they kept raising rates and then there was more bad policy making to come?

The record player thunders, Kick 'em when they're down. Kick 'em when they're up (Don Henley). So, I guess smart money, let's call him the Composite Operator, still moves before the government bureaucrats and the big media talking heads get the memo.

I am so relieved. Markets still seem to be a discounting mechanism, and now they are quickly doing the responsible work, so **follow the trend until the end when it bends!**

Wait, but it is true, the great American policy blunder of the 1930s got better and even more outrageous.

During the great stock market and economic unwind, after the 1929 crash, the White House thought raising taxes was sound advice to support the economy. So, The Revenue Act of 1932 was signed into law. Eat the rich (Krokus) as they raised U.S. tax rates across the board at the same time unemployment was accelerating. The rate on top incomes went up from 25 percent to 63 percent, and the policy makers branded the tax hike that year to be on a "Sound Basis".

Let's play some My Antidote (Slash ft. Myles Kennedy & the Conspirators). I guess I've been defined by my condition. I guess I've been defined by what they want. When paradise becomes your own petition. All there's left to find is a lost cause. But in the end I've only got myself to blame. I was only in the game. For the reasons that were wrong.

Tune sounds too familiar to us.





Toto, We're Not in Kansas Anymore



Its inflation caused by the Putin price hike, the COVID virus, you see help is here, raid the strategic petroleum reserve and lower gas prices until the mid-term elections are over, or maybe not because fewer can afford the commute. ABC, the closing line of lines this time around, it's such a classic and said with a straight face, "There Was 'Zero Inflation' in July, zero!" Lather, rinse, repeat, and let's fix it by cheating off of Nigeria's National Bureau of Statistics playbook.

So, at this juncture, the Fed seems to have a fantasy and a brain trust of PhDs soldiering ahead, thinking they know better and can cure inflation quickly by hiking interest rates at record rates of increase and driving the markets down while crushing the American people at the grocery store. So, let's play Ronald Reagan's famous line, about being from the government, and I am here to help! While the Fed shall fix this cycle's problems with some Sledgehammer Rock (Raven). As Bill Zox, portfolio manager at Brandywine Global, put it last week, "**75 is the new 25 until something breaks**".

They are busting the place up, as we said earlier, with M2 expansion the greatest on record, and not limiting money supply growth to 4 - 5% yearly. Why? In this cycle, they told us earlier in this piece, spending is not important anymore. Excuse me, that is a mis-quote, "**It (M2) is something we have to unlearn I guess**". This is what they said from the podium to the American people.

I think a Yale economist, turned market timer, coined the phrase "permanently high plateau" nine days before the crash in 1929. This time, they seem to be cheering from the bleachers for medium and longer-term interest rates to go up while housing prices fall, and people work several jobs to buy groceries and books for their kid's school. All because we better unlearn what we already know? Once in a Lifetime its, same as it ever was (Talking Heads).

This is a key policy difference between the current situation and another series of great American blunders that ran during the lead up to the Great Recession of 2008-09. However, during that installment of George W's creative destruction of U.S. housing, in the first round of Quantitative Easing ("QE") and the big spending bills such as the TARP, the Fed had the sense to keep the banks, what was left of them at the time, from lending aggressively, in part by raising capital standards. As a result of this policy implementation, inflation remained under control, despite enormous liquidity being pumped into the system. You know what? These current people look like me trying to do the moon walk.

You see fiscal prudence at this juncture would restrict government spending. This would put the current government spendaholics in a tight box and it may make AOC very, very pouty. So, they whisper, like Mom used to do when she needed to send a



confidential message to Dad across the couch. Notice in this cycle the Fed does not mention “money supply” loudly? They only indirectly talk about “letting their balance sheet decline as its securities mature”. Mom, I heard you, and yes the markets are raising their voice at us!

However, Uncle Vic had more to explain. When Bonds, Notes, and Bills mature, the U.S. Treasury simply replaces these funds by re-selling them to the banks. In turn, the banks print the fiat currency to buy them and put the bonds the Fed sold them into a Hold Maturity Account supported by Fed regulation, and there you go, **it's a beautiful Wall Street arbitrage!**

It reads like a dirty magazine hidden in the sock drawer, and there it is, we found Dad's Playboys. The moral of the story? The money supply does not shrink, and the government maintains its ability to spend without the worry of having to attract another sovereign like China or Japan to buy extra bonds, or better yet, the government does not need to go tell Mom, directly, that the government is raising taxes in a very public legislative battle. Uncle Vic's magazine, Smells of Teen Spirits (Nirvana).

So, as Alexis de Tocqueville stated, in one of the most influential books of the 19th century (1835), Democracy in America, **“The American Republic will endure until the day Congress discovers that it can bribe the public with the public's money.”**

Is it just us thinking this way when reading our forefather's works, or were humans just way smarter and more in touch with the nature of humanity, before TV and now, social media?

Are they sending our best and brightest to Washington D.C. these days?

In our humble opinion, Jerome Powell and Janet Yellen, are nowhere near as capable in the functions of global capital and debt markets as the U.S. Treasury and Fed were with Henry Paulson, Tim Geithner and Ben Bernanke, a person that spent his life studying the 1930s Depression. Say what you will, but these policy makers stood strong during the Great Recession. True, George W thought everybody should own a home sounded great, and Wall Street tried its best to accommodate and spike the punch at the Rock 'n' Roll High School (Ramonones) dance. Nonetheless, policy makers, on the whole, crossed the isle, made swift and decisive moves, and timed them well. Principal Paulson announcing weekend policy actions at the Japanese market open was classic, this was a guy who knew markets! These great Americans averted a Depression, full stop, and the fall out was derivatives traders on TV, cleaning their desks out at 383 Madison Avenue and hailing a black car with a box in their arms. Driver, take me to the Hamptons.



Seekin', Seek and Destroy

So, governments around the world, led by the U.S., never got off the QE juice, and like raw power in and of itself when it comes to an end, markets self-correct, and that is not pretty. Lesson learned, excess liquidity manifested in excess stock market returns, the bonanza trend lasted for a decade and a little more, but that is over for the indexes for now.

However, maybe the funny money helped Travie McCoy to become a billionaire? For some context, he wanted it so fcuking bad, but no more Fast Eddie Clark and the Easy Livin' (Fastway). The markets are Seekin', Seek and Destroy (Metallica). Creative destruction has taken hold as Schumpeter taught us, and this is what happens in a free-market capitalist system. As the market giveth, the market taketh out the stops.

Screaming for Vengeance

A few other classic periods of creative destruction as Rob Halford belts out his mighty scream with Judas Priest:



- Stick head in the sand during lead up to the Civil War, James Buchanan, Check.
- Tight money and raise taxes in a financial calamity, Herbert Hoover, Check.
- .com bubble and the world of valuations are driven by the eyeball matrix, Check.
- Everyone should own a home and the NINJA loan, Check.
- Equity valuations are suddenly divorced from GDP growth, and over perform the implied growth of the economy by 40% for a decade during the liquidity bonanza, Check and play it Eddie;
- Crypto shall be the new reserve currency of the world, Check.



And the Cradle Will Rock...



So, the bond vigilantes (RIP Marty Zweig) are back in their nice wing tipped shoes and pin stripe suits, and they are taking a baseball bat to it like Shelley Duvall when Jack Nicholson was playing the role of bond market yields in *The Shining*.

You see, the market has a responsibility, and that is to work out the overstayed excess liquidity of the last decade, while it steamrolls the overly tight Fed policy position. Bond yields lead a repricing of assets, as geo-political uncertain increases and economies digest the pandemic overreaction. As one astute colleague pointed out to me last night on WhatsApp, "will people even want stocks if the two-year or the ten-year goes and stays at 6% and Municipals bonds are at 5%, tax-free?" They sure didn't for long holding periods in the 1970s, and that resulted in a big, loud, wall of Marshal amplifiers trading range. What a fun decade for the indexing crew!

Ladies and gentlemen Mr. Jeremy Siegel on the drums, "The last two years [are] one of the biggest policy mistakes in the 110-year history of the Fed, by staying so easy when everything was booming," said the professor of finance at the Wharton School of the University of Pennsylvania, September 23, 2022, on CNBC.

Furthermore, Mr. Siegel explained, "When we have all commodities going up at rapid rates, Chairman Powell and the Fed said: 'we don't see any inflation. We see no need to raise interest rates in 2022.' Now when all those very same commodities and asset prices are going down, he says: 'Stubborn inflation that requires the Fed to stay tight all the way through 2023.' It makes absolutely no sense to me whatsoever, way too tight!"

Quick fact, when the song "And the Cradle Will Rock" starts that is not King Edward on the guitar! He starts with a flanger-effected Wurlitzer electric piano...and then later on, Dave tells us how it is, At an early age he hits the street, and winds up tired with who he meets. **An' he's unemployed.** His folks are overjoyed (Van Halen).



But wait how does it end, and didn't we see this movie before?

Maybe, but do you see the cartoon from September 2008 to the right? Do you remember? Damn, I miss Michael Jackson!

No, sorry, what I mean is do you remember the episode where they were putting the three fires out, and the banks were in deep trouble — i.e., kids, go look up the CDS levels of Goldman Sachs and Morgan Stanley on the fateful Merrill Lynch gets bought by BofA, and the



sacrificing of Lehman Brothers weekend, September 14, 2008. They were finished, all of them! Man, it was a real cliff hanger, but the regulators won, they all became commercial banks. This was after the first Bear Stearns season ending thriller, when a Wall Street legend collapses and JP Morgan swoops in to become a leader in the prime brokerage space, overnight, for \$1! Also, merged into a commercial bank under the regulators' thumb.

Ok, Mark Twain comes to mind, as all of us on Wall Street heard from a boss or nice-dressed analyst passing out doughnuts in the conference room, "**History Doesn't Repeat Itself, but It Often Rhymes**"!



Well, let me roll up on to the sidewalk and take a look, yes



As we wrote earlier, the problem we face in America is not an economic issue, yet, and we see strength in the balance sheets of American big banks. They are stronger and far more capitalized than in 2008 to handle the beating the bond market is taking. Also, they have the governments blessing because now they are all too big to fail, and pension funds are now going to squeal.

Eventually, we think the Fed may be inclined to taper, or if it goes too far, force a flood of liquidity onto the markets. This may take a slip, hook, and instantaneous Iron Mike Tyson punch to the temple, but through more bank cajolery and bond buying smelling salts, call it a Buy Extra Bonds from Suits — Duchess of Sussex meets The Grifters team, we should be in good hands with a bottom in place, eventually.

Think of it as a real wreck the world, save the world type moment, no, the Yankee Rose shot heard 'round the world! (David Lee Roth)

So then, off the canvas and to our stool in the corner, with a Wall Street salute, package the paper up and Reel 2 Real move it, move it.

It may take more time to work its way out, and remember, equity markets can and have gone sideways for a decade at a time when reconciling. Indexers take note, you could be the Last in Line (Dio), because 14% a year S&P 500 compounding and trees growing to the sky is not the new normal. It was a wet teenager's dream, but it's over, and maybe active and tactical money management and stock selection is coming back into vogue along with bell bottoms and inflation. Good music, lots of hair, bull runs up, bear sell-offs down, you know the active trading stuff pensions love, and parents hate. So, thanks Mr. Dombrowski, wherever you are, because we learned to study and love our history, and you taught us to do it fast and quick, then hand the paper in for a grade and go have some fun with Fall '86 at the ATO house.

Stay tune, now, it's going to be a must-see TV. We all may look a little older, but this seems to us, a little like Top Gun Maverick. Yes, we already saw the movie once, but there you go, we liked it the second time as well!

Que Metallica.

Adrenaline starts to flow.

You're thrashing all around.

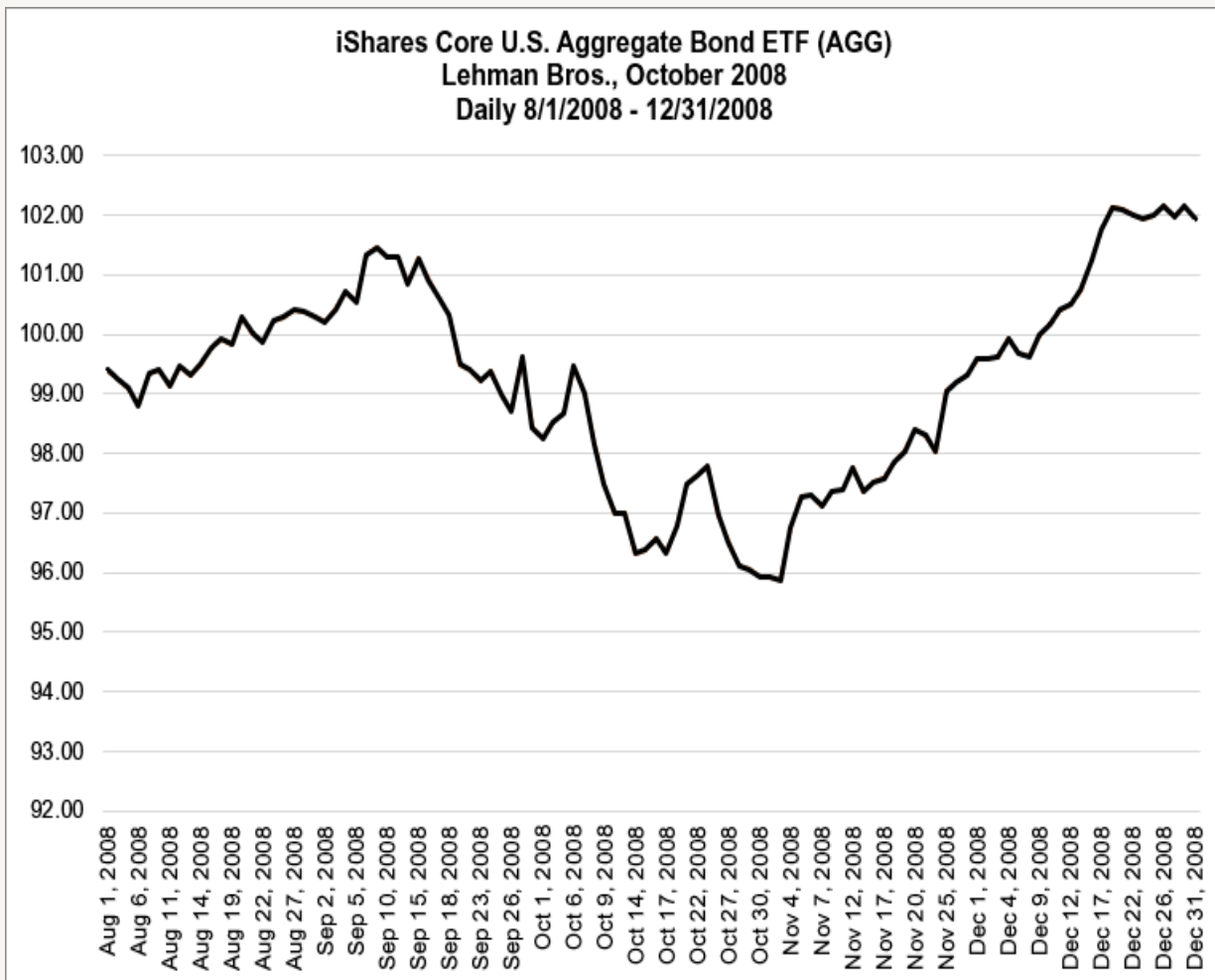
Acting like a maniac.

Whiplash!

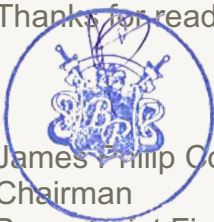


Sneak Preview: Where do we go now, Sweet Child of Mine.

Well, if the Fed stays the course, and keeps forcing rates up, too far too fast, it's going to be more trouble, and Bond V coming soon to a theatre near you!



Thanks for reading,



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If you would like to discuss anything in this paper or any other topic, email us at info@baronpoint.com or call +1 212 248 2733.