GORDON T LONG

NOTE

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WAS:

RATES = INFLATION + RISK

TODAY:

RATES = INFLATION + RISK

AGENDA

May 21st 2025

RATES: RISK v INFLATION

TERM PREMIUMS v EQUITY RISK PREMIUMS

- THE INFLATION DRIVER
- THE CREDIT RISK DRIVER

HISTORY OF LONG TERM YIELDS

- LESSONS FROM HISTORY

WHO OWNS US DEBT

- FUNDING TIED TO THE DOLLAR

A BREWING STORM

- THE DE-DOLLARIZATION PROBLEM

SLOWING RESERVE GROWTH

- RATE OF CREDIT GROWTH & A LACK OF UNENCUMBERED COLLATERAL
- A SLOWING WEALTH EFFECT IS ALL IT WILL TAKE!

CONCLUSIONS

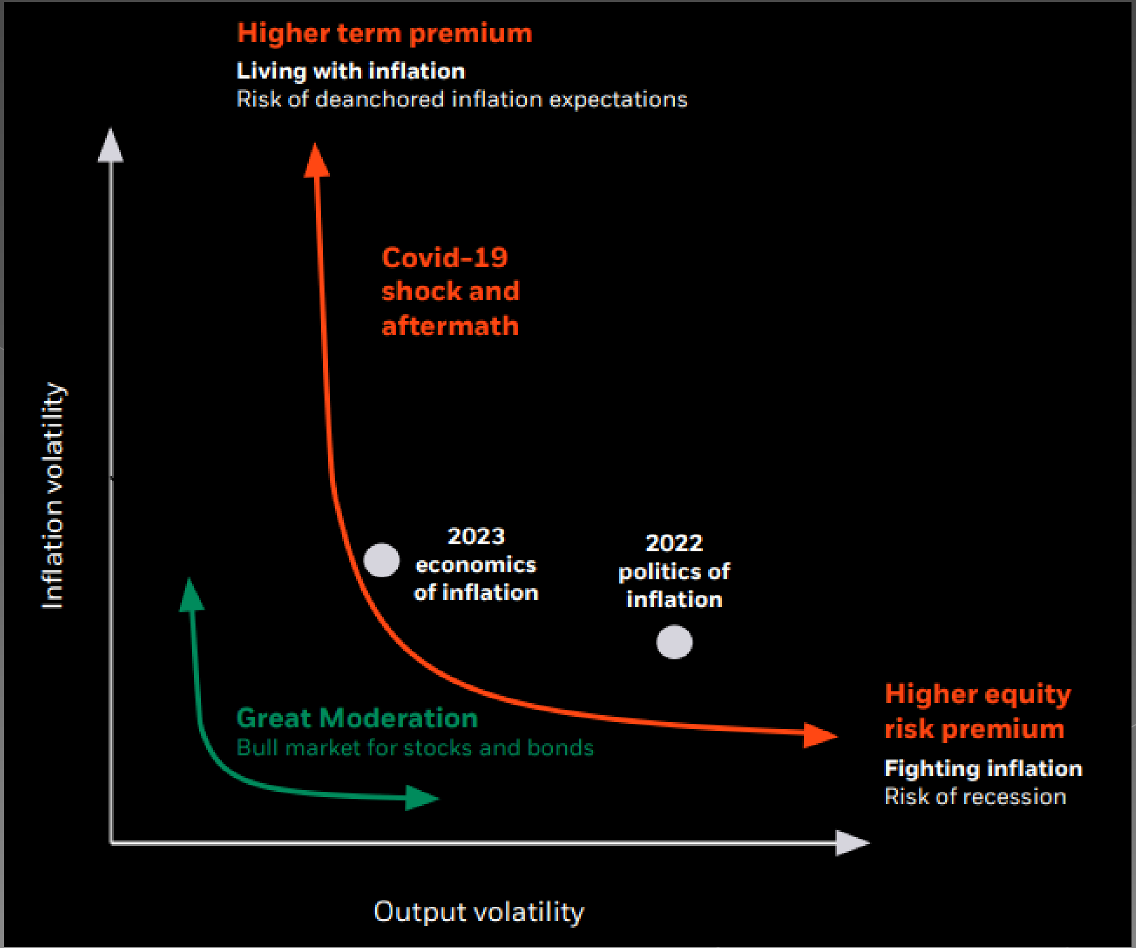
- EXPECT A US$ CURRENCY DEVALUATION BEFORE TRUMP'S TERM EXPIRES

THE INFLATION DRIVER

BONDS
Higher Term Premiums

EQUITIES*
Higher Equity Risk Premium

*HAVE BEEN SHELTERED BY EARNINGS GROWTH

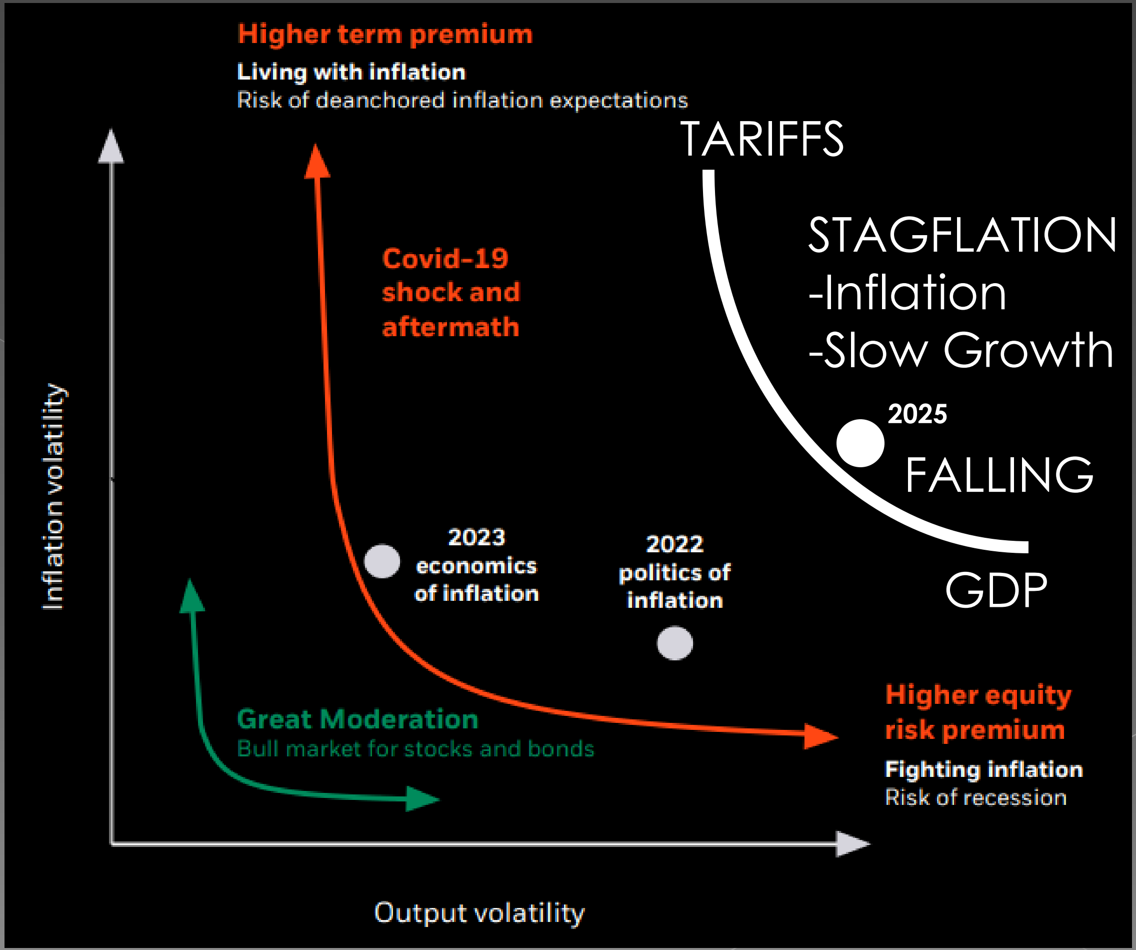


INFLATION BREAKEVENS

STAGFLATION DRIVER

BONDS
Higher Term Premiums

EQUITIES
Higher Equity Risk Premium



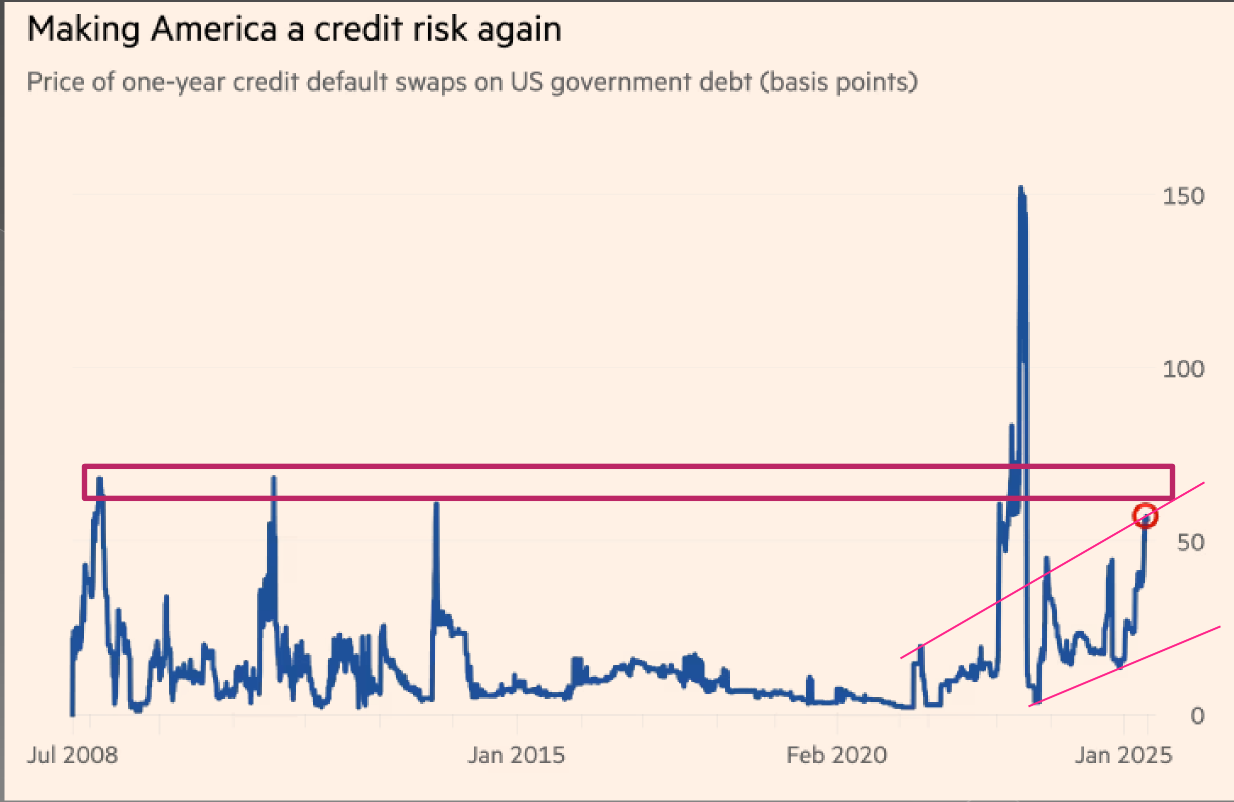
FISHER'S EQUATION

NOMINAL YIELD = INFLATION BREAKEVEN + REAL RATE

REAL RATE = NOMINAL YIELD – INFLATION BREAKEVEN

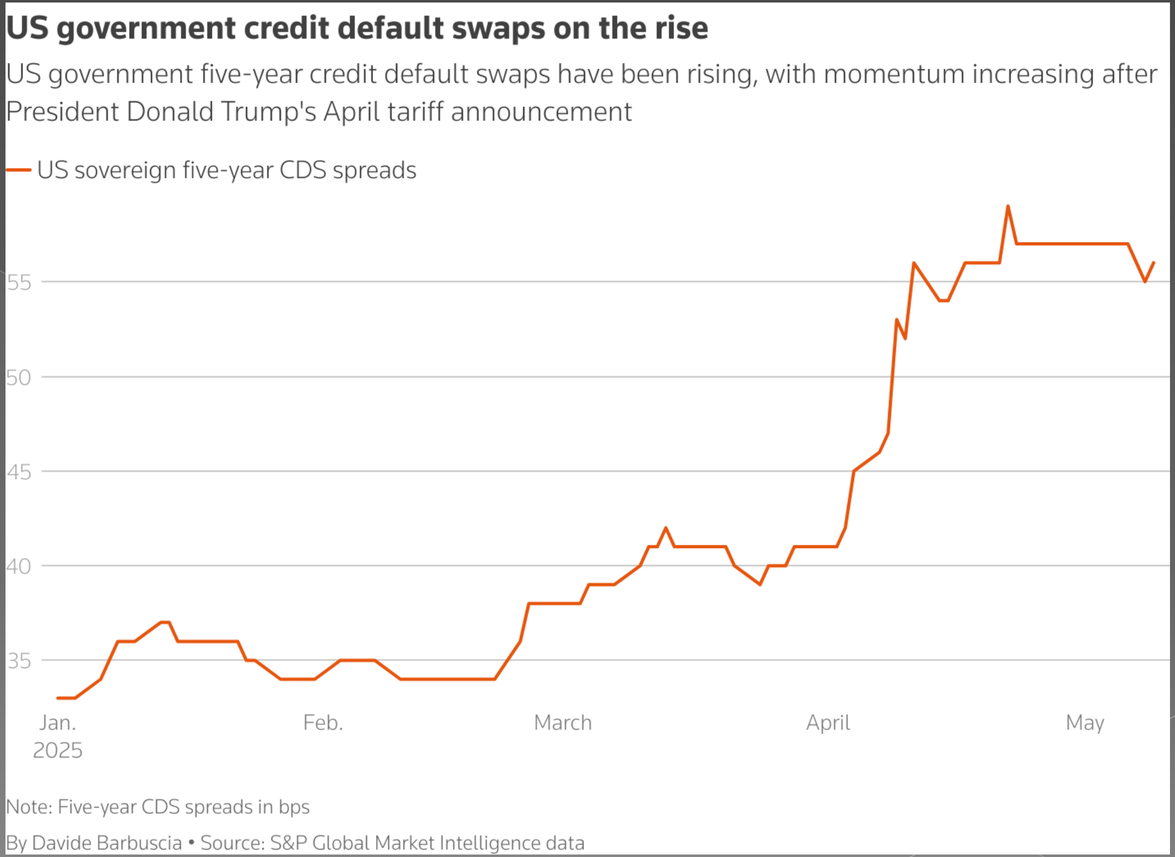
THE CREDIT RISK DRIVER

1 YEAR UST CDS



THE CREDIT RISK DRIVER

5 YEAR UST CDS



US Sovereign Credit Default Swaps are not buying any of this Wall Street nonsense.

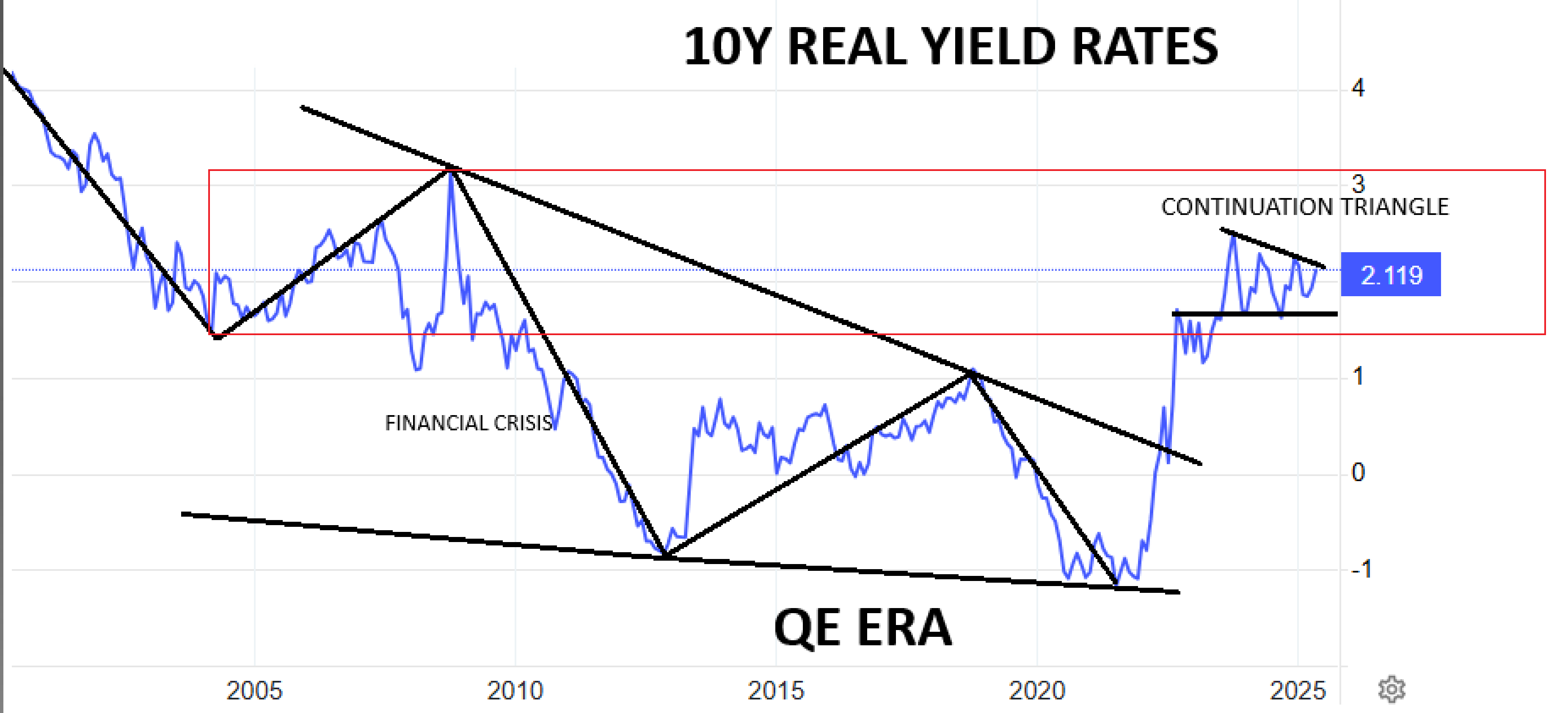
Meanwhile few paid any attention to **Moody downgrading the US Credit Rating to Aa1 from Aaa.**

This doesn't happen in a new Bull Market, but not unexpected in the early stages of a Bear Market!

Moody's Downgrades USA Credit Rating From Aaa

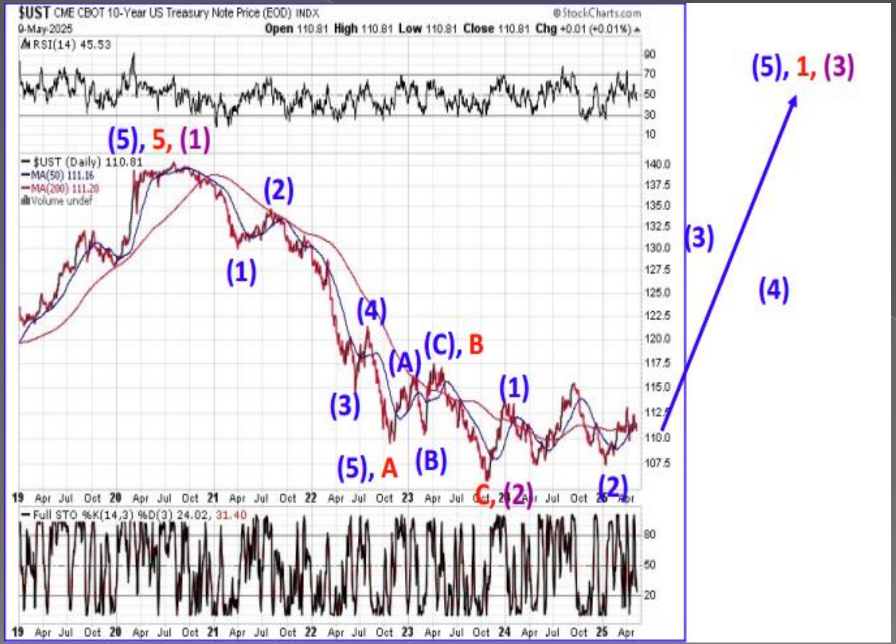
Successive US administrations and Congress have ***failed to agree on measures to reverse the trend of large annual fiscal deficits*** *and growing interest costs...*

SAT MAY 17, AT 11:00 AM



10Y REAL YIELD RATES
CONTINUATION TRIANGLE
2.119
FINANCIAL CRISIS
QE ERA
4
3
1
0
-1
2005
2010
2015
2020
2025

Since 2010, Billions USD
DERIVATIVES / INCOME AUM
Billions USD
250
200
150
100
+163B$
2010
2015
2020
2025


$UST CME CBOT 10-Year US Treasury Note Price (EOD) INDX
@StockCharts.com
9-May-2025
Open 110.81 High 110.81 Low 110.81 Close 110.81 Chg +0.01 (+0.01%)
RSI(14) 45.53
$UST (Daily) 110.81
MA(50) 111.16
MA(200) 111.20
Volume undef
Full STO %K(14,3) %D(3) 24.02, 31.40
(5), 5, (1)
(2)
(1)
(4)
(3)
(5), A
(A)
(B)
(C), B
C, (2)
(1)
(2)
(3)
(4)
(5), 1, (3)


$UST CME CBOT 10-Year US Treasury Note Price (EOD) INDX
@StockCharts.com
27-Dec-2024
Open 108.58 High 108.66 Low 108.38 Close 108.38 Chg -0.59 (-0.54%)
U.S. 10 Year Treasury and two Converging Fan Patterns: Blue projected a bottom at 108ish, then Red projecting a Rally to 140ish.
$UST (Weekly) 108.38
MA(50) 110.98
MA(200) 117.87
Volume undef
There are two Converging Fan Trend-line patterns, one with 6 trend-lines (blue), the other with 7 trendlines (red) first pointing to a near term low around 108ish, (it actually bottomed at 106) and the second pointing to a rally in the 10 Year U.S. Treasury to the 140ish area within 3 years. That tells us long-term interest rates will soon start declining.

RELIABLE RECOGNITION PATTERNS

COMPUTER DRIVEN TRIGGER POINTS

TA ALGORITHMS

AGENDA

April 23rd, 2025

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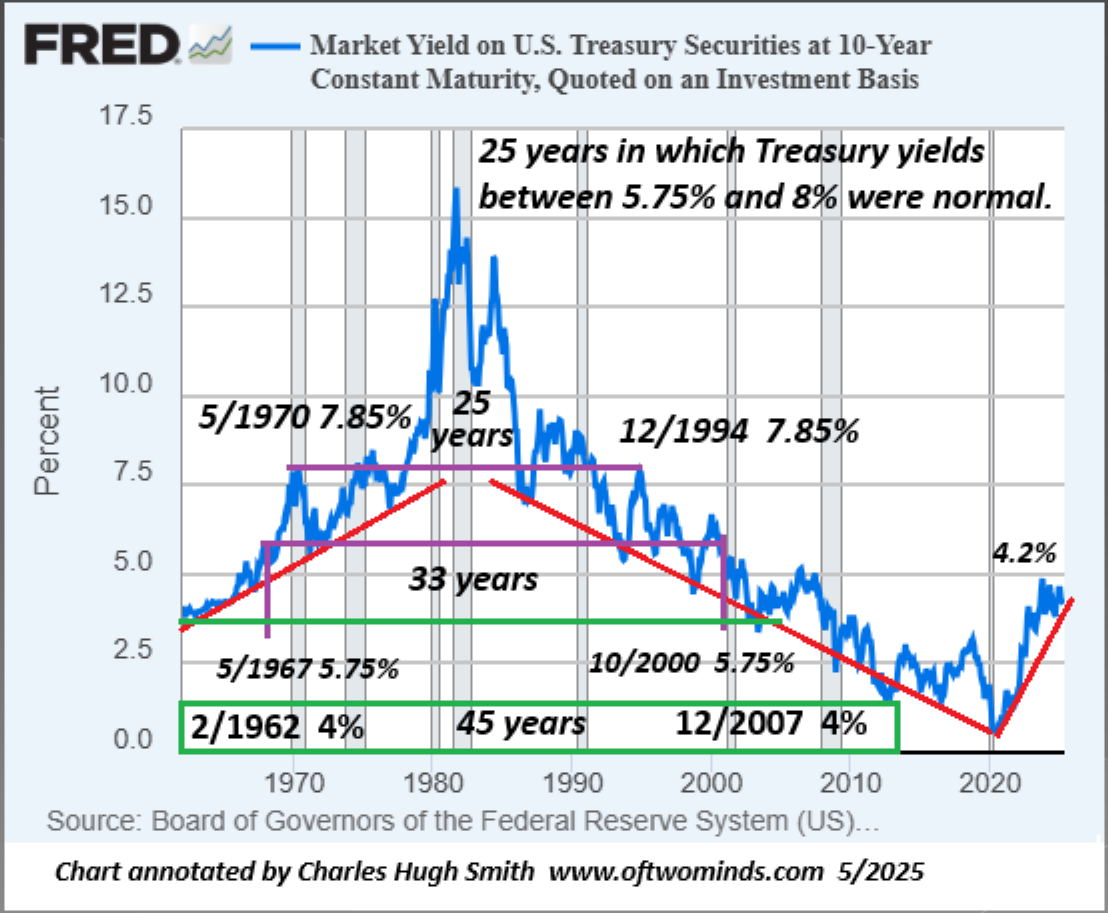

FRED
Market Yield on U.S. Treasury Securities at 10-Year Constant Maturity, Quoted on an Investment Basis
25 years in which Treasury yields between 5.75% and 8% were normal.
5/1970 7.85%
25 years
12/1994 7.85%
33 years
4.2%
5/1967 5.75%
10/2000 5.75%
2/1962 4%
45 years
12/2007 4%
Percent
17.5
15.0
12.5
10.0
7.5
5.0
2.5
0.0
1970
1980
1990
2000
2010
2020
Source: Board of Governors of the Federal Reserve System (US)...
Chart annotated by Charles Hugh Smith www.oftwominds.com 5/2025

The reason US Government Debt is important, because:

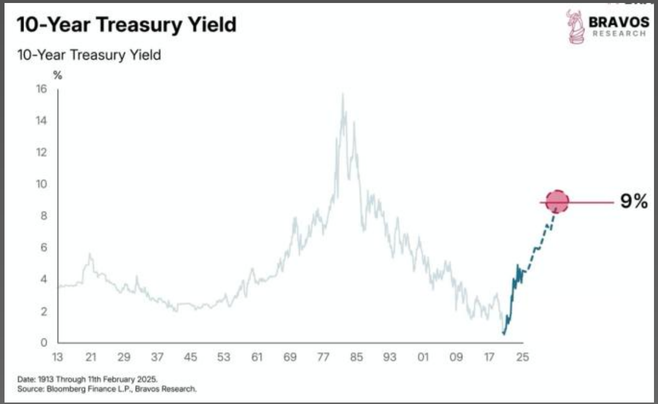
The U.S. Taxes GDP to service its debt.

- A high debt-to-GDP ratio raises concerns about sustainability.
- If investors doubt U.S. Treasuries' safety, they'll demand higher yields, pushing rates even higher.

This isn't just a theoretical concern…

- Studies show every 1% rise in debt-to-GDP increases bond yields by 4 basis points.
- So with today’s debt-to-GDP ratio level, it suggests that yields could be 400 basis points (or 4%) higher than they were back then.

If we apply that to today’s bond market, we could be looking at 10-year yields rising to 9%, without inflation even needing to move higher.
That alone could create extreme economic and market volatility.



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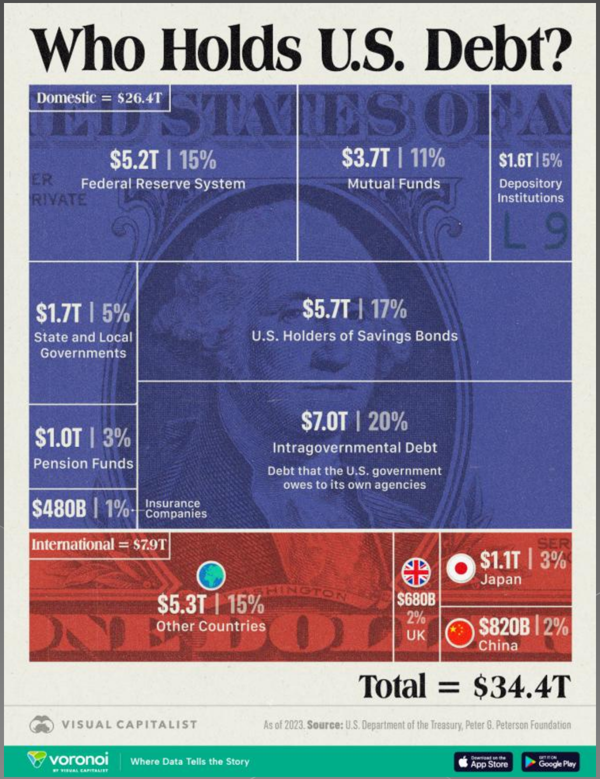
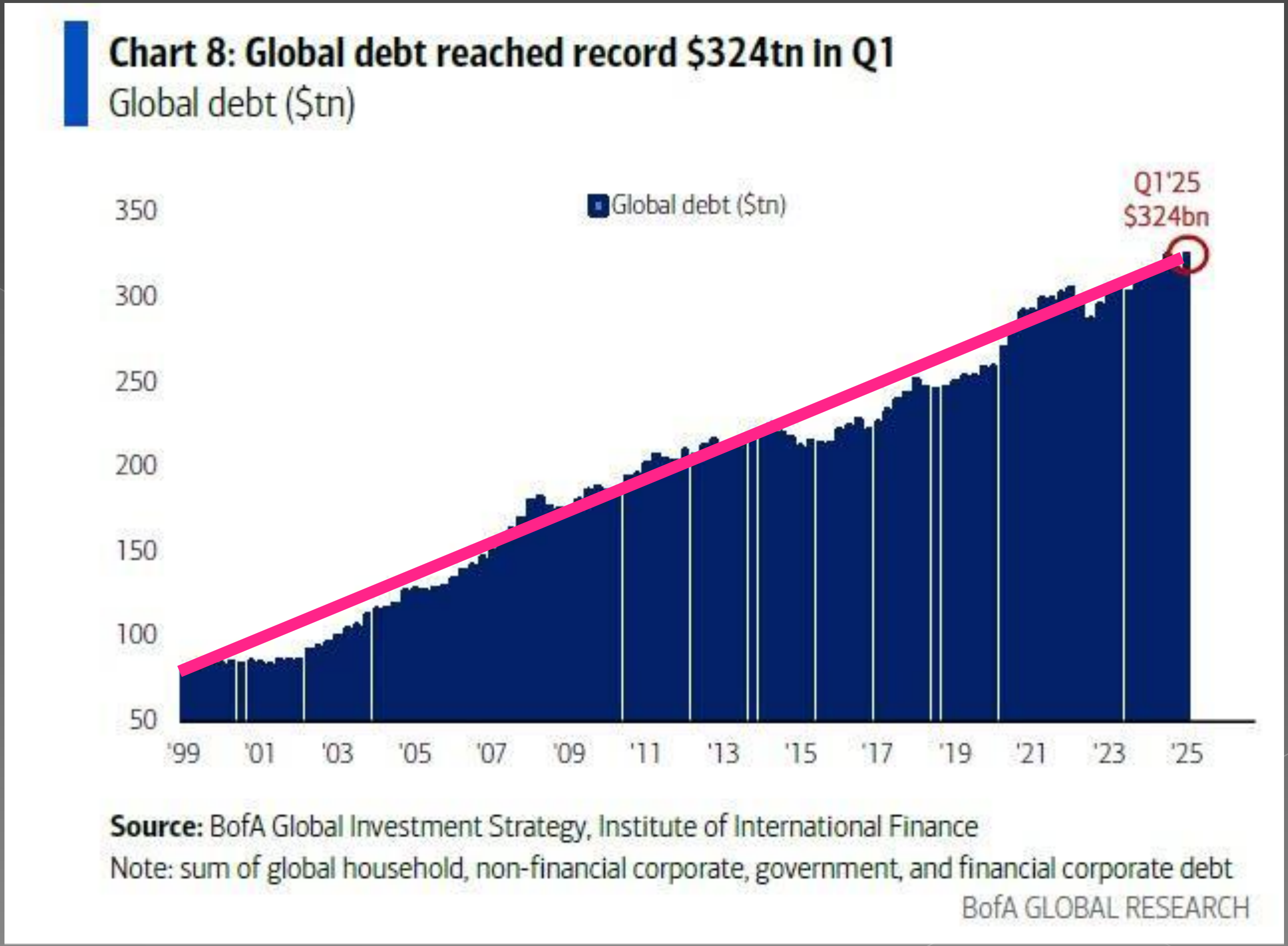
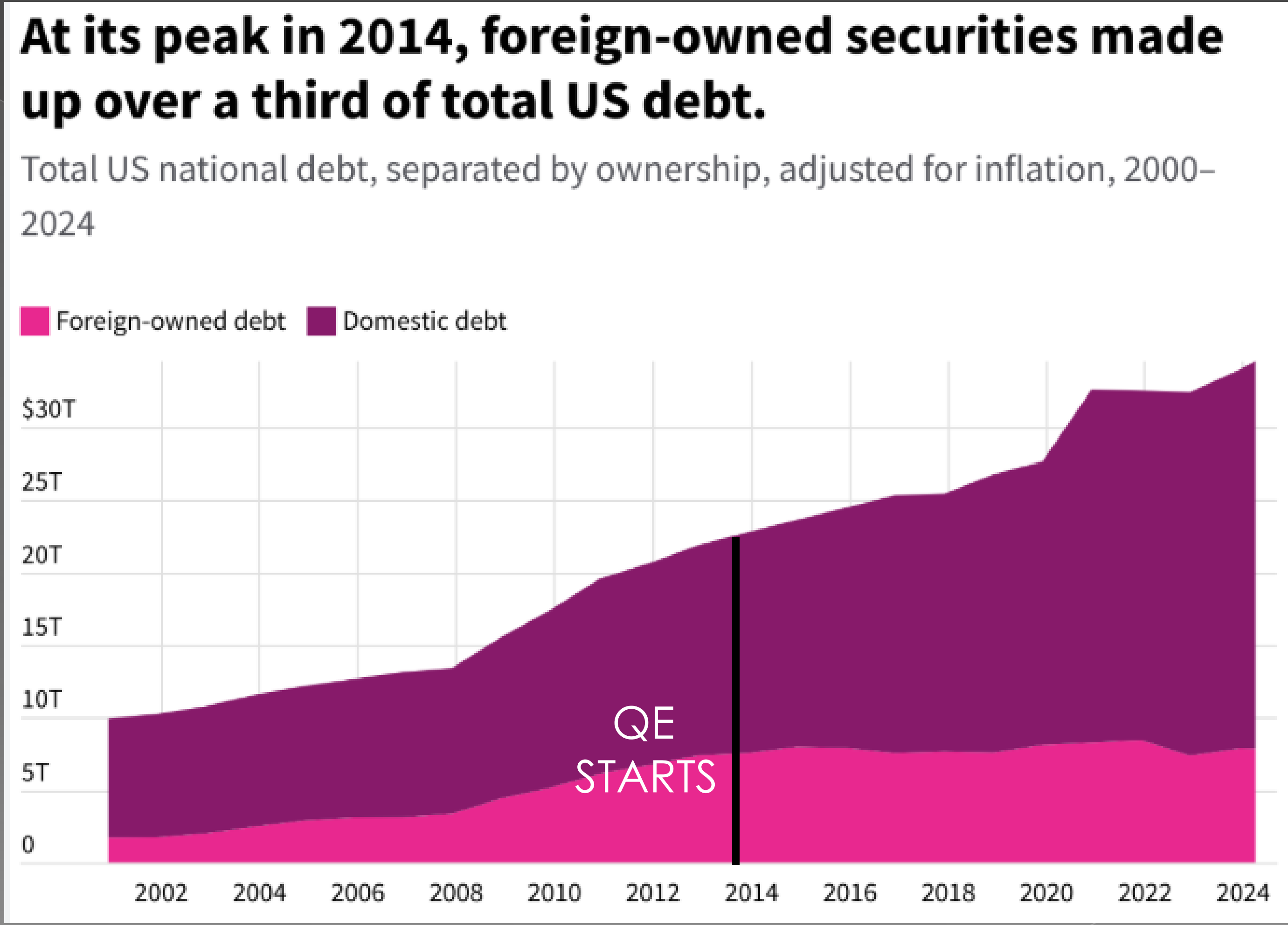


Q1 Global Debt levels hit all-time high $324T,

It's only a matter of time before we get a buyers strike!



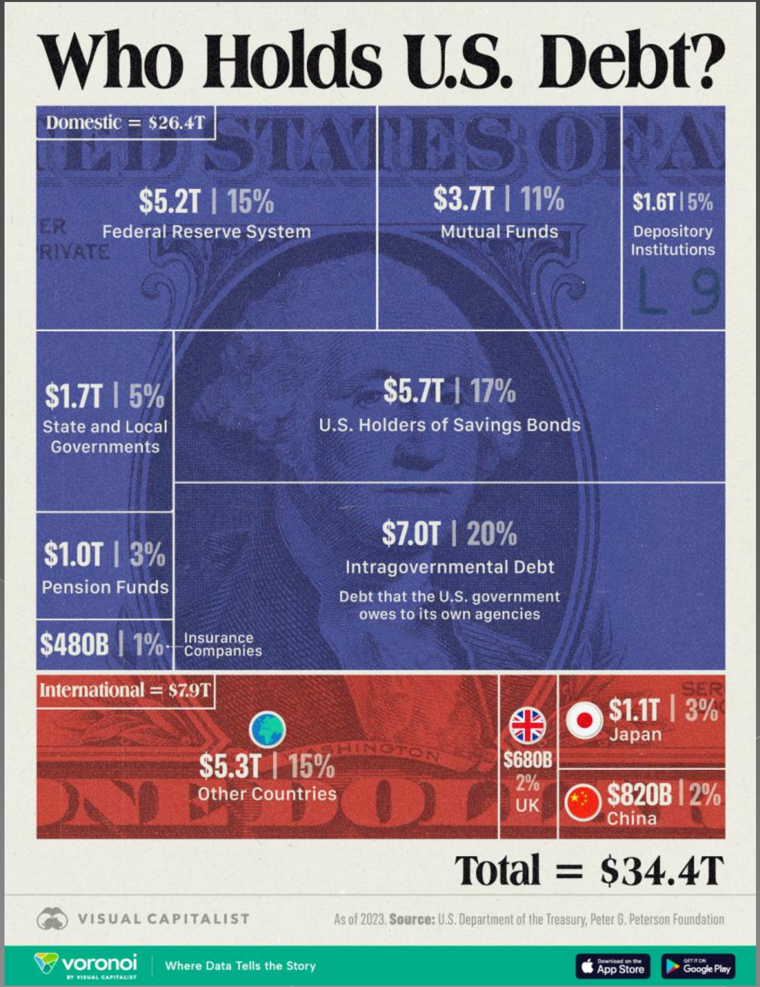

At its peak in 2014, foreign-owned securities made up over a third of total US debt.
Total US national debt, separated by ownership, adjusted for inflation, 2000–2024
Foreign-owned debt
Domestic debt
$30T
25T
20T
15T
10T
5T
0
2002
2004
2006
2008
2010
2012
2014
2016
2018
2020
2022
2024
QE
STARTS

USD/JPY has tracked the 10y UST yield closely

Source: Soc Gen FX

Bernanke:
Printed $2–3 trillion in three or four years.

Powell:
$5 Trillion in 18 months.



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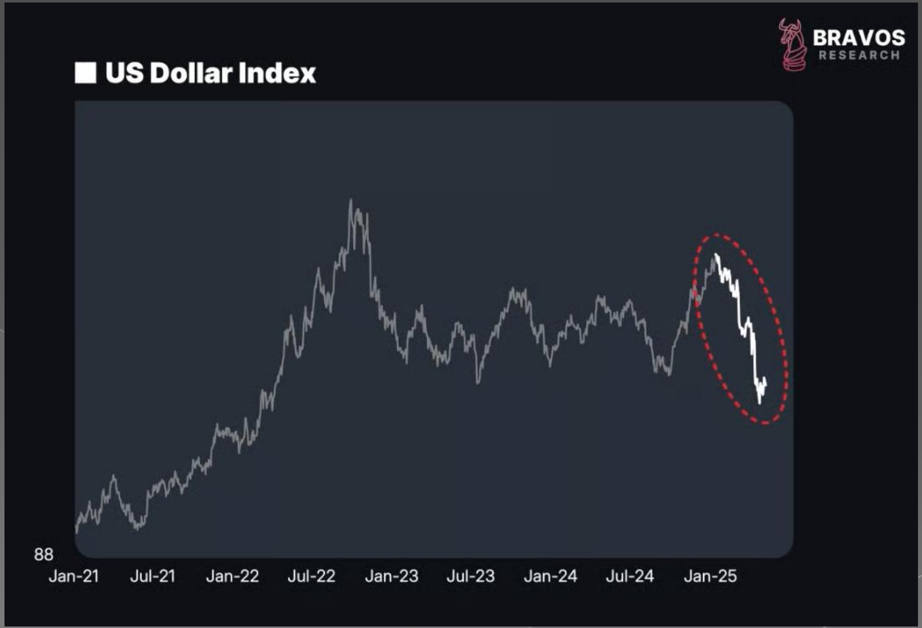
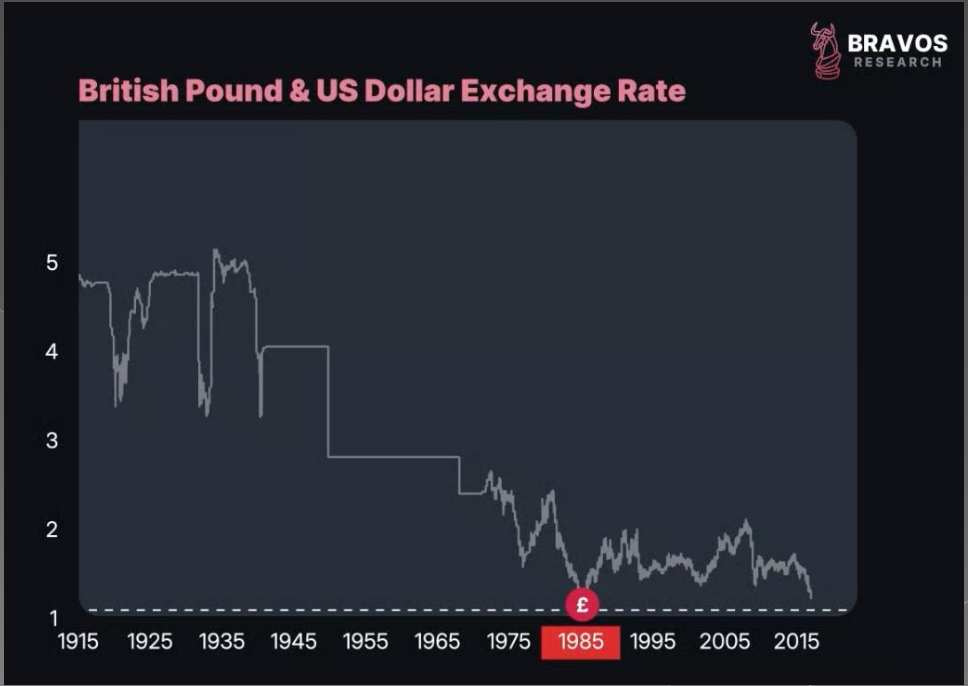
The US dollar index has witnessed its largest drop since COVID-19. It has now completely disconnected from its underlying fundamentals. This development could have massive implications for the economy and financial markets.

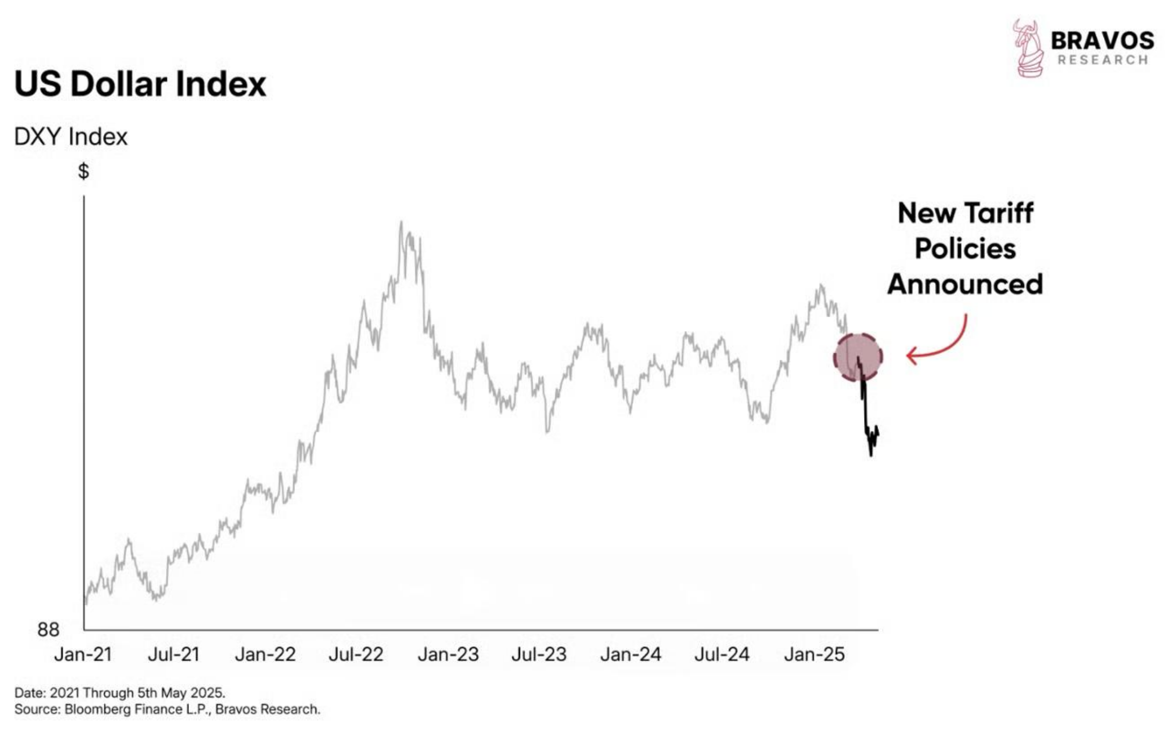


BRITISH POUND

In the 1940s, 1 British pound could be exchanged for 5 US dollars. It was the dominant global currency at the time. By the 1980s, the British pound was only worth 1 dollar, completely destroying the purchasing power of anybody holding pounds. This reshaped global trade, economic power and geopolitics.

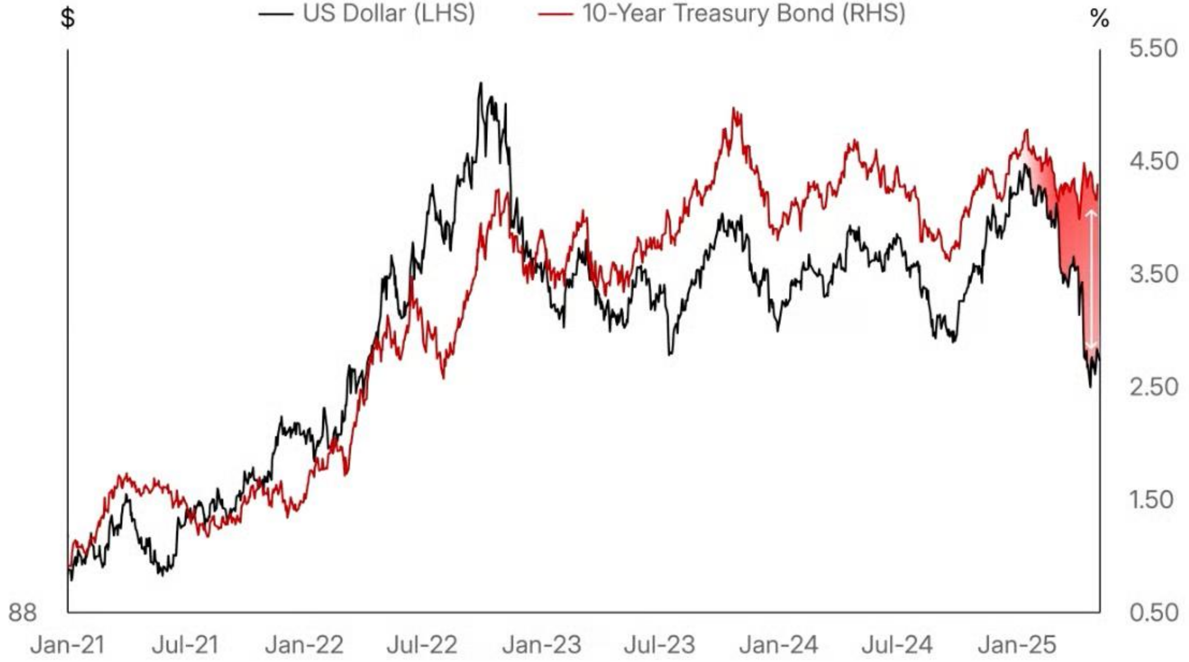


The US dollar index (DXY) has faced strong selling pressure since Trump's tariff policy announcement on April 2nd.



US Dollar Index and 10-Year Treasury Yield

DXY Index and 10-Year Treasury Bond Yield



Date: 2021 Through 5th May 2025.
Source: Bloomberg Finance L.P., Bravos Research.

UNDERSTANDING THE CAUSES

Before making definitive conclusions, we need to understand exactly why this gap has formed:

1. Tariffs Slow Economic Growth
   - Foreign exchange rates are heavily influenced by local economic growth.
   - If investors believe Trump's tariffs will slow growth in the US, it makes sense the dollar would weaken.
   - This could be temporary though, as the US economy remains strong and leads in key future industries.

2. Reduced Global Trade Volume
   - Trump's tariff policies will reduce global trade volume.
   - Since most global trade is conducted in US dollars, tariffs naturally reduce demand for dollars.
   - If we're heading into a world of declining global trade, that could put the dollar on a sustained weakening path.

UNDERSTANDING THE CAUSES

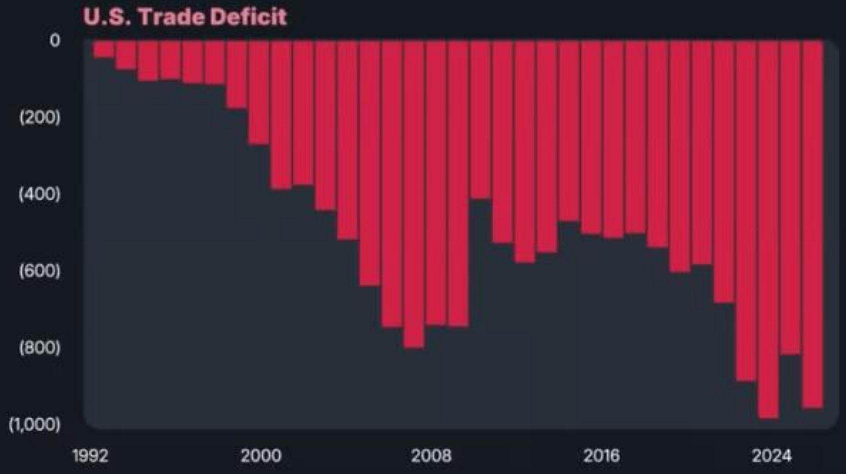
3. Deliberate Currency Weakening Policy

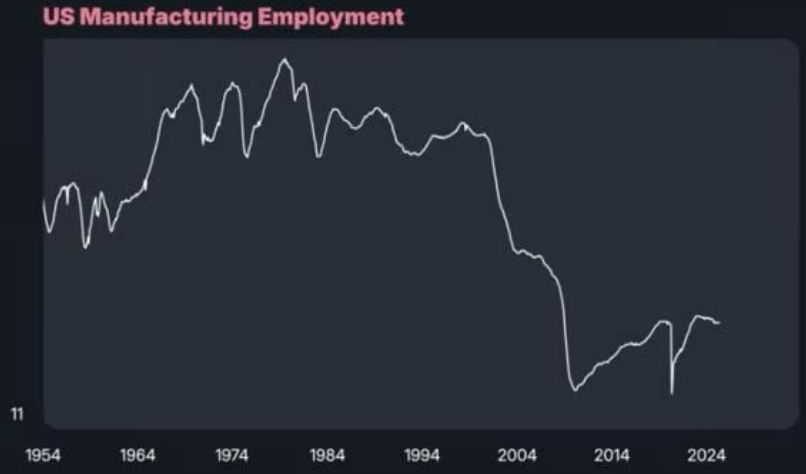
- Most concerning is the possibility that the current administration is deliberately seeking to weaken the dollar as part of its economic strategy.
- Trump has frequently expressed wanting a weaker dollar.
- A weak dollar makes American-produced goods more competitive, boosts exports and stimulates the manufacturing sector.
- All of these outcomes aligns with Trump’s "Make American Industry Great Again" objectives.

That’s exactly what happened with the British pound in the 1940s…

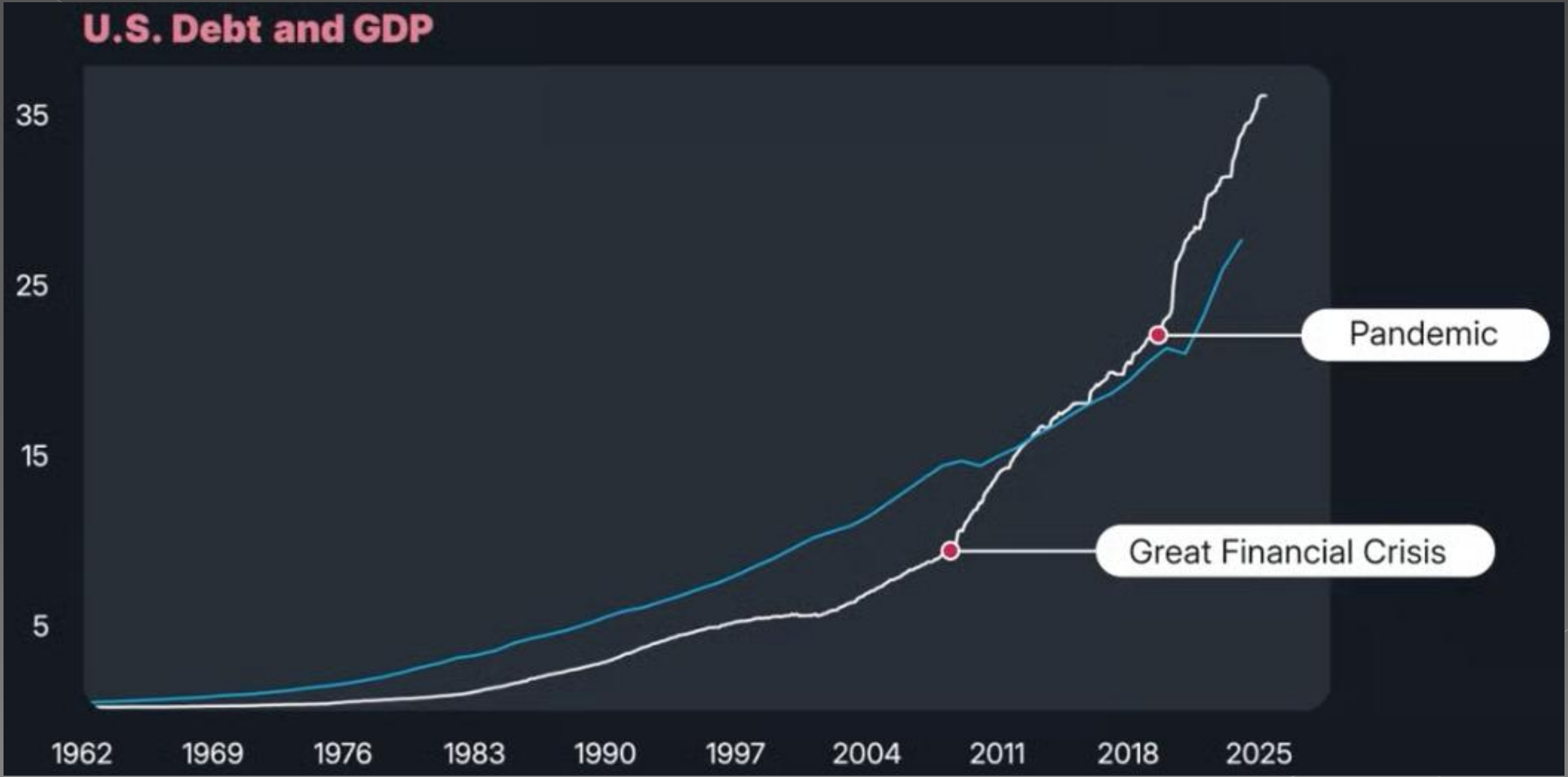
2 main factors drove the British pound's devaluation against the dollar.

- The British economy had a high trade deficit, meaning the UK wasn't manufacturing locally.
- Currency devaluation made British goods more competitive and stimulated the local economy.





BRAVOS
RESEARCH


U.S. Debt and GDP
35
25
15
5
1962
1969
1976
1983
1990
1997
2004
2011
2018
2025
Pandemic
Great Financial Crisis

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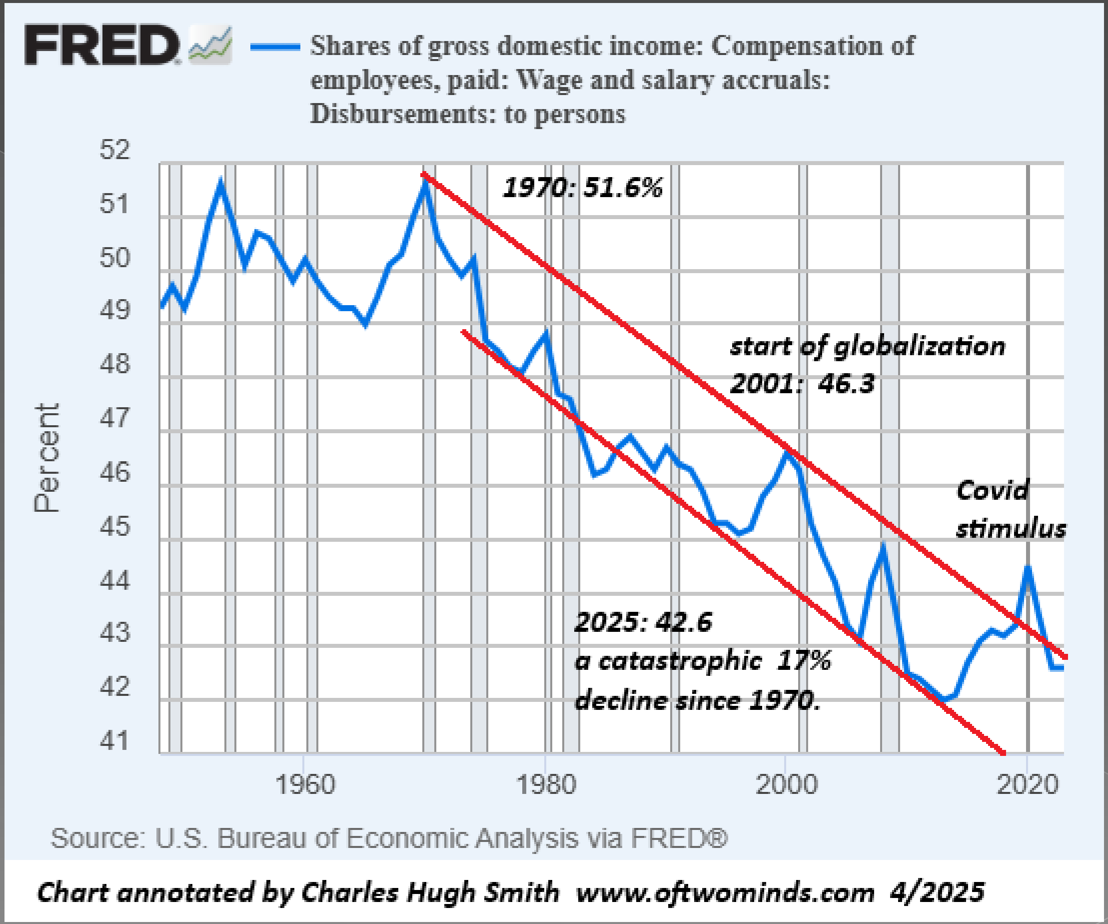
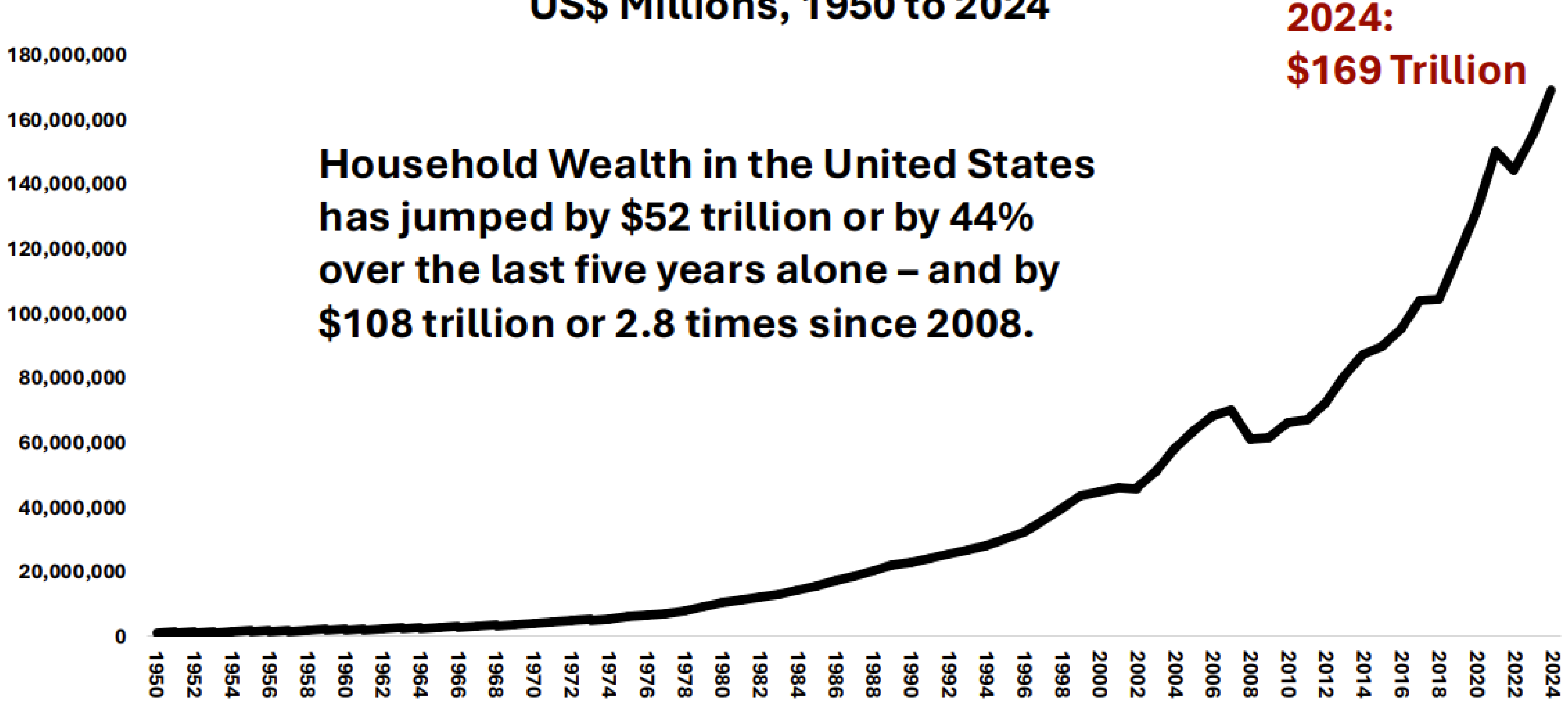
THE END OF THE TRIFFIN PARADOX

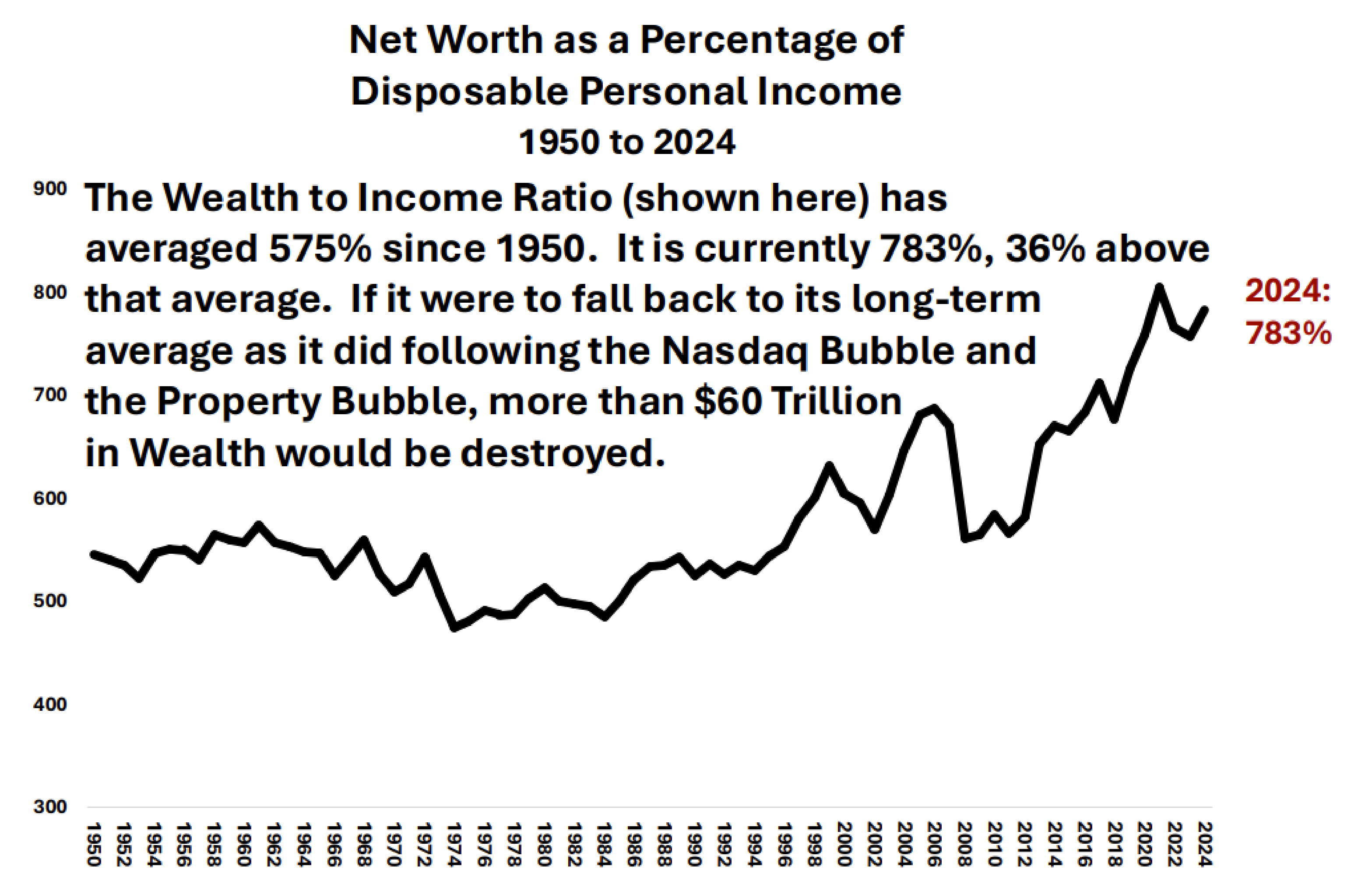

FRED
Shares of gross domestic income: Compensation of employees, paid: Wage and salary accruals: Disbursements: to persons
Percent
52
51
50
49
48
47
46
45
44
43
42
41
1960
1980
2000
2020
1970: 51.6%
start of globalization
2001: 46.3
Covid
stimulus
2025: 42.6
a catastrophic 17%
decline since 1970.
Source: U.S. Bureau of Economic Analysis via FRED®
Chart annotated by Charles Hugh Smith www.oftwominds.com 4/2025

Household Net Worth

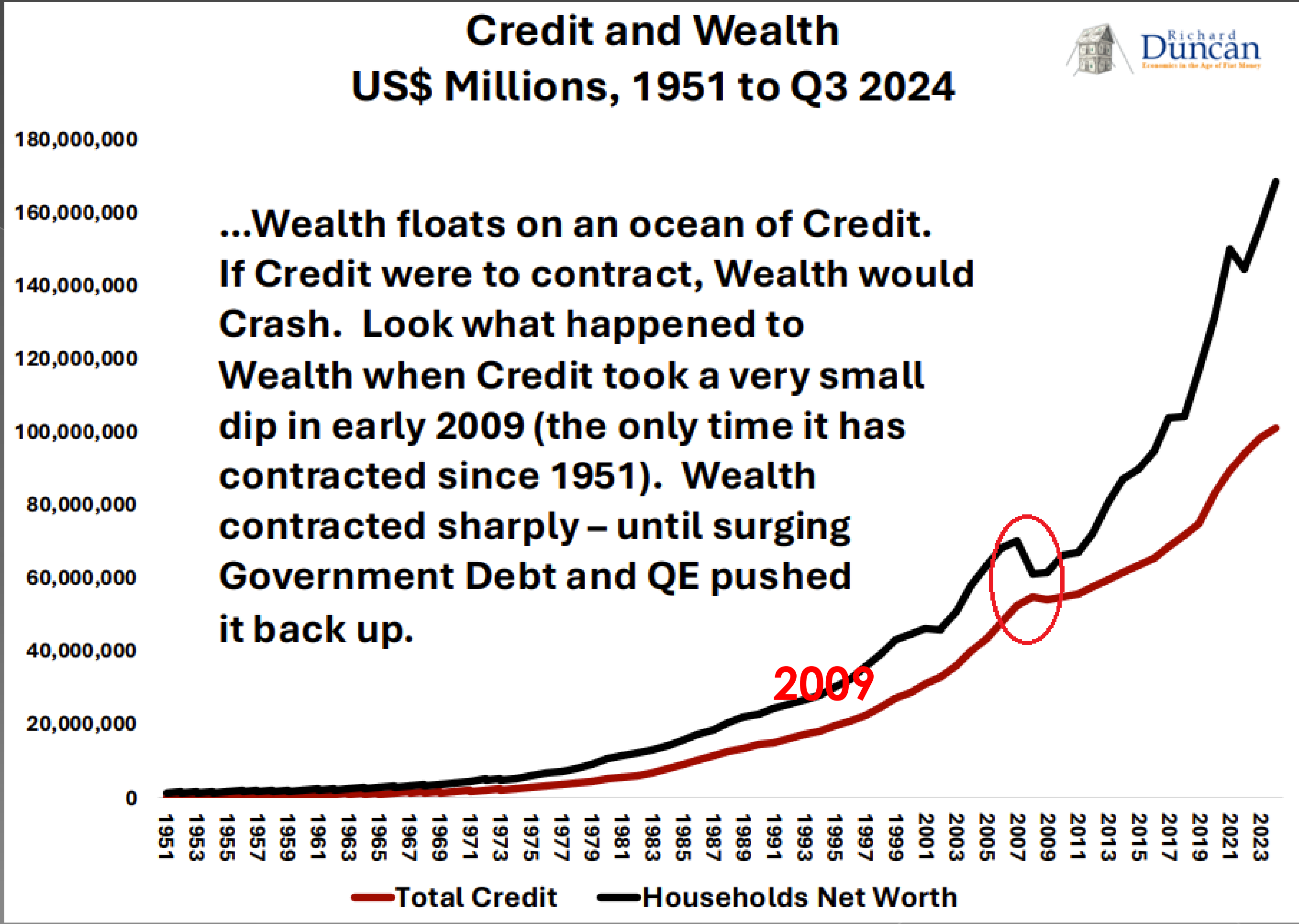
US$ Millions, 1950 to 2024



Household Wealth in the United States has jumped by $52 trillion or by 44% over the last five years alone – and by $108 trillion or 2.8 times since 2008.


Net Worth as a Percentage of
Disposable Personal Income
1950 to 2024
The Wealth to Income Ratio (shown here) has averaged 575% since 1950. It is currently 783%, 36% above that average. If it were to fall back to its long-term average as it did following the Nasdaq Bubble and the Property Bubble, more than $60 Trillion in Wealth would be destroyed.
2024:
783%
900
800
700
600
500
400
300
1950
1952
1954
1956
1958
1960
1962
1964
1966
1968
1970
1972
1974
1976
1978
1980
1982
1984
1986
1988
1990
1992
1994
1996
1998
2000
2002
2004
2006
2008
2010
2012
2014
2016
2018
2020
2022
2024

THE REAL BIG PROBLEM!



Since 2010, Billions USD
DERIVATIVES / INCOME AUM
Billions USD
250
200
150
100
2010
2015
2020
2025
+163B$

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"Restoring the U.S. to its historical trend rate of economic growth depends heavily on reversing the debt overhang.

The Fed has yet to cushion the economic restraint from current federal spending and adverse multipliers, the lagged effects of prior central bank actions, and the immediate demographic drag... the risk of recession is high, and the transition to meaningful recovery will be fitful, uncertain, and labored.

Such an uncertain environment of tepid or negative economic growth will be conducive to a downward trajectory of long-term Treasury rates."

Lacy Hunt PhD
Hoisington Investment Management

EXPECTATIONS

SHORT TERM – WEALTH EFFECT LIKELY TO BE ARTIFICIALLY MAINTAINED

INTERMEDIATE TERM – TRANSITION TO BALANCED TRADE & CURRENT ACCOUNTS

QE WILL RETURN

- Bernanke: Printed $2–3 trillion in three or four years.
- Powell: $5 Trillion in 18 months.
- This time: **It's going to be $7 to $10 Trillion.**

YCC WILL BE ADVANCED

THE DOLLAR WILL FALL WITH YIELDS

- Inflation
- Market Rises on a Shrinking Dollar

LONGER TERM – US RETURNS TO POSITION OF LEADERSHIP

American Exceptionalism Will Return.
Dollar Will Strengthen.
Economy will regain strong growth.

EXPECT A US$ CURRENCY DEVALUATION BEFORE TRUMP'S TERM EXPIRES!

ADMINISTRATIONS CHANGE – BUT THE PRINTING NEVER DOES ….

DON'T WORRY, THEY WILL PRINT THE MONEY!

EVERYONE IS NOW IN PLACE & READY!!

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- Real Time Charting
- Guest Interviews
- News Abstraction Process
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