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Buying US Treasury Bonds, A Sucker's Game

How the FED and other central banks conspired to transform US Treasury Bonds from "Junk Bonds" to AAA rated bonds.

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Future Fast Forward

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Buying US Treasury Bonds now as advocated by so-called experts is turning logic on its head.

What I am going to say is so outlandish and unconventional that my critics and detractors will in a single chorus declare that I have gone nuts! In another blast of Wall Street conventional wisdom (or rather FED's dogma) they will also accuse me of turning their logic on its head.

However, I am willing to take on any challenge that by the end of this article, I will be proven right because common sense always trump so-called logic of banksters and fraudsters.

After all, it was a child who exposed the scam and cried out, "The King has no clothes!" History is replete with examples that the minority of one (and right now I am in such a position pending the publication of this article) has been able to turn the tide by persistence, dedication and common sense. I believe strongly that the Joe Six-Packs of the world upon understanding the nature of the US Treasury Bond scam will not sit back and allow the scam to continue to their detriment.

Let me use some analogies and your own experience in money matters to drive home the point. Please be patient.

So, here we go!

Situation 1

Ask yourself this question – "Would you consider yourself prudent and reasonable and your bank prudent and reasonable in lending to a borrower a substantial sum of money in the following scenario?"

Jack of All Trades (Jack) is applying for a loan of US$3 million from his bank for a business venture. Just in case he may not get the loan or as much as he has applied for, Jack has asked you to extend a personal loan of US$1.5 million as a short-term cushion. You have been friends for ages.

His present financial situation is as follows:

His only real tangible asset is his matrimonial home in joint names of Jack and his wife Jill. It is valued at US$2.5 million and has been mortgaged to Citibank. There is an outstanding loan amounting to US$2.2 million. He has not paid any installments for the last six months. Interest is compounding!

Jack and Jill have outstanding credit card debts amounting to US$260,000 due to five different credit card companies. Jack gets a reprieve because he was able to get new credit card accounts from a new set of credit card companies by transferring the outstanding balances as advertised in the marketing brochures of most credit card companies. These advertisements tease credit card debtors that on transfer, the interest levied would be lower.

They are also in arrears on their car loans and the liability is US$65,000

The combined income of Jack and Jill is US$20,000 a month. Jill has just received a notice that she will be retrenched in three months' time.

I am confident that you would not agree to extend any loan to your friend and that his bank would likewise reject his loan application for the simple reason that the combined income stream of Jack and Jill (in the light of their present liabilities) would not be able to support such a credit application. The banker would be negligent or reckless to extend credit facility to Jack and Jill. But, that was what happened in USA when banks granted Sub-prime loans, "Liars Loans" etc.

Situation 2

Mills Inter-State Transport Co. is a reputable company and has been in the business for close to thirty years. The previous CEO has mismanaged the company and as a result revenues have plummeted to an all-time low for financial year ending January, 2013. Receivables have also dropped drastically as trade customers have difficulties in paying outstanding bills.

Cost has also gone up. So, the overall picture of the company is not too good. Fortunately, the only major liability is an outstanding loan of US$4 million that was obtained some three years ago to extend the warehouse and the truck maintenance facility.

The fleet of trucks is old – the average age is 20 years. There are just not enough funds to acquire new trucks to improve inter-alia productivity. The employees are all very loyal and have been willing to take a pay-cut to help the company tide over the bad times as the alternative would be retrenchment. A potential partner has shown interest in taking up a share of the business on offer and would be willing to inject new capital provided the company can secure short-term loans to address cash-flow problems for the immediate future (at least two years).

However, the new CEO has been able to cut costs, increased collection of receivables and more importantly secured three new contracts that would improve profit margins by 30 per cent in the current year and fifty per cent within two years. Financial advisers have advised that the company should approach their bankers for additional facilities as well as issuing a bond to some investors,
but cautioned that such a bond would be feasible if the yield (interest) is attractive – i.e. better than the existing rates.

I am confident that as a banker and or investor you would be willing to take a risk and extend a financial facility to the company provided the yields are attractive enough to compensate the risk of a presently cash-strapped company with improving revenues and profit margins. The financial status of this company is far better than that of Jack and Jill. The ethos of the company in financial matters is one of prudence and conservatism. While such a bond may not be rated AAA, it would also not be rated as a Junk Bond. It would be rated most likely somewhere in between.

Situation 3

The Republic of Extravagance have been on a consumption binge for two decades financed by easy credit by external trade creditors and loose monetary and fiscal policies of the regime. The country has a standing army that dwarfs the combined might of eight neighbours. T

here is not much manufacturing in the country and its main export is drugs, illicit arms and human trafficking. Because of its military might, the Republic of Extravagance is able to bully its neighbours into submission and demand that they sell their resources at rock bottom prices in exchange for illicit drugs, primarily cocaine. The country has been printing money to pay for other imports and as a result inflation is 230 per cent and rising.

National debt has ballooned 300 per cent of GDP.

The citizens have not rebelled, because of the tyranny of the state. The Department of Internal Security is almost as big as the standing army and in some areas have better equipment as a result of massive allocations under the previous five budgets. The Continental Union Bank reluctantly agreed to grant special loans only because the Republic is willing to pay 25 per cent yields!

Obviously, the third situation does not represent any existing country, but the point is that in Situation 1 and Situation 3, it would be unwise to extend any credit facilities and even if credit facility is to be granted it would be with a hefty premium – a spike in the yield to compensate for the high risk of default.

In the real world there would be creditors who would be willing to extend credit facilities to such countries BUT THERE IS ALWAYS THE CAVEAT – These countries have to pay a hefty yield!
Such bonds, whether corporate or sovereign are referred to as “Junk Bonds” as opposed to triple-A rated bonds.

This is common sense.

Situation 4

Peter is a small trader and is very popular with his customers for he has a big heart. Whenever a customer has difficulty in paying his bills after the expiry of his 14 days credit period, he would extend the period for another 14 days.

“Lucky” Jim was a new customer and though at times he was in arrears, he had always made good his debts. He was called “Lucky” because he was good at the local casino which is situated in the back room of a popular diner/bar. Lucky Jim has no business of any kind and don’t seem to be gainfully employed, but he has always been able to meet his obligations. The fact that it was rumoured that he was somehow linked to some mobster in Chicago have deterred people from being too curious.

One day, Peter called upon Lucky Jim at his home to enquire why he was overdue for more than 45 days and there was no attempt by him to explain the situation. He was pleasantly surprised to see Lucky Jim in overalls working frantically on a huge photocopying machine (a Japanese import) that can reproduce colour pictures, documents etc. as good as the originals. Lucky Jim was embarrassed by the unexpected visit and apologised for the delay in paying Peter, but promised to pay Peter in a matter of days. Peter not convinced, asked Lucky Jim how he would be able to meet his obligations. With his back to the wall, Lucky Jim volunteered that if he told Peter a secret, and if Peter would not divulged the secret, he would share the rewards with Peter.

Peter responded positively. So, Lucky Jim explained how by using the photocopying machine which he purchased at a hefty price from Japan, he could reproduce all the Federal Reserve Notes as if they were genuine. It was difficult for anyone to tell the difference unless he was an expert. Peter was bewildered and asked Lucky Jim how was it that he was never caught and was able to print so much money. Lucky Jim confided that he was not too greedy and only printed enough to meet his needs and a little more to indulge in some adult fun on the weekends with Patty "Galore" at Fun House at the corner of Main Street and Riverside road. Wow!!!!!

There were times when his friends who needed some emergency cash, he would lend them the "instant" cash hot from the printing machine and charge a small amount of interest. It was a good life.
He then lamented that a month ago, the machine broke down and he could not get the spare parts to repair the machine and so, he was now tinkering with it and hoped that he could repair the machine himself and that was why he was behind his payment. Peter was greedy and allowed Lucky Jim time to pay the outstanding debt as he was on to the game. However, when six months went by and Lucky Jim still could not repair the machine, it occurred to Peter that he would not be repaid at all. So, he called upon Lucky Jim and discovered to his horror that Lucky Jim has left town! The goose that laid the golden egg was dead. The party ended before it started!

We will now come back to reality.

Now, let me explain why I say that buying US Treasury Bonds is for suckers.

Some Basic Principles

Definition of Corporate Bond

A debt security issued by a corporation and sold to investors. The backing for the bond is usually the payment ability of the company, which is typically money to be earned from future operations. In some cases, the company's physical assets may be used as collateral for bonds.

Corporate bonds are considered higher risk than government bonds. As a result, interest rates are almost always higher, even for top-flight credit quality companies. (source: Investopedia)
Definition of Treasury Bonds

A marketable, fixed-interest U.S. government debt security with a maturity of more than 10 years. Treasury bonds make interest payments semi-annually and the income that holders receive is only taxed at the federal level.

Treasury bonds are issued with a minimum denomination of $1,000. The bonds are initially sold through auction in which the maximum purchase amount is $5 million if the bid is non-competitive or 35% of the offering if the bid is competitive. A competitive bid states the rate that the bidder is willing to accept; it will be accepted depending on how it compares to the set rate of the bond. A non-competitive bid ensures that the bidder will get the bond but he or she will have to accept the set rate. After the auction, the bonds can be sold in the secondary market. (source: Investopedia)
For the uninitiated, a bond with low yields (i.e. interest) is said to be a "good bond" – if rated AAA because the risk of default is minimum and would fetch a higher price because the issuer of the bond (the country) has a good credit standing. The country has no problems paying off its debts. The risk of default is very low or unlikely as opposed to the case of Republic of Extravagance in Situation 3.
Bonds issued by highly indebted companies and or countries are rated as "Junk Bonds" and as such the yields are very high to attract lenders and or investors who are willing to take extraordinary risks for a higher return. Very, very few financiers and or investors would go near them – they are toxic and hence fetch a lower price!

Please bear this principle of bond pricing in mind.

The case of the United States of America

Let's be real and honest. If the US is not a military super-power, it would be classified as a "Banana Republic" not unlike the country in Situation 3 above.

It is a bankrupt country and is the world's biggest debtor in the amount of US$ outstanding to foreign creditors!

This is not in dispute by all the experts. Just Google "which country is the biggest debtor?" and the answer is the US (source: IMF)! As at 2013, the total national debt is over US$16.805 trillion which is larger than the country's GDP! When we include the unfunded liabilities, some experts have calculated the debt to be over US$100 trillion. The US is a zombie debtor – walking DEAD.

There is just no way for the US to pay off the debt. It is mathematically impossible to repay the debt even if the US government were to raise taxes by 200 per cent! But, that would not be acceptable by the people and would spark off a revolution in the US.

So by any measure, any bonds issued by the US treasury ought to be classified as "Junk" and a hefty interest would have to be paid to creditors to buy the bonds.

The US$ trillion question to be asked is, "Why have foreign creditors lent so much money to the US when it is in such a hopeless financial mess?"

Many reasons have been put forward, but let's cut out all the crap and get real. The main reason is that these foreign creditors (stupid corrupt governments) just don't understand how the scam has been perpetrated, not unlike Peter in situation 4 above.

The world believed that fiat money (especially the US Dollar) which is backed by nothing except the good faith of the issuer is better than gold and is genuine money for all intent and purposes. The foundation for the acceptance of fiat currency as money is confidence and the artificial demand that has been created to inculcate such confidence.

In my previous article, I explained that in 1971, Nixon had abandoned the gold standard and that the US dollar would no longer be redeemable in gold and became pure fiat currency. To sustain confidence in the US$ toilet paper money, the idea of Petro-dollar was floated by Henry Kissinger to the Arabs who were coerced into agreeing to sell crude oil denominated in US$ toilet paper money in exchange for the guarantee that the US military would protect their regimes from external threats (specifically from Israel) and internal threats (i.e. coups and revolutions). And as they say, the rest is history.

The Shadow Banking Bubble

Let’s fast forward to the present moment – past the 2007/2008 Global Financial Tsunami.

In summary, as a result of the loose monetary policy started by Alan Greenspan, the predecessor of “Helicopter” Bernanke, several economic bubbles were created – the housing bubble, the stock market bubble, the Private debt consumption driven bubble which popped one after another in 2008.

Additionally, there was also the Shadow Banking Bubble (which no one mentions because so few understand the mechanics of Shadow Banking and the derivative casino).

In the result, the US became bankrupt. The music stopped and the champagne party was over. US$ trillions were wiped out. Families lost their homes through foreclosures, businesses collapsed and massive unemployment was the result. Millions were on food stamps (over 40 million Americans). So, who can we blame for this financial fiasco? Well, it must be the FED and the US Treasury who like “Lucky” Jim was able to print (digitally) so much money, thereby flooding the market with cheap credit and this was multiplied many, many times as a result of fractional reserve banking (which allows banks to create money out of thin air – 10 times customers’ deposits) and speculation in the global derivatives casino.

It was a financial orgy that defied all common sense and logic.

The US Treasury was bankrupt, but they needed to borrow more money, much, much more money to survive. At first, the foreign creditors like stupid China and Japan were willing to come forward to help the US as the cheap credit intoxicated American consumers were the biggest spenders / purchasers for their exports. The US was the largest consumer market in the world.

But, the financial status of the US has descended to that of a “Banana Republic” not much different from the case of the Republic of Extravaganza in Situation 3 above.

Fear gripped and chocked the powers that be in control of the FED and the US Treasury. They just could not afford a situation whereby creditors (any creditors) would demand exorbitant interest rates for lending to the US. Technically, any bonds to be issued by the Treasury would strictly and technically be rated as “Junk Bonds” and not AAA as was the case before the “Great Recession” (how brilliant it is to mis-name the financial catastrophe as such and not more appropriately the “Second Great Depression” as it should be called). I would even contend that even before the financial fiasco, there was no way to justify a AAA rating as the US was in a financial state no different from Jack in Situation1. The US succeeded in getting a AAA rating because it was a scam as all the world’s rating agencies were US rating agencies and why would they stop the music and end the party when such AAA ratings (fraudulently given) would generate US$ billions in profits and have generated such profits for a decade or more!

The Scam

To hoodwink the creditors, the FED adopted two strategies (and we must give credit to those fraudsters in the FED and Treasury for their audacity in the execution of this fraud).

Firstly, they ensured that the printing machine (digitally or otherwise) would be functioning at full speed without any glitches. They cannot afford a "Lucky" Jim scenario. With modern technology of the computer and the mouse, all that was needed was a simple click of the mouse, and there would be a Book Entry in the FED's computerised ledger in the columns – "Credit / Debit" and "Assets and Liabilities" – the requisite amount/value of the newly created digital monies. In technical jargon, the FED was monetising the debt by creating money out of thin air. But, for other countries and Joe Six-Packs, they have to work their guts out to earn an income, save the surplus to pay off any debts that they have incurred (borrowing US$) to purchase crude oil and other necessities (as all oil trades are denominated in US$ as well as other goods). We cannot create money out of thin air by the click of a computer mouse!

But, then any massive money printing would devalue the currency, so some of the monies were diverted into the stock market to create "asset inflation" i.e. to artificially jack up the price of the assets – the shares quoted in the stock exchange, thereby creating an artificial demand for more US$ toilet paper money and hence its value would be maintained and at worse would not depreciate that much. The new monies were also used to pay off existing debts and to finance new debts incurred by the US Treasury.

However, that would not really solve the problem of the risk of a junk rating of the US Treasury bonds. Technically, they are junk and would result in high yields so there was an urgent need to dress-up the bonds to justify an AAA rating.

Please grant me the indulgence of a digression.

This is why it is so important for the Joe Six-Packs to understand why the FED was given the power to control interest rates in addition to the power to print money (digitally). If the FED is only authorised to create money out of thin air, it would not be really useful because the mere printing of money would not confer any long lasting benefit to the financial elites and the entire fractional reserve banking system grounded on fiat money.

The Fed must control the rate of interest for interest is the life-blood of the banking system and whosoever controls interest controls the life-blood and in simple financial terms, control the revenues and profits to be made by the entire banking system thereby conferring on the privileged 1 per cent an unbridled means to limitless wealth. The only caveat is that at all times the members of the system must not be too greedy to demand more monies created out of thin air (with no risks) than were required to keep the system running and the party going as well. There must be a stream of interest payments (income) at a rate that would not kill the borrowers. Without borrowers there would be no customers for the fractional reserve banking ponzi scam!

Let's get back to the issue at hand.

So, there was a need to convince the world at large that the US Treasury is not Jack the pauper but a credible borrower and ought to be treated as such.
So what was the trick, the scam that would convince unthinking and greedy creditors, be they sovereign creditors like China and Japan and institutional and retail investors (foreign banks and pension funds etc.)?

To turn the trick, it required the combined efforts of selected economists (plus one or two Nobel Laureates), financial analysts, rating agencies who know there is a whole lot of money to be made by participating in the scam to spew the propaganda that US Treasury Bonds are the best assets (safe-haven) in times of crisis and not Gold (derogated as a Barbaric relic). And, since the financial elites also control the mass media – print, TV, and radio etc., it would be easy to spread the propaganda.

With the FED in total control of interest rates, all it needed to do is to announce the policy of zero interest rate (ZIRP) and automatically interest rates on any borrowings would plummet. Of course Joe Six-Packs did benefit somewhat, but that was purely collateral. The main beneficiary of ZIRP is the US Treasury, the biggest debtor in the world. And as they say, the rest is history.
Having over the years brainwashed students in economics at leading universities, financial harlots in global banks and financial services institutions etc. that low interest rates is the benchmark for financial credibility per se (i.e. to ignore the fundamentals when it comes to US Treasury bonds, but not any other borrowers), foreign sovereign creditors like China were conned into lending monies to the US and in the case of Japan were compelled to do so as the vanquished foe of the US after World War II and now a client state under the nuclear protection of the US military.

No one dared cry out, “the Emperor has no clothes”, it is bankrupt! The zero interest rate policy (ZIRP) is a scam to cover-up the reality that the bonds are in fact junk bonds. Bearing in mind the principles of bonds as explained above, low interest rates was the illusion that clouded the minds of creditors to believe that such bonds could not be junk bonds. These creditors totally ignored the financial fundamentals of the US as a debtor that cannot mathematically pay off its debts.

These creditors also overlooked the fact that even if there were repayments, it was by way of more of the same – US$ toilet paper money, more fiat money created out of thin air.

For those who think that what is stated here is conspiracy theory, good luck to you if you have invested in US Treasury Junk Bonds. The truth of the matter will be decided in the near future whether the US Treasury Bond market is also another huge bubble sustained thus far by the above scam perpetrated by the FED and other central banks.

It is not my objective to convert the establishment to my point of view. How can that be possible when they are the perpetrator of the fraud? My sole aim is to sound the alarm to all the Joe Six-Packs of this danger and to prevent their wealth and hard-earned money from being wiped out by this scam and or confiscated by outright legalised plunder when their bank deposits are used to bail-out the Too Big To Fail (TBTF) banks.

Please, don’t accept my assertions after reading my article. Pause and think and think deeply. Do your research, investigate the history of the Fed and other central banks and more importantly question the disinformation in the mass media.

Final Comments

Ask yourself and your friends if what I wrote is gibberish, why –

1) The global banks fraudulently manipulated the London Inter-Bank Offered Rate (the LIBOR)?
2) Why do they manipulate the stock markets, the commodities markets and the gold markets (especially COMEX) to depress the precious metals markets?
3) If what I wrote is not true, then why has the FED embarked on QE3 to purchase toxic assets from banks and US Treasury Bonds at this material time if there was no dearth of creditors all eager to buy US Treasury Bonds?
4) Is this not a sick joke – the US Treasury actually borrows from an institution, the FED which was created by Congress. The FED created money out of thin air, by a digital entry in the FED's computerised ledger?
5) Do you know that the interest derivative contracts traded in the global derivative casino is the largest of all derivative contracts? Do you know that the top 25 US global banks control this market and at the height of the financial orgy, the casino was notionally valued at US$800 trillion? That is not a typo. Please Google to find out the present value or go to the FED website. Some experts even valued the notional value of the derivatives casino at a US$ Quadrillion.

So, I hope you will agree with me that buying US Treasury Bonds is a sucker's game and you are the sucker if you had invested in these fraudulent bonds.

I make no apologies for being so blunt.

Addendum:

Many have asked me to write such an article two years ago, but I declined because it would have been very difficult to put across my arguments until the onset of QE 3 when the FED began to print digitally US$85 Billion a month to purchase mortgaged back securities (toxic waste from the TBTF banks) and US Treasury Bonds. This was the smoking gun. But, the nail in the coffin is the FED's Zero Interest Rate Policy (ZIRP).

This was the evidence I needed to show how the FED and other central banks conspired to transform US Treasury Bonds from "Junk Bonds" to AAA rated bonds.