

Bring on the Vigilantes

February 23, 2004

Bill Gross of Pimco is the icon of the bond management business. Some of his recent commentaries have made some of our clientele very nervous. In fact, we have lost a few, opting for the inflation scenario, which seems to be his message rather than deflation, which is our position. Please keep in mind that this man has \$300+ billion under management, whereas Central Plains Advisors, Inc. has only a small fraction of that amount. Also, you should know that in the one instance in which we both managed separate bond accounts for the same client, Central Plains Advisors, Inc. had a better record of performance. Both performances were good.

On various web sites that list a link for his works the explanation of his latest epistle suggests that his major assets for investment are commodities and foreign bonds. These are a play on inflation and a weaker dollar. You know this may work for a short period of time, as this seems to be the consensus. However, what he said in conclusion is what we have maintained for years: "Risk markets (stocks, high yield bonds, etc.) will be at risk should we move toward this outcome. And too treasury interest rate may then ultimately fall instead of rise as reflation fails and debt deflation takes hold." He assumes sometime rather soon the famous Bond Market Vigilantes will spike interest rates and bring the economy to its knees. We are not certain which way this puny recovery will come to an end. It may well die of it's own weight as the burden of debt cannot be overcome. If so this would result in a lack of demand, a reduction in prices, and a sharp move to safety. This is our best guess. If it develops that the vigilantes go on strike (rate spike) we will probably see a 1987 crash all over again that will result in a move to safety (government bonds). For selfish reasons that's fine with us.

What we read into his investment outlook "The Last Vigilante" is that he is preparing his clients for an upcoming recession and bond defaults. This, of course, will also result in a stock market decline. We would guess he believes that he can switch corporates to governments at just the right time. We don't believe we are that smart. Central Plains Advisors, Inc. prefers to own the ultimate winner and let Bill Gross buy our long governments at 3% or less. It's nice to know we have a buyer lurking out there in the marketplace.