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The Carlyle Compass

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*Welcome back to **The Carlyle Compass**, your weekly newsletter that brings together the latest research and market insights from our global team. Received this email as a forward? Subscribe here.*

Over the past year, the range of potential outcomes for stocks and bonds has widened massively, yet market pricing continues to focus on a very narrow band of that range that looks suspiciously close to a best-case scenario. In our new report, *Through the Looking Glass*, we explore some of the implications for investors.

- **"Blurring of the lines separating fiscal and monetary policy."** In the slump that followed the 2008 financial crisis, the Fed expanded its remit in ways that often blurred the lines between fiscal and monetary policy. It now appears to be the Treasury Department's turn to do some "blurring" of its own as it enlists the help of the Fed to drive down interest payments on the federal debt. While this strategy could prove a smashing success, it could also destabilize Treasury markets if bondholders perceive that monetary policy has been suborned to stabilize public finances rather than defend the real value of their principal.

- **AI isn't frictionless disinflation.** Proponents of sharply lower rates laugh off inflation concerns by pointing to the disinflationary force of AI. Yet the last three years have taught that the road to that Agentic AI future is paved with trillions of dollars of annual investment, driving up demand for construction workers, power, and capital. Real interest rates averaged nearly 4% during the last concentrated capex boom of comparable magnitude (the late 1990s internet and mobile telephony capex wave).

- **Concentrated public-market bets.** It is hardly obvious that AI-related revenues will arrive at the scale and time horizon necessary to validate these enormous outlays. Yet the US stock market looks like a concentrated bet on the best-case outcome, with total market capitalization dominated by a handful of richly-valued companies exposed to the same risk.

- **The prospect of market-neutral returns.** A stock market in thrall to "themes and memes" drives home the distinction between *trading*—buying assets to sell—and *investing*—buying assets to own. With transaction prices based on underwritten return expectations over multiyear holding periods, private markets have largely avoided the liquidity-driven froth observed in public markets. While the discipline enforced by private markets' arithmetic constraints has depressed transaction volumes in recent years, it also raises the prospect of attractive, market-neutral returns going forward.

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