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Morning Briefing

On Bitcoin, India,
And S&P 500 Earnings

Check out the accompanying chart collection.

Executive Summary: Today, Eric examines MSTR's strategy of levering up to buy bitcoin via equity and debt issuance. It's worked great until recently; but if the value of bitcoin were to continue to plummet, MSTR could be in trouble. We think bitcoin is here to stay; MSTR may not be. … Also: Melissa reports that India's financial markets have become speculative and its GDP growth has cooled from its former blistering 8% y/y rate. But the government has a plan: "Make India Great Again" aims to grow India into the world's third largest economy by 2030. … How supported by earnings are recent S&P 500 valuations? Joe shares timely data on which way the estimate revisions winds have been blowing.

Crypto: Leveraged Bitcoin with Convertible Bonds. We have viewed bitcoin as a digital tulip. That's not to rag on bitcoin or its investors; rather, we're suggesting that speculation in high-beta novel assets like bitcoin has evolved in the modern financial system.

Unlike tulip bulbs, bitcoin can be traded online, 24/7, globally, and has multiple uses. It can be used as a currency for transacting or stored for its appreciation potential. While bitcoin tends to trade like a triple-levered Nasdaq 100, it did not collapse during the recent Fed tightening cycle, a fact that has encouraged institutional players to join the fun (*Fig. 1*).

Michael Saylor's Strategy (a.k.a. MicroStrategy, ticker: MSTR) has garnered attention for its strategy of accumulating bitcoin during its meteoric rise. Even after falling roughly 40% since November (including 10% on Tuesday), MSTR is still up about 220% over the past year and about 2,180% since it began purchasing bitcoin in August 2020 (*Fig. 2*). Levering up to purchase bitcoin via a combination of equity and debt issuance has led to MSTR's trading at a premium to its nearly 500,000 of bitcoin holdings, which are worth roughly $47 billion. Bitcoin is up 706% since MSTR began buying it.

A key part of Strategy's strategy is to issue 0% coupon convertible bonds to fund its bitcoin purchases. Let's explain why this works, and perhaps how it unravels:

(1) *Bitcoin goes up*. A core component of Strategy's playbook is to issue 0% convertible bonds at little cost, buy bitcoin with the proceeds—driving up bitcoin's price, which in turn causes MSTR's share price to rise—then issue more debt or equity at a higher valuation, buy more bitcoin, and so on. Rinse, wash, repeat.

Since 2020, Strategy's bitcoin holdings have risen from $250 million to nearly $50 billion. The company's "21/21 Plan" aims to raise $42 billion over three years to buy more bitcoin.

(2) *Convertibles can't go belly up ... right?* On February 20, Strategy issued $2 billion in convertible senior notes due in 2030 with a 35% premium, meaning that investors could convert their bonds into MSTR shares if the price rose more than 35% and pocket the difference. That followed a $3 billion issuance of convertibles due in 2029 last November, which were priced at a 55% premium.

So if the convertibles pay no coupon and investors can only experience upside after sizable price appreciation, why don't they just buy MSTR? Or bitcoin?

Institutional investors are big fans of buying convertibles because they can participate in bitcoin's/MSTR's rise while limiting their downside risk. Bondholders still get their principal back if they choose not to convert into shares (i.e., if MSTR falls substantially, as it has been doing in recent days). In the event of bankruptcy, the notes are senior to shareholders. MSTR also has a legacy software business that brings in roughly $500 million in annual revenue, so there are some assets to fall back on, even in the event of a bankruptcy.

All that said, convertibles aren't "risk free." For instance, MSTR's zero-coupon convertibles issued in November are now trading at a 23% discount to par (or 77 cents on the dollar). The stock would now have to more than double in price for it to make sense for an investor to exercise the conversion option. Hedge funds using arbitrage strategies, such as shorting MSTR and buying the convertibles, might still profit from the price difference as well as the embedded long-volatility component of the convertibles. So there's protection in buying convertibles, but no free lunch.

(3) *When does the gravy train end?* Rather than repay principal on maturing convertibles, MSTR tends to roll them over, or issue more debt to pay off the old ones. If demand for bitcoin dries up or the price falls substantially, MSTR may not be able to tap the capital markets to repay investors their principal. Selling bitcoin to finance those repayments would lead to a downward spiral, as is often the case in the post-mortem of many leveraged bets.

We think bitcoin is probably here to stay. MSTR may or may not be. Trump 2.0 seems invested in crypto's success, but a recession or economic slowdown undoubtedly would hurt bitcoin's price. If you choose to invest, caveat emptor.

Following today's 3% drop, bitcoin is now down more than 16% from its December 17 peak. And after discounting its future cash flows and assessing the quality of its management team, we see additional downside as a reasonable possibility. Still, we do expect US macroeconomic data to improve next month, so we could see bitcoin back above $90,000 in short order.

India I: Is the Party Over? India's equity and credit markets have become hotbeds of speculation. Deputy Governor Rajeshwar Rao recently voiced concerns about over-leveraging in unsecured credit markets and a "frenzy" in capital markets. Overheating of Indian equities, a theme we've discussed since last summer, is now more evident.

Investor demand for India's government debt soared following its inclusion in global bond indices, helping to lower the spread between the 10-year Indian government bond yield and the comparable US yield to only 231bps (half as much as five years ago) (*Fig. 3*). But now, the upside in India's financial markets may be fading—especially with signs of a potential economic slowdown.

Let's have a closer look:

(1) *Equity valuation has downshifted.* India's MSCI stock market index surged from a low in October 2023 to a record high in September 2024, peaking at a valuation of 25 times forward earnings per share (EPS). This multiple since has retreated to a 14-month low of 20.8 as of Tuesday's close, marking a souring of investor sentiment.

(2) *Equities have retreated*. The India MSCI index is down 7.0% ytd (*Fig. 4*). Real Estate stocks, collectively down 22.1% ytd, have been a major drag on the index so far this year, while Communications Services stocks have bucked the trend with a modest ytd increase of 2.4% (*Fig. 5*).

(3) *Earnings momentum has stalled*. Forward EPS for Indian companies in the India MSCI rose 21.4% from August 2022 through the start of 2024 (*Fig. 6*). From mid-2024 until now, however, the index's forward EPS has stalled out.

(4) *Bond yields have cooled*. India's 10-year government bond yield fell below 7.00% in mid-

2024 and has continued to inch lower; it now stands at 6.70% (*Fig. 7*).

India II: India's Make-or-Break Moment. India's real GDP growth has cooled from its heady 8.4% y/y rate during India's last fiscal year, ended March 2024, and the Reserve Bank of India (RBI) projects continued slowing to around 6.5% y/y by fiscal 2026.

But Prime Minister Narendra Modi's government isn't sitting idle. To put growth back on the 8% track, fiscal and monetary policymakers have introduced stimulus measures that include substantial tax cuts and easing of credit rules. Driving these moves is Modi's ambition to transform India into the world's third-largest economy by 2030, his Make India Great Again (MIGA) plan. But whether the country can return to its previous pace is an open question.

To help support the economy, the RBI's new chief (as of December), Sanjay Malhotra, has moved the monetary policy needle to neutral from his predecessor's hawkish position. Accommodative measures taken include delaying new banking regulations that might have hampered credit flows and lowering the RBI's key short-term rate in February.

In addition to monetary policy support, the government recently has slashed taxes to reinvigorate consumption. But the fiscal supports are a mixed bag. Modi's budget for next fiscal year cuts spending on social programs. Modi has been criticized for allowing the economy to fall into a middle-income-trap.

It is not yet clear whether these fiscal and monetary supports will be enough to restore and sustain a growth trajectory near the previous 8% y/y pace. Here's more:

(1) *Growth slowdown is apparent.* India's Q3-2024 GDP fell 7.9% q/q but increased 5.6% y/y; that compares with year-earlier growth of 8.6% y/y (*Fig. 8*).

(2) *Sentiment is weakening*. Worsening this slowdown are weakening consumer and business sentiment (*Fig. 9*).

(3) *Fiscal support waivers*. Fiscal spending reached nearly 90% debt-to-nominal GDP shortly after the pandemic but eased to 83.5% by Q2-2024 (*Fig. 10*).

(4) *Monetary easing & inflation*. The RBI lowered the short-term rate to 6.25% in February 2025, after having held it steady at 6.50% since February 2023.

India's inflation remains above the bank's 4.0% target despite having fallen from above

6.0% in October 2024 to 4.3% in January 2025 (*Fig. 11*).

India III: Modi's MIGA Vision. India's path to becoming the third-largest economy by 2030 is fraught with challenges, from internal inefficiencies to geopolitical issues. But with monetary easing, fiscal support, and bold initiatives, India aims to reattain close to an 8% y/y growth trajectory. Whether these efforts can overcome the structural hurdles facing the economy remains to be seen; but for now, India continues to push ahead on the global stage.

Vineet Jain of *The Times Group* introduced Prime Minister Narendra Modi at the 2025 Global Business Summit, highlighting Modi's broad growth strategy and listing its key initiatives:

(1) *MIGA: Modi's strategy for global leadership*. Modi's MIGA plan seeks to position India as a global leader in key industries by 2030, promoting both self-sufficiency and stronger international partnerships.

(2) *US-India COMPACT*. The expanding US-India alliance is focused on technology, defense, and trade. This strategic partnership is designed to counterbalance China, creating new opportunities for collaboration in AI and space exploration.

(3) *"Make in India."* The Make in India initiative has revitalized domestic manufacturing, attracting significant foreign investment and positioning India as a competitive hub for manufacturing.

(4) *AI & "Digital India*." India is emerging as a global leader in AI, with a young population and increasing government support. The Digital India initiative is transforming the country, enhancing everything from e-commerce to government services.

(5) "*Startup India."* The Startup India initiative has fostered a flourishing entrepreneurial ecosystem, with growing investment in sectors like fintech and edtech.

(6) *India as a global manufacturing alternative*. India's push to become a global manufacturing hub is positioning the country as an alternative to China in the global supply chain.

(7) *Global technological leadership*. India's success in space exploration and its growing role in semiconductor production underscore its rise as a technological power.

Strategy: Are Earnings Forecasts Stalling or Falling? Ready or not, the Q4 earnings season is set to add Nvidia to the S&P 500's results as the index passes the 90% complete mark by week's end. It has been a "less strong" earnings season so far for the Magnificent-7 companies, with their future guidance less encouraging than in recent quarters. That has doused investors' enthusiasm for most of the group. Last week's earnings warning from richly valued Walmart unnerved investors even further, and some of them removed the stock from their shopping carts.

At a time when valuations are priced for perfection, investors urgently want to know: What's happening with earnings forecasts now? Below, Joe lends some perspective on recent consensus earnings estimate trends:

(1) *No sign of an earnings pothole ahead.* Estimates are pausing just below their recent record highs amid uncertainty about tariffs and lingering inflation. A return to estimate cutting as usual following the unusually strong post-pandemic years is occurring now. However, the recent declines have been relatively minor in the grand scheme of estimate revisions history even if they don't seem so in the context of recent years: From 2021 to 2024, consensus annual earnings forecasts on the whole fell less than usual and sometimes even improved from initial forecasts.

Since 1978, I/B/E/S has been calculating consensus bottom-up S&P 500 earnings forecasts, derived from each individual analyst's estimate for an S&P 500 company that they follow (*Fig. 12* and *Fig. 13*). Over time, professional investors—and hopefully the investing public generally—have learned that analysts' initial forecasts are typically too high and decline steadily until the company reports results.

It has been a good bet to make, as the annual forecast fell during 76% of time—or in 34 of the 45 years—from 1980 to 2024 (*Fig. 14*). Our measure tracks how much each calendar year's forecast changed in the 24 months from the initial estimate to actual reported earnings (e.g., for calendar year 2024's EPS forecast, we track how much that estimate changed from its initial forecast in February 2023 to its final value in February 2025).

(2) *Estimates are declining, but much less than in the past.* To give some perspective, the S&P 500's consensus annual earnings forecast fell an average of 11.1% during the past 45 years. During the 11 years that ended with results that were surprisingly better than initially expected, forecasts posted an average gain of 7.2%. During the 34 years with declining annual EPS forecasts, they tumbled an average 17.0%.

(3) *2024 estimate rallied higher.* The S&P 500's reading for the 2024 estimate ranked an impressively high 12th, with a 24-month decline of just 1.4%. The cumulative estimate change for 2024 actually *improved* as the finish line approached, something that typically occurred during one-third of the 45 years. So 2024 was a very good year, and we think that bodes well for the 2025 forecast.

(4) *How is the S&P 500's 2025's estimate looking at the halfway point?* The S&P 500's consensus annual earnings estimate for 2025 is down just 1.7% so far, after 12 months—the halfway mark between initial estimates for the year and the final results we'll see about a year from now.

When similar low-single-digit percentage 12-month declines occurred—which they did during 10 of the past 45 years—the actual earnings finally reported were down from initial estimates by percentages in the single digits for most years (all but 1981 and 1984).

We think that the momentum clocked at the halfway mark bodes well for the direction of the consensus 2025 estimate over the final 12 months.

(5) *Forward earnings remains strong for nine S&P 500 sectors.* Relatively few of the S&P 500 sectors have forward earnings still well below their post-pandemic record highs in 2022. In fact, most sectors still have forward earnings near their record highs. During the February 20 week, the S&P 500's forward earnings was just 0.3% below its record high in late January (*Fig. 15*). A whopping nine of the 11 sectors are less than 2.0% shy of their all-time record-high forward earnings! Just two sectors, Energy and Materials, remain far below their record highs and show few signs of improving.

Calendars

US: Wed: New Home Sales 680,000 units; MBA Mortgage Applications; Barkin; Bostic. **Thurs:** Real GDP & Price Index 2.3%/2.2; Durable Goods Orders 2.5%; Initial Claims 220k; Kansas City Manufacturing Index; Pending Home Sales -0.6%; Fed Balance Sheet; Golsbee; Barr; Harker. (FXStreet estimates)

Global: Wed: Germany Gfk Consumer Sentiment -21; Dhingra. **Thurs:** Eurozone Economic Sentiment 96; Spain CPI 3.1%y/y; ECB Monetary Meeting Accounts. (FXStreet estimates)

US Economic Indicators

Consumer Confidence (*link*): Consumer confidence fell for the third consecutive month, posting its largest monthly decline since August 2021 during February (-7.0 points). *Headline consumer confidence* sank from 112.8 in November to 98.3 by February, with the *expectations* component sinking from 93.7 to 72.9 over the same period—falling below the threshold of 80 for the first time since June 2024—a sign that a recession is likely ahead. Consumers' assessment of *current business conditions* dropped for the second month, from 144.0 in December to 136.5 in February. Of the five components of the index, only consumers' assessment of present business condition improved, though only modestly, with 19.6% of consumers saying business conditions were good, up from 18.5% in January, while 15.7% said business conditions were bad, up from 15.2% last month. *Turning to the labor market*, consumers' appraisals deteriorated this month, with 16.3% of consumer saying jobs were hard to get, up from 14.5% last month. Meanwhile, 33.4% said *jobs were plentiful*, edging down from 33.9% in January. Consumers turned negative on their outlook for *short-term business conditions* six months from now, with 26.7% expecting business conditions to worsen, up from 19.6% in January, while 20.2% of consumers expected business conditions to improve, down from 20.8% last month. Consumers' assessment of the *short-term labor market* also deteriorated this month, with 25.9% of consumers anticipating fewer jobs, up from 21.0% during January, while 18.4% expected more jobs to be available, down from 19.1% last month. Consumers were less optimistic about their *income prospects* this month, with 18.2% expecting their incomes to increase, only a tick above January's 18.1%, while 13.7% expected their incomes to decrease, up from 12.3% last month. As for *inflation expectations*, the 12-month expected inflation rate jumped from 5.2% in January to 6.0% in February—with references to inflation and prices in general ranking high in write-in responses—though the report noted "a sharp increase in mention of trade and tariffs, back to a levels unseen since 2019. Most notably, comments on the current Administration and its policies dominated the responses."

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