

KPP Financial Premium Newsletter

Independent Thinking, Shared Success

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KPP INSIGHTS: Digital Assets & the Disconnect of Scarcity

Recent price action in crypto markets has highlighted a growing disconnect between how digital assets are often described and how they actually trade. Headlines still focus on fixed supply narratives and halving cycles, yet day to day pricing is increasingly driven by derivatives, leverage, and rehypothecation. As a result, crypto now behaves less like a scarce commodity and more like a financial asset whose effective supply expands and contracts with risk appetite.

Start with the price behavior itself. Over the past several months, major cryptocurrencies have experienced sharp rallies followed by equally sharp pullbacks, often without a clear fundamental catalyst. These moves have been more violent than those seen in most equity indices and have frequently occurred outside of major macro news. That volatility reflects a market where marginal price setting is dominated by leveraged positioning rather than spot buying and long term holding.

Derivatives are central to this dynamic. Futures, perpetual swaps, and options now account for the majority of trading volume in major crypto assets. In many cases, derivatives volume exceeds spot volume by several multiples. This means that price discovery is happening in instruments that do not require full funding of the underlying asset. A trader can express a large directional view with a fraction of the capital that would be required in the spot market. That leverage amplifies moves in both directions and makes prices more sensitive to liquidations than to changes in actual ownership.

Perpetual futures are especially important. These contracts have no expiration date and are kept in line with spot prices through funding rates that shift between longs and shorts. When sentiment becomes one sided, funding rates rise and incentivize traders to take the opposite side. In theory this mechanism stabilizes prices. In practice it often creates crowded positioning that unwinds abruptly. When prices move against heavily leveraged traders, forced liquidations accelerate the move, creating the familiar cascade effect that defines many crypto selloffs.

Rehypothecation adds another layer. In traditional finance, rehypothecation refers to the reuse of collateral by intermediaries. In crypto, this practice has become widespread across exchanges, lenders, and decentralized finance platforms. The same underlying tokens can be pledged multiple times to support different positions. This means that while the protocol level supply of an asset like bitcoin may be fixed, the effective tradable supply in the financial system is not. Claims on the same asset can multiply, especially during periods of high leverage and yield seeking behavior.

This financialization weakens the argument that scarcity alone should drive prices higher over time. Scarcity matters when assets are held outright and removed from circulation. It matters far less when most activity occurs through synthetic exposure and rehypothecated collateral. In that environment, price is driven by balance sheet capacity, margin requirements, and risk controls rather than by the physical limits of supply.

This helps explain why crypto has recently diverged from equity markets. In earlier phases, crypto often traded as a high beta extension of tech stocks. When equities rallied, crypto rallied more. When equities sold off, crypto sold off harder. Recently that relationship has weakened. Equities have been supported by earnings resilience, buybacks, and a gradual easing of financial conditions. Crypto, by contrast, has been more sensitive to shifts in liquidity within its own ecosystem, particularly changes in leverage, stablecoin supply, and exchange level risk management.

Another source of divergence is the investor base. Equity markets are dominated by long term allocators, pensions, and corporations that respond slowly to price changes. Crypto markets are dominated by traders, hedge funds, and retail participants who respond quickly and often reflexively. That difference in time horizon means crypto prices can move independently of broader macro trends, especially when derivatives positioning becomes crowded.

Liquidity conditions also differ. While global liquidity has improved modestly, access to leverage within crypto has tightened relative to prior cycles. Exchanges have raised margin requirements, lenders have become more conservative, and regulators have constrained certain on ramps. When leverage is reduced, effective demand falls even if nominal interest remains high. This can pressure prices despite a stable macro backdrop.

Looking ahead, this structure has important implications. Crypto will likely remain volatile and prone to sharp moves that are driven more by positioning than by fundamentals. Supply narratives will continue to matter at the margin, but they will be filtered through a financial system that can expand synthetic exposure far beyond the underlying asset base. Periods of strong performance will likely coincide with expanding leverage and rehypothecation, while downturns will reflect rapid contraction in those same channels.

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STOCK IDEAS

Eli Lilly and Company (LLY)

Eli Lilly and Company's (LLY) latest results highlight a business still compounding at an exceptional rate as obesity and diabetes treatment demand scales. In Q4 2025, revenue increased 43% to \$19.3B and non-GAAP EPS rose 42% to \$7.54, driven by a 46% increase in volume. Mounjaro sales climbed 110% year over year to \$7.4B and Zepbound rose 123% to \$4.3B, underscoring continued category expansion. Management's 2026 outlook calls for \$80–\$83B of revenue and non-GAAP EPS of \$33.50–\$35.00, signaling confidence even as realized prices trend lower and access broadens. Lilly also announced a U.S. government agreement aimed at expanding access to obesity medicines for millions of Americans this year nationwide. The key debate is how pricing and reimbursement initiatives affect margins versus how quickly manufacturing scale, cost improvements, and product mix offset that pressure. Pipeline catalysts, including regulatory submissions for oral GLP-1 orforglipron and positive clinical readouts for retatrutide, support a longer runway beyond today's blockbusters.

Barrett Business Services (BBSI)

Barrett Business Services (BBSI) is a smaller, profitable PEO (Professional Employer Organization) that provides payroll, benefits, HR, and workers' comp administration for small and mid-sized employers. The stock has been soft recently, largely tracing back to the Q3 2025 report: revenue rose 8% to \$318.9M and gross billings grew 9% to \$2.32B, but profitability came in slightly light (EPS \$0.79 vs \$0.80 consensus and adjusted EBITDA below expectations), which triggered a selloff. Workers' comp expense was 2.2% of gross billings, helped by prior-year adjustments. What keeps the story promising is the ongoing controllable growth underneath the noise - average worksite employees increased 6% from net new clients, and management reiterated 2025 targets for 8.5%-9.5% gross-billings growth and 6%-8% WSE growth. The balance sheet is clean (debt-free, \$109.8M unrestricted cash/investments), and capital returns are meaningful via a \$100M repurchase authorization plus a \$0.08 quarterly dividend. Key swing factors remain labor demand and workers' compensation claims severity.

PORTFOLIO MANAGEMENT: Fixed-Income Strategies for 2026

In 2026, the fixed-income conversation has shifted from "waiting for rate cuts" to "capturing the carry." With the yield curve beginning to normalize and steepen, bond managers are increasingly moving away from the safety of cash and money market funds to lock in what are now the highest "real" (inflation-adjusted) yields in over a decade.

- **1. The Active ``Barbell" Strategy:** A popular approach this year is the Barbell Strategy, which splits allocations between very short-term and very long-term bonds, completely skipping the "belly" (intermediate) of the curve. The short end provides high liquidity and protection against sudden inflation spikes, while the long end allows managers to capture high yields and "roll-down" gains. In a steepening curve environment, this structure often outperforms a traditional balanced portfolio.
- **2. Laddering for Reinvestment Discipline:** For a more conservative, "all-weather" approach, many are returning to the Bond Ladder. By staggering maturities (e.g., having 10% of the portfolio mature every year for 10 years), you create a natural hedge against interest rate volatility. As each rung matures, the capital is reinvested at current market

rates. In 2026, this is particularly effective for managing “reinvestment risk” while ensuring a steady, predictable stream of cash flow.

- **3. Credit Selectivity over Broad Beta:** With corporate credit spreads sitting at historically tight levels, the mantra for 2026 is “Selectivity, not Caution.” Rather than buying a broad high-yield index, managers are moving into Structured Credit, such as investment-grade Collateralized Loan Obligations (CLOs) and Asset-Backed Securities (ABS). These often offer a “yield pickup” (higher returns) over standard corporate bonds with similar credit ratings. The goal is to avoid “zombie” companies that are struggling with higher refinancing costs.

THE SILENT KILLER: Why Making More Money Isn't Saving You

You just landed the promotion. Or maybe you finally hit that sales commission tier you’ve been chasing for months. You feel rich—for about three weeks. Then, suddenly, the “new” income feels like the “old” income. This is Lifestyle Creep, and it is the primary reason why even high-earners end up living paycheck to paycheck.

The “New Normal” Trap

Lifestyle creep happens because humans are experts at hedonic adaptation. We get used to “better” very quickly. That \$15 salad used to be a treat; now it’s just Tuesday lunch. That \$80 gym membership used to be a luxury; now it’s a necessity. The problem? If your expenses grow at the same rate as your income, your Net Worth remains \$0 (or worse).

How to Kill the Creep (Before it Kills Your Retirement)

1. **The 50% Raise Rule:** Next time you get a raise or a bonus, don’t spend it all, but don’t save it all either. 50% goes to “Future You” (investments/debt) and 50% goes to “Present You” (lifestyle upgrades).
2. **Audit Your “Ghost” Subscriptions:** Once a quarter, look at your bank statement. If you haven’t used a service in 30 days, cancel it. You can always sign up again later.
3. **Value-Based Spending:** Stop spending money on things you think you “should” have as a successful professional. Wealth is built by being frugal on the things that don’t matter so you can be extravagant on the things that do.

The Bottom Line: A bigger paycheck is a tool, not a trophy. If you don’t give that extra money a job (like buying your future freedom), it will find a way to disappear into the “noise” of daily life.

Final Thought: True wealth isn’t about what you buy; it’s about the number of days you could live without a paycheck. How many days did you add to your “freedom fund” this month?

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