

PRICE VALUE PARTNERS

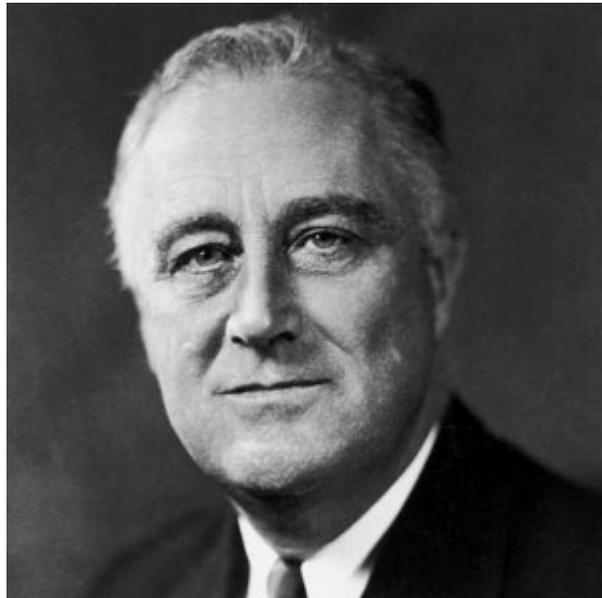
Everyone has a number

“New President Assures Nation,

‘The Only Thing We Have to Fear is a Crippling, Decade-Long Depression’

‘All is Lost,’ Says 32nd President in Address to Nation

America Doomed



- From ‘Our Dumb Century: 100 years of headlines from America’s finest news source’, The Onion.

“Although the institutions of our culture are so amazingly good that they have been able to manage stability in the face of rapid change for hundreds of years, the knowledge of what it takes to keep civilization stable in the face of rapidly increasing knowledge is not very widespread. In fact, severe misconceptions about several aspects of it are common among political leaders, educated people, and society at large. We’re like people on a huge, well-designed submarine, which has all sorts of lifesaving devices built in, who don’t know they’re

in a submarine. They think they're in a motorboat, and they're going to open all the hatches because they want to have a nicer view."

- David Deutsch, quoted by Dominic Cummings in his piece, '[The most secure bio-labs routinely make errors that could cause a global pandemic & are about to re-start experiments on pathogens engineered to make them mammalian-airborne-transmissible](#)', 4.3.2019.

"If you're going to panic, panic early."

- Anon.

As we wrote on 6th February ('[Bless you !](#)'), Jim Rickards has an intriguing thought experiment that touches on the same 'cave brain' behaviour as the new Covid-19 / coronavirus does. Imagine you were in a hotel ballroom with 500 other people:

How would **you** react, for example, if you happened to be there, and then suddenly one member of the audience suddenly shot up out of his or her seat and bolted for the exit, without explanation ? Probably you would be intrigued by this development – but you would perhaps be unlikely to act upon it. So how would you react if **ten** people then suddenly shot out of their seats, without warning, and dashed to leave the room ? Chances are, **you'd start to think about joining them, even though you had no idea why they were acting that way**. Everybody will have a number (of people suddenly leaving) that will cause them to join in the exodus, and that number will probably be somewhere between one and fifty, say – but it will likely not be the full 500.

Everyone has a number – but everybody's number is probably different.

As Morgan Housel [points out](#), there's a Chinese variation on the hotel ballroom experiment, 'Three Men Make a Tiger'. People will believe anything if they hear it from enough people. A Chinese proverb holds that if one person tells you there's a tiger on the loose, it's safe to assume they're lying. If two people tell you, it makes sense to keep an open mind on the issue. If three people warn you, you'll probably believe them, and start to panic a little.

Human-beings-as-investors are not evolutionarily well equipped to cope with surprises. While homo sapiens has been knocking around for roughly 200,000 years, modern stock markets as we understand them have only been around for a few centuries, which in evolutionary time is obviously no time at all. Nor are those same stock markets as rational or forward-thinking as we are sometimes led to believe. Harris Kupperman makes the analogy with [the run-up to the Great War](#):

A few years back, I read an incredible white paper regarding investor complacency in the final weeks leading up to the First World War. Archduke Ferdinand was

assassinated, global powers were trading demands, with the threat of war and investors didn't care. As the crisis heated up and the armies began to mobilize, investors still were in a fantasy world. Back then, bonds were the primary liquid investor product and a potential war would weaken a government's ability to redeem the bonds in gold—hence bond prices would collapse if there was a war. Four days before the war started, with armies mobilizing, outside of a few basis-point move in Austria, no one feared a crisis. Why were investors so complacent? There are plenty of reasons; there hadn't been a European war in their lifetimes, economic conditions were reasonably robust and everyone trusted the politicians to sort things out.

Table 1. Selected Financial Indicators, June–July 1914

Date	Government bond yields (percent a year)					Interest on commercial bills, first-class (percent a year)	Three-month-forward exchange rates (currency units per pound sterling, January 7 = 100)				
	U.K., 2.5% consols	France, 3% rentes	Russia, 5% of 1822	Austria, 4%	Germany, 3% of 1891		Paris	St. Petersburg	Vienna	Berlin	New York
June 5	3.38	3.49	4.13	4.71	3.90	2%	100.01	101.23	100.10	101.21	100.41
June 12	3.39	3.49	4.13	4.82	3.90	2%	100.05	101.23	100.10	101.18	100.49
June 19	3.34	3.55	4.13	4.82	3.90	2%	100.01	101.23	100.10	101.14	100.54
June 26	3.33	3.59	4.13	4.71	3.90	2%	100.03	101.09	100.23	101.09	100.39
July 3	3.31	3.58	4.13	4.65	3.90	1%	99.89	100.90	100.23	101.15	100.72
July 10	3.30	3.62	4.13	4.65	3.92	2	100.03	100.97	100.15	101.21	100.21
July 17	3.29	3.62	4.13	4.94	3.92	2%	99.95	100.40	100.15	101.16	100.21
July 24	3.33	3.69	4.13	5.00	3.95	2%	100.01	101.47	100.42	101.23	100.21
July 31	3.55	3.64	4.24	5.13	4.11	5	98.5	n.a.	n.a.	n.a.	n.a.

Source: *The Economist*.

I bring this all up as I sense a similar complacency surrounding the Coronavirus. Let me start by saying that I'm not a medical professional—I didn't even get good grades in high-school biology. I have read my fair share of information by "so-called experts" but am well-aware that at this stage, most of what's out there is just a bunch of theories using faulty Chinese data to arrive at a best guess for what will happen. Given the range of possible outcomes I have read, it is clear that there is absolutely zero consensus as to what will happen.

If diverging opinions on what will happen amongst "experts" sounds a lot like analyzing the stock market where the "experts" are also mostly wrong, then you're paying attention to the potential for outlier events. With this virus, you need to gather your own information, understand it as best as possible and then try to reach an actionable hypothesis based on the fast-moving information.

Chris MacIntosh highlights the potential for a global breakdown of trust:

Elsewhere in the world the zeitgeist is decidedly untrusting. The US hasn't been so politically polarized in my lifetime. The EU...pfff well we've just seen Boris Johnson explain in detail why the Brits don't see eye to eye with their neighbours.

The point is this. Distrust is massively elevated. What else?

The impact, at this point, on the global economy will be felt. No question. In China, it will be most acute. What will the PBOC do?

The same thing they've been doing every time they become concerned their magic 6% GDP print looked to be in jeopardy. Expand the PBOC balance sheet. But, unlike the west, they'll do what they have been doing. Spend it on fiscal policies.

What about the west?

Good question. Well, the inevitable economic impact itself will mean that millennial "non-binary tri-gender fluid" will lose their job making coffees at Starbucks and be unable to afford imported avocados and you know what that means don't you? They'll blame it on billionaires. The economic downturn will pit these already antagonistic forces against one another.

The billionaires don't trust the millennials – because they're threatening to take away their jets. And then, there is the average Joe, who trusts neither the billionaires (because they're doing sweetheart deals with the government...yes, you, Bezos) nor the green-haired girl...or is it a boy – (hard to tell) who is screeching about ice caps melting and hollering something or other about the polar bears. So there is bugger all unity because there is bugger all trust.

The question is – What do you want to own in a world that – dare I say it – feels rather combustibile at this point?

A world where trust is evaporating like common sense at an Extinction rebellion convention?

Distrust is the reason to own gold. And not because some bearded old fart is trying to sell you on the idea but because when you can trust little else, certain assets become relatively more interesting to investors than others..



Source: [Capitalist Exploits](#)

So we own gold, but then we always have – at least since the central banks of the world decided collectively to try and destroy the purchasing power of their various currencies. The gold price will probably get an unsustainable short-term bump from coronavirus jitters but we're in it for the long haul – those yet to invest in the yellow metal will probably want to average in from here.

And we own **more** portfolio insurance in the form of systematic trend-following managers – where a particularly appealing characteristic is their lack of correlation both to stocks and (utterly unsustainably priced) bonds.

Which takes us to the equity market. Electing to sell on the back of other people's panic isn't much of a strategy – and it raises the doubly thorny question of when to get back in. We have no direct exposure to China – nor do we want any – and we don't intend to be bounced out of stocks that are already inexpensive; more likely, we'll be buying more if the market puts them on sale.

Before you hit the panic button, it's worth analysing why. Deciding to sell the shares of certain companies because their earnings are likely to take a hit from the impact of a sustained coronavirus pandemic makes a certain amount of sense. Deciding to sell equities simply because other people are doing so, not so much. Terror is not the best investment counsellor.

Tim Price is co-manager of the [VT Price Value Portfolio](#) and author of 'Investing through the Looking Glass: a rational guide to irrational financial markets'. You can access a full archive of these weekly investment commentaries [here](#). You can access the archive of our regular 'State of the Markets' podcasts, with Paul Rodriguez of ThinkTrading.com, [here](#).

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