PRICE VALUE PARTNERS

Panic on the streets of London

"Interesting how no one would even think to describe medical doctors as naysayers for making diagnoses w/bad outcomes but as soon as an investment professional identifies a bubble or a coming systemic crisis, he/she gets branded as a doom and gloom type."

- Tweet by Simon Mikhailovich (S_Mikhailovich), 15 November 2019.

"There's a growing panic in Fed headquarters not only about the inability of policy to improve the economy, but over the fact that the board members don't even know what policy to pursue. It's one thing to say the "right" policy isn't working. It's quite another to realize the Fed doesn't even know what the right policy is.

"At some point panic sets in.

"This is not about panic in the markets. That will come soon enough. It's about panic among policymakers overwhelmed by forces they don't understand and cannot control..

"The Fed is in complete disarray. There's no intellectual coherence and no consensus on policy. That's not surprising because the Fed's models are badly flawed.

"The importance of these minutes is not the policy decision but the light they shine on the Fed's own confusion. Some Fed members want to cut a little, some want to cut a lot and some don't want to cut at all. They are already contemplating what to do when the Fed hits the zero bound:

"More QE ? Negative rates ? Both ?"

- Jim Rickards, 'The Fed has never been more divided', 8 October 2019.

"Looking forward to Corbyn vs Johnson in the same way I'd savour the two strangest kids at school having a punch-up."

- Tweet by Geoff Norcott (@GeoffNorcott), 19 November 2019.

A couple of thoughts strike the bemused, slightly appalled, observer of ITV's leaders' debate (19 November 2019) between Boris Johnson and Jeremy Corbyn. One is that the producers at ITV don't appear capable of running an orgy in a brothel. One is that at the highest level of political engagement in Britain today, you can expect to see weird experiments that may transgress the laws of thermodynamics, in that it is possible for supposed political leaders to generate almost infinite amounts of heat without any apparent light. Viewers to this lightweight bout without contact were "treated" to a continuation of the largely pointless political polarisation and tribalisation that has transfixed the country for the past three years and counting. Another is that neither Messrs Johnson nor Corbyn appear remotely concerned – or their spin doctors have advised them not to broach the topic with a bargepole – that we may all (i.e. the developed world) be collectively hurtling towards a bigger economic crisis than anything to do with either Brexit or accidental Marxism combined. The out-of-control spending pledge bidding war that has recently intensified between the major parties is both the absurd cause and grotesque symptom of the malaise.

During the first Gulf War, a US general was being interviewed by one of the news networks. The pounding of Baghdad by US forces seemed – to the casual observer, at least – somewhat, let us say, one-sided. "General, aren't you in danger of running out of targets ?" The response, when it came after a brief pause, was somewhat laconic. "No Sir, this is a very target-rich environment."

One feels the same way today about potential threats to the global investor's well-being. Put aside the risks associated with Brexit, or an accidental Corbyn government, or the messy stand-off between the US and China, increasingly on everything. Whereas the great value investor Peter Cundill once remarked, in a more positive light, that there was always something to do, from the vantage point of late 2019 it feels like there is always something to be petrified about. From an evolutionary perspective, it makes sense to have at least some concerns about potential threats. Our ancient forebears who had no qualms about leaping over cliffs, sight unseen, or taking on unusual noises in the dark, likely left little genetic legacy. But knowing just how many known or unknown unknowns we should fear can be tiring. The news cycle is a demanding mistress; ditto the infotainment industry supercharged by social media. The institutional investor Tony Deden has written well of the psychodrama that comes from attempting to surf the data and opinion Niagara:

> Daily, my mail box is full of emails, many of which come from well-meaning friends. 'Have you seen this article?' or 'Do you know this guru?' I follow the links as I frantically go from thenewyorktimes.com to financialarmageddon.com and everywhere in between. 'The dollar will rebound', 'Gold is another bubble', 'Buy bonds', 'Sell bonds', 'Pork bellies are undervalued', and so on. I pretend to read some of these writings just so that I can make up something to say should they follow up the email with a telephone call. In an enduring quest for understanding and picking kernels of knowledge, I find myself surrounded in an epochal – and mad – battle of the optimists versus the pessimists.

> Honestly, there are intractable and momentous problems which should be the cause of considerable pessimism. But when it comes to action with other people's money – particularly the irreplaceable kind – merely on account of the free advice of a well-known guru who writes for the-world-is-coming-to-an-end.com is complete madness. To follow the advice of an analyst working for a bank that can't even manage its own balance sheet and who is intentionally or accidentally divorced from reality, is madness squared.

The author Yuval Noah Harari, in *Sapiens*, highlighted the extent to which we are suckers for narrative. We are just as easily seduced by determined optimism, a topic embraced by Barbara Ehrenreich in her study *Bright-Sided: How the Relentless Promotion of Positive Thinking has Undermined America*. When relentless optimism mates with financial markets, the result is almost always a disaster.

And yet over the very long run, being optimistic about the markets has tended to be the right thing to do. Not for nothing is the Dimson, Staunton, Marsh study of the last century of stock market returns titled *Triumph of the Optimists*.

So what's our specific beef ? Since 2008 (if not long before), we have been increasingly concerned that central bankers throughout the world have given every indication that they haven't got a clue what they're doing. As John Maynard Keynes wrote, in his essay 'The Great Slump of 1930',

> We have involved ourselves in a colossal muddle.. having blundered in the control of a delicate machine, the working of which we do not understand. The result is that our possibilities of wealth may run to waste for a time – perhaps for a long time.

But Keynes was only half-right, if that. The Great Depression would certainly run on for the best part of a decade. Generations of schoolchildren have been taught that FDR was then parachuted in and that his 'New Deal' saved the day. Perhaps. Or perhaps the Second World War stepped in and lifted the US out of its slump – at the cost of tens of millions of lives.

More to the point, Keynes' metaphor of economy-as-machine was never remotely true. As the classical or Austrian economists were among the first to appreciate, the economy is not a machine that rigidly obeys simple commands and obediently responds to the pull of specific levers. The economy is ***us***. More relevant still, government is not the font of all wealth. It is not even the font of any wealth. Governments merely redistribute (and tax and spend). Wealth is created by entrepreneurs. Leaders' debaters, and Mr. Corbyn, please note.

But weird things happen at and below the zero lower bound, when interest rates reach and then break below zero. Zombie companies with unlimited access to free money deflationarily crowd out the more productive efforts of genuine entrepreneurial risk-taking. WeWork founders retire at 40 as billionaires. Crapitalism™ ensures the survival of bankrupt banks. Terrified elderly workers in the euro zone, seeing the destruction of their precious and irreplaceable pension capital by negative interest rates, elect to save ***even more***. As Captain Smith remarks to the shipbuilder Thomas Andrews in 'A Night to Remember', as RMS Titanic slowly sinks beneath the waves, with 2,200 souls on board and room on the lifeboats for only 1,200,

I don't think the Board of Trade regulations ever visualized this situation. Do you ?

So, how can we invest sensibly without being left to the tender mercies of vulnerability to market-timing ? By being always more or less fully invested, but across a broad array of sensibly priced assets offering multiple, discrete, uncorrelated potential return streams. In other words, we place our irreplaceable client capital as best we can. We invest in what we consider only the most secure forms of listed equity, namely businesses run by principled, shareholder-friendly owner-managers who are also superb allocators of capital, and even then only when the shares of those businesses can be purchased at a discount, or no great premium, to their inherent worth. We then supplement those holdings in our managed accounts with uncorrelated vehicles (systematic trend-following funds) which offer the potential for both decent gains as well as portfolio protection in the event of pronounced market shocks. We then double down on portfolio-, inflation- and crisis-protection by means of the monetary metals, gold and silver, which can't be magicked into being by bewildered central bankers but which have been stores of value for thousands of years. As the song says, there may be trouble ahead. But if it does make sense to panic, panic early.

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