

36 South Views

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Christmas at the Potemkin village

The end of 2020 approaches and whilst I am old enough to know better than to wish away time, I cannot wait for 2021!

I should be more grateful, we had the volatility event that long volatility managers dream of and managed to keep most of the resultant performance in spite of the V-shaped recovery. But my euphoria is cramped by the high toll of misery this year in the real economy whilst the financial economy rides the wave of central bank largesse.

Yet curiously, this is not the source of my disquiet.

I feel "gaslighted" ...

The term originates in the systematic psychological manipulation of a victim by her husband in the 1938 stage play Gaslight, known as Angel Street in the United States, and the film adaptations released in 1940 and 1944¹

...by central bankers and governments. Price and volatility are no longer instruments of truth for efficient allocation of capital but instruments of state.

By economists who purvey the old/new theory of "be a locust not an ant".

By equity markets driven predominantly by retail investors armed with helicopter money buying mostly call options and driving equity prices to nosebleed levels.

By investors flocking to identically correlated passive portfolios thus raising the liquidity risk to alarming levels.

By Greek bonds trading richer than US bonds rendering comparative analysis impossible.

By fake news and sociopathic utterances from political leaders, replacing truth with whatever "narrative" suits them.

Am I being gaslighted and going slowly crazy or is our current reality "unreal"?

Are we in a "far from equilibrium" situation as Soros describes or will monetary inflation render current prices rational from hindsight?

I have to assume that I am not going crazy so I wonder how far we are straying from the reality and if we are, is a tail event the only thing to get us back? Unfortunately, the answer is ...probably.

Either a left tail event, a black, grey or white swan which suddenly drives market perception like Covid-19 did, or a right tail event where either financial assets continue their meteoric rise, or in the real economy where inflation reappears which is certainly feasible given the depreciating US dollar combined with huge monetary stimulus amongst other things.

Either way, the economic status quo is fragile and there is a strong valence for rapidly changing perceptions in the year ahead.

¹en.wikipedia.org/wiki/Gaslighting

Hence, I fully expect another volatility event next year, as there is just too many nitro-glycerine packed stagecoaches running through Dodge i.e. multiple risks vectors.

Looking back at 2020, our Funds have performed superbly and clients who have us in their portfolio not only have done well in their traditional portfolios, they get extra performance from us via capturing volatility drag.

Whilst “all is quiet on the Western Front”, it just remains to wish our clients an enjoyable safe festive season. We appreciate your custom and look forward to serving you well for many years to come.

Disclosure

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