

36 South Views

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By George!

The reality is that financial markets are self-destabilising; occasionally they tend toward disequilibrium, not equilibrium.

George Soros

Frothy is the way I would describe asset prices around the world. Most people cannot afford anything worthwhile without going into debt. E.g. mortgages, margin buying of equities.

Doing that requires divorcing reason from judgement and diving in, fingers crossed.

Bitcoin's meteoric rise, which looks increasingly similar to the tulip mania of 400 years ago, is attracting mainstream punters including the 'blue rinse brigade'. Is it a bubble? Undoubtedly. It had the advantage that there was NEVER any value in the first place from which to price it, therefore no logic is required to buy it - at any price. Can it go up 100x more? Yes. Will the price be lower in 5 years than it is today? Probably.

But bitcoin is just the latest in a series of asset bubbles being blown – asset price inflation.

Why? Central bank reflation strategies – keeping interest rates low, buying assets with freshly printed money.

Is this good?

Yes it was good to stop a 2008 meltdown but they seem to have overshot the runway and now the unintended consequences are coming home to roost, i.e. wealth inequality is increasing (because asset price inflation favours the people who have assets!)

It is starting to feed into the real economy but in the form of price not wage inflation. People without assets are getting even poorer.

I see tremendous imbalance in the world. A very uneven playing field, which has gotten tilted very badly. I consider it unstable. At the same time, I don't exactly see what is going to reverse it.

George Soros

The central banks have started this; they have to end it. They can either be slow to raise interest rates in the face of massive asset price inflation, risking bigger and bigger bubbles with concomitant consequences or they can raise quickly, throwing all asset markets into immediate reverse.

Markets are constantly in a state of uncertainty and flux and money is made by discounting the obvious and betting on the unexpected.

George Soros

The unexpected is an unpredictable rise in interest rates followed by a fall in equity prices, the risk parity blow-up party. The scenario most asset managers fear and have done nothing about.

The financial markets generally are unpredictable. So that one has to have different scenarios... The idea that you can actually predict what's going to happen contradicts my way of looking at the market.

George Soros

It is true that we don't know what is going to happen but my knee is starting to twitch. I see middle class families on good incomes battling to keep their standard of living. I see poorer people worse off than that wondering how the hell they are going to get through the month. Against this backdrop Bezos and friends make billions in one day's movement in the stock market. Call me sentimental but envy is a bigger emotion than love.

Once we realise that imperfect understanding is the human condition there is no shame in being wrong, only in failing to correct our mistakes.

George Soros

My two cents worth is that interest rates need to stabilise toward their natural rate, asset markets need to deflate, property prices need to revise massively downward to become more affordable and we need a big reset to awaken from this drunken debt orgy we have participated in for the last 30 years.

The worse a situation becomes, the less it takes to turn it around, and the bigger the upside.

George Soros

Would central banks consider this? No one wants to be the one to say that the emperor has no clothes. I therefore doubt it, but it could be taken out of their hands.

The hardest thing to judge is what level of risk is safe.

George Soros

All investors, in a search for yield, have assumed too much risk. The bear always presses the basement button when the lift is full of unwary investors!

Nowhere is this more prevalent than in the options market. Everybody is selling options to get yield without due regard to the risk. It is creating a perfect storm of opportunity for option buyers at some date in the future.

"When you sell options, you get paid for assuming risk. That can be a profitable business, but it does not mix well with the risks inherent in a leveraged portfolio."

George Soros

As a long volatility fund manager, our patience is being tested. Every day the likelihood of an avalanche increases and every day the price of avalanche insurance goes down!

The day of reckoning is coming...

If I had to sum up my practical skills, I would use one word: survival. And operating a hedge fund utilized my training in survival to the fullest.

George Soros

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