36 South Views

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Oink oink flap flap

Yes, pigs can fly.

Radio stocks soared in the 20's.
Tv stocks in the 50's.
Internet stocks in the 90's and AI stocks in the 2020's.

Mmm roughly 30 years between each …. interesting

But it's different this time …. maybe…

So how do you invest in a potentially dangerously overhyped market?

There are four ways:

1) All in and devil may care - this is classic running with the bulls and a lot of professional money managers do it because it severely limits their career risk by being wrong footed in a bull market.

2) All out of equities - cash, bonds and real assets like gold/crypto.

3) Reduced equity exposure - this limits the losses on the downside and upside.

4) Stay risk on but increase the tail hedge - this allows an investor to stay in risk assets but decreases the consequences of being wrong.

Each strategy has its pros and cons.

The first one is good if indeed this time is different. One is at most risk of permanent impairment of capital though. If we have a Japanese style bear market which lasts thirty years you have lost a lot …mainly due to a loss of compounding time. Professional managers get carried out in a proper bear market but use the "who knew" defence to keep their jobs and bonuses.

The second one is good in a bear market obviously …one is out of the market. One can massively underperform a big bull market though.

Warren Buffet, for example, has been pursuing strategy 3 for the past couple of years. He owns 5% of the US t bill market. He is waiting for the blood to be flowing on the streets before he reinvests heavily.

With regard to strategy 4, increasing the tail hedge works because volatility (the price of hedging) is normally at or near its lows when prices are at their highs.

"Upon such a sea are we now afloat, and we must take the current when it serves, or lose our ventures" said Brutus (quote from Shakespeare's play Julius Caesar).

I feel that, whilst a bull market looks set to continue, the probability that a long-dated tail hedge pays off is rising substantially.

Fear is absent from the equity market which is a good tell that we are a lot closer to a top than the market thinks.

In 2009, there was a total absence of optimism which was the other side of the coin and a good tell that the bottom was in.