CANARIES IN THE COAL MINE

I would really feel much happier to be writing our next fortnightly commentary, rather than this one.

As of now it would be simple, "Following the expected Biden win, and a tight Senate race, the Democrats have a clear mandate. However, the euphoria that victory created, including a market buoyed by its long desired additional stimulus package, has failed to disguise the deep underlying economic and health crisis. The market in the meantime still senses instability with the same elevated readings on the VIX that have been apparent all summer."

In other words, everything will have changed, but nothing has changed. It seems far easier to do that piece, than trying to trade the forthcoming febrile run into the US election and a new COVID wave.

An old-fashioned economic recession

Still, we are in this week. The conundrum is, and here the US is really not alone, much as it sometimes feels otherwise, that the only real weapon global governments have against COVID is to press the self-destruct button on their own economies. Having tried that once, in the spring, they both know it works (for a while) and also that the impact was disastrous, and they simply can't hit that terrible red button twice.

So, we are all merrily sliding down the cliff into a natural disaster which we are effectively powerless to prevent. Indeed it comes with the added twist that all the excuses for staving off the inevitable and all the poisonous political blame games and all the potent belief in the all-conquering power of science, are just masking what looks like an old fashioned pretty awful flu season. Medical treatments are at least better and indeed better organized, so it will be much less deadly than the first wave, a mercy to be thankful for.

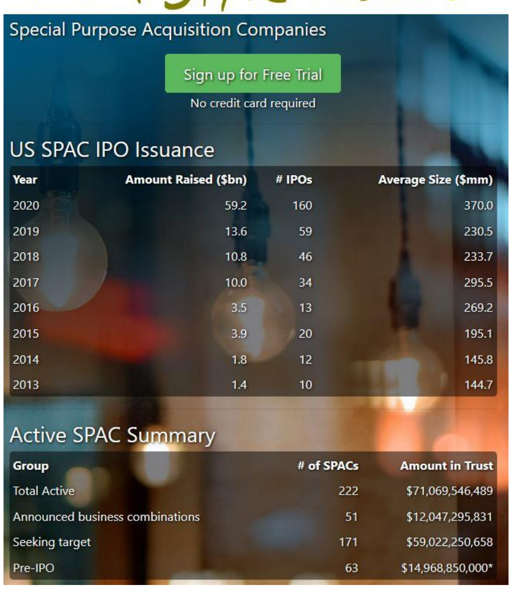
Well, I can't say it will be fun, and I am sorry we seem, still, to believe that all will be much better if we stop drinking and dancing, ban sports and keep the foreigners out (all good traditional Calvinist responses). Even those perceived moral failings, once rectified or banned, will sadly not stave off the punishment, but it somehow seems people feel better about it all with those restrictions. If we are not going to have fun, no one else should either.

So, is it business as usual? I think for the real economy it is, yes we have too much capacity and some of it must now go, and too many inputs, be it oil or labour, and that must be repriced or eliminated, where demand has plummeted. So, the residual questions are all now about managing those transitions and providing welfare. They no longer appear to be financial issues.

The return of the 'shell' company

Although one thing at least in terms of asset prices that does look really bad, is the spate of SPACS (Special Purpose Acquisition Companies)- true harbingers of an equity market top. You might recall centuries ago when bubbles had non-medical meanings, the raising of enormous amounts of money "for a purpose yet to be established" – what we used to call shell companies or blind pools are exactly that.

From SPAC Research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US SPAC IPO Issuance

Year	Amount Raised ($bn)	# IPOs	Average Size ($mm)
2020	59.2	160	370.0
2019	13.6	59	230.5
2018	10.8	46	233.7
2017	10.0	34	295.5
2016	3.5	13	269.2
2015	3.9	20	195.1
2014	1.8	12	145.8
2013	1.4	10	144.7

Active SPAC Summary

Group	# of SPACs	Amount in Trust
Total Active	222	$71,069,546,489
Announced business combinations	51	$12,047,295,831
Seeking target	171	$59,022,250,658
Pre-IPO	63	$14,968,850,000*

Both the size of these and the money raised, shown to the left, show a remorseless rise, with that little 2016-2018 plateau, before a blow out in 2020. It means the supply of money has become so inflated, that otherwise sensible folk will write blank cheques, to any plausible promoter, who after taking off a healthy slice themselves, will find something to stuff the rest into.

Now, we naturally get the pious explanations, the sudden, inexplicable presence of numerous "oven ready" virtual "dead certs" as business propositions, which just happened not to have made it to market (or made a profit) as yet, and for some technical (and really much too complicated for mere investors to fathom, reason), can't be floated through a normal capital raising process.

So conveniently a blind pool meets an unsighted investor and off they go to milk the unsuspecting punters together.

We also learnt (again) how good sales executives are at evading internal controls. With the Goldman Sachs compliance team explaining on record (and as revealed by the DoJ this week) that the IMDB Malaysian scam was something they would and should never touch. That bit went well. When big ticket banking revenue is on offer these things somehow just find a way onto the books.

Well of course “it will be different this time” is the eternal cry. But those SPACS tell me otherwise and that far smarter people than I have called a top. Smaller fry, like us, should be very careful when these games start, as we have noted before, when elephants dance the grass gets trampled.

What it also shows is that however much cash is flowing, many US investors simply will not touch European and Emerging Market stocks. Although, as ever the currency is a subtle counterbalance, as someone somewhere is also clearly selling an awful lot of dollars too.

So we have a nasty mix, health, economics, politics, winter, all scream caution, but against that the world’s most influential and widely held stock index just won’t give in, as all the excess liquidity unleashed to buy an election, pushes prices ever higher.

None of that makes us want to be too long into Christmas, indeed tucking away some of the year’s gain, if you are lucky enough to have held assets that have appreciated in value, is already rather tempting.

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