MEDALLION WEALTH MANAGEMENT

April 2021 Mid-quarter Market Commentary

Crazy Train

"Crazy, but that's how it goes
I've listened to preachers
I've listened to fools
I've watched all the dropouts
Who make their own rules…"
-Ozzy Osbourne

https://www.youtube.com/watch?v=FVovq9TGBw0

The image above is from the cover of New York magazine, and it speaks volumes about our current markets. If you find it all a little crazy you're not alone. This has certainly been a difficult time to be a financial professional, someone who's studied and worked in the industry for decades, as we watch in disbelief as segments of the market are *"going off the rails on a crazy train."*

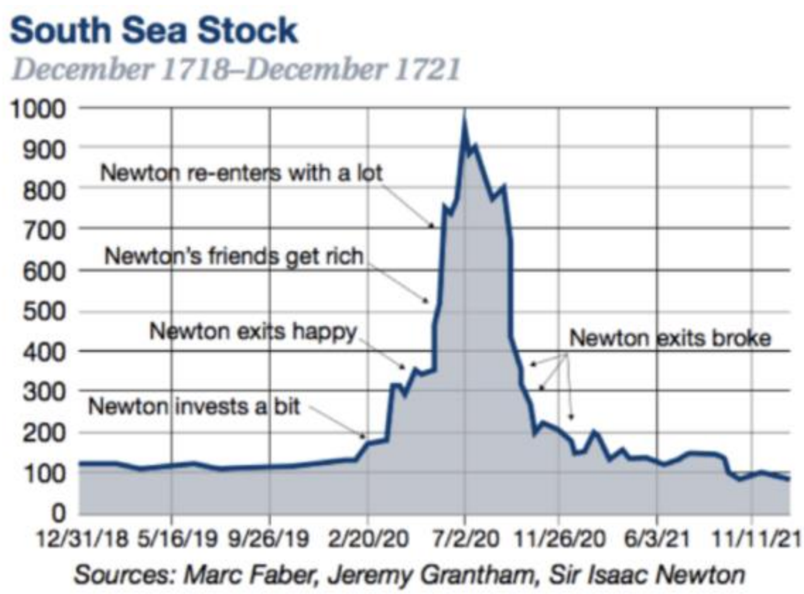
A relative wants to know what an NFT is and should they buy one? An NFT is a "non-fungible token", which essentially is a digital asset whose uniqueness, and therefore its value, is stored cryptographically on the digital ledger known as blockchain. Beeple, a millennial artist making animated-GIF NFTs is selling them for tens of millions of dollars.

Friends of children want to know if they should buy GME or AMC (GameStop and theater chain AMC), two of the hottest "meme stocks", a.k.a. "Stonks"? These stocks were nearly dead when they caught the interest of the Reddit crowd and were bid to inexplicably high prices that had absolutely nothing to do with fundamentals.

A friend wants to know what a SPAC is, and why is the company he works for thinking about merging with one? A SPAC is a "special-purpose acquisition company", a shell corporation created to go out and buy a private company so it can go public without the scrutiny of a traditional IPO. Celebrity venture capital investors, as well as just plain old celebrities like Shaq, Steph Curry, and Serena Williams, have started SPACs hoping to find a good private company to take public.

While much of this sounds strangely futuristic, computer dollars buying cyber art on a digital marketplace, the basic dynamic at work here is totally recognizable. There are a lot of suckers who want to get rich fast without a lot of work. This story is as old as time. An excellent investment book that was first published in 1841, ***"Extraordinary Popular Delusions and the Madness of Crowds"*** by Charles Mackay vividly chronicles some of man's earliest financial manias, such as the Dutch tulip mania, the South Sea Company, and the Mississippi Company bubbles. Mackay states, ***"every age has its peculiar folly; some scheme, project, or fantasy into which it plunges, spurred on by the love of gain, the necessity of excitement, or the mere force of imitation."*** Kind of resonates.

A great story from this time period is the rise and fall of Sir Isaac Newton's fortune. *Back in the spring of 1720, Sir Isaac Newton owned shares in the South Sea Company, the hottest stock in England. Sensing that the market was getting out of hand, the great physicist muttered that he '**could calculate the motions of the heavenly bodies, but not the madness of the people**.' Newton dumped his South Sea shares, pocketing a 100% profit totaling £7,000. But just months later, swept up in the wild enthusiasm of the market, Newton jumped back in at a much higher price — and lost £20,000 (or more than $3 million in [2002-2003's] money. For the rest of his life, he forbade anyone to speak the words 'South Sea' in his presence.*



Last week Coinbase (COIN), a new exchange where crypto-currencies are traded, went public at a market capitalization of about $86 billion. This compares quite favorably to the market capitalization of Intercontinental Exchange (ICE), the parent company of the New York Stock Exchange as well as 12 other exchanges and marketplaces, which after 229 years of operation has a valuation of $68 billion.

How can we explain what is happening? While a lot of the craziness in today's markets can be traced back to the beginning of capitalism and man's simple greed, self-interest, and inherent desire to improve his circumstances; another aspect of this frothiness is the abundance of fuel from the Fed and Treasury, specifically in the form of zero interest rates and actual free money from the government. But there also appears to be something deeper: the beginning of a fundamental shift in how we think about money.

Money has always been a way of figuring out what kind of life you could lead, dictating where you lived, what you drove, where your kids went to school, even how much free time you could afford. Money was a scarce and precious resource, and we were told that in order to acquire more of it we needed to work hard, save, and live prudently.

This all changed in 2009, when then Fed Chairman Ben Bernanke appeared on 60 Minutes and grinned when asked if all the money going to bail out the banks was tax-payer money. He shook his head and said, "To lend to a bank, we simply use the computer to mark up the size of the account that they have with the Fed." Presto, money out of thin air.

In the years since the financial crisis, our views of money have morphed. New theories (Modern Monetary Theory MMT) and crypto-currencies have emerged. These new theories promise an abundant future of lavish spending and full employment. As the pandemic hit, both liberals and conservatives bought into the idea that drastic action needed to be taken. The Fed and Treasury offered to make direct payments to all citizens, $372 billion worth, and the politicians gleefully went along.

For the citizens this was all profoundly strange: Free money from the government? We don't have to pay it back? Why don't they just do this all the time? People bought food, paid rent, paid off debt, and even speculated in the markets. Why not, it's free!

Gone is the belief that money is a scarce, quasi-natural resource that needs to be earned, saved, and treated with some reverence. What is replacing it? I don't know. Some of it is crypto-currencies, and NFTs, while some will be an increased willingness by politicians to embrace the free money school of MMT, and some will be something new that maybe incorporates all of them.

Greed and fear are still alive and well, and investors need to be cognizant of not getting caught up in the latest popular delusion, but we also have to be aware of the fact that something bigger may be going on here that will change how we think about money.

"Mental wounds not healing
Who and what's to blame?
I'm going off the rails on a crazy train."

Be careful out there,

Chris Wiles, CFA