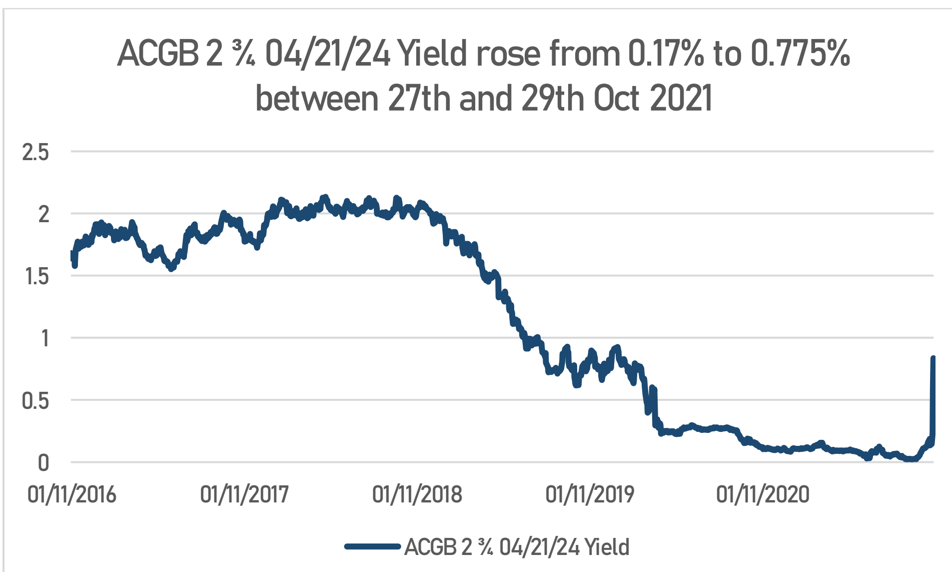
Rates Volatility, Renewable Craze & Forgotten Depression 1920-21

The last week saw one of the highest bond market volatility in years, as inflation fears stoked investors and central banks around the world to reconsider their highly accommodative stance. The 2yr Australian government bond, for example rose from 0.17% to 0.775% in just two days. The interest rate volatility should not be shrugged off, as market rumours hit the wires of some asset managers being liquidated amid volatility in interest rate derivatives. There are plenty of highly leveraged rates/RV hedge funds and while some of them should make money, the volatility will increase margins and those funds will need to liquidate positions quickly to provide more cash to the exchanges. Having worked at an RV hedge fund during the March 2020 crisis, these margin calls can be quite devastating and the volatility in rates markets suggests some funds may be liquidating already. The Fed could save these highly leveraged hedge funds back in March by buying assets and lowering rates, but can they do so in an environment where rates sell off rapidly? Surely, the treasury bond-future trade has come off and resulting high leverage is nowhere near where it was in 2020, but this is still something to watch out for…



Source: Bloomberg

In Monday's and Tuesday's UK Daily I outlined the UK's ten point plan towards net zero and questioned some of the points and how investors are currently pricing the renewable sector. Specifically, investors seem to overlook that oil demand and emissions have not peaked yet and emerging countries like India, Brazil, Nigeria and others will have much higher demand for coal and oil & gas. Specifically, the UK's Office for National Statistics is making generous assumptions on pricing for Electric Vehicles compared to combustion engine in 2030. Similar to faux meat, pricing will be the main trigger for switching to electric

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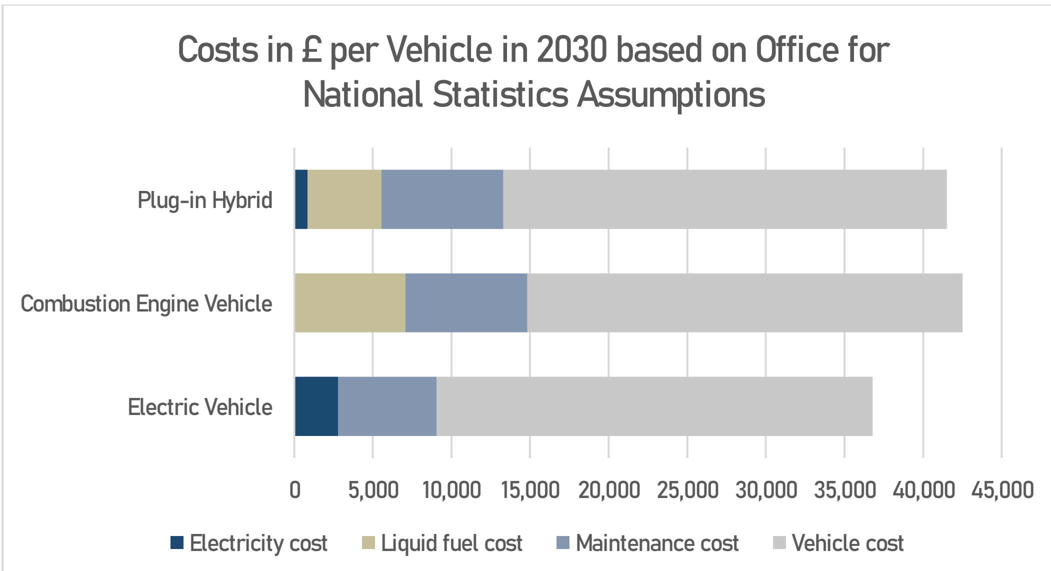
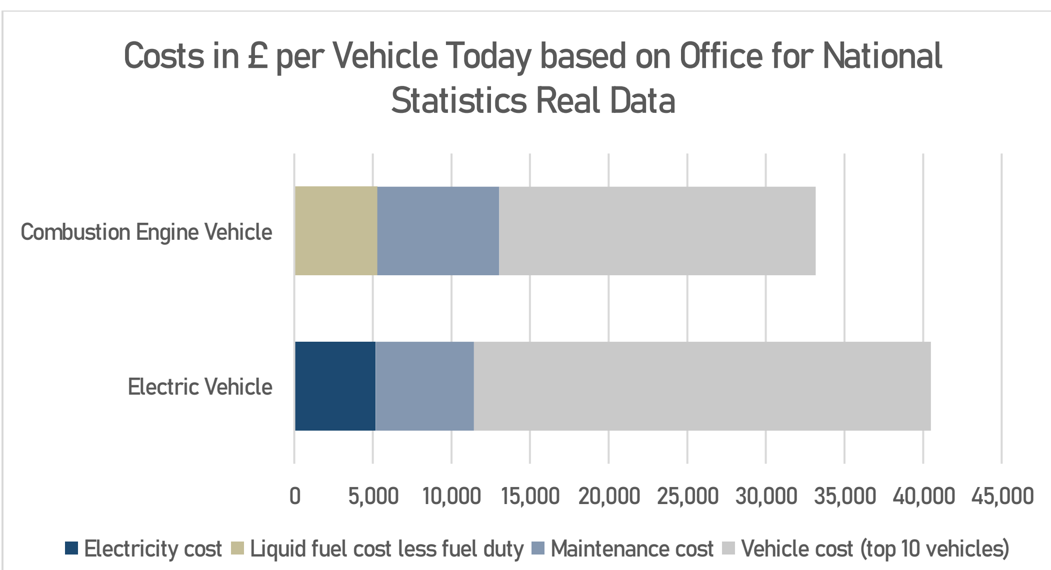
vehicles. Without having taking raw materials (nickel, copper) into the analysis, I do expect people to buy EVs in 2030 instead of combustion engine vehicles in Europe and maybe China and the US. But this is nine years ahead and with most people leasing a car for two years I think oil companies could be compared to tobacco companies in the year 2010. However, between 2010 and 2017 British American Tobacco's share price more than doubled, and this is why I believe oil firms will seal a similar destiny than tobacco firms, which means bullish over the next seven years at least.

*JOHNSON SAYS G-20 NET ZERO COMMITMENTS ARE TOO VAGUE



Source: Office for National Statistics



Source: Office for National Statistics

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Last but not least, below is an updated timeline of the run-up to the 1920/21 forgotten depression and the current environment. I continue to believe that using the 1920/21 forgotten depression as a template for the current market we are in is the right choice and would hence caution of what we might face in 2022. Therefore, monitoring any further similarities will remain key…

Influenza vs. Covid-19 waves

Influenza	**Covid-19**
1st wave: Early 1918	1st wave: Early 2020
2nd wave: Late 1918	2nd wave: Late 2020 (Alpha)
3rd wave: Early to mid-1919	3rd wave: Early & mid 2020 (Delta)
4th wave: Spring 2020	?

1918-20s vs. 2020-22s timeline

1918-1920 and beyond	**2020-2022**
1918: Lockdowns were introduced to curb the virus	2020/21: Lockdowns were introduced to curb the virus
1919: 1 in 5 American was striking to achieve higher wages	2021: Record number of people left their jobs, resulting in labour shortages
1919/early 1920: Inflationary boom with commodity prices reaching all-time highs	2021: Inflationary boom with commodity prices reaching all-time highs
November 1919: Stock market peak, just as the Federal Reserve hiked rates from 4% to 4.75% to fight inflation and speculators, stocks slumped 12.8%	November 2021: Fed expected to announce tapering. Central banks around the world turn hawkish
January 1920: Fed raises rates to 6%, stock market didn't react	
April 1920: A Tokyo bank defaulted, prices of rice, cotton and silk dropped quickly, GM shares dropped 8%	
1920: Consumers changed to non-inflationary living, buying used clothes	
Spring 1920: Consumers stopped buying cars, strong demand disappeared. GM sold 52,000 vehicles a month in early summer, 13,000 in November and only 6,150 in January 1921	
April 1920: Weather was cold, wet and caused wheat and other agricultural goods to spike in price, farmers started borrowing more, but then were facing huge losses in 1921	
April 1920: Steel Corporation had luxury of 10.4mio tons of unfilled orders. This backlog dwindled to 5.8mio tons from April 1920 to March 1921	
June 1920: Fed raises rates to 7%	
April 1922: Accumulated inventories were sold off for extremely low prices	

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Similarities between the two time periods

1918-20s	**2020-22s**
High inequality, with top 1% owning 12-19% of the total share of income	High inequality, with top 1% owning 30% of all household wealth
Combustion engine replaces horses	Electric vehicles set to replace combustion engine
High speculation with businesses borrowing excessively and individuals borrowing to buy stocks	High speculation with individuals investing in "no return" cryptocurrencies
Large backlogs	Large backlogs
Income tax and other taxes were set to be introduced	Global corporation tax is set to be introduced, taxes are increasing
World was in globalization mode, but faced headwinds with WW I	Globalization continues, but faces headwinds with China desiring to become a world power
World leader had excessive debt/GDP of over 130% (England)	World leader had excessive debt/GDP of over 120% (USA)
"*On the way up, inventory accumulation had contributed to the panicky sense that the world was running out of everything. On the way down, inventory destocking helped to enflame the fear that the world was oversupplied with everything*	We have high inventory accumulation right now, and while inventory/sales ratio are extremely low (automobile industry), some industries are stocking up in expectation of high Christmas sales and due to supply chain issues

Source: The Forgotten Depression by James Grant

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