IDIOSYNCRATIC RISK

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Idiosyncratic Risk is a monthly investment ideas newsletter published by Antrim Research Publications, LLC.

A list of salient fundamental indicators

AN ODD TIME FOR WRITER'S BLOCK

As we compose the November issue of *Idiosyncratic Risk*, earnings season is in full swing, the presidential election is merely days away, and a full blue moon has risen on Halloween night, which seems at least as likely to impact market sentiment as the price-to-earnings ratio of the S&P 500.

Speaking of the S&P, that august stock market index peaked (for now) at a new all-time high ($3,580.84) on September 2nd of this year. Barely one week later, on September 7th, the number of daily new positive tests for coronavirus cases in the United States troughed at 25,166 reported cases, having fallen from 75,687 new cases reported on July 16th of this year. In the intervening weeks, that number has risen steadily in the United States, as well as the rest of the world. On Friday October 30th, 99,784 new positive tests were reported in America.

We note, as have others before us, that anecdotes indicative of "toppy" market behavior abound. Never has there been more interest in your author's career path and prospects among his friends, except for, perhaps, a few months during our fourth year at the University of Virginia when on-grounds interviews were the topic du jour.

And yet, absent the idea of venturing into your author's personal politics (which is not a topic for this newsletter) it seems, oddly, that there is nothing worth writing about at the present time. Of course, I could opine on the implications of the coming election for the stock market, except that it hardly seems that there are differences between the Biden/Harris and Trump/Pence tickets that would have a meaningful impact on market participants' enthusiasm for software-as-a-service, cannibis, blockchain, legalized gaming, e-Commerce, or food delivery.

Of course, I do not mean to imply that the market will digest Tuesday's results without any outward display of discomfort in the form of volatility. Rather, I

would submit to my readership that any near term reaction directly related to the outcome of Tuesday's polling will be, necessarily, short-lived.

The super-salient issues for market sentiment since the inception of this newsletter on April 1st, 2020, have been (in no particular order) the pace and trajectory of the increase in daily new coronavirus cases in the United States, the pace and trajectory of the increase in daily new coronavirus cases worldwide, and the supply of liquidity to market participants from the federal reserve and U.S. Treasury, as well as the investment of pandemic related cash stimulus checks from the federal government to U.S. citizens.

Without naively implying that the two parties are "the same," as it regards these issues, I continue to posit that the election will not have any material near or medium term impact on the direction of these variables, should they continue to be the primary drivers of market sentiment and valuation. It seems clear that, for at least the remainder of this calendar year, the policies and procedures that are currently in place will continue to govern the state and federal response to the coronavirus pandemic. An efficacious vaccine will not be widely available, and a "full re-opening" will not be possible without a coincident spike in the reporting of new cases. Of course, after December 2020, it becomes increasingly likely that exogenous factors will begin to play a role.

But even that may not be ***too*** likely. On Tuesday, October 27th, Pfizer indicated that the first interim analysis of its Phase 3 trial for a coronavirus vaccine had not occurred on schedule. This means that, just as with SARS and other "related" coronavirus pandemics before Covid-19, efforts to combat the spread of the virus at the policy level have reduced the infection rate amongst the control group to a point where the trial has not yet gathered enough data to show statistically that the Pfizer vaccine is more efficacious than a placebo. Paradoxically, this particular issue has always been a stumbling block in the global effort to vaccinate against coronaviruses.

In a world where the "base case" scenario analysis suggests that we continue to "muddle through" with an adequate, but not exceptional, policy response, and a reduced, but not eliminated, infection rate, the overwhelming temptation facing investors in the professional sphere is to dwell, unproductively, on a question which has steadfastly dogged our personal lives these few months, "When do things go back to normal?"

Of course, the answer depends on your personal definition of "normal." But from an investment perspective, the question is irrelevant in light of a more pertinent question and framework for assessing a shifting market sentiment and response to forthcoming "market-moving" datapoints and events. For investors, the most apt avenues of inquiry ignore (for now) the precise measurement of the "new normal," and focus instead on the direction of the trend in consumer behaviors. To wit, as the third calendar quarter earnings season draws to a close, is it possible to imagine a world in which consumer behavior becomes increasingly abnormal over the coming quarters? And is it likely?

Your author is of the mind that the answer to both questions is a resounding, "no." Whether or not we can attain "normalcy," with any alacrity, it does appear to be overwhelmingly clear that we are now past the peak of "abnormal," as it relates both to the pandemic policy response and its impact on consumer behaviors. The implications for investment are clear.

As we move through the calendar, into and through the New Year, investors can be expected to understand that year over year comparisons will be determined arithmetically by normal, "seasonal" sequential growth in revenues and earnings.

Temporary increases and decreases in demand, having been driven by the pandemic, must begin to revert towards a new, “mean.” At the margin, anyway.

In that framework, there would presumably be downside to stocks that had raced to all time highs after mistaking temporarily increased demand for a structural shift in consumer preferences, just as there would be downside to stocks that had raced back to, or through, all time highs on the expectation of a quick, “V” shaped recovery and a resumption of “normal” structural, secular growth. In neither case can consensus expectations be satisfied by a measured and moderate reversion towards a “new mean.”

So too, would there be upside for stocks and companies for which temporarily reduced demand had been mistaken for a structural shift in consumer preferences, provided that no excessive financial leverage exists which truncates the event horizon and necessitates a strong, “V-shaped,” recovery in order to avoid tripping restrictive covenants or requiring costly refinancing.

Within the framework of a gradual return to “normal,” the analyst must contend with the fact that the United States entered into a recession in February of this year. While measured unemployment may have already peaked at 14.7% in April of this year, the composition of the United States labor force continues to deteriorate in a manner consistent with ongoing recession. As temporary, part-time, and service industry workers return to work en masse, white collar lay-offs are accelerating. Those businesses that had benefitted from the notion that the middle and upper classes had been insulated from the worst effects of the pandemic in the U.S. would seem to be poised to disappoint. Those businesses which benefitted disproportionately from the consumer recipients of government stimulus checks, meanwhile, will be hoping that part-time service laborers are able to return to work in a measure that allows wages to equal or exceed the amount of stimulus that had been received over the summer.

At the same time, the risk of inflation does not appear to be entirely benign, or sufficiently remote for the federal runds rate to remain comfortably in the range of 0.0-0.25%. As measured by CPI, y/y change in the price of consumer goods bottomed in May of 2020 at +0.1%, but has increased to +1.4% already by September of this same year. The measurement would be higher were it not for the discretionary category apparrel (-6.0% in September) and gasoline (-15.4% in September, with miles driven -10%+ y/y). As measured by the price of Gold (up over 20% y/y) and Silver (up over 30% y/y) inflation is already here.

Such things represent the concerns of an older generation of investors, for whom cyclical factors and fundamentals frequently overwhelmed esoteric, qualitative concerns like, “impact.”

Speaking of “impact,” on June 23rd, the Trump administration’s Department of Labor “quietly” proposed a rule that restricted 401(k) plans from making funds focused on so called, Environmental, Social, & Governance (“ESG”) criteria the default option for plan participants, and proposed a set of rules whereby a funds inclusion in plans must be based on selection criteria that narrowly consider only risk adjusted returns. During the comment period, over 95% of the comments on the proposed rule were apoplectic and opposed. It is asserted that ESG funds, contrary to the rule’s assumption, have the highest risk adjusted returns. But it is also asserted that they will be unfairly handicapped by any rules that require investors to justify their inclusion by measuring their risk adjusted returns. The rule was adopted in spite of public outcry in October.

In a different market, there might have been something in the news worth writing about.

PAST PERFORMANCE IS NOT A RELIABLE PREDICTOR OF FUTURE RESULTS

It has been the habit of this newsletter to discuss a number of specific, actionable, investment ideas in addition to offering its authors general commentary on markets, news, and investment philosophy. And it will continue to be our practice to do so in the future.

Unfortunately, Antrim Research Publications has been hard at work in recent weeks on a number of projects for paying clients and subscribers that have resulted in four coverage initiations over the last three months, and a fifth which is well on its way. With earnings season ongoing, and that work consuming a tremendous amount of our time, we have not had occasion to write up any notes on small or micro-cap ideas, special situations, and personal account "story stocks." Suffice it to say, we continue to believe that you can throw a dart at a list of tickers and find considerable downside to valuations and fundamental expectations.

It is our sincere hope that the relative lack of pages in this months missive will save my readers valuable printer ink and toner, which remains expensive, even in a "work from home" world. The near term performance of the ideas (speculative or otherwise) that have previously been discussed in ***Idiosyncratic Risk*** can be found in the following table:

Recommendation	**Date**	**Performance Since Recommendation**
Short ACEL	October 1st, 2020	-10.4%
S&P 500	*October 1st, 2020*	-2.8%
Long LMND	August 3rd, 2020	-11.1%
S&P 500	*August 3rd, 2020*	+0.0%
Short TSLA Short GSX Long AKRXQ	July 1st, 2020 July 1st, 2020 July 1st, 2020	+79.7% +10.7% -90.4%
S&P 500	*July 1st, 2020*	+5.5%
Long MIK Short QSR Long ZMTP	June 1st, 2020 June 1st, 2020 June 1st, 2020	+126.0% -2.8% +16.3%
S&P 500	*June 1st, 2020*	+7.4%
Long NLY Long AGNC Short SWKS	May 1st, 2020 May 1st, 2020 May 1st, 2020	+20.5% +18.3% +40.6%
S&P 500	*May 1st, 2020*	+15.6%
Long DESP Short KNSL	April 1st, 2020 April 1st, 2020	+19.9% +79.5%
S&P 500	*April 1st, 2020*	+26.6%

Tuesday, November 3rd, is election day. Vote.

DISCLOSURES

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AS ALWAYS, LIKE, SHARE, AND SUBSCRIBE!

If you are coming across this, the eighth issue of ***Idiosyncratic Risk***, for the first time, welcome. I would always like to make new friends. If you find my views interesting or helpful, and if you'd be so kind, feel free to forward this newsletter along in your network to those who might also make use of its content.

I sincerely appreciate the friendship, support, mentorship, and camraderie I've experienced during my career in Investment Management and I would like to thank my friends and readers for supporting me, whether by forwarding this email and my contact information along in your network, or merely reading these pages and considering what I have to say.

Feel free to reach out with questions, criticisms, suggestions, and investment ideas if you've got any good ones.

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