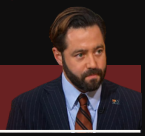
Australian Standfirst

SPAC's Spat & The North American Reopening Trade:

S&P500 Year End 4,800 Target, Fault Lines & An Avoidable ***Minsky Moment***

Hedge Fund Attribution

21st April 2021



Stirling Larkin, CIO

When speculation and markets run hot, reflex syncope suspends objectivity, emotive reasoning totally eclipses sound judgement and the sequence that follows looks more like a cheap ploy for drama than a subjective attempt at ascertaining price discovery or deep value.

The bellwether US S&P500 stock bourse will end calendar year 2021 at or hovering near 4,800 index level and to litigate the case for why and how such an ascent manifests in such, relative short order – remembering that markets climb the wall of worry – examination of the patent fault lines and ***Minsky Moment*** trigger points cleaves a path towards a clear indivisible equation.

Special Purpose Acquisition Companies, or SPAC's, have found their purple patch during these quixotic economic and financial times nevertheless the '***SPAC's Spat***' of recent weeks evidences the intolerance the market polity has for (currently) over-engineered synthetics.

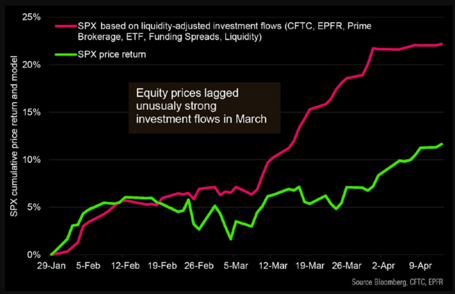
Cite:- Special Purpose Acquisition Companies (SPAC's): Funding Blind Pools, Mature Unicorns & Family-Owned Businesses During The Great Corona Crisis (GCC), 26 July 2020

[A SPAC is a company with no commercial operations that are formed strictly to raise capital through an initial public offering (IPO) to acquire an existing company. SPACs have tripled in number year over year, attracting big-name underwriters and investors and raising a record amount of IPO funding – the Australian Standfirst DDPM Team are regarded as Asia-Pacific's leading experts in these specialised investments and please contact your Client Services Representative to discuss further or field any questions]

On 31 March and 8 April, the US Securities and Exchange Commission (SEC) effectively halted the more than 550 SPACS filed to go public this year in the United States, airing legitimate trepidations surrounding the employment and thereafter, accounting treatment of warrants salaried to the '***Sponsor(s)***' and furthermore, the liability risk of forward-looking disclosures (after all, they are marketed as tax-aware investments).

The warrant-accounting issue raises the spectre of how companies should be classifying the warrants on their balance sheets as a liability in lieu of their current preferred treatment as equity.

The regulator appears to be playing catch-up with the boom in SPAC's by issuing guidance, leaving "***Business Combination***" companies to recalculate valuations for every quarter leading up



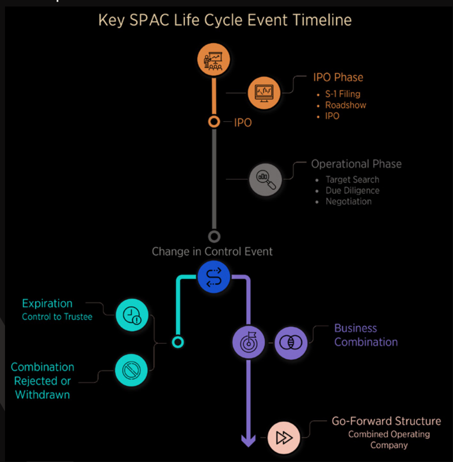
Strong investment inflows suggest the S&P500 should have risen more than it did in March 2021.

to and after the combination agreement using a complex analytical method beyond the traditional and relatively vanilla Black-Scholes methodology.

Companies issue the warrants along with shares in the SPAC as part of a unit to attract investors who are being asked to invest in the publicly traded shell company with no way of making money until it combines with a promising private company.

Market pundits see the SEC action as part of an effort to cool the SPAC market, which exploded last year under a deregulatory push by the last administration to encourage more companies to go public; the SEC leadership under the Biden administration has said it also wants to encourage more IPO's while ensuring alternatives, like SPAC's, are "***structured soundly***".

The market will eventually find a way to deal with this and they will go back in business events of April have all but paused this specialised market.



Parking the ***SPACs Spat*** for April-May and accepting that US Treasury yield stress-testing will soon prove to be nothing more than temporary, the reflation and reopening trade will resume, with ***Risk-On*** yields moving higher and rotation from value and cyclicals to growth, quality and momentum extending.

Market analysts en-masse expect S&P500 Earnings-Per-Share, or EPS, of US$176 in 2021, which is eight percent higher than pre-***Great Corona Crisis*** (***GCC***) levels and twenty-five percent higher than 2020 earnings.

There is a high chance that these EPS expectations are too low and for context, in 2010 {year one of post-GFC} EPS expanded forty percent from 2009 and matched {pre-crisis} 2007 levels.

If companies can beat earnings expectations at a fifteen to twenty percent pace – as they did in Q4 2020 – it would imply full-year earnings of ~US$200 in 2021.

Coincidentally, a forty percent growth rate to match 2010's EPS growth rate would also get the S&P500 index to US$200 in EPS in 2021.

In such an expansionary ***Risk-On*** and reflation fuelled ecosystem, even when assuming a conservative and flat price-to-earnings ratio of 24x, that implies an index level of 4,800 assuming reflationary fiscal and monetary wings remain inline.

Beyond *back-of-envelope* arithmetic and far more anecdotally, recent data from the US options market and investment flows show that investors are positioned for upside asymmetry this coming quarter, with call option buying pressure shows investors are positioned for upside over the next couple of weeks.

Calls are more expensive than normal *vis-à-vis* Put options and volume remains focused in short-term options.

Cite:- Options Remain Open: Defence, Protection & Risk Mitigation, 27 April 2020

Cite:- Options To Protect Your Portfolio, 2 August 2014

Reinforcing this, substantive Exchange Traded Funds, or ETF macro investment flows also evidences continued sponsorship for listed equities, with S&P500 trailing flow data significantly in March – a well-established market heuristic indicator proofing a continued tailwind for listed scrip (when S&P500 returns and flows deviate, they tend to mean revert in subsequent periods).

The breaking of a wave cannot explain the whole sea – the girth and momentum of the incumbent and exceptional reflationary supercycle should not be underestimated – and fallacious fears of Minsky Moments or rational retracements based on "***fundamentals***" (whatever that means anymore) are not only redundancies, they are dangerous misunderstandings about the ecosystem for which we all now find ourselves ensconced.

Cite:- Practical Guide For Australian Investors: 2020 to 2022 Roadmap, 13 April 2020

Cite:- Cheating, On Cheating, On Cheating, Maintaining Portfolio Quality In The Era Of Cheating, 13 March 2020

Retire regressive illusions of emotive reasonings that once were, and find your own path towards accepting the sustained expansionary dominion that will leave an indelible impression upon these Roaring 2020's. **Strap-in**. ■