25th Edition

3rd Quarter 2020

TILIA NEWS

INVESTMENT MANAGEMENT | FIDUCIARY ADVICE | RETIREMENT PLANNING

Gold: Investment, Inflation Hedge or Just Hype?

Some of our clients have recently reached out asking about a place for gold in their portfolio. Much of the interest is sparked by gold's recent rise to an all-time valuation high coupled with concerns about future inflation. We advocate for limited exposure to gold, if at all.

We are firm believers in the upward arc of human progress and innovation over time. As such, we favor ownership of human capital and production (stocks and bonds) over gold. While gold does have limited commercial applications, its appeal primarily lies in its universal acceptance as a store of value. When investors fear that their money supply may be devalued over time through currency printing, gold becomes an attractive haven. In the past, gold prices have surged during periods of political and economic uncertainty such as the 2008 financial crisis, 2001 dot com bust and early 1980s oil-shock-induced recession. Each of these crises

Return of the SPAC

"When Preston Waters sees an opportunity, he takes it"

Unless you were 12 years old in 1994, there is a very slim chance you are familiar with Preston Waters or the tagline above. Preston Waters was the fictional centerpiece of Disney's 1994 film, *Blank Check.* A young Mr. Waters had his bike run over in the movie and was inadvertantly handed a blank check by the driver. Being an opportunistic kid with big dreams and a non-chalant view of consequences, Waters fills in $1,000,000 and is miraculously able to cash the check.

Fast forward to 2020, and hedge fund managers & retired executives are seeing a similar "blank check" opportunity, and they are taking it at an alarming pace. This opportunistic group is capitalizing on a rise in popularity of "Special Purpose Acquisition Companies" aka SPACs. SPACs were initially conceived in the 1990s, and after a brief stint of popularity in the mid-2000s, they've finally garnered mainstream attention in 2020.

The basics of how a SPAC works is pretty simple. These fund managers & executives use their track record, along with connections on Wall Street, to raise hundreds of millions for a company via an Initial Public Offering (IPO) with no actual business (a shell company). With this "blank check" in hand, the SPAC then looks for a private company to acquire, which through the acquisition becomes a publicly traded company. Under most circumstances, private companies can be bought at lower valuations than publicly traded companies, so the bet is that quick and substantial money can be made in the transaction once the public is able to purchase shares. It is worth noting that shareholders in the SPAC have the power to vote "no" to the proposed acquisition, which provides some downside were marked by a dramatic climb in the price of gold followed by a similarly steep decline as investor confidence returned. We believe that this time is no different. With no earnings or dividend payments to fall back on, there is little to support the price of gold once market sentiment begins to swing in the other direction.

To help protect our clients against inflation we utilize, among other investments, Treasury inflation-protected securities (TIPS). These government bonds pay interest on a recurring basis while adjusting their yield based on inflation in the Consumer Price Index. This feature provides investors with an income stream that can keep up with price increases in the event of future inflation.

We believe that our clients should continue to own stocks and bonds, with investments in gold limited to a case by case basis. Historically, a balanced portfolio of stocks and bonds has provided investors with excellent defense against inflation. We don't expect that to change anytime soon. As always, please call our office if you have questions about adding an investment or just want to say hello!

Sources: koyfin.com; WSJ.com

protection for major investors. Investors also receive their original investment back, minus fees, if the SPAC fails to make an acquisition in the specified timeframe.

After trending up in issuance for years, several major deals in late 2019 - early 2020 drew national attention. Virgin Galactic (Richard Branson's space tourism venture), Draft Kings (online sports gambling) and Nikola Motors (development-stage electric trucks) were all acquired by SPACs, and each transaction resulted in shareholder returns in excess of 100% in a very short time period. SPAC issuance has exploded in the months since, with over $28 billion raised in 2020 so far, which is already more than double the $13.6 billion total from 2019.

While many SPACs have performed well this year, investors should approach them with caution. The one thing that many of these acquired companies have in common is a story that is based on hope for the future, with plenty of uncertainty & little to no current revenue to point towards. Since the Nikola Motors acquistion, a flood of new electric vehicle companies have been bought by SPACs, including Fisker, Lordstown Motors, & Canoo. Canoo's business plan includes offering the van below via a subscription service starting in 2022. Color us skeptics on Canoo.

Source: canoo.com

The rise in SPACs is a sign of greed and excessive risk-taking going on in markets right now. Plenty of great businesses can still be bought at attractive prices, but certain pockets of the market boast valuations that aren't based on reality. Just like Preston Waters found out, investors writing blank checks today are likely to have regrets down the road, as more dollars chase less attractive assets.

Sources: spacresearch.com; techcrunch.com; canoo.com; IMDB.com.