Global Matters Weekly

21 June 2021

For what it's worth

– Richard Parfect

What is it worth then? This is a question investors should be asking themselves all the time. However, the true answer is not always obvious. There are many ways to approach it and there is of course an easy "short cut" to establishing an answer; the stock market price. However, relying on such a public pricing mechanism implies a high level of faith on efficient markets and to believe there is no such thing as "the madness of crowds".

While it may be possible to assume markets are efficient for certain stocks much of the time; we believe, as active investors, that there are pockets of inefficiency throughout the market all of the time. Herd mentality and a reluctance to stand out from the crowd can lead to instances of a build up of excessive sentiment in either direction on stocks.

Benjamin Graham discussed how in the short term the stock market is a voting machine (sentiment) but in the long term it is a weighing machine (value). We certainly saw the stock market's short term failings in 2020 as COVID-19 brought company valuations down to levels that implied their futures were permanently impaired. The subsequent strong recovery reflects how the voting sentiment has swung the other way as investors play the "reopening trade". Share prices in the longer term (the weighing element of the market) will almost certainly be closer to (and above) the recovered prices than the distressed levels of 2020.

So, the short termism of markets presents a problem to investors as they see their holdings marked down in crises, however if they apply a more long term mindset, that presents a (buying) opportunity. Indeed, we are now starting to see parties enter the UK equity market with a clear view on the longer term return potential of listed companies; as a number are now facing bids from either trade buyers (competitors) or private equity.

In order to have confidence to act on those short term opportunities, then investors need to apply some fundamental analysis to the investment proposition; an inexhaustive list would include assessments on: intrinsic asset value and their future income/dividend generating potential supported by profit expansion (which in turn relies on revenues and margins). These are fundamental and important quantitative and qualitative questions to answer by digging into the company, its management and their philosophy.

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However, restricting one's framework to companies that are already established on a revenue or even profit generating path, can result in some missed opportunities. It can be argued that investing in pre-revenue generating companies is the preserve of "growth investors"; however if there is clear visibility in a company to profitable revenue generation and sensible assumptions can be put in place for that, then it should be possible to appraise whether the quoted market price is a fair value for those future returns. Nevertheless, it is important to distinguish here the difference between companies that have a credible product or technology platform that needs commercialisation at scale, from those that are more "blue sky" and uncertain

Valuing such companies can be more subjective and requires a more qualitative and in depth understanding of the company than a pure spreadsheet analysis will reveal. This is perhaps most apparent in the disruptive breed of owner-managed businesses raising "cross-over" private capital before they list on public markets. Similarly, sectors like healthcare can see companies valued, both by private and public markets, at material discounts to what they are intrinsically worth.

The clearest indication of what a company is worth is ultimately what someone is prepared to pay to own it out-right. A recent example would be Kymab, which was a private company held within Schroder UK Public Private Trust (SUPP). It develops monoclonal antibody therapeutics for use in oncology and immune disorders amongst other indications; technology that is transformative for medicine. It was recently purchased outright by the global pharmaceutical company, Sanofi, for up to $1.5bn; which is a price per share 4x the level of where it had been formally valued within SUPP.

In summary, it is important to understand that listed markets will immediately tell you the price of everything, but in that snapshot of time it will inform you the value of nothing.

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The Marketplace

- Global equities fell -1.9% last week
- The Federal Reserve struck a more hawkish tone at last week's FOMC meeting
- Brent crude oil rose +1.1% to $73.5 a barrel, hitting its highest level in more than two years
- Gold fell -6.0% last week to $1764.2 per ounce

Market Focus

US

- US equities fell -1.9% last week
- 10yr treasury yields rose following the hawkish FOMC announcement last week before falling again. Median expectations are now for two interest rate hikes in 2023 according to the dot plot
- The Federal Reserve increased their core PCE (personal consumption expenditure) forecasts for 2022 to 2.1% from 2.0%, while 2023's projection remained at 2.1%
- US retail sales missed expectations in May with a -1.3% contraction (vs. -0.8% expected), though the previous month's growth was revised 0.9pp higher to +0.9%
- US producer prices rose by a stronger-than-anticipated +6.6% over the last year (vs. +6.2% expected)
- The Philadelphia Fed's manufacturing business outlook survey showed the Prices Paid diffusion index rise to 80.7- its highest level since 1979. The current Prices Received index rose to 49, the highest level since 1980
- Weekly initial jobless claims for the week ending June 12 unexpectedly rose to 412k (vs. 360k expected)

UK

- UK equities fell -1.5% last week
- The UK CPI reading surprised to the upside at +2.1% (vs. +1.8% expected), whilst core inflation comfortably beat expectations at +2.0% (vs. +1.5% expected). CPI was above the BoE's 2% target for the first time in almost two years
- Payrolls rose for a sixth consecutive month with a +197k increase in May relative to April, though it still stands at -553k below its pre-pandemic level
- 80% of the UK adult population have now received a first vaccine dose

Europe

- European equities fell -0.9% last week
- Core eurozone government bond yields rose after the Federal Reserve's signal to begin raising interest rates in 2023. However, dovish comments from the European Central Bank reinforcing their commitment to ongoing quantitative easing helped to moderate the move
- Eurozone industrial production was stronger than expected in April, rising 0.8% sequentially and 39.3% year over year, as the output of consumer goods more than doubled
- The EU and the US came to an agreement at last week's summit on a 5-year tariff truce over aircraft subsidies for Airbus and Boeing
- The German Chancellery Minister Braun estimates that the country has surpassed 50% of the population having had at least one jab against Covid-19

Asia/Rest of The World

- The benchmark Global Emerging Markets index fell -1.5% last week
- Japanese equities fell -0.4% on the week
- Chinese equities fell -1% last week, their third weekly decline
- China's retail sales missed expectations, with year-on-year growth of +12.4% (vs. +14.0% expected), while industrial production was up +8.8% year-on-year (vs. +9.2% expected)
- The US Federal Communication Commission has proposed a ban on products from Huawei and four other Chinese electronics companies due to security concerns
- Japan's May CPI came in at -0.1% year-on-year (vs. -0.2% yoy expected) while the core CPI printed in line with expectations at +0.1% yoy

Past performance is not indicative of future returns.

Source: Bloomberg. Returns in local currency unless otherwise stated.

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Asset Class/Region	Currency	Currency returns			
		Week ending 18 June 2021	Month to date	YTD 2021	12 months
Developed Market Equities					
United States	USD	-1.9%	-0.8%	11.5%	35.2%
United Kingdom	GBP	-1.5%	0.0%	10.9%	15.9%
Continental Europe	EUR	-0.9%	1.8%	14.9%	28.0%
Japan	JPY	-0.4%	1.2%	8.9%	25.6%
Asia Pacific (ex Japan)	USD	-1.3%	-1.2%	5.9%	38.8%
Australia	AUD	0.8%	2.9%	13.6%	27.9%
Global	USD	-1.9%	-0.7%	10.6%	35.3%
Emerging markets equities					
Emerging Europe	USD	-2.7%	1.3%	14.0%	29.6%
Emerging Asia	USD	-1.2%	-1.2%	4.7%	40.3%
Emerging Latin America	USD	-1.5%	1.8%	7.9%	39.2%
BRICs	USD	-1.1%	-0.8%	3.7%	32.5%
China	USD	-1.0%	-2.2%	-0.5%	25.3%
MENA countries	USD	0.4%	2.1%	20.4%	38.5%
South Africa	USD	-6.5%	-7.8%	10.6%	42.1%
India	USD	-1.9%	-1.4%	11.3%	62.2%
Global emerging markets	USD	-1.5%	-0.9%	6.2%	39.5%
Bonds					
US Treasuries	USD	0.2%	0.9%	-2.8%	-3.1%
US Treasuries (inflation protected)	USD	-0.3%	0.0%	0.9%	6.4%
US Corporate (investment grade)	USD	0.6%	1.7%	-1.2%	3.5%
US High Yield	USD	-0.1%	0.7%	3.0%	12.8%
UK Gilts	GBP	0.2%	0.8%	-5.7%	-5.8%
UK Corporate (investment grade)	GBP	0.0%	0.7%	-3.0%	2.9%
Euro Government Bonds	EUR	-0.4%	0.4%	-3.1%	0.3%
Euro Corporate (investment grade)	EUR	-0.1%	0.4%	-0.4%	3.5%
Euro High Yield	EUR	-0.1%	0.6%	3.1%	10.7%
Japanese Government	JPY	-0.2%	0.1%	-0.1%	-0.2%
Australian Government	AUD	-0.7%	0.6%	-2.7%	-2.4%
Global Government Bonds	USD	-1.0%	-0.7%	-4.5%	0.2%
Global Bonds	USD	-1.0%	-0.7%	-3.5%	2.1%
Global Convertible Bonds	USD	-0.5%	0.0%	1.1%	21.1%
Emerging Market Bonds	USD	-0.4%	1.3%	-2.8%	4.5%

Source: Bloomberg. Past performance is not indicative of future returns

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Asset Class/Region	Currency	Currency returns			
		Week ending 18 June 2021	Month to date	YTD 2021	12 months
Property					
US Property Securities	USD	-3.6%	2.2%	20.8%	31.5%
Australian Property Securities	AUD	-0.3%	4.8%	8.4%	21.9%
Asia Property Securities	USD	-1.9%	1.2%	8.8%	13.5%
Global Property Securities	USD	-3.1%	1.0%	14.0%	27.3%
Currencies					
Euro	USD	-1.8%	-2.9%	-2.9%	6.1%
UK Pound Sterling	USD	-2.0%	-2.7%	1.2%	11.3%
Japanese Yen	USD	-0.5%	-0.7%	-6.3%	-3.0%
Australian Dollar	USD	-2.6%	-3.1%	-2.6%	9.6%
South African Rand	USD	-4.0%	-4.0%	2.4%	22.0%
Swiss Franc	USD	-2.4%	-2.5%	-4.0%	3.3%
Chinese Yuan	USD	-0.8%	-1.3%	1.1%	9.9%
Commodities & Alternatives					
Commodities	USD	-3.2%	0.0%	23.7%	54.5%
Agricultural Commodities	USD	-5.0%	-2.5%	16.0%	53.2%
Oil	USD	1.1%	6.0%	41.9%	77.1%
Gold	USD	-6.0%	-7.5%	-6.9%	2.4%
Hedge funds	USD	-0.4%	0.2%	3.7%	12.0%

Source: Bloomberg. Past performance is not indicative of future returns

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