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It's lights out and away we go

Global Matters Weekly

28 March 2022

– **Matt Connor**

The first race of the 2022 Formula One season didn't disappoint, as Sir Lewis Hamilton sought a strong start to his record-breaking 8th World Championship in Bahrain. Many were quick to write off the Mercedes man, due to a lack of pace in free practice and qualifying compared to rivals Ferrari and Red Bull. Despite the negative outlook, Hamilton still managed to achieve a podium. As value investors we often view negative sentiment around a company as a potential opportunity to capitalise on irrational valuations.

A prime example of such irrationality is Purplebricks, an online estate agent in the UK. After underperforming peers in a buoyant housing market, coupled with an issue in its lettings business, it's shares plummeted, reaching a low of 12.5p*. This gave a business with close to £60m of cash on the balance sheet, and no debt, a market capitalisation of just over £38m i.e. a negative enterprise value for what is the UK's largest estate agent brand.

The dislocation between Purplebricks' valuation and logicality did not go unnoticed by us or company directors who have been actively buying the stock over the last few weeks. With a new management team at the helm, market sentiment has now turned more positive, with the share price more than rallying from its lows, however the UK's largest estate agency still only has an enterprise value of less than £30m; a lot less than what it was twelve months ago, despite the company gaining market share in recent months.

Another recent opportunity presented to us was dotdigital Group, a SaaS omnichannel marketing company. Its shares tumbled after revenue growth slowed. We have followed dotdigital closely for some time and despite the recent headwinds to the business, we believe it to be of high quality and able to continue delivering healthy returns on invested capital. This was not reflected in the 2x enterprise value-to-sales multiple, a 66% discount to dotdigital's 5-year average. The shares have subsequently rallied 50% but still only trade on a 3.4x multiple.

"As value investors we often view negative sentiment around a company as a potential opportunity to capitalise on irrational valuations."

Irrational moves in valuations aren't always preceded by bad news or a downgrade, as demonstrated by our most recent investment, Games Workshop, the world's largest hobby miniatures company behind Warhammer. Games Workshop has seen its market capitalisation almost halve in the six months from September 2021 to March 2022, caught up in the market sell-off that started with the onset of Omicron.

Games Workshop is an extremely high-quality business with a shrewd management team and solid business model. The company has demonstrated that it can grow invested capital rapidly, whilst increasing economic profits meaningfully. The unwarranted sell-off in the company's shares has provided an attractive entry point.

Unlike Formula One where it is difficult to draw long term conclusions this early on in the season, our long-term, value focussed approach allows us to invest in companies that can provide shareholder value over the long haul, and in the short-term we can take advantage of opportunities that may arise, just like Hamilton in Bahrain.

Source: Bloomberg Finance L.P

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The **Marketplace**

- Global equities increased by +1.3% last week
- At the NATO summit, leaders said in their statement that the Russian use of chemical or biological weapons would result in severe consequences
- Brent crude increased by +11.8% to $97.9 a barrel
- Gold increased by +1.9% to $1889.3 per ounce

Market **Focus**

US

- US equities increased by +1.8% last week, buoyed by Technology, Energy and Material stocks.
- Hawkish comments from across the Federal Reserve indicate that 50bps rate hikes could be announced at each upcoming FOMC meeting – this led to a spike in yields across bond markets.
- US new home sales unexpectedly fell to an annualised rate of 772k in February (vs. 810k expected).
- Weekly initial jobless claims fell to 187k in the week ending 19 March (vs. 210k expected), their lowest level since 1969.
- The US composite PMI unexpectedly rose to 58.5 (vs. 54.7 expected).
- University of Michigan inflation expectations were unchanged, with expectations for the next year at +5.4% and 5-year expectations at +3.0%.
- President Biden appeared to back down from comments he made in Warsaw suggesting regime change in Russia. Germany, France and the UK distanced themselves from the statements fearing further inflaming of tensions.

Europe

- European equities fell by -0.9% last week.
- German Chancellor Scholz warned that halting Russian energy imports would 'mean plunging our country and the whole of Europe into a recession'.
- The Euro-area composite PMI reading decelerating by less than expected to 54.5 in March (vs. 53.8 expected).
- At the EU summit, leaders joined the US in accusing Russia of war crimes in Ukraine. They agreed to tighten some sanctions and close loopholes on others.
- EU leaders played down the idea that Russia could force payments for energy exports to be made in rubles, with Chancellor Scholz and Premier Draghi both saying it would represent a contract default.

UK

- UK equities increased by +1.5% last week.
- The UK consumer price index rose at an annual rate of 6.2%, exceeding the median forecast of 6% among economists.
- The Office for Budget Responsibility (OBR) projected that real household disposable income per capita would fall by 2.2% in 2022-'23; this would be the largest annual decline since records began in 1956.
- Chancellor Rishi Sunak announced measures to alleviate pressures on the cost of living. They included a 5p cut in fuel duty and an increase in the National Insurance threshold to £12,570 from July. The package was not well received, and further measures are now being considered.

Asia/Rest of The World

- The benchmark Global Emerging Markets index increased by +0.2% last week.
- Japanese equities increased by +3.8% on the back of assurances of accommodative monetary policy from the BoJ and further fiscal stimulus.
- Chinese equities fell by -1.4% last week.
- Japan's composite PMI rose to 49.3 in March (vs. 45.8 in February), though still remains in contractionary territory.
- Australia's composite PMI rose to 57.1 (vs. 56.6 in February).
- The Russian stock market partially reopened last Thursday after a month's closure, its longest suspension since the collapse of the Soviet Union. A shortened and volatile session was across only 33 stocks, including Gazprom and Sberbank.
- Russia-Ukraine talks resume in Turkey today. President Zelenskiy said he wants Russia to move its forces to 'compromise territories' they occupied before the war.

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Asset Class/Region	Currency	Currency returns			
		Week ending 25 March 2022	Month to date	YTD 2022	12 months
Developed Market Equities					
United States	USD	1.8%	3.7%	-4.4%	17.4%
United Kingdom	GBP	1.5%	1.2%	4.2%	19.2%
Continental Europe	EUR	-0.9%	-0.3%	-8.9%	6.9%
Japan	JPY	3.8%	5.6%	-0.5%	3.5%
Asia Pacific (ex Japan)	USD	-0.1%	-1.7%	-7.1%	-10.7%
Australia	AUD	1.6%	6.4%	0.9%	13.5%
Global	USD	1.3%	2.5%	-5.3%	11.4%
Emerging markets equities					
Emerging Europe	USD	-0.5%	-60.2%	-72.3%	-67.7%
Emerging Asia	USD	-0.7%	-4.3%	-10.1%	-15.0%
Emerging Latin America	USD	6.6%	12.7%	26.0%	25.1%
BRICs	USD	-0.1%	-8.6%	-15.2%	-22.9%
China	USD	-1.4%	-10.0%	-16.3%	-32.7%
MENA countries	USD	1.5%	5.5%	13.0%	36.1%
South Africa	USD	1.4%	7.5%	18.7%	15.1%
India	USD	-1.2%	1.4%	-3.3%	15.4%
Global emerging markets	USD	0.2%	-3.8%	-8.4%	-10.8%
Bonds					
US Treasuries	USD	-1.8%	-3.0%	-6.1%	-4.7%
US Treasuries (inflation protected)	USD	-1.5%	0.2%	-3.0%	4.3%
US Corporate (investment grade)	USD	-1.7%	-3.0%	-9.0%	-5.5%
US High Yield	USD	-0.6%	-1.8%	-5.7%	-1.2%
UK Gilts	GBP	-1.7%	-2.7%	-8.2%	-7.6%
UK Corporate (investment grade)	GBP	-1.0%	-1.8%	-7.6%	-7.0%
Euro Government Bonds	EUR	-1.2%	-1.9%	-5.2%	-6.9%
Euro Corporate (investment grade)	EUR	-0.7%	-1.4%	-5.3%	-5.8%
Euro High Yield	EUR	0.0%	-0.5%	-4.6%	-2.8%
Japanese Government	JPY	-0.5%	-0.4%	-2.0%	-1.9%
Australian Government	AUD	-1.2%	-3.1%	-6.0%	-5.8%
Global Government Bonds	USD	-1.9%	-3.8%	-7.1%	-8.7%
Global Bonds	USD	-1.8%	-3.6%	-7.6%	-8.8%
Global Convertible Bonds	USD	-0.3%	-2.0%	-8.3%	-10.5%
Emerging Market Bonds	USD	-1.8%	-6.2%	-16.1%	-14.1%

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

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Asset Class/Region	Currency	Currency returns			
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Property					
US Property Securities	USD	0.5%	2.7%	-6.0%	23.1%
Australian Property Securities	AUD	0.8%	1.9%	-7.9%	13.5%
Asia Property Securities	USD	-0.1%	0.2%	-0.3%	-9.5%
Global Property Securities	USD	0.2%	1.8%	-4.9%	11.5%
Currencies					
Euro	USD	-0.6%	-2.2%	-3.5%	-6.7%
UK Pound Sterling	USD	0.0%	-1.4%	-2.5%	-4.0%
Japanese Yen	USD	-2.4%	-5.2%	-5.8%	-10.6%
Australian Dollar	USD	1.4%	4.2%	3.3%	-0.8%
South African Rand	USD	2.7%	4.5%	9.5%	3.6%
Swiss Franc	USD	0.2%	-0.4%	-2.1%	0.8%
Chinese Yuan	USD	-0.1%	-0.8%	-0.2%	2.8%
Commodities & Alternatives					
Commodities	USD	6.2%	16.8%	33.7%	70.9%
Agricultural Commodities	USD	2.9%	12.1%	20.6%	52.1%
Oil	USD	11.8%	23.2%	55.1%	94.8%
Gold	USD	1.9%	3.6%	7.1%	13.3%
Hedge funds	USD	0.6%	0.0%	-1.6%	1.2%

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

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