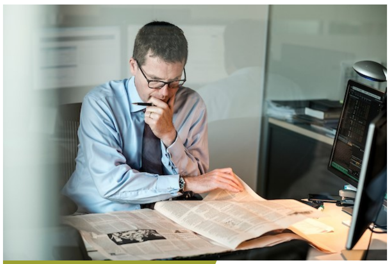


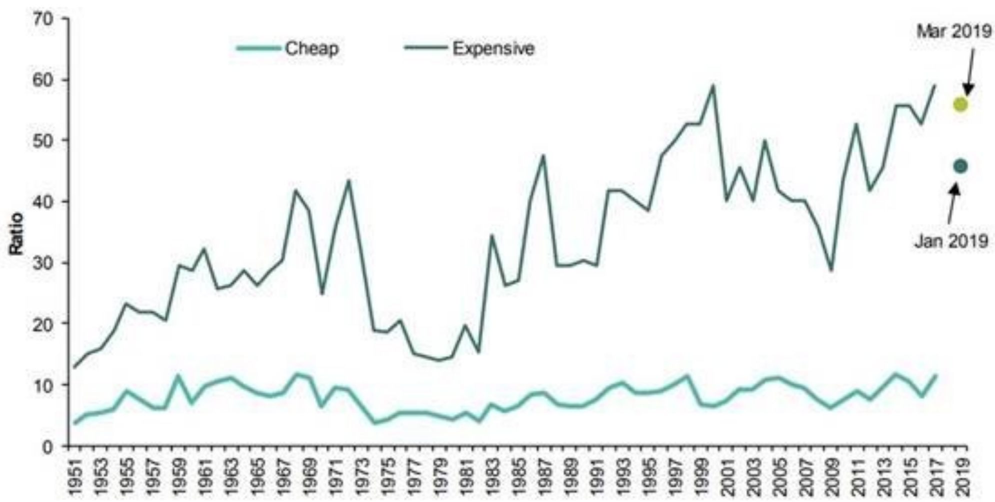
Friday Morning Coffee

Nr. 47 — Partly missing in action

One of our key convictions at ECP is that value as an investment style will make a comeback over the coming 12 to 18 months after 10 years of underperformance since the financial crisis. Our reasoning is based on the belief that, as central banks start to progressively normalize their monetary policies and interest rates increase, value stocks start to look much more attractive relative to the long duration growth stocks that generate most of their cashflows in a distant future. Another argument we put forward is that historically **the larger the valuation gap between growth and value stocks, the bigger the subsequent rebound and return of value stocks**.

After a difficult Q4 last year, global equity markets showed an impressive rally since the beginning of the year with most developed markets worldwide up 10% or more. Again, it was the most expensive growth stocks performing the best (+12.4%) with the value counterpart following close by with (+10.7%).

In an article on Bloomberg this week titled "Bernstein Quants Go Rogue and Tout Decade-Losing Stock Strategy", the authors show an interesting graph published by the Bernstein quant analyst team. As you can see below, the **valuation gap between the 20% most expensive and the 20% cheapest US stocks is at the highest level in 70 years**! According to the strategists from Bernstein value would therefore be poised for a rebound over the next 6 to 12 months once downwards earnings revisions bottom out and business sentiment improves. It is also interesting to note that the equity rally since the beginning of the year was driven by solid share price performance of the most expensive companies and not by the value stocks (see graph below).



Source: Ken French data library, Bernstein analysis, Bloomberg

The following note gives the opinion of the Investment team at the time of the publication. Please refer to important notice at the end of the document.

Friday Morning Coffee - **Nr. 47 — Partly missing in action**

In Europe the picture is somewhat similar. MSCI Europe Growth has outperformed MSCI Europe Value by 1.6% since the beginning of the year up to Wednesday this week. In light of the weakening economic conditions, the ECB is holding back on a more restrictive monetary policy and interest rates stay at low levels. The German 10-year Bund yield has more than halved since the beginning of the year to 12.6 bps. The longer the interest rates stay so low, the longer valuations are considered irrelevant and investors are willing to pay up for growth companies. The value bears also make the point that the least expensive companies in the stock market are cheap for very good reasons. Their business models may be under threat because they are either disrupted by technological change like for example the car industry moving to electrical or put into question by scandals like for example the banks shaken by money laundering affairs.

Where does this leave us as value investors at ECP? **We stick to our main conviction that our value investment style will come back into favour in the medium term. We continue to believe that valuation is what law of gravity is to physics**, in the end it kicks in. We avoid the most disrupted business models, prefer strong balance sheets and companies that have good business models producing solid cash flows over the cycle. If on top these businesses are lowly valued and offer us a significant discount to our estimated fair value, we stay invested as time will play into our favour. If value was partly missing in action in the recent rebound, it is far too early to write value off.

I wish you a nice weekend,

Léon Kirch, CFA
Partner & Chief Investment Officer
March 8th , 2019