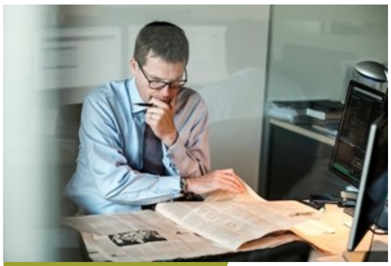
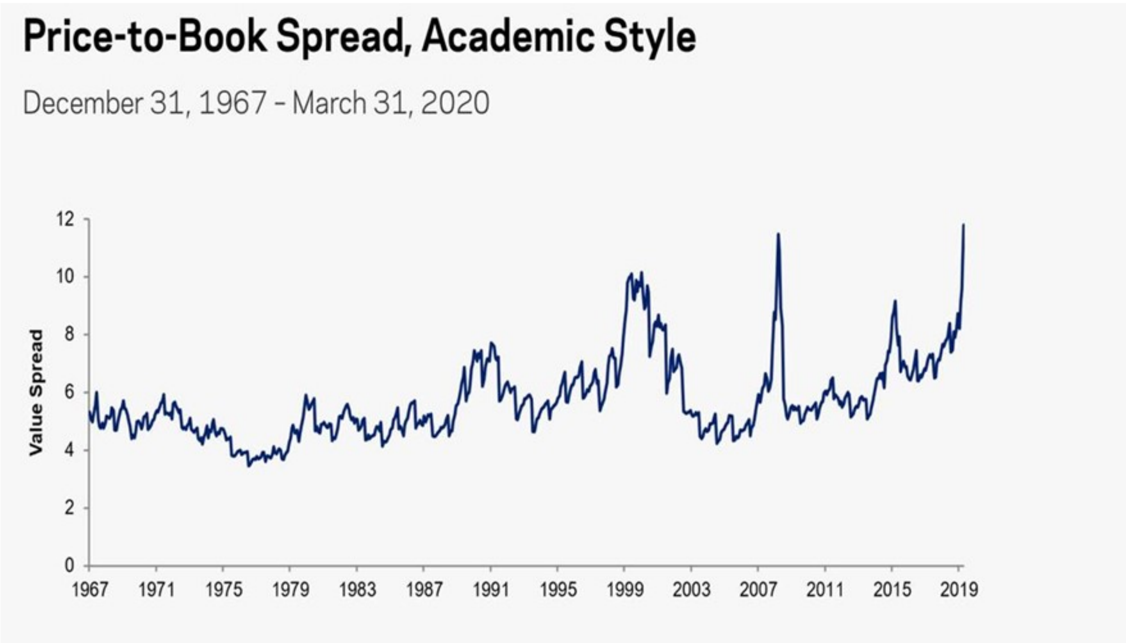


Nr. 103 — The FAAMGs and GRANOLASs

As value investors, we continue to have a tough time in the stock markets. The underperformance of value stocks has reached new extremes and is now like the levels seen before the Internet bubble burst. A limited number of companies have taken the leadership and represent currently an unprecedent level of the stock market capitalization. In a recent research piece, Goldman Sachs calls these leaders the FAAMGs in the US. These companies, namely Facebook, Amazon, Apple, Microsoft and Alphabet's Google represent 20% of the S&P 500. Their combined market value is higher than the GDP of Japan, 1/3 higher than the GDP of Germany and more than 6 times the value of all the companies comprised in the German DAX index. The European equivalent of the FAAMGs are the GRANOLAS : Glaxosmithkline, Roche, ASML, Nestlé, Novartis, Novo Nordisk, l'Oréal, LVMH, Astrazeneca, SAP and Sanofi. These 11 companies alone represent 24% of the Stoxx 600. As value investors we would certainly caution the ones buying ETF's on the S&P or the STOXX 600 as you now have an extreme concentration and probably some valuation excesses in some of these "happy few" companies.

In the meantime, we value investors underperform and the valuation gap between the cheapest and the most expensive companies continues to increase as shown in the recent paper from AQR. The authors looked at the valuation spread in terms of Price-to-Book between the cheapest and the most expensive US stocks over the last 50 years:



Source: AQR, Perspective, Is (Sytematic) Value Investing Dead, May 8, 2020,
https://www.aqr.com/Insights/Perspectives/Is-Systematic-Value-Investing-Dead

Friday Morning Coffee

Nr. 103 — The FAAMGs and GRANOLASs

The interesting point in the above is that the authors exclude the 5% largest companies. Therefore, the heavy weights in terms of market capitalization, the FAAMGs in the US, the technological winners who take it all have been deliberately excluded from this study. Still the spread between the cheapest and the most expensive companies is at an all-time high.

Price-to-book is often criticized as valuation measures do not consider the intangibles. A company like Microsoft has substantial intangible assets like licences, know-how and expertise that do not appear in its balance sheet and in it its book value. These companies would therefore deserve a higher price-to-book.

Value investors take that argument into account. However, the picture does not change if we replace Price-to-book value by other valuation ratios like price-to-sales, price to trailing earnings or price to forward earnings in the above analysis. **The picture is indeed similar: value stocks are cheaper than ever. And if history is any guide, such high valuations gaps are unsustainable. The question to ask is not if value stocks return but when …**

I wish you a nice weekend,

Léon Kirch, CFA
Partner & Chief Investment Officer
May 15 th, 2020