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Funds People

Here’s why the principles of value investing are sound

by Francesca Vercesi

In a highly volatile market, it makes sense to take contrarian decisions. There’s value in media, retail and in European domestic consumption in general. Speaking is **Angelo Meda**, Head of Equities at Banor SIM.

In this first quarter of the year we’ve seen world stock markets falling sharply and then picking up again, sometimes very quickly. What exactly has been happening?

In the early months of the year the markets moved downwards. They were strongly influenced by the fears that were already emerging at the end of 2015, of a slowdown in global growth, especially Chinese. Against this background, the sectors most exposed to Chinese consumption, like luxury goods or industrial machinery, were most heavily penalised. And while growth estimates were pointing to a slowdown, Japan and Europe were cutting rates and so also depressing the performance of banking sector stocks.

And now that things seem to be improving slightly…

The slightly improved growth forecasts in March and April, thanks also to the Chinese government’s action on the economy, the slight weakening of the dollar and the resulting recovery in commodities, enabled a partial recovery of the stock markets in the last part of the four-month period. One surprise was that the fall in oil production in the USA picked up speed in February, taking the price to above $40 a barrel after the collapse that immediately preceded it. The dollar too fell, giving some breathing space for commodities, although for now we don’t see any reason for it to return to 1.20 in the short term. The differential in rates, inflation and economic growth between Europe and the USA remains wide.

What are the expectations for the coming months? In Europe?

We’ll need to view this with a lot of caution. The risk of the Chinese economy again giving cause for concern is still there, not least in view of its very high public debt. The Chinese government is stimulating the industrial sector, but sooner or later the effect of this stimulus will tail off. At the same time, consumption continues to perform well, thanks to demographic trends. Some signals are arriving from the first-quarter results: while in the US the reporting seasons is almost over, in Europe we're still waiting for many companies' results. From what we've seen so far, Europe seems to be following the trend seen in the United States, where banks and energy sector companies posted unexpectedly good results.

The improvement is definitely less marked in Europe than in the USA, where the performance in these segments has prompted a review of the estimates for end-year earnings – but always upwards. We'll see how companies in the energy segment react to the stabilisation of the oil price. We take a positive view of companies linked to domestic consumption, while for the time being we're still avoiding sectors linked to exports to the Chinese market. In Europe, the biggest risk doesn't lie in the dreaded Brexit, which we think is far from likely, or in the situation in Greece. We're more worried about political instability in some countries, from Spain to Italy, and in general the political divisions inside Europe, which could hold back growth.

Do you think there are still investment opportunities in Europe, in spite of the volatility of the markets?

Our investment philosophy is inspired by the principles of value investing, which in a very volatile market tends to adopt a contrarian stance.. So we often increase our positions where the market is withdrawing, by choosing under-valued stocks with a very high potential yield. In this case our goal is a return of at least 30%. At the moment we're looking at the media, retail and the European domestic consumption sector in general.