Investment Insight

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ARIA | CAPITAL

Calling time: *Very few active US equity managers consistently outperform the benchmark, making it hard to justify paying the charges for active management. For that reason, we often recommend passive funds or ETFs as an efficient means of obtaining US equity exposure.*

However, most rules have exceptions, and so too does this one. The niche "small cap" part of the US equity market has been a profitable hunting ground for our clients. This is particularly the case when we identify exceptional small-cap exponents, and our go-to US small-cap growth manager, Drew Beja, is one such. In ***The Inside Track*** *this week we share some of Drew's recent thoughts on why market timing is a mug's game and on the type of opportunities that his investment team is finding currently.*

Dracula? *The mention of bats and fangs may ordinarily portend a macabre tale of Draculean dimension. Not so in investing terms. BATs (Baidu, Alibaba, Tencent), FANGs (Facebook, Amazon, Netflix, Google) and their ilk have provided quite the ride for investors over the past twenty-five years, a ride that was ultimately profitable for those who were willing and able to stay the course. The journey was punctuated by one particularly devastating correction and some analysts are concerned that another such may be on the horizon. We doubt it, but in the* ***Pic of the Week*** *we probe a little deeper.*

Quoted...

"Thunder is good, thunder is impressive; but it is lightning that does the work." – Mark Twain

The Inside Track

Drew Beja is Portfolio Manager of the GIM Small Cap Focused Growth strategy. His outperformance of the Russell 2000 Growth index has been stellar over the short, medium and long term. The following are some extracts from Drew's latest quarterly commentary.

Legendary investor Peter Lynch once said, "Far more money has been lost by investors in preparing for corrections, or anticipating corrections, than has been lost in the corrections themselves." Vanguard founder Jack Bogle echoed this when he said, "After nearly 50 years in this business, I do not know of anybody who has [timed the market] successfully and consistently. I don't even know of anybody who knows anybody who has done it successfully and consistently."

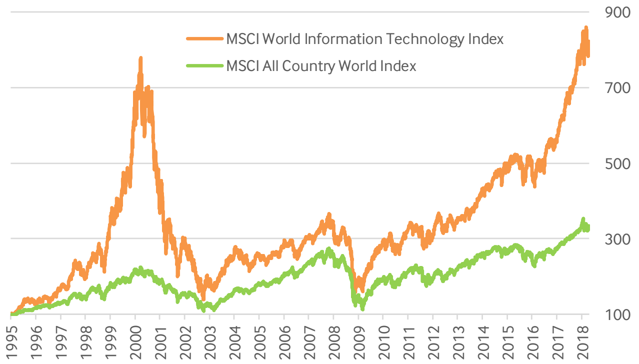
Channeling the late Texas Senator Lloyd Bentsen, I'm no Jack Bogle, and I've only been in the investment business for 33 years, but neither do I know anyone who has successfully and consistently executed market timing, nor anyone who knows anyone who has.

The first quarter of 2018 is "Exhibit Q1" for the case of why it is unwise for investors to try and market-time. Following a 35% gain in 2017, who would have predicted that the portfolio would rise double-digits in Q1? Not I, certainly. Given the tax reform enacted in Q4, it seemed more logical that stocks benefiting from corporate and individual tax cuts would lead the market as we headed into 2018. Logical yes, but as the market is wont to do, it does what it wants and such stocks did not lead in Q1.

The U.S. economy continues marching steadily, if not spectacularly, up and to the right. GDP growth of 3% annually since the financial crisis (source: US Bureau of Economic Analysis) has provided a healthy backdrop for the secular growth companies in which we invest. As a reminder, the portfolio consists of approximately 40 stocks of companies we consider "Desert Island Worthy" – i.e., if we were sent to a desert island for 5-7 years, these companies would all have enjoyed substantial growth by the time we returned. We overlay a disciplined valuation framework centered on risk/reward and probability-weighted expected returns to make sure that the stocks of these companies are attractive. Desert Island companies are often growing 25%-30%, multiples faster than U.S. GDP. Our investment team is focused on uncovering such opportunities, and we are finding plenty that are superbly positioned, have open-ended growth prospects, deliver excellent customer value propositions, and enjoy attractive business models. They also tend to have strong cultures, superb management teams, and solid balance sheets.

Pic of the Week

Technology stocks have strongly outperformed the broader market over the past decade. This is not so much a cyclically-driven sectoral trend as a secular evolution, where new technologies have become major forces not just in their sector but in the global economy and, by extension, in the stock market. Technology can no longer be narrowly defined; it permeates every industrial sector to a greater or lesser extent. The resultant trading performance has driven strong share price appreciation and, on some measures, lofty valuations. However, unlike the situation when the last technology-led stock market crash happened with the bursting of the Dot.Com bubble, today's tech stocks have strong levels of profit growth, well established business models and, for the leaders, substantial barriers to entry. This doesn't mean they are cheap, or impenetrable, and the time will come when their growth trajectories normalise. On that realisation, price-earnings multiples will contract, perhaps quickly and sharply, and investors should manage exposure carefully. However, in contrast to the Dot.Com meltdown, it is unlikely that an entire sector will experience a simultaneous valuation capitulation. Bats and fangs notwithstanding, nightmares are unlikely.



Week ahead: Key events

Market View

	Last 7 days (€)	Last 12 mths (€)	YTD (€)	5Y Ann. (€)
Global equities	+0.5%	+2.6%	-1.5%	+10.8%
US equities	+0.3%	+2.5%	-1.7%	+13.7%
European equities	+0.6%	+1.6%	-1.0%	+7.9%
EM equities	-1.5%	+5.9%	-2.7%	+5.2%
Irish equities	-0.1%	-2.3%	-4.0%	+11.6%
Commodities	+0.8%	-6.5%	+1.3%	-6.7%
Hedge funds	-0.1%	-0.3%	-2.3%	-1.5%

Currencies	Current	YTD Δ
EUR:USD	1.2107	+0.9%
EUR:GBP	0.8695	-2.2%
EUR:CNY	7.6629	-1.8%
GBP:USD	1.3922	+3.1%
Bitcoin	8,906	-38.5%

Commodities	Current	YTD Δ
Gold	1,317.74	+1.2%
Copper	6,960.00	-2.7%
Oil	74.04	+12.2%
Wheat	479.25	+12.3%

Central Bank rates	Current
Eurozone	0.00%
USA	1.25%
UK	0.25%

Economic indicators	Bond yields	Inflation	GDP YoY
Ireland	+1.0%	+0.2%	+7.2%
Germany	+0.6%	+1.6%	+2.9%
USA	+3.0%	+2.4%	+2.2%
China	+2.2%	+2.1%	+6.8%

30/04 Germany CPI & US Pending Home Sales
01/05 Japan Manufacturing PMI & US Retail Sales
01/05 US Manufacturing PMI
02/05 Japan Services PMI & Eurozone Manufacturing PMI
02/05 Eurozone GDP & Unemployment
02/05 US Interest Rate Decision
03/05 Eurozone Inflation & US initial Jobless Claims
04/05 US Employment Data

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