ValuAnalysis

ValuAnalysis research challenges long-held views around Growth vs. Value

"The Price of Value" paper reveals why 'undervalued' is not "lowly valued"

- Takes aim at misleading 'Value vs. Growth' categorisations
- Reveals factors that lead stocks to qualify falsely as Value

London, 12 February 2021 – Categorisation of stocks into either 'Growth' or 'Value', is misleading, according to latest research ValuAnalysis. Instead, the independent investment boutique, which focuses on equities and specialises in valuation, believes that the correct continuum is 'low to high expected growth' of any particular stock, at any level economic rent (free cash flow yield on economic assets).

The research comes amid relative outperformance by 'Value' stocks since 9 November 2020, when positive news on the efficacy of the Pfizer/BioNTech vaccine was announced and investor sentiment shifted toward cheaper stocks, after long-term underperformance. In its latest paper, examining the 'Price of Value', ValuAnalysis identifies factors that may cause a business to trade on multiples that are well below the median, and therefore qualify as 'Value' in most equity indices.

An appreciation for these factors can help investors identify when a stock is just lowly priced, as opposed to truly underpriced. "Value traps" can come from an inability to produce sustainable revenue growth (the Jam Tomorrow syndrome), a temporary lull in the growth trajectory (the Growth Evaporation syndrome) or a failure to leverage top-line growth to the bottom line (the Unlevered Growth Syndrome).

ValuAnalysis warns that investors must apply judgement or risk falling into "value traps". **Oracle** enjoys a phenomenal level of economic rent, similar to Microsoft's, but can only provide investors with *Jam Tomorrow* (no revenue growth) versus **Microsoft**'s 'honey today'. Oracle trades on exactly half the Microsoft's multiple as a result, despite a similar level of return on assets.

ValuAnalysis also identifies **LafargeHolcim** and **Novartis** as examples of stocks that should not be considered "Value", despite their low earnings multiple, but simply "low growth". Despite multiples of 17 to 22 times free cash flow, these stocks are adequately valued relative to their growth potential, says ValuAnalysis.

The ValuAnalysis investment team, who between them have extensive equity research and portfolio management experience from Deutsche Bank, Vontobel and UBP, believe the ideal Value stock would combine the following features:

- An accelerating rate of asset accumulation (aka "volume growth");
- An increase in the operational leverage, due either to revenue leverage or margin leverage, leading to an increase in the economic rent;
- A decrease in the risk premium.

The full ValuInsight paper, 'The Price of Value', can be found here.

Pascal Costantini, Managing Partner, Head of Research and Co-Portfolio Manager said: *"This artificial divide between growth and value was invented by the index providers largely for their own benefit. It implies that a growth business cannot be "good value", and, conversely, that only businesses that grow less than average are good value. This illogical symmetry would be inconsequential if it had not permeated the whole asset management industry, forcing managers to declare their allegiance, and putting stocks in boxes without context. An earnings multiple only measures expected growth and a risk premium. The "value" decision is about deciding if this level of expectation is right or wrong.*

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About ValuAnalysis

Authorised and regulated by the Financial Conduct Authority, ValuAnalysis is an independent investment boutique focusing on equities and specialising in valuation. The firm has developed a proprietary research model which identifies companies whose competitive advantage is under-appreciated by market participants.

The Partners have over twenty-five years of experience using, adapting and re-engineering the 'economic value-added' models used by industry consultants into stock market valuation models. These models replicate the thought process of an entrepreneur taking real investment decisions: what capital to commit where, at which cost, and for what return. Applied to the stock market, these tools provide invaluable insight about a firm's sustainable competitive advantage and the level of its economic rent.

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