MAERKI BAUMANN & CO. AG

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Value or growth?

Market Comment, April 2021

A frequently heard discussion in the investor community is the question of "value" or "growth". In other words, should investors opt for equities with historically low valuations or historically above-average business growth? In this debate between value and growth, balanced consideration of various aspects with an emphasis on robust companies looks like the sensible medium-term strategy.

The debate between the proponents of value stocks, i.e. equities with historically low valuations, and devotees of growth stocks (those exhibiting above-average business growth) has been going on for decades. But this debate has become more intense in recent years, partly due to the relative outperformance of growth-oriented US stocks compared to regions such as the Eurozone, and partly due to the increasing demand for value.

The US stock market has a high proportion of companies active in the technology and communications sectors. Many of these benefited strongly in 2020 from the spike in demand for internet services following the onset of the coronavirus pandemic, and thus exhibited historically above-average growth compared to other sectors. The renowned "FAANG" companies (**F**acebook, **A**mazon, **A**pple, **N**etflix, **G**oogle) are a good example of this.

Of course, there are also companies in Europe (as well as in some emerging markets) from the technology and communication sectors that are benefiting from structural changes. But more cyclical sectors with relatively low valuations – such as financial stocks with their sensitivity to interest rates, but also companies from the commodities, consumer, and manufacturing sectors – typically dominate, particularly in Europe.

As no one knows precisely how economic developments will unfold, or indeed predict the reversals that may occur due to further waves of coronavirus, a dogmatic insistence on either value or growth is probably a risky position to adopt. The more economy-dependent value sectors had a particularly hard time of it during the pandemic of 2020, and therefore have greater rebound potential in an improving global economy. Moreover, they are currently in greater demand, and have mostly benefited from rising bond yields in the past.

> "The expected improvement in the global economy in 2021/2022 now calls for a more balanced portfolio mix."
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> Gérard Piasko, Chief Investment Officer

On the other hand, some of the technology-oriented growth stocks have now become more expensive, which explains why some have become vulnerable to profit-taking. That said, the inexorable structural shift toward digitization can only be to their benefit. By contrast, market expectations in respect of the business development of value stocks remain fairly low compared to growth stocks or indeed the equity market as a whole, despite a certain degree of recovery being evident.

In any case, when viewed in historic terms, the difference in the relative valuations of the value and growth segments is now at such unusual levels that it probably makes sense to adopt a more balanced position that takes into account both groups. For us, this means – alongside our general philosophy of "security over return" – putting the emphasis on greater diversification between different equity regions, as well as a more balanced inclusion of both the value and growth principles. Why? Because as described above, the various global regions have different weightings of value and growth equities. Until such time as coronavirus has been definitively mastered, a more balanced regional spread of this kind could make more sense than a radical preference for one region or one investment style focused on either value or growth.

Conclusion: The likelihood of further improvement in the global economy in 2021 and 2022, together with historically high valuation differences, now calls for a more balanced mix of value and growth stocks. But particular attention should be paid by investors to the quality of a company's balance sheet, margins and market positioning – both in the value area with its more modest valuations and in the growth area that so often benefits from structural change. Due to the different weightings of these factors in the various global regions, a more balanced mix of these investment areas and regions would seem appropriate.

Gérard Piasko

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