CREDO WEALTH

Not all value is created equal

No doubt our clients are by now accustomed to our refrain: at Credo, we are value investors. The notion of focusing on valuation is intuitively appealing: after all, only a fool would pay over the odds. Yet within this comforting and attractive appellation are innumerable shades of grey. As far as the intuitive appeal goes, all valuation approaches are created equal but, when it comes to investment execution, some are more equal than others.

Though value may make for easy marketing, a glance at recent history confirms it by no means makes for easy investing. Over the last 10 years, the MSCI World Value Index has underperformed the MSCI World Growth Index by -2.3% on an annualised basis. Though such a figure tempts doubt, value is an article of faith for good reason: over the last 40 years, value has outperformed growth by 1.1%, annualised.

Yet, as the Orwellian logic above makes out, not all value is created equal; there are as many ways of measuring value as there are ways of implementing it within a portfolio. On one extreme, there is the “deep” value investor, who may care for little but the value of a company’s tangible assets less their liabilities. Our approach, however, is more nuanced: in surveying the investment landscape, our gaze is not restricted to a handful of metrics but rather searches for companies with robust long-term fundamentals where profitability, growth drivers, balance sheet strength, industry dynamics, and management factors offer attractive medium term returns. Ultimately, our analysis reduces to balancing a realistic assessment of the achievable total rate of return against risk, which induces a natural bias towards value-rich stocks.

But when it comes to investing, there are no panaceas; no process can protect the investor from the slings and arrows of the market. We have already witnessed one of the worst starts to the year, with the MSCI World down -6.0% in January and -0.7% in February (in US dollar terms). By contrast, our Best Ideas Portfolio fell “only” -4.3% in January and remained flat over February. Though it would be disingenuous to suggest that two months of data could ever demonstrate the relative merit of a strategy, since the inception of the Best Ideas Portfolio, of the 25 times that the MSCI World has ended a month down, the portfolio has outperformed 17 times, either falling less or even generating positive returns. This resilience has garnered an overall 2.1% annualised outperformance over the last 59 months.

Over the long-term, there can be little doubt that value investing has been a successful strategy and, we believe, shall continue to be so. While not all strategies are created equal, to reap the benefits of value at all, an investor must first weather the inevitable ebb and flow of the market. To guide investors along, our process is predicated on relative simplicity: we only invest in companies we understand at valuations that make sense. Only time will tell if our approach to value investing is more equal than others, but as the market inevitably ebbs, we hope the simplicity of our process will encourage investors to stay the course. As Orwell might have put it: “value good, simplicity better”.

CREDO
WEALTH

Important Notice