INVESTMENT FUNDS

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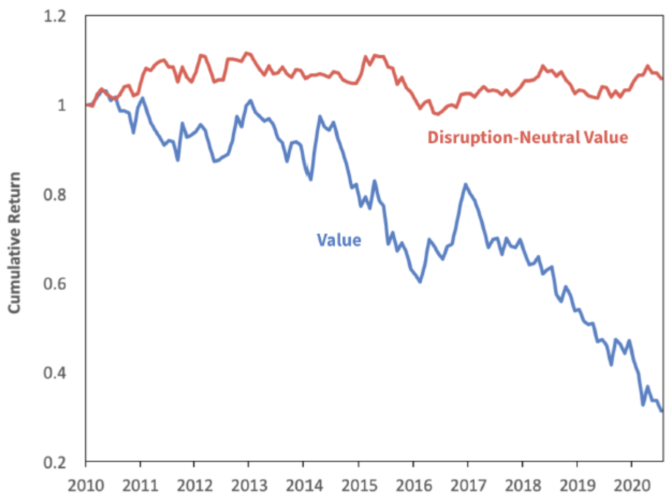
Value: A massive bet against technological disruption

Value investing has been underperforming since the great recession of 2008 and many pundits periodically call for a return to success of this strategy based on the thinking that eventually things will "revert to the mean". We think this debate of growth versus value investing is misplaced and lacks proper context. In fact, we think this should all be analyzed through the lens of technological disruption resulting in many fundamental winners and losers compared to previous "normalcy".

Traditional value investing has rotated into a massive bet against technological disruption. Using machine learning analysis, Sparkline Capital was able to neutralize tech disruption within the value equity universe and showed that a disruption-neutral basket of stocks achieved market outperformance. In other words, all the underperformance of value comes from the fact that many industries, like brick and mortar retail, traditional media or IT services, are being disrupted by e-commerce, digital advertising and cloud computing respectively. Demand shifting from physical businesses to the internet has only accelerated because of COVID-19 and exacerbates the demise of disrupted value.

Disruption Explains Value's Demise



Source: Sparkline, MSCI, S&P (as of 7/31/2020)

The narrative of value investing these days usually starts with a discussion on the outperformance of Big Tech stocks and ends up highlighting the historical spread with value stocks' valuation. In our view, through this recession, the market is only finally recognizing consumer-staple-like characteristics of the former, and the lack of fundamental resiliency of the latter. It's important to note that a tech-disruptor's value lies not in its book value, but in its newer business model and intellectual property. These businesses have pricing power and re-invest heavily, reducing near-term profits but growing long-term earnings power. Conversely, many disrupted value companies are price-takers and have already cut their cost structure to the bone in order to meet near-term earnings expectations, while significantly reducing earnings power in the long run. Don't get me wrong, Big Tech is both disruptive and monopolistic, which, coupled with increased market index concentration – especially in the Nasdaq, at over 40% – could be problematic.

At the end of the day, we are all tech investors. Technology is reshaping all industries and is quite often brought about not by pure technology companies, but by industry leaders using tech to stay at the forefront of innovation and to gain an edge over legacy incumbents. Tech should also not be viewed as a monolith: there is a broad universe of stocks that have disruption-like characteristics without the monopolistic nature of Big Tech. Thus, in our view, innovation is still in the driver's seat and as the economy recovers in the next few quarters, there are also many opportunities in value where business models are still relevant in a disruption-neutral framework. We think that investing is about being pragmatic and adjusting to new realities.

We will continue to question the traditional style of investing and pursue our journey as thematic investors, focused on the future!

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Main funds managed by the team

✓	Thematic Innovation
✓	U.S. Equity
✓	Global Equity
✓	Global True Conviction
✓	Thetmatic Innovation Hybrid 75/25
✓	Global Equity Hybrid 75/25
✓	Global True Conviction Hybrid 75/25
✓	IA Clarington Thematic Innovation Class
✓	IA Clarington Global Value Fund

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— Composed of experienced managers who emphasize fundamental analysis, identification of value and long-term investing

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