WHERE’S THE VALUE?

GARRY LAURENCE
Global Equities Portfolio Manager
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As a value manager, we are constantly looking to invest in tomorrow’s leaders at attractive prices. Most recent additions to Perpetual’s Global Share Fund have been in Asia and Europe where we are finding the greatest mispricing in quality businesses. We like to buy quality businesses when there is fear around a company, industry or geography; today we see a plethora of such opportunities.

Technology – Amazon versus Alibaba

Technology conjures images of fast escalating share prices; after all, both Apple and Amazon have this year broken through US$1 trillion valuation. While both the US and China have leading technology businesses we have been increasing our exposure to Asia as valuations have been falling. The region has globally leading businesses with strong balance sheets; a situation feared by the US and Donald Trump. The reality is that the strongest and most innovative survive in global capitalism. China is more advanced than the US in terms of e-commerce, with 18% of retail sales being online versus 14% in the US. Alibaba is a leader in ecommerce and is one step ahead of the US leader, Amazon, in payments.

There are numerous similarities between Amazon and Alibaba in terms of their businesses and new ventures. Amazon represents 5% of all retail spend in the US and 49% of all online retail spend with about 350 million active customers. Sales are growing at around 30% this year but are expected to slow to 20% in 2019.

Some of Amazon's greatest feats have been to build businesses from scratch, a testament to Jim Bezos. Amazon web services provides cloud services to large corporates and it's investing in artificial intelligence (AI). While Amazon is developing some wonderful assets and earnings streams, its valuation reached US$1 trillion and it trades on a price to earnings (PE) ratio of 100x.

On the other hand, Alibaba has fallen to an extremely attractive valuation, trading on a PE ratio of 20x one year forward. It has investments in cloud and video streaming that are loss making today but will create significant value going forward. Jack Ma has taken Jim Bezos' playbook and rolled it out into China.

Structured as a market place, Alibaba has two leading platforms – Taobao, its consumer to consumer platform and Tmall, its business to consumer platform. Alibaba has 58% of total retail e-commerce in China, revenue growth of 60% and its monthly active user base across Tmall and Taobao is at 634 million.

Alibaba is spreading its tentacles similarly to Amazon, investing in cloud services, fresh food offerings and AI with Tmall Genie, Alibaba's voice assistant.

Alipay is one of its undervalued assets with 870 million annual active users. During a recent trip to China, it was evident credit cards are rarely used. Consumers use Alipay and WeChat pay online and offline, and to transfer money between friends. Alibaba aims to roll out technology to convenience stores around China, whereby users scan an Alipay wallet as they enter the store, pick up the required items and exit; the account is automatically debited as the user leaves the store.

While the rest of the world is using a mix of PayPal, credit cards, Stripe, Square and Venmo for online payments, Alipay and WeChat pay are dominating the entire ecosystem in China. Alipay is looking to expand outside of China, as is Alibaba. We believe the valuation and earnings growth potential makes it a much more attractive investment than Amazon and also own an indirect stake in Alibaba through our investment in Softbank, which effectively gives us exposure to Alibaba at a 30% discount.

Deep dive – Euronet Worldwide

Euronet Worldwide (Euronet) is a global electronic processing company with three divisions – Electronic Funds Transfer (EFT), Money Transfer and Epay. Services include comprehensive ATM, POS and card outsourcing services, card issuing and merchant acquiring services, software solutions, money transfer services and electronic distribution of prepaid mobile credit and other prepaid products.

The company is exposed to several positive secular trends including increased global travel, increased use of ATMs in emerging markets and the need for money transfer globally. Euronet has a strong track record of successful acquisitions and an incentivised management team led by CEO Michael Brown. It operates within very fragmented industries and we expect Euronet to continue to consolidate the market going forward; this should help drive earnings growth over and above its strong organic growth potential.

As one of the largest independent ATM operators globally, Euronet is set to benefit from the recent announcement by Visa Inc to allow dynamic currency conversion (DCC) on ATM transactions globally from April 2019. Currently Visa only allows DCC on POS transactions globally and on intra-regional ATM transactions in Europe. This change will allow acquirers and ATM operators to offer DCC to all international ATM transactions on Visa-branded cards around the world. DCC is a high margin business within Euronet's EFT Processing business and this change will open up its total addressable market. Euronet is trading on 17x FY19 forecasts with 20% EPS CAGR for next three years versus competitor electronic payments companies at 20-25x PE.

At Perpetual, we continually review and visit a large number of companies, both current and prospective holdings. Our focus remains firmly on finding high quality, undervalued businesses and pooling them into a portfolio that makes a real difference to investors.

Find out more about the performance, strategy and holdings of the Perpetual Global Share Fund or read Garry Laurence's full October insights here.