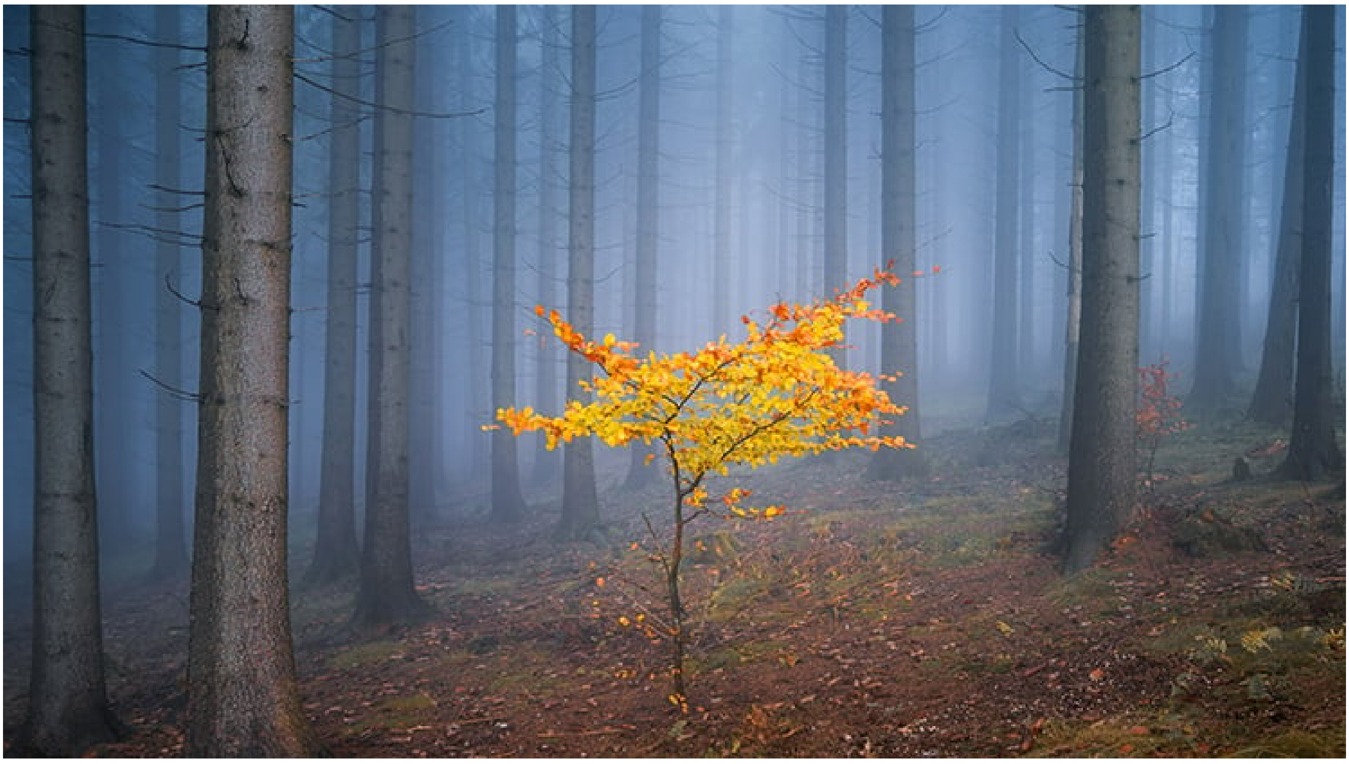
Barrow Hanley: Where global equities investors can find value amid tech mania

By Perpetual Asset Management
7 February 2024



While Big Tech continues to hog the limelight, the evidence still points to a cyclical value rotation, argues Barrow Hanley chief executive CORY MARTIN

- Early innings of a long value cycle
- Rates, inflation, growth rocket fuel for value investors
- Find out about Barrow Hanley's global equities investment solutions

BIG TECH again dominated headlines in the latest US earnings season.

But tech investors now appear to be more discerning, focusing on individual company results rather than the AI-driven "Magnificent Seven" halo effect.

That doesn't surprise Cory Martin, chief executive of global equities value investor Barrow Hanley.

"The Magnificent Seven has become the most crowded trade in the world," says Martin, referring to Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia and Tesla.

"When you have that narrow a market – when just a few stocks are driving the MSCI Index – the rest of the opportunity set grows dramatically for active managers.

"I believe we are in the earlier innings of a cyclical value rotation, with more normal interest rates, a higher cost-of-capital environment and a more-normal inflationary period.

"We believe in the value cycle," Martin says.

"It's indisputable – based on market indices such as the MSCI or Russell 1000 – that over the long-term, on a cumulative relative basis, value has outperformed growth investing."

It's a challenge to explain to investors and advisers the benefits of value investing, given the out-performance of growth stocks in the 2007-2020, post global financial crisis, low interest rate period.

And last year, growth indices outperformed.

But it's not uncommon to see a strong growth rally within a value cycle, says Martin.

"It happened in 2002-03 in a strong a period for value stocks," he says. "This is a bit like that."

Where to find value in a tech boom

The so-called Magnificent Seven stocks dominated Wall Street last year, driven largely by the potential for artificial intelligence.

That trend largely continued in the latest set of earnings results out last week.

The seven big US tech stocks comprise about 28 per cent of the S&P500, and their performance explains the growth indices last year.

“The Magnificent Seven tech stocks were up around 76 per cent last year, and the rest of the S&P500 was up just 13.75% per cent,” says Martin.

“As an asset allocator, you want to have growth stocks – there needs to be a healthy balance,” Martin says.

“But in value investing it’s all about the entry point. In growth investing, it’s all about the exit point.”

How can value investors participate in the AI boom, when the big tech stocks like Nvidia, Microsoft and Google seem to be benefiting most?

Those tech companies are considered growth stocks, particularly given historically high valuations.

“We do love these big tech companies,” Martin says. “But we don’t want to pay high multiples for them.”

Barrow Hanley has owned some of the tech companies previously, and could well in the future, if valuations drop.

Still, value investors can participate in the AI boom, he says.

“For example, we bought into an industrial company that is a big provider of cooling systems for data centres.

“Data centres are now growing exponentially with the development of AI. That company’s share price was up 200 per cent in 2023.

“We have another company that’s at the cutting edge of high-voltage connectivity and wiring. It’s one of the biggest providers of wiring for the electric vehicle market,” Martin says.

“On the surface it may seem that value investors can participate less in some of the mega trends such as AI.

“But there are ways they can, which are unique and not always apparent on the surface.”

Value investing opportunities

US-based Barrow Hanley – part of Perpetual Group – is long-term value investor.

“We target companies that are cheap for reasons we can identify and believe to be temporary,” says Martin. “And we look for catalysts for change.

“Most of the time we’re buying fairly good quality companies that are cheap, but exhibit rates of profitability above or in line with their industry group – and in many cases the broader market.

“That could be measured in return on equity, earnings per share or growth rates.”

“We’re buying cheap companies with multiple ways to win, apart from the normal reversion to mean.”

Around the world, the biggest dislocations, or valuation discounts, are in the consumer staples, consumer discretionary, energy, materials, real estate and healthcare sectors, Martin says.

“They’re all trading significantly below their long-term valuation averages.

“For our strategy, this translates into buying select REITs, primarily apartments. We’ve added more to utilities and materials which have been very out of favour.

“And we are overweight materials, healthcare and consumer staples

“We don’t have a broad view on whether the sectors will ultimately outperform.

"But we’ve found idiosyncratic stock stories in those undervalued areas of the market which should provide some very strong stock-specific results.

“I believe we are in the earlier innings of a value rotation, with more normal interest rates, a higher cost-of-capital environment and a more normal inflationary period.

“That would be rocket fuel for value and particularly cyclical value which we haven’t had in years."

About Barrow Hanley

Barrow Hanley is a global leader in value investing, managing assets for clients for more than 40 years.

Barrow Hanley Global Share Fund aims to provide investors with long-term capital growth through investment in quality global shares.

Rated "Highly Recommended" by Zenith, "Recommended" by Lonsec and with a Morningstar Medallist rating of "Gold", the investment team focuses on finding value in all the right places.

Find out more here.

Barrow Hanley is distributed by Perpetual Group in Australia.

Contact a Perpetual account manager

the Active ETF or the return of an investor's capital. All investments carry risk, including loss of principal. Past performance is not indicative of future performance.