

Thematic investing

Only by thinking differently than the herd can one truly aim to outperform.



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IF WE had a nickel for every time we've been asked at Tematica Research: which sectors do we like, we would probably be sitting on a beach somewhere instead of providing investment research to financial professionals.

It seems that at least once or twice per week we are asked, in some form or another, one of the following questions:

- What sectors do you rate as a buy right now?
- Do you like Financials? What about Technology?
- What is going to be the next big sector?
- What sectors do you think are best in bull markets? And which ones are best for sheltering gains in bear markets?

Our answer to any sector questions is simple: we like and dislike certain aspects of every sector. With our ever-changing technology and the fast pace at which trends are emerging globally, it's over simplifying to identify any one or two sectors as having the most potential. In any sector, there will be some companies that seize on a new opportunity faster than others based on the new trends or themes emerging in today's world.

Sector-based investing doesn't fit into our mindset at Tematica at all. When we analyze the market landscape, we approach it from an entirely different perspective.

Why we don't utilize a sector view of the markets

Let's use Apple (AAPL), Alphabet (GOOG) and Facebook (FB) as an example of why

we think viewing the markets through a sector-based lens is flawed. We touched on Alphabet earlier, but we chose it, as well as Apple and Facebook for this example not necessarily because their stocks are in the Tematica Select List of Investments (some are, some are not), but rather because they are among the largest market-cap stocks with business models that are pretty easy to understand, and all three sort of intersect one another in one capacity or another.

In a traditional sector-based view of investing, AAPL, GOOG and FB, would be slotted into Technology, Internet Software and Media sectors respectively. So, an investor could think, "Apple's stock seems to be struggling lately, and so the Technology sector is probably a little over-heated and maybe we should move away from that."

To view Apple as a technology-sector company however, would potentially lead an investor to be overly consumed with simply the latest iPhone sales figures. A sector-based lens would fail to see, let alone understand how Apple isn't just shipping out hardware, but is actually re-shaping the media we consumer (Apple Music and AppleTV), the services we are utilizing (through it's billions of app-downloads) and how we are paying for those purchases that we make (Apple Pay).

The same can be said for Alphabet (formerly Google) and Facebook – a sector-based lens would fail to see how these two apparent "media-sector" companies are pushing into retail sales and financial

services and are poised to change how we shop, how we pay, and how we save. And then there's the automotive category where both Apple and Alphabet are beginning to throw their weight around.

This new perspective, or "paradigm shift" – is what is called Thematic Investing. It is an investment approach that looks to identify structural changes emerging economically, politically and socially around the globe, and then seeks to determine which companies will be impacted by it.

A thematic view of the market

Referring to the questions at the beginning of this conversation, given this new paradigm, we see far better questions to ask:

- In today's world where connected devices are altering the way consumers and businesses interact and transact, which companies or business models are poised to be at the forefront of this movement, and which ones are looking like they will be left behind? We don't necessarily see the answer being within the Telecom sector.
- With China shifting towards a more Western diet and following the path of 1/3 of the

obese American population, what will be impact will be on life-expectancy for the worlds largest population and which companies are poised to gain (or lose) from that, whether its housing, financial services or healthcare? What will that mean for the health complications of expanding waistlines, to the clothes they purchase and the foods they eat? Is that a healthcare sector issue, a hospitality sector issue or a clothing and textile trend?

• An emerging trend where households are moving away from traditional broadcast models of cable or satellite TV, toward on-demand and streaming services – leads us to ask which players in the space are actually creating the most popular content currently being streamed and doing the best job of delivering the content?

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How we identify themes

In Thematic Investing, success still relies on the underlying principles of investing: identifying which securities within an emerging theme are mispriced or undervalued relative to the business opportunities ahead as a result of the sea change presenting itself through a theme. We identify such themes by looking at the intersection of shifting economics, demographics, psychographics, technologies, mixed in with regulatory mandates and other forces. Simply, we look at the real world that companies are operating in, and try and understand what's happening and why.

In our experience, the most attractive opportunities can be found when the business model for a company cuts across multiple themes that converge and reinforce one another. It is only when we look at the landscape through a thematic lens that we are able to see which company has legs, and then it is within in the stock fundamentals of each that drives us to identify the risk-to-reward ratio and determines whether we rate each one as either a buy or sell.

Find out more from Christopher Versace through his Masterclass on 5 August 2017. Log on to www.investfair.com.sg/ Chrisversace for more

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