Market madness

Be selective, advises Paul Gavaghan of Raymond James

Whilst there are still pockets of great opportunity across the globe, the past few weeks have also seen crazy price rises of some stocks as investors have rushed to join the herds buying certain technology stocks indiscriminately. Given the backdrop of a Western World with low interest rates and a pandemic that is highly disrupting many sectors, the relatively less affected technology sector is an attractive place to park money. It seems many investors taken this view but have forgotten the importance of valuations. The herd buying has pushed prices up which then reaffirms investors reasoning so they buy more again and so on which spirals share prices upwards.

There have been some particularly striking examples of craziness. Chinese property company 'Fangdd Network' went up over 12x in a day before crashing back down, purely because investors so desperate to buy tech stocks mistook it for the acronym FAANG which stands for Facebook, Amazon, Apple, Netflix, Google and thought it was a vehicle to invest in them. Another example- Nikola, a company with no revenues or real assets aspiring to make electric vehicles, saw its value reach $30bn (more than Ford) when it had listed for just $300mn in March largely because of it also taking its name from inventor Nikola Tesla like its older rival.

Let's look at Tesla further. Undeniably a very innovative company but quite clearly its outlook now is not as rosy as the start of the year. Its expensive products will suffer demand as a result of the global downturn, lockdown has caused production and supply problems, governments will have less available cash to subsidise electric vehicles and the price of oil has decreased significantly, making electric vehicles relatively not as attractive. Despite all these headwinds, as I write, the stock is up 138% just this year. Even Elon Musk himself has said that the share price is too high, yet it has carried on increasing even since then.

There is a lot of evidence to suggest that certain areas of the market are in bubble territory. The problem is, even if identifying overvalued stocks or markets, it does not mean that the bubble cannot carry on growing as was the case for tech stocks in 1998-1999. Valuations go out of the window until the bubble bursts or deflates but quickly become relevant at that point as investors look at intrinsic value rather than buying at any cost. It is not until then will the euphoric investors start to consider if the negative cashflow business models of the likes of Tesla and Netflix are sustainable.

There are large areas of global markets though that are offering very good value including some technology stocks. We are finding great opportunities, most notably in Asia and Australasia. More than ever we believe it is immensely important to be highly selective with stock picking and make sure that everything within portfolios offers good long term value and resilience.

Risk Warning: With investing your capital is at risk. Opinions constitute our judgement as of this date and are subject to change without warning. ◆

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