OLIVAR & ASSOCIATES
Global Investment Services

The Value Investor Note

Insights & Think Pieces for the Prudent Investor
November 17th 2017

Market Snapshot
DOW JONES: 23,271.28
S&P500: 2,564.62
NASAQ: 6,706.21

The Alibaba & Amazon Effect

Alibaba Group Holdings Ltd.'s Singles' Day generated a record $25.3B in sales. The vast majority of transactions were done via mobile, as the company handled a staggering 256,000 transactions per second. This 39% increase in sales topped analyst estimates, a positive sign for domestic demand in China.

Alibaba has publicly expressed intentions of making Single's Day a more global event, challenging Amazon, the goliath of the West. While Amazon stock was first to cross the $500B valuation, the two competitors remain similar in size and authority in their respective territories.

The tremendous success seen by ecommerce firms such as Alibaba and Amazon have translated to stock market outperformance the past 5 years, but from the perspective of an investor today, should we buy into the trend in hopes of continued returns over the next 5 years?

The first concerns are the valuations. These companies have attracted hoards of investors who continue supporting the share price, on expectations of continued exceptional growth. They have become overvalued by most metrics, and "priced for perfection". In the event that growth tapers, the share price could easily plunge. Another issue involves political risk. Amazon and Alibaba have been extremely harmful to traditional brick and mortar retail outlets. So much so, there are rumors they will soon be broken down and regulated by the government. While these firms are no longer considered "value investments", their paths of destruction within retail have created value investment opportunities.

Retail stocks continue their death spiral, but some are starting to show signs of life. Negative expectations are becoming increasingly overblown and many companies are "priced for bankruptcy". Regardless of whether or not Amazon has a realistic chance of putting the company under, share prices plummet. This is starting to create opportunities. As an example, an investor in Macy's Inc. (M) last week would have already returned over 10% as negative 3rd quarter earnings where simply not as bad as expected. Unlike Amazon or Alibaba, both with lofty expectations future, Macy's could easily outperform over the next few years for simply staying solvent.

A Note on Value Investing

Value investing is not always this simple, and requires both patience and a long-term time horizon. Returning to the Macy's example, take a hypothetical investor who bought the company back in May of this year, with the expectations that the company will not go out of business in the next 10 years. Despite the short-term 33% loss experienced this year, he can reasonably expect strong annualized returns in the future if his thesis plays out (that Macy's Inc. doesn't go bankrupt). Here lies the fundamental challenge. Value investing targets companies that are currently out of favor in the market, and picking the exact bottom is rare. Maintaining composure and the "buy and hold" mentality, value investing pays off over the course of a business cycle.