Businesses are doing well – Stock prices follow

The year has started with equity markets making a strong recovery. Sifter Fund NAV increased by 8.9% in January and YTD 11.5% vs comparison index 8.9 % (MSCI World). Even better is the news that Sifter invested businesses, particularly in the US, showed strong results in Q4

Why the upswing in equity prices?

There are always people, specialists, reporters, money managers etc. who claim to know what happened and then explain it afterwards. The most used clarification for the January rally were:

- End of year panic selling was over reacted, and market realized that the global economy and businesses are doing fine, especially in US.
- Trade war fears are partially postponed and there is a clear sign that China and US are both willing to reach an agreement.
- FED is not raising rates as fast as expected and thus encourages businesses to invest more and equities look more tempting that bonds.
- sentiment and expectations were so low in end of the year. However Q4 business profits have proven to be better than feared.

In Sifter investment philosophy we always avoid market timing and macroeconomic speculations. Yet, for Sifter investors, the last point "business profits" plays the most important role.

Less risks with Sifter Cylinder business

In a table below is presented the key performance indicators for Sifter businesses in the last 5 years. Those have been compared to the SP 500 market averages. One can easily see that Sifter's businesses are high quality and thus contain less risks.

Instead of speculating on countries, sectors or market timing Sifter strategy focuses on searching for quality businesses to be acquired on reasonable price (buy price / anticipated earnings). Currently Sifter Cylinder (portfolio) has invested in 30 businesses, in 17 sectors and in 10 countries.

Sifter 30 businesses	2014	2015	2016	2017	2018	S&P 500 2018
ROIC	14 %	13 %	14 %	15 %	16 %	11%
Operating Margin	20 %	20 %	22 %	26 %	26 %	14 %
Sales growth	2%	4%	8%	9%	9%	11%
Net debt/ Ebitda	0.4x	0.6x	1.0x	-0.1x	0x	1.6x
EPS*	12.8 €	11.9 €	11.6 €	14.6€	15.0€	n/a

Table 1. *Sifter invested businesses (30 companies globally) key numbers vs S&P 500*

ROIC (Return on invested capital) is important for us. We think it is one sing of a good company when creating added value in every euro/dollar invested in. In Sifter businesses, on average, ROIC (16 %) is better than e.g. S&P 500 businesses (11 %).

Operating Margin tells the business' ability to make profit for every euro they sell products or services. Sifter companies are clearly better (26 %) than one's in comparison (14%). We dislike businesses which have not proven to make money.

Sales growth is important for us but only when the business is making money. Sifter businesses' sales growth is slightly slower (9 %) than in comparison (11 %)

If Net debt/ebitda is high for a business but investments are well chosen and business is able pay off it's dept, it is not a problem. However, sometimes companies take too much risks in debt. That might lead troubles in finance cost and management attention is focused too much on survival and less in building the business growth. Therefore, Sifter businesses are mostly chosen debt free.

What next?

We do not know how the market will change or try to guess its movements correctly. We are aware of slower growth and political tensions in global economy. However, our focus is to see that the businesses we own remain strong. The secret sauce of being 100% invested in businesses is simple yet challenging. It requires a systematic process and tools to choose the best investment opportunities from the global equity universe. Our model has worked over 25 years and therefore we consider the Sifter equity elimination process and equities the safest asset class over other options.

Being the owner of good quality businesses makes you gain and feel safe.