

Thorntons Investments AIM IHT Portfolio

Markets Update

17th August 2020



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Summertime Blues

Although this has been a summer unlike any other, there is a faint familiarity of August torpor creeping into the markets. Typically, a time when the City empties (voluntarily) and activity and news slow down, the stock market seems to have settled into a range over the last month or two similar to summers past.

Of course, this is anything but a typical summer, or year for that matter. The stock market looks to be suspended between powerful forces for the moment. The eye watering 20% drop in GDP, in the second quarter, was a result of factories mothballing, construction being suspended and most of us being instructed to go home, not to travel and not to shop (apart for essentials). As some of these restrictions were lifted, activity started to recover, and GDP rose 8.7% in June. Indeed, the latest PMI activity surveys for July have turned positive almost everywhere and job vacancies are rising in the UK.

People are endlessly adaptive economic agents, so some activity did take place during shutdown: hands up who didn't order wine online? And those companies that assisted in new ways of operating (think Amazon and Zoom etc) have done extraordinarily well out of the crisis. Although there will be a return to past practices, years of structural change have in effect been packed into a handful of months. The corollary of this is that the sun has effectively set on many sunset businesses.

This has been reflected in markets, with tech stocks powering to new highs and trading on eye-watering valuations, whilst the more traditional cyclical stocks remain depressed and shunned. This has created the most bifurcated, or barbell, markets I have witnessed and raises the question of 'is there any value in value stocks'?

For the moment many of those in trouble are being effectively bankrolled by the government, or taxpayer ultimately. As support is withdrawn there is bound to be significant losses as they are unable to remain solvent. At the start of the Covid crisis our primary concern was to ensure all our portfolio companies could maintain solvency where they faced significant revenue loss. We remain very confident that this is the case. The next concern was the viability and vitality of their business in a new environment as we come out of the pandemic. Here we made some changes as reported in the second quarter factsheet.



As we learn to live with Covid it will likely feel like two steps forward, one step back. The just announced quarantine requirements for travellers returning from France and Holland is an obvious example. However, returning to the point about adaptability, Dart (Jet2) have also just announced that they are increasing flight and holiday capacity to Greece and Turkey due to demand.

The rise in Covid cases across Europe is causing concern, but it is not causing the same sort of rise in hospitalisation that we saw back in March. Better treatment, earlier diagnosis and the progress of vaccine development are all reasons for optimism.

This leads us to think that some value stocks really do offer value. An early example has been Scapa, which reported interim results earlier this month. Scapa has not been without its problems, with a slump in demand from auto and aero customers, and the loss of a major client last year. The company has moved swiftly to restructure operations and although the results still reflected how difficult business had been over the first half of the year, they were not as bad as expected. Scapa's share price jumped by 37% on the day they announced their interim results, and we expect we will see further increases as they win new business.



“Some of the best value may now be in more cyclical stocks”

Matt Strachan

We have written previously on the tech/growth exposure of AIM and the portfolio, but some of the best value may now be in more cyclical stocks where little, if anything, is ascribed for recovery.

To ensure diversity we have a number of these stocks in the portfolio and although we can't call when the value they offer will be recognised, we have growing confidence that they will be.

Matt Strachan
Chief Investment Officer, Thorntons Investments

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