

global investor by Jean Pierre Verster

War (what is it good for?)



Markets tend to be very efficient in discounting the impact of known events into the price of financial assets. Making investment decisions in reaction to market-moving events is therefore ill-advised. By the time an investor buys an asset that would obviously benefit from a recent event, or sells an asset that would clearly be affected negatively by such event, it is often already too late.

This is why the best default investment action in times of uncertainty is to do nothing.

At the same time, there is value in correctly allowing for what could happen next. Investors should analyse second- and third-order effects and visualise possible future scenarios (and what the fair values of various financial assets should be in such scenarios). This is easier said than done, as foreseeing how events could unfold represents a complex tree of probabilities that quickly branch off into thousands of possible permutations. The human brain is also predisposed to the base rate fallacy, which makes us particularly bad at estimating the true probabilities of contingent events.

What could increase the odds of being correct is to extend the time frame. This allows the phenomenon of reversion to the mean to play out. That is, over the long term things tend to revert to "normal". The problem with this approach in investment markets is that, in the case of regime change, prices tend to revert to a new normal, rather than to the previous mean.

Also, war significantly increases the risk of a total loss.

Keeping that in mind, here are a few global stocks listed in developed markets that have been affected by the war.

Ferrexpo

This London-listed company is the world's third-largest exporter of iron ore pellets. Its three iron ore mines are

all situated in central Ukraine. It has suspended exports and has sent force majeure notices to clients.

With revenue at zero, the company is estimated to have sufficient cash for one month's operating expenses. Shares are down roughly two-thirds since the start of the year and now trade at a historical p/e of less than one.

A safer option could be to buy shares in competitors that will benefit from Ferrexpo's lack of supply to the global iron ore market, such as Vale (which is listed in Brazil, with depository receipts traded in the US) or Rio Tinto (listed in the UK and Australia).

Epam Systems

Founded in 1993 and listed in New York in 2012, this company is a software engineering and IT consulting business with almost 60,000 employees. Of these, 14,000 are in Ukraine. Another 18,000 are employed in Belarus and Russia. This puts the company in an almost impossible position, as it straddles both sides of the conflict.

CEO Arkadiy Dobkin has come out in support of Ukraine, but has also been careful to not endanger his employees on the other side of the border, though services to Russian customers will be discontinued due to sanctions.

Shares in Epam Systems are down 70% in the year to date, but the company still has a market cap of roughly \$11bn and trades at a lofty p/e of 20.

Myronivsky Hliboproduct (MHP)

MHP is Ukraine's largest poultry producer. It's also a significant exporter of sunflower oil, wheat and soybeans.

Notwithstanding the current dangerous environment, MHP has not ceased production, to ensure the national food security of Ukraine. The company has indicated that significant unplanned losses have been incurred and that exports have been halted. MHP's London-listed

depository receipts are down 50% in the year to date and now trade at a historical p/e of 1.1, representing a market capitalisation of just under \$400m.

The better opportunity might be in the company's bonds, which now trade at a yield of 44%.

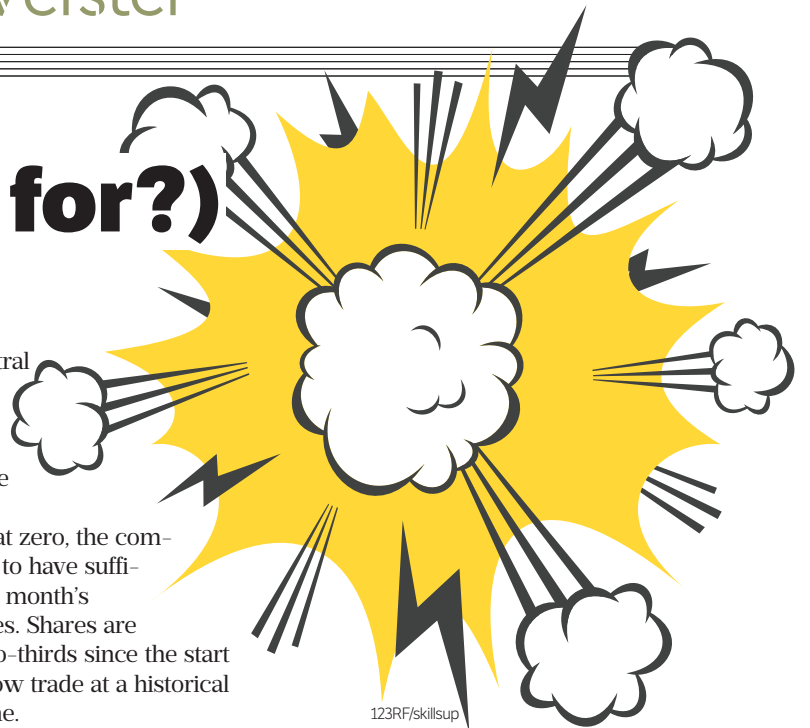
Defence stocks

War, by its very nature, is destructive. Instead of betting on an end to hostilities and resumed normality, one could take a grim view and rather bet on escalation. Unemotionally considered, defence stocks seem to offer an attractive risk/return opportunity in this regard. Shares in European defence companies such as Rheinmetall, Saab, BAE Systems and Thales have already risen sharply in the past two weeks. If increased defence spending is not just a one-off, there is more upside ahead.

The same goes for US-listed defence stocks such as Lockheed Martin, Northrop Grumman, General Dynamics and Raytheon Technologies. Some have even argued that by contributing to the defence of social values and liberties these companies are the new environmental, social and governance (ESG) champions.

With calls for more investment directed towards Europe's energy self-sufficiency also finding renewed support, the fuzzy concept of ESG investing might turn out to be another casualty of this unnecessary war. **x**

Verster is CEO of Protea Capital Management



123RF/skillsup

What could increase the odds of being correct [in forecasting] is to extend the time frame