Letter to stakeholders

Antwerp, 31 December 2020

Dear friends,

2020 serves as yet another excellent proof that predicting the future is impossible. This inevitably means that listening to pundits who claim to know what the near future holds, is a waste of time. At the start of the year, no-one could have possibly imagined the economy would grind to a halt as a result of massive government-imposed lockdowns. Markets correcting 30% in March was entirely justified since we were in uncharted territory and uncertainty reigned. Further, who could have imagined the straight-line recovery that would take us all the way back to where we started the year? The comeback rally proved resilient even to the news of further lockdowns as well as uncertain U.S. elections. Nothing could stop the party.

All of this is a great reminder of how forward-looking stock markets are. COVID-19 has become almost a non-event. What the market tells us today is that life will return to normal by the summer of next year. Some even speak of a 'Roaring Twenties' period as was the case 100 years ago, when the world economy got a resounding boost after the Spanish flu disappeared.

In terms of sectors, it was yet again the technology industry whose performance topped all others and carried the market. This makes sense in a world of lockdowns where the digital transformation accelerated at a record pace. What is more surprising is that defensive sectors such as consumer goods and pharmaceuticals are down in a year where the economy has taken a meaningful hit. Even more surprising is that they have significantly underperformed cyclical companies such as Arcelor Mittal or Ryanair who are in fact up on the year.

Taking a bird's eye view on the markets, it is clear that the divergence between growth and value has only strengthened this year. As was the case in previous years, growth companies were bid up, whereas a large part of the market remains effectively ignored. It is always tricky to compare different time periods, yet it is hard to ignore the similarities of today's market with that of the '90s, given features such as a vast number of unprofitable companies that fetch multibillion-dollar market valuations, IPOs doubling or even tripling on their first day of trading and indices that are dominated by a handful of companies.

Discipline remains, more than ever, the key. Do not overpay. High valuations imply high expectations and consequently the risk to disappoint only grows. Those who had the courage back in 2000 not to participate in the euphoric mindset of the moment and bought the least loved stocks ultimately fared best afterwards, largely avoiding the catastrophic consequences of holding the darlings of the moment that often no longer exist today.

A prime example is Warren Buffett. Back in January 2000, Forbes magazine was titled “Has Warren lost his touch?”. Since Buffett did not participate in the folly of Internet stocks, he had significantly underperformed the markets for two years in a row. Media quickly branded him as old-fashioned, no longer having the right strategy for good future returns. With hindsight, we can say that Buffett’s discipline generated a return of +36% in the 3 following years, whereas the markets lost -36%.

Today we see a similar story, with the media again suggesting Buffett has lost his touch, after an underperformance of 35% in the last two years. At the same time, there is no denying the master move he has made in Apple, now constituting roughly 25% of his portfolio. Taking into account history’s valuable lessons, we think it is highly likely Buffett will again outperform the market handsomely in the coming years.

Apart from Berkshire, we see a large list of undervalued stocks in our portfolio. We do not simply believe these have more upside potential than others, but more importantly deem the risk of loss due to multiple contraction as significantly lower.

Unsurprisingly, the best performing stocks in our portfolio this year mostly come from the technology sector: Netease, Tencent, NXP Semiconductors, Apple, Amazon, Alphabet, Facebook, Microsoft, Texas Instruments and Analog Devices. The other best performing stocks are DSM, LVMH, Sofina, Ageas, BNP Paribas, Peugeot, Arcelor Mittal and KKR. Some of these positions were bought during the year. As worst performing stocks this year we mostly see financials such as Citigroup, AIG, Markel and Fairfax Financial, but also defensive names such as Novartis, Merck, AB InBev and Inditex.

This year the euro proved to be one of the strongest currencies. This came at the cost of currencies in Latin America and Africa who depreciated significantly, but also the U.S. dollar lost almost 10% versus the euro. Inevitably this weighs on the performance of globally active companies where you can subtract 10% of their performance in U.S. dollar to obtain the euro result.

With respect to the fixed income part of our portfolio, it was a very active period due to the volatility during the year and we have ultimately generated a return of 4,5% on this part of the portfolio.

Despite COVID-19 Mercier Vanderlinden remains on a growth trajectory. In February we will open a new office in Waregem where we hope to welcome our clients in the region as soon as possible.

In 2020 we were looking forward to celebrating our 20th anniversary at a big event where we could thank all of you for your trust as well as the great collaboration we enjoy with you. Hopefully, we will be able to organize this in 2021 to celebrate our 21st anniversary.

For years we have had the habit of not sending out New Year gifts yet prefer to provide an equal donation to charity. This year is no different and the entire sum will go to the Anticancer fund which focuses on cancer research.

We wish all of you an excellent year 2021!

Thomas Vanderlinden *Stéphane Mercier* *Vincent de Pret* *Frédéric Van Doosselaere*

P.S.: Fund factsheets attached to this letter