PRESENTER: To discuss why growth stocks have got further to run, I'm joined now by Obe Ejikeme. He is a quantitative equity analyst at Carmignac. Well, Obe, the markets in 2018 seem to have behaved very differently to how they did in 2017; has something fundamental changed in the world? OBE EJIKEME: Well it's a difficult one. I'm really not sure if anything fundamentally has changed significantly. Some of the changes in the market behaviour have been in line with our expectations. I guess if you think that the world has come out of a one-and-a-half year to two-year process of recovering from the recession that we came out of in 2015 in emerging markets and commodities, then it's quite natural and quite normal for us to hit some sort of cyclical peak. And as you hit that cyclical peak and investors start to grapple with what the next 12 to 18 months are going to be like, the first thing you always see is a bit of volatility. And I think that's the one thing that people can definitely agree on this year has been there's been this increase in volatility since the start of the year. PRESENTER: You mentioned a cyclical peak, a peak in what? OBE EJIKEME: Well cyclical peaks and troughs are always difficult to analyse, and actually it's one of those things where you have so many different views. Part of the work that I do at Carmignac and the framework that I have is to try and identify points and inflection points when the market behaviour starts to discount that things going forward will be slightly different. So to me the definition of a cyclical peak is just where the growth data or the leading indicators of economic growth and activity have been rising so fast that on the margin you start to see a small about of deceleration. And that's a cyclical peak. It's just a regime change. Most things behave relatively normally. So you still see equities going up and people still feel relatively optimistic, but what changes is the dynamics of the market and what tends to lead you higher. PRESENTER: But, as you look at growth, do you think the market's got it right or wrong? OBE EJIKEME: It depends which way you're looking. So if we're looking backwards it's probably got it right. The question is about what happens going forwards, and that's really the big challenge. And in fact what's very noticeable this year together with the volatility is that lots of people are starting to recognise now that maybe the forward-looking aspect of growth is slightly different to what we've experienced in the last 12 to 18 months. And I think that's really the key to the regime shifts that we're talking about internally at Carmignac and certainly starting to position ourselves more effectively for. PRESENTER: So if we're in a world where there's less growth about, what happens? Do all companies just produce slightly worse results, or are there certain companies that do really well and everybody else does comparatively much worse? OBE EJIKEME: Well this phase of a cycle, so if I define it from the work and the framework that I have, I call it what we call scarce growth. Some people call it slowdown. I like scarce growth because what it essentially means is there's growth around; it's just going to be at a slower pace. Now no investors panic, generally, but what you do see is you start to see people paying a premium for the type of assets that will do well when growth slows. Bull markets are phenomenal. So when you're coming out of a recovery into what I call the speculative phase of the market where everything's going up, it's fantastic because all stocks participate, so everything goes up. The scarce growth phase is very different because what happens is the weakest members of the market start to struggle. So those companies which are classed as cyclicals, or have too much debt which is weighing them down, they start to struggle, so you get this investor shift into the growthier part of the market, or the names which have very strong balance sheets and that can do well when growth starts to slow. PRESENTER: So what are some of those quality growth companies? OBE EJIKEME: Well the one sector and what's interesting, the one sector that stands out in all of our quantitative analysis is the tech sector today. That's where we have significant positions in our book; probably more so than others and certainly more than our benchmark. But we feel relatively comfortable with that. Despite the recent volatility, we feel relatively comfortable because at the end of the day when growth slows you've got try and find companies that are able to not just grow their earnings but even grow their revenues. And that pool of assets and that pool of stocks is just getting smaller and smaller and smaller. So if you can identify the sectors and the types of stocks that do well, then you'll pick up those names. It's not just tech; there are other sectors as well that have stocks with those characteristics. PRESENTER: But a lot of those, and you mentioned tech there, has done really well if you look over the last few years. So what do you say to an investor who says but Obe they've done so well for so long it can't keep going on, it's time to take the bat off the table. OBE EJIKEME: Yes, so some of the points I'm raising right now are about the cyclical aspects of the cycle. So we had a cyclical trough in 2016; we've had a 18 months to two-year recovery. There's something structural going on here which is also part of the equation, which I think people need to consider. Coming out of the financial crisis, it's actually been, we've had a prolonged period of growth stock outperformance. And growth stocks typically outperform, or outperform value stocks, so the cheaper parts of the market, when growth is scarce. So one of the things I typically highlight when I'm talking about the style dynamics is this tells me that really we haven't had the kind of lift-off that we normally would have out of a financial crisis; hence why tech has continued to do well because it has the characteristics that do well when you have a benign subpar growth environment. PRESENTER: So if you are an investor that's in value as a style at the moment, what should you expect? OBE EJIKEME: I'd like to say you've got a brighter outlook ahead of you, but really for that to be the case you really need to see some of the growth-related indicators and the macro indicators. Most people follow things like the PMIs and the ISM manufacturing surveys and the German IFA indicators, but really for a prolonged period of value stock outperformance we need to see a prolonged period of growth acceleration. We did see it in 2016, and it lasted about six to eight months, but it wasn't prolonged. And that's partly because I think some of the structural reasons that were issues that we have with growth in general, let alone the debt issues that we face globally which haven't diminished either. PRESENTER: One thing people have been talking about this year is that growth around the world is synchronised; on balance is that a strength or a weakness for investors? OBE EJIKEME: Well I debate whether it's as synchronised as people think. Obviously it's great on the upside, whether it's emerging markets and Europe and US all firing on all cylinders at the same time, but I think you have to manage that risk reward in the same way both on the upside and the downside. So if there are chinks in the armour that we start to see and we certainly in the last three months have started to see some weakness in some of the data coming out of not just Europe, but also from other cyclical regions of the world like Japan, then you have to start to question in the same way whether this global synchronised acceleration could potentially become a global synchronised scarce growth slowdown. PRESENTER: And this period of what you described as scarce growth, how long does it typically stick around for? Is this an investment or a trading opportunity? OBE EJIKEME: Well I think it's an investment, and some would call it trading, it depends on your time horizon. I would call it an investment partly because the psychology of these moves, when they really take place it's very difficult for investors to avoid being involved in them. We just talked about the tech sector as a good example. Well it's very difficult as an investor to be out of tech stocks, given that they're the stocks that are leading the market higher. So you end up being caught up with it. The business cycle typically lasts between three and four years, which gives you 18 to 24 months on the upside, 18 to 24 months on the downside. It looks like we hit a cyclical peak in October into November last year. So in terms of how far we're into this, we're really only four to five months into investors starting to understand that something is not quite right with this cyclical or the synchronised global acceleration on growth. So let's say we're five months in. There's another at least five months to go before we get to the point where this becomes a bit more understood. PRESENTER: So how should investors think about valuation, particularly if they're looking at these stocks that you think and are predicting are going to benefit from scarce growth? OBE EJIKEME: Well, in my quant framework, valuation doesn't really fit into the way I look at stocks. I tend to focus on the style dynamics. Now we have other members of the team who do the valuation work, but I tend to focus on the style dynamics, so it's more about what you buy than the valuation of what you're buying. There is a significant risk that the stocks that you end up buying through this scarce growth phase will be at a higher premium to the cheaper part of the market; hence why the overall valuation of the market is a bit tricky. Let's put another way, if you're looking from a market valuation perspective, how do you put an underlying earnings number, which goes into your P/E of the market, how do you put an underlying earnings number on the market when the growth numbers going forward could be weaker? So the risk now for a lot of investors is the market valuations or their concept of market valuation may not be right based on where we're going. PRESENTER: And as you look at your quants models, if we're moving from a world of quantitative easing to one of quantitative tightening, how does that different environment affect the signals that come off your models and how you interpret them? OBE EJIKEME: Well I guess it depends on how you think that central banks interact with business cycles. Because at the end of the day it's all about what happens to the business cycle. You know, the theory and the belief is that when cycles tend to slow and you have decelerations in macro activity, what normally happens is central banks will step in, whether it's through QE or excess amounts of liquidity, to stimulate the growth cycle. Clearly what's very different this time around and we're going to have to wait to see how it plays out is that's not the mode that most central banks are in today. Most of them are looking to withdraw liquidity, quantitative tightening, or even further raise interest rates. And that's quite an unusual phenomenon for us to deal with as the growth cycle is starting to decelerate. PRESENTER: Now you mentioned the quants element that you input at Carmignac, how does that fit with the other parts of the investment process? OBE EJIKEME: Right, so we have a pretty sizeable team of not just macro analysts but underlying single stock fundamental analysts, and what we try to do is to marry all our macro work with a translation from macro to single stocks. Now I'm just one of the cogs in a very big chain of those who generate ideas for the firm and the discipline of my work is to focus on the quantitative aspects of it, but I try to, I like to think that it's a key element and an important part of the process of linking macro into underlying equities and single stocks. PRESENTER: So in summary what are the main opportunities and the main threats for equity investors today? OBE EJIKEME: So one of the first things I always say when I try and conclude where we are is every different phase of the cycle is an opportunity, so whether you're in the scarce growth phase, whether you're in the speculative phase. In fact actually what's rather perverse about the scare growth phase of the cycle for us is we can really differentiate ourselves as active managers from our peers because what typically happens is not all stocks go up. So we can start to look at alternative investment strategies from not just being long equities but for looking for specific short ideas. So that's one of the things I would say is it's not, each phase creates opportunities. In terms of where I think we're going to head is it's generally bullish for equities. So it's not about being out of the market, it's about being in the market. But the key thing is to be focused on the right type of assets. So being in the market, but being in stocks that do well when growth slows, typically higher quality assets. Typically some of the less cyclical assets in the market and typically the growthier assets tend to much better as people start to position themselves for a world where growth is not as strong as they perceived it to be previously. The other things that come with this are the natural things that tend to happen as people start to get a bit let's say concerned about the outlook as you start to see some increases in volatility. So that's one of the things that we've seen this year. We start to see issues with leverage and credit, which we haven't really seen yet, but these are the types of things that we'd expect to see play out over the next six to 12 months. And that's the type of investment environment that we're trying to focus on in terms of where we think the best opportunities are going forward. PRESENTER: Obe Ejikeme, thank you very much. OBE EJIKEME: Thank you.