



INTERNATIONAL SELECT



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Think like a scientist – but which one and when?

We hope that all of you and your families keep safe and healthy and follow the Covid-19 protocols. In the last few weeks, it has become clear that Asia mostly learned the lessons of SARS and how to deal with such outbreaks. Europe and the US did not and have not. This has made the global situation much worse.

It has also changed our evidence-based and probability-adjusted Bayesian scenario analysis to:

Scenario 1: 50% probability – an equity market bounce led by the same growth, quality, US, technology-type factor leadership.

Scenario 2: 10% probability – an equity market bounce led by deep value and cyclical-type factor leadership.

Scenario 3: 40% probability – equity markets keep falling, even from here, until the LTCM/Lehman-type bankruptcies emerge.

Thus far, as the Covid-19 crisis has worsened since our last update on 2 March 2020, our relative performance has been reasonable and we have not made any significant changes to the portfolio. We therefore do not have anything significant to add to that [special report](#). Our points about Modern Portfolio Theory not really working any more, machines/algorithms accelerating indiscriminate market sell-offs and the bleak outlook for oil and European banks all remain valid structural concerns for which we are striving to find portfolio solutions.

Those of you that know our investment process well (e.g. some clients/consultants who have been with us for 10-20 years - thank you for your longstanding trust and confidence in us) might remember that at very difficult times like these we have a time-tested decision making process wrapped around our 4-Dimensional investment approach. For those of you who know us less well, you may find the following a useful framework as you try to solve your near term investment-related problems:

1. How would a **chemist** see the current economic/market/human crisis?

- They would say: “Chemically nothing much has really changed, so carry on as usual.”

2. How would a **physicist** see the current economic/market/human crisis?

- They would say: “It is a classic phase transition (i.e. regime shift), like when water turns to ice.” They would adapt their behaviour patterns accordingly, while the chemist might perish still trying to swim - last heard saying “but it is still H₂O.”

3. How would a **biologist** see this economic/market/human crisis?

- They would say: “Look for the evolutionary changes that this shock to the system will inevitably bring.” Perhaps it will be fish that can walk, to extend the “water turning to ice” analogy.

Our 4-Dimensional investment process specifically recognises that different things work at different times and in different places: 1. Stocks, 2. Sectors, 3. Countries/Currencies and 4. Time/Change.

In normal times, Nudgem and I think and operate mostly like chemists – things don’t usually change that much.

During a crisis, we think and operate mostly like physicists – we don’t try and swim in ice, or ski in an avalanche, or pick stocks in freefall.

After the crisis, we think and operate mostly like biologists looking for the evolutionary changes from the shock of the crisis – e.g. the exciting new stocks and new themes that have learned or evolved to survive and thrive in the new environment.

This is how the two of us have sought to protect our clients’ capital in a relative sense during major crises over the last 20 years, and then go on to look for winners for our clients over the next 5-10 years. It has led to a radically different and outperforming portfolio each decade for our long-term clients. (If you’re interested in more of our forward-looking thoughts, please download our presentation [“Thoughts on winning the next decade”](#).)

The Achilles heel in our investment process is always the initial stage of every market recovery from a crisis. This is the so-called “dash for trash”, when the most beaten up, near-bankrupt stocks bounce the hardest. Never expect us to own them because they do not fit our investment process and this is such a difficult short-term trade to time correctly.

Until this crisis passes, we will continue operating mostly like physicists, trying to survive the phase transition (regime shift) and protect our clients’ capital as best we can in a relative sense in these crazy times. Then, at some point, we will see the signals to operate like biologists and buy the very exciting growth stocks and themes that have evolved to be the next decade’s major winners – e.g. clean & green growth, post-virus healthcare and digital economy and, for the even longer term, the hydrogen and circular economy.

Until then, we hope you and your families stay safe and healthy. We wish you all the best in these troubled times.

RISK CONSIDERATIONS:

Investors should note that investments in foreign securities involve additional risks due to currency fluctuations, economic and political conditions, and differences in financial reporting standards. Smaller company stocks are more volatile and less liquid than larger, more established company securities. The small and mid-cap companies the Fund may invest in may be more vulnerable to adverse business or economic events than larger companies and may be more volatile; the price movements of the Fund's shares may reflect that volatility. Fixed income securities will increase or decrease in value based on changes in interest rates. If rates increase, the value of the Fund's fixed income securities generally declines. Other risks may include and not limited to hedging strategies, derivatives and commodities.

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