

Rosefinch Research | 2022 Series # 26

Cool Thoughts on the Hot Stocks



In the past two years, we experienced the once-a-century pandemic, the first direct European conflict in 75 years, and a global inflation wave not seen for 40 years. A new age has dawned. The shifting industrial chains, divergent globalization views, and emerging recessionary worries are overhanging us like the dark storm clouds. But changes will always bring opportunities. The core of investment is to find direction in the fog of market, and bet on the new future trends. Once the fog dissipates, such opportunities will no longer exist. Finding these opportunities means identifying the “Beta of Our Time,” or as Buffett puts it: fish where the fish are.

Many people have heard the elevator story: three people take the elevator to the rooftop. Along the way, person A stood still, person B ran in place, and person C did pushups. When they arrived at the top floor, others asked how did they get up there? A said: I came up standing; B said: I came up running; and C said: I came up doing pushups. They all felt they made it to the top on their own, though none mentioned what was truly behind their rise. The “Beta of Our Time” is like the rising elevator – those who ride within it are more fortunate than those who took the stairs. **In investing, the successful Alpha is often built on the correct Beta.**

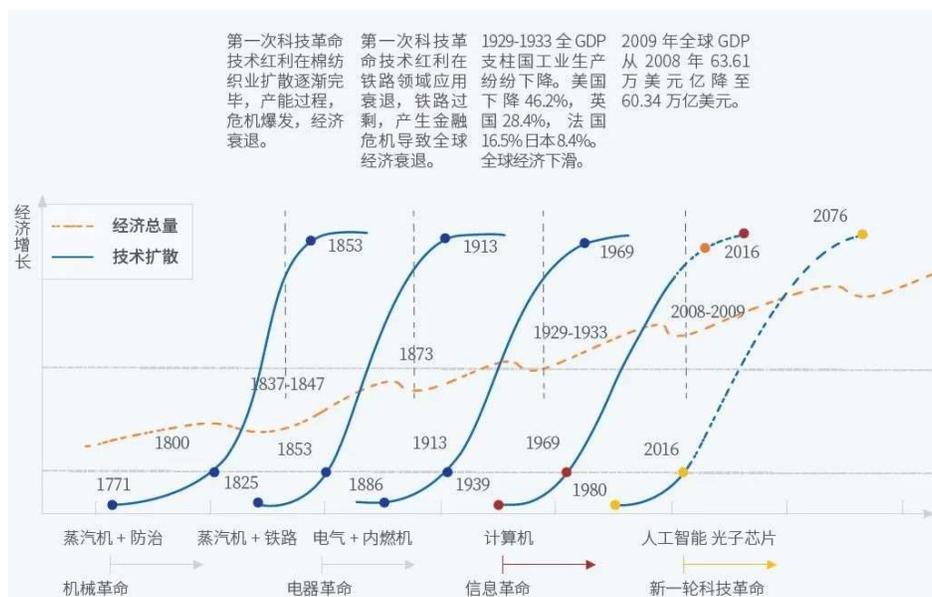
From early 1980s to mid-1990s, the globalization dividends paid off as China went through economic reform, Germany had unification, and US consumer goods accelerated global exports. US consumer sector became the best Beta of Our Time. Take Coca-Cola for example: it embarked on a fantastic

global journey and successfully penetrated diverse markets with different cultural and geographical backgrounds. Its global sales rose continuously, ROE went up from 20% in 80's to an incredible 55%, and the share price went up over 10 times compared to end of 1985. In 1988, Warren Buffett made his first investment in Coca-Cola, thus jumped on the speedboat in the wave of his time.

After the 2008 global financial crisis, internet moved from PC to mobile devices which gave rise to e-commerce and social media platforms and created new production channels. As the end-user product for the mobile internet, 2010's iPhone4 sales launched the smart phone age. Buffett was late to the internet stocks but did start investing in Apple in 2016 and increased his holdings to over 40%, becoming Buffett's most profitable investment in stock market. Even in 2022's turbulent year where FAANG stocks suffered greatly, Apple demonstrated resilience and is only down about 8% from the peak, contributing to Buffett's Alpha.

Across history, every age will create its unique leading industry. In the 1990s, with market economy dominating the scenes and personal incomes increased, household appliance demands skyrocketed. In the 2000s, China joined WTO and benefited from globalization, industrialization, and urbanization. In 2010s, information technology had waves of innovations that boosted internet wave. To use a mining analogy: capturing Beta is like finding a rich mine, while finding Alpha is like digging up the gold.

In the 2nd decade of 21st century, a new growth engine has started. Carbon-Neutral and affiliated technological innovations are revolutionary transformations on par with inventions like steam engine or electricity. In history, each technological revolution will bring about industrial chain shifts and economic structural changes, ultimately reflect in the capital market.



Source: Core Technology Institute, Rosefinch. The four major technological revolutions are mechanical, electrical, informational, and the new revolution we are experiencing now.

In our current technological revolution, we can also see how Chi-Next board's top stocks reflect the shifting industrial chain and economic structures in the 12 years since its inception. It's worth noting that battery and photovoltaic equipment account for almost 40% of the entire market cap. The top company in Chi-Next CATL is already in the top 5 A-share, with a market cap higher than the national oil or banks.



Source: Guosen Securities, Rosefinch.

2010-12: multiple sectors; 2013-15: media; 2016-17 agricultural & forestry, finance; 2018-20 biopharma; 2021-22: battery, photovoltaic

With the exciting waves of the Carbon-linked opportunities, a lot of hot money jumped in. Currently, there are already 43 mutual funds and 68 billion RMB funds with Carbon-Neutral or Low-Carbon investment themes. Countless other funds have also positioned heavily in new energy. Among the listed companies, many of them announced new energy initiatives, even if their core activities are in toys, paper, pigs, or milk. The existing market leaders are also aiming at each other's territory, encroaching from upstream to midstream and breaking the status quo in the process. **Competition in New Energy area is fierce and will become even tougher. In this scenario, a huge room for future development does not automatically mean everything we touch will be gold.**

On the one hand, with plentiful liquidity, stock prices have deviated from fundamentals with many over-extended company valuations, giving late investors limited upside or awkward position of high entry point in a volatile stock. On the other hand, in this dynamic market, the technological revolution will rewrite the commercial model and competitive landscape. We must redouble our efforts to closely analyze and track the emerging leaders and trends in New Energy. The technological innovations will lead to lower cost & higher efficiency, which will lead to explosive demand growth. This is the fundamental difference between new energy and traditional energy: the former relies on innovation while the latter relies on natural resources.

When people are investing on hot stocks, there are plenty of ambitions but not a lot of patience. By conducting deep industry chain research, we can position our investors with the future leaders before the hot money rush in. That will allow us to capture long-term values without getting trapped in the short-term trading. Of course, a correct decision does not guarantee a great result, while a wrong decision may get lucky. People tend to ignore the importance of decision process and mistaken luck for skill. **In the marathon of long-term investing, what we seek is repeatable success, which will require a mature investment philosophy. Our investment strategy must have a sound framework for each investment decision, and not just randomly following the market actions.**

Keynes once said: "... life is not enough – human nature desires quick results, there is a peculiar zest in making money quickly, and remoter gains are discounted by the average man at a very high rate." This "zest" reflects the animal spirit and can be an irrational behavior. In real life, many stories of catastrophic loss of wealth have their origins in the lure of "making money quickly." Gradually, people come to realize that in the land of investments, there are old investors, there are bold investors, but there are no old and bold investors.

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