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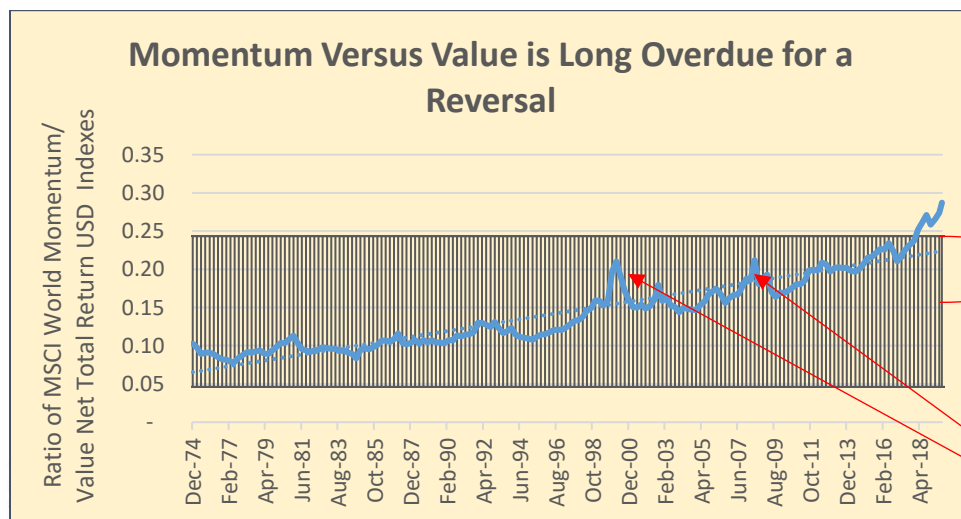
Outlook: Who's a Contrarian?

"Definition of contrarian: a person who takes a contrary position or attitude, specifically: an investor who buys shares of stock when most others are selling and sells when others are buying." Merriam Webster Dictionary

"A contrarian approach is just as foolish as a follow-the-crowd strategy. What's required is thinking rather than polling." Warren Buffett

As a value, active, and Frontier equity fund manager, Kyklos looks for contrarian opportunities. Each of those characteristics sits at a record out-of-favor point, or close to it. One-by-one:

Value: Most active fund managers consider themselves contrarians, in a belief that their trades are against current trends and anticipate future trends. The reality is that most managers are chasing past momentum rather than future trend changes, while ignoring valuation more than ever before. The illustration below compares world momentum stocks, which have already moved up, with value stocks, which have generally already gone down. Passive buying from index funds, quant, AI investors and the like, in effect, is momentum investing as well. Historically, note that when this momentum-to-value ratio hit the statistical mark of one standard deviation above neutral, momentum underperformed value for several following years. Today, probably thanks to the surge in passive flows (further below), the ratio is over double that level-- not necessarily a peak but certainly showing a stale trend.

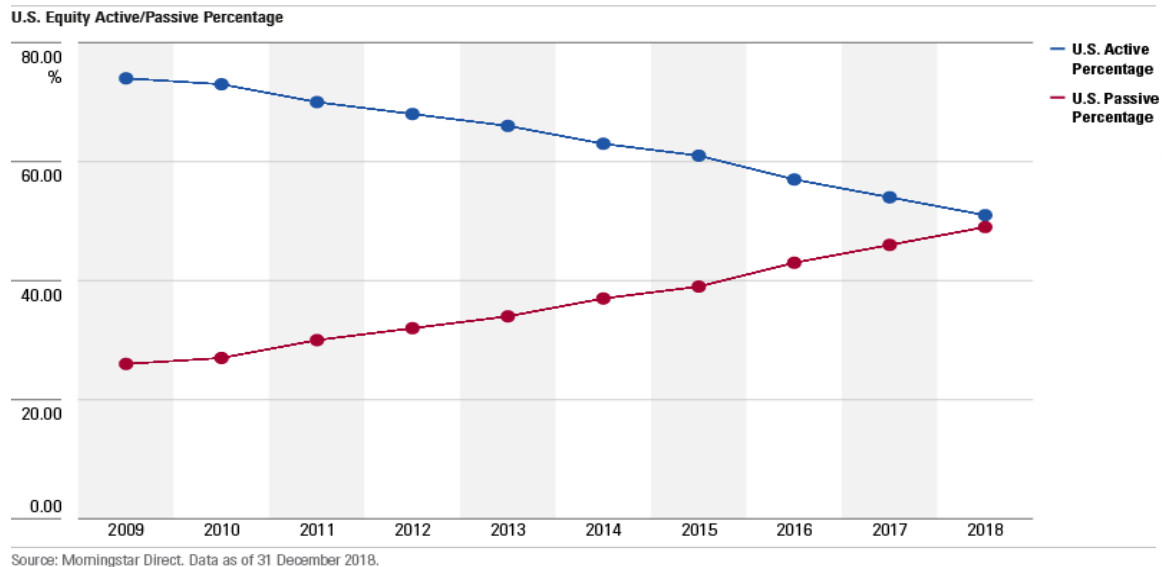


Sources: MSCI, Bloomberg

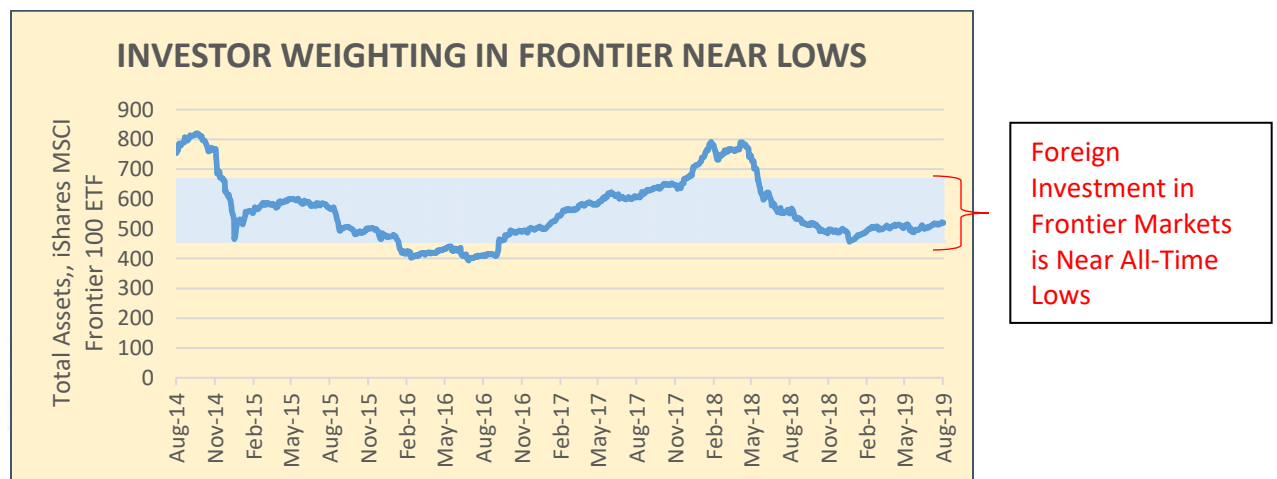
The ratio of momentum to value stocks is at an all-time high, an unsustainable 2 standard deviations above its long-term average. In the past, momentum underperformed value after reaching 1 standard deviation above.

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Active: Investors have already pulled much of their money from actively managed products globally (below). Frontier markets are a shelter from this trend because they require active management. Their lower trading liquidity and greater inefficiencies make them a largely no-go-territory for passive investors.



Frontier: As in 2015-16, investors have recently fled Frontier equity markets, offering an attractive opportunity to bet on a future rebound, seen here in the assets of the main Frontier ETF:



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Contrarian investing works, of course, because trends revert in the long term. Many market participants can recognize a moment, while few tolerate the inevitable uncertainty in order to take advantage of it. Calling all contrarians!

Charlie Gushee
August 30, 2019

Interesting August Reading

Damodaran on country risk: <https://aswathdamodaran.blogspot.com/2019/08/country-risk-mid-year-2019-update.html>

Why Nigeria's market does not reflect its 200m population: <https://medium.com/@drola/the-mystery-of-market-size-in-nigeria-a7c863f537bb>

Venezuela's Chavez/Maduro regime is a lot more reliant on Cuba than anyone thought: <https://www.reuters.com/article/us-venezuela-cuba-military-specialreport/special-report-how-cuba-taught-venezuela-to-quash-military-dissent-idUSKCN1VC1BX>

The bull case on Vietnam from trade sanctions on China: <https://www.barrons.com/articles/google-news-shows-vietnam-is-a-winner-in-the-u-s-china-trade-war-51567008823?mod=djem> Frontiers

Will Sudan's new regime anchor a new order in Africa? https://www.foreignaffairs.com/articles/africa/2019-07-19/what-happens-sudan-doesnt-stay-sudan?sp_mid=60221311&sp_rid=Y2d1c2hlZUBreWtsb3NjYXBpdGFsLmNvbQS2&spMailingID=60221311&spUserID=MzcOTM0NzU4Mzc1S0&spJobID=1703214676&spReportId=MTcwMzlxNDY3NgS2

Political fights threaten Botswana's Frontier success story: <https://www.economist.com/middle-east-and-africa/2019/08/29/the-battle-of-botswanas-big-men>

Foreign companies pay more than domestic ones—but it's because they go for more skilled workers: <https://www.economist.com/finance-and-economics/2019/08/22/who-wins-from-foreign-investment>

Gabon's cautionary tale for foreign investors: <https://www.economist.com/middle-east-and-africa/2019/08/15/why-many-foreign-companies-are-on-the-verge-of-leaving-gabon>

Hardship for Egypt's poor: <https://www.economist.com/middle-east-and-africa/2019/08/08/egypt-is-reforming-its-economy-but-poverty-is-rising>

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