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Investment Insights

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Investing involves risk. The value of an investment and the income from it may fall as well as rise and investors may not get back the full amount invested.

Investment Insights from Silicon Valley



Walter Price
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With over 40 years of experience of investing in technology companies, Walter Price has witnessed the evolution of the technology sector from the birth of the personal computer to the arrival of the internet and now the shift to cloud computing. Based in San Francisco, giving him close proximity to many of the world's most innovative companies, he heads up the Global Technology Team which manages US\$4 billion* in assets.

*Source: Allianz Global Investors GmbH.

European launch of the 'Gigafactory'

The 'Tesla Gigafactory' is coming to Europe. Chief executive Elon Musk said the group will establish its first major European factory just outside Berlin. This new factory, which will build batteries, powertrains and new cars may be just the ticket for the German car industry.

It has been a dismal year for German auto makers, whose weakness has contributed to a slide in the German economy this year. Trade war aside, many car companies in the country are struggling to make the transition to electric cars and if they can't, the future looks difficult.

BMW and Mercedes have brought out electric cars, which are well-engineered but aren't selling particularly well. It appears they haven't found the right price point to tempt consumers yet. This isn't an easy transition. There are over 100 German car companies, and we expect as many as half will fail to make the transition from petrol to electric.

It is perhaps no surprise, therefore, to see the German government offering Tesla strong incentives to build its European plant there. It will help create the infrastructure for electric cars. Marry this to German engineering and there should be success stories among the German car makers.

For the time being, these car companies still fall out of our remit. While we have looked at a number of conventional car companies, we don't yet see that it is technology driving them. Only Tesla falls into our universe at the moment, but we expect that to change if German carmakers can get it right.

The risks and opportunities in political advertising

Do politics and social media mix? It's been a question social media bosses, policymakers and users have been asking themselves as major elections loom in the UK and US. Online platforms have come under pressure to stop carrying political ads that contain false or misleading claims.

Facebook is keeping its political ads, ostensibly because it wants to defend open political debate, but also – perhaps – because it has proved a lucrative source of revenue. Either way, it has added the proviso that ads must not be misleading and will be fact-checked.

Twitter, in contrast, has said it won't take political advertising, with CEO Jack Dorsey saying "We believe political message reach should be earned, not bought." However, this decision has come under fire for hurting less-established candidates

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and also from the president's campaign, who labelled it 'dumb'¹.

Google has taken a more nuanced approach – it will allow advertising but has put limits on how those ads are targeted.

Election campaigns have typically been good for the advertising industry and this year looks to be no different. Ad agency Group M estimates that spending on political advertising will reach \$10 billion, up 59% from the 2016 election year². If social media can side-step any reputational damage, it promises to be a buoyant time for the sector.

Merger and acquisition boom

Deloitte's most recent study of M&A activity showed around three-quarters of tech sector executives expecting even bigger deals in the next 12 months³. This is higher than any other sector and the study showed an increased focus on buying a company in order to expand, rather than just for its technology.

There is a question, however, over whether companies should be making deals at this point in the market cycle. Valuations are high and we may be on the cusp of more difficult economic conditions. Are companies spending recklessly?

The answer is: it depends. If a company is sitting on piles of cash, has a history of making bad deals, or destroying value in the companies it acquires, then it should return that money to

shareholders. However, some companies have proved themselves capable of integrating acquisitions successfully.

M&A needs to be done thoughtfully – to plug a hole in an existing business and sustain growth, or to try and move into an alternative business. However, too often we see large companies guilty of a 'hit and hope' acquisition strategy.

Good idea versus good business

The history of technology is littered with great ideas that didn't cut it as a business, reminding investors that there is a world of difference between concept and execution. Part and parcel of being a technology investor is not being seduced by a good idea but instead understanding each company's path to profitability.

When we often meet prospective initial public offerings (IPOs), our 'sanity test' will look at whether they can make money in the longer-term. Are they too optimistic on their projections? Are they underestimating the competition? Is the company clear about the milestones it needs to hit?

That is not to say that every company needs to be making money. We were early investors in Salesforce.com – and remain investors today – but it was unprofitable for a long time. We believed the business model would eventually be profitable and the management team did a good job of being clear about its targets and then executing on them.

There is a real danger in valuing companies based on revenues and we have seen this too often in the private equity sector. When companies come to public markets, they are subject to greater scrutiny. Investors will vote with their feet if they don't like what a company is doing. Today, we see more of an emphasis on making money than has been present in the recent past.



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1 <https://www.newscientist.com/article/2221935-twitter-bans-all-political-ads-because-they-can-influence-votes/>

2 <https://www.forbes.com/sites/bradadgate/2019/09/03/the-2020-elections-will-set-another-ad-spending-record/>

3 <https://www.computerworld.com/article/3412327/notable-technology-acquisitions-2019.html>

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