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Technology share rally: USA head and shoulders above the rest

Dieter Kerschbaum



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After a strong set-back in December 2018, technology shares have staged a fantastic comeback in the first four months of the year. IPOs like the ones by the transportation network companies Uber and Lyft or by the online graphics provider Pinterest have drawn attention from the media. The profits of most technology companies have also matched or slightly exceeded expectations. What caused the latest rally? What does the technology sector benefit from, and what perspectives do investors have? This is what we were discussing with Bernhard Ruttenstorfer, Senior Fund Manager of [ESPA STOCK TECHNO](#).



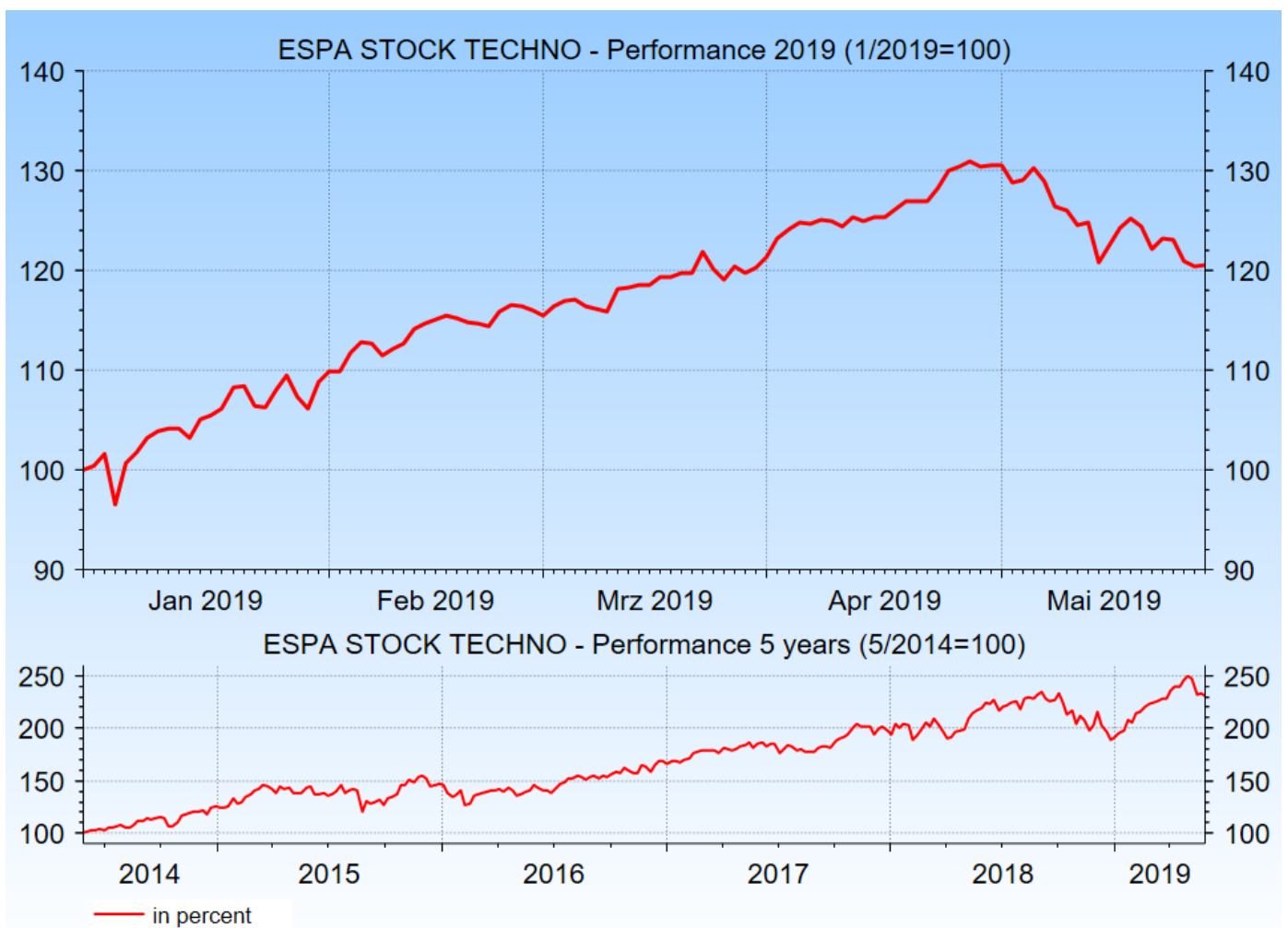
*Bernhard Ruttenstorfer,
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In your opinion, what are the reasons for the strong performance in 2019?

The rally in Q1 was largely due to the excessive losses in Q4 2018, which was an irrational sell-off. In Q1, investors have used the lower prices to build positions in the technology sector. This is of course based on a positive outlook on business, which the market expects to improve further from 2020 onwards. The equity market has this expectation already priced in. Q1 company earnings have matched or even exceeded expectations. Software companies have been particularly convincing. We regard 2019 as year of transition, with only minor earnings growth.

Are equities overvalued at this point or do you still see potential?

A price increase of about 20 percent (source: Reuters on the basis of a global technology equity index) within a few months does of course affect the valuation. But we have to differentiate: there are segments with very ambitious valuations such as for example some providers of cloud software and mobile payment services. As far as the latter ones are concerned, the valuations are largely justified because the market is growing significantly, and companies are profitable and only subject to minor earnings fluctuations. Here, we are talking about companies like Paypal, Mastercard or Visa. They are the structural winners in payment transactions and have benefited from changes in consumer behaviour, which manifests itself in more transaction via internet and smartphones. The semiconductor market is attractively valued. Here, we saw a slump in the second half of 2018. Now the market is on the rebound with demand recovering. Overall, the valuations in the technology sector are still attractive, and there is no reason why prices should not rise further.



Quelle: Thomson Reuters Datastream

Note: Past performance is not indicative of future development.

What are the themes that have potential? What are the key aspects of your investment strategy?

All of them are innovations that are or will be affecting the cycle of products, their production, sales, and distribution all the way to the consumer (please see the box "The drivers of the technology boom"). We can see themes like automation, the Internet of Things, Artificial Intelligence, self-driving ("autonomous") cars, mobile payment transactions, cyber security etc.

As far as software is concerned, cloud outsourcing is still a hot topic, as is video gaming with its gigantic growth prospects, and in connection with it the payments transaction providers. In the [ESPA STOCK TECHNO](#) funds we currently prefer software providers: prices fluctuate less significantly than for semiconductors. The product prices are just more stable.

Companies like Lyft, Uber, and Pinterest have done IPOs this year. Are there any other technology companies in the pipeline? How important is the stock exchange for such companies?

The USA is the engine of innovation and therefore also head and shoulders above the rest when it comes to the stock exchange: US stock exchanges see the biggest and most important IPOs. Also, the share prices in China have been affected more severely by the trade conflict than US tech companies. One example is Huawei, which was put on a black list - a move that blindsighted the stock exchanges. This means that US companies cannot supply Huawei with products any longer. This is of course a hurdle and detrimental for both parties to the conflict. I am convinced that that trade conflict will ultimately only be a source of irritation though. It does not change the radical shift that companies and consumers are subject to (on the basis of virtual reality). Many sectors have to brace themselves for significant changes: from car dealerships to print media.

The drivers of the technology share price rally

(source: www.fondsprofessionell.at; www.pwc.at)

Ultra-high-speed mobile networks

This year the new mobile telephony standard 5G will be launched. As a result, data volumes thousands of times bigger than currently will be transmitted at rates of up to 10,000 megabits per second through the mobile networks – i.e. 100 times faster than the current LTE standard 4G. For the first time ever, groups want to make use of this technology, too, which will create completely new industries and services. 1.5bn 5G contracts are expected for 2024.

Big business e-gaming

E-gaming has turned into a multi-billion-dollar market, having moved out of its niche a while ago. Changes in user behaviour such as increased mobile use and technological innovations cause paradigm shifts. For a while now, big e-commerce players such as Amazon et al. have increasingly tried to make inroads into this field. According to a PWC study, the market size is to double to USD 1.6bn within the coming four years Dollar.

Cloud services: high cost savings

The hard drive contains less and less data. Companies are shifting towards cloud computing in order to save costs in the long run. The cloud business is booming, offering IT service providers, IT outfitters, and software providers numerous opportunities. Analysts expect global cloud revenues to increase from USD 200bn to USD 500bn by 2026.

Growth sector digital media

The young people still watching TV nowadays have become a minority. Instead, they use their iPad or laptop to watch Netflix, Amazon Prime or YouTube. Once this generation grows up and has more purchase power, the ad market will be slipping from traditional print media to internet-based media. This is already the case, albeit at low levels (and thus comes with high growth potential). In particular, two companies should be among the winners: Google/Alphabet and Tinder.

Artificial Intelligence (AI)

Self-learning systems and intelligent software are sustainably revolutionising the economy. The topic of AI is about to turn into a megatrend. According to PWC, the growth potential until 2030 is USD 15,700bn. Big Data is the new Oil. Whoever uses the data best, will be at the top. However, the share price valuations are already quite ambitious.

▲ Risk notes according to 2011 Austrian Investment Fund Act

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