



# Value in Tech Stocks

Artisan Partners U.S. Value Team

ARTISAN PARTNERS  
**Insights**

For Institutional Investors Only — Not for Onward Distribution

## Value in Tech Stocks

The mantra of classic value investing is well summarized by Warren Buffet's aphorism: "It's far better to buy a wonderful company at a fair price than a fair company at a wonderful price." We operate in that spirit but use our own time-tested philosophy of finding cash-producing businesses in strong financial condition that are selling at undemanding valuations. These are our margin of safety criteria, and we employ them consistently. By doing so, we invest opportunistically. When we judge that a business meets our standards, we invest. Furthermore, we're benchmark agnostic, willing to step into any situation that meets these criteria, regardless

of whether the company is categorized by indexers as value or not. It's not uncommon now for large, diversified and mature technology companies to screen well on our criteria, even if the media and market still liken them to the growth-oriented startups they once were. Today, Facebook, Alphabet and Apple are mature, cash-generating businesses with dominant industry positions. Those attributes can potentially satisfy two of our margin of safety criteria. Then, if valuations move in our favor and meet our third criterium, we are comfortable acting opportunistically to own part of these businesses.

### Facebook

At the time of purchase in the Value portfolio in April 2018, we believed we could get our arms around Facebook's downside, including its increasing capital and operating expenditures to improve privacy protection in ways necessary to restore users' trust and protect the company's network effect. While Facebook was historically a growth-oriented company, it has matured into a name that meets our disciplined investment criteria. We consider Facebook a dominant social media platform that has monetized well both desktop and mobile platforms—indeed, it set the standard. Its healthy balance sheet and strong free cash flow make us comfortable

investing. We take the concerns around privacy and compliance seriously and expect higher expenses and capital expenditures over the near term. That said, we believe Facebook is taking the right steps to repair its image, as the network effect is its most enduring asset and user trust is of utmost importance. Its Instagram platform is becoming a force all its own, with approximately 1 billion users. Based on our time-of-purchase valuations, Facebook's Instagram assets were essentially free—not bad when we estimate those assets could be worth \$50 billion to \$100 billion.

		3-months Prior to Purchase 1/9/18	Purchase Date 4/9/18	Change (%)
<b>ROE</b> (1yr fwd consensus estimate)	<b>Facebook</b>	21	24	—
	Russell 1000® Growth Index	14	14	—
	Russell 1000® Value Index	31	33	—
<b>PE</b> (1yr fwd consensus estimate)	<b>Facebook</b>	18	15	—
	Russell 1000® Growth Index	15	14	—
	Russell 1000® Value Index	19	18	—
<b>Price/Index Level</b>	<b>Facebook</b>	188	158	-16
	Russell 1000® Growth Index	1246	1170	-6
	Russell 1000® Value Index	1403	1350	-4

Source: Bloomberg. **Past performance does not guarantee and is not a reliable indicator of future results.** Purchases after the initial purchase date in the portfolio may continue for an extended period of time, and the difference between the price at the initial purchase date and the current price may not be an accurate indication of the gain or loss in the portfolio. Purchase prices are based on the end-of-day security values and may not be representative of the holdings' initial intra-day purchase price.

## Apple

Apple is a mobile technology leader with one of the strongest brands and best balance sheets in the world. We have held Apple in the portfolio since Q2 2011. At that time, our opportunity to invest in Apple came about as its share price had not kept up with its dramatic earnings growth and cash build over the prior few years. Consequently, Apple's price-to-earnings multiple contracted from roughly the low 30Xs in the years leading up the global financial crisis to near 15X at our time of purchase. Following sharp price gains and slowing growth, sentiment weakened in late 2012, and shares fell through the first half of 2013. The stock went

from a growth investor darling to relatively un-loved in the span of a year. But we don't think much really changed for the business. Like Samsung Electronics, which we also hold in the portfolio, Apple has a dominant position in smartphones and tablets, but it also has its own proprietary operating system. Apple sells at a low double-digit multiple based on our view of normalized earnings. Thus, we were able to buy a premier brand with strong business economics and a stellar balance sheet at a discounted valuation.

		3-months Prior to Purchase 1/14/11	Purchase Date 4/14/11	Change (%)
<b>ROE</b> (1yr fwd consensus estimate)	<b>Apple</b>	27	29	—
	Russell 1000® Growth Index	12	12	—
	Russell 1000® Value Index	23	25	—
<b>PE</b> (1yr fwd consensus estimate)	<b>Apple</b>	15	13	—
	Russell 1000® Growth Index	11	11	—
	Russell 1000® Value Index	13	13	—
<b>Price/Index Level</b>	<b>Apple</b>	50	47	-5
	Russell 1000® Growth Index	657	669	2
	Russell 1000® Value Index	592	603	2

Source: Bloomberg.

## Alphabet (Google parent)

Google is a leading global online advertising company. Google has a dominant share of online search, is one of the top consumer brands worldwide, consistently generates strong returns on equity, and sports a healthy net cash position. Like consumer electronics giant Apple, Google may seem an odd pick as a value investment due to its remarkable growth over the past decade. Yet like Apple, Google's share price has not kept up with its earnings growth and cash accumulation. In fact, over the five years prior to our purchase of shares in December 2014, the valuation

(one-year forward PE) compressed from about 26.00X to as low as about 13.00X, as earnings per share grew 2.25X. Cash on the balance sheet was also up approximately 2.50X. To be sure, there are near-term concerns about deteriorating global macroeconomic conditions and longer-term worries about competition from social media players, but the company's long-term fundamentals look strong to us. We think we are purchasing the dominant search business at a discount and getting the rest of the company (Android™ mobile operating system, YouTube™, etc.) for free.

		3-months Prior to Purchase 9/20/14	Purchase Date 12/19/14	Change (%)
<b>ROE</b> (1yr fwd consensus estimate)	<b>Alphabet</b>	18	17	—
	Russell 1000® Growth Index	13	12	—
	Russell 1000® Value Index	29	30	—
<b>PE</b> (1yr fwd consensus estimate)	<b>Alphabet</b>	19	17	—
	Russell 1000® Growth Index	14	15	—
	Russell 1000® Value Index	17	18	—
<b>Price/Index Level</b>	<b>Alphabet</b>	594	515	-13
	Russell 1000® Growth Index	1010	1032	2
	Russell 1000® Value Index	936	967	3

Source: Bloomberg.

## Investment Results (% USD)

As of 30 June 2020	Average Annual Total Returns						
	QTD	YTD	1 Yr	3 Yr	5 Yr	10 Yr	Inception
<b>Composite — Gross</b>	<b>19.20</b>	<b>-14.82</b>	<b>-5.53</b>	<b>2.27</b>	<b>5.83</b>	<b>10.17</b>	<b>7.19</b>
<b>Composite — Net</b>	<b>19.01</b>	<b>-15.12</b>	<b>-6.18</b>	<b>1.57</b>	<b>5.10</b>	<b>9.40</b>	<b>6.37</b>
Russell 1000® Value Index	14.29	-16.26	-8.84	1.82	4.64	10.40	6.23
Russell 1000® Index	21.82	-2.81	7.48	10.63	10.46	13.96	8.90

## Annual Returns (% USD) 12 months ended 30 June

	2016	2017	2018	2019	2020
<b>Composite — Gross</b>	<b>3.66</b>	<b>19.72</b>	<b>10.97</b>	<b>2.05</b>	<b>-5.53</b>

Source: Artisan Partners/Russell. Returns for periods less than one year are not annualized.

**Past performance does not guarantee and is not a reliable indicator of future results. Current performance may be lower or higher than the performance shown. Composite performance has been presented in both gross and net of investment management fees.**

**Investment Risks:** Investments will rise and fall with market fluctuations and investor capital is at risk. Investors investing in strategies denominated in non-local currency should be aware of the risk of currency exchange fluctuations that may cause a loss of principal. These risks, among others, are further described on the next page, which should be read in conjunction with this material.

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Net-of-fees composite returns were calculated using the highest model investment advisory fees applicable to portfolios within the composite. Fees may be higher for certain pooled vehicles and the composite may include accounts with performance-based fees. All performance results are net of commissions and transaction costs, and have been presented gross and net of investment advisory fees. Dividend income is recorded net of foreign withholding taxes on ex-dividend date or as soon after the ex-dividend date as the information becomes available to Artisan Partners. Interest income is recorded on the accrual basis. Performance results for the Index include reinvested dividends and are presented net of foreign withholding taxes but, unlike the portfolio's returns, do not reflect the payment of sales commissions or other expenses incurred in the purchase or sale of the securities included in the indices.

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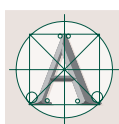
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