Educated Investing

Value Investing & the MPSIF Value Fund

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When we returned back to school in January 2009 after a long winter break, the stock market was in a precipitous decline. Nobody knew if this was going to be the worst depression since the Great Depression or if we were going to witness another Great Depression. Members of the Michael Price Student Investment Fund (MPSIF) Value Fund had the arduous task of identifying value investments.

So let us begin by first explaining what “value” investments are. Basically, it means stocks that offer more underlying value than the stock price currently reflects (we are always looking for ideas, so in the event you found a ridiculously undervalued stock for your Damodaran project, please let us know). The tricky part for investors is finding the fine line between an undervalued stock and the market reaction going forward (some stocks may remain undervalued for the next decade and as a result, you would have been better off investing in something else). Additionally, we are not in the same business as the most well-known value investor, Warren Buffett, who buys a railroad company with the comment: “we will hold it forever.”

The other issue faced by value investors is not to fall into the “value trap.” In January, majority of stocks looked undervalued. Looking back, we wish we bought Citi for $1 or General Electric for $6. But the reality is that we did not buy them due to the uncertainty –there was a real possibility that the world markets would implode or these companies would go bankrupt. As such, the Value Fund focused on investing in stocks that were undervalued and expected to survive the crisis (i.e. healthy balance sheet, sustainable competitive advantage).

The Value Fund did a great job of implementing a defensive portfolio, however, when the markets turned around in March after hitting a low, the portfolio was not in a position to benefit as much from the rally. We slowly began introducing less defensive names into our portfolio beginning in the Spring semester and after returning back to school this Fall, Value Fund analysts once again focused on finding companies expected to outperform given the “bullish” environment. Furthermore, the Value Fund increased its exposure to the Energy, Financials, Healthcare, and Materials sectors, which were identified by our sector analysts to be well-positioned for outperformance, by purchasing ETFs. The fund’s objective is to replace the ETFs with specific stocks as value opportunities are identified. Nevertheless, we remain cautious given the recent market rally and as such, have continued to maintain position in defensive names that we believe will outperform when things begin to normalize.
For the Value Fund, the question remains whether we should pick stocks that will fare well given the recent market upturn or invest into companies that we think will outperform given our future projections. Investing in financial markets is harder than it sounds, especially when you are managing real money for someone else. If you want to gain some hands-on experience while you are attending Stern, we would strongly suggest applying to MPSIF.