ECONOMIC COMMENTARY - By Dr. Francois Stofberg

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TECHNOLOGY REIGNS SUPREME

August was a good month for global markets. The MSCI World Index of stocks in developed markets was up 6.6%, its sharpest rally since 1986. The average move over the last 44 years, up or down, was less than half of that. The broader All Country World Index, which includes developing countries, gained 6.3%, its best run-on record. The best single performer was Tesla, that jumped 13% on one day to complete a 74% rally for the month. In total, Tesla is up by more than 495% this year and has added upwards of $389 billion in market value.

Like Tesla, many of the current stock market activities cannot be completely understood. A major driver of stock market performance is, of course, the unprecedented measures taken by governments and monetary authorities around the world, especially in the rich world. Support aimed at stabilizing economies and markets provided an influx of liquidity to equities but also improved their relative attractiveness. Aid kept consumption upbeat by keeping businesses alive while much of the tax breaks to households ended up invested, rather than spent. The type of support put a lot of pressure on bond yields and helped to push up inflation (read growth) expectations, especially in the United States. All of which favour equities as an asset class.

But among equities, not all are equal. If the black swan that is COVID-19 showed us anything, it is that some industries are a cut above. Two years ago, Apple became the first United States company to reach a valuation of $1 trillion. Shortly after that the stock shrunk back by almost 30%. Now, the company is worth more than $2 trillion and the United States boasts four firms with a valuation of more than $1 trillion: Apple, Microsoft, Alphabet, and Amazon.

Among the different industries, a major and persisting trend is the outperformance of technology stocks, which can to a certain extent be explained by the composition of these firms. Unlike pure industrials, or some other type of firm, technology, especially software technology, requires far less costly expenditures like deep exploration drills or gigantic factories. You can start a tech unicorn in your garage and reach a billion-dollar valuation with a handful of employees, probably still in your garage. It would be more difficult to do the same in the mining or manufacturing industries. Technology firms have perfected the game of low overheads and scale, i.e. virality. Consider the latest addition: TikTok. Four-year-old Tiktok is currently valued around $75 billion, close to the 70-year-old Sasol, but only employs 2 000 individuals, compared to Sasol's 30 000. Both made about the same profits during 2019, but 2020 will, of course, look vastly different. Unlike industrial mines or manufacturers, Facebook, Google, Netflix, TikTok, and the like, seem to be recession-proof. It seems only regulation will be able to provide a persistent threat to these firms. Competition seems to take a back seat, most of these tech titans spend more on research and investment than South Africa spends on education or healthcare, and far more effectively so. Tech stocks are probably too expensive, but "too" is a subjective concept that many believed about Apple two years ago. Maybe we are still missing something?

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