Aberdeen Global Technology Equities

Fund Manager Interview
July 2014

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Key fund points

- Bubble fears are overplayed outside certain social media stocks
- Our broad definition of the tech sector includes companies with a focus on tech innovation and those which will benefit from longer term growth trends
- Oracle Corp, Fanuc, Intel and Visa are among the global names in our portfolio

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What has happened in the technology sector?

Tech stocks suffered a sharp sell-off in April this year due to profit-taking and heightened risk aversion. This followed a run-up in the sector starting last year, led by social media stocks such as Facebook and Twitter.

While comparisons with 1999 are apt for some stocks, this time around companies do at least have earnings. The problem is how companies will monetise growth to the degree suggested by valuations. Twitter is trading at over 800 times price-to-earnings for FY2014. At the same time, there's been a wave of high-profile acquisitions among social media companies (Facebook's purchase of Whatsapp for US$16 billion, for example), as they look to spend excess cash and diversify their bets.

So what are the sector's prospects?

We are still anticipating a pickup in US demand. Until that appears more self-sustaining, however, companies are going to find it difficult to eke out higher returns. Timing apart, renewed IT spending will be spread across developed markets, not just the US, as companies look to replace or upgrade their existing hardware for the next cycle. We expect a moderate recovery in PC demand, as the rapid growth in tablet slows. The smartphone market should also remain resilient.

Can you give an example of a growth area within the technology sector?

One example would be 3D-printing whose huge potential across a wide of range of industries is rapidly becoming apparent. But like many new technologies, it's often a matter of timing and knowing where the true commercial uses lie and when the market will take off.

The Internet of Things (IoT) is shaping up to be the next megatrend. Can you tell us more about it?

The IoT is the third (and likely biggest) wave of the development of the Internet, after the rise of the fixed internet in the 1990s and the mobile internet in the 2000s. Broadly defined, IoT describes the connection of devices such as every day consumer objects and industrial equipment to the internet. One estimate is for that 28 billion 'things' to be connected by 2020, including devices such as wearable technology, cars, homes and even entire cities. Sectors that are poised to benefit include CommTech and Semiconductors while companies such as Cisco, a provider of networking equipment and Qualcomm, an industry leader in wireless technology and services, are well-placed to gain from increased demand. We hold both stocks in our portfolio.

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What do you make of China's homegrown tech sector?

National champions such as Alibaba and Tencent have flourished as domestic demand for internet services and e-commerce has risen exponentially. At the same time, they have moved into new (and unrelated) business areas in the absence of an established technology infrastructure that in the US constrains such expansion. As an example, Alibaba, China's biggest e-commerce company, now manages the mainland's largest money market fund, Yu'e Bao. Furthermore, these companies have also chosen to list in the US with dual-class share structures which awards majority shareowners more rights than others. This raises corporate governance red flags for us.

Name some holdings and say why you own them.

We favour industry leaders with robust balance sheets, stable cash flows and a conservative management team. Some of the names we own may not appear to be pure tech companies. But they have a strong focus on technological innovation (Japanese robotics maker Fanuc), and will benefit from longer term growth trends such as the increasing popularity of mobile banking (electronics payment network Visa comes to mind). Examples of other holdings we like include leading US-based software supplier Oracle Corporation, Taiwan Semiconductor (TSMC), the world's largest dedicated semiconductor foundry, Cognizant Technology Solutions, a provider of IT consulting and technology services and last but not least, US-based chip-maker, Intel.

Intel released an upbeat assessment of the PC business. Do you share that optimism?

We are skeptical. The PC industry had a tough 2013 and the operating environment is likely to remain challenging. That said, we are long-term believers in Intel's ability to diversify beyond the traditional PC business, with its focus on innovation and new product development. In fact, we have added to the stock over the last six months, on share price weakness, as valuations became more appealing.

Have you added any new holdings?

We introduced global payment services provider Visa for its high-quality business and attractive long-term prospects. We also initiated engineering software designer Aveva, French 3D design software company Dassault Systems and Japanese sensor systems maker Keyence on attractive valuations. Against that we sold Adobe Systems, IBM and Texas Instruments in favour of better opportunities elsewhere.

What importance do you attach to your active stock picking approach?

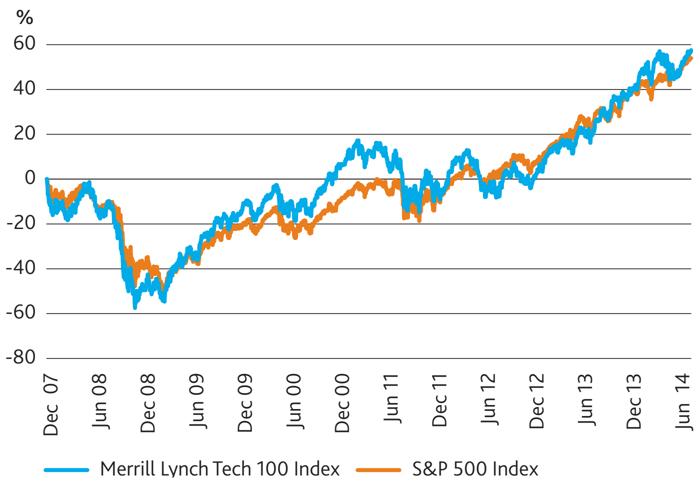
Stock selection is what sets us apart. We do our own company research and if a stock fails our screens we won't own it. Furthermore, no company is bought before we meet the management. Unlike many fund managers we're long term in our focus. That means we go back and visit companies again and again. The benefit of this is to isolate only the well-managed ones that have attractive long-term prospects and which represent good value. It's important for us to focus on price as well as quality – there's no point in overpaying however attractive a company might be.

Do you consider the holdings in the benchmark when you make stock selection decisions?

No, our active management presupposes we choose stocks independent of benchmark constituents. As mentioned, our decisions are an outcome of our research discipline, with quality and price the two key filters. We are always aware of the benchmark, but that's mainly for performance comparison – never for portfolio construction.

Chart 1: Tech stocks have delivered strong returns since 2013

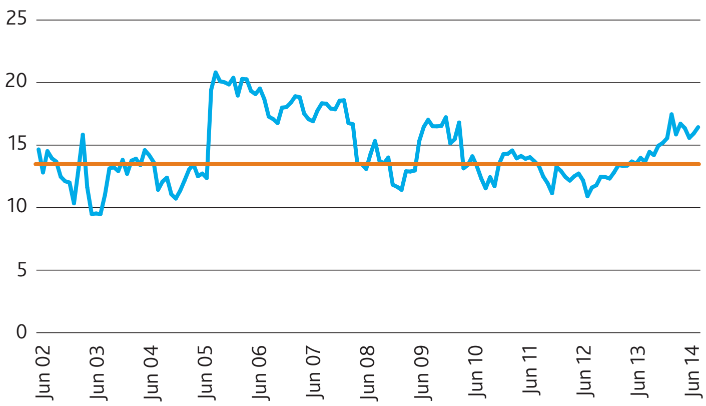
Merrill Lynch Technology 100 Index versus S&P 500 Index



Source: Bloomberg, June 2014.

Chart 2: Fairly valued

Merrill Lynch Technology 100 index forward P/E



Source: Bloomberg, June 2014.

The value of investments and the income from them can go down as well as up and your clients may get back less than the amount invested.

Contact details

Should you require any further information, please visit **aberdeen-asset.com** for details of your local Aberdeen representative.

For more information

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