

Focus Money

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Small but Good

Investors have most recently kept their hands off less-than-best shares. But the SDax offers unrecognised gems

Manuel Hölzle admits quite frankly that he misjudged the mood that has prevailed over the past few months. The Head of GBC, a research institute in Augsburg, Germany, revises his previous estimations: “We never expected or dared to hope that the markets would recover as decidedly as they have thanks to a strong counter movement even in the medium term, let alone within a matter of only a few weeks.”

Wherever one looks, the mood of company heads, analysts and investors has lifted perceptibly in the past few weeks, even if from a low level, with the most important indices on the German Stock Exchange already listing prices above those at the beginning of the year.

Manuel Hölzle refers to 2003 as a possible explanation for this development, when expectations were also initially way up, to eventually be matched by the situation. In 2003 the stock markets responded to a rise in Ifo (German institute for economic research) expectations with strong price rises. Although it is by no means certain that the line-up today is similar to that of 2003, the global recession could be followed by global recovery in the coming few years – also thanks to the massive, unprecedented wave of economic programmes worldwide.

Strong middle-market. “A recovered global economy could mainly give the currently battered middle-market companies in Germany a quick boost since these companies are very well-positioned for export business. This would help SDax companies, which have been under tremendous pressure since 2007, to get going again,” Hölzle explains.

A look at the chart on the right shows that third-row shares are currently reporting very attractive prices. The SDax, together with the MDax achievers of the first few years of the new century, dropped far more in value with the outbreak of the financial crisis than the Dax. This is because in crisis times, large-scale and small investors are quickest to sell off shares which are more illiquid than those trading on the Dax. However, illiquidity, i.e. trading in low numbers on the stock exchanges, discloses nothing about what is in the majority of cases a high fundamental quality of the investments, such as the quality which distinguishes the eleven SDax favourites chosen by the GBC analysts. “Many SDax companies are fundamentally better off than some of the blue chips of the SDax, on which around 20 per cent of the shares traded are strongly shaken financial shares,” Hölzle reports.

In terms of the price-earnings ratio, a measure of a company’s good value, the SDax, at a P/E ratio of ten, is currently clearly below that of the other indices and is thus up front in terms of favourably-priced shares. The small SDax shares are also best in dividend yields, which average 4.5 per cent and are thus in excess of the yields of investment grade securities.

The considerable potential for recovery of the small caps was not only recognised by analysts. Insiders, Hölzle observes, are currently already stocking up on selected small caps.