

# SARACEN

share success

## Rebirth of US Old Technology

The strong performance of global stock markets over the last few years has left investors struggling to find attractively priced opportunities. A sector with particular stand out performance is US Technology which has been dominated by high profile “new economy” names such as Facebook, Amazon, Netflix and Google (now called Alphabet), commonly known as the FANG stocks. Their performance has been driven by the long-term, secular trend of the increasing impact of technology and communication on our everyday lives.

Whilst we view the FANG stocks as expensive today, our research is finding significant value in some of the traditional US technology companies namely Cisco, IBM and Intel. These businesses enjoy many of the traits which we look for in an investment specifically, good market position, a strong and sustainable margin profile, robust balance sheet, cheap valuation and an attractive starting dividend yield of about 3%. These companies have been overlooked by investors because they have legacy businesses which still make up significant proportions of the group profits but which are either not growing or are in long-term decline. On closer inspection, however, it becomes apparent that these “old tech” businesses are slowly transforming themselves and, in time, like the FANG stocks, will benefit from the growth in connected devices, connections, data analytics and e-commerce.

Cisco is transitioning its business model away from a traditional “book and ship” every quarter model to a combination of hardware, software and recurring revenues. It is also now a global market leader in the fast growing software security market. IBM has created a “strategic imperatives” division which is growing at between 10% to 15% per annum and now represents over 40% of group revenue. Long-term, IBM hope to be able to monetise their significant investment in Watson, their supercomputer, which combines artificial intelligence and sophisticated analytical software for optimal performance as a “question answering” machine. Today Watson is predominantly being used in the Healthcare sector providing quicker and more accurate diagnosis for patients. Over time this will be rolled out across many different end markets. Intel is trying to evolve from a Personal Computer company to one that powers the infrastructure for this “increasingly smart and connected world”. The main strategic goals for Intel include the development of its data centre business, where its microprocessor chips help power the cloud servers of Amazon and Microsoft, as well as the Internet of Things division, where one of the growth drivers is powering the computers running autonomous cars.

Additionally, these businesses may also stand to benefit from the policies of Donald Trump, the new US President. They all have significant amounts of cash on the balance sheet which is currently held outside the USA for tax purposes. A change in the legislation may allow companies to bring this cash back to the USA for a one-off penalty. For example, Cisco currently has \$60bn of gross cash which is currently held overseas. This represents 40% of the market capitalisation of the company. If this cash can be successfully repatriated, we would expect shareholders to benefit from incremental returns through increased dividends or sharebuybacks or, even, further investment in the business. These businesses would also all benefit from a significant reduction in the corporate tax rate from the current 35% rate to the proposed new tax rate of 15%.

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