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Off the Cuff Video
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Hi everyone, my name is David Mann and here at Empire Life I focus predominantly on international equities. There's never really a shortage of topics to discuss in these markets, but today I want to talk about a relatively new concept. That concept is the K-shaped recovery. Then I'm going to tie the K-shaped recovery to an investment that we have in Empire Life's International Fund.

Historically there's been many letters used to describe different forms of recovery. On one end of the spectrum you have a V-shaped recovery, which describes a situation where there is a very quick snap back in economic momentum or equity markets or whatever is being discussed. On the opposite end of the spectrum you have an L-shaped recovery which is a recovery where there is no or very low growth and there can also be permanent impairment. A K-shaped recovery is a bit different. If you think about the shape of a K there's a vertical line and then an upward and downward sloping line. For the sake of this conversation the upper sloping line would represent improving trends whereas the downward sloping line would represent worsening trends. COVID-19 I think is resulting in a K-shaped recovery. It's causing an acceleration or an amplification in trends that we've already seen before. It (K-shaped) can be used to describe many different situations in the stock market, economy or sectors. Today I want to use it to talk about a business' digital capabilities. I think what's happening is that COVID-19 is causing an amplification or acceleration in a trend that we've seen whereby companies with high digital IQ or capabilities are outperforming those with low digital capabilities. And that's one of the first questions that we ask management teams; 1) what are your digital abilities? 2) What are your company growth plans? And ultimately; 3) what is your digital IQ?

In the Empire Life's International Equity Fund we have an investment in the business called Inditex. They offer many brands, but their most well-known brand is the apparel retailer Zara. During the lockdown at one point over 85% of their stores were closed. This meant it was really hard to go in, try on and ultimately buy clothing. Fortunately, for years they've invested a lot in building out their digital capabilities and building out their omni-channel presence. This meant you could buy apparel online and have the confidence to know that you could return it to them either through the mail or by going to stores, whenever that should open. That was fantastic because during the first half of the year their online sales grew by 74%. They had the profits from those sales to sustain operations, pay their employees and ultimately continue to invest in the business. Digital sales account for 14% of total revenues and by 2022 they expect that to reach 25%. We consider Inditex to be a business with very high digital IQ and it would represent a company on the upwards sloping line of a K. You can contrast that with a business that has no omni-channel capabilities and no digital presence. During the lockdown they would have had sales close to zero. They would have had no profits to sustain their business and ultimately it could result in bankruptcy. To be clear, there are many other factors that contributed to Inditex's performance, but their digital capability was a critical one.

COVID-19 we think has resulted in an acceleration of this trend again. Companies with higher digital IQ will continue to outperform those with low digital IQ. This is something that we think is

secular and is important to pay attention to when analyzing most businesses in equity markets. With that, I'd like to say thank-you very much.

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