



Insigneo Weekly Dispatch

Not all that glitters is gold (in the markets)

Get guidance on investments, and the major
structural factors behind your clients' portfolios.

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Investments that appear attractively valued can still underperform for extended periods when low valuations reflect structural constraints—such as limited growth, weak competitive positioning, or unfavorable industry dynamics—rather than temporary market inefficiencies.

Value traps are not confined to small or poor-quality companies; even dominant, high-quality firms or entire industries can stagnate if expectations, capital allocation, or growth drivers fail to evolve.

Investor behavior and psychological biases—such as loss aversion, confirmation bias, herd behavior, and FOMO—often exacerbate value traps by encouraging investors to ignore warning signs or cling to losing positions.

Identifying and avoiding value traps requires complementing traditional valuation analysis with a broader assessment of market context, investor behavior, and longer-term fundamentals.

Good bets lose all the time - What are value traps?

A few weeks ago, we met with the manager of an International Small Cap Value Fund who is currently raising capital for the strategy. As part of his presentation, he highlighted one of the portfolio holdings: a Japanese company specializing in the digitalization of accounting documents for Small and Medium-sized Enterprises in Japan. To support his investment case, the manager showcased his due diligence process, including visiting the company, meeting with its management team, and conducting multiple valuation analyses. After the meeting, a

natural question arose: is he seeing something that we are not? Despite all the effort devoted to assessing the company, does this truly make it a good investment? **After all, portfolios cannot be built on good intentions alone.**

Using the example of this portfolio manager, we should ask ourselves: if his trade does not play out as expected, what is the reason behind its failure? If an investor conducts deep fundamental research, applies all the theoretical tools required to value a stock, and goes well beyond the financial statements, **why might the market still fail to reward that insight?** As we will discuss later, part of the answer lies in behavioral biases and market dynamics, but for now, we can frame this phenomenon with what investors call “value traps”.

So, what is a value trap? It is a stock that seems to be attractively priced as it trades at low valuation metrics (for example, low P/E, low P/B, high dividend yields, etc.) but fails to catch up with its peers or the broader market due to **lack of revenue growth, loss of market share or poor scalability.** This does not necessarily mean that these are bad businesses; often these are mature companies with little room to expand, or good companies operating in mature markets. A clear example is Microsoft (MSFT), whose stock price stagnated roughly between USD 20 and 30 from 1998 to 2013. Microsoft looked inexpensive relative to its cash flows and dominant market position, yet the stock went nowhere. The problem was not the quality of the company, but **the lack of clear growth drivers and capital allocation that could change the market’s perception.** A similar pattern can be observed in airlines. Despite being critical for global transportation, the industry’s heavy debt, high capital expenditures, and frequent price wars have historically limited investors’ returns. For instance, United Airlines

(UAL), one of the largest publicly traded airlines, traded broadly between USD 40 and 50 between 2006 and 2024.

It is important to note that value traps are not limited to small companies, and that “cheap” does not necessarily mean a low share price. **Valuation is always relative to expectations and future earnings forecasts.** NVIDIA (NVDA), for example, saw its 2024 earnings expectations revised upward by roughly three to four times, and even 2026 forecasts have already been raised by another 15 to 20 percent. We are not suggesting NVDA is a value trap but simply showing how almost any asset can look attractively valued when projections keep moving higher. As mentioned before, Microsoft’s price stagnated for more than a decade despite being one of the most important technology companies in the world. **In a market shaped by FOMO (Fear of Missing Out), expectations can become so important that record-high prices still appear justified, at least on paper.**

As investors, we also must wonder whether certain assets, like gold, can appear attractive simply because expectations around them have become elevated. Gold has relatively limited industrial use, and most of its value comes from the fact that people have trusted it as a store of value for centuries. While gold has historically acted as a defensive allocation and we do not consider it a value trap, it is still a useful reminder of how an asset can look “cheap” or attractive on paper when driven largely by expectations.

One of the best ways to avoid value traps is to **look beyond valuation metrics and assess a company in context, using peer comparisons and other measures of long-term return potential.** Still, behavioral biases play a major role as investors often follow these stocks for years, and after seeing a company survive past challenges, it becomes easy to overlook

weaknesses. Humans are naturally biased, and that is normal, which is why we will now dive deeper into this topic.

The behavioral angle – the (not so) intelligent investor

It has long been argued that the fields of economics and finance are more an art than a science. Situations like the avoidance of value traps prove to be the perfect example, since investors are directly at odds with their beliefs and biases while trying not to let these permeate into their investment strategies.

Hence, a field that we need to consider when looking at value traps is that of behavioral finance – the economic theory that ascribes the irrational behavior of individuals making financial choices to psychological factors or biases. **Through the main principles of behavioral finance, investors are provided with a framework to assess their investments beyond the traditional measures of return and volatility.**

One of the first principles that needs to be accepted is that investors are not as rational as they hold themselves to be, and that emotions, beliefs, and biases tend to affect their decision-making process – oftentimes not in the best of ways. Investors can fall prey to some of the key warnings from behavioral finance. These include the prospect theory, herd behavior, or some other biases, such as confirmation or overconfidence bias, to name but a few.

Prospect theory was developed by Daniel Kahneman and Amos Tversky, and it states that people – in this case investors – value gains and losses differently. This translates into risk-averse behavior when facing potential gains and risk-seeking behavior when facing potential losses. **Think of how investors tend to prefer to see profits materialized sooner**

than when they would like to accept their losses, simply because a negative figure weighs more heavily than any potential profits. Unfortunately, this theory tends to be present when, for example, companies disclose challenging situations that get priced in by a financial asset's stark price decrease. For example, in the case of a bond, often, even if the fundamentals and the situation may point towards its default, investors are uncomfortable realizing their losses and end up trapped in a default reorganization process. Recent examples could be the Chapter 11 processes of Bed Bath & Beyond, or the Brazilian airline Gol Linhas Aéreas Inteligentes.

Another common principle of behavioral finance that is often spotted is herd behavior. This one is closely tied with FOMO and is characterized by investors following the actions of a larger group – the herd – without taking their own analysis into consideration, under the assumption that others who are following the same trend have already done the necessary research before investing. **Because of FOMO, investors may jump into a popular investment tendency, and since there is no fundamental basis for having made the investment in the first place, they lack parameters needed to properly exit their positions.** Furthermore, herd mentality can also translate into market crashes through behaviors like panic buying or panic selling.

In the current market setting, we have spotted two investment trends that exemplify FOMO investing: investing in the AI complex and in precious metals like gold and silver. Regarding the so-called “AI bubble”, [we have argued on previous occasions](#) that the key issue in this market is not necessarily the existence of a speculative bubble; rather, the current market concentration in a couple of specific names. **Again, the market's trend can be an investor's friend, but that does not mean it should be the only argument needed to follow a specific narrative.** As we

mentioned before, the importance of balancing diligent fundamental research with market trends before investing in a specific asset is a key component of a sound investment process.

With respect to precious metals, these have played the role of safe havens in times when uncertainty has peaked amid the shift away from traditional investment alternatives. Again, **with a meaningful share of investors trying to get their hands on gold, or gold-linked ETFs, a prudent, more rational investor would take a step back and gauge the potential implications of buying at an all-time high, even if FOMO could propel prices higher in the short-term.**

In the long term, we continue to believe that, on the back of the increased demand by governments and sovereign wealth funds, gold remains attractive. However, if we assess its potential from a short-term perspective, the risk of falling prey of FOMO and herd mentality looks increasingly high, bearing in mind that the precious metal has been used as a

hedge against heightened geopolitical risk – a variable that is becoming harder to forecast amid current global tensions.

In sum, current market dynamics compel investors' attentions to headlines and "noise." However, as was pointed out by Benjamin Graham in his book *The Intelligent Investor*, "An investment operation is one which, upon thorough analysis, promises safety of principal and an adequate return." Hence, we emphasize the need to implement a balancing act between avoiding value traps and performing rational, value-based investment decisions, which should lead investors to dodge opportunities that look initially shiny, but that end up being rather coal-like. ■



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