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THE DEAL DESK

GFMC Newsletter

Why sin stocks are an investor's salvation?

By Jainam Gandhi

Overview:

For a productive consequence to consume this article, first, it is essential to understand sin stocks. According to the description on Investopedia, "A sin stock is a publicly-traded company involved in or associated with an activity that is considered unethical or immoral. Sin stocks are generally in sectors that deal directly with morally dubious actions. They are perceived as making money from exploiting human weaknesses and frailties". Sin stocks are alcohol, cigarette, betting, sexuality-accompanying industries, marijuana, and armaments manufacturers. However, they can still be delimited by territorial and societal beliefs that change widely across the planet. For example, brewing has been a long tradition globally; therefore, everyone considers intoxicating stocks sin stocks. Some people's list will include all military builders while remaining it is their responsibility to support the military by buying defense equipment manufacturer stocks.

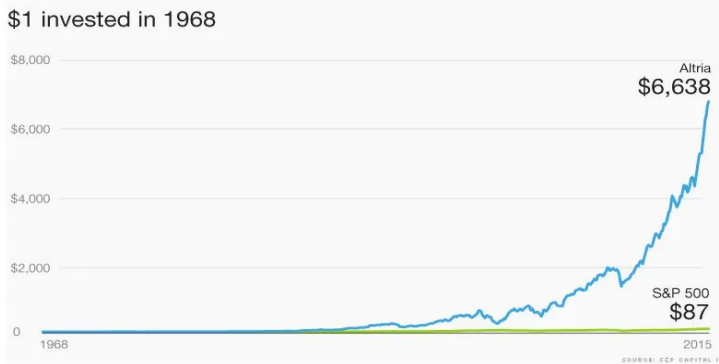
While talking about the weightage of sin stocks in various indexes around the globe, Altria has a weightage of 0.42% in the S&P 500, British American Tobacco has a weightage of 4.25% in FTSE 100, ITC limited has a weightage of 3.03% in NIFTY 50 index. Acknowledging the contribution of sin products industries to a nation's tax revenue is essential. Altria contributes around \$ 2.03 billion to US tax revenue, and ITC limited contributed 5850 crore rupees (\$1 billion) to India's tax revenue.

Key Takeaways

- Ethical or sustainable investing is all the rage right now. It sounds great, but the problem is that there's no accepted industry definition of what constitutes an ethical investment.
- Rightly or wrongly, sin stocks are popular. People like to drink, smoke and gamble. As an investor, having some exposure to these industries can be an interesting way to generate extra returns for your portfolio.
- Sin stocks are considered defensive stocks, meaning they tend to perform well even during an economic downturn.
- Though relatively stable, sin stocks carry some special risks, such as being vulnerable to changes in regulations or taxes.
- In June 2022, U.S. inflation reached 9.1%, a 40-year high. As a result, many investors are increasing their allocations to inflation hedging assets. One such asset that is seeing record demand is sin products industry.

The tobacco and alcohol industry alone contributes to about 1.03% and 1.5% of the world GDP from the different sin products industry.

Altria Group, Inc. (previously known as Philip Morris Companies, Inc.) is an American corporation which is one of the largest manufacturers and marketers of tobacco, cigarettes and other related products.



Source: money.cnn.com

What are the headwinds and tailwinds for the sin product industry?

Unfortunately for you and your moral compass, sin stocks are frequently money-making for various reasons. Adding a ruling class to your portfolio may be an appealing commercial move. Here are the important reasons why sin stocks are deliberately powerful investments.

1. They are cash cows

Many companies in sin industries are well established, have sound financials, and have usually rewarded profits to stakeholders for years.

Stock Name	Stock Symbol	Stock Sector	Dividend yield
Philip Morris International	PM	Tobacco	5.24%
Altria Group	MO	Tobacco	8.29%
British American Tobacco	BTI	Tobacco	7.43%
Diageo	DEO	Alcohol	2.17%
Brown Forman Corporation	BF-B	Alcohol	0.98%
ITC limited	ITC.NS	Tobacco	3.59%
United Breweries Limited	UBL.NS	Alcohol	0.62%

Source: finance.yahoo.com, dividend yield as on 09/20/22

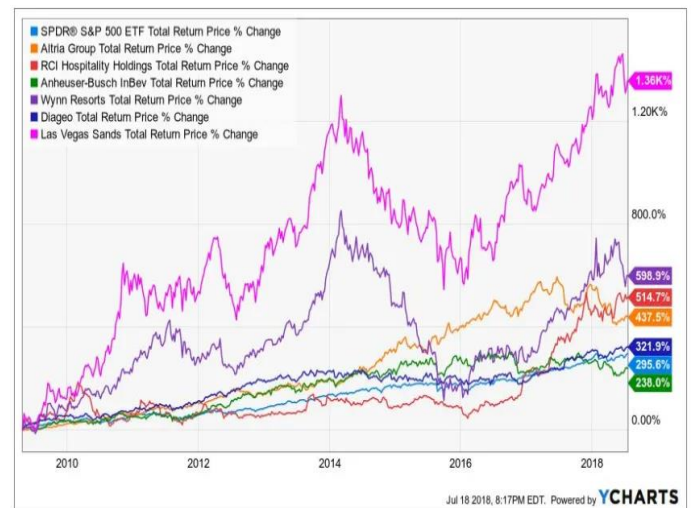
2. They are stable entertainers

Sin stocks are thought-out watchful stocks, meaning they are less concerned by trouble or economic downturns. Many of these stocks are slide-opposing, recession and bankruptcy resistant for the same reasons as commodity stocks. The demand for these goods is still high irrespective of the wide economic trends.

As interest rates fell from all-time highs in the 70s & 80s to essentially zero following the great recession, stocks that are 'bond proxies' performed demonstrably well. These sectors include utilities and consumer staples. Sin stocks (excluding casinos) are also very stable businesses with nearly inelastic demand. As such, as investors were pushed out of bonds and into stocks, these stable businesses with high dividends were solid opportunities.

Recession	2001 DOT-COM Bubble	2008 Financial Crisis
S&P 500	-11.89%	-37.00%
Altria	9.10%	-30.00%
FTSE 100	-16.00%	-31.00%
British Tobacco Company	13.51%	-21.00%
Nifty 50	-16.18%	-51.79%
ITC	-28.00%	-24.89%

Source: money.cnn.com



Source: ycharts.com

3. They have received little contest

The goods and aids that sin stock associations produce are likely to expect strict regulations from government institutions, constituting a more significant hurdle for competitors. Potential rivals concede, unwilling to participate in such a provisional trade atmosphere, conceiving more range for existent performers to grow. Consider cigarette companies which were told they could no longer advertise via new regulation. That essentially eliminated their marketing teams, increasing earnings and cash flow, but also eliminated any new entrants into their space (i.e., if you cannot advertise, you cannot enter). Even sin stocks' negative implications can work to their benefit. Certain fund managers- particularly those management assets for conscientious or academic groups- often have nothing to do with blatant or questionable trades. That can bring about the sin stock being underestimated and a good bargain.

Stock Name	Stock Symbol	PE Ratio
S&P 500 Index ETF	SPY	28.40
Philip Morris International	PM	16.49
Altria Group	MO	43.85
British American Tobacco	BTI	14.66
Diageo	DEO	27.16
Brown Forman Corporation	BF-B	38.40
Nifty-50 ETF	KOTAKNIFTY.NS	21.04
ITC limited	ITC.NS	25.32

Source: finance.yahoo.com, PE ratios as on 09/20/22

While sin stocks are usually resistant to financing, they create a few disadvantages:

1. There is extreme supervisory risk

All parties' fortunes can be liable to be subjected to regulations, but the supervisory risk is the concern accompanying sin stocks. For example, marijuana, though legalized in certain states and nations, has yet to be legalized worldwide. Even then, certain states and nations have their own set of managing rules that would complicate a marijuana company's movements and working model.

Disclaimer - The opinions expressed in this newsletter are those of the author and do not constitute as financial advice. Additionally, they do not purport to reflect the opinions or views of GFMC, JSOM or the MS Finance Program at UTD.

2. Taxes may be a question

All parties should handle taxation, but the sin stocks frequently have a monetary mark on their backs. Regulators and electors commit end to increase the taxes on the 'immoral' articles these companies produce; they are frequently the go-to beginning when nations need services. Higher taxes keep lower demand that, dampen profit and push the stock prices down.

Should an investor include sin stocks as a part of their portfolio?

The industry promises big money and investors can consider to add sin stocks on to their portfolios to enhance the diversification benefits. Not only that, but most of these industries have very long track records, and with human instincts unlikely to change, they will probably be around for a long time. Percentage of high school students (potential permanent future consumers) who currently used tobacco products, alcohol, and marijuana products as per CDC (center for disease control and prevention) records-

Characteristic	Male	Female
Electronic vapor product use	13.9	16.8
Current Cigarette use	3.6	3
Current Cigar use	3.1	1.3
Current smokeless tobacco use	3.2	0.6
Current alcohol use	16.4	22.4
Current marijuana use	12.9	12.7

Source: www.cdc.gov

About the Author

Jainam Paresh Gandhi
MSF Graduate

Jainam is a full-time MSF graduate who spends most of time in learning about the financial markets, researching about the efficient usage of option chains and studying the candlestick charts through technical analysis. He loves reading mangas, watches anime and listening to podcasts. He targets on securing a job role at the trading desk, keen on using his derivative trading experience of over three years.



Alumni Spotlight

Rose Wang
Spring-22, MSF

Rose obtained her Bachelor of Arts degree with majors in Human Resources from Concordia University before pursuing MS in Finance at UTD. Rose graduated in Spring 22 and has been working at Allegiance Capital Corporation as an Investment Banking Analyst, based out of Dallas. During her time at UTD, Rose worked as a Venture Capital Analyst for the UTD Seed Fund and as a Venture Fellow for Moonshots Capital. In her spare time, Rose enjoys dancing – ballet, classical Chinese, and folk dancing.



About GFMC

GFMC EVENTS CALENDAR

Fall' 2022

GFMC
Graduate Finance
Management Council

**AUG
25**

GFMC KICK-OFF MEETING

Join us in Room 11.214 or connect virtually through teams from 5:30 PM - 06:45 PM

1st COFFEE CHAT

Join us from 4:00 PM to 5:00 PM outside the Finance Lab (11.101) over a cup of coffee

**AUG
31**

**SEPT
14**

2nd Coffee Chat & Internship Roundtable

Join us in Room 1.502 from 5:00 PM to 06:00 PM with MSF Interns.

MOVIE NIGHT

Join us in Room 1.508 from 5 PM and enjoy a fun filled movie night with your group!

**SEPT
23**

**OCT
TBD**

Eikon Mini Flash Competition

Join us in Finance Lab (11.101) for a training session on Eikon & a mini case competition.

3rd Coffee chat with Industry Leaders

Join us in Room 1.502 from 5:00 PM to 06:00 PM to connect with our guest speakers.

**OCT
12**

**OCT
21/28**

FIELD TRIP

Join us for a fun filled day for some hands-on experience on a field trip. Limited Registrations!

ALUMNI ROUNDTABLE

Join us in Room 11.214/218 from 10:45 AM on Nov 5 for a roundtable session and lunch with our alumni

**NOV
05**

Special thanks to Dr. Reichert, Penny Jiang, Dr. Ma, past GFMC officers and finance alumni for growing the finance program and enhancing the experience of students

GFMC Officers



The DealDesk provides a platform to JSOM students to share their views on important events affecting the finance industry.

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