

“An investment in knowledge always pays the best interest”

Fund Manager Meeting Notes – JOHCM Investment Management Forum



In the review for the portfolios in 2014 we are looking at removing the Aberdeen and First State Asian Funds as they are reaching their capacity in terms of assets they hold.

Some of the new funds we are looking to add are from the JOHCM stable of funds. We were invited to their investor day in London and this gave us a chance to understand more about the group and their management style. We also had a brief insight to some of their managers and funds.

This update covers some highlights from the day.

We like the ethos of JOHCM because they are an investment-led boutique through active fund management. Many fund houses have house views which the managers follow, JOHCM do not share this so different managers have different views. We saw this with the Asia Manager and the Emerging Markets Manager and we will cover this later. The other area we like is the limitation on portfolio size.

So for example some companies have allowed the funds to balloon to several billion which eventually restricts what they can do and in the long run damages performance. Their UK strategy is close to capacity but other strategies have some way to go.

Overview of the funds

UK Equity Income – is there any value left

The first update was on their Equity Income Fund; my first impression was the style was similar to the SLI UK Unconstrained Income Fund.

One of the greatest challenges is whether the markets are at the top and whether there is any value left. It always depends on who you listen to as to what their view is. Clearly parts of the market are at the peak but Clive Beagles who is the manager of this fund feels that there are plenty of undervalued opportunities.

Clive accepts that the recovery is coming through but he feels it needs to broaden. A lot of the views are similar to JP Morgan. In that employment needs to improve but this needs to be broadened out, a lot of the growth is in low paid or part time roles and so the employment is poor. Once employment prospects improve then this is a sign that the recovery is gaining traction.

He accepts that some stocks have got expensive, for example the restaurant group is one they have recently sold out of as the earnings are around 20 times earnings. It remains a good business but just expensive.

Some trades he likes include Balfour Beatty and Kier who have suffered from a reduction of government contracts but still have value which he feels is not reflected in the market. Others include unloved food retailers like Sainsburys and Tesco. Tesco for example has a 30% market share and yet is trading around 11 times earnings.

The view is that these stocks are worth holding as they will benefit from a strong recovery when it comes through.

Recovery stocks they like are Aviva who have underperformed for 10 years and now have a new CEO who is driving through cost efficiencies and improving cash flow.

In summary Clive believes there is plenty of value and has added 17 new names to the portfolio this year.

JOHCM Global Select – Beware good houses in bad neighbourhoods

The fund is managed by Christopher Lees and is really interesting. We have two very good global funds and if there was room this would certainly be one to consider.

What was interesting was his comments about the markets. He feels that the market is potentially in the same place as 1994 where interest rates went up and bonds were massacred. Equities responded by falling and then coming back but being effectively flat for the year.

This comes onto the point of discussion beware good houses in bad neighbourhoods. What he means is that you have stocks like Samsung which should behave like a tech stock but doesn't and actually behaves as the Korean index behaves.

His argument is that to outperform you need to pick the right stocks in the right area. So for example LyondellBassell has a low sector / country correlation so would be a buy whereas Rio Tinto has a higher sector correlation so would be a sell. The fund is more weighted to the US but is starting to build a position in emerging markets as he expects this to trend positive during 2014.

In summary if the market returns move to flat then good stock pickers will be able to deliver if the opportunities exist. The fund has delivered strong performance since launch and Christopher has clearly demonstrated that he can do this through a very different and contrarian approach which we like.

JOHCM Asia ex Japan – Plus ça change, plus c'est la meme chose

There are two funds in this strategy and these are funds we are considering adding in the July review. The lead manager is Samir Mehta who we recently met.

Again like the other managers Samir focuses on stock picking however is less worried about the Macro picture. In June 2013 he accepts the fund was vulnerable because of its weighting to India and Indonesia but this also reflects his style of management.

75% of the fund is invested in quality long term sustainable businesses and he could hold these stocks for up to 10 years. His view is that the numbers tell the story.

A couple of examples are Zee Entertainment in India. This is an advertising and content company and looking at the macro picture falling GDP, increasing inflation and interest rates this would not be a company to invest in. However, sales are up 19% and profits up 42%. Samir believes the company can continue to deliver growth over the next 5 years.

Dr Reddy's another example where 74% of revenue is outside of India with growing sales and profits. These two businesses are examples of resilient businesses in tough times.

In fact despite the fund being weighted 55% to ASEAN and India it is still ahead of the benchmark over 12 months.

In summary this fund is an example of good stock picking whatever the macro environment. Good businesses will perform whatever the market, of course this is a different view to the global manager but shows the freedom the managers can operate in.

JOHCM Global Emerging Markets Opportunities Fund – They're digging in the wrong place

This is a fund we will add to the watch list, the manager is Paul Wimborne and he previously worked on the very successful Barings Emerging Market Fund.

Where some EM Funds are using their 20% of-benchmark allocation to buy non EM stocks this is a pure EM Fund. He does hold stocks like Baidu which is a Chinese company but is listed on the NASDAQ exchange.

The fund is very much about country allocation and he will place high conviction towards this. It was interesting as Samir mentioned that the Philipians is a great opportunity, Paul didn't share the same view and it again highlights the opportunities for managers to look where their conviction leads them.

When people talk about EM often they say that China is coming to an end therefore ending the EM story. Paul would dispute this and believes that the best place to be at the moment is China, Taiwan and Korea. He accepts these are unfavorable parts of the market but he believes the market is missing this.

These countries have made great advances in technology, brands and scale. Where they have had low cost exports they are happy to pass the baton to newer emerging market economies.

An example of this would be Lenovo who are the world's largest PC Manufacturer. 43% of sales come from China and 57% are exports to mainly the US and Japan. They are aggressively moving into the tablet and smartphone market and are the number 2 smartphone provider in China.

Where the fund is light is Latin America where he sees limited opportunities.

In summary again the manager takes a contrarian view and is moving away from the darlings of last year and focusing on economies where he believes value can be driven.

JOHCM UK Dynamic – A focus on change

This was a really interesting fund but in a space where there are already some very good funds. Alex launched the fund in 2008 and has built the process.

There were a number of things I liked, he mentioned about being a patient investor i.e. he is prepared to wait (we heard this from a lot of managers), he doesn't focus on cheap stocks but on where the stocks might be in four or five years' time and he focuses on a

concentrated portfolio. There are three investment types – hidden growth, recovery and restructuring.

There are three main holdings – the longer term holdings which have been held for 24 months or more. These are the core, high conviction, long duration ideas. So in restructuring this would include the likes of ManGroup and BP and in growth the likes of ITV and Legal and General.

The medium term stocks are where conviction is growing so the likes of Tesco and Aviva are in the restructuring phase, and Lloyds in recovery.

The final area is recent investments, in restructuring it includes Shanks which has a new management team and Balfour Beatty and in growth Old Mutual.

Again the message was that equities remain relatively attractive and Alex is able to find good opportunities.

In summary the UK strategies are close to maximum capacity and although we liked the style of management we already have good funds in place and with the potential for this to soft close it wouldn't be one we would add. If we had space in the portfolios, and capacity was not an issue, then we certainly would consider it.

Conclusion

We also heard from the Global Opportunities and Japanese Fund Managers and although there is no house view and that certainly comes across in the different styles there are two themes that run through. These are quality and patience. The performance across the range is strong and this just highlights why we should consider boutique providers.

In reality we can't take every fund but certainly the Asian and Emerging Market strategies are two we will be reviewing and adding to the watch list.

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