



Fund Bites

Liontrust Investment Conference

We started using Liontrust in the 2012 portfolios, and added to this in 2013. These notes are from the conference and provide insight to their style of investing.

Introduction

The ethos of Liontrust feels similar to our ethos. They are a specialist fund manager encouraging managers and their teams to follow their own particular style of management within the normal risk matrix you would expect from this type of business.

This style of management first attracted us to their European Fund and we have added to this fund in the latest review, and more recently the UK Special Situations Fund.

We came to this conference with no particular agenda other than to get a broader understanding of the way the managers invest and also identify other potential opportunities.

There were three presentations – the Liontrust Income Fund which is managed by the same team as the European Fund and has recently moved to a global remit, the Asian Income Fund and Macro Equity Income Fund.

In this update I want to focus on the Income Fund and Asian Income Fund as I feel these two have the greatest potential to add something to our portfolios.

Liontrust Income Fund



The fund is managed by James Inglis-Jones (see picture to the left) and Samantha Gleave. We have met Samantha before but this is the first time we have met James.

For some time we have used the M&G Global Dividend in our portfolios. The focus is more on the developed economies and as with many of the M&G Funds has become a victim of its own success, although the performance remains strong it has pegged back slightly and this could be because it is now a fund of nearly £8 billion which means it is harder to seek out opportunities.

This is not a reason to remove the fund but it does mean that we have to consider alternative options. The Liontrust Income Fund had not come onto our radar because it was a UK Fund.

In the last few months it has moved to a global remit and with the proven style of management we think this is an attractive fund going forward and could if we decide to look for alternative options be an attractive replacement for the M&G Fund.

There are three elements to this, the first one is the size of the fund which is around £200 million so significantly smaller than the M&G Fund, secondly the number of stocks which will be around 20 to 40 stocks – currently there are 27 stocks of which 10 are international firms – and thirdly the management style.

We talk about managers who see the importance of on the ground experience, so meeting the management team, reading analyst reports etc however with this team cash flow is the key. Effectively forensic analysis is where they focus.

They have a system which analyses the market to identify potential companies which have good cash flow and are cheap. Good cash flow is for them all about discipline and how a company deals with this. Also management having a buy into this is crucial to the process.

Using a global approach there are around 80 companies on a global basis that they would consider. At this point the forensic analysis begins. This is looking at the report and accounts and identifying the cash flow characteristics and how the market views these. By doing this they can narrow down to around 20 to 40 stocks.



A couple of examples they gave were Total where the free cash flow is around 12% and dividend yield is 6%. The share price is weak but the

capital investment that has been put into the business in recent years is coming to an end and should be declining from 2014. They have new fields opening, and exploration in frontier markets.

Effectively production is set to grow by around 35% up to 2018 just at a time when the capital investment programme is coming to an end and therefore declining. So increasing production and declining costs makes this an attractive investment.



Vodacom is a South African mobile phone operator with around 50% market share however this is a mature market

although very cash generative. It is the international side that is interesting in Frontier Markets like Tanzania and this is where they see the potential for upside.

In addition their net debt is down and they have low financial leverage.

So for a global income we would be buying into something which has a proven process, which ignores the noise and uses a different opportunity set.



We have met Samantha (picture left) before and I was able to speak to James on a one to one basis. Clearly he is passionate about this style of investment and has almost all his personal wealth in

these strategies and I think there can be no better endorsement than that.

From a volatility perspective this is not heightened by this style of management and in fact possibly dampens it slightly because of the investigative style of management. The question for us is really whether M&G Dividend Fund can continue to deliver and if

we feel it can't, whether this fund would be the right replacement.

Asian Income Fund



We have indicated in previous updates our desire to review the Asian, Emerging Market and Frontier Market Funds

especially in light of the restrictions to using the likes of Aberdeen and First State.

What I am starting to realise especially in the Asian space is that there are a few very good funds and managers to choose between so having alternatives may not be the problem, choosing the manager could be the challenge. Mark Williams (above is the fund manager of the Liontrust Income Fund).

We have talked about the story of these markets, the fund manager indicated that he expects Asia to provide around 40% of world GDP by 2050, and these are economies with lower levels of debt. So clearly if this happens then Asia will become a significant powerhouse in the future.

Asian Stocks have a tendency to pay dividends and it indicates strong businesses. Between 2003 and 2012 \$100 invested in Asia Pacific ex Japan index with dividends re-invested would be worth \$419. So the story behind why Asia remains strong. (Source: MSCI, Bloomberg, Liontrust. Estimated returns in Asia Pacific ex-Japan index, dividends paid daily. Past performance is not a guide to future performance).

We have indicated the need for active management and again the management was keen to emphasize this. So for example in 2008 companies in Taiwan, Hong Kong and South Korea significantly cut dividends whereas companies in Thailand, Indonesia and the Philippines significantly increased dividends. A fund tracking the index could not distinguish between these countries.

They are positive in China and negative to Australia which is possibly a contrarian view for many. China is becoming more domestically focused and growth is slowing but will rest at around 5 to 6% which is a level most economies would give their right hand for!

Also people keep saying spiralling wages in China will make the economy uncompetitive and these are up by nearly 250% (between 1995 and 2010) however income per household is as low as economies like Indonesia, Philippines and Thailand which have not seen as strong wage increases.

There has also been an indication that businesses will move out of China to remain competitive however a recent survey has indicated this might not be the case. Over 80% of businesses surveyed said they had no plans to relocate and nearly 80% of businesses indicated that they would be looking to automation to reduce costs.

One of the businesses they hold is a Taiwanese Office Supplier (Aurora). In China only 10% of companies have colour copiers and 75% of these have printers that have speeds of 20 sheets per minute or less. Aurora is increasing their distribution network in China and therefore is expected to benefit from a shift to more modern photocopying.



Another business they like is a Hong Kong based company called Bonjour. Chinese people come from the mainland to buy goods (it is a low end cosmetic shop) because they are cheaper. The average spend in the shops is around HK\$160, for Chinese tourists the average spend is HK\$600. Gross margins are expected to rise, it has a strong dividend yield and an excellent return on equity.

Hong Kong and China makes up around 40% of the fund but other emerging economies play an important part.

Thailand is seeing a growth in urbanisation and therefore infrastructure is becoming a key play to cope with this increase in rural movement.

One business they have invested in is Major Cineplex which is a high quality cinema business. It plays on the increase in urbanisation and the increase in minimum wages. It has over 60% of market share. Currently it has 78 cinemas; this is expected to grow to 118 by 2015.

The manager focus is more on the mid cap market. It has around 60 holdings and currently has around £20 million invested in the market.

Conclusion

In summary we like the style of Liontrust and we feel the two funds we have mentioned offer potential for inclusion in the portfolios however as we have indicated with Asia there are already some good managers and therefore nothing is a given. Equally with global funds there are a few good managers and we would need to consider whether we stick or look at the other options.

The source of information in this note has been provided by Liontrust and is correct as at 24 September 2013. These are notes from meeting the fund manager or representative and should not be seen as a recommendation to purchase this fund. Any reference to shares is not a recommendation to buy or sell. Should you wish to make a decision based on these notes we cannot take responsibility for this and you should carry out your own research before making a decision. You should note that past performance is not a reliable indicator of future returns and the value of your investments can fall as well as rise.