

Standing out from the crowd

CJ Cowan, Cirilium portfolio manager, explains what makes the Quilter Investors Global Equity Value Fund stand out from the crowd, while the manager of the strategy, Nick Clay at Redwheel, looks at what underpins their high-conviction approach to value investing.

1

What the fund does

The fund starts by applying a dividend lens to its global equity universe. To be included in the portfolio, a stock must offer a 25% yield premium to global equity markets.

The fund's sell discipline means that, if the yield on any holding falls below that threshold, it's sold. This serves to bank the price gains that drove the fall in yield.

A holding will also be sold if it cuts its dividend. However, this is a rare event and it's only occurred a handful of times since the strategy was launched.

Due to its yield-driven process, the fund delivers a higher dividend yield than global equity markets. The compounding of this dividend yield accounts for the largest part of returns.

The fund often buys into holdings when others are fearful, and the dividend yield is at its highest, which can make it stand out from the crowd.

2

What this means in practice

The companies identified by the fund's approach are 'cash compounders' at good valuations.

This means there's a natural tilt in the fund towards stable and cash-generative companies, typically with clear 'value' characteristics.

This creates a low-turnover portfolio that has kept the strategy resolutely overweight to staples and discretionary stocks, mainly through luxury brand and healthcare companies.

The fund has also been consistently underweight to financials, materials, and industrials stocks. Although the strategy excludes large parts of the tech sphere from its investable universe, it has maintained substantial positions in the semi-conductor sector.

At a country level, this means the strategy is significantly overweight to the UK and Europe but underweight to the US market.

3

Delving deeper

Usually, the only way for a stock to offer both 'quality' and 'value' is for some form of controversy to exist.

The team's process seeks out such controversies and assesses the range of likely outcomes to determine where their views differ from the broader market.

A good example of how it does this was when it took advantage of the overblown fears of a permanent Chinese lockdown.

The fund increased its exposure to European luxury goods companies that derive meaningful revenues from Chinese consumers, and its investors were well rewarded for this move.

The joint focus on finding sustainable dividend stocks and avoiding overvalued companies, acts to mitigate downside risks. This means that much of the strategy's relative outperformance is seen when markets are in retreat.

The fund often buys into holdings when others are fearful, and the dividend yield is at its highest, which can make it stand out from the crowd.

CJ Cowan, Cirilium portfolio manager



A pursuit of life's luxuries

"One of the most significant changes to the fund in the last two years has been our increased investment in luxury retailers. It's a good example of how the strategy looks to invest in quality companies that are out of favour, due to some temporary controversy. In this case, we invested while concerns over China's lockdown becoming a permanent situation still hung heavy over the sector.

"During the period, we added to our holdings in Richemont (*Cartier*), Kering (*Gucci*), and Tapestry (*Coach*). We also introduced Inditex (*Zara*) as their robust business models demonstrated their ability to weather more difficult backdrops.

As it turned out, the most likely outcome, namely that the lockdowns in China were a temporary phenomenon, turned out to be true. Thanks to the robustness of their product offerings and their pricing power, these companies delivered strong numbers and meaningful share price appreciation when China ended its 'zero-covid' regime."



Nick Clay, manager of the Quilter Investors Global Equity Value Fund

Looking for more fizz

"More broadly, the strategy seeks out those companies that are best able to endure a range of different outcomes owing to the durability of their cashflows. In an inflationary environment, this requires companies to have strong pricing power to offset input cost inflation and to protect their margins. Good examples of such stocks in the portfolio include staples companies such as PepsiCo and Nestlé, which have both seen strong performance in the last two years."

No crystal balls

"Part of the strategy's strength derives from the fact that our team recognises it can't predict the future. We frame all investment opportunities within a range of possible outcomes and only look to invest when that range of outcomes is skewed in our favour. Our understanding of the range of possible outcomes is guided by the way we view companies, namely by business type, rather than by sector. For example, we view banks as capital-intensive businesses, which means we see much of the banking sector as highly vulnerable to small things going wrong as they're naturally highly-levered businesses."

Challenging times

"There are currently two related challenges facing the strategy. The first is that the environment of quantitative easing and zero-interest rates lasted so long that investors have been conditioned to believe that there's only one way to generate long-term returns; namely growth investing backstopped by central banks which are poised to step-in to prevent the worse outcomes from materialising.

"This conditioning means that investors' obsession with large-cap technology stocks is likely to persist for some time yet. More broadly, a return to that 'growth-only' environment would also be to the detriment of our approach, as it would simply reaffirm the common consensus view on investing.

"Fortunately, we see a return to the previous regime as unlikely. To us, the more probable outcome is a return to a more 'normal' environment of economic cycles and volatility, which suits the way the strategy generates long-term, total returns for its investors."

Key takeaways

- ▶ To be included in the fund, a stock must offer a 25% yield premium to global equity markets, and if the yield on any holding falls below that threshold, it's sold.
- ▶ The team's approach focuses on identifying stocks that are subject to a controversy of some kind. Such stocks can offer both 'quality' and 'value'.
- ▶ The fund should always deliver a greater dividend yield than global equity markets and it will naturally compound this higher over time.

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