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Matt Williams
portfolio manager
Airlie Funds Management

Combining value and experience

The Airlie Australian Share Fund is a concentrated, long only fund with an experienced investment team ready to find companies that are undervalued and unloved

Some years back there was a time when Airlie Funds Management portfolio manager Matt Williams[01] would have been wary of investing in Qantas.

We are speaking of a time when the iconic Australian company had a bad balance sheet and a lot of off-balance sheet liabilities.

But in came new management and the brand started to turn around – so much so it ended up with one of the best balance sheets of any airline globally, Williams recalls.

With the quality of the business on the up and the capacity war between Virgin and Qantas finally coming to an end, Airlie Funds Management decided the airline industry's structure was changing for the better.

"We could see the opportunity to make money was good. The management had steered Qantas through some turbulent times," Williams says.

"On valuation, the company was trading on very low multiples compared to the rest of the airlines around the world and for us it was a very attractive opportunity and it's played out."

In the last few years Qantas' share price has almost doubled. Yet it still remains a stock many people wouldn't associate with Airlie's bottom-up, long-term capital growth approach to investing.

The investment approach

What many don't realise is that portfolio managers at the Airlie Australian Share Fund use a four-pronged assessment method when it comes to making key calls on the stocks demanding the most attention.

"The first step in the process is to exclude stocks with excessive leverage," Williams says.

"We feel we want to take that issue off the table in the sense that if the economy or the industry or the company hits turbulent times they can see their way through a bad period comfortably in a financial sense."

Airlie then looks at the capital structure of companies and makes sure they're appropriate for both the industry the respective company is in, as well as where they're at in the business cycle.

"Once companies pass that test, we then asses them for business quality. What we're looking for there is where the company is placed in the industry, and the strengths and weaknesses of its position – so we're looking for changes in industry structure or companies that really have something differential about themselves in their space," he adds.

"Once we like that idea, we then look at company management. This is where years of experience in dealing with company management means that our investment team really comes into play.

"Sometimes we know the history of the company better than the new management teams. So what we're looking for in management are sensible and rational people that we're comfortable investing our clients' money."

Lastly, after the company has passed all those tests, Airlie then looks at valuation. Williams reiterates that the Australian Share Fund doesn't start its research at valuation point, rather this comes last.

At a Sydney financial adviser roadshow earlier this year, Williams and his co-portfolio manager Emma Goodsell further explained the value manager's discipline.

Williams said a financial company such as AMP, for example, may look relatively cheap on a valuation basis but it struggles to pass the manager's business quality tests.

In a post Royal Commission environment and with a new management structure, there will be periods where AMP will perform "but on a three to five year view we can't make the [investment] case stand up with what we know now," he said.

Goodsell explained companies such as Myer and Fletcher Building have also failed the business quality tests. She said the manager would invest in TPG over Telstra, and there are good investment cases for Wesfarmers, CSL, Qantas and Reece.

Experience counts

Combining from their days at Perpetual, Williams and Airlie co-founder John Sevior have been investing in the Australian market for 25 years – also meaning the pair has highly-valued expertise in engaging with companies' senior management.

Williams says the pair has always surrounded themselves with great talent. This is especially highlighted with Goodsell on the team – a portfolio manager with eight years' experience and former investment analyst roles at Fidelity International and Nomura Securities.

"She's experienced but quite a bit younger than John and myself and brings a great, fresh perspective to the team," he says.

"We've also got David Spotswood and Annabelle Riggs. David has covered telecommunications and financials for more than 30 years in the Australian market. We also have Terry Couper who has 15 years' experience."

Williams explains that each investment team member takes on individual sectors and stocks where they have close relationships with management, "and then we get together and we pick those best 25 stocks for the portfolio. Emma and I as co-portfolio managers obviously have final say."

As mentioned, Airlie has honed its investment process down to a 25-stock, best ideas portfolio and these stocks can come from anywhere in the Australian market. Because of the team's experience it can look at companies that are not always mainstream.

"We get classed a lot as a traditional value manager, which is not a term we really like because we're experienced enough and pragmatic enough to know that a company, on a price earnings ratio of 20-times, maybe a better medium term investment than a company on a price earnings ratio of 10-times," Williams says.

Joining the retail ranks

Airlie Funds Management first announced it would join the Magellan stable in February 2018. It was a clear opportunity for Sevior and Williams to use Magellan's operational and distribution expertise to expand into the retail investment market after building and maintaining a loyal institutional and high-net-worth investor base.

And as Williams reiterates, "nothing's changed in the way we invest."

"We still use the same process that we've been using for more than 20 years. Nothing has changed in the way we select companies – the macro conditions are always changing though," he says.

"At the moment the big things we're looking at are regulation and disruption. They're the big factors that are playing into companies at the moment. Five years ago we would have said disruption rather than regulation first."

This said, about one-quarter (23%) of the fund's concentrated portfolio is in financials – it is about six stocks in a fund which currently manages 26 active investments. Three of its top 10 investment ideas over the next three to five years include Suncorp, Link Group and Clydesdale Bank. It also holds a current position in Macquarie Group.

These financial companies are much less exposed to any outcomes from the Royal Commission than others. "Now regulation has really come to the fore and affecting a lot of companies both in the financial sector and the energy sector and we think this could play out in further sectors as the difficult political environment continues to play out," Williams says. FS

The quote

What we're looking for in management are sensible and rational people that we're comfortable investing alongside our clients' money.

Watch the video on www.fsitv.com