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02:
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Growing the global equities opportunity

The Loomis Sayles Global Equity Fund looks past the next news headline and builds positions in companies that should last well beyond short-term market turmoil

For all the recent uncertainty and volatility in global equity markets, one constant remains: opportunity.

Loomis Sayles Global Equity Fund co-portfolio managers Eileen Riley and Lee Rosenbaum say investors would do well to embrace volatility and challenging global economic conditions in 2019 because strong investment opportunities may continue to arise.

“Short-term volatility often provides us with entry points to build long-term positions in high-quality companies and opportunities to trim or sell positions at what we consider attractive levels,” the pair says in a recent fund update.

“Rather than try to predict macroeconomic events, we focus on companies with sustainable business models and attractive valuations.”

This might sound all too familiar to experienced global equities investors; so what makes the fund different in its approach?

Alpha generation

Sticking to a disciplined investment approach and adding outperformance among all the noise in global markets sounds simple, yet without proper consideration it can quickly turn sour.

For Riley and Rosenbaum, investment discipline means sticking to three key alpha drivers. Quality, intrinsic value growth and valuation will each work together to help determine the best companies and investment ideas.

“Investment managers able to identify quality and value will stand the test of time — ignoring the slings and arrows of short-term market fluctuations — and produce long-term investment performance,” Riley says.

Quality has several dimensions, she adds, including the sustainability of the company’s business model in its given market, the strength of management and their ability to allocate capital and ESG considerations.

Intrinsic value growth speaks to a company’s capability to grow profits and, specifically, free cash flow.

“Quality businesses are better positioned to grow their intrinsic value; it is the combination of quality and intrinsic value growth which generate a ‘duration effect’— in other words, they add value to a stock over time,” she says.

On valuation, Riley says the portfolio does not focus on relative valuation metrics when it comes to assessing businesses. She explains that commonly used valuation metrics, such as 12-month forward price earnings ratios, “do not capture the value derived from a quality com-

pany’s ability to sustainably grow its free cash flow over time.”

The portfolio managers believe keeping their investment decisions glued to these three alpha drivers is vital – along with the appropriate risk assessments – to help deliver outperformance.

Long-term focus

Co-portfolio manager Rosenbaum says investing in their best ideas from around the world and identifying business’ underlying fundamentals is key to performing well over the long term in international equities.

The Loomis Sayles Global Equity Fund seeks to generate long-term investment performance relative to the MSCI AC World Index, Rosenbaum adds, by identifying companies globally with attractive total return potential.

The fund’s unconstrained approach also allows the team to identify its best alpha opportunities to be “optimally combined in a portfolio leveraging extensive firm resources and research capabilities.”

“It is important to stress that being unconstrained doesn’t mean a portfolio of hundreds of stocks. A concentrated portfolio can be a good thing, if you are concentrated in quality,” Riley says.

“As important as diversification is, in our view, a concentration of very good ideas is always better than a broader portfolio which (by default) would include less good ideas. There is nothing to be gained by allowing good investment ideas to be diversified away.”

Loomis Sayles, which manages US\$250 billion (\$350bn) globally, employs close to 300 investment professionals with 75% dedicated to research and trading. The professionals are organised in small teams to debate and discuss investment decisions “openly and candidly with a great deal of transparency and sharing of ideas.”

“These investment teams are supported by the firm’s commitment to research across the broad spectrum of credit research, equity research, sovereign research, securitised research, macroeconomic research and quantitative research,” says Kevin Charleston, Loomis Sayles’ CEO.

Co-portfolio manager Riley says the ultimate aim of deep fundamental research on quality and value is to produce long-term returns by taking advantage of key inefficiencies, in terms of duration and mispricing.

“To capture the benefit of the duration effect an investor needs a longer-term view. That said, short-term market volatility is often driven by

more macro-oriented events and the underlying fundamentals of a business have not changed,” she says.

“By continuing to focus on long-term alpha drivers in periods of market uncertainty, investors can build position sizes in favoured stocks or trim positions that have not done well.”

What’s next in global equities

In their December 2018 update to investors, the fund managers say recent global volatility is expected to continue. Monetary stimulus will continue to be removed, trade tensions will continue and “political uncertainty persists in many regions around the globe.”

But again, this should provide several opportunities for the fund over the long term.

Even with a potentially less positive economic backdrop there are opportunities in financials, the portfolio managers say.

“These include companies which are beneficiaries of volatility such as financial exchanges, companies which are supported by broad secular trends such as ageing and increasingly affluent populations and companies with valuations reflecting an overly bearish economic scenario.”

Boston-based Riley and Rosenbaum expect the continued negative news flow around issues such as data privacy and market concentration will pressure technology and communication stocks in the short term, however several long-term opportunities remain.

“Whether it is search, e-commerce or social media, these services remain highly desired by consumers,” the investor update says.

Recently the fund also received a Recommended rating from Zenith, and the research house acknowledges the portfolio managers’ oversight ensures analysts “remain focused on the most promising opportunities.”

Over the longer term Loomis Sayles also remains committed to the Australian market. Serving institutional clients here for more than 20 years, the investment manager, in partnership with Investors Mutual Limited (IML), opened the Global Equity Fund in Australia in November 2018, and has just completed its first national financial adviser roadshow.

Wayne McGauley, Head of Retail at IML said “we are encouraged by the recognition of the quality of the fund by the ratings houses and demand for the fund from advisers and platforms.”

Loomis Sayles is an affiliate of Natixis Investment Managers, a global multi-affiliate fund manager. IML became a fellow-affiliate in 2017. **FS**



The quote

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