The Year That Was for the International Shares Fund

As part of the December 2020 Quarterly Video Series, we took a look at the year that was for each Fund. This video focuses on the Forager International Shares Fund.

Chief Investment Officer, Steve Johnson, is joined by Gareth Brown and Harvey Migotti, Co-Portfolio Managers on the International Shares Fund, as they reflect on the key contributors to the Fund's success over the last year. They also provide insight into some recent additions that have added value to the portfolio including Whole Earth Brands and Twitter.

Transcript:

Steve

Welcome, Steve Johnson here, Chief Investment Officer at Forager Funds, and we're recording our quarterly videos for the year ended 31 December 2020 and it was a crazy year. I'm joined by Harvey Migotti down the end and Gareth Brown in the middle. Congratulations guys, absolutely fantastic year for the International Fund with returns that we probably didn't imagine at the start of the year, let alone at the end of March when things were looking pretty hairy out there, but well done.

First, to you Harvey, what did you make of it all?

Harvey

Thank you. Good to be here. There's been some great stock picking across the board from the whole team. I think that really helped. The bottom up was good, we got the top down right in March. But it's more than that, I think it's the Fund's philosophy, the nimble team, the ability to move quickly, fund size and everything just came together really well for us.

Steve

It was a lot of nimbleness through the year, it was a pretty frantic time. You've just had a couple of weeks off and a nice rest on the beach. What did the time for reflection say to you about the year of 2020?

Gareth

It was nice to have some time off that's for sure. There was a quote that Charlie Munger made in a presentation late last year where he said the good investing requires this weird mix of patience and aggression.

We were aggressive for a lot of last year, and I think that was the right call. We were aggressive at the bottom and that really carried on through the year. I think increasingly it's becoming a time for patience. Now that doesn't mean we shouldn't be turning over rocks, but we should be thinking more and more about the moves we make and perhaps try to be a bit slower to come to conclusions.

Steve

On that front Jeremy Grantham published a pretty widely re-published piece over the last couple of weeks talking about bubbles, particularly in some US concept stocks. I know you read a lot of his stuff. What did you make of that? We've all come back from the break and a fantastic year feeling pretty nervous about things.

Gareth

Firstly, he gets a lot of flack for being a "perma-bear" and it's just not right. There was an article that he wrote three or four days before the bottom in 2009 called *Reinvesting When Terrified*. It was something I went back to earlier this year when the COVID crash was happening and it was really my north star for a while.

We mentioned it on that long webinar that you and I did on March 23 right at the bottom. He's got an amazing track record of those pivot points in markets in my opinion. The 2000 bubble, the 2007 bubble, the 2009 bottom. I find him a really fascinating character, he thinks quite differently than we do.

He's calling this period now a bubble in the bigger tech names in the US in particular. You look at the Tesla's of the world it's hard not to agree with him. From our point of view we just want to make sure we're not caught up in any of the backlash around that.

We have some things that are at the growthier end of the spectrum and we've aggressively been taking profits for more than six months and thinking about it in the portfolio management context, we just want to be careful not to get dragged into anything if there is an unwind there.

Steve

I think you do need to be careful, particularly with the overconfidence thing coming out of a really good year. But Harvey, you were adamant there's plenty of good ideas out there. I think just being back in the office together for a week and bouncing some ideas off each other and having a look in some different spaces, it's clear to me at least that this is not applicable to the whole market out there.

Harvey

I definitely agree. I think it's about balance, you have first the portfolio where you see value within growth stocks and then you have other things that have been left behind lagging, and there's a case for them to start working once again. Whether that be because of the unlock or whatever else there's a ton of opportunities that I see every day.

We were working on some two or three months ago that have already doubled and we missed

them just because we didn't look fast enough. The market's aggressive, but there's always lots of rocks to turn over and things to find.

So I have two charts here that I think it would be interesting, particularly when it comes to global valuations and we can put them up on the screen. This is the performance of growth versus value right here on this one. And you can see we're in very extreme levels since the GFC with money printing and rates continuing to decline to now almost levels that can't go much lower.

What's happened is that sectors perform well, but that also means that a big portion of the market's been left behind and part of the market is those stocks are finally starting to work now. You can look at the valuations as well, this is a chart of percentage of value versus growth. We have extreme levels, clearly upwards over the last two or three years, you've come to extended levels.

Some of these are amazing companies that will continue to grow and there is a right price for them. The price might be right at this point, but it's hard to see them going too much further. So I agree. There's bubbles in pockets of the market, but there's a lot of very reasonable prices.

Steve

I think you can see that even in some market indices, the UK market has gone absolutely nowhere over 20 years and Europe is largely the same. There's plenty of good debates to have about the value versus growth thing, and whether all this disruption is killing things, but the one thing that is clear is by number of stocks, you've got huge swathes of the market that have not participated in this bubble.

I think amongst that there might be some businesses that are in decline and plenty that are not and are able to reinvent themselves and move on as well. I think a really good example of the type of opportunity that's out there is Whole Earth, as you wrote about in the latest quarterly report Harvey. Really interesting business. Can you just give us a start with a quick insight about what it is?

Harvey

Really simply at a high level, the majority of the business is natural and artificial sweeteners. It's trading at a ridiculously attractive valuation for what is a staple, but also exposed to secular growing markets.

Organic and natural sweeteners is a category that's expanding really rapidly from a low level. To give you a sense, penetration in the US is 13% for this category. Globally it's only 3%. So you have a company that's compounding nicely at 5-8% a year at their earnings level and that's trading less than seven times EBITDA, which is operating profits before the amortization and depreciation, which you need to look at because there's some amortization in this from deals and M&A now.

Now what I really liked about this one is the setup. It's come to the market as a fire sale by corporate raider, Ron Perelman. He's been selling everything from yachts to artwork to try to deliver across this portfolio. Two of the assets he owned merged together to form what is now Whole Earth Brands.

So it's still flying below the radar for many people. It's a small cap stock. Not so small anymore, it's gone up a bit since we've dipped our toes in the water, but it's still a small cap. Not very well researched and just a gem that's hidden in plain sight, so to speak. So we're very positive on it. The fact that he had to sell it at a very discounted prices is an opportunity that we get to capitalise on.

Steve

Most of our investors are probably familiar with some of those brands. Equal is a very popular sweetener here in Australia and they have the number one position in a number of markets around the world.

You've been with us for 18 months now and I think it's something that's gelled really well between the team is that we all look at ideas from a setup perspective first, rather than doing five days of research on something and saying ‘I think it's a great business. I think it's a great price. Oh, there's a really good reason why this thing is cheap’. We try and start with that reason and unpack it first and often that's maybe a 10 or 20 minute exercise saying ‘this is interesting because … I'm going to do more work’. Rather than ‘I'm just going to work on this business for two weeks and then work out whether I think it's cheap or not’.

So I think that's worked really well. I love the setup here with a forced seller and that was going on post the effective IPO square, where he was dumping a whole heap.

Gareth

Chances are this business has been held back for quite a few years by Perelman’s financial situations.

Steve

Exactly right. Just the investment and people being freed from it, we often see that when there's a spinoff from a large corporate to a little business we see that work well.

Harvey

The business was over levered, the free cash was paid in dividends to pay off debt elsewhere. Now you can just imagine what a great management team, and this is a great management team, what they can do when this debt is unshackled.

You've already seen them do two large M&A deals, they've almost doubled their sales over the past year through M&A. They acquired some amazing brands in the US, sensible acquisitions and really exciting. So we feel good about that one.

Steve

Gareth, you wrote up a short piece on Twitter, but we could sit here and talk about it all day. It's been on the front pages of the newspapers over the past couple of weeks. Twitter's role in the US election, Twitter's role in what's happened over the past few weeks and then Twitter firing Donald Trump from the platform.

It's been a fascinating few weeks but, what do you make of at all? And what does that mean for what you're writing?

Gareth

We can talk about the thesis more or if you want to read the quarterly, we've sort of laid the simple thesis down there. It's really interesting being dragged into the free speech discussion here.

We've made some money on the stock, but it has come back a lot in the last few weeks. Donald Trump's been de-platformed on Twitter he's been banned permanently, at least permanently for now - we'll see.

It's a complicated issue. I believe in free speech but I don't want suicide bombers and paedophiles walking around typing whatever they want on the internet.

So it is a relative discussion rather than an absolute one and there's a fine line there that tech gatekeepers do have to walk and we can discuss whether they've got it right or not. But there is a policing of speech involved and it's a massive question I think about whose job it is to decide where that line is.

Steve

What does it mean for you as an investor in this business? Is it an important issue from a financial perspective and evaluation perspective?

Gareth

It certainly could be. Do you ban the sitting president from a mouth piece? This is begging for regulation and it may not happen under the Democrats, but it's certainly something that Republicans might want to look to down the track,

I think it's just if you want to be the gatekeeper to the global conversation then that's a price of doing business and something they're going to have to work around and be part of, whether they're the ones doing it or whether it's independent third parties doing it.

My personal thoughts are that it's still somewhat of a sideshow. The thesis here was, this is a massively under monetized asset. For anyone that doesn't use Twitter, it's really where the global conversations around topics go on now.

So if you're interested in politics, even if briefly around the presidential elections or sport or science or some weird little niche that's where the conversations between experts happen. And you can sit in your living room and be part of the discussion if you want. There's a lot of money they can make from that and it's been perpetually under monetized.

But a few things are falling into place there with some big activist investors chiefly being part of it. We think there's some really good potential in that business.

Steve

How are you seeing that financial side of things going? Are you noticing the changes that you're hoping to see and that the dollars turn up in the bank account?

Gareth

It was woefully managed five years ago, and I think they've made some steps that go back at least a couple of years now. The involvement of some activist shareholders was about speeding up the pace of that. I feel we're seeing that we still have some good growth in the user base.

I think interestingly de-platforming Trump is maybe part of bookending his presidency. For years everybody has been talking about the value he's added to Twitter and I'm not sure I buy it. It's definitely bought some eyeballs and created some interesting moments on Twitter, but it has made advertisers nervous.

This is a business that to this day is very much driven by brand advertising and maybe the end of the Trump presidency is a good thing for the actual dollars coming into the business.

Steve

I said to my wife this morning, what's Trump making of all this impeachment stuff? And she said, how will we know he's not allowed on Twitter anymore.

So there's a couple of interesting ideas in the portfolio at the moment. It's been a year of extraordinary change and performance in the fund. So if you pick up this latest quarterly report, you'll notice a lot of difference at the top end of the portfolio and that's all through the portfolio as well, and probably lots of change to come as we keep finding these new ideas and replacing some of the ones that haven’t worked out. Thanks for tuning in and thanks for your support.

This video is part of the December 2020 Quarterly video series. You can view the full December 2020 quarterly report here:

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