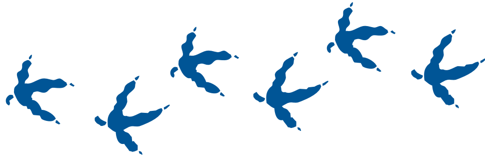

ARTEMIS
The PROFIT Hunter

Phillip Wolstencroft – Artemis European Growth Fund Q2 2009

Transcript from the Q2 2009 Film Club recorded on 2 June 2009.

Q1: After strong outperformance ever since you launched the fund, the fund has endured a tough 2008 and 2009. What has happened?

Over the years the fund has done very well in terms of outperforming the indices. 2007/2008 were poor years. Essentially we owned too many stocks where the profits fell versus the market. This dragged down the performance of the fund.

Q2: Your exposure to the financial sector, particularly banks, has hurt returns. What was the basis for favouring this sector and how do you see bank shares performing going forwards?

At the beginning of 2008 we had too many banks and this hampered returns last year. We owned them because of contrarian factors: they were cheap and unloved, and in general although their profits were being trimmed, it was by no more than the market. In retrospect, the banks had bigger problems and so the share prices were hit by that. When the news came out, we ended up closing our positions. But in hindsight, that was too late.

Q3: You also had a long-standing overweight to insurance companies, which has also hit returns – are you still comfortable with this position?

In the insurance sector, we've been overweight since the end of 2008. So it's been a fairly recent position and has actually helped performance of late. The reason for owning this sector is that whilst everybody else is focused on the weakness of asset prices, we've observed that the trading profits of these companies is improving. They're pushing up insurance premiums, and that ultimately is what drives their share prices up.

Q4: The market has rallied strongly since March. To what extent do you subscribe to the 'green shoots of recovery' argument?

There is certainly less bad news out there than there was, and if you're going to get green shoots, you have to have less bad news prior to that. In that sense I can believe that the market is recovering for perfectly good reasons and we'd be inclined to believe it for the time being.

In terms of a longer term outlook, I would generally be sceptical that there's going to be a big recovery. It's going to be pretty tepid over the next few years, but share prices really are driven by valuations and profits rather than by economies. And so from what we see, share prices are probably pretty good value.

Q5: You rely heavily on SmartGARP™ to filter the stock universe. Have you had to modify your use of the tool?

SmartGARP is a tool which screens stocks in Europe for the best combination of good valuations, strong growth and pleasant surprises. Over the years it has done very well. Last year there was a big shock to the economy and we struggled in that environment. Nevertheless, the rules of investment haven't been rewritten: it's still the case that stocks which offer good value and strong growth will ultimately deliver good results. SmartGARP helps us in that and it's showing plenty of signs that it's uncovering some of these stocks now. Traction seems to be improving. So we have confidence for the future.

Q6: Europe has a broad selection of stocks to choose from. Are you still able to find companies that are delivering earnings and profit growth?

At the moment the European economy is in recession and so some people are asking whether there are many companies out there which are delivering profit growth. The answer is they are few and far between, but they do exist. So for example we have a smattering of banks where they've got good balance sheets, and trading conditions are improving. We've got a few food retailers which are churning out solid growth and then we've got the insurance companies we touched on earlier and a fair number of oil stocks. So they're not abundant, but SmartGARP is certainly turning up a few gems at the moment.

Q7: What is company management telling you about the economic backdrop in Europe?

It's mixed. A lot of cyclical companies like car companies and industrial businesses are generally pessimistic. They can see that demand has collapsed and whilst it has stabilised, it's a pretty lousy environment for them. They are basically close to break-even. More defensive parts of the market like utilities and food retailers and telecom companies are pretty relaxed about life. And then the financials quite rightly are keeping their mouths closed; they don't want to attract much attention, but their businesses are actually on a bit of an improving trend at the moment.

Q8: Are there any regions you are nervous about in Europe?

We are largely avoiding Ireland and Spain and eastern Europe where the economic backdrop is very poor and the companies are suffering. Sector-wise, the profits of a lot of the auto stocks and industrial companies and basic resource companies are very depressed, they are not showing much evidence of a recovery and the share prices are very high. So we have largely avoided that part of the market.

Q9: Unlike sterling and the US dollar, the euro has held up very well over the past year. Has this surprised you and do you see continued strength going forward?

We tend to get as confused as most people about currencies, and don't really feed that into our analysis. We generally stand back from the politics, the currencies, the economies. We just constantly focus on trying to find the best stocks out there. That's what we have done, and what we will continue to do.

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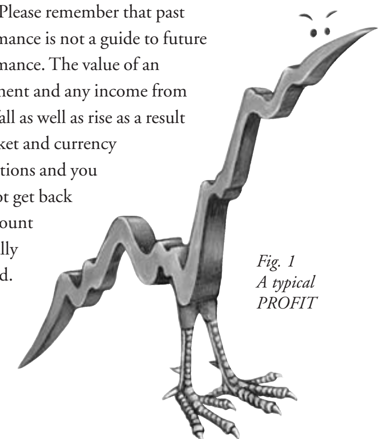

Fig. 1
A typical PROFIT

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