

SHINING A LIGHT ON..... ARTEMIS US FUND RANGE

At a glance

The US market is notoriously difficult for active managers to outperform; the argument is that it is highly efficient and therefore investors would be better to hold a fund that tracks the index rather than paying for active management.

For some time we have supported the Threadneedle American Smaller Companies Fund run by Cormac Weldon. When Cormac left Threadneedle we were concerned that the fund would not be able to continue to deliver in the same style as originally established. In this update we want to consider the new US Funds from Artemis where Cormac has gone.

In the meeting we had with Cormac it was clear that the hole left by his departure is deep but one we are sure Threadneedle can fill! Cormac set in place the process for his US Funds at Threadneedle and recruited much of the team which ran that process with him. When he left he took the key members of the team with him.

Therefore, although there is some argument that all he is doing is replicating what was at Threadneedle (which to some extent is true) there are some subtle differences. One of the key reasons for the move was to return to being an investor, at Threadneedle his position meant that increasingly he was being taken away from what he enjoyed and did best. The second subtle change is the size of the fund which will be small to start with and therefore gives him more opportunities which he was finding increasingly harder to do at Threadneedle.

The review will look at some of the key components of his style. Without a performance track record under Artemis investors will need to judge whether the performance at Threadneedle can continue without the team, and whether the team can not only replicate their previous success but improve on it.

The management team

Cormac Weldon joined Threadneedle in 1997 becoming head of the company's North America Team and lead manager of the Threadneedle American Select Fund in 2001, American Smaller Companies Fund in 2005 and American Fund in 2011. He is supported by Stephen Moore who joined Threadneedle in 2005 and William Warren who worked alongside both Cormac and Stephen for a number of years at Threadneedle.

They are also joined by four analysts who worked with them at Threadneedle (and who were personally recruited by Cormac).

The team are well respected and over the long-term have delivered a track record of outperformance.

Fund highlights?

The management team aim to deliver outperformance through stock picking but the key is selecting low volatile stocks.

Cormac describes the style of management as being macro aware – this is at its basic level identifying trends that are shaping the US economy and then finding stocks which will benefit from these trends.

Care is taken with all stocks as each stock must carry twice as much upside to downside. So an example Cormac discussed was Apple. There are, for example, three things driving Apple at the moment – the new iPhone 6, iWatch and growth in China. Analysts will set a price for the stock based on the information they have and then look at the risks. This could be that a competitor like Samsung delivers something better or entry into China is delayed etc.

They then work out what happens if the analysis is wrong – so for example looking at the target price and considering what the potential upside or downside is based on different scenarios. Only if the upside is twice as much as the downside will they then consider adding the stock to the portfolio.

This approach ensures volatility is kept under control and past performance indicates that investors do not compromise on returns through this style.

We discussed the US market and whether the US is overvalued. Cormac highlighted some areas where he argues there is still value to be made.

Two examples we covered, the energy revolution – the US is expected to produce the same amount of oil as Saudi Arabia and Russia by 2017 and it is highly likely over the next few years it will become self-sufficient. This brings obvious benefits to the economy but tied in with this is natural gas production.

Fertiliser used to be imported from China; China would import coal from Australia as part of the production and then export to the US. The US can now produce fertiliser significantly cheaper because it has the resources (natural gas) at home. Manufacturers are now coming back to the US because of these low costs.

The second area of interest is the US housing recovery. This has slowed and there are a number of possible reasons. One reason which was of interest was that people are simply not taking the step onto the property ladder. This could be that student debt has increased significantly and people don't want to take that step but also rent is now more expensive than mortgage payments so it becomes harder to take that step. There is also wage constraint where some wages have significantly increased especially in the energy sector but others haven't seen this. Cormac expects this to change.

The energy sector is a major component to US recovery and growth but this is not filtering to everyone as can be seen in the slowing housing market. When this turns, he expects this will provide some growth within the market. Another area which will help in the growth story is that the US is one economy tackling their aging population through immigration. A growing Hispanic

population is a big plus for the economy and will help with the continued growth. Other countries like Japan and Germany are still struggling to tackle an aging population.

To reflect this, interest rates are likely to rise next year but there will need to be signs of wage growth across the board and an improvement in the housing sector. The fund itself is positioned to take advantage of the next phase of US growth; for example looking to beneficiaries of cheap US natural gas, internet growth companies and domestic cable companies.

The US has clearly moved forward from the lows of 2008 / 2009, and the discussion with Cormac was fascinating. Clearly care is taken with companies, even in the smaller company's fund Cormac takes care and was careful; to say companies were 'smaller' rather than micro. Everything is about balancing risk and reward. The biggest danger is if they get the macro call wrong but that is balanced by assessing the risks of any stocks they purchase.

The three main funds are US Equity, US Select and US Smaller Companies Fund. There are also two others the US Extended Alpha Fund and US Absolute Return Fund. For investors the process is proven, clearly Cormac believes there remains value in the market and therefore the question for investors who believe there is value is whether they believe Cormac is the right manager to ensure they benefit from this. His track record is good but not all managers who move succeed in a different environment and that is for individual investors to decide on.

The source of information in this note has been provided by Artemis and is correct as at September 2014. These are notes from meeting the fund manager or representative and should not be seen as a recommendation to purchase any fund mentioned. Any reference to shares is not a recommendation to buy or sell. Should you wish to make a decision based on these notes we cannot take responsibility for this and you should carry out your own research before making a decision. You should note that past performance is not a reliable indicator of future returns and the value of your investments can fall as well rise.