Oldfield Partners

Panel Discussion

19th June 2017

Oldfield Partners (OP): *Claus Anthon (CA), Harry Fraser (HF), Richard Garstang (RG), Juliet Marber (JM), Tom Taylor (TT), Nigel Waller (NW), Sam Ziff (SZ)*

NW: Welcome to the Goring. I'm Nigel Waller. I'm CIO and I'm going to chair the panel discussion this afternoon. I want to say thank you to those of you who emailed in questions in advance because I'm going to use those as a basic structure for the Q&A. I do want it to be as interactive as possible so if you've got questions raise your hand.

Let me introduce the panel. On my far right, Juliet Marber, representing the Japanese equity product; Claus Anthon representing European equities; Tom Taylor for emerging markets; Richard Garstang for global equity income; and finally, last but not least, Harry Fraser for global smaller companies.

We're going to finish by 5pm for a cup of tea and those that want to stay on afterwards, we can. We can reconvene and answer any questions that you have.

I think there are a couple of new faces, so I'll just say a couple of basics about what we do before we continue, just to cover it off. We are contrarian, bottom up, value managers. We run concentrated portfolios, 17 to 25 holdings typically. When we're looking for individual stocks we're looking for a minimum of 25% upside over two years and in terms of macro views, we obviously have macro views but we work hard to ensure that they do not influence every part of the portfolios that we manage. We are very concerned about diversification with these concentrated portfolios, we are keen that the stocks are diversified by country, sector and theme, because we know if you're lucky or smart in this business, you're right only 60% of the time. If you have a strong global theme which you ensure is embedded in everything in the portfolio and you get that wrong, the entire portfolio is wrong, so we don't do that.

In terms of risk I should say volatility is not risk for us. Risk is the potential to lose money on a permanent basis. That is what we worry about and that is why we tend to limit our exposure to companies where there is a combination of operational and financial leverage, because clearly that can limit your ability to have the patience, which is absolutely a prerequisite of our approach to investment. That's patience on our side and the side of our clients too.

The first question is very topical. How do you see the investment landscape across Europe after Brexit and given the recent elections? Has it prompted you to change anything in the portfolio? That has got to go to Claus.

CA: In the European fund we decided after Brexit to increase our exposure to the UK. Initially we did it by buying into existing stocks we held like Lloyds and Bovis. Later in the year we continued to look for opportunities. We bought into a company called IWG (formerly Regus), operating within the temporary office space. At the time there were concerns over Brexit and we felt the market did not appreciate that nearly 75% of its business is generated outside the UK and of course with the devaluation of Sterling the company should do well. We purchased a position and are happy with that performance since then.

If we move to Core Europe we have now had elections in France and in Holland and for us they have cemented the attraction of Europe because, in my mind, Europe is extremely cheap as a region compared to others. If you compare it to the US market, normally the US and European markets have traded in a relative performance band of around 20% since the 1970s, but since 2008 after the financial crisis, it's just been a one way bet for the US as we all know. At the extreme, back in December last year, the relative performance differential between the US and Europe had reached over 100%. We don't think this can continue forever so we feel we will see a rebalancing. Also, based on Shiller P/E's, the US is today trading around 29.5 times, whereas Europe is only trading around 16 times, so there is definitely upside in Europe.

The reason for this discrepancy can be explained by Europe having been through a weak economic situation for years, especially with the recession in Southern Europe but it has also been bad across most other European markets. Although many European companies have gone through major cost cutting programmes and been very successful in that, they never managed to convert that benefit into better earnings as the weakness of the European economies hit the companies' revenue line. However, all that changed last year when for the first time in many years we saw a recovery in earnings. With leading economic indicators across Europe continuing to improve we expect further recovery in earnings and on that basis are quite confident that we're likely to see Europe continue to outperform.

NW: Are there any particular bright spots; so country, or sectors?

CA: Apart from the UK, which is slightly different because of Brexit, in Core Europe we are quite happy with what we already hold as many of these companies should benefit like Siemens, ABB, Maersk and Investor (being a Swedish holding company exposed to financial and industrial companies).

NW: We also had a question about the UK and specifically around relatively large exposure both in smaller companies and in the global equity income fund. So perhaps if we ask the two of you, given the UK is more specific to you, first of all any views and how they have changed since the election? Then the second thing would be whether or not the scale of your investment in the UK is a permanent feature for you or not?

HF: On the first point, this recent election, although it's another shock, it's not as serious as Brexit will be in terms of whether it's positive or negative. It's going to be less extreme. Potentially with a minority government that needs the help of both the Scottish Conservatives and the Irish DUP, there is a chance that immigration might be cut a little bit less, which might help some of the companies like Bovis, but that's at the margin. Our main thinking and the reason why, as with Claus, we added to a lot of companies after Brexit was simply the underlying valuations, regardless of what we think will happen to the domestically focused UK companies, have got so cheap that there is low downside in the worst case and if we muddle on through then returns should be much better in the UK than in other countries.

In terms of will there be a permanent bias, I think there won't be and I say that because of the 60 companies on our watchlist only about 15 are UK companies and so my expectation is the weighting over time will change but it doesn't look like it will in the immediate term.

RG: I would agree with many of the things that have been said already. A couple of additional thoughts though. We found the opportunities in domestic UK. The global equity income strategy does hold companies like BP and Rio, which means we have a high weighting to the UK but not necessarily UK focused companies. But we see the opportunities in UK domestic and, like others, added to companies like Bovis and Lloyds after Brexit. Both had yields over 6% and were trading under book value. Valuations were very attractive and you didn't need to spend as long worrying about the macro, the business fundamentals were good enough to allow for decent returns over the long run and you could take advantage of those prices.

More recently, at the beginning of this year, we purchased a couple more UK domestically focused names: Greene King, the UK pub group, and Britvic, the soft drinks manufacturer. Again, picking both of those up at just under 5% yield. In the case of Britvic it was trading on 12 times earnings. It's historically traded on close to 17 times. It's a consumer staple and if you look anywhere else in the world, consumer staples are the darlings and yet, because of Brexit, you were able to pick up this high quality, high free cash flow generative, high returns on capital business at a really good valuation.

In terms of bias, it's a much more obvious question for global equity income because the UK market does have an attractive yield. And we do target a portfolio dividend yield that is at least 1.3 times that of the MSCI World. So it's easy to get drawn to those high yielding markets. However, when we look for ideas we look at the yields on a market by market view, so we don't get a bias towards any one particular market. So if we're looking at the US we think about company yields relative to the US market. The UK has provided some good opportunities recently. But only about 10% of our current watch list is UK based.

NW: Thank you. I suppose any questions on UK and Europe from the audience?

Q: You referred to the relative valuations of Europe versus the US. If you strip out the effect of US technology stocks, are things as extreme?

CA: No, it wouldn't be as extreme. There's two things in there. One is the currency. We have stripped out the currency but we still have a strong outperformance of the US of around 80%-85%. Technology, I will have to check.

SZ: If you look over history, the US does trade on that metric on the Shiller PE, so the average of the last 10 years, is at a premium to Europe, probably around 3 to 5 times historically and that gap's just widened massively over the last seven years. I think on the technology point, if you look through history, back in 2000 it was all about Windows and Intel, so actually throughout history the technology disruption has come from the US often as well, but you didn't get that massive divergence in valuation of those markets. So it may well be that it's partly that but I don't think it explains all of it.

Q: How worried if at all are you about banking problems in Italy and Spain, for example?

CA: For us in the European fund, we don't have any exposure to the Spanish or Italian banks. We decided to hold some of the safer banks in Europe, which we see as Lloyds Bank and ING in Holland and then on the other side, to take more risk, we hold a position in a Greek bank but again would never hold more than a 2.5-3.5% position. On the Spanish banks, we don't really understand their balance sheet exposure likewise with banks like Deutsche Bank and Credit Suisse. With Alpha Bank in Greece we feel it is cheap enough, trading at just 0.3 times book which we find extreme. So with the Spanish and Italian banks trading at 0.7 times book value and upwards, we'd rather hold something at 0.3 times book value but could have a 4-5 times upside.

Q: Yes, I suppose my question was whether you thought it was contagious and as a result a headwind to Europe or whether in fact the chance of a banking crisis after one so recently is pretty small.

RG: It's got to be somewhere in between, hasn't it? I think the chances have reduced over time as we have seen actions taken to improve the situation. But the Europeans have been much slower to deal with the problem than the Americans. The Americans really dealt with it very quickly, injected huge amounts of capital and ultimately rectifying some of the problems more quickly. The Eurozone has a problem around regulation. It's not able to do as much, not able to take as much control and restructure the banks, but we are getting there and we have seen that recently. I think probably more in Spain than we have in Italy. Italy's still got more problems. The non-performing loans are horrendous and the way to get rid of the non-performing loans takes a long time. Spain looks like we're on a bit more of a recovery. Asset prices are improving a bit as well. You also saw recently Banco Popular was taken over by Santander, so they were willing to take quick action around a bank that would have gone bust and could have resulted in contagion. But another bank stepped in, with political support, and solved the problem. So perhaps you're starting to see more solutions than problems in these areas. But never say never to a banking crisis and there are still concerns in Southern Europe.

NW: Let's move on. Japan, we've had three questions on Japan. There is a bleak consensus outlook for GDP, headwinds such as population decline, is it very hard to find value in Japan?

JM: Following the banking crisis and the stock market collapse, the GDP fell and bottomed at the time of the earthquake in 2011 at about 0.6%. Since then it's recovered a bit and obviously since Prime Minister Abe came into power, he has focused on trying to boost nominal GDP.

In terms of the population, in terms of the number of live births, it's been declining since 1947, except for the baby boom, which was 1960 to 1974. That declining population didn't stop any of the economists forecasting 6% GDP growth in 1990, but of course it is a problem in terms of final demand. But for us, looking for value opportunities, then of course it increases the pressure on Japanese companies to have to adapt and to change to falling demand conditions domestically. So we find this quite a big hunting ground and we can also find companies, like NTT, which in a society where there's a seniority based pay system, benefit hugely from falling costs as a large number of highly paid senior employees retire. The group still saves money when at the same time they increase the base salaries of graduates. They've actually started to restructure, they've increased EPS by 60% over the last four years, increased shareholder returns and we think the next stage is going to be the restructuring of NTT's real estate assets, because as they shift from analogue to digital, they're not going to need a lot of their old switching stations and costs can be cut further. We still have a minimum of 25% upside for their share price.

HF: Japan has been renowned for having companies trading on a low price to book. They tend to have a lot of liquid assets and even after Japanese companies have done relatively well we've still got, on the watch list, three companies that are trading below cash or at cash. These are all profitable companies. So I'd say, in the developed world, Japan remains one of the cheapest developed markets.

RG: We're still finding opportunities. We own Toyota, for example, one of the world's leading car companies. It's got oodles of cash and investments, which are 70% of the market cap. You're getting a 3.5% yield. It's trading just under book value now, which it's rarely done in the last couple of decades. So you do still get the opportunities to pick up these world-leading companies at good valuations. The shift in governance is happening - payout ratios are improving, buy back ratios are improving. That's all coming back to us as shareholders, which is great because they do have these large cash balances. It just needs to continue happening.

NW: Juliet, would you concur with that in terms of the improvement in governance and capital allocation? Are Mr Abe's arrows hitting their mark?

JM: Yes. I started looking at Japan in 1986. That is a long time ago and I would only caution that it tends to be three steps forward and then a step back. So I agree with my colleagues, it's just the speed. The direction of travel is very positive but sometimes we wish the speed would be faster and for example the bank, MUFG, has just announced, within the last week, that in their next midterm plan they are going to cut the number of employees globally by 10k and they're finally going to move domestically to what they call One MUFG, as they have done overseas, which is that they've tried to integrate some of their overseas duties to cut costs, but in Japan they're saying that these changes will take two midterm plans or ten years. Do you want to add anything, Andrew?

AG: They target 60% cost income ratio and they've exceeded that in the last three to four years, as they've expanded overseas. At last perhaps we are seeing progress, but it will take its time.

NW: Any questions on Japan? No? Ok, let's move on to emerging markets then. Tom, you've been asked about headwinds and tailwinds and bright spots for the remainder of 2017. What do you have to say?

TT: It's been a very tricky year for the value investor in emerging markets. Of course the flip side of that is that we have quite a lot of upside and a very significant skew towards cyclicals. That is really where we find value within the emerging market space. A lot of money has come in to emerging markets, primarily into ETF's and has found a home in Chinese internet stocks that are trading on 50 times earnings. That's quite difficult for us, given that really what we have left to invest in is the cyclical space. Probably the most attractive thing about emerging markets for us, is that we do have 45% upside to the price targets in the portfolio, but it could be a very difficult rest of the year.

NW: Any questions on emerging markets specifically? No? Ok, we've got a more general question next, which is applicable to everybody. Can QE come to an end without causing a recession?

TT: That's a big question. A difficult one for someone who doesn't really look at macro. I think QE and the winding down and hopefully the normalisation of central bank balance sheets has been very well flagged to the market, so there probably aren't that many surprises in the direction of travel. We hopefully won't have a taper tantrum type affair again. It's difficult. In any circumstances you're taking liquidity away from emerging markets, that can be problematic. The interesting thing, as Claus mentioned, the US is quite highly valued and a lot of the rest of the world is fairly lowly valued, so there is an amount of money that can continue to flow towards emerging markets.

NW: Any other views on QE and avoiding recession from our panel?

HF: I would just say that in the 30s, the same thing happened. The Fed had to pump in a lot of liquidity. Afterwards they didn't remove it. It just became less of a share of US GDP as the US GDP grew and I don't see why that couldn't happen again. But as Tom says, there's so many different potential outcomes.

RG: It also comes back to the point that some of the QE was used to recapitalise the banks and that doesn't need to come out, it's just recapitalised an over leveraged system in the first place.

Q: Another macro question about the EM fund, strong dollar correlation and the commodity dependence and whether you think these ties are still absolutely intact or whether there's some sort of break as people think in the last year or so.

TT: That's been changing for a long time, the overall commodity EM focus. I think that continues to get weaker and weaker, just as those emerging markets develop and their domestic economies become a bigger share. If you just look at Asia, which is an oil importer, there's no reason why, when oil goes down, that would negatively impact what is the largest part of emerging markets. So the commodity part of emerging markets is becoming smaller over time and the impact on emerging markets is also.

Q: And then on the dollar front, strong dollar effect.

TT: Yes, it's almost the same argument there as well. For us, we only need to find 20 stocks. That's the beauty of it. We don't have to buy an index, we don't have to mimic the index, so there's clearly stocks that do well from a strong dollar and there's clearly stocks that do badly from it. So we can be very selective.

Q: On that subject, can you find any value in the consumer stocks in emerging economies?

TT: It's harder, it is certainly harder.

Q: It's always been expensive but it's always been strong.

TT: For many years now, going back to 2009 - where these defensive consumer staple type of stocks became and still are pretty highly rated - we're not going to be paying 30 to 40 times earnings for a stock. We do have some on 15, approaching 20 times earnings, but that's where we can see some growth and that stock needs to be doing something a bit special, entering a new market which is untapped or launching new products that can see that growth supported.

Q: Sticking with emerging markets, China, do you have any views on whether it's learning in this transition from investment based growth to consumption led growth or whether the banking crisis is going to bring it down?

TT: The government is very clear on the switch that they wanted to make from the old investment led model to a more consumer and more balanced overall economy and they've been progressing towards that over a number of years. The consumer sector continues to grow, retail continues to grow at plus 12% every year. We would love to be able to get that sort of growth, but we're not going to pay the valuations I mentioned before, 30 to 40 times earnings, to be able to do that.

We've found an interesting way to play it though through a Chinese stock called Lee and Man Paper, which is a container board manufacturer. Container board goes into cardboard boxes and when we looked at that stock we found that 70% of its end demand was the consumer. Particularly internet with Alibaba, like Amazon, has lots of cardboard boxes being delivered. You can get that at an old economy type of valuation that's still set for growth in that newer sector that's doing well.

So the government will continue to rebalance. I think they've been successful at it so far and that's not likely to change. China is effectively a closed financial system, so you can see that debt continuing to go up. They'll have episodes where it pops up. The government will push it down. It will move, it pops up again and will be called something else, but it can continue to increase because it's a closed financial system. So it's worrying but we have no idea when or if that level of debt will bring China down.

Q: Can you just go back to the macro policy, which I appreciate is not your specialist subject, but all the same it looks as if we've been through a period of 10 years where monetary policy has been both coordinated and extremely loose. It is possible now that we're on the cusp of some sort of change in that respect, change is coming from the US where there's serious talk of selling securities rather than buying securities. Would it be possible to go through each geography and ask the fund managers what monetary effect that action might have and if it came to that, take Japan, and whether two diametrically opposed monetary policies, one very loose, one very strong, are going to continue?

JM: I'm sure you've read that the Bank of Japan has been buying about Yen 80 trillion of bonds per annum and there's talk now that they are not going to continue with such a high level. Monetary policy is being tapered slightly, The Bank of Japan is being very clear in indicating that they've made mistakes before and that they are going to be very cautious about removing any of their stimulus. And they are still, as of last week, according to Mr Kuroda, committed to trying to fix the 10 year bond yield at around zero, which in the face of the Fed raising rates, all things being equal, we would expect would lead to a weaker yen. But of course all things are not equal because of the prospect of Mr Trump's tax cuts and his opposition to the yen being too weak versus the US dollar. So that's why, for now, we would expect the yen to trade in a range, probably from 115 to 100 versus the dollar.

Mr Kuroda will be replaced or his term extended in the next year and that will lead to uncertainty in terms of the Bank of Japan's monetary policy as we approach that time. At the moment there is talk that he will stay on and therefore the current monetary policy will continue.

CA: In Europe they have already started to slow down QE. I can't see why that should not continue considering the economic recovery. In the US we are definitely experiencing a recovery and as I said earlier we're starting to see that in Europe as well with, GDP growing in Germany and France, so I can't see QE stopping, so long as we have the underlying growth coming through

The UK, I can't say, I don't know what's happening with the Brexit negotiations and where we are. That is a very difficult question to answer.

JM: I mentioned before that Prime Minister Abe is focused on stimulating nominal GDP growth and achieving The BOJ's 2% inflation target which is a long way off in terms of what Claus said. The problem for Japan is to try to stimulate growth, change the deflationary mindset, (which we think would happen if inflation could exceed 1%), and at the same time maintain control of the 10 year government bond yield. Achieving all of the above will not be easy.

TT: I guess we're talking about the Fed for emerging markets and if there's an increase, as there has been an increase in interest rates, that's taking liquidity away from the emerging markets and tends to expose things that are of a negative nature in emerging markets. Normally debt and companies and governments can get into problems with debt. In the portfolio, we have companies primarily with a very strong balance sheet and also we do not hold emerging market banks, so that helps mitigate the debt problems there.

For the US, it looks like a very slow protracted interest rate cycle this time. So we're not expecting very dramatic moves in US interest rates.

NW: Richard, how does this impact on your global search for value and yield?

RG: I agree that it will be a slower burn. A couple of other thoughts. First of all, I think the areas we're finding most value are cyclicals. And we're really only going to see interest rate hikes under good economic conditions which then supports some of those cyclical companies where valuations are more attractive.

The other thing, we have talked about this before as well, that generally a higher interest rate may actually be quite good for value stocks. It's the concept around the discounted cash flows. The cash flows of growth stocks tend to be far out in the future but, with low rates, the discount rate applied to these cash flows is low and time is therefore less of a concern. While rates are low, that works. But it would reverse with higher rates and then the companies with near-term cash flows would looks more attractive. So you can think about the impact of higher rates that way.

Q: Just staying on Europe, do you think it's possible that in response to Brexit, the EU tries to actually carry forward it's dream of fiscal union and if it manages to make progress in that area, it seems to me it would be quite risky and likely to choke-off the underlying growth in Europe?

CA: We are getting more Pro-Europe with Macron winning in France and same can be said about The Netherlands. Fiscal union could happen but as we know it will be difficult, especially with high unemployment in Southern Europe. That's the same as we've had for years.

HF: In the UK, we've had a union with Scotland for 300 years where we've had the same language and similar culture and that even looks fragile. The idea of 27 countries with very distinct histories and different languages, there's less chance I think.

NW: We've got a few more questions that have been sent in. Richard and Sam, on global equity income, it's been pointed out that in the video on the website, you talk about a majority of your competitors' equity income funds being very narrowly focused. Tom was talking about emerging market valuations with regard to consumer staples. Could you talk about the fact that so many of your competitors are narrowly focused on these sectors and the valuations you see in such sectors?

RG: We've touched on a few of these points already. Consumer staples, healthcare, utilities have been the darlings of the global equity income space for some time now and valuations have reached quite stretched levels in our mind. You're paying 17, 18 or 19 times plus for many of these businesses. They are good businesses, we wouldn't disagree with that, but there is a price for everything and we think the potential returns going forward, given these starting valuations, are less attractive. It seems particularly relevant in the global equity income space. These bond proxies have paid good dividends for a long time. But we're now finding they are having to use ever more of their earnings and pay-out ratios are going up in order to support the yield. They've also used their balance sheets to help and keep returns going. We believe there is a crowded trade in these areas within the global equity income space and we are concerned about diversification of income sources. I think you can find good companies that are essentially sound, give you good returns over time, but are not in these specific areas where valuations are stretched. You can go to Rio Tinto for example and get yourself a 4% yield. It's got a very good balance sheet, it's the bottom end of the cost curve, but you're playing a different strategy - it's the diversification of income sources which we think is important.

NW: Following on more generally, we've talked about Europe and Japan a lot and we've touched on the fact that the US market looks expensive. Does that mean you [Richard and Sam] and Harry for instance, as our global equity managers in the panel, you're finding it difficult to find value in the US full stop?

RG: At an aggregate level it's expensive. The Shiller PE, which is the price divided by the average earnings of the last 10 years, to try and take out the cyclical effect, is on about 27, 28 times now. It's only been higher twice in the last 100 years. We are really getting to some quite extreme levels. So at an aggregate level we do struggle. But there are still opportunities at the stock level. We most recently purchased IBM. We paid 12 times earnings and we're getting a 3.5% yield. We think the business is very interesting. It's going through a bit of a transition where some of the legacy businesses are slowing. But it is taking part The Cloud, it is taking part in services and those areas will soon become the drivers of revenue and earnings growth. We owned Microsoft for a long time and everyone said the business was struggling, it was not growing, it was boring but actually when you get a couple of key drivers working and the top line inflects, things look a bit more interesting. In that case it was Microsoft's Cloud business, which is also a space that IBM is playing in. We get 3.5% yield with IBM while we wait for the value to be realised.

NW: Harry, what are you finding in the US?

HF: I agree with Richard that on an aggregate level it's not as cheap and actually frustratingly so, in the sense that often some of the best companies we find are in the US and they're never quite at the valuation that we want. But that said, we've recently bought a company called Oceaneering which is the market leader in remotely operated vehicles for offshore oil projects. They have a 70% market share. They're used throughout the whole process, from the beginning all the way to decommissioning and they generate high returns on capital through the cycle.Their market position has got stronger over the last three or four years. We've been able to pick it up at the lowest valuation in its 30 year listed history. So we do find value there, but less than elsewhere.

NW: What we always do at these panels is ask each panel member to suggest their favourite stock for the year ahead and I had a look back at what we did last year. So just to give you that before I ask them. Last year Tom gave us Samsung, which I can tell you was the best performer of the panel, 60% rise against 18% MSCI World for the period. Richard Garstang gave us MUFG in Japan, up 55%. Claus cheated and had both Maersk and Exor and Exor was up 55% and Maersk was up 44%. Harry had 34% from Weatherspoon, these are all dollar returns. Robert had Seven & I which gave us 6% return. Could we ask you to talk about your top stock for the next twelve months?

JM: There are a number of stocks with upside of more than 40%, but I think probably I will choose the one with the highest upside, which is JR East, the railway company, where we've got 53% upside based on the defensive railway business, the existing property portfolio and the redevelopment of their largest asset, which is the redevelopment of Shinagawa. Shinagawa is an enormous, 100k square metre tract of land in the centre of Tokyo, which was used as a marshalling yard, which is being redeveloped to include a new station, offices, shops and hotels. The new maglev train will be based here in 2024. Part of the redevelopment will be ready for the Olympics in 2020.

CA: It may sound stupid, but I'm going to say Exor again and the outperformance will continue. It's an Agnelli family holding company and if you take the sum of the parts valuation of all the businesses, you end up getting Fiat Chrysler at a multiple of around 3.5 to 4 times earnings. We just heard that there are car companies around the world trading on 5 to 7 times and I think this adjustment will take place, I see it will continue to move higher even though it's already done very well.

TT: I want to say one of the commodity stocks, just because they're so unloved at the moment, but I am going to stick again with Samsung Electronics, partly because we're halfway through the year, so there's only half to go.

NW: No, no – your time frame is the next 12 months!

TT: I'm still sticking with it. Semi-conductors are doing very well, this industry has changed. The mobile phone side of it is picking up and doing well with the launch of new Galaxy S8 and the display business is doing very well. Trades on unreasonably low valuation, has around 25% of its market cap in cash and the corporate governance is improving vastly.

NW: Do you see any threat to the semi-conductor business? It is earning a disgusting return on capital despite the fact the amount of capital it has to invest. Also, can you comment on corporate governance including question marks around whether elements of the Lee family will go to prison or not.

TT: Semi-conductors, I've been watching since early 2000s and it's an industry that has become highly concentrated. There used to be around 20 players back then. There's now three players and they are very focused on profit maximisation. The demand backdrop is very positive and they are effectively not incentivised to increase supply much. So the high operating margins that they're making now, I think will continue. In fact, I think we're still in an upcycle. But those cycles, rather than being very dramatic as they have been in the past are going to be at higher level and rather shallow. So you'll see that continuing.

The corporate governance has improved an awful lot. The shareholder return policy they put in place is generous. They have a lot of net cash sitting around to help with that. Unfortunately, yes, Lee Jr. will likely be heading to jail. In the past, many of these chaebol families have seen family members go to jail and still be able to run the businesses from behind bars. Not an ideal situation but it is what it is, but Samsung does have very, very talented and capable managers in each of those main divisions and the overall strategy is already set. So we don't really see it having a large impact on the company.

RG: I'll go for our most recent purchase which is Greene King. We bought it earlier this year. We paid 10 times earnings, it's trading on 1.2 times book and it gives us a 4.5% yield. The dividend has actually compounded at 8.5% since 1950. So we feel very comfortable that the business will continue paying us a dividend which will grow over time. Actually, Sam pointed out to me the other day that Unilever has compounded its dividend at 8% over a similar timeframe, but you pay 20 times for that business. The other thing we like about Greene King is that it operates in an industry that been going for 300 years and the risk of disruption is low. And, despite Brexit, the UK election and the European elections, we'll probably still be drinking beer in 300 years' time.

HF: This time I'm not going to pick the largest holding. In fact I'm going to pick the worst performer which has been a company called Dundee Corporation which is a holding company in Canada. They have a whole host of assets. Many of their assets are unpopular currently because they tend to be early stage commodity companies in particular, early stage gold companies. They're also building a big hotel complex in Vancouver, which again is not generating any cash yet. The company has net assets of $13 per share and it's currently trading at less than $3 per share. We also may be at an inflection point as some of their assets become profitable including their hotel. They've reduced costs across the group and the net asset value in the last quarter at last grew. It's taken longer than I thought, but the moment the net asset value stabilises and they become cashflow generative, I suspect that enormous discount will narrow. We've got over 200% upside now and that includes a decent discount from the net asset value. So that would be my pick, but it's not the largest holding.

NW: Any questions from the audience?

Q: Do Dundee know about hotels? Is this hotel they are building going to be successful?

HF: They actually have got quite a lot of background in construction, but are they brilliant at hotels? That's still untested. Property prices in Vancouver have increased dramatically over the last 10 years, so they should be able to refinance and possibly sell down some of their stake at a higher valuation to book value.

NOW: But they're intending to manage it themselves or they're going to outsource it?

HF: They own 40% of the hotel group but a majority share in the company running it.

Q: Could you give us the bear case for Greene King?

RG: The bear case for Greene King, I think it would be around macro concerns. Whether people still go out to drink beer and have food. Obviously people worry about spending habits given Brexit and the UK election. There's been a transition over time with more people eating out and that's helped margins. That can reverse.

The other area of concern would be costs. You've got higher minimum wages coming through. You've got rental increases coming through. So you could end up with a squeeze on margins, coming from higher costs and coming from lower revenue. Other things - they've recently bought another pub business, Spirit, and they are having to integrate that. That ultimately may provide them with some good cost savings to offset some cost pressures, but there's integration risk and Greene King has taken a bit of leverage to do the acquisition. It does have debt but there's a good amount of freehold property backing.

Q: The history of Greene King to which you refer was built without debt. Under Anand Rooney debt has gone up to well over a £1billion plus and that's the thing that's a worry. It's never really had any debt until Anand Rooney came on board.

RG: That's very true, but it at least does have the freehold property to back it, but you're absolutely right, over the long run it has used debt to finance its expansion.

HF: The debt is also structured in a way that there's no bullet payment and it's relatively long term.

Q: Generally speaking, do you see value left in Tesco and if so, is it going to survive the Competition Commission's ruling?

NW: In terms of the CMA review, we think that should be fine. We're content with the focus of that review at this point, as is the company. We met with CEO Dave Lewis about two months ago to talk through Booker as well as Tesco. We berated him for overpaying for the asset pre-synergies. He is paying a very high multiple. His argument is that he had to pay that multiple or he wouldn't have got it but what emerged from the discussion is that there are a lot more in the way of cost and revenue synergies to come out of that combination of the business which he has not publicised. If that's true, then the post-synergy multiple that they will have paid will actually fall down into a level that we could understand, mid to high single digit EBIT multiple, which we'd be happy with, although most of the existing synergies that they've highlighted, £275 million would effectively go to Booker shareholders.

In terms of Tesco overall, it's all about the UK business and trading and that does seem to be improving. Volume growth is just about still happening despite the inflation that we've seen come through over the last 6 months, particularly in the last quarter. They've had 6 quarters of like for like growth. We value it on a sum of the parts basis and we get to a fair value of around £2.70 as a fair value. Now that assumes that they get back to the upper end of their guided range of margin, 3.5 to 4%. Clearly if that doesn't happen, that will reduce the potential upside from standalone Tesco, but we're content with it for now.

Q: Is that valuation post-Amazon (bid for Whole Foods)?

NW: That is pre-Amazon and I think it's fair to say that we're going to have put our thinking caps on and think about that one. I think, (we haven't discussed it as a team) it's fair to say that long term, this is not a positive development for any of the food retailers around the world. They're clearly spending a lot of money in the US with Whole Foods and will try and develop a model which presumably they'll then bring to the UK. So we think we've got some time. The question is what happens to the multiple accorded by the market to this business? Is that fear going to stay in the stock price for too long for us to produce the return that we think is possible? If we're not going to be able to get a 14 times multiple on what we think is the sustainable margin in the UK, then it would undermine the investment case, so we need to think about that.

It gives Amazon access to a vertical supply chain, knowledge which they don't currently have in fresh food, so that's something that we worry about as investors in food retailers. It slightly validates the concept of bricks and mortar as a complement to online in food retailing. So I think there's a validation of that, but yes, the thought of Amazon doing anything really is something we need to process and clearly the market's worried about it with the food retailers down 3 to 7% on Friday.

Q: More generally on Tesco, if you didn't have it, would you go out and buy it today?

NW: We need to think about this particular transaction first to answer that question. In terms of current upside, yes, but we need to process the potential for how long it might take to affect the fundamentals in the UK and whether the market will accord Tesco the fair multiple we currently think reasonable.

Q: Can I ask more about Exor and the discount and whether that's changed and what is the market worried about with the Fiat Chrysler business?

CA: Let's go first with how cheap Fiat Chrysler is. So let's just say the main business today is composed of CNH, Fiat Chrysler, Partners Re and the Economist which is a smaller magazine, and Ferrari as well. If you add the value of all these things up, you get to a valuation which, if you strip out Fiat, gives about 3.5 to 4 times earnings, much cheaper than other car companies. Fiat Chrysler is a company we have followed for many years and there's always been some uncertainty about whether they can succeed as a company. Chrysler is the third largest player in the US, but they have managed to be very profitable with that business. At Ferrari's valuation, going back five or six years, people initially thought it could be worth three to four billion euros, and when Sergio Marchionne said it could be worth 10 billion, people laughed at him, and said that it wasn't possible. Today it's worth €15 billion. So you can maybe argue that Ferrari is too expensive, but in my mind, I do think Ferrari is a brand. I think it will continue to have a very high valuation. I'm sure any Middle Eastern buyer would buy it, considering they spent 8 billionon building Ferrari World in Abu Dhabi. If they can build that as a fun place, what would they do to get the brand themselves? So I think there's definitely a value in it, and on that basis that's what we've seen- it's gone about 50%, and it's because people are starting to realise the underlying value in the company, and I think there's more to come.

Q: There's a certain irony in the value being in a very highly valued stock. It's a very highly priced holding but it's the other components that hold value rather than in Ferrari.

CA: It does show that Sergio Marchionne is a master financier. He managed to build and change his company. People still talk about him stepping down in 2019. It's said eventually he will get into a deal with GM and do a merger or something along those lines. No one knows if it can happen, they deny it all the time. It will happen eventually and I'm sure that the family would like to get out. They want to keep Ferrari, but they don't really want a stake in volume cars, they would be happy to sell their stake.

SZ: That's probably a key opportunity. Fiat trades at a discount to the other auto manufacturers, partly because it's probably under invested over the last 10 years, relative to the large operators and the amount of investment that's required at the moment in autos is clearly driving down valuations in the entire industry. But the family and Marchionne couldn't have made it clearer they want out of the business, really and if they are able to, they'd be making a general positioning of the business over time away from these capital intense Italian businesses. They purchased Partners Re, which is now half of the net asset value of Exor, so that's a re-insurance business in the US that trades effectively at book value and it's historically delivered returns in the low teens so we're quite comfortable with that. Ferrari may be a bit expensive but a long term success story. So hopefully they exit Fiat and re-deploy the capital elsewhere, which is what they've worked towards over the last four to five years.

NW: Thank you very much for coming.