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Simon Shields
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Investors

“Some of the fund managers out there start losing out on returns because they get too big,” he says. “The liquidity just isn’t there anymore to take a concentrated position. We’re not looking to grow our assets for the sake of growing our assets.”

Focusing on outcomes

Monash Investors principal Simon Shields ⁰⁴ shares Cheruvu’s appetite for innovation in the Australian equities space, albeit with a somewhat different approach.

Shields, a previous head of Australian equities at both UBS Global Asset Management and Colonial First State, recently launched an absolute return Australian equities fund, underpinned by a belief that “we need more degrees of freedom in generating a steady return for investors than if we were just trying to beat the market.”

Like Cheruvu, Shields acknowledges that there are “a lot of people doing Australian equities now.”

“In fact when I left my last job, there were 130 managers in a survey. I don’t know how many there are now, but when I started in the late 1980s, there were about 12. Now the big conversation is around which of these guys actually add value above the index, and that’s pushed a lot of them towards having a very tight style and a tight tracking area,” Shields says.

The problem with this, he argues, is that the industry now largely comprises managers that will perform well in particular conditions and badly in others. And because of those restrictive styles, he adds, “they’re never going to do too much worse or too much better than the market. They’re limited by their tracking areas and the bet sizes they can take around the index in terms of stocks and sectors.”

Shields concedes he did that himself for 27 years; and this new fund arguably came about because he didn’t want to anymore.

“I wanted to do something different. I wanted an outcomes-based approach. Then the question became, ‘How can you have an absolute return by investing in the Australian market?’ The answer is that you can’t be concerned about trying to beat the index all the time – you start thinking about doing that and you end up in the position I was in before,” he says.

On the other hand, focusing on outcomes lets Shields focus on the primary task of growing investor wealth year-on-year. And a crucial component of this is taking both long and short positions with his fund.

“You’ve got to have the freedom to not invest, too,” he says.

“You’ve got to be able to go short, get exposure to different sectors, use options – all these things that effectively lower your exposure to market volatility.

“What we do every time we go into one of our investments is we put a price target on what we want to achieve, and we only invest if we can

get the payoff. And when we get that payoff, we exit. The investor wants a return target of their own to meet their own goals, so we’re fulfilling that component of their portfolio by always aiming for that targeted payoff.”

New ideas, new sectors

The fund targets 12 to 15% per annum after fees. Because of the need to target stocks that are growing earnings strongly each year, Shields says “we’re generally going after the mid to smaller-caps, because that’s where the growth is coming from. And it also means you’re more diversified than the market in general.”

“If we look at global growth trends, what do you have? Technology is a big one, but it’s not well-represented in the ASX 200.

“The other side of that is healthcare and pharmacological companies, whose growth is driven by ageing populations and the increasing incidence of health problems like diabetes, heart disease and obesity. Technology companies are working with those medical companies to create new devices, products and services.”

Shields is also looking at telecommunications companies, especially those with overseas distribution and mobile specialisation.

“It’s a fast-moving area – and a lot of these companies are developing new applications and technologies that are moving to offshore markets,” he says.

“A lot of characteristics about these kinds of tech and mobile companies aren’t really correlated to what’s going on in the global economy. Greencross, which owns Petbarn, is still rolling out new stores – and they say they still have a long way to go.”

Where the shorts come in is industries and sectors that have been directly impacted by the companies above. Consider SkyTV, a New Zealand-based pay-TV company which Shields says has been significantly affected by the rise of Netflix.

“Or Woolworths,” he continues, “which we previously had shorts in because of how it was disrupted by the rollout of Aldi in Australia. In fact, even the rising healthcare issues I mentioned have had their own impact on our short positions: we’ve had shorts in Coca Cola because rising health awareness has driven down consumer demand for carbonated soft drinks and fruit juices.”

Zeroing in on income

Unlike Cheruvu and Shields’ funds, Plato Investment Management’s Australian Shares Income Fund does attempt to beat the market, but with an income focus.

Plato managing director Don Hamson ⁰⁵ says the fund has a “dual objective,” based on his belief that while investors in the pension phase have a strong need from income, “you don’t want to sacrifice capital in the process.”



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Simon Shields

The Australian Shares Income Fund is designed for two distinct investor groups: retirees and self-managed super funds in the pension phase, and charitable foundations. Both groups, Hamson says, cite income as a priority.

“The beauty of the Australian tax system is that you get a refund of franking credits – but that’s not our primary aim. It’s to get strong total income, not just maximise franking credits. So we’re looking at anomalies around dividends where there is value to be added.”

To find those anomalies, Hamson starts with forecasts based on interim and final dividends, rather than just looking at annual payouts.

“For us, it’s not just a buy-and-hold strategy,” he explains.

“We’re actively trading to get more income than the market. To make sure that’s effective, though, we need to also identify stocks that might cut their dividends – because there’s a big dividend trap where stocks that trade on a good historic yield will often do just that. After all, the easiest way to have a high yield stock is if the price has crashed in the last 12 months.

“Look at Metcash, ANZ and BHP: so many people were surprised when they cut their dividends. But they had extremely high historic yield. When the share prices falls significantly, the market is telling you there’s something wrong with the company. BHP, for instance, cut its dividend because the underlying business was struggling. Commodity prices were going down for some time, the share price was falling in response to those fundamentals, the historic