

Aviva Investors

Global Equity Endurance Fund

Giles Parkinson, Fund Manager

December 2019

December Commentary – How to Kill a Stock

Fund Overview

The Fund seeks to achieve resilient returns over the long term by investing in a high-conviction, low turnover portfolio of ‘cheap durables’, predictable cash generative businesses acquired at attractive cash-based valuations.

Monthly Performance

- The Fund rose by 3.1% in December; the MSCI All-Countries World Index increased by 3.5%
- In 2019 the Fund increased by 33.2%; the MSCI All-Countries World Index rose by 26.6%
- Since inception the cumulative monthly capture ratio of the Fund has been 1.3, with an average upside capture of 99% and downside capture of 74%.

Month in Review

Equities recorded all-time-highs in December.

For a second consecutive month the largest single positive contributor to returns was **British American Tobacco** (+31bps). Our November factsheet discussed how a formal change in regulatory policy from the FDA potentially heralded the ‘end of the beginning’ for the underperformance of tobacco shares. Time will tell.

St James’s Place (+24bps) rose 10% in USD terms in the month as the share price increased, and sterling appreciated. Something of a ‘battleground stock’ where all manner of immaterial, irrelevant and ignorant bearish arguments were being deployed to justify a fallen share price amidst unfavourable media coverage from the ‘Cruises & Cufflinks’ “scandal”, we added to the position back in September. In hindsight, the shares were being caught up in a generic aversion to stocks focused on the UK domestic economy, which was lifted with the Conservative Party winning their biggest parliamentary majority since 1987. We did not predict this outcome, but we did recognise and act when perceived value went on sale.

The biggest detractor was **Jack Henry** (-7bps) for which there is no discernible reason. We substantially reduced the position in October 2018 on valuation grounds and, given the subsequent underperformance of the stock yet ongoing strength from the company, we may rebuild the holding.

Another notable detractor **Unilever** (-3bps) had been sold progressively throughout the year as our conviction in the long-run growth outlook waned amidst a stock price that was hitting all-time highs, something we touched on in our September commentary ‘Turbulence’. The small position that remained was sold immediately following a profit warning in the middle of the month. At around 14%, our exposure to branded manufacturers of fast-moving consumer goods are now down to the lowest level since fund inception, as we see the future for these industries as being much tougher than in previous decades to an extent that is not reflected in valuations. Our selective investments in this area are in just three categories: tobacco (British American Tobacco and Philip Morris, both of whom we regarded as having leading technologies beyond conventional cigarettes), beer and cosmetics (Heineken and L’Oreal, both of whom have a strong track record of market share gains).

Aviva Investors

Global Equity Endurance Fund

Giles Parkinson, Fund Manager

December 2019

Project managers and strategic planning circles have long recognised the distinct danger posed by unknown unknowns – risks that come from situations that are so unexpected they were left unconsidered and hence encountered without a contingency plan. One tool we use to mitigate against this is the pre-mortem, a mental exercise in which we travel forward in time, find that the investment has turned out badly, and conjecture reasons for the flop. Research shows that it is easier to find reasons for why something *has* happened as opposed to developing different scenarios for things that *might* happen. Reframing the problem shifts the mindset to accept that the investment has failed – shock horror – and obliges us to become creative in identifying the weaknesses, poor assumptions and hidden risks that led us there.

We have found numerous benefits from incorporating this approach. The first is in allocating our time, the most scarce resource we possess. When triaging research candidates for deeper study, if it is relatively easy to kill a stock at the current valuation then our attention is better spent elsewhere. This aspect iterates throughout the subsequent layers of the research phase as we are continually on the lookout for excuses to drop the idea and move on. Secondly, freeing up analytical and critical thinking helps to drive better debate, as we are obliged to ask wider questions about what really drives value. The third contribution is using the pre-mortem as a risk management tool. The longer the list of risk factors, the more severe and likely the pre-mortem scenarios, the smaller the position size will be (if the stock is owned at all). Fourth, we apply our pre-mortem learnings in executing ideas. Thanks to the exercise, we have a better understanding of what constitutes a thesis breaking event, can distinguish between situations that are an impairment of fundamental value as opposed to those that are merely having an impact on investor sentiment, and are more attune to the nascent development of adverse risks as they start to build. Should a stock fall, we are better prepared for the real-time decisions around ‘when to add’ versus ‘when to sell’. Finally, we incorporate the pre-mortem into investment post-mortems to improve our thought process. Hindsight bias is the revisionist tendency to think that an outcome was more predictable than it actually was before the events took place. But, really, the needed information wasn’t available, the pre-mortem shows this, and the exposed deficiency feeds into refining our consideration of future investments. *There are more things in heaven and earth, Horatio, than are dreamt of in your philosophy.*

Looking Ahead

The Global Equity Endurance Fund is a portfolio of what we believe to be above-average businesses trading at a cheaper free cash flow yield than the market and a discount to their intrinsic value. A combined focus on the durability of a company and the price we pay for the stock enables us to exploit opportunities and ought to make the approach adaptive to changing market conditions. As a long-term strategy with low turnover we fully expect and recommend that unitholders judge our performance over a period of five years or more.

Source: December 2019

Aviva Investors

Global Equity Endurance Fund

Giles Parkinson, Fund Manager

December 2019

Key Risks

The value of an investment and any income from it can go down as well as up and can fluctuate in response to changes in currency and exchange rates. Investors may not get back the original amount invested.

Certain assets held in the Fund could be hard to value or to sell at a desired time or at a price considered to be fair (especially in large quantities), and as a result their prices could be very volatile.

The Fund invests in emerging markets, these markets may be volatile and carry higher risk than developed markets.

The Fund invests in a small portfolio of securities. Losses from a single investment may be more detrimental to the overall performance than if a larger number of investments were made.

The Fund uses derivatives; these can be complex and highly volatile. This means in unusual market conditions the Fund may suffer significant losses. In unusual market conditions, the Fund may have difficulty selling its investments, which may cause it to suffer losses, defer redemption payments or suspend dealing in shares.

Investors' attention is drawn to the specific risk factors set out in the fund's share class key investor information document ("KIID") and Prospectus. Investors should read these in full before investing.

Important Information

Unless stated otherwise any opinions expressed are those of Aviva Investors. They should not be viewed as indicating any guarantee of return from an investment managed by Aviva Investors nor as personalised advice of any nature. This document should not be taken as a recommendation or offer by anyone in any jurisdiction in which such an offer is not authorised or to any person to whom it is unlawful to make such an offer or solicitation. The legal documentation and the subscription documents should be read before an investment is made. Portfolio holdings are subject to change at any time without notice and information about specific securities should not be construed as a recommendation to buy or sell any securities.

The Prospectus and Key Investor Information Document (KIID), are available, together with the Report and Accounts of the SICAV, free of charge from Aviva Investors Luxembourg, 2 rue du Fort Bourbon 1st Floor.L-1249 Luxembourg, Grand Duchy of Luxembourg R.C.S. Luxembourg B25708, Aviva Investors, St Helen's, 1 Undershaft, London EC3P 3DQ or relevant office below. The Prospectus is available in English and German. Where a sub fund of the SICAV is registered for public distribution in a jurisdiction, a KIID in the official language of that jurisdiction will be available. The Prospectus, the KIIDs, the Articles of Incorporation as well as the Annual and Semi-Annual Reports are available free of charge in Austria from Raiffeisen Bank International AG, Am Stadtpark 9, 1030 Vienna the paying agent and in Switzerland, from the representative and paying agent BNP Paribas Securities Services, Paris, succursale de Zurich, Selnaustrasse 16, 8002 Zurich, Switzerland. In Germany, The Paying and Information Agent in the Federal Republic of Germany is Marcard, Stein & Co AG Ballindamm 36 20095 Hamburg, Germany. In Spain, copies of the Prospectus and KIID together with the Report and Accounts are available free of charge from the offices of distributors in Spain. The UCITS is authorised by the CNMV with registration number 7. You can also download copies at www.avivainvestors.com. Aviva Investors Global Services Limited, registered in England No. 1151805. Registered Office: St Helen's, 1 Undershaft, London EC3P 3DQ. Authorised and regulated in the UK by the Financial Conduct Authority and a member of the Investment Association.

Issued by Aviva Investors Global Services Limited. Registered in England No. 1151805. Registered Office: St Helens, 1 Undershaft, London EC3P 3DQ. Authorised and regulated by the Financial Conduct Authority. Firm Reference No. 119178.