

Launch of Prudential Global Basics

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1. Some investors might find it hard to understand the focus of the fund (can invest in almost anything). Is there a danger the fund is trying to cover too much?

Holdings in the Fund must meet the manager's investment criteria. Firstly, it must be a "basic" company which we would define as being a "building block" of the world economy, and often described by the manager as one that produces "anything you can eat, drink, wear, drive, smoke...". Secondly, it must be a well-established, global, profitable, cash generative business with tangible attractive assets, financial strength (as evidenced by a strong balance sheet, good revenue growth, and high quality, sustainable cash flow) and a strong brand or market position.

Given these criteria, the Fund is extremely unlikely to hold stocks from the technology, financials, media, telecoms and pharmaceuticals sectors; and the Fund's investment universe is around 60% of the FTSE World Index. The manager takes very high conviction positions in the companies that he likes. Stock picks will also generally be part of a bigger theme – such as companies benefiting from demand for raw materials or consumer goods in Asia. Hence, there is also a likelihood that the Fund exhibits strong sector or common factor biases at any one time.

The PRU Global Basics Fund is run as a relatively concentrated portfolio (between 40 to 80 stocks) of equity positions designed to achieve consistently strong returns. It is a global equity fund and country positions are a result of bottom-up stock picking.

2. Resources are a hot topic now and seem to have been a big driver of performance of the fund. Couldn't this backfire if that sector takes a hit?

Given the exceptionally strong returns produced by resources stocks over the last two years, Graham admits that he ought to be feeling more apprehension when looking forward. However, his meetings with company management are regularly reassuring him that there is still much more to come from commodities.

Recently, the fund manager and his team met the management of Rio Tinto. The CFO of Rio Tinto admitted that he had never seen anything like the levels of demand that they are currently experiencing. Critically, he saw no evidence of a slow down from China and qualified this with reference to shipping rates (ie. the cost of shipping raw materials from A to B). Despite the many new ships that continue to come on stream, there is insufficient supply to satisfy demand and shipping rates have started to creep up as a result. The same applies to the railways – they are at full capacity. Just about the same time, there has been similar comment from Chip Goodyear, the chief Executive of BHP Billiton.

M&A activity lends further support to commodities – already this year, the Fund has benefited from bids for WMC Resources (from BHP Billiton) and Falconbridge (from Noranda Inc), and the prospect of further activity continues to underpin prices. And finally, on the demand side, there is a wild card in the shape of Japan and Europe, which together account for around 40% of global demand. Both economies are showing signs of recovery after long periods of underperformance.

3. Under what circumstances would natural resources and energy sector stocks suffer big falls?

At the moment, global growth is highly dependent on growth in both China and India, even though US and (to a lesser extent) Japanese growth rates are improving. The demand for both basic materials and commodities would likely be impacted, should either China or India falter. It is their exploding demand for oil, for example, that lies behind the sustained upward trend in oil prices. To illustrate their impact further, commodity prices plunge last year when China introduced measures to slow its overheating economy. Investors, fearing that China's government would stem growth as they did in the early 1990s, drove commodity prices sharply lower. It was only when it became evident that China's growth was not slowing, that commodity prices bounced back.

Over the past few years incremental demand growth in China has been equivalent to incremental supply growth in Russia. Russia's production problems today are highlighting a more widespread problem across the non-OPEC region to meet rapidly expanding oil demand, particularly across Asia. Under-investment in productive capacity, limits to refining capacity and the potential for further extreme weather events are sustaining a bullish price outlook for energy prices into 2006. The dangers of a US recession in the near term are low. However, we expect the vigour of the US expansion to begin to slow during 2007 and this offers the best chance for oil prices to fall from current record highs. We see little chance of oil prices returning to the levels of the 1990s and envisage oil prices at more than twice the average level of the 1990s over the medium term.

Base metals prices should remain well above long-run averages. We are in the middle of a huge bull run in commodities, and as long as the global economy does not nosedive, 2006 is shaping up to be another strong year for pricing.

4. Is the fund too big now to outperform?

The M&G Global Basics Fund is a S\$2.403 billion fund (as at 31 July 2005) and we expect this figure to grow. Although a large fund compared with many, Graham does not believe that he is restricted by the size of the Fund in any way. The portfolio is extremely liquid, with 80% of the portfolio invested in stocks that could be sold immediately, 10% in stocks which might take a couple of days to fully liquidate and another 10% which might take up to a week. By contrast, other high profile resources funds have tended to invest heavily in less liquid companies. This is fine when the market is going up as it has been, but can become problematic when it is not. Graham maintains that it is much easier to sell 15% of Rio Tinto than it is to sell even 1% of an AIM listed mining stock.

5. Isn't the fund too dependent on one person - Graham French - which could be a risk?

The fund manager's investment process is supported by a strong and highly qualified investment team with a diverse skill-set. This include senior analysts, analysts and other M&G fund managers in the UK, European and global teams, where a collegial atmosphere is reflected in a number of common holdings across M&G Funds. Graham is also supported by the presence of an in-house analyst team, in particular by analysts dedicated to covering the global mining and global basic industries sectors (please see their CVs attached).

The fund manager may be accompanied to company meetings by the analysts and other fund managers, so that all parties are able to make judgments based on the same information. Given the inherent subjective nature of the process, any resultant

The fund manager is also fully supported by the work of the Portfolio Strategy and Risk Team, Equities Investment Committee and Heads of Equities and Portfolio Risk. To meet investors' objectives, the Fund needs to meet stretching performance targets which cannot be achieved without sufficient risks of the right kind being taken. The Portfolio Strategy and Risk team's key task is to ensure that Graham is allocating his risk budget (i.e. total risk that the fund can take) in a manner that makes maximum use of his stock picking skills. The Team analyses the various dimensions of portfolio risk including common factor risk and correlation; allocation of the risk budget; exposure to unintended factors; and style analysis. These risks could be strategic, arising as a result of the Fund's own distinctive mandate, or tactical, arising as a result of the fund manager's particular investment view at that time. Using a variety of risk models and techniques, the analysis aims to capture intended investment risks, and more importantly, the unintended risks that can arise as a result of a stock specific investment approach.

6. Can you hold a lot of cash (or do other defensive maneuvers) if things looks bad?

During the year 2005, to date, the average liquidity held in the Fund has been 4.0%. The cash position is not actively managed. As replied in answer 4, the Fund avoids small illiquid stocks and so flexibility of movement is not an issue for the Fund's investment strategy. As part of our risk management procedure, we regularly monitor the following set of portfolio parameters:

- The Fund invests in between 40 to 80 stocks (ensures sufficient diversification)
- No less than 30% of the portfolio will be invested in the 30 largest stocks in the benchmark index
- Holdings of stocks with a market cap of less than US\$1 billion will be limited to 30% of the portfolio (to avoid being exposed to the small, speculative end of the market)
- Individual holdings will be limited to 10% of the Fund
- Regional weightings will be limited to +/-20% of the benchmark index (ensures we are aware of country positions that have arisen as a result of stock selection decisions)
- The portfolio will be fully invested with no more than 10% in cash
- The Fund does not use derivatives
- The Fund does not hedge.

7. What stock picking process do you have to distinguish this fund from others?

Stock selection for the M&G Global Basics Fund is undertaken on a pure bottom-up basis. Adhering to the Investment Objective of the Fund, the fund manager has a long-term investment philosophy that avoids reacting to short-term movements and noise. He has a value bias, seeking out well-established, fundamentally undervalued companies that are capable of generating consistently strong margins throughout economic cycles. The Fund is not managed relative to a benchmark market index and the manager pays no particular attention to a stock's individual index weighting. The manager will take significant positions in his high conviction views.

When selecting holdings, emphasis is placed upon the following characteristics:

- Attractive, tangible assets
- Strong competitive edge and sustainable market share (leadership in niche market)
- A proven business model
- Financial strength (strong b/s, good revenue growth, cash generative)
- Low valuations

In particular, the valuation analyses examine several financial metrics and ratios including:

- Discounted cash flow
- Cash Flow Return on Investment (HOLT)
- Return on Invested Capital relative to the Weighted Average Cost of Capital
- Price / Book value
- Earnings Yield

The quality of the business environment and marketplace in which companies operate are also important consideration for the stock selection process. Critical to the stock selection process is also the manager's qualitative assessment of management ability and experience for creating shareholder value across the entire portfolio. In addition to his assessment of management ability, experience and proven success, he also regards strict levels of corporate governance as essential.

8. Stock markets in general look a little overvalued, so should investors look elsewhere for 6-12 months?

We believe there is still value to be found on a selective basis. Expert stock picking by experienced managers is important. Graham French adopts a pure bottom-up stock picking approach for the Fund, with a long-term investment philosophy that avoids short-term fluctuations and noises. The stocks which he picks are well established, fundamentally undervalued companies that are capable of generating consistently strong margins throughout economic cycles. Critical to the stock selection process is the fund manager's assessment of management ability, levels of corporate governance and experience for creating shareholder value.

9. When is the end of the launch period?

The launch period will end on 14th Oct, 2005. 17th Oct will be the first pricing date.