



Evenlode Investment View

July 2018 – Rewarding Strategies for Long-Term Shareholders

July has, as usual, been a busy month for fundamental news flow. Interim results season is in full swing and more than 80% of the Evenlode Income portfolio has now released updates since the end of June.

The global economy has been quite strong so far this year creating a reasonably positive backdrop. Multinationals are seeing better growth return in many emerging markets, whilst industrial production markets and other more economically sensitive sectors are enjoying notably more buoyant conditions than those that prevailed a couple of years ago. This has all helped stock markets in recent weeks. As I write, the FTSE All-Share has risen +2.5% since the start of 2018 whilst Evenlode Income has returned +7.3%*.

However, operating conditions remain varied and volatile by region and sector, and companies in the portfolio have been impacted (both positively and negatively) by many factors including Brexit uncertainty in the UK, US trade tariffs, the FIFA World Cup, a hot European summer, natural disasters, the Brazilian trucker's strike, rampant inflation in Argentina and Venezuela, Turkish elections, rising commodity prices and tightening US monetary policy.

In the context of this 'positive but patchy' world, we have been reassured by the progress the aggregate portfolio is making, and in next month's investment view I will give an update on the portfolio across the key sectors to which it is exposed. This month I'd like to briefly discuss recent results from three companies in the portfolio, each of which illustrates a strategic approach that we think is well aligned to the priorities of long-term shareholders:

1) Relx: Staying Close To The Customer

Some might find business-to-business media company Relx a little boring, but recent interim results were a reminder of the attractiveness of this stable, diversified, highly cash generative business (currently the third largest holding in the fund). Approximately 75% of revenues now come from digital products (with most of the remainder from its face to-face exhibitions business). We have been particularly impressed with the focus that Relx has had on the organic development of its digital analytics tools over the last few years. These products help academics, doctors, lawyers and businesses make better decisions, often saving costs and improving the quality of their own services and products.

Relx's strategy is to pursue a simple formula - ask yourself how you can make your customer's life easier, and then invest continuously in improving your product offering to achieve this goal. If your customer is able to make better decisions then their own efficiency and product quality should improve. They will therefore want (and be able) to use more of your services. This should lead to growth, more attractive economics, a more embedded relationship with your customer and more cash to plough back into improving your product range some more.

I find this strategy very compelling. It creates a virtuous circle that ensures the company's success is well aligned with its customer's success, and should also ensure that the company's 'economic moat' and returns on capital remain healthy over time. As CEO Erik Engstrom pointed out at recent

results, this customer-centric approach is much more about growing the overall market than a zero-sum attempt to simply 'win' market share from competitors:

We don't focus so much on market share as on increased value to our customers, because we believe that if we can add more value to our customers – demonstrably higher value in a way that they can see, measure and quantify – our customers will want more of it. And if that, over time, means that we are gaining share in a defined market, then that's OK, but it's not our primary objective.

Relx grew organic sales +4% and earnings +7% during the first half of the year, and announced a dividend increase of +6%.

2) Jardine Lloyd Thompson: Taking a Long-Term View

Jardine Lloyd Thompson (JLT) has a strong position in the global insurance broking market, specialising in sectors such as aviation, healthcare, infrastructure and construction. It is a capital-light people-business, with strong customer relationships and a reputation for client advocacy. The company takes no insurance risk and profits are consistently converted into cash flow. Back in 2015 I discussed JLT's decision to make a significant organic investment (c.\$100m over about four years) in building out a much greater presence in the US market, a region to which it had historically been under-exposed and a move with the potential to significantly strengthen its global competitive position.

Despite this large investment and some non-trivial headwinds in its underlying markets, JLT has grown its earnings and dividends over subsequent years and remained highly cash generative. Now, market conditions have stabilised and the US business is set to contribute meaningfully to profitability from 2019. It's been an exercise in patience for both management and shareholders, but the long-term strategic benefits, returns-on-capital and cash generation that this growth project should generate have been worth the wait.

JLT increased its dividend by +4% along with its interims and in my view prospects for steady dividend growth are very good.

3) Moneysupermarket: Investing in Technology

Moneysupermarket, a new position for the fund last year, is the UK's market-leading price comparison website with strong positions in its key verticals of insurance, utilities and money. It performs a useful service to the UK public: the business saved an estimated £1.1bn for its 13 million active users over the first half of 2018. Whilst its strong consumer brand and embedded relationships with suppliers are important, its technology and data analytics capability also form a key part of its competitive position.

I have been impressed with Moneysupermarket's significant investment in technology over the last few years. As with JLT it has been a project that, though burdening financial results in the shorter-term, has clear benefits for the company's competitive position and customer-offering over the longer-term. Up until this year, this investment has mainly been 'behind the scenes' to produce a more consistent, modern, flexible IT platform. But management are now in a position to use this technology to help enhance the user experience of both its website and its mobile app. In recent months, for instance, using an iterative 'test and learn' approach, management have made some

simple changes to Moneysupermarket's energy price comparison search process that led to a more than +50% increase in both customer conversion rates and revenues in that segment. A similar approach will now be applied to other areas of the business to help drive growth.

Moneysupermarket raised its dividend by +4% with its interim results. The company continues to enjoy a net cash balance sheet and there are good prospects for surplus cash returns to shareholders, over and above the ordinary dividend.

Leftover Cash

More generally, it has been reassuring during the latest results season to see many portfolio holdings invest meaningfully in their businesses, grow their dividends at a steady rate, and still end up with leftover cash at the end of the period. I apologise for repetition but investing in companies that regularly give you cash (rather than regularly ask you for cash) tends to be a very rewarding experience for the patient investor. When all is said and done, it is a company's long-term free cash flow stream that represents the intrinsic value of any share. Therefore, the more free cash flow a company generates as the years go by, the more valuable each share should prove to be over time. And sometimes, as the above examples hopefully illustrate, it can make sense for a business to sacrifice a little cash today in return for a lot more cash in the future: a principle that lies at the heart of long-term compounding.

I look forward to updating you on the evolution of the portfolio over the coming months. In the meantime, I hope you have a very enjoyable August.

Hugh Yarrow
Fund Manager
30th July 2018

**Source: Financial Express (Total return: 31st December 2017 to 30th July 2018)*

Please note, these views represent the opinions of Hugh Yarrow as at 30th July 2018 and do not constitute investment advice.

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For the most up to date information, please refer to the TB Evenlode Income Fund and B Acc GBP share class-specific Key Investor Information Documents, the Supplementary Information Document, the Annual or Interim Reports and the Prospectus, which are available on the Literature tab.

Past performance is not a guide to future returns. The value of investments and any income will fluctuate (this may partly be the result of exchange rate fluctuations) and investors may not get back the full amount invested. Performance figures are based on the B Acc GBP share class. Performance figures for all share classes can be found in the relevant Key Investor Information Document. Fund performance figures are shown in Pound Sterling, inclusive of reinvested income and net of the ongoing charges and portfolio transaction costs to 30 July 2018 unless otherwise stated. The figures do not reflect the entry charge paid by individual investors. The standardised past performance information is updated on a quarterly basis.

Source: Evenlode Investment Management Limited.