Future Generation
INVESTMENT & SOCIAL RETURNS

2fold: Take Stock podcast

John Coombe
JANA Investment Advisors

CAROLINE GURNEY, CEO, FUTURE GENERATION: I'd like to begin by acknowledging the Traditional Owners of the land on which we meet today, and recognise their continuing connection to lands, waters and communities. We pay our respects to Elders past and present.

Hello and welcome to Take Stock, a podcast by Future Generation. I'm Caroline Gurney, Chief Executive of Future Generation and today I'm joined by John Coombe. John is the Executive Director of JANA Investment Advisors, where he advises some of Australia's biggest superannuation and investment funds, managing hundreds of billions of dollars in capital.

He also serves, thankfully, on the investment committees for Future Generation Australia (ASX: FGX), Future Generation Global (ASX: FGG) and more recently, Future Generation Women. We are incredibly fortunate to have John's expertise, which I should obviously mention to you, he generously provides us pro bono support. John, welcome. Thank you so much for joining us today.

JOHN COOMBE: Thank you, Caroline. It's wonderful to see you again.

CAROLINE GURNEY: Today, John is actually going to provide us with an update on Future Generation Global's portfolio and give us his perspective on the broader global markets. But before we dive into that, I just want to give our listeners some context about the investment objective of Future Generation Global. John, Future Generation Global, it's a funds of funds model. What are you aiming to achieve with this strategy?

JOHN COOMBE: We're aiming to outperform the index over the medium term, Caroline. So in the case of FGG, it's the Capital International World Index, and that's all the developed market world index. So we're trying to outperform that MSCI, and after we take away the 1% feed too.

CAROLINE GURNEY: So that 1% is the 1% that we give total net assets to not-for-profits across Australia, supporting youth mental health prevention. So, the model is incredibly unique and something that, when it was set up, has now provided with all of the Future Generation vehicles, more than $90 million to not-for-profits, and now we manage $1.4 billion.

So John, let's just talk about Future Generation Global. How do you go about constructing a portfolio that really ensures that right mix of managers to meet the goal that you just discussed?

JOHN COOMBE: We use a fair bit of technology, Caroline. Fortunately, one of the other firms provides pro bono access to their systems so that we can put managers on and see what it does to our portfolio, whether we have too much risk in certain areas of the market, whether we have too much style in value or growth. And so, we basically use that to build out a portfolio that we think doesn't have excessive risk in any one particular area, but will outperform the market over the medium term.

CAROLINE GURNEY: So that's Lonsec that provides that pro bono data for us. But obviously, the Investment Committee members have a big input into new fund managers. So, what is the process you use to determine the optimal mix of managers and what other kind of information do you rely on in terms of the Investment Committee's expertise?

JOHN COOMBE: So perhaps if we give an example of the latest changes and sort of how that came about, that might be a bit of insight for investors, Caroline. One of the committee members, we were talking about our small cap allocation, and they had just done a research piece which basically was in favour of having small caps within a broader portfolio of stocks to beat the index in a global portfolio. So, we discussed it at length, and then we had a look at our two existing small cap managers who we had in the portfolio. Both of those managers had sort of been on our radar watch for a while because their performance hadn't been fantastic, which is pretty common for small cap managers. But also, when we looked and dived deeper into the managers, they were very similar in style. So, we had basically two value managers sitting in our portfolio in the small cap area.

And whilst over the longer term, we could expect value to outperform and small caps to outperform, it was actually hurting our short and medium term performance. And fortunately, because our fellow committee member had done some work at their organisation, they nominated a number of different companies in the small cap area for us to interview.

So, the way the process works is once we've identified firms who we think we want to talk to, we get a very extensive reply from them in terms of all the questions that we ask in our RFP, and it seeks to give us a broader understanding of the organisation before we do the interviews. And then as a committee, we had interviews with a number of different managers. And then we all came back together at another committee meeting and basically decided that we would hire two of the new small cap managers who had a different style to our existing managers, but that we wouldn't increase our allocation to small caps from where we were, but we would actually take some money off the existing and give it to the new managers. So that all took two months or three months to complete, but that's the sort of process that we go through. Idea generation, getting information, interviewing potential managers, then deciding about how we want to do it. And while we meet the broad criteria that we set ourselves as a committee.

CAROLINE GURNEY: As you said, John, you've mentioned two of the new managers, but we've also added another manager. So, three new managers into the portfolio. GCQ Funds Management, Langdon Equity Partners, and Fairlight Asset Management. Would you mind telling us a little bit about each of these managers and what they do bring to the portfolio?

JOHN COOMBE: Langdon and Fairlight are the new two small cap managers. So interestingly, Langdon is a Canadian firm but has its roots here in Australia in that it's partly owned by Pinnacle. It's a firm of people that all worked at Cambridge Global Asset Management together, or the principals worked at Cambridge together. They run both a global and a small cap portfolio and have a growth bent to it.

There is a really interesting manager on Fairlight. One of the committee members knows them particularly well, but we needed to do proper DD on them. So, a number of us interviewed them, and they are a really interesting firm based here in Sydney and doing a lot of good work.

CAROLINE GURNEY: John, that was really interesting. And GCQ funds management, what was the catalyst there for bringing them in?

JOHN COOMBE: We actually knew the portfolio manager and had for quite some time. He used to be the deputy at a fund management firm that we had a couple of years ago, who unfortunately we had to terminate because of loss of staff, etc. But he set the firm up four years ago - large cap concentrated growth, very tight number of stocks in the portfolio.

We've been following him for a while. His performance has been very good, and we decided that the time was right to have him back in the portfolio. So, we're very excited about that, given that we had a history with him before he went out and set up his own.

So again, it's sort of using our network. Doug had kept in contact with us and was very keen to be involved again in Future Generation. So sometimes some managers go out of their way, Caroline, as you know, to reach out to us.

It's not just us reaching out to managers. And here's a classic example of a person who willingly took a step, set up his own, and after four years, we're more than comfortable in putting some money with him.

CAROLINE GURNEY: Let's turn now to global markets. You’ve got volatility, it’s just incredible, I'm kind of addicted to reading what's happening overseas. A lot of uncertainty. We've got geopolitical tension, you've got tariffs, you've got Trump in terms of his policies, is he actually going to do what he said he's going to do, and he seems to be. So how do you actually manage these risks in portfolio construction?

How are you going about it on a regular basis?

JOHN COOMBE: Well, fortunately, because we try to make a portfolio that should be robust in all market circumstances, and we're trying not to have big overweights or big, large positions based on economics or GA politics. You hope the portfolio is robust enough and resilient enough to withstand even a Donald Trump and his constant desire to be in the press with new announcements and new tariffs, et cetera.

But look, it is worrying in a longer-term sense because it will put pressure on global equity markets. And we've seen in the last week or so quite a downshift in the US market, mainly caused by the tariffs. But some of the studies we've looked at - getting rid of the workforce is one of the biggest. If he does what he says he's going to do with illegal immigrants, that's a big blow to the US economy if he takes four million people out of the economy. It's a lot of people. And so we don't know. So, you just have to build a portfolio that's going to be resilient. And that's what we try to do.

Be as resilient as possible in the portfolio, in its construction. That's why we have the quants in there. Caroline, as you know, we introduced the quants a couple of years ago. To make certain we had broad coverage, that we didn't have big sectoral overweights or underweights, that we didn't have big country positions, because you can get very hurt in sell-offs if geopolitics takes over, which we're starting to see. And we just don't want that in the portfolio.

CAROLINE GURNEY: And it is good to see in terms of the quant, as you mentioned. So we have Vinva and Plato, and they have positively contributed to that portfolio.

But one thing I enjoy talking about is really that sort of market rotation away from the Magnificent Seven. You've expressed concerns quite widely about market concentration in the past. At Future Generation Global, we've got that bias towards small and mid-cap stocks. How do you see the portfolio performing in this kind of environment that we're in now, and for the next six months to the year? Because we're a long-term investment.

JOHN COOMBE: I pray that we do see a market rotation. It'll be good for the market, to be honest. A very concentrated market, as we know in Australia, can be quite negative on people's perceptions. And also, what we've seen globally is it's become very difficult for some of the global fund managers who just aren't used to having this sort of market concentration.

I'll give you an example. I was talking to a manager the other day, and they usually run an equally weighted portfolio across their 30 stocks. So that's about 3% in each stock. And I said to him, of the Magnificent Seven, who do you like? And he said, we love Microsoft. I said, so you have 3% in Microsoft.

So, you're underweight Microsoft, even though you like it. So, this is really causing issues for fund managers, this real concentration in the market, because we're used to it in Australia with the banks, right? The banks are 25 or so percent of the index, etc. And so, fund managers have to have some bank stocks. They have to think about the banks. Globally, they've never had to worry about this before. Now they're worrying about, you know, if I like NVIDIA, I have to have something like 90% of my portfolio or more in NVIDIA to even have an active weight.

It's so unusual for them to think like that, because most global portfolios have an active share of about 80%. Now, what does active share mean? Active share says, if I add up all of my stocks in the portfolio and take away the index weight, what am I left with? And so normally it's about 80% of the portfolio is not in any index stocks. And so suddenly, when you've got seven stocks that are 20 something percent of the index, suddenly you have to think about it, right?

And so, it's been very difficult for global managers in some respects, thinking about index concentration. I think if we have a rotation away back to the broader stock market, that'll be good. It'll also be good for new issues, etc, etc. And we usually do pretty well in the new issue market.

CAROLINE GURNEY: Is there anything else that we haven't mentioned that you wanted to say about the portfolio as your final answer?

JOHN COOMBE: Look, I do think it looks really attractive at the moment when we looked across and we put in the new couple of small cap managers and, it looks like a very interesting portfolio at the moment. There's a couple of managers that we have a really high opinion of who have struggled in the last six months. So we're hoping that this rotation in market really helps them and we see some really strong outperformance from some of those managers who've sort of lagged in the last six months.

I'm excited about the portfolio. And I think it looks good value, and hopefully that comes out into stronger performance. As one market commentator said the other day, valuation doesn't matter until it does matter. And suddenly valuation has started to matter. So maybe our portfolio will behave as we would hope it would.

CAROLINE GURNEY: John, thank you so much for sharing your insights with us today. It is really reassuring that you and obviously the Future Generation Global Investment Committee take this sort of strategic approach to making sure that we do navigate the global markets.

And thank you to everyone who's listening. We hope you've gained some valuable perspectives on how global markets are evolving and how Future Generation Global is positioning itself to stay ahead of the curve.

If you'd like to learn more about Future Generation, be sure to go to our website at www.futuregeninvest.com.au. Thank you. Until next time, take care and keep taking stock.

We hope you enjoyed today's episode. Please join the Future Generation family, Australia's first listed investment company to provide investment and social returns. We are proud to have given more than $75 million to Australian not-for-profit organisations. You can be part of this and gain investment returns while contributing to improving the lives of young Australians. For more information, please visit our website, www.futuregeninvest.com.au.

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