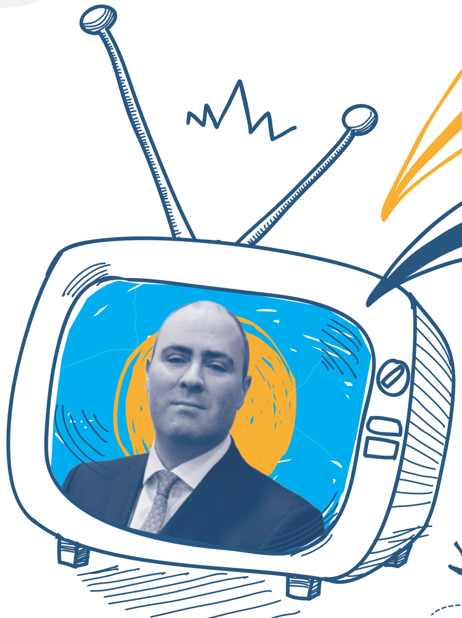
150 years of the Foreign & Colonial Investment Trust

Talking Investment Trusts, markets and tennis with Richard Romer-Lee, Square Mile

TALKING WITH

Paul Niven



Paul Niven, Fund Manager

HOW DID YOU GET INTO THE INDUSTRY?

My mum said I had an interest in money from a young age – I was entrepreneurial, wanting to make my own money by doing tasks for neighbours. I had a long-term interest in finance, but I was not sure exactly what I wanted to do.

I underwent a sort of psychometric test at school to give guidance on what to study at university – my profile threw up investment analyst as number 1 – although I knew nothing about it. I therefore took a degree in Accounting and Economics, following which I was offered jobs in accounting but not in investment analysis, which is what I really wanted. So I stayed at university to defer the decision. My MPhil thesis was called "Paramorphic Model of Investment Analysts' Cognitive Processes in Determination of Earnings Quality" – or rather heuristics in how analysts model. I remember it was about the same time as Terry Smith wrote 'Accounting for Growth'. Companies were using accounting practices to manipulate earnings – it's still relevant today.

I was offered a job by Royal Insurance Asset Management as a graduate trainee in investment analysis of the Food Producers sector on the UK desk. I soon realised this wasn't what I really wanted to do – but an opportunity arose on the Asian desk, which sounded much more exotic and interesting. It combined stocks, sectors, countries, politics, macro-economics and a proper challenge with so many moving parts. It was a great opportunity to design and implement a process to bring all the areas together. This, and being good at taking exams, led to my being asked to work in the asset allocation team and I haven't looked back.

WHAT MAKES A GOOD FUND MANAGER?

An analytical mind and the ability to understand and filter a wide set of data – especially in multi – asset investing. A willingness and ability to take risk positions – in other words to be uncomfortable. An element of arrogance, or rather confidence – trying to beat markets and peers and the belief in your ability to beat the herd – whilst being humble enough to recognise you will only get a certain proportion of your decisions right. And to be able to recognise and accept when you are wrong.

...AND A GOOD INVESTMENT TRUST MANAGER?

It's not fundamentally different from running open-ended funds, but working with boards is. To illustrate with Foreign & Colonial, I have to work strategically with the board on long-term strategy beyond the micro, such as investing in listed or unlisted securities, gearing, growing the dividend and therefore balancing both capital and income requirements. The trust has paid a dividend every year since 1868 and grown the dividend every year since 1970.

WHAT CHALLENGES DOES THE INVESTMENT TRUST SECTOR FACE?

Investments Trusts are a fantastic product for investors – their ability to borrow to invest, the long-term approach, particularly for buying illiquid investments, and the benefits of an independent board working on behalf of shareholders. They are a great one-stop shop. There is a strong proof statement in their long-term performance. However the challenge is disintermediation – we are competing with wealth managers, financial advisers and platforms and the consolidation in the industry. We are trying to provide diversified exposure through a range of concentrated and focussed portfolios within the trust. Returns are additive – risk is not.

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HOW IMPORTANT IS FUND MANAGER TENURE?

There have been only 11 managers of the trust in 150 years – I am the third since 1969 – and my predecessor Jeremy Tigue ran it for 17 years. The trust doesn't set out with a target but it is important to have a long term perspective. But one can't be complacent – the board is demanding and challenging. It is a tremendous privilege to be the manager. The heritage is great, but more importantly it's a great product and investment trust due to its size and vast number of shareholders.

WHAT HAS BEEN THE SECRET OF THE TRUST'S LONGEVITY?

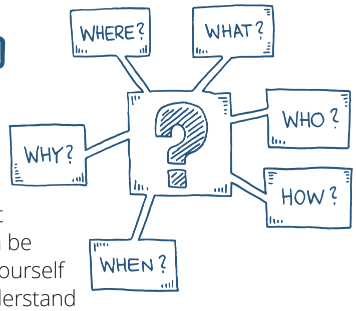
The trust has managed to change with the times. Its original purpose was to provide wholly overseas, diversified access to other investments consumers could not easily access themselves. It started out investing in 18 emerging market bonds. Equities were added in 1925: private equity in 1942 – when the trust bought Flemings Bank, which was sold many years later for almost £200m; and in the mid 1960s it was invested over 95% in equities, which was a big call at the time. In fact it was the biggest decision in its 150 year history and one of the main reasons it's still around today. That and removing its UK bias in 2013 and going global.

WHAT EXCITES YOU AND WORRIES YOU ABOUT MARKETS AT THE MOMENT?

Many strategies look for strong, sustainable advantages in business models – a competitive advantage – we are no different in that respect. We have seen rising concentration and therefore less competition in many sectors. For example, there are fewer banks, fewer airlines and network effects in technology. This has created a fantastic period for owners of capital. The gap between winners and losers is widening. This is likely to be exacerbated in the next downturn – it's not right to assume a normalisation of profits. This excites me.

The flip side, and this worries me, is that labour is losing out and the pricing power of labour has diminished. There is less competition for services, low productivity and a disenfranchised majority. This is a concern not just politically but economically too. Thus the great news for owners of capital comes with the danger of a social and regulatory backlash and how this may manifest itself – what are the consequences of the unwinding of balance sheets and liquidity, when the cost of borrowing goes up? Keeping an eye on inflation in the labour market is key.

WHAT ADVICE WOULD YOU GIVE TO SOMEONE STARTING OUT TODAY?

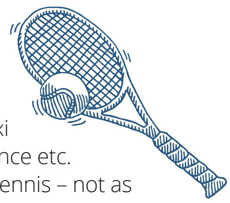


In the early days, ask as many questions as you can and get as much exposure to as many different things as you can. Otherwise life can be very confusing. Only by immersing yourself in a wide range of areas will you understand the important influences on stocks and markets. Some people never get that breadth – it takes a few years but that ability to filter out the noise comes with experience.

WHAT'S THE BEST LESSON YOU HAVE LEARNT?

Events don't always pan out as you expect. I cut my teeth in the Asian markets in the late 1990s – and experienced the Asian financial crisis, Russian default, LTCM, the tech bubble – it was a baptism of fire. I learned first–hand about what Credit Lyonnais called the butterfly effect – that small seemingly unconnected events can lead to big effects. Ignore bigger picture influences at your peril.

HOW DO YOU RELAX?



I have 2 daughters for whom I act as a local taxi service and by watching their sports, ballet, dance etc. It's very rewarding but time consuming. I play tennis – not as well as I used to or would have liked to! I enjoy going on holidays – for many years to Florida for the theme parks. For our honeymoon we splashed out on a once in a lifetime trip to the Maldives. Unfortunately so far it has remained once in a lifetime, but perhaps one day... I can't help noticing, as a Scotsman, the price inflation of holidays – it's unbelievable!