Hosking Partners®

An introduction to Hosking Partners

HISTORY

Hosking Partners' origins date back to November 2013 when Jeremy Hosking launched the global equity strategy. Previously, Jeremy was Head of Global Equity at Marathon Asset Management, a firm he co-founded in 1986. When Jeremy left in 2012, colleagues James Seddon, Jules Mort and Luke Bridgeman also left their roles at Marathon and alongside Django Davidson formed the investment team at Hosking Partners. They were joined by Jennifer Buchanan and Emily Mansouri, co-heads of the Client Service & Business Development team, who are also founding partners.

OWNERSHIP AND STRUCTURE

Hosking Partners is a limited liability partnership (LLP) which is wholly owned by its partners with no one partner owning more than 25% of the business. We believe an independent ownership structure is important for an asset management company. It helps to ensure that the business remains focused on generating investment returns for clients rather than for external shareholders. We have also implemented a perpetual partnership to ensure that the business retains its boutique, partnership structure over the long-term.

PRODUCTS AND FEES

We are a one product firm. Our entire team is dedicated to managing our one global equity strategy for institutional investors. The strategy is available via pooled vehicles (min. account size $25m) and segregated accounts. We charge a low base fee plus a performance fee. There is also a tiering mechanism which means the base fee lowers as firm-wide AUM increases. We intentionally align our business interests with those of our clients and place emphasis on performance rather than asset growth.

INVESTMENT PHILOSOPHY

Faced with the challenge of distilling a large universe of potential opportunities into a portfolio with attributes that are associated with value creation, the investment team has developed a series of mental models. The models have evolved over many years and reflect common characteristics of successful investments. Many of the models are behavioural and help us to spot contrarian ideas. The use of reductionist models is supported by the finding that analysing more information does not result in greater forecast accuracy, it simply results in greater confidence that forecasts are correct.

The *Capital Cycle* was the first model developed in the 1980s. It recognises the gradual changes that the supply of capital has on the competitive landscape of an industry and the inverse relationship that exists between supply and returns. Under the capital cycle approach, accelerated consolidation is regarded as bullish and the opposite, a proliferation of competing firms, is regarded as bearish. This approach leads us to shun areas of the market where profitability is high and investors are enthusiastic and to target areas where profitability is low and investors are apathetic.

Over the years further filters have been developed. Just as the *Capital Cycle* draws us towards industries that are consolidating and, consequently improving profitability, so the more recent filters reinforce the selection of companies with latent profit that is under-appreciated by the market. These filters include *Jam Tomorrow* and *Inside Ownership*. *Jam Tomorrow* recognises the value of suppressing short-term profit for long-term gain, while *Inside Ownership* seeks to benefit from the alignment of interest often created by a large insider shareholder, frequently a family.

The models transcend sectors and countries. Therefore, each of the portfolio managers has a remit to invest globally. Global generalists benefit from the neuroscientific finding that cognition is improved as contrast levels increase. A Japanese pharmaceutical company is different to a Mexican cement company and, in most fund management architectures, the two are never compared directly due to silo-based investment teams. Such an omission should, in our opinion, be a source of latent alpha.

VALUATION

Superimposed on our models is a valuation discipline that recognises that the greatest source of portfolio risk is buying stocks at the wrong price. We employ a range of valuation tools and avoid the use of elaborate forecasting models. We prefer inference over forecasting and tend to invest if our assumptions are more optimistic than those inferred by the current market price. We also prefer valuation metrics based on replacement costs, takeover values or revenues as these metrics are generally less volatile than corporate earnings. We are flexible in our application of these metrics and adapt our approach depending on market conditions and sectors.

INVESTMENT PROCESS

The fundamental building block behind our portfolio construction is the global generalist, multi-counsellor system. It is premised on the beliefs that the broader the opportunity set the better the chances of good investment outcomes and that individuals make better decisions than committees. Each of our portfolio managers is assigned a portion of the portfolio for which they have sole responsibility for making investment decisions. Although the portfolio managers are autonomous, the team is held together by our investment philosophy.

While investment ideas are discussed among the team, they are deployed individually within each sub-portfolio. The portfolio managers are responsible for conducting their own research. In line with the absence of a top-down policy there are no regularly scheduled investment meetings. Such meetings risk ‘groupthink’ where doubts against the consensus may not be voiced. There is a fair degree of overlap in holdings which we consider a positive attribute as *overlappers* have ideally been independently assessed by more than one portfolio manager. The approach also facilitates bottom-up asset allocation which avoids some of the behavioural risks inherent in top-down asset allocation and portfolio rebalancing.

ENVIRONMENTAL, SOCIAL & GOVERNANCE

Consideration of ESG issues forms a part of the investment analysis, in an integrated approach, as we do not think it is appropriate to isolate any aspect of a company’s activities from the rest. Whilst we may consult third-party ESG research, ratings or screens, we do not exclude any geographies, sectors or stocks from our analysis based on ESG profile alone.

Engagement is an important part of our process and our willingness to take on large stakes in companies increases the impact of our engagement. As well as engaging in specific situations, we focus on company management, and careful consideration is undertaken by the team to assess whether the management teams’ time horizons and incentive frameworks are aligned with the long-term interests of our clients. We also look to confirm management's understanding of capital allocation and believe part of getting capital allocation right is to consider environmental and social risks, along with other factors that might affect a company's long-term valuation.

Proxy voting is a fundamental part of active ownership and our procedures are designed to ensure we instruct the voting of proxies in line with our long-term investment perspective and client investment objectives.

COMPETITIVE ADVANTAGES

We had the rare opportunity and good fortune to start an investment management business from scratch, but with the benefit of 30 years of investment experience. Multiple elements of our approach contribute to the scalability of our product and both our investment approach and organisational structure display unusual characteristics.
Factors that differentiate us:

- One product focus – Global equities
- A fee structure designed to align our interests with those of our clients.
- Global generalist multi-counsellor system.
- An environment that values being roughly right over being precisely wrong
- A highly diversified, all-cap portfolio of over 450 stocks, with a marked value bias and active share of over 80%.
- Low stock specific risk that allows us to invest in riskier and, potentially more rewarding, investment ideas.
- Flexible investment guidelines to capitalise on investment ideas in under-researched areas of the market and to buy securities at the most appropriate level of the capital structure.
- Long-term investment horizon - our holding period is in excess of 7 years.

Above all, the team is unashamedly contrarian and seek to *fish where the fish are, rather than alongside the rest of the fishermen.*