Paramés: "The quality of our portfolio is the best we have ever had"

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10th Annual Client Conference, Madrid

With the Conference Centre absolutely packed, Bestinver has held yet another of its Annual Client Conferences in Madrid, its tenth to be precise.

Three hours in which the three fund managers presented their opinion on their investments, their current portfolio situation and their results, and for a large part of the three hours they focused on taking numerous questions put to them by the investors who had turned up to the conference. This year, for the first time, those taking part were able to follow online through the live webcast available to those in the private user group which the management company has set up on the website of investor community Unience, which some 2,100 of its clients have already joined.

A three-hour presentation allows discussion of several issues, and on this occasion Paramés and his team appeared very much at ease and willing to comment on all the subjects raised. They thus went into detail on aspects ranging from the fact that they still have their entire savings invested in the management company's funds (in the case of Fernando Bernad and Álvaro Guzmán they claim this is so because they are still living in rented accommodation) through to describing how they are in the process of buying into a Chinese company for the first time. They also went into some depth about what for them is the target value for their portfolio and made observations about Spain's financial sector (they are standing by their policy of not investing in it until the day when the full real estate portfolio held by entities is included on-balance sheet), as well as briefly describing their view of the Spanish economy (they prefer investing in Portugal rather than in Spain due to the property bubble in Spain at the moment).

There were also quite a few questions on the value style they pursue in their investments and, more specifically, on the Austrian School of Economics which influences their macroeconomic outlook. Another of the subjects of most concern to investors, judging by the number of questions asked on it, was whether there might be problems in maintaining the level of investments if the company's managed assets increase.

The best portfolio ever

From three years ago, the managers at Bestinver have been steering their portfolio in the direction of stepping up the search for quality in their investments and cutting down on the number of companies they invest in, and this shift has been fruitful. "I can say that the quality of our portfolio is the best we have ever had", says Paramés. As Guzmán explained, this increased quality is because they have better businesses on-portfolio (as the companies have more and bigger competitive advantages), because they are companies that do not need to invest heavily and they operate in industries that will still be there in the next 15 years and the companies will still have a major market share in these. Managers have additionally persisted in their efforts to pick out companies to invest in that have real assets.

As a result, its international portfolio currently has a larger upside potential than before the crisis in July 2007. In specific terms, Bestinver Internacional at the moment has an upside potential of 102%, Bestinver Bolsa one of 85%, Bestinfond 97% and its hedge fund upside of 130%. "At Bestinver we like to think that we are in the business of studying companies, and this works out at a figure which is the target value for our portfolio", pointed out Guzmán. "I recommend seeing this like a traffic light which has gone green".

The largest positions in the international portfolio are BMW (8.5%), Exor (7.1%), CIR/COFIDE (6.9%), Wolters Kluwer (6.8%), Schindler (5.7%) and Thales (4.6%) and the El PER 2011 for the international portfolio is 7.4. "We like to know why companies are cheap and the answer in many cases is patience. We are willing to wait until they reach the target price which we feel they have the potential for", explain the managers, who have insisted in their claims that there is no "magic" in their investments.

On the other hand, in the Iberian portfolio the target value has come up by 7.4% since December 2009 and currently stands at 77.4 euros per share, which would imply a rise of 85%. In general terms they have companies with very little exposure to the Spanish economy and none of those they have are in the financial sector. In this case the PER 2011 is 8.1 and their biggest positions are in Semapa Portucel (9.2% of the fund), Ferrovial (9.2%), Corporación Alba (7.9%), Sonae (6.8%) and Gas Natural (5.9%).

The managers at Bestinver spend 90% of their time researching companies and, as Paramés pointed out, they have “blind" faith in them.

During the conference Paramés briefly made mention of two Spanish companies with disparate results. On the one hand he said that CAF has been probably the best investment they have made in the management company’s 20 years of existence and recognises that it is still an "exceptional" company that remains undervalued, though not at the same level as some years ago. They have therefore been scaling down their position in the company. On the other hand, Paramés acknowledged that Inditex has been an "error of omission" through never having been in the portfolio. "We have studied it several times but it has always been too expensive for our liking, and right now I don’t know whether it is a good investment, but, whatever the case, in retrospect it was clearly a mistake", he admits.

At Bestinver they advise their clients to split their portfolio with the management company, putting 70% into its international funds and 30% into the domestic portfolio, while they in any case advise against trying to optimise positions in one or the other portfolio as, in his opinion, it is not worth it, since both have good growth potential and in the long run offer similar results (according to their calculations, in the last five years Bestinver Bolsa has offered a total yield of 42.66% and Bestinver Internacional one of 43.17%). There are greater differences in results between Bestinfond and Bestinver Hedge Value, though, as Paramés explained, this is due to the hedge fund’s smaller size and its greater flexibility, although, as he reminded, it is the same portfolio as Bestinfond but more concentrated. In this case, between September 2007 and February 2011 Bestinfond managed a total yield of 3.15% versus 15.98% for the hedge fund.

Whatever the case, they are still charging a redemption fee for withdrawals from their funds earlier than one year since, as Paramés said, what they ask of their clients is "stability". As Paramés stated, they are always asked what they understand by long term and, according to their latest calculations, this would be ten years. Thus the yield over ten years at any given time for the international portfolio would have been a maximum of 12.06% and a minimum of 4.45%, which the managers hope to continue achieving over the next ten years, although Paramés reminds us of the phrase "past performance is no guarantee of future returns". These positive figures are also true for the management company’s Iberian portfolio.

Investing in China

Paramés has repeatedly said that they focus on investing in companies which are within a radius of two hours by plane. The in-depth research they carry out into companies requires that they have a profound knowledge of them, and such proximity has its advantages. Yet exceptions exist to be applied and, as Paramés announced at the conference, they are in the process of investing in a company in China for the first time. The manager did not reveal the name of the company and limited himself to saying that it is half-way between Taiwan and China and that it is a sector leader.

Bestinver has had an office in Asia since February 2009 and it was through the work of the manager based there, Herman Chan, that they decided to take a holding in the company. It admits there are certain barriers to investing in more Chinese companies, such as distance or the language, but it does not rule out this initial investment opening up a new direction. "You don’t know what might happen; maybe in ten years’ time we will have to go and live there", said Paramés.

The capacity issue

Following the redemptions suffered by Bestinver in 2008, the management company has steadily built up net subscriptions since May 2009, and currently has total assets under management of 5.34 billion euros. As Paramés said, over the last year alone, 3,000 new clients have come to the management company.

Asked about the new mandate from the Norwegian Government Pension Fund (see news-item), the team at Bestinver takes the view that it should be seen as good news for all clients of the company, as it involves very long-term investments which partly offset the redemptions suffered by Bestinver Bolsa (it dropped from 1.1 billion euros before the crisis to the figure of 303 million it now has), for which reason there are no capacity problems. Paramés in any case recognised that they spent a long time deciding to accept the mandate and they will not “say yes to just any sovereign fund".

Paramés actually insisted several times during the conference that the management company does not do any marketing ("the work we do is the best form of marketing we do", he said) and said that under no circumstances will they turn Bestinver into "a money-making machine". According to the manager it is not guided by a desire to attract more money, but instead "to make money profitable and that alters our day-to-day approach to our work", since they can focus on the management and research side without having to engage in sales efforts.

As they have already stated on previous occasions, at the management company they are leaving the door open to the possibility of taking steps to limiting the growth of funds, should the need arise. They would therefore consider options ranging from closing a certain product to new subscriptions to charging high front end fees but, whatever the case, such measures are envisaged for the future.

Macroeconomic view

Paramés and his team avoid making macroeconomic predictions and the only thing they observe is that world economic growth for 2011 will be reasonable. "If any small European financial system should collapse, that is not important", says Paramés. "But if the USA or Japan collapsed, that *would* be serious. In such cases the best thing is to hold companies that have real assets".

Regarding the Spanish financial system the management team at Bestinver sticks to the same line that it has taken for some years now. "Until the real estate assets held by financial institutions are shown on the balance sheet in a way which we consider truly representative, we shall not be investing in the financial system", they say.