INVESTMENT MANAGER COMMENTARY

PALM CAPITAL

Q1 2019

April 2019 | Mahomed Ibrahim

At Palm Capital, we look for businesses with durable competitive advantages run by exceptional managers. We patiently wait to invest when their prices are less than we think they are worth, aiming to benefit as they compound economic value over time. We only sell if fundamentals deteriorate, or we find others offering potentially better after-tax returns.

Our performance

Our portfolio returned 17.3% over the quarter after all fees and expenses, outperforming the MSCI World Index by 4.8%.

Since we started just over a year ago, our portfolio has returned 6.9% cumulatively after all fees and expenses or 8.0% before fees but after expenses, outperforming the Index which has returned 0.2%.

We'd like to remind clients that such large deviations are to be expected as the portfolio differs vastly from the benchmark. We'd also like to remind you that given that this is still a short period of time in the market, our relative performance could easily have been reversed.

The market's rally

Over the last three months, markets reversed most of the preceding quarter's decline. As we mentioned in our last commentary, in the short-term, prices move randomly and it's impossible to know which direction they will take. As compelling as media narratives sound, they are rarely right.

What we do know, however, is that in the long-term, share prices follow the fundamentals of businesses. Therefore, buying good businesses at good prices will earn us attractive returns over the long-term.

The share prices of every single share in our portfolio increased over the period. For a change, the tobacco shares were bright spots, with Philip Morris and BAT rallying 32% and 27% respectively. Many of our new purchases in the last quarter were also strong contributors; Adobe, Analog Devices, Equifax, Microsoft and Texas Instruments all had double digit returns.

A note on our approach

We've had a few questions from clients about how to classify our approach. "Are we value managers or growth managers?" they ask. We aren't surprised by this question as the definitions of these two investment approaches aren't standard across the industry.

Our answer is that our primary focus is value. Future returns from an asset depend on the price paid for it relative to how much it's worth. That's irrespective of how fast or slow the asset is growing.

While this sounds simple, the tricky part is in correctly estimating how much an asset is worth. History is littered with examples of entrepreneurs or managers selling their businesses for a lot less than their worth or buying similar businesses to their own for a lot more than their worth. So, if people with such intricate knowledge of companies and industries can make these mistakes, how can we, as outsiders, expect to do any better?

Our solution to this problem is to focus on businesses with enduring competitive advantages. We believe that these advantages increase our chances of being right in our estimates of future cashflows and hence correctly estimating worth. And if we're patient enough to wait for attractive prices, we should earn very attractive returns from them over time. Many of these businesses, by virtue of their advantages, happen to be growing very quickly.

Our portfolio

Although the portfolio rallied, we placed only one trade over the quarter, trimming our holding in Blackrock back down to our prudent limit. None of our other holdings were far enough above our estimate of their fair value to justify taking profits.

Top 10 holdings as at 31 March 2019

Share	% of fund
British American Tobacco plc	12.8%
Amazon.com, Inc	11.6%
Alphabet Inc (Class C)	6.2%
Facebook, Inc	5.9%
AIA Group Ltd	5.9%
Allergan plc	5.8%
Philip Morris International Inc	5.6%
Microsoft Corp	5.2%
Adobe Systems Inc	4.8%
PepsiCo, Inc	3.6%