

## Patient, unconstrained, contrarian value investing

Oldfield Partners has about \$3.9 billion under management for families, individuals, charities, trusts, endowment funds and pension funds, through separate portfolios and pooled funds. The executive partners are Jamie Carter, Chris Driver, Harry Fraser, Richard Garstang, Andrew Goodwin, David Jones, Juliet Marber, John McEwing, Richard Oldfield, Tom Taylor, Edward Troughton, Nigel Waller, Robert White and Samuel Ziff.

This quarterly newsletter is the companion to our monthly reports on the pooled funds which we manage. If you do not currently receive a monthly report for any of these but want to in the future, please email [info@oldfieldpartners.com](mailto:info@oldfieldpartners.com).

Our approach in the management of all portfolios is long-only, no leverage, value-focused, index-ignorant, highly concentrated, and anti-short-term. The focus is on investing in individually attractive companies rather than on considering the respective attractions of different countries or sectors. With rare exceptions the country and sector weightings are the result of stock selection.

We manage global equity portfolios, emerging market equity portfolios, an EAFE equity fund, a global equity income fund and a global smaller companies equity fund.

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### Commentary

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“A trend is your friend  
Until it should bend  
And come to an end  
And then it’s no longer your friend.”

Two trends still firmly in place are the outstanding performance of the US equity market, outperforming nearly all others, and the outperformance of “Growth”. In the first half of this year, the S&P 500 in the US has given a return of 17.2%, its strongest showing since 1997. The supremacy of US equities has been well justified by the strength of technology innovation and by earnings growth: earnings per share have risen by 6.1% per annum since 2008. The result is that the current price-earnings ratio of the S&P 500 is 18.1, exactly the same (Cerno Capital point out) as prevailed in June 2009, close to the beginning of the bull market. On the other hand, the Shiller price-earnings ratio, which takes today’s share prices divided by the average of the last ten years’ earnings (in order to smooth out cyclical ups and downs) is at an extremely high level. Critics of the use of Shiller point out that it is not much of a predictor: that is true of the short term, but not of the long term. Markets with high Shiller P/E ratios tend to have low returns over 10 years, markets with low P/E ratios tend to have high returns.

A good chunk of the US earnings per share growth has been achieved by share buybacks, given extra acceleration recently by tax cuts in the last two years. The value of share buybacks has exceeded total net income in several of the last few years. The result is that, according to Cerno, 134 of the 398 non-financial companies in the S&P 500 have more net debt than equity, usually an indication of over-extension. We remain very wary of the trend of US equity performance. We cannot know when the trend will end, though we have a stab at guessing from time to time, but it is a question of when rather than if.

As for Value versus Growth, we have had a stab at the timing of a turn in this trend, too. We felt very convinced in February 2016 that we were seeing the turn, and indeed 2016 was a golden year; but no gold since for our global portfolios, and our emerging markets portfolios, which had an excellent 2018, have also been struggling this year. Growth has outperformed Value to an extent unprecedented in recent times. In the long term there is some advantage to Value because of the simple but true proposition that low valuations lead in the long term to high returns. The Value path requires enormous patience because in the short term companies which have low valuations so often have some problem which may or may not prove to be temporary and because there can therefore be periods of several years when the proposition does not work.

Frequently a precursor to the outperformance of Value is the beginning of a rise in interest rates – as in November 2015. The reversal of Fed policy earlier this year provided a new boost to Growth. There is no sign of another about-turn: around the world, interest rates look likely to remain very low. We would not depend too much on this prediction. In September last year there was complete unanimity among economists that interest rates were set to rise, and the consensus, both of the economists and of Fed members themselves, was that there would be three interest rate rises in the US during 2019. Now there is complete unanimity in the opposite direction, encouraged by the President: “if we had a Fed that would lower interest rates we’d be like a rocket ship.” Forecasting is notoriously difficult. We are in an extraordinary time in which around the world in many places interest rates are actually negative: there are \$12 trillion of bonds globally with negative yields. This cannot last for ever, or even for long.

## Commentary – continued

Japan is one market in which there continue to be plenty of opportunities for Value investors. CLSA have pointed out that there are 75 non-financial companies with market capitalisations of more than \$1 billion, a dividend yield of 3.3% or more, and these dividends well covered by earnings. These companies have an average price to tangible book value ratio of 1.1 and an average price-earnings ratio of under 10. As we have discussed in recent years shareholders are becoming more demanding in Japan. The Financial Times began a recent leading article: “corporate Japan is on the cusp of change.” In 2011, only 20 shareholder proposals were put forward at corporate AGMs. This year, the number has been 54. The introduction of stewardship and governance codes has benefited shareholders. The world’s largest pension fund, that of the Japanese government, now requires its asset managers to disclose their voting records and to provide a rationale. The recent AGM at Nomura provided an example of the effect of this greater engagement: the chief executive received a vote in favour of his reappointment of only 62%. These activist influences are likely to shift managements from their tendency to inertia.

One trend at OP has come to an end: Claus Anthon retired, as planned, on his 62<sup>nd</sup> birthday, at the end of May 2019. Claus is the first person to leave the investment team since we started in 2005 and we are grateful for all he has done for the firm. We wish him well and look forward to a new relationship with him, as a client rather than a colleague.

## Strategy performance summary

	Launch date	Currency	Since launch (%)		Year to date (%)	
			Strategy	Index	Strategy	Index
EAFE Equity	01/01/2019	USD	+5.7	+14.0	+5.7	+14.0
Emerging Markets Equity	01/01/2001	USD	+855.0	+392.6	+3.5	+10.6
Global Equity	01/01/2000	USD	+239.7	+121.0	+7.2	+17.0
Global Equity Income	01/01/2012	GBP	+120.1	+125.0	+14.5	+14.2
Global Smaller Companies	01/04/2005	USD	+139.8	+180.4	+16.8	+17.1

Source: Oldfield Partners. Performance shown is the composite performance for each respective strategy. Performance is calculated net of investment management fees and expenses and on a total return basis.

## Strategy snapshot

	Number of holdings	Market cap. focus	Active share	Year to date turnover
EAFE Equity	22	>US\$10.0bn	94%	4%
Emerging Markets Equity	17	>US\$0.5bn	94%	2%
Global Equity	23	>US\$10.0bn	98%	8%
Global Equity Income	27	>US\$1.0bn	93%	7%
Global Smaller Companies	24	<US\$5.0bn	100%	8%

Source: Oldfield Partners, Bloomberg. Strategy representative portfolios used. Active share is calculated using the sum of the absolute value of the differences of the weight of each holding in the manager’s portfolio versus the weight of each holding in the benchmark index, divided by two. Turnover is calculated by dividing the lesser of purchases and sales by the average market value.

**The value of all investments and the income from them can go down as well as up; this may be due, in part, to exchange rate fluctuations. Past performance is not necessarily a guide to future performance.**

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