



Martin Currie Global Portfolio

Utilising a complex investment process and concentrated portfolio, MNP has a track record of outperforming global equities...

Summary

Update
17 February 2021

Martin Currie Global Portfolio Trust (MNP), managed by Zehrid Osmani, offers investors a concentrated portfolio of global equities with a high active share of c. 97%, differentiating it from both its peers and its benchmark. MNP’s impressive track record is in large part thanks to Zehrid’s successful stock selection and three-part investment process, outlined in detail in the **Portfolio section**. Zehrid’s forward-looking approach to analysis has led him to create a robust portfolio which has been partly insulated from the impacts of COVID-19, having evaluated for just such a worst-case scenario prior to the outbreak. The team also make exhaustive use of proprietary **ESG** analysis, and MNP ranks in the top 2% for sustainability amongst over 6,700 global equity peers.

Since taking over sole management of MNP in October 2018, Zehrid has generated an NAV total return of 42%, exceeding the MSCI ACWI benchmark’s 22.9% return over the same period. It is important to note that this **performance** was achieved with a substantial underweight to the large-cap technology stocks which have driven a significant proportion of global equity markets’ performance over the last two years. Despite its commendable performance, MNP has traded closely to NAV, helped by the board’s proactive policy of **discount** control, and currently the trust trades on a premium of 3.1%.

Recently MNP has enacted a new **gearing** policy to better take advantage of the trust structure, whereby it has implemented £30m in gearing, equivalent to 9% of the current NAV. Alongside this the board has seen fit to implement a new **charges** structure, with the intention of simplifying the overall cost of the strategy.

Analyst’s View

We view MNP as a highly differentiated, high-conviction portfolio due to its zero exposure to FAANG stocks and high active share. Zehrid’s strategy of constructing a diversified portfolio, rather than simply being overweight to his highest-conviction stocks, gives us confidence in MNP’s ability to offer clients a superior source of diversification. From the start of his tenure Zehrid has been able to provide returns in excess of those of MNP’s benchmark, despite MNP’s underweight to mega-cap technology shares, ultimately fulfilling the trust’s objective of outperformance.

The two recent changes to MNP, specifically the introduction of £30m in gearing and reduction in fees, are ultimately a benefit for investors. It is our opinion that the introduction of gearing will improve the overall return potential of MNP (given its long-term outperformance), as well as making use of the unique advantages of a trust’s structure. The change in the fee structure reflects the board’s desire to grow the trust, something we also foresee occurring given Zehrid’s record of outperformance.

While we believe MNP’s advantage ultimately lies in its ability to provide both superior returns and diversification, the presence of a modest yield is welcome. MNP’s track record of growing, or at least maintaining, its dividend over the last 16 years is yet another attractive feature of an already competitive trust. We believe that its ESG credentials are almost unrivalled in both the open- and closed-ended spaces, with a five-globe rating from Morningstar making it an excellent choice for a sustainability-minded investor.

Analysts: David Johnson



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BULL

Diversified portfolio of global equities with high active share

Strong outperformance since the manager took over

Portfolio does not hold traditional mega-cap names, yet has still generated strong returns

BEAR

Large bias to quality growth stocks may cause underperformance in a value recovery

Manager’s intentional avoidance of direct exposure to the FAANG stocks has been an overall detractor

Recent use of gearing may negatively impact performance during down markets



Portfolio

Martin Currie Global Portfolio Trust (MNP) offers investors a concentrated, high-conviction portfolio of global equities. MNP is run by Martin Currie, a boutique asset manager owned by Franklin Templeton, with the strategy having been managed solely by Zehrid Osmani since October 2018. Zehrid is supported by a further team of 12 analysts, each with their own sectors of expertise and accountability within the investment process; there is an average of 15 years' experience per member. MNP's investment process is ultimately one of bottom-up stock selection, seeking to generate sustainable, long-term returns in excess of the MSCI All Country World Index. The two most important changes to MNP since **our last note** have been the introduction of a 10% gearing target (something we outline further in the **Gearing section**), and the introduction of a new fee structure (as outlined in the **Charges section**).

Given the bottom-up nature of MNP, Zehrid does not focus on the analysis of macroeconomic factors despite the trust's global remit; rather, he uses a proprietary three-step process of stock analysis and portfolio construction. The first step is 'idea generation', where Zehrid uses a screening process to filter down his universe, which is important considering the global reach of the strategy and MNP's ability to invest across the market-cap spectrum (although the portfolio currently has a large-cap bias). The screen's purpose is to identify companies with superior quality factors, e.g. high return on invested capital (ROIC), a good growth profile, balance sheet strength, and revenue and cash growth. The second step is for the team to perform deep fundamental analysis on the resulting pool of companies. Not only do the team scrutinise quality factors in greater depth, but they also create a detailed risk/return profile for each company as well as assigning it a valuation.

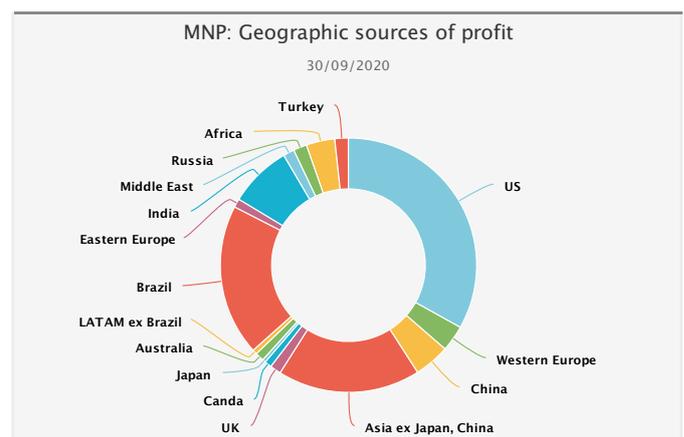
The team's fundamental analysis of a company looks beyond its conventional quality metrics and instead analyses the sustainability of its business model. Zehrid outlines eight key broad characteristics which he and the team use: high barriers to entry; a dominant market position; strong pricing power; low disruption risk; structural growth prospects; a high and sustainable Return on Invested Capital (ROIC); strong compounding cash flows; and quality management. Companies which can embody all, or the majority, of these characteristics are considered to have sufficiently strong business models to be potential buys. The team's assessment of a company's business model goes hand in hand with the value they assign it. When valuing a company, the team use a weighted average of discounted cash flows, ROIC over the weighted average cost of capital, and target price multiples. When assigning valuations we understand that the team tend to err on the conservative side, using what

they believe are large discount values when pricing a company.

The third step of Zehrid's fundamental analysis is an assessment of a company's risk. The team use a detailed risk framework, akin to a checklist, with the same set of criteria being applied systemically across any company. While the list is exhaustive in its coverage, it can be broken down into four broad criteria: industry risks, e.g. the risk of competition and loss of pricing power; company risks, e.g. regulatory impacts and inflation risk; governance and sustainability risks; and portfolio risks, e.g. liquidity risk and momentum. A common factor shared in both the analysis of risk and reward is ESG, with Zehrid utilising an exhaustive ESG process to understand both the risks and opportunities it presents, something we outline in more detail in the **ESG section**.

The final stage in MNP's investment process is portfolio construction. The team aims to ensure that MNP's portfolio does not simply reflect the team's best ideas but rather a complex balance of risk and return based around a host of factors. For example, the team aim to ensure that the portfolio is diversified not just by region and sector, but also by the underlying sources of revenue and profit, and by end markets that the companies invested in by the trust are addressing. While MNP's portfolio tracks its benchmark's regional allocation relatively closely, it is far more diversified when it comes to the underlying sources of revenue and profit, with the breakdown of revenue sources by region shown by the chart below. As an example, while MNP is underweight to UK-listed companies, it has a neutral exposure to UK revenues.

Fig.1: Geographic Sources Of Profit



Source: Martin Currie

The team take their analysis beyond mere regions, but also look at the end market user exposure, as they seek to have a diverse client base to prevent a shock to any one type of consumer having a disproportionate impact on the portfolio. MNP's end users' market exposure is currently



split 47% business, 48% consumer and 12% government of net assets (with the portfolio currently geared). End user and revenue source are merely two examples of the types of unconventional risks the team look to diversify away from, as they also assess the balance between quality and earnings growth, the risks posed to the supply chain and how sensitive MNP is to business cycles.

While MNP's investment process is undeniably exhaustive, what we find particularly interesting is the forward-looking nature of Zehrid's analysis. Whereas much of the available data is by its very nature backward-looking (as companies primarily report their historical accounts), Zehrid makes a point to place greater weight on forecasting. He and the team will often forecast multiple scenarios for each stage of analysis, in order to assess how a company will perform in various scenarios. COVID-19 has vindicated Zehrid's forward-looking approach in our opinion, as one of the scenarios the team analysed was based on a 'Dark sky', which accounts for the worst possible case (such as the COVID-19 pandemic). This helped ensure that MNP was crisis-ready going into the pandemic, and for example prevented the trust's holdings from being materially impacted by supply chain disruptions. Thanks to this forward-looking nature, Zehrid has been afforded the luxury of being able to increase MNP's exposure to companies with shorter track records. Under the previous manager MNP's holdings would often be required to have ten-year track records as a minimum (to provide sufficient data for analysis), but Zehrid has instead invested in companies with much shorter histories of public trading, with one example being his holding of Ferrari (which only went public in 2015).

The result of MNP's investment process is a highly concentrated yet well-diversified portfolio, currently with 30 holdings and with 44% of the portfolio held in the top ten stocks. Since taking over the trust in 2018, we understand that Zehrid has seen fit to increase the concentration of the portfolio and its exposure to high-quality, high-growth names while simultaneously increasing the use of diversification in the investment process. The result is a portfolio which is more reflective of the team's highest-conviction stocks without skewing the risk as a result. Despite its concentration and high active share (currently 97%), most of MNP's risk comes through stock selection, which we understand he is able to achieve as a result of the on-benchmark regional allocation and heavy use of portfolio diversification. A list of MNP's current top ten holdings can be seen below.

While Zehrid and the team follow a wholly bottom-up process, they do acknowledge the three broader themes which underpin many of their holdings. Such themes help the team identify businesses which they forecast having the highest return on invested capital, as well as highlighting additional factors through which they can further diversify their portfolio. The three themes are:

the future of technology (e.g. cloud computing); resource scarcity (e.g. physical infrastructure); and demographic change (e.g. emerging market consumer growth). When investing along these themes, Zehrid prefers to focus on companies which are downstream from the more commonly associated names, so as to prevent his exposure to a single brand or producer.

Top Ten Holdings

HOLDING	WEIGHT (%)
Masimo	5.4
Taiwan Semiconductor Manufacturing	5.1
ResMed	4.6
Microsoft	4.4
Moncler	4.4
Visa	4.1
Linde	4.1
Hexagon	4.1
Ansys	3.9
Atlas Copco	3.9
Total	44.0

Source: Martin Currie, as at 31/12/2020

For example, Apple is one of the largest players in the digital media space and a key beneficiary of the expanding emerging market consumer base factors which sit squarely within MNP's underlying themes. Yet rather than invest in Apple, Zehrid instead prefers to invest in the semiconductor equipment providers, the gaming publishers and payment services which are key suppliers to Apple. While such allocations have positively contributed to MNP's alpha and active share, Zehrid's avoidance of these mega-cap technology stocks has resulted in a drag on relative returns, given that the FAANG stocks were amongst 2020's best performers.

Despite the turbulent markets resulting from COVID-19, MNP has seen relatively little turnover during 2020, thanks to Zehrid's long-term approach to investing and his forward-looking analysis preventing exposure to many of the COVID-19 'losers'. Recent purchases include Kingspan, a global leader in insulation and building envelope solutions and a clear beneficiary of the resource scarcity theme. The other recent addition to MNP is WuXi Biologics, a Chinese firm with global leadership in bioprocessing which provides integrated technology platforms for biologics drug development, an example of an overlap between the future of technology and demographic change themes. There have been two corresponding sales over the last three months: of Canadian National Railway and of Straumann.

As is reflected in its high valuation ratios, MNP's current portfolio has a strong tilt towards quality growth but



also superior historic return statistics when compared to those of its benchmark, as demonstrated in the table below. While each of the major valuation ratios of MNP is higher than its benchmark's, the statistics which indicate the quality of the portfolio are also high, indicating the superior quality of its underlying holdings. Most importantly, the ROIC of the trust is more than double that of the index, a figure that is a key component of MNP's determination of a company's superior earnings potential.

Price Ratios And Equity Statistics

	MNP	MSCI ALL COUNTRY WORLD INDEX
P/E Ratio	47.4	24.7
P/B Ratio	7.3	2.7
P/S Ratio	6.7	2.1
P/C Ratio	27.7	13.4
ROA %	11.9	6.9
ROE %	25.2	20.0
P/FCF Ratio	45.1	27.1
ROIC %	29.0	12.0

Source: Morningstar, Martin Currie, as at 31/12/2020

Past performance is not a reliable guide to future returns

Gearing

On 23/11/2020 MNP's board announced the introduction of gearing – prior to that MNP had operated without it. A three-year £30m loan facility is now in place, which represented gearing of 10% of the NAV at time of investment. With the recent growth in NAV, MNP currently has a 9% level of gearing, though this is still higher than the 5% average of its peer group (Source: JPMorgan Cazenove, as at 25/01/2021).

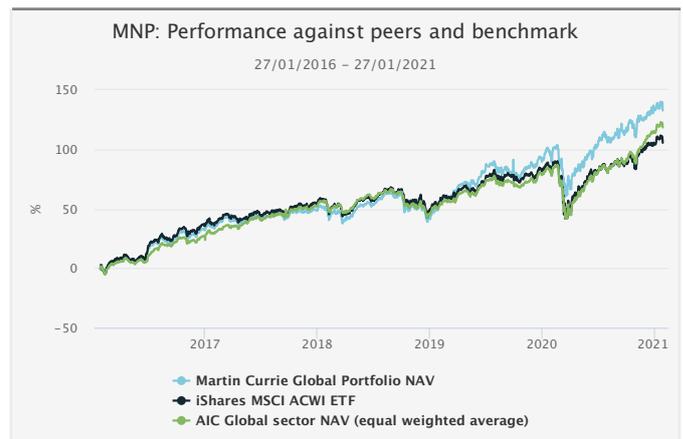
The gearing will be structural in nature, with the manager and board expecting to keep the current amount of gearing in place going forward. Rather than being used in an opportunistic fashion or to add additional holdings, the gearing has been deployed proportionally across all holdings so as to increase the overall market exposure of the portfolio.

Performance

Zehrid took over sole management of MNP in October 2018. Since then the portfolio has generated NAV total returns of 42%, compared to benchmark MSCI ACWI index returns of 22.9%. The AIC Global sector has returned 46.6%, although we note that this is dominated by the returns of Scottish Mortgage, which has had an exceptional run of performance. This outperformance of the benchmark

is exceptionally impressive in our view, given it has been achieved without exposure to the FAANG stocks which have led the market. We use an equally weighted version of the peer group to control for the impact of Scottish Mortgage. Over the last five years MNP has managed to generate an NAV return of 132.4% and a share price return of 136.3%, exceeding the 105.5% return of its benchmark. MNP has also been able to exceed its peer group's performance over the last five years, with the peer group generating an NAV performance of 118.4%.

Fig.2: Five-Year Performance

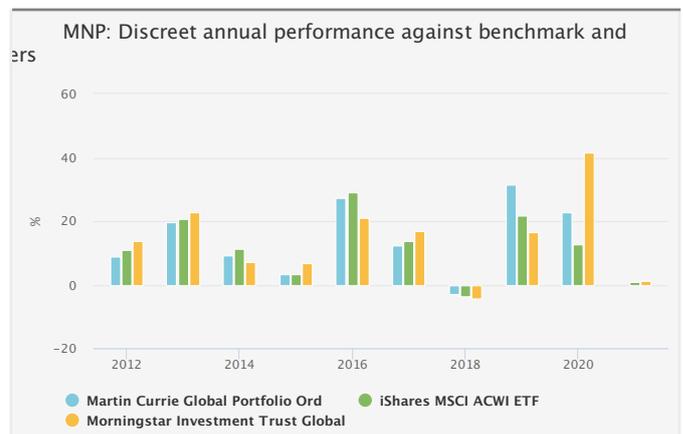


Source: Morningstar

Past performance is not a reliable indicator of future results.

We believe the trust's discrete calendar-year performance is a useful comparative tool, as through it we are able to see the consistency of MNP's outperformance over its benchmark. MNP outperformed its benchmark in 2019 and 2020, the two complete past years that Zehrid has been manager, as well as in 2018. The large-cap US technology names which make up the FAANGs have been among the major contributors to the benchmark's performance over both 2019 and 2020, and while Zehrid acknowledges that underexposure to these names has negatively impacted the trust's relative performance, MNP has still been able to outperform regardless.

Fig.3: Discrete Annual Performance



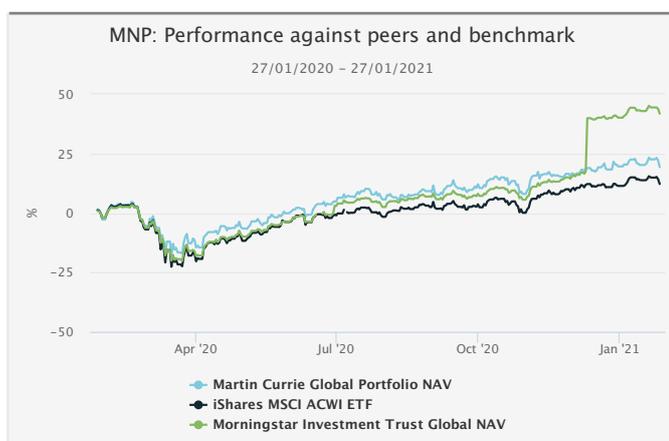
Source: Morningstar

Past performance is not a reliable indicator of future results.



Over the past year MNP has generated an NAV return of 19.3%, compared to the 12.2% return of its benchmark and the 17.9% return of its peer group. MNP has displayed a high sector contribution, thanks to its overweight to growth sectors like technology, but has also provided a high stock contribution despite the underweight to the FAANGS (something rarely seen in the equity sector). We believe that it is the combination of these two factors (i.e. the overweight to quality growth and underweight to the common mega caps) that has allowed MNP to provide both alpha and diversification in what is one of the most crowded sectors, quality growth.

Fig.4: One-Year Performance



Source: Morningstar

Past performance is not a reliable indicator of future results.

Looking forward, overall Zehrid is optimistic for 2021. He believes that although it will likely be a year of recovery, the magnitude of the recovery remains uncertain. The size of the recovery will depend on the scale of the fiscal stimulus across the world and the ability for the vaccine roll-out to normalise the day-to-day operations of global economies. Zehrid believes that US valuations are appearing increasingly stretched versus their historical average, while the valuations of Asian and European equities remain attractive. Zehrid also sees tailwinds emerging from the upcoming Biden presidency thanks to the new president's more diplomatic approach to foreign policy, which may reduce volatility in global equity markets. Zehrid is also increasingly excited about consumer goods, given the propensity for a post-pandemic recovery in consumer spending which should act as a tailwind for his holdings in Moncler and Masimo (which are amongst MNP's top ten holdings), both of which are producers of high-end consumer goods.

Dividend

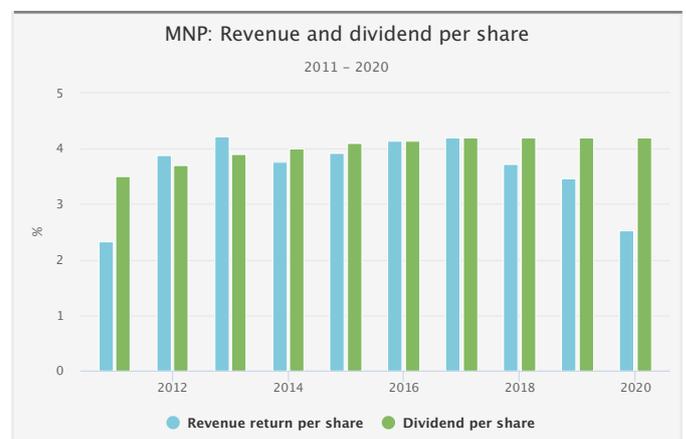
Given MNP's objective of total return in excess of its benchmark, the provision and growth of its dividend is not a primary concern. That being said, MNP does provide a

quarterly dividend payment, and has either maintained or grown its dividend each financial year since launching in 1999.

In April the trust paid its final dividend for FY 2020, taking the total payment for the year to 4.2p per share. This was in line with the previous three years, meaning the trust's five-year dividend growth now stands at 0.5%. The trust's historical yield is 1.1% at the time of writing (Source: JPMorgan Cazenove, as at 25/01/2021).

The most recent dividend was not fully covered by the year's income, requiring the use of reserves. We estimate that MNP's current revenue reserve coverage is 0.7x, based on the last full-year dividend and most recently reported accounts. The declining revenue per share can be attributed to the increasing performance of, and thus allocation to, lower-yielding quality growth stocks. While the trust has been dipping into revenue reserves in recent years, MNP does have a substantial special revenue reserve of £65.5m (source: Martin Currie, as at 31/07/2020) which the board can use to support that dividend in the future as it sees fit, paying the dividend from capital if it so wishes. MNP has paid an interim dividend of 1.8p per share, the same as the prior year's interim dividend, though the interim revenue of 1.31p per share fell short of covering the dividend.

Fig.5: Dividend And Revenue Per Share



Source: Martin Currie

Past performance is not a reliable indicator of future results.

Management

MNP has been run by Zehrid Osmani since 30/06/2018 as co-manager alongside Tom Walker, and as sole manager since October 2018; prior to that it was run by Tom Walker for the prior 18 years. Outside of his responsibilities to MNP, Zehrid acts as the head of the Global Long-Term Unconstrained strategy at Martin Currie (a subsidiary of Franklin Templeton). He also leads the Global Long-Term Unconstrained strategy's team and has

a management role in Martin Currie’s four open-ended long-term unconstrained strategies. The Global Long-Term Unconstrained team consists of nine investment professionals, each with their own sectors of expertise and accountability within MNP’s investment process, with an average of 15 years’ experience per member.

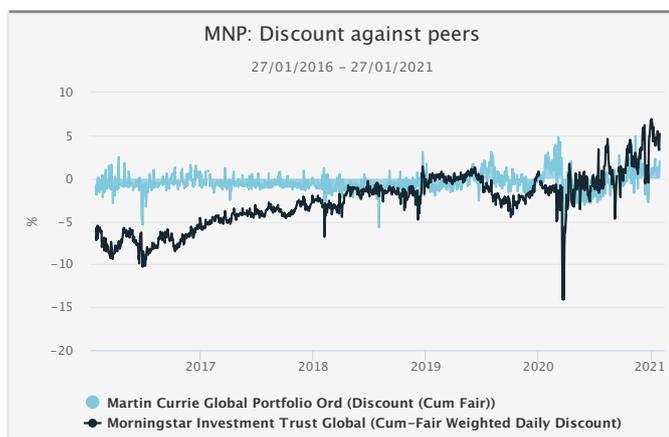
Zehrid joined Martin Currie from BlackRock where, during his ten years there, he played a key part in building the company’s successful European equity franchise. He held a number of senior roles at the company, including as head of European equities research with responsibility for a 23-strong team of analysts. In this role, he developed and implemented a fundamental research platform, demonstrating his strong understanding of equity research. Zehrid also managed a number of equity funds at BlackRock, with a specific focus on managing the team’s unconstrained high-conviction, long-term portfolios, driven by fundamental research.

Discount

MNP currently trades at a 3.1% premium, above the 0.3% average premium of the AIC global peer group. Over the last few years MNP has traded tightly around its NAV, except for the brief period of extreme market volatility in early 2020 resulting from COVID-19. (Source: JPMorgan Cazenove, as at 15/02/2021)

We would comment that this has partly been the result of the successful ‘zero discount’ policy of the board. While this policy does not include any hard limits around the amount of repurchases that may be made, it does allow the board to intervene in order to prevent the share price from falling materially below NAV in normal market conditions. Shares bought back as part of this policy are held in treasury and reissued when demand exists which the market cannot supply. Since the start of 2020, the board saw fit to both issue and buy back shares at varying

Fig.6: Discount



Source: Morningstar

Past performance is not a reliable indicator of future results.

periods so as to ensure the trust trades close to NAV. The total effect of these transactions has been for the board to issue a net of 1.6m shares, equivalent to 2% of the current shares in issue.

Charges

The board has recently announced the removal of MNP’s performance fee and the introduction of a new, highly competitive fee structure, effective from 01/02/2021. The new fee structure will follow a two-tiered management fee. A 0.5% p.a. fee will be applied to the first £300m of NAV, and a second tier of 0.35% p.a. will be applied to NAV exceeding £300m. MNP’s current OCF is 0.61%, slightly above the 0.49% average of the peer group (though this figure is heavily skewed downward by the presence of Scottish Mortgage). The change in the fee structure reflects the desire of the board and Martin Currie to grow the trust; if such an outcome occurs, one can expect the OCF to reduce over time.

MNP currently has a KID RIY of 0.86%, below the peer group’s average of 1.03%. However, we caution that the calculation method for the KID RIY varies between trusts, and that MNP’s figure may change because of the new fee structure.

ESG

ESG is a fundamental part of Zehrid’s investment process, a component in the analysis of both risk and return. ESG is incorporated through a proprietary scoring system, which is a similar framework to the risk score used in MNP’s fundamental analysis. Each ESG risk factor is given a score of 1 to 5, with a lower score reflecting a lower ESG risk. We believe that MNP’s ESG risk framework encompasses the vast majority of the key ESG risks faced by a company, with an especially detailed analysis of sustainability. For example, MNP accounts for environmental risks such as a company’s carbon footprint and pollution risks, while it also accounts for social risks like a lack of diversity, exploitation and consumer trust. These factors are not assessed separately, but are instead an aggregate of a much larger subset of ESG factors the team consider, with exploitation risk being calculated through the aggregate assessment of a further 20 risk factors, as can be seen below.

MNP’s ESG framework has also been a deciding factor in its sell discipline. The exit from a position in Reckitt Benckiser in April 2019 was in part a result of that company’s deteriorating corporate culture and ethics, while the sale of Unilever in early 2020 was the result of a profit warning due to the lack of oversight and control in the company’s African operations.



Fig.7: Example Analysis Of MNP'S ESG Integration



Source: Martin Currie

We believe that MNP offers investors a truly ESG-compliant strategy, not just through the consistent integration of ESG in its investment process but also due to the scope and granularity of its ESG analysis, with hundreds of individual ESG factors being considered per company. Our opinion is supported by Morningstar’s sustainability rating for MNP, having ranked it as ‘high’. A high rating places it in the top 10% of Morningstar’s global equity large-cap peer group for sustainability, and MNP is also the only trust in the AIC Global sector to achieve this rating. MNP is in fact so sustainable that it ranks in the top 2% of the Morningstar peer group for this measure (the equivalent of being one of the top 100 most sustainable strategies in a universe of 6,700).



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