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[INTERVIEW]

Chris Salih (CS):

Hello, and welcome to the investing on the go podcast. I'm Chris Salih, and today we're here to talk all things UK with Charles Luke, manager of the Elite Rated Murray Income Trust. Thank for joining us again, Charles.

Charles Luke (CL):

Hi, Chris. Great to speak to you. Thank you for your time.

(CS):

Thank you. Let's start with a recap of the investment proposition of the Murray Income Trust, and maybe just talk to us about what you're trying to do and how it can help in a difficult environment like this.

(CL):

Yeah, sure. So, in short, Murray Income provides exposure to a diversified portfolio of high quality, mostly UK-listed companies, with a strong focus on ESG characteristics. The portfolio includes many interesting mid-size companies and some overseas-listed companies, all helping to deliver an attractive dividend yield. The company also benefits from the oversight of an experienced and independent board of directors.

In terms of how we're doing, I sort of like to think of that in two parts, given that we are an income fund. So, first the income and then capital. So, from an income perspective, income generation has been very robust. Our year end was June, and the income delivered by the portfolio has been well above pre-pandemic levels, which is well in advance of the market as a whole. So, doing well from an income perspective. And then, from a capital perspective, over the last six months, the portfolio has marginally outperformed its benchmark - the FTSE All Share Index - which is up a couple of percent or so.

(CS):

I mentioned the challenging backdrop we've got at the moment. Do you still believe the UK market is generally supportive for a number of reasons? Maybe just talk us through what you see in the market and whether there are opportunities in your segment?

(CL):

Well, as you know, as you say, it's certainly not difficult to be bearish [with the] cost of living crisis, concerns about global recession, the weak pound, high inflation, rising interest rates, you know, the list goes on. But what I would say, is the equity market is always looking ahead and these concerns I think are very well known, and to my mind actually largely reflected in the valuations of companies that we're seeing at the moment.

And I think it is important to remember that the UK market is not the same as the UK economy. The UK market is home to a wide variety of attractive global companies, and some very nimble mid-caps, so for me, it's not difficult to find companies with strong, intellectual property, well-known brands, all benefiting from good levels of corporate governance that are now actually trading at very sensible valuations. And just the sorts of companies that you want to own for the long term.

And together with that, you know, from a sort of income perspective as an income manager, the UK market has a very strong income culture and an attractive dividend yield. And that yield is higher than virtually every other regional equity market so, I think, you know, [there are] quite a number of reasons to be optimistic about the UK market.

(CS):

Okay. You mentioned mid-caps there, let's have a bit of a chat about that. I mean, I think we spoke about 15-16 months ago, and at the time you were sort of bullish on the UK mid-cap market. Is that still the case? Are you, I mean, they've had challenging times since then. Are you finding opportunities are even greater than they were then? Maybe just highlight a couple as well, please.

(CL):

Yep, so I mean, that certainly is the case. So, around 30% of the portfolio is invested in mid-cap companies. To give you sort of an example of a recent new holding, that would be Oxford Instruments, which is a mid-cap company with a market cap of around a billion pounds. It's a leading provider of scientific instrumentation equipment. It's got some really fantastic expertise in the company, some very strong customer relationships, high barriers to entry, and together with what I really like, is a very strong balance sheet as well. And that sort of epitomises the conservative nature in which the company is managed.

Another company would be Safestore, which has a market capitalisation of around 2 billion pounds. It's the UK's largest self-storage company but is also expanding in Europe. I think that's a great business because it has a well-known, trusted brand. Self-storage is a growing market. The company has significant marketing synergies from having the scale that it does. Its customers tend to be very sticky. The sites are very scarce and, in many cases, they typically actually have more value being used for other purposes, such as residential. And also, like actually Oxford instruments, it's got a fantastic management team, really laser-focused on returns. And it's just really a very uncomplicated business, so less things to go wrong. So, you know, Safestore is a couple of percent of the portfolio. So, one of the largest holdings.

(CS):

Okay. And obviously your style is to invest in sort of quality growth and more the opposite of value. Do you factor any economic headwinds or tailwinds into your decision when you are talking about making an investment in a company, and just go into that in a bit more detail as well?

(CL):

Yeah, sure. So, for me, it's really all about the companies. You know, macro factors can certainly have a big influence in the short term but forecasting those correctly is fraught with difficulty. And you sort of tend to find there's not always a smooth link between, or not necessarily a smooth link between those sort of macro factors and share price performance.

So, for me, you know as a bottom-up investor, it's about the companies and interestingly, if you look at the best performing companies in the UK market over the last 10 or 20 or 30 years, you'll see sort of really two things. So firstly, they come from a wide variety of different sectors. But secondly, nearly all of them actually have one thing in common, which is a high return on invested capital. And to maintain that high return on invested capital, they need some sort of sustainable competitive advantage, so that those returns aren't competed away or in other words, they're good quality companies.

And that's what reminds me of the quote attributed to Benjamin Graham, which is that in the short run, the market’s a voting machine, but in the long run, a weighing machine. So, my focus is really on finding or building a diversified portfolio of good quality companies, that we can hold for the long term, rather than worrying about the current or short-term macro vicissitudes.

(CS):

And given you said that though, a lot of your peers in the sort of growth, quality growth space, talking to them about what's been happening this year, we did see a very much sort of indiscriminate sell-off earlier this year. You've mentioned your focus is on the companies, but surely there were opportunities in that time period?

(CL):

Yep, absolutely. So, you know, we are always looking at good quality companies that potentially may have been a little bit expensive, but as you say, what we saw at the start of the year with discount rates rising and the sort of valuations for some of those quality growth companies that PE is falling, was the opportunity to add what we think are some really good quality companies to the portfolio.

So, one example would be London Stock Exchange which we added in the spring. That's a company that's been on a journey from a sort of traditional exchange towards being a global financial markets infrastructure and data provider. And that's been helped by the acquisition of a business called Refinitiv.

So, post the acquisition, approximately 70% of revenues for the London Stock Exchange Group come from providing data and analytics services where there is really strong structural demand. Those revenues are recurring, they're subscription-based, and that provides some really good resilience. And the cash generative nature of the business means that, actually the balance sheet - having been a little bit stretched post-Refinitive - is now strengthening really quickly. And I think that for a business like London Stock Exchange Group, where revenue growth can accelerate, the benefits of the acquisition are starting to come through, that can lead to the company becoming more valued as a really, really high quality leading information services company with the capability to deliver many years of strong growth to come.

And, you know, if the market is willing to depress the valuation from macro concerns, that's just an example of a really high-quality company that was a little bit expensive, but we were very happy to add to the portfolio and, and own to the next five or 10 years.

(CS):

When we talk to people about the UK and the sort of fears about the outlook, and I know you're not too focused on the outlook, it's all on the companies, but M&A activity must come onto the radar at some point for anyone including yourselves. Could you maybe just talk to us about whether you've seen that in the portfolio, and do you sort of extrapolate that into your outlook for companies, or is it just purely on a case-by-case basis?

(CL):

Yeah, so we have noticed that in the portfolio. So recently Schneider Electric announced they were considering making a bid for the part of Aveva, the software company that they don't own. Our holdings of HomeServe and Euromoney have been bid for by private equity in the last six months or so. A year ago, John Laing & Son which were also a holding were also bid for by private equity. And there have also being sort of plenty of rumors about other companies in the portfolio that are being looked at, either by other corporates or by private equity.

And, I guess, the sort of level of M&A activity in the portfolio isn't that surprising, particularly from private equity as you know, it's one group of buyers that have a lot of dry powder, the characteristics that they tend to look for dovetail with the sort of quality income strategy that we have in the portfolio, such as, you know, strong business model, a robust balance sheets, good long term growth opportunities. And you know, of course, valuations have come down to attractive levels as well. So, at the moment, I'd say a fair proportion of portfolio is probably vulnerable to M&A activity.

(CS):

Just to follow up on that. You used the word vulnerable, and you mentioned the valuations; as a fund, as a company or as a trust, do you actually push back if you feel that it's not the right thing to do?

(CL):

Yeah. Absolutely. We're interested in the long term. We're not interested in making a quick turn on the holding. So, if we feel, or if we think that the valuation from the bidder is too low, you know, we are very happy to make our views clear and vote against a deal if we really do believe that.

(CS):

You obviously just talked a bit there about your active involvement, let's turn to the ESG side. So, obviously the trust is a sustainable trust, and you'd look at ESG considerations and I believe you recently sold out a company based on an internal bullying culture. Could you maybe talk to us a bit, about how you go about that and how it pans out in terms of your approach to the portfolio?

(CL):

Yes, so ESG is very, very important in the way we manage the portfolio. And I think that's reflected in the Triple A MSCI ESG rating. So, we're always thinking about how a company manages its risks and opportunities and whether it's acting in the best long-term interest of shareholders and wider society. And I think we are very fortunate. We have a lot of expertise to help with our analysis. So, that includes a couple of ESG analysts on the team, and an overarching central ESG team with more than 30 experts.

In terms of the sort of shape and fit with ESG in the holdings, I should say that we do own a couple of oil companies, but that's on the basis that they're sort of best positioned for the energy transition, but we'll generally have only modest weights in the oil sector. We don't have any holdings at all in any tobacco companies in the portfolio. We don't think that sits comfortably at all with a focus on ESG, given how dangerous cigarettes are to their consumers.

You mentioned the sort of bullying example, that refers to Rio Tinto, and the publication earlier in the year of the independent Broderick report on workplace culture. And that made really sobering reading in terms of the sort of internal bullying at Rio Tinto, their sort of sexual harassment and racism. And we spent a lot of time engaging with the company but didn't think it was appropriate to maintain our holding in Rio Tinto, given the ESG concerns that there were very clearly highlighted in that report.

(CS):

Okay. Last question. I could end it on an optimistic or a pessimistic note, but I'm going to leave that to you. So, obviously things are challenging at the moment; we've got inflationary pressures, we've got the threat of recession, slower global growth. It is bleak. Are you as concerned as the headlines in the press would suggest, or do you not care and it's all about the companies? Maybe just give us your take on the next 12 to 18 months. Does the bleakness mean opportunities, or are you worried?

(CL):

Yeah, I mean, to be candid I'm not very good at short term outlooks and my sort of crystal ball is a bit sort of fuzzy at the moment, but what I would say is that I think it is really important to take a long-term perspective and actually next year, the trust will be a hundred years old and we'll also hopefully be celebrating its 50th consecutive year of dividend increases. And in that time, the portfolio's been through many difficult periods, but what will, I think continue to hold it in good stead is that focus on good quality, profitable companies with robust business models, strong balance sheets and sound growth opportunities because that really helps to insulate both the capital and the income from a more challenging environment.

(CS):

Thank you very much for joining us today, Charles.

(CL):

Thank you, Chris, and thank you everyone for listening.

(CS):

And if you'd like to learn more about the Murray Income Trust, please visit fundcalibre.com and while you’re there, remember to subscribe to the ‘Investing on the go’ podcast.

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