Sifting for gold

Our investment fund screening process

We are extremely disciplined when it comes to finding the right funds for investment.

Following your heart or your gut instincts can lead to all types of trouble in investing. That's why we leave sentiment out of the equation and focus on the cold, hard data when screening for fund opportunities.

There are literally thousands of different funds to choose from. Our asset allocation process narrows these down to a specific geographic area (like Japan) or theme (like technology) or other particular areas that could drive returns but with a close eye on risks. Using our systems we can then list all the possible candidates for consideration.

Then the data-crunching begins. This not only eliminates any emotional bias we may have from one fund manager to another but is also core to our evidence-based approach to investing. Indeed, the inclusion of all relevant candidates in the screening means we are agnostic as to whether the funds are actively managed, index-trackers, smart beta or any other portfolio type.

We use a custom screening process we have built from experience over time – it sifts through the data showing us which funds can produce the desired returns but also, crucially, the amount of risk they take. A wide range of factors are included such as looking at their track record throughout economic cycles, and asking how persistent is their performance or are they a flash in the pan?

The screening process spits out our shortlist, and then we roll up our sleeves.

The funds from the list will be divided up across the investment team and the detailed due diligence process begins. There are a number of elements to this: a full analysis of the fund; research into how it has performed in different market and economic conditions in the past; meetings or conference calls with the fund managers to understand their approach and a request for a list of the current holdings.

That last request might seem like a mundane piece of box-ticking but it is pivotal to the whole process.

By lifting the lid and seeing what is actually held in the fund we can determine if it really does what it says on the tin. Using our systems, we can not only track and monitor our existing fund holdings, but will combine the data on any proposed new assets with our existing holdings to see what the new blend looks like – have we suddenly inadvertently increased the exposure to something? Increased diversification? Reduced environmental ratings? Reduced liquidity?

Indeed, we can run scenarios on the data (such as a re-run of the credit crisis) to get an insight into how the new and combined assets may behave should the same happen again.

It was an early version of this system that was used to scrutinise the original investment in the Woodford UK Equity Income Fund in 2015 but which raised a number of red flags in 2017 that led to us to divest of the fund in August of that year.

This rigorous testing of the data and understanding of the fund manager's process and philosophy is essential. Only once we have this information will we have a sufficient picture to sit down as a team and thoroughly challenge the proposed new fund from a 360˚ viewpoint to decide whether it is right for our clients.

Foresight UK Infrastructure Income Fund – Power Play

In his book focusing on climate change and environmental conservation, *There Is No Planet B*, published last year, Mike Berners-Lee stated that "we desperately need investment in the following: Renewable energy, particularly solar, and the accompanying technologies to store and distribute electricity…".

Clearly, he is writing from a perspective beyond the sphere of pure investing, but the greater demand for renewable energy and the improving economics of solar energy (even without government subsidies) led us to look into this area at the start of 2019. We had established a portion of the portfolio for infrastructure, such as railways and toll roads, two years prior and we considered adding to this position given it was ripe with opportunity.

Our screening process kicked up a number of candidates and we reviewed them all. The problem we found was that many managers lacked the track record, or were 'wildcatting' with risky, unproven technologies, or had too wide a definition of infrastructure.

Since 2017, Foresight has managed the UK Infrastructure Income Fund which looks to derive a steady income (it targets a 5% yield) from investing in investment trust companies specialising in infrastructure. Not all of it is renewables but we believe they know what they are doing when selecting where their investors' money goes.

They have deep and broad experience in this field – funds managed by Foresight include the ownership of more than 100 solar projects around the world, 22 onshore wind projects, 35 bioenergy and waste facilities in the UK and Europe and 22 reserve power assets. Together their projects have a generating capacity of over 2.0 gigawatts, enough clean renewable electricity to power a city the size of Newcastle. In addition, they invest in wider renewable infrastructure markets including battery storage and smart metering.

With the focus on deriving returns from income, rather than capital gains this has avoided many of the speculative projects and only investments which have strong enough cash generation to pay cash dividends qualify for inclusion. This shows up nicely in the volatility figures for the fund which, at 4.7%, are less than half those of the FTSE All Share Index of 11.5% since the inception of the fund.

We are pleased to report that the fund has performed well since inclusion into our portfolios and is not only fulfilling our investment objectives but also playing its part in funding cleaner energy for the future.