Global Value and Income Dispatch

A fund for all seasons (and other reasons)

What is the role of the JOHCM Global Income Builder Fund within an individual's overall investment portfolio?

We believe the fund can be a useful tool for long-term saving across a range of investment scenarios. It aims to preserve and grow capital while also generating a stable income stream over long time horizons and different market environments. Flexibility is central to our benchmark-agnostic approach. Our team can move across sectors, asset classes and global financial markets in search of the best individual investment opportunities available. This flexibility is protected by our commitment to capacity discipline and intention to restrict asset growth within the strategy above $10 billion. Beyond this level, we believe allocation fund managers like us may lose their ability to make material investments in smaller equity and credit opportunities. And they may generally compromise their ability to make portfolio adjustments in a timely and efficient way, either to seize opportunities or, more importantly, to protect capital.

Exploiting Mr. Market and his moods from the bottom up

We are value investors. That means we are sensitive to price. Ben Graham, the founder of value investing, famously described "Mr. Market" as a fickle individual, prone to rather wild mood swings. What he is willing to pay for a security varies from one day to the next. These mood swings sometimes – but often don't – properly reflect genuine shifts in the intrinsic value of the underlying business.

Our job as managers is to locate when and where margin of safety – the gap between Mr. Market's current view and our assessment of the long-term value of a business – expands and contracts and invest accordingly. Unlike top-down managers who make broad calls on the economy or an asset class, we perform this function security by security. And we use our freedom to move across global financial markets in this never-ending pursuit.

How to use this fund – part 1

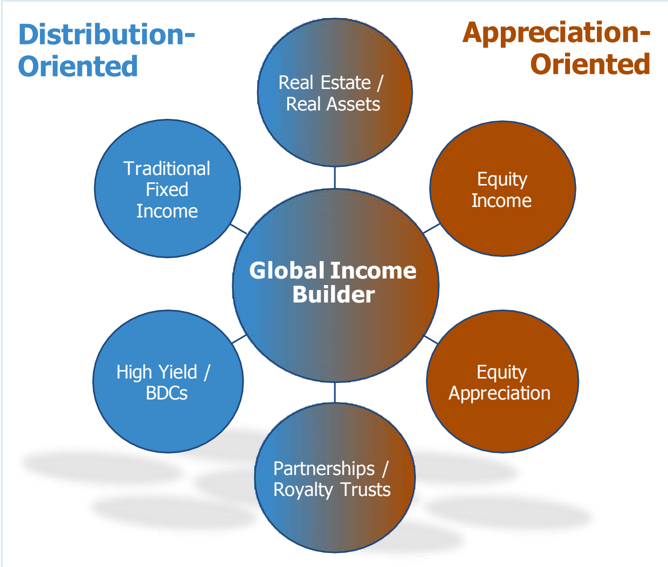
As a core multi-asset fund

We designed the fund to function much like an endowment for individual investors. We also sought to create a vehicle that would be sufficiently diversified and balanced across asset classes and risk factors, so that a prudent investor could, at least in principle, have all their long-term savings in the fund if necessary. Indeed, as managers, we hold a significant chunk of our personal savings in the fund.

Endowments, whether for a university or a charitable foundation, are pools of capital established to provide financial support to institutions indefinitely. In the U.S., the IRS requires private foundations to pay out five percent of the value of their funds annually to maintain tax-free status. The challenge facing an endowment manager is how to deliver this five percent every year without shortening the lifespan of the capital base. This problem is made worse by inflation, which eats away at the value of the fund in real terms over time.

Many individual investors, especially those whose investment focus has moved from growing their capital towards needing regular income, e.g. those retired or nearing retirement, find themselves in a similar predicament. To meet the potential income needs of our investors, we seek to maintain a diversified portfolio of equity and fixed income securities that will, over time, generate a meaningful level of distributable income without sacrificing real long-term portfolio growth. In particular, we believe our specific capabilities in international equities (where dividend yields are generally higher than in the U.S.) and high yield credit are especially helpful for achieving our income objectives.

What does a level of distributable income that is compatible with real long-term portfolio growth look like in practice? Given our current estimates of potential expected returns across asset classes, we view this sustainable level as three to four percent net of fees. This figure may change over time as market conditions evolve.



Dry powder

Like most endowment managers, we appreciate the long- term benefit of being invested in risk assets, albeit in a highly selective way. We never try and time the market; we see that as speculation that can have painful consequences. But we do maintain a portion of our portfolio (typically five to fifteen percent) as our reserve buying power. This usually consists of cash, government bonds and gold-related investments. These reserve funds serve as a source of liquidity to take advantage of market environments in which margin of safety opportunities become more abundant and compelling. These will often be periods of increased risk aversion and negative market sentiment.

With a portion of total return anchored by investments that generate predictable cash returns, consistent exposure to what we view as the best value opportunities in durable businesses in equity and fixed income markets, and the ability to invest in riskier assets when prices become especially favorable, we argue the fund can be viewed as *an active core holding for the long term*. Individuals and their advisors can then use other instruments (such as specialized funds or ETFs) as satellite investments to adjust for risk and income preferences, or to gain exposure to specific market opportunities.

How to use this fund – part 2
A conservative alternative to global equity funds

The fund can also be seen as a lower volatility alternative to global equity funds. We expect the equity exposure to range from 40-65%. The level of equity exposure will generally be a function of the availability of margin of safety opportunities. We will typically raise equity exposure in environments when risk appetite is waning and decrease it in environments where investors are more complacent or even exuberant. We believe this preference for putting capital to work in 'risk off' scenarios, while paring back our exposure in 'risk on' scenarios, may contribute over time to better downside capture performance and risk-adjusted returns relative to strategies that are fully invested in equities at all times.

The fund's exposure to high yield corporate credit also lends itself to the 'conservative equity' use case. Though different from equities in their contractual nature, seniority in the capital structure and limited upside potential, high yield bonds are like equities in many respects. Similar to equities, high yield instruments are fundamentally claims upon the cash generating power of the businesses to which they belong. Historically, high yield bonds have exhibited lower volatility than the stock market, while generating total returns substantially higher than fixed income alternatives. While not properly speaking equity, we believe the high yield component of our fund may offer a return profile that could be attractive to more cautious equity-oriented investors.

A differentiated approach for income portfolios

We think our emphasis on investing with a margin of safety coupled with global perspective distinguishes us from other income-oriented funds.

In many cases, income funds have a tendency to skew towards U.S. dividend stocks which tend to be narrowly clustered in a few sectors – see the August 2018 'Global Value and Income Dispatch: 'Looking for income? Three reasons to go global' for a more detailed look at this topic. And some income funds rely heavily on investment vehicles carrying substantial debt (such as mortgage REITs or infrastructure funds) or present significant duration (interest rate) risk, perhaps because of high exposure to "bond proxy" equities or a high allocation to long-dated investment grade debt.

By emphasizing international opportunities, balance sheet strength and free cash generation, while avoiding investments which we think involve excessive and under- compensated interest rate risk, the fund can potentially improve and diversify income-oriented portfolios. Furthermore, our opportunistic investments in more eclectic securities, including small/mid-cap global equities and smaller credit issues, are likely to be complementary to the holdings of other income funds.