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The magazine for FINANCIAL PLANNING PROFESSIONALS

MONEY & LIFE

A SPECIAL CONTRARIAN INVESTMENT SUPPLEMENT

PATIENCE:

THE KEY TO LONG-TERM SUCCESS

Understanding the finer points of contrarian investing

FINANCIAL PLANNING ASSOCIATION *of* AUSTRALIA

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moneyandlife.com.au
fpa.com.au

Level 6, Suite 603, 55 Clarence Street, Sydney NSW 2000
T 02 9220 4500 | **F** 02 9220 4580 | **E** fpa@fpa.com.au

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Paper+ Spark

Paper + Spark P.O. Box 443, Pyrmont NSW 2009

EDITORIAL TEAM
Jayson Forrest, Miriam Fine
editor@paperandspark.com.au

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PUBLISHER
Zeina Khodr
M +61 414 375 371
E zeina@paperandspark.com.au

ADVERTISING
Suma Wiggins
M +61 404 118 729
E suma@paperandspark.com.au

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FOREWORD

It's not easy being a contrarian investor. By definition, you're buying shares that most people are selling and selling shares that most people are buying. Constantly going against the crowd can feel extremely uncomfortable. It requires a strong level of conviction in your analysis and investment process.

I've worked for Allan Gray for over 20 years, starting in South Africa then coming to Australia to help grow the retail business for the last 12 years. Although I'd previously worked at a number of financial service businesses over time, there's a good reason why I've stayed at Allan Gray for so long. This is a company that lives and breathes its contrarian investment philosophy. Every fund we manage uses the contrarian investment strategy at their core – we focus solely on what we are good at. I've never worked anywhere quite like Allan Gray.

Why have we used a contrarian investment philosophy for almost 50 years? Quite simply for the potential to outperform. Not only does contrarian investing provide much-needed diversification to your client portfolios, as we actively look to invest against current market trends, it also increases the chance of upside as we're buying shares that we believe are well below their intrinsic value.

In a world where many fund managers are increasingly unable (or afraid) to stray too far from the index, it's more important than ever to differentiate your client portfolios if you want the opportunity to outperform.

Our contrarian approach is not about being different for the sake of it, but driven by performance and a desire to succeed. To seek better-than-average returns, you need independent thinking. You can't just follow the herd.

After all, if you invest in the same way as everyone else, you can't expect a different result.

The following guide explains what contrarian investing is and how it works in practice. We hope you can gain greater insights into this fascinating investment strategy and how you can use it with your clients in the quest for better results.

JD DE LANGE
CHIEF OPERATING OFFICER
ALLAN GRAY AUSTRALIA

CONTRARIAN INVESTING: MORE THAN AN INVESTMENT PHILOSOPHY

What exactly is contrarian investing, and how should financial planners consider this approach when constructing portfolios for clients?

Warren Buffett famously said: "Be fearful when others are greedy, and greedy when others are fearful." This quote beautifully sums up his patient, long-term approach to investing.

Buffett's success has largely been built on an investment approach that goes against current market trends, which at its simplest, is what contrarian investing is all about.

As its name suggests, contrarian investing is an investment philosophy and approach to investing in which investors purposefully go against prevailing market trends by selling when others are buying and buying when most investors are selling. It is a disciplined, long-term approach to investing, requiring patience.

By going against popular trends and avoiding following the crowd, contrarian investing can result in very meaningful differences in portfolio holdings, potentially delivering investors better returns than the broader market over the long term. Why? Because if you buy and sell the same shares as the majority of investors at the same time, it is almost impossible to outperform the market.

"It's an approach that tends to exhibit deeper value characteristics, but is not exclusively value in style. The main focus with contrarian investing is on valuation and buying companies at prices that are significantly less than their intrinsic value," says Julian Morrison – Investment Specialist at Allan Gray.

According to Julian, investment opportunities often occur when companies are experiencing challenges or problems, and it's these challenges that cause investors to become fearful. This fear can result in investors selling, which drives down the price, making the stocks attractive to long-term, contrarian investors.

INDEPENDENT THINKING

As an investment manager with a pedigree in contrarian investing spanning almost 50 years globally and 17 years in Australia, Allan Gray believes that to be a contrarian investor means more than simply going against all current market trends. Some stocks have fallen out of favour for good reason. To uncover the right opportunities, independent thinking and research is vital for investors to form their own view that is unconnected to the prevailing market consensus.

Allan Gray remains wholeheartedly contrarian in its approach to investing. It maintains a highly focused approach to investing that allows it to keep it simple by offering investors a choice of just three funds: the Allan Gray Australia Equity Fund, the Allan Gray Australia Balanced Fund, and the Allan Gray Australia Stable Fund (see pages 14-15).

According to Julian, Allan Gray's approach to contrarian investing is built on never trying to guess external sentiments, the next share price movement, or market trends. Instead, it scrutinises opportunities that aren't necessarily obvious.

It does this by searching for value in companies that others have overlooked or undervalued. It then determines the things that drive the company's performance and create value over the next five to 10 years.

"As opposed to managers that exhibit a strict value bias, contrarian investors may also find value in companies where their future growth prospects are not being rewarded by the market, or perhaps where companies are not well covered by the market and limited research on them is available," Julian says. "These are the types of companies and opportunities contrarians are looking for."

AN APPROACH WORTH CONSIDERATION

When considering whether contrarian investing is right for your clients, there are a number of important factors to examine. Here is a rundown of some of the risks and rewards with this approach to investing.

By going against the herd and popular trends in the market, contrarian investing will often lead investors to companies that are unloved and overlooked by the market. This can not only improve the diversification qualities of a portfolio, but potentially also deliver better than average returns over time. It can also avoid overpaying for a company, which can be one of the largest risks that investors face with their investment selection.

But financial planners need to understand the features of contrarian investing. Like any approach to investing, it has its pros and cons. And while there are inherent risks involved, the upside can see investors perform well over the long-term. Here are some key aspects of contrarian investing that financial planners need to consider.

> *"When buying a company that is unloved and out of favour, you need to be willing to take comfort in discomfort when investing differently from the herd... You need to avoid behavioural biases and emotion that may impact the investment decision-making process and trust your fundamental research."*

UPSIDE

- **Potential for outperformance:** Because you are investing against the herd, a contrarian approach improves your chance of paying a lower price for an investment and, therefore, the opportunity for greater returns.
- **Avoid overpriced investments:** It helps you to avoid speculative overoptimism. When stock prices have risen too high, it increases the risk of overpaying. If you are willing to look in areas of the market that are unpopular with investors, you are more likely to find bargains.
- **Independent thinking:** Contrarian investing enables you to form your own views of stocks that is separate to the prevailing market consensus.
- **Market bubbles:** By investing independently of general market sentiment, contrarian investing can potentially help investors avoid market bubbles, like the dot-com bubble.
- **Portfolio diversification:** A contrarian fund often holds unpopular stocks that have been discarded by the market. This can bring exposure to stocks that the average investor may not otherwise have exposure to, providing greater portfolio diversification.

DOWNSIDE

- **Patience is required:** It can often take a long time for a stock's value to be recognised and for it to be rerated by the market. A successful contrarian investor needs patience.
- **Long-term:** Contrarian investing is long-term in nature. This means investors need to take on a 'business owner' mentality, not a 'share trader' mentality. You need to approach investing in a company as if you were buying the entire business, not just looking to trade a few shares in that business. Approaching an investment with a business owner mindset gives the investor a deeper understanding of how a business operates, not just a view on the next short-term share price movement, which can be incredibly difficult to predict.
- **Uncomfortable:** When buying a company that is unloved and out of favour, you need to be willing to take comfort in discomfort when investing differently from the herd. At extreme points in the cycle, you can feel uncomfortable and look like you've made a bad decision, but you need to be confident in your decision and stay the course. You need to avoid behavioural biases and emotion that may impact the investment decision-making process and trust your fundamental research.

COUNTER-INTUITIVE

The nature of contrarian investing means investors often own companies that are unpopular and, at times, receive less favourable coverage in the media. For many investors, it's difficult to own businesses of this nature, particularly when their share prices are under pressure. To buy when everyone else is selling is much easier said than done.

This makes contrarian investing counterintuitive from a behavioural perspective, as it requires a strong and disciplined approach to investing.

"So, in effect, contrarian managers do what many investors know they should be doing, but find it too difficult to do," says Julian. "Adopting a contrarian approach will invariably lead to a very different looking portfolio, but one that's focused on the preservation of capital and long-term outperformance."

THINK DIFFERENTLY

There's no doubt that contrarian investing is a very different approach to more traditional investing, as it allows access to a part of the market that represents great opportunity from a valuation perspective, potentially providing better-than-average results over the long-term, as well as portfolio diversification.

However, it is important for financial planners to understand that this is a long-term approach to investing, requiring discipline and patience from the investor.

"It's difficult being different," says Julian. "Philosophically, financial planners need to understand that this is a sound and logical way of investing. By doing so, it will assist them and their clients to stay the course through difficult patches."

ASKING THE RIGHT QUESTIONS

Contrarian investing may not be suitable for every client, and depends largely on an investor's risk appetite, time horizon and patience.

To ascertain whether this investment approach is right for your clients, there are a number of key questions that financial planners need to ask.

1. ARE YOU AIMING TO ACHIEVE A BETTER THAN AVERAGE RETURN?

One of the aspects of contrarian investing is you are actively taking a stance that is different to the market. If investors have a desire to outperform the market, they can't do the same thing as everyone else and expect a better than average return. Contrarian investing requires going against prevailing market trends, selling when others are buying, and buying when others are selling, in order to outperform.

2. ARE YOU WILLING TO GO AGAINST THE HERD?

If you are buying a company that is out of favour with the consensus, you need to be willing to take comfort in discomfort. That doesn't mean that all positions that are contrarian have to be uncomfortable for the investor, but investors need to be comfortable with being different from the herd.

One of the main errors investors make is to look at what other people are doing, like friends and family, and follow them.

While popular opinion might be useful when choosing a movie to watch or a restaurant to eat at, it's certainly not good to follow the herd when investing. This is because when stocks become popular with investors, competition to buy increases and stocks can become overbought. This pushes the price higher, leaving you paying more, which detracts from the future return of that investment.

3. ARE YOU IN IT FOR THE LONG-TERM?

As an investor, how patient are you with your investments? Are you willing to wait a little longer for your investments to outperform the market? Are you prepared to see through a period of underperformance?

When it comes to investing, patience is one of the few qualities that provides an investor with an edge in the market. Many investors are looking to 'make a quick buck', but it may take time for a contrarian investment thesis to play out. Everybody has access to the same, publicly available information, which means human behavioural errors can lead to opportunities.

"Behavioural errors tend to persist over time," says Julian. "These include confirmation bias, where you look for information that confirms your existing view, but ignore evidence that contradicts this view. Or recency bias, where we believe recent events will have greater bearing on stocks than is likely in future These behavioural biases tend to lean towards the error of impulsiveness and impatience.

"To be a contrarian investor, you need to be patient, disciplined, and willing to invest for the long-term."

SECTION 03

THE BIG 5

Did you know one of the common myths about contrarian investing is that it's simply value investing? Well, it's actually a lot more than that. Let's take a look at some common myths and aspects of contrarian investing you probably didn't know about.

> *"If you buy and sell the same shares as the majority of investors, at the same time, it is by definition almost impossible to outperform the market... The complications don't come from the philosophy, but from human instinct. While it's easy to say you will invest against the crowd, putting it into practice goes against human nature and requires the utmost courage of your convictions."*

1 CONTRARIAN INVESTING IS JUST VALUE INVESTING

One of the biggest myths surrounding contrarian investing is that it's simply value investing.

Value stocks are often considered to be those with a low price to earnings (P/E) ratio, which measures a company's current share price in relation to its current earnings per share. It helps investors to compare the relative value of different companies. A high P/E ratio could mean a stock is overvalued, or that investors are expecting higher growth rates in the future. Conversely, a low P/E ratio could mean the company is undervalued.

But a contrarian investor doesn't always invest in companies with a low current P/E ratio. In fact, a contrarian will sometimes invest in companies that appear to have a high P/E ratio, based on current earnings.

But why would investors do this? The reason is that the 'E' (earnings) may have collapsed in the short-term. However, long-term, normalised earnings may be much higher than current depressed earnings. Therefore, the normalised P/E ratio may actually be much lower.

2 CONTRARIAN INVESTORS NEED A CATALYST

Another myth is that contrarian investors must predict a catalyst that will trigger an earnings turnaround and a rise in the share price, but this is rarely the case.

Much like economic forecasting, catalysts are exceptionally difficult to predict. For example, market expectations for a company's earnings may be terrible and this will be priced into the stock. But if the company's actual earnings are only 'bad', and not 'terrible', the stock beats the market's expectations and the share price rises.

Contrarian investors don't need to predict a catalyst to trigger an improvement. The stock just needs to beat market expectations and investors can do well.

Importantly, contrarian investors assess situations where there has been negative overreaction, which can make a stock highly sensitive to future positive developments

3 CONTRARIAN INVESTING ONLY PERFORMS AT CERTAIN POINTS IN THE CYCLE

Different investment styles tend to outperform at different points in the market cycle. Investment managers with a growth bias tend to outperform when markets are rising and economies are strong, given their focus on expected future earnings. Value investors tend to outperform during periods of uncertainty, given their focus on businesses with typically attractive valuations versus the market.

Conversely, contrarian investing could outperform in many market environments. That's because contrarians select stocks based on potential upside and opportunity, not because they fit into a preconceived value or growth investment style. Contrarian investors can own growth stocks, or value stocks, or any combination, depending on where they find opportunities. Also, due to the highly selective stock picking nature of contrarian investing, managers may invest in companies that are bucking their sector's trend and therefore, perform independently.

By not pigeonholing themselves into an investment style, contrarian managers increase the potential for outperformance through the market cycle.

4 CONTRARIAN INVESTING INCREASES RISK

Contrary to popular belief, contrarian investing can potentially reduce risk in a portfolio.

For example, given the propensity to invest in out of favour stocks, contrarians are often aiming to buy stocks at the bottom of the cycle; ideally, there isn't much further for prices to fall. Minimising losses is arguably more important than maximising returns for the long-term investor.

Perhaps the most important focus is on buying stocks below fair value. This avoids overpaying and the risk of permanent loss of capital.

Diversification should be the cornerstone of even the most basic investment portfolio. Having your portfolio allocated to several different sectors, companies, and asset classes, vastly reduces the probability of losing a major amount of capital in a short time.

A contrarian strategy can provide exposure to stocks that the average investor may not hold, providing greater portfolio diversification than the average managed fund or an index tracker.

5 CONTRARIAN INVESTING IS COMPLICATED

Contrarian investing doesn't need to be complicated, in fact, the premise is simple – you need to assess the true value of the company and based on that true value, buy shares when others are selling and to sell when others are buying.

If you buy and sell the same shares as the majority of investors, at the same time, it is by definition almost impossible to outperform the market.

The complications don't come from the philosophy, but from human instinct. While it's easy to say you will invest against the crowd, putting it into practice goes against human nature and requires the utmost courage of your convictions.

INVESTING FOR THE LONG HAUL

How do you apply contrarian investing consistently for the long-term, particularly in a low return and inflationary environment? It's a good question, so read on.

Allan Gray believes the secret to successful investing rests with three key components: being contrarian; having a long-term view; and analysing company fundamentals. Let's take a look at all three.

1. BEING CONTRARIAN

To gain a competitive edge in a market where every investor has access to the same information, do not follow the crowd. Contrarians resist trends, instead, seeking to uncover opportunities in places that the market has overlooked or undervalued. This requires independent thinking, as some shares will have been discarded by the market for good reason.

2. LONG-TERM VIEW

In an increasingly competitive market, exercising patience can give you a distinct advantage. By waiting for the right opportunity to buy and giving an investment time for its value to develop and be recognised by the market, you may discover enormous potential for an undervalued company.

3. COMPANY FUNDAMENTALS

Seek out companies that are out of favour and wait for an opportunity to buy their shares at a price well below their value. You can do that by studying a company's fundamentals and then calculate what you believe to be its true value.

Julian explains: "Some financial planners may embrace the contrarian philosophy as wholeheartedly as Allan Gray, either using fund managers or buying shares directly. Other financial planners like to use contrarian investing as a diversification tool that complements other investments in the portfolio, or even other styles of investing, like momentum or growth, that planners might want to pursue."

He adds that using contrarian investing in a diversified portfolio is a good complement to other styles of investing, as certain investments and sectors are likely to 'fire off' at different times. This enables the investor to generate alpha, or outperformance, from different stocks at different times.

"And it can potentially dampen the negative effects of other investments when you combine contrarian investing in a portfolio," says Julian.

DIFFERENT APPROACHES TO PORTFOLIO CONSTRUCTION

Typically, financial planners constructing a portfolio with contrarian investments take one of two approaches.

The first and most common approach is to build a well-diversified portfolio, with different types of strategies and styles. This means that over the long-term, through different market cycles, investors have different parts of the portfolio working for them.

The second approach is to try and better understand the market environment. Financial planners can then allocate more capital to strategies they think will outperform by reducing exposure to strategies they believe will underperform. This approach is riskier, as it relies on the financial planner making the right calls, but also offers the potential for higher returns if those calls are right.

Contrarian investing can fit into each of these strategies, either as one of the investment styles in a diversified portfolio, or to play a more prominent part in a portfolio that uses a more active asset allocation. The major caveat here would be that history shows that consistently making the right call at the right time is nearly impossible.

"With contrarian investing, investors need to understand that there will be periods where their investments will underperform the market. They need to be patient, because this is a different type of strategy, but it's definitely a complementary approach to other strategies," says Julian.

THE ALLAN GRAY WAY

When it comes to contrarian investing, the approach Allan Gray takes to stock selection begins with an assessment of the company's true value, with the aim of investing when the price is well below this value.

This increases the likelihood that potential risks are already in the price, reducing future risk and increasing return potential. The manager then looks to sell the security when it reaches its assessment of its true value.

You can see Allan Gray's investment strategy illustrated clearly in the graph on page 11, which shows how it invests through a share's investment cycle.

According to Julian, when Allan Gray first buys a security, the price may continue to fall. That's because the

manager is buying at a time of negative sentiment, when news about the stock often gets worse before it gets better. Allan Gray views this stage of investment selection as an opportunity.

"If the price continues to fall but our thesis remains intact, this is a great chance to buy more of the stock at a lower price, increasing our anticipated gain if and when the price rises," says Julian.

"When the price rises and sentiment improves, it may reach or even exceed our assessment of its value. This is the ideal time for us to sell, as there are usually plenty of willing buyers in the market making it easier for us to sell the security."

A LOW RETURN ENVIRONMENT

It can be challenging for financial planners to invest in a low return environment, with the risk of rising inflation. However, those market conditions can also provide significant opportunities for contrarian investors.

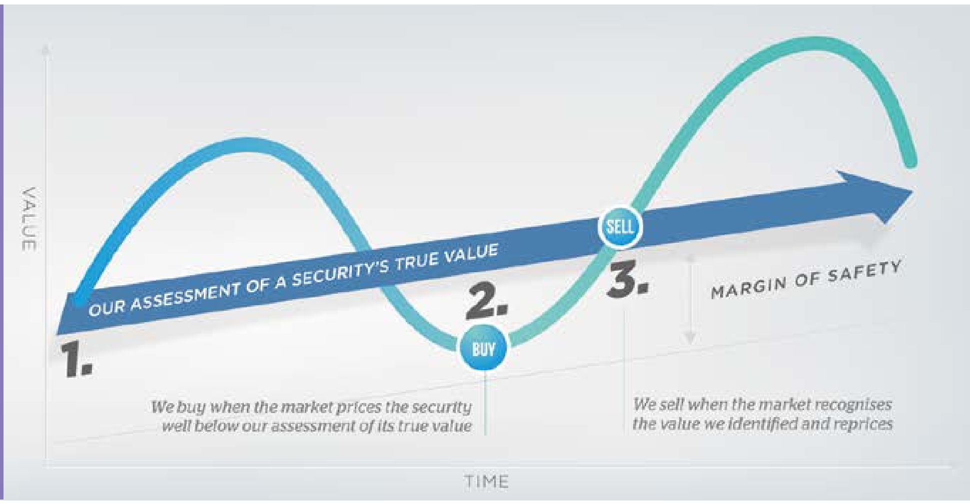
Both in Australia and globally, some of the stocks that are currently out of favour and have dropped in price over recent years are in sectors that are cyclically challenged and may benefit from rising prices. Julian points, for example, to some of the materials companies that extract or produce products and services that are linked to the underlying price of a commodity.

"Allan Gray often finds value in sectors that have been in, or are going through, a tough period, which is not to say we buy them all," says Julian. "As it applies to commodity companies, this often occurs when the dynamics of supply and demand lead to a change in the price of commodities, where profitability declines and capital investment dries up. Here, sentiment is often weak and opportunities may arise."

In addition, this means in times of rising inflation, energy and materials companies may be the beneficiaries of this. They are also the types of companies that can add considerable diversification to a portfolio, including the potential for outperformance.

"In a low return environment with the risk of rising inflation, this sort of contrarian approach will result in a very different portfolio, compared to the average Australian equities fund," says Julian. "But it's this variation that means contrarian investing can make a meaningful difference to an investor's returns over the long-term."

HOW CONTRARIAN INVESTING WORKS



CONTRARIAN INVESTING IN THE REAL WORLD

Contrarian investing provides a great way to diversify your clients' portfolios and manage their risk, however, it requires a long-term focus, patience, and good communication skills. Here we talk with two financial planners about their experiences.

MICHAEL CONNICK CFP®

PINNACLE FINANCIAL PLANNING

SENIOR FINANCIAL PLANNER & PARTNER

Michael Connick CFP® is a Senior Financial Planner and Partner at Pinnacle Financial Planning. Michael has been a financial planner for 26 years, with the past 16 years leading the financial planning practice for Pinnacle. Michael explains Pinnacle's approach to contrarian investing.

"Pinnacle Financial Planning was an early adopter of Allan Gray Australia and we've been working with them for the past 11 years. At Pinnacle, we use an active, concentrated approach and look to blend complementary managers within each investment sector. We choose to include Allan Gray in our clients' portfolios as it provides significant diversification away from the 'crowd'.

"Allan Gray is one of five Australian equities managers we currently use. We find the benefits to our clients are we can avoid the portfolio replication present in many other traditional Australian equity managers. Contrarian investing brings real diversification benefits to our clients.

"When it comes to incorporating Allan Gray into our client portfolios, we use it with a large majority of our clients - between 70-75 per cent would have some Allan Gray exposure in their portfolio.

"The percentage allocation within our clients' portfolio would range between 4-6 per cent, and within the Australian shares sleeve this range is between 15-20 per cent of the total domestic equity exposure. The percentage of a client's portfolio is based on their risk profile, with more conservative clients sitting at about 4 per cent and clients who are more open to risk, at the higher range of 6 per cent. This allocation to Allan Gray in a portfolio is used across all investment stages, regardless of whether a client is in the accumulation, wealth creation or retirement phase.

"Investing in Allan Gray needs to be carefully explained to clients and we do this at the beginning of all client relationships. It is definitely a longer term strategy of approximately 7-10 years, as opposed to other managers who might target a 5-7 year cycle. It is important to explain that with Allan Gray investors can expect to have greater swings and periods of uncomfortable underperformance. Being patient and sticking with the long-term investment strategy has delivered the expected results for our clients over the last 11 years.

"We do see an increase in questions from clients when Allan Gray has been underperforming for a period of time. In those times it is important to reiterate the long-term nature of an investment in Allan Gray and the patience required if the fund continues to underperform. This can be tolerated where the investment strategy matches the client's risk profile and investment time horizon so careful consideration of these factors should be undertaken upfront. It is also important that clients understand the importance of staying invested so they don't miss the potential upswing when it comes.

"Given our history with Allan Gray, we are fortunate to have had a long-standing relationship with them and we have direct access to the portfolio manager. We have seen first-hand the benefits of contrarian investing when the market cycle and/or investor sentiment changes and how this has provided a meaningful contribution to the overall performance of our Australian equites sleeve.

"For financial planners using managed funds and considering investing in a contrarian fund, my advice is to look at the existing managers you use in the Australian equities sector and look at the level of stock replication across the underlying securities. Investing in Allan Gray helps reduce this and offers access to parts of the market that are simply not offered by most other managers. As a result, Contrarian investing may improve diversification benefits to your current client portfolios."

"We currently use five to six different managers, including growth and value managers, in our Australian share portfolio. Planning Partners added contrarian investing to our portfolio of funds about 10 years ago.

"Since we started in 1999, we have always had value funds on our recommended list. It's an investment strategy that we can get behind. Contrarian investing, while similar to value investing, can provide an extra level of diversification.

"For myself, I include Allan Gray in my clients' portfolios because of the opportunity it provides for diversification with an aim to reduce some risk. And the benefit to our clients is that contrarian investing tries to provide for investment returns to be smoothed out over the long run.

"When it comes to including Allan Gray in our clients' portfolios, we use it with the majority of our clients. From an allocation perspective, Allan Gray will make up between 10-20 per cent of the portfolio for the Australian equities allocation.

"We do find that experienced clients with a good investment knowledge have a better understanding of contrarian investing. Those clients who prefer to move with the market can sometimes struggle to understand what a contrarian manager is doing, especially in periods of very strong markets and if the contrarian fund is experiencing a period of underperformance. Also, very conservative clients are sometimes not suited to a contrarian fund.

"As with any investment decision you make for your clients, it needs to be explained, and contrarian investing is no different. It's important that we educate our clients on why we use the fund, and with contrarian investing, we spend time with the client setting expectations around what the fund can do. However, in saying that, we don't get a lot of questions from our clients, and I put that down to our good relationship with them and the immense trust they have in us for what we are doing and the advice we are providing them.

"The only time we see questions or concerns around contrarian investing is when performance has been poor against the market. In this instance, we remind them that the purpose of a contrarian fund is to be very different to the general market and when the time is right, they could see the benefits of being in a contrarian fund that aims to outperform over the long-term.

"I also like that Allan Gray is actively involved with the management of the companies it invests in, which is another benefit to our clients.

"For those financial planners considering contrarian investing it's important to educate your clients on what a growth manager and a contrarian manager does and set expectations for both."

For the right investor, Allan Gray can provide clients with greater diversification for their Managed Fund portfolios. It is however a long-term investment strategy that takes patience and a disciplined approach to maximise the benefits of this style of investing.

PETER BAILEY CFP®

PLANNING PARTNERS

FINANCIAL PLANNER & CHIEF INVESTMENT OFFICER

Peter Bailey CFP® is a Financial Planner and the Chief Investment Officer of Planning Partners. Peter provides his insights on contrarian investing.

ARE YOU READY TO SHUN THE HERD?

Investors can take advantage of Allan Gray's distinctive contrarian philosophy, which seeks to take a contrarian approach, apply it consistently, and invest for the long-term.

> "With an established global pedigree spanning almost 50 years, it maintains a highly focused investment approach that allows it to keep investing simple by offering investors a choice of just three funds: the Allan Gray Australia Equity Fund (the Equity Fund), the Allan Gray Australia Balanced Fund (the Balanced Fund), and the Allan Gray Australia Stable Fund (the Stable Fund) – together, the Allan Gray Funds."

For any financial planner considering implementing a contrarian investing strategy, it's important they first properly understand the underlying philosophy of the contrarian fund manager and its approach to investing.

As a fund manager, Allan Gray remains wholeheartedly contrarian in its investment approach.

With an established global pedigree spanning almost 50 years, it maintains a highly focused investment approach that allows it to keep investing simple by offering investors a choice of just three funds: the Allan Gray Australia Equity Fund (the Equity Fund), the Allan Gray Australia Balanced Fund (the Balanced Fund), and the Allan Gray Australia Stable Fund (the Stable Fund) – together, the Allan Gray Funds.

THE ALLAN GRAY DIFFERENCE

Let's take a look at the three Allan Gray Funds.

ALLAN GRAY AUSTRALIA EQUITY FUND

The Equity Fund is an actively managed fund that aims to create wealth by buying undervalued Australian shares with a view to profiting when the price rises.

The Equity Fund seeks to provide a long-term return that exceeds the S&P/ASX 300 Accumulation Index. Constant monitoring allows the investment mix to be adjusted to maximise opportunities as they arise.

Because Allan Gray chooses shares that are often overlooked by other investors, the Equity Fund looks very different to other Australian equity funds and can be an effective way to diversify your portfolio.

You can choose from two unit classes, each with its own fee structure: Class A, with a base fee and performance fee, and Class B, with no base fee but a higher performance fee based on the returns you make.

ALLAN GRAY AUSTRALIA BALANCED FUND

In carrying out Allan Gray's contrarian investment approach, the Balanced Fund has significant freedom to invest in different asset classes to take advantage of the best opportunities. This means the manager has great flexibility and can capitalise when markets are cheap.

The Balanced Fund's target range is to have anything between 40%-90% of the Balanced Fund invested in shares, 10%-50% in fixed income and cash, and 0%-10% in commodity-linked instruments, depending on where the opportunities are.

Generally, a significant proportion (around 60%) of the Balanced Fund's portfolio is expected to be invested in Australian assets, with the remainder in international assets.

As a result, the Balanced Fund can look very different to other funds of its kind, as the investment mix is based on finding the best value.

For example, when Australian shares are expensive, more of the Balanced Fund may be invested in global shares. The same applies for other asset classes and regions.

ALLAN GRAY AUSTRALIA STABLE FUND

The Stable Fund is a more conservative investment that aims to outperform cash and boost returns by blending cash with selected Australian shares.It aims to provide a long-term return that exceeds the RBA's cash rate, with less volatility than the Australian sharemarket.

The Stable Fund starts with at least 50% of its portfolio invested in cash and money market instruments. The remainder is invested in carefully selected Australian shares when the opportunity arises. The Stable Fund aims to outperform cash over the long-term, but with less volatility than the sharemarket.

Using the same contrarian philosophy as all the Allan Gray Funds, the Stable Fund buys shares when they are undervalued and therefore, a good opportunity, with the aim of benefiting when their value is recognised.

A DISTINCTIVE TAKE ON INVESTING

Each of the Allan Gray Funds allow investors to take advantage of Allan Gray's established contrarian philosophy, while providing investors with investment options that suit a variety of needs.

"Our distinctive take on investing means that each of our funds brings something very different to an investor's portfolio," says Julian. "We select investments that are often undervalued and overlooked, but with the potential to increase in value over the long-term. It is this approach that helps investors earn the higher long-term returns that Allan Gray aims to deliver."

There's no doubt that contrarian investing is a very different approach to more traditional investing. It allows access to a part of the market that represents great opportunity from a valuation perspective, potentially providing better-than-average results over the long-term, as well as portfolio diversification.

However, it is important for financial planners to understand that this is a long-term approach to investing, requiring discipline and patience from the investor.

"It's difficult being different," says Julian. "Philosophically, planners need to understand that this is a sound and logical way of investing. By doing so, it will assist them and their clients to stay the course through difficult patches."

However, he adds that financial planners need to remember that contrarian investing means there can be periods of short-term underperformance, requiring restraint and patience from investors.

"Going against human instinct and taking a contrarian approach to investing is not always easy. It can be challenging, and requires patience and commitment in your convictions.

"There aren't many managers that invest the way we do, so our portfolios can look very different. And while it's not always easy to be different, for those who are willing to shun the herd, the rewards can be great."

Isn't it time you discovered the Allan Gray difference? To learn more about how a contrarian approach can help your clients with their investment needs, go to: allangray.com.au or call 1300 604 604.

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