Feeling uncomfortable can help to unlock value

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It's no secret that value investing has been out of favour for some time.

Funds not willing to chase the tech rally have broadly underperformed the market and many value managers left behind have been forced to explain poor performance quarter after quarter.



Michael Goldberg's Collins St Value Fund was among the best performing funds last year. **Arsineh Houspian**

But Collins St Value Fund is doing something different.

The fund placed third in the Mercer survey of investment manager performance, beaten only by a long-short fund started in May 2019 and a growth fund with overweight holdings in the market's highest fliers, including Xero, Afterpay, Domino's Pizza and CSL.

"I think what differentiates us is that we manage a concentrated portfolio of our favourite ideas," says fund principal Michael Goldberg.

"We're not compelled to buy something because it makes up a large portion of the stock market, and we're not diluting our favourite ideas with our 15th or 20th favourite idea. We're just buying our favourite stocks."

The fund made a return of 13.5 per cent through 2019-20 compared with the S&P/ASX 200 Index which fell 7.7 per cent.

"Over the last 12 months it's been exceptional and 70 per cent of the stocks we've owned over the last year went up, in a market that was down more than 7 per cent," says Goldberg.

"We're not getting it right every time, but we're spending all the time we can to get that informational advantage and ensure we're not taking risks we don't understand."

The company runs a high conviction concentrated portfolio, holding on average between 10 and 15 stocks at any given time.

There's a disconnect between the way people feel about a company and what they know. Between those two lines lies a lot of opportunity.

— Michael Goldberg

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"We're running our own race," he says. "We spend so much time working on the stocks we end up buying, looking for that information advantage, finding those businesses that are most attractive to us, and I've never really understood why people are so eager to diversify their exposure away from their best ideas."

And Goldberg's best ideas are largely unique.

The fund's best-performing stocks in the last 12 months have been Black Cat Syndicate, Paradigm Biopharmaceuticals, and Lotus Energy, stocks unlikely to be found in most manager's portfolios.

Black Cat, an $89 million gold explorer, made a 200 per cent return in the last 12 months, helping to drive the portfolio's strong returns.

"We didn't go out to buy Black Cat," says Goldberg. "In 2019 we started thinking about more insurance against a crazy world might be a good idea, so we started to invest in some gold stocks.

"We bought a number of companies to make up our basket of gold stocks. We were looking for mines with great prospects across different ranges and stages of production. Black Cat was one of those investments."

An uncomfortable investment

The fund's high exposure to uranium stocks has also proved fruitful, with $53 million Lotus Energy rising 75 per cent in the last 12 months.

"We never thought we'd invest in something like uranium," says Goldberg, who said the idea came from a broker who they had asked to pitch an investment he liked but felt uncomfortable telling clients.

"He sent us some videos and some research and we realised this was a commodity trading at a massive discount to the cost of production.

"We decided to create out own ETF because there was none in Australia to get exposure to uranium stocks. We arranged them by balance sheet strength and on that basis we allocated weightings. Obviously over time, we've come to understand the sector and the management team."

It's an investment that is still yet to fully pay off the fund, though.

"We actually perfectly picked the bottom of the uranium market, but unfortunately for us the uranium companies haven't quite done so well," says Goldberg.

"If you want to compare market caps in the sector last time uranium was at this price, you'd have a tripling of share prices."



Michael Goldberg says the fund holds a basket of gold and uranium stocks.
Arsineh Houspian

Another of the fund's key positions has been Paradigm Biopharmaceuticals, a company re-purposing the drug pentosan polysulfate sodium for the treatment of inflammation.

Goldberg said the fund took an early bet on the company when it was in phase two trials. While trials were still ongoing, a number of real-life patients were being treated with the drug in advance under the government's special access scheme.

"It didn't make sense to us because the phase two trial had 240 patients but there were 500 people being practically treated with this thing and the company was making the market aware of what those results were," he says.

"We spoke to patients, brokers, doctors, and the market was just waiting, when we knew it worked. Even though we were taking a risk, we were very confident at that point when it worked, so when they did a capital raising two years ago, we actually cornerstoned it.

"I think there's a disconnect between the way people feel about a company and what they know. Between those two lines lies a lot of opportunity. People knew that it worked but they didn't feel comfortable until the clinical trial results came out."

Goldberg believes many investors can be too emotional when it comes to investing, pointing to his investment in Alinta, a company that fell out of favour due to its ownership by Babcock & Brown, a highly leveraged investment vehicle that went into administration in the wake of the global financial crisis.

"[Alinta] were winding up the business and they were going to hold on to just one power station. At the time they were trading at about 9¢ and they said their distribution was going to be 10¢," says Goldberg.

"For a two-week investment, you could buy a 10¢ distribution plus a power station that would be worth something, for 9.5¢. So we bought quite a lot of that. It seems like pretty simple maths, but as soon as you mentioned it was Babcock & Brown Power, people just didn't care, they just didn't want to own the brand."

Getting comfortable with investments others feel uncomfortable with has proved to be a winning strategy for the fund, which has made a 15.7 per cent annualised return since inception in February 2016.

"Sometimes doing those things that are a little bit uncomfortable, because no one else likes to be uncomfortable, can generate massive opportunity," says Goldberg.

"It's there if you go and grab it, but it's not always comfortable to go grab it."

Primary school hustle

Goldberg's passion for investing and entrepreneurship came early on.

"I think it was grade six where I might have partook in my first arbitrage trade and in terms of return on investment, I think it was the best one I ever made," he says.



Goldberg says he has always had an entrepreneurial spirit. **Arsineh Houspian**

"We stumbled upon boxes of cricket cards at a $2 shop and we were confident we could sell each set for way more than $2. So we bought three boxes, collected the sets, went to the local card shop and promptly sold them for $9.

"We went back to the $2 shop and bought out the rest of the stock."

A few years later he was given shares in CSR, and by high school, had bought shares in NAB.

"I didn't fully grasp what it meant to own stocks but I knew I owned a part of the business, so every time mum went to the shops, she had to buy the CSR sugar," he says.

"I went to Caulfield Grammar School and they had chapel a few times a week, but being an Orthodox Jew, I was the first person to be dispensated from going to chapel. For that 15 to 20 minutes I used to go and check what my National Australia Bank shares were doing.

"It's cool to feel like you own a part of this business, but I realised there was a disparity between what the wider world knew about these companies and what you could know if you really put in the effort to find out about these companies."

While many investors in the last few years have topped the Mercer charts due to their exposure to tech stocks, Goldberg hasn't gone anywhere near it for his returns.

"Would I have liked to have bought Afterpay at $8 and now it's sitting on $60? Of course I would. But I could never see myself taking a punt on them at $8," he says.

"The buy now, pay later sector - they legitimately could be an industry that replaces credit cards - but even if that is the case, how do you value this thing? If you want to value them on the basis of their earnings you're a million miles away from anything that could be considered value."

Goldberg also believes it is unreasonable that some value investors have been chastised for not chasing the returns in the sector.

"The market will do what the market will do. I don't think it's fair, in a market that's being driven by technology, to people who aren't playing in that space to expect them to match the market. It's just unreasonable," he says.

"It's going to be a challenge for a value investor to outperform the market when markets are being overly exuberant. That's just not where value investors will shine.

"I'm bearish about the market going forward and I think in bear markets you'll see the value investors seriously outperform."

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