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OWNING THE FUTURE

Geoff Wilson, chair, Wilson Asset Management

Wilson Asset Management chair Geoff Wilson talks about his investment philosophy, going all the way back to reading the "numbers page" in his father's newspaper. **Alex Burke** writes.

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The young Geoff Wilson was watching his father reading the newspaper when he noticed something odd – something that, arguably, was the catalyst for his entire career.

His father – a doctor by trade – would often spend what seemed like an inordinate amount of time scanning one page in the paper. "The one with all the numbers," Wilson recalls. After asking his dad about it, Wilson realised he was reading share prices. He'd already become acquainted with the idea earlier on, when his grandfather passed and the estate offered his father either cash or shares in a mining company.

"It puzzled me that he'd spend so much time reading that page," Wilson says. "So I asked him why, and he effectively explained how the stock market works."

Wilson scanned the page to find something he could afford, and saw Cox Brothers, a Victorian retailer, trading for one cent. Becoming more interested in what his father had told him, Wilson checked back later on and found it had fallen to half a cent, then went back up to one: "I thought, 'Jeez, if I'd bought it at half a cent and sold it at one cent, I'd have made 100% of my money!'"

That was his first lesson. The second came later, when he looked for Cox Brothers again in the paper and couldn't find it. "I asked my dad," he says. "I didn't understand where it had gone. He told me it had gone under – it was a high-end retailer, but it didn't last."

These two ideas – that the ongoing valuation of a company could make you money, and that it was important to understand how a company worked to ensure a quality investment – would eventually become some of the founding principles of the WAM Capital listed investment company, now worth over $1 billion in assets.

Several years after Cox Brothers disappeared from the "numbers page," Wilson was at university, studying chemistry and mathematics. His father gave him some money and told him to buy shares – he looked for the cheapest one he could find, Timor Oil and Gas, which was trading at 10c a share.

He remembers: "I thought to myself, 'If it goes up to 12c, I make 20% of my money.' So I bought $1000 worth. It went to 12c, I sold half, and wasn't even aware that they were drilling for oil somewhere at the time. The share price kept going up – to 35c. My first investment! I thought, 'How good is this?'"

After finishing university, trained as an industrial chemist, Wilson started looking for work. But after visiting a friend who was working at Rowntree-Hoadley – named for Australian hero Abel Hoadley, inventor of the Violet Crumble – he realised he didn't want a career testing chocolate bars.

Having taken on a number of roles, Wilson ultimately found himself working in the investment team at life insurer Scottish Amicable. In the early '80s, institutional investment wasn't as prominent in the Australian market, but Scottish Amicable had come in with $70 million.

The quote

You're not just placing a bet when you buy a stock – you're becoming a part-owner of that business.

The process of working out where to invest this kind of money taught Wilson his third – and possibly most important – lesson about what it meant to be a fund manager.

"I started off thinking of the stock market as a racetrack," he says, "except that in this case, you could bet on a horse and cash out halfway through if your horse isn't doing so well, or is doing well enough. I later realised that when you invest, you're not just placing a bet – you're becoming a part-owner of that business. It was important to do the hard yards, meet the companies, understand how the management operated. And if it's a bad business, do you really want to be a part-owner of it?"

Wilson stayed at Scottish Amicable for two years, visiting knitting mills and liaising with managing directors, before taking on a Sydney-based industrial analyst role in 1982 at broking house Potter Partners, which was later acquired by UBS. His goal at the time was to work in Sydney, London and New York – having ticked off one, he moved onto an institutional sales position in London, where he learned yet another lesson about investing: in this case, market anomalies, market dynamics and human behaviour.

This lesson involved pubs. And bombs.

"If you go forward to September 11," he says, "you'll see how the markets fell significantly after that happened. But fortunately or unfortunately, as human beings, we adapt. And I'd already learned this in London in the '80s, when the IRA was bombing the pubs. When the first pub blew up, no one went to the pub for a week. When the second pub blew up, no one went for a day.

"When the third pub blew up – well, you just began to think of it as a risk of going to the pub. This gradual adaptation plays a huge role in market booms and busts."

Having come out favourably in the pub death risk/return curve, Wilson ticked off his last box – New York – by taking on a role at McIntosh Hamson Hoare Govett (now Merrill Lynch Australia) over the '86-87 crash. He then moved back to Australia with the same firm, took nine months off to travel the country with his girlfriend (now wife), and returned to the industry with Prudential-Bache, the investment subsidiary of insurer Prudential Financial. He stayed there for eight years until shortly after his 40th birthday.

"I had a four-year-old daughter at the time," Wilson says, "and I decided I wanted to have breakfast with her in the morning."

One of Prudential's clients at the time was RG Capital, the investment business owned by media magnate Reg Grundy which would later be acquired by Macquarie. Having made his decision to spend more time with his daughter, Wilson spoke with RG Capital's then-chief executive Tim Hughes about his plans for the future.

"I told him I wanted to run my own funds management business," he says. "He said, 'Well, if you want to, we'll back you and commit $10 million.'"

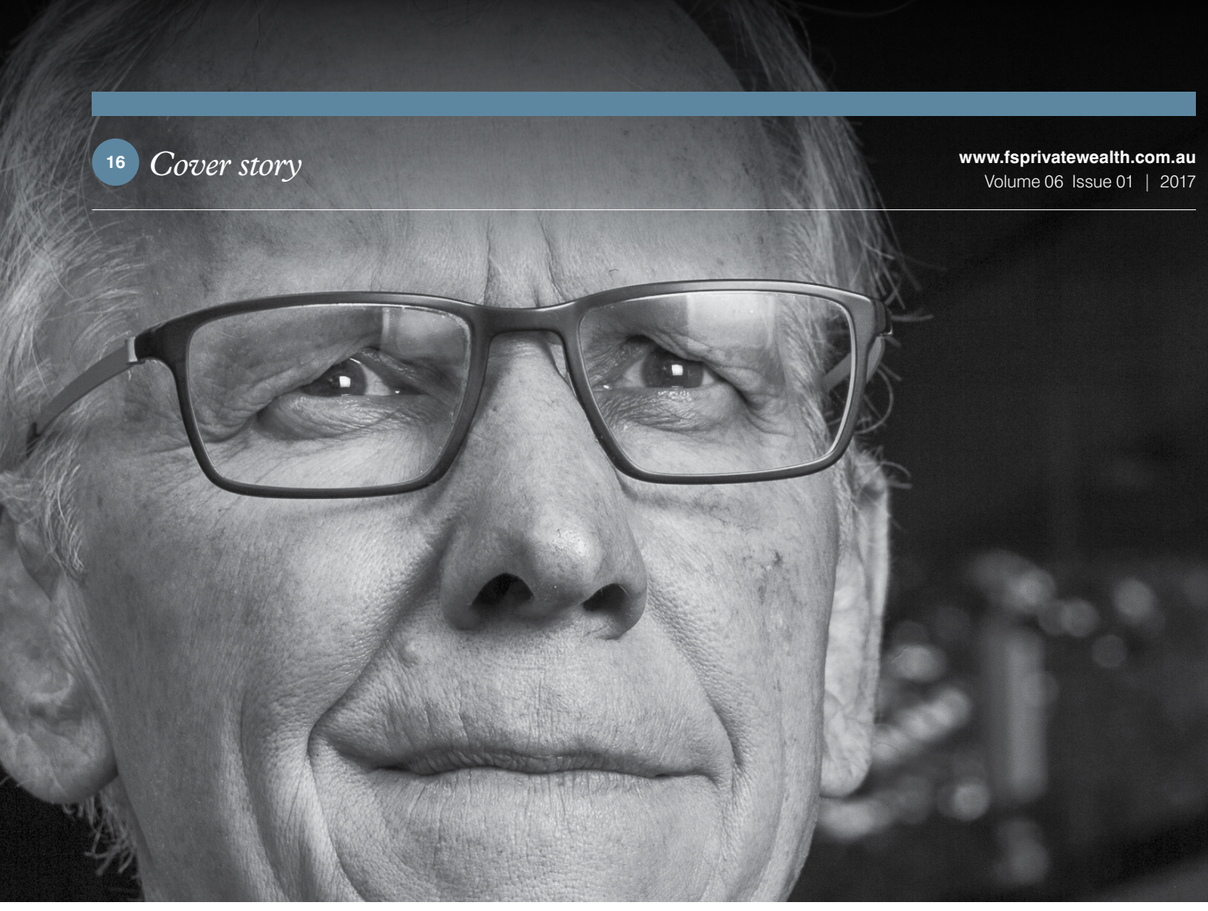
Recognising the opportunity, Wilson established Wilson Asset Management in 1997. He had half a million of his own money to put into the nascent WAM Equity Fund – the same fund upon which WAM Capital is based – and asked Hughes for the $10 million: "He said, 'How much are you putting in?' I told him $500,000, and he said, 'Okay, we'll put in $500,000 too.'"

The fund started with $1 million in 1998, and in the first year was up roughly 56% - further flows came in, but initially it was "very slow," according to Wilson. The fund performed even better in the second year, though, and in the 19 years since inception, it's only underperformed in two.

"The way I saw it," Wilson says, "running the fund was very much like managing your own personal money. Rule number one? Don't lose money. Rule number two? Don't lose money. Rule number

The quote

Rule number one? Don't lose money. Rule number two? Don't lose money.



three? You get the idea. A lot of people manage their money on a relative basis; we manage it on an absolute basis. We're not trying to 'beat the market': we don't want to lose a cent.

"Our default position is to hold cash. We can hold 100% cash if we need to. And we won't buy a company unless we're convinced we'll make money. Convinced. And that's partly because, personally, I started with half of all the cash in the fund and I didn't want to lose any of it."

The strategy for investing in companies flows on from those aforementioned lessons, albeit implemented in a far more complex and labour-intensive way. To Wilson, the most important correlation between a share price and anything else in the company is growth in earnings per share. He says: "A lot of companies will talk return on equity or cash flow, in the old days maybe assets, perhaps dividend yield – for us, it's about EPS growth. Those other things are important, but EPS is paramount.

"When we meet the management team, it's important to understand how they make money. Because it's only when you do that that you can forecast what their profits will be. We also look at how the company funds itself. Do I want to be a part-owner of this company? Do I think it's a great business? Do I believe the management are honest, high-quality managers?"

After answering those questions, WAM then looks at valuation and market catalysts. "We won't just buy a stock and then hope it gets re-rated," he says. "We'll sit in cash while other people might hold that company. We need to identify some kind of event that is going to affect valuation, whether that's an earnings surprise, some other change in the business, or something even broader."

Like, for example, September 11. During the GFC, the fund was up to 70% cash, but after the terrorist attacks in 2001, it was fully invested. While recognising the tragedy of the situation, Wilson notes "it's the kind of time you can buy a dollar of assets for 50c."

WAM Capital had listed two years before that. The fund itself had a stable of high-net-worth/family office wholesale investors, but now it was open to retail as well. "A lot of investors from those early days are still there," Wilson says. "Our first couple of years were quite extraordinary. But even then, when we floated WAM Capital, I honestly thought I'd be lucky to raise $5-6 million. The absolute maximum, which I never thought we'd get, was $20 million. Well, we ended up being oversubscribed."

The LIC is now capitalised at $1.4 billion.

WAM has since launched three other LICs –WAM Leaders, WAM Research and WAM Active – which apply the same fundamental philosophies to investing Wilson accrued since reading his father's newspaper. During that time, he's become cognisant of his reputation as an activist investor – especially in light of involvement in management shake-ups at, say, the AMP Capital China Growth Fund, Templeton Global Growth Fund and, most recently, Hunter Hall Global Value following Hunter Hall chief investment officer Peter Hall's surprise resignation.

He denies the charge, saying these so-called activist positions are fundamentally driven by the goal of preserving investors' money – investors in his funds and theirs. "When you invest in a company," he says, "you're fundamentally trusting in the management. You're giving them your money and you have to trust they'll make the right decisions with that business. Pretty early on I learned that lesson. It's the same with funds management – people give us money and they believe we will do the right thing with it. They trust we're buying shares in companies that are managed by people we trust, and when that trust breaks down, you have to find a way to extract yourself from that situation in a way that represents the best interests of your investors."

The quote

We won't buy a company unless we're convinced we'll make money. Convinced.

If Wilson isn't an activist in his investment behaviour, though, he certainly is when it comes to philanthropic activities. Inspired by his wife's involvement in children's welfare through their private ancillary fund, Wilson came upon a new approach to philanthropy – through a LIC structure.

"I was in the UK about five years ago," he says, "and I saw a gentleman named Tom Henderson raising money for a company called Battle Against Cancer Investment Trust, or BACIT. He ended up getting it to around £400 billion. His concept was to get fund managers to manage money, pro bono and give 1% of the money to charity. It seemed like a phenomenal structure to me."

He decided he wanted to launch a similar vehicle in Australia, now known as the Future Generation Investment Fund. Once again, he wasn't confident in how much money this unusual type of charitable fund would raise. "I thought we'd be lucky to hit $20 million," he says. "So we used the Australian Infrastructure Fund, which had wound down and had about $3 million left.

"We put in a new board and allowed people to get out at NTA, which is the right thing to do" – here, he doesn't try to disguise referencing his ongoing proposal for the board of Hunter Hall Global Value to do the same thing – "and then raised the money for the Future Generation LIC, where 1% of the proceeds goes to children at risk charities. We had a maximum of $200 million, I didn't think we'd get close, started our roadshow in Perth and before the issue closed we were oversubscribed to the tune of $300 million."

He describes Future Generation as a "win for fund managers, because even though they're managing money for free, but they're in a good group with a good profile. It's a win for the investor, because they don't pay a management or performance fee. And it's a win for the charities, because they get annuities."

Future Generation was successful enough that Wilson started getting requests to launch a global vehicle, a proposition he found exhausting at the time. When he was offered help, though, he was able to launch Future Generation Global and raise $302 million – this time with the 1% going to youth mental health charities.

> You want to invest in the future. You want youth safety, and you want mental fitness. Because that leads to high productivity.

When discussing the importance of youth mental health, Wilson characteristically frames it from an investment perspective. "Think about it," he says. "That's what you want to invest in. You want to invest in the future. You want youth safety, and you want mental fitness. Because that leads to high productivity. If we can stop just one person committing suicide I'd consider that a success, but obviously our goal is a lot bigger than that. And to me, this investment vehicle is the perfect structure for that."

Viewing these charitable initiatives through the lens of investment management may seem unusually utilitarian, but to Wilson it makes perfect sense. It's not a racetrack, after all. He's a part-owner: both in businesses and the future. FS