KENNOX
TRUE VALUE INVESTORS

QUARTERLY INVESTMENT REPORT

September 2024

Kennox has had an improved time over the last three years. Over this period the Fund is a touch ahead of global markets, up 35%[1] and 32%[2] respectively, but without having owned any of the oh-so-fashionable Magnificent 7 stocks (or anything like them). Let's consider this performance in the context of three of the top-performing stocks for Kennox in the period – the three "S"s: Stella International, Shell and Singapore Telecom (Singtel).

We have written about Stella in these commentaries in the past, scratching our heads at the time as to why it was completely ignored by the market – yielding up to 12% for around eighteen months, with dividends well covered by robust free cash flows, a pristine balance sheet featuring net cash, and even with growing earnings. Eventually, the market cottoned on, and the share price moved up significantly starting in the summer 2023.

Shell had fallen significantly out of favour due to the energy price disruption of the pandemic blended with the market chasing an overly simplified ESG narrative. The shares subsequently recovered on the back of Shell's prodigious cash flows and the pragmatic realisation that their products, however flawed, are for now essential to the smooth functioning of the global economy.

Lastly, Singtel has excellent communication franchises across Asia – in Singapore, Australia, Thailand, Indonesia and the Philippines – providing services that its customers essentially believe they cannot live without. Singtel was severely overlooked as the market chased sexier names in the space such as the Googles & Apples of this world. Singtel also has a hidden-in-plain-sight jewel in the form of its chunky holding in India's Bharti Airtel.

What is interesting is not just how different these stocks are from each other and to the hot sectors of the last few years, it is also that the performance for each didn't come from the market's belief they would transform the world. Instead, the performance came simply as they were too cheap relative to their robust businesses. The portfolio continues to consist of a range of these types of opportunities, and we relish this form of pragmatic investing – the opposite of thrilling but inherently durable, and repeatable.

This led us to think about some obvious pitfalls for all investors to watch out for. Let's look at a few examples.

First is not taking enough risk – think of the person who sits on a bank savings account indefinitely. If an investor is holding a bit of cash as a reserve for a rainy day, great. If an investor holds all their long-term savings in cash for decades, it's horrendous. Even with low consumer price inflation since the 1990s, the buying power of cash has been decimated over twenty or more years.

The second is to continuously chase the hottest fad. There are many investors who are drawn like the proverbial moth to a beguiling theme featuring a wonderful narrative and stellar recent performance.

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[1] Source: Bloomberg. 3-year total return to 30 September 2024 for A Class Accumulation shares
[2] Source: Bloomberg. 3-year performance to 30 September 2024. MSCI World Index, +32.3%; MSCI World Value Index +33.7%

At that point, too often the theme is closer to the top than to the bottom. Morningstar has written on this issue, looking at the average investor in the ARK Innovation fund, pointing out that they have tended to buy after great performance, and sell after terrible performance, locking in poor results (see this article here). This means the average investor has had a horrible experience, suffering painful losses in contrast to ARK's still good long-term performance. Timing markets is possible, but goodness it's not easy, and chasing hot and volatile themes needs special care and attention.

Third is finding out that all one's investments end up being highly correlated. 2022 is a good example – practically nothing of what performed well up to 2022 was then able to perform again in that difficult year. Whilst appearing different at first impression, too many investors discovered to their dismay that most or all their investments were all pointed in the same direction.

Kennox isn't for everyone, but we can certainly mitigate against the three hazards listed above. First, we know from experience that even difficult markets can be managed with a comprehensible but effective process, risk-focussed and differentiated, income-paying and balanced, holding and thinking for the long term. Even a risk-averse investor could get on board with this. On the second, Kennox's philosophy rests on the opposite of chasing the hot themes and momentum trades, finding high-quality companies that are out of favour due to temporary headwinds and holding until tailwinds return. Powered by this dynamic and different to what has driven the market in the last decade (see the graph on page 2 of the quarterly commentary of December 2023 here), value investing as practiced by Kennox continuing to offer genuine diversification to almost all investors, a counterbalance for the third pitfall.

Investors need to continue to assess the key issues that markets currently face. Will wars in the Middle East and in Eastern Europe fade or explode? What are the chances of an all-out trade war with China (or an actual one, for that matter)? Will the global economy painlessly flip back to low and stable inflation or has the inflation regime substantially changed? Is there too much complacency around leverage and the financialization of the economy? Is the safety of running with the herd increasing or decreasing the chance of a painful outcome?

One of the most interesting issues is one expressed recently by Cliff Asness (co-founder of AQR Capital Management), who believes that the market is less efficient than at any other time in his career dating back three decades and counting. He assesses three possible reasons: indexing, cheap money, or, most likely according to him, to technologies such as social media. Whatever the reason, if correct this has big implications for society, as misallocating capital on a wide scale has large real-world implications. More pertinently for investments, this could hamstring the backward-looking or otherwise unaware investor. (The paper can be found here).

These issues are threats, but also opportunities for those able to identify and seize them. Kennox feels especially well positioned in this – operating a sensible strategy underpinned by robust businesses overlooked in the market, with an awareness of obvious pitfalls, and lastly maintaining an independent outlook clearly focussed on the long term and on the most attractive opportunities on offer at any time.

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If you have any questions on Kennox or the Kennox Strategic Value Fund, please contact us on +44 (0) 131 563 5440 or email at clients@kennox.co.uk. Our website is www.kennox.co.uk

Fund Data – 30 September 2024

Performance (total return net of fees) in Pounds Sterling

PERIOD	SHARE CLASS	
	CLASS I	CLASS A
YTD	10.1%	10.3%
2023	8.0%	8.2%
2022	12.6%	12.9%
2021	10.1%	10.5%
2020	-11.1%	-10.9%
2019	4.8%	5.1%
2018	-2.2%	-2.0%
2017	2.5%	2.6%
2016	35.8%	36.2%
2015	-4.0%	-3.8%
2014	-1.1%	-0.9%
2013	15%	4.3%*
2012	10%	N/A
2011	-4.0%	N/A
2010	12%*	N/A
2009	N/A	N/A

Source: Kennox. Performance figures are total return generated from the accumulation units since their launch (29 April 2013), and from the income shares prior to that. * Share classes launched mid-year: Class I on 12 May 2010; and Class A on 29 April 2013.

Top 10 Holdings

STOCK	REGION	SECTOR	MARKET CAP (US$M)	WEIGHT (%)
NEWMONT CORP	N. America	Materials	61,500	7.9
STELLA INTERNATIONAL	Asia	Consumer Discretionary	1,500	7.5
SHELL	UK	Energy	202,000	6.1
SINGAPORE TELECOM	Asia	Communication Services	41,500	5.4
AGNICO EAGLE MINES	N. America	Materials	40,000	5.2
FUKUDA DENSHI	Japan	Health Care	2,000	5.2
CANON MARKETING	Japan	Information Technology	3,500	4.3
YOUNGONE HOLDINGS	Asia	Consumer Discretionary	1,000	4.1
YUE YUEN	Asia	Consumer Discretionary	3,000	3.5
STAR MICRONICS	Japan	Industrials	600	3.5
TOTAL TOP 10				**52.6**
20 OTHER HOLDINGS				46.5
CASH				0.9

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