Buffettology fund interview – why I love a market crash

[Start of recorded material at 00:00:08]

Interviewer: Hello. With me today I have Keith Ashworth-Lord, manager of the Sanford DeLand UK Buffettology Fund. Hello, Keith. Thanks for joining us.

Keith Ashworth-Lord: Hi.

Interviewer: Now, it's been one of the most eventful periods in stock market history, and that's to put it lightly. The market's fallen sharply. Private investors are wondering "is the market going to go any lower and is this company still good value? Should I be looking at it, should I dismiss it?" I mean, what assumptions are you currently using as a basis for your investment decisions. I mean, your process will be well-honed, but if I mean if you worry about the market lurching lower or do you say "no, I know this is a good company"? How do you do that?

Keith: Well, first of all I never worry about what the market's going to do. The market will do what it will do. From a personal angle, there feels to be a bit of a disconnect between the recovery in prices we've seen and the external circumstances in the economy. I just can't quite square that in my mind at the moment, so it wouldn't surprise me if we had another lurch down at some point. It depends – when the coronavirus news is bad, down goes the market. Then the Fed steps in and you know the old adage "don't bet against the Fed", but markets don't. So they all correlate and go up at that point. It's really a very strange situation, but you know, every bear market plays out the same in the end and the secret, I think – I really do think this is the survivor's guide to bear markets, as I said – is that you average down, you buy on the bad days when the market really has a thunk, those are the days when you should venture forth but don't try and do everything at once. Keep powder dry.

It's almost like pound cost averaging down, because sure as eggs are eggs, when you're buying into a fall, the week after you always look a fool. You know, you buy in and then you'll think "why did I do that last week? I could have done it this week" and the secret I think is just to bide your time, commit capital in a steady way, unless you see something that's an absolute screamer – first-class company selling at a knockdown price, in which case you might want to just go and take a holding and pump 30 million into it there and then. But by and large, my approach is always a patient one. It's trying not to react to events but actually predict in the sense that how will I respond to this if this happens?

And I can honestly tell you, I mean, my broker friends think I'm nuts. I love it on days when the market is absolutely smashed because the first thing I do is start looking at prices against things that I'm interested in. That's the time to be buying, not on days like today when the market's sort of had one of its periodic bounces up, and we've had enough of those over the last few weeks. In bear markets you do get exceptionally strong rallies and it doesn't always mark the bottom. They can just lurch back down. So that's my survivor's guide in my fifth bear market, or if you include the LTCM thing in '98 and the small one in '89 it's actually my seventh bear market, so I'm getting a bit used to them.

Interviewer: You mentioned earlier about the consumer-facing businesses and we talked about that because I'd seen in your last sort of comment to shareholders, you said "the older I get, the less enamoured with consumer-facing businesses I become". So you've touched on that already with Next, but I was just wondering, does this – I mean, it clearly does, I imagine. I was going to say will this impact the fund's approach in future?

Keith: I think it will. I think it will sanitise us more away from that type of business. I mean, I'm not saying every consumer business is bad. I mean, we own Games Workshop. You could call that a consumer business. It actually sits in leisure goods, and when you look at the make-up of its customer base it's anything but Next-like or Rev Bars-like. I mean, these guys who buy the Games Workshop products, they're fanatics. They spend their last dime on the hobby. There's a real sense of community there, so that's a very different sort of consumer business, but ultimately it's selling to people like you and me. Well, perhaps a little bit younger than you and me but that type of person anyway.

So there are some great consumer businesses out there, so I'm not sort of blanketing it. You could say Diageo, we're happy holders of Diageo. You'd call that a consumer business, I think, in the sense that it's selling to an end user, but it's not consumer in the sense that a restaurant or a bar or a bricks-and-mortar shop is. So that's what I mean. I think this has finally convinced me that – you know, look somewhere else for the great businesses. They don't really sort of cluster around direct customers.

Interviewer: I mean, is it just I guess the vulnerability to downturns? I mean, we can all see how consumer-facing business has been impacted but is it that vulnerability that really puts you off?

Keith: I mean, I don't think any of us saw this coming, what's happened to them now where basically they're being shut down for extended periods of time. I don't think any of us really expected that. That's the black swan event, if I could put it that way. But the thing in particular that gets me is they have a good ride and then fashions change, tastes change and suddenly they're playing catch-up and there's a new kid on the block. And you've only to look – one of the thing I did was go back and just look at the history of businesses, perfectly good businesses that were once cutting edge, like Carluccio's is a great example. That was once a cutting edge business with the store at the front and the restaurant at the rear and freshly sourced ingredients and everybody thought it was wonderful, and five years down the track, suddenly it's old hat.

And this is what gets me, because if you've got a perspective of a five, 10, 20 year investor, you don't really want to be buying into businesses that might not be where they are now in five, 10 or 20 years' time. You want solid, enduring franchises. So that's what's really started to percolate around my head in the last couple of months. But as I say, I don't think any of us thought this could have happened to hospitality-type businesses, where a lot of them are on death row.

Interviewer: Yeah. One company I guess that isn't on death row is Games Workshop, and you've just mentioned it and it was something I wanted to talk about. It's still your largest holding and it's been an absolute star performer over the years, and it did have a fantastic 2019. So the shares are at levels we probably saw in November last year. So what's your current view on Games Workshop? Clearly you still like them but what is it about Games Workshop that you like so much?

Keith: Warren Buffett says the best businesses are those that sell for a dollar, that are produced for a penny and are preferably habit-forming. This is a business – I can't say it makes for a penny but you've got operating margins there, gross margins sixties, seventies, operating margins in the late twenties, thirties. So it's a pretty profitable business, and without a doubt it is habit-forming in the sense that the people who play that hobby are, as I said, fanatical. I once described it as the nearest thing to legalised drug dealing on the stock exchange and the chairman in his next annual report and account actually nicked that phrase off me and put it in his annual report and accounts.

It really is habit-forming. The community that play this war gaming hobby, it really is the be all and end all. So there's a real moat there, and when you look at the business, it's 75 percent overseas, 25 percent UK, wholly UK manufacture and distribution. It's still selling almost half – I think it's about 45 percent or maybe slightly more than that – through independent retailers rather than its own network or online, so there's 500-odd stores worldwide. There's still plenty of scope for rolling out more stores. It's currently been investing heavily in new manufacturing and distribution facilities in this country to prepare the grounds for future growth and even while it's been doing that, it's been throwing off surplus cash and repatriating that to we owners as dividends. It's a lovely little business model and something quite unique.

And I think the final thing that I really like about it is the manner in which it's started to exploit its IPR. So it's using its intellectual property, its imagery, it's actually renting that out, if I can put it that way, to other people who are using that content. Five years ago, royalty income was about a million and a half a year. In the first half of this year it was ten million, in the first half. And you know royalty income, it's wonderful. It's got absolutely no fulfilment cost attached. It's pure profit. So to me, under Kevin Rowntree who is the chief exec who took over from Tom Kirby, this business has been transformed. It really is, it's a lovely little business and unique. There's nothing quite like it, and that's what I like.

Interviewer: So you won't be selling that any time soon?

Keith: No way.

Interviewer: That's great advice. I really appreciate your time today.

Keith: Thank you very much indeed.

Interviewer: Thank you.

[End of recorded material at 00:10:40]