

The new rock stars?

The listed investment company sector has seen significant market growth over the last couple of years. **Tony Featherstone** looks at what is driving the boom.



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MORE TECHNOLOGY COMPANIES ARE EXPECTED TO list on ASX in the next few years as the sector rapidly expands. So too could funds that invest in tech ventures, judging by Bailador Investment Technology’s early success as a Listed Investment Company (LIC).

Co-led by David Kirk, the former Fairfax Media CEO and All Blacks rugby captain, Bailador joined ASX through an initial public offering (IPO) in November 2014. It is the only tech-focused LIC and one of few that invest in private companies.

Bailador is part of an unfolding LIC boom that has seen some of the market’s best-known funds managers launch listed funds in the past two years. They include Platinum Asset Management, Perpetual, PM Capital and Ellerston Capital.

“We felt very confident in the decision to structure Bailador as a LIC and list it on ASX,” says Kirk, who manages Bailador with co-founder Paul Wilson. “The ASX platform was an opportunity to target SMSFs and other high net worth investors, and give them access to private tech companies in the expansion phase, something that has traditionally been hard for retail investors to achieve.”

The value of LICs and listed trusts was \$28 billion in March 2016, from \$24 billion two years earlier, ASX/Morningstar data shows. LIC listings have grown from 65 to 87 in that period. Global equities funds, absolute return funds and specialist funds, such as Bailador, have enhanced the LIC market’s breadth and liquidity.

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Four factors are driving this growth. The first is regulatory change. Financial advisers historically shunned LICs because they did not offer trailing commissions, unlike unit trusts. Future of Financial Advice (FOFA) reforms that banned conflicted sales commissions to advisers evened the playing field.

The second factor is self-managed superannuation funds (SMSFs). SMSF trustees can prefer listed over unlisted investments because they offer more control and lower fees. Other ASX-listed funds, such as exchange-traded products (ETPs) are also benefiting from growth in the \$594 billion SMSF sector. The ASX’s new settlement service for unit trusts, mFund, is also growing strongly.

Dividends are the third factor behind LIC growth. Record-low interest rates have encouraged more investors to buy equities for yield. LICs are close-ended funds that manage a fixed pool of capital, unlike open-ended unit trusts whose assets rise or fall depending on fund flows and market movements. In theory, this means LICs have greater scope to manage dividends and franking credits, and thus appeal to income-focused investors.

Managing a fixed pool of capital (that the LIC manager can increase with capital raisings) is the fourth LIC attraction. Unit trust managers are sometimes forced to sell stocks during bear markets to meet investor redemptions, and buy stocks during bull markets to put new money to work. LIC managers do not have to invest according to fund flows.

Kirk says a LIC’s permanent capital was the main reason Bailador chose this structure. “Managing capital for longer periods best serves our investors. In our previous private fund, we had great success in our investment in SiteMinder (a hotel channel management provider), and realised that we may want to hold the investment beyond the end of the lifetime of the typical private fund. We moved to a listed fund so we can hold investments for as long as is optimal for investor value creation.”

Like many smaller LICs, Bailador has traded at a discount to its pre-tax net tangible assets (NTA) since listing, meaning it is theoretically worth less than the value of its assets, which is determined by third-party investments in its portfolio. The discount to its share price was 20 per cent in March 2016, ASX data shows.

Bailador traded in line with its \$1 IPO issue price in March, despite increasing the value of its assets by more than 25 cents per share since listing.

Seemingly permanent NTA discounts frustrate LIC managers and their shareholders, and fuel LIC critics. LICs can trade below their asset backing if they are new to the market or if investors are concerned about the manager’s performance, investment style, the fund’s underlying holdings or the liquidity of the securities it invests in.

Reaching investors

Investor relations (IR) can be another factor and the LIC sector, tiny compared to the unit trust market, is not known for its IR. Many LICs are run lean and their chief investment officers often have to juggle managing money with marketing roadshows.

Kirk says Bailador erred by not investing enough in IR. “In hindsight, we should have put more focus on explaining our investment strategy after the listing,” he says. “Having secured



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IPO funds, we wanted to focus on investing them and running the business, and expected our investment results to speak for themselves.”

The LIC market’s profile is slowly lifting as prominent managers launch listed funds. One of them, PM Capital, launched two LICs: the PM Capital Global Opportunities Fund in December 2013 and the PM Capital Asian Opportunities Fund in May 2014. They collectively raised \$228 million, but like other newcomers are trading at a discount to NTA.

This rush of larger LICs has led to suggestions that fund managers are capitalising on growing LIC interest to “gather assets” rather than make a permanent contribution to the sector. “There’s probably some truth in that,” says PM Capital founder Paul Moore. “But if investor interest in LICs is there, it makes sense for the bigger fund managers to launch LICs and satisfy demand. More liquidity and profile in the LIC market benefits all LIC managers.”

Moore says the LIC structure suits PM Capital’s investment style. The veteran investor, one of this market’s most successful over three decades, is known for long-term bets, sometimes up to 15 years in a favoured company.

A tactical opportunity in global equities, PM Capital’s speciality, was another reason for the LICs. Moore says: “In 2013, the Aussie dollar traded above parity with the US dollar and Australian equities looked overvalued compared to offshore developed markets.”

Reaching SMSF trustees via ASX was another attraction, Moore says. “All the research says SMSFs are badly underweight in global equities. We gave SMSFs access to global and Asian equities via our new LICs. Fund managers need to use different channels, such as ASX, to reach SMSFs because they are such a large pool of investable capital.”

The rise of global equity LICs means Australian investors, who prefer to invest directly, have more options to add offshore exposure to portfolios via ASX. There is also renewed interest in absolute-return LICs that have broader investment mandates and, in theory, greater scope to preserve capital in falling markets.

LICs that invest in small-cap equities are another feature. Barrack Street Investments joined ASX in August 2014 through a \$16 million IPO. Its chief investment officer, Manny Pohl, runs two other LICs: Flagship Investments and Global Masters LIC.

Dr Pohl says ASX offers advantages over investment platforms that focus mostly on unit trusts. “Getting a unit trust up on a platform is complicated. You need research



LIC listings on ASX since 2013

	Asset class LIC invests in	Listing Date
Absolute Equity Performance Fund	Equity - Australia	Dec-15
8lp Emerging Companies	Equity - Australia	Dec-15
Ryder Capital	Equity - Australia	Sep-15
Platinum Asia Investments	Equity - Global	Sep-15
Ellerston Asian Investments	Equity - Global	Sep-15
Future Generation Global Investment Company	Equity - Global	Sep-15
Glenon Small Companies	Equity - Australia	Aug-15
Contango Income Generator	Equity - Australia	Aug-15
Australian Masters Yield Fund No 5	Fixed Income - Australia	Aug-15
Argo Global Listed Infrastructure	Infrastructure	Jul-15
Wealth Defender Equities	Equity - Australia	May-15
Arowana Australasian Value Opportunities Fund	Equity - Australia	Jan-15
CBG Capital	Equity - Australia	Dec-14
Perpetual Equity Investment Company	Equity - Australia	Dec-14
8I Holdings Ltd	Equity - Global	Dec-14
Bailador Technology Investments	Equity - Australia	Nov-14
Naos Absolute Opportunities Company	Equity - Australia	Nov-14
Ellerston Global Investments	Equity - Global	Oct-14
Qv Equities	Equity - Australia	Aug-14
Barrack St Investments	Equity - Australia	Aug-14
Global Value Fund	Equity - Global	Jul-14
Blue Sky Alternatives Access Fund	Equity - Australia	Jun-14
Pm Capital Asian Opportunities Fund	Equity - Global	May-14
Acorn Capital Investment Fund	Equity - Australia	May-14
Sandon Capital Investments	Equity - Australia	Dec-13
Pm Capital Global Opportunities Fund	Equity - Global	Dec-13
Australian Masters Yield Fund No 3	Fixed Income - Australia	Oct-13
Australian Masters Yield Fund No 4	Fixed Income - Australia	Oct-13
Watermark Market Neutral Fund	Equity - Australia	Jul-13
Zeta Resources	Equity - Global	Jun-13
Us Select Private Opportunities Fund II	Equity - Global	Apr-13
Lion Selection Group	Equity - Global	Mar-13
Naos Emerging Opportunities Company	Equity - Australia	Feb-13

Source: ASX. Data to February 2016

on the fund, dealer-group support, and have to go through investment committees on the platform. It's a nightmare compared to listing an LIC on ASX, once you have secured the minimum subscription and met ASX Listing Rules."

Pohl expects more funds to list on ASX. "It's a fabulous way to raise capital and get your fund to market quickly and raise its profile. Critics say the potential to trade at a discount is a turn-off, but I don't see it as a problem if LICs, such as ours, have a long-term focus and a good record of increasing NTA over time. Eventually the discount narrows and becomes a premium if the returns keep rising."

Boyd Peters, a LIC investor relations expert, says the market is suffering from saturation because of the increase in new LICs. "Brokers have many companies vying for their attention that can offer a quick (share price) pickup, so a LIC that offers a slow grind of performance has to be compelling to catch their attention."

Peters encourages LICs to market directly to end investors, in addition to building adviser channels. "LIC managers have to go to the main investor conferences and have an active roadshow schedule," he says. "I've driven hours to give presentations in country towns. Retail investors want to see the LIC manager and hear what they have to say. Fund managers used to adviser groups distributing their unit trust get a shock when they realise how much direct marketing and legwork is needed with LICs."

Peters adds: "The LIC sector has a good story to tell and it has some of the most exceptional fund managers. Typically, they worked at large managers, realised an LIC structure would better serve investors, and put their own money into the LIC. The message is starting to get out, but there is a long way to go."