



Stock selection is key to outperformance, not **SECOND-GUESSING MACRO TRENDS**

By Craig Baker, Chief Investment Officer, Willis Towers Watson

In meetings with shareholders, we're often asked for our views on macro events. Typically, these include the consequences of the end of quantitative easing, Brexit, and Trump's trade wars – all hugely complex issues that stimulate endless debate in financial markets. Like many other firms, we have a large team helping us understand these factors as well as many others, but for us it is primarily with the aim of understanding risk, because we don't see short-term tactical asset allocation as the best way of achieving long-term wealth creation.

The Alliance Trust portfolio has been built to deliberately avoid large bets against the market in terms of over or underweight allocations to countries, sectors or investment styles. Trying to predict business cycles or politics, and positioning equity portfolios accordingly, can be something of a mug's game. There are just too many variables to consider. It's why successful investors such as Warren Buffett gave up trying to second-guess macro factors years ago. "I make no attempt to forecast the general market – my efforts are devoted to finding undervalued securities," he said.

We agree that stock selection within equities is far more reliable as a source of added value through time and, as a result, this is the key focus of the Alliance Trust portfolio. We allocate capital to a range of skilled, bottom-up stock pickers, who look at the potential profitability of individual businesses. This involves painstaking fundamental research into business models, industry dynamics and the quality of company management. Macro events may still influence how those businesses trade and, therefore, do have to be considered. But they are generally secondary to the industry and company-specific factors that ultimately drive share prices over the long term. These factors are easier to analyse and predict than, say, the trigger for the next economic downturn or the outcome of a referendum.

The MSCI All Countries World Index captures all sources of equity returns in 23 developed and 24 developing countries. For investors increasingly looking beyond their home market toward the full global opportunity set as the starting point for their investments, it represents an ideal proxy for the global economy.

We construct the Alliance Trust portfolio by assembling a line-up of eight talented stock pickers, asking them to each forget about risk and just focus on picking the 10-20 best companies globally which they consider to have the highest long-term return potential. All of the managers have been through our rigorous research process and are judged by us to be among the best in the world. We deliberately choose them to be different from and complementary to each other. This natural diversification of styles and ideas results in a combined portfolio, that is quite similar to the MSCI All Countries World Index when viewed simply from a country, sector and style perspective, thus controlling risk. However, from a stock perspective it looks totally different. That is exactly what's needed if the main determinant of returns is going to be stock selection.

Fear of being fired leads to most managers adding filler stocks

Very few fund managers would be bold enough to run a highly concentrated portfolio of 10-20 stocks. Although research shows that these portfolios can deliver significant outperformance over the long run, they can also be very volatile. While patient investors may stick with a skilled manager through an extended bout of turbulence, others with shorter time horizons may cut and run. Behavioural economics teaches us that the fear of being fired in the manager's mind is likely to loom larger than the hope of delivering outsized returns. So, left to their own devices, an individual manager is likely to guard against this risk, by adding some filler stocks that might prevent performance straying too far from the benchmark.

However, if the managers are asked to play as a team, they will embrace risk because none of them is likely to be blamed individually if the portfolio underperforms. That is the principle underpinning the design of the Alliance Trust portfolio. By removing the threat of being criticised for short-term underperformance, the underlying stock pickers are free to focus on only their best ideas.

At an ongoing charges ratio of 0.65% pa for some of the best-in-class active global equity managers in the world, we believe Alliance Trust is the ideal core fund for any return-seeking portfolio*. As Morningstar stated in its recent write-up on the fund, "We feel that investors are in safe hands with Alliance Trust." ■

* As rated by Willis Towers Watson.

Important information: This information is not a personal recommendation for any particular investment. If you are unsure about the suitability of an investment, you should speak to an authorised financial adviser. Please remember, past performance is not a guide to future performance, and the value of shares and the income from them can rise and fall, so investors may not get back the amount originally invested.

Towers Watson Investment Management Limited have approved this financial promotion for issue to Retail Clients.

The Alliance Trust Board has appointed Towers Watson Investment Management (Ireland) Limited (TWIMI) as its Alternative Investment Fund Manager (AIFM). TWIMI has delegated the investment management of the Alliance Trust portfolio to its specialist division, Towers Watson Investment Management Limited (TWIM). TWIMI and TWIM are both part of Willis Towers Watson (WTW).



Craig Baker
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Craig is ultimately responsible for all aspects of Willis Tower Watson's investment philosophy and process. He is Chair of the Investment Committee which selects and oversees the eight managers who run Alliance Trust's global equity portfolio of high conviction stocks. Craig joined Towers Watson, as it then was, in 1994. He is a Fellow of the Institute of Actuaries.

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