

RADAR ALERT – ARGONAUT EUROPEAN ALPHA

Argonaut's Barry Norris sees little sign of financial issues spilling into real economy in Europe and believes we are past peak of volatility

Norris currently at most bullish for 18 months



BARRY NORRIS

- Launched Argonaut European Alpha fund in 2005.
- Launched first fund on joining Neptune Investment Management in 2002.

By Natalie Kenway

Argonaut manager Barry Norris is currently more bullish on European equities than he has been for the last 18 months.

He said there is little sign of the crisis in the financials sector spilling over into the real economy and believes we are past the worst peak of the volatility.

"The consensual opinion is that this is not a time to be investing in the stock market but I think this could be very wrong for a number of reasons," he said.

"Liquidity has been restored to the global financial system. Outside of the financial and property sectors, there have been few tangible signs of economic slowdown and company management remain resolutely bullish.

"There are obviously still a lot of things to worry about but there is a danger many investors only sound the all-clear at much higher share prices and will miss out on many of the better opportunities."

Former Neptune manager Norris set up the Argonaut boutique, a joint venture with Resolution, alongside Oliver Russ just over three years ago and launched the European Alpha fund.

Over the past three years to 19 May, the vehicle boasts top quartile returns.

It is second in the Europe ex UK sector returning 100.8% bid to bid, compared to the average of 67.1%, according to Morningstar.

Norris said he values company management and industry trends much higher than macroeconomic data and forecasts and these govern where the fund invests.

He looks for companies that are doing well, and will continue to do so, as well as those that have done badly but are in a period of transition.

The fund invests in 45 high conviction ideas and is not restricted by geographical, index or cap-size constraints.

Two areas Norris said he believes will perform much better in 2008 than in 2007 are the and steel sectors.

"Energy is the obvious one as the oil price is currently \$130 a barrel compared to \$70 last year. Those companies that can display operating leverage will do well," he added.

In the steel sector, Norris said the price of the metal for the global export market has doubled over the past six months.

"China has stopped exporting as the country needs steel for its own market, which has given the rest of the world pricing power. The sector is going to have a far better year in terms of profit."

European Alpha currently has no financial positions where Norris believes the de-leveraging process will take some time.

"In general, banks have been making too many loans relative to their size. Profits will come down and capital to support the business will go up resulting in a negative double-whammy for shareholders," he added.

"Earnings momentum in financials continues to be negative and more downgrades are anticipated."

The manager also finds it difficult to construct a bullish thesis for the automobiles sector, which is likely to suffer from the pressured consumer in the developed world and higher steel prices.

Norwegian oil company Statoil has been a positive performer for the fund because, Norris said, it has the highest leverage to the oil price and is purely upstream.

"It does very little refining and owns nearly all of its own acreage. Other major oil companies have production sharing agreements so they have less operating leverage to higher prices as someone else owns the acreage. It is still very cheap and with oil at \$130 a barrel it is likely to see more upgrades," he added.

ANDREW MERRICKS

Head of investments, Skerritt Consultants

Norris made his name initially at Neptune and, as with any good manager, we looked closely at the proposition when he left to set up his own boutique with the help of Resolution. I tend to favour funds whose managers have a direct alignment of interest with their investors through part ownership of their company.

Norris is prepared to take unorthodox positions in companies within his portfolio if he thinks it will make him money.

As such, he finds stocks within parts of Europe that other managers tend to ignore, and it is in this practice that he adds more value than many competitors. He also runs a tight portfolio in terms of number of stocks held, so that if he picks stocks well, the performance is magnified. Although the opposite is true if he gets it wrong, happily he has generally been one of the better European stockpickers available to retail investors, and for this reason remains high on our favoured funds list.



German steel company Salzgitter has also been one of the better-performing positions.

Norris said it has a strong balance sheet with lots of cash from parts of the business it has sold off.

It has been able to re-negotiate contracts upwards and it is seeing robust demand from the industries it sells to

– for example, pipes to build infrastructure.

From a negative view, Finnish telecom firm Elisa has not performed as well.

"I think it is very good value for the cash generation and dividend yield but the problem is the management have made some blunders in terms of executing the business plan," he added.

JUSTINE FEARNS

Head of investment research, AWD Chase De Vere

The Argonaut boutique has gone from strength to strength since launch in 2005. There are a number of reasons for this, including the experience and track record of the management team, the ownership of Argonaut within Resolution, the marketing strategy behind the boutiques, and of course the investment process and philosophy underpinning the fund and the performance this has helped generate.

The philosophy is based on the view that market rewards earnings growth in the long term and earnings surprises drive outperformance but this all needs to be reviewed relative to valuation.

This philosophy is captured within a very robust investment process driven by fundamental stockpicking. The market is screened using a proprietary quant tool, earnings surprises and valuations are obviously key, and some under-researched areas are identified through specialist brokers. Valuation also plays a key part in the sell discipline but is by no means the only trigger.

This has combined to generate some strong returns over and above the sector average since launch, both on a discrete and cumulative basis, which I would imagine has led to some pretty happy investors.

