

INVESTING? IT'S A FUNNY OLD GAME

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It was while watching last season's Champions League semi-finals between Real Madrid and Bayern Munich that my mind once again began drawing parallels between football and investing. Specifically, it was seeing James Rodriguez, the Colombian wunderkid from the 2014 Brazil World Cup, turning out in a Munich shirt, on loan from his parent club Real.

Rodriguez, lest anyone has forgotten, had a magnificent tournament four years ago, scoring six goals to scoop the Golden Boot and being named in the World Cup All-Star XI. This achievement prompted Real Madrid to splash out a handsome £63 million for him. But he never really settled: in three seasons he managed just 77 appearances before Real capitulated and loaned him out to Bayern Munich. The lesson is that yet another World Cup star was proven to be overvalued – in the same way that many glory stocks can fail to live up to their premium versus their peers. Just as being wary of buying stars of the World Cup, make sure you **don't overpay for growth stocks!**

With the 2018 World Cup now underway (yes folks, it's a tournament tie-in piece!), I've taken a break from portfolio management – and filling in my Panini sticker album – to draw seven other lessons from football that can be applied to investing.¹

1. Make your actions count. Manchester City have been an almost all-conquering juggernaut this season, racing to a record points total and scoring a record number of goals. But

¹ Concept inspired by *Why England Lose & Other Curious Football Phenomena Explained*, by Simon Kuper and Stefan Szymanski, HarperSport, 2009.

they were dumped out of the FA Cup by lowly League One side Wigan Athletic who, despite having just 17.5% possession and only two shots on target, were 1-0 winners. How did Wigan do it? By doing their research. Fund management is similar. It's about what you do before and after a trade that determines long-term success. It's the analysis and research to evaluate a company's strengths and weaknesses versus its competitors; and it's about constant monitoring to ensure a company is still worth its place in a portfolio.

- 2. Don't ignore late bloomers.** Not all players announce themselves at 16 by coming off the bench to score a last-minute 30-yard winner (doff of the cap to you, Mr Rooney). Some toil away in amateur and non-league teams before eventually turning professional (such as Jamie Vardy, who won the Premier League in 2015-16). Others struggle to make their mark before maturing and eventually returning in glory (such as Australian Aaron Mooy who toiled away in Scotland and his home country before eventually helping Huddersfield Town reach the Premier League in 2017 for the first time in 45 years). Both these players went to the world cup in Russia yet neither really got going until their mid-20s.

Ideas and companies develop at different speeds too. The market can be fixated on those aspects of a company that are going wrong, ignoring that there are other businesses operating well or that there's a great business waiting to get out. But patience can pay off: Rentokil, for example, was being dragged down by its parcels division City Link. But it sold it off for £1 in 2013 (a very good trade as it ultimately went bust), while Rentokil has since easily more than trebled its price.² The key, of course, is identifying the potential and getting in before the recovery.

- 3. Centre forwards are overvalued, goalkeepers are undervalued.** Teams that score more than their opponent will always win, but the flipside is that teams that concede fewer will also always win. Yet you will only find one goalkeeper in the Transfermarkt Top 50 most expensive transfers (Gianluigi Buffon) amid countless strikers.³ This is because, whereas clean sheets are merely valued and mentioned, goals are actively celebrated. Similarly, getting your portfolio to consistently outperform is as much about avoiding share collapses as it is backing the winners: ie, defence and attack.

Liverpool's loss in the recent Champions League Final is a case in point. While manager Jürgen Klopp has assembled an attacking unit which is the envy of Europe, he should perhaps have paid more attention to a known weakness in his goalkeeping department. And it cost his team big time as goalkeeper Loris Karius made two quite spectacular unforced errors to give away two goals. To sum up: avoid buffoonery, buy more Buffon!

- 4. Tune out the noise.** Football itself is now almost the sideshow; the noise that accompanies it has become the main event. Reams of column inches and thousands of TV minutes devoted to ex-player pundits opining on the state of teams, who will win the league, who will go down. These views are either momentum-driven or deeply biased. Ex-Liverpool player Mark Lawrenson has a BBC column in which he predicts the scores each week. The last two seasons he has made a reasonable stab at

² Bloomberg, as at 23/5/18.

³ Transfermarkt.com, 23/5/2018.

picking the top four finishers, but most noticeable in his predictions is that one team has managed a truly incredible two whole seasons unbeaten ... Liverpool. All hail the invincibles!

These cognitive biases are also rife in the investment world, with sell-side commentators and portfolio managers often anchoring to preconceptions despite evidence to the contrary, or suffering from, among other things, overconfidence, loss aversion or inertia.

- 5. Squad management.** Be prepared to sell any player if another club offers more than he's worth – and with this analogy we're back at Liverpool. Luis Suarez was on fire for the side in the 2013-14 season, winning the FA's player of the year. But his head was turned by interest from Spain and he was sold to Barcelona for £75 million.⁴ The fans went crazy. But a younger player in the ranks, Philippe Coutinho, bought from Italy for only £8.5 million⁵, was just blossoming, and he eventually became a new focus and fulcrum for the team. (For the more seasoned student of the game, perhaps read the purchase of Kenny Dalglish to replace the departing Kevin Keegan in 1977 at Liverpool!)

This is portfolio management, and you should always have an incubator of replacement stocks, which is the same as replacing your best players. In January of this year Barcelona came sniffing again, and Coutinho was sold for an initial £105m.⁶ Liverpool once again felt confident their squad would ultimately benefit from the Brazilian's sale. Step forward Mohamed Salah, ably assisted by one or two other star performers just reaching their peaks. Likewise, if one stock is sold entirely, there should be a cohort of others ready to flourish in their own right.

- 6. Evaluate and evolve what you own.** James Milner was the youngest player to score a Premier League goal. He played for Leeds United (when they were good), Newcastle, Aston Villa and Manchester City, twice winning the league as well as an FA Cup with the latter. When he was sold to Liverpool it was a move that wasn't greatly heralded. But he's quietly evolved into a hugely dependable and consistent player.

As a business, there is theoretically a growth phase, a roll out and a maturity phase. In practice, listed companies can go through many different phases in their lifespans and the nuances of these can sometimes be misidentified by the market. As part of our fundamental approach, we try to keep in mind when looking at current or prospective holdings the evolving roles they could play in our portfolios, and take advantage of the occasion when the market fails to accurately evaluate this. Another manager's mature, slowing growth stock could well one day become our very own James Milner!

- 7. Be more like Spain.** England's "golden generation" of players were massively hyped yet failed to deliver a World Cup or European Championship victory. The best players were picked rather than the best squad; shoehorned into ill-fitting positions because

⁴ <https://www.bbc.co.uk/sport/football/28180600>

⁵ <https://www.bbc.co.uk/sport/football/21266402>

⁶ <https://www.telegraph.co.uk/football/2018/01/04/barcelona-prepared-spend-140m-sign-philippe-coutinho-liverpool/>

they were too big to be dropped. Spain were similar underachievers, for many years the sum of the parts was never as good as the individual components. Yet victory in the 2008 European Championships was followed by a 2010 World Cup win and the 2012 European Championship.

This is because Spain was not just a bunch of the best players for whom individual momentum was strong; it was a carefully considered squad, working towards the same goal, each evaluated for what they could bring and combined to create a formidable team. This is all the more remarkable considering the bitter club rivalry between Real Madrid and Barcelona which dominates the Spanish football landscape. Recent comments made to the press by Rio Ferdinand reveal that the England players of the golden generation picked to represent their nation were unable to overcome the deep club divisions in the squad.⁷

So in constructing our portfolios we should aim to avoid the internal conflicts which scuppered England's "golden generation" and instead emulate Spain by focusing on balance, and on achieving the right blend of companies that will, as a whole, deliver strong risk-adjusted returns. But maybe don't fire your manager the day before the tournament!

Football and investing are interchangeable. Like the best football teams and managers, we exchange and debate ideas in a collaborative environment. This enriches our teams' investment processes and ensures our best insights are applied to portfolios – all in the service of clients. Likewise, great football teams work together to deliver consistent performances, all in service of supporters (is that the sound of disgruntled fans spitting coffee over their computer screens?).

Just like football managers, portfolio managers must be consistent from the first to the 90th minute – and not, it should be added, in the way Theo Walcott talks about it: "I've been consistent in patches this season," he once uttered.⁸ Football managers try and surround themselves with the best support, from coaches to trainers, just as portfolio managers must create winning teams of analysts, researchers and assistants.

So, does World Cup glory beckon for England? Who knows, because there's one thing we haven't mentioned – chance and luck. It's our job to ensure that this is the one area where portfolio management does not correlate with football.

Enjoy the tournament!

⁷ Matthey Syed. "If England are to succeed Southgate must root out cliques within his squad." The Times, 13 May 2018.

⁸ We Love Football: Best Football Quotes On Earth, by Adrian Adams

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