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Monks Investment Trust: interview with Spencer Adair

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Financial journalist Cherry Reynard and investment manager Spencer Adair explore Monks Investment Trust and the long-term growth opportunities within diversified portfolios.

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Cherry Reynard (CR): So, welcome, Spencer. Now, a quick introduction for anyone who may not be familiar with Spencer. You've been a partner in the firm since 2013, and you're an Investment Manager in the Global Alpha Team, which manages the Monks Investment Trust. So perhaps we could kick off with an overview of what Monks is all about.

Spencer Adair (SA): Absolutely. Thank you. So Monks is a diversified, long-term growth trust, with low cost. The diversified growth is we can go anywhere in the world. So we can invest in all four corners of the globe and across all industries or sectors. So, currently, we've got 33 different industries that we invest in, so it really is very broad-based.

And we make money for our clients by the growth, the fundamental growth of those businesses. And the good news is that those businesses are in great shape.

CR: Okay, great. And with that broad palette, can you tell me a bit more about how you are defining growth?

SA: Absolutely. So we've got three definitions of growth.

One is our growth stalwarts. So these are our get-rich-slowly, compounding companies. So in there today would be the likes of Microsoft or Novo Nordisk. They are companies you're prepared to own for decades, and they can churn away and grow.

Second up would be more immature companies, the rapid growers. The next five years look very bright, but they're doing something radical, something different. So it's really cutting-edge things.

And then the third type would be cyclical growth. And these are more established industries, they've got a bit of a cycle to them, but they're run by people that have done this before. So they're run by people that lean in when everyone else is leaning out, and they take a step back when everyone else gets excited.

CR: Okay. Let's start at that grittier end, because I think those are the type of companies people wouldn't necessarily associate with Baillie Gifford. Can you talk through some of those underappreciated opportunities?

SA: Yes. So what Monks is really trying to do, we're trying to combine some of the glitz and glamour, if you like, of Silicon Valley and that growth, but also some of the grit of the real-world businesses. And we've owned some of these companies for decades. So that may include the likes of Ryanair, CRH, Martin Marietta, companies that are airlines or aggregate companies. So I get excited about gravel and that kind of thing, which not everyone can say that.

Look, one recent example. I was in Canada last week, and one of our new holdings in Canada is a company called Stella-Jones. Now, that sounds a little bit like a Welsh performer, but Stella-Jones is actually North America's largest electrical pole company. So it takes very long, straight trees, it strips them, treats them and stores them. And these poles literally support the whole grid, the electric grid in North America.

Now, Stella-Jones has a terrific record. Over the last 25 years, it's been consolidating the market, and it's up a hundredfold. So you can get excited about boring things like poles, and you can make a lot of money out of them. But for us, the exciting thing is that the growth we think actually over the next 25 years, could be equally bright. And that's because of a couple of things.

Whenever a lot of the infrastructure was put in place, it was in that 1945 to 1960 period. Now, these are wooden poles. They have beetles, they have rot, they last a certain amount of time, and they're getting on a bit, so they need to be replaced. So next time there's a big windstorm, it'll be very good for Stella-Jones. So we've got a replacement cycle going on, which means we're in for a pretty ripe or pretty strong 25 years of growth.

But on top of that, you've got all the extra needs for electricity. That could be powering electric cars, it could be the new solar and wind turbines. So you're generating the electricity in different places and you're also consuming it a lot more in other areas. So the grid investment is going to have to go up a lot. And so that's what excites us about the likes of that company.

Finally, there are significant barriers to entry. There are some biological barriers. You cannot just grow really tall trees straight away. You have to wait 40 years before these are ready. And so the supply side can't just respond quickly. But also, you've got to treat these poles, you've got to store them. There's a lot of working capital, a lot of quite harsh chemicals. So these things, we're really excited about that kind of strong growth, underappreciated, strong track record, and yet trading on a well below market multiple of earnings.

CR: Is there any vulnerability to a change in US administration?

SA: There always might be, because you never know. US politics is never 100 per cent forecastable. But what we're talking about in these kind of infrastructure investments, there's bipartisan support. There's also lots of local support. If your grid goes down and you don't have local power or you don't have bridges or your roads are terrible, and potholes, that annoys the local voters. And so you tend to have both local activism plus bipartisan support.

And then on top of that, you've got this element of geopolitical will to bring more high-end manufacturing back into the US and to deal with some of the more greener ways to produce electricity. So actually, of course, any one politician could interfere for a little bit, but we think, structurally, there's going to have to be significant long-term investment in some of these infrastructure-type investments.

CR: Okay, great. Now, so you talked about the glitzier side.

SA: Yes.

CR: You have some exposure to AI and tech more broadly. Can you talk me through a couple of those?

SA: Yes, of course. So I'm not going to repeat the NVIDIA or the Novo Nordisk cases because they've been done. They've been done to death, I'm sure. But whenever we speak to all of our high growth companies, we're looking for two things. We're looking for what's changing in the world and what's the bottleneck.

And the bottleneck, whenever I speak to battery companies or chip companies, hi-tech biotech manufacturing, electric cars, the big bottleneck is skilled labour to actually build these plants. So this is the thing which is holding them back. It used to be equipment, maybe a couple of years ago, but the supply chains got resolved. But now it's actually people to build. ChatGPT is fantastic, but it can't build your factory, it can't do your wiring for you. And that's the real bottleneck.

So a company I met last week that's from Texas is called Comfort Systems, which we own in Monks. And it has got 16,000 employees, and they're either electrical engineers, contractors, or they're air conditioning contractors. And they're in huge demand at the moment. In 2020, their backlog was about six months and about $1.5bn worth of work they had on their books. Today, they're booked out until 2026, you can't put them in your diary, and the backlog's about $6bn. So it's risen fourfold in the last few years. So it's the type of growth where, if you can identify that bottleneck, you can identify where growth's going to accrue.

CR: Yes, that's quite a pipeline. And then just finally, with such a diversified portfolio, is there anything that unites these examples?

SA: Well, so the two things I talked about were change and bottlenecks. And if you can identify those two things, it doesn't matter if you're the latest AI chip, it doesn't matter if you're someone making utility poles, those are the things which, if those two are in place, those are the precursors for growth.

And then afterwards, we then say, if you've got change and a bottleneck, can we see a plausible chance that any individual holding will double over the next five years? That's not necessarily a central case, but it's a possibility of doubling. And everything has to pass that test, and it does so. So that's both the drivers of what we're looking for, but also, there's a valuation driver or an upside driver that we also put in place.

CR: Brilliant. Okay. I've noticed your turnover has ticked up to 20 per cent recently. That doesn't sound very high. But why are you trading more of late?

SA: So not too much has changed. So, technically, that is correct. Turnover was about 15 per cent, and now it's about 20. But I wouldn't read too much into any one single year's numbers. Long term, we are a five-year holding period. 20 per cent is in line with that, so nothing unusual. But I don't manage it on a rolling 12-month basis, so it's perfectly possible that my turnover is 10 per cent in one 12-month period or 30 per cent. It's going to average 20 per cent over the long run, so don't read too much into short-term numbers. The reason why turnover is a little bit higher is we've had lots of change, lots of new opportunities, and so it's driven by those new ideas coming into the portfolio.

CR: Okay. One more. Can we have some examples of growth companies that have adapted to this environment of elevated rates?

SA: Absolutely. So about 20 per cent of the portfolio is in companies that we would call capital-advantaged, in that they've got a big beneficiary, or they've got a big benefit of having raised a lot of capital and are now really proving their profitability. This was probably most visible by the likes of Meta, formerly called Facebook, who, if I go back two years, they could not spend enough money, quickly enough, on augmented reality and virtual reality. And today, they have really pivoted to, well, let's just show a bit of growth, let's just show some profitable growth, and the share price was rewarded with a very, very strong run in the markets the last couple of years.

And a number of the smaller tech companies are doing exactly the same. They're saying, before I can go and become go-go growth again, I'll prove it to you. It's like doubting Thomas. They're saying, look, I can grow, I'm valuable, my business model works. And so there is everything from, even the big companies, like Amazon, are beginning to do it, but some of the smaller ones, like Block, are doing it. And so it's a really common theme among many of the rapid growers. And then the other bucket we have are these stocks which have got a lot of spare capital, and they're deploying it, they're using it, they're taking advantage of the bargain prices out there.

CR: Great. Okay, thank you. And then I guess we've got about 30 seconds for this one.

SA: Okay.

CR: But what's your overall outlook from here?

SA: Okay. Very enthusiastic. Growth is broadening, which we like. It's not just about seven stocks anymore. That plays into our hands. And our companies have got great balance sheets, structurally faster growth, they're doing the right things, and they're all self-funding. So I'm very excited.

CR: Brilliant. Okay, thank you so much, Spencer, for your time today. And thank you all for joining us.

To find out more about the topics we've discussed on the programme, please do go to the website, bailliegifford.com. Do get in touch if you have any questions. So, until next time, goodbye.

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