

# Pictet Asset Management: Our Thematic DNA

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# Our Thematic DNA

November 2018

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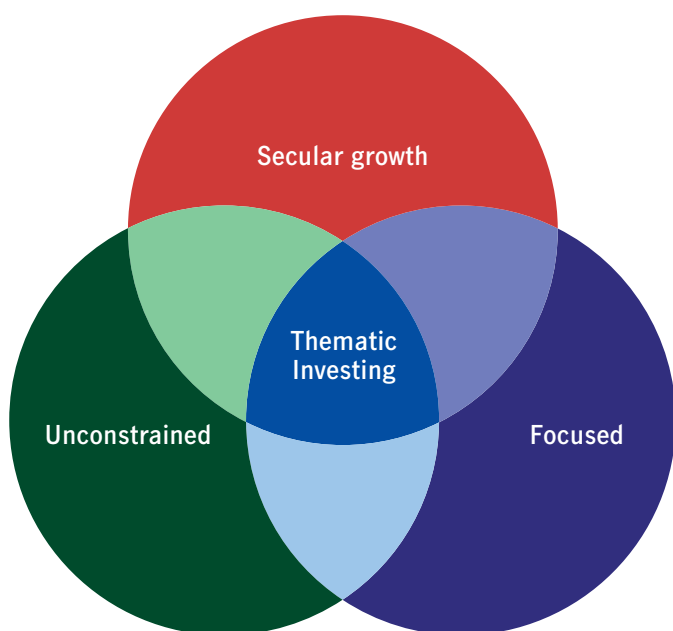
We've designed our thematic strategies around three key investment pillars. Together, they form the foundations on which we seek to build strong long-term performance. Here's what they are and why they work.

## How we invest

What makes our thematic investment approach different is the combination of three key investment principles – our unique investment DNA:

1. Our emphasis on secular growth
2. Our focus
3. Our ability to manage portfolios in an unconstrained manner

**Fig 1: Pictet Asset Management's Thematic DNA**



Source: Pictet Asset Management

## Table of contents

- 1 Secular growth prospects
- 2 Focus
- 3 Unconstrained, forward looking portfolios

# 1

## Secular growth prospects

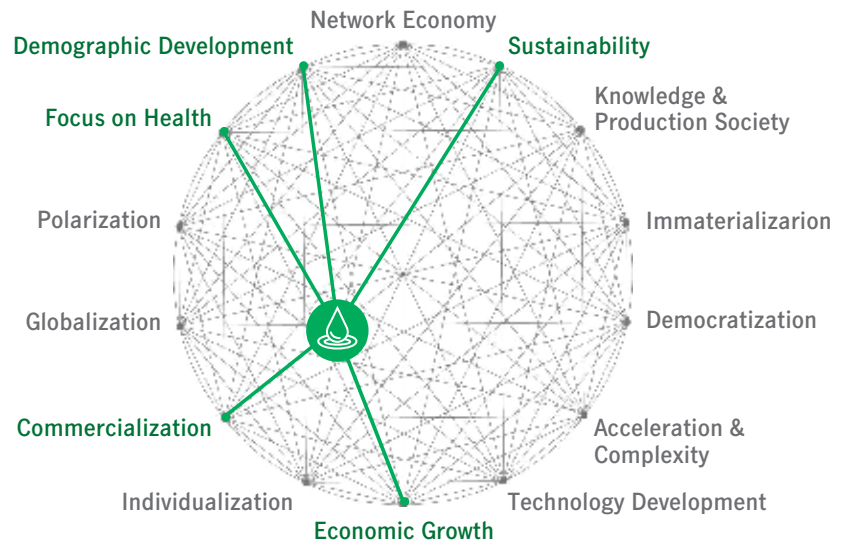
Megatrends are secular shifts that will shape the world for decades to come. We think they are a crucial driver of long-run investment performance, which is why we use them as the basis for each of our thematic equity strategies.

Our approach demands that **thematic** strategies be underpinned by multiple megatrends, which together engender clear and predictable sources of value, growth & margins. Theme-based strategies work because of the existence of short-term market inefficiencies – for example, the failure to recognise the future impact of megatrends.

For instance, take one of the megatrends supporting our **Water** thematic strategy: **commercialisation**.

### Fig 2: The Weight of Water

As the diagram below shows the water theme is underpinned by 5 megatrends.



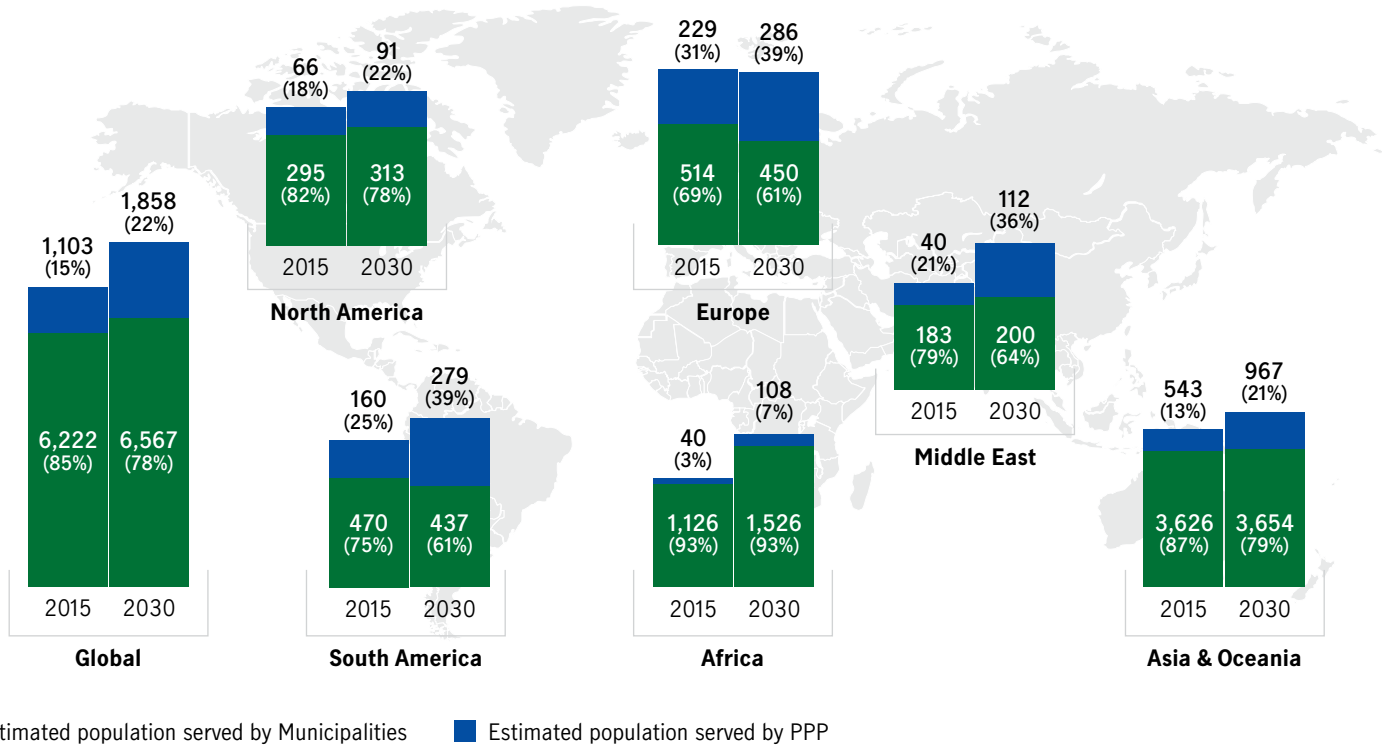
Source: Pictet Asset Management

As Fig. 3 below shows, the water sector is undergoing a secular shift away from a public-sector management model to one with ever greater private participation. This commercialisation is not just a phenomenon in the US but is happening across all global markets.

Being able to assess the long-term commercial impacts of this megatrend was key to validating the Pictet Water strategy.

**Fig 3: The Commercialisation of Water**

Growth in water public private partnership (PPP) across all regions



Source: Envisager 2015



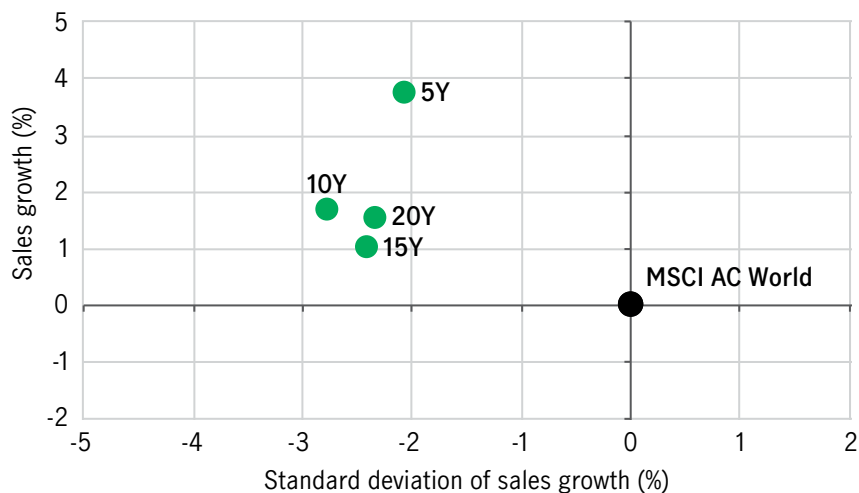
## Secular growth makes it easier to predict growth and margins

The structural forces that underpin the thematic companies in which we invest make it easier to understand how they're likely to perform compared to the wider global equity universe.

The dots in Fig. 4 below show the sales growth of our thematic universes versus the companies in the MSCI All Cap World Index over 5, 10, 15 and 20 year periods. Companies in our thematic universes have experienced higher and more reliable (ie. less volatile) long-term sales growth than the market in general.

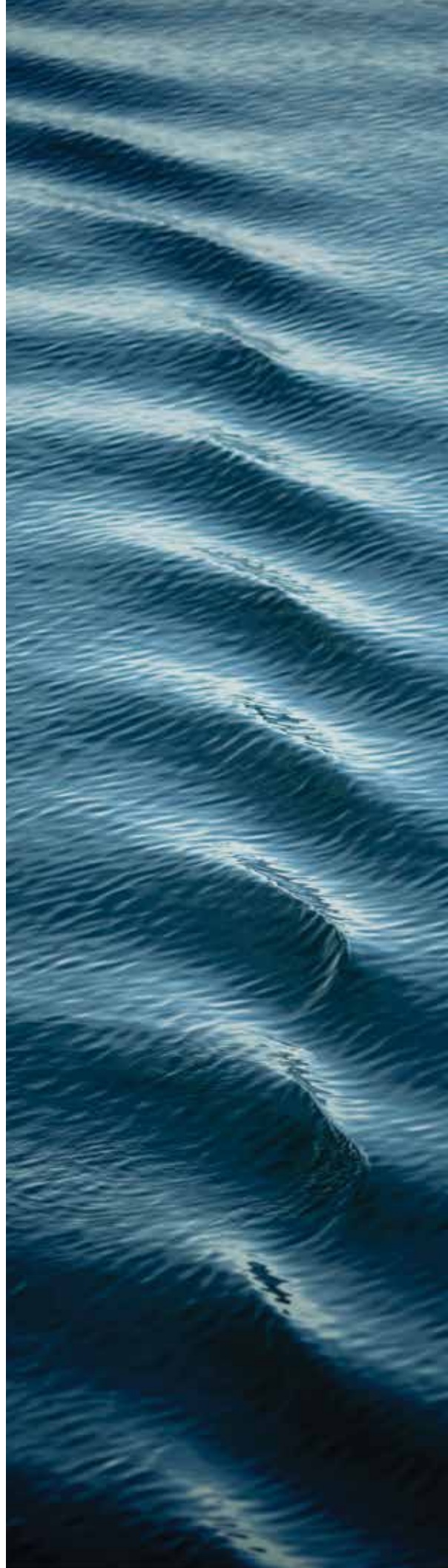
Paradoxically – and fortunately for us the best thematic companies, and therefore those that we target, often trade at a discount to their long-term potential. Indeed, we see evidence that the often short-term mindset of the wider market overestimates the rate at which the cash flows generated by thematic companies 'fade'.

**Fig 4: Thematics Over The Long Term**



Source: Pictet Asset Management analysis based on backtest of our Global Megatrend Selection portfolio<sup>1</sup>. Data to December 31, 2017.

<sup>1</sup> Global Megatrend Selection is a Thematic Strategy investing in multiple themes offered by Pictet Asset Management in Europe and is not available in Canada. Global Megatrend Selection was launched Oct 30, 2008. This backtest includes historical sales data for current holdings in the fund to illustrate the characteristics of sales growth and standard deviation of that growth over longer time periods. These characteristics are not representative of the Manulife Global Thematic Opportunities Fund launched in Canada Oct 17, 2018.





# 2

## Focus

### Successful thematic investment demands several different types of focus.

First, focus means being specialists in the themes in which we invest. Being able to navigate the implications of the multiple megatrends driving a theme demands concentrated effort. We are not generalists covering multiple sectors or themes. Some of us have been following certain stocks in our universe for over two decades. We know the management teams inside-out and have good access given the size of our holdings.

Second, the companies we buy have to be focused on the themes they belong to – what we call “thematic purity”. Only companies whose activities predominantly lie within the scope of a particular theme become candidates for investment: pure plays are always favoured over more diversified companies.

In part, that’s because a large body of research suggests specialist companies make for better long-term investments than larger, more diversified firms. This academic literature, which appears to have been overlooked in recent years, points to the existence of a “conglomerate discount” – i.e. that big firms are worth less than the sum of their parts<sup>2</sup>.

By extension, portfolios made up of pure-plays – firms that specialise in activities in which they have a distinctive competitive edge – can be expected to do better than a portfolio that contains conglomerates<sup>3</sup>. And although mega cap companies are no longer called conglomerates, a large number of such firms pursue the same wide range of activities. Unsurprisingly our strategies are tilted towards smaller- and mid-cap companies. We believe therefore that our focus on purity creates a tailwind for our equity strategies.

### Focused investment teams with combined portfolio manager and analyst functions

Finally, focus is embedded in how our investment teams are structured. Each team member is not only a portfolio manager, sharing responsibility for the management of the strategy, but is also a stock analyst. By dedicating all their attention to a clearly-defined universe of stocks, our investment managers develop distinctive, specialist expertise.

We believe this gives them an advantage over the typical active global equity team, which works rather differently. Most mainstream global equity funds are run by managers supported by several analysts, whose task it is to generate lists of their best ideas within their assigned sectors. The portfolio construction team then chooses stocks from among those recommendations.

A typical global equity manager tends to have to cover a very large universe of stocks and thus can be less focused than analysts. This can make it very difficult for them to add value in the portfolio construction process, as successfully picking stocks from a list of analyst recommendations is difficult.

<sup>2</sup> Ammann, Manuel and Hoechle, Daniel and Schmid, successful stock picking. Markus M., “Is There Really No Conglomerate Discount?” (Working paper, 2011).

<sup>3</sup> Larry H. P. Lang, and René M. Stulz. “Tobin’s Q, Corporate Diversification, and Firm Performance”. *Journal of Political Economy* 102.6 (1994): 1248–1280.



# 3

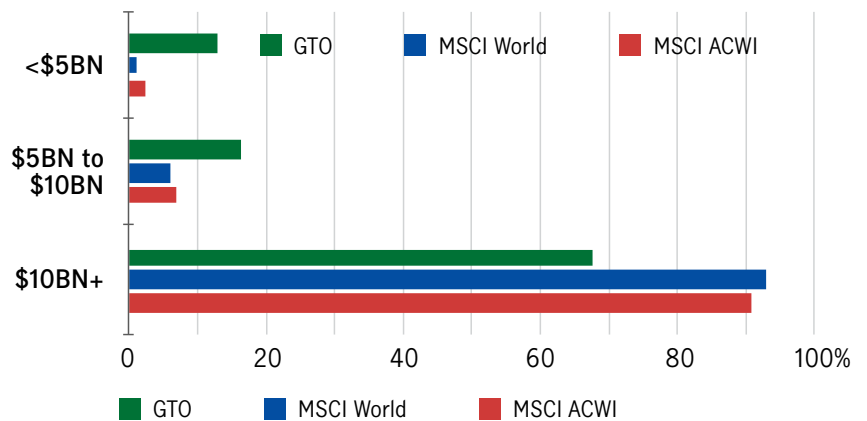
## Unconstrained, forward looking portfolios

The third pillar of our investment DNA can be defined simply as taking an unconstrained or benchmark-agnostic approach. We devote ourselves to finding the best companies within our investment universes on a bottom-up basis. As long as companies meet our minimum liquidity requirements, we don't care which indices they sit in. We want a portfolio of companies that will do well in the future, whatever indices they belong to.

For example, as Fig. 5 shows, our Pictet Global Thematic Opportunities strategy has a greater allocation to small- and mid-cap stocks than either the MSCI World Index or MSCI All Cap World Index. This is purely a residual of our stock selection, as we don't pick out companies based on their size – just the best ones.

**Fig 5: Dare to Be Different**

Pictet Global Thematic Opportunities portfolio market cap breakdown vs global equity indices<sup>4</sup>.



Source: Pictet Asset Management, September 30, 2018

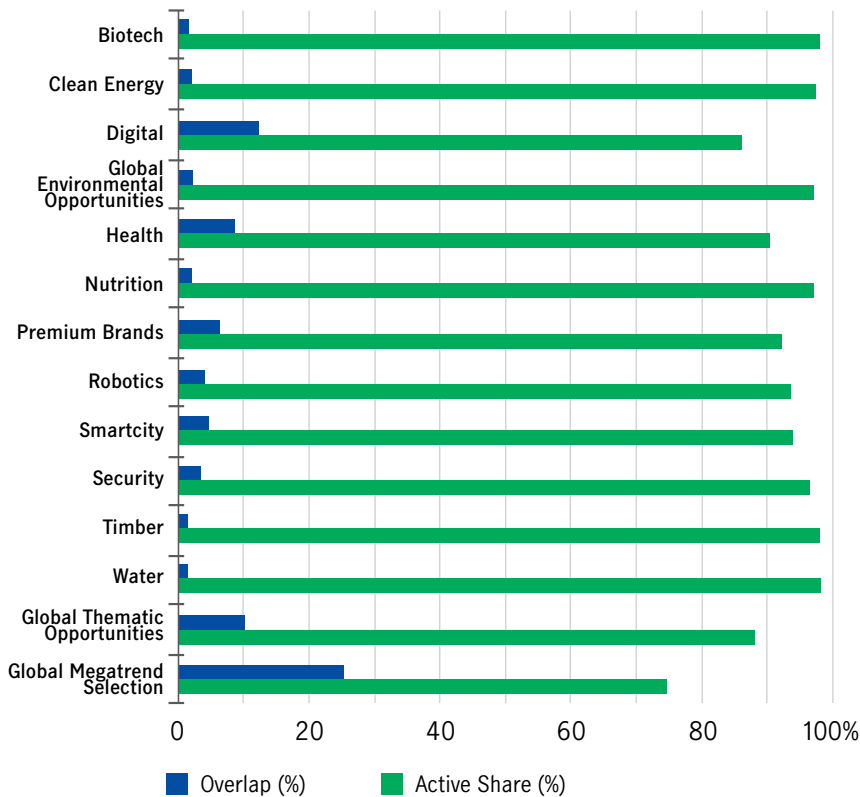
<sup>4</sup> Information provided is not representative of the Manulife Global Thematic Opportunities Fund but is based on the Pictet Global Thematic Opportunities Fund launched Sept. 30, 2016 in Europe which is not available for sale in Canada. The Manulife Global Thematic Opportunities Fund was launched Oct. 17, 2018.

## Low overlap with global equity indices

Further evidence of our unconstrained approach can be found in Fig. 6, which shows the active share and overlap with the MSCI World Index of all of our main thematic equity strategies.

**Fig 6: Dare To Be Different – Part 2**

Overlap and active share of Pictet thematic equity strategies versus MSCI World Index<sup>5</sup>.



Source: Pictet Asset Management, MSCI, Bloomberg, September 30, 2018.  
 Overlap = sum of all overlapping fund holdings with index, adding up the min of the two weights.  
 Active Share = a measure of the percentage of stock holdings that differs from the benchmark index.

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## Written in our genes

In a nutshell, that's the 'DNA' of our thematic strategies: investment themes based on secular growth trends; an investment approach centred on focus and thematic purity; and portfolios that are unconstrained and based on long-term future prospects not short-term noise and speculation.

Of course a thematic approach is not for every investor. Please speak to your advisor. It won't suit anyone subject to a short investment horizon. Nor investors unable to tolerate significant deviations as there are inevitably periods when thematic equities lag equity indices.

But for investors willing and able to escape the herd and take a longer-term view, a thematic approach can offer highly attractive prospects.



To learn more, contact your advisor or visit  
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