Moerus Worldwide Value (MOWNX/MOWIX)

By David Snowball

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"There are a few old, bold—that is, persistently independent—managers out there. Amit Wadhwaney is one of them."

Objective and strategy Moerus Worldwide Value pursues long term capital appreciation, primarily by investing in foreign and domestic common stocks that it believes are deeply undervalued. The portfolio is constructed from the bottom-up through fundamental analysis; which is to say the manager cares about finding 15-50 great stocks with no particular interest in paralleling some indexes' sector, size or country weightings. As of May 31, 2017, the fund is invested in 37 stocks.

Adviser Moerus Capital Management LLC. Moerus is a New York-based investment management company founded in 2015. The firm was founded by Amit Wadhwaney, John Mauro and Michael Campagna, all of whom worked together for nearly a decade at Third Avenue Management. They were joined by a fourth Third Avenue alumnus, Ian Lapey, in 2016.

Manager Amit Wadhwaney. Mr. Wadhwaney is co-founder and Chief Investment Officer, as well as portfolio manager. Prior to Moerus, he was best known as a portfolio manager and partner at **Third Avenue Management LLC** where he managed Third Avenue International Value (TAVIX) from December 2001 to June 2014.

Morningstar's valedictory judgment when Third Avenue announced Mr. Wadhwaney's departure was very positive, noting, "The disciplined execution of his uncommon strategy has made the fund a good diversifier for investor portfolios and supported the fund's ability to limit volatility in a risky category." In addition to an M.B.A. in Finance from The University of Chicago, he holds degrees on economics, chemical engineering and mathematics.

Strategy capacity and closure Moerus estimates that the strategy's capacity is somewhere around $5 billion. Mr. Campagna notes that "This estimate is based on many factors, including liquidity requirements, the areas where we have traditionally found opportunity, our fee structure, as well as the economics of running the business and attracting the quality of employees that we seek." The wild cards would be the rate of inflow (too much money too quickly might not be manageable) and the state of the market, which might dramatically expand or contract their opportunity set. Because the Moerus folks are committed to growing their personal wealth through their investments in the fund, rather than by attracting excess assets which might dilute performance, they judge that their $5 billion estimate is "conservative."

Management's stake in the fund Mr. Wadhwaney has over $1 million invested in the fund. According to the most recent SAI, his personal investment represents 27.49% of the assets in the fund's institutional share class, as of March 6, 2017. As of the end of July 28, 2017, Moerus employees as a group accounted for 11.1% of the total assets of the Moerus Worldwide Value Fund.

Opening date May 31, 2016

Minimum investment $2,500 for "N" class shares, $100,000 for "I" shares

Expense ratio 1.65% for "N" shares and 1.40% for "I" shares, in both cases after contractual waivers which are in effect until at least March 31, 2018. The difference in expenses is that the retail shares carry a 0.25% marketing fee which helps defray the expense of giving investors access through platforms such as Schwab. The fund has assets of $37.2 million, as of July 31, 2017.

Comments Harry Copland, who piloted his first plane in 1911 at the age of 15, is credited with the adage, "There are old pilots and there are bold pilots, but there are no old, bold pilots." (He lived to be 80.) For pilots, deviating from proper procedures by even a little bit is not just a career risk, it's a life risk.

"Moerus offers a rare and intriguing opportunity to invest alongside a distinguished 'aggressive conservative investor.'"

For fund managers, the price of independence is not quite so high: independent managers tend to be unemployed, rather than expired. Running outside the herd frightens investors and absolutely terrifies fund company executives, who worship "sticky assets" above all else. And so most managers, no matter how promising, are eventually tamed into compliant mediocrity. That's evidenced in two distinct ways. First, a July 2017 Morningstar study of the effects of manager changes on a fund's performance finds, well, on average, none. That is, the average manager is an interchangeable cog who contributes no individual value. Second, the "active share" research done by Martijn Cremers and Antti Petajisto finds that only 30% of U.S. fund assets are in funds that are reasonably independent of their benchmarks (80 or above) and only a tenth of assets go to highly active managers (90 or above). Sadly, investors migrate toward, rather than away from, closet indexers when markets turn south.

Independence is hard on managers and investors alike.

Yet there are a few old, bold—that is, persistently independent—managers out there. Third Avenue founder Marty Whitman, who launched the Third Avenue Value Fund (TAVFX) at age 66 and managed it until he was 88, is one. His former protégé Amit Wadhwaney, a youngster at age 63, is another.

Twenty five years into his career as a professional investor, Mr. Wadhwaney, then 62, launched Moerus Worldwide Value as a new expression of the deep-value investing style that Mr. Whitman espoused.

Moerus is a concentrated, deep value fund. The fund brings two distinctions to the table.

First, **the investment strategy is distinctive and disciplined**. All active investors need to determine what a potential investment is likely worth; it's called "price discovery." Almost all investors make their determinations by forecasting what the future holds for a firm: "TechnoZon's Bluetooth division had $50 million in EBITDA, minus a goodwill write-off, last year; based on 2014-16 trends, we're projecting EBITDA growth of 4% in 2017 and 5.2% in 2018 before it levels off to a sustainable 2.4% in the out years, which gives us a fair value of…"

Mr. Wadhwaney considers such projections as fantasies swathed in fiction: earnings numbers are often works of creative writing and the prospect of consistently foreseeing the future is nil.

Instead, his discipline starts with the question, "if we had to sell this entire firm today, based on what it's already accomplished and built, and allowing for any highly-predictable income streams it has, what could we get for it?" He then asks, "and what could we get for it if things starting going bad in a big way?" That gives him a conservative estimate of what the firm's worth; he'll only buy the stock if (a) the firm's attractive and (b) it's selling at a substantial discount to his caustic assessment of the firm's actual value.

He is, at base, looking for reasons not to buy each firm, rather than for reasons to buy them. If he can find a reason to say "no," he immediately and resolutely does. He's joking both about the moniker "Dr. No" and about a playful video made by his associates which shows one of them pretending to be Amit; they accomplished this by wearing a blonde wig (oddly) and tossing corporate reports aside while crying out "no, no … No!" (It was a fund manager's version of Queen's "Another One Bites the Dust.")

"Moerus's two distinctions: a rare and disciplined investment strategy and Mr. Wadhwaney, who does good work.."

There are three significant consequences of his price discipline. First, he's willing to hold substantial amounts of cash when he can't find stocks that meet his stringent valuation and risk management criteria. Currently his cash reserve is 18%. Second, he may follow some firms for five to eight years before moving on them, which suggests that he knows them really well by the time an opportunity presents itself. Third, his discipline intrinsically favors some sorts of businesses— those with real assets and annuity-like cash streams—over others. As of 2/28/2017, he had zero combined exposure to three sectors (tech, healthcare and utilities) that represent 35% of his average peer's portfolio.

Second, **Mr. Wadhwaney does good work**. He posted competitive returns with high degrees of independence and strong downside protection with his previous fund. Morningstar, which has followed him for years, quickly designated Moerus as a Morningstar Prospect and invited him to speak at their 2017 investment conference in Chicago. Moerus Worldwide returned 24.2% in the 12 months ending July 31, 2017, outpacing both its benchmark and peer group by over 500 basis points. That's despite the effects of relatively high start-up expenses and a substantial cash reserve. His median market cap, geographic distribution, asset allocation, and sector allocation are all substantially different from his peers.

Bottom Line Independence is not easy, for manager or for fundholder. It's hard to be out of step, especially when those around you are smugly basking in the illusory safety of passive investments. In the long term, though, success requires discipline and difference. For folks willing to take their obligations as investors seriously—that is, to invest alongside their managers, through thick and thin, based on a fundamental understanding of and agreement with their strategy—Moerus offers a rare and intriguing opportunity to invest alongside (in another of Mr. Whitman's phrases) a distinguished "aggressive conservative investor."

Fund website The Moerus Funds site is perfectly respectable, but folks interested in a bit more detailed understanding of Mr. Wadhwaney's style and strategy might benefit from browsing the "news" page on the Moerus Capital website, too. There are a couple nice interviews and his Investor Memos which might have been judged a bit too much for the casual passerby.

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Fund Returns (as of June 30, 2017):	One year	Since inception[1]
Moerus Worldwide Value Fund (Class Inst.)	21.13%	21.25%
Moerus Worldwide Value Fund (Class N)	20.75%	20.91%
MSCI All-Country World Index (Net)[2]	18.78%	16.58%

1. Since Inception return is annualized. The inception date of the Moerus Worldwide Value Fund is June 1, 2016.

2. The MSCI All Country World Index (Net) is an unmanaged index consisting of 46 country indices comprised of 23 developed and 23 emerging market country indices and is calculated with dividends reinvested after deduction of withholding tax. The Index is a trademark of MSCI Inc. and is not available for direct investment.

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