

Value Investing With Legends

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Viewpoints

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International Value team portfolio manager David Samra has a passion for value investing. He recently sat down with Tano Santos, the David L. and Elsie M. Dodd Professor of Finance at the Heilbrunn Center for Graham and Dodd Investing at Columbia Business School, to discuss his career and the past, present and future of value investing.



N. David Samra
Portfolio Manager

30 Years Investment
Experience

Value investing is more than an investment strategy. It's a fundamental way of thinking about finance. Welcome to Value Investing with Legends, a podcast hosted by Tano Santos, the David L. and Elsie M. Dodd Professor of Finance at the Heilbrunn Center for Graham and Dodd Investing at Columbia Business School.

Our mission today is to promote the study and practice of Graham and Dodd's original investing principles, and to improve investing with world class education, research, and practitioner academic dialogue. In this podcast, you will hear from some of the world's greatest investors, their views on the investment management industry, how they develop their investment process, and how they see the field changing over time. To learn more and to subscribe to this podcast, please visit grahamanddodd.com.

Prof. Santos Welcome to our first Value Investing with Legends podcast of 2020. I'm your host, Tano Santos, a David and Elsie Dodd Professor of Finance at Columbia Business School and the faculty director of the Heilbrunn Center for Graham and Dodd Investing.

It is always a pleasure to welcome to our podcast an alum of Columbia Business School, as it is the case with my guest today. I always say that Columbia Business School is a wonderful community of students, faculty, and administrators, but it is our students and alums that carry the values and ideas of this remarkable institution into the broader world. If CBS is impactful, it is thanks to them.

We have had a few of those alums in this podcast—Mario Gabelli, Jenny Wallace, Lee Cooperman—and today, we welcome David Samra, MBA 1993. David, welcome to the Value Investing with Legends podcast.

Mr. Samra Thank you for having me, Tano.

Prof. Santos So, David Samra is the managing director of Artisan Partners and the founding partner of the Artisan Partners International Value Team. He joined the firm in 2002 as Lead Portfolio Manager. Before joining Artisan Partners in May 2002, David was a portfolio manager and a senior analyst in international equities in one of the legendary names in value investing, Harris Associates, from August 1997 through May 2002. So, David, welcome again.

I want to start, as we always do in this podcast, a little bit with your education, your background, where did you get this career in investing from, what was your education like, and what drove you to this? So why don't you tell us a little bit about that, about your background, your college education?

A R T I S A N



P A R T N E R S

Mr. Samra I grew up in Massachusetts to a family of, I guess I would call them blue-collar entrepreneurs. Both my parents had small businesses doing mainly labor. And we grew up in a modest suburb of Boston called Medford, Massachusetts, and the ambition inside of me was to try to prosper in business. So, it was very simple for me, after coming out of high school, to aim at getting an education with a business background.

Prof. Santos And that's how you ended up at Bentley, which has a wonderful tradition of business education, I guess?

Mr. Samra It does. It does. And I think the reputation is growing over time. When I entered Bentley College, it was coming off of a history of being more or less an accounting trade school. And so, what they would do is put people through a basic undergraduate education focused on accounting, and put people through the CPA track, and they were a great recruiting platform for the big five accounting firms.

Prof. Santos It's a wonderful institution. They've been at this for more than a century now. They were real pioneers in this.

Mr. Samra Yes, and when I got there, they had started to branch out into other majors, one of which was finance, which I found to be far more interesting than the basic accounting classes. The accounting classes were terrific. I had a dual focus, both on finance and accounting, and, of course, accounting is the language of money, and you can't prosper as a money manager, at least certainly not a value investor, without having a solid grounding in accounting, but I did find the finance courses to be far more interesting, specifically the security analysis courses.

Prof. Santos That's where you got the asset management bug, so to speak, is that Bentley was the place where you discovered your vocation as an asset manager, yes?

Mr. Samra Yeah, and the finance professors dressed better than the accounting professors, so.

Prof. Santos We definitely do.

Mr. Samra And so, it made it attractive. And it was sort of interesting that, similar to what happens here at Columbia Business School, you would have an assigned project to analyze a company, to go through the whole process—building a financial model, doing some fundamental homework around the business, and coming to some determination as to whether or not you think it's a good investment.

And we worked in teams, and there was a fellow on my team, and we had to pick some securities in the pharmaceutical industry. And at the time, the pharmaceutical industry was a growth industry. And my partner picked a company called Merck, which is still around, which was a very expensive growth stock, and I picked a company called—which is now gone—called A. H. Robins.

And A. H. Robins was a troubled stock. They had two main products. One was Robitussin, which is a cough medicine, which is perfectly fine, very profitable, very valuable product. Yeah, a wonderful brand. And the other one was an IUD, which had sickened several women who had used it, and they were getting sued, and as a result, the share price undervalued Robitussin. And I don't know why I'm wired the way that I am.

Prof. Santos Yeah, so it's genetic.

Mr. Samra Yeah, it was just much more attractive to me to look at something and see that, well, if the liability associated with this product ends up being far lower than what's being implied in the share price, I'm basically getting Robitussin at a very low earnings multiple, and that looked like a very good risk/reward. So, again, I don't know why I was wired that way and still am wired that way, but that was the beginnings of my interest in value investing.

Prof. Santos Before we explore that even more deeply, so you graduate from Bentley. What do you do next?

Mr. Samra So, I had worked my way through school. I came out, and I had, ironically, a couple of accounting jobs, and that evolved into a job working as a certified financial planner, where I was trying to get as close as possible to the money management world.

I was also at the time running a small investment club. We had a partnership. Myself and a number of my friends would contribute monthly a sum of money. And we experimented. We experimented with investing, and we did everything from—we bought growth stocks. We bought value stocks. We played option strategies. So, it was a very experimental time for me to learn on my own on how to manage money, how to allocate capital, and how to think about returns, and what works and what doesn't work.

- Prof. Santos** That period of prudent experimentation, where you're not investing an inordinate amount of money experimentally—I think that's super useful to actually develop a sense of, what are your biases, what are the things that you're attracted to, what is that you like in a particular stock, and so on and so forth.
- Mr. Samra** It still hurt when we lost money, even when it's relatively small sums.
- Prof. Santos** OK. I'm sure. Oh yeah. I have plenty of experience with that as well.
- Mr. Samra** And somebody that I worked for was an alum of Columbia Business School, and I had been expressing interest to her in the school and value investing, generally speaking. And so, I applied to Columbia Business School, and I think I was probably the last person admitted in 1991. I think I got my letter in August off the wait list. And I found myself here in September, feeling very humbled and very privileged to have been here.
- Prof. Santos** So, I mean, it's wonderful that you're here. One of the things that I think when I was thinking about this interview is that you came at a very peculiar moment at Columbia Business School, because Bruce Greenwald, whom we had last in the podcast had not launched the value investing program. So I read somewhere in an interview with you that essentially, what we were teaching at the time was kind of market efficiency, I guess how to build the screens or the quant view of asset markets, that this is efficient, there is nothing for you to do. I'm curious about that kind of intellectual experience that you had. You were, in a way, came at that moment where Columbia is about to turn, so to speak, and Bruce is about to change and rediscover, so to speak, the long tradition in teaching value investing that we have here, but you kind of missed that a little bit. So, tell us a little bit about that.
- Mr. Samra** Yeah, I was a little bit early.
- Prof. Santos** Right.
- Mr. Samra** And sort of early and late.
- Prof. Santos** It doesn't seem to have hurt you at all, by the way, so.
- Mr. Samra** In fact, in some ways it benefited me enormously. So, first, there were a limited number of fundamental investing classes, which I was primarily interested in. So, you had to pick and choose from what was available, and there was an adjunct professor here at the time by the name of Joel Stern, and Joel was a partner in a company called Stern Stewart, and Bennett Stewart had written the book *Quest for Value*. And that class turned out to be enormously helpful, because what he effectively taught was the difference between a good business and a bad business. He was an efficient markets guy, but that was OK. What he did provide for me specifically was the financial construct and the understanding of how wealth compounds at a rapid rate when you own a great business.
- And that is when you read *The Intelligent Investor* and you read what Buffett has written about historically, and how he evolved once Charlie Munger started to have some influence into him, it's not easy to put a financial framework around it, and it wasn't commonly taught. So, I was able—because I was wired a certain way—to be interested in value investing, because I was working with Mario Gabelli on Fridays.
- Prof. Santos** Oh, that I didn't know. So, you had like an internship with Mario?
- Mr. Samra** Yeah, he would hire a number of students to come, because we didn't have classes on Friday. So, I would go there and work with him on Fridays. And I was able to take that academic experience and marry it with buying securities at a significant discount to intrinsic value, which eventually formed the basis of the philosophy that we've been using at Artisan for the last 18 years. So, in a way, the fact that the school had lost its basis of value investing forced me into this classroom that created benefits that I've used in my career since I've left the business school.
- Prof. Santos** Very good. So obviously, we want to come back at this kind of implementation of these ideas shortly. Before that, so you graduate from Columbia Business School and you go to Montgomery. What was Montgomery at the time, and what were your responsibilities there? What is that you first did after leaving Columbia Business School?
- Mr. Samra** Montgomery Securities was a Silicon Valley-oriented broker-dealer—let's say a medium-sized broker-dealer—and they started up an asset management division, which did not have an international platform. I was hired by a fellow who I had met to come out and help them start an international investing platform. So, this is 1993. There were only really a few other shops that were investing actively outside of the United States at that time.

Prof. Santos So, can I ask you briefly about this, because this is something that you immediately notice about your career is that from the very beginning, you had this focus? Where does this come from? I mean, when do you—we had Tom Russo in this podcast, and he was very early on as well on that kind of broader outlook. There's a big world out there. There are great opportunities out there. It's easier sometimes because you don't have these tough competitors that we have in the United States to invest. How do you—was it something you had from the very beginning, or something that you thought it was a wonderful opportunity?

Mr. Samra So, while I was here at Columbia Business School, I was a teaching assistant in the International Accounting class. And when I had my summer internship at The Boston Company in Boston, I would go, whenever the international manager there had a meeting with a management team that would come in, I would go to those meetings because I was curious, and I got to know the international manager who eventually left the Boston company and started this organization out at Montgomery.

I had had other job offers before I left. One of them was in bankruptcy investing, which is a natural inclination for a value investor. However, we were coming out of a recession in 1993, and I thought, well, I might be the last man in bankruptcy investing, but I'm going to be the first man in international investing. So, I looked at it. It paid much less, but it was a long-term opportunity for me to get involved in a part of the market that was far less efficient and, quite frankly, far more interesting, I thought, than spending a lot of my time looking at legal documents.

Prof. Santos So, and your responsibilities at Montgomery Securities analyst for international stocks—that's kind of a broad definition of what you were doing there. How long were you there?

Mr. Samra I was there for four years. It was a successful organization. We started with just about nothing and built it into a few billion dollars. The investment performance was very good.

Prof. Santos Did you have any portfolio managing responsibilities while at Montgomery Securities or no?

Mr. Samra A little bit. But most of my time was spent doing research. And it was a great place to work for me, because the people that I worked for had a lot of trust and confidence, and they gave me the ability to do whatever I needed to do in order to find a security, and back then, it was very hard to get a screening tool. We didn't really have the type of databases that we have now, and most of the databases that were available were looking at US securities, not non-US securities.

So, this is a little bit embarrassing, but what I did is I took the Tweedy, Browne Global Value Fund portfolio, and I would spend weeks at a time running around the world, visiting the companies that they owned in their portfolio. And if you think about having a job where somebody gives you that type of freedom, and what I learned by spending weeks and weeks at a time out visiting with management teams in parts of the world where nobody else was doing this, it was very good training grounds and helped push my career along a lot more quickly than if I had been contained in an office.

Prof. Santos A large office, where you get a little bit lost. Absolutely.

Mr. Samra Yeah, or doing assignments.

Prof. Santos Yeah, exactly. So, we still do that, by the way. We still take the portfolios of some distinguished investors, including yours, and we look at them, and say, why are they holding this. So, you're there for four years, and then you move to one of the great names in the industry, Harris Associates. How did that come about? What did you do there? Were you initially an analyst? Well, you ended up being—managing, being a PM at Harris Associates. But was that originally there?

Mr. Samra Again, it was mostly as an analyst. I spent almost all my time as an analyst. And it was a much more comfortable home for me. The folks at Montgomery didn't have a distinct value discipline. When I arrived at Harris Associates, I worked with a famous value investor—his name is David Herro—and the way that we looked at securities was almost exactly the same.

I would say that the big differentiating factor is—what I alluded to earlier—is a focus on better businesses. So David, I would say, was more of a traditional value investor, where he considered multiples, and was very much a contrarian, and a very good investor—still is a very good investor, in fact—and I brought to the table more of a focus on better businesses and understanding. If you have Google and General Motors as a comparison and they're both at eight times earnings, it's pretty easy to tell that you want to put all your money in Google, and going through a process of working inside an organization and being allowed to exercise that philosophy, and once you start buying securities that have those features in an inefficient marketplace—to get back to Tom's point—where you could find a fabulous business like Nestlé or L'Oréal trading at very attractive valuations, where excess assets weren't considered, and they were great businesses that were generating cash that could compound wealth over time, you're in a somewhat unique position that in this day and age is very, very difficult to find.

Prof. Santos I think that's a very important insight, and one that I stress constantly to the students that, in a way, there are two faces to the value investing stories, so to speak. There's kind of this initial phase where you're just focusing on valuation and downside protection and asset value protection and things like this, and where the quality of the business was not paramount, and Ben Graham obviously was a brilliant man with a phenomenal insight, but there's surprisingly little economics almost about the businesses in his writings, I would say. And I always think that what Munger brought to the Buffett discipline is precisely that focus on the quality of the business, that you can buy that business. If it's better, it's going to compound it's going to do these wonderful value creations for you for a long time, essentially, do the capital allocation for you, almost.

So, it's interesting to see that contrast between a traditional value investor and a modern value investor, as they call it, with a focus on the quality of the business.

Mr. Samra It's very interesting that when we started in 2002, and I looked at—

Prof. Santos Now in Artisan?

Mr. Samra In Artisan, yeah. We looked at the competitors set and what they were doing, including at my prior firm. There are very few value investors who actually had evolved. I even think Jean-Marie [Eveillard], I've heard him talk about how long it took him to make that evolution, and it really started to change after the financial crisis, because so many value investors had such bad performance in the middle of the crisis, because there are two underlying concepts to value investing.

One is, of course, generating returns—that's what we're all here to do—but the second component is managing risk. And when you think about risk embedded inside of each and every security in each and every business, one of the main risks that you subject yourself, if you use that more traditional form of value investing, is time value of money risk. Inflation is ever present, and if you own a business over a number of years and the underlying value of the business is not growing, your purchasing power is very simply being eroded.

So, when we started in 2002, we had that playing field. It's a very nuanced playing field versus the playing field I had in 1993. 1993, all I needed was information. I just had to go, and if I had the information and nobody else did, I had a big leg up. By the time I got to 2002, we had the internet. We had the development of capital markets. Information became freely available at a fast pace. You needed a different leg up than the one that I had initially, and our leg up was we were focused on better quality businesses that were still at a cheap price, running a very focused portfolio.

And then the financial crisis happened, and all my competitors went in that direction, and then it became a much, much more competitive world.

Prof. Santos So, I'm quite taken by this, because I always thought, when I got into value investing and started reading and thinking through it, that this was always kind of a weakness of the traditional value investing approach. So, there was this, obviously, margin of safety and preservation of capital, which are powerful ideas—the idea of robustness—that you want to think about the downside, but in a way, not in one's view of risks beyond that. And when you run a concentrated portfolio, you really need to understand the risk of that individual position you have in that company. And that you will have to have a taxonomy in your head about how to classify those risks.

Which are the ones that I can take, and which ones are the ones that I stay away from, because I don't understand them. Or they correlate in a funny way with the rest of my portfolio. So that understanding—I always thought that it was a weakness of the traditional value approach.

I entirely agree with you. We'll come back to this issue of risk management, because I know it's dear to your heart. And I want to discuss it with you a little bit later. So, Harris Associates—for how many years were you there?

Mr. Samra I was there for five years.

Prof. Santos Five years. And you end up being a portfolio manager, core portfolio manager of anything. You have any responsibilities there?

Mr. Samra Yeah, we had launched a global value fund towards the end of my tenure at Harris Associates. For the main part, I was selecting equities that were on a pre-approved list. There was a little bit of asset allocation that was going on. But the thrust of what I was doing was as an analyst.

Prof. Santos And now we move to Artisan with bigger responsibilities, so to speak, from the very beginning. How did that come about? And how was that opportunity?

Mr. Samra Artisan had been looking to get in the international value business. They already had an international fund at the time. And the CEO there had spent several years looking for someone. They have a very robust approach at selecting managers at Artisan.

At that time, they had never hired someone that didn't have a direct track record. So, they took a risk that they hadn't taken before when they hired me. Because I did not have a direct track record.

And they saw that there was a business opportunity to build a platform for international value, because the marketplace of investors were starting to put managers into individual boxes. And in the United States, you had domestic-growth managers and domestic-value managers. Outside the United States, they were mainly just international managers without a specific discipline. So, they were interested in it from a business standpoint. I was interested in evolving, taking the system that I had developed over the nine years that I had been an analyst. Putting it together into a strategy.

And so, the marriage worked out very well. We both got what we wanted out of it. However, what I would say is that, when I arrived there, I never thought I would manage much more than a billion or maybe two billion dollars.

Prof. Santos Well, it got a little larger than that.

Mr. Samra Yeah, I think that in a sense the financial crisis allowed for that. As a value investor with relatively small amounts of capital, you have the benefit of focusing on smaller companies, which you can buy, generally speaking, over most periods of time, you can buy extraordinary values in smaller companies.

But during the financial crisis, of course, you had the ability to buy pretty much any company that you wanted. And recognizing that, recognizing your ability and that you were buying something that was special at a great price, created this opportunity to deploy a lot more capital.

Prof. Santos So, can I ask you then, let's talk a little bit about your experience. You are that investor that went through two massive cycles. One, the tech bubble as an analyst in Harris. You were still there. And then the global financial crisis. And before we run out of time, I wanted to ask you this question, which is: I mean, these are two big things in the history of financial history of the United States over the last 50 years, I would say these are really remarkable episodes. And when I was preparing this interview, I was thinking, well, I just got my first job at the University of Chicago in the mid-90s. I had many interesting discussions in the birthplace of market efficiency about the tech bubble. And of course, the global financial crisis.

A faculty member at Columbia Business School had a big impact on how economists think about the economy, the comings and goings of financial markets, and so on and so forth. What were the lessons? And how did they inform your approach to investing? These two big things in the recent economic and financial history, not just of the United States, of the world.

Mr. Samra There are two lessons. One is on the risk-management side. So, one of the other components that we look for, aside from a cheap stock and a good business, is a very strong balance sheet. And if you own a company that has a very strong balance sheet, and the economic environment gets difficult, that company—if the management team is good and wise and bold and experienced—they can use that crisis effectively to take that capital, deploy it, and take market share from their competitors.

And once you come out of one of those difficult economic periods, the pace at which value is created is accelerated dramatically, putting you as an investor in a position to prosper very nicely. So that's one.

And then second is this—so you have a great business with a good balance sheet on one hand, and as you enter the crisis, maybe some of those great businesses hold up really well. But on the other hand, at our core, we are value investors. And price drives our behavior.

And so, the willingness to sell a great business that has held up really well in the middle of a very difficult economic period, and purchase businesses that are just trading at absurdly cheap prices—maybe they're not as high quality. But that balance between price and quality—you have to weigh that and put yourself in the best position from a risk-reward profile.

And that's really a reflection of what happened during the financial crisis. The tech bubble was a little bit different in that, gifts were being handed to you. And you didn't know if you were a dinosaur. But it certainly seemed that other people were doing things that were irrational.

Mr. Samra We all lived in very rational economic-driven world. And Cisco Systems, at 45- or 50-times earnings, didn't seem rational or reasonable in any way. And so, we were just waiting. Our assets were going out the door. You weren't making as much money as you had been. And everybody in the value-investing world was suffering as a result.

So, you did have company. And you knew that at some point it is likely to end. You just didn't know when. And so, we just kept on buying.

And at one point, I think, we collectively, as the investors of what was then the Oakmark International Small Cap Fund, I think we were sort of singlehandedly the only people putting money into the fund in the middle of that crisis. The tech bubble was an interesting period, but very, very different than what happened during the financial crisis.

Prof. Santos Oh, yeah, definitely. You could see the tech bubble—in a way it was one of those speculative periods that obviously, a lot of wealth destruction associated with the bust. But a lot of it was funded with equity, so the adjustment mechanism was not as painful as it was during the global financial crisis, where you had to renegotiate essentially trillions of dollars of fixed liabilities across the world. So, let's start talking, then, a little bit about process and how you guys go about this at Artisan?

So, something that interests me quite a bit is that you were very early on—I want to start thinking about, talking with you about search. And how you locate good ideas. And you've talked about this in a couple of interviews, the use of screens that you've used for a long time, which is now a standard. It wasn't 25 years ago. We always forget about this.

We run it with the students. We do a lot of fun things with them. But of course, this was new stuff in the mid-90s say. So, tell us a little bit about that. How you guys go about—inside Artisan, about locating good ideas, finding them? Where does this idea-generation come from?

Mr. Samra I would say it's evolved over time. As I mentioned earlier, early in my career, these databases weren't available. By the time I showed up at Artisan, they were very available. And we would run screens, some you would expect a value investor to run. Low P/E, low price to book, high dividend yield.

And some you wouldn't expect a value investor to run. Companies with high return on capital employed and high operating profitability. And that allowed us to get to know the better businesses. Over time we've added searches in newspapers looking for things like profit warnings, spin-offs, de-mergers, rights offerings.

Prof. Santos Screens run on textual kind of stuff?

Mr. Samra Yeah, there's a search inside newspapers or other publications. And I think, now we're at the point where we're searching inside transcripts to find keywords. So, you've had to get more creative about finding securities where some owner is being disenfranchised for some reason. And is selling the security without paying too much attention to the price.

But I have to say, Tano, the most fruitful method that we have of finding securities is by, what I call, knowing our markets. So, we spend a lot of time out on the road, in our assigned countries, visiting companies.

And we'll go for two weeks at a time, similar to the way that I did at the very start of my career. And we'll visit 30 companies over the course of a couple of weeks. And we'll visit the burnt-out, dirt-cheap businesses that look like we could potentially buy them.

But we oftentimes will be visiting very good companies, companies that are highly profitable, that are growing, have able management teams. They're simply not at a price that we would be interested in buying today.

Prof. Santos But you monitor them, and you follow them to see, you have that folder that you can pull out the moment they get attractive from a valuation point of view, and you're ready to deploy the capital quickly, I assume.

Mr. Samra Yeah, and we've even abandoned the folder. And we have an electronic note system.

Prof. Santos Oh, you make me feel old.

Mr. Samra And we have an email system, because we put a preliminary evaluation on these businesses. And when the share price falls within 10% of our buy price—we never buy at a fair price, of course. We buy at a large discount.

And when it falls within 10% of our buy price, an email comes out. We all look at it, and say, OK, let's go in and figure out what's happening with this business. So that's—knowing the marketplace in which you're investing is a very robust way to find ideas.

Prof. Santos And when you think about—so this we can touch upon a little bit. The portfolio. Is this specialization that you guys pursue a geographic one? An industry one? How do you think about knowledge acquisition inside Artisan?

Mr. Samra Yeah. I've always been a generalist in my career. And the way that I've organized the research team at Artisan is by geography. Everybody is a generalist, and everybody has a very large geographic coverage area. So, the European analysts have all of Europe, and the Asian analysts have all of Asia.

And so, it's developed markets and emerging markets, of course. Those markets have very different characteristics. And so, the objective there is to build investors, people who understand multiple business models, and effectively can go where stocks are cheap.

I don't want people thinking on a relative basis. This is relatively cheap. I want people thinking, if I buy this security, I'm going to enhance my purchasing power over the course of my investment horizon.

So, I want to go where I can find a security where I believe I can generate wealth over time. So, there is no sort of theme-based investing, there's no allocation by country, and there is no industry focus. But very simply, we go out to the universe, and we try to find the most undervalued securities of good quality companies that we can find.

Prof. Santos In that particular geography?

Mr. Samra Yeah.

Prof. Santos Let me ask you a little bit about this then. So, it's not that you know, I've had investors come into class saying, well, the way I think about this, I think a particular trend is in place: consumer trend or a technological trend or a regulatory trend.

I try to understand it. And then you know, I develop this mental model of which are the companies that stand to benefit or perhaps not in this particular trend. And then I organize part of my portfolio, however much capital I can deploy with that particular idea around a thorough understanding of these long-term dynamics that can be very subtle.

These nations are drinking more coffee, or Europeans are exercising more. Those type of things. Then I tried to think a little bit about, how can those things help organizing my portfolio? None of that whatsoever? It's just a country, a specific kind of analysis that you guys pursue? Regional specific?

Mr. Samra Yeah. It's more company specific. So even if there's some underlying trend. For example, people are aging, and they need more health care. Within that stream of healthcare, stocks that are available outside the United States, we're only going to get involved when there is some dislocation, some idiosyncratic issue with the business that's creating a situation where we can come in and buy it at a meaningful discount.

So, we don't think about themes all that much. We want something that has been really knocked off its post, rather than trying to reduce the amount of certainty as to whether or not that theme is going to create more economics. We would rather enjoy the theme if it comes, but because we're buying a security at a big discount, even if it doesn't come, we still stand to make a very good return.

Prof. Santos It's almost like an additional risk-management layer on the process. I understand. So, can we talk a little bit about valuation and how you approach this. So, let's assume you've got that idea. You are happy with what you are seeing in terms of the quality of the business, which is a precondition, almost for you to invest in that particular company.

And now you have to decide, well, I have to go in and see that, indeed, they have the ability to redeploy the capital. How do you go about that process of assessing the return on invested capital? The qualitative aspects associated with the competitive position of the industry, of the company and the industry in which it operates? How do you go about that process of valuation and economic understanding of the business operations of the firm?

Mr. Samra I would put us in the category of reasonably detailed analysts. We start with all the legal information that's available to us. The annual reports or 10K like publications that we get from companies. And we build long-term financial models. It's not as different anymore, but there are still big differences in accounting standards from country to country. So, we try to drill everything down to the free cash flow a company generates.

And we're actively in dialogue with the companies that we're looking at. We're actively in dialogue with their competitors. We'll talk to customers, former employees, consultants, substitutable products. We will talk to anyone who can help us understand what is the normalized earnings power of that business.

Mr. Samra Now there is another overlay, which comes back to corporate governance. Because governance standards, legal standards, protections for you as a minority shareholder, are also very different around the globe. And so, we want to make sure within that country, what are our shareholder rights? Who's on the board of directors? Who are the controlling shareholders? What are the incentive systems?

European executives are paid a lot less than American executives. And one of the risks that is sort of hard to see from the outside is, if I'm a European executive, and I'm doing a fabulous job for my company, creating a lot of value, it's very easy for a US Company to go over there and poach them. And you lose your executive.

So, there are a lot of considerations that go simply beyond the fundamental analysis. But we spend a lot of time in these markets traveling, visiting companies. But I would say that that has also changed over time. Whereas, as I mentioned, initially, you just had to go there and get the information. Today you have to be a superb business analyst in order to be competitive. And a lot of that work can be done much more effectively in the office.

Prof. Santos This is a very important point that Bruce and I stress it constantly with the students. That it seems that, in a way, the better value investor today is more of an economist than it used to be. I mean, you really, really have to understand well the economics of the firm, of the industry, competitive dynamics.

Those things have become absolutely paramount, right? I find myself in the classroom spending more and more time talking with the students about that than actually the valuation itself. Which, of course, we have to know. We have to learn. We have to build those models. We have to understand the accounting, absolutely.

But it looks to me like the competitive edge going forward is going to be these kind of very specialized understanding of the particular economics of the firm. Is that true?

Mr. Samra Yeah, and I think that being a refined investor has always demanded that you truly understand the fundamentals of the business that you're getting involved with. The latest buzzword, of course, is innovation. You've had innovation disrupting many industries, especially some of these older value-oriented stocks, even to the point where things like cigarettes have been innovated.

And as I said, it requires an analytical skill set that goes beyond just collecting the information. It's understanding a business, understanding the people, understanding that industry dynamic. And this is what we spend all of our time on.

Prof. Santos It sounds like, actually, a lot of fun.

So, we always finish these conversations, David, talking about the future of value investing, which I'm sure comes up with you as well in many interviews and conversations. The subject comes up often when I sit in panels and in classroom as well. So, I want to finish with this.

There's been obviously a lot of challenges lately in some of the spaces in which value investors traditionally operate. What is your view on this? Or let's divide the question in two parts. What do you think is kind of going on in financial markets? What is the overall outlook that you have for the development of financial markets? And second, what do you think is going on specifically with value investing? And whether we are at the end of the value investing?

Mr. Samra Luckily, we're here at Columbia Business School, where people like to run financial models. And if you take a business that has a relatively slow growth rate and stick it in your DCF and, let's say at a 12% discount rate. And then take a business that grows very rapidly and put it in the model at a 12% discount rate. And then drop that discount rate down to 5%. And you will see what happens to the valuation of the growth company versus the value company.

And if I had to boil it down to a mathematical model, since the financial crisis, you've had liquidity coming into the marketplace. And you've had very, very low interest rates, to the point where we have record amounts of bonds trading at negative yields. And these are your risk-free comparisons, your risk-free bund, trading at a negative yield.

And that, by its very nature, is going to benefit growth stocks. If you're looking for reversion to the mean in that cycle, you're basically making a call on interest rates. I think all boats have risen, even what we would consider traditional value securities.

I think that it's incumbent upon all investors, value investors included, to be able to understand the environment that you're working in, stick to your discipline and really fall back on the fundamental underpinning of value investing. I need to find a security where I can generate wealth, and both generate a good return and manage risk.

Mr. Samra And I don't think that the value of a business is the present value of its future cash flows is ever going away. And I don't think buying an A.H. Robbins below what it's really worth is ever going to go away as a very strong disciplined system to generate returns and manage risk over time. It's financially and mathematically impossible for it to go away.

Now what I would say is, getting back to your comments about people employing mathematical models in order to drive investment returns, that there is a mass market part of the investable universe. So, getting back to what I do as a businessman, where the mass market is being sold passive products and ETFs where decisions are made based on liquidity movements. And they're not thinking decisions.

And they're being pushed out of active management. Now I know active management hasn't shrouded itself in excellence over the course of my career. But of course, there are active managers that have done very well. And removing your—whether it be your retirement fund or your kid's education fund into a product that is driven by liquidity seems to be unfortunate for that part of the marketplace. So, I think value investing will survive. But that part of the marketplace is unlikely to come back to active management.

Prof. Santos Right. So, I entirely agree with you. I mean it's difficult to contemplate a world without active investors actually doing this, visiting the company, talking with management, reading the hour reports, trying to come up with an economic model of the firm. It's difficult to contemplate that ever going away, because who is going to be impounding the information in prices somehow.

Mr. Samra Systems are human based.

Prof. Santos Yeah. David, thank you very much for this wonderful conversation.

Mr. Samra Thank you. Again, I'm humbled to be here.

Prof. Santos No, thank you so much for coming.

Mr. Samra Thank you very much.

Prof. Santos Thank you.

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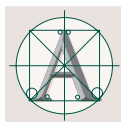
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