Roger Montgomery prefers growth businesses and avoids resources. **Michele Mossop**

by Philip Baker Vesna Poljak

Roger Montgomery decided he was going to be a fund manager when the Gulf War broke out in 1990.

At the time, he was working at the old Price Waterhouse on a summer job auditing the Bank of Singapore's bond trades from their dealing room. He figured out he was on the wrong side of the floor.

"It became apparent to me instantly that what I wanted to do was get involved in financial markets and not accounting. It struck me that accounting was looking at what has passed or what has happened, and yet financial markets were looking at what was going to happen," he recalls.

After a year at F.W. Holst he moved on to BT in Sydney where highly successful investors Ivan Ritossa, Kerr Neilson and Richard Farleigh commanded the morning meeting. His eponymous investment house did not start until 2010, a few years after he exited Clime in 2007.


Roger Montgomery is also an amateur mountain biker and climber - he has scaled in record time Mount Kinabalu, Southeast Asia's tallest peak in Borneo. **supplied**

In between, he wrote a book, *Value.able,* and was encouraged to get back into managing money by fellow value investors Chris Cuffe, Chris Mackay and Hamish Douglass. Mr Mackay's philanthropic fund Third Link was his first investor, and Magellan (co-founded by Mr Mackay and Mr Douglass) owns a stake in the Montgomery Investment Management business. "They are our only external shareholder and we are their only other boutique that they have a stake in."

The way Montgomery sees markets, the short-term is a popularity contest but the long-term is where the real money is made.

"We believe that it's pretty easy to work out how a company increases in value, not its price necessarily, but its value, and the way it does that is by retaining capital and generating very high rates of return on that," he says.

"So even if the stockmarket were turned off between now and [10 years' time] I don't need to worry about Brexit, I don't have to worry about China, I don't need to worry about the Middle East... I can be comfortable in the knowledge that while the price will be volatile, the value of the business will rise and in the long run the market does a very good job of reflecting the changing value of a business.

"Really what we are talking about is investing in businesses rather than picking stocks. So to us, picking stocks is a little bit like betting on up and down. Which is tantamount to betting on black and red at the casino. And what we're doing is we care less about that and more about the sustainability of the underlying business. Rather than using the sharemarket to bet on whether something is going up or down, we're treating the sharemarket as a venue where we can buy pieces of businesses, fantastic businesses, that also happen to be listed here in Australia."

The fund manager and amateur mountain biker and climber - he has scaled in record time Mount Kinabalu, Southeast Asia's tallest peak in Borneo as well as other mountains in Austria - says that out of the 1800 businesses that are listed in Australia only 600 actually make a profit.

"There's a disproportionately large number of businesses in Australia that out of the profitable group generate high rates of return on equity because over time what tends to happen in Australia at least, we end up with oligopolies, duopolies and monopolies, whether it be in supermarkets, or airlines or banking," Montgomery says. "Once businesses reach that point where they have got a moat that is really insurmountable, they can sustain those high rates of return on equity for quite some time." REA Group and Challenger are two examples.

Montgomery also runs an international strategy managed by Andrew Macken, which has enjoyed some huge returns on short bets. They have targeted the struggling luxury stock Prada and Outerwall, the company that owns the Redbox chain of DVD vending machines.

He declines to name his Australian short bets. "We're not a Bill Ackman, putting a short on and then telling the world about it. One of the flaws in that particular model is if you publish a 40-page dissertation on why you are short and then distribute to the world on every newsstand, and then when new info comes to hand it gets very hard to change your view."

Montgomery Investment Management has just over $1 billion under management in domestic and global equities, while the Montgomery Fund has returned 73 per cent, after fees and including dividends, since it started in August 2012, compared to a 37 per cent gain in the ASX 300 Accumulation Index.

Right now the fund has about 23 per cent in cash, and it's top five holdings are REA Group ,Challenger Financial, Commonwealth Bank, CSL and TPG Telecom.

Mining stocks, however, have never been a good fit for Montgomery's investment philosophy.

"The best business to own is a business that can take large amounts of incremental capital and employ it at very high rates of return," he says. "Mining companies are the antithesis of that. They're not able to tell you what the return on the money that they take from owners to reinvest is going to be. And the most valuable competitive advantage is the ability to raise the price of your product without having a detrimental impact on unit sales volume.

"We love businesses that can raise their prices even in the face of excess supply. So an example of that is Isentia or REA or Tiffany's." The jeweller charges more for diamonds than its peers, "but people still cross the road to buy their diamonds from Tiffany's".

Australia is in for a long election campaign in 2016 but Montgomery shrugs it off, arguing it is not a factor for his portfolio. "There's going to be an election every three years so if [a business] is going to suffer every time there is an election, why would you invest in that?"