

Katana reveals its secret: stop looking for perfection

Fund managers Perth team's outperformance based on deep research and acceptance every stock has its issues.

Vesna Poljak

After a decade in stockbroking, Romano Sala Tenna had a revelation: there was no such thing as a perfect company.

"I gave up," the fund manager recalls. "Every company's got problems."

After making peace with his exhausting search, he now focuses on prioritising his exacting criteria: everything from great management, strong business model, high return on equity, low price-earnings ratio and high earnings growth. In some ways, he is looking for the least imperfect companies.

Katana has emerged as the No. 1 Australian long-only share manager over 12 months, according to the latest surveys by Mercer, vindicating Sala Tenna and his four fellow portfolio managers' approach.

The Perth-based fund can attribute part of its outperformance to being heavily underweight against the resources sector, a bold move given Katana's west coast roots and evidence that the fund is truly active – it deviates by 73 per cent from the All Ordinaries Index and is free to invest in small to large stocks.

Sala Tenna and the team, including

Stephen Thomas, who joined earlier this year from Bell Potter where he was a resources analyst, are doing a lot of work in the small resources space in anticipation of a few portfolio additions. But they won't be rushed. "The biggest problem you find is going too early or just being too clever," he says.

"With resources at the smaller end of the market you've got to get on site, talk to people, get underground."

Thomas – whose strongest calls historically have been picking Jubilee Mines, Sandfire Resources, Regis Resources and Sirius Resources – "is doing 2300 kilometres over a week or so and he loves it".

The iron ore stocks are about 10 per cent too expensive relative to Katana's expectations for the commodity price, for example. "We've got some iron ore stocks that we really like but we're not in them." The last time the iron ore price was trading at \$US87 a tonne – where it is now – BHP Billiton stock was trading in the low \$30 range. BHP closed at \$36.67 on Friday.

Sala Tenna accepts Perth's advantages and disadvantages and, besides the obvious challenge of proximity to companies and clients, he is a big advocate for the west coast's untapped reserve of financial markets talent.

"The talent in Perth is very much under-competed for," he says. "There's a lot of really good companies, at the big end Wesfarmers; at the small end Navitas, Mineral Resources, Automotive Holdings. There's a lot of very good WA-based companies that come through and they're under-researched."



Romano Sala Tenna has been wary of resources. PHOTO: TONY MCDONOUGH

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Romano Sala Tenna, Katana

Some of Katana's positions at the moment include Insurance Australia Group, Fairfax Media and Mystate, underscoring its complete disregard

for size. At Fairfax (publisher of *The Australian Financial Review*) he highlights the value of Domain and its digital opportunities, and at Mystate the fund is intrigued by a good yield and the building society's expansion as it edges towards earning bank status.

And though each member of the team is a natural specialist in something, nobody has jurisdiction over any sector. Once an investment idea is tested and proposed, it goes to the internal investment committee, which is composed of all five portfolio managers, each with the power of veto.

That means it only takes one member of the group to turf an idea, even if

the other four support it. "Don't get me wrong, it creates some tension," Sala Tenna says. "A more common thing we find is three or four members will be supportive and one or two will abstain."

The system complements a stop-loss policy that keeps investing as objective as possible. "Twelve years on [some of us are] still working together and good buddies, so that is probably an indication we've got the right balance."

The stop-loss kicks in if a stock drops by 7.5 per cent on a trade or 15 per cent on an investment, then a portfolio manager must re-submit their thesis to the investment committee.

"In a bull market we only focus on the positive attributes of a business and in a bear market the opposite is true," Sala Tenna says. Recalling the lesson he learned when he started out in broking, he adds: "We need to take a more holistic view and understand that every company has positive and negative attributes." Price has a role to play too.

One of the hardest attributes of a company to assess is competence and trust in management, a quality Katana ranks as one of the most critical. This can be measured through vision and passion, but that's typically more evident in the smaller end of the market. Sala Tenna generally thinks leaders with skin in the game are a good idea.

"It's not as important in the top end of the market, but in the smaller end where management can do undesirable things ... they're less prone to pay themselves too much, to take a risk with the business, to give themselves a whole lot of options."