

# Discipline and patience epitomise SilverCross Investment Management's approach to investment

*Return on investments can be generated in many ways. For instance, investing in successful, but unknown, small listed companies who have fallen from grace due to temporary factors. The resulting undervaluation forms the basis for significant returns in the long term. At any rate, that is the philosophy of SilverCross Investment Management, founded in 2014. Managing director and portfolio manager David Simons explains how the fund generates value for high-net-worth clients and institutional investors. 'Entrepreneurship takes centre stage at SilverCross.'*

## **How did SilverCross come about?**

'We had the idea to develop a globally oriented, small-cap strategy when Chris Andrews and I still worked for Kempen & Co. The demand for worldwide investment funds is growing. There are various reasons why global investment has taken off: for managers it strategy offers more flexibility

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to select the best investments while at the same time avoiding geopolitical risks. The advantage for clients is that they don't need to find and monitor as many managers. Instead of three regional managers, clients now choose one worldwide manager. Under the umbrella of our partner IBS Capital Management, we launched our firm last year with a team of three portfolio managers. The

operational handling is done by IBS while KAS BANK takes care of fund administration and custodianship. This means that we can concentrate fully on the sharp end of the investment process: the analysis and selection of around 30 successful small companies with strong balance sheets, a proven business model, strong brands and recurring revenue.

## **How does your approach differ from other small-cap funds?**

The words discipline and patience encapsulate the most important difference. We focus on investments in niche players with very good reputations and strong profitability. These businesses, however, are generally highly valued. Our principle is that 'a good company bought at the wrong price is a bad investment'. So we hold back on investing until such time as there is a setback, or the fear of one, resulting in a drop in share price and consequent undervaluation. That is when we invest. This could be many years later than when we first determine that a company meets our criteria. In other words: our approach is characterised by a great deal of patience and the discipline to allow valuation to be the guiding principle.

## **How do you select your companies from such an enormous universe?**

Our universe consists of around 10,000 businesses in the developed markets. We investigate the companies we have our eye on very thoroughly. After the initial selection, based on liquidity and a number of exclusion criteria, around 4,500 businesses are left. After that, we carry out quantitative screenings based on quality factors, various valuation criteria and financial strength. This leaves us a few hundred companies, which we then

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subject to a qualitative analysis. Some will be dropped quickly because they clearly don't meet the strict criteria that we apply. For instance, some businesses don't meet our ESG criteria; others have, for example, gone through four CEOs in the space of ten years.

We only invest in businesses which have a business model that is easy to understand and whose management preferably has a significant shareholding in the company. Once we have invested in an 'excellent' company, the holding period we have in mind is as long as possible, so preferably longer than 5 years. This means that we can spend considerable time on the investments that we have made. We engage in active dialogue with management, for instance, and regularly visit the company, whether it's in Germany or in Japan. Which is why we sometimes refer to ourselves as backers rather than investors. We are able to work like this because our portfolio consists of 'only' 25 to 35 businesses.

**You are co-owners and invest in the fund yourselves. Why do you feel this is important?**

The first and foremost reason, of course, is because we have great faith in the power of our investment strategy. The good thing about it is that we automatically establish that our interests are in line with those who invest in the SilverCross Global Small-cap Fund. We also look at entrepreneurship and shared interests when we invest. Many of the companies we follow are led by entrepreneurial families who have a significant stake in their 'own' company. This means that the interests of management are the same as those of the external shareholders. This ensures

that management focuses on long-term value creation instead of quarterly figures, and so it has the courage to invest, even if this has a negative impact on the profits for the coming year. Performance is, after all, always a matter of high standards and a clear strategy.

**SilverCross is going to focus more on institutional investors as participants in the fund. Where do you see opportunities?**

We got off to a flying start. As it stands now, we have 25 clients with 35 million euro under management. These assets come from an institutional investor, several high-net-worth former as well as active entrepreneurs, and members of staff. The capacity of our strategy is around one billion euro. This opens up space for institutional investors alongside high-net-worth families or individuals. With their long-term investment strategies, institutional investors suit our investment philosophy perfectly. Professional investors only step in once you have a track record of at least 3 years. They work with pension capital belonging to other people, not their own money. For this reason, it is crucial for pension funds that SilverCross is properly organised behind the scenes. And with IBS for the back office and KAS BANK for the custodianship and participant administration, this is the case.

**Was there a particular reason for establishing SilverCross in the Netherlands in 2014?**

I'd say, why not? Chris and I both work from the Netherlands, our partner IBS Capital Management is in Amsterdam and so are you. So there was no reason to set ourselves up in another country. A possible reason for not staying here might be that



**David Simons** (left) founded SilverCross Investment Management together with Chris Andrews. He is the managing director, analyst and co-portfolio manager. Before this, he was managing director at Kempen Capital Management UK in Edinburgh and at the equity sales department of Kempen & Co USA in New York. He started his career at Kempen Capital Management in Amsterdam, as co-portfolio manager of the Orange Midcap Fund. Simons graduated from the University of Applied Sciences Holland and earned his MBA at Nyenrode University.

the talent pool here is so much smaller than it is in London, for example. In that respect the Netherlands could be a less advantageous place to set up a business. What's more, legislation and regulations are gradually becoming so strict and complex that it is becoming increasingly difficult to be innovative in the financial sector. The cost and time spent complying with all the regulations and reporting requirements is becoming too much for smaller financial institutions. And, even if you have a fantastic idea, if you don't have sufficient experience at board level, the DNB is not likely to give you permission to launch a financial product.

Yet, being in business means taking risks. This should be possible, even in the financial sector. 'Make mistakes by throwing the ball, not by holding the ball,' as Mr Möllenkopf of Qualcomm was wont to say. What you need to do is you make sure that you keep making better mistakes. The financial sector in the Netherlands has shrunk drastically in recent years due to a lack of innovation. And it is probably on the brink of significant change as a consequence of the digitisation of society. We can be part of this, but only if we create a platform for it. This will allow us to build something for society.

#### **Are you considering an IPO for the fund so that you can carry on expanding?**

Not now, at any rate, because we're still busy building. Going public must represent added value. We report to our investors regularly about our performance; we don't need a stock exchange listing for that.

We're looking into whether we need to get an AIFMD licence or not, even though, strictly speaking, it's not necessary. Other examples from amongst our funds have IPOed, or we are considering them going

public. We're watching them to see how they get on and whether going public will be financially advantageous for SilverCross too. The most important argument against going public is that we are keen to know who the other participants are so that we can make sure that only those participants join who have an investment horizon that suits our investment strategy.

#### **What are your plans then for the near future?**

For now, we're focussing fully on achieving really exceptional long-term returns for our participants. We are aiming for an alpha of 300 basis points above our reference index. A strong track record will attract new participants. Together with them, we want our assets under management to get to about two or three hundred million euro. Perhaps in due course, SilverCross will introduce another asset class with its own specialised investment team. But we can't really see a reason for doing that right now. We will only consider ourselves successful once SilverCross is regarded internationally as a leader among global small-caps, in a few years' time. To realise that vision, we'll continue to invest in the organisation in the coming years. We are optimistic about what we can achieve in the Netherlands.

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