

Ireland — A Closer Look at Investment Opportunities within Europe

The Closed-End Fund Association (CEFA) spoke with Noel O'Halloran, Chief Investment Officer with KBI Global Investors and Portfolio Manager of the New Ireland Fund, about Ireland's investment landscape, what's by many, an underappreciated investment opportunity in the European market.



Noel O'Halloran



Libby Hastert

The following Q&A recaps the conversation that originally took place as part of CEFA's podcast series on October 16, 2017, which can be heard at CEFA.com.

Speaker: Welcome, and thanks for joining the Closed-End Fund Association for another discussion. Today, we will hear from an industry expert who shares insight on a timely issue affecting the Closed-End Fund space.

LH: Hello, I'm Libby Hastert, Content Specialist at the Closed-End Fund Association. Today, we're speaking with Noel O'Halloran, Chief Investment Officer with KBI Global Investors Limited ("KBIGI") and Portfolio Manager of the New Ireland Fund. I'm especially excited for today's podcast because we're taking a closer look at Ireland, what's by many, an underappreciated investment opportunity in the European market. Noel can offer an especially interesting perspective on this topic, as he manages the fund from KBIGI's office in Dublin.

Thank you for joining me, Noel. Let's go ahead and talk Ireland, starting with the transformation it's undergone in a relatively short period of time. During the global financial crisis, Ireland struggled. Since the economy has steadily improved, how far has Ireland come and where does it stand now? Noel?

NOH: Yeah, I would say right now that Ireland is in great shape. And as a reminder, post-the 2008 financial crisis, Ireland itself suffered a serious recession that particularly affected domestic consumer economy and the banking sector and the real estate sector in particular. And then around 2011/2012 we had a very aggressive restructuring of the economy, and Ireland became a poster-child of how to restructure an economy. And since then we've seen a very, very strong and sustained recovery in the economy.

And I would say to get to where we are today, there's been three phases. The first phase was an export-led recovery in the economy. That then moved to an investment phase, where we saw in particular many multinational companies re-investing into Ireland because the cost base was suddenly much more attractive, and many of the other things that have always made Ireland attractive were still in place. And then finally, to get to the comment about great shape today, I would say that we've seen a very strong domestic recovery in the economy over the last two years, in particular. So, the consumer economy is back, it's strong. If we look at the things that make the consumer strong, it's typically around their house or their job. The unemployment rate today is more than half what it was at the peak. So, today we're about 6% unemployment, having been at close to 14.5% at the peak of the recession. And the housing market has also recovered strongly.

So, overall, Ireland today is in very, very good shape, from my perspective.



LH: So, Ireland has been growing strongly, but Europe in general has been more sluggish. Are you seeing positive signs in the Eurozone? How does pick-up in the European growth impact Ireland?

NOH: Yeah, it's an interesting question. So, as we came into the year 2017, I think, a lot of global investors, their focus was on politics in Europe, and focused on the negatives in Europe. And 10 months on, the European political situation, elections in the Netherlands, elections in France in particular, and Germany, have all passed pretty uneventfully. And while everybody had been worried about that, it's actually turned out to be a non-surprise. The real surprise so far in 2017 has been the strength of the recovery in the European economy.

So, the European economy, this year, will grow at over 2%, and all the indicators are that it will grow again in 2018 at over 2%. So that would put Europe growing in excess of the USA, for example. And that's a real positive surprise. From an Irish perspective, Europe is one of our largest trading partners and Ireland has a very export-led economy. That's just very, very positive news for Ireland.

So, overall, I think Ireland itself is going well, but the strength in Europe, which looks to be sustained into next year, is also a strong benefit for Ireland.

LH: The United Kingdom is Ireland's largest trading partner. With the UK leaving the European Union, what are the short-term and long-term effects on Irish companies and the Irish economy?

NOH: Yeah. The UK is our largest trading partner. But just to put that into context, if we had the same discussion 10 or 20 years ago, I think the UK would've been a far, far bigger trading partner of Ireland. So Ireland has successfully diversified its overall terms of trade. And the UK today is around 15% of our exports, just to put it into context, which is not dissimilar to Europe as a Pan-European area.

That said, the short-term, Brexit, as it's commonly called, is a short-term head wind for Ireland. Apart from being our largest trading partner, one of our domestic issues is the border and what happens with border enforcement with Northern Ireland, where obviously there's a land border between Ireland South and Northern Ireland, so that's an uncertainty that is there in the short-term.

And then the other short-term issue is the nature of the negotiations of the divorce, as such, between the UK and Europe. Were that to be a benign and what's called a soft exit, I think that's not a major issue for Ireland. If it's a harder, bumpier divorce, then that is, short-term, more difficult for Ireland to cope with.

So, that's the short-term. It's an uncertainty and nobody really knows, but the going consensus is that we'll end up with some sort of a negotiated period and that all efforts will be made to make that as smooth a transition as possible.

In the longer term, I think I find myself in the bullish camp, because particularly for Ireland, Ireland retains a number of advantages. It will still be a member of the EU. More importantly, it will be the only English-speaking member of the EU, which is actually very interesting, from a multinational company perspective, many people like that obviously if you are looking in from the US or elsewhere. And from a portfolio point of view, or from an economy point of view, there will be sectors that do extremely well. And so the financial sector is obviously one. If we see lots of jobs moving from London, Ireland will be one of the top three centers globally that will really be competing for those sort of investment banking and fund management jobs and financial jobs, generally. And other areas that will really benefit is real estate, both the commercial real estate and obviously housing, were there to be more highly paid, skilled jobs moving to Ireland.



So, for the short-term, I don't know. Nobody really knows. But longer term, definitely a benefit to Ireland. Just one comment from a portfolio point of view is that I have been moving any sort of UK exposure away from the portfolio for the last two years, and more towards European exposure so that I don't feel particularly exposed for the portfolio.

LH: While many Americans' ancestors call Ireland home, few of today's US investor portfolios have made Ireland a home for their global investing strategy. In spite of this, financial advisors continue to encourage US investors to diversify with non-US equities, particularly Europe. Ireland is a very small percentage of the broader European equity products. So how would you see Irish equity's best position in a US investor's portfolio? Noel?

NOH: Yeah. It's been a very interesting year, in 2017. I'd say at this point in time, I'd say there's a push and a pull going on for Europe versus the US generally. And I think the push is really that when advisors look at the US, they find a market that's pretty much priced for perfection. The economy itself is much later in its economic cycle. The US stock market is at record highs and earnings and return on equity and margins are also at record highs. And domestically, there is more uncertainty in politics than there has been for quite some time. So, that's the sort of push case, from the US.

In terms of Europe, I think the pull generally has been a much stronger economic recovery, as we've already discussed. A political situation that is relatively stable, notwithstanding recent noise in areas like Catalonia and Spain, which we do believe will calm down and is already calming down. But Europe itself is much earlier in its economic recovery. And earnings in Europe as distinct from the US are far, far from their highs. And Ireland is no different. Ireland is bang in line with the rest of Europe, from that perspective.

So, I think year to date what I would say we've seen is, wave one would've been general ETF and index flows into Europe. Wave two, was moving that from an investor point of view, or an advisor point of view, to look for broad active managers who will manage portfolios pan Europe. And then the third wave will be targeted allocations, looking for greater upside, looking for special, unique situations. And that's where Ireland itself really coming to the fore.

Ireland has stronger growth, stronger earnings growth, stronger economic growth, than the rest of Europe. If I look broadly at the valuations of Ireland today, we're at a 10% discount to the rest of Europe. And growing more quickly. We're at a 20% discount to S&P 500. So I think that next phase is very much where this portfolio and Ireland would be seen by advisors and a great way to look for the next investment.

LH: The New Ireland Fund is one of the few investment products enabling US investors to gain exposure to a portfolio of Irish equities. So, as an investment manager, do you see advantages to managing the portfolio in a closed-end fund structure?

NOH: Yes, absolutely. The New Ireland Fund itself is a very unique and differentiated fund. And as a portfolio manager who's been managing it for a number of years, I see very obvious advantages. The first advantage that I would point to, is that as a closed-end fund, I don't have to worry about daily cash inflows or outflows as, for example, a mutual fund manager does. So, this allows me to manage the portfolio itself with certainty and with confidence that I can invest in my preferred securities and not have any sudden cash call that in itself would require me to trim or liquidate my top positions that I'd rather not at that particular point in time.



Another further advantage, I'd highlight and maybe one that people don't consider enough, that is an advantage of closed-end funds, is the Fund Board itself a structure that should provide investors with strong confidence that the Fund itself has very strong oversight. It has strong governance, as well as transparency. And for the latter I'd highlight even in the case of the New Ireland Fund, the Fund's managed distribution policy over recent years, which has been strongly advertised to shareholders during that period.

LH: What's your outlook for the Irish economy and equity market?

NOH: Yeah. Overall, I remain, as I have been for a couple of years now, very, very positive for the outlook for the Irish economy. I think we're nowhere close to the end of this economic cycle. Still at a European level, the European Central bank, which is the Irish, which governs the interest rates for Ireland for example, there's no sign of interest rates going back up. So, the interest rate environment is very, very supportive. The macro fundamentals for Ireland remain very strong. At a government level, we're almost running a balanced budget at this point in time. Our national debt has been paid down, aggressively over recent years. We still do have domestic debt, at the consumer level, but that also is coming down and is also being helped by lower interest rates.

Overall, you know, that 4% to 6% economic growth range that we've seen over recent years, I expect to continue. And that will lead to strong earnings growth for the stock market and I'm able to capture that earnings growth at valuations, that to me still look very attractive. So, overall, it's still a very nice positive cocktail for managing a portfolio, and a positive outlook.

LH: The New Ireland Fund is currently conducting a rights offering. What are the terms? How do you expect to invest the capital?

NOH: Yeah. Well, firstly, I'll be investing the proceeds consistent with the investment objectives of the Fund. In terms of the rights offering itself, the full details are on the Fund's website, including the relevant dates. But in summary, it is a transferrable rights offering. Holders are entitled to one right for each common share held on the record date. As it is a transferrable rights offering, the rights may trade and will do so under the ticker IRL RT.

Of more direct concern to myself, in terms of deploying the proceeds, firstly, I would say as PM I welcome the offering, and I see a number of avenues for investment of the proceeds. The first of those I would like to do is to diversify into Irish stocks that I haven't invested in for a number of years. There are names that I wouldn't have touched into the downturn. But increasingly, the economy and the stock market itself are growing, these stocks are increasingly attractive to look at again. So those stocks that remain that I think I would like to see back in the portfolio.

The second area where I have been selectively adding to over recent years, has been to add some pan European listed stocks and sectors. And in those cases, and they're mainly non-UK stocks and I'll point to stocks or sectors that complement or provide diversification to the portfolio. And in particular, in areas that aren't widely available in Ireland. A current example in the portfolio, is an investment in some European utility stocks, and that's something that I would look to continue to expand, but selectively. Another strong feature over recent years has been the reemergence of IPOs on the Irish stock market. Again, in common with the economy and the stock market recovering strongly, I already have over recent years invested in 5 or so IPOs. And I expect further opportunities of new IPOs will present themselves and therefore I'd like to have proceeds available to take part in such IPOs.

Then finally, and very selectively, I'd like to add to some existing positions in the portfolio, but only where a valuation opportunity may present itself.



So, overall, as you can see, there are a number of avenues for investment of the proceeds of the rights offering.

LH: Any closing thoughts on the Irish equity market, or the Fund?

NOH: I suppose my closing thoughts, as I think of Ireland, I think of Ireland at a macro-level as being a very well managed economy at this point in the cycle. I think the economy itself is in a very strong recovery phase. And that we're far from any sort of peak in the economy or any concerns about the next recession. So, I think that's a number of years away. So, a very, very stable macro-environment.

I think in terms of our neighbors, as we've already discussed, the UK short-term is definitely a headwind and something that I think from a portfolio point of view, I have well managed. I think on the opposite to that, other trading partners such as the US and in particular Europe are in a very, very strong stead.

So, that leads me to the equity market itself. The equity market itself is in good shape. We're seeing strong recovery in earnings. We're seeing very strong shareholder focus from the companies we're investing in. And we're able to achieve those sorts of earnings growth and valuations that I like. So, a nice cocktail from a macro and micro perspective from that point of view.

And for investors, the last thing I would highlight I suppose is KBI Global Investors, who I work with who advise the Fund. We are managing this portfolio for a number of years, and we are very, very stable in terms of our own firm, in terms of the staff, myself and the other staff involved in managing the portfolio. There's been no changes. It's been a very stable background from that perspective so that should also give investors' strong confidence in the portfolio and the management of it.

LH: **Thanks for that update, Noel. This podcast is for informational purposes only, and should not be regarded as an offer to sell, or as a solicitation of an offer to buy, any financial product, or as an official confirmation of any transaction. Investors should carefully consider the investment objectives, risks, charges, and expenses of the Fund before investing. The prospectus, which contains more complete information about this and other matters, should be read carefully before investing. To obtain a prospectus, please call 1-800-468-6475, or visit www.NewIrelandFund.com.**

To all those listening in, thank you and stay tuned until next time's market update.

Speaker: Thank you for joining us. We hope you will stop by again for news on this ever changing space. Until next time, connect with us on Twitter at @CEFAssociation, or by searching for the Closed-End Fund Association on LinkedIn and YouTube.

You can find more insight from New Ireland Fund and information about their closed-end funds on their website at www.newirelandfund.com. Information is also available on CEFA.com – your comprehensive resource for education, data, and timely insight on closed-end funds.

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