Strategy Directors

# AN INTERVIEW WITH FRANK PINKERTON

DIRECTOR OF CORE EQUITY STRATEGY

SENIOR ANALYST - HEALTHCARE AND MATERIALS

JOINED CRAWFORD IN 2015

**Interviewer: How did you first become interested in investing?**

**Frank Pinkerton:** I believe I was seven or eight when I first became interested in investing. For my birthday, my grandfather gave me stock in the bank where he was, at the time, Chairman. My dad had already explained to me what a bank was and what it did, but once I had stock, I was intrigued. Ownership raised a lot of curiosity on my part. It was the start of my journey to become a diligent saver and, later, a diligent investor. A second big step was right after I graduated college. Basically, I got lucky to invest in a little company called Yahoo in the early innings of the dot-com craze. I then cashed the entire thing out to invest in myself by paying for my MBA. From that point on, you could say that my curiosity continued to grow and I was hooked on investing.

**I: What brought you to Crawford?**

**FP:** I moved back to Atlanta after a decade of working on Wall Street as a research analyst in Healthcare. I continued to work for a regional bank in Atlanta, but I wasn't finding the work to be fulfilling. I then met John Crawford, Jr., and after about nine months of conversation and getting to know the team, I joined the firm. More than anything, I joined Crawford because I liked the people. I like the philosophy and mission. It is a good fit for me. The opportunity that I've had to both follow Healthcare stocks and manage the Core Equity portfolio has been a great role for me.

**I: You run the Core Equity Strategy. How would you define Core Equity?**

**FP:** At its heart, Core Equity is a "best ideas" portfolio. Most of the strategies that we have at Crawford are specifically focused on attaining a goal. Our Strategy Directors are very hands-on in attempting to satisfy specific portfolio objectives that align with investors' expectations. Core Equity, however, is more of a total shareholder return portfolio. It has a little more art than science, and there is more freedom of choice on the stocks that can go into the portfolio. Core Equity doesn't have a specific yield or income mandate. We are just looking for dividend-paying stocks across the cap spectrum that we think will provide the best total returns. Usually, we are looking at a one- to two-year time frame, but we often hold our companies for much longer time periods.

**I: As the director of a "best ideas" portfolio of the firm's highest-conviction stocks, how do you ensure that this is reflected in the Core Equity portfolio constituents?**

**FP:** From a Strategy Director's standpoint, I always keep in touch with the analysts, seek their best ideas, and do what I can to work them into the portfolio. The one big change that I've implemented since taking over Core is being more proactive with a macro overlay, specifically with regard to our industry weightings. This is important because industry dynamics drive a significant portion of overall market returns, especially in the current market environment. For example, over the last decade, if you haven't had Technology and/or growth weightings, it has likely been very difficult to have strong performance. Strictly value investors have been left behind. Over the last several years, the team has increased our exposure to what we consider to be the growth areas of the portfolio. While to some degree that is technology, we also have to be creative. For instance, we have owned datacenter and tower REITs that have exposure to the same growth trends as Technology companies. This allows Core Equity to benefit from growth in infrastructure buildouts through companies that pay dividends. We have been very selective in honoring our dividend mandate while trying to make sure that our investments match up with the undercurrents of the market.

**I: How does the Core Equity investable universe differ from that of other Crawford strategies?**

**FP:** The Core portfolio represents our analysts' best ideas across the entire Crawford research complex, so the universe for Core is the largest collective universe of all of our strategies. Core is focused on companies with market capitalizations of $1B and up, and all of these companies must pay dividends. In Core, we can own companies that don't necessarily have the dividend-paying history that we require for our Dividend Growth strategy or the higher yield required for our Dividend Yield strategy. And we can own many of the smaller and faster-growing companies that we own in our Small Cap strategy. It is a broader investable universe. The challenge is narrowing that set of companies down to the appropriate ones. This is where our team of analysts, who are sector specialists, are very helpful. They identify the stocks that they believe to have the strongest return potential. My role is to sift through these best ideas and arrive at a portfolio that is balanced in terms of market exposures and risk/return concentration.

**I: What does volatility look like in Crawford's Core Equity investment universe?**

**FP:** The simple answer is Core has lower volatility than its benchmark, the S&P 500. Core should also have lower volatility than a total market index. We actually have a lot less volatility than the majority of our peers in the marketplace, which is consistent with our quality bias across all Crawford strategies. When we start speaking about volatility, things can get nerdy pretty fast. We use several models to track multiple factors across the portfolio. These factor models typically show Core as having somewhere between one standard deviation and two standard deviations of lower volatility than the market. Basically, Core's volatility should be at least 15% less than the S&P 500.

**I: How do you work to mitigate risk?**

**FP:** The biggest component of risk reduction starts with our central process for screening, analyzing, and evaluating stocks. By simply requiring companies in Core Equity to pay a dividend, there is a reduction in risk. Each analyst then weighs the various potential outcomes for each company and determines if the potential reward is worth the risk. Further, I like to think that our reduced risk can be explained by owning stocks that have a sustainable quality advantage. Even if the market may not recognize that quality advantage over some short period of time, over the long term, the benefits will become apparent. Some of these benefits include consistent growth of dividends, profits, cash flows, and ultimately, growth in share prices.

**I: How do you define quality and what metrics do you use to measure this?**

**FP:** At Crawford, we believe that dividends are an indicator of quality. More specifically, dividends represent a company's ability to sustainably produce excess free cash flow and the willingness of a management team to reward shareholders. Aside from the dividend, we have various other quality metrics that we employ. The truth is that our analysts use different quality metrics for each sector, because fundamental business drivers vary between sectors. Back to the nerdiness and the volatility question above, the models that we use to determine if a portfolio has volatility are driven by each individual company. Thus, we can look at Core Equity like it is a company, instead of a portfolio. We measure the debt of the portfolio against the market, and our portfolio ends up having less debt. Core Equity falls on the higher-quality side of important financial statistics like stronger cash flow, higher margins, and higher return metrics.

**I: What about value? How do you quantify value?**

**FP:** Value is somewhat different altogether. When I think of value, yes, I want to know the price of the stock. By price, I do not mean where the stock is currently trading in the market, but rather, what would we have to pay for the entire business. It is important to analyze the various layers of the business. Often times, when investors think about value, they use the term earnings. Our team typically deploys specific cash flow metrics for each sector and uses that metric consistently within its given sector. This gives us the opportunity to figure out which companies we believe will grow the fastest and can continue to achieve at the highest level. At Crawford, because we focus on quality instead of deep value, we often think in terms of relative value. We most definitely own companies that might appear to be highly or overvalued today, but that we believe in the long term are going to continue to appreciate.