Interview Series

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INVESTMENT COUNSEL
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AN INTERVIEW WITH CHRIS KENDRICK

SENIOR RESEARCH ANALYST

ENERGY, REITS, AND UTILITIES

JOINED CRAWFORD IN 2017

Interviewer: How did you first become interested in investing?

Chris Kendrick: I became interested in investing while I was in college, during the technology bubble of 2000. It was an exciting time to be an investor, and the truth is, that is exactly what investing is not supposed to be: exciting. I subsequently paid my "market tuition" in 2001, and along with many other investors, I experienced the massive market decline during that period. Despite this, I was hooked on learning about businesses and the market. I'll add that, in addition to the dot-com bubble in 2000, I also experienced the 2008 housing bubble. These are two supposed "100-year events" that occurred within a decade. This is what makes this field so challenging and enjoyable, at least for me.

I: How would you describe your investment approach or philosophy?

CK: My approach to investing has evolved over the years. I used to look for stocks with low Price to Earnings and low Price to Cash Flow multiples. Over time, however, I've realized that there are a lot of businesses that deserve to have low valuations. With that being said, I've come to believe that quality and value are interconnected. I believe that good companies deserve higher valuations. Nevertheless, the trick is to do your work in advance and buy these companies during market dislocations and without delay. I have found it to be true that the strongest businesses have three primary characteristics: recurring revenue, low capital requirements, and they have pre-set capital allocation policies, including the return of capital to shareholders and how they might engage retained earnings to grow their enterprise. These attributes tend to be very consistent with quality metrics.

I: How did your prior experience help prepare you for your role at CIC?

CK: Prior to joining Crawford, I was an analyst at a real estate investment firm where I gained experience identifying systematic value and yield-advantage within REITs. I'm also a CPA®, so my understanding of accounting provides a solid foundation for the work that I'm doing. I follow REITs, Utilities, and Energy, all of which are considered to be the higher-yielding sectors of the market. With that being said, I think that my real estate experience, in a way, informs the way that I think about Utilities. While REITs and Utilities have totally different business models, they do tend to behave similarly in relation to interest rate moves.

I: Do you utilize a macro-economic overview in your approach to the sectors you follow?

CK: We are bottom-up, fundamental investors, so we are not trying to predict the economy. Consequently, I believe that any good analyst must have a view on interest rate policy in order to know if there are headwinds or tailwinds to their respective sector(s). Given the Fed's communication updates that started after the Global Financial Crisis, we can usually get a clear signal on interest rate policy in both its Q&A sessions and commentary. That message has been clear for 10 years: short-term rates will stay low for a long time. For REITs and Utilities, lower interest rates tend to drive better performance, with all other things being equal.

I: Are Energy, Utility and REIT stocks correlated? What factors tend to drive returns of the various sectors?

CK: Both REITs and Utilities are known as "bond proxies" in market parlance. With Energy, it is relatively simple. Higher

oil and gas prices drive higher cash flows for the sector. For Utilities, the most important factors are both regulatory constructs within states and rate case activity. In order for a utility company to earn its allowed return, it must file rate cases with its respective commissioner, who approves the utilities plan. This approval allows the utility companies to earn a sufficient return for delivering services to their customers. This allowed return is typically somewhere between nine and eleven percent. For REITs, on the other hand, the biggest factors driving returns are rent growth, supply growth, and balance sheet strength. REITs with faster rent growth, lower supply growth, and lower debt tend to outperform. REITs of this nature, over the past decade, have been cell towers, data centers, multifamily, and industrial REITs. Thinking about Total Shareholder Return (TSR) is quite effective for REITs and Utilities, as the dividend is a large portion of the return. Energy, however, is more complex, given its dependence on energy prices, and the TSR model is not easily estimated.

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