
FINANCIAL REVIEW

How fund manager Artisan found growth in unloved industrials stocks

Vesna Poljak and Philip Baker | 09-04-16

The massive upgrade cycle in commercial lighting away from energy-intensive globes to greener LED set-ups has a surprising role to play in the evolution of the industrial internet and connecting consumers, manufacturers and retailers.

Acuity Brands, an Atlanta-based lighting company, is one of the stocks Artisan Partners believes fits neatly into its growth portfolio. That's because Acuity can equip stores such as America's Target with sensor-embedded fittings that track the movement of customers through aisles to the checkout. Acuity shares are on track to rally for a fifth-straight year, having advanced 17.2 per cent in 2016.

Mike Schneider, who follows industrials stocks for Artisan, says "smart lighting" is exactly how an industrial stock can reinvent itself with technology. "Here, a traditional industrial lighting company has found means to bring information and data analytics to what is a very traditional fixture within a commercial setting," he says.

"They make the lighting systems that follow your smartphone in your pocket via bluetooth or Wi-Fi, because you're always emitting a signal unless you've got it entirely powered off. It knows when you enter the car park, when you enter the front door, how you proceed through the store, it knows where you've lingered, whether you're looking at the top of the shelf or the lower end of the shelf." Companies have figured out that ceiling lights are the least obstructive, most accurate and inexpensive way to introduce the kind of sensors that are becoming ubiquitous. "The capabilities aren't even really understood but why not, if you're retrofitting hundreds of stores, give yourself the optionality to use that sensor technology in a way you might not even envision right now?"

"The consumer goods companies in particular are really interested in this. It also has big implications for shrinkage, one of the biggest costs for retailers is theft. They've done studies using this lighting and sensor technology and specific localisation to show you can analyse a person's stall time or linger time and statistically indicate there's a theft occurring," Schneider says.

The commodities collapse and the deflationary signals around the world have made life tough for some dominant industrials stocks. "We were lulled into thinking industrials were a higher growth market than they really were based on this distortion coming out of emerging markets and China. Now we're faced with the aftermath of that bust and it's become apparent that GDP within at least the industrials sector is very low."

Artisan offers up plenty of stocks where technology is driving growth for "atypical industrials." Its investment process looks for stocks in the stage of "accelerated profits," so "the challenge is to find those technologies that are on the cusp of new applications or new geographies," Schneider says.



*Mike Schneider, from Artisan Partners, looks for "accelerating profit cycles".
Daniel Munoz*

On the software side, Artisan likes vision systems companies Keyence and Cognex which make the systems used on the factory floor for quality control and inspection. There are two big leaps here: processing speed, which enables read time inspection as product is coming down the line, and 3D capability, which means the technology can do the job of the human eye. Using both from a manufacturing perspective frees up capacity by eliminating the need for offline inspecting.

Schneider is a mid-westerner from Wisconsin who graduated law school but was more intrigued with investing. He used his earnings from a paper delivery route to buy his first stock, Sun Oil, which went bankrupt. "That was my first lesson in investing, that stocks can go to zero," he recalls.

Schneider considers the future for the utilities sector and argues that stranded assets “are a real and imminent threat.”

“The power generators, the power distribution companies, the poles and wires, for 100 years we’ve had this massive investment in power generation built typically on fossil fuels with long distance transmission lines connecting various parts of countries, and now you bring in solar farms and wind farms and you threaten the economics of those very legacy infrastructure investments,” he says.

“If you’re a utility you’ve got a real challenge to seize the economics of these massive billion-dollar plants and billion-dollar transmission lines and there is a real power struggle that is underway already between the alternative energy companies and the traditional utilities. The utility stocks are now at all-time highs because of this chase for yield at a very time when their economics are most in question.

“Ten years ago nobody was questioning the value of a public utility and the investments it’s making, fast-forward to today, there’s a real threat on the horizon and it’s moving ever closer and the tipping point is battery technology.”

One lesson Schneider subscribes to is don’t be too early and get caught up in the hype cycle. It’s a problem he saw in the arrival of 3D printing, for example, where the market rewards all players fairly early. “Technology generally takes longer than expected but the impact is greater than expected,” he says. “Let the market first ferret out who those winners will be rather than catch a rising tide.”

This article represents the views of Vesna Poljak and Philip Baker of Australian Financial Review and Mike Schneider, an analyst for the Artisan Partners Growth Team, as of the date of publication and those views and opinions presented are his own. Artisan Partners is not responsible for and cannot guarantee the accuracy or completeness of any statement in the discussion. This material does not constitute investment advice or a solicitation of any specific investment product or service. Any forecasts contained herein are for illustrative purposes only and are not to be relied upon as advice or interpreted as a recommendation. Prospective investors should consult their financial and tax adviser before making investments in order to determine whether an investment will be suitable for them.

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