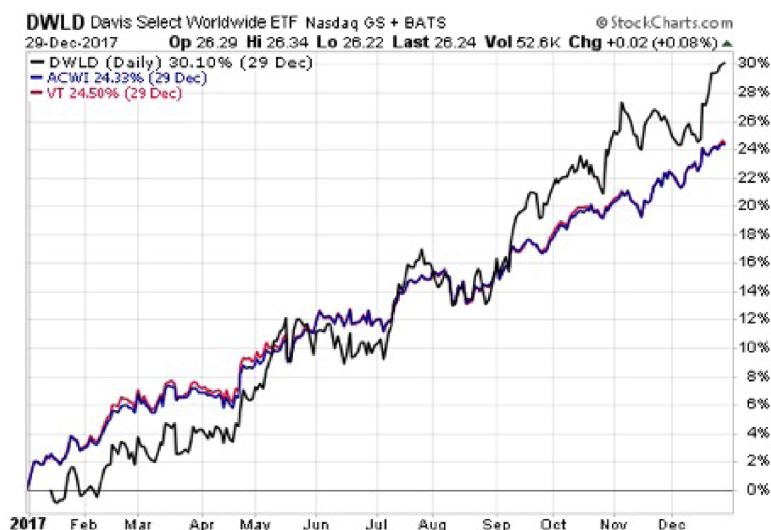
LESS IS MORE FOR THIS ACTIVE GLOBAL ETF

ETF .com

By Cinthia Murphy | August 15, 2018

The Davis Select Worldwide ETF (DWLD) is a global equity ETF described as "high conviction active." This is a go-anywhere, best-ideas-type strategy serving up a concentrated portfolio of global stocks that, in 2017—its debut year—notably outperformed passive giants in the segment, such as the iShares MSCI ACWI ETF (ACWI)and the Vanguard Total World Stock ETF (VT).



So far in 2018, DWLD, with $254 million in assets under management, has lagged a bit, but the fund's construct and performance speak to the importance of security selection, of finding good value, and of having conviction in long-term themes when you are truly steering clear of an index. Davis Funds' portfolio manager Danton Goei gives us a glimpse at the legwork that goes into an active ETF such as DWLD.

ETF.com: DWLD owns only about 35 holdings; it accesses at least three countries at a time, and the positions are ideally held for at least three to five years. This is a concentrated portfolio that holds on to its bets for a good length of time. Why is this the way to go in global equities?

Danton Goei: It's a globally diversified fund, actively managed, index-agnostic. We think that's one of the big benefits. It's a go-anywhere fund based on bottom-up research. Our view is that, in the global space where the index comparison, the MSCI All Country Weighted Index (ACWI), has 2,500 names in it, we're pretty sure there aren't 2,500 good companies out there. We do the legwork and choose what we think are 35 great investments and build a portfolio around that.

ETF.com: Performance of this fund is highly dependent on individual securities. In the past, allocations to Amazon and Google drove most of the outperformance DWLD had against funds like the iShares MSCI ACWI ETF (ACWI) and the Vanguard Total World Stock ETF (VT). What company-specific metrics are you considering when picking stocks in a global pool?

Goei: It's a concentrated portfolio, and at different points, different names will drive the performance. Our overall investment philosophy is long term—a three- to five-year investment horizon. We're looking for companies with great competitive advantages, with high return on investment.

We try to invest in what we call "compounding machines"—names where time is your friend, companies that, over time, have great investment opportunities in their own businesses.

We also spend a lot of time with management. If you only own a stock for five weeks, like a lot of funds do, it's not going to matter. But if you own it for five years, then management matters hugely. We spend a lot of time with management talking about capital allocation.

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Finally, we're very valuation-sensitive. In our mind, there's no such thing as must-own. It's all depending on the price that you get relative to the opportunity.

If you look at the portfolio, it's pretty eclectic. You have names like Google (GOOG) next to names like Wells Fargo (WFC). You don't often see portfolios that have those names side by side, but we think about the multiples we're paying now relative to the growth rate over time. Wells Fargo is trading at 11 or 12 times earnings, so that's 8% or 9% current earnings yield. It's a great starting point. We think those earnings will continue to grow.

But then you look at Google and you've got something that's trading double the multiple, 23 times earnings. But their earnings and revenues are growing in the 15-20% range. A 15% growth rate would mean a doubling of earnings in five years, so the multiple's halving in five years. That's also very attractive, and we have a lot of confidence that's going to happen. It's bottom-up, valuation-focused analysis.

ETF.com: People seem to love factors. In DWLD, you've favored larger-cap growth names and smaller-cap value names. You also seem to avoid value stocks that have higher yields. But it sounds like the underlying factor here is value.

Goei: Correct. We focus on value. But you bring up a good point: What you own is just as important as what you don't own. We don't own a lot of these high-dividend yielders—a lot of the consumer product companies that have been seen as either safe or attractive because they have a high dividend. People are wrong on both ends.

There are a lot of things happening in the consumer space that makes a lot of these companies less attractive than they were 10 years ago—online retailers, stronger competition in emerging markets, which has been a big growth area for them.

But the idea that just because you have a 3% or 4% dividend yield you're an attractive company, and I'm willing to pay 20-25 times earnings even though those earnings are only growing 0-5%, low single digits is a dangerous place to be. Even though they're global, multinational, well-established companies, we think they actually make for risky investments.

ETF.com: Outside the U.S., DWLD has a big allocation to China. That's paid off in the past. It's not doing so well this year. What's your view on China going forward?

Goei: I just returned from six weeks in China meeting with companies there. Part of our research effort is going to meet with companies and talk to management, as well as to their competitors, suppliers and customers. China is an area we're very interested in. But we don't invest in a country. We have a very focused approach, and only own names we find interesting, and that's in the consumer space.

Even though historically China's been driven by commodity, industrial and construction companies, the consumer space is faster-growing. Chinese net exports as a percentage of GDP in 2007 was 9%. That's fallen to 2% last year because the economy in China has been pivoting toward much more of a consumer-led, domestically driven economy. Just like ours, the U.S. is driven by how the U.S. consumer does.

You can find some great businesses in the consumer space, where there are high barriers to entry, real competitive advantages, high-free-cash-generation-type of businesses, whether you have economies of scale or brand.

But right now, China's been struggling a bit, mainly because of macro fears around trade disputes. That said, a trade war would have some impact on the Chinese economy, but it would be limited due to its growing consumer focus. The companies we invest in have very little exposure to exports; they're domestically driven.

ETF.com: DWLD is still pretty young, but you have a lot of experience in this space. Have you ever picked a stock that turned out to be a complete sour apple? How did you manage that?

Goei: Yes, we've certainly had our misses in the past. Even though the ETF is a year-and-a-half old, our global strategy is almost 15 years old. So, we have a long track record there with lots of winners, but also our share of misses.

We want to be long term. But we assess every holding we have on a daily basis relative to the opportunity costs that are out there. If something is amiss for whatever reason—we were wrong about management, or about the market opportunity or competition or regulatory environments—and we now think the risk/reward is poor from here on, we'll certainly sell. We're not tied to the idea that we have to hold it for at least three to five years.

ETF.com: Active management gets a pretty bad rap for often underperforming benchmarks, failing to deliver consistent performance year after year and for being expensive. You're out there pitching a high-conviction, concentrated global active ETF at 0.65% when you have funds like ACWI at 0.32% and VT at 0.10%; that can't be easy. Are there any misconceptions people have about what an active ETF like DWLD can offer at the end of the day?

Goei: We realize the competition is funds like ACWI. But we think our rates are very competitive, and that's one of the reasons we started the ETF. We were already low rate relative to other active managers, so we thought we were a great candidate to do ETFs. But we realize the passive manager is even lower. Still, we can add a lot of value. We talked about ACWI and its 2,500 names—it's way overdiversified.

And it's not just the number of names, but the list is chock-full of state-owned enterprises, like banks, industrials, insurance companies, telecom. A lot of these companies, outside the index, investors would never dream of investing in—a Chinese state-owned bank or an Indian telecom company run by the government? They aren't well run and they're not run for the benefit of shareholders.

An active manager in the global space can really add a lot of value by avoiding those types of companies, and focusing on the right ones.

Average Annual Total Returns as of June 30, 2018			
	YTD	1 Year	Inception (01/11/17)
Davis Select Worldwide ETF *NAV Price*	0.10%	18.32%	19.87%
Davis Select Worldwide ETF *Market Price*	0.06%	18.38%	20.02%
MSCI All Country World Index	-0.43%	10.73%	14.12%

The performance presented represents past performance and is not a guarantee of future results. *Investment return and principal value will vary so that, when redeemed, an investor's shares may be worth more or less than their original cost. Returns of less than one year are not annualized. NAV prices are used to calculate market price performance prior to the date when the Fund first traded on NASDAQ. Market performance is determined using the bid/ask midpoint at 4:00 pm Eastern time, when the NAV is typically calculated. Market performance does not represent the returns you would receive if you traded shares at other times. For the Fund's most recent month end performance, please call 800-279-0279 or visit www.davisetfs.com. The total annual operating expense ratio as of the most recent prospectus was 0.65%. The Adviser is contractually committed to waive fees and/or reimburse the Fund's expenses to the extent necessary to cap total annual fund operating expenses at 0.65% until March 1, 2019. After that date, there is no assurance that Davis Selected Advisers, L.P. will continue to cap expenses. The expense cap cannot be terminated prior to that date, without the consent of the Board of Trustees. The expense ratio before the cap was 0.86%. The total annual operating expense ratio may vary in future years. Current performance may be higher or lower than the performance quoted.*

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Objective and Risks. Davis Select Worldwide ETF's investment objective is long-term growth of capital. There can be no assurance that the Fund will achieve its objective. Some important risks of an investment in the Fund are: **authorized participant concentration risk:** to the extent that Authorized Participants exit the business or are unable or unwilling to proceed with creation and/or redemption orders with respect to the Fund and no other Authorized Participant is able to step forward to create or redeem Creation Units, Fund shares may trade at a discount to NAV and could face delisting; **common stock risk, cybersecurity risk; depositary receipts risk:** depositary receipts involve higher expenses and may trade at a discount (or premium) to the underlying security; **emerging market risk:** securities of issuers in emerging and developing markets may present risks not found in more mature markets. As of June 30, 2018, Davis Select Worldwide ETF had approximately 34.2% of assets invested in emerging markets; **exchange-traded fund risk:** the Fund is subject to the risks of owning the underlying securities as well as the risks of owning an exchange-traded fund generally; **fees and expenses risk; foreign country risk; foreign currency risk; foreign market risk; headline risk; intraday indicative value risk:** the Fund's INAV agent intends to disseminate the approximate per share value of the Fund's published basket of portfolio securities every 15 seconds. The IIV should not be viewed as a ''real-time'' update of the NAV per share of the Fund because the IIV may not be calculated in the same manner as the NAV, the calculation of NAV may be subject to fair valuation at different prices, the IIV does not take into account Fund expenses, and the IIV calculations are based on local market prices and may not reflect events that occur subsequent to the local market's close; **large-capitalization companies risk; manager risk; market trading risk:** includes the possibility of an inactive market for Fund shares, losses from trading in secondary markets, periods of high volatility, and disruptions in the creation/redemption process. **ONE OR MORE OF THESE FACTORS, AMONG OTHERS, COULD LEAD TO THE FUND'S SHARES TRADING AT A PREMIUM OR DISCOUNT TO NAV; mid- and small-capitalization companies risk; and stock market risk.** See the prospectus for a complete description of the principal risks.

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The **MSCI ACWI (All Country World Index)** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets throughout the world. The Index includes reinvestment of dividends, net foreign withholding taxes. Investments cannot be made directly in an index.

Shares of the Davis Select Worldwide ETF are not deposits or obligations of any bank, are not guaranteed by any bank, are not insured by the FDIC or any other agency, and involve investment risks, including possible loss of the principal amount invested.

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