Rathbone Unit Trust Management

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Rathbones
Look forward

Rathbone UK Opportunities Fund

Update, October 2018

October was a grim month for markets and unfortunately particularly grim for our fund, which fell 10.7% versus the IA UK All Companies sector's 6.7% drop.

A combination of worries over trade wars, Italy's Budget deadlock, a never-ending Brexit, softening economic data and a pick-up in bond yields sparked a sharp correction. These factors came together to put pressure on corporate profits, leading to downbeat messages during earnings season. Companies that didn't meet expectations or lowered future guidance were punished harshly; down moves were even more acute for stocks perceived as highly rated growth names. Even 'growth' companies with no news to speak of were sold off. Additionally, while all size groups were down over the month, larger companies generally fared better at the expense of the smaller names.

These difficult conditions were compounded by a major fraud that was unearthed at **Patisserie Holdings**. We are sorry to say that 2.3% of our fund was invested in CAKE shares. Trading is currently suspended with the shares valued at 50p (compared to 430p immediately prior). We were very shocked by the news that the chief financial officer had been materially misstating the business's financial position – while it doesn't appear he did this for any great personal gain, we still don't have the full facts. The shares are likely to remain suspended for the foreseeable future as the investigation continues. We were, however, able to participate in the rescue rights issue in a small way. As we understand it, there is a viable business despite the fraud and we are reassured that initial re-stated estimates of profit have not changed in recent weeks. Our goal now is to maximise whatever value there is for unitholders, and to ensure we learn from this shambles. Corporate governance is high on our list. A small crumb of comfort: we bought our position initially at IPO and sold down half our holding after the shares more than doubled, thereby taking out our initial investment.

So far, we believe October's correction is more a valuation and confidence event than a genuine growth scare, but it's clear that certain segments of the market were intent on rapidly de-risking at the first sign of trouble. If you're looking for a silver lining, it has to be that multiples have de-rated and market technicals now look more supportive into year end. Indeed, November usually marks the start of a more favourable period for investors. We have been gently adding to our favoured holdings that look oversold, using some of the cash we raised in September. Although, we want to retain some firepower for the final months of the year, which could be unusually challenging given the looming Brexit negotiations.

In our view, a lot of the external concerns we noted above will linger. Also investors need to get used to higher interest rates, lower earnings growth and more global volatility. In an environment where consistent growth is becoming scarcer, investors will likely need to look a little harder and be willing to pay a little more for it. This fund is well set up for this: our natural skew is towards structural growth areas with differentiated offerings (which equals pricing power) and where forecasts are supported.

Alexandra Jackson, CFA
Fund Manager

This is a financial promotion relating to a particular fund. Any views and opinions are those of the investment manager, and coverage of any assets held must be taken in context of the constitution of the fund and in no way reflect an investment recommendation. Past performance should not be seen as an indication of future performance. The value of investments may go down as well as up and you may not get back your original investment.

Source performance data, Financial Express, bid to bid, net income re-invested.

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