

For professional
intermediaries only

Coming to America

A first hand look at
one of the world's
great growth engines



Rathbones
Look forward



David Coombs
Head of Multi-Asset Investments

David is Head of Multi Asset Investments for Rathbone Unit Trust Management. He lead manages the Rathbone Multi Asset Portfolios (Rathbone Strategic Growth, Rathbone Strategic Income, Total Return and Enhanced Growth Funds), and co-manages the Rathbone Strategic Bond Fund with Bryn Jones.

He is a member of Rathbones' Investment Executive Committee, with responsibility across the Group for Rathbones investment proposition offered to multi office financial advisory firms. He also sits on Rathbones' Strategic Asset Allocation Committee.

David joined Rathbones in April 2007 from Baring Asset Management, where he developed their absolute return investment process in the 1990s.

Over his 30 years experience (20 years plus in multi-asset management), David has managed unitised and segregated funds for institutional pension funds, captive insurance companies, corporate trustees and private clients including the Baring Optimum and Extended Risk funds. He joined Barings in 1988 from Hambros Bank in Guernsey, where he started his career in 1984.

David is an Associate of the Chartered Institute of Financial Services.



David Harrison
Global Equity Analyst

David joined Rathbones in June 2014 as a global equity analyst from Merrill Lynch. He is an assistant fund manager in the Income team and helps manage the Rathbone Heritage Fund. He is also lead manager of the Rathbone Global Sustainability Fund.

David has more than 17 years' experience in equity analysis and fund management, including positions at Hermes and Goldman Sachs. David holds the Investment Management Certificate and a BSc (Hons) in Economics and Politics from the University of Southampton. He is a CFA charter-holder.

The value of investments and the income from them may go down as well as up and you may not get back your original investment.

Never mind the gloomy talk of 'late-cycle capitalism', the US is booming right now.

For years I've believed that the US is one of the two great growth engines of the world and the place that sports many of the very best companies. But it's been a few years since I've crossed the pond and I wanted to find out first-hand how the American Main Streets were faring; I wanted to kick the tyres a bit, and most of all, test my views on the world's largest economy. News sites and brokers constantly feed certain narratives to us; I wanted to see the whole bubbling truth.

There has been a lot of murmuring lately about how expensive US stocks are and whether it's right to continue investing in them, an idea that recurs at regular intervals. We've maintained our bias to American equities throughout - we even increased it in 2016 following the election of President Donald Trump. This stance has often been at odds with our competitors, who constantly cite Europe's cheapness and the potential for a renaissance in productivity and growth. We just haven't been able to get on board with that argument, but I won't repeat our well-rehearsed reasons here.

So in early May, I set off with my colleague David Harrison (who covers US equities for the team). We planned to visit companies in New York, Connecticut, Chicago, Milwaukee, Minnesota and Atlanta. My six-day trip was a white-knuckle ride filled from top to bottom with meetings. Needless to say it didn't go quite to plan!

I kept a diary of my visit to make sure that my impressions of both the companies I met and the health of the wider economy were sharp and detailed for when I got back. I thought it would be helpful to share these insights with you.

David Coombs
Head of Multi-Asset Investments

This is what I discovered...

1. The US economy is in fine fettle — positivity everywhere

2. Capital spending discipline and attention to shareholder value is in senior managers' DNA

3. Companies here 'get' the Amazon threat — customer experience is much more of a focus than in the past

4. Similarly, they understand that data security is the number one threat to brand value
5. Corporate earnings are growing and reinvestment (capex) has increased

6. Skills shortages and wages are rising

7. Infrastructure needs a lot of work, although exactly where is a surprise

8. US is still behind on things we now take for granted:

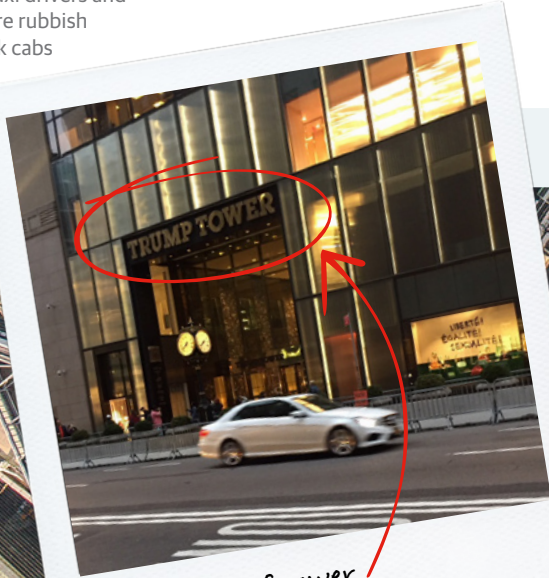
a. food labelling

b. contactless payments

c. decent duty free and airport malls

d. New York taxi drivers and their cars are rubbish versus black cabs
9. China's importance as a market clashes with American concerns about intellectual property theft

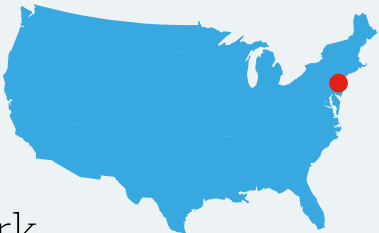
10. Nobody there cares about Brexit: it wasn't mentioned by any managers we met.



The centre of power

MAY
13

Day 1 Touchdown at JFK, New York



The start of our journey had a distinctly retro feel. I boarded an ancient British Airways Jumbo Jet (747) at Heathrow. Grubby and delayed because of a broken overhead cabin, the business class seats malfunctioned and the food was appalling. Even BA's business class is falling way behind competitors. Avoid International Airlines Group...

Still, the rickety plane made for a seamless arrival in New York's JFK Airport and, apparently, the 1970s. I swear Terminal 7 has not changed since I first visited as a teenager. Immigration queues remain long and slow (unrelenting and snail-like queues become a feature of the trip). America doesn't feel like a country that wants to be visited - is this America First?

I caught a ride to Manhattan. We drove across the Queensboro Bridge, famous for the intro of the sitcom *Taxi*. I started to worry about these 1970s throwbacks; was America really great again? The roads had more potholes than Swiss cheese and the infrastructure in the nation's foremost city felt decidedly Third World. Surely a US government is going to invest soon? It's an embarrassment. It's particularly jarring as I had recently returned from Crete. Its EU-funded roads were black-tar and smooth. Of course it's easier when you get to use someone else's money...

I met with David Harrison for dinner in Midtown. When it comes time to pay we use Amex: no contactless here, you still sign. The only nod to digital development is that you can sign on a terminal with your finger!

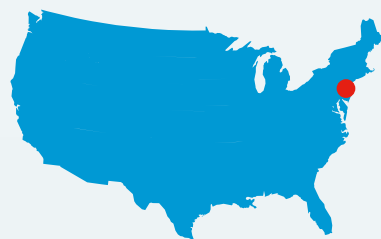


1901 - stunning but...



Blockchain in the mainstream

MAY 14 Day 2 Heading upstate



Whenever I'm overseas, I like to put the local news on when I'm getting ready for the day ahead. Today, I've gone for CNN. The first three stories are Trump, Trump and Trump. He has swooped in asking the US Department of Commerce to lift a crippling ban on Chinese handset manufacturer ZTE; the controversial US embassy in Jerusalem opens today; and then there's the omnipresent Russia probe.

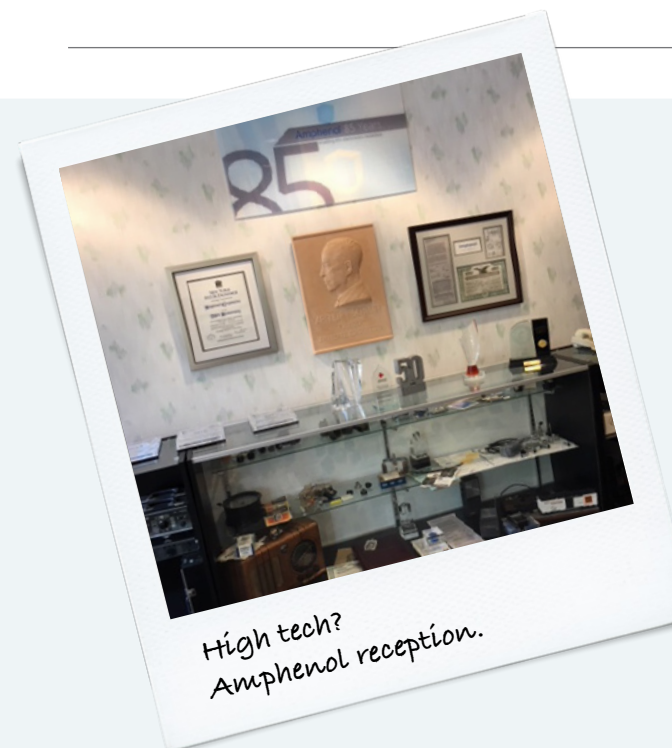
In fact, every day I watched CNN the only story was Donald Trump, except toward the end of the week when the American duchess fairy tale ending got traction. I suspect Americans were devastated that the President wasn't invited (past or present); I'm sure the happy royal couple weren't. Throughout my trip I found no-one speaking up for Mr Trump the man; however, no-one was complaining about his economic moves either.

As we drive up 6th Avenue out of Manhattan we pass a blockchain conference put on by CoinDesk and New York's economic development unit. A whole bunch of noisy demonstrators are outside, but at first glance they aren't your typical '99 Percenters'. A few placards and banners say they are Bankers Against Bitcoin. A quick Google shows the gathering is actually an ironic protest by cryptocurrency enthusiasts. They reckon new technology will sweep away the big banks if they don't adapt to the new world. I guess I can agree with that, although the protest bends my mind a little...

Speaking of currencies and payment systems, our first meeting is with household name Mastercard, which we have held for some time. Fittingly, its massive campus is based in Purchase, upstate New York. It's the American equivalent of Virginia Water, Surrey: leafy, wealthy and full of commuters. We soon find that Mastercard has enlisted G4S as security – the terrible gift that keeps on giving! 25 minutes after arriving we're allowed entry. This annoyance is partially offset when we're met by someone who zooms down the corridor on a scooter. You don't get that at Rathbones Central.

Mastercard believes the current global B2C market is approximately \$45trillion of which \$20trillion is currently transacted by card. However, it thinks the total market could be as large as \$220trillion if you include business-to-business transactions. Emerging markets are shaping up for particularly dramatic growth, especially Africa where millions have adopted mobile banking in lieu access to traditional banking. The opportunity for using prepaid debit cards and mobile technology for the 'unbanked' is particularly interesting to me. A good example is in Egypt where Mastercard ties your ID card to a national mobile money platform and the welfare system. You'd be surprised just how many unbanked people there are in America for that matter: about 8% of the population or 9 million households (it's 2.3% in the UK).

The business has a virtual global duopoly alongside Visa, with huge technological barriers to entry. The 'protesters' outside the crypto conference are right about the pace of



High tech?
Amphenol reception.

technological change, but it takes days to settle BitCoin transactions, a far cry from the payment giants' instantaneous networks. And BitCoin needs more power than New Zealand or the Czech Republic to function, despite accounting for a minuscule amount of global commerce. It's difficult to determine exactly, but the power needed for one BitCoin transaction is roughly the same as running an average house with all the typical appliances for a week. It takes Visa just one-sixth the juice to complete 100,000 transactions. In no way is that sustainable. I think cryptocurrencies have a long way to go before they challenge the likes of Mastercard and Visa.

We cross the state line to Connecticut, home to two businesses that we didn't own but wanted to see more of. One is an extraordinarily large industrial gas company that prides itself on safety and cash flow. It could be on the cusp of a massive expansion, which would test its admittedly adept managers and make it harder to keep its crucial safety standards high. It's also highly exposed to the global economy, for good or ill, which is a departure from most of our holdings.

The second company is Amphenol, one of the world's largest cabling/connection businesses. It designs and makes all sorts of connector cables for personal computers, data centres and fibre optic networks, as well as the wiring for cars, aircraft, hi-tech sensors, satellites and fridges. This is a boring company run by smart penny-pinchers with a problem-solving attitude.

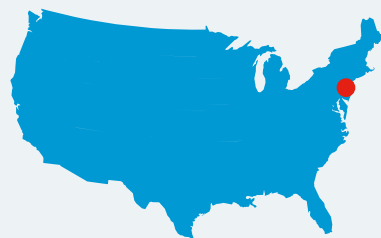
The offices are spartan, divisional leadership is highly devolved and the managers are lifers. They encourage managers to take chances on reasonable projects rather than spend their time avoiding failure. We liked this honest approach. This is also a case of necessity giving birth to invention. Components and parts are constantly squeezed on price and there is always the risk that customers start making the parts themselves if innovation isn't compelling enough. On balance we liked what we saw (we have since bought a small stake in the company).

Much to ponder after the first day of meetings!



Trump 'take over' on CNN

MAY 15 Day 3 The Big Apple



Today starts off like every other day:
with toothpaste.

We meet Colgate-Palmolive at Pret a Manger in Hudson Yards for 7am. Oh the glamour. Still, an interesting part of the city. Hudson Yards is quickly becoming the new financials hub as the final holdouts from Wall Street depart (no surprises that Deutsche Bank is pretty much the last one left on the street). This is a good reminder that change is the only constant. We have held Colgate, a consumer brands giant, for about two years, but we have been debating whether we continue over the past few months. We believe consumers are rapidly becoming much keener on value for money, which is dangerous for a firm that touts significant margins on simple products with countless challengers. The Western consumer brand giants are being outflanked on the super-premium end too: tastes are different out East and companies have to understand and adapt – particularly in the home. A new Chinese rival is growing swiftly with its green tea and jasmine flavours at punchy price tags; similarly Splat in Russia offers charcoal and juniper-flavoured toothpaste with zero fluoride. This vegan-friendly eco brand has already made inroads in the UK.

One interesting comment from our meeting: Colgate thinks Alibaba's data is far superior to Amazon's. The Western focus is very much on the American titans, but investors ignore the Eastern rivals at their peril. They have comprehensively beaten the Silicon Valley raiders wherever they have clashed in Asia.

Next, we meet several banks and a large business strategy consultancy that we have been pondering as additions to our portfolios. US banks have that incredible global scale that is the greatest advantage in financial services. Of course, such unwieldy size has its own problems: poor systems and bad customer experiences can be highly damaging. Because of this, most of the banks we spoke with are investing billions in IT and customer support. As hard as it is for Brits to fathom, this spending includes improving their branch networks. Unlike the UK where the market has fragmented dramatically, American banks are still the gatekeepers important for moving all sorts of products from car insurance to mortgages and life assurance. Millennials are visiting US branches much more than you would think too. It's important for us to register how markets differ depending on the country: it can call for a radical change in a business's strategy.

The business consultancy is also highly geared to the development of the digital economy and helping old world businesses quickly adapt to the needs of the new. Cyber-protection is a very promising growth area. This could be a particularly lucrative business model if they manage to expand to nations that are behind the digital curve.

Our last meeting of the day is the polar opposite of Pret a Manger: Estée Lauder. This office was as opulent as you would expect from a purveyor of premium beauty products. It looked like a French drawing room and the view overlooking Central Park from the south was majestic.

However, this brand is more 'woke' than the decorated porcelain and gold candelabras would have you believe. We hold this company because it has a lucrative knack for picking up small brands and building them into massive premier franchises that command astounding loyalty from its customers. Estée's North American growth is minimal, but we think its success in China and other developing markets should more than offset that. Still, this business has to overcome some huge challenges: department stores, its traditional stomping ground, are dying. It's having to adapt its 'try then buy' business model to the internet.

Still, I reckon there's plenty of money for Estée to make when the US gets around to refurbishing the tired airport malls and duty-free shops I've seen so far...



*Estée Lauder's reception above
the Apple store sends a message!*

We're halfway to La Guardia Airport to catch a flight to Chicago when we're hit by a severe thunderstorm. By the time we reach the airport all flights are cancelled and all of New York's airports have shutdown runways for the evening. Chaos. After a lengthy wait, American Airlines rebooks us onto a flight to Minneapolis at 2.30pm tomorrow. Our meeting with the Northern Trust chief financial officer in Chicago has to be cancelled. It's a shame as I knew him from my days at Barings/Northern Trust in the early noughties. Our meetings with Ulta Beauty in Chicago and a Milwaukee boilermaker are also down the pan.

We called our corporate travel agent to help us find some last-minute hotel rooms. According to the internet, there were no rooms left anywhere in New York due to the number of people stranded. But he could book us on an early flight to Milwaukee in the morning – the boilermaker meeting is saved! Spirits lifted.

We rode a cab to Manhattan to try our luck door-knocking for a room. We had found a number of (suddenly more expensive) hotels available on Expedia and Booking.com, but any booking attempt crashed midway through. We arrived at the first hotel we had tried to book. Maurice, the head receptionist, was delighted to see us and indeed had two free rooms at \$1,500 each. He had us by the particulars. We accepted. He did throw in free premium Wifi. Bargain.

More importantly, Maurice explained the reason why the internet had failed us. As soon as there's any travel disruption, all the hotels pull their rooms from the booking sites. Next time we meet managers from these aggregator services, we might ask about this...



MAY
16

Day 4 Halfway to the Midwest

We arrive at La Guardia for 6.30am to find out our flight has been cancelled. The boilermaker meeting was just not meant to be. At least we still have the first flight to Minneapolis, as we hadn't cancelled it (it pays to be dubious of good fortune here).

We relocated to Greenwich Village for breakfast. Unfortunately the 'City that Never Sleeps' doesn't open for food or coffee until 8am here. We made our way back to the airport around mid-morning to find our plane hadn't been cancelled – huzzah! – unfortunately, our tickets had been. We pitched our plight to four members of staff before we managed to rebook at no cost. Basically they took pity on us.

When we got on the plane we found out it was over booked and they needed three passengers

to get off the plane. Guilt compounded our sorrows. But we did get to see one of those bizarre auctions for people to give up their seats that made the headlines last year – luckily no-one was dragged off our flight. The bidding started at \$200 and got to \$600 before two younger travellers took the money. It's no wonder domestic airlines have such appalling customer satisfaction. Avoid. Even when they look cheap. Remember this trip and avoid.

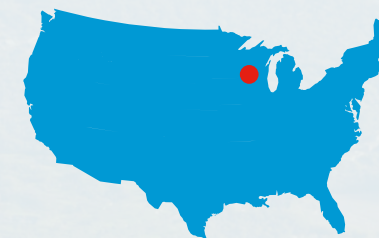
We get to Minneapolis in the mid-afternoon. It threw me that this Midwestern airport on the edge of the Great Plains was by far the best I have seen in the US. The whole city and surrounding areas seem prosperous and vibrant. It boasts a handful of Fortune 500 companies and strong clusters for finance, healthcare transportation and industry.

All of our day's meetings have been canned because of the travel disruption. But we take the time in a downtown diner to go over our notes and chat about what we've seen and heard so far. The place is full to the rafters, like all the others we saw. You can't help feeling this was a town doing well. David Harrison's carrot cake alone confirms this: it's the size of a small breeze block. Combating obesity is one of our key investment themes. David's research in this area was above and beyond the call of duty.



Combating obesity. The message is not getting through!

MAY 17 Day 5 The Twins



If you love omelettes, Manny's Steakhouse in Minneapolis is worth dying for: Prime Rib, sausages and bacon and a bit of egg to make it all stick together. We're meeting the head of investor relations for one of the state's namesake companies and trying to keep our mind on the business at hand.

This manufacturing company invented sellotape and countless other adhesive products. It now makes all sorts for consumers and businesses, including medical tools, fire protectors, car-care products, optical film and circuitry. For almost a century, every chief executive it appointed was an internal hire and the firm was run as if it were a family business. Recently its signed leaders from outside the company, bringing helpful fresh eyes to its operation and helping it focus.

It can be difficult for a company that prides itself on innovation to avoid getting lost in the weeds on projects that are likely to be fruitless. But it can be easy for a new culture to suffocate the old, along with the lateral thinking that led to its past successes...



18 Fortune 500 companies
headquarter in 'The Mini Apple'

We drive across the Mississippi River to St. Paul, which makes up the other half of the Twin Cities area. We have to endure another 20-minute registration ordeal at chemical manufacturer Ecolab, but it turns out to be well worth it in the end. It commands a hefty market share, giving it the scale to keep costs low and allow enough elbow room to spend money on R&D.

The largest portion of its business is supplying cleaning products for the restaurant and food industries, but it also supplies water treatment facilities, hotels and hospitals, among others. This isn't just truckloads of bleach. Ecolab is designing hardtops that actively kill bacteria and dangerous microbes for food processors. It is making extremely efficient cleaning agents that need only a fraction of the water previously used. Ecolab's chemicals reduce an industrial dishwasher cycle to one minute! Compare that to your one at home. We decided to buy this company soon after the meeting.

What attracted us was that their philosophy is driven by what would help their customers. By constantly improving the products and service it offers, Ecolab saves money for its clients even as it raises its own prices. Still, its products are about 20% more expensive than its rivals', so if innovation hits a rough patch – or competitors catch up – there's a risk that it starts to lose customers and pricing power.

Back to Minneapolis to visit US Bancorp, the fifth-largest bank in the US. Its place at the top of the second stratum of the American financial world is actually quite positive. It doesn't have any of the investment banking divisions that make the large firms so volatile, but Bancorp still has the scale to serve both the people and the businesses on Main Streets across the Midwest (the mix is 50/50) while delivering a best-in-class return on equity of 13.4%. There is plenty of scope for efficiency gains here: almost three-quarters of business to business payments in the US are cleared by cheque! Over the past few years it has built a strong corporate services and lending business for larger enterprises across the country, but the mainstay of its operation is Middle America, both geographically and socially. You have probably realised that we are more upbeat on working class America than the average manager.

We bought US Bancorp soon after our meeting because we felt it was in a great position to capitalise on this grass-roots improvement in the US economy.

After a couple more meetings we headed to the airport to catch a late flight to the South. We arrived in Atlanta and checked in about midnight. Totally beat.

MAY 18 Day 6 Atlanta

It felt like my head had hardly hit the pillow before I was furiously hitting the buzzing red 05:30 floating next to my face.

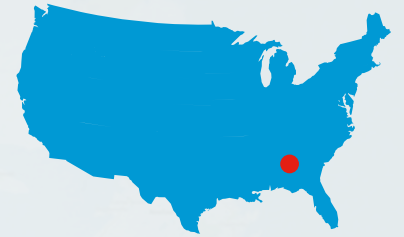
The first meeting of the day is with a home improvement giant (think B&Q or Homebase). It has a network of more than 2,000 stores, mostly in the US but also Mexico, Canada and South America. The biggest driver of its business is the US housing market, which has been improving steadily for a few years now. Of particular note is the change in fortunes for some of the less-glamorous towns and cities. Many homeowners have only recently been able to sell houses they bought for inflated prices at the height of the '05/'06 property bubble. Earlier this year, I read a *Wall Street Journal* reporter's account of how it took him about 10 years and a \$25,000 haircut to get rid of his albatross house in neighbouring Alabama. His story is just one among millions: US foreclosures are only now getting back to pre-crisis lows, helping encourage the recovery in property prices that has significantly cut the number of homeowners with negative equity.

Why does this matter? When these households finally see light at the end of the tunnel, the effect on their confidence is substantial. They are free to move, to take new opportunities or, perhaps, embark on renovations to help boost the value of their homes. Home improvement stores should benefit from this, as well as from tradesmen who are encouraged to build new homes because of the higher prices. The parable of selling pickaxes for a gold rush comes to mind. However, that's a little too simplistic.

Large stores like this one employ a lot of people, particularly at the low-skill end of the market. And rather than cut staff, the company plans to increase the amount of handy DIY advice its shop assistants can offer. That means its labour costs are at risk of rising quickly given the strength of the US labour market. It is also investing heavily in a flexible and rapid delivery network, particularly for its trade customers.

The reasoning behind these strategies appears sound: by offering industry advice and flexibility it hopes to keep Amazon at bay and attract more professional business. It's focusing on its customers. We like what the housing revival implies for the US economy, but we prefer to play this through a different company. One thing's for sure: unlike the UK where big-box hardware stores are in disarray, American hardware stores have strong free cash flow and confidence.

The last meeting is with one of the scores of auto-part suppliers that have popped up in Georgia (and Alabama) over the past decade or so. After years of outsourcing parts manufacturing to Asia, the trend has definitely reversed in this industry. Relatively cheap labour (as wages rose in the East and South America) and the ability to hit quicker delivery targets created a competitive advantage down here. We met the chief executive a week earlier back in London and we thought we'd head out and visit one of their distribution centres. Anyone expecting a mythical big-box warehouse full of robots and flying drones would be disappointed.



I say farewell to David and travel to the airport for my flight home via New York. I'm not confident that my flight will actually take off, or that I'll be on it if it does...

As it happens the plane is on time and I'm on the manifest. But it soon transpires that I'm not on time. As the time to departure ticks away the security queue continues to wind endlessly ahead of me. Finally, I blag my way into the fast track – a Welsh accent during the royal wedding week is a distinct advantage (they can't tell the difference) – and make the gate with minutes to spare.



Suburbia makes a comeback

Inflight debrief

I believe these sorts of trips are invaluable. All the experiences – good and bad, large and small, serious and humorous – have a bearing on how you think about investing.

We all know the US is big, but its titanic vastness is brought into serious focus when you consider the logistical challenges it took for us to see only a small part of it. While we visited only a handful of cities, they were spread across the nation and, we believe, should offer a decent sample of the nation. We saw 14 companies across a range of industries in less than a week and it really gave us a feel for common themes such as employment and confidence. You don't get that seeing foreign companies ad-hoc back in the UK.

I was surprised and encouraged to hear that most of the companies we spoke with had used the recent tax windfalls to invest in their businesses and give bonuses or pay rises to their employees: the 'trickle down' effect working in practice. Managers were keen to increase capex to support growth, an attitude that is less popular with companies in the UK and Europe. Everyone was very confident on both US and Chinese consumers. They saw opportunities for growth in the US, Asia and the Americas. Optimism for European markets was much patchier. Some companies were polite, but slightly sceptical about capital discipline in Europe and the constraints of the labour market there.

I went to the US with a positive outlook. I returned, somehow, even more confident and with a number of promising candidates for our portfolios. The business cycle doesn't seem to be about to turn down to me. The main risk is probably a monetary policy misstep by the Federal Reserve; however, company managers are relaxed about the gradual path currently set out.

I'm used to US companies' dogged focus on shareholder value, but what struck me during this visit was the greater emphasis on creating value for the customer as well. When done well this gives businesses tremendous pricing power. When you become a major source of efficiency for your customers, it costs customers more to go with the cheaper option. Some teams were honest and admitted that complacency had meant they missed some of the new trends in e-commerce and the digital economy.

This concurs with one of our core themes: be the cheapest or the best; anything in between is toast.

So our bias to the US over Europe continues. I don't anticipate that changing in the foreseeable future. This trip reminded me that there is no substitute for meeting managers in their own backyard, particularly for a long-term investment approach like ours. We want to make sure these teams can be trusted to maximise the return on your money.



NY – never knowingly undersold!



Taxi to anywhere please!

Get in touch

For more information, contact our intermediaries team on 020 7399 0000 or visit rathbones.com

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Past performance should not be seen as an indication of future performance. Changes in rates of exchange between currencies may cause the value of investments to decrease or increase.

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