Rathbone Unit Trust Management

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Rathbones
Look forward

Rathbone Global Opportunities Fund

Update, October 2019

In October, the Rathbone Global Opportunities Fund returned -1.7% versus a -2% average for the IA Global sector. Year to date your fund is up 21.1%.

Over the past three months, returns from funds in our sector have been widely dispersed. As the stock market rotates out of ‘growth’ companies into ‘value’ oriented strategies, businesses with resilient and visible earnings have been sold in the hunt for earnings recovery potential.

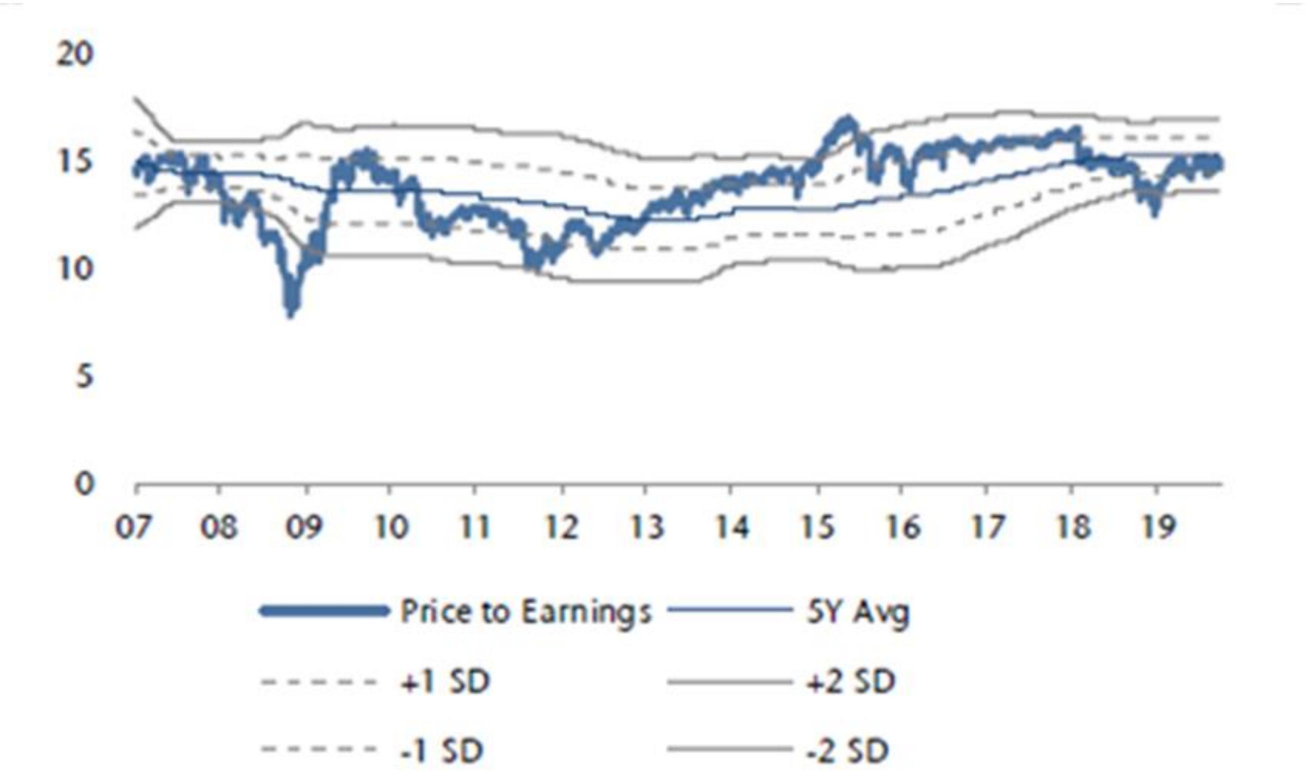
For much of the past couple of years, these value stocks have lagged because a sluggish economy encouraged nervous investors to put yet-higher premiums on sustainable growth. But by the end of the summer, panic about the global economy and the trade war had pushed this growth premium too far. Some brave contrarian investors have now started buying these cyclical companies, which are highly operationally geared if a recovery is unmasked. Value sectors like autos, commodities, industrials, construction and banks have roared back to life. The risk with this strategy is that it is running ahead of the evidence, albeit as it did (correctly) in March 2009. But this time round it could be a false dawn: it relies heavily on businesses restocking inventory and economic growth accelerating.

As a growth-focused fund, the tide is against us. Yet good stock-picking and strong third-quarter results kept our performance in line with the October sector average. Year-to-date returns are still healthy at +21%. We don’t like companies whose main driver of success is an economic resurgence, instead preferring robust and resilient growth stocks, and companies that are significantly outgrowing traditional competitors.

Our top performers this month required knockout results or a major stock-specific driver to push their prices higher. **RingCentral** was top of the leaderboard this month and is one of our best performers in 2019. The cloud-based telephone provider announced a partnership with Avaya which gives it immediate access to Avaya’s 100 million on-premise users. This meaningfully accelerates RingCentral’s shift from legacy corporate telecom systems to cheaper cloud-based systems offering office workers much more functionality and collaboration and improved productivity. Another outperformer, but in a very different corner of the technology world, was semiconductor company **Nvidia**. This company’s growth potential was highly out of favour last year because investors were worried about the trade war and customers had reduced computer chip inventories to conserve cash ahead of an economic slowdown. But Nvidia remains at the cutting edge of PC gaming and data centre growth, and investors are starting to see green shoots of a cycle turn in what most consider to be a best-in-class business in a volatile industry.

Our worst performers this month were generally victims of a “sell the winners” strategy. Investors wanted to rotate into laggards and earnings recovery stories. **Costar**, a holding that has quietly become our portfolio’s second-best performer year to date, was hit by profit-taking. This business is often called the Bloomberg of commercial real estate. Costar’s database holds vital details about 6 million properties – essential for investors, brokers, landlords and tenants – and there is no competitor and no alternative to this vital information.

US valuations are in no way stretched



Source: FactSet, Jefferies

Investors clearly feel that the probability of a recession is receding. A supportive US Federal Reserve and no further escalation in the trade war is encouraging risk-taking in the most cyclical sectors of the market. All the bad news is already discounted in prices for these sectors, so they would be highly geared if the economy beats back the recession that many thought was a dead certainty. The skittishness is now aimed at growth stocks that show any sign of faltering. Strong share price returns in the year so far imply little room for error. But America continues to show the strongest fundamentals and continued cries of high valuations ring hollow when you look at the data. The chart above shows the S&P 500's forward price/earnings ratio is actually trading below its five-year average.

The UK stock market has started to recover recently as the odds of a crash-out 'no deal' fade. We still have very little insight into the actual outcome, so prefer to focus our firepower on overseas investments. But clearly the recent strength of sterling has been a headwind for us and will remain a risk for all unhedged global equity funds like ours.

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

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