

Rathbone Multi-Asset Strategic Growth Portfolio

Update, April 2018

Overview



Despite virtually all major UK economic data undershooting expectations, the FTSE All-Share has been on a rip lately.

The index was up 6.4% in April, its greatest monthly rise in almost five years, and the FTSE 100 was up even more. The slump in sterling following the Bank of England's about-turn on a May rate hike would no doubt have helped. So would higher oil prices and a rise in many defensive sectors, including utilities and telcos, which combine to make up a large proportion of the UK market.

There have been a lot of proposed mergers and acquisitions on both sides of the Atlantic as well. It seems like many of these tie-ups – Sainsbury's/Asda, Sprint/T-Mobile, Takeda/Shire – are the result of companies reaching for growth. With economic expansion so lacklustre, for some the only option is to pay up for it.

The construction PMI was a bright spot for the UK, bouncing back from a weather-beaten March to wildly top estimates in April. However, services and manufacturing were both muted. Rather than coming in flat at 2.7%, inflation decelerated to 2.5%. Retail sales were just 1.1% higher than a year ago and the GfK Consumer Confidence Index dropped noticeably over the month. GDP growth was just 0.1% in the first-quarter, well below the 0.3% expected. Since the first quarter of 2017, the annual rate of GDP growth has crumbled from 2.1% to 1.2%.

All of this led BoE Governor Mark Carney to renege on his widely expected interest rate hike. By mid-April Bloomberg put the probability of a May hike at 96%, so the reversal led trade-weighted sterling to slump more than 2% from its recent peak.

Meanwhile, the dollar has been rising after an extended slump. The trade-weighted greenback was up 2% in April and has gone even higher since month-end. At time of writing the sterling-dollar exchange rate was just above \$1.36. US retail sales beat analyst forecasts, the number of people who have recently signed on for unemployment benefits is lower than anytime since 1969 and house prices are growing well. ISM Manufacturing figures disappointed, but the measure is still at a very healthy level. Most investors believe the Federal Reserve will continue with its slow-but-steady tightening of interest rates and we are inclined to agree. A 25bps increase to 1.75-2.00% is all but locked in for June, according to Bloomberg.

This month's trades

We have sold **AB-InBev** because we were concerned about how slowly it's reducing its debt burden after the SABMiller takeover. Also, increasing competition in beer markets may lead to a lack of pricing power. Also, we trimmed the **Tritax Big Box REIT** after its premium over net asset value rose during the month.

We bought the **Gilt 1.5% 2026** as 10-year yields approached 1.60%. We think sterling and bond yields will be pretty volatile for the foreseeable future, so we are taking the opportunity to buy duration (interest rate sensitivity) whenever the price drops significantly.

We also started a position in **WEC Energy Group**, a Midwestern gas and electric power generation and distribution company that has spread from its home state of Wisconsin into neighbouring Illinois and Minnesota. It also owns transmission networks in California. We think this company is in a great position, with a spread of nuclear, coal, natural gas and renewable assets. About 95% of its business is regulated monopoly, meaning it can invest in updating its network and churn out a reasonable return on equity. We think the roll out of new technology should help reduce its costs, giving it a modest boost to earnings in coming years.

Outlook

Last month the US 10-year Treasury yield breached 3% for the first time since January 2014. As interest rates continue to rise, and the cost of equity with them, it reinforces our preference for companies with low levels of debt. We are also happier holding companies that can generate their own growth without recourse to paying large multiples to acquire competitors.

Considering the chaotic and uncertain Sino-American trade clash and the steadily tightening monetary policy around the globe, we believe this year is likely to be a gruelling trek for investors. We have bolstered our portfolio protection by adding to our commodities exposure, buying safe haven assets, and purchasing put options on the S&P 500. We have also been increasing our gilts position from virtually zero whenever yields have risen to an attractive level.

We're comfortable with how the US economy is ticking along, although we are not too optimistic about the UK. Politics and national posturing will likely dominate the headlines this year, injecting fear into markets at times. We will be trying to use these downturns to our advantage: by buying great businesses at lower prices.

David Coombs
Head of Multi-Asset Investments

Will McIntosh-Whyte
Assistant Fund Manager

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