

# Rathbone Multi-Asset Total Return Portfolio

Update, November 2017

## Overview



Shortly after month end, the US Senate approved its tax reform bill. The draft plan, which is still to be reconciled with the House of Representatives version, offers a decent reduction in statutory tax rates and the ability for companies to expense 100% of investments into plant and equipment upfront for the next five years.

The generous expensing allowance makes it more compelling for companies to invest now and reap the benefits of better productivity and higher revenues in the future. Industrials, which we own quite a lot of, would do very well out of this – as would the banks that would finance much of the spending. Both sectors have soared in the past week or so. As for the lowering of corporate taxes, that has different effects on different parts of the share market. Banks, particularly those that do a large proportion of their business in the US, actually pay relatively high effective taxes rates. Dropping the tax rate to 20% should boost their profitability significantly. Technology, meanwhile, could lose out from alterations that would negate their research and development tax credits, effectively boosting their effective tax rate.

We think this rotation from growth to value has got a little out of hand. Also, we believe the overall growth effects of the tax plan, if it's ratified, will be significantly lower than the market seems to expect.

Markets broadly shrugged off several political set-pieces in November. The investigation into the Trump campaign's improper contact with Russian officials rumbled on, the UK Budget was a yawn-fest and Jerome Powell was appointed as next Federal Reserve Chair. The 10-year gilt began and ended November at 1.33%, while the US treasury yield went from 2.38% to 2.41%.

Earnings have been pretty good recently, but investors seem to be less inclined to reward strong performance as they are to punish missteps.

## This month's trades

We bought the **Tesco Personal Finance 1% Index-Linked 2019** bond at a price that completely protects our capital in real terms – after RPI inflation which is currently running at 4% – over the next two years. The risk to our investment here is if Tesco goes bankrupt during that time, which we believe is highly unlikely.

Another purchase was the **Legal & General Group 5.875% Subordinated 2049-19** bond. This is a high-coupon issue that can be bought back at par by L&G in 2019, something that we expect will happen. This gives us a slightly higher yield, but the duration – sensitivity to changes in interest rates – will actually be relatively low.

Following this year's spate of destructive storms and earthquakes, we bought a C-share issue of the **CATCo Reinsurance Opportunities Fund**. This fund takes on the ultimate calamity risk for

insurance companies. After large scale losses, such as we have just witnessed, premiums for this kind of risk tend to balloon. Historically, this tends to be a lucrative time to invest in reinsurance.

We sold some shares in the **Tritax Big Box REIT**, which leases distribution warehouses to blue chip clients. We took some profits in information provider **RELX** after the share price rose over the past couple of months.

## Outlook

Investors have been complaining about this equity bull market for what feels like years. It's an odd situation, as it doesn't really seem like something you should be complaining about. Still, we get the point: things are getting pricey, particularly those stocks that everybody wants to own.

Because of our mandate, we are less inclined to shoot for the moon and get every bit of market upside. Instead, we can focus on delivering the returns our investors expect, with less volatility than the market. Timing markets is very difficult, and we don't try to. We've been building up significant cash holdings but, importantly, this cash has come from selling government bonds, not from selling equities. We have also reduced our commercial property funds.

Holding this cash keeps our portfolio risk in-line with our targets at a time when we find bonds supremely unattractive and gives us the flexibility to take advantage of a correction – in bonds, equities or otherwise.

We continue to be optimistic about equities because the chances of a recession in the US or China are remote. Any sign of potential recession in these two countries would lead us to reassess our strategy, as such a downturn would drag the rest of the globe into recession too.

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