Rathbone Unit Trust Management

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Rathbones
Look forward

Rathbone Multi-Asset Defensive Growth Portfolio

Monthly update April 2022

April was another brutal month for markets as government bond yields continued to grind higher.

Speculative technology stocks – those burning cash by the barrel with no profits in sight – have been absolutely clobbered by rising interest rates. Some quality 'growth' businesses, which do have profitable business models, have been caught up in this downdraft. We own a few of them and have been buying into the falls in these stocks.

The pain has continued into May. Pay no heed to technicalities: we are in a bear market for stocks. That doesn't necessarily mean that markets are doomed for the foreseeable, but there definitely needs to be a whole host of good news for stock prices to perk up again. With rates higher and likely to rise further, price-earnings multiples are unlikely to return to the record levels of the past few years. Yet profit growth is still possible, for quality businesses run by savvy managers.

Clarity is difficult given the complexity of current conditions, but we think interest rates will peak at a lower level than most people expect – especially if American inflation does continue to fall back from its highs over the coming months. It's hard to say exactly where rates will peak, but a lower level than the highs most expect would be welcomed by investors who see nothing but gloom at the moment.

The FTSE foil

One turn-up for the books was the change in fortunes of the FTSE 100 Index. Large-cap UK companies have lagged global peers for years and years, yet since commodity prices and bond yields have leapt, the petrochemical, mining and pharmaceutical and utilities-heavy index has been like a buoy as other stock markets plunge deep underwater. While we are wary of the fragility of the UK economy, we have a healthy number of investments in multinationals who just happen to be listed here in the UK. Solid businesses that tended to go for a discount solely because they are priced in pounds, like miner **Rio Tinto**, oil major **Shell**, and electricity and pipe network **National Grid**.

During April the prices of shorter-dated US Treasury Inflation-Protected Securities (TIPS) began assuming a huge amount of inflation. Because of this increase in their price, we sold our **US TIPS 0.125% 2024** bonds and replaced them with the cheaper **US TIPS 0.125% 2031**, which looked better value.

We bought more conventional, fixed-rate bonds as well, as the rapid rise in yields made them more attractive. These included the **US Treasury 1.875% 2032** and the **UK Treasury 4 ¼% 2032**. We also bought a bunch of corporate debt, across a range of short and medium-term maturities and different credit qualities, such as the **BNP Paribas 3.375% Senior Non-Preferred 2026**, the **Yorkshire Building Society 3% 2025** and the **Beazley Insurance 5.5% 2029**. We used cash we have been holding in the fund for just this sort of rainy day, so our cash holdings have fallen significantly.

We took profits from aerospace giant **Lockheed Martin** after it rallied strongly on increased defence spending in the wake of Russia's invasion of Ukraine. We also trimmed **SSE**, which had benefited from the jump in power prices. We topped up some of our stocks on market weakness. Many strong businesses have been clobbered because they are filed too closely to some very speculative cash-burners. We think many stock prices have dipped too low, given the business potential over the coming five to 10 years.

Which will prevail?

Bond yields continued to march higher in April and early May, yet they have sunk back slightly as recession concerns have bubbled to the surface. Extremely weak sentiment surveys – from households through businesses and investors – have combined with disappointing retail sales and PMI readings to renew worries about a global slowdown. The cost of living has skyrocketed all over the world, pinching many people's spending power. Meanwhile rapid rises in the cost of labour and raw materials have tripped up more than a few companies reporting earnings.

The sugar rush from reopening, driven by pent-up savings and boredom, still seems to be driving a lot of people's decisions. Flights are full again, restaurants and pubs seem to be doing alright. But the question is how quickly people may rein in spending as the summer of high prices rolls on. Wages are rising though, which could offset some of the effects and support spending.

We're feeling better about the prospects for the US, rather than Europe and the UK, where the Ukraine war and upended energy markets are having a greater impact. This year has been a painful one for holders of US companies, yet we are sticking with our focus on exposure to America. We have added steadily to our companies throughout the drawdowns.

Emerging markets are also under the cosh. Food and transport costs are a much higher proportion of people's spending in poorer nations, so the dramatic increases are potentially devastating. Meanwhile China, the locomotive driving Asian demand and the nexus for supplying good to the world, is wedded to a zero-COVID policy that is economically crippling. Several developing countries are already showing signs of social strain. This sad tale appears to be only in its opening act.

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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 and the income from them may go down as well as up and you may not get back what you originally invested.

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7835.05.22