

Rathbone SICAV Multi-Asset Total Return Portfolio

Quarterly investment update, July to end September 2022



Rathbones
Look forward



This is a marketing communication

Hot topics – ‘Top-down’ (market and macroeconomic)

Wild ride. We’ve become accustomed to some breakneck market shifts in recent years, yet they pale in comparison to this September. Equities around the world tumbled back after getting more than a little overoptimistic about the US Federal Reserve (Fed) shying away from interest rate hikes. Yet bond markets were arguably the epicentre of the pain. The US 10-year government bond yield rose about 150 basis points from its August low to 4% in the dying days of September. In the UK, in the wake of



the mini-budget, it was even worse at a roughly 250 basis points increase. This flowed through to corporate bond yields as well, with their spreads (the extra return over government bond yields to compensate for the risk of default) flying much higher. We were sceptical of the run-up in markets, so the disintegration of the rally wasn’t a surprise; the sheer violence of the moves was, however. We think US interest rates will continue to rise to about 4%. If the Fed goes much higher than that, we think it will increase the chance of a deep global recession (i.e. that it would be a policy mistake). Yet when interest rates rise rapidly, as they are now, it puts strain on everything, causing things to break. As usual, we took advantage of the volatility to trade where we were able (liquidity evaporated often in many markets). This meant a lot of buys, sells, switches, crystallising of profits and tactical moves. The UK seemingly now has a permanently higher cost of borrowing and capital to account for less credibility at the top. While this is disappointing and arguably unnecessary, in time it should make gilts and some UK companies more attractive investments, both to us and to overseas investors.

Mini-catastrophe. The UK mini-budget was an own goal. New Prime Minister Liz Truss and her Chancellor Kwasi Kwarteng admirably tried a bold dash for boosting flagging economic growth – a particularly apt idea given the nation is headed for recession. However, the fiscal set-piece was bungled from the start by a lack of communication, a cocksure disregard for the fiscal watchdog and a failure to read the room politically. The announcement of unfunded tax cuts for the wealthiest went down like a lead balloon with investors and voters alike. Sterling plunged, government bond yields soared (taking mortgage rates with them) and Labour took a 30-something-point lead in the polls. Having said all that, the plan does actually have some coherency to it. Encouraging work by increasing the amount people keep for themselves should improve output and therefore potentially increase the total tax take. Doing this by adjusting the tax rate thresholds rather than tinkering with the rates themselves



would have been a more astute and fair way to do it. Meanwhile, plans to reform planning laws and reduce regulation are more than welcome and a long time coming. Whether they can convince Conservative MPs and voters is another matter though.

High-cost energy. The number one biggest upset to the world today is the considerable rise in the cost of energy. This is tremendously broad brush – the world is a mess of different causes, effects and complexities. Yet it really does seem that much of the upheaval and strains of 2022 have their roots in a world that became accustomed to cheap and abundant energy, which was then suddenly taken away. Power is a crucial input for virtually everything. Without it, there’s no technological uplift, so the progress of centuries is discounted. And when it becomes more expensive and rationed, it means less output is possible or profitable, and less fun can be afforded by everyone. There is actually one of those ‘theory of everything’ sort of arguments



that says booms and busts can be mapped solely on the cost and abundance of popular energy sources. Our current energy crisis has its base in climate change, really. It’s a dirty secret of Western nations that, to reduce carbon emissions, they became ever more dependent on gas for heating and electricity generation. While a much cleaner option than coal, it is still bad for the environment and requires long-term infrastructure that binds you to specific suppliers. Not only that, but in Europe in particular, it meant countries were dependent on regimes that became politically troublesome. This year, Russian President Vladimir Putin jumped the shark and invaded Ukraine. It was perhaps inevitable that this decision would lead to the gas pipes being turned off to Europe (the cognitive dissonance, for both sides, of continuing this trade relationship while effectively in a proxy war was simply too great). And so, finally, this quarter Putin turned the taps off, sending gas prices spiking once again. Meanwhile, oil prices remain relatively high, especially given the monumental strength of the dollar, coached that way by the organisation of the petroleum exporting countries (OPEC) cartel. Because of the need to reduce the carbon intensity of our societies, supply of hydrocarbons is politically constrained, so the era of low-cost energy is probably behind us. At least until the next energy source comes along. That requires some adjustment from everyone – people, businesses and governments.

Portfolio activity

Key purchases/additions	Key sales/trims
Aviva 6.125% Subordinated 2036 (new purchase)	US Treasury 0.25% Inflation-Protected Securities (TIPS) 2025 (sale)
NatWest 5.125% Perpetual (new purchase)	iShares China CNY Bond ETF (sale)
Zurich Finance (UK) 6.625% Floating Rate Perpetual (new purchase)	Amazon (trim)
Merck (new purchase)	Aptiv (trim)
Apple (new purchase)	Ulta Beauty (trim)

Source: Rathbones

As bond yields flew higher around the world, we added to our holdings of the **US Treasury 1.875% 2032** and **2.5% 2024**, and the **UK Government 4.25% 2032** and 1.5% 2026 following the mini-budget. While rates likely have a bit further to rise, we believe it was time to start adding to these sorts of assets to protect ourselves if yields fall suddenly, as they would if the world tumbles into recession, for instance. Meanwhile, we sold our **US Treasury 0.25% Inflation-Protected Securities (TIPS) 2025** and **0.125% TIPS 2031** in late July and August.

We bought a few high-yielding corporate bonds as well, as corporate spreads moved significantly higher over the quarter. They included insurer **Aviva 6.125% Subordinated 2036**, lenders **NatWest 5.125% Perpetual** and **Zurich Finance (UK) 6.625% Floating Rate Perpetual**, airport business **Heathrow Funding 7.125% 2024**, utility **Thames Water Finance 4.625% 2026** and investment bank **Goldman Sachs 1.875% Senior 2030**. Even though interest rates and prevailing yields are rising, we think inflation should peak and begin to fall next year. If we're right, these bonds should offer decent real returns (after adjusting for inflation) over three years or so.

We bought US-listed pharmaceutical, veterinary medicine and vaccine manufacturer **Merck**. Its sales have grown steadily over many years and it sports exceptionally high gross profit margins (gross profit is revenue less the costs of production). The business should also be less susceptible to rising costs from inflation.

Another purchase was mobile phone and media giant **Apple**. We have long admired this business, which is the gold standard in user experience, cash flow and recurring revenues with high, defensible profit margins. However, for a very long time its valuation was a bit rich to jump in. During the last few months Apple's multiple fell significantly, giving us the ability to purchase it for what we considered a more reasonable price.

As stock markets rose in early August, we added another **UBS Put Spread** structured product, which protected us as markets dropped (we are exposed to any fall greater than 25%). These options are effectively an insurance policy on our US stock portfolio. We pay an upfront premium in return for the right to 'sell' a given value of the S&P 500 Index at a pre-agreed level.

We sold the **iShares China CNY Bond ETF** in August. This tracker holds a range of government-issued and government-backed Chinese bonds. We have held it for some time as Chinese yields were significantly higher than similar bonds in the West, providing a more attractive risk-off asset. During the recent market falls, these yields actually held up relatively well, so we sold this position to recycle the cash into Western markets now that their yields have increased to more attractive levels.

We reduced the **Invesco LGIM Commodity Composite ETF**. We also trimmed some of our equities as well, including ecommerce giant **Amazon**, electric car-parts supplier **Aptiv**, American beauty store chain **Ulta Beauty** and oil services business **Schlumberger**.

Spotlight

In this quarter, the spotlight is on our **Gaming Basket** and **CME**.



Gaming Basket

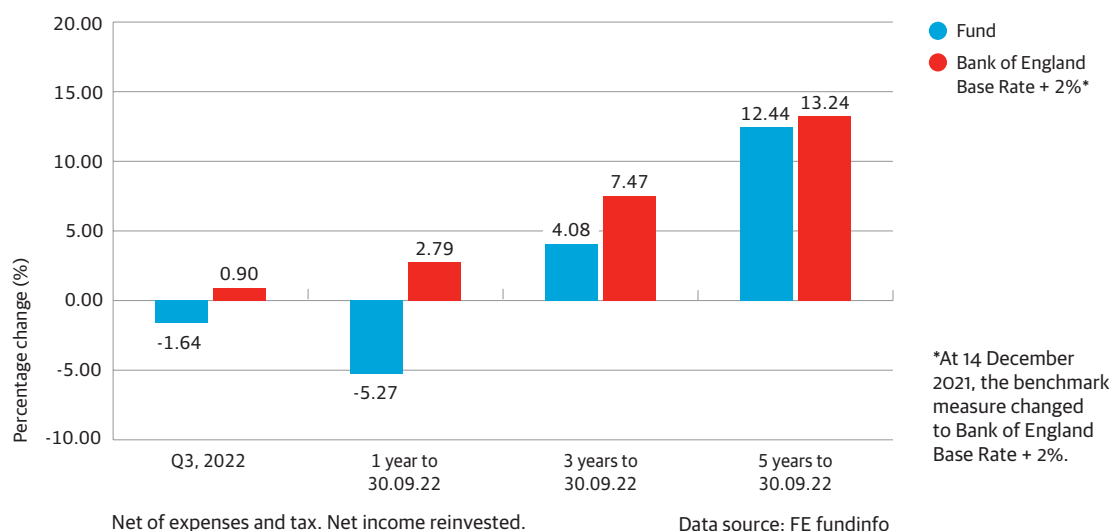
- The gaming market is large and is growing quickly – it is estimated there are already over 2 billion gamers across the globe and the revenues are already many times greater than that of Hollywood
- Move to downloading and streaming games has meant the market can be larger and more profitable as the need for physical discs and places to sell them reduces – 5G could also increase the addressable market with better game streaming on the move
- The average age of a gamer in the US is 35 years old – these are people with jobs and money to spend rather than the stereotypes
- A lot of focus is now on in-game purchases for the latest 'skin' or celebratory dance for your character – the cost of this can be fairly low, perhaps only a few dollars a month, and in tougher times we'd expect that spend to be stickier than something like visits to the cinema where hours of entertainment vs cost is skewed heavily in favour of gaming
- We own four stocks in a basket to provide adequate diversification and to address the higher volatility you can see in these names – they tend to fluctuate a great deal around their latest game release
- In our gaming basket we own, Electronic Arts (FIFA football game franchise), Activision Blizzard (Call of Duty games), Take-Two Interactive (Grand Theft Auto games), and Nvidia (key producer of the graphics processing units – GPUs – used in gaming hardware)

CME

- CME is a global markets company with the largest financial derivatives exchange in the world – includes Chicago Mercantile Exchange, Chicago Board of Trade, New York Mercantile Exchange, and The Commodity Exchange
- Its product suite includes a range of markets, including futures and options on rates, foreign exchange, equities, energy, and metals
- They have been able to step in and take advantage of the void left after banks left certain areas of the derivatives market after regulation meant capital requirements became too onerous – many banks are actually now becoming their customers and regulation is generally a positive for CME
- The business has been restructured and is now able to have a greater focus on customer demand driving the offering
- CME does not take capital risk as they only match buyers and sellers and with most of their revenue growth coming from trading and clearing
- It can be counter cyclical as volatility is their friend – higher volatility, outside a 2008 type scenario, typically means more trading



Fund performance



Discrete annual performance					
Year to:	End Sep 2018	End Sep 2019	End Sep 2020	End Sep 2021	End Sep 2022
Fund	+1.96%	+5.95%	+1.62%	+8.12%	-5.27%
Bank of England Base Rate + 2%	+2.52%	+2.78%	+2.40%	+2.10%	+2.79%

Our benchmarks are calculated on the rate of change of the CPI index, over different time periods (e.g. if we were calculating year to date figures in January 2021, we would look at the percentage change from December 2020 to the end of January 2021). So we take CPI to the current value, and add on 3%, prorated over a year (roughly 0.25% per month). If the CPI Index benchmark were to fall, more than the amount pro-rata, the benchmark year-to-date will be negative, even though inflation as reported by the media (calculated specifically as a 12M rate of change), remains positive.

The performance shown is for our 0.5% (L-class) annual management charge share class. Some of our existing clients may be invested in a more expensive share class, the performance for which will therefore be lower. Factsheets for all share classes showing our charges and respective performance are available on request, free of charge or on our website rathbonefunds.com.

Past performance does not predict future returns. For further information on risks and costs, please read the Prospectus and Key Investor Information Documents (KIIDs), available for free at rathbonefunds.com. 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.

The investment objective of the sub-fund changed on 25 March 2019 due to the sub-fund ceasing to be part of a master feeder arrangement. Therefore, performance in the chart shown prior to this date was achieved under differing circumstances.

Top performers (%)			Bottom performers (%)		
Holding	Performance	Contribution	Holding	Performance	Contribution
Charles Schwab	+24.13	+0.10	Vodafone	-20.08	-0.09
Ashtead	+20.40	+0.06	Adobe	-17.94	-0.09
Cadence Design Systems	+18.65	+0.10	National Grid	-17.86	-0.09
Dexcom	+17.47	+0.09	Verizon Communications	-17.60	-0.09
Société Générale US Rates Volatility Trend Note	+16.34	+0.33	Macquarie	-16.55	-0.12

Note: Top and bottom performers are taken from the list of all holdings of 0.25% and above of the portfolio. Performance and contribution data shown above is based on unhedged GBP capital returns. Performance (table above only): Gross of charges.

Source: Rathbones

Fund performance (continued)

In the third quarter of 2022, we've continued to see a broader risk-off sentiment and a fair amount of volatility in both equity and bond markets. This comes as investors are becoming increasingly worried of the risk of a US Federal Reserve policy error leading to a recession, particularly following their recent hawkish rhetoric, and also remain unconvinced of the UK government's fiscal plans after the mini budget. Given this environment, many of our assets within the Diversifiers component of the portfolio were the most helpful at providing protection and returns during the quarter. The two **US rates volatility notes** again benefitted from additional volatility in rates as investors grapple with conflicting data prints coming out of the US and struggle to project where interest rates may go over the next year. Our three **S&P put spreads** were also all in the money at quarter-end and contributed positively to performance.

Given the risk-off sentiment generally, it is unsurprising that equities overall were the largest drag on performance. Names such as **Vodafone** and **Kion** struggling the most. Kion has been suffering much of the year as it has been caught in somewhat of a perfect storm of having continued supply chain issues hampering their numbers, material increases to costs of energy and materials, and a general souring on sentiment for European industrial companies. In September, the company dampened its outlook for the year further given these continued issues, which led to another material leg down for the stock. It's been a painful and disappointing year so far for Kion and its shareholders, but we continue to believe the longer-term structural story of driving technology-led efficiencies in warehouses, distributions centres, and fulfilment centres, particularly with automation being a key aspect of change, remains intact and Kion still stands to be a key beneficiary of these developments.

Asset allocation ranges

Liquidity	Equity-type risk	Diversifiers
10% to 50%	20% to 60%	0% to 50%

Asset allocation change and strategy

We increased our holdings of overseas conventional government bonds from 13% to 17% and completely sold our 6% position in inflation-linked government bonds.

Asset allocation split	30.06.22	30.09.22	% Change		12 month change	
Liquid assets	28.29%	32.66%	4.37%	▲	-9.49%	▼
Equity-type risk	45.70%	43.17%	-2.53%	▼	3.44%	▲
Diversifiers	26.01%	24.17%	-1.84%	▼	6.05%	▲
	100.00%	100.00%				
Asset class split	30.06.22	30.09.22	% Change		12 month change	
Equities	34.64%	31.63%	-3.01%	▼	-1.06%	▼
Index-linked bonds	6.46%	0.00%	-6.46%	▼	-7.18%	▼
Conventional government bonds	20.83%	28.70%	7.87%	▲	3.59%	▲
Corporate bonds	14.34%	14.44%	0.10%	▲	1.77%	▲
Emerging market debt	0.00%	0.00%	0.00%	◀▶	-0.52%	▼
Private equity	0.42%	0.43%	0.01%	▲	-0.04%	▼
Alternative investment strategies	9.06%	10.57%	1.51%	▲	4.22%	▲
Property	0.00%	0.00%	0.00%	◀▶	0.00%	◀▶
Commodities	8.98%	7.63%	-1.35%	▼	2.07%	▲
Cash	5.27%	6.60%	1.33%	▲	-2.85%	▼
	100.00%	100.00%				

The fund is actively managed.

For more information on our liquidity, equity-type risk and diversifiers (LED) risk framework, please consult our investor brochure.

The investment objective of the sub-fund changed on 25 March 2019 due to the sub-fund ceasing to be part of a master feeder arrangement. Therefore, asset allocation shown prior to this date was prevalent under differing circumstances.

Investment outlook

Investors' hopes that the US Federal Reserve (Fed) would be cutting rates by early next year always seemed fanciful to us. So, when they pushed stock markets higher in August, we took the opportunity to trim some of our winners and increase cash. Now that investors have decided the Fed really isn't for turning, prices of stocks and bonds have dropped significantly lower. Broadly, that makes us buyers at current levels.

There are still lots of risks out there and we think a global recession is almost a foregone conclusion (if it's not already here). The question is how deep will that downturn be? At the moment, it seems likely to be mild, with shallow GDP contraction for two or three quarters. Then, if inflation falls back toward central banks' target levels, it will give policymakers more flexibility to help drive the economy forward once again. The risk is that inflation simply doesn't quit, that it gets baked into the collective psyche and central bankers must continue hiking rates to the point that it leads to a deeper and harsher recession. We are keeping extremely vigilant for this scenario, even though we think it's not the most likely outcome right now.



Rathbone Unit Trust Management Limited
8 Finsbury Circus, London EC2M 7AZ

International information line
+44 (0)20 7399 0800
international@rathbones.com
rathbonefunds.com

Investment manager:
Rathbone Unit Trust Management Limited
Authorised and regulated by the Financial
Conduct Authority
A member of the Investment Association
A member of the Rathbones Group.
Registered No. 02376568

Management company:
FundRock Management Company S.A.
Authorised in Luxembourg and regulated
by the Commission de Surveillance du
Secteur Financier

Rathbones
Look forward

Please note that the Rathbone Luxembourg SICAV may decide to terminate the agreements made for the marketing of the fund pursuant to Article 93a of Directive 2009/65/EC. For a summary of investor rights and guidelines regarding an individual or collective action for litigation on a financial product at European Union level and in the respective country of residence of the investor, please refer to the following link: rathbonefunds.com. The summary is available in English or an authorised language in the investor's country of residence.

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.

Please refer to the Prospectus of the UCITS and the KIID before making any final investment decisions.

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 your original investment.