Rathbone Greenbank Dynamic Growth Portfolio

Quarterly investment update, July to end September 2022

Rathbones
Look forward

Professional Adviser PA AWARDS 2022
WINNER
Best Multi-Asset Fund: Risk Managed

Professional Adviser PA AWARDS 2022
WINNER
Multi-Asset Group of the Year

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, crystalising 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
Idexx Laboratories (new purchase)	Vestas Wind Systems (sale)
New South Wales Treasury 2.5% 2032 (addition)	Advanced Drainage Systems (trim)
Ball Corp (addition)	Alfen (trim)
Deere (addition)	
AIA (addition)	

Source: Rathbones

As bond yields flew higher around the world, we added to our holdings of the Australian dollar-denominated **New South Wales Treasury 2.5% 2032** and US dollar-denominated **Asian Development Bank 1.5% Senior 2031**. We have locked in the currency exchange for both positions, so we will not lose out if sterling recovers nor benefit if sterling weakens further. We also bought a small amount of **UK Treasury 4.25% 2032** bonds, predominantly 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.

We bought **Idexx Laboratories**, a US-based veterinary diagnostic and software business that also branches into testing and monitoring of water and milk. Idexx also covers livestock and horses. The company has grown its sales steadily in double-digits for the past five years and profits by even more. We think this momentum should continue, especially as farmers must become more efficient and improve the yield from their animals while reducing environmental effects. Meanwhile, vets are in heavy demand after the significant uplift in pet ownership following the pandemic and its loosening of flexible work. Idexx seems well placed to make the most of both of these trends.

We received consumer health business **Haleon** as a spin-off from **GSK** (formerly GlaxoSmithKline) during the quarter. We bought more of it once it started trading on the stock exchange as well. Haleon owns many strong consumer health brands, including Sensodyne toothpaste and pain relief medicines Panadol, Voltaren and Advil. We believe there's a great opportunity for global growth, and unlike mainstream consumer goods, the pills business is less sensitive to commodities, too, which should reduce any pressure on profit margins if inflation stays high.

As stock markets rose in 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 added generally to equities on weakness, including recyclable aluminium can producer **Ball Corp**, tractor maker **Deere** and pan-Asian insurer **AIA**. We took profits from wastewater pipe manufacturer **Advanced Drainage Systems** and smart grid and energy storage business **Alfen**.

Finally, we sold Danish wind turbine manufacturer **Vestas Wind Systems** because we felt there were better places to invest, given the increased competition in the wind power industry and higher costs of materials, labour and transport.

Spotlight

In this quarter, the spotlight is on our **Linde** and **Jack Henry & Associates** holdings.

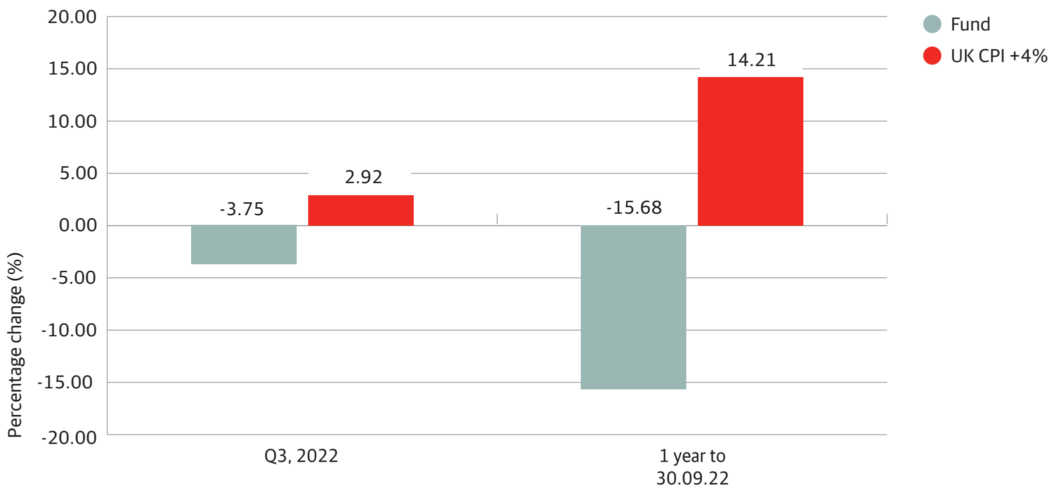
Linde

- Linde is the largest industrial gases company in world, providing industrial gases and engineering services for customers in multiple sectors, including healthcare, food and beverage, and electronics
- It provides innovative services, such as a CO_2-based solution for paper mills which helps to improve pulp washing efficiency and an ultra-high purity oxygen to keep a room 'clean' for electronics manufacturing, which are vital to its customer' operations
- The end markets Linde provides to are either very robust or have large fixed-fee components, such as a rental on gas cylinders, which are needed in order to be able to restart manufacturing quickly – this provides Linde's own business model with resilience
- Its products, services and technologies offer environmental benefits to a wide variety of industries, for example, supplying oxygen to steelmakers helps them lower energy consumption, supplying oxygen to medical patients helps provide respiratory assistance and its hydrogen helps produce cleaner air by reducing sulphur emissions from trucks and cars
- Globally, a lot of focus is on how hydrogen could help in decarbonising numerous sectors and Linde are playing a very promising, active role in the hydrogen market along the entire value chain from generation and liquefaction to solutions for transport and storage – it also took a minority stake in ITM Power last year which reinforces a strategic move into green hydrogen

Jack Henry & Associates

- Jack Henry is the leading American provider of technology solutions and payment processing services to financial services, primarily community and regional US institutional banks
- Its services are designed to help these small-medium sized financial institutions begin their journey into digital and operate more efficiently (through automation and streamlining), overcome revenue challenges (by optimising financial management) and reduce risk and fraud (by securing information and networks)
- Jack Henry has a great economic moat around its business – its superior technology offering and high spend on research and development has helped it to maintain competitive advantage and take market share and it has highly recurring revenues from customers with the majority of contracts at around seven years
- Dedicated to promoting financial inclusion, for example, in 2020 it established a partnership with the American Bankers Association (ABA) to create 'Bank On-certified accounts' which serve the unbanked and underbanked population with modern banking services, such as debit or prepaid cards and bill pay – all at a low cost and without overdraft fees
- Its diversity, equity and inclusion framework is designed to help achieve increased representation or underrepresented group at all levels, fostering an even more inclusive workforce by, for example, leadership development and mentoring opportunities, using empowering and equitable language in the workplace, and introducing a 'floating holiday' which allows employees the choice to use the day however they prefer – such as a religious or cultural holiday with meaning to them

Fund performance



Performance (based on 'S-class' shares). Net of expenses and tax. Net income reinvested.

Data source: FE fundinfo

Discrete annual performance					
Year to:	**End Sep 2018**	**End Sep 2019**	**End Sep 2020**	**End Sep 2021**	**End Sep 2022**
Fund	–	–	–	–	-15.68%
UK CPI +4%	+6.71%	+5.84%	+4.21%	+7.35%	+14.21%

Price performance based upon single price (mid). 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.

Top performers (%)		
Holding	**Performance**	**Contribution**
UBS 10121 S&P Put Warrant	+112.00	+0.15
Advanced Drainage Systems	+49.90	+0.43
Badger Meter	+24.55	+0.18
Deere	+21.15	+0.12
DBS	+19.97	+0.17

Bottom performers (%)		
Holding	**Performance**	**Contribution**
GN Store Nord	-44.72	-0.52
GSK	-25.79	-0.36
Ball Corp	-23.00	-0.36
Vodafone	-20.04	-0.24
Adobe	-17.67	-0.23

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.

Source: Rathbones

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. Aside from these, industrial and healthcare names such as **Advanced Drainage Systems**, **Badger Meter**, **Deere** and **Roche** have held up well in this economic backdrop. Advanced Drainage Systems has seen solid growth over the past three months across its construction end markets, with management decisions on pricing helping to offset its raw material costs.

Fund performance (continued)

Given the risk-off sentiment generally, it is unsurprising that equities overall were the largest drag on performance. UK equities were the largest detractor and names such as **GSK** and **Vodafone** struggled the most. GSK suffered after they were named defendants in a federal litigation in the US related to their marketing of the heartburn medicine Zantac which was withdrawn from market in the US and other countries in 2020 due to contamination. The first lawsuit against the company has been dropped which helped ease shares and we do remain confident in its investment case longer term. US provider of innovative, sustainable aluminium packaging **Ball Corp** also saw weakness following disappointing second quarter results due to significantly weaker demand vs expectations and cost-push inflation. However, despite this short-term volatility, we continue to like Ball Corp as a defensive name which we believe still has strong tailwinds behind it in the sustainable packaging space.

Asset allocation ranges

Liquidity	Equity-type risk	Diversifiers
0% to 30%	50% to 90%	0% to 30%

Asset allocation change and strategy

During the quarter we increased our overseas high-quality credit exposure.

Asset allocation split	30.06.22	30.09.22	% Change	12 month change
Liquid assets	18.06%	17.90%	-0.16%	1.71%
Equity-type risk	76.44%	74.87%	-1.57%	-2.95%
Diversifiers	5.50%	7.23%	1.73%	1.24%
	100.00%	100.00%		

Asset class split	30.06.22	30.09.22	% Change	12 month change
Equities	71.22%	70.30%	-0.92%	-3.67%
Index-linked bonds	1.15%	1.42%	0.27%	0.18%
Conventional government bonds	5.37%	4.95%	-0.42%	0.15%
Corporate bonds	9.93%	10.30%	0.37%	6.45%
Emerging market debt	0.00%	0.00%	0.00%	0.00%
Private equity	0.00%	0.00%	0.00%	0.00%
Alternative investment strategies	5.50%	6.57%	1.07%	0.58%
Property	0.00%	0.00%	0.00%	0.00%
Commodities	0.00%	0.00%	0.00%	0.00%
Cash	6.83%	6.46%	-0.37%	-3.69%
	100.00%	100.00%		

Asset allocation (continued)

Sustainable category split	30.06.22	30.09.22	% Change		12 month change	
Decent work	14.40%	12.86%	-1.54%	▼	-1.00%	▼
Resource efficiency	9.09%	9.57%	0.48%	▲	-1.19%	▼
Habitats and ecosystems	0.00%	0.00%	0.00%	◀▶	0.00%	◀▶
Inclusive economies	2.20%	4.61%	2.41%	▲	3.31%	▲
Energy and climate	17.98%	19.11%	1.13%	▲	3.02%	▲
Health and wellbeing	15.12%	15.74%	0.62%	▲	-0.17%	▼
Resilient institutions	5.57%	5.14%	-0.43%	▼	-0.90%	▼
Innovation and infrastructure	23.31%	19.94%	-3.37%	▼	0.04%	▲
Diversifiers	5.50%	6.57%	1.07%	▲	0.58%	▲
Cash	6.83%	6.46%	-0.37%	▼	-3.69%	▼
	100.00%	100.00%				

The 'resilient institutions' category includes government bonds.

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.

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Rathbones
Look forward

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.

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