

Rathbone Heritage Fund

Update, Q1 2019 update

Over the first quarter your fund was up 8.5%, while the FTSE World (GBP) rose 9.6% and the benchmark of CPI+5% returned 1.1%. The fund's maximum drawdown during the quarter was -2.3%, compared with -2.8% for the FTSE World.

The quarter saw a rebound following the turbulence of the final months of 2018. Interest rate expectations in the US changed markedly, with the prospect of rate rises in the coming year virtually gone, and fears about global growth becoming less pronounced. Also, company results in the first few months were broadly in line with expectations, which helped calm markets. In the UK, Brexit dominated the news, as usual, and while it's an important issue, it must be kept in context: the majority of our UK-listed holdings are in fact globally focused businesses. Only **Big Yellow** and **PRS REIT** are solely exposed to the UK.

Performance of your fund in the quarter was broad based. The top contributor was **Ulta Beauty**, which delivered strong results due to the successful execution of its strategy. Also at the top of the pack were **Micro Focus** and **Aptiv**. Following the problems surrounding Micro Focus's integration of the HPE division that came to light at the beginning of 2018, management have been working through them and appear to have turned a corner. Aptiv was hit last year by fears that demand for passenger cars was about to slump, but these worries have lessened of late.

Speculation about a potential bid for Italian financial business **Cerved** drove shares higher; we sold half our holding once the ticker neared the rumoured acquisition price. The deal fell apart soon after it became public, sending the shares tumbling back, but they remain above the pre-bid price. The company has shown itself open to interest from potential acquirers and more offers could arrive in due course.

The worst contributor to our quarterly performance was the final impact of the fraudulent accounting at **Patisserie Holdings**, discussed last quarter.

The only other negative contributions were minor, and came from Covetrus and Kinopolis, two holdings which we have exited this quarter.

We received shares in Covetrus as a spin-off from US healthcare distributor **Henry Schein**. In February, Henry Schein hived off its pet care distribution divisions, which then merged with veterinary software business Vets First Choice, to create the new business Covetrus. These shares were volatile and didn't perform well after going it alone. Although spin-offs can provide opportunities as investors sell sub-scale holdings and analyst coverage can be low, in this case we weighed these factors against the integration risks and debt levels. We met management soon after the spin-off occurred and were unable to get satisfactory answers so sold the company.

We also exited our holding in Kinopolis. The acquisition of Canadian cinema group Landmark Cinemas has changed the business. The strategy of buying small cinema chains in regions Kinopolis knew well and improving returns by running them the Kinopolis way is somewhat different to buying a large chain operating in leased sites in a well-developed, distant market with a dominant competitor. The expectations reflected in the price were greater than what we felt Kinopolis could achieve, so we sold our holding.

These were the only positions exited and we didn't add any new holdings during the month.

Looking ahead, despite the improvement in sentiment around the globe we remain cautious about the future. As well as monitoring what is currently in your fund and searching for new ideas, we are also spending time looking at businesses that could offer us opportunities in the future, so that we are ready to take advantage when they appear.

The Rathbone Heritage Fund team

The Rathbone Heritage fund team's views are their own and not to be taken as investment advice.

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