

Rathbone Multi-Asset Enhanced Growth 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

On the first day of the month, we sold the **Provident Financial 6% 2021** bond that we bought in August after the payday lender warned on its profits, revealed it was being investigated by the FCA and told investors that its chief executive has resigned. Back then, the yield on this bond spiked as investors panicked; however, we thought the company had enough cash to cover the repayment of this debt when it came due in 2021. We bought this bond at 70p and sold it for 98p, banking a tidy profit. Subsequently, the FCA has announced another FCA probe, this time into its car financing arm.

We added to our holdings of **TravelSky** after the share price dipped during the month. Investors periodically get nervous about China, but we think the economy will be one of the main drivers of global growth over the next few decades. We are very happy to buy into the monopoly ticketing provider for Chinese air travellers – a group that is growing rapidly each day.

We added to Scandinavian lender **Danske Bank** and Swedish locksmith and entranceway security firm **Assa Abloy**, after slight weakness in the shares.

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.

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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