Rathbone Unit Trust Management
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Rathbones
Look forward

Rathbone SICAV Income Fund

Update November 2019

Back in 2000, the privatised utilities were a dull and sleepy crew, unexciting in contrast to the fireworks on offer at the height of the TMT (technology, media, and telecommunications) bubble.

Across the electricity, gas and water industries, these business promised income investors cash returns on defensive, regulated assets, and very healthy dividend yields, a veritable smorgasbord of delights that nevertheless failed to excite in those heady days. In the intervening decades, their fortunes have waxed and waned. When the tech bubble burst, income shareholders enjoyed some halcyon days, as round upon round of takeovers generated great capital gains and substantial outperformance. Latterly, utilities have been targets for both regulators and politicians; the last decade has been far more challenging.

Carl Stick will celebrate his twentieth anniversary running the Rathbone Income Fund on 1 January. Interestingly, just one stock has been ever-present in our fund over that period: **SSE**, formerly Scottish & Southern Energy. Unitholders have benefited from the highs of an outstanding share price performance in the noughties (a total return of 273% versus the FTSE All-Share Index's paltry 19%). The last decade has been more pedestrian, but still in line with the market, as the company has faced two major headwinds. Firstly, it has been almost impossible to invest in new thermal electricity generation (coal, gas and biomass) without clear line of sight into the regulatory and political environments. Secondly, the retail function of providing utility services to the public has been mired in pricing controversy and competition.

But we sense the tide is turning – it certainly has for the shares (up 31% this year versus the FTSE All-Share Index's 15% increase through to the end of November). The retail business will be sold in the 2020. The last coal-fired power stations will be turned off in March and, while the company still operates new clean-gas-powered generation facilities, it is evolving into the leader in renewable generation. Indeed, SSE's intention is to treble annual output of renewable electricity to 30 Terawatt hours (TWh) by investing in a combination of offshore and onshore wind assets. To put this into context, its current traditional thermal generation is 20TWh a year. Established principally north of the border, these windfarms will sit nicely alongside SSE's crown jewels, Scottish electricity and gas networks.

The point is, this is a business, and an industry, that is going through rapid change. There remain some big hurdles to overcome this December, not least the election; a Labour majority honouring a pledge to re-nationalise would be an existential threat. More predictably, regulatory headwinds will persist through the next pricing review, with the catchy name RIIO T2, which concludes in 2021. However, SSE exudes a far greater sense of purpose. Renewable energy generation has always been central to our investment case, and the nation's aspirations for a greener future need investment on the scale that SSE is planning. From stock market darling to the shadows of political and regulatory duress, we wonder whether SSE may be finally re-emerging into the light.

Recent trading: Happy with our positioning ahead of the election we made just one trade this month – a small addition to **Micro Focus International**.

Companies seen in November: SSE, **Halfords**, **DCC**, **Big Yellow Group**, **UDG Healthcare**, **Great Portland Estates**, **Halma,** and **Altria**.

Carl Stick
Fund Manager

Alan Dobbie
Fund Manager

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A member of the Rathbone Group.
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