Rathbone Unit Trust Management

Contact us 020 7399 0399 rutm@rathbones.com

Rathbone UK Opportunities Fund

Quarterly update June 2021

In the second quarter, your fund returned 8.0% versus an average 5.6% increase in the IA All Companies sector.

	3 months	6 months	1 year	3 years	5 years
Rathbone UK Opportunities Fund	8.0%	10.7%	36.9%	18.6%	63.5%
IA All Companies Sector	5.6%	11.8%	27.7%	11.1%	48.5%
FTSE All-Share Index	5.6%	11.1%	21.5%	6.3%	36.9%

	30 Jun 20-30 Jun 21	30 Jun 19-30 Jun 20	30 Jun 18-30 Jun 19	30 Jun 17-30 Jun 18	30 Jun 16-30 Jun 17
Rathbone UK Opportunities Fund	36.9%	-4.8%	-9.0%	11.6%	23.5%
IA All Companies Sector	27.7%	-11.0%	-2.2%	9.1%	22.5%
FTSE All-Share Index	21.5%	-13.0%	0.6%	9.0%	18.1%

Source: FE Analytics; data to 30 June, I-class, mid price to mid price.

These figures refer to past performance, which isn't a reliable indicator of future performance.

Slowly, but surely...

Another quarter comes to a close and we inch ever closer to 'normalisation'. Compared with the aggressive rotation towards cyclical stocks in the first quarter, there was a more gentle reassessment and appreciation of 'quality' in Q2. Worries over surging inflation have potentially peaked; central banks are on the lookout for longer-term price pressures, but aren't ready to raise rates yet. Having topped up a few high-quality names that had been caught in the crossfire earlier in the year, our more recent performance has been strong.

Once again, technology or tech-enabled businesses have soared. Tech hardware business **discoverIE** is racing ahead thanks to its solid growth and exposure to tidal wave trends like renewable energy. The value of European tech venture capitalist **Draper Esprit** has almost tripled since this time last year and it is about to move on from AIM to the FTSE 250. We are impressed by the value that Draper has recently realised from its investments (by selling some of its stakes), and it's raised yet more cash for investing in further early-stage high-growth tech companies. We're even more enthused by other gems remaining in Draper's portfolio, such as fashion search platform Lyst, AI chipmaker Graphcore, and used car platform Cazoo which is likely to list in the US this year. discoverIE and Draper Esprit are two of the largest holdings in our fund so they're making chunky contributions to your performance.

Another name fast making headway is sustainable wood manufacturer **Accsys Technologies**, which we discussed in our May note. Despite announcing a near-term delay to its new plant in Hull, the stock price is moving up thanks to the huge long-term opportunity for this 'green' product. All its available capacity is sold out, yet management is resisting the urge to ramp up prices in order to maintain long-term relationships and reduce earnings volatility. This is just the sort of quality management that we like to back.

Less positively, the rise of the Delta variant has dampened enthusiasm for 'reopening' stocks. The FTSE 250 tends to bear the brunt of such anxieties. Businesses like travel food caterer **SSP** and retailer **WH Smith** have been soft as investors reassessed the risk of more prolonged restrictions. However, we have been topping up WH Smith, for example, during this period — analysis shows that while COVID-19 cases are rising rapidly in the UK, hospitalisations are not, as vaccines appear to afford effective protection against serious illness. So, the economy will continue to reopen and consumers will continue to spend more. WH Smith is no longer a high street stationery store, but a travel retailer with a large presence in the US thanks to its recent acquisitions. Flight activity in the US is already much higher than in Europe, giving the business an early fillip. Additionally, WH Smith has taken over space from Boots in major London airports thanks to the strength of its offering, which is now wider than ever.

Stock fundamentals reassert their importance

Looking at the quarter more broadly, it seems that style rotation took more of a backseat to fundamentals than has been the case for a while. Our best performers, like online magazine company **Future**, discoverIE and **Dechra Pharmaceuticals**, all posted really strong results and are benefitting from long-term structural drivers. Dechra is trading exceptionally well through a sweet spot created by the surge in pet ownership thanks to more flexible working.

Perhaps unsurprisingly, the price of fuel cell technology firm **Ceres Power** fell back after its phenomenal 2020. It's a volatile stock with a lot of retail participation in a hot sector, so we have been managing our position size down. But we like the work it's doing around 'reversing' its fuel cell technology to create an electrolyser. This is a big differentiator in the market and adds another leg for the company.

Large-caps actually fared well over the quarter so our underweight position here was a drag, but this was more than made up for by strong performances from our biggest positions and our AIM holdings.

We sold our remaining stake in robotic process automation company **Blue Prism**. We had such high hopes for this business — the market for installing software to automate repetitive tasks is huge and growing fast. But we are increasingly worried that Blue Prism doesn't have the right go-to-market strategy to capture this growth. We retain some exposure to the space through Draper Esprit, mentioned above, which has a nice stake in UI Path, a peer of Blue Prism that listed on the NASDAQ in April.

Finally, M&A deals have continued to flood UK indices — year-to-date M&A levels are running at 2.6 times their pre-COVID rate. With corporate confidence high and rising but valuations still at record discounts (versus US stocks), we expect this interest to continue over the summer and to provide welcome support for the UK market as a whole.

Alexandra Jackson
Fund Manager

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Rathbone Unit Trust Management Limited
8 Finsbury Circus, London EC2M 7AZ
Tel 020 7399 0000

Information line
020 7399 0399
rutm@rathbones.com
rathbonefunds.com

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