Rathbone Unit Trust Management

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Rathbones
Look forward

Rathbone UK Opportunities Fund

Quarterly update December 2022

Few investors will be sorry to see the back of 2022. This manager certainly isn't: it proved an enormously frustrating year in which the vast majority of our portfolio holdings delivered strong operational performance, but investment performance was abysmal.

	3 months	6 months	1 year	3 years	5 years
Rathbone UK Opportunities Fund	13.3%	1.1%	-29.4%	-8.5%	-7.7%
IA UK All Companies Sector	9.7%	4.2%	-9.1%	0.2%	8.8%
FTSE All-Share Index	8.9%	5.1%	0.3%	7.1%	15.5%

	30 Dec 21- 30 Dec 22	30 Dec 20- 30 Dec 21	30 Dec 19- 30 Dec 20	30 Dec 18- 30 Dec 19	30 Dec 17- 30 Dec 18
Rathbone UK Opportunities Fund	-29.4%	21.4%	6.8%	25.1%	-19.4%
IA UK All Companies Sector	-9.1%	17.3%	-6.0%	22.2%	-11.2%
FTSE All-Share Index	0.3%	18.3%	-9.8%	19.2%	-9.5%

Source: FE Analytics; data to 31 Dec, I-class, mid price to mid price.

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

The bleak backdrop has dominated...

Macro considerations took hold, with stock-picking little more than a distraction from the dot plots that forecast central banks' interest rate decisions. Valuations were too high to accommodate the pace and level of tightening inflicted by central banks trying to contain the inflation genie. On top of which, our asset class, UK mid-caps, suffered mightily from the ignominy of the Truss/Kwarteng experiment because of their sensitivity to the outlook for the UK economy (via sterling and interest rates, which both went in the wrong direction). It was a year when stock-picking didn't mean analysing fundamentals, but assessing how share prices would react to central bank rhetoric.

It feels crass to offer up optimism for UK midcaps after the year just endured and the poor performance of your fund. And perhaps equally incongruous to note that we've made few changes to the portfolio despite the tumult in the wider world. Our portfolio activity has once again centred on upweighting quality — the process we tend to go through each time there's market dislocation. In October, for example, we found that UK assets had sold off so indiscriminately that we could buy the highest quality (return on capital) businesses for similar multiples to the weakest.

Our long-term strategy, to own the very best stocks we can afford, is starting to pay off. In the final quarter of 2022, your fund bounced strongly, and by more than our peers. Unfortunately, this wasn't enough to negate losses from earlier in the year, so we believe there's plenty of 'bounce' still left in the tank.

The value of investments and the income from them may go down as well as up and you may not get back what you originally invested.

Are things turning around?

So what's changed in the last three months? Again, it's all in the macro. Several items on our 'wish list' for improved returns have been ticked off, including:

- Inflation prints are topping out, which should allow central banks to slow rate hikes, giving them more chance to achieve the mythical 'soft landing' that risk assets would enjoy
- So far, recent economic data has actually been slightly better than expected. Germany for example, and the UK, have both reported reasonable GDP numbers
- We've avoided energy rationing after the cut-off in Russian gas supplies. Gas prices are now below where they were before Russia invaded Ukraine, halving since mid-December. This is a great boon for consumers and sentiment
- The dollar has weakened aggressively in the last few months as the US Federal Reserve is unlikely to remain the most hawkish central bank out there
- And China is now reopening.

We are seeing a reversal in many of the macro trends that hurt equities, particularly UK equities, so much in 2022. And now the UK is one of the few developed markets where valuations are pricing in a recession. When earnings are being downgraded, which they will be over the course of the next three months, this valuation cushion is critical.

In our previous note, we stated that finding areas where interest rate-related bad news is priced in will be key for 2023. Early trading sessions are, so far, corroborating the idea that pockets of UK assets fit this criterion; some retailers, for example **JD Sports**, are reporting decent trading, and the stocks have gone up a chunk. More interestingly, some of the housebuilders (another great bellwether sector) have been issuing nasty looking outlooks, and these stocks have bounced too. If you're looking for a signal, we might have just found it.

With best wishes to all our clients for a peaceful and prosperous 2023.

Alexandra Jackson
Fund Manager

Any views and opinions are those of the investment manager, and coverage of any assets held must be taken in context of the constitution of the fund and in no way reflect an investment recommendation. 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 what you originally invested.

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