

# Rathbone SICAV Multi-Asset Strategic Growth Portfolio

## Monthly update July 2021

One of the fun, bizarre features of our age is that the freewheeling capitalist global economy is reliant on a communist nation for much of its goods, and a punchy chunk of its GDP growth too.

Of course, China is far from Karl Marx's ideal. Workers aren't allowed to join a union (except the one that is in hock to the ruling Chinese Communist Party); the top flight of that ruling party has become fabulously wealthy somehow; and markets and free enterprise have been allowed to flourish under the hammer and sickle as long as people bow to the state whenever asked. You could argue this simply makes it authoritarian not communist. Because no matter which way you look at China, you see hustle, bustle, massive growth, innovation and huge consumption. In other words, you see a vibrant capitalist society. And yet...

### Hammer time

Communism tends to have little bearing on what China gets up to during business hours. It's like some weird wallpaper in the boardroom – it prompts a comment or two but doesn't influence the discussion. Still, it pays for investors to keep it in mind! It may be wallpaper, but the guy who owns the place liked it enough to hang it. China was restored to greatness by communist leadership using capitalist tools to become wealthy. And that's the rub: China's government uses capitalism, it isn't capitalist at heart.

Recently, the Chinese leadership have been concerned that some of its more swashbuckling technology companies have been getting a little too big for their boots – that they were no longer listening carefully enough to the state's subtle hints about what was acceptable. Similarly, the authorities haven't been happy with how private tutors have fuelled the arms race of education, which has in turn become a burden on Chinese families. **This came to a head last month.** Chinese leaders don't need to put their solutions to a public vote; they can do it overnight. So they made some bruising changes to the technology market and effectively outlawed for-profit tutoring, both of which sent Chinese markets tumbling (along with a few domestic stocks that were listed in the US through convoluted ownership structures). This then spread to American firms that sell educational services to China as well.

Instantly the debate roared to life: is this the end of the road for Chinese capitalism? We think that's unlikely. China's leaders know

that markets are pivotal to Chinese prosperity. We think they are trying to fix some problems that aren't exactly unique: data security, spiralling education costs and rising inequality. They just have a habit of bringing a hammer to the problem. We are sticking with China, but we will be extremely careful about any exposure that could be seen to aggravate inequality or that plays fast and loose with Chinese data. The risk of greater intervention has increased dramatically in these areas, we believe.

### Inflation's sharp sting

Another risk that we're keeping our eye on is inflation. Central banks are adamant that the current spike in inflation is 'transitory', and the market is apt to believe them. We too think the price spikes will die down in time, but we think that it may take a year or two for that to happen. If the market's idea of 'transitory' is four to six months, there could be a few wobbles as they come to terms with that misunderstanding. We had a chat about this in [episode one of our The Sharpe End podcast](#).

In recent months quite a few consumer staple giants warned that the cost of goods sold – raw materials, energy, packaging and transportation – had ballooned recently. They are considering price increases to offset some of this, but that tends to lag the cost inflation by a year or so. One day, we'll all be scratching our heads and wondering if our shampoo bottle isn't a little bit smaller than it used to be. In the meantime, the share price of many staples businesses have lurched lower.

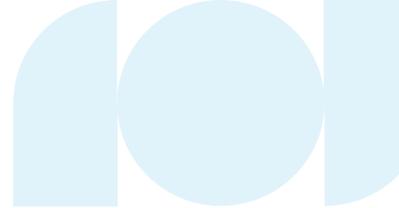
We continued to build our position in German electronics company **Siemens**. The conglomerate is focused on digital services and automation for power grids, transport networks, factories and other commercial buildings. It also has an impressive healthcare division focusing on scans, diagnostics, cancer treatments and state-of-the-art machines for operating theatres.

Meanwhile, we added to computer chip producer **Taiwan Semiconductor Manufacturing Company** and e-commerce giant Amazon, which was weak this month. We took profits from US PDF and creative industries software developer **Adobe** and from American diabetes monitoring business **Dexcom**. Both companies' share prices have soared so far this year, so we felt it was prudent to trim our investments and recycle the cash into other holdings.

We sold the **iShares MSCI Far East Ex-Japan ETF** and used the cash to add to stocks we hold directly, particularly in the West. As the pandemic has progressed, the developed world appears to be in the better position for recovery, given the vaccine rollouts. It seems like it will be a very long time before the East will manage to catch up in this regard.

Finally, we took profits from payments network **Visa**, locks and entryway supplier **Assa Abloy** and business consultant **Accenture**.





### Out of the comfort zone

As summer winds down without ever getting going, inflation remains the hot topic both here in the UK and abroad. Its path and people's reaction to it will have fundamental effects on borrowing costs, monetary policy, spending habits and businesses' bottom lines.

Inflation is extraordinarily complicated, yet it is often victim to anecdotal and emotive arguments. People paying £6 for a pint grumble about lies, damned lies and statistics. Others feel the burn of paying to get on a train again or the cost of post-pandemic airfares. Yet inflation is when the *general level* of prices is increasing, not when one or two things become very expensive. Many people forget about the generally low price of electronics, home appliances and food. In particular, the increase in quality relative to price is often not adequately accounted for by punters. The most obvious example of this is mobile phones: they are roughly the same price as 25 years ago (adjusted for inflation), but now incorporate all the tasks of a camera, GPS unit, games console, scanner, personal organiser, gardening almanac and more besides. That's a lot of stuff that people no longer need to buy. Technological progress often has this hidden deflationary effect in the background.

This longer-term phenomenon, along with the large productive capacity that exists around the world – in factories' possible output, underutilised labour and piles of savings – persuades us that inflation shouldn't stay hot for years and years. But people live in the short term, and right now inflation has hit 2.5% in the UK for the first time in three years. In the US it's 5.4%, the highest level since 2008. There could be still higher numbers in coming months as supply chains continue to untangle themselves.

In a meeting with Generac, an American manufacturer of power generators, we were told that the cost of a shipping container to get something from China to San Francisco had shot up to \$20,000 from roughly \$3,000 a year ago. Ships, containers and orders have been knocked completely out of sync by quarantined ports, interrupted output from factories and sporadic orders from shuttered retailers. This sort of thing will crimp some companies' profits and no doubt frighten investors, causing gyrations in bond yields that will reverberate through stock markets. Expect 'growth' companies to shoot higher at the expense of 'value' stocks, only for them to reverse a couple of weeks later. These rotations will probably zigzag like that for the rest of the year, until some feeling of normality is reached.

If markets do go on as we expect, it will be an uncomfortable time for investors. Yet all that volatility would offer opportunities as well. It sounds hackneyed, but it's true. With a greater spread of possible prices, it gives you more options to adjust your portfolio, to buy into companies at a lower price and take profits on your investments at attractive heights.



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