Ravenscroft

Quarterly Newsletter Q1 2021

COMMENTARY

Time keeps on slippin'...

by MARK BOUSFIELD

I turn 50 this month, which, to be honest, isn't something I have really thought about much (at least, not meaningfully). As I write, however, it has become the cause for some reflection. The short version: how did that happen? Why can my 11 and 12-year old sons now run faster than me? All allied to a variety of similar woe-is-me age-related angst! Of course, whilst my life has flashed past in a matter of heartbeats, the reality is that half a century has elapsed in our ever-changing and evolving world. Generally for the better, I would argue. I certainly believe, looking to the future and to the motivation of younger generations (I can say that now...wow!) that the future is bright: ever improving healthcare, the adoption of technology and an increasing focus on environmental issues and solutions all bode well.

There are, as there always have been, problems – those moments that require calm and patient navigation. The current pandemic would be a classic case in point. A major healthcare crisis today, but most likely a bump in the road when viewed with a much longer-term perspective. A major deal, certainly, in terms of the current economic strategy of global governments, but with epochal impact or merely another blip in the chart?

Either way, in investing terms, we believe that the future of our themes remain both vibrant and clear. They have been at the core of our portfolios for more than a decade and will, I imagine, remain there for years to come; they are as close to incontrovertible as we can get.

In the shorter term, however, there are adjustments to be made. The irrefutable nature of technology, healthcare, global consumerism and growth of the emerging consumer has allowed us to maintain a low-turnover portfolio while it does the talking. The flip-side is that many of our themes, whilst attractive investments for the long term, are looking increasingly expensive. This has only been exacerbated through lockdown. Technology, healthcare and staple goods have all been net beneficiaries of the crisis.

> "Time keeps on slippin', slippin', slippin',
> Into the future
> Time keeps on slippin', slippin', slippin',
> Into the future."
>
> ***Fly Like an Eagle*** - *Steve Miller Band (1976)*

Over the last few months there has been a swing in the leadership of markets as investors focus on the post-pandemic environment. Stocks and sectors that have suffered over the last couple of years now offer value – not only on a relative basis (when compared with tech and healthcare), but in real terms. For example, energy stocks and oil have performed strongly this year. Who remembers oil trading negatively in April last year? Extraordinary!

What does this mean for our investment strategy? In simple terms (as ever) it means that we need to remain aware of the world we live in and adjust accordingly. Some touches of the tiller are highlighted in the individual strategy pieces that follow.

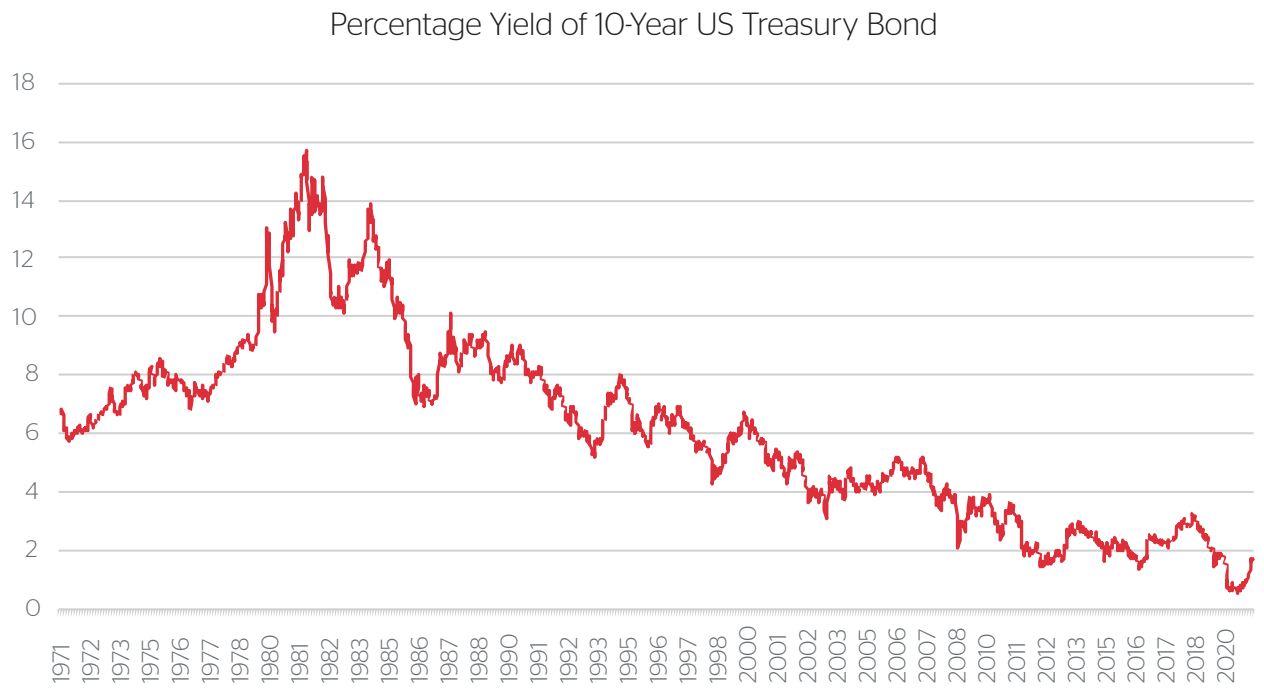
Longer term? Our investment themes endure – and will be the foundation of our portfolios for many years to come. As I turn 50, I am excited about the prospects ahead and as to what the next 50 will bring. Meanwhile, here's to more of those healthcare innovations!

CAUTIOUS PORTFOLIOS:
LOWER RISK
by ROBERT TANNAHILL

Objective: The Cautious portfolio's objective is to increase its value by predominantly allocating capital to fixed-income investments. The portfolio can also invest into global blue-chip equities with strong cash-flows and progressive dividend policies. A neutral position would be a 75% bond/25% equity split and the maximum equity-weighting of approximately 35%. The cash generated can be re-invested to provide capital growth or taken as an income stream.

The first quarter of 2021 has been a tough period for bond markets. With the Democrats eventually winning marginal control of the US Senate, following the Georgia run-off elections in early January, and the vaccine program in the US picking-up pace, markets have increasingly been focusing on the prospect of a stronger US (and so global) recovery backed by significant levels of government spending (aka fiscal stimulus). This drove the interest rate ("yield") on the 10-year US government bond up from 0.9% at the year-end to 1.7% [1] at the end of the quarter. As bond prices move in the opposite direction to their yields – and most bond markets are impacted by moves in the US Treasury bond – this caused widespread drops in bond prices across the world. Thankfully, bonds are far from a single market that moves in perfect sync and this created both winners and losers depending on how investors were positioned. To put these differences in context, the US government issued a long-dated (30-year) bond last May. Investors who put $100 into that bond at the end of May are today sitting on a loss of roughly 24% with the bond priced at just over $75 [2]. While long-dated bonds are always more volatile than shorter-dated ones, this equity-like level of loss on an asset that has spent the last 40 years going up has been a painful wake-up call to any investors who were sleepy holders of long-dated government bonds. The other end of the bond spectrum would be short-dated bonds with higher levels of credit risk. The Schroder Strategic Credit Fund that we own is up more than 10% over the same period [3]. The size of this gap illustrates just how unusual a period the last year or so has been for bond markets.

So, are we near the end of this move? While we would love to have the answer, nobody truly knows where markets will go over the short term. What we can do, however, is put the recent move and the current level of bond yields in perspective. If we look back at the history (the last 50 years) of US Treasury bond yields, we have seen them rise and fall in a series of 110 peaks and troughs. Of these cyclical moves from low to high (or vice versa) 95 are smaller than 2% in size [4]. Of the other fifteen, ten occurred in a cluster during the early 1980's when Paul Volcker, as chairman of the Federal Reserve, was trying to wrestle rampant inflation back under control. So while we would not be surprised to see the recent run continue (with, perhaps, the 10-year Treasury bond rising into the low 2% area) it would be an historic outlier to see yields move materially higher in the short term. This also chimes with what our bond managers have been saying. Speaking to one of the most notable bond managers in the world, recently, the view was that a 10-year yield above 1.5% would look attractive. Clearly, we are well past this now.



Source: U.S. Department of the Treasury.
The change in 10-year US Government Bond Yield 1971 to 2020.
Collated: 10/04/2021.

PORTFOLIOS

We have been thinking about the risk of rising bond yields for a number of years now. While we don't think that income-focused investors can avoid bonds, we do think that these risks can be managed. We are therefore relatively pleased that the Cautious strategy has defended your money well over this period, ending the quarter down 0.1% (including both changes in capital value and income) [5].

Such thinking has underlain a number of our core positions as well as more recent changes in this strategy. We have long argued that cautious investors should run a suitably sized allocation to equity. This is because while equity adds capital volatility to a portfolio in the short term, there are times when bond investors will be very happy to have some exposure; this quarter proved a classic example. Over the period, global corporate bonds fell some 3.4% [6]. On the other hand, all of our equity funds posted positive returns. The star performer, Fidelity Global Dividend (aided by some currency hedging) rose 6.8% [7]. Nevertheless, on average, our bond allocation beat global bonds over the quarter – although there were winners and losers within the portfolio.

The only material laggard was Stratton Street's NFA Global Bond Fund, which fell some 4.8% [8] due to focus on longer-dated US dollar denominated bonds. While this was painful, the Fund has an unusual long-term approach and we remain very confident in its ability to deliver. This is illustrated by returns of 15.6% [9] over the last three years even after inclusion of the recent sell-off.

We have taken steps to mitigate risks within our core bond allocation. One example is the replacement of our UK government bonds ("gilts") with US Treasury inflation-protected securities ("TIPS"). While these bonds do fall with government bond markets, we are pleased to see them acting relatively defensively this year: falling 1.9% versus gilts' more than 7% (depending upon which bond you look at) [10].

The biggest change to the bond allocation in the portfolio in recent years has been the expansion of the short-dated "credit" allocation that we have been building up for some time and today sits at just over 20% of the portfolio. This consists of three funds all managed by careful stock pickers who lend money for shorter periods (generally around three years) to businesses with a medium level of credit risk. We like this space because the higher yields and lower exposure to moves in government bond yields (lower duration) offer a relatively defensive income source that is well insulated from a rate-rising environment. That played out this quarter with these funds posting positive returns ranging from 0.2% to 1.4% [11].

Looking forward, we firmly believe that there remain sensible ways to generate an income stream – even if we do enter a period of structurally rising long-term interest rates. While there are parts of the market that look risky today, there are also areas that offer sensible returns for patient investors building diversified portfolios. We continue to think long and hard about how the world may be changing in the aftermath of the pandemic. As I write, we are adding a new infrastructure allocation to the portfolio in the form of the KBI Global Sustainable Infrastructure Fund. This provides both more thematic exposure (environmental solutions theme) to the strategy and helps defend the portfolio from inflation concerns; Shannon covers this in more detail in her Fund in Focus section. Next on the block is to look for any areas of value that might make suitable additions to the portfolio should the nascent global recovery become self-sustaining.

As always, we are very grateful for your continued support. We trust that you are pleased with our service; but, should you need anything further, please feel free to get in touch.

12 MONTHS ROLLING PERFORMANCE

	31/03/2021 - 31/03/2020	31/03/2020 - 31/03/2019	31/03/2019 - 31/03/2018	31/03/2018 - 31/03/2017	31/03/2017 - 31/03/2016	Annualised Since Inception 31.12.11
Cautious Portfolio	12.1%	-1.7%	4.0%	-0.3%	9.1%	5.2%

Data is based on sterling based model portfolios net of a 0.75% per annual management fee. The models are run in real-time in line with our equivalent client portfolios and provide a fair representation of actual performance achieved by clients in our opinion. The models are maintained internally and are not subject to external auditing. It is important to note that past performance is not a reliable indicator of future results. Source data: Ravenscroft Investment Management Limited and FE fundinfo; collated 05/01/2021.

BALANCED PORTFOLIOS: MEDIUM RISK

BY GEORGIE FLETCHER

Objective: The Balanced portfolio's objective is to provide capital appreciation through a balance of fixed income and global equities. A neutral position is a 50% bond/50% equity split and the maximum equity weighting is 60%. The cash generated can be re-invested to provide capital or taken as an income stream.

In the last commentary, we spoke about the strategy's best performer, Lazard Global Equity Franchise, a newly-introduced position in the second half of last year. Growth and value stocks behave differently under certain market conditions and navigating this oscillation is the crux of portfolio construction. Lazard (being a value-biased portfolio) was purchased to provide diversification to an otherwise growth-focused global equity allocation – and, as investors' appetites for value over growth materialised, the introduction worked extremely well.

This quarter saw the rotation into value continue. We have, over time, been reducing our exposures to growth holdings within the global equity space (Fundsmith and Lindsell Train) and are happy with these funds at their current weighting. Fidelity Global Dividend, being somewhat growth orientated (i.e. not a pure value play) and the strategy's largest holding (at 6.5%), we reduced the position by 2.5% and rotated the proceeds into Lazard (now 7.5%) to create more of a balance between value and growth.

We avoid knee-jerk decisions and themes dominate our portfolio construction. Nevertheless, we try hard to stay attuned to the evolving environment around us. During lockdown, our investment themes (which steer our asset allocation towards the consumer staples, technology and healthcare sectors) have understandably been popular and experienced considerable outperformance as a result. Whilst this has been extremely fortuitous for the strategy, we are very aware of the premiums these sectors are now attracting when compared to the broader market and have continued taking steps to balance the portfolio in terms of valuation.

Which brings us to the UK. Gradually emerging from BREXIT uncertainty, high-quality domestic-facing UK companies are trading at very reasonable valuations. A weaker pound adds to this attraction for foreign investors and the Covid-19 vaccine is being rolled out at pace. All this makes for an attractive investment position.

In light of this, we made the decision to build a position in a UK-focused fund, Polar Capital UK Value Opportunities. The Fund is exceptionally well-managed and has all the qualities we look for when investing in managers using a fundamental, bottom-up stock selection process. The managers predominantly invest in the small-to-mid-cap space across over fifteen sectors. Following a series of meetings, we initiated a position in February.

Since its introduction into the strategy, now at 5%, Polar UK Value has returned 6.5% [12] versus Fundsmith Global Equity at 0.9% [13] and Lindsell Train at -2.7% [14]. This divergence serves both to emphasise the market's increasing appetite for the UK and to highlight the performance differential we sometimes see between growth-focused and value-focused funds (and the benefit of owning a diversified equity allocation).

Touching on the currency story and our themes, fuelled by prospects of a strong domestic recovery, the US dollar saw highs not seen since 2016 and experienced its best quarter since 2018; sterling was, however, stronger, which caused pain for the strategy's unhedged thematic positions (denominated in US dollars).

The increase in sentiment, coupled with higher future growth prospects, extended government spending and the likelihood of interest rates rising, has increased the risk of inflation materialising throughout the second half of the year. Markets are already pricing in these concerns, which was reflected in the narrowing of credit spreads in mid-February, as investors sought returns from higher-risk, fixed-income assets. This yield play was the catalyst for weakness seen in emerging markets (which were behaving well up until this point). We also saw the more expensive growth assets fall, including the likes of the Arisaig Global Emerging Consumer Fund and, golden child, Polar Capital Global Technology. This said, RLAM Short Duration Global High Yield showed their mettle this quarter, posting 0.7% [15]. Considering these variables, across the quarter, the Balanced strategy posted -2.2% [16].

The start of 2021 has seen increased volatility, reflecting the uncertain sentiment of investors and direction of markets. Large-scale reopening of both the UK and US economies looks set to materialise in the latter half of the year, fuelling the gradual return to normality (albeit post-pandemic "new normal"). Currencies, commodities, bonds and equities have all seen the impact of inflationary fears and there is no denying that it has been a tough start to the year for markets. As ever, we remain vigilant with plenty of liquidity to respond, where appropriate.

12 MONTHS ROLLING PERFORMANCE

	31/03/2021 - 31/03/2020	31/03/2020 - 31/03/2019	31/03/2019 - 31/03/2018	31/03/2018 - 31/03/2017	31/03/2017 - 31/03/2016	Annualised Since Inception 31.12.11
Balanced Portfolio	16.2%	-3.4%	7.4%	3.3%	16.5%	8.8%

Data is based on sterling based model portfolios net of a 0.75% per annual management fee. The models are run in real-time in line with our equivalent client portfolios and provide a fair representation of actual performance achieved by clients in our opinion. The models are maintained internally and are not subject to external auditing. It is important to note that past performance is not a reliable indicator of future results. Source data: Ravenscroft Investment Management Limited and FE fundinfo; collated 05/01/2021.

GROWTH PORTFOLIOS: HIGHER RISK

by SAMANTHA DOVEY

Objective: The Growth Portfolio's objective is to provide long-term capital appreciation by investing predominantly into global equities. A neutral position is a 25% bond/75% equity split and the maximum equity weighting is approximately 85%.

We do not want to spend too much time reliving the rollercoaster year of 2020, but, in terms of market action, the first quarter of this year was completely different to Q1 2020. Unfortunately, some things have not changed – many of us are still working from home, our colleagues in the UK approaching their 12-month anniversary.

Thinking back a year, equity markets began rolling over on 22 February, bonds followed on 6 March and markets bottomed on 23 March. Then central banks stepped in, providing both fiscal and monetary stimulus like we had never seen before; and the rest, as they say, is history. 2020 ended in positive territory, which was somewhat surprising given the world was still in the throes of a global pandemic.

The main difference when comparing Q1 2021 versus 2020, is the wobble the fixed-income market experienced (as opposed to the equity market hiccough we saw last year). If we look specifically at the US Treasury market, using the 10-year US Treasury as an example, we saw yields move from 0.9% at the beginning of the year to 1.7% by the end of March [17].

Bond yields and prices are "inversely correlated", when yields rise, prices fall. The yield increase caused a price fall across the first quarter of this year. In the case of the US 10-year, this was somewhere in the region of 5%. A key variable investors must remain mindful of with bonds is duration: the longer you agree to lend money, the more sensitive you are to interest-rate movement.

I suppose this begs the question, why did bond yields rise so steeply?

Firstly, bonds have been on a bull-run since 1980. What we mean by this is that yields have fallen, so (based on the inverse relationship) prices have risen. By the middle of 2020, yields reached a low of about 0.6% [18] (that is, you were paid 0.6% a year for lending money to the US Government for 10 years). There are many reasons as to why we ended up there, which include low interest rates as well lots of "money" flowing round the system, to name but two. A rebound off these lows was thus not unreasonable. In the context of the 40-year downward movement, the rate at which the yields "bounced" was a bit of surprise!

Yields rebounded hard as markets became concerned about inflation; the US Federal Reserve (the FED), however, was not. It "held the line" on not increasing interest rates since it does not see inflation as an issue – and, ultimately, it would like to see inflation stay structurally above 2% for a period of time to achieve an average of 2%. We have had many an internal discussion about inflation (is it coming or not?) and, if so, is it transitory or structural?

The fixed-income allocation in the Growth strategy is quite small at approximately 20%. It is predominantly allocated to what we refer to as "credit selection" fund managers (i.e. not taking "bets" on interest rates or duration, as highlighted above). Instead, we prefer our bond managers to look at underlying companies and assess whether they can repay their debt; as a result, the companies they select tend to have a shorter duration profile. The best fund to use as an example of this is Schroder Strategic Credit, which has a 5% allocation within the strategy.

Schroder is managed by Peter Harvey and has been under his control since inception in 2007. The Fund Manager selects credit based on fundamental analysis in the investment-grade and high-yield sector of the bond market; it has a duration of 2.5 years and pays a yield of 3.5%-5% [19].

Taking the 10-year US Treasury, as an example, where you were agreeing to lend money for 10 years at 0.6% last year (this year at 1.7%); with Schroder you are lending money for 2.5 years at 4.4%. We've concluded that for a growth investor who can withstand the relatively higher level of volatility associated with high-yield credit, this looks like the more attractive investment case.

This has been reflected in returns so far this year: the 10-year Treasury is down -5.4% [20] in GBP terms whilst Schroder is up 1.5% [21]. Similarly, the Growth strategy returned -1.6% [22] for the quarter.

Turning to investment trades, in March of this year, the strategy introduced two new positions into the portfolio: US Treasury TIPS (hedged back to GBP) at 3% and Polar UK Value Opportunities at 4%. TIPS were purchased as a risk-off asset (as well as to provide protection should inflation turn out to be structural) and Polar UK Value Opportunities for a combination of reasons including attractive valuations within the region – which Georgie has covered in the Balanced commentary, should you want more colour!

12 MONTHS ROLLING PERFORMANCE

	31/03/2021 - 31/03/2020	31/03/2020 - 31/03/2019	31/03/2019 - 31/03/2018	31/03/2018 - 31/03/2017	31/03/2017 - 31/03/2016	Annualised Since Inception 31.12.11
Growth Portfolio	26.0%	-7.7%	7.7%	3.3%	20.1%	9.9%

Data is based on sterling based model portfolios net of a 0.75% per annual management fee. The models are run in real-time in line with our equivalent client portfolios and provide a fair representation of actual performance achieved by clients in our opinion. The models are maintained internally and are not subject to external auditing. It is important to note that past performance is not a reliable indicator of future results. Source data: Ravenscroft Investment Management Limited and FE fundinfo; collated 05/01/2021.

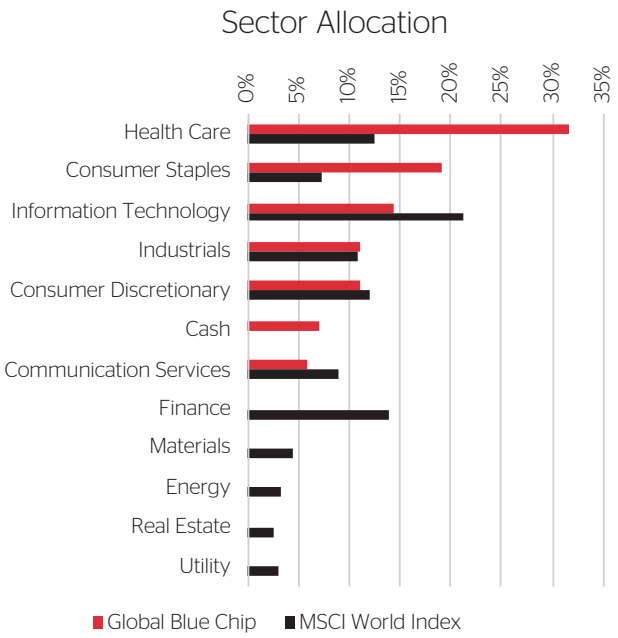
GLOBAL BLUE CHIP PORTFOLIOS: HIGHER RISK

by SAMUEL CORBET

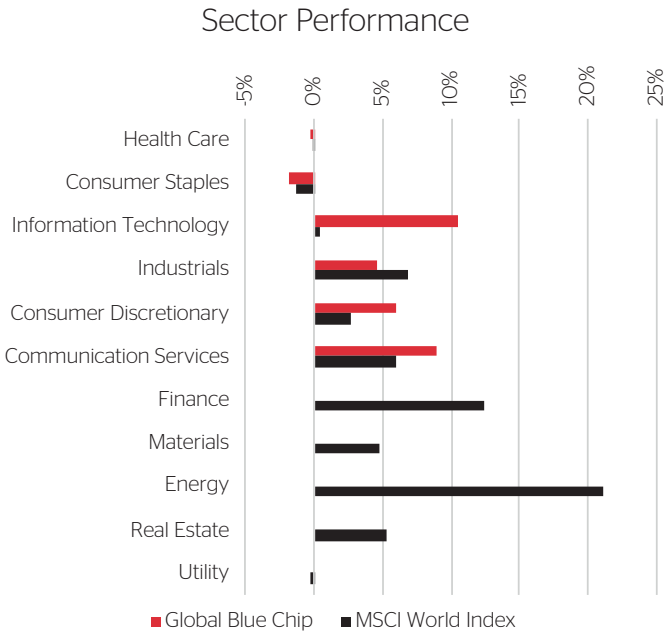
Objective: The Global Blue Chip portfolio invests into approximately 25-30 global blue chip companies, that are in line with our long-term investment themes. The aim is to invest into such companies at an attractive valuation and hold them for the long term. The cash generated can be reinvested to provide capital growth or taken as an income stream.

The Global Blue Chip strategy returned 2.2% [23] during the quarter. In comparison, the MSCI World Index produced a total return of 4.0% [24] fuelled by the strong performance of the energy and financials sectors (+20.7% [25] and +12.2% [26] respectively) as shown on the sector performance graph to the right. Investors will know these are areas of the market that the strategy does not own due to the capex-intensive nature of their business models and cyclical earnings.

By contrast, the information technology, health care and consumer staples sectors (which combined make up 65% of the strategy – 24% more than the index allocation) made up three of the four bottom performing sectors. Given the weighting of the strategy relative to the index (please see the allocation graph below), we were generally pleased with the overall performance of the businesses you own.



Charts above & top right: Ravenscroft Investment Management Limited & FactSet.
Collated: 10/04/2021.



Turning to the underlying businesses, Intel was both the best outright performer (+28.0%) [27] and highest contributor (+1.1%) [28] during the quarter. This comes hot-off-the-heels of a difficult 2020 where serious doubts surfaced concerning Intel's ability to maintain its technological advantage. The market took kindly to the appointment of Pat Gelsinger (former Intel engineer and most recently VM Ware CEO) as CEO and the share price was further bolstered by the recent announcement that the Company will spend $20 billion on construction of two new semiconductor factories in Arizona.

Alphabet (+17.0% [29], 0.5% [30]) had impressive quarterly results with revenues increasing 23.5% compared to the same period a year earlier. The Company also provided additional disclosures on its Google Cloud business for the first time; we welcome the added transparency.

The market welcomed BMW's (+15.9% [31], +0.5% [32]) "new" battery electric vehicle ("BEV") strategy following the announcement at its annual conference that at least 50% of BMW's global sales will be fully electric by 2030. We would argue that this was not a new revelation but rather a continuation of the Company's pre-existing strategy centred around a flexible approach that allows BMW's propulsion mix to be led by consumer demand.

3M (+10.6% [33], 0.4% [34]) announced good organic sales growth for its fiscal fourth quarter, driven by strong demand across a number of product categories. The Company warned that it had seen signs of inflation in three areas: raw materials and feed, logistics and labour. The Company is aiming to increase prices in order to pass any cost rises onto the end consumer.

During its recent earnings call, Oracle (+7.8% [35], +0.4% [36]) provided what was, in our view, a very bullish outlook. The Company has always maintained that it would not front-run demand by investing in increased capacity ahead of demand. As such, we viewed the announcement that they planned to double expenditure on capex next quarter (to $1 billon) as a clear indication of the demand (and associated cash flows) they are now anticipating. Conversely, the market was underwhelmed by the reported growth and the shares retraced from their recent highs following the announcement.

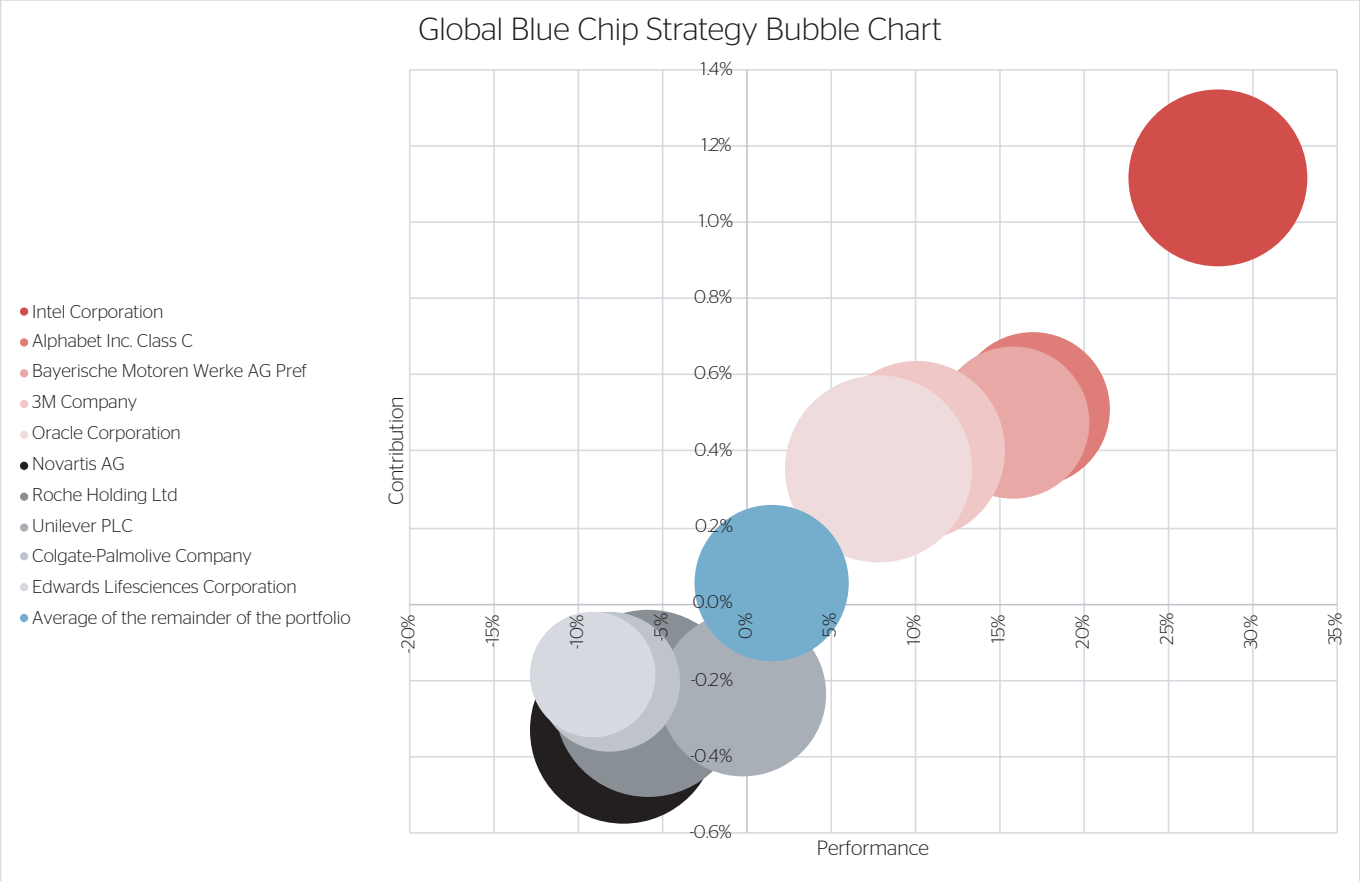
Looking now at the largest detractors.

Given the performance of the sectors, it will come as little surprise that three of the strategy's healthcare holdings were among the top detractors: Novartis (-7.3% [37], -0.3% [38]), Roche (-5.8% [39], -0.3% [40]) and Edwards Lifesciences (-9.2% [41], -0.2% [42]). On a valuation basis, our healthcare names offer compelling value and this is why we maintain our largest allocation to this sector. We are confident in the quality of the businesses and that this overweight allocation will serve our investors well over the long term.

Outside of healthcare (and similarly to 3M) Unilever (-6.8% [43], -0.2% [44]) saw commodity input costs rise which it intends to pass on via prices rise in the immediate term. Demand remained strong for its at-home cooking, hygiene and e-commerce categories, but margins were negatively impacted by lower demand for its beauty products with salons and stores remaining closed.

Colgate-Palmolive (-8.15% [45], -0.2% [46]) offered-up very strong 2020 earnings suggesting a return to high-single-digit organic growth due to its pivot towards higher-value, higher-margin product ranges. The Company is expected to show slower growth in 2021 as year-on-year comparisons get tougher and margins face pressure from commodity cost inflation. Staple stocks also came under pressure as investors rotated out of quality into value.

We made a number of changes to the strategy during the quarter. First, we exited the remainder of the strategy's allocation to Nestle on valuation grounds. We used the proceeds to top-up the BMW position, which looked compelling by all measures and had recently surpassed the self-imposed, 6-month trading moratorium we stipulate for newly-introduced holdings. We also added marginally to Colgate and Unilever, both of which had retraced from recent highs over input-inflation fears. Finally, we took the broader rotation out of the technology sector as an opportunity to add to the strategy's Microsoft allocation on a rare period of weakness, increasing the holding from a 2.5% to 3% position.



Source: Ravenscroft Investment Management Limited & FactSet.
Collated: 10/04/2021.

12 MONTHS ROLLING PERFORMANCE

	31/03/2021 - 31/03/2020	31/03/2020 - 31/03/2019	31/03/2019 - 31/03/2018	31/03/2018 - 31/03/2017	31/03/2017 - 31/03/2016	Annualised Since Inception 31.12.11
Global Blue Chip Portfolio	22.6%	3.1%	20.2%	-5.1%	28.5%	12.2%

Data is based on sterling based model portfolios net of a 0.75% per annual management fee. The models are run in real-time in line with our equivalent client portfolios and provide a fair representation of actual performance achieved by clients in our opinion. The models are maintained internally and are not subject to external auditing. It is important to note that past performance is not a reliable indicator of future results. Source data: Ravenscroft Investment Management Limited and FE fundinfo; collated 05/01/2021.

FUND IN FOCUS:
by SHANNON LANCASTER

This quarter we welcomed the first pure thematic exposure for the Cautious portfolio in the form of KBI Global Sustainable Infrastructure Fund. We have been on the hunt for a worthy companion to our three existing global equity income funds, both to gain exposure to the environmental solutions theme and to provide some diversification; KBI Global Sustainable Infrastructure ticks those boxes.

The KBI team has specialised in environmental portfolios for over twenty years. The managers recognise that trillions of dollars of sustainable infrastructure investment is required to ensure the delivery of clean, safe and high-quality water, energy, and food to the global population in the coming years – and that investors are often under-exposed to these sectors.

Their primary focus is on three core resources – water, food and clean energy – and the team runs a range of strategies in these areas. In 2017, after the investible listed-infrastructure universe grew, KBI took the opportunity to launch a fund. The team's stock inclusion criteria produces a universe of around 600 stocks from which they identify owners or operators of sustainable infrastructure assets or beneficiaries of investment in this area. From there, the team constructs a portfolio of around 45 stocks with three main characteristics:

- Lower correlation to global equities
- High and sustainable dividend yield
- Predicable cash-flow generation

It is clear from the portfolio that this is no ordinary 'traditional' infrastructure fund. For example, it owns Iberdrola, the leader in transition towards a sustainable energy model, through investments in renewable energy, smart grids, large-scale energy storage and digital transformation. It also owns smart infrastructure business, Costain Group, which focuses on meeting national needs across the UK's energy, water, transportation and defence markets. These sustainable infrastructure businesses, along with the rest of the portfolio, have a lower cost of capital than traditional projects: they carry less commodity-price risk, and their end-markets are tied to energy transition with a multi-decade runway on growth.

The portfolio is set to benefit from various tailwinds over the next few years, unlike traditional infrastructure. There are three main drivers supporting increased growth in sustainable infrastructure. First, significant demographic changes, such as population growth, emerging-market middle-class growth, and urbanization, will likely raise demand for infrastructure sharply over coming decades. Second, governments have moved climate-change objectives up their to-do lists and are set to launch various incentives schemes to support them. The policy response to climate change since the onset of the pandemic has been noteworthy: several countries have announced new net-zero carbon targets, while stimulus packages have incorporated climate protection measures. (The change in US administration in early 2021 will, in our view, herald the dawn of a new era in the US, one where the White House will prioritise more sustainable policies. President Biden is targeting a massive $2 trillion to be spent on clean energy infrastructure over the coming four years and has re-committed the US to the Paris Accord, originally signed in December 2015.) Third, the technological leaps we have witnessed over the past few years are accelerating the decarbonisation trend. That such technology shapes our lives is not a new story – it obviously remains a core theme in our funds – further advances in these areas will benefit decarbonisation efforts over the coming years.

These three growth drivers are combined with a promising investment outlook for this space. Government stimulus has included recovery plans with allocations for climate protection. The combination of stimulus with an ultra-low interest-rate environment could prove attractive for starting new infrastructure projects. Clean energy demand is rising while costs associated with renewable energy continue to decline.

As we would expect from a fund that invests in environmental solution-providers and integrates ESG analysis, KBI also supports achievement of the United Nation's Sustainable Development Goals. These are a collection of objectives designed to be a blueprint to achieve a more sustainable future. In addition, management engage directly with the underlying companies on key issues. In order to make the most impact, KBI focuses on 'laggards' in commitment to address climate change issues; those which do not publish adequate environmental information; or those companies where there are particular ESG-related concerns.

The KBI Global Infrastructure Fund is an exciting new addition and early signs show it already acting as a diversifier for our other global equity income funds. Given its long history as a specialist provider of these type of products, we consider that we are in good hands with KBI. We look forward to strengthening our relationship with the team in the coming year.

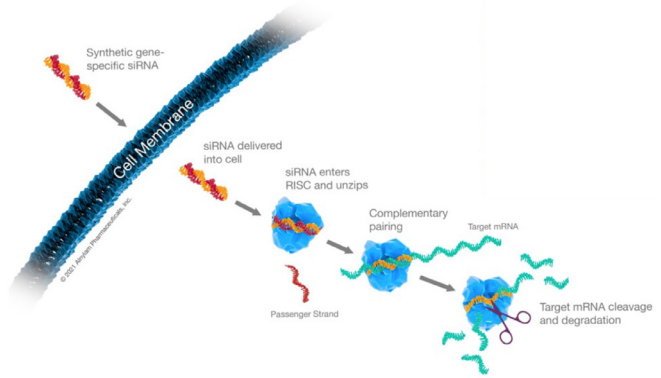
STOCK IN FOCUS:
by OLIVER TOSTEVIN

Towards the end of last year, we added shares in Alnylam Pharmaceuticals to the Global Blue Chip portfolio.

Alnylam is a biopharma business based in Cambridge, Massachusetts. We have grown familiar with the Company through our holdings in Regeneron, Sanofi and Novartis, each of which collaborates with Alnylam to access its technology. For us, Alnylam represents an exceptional investment – in the sense that the Company is yet to make a profit. You can be assured that we will not make a habit of this! But Alnylam is also a truly exceptional business that we view as having a very clear and de-risked path towards becoming a highly profitable blue chip over the coming years. We came to the conclusion that we'd rather own the shares today than wait to own them later when the situation has become more obvious.

Since its founding in 2002, Alnylam has pioneered an entirely new class of medicines called "small interfering RNA" or "siRNA". siRNA (not to be confused with the mRNA vaccine technologies of recent prominence) has numerous advantages over prevailing technologies in treating many diseases ranging from the rare to the ubiquitous. Alnylam has by far the strongest capabilities in this space.

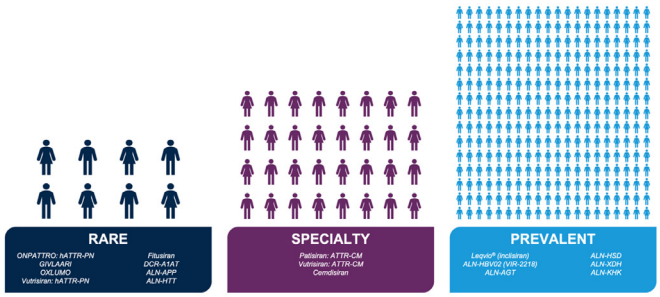
siRNAs work by harnessing a natural cellular process to interrupt the production of disease-causing proteins. Most drugs work by interacting with the proteins after they have already been produced. Alnylam likens the dynamic to fixing a leaky tap rather than settling for mopping the floor.



Source: Alnylam Pharmaceuticals. Collated: 29/03/21.

Treating diseases this way carries numerous important advantages over other approaches. In some cases, it allows Alnylam to "drug the undruggable". For example, Alnylam has invented effective treatments for acute hepatic porphyria and primary hyperoxaluria, two serious rare diseases that previously had no effective treatment options at all. Additionally, the natural RNA interference process helps the effect to endure for a long time, with dosing required as little as twice a year. Lastly, as RNA-based therapeutics, siRNAs are essentially written in the same "programming language" that our own cells use – this means they can be made to be extremely precise.

In the last two years, the Company has launched its first four medicines and still has the only siRNA drugs on the market. What has become increasingly clear during this period, is that the technology is highly effective, safe and repeatable across many diseases where there is unmet need. You can expect a wave of further launches in the years ahead and, in particular, an expansion from the Company's initial focus on rare diseases into much larger patient populations.



Source: Alnylam Pharmaceuticals. Collated: 29/03/21.

The main limitation at this stage is the absence of profits while the Company invests in ramping-up commercial operations, meaning that the Company has more ideas than it can sustainably fund through the development process. One exciting thing it has done to address this is to enter into a wide-ranging partnership with Regeneron to co-develop up to 30 different assets. We see this partnership as highly synergistic for a number of reasons, not least Regeneron's deep pockets and industry-leading capabilities in finding new genetically validated drug targets. As an example, the two companies have started testing an Alnylam-invented siRNA using a Regeneron-discovered target for the treatment of non-alcoholic steatohepatitis (NASH) – a prevalent liver disease that has proved a tough nut to crack so far. Another promising line of investigation is the combination of Alnylam's siRNAs with Regeneron's industry-leading antibodies, i.e. fixing the leaky tap and mopping-up at the same time. The companies are trialling this approach in paroxysmal nocturnal hemoglobinuria (PNH), a serious rare blood disease, where neither "fixing" nor "mopping" alone is entirely sufficient.

For us, 2020 marked a turning point because Alnylam secured complete funding all the way through to profitability with no more cause for dilutive equity raises – a critical catalyst for our decision to invest. We expect profits to follow within two to three years from now, and for the rate of revenue growth to continue to be very high.

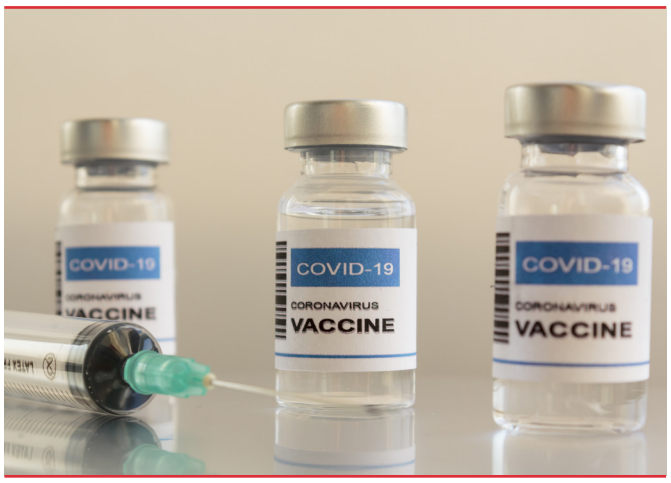
While the shares look expensive today, we see Alnylam as a "blue chip in waiting", or, in other words, a much bigger company than the share price implies. But we do expect the road ahead to be somewhat bumpy. Alnylam shares are likely to remain volatile for some time, which necessitates a long-term investment horizon. For this reason, our position size is currently modest, although we may well use the volatility to our advantage over time.

BOSCHER'S (BITE-SIZED) BIG PICTURE: NOT A GOOD TIME FOR POLICY ERROR

by KEVIN BOSCHER

Investors are becoming increasingly concerned about rising bond yields and the prospect of higher inflation. During the past few weeks, we have seen an increase in equity market volatility, a sell-off in some of the more expensive and "speculative" parts of the market (including Growth stocks), an increase in inflation expectations and 10-year bond yields rising rapidly to 1 year highs. These moves are largely the result of a good news event: the expectation that the global economy is recovering very strongly on the back of extremely expansionary fiscal and monetary policies, together with clear evidence that COVID vaccination programmes are working. There is also an expectation that strengthening economic activity will result in higher inflation and bond yields.

It's true that global reflation is in full swing. The US has agreed another huge $1.9tn fiscal stimulus package whilst Janet Yellen (US Treasury Secretary and former Fed Chair) is also talking about an additional $3-4tn investment programme over the next few years. Having the unique insight that comes from her academic background and time at the Fed, she clearly believes that now is absolutely the time to "go big" to ensure that the US economy not only recovers to its pre-pandemic path as quickly as possible, but also moves to a higher growth trajectory through increased productivity and maximum employment. Yellen also believes this is possible without worrying about the high and growing debt levels because "interest rates are at historic lows". There are two important assumptions to note here: first, that US fiscal spending will stay extremely strong; second, that interest rates and financing costs will stay very low. Other governments will seemingly pursue similar policies.



Fed Chair Powell is absolutely on board with this and has made it quite clear that the Fed will keep monetary policy as easy as possible until the US gets back to "full employment" and achieves its longer-term inflation target. For US inflation to hit the Fed's target, which is based on an average rate of 2% over the long term, US inflation could run as high as 4% for a few years without troubling the Fed too much. However, higher inflation could easily "spook" markets in the interim and, to some extent, recent market moves are reflective of the reality that we will see higher headline inflation rates over the next few months – mainly as a result of the base-effects of higher energy and food prices.

The key point for markets, however, is that core inflation remains subdued and that the cyclical and secular disinflationary forces remain powerful and dominant. Central banks, led by the Fed, will look through any transient rise in near-term inflation and will continue to keep short-term rates near zero for years to come, using all policy levers available to prevent longer-term rates rising much above current levels. This will be crucial to ensuring that the economic recovery gains traction, both to overcome the powerful deflationary pressures and to boost nominal growth in order to "inflate" away the debt problem.

In my view, we remain in a liquidity and economic recovery-driven bull market for equities. All components of growth are contributing to the reflation story: pent-up consumption, increased government spending, rising corporate investment and improving global trade. Stronger growth, a weaker Dollar, rising profit expectations and higher bond yields should ensure that the equity rotation into value, cyclicals, small cap and emerging markets continues for some time. Expensive growth stocks – mega-cap Tech, in particular – will struggle due to expensive valuations and because they are longer-duration assets that tend to underperform in periods of rising bond yields. Nonetheless, the long-term bullish arguments for these stocks remain intact and the most likely scenario is that they underperform in relative terms for a while, rather than suffer a period of absolute decline. In the meantime, any significant pull-back in these stocks will present an opportunity to add to preferred holdings.

On a more cautious note, however, I expect volatility in all asset classes to move (and stay) higher over the next few years. The global economy is undergoing a regime change from one where monetary policy has dominated to that of a Keynesian-style reflation, led instead by fiscal policy. The geopolitical landscape is also changing significantly as China challenges the US for hegemony and globalisation wanes in the face of populism. Volatility always rises at such inflection points and it is probable that the changing landscape will eventually result in significantly higher inflation and bond yields, although not for some considerable time. In addition, all of the necessary conditions for financial bubbles to thrive are in place and there are clear signs of speculation in some areas of the market. Hopefully, some of this "excess" can be worked off without any systemic event.

For the past decade, holding growth stocks and "buying on dips" has been the winning strategy for investors. A more flexible, active and balanced investment strategy will likely be needed for the rest of this decade. Accordingly, we have retained exposure to preferred long-term themes at the core of our portfolios but have increased weightings to some of the more cyclical and value sectors, in addition to some natural hedges against higher inflation, should this materialise. In this way, we are hoping to continue to deliver superior returns in both relative and absolute terms, whilst managing risk.

Data Sources

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19. Estimated short to long-term income yield for Schroder Strategic Credit 31/03/2021. Source: Schroder.
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21. Schroder Strategic Credit, GBP Total Return 31/12/2020 to 31/03/2021. Source: FE fundinfo.
22. GBP Ravenscroft Growth Model Performance Data, Total Return 31/12/2020 to 31/03/2021. Source: Ravenscroft Investment Management Limited.
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30. Alphabet (GOOG US Equity), GBP Performance Contribution 31/12/2020 to 31/03/2021. Source: FactSet.
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34. 3M (MMM US Equity), GBP Performance Contribution 31/12/2020 to 31/03/2021. Source: FactSet.
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36. Oracle (ORCL US Equity), GBP Performance Contribution 31/12/2020 to 31/03/2021. Source: FactSet.
37. Novartis (NOVN CH Equity), GBP Total Return 31/12/2020 to 31/03/2021. Source: FactSet.
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40. Roche (ROG CH Equity), GBP Performance Contribution 31/12/2020 to 31/03/2021. Source: FactSet.
41. Edwards Lifescienes (EW US Equity), GBP Total Return 31/12/2020 to 31/03/2021. Source: FactSet.
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44. Unilever (ULVR GB Equity), GBP Performance Contribution 31/12/2020 to 31/03/2021. Source: FactSet.
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All performance data above was collated on 08/04/2021.

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