J O Hambro
Capital Management Group

# CORE THOUGHTS

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## Q4 update

- The Fund's outperformance in Q3 was helped by our significant deployment of cash in Q1 and Q2 into what we believe are structurally well-placed businesses.
- The Fund is, we feel, well positioned against a political and economic background that seems likely to remain turbulent. We are currently focused on:(1) large cap companies with diverse cash flows; (2) companies with recurring revenues in structural growth markets; (3) companies able to invest and come out of the downturn stronger; and (4) companies that treat all stakeholders fairly, not just shareholders but their staff, suppliers and wider society.
- The Fund has a 'AA' MSCI ESG rating and sits in the top 1% of funds globally.
- We believe our absolute mentality and concentrated approach make the fund a potential core UK equity holding.

## JOHCM UK Opportunities Fund

### Fund positioning and company updates:

#### 1. Large cap companies with diverse cash flows

The Fund's exposure to large and structurally growing conglomerate businesses has been a key factor in the overall resilience of the portfolio this year. It remains an important defensive characteristic given the prospects of raised political risk and an uneven economic recovery ahead.

**Experian's** first quarter results were a perfect example of the benefits of diverse income streams. Its Consumer Services division (credit checking for mortgages, risk analysis and identity monitoring) saw revenue growth of +10% year-on-year in its largest businesses in the US, +104% in Brazil (helped by the introduction of positive data), but an -18% fall in the UK, where there has been both a reduction in demand for credit and supply from banks and other lenders (data that doesn't bode well for a rapid UK economic recovery).

Consumer product groups **Unilever** and **Reckitt Benckiser** have performed particularly well, with a shift back to in-home consumption and a permanent change in global attitudes towards hygiene. Whilst we can't be completely sheltered from randomised and populist-driven political events, a holding like Unilever, with more than 400 brands sold in 190 countries, should contribute to a smoother outcome for our end clients than a domestic company which relies upon the sale of one key product.

#### 2. Recurring revenue streams with structural growth

We have long prized companies with a high degree of stickiness in their revenue streams that are also positioned to benefit from growth in their end markets.

**Sage** delivered organic growth of 4% during Q2 2020, with some 88% of its revenues being recurring in nature. Its investment in cloud technology is paying off and growth is accelerating as the shift to working from home becomes more permanent and businesses need to invest in cloud-based technologies to facilitate more flexible and efficient operations.

**RELX's** largest division, Risk and Business Information, supplies data and analytics to almost all US personal insurance companies and 80% of federal agencies. This data is essential to the daily operations and the future growth of RELX's customers. In spite of the challenging economic backdrop in the first half of 2020, this division grew revenues by +3%.

#### 3. Ability to invest

Large companies who came into the crisis with strong market positions, healthy balance sheets and with a management willing to invest are in a position to emerge stronger.

There's no doubt that large companies are having a better crisis than smaller ones. This point was emphasised in **WPP's** interim results, which showed

its top 200 largest clients' revenues -8% year-on-year in Q2 2020. This compares to wider group revenues, which were -15%, driven down by the halting of smaller clients' advertising budgets. WPP used the lockdown period to improve its employees' digital skills, receiving more than 20,000 partner accreditations from Adobe, Amazon, Facebook, Google and Salesforce in the first six months of the year. This investment in employee skills will enhance WPP's exposure to the fast growing digital advertising market and help brands to re-connect to consumers in more digitally focused world. We started a position in WPP in July and increased the holding after the positive strategic update given by the company in August.

**Intertek** has been able to use its global testing network and expertise in health and safety to launch a new product, Protek, the first truly global safety and wellbeing assurance programme for people, workplaces and public places. Intertek is also putting itself at the forefront of supply chain analysis and audit, helping companies and consumers to understand the provenance of products.

Equipment rental business **Ashtead** recorded its best ever quarter of cash generation in Q2. It has continued to open new branches since July, made no redundancies and is increasing investments in customer service. These actions will accelerate Ashtead's impressive track record of growth through larger market share.

**Hays**, which went into the crisis with £50m net cash on its balance sheet and raised a further £200m, has increased its spend on growth markets such as life sciences and IT. It has also developed an online training platform called Hays Thrive. This is being used by candidates and companies as a way of re-skilling, further embedding the role Hays plays for its clients.

We started a new position in **Whitbread** in May when it raised over £1bn to bolster its balance sheet and accelerate its hotel expansion plans in the UK and Germany. Whitbread has a well-invested and digitally-enabled estate that is well placed to dominate the UK and German hotel markets. The UK's second largest player Travelodge is going through a CVA process with its landlords. Meanwhile the 48% of the hotel market still in private hands is struggling to come to terms with more complex operating conditions. Whitbread's strong long-term prospects are largely ignored in the unloved UK equity market.

## 4. Company treatment of stakeholders

The pandemic has increased the focus on the wider behaviour and impacts of companies. We believe that firms who have looked after their staff, paid their suppliers and landlords and that have tried to reduce their environmental footprint will be in a strong position as we emerge into the 'new normal'. Our engagement on ESG issues is an integral part of our focus on both capital preservation and long-term structural growth.

In the last three months we have had frequent engagement with companies on these matters. We spoke to the Head of Products and Sustainable Development at **Next** in response to the failure of competitor Boohoo to ensure acceptable working conditions in its supply chain. We talked through the rigorous processes Next has in place thanks to its 46-strong product governance team, who in 2019/20 undertook 2,417 factory audits, many unannounced, the standards it expects of brands listing on its website, and its ambition to materially increase all products under its 2025 Responsible Sourcing Strategy. We are supportive of the group's approach to try and work to improve conditions, rather than take a knee-jerk response which could have disastrous impacts on local communities who rely upon textile factories for their own livelihoods.

We've had a series of engagements with **PZ Cussons**, expressing our concern about the unintended consequences of management incentive plans based on short-term earnings growth measures. We have put forward the case for organic growth, return on capital and more ambitious environmental targets to be included in the next set of incentive structures.

We have been engaging with **DCC** for nearly two years to request the company improves its accounting disclosure and particularly report on organic growth, which we believe can be masked by acquisitions. We were frustrated at the level of 'below the line' accounting adjustments and that management were paid on the basis of the company's adjusted earnings. The lack of change from the company, the fact that 70% of the business faces into oil, gas and other energy markets and the full valuation of the shares resulted in us selling out of our position in August.

### JOHCM UK Opportunities Fund
Periodic performance (%)

| | 3 m | 6 m | 1 y | 3 y | 5 y | SI p.a.[1] |
|---|---|---|---|---|---|---|
| JOHCM UK Opportunities Fund | -0.42 | 12.93 | -7.24 | 0.86 | 23.74 | 7.26 |
| Benchmark | -3.21 | 8.21 | -16.51 | -9.23 | 19.01 | 4.88 |
| UK All Companies Sector | -1.02 | 13.05 | -12.97 | -7.98 | 17.34 | 5.40 |
| Quartile* | 2 | 2 | 1 | 1 | 1 | 1 |

**Past performance is no guarantee of future performance.**

Source: JOHCM/Bloomberg/FTSE International. NAV of share class A in GBP, net income reinvested, net of fees, as at 30 September 2020. Benchmark: FTSE All-Share TR Index (12pm adjusted). Performance of other share classes may vary and is available upon request. Inception date: 30 November 2005. *Lipper Hindsight, IA UK All Companies Sector Rankings to 31 August 2020. Note: The current managers took over the fund on 1 October 2017. [1]Annualised.

### JOHCM UK Opportunities Fund
5 year discrete performance (%)

Discrete 12 month performance (%):

| | 30.09.20 | 30.09.19 | 30.09.18 | 30.09.17 | 30.09.16 |
|---|---|---|---|---|---|
| A GBP Class | -7.24 | 5.68 | 2.89 | 4.16 | 17.80 |
| Benchmark | -16.51 | 2.72 | 5.84 | 12.62 | 16.43 |
| Relative return | 11.10 | 2.89 | -2.79 | -7.51 | 1.17 |

**Past performance is no guarantee of future performance.**

Source: JOHCM/FTSE International/Bloomberg, NAV of Share Class A in GBP, net income reinvested, net of fees as at 30 September 2020. The A Acc GBP class was launched on 30 November 2005. Benchmark: FTSE All-Share TR (12pm adjusted). Performance of other share classes may vary and is available on request.

### JOHCM UK Opportunities Fund
Top ten holdings (%)

| | Stock | Weight |
|---|---|---|
| 1 | Unilever | 3.8 |
| 2 | GlaxoSmithKline | 3.4 |
| 3 | Reckitt Benckiser | 3.4 |
| 4 | PZ Cussons | 3.4 |
| 5 | Homeserve | 3.3 |
| 6 | Ferguson | 3.3 |
| 7 | Diageo | 3.2 |
| 8 | Intertek | 3.2 |
| 9 | Smith & Nephew | 3.1 |
| 10 | Tate & Lyle | 3.1 |

Source: JOHCM/Bloomberg as at 30 September 2020. Cash position is 9.72%. Cash includes cash on deposit and investments in UK Treasury Bills.

The value of an investment and the income from it can fall as well as rise as a result of market and currency fluctuations and you may not get back the amount originally invested. The annual management charge is deducted from the capital of the Fund. This will increase the income from the Fund but may constrain or erode potential for capital growth. We recommend that you read the Prospectus and Key Investor Information Document available from the address overleaf or from our website. Information on how JOHCM handles personal data which it receives can be found in the JOHCM Privacy Statement on our website: www.johcm.com. The information contained herein including any expression of opinion is for information purposes only and is given on the understanding that it is not a recommendation. Issued and approved in the UK by J O Hambro Capital Management Limited, which is authorised and regulated by the Financial Conduct Authority. JOHCM® is a registered trademark of J O Hambro Capital Management Ltd. J O Hambro® is a registered trademark of Barnham Broom Ltd. Registered in England and Wales under No:2176004. Registered office: Level 3, 1 St James's Market, London SW1Y 4AH.