



June 2019

FOR PROFESSIONAL INVESTORS ONLY

JOHCM UK Opportunities Fund Bulletin

For six-month period to 31 May 2019

Overview

- **Go shopping when the sales are on** – Quarter 4 2018 sell-off provided some buying opportunities
- **Dodge the rising political risks** – duck below the parapet of elevated political risk
- **Valuation still matters** – bridge the gap between expensive growth and high risk value
- **Avoid companies with too much debt** – sell companies accumulating debt and don't own banks.

Performance: encouraging results from our holdings

Our overriding objective remains to protect and then grow client capital. Over the last six months our fund generated a positive return of 2.52% in a market that has risen by 4.70%.

A number of stocks saw price increases of over 20%, including Sage, Rio Tinto, Howdens Joinery and Tesco. Whilst the underlying progress of these businesses remains on track, their strong share price performance was driven by the ongoing dominance of flow and market sentiment over stock fundamentals.

Vodafone was again a drag on performance. We stated our belief that the company should reduce its dividend to pay down debt during a meeting with the CEO at our offices in April. We were pleased that the board announced a dividend cut in May, together with assurances made at the results presentation that a strong balance sheet is now a priority.

Many of our holdings reported full-year results during the period. Pleasingly, these results demonstrated both the resilience of existing cash flows and a willingness to invest for long-term future growth. Johnson Matthey has accelerated its investment into cathode materials that will benefit from the ongoing trend towards electric vehicles. Smiths Group reported a 25% increase in R&D spend over the last three years, which is now delivering better organic revenue growth. Sage has demonstrated success in increasing its subscription revenues. These repeatable revenues generate the stability of cash flow that typifies a UK Opportunities business.

Christmas shopping followed by some sales

Market weakness at the end of 2018 presented the opportunity to invest a significant proportion of our cash balance. The team conducts work on potential new investments, meeting management and talking to customers and suppliers in anticipation of such periods of share price weakness that allow us to buy at attractive valuations.

- We started a position in **Tesco**. Management have repaired the balance sheet, disposed of non-core assets and embarked on a long-term strategy to rebuild trust among customers, employees and suppliers. There are early signs that the strategy is working and weakness in the share price during December provided an attractive entry point.
- We added **Johnson Matthey** to the portfolio. The business remains a market leader in a number of chemical technology areas and has increased R&D investment in order to benefit



Michael Ulrich, CFA
Senior Fund Manager

Michael has worked on the Fund since he joined JOHCM in August 2015 and has 22 years of industry experience.



Rachel Reutter, CFA
Senior Fund Manager

Rachel has worked on the Fund since she joined JOHCM in September 2012 and has 12 years of industry experience.



Roshni Rajan, CFA
Analyst

Roshni has worked on the Fund since she joined JOHCM in February 2018 and has 5 years of industry experience.

from trends towards pollution reduction and electric vehicles.

- We took advantage of share price weakness to re-establish a holding in **Rio Tinto**, which has market-leading iron ore assets and a strong balance sheet.
- We established smaller positions in **Hays, Bodycote** and Howden Joinery. All three businesses have strong long-term prospects and no debt, both of which are essential in businesses where we should expect cyclical swings in profits. Howden was subsequently sold after a 25% rise in the share price as we remain committed to implementing our valuation control.
- We have sold our position in Land Securities. The prospect of a weakening London office market will add to the already deteriorating environment for retail property.
- Shifts in the political environment led us to sell National Grid and to mark a complete exit from the UK utilities sector. Threats of nationalisation from the Labour Party and tougher regulation under the current government make this sector particularly unattractive at present.
- We have more recently reduced holdings in a number of stocks where valuations again look expensive: **Diageo, GlaxoSmithKline** and **Compass**.

Watch valuations (and the politics)

Valuations remain expensive across the market. Stocks that may look cheap based on short-term profits often possess structural and cyclical headwinds as well as overleveraged balance sheets. There is no shortage of well-run UK-listed businesses with good long-term prospects. Few offer attractive valuations, however. We have continued to sell stocks when they become too expensive and hold cash which we will spend only when the odds are in our favour. We maintain a high quality portfolio with an average free cash flow yield of 6%.

The political trend towards protectionism and state regulation has continued. In response we will continue to avoid those businesses where tougher regulation wins political votes such as utilities and government outsourcers. We will seek companies operating outside of the political spotlight or those which could benefit from government policies, such as brickmaker Ibstock, or from rising wages, such as Hays and Page Group.

As investors seek returns in more esoteric and illiquid assets, we believe asset liquidity will be a cause of financial distress when volatility returns to markets. Our fund remains dominated by larger, more liquid stocks. We hold no derivatives or unlisted equities and have no exposure to the illiquid small cap or AIM markets.

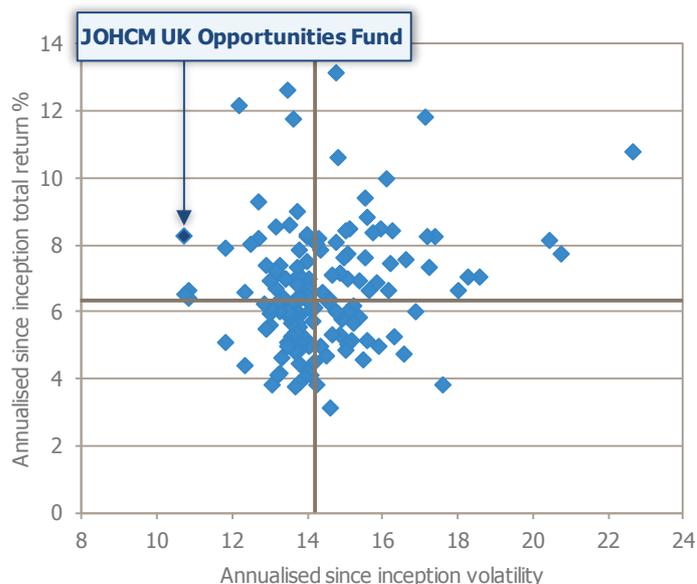
The Fund remains defensively positioned. We will avoid companies prepared to take on excessive debt. We hold no banks or life insurance companies. We favour companies with recurring and stable cash flows generated from multiple products or geographies. In an increasingly uncertain environment the portfolio comprises a diverse set of risks.

Patience and discipline are key to our process. Our research efforts have resulted in a full shopping list of high quality businesses in which we will deploy our cash when changes in valuations, balance sheets or management behaviour turn the risk/reward relationship in our favour.

Despite our elevated cash position, the Fund is currently yielding 2.8%.

Strong track record of risk-adjusted returns

JOHCM UK Opportunities Fund since inception risk return scatter to 31 May 2019 – IA UK All Companies



Past performance is no guarantee of future performance. Source: JOHCM / Lipper as at 31 May 2019 based on JOHCM UK Opportunities Fund A GBP share class against the IA UK All Companies. Please note the IA UK All Companies sector is used

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Source: JOHCM/Bloomberg unless otherwise stated. Issued by J O Hambro Capital Management Limited authorised and regulated by the Financial Conduct Authority. Past performance is no guarantee 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 your original investment. Dividend yield quoted is prospective, is based on internal estimates and is not guaranteed. 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 below or from our website. 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. Source: JOHCM/Bloomberg/FTSE International. FTSE International Limited ("FTSE") © FTSE 2017. The Industry Classification Benchmark ("ICB") and all rights in it are owned by and vest in FTSE and/or its licensors. "FTSE" ® is a trademark of the London Stock Exchange Group companies and is used by FTSE International Limited under licence. Neither FTSE or its licensors accept any liability for errors or omissions in the ICV. No further distribution of ICB is permitted without FTSE's express written consent. Information on how JOHCM handles personal data which it receives can be found in the JOHCM Privacy Statement on our website: www.johcm.com. JOHCM® is a registered trademark of J O Hambro Capital Management Ltd. J O Hambro® is a registered trademark of Barnham Broom Holdings Ltd. Registered in England and Wales under No: 2176004. Registered address: Level 3, 1 St James's Market, London SW1Y 4AH, United Kingdom.

for comparative purposes only. The Fund is currently classified within the IA Specialist sector because its UK equities holdings currently represent less than 80% of the portfolio.

JOHCM UK Opportunities Fund

Data as at 31 May 2019

Return history (%):

	6m	1yr	3yr	5yr	SL	Annualised*
Fund	2.52	1.53	17.01	28.92	192.40	8.27
Index	4.70	-3.52	27.82	28.94	131.21	6.40
Relative	-2.08	5.23	-8.46	-0.01	26.47	1.75

Discrete 12 month performance (%):

	31.05.19	31.05.18	31.05.17	31.05.16	31.05.15
A Acc GBP	1.53	0.24	14.97	1.50	8.55

Past performance is no guarantee of future performance. 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.

Source: JOHCM/FTSE International/Bloomberg, NAV of Share Class A in GBP, net income reinvested, net of fees as at 31 May 2019. 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. *Annualised since launch. Relative return calculated on a geometric basis.

Full portfolio holdings (28)

	Weight (%)	Weight (%)	
Royal Dutch Shell	5.62	Direct Line Insurance	2.73
RELX	3.40	Diageo	2.69
Tesco	3.40	Morrisons	2.59
Reckitt Benckiser	3.24	Bunzl	2.44
BP	3.22	Imperial Brands	2.43
Unilever	3.21	Barrick Gold	2.32
PZ Cussons	3.13	Sage	2.23
Smiths	3.10	Smith & Nephew	2.16
GlaxoSmithKline	3.09	Rio Tinto	2.07
Compass	3.08	Ibstock	1.99
DCC	3.06	Next	1.78
Associated British foods	3.01	Hays	1.12
Vodafone	2.79	PageGroup	0.98
Johnson Matthey	2.79	Bodycote	0.78

Note: Cash position is 25.56%. Cash includes cash on deposit and investments in UK Treasury bills. Please note that due to rounding breakdowns may not add to 100.00%.