



UK OPPORTUNITIES



9 APRIL 2020

Rachel Reutter, Senior Fund Manager

Michael Ulrich, Senior Fund Manager

Management behaving better

The Covid-19 pandemic continues to put immense pressure on health services, economies and societies around the world. In particular, it has reshaped the political backdrop in which we invest. We are far from experts in the pace of change in the terrible number of cases and recognise that the art of timing when to become more constructive on equities based on constantly-moving factors is very difficult.

At the top-down level, we are adapting our portfolio to be as far away from government intervention as possible. We continue to steer away from companies where the likelihood of state support is high, revenues remain volatile and returns are going to come down dramatically.

At the company level, we have found it useful to think about the changes which are taking place. And the good news amongst all of the bad is that management behaviour is starting to change for the better.

To put this in a framework, before this crisis we had three major issues with companies in our investment universe:

1. Overdistribution
2. Overleverage
3. Overvaluation

Where are we with these issues today?

- 1. Overdistribution via dividends and buybacks** – As of 9 April 2020, 43% of companies within the FTSE 250 index (excluding investment trusts) have cancelled or suspended their dividends (source: Liberum). There will be no buybacks. Some very difficult circumstances have succeeded in stopping companies from behaving like ‘cash machines’. The great shift in capital allocation from distributions to shoring up balance sheets and investing again will continue to open up some interesting investment opportunities.
- 2. Overleverage** – The suspension of dividends is positive for the de-gearing of UK plc, which went into this crisis with an all-time high average net debt: EBITDA of 2.5x (excluding financials). We are hopeful that when dividends resume, they will be at more appropriate levels. The next stage of recapitalising companies with equity has only just begun. We backed Hays in its recent placing and are ready with plenty of liquidity to support other companies, providing they raise enough and solve their debt problems.
- 3. Overvaluation** – Whilst we expect the short-term backdrop to remain challenging for a while to come, we have good levels of valuation upside potential in our portfolio on a three to five-year view. The quality of the portfolio has improved, and we have been careful to ‘update the facts’ on company-specific growth drivers in order to own companies which still have growth tailwinds as we come out of the Covid-19 pandemic.

You should expect us to continue to use this framework at the bottom-up level to guide the deployment of cash into new and existing stocks, whilst remaining mindful of the huge shift in the top-down backdrop, from a world of financialisation to one of nationalisation.

Rachel Reutter & Michael Ulrich

JOHCM UK Opportunities Fund

5 year discrete performance (%)

Discrete 12 month performance (%):

	31.03.20	31.03.19	31.03.18	31.03.17	31.03.16
A GBP Class	-14.67	9.71	-3.46	12.31	5.87
Benchmark	-19.06	5.93	1.36	21.88	-4.42
Relative return	5.41	3.57	-4.76	-7.85	10.77

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 31 March 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.

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. 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.