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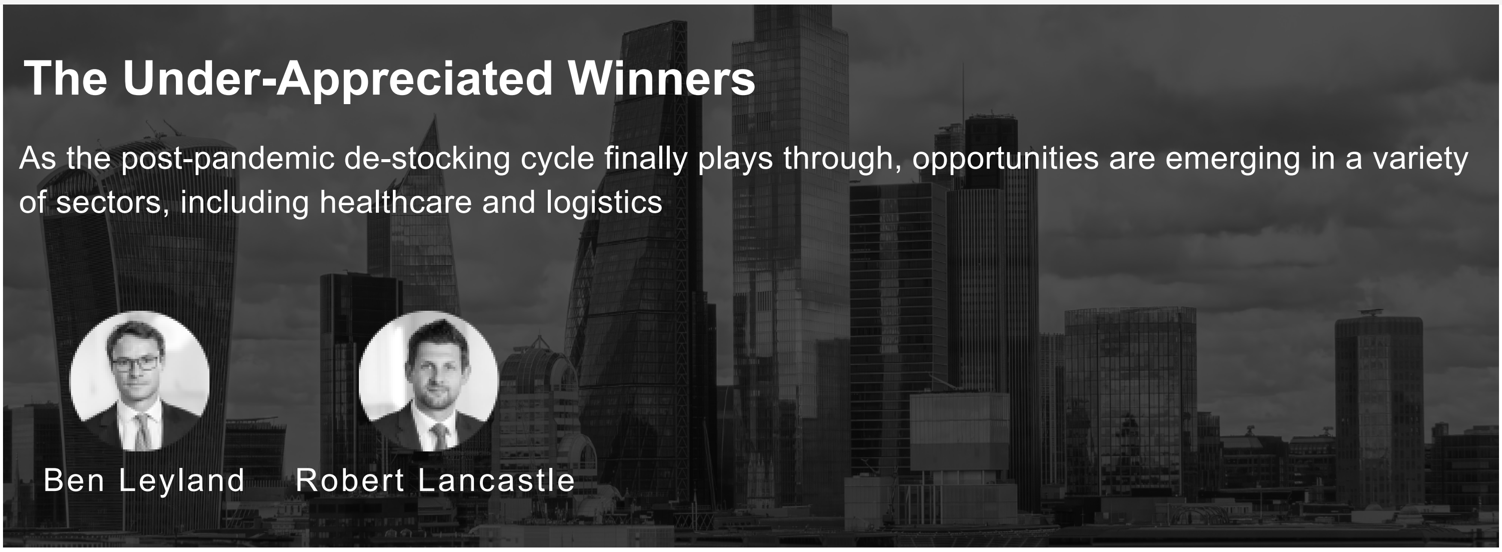

15 Apr 2024

As the post-pandemic de-stocking cycle finally plays through, opportunities are emerging in a variety of sectors, including healthcare and logistics

A Conversation with Ben Leyland and Robert Lancastle Senior fund managers, JOHCM Global Opportunities and JOHCM International Opportunities

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Ben: There is a lot of momentum in cyclicals because the PMI is now back in expansionary territory above 50, which indicates growth of the US manufacturing sector, meaning recession has been averted.

Rob: Yes, there's a lot of top-level metrics that indicate all is well. But we've never bought cyclicals for a trade on the PMI index. We've bought structural growth businesses, which happened to be cyclical rather than just cyclicals per se.

Ben: It's certainly true that a lot of cyclicals are picking up, such as US Industrials and companies in the semi-conductor space, where Nvidia is getting all the headlines. But there are also cyclical headwinds affecting certain companies in a variety of sectors which are going through destocking cycles. This is now presenting opportunities, for example in sectors such as healthcare, logistics and beverages.

Rob: Our job ultimately is to go rooting around the areas of the market which we think have a short-term underperformance cycle going on. But we believe they're ultimately long-term winners because of their advantages in their industries.

Ben: Our portfolio always has a balance of some names firing on all cylinders and some names going through a temporary slowdown. We have companies which are starting to execute well and enjoying the benefits of an upcycle, but where the ultimate potential is not fully priced in yet. But we also like to have companies which aren't working so well and are more attractively valued. With these, it's the short-term lack of earnings momentum which is creating the opportunity on a three-year view.

Rob: We are willing to not follow the momentum. We like areas of the market that are weak from soggy short-term fundamentals but where the long-term growth opportunity is being overlooked. If this goes on for a prolonged period, we may own several names to make a cluster and ultimately increase weight further as the fundamentals rise. Life science companies in healthcare sector are a cluster we have been building recently.

Ben: Healthcare companies are structural beneficiaries of demographic trends combined with budgetary constraints. The need for healthcare systems globally to deliver better outcomes, more cost effectively, is continuing to increase, regardless of what the political situation is within any country.

But over the last four years we’ve seen a huge wave of demand driven by Covid, followed by a huge wave of destocking, also driven by Covid. Then, the constrained supply encouraged companies to build up inventory in case of supply chain disruption.

Now, companies are running down their inventories in the context of falling demand from super normal levels. That starts to make it look like the healthcare system has temporary headwinds which are masking these longer-term positive dynamics.

That's the rationale for the under-appreciation. But it fits what we're looking for, a great 10-year story, maybe halfway through a three-year period of headwinds.

Rob: They might not grow as much as they did a year or two ago because of the ultimate industry dynamics being soggy for a bit. But we are looking for things that will survive and then very much thrive. It's clearly defined by things that we think will be temporary in companies that we have a really strong belief will be natural winners. It’s an important differential to a classic value and mean reversion type approach.

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