

JOHCM UK DYNAMIC FUND



UNDER THE BONNET



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OCTOBER 2021 REVIEW

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INVESTMENT BACKGROUND

Economic activity generally remained buoyant in October, driven in particular by continuing strength in the service sector as economies continue to open up and bounce back from Covid-19 lockdowns. The manufacturing sector, whilst strong, remained affected by supply shortages and bottlenecks leading to a continued rise in both input and output inflation, particularly in the US.

Employment indices continue to signal tight market conditions and building wage cost pressures with the UK KPMG / REC survey posting the sharpest rate of starting salary increases for both temporary and permanent workers in 24 years of data collection.

The Deloitte CFO survey for Q3 indicated an expectation in the UK that the labour shortages and supply disruptions were likely to persist for a year with labour supply being of particular concern. However despite these concerns, most respondents remain in expansionary mode with more CFO's placing greater emphasis on increasing capital expenditure than at any time in the survey's history. The survey can be found [here](#).

Short-dated (2Y) UK bond yields surged above 2Y US Treasury yields following hawkish commentary from the Bank of England. Warnings that higher energy costs meant that the central bank would 'have to act' to curb inflationary forces drove market expectations of an interest rate hike in the final months of 2021.

STRATEGY UPDATE

The Fund underperformed for the second month running with the fund price ending the month broadly flat whilst the benchmark, the FTSE All-Share index rose 1.32%. The underperformance was mostly driven by idiosyncratic (and we feel shorter-term) share price movements relating to two stocks in particular, but was also not helped by shorter-term macro and factor movements.

Given the continued backdrop of raw material shortages, supply chain issues, excess demand and inflationary pressures, October saw a continuation of Value (factor) leadership in the UK. Whilst this could be construed as positive for the Fund, in reality, Value leadership in the FTSE All Share was driven heavily by banks within financials (the FTSE 350 bank sector rose 9.4%) and by the oil & gas sector (Brent crude rose 8% to \$84 per barrel - a level not seen since 2014). In the Fund, the performance of energy and financials over the month was broadly neutral, reflecting the sector positioning the Fund currently has.

Staying on the factor thematic, Growth underperformed, but the stand out negative was continued weakness from high Dividend Yield which returned -3.8% relative. The Dividend Yield factor has now underperformed -13.6% year to date. This has definitely had an effect on some of the higher yielding names in the portfolio like **Direct Line**, **Vodafone** and **Aviva**.

Turning to the more idiosyncratic underperformers, October saw sharp declines in **QinetiQ** and **Pearson**. Both were similar size positions in the portfolio at the beginning of October (at c.3.3%) and both reacted extremely negatively to what might have been seen as either in-line or slightly negative statements. The stocks fell 17% and 15% respectively, after minor revisions to their underlying forecasts but saw material declines to their forward P/E estimates and therefore a reduction in future growth and profit expectations. This might be understandable in some circumstances (for example with a materially negative change in profit mix or where there is a highly levered balance sheet leaving the equity sensitive to minor EPS changes), but in our reading of both sets of results, the higher valued parts of both businesses remain on an extremely positive trajectory and in both cases the balance sheets are under-levered not over-levered. Both shares again offer opportunity as both now trade on P/E ratios that are, in our opinion, too low, given their businesses, their strategic narratives, their balance sheets, and their future opportunities.

Other negatives over the month were, in the main, just timing issues and not representative of anything in particular. **DMGT** is a case in point. It cost us c. 30bps relative over the month as the market became impatient waiting for news on the formal bid from the Rothermere family. As we write, the bid has been received, the shares have moved higher again, the underperformance has more than unwound and we are considering our stance.

Vodafone was another example. In line with the Telecoms sector and perhaps also exposed to the Dividend Yield Factor, the stock was weak but for no good reason that we could see.

Away from these shorter-term negatives we remain extremely excited by the prospects for this portfolio of transformation investments. There are very good things going on strategically – note the accelerating changes at (new idea) **Landsec** as an example and the fantastic performance of **Man Group** recently, which is testament to the patient and disciplined transformation that has occurred within the Group over a number of years but which only now seems to be gaining the external acceptance it has long deserved.

As we look into November, during which the Fund has a material number of trading statements and results to be announced, we are extremely confident of further positive strategic and financial delivery, and, with it, a bounce back in performance.

FUND PERFORMANCE

JOHCM UK Dynamic Fund performance (%):

	1 month	3 months	1 year	5 years	10 years	SI annualised
Fund	-0.04	1.17	52.08	30.68	152.04	9.22
Benchmark	1.32	3.57	35.48	31.21	103.26	6.27
Relative return ¹	-1.34	-2.32	12.26	-0.40	24.00	2.77

Discrete 12 month performance (%):

	31.10.21	31.10.20	31.10.19	31.10.18	31.10.17
Fund	52.08	-31.02	5.92	-2.00	20.00
Benchmark	35.48	-18.85	6.78	-1.34	13.29
Relative return ¹	12.26	-15.00	-0.80	-0.67	5.92

Past performance is not necessarily a guide to future performance

Source: JOHCM/Bloomberg/FTSE International. NAV of share class A in GBP, net income reinvested, net of fees, as at 31 October 2021. Inception date: 16 June 2008. Note: Performance data for the period 16 June 2008 to 22 October 2009 is for Ryder Court UK Dynamic Fund. From 23 October 2009 onwards, the Fund converted to JOHCM UK Dynamic Fund. All fund performance is shown against the FTSE All-Share TR Index (12pm adjusted). Performance of other share classes may vary and is available upon request. ¹Geometric relative.

ONE MONTH STOCK RELATIVE CONTRIBUTORS

Top five

Rank	Stock	Relative Return Contribution %
1	Man Group	0.25
2	3i	0.21
3	WPP	0.21
4	Rio Tinto*	0.19
5	Barclays	0.18

Bottom five

Rank	Stock	Relative Return Contribution %
1	QinetiQ	-0.61
2	Pearson	-0.54
3	DMGT	-0.30
4	Melrose	-0.23
5	Vodafone	-0.19

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Source: JOHCM/FTSE International/Bloomberg. Figures are at end of day and calculated gross of fees on an arithmetic basis in GBP. All performance is shown against the FTSE All-Share TR Index (12pm adjusted). Data from 30 September 2021 to 31 October 2021. *Stock was not held during this period.

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The Fund’s investment includes shares in small-cap companies and these tend to be traded less frequently and in lower volumes than larger companies making them potentially less liquid and more volatile.

Note for return history: NAV of share class A in GBP, net income reinvested. Benchmark: FTSE All-Share TR Index. Performance of other share classes may vary and is available on request.

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