Sanlam Investments

Sanlam FOUR Active UK Equity Fund

Q4 2018 | Quarterly newsletter

Market recap

In our Q3 report we highlighted the risk to equity markets from rising short term US interest rates, suggesting that "at some point investors will believe that enough has been done and the risk of a Fed policy mistake will undermine equity confidence." The main feature of Q4 has been precisely this. These concerns began to intensify in October but the tipping point for markets only really came after the Fed meeting in December where comments made following the rate rise (largely expected) failed to provide the reassurance needed that policy would become more data sensitive.

While we were alert to this risk, we did not anticipate such a rapid escalation, particularly given the continuing strong US economic growth. What little US investor confidence remained quickly evaporated, sending equity markets tumbling and volatility spiking higher. In this "risk-off" climate US Government 10 year bond yields drifted further below the perceived critical 3% level, helped by receding inflation risks as commodity prices also fell. The ongoing US/China trade war continued to sap confidence, both at the corporate spending level and for investors.

Equities market moves are largely consistent with the narrative that US growth has peaked and global recession risks are rising; the sharpest falls have been in industrial, energy and consumer discretionary sectors, whilst healthcare and utilities have displayed their traditionally defensive qualities.

Fund review

The fund fell sharply in the quarter, albeit in-line with the benchmark. This is disappointing in absolute price terms but we believe the fall represents a derating rather than a permanent loss of equity value. Surprisingly, some of the most significant out-performers contributing positively have been UK economically exposed companies. In contrast, the main detractors have tended to be more internationally oriented businesses that continue to meet growth expectations yet have been significantly de-rated.

Across the market, temporary trading set-backs have been met with significant share price falls. This impacted our holdings in Sophos and IQE, whilst longer term structural concerns have continued to depress the rating on ITV shares. The only new holding in the period was housebuilder Taylor Wimpey. Following recent share price weakness (impacting all UK housebuilders) we believe that valuation attractions have become exceptionally compelling. This was largely funded by the disposal of Shire, a strong recent performer ahead of the closure of the takeover by Takeda.

Performance data

	Inception	QTR	YTD	1yr	3yrs	5yrs	Since Inception
A Accumulation GBP	02/04/07	-10.0	-11.3	-11.3	2.6	0.6	4.0
MSCI UK		-9.7	-8.8	-8.8	6.7	3.6	4.2

Performance beyond one year is annualised

12 Months to	Dec-18	Dec-17	Dec-16	Dec-15	Dec-14
A Accumulation GBP	-11.3	15.3	5.5	0.8	-5.5
MSCI UK	-8.8	11.7	19.2	-2.2	0.5

Past performance is not an indicator of future performance.

Source: Sanlam, Morningstar and Lipper as at 31/12//2018.

Key facts

Fund AuM	£24.8m
Strategy AuM	£24.8m
Number of Holdings	41
Active Share	57.3%
Yield	4.9%
Fund Managers	Chris Rodgers Andrew Evans
Benchmark	MSCI UK
Fund Launch Date	02 April 2007
Domicile	Ireland
Base Currency	Sterling
Fund Type	OEIC, UCITS V
IA Sector	UK All Companies
Morningstar Category	UK Flex-Cap
Dealing Deadline	11:00 (GMT)
Settlement Time	T+3
Valuation Point	Midday (GMT)
Distribution	Semi-Annually

Performance attribution

The fund's fall is disappointing in absolute terms, but in a relative sense this is a resilient out-turn given the escalating concerns for global economic growth. As long term, bottom-up stock pickers, our process is not especially focussed on trying to time the economic cycle. Our current thematic portfolio positioning, being overweight in stocks with cyclical and structural growth characteristics and underweight in defensive areas such as food and drink, utilities and healthcare, has not been ideal when global growth concerns have been the main driver of market returns.

Holdings contributing positively to performance have been an eclectic grouping, including resilient domestic companies such as Whitbread and Great Portland Estates, international stable growth businesses such as RELX and John Laing, and beneficiaries of recovering sentiment such as Sage, BT Group and Paddy Power Betfair. We also received a relative benefit from being underweight in British American Tobacco, where the shares fell sharply in response to news that the US FDA might ban the sale of menthol cigarettes, which represent a major part of their US business.

The main detractor was First Derivatives, where a near halving in the share price bears no relation to the continuing strong growth and positive trading updates. However, several other high growth stocks have seen similar rerating in valuations and seems to reflect a changed mood in the market rather than business fundamentals. Less extreme deratings also impacted our Sophos, XP Power and Integrafin holdings. Not holding defensive large cap stocks such as Diageo and AstraZeneca also impacted negatively, along with our overweight position in Prudential and underweight in HSBC. Finally, Wood Group issued a reassuring trading update only to see the shares fall sharply reflecting generalised concerns following recent oil price weakness.

Key purchases:

- Taylor Wimpey (new holding): Like other housebuilders, this leading UK housebuilder has recently seen its shares fall sharply despite satisfactory trading. With its national coverage and minimal exposure to London, the business is well placed to continue to generate strong profitability and free cash flow. Brexit risks have spooked investors to the point where the shares now offer a relatively safe yield of over 10%.

- Howden Joinery (significant addition): generalised weakness in building related stocks offered an opportunity to increase exposure to this high quality and well managed business. The business model of selling to small, local builders and tradesman has proven to be popular and resilient.

These purchases were funded from the disposal of Shire (ahead of the completion of the takeover by Takeda and receipt of Takeda shares). Elsewhere, we trimmed holdings in Wood Group, Imperial Brands, Crest Nicholson and BT, while topping up positions in GlaxoSmithKline, Unilever and Lloyds Banking.

Outlook

Following the collapse and subsequent choppy trading in the US equity market, with a knock on effect globally, investor sentiment is now at depressed levels that seem to already discount much potential bad news. Taken in tandem with lower government bond yields and widening credit spreads this would seem to anticipate much weaker economic growth, or at least heightened risk aversion thereof.

Against this gloomy backdrop the US economy actually ended the year in good shape, with strong consumption and consumer confidence, yet moderating inflationary pressures. Undoubtedly the impact of US fiscal stimulus from Trumps' tax cuts will start to fade in 2019, but with high employment, still healthy corporate profitability and a strong banking sector, there is little reason to expect an imminent slump into recession. Some moderation in US growth is likely, but this would not be unwelcome as it would encourage a more dovish Fed policy. This in turn would take the upwards pressure off the dollar and could encourage a resynchronisation of the global economy.

Obviously there are many risks to this rosy scenario, but it is mentioned in order to provide a counter-balance to prevailing pessimism and suggest that there is a path of successful policy normalisation that need not end in a global recession. Whilst most of the risks are now well known to investors, perhaps the most unfathomable are the erratic and damaging policies of an astonishingly ignorant and inept US president. Along with global trade wars, rising populism, Chinese economic slowdown and Brexit, there will be plenty of reasons to expect markets to remain volatile in 2019. The counterbalancing positive considerations are that stock valuations are no longer stretched and the global economy is still set for reasonable growth despite these headwinds.

Contact us

Liz Adnitt
Sales Director

+44 (0) 20 3116 4071
Liz.Adnitt@Sanlam.co.uk

Alexandra Dacres-Hogg
Sales Manager

+44 (0) 20 3116 4041
Alexandra.Dacreshogg@Sanlam.co.uk

Sanlam Investments
Monument Place
24 Monument Street
London
EC3R 8AJ

Important Information

The Fund invests geographically in a narrow range, there is an increased risk of volatility which may result in frequent rises and falls in the Fund's share price.
The value of this portfolio is subject to fluctuation and past performance is not necessarily a guide to future performance. The performance is calculated for the portfolio and the actual individual investor performance will differ as a result of initial fees, the actual investment date, the date of reinvestment and dividend withholding tax. All terms exclude costs. Fluctuations or movements in exchange rates may cause the value of underlying investments to go up or down. Do remember that the value of participatory interests or the investment and the income generated from them may go down as well as up and is not guaranteed, therefore, you may not get back the amount originally invested and potentially risk total loss of capital. Therefore, the Manager does not provide any guarantee either with respect to the capital or the return of a portfolio. The Manager has the right to close any Portfolios to new investors to manage them more efficiently in accordance with their mandates. Collective Investment Schemes are traded at ruling prices and can engage in borrowing and scrip lending. Collective Investment Schemes (CIS) are generally medium to long term investments. A schedule of fees and charges and maximum commissions is available on request free of charge from the Manager, the Investment Manager or at www.sanlam.ie.
Issued and approved by Sanlam Investments. Sanlam Investments is the trading name for our two Financial Conduct Authority (FCA) regulated entities: Sanlam FOUR Investments UK Limited (FRN 459237), having its registered office at 1 Ely Place, London EC1N 6RY and Sanlam Private Investments (UK) Ltd (FRN 122588) having its registered office at 16 South Park, Sevenoaks, Kent, TN13 1AN.
The Fund is a sub-fund of the Sanlam Universal Funds plc, a company incorporated with limited liability as an open-ended umbrella investment company with variable capital and segregated liability between sub-funds under the laws of Ireland and authorised by the Central Bank. The Fund is managed by Sanlam Asset Management (Ireland) Limited, Beech House, Beech Hill Road, Dublin 4, Ireland, Tel + 353 1 205 3510, Fax + 353 1 205 3521 which is authorised by the Central Bank of Ireland, as a UCITS Management Company and Alternative Investment Fund Manager, and is licensed as a Financial Service Provider in terms of Section 8 of the South African FAIS Act of 2002. Sanlam Asset Management is a registered business name of Sanlam Asset Management (Ireland) Limited. Sanlam Asset Management has appointed Sanlam FOUR Investments UK Ltd as Investment Manager to this fund.
This document is provided to give an indication of the investment and does not constitute an offer/invitation to sell or buy any securities in any fund managed by us nor a solicitation to purchase securities in any company or investment product. It does not form part of any contract for the sale or purchase of any investment. The information contained in this document is for guidance only and does not constitute financial advice.
The fund price is calculated on a net asset value basis, which is the total value of all assets in the portfolio including any income and expense accruals. Trail commission and incentives may be paid and are for the account of the manager. Performance figures quoted are from Sanlam FOUR and are shown net of fees. Performance figures for periods longer than 12 months are annualized. NAV to NAV figures are used. Calculations are based on a lump sum investment.
Please note that all Sanlam FOUR Funds carry some degree of risks which may have an adverse effect on the future value of your investment. Any offering is made only pursuant to the relevant offering document, together with the current financial statements of the relevant fund, and the relevant subscription/application forms, all of which must be read in their entirety together with the Sanlam Universal Funds plc prospectus, the Fund supplement, the MDD and the KIID. All these documents explain different types of specific risks associated with the investment portfolio of each of our products and are available free of charge from the Manager or at www.sanlam.ie. No offer to purchase securities will be made or accepted prior to receipt by the offeree of these documents, and the completion of all appropriate documentation. Use or rely on this information at your own risk. Independent professional financial advice should always be sought before making an investment decision as not all investments are suitable for all investors.
This document contains information intended only for the person to whom it is addressed or presented (Investment Professionals, defined as Eligible Counterparties or Professional Clients), and is intended for evaluation purposes, with no licence to use the content or materials within. It must not be distributed to general public, or relied upon by Retail Investors.
The opinions are those of the author at the time of publication and are subject to change, without notice, at any time due to changes in market or economic conditions. Whilst care has been taken in compiling the content of this document, neither Sanlam FOUR nor any other person makes any guarantee, representation or warranty, express or implied as to its accuracy, completeness or fairness of the information and opinions contained in this document, which has been prepared in good faith, and to the fullest extent permissible under UK law. Some parts/sections of this document may been compiled from external sources. Whilst these sources are believed to be reliable, the information has not been independently verified and is subject to material amendment, revision and updating, therefore no representation is made as to its accuracy or completeness. No reliance may be placed for any purpose whatsoever on the information, representations or opinions contained in this document nor shall it or any part of it form the basis of or act as an inducement to enter into any contract for any securities, and to the fullest extent permissible under UK law no liability is accepted or any such information, representations or opinions. The comments should not be construed as a recommendation of individual holdings or market sectors, but as an illustration of broader themes.
Statements in this document that reflect projections or expectations of future financial or economic performance of a strategy, or of markets in general, and statements of any Sanlam FOUR strategies' plans and objectives for future operations are forward-looking statements. Actual results or events may differ materially from those projected, estimated, assumed or anticipated in any such forward-looking statement. Important factors that could result in such differences, in addition to the other factors noted with forward-looking statements, include general economic conditions such as inflation, recession and interest rates, political or business conditions or in the tax or regulatory framework in the UK or other relevant jurisdictions, any of which could cause actual results to vary materially from the future results implied in such forward-looking statements. No assurance can be given as to the future results that will be achieved.
Sanlam FOUR makes no representation as to whether any illustration/example mentioned in this document is now or was ever held in any Sanlam FOUR Fund or Model Portfolio. Examples / Illustrations shown are only for the limited purpose of analysing general market, economic conditions or highlighting specific elements of the research process.
All of the information herein should be treated as confidential material with no less care than that afforded to the addressee's own confidential material of the most sensitive nature
Neither Sanlam FOUR nor any other person accepts responsibility or liability whatsoever for any loss howsoever arising, either directly or indirectly from any use of this presentation or its contents or otherwise arising in connection therewith. It should not be copied, faxed, reproduced, divulged or redistributed or passed on, directly or indirectly, to any other person or published in whole or in part, for any purpose, without the express written consent of Sanlam FOUR.
This document may constitute material non-public information, the disclosure of which may be prohibited by law, and the legal responsibility for its use is borne solely by the recipient.
There is no certainty the investment objectives of the portfolios or strategies mentioned in this document will actually be achieved and no warranty or representation is given to this effect.
Sanlam FOUR funds mentioned in this document are only available for sale in certain jurisdictions. For the avoidance of doubt, this document is not intended to promote these Funds to any person in any jurisdiction where such promotion is not permitted under applicable laws and regulations. Potential investors in these Funds should inform themselves of the applicable laws and regulations of the countries of their citizenship, residence or domicile and which might be relevant to any type of transaction in shares/units of our Funds. By accepting the terms of this disclaimer, you expressly acknowledge that you are, as the case may be, an investor who is legally or otherwise duly authorised to seek information about our Funds. NS0119(06)0419 UKRet