

RATHBONE GREENBANK MULTI-ASSET PORTFOLIOS

DEFENSIVE GROWTH FUND

Quarterly investment update
January to end March 2024

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HOT TOPICS

'TOP-DOWN' (MARKET AND MACROECONOMIC)

SO NEAR, YET SO FAR

At the back end of last year, investors were confidently forecasting six or seven interest rate cuts from the US Federal Reserve (Fed) in 2024. They've since reined those bets in big time and currently think the Fed will deliver about three 0.25% cuts – if that – perhaps starting in the early summer.

That about-turn has driven big moves in government bond markets. Government bonds are the asset class most sensitive to rate expectations, so it's hardly surprising that their yields have risen, driving their prices down.

We think American rates will fall in time, but inflation and economic growth will need to moderate further first, and exactly when that will happen is anyone's guess. Ours, for what it's worth, is sometime in the second half of this year.

On this side of the Atlantic, however, we think there's a greater chance of rates falling faster and further. Given dire economic growth in the UK and a lot of Europe, the rates situation seems more favourable than in the US, where there's greater evidence that inflation mightn't yet be vanquished. The UK and EU seem more likely to cut sometime around the middle of the year.

Expectations for Fed interest rate cuts fall from six 0.25% cuts to three in just one quarter.



WHO NEEDS RATE CUTS ANYWAY?

For much of 2023, investor confidence tracked central bank-speak slavishly. Stocks sold off in early autumn when investors expected the Fed to keep rates higher for longer in its ongoing fight against inflation and then surged towards year-end when the central bank seemed more confident about getting inflation down to its 2% target.

So why have stock markets hardly blinked this year as rate cut bets have been pared back so aggressively? It seems that as 2023's higher-rate-driven US bank failures fade from their collective memories, investors have got a lot more comfortable about higher-for-longer rates. Who needs cuts when America's economy keeps defying recession forecasts and is booming instead?

Providing company profits prove sustainable, stocks can probably keep rallying for a while longer. Stronger profitability would tend to imply a better economy and, therefore, less pressing need for those ever-elusive rate cuts. Stock market bulls also argue that gains are getting broader, and less alarmingly concentrated. In contrast to the first 10 months of 2023, when an unusually small number of stocks contributed to the gains of the entire US index and most underperformed, more global companies are participating in this year's rising markets.



**Who needs rate cuts when
America's economy keeps
defying recession forecasts
and is booming instead?**

FROM PASTIME TO PARADIGM

You wouldn't be too far wrong if you said that computer chip designer Nvidia *was* the market this quarter. It seemed like everyone was waiting for its results and the S&P 500 Index was a flock of sheep following its bellwether. In the first quarter, Nvidia's share price soared 82%, while the S&P 500 was up 11%. Nvidia accounted for almost a quarter of the index's total gain in Q1.

This huge increase in the price of Nvidia's shares wasn't driven by hype. It was underpinned by a more than 400% rise in its quarterly earnings per share compared with a year earlier. This surge in profits means that despite Nvidia's soaring share price, its price-to-earnings multiple (at 35x next year's forecast profits) is roughly half what it was in the second half of last year. Without Nvidia's profit growth, the S&P's information technology sector's Q1 profits would have gained just 8% on the previous year. With Nvidia, the sector – which is stacked with some of the world's largest and most successful companies – made 20% more.

However, Nvidia was just the posterchild for a wider dawning of AI. Most companies in the AI supply chain soared as well. Businesses that print the chips, like Taiwan Semiconductor Manufacturing Company, and those that sell the intricate machines that allow companies to make chips, like ASML, have performed very well this quarter as well (we own both). To roll out AI as expected, there needs to be huge investment in the infrastructure: in the data centres and servers that deliver the computing power AI requires. Because of exponential improvements in computing power from year to year, the life cycles of these AI-enabling data centres are decreasing. Meanwhile, rampant demand is driving the need for more. More chips are needed each year to go into the centres today, and better ones need to be ready for replacing them in years to come.

This has all the hallmarks of a step-change in technology akin to the Industrial Revolution and the creation of the internet. And that means great opportunities and great risks. Moments of change like this often make fortunes and squander others. It's very easy for people and businesses to get overexcited and overbuild, creating a glut that upends prices and profits. Sometimes businesses simply find themselves with the wrong business model. Everything is new, so no one knows just how many chips we will need, what the most lucrative part of the business will be, or what pitfalls lurk in an AI-enabled future.

We have spread our investments across the AI supply chain, owning the chip designers, the chip makers, the companies that make the printers for the makers, the businesses that run the data centres and then the companies monetising AI and selling it to households and businesses. The steady and punchy increases in sales across all parts of the AI supply chain show that this is no longer just over the horizon, this is happening right now.

PORTFOLIO ACTIVITY

Key purchases/additions	Key sales/trims
LKQ (purchase)	Vodafone (sale)
UK Gilt 0.625% 06/07/2025 (purchase)	Nidec (sale)
UK Gilt 1.5% 07/31/2053 (addition)	Edwards Lifesciences (trim)
UK I/L Gilt 0.75% 03/22/2034 (purchase)	UK Gilt 0.125% 08/10/2031 (sale)
BNP 10YR US Rates Swaption May 2024 (purchase)	Advanced Drainage Systems (trim)

Source: Rathbones

Nvidia was created in the early 1990s to make computer game graphics more beautiful. Its work over the past 30 years led it by chance into driving AI, one of the most important technologies of the 21st century. You've probably heard a lot about it lately, although for many years it was known only by computer nerds and video gamers.

Focused on building computer chips that could process graphics for computer games, Nvidia got better and better at designing chips. Graphics used to be blocky like Lego, and virtually all two-dimensional; now they are ultra-realistic – take the CGI (computer-generated imagery) scenes that pepper action movies, like Dune and Napoleon. When you boil it down, these CGI effects are really just computer game graphics spliced into digital films.

Because processing graphics involves making millions of small calculations simultaneously, graphics chips are designed differently to central processing units (CPUs). The CPU is the primary brain of a computer because it runs logically from the start of a process to the end (they run 'serially'). This is both helpful (programs can work without going haywire) and a drawback (like a sledgehammer cracking nuts one at a time, its computing power can be wasted because it can't do more than one thing at a time). Graphics processing units (GPUs), like those made by Nvidia, can spread their resources across many different tasks.

This ability to do many things at the same time makes GPUs perfect for AI. If you've read up on AI, you'll know that much of it is predicated on 'parallel processing' – on being able to run millions of calculations simultaneously. Nvidia's work on making ever smoother graphics led it to stumble onto helping drive what many people are calling the next technological leap of our species. Nvidia's GPU chips are the best in the market for data centres – the huge warehouses of computers that lend the power to develop and run AI programs.

We think the usage of AI will only increase, boosting demand for Nvidia's chips over the next decade, so we added Nvidia to our portfolio over the past two quarters. The stock is quite expensive – so we could lose money if sales growth moderates significantly because of missteps or competition – yet we believe Nvidia is well managed and has a strong head start.

Another new stock is LKQ, an American distributor of recycled auto parts. Half its business is in the US and the other half predominantly focused on Europe. It owns the Euro Car Parts brand, that you may see dotted around the UK. LKQ sells brand new car parts to retail and trade customers. And through its 170 dismantling facilities across North America and Europe, LKQ is the largest recycler of cars in the world. It strips around 800,000 vehicles each year, with almost nothing going to waste. Usable parts are cleaned up and repaired and sent on for resale, while metal, plastic and glass is sent to third-party recyclers. It's not just the parts, either, but the harmful liquid in old cars, such as transmission fluid, engine oil and battery acid. LKQ keeps these out of landfill as well. This isn't the glitziest of businesses. It's essentially a global chop shop – although this one operates completely above board. And that means reputable customers can get replacement parts at much better prices. Insurers, in particular, are willing customers. Repair costs for collisions have soared in recent years, LKQ offers a way to cut costs safely while also reducing the amount of waste that goes to the dump.

We added to our government bonds over the quarter because we felt 10-year yields north of 4% in the UK were a prudent long-term investment that should also protect our portfolios if stock markets drop markedly. Specifically, we bought the UK Treasury 0.625% 2025, 0.375% 2026, 0.875% 2033 and 1.5% 2053. We also bought some UK Index-Linked Treasury 0.75% 2034 because market expectations of inflation reduced significantly and these bonds should benefit if inflation overshoots. The capital and income from index-linked gilts ('linkers') rise with RPI inflation, which removes one of the key risks to a bond's return. However, you tend

to pay for that benefit through a higher upfront price or lower coupon payments. This also makes linkers even more sensitive to interest rate changes than conventional government bonds.

We bought a new diversifier to protect against the risk that US interest rates don't fall as fast as people hope. The BNP Paribas 10-Year US Rates Swaption May 2024 covers half the value of our US bond portfolio and makes money if 10-year yields rise. Usually, a swaption gives you the option to swap your fixed rate interest payments for floating ones; however, rather than giving us a series of floating cashflows into the future, ours is set up to simply pay us a lump sum when it's exercised. If rates remain flat or fall, all we lose is the small premium payment we made to buy the swaption.

We also added to our Put Options on the US stock market as the S&P 500 kept ripping higher. These work like portfolio insurance in that you pay a premium up front and receive protection if markets drop. They become cheaper to buy when volatility is low and more

expensive when it's high. The reason for this is that if volatility is high – if prices are yo-yoing all over the place – there's more chance that the option will be used, so it's more attractive. However, volatility isn't stagnant, so it's often best to buy insurance when the sun is shining, which is why we added to our put option exposure – stock market volatility has been low for several months.

Because we think central banks are now done raising rates, we continued buying assets that seem well priced for a coming period of falling bond yields and borrowing costs. Part of this shift is picking up infrastructure companies whose prices have been battered by increasing bond yields. These companies own the roads, railways, mobile data facilities, electricity networks and hospitals that we simply can't do without, recession or not. Some of them literally keep the lights on. We added to our holdings in HICL Infrastructure, The Renewables Infrastructure Group and International Public Partnerships, as their share prices are still trading well below the value of their assets less debts (at a 'discount').



SPOTLIGHT

IN THIS QUARTER, THE SPOTLIGHT IS ON OUR L'ORÉAL AND WASTE MANAGEMENT HOLDINGS.

L'ORÉAL



L'ORÉAL

- L'Oréal is the world largest cosmetics company, with a broad and balanced product portfolio across beauty, skincare, fragrances, and haircare. Its products include more budget labels like Garnier and CeraVe, and more premium names like YSL and Lancôme providing it with greater resilience than more niche players
- The skincare industry is booming as people of all ages – and all genders – spend more on looking after themselves. This is a truly global trend, and L'Oréal's sales are split almost equally across Europe, America, and Asia, so it's not dependent on any one region
- We believe its sales should be relatively resilient in a recession, as people tend to be reluctant to cut costs when it comes to what they are putting on the skin
- L'Oréal is the only company in the world to have achieved an 'A' score in all three CDP rankings (climate change, water and forests) for seven consecutive years
- As part of its 2030 L'Oréal for the Future' strategy, L'Oréal demonstrates ambitious sustainability objectives. For example, the company's emissions reductions targets cover all scopes, with additional targets specifically in place for the end use of products and strategic suppliers. Targets also cover key issues such as biodiversity, resource efficiency and water use
- L'Oréal has allocated €100m to an impact investing strategy dedicated to the regeneration of ecosystems and the development of the circular economy, and has created L'Oréal Fund for Women, a €50m charitable endowment fund to support on the ground organizations and local charities helping highly vulnerable women

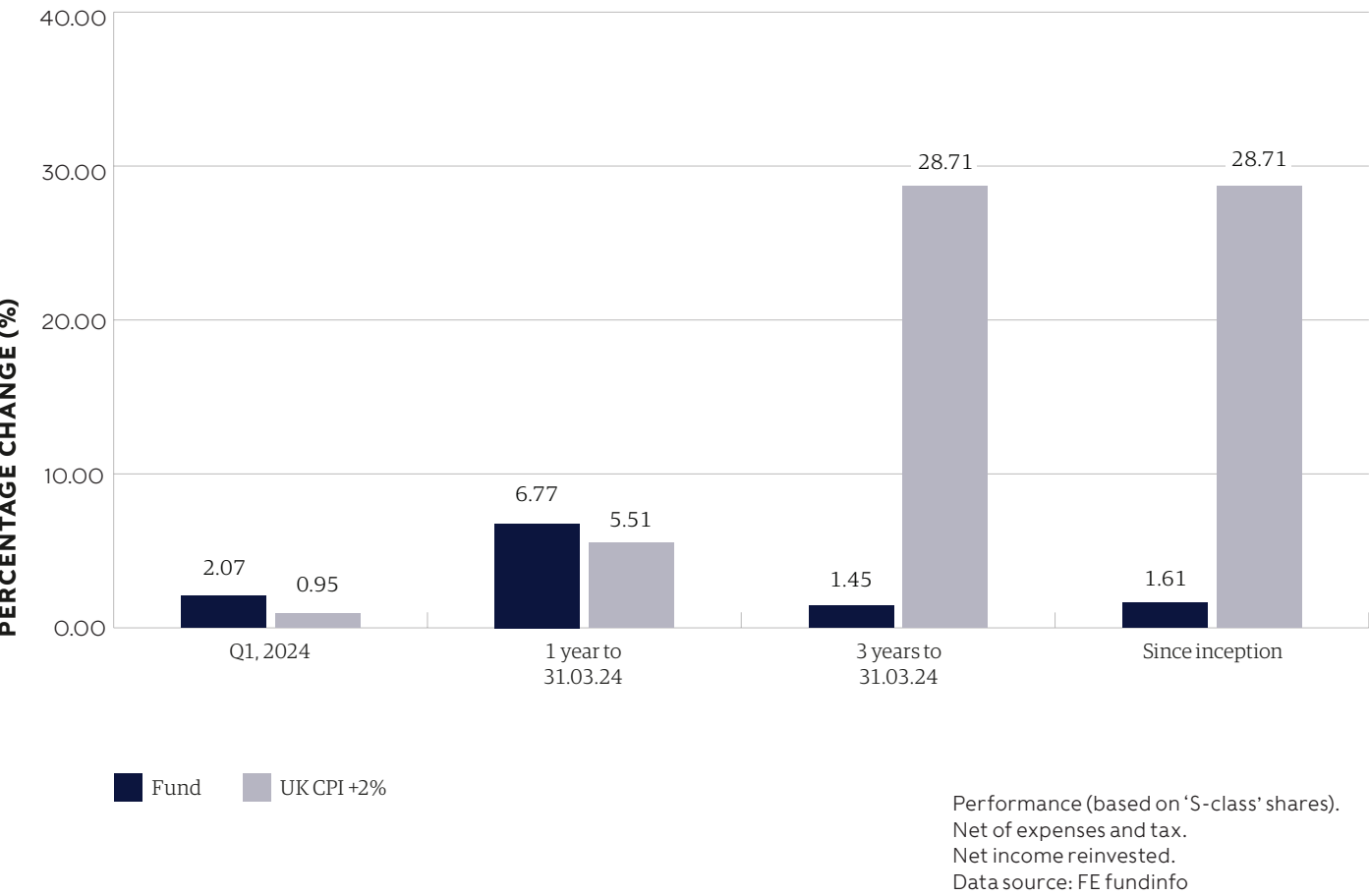
WASTE MANAGEMENT

- North America's leading provider of comprehensive waste management environmental services for residential, commercial, industrial and municipal customers through collection, landfill, transfer and recycling
- Collections operations are its largest revenue driver which involves picking up solid waste and recyclables from where they were generated and transporting them to a transfer station, material recovery facility (MRF), or landfill
- A very high proportion of their revenues are recurring, and they are the market leader with around 24% market share in what is a very fragmented industry, but one that tends to be more resilient during economic weakness
- Though recycling makes up a smaller part of Waste Management's total revenues right now, the company's long-term outlook to transition to a more circular business model could have a significant impact in the US market. It was the first major solid waste company to focus on residential single-stream recycling, which allows customers to mix recyclable paper, plastic, and glass in one bin. Residential single-stream programs have greatly increased recycling participation, resulting in increased volumes of recycled materials
- Waste Management claims that it avoids over three times the volume of its operational emissions through its waste recovery services and the company is investing over \$100m annually into new materials recovery technologies
- Over the medium-longer term, Waste Management's services are also crucial in helping promote a more circular economy, reduce waste and protect the environment which is of keen focus for companies and governments alike



FUND PERFORMANCE

RATHBONE GREENBANK DEFENSIVE GROWTH FUND — QUARTER 1 2024



12-month rolling performance					
Year to:	End Mar 2024	End Mar 2023	End Mar 2022	End Mar 2021	End Mar 2020
Fund	+6.77%	-6.74%	+1.89%	—	—
UK CPI +2%	+5.51%	+12.66%	+8.28%	+2.46%	+3.72%
Annual calendar performance					
Calendar year	2023	2022	2021	2020	2019
Fund	+5.85%	-12.23%	—	—	—
UK CPI +2%	+6.03%	+12.87%	+7.24%	+2.38%	+3.42%

Price performance based upon single price (mid).
Past performance should not be seen as an indication 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.

Top performers (%)			Bottom performers (%)		
Holding	Performance	Contribution	Holding	Performance	Contribution
Nvidia	+84.33	+0.29	AIA Group	-21.71	-0.17
TSMC	+32.45	+0.19	Adobe	-14.64	-0.09
Tomra Systems	+29.75	+0.08	Zoetis	-12.70	-0.05
ASML	+29.35	+0.21	Aptiv	-10.17	-0.05
Edwards Lifesciences	+26.40	+0.18	SSE	-9.95	-0.08

Note: Top and bottom performers are taken from the list of all holdings of 0.25% and above of the portfolio. Performance and contribution data shown above is based on unhedged GBP capital returns.

Source: Rathbones

Government bond yields rose in the first quarter, driving down their prices. Government bonds had rallied into year-end after the US Federal Reserve (Fed) seemed to imply that it could cut interest rates sooner than investors had been expecting. However, the strength of US economic data, combined with stickier inflation numbers, subsequently led the US central bank to adopt a more conservative tone and yields rose again. Higher bond yields proved a headwind to performance, reversing some of our gains from bonds over the previous three months.

We used first quarter weakness to add further to our UK government bonds. We continue to believe they offer attractive return potential after accounting for inflation and should also offset any equity market weakness in the event of a material economic downturn.

AI chip designer Nvidia was the most significant contributor to performance as the stock continued its meteoric rise into 2024. In late February, it again reported very strong earnings as data centre demand for its chips continued to soar off the back of burgeoning artificial intelligence demand. Nvidia's revenues jumped 265% from the previous quarter and the stock has rallied by 80% over the first three months. Other chip-related stocks,

such as ASML (which makes the machines that make chips) and Cadence Design Systems (whose software helps design and test chips), were also strong contributors to the portfolios.

Elsewhere in technology, Microsoft had another good quarter and broadly backed this up with strong earnings and a healthy outlook. The stock is a key competitor in the cloud space and is also perceived as a leader in AI development through its OpenAI partnership, helping to drive the stock to near its all-time high.

Stock markets have continued to move higher as investors have grown more confident about the chances of a soft, or at least softer, economic landing. That's helped support industrials such as Advanced Drainage Systems (manufacturer of drainage pipes) and Linde (industrial gases) which rallied sharply. Names such as payments business Mastercard and Canadian Pacific Kansas City (railroads) were also stronger off the back of a sunnier outlook for the US economy.

A key detractor from our performance for the quarter was Hong Kong insurer AIA whose share price fell by around 20%, dragged lower after its management warned about weaker profit margins in its China business.

ASSET ALLOCATION CHANGES

Asset allocation split	31.12.23	31.03.24	% Change	12 month change
Liquidity (5%-45%)	42.4%	42.0%	∨	-0.4%
Equity-type risk (30%-70%)	49.1%	49.8%	∧	0.7%
Diversifiers (0%-45%)	8.5%	8.2%	∨	-0.3%

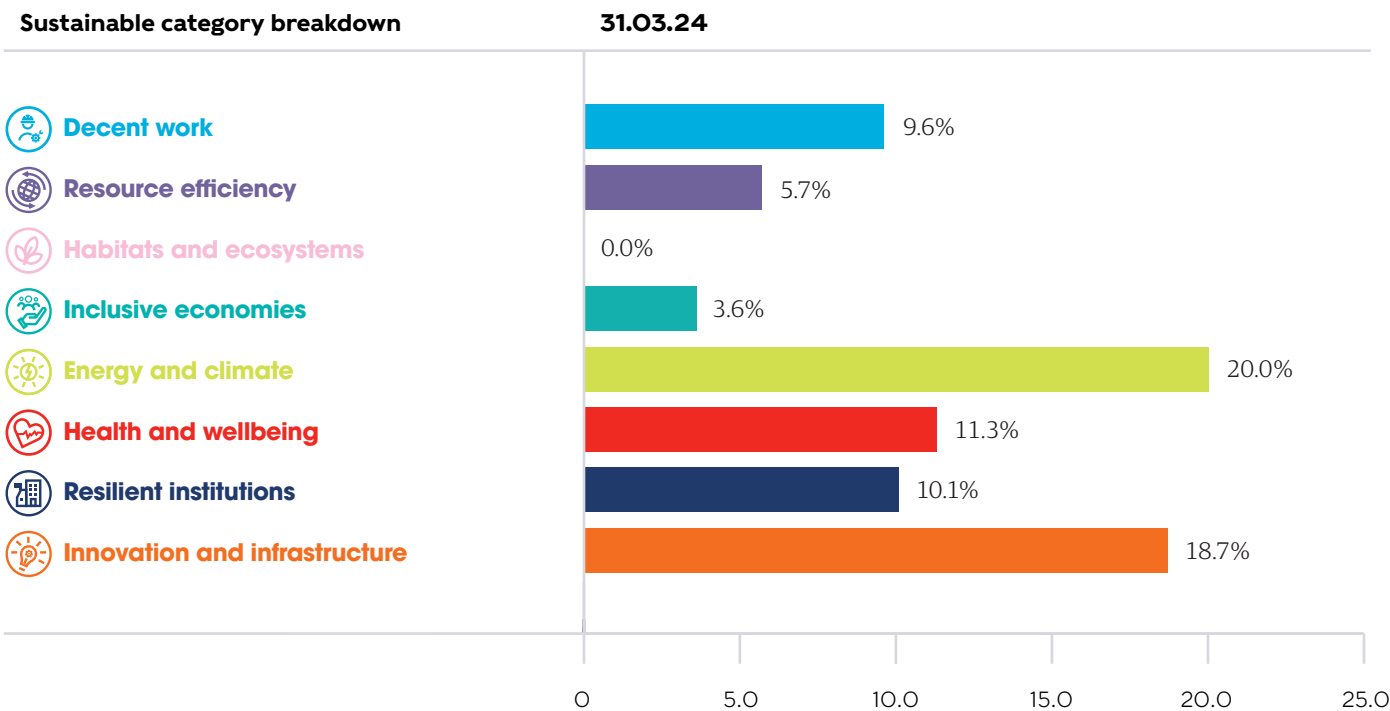
For more information on our liquidity, equity-type risk and diversifiers (LED) risk framework, please consult our investor brochure.

Asset class split	31.12.23	31.03.24	% Change	12 month change
Equities	42.1%	43.1%	∧	1.0%
UK	8.3%	9.8%		2.7%
US	22.9%	23.7%		1.8%
Europe	8.2%	7.1%		-1.2%
Japan	0.8%	0.5%		-0.6%
Asia ex-Japan	2.0%	2.1%		0.2%
Emerging Markets	0.0%	0.0%		0.0%
Global	0.0%	0.0%		0.0%
Index-linked bonds	1.5%	2.8%	∧	1.2%
Conventional government bonds	14.9%	15.6%	∧	0.7%
Corporate bonds	18.8%	16.9%	∨	-1.9%
Emerging market debt	0.0%	0.0%	<>	0.0%
Private equity	0.0%	0.0%	<>	0.0%
Alternative investment strategies	8.5%	8.2%	∨	-0.3%
Property	0.0%	0.0%	<>	0.0%
Infrastructure	0.5%	0.5%	<>	0.0%
Commodities	0.0%	0.0%	<>	0.0%
Cash	13.6%	12.8%	∨	-0.8%

SUSTAINABLE CATEGORY BREAKDOWN

GREENBANK HAS MAPPED THE UN SUSTAINABLE DEVELOPMENT GOALS (SDGS) TO A SET OF EIGHT SUSTAINABLE DEVELOPMENT CATEGORIES.

These categories ultimately align with the same ambitions as the SDGs but focus on the areas most relevant to companies and investors. Assets in the fund must align to at least one of these categories and the current breakdown of these alignment is shown below.



The 'resilient institutions' category includes government bonds.
For more information on our sustainability criteria, please consult [our sustainability process brochure](#).



INVESTMENT OUTLOOK

THE YEARS-LONG WAIT FOR AMERICAN RATE CUTS THAT REMAIN ALWAYS JUST OVER THE HORIZON REMIND US OF ASYMPTOTES: CONSTANTLY APPROACHING AND NEVER ARRIVING.

The last couple of months have done little to disabuse us of this notion. Businesses, households and investors are eagerly awaiting drops in benchmark rates, yet they keep floating on the horizon.

The big piece of the puzzle is inflation: will it continue to fall (we think it will), reassuring central banks that they can reduce borrowing costs without sparking another flare-up in prices? We have always suspected that the last mile of getting inflation back to 2% would be the hardest. And so it has been so far. To add another nuance to this point: all else equal, it's harder to get inflation lower when your economy is flying than when it's in the doldrums.

To avoid being burned by any shifts in expectations that arise as investors continually re-evaluate the likelihood of rate cuts and the strength of economies, we've continued trimming stocks whose valuations appear to have got a bit over-optimistic. We've used that money to add to equities and other assets that have fallen from favour. We don't want to sell outperforming businesses completely – lots of people want to buy them for a reason! – because over five years or more, we think they have the opportunity to grow well and become more valuable. Yet we try to minimise the short-term draughts that happen.

2% INFLATION

We have always suspected that the last mile of getting inflation back to normal would be the hardest.

WANT TO HEAR MORE FROM THE TEAM

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If there are any of the commentaries you require further clarification on, then please contact your advisers or Rathbones Asset Management (RAM) at the contact details contained on the RAM website.

Past performance should not be seen as an indication 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.

Any views and opinions are those of the investment manager, and coverage of any assets held must be taken in context of the constitution of the fund and in no way reflect an investment recommendation.

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