

RATHBONE GREENBANK GLOBAL SUSTAINABILITY FUND

QUARTERLY UPDATE SEPTEMBER 2024

After a long wait, global interest rates are finally falling in earnest. UK and US interest rates were cut this quarter, following falls in continental Europe and elsewhere a bit earlier in the year.

While the Bank of England made a typical cut of 0.25%, the first rate reduction by the US Federal Reserve (Fed) was a 'jumbo' cut of half a percentage point. The benchmark borrowing rates in both the UK and US are now 5.00%. Stock markets have gained considerably, both in anticipation of the cuts and afterwards as well. Although the headline numbers mask massive volatility throughout the year, with the largest falls coming in the summer.

In late July and early August investors had convinced themselves that the US economy might have been weakening so much that recession was in the offing. A couple of bad labour market releases triggered a substantial drop in American stocks that sparked a lightening fall in Japan, leading to more fears and more selling that spread to virtually all markets. Only a few days after all this kicked off, equity markets bounced back on the release of a contradictory jobs report (which showed jobless claims falling) and very positive services sector data. Since then, the US economy has chugged along well, while inflation has steadily fallen to 2.4%. This bolstered investor confidence in a 'soft landing' for the US economy. And that scenario is bullish for stocks: the summer stock market falls have since reversed completely. Both the FTSE World index of developed world stock markets and the US S&P 500 index hit new record highs.

The big question now is whether they can sustain the pretty sizeable gains they've chalked up so far this year. US political uncertainty looms large ahead of the 5 November election, while Labour's first Budget on 30 October could have big implications for companies and investors. There are also plenty of geopolitical tensions simmering away that could suddenly knock investor confidence and trigger bouts of market volatility.

We're quietly confident that global growth, driven by a robust American economy, can support stock markets and provide the environment for businesses to thrive.

Getting sensitive to interest rates

In July and August – ahead of the Fed's first rate cut – we bought two infrastructure companies that we felt should benefit from falling global interest rates. These types of businesses look a little like bonds: they pay out large amounts of cash today for land and equipment in return for a series of smaller ongoing cash payments from customers for many years into the future. And long-dated 'bonds' like these become more valuable when interest rates fall, as their (generally) fixed payments become more valuable in a world where you get less yield for each of your pounds (or dollars). On the flipside, bonds – and companies with similar payoffs – become less valuable when rates are expected to be higher. That's why infrastructure companies had a very tough time between 2022 and late 2023 as investors accepted that US rates would be much higher for much longer than expected. Also, infrastructure companies tend to have quite a bit of debt to finance their big upfront investments, so changes in financing costs can make a significant difference to the bottom line.

The first addition to our portfolio is **American Tower**, a company that builds, maintains and leases out mobile data towers to telcos and radio and TV companies. This is a well-run business that's produced consistent free cashflow (cash profits after day-to-day expenses and the costs of reinvesting in its towers and other assets) despite the big increase in interest payments over the last few years. Its return on equity is very high, averaging 39% over the past five years. This is an important metric for our investment process. With rates now falling as expected, this should create a double-strength tailwind for American Tower. If rates don't continue dropping, however, the stock could come under pressure.

Another infrastructure stock with a similar, bond-like payoff is **Hannon Armstrong**. We have added this specialist renewable energy investment business back into our portfolio, having held it previously between mid-2020 and early 2023. This company runs a wide range of projects, from energy efficiency to renewable energy and sustainable infrastructure. This year, Hannon has partnered with private equity company KKR to invest up to a combined \$2 billion in clean energy projects in the US over the next 18 months. This is a helpful way for Hannon to grow without tapping equity investors for more money, and it should flow through to increased earnings in coming years. If the world is to move from carbon-heavy energy systems to cleaner, renewable alternatives, a massive amount of new infrastructure needs to be built. Hannon focuses on delivering it.

Performance review

	3 months	6 months	1 year	3 years	5 years
Rathbone Greenbank Global Sustainability Fund	-2.8%	-2.6%	18.0%	-5.6%	43.8%
IA Global Sector	0.2%	0.9%	16.2%	14.1%	50.7%
FTSE World Index (GBP)	0.3%	2.9%	20.6%	31.2%	71.2%

	30 Sep 23-30 Sep 24	30 Sep 22-30 Sep 23	30 Sep 21-30 Sep 22	30 Sep 20-30 Sep 21	30 Sep 19-30 Sep 20
Rathbone Greenbank Global Sustainability Fund	18.0%	3.2%	-22.5%	22.3%	24.7%
IA Global Sector	16.2%	7.8%	-8.9%	23.2%	7.2%
FTSE World Index (GBP)	20.6%	12.2%	-3.0%	24.0%	5.2%

Source: FE Analytics; data to 30 September, S-class, mid price to mid price.

These figures refer to past performance, which isn't a reliable indicator of future returns.

Making a few slight adjustments

To fund these purchases, we made a few sales over the quarter. We sold Germany's **Sartorius Stedim Biotech**, which helps companies develop drugs. While this is an attractive industry, with strong demand for drug production services, there's a capacity overhang from the COVID-19 pandemic that is affecting Sartorius more than drug development peers such as **ThermoFisher Scientific** (which we own and added to over the quarter) and Danaher (which we don't). Massive efforts were made to boost vaccine production to fight the illness, but that inevitably left excess stock and underutilised laboratories afterwards. While this overhang is shrinking, a catalyst for Sartorius's improvement isn't visible right now, so we think there are better opportunities elsewhere.

We also exited diabetes monitoring business **Dexcom**. An unexpected market update in July revealed issues with the reorganisation of its salesforce. Demand for the company's glucose monitoring equipment had been growing strongly and we had anticipated it would continue for several years or more. The sales team changes significantly hurt order flow and led to loss of market share. We were concerned that there were no short-term fixes to this issue and didn't agree with the business's explanation that it will be an isolated profit problem.

Over the quarter, we used market dips and spikes to add to and trim our existing holdings.

We added to vehicle electrification supplier **Aptiv**, which makes the sensors, wiring and safety measures that go in all types of car. Cars have become vastly more complex since the roll-down windows and manual chokes of yesteryear. Electrical components are doing these jobs – and also automatically calibrating engines and tyres and other parts of the car as we drive. All in the pursuit of making the journey more energy-efficient and comfortable. Aptiv isn't tied to any one type or brand of vehicle, which we see as a massive plus: this makes it less susceptible

to the failure of a single customer. Aptiv's share price is trading at a large discount both to the wider US stock market and to where it has typically traded in the past. Its price is roughly 9x the profits analysts forecast for next year; the S&P 500 average is almost 22x.

This depressed mood could be because the take-up of electric cars has undershot expectations in the past couple of years, particularly in the US. However, it's important to remember that Aptiv products are suitable for all car types, regardless of what fuels their engines, so this should be less of an issue that you might think. Aptiv's leaders share our optimism about the company's long-term prospects: they've announced the business will buy back more than a fifth of its outstanding shares. All else being equal, share buybacks boost the value of the remaining shares as the same business's profits are spread across fewer owners.

We trimmed our holding in smart-grid designer **Schneider Electric** after it posted strong share price performance in the past year, to the point where its valuation looked a little full. We believe Schneider is well positioned to benefit from sustained global investment in electrification and power supply. The outlook for Schneider's profit growth in next few years looks strong to us.

Another slight reduction was in UK household brands business **Unilever**. We bought a significant position in Unilever earlier this year because we felt that there was a substantial change in strategy under way. The board had decided to slim down the number of products and brands that it holds to sharpen its focus and increase sales. This meant reorganising the business into new business groups and preparing for the sale of unwanted brands. Unilever's managers have delivered on this so far – a £15 billion spin-off for its ice cream brands is in the works – and the shares have performed very well so far this year. We're very confident in the continued improvement of this iconic British business, but we think it's prudent to take some profits after a strong run.

**BIDEN CONSTRUCTION BOOM HAS BENEFITED
ADVANCED DRAINAGE SYSTEMS**



Source: US Census Bureau, St Louis Fed; monthly spending on all US construction

Finally, we pruned our holding of US stormwater pipe supplier **Advanced Drainage Systems (ADS)** ahead of its August results. Its share price has been trading at all-time highs after several bumper years driven by American government spending on infrastructure. With an election in the offing, we're unsure whether this public spending will continue into the coming years, so we thought it was a good time to take profits. Longer term, we remain happy holders. ADS is expanding into sustainable building products to widen its product range and diversify its sales drivers to make it less dependent on highway and drainage projects. We think this is a sound strategy, which appears to be progressing well



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For more info on our fund, including factsheets, performance and fund manager views, please click [here](#).

If you require further clarification on this commentary, then please contact your adviser or Rathbones at the contact details below.

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. 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 what you originally invested.

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