



FOREWORD

Dear Reader/client,

Half-way through 2021 and the pandemic – certainly in the UK – seems to have entered a new phase. The delta strain is causing new cases to rise considerably, but not hospitalisations. How policymakers deal with this remains to be seen, but at the moment, it seems that re-opening of our economies will continue as planned.

Economic sentiment has rebounded sharply and equities have continued their long rally. Underneath the hood there have been sharp variations between the value and growth styles indicating it is not all plain sailing.

Faster economic growth expectations have brought with them increased concerns about higher inflation and tighter monetary policy. We continue to believe that such concerns should ease in time. Nonetheless as the COVID-19 recovery matures, we need to be mindful of the risk that either growth disappoints, or central banks may be pressed quickly into action.

Our investment style has held up well as we pick stocks which have structural growth drivers and can pass through price increases. Whilst maintaining our positive outlook, our strategists and portfolio managers are bringing some caution to portfolio positioning.

We hope you enjoy reading about this in further detail and wish you some relaxing time over the summer.

Richard Brass

Head of Wealth & Asset Management, UK

ADVISORY

IN A NUTSHELL

- Mixed market sentiment continues despite rising inflationary concerns.
- High proportion of US and UK population have been vaccinated and lockdowns are gradually easing.
- Reduced risk with sale of Talanx and trimming of Whitbread.

Overview

Despite rapid vaccinations, the emergence of the delta variant has imposed concerns of infection rates once more. Compounded with this, pent up demand and spending is evident with the easing of lockdown restrictions driving inflation and therefore giving rise to concerns of interest rate hikes sooner than initially expected.

With this in mind, growth stocks have lagged during this period as their future cashflows are more tilted towards the long end and will be worth less in Net Present Value terms if interest rates were to rise. Our portfolio holdings at large have lower valuations, reasonable organic growth rates of up to 10% and strong pricing power. Hence, we believe we are well positioned even if inflationary concerns will materialise in the future.

Despite the risk of interest rates rising, we believe with the emergence of new variants and the position of Central Banks generally allowing economies to run above inflation for a short period of time, the concern of interest rate hikes may be premature/overdone. With this in mind, we saw an opportunity to crystallise the position in **Talanx**. The stock has rallied over 30% since our purchase in October 2020. With rising inflationary concerns and subsequently higher yields, its investment portfolio may suffer in the short term.

Furthermore, we believe optimism around lockdown easing could be excessive given travel restrictions for holidaymakers (particularly for short city breaks) and potentially subdued business travel for a longer period of time. As a result, we believe **Whitbread** will suffer from lower bookings than hoped in the latter half of the year. With this in mind, we halved the position in the company.

Tomra had performed strongly over the quarter rising 28.6% in light of its strong order intake, alongside **AstraZeneca** (AZN) which had recovered from headwinds concerning the rare cases



of blood clots from its COVID-19 vaccine and progress in its oncology and Cardiovascular, Renal and Metabolism ("CVRM") division. Furthermore, AZN has received approval from all important regulators for the USD 39bn takeover of Alexion.

THEMATICS

As indicated in our initial Quarterly Review, every quarter we discuss a key topic within one of the four core themes¹ to raise the awareness of them and display how these trends feed into our stock selection. For this quarter we delve into the theme of Demographic Change, namely the trend of urbanisation.

Urbanisation shapes societies and economies ...

Today, more than half of the world's population reside in urban areas. As a result, cities grow larger and become more densely populated. While Tokyo is the largest city with more than 37m dwellers, Dhaka is the most densely populated city with 44,500 people/m² (to compare the UK has a population of 68m people and a population density of 275 people/m²).

As people move into cities, it not only changes the general urban appearance, but it also affects the way we live, consume, work and/or commute. Some studies show that urbanisation is likely to stimulate both innovation and economic growth. As cities grow larger in terms of height and area, connectivity and transportation become critical elements in urban planning.

... with differences across regions ...

Countries across Asia, Latin America and Africa have experienced the highest growth rates in terms of urban population. In Asia, the percentage of people residing in urban areas has increased from 17.5% in 1950 to 51.1% in 2020 and is projected to reach 66.1% by 2050. In comparison, the urban population in North America has grown at a substantially slower pace due to its higher base level, being 63.9% in 1950 and 82.6% in 2020.

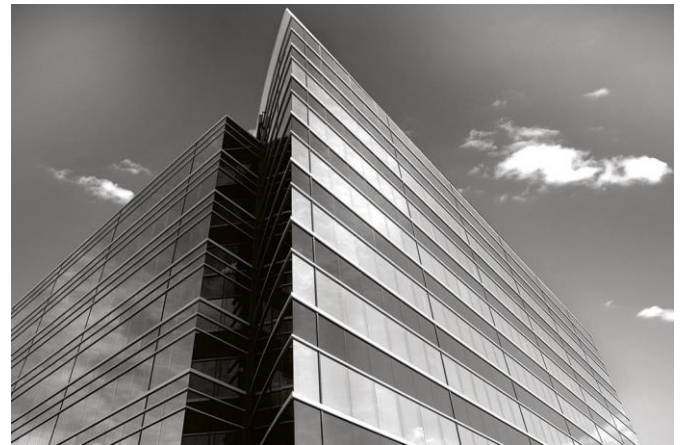
... attributable to natural population increase, migration, urban sprawl

Urbanisation is broadly driven by three key factors. Firstly, urban population may rise due to a higher growth rate of the incumbent urban population as a result of longevity. Better access to health care systems tends to result in lower mortality rates in urban

areas. Provided that births exceed deaths, and birth rates exceed mortality rates, this will cause a natural increase in urban population.

Secondly, migration plays an important role. People seeking higher job salaries or better education tend to reside in cities.

Finally, urban sprawl captures a higher number of people thus increasing the urban population. It is often observed that fast-growing cities incorporate adjacent areas and their populations in the course of urban growth.



Urbanisation: moving into cities – Otis: moving within cities

We believe that **OTIS Worldwide**, the world's largest elevator and escalator manufacturer, will be a key beneficiary of the urbanisation theme. In providing buildings and outdoor spaces with both elevator and escalator maintenance and installation, OTIS moves 2 billion people in more than 200 countries a day. Famous projects include the Shanghai World Financial Centre, Christ the Redeemer, Bahrain World Trade Centre, Empire State Building, Eiffel Tower, Abu Dhabi Airport and Lotte World Tower.²

OTIS is a truly global company and the largest player in the elevator OEM industry, followed by Schindler and Kone (the Big Three listed companies). Given the strong market position (15% market share), OTIS may significantly benefit from organic market growth. Urbanisation and sustainability are likely to be the key drivers of future market growth in the elevator space.

¹ (i) Demographic change (ii) Innovative and disruptive technologies (iii) New energy and resource management (iv) Future health and wellness

² <https://www.otis.com/en/vn/our-company/global-projects/project-showcase>



... providing smart and innovative solutions.

The trend towards more sustainable cities and communities (SDG 11) requires cities to take into account factors related to energy efficiency and connectivity. OTIS is known for its innovation capabilities and has been at the forefront of sustainable technology and resource efficiency. Innovative solutions enable the company to operate elevators, which consume 75% less energy than conventional systems.³ In addition, the company's aspiration to deploy artificial intelligence and the internet of things contributes to making cities smarter and more efficient.

Long-term growth prospects paired with strong financials.

Taking a closer look at OTIS' financials suggests that the company is well positioned for sustainable future growth. The quality of the firm's business model and balance sheet have proven remarkably strong after last year's COVID-19 acid test. While sales have declined by only 2.8% in 2020, a relatively strong net income result of USD 1.1bn has been reported. In addition, Free Cashflow yield was 3.9% in 2020 and an increase in capital expenditures is representative of the firm's growth strategy.

The world of tomorrow: urban, sustainable and connected.

Urbanisation changes how people work and live. The world is becoming faster, smarter and taller. As a result, innovative and eco-friendly connectivity solutions play a vital role in modern societies. Moving people over long distances, both vertically and horizontally, ensures the frictionless functioning of urban life. OTIS provides innovative, smart and sustainable solutions all over the world. As OTIS has a strong market position in a market with significant growth potential, we believe that it is an attractive long-term urbanisation play.

³ <https://www.otis.com/en/us/our-company/sustainability>



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As of: June 2021