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UK Mid Cap strategy

Growing evidence of corporate cashflows being used to repay government financial support

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- Stock picking was the main driver of outperformance
- A new position in Secro was initiated

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What's happening?

Global equities were up in July in local-currency terms, but down in sterling due to the relative strength of the pound. Growth continued to outperform value in all major markets, most notably in the UK. Businesses with strong balance sheets and good cashflow conversion have continue to perform well.

Coronavirus infections continue to rise globally, causing unease. In the UK, the government imposed restrictions in areas of the country where new cases were rapidly increasing, as well as pausing lockdown easing in England. A localised approach in dealing with spikes of new cases has been adopted by many countries in an attempt to reduce disruption on broader population and economy. Support from governments and central banks continues to be supportive, remaining crucial for a recovery.

Tensions between China and the US and UK continued to increase over the month. The US confirmed that Hong Kong had lost favoured trading status. With the UK suggesting the removal of Chinese firm Huawei Technologies' from its 5G network. Gold, often considered a safe-haven investment in times of uncertainty, saw spot prices hit a record high during the month.

Portfolio positioning and performance

The UK Mid Cap strategy outperformed the FTSE 250 Index, which fell in July. Stock picking was the main driver of outperformance, most notably in the Consumer Services sector. The strategy's overweight in the Technology sector contributed positively to outperforms, whilst the underweight to the Basic Materials and Utilities sectors detracted from performance.

The strategy benefited from its positions Pets At home, a pet supplies retailer, Ultra Electronics, specialist in providing application-engineered bespoke solutions, and Spirent Communications, a specialist in telecommunications testing systems, including computer software and hardware systems, cable management systems, and transmitters. Pets at Home's share price rose on news that demand for pet ownership had increased after the coronavirus lockdown, a good indication of long term growth in the market. Detractors on a relative basis included Boohoo and Centrica.

In July, a new position in Serco, a company who specialise in outsourcing of public services, was initiated. The position in SSP, an operator of food and beverage outlets in travel locations, was sold.

Outlook

The equity market is likely to remain volatile as the forces of Central Bank stimulus, Government support and the economic impact of increasing or decreasing Covid-19 cases battle for supremacy.

UK economic output should improve, provided businesses continue to reopen and welcome back furloughed staff. As ever, there will be winners and losers as the long term changes to individual behaviours impose themselves.

We are encouraged by the operational updates of UK listed businesses, many of which are reporting trading ahead of expectations set in March and April. There is growing evidence of corporate cashflows being used to repay government financial support and this bodes well for the potential reintroduction of dividend payments.

We remain focused on UK and internationally-exposed businesses, where the fundamental profit drivers remain entrenched and equity holders benefit from the capital allocated and risks taken by management. We continue to believe that a rewarding strategy is to actively invest in UK-listed companies that are compounding their earnings and dividends, where corporate governance is world leading, where contract law and title law are dependable, and where company management teams are permanently accessible.

No assurance can be given that the UK Mid Cap Strategy will be successful. Investors can lose some or all of their capital invested. The UK Mid Cap strategy is subject to risks including; Equity; Smaller companies risk; Liquidity risk.

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