RATHBONE GREENBANK DYNAMIC GROWTH PORTFOLIO

MONTHLY UPDATE MAY 2024

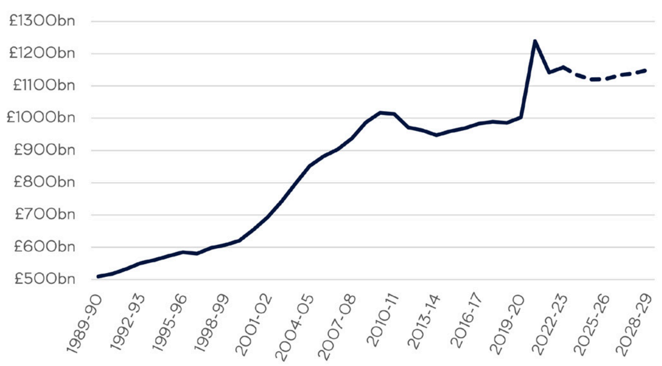
UK Prime Minister Rishi Sunak has rolled the dice, calling a snap summer election. As the dice and the politicians tumble across the land, we're faced with the question: does it matter?

Britain has emerged from a short and shallow recession with reasonable GDP growth. Inflation — while erratic — is trending downwards, albeit services prices remain elevated (see chart on next page). The housing market is holding up ok despite multi-decade-high interest rates. For all the energetic campaigning, the economic policies of both sides are very similar. Labour has mostly signed up to the Conservatives' fiscal rules, has also ruled out hikes in VAT, income tax and national insurance and greater borrowing, and refused to discuss even a partial reversal of Brexit. That doesn't leave much room for changing the nation's course!

The die is cast

The way we see it, something has to give. Whoever wins the election will have to either break at least one of these promises or preside over a substantial slump in public services, continued middling growth (or worse), or both. Exactly which promises are broken (or bent) and when is hard to say. But there are politically difficult spending cuts pencilled in for the next few years that may force the issue (see chart). So we don't expect the election to deliver a sea change in the UK's short to medium term prospects, regardless of who wins.

FORECAST WHITEHALL SPENDING CUTS UNLIKELY



Source: Office for Budget Responsibility, Rathbones; inflation adjusted government spending

Changes to the UK's byzantine and unpredictable planning laws are on the agenda of both major parties. It's a serious problem that needs addressing. Anyone hoping to build or invest in the country often feels like they're paying huge amounts to play at a depressing game of craps with loaded dice. No wonder investment in the UK has been depressed for years! Yet this will take time to investigate and reform — years probably.

One thing that could help the UK would be a closer relationship with the EU, our largest trading partner. Labour has said that it wants to renegotiate the bare bones deal agreed by the government, so if Labour does win and the cross-channel dialogue improves, that may help global investors get back on board with the UK. However, the straitjacket seems to remain here as well: Labour has ruled out joining the customs union or revisiting Brexit, so it's hard to see really needle-moving changes here either. And yet. There's been quite an entente forming of late between Labour leader Keir Starmer and the EU top brass. There's a review and option for renegotiation set for the fifth anniversary of the Brexit agreement in 2025. Perhaps some trade consultants do a review. Perhaps they find shortcomings. Perhaps those shortcomings are addressed — but that's not reversing Brexit, that's just a *review*. Yes, we're into semantics, but this is politics we're talking about. Messages matter.

So if Labour does win (which we think is fair to assume, given its huge lead in the polls), it will have to break its campaign promises at some point. We hope that it has learned the lessons of the past and doesn't break its word on borrowing. We hope that Labour understands that it can't just raise debt aggressively, otherwise it could upend the government bond market like the short-lived Truss-Kwarteng government did back in 2022. We imagine it will have to raise taxes (probably through some sort of indirect wealth taxes, say capital gains or a second home tax) and curtail any big spending projects. But if it can thrash out a better trading relationship with Europe without re-tabling the Brexit arguments that stupefied the nation for the best part of a decade, that could boost trade between the two, improve productivity and help increase economic growth and therefore tax revenue. That would be a step in the right direction …

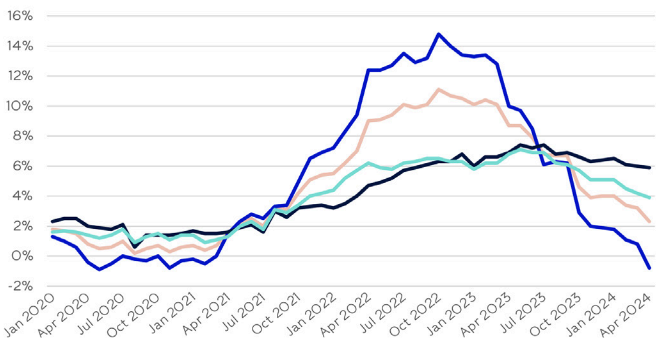
How hot will summer be?

With the election due to be done and dusted by early July, the path would open for the Bank of England (BoE) to cut interest rates (as long as inflation plays ball). While the April inflation figures undershot expectations, it was still a sizeable drop on the previous month with more to come. We concur with the market expectation that the BoE will follow the European Central Bank's footsteps and cut before the US Federal Reserve.

The US economy is slowing, but it still seems a bit hot for the Fed to pull the trigger. Especially with a tightly contested presidential campaign running until November (moving rates in the run-up to an election often attracts accusations of political interference). Headline CPI inflation has been disappointingly high over the past few months, yet the last two PCE inflation releases were in line or below economists' forecasts, with personal spending coming in below expectations. Indeed, some company management teams seem to be guiding expectations lower in recent earnings calls. We're very far away from earnings cratering, yet we think businesses are telling us things are slowing a little. If the US economic picture continues to weaken over the summer, it seems like the sort of environment that would allow a cut perhaps a few days after the election in November or in December.

Here in the UK, markets forecast a quarter-percentage-point cut won't arrive till September or November. Yet that will heavily depend on how inflation tracks over the summer — keep a close eye on the all-important services inflation component (businesses that tend to be labour-intensive, like cafes, travel businesses, accountants, etc). Expect UK bond yields to bounce around like a beachball in a crosswind, which isn't exactly a change on the recent situation!

UK INFLATION FALLS PAVE WAY FOR RATE CUTS, DESPITE STILL-STRONG SERVICES



Services inflation | CPI Inflation | CPI core (excl energy, food) | Goods inflation

Source: Office for National Statistics, Rathbones

This month we took the opportunity to trim our holding in high-end computer chip designer **Nvidia**, which has done well lately. We also took the chance to add to some of our stocks that were weak after recent earnings releases. These included fire safety and air conditioning business **Johnson Controls**, customer relationship management (CRM) designer **Salesforce**, digital payment business **Mastercard** and e-commerce platform **Shopify**.

DAVID COOMBS
Head of Multi-Asset Investments

WILL MCINTOSH-WHYTE
Fund Manager

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.

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Rathbones Asset Management

8 Finsbury Circus
London EC2M 7AZ
+44 (0)20 7399 0000
Information line:
+44 (0)20 7399 0399
ram@rathbones.com
rathbonesam.com