Marlborough Multi-Cap Growth: COVID-19 investment update

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Richard Hallett

Marlborough Multi-Cap Growth Fund Manager Richard Hallett explains how he has reacted to the market volatility caused by the COVID-19 outbreak and where he has been identifying opportunities.

How have you responded to the sharp market falls caused by the COVID-19 outbreak?

"What we've done is to look carefully at the companies in our portfolio and ask whether anything's changed about the characteristics that made us invest in the first place.

"We have a pretty demanding set of criteria when we're selecting stocks for the fund. We look for companies that have a sustainable competitive advantage, that are leaders in a niche business area with few competitors and that are benefiting from an established long-term structural growth trend.

"So, we've looked at each of our holdings, considering a number of key points such as whether the company's competitive position has changed and if the underlying growth trend we originally identified remains as strong as ever.

"In a number of cases, that trend is actually stronger. For example, several of the technology trends we like, such as the growth of ecommerce and the increasing use of cloud computing services, have been accelerated by the lockdown.

"Relatively early on in the crisis we took advantage of the volatility to gradually add to our positions in Amazon and Microsoft. With shops closed and restrictions on movement, Amazon is reaping the benefits and has said it will be recruiting another 175,000 warehouse and logistics staff, mainly in the US.

"Microsoft is benefiting from the huge increase in people working from home, which is driving a greater demand for its cloud-based business software services for things like video conferences and remote collaborative working. In addition to its strength as an ecommerce juggernaut, Amazon is a leading player in cloud-based services too, so it's also benefiting from the increase in remote working.

"With the increased popularity of ecommerce and cloud-based business services, we believe that changes in behaviour caused by the pandemic aren't merely providing short-term boosts, rather we're seeing the acceleration of what were already powerful long-term structural trends."

Looking beyond technology, what has been the impact on companies you hold in other sectors?

"In other sectors, there will be no escaping short-term pain, but robust companies, with a healthy balance sheet and a strong competitive edge, are likely to weather the storm. As competitors flounder, these companies should emerge in good shape, with some benefiting from a greater demand than ever for their products and services.

"A good example is Rentokil Initial, one of our holdings, which is one of the world's leading commercial hygiene services provider. When businesses begin to return to normality, we anticipate a greater focus, and increased spending, on hygiene and pest control, with Rentokil well positioned to reap the benefits.

"The disruption brought by COVID-19 is also likely to mean changes to supply chains, as companies seek to avoid any repeat of the impact of China's shutdown. This repositioning will, we believe, be good news for another of our holdings, Intertek, a global leader in the testing of products and services, which can assess whether potential new suppliers meet quality benchmarks.

"It may seem counterintuitive, but we've added to our position in Dart Group, which owns airline and package holiday business Jet2.com. The company's done incredibly well for many years, but has, of course, been hugely impacted by the pandemic, with all its flights suspended.

"What we like about Dart Group is that it has one of the strongest balance sheets in the travel sector. It's been managed conservatively with an aversion to debt, while its main competitors are heavily leveraged. So, we believe it's going to emerge stronger than its rivals and ready for robust growth, albeit with more debt than in the past.

"Generally, we've taken advantage of price weakness to add to companies in the portfolio. We have though top-sliced our holdings in the London Stock Exchange and Genus, which is a global supplier of high-quality agricultural breeding stock. That's because these two companies held up so well while other stocks sold off. In both cases they'd grown to more than 4.5% of the overall portfolio, which is the ceiling we tend to apply to avoid over-concentration.

"We've also sold out of Marshalls, which supplies paving products to the building industry. It's a good-quality company, but we'd bought it as tactical play based on an increase in construction work after the decisive UK general election result. In light of the virus outbreak and its impact, we decided the capital could be deployed more effectively elsewhere."

The fund's name and objectives have been changed. Why was that and has it made a difference during the recent volatility?

"At the beginning of March we dropped 'UK' from the fund name and updated the investment objectives to broaden its geographical scope. So, while we're still primarily a UK fund, we're now free to invest up to 20% of the portfolio in overseas companies.

"Investors won't see major changes - we're not rushing to rebalance and put 20% into overseas stocks. Rather it's an additional freedom that we'll be able to exercise when, as time goes by, the right opportunities arise that fit with our very demanding investment process.

"What it's meant is that we've been able to gradually build positions in Amazon and Microsoft and add to them when markets sold off at the beginning of the crisis. Previously we were restricted to UK stocks, so, even though these two companies are very strong leaders in tech sectors we like, we weren't able to hold them. We believe the increased freedom we now have is a strong positive for the fund and its investors."

How would you summarise the investment outlook?

"Plainly these are challenging times for many companies, with crisis measures that have almost entirely halted trading in sectors such as travel, leisure and some areas of retail. We've already had companies like Carluccio's, Warehouse and Debenhams calling in the administrators and I think it's inevitable that we'll see others flounder too.

"On the other hand though, there are robust companies that will emerge stronger than before, with competitors weakened or gone altogether. At the same time, equity markets have fallen a long way and plenty of quality companies now look much better value than they did in January. In many cases, the fall in a company's share price appears to have gone beyond what can reasonably be expected to be the hit to their earnings.

"The difficulty in quantifying that blow to earnings is one factor weighing heavily on markets, as uncertainty reigns about the economic impact of the crisis. There are concerns too about whether the experience will change consumer behaviour for the long term, affecting spending on things like restaurants and travel.

"It's worth remembering though that normal life and business aren't over, they've merely been suspended for a time, and steep share price falls have created attractive opportunities for the patient investor."

Risk Warnings

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Investment in the Company should only be undertaken as part of a diversified investment portfolio.
Investment in the Shares should be viewed as a medium to long term investment.
Shares may not be redeemed other than on any Dealing Day.
There will not be any secondary market in the shares of the Company.
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