RESPONSIBLE AND SUSTAINABLE UK EQUITY FUND

COMMENTARY FOR QUARTER TO END SEPTEMBER 2022

PERFORMANCE

	3 Months	6 Months	1 Year	3 Years	5 Years	10 Years
Fund Performance (B Class)	-7.3%	-17.0%	-26.5%	-13.5%	-10.1%	51.4%
FTSE AllShare TR GBP	-3.4%	-8.3%	-4.0%	2.4%	11.3%	79.5%
IA UK All Companies	-5.0%	-12.9%	-15.5%	-2.6%	2.9%	73.1%
Sector Quartile	4	4	4	4	4	4

Source: Morningstar. Figures compared on a Bid to Bid basis with Net Income Reinvested.

REVIEW

The UK stock market performed poorly in the quarter largely due to recessionary fears, interest rate increases and falling consumer confidence. The US market also performed poorly reflecting the increasing determination of the Federal Reserve to tackle persistent inflation. The conflict in Ukraine has continued and has seen Russia not restart gas flows through a critical pipeline to Europe, which has contributed to higher commodity prices, and fed into cost of living pressures. The Federal Reserve increased the federal funds rate by 0.75% to a target rate of 3.0-3.25% and all signs point to further rate increases in order to tackle inflation.

Boris Johnson resigned as Prime Minister following various scandals and resignations from his government and was replaced by Liz Truss. The mini-Budget saw the new UK chancellor Kwasi Kwarteng unveil an energy package which would cap energy costs for customers and businesses as well as a series of tax cutting measures funded by increased borrowing. Sterling fell against the US dollar and gilt yields rose sharply as investors reacted negatively to scale of the increased borrowing. The Bank of England voted to raise interest rates by 0.5% to 2.25% although there was a three-way split with three members voting for a larger 0.75% increase and one member voting for a 0.25% increase. The Bank of England also pledged to buy £65bn of long dated bonds in an attempt to stabilise the gilt markets which was negatively impacting pension funds. All the UK indices were in negative territory in the quarter.

Elsewhere, the Brent Crude oil price decreased to below $90 in the quarter largely due to persistent demand fears. The European Central Bank raised interest rates to 1.25% in order to tackle inflation which was unanimously backed by all 25 members of the governing council. The President of the European Central Bank (ECB), Christine Lagarde signalled for several interest rate rises in the coming months.

PERFORMANCE & ACTIVITY

Against a volatile backdrop, the Fund lost ground in absolute and relative terms during the quarter. Stock returns across the market continued to be dominated by macro-economic and geopolitical considerations which have created a great deal of uncertainty for short term corporate earnings but also some exciting valuations for companies with strong and growing market positions, including innovative businesses with leading technology, products or operations that are hard to replicate, providing strong economic moats.

Nevertheless, it has been another difficult quarter for the Fund and, more broadly, a torrid year for our investment approach, which tends to have a quality growth focus with a blend of UK domestic and multinational companies. Fossil fuel companies, which we obviously don’t hold, and large companies whose revenues are in dollars, have dominated – and distorted – the returns of the FTSE All Share Index this year. This is shown starkly by the divergent performances of the FTSE100 and the more domestically focused FTSE 250 indices which has returned -3.8% and -25.3% year-to-date. The FTSE 250 is therefore in bear market territory and has suffered a similar decline as major stock indices in the US, Europe and many other parts of the world. Similarly, there has been a marked divergence in the performance of global growth and quality indices, areas in which we tend to invest, and value this year.

While we are disappointed by the Fund’s recent performance, we are confident about portfolio positioning and remain extremely close to the companies in which we invest. Moreover, times such as we are seeing now when the market is ultra-focused on short-term earnings can create exciting opportunities to investors such as ourselves who appraise corporate prospects on a three-to-five-year horizon, a period over which the true value of a business can be realised.

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With this in mind, we started positions in NextEnergy Solar, Diploma, Intertek, Morgan Advanced Materials, Unite, Segro, NatWest, Convatec, Spirax-Sarco, Bluefield Solar and Harmony Energy and added to positions in Porvair, London Stock Exchange, Close Brothers, Phoenix, Mears and UK Wind. We reduced our position in AstraZenca and sold out of Trifast, IP Group and Fevertree..

At a stock level, NCC (Technology) and Wise (Technology) were amongst the biggest contributors to performance whilst detractors included Hotel Chocolat (Consumer Staples), Dechra (Pharmaceuticals) and Sabre Insurance (Insurance).

OUTLOOK

The continuation of the conflict in Ukraine will likely see continued high commodity prices, high inflation and increasing recessionary fears. President Xi is likely to obtain a third term in China and his policy direction will likely have a big impact on global economic growth. Mistrust still exists between the UK and EU, largely over the Northern Ireland protocol, although relations have warmed somewhat under new Prime Minister Liz Truss. The UK government's energy price support package will help in partially mitigating the increase in the cost of living but negative implications on consumer spending are still likely. Conservative Party infighting over certain aspects of government policy could result in elevated political risk. Labour disputes are likely to be a feature going forward as wage increases fail to keep pace with inflation and disputes could spread across more industries.

European economic activity is likely to be impacted by its proximity to the conflict in Ukraine. President Biden will face mid-term elections, buoyed by his recent legislative successes, and the outcome of these elections and whether the Democrats continue to control both houses of Congress, will shape the rest of President Biden's first term. Central bankers around the world have continued to increase interest rates in order to combat inflation and the economic impact of less accommodative monetary policy could be painful. While, as ever, some political and economic risks lie ahead, we remain focused on finding new opportunities in companies that meet our strict criteria of strong earnings growth, high margins and strong cash flows.

To obtain further information please speak to your normal EdenTree representative, visit **www.edentreeim.com** or call our support team on **0800 011 3821**

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