Comment

The next secular growth story

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Tech has beaten every other sector hands-down in both up and down markets, but nothing lasts forever. Where should investors look next?

How does one achieve diversification from technology without reducing the potential for growth? Sector dispersion this year has been startling. However, what has transpired in the technology sector, has actually occurred in a relatively wide range of different businesses, which are loosely defined as technology. An alternative moniker might be 'the ability of platform companies to distribute products globally with almost zero marginal cost,' or perhaps as what James Anderson of Baillie Gifford describes as 'companies that derive increasing returns to scale.'

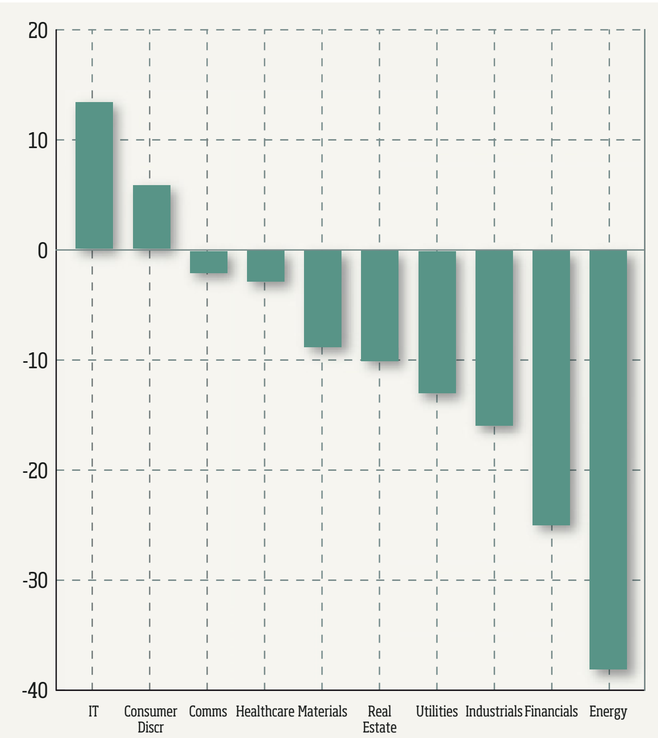
In his view, investors have been slow to recognise this phenomenon.

So where should one turn? Secular trends are defined as being neither seasonal or cyclical. Instead, they are a constant tailwind over time (often defined as five years or more), which should persist regardless of the economic path of the global economy. The theory behind thematic investing in this way, is that companies like this should provide stronger returns than wider markets.

In our view the best themes are those wrapped around several other secular themes. This offers a broad spectrum of opportunities allowing a manager to balance the risk – as well as betting on the right race having not chosen the wrong horse.

We believe there are two broad secular growth themes that are likely to persist for the next decade at the very least.

Total return YTD (%)



Source: Bloomberg

Healthcare

Healthcare as a secular growth theme offers sparkling investment prospects. Aside from benefitting from innovation and R&D spend, healthcare also encompasses two mega-themes oft-quoted by many managers: that of ageing populations in the West; and the rise of the middle classes in emerging markets.

The managers of the **BB Healthcare Trust** take the view healthcare systems around the world are fundamentally broken and seek to identify companies that offer a new approach for governments, recognising that simply pumping more money into the existing system is not going to solve the 'care crisis.' They see the entire industry as their universe, including companies within industries such as pharmaceuticals, biotechnology, medical devices and equipment, and healthcare insurers to name but a few. The managers have a concentrated, multi-cap approach. In our view, the trust is worthy of consideration for a differentiated high-growth exposure to a secular-growth story.

International Biotechnology Trust (IBT), on the other hand, invests in biotechnology companies around the world, which are working to provide solutions to unmet medical needs. IBT has a unique position in the trust universe given that it invests in both listed and unlisted companies.

A key part of the investment philosophy is to manage risk by reducing exposure to companies in the run-up to significant drug trial result announcements.

This manifests itself in a lower NAV volatility over five years relative to the benchmark, but still showing outperformance. IBT pays a dividend of 4% to the end August NAV each year from capital. Given it employs a growth strategy, this provides a very different (potentially diversifying) underlying exposure to that provided by equity income funds.

The end of carbon

We believe the other theme that will affect billions of people is the end of carbon. This is clearly a multi-faceted investment opportunity that will require many billions of dollars to wean us off fossil fuels. The likes of **Greencoat UK Wind (UKW)** and **The Renewables Infrastructure Group (TRIG)** are perhaps among the more obvious beneficiaries.

Reducing our use of fossil fuels will require us to be significantly less profligate. **Menhaden (MHN)** is a less well-known trust, investing in companies that benefit from increased efficiency in the use of energy. The portfolio is highly concentrated (only 14 holdings currently).

Impax Environmental Markets (IEM) offers investors a differentiated exposure to companies profiting from the transition to a more sustainable economy. The managers are small- and mid-cap specialists. Around the world electorates are saying that Covid-19 should provide an opportunity to 'build back better,' embedding low carbon energy systems and cleaner air in cities. Many of the specialist companies that help achieve this can be found in IEM's diverse portfolio.

One trust that is starting to align its portfolio towards the end of carbon is **BlackRock Energy and Resources Income (BERI)**. Starting from 1 June 2020, BERI has had a neutral sector weight of 40%, 30% and 30% between mining, energy and energy transition stocks.

Clearly with BERI's own transition stocks having only just been introduced the underlying portfolio does not quite qualify yet. However, with the discount to NAV of around 17%, and the board having stated they are prepared to use capital to support the 4p dividend (which yields 7% at the current share price), BERI looks interesting.

For investors who wish to diversify their exposure to themes within one trust, **Mid Wynd International (MWY)** offers access to a global stockpicking team and several themes that are less correlated to each other, which will enable them to perform well on a relative basis when markets fall.

As at 30 April, the portfolio had 10.7% exposure to what the managers call the 'low carbon world' theme, and 21.7% of NAV exposed to healthcare.

From a thematic perspective MWY might be considered a proven one-stop shop for thematic investors.