

Close Portfolio Funds

Monthly fund manager update

January 2025



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STRATEGY OVERVIEW

The Close Portfolio Funds seek to achieve resilient returns over the long term through a company-led approach to investing in a multi-asset context. Our strategy of acquiring ‘cheap durables’ – direct interests in predictable businesses that will grow in value and repay their debts purchased at attractive cash-based valuations – is complemented by allocations to fixed income securities and alternative assets as appropriate.

MONTHLY PERFORMANCE REVIEW & ACTIVITY

President Trump wasted little time post inauguration on several fronts and was quick to threaten his favourite word, ‘tariffs’, which he seems intent on leveraging to achieve a grab-bag of foreign policy goals: on Canadian/Mexican border control, on Colombian deportees, on NATO defence spending and on reducing trade deficits. Currency markets were volatile as tariff scope, scale and actuality fluctuated, but the US dollar ended the month broadly higher, buoyed by the Federal Reserve’s rate cutting pause and anticipated tariffs. Global equity markets returned 3.5% in dollar terms, translating to a 4.4% gain in sterling terms, whilst sterling bond markets returned 0.9%.

Large market moves in January were observed in the semiconductor “chip” supply chain stocks. Back in 2021, Chinese President Xi warned the US against overusing “national security” to suppress Chinese businesses. Cut to 2025 and, despite ostensibly widespread chip bans, China’s DeepSeek upended artificial intelligence (AI) economics, developing an open-source large language model that matched OpenAI’s

performance, allegedly at a fraction of the cost. DeepSeek’s claim to have trained the model on 2000 graphic processing units (10x less than Meta’s Llama3) and to have spent just \$6 million doing so, forced the market to review the enormous capital expenditure (capex) spends which were supposed to be safeguarding the US’ AI dominance. Who are the potential winners? Hyperscalers like Meta, Apple and Microsoft, now facing lower AI capex. And the losers? Potentially chip giants like Nvidia and their supply chains including TSMC and data centre providers. While Jevon’s Paradox* may drive longer term chip adoption on cheaper economics, commoditisation is now a nearer-term risk. As a result, we reduced our position in TSMC and added to weakness in Microsoft.

Earlier in the month, with rising bond yields putting pressure on the soft-landing narrative, we reduced the Portfolio Funds’ exposure to cyclical, rate sensitive stocks including Ameriprise, which has a high market beta, and Visa where the stock has outperformed. Elsewhere, we took advantage of the pullback in insurance stocks after the disastrous Californian wildfires to start a position in best-in-class US auto insurer Progressive, where structural market gains support the mid-term growth outlook. In alternatives, we increased our weighting to gold which is likely to outperform in the event of a growth scare. The portfolios remain underweight duration (or interest rate sensitivity).

All three Portfolio Fund strategies delivered strong positive returns ahead of their respective

Investment Association (IA) benchmarks in January.

**Jevon's Paradox is a concept in economics which suggests that while technological advancements make a resource more efficient to use (reducing the amount needed for a single application), if the overall demand increases as the cost of using the resource falls it ultimately causes total consumption of that resource to rise.*

LOOKING AHEAD

It is now over a year since we reversed our more cautious stance on markets and became the most optimistic we have been since assuming responsibility for the management of the Close Portfolio Funds. As long as there are no signs that America has entered recession, we will maintain an overweight stance on equities. Within fixed income we will continue to seek out above-average yields for below-average risk in corporate bonds, complemented by sovereign bonds to protect against a recession scenario should it come to pass, which is the main risk to the portfolios. However, whilst a 'soft landing' for the US economy and interest rates remains on track, we are also vigilant for exogenous shocks such as pandemics and geopolitical upsets.

As a long-term strategy with low turnover, we fully expect and recommend that unitholders judge our performance over a period of five years or more.

STOCK OF THE MONTH – PROGRESSIVE CORPORATION

This month's stock of the month is Progressive Corporation, which is held across the Close Portfolio Fund range.

Progressive Corporation has grown to be the number two US car insurer taking material share over the past thirty years from less than 1% to now c.15%. These impressive market share gains have been driven by its key competitive advantages. Firstly, Progressive was an early adopter of the market increasingly shifting towards call centres and the internet. Historically, in the US, car insurance was bought through agents, but this increases costs as agents take commissions. Shifting towards selling direct-to-consumers enabled policies to be structurally lower cost, which is an important factor as consumers are rarely sentimental or

have brand loyalty when it comes to car insurance. Secondly, Progressive also pioneered the use of telematics through its Snapshot programme that monitors driving behaviour such as speed, braking habits and mileage allowing insurance to be based off driving habits rather than general demographic factors. This technology-led underwriting process drives a best in-class underwriting profitability and the ability to invest counter-cyclically when peers are capital constrained.

These dynamics occurred coming out of the pandemic as inflationary pressures drove an acceleration in the cost of claims. Progressive experienced a period of outsized market share gains as competitors cut back to repair their profitability. Progressive is expected to become the number one player in the US in the near-term, with a long runway of share gains ahead of it. This dominance can then drive further economies of scale benefits, reinforcing its durable competitive advantage from its direct-to-consumer technology-led approach to car insurance. Having only entered the industry ten years ago, Progressive's market share in homeowners' insurance remains small (number eleven player with 2% US market share), but this can also represent a roadmap for future growth.

As Progressive grows its multi-line product offering this will increase the earnings quality of the business as consumers become stickier. Overall, this set-up is forecasted to drive sustainable growth materially above the compounding auto-insurance market, with the business seen as a growth stock in a defensive end-market.

ESG

Progressive's use of telematics through its Snapshot programme strives to match rates to behaviour, rewarding customers who take less risk with their health and safety. This drives the best-in-class loss ratio enabling further products that reward customers' environmental stewardship and commitment to sustainable practices.

IMPORTANT INFORMATION

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