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Multi-Asset

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Great British opportunities

Political events typically do not have a long-term impact on investment markets. The UK general election on 4 July, however, may have signalled a new period for the stock market, which we believe has long been undervalued. These new political winds, combined with cheap valuations and reasonable economic backdrop provide a positive platform for UK companies of all sizes.

Let's start with politics. Labour's large majority may herald political and policy stability for the UK. This is essential if the UK is to attract international investors to return, whether to invest in the economy or the stock market. With political uncertainty elsewhere in the world, including the elections in France and the US, the UK may actually become one of the more stable countries.

Second, the new government has stated its commitment to a pro-growth agenda and other policy reforms such as the simplification of pensions. These also have the potential to boost the economy and stock market.

There are a number of reasons why the UK has looked cheaply valued to us, which has led to the Liontrust Multi-Asset team scoring the market a 4 in the Tactical Asset Allocation process, in which 5 is the most positive and 1 the most negative.

First, as our colleagues on the Liontrust Economic Advantage team have stated, the capitalisation of the entire UK stock market is 17% below the fair equity value, according to estimates by Canaccord Genuity Quest. The opportunity is particularly pronounced among small caps, where the discount to fair value is 29%. This discount is even more pronounced when the UK market is compared to other indices such as the US.

We would argue that the spate of acquisitions of UK listed stocks by private equity and overseas companies reinforces this belief that the UK is cheap.

Second, is the outlook for the UK economy. It appears as though the economy is through the worst, with the UK having cleared the shallow recession of the second half of 2023 and inflation having returned to the Bank of England's 2% target. The UK has some unique characteristics that pushed inflation higher than the US and much of Europe, including the country's energy policy. These same characteristics, however, have enabled inflation to fall quicker than most other developed markets as well.

Inflation in the services sector has remained stubbornly higher than elsewhere in the economy but this is also now coming down.

Having got through the general election, the belief is that interest rates will start being reduced soon. Bloomberg stated in late June that there was a 66% chance of a rate cut in August, with the expectation it will be a 0.25% reduction.

Interest rate cuts will be supportive of stocks, especially smaller companies that have suffered disproportionately from being out of favour with investors and dealing with high borrowing costs from lenders. The Multi-Asset team has been adding to funds with good exposure to small and mid caps in the UK.

We are generally biased towards being overweight equities. In addition to the UK, we are most bullish about Japan, Asia, emerging markets and US small caps. The economic environment and outlook are positive for equities, they are still generally cheap, under-owned and there is a lot of cash waiting on the sidelines. A strengthening global economy or further improvements in investor sentiment would give a major boost to them.

It is always hard to predict when a market can realise the value identified by investors and what the catalyst might be. Typically, this does not usually require a major catalyst, and an increase in positive sentiment may be sufficient. We believe the UK is moving into just such an environment where there will be greater recognition of how the market, in particular small and mid caps, are undervalued.

For a comprehensive list of common financial words and terms, see our glossary at:
https://www.liontrust.co.uk/benefits-of-investing/guide-financial-words-terms

Key Risks

Past performance does not predict future returns. You may get back less than you originally invested.

The Funds and Model Portfolios managed by the Multi-Asset Team may be exposed to the following risks:

Credit Risk: There is a risk that an investment will fail to make required payments and this may reduce the income paid to the fund, or its capital value. The creditworthiness of a bond issuer may also affect that bond's value. Bonds that produce a higher level of income usually also carry greater risk as such bond issuers may have difficulty in paying their debts. The value of a bond would be significantly affected if the issuer either refused to pay or was unable to pay; Counterparty Risk: The insolvency of any institutions providing services such as safekeeping of assets or acting as counterparty to derivatives or other instruments, may expose the Fund to financial loss; Liquidity Risk: If underlying funds suspend or defer the payment of redemption proceeds, the Fund's ability to meet redemption requests may also be affected; Interest Rate Risk: Fluctuations in interest rates may affect the value of the Fund and your investment. Bonds are affected by changes in interest rates and their value and the income they generate can rise or fall as a result; Derivatives Risk: Some of the underlying funds may invest in derivatives, which can, in some circumstances, create wider fluctuations in their prices over time; Emerging Markets: The Fund may invest in less economically developed markets (emerging markets) which can involve greater risks than well developed economies; Currency Risk: The Fund invests in overseas markets and the value of the Fund may fall or rise as a result of changes in exchange rates. Index Tracking Risk: The performance of any passive funds used may not exactly track that of their Indices. Any performance shown in respect of the Model Portfolios are periodically restructured and/or rebalanced. Actual returns may vary from the model returns. The risks detailed above are reflective of the full range of Funds managed by the Multi-Asset Team and not all of the risks listed are applicable to each individual Fund. For the risks associated with an individual Fund, please refer to its Key Investor Information Document (KIID)/PRIIP KID.

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