UK Multi-Cap strategy

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- Weak stock market reflected concerns about a global economic slowdown over the month
- Strong relative performance from technology and industrials sectors drove outperformance
- We remain focus on well capitalised companies with growing profits

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What's happening?

May was a weak month of stock market returns on concerns about a global slowdown following China's continued weak economic data and uncertainty around the US debt ceiling, which outpaced optimism around slowing inflation in many developed market economies. The FTSE 100 hit a two-month low at the end of the month on these combined headwinds as the Oil & Gas and Metals & Mining sectors came under pressure.

Contrary to many market economists and indeed the Bank of England (BOE) and the International Monetary Fund (IMF), the UK economy once again beat the rather gloomy economic expectations. Indeed, the IMF no longer expects a recession in Britain this year. It said the steps taken by the government to stabilise the economy and fight inflation would help GDP grow by 0.4% in 2023 rather than contracting 0.3% as it had predicted in April. The Bank of England also upgraded their 2023 forecasts in May, showing that it too had become overly pessimistic.

While the Consumer Price Index (CPI) rate of inflation fell to 8.7% year-on-year in April 2023, the lowest since March 2022, the rate still exceeded market expectations of 8.2% and remains well above the Bank of England's (BoE) 2% target. Inflation is currently being driven by 'shop inflation' which reached its highest rate since industry records began in 2005. The British Retail Consortium said prices in supermarkets and retail chains rose 9.0% in the year to May, after an 8.8% increase in April, although food prices cooled slightly. In response the BOE increased the cost of borrowing by another 25 basis points (bps), in line with its central bank peers in the US and Europe, to reach 4.5%.

The FTSE All Share (-4.72%) and its constituent parts (the FTSE 100 -5.04%, FTSE 250 ex-Investment Companies -4.11% and FTSE Small Cap ex-Investment companies -1.71%) all posted sizable declines[1].

Portfolio positioning and performance

The strategy outperformed its comparative index, the FTSE All Share. The overweight positions in the Technology and Industrials sectors contributed positively to performance.

[1] Source: Bloomberg, as at 31/05/2023

Positive contributors of note included Bytes Technology and Melrose. Bytes reported strong organic growth numbers, helped by the demand for Microsoft and cyber security products. Not owning British American Tobacco and Unilever was positive.

Detractors included Future, Prudential and not owning HSBC. Future reported in-line interim results but were more cautious on the outlook for the remainder of their financial year. The UK part of their business posted more resilient performance while media revenues in the US fell.

We continue to focus on well capitalised companies that have growing profits, cash flows and, where appropriate, dividends. Market volatility was used to add to and reduce core holdings. No new holdings were taken over the month. The position in RS Group was sold following a change of management team and cyclical concerns over its growth potential. The position in iEnergizer was also closed.

Outlook

Inflation, interest rate expectations, macro-economic data points and the path of conflict in Ukraine are likely to govern capital flow, volatility and short term returns of both equites and debt.

Equity market returns continue to be governed by movements in global bond markets. Market volatility will remain in the near-term as central bankers move into a new data dependant framework and investors will pay close attention to the immediate data releases, along with the forthcoming central bank meetings, which will be key in the assessment of how close central banks are to ending their tightening cycle. Growing evidence suggests that inflation has peaked, however the speed of decline and the trough level continues to be debated.

UK equities remain at a mid 20% discount to global equities and with circa 10 take over approaches of UK listed businesses in April, private equity funds, in particular, are becoming increasingly active in releasing this value and opportunity.

While the outlook for equities may be finely balanced, our approach remains centred on owning good quality businesses that can reinvest and compound their returns over time. We continue to believe that understanding longer term structural trends and identifying responsible, reliable and ultimately sustainable companies, in a targeted, focused and active approach, remains the key to longer-term success.

No assurance can be given that the UK Multi-Cap Strategy will be successful. Investors can lose some or all of their capital invested. The UK Multi-Cap strategy is subject to risks including; Equity; Smaller companies risk; Liquidity risk; Investments in small and/or micro-capitalisation universe; Investments in specific countries or geographical zones.

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