BROMPTON ASSET MANAGEMENT

UK general election commentary

13 December 2019

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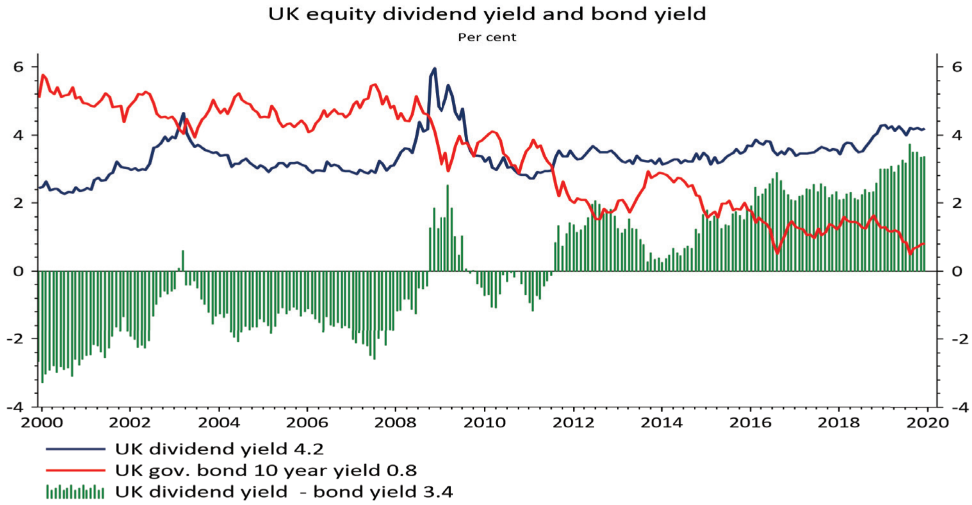
Glad tidings of good cheer for investors as Conservatives win big majority

A landslide victory for the Conservatives in the UK general election gives the government a mandate to "get Brexit done" and deliver on manifesto pledges to increase public sector spending. In the immediate aftermath, UK assets were in demand. The pound rose more than 1% against the dollar overnight as US traders digested the implications of an exit poll predicting a big Tory win. This rise came on top of a 7.12% gain since 30 September as investors grew more optimistic about the UK political situation.

UK stocks rose more than 2% before lunchtime as investors celebrated the extent of the Labour rout while medium-sized and smaller companies rose almost 4% and more than 2% respectively because of their higher sensitivity to domestic economic trends. Brompton Asset Management clients should benefit from the fund management team's selections of UK equity funds that have relatively high allocations to small and medium-sized companies. Brompton has also invested in UK value managers to gain exposure to out-of-favour UK domestic stocks that have fallen into the value managers' province.

The UK election result is the catalyst the fund management team needed to invest on behalf of clients more in Brompton's preferred UK equity funds. Brexit-uncertainty had driven down UK equity valuations to historic lows, leaving the UK market dividend yield at more than 4%, a level that appears particularly attractive in an environment of low inflation and low interest rates, as the chart below shows.



Source: Refinitiv Datastream

There are uncertainties. Boris Johnson's campaign promise of delivering Brexit by 31 January may be honoured and "no deal" averted for now yet the subsequent trade negotiations may bring fresh difficulties. Increased clarity may, however, stimulate corporate spending.

This, combined with Conservative pledges to increase public sector spending, may lead to some acceleration in faltering UK gross domestic product growth.

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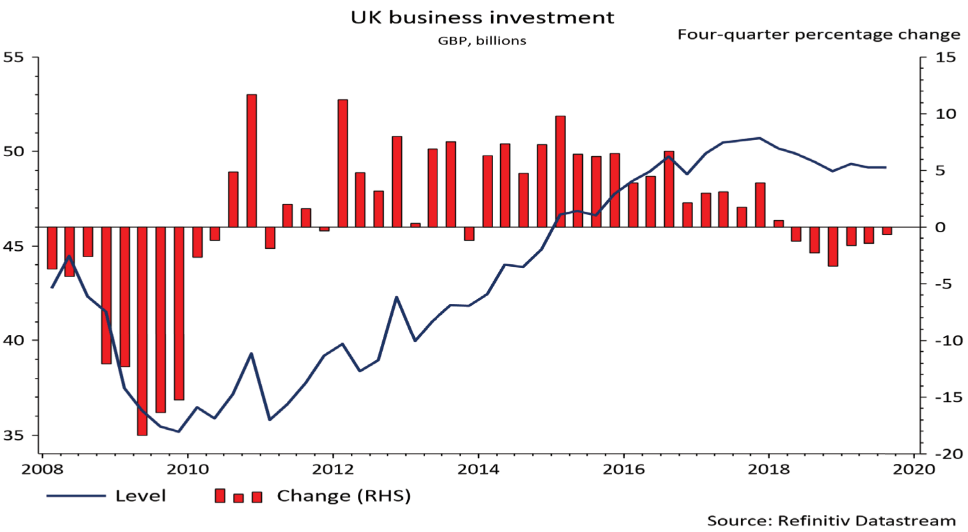

Business investment in the UK has fallen for the last five quarters, as the chart above shows.

The Bank of England has kept interest rates low in part because of Brexit uncertainty. In such circumstances, UK government bonds appear expensive and may fall. A smooth Brexit transition accompanied by some acceleration in economic growth might give the Bank the scope to increase interest rates.

In overseas markets, positive news that President Trump has agreed an interim Sino-US trade deal in principle, averting planned tariff increases, should not be overshadowed by the UK election result. There appears to be no silver bullet or easy resolution of the thorny issues of national security and leadership in key technological industries, which have soured trading relations, but this development is further good news for investors.

The Brompton fund management team's positive view on the outlook for risky assets is founded on the supportive monetary policies adopted by the Federal Reserve and some other central banks. The UK election result and positive developments on trade remove some of the policy risk and may lead to further gains for equities.

Important information