Understanding investing: UK versus overseas equities

Insight for charities

Rathbones
Look forward

The value of investments and the income from them may go down as well as up and you may not get back your original investment. Past performance should not be seen as an indication of future performance.

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Contents

An overview of some of the key factors to be considered when analysing the merits of UK equities compared to overseas markets.

Investment sentiment towards the listed UK market has been rather disparaging in recent years and one of the key questions for many investors has been, ‘why bother with the UK?’ After all, it only accounts for 4.38% of the world market and is more than ten times smaller than the United States’ weighting[1].

However, while diversifying away from the UK has been an integral part of Rathbones’ overall portfolio strategy for charity clients over the past few years, we believe the UK market should no longer be ignored in this next phase of economic recovery.

[1]. MSCI World Index as at 31 May 2021

An underperforming market

A country's political landscape and related events often play a crucial role in affecting investor sentiment, and go some way to explaining why overseas markets have consistently outperformed the UK market for a number of years.

Most recently, the enormous uncertainty caused by the Brexit referendum outcome, combined with continued political uncertainty, resulted in many international investors ignoring the UK equity market altogether. Indeed, over the four years to the end of 2020 the UK equity market underperformed by approximately 45%[2].

Currency also has an important role to play. For example, sterling-denominated investors have benefited from the appreciation of the dollar, which has given unhedged US stocks a welcome boost.

It's also important to consider a market's sector make-up. Despite its multinational exposure, the UK equity market has been regarded as 'unfashionable' in recent years from a sectoral point of view. Investors have focused more heavily on the technology sector, which makes up more than a third of the US market, while more cyclical sectors such as financials and commodities, which form a large part of the FTSE 100, have experienced a dramatic drop in investor interest.

[2]. Datastream, Bloomberg Finance L.P

Look to the future

While we can learn many things from history, one of our primary tasks as investment managers is to seek out future opportunities and mispriced assets.

The underperformance of the UK in recent years has resulted in UK valuations hitting a 30-year low compared to global peers[3]. This valuation discount relative to overseas markets is too hard to ignore, suggesting that now may not be the best time to dramatically reduce one's UK exposure.

This long-term investment position has also been reinforced by the actions of global private equity firms: there has been a significant increase in interest in the UK market in recent months, and merger and acquisition activity has rocketed.

From an income perspective, while it may be easy to assume that the UK is a write-off given the events of 2020, the UK is anticipated to have the highest dividend yield of the main markets in 2021 as the income outlook improves with the economic recovery.

[3]. Morgan Stanley Research, 1 January 1988 to 27 January 2021. MSCI UK versus MSCI World

‘Follow the money not the mail’

Finally, a company’s geographic listing is becoming less and less relevant to investment decisions.

In fact, companies listed on the FTSE 100 tend to generate more revenue from emerging markets than the domestic UK economy: only 23% of their revenues came from the domestic UK economy in 2019[4].

Take, for example, pharmaceutical company AstraZeneca. Listed in London, it currently only generates 6.5% of its revenues from the UK[5]; it’s a truly global business that just happens to be listed in the UK.

It’s imperative that investors concentrate on where a company's revenue is generated, as opposed to where it’s listed or registered – “follow the money not the mail,” as the saying goes.

[4]. Capital Group International

[5]. Factset

The fundamentals of investing

This guide accompanies one of our charity investment training webinar series: Equities - which markets? You can watch the full webinar by following this link.

Our training webinar series is designed to provide trustees and senior finance staff with an understanding of the fundamentals of charity investment as well as highlighting their responsibilities.

Please visit:
rathbones.com/charities to find out more about the training series or to read our other guides.

To find out more about Rathbones' approach to portfolio construction and investing for charities, please contact:

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Look forward

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