

Active is: Navigating geopolitics

# UK: still no reason for optimism?

25/07/2019   

## Summary

“Under-owned, cheap and unloved” – those words sum up how many investors view the UK today. Some see a fresh start in the arrival of a new prime minister eager to change the narrative. But it’s difficult at this stage to look beyond Brexit to make a convincing short-term investment case for UK assets, despite a number of enduring positive fundamentals.

### Key takeaways

- It’s tempting to see the Boris Johnson premiership as a fresh start for the UK – but Brexit-related uncertainty remains a major obstacle for investors
- While the UK boasts some positive fundamental qualities, it’s difficult to see beyond Brexit in the short term
- Any future reassessment of the UK relies on Mr Johnson doing two things: achieving a satisfactory Brexit resolution and creating a compelling, forward-looking and positive narrative

This week, the UK announced its new prime minister. Boris Johnson stepped into Downing Street as the new Conservative Party leader and replacement for Theresa May, whose premiership foundered on her failure to deliver Brexit.

Meanwhile, the UK markets remain in the doldrums even though the economy has been surprisingly resilient and stocks of internationally focused UK companies have done relatively well, at least in sterling terms. Indeed, the “valuation gap” between internationally focused stocks and their more domestic counterparts is among the most extreme in recent times.

We are not surprised investors have been underweight the UK; it is a difficult market to navigate. Not only is overall sentiment pessimistic, but UK equity and bond markets are pointing in different directions.

Brexit is, of course, a large part of the reason why the UK is struggling, and Mr Johnson takes office with the clock ticking on a 31 October deadline – the end date for the current Brexit extension granted by the European Union. In the face of this major challenge, the new prime minister will be eager to change the narrative and inject optimism.

Yet we think that any positive rhetoric from Mr Johnson will be insufficient for changing investors’ view of the UK fundamentally. He must first resolve Brexit – and until he does, it will always get in the way.

## The first important days

One of the challenges facing the incoming prime minister is that his party holds only a small majority in the UK parliament. Unless and until Mr Johnson calls a general election, and his Conservative Party gain a sizeable majority, the parliamentary maths remain forbidding – on Brexit and any other issues that require primary legislation. That doesn’t give him much support for a radical new fiscal programme. Nor would Mr Johnson have much room for manoeuvre if he were to

find the votes: the current-account budget deficit may be down, but the UK faces a late-cycle environment with a mountain of debt.

So what can the new prime minister do from a fiscal perspective to set the tone for his premiership while positioning his government – and the country at large – for an uncertain Brexit outcome or even a general election?

In his first speech as prime minister, Mr Johnson said that those people “who bet against Britain are going to lose their shirts” and spoke of an economic package in the autumn to boost the country’s competitiveness. Given his lack of a meaningful parliamentary majority, he may need to focus initially on measures that require no primary legislation. These could include housing-market stimulus such as a reduction in stamp duty, cuts to value-added tax (VAT) or a vehicle-scrappage scheme that encourages use of more environmentally friendly cars.

Short-term stimulus aside, there is no avoiding the Brexit question. We’re not going to speculate on the likely outcome, but the new prime minister has been bullish on Brexit, even if that means a hard, no-deal departure. At the same time, he will be cognisant of the existential threat posed by the Brexit Party, which made major inroads into the Conservative vote in the European elections with its uncompromising approach to Brexit.

## What this means for investors

From our perspective, a lot of “ifs” remain. If Mr Johnson is able to pull off a satisfactory resolution to Brexit – no mean feat – and if he creates a compelling, positive narrative, we could see a reassessment of the UK’s prospects:

- The British pound sterling has struggled since the Brexit referendum in 2016, and we continue to be nervous about the currency in the short term – despite it being undervalued on just about every measure. Sterling would be among the first beneficiaries of an improved outlook for the UK.
- The UK may turn out to be the value trade it has promised to be. For example, real estate and utilities have been discounted, in part because of Brexit-induced economic and political uncertainty. A positive resolution of Brexit that reduces near-term economic and political risks could mean a move upward as these risks are priced out.
- From an environmental, social and governance (ESG) perspective, the UK has some of the highest corporate governance and stewardship standards. We believe this may become more important over time as ESG risks come to play a greater role in separating the long-term winners from the losers.
- The UK economy has many long-term attractions, such as a well-educated workforce, a commitment to liberal values and the protection of property rights. In a world where markets are driven by energy and conviction, a shift in direction could be the boost people need to look past the negative noise and see the positive fundamentals.

Still, despite Mr Johnson’s victory, nothing significant has changed overnight, and it may be too soon for investors who are underweight the UK to take a new tack.

908802

## Want to view more?

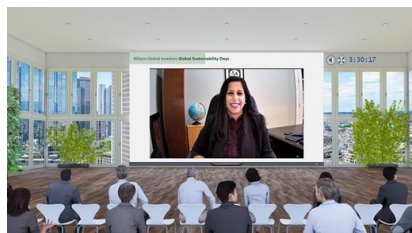


### Outlook & commentary

2021 outlook: portfolios need a broader mix as the pandemic prolongs the uncertainty

→ [DISCOVER MORE](#)

3 days ago



### Outlook & commentary

US election: commentary and implications

→ [DISCOVER MORE](#)

by [Mona Mahajan](#) | 12/11/2020



### Outlook & commentary

Will Fed easing support risk assets?

→ [DISCOVER MORE](#)

by [Mona Mahajan](#) | 12/07/2019



Active is: Anticipating what’s ahead

# A major about-turn for the Fed

by [Franck Dixmier](#) | 25/07/2019   



## Summary

In the face of slowing global economic growth, continued trade tensions and the prospect of a “hard Brexit”, the FOMC seems set to announce a reduction in interest rates at its next meeting. We expect a 50-basis-point cut that will start a new rate-cut cycle, and we think the markets should react favourably.

### Key takeaways

- The FOMC meeting on 30-31 July seems likely to mark a major turning point in monetary policy for the Fed
- The Fed appears set to enter a rate-cut cycle; we expect the FOMC to announce a decrease of 50 basis points
- Given a weakening global economy and persistent trade tensions, the Fed likely wishes to act pre-emptively as an exercise in risk management
- Markets might be surprised at the news, but will likely react positively given the historically favourable impact of rate cuts on equity markets

↓ [LOAD MORE](#)

---

## Disclaimer

**Investing involves risk.** The value of an investment and the income from it will fluctuate and investors may not get back the principal invested. [\*] Past performance is not indicative of future performance. This is a marketing communication. It is for informational purposes only. This document does not constitute investment advice or a recommendation to buy, sell or hold any security and shall not be deemed an offer to sell or a solicitation of an offer to buy any security.

The views and opinions expressed herein, which are subject to change without notice, are those of the issuer or its affiliated companies at the time of publication. Certain data used are derived from various sources believed to be reliable, but the accuracy or completeness of the data is not guaranteed and no liability is assumed for any direct or consequential losses arising from their use. The duplication, publication, extraction or transmission of the contents, irrespective of the form, is not permitted.

This material has not been reviewed by any regulatory authorities. In mainland China, it is used only as supporting material to the offshore investment products offered by commercial banks under the Qualified Domestic Institutional Investors scheme pursuant to applicable rules and regulations. This document does not constitute a public offer by virtue of Act Number 26.831 of the Argentine Republic and General Resolution No. 622/2013 of the NSC. This communication's sole purpose is to inform and does not under any circumstance constitute promotion or publicity of Allianz Global Investors products and/or services in Colombia or to Colombian residents pursuant to part 4 of Decree 2555 of 2010. This communication does not in any way aim to directly or indirectly initiate the purchase of a product or the provision of a service offered by Allianz Global Investors. Via reception of this document, each resident in Colombia acknowledges and accepts to have contacted Allianz Global Investors via their own initiative and that the communication under no circumstances does not arise from any promotional or marketing activities carried out by Allianz Global Investors. Colombian residents accept that accessing any type of social network page of Allianz Global Investors is done under their own responsibility and initiative and are aware that they may access specific information on the products and services of Allianz Global Investors. This communication is strictly private and confidential and may not be reproduced. This communication does not constitute a public offer of securities in Colombia pursuant to the public offer regulation set forth in Decree 2555 of 2010. This communication and the information provided herein should not be considered a solicitation or an offer by Allianz Global Investors or its affiliates to provide any financial products in Brazil, Panama, Peru, and Uruguay. In Australia, this material is presented by Allianz Global Investors Asia Pacific Limited (“AllianzGI AP”) and is intended for the use of investment consultants and other institutional/professional investors only, and is not directed to the public or individual retail investors. AllianzGI AP is not licensed to provide financial services to retail clients in Australia. AllianzGI AP (Australian Registered Body Number 160 464 200) is exempt from the requirement to hold an Australian Foreign Financial Service License under the Corporations Act 2001 (Cth) pursuant to ASIC Class Order (CO 03/1103) with respect to the provision of financial services to wholesale clients only. AllianzGI AP is licensed and regulated by Hong Kong Securities and Futures Commission under Hong Kong laws, which differ from Australian laws.

This document is being distributed by the following Allianz Global Investors companies: Allianz Global Investors U.S. LLC, an investment adviser registered with the U.S. Securities and Exchange Commission; Allianz Global Investors Distributors LLC, distributor registered with FINRA, is affiliated with Allianz Global Investors U.S. LLC; Allianz Global Investors GmbH, an investment company in Germany, authorized by the German Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin); Allianz Global Investors (Schweiz) AG; Allianz Global Investors Asia Pacific Ltd., licensed by the Hong Kong Securities and Futures Commission; Allianz Global Investors Singapore Ltd., regulated by the Monetary Authority of Singapore [Company Registration No. 199907169Z]; Allianz Global Investors Japan Co., Ltd., registered in Japan as a Financial Instruments Business Operator [Registered No. The Director of Kanto Local Finance Bureau (Financial Instruments Business Operator), No. 424, Member of Japan Investment Advisers Association and Investment Trust Association, Japan]; and Allianz Global Investors Taiwan Ltd., licensed by Financial Supervisory Commission in Taiwan.

[\*Subject to change – depends on the content of the material which may mention certain investment instruments that involve particular risk]

**Our firm**

- Why partner with us
- A brief history
- Inclusion & diversity
- Sustainability
- The SeaCleaners
- Our leadership team
- Our experts
- Careers
- Contact us

**Insights**

- Outlook & commentary
- Investment themes & strategy
- Why active?
- 2020 Outlook
- Coronavirus
- Update Magazine
- The Investment Intelligence
- Podcast
- Staying active

**Capabilities**

- Alternatives
- Equity
- Fixed income
- Multi asset
- China A-shares
- Research
- risklab

**Press centre**



Allianz Global Investors is comprised of the **AllianzGI Affiliated Entities** worldwide. Product availability will vary by jurisdiction.