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Investing for a
world of change

An attractive alternative to the concentrated trade



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How did UK equities fare during 2025?

UK equities were strong performers over the year, shrugging off the significant 'Liberation Day' weakness in April, with the FTSE 100 passing the 9,000 mark for the first time since its launch in 1984. Gains were widespread, with notable advances for financials, healthcare, and defence names, particularly after increased NATO spending commitments were made. There were, however, some concerns surrounding the consumer and broader economic health of the country and its finances, all of which contributed to the mid-cap FTSE 250 lagging its more global sibling.

Yet, despite these concerns, 2025 highlighted the enduring relevance of the UK market and reminded investors of the important role it can play within diversified portfolios. Much of this renewed focus was driven by the resurgence of the Value style, which the UK market is well known for. Returns within UK Value over the past five years have been remarkable, even surpassing those of the S&P 500. While Value, Growth, and high-dividend stocks all rallied strongly in 2025, Quality as a style derated, and is now trading below its 10-year median valuation. With previously discounted cyclicals now more fairly priced and quality compounders having derated, the destination of future leadership is in focus.

Do you expect Quality to come back in favour in 2026?

For much of the post-GFC period of low interest rates, diversified, franchise type businesses with recurring revenue streams commanded elevated multiples and patient shareholders were well rewarded. However, since 2022, the fortunes of this Quality opportunity set have suffered, bringing into question its role within portfolios.

While we typically try to avoid attempts at crystal ball gazing, we do think it is important to maintain discipline and perspective as market leadership shifts and investment styles rotate. The last three years have seen a significant revaluation of many cyclical businesses which had simply become too cheap. The FTSE All-Share has rerated from 9x to 14x earnings over this period. At the same time, much of the Quality universe derated and we now find ourselves at a point where free-cash-flow valuations for UK Quality stocks and the broader benchmark are virtually at parity. We are therefore not at all surprised to see more of the Value investment community turn up to investor meetings with some of the Quality companies within our universe.

This gives us increased confidence in the outlook for Quality as a style, focusing on those companies with top-line rigidity driven by high retention ratios, high recurring revenue streams and/or staple-like products. In contrast, the All-Share's profits are largely driven by exogenous factors such as interest rates for the banks or commodity prices. At a moment when global equity valuations are elevated and economic indicators are faltering, we remain as convinced as ever that a combination of defensiveness and valuation support provides a strong foundation.

To take the temperature of the real economy, we spent time on the road earlier in 2025 visiting a number of our portfolio holdings to build a picture of how companies are experiencing business on the ground. We were reminded of the competitive strength possessed by many of the businesses we own. As we have written previously, many industrials have suffered from weak end markets over the last 12-24 months. However, we have built positions in businesses with dominant market positions, which primarily provide business-critical components, enabling pricing power, and are financially very secure. We remain optimistic about the store of value we see in the portfolio, both in Quality businesses in out-of-favour industries which will recover in time, and in Quality compounders which are in control of their growth.

Do you expect Value to continue its strong run?

Despite perceived domestic headwinds, we believe the UK remains an attractive place to invest for those seeking an alternative to the concentrated US trade with its mix of well-run domestic businesses and global champions, both of which are trading at relatively low valuations. Despite its strength in 2025, the UK equity market still trades at a substantial discount to other major markets – about half of the S&P 500, for example. It is important to remember that, as well as some well-run, cheap domestic businesses, the UK is also home to many global champions that trade at lower valuations than their peers elsewhere. This mix of UK-focused and globally oriented companies allows for the construction of attractively valued, diversified portfolios.

And then there are buybacks, which support share prices and are rising in many countries outside the US, but fastest of all in the UK. This gives us some reassurance that many management teams and/or boards observe the value creation opportunity in a similar way to us. In addition, UK companies continue to return cash to shareholders with particularly generous dividends relative to most other advanced economies. Despite negative domestic flows, UK PLC is taking matters into its own hands!

Could the UK be an attractive alternative to the US?

As has been the case for much of the last five years, the US looks expensive. By contrast, we continue to see significant opportunity in UK equities. Whilst at the headline level this helps guide our opportunity set, we do not construct our portfolios based on any reliance on macro scenarios or mean reversion playing out; instead, we look for the best UK and international ideas on a bottom-up basis that meet our return criteria, irrespective of what other investors may determine a 'fair' equity risk premium at different points in the investment cycle. With this approach, we continue to find a deep bench of potential investments.

Given the uncertain global market backdrop, we believe it makes sense to adopt an active, selective investment approach to UK equities, seeking to capture alpha rather than relying solely on the market return. For UK equity investors, Quality and Value are complementary active approaches with differentiated drivers of potential return, which can add diversification benefits to investors' portfolios.

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