# MARKET INSIGHT

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Redmayne Bentley

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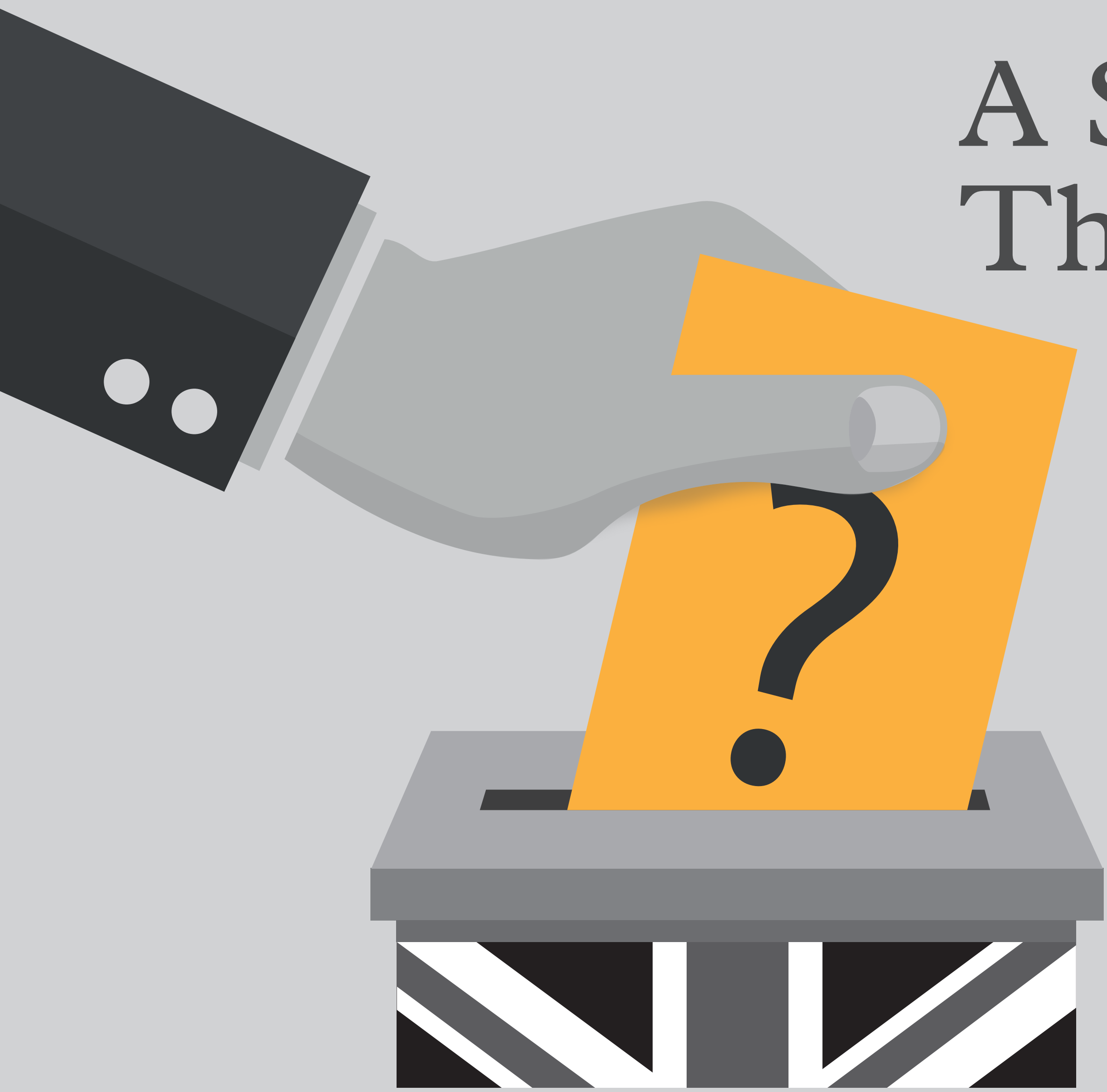
# A Sure Thing?



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# A SURE THING?

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## IN THIS ISSUE



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**This edition of Market Insight is significant, if only because it is the last issue before the upcoming election. Recent polling appears to indicate a change of colour in the UK's political leadership, shifting from blue to red. At the time of writing, YouGov, the research and analytics specialist, is predicting a Labour majority, with four hundred and twenty-two seats to the Conservatives' one hundred and forty. Predicting a Labour win might feel like a safe bet, but personal experience warns against making predictions about how the markets will react.**

Elections can be highly distracting events, leading investors to place undue weight on short-term outcomes as opposed to their longer-term investment goals. Successfully predicting the voting outcome does not qualify one for success in predicting the subsequent market reaction. If anything, individual political biases can leave the forecaster on shaky ground. Take the 2016 US Presidential Election, for example: a democrat conceding that Donald Trump might be victorious could have assumed the outcome would be bad for financial markets. A decision to then sell or abstain from investing in the US flagship S&P500 index could have resulted in some or all of the 83.2% return of the index being missed during his tenure.

While there's a general desire to refrain from predicting financial market reactions, one which can be made is the expectation that the future path of interest rates will remain the dominant driver of market sentiment. Regardless of the outcome, the party in power will need to tackle the challenge of igniting economic growth, which has become more difficult in the current higher interest rate environment.

Away from the general election, FTSE Russell, the provider behind the FTSE indices, recently conducted one of its regular rebalances, with several changes expected to be applied in late June. Within the UK's flagship FTSE100 index, Ocado Group, RS Group and St. James's Place all exit, to be replaced by Darktrace, LondonMetric Property, and Vistry Group. Our stock focus article takes a deeper look at LondonMetric Property given the transformational twelve months that has seen the portfolio double in size following the acquisitions of CT Property Trust and LXi REIT. The company has been no stranger to merger and acquisition activity over the years, with its origins tracing back to 2007 and the £246m initial public offering of London & Stamford. Today, the company is one of the UK's largest real estate investment trusts with a market capitalisation of £3.97bn and a portfolio value of £6.2bn.

Between the time of writing and 4th July, forecasts and polls will undoubtedly change, but the outcome at this moment in time feels to have been accepted and the attention of financial markets remains focused on macroeconomic data. Volatility is always likely and could return should there be a shock outcome on polling day.

# STOCK FOCUS

## LONDONMETRIC PROPERTY PLC

ALASTAIR POWER | INVESTMENT RESEARCH MANAGER

**In early June the global index provider FTSE Russell announced the latest rules-driven changes to the UK indices. Within the announcement, three switches are expected within the larger capitalisation FTSE 100 index and six in the mid-capitalisation FTSE 250 index. For the FTSE 100, Ocado Group, RS Group, and St. James's Place exit, to be replaced by Darktrace, LondonMetric Property, and Vistry Group. In this Stock Focus, we take a closer look at LondonMetric Property and consider its transformational twelve months.**

LondonMetric Property is a name which may not be instantly recognised. Its current form is the result of a series of mergers and acquisitions under the existing management team that has resulted in qualification for the UK's flagship equity index. Its origins date back to 2007 when London & Stamford raised £246m at initial public offering (IPO) to invest in a diversified property portfolio. In 2013, London & Stamford merged with Metric Property Investments, creating an enlarged entity under the revised name of LondonMetric Property plc. The merger trend would continue over time, with the company increasing its scale through acquisitions. In 2019, it acquired

A&J Mucklow, followed by CT Property Trust in 2023, and LXi REIT plc earlier this year.

Through mergers and day-to-day investment activity, LondonMetric Property is now one of the UK's largest Real Estate Investment Trusts (REITs) with a £3.97bn market capitalisation and a property portfolio of £6.2bn. While the operating company has evolved, so too has the portfolio. Initially focusing on out-of-town retail parks, the leadership has been skilfully adjusting the composition, shifting towards distribution warehousing in the mid-2010s before focusing on urban warehousing and long income assets in the logistics and convenience grocery sectors. Since acquiring LXi's £2.9bn portfolio earlier this year, the portfolio has seen the addition of assets within healthcare, entertainment and leisure sectors, including the Alton Towers theme park.

While the portfolio remains diverse and focused on emerging consumer themes, such as convenience shopping and key operational assets, the focus remains on a particular type of lease, the triple net lease.

In simplest terms, the triple net lease structure is one in which the tenant is responsible for both the rent and the operational expenses associated with the building, such as maintenance and insurance. The benefit of this leasing structure comes in the minimal loss of rental income through property costs. In the latest results, the company lost just 1% of revenue through property-related costs, allowing a larger amount of rental income to move through the income statement to earnings and subsequently be distributed to shareholders via dividends. By minimising property costs and keeping a tight control of both financing and administration costs at the parent company level, rental growth is expected to feed through into growing dividend distributions. The proof is in the pudding as they say, and LondonMetric has grown its dividend in each of the last nine financial years and announced a 17.6% increase in the target dividend for the coming financial year.

Against its peer group, LondonMetric stands out for its share price, trading at a premium to the net tangible assets per share, whilst many others trade at a discount. This may put some investors off, given the ability to buy other REITs at a 25-35% discount to their net tangible assets. If we consider the yield, however, investors may find the company more appetising. The target total dividend distribution for the coming financial year of 12p per share equates to a forward yield of 6.2% against the 194p share price at the time of writing, firmly in line with some of the other large, diversified REITs such as Land Securities. Taking these data points together could lead to the conclusion that the shares are fairly priced. The aforementioned 17.6% dividend increase is a big one, driven mostly by the recent merger with LXi. Going forward, dividend growth is expected to moderate and become more in-line with the longer-term growth rate around the 4% mark.

*"Through mergers and day-to-day investment activity, LondonMetric Property is now one of the UK's largest Real Estate Investment Trusts (REITs) with a £3.97bn market capitalisation and a property portfolio of £6.2bn."*

LondonMetric has clearly had a transformational twelve months, capped off by its entry into the FTSE 100. Dividend growth has been strong and the focus on sectors with strong tailwinds and triple net leases is appealing for reasons already discussed. However, the leasing structure isn't a requirement for long-term value creation for shareholders. Companies such as Unite Group and Segro both operate in sectors with higher levels of cost associated with the rental income generated and yet have generated significant shareholder value in the last ten years, in excess of that generated by LondonMetric. The difference remains that both Unite and Segro are sector-focused portfolios, whereas LondonMetric's takes a diversified approach to the long-term goal of compounding shareholder returns. ■

*Please note that this communication is for information only and does not constitute a recommendation to buy or sell the investments mentioned. Investments and income arising from them can fall as well as rise in value. The information and views were correct at time of publication but may have changed at point of reading.*

# INSIGHT

## WHAT THE 2024 GENERAL ELECTION MIGHT MEAN FOR THE MAIN PARTIES

GREG LODGE | PERFORMANCE AND RISK ANALYST


**In just a few short weeks, the United Kingdom will go to the polls. While summer elections aren't unusual, this will be the first July general election since 1945 which, incidentally, resulted in a Labour landslide. When Prime Minister Rishi Sunak stood outside Downing Street in the pouring rain to announce his decision to call the election, it was something of a surprise move. An autumn election had been widely expected, and the Prime Minister had the option of holding off until January 2025. Perhaps most taken aback by the announcement were Sunak's own MPs - polls have consistently shown the incumbent Conservative Party to be 20 points behind Labour.**

So why call the election now when polling suggests an almost certain defeat? The UK has been through a rocky period since the last general election in December 2019, which saw the Conservative Party win a comfortable 80-seat majority. Mere months later, the COVID-19 pandemic arrived, and following close at its heels came a cost-of-living crisis which saw the price of energy and household essentials shoot up. Former Prime Minister Boris Johnson resigned, only to be replaced by Liz Truss, whose short-lived 'mini budget' caused her own downfall just weeks after taking office. With this chaotic background in recent memory, Sunak claims that the economy is now on the right track and that he and his party can deliver stability. Economic growth remains subdued, however, and the base rate has remained at 5.25% since August 2023. This is perhaps not the sort of stability the Prime Minister had in mind. If prospects are unlikely to improve before the latest point at which he could have called the election, Sunak may have felt that there was no better option than to pull the trigger.

*"...whoever wins in July will be hoping for a strengthening economy and any achievements they can point to when the next election rolls around within another five years' time."*

When the Prime Minister announced that he was calling an election, his speech appeared to function as his opening pitch to the voting public. He emphasised his record on tackling inflation and improving economic growth, stating that "this is proof that the plan and priorities I set out are working." He went on to suggest that Labour leader Keir Starmer lacked conviction and that only his Conservative government could maintain economic stability. Starmer was quick to respond; surrounded by Union flags, the central message of his first election speech was one of change. He highlighted "Tory chaos" in Westminster over the previous 14 years and promised a long-term plan to rebuild Britain.

Having announced the date of the election and with Parliament dissolved, the race is on. The Conservatives, Labour and the smaller parties are canvassing, debating and have published their manifestos. The issues at stake are substantial and there are many of them. The economy, healthcare and immigration have frequently polled as some of the nation's top concerns. Housing, climate change and the state of the public sector are also commonly cited. Campaigning is now well underway and both Labour and the Tories have promised to address these issues but whoever ultimately wins will have a substantial amount of work to do if any of them are to have any impact. Let's examine the Conservative and Labour manifestos to get an idea of which direction the winning party could take the country in.

The Conservative manifesto, under the slogan "clear plan, bold action, secure future", promises action on housing, tax, defence and social care. Tax cuts came front and centre. National Insurance would be abolished for the self-employed, who currently pay 6% and 2% depending on their profits. The tax-free personal allowance for pensioners would be increased in a policy which has been dubbed the 'Triple Lock Plus.' On housing, Sunak has announced his intentions to create an "ownership society" but acknowledged ahead of the manifesto launch that getting onto the property ladder has become harder under the Conservative's tenure. To this end, the party has included a goal to build 1.6m homes in England over five years and a return of the Help to Buy scheme, where first-time buyers could claim an equity loan towards the cost of a new home. In addition, the Stamp Duty threshold would be kept at £425,000 for first-time buyers.

The Labour document, straightforwardly titled "Change", emphasised themselves as the party of wealth creation – a strong hint that the party's leadership and priorities have changed since the Jeremy Corbyn era. It presented a raft of policies aimed at improving business investment and productivity – something the party sees as key to increasing living standards. Keen to downplay the 'tax and spend' label, the plans announced here are relatively modest. A plan to raise £8bn in revenue would come from removing the non-domiciled scheme, levying VAT on private schools and further windfall taxes on energy companies. VAT on private school fees has garnered the most press attention, a move which, according to estimates, would raise up to £1.6bn per year. Similarly to the Conservatives, the Labour manifesto also has a housebuilding target – 1.5m in this case, or 100,000 fewer. Where they differ is that Labour has also included measures to address planning rules and the price of land, which the party believes has been a hindrance to development.

As the countdown to polling day progresses, both leading parties have had crises to contend with. Labour has caused controversy amongst supporters over the deselection of candidates and the expulsion of former leader Jeremy Corbyn over his plans to stand against the party as an independent. These contrast to those experienced by the Conservative campaign; Reform UK, already a threat to the Conservative's vote share, has seen Nigel Farage return to frontline politics and may tempt away traditional supporters on the party's right. Sunak's decision to leave the D-Day commemoration event necessitated repeated apologies and may have coloured voters' views. As it stands, the polls have changed little. Labour retain a lead of around 20 points and barring any unexpected events, the next Prime Minister looks set to be Keir Starmer. Nonetheless, whoever wins in July will be hoping for a strengthening economy and any achievements they can point to when the next election rolls around within another five years' time. ■

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Redmayne
Bentley