SKERRITTS VIEW – FEBRUARY 2019

A Report That Doesn't Mention Brexit:

We're not going to mention Brexit at all in this report.

There. We've failed. Not even one sentence in and we've mentioned the "B" word. Having failed so dismally, we may as well carry on and add what we're thinking about it to the millions of other thoughts on the subject.

Actually, we'll not add our thoughts as such, but say what we're doing from an investment perspective. As an investor, and even more as investors who run other people's money for them, we have to leave our personal views to one side. What we *think* about Brexit is irrelevant. What we *think* about Trump is irrelevant. What we *think* about the various factions in the Middle East is irrelevant. As fund and portfolio managers, our personal preferences and beliefs cannot be allowed to get in the way of facts, and the fact of the matter is that the world is in a very unstable place right now. We need to study the facts closely to both safeguard, and profit from, the anomalies that this destabilisation throws up.

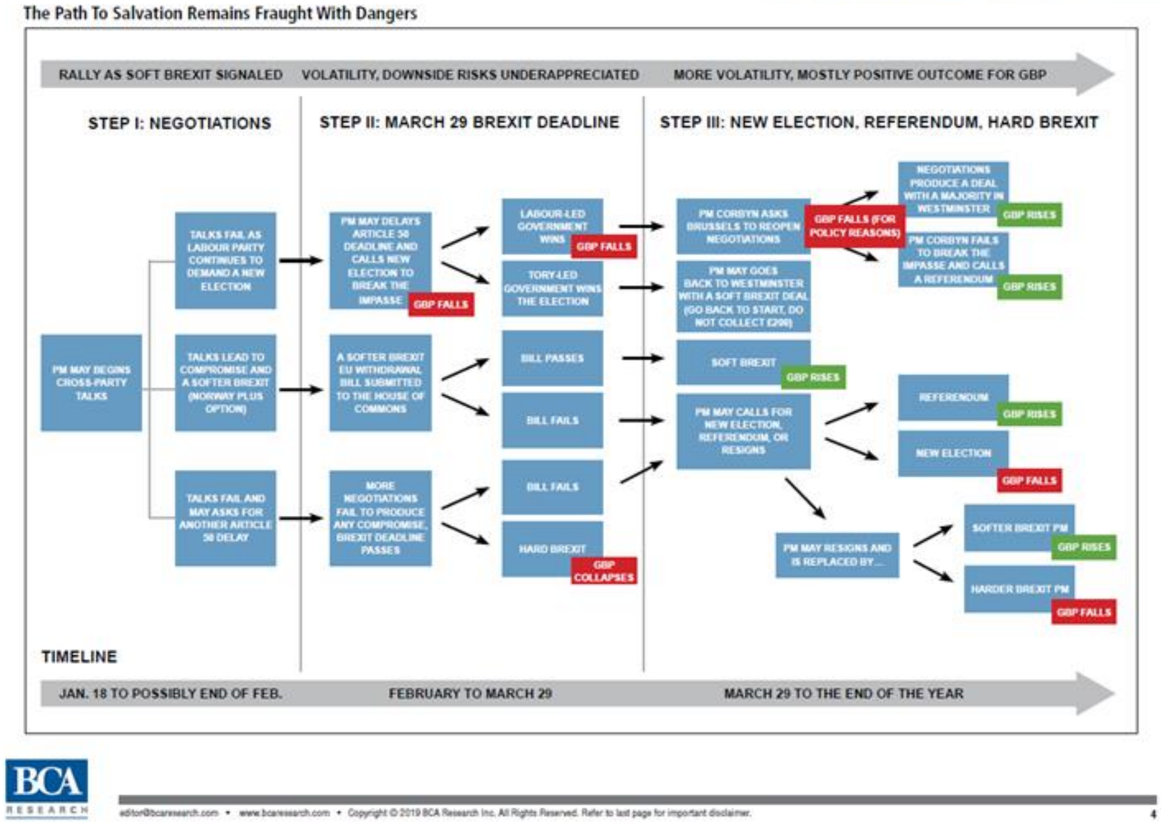
So, back to Brexit. The flowchart that is shown below is by far the best one that we've seen that sets out concisely what the complexities are, how the various decisions can lead to different outcomes, and how, quite frankly, we're still guessing rather than forecasting how it's all going to end up. And, importantly, when.

Investment Is Not Guessment:

We've had an (initially) unconventional policy since late June 2016 – others have since followed – of avoiding virtually any investment in UK assets due to the uncertainty over what happens next. Most UK investors will feel more comfortable investing in their own market even if it offers far less scope to deliver meaningful returns. One benefit of investing in domestic assets is that it eliminates the vagaries of currency movements, as your investment is made in Sterling and comes back to you in Sterling with no conversion rates in between. This is not strictly accurate, but let's go with it. It is even more pertinent for income investors.

We have taken the view that the Brexit uncertainty actually offers *opportunities* to invest elsewhere and, yes, use the weakness in Sterling to our advantage. This is why we've pursued a thematic and tactical path rather than a geographically based one that is favoured by so many fund managers.

The flow chart below however indicates that this may be about to change. Having sat on the sidelines for so long, we are readying ourselves to re-enter the UK field of play as the uncertainties threaten to lift. But not yet. The uncertainties are still very much in place.



From the chart it is clear to see that what happens to Sterling, and by association the FTSE, ranges from collapse to rise in short order. The latest round of votes in the Commons has only clarified the situation in so much as there is a Parliamentary majority to pass a deal, but a deal that the EU say they will not consider, as well as a Parliamentary majority to not leave the EU with no deal, which of course means that there needs to be a deal, which is the one thing that no majority can currently agree on. To make clear decisions in such an uncertain environment equates to guessment, not investment.

Edging Closer:

We are, however, edging closer to a fantastic investment opportunity. *Whatever* the final outcome, the UK market is probably a buy, but at slightly different times. When we talk about "the market", we are talking more in terms of the FTSE 250 and Small Cap sectors which are far more domestically focussed and which contain some good UK companies that have been unfairly marked down because of the uncertainty.

Our view, which is not universally shared, is that in the event of a soft Brexit, or a no Brexit, the opportunities to get involved in the UK are immediate. We have a range of funds ready and waiting on our subs bench.

More controversially, in the event of a no deal Brexit, we expect a severe sell-off in both the UK currency and equities. However, after a while it will become clear that the world has continued to turn and not all UK companies are affected as much as others. At this point, even better bargains may emerge from the initial debris. Again, our subs bench is ready, but will be played later.

Right now though, our investment attention is concentrated on wider issues such as a more dovish Fed and better-than-expected corporate results peeking out from behind the storm clouds that gathered before Christmas. With bond yields tumbling in the US and Italy we're getting a clear "buy" signal for equities…just not the UK ones. Yet.

These are our views and are for professional use only.