

UK equities

Which stocks are most exposed to Brexit?

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- In our House view Tactical allocation we are neutral on UK equities. Whilst the valuation is attractive, the uncertainties around Brexit and commodities give us low visibility.
- Under a Brexit deal scenario we anticipate domestic stocks to outperform international stocks, and for FTSE 250 to outperform FTSE 100. Under a no deal scenario we expect the reverse. For investors wishing to take a view on the outcome, we offer one list of FTSE 100 single stocks with high domestic exposure and another with high international exposure.
- Our preferred strategies within the UK are UK quality and UK diversified dividends, which should perform well under either Brexit outcome.



Source: iStock

Our View

For a full commentary on the Brexit developments up to the Cabinet approval of the draft withdrawal agreement on the 14th of November; as well as our economic and other asset class scenario impacts please see our publication UK economy: Brexit Brief: Endgame; published 14 November 2018.

Meanwhile in this report, we assess the potential exposures of the equity market to a Brexit deal, and a Brexit no deal. The political complications are increasing today and are ever evolving so our analysis mainly focuses on first order impacts of a Brexit deal or no deal, rather than second order impacts (like changes of leadership).

The equity market is exposed to Brexit through five main mechanisms: Sterling; other costs; UK GDP; the gilt yield/equity risk premium; the UK corporate tax rate. As a result we anticipate that companies with high domestic exposure will outperform under a Brexit deal scenario, meanwhile given that we anticipate sterling to weaken to GBPUSD 1.15 under a no Brexit deal scenario we would anticipate international companies to outperform in a no deal scenario. We therefore believe the FTSE 250 would outperform the FTSE 100 in a deal; and vice versa under a no deal scenario.

Related publications

- UK economy: Brexit Brief: Endgame, published 14 November 2018
- UK equities: How are UK equities impacted by Brexit?, published 27 September 2018

Which companies have the most exposure to the differing Brexit outcomes?

In our view political event risk is best managed through diversified portfolios, across regions and asset classes. Given the outcome of the Brexit negotiations are still uncertain and rapidly evolving with now additional political uncertainty, we do not feel confident to try and take a position around the Brexit outcome (see below for our UK most preferred strategies).

In a previous publication (How are UK equities impacted by Brexit published, 27 September 2018), we covered the mechanisms via which the UK equity market can be impacted by Brexit which include: Sterling; other costs; UK GDP; the gilt yield/equity risk premium; the UK corporate tax rate

Broadly speaking companies with a high exposure to the UK and to sterling are more likely to do well under a deal scenario (where we assume UK GDP growth rebounds to 1.8% in 2019 and GBPUSD moves to 1.30 over the next three to six months). Meanwhile companies with a high exposure to international revenues and non sterling currencies are likely to outperform in a scenario of no deal/hard exit, where we anticipate UK GDP growth to fall possibly into a brief recession; and for GBPUSD to fall to 1.15 over the next three to six months.

In this report we identify two lists of companies, one representing the 35 companies in the FTSE 100 with the highest domestic exposure (Table. 1). And the second one identifying the 35 companies in the FTSE 100 with the highest international exposure (Table. 2). These are exposure reference lists, not recommendation lists. Therefore if there are clients with particular over or under exposures at a stock level they have the factual information available to them to address their portfolios should they wish to do so.

Table. 1: MSCI UK stocks with a high domestic exposure

Company	ISIN	Sector	Domestic sales exposure	Foreign sales exposure
Barratt Developments PLC	GB0000811801	Consumer Discretionary	100%	0%
British Land Company PLC	GB0001367019	Real Estate	100%	0%
Wm Morrison Supermarkets plc	GB0006043169	Consumer Staples	100%	0%
United Utilities Group PLC	GB00B39J2M42	Utilities	100%	0%
Persimmon Plc	GB0006825383	Consumer Discretionary	100%	0%
J Sainsbury plc	GB00B019KW72	Consumer Staples	100%	0%
Scottish Mortgage Investment Tr	GB00BLDYK618	Financials	100%	0%
SSE plc	GB0007908733	Utilities	100%	0%
Lloyds Banking Group plc	GB0008706128	Financials	100%	0%
Taylor Wimpey plc	GB0008782301	Consumer Discretionary	100%	0%
Whitbread PLC	GB00B1KJJ408	Consumer Discretionary	100%	0%
Land Securities Group PLC	GB00BYW0PQ60	Real Estate	100%	0%
Berkeley Group Holdings plc	GB00B02L3W35	Consumer Discretionary	100%	0%
Hargreaves Lansdown plc	GB00B1VZ0M25	Financials	100%	0%
Ocado Group PLC	GB00B3MBS747	Consumer Discretionary	100%	0%
Direct Line Insurance Group Plc	GB00BY9D0Y18	Financials	100%	0%
St. James's Place Plc	GB0007669376	Financials	100%	1%
Rightmove plc	GB00BGDT3G23	Communication Services	97%	3%
Next plc	GB0032089863	Consumer Discretionary	97%	3%
NMC Health PLC	GB00B7FC0762	Health Care	92%	8%
Marks and Spencer Group plc	GB0031274896	Consumer Discretionary	90%	10%
Legal & General Group Plc	GB0005603997	Financials	89%	11%
Centrica plc	GB00B033F229	Utilities	86%	14%
Admiral Group plc	GB00B02J6398	Financials	85%	15%
ITV plc	GB0033986497	Communication Services	85%	15%
Standard Life Aberdeen PLC	GB00BF8Q6K64	Financials	84%	16%
BT Group plc	GB0030913577	Communication Services	83%	17%
Royal Mail plc	GB00BDVZY77	Industrials	82%	18%
Tesco PLC	GB0008847096	Consumer Staples	80%	20%
Royal Bank of Scotland Group pl	GB00B7T77214	Financials	79%	21%
SEGRO plc	GB00B5ZN1N88	Real Estate	70%	30%
Aviva plc	GB0002162385	Financials	66%	34%
National Grid plc	GB00BDR05C01	Utilities	65%	35%
Paddy Power Betfair plc	IE00BWT6H894	Consumer Discretionary	61%	39%

Source: Morgan Stanley, FactSet Fundamentals, UBS, as of 15 November 2018

Important note: This is a reference list, of MSCI UK companies with high domestic exposure, it is not a recommendation list. We screen the FTSE 100 for and include the top 35 companies with the most domestic exposure.

Table. 2: MSCI UK stocks with a high international exposure

Company	ISIN	Sector	Domestic sales exposure	Foreign sales exposure
British American Tobacco p.l.c.	GB0002875804	Consumer Staples	1%	99%
Antofagasta plc	GB0000456144	Materials	1%	99%
Randgold Resources Limited	GB00B01C3532	Materials	1%	99%
Mondi plc	GB00B1CRLC47	Materials	1%	99%
Rio Tinto plc	GB0007188757	Materials	1%	99%
Smurfit Kappa Group Plc	IE00B1RR8406	Materials	1%	99%
Evraz PLC	GB00B71N6K86	Materials	1%	99%
Royal Dutch Shell Plc Class A	GB00B03MLX29	Energy	2%	98%
BP p.l.c.	GB0007980591	Energy	2%	98%
CRH Plc	IE0001827041	Materials	2%	98%
Fresnillo PLC	GB00B2QPKJ12	Materials	2%	98%
BHP Billiton Plc	GB0000566504	Materials	3%	97%
Smiths Group Plc	GB00B1WY2338	Industrials	4%	96%
Croda International Plc	GB00BYZWX769	Materials	4%	96%
HSBC Holdings Plc	GB0005405286	Financials	4%	96%
Micro Focus International plc	GB00BD8YWM01	Information Technology	5%	95%
Reckitt Benckiser Group plc	GB00B24CGK77	Consumer Staples	5%	95%
InterContinental Hotels Group Pl	GB00BD8QVH41	Consumer Discretionary	5%	95%
Melrose Industries PLC	GB00BZ1G4322	Industrials	5%	95%
Standard Chartered PLC	GB0004082847	Financials	5%	95%
Anglo American plc	GB00B1XZS820	Materials	5%	95%
Smith & Nephew plc	GB0009223206	Health Care	6%	94%
Diageo plc	GB0002374006	Consumer Staples	6%	94%
Intertek Group plc	GB0031638363	Industrials	7%	93%
RELX PLC	GB00B2B0DG97	Industrials	7%	93%
Johnson Matthey Plc	GB00BZ4BQC70	Materials	7%	93%
Unilever PLC	GB00B10RZP78	Consumer Staples	7%	93%
AstraZeneca PLC	GB0009895292	Health Care	8%	92%
Compass Group PLC	GB00BD6K4575	Consumer Discretionary	10%	90%
Carnival plc	GB0031215220	Consumer Discretionary	10%	90%
GVC Holdings PLC	IM00B5VQMV65	Consumer Discretionary	10%	90%
Burberry Group plc	GB0031743007	Consumer Discretionary	11%	89%
Rentokil Initial plc	GB00B082RF11	Industrials	11%	89%
Rolls-Royce Holdings plc	GB00B63H8491	Industrials	12%	88%

Source: Morgan Stanley, FactSet Fundamentals, UBS, as of 15 November 2018

Important note: This is a reference list, of MSCI UK companies with high international exposure, it is not a recommendation list. We screen the FTSE 100 for and include the top 35 companies with the most domestic exposure.

What are the preferred strategies within the UK market?

Meanwhile within the UK in our preferred strategies we have focused on two themes which we believe should outperform under any of the Brexit outcomes, and taking account of the current global backdrop.

- UK quality - A quality strategy focuses on companies that have higher average profitability, lower financial leverage, and lower earnings variability. As a result, quality tends to outperform during periods of increased equity market volatility and slowing economic growth momentum. We believe the MSCI UK quality index will outperform the MSCI UK index over the coming months, as we expect continued equity market volatility against a weak UK growth backdrop.
- UK diversified dividends - The UK market's 4.8% yield remains attractive against a backdrop of low fixed income yields, in our view. Given the current environment of continued global growth and inflation, along with lingering political and monetary policy risk, we advocate a spread across sectors. We prefer to take a diversified dividend approach in this period of fluctuating bond yields. The outcome of the UK Brexit negotiations may also lead to additional fluctuations in the UK bond yield, with a no deal Brexit viewed as a risk off event and bond yields likely declining, but on the other a deal and transition agreement likely paving the way for more interest rates hikes from the Bank of England and thus an increase in the UK bond yield.

Conclusion

In our view political event risk is best managed through diversified portfolios, across regions and asset classes. Given the outcome of the Brexit negotiations are still uncertain and rapidly evolving with now additional political uncertainty, we do not feel confident to try and take a position around the Brexit outcome. Within our house view tactical asset allocation we are neutral on UK equities. Our preferred strategies within the UK include UK quality and UK diversified dividends, which should navigate well any Brexit scenario.

Meanwhile for those clients wishing to manage specific exposures or taking a view on the outcome of the negotiations, we anticipate that companies with a high domestic exposure are likely to outperform international companies under a deal scenario. And we anticipate that companies with a high international exposure are likely to outperform domestic companies under a no deal scenario. Therefore at an index level the FTSE 250 which is more domestic is likely to outperform under a deal scenario, meanwhile the FTSE 100 which is more international is likely to outperform under a no deal scenario.

At a single company level we have highlighted the 35 companies from the FTSE 100 with the most domestic and the 35 with the most international exposures. These are reference lists of exposure, not recommendation lists.

Appendix

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