FTSE leaders bullish on London's pulling power

Reforms being driven by the UK government and financial regulators are set to re-energise the country's stock market and global status as a listing venue

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The past few years have been challenging for both investors in UK equities and companies listed on Europe's largest exchange.

The performance of the UK stock market has lagged some developed market peers, such as the US, as it has struggled to recover from considerable headwinds, including the covid-19 pandemic and the conflict in Ukraine, as well as the uncertainties created by Brexit.

The meteoric, decade-long rise of private markets has posed a challenge to listed equities, too. Flush with cash and access to cheap funding, private equity funds have bought up a range of successful UK-listed companies. In addition, overseas corporates have taken advantage of depressed valuations in the UK to pounce on acquisition targets. The result is a trend of de-equitisation, which has gathered pace during the last couple of years as there have been a lack of IPOs to compensate for the number of companies exiting the market.

However, there are several factors coming into play in the UK that look set to re-energise the country's equity markets and reinforce its position as a global investment and listing hub.

Building from a position of strength

Our survey of 150 UK FTSE leaders, including chairpersons and CEOs, found an overwhelmingly positive outlook for London equity markets.[i] With the UK government and financial regulator, the Financial Conduct Authority (FCA), both rolling out significant reforms for markets and investors, the country is only likely to get more attractive, our survey indicates.

Despite the turmoil of the past few years, nine in 10 respondents agreed that the UK was still an attractive market for IPOs and capital raising and is likely to get more competitive versus alternative venues over the next three years.

Right rules, right place

One of the main reasons for this confidence is London's high-quality regulatory regime. FTSE leaders told us that the City's comprehensive rulebook made it a better option than many other jurisdictions.

However, policymakers are not resting on their laurels. In the wake of Brexit, the UK is seeking to use its new-found independence to enhance its rules to attract more investors and more listings.

Key reasons why international investors are attracted to the UK. Rated in order of priority – starting with the most important first.

1. High quality regulation
2. Strong financial networks
3. Good governance
4. Transparency
5. The UK hosts many high-quality public companies
6. The most liquid markets in the world after the US
7. An excellent financial services support network
8. A robust common law legal system

The FCA has proposed changes to the UK's listing regime, including the removal of the current two-tier system for share issuance to create a single-tier system that is "more straightforward with a clear purpose".[ii]

More than half (57%) of our surveyed directors are very supportive of this idea, while a further 42% support it but believe it doesn't go far enough to improve the UK's attractiveness as a listing venue.

Almost all the directors in our survey (98%) said they were either quite confident or very confident that these post-Brexit reforms could make the UK a significantly more attractive place to invest.

Leveraging pension pots

If the persistent pension fund outflows from UK equities were to be reversed and instead we had incremental buying interest, it would be to the benefit of valuations and liquidity, and create a more dynamic IPO market.

In a landmark speech at London's Mansion House on 10 July, UK Chancellor Jeremy Hunt unveiled a range of proposals designed to encourage more domestic pension funds to allocate to UK assets.[iii] This was designed to address a long-term decline in UK equity ownership by pension funds, and to take advantage of a rapidly growing pool of capital in the shape of defined contribution (DC) schemes.

Hunt's speech outlined plans to encourage DC funds to allocate "at least 5%" to unlisted equities by 2030, which could unlock as much as £50bn for high-growth companies. Whilst these reforms are primarily aimed at high-growth private companies, we also hope that there is a broader encouragement for pension funds to allocate away from bonds and towards risk assets, which should also include UK-listed companies.

Our survey was conducted before the Chancellor's speech, but three quarters of respondents (75%) said they believe UK pension funds will invest more in the UK over the next two years, and 80% believe they will increase exposure to UK equities. This is notable as our respondees often wear dual hats as company executives but also as guardians of corporate pension funds.

Further afield

It's not just UK investors that can bring capital to their own country's markets. Overseas allocators of capital are being attracted to the UK, particularly as it is currently seen as good value relative to other developed markets such as the US.

In addition, stock exchanges are increasingly collaborating to improve market access for both companies and investors around the world. A key example is the London Stock Exchange's groundbreaking project with the Shanghai Stock Exchange in 2019. Stock Connect allows companies listed in the UK or China to issue, list and trade depositary receipts on the other country's stock exchange.

These trends are also positive for UK markets as they further increase available liquidity and diversify the pool of potential investors.

Onwards and upwards

The UK government and FCA have made strides in tackling some of the factors impacting the competitiveness of London's markets, but there is still work to be done. However, whichever way you look at it, there are plenty of reasons to be cheerful as an investor or a corporate executive in the UK market.

If UK pension funds could be coaxed to meaningfully increase their investments into UK equities, would it make a material difference to valuations and encourage more IPO activity in UK markets?

i The FTSE Leaders on UK Capital Markets survey (May 2023) - Numis commissioned a FTSE Leaders' survey on capital markets. The responses are based on 150 board/senior directors of UK-listed companies, of which 27% work for FTSE 100 companies; 27% for FTSE 250 companies; 33% for AIM companies and 13% for other FTSE listed companies. Respondents are CEOs, CFOs, heads of investor relations, senior independent directors and chairpersons.

ii 'CP23/10 Primary Markets Effectiveness Review: Feedback to DP22/2 and proposed equity listing rule reforms', FCA consultation paper, May 2023. www.fca.org.uk/publication/consultation/cp23-10.pdf

iii 'Chancellor Jeremy Hunt's Mansion House Speech', HM Treasury, 10 July 2023. www.gov.uk/government/speeches/chancellor-jeremy-hunts-mansion-house-speech

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