FUND COMMENTARY – Q2 2025
CT UK GROWTH AND INCOME FUND

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Summary

- The FTSE All-Share index returned 4.4% for the quarter.
- Gross of fees, the fund outperformed its benchmark over the period.[1]
- Key contributors included FirstGroup and Burberry, as well as the zero weight in Shell. The holding in Pearson detracted, as did the lack of exposure to Rolls-Royce and BAE Systems.
- We opened positions in Schroders and Bellway.

Market Background

UK equities posted further gains over the second quarter (Q2), with the FTSE All-Share returning 4.4%.

The period started with a sharp sell-off in global equity markets following US President Trump's "Liberation Day" announcement of sweeping "reciprocal" tariffs, which were much larger than expected in size and scope and stoked fears of higher inflation and lower growth. Given its heavier exposure to defensive sectors, the UK stock market held up better than its US and European counterparts in the sell-off.

Global markets soon rebounded as Trump called a 90-day pause on many of the highest tariffs. Hopes grew that the US could reach trade deals with key partners, with the UK becoming the first country to do so. The UK also signed deals with the EU and India in May, though these had little market impact. However, equities were boosted by optimism that the US and China would reach an agreement on trade.

The FTSE All-Share lagged the global rally, which was led by high-growth names. A stronger pound and lower oil prices also proved unhelpful given the market's sizeable exposure to "dollar earners" and energy stocks. Oil prices declined amid concerns over subdued demand and as the OPEC+ group announced plans to ramp up output. That said, prices spiked briefly in June following a brief spat between Iran and Israel, before later stabilising after the two countries agreed to a US-brokered ceasefire.

Q2 was also marked by concern over rising government debts and deficits in the developed world. Prime Minister Keir Starmer had to make concessions to Labour MPs who rebelled against planned cuts to disability support and benefits, halving the fiscal "headroom" available to Chancellor Rachel Reeves. Shortly thereafter, a spending review highlighted the limited fiscal resources available to boost growth in the near term.

Meanwhile, economic data pointed to a slowdown in the UK after a strong start to 2025. Consumer price inflation remained above the Bank of England's (BoE's) 2% target, rising more than expected in April and May. The BoE reduced interest rates by 25 basis points (bps) in May and then held rates at its meeting in June, though three of the nine rate setters voted for a cut. This was a more dovish outcome than anticipated and stoked expectations of further easing.

By sector, technology fared best in the FTSE All-Share, aided by a global rebound in the sector amid renewed optimism around AI and demand for semiconductors. Industrials also outperformed, as did the interest-rate-sensitive utilities and real estate sectors, which were boosted by hopes of further rate cuts. On the other side, energy was weakest owing to lower oil prices. In addition, healthcare

[1] Past performance does not predict future returns. Please refer to the KIID document found on our website for further information on the fund performance.

underperformed amid concerns over tariffs and Trump's plans to lower the prices of prescription drugs in the US.

Performance

Gross of fees, the fund returned 6.9% over the quarter and outperformed the FTSE All-Share.[1]

Favourable stock selection aided relative returns, especially in healthcare, materials and consumer staples. Sector allocation also added value, particularly our long-term avoidance of energy. The overweights in communication services and industrials were also helpful, but the underweight in financials (where we have no exposure to banks) and overweight in healthcare weighed on relative returns.

At the stock level, key contributors included FirstGroup and Burberry.

FirstGroup reported strong results for its fiscal 2025, with increases in revenue and earnings for both the bus and train businesses. The company also announced a new £50 million share buyback and hiked the full-year dividend. FirstGroup's rail division generates surplus cash, which provides the potential to enhance shareholder returns through a progressive dividend policy, buybacks and bolt-on M&A deals. The firm's regional bus business is now making good progress on improving margins. FirstGroup also boasts the largest electric bus fleet in the UK, which continues to expand. We believe the shift to electric buses could bring about further cost reductions and present additional revenue opportunities for the firm. FirstGroup also has plans to branch into leisure transportation, notably through its contract to operate the London cable car.

While Burberry reported lower full-year revenues and operating profits, the shares outperformed on signs of progress in its "Burberry Forward" strategy reset, which management credited for improved performance in the second half of the firm's financial year. The company also highlighted cost reductions. There is still significant uncertainty over Burberry's near-term earnings trajectory owing to the tough backdrop for luxury goods companies. However, brand resonance remains strong. Having reviewed the strategy he inherited, which was elevating the brand to higher price levels but leaving core Burberry customers behind, the firm's CEO is seeking to reinvigorate the appeal and revenue generation of the brand. We feel the current share price is highly attractive, having only been lower during the global financial crisis in 2008.

In addition, the lack of exposure to Shell was beneficial. The shares sold off particularly sharply following the Liberation Day tariff announcement amid concerns that a trade war could hit demand for oil. Weakness in oil prices over the period was another headwind.

On the other side, detractors included educational publisher Pearson. Q1 results were in line with expectations, with sales edging up, and management reaffirmed its full-year guidance. However, the shares fell amid signs of slowing sales in the Virtual Learning and English Language Learning segments. Concerns about demand for English language learning services were exacerbated after sector peer IDP Education pointed to changes to visa rules in several countries as a potential headwind. The pound strengthening against the dollar – Pearson has significant US earnings – may have weighed on the stock as well. Nevertheless, our investment thesis remains intact. Pearson plans to use AI to create improved, more personalised learning experiences for its customers. While Pearson has had to deal with a painful print-to-digital transition within its US higher education textbook division, management has introduced a digital learning platform called Pearson+, which is aimed at winning back the secondary market for US courseware. The company is also expanding its presence in workforce skills and English-language learning. Core competitive advantages include the firm's strong intellectual property and brand name, as well as potential network effects and switching costs via Pearson's subscription model.

The zero weights in Rolls-Royce and BAE Systems also detracted. Both stocks rose amid optimism about European countries enhancing military capabilities, especially as a NATO summit during the quarter resulted in most members committing to higher defence spending. Additionally, the UK government announced that Rolls-Royce will be part of a consortium to manufacture small modular nuclear reactors.

Activity

We opened positions in Schroders and Bellway.

Global asset manager Schroders is a high-quality franchise trading at an attractive valuation. Despite near-term challenges due to market uncertainty, we feel the business has potential to grow earnings once the wider environment stabilises, driven at first by cost reductions and thereafter by a more balanced combination of revenue growth and margin improvement. We also feel there is room for upside from a re-rating of the stock versus its peers as well as for its peer group as a whole.

Bellway is a quality, highly cash-generative, diversified housebuilder with a consistent track record. Valuations across the homebuilding sector are very attractive, and Bellway is well positioned to capitalise on a recovery as interest rates fall and the UK government pushes to build new homes. Due to the increasing complexity of scheme applications and climate reports, major housebuilders such as Bellway have a huge competitive advantage. Bellway is conservatively run and has a great brand at the lower price spectrum, so the company should be able to achieve higher densities in new sites and has the largest strategic landbank relative to its size. This should provide a high degree of control in releasing more space. In addition, the firm’s return on invested capital (ROIC) is currently lower than its peers, meaning that the discount to its net asset value is larger. Bellway’s chair has expressed confidence in improving the ROIC.

In addition, we added to our existing holdings in Travis Perkins, Castings, Hays and WPP.

We sold out of Direct Line ahead of its takeover by Aviva to help fund the purchases above.

Outlook

The US exceptionalism trade has been challenged this year, while the UK market has outperformed. There are also signs that the long-term structural sales of UK equities by major asset allocators are now ending.

Moreover, the UK is becoming a more attractive place to invest, despite recent concerns about the elevated fiscal deficit. Speculation is already rife around whether the government may be forced to break its pledge not to raise taxes during the current parliament in this year’s autumn budget. Nevertheless, the UK still boasts a relatively stable government. We also expect interest-rate cuts to continue, with the BoE having more room to ease than the Federal Reserve. Along with still-intact Covid-era “piggy banks”, rising house prices and the potential to draw on home equity, this should encourage consumers to spend rather than save. The key ingredients are therefore present for a UK consumer boom, especially if confidence rises.

While there are concerns about the impact of US tariffs on trade under the Trump administration, the UK has so far avoided the worst potential outcomes. We believe this is due in part to the UK market’s heavier exposure to defensive sectors, in which the fund is overweight, and low trade surplus with the US. In addition, while the details are still unclear, the limited UK–US trade deal reached in early May included concessions on some of the higher levies previously announced, including for steel and automobiles.

At the same time, the fund has limited exposure to the top five index constituents (HSBC, Shell, AstraZeneca, Unilever and Rolls-Royce), where most of the gains in the FTSE All-Share have been concentrated this year. We suspect that hedge fund and index repositioning has to some degree been at work behind the gains from these mega-caps given the diverse nature of their business activities.

Meanwhile, with 75% of the UK market’s revenues coming from overseas, UK businesses are generally resilient to any potential domestic economic headwinds. The UK equity market as a whole is still attractively valued relative to its own history and to international peers, despite its outperformance this year. We therefore expect UK companies to remain attractive targets for overseas takeover and private-equity bids.

Our focus remains on long-term ownership and quality stewardship. As patient conviction investors, we will continue to avoid whipsaw momentum trades and concentrate on company fundamentals to target strong risk-adjusted returns.

Key Risks

The value of investments can fall as well as rise and investors might not get back the sum originally invested.

Where investments are in assets that are denominated in multiple currencies, or currencies other than your own, changes in exchange rates may affect the value of the investments.

The fund may invest in derivatives (complex instruments linked to the rise and fall of the value of other assets) with the aim of reducing risk or minimising the cost of transactions. Such derivative transactions may benefit or negatively affect the performance of the fund. The Manager does not intend that such use of derivatives will affect the overall risk profile of the fund.

The fund typically carries a risk of high volatility due to its portfolio composition or the portfolio management techniques used. This means that the fund’s value is likely to fall and rise more frequently and this could be more pronounced than with other funds.

The risks currently identified as applying to the fund are set out in the Risk Factors section of the prospectus.