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Middle East Tensions Prompt Investor Caution in June

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In June, escalating tensions in the Middle East, particularly between Israel and Iran, prompted a noticeable shift in investor behaviour. According to the latest Fund Flow Index from Calastone, a net £98 million was withdrawn from equity funds, marking a pause rather than a widespread retreat from the stock market. Investors, wary of geopolitical uncertainty, redirected capital towards fixed income, safe-haven markets, and lower-cost passive funds.

The data reveals a cautious approach rather than outright panic. Sell orders for equity funds dropped by 2.5% to £11.4 billion, but buy orders fell more sharply by 7.5% to £11.3 billion, the lowest since September 2023. Edward Glyn, head of global markets at Calastone, commented in a recent interview: "June was characterised by caution, not fear. A net outflow from equity funds is relatively rare, occurring in just one in five months over the past decade, so any withdrawal is significant. However, £98 million is negligible against £22.7 billion in total transactions."

Global stock indices showed resilience, dipping initially but recovering by month-end, while bond markets rallied steadily. UK-focused and global equity funds, however, faced challenges. Calastone reported a £594 million net outflow from UK equity funds, reflecting a persistent trend of monthly selling by British investors. Global equity funds saw a £365 million outflow, the first net selling since the market turmoil following Liz Truss' mini-budget in September 2022.

In contrast, European equity funds attracted £301 million in inflows, and North American funds saw £306 million. Bond funds, while still positive, saw inflows decline to £195 million from £328 million in May. Safe-haven money market funds, however, gained traction, with inflows rising to £218 million from £85 million the previous month.

A notable trend was the preference for passive funds, which saw £1.3 billion in new capital despite the broader equity fund outflows. Active funds, particularly UK-focused ones, continued to lose ground. Since January 2015, active UK equity funds have shed £51.8 billion, while passive funds have attracted £7.3 billion. Glyn noted: “Active funds are not only struggling to attract new capital but also losing existing assets. Over the last three years, active funds have seen outflows in eight out of twelve months, compared to just one in twelve for passive funds. Their low-cost structure gives passive funds a clear edge.”

The shift towards passive funds underscores a broader investor focus on cost efficiency, particularly in uncertain times. While Middle East tensions and the Labour government’s economic policies have done little to inspire confidence in UK markets, the resilience of global indices and the appeal of low-cost investments suggest investors are adapting rather than retreating. As geopolitical risks linger, the preference for stability and affordability is likely to shape market flows in the months ahead.