



### Investment Headlines & Comment

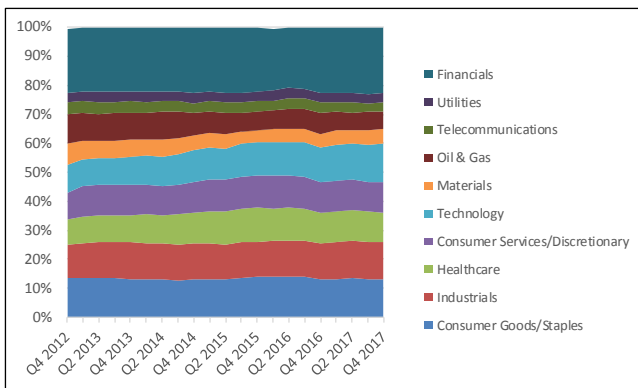
- **Sterling** did well against the major currencies, and US-centred debt underperformed.
- **Gilt** yields (real and nominal) rose. **Corporate bonds** have been well ahead over 12 months.
- A [UN PRI report](#) is due out on how consultants are to “increase responsible investment”.

### Feature Section

This month we look at the way the sector mix in world equity markets has developed over the last 5 years, and we test whether there has been any significant change of scale, either through companies entering or exiting the FTSE All World equity index, or altering the scope of their operations. There has been a wide dispersion of cumulative returns over that period, so even modest sector-led positions away from benchmarks could have produced significant relative returns (good or bad) for active global equity managers.

We start in Figure 1a with the strata chart for the FTSE All-World sector index weightings. This suggests relatively little development in *absolute* values for sector weightings, the main contraction being in Oil & Gas by 4.3% and the main expansion being in Technology by 2.8%. Figure 1b shows the cumulative (i.e. not annualized) returns for the sectors, both by total return and price indices, thus allowing us to infer the contribution of dividends to the total returns (calculated geometrically). It also notes the dispersion (best sector versus worst sector) for each of these measures. The difference between returns in the Technology and Oil & Gas sectors is very striking, and the range on dividends is also noticeable. For our final piece of output, Figure 1c plots the ratio of the start and end weights for each sector versus the cumulative price returns.

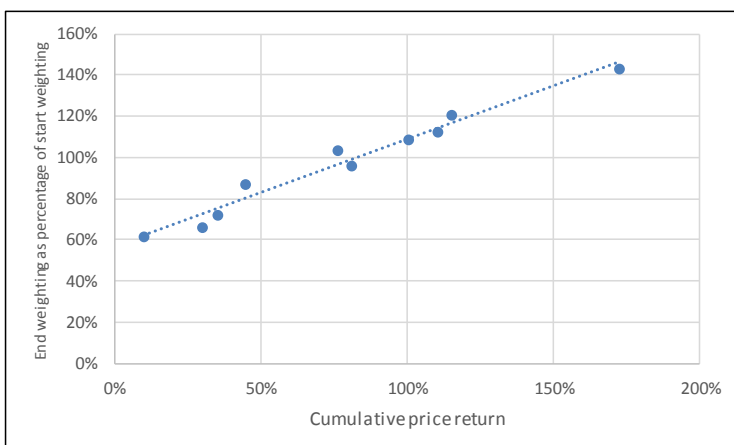
**Figure 1a: World Equity index sector weights**



**Figure 1b: World Equity sector returns (%)**

	Total	Price	Dividends
Consumer Goods/Staples	105	81	13
Industrials	124	100	12
Healthcare	139	115	11
Consumer Services/Discretionary	130	110	9
Technology	197	173	9
Materials	49	30	14
Oil & Gas	30	10	18
Telecommunications	66	35	23
Utilities	75	45	21
Financials	104	76	16
All World	107	82	13
<i>Dispersion at sector level</i>	<b>167</b>	<b>163</b>	<b>14</b>

**Figure 1c: Relationship between price returns and sector development**



This chart shows a very strong linear relationship (with  $R^2$  of around 97%, for those who like statistics), which implies that company transition has been pretty insignificant in the development of the overall index level, although the chart does suggest some positive transition areas (Utilities and Financials) and one marked negative transition area (Materials).

If the Oil & Gas area continues to come under pressure for disinvestments on environmental grounds, we may expect negative transition, but at this stage, they are simply the blob at the bottom left of the line (and pretty much on it), in that their poor price return fits closely with their decline within the overall index weightings.



**Asset Returns and Financial Measures [in Sterling unless marked otherwise]**

The cells in bold with light shading show the best and worst performing asset classes from each column. The commodities and \$-based and unhedged-£-conversion hedge fund returns are excluded from that.

[NB Future returns cannot be inferred from this table alone, but coupled with other items within *Update*, readers can make inferences as to whether they should be higher or lower than the past returns shown below.]

**Table 1: Investment Data to 31 January 2018**

Asset Class	1 month (%)	3 months (%)	12 months (%)	3 years (% p.a.)	5 years (% p.a.)	10 years (% p.a.)	20 years (% p.a.)
UK Equities	-1.9	1.0	11.3	8.4	8.5	7.1	5.9
Overseas Equities	0.6	2.4	13.6	15.2	14.6	10.7	7.9
US Equities	0.6	2.9	11.9	<b>16.6</b>	<b>18.4</b>	<b>13.6</b>	7.4
Europe ex UK Equities	1.4	0.4	17.8	13.3	11.1	7.2	8.3
Japan Equities	-0.6	1.4	11.7	15.5	14.7	8.2	4.9
Pacific ex Japan Equities	1.3	3.5	20.6	13.7	10.4	9.8	<b>10.4</b>
Emerging Markets	<b>3.1</b>	<b>5.1</b>	<b>25.2</b>	14.3	8.5	7.8	10.0
UK Long-dated Gilts	-3.1	0.0	3.4	2.9	7.9	8.0	7.2
UK Long-dated Corp. Bonds	-1.2	1.3	7.0	4.1	8.2	8.1	7.4
UK Over 5 Yrs Index-Linked Gilts	-2.8	0.0	-0.5	6.1	7.9	8.3	7.8
High Yield (Global)	-3.5	-4.9	-2.9	9.4	7.8	11.9	7.6
Overseas Bonds	-3.7	-4.3	-5.6	4.2	3.0	6.2	5.3
Property *	1.4	3.4	11.2	9.1	11.5	5.6	8.7
Cash	0.0	0.1	0.4	<b>0.5</b>	<b>0.5</b>	<b>1.1</b>	<b>3.2</b>
Commodities £-converted	-4.9	-1.1	-5.1	-3.3	-11.0	-7.1	-0.1
Hedge Funds original \$ basis *	1.1	2.6	8.6	4.3	5.0	3.2	6.5
Illustrative £-converted version *	1.1	1.8	-0.8	9.3	8.9	7.3	7.6
Euro relative to Sterling	-1.3	-0.1	2.0	5.3	0.5	1.6	-
US \$ relative to Sterling	-4.9	-6.6	-11.5	1.8	2.2	3.4	0.7
Japanese Yen relative to Sterling	-1.8	-2.8	-8.8	4.4	-1.4	3.1	1.5
Sterling trade weighted	2.3	2.0	2.9	-3.4	-0.2	-1.9	-1.1
Price Inflation (RPI) *	0.8	1.1	4.1	2.6	2.4	2.8	2.8
Price Inflation (CPI) *	0.3	0.8	2.9	1.6	1.5	2.4	2.0
Price Inflation (RPIX) *	0.8	1.0	4.2	2.7	2.5	3.2	2.9
Earnings Inflation **	-0.1	0.1	2.4	2.6	2.0	1.9	3.0
All Share Capital Growth	-2.0	0.5	7.2	4.5	4.7	3.3	2.5
Dividend Growth	0.2	1.6	12.8	8.4	6.5	4.3	4.4
Earnings Growth	2.1	11.6	58.4	-2.8	-4.2	-2.9	2.5

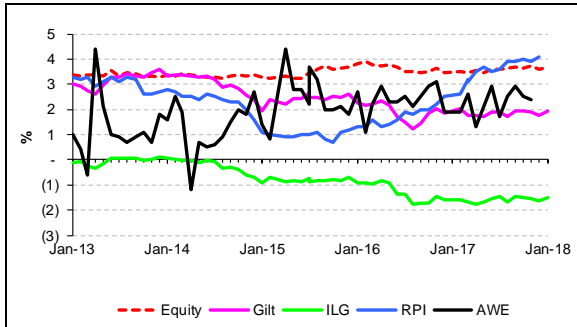
Note: All market returns are total returns for pension funds with income reinvested monthly. Indices used are as follows:

- UK Equities (incl. dividends and earnings) – FT-A All Share.
- Overseas Equities (incl. regions) – blend of FT All-World / World subindices
- Emerging Markets from MSCI US \$ based total return index (overall Index to 31 Oct 2001, Free Index from 1 Nov 2001 to take account of foreign investment restrictions), conversion to UK £ by J&A.
- UK Bonds – FT-A indices (Gilts Over 15 Years, ILG Over 5 Years)
- UK Corporate Bonds – iBoxx Non-Gilt Over 15 Year index (all credit ratings combined)
- High Yield – Merrill Lynch Global, £ Unhedged
- Overseas Bonds – JP Morgan Traded Unhedged World ex UK
- Property – MSCI IPD UK Monthly Property Index
- Commodities – GSCI Total Return, converted to UK £ by J&A
- Hedge Funds Composite – HFRI US \$ based total return index plus converted to UK £ by J&A. NB A smooth “cash+x%” return will only be shown in the base ‘hedged’ currency, here the US \$.
- Cash – an indicative index based on the three-month London Interbank Sterling mid-rate, calculated internally by J&A
- Price and earnings inflation – RPI, CPI, RPIX, and Average Weekly Earnings (whole economy, not seasonally adjusted, latest provisional data)
- Currency data – London close, from the Financial Times
- \* denotes data lagged by 1 month, \*\* by 2 months – these reflect the later publication dates of these data items.

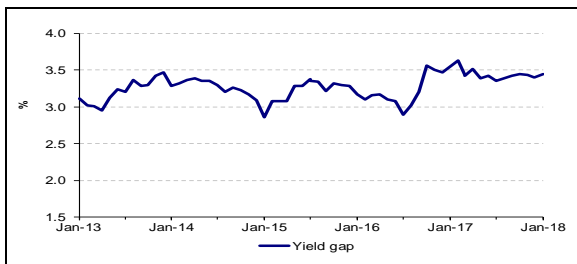


## Yields and Yield Gaps

Figure 2: Yields, Inflation and Yield Gaps



The yield gap is a measure of expected average future inflation, derived as long bond yield minus ILG yield.

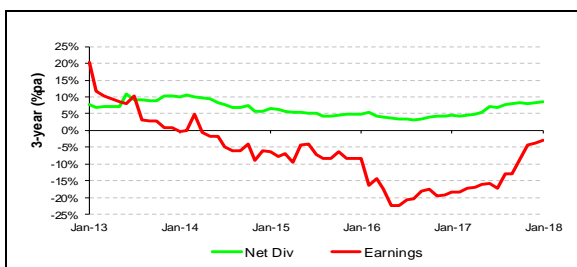
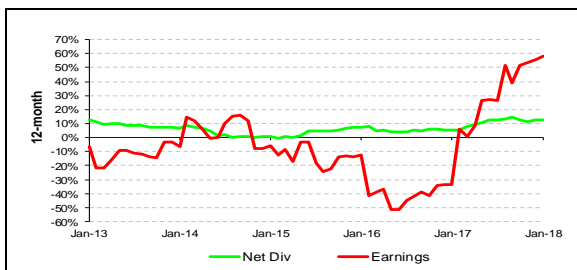


The gap gives a current expectation around 3.5% for longer-term inflation + risk premium for gilts, relative to index-linked gilts.

## Growth in Earnings and Dividends

These charts show movements in rolling 12-month and 3-year dividend and earnings growth for UK Equities over the last 5 years. [NB the charts have different scales]

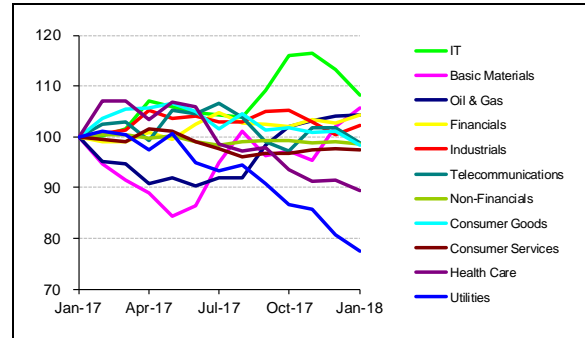
Figure 3: Dividend & Earnings Growth



Note: Earnings data from mid 2015 onwards is under review by FTSE Russell as one-off events may be affecting the prospective P/E ratios

## UK Equity Sector Returns

Figure 4a: Sectors relative to All Share



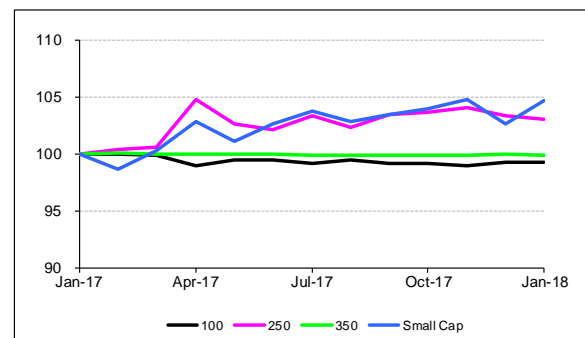
Note: Sector labels for relative lines are in end-value order

There was a fall this month in the rolling 12-month sector dispersion (from 35% to 31%).

(% absolute return)	1 mth	3 mth	12 mth
Oil & Gas	-1.7	3.2	16.0
Basic Materials	1.7	9.8	17.6
Industrials	-0.1	-1.9	13.7
Consumer Goods	-4.6	-2.4	9.4
Health Care	-4.3	-3.6	-0.6
Consumer Services	-2.0	1.8	8.4
Telecommunications	-5.0	2.6	9.8
Utilities	-5.9	-9.6	-13.9
Non-Financials	-2.5	0.2	9.6
Financials	-0.5	3.3	15.9
IT	-6.4	-5.8	20.3
All Share	-1.9	1.0	11.3

## UK Equity Size Returns

Figure 4b: Size groups relative to All Share



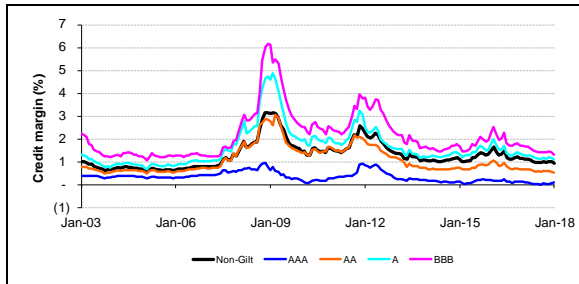
Mid Cap fell but Small Cap rose in relative terms this month.

Sources for charts on this page:  
Financial Times, Office for National Statistics, J&A



**Bond market information**

**Figure 5: £ Non-Gilt Credit Margins**



**Table 2a: Over 15 Yr Corporate Yields & Margins**

Month End	iBoxx Corp AA Y'ld (%)	FT 20 yr Gilt (%)	Margin (%)
Aug '17	2.38	1.72	0.66
Sep '17	2.62	1.94	0.68
Oct '17	2.62	1.93	0.69
Nov '17	2.64	1.89	0.75
Dec '17	2.42	1.77	0.65
Jan '18	<b>2.56</b>	<b>1.95</b>	<b>0.61</b>

**Tables 2b, 2c: £ Market Size (£bn) and Maturity**

Category	Mkt Val @ Jan 18 & 15, 12			Weight (%)
	Jan 18	Jan 15	Jan 12	
Gilts (41)	1,336	1,279	1,018	70.3
Non Gilts (1,043)	565	567	474	29.7
AAA (128)	107	101	123	5.6
AA (152)	78	95	67	4.1
A (335)	166	188	162	8.7
BBB (428)	215	183	123	11.3

Category	Mkt Val @ Jan 18 & 15		W't (%)	Dur'n (yrs)
Gilts (41)	1,336	1,279	70.3	11.5
< 5 Yrs (12)	399	328	21.0	2.7
5-15 Yrs (11)	355	399	18.7	8.0
> 15 Yrs (18)	581	552	30.6	19.7
Non Gilts (1,043)	565	567	29.7	8.2
< 5 Yrs (362)	180	148	9.5	2.9
5-15 Yrs (448)	234	243	12.3	7.7
> 15 Yrs (233)	151	176	7.9	15.5

**£ Gilt Market “main” Issuance**

- o £2.50bn ¾% 2023 (2.07x, 0.99%, 0%, Dec 17)
- o £2.59bn 1¼% 2027 (2.38x, 1.29%, 15%, Nov 17)
- o £2.25bn 1¾% 2037 (2.21x, 1.79%, 0%, Oct 17)
- o £1.00bn 1/8% IL 2026 (2.82x, ry -1.81%, 0%, Nov 17)

Note: Issuance amounts are nominals. The first % figure in each row is the yield or real yield. The second % figure is the additional amount taken up under the Post Auction Option Facility (PAOF), as a % of the amount of the issue. PAOF does not apply for syndication cases.

**Tables 2d, 2e: € Market Size and Maturity (Jan 18)**

Category	Mkt Val (€bn)	Weight (%)
Sovereigns (356)	6,064	59.8
Non Sovereigns	4,079	40.2
AAA (813)	1,153	11.4
AA (637)	993	9.8
A (915)	879	8.7
BBB (1,220)	1,055	10.4

Category	Mkt Val (€bn)	Weight (%)
1 – 3 Yrs (892)	2,247	22.2
3 – 5 Yrs (1,024)	2,163	21.3
5 – 7 Yrs (831)	1,690	16.7
7 – 10 Yrs (762)	1,865	18.4
10+ Yrs (432)	2,178	21.5

**Table 2f: Breakdown of £ Index-Linked Market**

Category (Number of issues)	Mkt Val (£bn @ Jan 18 & 15)		W't (%)	Dur'n (yrs)
Gilts (28)	640	504	100.0	22.8
< 5 Yrs (3)	59	52	9.2	3.2
5 – 15 Yrs (7)	150	131	23.4	9.5
> 15 Yrs (18)	431	321	67.4	30.1

**Table 2g: High Yield bond yields (BB-B indices)**

Month End	US (%)	Euro (%)	Sterling (%)
Aug '17	5.28	3.00	5.33
Sep '17	5.21	2.92	5.25
Oct '17	5.22	2.73	5.15
Nov '17	5.39	2.88	5.37
Dec '17	5.45	2.95	5.40
Jan '18	<b>5.48</b>	<b>2.95</b>	<b>5.39</b>

Sources: DMO, FTSE, iBoxx, J&A, MLX

