



Investment Headlines & Comment

- A good month for equities and for Sterling.
- Nominal & real gilt yields rose – is high issuance finally felt?
- UK Equity earnings data still generates anomalies.

Feature Section

This month we consider how much the gilt market has changed as result of the recent issuance and Quantitative Easing. We last looked at the market’s profile in our October 2018 edition. Figure 1a below shows the profile then, and Figure 1b shows the profile at the end of August 2020 – the same vertical scale is used for both. Figure 1c then identifies where the new issuance has been focused, and how the Bank of England’s interventions have been allocated.

Figure 1a: Gilt nominals – Oct 18

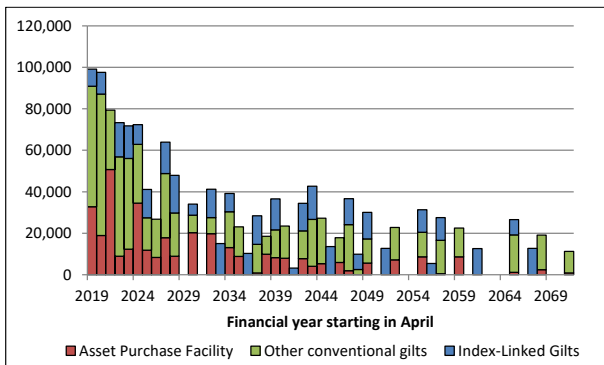


Figure 1b: Gilt nominals – Aug 20

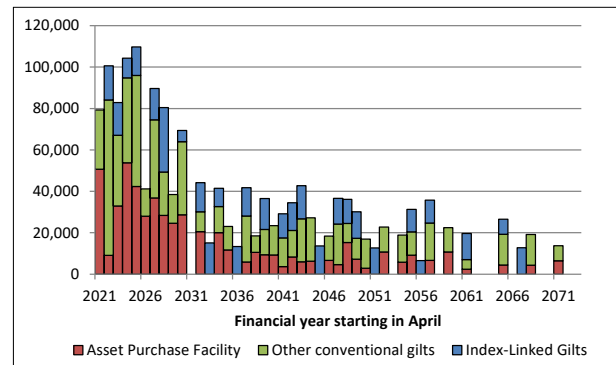
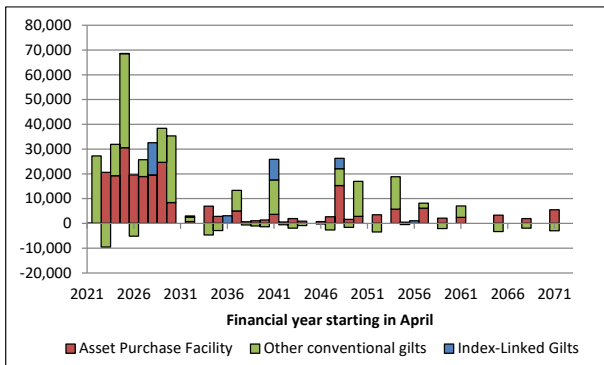


Figure 1c: Intervening issuance



Sources: DMO, Bank of England

gilts by the Bank from long-term investors (although admittedly the amounts involved are relatively small).

From Figure 1b, the Asset Purchase Facility will account for around 40% of maturities in the next 5 financial years (and 46% in the following 5 years). So, the Bank of England’s future behaviour could have a dramatic effect on gilt yields. If they continue with their current policy of using maturity proceeds to purchase further gilts, that will soften the potential for rises in gilt yields. However, whilst Quantitative Easing has been around for over a decade, it still seems desirable that it will not be around forever, not least because it has the potential to create undesirable levels of inflation, but also because it is seen as increasing inequality.

It is an interesting question as to whether the Bank of England would change its policy ahead of seeing whether the Federal Reserve could start unwinding its stimulus programme without alarming markets – which in turn may depend on who gets into the White House next, and whether reducing inequality matters to them.



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 August 2020

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	2.4	0.3	-12.6	-2.8	3.2	5.9	3.7
Overseas Equities	4.2	6.8	7.5	8.7	14.5	12.4	6.2
US Equities	5.5	7.5	12.6	13.5	17.9	16.9	5.2
Europe ex UK Equities	2.1	5.3	0.2	2.4	9.4	8.5	6.9
Japan Equities	5.7	-2.4	0.7	3.0	9.2	8.5	2.6
Pacific ex Japan Equities	1.9	12.0	7.9	3.9	13.3	8.2	8.9
Emerging Markets	2.5	13.0	6.9	2.7	12.6	5.8	8.3
UK Long-dated Gilts	-5.6	-6.3	3.4	7.0	8.4	8.3	7.1
UK Long-dated Corp. Bonds	-3.2	0.8	5.0	6.4	8.8	7.9	7.6
UK Over 5 Yrs Index-Linked Gilts	-4.9	-3.7	-1.8	4.8	7.9	8.7	7.4
High Yield (Global)	-0.5	0.1	-3.8	3.1	9.4	8.2	7.6
Overseas Bonds	-2.5	-4.8	-4.6	2.7	7.2	3.6	5.3
Property *	0.1	-0.8	-2.8	3.7	5.0	7.7	7.2
Cash	0.0	0.0	0.6	0.7	0.6	0.6	2.4
Commodities £-converted	3.0	5.8	-30.4	-8.4	-5.7	-6.4	-3.4
Hedge Funds original \$ basis *	2.9	7.4	1.8	2.7	3.0	3.9	4.9
Illustrative £-converted version *	-3.1	3.2	-5.0	2.9	6.6	5.7	5.6
Euro relative to Sterling	-0.9	-0.8	-1.3	-1.1	4.1	0.8	1.9
US \$ relative to Sterling	-1.5	-7.3	-8.6	-1.1	2.9	1.4	0.4
Japanese Yen relative to Sterling	-1.1	-5.1	-7.9	0.3	5.8	-0.8	0.5
Sterling trade weighted	1.0	2.8	4.4	1.9	-3.0	-0.4	-1.1
Price Inflation (RPI) *	0.5	0.5	1.6	2.5	2.6	2.8	2.8
Price Inflation (CPI) *	0.5	0.6	1.1	1.9	1.8	2.0	2.1
Price Inflation (RPIX) *	0.5	0.8	1.9	2.6	2.7	2.9	2.9
Earnings Inflation **	0.6	-11.0	-1.5	1.4	1.9	1.8	2.7
All Share Capital Growth	1.8	-0.6	-15.4	-6.4	-0.5	2.2	0.2
Dividend Growth	-4.7	-5.7	-11.5	0.7	4.0	5.2	4.2
Earnings Growth	-25.1	-29.8	-31.6	0.8	-2.2	-1.5	1.7

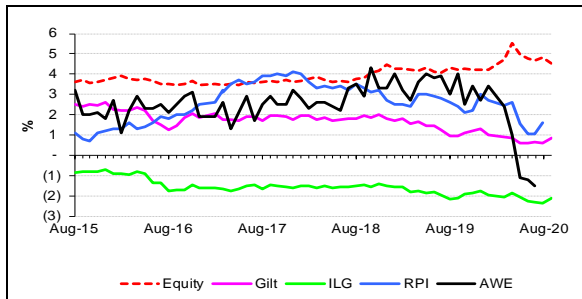
Note: All market returns are total returns for pension funds with income reinvested monthly. Indices used are as follows:

- UK Equities (incl. dividends and earnings) – FT-A All Share.
- Overseas Equities (incl. regions) – blend of FT All-World / World sub-indices
- 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 – ICE 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.

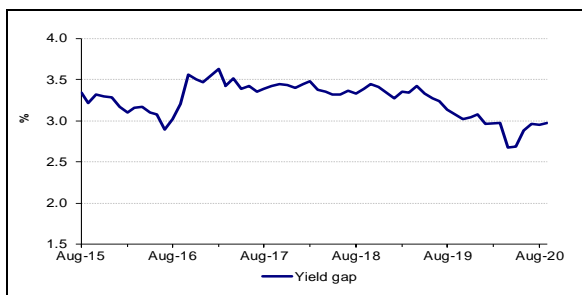


Yields and Yield Gaps

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.

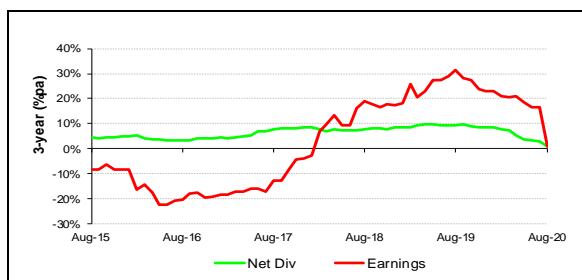
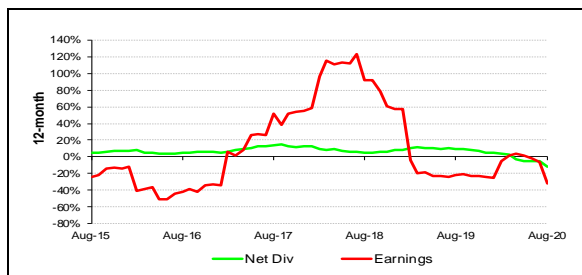


The gap gives a current expectation around 3.0% for longer-term inflation including the risk premium for gilts, relative to index-linked gilts.

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]

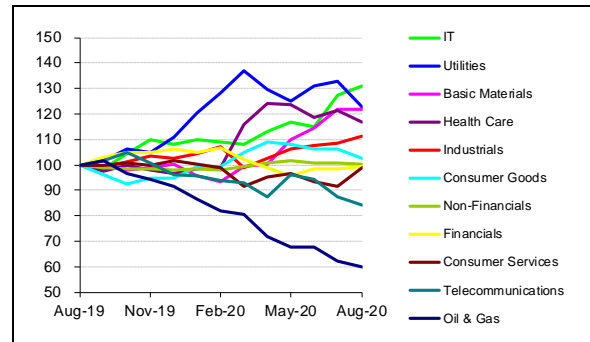
Figure 3: Dividend & Earnings Growth



Note: Earnings data from mid-2015 onwards is no longer reliable as one-off events may be affecting the prospective P/E ratios

UK Equity Sector Returns

Figure 4a: Sectors relative to All Share



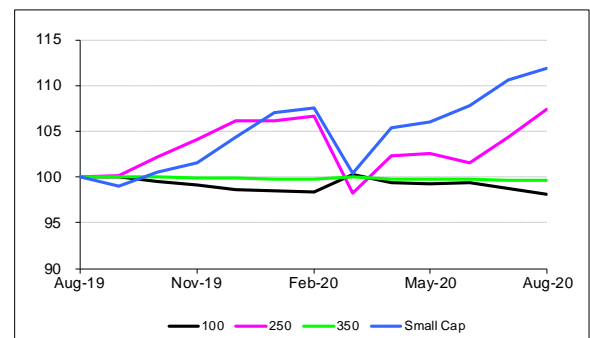
Note: Sector labels for relative lines are in end-value order

There was a fall this month in the rolling 12-month sector dispersion (down from 82% to 71%).

(% absolute return)	1 mth	3 mth	12 mth
Oil & Gas	-1.1	-11.5	-47.7
Basic Materials	2.7	11.3	6.5
Industrials	5.1	5.0	-2.9
Consumer Goods	-1.1	-4.8	-10.3
Health Care	-1.4	-5.2	1.9
Consumer Services	10.6	2.5	-13.7
Telecommunications	-1.2	-12.1	-26.3
Utilities	-5.4	-1.8	7.1
Non-Financials	2.0	-1.0	-12.4
Financials	3.6	4.2	-13.1
IT	5.4	12.4	14.5
All Share	2.4	0.3	-12.6

UK Equity Size Returns

Figure 4b: Size groups relative to All Share



Mid and Small Cap both 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

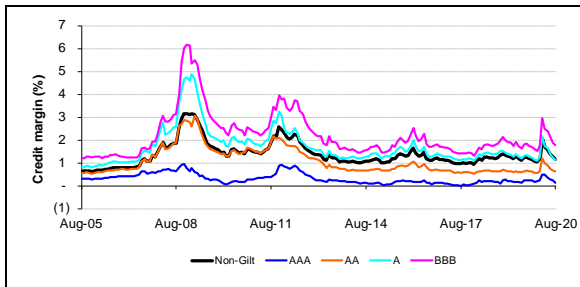


Table 2a: Over 15 Yr Corporate Yields & Margins

Month End	iBoxx Corp AA Y'ld (%)	FT 20 yr Gilt (%)	Margin (%)
Mar '20	2.30	0.83	1.47
Apr '20	1.57	0.60	0.97
May '20	1.52	0.59	0.93
Jun '20	1.45	0.64	0.81
Jul '20	1.37	0.60	0.77
Aug '20	1.60	0.86	0.74

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

Category	Mkt Val @ Aug 20 & 17, 14			Weight (%)
	Aug 20	Aug 17	Aug 14	
Gilts (47)	1,677	1,358	1,181	71.5
Non-Gilts (1,165)	668	579	554	28.5
AAA (150)	135	112	104	5.8
AA (152)	82	90	94	3.5
A (361)	187	164	179	8.0
BBB (502)	263	213	177	11.2

Category	Mkt Val (£bn @ Aug 20 & 17)		W't (%)	Dur'n (yrs)
Gilts (47)	1,677	1,358	71.5	13.1
< 5 Yrs (11)	388	380	16.5	2.9
5-15 Yrs (13)	486	380	20.7	7.9
> 15 Yrs (23)	803	598	34.3	21.2
Non-Gilts (1,165)	668	579	28.5	7.9
< 5 Yrs (421)	228	181	9.7	2.7
5-15 Yrs (510)	281	246	12.0	7.4
> 15 Yrs (234)	159	152	6.8	16.4

Tables 2d, 2e: € Market Size and Maturity (Aug 20)

Category	Mkt Val (€bn)	Weight (%)
Sovereigns (397)	7,374	59.4
Non-Sovereigns	5,036	40.6
AAA (975)	1,325	10.7
AA (811)	1,229	9.9
A (1,243)	1,114	9.0
BBB (1,666)	1,367	11.0

Category	Mkt Val (€bn)	Weight (%)
1 – 3 Yrs (1,228)	2,596	20.9
3 – 5 Yrs (1,348)	2,554	20.6
5 – 7 Yrs (997)	1,976	15.9
7 – 10 Yrs (852)	2,153	17.3
10+ Yrs (667)	3,130	25.2

Table 2f: Breakdown of £ Index-Linked Market

Category (Number of issues)	Mkt Val (£bn @ Aug 20 & 17)		W't (%)	Dur'n (yrs)
Gilts (28)	780	668	100.0	22.0
< 5 Yrs (3)	70	51	9.0	3.2
5 – 15 Yrs (8)	198	152	25.4	9.9
> 15 Yrs (17)	512	465	65.6	29.3

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

Month End	US (%)	Euro (%)	Sterling (%)
Mar '20	8.26	6.51	8.75
Apr '20	6.94	4.94	7.38
May '20	6.04	4.38	6.60
Jun '20	5.96	4.05	5.88
Jul '20	5.11	3.69	5.62
Aug '20	4.98	3.45	5.32

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

£ Gilt Market “main” Issuance

- o During the expanded gilt issuance programme, there is insufficient space here to list all the auction / tender exercises, so please click [here](#) for the details.

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. No PAOF applies for tender or syndication cases.

