



Investment Headlines & Comment

- Russian action in Ukraine caused significant volatility.
- There was heavy demand for the new conventional 2073 gilt.
- The PPI has issued interesting [research](#) on DC arrangements.

Feature Section

This month, we return to the subject of Absolute Return / Diversified Growth funds. We last looked at these in our [April 2020](#) issue, when considering how much impact there had been from the first “pandemic-affected” quarter in Q1 2020. This time we consider the 5-year gross of fees risk-return plots for those funds having such records at the year ends of *both* 2016 and 2021 (i.e. funds which have two *non-overlapping* 5-year periods). In our peer group there are 15 such funds.

Figure 1a shows the peer group plotted as groups at the end of Q4 2016 and Q4 2021, looking at the annualized 5-year return, and the associated volatility. The second 5 years generally saw lower returns and higher volatility. Figure 1b links up the quarter ends’ points pairwise by manager, including an arrow head on each pair to show the direction of change from Q4 2016 to Q4 2021 (users may have to increase the magnification on screen to spot some of them – we have expanded the axes in Figure 1b to try to help here). Figure 1c shows the results for each fund from combining the two 5-year periods into a single 10-year period.

Figure 1a: Peer group by date

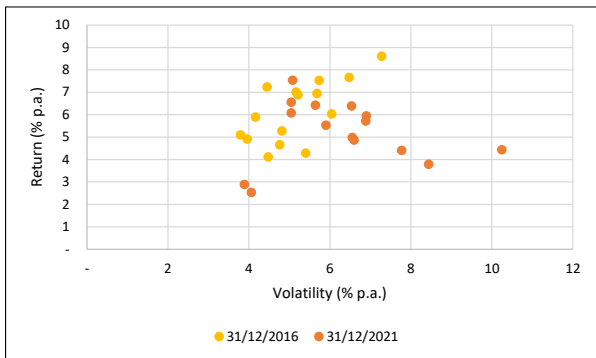
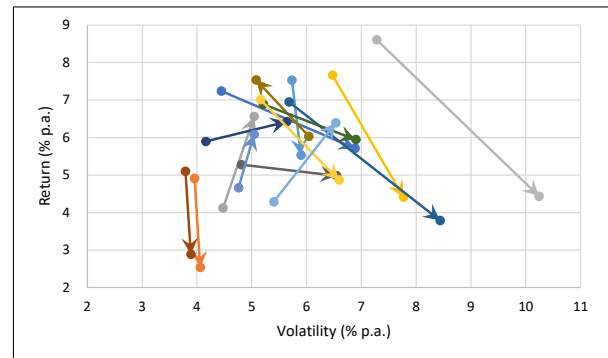


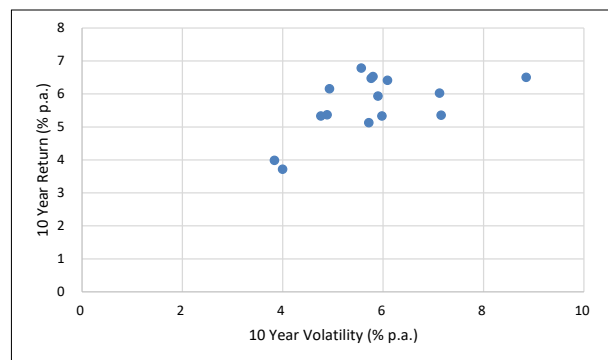
Figure 1b: Peer group movement by manager



Of the 15 funds involved, only one saw clearly lower volatility in the second 5-year period, although it is fair to note that three managers did have broadly unchanged volatility. Of the other 11 funds, 6 saw their volatility up by over 30% in relative terms, largely from catching the impact of the pandemic-led market falls and subsequent bounceback.

From a return perspective, only 5 funds produced higher returns in the second 5-year period than in the first. Of the other 10 funds, 8 saw their returns down by over 20% in relative terms (hence a lot of south-easterly arrows in Figure 1b). So, investors making any manager selections in 2016 under the influence of past returns may have been subsequently disappointed.

Figure 1c: 10-year peer group at Q4 2021



Within Figure 1c, the top-right “high-ish return, high volatility” outlier is a fund generally fully invested in risk-on assets, known for making relatively little change to its asset allocation. Interestingly, at the opposite end, the two “low return, low volatility” outliers have contrasting approaches to each other – one makes significant use of “relative value” pairs, whilst the other only has a relatively narrow toolkit of assets which it is prepared to use. However, both funds have still produced returns in excess of RPI inflation for the 10-year period, though 10-year inflation (at 2.9% p.a.) has hardly been a demanding target. Who knows how the next 10 years will turn out??



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 28 February 2022

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	-0.5	3.8	16.0	5.8	4.7	6.9	6.3
Overseas Equities	-2.6	-5.1	12.6	14.0	10.5	12.7	8.9
US Equities	-3.0	-6.0	19.1	17.9	13.5	16.6	7.6
Europe ex UK Equities	-5.1	-6.8	7.8	9.5	7.5	9.3	9.7
Japan Equities	-0.9	-5.0	-0.6	7.0	4.8	9.0	6.1
Pacific ex Japan Equities	-1.0	-4.0	-6.5	7.8	6.4	7.9	10.2
Emerging Markets	-3.0	-4.3	-6.6	6.1	5.8	5.4	9.7
UK Long-dated Gilts	-2.9	-13.9	-4.0	2.2	1.7	5.1	6.1
UK Long-dated Corp. Bonds	-5.3	-13.8	-7.6	3.1	2.4	5.9	6.0
UK Over 5 Yrs Index-Linked Gilts	-0.5	-9.4	10.1	6.5	4.0	6.8	7.5
High Yield (Global)	-2.1	-4.5	0.1	3.6	2.6	7.1	7.8
Overseas Bonds	-0.8	-4.6	-1.6	1.4	0.5	2.5	4.6
Property *	1.2	7.5	20.7	7.0	7.8	8.8	7.8
Cash	0.1	0.1	0.2	0.4	0.5	0.5	2.1
Commodities £-converted	8.8	28.8	53.0	10.2	5.5	-2.7	1.1
Hedge Funds original \$ basis *	-2.1	-2.9	6.6	8.8	6.4	5.3	5.7
Illustrative £-converted version *	-1.1	-0.8	9.1	8.1	5.0	7.0	6.0
Euro relative to Sterling	0.2	-1.6	-3.6	-0.7	-0.4	0.0	1.6
US \$ relative to Sterling	0.0	-1.4	4.2	-0.3	-1.5	1.8	0.3
Japanese Yen relative to Sterling	0.0	-2.8	-3.6	-1.4	-2.1	-1.8	1.0
Sterling trade weighted	-0.1	1.6	1.4	0.9	1.3	0.1	-1.0
Price Inflation (RPI) *	0.0	1.8	7.8	3.9	3.7	2.9	3.1
Price Inflation (CPI) *	-0.2	1.1	5.4	2.6	2.5	2.0	2.2
Price Inflation (RPIX) *	0.0	1.9	8.0	4.1	3.7	3.0	3.1
Earnings Inflation **	4.8	6.0	5.1	4.5	4.0	2.9	3.0
All Share Capital Growth	-0.8	3.3	12.3	2.3	1.0	3.2	2.6
Dividend Growth	1.2	-1.9	10.5	-8.8	-1.7	2.4	3.2
Earnings Growth	3.2	-6.6	59.8	2.1	14.8	-0.3	4.7

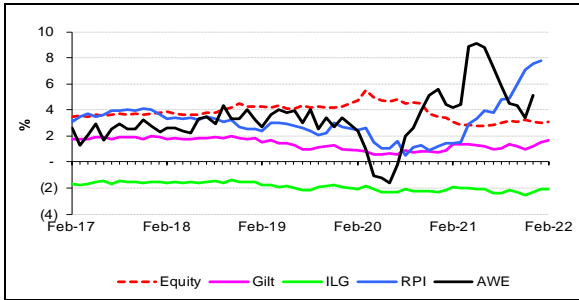
Note: All market returns are total returns for pension funds with income reinvested monthly. Indices used are as follows:

- 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.

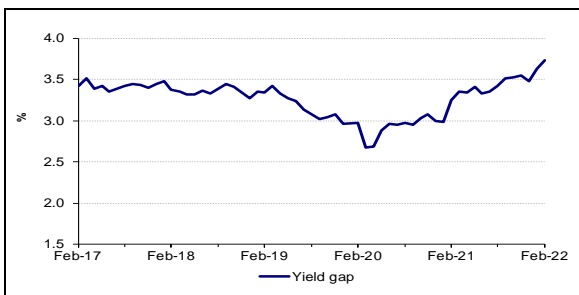


Yields and Yield Gaps

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.

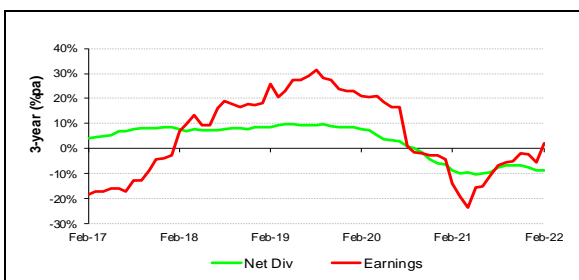
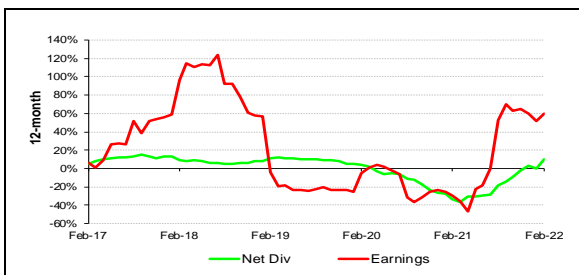


The gap gives a current expectation around 3.7% for longer-term inflation including the (unknown) risk premium for gilts, relative to index-linked gilts.

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]

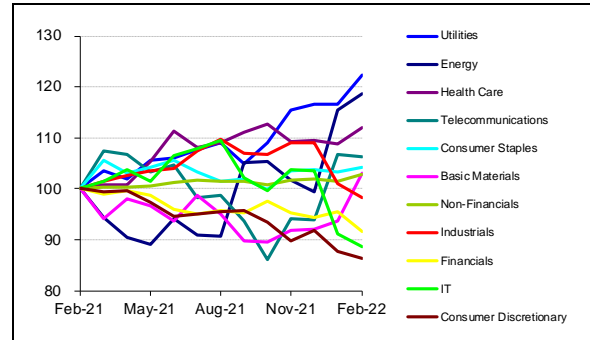
Figure 3: Dividend & Earnings Growth



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



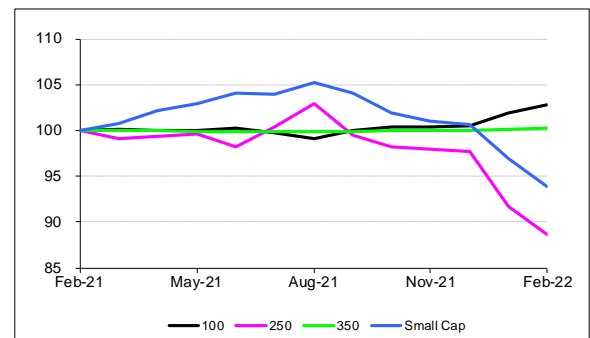
Note: Sector labels for relative lines are in end-value order

There was a small drop this month in the rolling 12-month sector dispersion (falling from 37% to 36%).

(% absolute return)	1 mth	3 mth	12 mth
Energy	2.3	21.2	37.7
Basic Materials	9.5	16.5	19.6
Industrials	-3.1	-6.4	14.0
Consumer Staples	0.4	4.5	20.8
Health Care	2.5	6.5	29.9
Consumer Discretionary	-2.0	-0.2	0.2
Telecommunications	-1.0	17.3	23.3
Utilities	4.6	10.1	42.0
Non-Finan	0.8	5.1	19.2
Financials	-4.7	-0.2	6.2
IT	-3.3	-11.4	2.7
All Share	-0.5	3.8	16.0

UK Equity Size Returns

Figure 4b: Size groups relative to All Share



This month, Mid Cap and Small Cap both fell relative to the All Share.

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



Bond market information

Figure 5: £ Non-Gilt Credit Margins

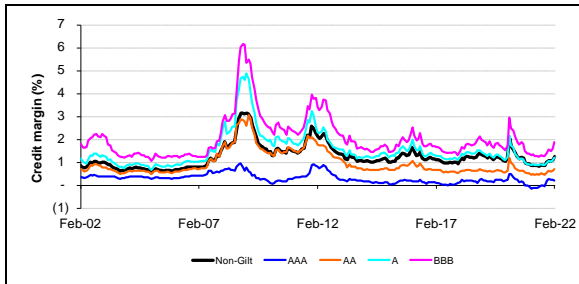


Table 2a: Over 15 Yr Corporate Yields & Margins

Month End	iBoxx Corp AA Y'ld (%)	FT 20 yr Gilt (%)	Margin (%)
Sep '21	2.01	1.39	0.62
Oct '21	1.78	1.19	0.59
Nov '21	1.64	1.00	0.64
Dec '21	1.89	1.20	0.69
Jan '22	2.25	1.52	0.73
Feb '22	2.62	1.67	0.95

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

Category	Mkt Val (£bn @ Feb 22 & 19, 16)			Weight (%)
Gilts (55)	1,719	1,334	1,259	73.4
Non-Gilts (1,180)	622	571	523	26.6
AAA (138)	128	115	101	5.5
AA (147)	77	82	95	3.3
A (377)	166	155	154	7.1
BBB (518)	251	219	174	10.7

Category	Mkt Val (£bn @ Feb 22, 19)		W't (%)	Dur'n (yrs)
Gilts (55)	1,719	1,334	73.4	12.2
< 5 Yrs (13)	445	350	19.0	2.7
5-15 Yrs (16)	522	355	22.3	8.1
> 15 Yrs (26)	752	629	32.1	20.6
Non-Gilts (1,180)	622	571	26.6	7.4
< 5 Yrs (452)	246	198	10.5	3.1
5-15 Yrs (495)	245	233	10.5	7.3
> 15 Yrs (233)	131	139	5.6	15.7

Tables 2d, 2e: € Market Size and Maturity (Feb 22)

Category	Mkt Val (€bn)	Weight (%)
Sovereigns (445)	7,532	59.0
Non-Sovereigns	5,244	41.0
AAA (1,024)	1,373	10.7
AA (792)	1,269	9.9
A (1,327)	1,107	8.7
BBB (1,979)	1,495	11.7

Category	Mkt Val (€bn)	Weight (%)
1 – 3 Yrs (1,376)	2,746	21.5
3 – 5 Yrs (1,357)	2,630	20.6
5 – 7 Yrs (1,057)	2,021	15.8
7 – 10 Yrs (956)	2,188	17.1
10+ Yrs (821)	3,191	25.0

Table 2f: Breakdown of £ Index-Linked Market

Category (Number of issues)	Mkt Val (£bn @ Feb 22 & 19)		W't (%)	Dur'n (yrs)
Gilts (32)	850	678	100.0	20.6
< 5 Yrs (4)	93	59	10.9	2.2
5 – 15 Yrs (9)	225	160	26.4	9.5
> 15 Yrs (19)	532	460	62.6	28.5

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

Month End	US (%)	Euro (%)	Sterling (%)
Sep '21	4.25	2.69	4.32
Oct '21	4.40	2.94	4.65
Nov '21	4.73	3.14	4.84
Dec '21	4.46	2.99	4.80
Jan '22	5.09	3.38	5.22
Feb '22	5.36	4.16	5.86

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

£ Gilt Market “main” Issuance

- £4.25bn, 1¹/₈% 2073 (9.51x, 1.29%, n/a, new)
- £2.25bn, 1% 2032 (2.51x, 1.60%, 0%, Dec '21)

Note: Issuance amounts are nominals. The second % figure in each row is the yield or real yield. The third % 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.

