



## Investment Update June 2023

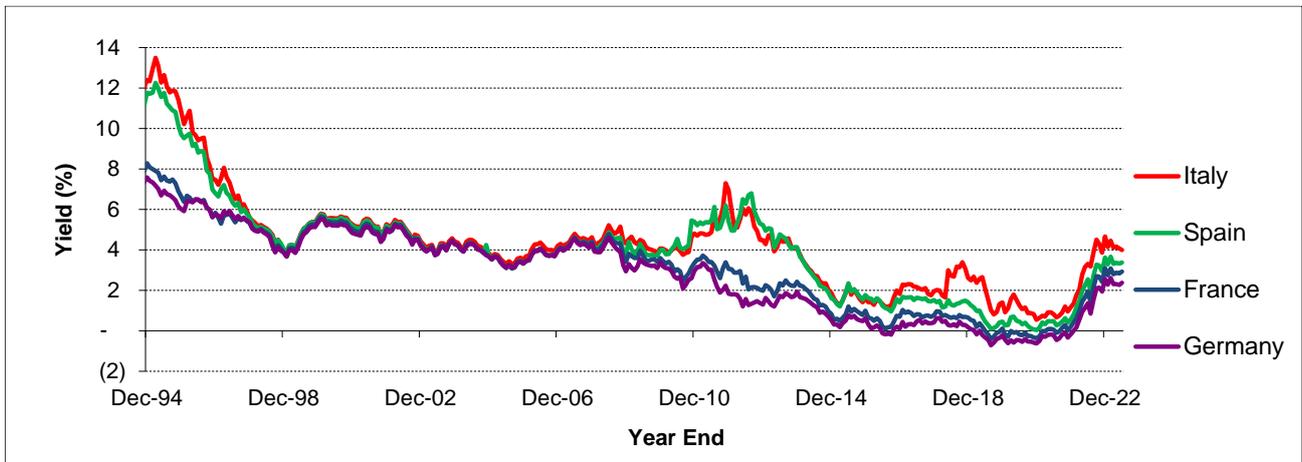
### Investment Headlines & Comment

- A good month for Sterling as interest rates rise again.
- UK inflation remains high in spite of the rate rises.
- UK Government borrowing now exceeds 100% of GDP.

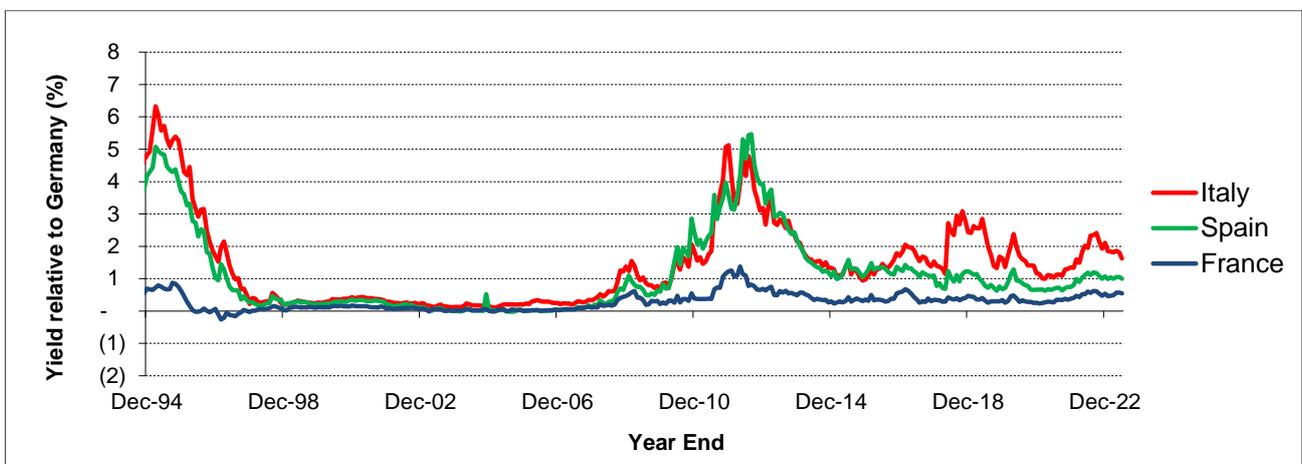
**Feature Section** This month we return to the subject of Eurozone bond yields, which we last looked at in our [March 2019](#) edition. As in the UK, the ECB is repeatedly raising interest rates in a bid to control inflation, which is leading to higher longer-term bond yields.

Figure 1a plots the history of some Euro member countries' 10-year yields, as a reminder of the convergence process that took place in the mid 1990s, and the subsequent decade-long synchronization, before instability set in. Figure 1b then plots the yields relative to those on German 10-year government bonds.

**Figure 1a: Absolute 10-year yields**



**Figure 1b: "Relative to Germany" 10-year yields**



Sources: FT, JP Morgan

From Figure 1b, it is clear that the Italian-German yield divergence is not at the levels seen during the Eurozone crisis in late 2011, but the divergence over the last 13 years does once again prompt the question of just how the Euro really can continue to survive in its current form. The relative position is equally striking for those bonds out at 30-year maturity – as of the end of June 2023, a German yield of 2.38% p.a. but an Italian one of 4.44% p.a.



**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 30 June 2023**

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	1.0	-0.3	5.8	10.0	3.1	5.9	7.4
Overseas Equities	3.1	3.5	11.8	10.4	9.7	11.6	10.5
US Equities	<b>3.9</b>	<b>5.7</b>	14.2	<b>12.9</b>	<b>12.9</b>	<b>14.7</b>	9.1
Europe ex UK Equities	2.4	0.6	<b>19.6</b>	8.8	7.0	8.7	<b>11.6</b>
Japan Equities	1.3	3.0	12.6	4.9	4.0	7.6	7.3
Pacific ex Japan Equities	0.6	-3.2	-3.0	2.8	3.3	6.9	10.7
Emerging Markets	1.3	-1.6	-2.4	1.7	2.1	5.2	10.0
UK Long-dated Gilts	1.6	-8.6	-24.9	-19.8	-7.9	<b>0.3</b>	3.1
UK Long-dated Corp. Bonds	0.5	-4.8	-13.6	-13.5	-4.2	1.8	3.7
UK Over 5 Yrs Index-Linked Gilts	3.8	-8.4	-20.0	-14.8	-5.5	1.6	4.3
High Yield (Global)	-0.6	-1.2	4.8	0.5	3.0	5.5	7.8
Overseas Bonds	-2.9	-4.9	-6.7	-7.1	-0.9	1.6	3.6
Property *	0.5	1.7	-16.3	3.8	2.7	7.2	6.5
Cash	0.4	1.2	3.8	1.5	1.2	0.8	<b>2.0</b>
Commodities £-converted	1.8	-5.3	-18.1	23.9	3.5	-1.8	0.2
Hedge Funds original \$ basis *	-0.2	-0.8	-0.1	8.1	4.4	4.3	5.4
Illustrative £-converted version *	1.2	-3.1	1.6	8.0	5.9	6.5	6.9
Euro relative to Sterling	-0.2	-2.6	-0.3	-1.9	-0.6	0.0	1.1
US \$ relative to Sterling	-2.5	-2.6	-4.5	-0.9	0.8	1.8	1.3
Japanese Yen relative to Sterling	-5.8	-10.6	-10.2	-10.1	-4.5	-2.0	0.4
Sterling trade weighted	2.0	4.1	4.5	2.6	1.0	0.2	-0.8
Price Inflation (RPI) *	0.7	3.0	11.3	8.7	6.0	4.1	3.7
Price Inflation (CPI) *	0.7	2.7	8.7	6.6	4.4	2.9	2.8
Price Inflation (RPIX) *	0.7	2.8	10.3	8.4	5.9	4.1	3.7
Earnings Inflation **	-10.2	1.7	7.4	7.1	4.7	3.2	3.2
All Share Capital Growth	0.7	-1.3	1.9	6.3	-0.5	2.2	3.7
Dividend Growth	0.7	2.8	10.5	-1.2	0.0	2.8	4.2
Earnings Growth	1.7	-19.8	-8.1	3.1	-3.9	0.4	4.1

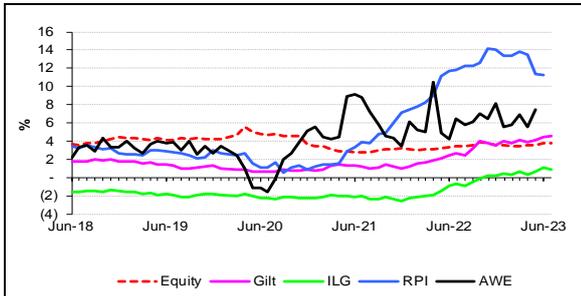
Note: All market returns are total returns for pension funds with income reinvested monthly. Indices used are as follows:

- 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.

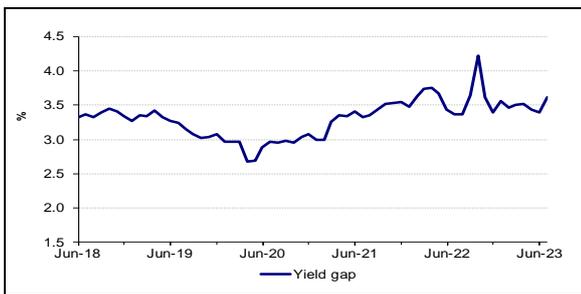


## Yields and Yield Gaps

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.

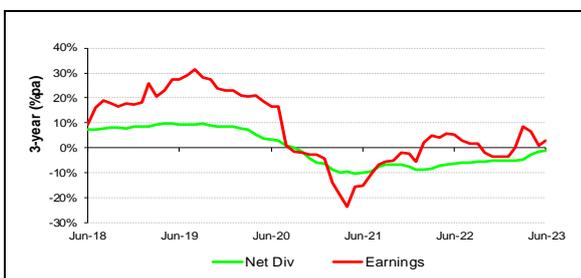
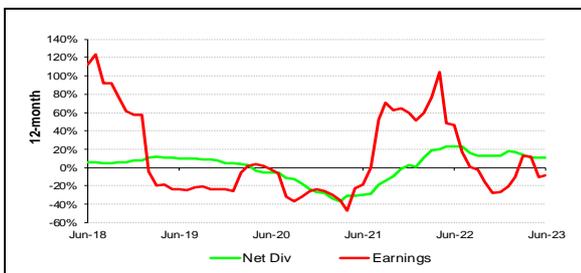


The gap gives a current expectation of around 3.6% p.a. for longer-term inflation including the (unknown) risk premium for gilts, relative to index-linked gilts.

## 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]

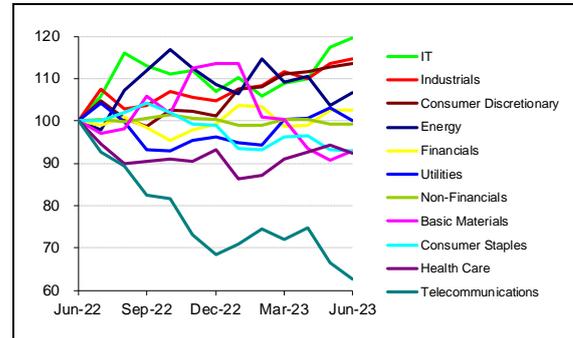
Figure 3: Dividend & Earnings Growth



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



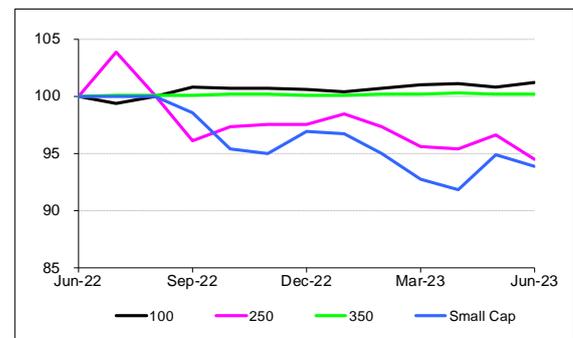
Note: Sector labels for relative lines are in end-value order

There was a rise this month in the rolling 12-month sector dispersion (up from 46% to 57%).

(% absolute return)	1 mth	3 mth	12 mth
Energy	3.9	-2.6	12.7
Basic Materials	3.5	-7.5	-1.6
Industrials	2.1	2.6	21.4
Consumer Staples	0.6	-3.9	-1.8
Health Care	-0.9	1.4	-2.2
Consumer Discretionary	1.6	1.7	20.0
Telecommunications	-4.7	-13.3	-33.7
Utilities	-1.8	-0.5	5.9
Non-Finan	1.0	-1.4	5.0
Financials	0.8	3.5	8.4
IT	2.8	9.3	26.4
All Share	1.0	-0.3	5.8

## 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.

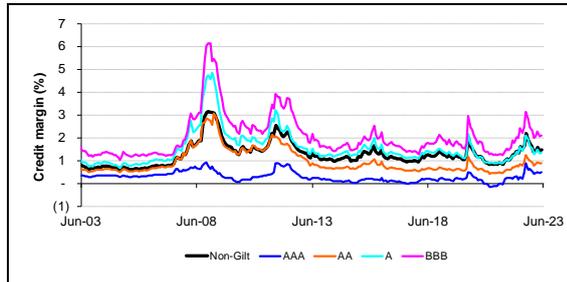
Sources for charts on this page:

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 (%)
Jan '23	4.40	3.77	0.63
Feb '23	4.81	4.14	0.67
Mar '23	4.67	3.84	0.83
Apr '23	4.78	4.06	0.72
May '23	5.20	4.47	0.73
Jun '23	<b>5.08</b>	<b>4.50</b>	<b>0.58</b>

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

Category	Mkt Val (£bn @ Jun 23 & 20, 17)			Weight (%)
	2023	2020	2017	
Gilts (57)	1,350	1,630	1,349	71.7
Non-Gilts (1,231)	532	664	560	28.3
AAA (150)	113	138	108	6.0
AA (156)	70	84	87	3.7
A (416)	151	182	168	8.0
BBB (509)	198	259	197	10.5

Category	Mkt Val (£bn @ Jun 23 & 20)		W't (%)	Dur'n (yrs)
Gilts (57)	1,350	1,630	71.7	9.6
< 5 Yrs (13)	421	345	22.4	2.7
5-15 Yrs (16)	438	470	23.3	7.8
> 15 Yrs (28)	491	815	26.1	17.2
Non-Gilts (1,231)	532	664	28.3	5.8
< 5 Yrs (530)	260	224	13.8	2.7
5-15 Yrs (476)	189	279	10.1	6.8
> 15 Yrs (225)	83	161	4.4	13.4

**Tables 2d, 2e: € Market Size and Maturity (Jun 23)**

Category	Mkt Val (£bn)	Weight (%)
Sovereigns (483)	6,784	57.0
Non-Sovereigns	5,119	43.0
AAA (1,208)	1,667	14.0
AA (808)	974	8.2
A (1,538)	1,166	9.8
BBB (1,971)	1,311	11.0

Category	Mkt Val (£bn)	Weight (%)
1 – 3 Yrs (1,571)	2,875	24.2
3 – 5 Yrs (1,617)	2,664	22.4
5 – 7 Yrs (1,114)	1,904	16.0
7 – 10 Yrs (954)	1,972	16.6
10+ Yrs (752)	2,488	20.9

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

Category (Number of issues)	Mkt Val (£bn @ Jun 23 & 20)		W't (%)	Dur'n (yrs)
Gilts (33)	563	805	100.0	16.0
< 5 Yrs (4)	95	70	16.9	2.2
5 – 15 Yrs (10)	195	195	34.6	9.1
> 15 Yrs (19)	273	540	48.5	25.7

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

Month End	US (%)	Euro (%)	Sterling (%)
Feb '23	7.97	6.76	9.46
Mar '23	7.75	6.85	9.93
Apr '23	7.70	6.86	10.11
May '23	8.11	6.94	10.28
Jun '23	<b>7.92</b>	<b>7.01</b>	<b>10.62</b>

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

**£ Gilt Market “main” & “Green” Issuance**

- £4.08bn, 3½% 2025 (2.34x, 4.87%, 2%, Mar 23)
- £4.69bn, 4½% 2028 (2.39x, 4.93%, 25%, new)
- £3.50bn, 3¼% 2033 (2.33x, 4.35%, 0%, Apr 23)
- £1.69bn, ¾% IL 2033 (2.33x, 0.60%, 13%, new)
- £3.44bn, 3¾% 2038 (2.26x, 4.46%, 25%, Mar 23)
- £3.11bn, 3¾% 2053 (2.58x, 4.48%, 24%, Apr 23)

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 Green Gilt (Gr), tender or syndication cases.

