



Investment Update September 2023

Investment Headlines & Comment

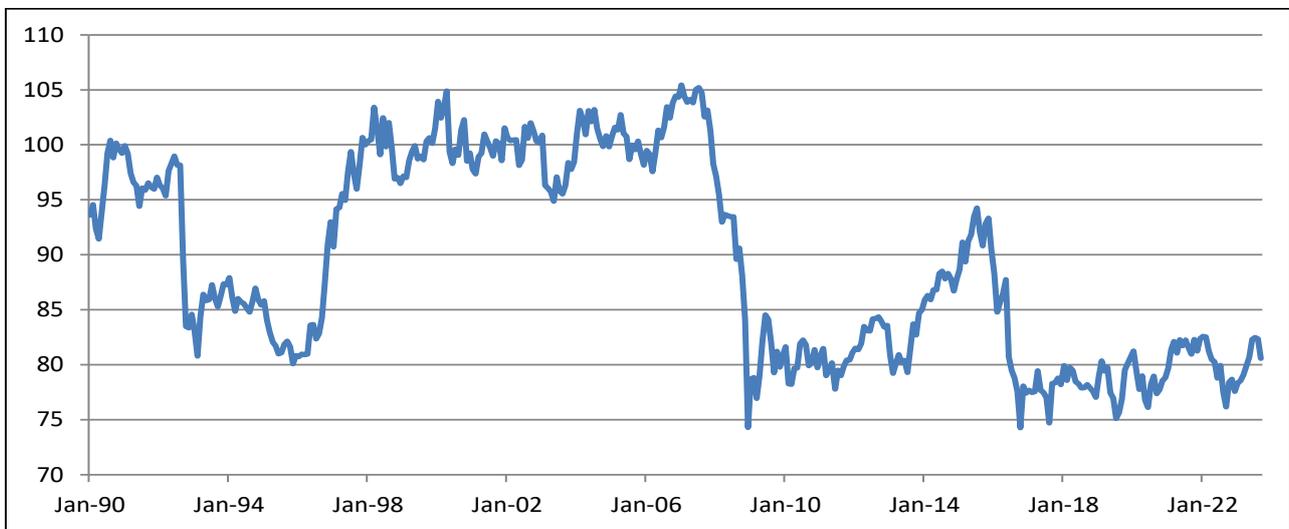
- Another bad month for UK government bonds.
- Sterling fell, particularly relative to the US Dollar.
- A split vote saw the UK bank base rate remain at 5.25%.

Feature Section

This month we revisit the trade-weighted index for £ Sterling, which we originally examined in our [May 2014](#) and [October 2016](#) editions.

Figure 1a shows the history of the trade-weighted index since it was created in January 1990. As a reminder, prior to that date, the US Dollar & £ Sterling exchange rate was considered to be the default measure for determining if £ Sterling was cheap or dear. It is not obvious what a “natural” level should be for the index, and hence whether the current index level of around 81 is strong or weak, but based on historical values, weak would seem more likely. For that to change significantly, potential catalysts could be the collapse of the Euro, or Brexit eventually emerging as a success.

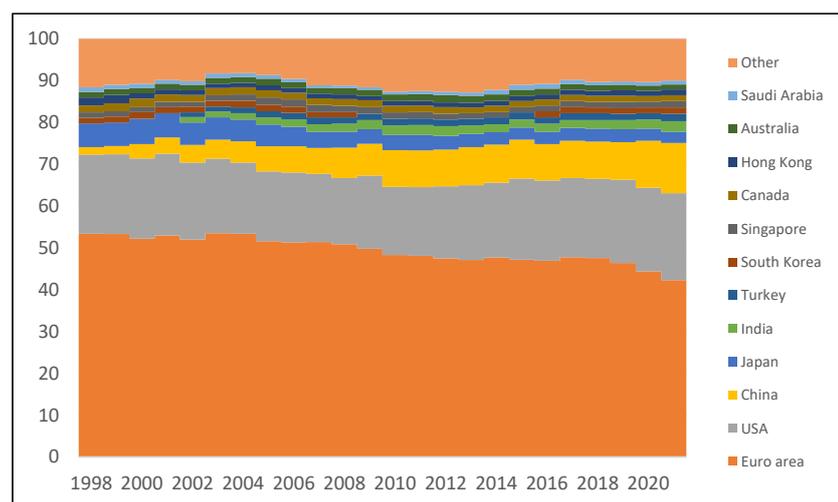
Figure 1a: £ Sterling Trade-Weighted Index



Source: Bank of England

The latest (“narrow index”) [weights](#) were set in March 2023, with the main contributors being the Euro area having 42% weight, the USA 21%, China 12%, Japan 3% and India 3%. Figure 1b shows the history of the weights since the Eurozone was created. The steady increase of the Chinese weighting and the Eurozone decline are of particular interest.

Figure 1b: Country Index Weights



Source: Bank of England



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 September 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 | 1.6 | 1.7 | 13.6 | 11.7 | 3.6 | 5.5 | 7.3 |
| Overseas Equities | -0.7 | 0.6 | 10.7 | 9.3 | 8.6 | 11.6 | 10.2 |
| US Equities | -0.9 | 1.1 | 11.4 | 11.6 | 11.3 | 15.0 | 8.8 |
| Europe ex UK Equities | -1.2 | -1.6 | 20.4 | 7.8 | 6.0 | 7.8 | 11.5 |
| Japan Equities | 1.8 | 3.1 | 15.0 | 5.1 | 3.6 | 7.9 | 6.5 |
| Pacific ex Japan Equities | 0.0 | 0.1 | 1.6 | 1.3 | 3.2 | 6.8 | 10.0 |
| Emerging Markets | 1.2 | 1.3 | 2.6 | 0.6 | 2.3 | 5.4 | 9.4 |
| UK Long-dated Gilts | -5.0 | -6.9 | -13.9 | -21.0 | -8.6 | -0.5 | 2.8 |
| UK Long-dated Corp. Bonds | -2.5 | -2.2 | 2.8 | -14.3 | -4.4 | 1.2 | 3.5 |
| UK Over 5 Yrs Index-Linked Gilts | -5.3 | -7.4 | -17.1 | -16.3 | -6.6 | 0.7 | 3.9 |
| High Yield (Global) | 2.5 | 4.3 | 3.1 | 1.8 | 3.2 | 6.3 | 7.9 |
| Overseas Bonds | 0.7 | -0.3 | -8.7 | -6.5 | -0.9 | 2.0 | 3.6 |
| Property * | 0.1 | 0.1 | -15.3 | 3.8 | 2.3 | 6.9 | 6.4 |
| Cash | 0.5 | 1.4 | 4.6 | 1.9 | 1.4 | 1.0 | 2.0 |
| Commodities £-converted | 8.2 | 20.9 | 1.5 | 32.0 | 7.0 | 0.3 | 1.2 |
| Hedge Funds original \$ basis * | -0.7 | 3.2 | 4.3 | 6.6 | 5.0 | 4.8 | 5.3 |
| Illustrative £-converted version * | 0.8 | 0.9 | -4.2 | 8.4 | 5.6 | 6.9 | 6.5 |
| Euro relative to Sterling | 1.1 | 0.9 | -1.3 | -1.5 | -0.6 | 0.4 | 1.1 |
| US \$ relative to Sterling | 3.9 | 4.2 | -8.5 | 2.0 | 1.3 | 2.9 | 1.6 |
| Japanese Yen relative to Sterling | 1.2 | 0.8 | -11.3 | -9.2 | -4.1 | -1.4 | 0.1 |
| Sterling trade weighted | -2.1 | -2.1 | 5.8 | 1.4 | 0.6 | -0.4 | -0.9 |
| Price Inflation (RPI) * | 0.6 | 0.3 | 9.1 | 8.7 | 5.8 | 4.1 | 3.7 |
| Price Inflation (CPI) * | 0.3 | 0.0 | 6.7 | 6.5 | 4.3 | 2.9 | 2.8 |
| Price Inflation (RPIX) * | 0.5 | -0.1 | 7.8 | 8.3 | 5.6 | 4.1 | 3.7 |
| Earnings Inflation ** | -2.8 | 0.3 | 8.0 | 7.0 | 4.9 | 3.6 | 3.2 |
| All Share Capital Growth | 1.4 | 0.5 | 9.4 | 7.9 | 0.0 | 1.8 | 3.6 |
| Dividend Growth | 0.1 | 2.7 | 9.1 | 1.7 | 0.1 | 3.0 | 4.3 |
| Earnings Growth | 1.5 | 9.3 | 4.8 | 20.4 | -2.8 | 2.5 | 4.5 |

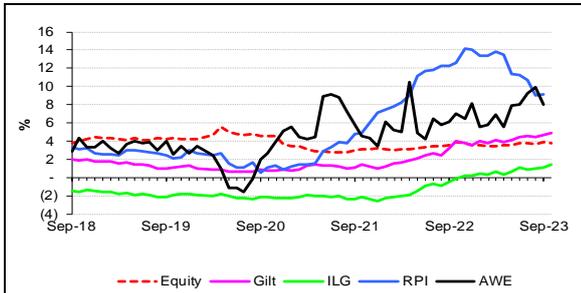
Note: All market returns are total returns for pension funds with income reinvested monthly. Indices used are as follows:

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

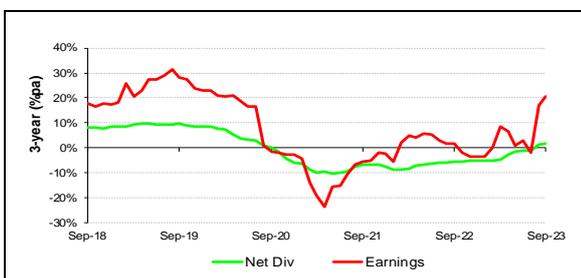
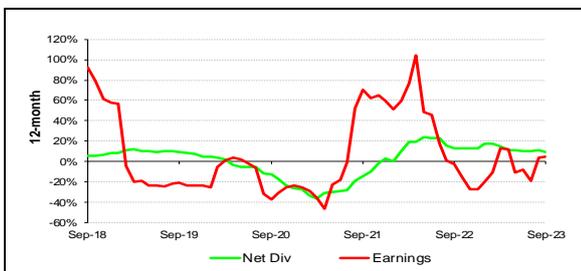


The gap gives a current expectation of around 3.5% p.a. for longer-term inflation including the (unknown) risk premium for gilts, relative to index-linked gilts.

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]

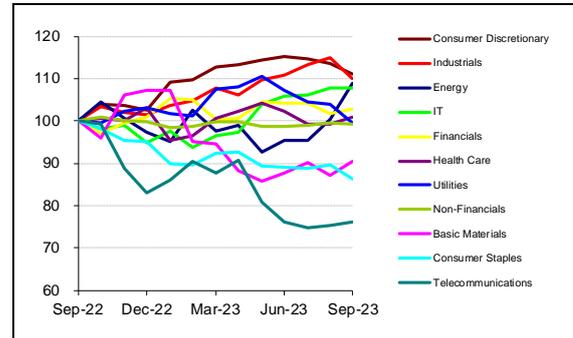
Figure 3: Dividend & Earnings Growth



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



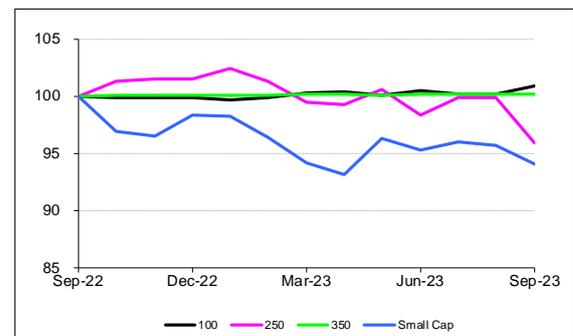
Note: Sector labels for relative lines are in end-value order

There was a fall this month in the rolling 12-month sector dispersion (down from 46% to 35%).

| (% absolute return) | 1 mth | 3 mth | 12 mth |
|------------------------|-------|-------|--------|
| Energy | 10.3 | 16.2 | 23.8 |
| Basic Materials | 5.4 | 4.7 | 2.7 |
| Industrials | -2.8 | 0.9 | 24.9 |
| Consumer Staples | -2.2 | -1.6 | -2.1 |
| Health Care | 3.4 | 0.3 | 14.6 |
| Consumer Discretionary | -0.7 | -1.9 | 26.2 |
| Telecommunications | 2.7 | 1.7 | -13.4 |
| Utilities | -2.7 | -5.7 | 13.0 |
| Non-Finan | 1.3 | 2.0 | 12.7 |
| Financials | 2.7 | 0.4 | 16.9 |
| IT | 1.4 | 3.5 | 22.3 |
| All Share | 1.6 | 1.7 | 13.6 |

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

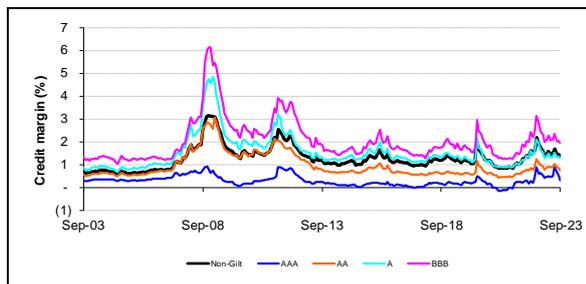


Table 2a: Over 15 Yr Corporate Yields & Margins

| Month End | iBoxx Corp AA Y'ld (%) | FT 20 yr Gilt (%) | Margin (%) |
|-----------|------------------------|-------------------|-------------|
| Apr '23 | 4.78 | 4.06 | 0.72 |
| May '23 | 5.20 | 4.47 | 0.73 |
| Jun '23 | 5.08 | 4.50 | 0.58 |
| Jul '23 | 4.99 | 4.48 | 0.51 |
| Aug '23 | 5.15 | 4.61 | 0.54 |
| Sep '23 | 5.37 | 4.90 | 0.47 |

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

| Category | Mkt Val (£bn @ Sep 23 & 20, 17) | | | Weight (%) |
|-------------------|---------------------------------|--------|--------|------------|
| | Sep 23 | Sep 20 | Sep 17 | |
| Gilts (58) | 1,373 | 1,735 | 1,319 | 71.4 |
| Non-Gilts (1,252) | 550 | 670 | 568 | 28.6 |
| AAA (153) | 119 | 135 | 111 | 6.2 |
| AA (163) | 73 | 85 | 87 | 3.8 |
| A (431) | 161 | 189 | 160 | 8.4 |
| BBB (505) | 197 | 262 | 210 | 10.3 |

| Category | Mkt Val (£bn @ Sep 23 & 20) | | W't (%) | Dur'n (yrs) |
|-------------------|-----------------------------|-------|---------|-------------|
| Gilts (58) | 1,373 | 1,735 | 71.4 | 9.0 |
| < 5 Yrs (14) | 450 | 392 | 23.4 | 2.5 |
| 5-15 Yrs (16) | 457 | 509 | 23.7 | 7.6 |
| > 15 Yrs (28) | 466 | 834 | 24.2 | 16.5 |
| Non-Gilts (1,252) | 550 | 670 | 28.6 | 5.6 |
| < 5 Yrs (561) | 281 | 230 | 14.6 | 2.6 |
| 5-15 Yrs (472) | 190 | 278 | 9.9 | 6.8 |
| > 15 Yrs (219) | 79 | 161 | 4.1 | 13.2 |

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

| Category | Mkt Val (£bn) | Weight (%) |
|------------------|---------------|------------|
| Sovereigns (484) | 6,697 | 56.7 |
| Non-Sovereigns | 5,113 | 43.3 |
| AAA (1,220) | 1,677 | 14.2 |
| AA (810) | 957 | 8.1 |
| A (1,553) | 1,181 | 10.0 |
| BBB (1,966) | 1,299 | 11.0 |

| Category | Mkt Val (£bn) | Weight (%) |
|-------------------|---------------|------------|
| 1 – 3 Yrs (1,590) | 2,972 | 25.2 |
| 3 – 5 Yrs (1,652) | 2,654 | 22.5 |
| 5 – 7 Yrs (1,094) | 1,911 | 16.2 |
| 7 – 10 Yrs (954) | 1,923 | 16.3 |
| 10+ Yrs (743) | 2,350 | 19.9 |

Table 2f: Breakdown of £ Index-Linked Market

| Category (Number of issues) | Mkt Val (£bn @ Sep 23 & 20) | | W't (%) | Dur'n (yrs) |
|-----------------------------|-----------------------------|-----|---------|-------------|
| Gilts (33) | 542 | 796 | 100.0 | 14.9 |
| < 5 Yrs (5) | 121 | 70 | 22.2 | 2.5 |
| 5 – 15 Yrs (9) | 173 | 201 | 32.0 | 9.4 |
| > 15 Yrs (19) | 248 | 525 | 45.8 | 24.7 |

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

| Month End | US (%) | Euro (%) | Sterling (%) |
|-----------|-------------|-------------|--------------|
| Jun '23 | 7.92 | 7.01 | 10.62 |
| Jul '23 | 7.72 | 6.86 | 10.20 |
| Aug '23 | 7.84 | 6.87 | 10.45 |
| Sep '23 | 8.32 | 7.06 | 10.31 |

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

£ Gilt Market “main” & “Green” Issuance

- £4.66bn, 4½% 2028 (2.47x, 4.80%, 17%, Jul '23)
- £4.00bn, 3¼% 2033 (2.38x, 4.40%, 7%, Aug '23)
- £3.00bn, 7/8% Gr 2033 (2.56x, 4.32%, n/a, May '23)
- £0.91bn, 1/8% IL 2051 (2.54x, 1.33%, 1%, May '23)
- £2.75bn, 3¾% 2053 (2.38x, 4.70%, 0%, Jul '23)
- £5.00bn, 4% 2063 (**11.9x**, 4.66%, n/a, May '23)
- £0.75bn, 1 1/8% 2073 (2.88x, 4.29%, n/a, Jun '22)

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.

