

Investment Update October 2024



Investment Headlines & Comment

- A poor month for UK bonds.
- Sterling also suffered.
- At least inflation was subdued.

Feature Section

This month we update our yearly analysis of the UK Government borrowing situation. It is made quite head-scratching this year because of the way the definition of UK Government debt has been changed to allow offsets by owned financial assets (e.g. shares) and debtors (e.g. student loans) yet the true value of those can vary wildly (e.g. student loan defaults).

The Office for Budget Responsibility (OBR) was involved, and its commentary can be found [here](#). The Office for National Statistics explains the debt definition change [here](#). Figures 1a-1d show the usual metrics, including the Office for Budget Responsibility's (OBR) projections for the current tax year, and the next five tax years. Figure 1e shows just how much effect the debt rule change has on the perceived borrowing %. **Hint:** It's whopping.

Figure 1a: Public Sector Net Borrowing (%)

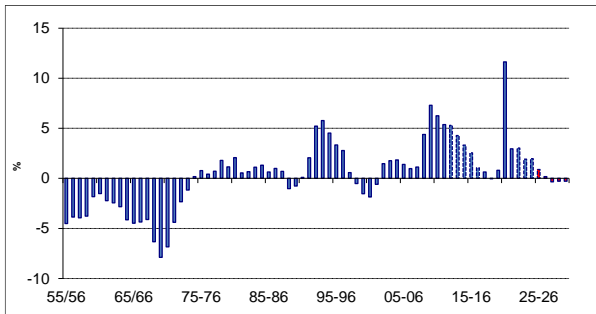


Figure 1b: Debt to GDP Ratio (%)

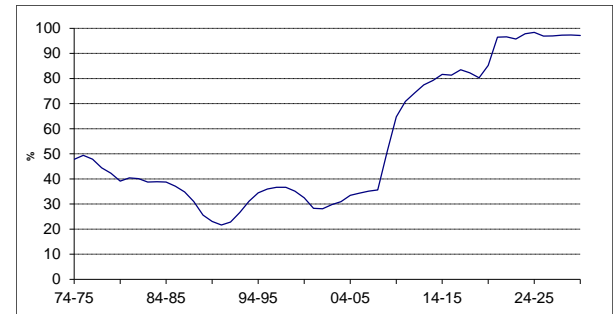


Figure 1c: Interest to GDP Ratio (%)

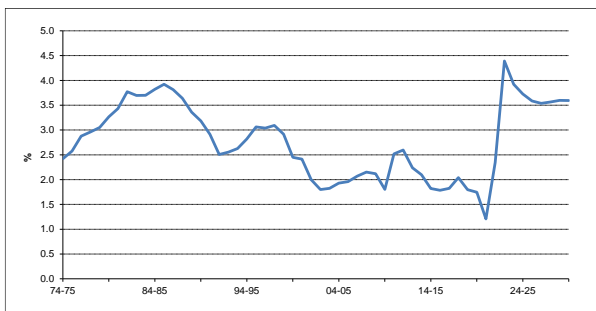


Figure 1d: Interest to Debt Ratio (%)

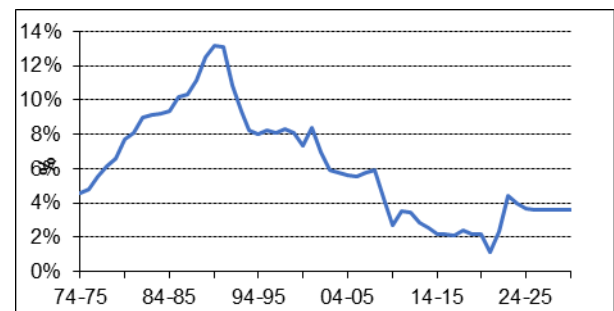
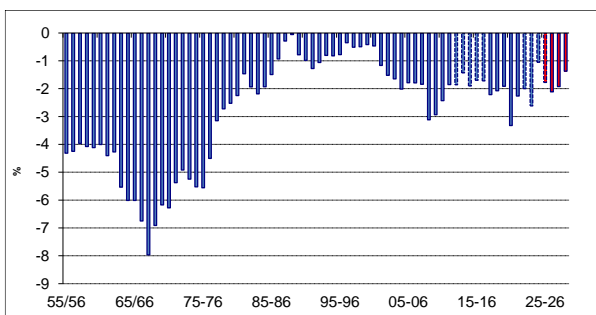


Figure 1e: PSNB definition effect (%)



Source: Office for Budget Responsibility (OBR)

Figure 1e is striking in terms of the effect of the change in the measurement of debt. Leaving aside the bizarre figures from 50+ years ago (when a lot of current non-government assets were still nationalised), the effect over the last 30 years has been an average reduction of 1.7% p.a. of GDP.

Without the rule change, there would be no return to a small budget surplus in the projection. Factor in the probable side-effects of the Budget's other changes (e.g. the *Times* already reported over 10k children were moved from private to state schools before the Budget) and you conclude this is probably achieving nothing. Worse, putting inheritance tax on pension lump sums hurts those that were prudent and did the right thing and saved for their families' future. This Budget feels decidedly flawed.



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 October 2024

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	-2.5	16.3	6.2	5.7	6.2	7.1
Overseas Equities	2.3	2.4	26.0	8.3	11.9	12.3	10.9
US Equities	3.5	3.8	30.3	10.7	15.3	15.4	8.3
Europe ex UK Equities	-1.9	-1.7	13.3	2.9	6.9	8.4	12.6
Japan Equities	-0.1	-3.7	15.1	5.0	5.7	8.9	6.9
Pacific ex Japan Equities	0.5	2.8	22.9	2.6	6.1	7.5	10.2
Emerging Markets	-0.2	3.7	18.9	1.2	4.5	6.1	9.2
UK Long-dated Gilts	-4.4	-4.3	6.6	-17.5	-10.6	-1.2	2.8
UK Long-dated Corp. Bonds	-2.8	-3.1	10.5	-12.0	-5.9	1.0	3.7
UK Over 5 Yrs Index-Linked Gilts	-2.5	-3.1	5.7	-16.4	-8.0	0.1	3.8
High Yield (Global)	3.4	2.8	10.6	4.2	3.7	6.4	8.1
Overseas Bonds	0.6	0.2	1.3	-3.1	-2.7	1.9	3.6
Property *	0.8	1.8	2.9	0.3	2.2	5.2	5.6
Cash	0.4	1.2	5.2	3.4	2.2	1.4	2.0
Commodities £-converted	4.8	-1.4	-7.0	9.3	8.0	0.5	-1.0
Hedge Funds original \$ basis *	1.4	2.9	12.7	4.0	7.4	5.1	5.4
Illustrative £-converted version *	-0.7	-3.0	2.5	4.2	5.6	7.1	7.0
Euro relative to Sterling	1.5	0.2	-3.1	0.0	-0.4	0.8	1.0
US \$ relative to Sterling	4.3	-0.1	-5.6	2.2	0.1	2.2	1.8
Japanese Yen relative to Sterling	-2.0	-1.3	-6.2	-7.2	-6.5	-0.9	0.0
Sterling trade weighted	-2.1	-0.1	4.5	0.7	1.1	-0.4	-0.9
Price Inflation (RPI) *	-0.3	0.3	2.7	8.0	6.0	4.2	3.7
Price Inflation (CPI) *	-0.1	0.1	1.7	6.1	4.3	3.0	2.8
Price Inflation (RPIX) *	-0.4	0.2	2.0	7.3	5.6	4.1	3.7
Earnings Inflation **	-0.8	-0.4	4.3	5.9	5.1	4.0	3.2
All Share Capital Growth	-1.8	-3.4	12.1	2.4	2.1	2.4	3.3
Dividend Growth	0.2	-1.0	4.1	8.2	-1.0	3.3	4.2
Earnings Growth	-2.7	-1.7	5.1	4.1	4.7	2.8	3.7

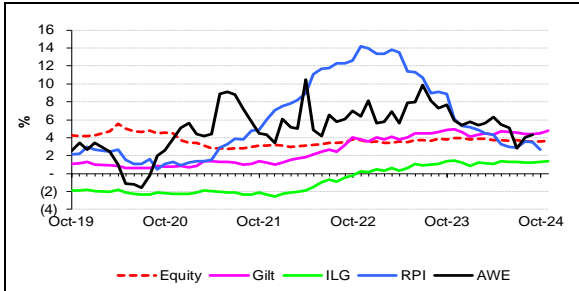
Note: All market returns are total returns for pension funds with income reinvested monthly. Indices used are as follows:

- 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, and SONIA since March 2021, 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.

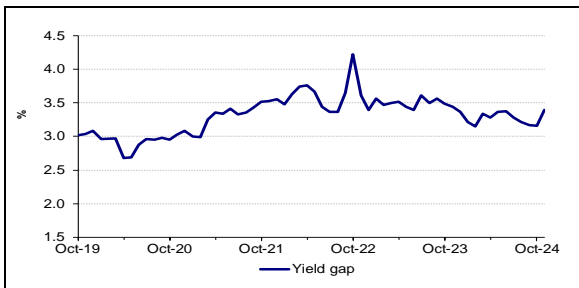


Yields and Yield Gaps

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.

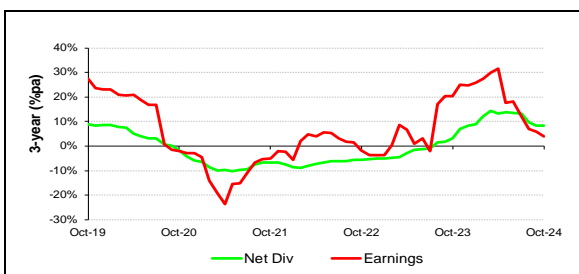
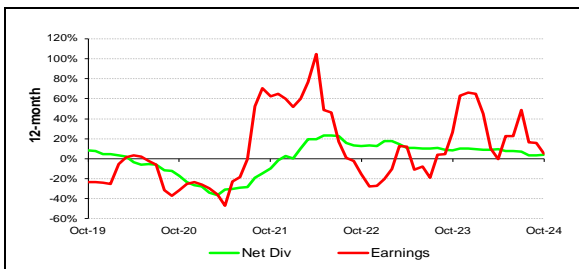


The gap gives a current expectation of around 3.4% p.a. for longer-term inflation including the (unknown) risk premium for gilts, relative to index-linked gilts.

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]

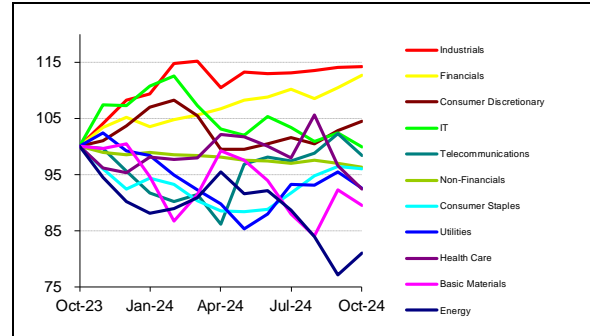
Figure 3: Dividend & Earnings Growth



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



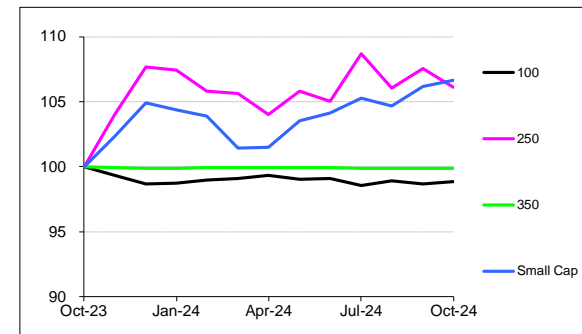
Note: Sector labels for relative lines are in end-value order

There was a small fall this month in the rolling 12-month sector dispersion (down from 35% to 33%).

(% absolute return)	1 mth	3 mth	12 mth
Energy	3.3	-11.0	-5.8
Basic Materials	-4.5	-0.8	4.1
Industrials	-1.6	-1.5	32.9
Consumer Staples	-2.1	2.1	11.7
Health Care	-5.8	-7.9	7.5
Consumer Discretionary	-0.1	0.3	21.6
Telecommunications	-5.3	-1.4	14.5
Utilities	-4.6	-3.1	7.6
Non-Finan	-2.3	-3.2	12.0
Financials	0.3	-0.3	31.0
IT	-4.0	-5.7	16.3
All Share	-1.6	-2.5	16.3

UK Equity Size Returns

Figure 4b: Size groups relative to All Share



This month, Mid Cap fell but Small Cap rose 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

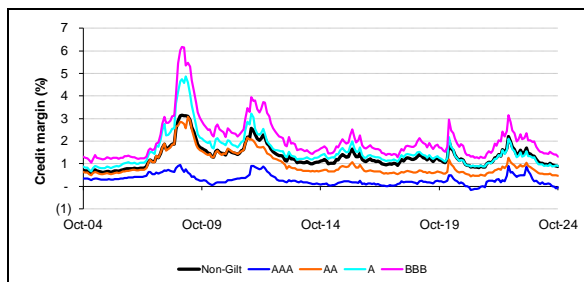


Table 2a: Over 15 Yr Corporate Yields & Margins

Month End	iBoxx Corp AA Y'ld (%)	FT 20 yr Gilt (%)	Margin (%)
May '24	5.11	4.67	0.44
Jun '24	5.05	4.58	0.47
Jul '24	4.90	4.43	0.47
Aug '24	4.90	4.40	0.50
Sep '24	5.00	4.45	0.55
Oct '24	5.26	4.79	0.47

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

Category	Mkt Val (£bn @ Oct 24 & 21, 18)			Weight (%)
Gilts (61)	1,482	1,786	1,289	72.2
Non-Gilts (1,253)	570	657	572	27.8
AAA (151)	120	127	117	5.8
AA (176)	79	77	82	3.8
A (436)	169	188	162	8.2
BBB (490)	203	265	210	9.9

Category	Mkt Val (£bn @ Oct 24 & 21)		W't (%)	Dur'n (yrs)
Gilts (61)	1,482	1,786	72.2	9.1
< 5 Yrs (14)	453	415	22.1	2.6
5-15 Yrs (19)	550	548	26.8	7.9
> 15 Yrs (28)	478	822	23.3	16.7
Non-Gilts (1,253)	570	657	27.8	5.5
< 5 Yrs (588)	303	230	14.7	2.6
5-15 Yrs (449)	188	274	9.1	7.0
> 15 Yrs (216)	80	152	3.9	13.2

Tables 2d, 2e: € Market Size and Maturity (Oct 24)

Category	Mkt Val (£bn)	Weight (%)
Sovereigns (522)	7,674	56.7
Non-Sovereigns	5,853	43.3
AAA (1,315)	1,983	14.7
AA (891)	1,091	8.1
A (1,587)	1,282	9.5
BBB (2,098)	1,497	11.1

Category	Mkt Val (£bn)	Weight (%)
1 - 3 Yrs (1,825)	3,320	24.5
3 - 5 Yrs (1,662)	2,964	21.9
5 - 7 Yrs (1,147)	2,140	15.8
7 - 10 Yrs (993)	2,215	16.4
10+ Yrs (786)	2,888	21.4

Table 2f: Breakdown of £ Index-Linked Market

Category (Number of issues)	Mkt Val (£bn @ Oct 24 & 21)		W't (%)	Dur'n (yrs)
Gilts (32)	543	868	100.0	15.3
< 5 Yrs (4)	99	91	18.3	3.2
5 - 15 Yrs (9)	184	195	33.8	9.5
> 15 Yrs (19)	260	582	47.9	24.1

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

Month End	US (%)	Euro (%)	Sterling (%)
Aug '24	6.69	5.33	8.13
Sep '24	6.52	5.18	7.82
Oct '24	6.86	5.18	7.86

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

£ Gilt Market "main" & "Green" Issuance

- o £4.79bn, 3¾% 2027 (3.29x, 4.08%, 20%, Aug '24)
- o £4.02bn, 4¼% 2029 (2.93x, 3.88%, 1%, Sep '24)
- o £4.00bn, 4¼% 2029 (3.05x, 4.15%, 0%, Oct '24)
- o £4.38bn, 4% 2031 (3.42x, 3.99%, 25%, Sep '24)
- o £3.77bn, 4¼% 2034 (3.25x, 4.17%, 1%, Sep '24)
- o £1.15bn, ¼% IL 2039 (3.14x, 1.04%, 15%, Jul '24)
- o £2.81bn, 4¾% 2043 (3.27x, 4.42%, 25%, Aug '24)
- o £1.08bn, 5/8% IL 2045 (3.57x, 1.33%, 21%, Sep '24)
- o £2.25bn, 1½ Gr 2053 (3.15x, 4.83%, n/a, May '24)
- o £2.81bn, 4¾% 2054 (3.08x, 4.74%, 25%, Sep '24)

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.

