JAGGER & ASSOCIATES

Investment Update
February 2016

Investment Headlines & Comment

- A very v-shaped month for **equity markets**, although hidden by £ moves and overall monthly returns.
- A poor month for **Sterling** as the EU referendum gets underway, as its trade weighting drops 4%.
- UK Equity **earnings data** goes haywire for Oil & Gas, Basic Materials, and Telecoms.

Feature Section

This month we consider some investment features of Silver, usually in the shadow of Gold. Neither metal generates any income, but Silver has rather more in the way of practical uses than Gold, including various industrial and military applications.

This topic also allows us to look back on a rather peculiar incident in US trading history. Figure 1a below shows the Gold and Silver prices (in US Dollars and Sterling), over the period since 1968 – Gold on the left-hand axis, Silver on the right-hand one. What jumps out is the spike back in 1980, which was when the so-called "Silver Thursday" incident happened. At the time, it seems two brothers, sons of a Texan oil billionaire, were estimated to control *one third* of the entire world supply of silver (other than that held by governments). They had built this up through spectacular leverage (akin to early hedge fund managers). When the permitted leverage rules were changed on the relevant metals exchange, the Silver price fell dramatically, and some years later the brothers eventually declared bankruptcy.

Figure 1a: Gold and Silver prices, 1968-2016

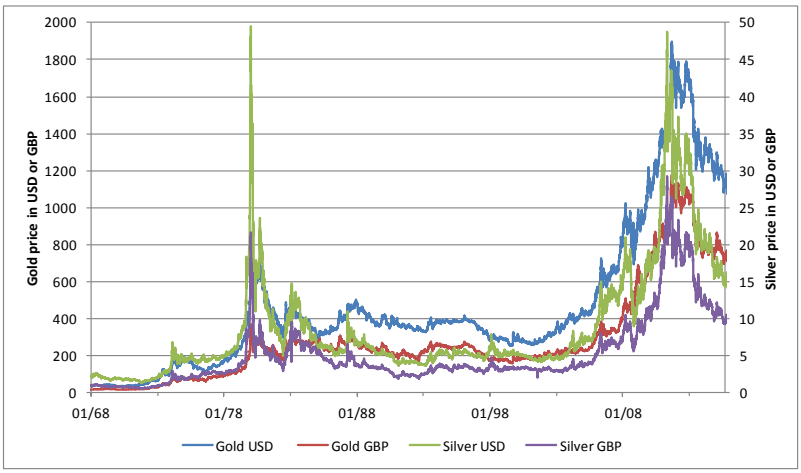
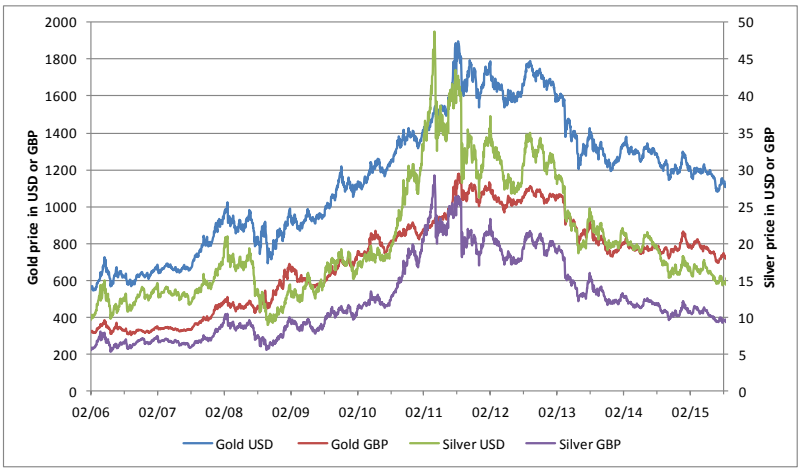


Figure 1b: Gold and Silver prices, 2006-2016



Source: LBMA

You can put this into context if you compare the daily USD moves on the Gold price and the Silver price. For Gold, 74% of days see moves within the +/-1% range, whereas for Silver it is only 52%. At its most extreme, Gold has 'only' moved by +/-15% in a day, whereas for Silver, there have been huge *successive* one-day moves in 1983 of -47% and +82% respectively. (**Ed:** Reader, we didn't predict those values either.)

Things were not much more rational in 2011, when a further bout of speculative activity occurred. Seemingly led by a mass of private individuals who viewed Silver as a cheap alternative to Gold, it saw another spike in nominal terms (but less than for the 1980 event, once inflation is allowed for). Figure 1b shows the movements for just the last 10 years, and the contrast between the two metals is clear. (**Ed:** The extreme 1-day moves for Silver over this period are +20% and -17% respectively, so still bigger than Gold has ever done.)

The main reason for the contrast is that whilst Silver and Gold may be similar if thought of as an item to be hoarded (investment demand), the industrial supply/demand equation for silver exerts an equally strong influence on its price, unlike Gold, particularly as and when unexpected new uses are identified.

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 29 February 2016

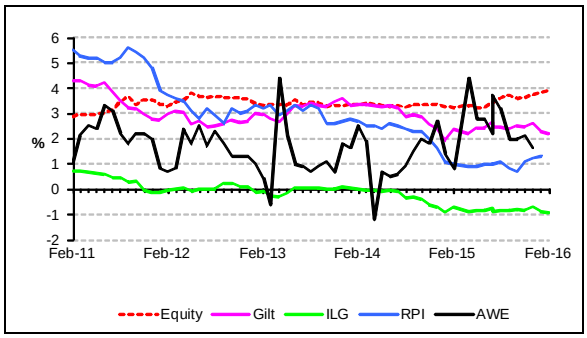
Asset Class	1 month (%)	3 months (%)	12 months (%)	3 years (% p.a.)	5 years (% p.a.)	10 years (% p.a.)	20 years (% p.a.)
UK Equities	0.8	-3.5	-7.3	3.5	5.1	4.9	6.5
Overseas Equities	1.1	-0.7	-1.6	7.7	7.8	6.9	6.6
US Equities	1.7	0.4	3.1	13.7	**13.4**	9.0	7.1
Europe ex UK Equities	-0.1	-3.1	-5.1	4.1	3.7	4.7	8.2
Japan Equities	**-1.4**	**-3.7**	0.7	7.6	4.9	**1.9**	**0.8**
Pacific ex Japan Equities	0.8	-0.8	-11.8	-2.1	2.2	7.5	5.2
Emerging Markets	1.6	-1.3	**-14.8**	**-5.9**	**-2.1**	4.5	5.6
UK Long-dated Gilts	1.7	5.8	7.3	9.6	11.2	7.0	8.6
UK Long-dated Corp. Bonds	-1.0	-1.0	-3.3	6.1	8.4	5.4	-
UK Over 5 Yrs Index-Linked Gilts	-0.1	1.8	5.0	6.9	9.7	7.5	8.0
High Yield (Global)	2.2	4.4	3.4	3.1	7.0	**9.1**	-
Overseas Bonds	**5.0**	**14.5**	**14.6**	2.8	4.1	6.6	5.2
Property *	0.7	2.8	13.6	**14.7**	10.7	5.3	**9.0**
Cash	0.0	0.1	0.6	0.5	0.7	2.1	3.8
Commodities £-converted	-0.3	-8.3	-29.8	-23.3	-14.9	-8.6	-1.1
Hedge Funds original $ basis *	-2.5	-3.4	-3.5	1.9	1.7	3.5	7.4
Illustrative £-converted version *	1.4	5.1	2.2	5.8	4.2	5.8	7.7
Euro relative to Sterling	2.2	11.1	7.4	-3.3	-1.7	1.4	-
US $ relative to Sterling	1.8	8.0	10.9	2.9	3.1	2.3	0.5
Japanese Yen relative to Sterling	9.2	18.0	17.4	-3.8	-3.3	2.6	0.1
Sterling trade weighted	-3.9	-9.1	-7.0	2.3	0.8	-1.6	0.2
Price Inflation (RPI) *	-0.7	-0.3	1.3	1.7	2.5	3.0	2.8
Price Inflation (CPI) *	-0.8	-0.8	0.2	0.8	1.7	2.4	1.9
Price Inflation (RPIX) *	-0.7	-0.3	1.4	1.8	2.5	3.2	2.8
Earnings Inflation **	3.7	3.4	1.6	2.0	1.9	2.3	3.2
All Share Capital Growth	0.3	-4.2	-10.6	0.0	1.5	1.2	3.0
Net Dividend Growth	2.1	2.9	8.2	5.4	7.8	4.1	-
Earnings Growth	-32.6	-32.5	-41.4	-16.3	-12.6	-4.8	0.8

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 subindices*
- *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 – Merrill Lynch Global, £ Unhedged*
- *Overseas Bonds – JP Morgan Traded Unhedged World ex UK*
- *Property – IPD Monthly 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



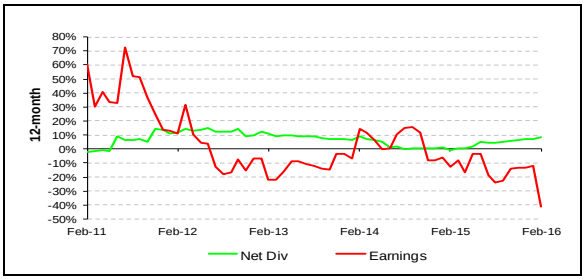
The yield gap is a measure of expected average future inflation, derived as long bond yield minus ILG yield.

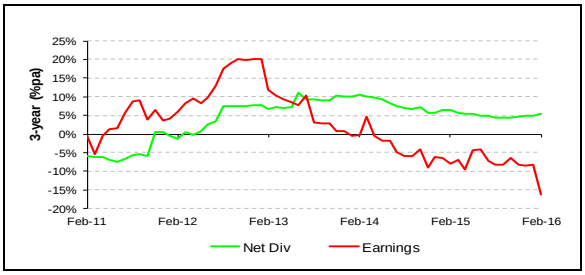
The gap gives a current expectation around 3.1% for longer-term inflation + risk premium for gilts, relative to index-linked gilts.

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

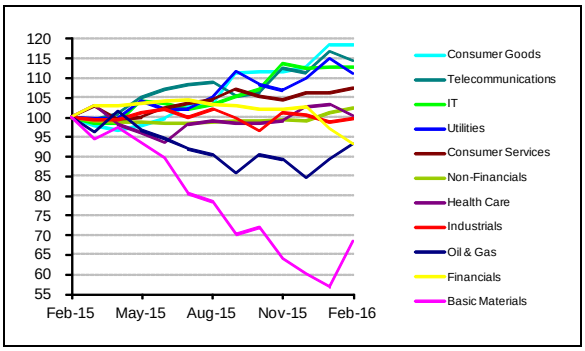




Sources for charts on this page:
Financial Times, Office for National Statistics, J&A

UK Equity Sector Returns

Figure 4a: Sectors relative to All Share



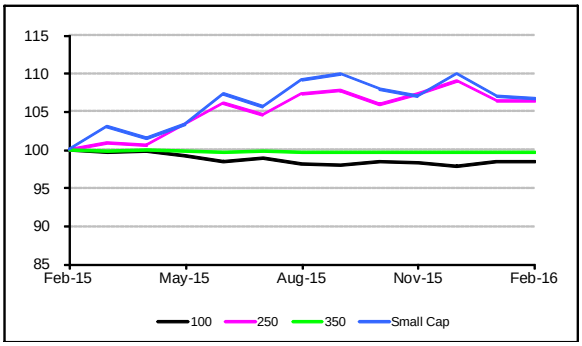
Note: Sector labels for relative lines are in end-value order

There was a slight fall this month in the rolling 12-month sector dispersion (from 56% to 50%).

(% absolute return)	1 mth	3 mth	12 mth
Oil & Gas	5.2	0.6	-13.7
Basic Materials	21.3	3.3	-36.6
Industrials	1.8	-5.0	-7.5
Consumer Goods	0.9	2.6	9.9
Health Care	-2.0	-2.3	-7.0
Consumer Services	2.0	-0.9	-0.4
Telecommunications	-1.2	-2.1	5.9
Utilities	-2.6	0.2	2.8
Non-Financials	2.2	-0.5	-5.1
Financials	-3.3	-12.0	-13.7
IT	0.8	-4.4	4.5
All Share	0.8	-3.5	-7.3

UK Equity Size Returns

Figure 4b: Size groups relative to All Share



Small Cap fell in relative terms this month, but Mid and Large Cap were effectively flat in relative terms.

FRS17 volatility indicator

Now discontinued, but available on request.

Bond market information

Figure 5: £ Non-Gilt Credit Margins

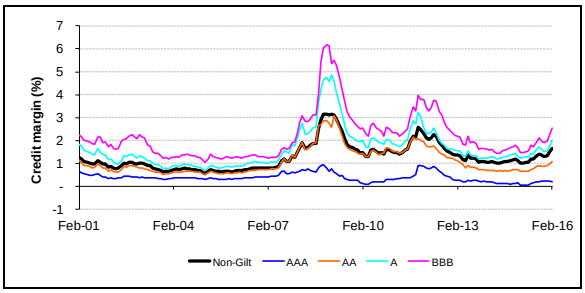


Table 2a: Over 15 Yr Corporate Yields & Margins

Month End	iBoxx Corp AA Y'ld (%)	FT 20 yr Gilt (%)	Margin (%)
Sep '15	3.59	2.39	1.20
Oct '15	3.66	2.53	1.13
Nov '15	3.49	2.47	1.02
Dec '15	3.65	2.59	1.06
Jan '16	3.52	2.27	1.25
Feb '16	**3.61**	**2.18**	**1.43**

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

Category	Mkt Val @ Feb 16 & 13, 10			Weight (%)
Gilts (38)	1,259	1,110	704	70.6
Non Gilts (1,018)	523	529	468	29.4
AAA (119)	101	127	146	5.7
AA (189)	95	72	75	5.3
A (330)	154	180	165	8.6
BBB (380)	174	150	82	9.7

Category	Mkt Val @ Feb 16 & 13		W't (%)	Dur'n (yrs)
Gilts (38)	1,259	1,110	70.6	11.1
< 5 Yrs (11)	342	313	19.2	3.1
5–15 Yrs (11)	391	399	21.9	7.6
> 15 Yrs (16)	526	398	29.5	18.8
Non Gilts (1,018)	523	529	29.4	7.8
< 5 Yrs (337)	154	146	8.6	2.6
5–15 Yrs (443)	228	215	12.8	7.5
> 15 Yrs (238)	142	168	8.0	14.1

£ Gilt Market "main" Issuance

- £2.75bn 1½% 2026 (1.52x, 1.59%, new)
- £1.65bn 3½% 2045 (2.08x, 2.21%, Dec 15)
- £1.43bn $^1/_8$% IL 2026 (1.90x, ry -0.90%, Oct 15)
- £2.75bn $^1/_8$% IL 2065 (3.82x, ry -0.89%, new)

Note: Issuance amounts are nominals.

Tables 2d, 2e: € Market Size and Maturity (Feb 16)

Category	Mkt Val (€bn)	Weight (%)
Sovereigns (321)	5,852	61.8
Non Sovereigns	3,615	38.2
AAA (634)	1,055	11.1
AA (593)	960	10.1
A (759)	764	8.1
BBB (932)	836	8.8

Category	Mkt Val (€bn)	Weight (%)
1 – 3 Yrs (774)	2,086	22.0
3 – 5 Yrs (809)	2,041	21.6
5 – 7 Yrs (736)	1,598	16.9
7 – 10 Yrs (602)	1,733	18.3
10+ Yrs (318)	2,008	21.2

Table 2f: Breakdown of £ Index-Linked Market

Category (Number of issues)	Mkt Val (£bn @ Feb 16 & 13)		W't (%)	Dur'n (yrs)
Gilts (26)	507	360	93.4	21.9
< 5 Yrs (3)	50	46	9.2	-
5 – 15 Yrs (7)	129	102	23.8	-
> 15 Yrs (16)	328	212	60.5	29.6
Non Gilts (37)	36	31	6.6	17.0

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

Month End	US (%)	Euro (%)	Sterling (%)
Aug '15	6.61	4.43	6.38
Sep '15	7.21	5.14	6.58
Oct '15	6.68	4.52	6.40
Nov '15	7.03	4.37	6.30
Dec '15	7.51	5.13	6.51
Jan '16	7.81	5.21	6.80
Feb '16	**7.62**	**5.48**	**7.20**

Sources: Barclays Capital, DMO, iBoxx, J&A, MLX

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