



Investment Update March 2022

Investment Headlines & Comment

- A mixed month for equity markets.
- Gilt nominal and real yields continued to rise.
- A further small rise in UK interest rates – just not enough?

Feature Section

This month, given the additional UK finances data provided in the Spring Statement, we revisit the various metrics that can be used to assess where things have got to and where we may be heading. We last looked at this fully in our [December 2019](#) issue, and also as part of our [March 2021](#) issue.

Figures 1a-1d show the usual metrics, including the Office for Budget Responsibility's (OBR) projections for the current tax year that is nearly over, and the next five tax years. The (hopefully) unique nature of the Covid spike in Figure 1a is clear, and it is also interesting to note how much lower the *actual* 2021/22 percentage looks set to turn out to be (5.4%) compared with the OBR's forecast 12 months ago (10.3%).

Figure 1a: Public Sector Net Borrowing (%)

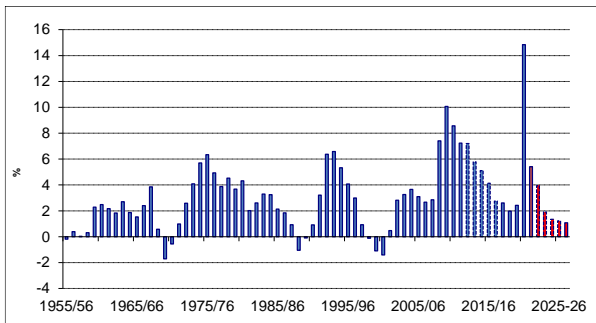


Figure 1b: Debt to GDP Ratio (%)

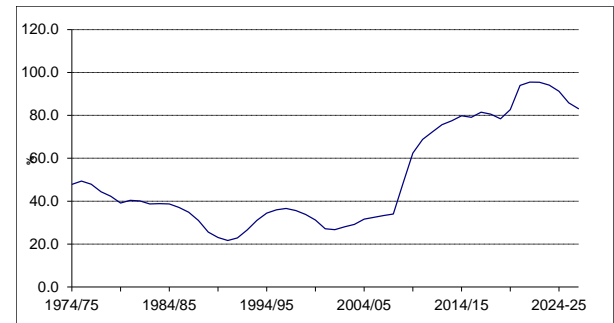
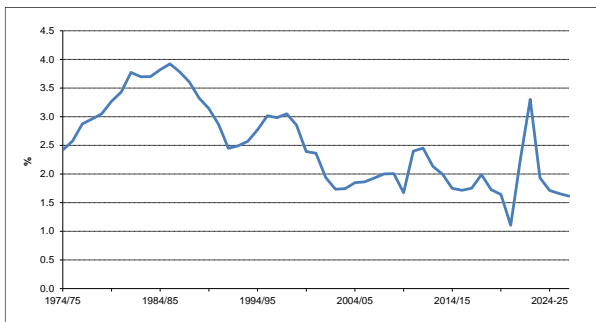


Figure 1c: Interest to GDP Ratio (%)



In Figure 1c, the projected interest spike in 2022/23 appears to be due to the spike in inflation (as measured by RPI) that the UK is currently experiencing. The speed at which the ratio falls back suggests the OBR is modelling on the basis that it is a temporary inflation spike, consistent with the oscillation observation we made in our [January 2022](#) edition. The interest ratio is set to stabilize again at just over 1.5%.

Figure 1d: Interest to Debt Ratio (%)

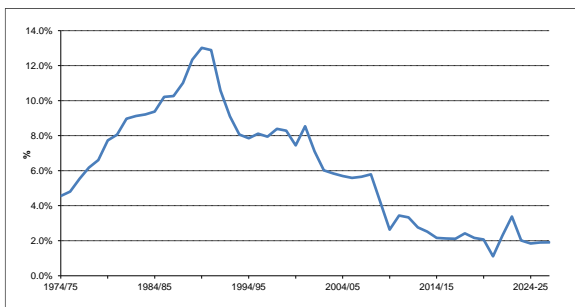


Figure 1d can be thought of as illustrating the average coupon rate across the government's debt portfolio. It too is set to stabilize, again at around 2%, reflecting the proportion of overall market issuance that has taken place in the recent time of comparatively low yields.

In December 2019, we noted that, on the then values of these measures, an increase in public spending might be reasonable. However, given what has happened since then, it would seem prudent to defer any more increase for a few years, until the ratio in Figure 1b actually comes down in the way that the OBR currently projects it to do. Quite how future generations might reduce the debt further remains an interesting question!

Source: Office for Budget Responsibility (OBR)



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 March 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	1.3	0.5	13.0	5.3	4.7	7.2	6.2
Overseas Equities	4.3	-2.6	12.6	14.3	11.3	13.1	8.9
US Equities	5.5	-2.5	19.3	18.5	14.8	16.8	7.4
Europe ex UK Equities	0.7	-9.5	3.9	8.8	6.7	9.5	9.8
Japan Equities	1.2	-3.5	-2.3	6.5	5.2	9.0	5.9
Pacific ex Japan Equities	1.8	-2.2	-4.3	7.1	6.3	8.4	10.1
Emerging Markets	-0.4	-4.3	-6.8	4.9	5.3	5.8	9.4
UK Long-dated Gilts	-3.3	-12.3	-7.2	-0.7	0.9	5.0	6.1
UK Long-dated Corp. Bonds	-1.0	-11.9	-8.3	1.3	2.1	5.9	6.1
UK Over 5 Yrs Index-Linked Gilts	-3.0	-6.4	4.8	3.3	3.2	6.5	7.4
High Yield (Global)	0.5	-3.3	-0.1	2.8	2.8	7.1	7.7
Overseas Bonds	-1.6	-3.3	-2.4	-0.3	0.2	2.4	4.6
Property *	1.4	6.7	21.8	7.4	8.0	8.9	7.8
Cash	0.1	0.2	0.3	0.4	0.5	0.5	2.0
Commodities £-converted	11.7	36.9	72.4	13.0	8.9	-1.4	1.1
Hedge Funds original \$ basis *	-0.1	-1.1	2.7	8.3	6.2	5.1	5.7
Illustrative £-converted version *	-0.1	-2.4	7.0	8.0	4.6	6.9	6.0
Euro relative to Sterling	1.0	0.7	-0.8	-0.6	-0.2	0.1	1.6
US \$ relative to Sterling	1.9	2.9	4.8	-0.3	-1.0	2.0	0.4
Japanese Yen relative to Sterling	-3.3	-2.4	-4.6	-3.4	-2.7	-1.9	0.8
Sterling trade weighted	-1.5	-1.4	-1.1	0.8	0.9	-0.1	-1.1
Price Inflation (RPI) *	0.8	1.9	8.2	4.0	3.6	2.9	3.1
Price Inflation (CPI) *	0.8	1.1	6.1	2.7	2.6	2.0	2.3
Price Inflation (RPIX) *	0.8	1.9	8.3	4.1	3.7	3.0	3.2
Earnings Inflation **	-1.2	4.9	5.1	4.3	3.9	2.8	2.9
All Share Capital Growth	0.7	-0.5	9.3	1.7	1.0	3.4	2.5
Dividend Growth	3.0	0.2	19.3	-8.1	-1.2	2.3	3.3
Earnings Growth	1.5	-3.8	76.6	4.9	14.8	-0.1	4.8

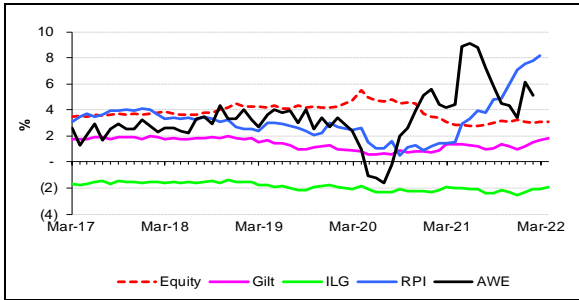
Note: All market returns are total returns for pension funds with income reinvested monthly. Indices used are as follows:

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

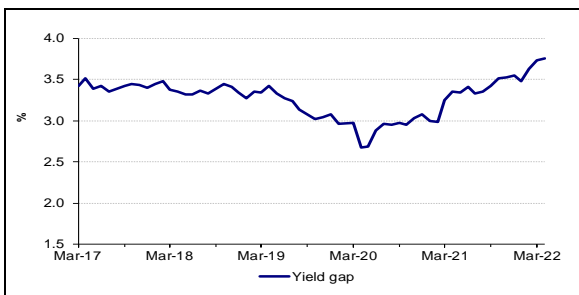


Yields and Yield Gaps

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.

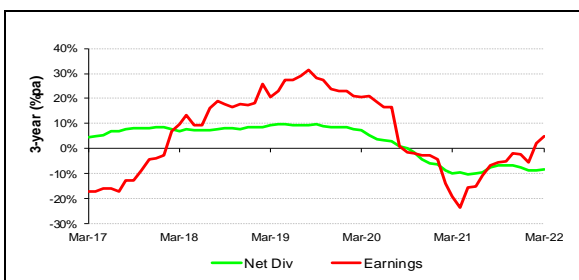
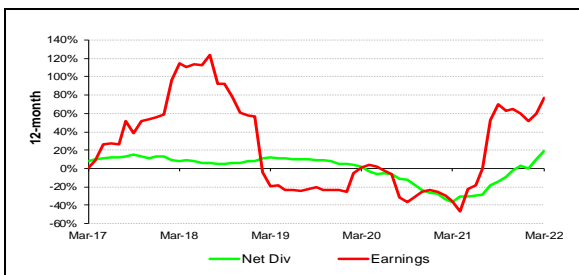


The gap gives a current expectation around 3.8% for longer-term inflation including the (unknown) risk premium for gilts, relative to index-linked gilts.

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]

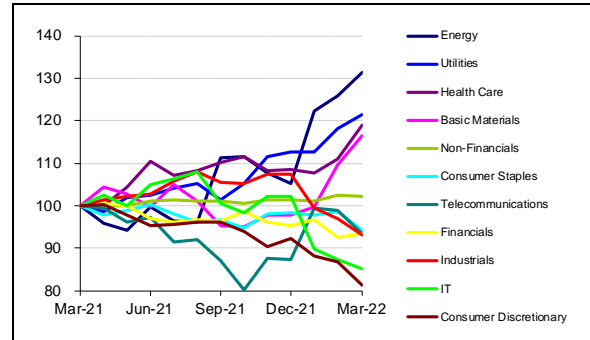
Figure 3: Dividend & Earnings Growth



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



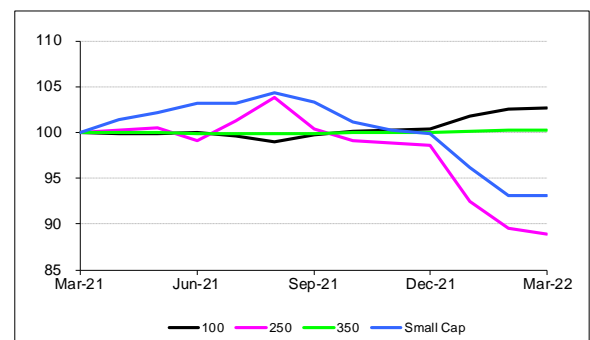
Note: Sector labels for relative lines are in end-value order

There was a rise this month in the rolling 12-month sector dispersion (rising from 36% to 50%).

(% absolute return)	1 mth	3 mth	12 mth
Energy	5.8	25.4	48.5
Basic Materials	7.7	19.6	31.7
Industrials	-2.5	-12.9	5.3
Consumer Staples	-3.3	-3.7	6.6
Health Care	8.6	10.2	34.5
Consumer Discretionary	-5.2	-11.5	-8.1
Telecommunications	-4.3	7.4	5.6
Utilities	4.0	8.4	37.2
Non-Finan	1.0	1.1	15.4
Financials	2.3	-1.6	5.5
IT	-1.1	-16.1	-3.7
All Share	1.3	0.5	13.0

UK Equity Size Returns

Figure 4b: Size groups relative to All Share



This month, Mid Cap fell relative to the All Share, but Small Cap was unchanged.

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



Bond market information

Figure 5: £ Non-Gilt Credit Margins

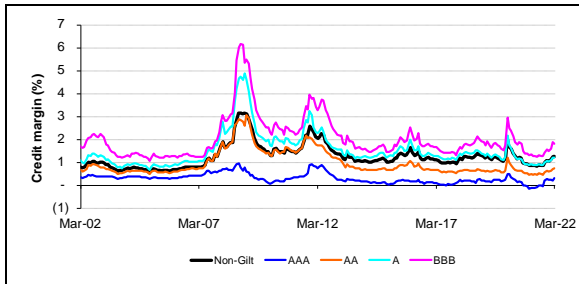


Table 2a: Over 15 Yr Corporate Yields & Margins

Month End	iBoxx Corp AA Y'ld (%)	FT 20 yr Gilt (%)	Margin (%)
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
Mar '22	2.71	1.84	0.87

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

Category	Mkt Val (£bn @ Mar 22 & 19, 16)			Weight (%)
Gilts (55)	1,650	1,376	1,253	72.8
Non-Gilts (1,183)	615	588	534	27.2
AAA (140)	128	121	104	5.6
AA (147)	76	84	97	3.4
A (379)	164	158	157	7.2
BBB (517)	248	225	177	10.9

Category	Mkt Val (£bn @ Mar 22, 19)		W't (%)	Dur'n (yrs)
Gilts (55)	1,650	1,376	72.8	12.2
< 5 Yrs (12)	406	348	17.9	2.8
5-15 Yrs (16)	514	364	22.7	8.0
> 15 Yrs (27)	730	664	32.2	20.4
Non-Gilts (1,183)	615	588	27.2	7.4
< 5 Yrs (457)	247	202	10.9	3.0
5-15 Yrs (493)	240	242	10.6	7.3
> 15 Yrs (233)	129	144	5.7	15.7

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

Category	Mkt Val (€bn)	Weight (%)
Sovereigns (448)	7,380	58.9
Non-Sovereigns	5,155	41.1
AAA (1,026)	1,347	10.7
AA (791)	1,241	9.9
A (1,332)	1,096	8.7
BBB (1,983)	1,470	11.7

Category	Mkt Val (€bn)	Weight (%)
1 – 3 Yrs (1,390)	2,773	22.1
3 – 5 Yrs (1,368)	2,589	20.7
5 – 7 Yrs (1,054)	2,004	16.0
7 – 10 Yrs (948)	2,065	16.5
10+ Yrs (820)	3,104	24.8

Table 2f: Breakdown of £ Index-Linked Market

Category (Number of issues)	Mkt Val (£bn @ Mar 22 & 19)		W't (%)	Dur'n (yrs)
Gilts (32)	829	720	100.0	20.3
< 5 Yrs (4)	93	79	11.2	2.1
5 – 15 Yrs (9)	223	170	26.9	9.4
> 15 Yrs (19)	513	470	61.9	28.3

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

Month End	US (%)	Euro (%)	Sterling (%)
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
Mar '22	5.70	4.23	6.08

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

£ Gilt Market “main” Issuance

- £3.25bn, ¼% 2025 (1.91x, 0.95%, 0%, Nov '21)
- £1.24bn, 1/8% IL 2031 (2.30x, -2.83%, 3%, Nov '21)
- £1.87bn, 1¼% 2051 (2.31x, 1.58%, 25%, 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.

