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OXFORDSHIRE COUNCIL PENSION FUND – 6 SEPTEMBER 2019

OVERVIEW AND OUTLOOK FOR INVESTMENT MARKETS

Report by the Independent Financial Adviser

Economy

1. The growth rate of the US economy in Q2 slowed to 2.2%, and China's to 6.2% (both annualised), while Japan, Europe and the UK all recorded growth close to 2%. On July 31st the Federal Reserve cut the US interest rate by ¼% to the 2 – 2 ¼% range – the first cut in over 10 years. Further cuts could be made later in the year depending on the progress of the economy and inflation. (In the table below the bracketed figures show the forecasts made in May)

Consensus real growth (%)						Consumer prices latest (%)
	2015	2016	2017	2018	2019E	
UK	+2.3	+2.0	+1.6	+1.4	+1.3(+1.0)	+2.0(CPI)
USA	+2.4	+1.6	+2.3	+2.9	+2.2(+2.2)	+ 1.6
Eurozone	+1.5	+1.6	+2.3	+1.9	+1.2(+1.3)	+ 1.3
Japan	+0.6	+0.9	+1.7	+0.7	+1.0(+1.0)	+ 0.7
China	+6.9	+6.7	+6.8	+6.6	+6.2(+6.3)	+ 2.7

[Source of estimates: Economist Intelligence Unit, July 27th, 2019]

2. Having failed on three occasions to gain parliamentary approval for the Withdrawal Agreement from the EU, Theresa May announced on June 7th that she would be standing down as Prime Minister once a successor had been chosen by the Conservative party. Boris Johnson became Prime Minister on July 24th, and chose a Cabinet fully committed to his policy of achieving Brexit by October 31st 'do or die'.
3. The increased tariffs imposed by the US on Chinese imports came into force in May and were reciprocated by China raising tariffs on \$60bn of US imports. Tensions between the two countries eased at the end of June when it was announced that trade talks would resume and the US lifted its ban on US companies supplying Huawei.
4. The situation in Iran has become an increasing cause of concern. In May Iran said it would stop adhering to some of its nuclear energy commitments under the 2015 Accord (from which the US had withdrawn), and after an unmanned US drone had been shot down by Iran in June, the US pulled back at the last minute from launching retaliatory air attacks. In July the UK impounded an Iranian oil tanker carrying oil to Syria, and Iran responded by harassing British-

flagged ships in the Persian Gulf, and then seizing the Stena Impero on July 19th.

- In Hong Kong in early June, massive demonstrations were mounted in protest at the proposed Extradition Law, which was later shelved. However, marches have continued to take place each weekend, accompanied by other protesters breaking into government buildings and defacing symbols of China's authority.

Markets

Equities

- Equity markets advanced strongly for the second successive quarter – the All-World Index has risen by almost 15% in the first half of 2019. Markets responded to the monetary easing in all regions, and to the (temporary) improvement in US-China relations. The relative weakness of the UK over the past three years is highlighted in the table, while Continental European Equities have rebounded sharply in 2019.

	Capital return (in £, %) to 30.6.19			
Weight %	Region	3 months	12 months	36 months
100.0	FTSE All-World Index	+5.3	+7.3	+37.4
56.9	FTSE All-World North America	+6.3	+11.8	+46.4
7.7	FTSE All-World Japan	+2.7	-3.5	+25.5
12.6	FTSE All-World Asia Pac ex Japan	+2.3	+1.9	+31.4
14.7	FTSE All-World Europe (ex-UK)	+6.9	+5.1	+30.9
5.2	FTSE All-World UK	+2.0	-3.0	+13.7
10.4	FTSE All-World Emerging Markets	+2.6	+5.0	+30.6

[Source: FTSE All-World Review, June 2019]

FTSE World Europe ex UK



Internal

7. All sectors – other than Oil & Gas – registered steady gains during the quarter.

	Capital return (in £, %) to 30.6.19		
Weight %	Industry Group	3 months	12 months
3.3	Utilities	+4.1	+15.0
10.8	Health Care	+3.0	+11.5
15.8	Technology	+5.7	+11.1
11.5	Consumer Services	+6.9	+10.1
13.0	Industrials	+7.0	+9.2
2.8	Telecommunications	+4.3	+7.6
100.0	FTSE All-World	+5.3	+7.3
21.5	Financials	+6.6	+6.5
11.1	Consumer Goods	+4.8	+4.5
4.3	Basic Materials	+4.6	+0.2
5.9	Oil & Gas	+0.5	-6.5

[Source: FTSE All-World Review, June 2019]

8. After a uniform rise across the market during the quarter, the mid- and small-cap sectors of the UK market continue to out-perform the large-cap sector over one and three years.

(Capital only %, to 30.6.19)	3 months	12 months	36 months
FTSE 100	+2.0	-2.8	+14.2
FTSE 250	+1.8	-6.6	+19.6
FTSE Small Cap	+1.9	-5.2	+24.6
FTSE All-Share	+2.0	-3.5	+15.4

[Source: Financial Times]

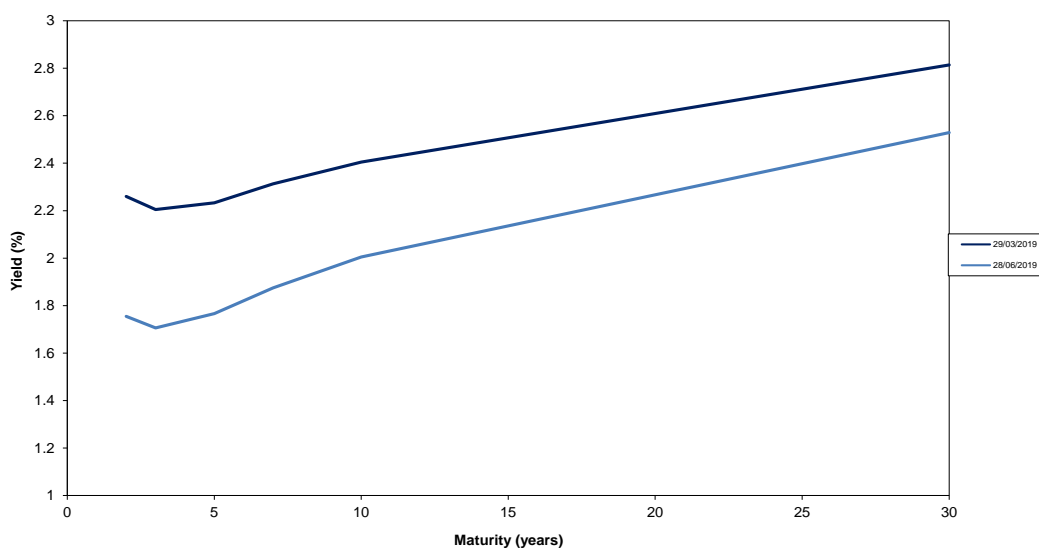
Bonds

9. Bond prices continued their first-quarter rise, as it became accepted that interest rates in the US and elsewhere were on a downward path. Yields on US Government bonds at all durations have fallen significantly during the quarter.

10-year government bond yields (%)	Dec 2016	Dec 2017	Dec 2018	Mar 2019	June 2019
US	2.46	2.43	2.68	2.42	2.01
UK	1.24	1.23	1.14	1.00	0.83
Germany	0.11	0.43	0.24	-0.07	-0.33
Japan	0.04	0.05	-0.01	-0.10	-0.17

[Source: Financial Times]

US Yield Curve



Currencies

10. Sterling weakened in May and June on political uncertainty, and fell by a further 4% against the dollar in July as the prospect of a no-deal Brexit became more likely under the new government.

				£ move (%)	
				3m	12m
	30.6.18	31.3.19	30.6.19		
\$ per £	1.320	1.303	1.273	-2.3	-3.6
€ per £	1.131	1.161	1.118	-3.7	-1.1
¥ per £	146.2	144.2	137.1	-4.9	-6.2

GBP vs USD



Internal

Commodities

11. The oil price rose to \$75/barrel in late-April when the US ended sanctions waivers on Iranian oil imports to India, China, Japan, S. Korea and Turkey, but later fell back to the mid \$60's range. Gold reached its highest price for over five years.

(\$)	<u>30.6.18</u>	<u>31.3.19</u>	<u>30.6.19</u>	<u>3m (%)</u>	<u>12m</u>
Gold	1251.6	1295.1	1402.5	+8.3	+12.1
Brent crude	79.2	67.6	64.4	-4.7	-18.7



Internal

Property

12. Following a similar pattern to that of the previous quarter, UK property values eased, so that it was only the income element which produced a positive total return. The woes of the retail sector became more widespread, as several big names announced store closures and negotiated for rent reductions from landlords. The 12-month total return of 4.0% is similar to that on the All Stock Gilt Index (+4.9%) and ahead of the All-Share Index (+0.6%).

	3-month (%)	12-month
All Property	+ 0.6	+ 4.0
Retail	- 0.9	- 3.9
Office	0.9	+ 5.8
Industrial	+ 1.7	+10.8

[MSCI UK Monthly Index of total returns, June 2019]

Outlook

13. From a UK perspective the progress of the Brexit negotiations before the deadline of October 31st overshadows all else, with the prospect of an early General Election a real possibility if parliament refuses to permit a no-deal exit. The outlook for UK equities, and for sterling, is unsettling under almost any scenario.
14. Elsewhere the situation with Iran, the US-China trade talks and China's possible reaction to the demonstrations in Hong Kong all have the potential to disturb equity markets. In such circumstances, however, government bonds are likely to be in demand because of their 'safe haven' status.

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August 1st, 2019

[Graphs supplied by Legal & General Investment Management]

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