

PENSION FUND COMMITTEE – 6 MARCH 2020

OVERVIEW AND OUTLOOK FOR INVESTMENT MARKETS

Report by the Independent Financial Adviser

Economy

1. The German economy grew by just 0.6% in 2019, its lowest annual rate since 2013. While keeping interest rates unchanged at the end of January, the Bank of England lowered its forecasts for UK growth to 0.8% in 2020 and 1.4% in 2021.

(In the table below the bracketed figures show the forecasts made in November)

Consensus real growth (%)						Consumer prices latest (%)
	2016	2017	2018	2019E	2020E	
UK	+2.0	+1.6	+1.4	+1.3(+1.2)	+1.2	+1.3 (CPI)
USA	+1.6	+2.3	+2.9	+2.3(+2.2)	+1.8	+2.3
Eurozone	+1.6	+2.3	+1.9	+1.2(+1.2)	+0.8	+1.3
Japan	+0.9	+1.7	+0.7	+0.8(+1.0)	+0.4	+0.8
China	+6.7	+6.8	+6.6	+6.1(+6.2)	+5.8*	+4.5

[Sources of estimates: 2019 - Economist Intelligence Unit, February 1st, 2020
2020- Legal & General Investment Management, end-2019]

*Since revised to 5%

2. In the UK General Election on December 12th the Conservatives gained an overall majority of 80 seats, which enabled them to pass legislation for the UK to withdraw from the EU on January 31st, 2020. Sterling had strengthened in anticipation of a resolution to the Brexit saga, rising to \$1.33 on the election result.
3. The US and China signed a phase 1 trade deal in mid-December, which rolled back some of the threatened tariffs, but still left several disputed areas unresolved.
4. Tensions rose in the Middle East after the US assassinated General Soleimani, a very senior Iranian, and several others, close to Baghdad airport. Iran retaliated by firing missiles at a US base in Iraq, but also mistakenly shot down a Ukrainian passenger plane taking off from Teheran airport, killing all those on board.

5. The spread of the coronavirus from Wuhan in China had caused 500 deaths by February 5th, from 25,000 confirmed cases. In an attempt to slow the spread of the virus, travel to and from China has been curtailed, and factories in Wuhan and elsewhere have remained closed after the China New Year holiday.

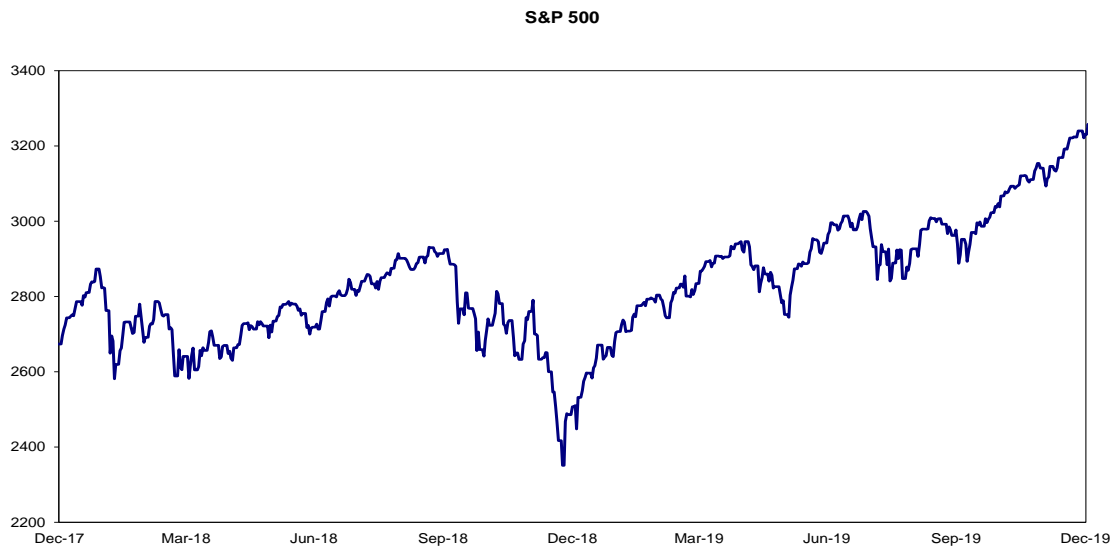
Markets

Equities

6. Although Overseas Equities were strong in local currency terms during the quarter, these gains were largely offset by the strength of sterling. The 19% return for the full year represented a very strong performance – following a weak 2018 – driven primarily by the strength of North American Equities (see graph below).

	Capital return (in £, %) to 31.12.19			
Weight %	Region	3 months	12 months	36 months
100.0	FTSE All-World Index	+1.1	+19.2	+24.8
57.2	FTSE All-World North America	+0.9	+23.9	+33.5
7.7	FTSE All-World Japan	+0.1	+12.1	+13.6
12.8	FTSE All-World Asia Pac ex Japan	+2.3	+11.1	+18.2
14.5	FTSE All-World Europe (ex-UK)	+0.9	+17.2	+17.1
5.1	FTSE All-World UK	+2.1	+12.9	+5.7
10.8	FTSE All-World Emerging Markets	+3.6	+12.4	+18.7

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



Internal

7. Technology continued to be the outstanding sector during the quarter, and for the year as a whole.

	Capital return (in £, %) to 31.12.19		
Weight %	Industry Group	3 months	12 months
17.1	Technology	+6.3	+36.7
12.8	Industrials	+0.5	+23.1
11.5	Consumer Services	-0.5	+19.9
100.0	FTSE All-World	+1.1	+19.2
21.2	Financials	+0.2	+16.3
10.9	Consumer Goods	-2.4	+15.8
11.1	Health Care	+5.7	+15.7
3.3	Utilities	-5.0	+13.8
4.1	Basic Materials	+1.8	+10.4
5.3	Oil & Gas	-2.1	+10.1
2.7	Telecommunications	-4.5	+7.7

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

8. UK Equities moved sideways in October and November, but then rose sharply in December on the Election result and the resolution of the Brexit deadlock.

Mid- and small-cap stocks were particularly strong, being less adversely affected by the strength of sterling.

(Capital only %, to 31.12.19)	3 months	12 months	36 months
FTSE 100	+1.8	+12.1	+5.6
FTSE 250	+9.8	+25.0	+16.6
FTSE Small Cap	+8.8	+14.9	+15.7
FTSE All-Share	+3.3	+14.2	+8.3

[Source: Financial Times]

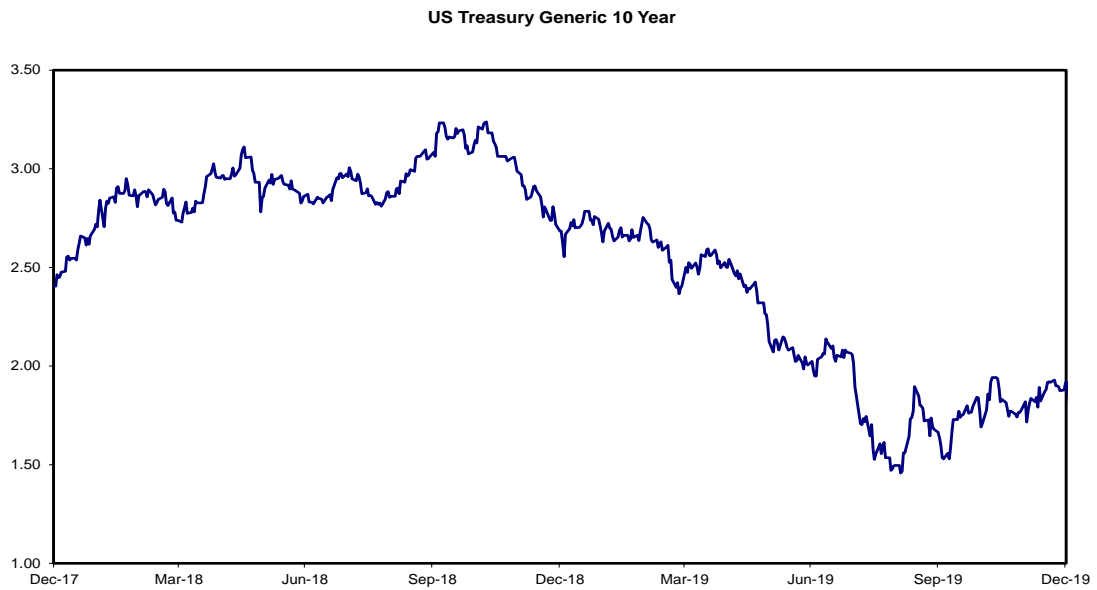
Bonds

9. Yields on Government bonds edged higher during the quarter, although they have fallen sharply in January on the expectation of slowing economic growth.

10-year government bond yields (%)					
	Dec 2016	Dec 2017	Dec 2018	Sept 2019	Dec 2019
US	2.46	2.43	2.68	1.68	1.92
UK	1.24	1.23	1.14	0.41	0.73
Germany	0.11	0.43	0.24	-0.58	-0.19
Japan	0.04	0.05	-0.01	-0.23	-0.02

[Source: Financial Times]

10. The 10-year US Treasury yield has fallen from over 3% to below 2% in the past 15 months.



Internal

Currencies

11. Sterling strengthened as the likelihood of a no-deal Brexit diminished, and rose further in December after the General Election resulted in a clear majority for the Conservative Party.

				£ move (%)	
				3m	12m
	31.12.18	30.9.19	31.12.19		
\$ per £	1.274	1.232	1.325	+7.5	+4.0
€ per £	1.114	1.130	1.180	+4.4	+5.9
¥ per £	139.7	133.2	144.0	+8.1	+3.1



Internal

Commodities

12. The price of Gold has reached its highest level for five years. The oil price was stable during the quarter, but then fell by nearly 20% in January on the likely impact of the coronavirus outbreak on China's economic activity.

(\$)	<u>31.12.18</u>	<u>30.9.19</u>	<u>31.12.19</u>	<u>3m (%)</u>	<u>12m</u>
Gold	1291.0	1489.9	1514.7	+ 1.7	+17.3
Brent crude	66.9	60.3	66.0	+ 9.5	- 1.3

Property

13. The total return on UK Property was below 1% for the third successive quarter, so that the 12-month All Property return of 2.1% compared poorly with the returns on UK Equities and Bonds over the same period.

	3-month (%)	12-month
All Property	+ 0.3	+ 2.1
Retail	- 2.8	- 6.4
Office	+ 1.5	+ 5.0
Industrial	+ 1.9	+ 7.2

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

Outlook

14. While the General Election has given the Conservatives a clear majority, it remains to be seen how the negotiations with the EU will progress during the remainder of 2020. The forthcoming Budget Speech will be analysed closely as a guide to how the government plans to adhere to its fiscal targets while honouring its election promises on taxes and spending.
15. The outbreak of the coronavirus epidemic has already had severe effects on travel and trade with China, which is likely to result in slower global economic activity for an indeterminate period.
16. In the United States, the acquittal of President Trump in the impeachment trial has ensured that he will be running for re-election in November. His Democratic Party challenger will not be known until July, but US stock market sentiment over the summer will be strongly influenced by whether it is likely that a less market-friendly candidate could oust President Trump in November.

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February 6th, 2020

[Graphs supplied by Legal & General Investment Management]

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