December 2023

# XPS Investment News

Bringing you our market round-up and the latest news affecting UK pension scheme investments

## Month in brief

- Both equities and bonds rallied on the growing belief that major central banks are winning the fight against inflation
- Another volatile month for UK gilts culminated in yields falling sharply overall despite expectations of UK borrowing rising in the aftermath of the Autumn Statement
- Prospects for economic growth remain a concern especially in the UK where there was no growth in Q3 and forecasts have been revised down for the next two years

Joe Howley
Investment Consultant

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Joe's December update

# Markets bounce back in November fuelled by optimism over interest rate cuts in 2024

Equities and bonds performed strongly over November, as markets began to price in interest rate cuts sooner in 2024 than previously expected. Comments from US and UK central bank policymakers left the door open to a relaxation of contractionary monetary policy in the first half of next year, but the timing of any rate reductions remains uncertain.

Global equities experienced their best month in three years during November as consensus grew that inflation has peaked in this current cycle. UK equities also finished in positive territory for November despite the revelation that the UK economy failed to grow at all in the third quarter.

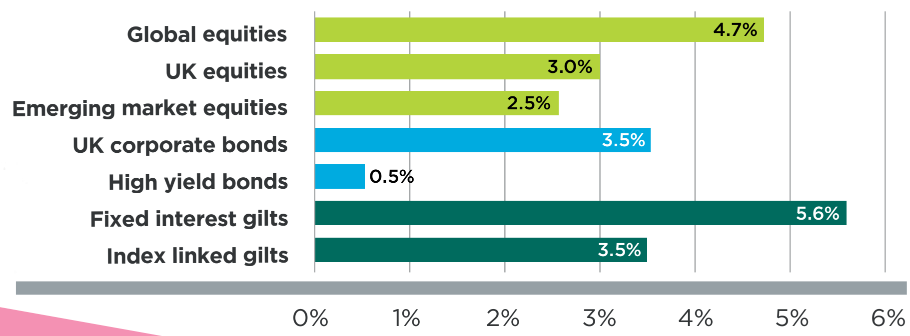
In fixed income markets, tightening credit spreads together with falling gilt yields brought about a bumper month for UK corporate bonds. Global high yield bonds also gained modest ground – spurred on by increasing confidence that falling borrowing costs next year will ease pressure on more highly indebted companies.

A series of rallies in gilt markets during the month saw both fixed interest and index linked gilts perform strongly overall. Expectations of higher public spending and tax cuts from the Autumn Statement briefly threatened to claw back some of the gains but gilts rallied again in the last week of the month to reverse this. Long term inflation expectations fell slightly and so the performance of index linked gilts lagged fixed interest gilts.

There was mixed messaging from the Bank of England (BoE) during the month over when interest rates in the UK might start to come down. The BoE's Chief Economist, Huw Pill, was dovish in

### Gilts rallied strongly over November

One Month to 30 November 2023



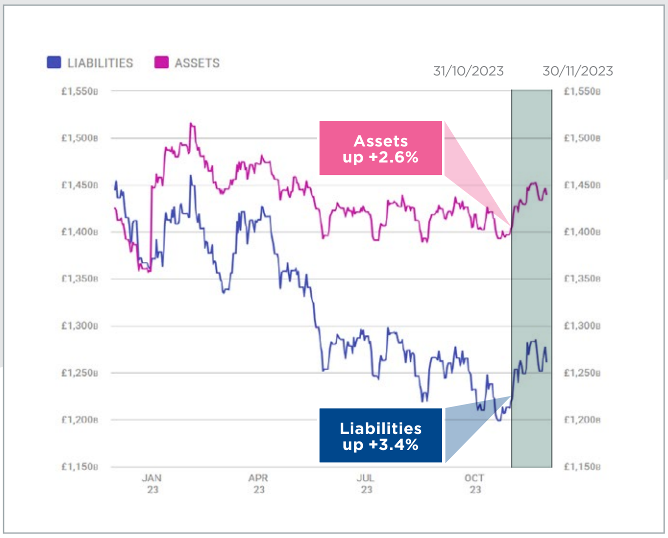

**Source**: Refinitiv Datastream

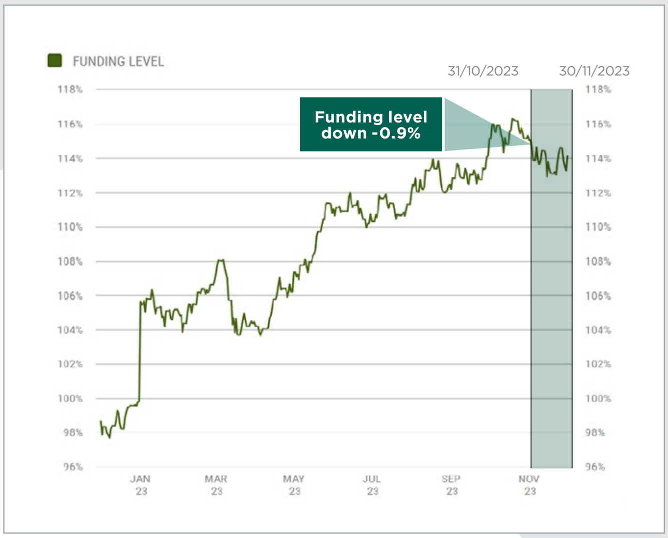
the early days of the month stating that expectations of cuts from next summer were not 'unreasonable'. But sentiment from senior policy makers turned more hawkish late in the month as the Deputy Governor, Dave Ramsden, warned that there was a long road ahead to squeeze inflation out of the system.

There was a similar mix of optimism and hesitation over the direction of interest rates in the US. Comments from one of the Federal Reserve's most hawkish policymakers, Christopher Waller, that interest rates could come down next year if inflation moderates 'for several more months' sat in contrast to Chairman Jerome Powell's wariness of the market being misled by positive news on headline inflation.

The outlook for global growth remains a key challenge for central banks globally. In November UK growth expectations for 2024 and 2025 were revised downwards to 0.7% and 1.4% by the Office for Budget Responsibility. Sluggish growth is also forecast in the US, Euro area and China in 2024.

Aggregate UK DB pension scheme funding on a low risk basis was modestly lower as liabilities grew by more than assets. However funding remains healthy overall especially after the substantial bond market sell off over the year to date.




**Source**: XPS DB:UK www.xpsgroup.com/services/xps-pensions/xps-dbuk-funding-watch

The charts above are based on data from The Pensions Regulator, the PPF 7800 Index and the XPS data pool. The assumptions used in the UK:DB long-term target basis include a discount interest rate of gilt yields plus 0.5%. The assumed asset allocation is 16.9% equities, 20.0% corporate bonds, 6.9% multi-asset, 5.1% property, 3.8% private markets and 47.3% in liability driven investment (LDI) with the LDI overlay providing a 60% hedge on inflation and interest rates.

## To discuss any of the issues covered in this edition, please get in touch with Joe Howley.

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## Alternatively, please speak to your usual XPS Investment contact.

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