Investment report for Teesside Pension Fund
March 2024

Before I get into the meat of the paper I thought I should share some academic thinking on the best strategy to enable pensions to be paid in the future. Three academics from the Universities of Missouri, Emory and Arizona in the United States looked at various styles of investment strategy. They evaluated fixed bond and equity strategies, dynamic lifestyle strategies, and 100% equity strategies and concluded that the 100% equity strategy was the most appropriate and most likely to provide the best pension cover.

I think the committee should give itself a pat on the back for having the vision to adopt such an equity heavy policy many years ago.

(I suggest we ignore, for the moment, the myriad of academic papers which are at odds with these findings.)

Political and economic outlook

When I wrote my last piece Jeremy Hunt had just presented the autumn statement which highlighted just how little room he had for manoeuvre and the pressure it would put on departments providing services and support. As I write this, despite his assertions that the UK economy is doing well he's going the media rounds explaining why he can't give that much away due to constraints on government funding. All will be revealed on Wednesday.

I have batted on previously about the increasingly multi-sector nature of economies and the declining impact of governments' fiscal policy and central banks' monetary policy. As the number of sectors in the economy become greater and they become less correlated and dependent on one another GDP growth takes on an autonomous nature. It ploughs on near

regardless of government and central bank actions. In effect this explains why central banks raising interest rates has had little or no material impact on inflation levels which have come down naturally as supply constraints have resolved themselves. Higher interest rates do slow economic growth and this is worrying as I think an inflation target of 2% , which was set in a golden age of global goods disinflation, is unachievable in today's economic climate. As I have said previously the inflation rate is likely to settle at about 4% in the UK and about 3% in the United States. If central banks misguidedly think the 2% level is achievable in the short-term and over the longer term then downward pressure will be put on economic growth despite the resilience inherent in the current economic structure.

If endogenous actions become less relevant to the direction of the economy and stock markets, then by implication exogenous factors become a greater determinant of performance. Those investors able to correctly read the implications of exogenous events will be the winners.

The absence of resolution to the wars in Gaza and Ukraine and elsewhere in the world is very worrying. The US failure to provide more arms to Ukraine is particularly concerning but hopefully will be resolved by mid March.

George Galloway's success in Rochdale was not a surprise after labour's withdrawal and in my opinion does not signal a move to extremism in British politics. Far more worrying is Donald Trump's success in gaining the Republican party nomination as this has profound implications on the future world order. It has the potential to emasculate the West and hand over power to totalitarian governments such as Russia or China.

Apart from the United States and some Southeast Asian countries (excluding China) economic growth is likely to be subdued over the medium term. The US is likely to be the most dominant economy for the foreseeable future albeit driven by a small base of companies. This clearly has risks.

Markets

With US inflation at 3.1% the real yield on treasuries is just over 1%. In the UK 10-year gilts have a zero real return with inflation standing at 4%. I believe there will be little improvement in the inflation figures for some time. The attitude of both jurisdictions to issuing more and more debt would indicate that these real yield levels are on the low side. Corporate bonds will trend in the same direction as government bonds which is likely to be down.
Index linked securities will suffer as yields revert to the long-term norm.
Major equity markets have been on a generally positive trend over the past year and this is unlikely to alter. Short term interest rates are near or at a peak which should prove beneficial to equity performance.
Opportunities are likely to present themselves in the property market due to its inefficiency with the usual caveats on covenants etc..
The same applies to private markets, infrastructure and the like where individual investment opportunities are of a diverse nature.
Although it is still not a preferred investment, holding cash it's not the drain on returns that it was 18 months or so ago.

Portfolio recommendation

The continuing low level of real yields make fixed interest, both conventional and index linked unattractive.
Quoted equities continue to look better value than fixed interest and should be able to make some small absolute gains over the coming year.
The substantial commitment to private markets and infrastructure have reduced the options available for diversification over the medium and long

term. This might not be such a bad thing because of the equity style nature of the private portfolios which should enhance long-term returns.
Despite the above there could still be some attractive opportunities in the property market.
Cash should ,as usual, be used as a facilitator.

Peter Moon
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