Investment report for Teesside Pension Fund
June 2024

Political and economic outlook

It's been a busy time for democracies on both sides of the pond. Joe Biden must be wondering just what he has to do to ensure a victory over Donald Trump in the Presidential elections in November. The fact that Trump has been convicted of some pretty serious offences does not seem to have dented his popularity at all. Additionally Trump himself, his supporters and his legal team have criticised the legal system and democracy itself in the United States. This is playing fast and loose with hard fought freedoms now enshrined in democracies worldwide. Dangerous territory indeed. The whole worrying farce makes me think that Trump's supporters are the very antithesis of comedy writer Frank Muir's description of Joan Bakewell as "the thinking man's crumpet". Clearly not a phrase that can be used nowadays but justifiable when referring to a man like Trump and by association his supporters.

Meanwhile an election has been called in the UK. When he became prime minister I thought that Rishi Sunak would be a breath of fresh air compared to a number of his predecessors, especially in terms of his political and economic judgement. It beggars belief that apparently an election can be called on the basis of an unexpectedly good CPI inflation number when the Conservative Party is over 20% behind in the opinion polls. It could be that the Prime Minister has been reading your advisors' investment reports and has taken their view that inflation of around 2% is unsustainable. If so I would certainly question his political and economic judgement.

The seemingly unstoppable rise of populism could have a detrimental impact on democracies in Europe and potentially on the European Union.

All this uncertainty puts a strain on the rules based system of world order and on the functioning of democratic governments it could well beckon a sustained period of instability in the world.
World economic growth forecasts are pretty anaemic at around the 3% level. China is supposedly growing at around 5% but this is aided and abetted by some unnecessary construction and government expenditure. Without this expenditure China's growth rate is probably near zero.
The US economy is growing at a modest 2%, below its long term average.
Brexit will continue to have a negative impact long-term on UK growth prospects which at the moment is forecast to be a paltry 0.6% in 2024.
The modest growth rate is reflected across the world including the EU, Asia (driven mainly by China) and resource and commodity economies. India, with a forecast growth rate of 6.5%, is doing relatively well and should continue to do so.
Both short term and long-term interest rates look as if they are at or near peaks with declines expected by markets over the next two years.
Inflation should continue to be modest but I expect it to remain above central banks’ target levels.
Conflict and instability are still a major concern, with little prospect of a return to a more comfortable environment. The war in Ukraine has turned in Russia's favour and this will force some difficult choices on European countries and NATO. The war in Gaza, and its conduct, will leave long-term scars and will have done nothing to have eased tensions in the Middle East in the future.

Markets

Real interest rates remain low but have increased as inflation has continued to decline. The question is whether they have increased enough

to satisfy buyers when the debt to GDP in most western economies is at a near time high.
10 year UK Index linked gilts have a real yield of about 1.1% which is about half the yield on U.S TIPS. The US index linked market is trading on a yield comparable with those pre- the financial crisis. UK gilts on the other hand are trading at about half the level pre- the global financial crisis.
Developed equity markets are trading at all time highs despite the rising bond yield environment. As I said previously, equity markets don't like uncertainty but at present they seem to be ignoring the perilous political environment and extreme economic imbalances.
It is difficult to see the property market making much progress in a slow economy and higher interest rate environment.
Capital raising has been difficult in the alternatives market and this is likely to be reflected in the performance of this sector.

Portfolio recommendation

.

Although real yields have risen the environment for fixed interest and gilt markets is not particularly attractive and a low weighting should be maintained for these assets.
UK index linked have become more attractive but not yet sufficiently well priced to be purchased.
Equity markets have made good progress in most areas apart from emerging markets. There are clearly uncertain times ahead and the fund has already taken substantial amounts out of equities. The current weighting would seem appropriate until other assets become more attractive.

The property weighting should be maintained until better opportunities present themselves in an improved environment.
The current commitments to alternatives is more than adequate as we have discussed previously.
Given the apparent cash flow deficit because of the nature of the units we hold with Borders to Coast it would be prudent to hold a sufficient cash balance to meet the imbalance.

Peter Moon
3 June 2024