PML GROUP
Pensions Management
& Financial Services

Welcome to Bulletin 37 | December 2013

In this issue we focus on:

- Debt is good?
- Mark Carney's strategy. Will it succeed?
- Opportunities for the coming year

In this closing bulletin of 2013, I want to take a moment to reflect upon the year that's passing and then shout a big welcome to the opportunities that I see unfolding in the year to come.

Debt is good?

2013 was the year we finally recognised that we shouldn't worry any longer about debt. Debt is good; debt is cheap, it has the Government's blessing; it isn't going away and doesn't threaten our existence at all. Welcome back, the old order. An order where spending is admired and applauded – and prudence roundly discouraged. Five years ago, it seemed that 'time' was about to be called on the economic booze-up – but no, all's well. Living beyond our means isn't only acceptable, it's positively encouraged. So keep spending – the nation's health is at stake – and our recovery depends on it.

Over the last 3½ years, George Osborne has steadily run up an additional £500 billion of Government borrowing, nearly doubled our Debt/GDP ratio (to 75%) and taken the national debt up to £1.2 trillion. Interest payments on the nation's borrowings are now the 4th highest item of departmental expenditure of all Government departmental costs. And still the borrowing goes on. But good news – there's no need for us to change our ways after all.

Mark Carney's strategy. Will it succeed?

Should you seek endorsement of these extraordinary circumstances then look no further than the way in which our Conservative led coalition Government is now being lauded as an example to our friends in Europe – upon how to stage a recovery from recession. The formula of ultra-low interest rates, phantom money printing, endless debt remortgaging and unrestrained commitment to huge capital projects, might defy logic and baffle brains – but is considered sufficient for the day – because it lifts morale... and buys time. It's little surprise that Mark Carney's 'forward guidance' strives to contain and control interest rates within their current negative real territory.

But is Mark Carney's strategy likely to succeed? In recent months, UK gilt yield has reflected a global rise in interest rates, where the UK 10 year gilt yield had climbed steadily from 1.7%, a year ago, to just short of 3% today. This rise in yield constitutes international opinion upon the health of UK finances, the inevitable ending of QE... and the expectation of modest economic recovery.

Our economic recovery may well be courtesy of negative real interest rates and a growing debt mountain – but it is gaining ground. And higher levels of economic activity herald an emerging appetite for risk. So, whilst Mark Carney may well succeed in containing domestic interest rates for a while yet, international opinion is that something is going to have to give. Credit restraint would be ideal – but don't expect it on any political agenda.

Opportunities for the coming year

The recovering economic climate seems unlikely to alter course within the next 12 months. Over the uncertain times of the last 12 months, the FTSE 100 has gained ground and recorded a gain of over 9%, whilst delivering a yield of around 3%. Over the same period, 10 year gilt yield has grown from 1.7% to 3% and so delivered capital losses. Meanwhile, Fixed Term Deposit rates have declined from a dismal 2.50% to a laughable 1% - or minus 2% in real terms.

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It therefore seems that the stage is set for lively asset allocation discussions.

The disincentives for holding cash on deposit will be clear to all – 'real' value will now be lost. Bond investment will always have a purpose, both as an asset class balance and a known maturity value, but Bond yields have plotted an upwards course – which may well have much further to go and rising yields spell capital losses. Property will always have a part to play as an important asset class, a generator of income and as a longer term investment hold. Property prices seem to have stabilised and should the recovery strengthen may next be moving higher.

Looking beyond property and setting aside, for the moment, the multiple esoteric investment vehicles we witness, we arrive finally at Equities. Dismal yields elsewhere are no reason whatever to plunge into equity risk – but they do form part of the background, from which equity investment might well flourish. There will, I think, be a time when equity markets begin to reflect the economic recovery that our debt accepting philosophy will engender. And I don't think that time is very far away.

So, the message for 2014 is: take a fresh look at asset class spread, asset class apportionment and the time period over which your assets are required to perform.

We're here to help.

May I wish you a Merry Christmas and a prosperous new year.

Geoffrey Stait
18 December 2013