Appendix A

Q2 2021
Capital Markets Outlook

September 2021

Essex County Council

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HYMANS ROBERTSON

Economic background

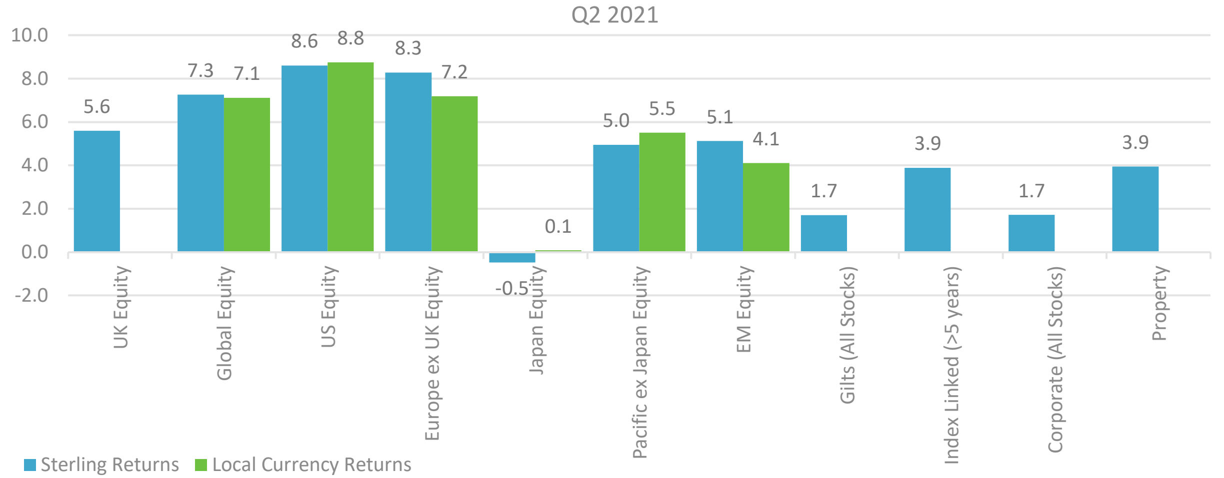
Despite upside inflation surprises, US and UK sovereign bond yields have fallen since the end of March. On news the Fed expects to increase its policy rate twice in 2023, short-term yields rose, and longer-term yields fell.

Equity markets rose over the quarter but the recent fall in yields saw shorter duration sectors and styles underperforming..

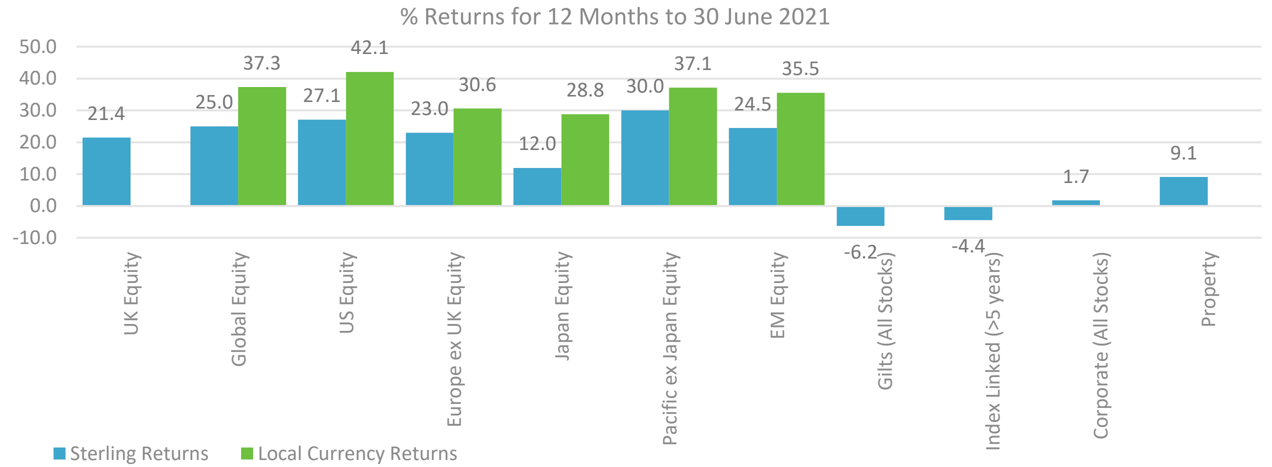
Global credit spreads continued to trend lower in-line with improving credit fundamentals and oil prices rose strongly.

The rolling 12-month total return on the index was 9.1% to end-June, with monthly returns positive since July 2020.

Market Returns



Source: DataStream



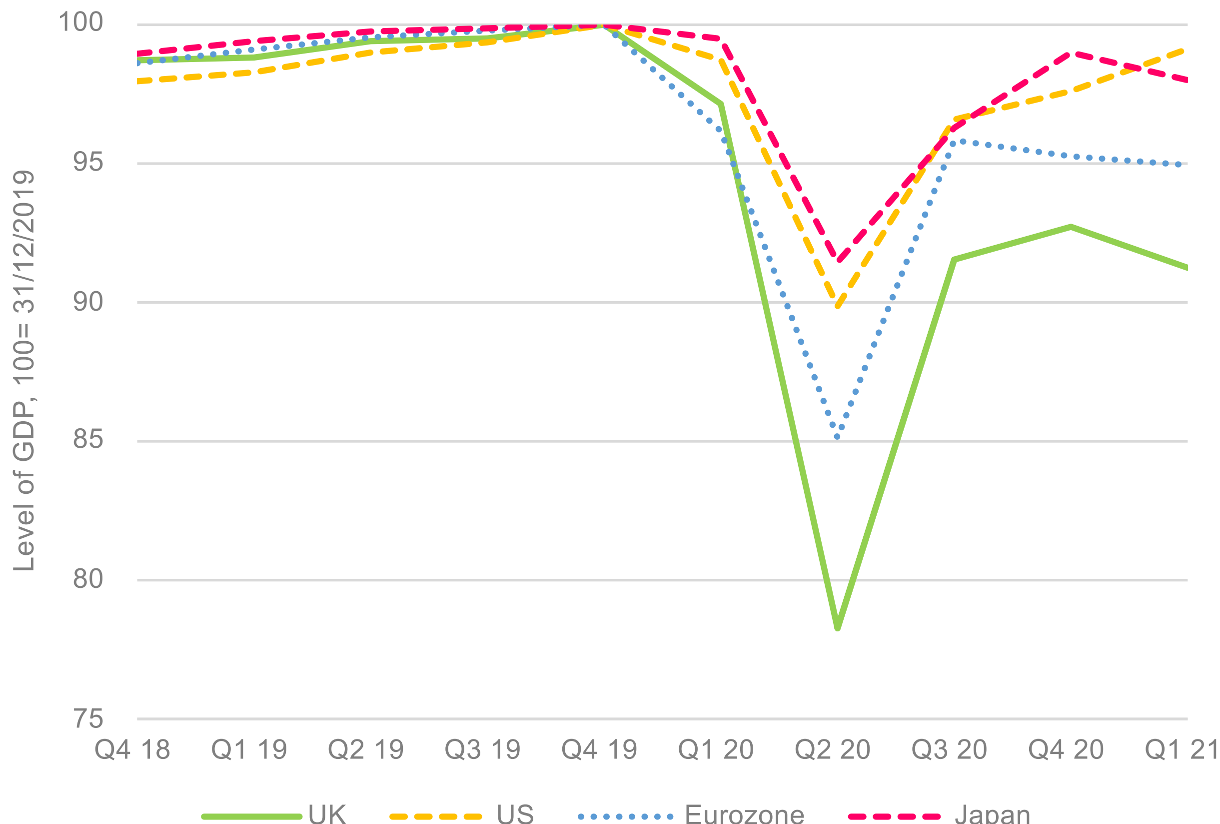
Source: DataStream

Recent data confirm that although the quarterly pace of global growth slowed in Q1 2021 after a robust H2 2020, the hit to activity from tighter restrictions had been less than feared.

The US economy expanded 1.6% quarter-on-quarter, as household spending started to show the impact of fiscal stimulus, contractions of 0.6% and 1.5% in the UK were smaller than economists had expected.

Effective vaccines enabling an easing of restrictions and greater economic resilience to the latest waves of COVID-19 suggest the global economy grew at a robust pace in Q2.

GDP Growth



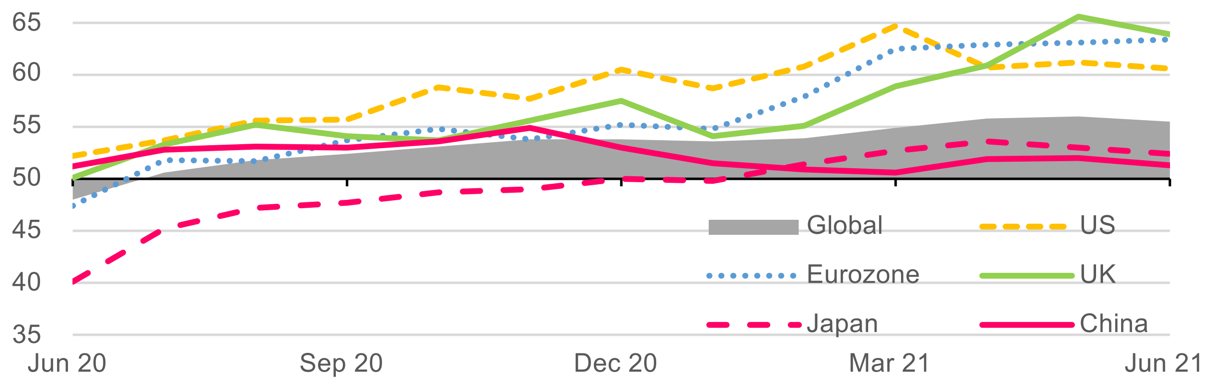
Source: DataStream

June's survey data show composite PMIs remain at or near record highs, suggesting growth momentum remains robust.

Global service sector data have been more resilient than manufacturing data in recent months, indicating the recovery is increasingly spreading from manufacturing to services as economies benefit from a relaxation in restrictions.

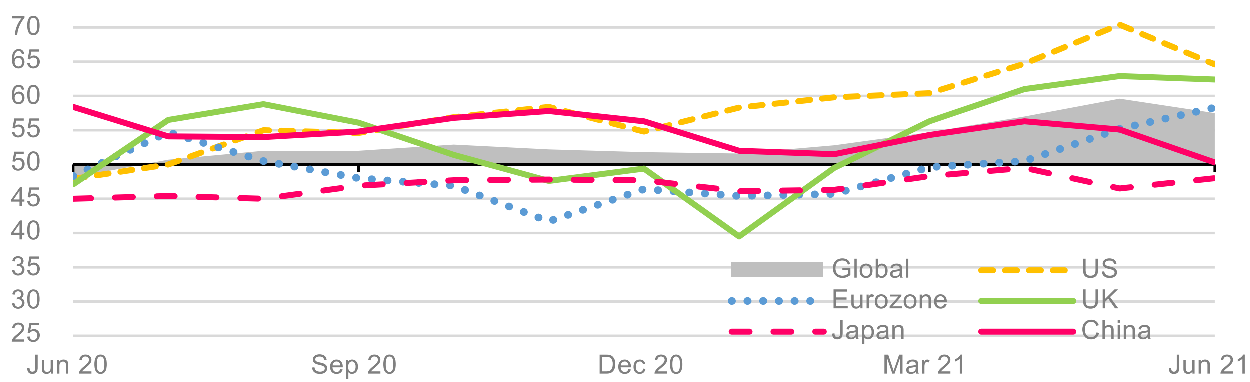
The detail of surveys show businesses are still constrained by problems in the supply of materials and labour. Selling prices for both goods and services are rising at unprecedented rates.

Manufacturing PMI



Source: Bloomberg

Services PMI



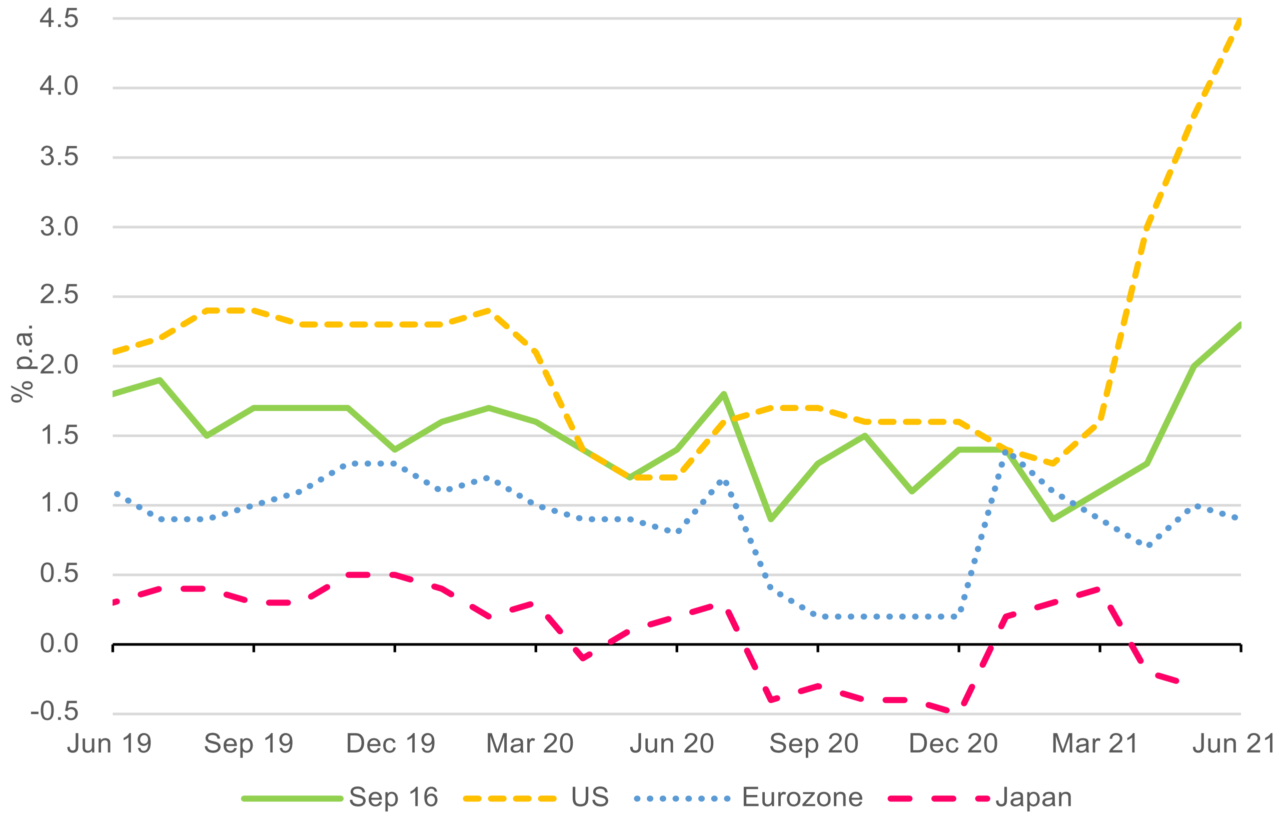
Source Bloomberg

UK headline CPI inflation rose to 2.5% year-on-year in June, partly due to price rises for food, second-hand cars, clothing and footwear, and dining out. Core inflation, which excludes volatile elements like food and energy rose to 2.3%.

After rising to 5.0% in May, US headline inflation rose to 5.4% year-on-year in June. Core CPI rose to 3.8% in May and 4.5% in June.

Although these recent numbers have exceeded expectations most forecasters expect the inflationary spike to prove temporary, and pressures to ease as we enter 2022.

Core CPI Inflation



Source: DataStream

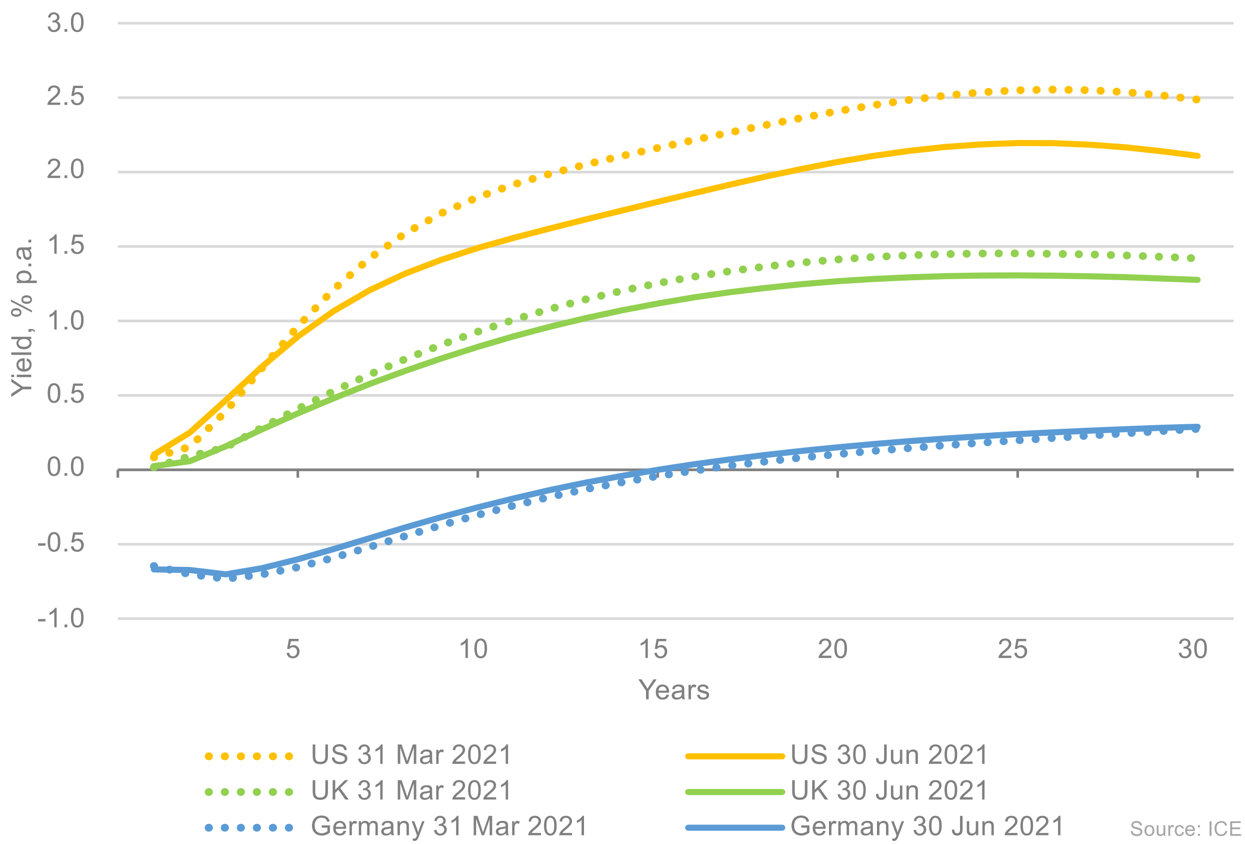
Asset class views

The Fed surprised markets by suggesting rates may rise in 2023 even as they re-iterated current inflationary pressures are likely transitory. Nevertheless, Treasury yields declined in Q2, perhaps reflecting perceptions the quarterly pace of US growth has already passed its peak.

The UK yield curve has also flattened since the end of March as longer-term yields fell, despite upside inflation surprises.

In contrast, there was little change in yields across the German yield curve.

Conventional government bonds



Source: ICE

Global credit spreads continued to trend lower in-line with declining default rates and improving credit fundamentals.

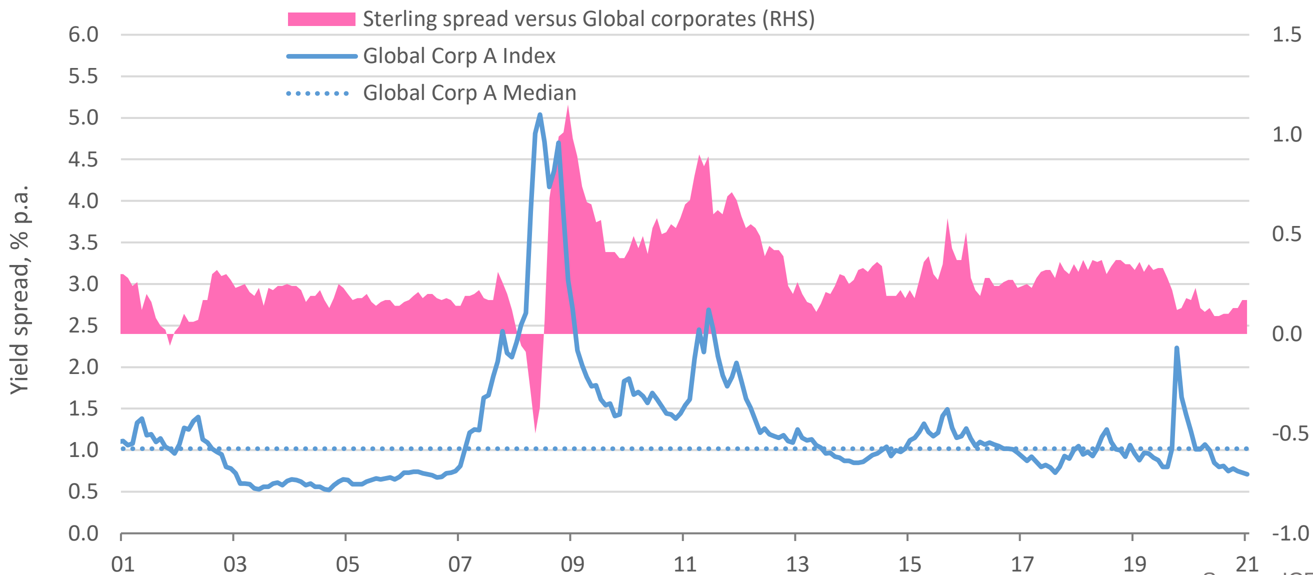
Corporate earnings have continued to accelerate, and economic optimism has improved. However, investment grade spreads (UK and Global), on a ratings-consistent basis, are at or near all-time lows.

While consensus points to inflationary pressures being transient, long-duration, low spread, investment-grade credit markets are susceptible to potential rates volatility and upside inflation surprises.

Overall, despite near-term fundamental support and tailwinds from ongoing investor demand and accommodative central bank policy, we maintain a degree of caution given current valuations.

Investment-grade corporate credit

Spreads (bps)	30 June	-3 Mth	-12 Mth	10-yr Median
US IG	**86**	97	160	**136**
Sterling IG	**106**	113	175	**149**
Euro IG	**84**	91	148	**120**



Source: ICE

	Fundamentals	Valuations	Technicals	Overall
Global IG credit	Neutral	Unattractive	Neutral	**Cautious**
Sterling IG credit	Neutral	Unattractive	Neutral	**Cautious**

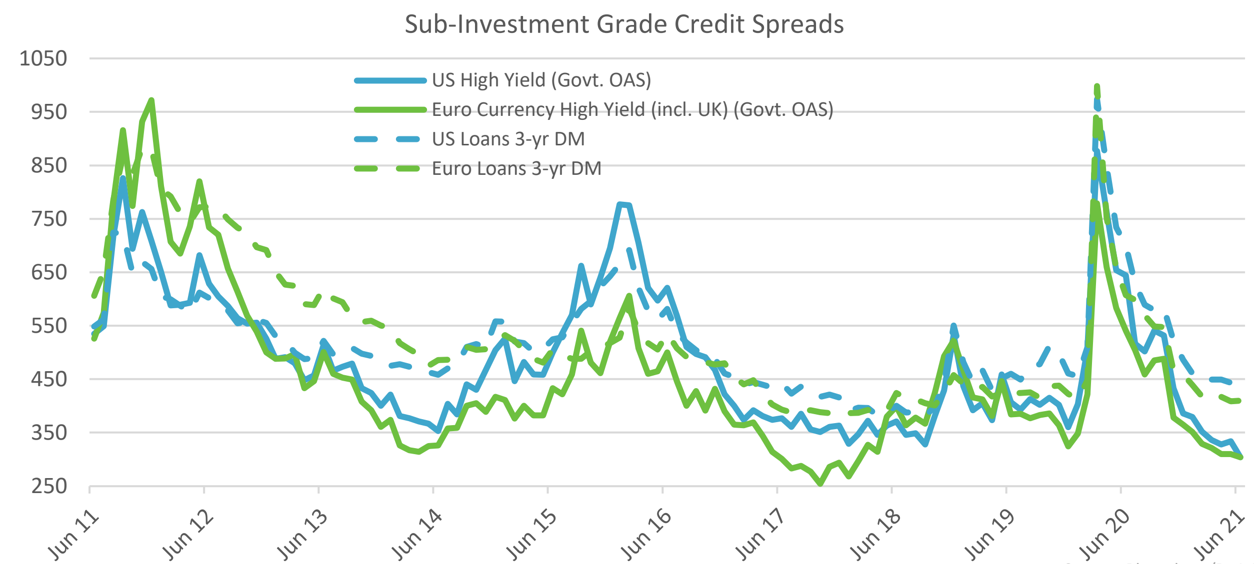
Speculative-grade credit yield

Global speculative-grade spreads fell 0.3% p.a. to 3.5% p.a. and are now below end-2019 levels and in-line with the lows of January 2020.

Default levels have passed their peak and are expected to fall well below longer-term average levels by the end of the year. However, our cautious view is predicated on spreads which are well below long-term median levels and are already fully pricing in the more favourable environment.

In private debt, the illiquidity premium relative to the traded loans market is in-line with historical averages. And, while traded loan spreads are low versus history, they are less so than equivalent high yield spreads. Market activity is high and competitive, particularly in defensive assets.

Spreads (bps)	30 June	-3 Mth	-12 Mth	10-yr Median
US HY	**304**	336	644	**458**
Euro Currency HY	**304**	321	541	**412**
US Loans 3-yr DM	**443**	449	700	**502**
Euro Loans 3-yr DM	**410**	425	607	**498**



Source: Bloomberg/BoA ML

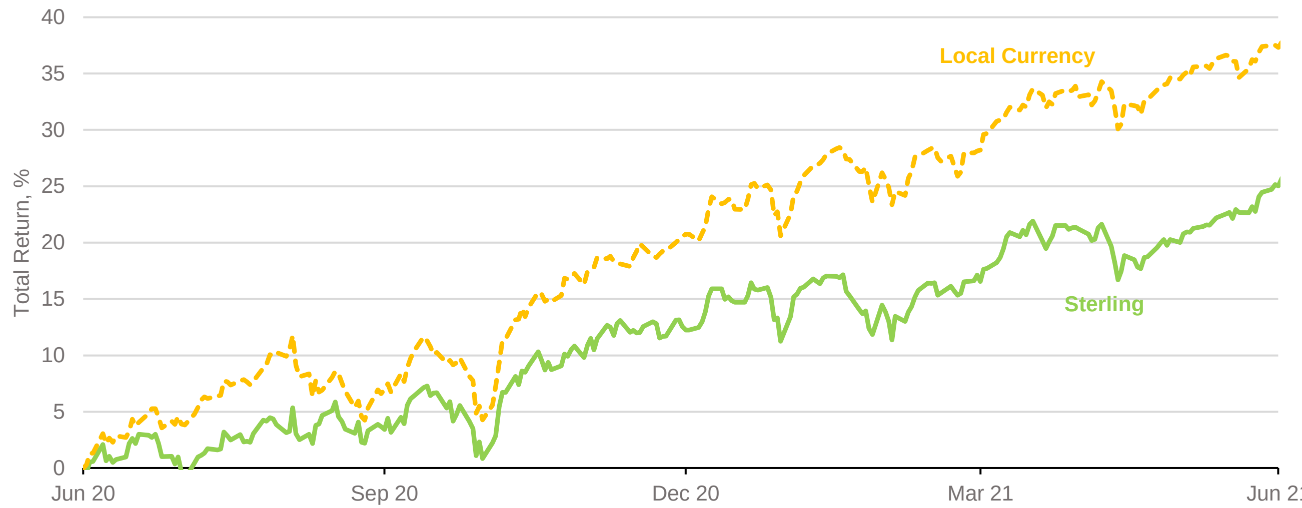
	Fundamentals	Valuations	Technicals	Overall
Liquid HY/loans	Neutral	Unattractive	Neutral	**Cautious**
Private loans	Neutral	Neutral (*relative*)	Neutral	**Neutral to Cautious**

Equities

Global equity markets gained 7.1% in Q2 to reach new highs, shrugging off inflation concerns and any indications of monetary tightening. Performance over the quarter has been aided by strong flows on the back of positive economic growth and earnings momentum.

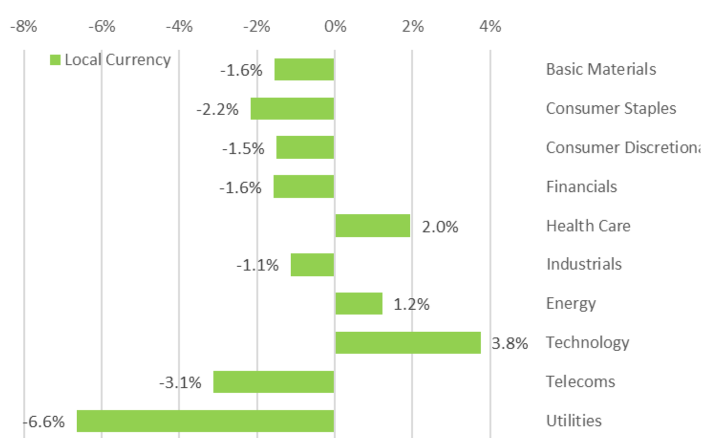
Cyclical, shorter-duration sectors, such as financials, industrials and basic materials, and styles, such as value and small-cap, have underperformed, having outperformed significantly since the initial positive vaccine news in November last year. Conversely, technology, with its longer-duration growth characteristics, outperformed during Q2.

Global equity returns



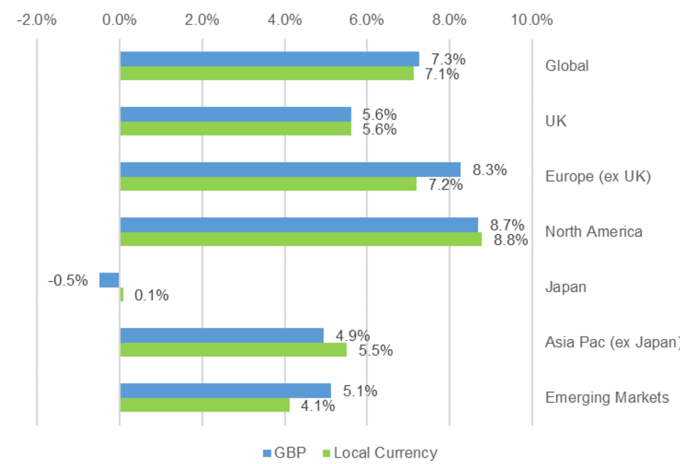
Total returns 30 Jun 2020 to 30 Jun 2021. Source: DataStream

Relative Q2 equity sector performance



Global Sector returns relative to FTSE All World Index 31 Mar 2021 to 30 Jun 2021. Source: Datastrea

Q2 Regional Equity performance



Total returns 31 Mar 21 to 30 Jun 21. Source: DataStream

The final Q2 earnings growth rate for US companies (S&P 500) was 64 %, the strongest year-on-year earnings growth rate since 2010, with a record number of companies indicating positive EPS guidance. Cyclical sectors such as energy, materials and financials led the EPS guidance increases (in the US) alongside technology.

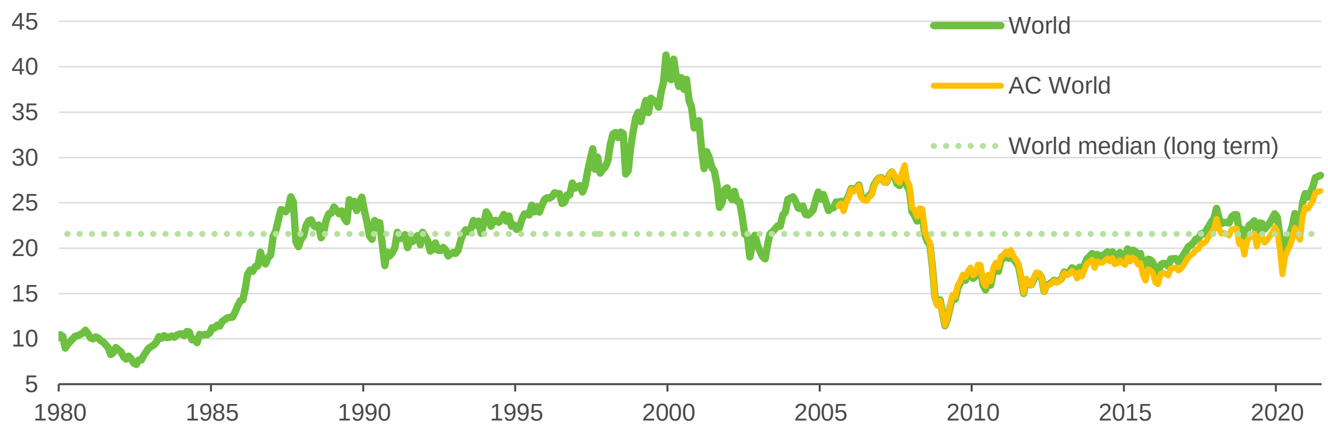
IBES forecasts for full-year earnings rebound for the MSCI World index in 2021 stand at approximately 38%, which would leave earnings 16% above end-2019 levels.

Global equity prices have risen in-line with the improving fundamental outlook, with valuation multiples still looking stretched vs history.

Global equities

Region (MSCI index)	P/E (Trailing)		P/E (Shiller)		Price/Book		Price/Sales		EV/EBITDA		Dividend Yield (%)
	Current	Historic Median	Current	Historic Median	Current	Historic Median	Current	Historic Median	Current	Historic Median	
World	27.4	18.6	27.9	21.6	3.2	2.2	2.0	1.3	14.2	10.0	1.7
US	29.7	18.3	35.4	20.7	4.8	2.6	2.6	1.6	16.3	10.8	1.3
EM	18.7	14.5	16.7	15.4	2.1	1.7	1.1	0.9	11.0	8.2	1.8
UK	23.6	14.1	14.2	14.9	1.8	1.9	1.2	1.2	8.9	7.7	3.2

MSCI World and AC World cyclically adjusted price-to-earnings ratio



	Fundamentals	Valuations	Technicals	Overall
Global equity	Attractive	Unattractive	Neutral	**Neutral**

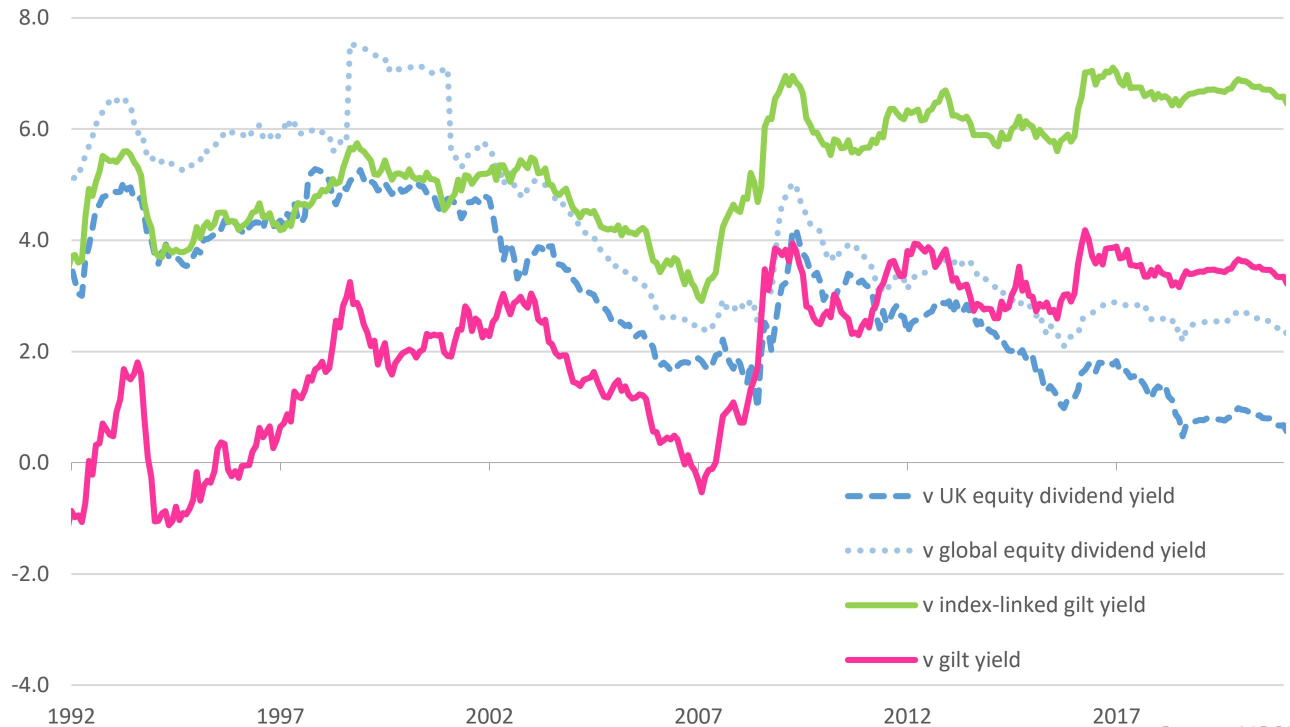
Rolling annual capital returns for the UK Monthly Property Index are in positive territory and continue their upwards rise as the steep falls recorded at the outset of the pandemic fall out of the comparison.

A 3.4% rise in the year to June is attributable the buoyant industrials sector, where capital values have risen 17.9% over the last 12 months. Retail sector capital values are 5.4% lower over 12 months, but the pace of declines is slowing.

There are positive signs for UK property market fundamentals, particularly from the occupier market. The recovery in transaction activity continues to gather pace although it remains too early to conclude that this will be sustained despite greater course of optimism.

UK property

UK property initial yield



Source: MSCI

	Fundamentals	Valuations	Technicals	Overall
Core	Neutral to Unattractive	Unattractive	Neutral	**Cautious**
Long Lease	Neutral	Unattractive	Neutral	**Neutral to Cautious**

Appendix

Consensus forecasts

GDP Growth (%)	2020 Actual	Forecasts for 2021		Forecast for 2022	
		Jun 21	***Mar 21***	**Jun 21**	***Mar 21***
World	-3.6	5.8	*5.3*	4.3	*4.1*
US	-3.5	6.7	*5.7*	4.1	*4.0*
UK	-9.8	6.6	*4.6*	5.3	*5.8*
Eurozone	-6.7	4.4	*4.3*	4.4	*4.2*

Consumer Prices (%)	2020 Actual	Forecasts for 2021		Forecast for 2022	
		Jun 21	***Mar 21***	**Jun 21**	***Mar 21***
World	2.1	3.1	*2.6*	2.8	*2.7*
US	1.2	3.5	*2.4*	2.6	*2.2*
UK	0.8	1.7	*1.6*	2.3	*2.0*
Eurozone	0.3	1.8	*1.5*	1.4	*1.3*

Asset class views framework

The views are intended to give a guide to our views on markets over the medium term; although they are updated quarterly, they are not intended as tactical calls.

The views reflect our expectations of absolute returns and assume no constraints on the investment decisions. In practice, they need to be interpreted in the context of the strategic framework within which individual funds are managed.

Fundamentals

These are the underlying economic drivers of an asset class which impact returns. Examples of fundamental factors include earnings, rents, inflation, interest rates, defaults, and leverage levels.

Valuation

Valuation is concerned with the price the market places on the relevant fundamentals and how that compares with history and/or our view of fair value.

Technicals

These are shorter-term factors that may tend to move markets back towards or further away from fair value. These are often factors which impact the supply/demand balance and include asset flows, issuance, investor confidence, central bank intervention, and geopolitical risk.

Risk warnings

General risk warning

Please note the value of investments, and income from them, may fall as well as rise. This includes equities, government or corporate bonds, and property, whether held directly or in a pooled or collective investment vehicle. Further, investments in developing or emerging markets may be more volatile and less marketable than in mature markets.

Exchange rates may also affect the value of an overseas investment. As a result, an investor may not get back the amount originally invested. Past performance is not necessarily a guide to future performance. Private equity investments, whether held directly or in pooled fund arrangements carry a higher risk than publicly quoted securities. The nature of private equity pooling vehicles makes them particularly illiquid and investment in private equity should be considered to have a long time horizon.

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