Institute and Faculty of Actuaries

Implications of Low Gilts Yields and Outlook for Capital Markets

Duncan MacInnes, Ruffer LLP

15 March 2017

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Started in 1994 by Jonathan Ruffer

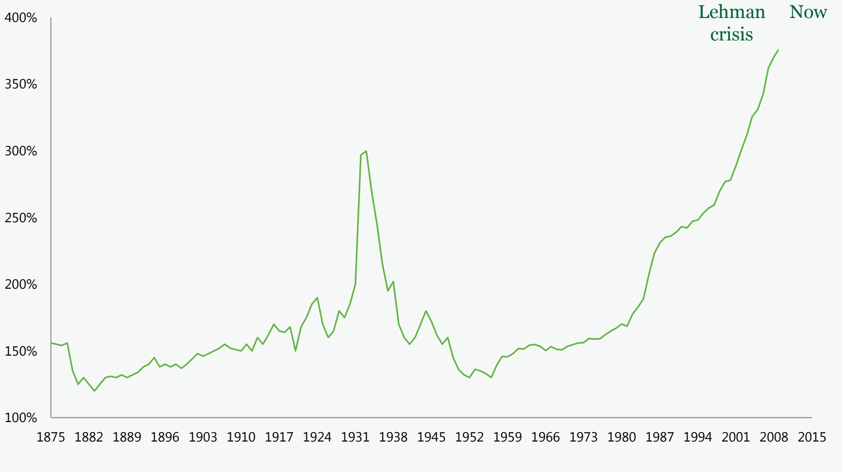
Single investment objective: absolute return

- capital preservation: not to lose money on a rolling 12 month basis
- consistent positive returns: significantly greater than the return on cash

'Multi asset' approach, unbenchmarked

Active asset allocation

Deleveraging has only just begun



Source: US total debt to GDP; Datastream to 31 December 2015

Ways of reducing a debt burden?

Real growth

Austerity

Default

Surprise inflation

Prolonged financial repression

According to Reinhart and Sbrancia ('The Liquidation of Government Debt', NBER, 2011). Source: National Bureau of Economic Research

2015: policy response

Monetary policy[1] → ← Fiscal policy[2]

	Lower interest rates	Sovereign QE	Credit QE	Equity purchases	Monetise debt[3]	Fiscal expansion in co-ordination with central bank	Fiscal expansion
	●	●					
	●	●	●				
	●	●		●			
	●	●	●				
	●						

1 Monetary policy is conducted largely through interest rates and quantitative easing (QE), purchases of assets to reduce yields
2 Fiscal stimulus involves increasing government spending and/or reducing taxes; the government's debt rises
3 Monetising debt is where a central bank creates money (quantitative easing) to buy government debt, without requiring the government to re-purchase that debt – this usually leads to inflation

Source: Ruffer LLP

2016-2017: policy response

Monetary policy[1] → ← Fiscal policy[2]

	Lower interest rates	Sovereign QE	Credit QE	Equity purchases	Monetise debt[3]	Fiscal expansion in co-ordination with central bank	Fiscal expansion
UK	●	●				●	●
US	●	●	●				●
Japan	●	●		●		●	●
EU	●	●	●				●
Canada	●					●	●

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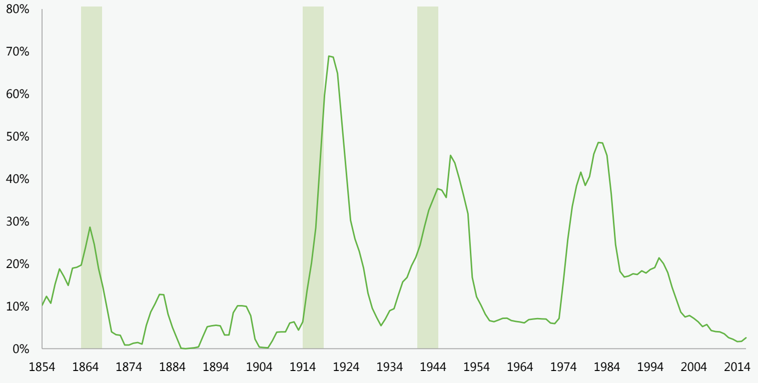
Source: Ruffer LLP

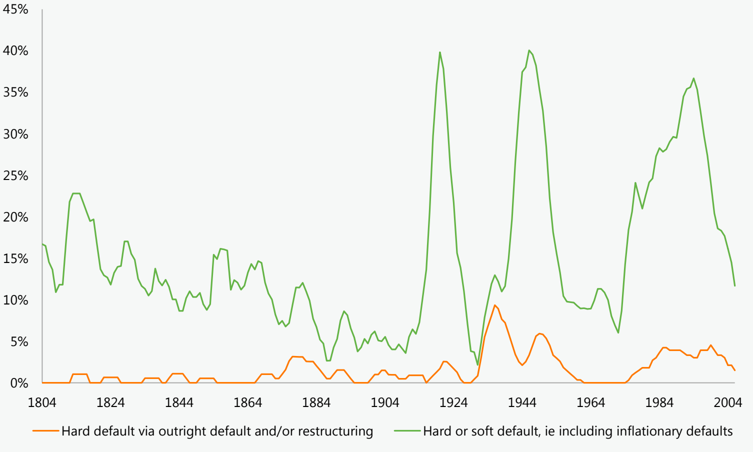
The shift into the inflationary regime could be rapid



Source: Reinhart & Rogoff data, 'inflation crisis' where three year moving average inflation rate >10%

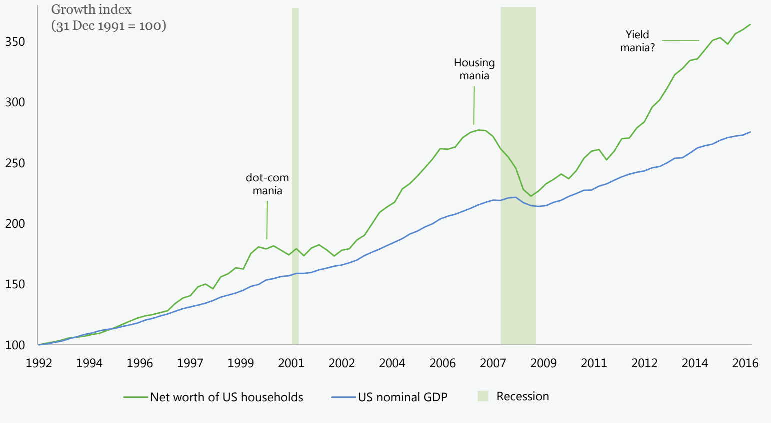
Governments use inflation to default on debt

% of countries defaulting on domestic sovereign debt



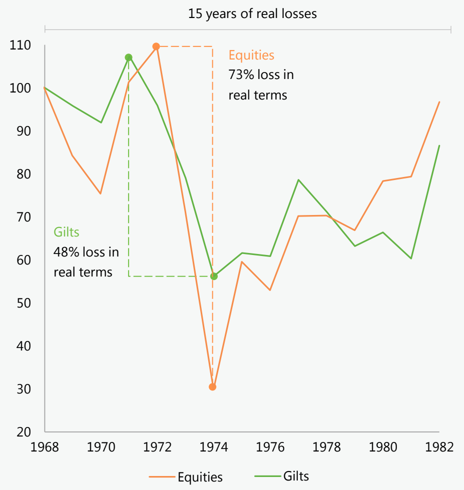
Source: Reinhart & Rogoff

Assets are outstripping the economy again



Net worth of US households (stocks, bonds, real-estate) against that of aggregate income (GDP). Source: TCA and Bloomberg

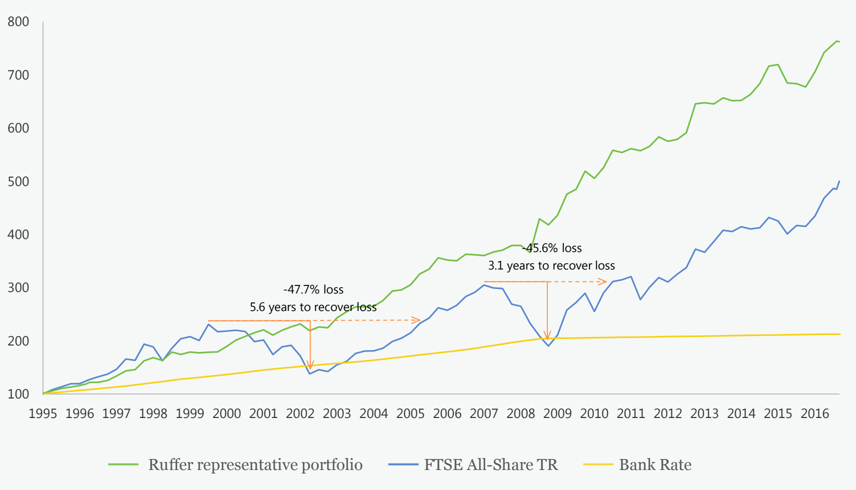
A precedent for the next crisis in markets?



Data illustrates returns on UK equities and gilts during the 1970s. This is not a forecast, but represents an example of how asset classes have performed in previous instances of high inflation in the UK market. Total returns of UK equities and gilts (adjusted for inflation) from 1968 to 1982. Source: Barclays equity gilt study 2016

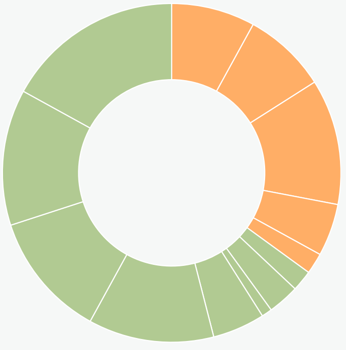
What are we trying to avoid?

Cumulative performance 1995 – 2017



Source: Thomson Datastream, Ruffer, FTSE International (FTSE)†. Cumulative performance 30 June 1995 to 31 January 2017, in pounds sterling. Performance data is included in the appendix. All figures include reinvested income. Ruffer's representative portfolio is an unconstrained segregated portfolio following Ruffer's investment approach. Ruffer performance is shown after deduction of all fees and management charges. Please note that past performance is not a reliable indicator of future performance. The value of the investments and the income from them can go down as well as up and you may not get back the full amount originally invested. The value of overseas investments will be influenced by the rate of exchange. Calendar quarter data has been used up to the latest quarter end and monthly data thereafter.

Portfolio structure



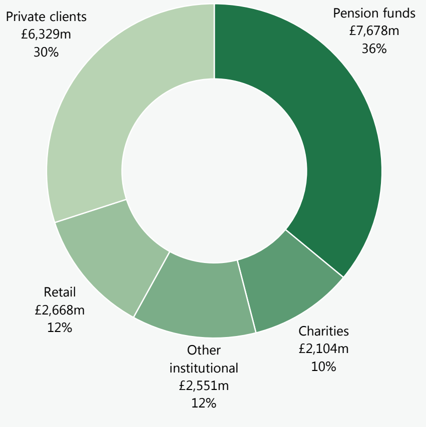
	%
Non-UK index-linked	17
Long-dated index-linked gilts	12
Index-linked gilts	12
Cash	13
Gold and gold equities	5
Options	1
Illiquid strategies	3

	%
Japan financials	8
Japan equities	8
UK equities	12
North America equities	5
Europe equities	2
Asia ex-Japan equities	2

Source: CF Ruffer Absolute Return Fund as at 28 February 2017

Current assets under management

February 2017, £21.3 billion



Source: Ruffer LLP

Independent firm with single investment strategy

Cash-plus returns with low volatility and low correlation to equity markets

Twenty-one year track record

Regulatory performance data

Percentage growth

From 31 Dec %	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
To 31 Dec %	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Ruffer	10.6	19.8	22.7	-0.2	16.8	5.5	3.0	16.8	11.3	14.1	8.4	2.1	16.0	13.0	15.1	1.3	4.6	11.1	4.2	-0.1	10.9
FTSE All-Share	16.7	23.6	13.8	24.2	-5.9	-13.3	-22.7	20.9	12.8	22.1	16.7	5.3	-29.9	30.1	14.5	-3.5	12.3	20.8	1.2	1.0	16.8
Bank Rate	6.1	6.5	7.5	5.6	6.0	5.5	4.1	3.8	4.4	4.8	4.7	5.6	5.0	0.8	0.5	0.5	0.5	0.5	0.5	0.5	0.4

Principal risk summary

Our investment approach is not suitable for the circumstances of all prospective clients.

Potential clients should consider an investment period of at least two years if they decide to appoint Ruffer.

We do lose money and have done so in 12 month rolling periods in the past. We will frequently lose money in shorter periods.

We take risk in portfolios and individual investments may carry significant risk.

We may misjudge investments and their relationship when held together so that the portfolio is riskier than anticipated and loses money.

Investment Managers follow Ruffer's asset allocation and have a degree of freedom in the stocks they select. This means that different clients have slightly different portfolios which may lead to variations in performance that are monitored.

We may invest in derivatives, usually options, intended to protect the portfolio against the risks we see. These can, and often do, lose all of their value.

Illiquid strategies investments are part of Ruffer's asset allocation but may take time to sell, so we will always communicate with you in advance to see if they are suitable.

Source

Thomson Datastream, Ruffer, FTSE International (FTSE)†. Ruffer performance is shown after deduction of all fees and management charges, and on the basis of income being reinvested.

Please note that past performance is not a reliable indicator of future performance. The value of the shares and the income from them can go down as well as up and you may not get back the full amount originally invested. The value of overseas investments will be influenced by the rate of exchange. Calendar quarter data has been used up to the latest quarter end.

Ruffer LLP is authorised and regulated by the Financial Conduct Authority.

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