State of Play

Time, patience and persistence

7 September 2023

Ever since the Global Financial Crisis, the consequences for savers and investors have been profound. Policymakers slashed interest rates to near zero and printed vast quantities of new money to support our financial way of life. However, in the last two years, with the return of inflation, this approach has been reversed in the blink of an eye, bringing interest rates closer to historic norms. However, does this mean investing for the longer term has become unattractive? Simon Durling, from Santander Asset Management, shares his thoughts in this week's State of Play.

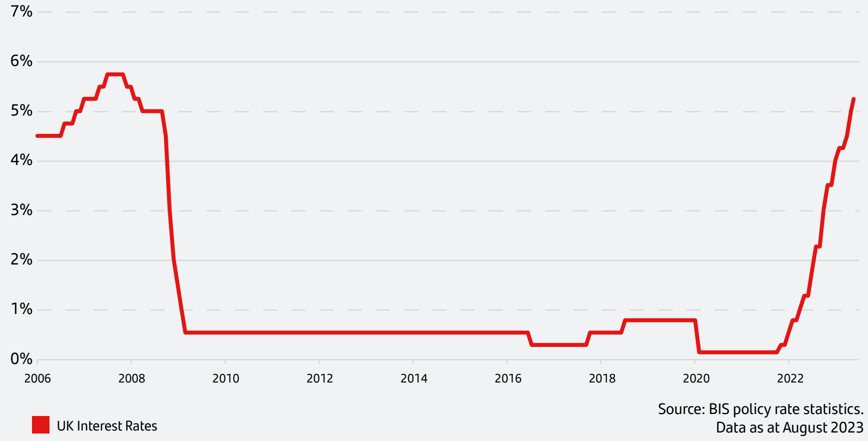
Key highlights from this week's State of Play

- Is cash now king?
- Why invest?
- Time in, not timing
- Time, patience and importantly persistence

Is cash now king?

This month, we are likely to see the Bank of England raise interest rates for the fifteenth (yes that is 15!) consecutive time since December 2021. If the Monetary Policy Committee raises rates by a further 0.25%, as anticipated, it will take the base rate to 5.5%, the highest since January 2008.[1] In their commitment to tackling rising prices, policymakers have normalised interest rates at a breath-taking speed. In many respects, the speed at which they responded to the financial crisis has been mirrored by how quickly things have changed some 15 years later.[1] This is the first such period of sustained 'financial tightening' (defined by less money in circulation and higher interest rates) we have seen since the Bank of England was appointed by Gordon Brown, the then Chancellor, in May 1997.[2]

Bank of England base rates since 2006



Source: BIS policy rate statistics.
Data as at August 2023

Last week, the Treasury-backed National Savings and Investments (NS&I) increased their savings rates by 1.2% on the 1-year guaranteed growth bond to 6.2%, the highest since the bonds were launched in 2008.[3] This places NS&I at the very top of the savings best buy tables at the time of writing for 1-year fixed rate savings.[4] Given that Santander now offers an easy access account paying 5.2%[5], many, especially those who have suffered from last year's historic fall in bond values, may be asking - is investing worth the risk? Let's step back and look in more detail at the balance between saving and investing and why investing still remains an important part of an overall long-term financial plan for many.

The importance of tax

Many savers may be delighted with the improvement in savings interest rates, but as I am sure we all know, how our savings or investments are taxed is a crucial element when considering what portion of your wealth is placed in a savings account and how much should be allocated for the long-term in an investment portfolio, assuming that is appropriate given your circumstances.

Clearly, ever since April 1999, savers and investors have had the advantage of their ISA allowance. The rules have evolved since their launch and now stand at £20,000 per person per tax year, whether this is in savings or investments. This allows savings interest to be tax-free in a cash ISA. If you invest in a Stocks and Shares ISA, it is tax-efficient but not tax-free. Anything outside of an ISA wrapper is subject to different taxation, depending on whether it is an investment or savings.

For savers, there is a personal savings allowance (PSA) which lets you earn interest on your savings without paying tax on that interest.[6] The allowance you get depends on what rate of income tax you pay and while it sounds simple, it is always worth checking how you are affected individually depending on your financial circumstances:

- **Basic-rate (20%) taxpayers:** can earn £1,000 in savings interest per year with no tax
- **Higher-rate (40%) taxpayers:** can earn £500 in savings interest per year with no tax
- **Additional-rate (45%) taxpayers:** £0 – they do not get an allowance.[6]

The reason I highlight tax is because some may see a headline rate advertised and take that as the return they will receive on their savings. So, as a simple example, if you have £10,000 in savings and see a one-year fixed-rate savings bond account offering 5%, depending on your tax position and income, you may not receive all the 5%. A higher-rate taxpayer only receives £60 for every £100 in interest being paid. So, in this specific example, the 5% rate after tax only pays 3%. However, it is important to remember that investments are also subject to tax. Depending on your tax position and income, you may not receive all of the positive performance reported after tax.

Asset Management

Why invest?

This State of Play weekly update has in previous editions spelled out the reasons why people choose to invest, primarily driven by a desire to achieve returns in excess of inflation by accessing the returns available from bonds, shares, property, and other alternative asset classes. Clearly, any investment, depending on what assets you choose, will vary in value and experience volatility where the value goes down as well as up, with no guarantees.

The power of diversification and long-term investing*

Year on year ranking of asset classes

Performance ranking	2015	2016	2017	2018	2019	2020	2021	2022	Q2 '23	YTD	10-year ann. return	Vol.
Highest	8.2% REITs	36.9% HY bonds	25.8% EM equities	5.8% Govt bonds	23.4% DM equities	15.0% EM equities	41.2% REITs	30.7% Cmdty	4.1% DM equities	9.2% DM equities	12.8% DM equities	18.8% Cmdty
	7.0% EMD	33.3% Cmdty	12.4% DM equities	2.7% HY bonds	23.1% REITs	12.9% DM equities	28.3% Cmdty	7.6% Hedge funds	0.8% Cash	1.2% Cash	10.1% REITs	18.5% REITs
	5.5% DM equities	33.1% EM equities	0.7% EMD	2.4% IG bonds	14.3% EM equities	7.0% IG bonds	23.5% DM equities	0.0% Cash	-0.6% EMD	-0.4% HY bonds	6.3% HY bonds	14.7% EM equities
	2.3% Govt bonds	31.4% EMD	0.6% HY bonds	1.9% REITs	10.6% EMD	6.1% Govt bonds	4.6% Hedge funds	-2.3% HY bonds	-1.2% HY bonds	-0.6% EM equities	4.9% EM equities	11.5% DM equities
	2.0% IG bonds	30.4% REITs	0.4% Cash	1.7% EMD	9.3% HY bonds	4.7% HY bonds	2.3% HY bonds	-6.2% IG bonds	-1.2% REITs	-1.5% EMD	4.9% Hedge funds	10.9% EMD
	1.9% Hedge funds	29.0% DM equities	-0.2% REITs	0.9% Cash	7.2% IG bonds	3.5% Hedge funds	0.1% Cash	-7.1% Govt bonds	-1.7% EM equities	-2.0% IG bonds	4.7% EMD	10.5% HY bonds
	1.4% HY bonds	24.4% IG bonds	-0.4% IG bonds	-0.9% Hedge funds	4.4% Hedge funds	2.0% EMD	-0.9% EMD	-7.4% DM equities	-2.3% Hedge funds	-2.4% REITs	3.9% IG bonds	8.1% IG bonds
	0.7% Cash	22.3% Hedge funds	-2.0% Govt bonds	-2.5% DM equities	3.5% Cmdty	0.6% Cash	-1.3% EM equities	-7.4% EMD	-2.7% IG bonds	-4.8% Govt bonds	1.9% Govt bonds	8.0% Govt bonds
	-9.7% EM equities	21.3% Govt bonds	-3.2% Hedge funds	-5.7% Cmdty	1.5% Govt bonds	-6.1% Cmdty	-2.0% IG bonds	-9.6% EM equities	-5.1% Govt bonds	-4.9% Hedge funds	1.7% Cmdty	6.5% Hedge funds
Lowest	-20.3% Cmdty	0.7% Cash	-7.1% Cmdty	-8.9% EM equities	1.0% Cash	-8.8% REITs	-5.7% Govt bonds	-15.7% REITs	-5.2% Cmdty	-12.8% Cmdty	0.5% Cash	0.3% Cash

Asset class returns can significantly change year on year, as seen in this multi-year asset class return table above. As an example, in 2017, Emerging Market shares returned 25.8%, the highest-performing asset class. In 2018, the following year, Emerging Market shares returned -8.9% and were the lowest-performing asset class. Being exposed to too much of any single asset class can add volatility to an investment portfolio. Incidentally, cash provided the lowest annualised return over the last 10 years, although this was during an extreme period where interest rates were kept at near zero by policymakers. The key lesson from this 'asset class blanket' is that investing in a well-diversified investment portfolio aligned to your risk comfort and time horizon can help reduce volatility and potentially increase your chances of achieving your long-term financial ambitions. Past performance is no guide to future performance. Investments can go down as well as up. You may not get back the amount you invested.

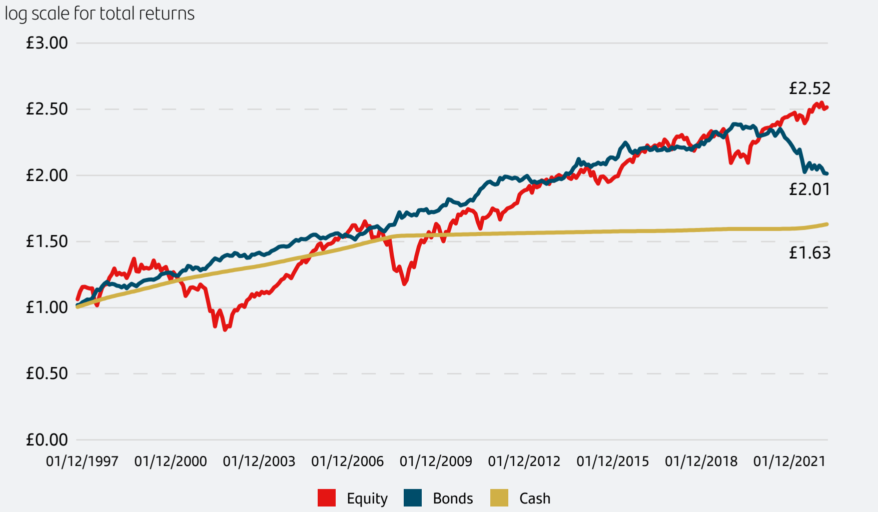
*Source: Bloomberg Barclays, FTSE, J.P. Morgan Economic Research, MSCI, Refinitiv Datastream, J.P. Morgan Asset Management. Annualised return and volatility covers the period from 2013 to 2022. Vol. is the standard deviation of annual returns. Govt bonds: Bloomberg Barclays Global Aggregate Government Treasuries; HY bonds: ICE BofA Global High Yield; EMD: J.P. Morgan EMBI Global Diversified; IG bonds: Bloomberg Barclays Global Aggregate – Corporates; Cmdty: Bloomberg Commodity; REITs: FTSE NAREIT All REITS; DM equities: MSCI World; EM equities: MSCI EM; Hedge funds: HFRI Global Hedge Fund Index; Cash: JP Morgan Cash United Kingdom (3M).

How have UK shares performed versus cash over the longer term?

The chart below shows the long-term returns for cash when compared to UK shares and UK bonds between 1998 and June 2023. These returns have been lowered to show the effects of inflation over the same time period. More recently, as I have highlighted earlier, cash has become more attractive with higher rates. However, rates are expected to reduce in the next few years as inflation returns back down to the central bank's target of 2%.[7] If the past is anything to go by, cash tends to offer much lower long-term returns when compared to investments, especially when you factor in both inflation and taxation impacts. Obviously, the caveats are that the past is no guide to future events, as the last few years have demonstrated graphically.

Total return of £1 in real terms

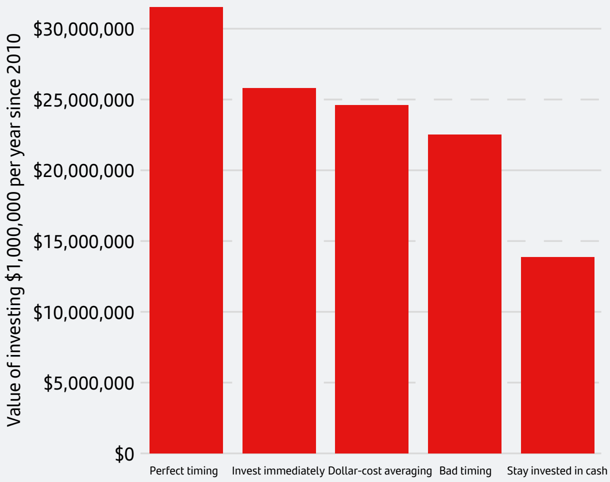
	Annualised Total Returns
	1998 - June 2023
Equities	5.11%
Bonds	3.81%
Cash	2.50%



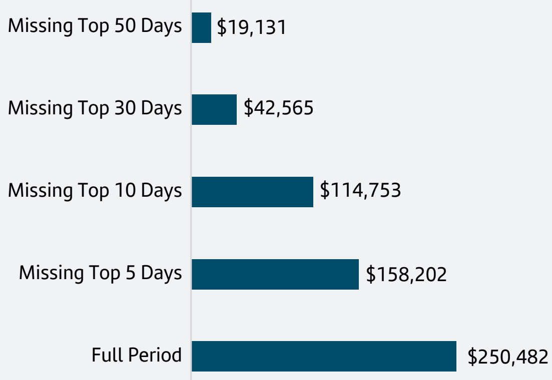
Source: Eikon. Equities: FTSE 100; Bonds: IBOXX £ GILTS; Cash: UK SONIA – Offered Rate (Excluding personal tax position).

Time in the market, not timing, matters most

One important lesson about investing is that it is about time in the markets rather than trying to 'time' when you invest. Many investors can become nervous as they approach the point at which they invest, hoping to pick the optimum moment. However, while timing your decision to invest can have a positive impact, it is almost impossible to get it right unless you have the benefit of hindsight. Delaying a decision to invest until you feel it is the right time can reduce your returns considerably, or worse still, staying in cash may be worse over the long-term. The chart on the left shows the outcome of investing since 2010, which, regardless of market and economic conditions, even if you picked a bad time, is much better than staying in cash. Importantly, investing immediately is not far below benefiting from luck and investing at the perfect time. The chart on the right shows the impact of missing the top 50 days in the S&P500 (US shares). Even if you miss just the top 5 days, the reduced returns compared to staying invested are significant.



Hypothical growth of $10,000 USD in S&P since January 1990 to June 2023



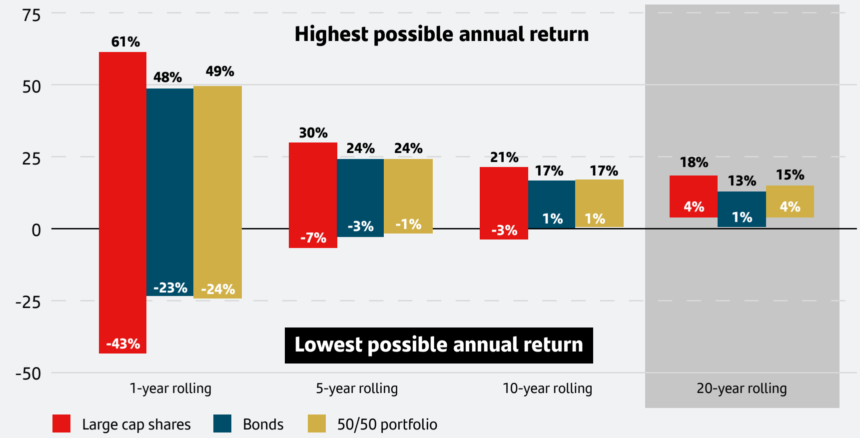
Source: Bloomberg, Barclays Private Bank, May 2023.

Investing is time, patience and importantly, persistence

Investing is almost always an emotional journey, especially for first-time investors who take advice and commit for the first time to a longer-term financial plan that includes investing. One of the key principles of investing, arguably for most people, is investing for an appropriate period of time. While history may not repeat itself, if you look back over very long time periods, the longer you are prepared to invest, the narrower your outcomes are likely to be and the less chance you have of losing either some or all of your capital. The chart below illustrates this very well.

Range of share and bond total returns

%, annualised total returns, 1950-present



The chart shows historical returns over various holding periods for US Equities, US Bonds and a 50/50 even split portfolio of the two.

The bars show the highest and lowest return that you could have received during each of the time periods.

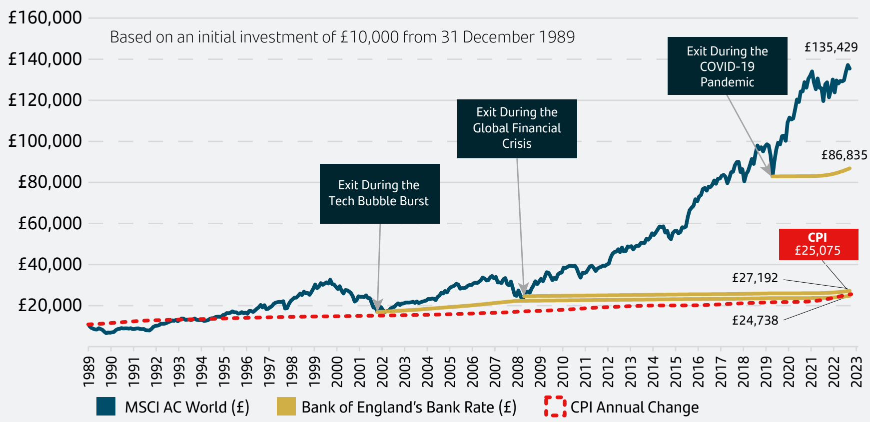
The benefit to investors of remaining invested over the longer term, regardless of whether an investor held US shares, US bonds or a balanced portfolio over the 20-year rolling period, all provided positive returns with lower volatility.

Source: Bloomberg Barclays, Refinitiv Datastream, S&P Global, Strategas/Ibbotson, J.P. Morgan Asset Management. Large cap equity represents the S&P 500 Composite and Bonds represents the Strategas/Ibbotson US Government Bond Index, the US Long-term Corporate Bond Index until 2000 and the Bloomberg Barclays US Agg. Corporate – Investment Grade Index from 2000 onwards. Returns shown are per annum and are calculated based on monthly returns from 1950 to latest available and include dividends. Past performance is not a reliable indicator of current and future results. Guide to the Markets - UK. Data as of 30 June 2023.

Past performance is not a guide to future performance. Investments can go down as well as up. You may not get back the amount you invested.

The strength of human emotions has been covered extensively in previous State of Play editions, which explored our natural human biases, which in many respects can hinder our decision-making when investment markets become very volatile or financial uncertainty dominates the headlines. If you look back over history and directly plot key events that triggered significant falls in investment market values and chart the returns of an investor who chose to sell their investments when compared to those who remained invested, it is, in my humble opinion, quite extraordinary. The chart below highlights the key events since 1989, based on an initial investment of £10,000, and shows the values as at, the end of last month (August 2023) comparing the values against each of these trigger points. The £10,000 of the investors who didn't sell is today worth £135,429.79, when compared to the investor who sold when the tech bubble burst in 2002 and went into cash, their savings are worth only £27,997.77. Even if you held your nerve and sold at the start of the global pandemic, just over three years ago, the difference between selling and remaining invested is around £50,000. The other important measure on the chart is inflation. As you can see, in order to keep pace with rising prices, your original £10,000 investment has to have grown to just above £25,000 to achieve any 'real' long-term growth.

£10,000 invested in the stock market in 31st December 1989



Source: Refinitiv Eikon, Datastream.
Data: MSCI AC WORLD, Bank of England's Bank Rate, as of the end of August 2023, in GBP.
Data: UK Consumer Price Index Annual Percentage Change as of the end of July 2023, in GBP.

Conclusions

At this point in the typical cycles of investing, with cash rates now offering competitive returns, at least in the short-term, savers and investors understandably might question the principle of investing. However, while the normalisation of interest rates has significantly improved the options available, depending on your specific personal financial circumstances, the reason why people may be motivated to invest has, in my opinion, hasn't changed. In previous editions, I have explained that any investment decision needs to be based on your financial ambitions, your time horizon and your risk comfort. Arguably, all financial plans over long time periods of over five years would typically incorporate a balance between savings and investments. At present, the proportion you may allocate to savings to capture the competitive rates available right now may be higher than, say, three years ago, but history shows that relying on cash rates to achieve our goals can prove to be foolish. It will be interesting to observe, if some believe that cash is indeed King at present, how long will the reign last?

The value of seeking guidance and advice

It is important to seek advice and guidance from a professional financial adviser who can help to explain how to build an appropriate financial plan to match your time horizons, financial ambitions, and risk comfort. If you already have a plan in place, or have already invested, it is important to allocate time to review this to ensure this remains on track and appropriate for your needs.

Learn more!

Investing can feel complex and overwhelming, but our educational insights can help you cut through the noise. Learn more about the Principles of Investing here.

Note: Data as at 7 September 2023.

[1] Bank of England, 9 August 2023
[2] The Guardian, 7 May 1997
[3] National Savings & Investments (NSI), 6 September 2023
[4] Money Saving Expert, 6 September 2023
[5] Santander, 6 September 2023
[6] Money Saving Expert, 9 May 2023
[7] Bank of England, 3 August 2023

Asset Management

A Week in the Markets

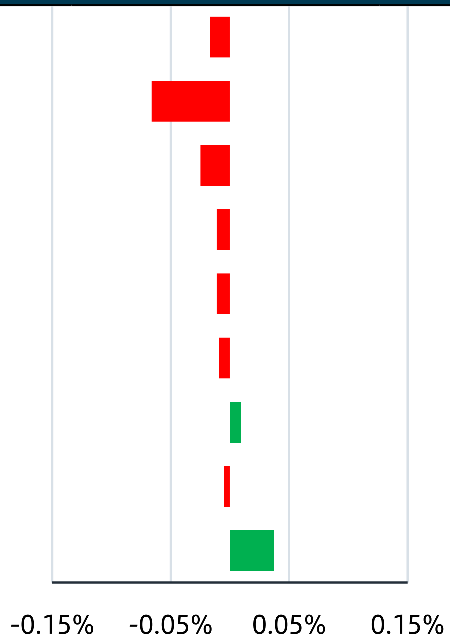
Performance

Index	Value	Change	%	12 Month High	12 Month Low
FTSE 100	7,465	**125.96**	**1.72%**	8,014	6,826
FTSE 250	18,537	**405.88**	**2.24%**	20,615	16,611
Dow Jones Industry	34,838	**490.81**	**1.43%**	35,631	28,726
S&P 500	4,516	**110.06**	**2.50%**	4,589	3,577
NASDAQ	15,491	**549.03**	**3.67%**	15,841	10,679
Hang Seng	18,382	**425.68**	**2.37%**	22,689	14,687
Nikkei 225	32,711	**1086.34**	**3.44%**	33,753	25,717
CAC 40	7,297	**67.17**	**0.93%**	7,577	5,677
DAX	15,840	**208.52**	**1.33%**	16,470	11,976
FTSE Eurofirst 300 Eurozone	2,398	**26.03**	**1.10%**	2,547	1,950
S&P TSX Composite Index	20,545	**709.61**	**3.58%**	20,767	18,206
Commodity markets*					
Gold	$1,939.25	**34.20**	**1.80%**	$2,047.01	$1,628.00
Crude Oil	$90.41	**4.65**	**5.42%**	$99.93	$70.96

Source: Refinitiv Eikon, prices displayed in the local currency.
*Gold Bullion London Bullion Market $ Per Metric Tonne Ounce Delay & Brent Forties and Oseberg Dated Free on Board Northsea Crude used for commodity performance.
Source Data from the 28 August 2023 to 1 September 2023.

10-year bond yields

Country		Variation	12 Month High	12 Month Low
UK	4.43%		4.75%	2.88%
US	4.17%		4.34%	3.19%
Japan	0.63%		0.68%	0.23%
Euro	2.55%		2.75%	1.52%
Germany	2.55%		2.75%	1.52%
France	3.07%		3.25%	2.15%
Italy	4.24%		4.82%	3.61%
Spain	3.57%		3.79%	2.73%
China	2.61%		2.99%	2.54%



Currencies

Currency	Conversion	Price	Change	12 Month High	12 Month Low
Dollar	GBP > USD	$1.26	0.00%	$1.31	$1.07
Euro	GBP > EUR	€ 1.17	0.00%	€ 1.17	€ 1.11
Yen	GBP > YEN	¥184.07	-0.08%	¥186.51	¥154.73

Source: Refinitiv Eikon.
Source Data from the 28 August 2023 to 1 September 2023.