Uncommon truths

Joining the dots: UK budget, banks, gold and AI

Though unpopular in the media, the recent UK budget seemed to calm financial markets. It also helped UK bank share price performance and may shed light on the popular themes of gold and AI.

The 26 November UK government budget was eagerly anticipated…in the UK. The post-budget decline in gilt yields and appreciation of sterling suggest the budget was well received by financial markets, though UK media reaction was less kind. In my opinion the budget was too piecemeal to be of great consequence and speaks to the constraints faced by Chancellor Reeves and the lack of vision of Keir Starmer's government. A full description of the budget can be found in *UK Budget: The waiting game is over* by Invesco's Graham Hook and Ben Jones.

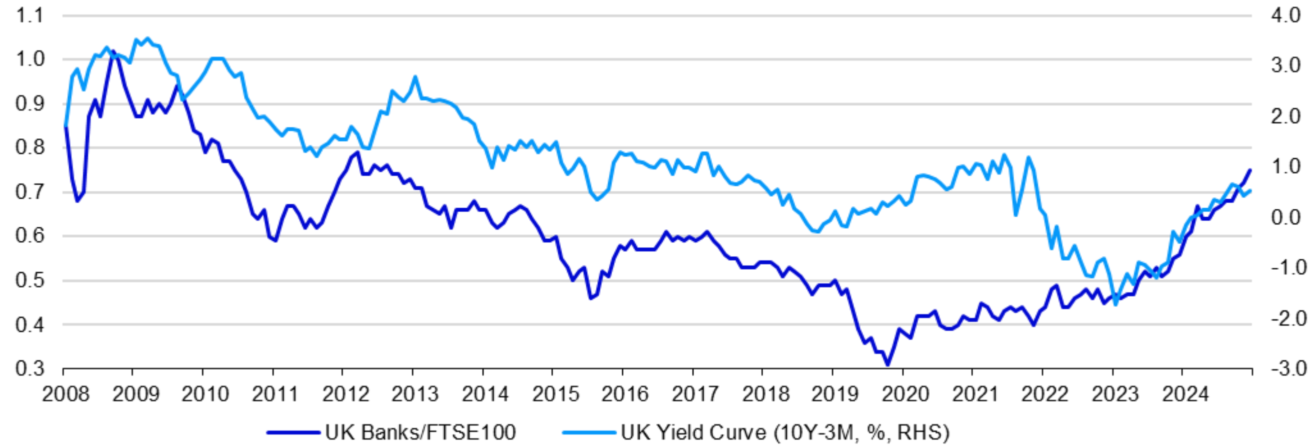
For macro-economic and financial market purposes the main take-aways are an extra £26bn in tax revenues by 2029-30 and an additional £11bn of spending by 2029-30 (mainly on welfare). The upshot will be a record 38% tax/GDP ratio in 2030-31 (according to the UK Office for Budget Responsibility, OBR) and an increase in the headroom versus the primary fiscal rule to £22bn (it was the latter that reassured financial markets, in my opinion).

Graham and Ben see little in the budget to change the dial on the UK economy and I agree. That probably explains the indifferent stock market reaction (the FTSE 100 is up 1.2% since the day before the budget, the same as for the S&P 500 and less than the 1.7% gain in the Euro Stoxx 50, as of 28 November 2025, according to Bloomberg data). Where the budget did seem to have a positive impact was in the gilt market, where 30-year yields have fallen by around 13 basis points since the day before the budget, versus gains of 1 basis point and 3 basis points in the US and Germany, respectively (based on data from LSEG Datastream). Even better, and despite the relative decline in UK yields, sterling strengthened a bit over those three days (by 0.5% versus USD and by 0.3% versus EUR, according to Bloomberg data). That strengthening of the pound could partly explain why UK stocks didn't seem to benefit.

Within the UK stock market, the actions not taken in the budget may have been more important than what did happen. In particular, the much feared windfall tax hike on banks didn't materialise, which helped the sector continue outperforming the overall market (see **Figure 1**). As shown in the chart, UK bank stocks have tended to outperform the broad UK market when the yield curve steepens, as has been the case since early 2023. If the budget encourages the Bank of England to cut interest rates (because it contained nothing particularly inflationary), then I would expect bank sector outperformance to continue (I expect 75 basis points of BOE easing by end-2026).

The UK government is receiving a lot of criticism about its lack of vision and ambition (from one side because of its "tax and spend" approach and lack of measures to boost the economy, and from the other because it is not spending enough on welfare etc.). In truth, I believe the government faces the unenviable task of trying to repair the fabric of the UK economy (infrastructure, healthcare, education etc.) while trying to keep government finances in reasonable order. Not only is the UK government's net debt-to-GDP ratio already around 100%, but it is also expected to roughly triple over the next 50 years (according to OBR projections) under the pressure of demographic and climate challenges (see **Figure 2**). That would take the UK government debt-to-GDP ratio above the 250% seen at the end of the second world war.

Figure 1 – UK banks tend to outperform when the yield curve steepens



Note: **Past performance is no guarantee of future results**. Based on monthly data from January 2008 to November 2025 (as of 28 November 2025). "UK Banks" is the FT All Share Banks index. "UK Yield Curve" is the 10-year UK gilt yield minus the UK treasury bill 3-month yield. Source: LSEG Datastream and Invesco Strategy & Insights

I suspect markets would judge that unsustainable, especially since Congressional Budget Office projections suggest US government debt is heading in the same direction (see **Figure 2**) and my own projections suggest other countries face the same dilemma (France, for example). This may explain why 30-year government yields have been trending upward this year. Unless governments get to grips with the problem (meaning less spending and/or more tax), I think the attraction of public sector debt may be diminished, perhaps meaning a long-term shift in strategic allocations toward private sector alternatives such as credit (both publicly quoted and private).

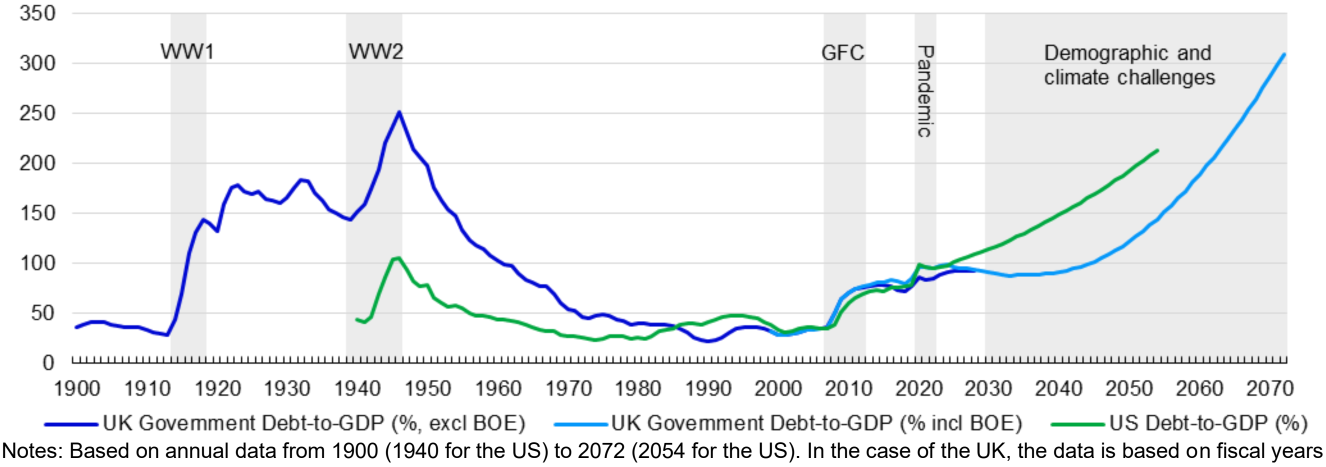
Concern about government debt may also help explain the strength of gold (the yellow metal is up 62% so far during 2025, based on Bloomberg data). Recent meetings in Europe and Asia suggest investors remain enthusiastic. However, they rarely mention government debt as a factor, focussing instead on central bank buying. That is interesting given that CBs bought 13% less gold in the first three quarters of this year than in the same period of 2024 (according to World Gold Council data). Likewise, jewellery demand has fallen 20%, while industrial demand is down around 1%. On the other hand, investment demand is up 87%, the big swing factor being ETFs, which have gone from outflows in the first three quarters of 2024 to sizeable inflows in 2025. It would appear that high prices are dampening all forms of demand except investment, which for the moment seems to be feeding on momentum.

Of course, governments would be helped by a growth boosting productivity miracle, which brings us to AI, another popular theme at recent meetings. For AI to turn into a productivity miracle, I believe we will need to see the benefits also accruing to adopters and not just enablers. A recent study by MIT (Massachusetts Institute of Technology) suggested that AI could already perform the work associated with 11.7% of US jobs (see *The Iceberg Index: Measuring Skills-centered Exposure in the AI Economy*, October 2025). That sounds promising but an earlier MIT report suggested that 95% of adopters have failed to extract a measurable P&L impact, due to poor implementation (see *The GenAI Divide: State of AI in Business 2025*, July 2025). I suspect we will see productivity gains from AI but not the decades long uplift to growth needed to help governments.

Despite investor enthusiasm, the global technology sector has lagged basic resources and banks so far this year (see **Figure 4**) and performance among AI enablers has been variable. With that in mind, it was interesting to listen to Google CEO, Sundar Pichai, in a lengthy BBC interview, in which he suggested there was some “irrationality” in the AI boom and that, when it came to a potential bursting of the bubble, “no company is going to be immune, including us”. Whether there is a bubble or not, I suspect that limitations on AI-enabler share price performance will come from competition, over investment, physical limitations on data centres (see the effect of data centre cooling issues on recent CME trading activity) and, ultimately, from the next “big thing”. Imagine how disruptive it would be if quantum computing advances, thus reducing the need for hardware and data centres.

Unless stated otherwise, all data as of 28 November 2025.

Figure 2 – Long-term UK and US government net debt-to-GDP ratios (1900-2072)



Notes: Based on annual data from 1900 (1940 for the US) to 2072 (2054 for the US). In the case of the UK, the data is based on fiscal years (April to April), with 1900-01 labelled as 1900, for example. UK data is provided by the UK’s Office for Budget Responsibility (OBR) and is taken from two reports (OBR Fiscal Risks and Sustainability July 2023 for the “excl. BOE” data prior to 1999 and OBR Economic and Fiscal Outlook March 2024 for the “excl. BOE” data from 1999 all the “incl. BOE” data). Note that the OBR has updated its forecasts since but has not provided the full set of data. In its Fiscal Risks and Sustainability Report July 2025 it suggested that debt-to-GDP would be above 270% in the early 2070s. US data is taken from the Congressional Budget Office, with the forecasts from 2025 on the basis that 2017 tax cuts will not be reversed. “GFC” is the global financial crisis.
Source: UK Office for Budget Responsibility, US Congressional Budget Office and Invesco Strategy & Insights

Figure 3 – Asset class total returns (%)

Data as at 28 Nov 2025	Index	Current Level/RY	Total Return (USD, %)					Total Return (Local Currency, %)				
			1w	1m	QTD	YTD	12m	1w	1m	QTD	YTD	12m
Equities												
World	MSCI	1005	3.6	-0.7	2.3	21.6	19.3	3.3	-0.4	2.9	19.3	17.9
Emerging Markets	MSCI	1367	2.5	-2.5	1.7	30.4	30.2	2.2	-1.5	3.0	28.7	30.0
China	MSCI	84	2.3	-4.6	-6.2	33.0	37.1	2.2	-4.4	-6.3	32.6	36.6
US	MSCI	6539	3.8	-0.6	2.4	17.7	15.4	3.8	-0.6	2.4	17.7	15.4
Europe	MSCI	2545	3.5	-0.1	2.3	31.1	28.8	2.5	0.4	3.5	18.3	18.3
Europe ex-UK	MSCI	3140	3.5	-0.4	2.0	31.4	29.4	2.6	0.3	3.2	17.0	17.4
UK	MSCI	1531	3.2	0.6	3.1	30.2	27.0	1.9	0.8	4.7	23.1	21.5
Japan	MSCI	4779	2.7	-0.1	2.7	24.4	24.7	2.3	2.4	8.5	23.5	28.4
Government Bonds												
World	BofA-ML	3.25	0.7	-0.8	-0.5	6.7	4.1	0.2	-0.3	0.8	2.9	1.8
Emerging Markets	JP Morgan	3.59	0.6	0.5	1.3	9.0	9.0	0.0	0.2	0.8	4.4	5.4
China	BofA-ML	1.65	0.2	0.3	1.1	3.5	5.0	-0.2	0.0	0.5	0.4	2.5
US (10y)	Datastream	4.00	0.4	0.2	1.8	8.9	6.6	0.4	0.2	1.8	8.9	6.6
Europe	Bofa-ML	2.81	1.2	-0.5	-0.4	13.5	10.1	0.3	-0.1	0.8	1.3	0.1
Europe ex-UK (EMU, 10y)	Datastream	2.65	1.0	-0.8	-0.7	12.0	7.9	0.1	-0.3	0.6	-0.1	-1.9
UK (10y)	Datastream	4.51	2.2	-0.1	1.4	11.8	8.4	0.9	0.1	3.0	5.7	3.7
Japan (10y)	Datastream	1.80	0.2	-3.7	-6.3	-3.5	-7.2	-0.1	-1.2	-1.0	-4.2	-4.4
IG Corporate Bonds												
Global	BofA-ML	4.31	0.8	-0.5	0.5	10.1	8.4	0.5	-0.3	0.9	6.5	5.5
Emerging Markets	BBloom	6.12	0.1	-0.2	0.4	7.6	6.9	0.1	-0.2	0.4	7.6	6.9
China	BofA-ML	2.23	0.4	0.5	1.2	4.4	5.3	-0.1	0.2	0.6	1.3	2.8
US	BofA-ML	4.80	0.6	-0.3	1.1	8.1	6.6	0.6	-0.3	1.1	8.1	6.6
Europe	BofA-ML	3.19	1.1	-0.7	-0.8	15.7	13.3	0.2	-0.3	0.4	3.2	3.0
UK	BofA-ML	5.19	2.1	-0.1	0.7	12.8	11.0	0.9	0.1	2.3	6.6	6.3
Japan	BofA-ML	1.72	0.3	-2.7	-5.4	-0.1	-3.6	-0.1	-0.2	0.0	-0.8	-0.8
HY Corporate Bonds												
Global	BofA-ML	6.90	0.8	-0.1	0.2	9.8	9.2	0.6	0.0	0.5	7.4	7.2
US	BofA-ML	7.13	0.7	0.1	0.7	7.8	7.4	0.7	0.1	0.7	7.8	7.4
Europe	BofA-ML	5.52	1.4	-0.4	-1.1	17.4	16.0	0.5	0.1	0.1	4.8	5.5
Cash (Overnight rates)												
US		3.91	0.1	0.4	0.6	3.9	4.4	0.1	0.4	0.6	3.9	4.4
Euro Area		1.93	-0.9	-0.6	-1.6	13.4	12.5	0.0	0.2	0.3	2.0	2.3
UK		3.97	-0.5	-1.7	-2.0	8.7	8.6	0.1	0.4	0.6	3.9	4.4
Japan		0.48	-1.2	-2.8	-5.4	0.9	-0.8	0.0	0.0	0.1	0.4	0.4
Real Estate (REITs)												
Global	FTSE	1728	2.2	0.2	0.5	12.2	4.5	1.3	0.7	1.8	0.1	-4.9
Emerging Markets	FTSE	1328	1.5	0.8	0.4	17.0	15.6	0.6	1.2	1.7	4.4	5.2
US	FTSE	3241	1.9	1.0	0.7	5.2	-3.1	1.9	1.0	0.7	5.2	-3.1
Europe ex-UK	FTSE	2703	2.6	-1.6	0.0	21.5	14.4	1.7	-1.1	1.3	8.4	4.1
UK	FTSE	901	5.2	-0.6	2.9	16.5	7.5	3.9	-0.4	4.6	10.1	2.9
Japan	FTSE	2609	2.7	4.3	2.6	39.5	36.0	2.4	7.0	8.4	38.5	40.0
Commodities												
All	GSCI	3928	1.7	1.1	1.3	7.4	10.8	-	-	-	-	-
Energy	GSCI	630	0.4	0.5	-0.9	-1.0	4.5	-	-	-	-	-
Industrial Metals	GSCI	1974	3.3	0.3	7.3	19.9	16.5	-	-	-	-	-
Precious Metals	GSCI	4718	4.3	7.4	10.7	61.5	60.2	-	-	-	-	-
Agricultural Goods	GSCI	490	1.9	1.4	3.6	-4.8	-1.9	-	-	-	-	-
Currencies (vs USD)*												
EUR		1.16	0.7	-0.5	-1.2	12.0	9.9	-	-	-	-	-
JPY		156.18	0.1	-2.6	-5.3	0.7	-3.0	-	-	-	-	-
GBP		1.33	1.3	-0.2	-1.6	5.8	4.5	-	-	-	-	-
CHF		1.24	0.6	-1.3	-0.9	12.9	9.9	-	-	-	-	-
CNY		7.08	0.5	0.3	0.6	3.2	2.4	-	-	-	-	-

Notes: **Past performance is no guarantee of future results.** *The currency section is organised so that in all cases the numbers show the movement in the mentioned currency versus USD (+ve indicates appreciation, -ve indicates depreciation). Please see appendix for definitions, methodology and disclaimers.
Source: LSEG Datastream and Invesco Strategy & Insights

Figure 4 – Global equity sector total returns relative to market (%)

Data as of 28 Nov 2025	Global				
	1w	1m	QTD	YTD	12m
Energy	**-2.9**	**1.9**	**1.5**	**-7.8**	**-9.0**
Basic Materials	**2.3**	**4.0**	**0.9**	**11.9**	**6.5**
Basic Resources	4.1	6.3	3.9	27.9	20.4
Chemicals	-1.2	-0.8	-4.9	-11.6	-14.4
Industrials	**-0.2**	**-1.6**	**-2.0**	**-1.7**	**-4.3**
Construction & Materials	1.5	0.9	0.5	2.9	-1.2
Industrial Goods & Services	-0.4	-2.0	-2.4	-2.4	-4.7
Consumer Discretionary	**0.7**	**-0.8**	**-2.8**	**-8.1**	**-5.1**
Automobiles & Parts	2.4	-2.7	-2.6	-7.5	4.6
Media	-1.2	-2.7	-10.0	-7.7	-7.8
Retailers	1.0	0.8	-0.8	-7.3	-5.5
Travel & Leisure	-0.2	1.0	-3.6	-13.5	-14.3
Consumer Products & Services	-0.3	-2.3	-3.4	-6.7	-5.2
Consumer Staples	**-2.3**	**1.7**	**0.1**	**-6.7**	**-9.4**
Food, Beverage & Tobacco	-2.1	2.0	0.5	-5.9	-7.9
Personal Care, Drug & Grocery Stores	-2.6	1.3	-0.7	-8.0	-11.8
Healthcare	**-1.1**	**7.5**	**8.3**	**-3.7**	**-6.9**
Financials	**-0.3**	**2.2**	**-0.8**	**3.9**	**2.6**
Banks	-0.3	2.9	1.0	12.0	12.4
Financial Services	0.4	0.7	-2.7	-4.2	-6.7
Insurance	-1.5	3.1	-2.1	-1.4	-4.0
Real Estate	**-0.9**	**0.5**	**-1.7**	**-5.7**	**-9.6**
Technology	**1.4**	**-3.1**	**0.5**	**6.0**	**10.5**
Telecommunications	**-1.3**	**-3.7**	**-2.9**	**3.4**	**2.5**
Utilities	**-1.2**	**1.6**	**1.7**	**1.3**	**-1.1**

Notes: **Past performance is no guarantee of future results.** Returns shown are for Datastream sector indices versus the total market index. Source: LSEG Datastream and Invesco Strategy & Insights

Figure 5a – US factor index total returns (%)

Data as of 28 Nov 2025	Absolute					Relative to Market				
	1w	1m	QTD	YTD	12m	1w	1m	QTD	YTD	12m
Growth	3.4	-0.7	4.6	10.8	4.1	-0.3	-0.2	-5.7	-5.9	-10.0
Low volatility	1.5	1.1	1.3	4.3	-1.9	-2.1	1.6	-8.6	-11.5	-15.2
Price momentum	5.6	-0.2	8.2	15.3	8.4	1.7	0.3	-2.5	-2.2	-6.3
Quality	3.1	1.5	9.6	16.3	8.4	-0.6	2.0	-1.2	-1.3	-6.3
Size	2.8	0.8	6.7	8.0	1.9	-0.9	1.3	-3.9	-8.3	-11.9
Value	3.4	3.0	10.9	17.7	9.4	-0.3	3.5	-0.1	-0.1	-5.4
Market	3.7	-0.5	10.9	17.8	15.7					
Market - Equal-Weighted	3.1	0.6	5.8	10.9	4.3					

Notes: **Past performance is no guarantee of future results.** All indices are subsets of the S&P 500 index, they are rebalanced monthly, use data in US dollars and are equal-weighted. Growth includes stocks in the top third based on both their 5-year sales per share trend and their internal growth rate (the product of the 5-year average return on equity and the retention ratio); Low volatility includes stocks in the bottom quintile based on the standard deviation of their daily returns in the previous three months; Price momentum includes stocks in the top quintile based on their performance in the previous 12 months; Quality includes stocks in the top third based on both their return on invested capital and their EBIT to EV ratio (earnings before interest and taxes to enterprise value); Size includes stocks in the bottom quintile based on their market value in US dollars. Value includes stocks in the bottom quintile based on their price to book value ratios. The market represents the S&P 500 index. Source: LSEG Datastream and Invesco Strategy & Insights

Figure 5b – European factor index total returns relative to market (%)

Data as of 28 Nov 2025	Absolute					Relative to Market				
	1w	1m	QTD	YTD	12m	1w	1m	QTD	YTD	12m
Growth	3.0	-1.4	1.7	8.7	10.5	0.4	-1.7	-5.1	-7.3	-5.9
Low volatility	2.1	0.4	1.7	14.1	13.0	-0.5	0.1	-5.1	-2.7	-3.7
Price momentum	4.5	1.7	10.4	32.5	32.8	1.8	1.4	2.9	12.9	13.1
Quality	3.1	0.1	7.5	21.6	21.7	0.5	-0.2	0.2	3.7	3.6
Size	4.2	-1.4	-0.3	10.1	10.2	1.6	-1.7	-7.0	-6.1	-6.2
Value	3.7	1.2	8.6	29.3	30.5	1.1	0.9	1.3	10.3	11.2
Market	2.6	0.3	7.2	17.3	17.4					
Market - Equal-Weighted	3.1	-0.7	4.4	16.1	16.1					

Notes: **Past performance is no guarantee of future results.** All indices are subsets of the STOXX 600 index, they are rebalanced monthly, use data in euros and are equal-weighted. Growth includes stocks in the top third based on both their 5-year sales per share trend and their internal growth rate (the product of the 5-year average return on equity and the retention ratio); Low volatility includes stocks in the bottom quintile based on the standard deviation of their daily returns in the previous three months; Price momentum includes stocks in the top quintile based on their performance in the previous 12 months; Quality includes stocks in the top third based on both their return on invested capital and their EBIT to EV ratio (earnings before interest and taxes to enterprise value); Size includes stocks in the bottom quintile based on their market value in euros; Value includes stocks in the bottom quintile based on their price to book value ratios. The market represents the STOXX 600 index. Source: LSEG Datastream and Invesco Strategy & Insights

Figure 6 – Model asset allocation

	Neutral	Policy Range		Allocation	Position vs Neutral	Hedged	Currency
Cash Equivalents	**5%**	**0-10%**	↑	**4%**			
Cash	3%		↓	0%			
AAA CLOs	2%		↑	4%			
Bank Loans	**4%**	**0-8%**		**8%**			
US	3%			6%			
Europe	1%			2%			
Bonds	**40%**	**10-70%**	↓	**36%**			
Government	25%	10-40%	↓	22%			
US	8%		↓	7%		50%	JPY
Europe ex-UK (Eurozone)	7%		↓	6%			
UK	1%			2%			
Japan	7%		↓	3%			
Emerging Markets	2%			4%			
China**	0.2%			0%			
Corporate IG	10%	0-20%	↓	9%			
US Dollar	5%		↓	4%		50%	JPY
Euro	2%			1%			
Sterling	1%			2%			
Japanese Yen	1%			0%			
Emerging Markets	1%			2%			
China**	0.1%			0%			
Corporate HY	5%	0-10%	↑	5%			
US Dollar	4%		↑	4%		50%	JPY
Euro	1%			1%			
Equities	**45%**	**25-65%**		**42%**			
US	25%			10%			
Europe ex-UK	7%		↓	10%			
UK	4%			6%			
Japan	4%		↑	7%			
Emerging Markets	5%			9%			
China**	2%			4%			
Real Estate	**4%**	**0-8%**		**6%**			
US	1%		↓	0%			
Europe ex-UK	1%			2%			
UK	1%			2%			
Japan	1%		↑	2%			
Emerging Markets	1%			0%			
Commodities	**2%**	**0-4%**		**4%**			
Energy	1%			2%			
Industrial Metals	0.3%			1%			
Precious Metals	0.3%			0%			
Agriculture	0.3%			1%			
Total	**100%**			**100%**			

Currency Exposure (including effect of hedging)					
USD	51%		↑	30%	
EUR	20%		↓	24%	
GBP	7%		↓	12%	
JPY	14%		↑	20%	
EM	9%			15%	
Total	**100%**			**100%**	

Notes: **China is included in Emerging Markets allocations. This is a theoretical portfolio and is for illustrative purposes only. See the latest The Big Picture document for more details. It does not represent an actual portfolio and is not a recommendation of any investment or trading strategy. Arrows indicate the direction of the most recent changes.
Source: Invesco Strategy & Insights

Figure 7 – Model allocations for global sectors

	Neutral	Invesco		Preferred Region
Energy	**5.3%**	**Overweight**		**US**
Basic Materials	**3.6%**	**Neutral**		**Europe**
Basic Resources	2.4%	Underweight	↓	Europe
Chemicals	1.2%	Overweight		US
Industrials	**13.0%**	**Neutral**		**US**
Construction & Materials	1.7%	Neutral		Europe
Industrial Goods & Services	11.3%	Neutral		US
Consumer Discretionary	**14.1%**	**Underweight**		**Europe**
Automobiles & Parts	2.7%	Underweight		Europe
Media	1.2%	Underweight		Europe
Retailers	5.4%	Neutral		US
Travel & Leisure	1.8%	Overweight	↑	EM
Consumer Products & Services	3.0%	Underweight		Europe
Consumer Staples	**4.5%**	**Neutral**		**US**
Food, Beverage & Tobacco	2.8%	Neutral		US
Personal Care, Drug & Grocery Stores	1.7%	Overweight		Europe
Healthcare	**7.5%**	**Overweight**		**US**
Financials	**16.4%**	**Neutral**		**US**
Banks	8.0%	Overweight		US
Financial Services	5.4%	Neutral	↑	Japan
Insurance	3.0%	Neutral		US
Real Estate	**2.6%**	**Overweight**		**Japan**
Technology	**26.3%**	**Underweight**	↓	**US**
Telecommunications	**3.5%**	**Underweight**		**US**
Utilities	**3.2%**	**Neutral**	↓	**Europe**

Notes: These are theoretical allocations which are for illustrative purposes only. They do not represent an actual portfolio and are not a recommendation of any investment or trading strategy. See the latest Strategic Sector Selector for more details.
Source: LSEG Datastream and Invesco Strategy & Insights

Appendix

Methodology for asset allocation and expected returns

Which asset classes?

We look for investibility, size and liquidity. We have chosen to include equities, bonds (government, corporate investment grade and corporate high yield), bank loans, REITs to represent real estate, commodities and cash (all across a range of geographies). We use cross-asset correlations to determine which decisions are the most important.

Neutral allocations and policy ranges

We use market capitalisation in USD for major benchmark indices to calculate neutral allocations. For commodities, we use industry estimates for total ETP market cap + assets under management in hedge funds + direct investments. We use an arbitrary 5% for the combination of cash and gold. We impose diversification by using policy ranges for each asset category (the range is usually symmetric around neutral).

Expected/projected returns

The process for estimating expected returns is based upon yield (except commodities, of course). After analysing how yields vary with the economic cycle, and where they are situated within historical ranges, we forecast the direction and amplitude of moves over the next year. Cash returns are calculated assuming a straight-line move in short term rates towards our targets (with, of course, no capital gain or loss). Bond returns assume a straight-line progression in yields, with capital gains/losses predicated upon constant maturity (effectively supposing constant turnover to achieve that). Forecasts of corporate investment-grade, high-yield and bank loan spreads are based upon our view of the economic cycle (as are forecasts of credit losses). Coupon/interest payments are added to give total returns. Equity and REIT returns are based on dividend growth assumptions. We calculate total returns by applying those growth assumptions and adding the forecast dividend yield. No such metrics exist for commodities; therefore, we base our projections on US CPI-adjusted real prices relative to their long-term averages and views on the economic cycle. All expected returns are calculated in local currency and then, where necessary, converted into other currency bases using our exchange rate forecasts.

Currency hedging

We adopt a cautious approach when it comes to currency hedging as currency movements are notoriously difficult to accurately predict and sometimes hedging can be costly. Also, some of our asset allocation choices are based on currency forecasts. We use an amalgam of central bank rate forecasts, policy expectations and real exchange rates relative to their historical averages to predict the direction and amplitude of currency moves.

Definitions of data and benchmarks for Figure 3

Sources: we source data from LSEG Datastream unless otherwise indicated.

Cash: returns are based on a proprietary index calculated using the Intercontinental Exchange Benchmark Administration overnight LIBOR (London Interbank Offer Rate). From 1st January 2022, we use the euro short term rate, the UK Sterling Overnight Index Average (SONIA), the US Secured Overnight Financing Rate (SOFR) and the uncollateralised overnight rate for the Japanese yen. The global rate is the average of the euro, British pound, US dollar and Japanese yen rates. The series started on 1 January 2001 with a value of 100.

Gold: London bullion market spot price in USD/troy ounce.

Government bonds: Current levels, yields and total returns use Datastream benchmark 10-year yields for the US, Eurozone, Japan and the UK, and the ICE BofA government bond total return index for the World and Europe. The emerging markets yields and returns are based on the JP Morgan Emerging Markets Global Composite Index.

Corporate investment grade (IG) bonds: ICE BofA investment grade corporate bond total return indices, except for in emerging markets where we use the Bloomberg emerging markets corporate US dollar bond index.

Corporate high yield (HY) bonds: ICE BofA high yield total return indices

Equities: We use MSCI benchmark gross total return indices for all regions.

Commodities: Goldman Sachs Commodity total return indices

Real estate: FTSE EPRA/NAREIT total return indices

Currencies: Global Trade Information Services spot rates

Investment risks

The value of investments and any income will fluctuate (this may partly be the result of exchange rate fluctuations) and investors may not get back the full amount invested.

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