



# Volcker's Ghost

A meander through the current macroeconomic environment and the outlook for investment

AIC Investment Company Showcase  
October 2022



# Disclaimer

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This presentation was prepared on 21<sup>st</sup> October 2022, and fund performance data is updated to 31<sup>st</sup> September 2022. Other market data may be less up to date, nevertheless the managers consider such data to be representative of prevailing market conditions.

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# Where are we?

*Reflections on the current macroeconomic outlook*

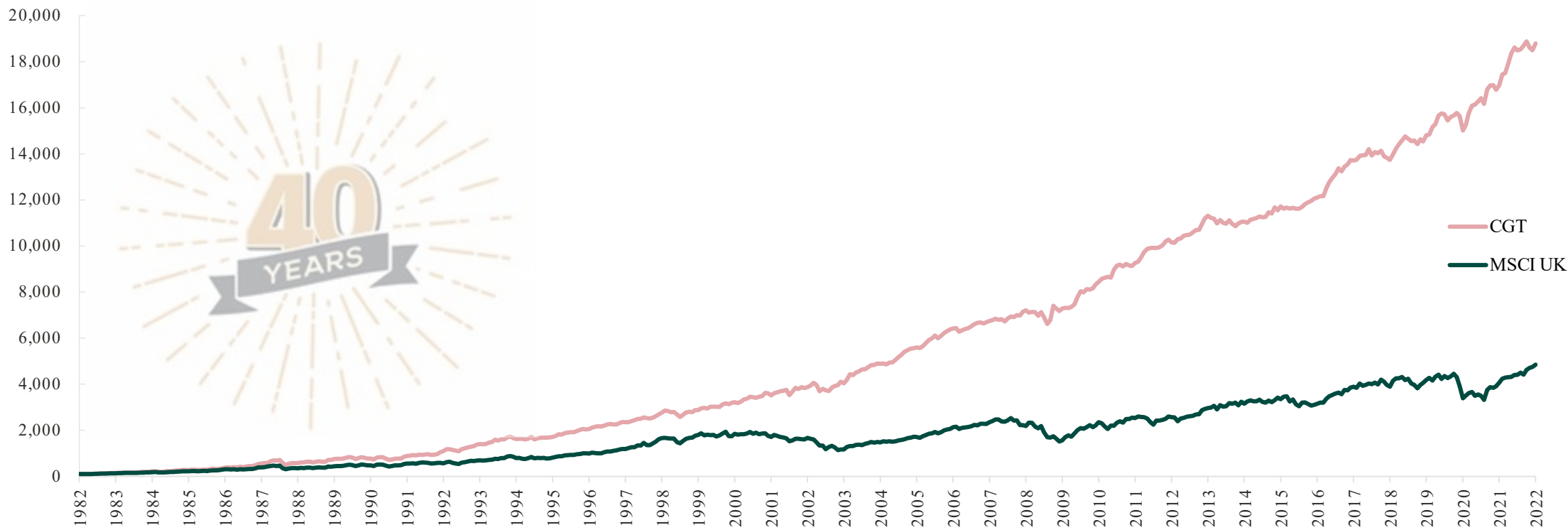
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CGAM BACKGROUND

Since 1982 CGT has returned 280x<sup>1)</sup> with only one down year

NAV Total Return History (Rebased) Apr 1982 to Apr 2022

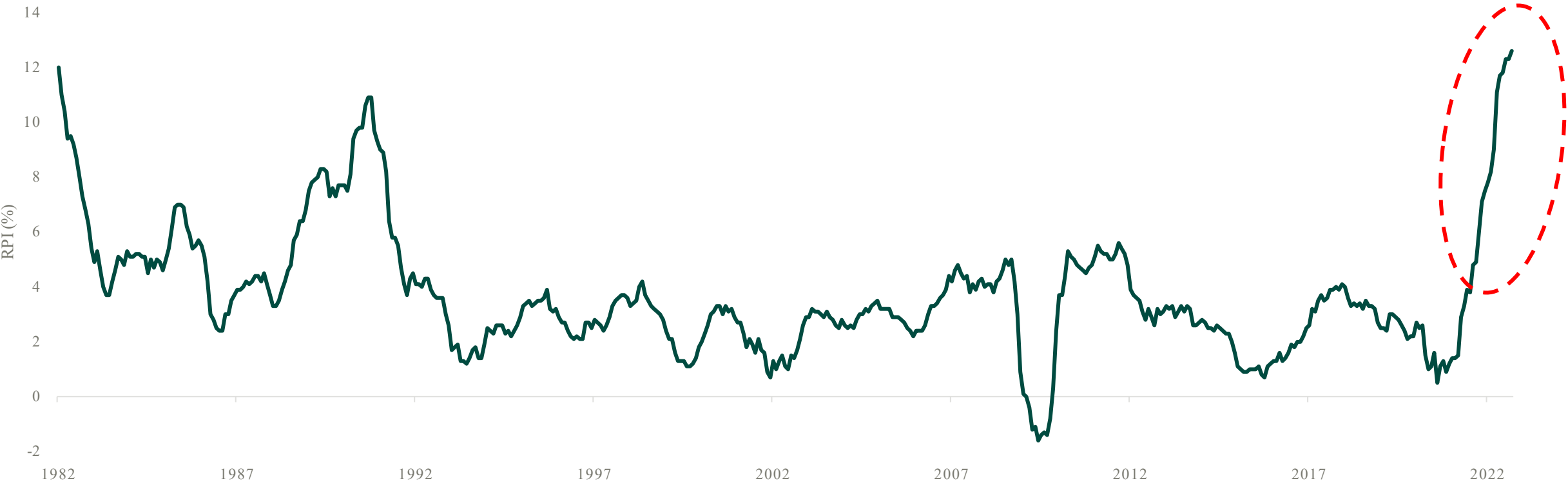


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MACROECONOMIC OUTLOOK

# UK inflation is now at 40-year highs

UK Retail Price Index, year-on-year change



## MACROECONOMIC OUTLOOK

Inflation and interest rates have been low for the past 30 years, but we believe that we are now in a new regime, which looks closer to the 1960s

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### *Old regime*

- *Demographics* X
- *Globalisation* X
- *Technology* ?

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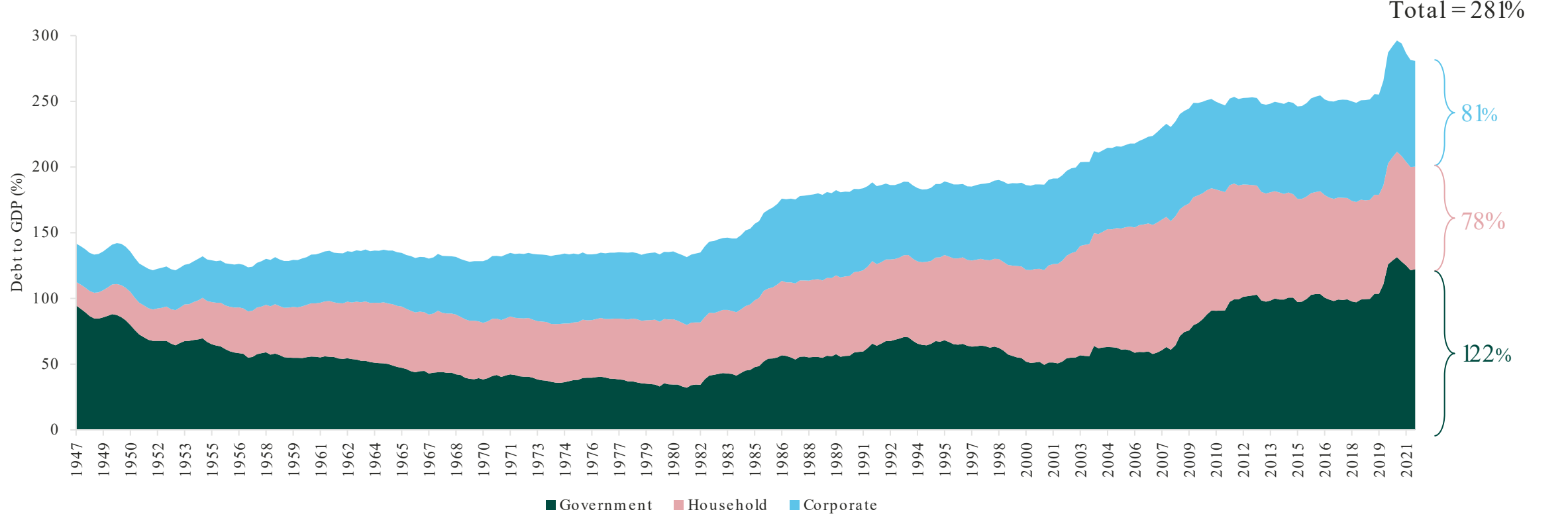
### *New regime*

- *Green inflation* ✓
- *Structural change* ✓
- *Pricking asset bubble* ?

MACROECONOMIC OUTLOOK

The *entire financial system* is characterised by high levels of indebtedness – there is never only one cockroach in the kitchen!

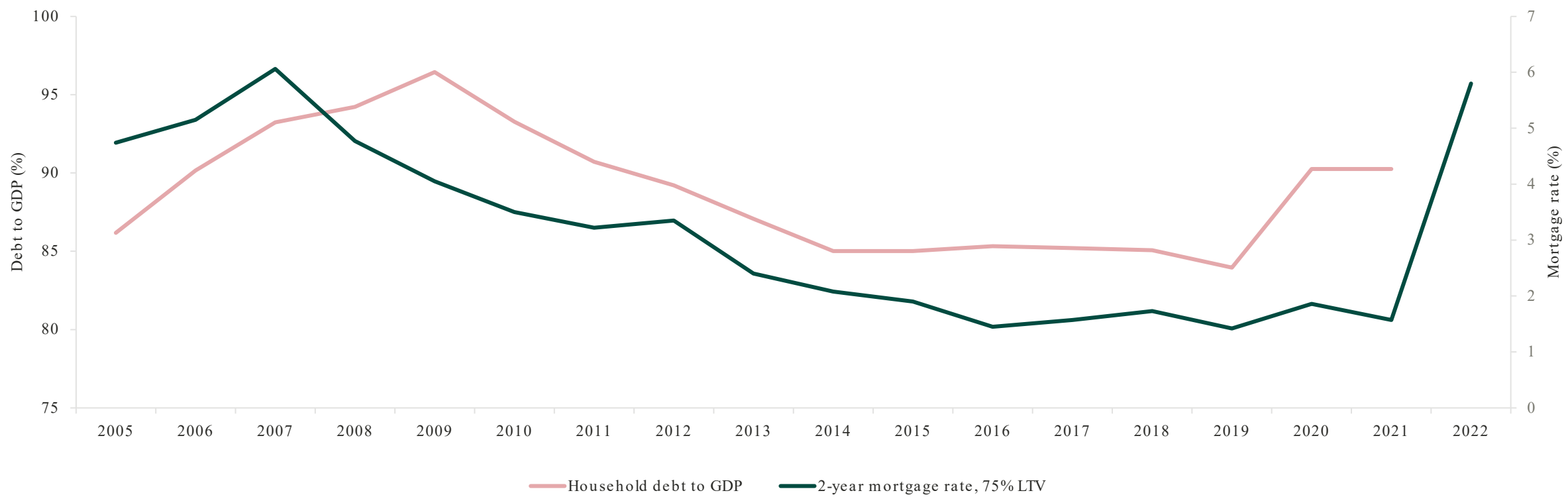
US Non-Financial Debt to GDP



MACROECONOMIC OUTLOOK

The last time household debt and mortgage rates were this elevated was the eve of the global financial crisis

UK household debt to GDP versus 2-year fixed mortgage rate

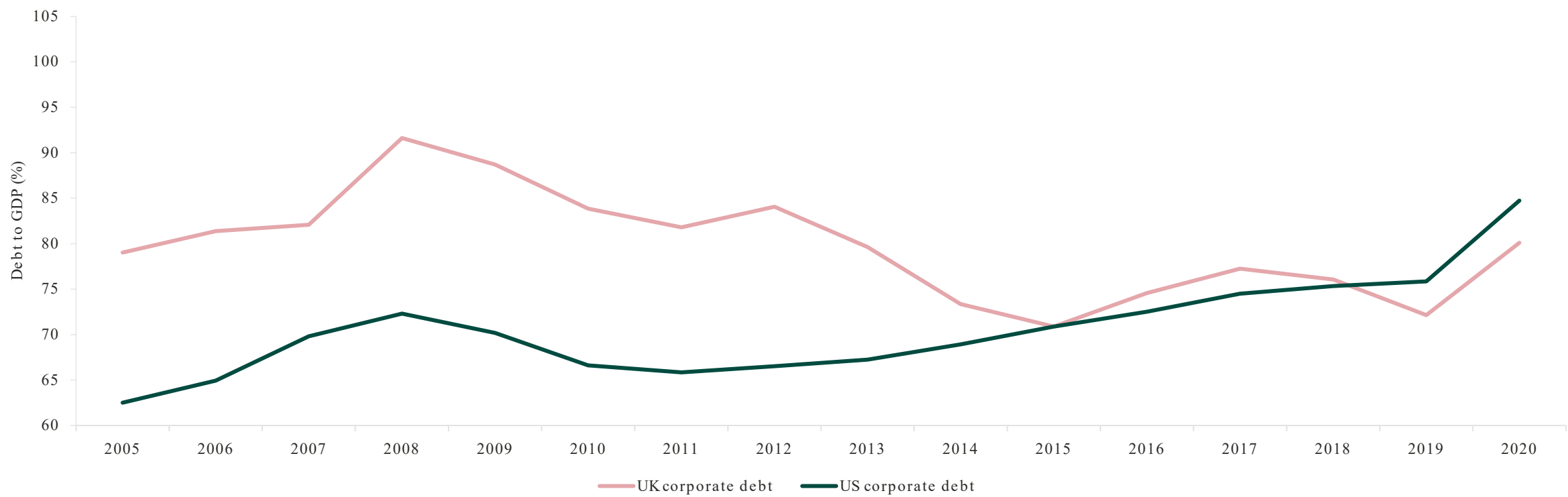




MACROECONOMIC OUTLOOK

Corporates have also come out of the pandemic with elevated debt levels

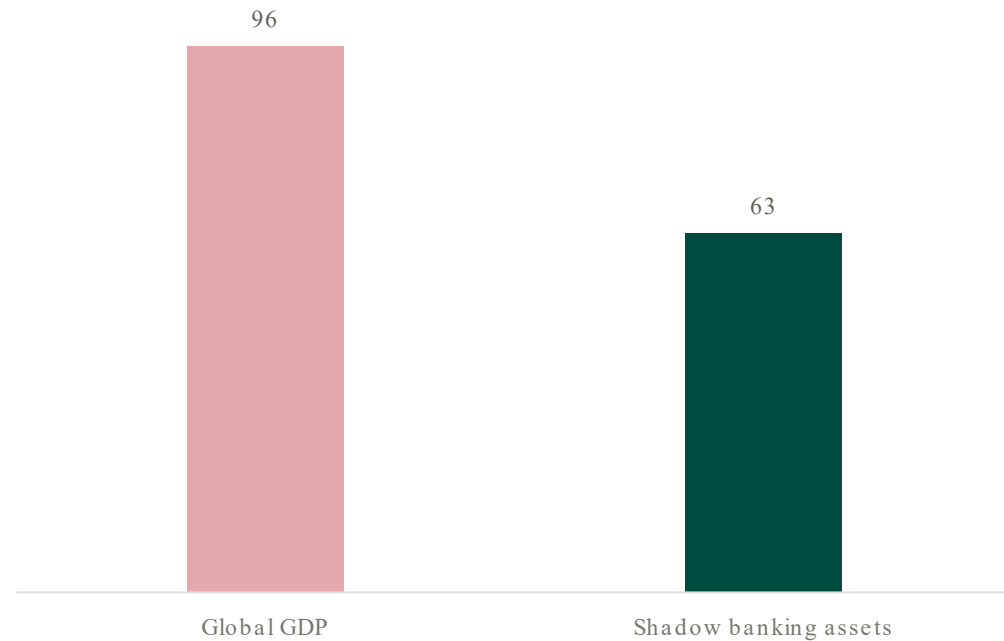
US and UK corporate debt to GDP



## MACROECONOMIC OUTLOOK

# Persistent easy monetary policy has led to extraordinary leverage within the global financial system

Value of global shadow banking assets relative to global GDP (USD trillions)



*Shadow banks manage more than \$63 trillion in assets, a **number that has doubled** across the past decade, and which represents approximately two thirds of global GDP.*

# Where to from here?

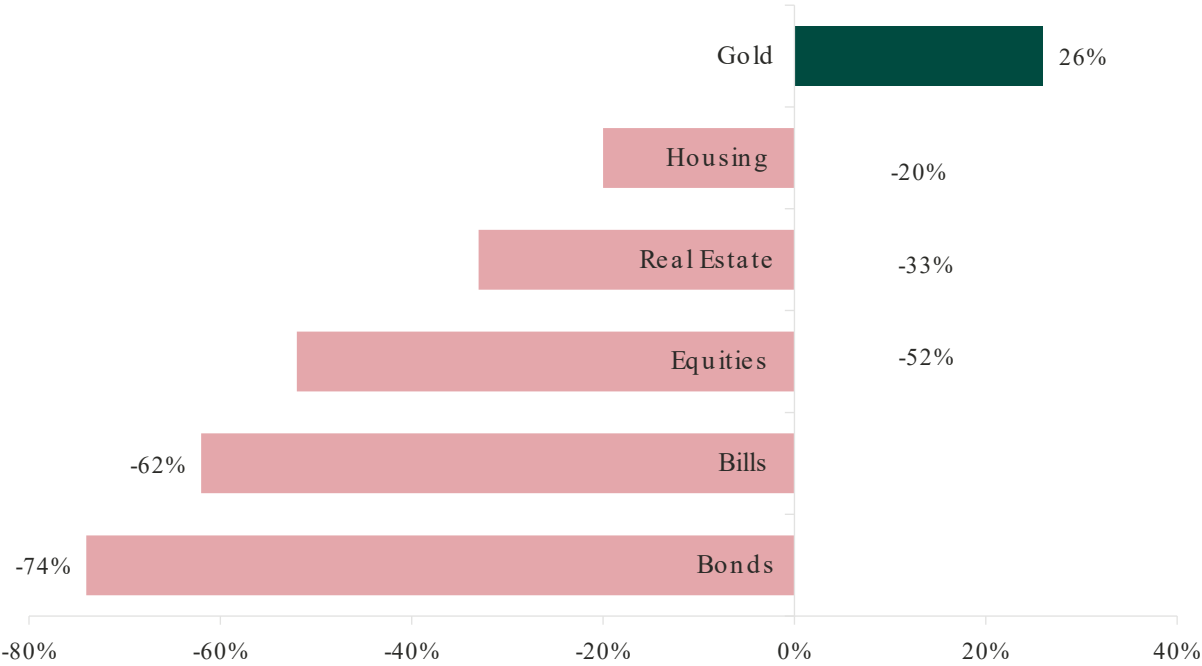
*Reflections on how investors might respond  
to the current environment*

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INVESTING ENVIRONMENT

Very few asset classes have consistently performed well during rising inflation

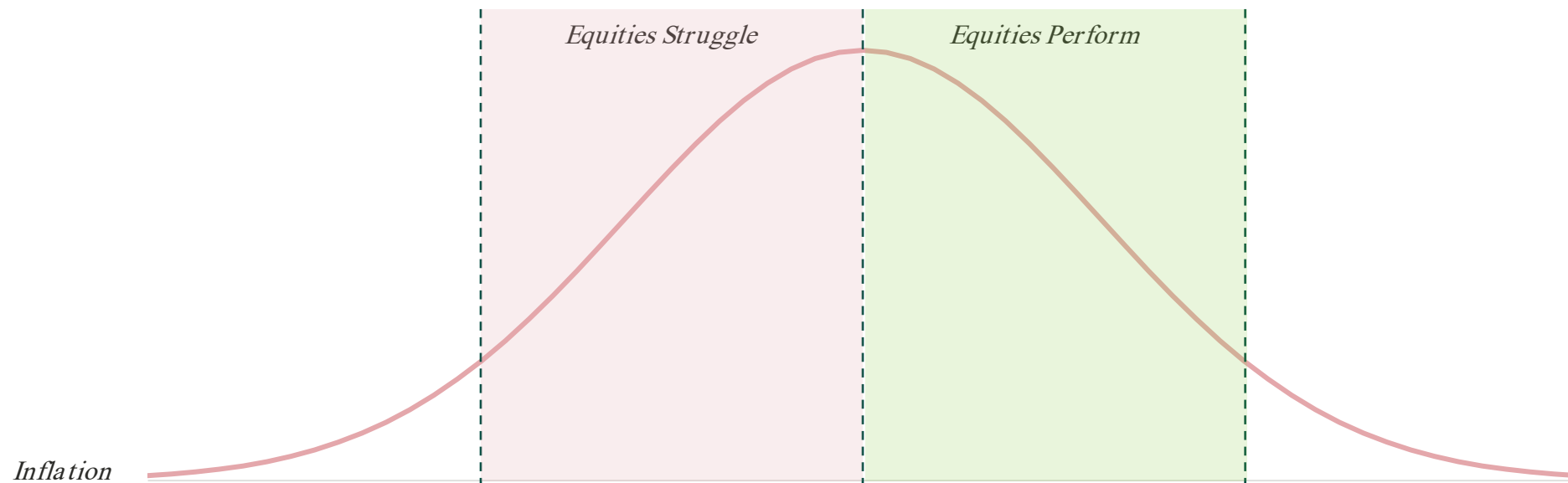
Real Return vs. Inflation 1900-2011



Regression of annual real return vs. same year inflation across 19 developed countries

## INVESTING ENVIRONMENT

# Equities actually love disinflation



“For a variety of reasons reviewed here, inflation tends to raise investors’ required real rate of return on equity and to lower real capital income for tax-related reasons. **As a result there is a strong negative correlation between inflation and real and nominal stock prices.**”

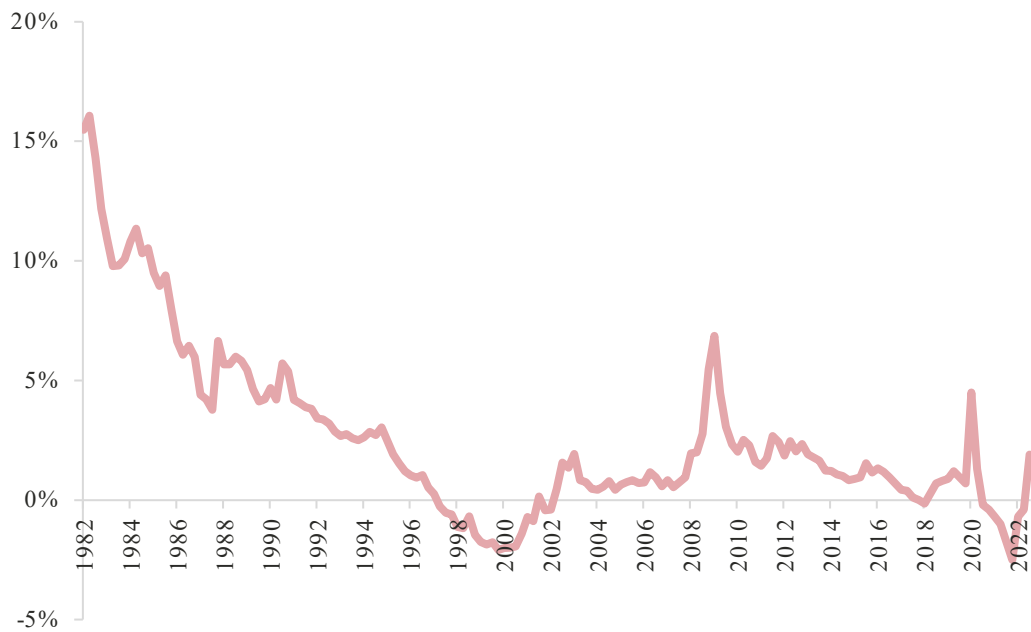
John Tatom, November 2011

Inflation and Asset Prices

INVESTING ENVIRONMENT

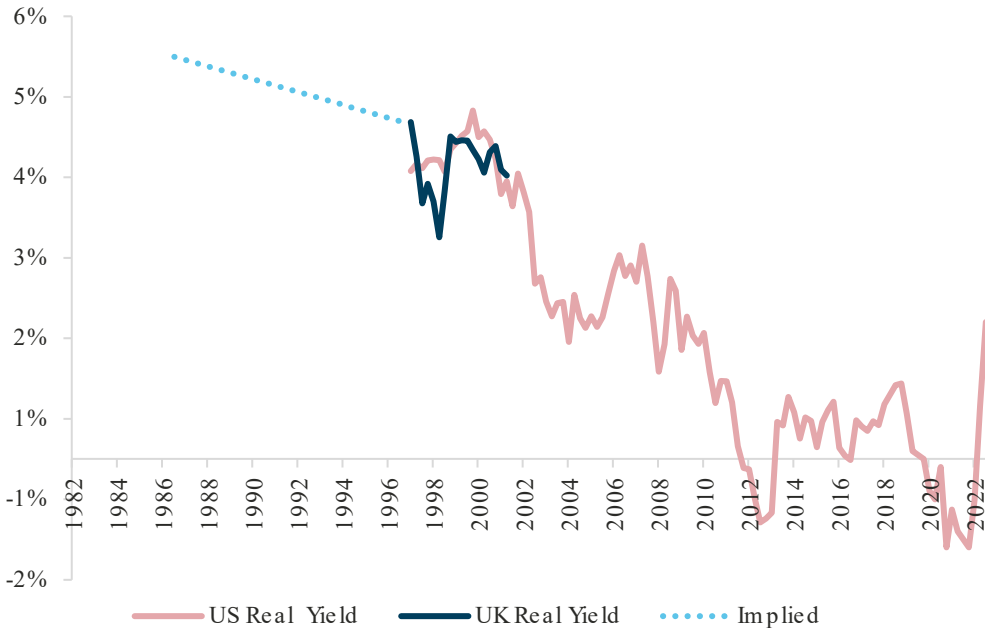
We believe that equities offer poor prospective returns due to elevated valuations ...real yields are more attractive with less risk

S&P 10 Year Real Return Model – 1982 to 2022<sup>1</sup>



<sup>1</sup>Model based on: Dividend + Earnings Growth + Valuation Change

10 Year US Real Yields – 1982 to 2022





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## INVESTING ENVIRONMENT

### Areas we are currently focused on:

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#### *Real Interest Rates*

- *Recent additions have been made to UK index linked adding to the global portfolio of inflation linked bonds*

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#### *Alternatives*

- *Some alternatives offer a higher potential reward but with higher risk*

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#### *Yen Assets*

- *The Yen is offering exceptional value and Japan could come to be seen as a safe haven in an inflationary world*

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#### *Energy Equities*

- *Supply constrained due to under-investment, Ukraine and OPEC+ cuts*
- *Undemanding valuations due to ESG selling constraints*

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#### *Sterling credit*

- *Combination of pension fund selling and BoE selling has led to high spreads even in short dated, economically insensitive sterling credit*

# Contact us

Lisa Bajardi

+(44) 203 906 1637

[Lbajardi@casset.com](mailto:Lbajardi@casset.com)

CG Asset Management  
20 King Street London  
EC2V 8EG

[info@casset.com](mailto:info@casset.com)

[www.casset.com](http://www.casset.com)