State of Play

15 July 2021

Our Investment Specialist, Simon Durling, shares his thoughts in our latest update. As ‘Freedom Day’ is approved, signs that consumers are returning to shops provides encouraging signs of an economic bounce back.

Freedom Day

Despite a backdrop of rising infection rates, ‘Freedom Day’ was approved by the UK Government at the planned review on 12 July. Further delaying the lifting of restrictions was seen as the greater risk leading into autumn, but some scientists have cautioned that the risk of the third wave filling up hospital beds is very real. The other concern is that the vaccination programme has slowed in recent weeks due to less support for being vaccinated in the younger age groups (rather than supply issues). Two thirds of UK adults have now received both injections and 87% have had at least one jab. Whilst the number of people being admitted to hospital and deaths have both increased by over 50% in the last seven days, the numbers are a fraction of those recorded in January and February at the height of the second wave. Experts guiding the UK Government have predicted the current wave will reach its peak in mid-August. Whilst all legal restrictions will be lifted on 19 July, the UK Government has urged caution and common sense to help slow the spread of the latest wave suggesting that individuals continue to wear masks in inside venues and crowded public transport.

Retail sales boost

Retail sales enjoyed a springtime recovery, recording the best April to June growth on record according to the British Retail Consortium (BRC). Sales in the period rose 28.4% from a year ago, which given the lockdown is not surprising, but when compared with pre-pandemic showed how strong the recovery has been as they were up 10.4% from 2019. The Euro football tournament and initial sunny weather helped boost trade with fashion and footwear doing well and the sale of new televisions surged as England progressed through to the final. But the BRC warned that many retailers still faced 'strong headwinds' as the UK economy recovers from the pandemic. However, online sales remained much higher than their pre-pandemic levels, suggesting the shift to online is 'here to stay', a BRC-KPMG retail sales report found.

The economic rebound slowed unexpectedly in May

The UK's economy grew slower than expected in May after disruptions to car production offset a surge in the hospitality sector. According to the Office for National Statistics (ONS) the economy expanded by 0.8% in May as COVID-19 restrictions eased to allow pubs and restaurants to serve indoors. This is the fourth month in a row of economic growth but at a much slower pace than the 2.1% seen in April with the UK economy still 3.1% below pre-pandemic levels. 'Pubs and restaurants were responsible for the vast majority of the growth seen in May', said Jonathan Athow, ONS Deputy National Statistician for Economic Statistics. 'Hotels also saw a marked recovery as restrictions lifted', he added. Accommodation and food services grew by a massive 37.1% in May, with the overall services sector growing 0.9%. UK carmakers struggled with a shortage of microchips, with the manufacture of transport equipment falling by 16.5%. Construction firms were hit by very wet weather in May as firms lost working days, although the ONS said the sector remained 0.3% above February 2020's pre-pandemic level.

House prices may continue to rise as supply shrinks

A lack of available properties is helping to push up house prices according to the Royal Institution of Chartered Surveyors (RICS), with the number of new properties coming to the market falling by a third in June. 'Respondents are pretty unanimous in once again highlighting the challenge around supply, whether in the sales or rental markets', said Simon Rubinsohn, RICS Chief Economist. Looking ahead the report said a net balance of 56% anticipated that prices will continue to increase over the next 12 months. Many industry commentators have agreed with this prediction despite the stamp duty incentives coming to an end last month simply because the UK is not building enough homes. The supply issues have been amplified by a lack of raw construction materials caused by a combination of Brexit and COVID-19 issues.

G20 finance ministers back 'historic' tax plan

Plans to combat tax avoidance by introducing a minimum global corporate tax rate of 15% has been boosted by the Organisation for Economic Cooperation and Development (OECD) signing 132 countries up to the framework. This is in addition to the plan agreed by leaders of the G7 major economies in Cornwall a month ago. The G20 finance ministers announced their support following a two-day meeting in Venice, Italy where 19 countries with the largest and fastest-growing economies, as well as the European Union, reached an agreement in principle. The UK's Chancellor of the Exchequer Rishi Sunak hailed the deal as 'historic', adding it would ensure the 'global tax system is fit for purpose in a digital age'. The policy, which will make companies pay more in the countries where they do business, will now go to a final meeting of the G20 leaders in October for consideration before signing on the dotted line.

Relief for income investors as the Bank of England lifts the bank dividend ban

Banks have been given the go ahead to start paying normal dividends after the Prudential Regulation Authority (PRA) deemed them financially resilient. In December the regulator said dividends could restart following a nine-month ban during the pandemic last year but introduced limitations on the pay-outs. Those restrictions have been removed with 'immediate effect', the PRA said on 13 July. Their announcement was at the same time as the Bank of England's Financial Stability Report, which found that banks were 'resilient to outcomes for the economy that are much more severe than the Monetary Policy Committee's central forecast'. Banks could withstand £70bn (pound sterling) of losses on top of the £20bn they took last year in impairments, the Bank's Financial Policy Committee (FPC) found in an interim stress test conducted on the country's biggest lenders. 'The total impact of the stress would use up less than 60% of banks' aggregate capital buffers', the FPC said. That health check has cleared the way for banks' boards to be able to resume making their own decisions about distributions to shareholders, in a move which analysts said would boost the sector's share prices. The Financial Stability Report is published every six months to consider present issues affecting the economy and to identify potential future threats.

Market update

Markets were buoyed by Chinese exports which grew much faster than expected in June as the global economy powered ahead on the renewed confidence provided by the vaccines. Chinese exports increased by 32.2% in June compared with the previous year, beating the 23% forecast. While exports to the US softened, growth to the European Union, Japan and emerging markets in Asia accelerated from May. Chinese trade has come under pressure recently due to a shortage of semiconductors and supply bottlenecks on top of higher raw material and freight costs. China remains a global economic indicator in the pandemic for its role as the world's manufacturer and strong growth in industrial production and exports are signs that global demand is strengthening. The world's second largest economy rebounded sharply from the outbreak of the virus, with gross domestic product (GDP) now back above pre-pandemic levels. China's imports increased 36.7% year-on-year in June, beating forecasts but slowing from a 51.1% rise in May.

UK shares managed to outperform their European counterparts earlier this week as mining companies were given a boost by promising trade data from China. The health of the Chinese economy is particularly important to the mining sector, given the Asian powerhouse's position as the world's biggest consumer of raw materials. Banking shares also nudged higher following confirmation from the Bank of England that the ban on dividends had been lifted.

Investors will keep a close eye on market reaction over the next few days as prices paid by US consumers increased in June by more than expected as higher commodity and labour costs associated with the economy's reopening continued to fuel inflationary pressures. The Consumer Price Index (CPI) jumped 0.9% in June taking the year-on-year figure to 5.4%, according to US Labor Department data released on 13 July. Used vehicles accounted for one third of the gain in the CPI last month, the agency said.

Find out more!

Click **here** to read our latest A Month in the Markets, where our Head of Multi-Asset Solutions Stefano Amato looks at how key themes impacted markets in June.

Note: Data as at 13 July 2021.

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