Rathbones
Look forward

Review of the week

21 February 2022

Back to the shops

UK retail sales bounced back after a COVID-crushed Christmas. Yet the longest income squeeze since Sir Robert Peel was Prime Minister is set to intensify in the coming months.

Markets have again been very volatile, with worries to suit the proclivities of any investor. Yet there have been some glimmers of better news as well, if you can look past some of the more glaring headlines. It's difficult to determine whether the positives or the negatives will prevail in the coming months. It's a strange time.

The UK stock market has been doing well lately, buoyed by its larger proportion of commodities companies and 'value' businesses whose profits should benefit as the pandemic melts into the background. UK property prices are soaring once again. The average asking price leapt 2.3% in the month to mid-February, the largest jump since Rightmove started the measure in 2001. The average listing price of £248,800 is almost 10% higher than a year ago.

And British retail sales were unexpectedly strong in January, with a 1.9% month-on-month increase. Economists had expected a rise of just 1.0%. The surge in spending was driven mostly by people shelling out on household goods and renewed petrol sales. However, this bounce back only offsets half of December's 4.0% fall as Omicron pushed the country back into quasi-lockdown.

Despite this ramp up in spending and the value of homes, a cost of living crisis is well underway in the UK. The annual decline in real wages could reach 3% or 4% by April as inflation rises and pay rises slow. For the average Brit, inflation-adjusted wages are lower now than they were in the first three months of 2007. This 15-year stagnation in the standard of living is the most protracted Britain has experienced since the mid-19th century. And this is unique to the UK - caused in no small part by a lot of unforced errors in economic policy.

The UK consumer confidence index is due out this week. It's been slipping back since its peak last summer and isn't expected to change much this month. In the coming months, we will be watching to see how UK households are feeling and spending - particularly whether they are continuing to switch from goods to services (which includes restaurants, cafes, theatre and travel). If so, this should help ease inflationary pressure, much of which is wrapped up in supernormal demand for goods in our usually services-rich economy.

There are two major factors bearing on how Brits are feeling and how they are spending. The main one is COVID-19. The government is this week due to update Parliament on the nation's long-term strategy for living with COVID. Case numbers, hospitalisation and deaths are sharply down from December, leading to the hope that the end of the pandemic is finally in sight. The government reportedly wants to keep the infrastructure in place to quickly respond to another problem variant, yet it wants to strip away most of the testing and isolation requirements to ease staffing problems and reduce costs for the public and private sectors.

As for the other factor influencing the optimism of the British people...

A poorer pound

The pump prices of diesel and petrol are at record highs. Both are trading at roughly £1.50 a litre, a level that drivers have never seen before.

The AA says nearly half of members it surveyed are driving less because of the soaring cost. About 30% reported they are cutting back on spending elsewhere because of the increase cost of a tank as well.

Brent Crude Oil is trading near $95 a barrel, much higher than at any point since late 2014. Of course, oil has broken $100 before. Back in 2014, it traded between $100 and $120 a barrel for most of the year. This time around, however, the pound is worth much, much less. In 2014, sterling bought between $1.50 and $1.60; today, the exchange rate is $1.35. That means the pounds and pence cost for fuel is that much higher. It's a cruel lesson in the economics of exchange rates and the prevailing cost of globalised commodities. Filling the car is a significant expense for many people and prices at the pump tend to have a noticeable impact on people's perception of inflation

and sense of buying power. So fuel passing the $1.50/litre level, combined with soaring electricity and gas prices, may worry many families and persuade them to rein in spending.

High oil and gas prices are likely to remain for as long as the **Ukraine stand-off between the West and Russia continues**. The potential for supply disruption - whether by sanctions, damaged infrastructure or weaponised withholding of deliveries - will keep commodity investors on edge. This doesn't just affect the UK, of course. European inflation is due out this week. It's expected to remain flat at 5.1%, which is by far the highest level of this millennium. And US inflation is 7.5%, its highest level since 1983.

The longer this global squeeze on living standards goes on, the greater the pressure on companies to raise wages. This could risk a spiral of wages and prices, however, it would be extremely unlikely for the phenomenon to be as rampant and costly as it was in the 1970s or 1980s.

Today, central banks are independent and tasked with maintaining inflation at a low, healthy rate. Also, much weaker union membership makes it harder for workers to secure rapid, widespread gains in pay. And, finally, productivity growth - the ability to create more with less - may get a jump-start from the huge amount of investment businesses made during the pandemic. New ways of working might make workers more productive, businesses more profitable and therefore allow wages to rise without creating inflationary price hikes in the wider economy.

If you have any questions or comments, or if there's anything you would like to see covered, please get in touch by emailing review@rathbones.com. We'd love to hear from you.

Rathbones
Look forward

Important information

This document is published by Rathbone Investment Management Limited and does not constitute a solicitation, nor a personal recommendation for the purchase or sale of any investment; investments or investment services referred to may not be suitable for all investors. No consideration has been given to the particular investment objectives, financial situations or particular needs of any recipient and you should take appropriate professional advice before acting. The price or value of investments, and the income derived from them, can go down as well as up and an investor may get back less than the amount invested. Rathbone Investment Management Limited will not, by virtue of distribution of this document, be responsible to any other person for providing the protections afforded to customers or for advising on any investment. Rathbone Investment Management International is the registered business name of Rathbone Investment Management International Limited which is regulated by the Jersey Financial Services Commission. Registered office: 26 Esplanade, St Helier, Jersey JE1 2RB. Company Registration No. 50503.

Rathbones Group Plc is independently owned, is the sole shareholder in each of its subsidiary businesses and is listed on the London Stock Exchange. Rathbones is the trading name of Rathbone Investment Management Limited, which is authorised by the Prudential Regulation Authority and regulated by the Financial Regulation Authority and the Prudential Regulation Authority. Registered office: Port of Liverpool Building, Pier Head, Liverpool L3 1NW. The information and opinions expressed herein are considered valid at publication, but are subject to change without notice and their accuracy and completeness cannot be guaranteed. No part of this document may be reproduced in any manner without prior permission.

Any views and opinions are those of the author, and coverage of any assets in no way reflects an investment recommendation. Past performance should not be seen as an indication of future performance. The value of investments and the income from them may go down as well as up and you may not get back your original investment. Fluctuations in exchange rates may increase or decrease the return on investments denominated in a foreign currency.