Monthly

Economic Review

Provident Solutions
Wealth Creation & Wealth Management
Financial Lifestyle Planners

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Economic review of: **February 2014**

Our monthly economic review is intended to provide background to recent developments in investment markets as well as to give an indication of how some key issues could impact in the future.
It is not intended that individual investment decisions should be taken based on this information; my colleagues and I are always ready to discuss your individual requirements. I hope you will find this review to be of interest.

Paul Smith

Inflation dips below 2%

More good news on the economy was announced in mid February, as for the first time in four years the UK's Consumer Prices Index (CPI) fell below 2% to 1.9% in January. However, at the same time the wider Retail Prices Index (RPI) rose to 2.8% from the previous level of 2.7%.

This is of some importance, as the inflation rate is now below the target set the Bank of England (BoE) by the Government, which requires the Governor of the Bank to write in explanation to the Chancellor, should the CPI movement be more than 1 percentage point above or below target.

These inflation figures, released by the Office for National Statistics (ONS), have added weight to the BoE's recent statement that there is no need to raise interest rates at this time.

David Kern, the Chief Economist of the British Chambers of Commerce (BCC), reinforcing this policy, was quoted as saying: *"An economic environment of low inflation and low interest rates allows people and firms to plan ahead, as they can be confident that they will not encounter any unwelcome surprises."*

Whilst the good news on this front is warmly welcomed, as average earnings growth still remains muted, at only 1.1% in the year to December 2013, it is questionable if people generally are feeling better off.

Among the main factors behind the dip in the CPI rate were; lower alcohol prices, a fall in tobacco prices, discounts on household goods and furniture, and lower entrance fees for cultural and leisure activities.

The Chancellor of the Exchequer, George Osborne, commenting on these results, tweeted: *"Today's fall in inflation is more evidence our long-term economic plan is working. We want to ensure a secure future for hard-working people."*

Retail sales defy the weather

Despite the atrocious weather experienced in the first two months of the year and a warning from the Governor of the Bank of England, Mark Carney that the recent floods may: *"Affect the near-term (growth) outlook"*, February saw retail sales grow at their fastest pace for two years. This represents the ninth consecutive month of expansion.

The Confederation of British Industry (CBI) reported in their Distributive Trades survey, that whilst January saw disappointing sales, February compensated with improved sales of clothing and given the resurgent housing market, improved sales of carpets, household goods and furniture.

Shoppers brave the storms

Their survey, which canvassed 120 companies, reported that 45% of respondents saw higher sales in February, whilst only 8% saw a decline. The positive balance of 36% is the highest recorded since June 2012.

Furthermore, 28% of respondents expected further sales growth in March and 17% of retailers expect to increase their investment in their businesses.

The Chairman of the CBI's Distributive Trades survey, Barry Williams, said of these findings: *"The high streets have kicked on once again this month.*

"Overall sales have been remarkably resilient in the face of disruption from exceptional weather across the UK, which has badly affected many families and businesses."

This survey follows on from a January report from The British Retail Consortium (BRC), representing the major retail chains in the UK, together with KPMG's Retail Sales Monitor.

In the latter, David McCorquodale, Head of Retail, said: *"The divide between food and non-food is stark, with the battle for market share in food remaining ferocious, customer loyalty fickle and cost deflation being passed through to the customer."*

Markets: (Data compiled by The Outsourced Marketing Department)

Global equity markets regained their composure in February with the FTSE100 gaining 4.6% to end the month on 6,809.7, whilst the wider FTSE250 also saw a 6.71% gain, closing on 16,726.00, and the junior

Equities regain a little composure

AIM market finishing on 886.3, a rise of 3.17%. Across the pond, the Dow Jones did likewise, gaining 3.97% to 16,321.71 and the Nasdaq rising 4.98% to 4,308.12.

In mainland Europe, the Eurostoxx50 also rose by 4.49% to close at 3,149.23. However, in Japan the Nikkei 225 failed to rally, ending February down a marginal 0.49% at 14,841.07.

On the foreign exchanges, sterling was in favour, given the clearer forward guidance on interest rate policy offered by the Bank of England. It closed at $1.67, up 1.83% against the greenback but virtually flat against the Euro at €1.21. The Euro itself gained 2.22% against the US Dollar, closing the month on $1.38.

As for the commodities, Oil, as measured by the Brent Crude benchmark, rose by 2.45% over the month to finish at $109.01. Gold continued its recent rally, gaining 8.17% to close at $1,345.75 an ounce.

N.B. Given the military intervention of Russia, attempting to annexe the Crimea region of the Ukraine, which took place over the weekend of March 1st and 2nd , most markets reacted negatively on the first working day of March. As we go to press on March 3rd the FTSE100 is down 78.42 points to 6,731.1, a 1.4% fall, the FTSE250 down 308.01 points at 16,416.99, or 1.8%, the Eurostoxx50 off 60.42 points at 3,088.81, down 1.9%, and the Nikkei 225 off 188.84 points at 14,652.23, down 1.3%.

Bank of England clarifies position

In a highly anticipated move, the Governor of the Bank of England (BoE), Mark Carney, has restated the Bank's guidance on its interest rate policy, given the fact that UK unemployment has declined to very close to the 7% target level they previously set for possible action on this front.

Forward guidance expanded

Whilst reiterating that their forward guidance *"is working"*, by reducing uncertainty in the market place and promoting businesses to invest and increase recruitment - thus helping the economy to grow – he did say, however, *"as a result of exceptionally strong jobs growth"* it is time to look at a wider range of factors in determining their interest rate stance, as at the moment the UK economy is still not secure.

These factors may include; wages, spare productivity and the gap between potential and actual economic growth, known as the 'output gap'.

The Governor intimated that in the short term the BoE would only *"gradually"* raise interest rates to around 2% by 2017, further reassuring the market. Analysts believe that this process could start by Q1 or Q2 2015.

The BoE will also be publishing forecasts of a number of economic factors based on this assumption of rates reaching 2% by 2017.
Overall, Mark Carney's projections for the economy were slightly bullish, saying that business investment was likely to gather pace in 2014, enabling them to increase their forecast for economic growth in 2014, from 2.8% to 3.4%. He did, however, caution that, at present, the economy was *"neither balanced nor sustainable"*, and that *"A few quarters of above trend growth driven by household spending are a good start but aren't sufficient for sustained momentum."*

The clear message was; there was still work to be done, but that their own inflation report stated; *"Bank rate may need to remain at low levels for some time to come."*

Unemployment continues to fall

Positive data also came in February with regard to the UK's unemployment rate, which was reported at 7.2% by the Office for National Statistics (ONS). This represents a fall of 125,000 people to 2.34 million in the three months to December 2013. The previous three months figure was 7.6%, so a fall of 0.4% over the period.

There are now a total of 30 million people in employment in the UK, a rise of 193,000 on the quarter. This represents an employment rate in the country of 72.1%, an increase of 0.6% from the previous period.

Youth unemployment also fell to its lowest level since early 2011, to 900,000, and a fall in the long-term unemployed was also reported by the ONS.

Those claiming Jobseeker's Allowance saw a 15th consecutive monthly drop to 1.22 million; this is a reduction of 27,600 people.

Other statistics released by the ONS showed that self-employment had reached a record high at 4.37 million, an increase of 172,000, and that there are now 14 million women in employment and this is the highest figure seen since records began. There are now 1.4 million people in part-time employment because they cannot find full-time work, however, this represents a fall of 29,000 on the previous quarter, although 46,000 higher than a year earlier.

So all good figures, but Nick Palmer, the Senior Labour Market Statistician at the ONS cautioned: *"The main conclusion that should be drawn from these latest figures is that the rate at which unemployment has been falling is likely to have slowed down."*

In a more positive, though political response, Esther McVey, the Employment Minister said that: *"Record numbers of women are in work and youth unemployment continues to fall, which means more people have the security of a regular wage and can plan for their future."*

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