ECONOMICREVIEW of November 2015

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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; we are always ready to discuss your individual requirements. I hope you will find this review to be of interest.

Paul Smith

The Bank of England's Inflation Report

In early November the Bank of England released its Inflation Report, as recorded by their Monetary Policy Committee (MPC). The committee decided, by an 8-1 majority, to leave the Bank Rate at its historical low of 0.5%. There was one dissenting MPC member, Ian McCafferty, who would have preferred to see a 25 basis point (1/4%) increase. They did, however, unanimously vote to leave their purchase of assets at the current level of £375 billion. This is also colloquially known as their *'Quantitative Easing'* programme.

Sanguine view on the inflation front from BoE

As at the end of September, the Consumer Prices Index (CPI) stood at -0.1%, which is marginally more than 2% below the Bank's own inflation target. They cite lower prices in food, imported goods and energy as the major factors here, with lower domestic cost growth as a lesser influence. The wider core inflation rate currently stands at 1%.

Whilst they believe that CPI will remain subdued at around the 1% level until Q3 or Q4 of 2016, the Bank did confirm that they are determined to return inflation to the 2% target range within two years in a careful and sustainable way, avoiding the danger of it overshooting, should the current disinflationary factors diminish. They also believe domestic momentum is strong, consumer confidence is high and wage growth is continuing to improve.

Given that the MPC believes that the Bank Rate will rise in due course, as inflationary factors reverse, it also expects any such rise to be more gradual and to a lower level than seen in previous economic cycles.

UK's service sector sees improvement

The UK service sector saw growth in October; the first time in four months that the growth rate has improved.

The closely followed 'Markit/CIPS Service Sector Purchasing Managers Index' (PMI) improved from the 53.3 level, seen in the previous month, to 54.9 – any figure above the 50 mark represents growth in the sector.

Whilst this data was welcomed, Markit did state that the pace of improvement was still *"relatively subdued"*.

The PMI went on to say that within the sector there was strong jobs growth, as it hit a five-month high.

This good news follows similar bullish results, released recently by PMI, from both the 'manufacturing' and 'construction' sectors.

Chris Williamson, the Chief Economist of Markit, was reported as saying: *"Such an improvement, together with the revival in hiring signalled by the three surveys… may coax more policymakers into (voting to raise) interest rates before the end of the year."*

However, he reportedly went on to add: *"Dovish policymakers will note the ongoing lack of inflationary pressures in October, suggesting that there is no need to rush into raising rates."*

The Government itself will be very pleased to see more business sectors seeing improved performance, as the Chancellor of the Exchequer, George Osborne, has stated that he is committed to seeing a far more balanced economy evolving across the country, with less reliance on any one sector to drive GDP growth.

Editor's note: The future direction and timing of interest rates remains a contentious subject, given the Governor of the Bank of England, Mark Carney's recent comments on the subject. See *'The Bank of England's inflation report'* article.

More balance seen in economy

Markets: (Data compiled by The Outsourced Marketing Department)

Despite tragic terrorist activity in Paris, resulting in the death of 130 innocent civilians, and the shooting down of a Russian bomber across the Syrian/Turkish border, the equity markets, surprisingly, maintained their composure.

Despite incurring large losses in mid-November, the FTSE100 rallied to close at 6,356.1, down just 0.08% on the month and up 1.7% on the quarter. The wider FTSE250 fared even better gaining 1.77% in November to finish at 17,420.7, whilst the junior AIM market matched the FTSE100 performance to lose 0.08% at 737.3.

In the USA the Dow Jones trod water, closing out November at 17,719.92 for a marginal gain of 0.32%, with the Nasdaq index rising 1.09% to end at 5,108.67.

As reported last month, the prospect of renewed fiscal stimulus from the European Central Bank, allowed the Eurostoxx50 to maintain its positive momentum, as it gained just under 45 points to 3,488.99 for a 2.07% improvement on the month.

Likewise, the Japanese Nikkei225 index also remained in positive territory, finishing at 19,747.47 an improvement of 3.48%.

The foreign exchange markets saw the US Dollar powering ahead of the Euro currency, breaking parity to $0.94 for a 14.5% uplift, whilst the Euro also slipped against Sterling to €1.42 a fall of 1.43%. Given the bullish sentiment in the US Dollar, due to the anticipation that the US Fed will raise interest rates soon, Sterling slipped 1.43% to $1.51.

Markets remain resilient under pressure

Gold lost its recent momentum falling $76 in the month to $1,065.8 an ounce and recording a 6.62% fall.

Oil, as measured by the Brent Crude benchmark, fell yet again - as a result of continuing oversupply - to $44.61 a barrel and compounding its year-to-date fall to 22.19%.

OBR gives Chancellor room to manoeuvre

With a surprise major U-turn over his intended Tax Credit cuts, George Osborne, the Chancellor of the Exchequer, delivered his joint Spending Review and Autumn Statement.

Despite this setback to his finances, from which he had hoped to save £4.4bn in welfare costs, he still maintains that he will be able to achieve £12bn of welfare saving each year up to 2020.

His main announcements were a pledge to bring the UK's budget into a surplus of £10.1bn by tax year 2019/20, increase spending on the NHS by £6bn in 2016, whilst defence spending will meet NATO's recommended 2% of GDP with a total spend of £178bn over the next decade. He will maintain the current budgets allocated to education, overseas aid, and the police force.

Housing will get a huge boost with him promising the building of 400,000 new homes, 200,000 of which will be 'starter homes'. House builders and developers will be offered grants to achieve this target and incentives to regenerate brown-field sites for such development.

The basic State Pension will rise by £3.35 a week to £119.30, whilst the maximum flat rate New State Pension will be set at £155.65 per week. The newly introduced Automatic Enrolment pensions for all employees, will see the proposed increase in employer contributions to 2% of payroll, pushed back from 2017-18 to 2018-19.

Tax avoidance is to be targeted with the ambition of recouping £5bn of tax annually. They will introduce a General Anti-Abuse Rule with penalties imposed for disguised remuneration schemes, blatant stamp duty avoidance and the abuse of the intangible fixed assets regime and capital allowances. In future all tax returns for individuals will be digitalised and handled on-line by the end of the decade. As a result of this the HMRC will close 177 local tax offices.

Average UK house prices up 6.1%

House prices in the UK have increased in value by 6.1% annually in the year to September 2015, according to the Office for National Statistics (ONS). This is a larger increase than the 5.5% rise recorded in August and the 5.2% one in July. This brings the average house price across England to £286,000.

Although an impressive increase in value, it does not match the price rise seen a year earlier of 12%.

As always, there were wide regional variations, with price increases in Northern Ireland topping the list at 10.2%, whilst Wales and Scotland could only record a modest 1.1% rise. In average house price terms, London, as usual, topped the list with houses there now averaging £531,000 and recording an average increase of 7.2%.

Overall, the increase in house prices in England was driven by the annual increases in London (as above), in the East by 8.4% and the South East rising by 7.4%. At the other end of the scale, houses in the North East of England averaged £158,000 with a more modest annual increase of 1.8%.

In September 2015, prices paid by first time buyers were 4.3% higher on average, against the same time last year, while owner-occupiers (existing owners) also saw an annual increase of 6.9%.

Commenting on these figures, a former Chairman of the Royal Institute of Chartered Surveyors (Rics), Jeremy Leaf, was reported to have said: *"With the average property price in London now £531,000, unless you earn way above the national average salary, you have precious little hope of being in a position to buy.*

"Generation Rent is being left out in the cold; they have aspirations to buy but are being pushed further away from their goal."

It is important always to seek professional advice before making any decision regarding your finances. If you would like any assistance, please contact us.
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