ECONOMICREVIEW
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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

A new paradigm in oil prices

The price of oil has been below $100 a barrel now for two months, after spiking at $115 a barrel in June.

Currently sitting at $85.86 a barrel, as measured by the Brent Crude (BC) benchmark, this level sees the price having dropped nearly 25% in the last five months of 2014.

Prices to remain low into 2015

Industry analysts are predicting that it will drop as low as $80 per barrel by Q2 2015. At the same time they believe the West Texas Intermediate (WTI) benchmark price will also fall to $70 per barrel, after it spiked at $103 in June.

There are many reasons for this dramatic fall in prices; primarily through oversupply, with Saudi Arabia continuing to boost production to safeguard their petrodollar income, the revival of Libya's production capability and increased production from non-OPEC countries outside of the United States.

In America itself, the massive shift to production of Shale Gas, enabling the USA to become a net-exporter of energy, has compounded the supply side.

Russia was also ramping up oil and gas production to counter the loss of income via its petrodollar revenues, as a consequence of the weakness of the Rouble, which has devalued considerably since the introduction of economic sanctions imposed by the EU and America, because of its incursions into the Ukraine.

Meanwhile, BG Group - one of the UK's largest energy groups after BP and Royal Dutch Shell - said its production had increased in both the UK and Brazil.

On the other side of the equation, global demand has diminished considerably, particularly in China, which has seen a slowing of its economy and therefore a reduction in its imported energy needs and the near stagnation of the eurozone, with many of the southern states there flirting with deflation and thus reduced manufacturing output.

Analysts believe that this trend will ease come the second half of 2015.

Inflation continues to fall

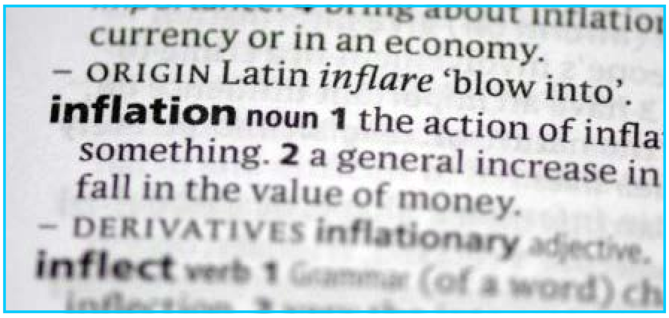
Further encouraging news came on the inflation front with the headline Consumer Prices Index (CPI) dipping to 1.2% in September, down from the 1.5% recorded the month before. This is the lowest CPI figure seen since September 2009.

The Office for National Statistics (ONS), who compile the data, reported that transport costs, with the price of fuel falling 6%, compared with September last year, and the price of recreational goods and food, down 1.5%, as a result of the continuing price competition between the major supermarket chains, were the major factors in the reduced inflation rate.

The wider Retail Prices Index (RPI), which used to be used as the benchmark for many welfare payment increases and public sector wage increments, also fell from 2.4% to 2.3%. However, this link has been diminished recently with the government limiting such public sector pay rises to 1% and the *'triple-lock'* mechanism of the highest of inflation, earnings, or 2.5%, now seeing state pensions rise by that higher rate of 2.5%.

Given that the Bank of England (BoE) has been charged by the government with meeting a 2% target for CPI inflation, the fact that the true figures have undershot this level for several months now, indicates that the Monetary Policy Committee of the BoE would be unlikely to raise interest rates from their historic low of 0.5% until early 2015 at the earliest and maybe not even before the next UK general election, currently scheduled for May 2015.

Because of this benign outlook for future inflation and its likely effect on UK interest rate decisions, the global foreign exchange markets immediately sold Sterling against both the US Dollar and the Euro. The initial reaction saw the US Dollar/Sterling rate fall to $1.597 and the Euro/Sterling rate to €1.253, as the markets' expectation of imminently higher interest rates diminished.



UK Inflation remains benign

Markets: (Data compiled by The Outsourced Marketing Department)

October saw the equity markets continue in the volatile fashion they performed in September. The London markets reacted badly to the continuing accountancy issues at Tesco, prolonged economic weakness in the eurozone and the slowing Chinese economy. At one point in mid-October the FTSE100 had fallen to 6,195.9; a drop of 6.5% from its September close, but managed a late rally to end October at 6,546.5 for a loss of only 1.16% on the month. The wider FTSE250 fared a little better closing out at 15,501.73, recording a modest gain of 0.79%, whilst the junior AIM market lost 3.91% to end the month on 720.17.

Across the pond the US Treasury confirmed it is ending its quantitative easing programme, as it feels its economy is now on a sound footing. As a result, the Dow Jones index rallied to a record closing level of 17,390.52, for a monthly gain of 2.04%. The Nasdaq also saw gains of 3.06%, finishing October at 4,630.74.

Persistent weakness in the eurozone economies and the remaining threat of deflation there saw the Eurostoxx50 lose 4.43% to end at 3,082.92, reversing its recent gains. In Japan the 'Abenomics' of massive quantitative easing drove down the Yen and also saw the Nikkei 225 drop by 3.19% to 15,658.20, also reversing the gains achieved in September.

Given that pundits now believe UK interest rates will remain low, possibly even into 2016, Sterling lost its admirers, losing 1.23% against the US Dollar to $1.60 and a less dramatic 0.78% against the Euro at €1.28. Meanwhile, the US Dollar gained a similar 0.79% to end at $1.25 against the Euro.

As reported elsewhere here, oil has fallen dramatically to only $85.86 a barrel, as measured by the Brent Crude benchmark and economists believe it has further to fall.

Gold, the usual safe-haven asset in times of unrest, did not react accordingly, as it lost 2.82% to end the month at $1,172.64 a troy ounce.

A volatile month in the markets

Property market pauses for breath

With home loans hitting their lowest level for two years, property prices in the UK have lost their momentum.

Partly as a result of the stricter mortgage qualification process, introduced with the Mortgage Market Review (MMR) and a cap on the number of mortgages with high loan-to-value ratios, the Bank of England (BoE) reported that mortgage lenders reduced their loan availability to its lowest level since the Lehman Brothers collapse. The 'sentiment survey', which measures mortgage availability, dipped to -28.5 in the three months through early September, from Q2's level of 8.2. This confirms that the demand for home loans *"decreased significantly"* in the period.

Whilst the repercussions of the MMR's stricter criteria greatly lengthened the application process for borrowers, the survey also showed that the majority of lenders believed that lending will return to its previous levels in the next three months.

Meanwhile, the Royal Institution of Chartered Surveyors (RICS) confirmed this trend by reporting that new property buyers fell for a third month in a row in September. They went on to add that in London *"caution took a particular toll"* as demand here was down for a fifth consecutive month and they expected prices here to continue to dip over the next three months. However, at the same time the majority of RICS respondents still saw prices elsewhere rising, albeit at a subdued level.

Simon Rubinsohn, the Chief Economist at RICS, was quoted as saying: *"Part of this is down to the Bank of England becoming more vocal about the risks, part of this is down to affordability, part of this is down to the new mortgage rules and part of this is down to expectations of higher interest rates."*

The Council of Mortgage Lenders also reported a decline in first-time buyers in August, compared to July, of 4%.

Mortgages taking longer to approve

Unemployment falls below 2 million mark

The latest unemployment figures, released by the Office for National Statistics (ONS) in mid-October, confirmed that unemployment in the UK has dropped below 2 million for the first time in nearly six years.

With the number of jobless falling by 154,000 to 1.97 million in the three months to August 2014, the latest data surprised many analysts as the rate dropped to 6%.

On an annual basis, unemployment in the UK has now fallen by 538,000, which is the largest fall recorded since records began.

There are now 30.76 million people in employment, a rise of 46,000 over the latest three-month period covered; however, this was the poorest quarterly gain since May 2013, which may indicate that the surge in economic activity and hence employment may be slowing somewhat.

The figures showed an improvement across the workforce, including youth unemployment (those aged between 16-24) down by 88,000 to 733,000. This represents an unemployment figure of 16% for this age group.

Those claiming the Jobseeker's Allowance in September also fell to 951,900, a fall of 18,600 over the quarter, and the number of people now classified as self-employed dropped by 76,000 to 4.5 million, which is 279,000 more than recorded a year ago.

Good as these figures are, it is interesting to note that the employed figures include 6.8 million people in part-time jobs and the average wage increases are only 0.7%, which remain stubbornly below the current rate of inflation of 1.2% (CPI).

Commenting on these figures, the Chancellor of the Exchequer, George Osborne, was quoted as saying it was: *"evidence that our long-term economic plan is working.*

"I'm the first to say there are still many people out of work. We need to make further reforms to our welfare system so that people have a life of work, rather than a life on the dole."