

Market Monitor – United Kingdom

Delay of Reopening Weighs on UK Economy



UK economy benefits from reopening

The British economy has recovered further following the relaxation of lockdown measures. While failing to meet the market expectation, monthly GDP nonetheless continued to grow by 2.3% in April, following a 2.1% increase in March. The consumer-facing services sector saw a significant rebound following the reopening of non-essential retail stores and the resumption of outdoor catering services. This has helped most recent economic figures remain robust. Although the manufacturing and services purchasing managers' indices (PMIs) in June were lower than in May due to the delayed lockdown relaxation, they remained elevated at 63.9 and 62.4, respectively. The GfK consumer confidence index stood at -9. Unemployment dropped further to 4.7% in May, down from 4.8% in April.

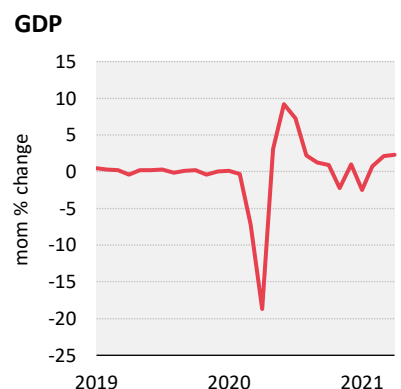
The economic outlook is clouded by the new virus mutant and post-Brexit talks

However, the UK economy is expected to remain impacted by the pandemic in the short term. Although the rapid vaccination progress is expected to boost the consumer and business sentiment, the delay of the final stage of lockdown easing amid the spread of the Delta variant will limit economic activity. The new variant proved to be more transmissible just as rules about social gatherings were relaxed, and the number of new cases has surged since the start of June. The 7-day rolling of daily new cases was over 20,000 in early-July, compared to the low of less than 2,100 in early May. To bar the virus from spreading further, the UK government has delayed the final stage of lockdown easing to 19th July rather than 21st June as previously scheduled.

The delay in the reopening schedule and the dispute with the EU may drag the near-term UK economic performance.

In view of the new virus mutant and the fade of the furlough scheme, the Bank of England is expected to keep the Bank rate unchanged.

The housing price rose further. Yet the end of the stamp duty holiday and furlough scheme may hit the housing market.



Source: Bloomberg, data as of 2/7/2021

Meanwhile, to better shield against the new variant, the UK government is speeding up the vaccination programme. In England, vaccines are now available to individuals aged 18 or above. The second dose for individuals aged 40 or above will be accelerated, with the gap between the two jabs being shortened to 8 weeks instead of 12. As of 3rd July, over 45 million UK citizens, or 67.8% of the population, had received at least one dose of vaccine. More than 33 million people, or 50.3% of the population, were fully vaccinated. By 19th July, the government targets to have fully inoculated two thirds of individuals aged 18 or above, including all individuals aged 50 or over and the clinically extremely vulnerable, and to have given all adults the first dose. A high proportion of fully vaccinated individuals will aid the economy by allowing for all movement restrictions to be relaxed.

Alongside the pandemic, another downside risk is the post-Brexit talks with the EU. The two have reached a deal regarding the fishing quota for the remainder of 2021, which is said to worth GBP333 million. But they have not yet agreed on the Northern Ireland issue. The mandatory checks on fresh foods from the UK to the Northern Ireland will be implemented from July onwards under the Northern Ireland Protocol. The EU agreed the UK's request for a three-month grace period until end-September.

Meanwhile, jobs website Indeed found that the number of EU citizens searching for UK jobs has fallen 36% since Brexit. While some vacancies in advanced sectors can be filled by jobseekers from around the world, it is harder to find foreign workers for lower-paid jobs, which increasingly rely on domestic workers. The shortage of workers in industries such as hospitality and the care sector may limit the UK's economic growth.

Bank of England expected to keep interest rates unchanged given the new Covid variant

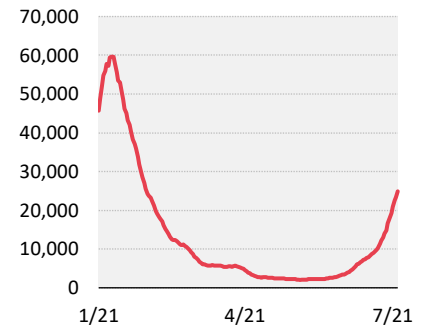
Despite a hawkish move in its May meeting, the Bank of England (BoE) kept the Bank Rate unchanged at its next monetary policy meeting. In view of the 2.1% inflation seen in May, which exceeded the BoE's inflation target of 2.0%, the Bank of England (BoE) expected inflation to exceed 3.0% in its June meeting. Yet, the BoE considers the recent rise to be short-term. It has also shown no sign of further monetary policy tightening ahead.

However, given the delay in the UK's reopening schedule, the BoE kept the scale of its asset purchase programme at GBP 845 billion. In addition, the BoE is concerned about the impact on the labour market after the furlough programme ends in September, which may further reinforce its decision to keep the Bank Rate and quantitative easing unchanged.

The housing market is supported by policies and changes in preferences

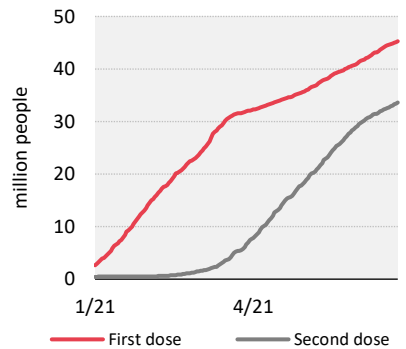
The BoE is nevertheless eying the housing market due to the continuous rise in house prices. The Nationwide Housing Price Index grew 0.7% monthly in June, marking a 13.4% yearly growth, the largest increase since December 2004. This is because of the extension of the stamp duty holiday until end-September and the change in preference for more

7-day rolling average of daily new cases



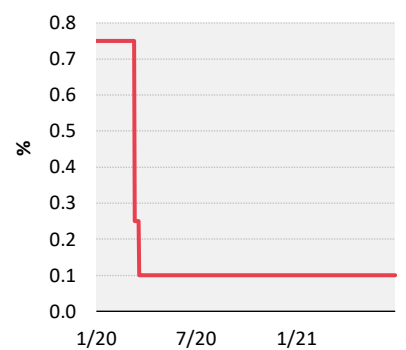
Source: UK Government, data as of 5/7/2021

Number of people vaccinated



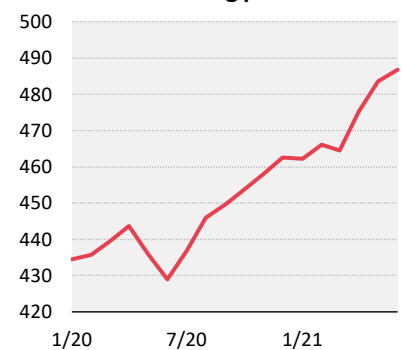
Source: UK Government, data as of 5/7/2021

Bank Rate



Source: Bloomberg, data as of 2/7/2021

Nationwide housing price index



Source: Nationwide Building Society, data as of 5/7/2021

Economic Research

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spacious flats. The BoE has commented that the housing market is on fire and is carefully monitoring the inflationary pressure this is generating.

Looking ahead, the housing market is expected to be further supported by the change in buyer preferences and the government's new mortgage guarantee scheme that provides a guarantee on mortgages for home buyers who can only afford a 5% deposit. However, if the labour market deteriorates sharply following the end of the furlough scheme, the housing market will be hit. The end of the stamp duty holiday at the end of September may put further pressure on housing prices.

Financial markets supported by strong economic performance, yet impacted by the delay in economic reopening

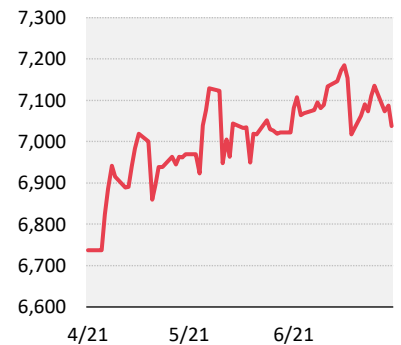
In the stock market, the FTSE 100 Index rose slightly by 0.2% in June. The performance was supported by upbeat economic figures and the dovish stance of the BoE. However, market sentiment is constrained by the aggravated pandemic and the delay of reopening.

In the bond market, the 10-year UK government bond yield dropped 79 basis points in June. The surge in UK inflation and the Fed's plan for earlier rate hikes has caused some risk aversion, triggering demands for bonds.

In the foreign exchange market, the pound appreciated 0.4% against the euro in June. Despite the UK's resurgence in new infections and the dispute over the Northern Ireland issue, the pound has been supported by the country's strong economic performance and good vaccination progress. But the pound depreciated 2.7% against the US dollar due to the latter's strength.

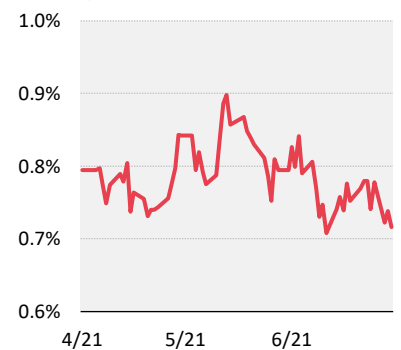
Looking ahead, although the UK financial markets will remain supported by economic performance, disputes with the EU and the reopening schedule are expected to dictate market sentiment. In the meantime, any BoE signal of monetary tightening before that of the Fed or the European Central Bank is expected to support the pound's performance against the US dollar and the euro, at the expense of the stock market.

FTSE 100 Index



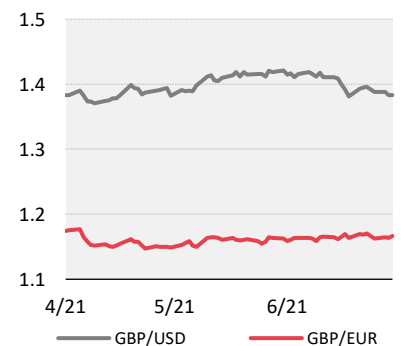
Source: Bloomberg, data as of 30/6/2021

UK 10-year Government Bond Yield



Source: Bloomberg, data as of 30/6/2021

British Pound Exchange Rate



Source: Bloomberg, data as of 30/6/2021

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