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INDEPENDENT FINANCIAL ADVISERS

Economic Review

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Chancellor's Growth Plan

In his first fiscal statement since becoming Chancellor, Kwasi Kwarteng hailed a "new approach for a new era" as he unveiled a series of tax cuts and other measures designed to spur economic growth.

During a 'mini-budget' delivered on 23 September, the Chancellor outlined a Growth Plan centred on the biggest package of tax cuts in fifty years. As well as reversing April's National Insurance rise and the planned increase in Corporation Tax, Mr Kwarteng also announced Income Tax and Stamp Duty cuts with the total cost of the package estimated to be almost £45bn by 2027. On 3 October, the Chancellor announced a U-turn on plans to scrap the 45p rate of Income Tax.

These plans are set to be funded via a large increase in borrowing, with Treasury estimates suggesting an additional £72bn of government borrowing as a result of the Chancellor's announcement. Paul Johnson, Director of the independent Institute for Fiscal Studies, described the plans as a "big gamble" and sterling came under intense pressure after the statement as financial markets gave their verdict on Mr Kwarteng's Growth Plan.

In an unusual intervention, the International Monetary Fund (IMF) also openly criticised the Chancellor's proposals, warning that 'large and untargeted fiscal packages' were not recommended at a time of 'elevated inflation pressures.' The IMF, which works to stabilise the global economy, said it was 'closely monitoring' developments in the UK and urged the government to 're-evaluate' its policies in the coming weeks.

Despite the criticism and market turmoil, the government had insisted the tax cuts outlined in the Growth Plan are the 'right plan.' The Treasury has also now announced a date when the Chancellor will set out details of his Medium-Term Fiscal Plan. Mr Kwarteng will deliver his next fiscal statement on 23 November and this time it will be accompanied by growth and borrowing forecasts produced by the Office for Budget Responsibility (OBR).



Bank under rate hike pressure

Despite increasing its benchmark interest rate for the seventh meeting in a row, the Bank of England's (BoE's) Monetary Policy Committee (MPC) remains under intense pressure to further raise rates.

At its latest meeting, the MPC voted by a 5-4 majority to hike the Bank Rate by 0.5 percentage points to 2.25%. Among the dissenting voices, three were in favour of raising rates by a larger amount of 0.75 percentage points, while the other would have preferred a smaller quarter-point rise.

When announcing its decision on 22 September, the MPC once again expressed a readiness to implement further rate rises as required. Specifically, the minutes to the meeting stated that, 'Should the outlook suggest more persistent inflationary pressures, including from stronger demand, the Committee will respond forcefully, as necessary.'

The MPC's next policy announcement is scheduled for 3 November, but some analysts have warned the Bank may need to act sooner following the sharp decline in the value of sterling in the aftermath of the Growth Plan. On 26 September, the BoE responded to this speculation by saying it 'will not hesitate' to raise interest rates if needed and that it was monitoring markets 'very closely.'

Speaking at the International Monetary Policy Forum the following day, the Bank's Chief Economist Huw Pill reiterated this position. Mr Pill said he had concluded that "the combination of fiscal announcements that we've seen will act as a stimulus" before adding that this will require "a significant monetary policy response."

The Bank is clearly under intense pressure to act decisively, either before or following the MPC's next scheduled meeting. Money markets have already fully priced in a one percentage point increase in the Bank Rate to 3.25% at the November meeting and analysts have suggested rates could potentially hit 5.5% or even higher by next spring.

September was a challenging month for global stock markets, which largely closed the month in negative territory as global recessionary fears intensified.

In the UK, the Prime Minister and Chancellor met with the OBR on 30 September, in a move widely seen as an attempt to reassure financial markets following a challenging week, which saw an abrupt policy shift by the BoE to restart bond purchases.

Positive data released by the Office for National Statistics (ONS) on the last day of the month showed UK economic output increased by 0.2% in Q2, revised up from a previous reading of -0.1%. European markets responded positively on the last day of Q3. The FTSE 100 edged up by 12.22 points on the final day of trading to 6,893.81, the blue-chip index closed the month down over 5%. The midcap-focused FTSE 250 and the AIM registered losses of 9.94% and 8.65% respectively in September. The Euro Stoxx 50 closed the month down 5.66%.

US stocks recorded another week of losses in a downbeat end to the month and quarter. The Dow closed the month down 8.84% on 28,725.51. The tech-heavy Nasdaq closed September on 10,575.62, down 10.50%. In Japan, the Nikkei 225 closed September on 25,937.21, down 7.67%.

On 30 September, sterling managed a rebound, edging back up to the levels seen before the Chancellor unveiled his Growth Plan.

Index	Value (30/09/22)	% Movement (since 31/08/22)
 FTSE 100	6,893.81	▼ -5.36%
 FTSE 250	17,168.34	▼ -9.94%
 FTSE AIM	806.38	▼ -8.65%
 EURO STOXX 50	3,318.20	▼ -5.66%
 NASDAQ COMPOSITE	10,575.62	▼ -10.50%
 DOW JONES	28,725.51	▼ -8.84%
 NIKKEI 225	25,937.21	▼ -7.67%

On the foreign exchanges, the euro closed at €1.13 against sterling. The US dollar closed the month at \$1.11 against sterling and at \$0.97 against the euro.

Brent Crude closed the month trading at around \$85 a barrel, a drop of 10.16%, as recessionary concerns weigh, and the impact on demand is considered. Gold is currently trading at around \$1,670 a troy ounce, a loss of 2.57% on the month.

UK inflation dips slightly

While the latest official figures did report a small decline in consumer price growth and the government's energy price cap is set to reduce the anticipated peak, economists still believe inflation could be relatively slow to fall back from current elevated levels.

Data released last month by ONS revealed that UK consumer price inflation eased for the first time in almost a year. A decline in petrol and diesel prices saw the headline rate dip to 9.9% in August, down from 10.1% in the previous month.

The government's decision to introduce its Energy Price Guarantee has also limited the impact of October's rise in household energy bills. The decision means typical bills will now rise by around 25% rather than 80% and, as a result, will thereby reduce the anticipated peak in the rate of inflation.

According to updated forecasts released by the BoE, inflation is now expected to reach a high of just under 11% in October, significantly below the 13% figure predicted prior to the energy price cap announcement. However, the Bank also said it then expects inflation to remain above 10% 'over the following few months' before it starts to fall back.

Signs that jobs boom is fading

Although the latest set of employment statistics did reveal that unemployment fell to its lowest level since 1974, experts have warned that the UK labour market might be starting to turn.

Figures released last month by ONS showed that the unemployment rate across the May-July period dropped to 3.6%, a 0.2 percentage point decrease compared to February-April's figure. The data, however, also showed that the decline was mostly due to a fall in the size of the workforce, with the number of people no longer looking for work hitting a five-year high.

The latest update also revealed a fall in both the employment rate and job vacancies. The employment rate in the three months to July slipped to 75.4%, 0.2 percentage points lower than in the previous three-month period, while the total number of job vacancies, although still historically high, fell by 34,000 during the June-August period, the largest decline in two years.

Survey evidence released last month by the Recruitment and Employment Confederation (REC) also highlighted a slowdown in hiring, reflecting greater economic uncertainty, rising costs and candidate shortages. Commenting on the findings, REC Chief Executive Neil Carberry suggested "the post-pandemic jobs rush is now abating."

All details are correct at the time of writing (03 Oct 2022).

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