



## BLEAK OUTLOOK FROM THE BANK OF ENGLAND INCREASES PROBLEMS FOR NEXT PM

This week we heard the Bank of England forecast a deep recession, runaway inflation and the standard of living being eroded at an alarming rate. In January the bank was predicting inflation of more than 6% and saying gradual interest rate rises would be able to tame inflation and sidestep a recession. The aim was to end up with neither inflation nor recession but we're ending up with both. Back then Governor Andrew Bailey was talking about the squeeze on the cost of living to providing a way of easing inflationary pressures. He should be careful what he wishes for.

The headlines were all about inflation topping 13% and of a recession lasting through to the end of next year. But it is the forecast of an average real terms drop in income of 5% which should be alarming the next prospective residents of 10 and 11 Downing Street as nothing gets a politician voted out of office quite like a sharp fall in the standard of living in their electorate. At the last election Boris Johnson campaigned on the promise of 'levelling up' but the economy has ended up being flattened.

### THE MARKETS THIS WEEK

| FTSE 100 | S&P 500 | Nikkei 225 | MSCI Europe | Hang Seng | US 10 Yr | UK 10 Yr | Brent Crude | Gold   | Iron Ore | GBP USD |
|----------|---------|------------|-------------|-----------|----------|----------|-------------|--------|----------|---------|
| +0.33%   | +0.52%  | +0.47%     | +0.41%      | +0.23%    | +0.03%   | -0.03%   | -12.60%     | +1.49% | -1.28%   | -0.48%  |

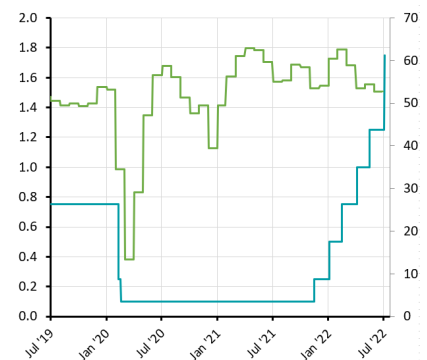


#### UK: BANK OF ENGLAND OPTS FOR BIGGEST HIKE IN 30 YEARS

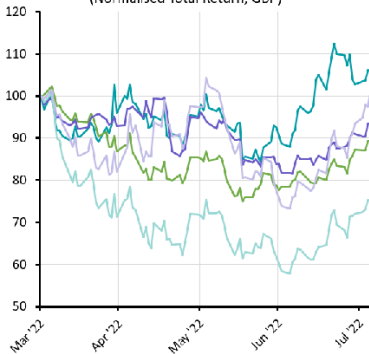
The Bank of England raised rates by 0.5% as it warned it expects inflation to keep rising. The interest rate hike was in line with expectations after Governor Bailey commented on the prospect. However, the upgrade to inflation forecasts was accompanied by a warning of imminent recession which sent the yield on 10-year gilts down sharply as investors looked to safety of government bonds amid the pending slowdown. The bank expects inflation to exceed 13% by year end, driven by the latest increase in natural gas, and to remain high next year before returning to its 2% target in 2024.

The squeeze on living standards is expected to contribute to a recession which the bank predicts will begin in Q4 this year and last throughout 2023. The latest PMI figures show that services and manufacturing output is already dropping sharply. The prime ministerial candidates tried to use the decision to boost their campaigns. Truss promised to overhaul Bank's inflation target while Sunak suggested more government borrowing would be wrong.

Bank of England Base Rate (% LHS) and CIPS PMI - UK Service Sector (RHS)



Qualcomm, Broadcom, AMD, NVIDIA, and the NASDAQ (Normalised Total Return, GBP)



#### CHINA: MARKETS NERVOUS AS TENSIONS OVER TAIWAN RISE

There was more volatility in Chinese equity markets this week as tensions over Taiwan's status intensified following US speaker Nancy Pelosi's visit. After its attempts to prevent Pelosi's visit didn't work, China launched a huge demonstration of its military and naval capability in an attempt to assert authority over its neighbour. The Shanghai Composite Index dropped 3% at the start of the week as political tensions rose.

The economic struggle between the US and China continues in other areas too. Alibaba recently became the latest company to be put on notice of delisting in the US if it fails to meet US audit regulations. Alibaba joins Yum China, Baidu and Weibo on the long list of companies under threat of removal. Joe Biden has also recently signed the CHIPS and Science Act which promises investment of up to \$52bn and tax breaks of up to \$25bn to encourage micro chip research and manufacture in the US. Among the rules for qualifying for the benefits is a ban on significant investment in foreign countries such as China.

Natural Gas Spot NYMEX (LHS, \$/Mmbtu) and Brent Crude (\$/bbl, RHS)



#### OIL: BP REPORTS RECORD PROFITS AS OPEC TWEAKS PRODUCTION TARGET

BP is the latest energy company to announce bumper profits as it reaped the benefit of high oil and gas prices. BP's underlying profits for Q2 jumped to \$8.5bn, more than three times its profits for the same quarter in 2021. Last week Shell reported record profits of \$11.5bn. This comes in the same week as warnings that UK energy bills are set to rise higher than expected and remain high for longer with Cornwall Insight predicting average domestic energy bills will remain above £3,000 a year until 2024. The Bank of England also warned that high energy costs are eroding living standards.

The latest meeting of the OPEC+ cartel of oil producing countries announced a slight increase in its production target as it remains under intense pressure to pump more oil to dampen down prices. The group agreed to increase planned production by 100,000 barrels a day, or 0.1% of total production. The price of oil has fallen more than 6% this week as some data points to a drop in consumer demand.

Data Sourced from FE Analytics, the IMF and FactSet

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