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Heartwood Investment Management

Investment Insight

Weekly Insight

Gloomy UK growth forecasts confirm our caution

Chancellor Hammond's latest budget was generally unexciting and, arguably aimed at placating Westminster. Importantly, though, the budget marked a step away from austerity and did not deliver the usual 'bad news' coming from a newly-elected government. In this respect, the current government has little room for manoeuvre given its razor thin majority.

Over the next five years, the UK economy can expect to see an overall net loosening of £25 billion. The biggest fiscal stimulus will come in 2019/2020, during which time stimulus will amount to nearly £10 billion or 0.5% of GDP. More money will be made available for the NHS, first-time buyers and rail travellers, as well as funding to help ease the introduction of the universal credit. The timing of this stimulus coincides with the UK's departure from the European Union and is probably being offered to help offset some of the 'Brexit pain'. One highlight is that £3 billion is being set aside for Brexit preparations, although the details have yet to be specified.

The slower pace of austerity comes as UK growth forecasts have been revised lower, mainly resulting from downgrades to UK productivity. Since the financial crisis in 2008, the UK economy has made little headway in advancing productivity growth, particularly compared with the exponential rate of productivity growth experienced between 1999 and 2007. This is not just a UK phenomenon, of course, but the productivity conundrum presents challenges for policymakers across developed economies. For the UK, though, the consequences of these economic downgrades will mean higher borrowing over the forecast period.

Public sector net debt is currently just under 87% of GDP – levels that have not been seen since the mid-1960s. Net borrowing, meanwhile, is just under 3% of GDP having fallen significantly from 10% at the height of the fiscal debt crisis in 2009. Chancellor Hammond does not plan to balance the books in the current Parliament, although he is expected to meet the fiscal rules of reducing the structural deficit to below 2% of GDP by 2020-2021 and lowering overall levels of net debt to GDP. Much will depend on the resilience of the UK economy against an increasingly uncertain political backdrop.

And all of this confirms our cautious stance in UK assets. We have no plans to repatriate assets back to the UK any time soon, having taken a long-standing underweight stance in UK equities and UK property. In equity, most of our exposure to UK indices is via large-capitalisation companies listed in the UK but operating principally overseas. Moreover, the UK's weak economic fundamentals relative to other developed evonomies keeps us holding a short duration position in UK gilts, as well as overweight positions in the US dollar and the euro.

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Clear Thinking

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To find out more about the Heartwood strategies, visit our website or contact your local representative.

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