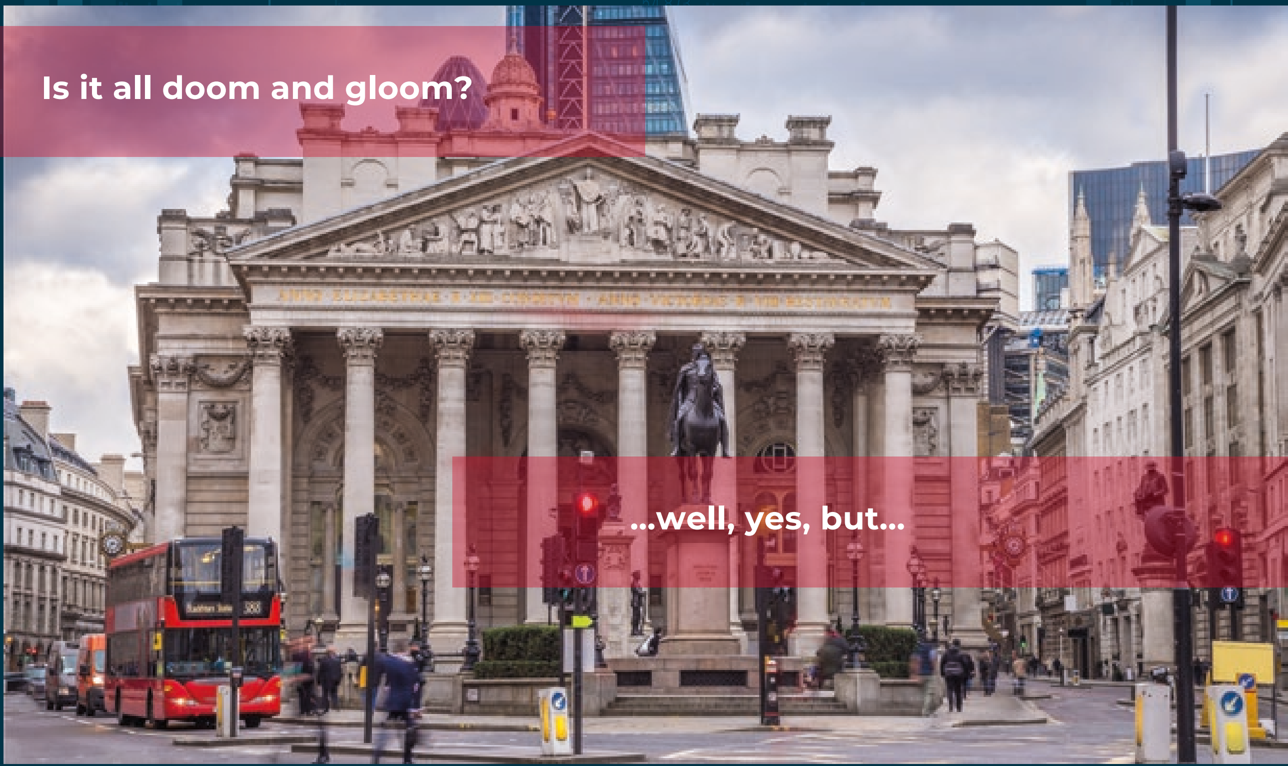
RECESSION, INFLATION, AND RISING INTEREST RATES

August 2022



With the Bank of England announcing the biggest interest rate hike in 27 years and forecasting that Britain will enter a year-long recession with inflation topping 13%, you could be forgiven for feeling a little gloomy about things.

Granted, the picture that was painted at the last Monetary Policy Committee (MPC) meeting isn't a pretty one.

Take mortgages as an example. Interest rates are now at their highest level in the UK since 2008, just after the financial crash. Although most mortgages in the UK are fixed (around three quarters of all mortgages in the UK) that won't always be the case; once already stretched households look to re-mortgage, the prospect of paying a larger proportion of household income on a monthly mortgage payment will cause many to tighten their belts even further than they have recently been forced to do, due to the cost-of-living crisis. Then there are the many homeowners already sitting on variable rate mortgages which are about to make them poorer each month as those monthly payments rise.

These increased borrowing costs mean that the UK is more likely to fall into a recession (the term used when there is negative growth within the economy for two consecutive quarters of the year) which, according to the Bank of England, could last as long as the 2008 financial crisis (which was five quarters).

Throw into the mix the huge rise in energy prices, with more to come in the Autumn, and a shortage of supply to meet the demand for goods now that COVID restrictions are being eased globally, it makes for an unpleasant tasting cocktail for many over the next year or so.

With all that said...

There are chinks of light.

Firstly, we need to remember that economic downturns are a part of life. Economies breathe in and out, they are living things and will at times test us, but history tells us they have always recovered. Equally, markets rise and fall - they never go up in a straight line but when there is a downturn, it is followed by a period of expansion. We wrote about it in a recent blog called What We Learn from History.

We also need to look for opportunities when allocating capital. There are opportunities to protect oneself from a downturn; defensive positing, allocating capital to traditional safe havens such as gold and the US Dollar, looking to invest in well-capitalised companies paying a regular dividend stream etc. We wrote about that too in a recent blog called Market Thoughts.

What Next?

The most important thing to do is to have a methodical plan and revisit that plan with a Financial Adviser, regularly.

The next few months, possibly years, will be difficult for many, but it is important to be calm, disciplined and diversified in one's investment approach.

As Rudyard Kipling wrote,

if you can keep your head when all about you are losing theirs....

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