State of Play

Not all is what it seems

18 January 2024

By the time you read this week's edition of the State of Play, what is often described as the most depressing day of the year, so called 'Blue Monday', this year falling on 15 January, will have passed.

Reasons to remain optimistic

If it weren't for the fact that the concept of Blue Monday is in fact a myth, conjured up by the marketeers of a travel company aiming to tempt us Christmas weary, cold, tired and broke consumers into booking a summer holiday, then its passing would surely be cause for cheer.

There are of course more genuine reasons to remain optimistic, look hard enough and the promise of lighter evenings and warmer days lies ahead. We can also look to the recent positive economic data, such as the stronger than expected 216k jobs created in the US versus the forecast 173K (US Non-Farm Payrolls), and UK GDP figures showing the UK economy expanded 0.3% year on year in Q3 2023, pointing to the robustness of economic growth both at home and across the pond. On most investors radars, the prospect of interest rate cuts will loom large. The much-awaited pivot in monetary policy by central banks, which is very much a case of when and not if, is providing a supportive environment for both shares and bonds. This further adds weight to the case for patience in, and the benefits of, long-term investing.

Cause for concern

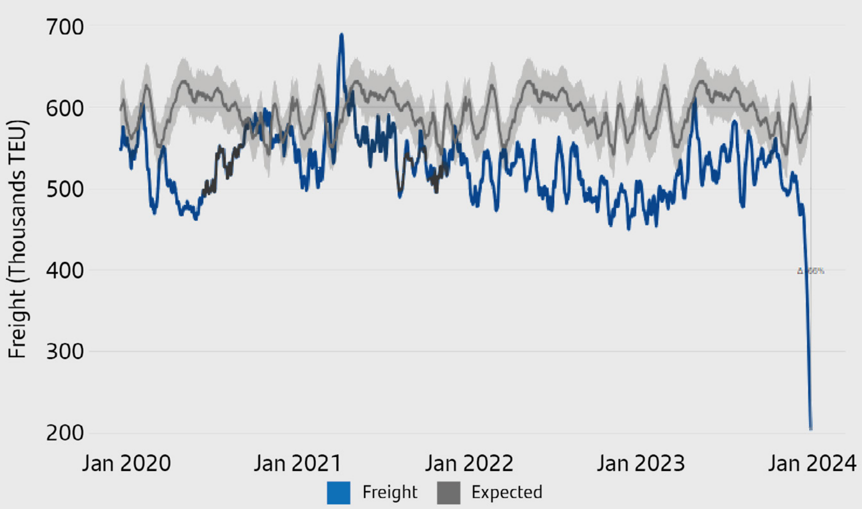
However, we must and should remain alert to events that could disrupt this positive momentum. Here we must turn our attention to last week's events in the Red Sea, which saw US and UK military strikes on Houthi rebel positions within Lebanon.

These strikes follow an increase in attacks on global shipping within the region and raise the following questions about the potential that this escalation of tensions in the Middle East has to disrupt global supply chains by forcing shipping to take longer and more expensive routes, raising the oil price, fuelling higher inflation and impacting the central bank's ability to cut rates.

It is important, while tensions run high, to look at the facts in determining just how disruptive such events could be. For example, the UK imports most of its oil from the US and Norway. While the price of Brent crude increased 2% to just over $80 per barrel following the US and UK military strikes , it has at the time of writing (15 January) fallen back to $77 per barrel.[2]

The inevitable detour now being taken by ships as they look to avoid the Red Sea is significant, dropping by more than half in December and below 70% of usual January volumes (graph below is the latest data published by the Kiel Institute for the World Economy).

Daily freight capacity, Red Sea



Source: Kiel Institute for the World Economy. Data as at January 2023.

This raises the prospect of increased shipping costs, delays in the delivery of supplies and concerns about subsequent higher prices and inflation. While it is true that shipping container costs from China to Northern Europe have increased from $1,500 to more than $4,000 they remain significantly below the $14,000 reached during the height of the pandemic.[3]

So, what are the prospects of these delays and increased shipping costs acting as an anchor on the more positive recent economic growth data?

The answer depends on how long this conflict lasts. In the short term, let's say over 1-2 months, it's unlikely to have much, if any, of a negative impact on increasing costs of goods and inflation. But if it drags on for 6 months or more, then the consensus suggests it could be a different matter, one we will keep a close eye on as the situation evolves.

One truism remains, and that is that evidence matters. We know that Blue Monday is nothing but an artificial construct with no scientific proof behind it, and it's important that we take the same evidence-led approach in trying to understand and determine the economic impact of events such as those currently playing out in the Middle East.

We will of course return to this subject as required, but in the meantime, remember that there are still reasons to remain optimistic, especially if you have recently booked your summer holiday.

Note: Data as at 18 January 2024.

[1] Statista, 8 January 2024
[2] Trading economics, 15 January 2024
[3] Kiel Institute for the World Economy, 11 January 2024

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