State of Play

17 September 2020

Our Investment Specialist, Simon Durling, shares his thoughts in our latest update.

Brexit returns to forefront amidst ongoing COVID-19 developments

Prior to the COVID-19 pandemic, Brexit had dominated our media for over four years, this week we saw it returning to our front pages as the UK Government seeks to pass an Internal Market Bill which could lead to a breach of the Withdrawal Agreement sparking a backlash from the European Union (EU) and many politicians on all sides.

As the clock ticks closer to the end of the transition period on 31 December 2020, Prime Minister Boris Johnson, laid down the gauntlet to the EU in the negotiating process by passing an Internal Market Bill in Parliament at the second reading on Monday evening with a majority of 77, despite a number of Conservative Members of Parliament either abstaining or voting against. Initially, this legislation wasn't overly controversial, however this changed when new clauses were added by ministers just before it was published. The clauses would give the UK Government powers to override parts of the Withdrawal Agreement that was signed and passed into UK law on 23 January 2020.

The legal framework and rules relating to Northern Ireland and the EU border with the South, have been the greatest challenge throughout the negotiation process since the 2016 EU Referendum vote. The UK Government and the EU have been working through which products passing between the UK mainland and Northern Ireland would need custom checks and paperwork completed ever since the Withdrawal Agreement was signed off, in an attempt to protect the Good Friday Agreement - which stipulates that the border between the North and South remain open, and without checks.

The Prime Minister has complained that the EU has threatened to impose trade barriers between Northern Ireland and the rest of the UK mainland, and impose a food blockade - steps he said threatened the United Kingdom's unity. 'The EU still have not taken this revolver off the table' Prime Minister Boris Johnson told UK Parliament before the vote. 'What we cannot do now is tolerate a situation where our EU counterparts seriously believe that they have the power to break up our country'. After reacting at first with anger, EU officials have tempered their language in the last few days, identifying the move by the UK as a way to create leverage in the negotiations. And despite the UK Government's provocative move, trade negotiations have been making reasonable progress in recent weeks. It is a distinct possibility that when the two sides meet again next week a mutually acceptable deal may be on the table. In those circumstances the Prime Minister Boris Johnson is expected to drop the clauses from the Internal Market Bill before it even reaches the statute book.

In other news, the UK Government is coming under increasing scrutiny for the lack of COVID-19 tests being available to those who need it. The Health Secretary, Matt Hancock, has said the system faces an 'enormous challenge' and that it would take 'a matter of weeks' to rectify the problems. As schools reopen and many return to offices, an increase in demand for tests has placed a huge burden on virus hotspots leading to many having to travel long distances in order to be tested. In addition, there have been long backlogs in getting test results as some of the laboratories have run out of testing kits or are struggling with recruiting enough staff, as some of their senior staff return to teach at universities and the temporary student employees restart their degree courses.

Care home leaders have accused ministers of failing to deliver on the promise to prioritise the sector, amid testing delays and fear that there could be a rush on Personal Protective Equipment before the winter. In July, the UK Government announced that testing would be introduced across the adult social care sector to enable screening of staff every seven days and residents every four weeks. However, industry leaders say that the failure of couriers to pick up samples in time and a backlog at testing laboratories has led to the waiting time doubling for results in some areas. Care homes are increasingly worried that the problems in testing may result in outbreaks which were devastating at the height of the national lockdown. Around 220,000 tests are processed each day, according to UK Government figures released last week, with a testing capacity of more than 350,000 (which includes swab tests and antibody tests). The aim is to increase that to 500,000 a day by the end of October 2020.

Latest economic news

According to the Office for National Statistics (ONS) the unemployment rate increased to 4.1% in the three months to July. This is in line with expectations but hides a much more complex picture when you study some of the other statistics within their data released. Firstly, the previous estimate from the ONS had indicated a sharp fall in the payroll numbers between March and July. This has been revised significantly following more detailed data analysis. The ONS said its figures might be 'slightly impacted' by a change in the way it interviews households since the

start of the COVID-19 pandemic. The surveys, which now rely on telephone calls rather than face-to-face interviews, over-represent homeowners who are less at risk of unemployment. The data from search engines from people using the word 'redundancy' in the search box has surged to a record number in July - pointing to a gloomy outlook for further job losses this autumn. Redundancies increased by 48,000 on the quarter to the end of July to a total 156,000, the biggest rise in 10 years. Separate tax office data showed the number of staff on company payrolls fell by a monthly 36,000 in August.

The Bank of England has forecast that the unemployment rate will hit 7.5% at the end of this year, when it is expected to expand its bond-buying stimulus programme again. Young people were particularly hard hit, with those aged 16 to 24 suffering the biggest drop in employment compared with other age groups. The number of job vacancies rose to 434,000 in the three months to August, about 30% higher than in the April-June period but almost half their level before the crisis began. The Chancellor of the Exchequer, Rishi Sunak, is under increasing pressure to extend the furlough scheme which is due to finish at the end of October. The expectation is that about six to eight weeks after the scheme ends the employment data will significantly worsen as the measurement only includes those who have been out of work for four weeks and have been actively seeking work for at least two weeks.

Small businesses are cautiously optimistic after the High Court has found in favour of policyholders in a dispute on the claims made against their business interruption insurance policies which many insurers refused to pay out in the wake of the COVID-19 pandemic. The landmark test case was brought by the Financial Conduct Authority to help work out which policies should be honoured, given the unprecedented impact of the virus outbreak and subsequent lockdowns. In a judgement handed down on 15 September, Lord Justice Flaux and Mr Justice Butcher found in favour of policyholders in a number of areas that could mean tens of thousands of businesses are in line for pay outs. There are approximately 370,000 policies in the UK across a vast range of sectors. The judgement considered 21 example policy wordings. While different conclusions were reached for each, the court found in favour of a number of key issues. These included 'notifiable disease' clauses in policies, which appeared to offer cover for pandemics even though many insurers refused to pay out. Most, but not all, of the disease clauses considered provide cover, the court found. Certain 'denial of access' clauses which appeared to offer cover for forced closure of companies should also pay out. The case is expected to be appealed and lawyers have said that it may jump straight to the Supreme Court, the highest UK court, in order to reduce the time delay as many businesses struggle for survival.

Market update

Global markets recovered some of their composure over the last week after the dramatic falls seen in previous weeks, particuarly affecting the technology sector. Encouraging data from China and the US provided some reassurance but momentum is lacking until markets hear the latest updates from central banks, including the US Federal Reserve which is due to report on the state of the US economy.

Many are asking the question about the long-term impacts on the structure of our economy post COVID-19. Two stories this week which I think paint the potentially different path are Ocado's change in partner and New Look's latest deal.

Ocado has been in a long-term business relationship with Waitrose since 2002, offering a delivery service for its grocery's. It has grown substantially since then as the migration over to online grocery shopping has gradually changed the shopping habits of millions of consumers. On 1 September 2019, Waitrose sold its 50% stake in Ocado's retail business to Marks and Spencer (M&S) for £750m and now offers its own online delivery service. Ocado reported that the change over to M&S has proved to be a big hit with shoppers. Shoppers are buying more M&S groceries on Ocado than they did Waitrose products, the online grocer claimed yesterday as it reported a 52% rise in sales. The deal with Ocado is crucial to M&S as it invests in the business and moves with the digital revolution, which has been a higher priority since the crisis struck back in March. After overcoming initial teething problems, as the service was swamped in the first week of launch, the results are an impressive start to the new relationship in the new normal. The online retailer, which delivers 350,000 orders a week, said that it planned to add 40% more capacity next year by building three robotic warehouses in Bristol, Essex and Hampshire. Its shares closed up 253p, or 10.7%, at £26.08 on Tuesday's close. In a sign of our new normal, Ocado is now worth nine times the market value of M&S at £18.5bn versus £2.1bn.

As many retail businesses struggled through the lockdowns, in what has been a beleaguered sector even before the crisis, most approached their landlords for a rent holiday to help them survive the period they were forced to close and the subsequent drop in shoppers once restrictions were lifted. New Look reached a deal yesterday which may reshape how retailers navigate the stormy waters ahead. The struggling fashion chain said yesterday that its Company Voluntary Arrangement (CVA) had been voted through by 75% of its creditors, despite fears that the company's survival was potentially doomed amid warnings from the UK's biggest property owners that they would veto the plan. The British Property Federation is horrified, as the implications for other such deals may prove to be a significant blow to future returns in the sector. The CVA includes landlords accepting no rent on 68 shops and as little as 2% of turnover on 402 shops. Boohoo, the online fashion retailer, had been waiting patiently in case the CVA failed as part of its plans to add to its growing stable of former bricks-and-mortar retailers, which already includes Warehouse, Coast, Karen Millen and Oasis. However, a sale to Boohoo inevitably would result in the immediate closure of all 500 of New Look's shops and the loss of 11,200 jobs.

Find out more

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Note: Data as at 16 September 2020.

Important Information