11 March 2020
For Client Use

Investment Event
UK: A coordinated policy response

Amid ongoing challenges facing the UK economy due to the COVID-19 outbreak, The Bank of England has announced an emergency package of measures ahead of the UK Budget

These combined measures should help counter cash flow problems likely to be faced by many UK businesses and households in the coming months, whilst also supporting demand in the economy

Our views

Ongoing action of this nature by global policymakers and increasingly favourable valuations for risky asset classes means we remain comfortable with our moderate pro-risk investment strategy. Nevertheless, building portfolio resilience against downside scenarios remains important

Bank of England cuts rates at emergency meeting…

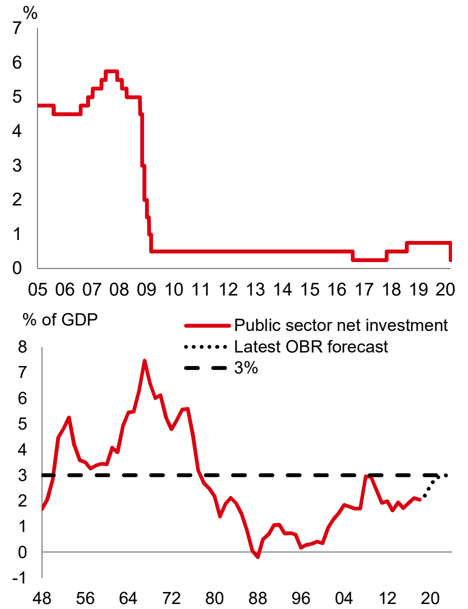
Amid increasing challenges to the UK growth outlook and financial market turmoil on the back of the global COVID-19 outbreak, early on 11 March the Bank of England (BoE) announced an **emergency 50 basis point** (bp) cut to the benchmark UK policy rate (also known as "Bank Rate"), down from 0.75% to 0.25%. This takes Bank Rate back to the record low reached in the immediate aftermath of the UK referendum on EU membership in 2016 (Figure 1).

The surprise move was the BoE's first emergency rate cut since October 2008, during the global financial crisis, and comes a week after a similar move by the US Federal Reserve, with other global central banks and governments having announced stimulus measures in the meantime.

The Bank of England also announced a new "Term Funding Scheme". In effect this provides **cheap loans to UK banks** tied to Bank Rate, with the aim of boosting banks' lending to the real economy. Additional funding will be made available to banks that lend to small and medium-sized enterprises (SMEs).

To provide more room for banks to lend, the BoE also **cut the "counter-cyclical" capital buffer** required for banks to 0%, which means banks are no longer required to build up an additional cushion of capital with which to absorb potential losses.

Figures 1 & 2: UK Bank Rate, and UK net investment



Source: Macrobond, Office for Budget Responsibility (OBR), Data as at 11 March 2020.

…ahead of the UK budget

The BoE's actions came a few hours before the UK Budget, highlighting the **"coordinated" nature of the policy response**.

UK Chancellor Rishi Sunak announced a stimulus package worth around GBP30bn (1.4% of GDP) including measures to tackle the challenges COVID-19 presents to the UK economy.

This will include around GBP7bn to support businesses, self-employed and vulnerable individuals, and GBP5bn to support the National Health Service (NHS). Among other various measures to boost day-to-day spending over the rest of this parliament's term, the government is also planning a significant increase in infrastructure spending, which is expected to rise toward 3% of GDP over the coming years (Figure 2).

Investments, annuity and insurance products

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Market considerations

The package of measures announced should help counter cash flow problems likely to be faced by many UK businesses and households in the coming months, whilst also supporting demand in the economy. It may also mark the start of a trend at the global level towards greater fiscal and monetary policy coordination.

Given the significant downside risks to UK growth, there is a good chance that further stimulus will be required this year. Indeed, the Bank of England believes it has only used up “roughly half” of its available policy space with these measures, while Chancellor Sunak has signalled he may loosen the existing fiscal rules that require a balanced day-to-day budget by 2023.

Overall, ongoing action of this nature by global policymakers and increasingly favourable valuations for risky asset classes (particularly UK) means we remain comfortable with our moderate pro-risk investment strategy. Nevertheless, high uncertainty over the outlook, and a risk that policymakers in some jurisdictions may be relatively slow to react, means we are also still focussed on incorporating asset classes that help build up the resilience of our portfolios against downside scenarios. We continue to monitor developments at the global level very closely.

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