Weekly Digest

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Fast Lane, Slow Lane

A few years ago, I was on holiday in Malta. If you've never been there, you might not know that the roads are pretty much entirely single lane, single carriageway, and sufficiently winding in most places to make overtaking impossible. Although it's not very far from one end of Malta to the other – about 30km – the time it takes to make the journey is very much dependent upon the speed of the slowest driver on the road. And I can tell you that the Maltese are generally not people in a hurry. I named this the "slowest common denominator" problem. Is it possible that we are going to witness similar hold-ups on the road to post-COVID normalisation?

Last week I highlighted some research illustrating how difficult it would be to reach herd immunity in countries where the highly infectious Delta variant is prominent, with the hurdle being potentially as high as a 90% vaccination rate, at least in the absence of non-pharmaceutical interventions (NPIs). Funnily enough, Malta is the only country that is anywhere near that number, with 80.4% having received one dose, and 60.7% having had two, but the rates drop off pretty quickly after that. Israel is also high on the list, but it is notable that Israel's vaccination rate has tailed off sharply after a very strong initial rollout. There the respective figures are 64% and 59.5%.

There are various factors at play in Israel, including some (possibly self-inflicted) supply issues, difficulties accessing more remote citizens, and, critically, vaccine hesitancy, whether on ethical, religious, medical or fear-of-side-effects grounds. While cranking up supplies (and supplying them as aid packages if required), and tracking down hermits in caves (who probably constitute a limited risk to society anyway) are things that money and patience can deal with, the latter factor, vaccine hesitancy, could well be the biggest obstacle to get past. It will be most informative to see how vaccination curves in leading countries such as the UK and US develop once the rate moves beyond 60%.

Even as I am writing this the story is progressing. Fear of the Delta variant has prompted Hong Kong to ban flights from the UK. Malta (when was the last time Malta had three mentions in an investment commentary?) is requiring tourists from the UK to have proof of vaccination, and Spain and Portugal are tightening entry requirements as well.

Greece, which remains open for business, is going further down the self-protection route by offering 18-25 year-olds €150 in cash and a month's free mobile data. In the US we have seen everything from $1 million lotteries to free doughnuts, beer and even cannabis. If one were cynical, you might think some people are waiting for these incentives before rolling up their sleeves for a jab.

Humanity's enduring inability to make proper risk assessments remains a problem. In Singapore, a group of doctors wrote to the government asking them to ban mRNA vaccines on the basis of the case of a thirteen year-old boy who died of heart failure in the US after being given his first dose, although no direct link has been proved. As it happens, the Singapore health ministry did not acquiesce, but it does show the pressure that authorities could come under – and we have already seen plenty of stop/start with the AstraZeneca vaccine.

Then, of course, it's also important which vaccine you are getting. Some are more effective than others. China's Sinopharm vaccine is one of the less effective, and that is the one mainly being used in the United Arab Emirates. The UAE has a 71% full vaccination rate, one of the highest, but is still seeing a pick-up in cases. However, it also says that unvaccinated people account for 94% of deaths, 92% of intensive care admission, 89% of hospitalisations and 84% of reported cases.

Finally, on this topic, down to Australia, which is currently experiencing a pick-up in cases, although at least from a very low base. What does one make of the fact that one cluster is attributed to an unvaccinated driver who was ferrying incoming travellers from the airport to a quarantine hotel? There is certainly no herd immunity in Australia, where currently only 30% of the population has had one dose, and just 5% the double. New Zealand is also well below 10% on the latter measure. Don't expect to be travelling there any time soon.

The point of all these figures is to illustrate that every country is moving at a different speed. I guess that at least we have something of a multi-lane highway, and so the faster countries are not limited domestically by the slow pace of others. But it does mean that borders will be slower to open, and also that countries with lower vaccination rates could be responsible for creating more bottlenecks in global supply chains. For example, we have recently seen more disruption in certain Chinese ports owing to localised lockdowns – China is 15% double-vaccinated, but with the less effective Sinopharm vaccine.

And these are uncertainties emanating purely from COVID. Additionally we continue to have to consider numerous other influences: the potential longer-term inflationary effects; the impact of fiscal packages such as last week's agreed infrastructure spending plan in the US; the reaction function of central banks, to name but a few. While equities remain our preferred asset class in most situations, and certainly for the longer term, it remains difficult to have sufficient confidence to be overweight relative to strategic asset allocation benchmarks. At the same time, economic and corporate profit growth that looks set to continue above trend should provide support, even if monetary conditions will be gradually tightened.

At last week's meeting of our Asset Allocation Committee, we summed up the current position as follows: "We can continue to take a useful cue from market-derived inflation expectations, and these are relatively encouraging. Two-year breakeven rates remain the highest part of the forward curve, suggesting that the market also supports the "transitory" narrative put forward by the Fed. But it is fair to say that

expectations are not set in stone, as the movements in the curve over the last year demonstrate. AAC believes there is a non-negligible risk that higher-than-expected CPI prints will persist for longer than the market will be comfortable with, and that an “inflation flinch” is a real possibility. This would trigger a new upward shift in bond yields, with the higher discount rate (and fears of tighter policy) weighing on risk assets. However, the lack of real return available from non-equity assets (notably government bonds and cash) continues to make it very difficult to recommend a pre-emptive equity underweight position, especially as there is no economic recession expected within our 18-month forecast horizon, and enduring equity and credit drawdowns tend to be associated with recessions. Tactically, the AAC is more likely to increase equity exposure to take advantage of any future potential drawdown triggered by an inflation scare (assuming that we continue to believe it to be temporary).”

Last week's Economic Highlights

FTSE 100 Weekly Winners

Anglo American plc	9.2%
JD Sports Fashion Plc	8.6%
Ashtead Group plc	8.1%
BHP Group Plc	7.2%
Royal Dutch Shell Plc Class B	6.4%
British Land Company PLC	6.1%
Glencore plc	5.9%

FTSE 100 Weekly Losers

International Consolidated Airlines Group SA	-5.7%
Phoenix Group Holdings plc	-3.9%
Vodafone Group Plc	-3.7%
Informa Plc	-3.5%
United Utilities Group PLC	-2.7%
M&G Plc	-2.4%
Compass Group PLC	-2.3%

FTSE 100 Index, Past 12 months

Source: Factset

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