## Warner Matthews Diaries – First Quarter 2021

### Asset Allocation Musings:

With the festivities over and a chance to reflect on the somber end to 2020, your scribe was curious as to how the music industry has evolved since his teenage years. Back then the chances of gaining the coveted top spot in the charts on Christmas Day could provide a band or singer with a recurring revenue stream that would embarrass even the most generous final salary pension annuity. It is hard to exactly determine the true value of a Christmas hit as the Performing Rights Society, the organization charged with protecting clients' privacy, prevents this information being made public. However, it is assumed that Slade's *Merry Christmas Everybody* nets £1,000,000 per year, not bad for a song that was sketched out in the lead singers mother's house after a night out on the tiles and completed in one draft…

### Looking Back:

Moving on to matters at hand, it somehow doesn't feel appropriate to expend too much energy on the year just passed. Most of us now know which were the investment winners and losers during the pandemic. What is clear is that Covid-19 comes in waves, but the tides that accompanied it lifted some boats, whilst others were wrecked. Should we therefore get ready for a continued set of Covid tides and prepare ourselves for more bouts of volatility?

Some things have undoubtedly changed for good – employees' work/life balance has been enhanced through the shift to working from home, with 30% of the workforce still exclusively working from home according to recent surveys. Employers are however right to be wary about how to build a business with key employees working remotely, yet with potentially significant reduction in rental costs, the happy medium may well end up being more flexibility for employees. The second derivative impact for the property market should in theory support provincial towns at the expense of regional city centres, surely good for those that have found it hard to step onto the property ladder.

The pandemic also accelerated the shift in shopping habits away from physical stores to online. The polarisation between winners (Amazon) and losers (the High Street) got even more pronounced. How will bricks and mortar operators win back customers? I wonder if I am in a minority that still prefers to try on an item of clothing rather than click a button for instant wardrobe satisfaction. Perhaps the second derivative benefits in this instance are for those artisan retailers that are entwined to the local community through sourcing and selling local products – it's good for the environment and should enhance the feel good factor.

The one area that we find it hard to square the circle is the huge rise in public and corporate debt. In order to rescue the global economy, governments and central banks stepped up to the challenge and opened up the printing presses to avoid a collapse in confidence. The numbers are eye watering. The US has to date committed over $2 trillion in rescue packages; the UK borrowed £394 billion in 2020 pushing national debt above 100 per cent of national income – a metric used by economists to highlight pending warning signals. This appears inconspicuous when interest rates are at near zero per cent, however every 1% rise in interest rates will add £20 billion to the UK's debt pile. We fear that in the end someone will have to pay to clean up the debt burden. Will it be pushed down to the next generation to deal with or will the chancellor begin to implement tax changes in an attempt to realign the UK's debt problem? The second derivative impact in this subject matter being the possible return of inflation. Economic theory implies that inflation allows debt to shrink, but for those with a keen memory, the 1980s inflationary environment created higher prices and eventually higher interest rates. Try telling today's house-buying generation that their mortgage rates may balloon up to double digits just like in the late 1980s and early 1990s.

One final observation of government's noble endeavour to keep the economy ticking over. The various measures to support UK corporates enabled struggling companies to survive, but the downside to this is it increased their debt profiles. The government will need to step back at some point and recoup the loans. Have corporates therefore relied too much on bailouts at the expense of innovation and nimbleness? For cash rich companies however, the future looks more akin to thriving not just surviving….

## Looking Forward:

The start of a new year is a time for reflection, resolution and optimism. Will 2021 be the year we move away from the darkness of the pandemic towards the light of prosperity? Comparisons have been made with the 1920s, so we should surely seize the moment and usher in the Roaring Twenties again. There are reasons to be optimistic. For starters, the rollout of vaccines and mass vaccination programs are under way and will accelerate with each day of lockdown. Britain was the first country to licence the vaccines giving it an important head start. Some of the key vaccines are homegrown showing our capabilities in the field of medicine. The goal is that everyone should have the ability to get vaccinated by March. That should mean that by Easter a certain degree of normality may again prevail.

With a return to the way things were, we know from last summer how quickly the economy rebounded. There is undeniably a lot of pent of demand for all things we have been denied in the last few months. Household savings rates have moved higher and will be put to good use to fuel the recovery. Missed holiday opportunities, dining out with friends, recreational activities will all rebound with gusto. We can use Asia's recovery path as a template for seeing how rapid the rebound can be. China's air travel statistics show that the industry is back to pre-Covid levels.

The Brexit cloud has dissipated as well. It was indeed hard for businesses to plan for the future with the uncertainty over Europe. Whether this is our Carpe Diem or Better the Devil you Know moment, only time will tell. However, for now we have the prospect of being able to operate as we want outside the European Union, perhaps more nimbly. The missing component of previous economic rebounds was improvements in productivity creating sustainable economic growth and higher wages (and better living standards). Could 2021 signal the start of this now that the government's time and resources can be directed more efficiently?

As we have alluded to in previous missives, the prospect of a Green Stimulus package will assist economic growth. That has been reinforced with Biden's US election win late last year. One of his first policies is likely to be to reengage on climate (including rejoining the Paris Climate Agreement), which should entail large fiscal spending packages targeting infrastructure. The UK is likely to follow suit in a smaller fashion, however, the future will no doubt be painted green.

## What's on our Minds – ISA and Pensions

It's that time of the year when the Warner Matthews Team readies themselves for the end of the tax year particulars, namely ISA subscriptions and pension contributions for 2020/21. As you will know, ISAs are "tax free wrappers" where you can place money to earn interest or returns without having to pay the tax man any income or capital gains tax. The maximum subscription is £20,000 for this tax year.

Similarly pension contributions come with attractive tax relief. This tax relief is paid on your pension contributions at the highest rate of income tax you pay, so if you are a higher-rate taxpayer you can claim 40% pension tax relief. In layman terms, as a higher-rate tax payer contributing £100 to your pension, the government will contribute £40 for you, so you the tax-payer need only pay £60. There is a limit of £40,000 for the tax year 2020/21, so any contributions above this will be subject to tax at your marginal rate. You can carry forward unused allowances from the previous three years as long as you were a member of a pension scheme during those years. For anyone not working or earning less than £3,600, the maximum gross contribution is £3,600 (this includes the government top up, so your personal contribution is limited at £2,800).

The deadline for ISA subscription and pension contributions for 2020/21 is 5th April, so don't forget to utilise these tax incentives. If you intend to sell assets to fund ISA or pension contributions, remember there may be a CGT implication, feel free to check with us. You never know, they could be in the firing line for the chancellor's ambition to recoup the money spent to ease the impact of Covid..