

Back to Basics

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It is, perhaps, hard to believe that the 5-year anniversary of the Covid pandemic will occur later this year. The clue is to be found in the number 19 since novel viruses are named after their year of discovery.

The full economic ramifications of that period, bound up as it is with Brexit and the war in Ukraine, will doubtless take decades to unravel. Indeed, economists are unsure whether the period constitutes a “demand” shock or a “supply” shock with the developing consensus plumping for a “bit of both.”

Words like “unique” and “unprecedented” are badly over-used these days but few of us had ever experienced a period quite like it. To bowdlerize Winston Churchill, “never have so many worked so little for so much.”

Furlough schemes funded by massive state interventions kept businesses afloat and personal incomes buoyant. In fact, measures of household savings soared throughout the pandemic as largely uninterrupted incomes simply could not be spent and were accumulated.

Ironically, given the distress caused by the ravages of the virus before treatment regimens were developed and vaccines were perfected, the demand for luxury goods boomed.

Companies like Diageo crested on what they described as “premiumisation,” where consumers traded up to KetelOne and Johnnie Walker Black Label from cheaper brands. Fine wines boomed in price and luxury goods companies, Richemont, LVMH and Hermes all reported strong sales. Strong primary market sales were reflected in secondary market prices. The Liv-Ex fine wine index rose by 1/5 and the index of fine watches more than doubled: Patek Philippe, Rolex and Audemars Piguet became all but unobtainable.

That all changed in March 2022.

The end of the pandemic accompanied by large unspent cash deposits unleashed a surge in demand for social and retail experiences, construction activities restarted, and workers began to return to the office. Resurgent demand hit the buffers of impaired supply-chains and the rest is... well, inflation.

In March 22, central banks began the job of squeezing demand to fit available supply by raising interest rates. In the US, rates went from “zero” in March 22 to 5.25% in September 2023. The sudden end of “free money” pulled the rug from under the luxury goods companies and the wine and watch indices gave up all their pandemic gains. The other major central banks quickly followed suit including the UK’s Bank of England.

An old stock market saying goes, “Follow the money.” A recent Office for National Statistics survey sheds some light on current consumer spending habits, and they have changed. Or, perhaps, reverted.

According to the survey, 67% of us say we are “spending less on non-essentials” (luxury goods, for example), half of us say we are “shopping around more” and half of us say we are “using less fuel or electricity.” 41% are spending less on food and a third of consumers are using their savings to support day-to-day expenses with the same proportion “cutting back on non-essential journeys.”

Needless to say, the luxury goods companies most recent reports and accounts don't make for happy reading. The trend towards "premiumisation" has evidently gone into reverse.

If we follow the money, 2024 looks like a period when consumers retrench and go back to basics: "premiumisation" gives way to "value for money."

In stock market terms, fashionable "growth stocks" have outperformed cheaper "value" stocks for years. Yet, 2024 might be the year when markets follow the consumer and the old-fashioned "value proposition" comes back into vogue as investors begin to price-in the changing direction of straitened consumer spending. A balanced approach, mixing companies which show future potential (growth) with those that have been left behind (value), appears to us to be a logical conclusion for 2024 and beyond.

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