



Future uncertain

Currency fluctuations can have a huge effect on the value of deals in the shipping market. Jamie Jemmeson a Baltic Exchange member, Corporate FX gives the outlook for sterling this year

The British pound was one of the worst performing currencies of 2008, and 2009 didn't start too well either, as sterling hit its lowest level since 1985 – 1.3500 against the US dollar. This was a direct reflection of weak fundamentals and the fact that the UK officially entered recession. However, since then the pound has strengthened and has recently moved back above the key level of 1.50 against the US Dollar. Long-term recovery will depend on a number of fundamentals.

The UK technically moved into recession in the fourth quarter of 2008, according to GDP figures released in January. This is the first time the UK has been in recession since 1991. The housing market and the financial sector over the last few years have been the backbone of the economy. In 2008 both saw substantial losses to their market value.

There have been mixed views on the length and depth of the recession. The International Monetary Fund (IMF) believes that the recession will extend into 2010 and that economic activity will contract by 4.1% this year. Alistair Darling was slightly more optimistic during the UK Budget, predicting the economy will shrink by 3.5% for 2009, while expanding by 1.25% in 2010, and 3.5% in 2011.

In response to the situation, the Bank of England introduced "quantitative easing" (QE), expanding the amount of money in the system. The Bank has initially said it will buy UK government bonds, or gilts, maturing between five and 25 years. If QE works, credit growth will pick up and businesses will find it easier to get

credit. That, in turn, should help to stimulate the economy. However, it may still be too early to pass judgment.

S&P outlook

Rating agency Standard and Poor's recently changed its outlook for the UK, from stable to negative. Behind Standard and Poor's argument was an estimate that the UK's net debt-to-Gross Domestic Product ratio could rise to 100% of GDP in the medium term and stay there for some time. Standard and Poor's have stated that the UK AAA credit rating still stands but the main question is for how much longer? Should the UK lose its AAA credit rating, the implications for sterling could be extremely negative.

Inflation

In its most recent quarterly inflation report, the Bank of England stated that it believes inflation will fall below its target of 2% for the medium term. The Retail Price Index registered its first negative reading since 1960 as the recession drove prices lower. This makes the issue of deflation more pertinent.

Interest rates

The Bank of England has almost exhausted its interest rate firepower, having cut base rates by 525bp since December 2007. Interest rates are currently at the lowest level in the Bank of England's 315-year history. Ultimately the Bank

of England has not ruled out cutting rates further to 0%. However, the launch of the quantitative easing program suggests this avenue may have already been dismissed.

Are there signs of recovery?

Once the global economy begins to recover, it is expected that the UK economy will outperform the Eurozone, largely due to the proactive measures taken by the Bank of England.

Although there is no doubt that the UK is experiencing some difficult times, we are starting to see some "green shoots". Several of the large retailers have posted figures better than expected, and an additional positive from this is job creation. House prices continue to fall but at a much slower pace, with some surveys actually posting small increases in some areas.

Despite all this, it is much too early to start talking of a real recovery. Recently Britain's treasury rejected a request made under freedom of information legislation, by news agency Bloomberg, for publication of stress tests conducted by the Financial Services Authority earlier in the year. The information has been withheld on the basis that publication may lead to uncertainty in the financial markets, either in relation to specific institutions or more generally. So far Barclays is the only major bank to have said that it passed the FSA's stress-testing process, casting doubt that others such as RBS and Lloyds will.

Taking all this into account there are some promising signs for the future, but the UK is still on a very unclear path in terms of recovery.