

Economic review

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Our monthly economic review is intended to provide background to recent developments in investment markets as well as to give an indication of how some key issues could impact in the future.

It is not intended that individual investment decisions should be taken based on this information; we are always ready to discuss your individual requirements. We hope you will find this review to be of interest.

Chancellor unveils plan for growth

On 29 January, the Chancellor outlined her plan to boost economic growth during a speech in Oxford, although data released last month suggests the UK economy remained largely stalled at the start of this year.

In her speech to business leaders, Rachel Reeves set out a series of major announcements on infrastructure projects which she said would revive the country's economic fortunes after years of sluggish growth. Among the announcements was backing for a third runway at Heathrow, expansions at Luton and Gatwick airports, a major redevelopment of Old Trafford, plans for new wind farms and reservoirs, and a "growth corridor" between Oxford and Cambridge which it is hoped will help create "Europe's Silicon Valley."

The Chancellor described the UK as a country of "huge potential" which had been "held back" for "too long." And she added, "Low growth is not our destiny, but growth will not come without a fight, without a government willing to take the right decisions now to change our country's future for the better."

Official figures released by the Office for National Statistics (ONS), however, showed that growth currently remains tepid

with the economy barely growing in November. The 0.1% monthly expansion was below analysts' expectations and means the economy actually produced no growth at all during the three months to November.

Data from the latest S&P Global/CIPS UK Purchasing Managers' Index (PMI) also suggests the economy remains largely stalled. While January's flash headline growth indicator did rise to a three-month high of 50.9, this left the index only marginally above the 50.0 no change threshold, implying the economy continues to broadly flatline.

Economists do expect growth to pick up, though. For instance, the International Monetary Fund's recently released World Economic Outlook forecasts the UK economy will grow by 1.6% in 2025, a 0.1 percentage point upgrade from October's prediction.

Surprise dip in rate of inflation

The latest batch of consumer price statistics revealed an unexpected decline in the UK inflation rate, raising expectations of an interest rate cut at this month's Monetary Policy Committee (MPC) meeting.

Figures published last month by ONS showed the Consumer Prices Index (CPI) 12-month rate – which compares prices in the current month with the same period a year earlier – fell to 2.5% in December from 2.6% the previous month. This represents the first drop in inflation for three months, with ONS noting that the decline was primarily driven by falling hotel prices and a smaller than usual rise in airfares for this time of year.

The data release also showed that underlying measures of price growth fell even more sharply. Core inflation, for instance, which excludes energy, food, alcohol and tobacco prices, fell to 3.2% in December from 3.5% in November, while services inflation dropped to 4.4% from 5.0% a month earlier.

While economists do expect the rate of inflation to tick higher over the next few months due to a combination of higher energy prices, growth in real wages and a temporary stimulus from the Autumn Budget, December's inflation dip did bolster hopes of an imminent reduction in interest rates.

The Bank of England's (BoE's) interest-rate setting committee is due to announce its next decision on 6 February, with the MPC widely expected to sanction another quarter-point reduction. Indeed, all 65 economists polled in a recent Reuters survey predicted that Bank Rate would be trimmed this week.

In addition, a majority of economists are forecasting a further three quarter-point cuts this year, which would take Bank Rate down to 3.75% by the end of 2025. A significant minority of surveyed respondents, however, felt the BoE would deliver fewer rate cuts this year, echoing the relatively cautious language adopted by policymakers themselves.

Wage growth strong but starting to cool

While official earnings figures released last month did show that UK pay growth stayed strong across the autumn months, more recent survey data suggests growth has begun to cool and is likely to continue doing so this year.

The latest ONS statistics revealed that average weekly earnings excluding bonuses rose at an annual rate of 5.6% in the three months to November. This was up from 5.2% in the previous three-month period, driven by particularly strong private sector pay growth. After adjusting for CPI inflation, total regular wages on average rose at an annual rate of 3.4%; this represents the fastest growth in real earnings for over three years.

More recent survey evidence, however, suggests pay settlements have already started to fall. Findings from a poll conducted by human resources data firm Brightmine, for instance, showed median pay awards in the three months to December fell to their lowest level since December 2021.

Another recently published survey points to a further cooling in wage growth over the coming months. Indeed, the Incomes Data Research poll found that seven out of ten British businesses were either extremely or moderately likely to reduce pay awards in order to offset the tax hikes announced in last October's Budget.

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Government finances under pressure

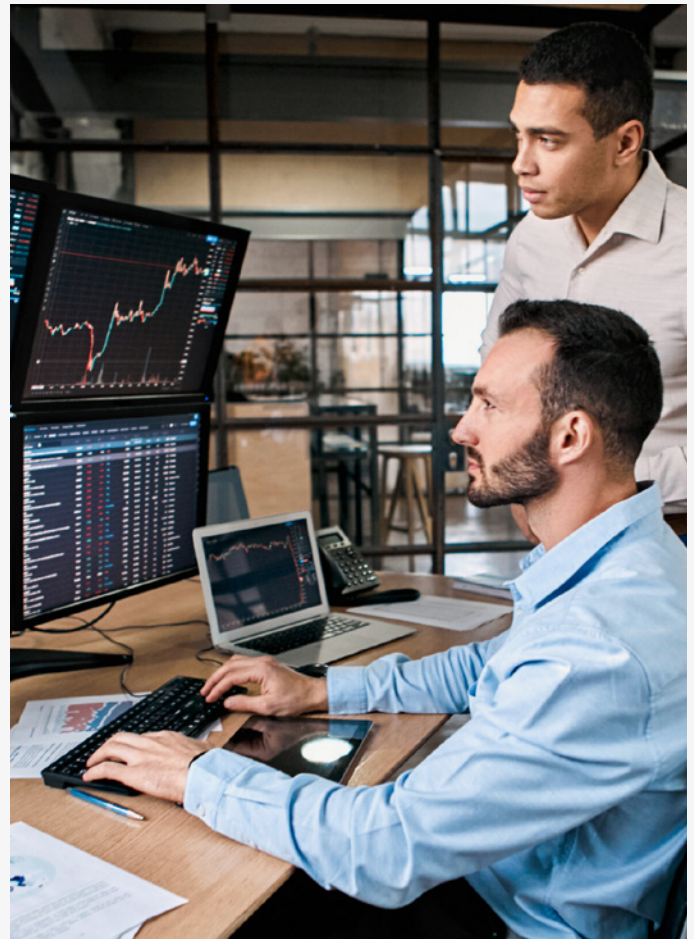
Public finance statistics released last month by ONS revealed an unexpected jump in the level of government borrowing which once again underlined the significant fiscal pressures faced by the Chancellor.

The latest data release showed that government borrowing totalled £17.8bn in December, the highest level for that particular month in four years. This figure was above analysts' expectations and left fiscal year-to-date borrowing £4.1bn ahead of the Office for Budget Responsibility's official forecast produced for the Chancellor's Autumn Budget.

A significant chunk of December's borrowing related to debt interest payments; in total, interest charged servicing the government's debt stood at £8.3bn. Earlier last month, a combination of international factors and fears over the UK economic outlook also saw long-term government borrowing costs rise to a 26-year high.

While borrowing costs subsequently fell back following release of last month's UK inflation data and an unexpected drop in US core inflation, they remain above levels forecast at the time of the October Budget. This recently led the Resolution Foundation to warn that the Chancellor may need to raise taxes or cut spending if she wants to stick to her self-imposed financial rules when she delivers the Spring Statement on 26 March.

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All details are correct at the time of writing (03 February 2025)

It is important to take professional advice before making any decision relating to your personal finances. Information within this document is based on our current understanding and can be subject to change without notice and the accuracy and completeness of the information cannot be guaranteed. It does not provide individual tailored investment advice and is for guidance only. Some rules may vary in different parts of the UK.