UK Economic Outlook

LPM Conference 2025

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Inflation

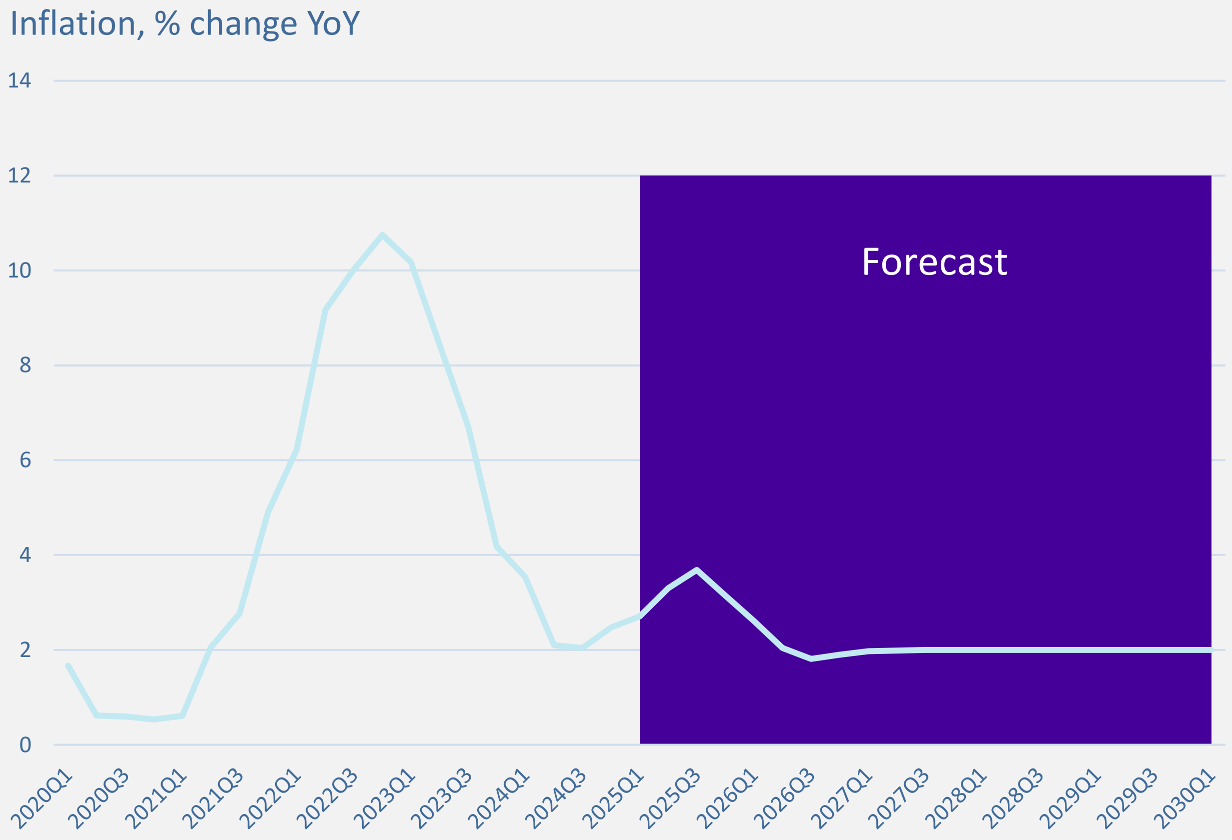
Inflation fell to 2% target in Sep 2024, but is now rising.

Inflationary pressures:

- Increasing energy and water prices
- Public spending

Deflationary pressures:

- Fiscal drag
- Employer NI contributions



Data: OBR

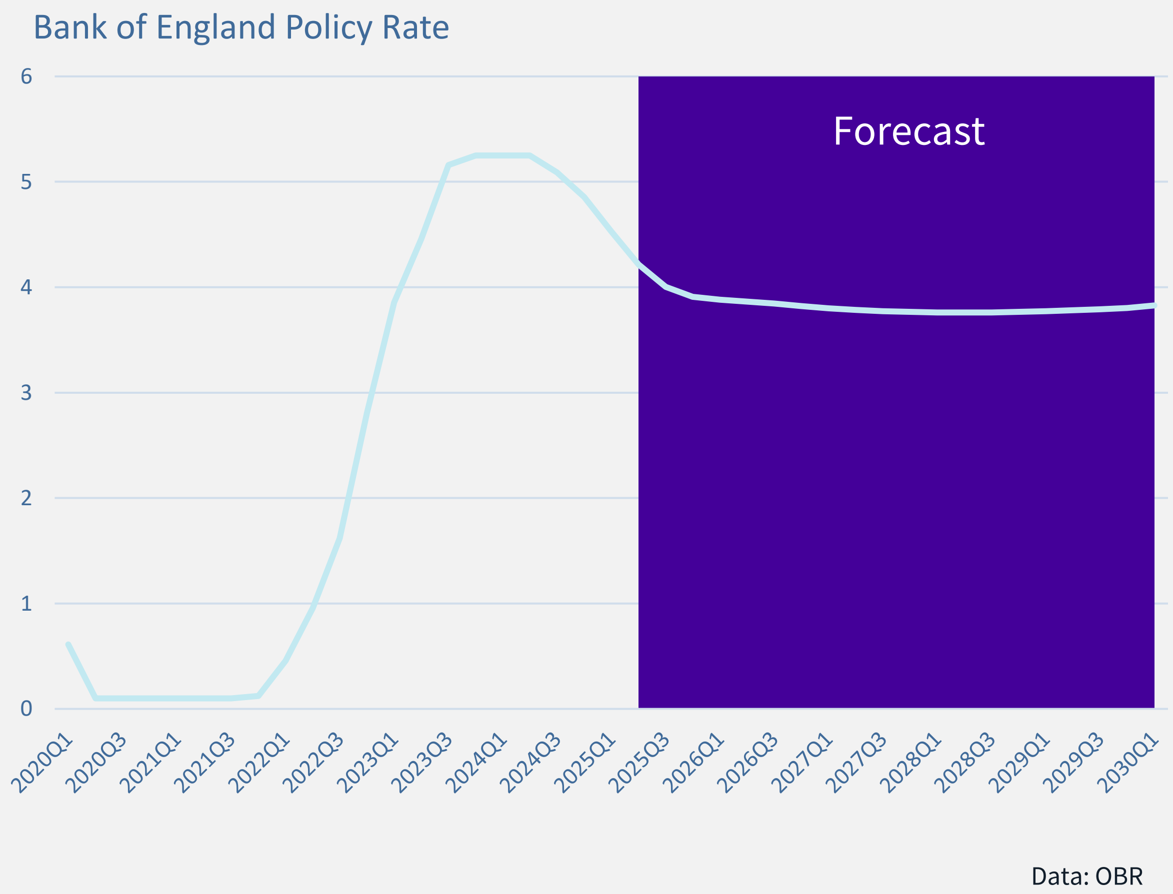
Interest rate

Bank rate at 4.25% following a cut in May 2025.

In June, the MPC was split 6-3 in favour of holding rates.

Expect two more cuts this year.

But combination of public spending and increased cost pressures for business, plus volatile environment, gives the MPC a tricky task!



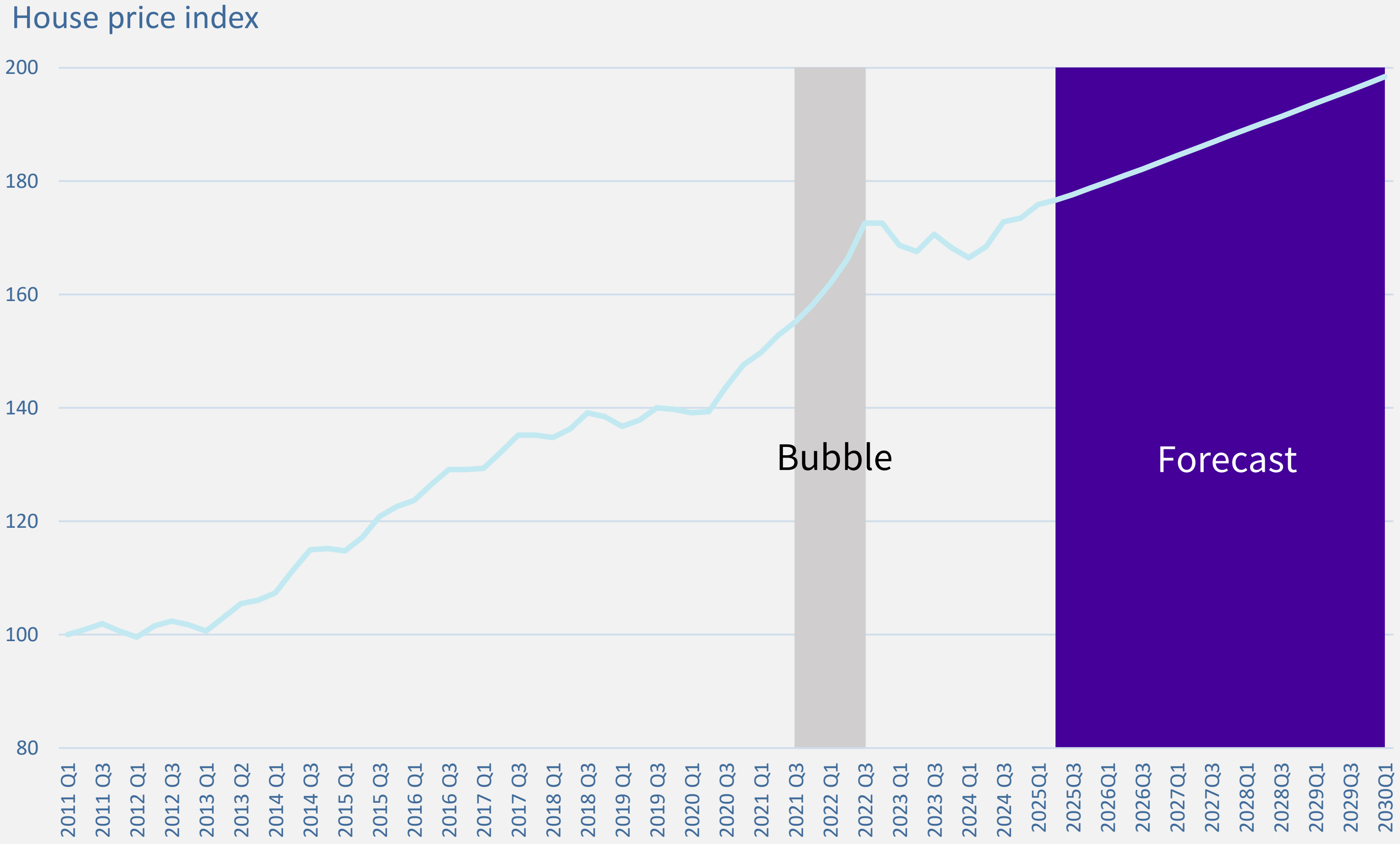
Residential housing market

Strong house price growth in the aftermath of Covid-19.

Recent research detects signs of a bubble from 2021:Q3 - 2022:Q3.

30% of fixed mortgage accounts agreed prior to 2021:Q4 are yet to refinance.

Effect of higher interest rates will take time to transmit through to house prices.



Data: ONS and OBR
Whitehouse et al. (2023) real time monitoring detection dates

Residential housing market

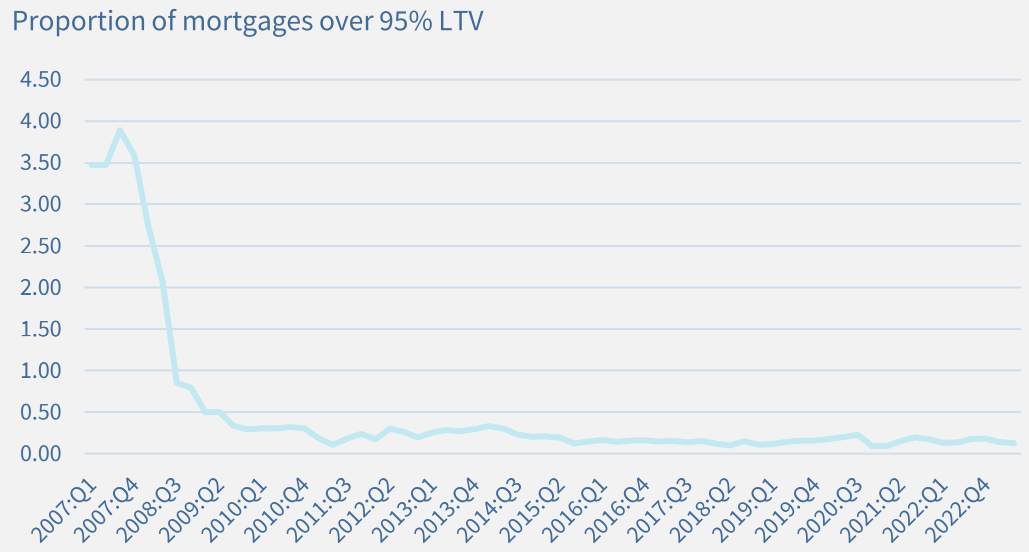
Approximately 30% of UK households have a mortgage.

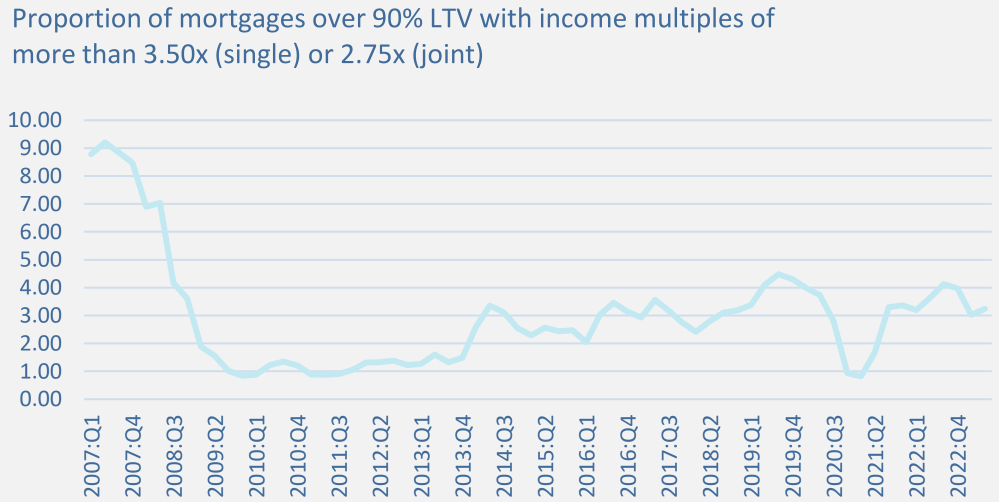
Compared to 2007:

- Tighter lending standards
- Higher proportion of fixed-rate mortgages (85% vs 50% - OBR)

Spring Statement gave a commitment to build 1.3 million new homes over next 5 years, increasing supply.

Stamp duty changes in April 2025 may be reducing demand for housing, but likely to be offset by reduction in mortgage rates which should have larger impact.





Data: FCA

Commercial property market

Shift to work from home, induced by Covid pandemic, may be permanent rather than temporary.

Office vacancy rates continue to trend upwards.

Reduced demand due to change in worker behaviour, plus end to cheap lending, could lead to more permanent change in the commercial property market.

Empty office spaces in city centres have knock on effect for retail property, exacerbating the problem.

Data: Cluttons Research

Key regional cities: Birmingham, Bristol, Leeds and Manchester

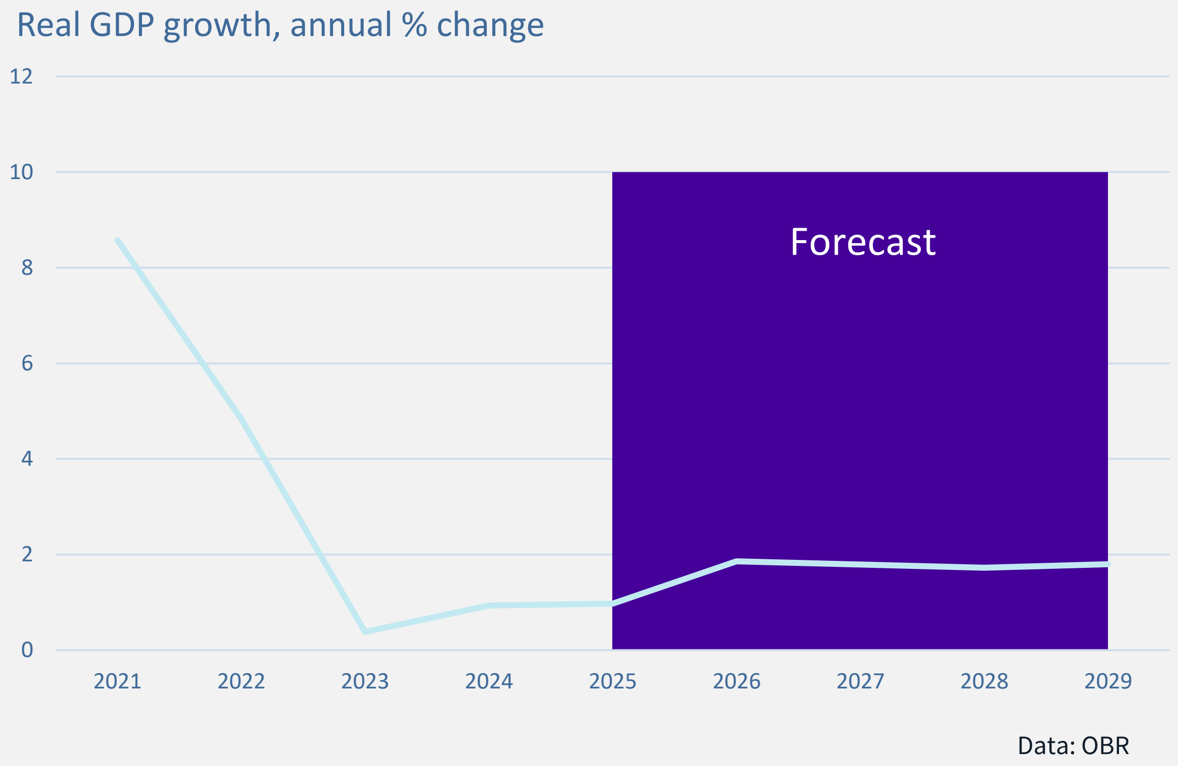
GDP growth

GDP growth in 2025 has been modest.

The Government's autumn budget and spring statement make clear commitments to increase public spending.

Private sector investment expected to be weaker: rising business costs, lower household disposable income, global uncertainty.

GDP growth forecast to increase in 2026 to nearly 2%.



A difficult time for business?

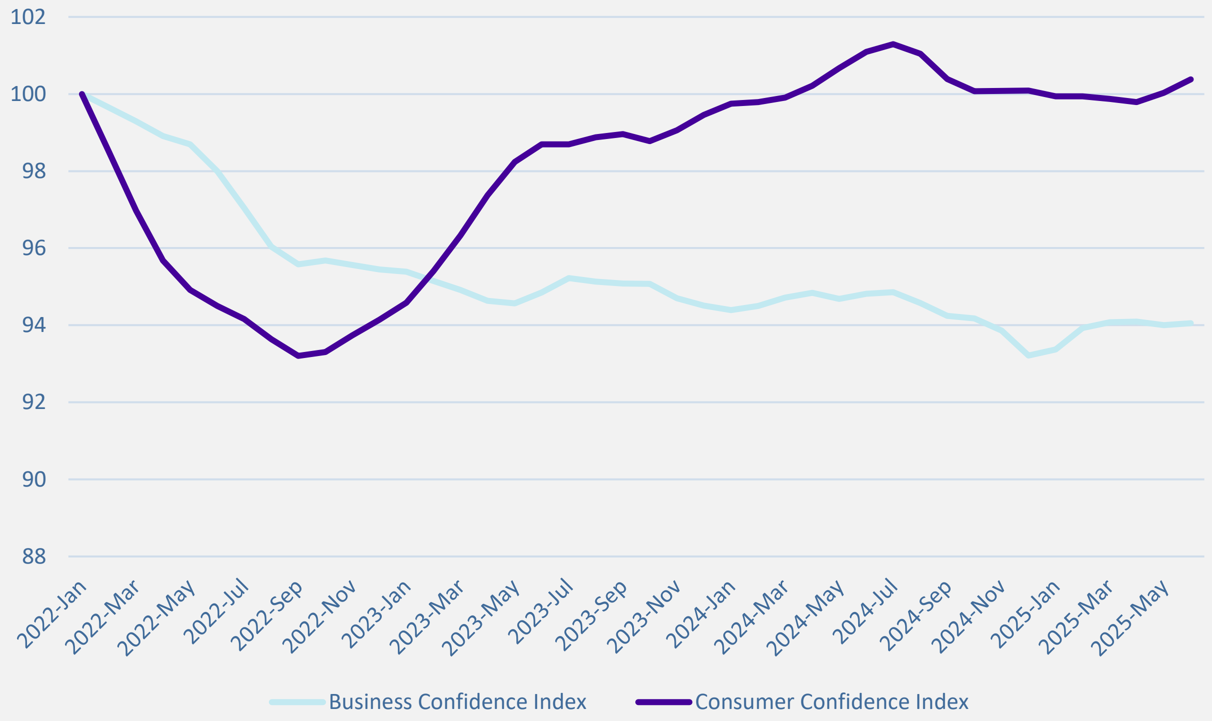
Business confidence has been declining since Jan 2022.

Increase in national minimum wage and employer NIC: **Low-wage, labour intensive businesses will be hit hardest.**

Global uncertainty: businesses may delay investment, reduce hiring.

Fiscal drag: reduces consumer spending.

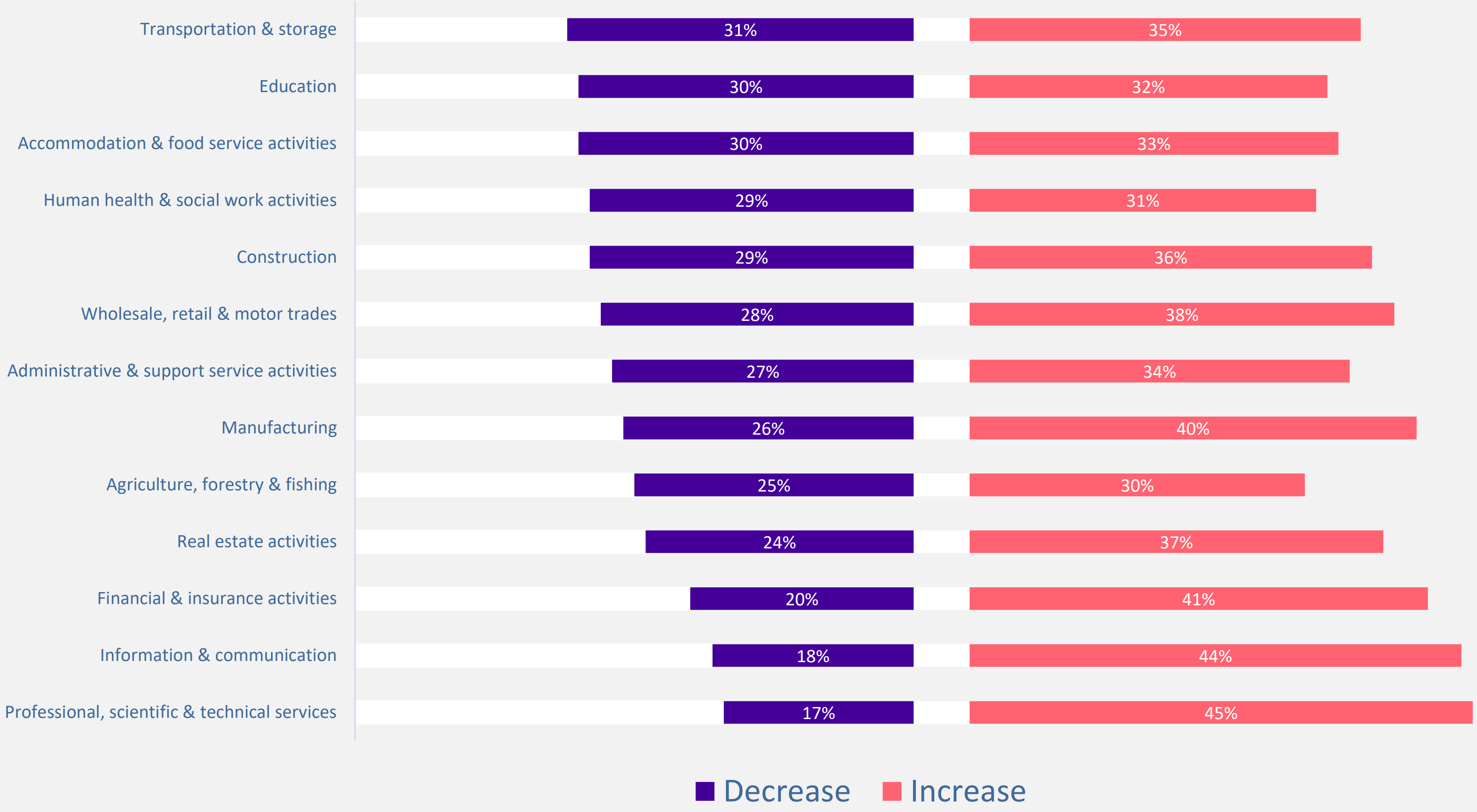
Business and Consumer Confidence Indices



Data: OECD

Industry sector performance

Proportion of firms whose turnover increase or decreased in July 2025 relative to June 2025



Data: ONS

Opportunities

Defence

Defence spending to increase to 2.5% of GDP by 2027, with an additional £2.2bn payment to MoD this year.

Direct SME spending targets to encourage MoD to issue contracts to wider pool of suppliers.

Defence Innovation Fund may provide easier path for start-ups to scale up.

Green / Renewable Energy

Government to invest in capital spending over the next 5 years, to include:

- Low-carbon transport
- Business grants for ‘green’ projects
- Green SME hub

Construction

£600m Government package to train up to 60,000 new workers.

The Regional Picture

- Nearly 70% of current defence spending goes to businesses outside of London and South East:
    - Rolls-Royce (Derby) signs £9bn contract to provide nuclear reactors to Navy
    - BAE (Barrow) to receive £200m for Navy submarines
    - Defence tech company ‘Helsing’ to open advanced manufacturing facility (Plymouth)
    - Rheinmetall to open gun barrel manufacturing plant (Shropshire)

- Most exposed regions to potential US tariffs are West Midlands and Wales (automotive, aerospace, steel industries)

- Capital infrastructure investment may focus on already thriving areas (Heathrow third runway, Lower Thames crossing)

Global Risks: Middle-East Conflict & Russia-Ukraine

Geopolitical uncertainty:

- Negative impact on consumer and business confidence.
- Businesses delay investment decisions.
- Consumers cut non-essential spending.

Energy prices:

- Disruptions to oil supply increase energy prices, with impact on inflation, interest rates and GDP growth.

Supply chain disruption:

- Rerouting commercial shipping.
- Increased shipping costs.

Domestic Risk: Unreliable employment data

UK (un)employment data produced by ONS using the Labour Force Survey:

- Low response rates, exacerbated by Covid, make the data unreliable.
- Not clear if reported changes to unemployment are reflecting actual changes in the labour market or sampling variability.
- Especially the case for regional or age breakdowns.

Discrepancy between ONS data and other employment indicators.

Reliable data necessary for monetary and fiscal policy decisions and evaluating impact of these policies.