UK Finance

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Monthly Economic Review

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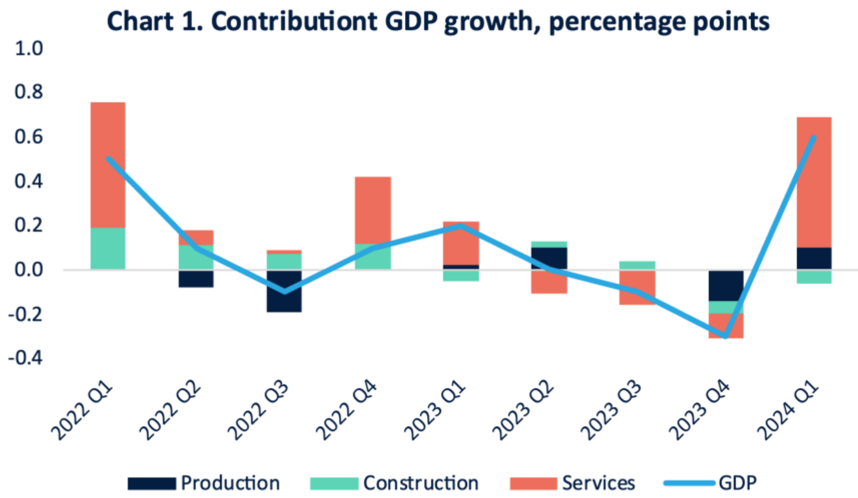
The UK economy had a stronger than expected start to 2024, but with some sector exceptions. We take a look at how household costs and spending patterns have evolved so far this year. And as everyone else is talking about it, we have some general election analysis.

Strong start to 2024

The UK economy bounced back more strongly than expected from recession in the second half of 2023. GDP rose by 0.6 per cent in the first three months of the year, compared with the previous quarter, beating market expectations and the Bank of England's most recent prediction of 0.4 per cent.

Growth of 0.6 per cent represents the fastest pace of quarterly expansion since the final quarter of 2021 – when we were still benefitting from post-pandemic catch-up. Moreover, it was a stronger performance than the US and main eurozone economies, the latter of which also returned to growth at the start of the year.

Recovery was not, however, felt across all sectors of the economy. The news continued to be positive from the manufacturing sector, which has seen a particulary marked upturn since the start of the year. In [last month's briefing](#) we touched on the strong performance of auto manufacturers – this was confirmed in the quarterly data – but there was also a strong showing across the foundation industries (metals, glass, and non-metallic minerals) and food manufacturing.



Source: ONS

There was also a relatively broad-based improvement in output in services, which expanded by 0.7 per cent on the quarter (the strongest pace of growth since 2022 Q1). There were only a few services sub-sectors that bucked the positive trend, such as accommodation, wholesale and retail trade of vehicles, and parts of the real estate sector were among the notable exceptions.

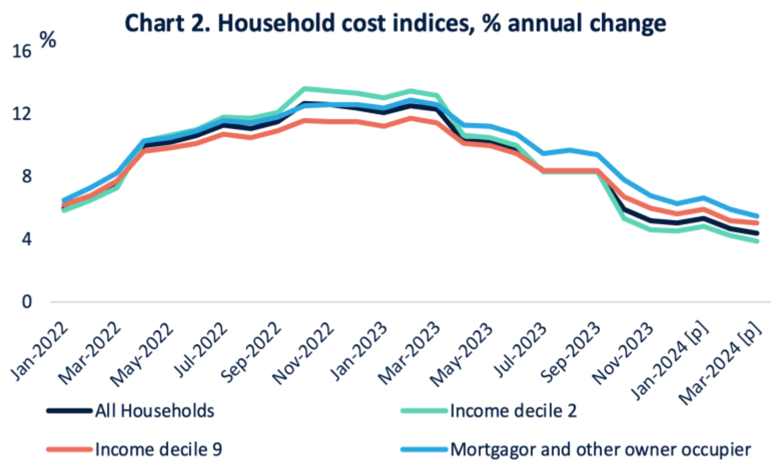
The main outlier to the brighter picture in Q1 was construction, now technically in recession, with two consecutive quarterly falls in output of 0.9 per cent. ONS pointed the finger at the poor weather at the start of the year, but the challenges of construction extend beyond the rain. Almost all work was down in the three months to March, except repair and maintenance. The Construction Products Association released a rather downbeat forecast of a full year contraction in construction output of 2.2 per cent this year.

One final, moderately positive nugget, from the ONS GDP release, was a further rise in business investment over the quarter. This is much needed after the period of sustained weakness that pre-dates the pandemic. This could be a result of the various tax measures to support investment. In any case, if this continues it will be a positive for productivity.

Inflation eases … as expected

Inflation has been much discussed in recent briefings as it has been a source of pain for households, businesses, and policy makers. April's data, more or less, confirmed economist's expectations of CPI heading back to target, coming in at 2.3 per cent, mainly as a result of the fall in the energy price cap. Food inflation also continued to ease. However, the closely watched core and services inflation measures held up at 3.9 per cent and 5.9 per cent respectively.

Through the cost-of-living crisis there has been a particular emphasis on lower income households facing higher inflation rates as a disproportionate share of incomes are devoted to food and energy, which have seen especially high inflation rates. The ONS's helpful Household Cost Indices provides some insight on how different income deciles and household types are experiencing cost increases.



Source: ONS

Chart 2 shows the annual increase in household costs in aggregate, for the second- and ninth-income decile (a proxy for bottom and top of the income spectrum) and mortgaged households.

In a change from the latter part of 2022 when lower income households were experiencing much higher inflation rates than higher income counterparts, the easing in food and energy costs is helping to bear down on cost increases for the former cohort. Provisional estimates for the first few months of this year point to higher income and mortgaged households now seeing higher rates of cost increases (up 5 per cent and 5.5 per cent respectively compared with 3.9 per cent for lower income deciles). The key driver of this is rising interest rates and as we have discussed in our **Household Finance Review** on many occasions, the impact of higher rates will be most acutely felt by those households refinancing from mortgages fixed on much lower interest rates.

With another 700,000 mortgages rolling off fixed rates in the second half of the year faster rises in household costs for mortgages and higher income households might prove more persistent this year.

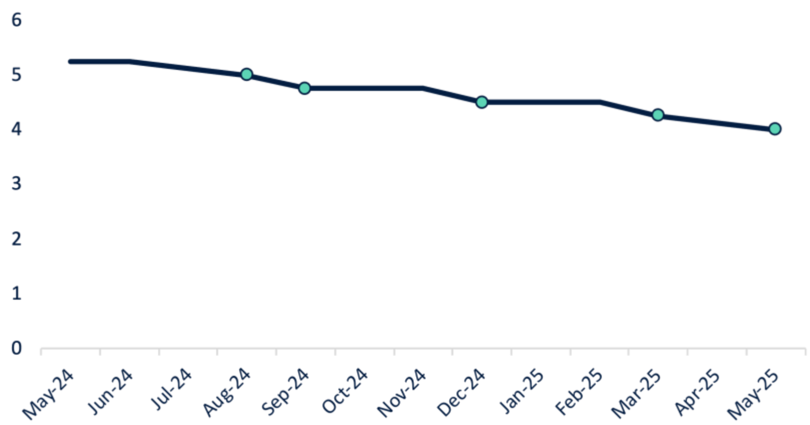
May Monetary Policy Report

The Monetary Policy Committee (MPC) held Bank Rate at 5.25 per cent in May. Alongside the decision, the Bank published its quarterly Monetary Policy Report (MPR) outlining updated forecasts for UK growth and inflation.

Starting with GDP growth, there was a modest upgrade to the outlook for 2024, with the Bank now expecting GDP to rise by 0.5 per cent and then one per cent in 2025 (up from 0.25 per cent and 0.75 per cent in the February forecast). On the upside, the energy price shock will continue to unwind over the course of the year and real incomes will recover, helped by the recent cuts to national insurance contributions. Nevertheless, some of the impact of higher interest rates is yet to be felt and will continue to bear down on demand. Overseas demand should recover gradually too this year, but there are more marterial risks from conflict in the Middle East and a weaker than expected Chinese economy.

As noted above, the inflation data released after the MPR, shows CPI moving broadly in line with expectations. The Bank judges that much of the pass through from external price shocks has occurred. While inflation has headed close to target, it is expected to head higher in the latter part of this year due to the ongoing presence of domestic inflationary pressures. The MPR again calls out the elevated rate of services inflation and CPI excluding energy prices. CPI is forecast to be just under the two per cent target in two years time, but geopolitical risks again present some upside risks.

Chart 3. Median expecations for Bank Rate, %



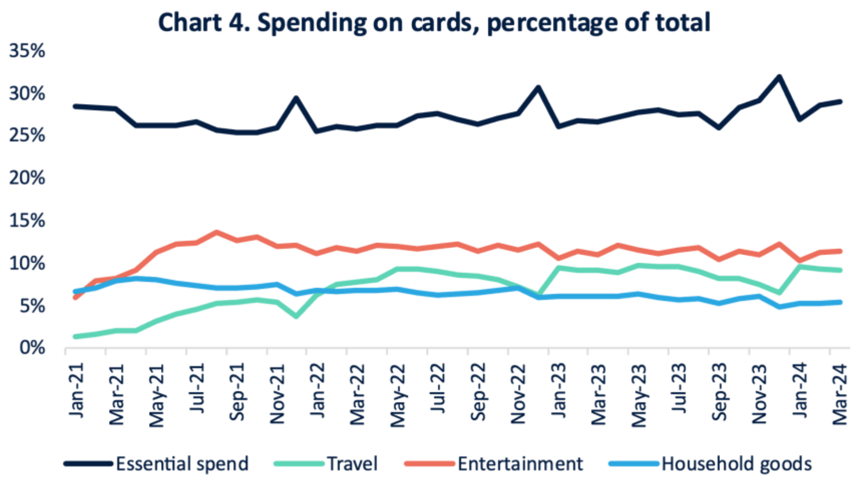
Source: Bank of England Market Participants Survey

Earlier this year some forecasters were expecting the first interest rate cut to come in May or June, but predictions have since been pushed out to later in the summer. The Bank's survey of market participants, for example, shows the median expectation of a 25-basis point cut in Bank Rate in August. With two more quarter point cuts coming in September and December.

The minutes of the May meeting, when two MPC members voted for an immediate quarter-point cut, leaves the possibility of an earlier rate cut on the table. The minutes point to a range of views on the risks around the inflation projection and the weight of data evidence required to materially reconsider their position on the restrictiveness of monetary policy.

Household spending patterns

Retail sales, according to ONS, have had a bumpy ride since the start of the year – there was a solid rebound in January after a disappointing festive period, then renewed weakness in April – possibly the weather and/or the timing of Easter. That retail sales volumes have been on a downward trajectory for the best part of three years is not surprising given the squeeze to real incomes, weak consumer confidence and reticience to commit to major purchases.



Source: UK Finance

Digging into UK Finance's detailed card spending data, we see some changes in the composition of spending on debit and credit cards.

Chart 4 illustrates four broad categories of spending on cards in the UK – essential spending (supermarkets, petrol, chemists, buses, utilities and telecomms), travel (airlines, hotels, and travel agents), entertainment (restaurants, sports, and recreation) and household goods (furniture and electrical goods). Together these categories account for over half of monthlty spend on cards (or around £40 billion in March 2024).

The proportion of 'essential spend' has remained relatively stable post-pandemic but has increased compared with the average in 2018/19 (around a quarter of all spend fell into this category) – a factor of significantly higher prices across all essential spend categories.

Spending on travel rebounded after the pandemic as people returned to international holidays. While cost of living pressures persist, travel spend saw the usual seasaonal bounce at the start of 2024 and as a proportion of total card spending, travel is trending in line with pre-pademic levels – seemingly one area of spending that households are continuing to prioritise even if cuts need to be made elsewhere. And one of those areas has been household goods – also depressed by the slow housing market.

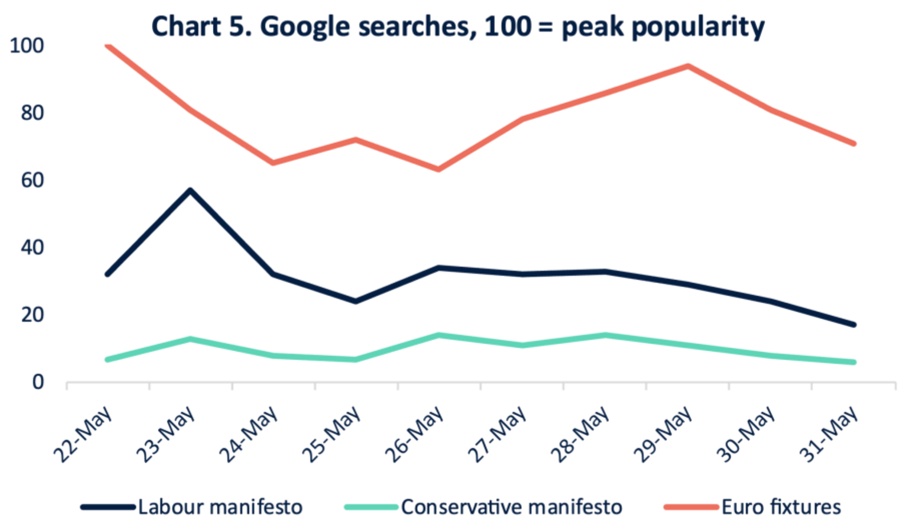
‘What people really want to hear is…’

A common refrain from politicians trying to navigate tricky questions on the morning news round. We’re likely to hear more of this now the date of the general election has been set for 4th July and political campaigning is well underway.

As the representative body for the banking and finance sector, [UK Finance recently set out the policies it wants to see] being discussed by the main parties, a framework for the sector to continue to support households and businesses as the economy recovers.

It is not for this briefing to discuss the various polls or the economic implications of policies being floated ahead of the election – we’ll get to that, no doubt, once the next government has been formed.

For now, we’ve turned to google trends to look for signs of public engagement with the first seek or so of campaigning. There was a bit of a bounce in interest in the manifestos the main parties were standing on just after the election was called (there are similar results for labour/ conservative policies). But so far, electioneering isn’t quite capturing the interest of the nation like the upcoming Euros tournament (see also the UK release date for the new Deadpool film.)



Source: UK Finance

While pundits and policy wonks will be pouring over the detail of all the policy speechs and inevitable mis-steps, the upcoming leaders’ debates may well start to ignite a broader interest in the campaign. We’ll be looking at what the election results mean for economic policy and the home nations progress in the Euros in a future briefing.

Key indicators

Indicator	Period	Value	Change	2023 Forecast*
GDP	Q1 2024	0.6%	↑	0.6%
CPI inflation	Apr 2024	2.3%	↓	2.2%*
Unemployment rate	Mar 2024	4.3%	↑	4.4%*
Average earnings	Mar 2024	5.7%	↔	4.0%
Brent crude	Apr 2024	$89.84	↑	-
$ Exchange rate	Apr 2024	$1.26	↑	-
Bank Rate	May 2024	5.25%	↔	4.5%*

Source: ONS, HM Treasury, Bank of England, EIA

*Q4 2024