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Monthly Economic Review

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This month we take a look at the shape of the UK economy the next government will inherit after 4th July, and we give a quick recap of UK Finance's prioirities for the next parliament. While British eyes are on the UK polls, there are still plenty of elections in 2024 H2. We'll take a look at international developments in 2024 so far.

Pre-election data round-up

With just a few days left on the campaign trail we start this month's review with a round up the latest data releases, which provide the economic starting point for the next government.

Kicking off with growth – GDP estimates for April indicate a bump in the recovery after a solid quarter of growth at the start of 2024; Q1 GDP growth was revised up to 0.7 per cent. While output was unchanged in April compared with the previous month, this was not out of line with some expected unwinding of relatively strong growth in March.

Total services output rose by 0.2 per cent in April – the fourth month of growth – but the sub-sector picture was mixed. Increasing services output was offset by a hefty 1.4 per cent fall in manufacturing (with a fairly poor month across most parts of the sector) and a continued contraction in construction output.

Monthly GDP numbers are volatile, nevertheless, a somewhat weaker picture in Arpil across a fairly broad cross section of sectors continues to indicate that the UK economy is facing some constraints from squeezed consumers, stuttering global demand and the effects of higher interest rates. Other business surveys, such as the purchasing managers' indices indicate a bit of a loss of momentum in services activity in June. All in, the Bank of England see modest quarterly growth of around 0.25 per through the rest of 2024 as the effects of cost-of-living pressures take time to dissipate.

The news on inflation continues to head in the right direction. CPI came in at bang on the Bank of England's two per cent target in May for the first time in three years. The lower energy price cap in April contributed to a significant fall in the headline rate of inflation last month, and in May a material moderation in food inflation was the main contributor to the further fall. We are not yet seeing the same magnitude of fall in services inflation, which edged down to 5.7 per cent in May from 5.9 per cent in April. Though, part of the still elevated services inflation relates to the indexation of some services (e.g. communications) pushing prices higher.

Most labour market indicators point to further softening. While ongoing work to the ONS labour market survey means it's a bit tricky to get a clear read out from the official statistics, they do point to a further uptick in unemployment and continuing declines in vacancies and hiring activity. Wage growth is still solid, though the annual rate of increase was flattered by the big national minimum wage increase in April, but other survey metrics point to moderation in pay pressures through this year.

While the retail sales figures for May looked solid, with monthly volume growth of nearly three per cent (after a very poor April), the timing of Bank holidays and the weather are adding to some volatility in the data. Consumer confidence, while continuing to edge upwards, is still in the doldrums.

Developments in these metrics were broadly in line with the expectations of Monetary Policy Committee (MPC) members at their meeting in June. Economic activity is still expected to head higher over the rest of this year, but, as yet there are no real signs of much momentum. Any action from a new government (and a budget statement is unlikely to take place before September given the lead time needed for Office for Budget Responsibility forecasts) won't move the growth needle in the short term.

The MPC held rates again at 5.25 per cent, but discussion appeared more finely balanced than in previous meetings. Two members voted for a quarter point cut in June, seeing medium term inflation risks now skewed to the downside. Amongst those voting to maintain Bank Rate at 5.25 per cent in June, there as mix of views on the inflation outlook, with some noting that recent news had not changed the view that the economy was now on a disinflationary trajectory. The Bank's market participant's survey reported a modal expectation of a qurter point cut in Bank Rate at the next meeting in August.

A financial services manifesto for the UK

While the UK economy trundles along (in spite of political ambitions for a significant change of pace) financial services will be a important contributor to our future economic fortunes.

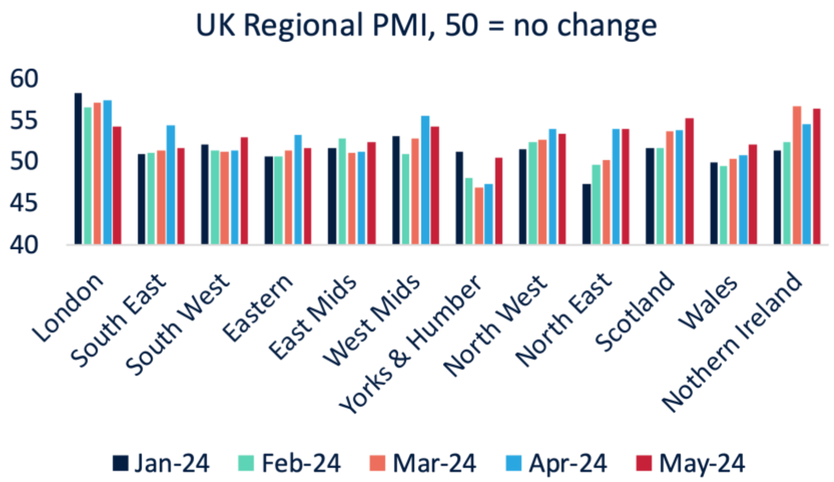
The financial services sector delivers real benefits to UK consumers and businesses by helping people buy their first home, supporting small businesses to begin trading, enabling payments to be made swiftly and securely, and helping companies scale up and trade internationally.

Across these and many more issues, our approach is to work with government to support key public policy objectives. **Our manifesto** outlines the policy agenda that the sector would like to see taken forward post-election and through working in partnership, we can help build a better society for all. Key recommendations include:

Support people and businesses	Support communities and society	Support growth
Review personal savings allowances	Introduce a new Fraud and Scams Bill	Champion the National Payments Vision and Strategy
Establish taskforce to tackle financial abuse	Give the UK Infrastructure Bank a greater mandate to invest in net zero projects	Issue a digital gilt backed by HM Treasury to encourage the development of securities tokenisation.
Increase Stamp Duty bands in line with the UK House Price Index	Make technology, social media and telecoms firms contribute to the cost of tackling economic crime and reimbursement	Create a Government Champion for Competitiveness with a remit to produce an annual report to Parliament on the burden of regulation for financial services
Extend the new Growth Guarantee Scheme	Publish detailed net zero investment roadmaps for key sectors of the economy	Publish a tax roadmap for financial services.
Create an independent Retrofit Advisory Service	Legislate to ensure information held on Companies House can be properly verified and relied upon.	Use the Berne Financial Services Agreement as a blueprint for other overseas financial centres

Regional business activity

While the UK growth picture is looking moderately better, on current forecasts we're some way from the manifesto ambitions of the main political parties. While we've noted some variation in performance across sectors (above) in the official statistics, there is also some divergence in business activity across regions as reported in surveys, such as the purchasing manager's index (PMI).



Source: NatWest Regional PMI

As the chart illustrates there has been an uneven performance in business activity across UK regions and nations since the start of the year. Only in the latest data, for May, is activity expanding across all regions, and for the first time in over a year (an index reading over 50).

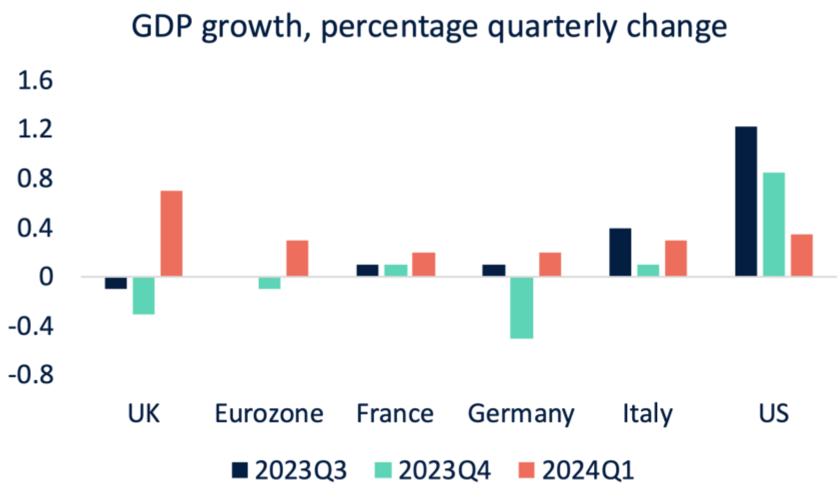
At the start of the year London was leading the way, with the strongest expansion in private sector activity, but this dropped off in May with a slowing in new orders and waning customer growth. In contrast, there has been a rebound in Northern Ireland business activity following a slow start to the year, with increased activity attributed to a strengthening manufacturing sector, even as retail activity remains weak. Business activity in Wales, Yorkshire and Humberside, and parts of the Midlands, while expanding, has been subdued so far this year. A reminder that national statistics don't necessarily represent how all regions of the economy are feeling.

The survey does, however, make for some encouraging reading on the inflation outlook for those MPC members potentially poised to argue for a cut in interest rates. Across all regions business cost pressures are easing, following an uptick in April driven by the minimum wage increase, and prices charged for goods and services also rose at a more modest pace.

GDP growth

The UK was not alone is seeing an uptick in GDP growth at the start of the year. Across the EU there were also some increasing signs of pick up in activity following a difficult

2023. In the eurozone GDP rose by 0.3 per cent after a modest contraction at the end of last year – this was the fastest rate of expansion since 2022 Q3. There was a modest increase in consumer spending as households recover from last year's cost of living pressures, but net trade was the main driver of growth at the start of the year.



Source: Trading Economics

Across the main eurozone economies, there was a similar story. A modest quarter of economic expansion, with external demand playing a key role, in addition to increased government spending in France and Italy.

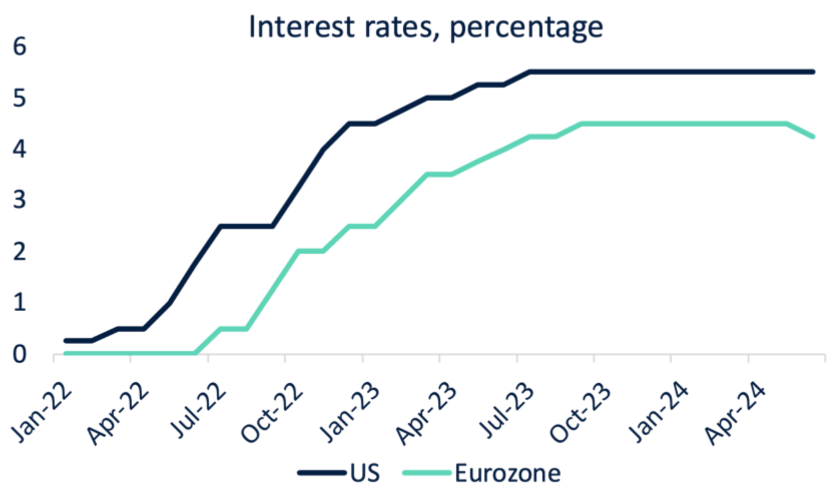
Snap elections were also recently called in France, and the first round of voting kicked off at the end of June, after a poor performance in the European elections and the challenges faced by Macron's Renaissance party without a parliamentary majority. The election debate does appear to have an economic dimension, with voter worries about living standards, inequality and welfare, but immigration as well as support for Ukraine are also key election topics. Unlike in the UK, the snap election hasn't done anything for consumer confidence. The latest reading from INSEE showed confidence fell in June, remaining well below the long-run average as standard of living concerns persist.

Finally turning to the US, which was the strongest G7 performer last year, growth slowed to 0.4 per cent in the first three months of 2024. Consumer spending growth slowed, notably on goods, but investment and government spending remained a prop to growth. The US economy continued to create jobs in May and inflation is also easing – but there is little sign of news, good or bad, on the economy having a significant impact on the polls ahead of the November election. The first Biden v Trump debate glossed over how the candidates would manage the economic challenges and opportunities facing the US, instead focusing on …. well, it wasn't entirely clear.

Interest rates

As we noted in May, inflation developments and messaging from the European Central Bank pointed to the ECB being one of the first major central banks to cut interest rates.

And so it was in June that interest rates were cut by a quarter point to 4.25 per cent. Eurozone inflation has halved compared with a year ago with ECB forecasts expecting it to average 2.5 per cent this year. The 'marked improvement', therefore, paved the way for rate cuts, but future decisions would be data dependent. Economists are expecting two more quarter point cuts this year.



Source: Trading Economics

The outlook for US interest rates hasn't shifted. The Fed revised up its expectations for core inflation in 2024 in June, with markets still looking for just the one reduction in the Fed funds rate in 2024.

Key indicators

Indicator	Period	Value	Change	2024 Forecast*
GDP	Q1 2024	0.6%	↑	0.7%
CPI inflation	May 2024	2.0%	↓	2.2%*
Unemployment rate	Apr 2024	4.4%	↑	4.4%*
Average earnings	Apr 2024	5.9%	↔	4.0%
Brent crude	May 2024	$81.75	↓	-
$ Exchange rate	May 2024	$1.26	↔	-
Bank Rate	Jun 2024	5.25%	↔	4.5%*

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

*Q4 2024