

# The UK Economy: Sluggish momentum

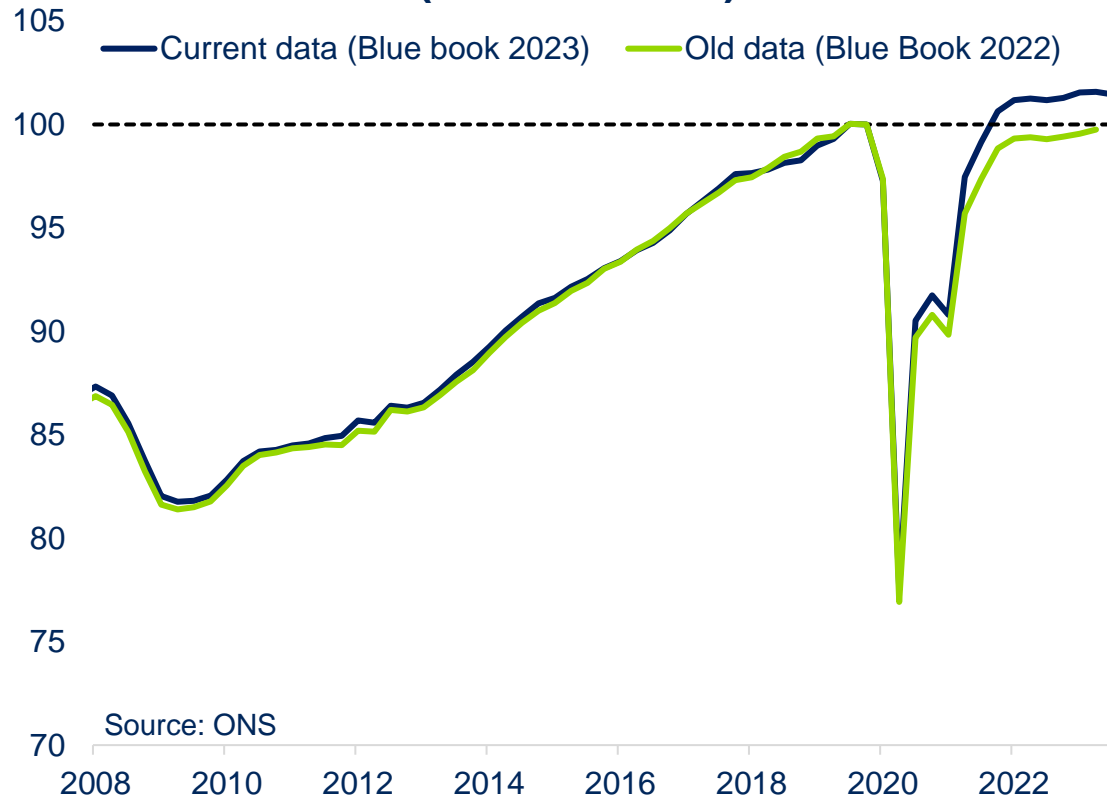
Anna Leach  
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January 2024

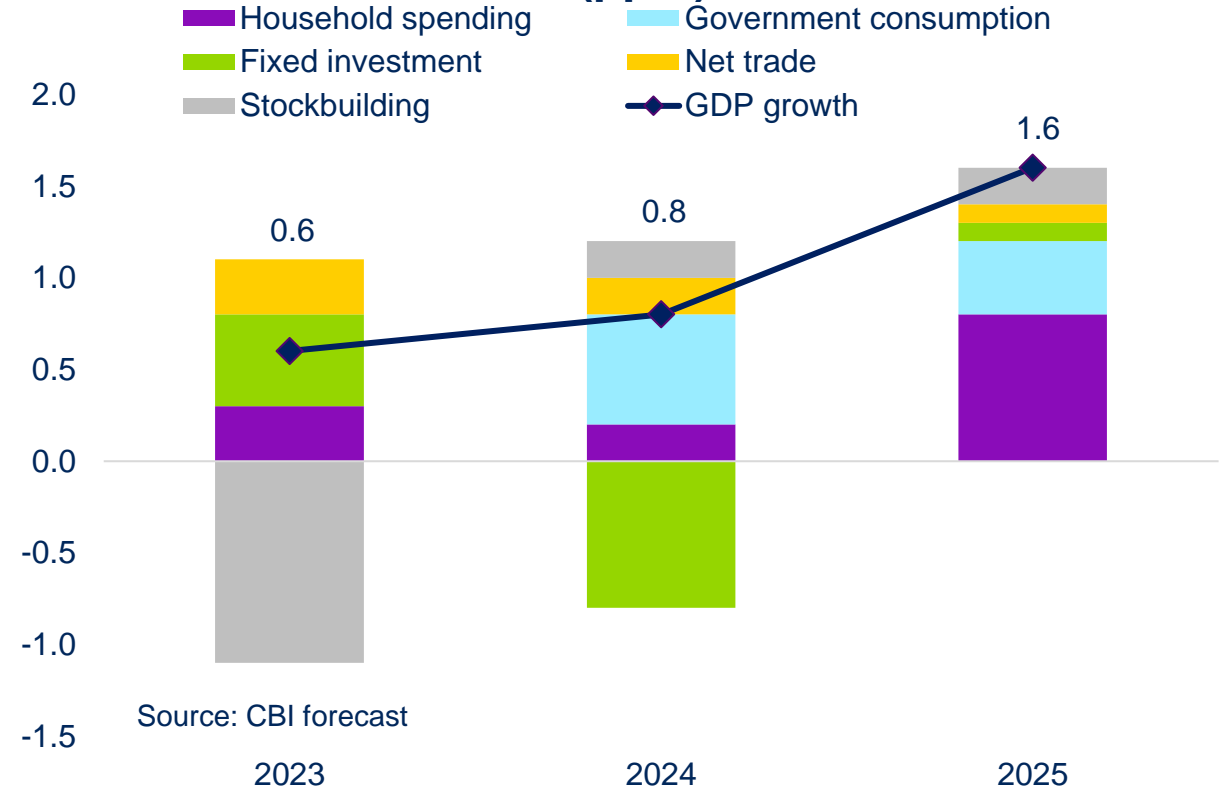


# The growth outlook: a tepid “recovery”

**UK Quarterly GDP Index  
(Q4 2019=100)**



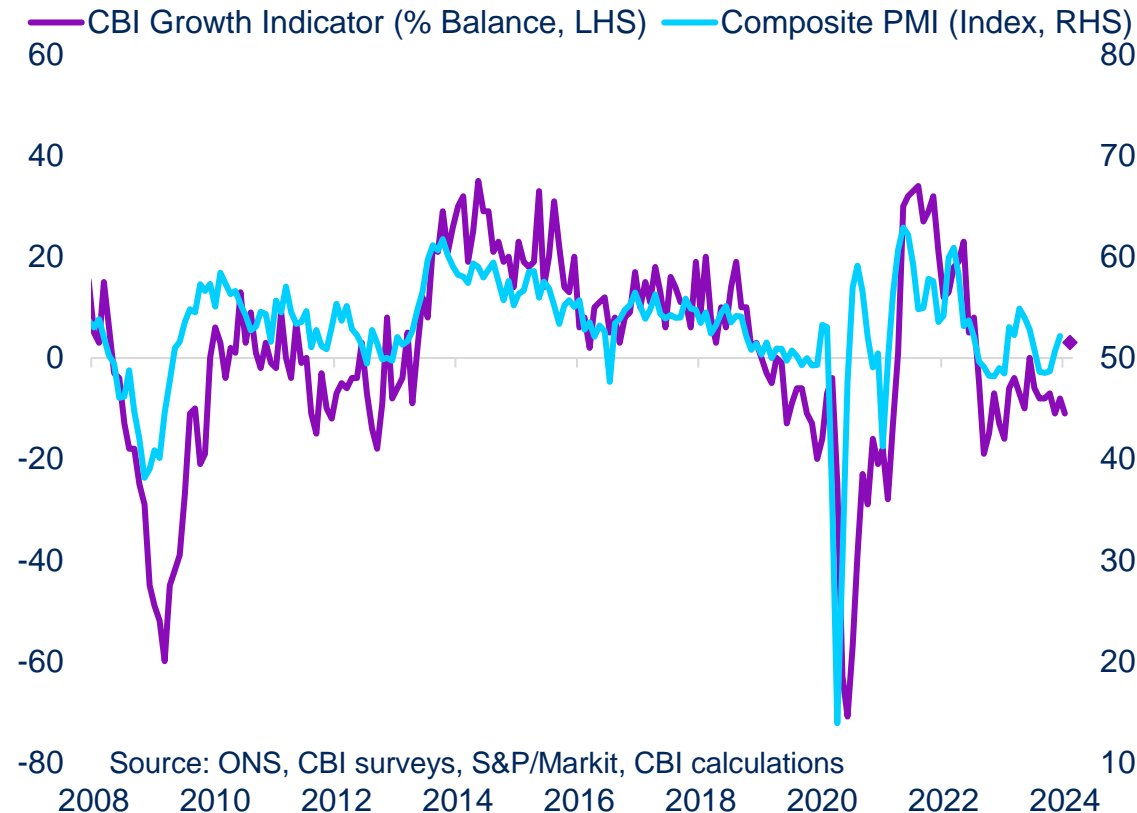
**GDP growth (y/y%) and contributions  
(ppts)**



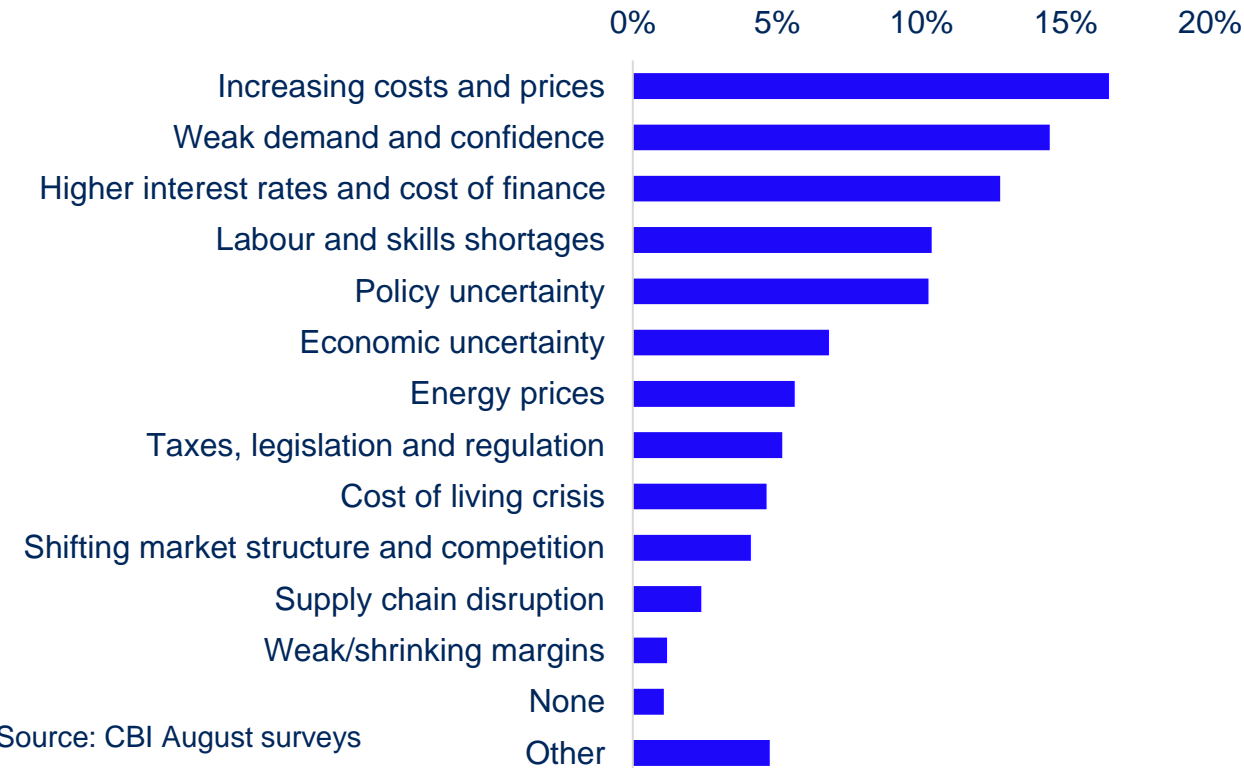
- The economy has only grown minimally over the last one-and-a-half years. Despite recent revisions finding that the UK had a much stronger recovery following the COVID-19 pandemic, economic activity remains subdued with activity flat over Q2 and falling slightly (-0.1%) in Q3.
- Our latest economic forecast expects weak growth momentum to persist over the year ahead. Following growth of 0.6% in 2023, we expect a similar rise in GDP over 2024 (0.8%), strengthening to 1.6% in 2025.

# Multiple headwinds to weak activity

## UK Private Sector Activity

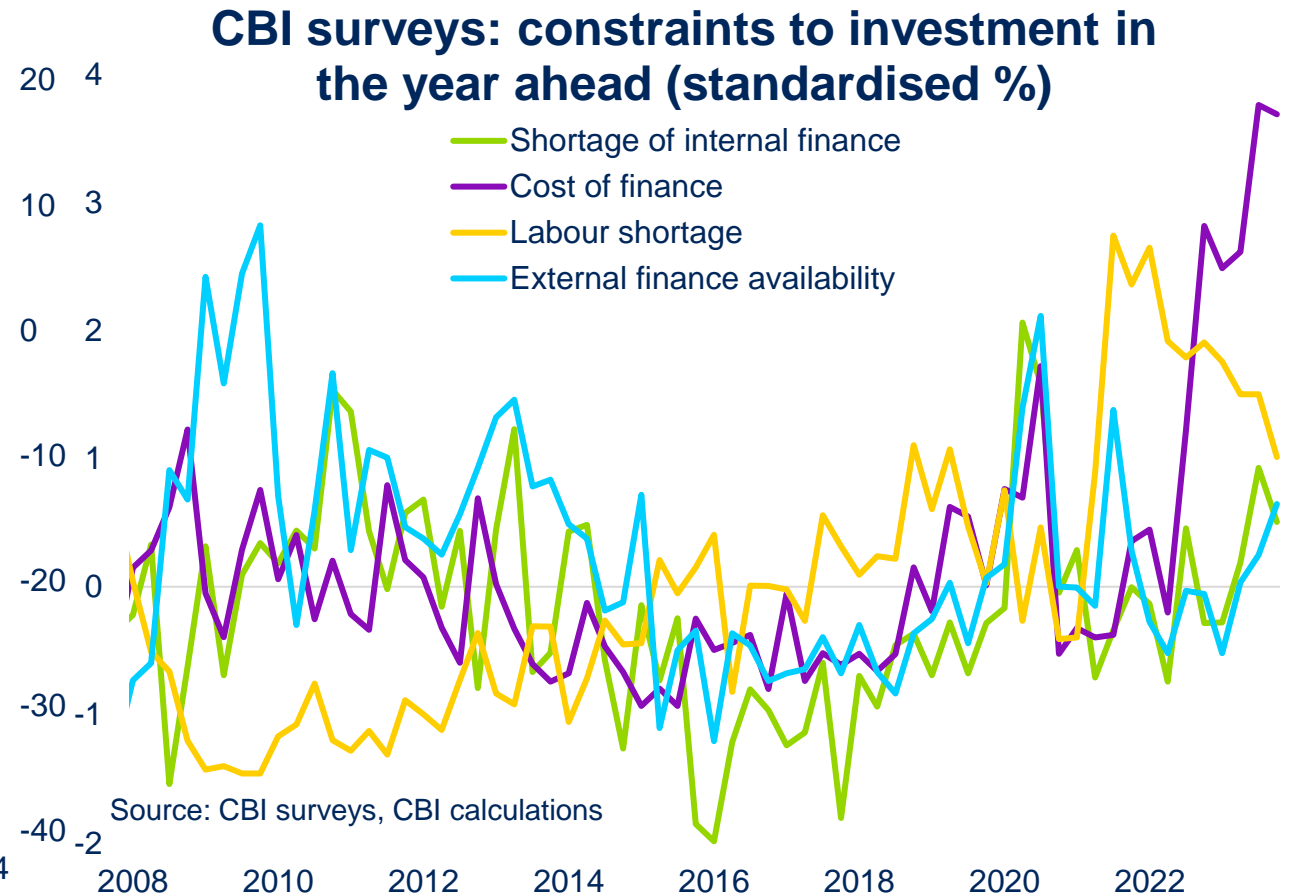
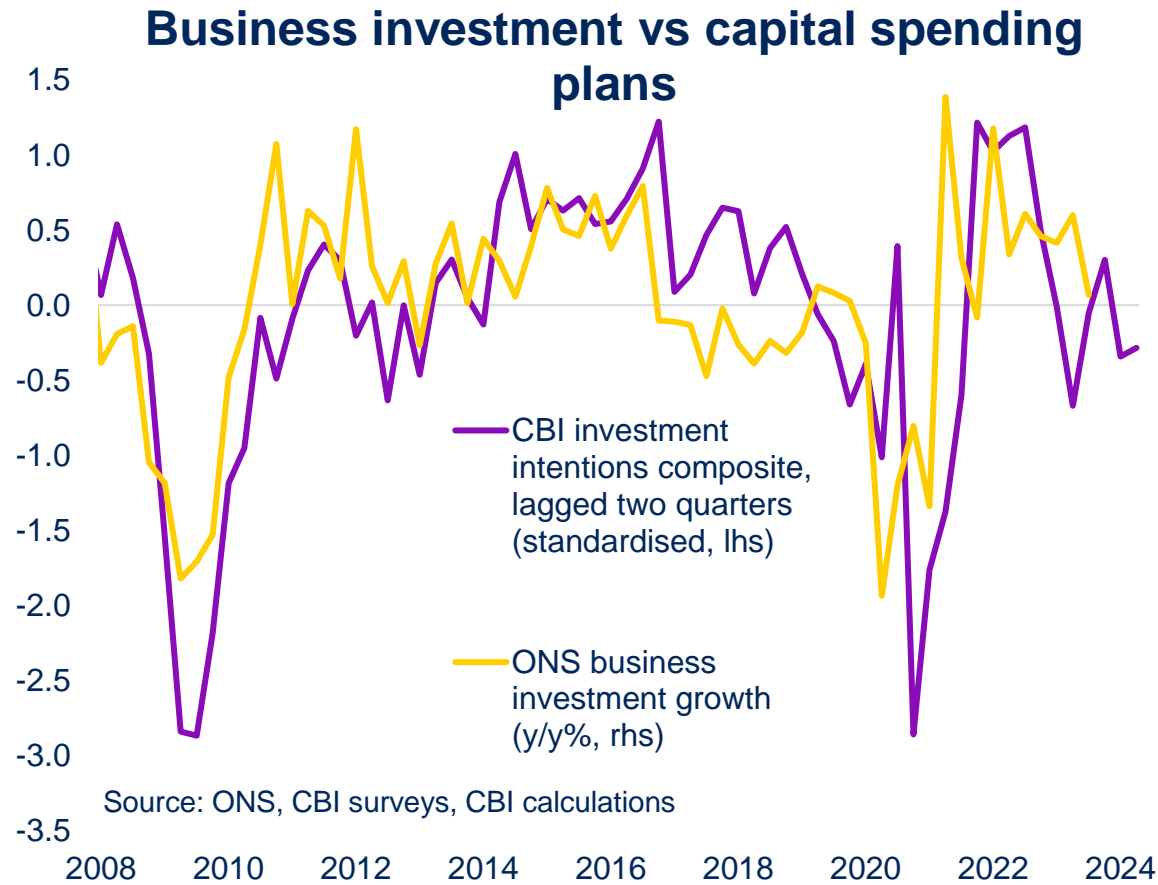


## Economic challenges facing UK businesses over the next 6-12 months (% of responses)



- Our December surveys point to a slight expansion (0.1%) over Q4 as a whole. However, even a slight contraction in December would be enough to tip the UK into a “technical recession”, barring any further revisions.
- Anecdote from our members point to a number of headwinds constraining growth: the most prominent being continually high cost pressures, weakening demand, the growing impact of higher interest rates, and labour shortages. Our conversations with members have also revealed concerns over a number of policy issues, including: the overall regulatory burden, a risk of divergent agendas, the complexity of the planning system; and relatively high political instability.

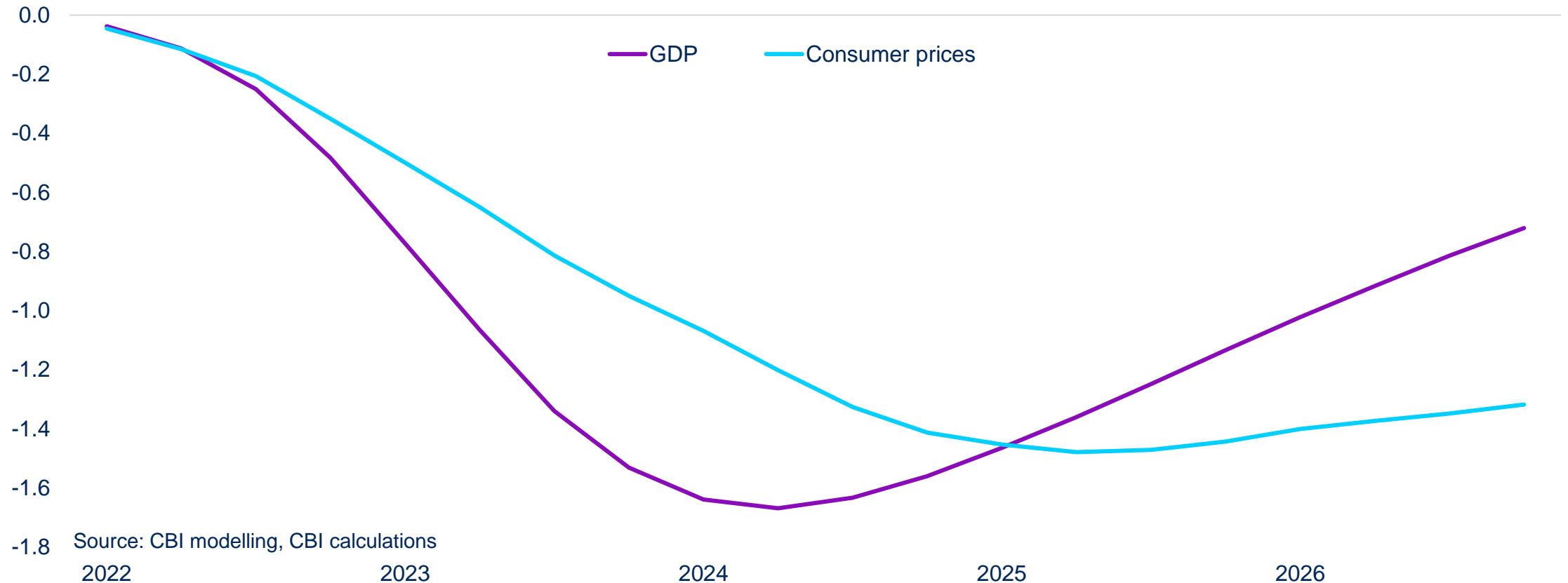
# Investment plans remain soft as the cost of finance becomes a more biting concern



- Business investment growth was relatively resilient through 2023. But capital spending plans for the year ahead look weak.
- Our surveys indicate that the cost of finance is a biting constraint on capex plans, and one that has intensified over the past year, likely in response to increasing interest rates. Wider concerns over finance availability have also been creeping up since the start of 2023.

# Bank rate to remain “higher for longer”

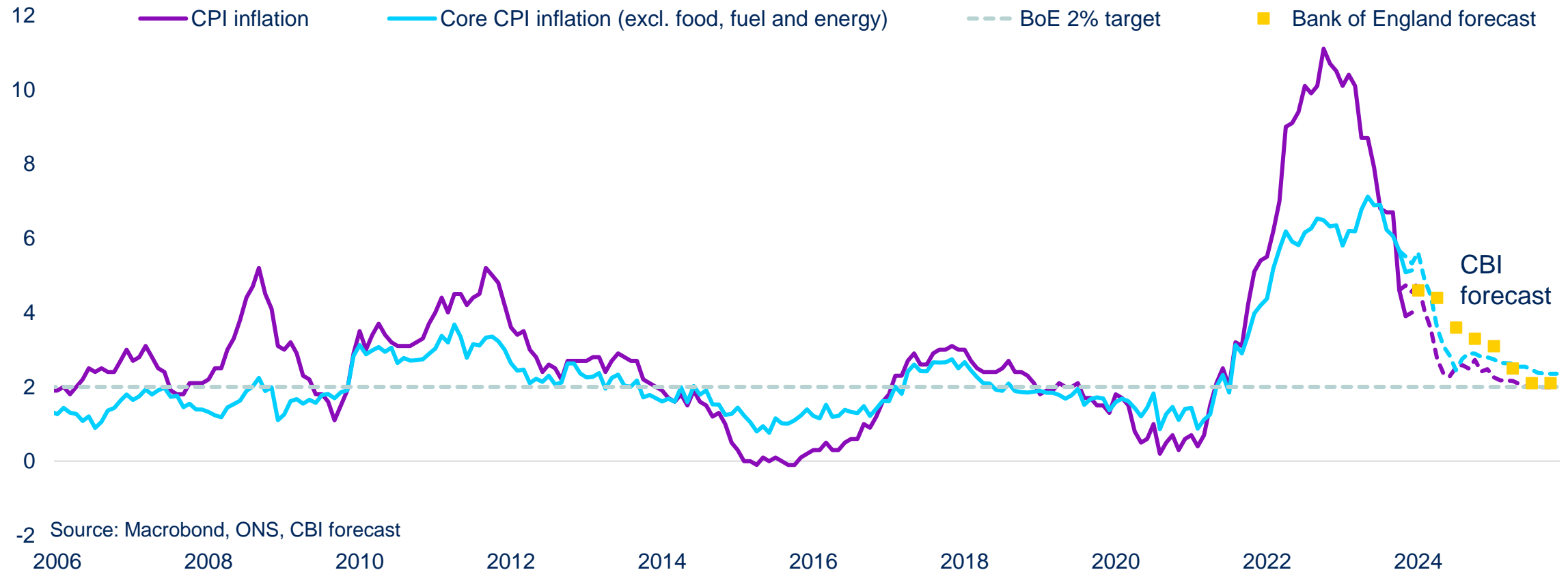
Cumulative impact from rise in Bank rate since end-2021 (%)



- We expect the Bank rate to have peaked at 5.25%, with the Monetary Policy Committee having kept rates unchanged for three consecutive meetings. The Committee have signalled their view that the current Bank rate is sufficiently restrictive to bring inflation back to target and are mindful of weakening economic growth and a loosening in the labour market.
- But the impact of rising interest rates is only just starting to be felt. Our modelling suggests that the peak impact on GDP will hit in the middle of 2024, with the peak impact on prices occurring only a year later. Though these estimates need to be treated with caution.

# Inflation eases, but underlying price pressures remain strong

## CPI inflation and CBI forecast vs Bank of England forecast (y/y%)

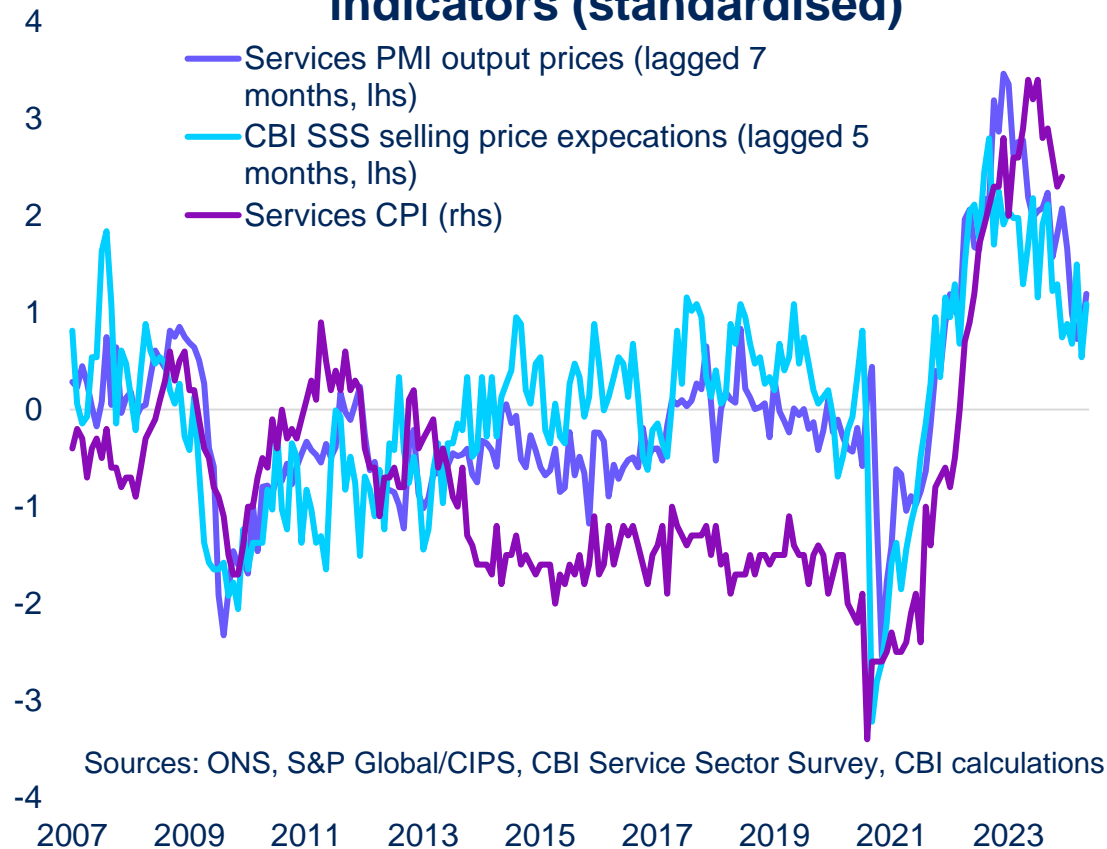


Source: Macrobond, ONS, CBI forecast

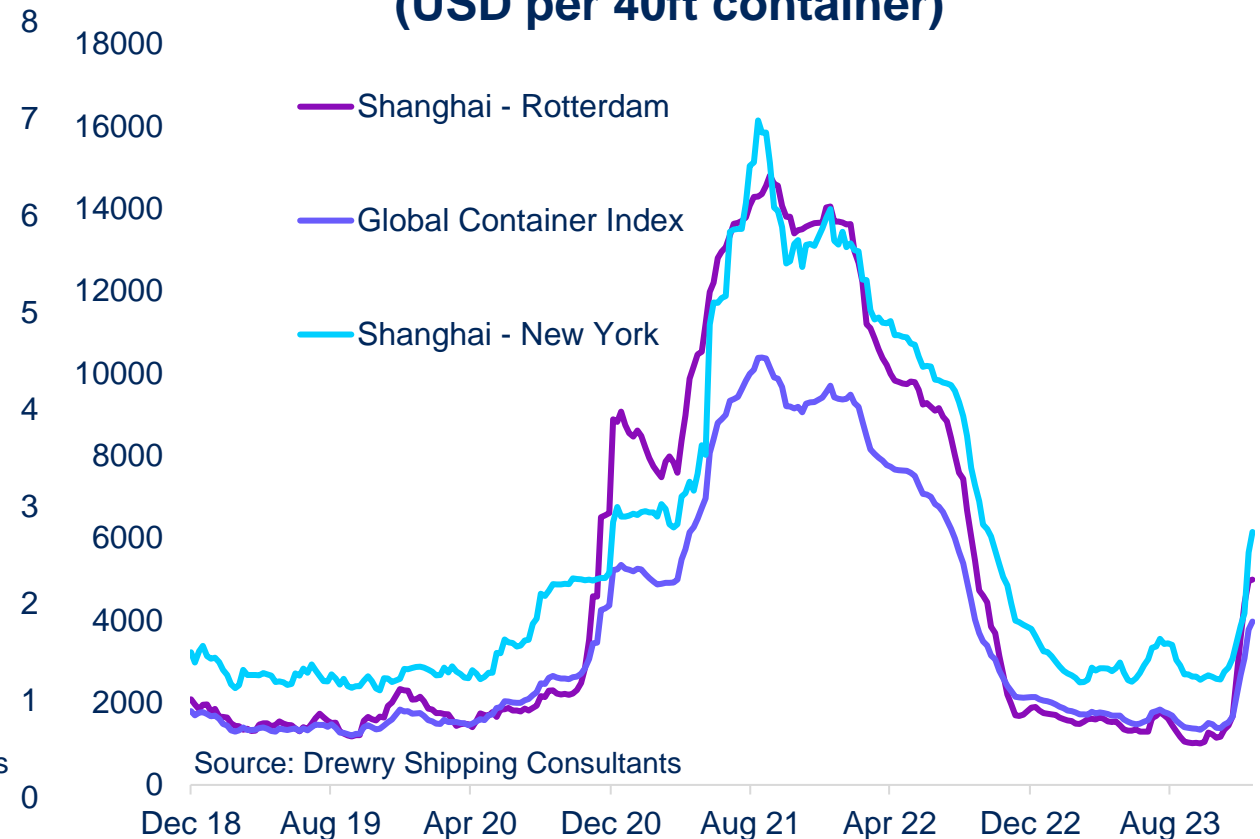
- High inflation has been a strong headwind to economic activity. Headline inflation ticked up to 4% in December (from 3.9% in November) but remains close to two-year lows. Downward pressure in recent months has come from lower energy and transport prices.
- Inflation is expected to tick up slightly again in January, in line with a higher Ofgem price cap from the start of the month, but we still expect some disinflation to come from the goods side. Although the rapid easing of headline inflation in October and November were a surprise, it is too soon to say that domestic price pressures have definitively cooled. Our December forecast assumes inflation will continue to fall gradually this year, but not to hit the Bank's 2% target until mid-2025.

# Inflationary pressures remain heightened

## Services CPI inflation (y/y%) vs survey indicators (standardised)



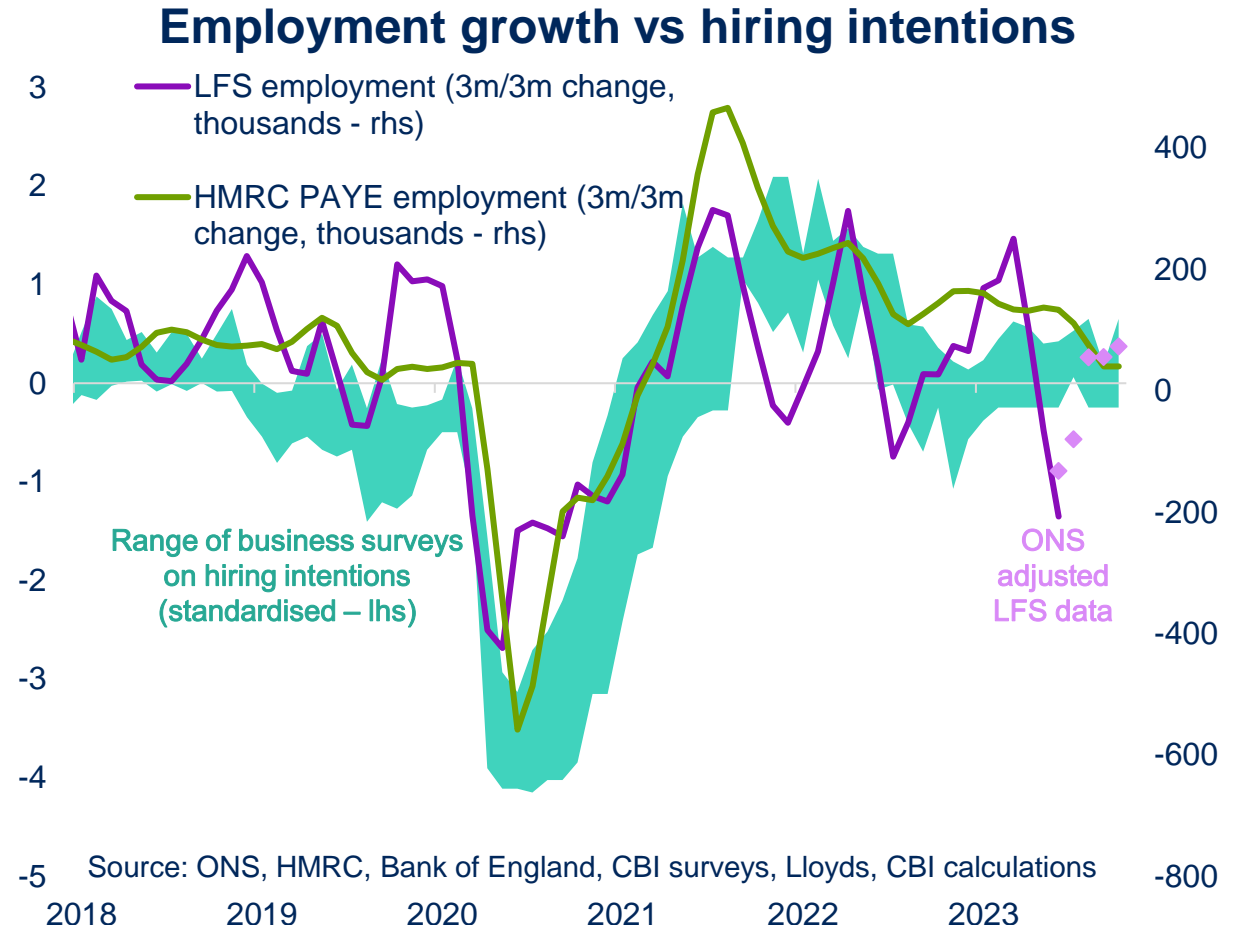
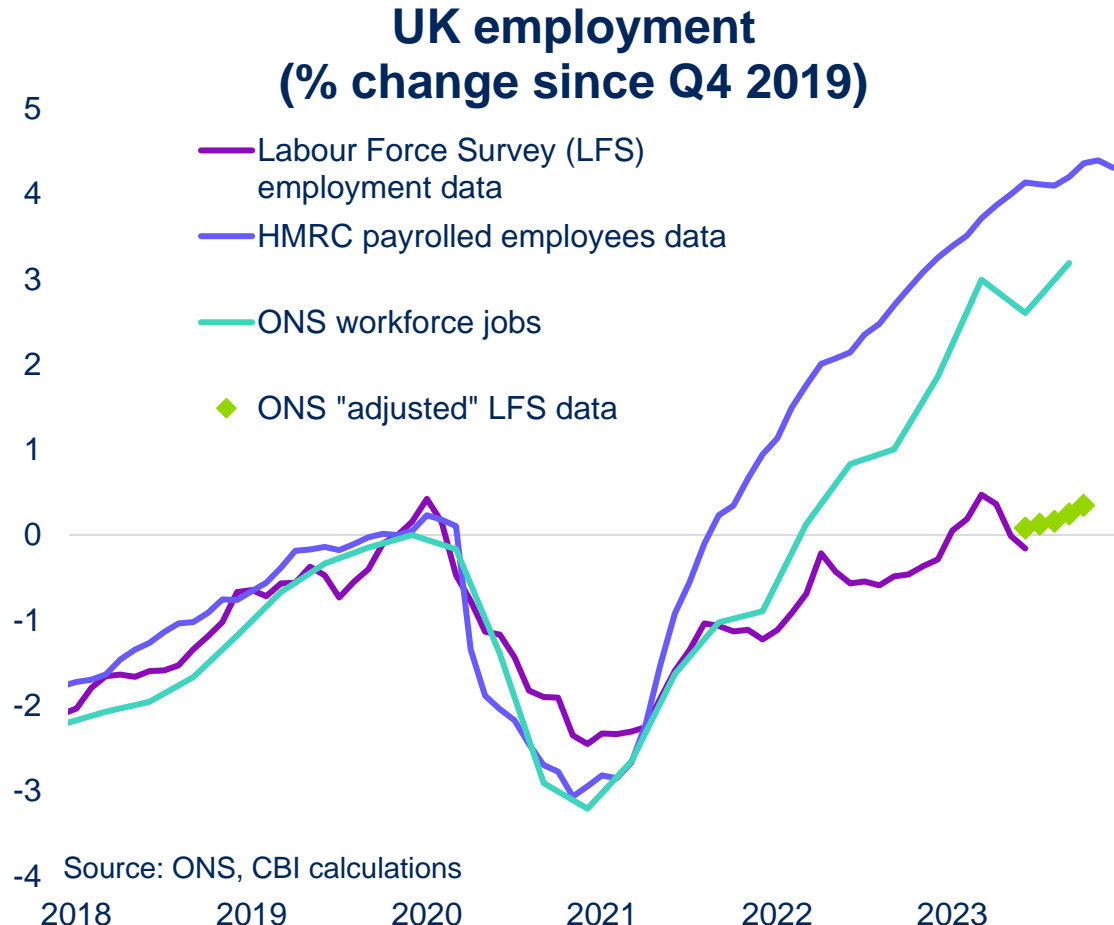
## Ocean freight costs (USD per 40ft container)



- Domestic price pressures remain stubbornly strong, with services inflation having only eased slightly from its 30-year high. A “second round” impact of high inflation poses an upside risk to our forecast of inflation falling back persistently.
- Disruption to shipping in the Red Sea is unlikely to have a major impact on prices in the UK, but if the recent rise in shipping costs is sustained. It could be sufficient to gradually add as much as one percentage point to the rate of UK inflation over the next year.



# What is the UK's true labour market story?



- ONS sampling issues have muddied the water on what is happening with the UK's labour market. This leaves a vacuum of robust labour market data until new estimates are launched in the Spring, complicating assessments of labour market developments and prospects.
- The "adjusted" series produced by the ONS implies that while the labour market is still loosening, it is doing so to a lesser degree than the LFS data suggests. Other measures – such as payrolled employees and workforce jobs – suggest a much stronger labour market picture.
- Survey data (including the CBI's) suggest that hiring intentions have softened over the last year, but the picture still seems to be one of relative resilience.



# This year's General Election presents risks, and opportunities

## CBI members generally welcomed the Autumn Statement, but more is needed

- Positive announcements: Permanent Full Expensing, simplification of the R&D tax credit system, and announcements on grid connectivity.
- Disappointing announcements: very little on skills including no reform to the Apprenticeship Levy, no reform of business rates and how the system works and the R&D system continuing to exclude capital spending.

## 2024 offers a chance to write a more positive UK story

- The UK is at a critical turning point, with some big choices to make this year about its future.
- With the UK on course for another year of weak growth now is the time for leaders to look beyond the short-term crisis management of recent years and deliver a long-term plan to unlock our country's full potential. So, the CBI is calling on political stakeholders to work with business and make the 2020s a decade of sustainable growth, resilience and opportunity that it could – and needs – to be.

## Politics comes to the fore in an election year

- We know that we are in an election year and politics will increasingly take centre-stage and we will tailor our Spring Budget submission, accordingly, ensuring that we put down markers for the next government on the CBI's Business Manifesto asks such as broader reform of the Apprenticeship Levy and Business Rates for example, while including specific asks this government can implement in the short-term.
- We are putting forward the following themes in our submission to the Chancellor:
  1. Taking further action to address labour shortages
  2. Addressing barriers to growth and business investment
  3. Setting out the next steps on net zero

## What did CBI members think of the Autumn Statement?

Very positive	8%
Somewhat positive	51%
Neutral	24%
Somewhat negative	14%
Very negative	3%

**Anna Leach**

Deputy Chief Economist, CBI

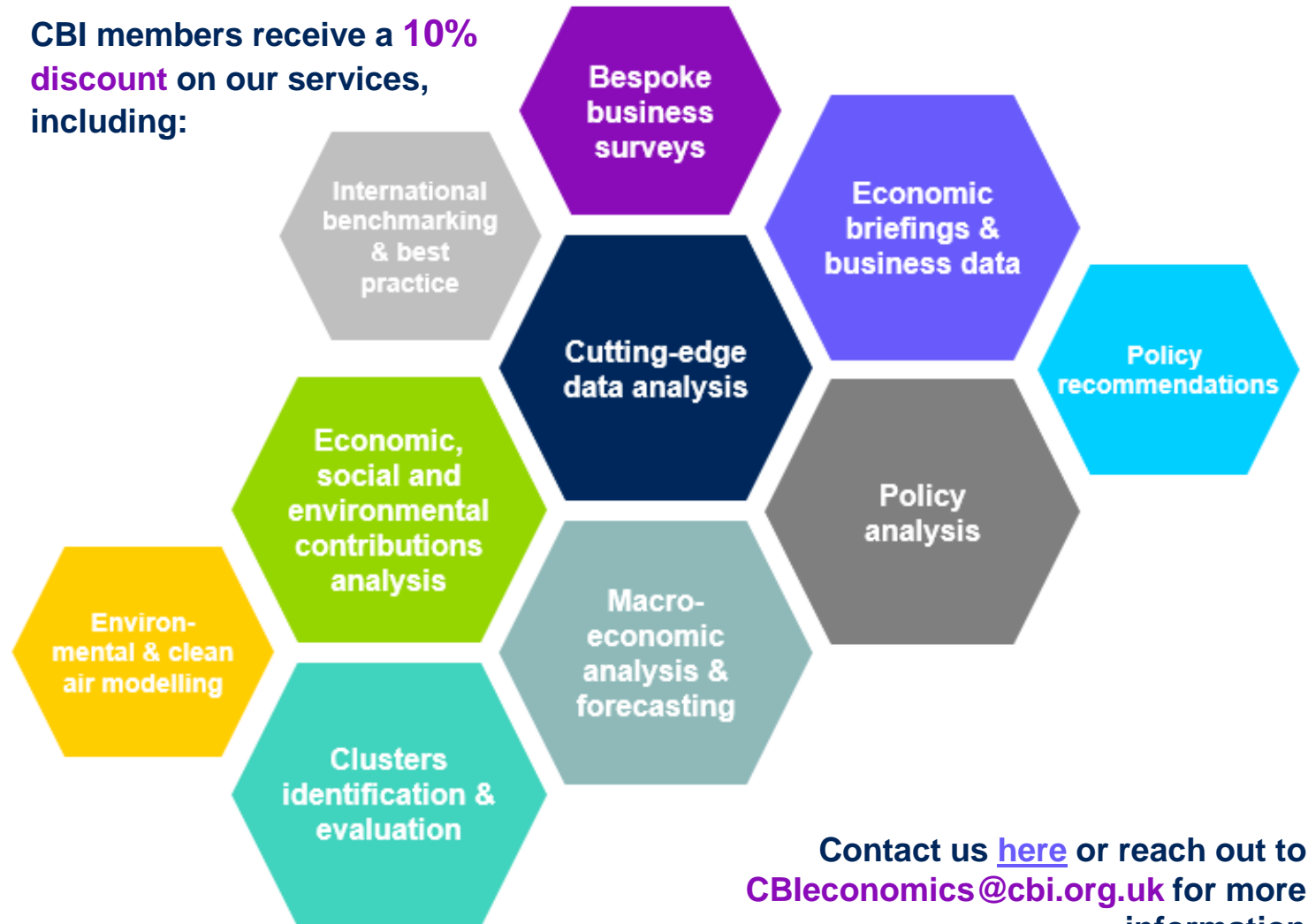
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