UNITED KINGDOM
2024-2025 SCENARIO

TOWARDS MORE MODERATE GROWTH RATES

October 2024

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WORKING EVERY DAY IN YOUR INTEREST AND FOR SOCIETY

GROUP ECONOMIC RESEARCH

SLOWDOWN AFTER SOLID FIRST-HALF GROWTH

Scenario highlights

- **The impacts of past price shocks and rate hikes are dissipating.**
- **Real wages will continue to recover, albeit at a slower pace, eventually fuelling private consumption.**
- **Monetary easing and the Labour government's policy will bolster private investment.**
- **A more flexible fiscal framework should increase investment and limit budget cuts, but not without an increase in taxation.**
- **Inflation is finally surprising favorably. It is expected to rebound in Q4 2024 before falling sharply in early 2025.**
- **The BoE could step up its rate cut cycle in 2025.**

	2022	2023	2024	2025
% annual change				
GDP	4.8	0.3	1.0	1.5
Household consumption	7.3	0.5	0.8	1.9
Public consumption	0.6	0.6	1.9	1.6
Investment	5.1	-0.1	1.3	3.1
Inflation	9.1	7.3	2.6	2.1
Unemployment rate %	3.9	4.1	4.6	4.7
Contribution to GDP growth, pp				
Domestic demand	5.1	-0.1	3.8	4.0
Net exports	-0.3	0.5	-3.0	-2.6
Change in inventories	0.8	-0.9	0.1	0.4

Sources: ONS, Crédit Agricole S.A./ECO.

UK economic growth was sluggish in 2023, with a slight recession in H2 2023, as past shocks on producer costs and consumer prices coupled with tight monetary policy weighed on demand. Economic activity grew strongly in H1 2024 on expectations of monetary policy easing (which the Bank of England effectively started in August 2024), but growth is expected to slow going forward to an expected +0.3% QoQ in Q3 and Q4. Indeed, private consumption remains weak as households continue to be excessively cautious owing to past price shocks, high interest rates and the ongoing easing in the labour market.

Growth is expected to accelerate slightly in 2025 with domestic demand being its main driver supported by still strong household real-income growth. Investment should also make a positive contribution to growth, the outlook being underpinned by an upward bias thanks to the pro-business, pro-investment policy of the Labour government.

Inflation returned to the 2% target in May 2024 and has been volatile since then. After a plunge below target in September, it should rebound above target in Q4, on higher gas and electricity prices, but is expected to return to target by mid-2025.

Consistent with expectations, the BoE began its monetary easing cycle in August with a 25bp cut and announced gradual rate cuts ahead. We expect one additional 25bp rate cut by the end of the year, in November, but a faster pace of cuts in 2025.

SLOWDOWN AFTER SOLID FIRST-HALF GROWTH

INFLATION WILL RISE TEMPORARILY IN Q4 BEFORE EASING IN 2025

Solid growth in H1 2024 pushes up our growth forecasts

After a vigorous growth in Q1 and Q2 2024 (0.7% and 0.5% QoQ), we expect GDP growth to slow to in H2 2024 to 0.3% per quarter and then pick up further to 0.4% per quarter on average in 2025. On an annual average basis, we have raised our growth forecast by 0.1 pp per year in 2024 and 2025 to 1.0% and 1.5% respectively. This upwards revision is motivated entirely by H1 2024 growth, which exceeded expectations but did not appear to be sustainable. And, indeed, GDP growth proved flat in June and July. Underlying domestic demand is weak. Growth in household consumption came out at just 0.2% QoQ in Q2, decelerating compared with Q1. Gross fixed capital formation also slowed in Q2, driven down by real estate investment, while business investment increased for the third consecutive quarter (+1.4% QoQ after +0.6% QoQ in Q2). Business climate surveys have continued to improve, suggesting activity is expanding moderately in services, industry and construction.

A light at the end of the tunnel for consumers

UK consumers continue to favour precautionary savings (with the ONS estimating the savings rate at 10% in Q2, after 8.9% in Q1) over consuming and investing. The savings surplus built up since the pandemic now exceeds GBP450bn. Consumer confidence is being undermined by past price shocks and still high interest rates, together with uncertainties over the new Labour government's fiscal policy and the easing of the job market. According to the Gfk survey, confidence sagged in September for the first time in seven months. The survey shows lower expectations relative to the economic situation and personal finances for the next 12 months.

But the factors conducive to a gradual acceleration in household consumption are all there. Growth in real wages has held up for several quarters and should stay clearly positive through the forecast period, thanks to inflation's expected ebb in 2025 (after a spike anticipated in Q4 2024). While high rates will continue to impact indebted households, specifically those that will need to renew their fixed-rate loans again, the peak impact of past monetary tightening is largely behind us. The monetary easing to come should encourage households less to save and more to consume and invest. We expect private consumption to pick up slightly, with an average annual increase of 0.8% in 2024 and 1.9% in 2025 after just 0.5% in 2023.

Uncertainties related to the 30 October budget

In the short term, uncertainties over the Autumn Statement are undermining confidence. Prime Minister Keir Starmer has already warned that this will be a "painful" budget and that "things will get worse before they get better". Tax hikes to finance a GBP22bn hole (0.8% of GDP) in the public accounts will most likely be heftier than promised during the electoral campaign. However, the growth impact of an increase in current government spending financed by an increase in taxes should be broadly neutral for growth, given similar tax multipliers, while the increase in investment spending should have a positive impact on the outlook, given the highest tax multiplier. Moreover, an industrial government strategy aiming to support business investment in green energy and housing construction should boost confidence and be positive for the growth outlook.

With public debt exceeding 100% of GDP and a higher-than-expected budget deficit in the first few months of the current fiscal year (GBP64.1bn vs. GBP57.8bn forecast for the April-August period), the government is "walking on thin ice". Its intention to adjust the fiscal mandate in order to generate a room for manoeuvre for investment is already worrying the markets. In particular, the government intends to change the way public debt is accounted for (see page 13). The challenge is safeguarding credibility with the financial markets and avoiding the risk of a new crisis on the gilt markets.

The removal of uncertainty once the 30 October budget is passed has the potential to drive a stronger recovery in business and consumer confidence, posing some upward risks on our forecasts. What's more, the BoE may front-load its monetary easing based on pleasant surprises on the inflation front, which would support growth and give the government back some leeway.

SLOWDOWN AFTER SOLID FIRST-HALF GROWTH

INFLATION WILL RISE TEMPORARILY IN Q4 BEFORE EASING IN 2025

Disinflation is expected to pick up in 2025, increasing the chances of more rate cuts

We expect an additional 25bp rate cut this year, in November, when the BoE updates its inflation forecasts. Inflation is expected to be volatile in the last few months of the year. It is expected to decline to 1.9% in September on falling oil prices and then increase in Q4 to an average of 2.6% over the quarter, the result of a 10% rise in administered gas and electricity prices in October, together with less favourable base effects on energy prices. We expect inflation to drop swiftly in H1 2025, returning to the target by mid-year and falling to 1.8% in Q4 2025. Furthermore, we are forecasting a sharp decrease in service inflation in H1 2025, leading to a decline in the core inflation rate to 1.8% in July.

With disinflation expected to accelerate next year, and in the absence of any additional shock on prices, the BoE could step up monetary easing. We now expect two additional rate cuts in H2 2025 and a total of six cuts over the year. The key rate is thus expected to reach 3.25% in December 2025.

Completed on 14 October 2024

INTRODUCTION

THE INTERNATIONAL ENVIRONMENT

With growth slowing in its two main partner regions – the eurozone and the United States – UK GDP growth will hinge primarily on momentum in domestic demand. In the eurozone, we are forecasting GDP growth of 0.8% in 2024 and 1.3% in 2025. The recovery in eurozone domestic demand is lagging and will likely come at a more moderate pace than previously expected. We expect US growth to slow substantially towards the end of the year, though a recession is no longer on the cards. Growth is expected to reach 2.5% in 2024, the same as in 2023, before slipping to 1.3% in 2025. Headline inflation is expected to average around 2.9% in 2024 and 2.2% in 2025. In China, the stimulus plan aimed at revitalising a slackening economy is expected to generate GDP growth of 4.7% in 2024 and 4.2% in 2025. Despite weak demand, control over supply should allow the oil market to gradually return to equilibrium, with prices at around $80 per barrel.

The monetary easing process is thus set to continue. In the United States, the cumulative decrease is expected to come out at 100bp in 2024 and an identical 100bp in 2025. The upper bound of the *Fed Funds* rate will thus fall from 4.5% at end-2024 to 3.5% in Q3 2025. The ECB is expected to maintain the pace of cuts initiated in June and September, with a 25bp rate cut per quarter until the deposit rate reaches 2.50% in September 2025. Market interest rates have already taken a substantial downward turn and the potential for further decline is limited. In the United States, ten-year yields are expected to reach 3.80% at end-2024 and 3.60% at end-2025. In the eurozone, the Bund yield is expected to nudge 2.15% at end-2024 and 2.30% at end-2025.

International background assumptions

	2023	2024	2025	2023				2024				2025			
				T1	T2	T3	T4	T1	T2	T3	T4	T1	T2	T3	T4
World GDP (y/y, q/q, %)	3.3	3.0	2.7	-	-	-	-	-	-	-	-	-	-	-	-
United States GDP (y/y, q/q, annualised, %)	2.5	2.5	1.3	2.8	2.5	4.4	3.2	1.6	3.0	1.7	0.5	0.8	1.4	1.7	2.0
Eurozone GDP (y/y, q/q, %)	0.5	0.8	1.3	0.5	0.1	0.0	0.1	0.3	0.2	0.4	0.3	0.3	0.4	0.3	0.4
China GDP (y/y, q/q, %)	5.2	4.7	4.2	1.8	0.8	1.5	1.2	1.6	0.6	1.1	1.1	1.1	1.0	1.0	1.0
ECB deposit rate (end of period, %)	4.00	3.25	2.50	3.00	3.50	4.00	4.00	4.00	3.75	3.50	3.25	3.00	2.75	2.50	2.50
Federal Reserve funds rate (end of period, %)	5.50	4.50	3.50	5.00	5.50	5.50	5.50	5.50	5.50	5.00	4.50	4.00	3.75	3.50	3.50
Exchange rate (average, EUR/USD)	1.08	1.09	1.10	1.07	1.09	1.09	1.08	1.09	1.08	1.10	1.08	1.08	1.09	1.10	1.12
Brent (average, USD/barrel)	82.2	80.9	80.5	82.2	77.9	85.9	83.0	81.9	85.0	78.9	78.0	75.0	80.0	82.0	85.0

Sources: BoE, ECB, Eurostat, IMF, Refinitiv, Federal Reserve, Crédit Agricole S.A./ECO.

CYCLICAL DEVELOPMENTS

EXPECTED GROWTH RATE OF +0.3% IN Q3 AFTER +0.5% IN Q2 2024

Activity returned to growth in 2024. The economy recovered the losses recorded during the recession of H2 2023 with a higher-than-expected increase in GDP in H1 2024 (+0.7% QoQ in Q1 and +0.5% QoQ in Q2). Real GDP is 1.2% higher than in Q4 2023 and 2.9% higher than before Covid – the worst performance by a G7 country apart from Germany (whose real GDP is barely 0.2% above its Q4 2019 level). Real GDP per capita gained 0.5% in Q1 and 0.2% in Q2, after six consecutive quarters of negative or zero growth. This still leaves GDP per capita 0.3% lower than a year ago.

Domestic demand is driving the recovery. Domestic demand made the largest contribution to growth in H1 2024 (+2.7pp in Q2, after +0.6pp in Q1), while the external balance contributed negatively overall (-2.2pp in Q2, after +0.1pp in Q1). Among the main contributors to growth were public and private consumption, changes in inventories and investment, particularly business investment. Household consumption was the main contributor to growth in Q1 (+0.4pp) but decelerated in Q2 (+0.2% QoQ in Q2, after +0.6% QoQ in Q1), still below the growth rate of real gross disposable income (1.3% QoQ in Q2, after 1.6% QoQ in Q1), which led to an increase in the savings rate to 10% in Q2 (vs. 8.9% in Q1). Monthly retail sales data suggest a solid increase in consumer spending in Q3, up 1% MoM in August after +0.7% MoM in July. Business investment has picked up over the past three quarters, though margins dipped in Q2.

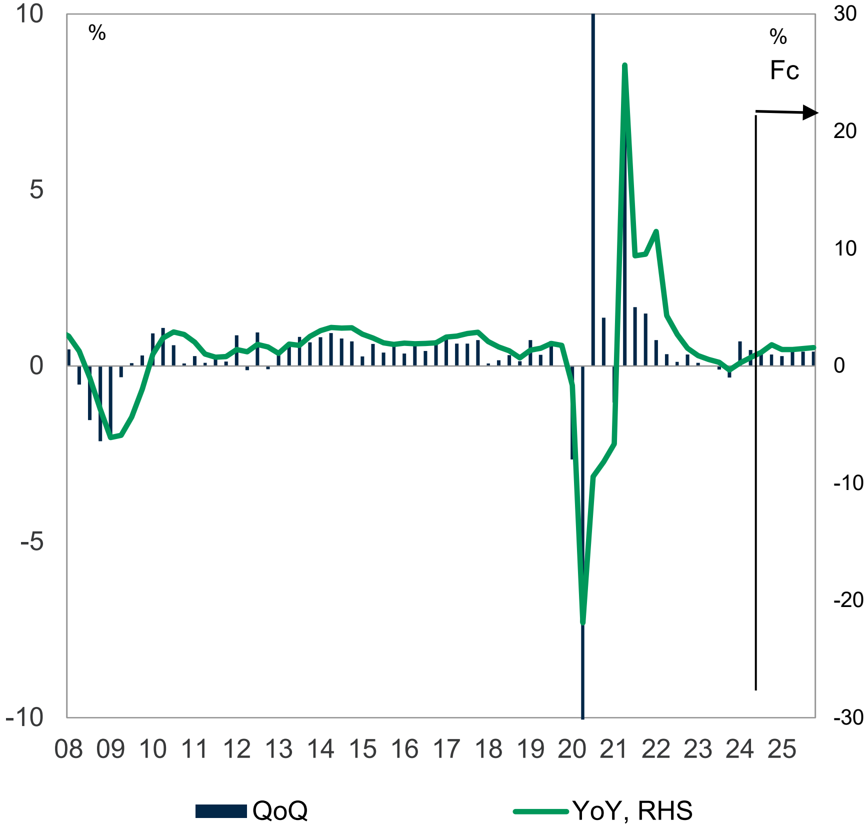
Economic data for Q3 point to a slowdown in the pace of growth. Monthly real GDP was stable in June and July followed by a 0.2% rebound in August. The services sector was the main contributor to growth, with barely positive growth (+0.1%) in the last three months to end-August, with the professional, scientific and technical sectors gaining 0.8% over the period, followed by information and communication. Industrial production growth came out at zero, while the construction sector gained 1%. The carry-over effect for Q3 stands at a mere 0.1pp, which does not call into question our growth forecast of 0.3% for the quarter, assuming a rebound of at least 0.4% in September.

PMI surveys have remained above the 50-threshold signalling expansion of activity, but uncertainties over the Autumn Statement on 30 October are undermining confidence. The surveys point to moderate growth in services, supported by an improvement in domestic demand, while external demand is sluggish. New orders are accelerating sharply, driven in particular by an increase in investment spending since the elections. In other positive news, domestic inflationary pressures fell for the third consecutive month, reaching their lowest level since February 2021. While some services companies are postponing their investment decisions pending the Autumn Statement, most of them expect business activity to increase in the coming year. Lower borrowing costs, moderating inflationary pressures and forthcoming monetary easing are contributing to the improvement in economic expectations. Regarding the industrial sector, in September, the PMI remained in expansion territory for the fifth consecutive month. Production volumes picked up in Q3 relative to Q2. The main driver was domestic demand, particularly in the consumer goods and intermediate goods sectors, while the investment goods sector contracted once again. As in the services sector, companies have adopted a wait-and-see attitude ahead of the 30 October budget, with confidence shrinking in September. However, in terms of inflationary pressures, the industry survey points to a further acceleration in input prices, which are growing at their highest rate since January 2023. The prices of certain materials continue to rise as a result of the increase in freight rates and the lengthening of maritime routes subsequent to the conflict in the Near East.

CYCLICAL DEVELOPMENTS

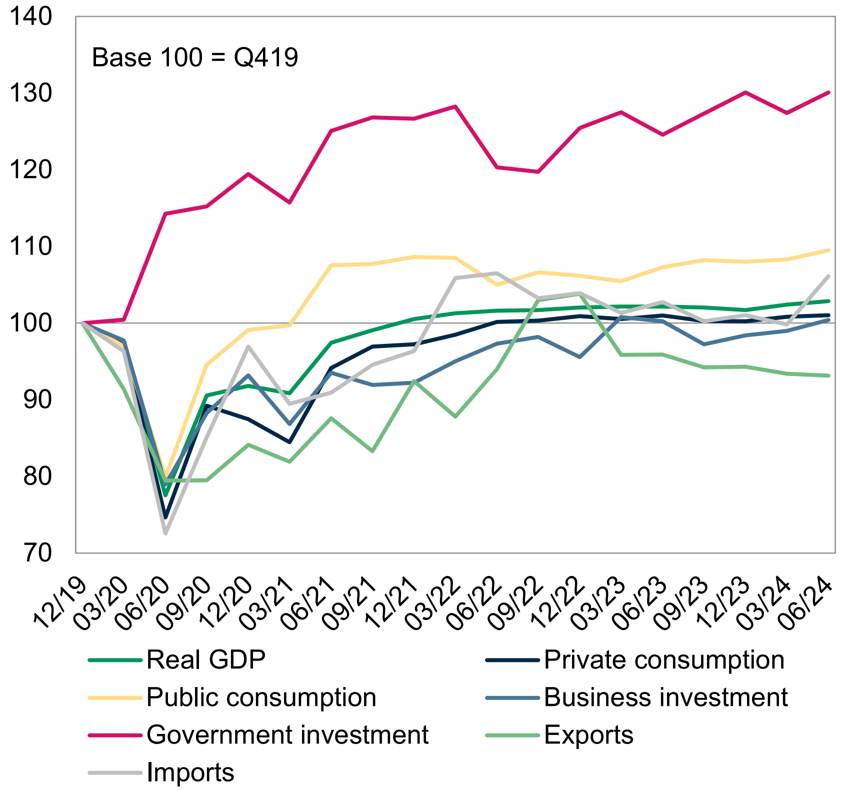
REAL GDP

Real GDP growth



Sources: ONS, Crédit Agricole S.A./ECO.

Evolution of real GDP and its components since Covid

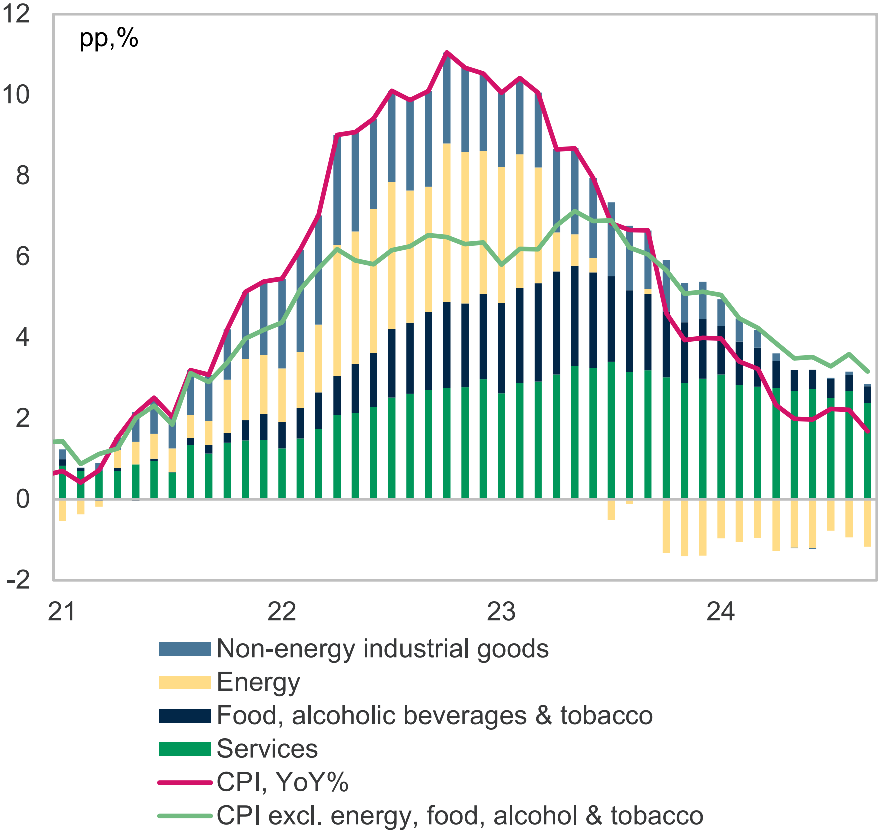


Sources: Gfk, Crédit Agricole S.A./ECO.

CYCLICAL DEVELOPMENTS

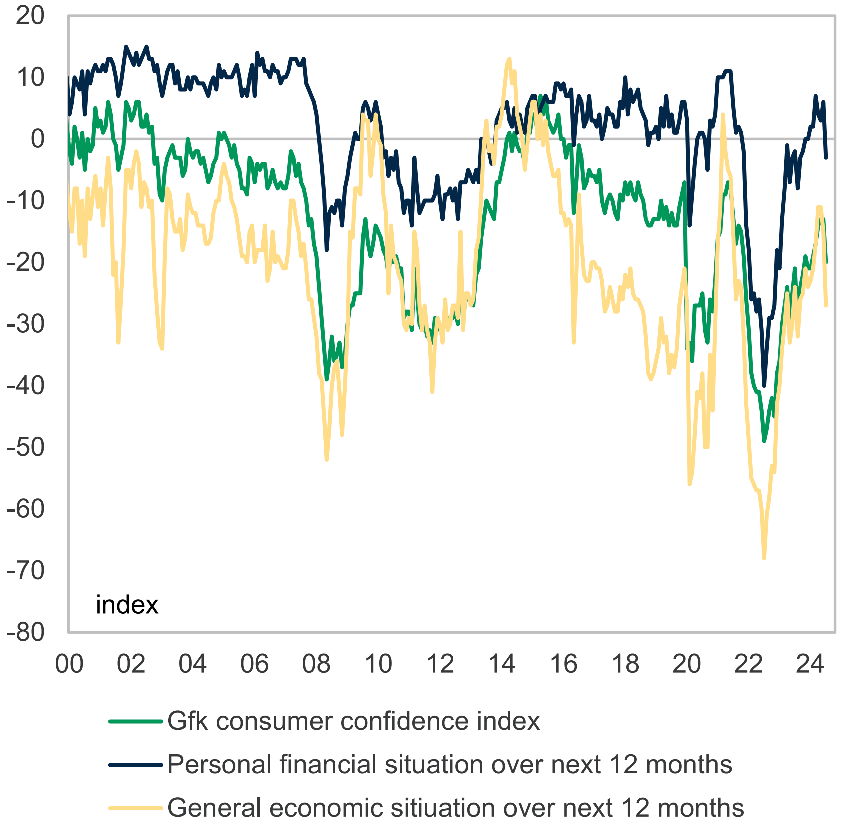
HOUSEHOLDS STILL CAUTIOUS DESPITE FALLING INFLATION

CPI inflation stabilised at 2.2% in July and August



Sources: ONS, Crédit Agricole S.A./ECO.

Consumer sentiment dipped again over the summer



Sources: Gfk, Crédit Agricole S.A./ECO.

HOUSEHOLDS

RELAPSE – LIKELY TEMPORARY – IN HOUSEHOLD CONFIDENCE

Households are worried about the government's upcoming policy moves.

In contrast to the sharp recovery in retail sales in July and August, consumer confidence dipped considerably in September. The Gfk index contracted by 7 points to -20, a low since March. All the components of the index are deteriorating, but the biggest corrections were linked to the outlook for personal financial situations for the next 12 months (-9 points), the outlook for the general economy in the coming year (-12 points) and the major purchase index (-10 points). The government's warnings about the difficult decisions that need to be made in the 30 October budget appear to be central to this waning confidence, with households worried about higher taxes and cuts in public spending and family benefits.

The government is expected to honour its commitment not to raise key taxes in the *Autumn Statement*, as promised during its election campaign. Instead, the government is expected to announce a host of secondary tax increases (VAT on private tuition fees, increased tax on profits in the oil and gas sector, on fuel, alcohol, tobacco, and a higher inheritance tax and capital gains tax). In addition to these increases, the government is looking to take tougher measures against tax evasion. The aim is to generate tax revenue of at least GBP20bn in the next five years to avoid massive cuts in the expenditure of "unprotected" ministries. The government is also seeking to expand its room for manoeuvre in terms of investment by tweaking accounting rules (see *page 13*).

Expected recovery in confidence once uncertainty dissipates. We expect consumer confidence to improve once the 30 October budget is passed. But a certain degree of caution is likely to persist. Some households have yet to see an increase in their debt-servicing cost after the rise in rates. According to the BoE, one-third of the GDP impact of past rate hikes has not yet occurred. The borrowing costs of some households with fixed-rate mortgages will increase if they have to renew their loans at higher rights once they reach their term. Households also expect the unemployment rate to rise as demand for labour continues to fall.

However, there are good reasons to expect a gradual acceleration in household consumption.

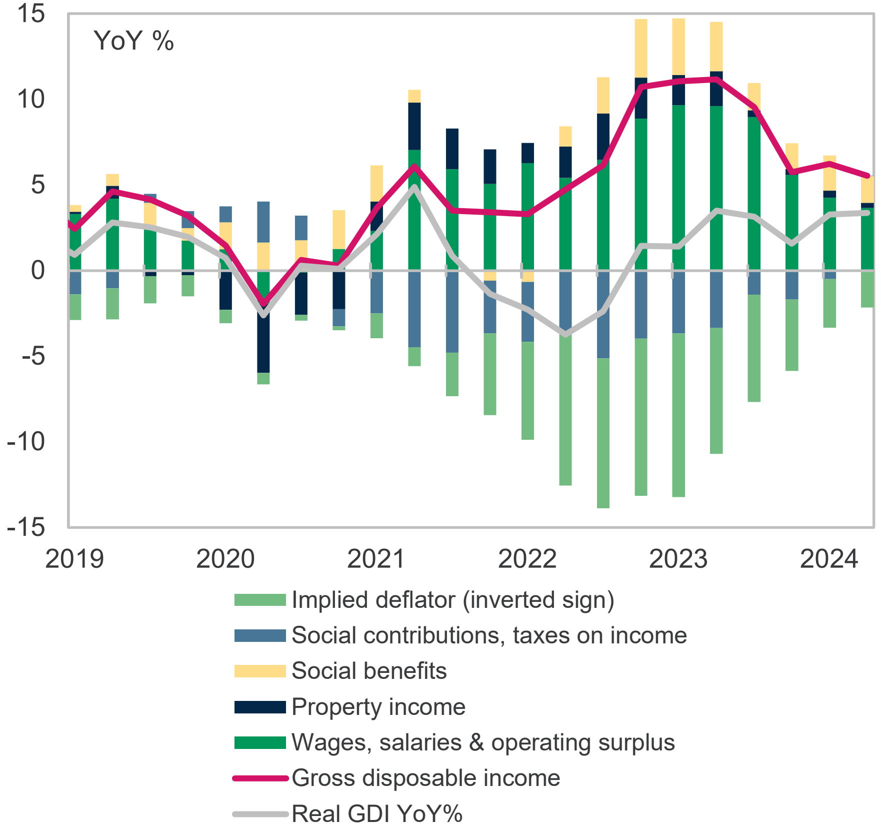
Real wage growth has been strong for several quarters and should remain largely positive throughout our forecast horizon owing to the expected decline in inflation in 2025 (after an expected reacceleration in Q4 2024). Although high interest rates continue to impact the finances of indebted households, particularly those having yet to renew their fixed-rate loans, the peak impact of past monetary tightening is far behind us and upcoming monetary easing should encourage households to save less and consume and invest more. Real disposable income continued to grow strongly, gaining 3.4% YoY in Q1 2024. After falling by 2.8% between Q3 2021 and Q3 2022, it is now 1.8% higher than in Q2 2021. The recovery stems primarily from strong growth in activity income (wages, mixed income) and the decline in inflation. Growth in earned income is slowing but remains robust, at nearly 4% YoY in Q2 2024, while the growth rate of the implicit consumption deflator dipped to 2.2% (compared with a high of 9.6% in Q1 2023). Real disposable income is expected to slow in Q4 2024 as inflation rises temporarily and wage growth continues to moderate but should remain strong throughout 2025.

Given these contrasting factors, we expect household consumption to firm up gradually, with average annual growth remaining low this year, at 0.8%, before increasing to 1.9% in 2025.

HOUSEHOLDS

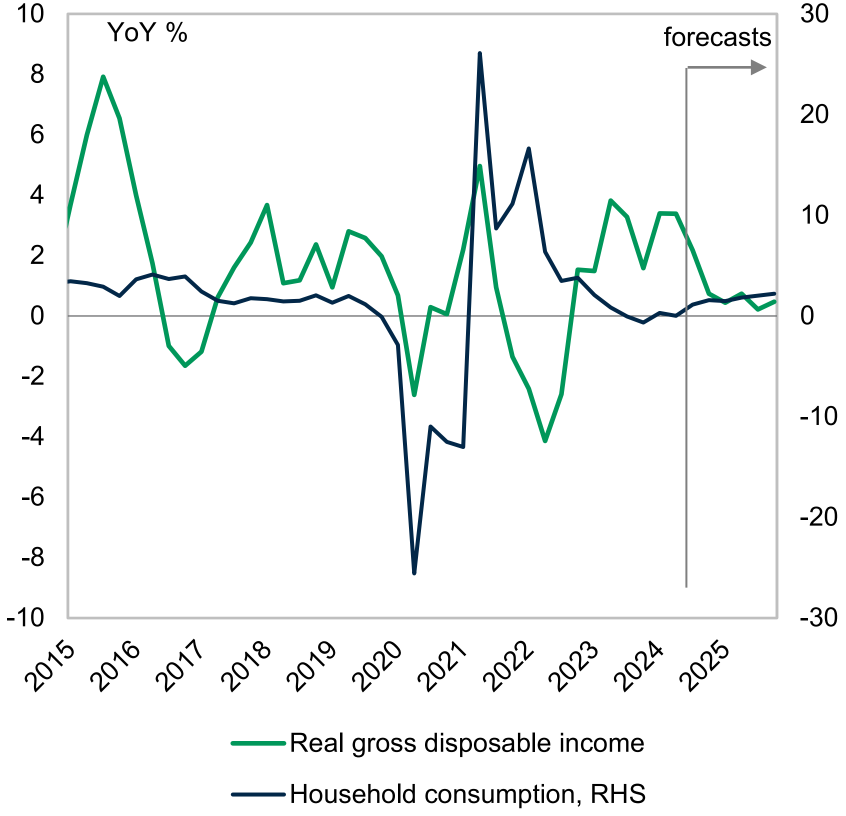
THE PURCHASING POWER CONTINUES TO GROW STRONGLY

Real incomes are growing by more 3% a year



Sources: ONS, Crédit Agricole S.A./ECO.

Household consumption is expected to grow in line with real income



Sources: ONS, Crédit Agricole S.A./ECO.

JOB MARKET

THE LABOUR MARKET CONTINUES TO EASE BUT REMAINS TIGHT

We continue to expect a deterioration in the unemployment rate but have proceed to downward revisions in our forecasts. The number of job vacancies has continued to decline. The ratio between the number of unemployed and the number of vacancies – a key indicator of the degree of easing in the labour market – has now risen to 2019 levels (1.6). The relationship between the unemployment rate and the job vacancy rate (known as the Beveridge curve) has reached a situation which suggests that any further easing of the labour market in the coming months should result in higher unemployment. However, this increase is taking its time to materialise. The unemployment rate fell unexpectedly to 4.1% in the three months to end-July, from 4.4% in the three months to end-April, which is not surprising given the stronger-than-expected expansion in activity in H1 2024. The expected moderation in GDP growth rates should lead to a decline in job creation and an increase in the unemployment rate by the end of the year. However, the actual data have prompted us to make a substantial downwards revision to our forecasts for the unemployment rate (to 4.3% in Q4 2024, vs. 4.8% previously) and we now expect relative stability on an annual average basis, at 4.2% in 2024 and 2025.

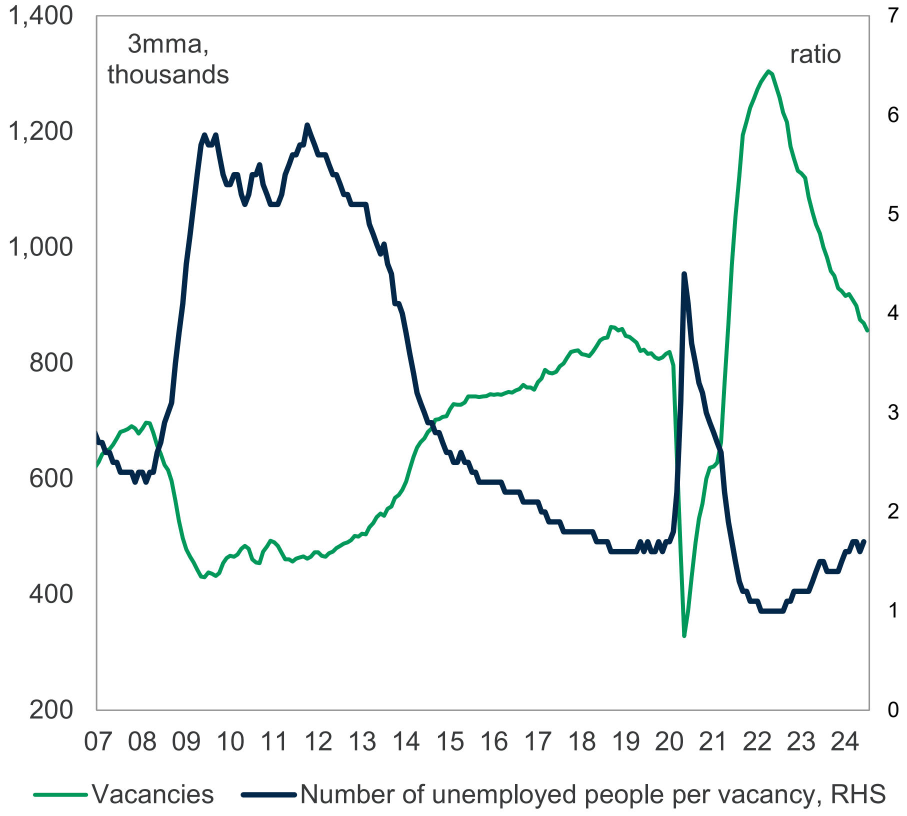
Nominal wage growth remains strong (5.1% in the three months to end-July) but continues to slow (7.8% a year earlier). Total pay (including bonuses) fell more sharply, to 4% in the three months to end-July, compared with 8.3% a year earlier. However, this results largely from the one-off payments in the NHS and public service sector made in June and July 2023, which were not renewed in 2024. The BoE's leading indicators continue to point to a slowdown in wage growth in the coming year.

The UK labour market continues to be marked by an abnormally high economic inactivity rate since the pandemic, which is due to an increase in long-term illnesses and the number of students. The increase in the economic inactivity can also be attributed to movements in the composition of the population (and the age pyramid in particular). The low labour market participation rate contributes, in turn, to explain the low levels of the unemployment rate as people leaving the labour market are obviously not counted as unemployed. *Brexit* has not helped in this respect. The split has generated a labour shortage in some activity sectors that an increase in non-EU immigration has failed to offset, thereby putting extra pressure on wages.

JOB MARKET

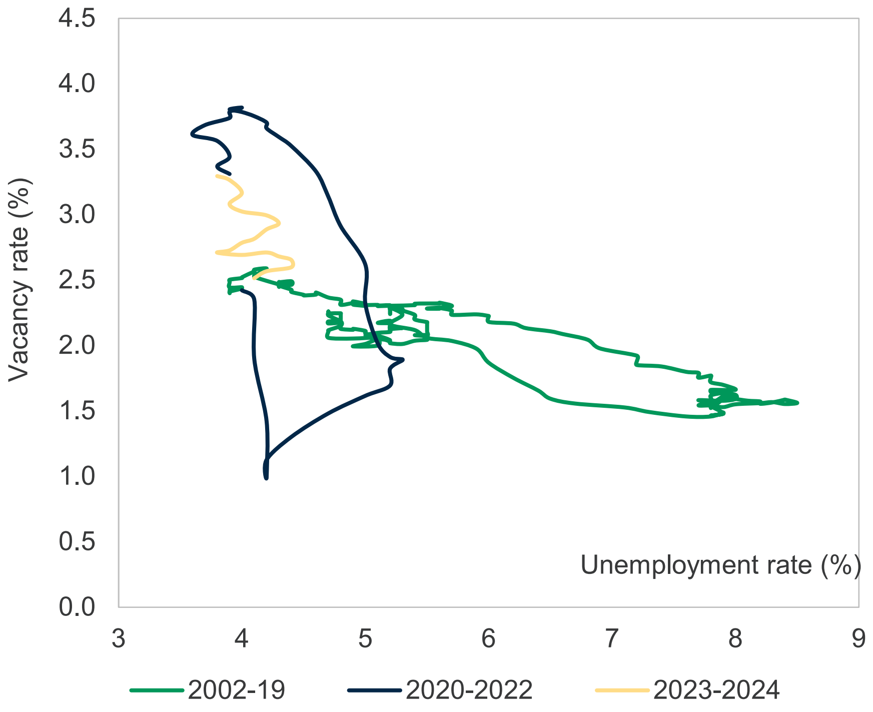
THE LABOUR MARKET CONTINUES TO EASE BUT REMAINS TIGHT

Labour demand continues to return to normal, but the ratio of the number of unemployed per vacancy remains extremely low



Sources: ONS, Crédit Agricole S.A./ECO.

Beveridge curve: the unemployment rate is expected to rise in the coming months as the ratio returns to pre-Covid levels



Note: The vacancy rate is calculated as the ratio between the number of vacancies and the sum between employment and the number of vacancies in a given period.

Sources: ONS, Crédit Agricole S.A./ECO.

PUBLIC FINANCES

THE BUDGET OF 30 OCTOBER 2024, OR HOW TO CREATE ROOM FOR MANOEUVRE TO INVEST?

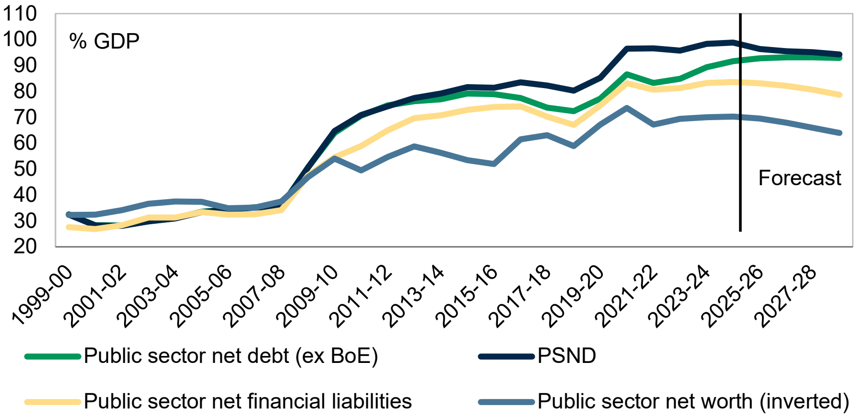
During its election campaign, Labour set itself two budget rules, which have since been confirmed by the Chancellor of the Exchequer, Rachel Reeves:

- Debt rule: reduce the debt-to-GDP ratio over the next five years;
- Public deficit rule: achieve a current budget balance (i.e. excluding public investment). This represents a major shift from the previous government's rule, which targeted the total budget deficit (3% in the fifth and final year of the forecast horizon).

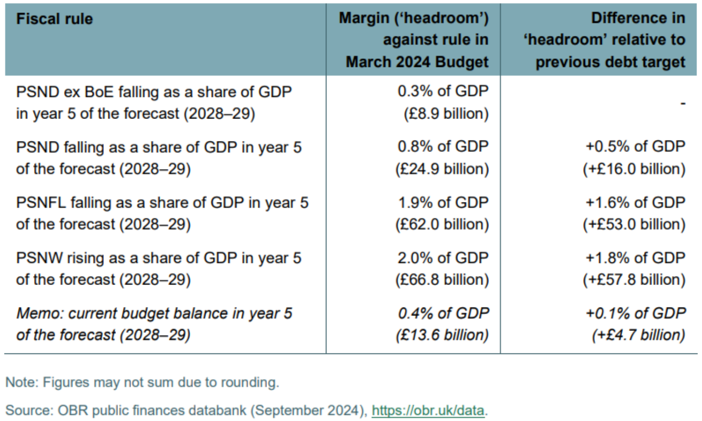
As the government's objective is to increase investment, particularly in the green transition, it reserves the right to borrow solely to invest. According to the latest OBR forecasts of March 2024, the public sector net debt ratio (PSND ex BoE, which excludes items of the BoE's balance sheet, including loans made by the BoE to companies under its *Term Funding Scheme*) will decline only in the last forecast year, to 92.9% of GDP, after reaching 93.2% in 2026-2027 and 2027-2028, for a decrease of £8.9bn (0.3% of GDP).

To give itself more room for manoeuvre in terms of investment, the government is reviewing several options for the accounting definition of public debt. It could exclude other debt measurement items used in the budgetary rule (e.g. any debt incurred by public banks, such as the new National Wealth Fund, or losses associated with the BoE's asset purchase facility). Other possibilities would be to use a broader definition of public debt, such as *public sector net financial liabilities* (PSNFL), *public sector net worth* (PSNW) or *public sector net debt* (PSND, which excludes the value of liquid financial assets). Depending on the definition, the government could increase its room for manoeuvre to more than £50bn, based on the OBR's forecasts (as shown in the table below).

Public debt measures



Sources: OBR databank September 2024, Crédit Agricole S.A./ECO.



Fiscal rule	Margin ('headroom') against rule in March 2024 Budget	Difference in 'headroom' relative to previous debt target
PSND ex BoE falling as a share of GDP in year 5 of the forecast (2028–29)	0.3% of GDP (£8.9 billion)	-
PSND falling as a share of GDP in year 5 of the forecast (2028–29)	0.8% of GDP (£24.9 billion)	+0.5% of GDP (+£16.0 billion)
PSNFL falling as a share of GDP in year 5 of the forecast (2028–29)	1.9% of GDP (£62.0 billion)	+1.6% of GDP (+£53.0 billion)
PSNW rising as a share of GDP in year 5 of the forecast (2028–29)	2.0% of GDP (£66.8 billion)	+1.8% of GDP (+£57.8 billion)
Memo: current budget balance in year 5 of the forecast (2028–29)	*0.4% of GDP (£13.6 billion)*	*+0.1% of GDP (+£4.7 billion)*

Note: Figures may not sum due to rounding.

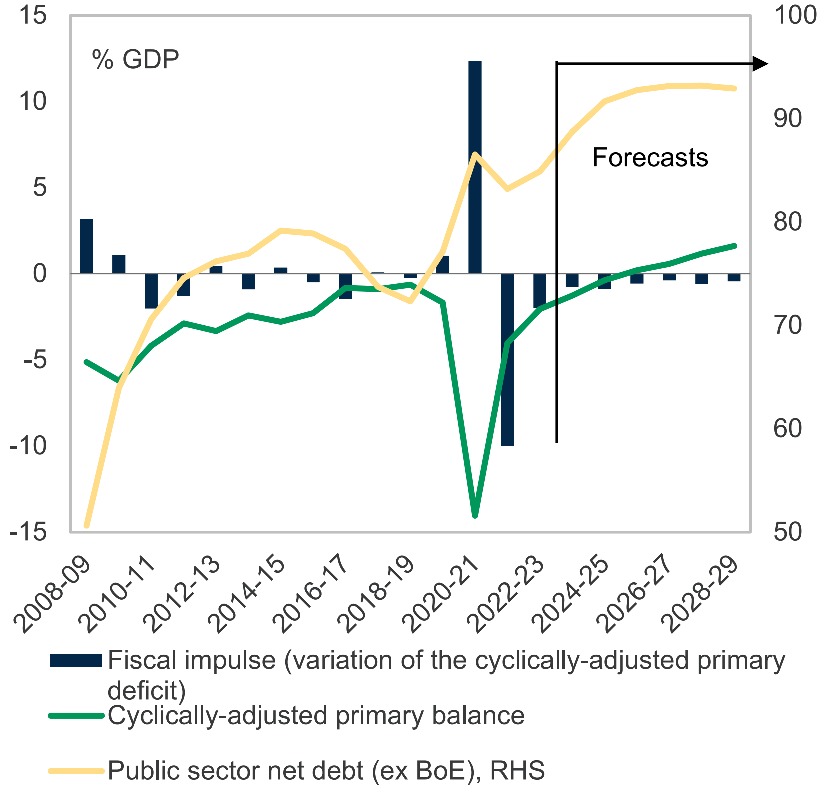
Source: OBR public finances databank (September 2024), https://obr.uk/data.

Source of the table: IFS, The-outlook-for-the-public-finances-in-the-new-parliament-IFS-report339.pdf

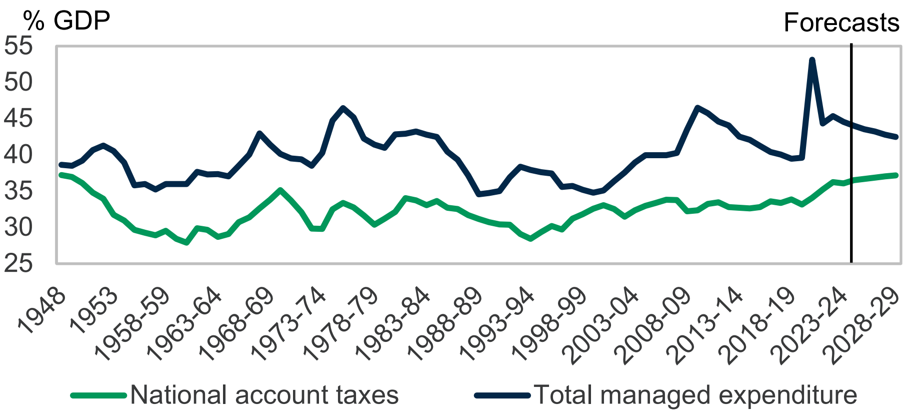
PUBLIC FINANCES

AN UNENVIABLE FISCAL SITUATION

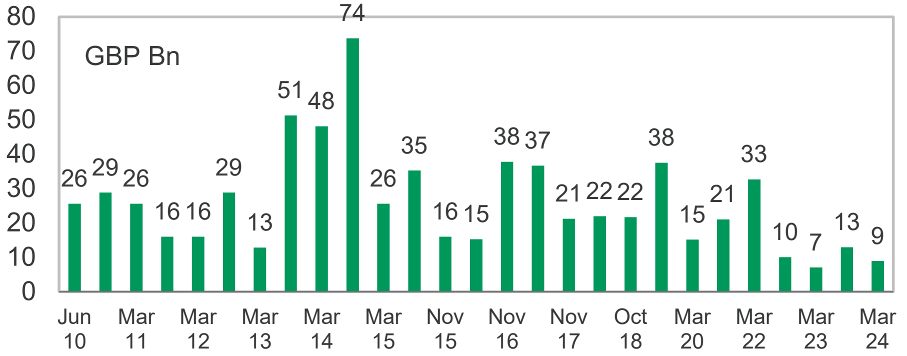
Fiscal stimulus needs to be negative to stabilise the debt-to-GDP ratio



Record taxation, public services under pressure



Narrow room for manoeuvre regarding the budgetary rule



Sources: OBR EFO March 2024, Crédit Agricole S.A./ECO.

MONETARY POLICY

WE NOW EXPECT FURTHER RATE CUTS IN 2025

Stubborn inflation requires a gradual approach to monetary easing

After starting to ease its monetary policy in August with an initial 25bp rate cut, the BoE left its key rate unchanged at 5.00% in September as expected. Only one member of the Monetary Policy Committee (MPC) voted for a rate cut of a further 25bp, suggesting a near-unanimous stance in favour of a gradual approach to monetary easing. Although inflation reached the 2% target in May and has surprised to the downside since, the BoE remains worried about the possibility of an unsustainable return to the target. The BoE has set out three possible scenarios in this respect: first, disinflation continues on its own as global shocks dissipate, even with a less restrictive monetary policy; second, the normalisation of prices and wages requires a negative output gap with labour market slack for a certain time; and third, structural changes in price and wage trends might have taken place, meaning that monetary policy is not restrictive enough and the BoE would need to keep rates higher for longer than in the previous scenario. Opinions differ among MPC members regarding the likelihood of these scenarios, but “for most members, in the absence of material developments, a gradual approach to removing policy restraint would be warranted”. Meanwhile, the Bank’s forward guidance continues to state that “monetary policy will need to continue to remain restrictive for sufficiently long enough until the risks to inflation returning sustainably to the 2% target in the medium term have dissipated further” and that “the committee continues to monitor closely the risks of inflation persistence and will decide the appropriate degree of monetary policy restrictiveness at each meeting”.

Disinflation is expected to pick up in 2025, increasing the chances of more rate cuts

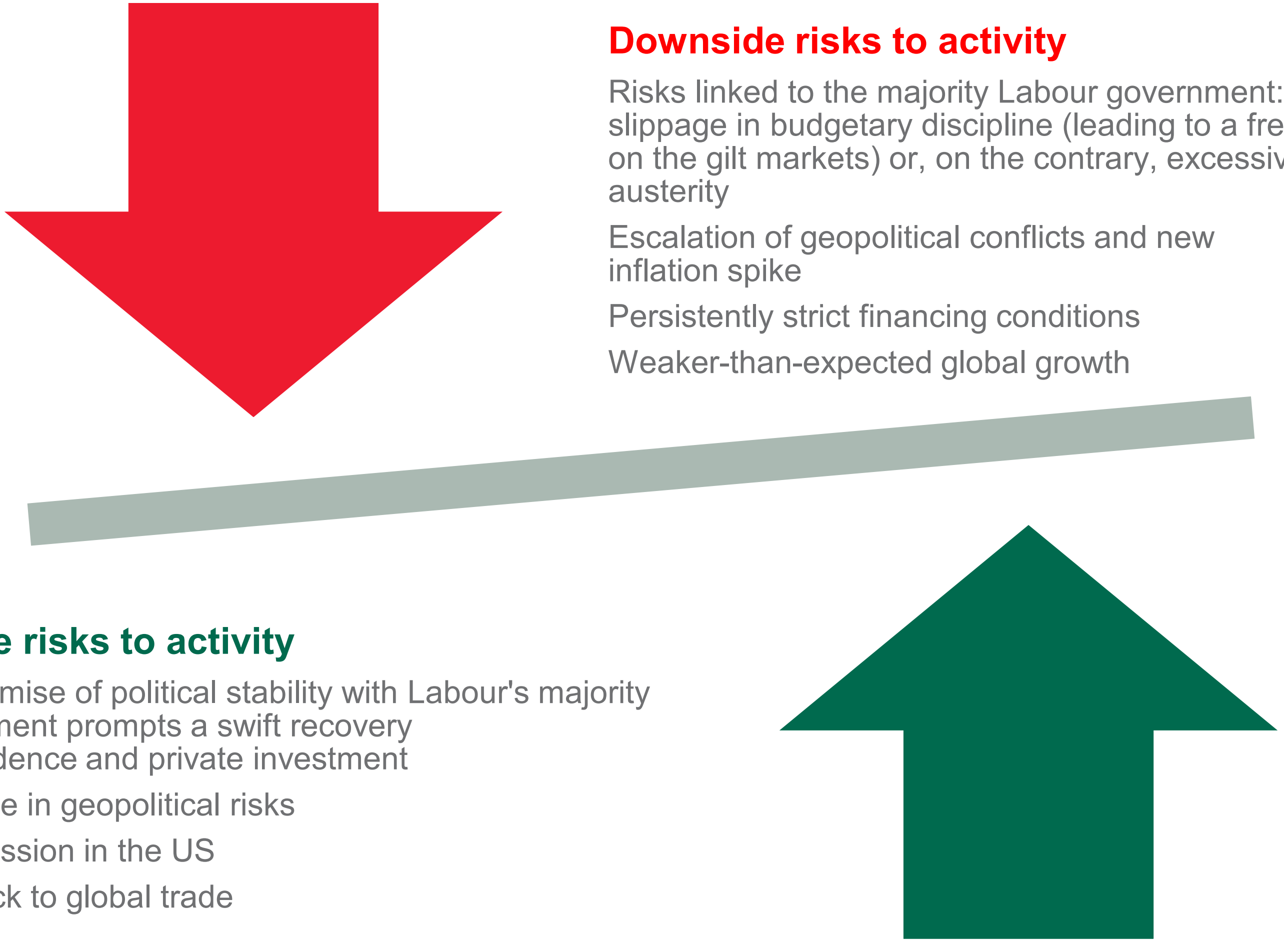
Our scenario assumes an additional 25bp rate cut in November 2024, when the BoE will also update its inflation forecasts. Inflation is expected to be volatile in the last few months of 2024. It is expected to dip to 1.9% in September against a backdrop of lower oil prices and then increase to an average of 2.6% in Q4, peaking at 2.7% in November. The main reason for this acceleration is the 10% increase in administered gas and electricity prices in October, accompanied by less favourable base effects on energy prices.

In 2025, we expect inflation to fall sharply in the first half of the year, returning to the target by mid-year and falling to 1.8% in Q4 2025. We are forecasting a substantial drop in service inflation in early 2025, bringing the core inflation rate down to 1.8% by next July.

With the acceleration of the disinflation process in 2025, and in the absence of any further shocks, the BoE may accelerate its monetary easing; we are adding two additional rate cuts for H2 2025, bringing to 150 bps the monetary easing in 2025 (or six rate cuts of 25 bps each) after 50 bps in 2024. The key rate is thus expected to reach 3.25% in December 2025.

RISKS

CENTRAL SCENARIO: START OF A SLUGGISH GROWTH CYCLE



Downside risks to activity

Risks linked to the majority Labour government: slippage in budgetary discipline (leading to a fresh crisis on the gilt markets) or, on the contrary, excessive austerity

Escalation of geopolitical conflicts and new inflation spike

Persistently strict financing conditions

Weaker-than-expected global growth

Upside risks to activity

The promise of political stability with Labour's majority government prompts a swift recovery in confidence and private investment

A decline in geopolitical risks

No recession in the US

No shock to global trade

THE SCENARIO IN FIGURES

FORECASTS

annual average, % — quarterly variation, %

United Kingdom	2023	2024	2025	2023				2024				2025			
				Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
GDP (%)	0.3	1.0	1.5	0.1	0.0	-0.1	-0.3	0.7	0.5	0.3	0.3	0.3	0.5	0.4	0.4
household consumption	0.5	0.8	1.9	-0.4	0.5	-0.7	0.0	0.6	0.2	0.4	0.4	0.5	0.5	0.6	0.6
public consumption	0.6	1.9	1.6	-0.7	1.7	0.9	-0.2	0.3	1.1	0.0	0.4	0.4	0.4	0.4	0.4
investment	-0.1	1.3	3.1	2.7	-1.6	-1.7	0.7	1.2	0.6	0.4	0.8	0.8	0.8	1.0	1.0
change in inventories*	-0.9	0.1	0.4	0.3	-0.3	-0.4	0.3	-0.4	0.7	0.0	0.0	0.0	0.2	0.1	0.1
net exports*	0.5	-3.0	-2.6	-1.9	-0.5	0.3	-0.2	0.1	-2.2	-2.5	-0.1	-0.3	-0.2	-0.3	-0.3
Unemployment rate (ILO)	4.1	4.2	4.2	3.9	4.3	4.0	4.0	4.4	4.1	4.1	4.3	4.3	4.2	4.1	4.2
Inflation (CPI, YoY%)	7.3	2.6	2.1	10.2	8.4	6.7	4.2	3.5	2.1	2.1	2.6	2.4	2.1	2.1	1.8
Core CPI (YoY%)	6.2	3.8	2.3	6.1	6.9	6.4	5.3	4.6	3.6	3.4	3.5	3.4	2.4	1.9	1.8
Current account (% GDP)	-2.0	-3.0	-6.5	-2.0	-3.0	-1.1	-1.6	-2.0	-4.0	-	-	-	-	-	-
General gov. balance, % GDP	-5.9	-3.7	-2.7	-	-	-	-	-	-	-	-	-	-	-	-
Public debt % GDP	101.3	103.3	105.2	-	-	-	-	-	-	-	-	-	-	-	-
Bank rate**	5.25	4.75	3.25	4.25	5.00	5.25	5.25	5.25	5.25	5.00	4.75	4.50	4.25	3.75	3.25

** Contributions to GDP growth*

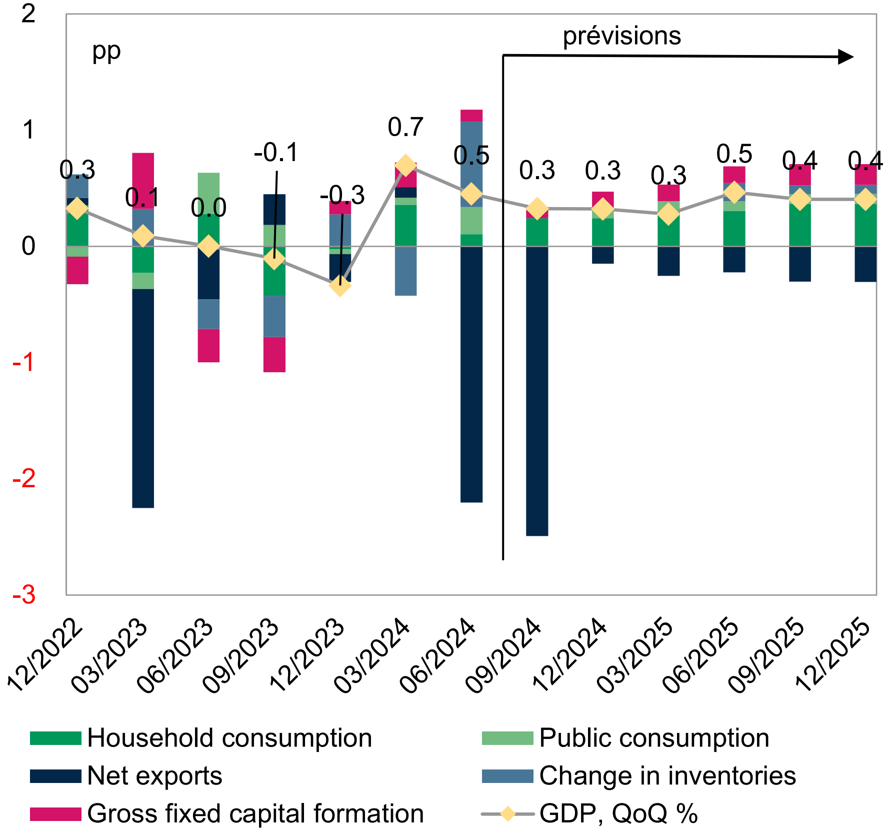
*** End of period*

Sources: ONS, BoE, Crédit Agricole S.A./ECO.

THE SCENARIO IN PICTURES

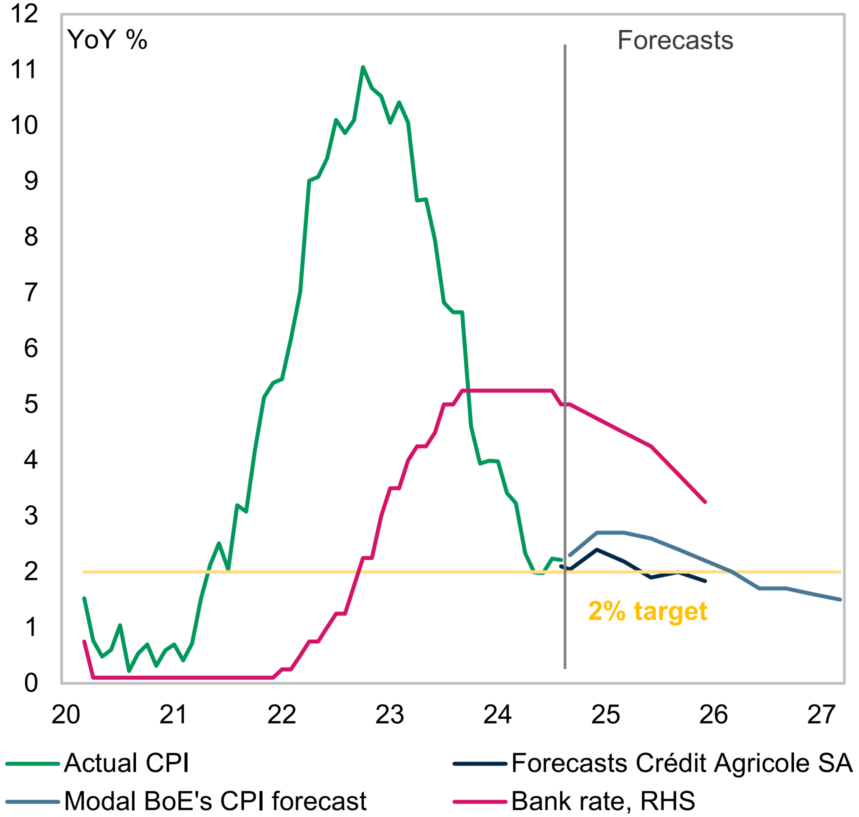
SLOWDOWN IN THE SHORT TERM AFTER A STRONG START TO THE YEAR

Growth to be driven by households and private investment…



Sources: ONS, Crédit Agricole S.A./ECO forecasts.

… thanks to the fall in inflation and monetary easing

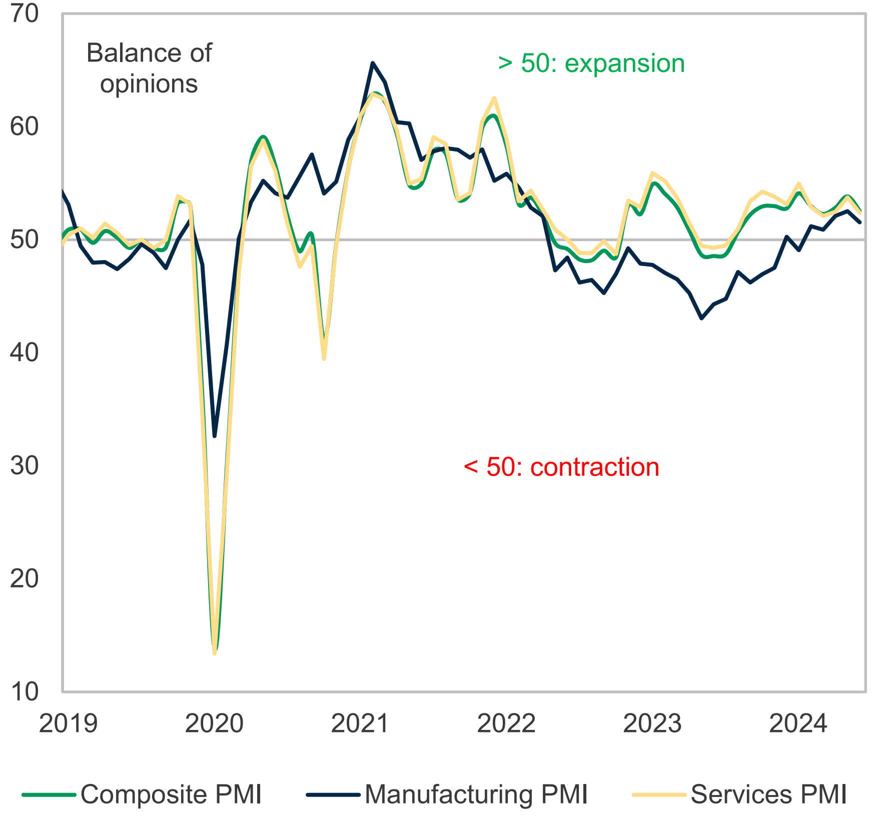


Sources: ONS, BoE Monetary Policy Report of August 2024, Crédit Agricole S.A./ECO (forecasts for end-2025).

THE SCENARIO IN PICTURES

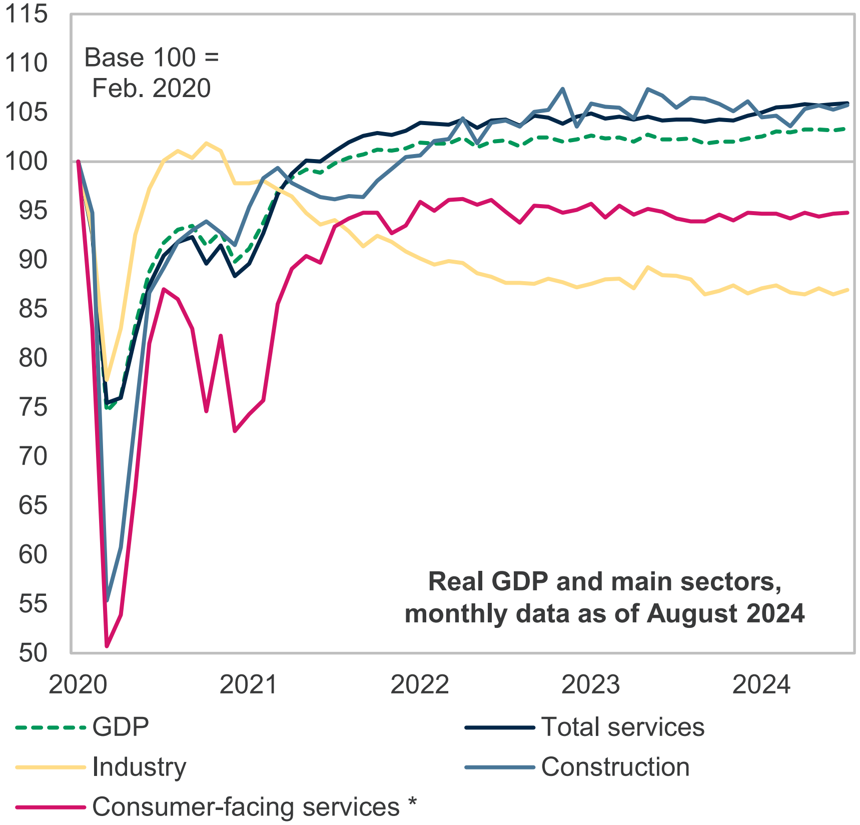
MODEST GROWTH RATES

Business confidence surveys remain in expansion territory



Sources: S&P Global, Crédit Agricole S.A./ECO.

Growth remains driven by services

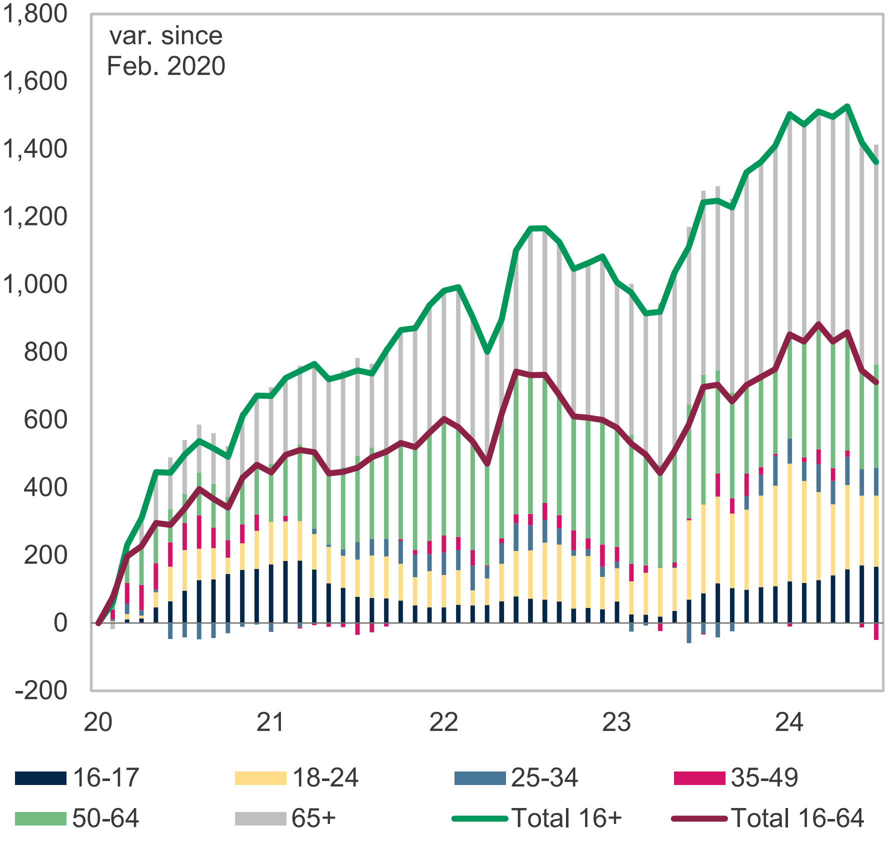


** Retail, catering, transport and travel, leisure and entertainment.*
Sources: ONS, Crédit Agricole S.A./ECO.

THE SCENARIO IN PICTURES

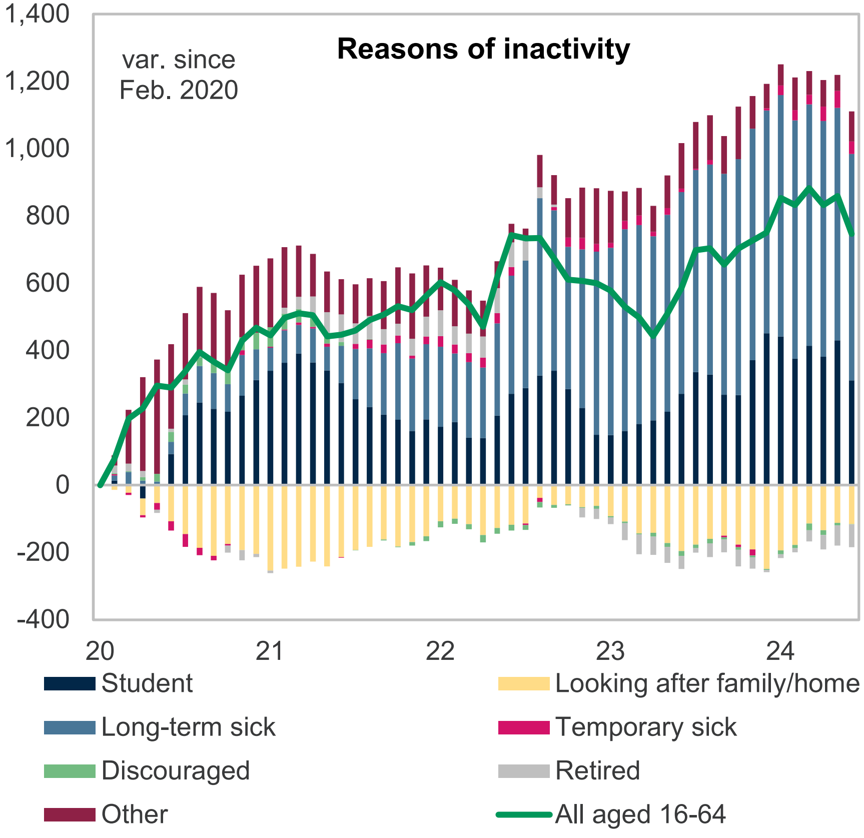
LABOUR MARKET STILL TIGHT DESPITE SOME EASING: THE RESULT OF A HIGH ECONOMIC INACTIVITY RATE

Economically inactive population by age group since Covid



Sources: ONS, Crédit Agricole S.A./ECO.

Economically inactive population by type of reason since Covid

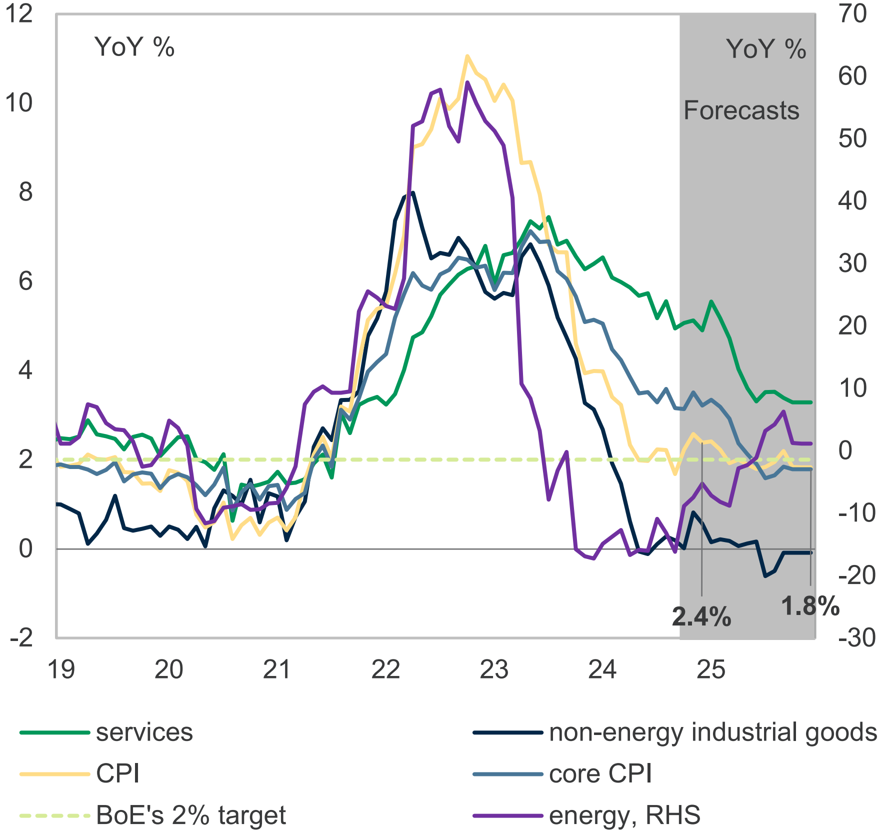


Sources: ONS, Crédit Agricole S.A./ECO.

THE SCENARIO IN PICTURES

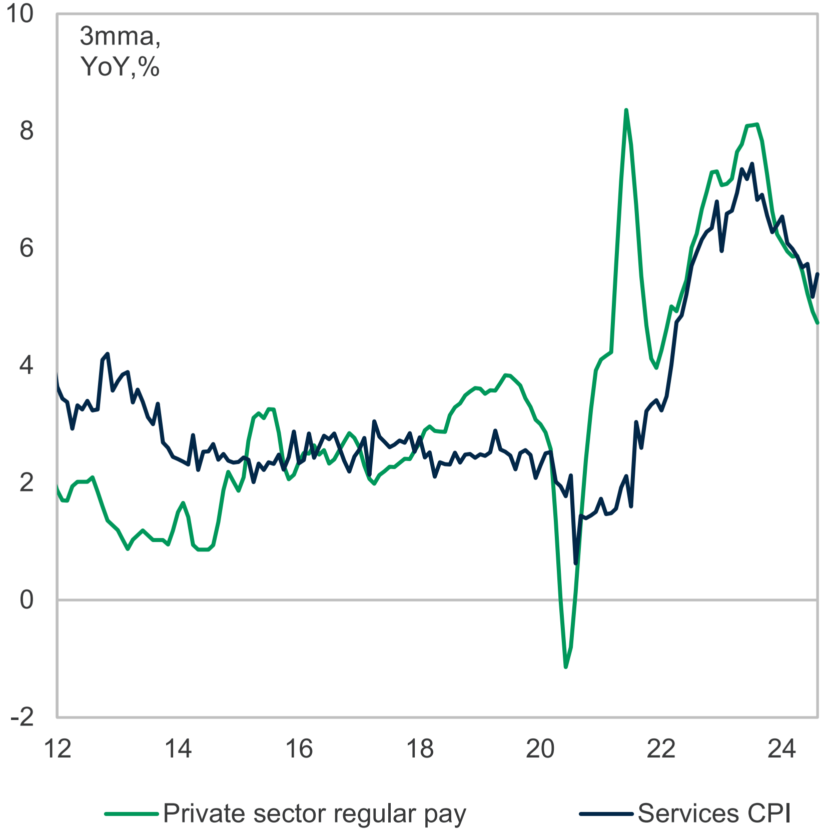
INFLATION: VOLATILE IN THE SHORT TERM BUT NOT MOVING FAR ENOUGH FROM THE TARGET TO CALL MONETARY EASING INTO QUESTION

Inflation to pick up slightly in the short term due to energy prices



Sources: ONS, Crédit Agricole S.A./ECO.

Wage growth and service inflation: continued moderation



Sources: ONS, Crédit Agricole S.A./ECO.

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