Market Overview

UK Economy & October Budget

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26th September 2024

YORKSHIRE BUILDING SOCIETY

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Overview

<u>Pt1 – State of UK Economy</u>

- Labour market
- Inflation
- Housing market
- Interest rates

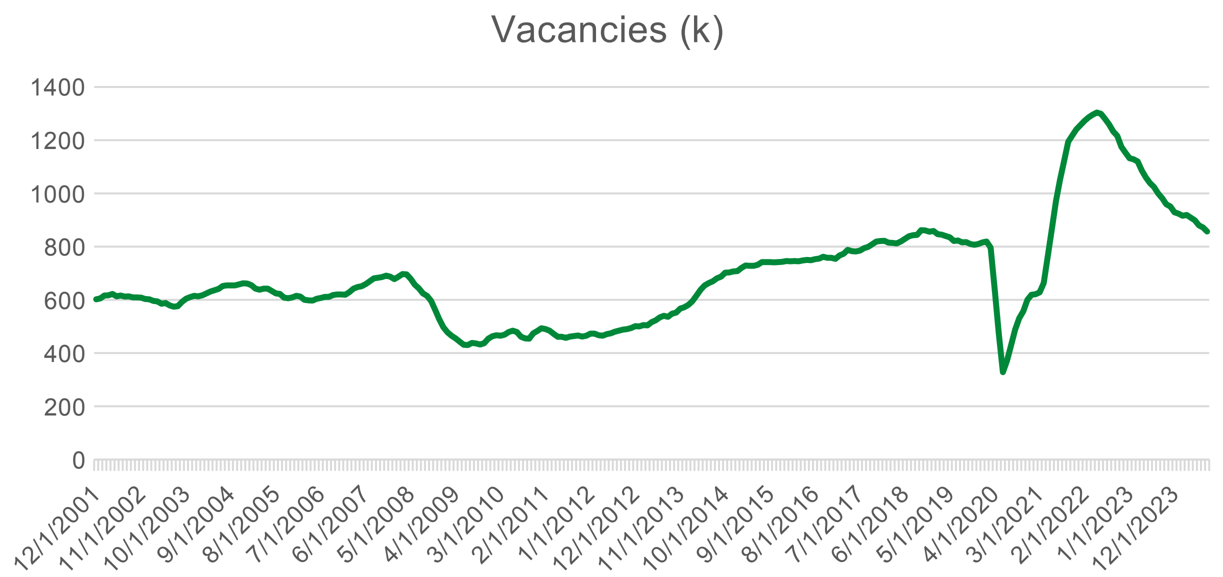
<u>Pt2 - Fiscal Picture – What can Labour do?</u>

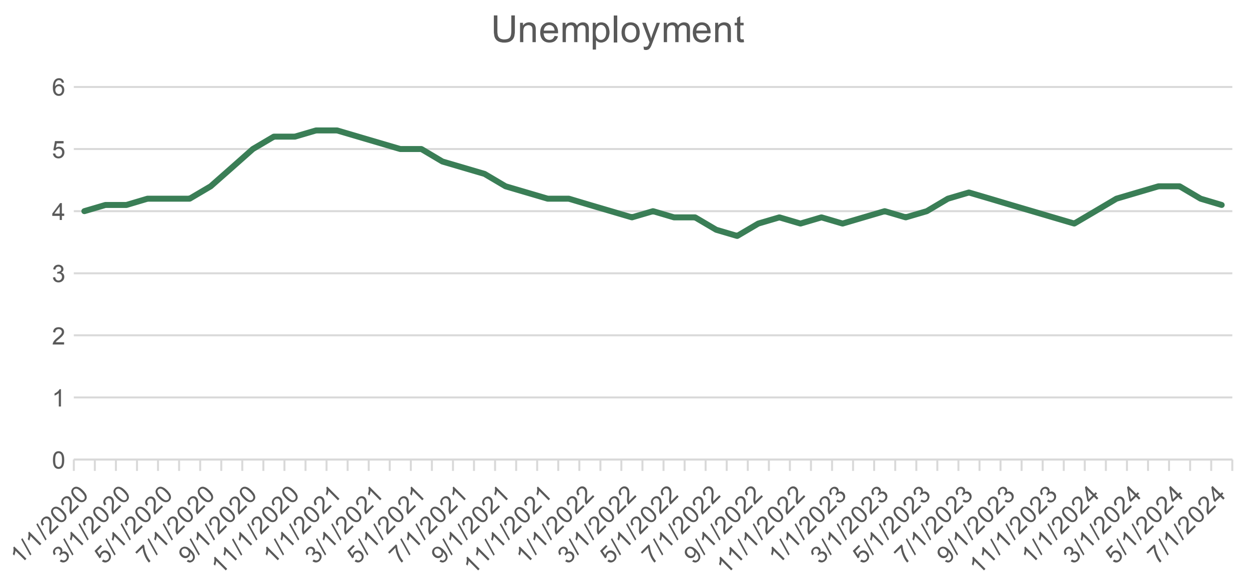
- Growth problem
- Fiscal situation
- What might they do in the budget?

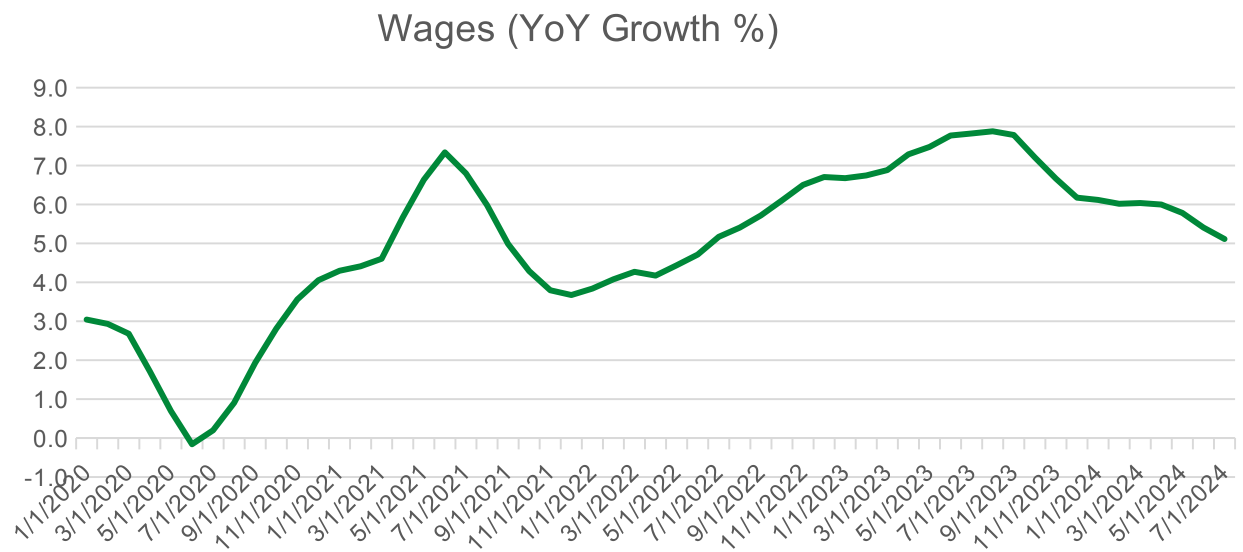
UK Economy

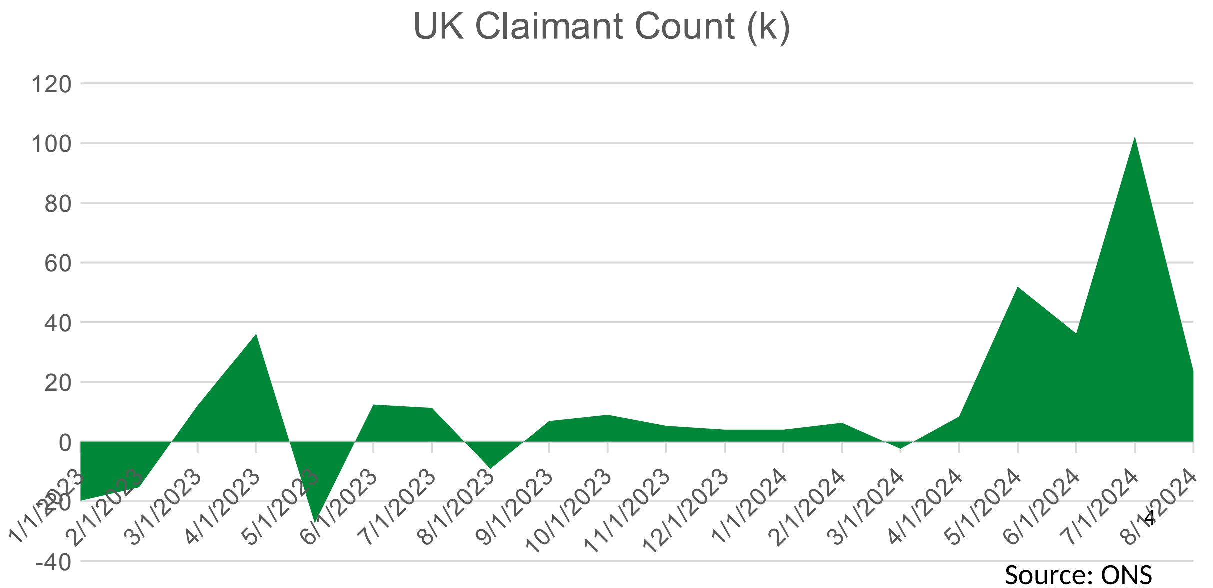
2024 so far

Is the Labour market Deteriorating?







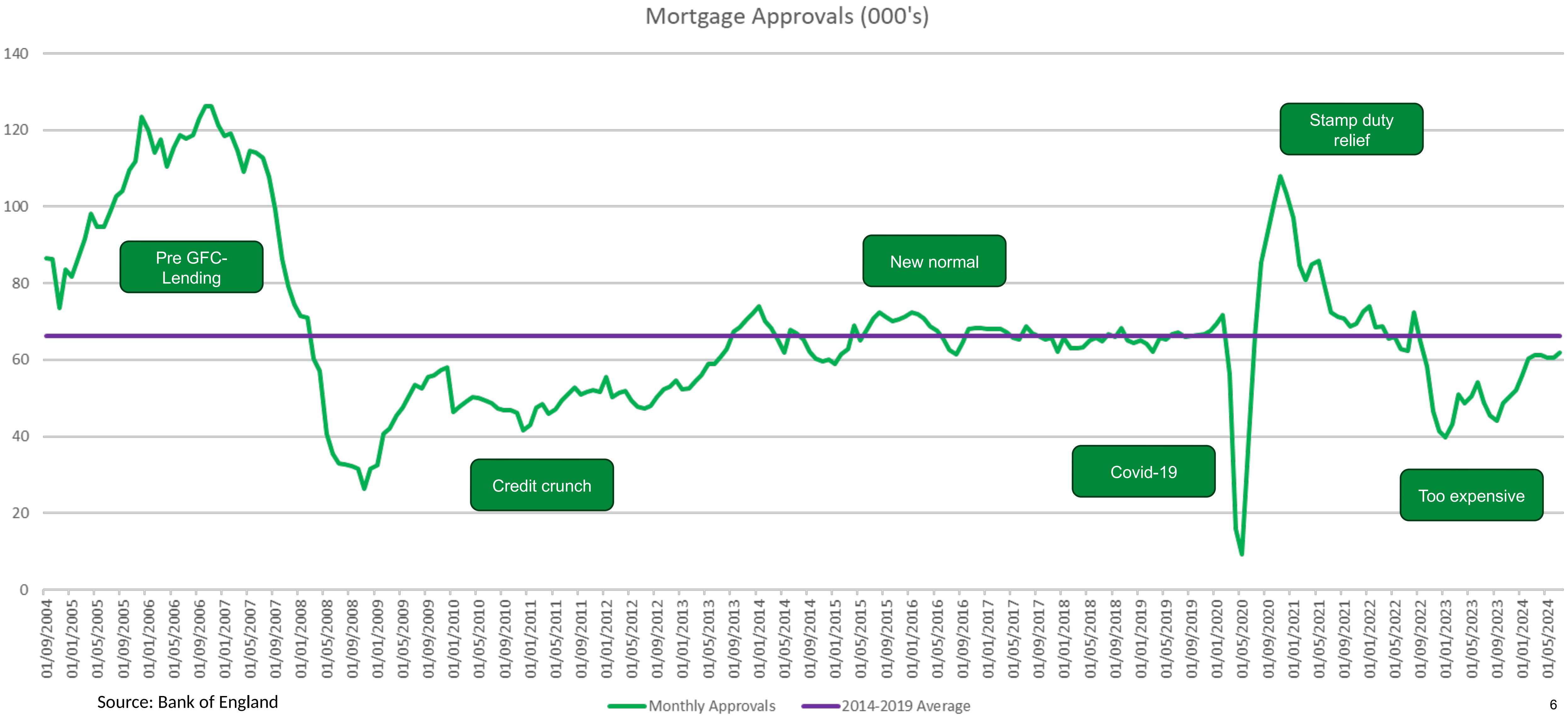


Source: ONS

Inflation - still a concern for the BoE?

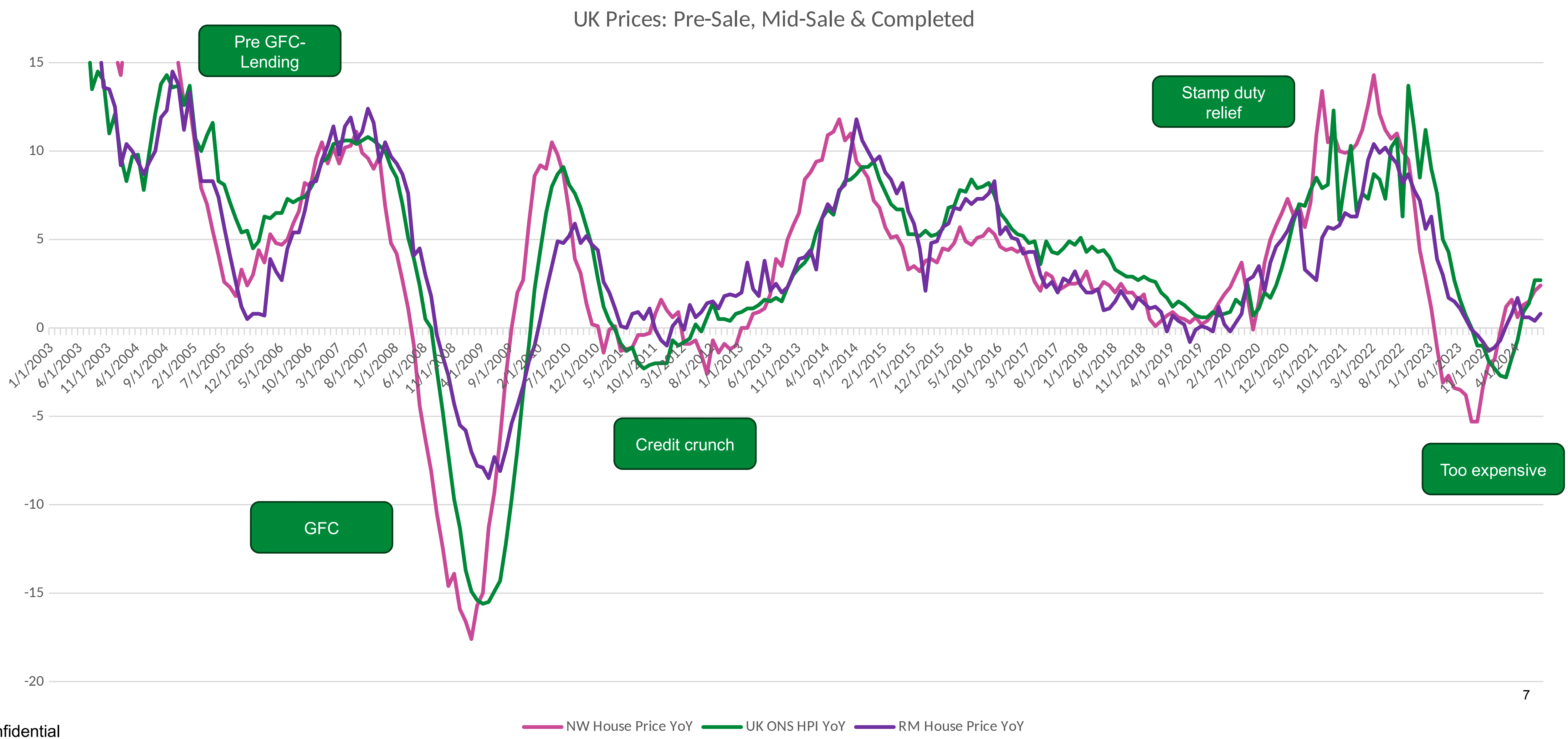
Source: ONS

Housing Market



Source: Bank of England

Housing Market



Interest Rate Environment

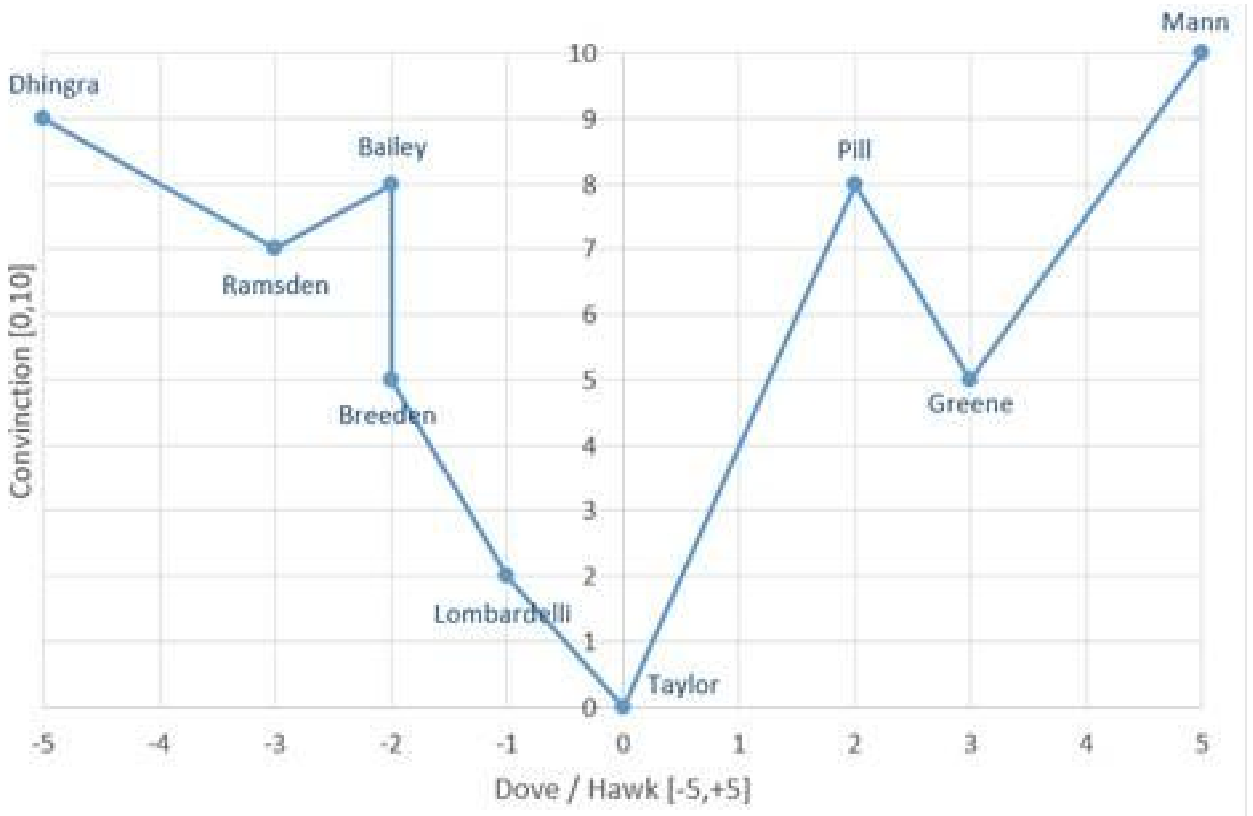
Confidential Source: Bloomberg

Interest Rates – Where next?

In the absence of material developments, a gradual approach to removing policy restraint remains appropriate.
September MPC Minutes

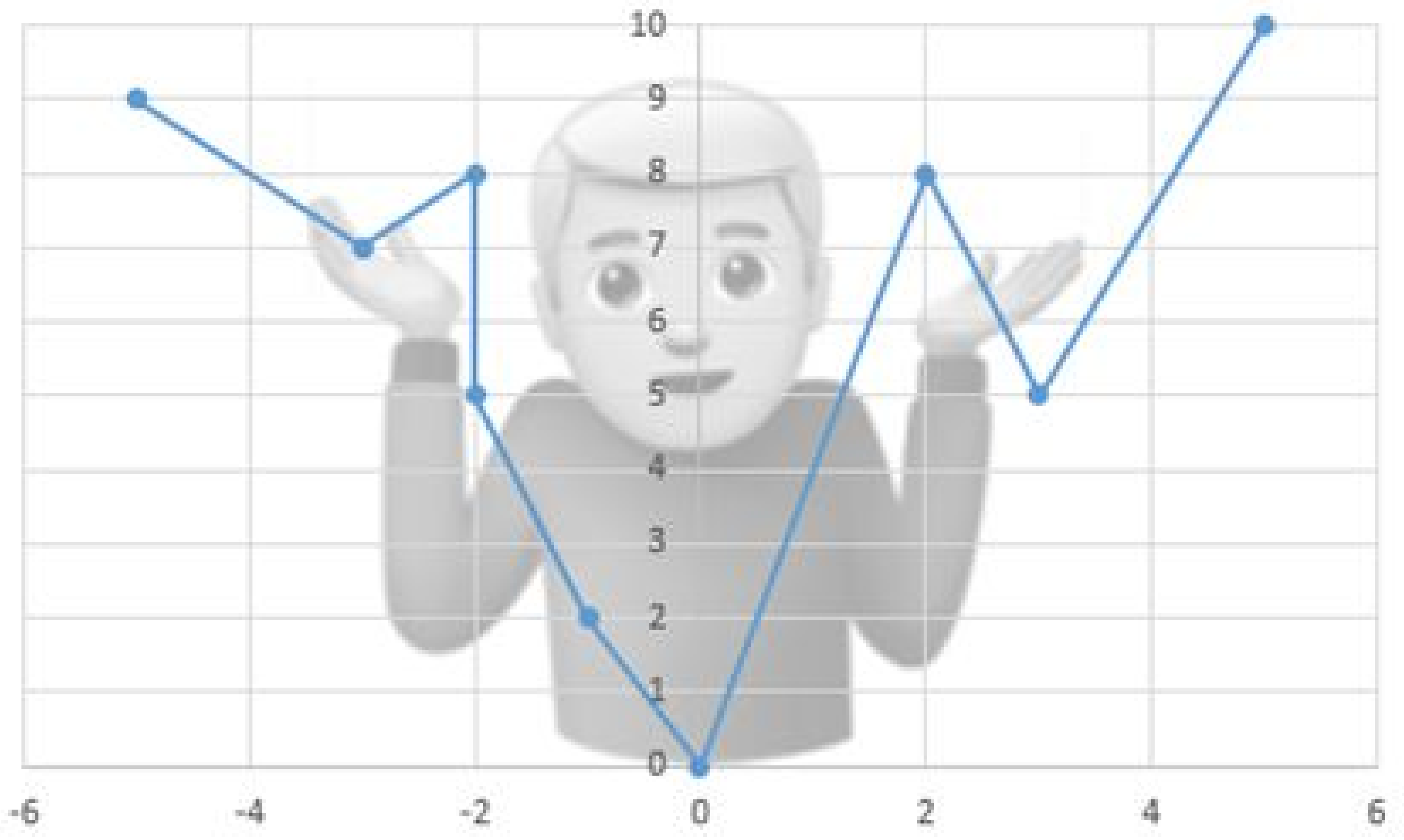
- Views of MPC members still mixed.
- Quarterly cuts seem appropriate, risk of global rate environment speeding BoE up.
- Market expects rates to fall to 3.5% over next 12 months.

	Dove / Hawk	Conviction	Comments	Votes
Bailey	-2	8	5	3
Breeden	-2	5	2	3
Dhingra	-5	9	4	5
Greene	3	5	2	3
Mann	5	10	5	5
Lombardelli	-1	2	0	2
Pill	2	8	5	3
Ramsden	-3	7	3	4
Taylor	0	0	0	0



Source: Andy Chaytor, Nomura Bank

Interest Rates – Where next?



Change in Government

What will Labour do?

The growth problem

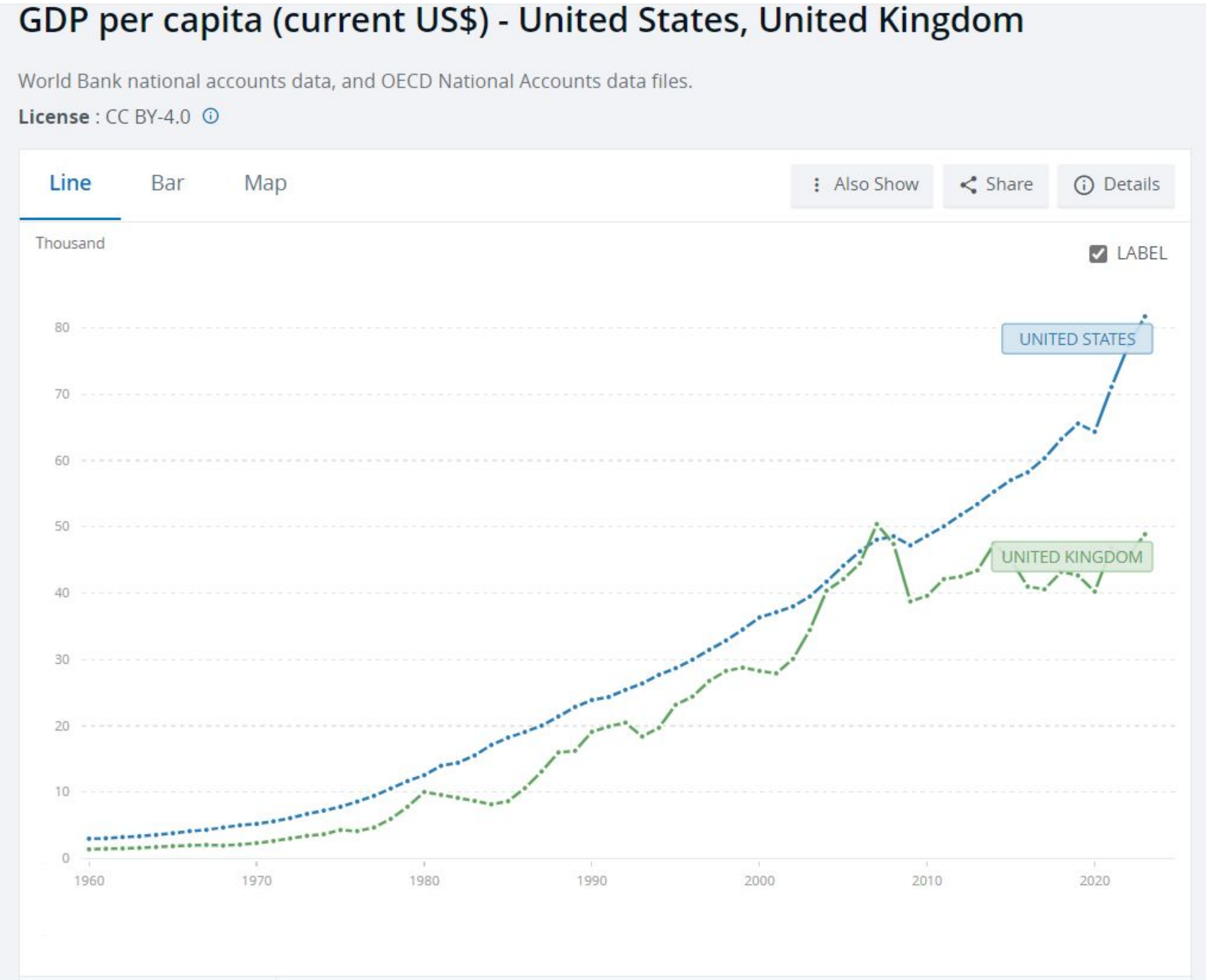
1) Kickstart economic growth

to secure the highest sustained growth in the G7 – with good jobs and productivity growth in every part of the country making everyone, not just a few, better off.

- We have recovered from the technical recession in H2 2023 and returned to slow growth.

- Real GDP grew by an average of 1.5% per year between 2010 and 2023, putting us third in the G7, behind the US and Canada but ahead of France, Germany, Italy and Japan.

- But our growing population flatters the UK's performance. The population grew by 0.7% per year between 2010 and 2023, equivalent to 6 million more people. This was the fastest rate of population growth for a century.



Productivity lagging behind

Figure 1 Output per hour in the UK and other advanced economies ($US 2010 ppp per hours), 1890 - 2019

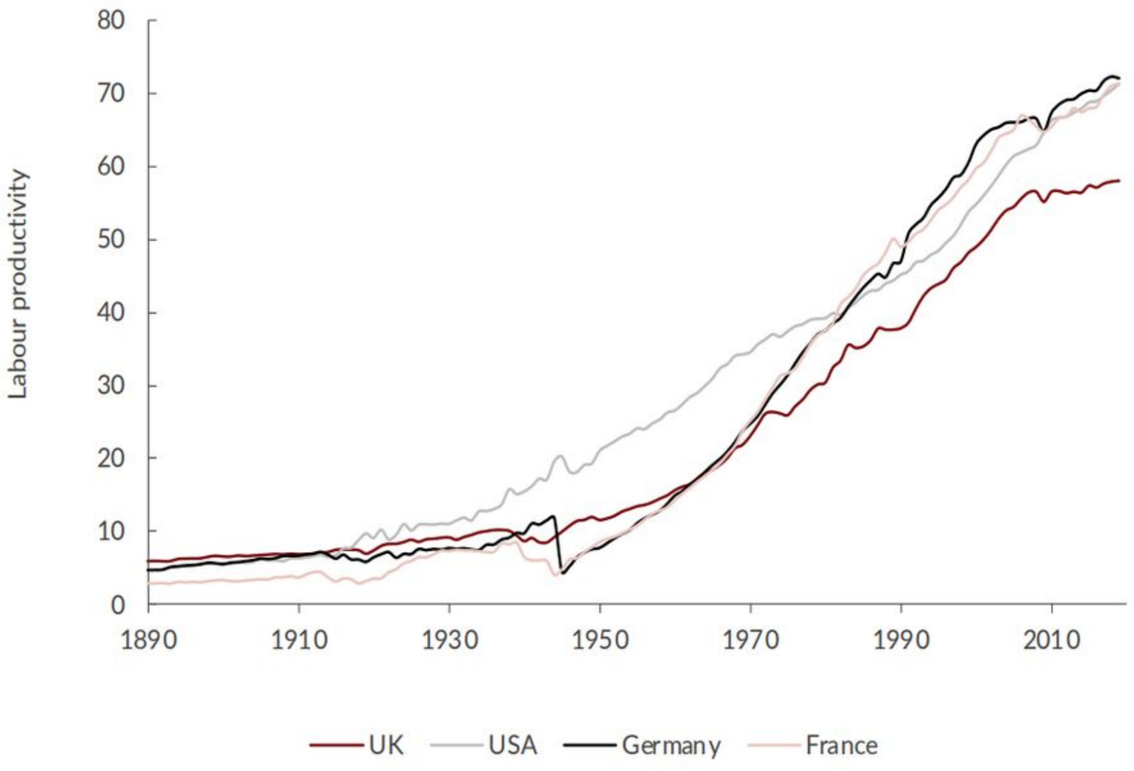
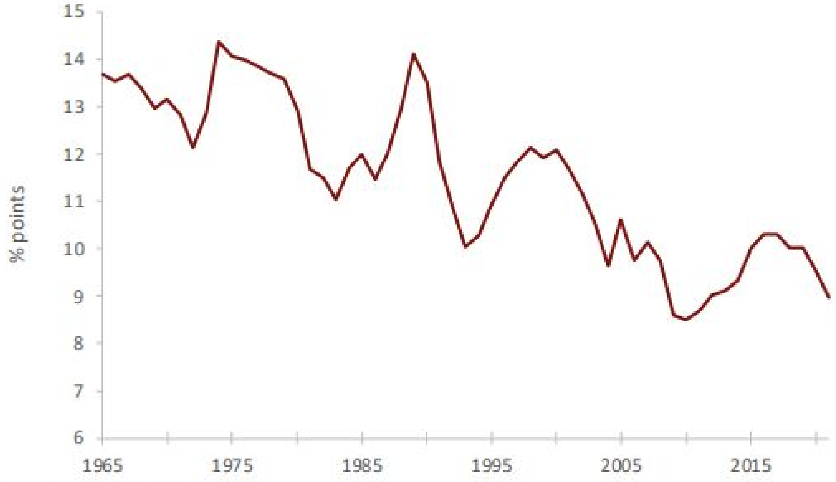


Table 1 Growth rates of the standard of living and of productivity, 1977-2019 (% p.a.)

	1977-1990	1990-2007	2007-2019
Standard of living	3.07	1.96	0.47
Productivity	2.35	2.34	0.21

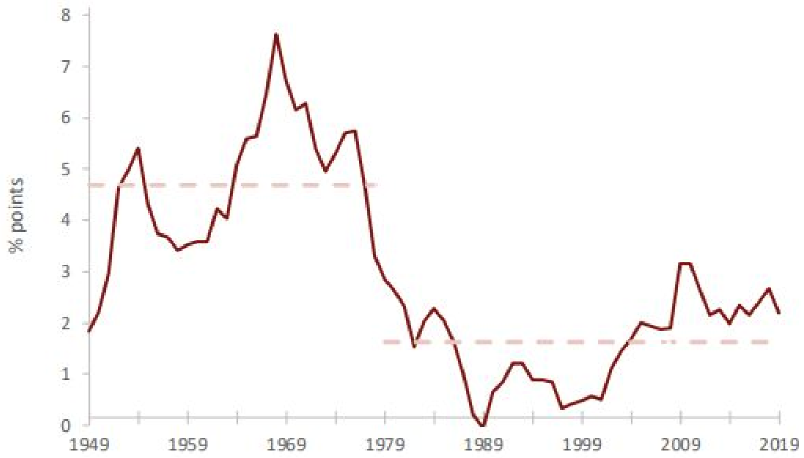
Source: Nicholas Oulton submission

Figure 1 Business investment to GDP ratio. Both GDP and business investments are in current prices.



Source: ONS and NIESR calculations

Figure 2 Public sector net investment as a percentage of GDP with the 1949-1979 and 1980 - 2021 averages.



Source: OBR, ONS and authors' calculations

Why does Growth matter for the Government?

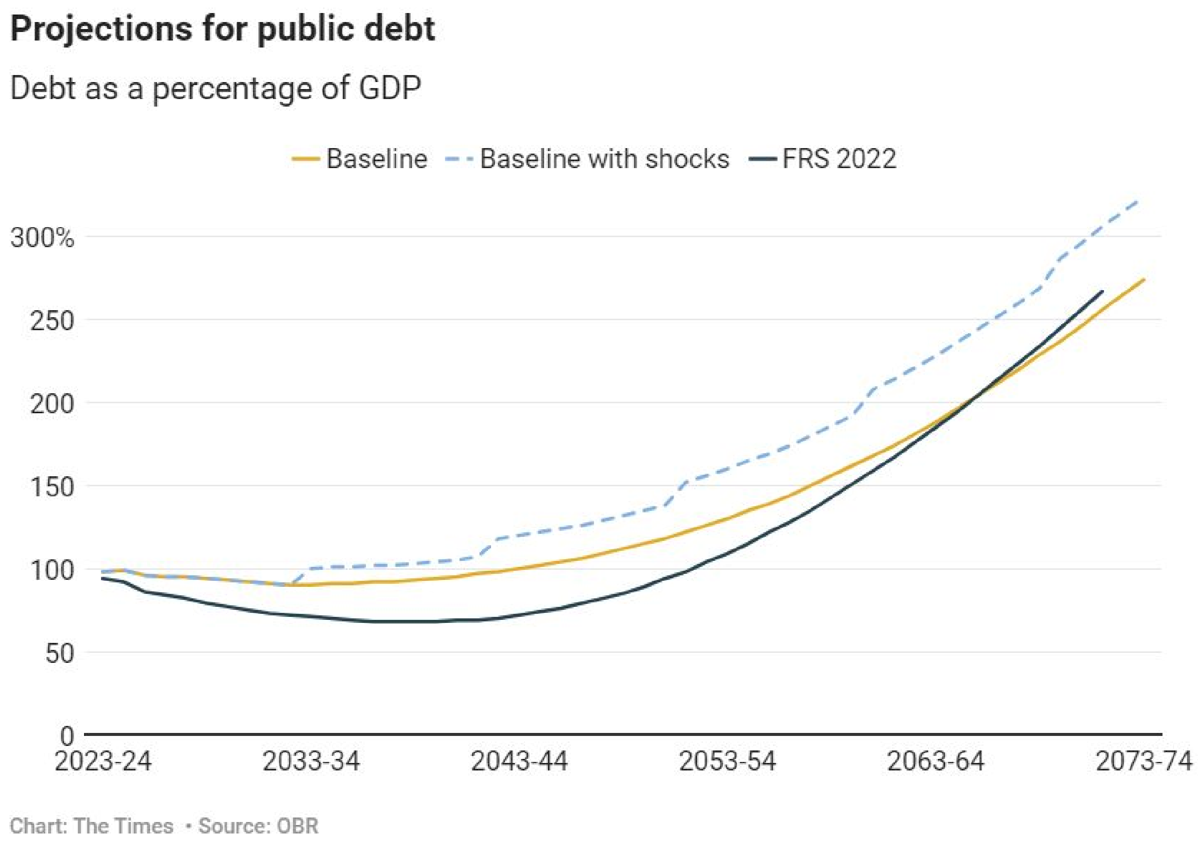
- Increases the standard of living across the UK
- Increases tax revenue
- Allows for greater spending on public services
- Slows down / reverses the rise in debt to GDP ratio

<u>Fiscal Rules</u>

- Debt should be on course to fall as a share of GDP in five years' time.
- Public sector borrowing should not exceed 3% of GDP in five years' time.

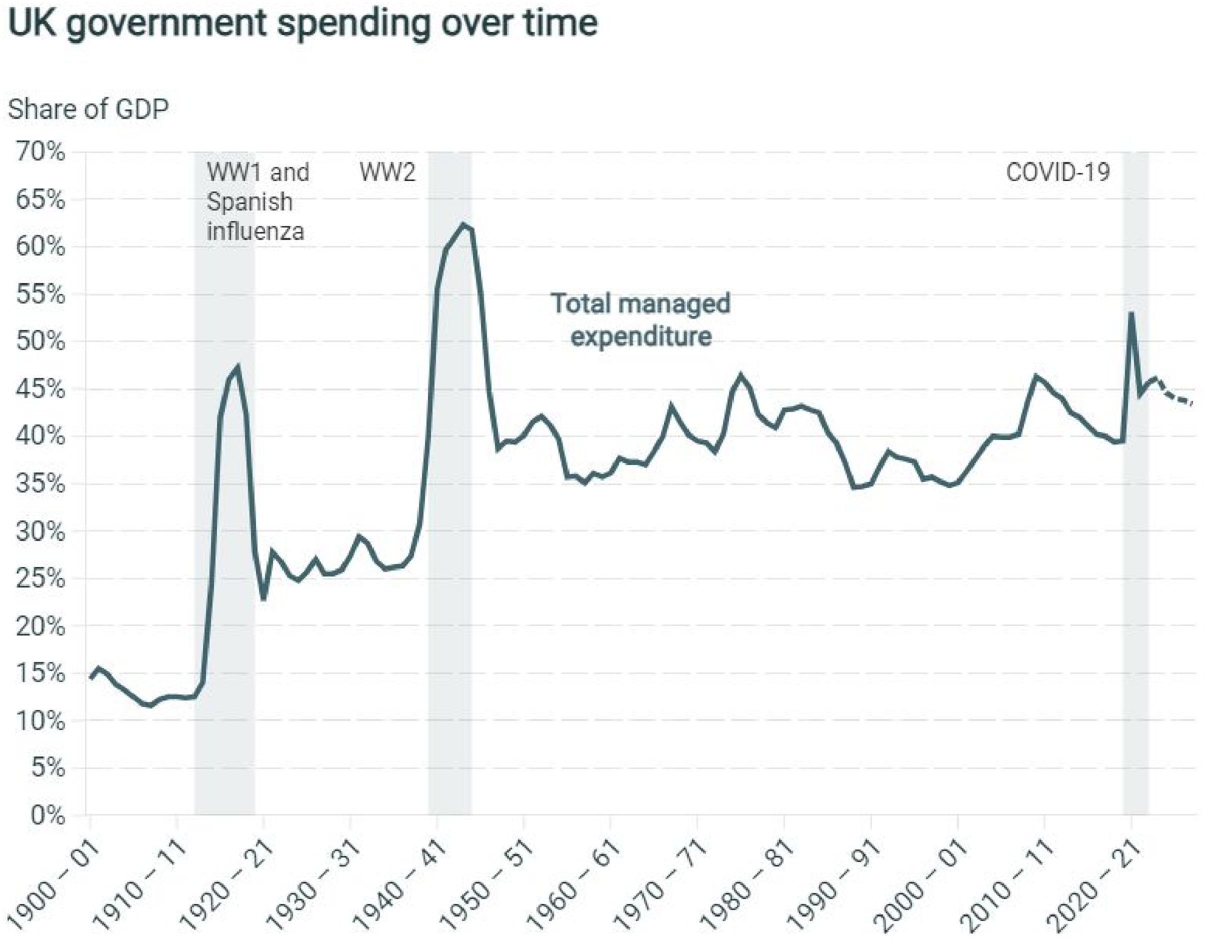
<u>Fiscal challenges</u>

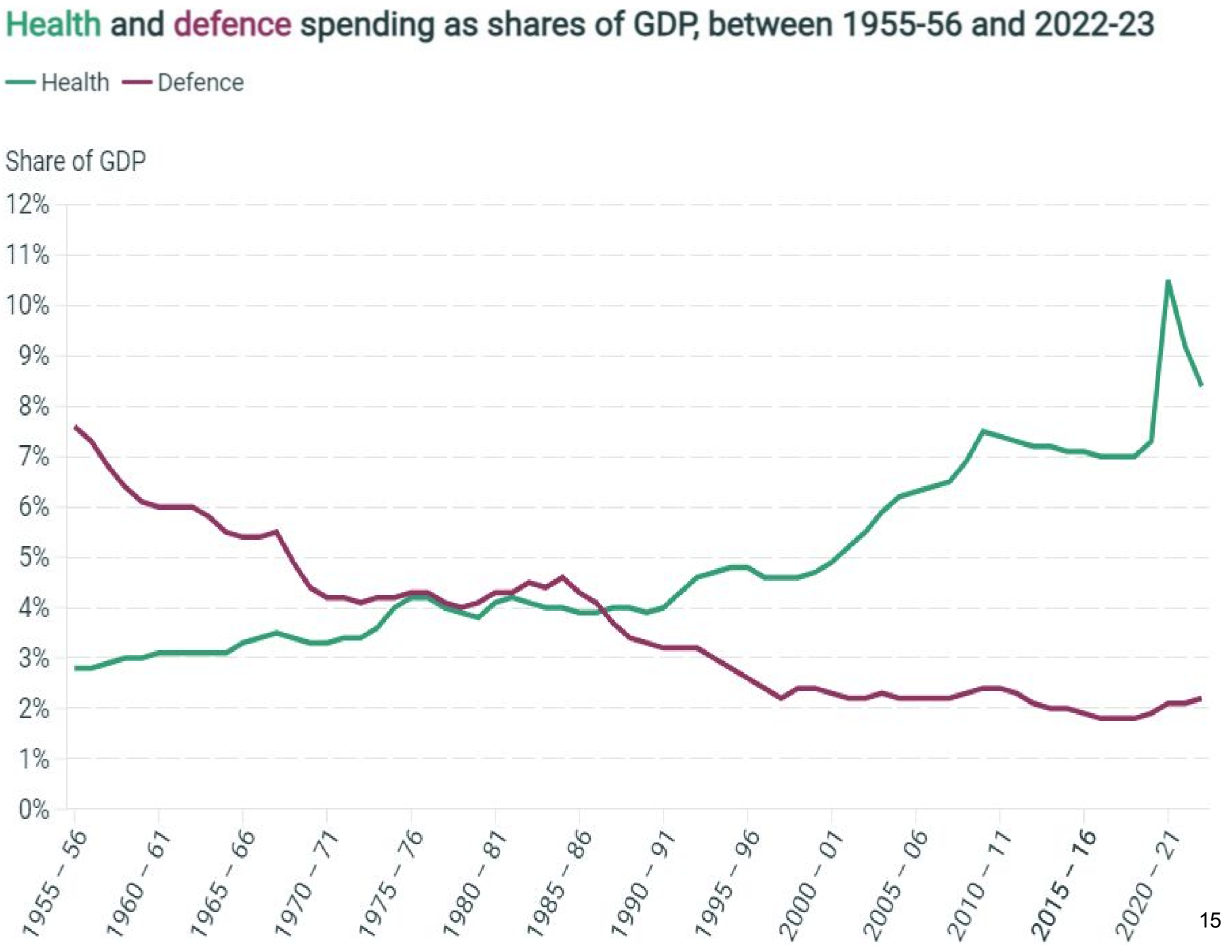
- £22bn 'blackhole' in government finances
- Limited headroom against first fiscal rule



Government Spending

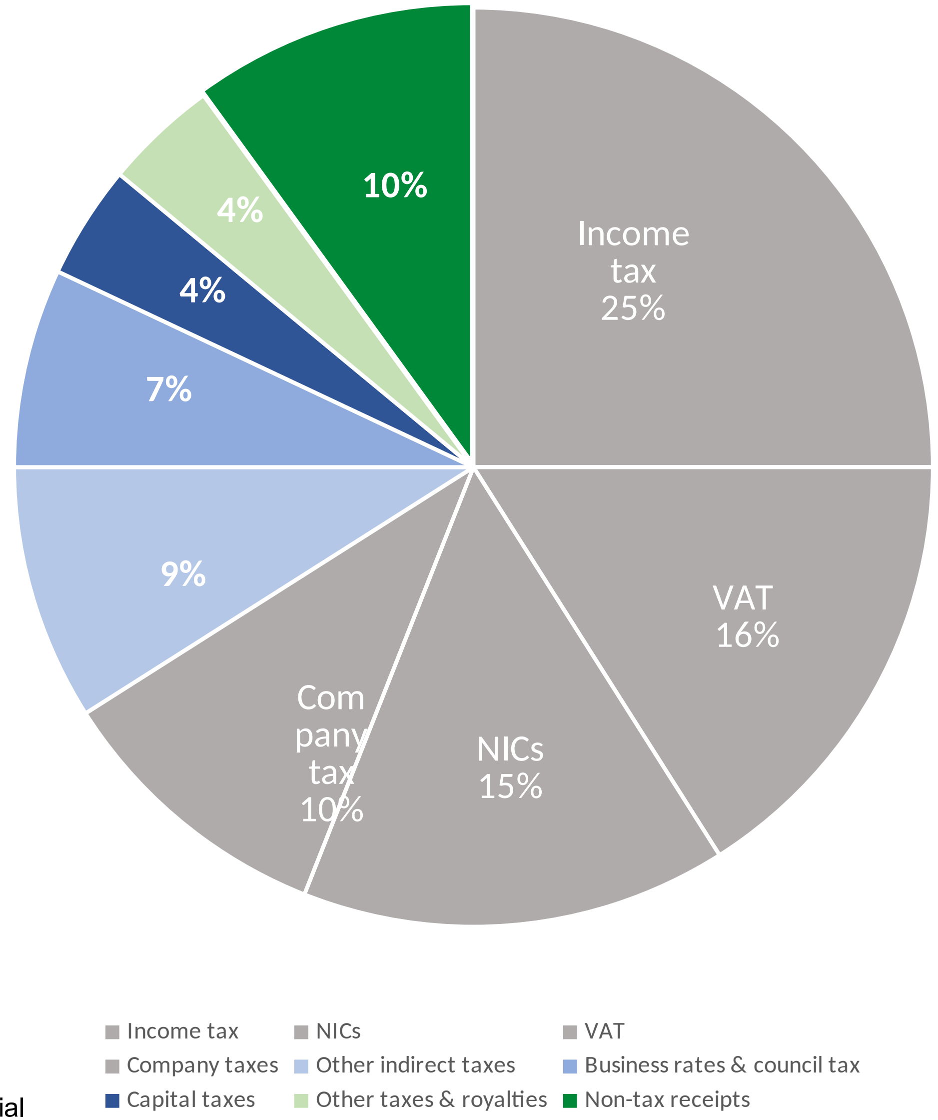
Data from the Institute for Fiscal Studies shows that spending on healthcare since 2007-2008 has increased around 50% in real terms to 2022-2023, compared to GDP which has grown only 18% in the same period.



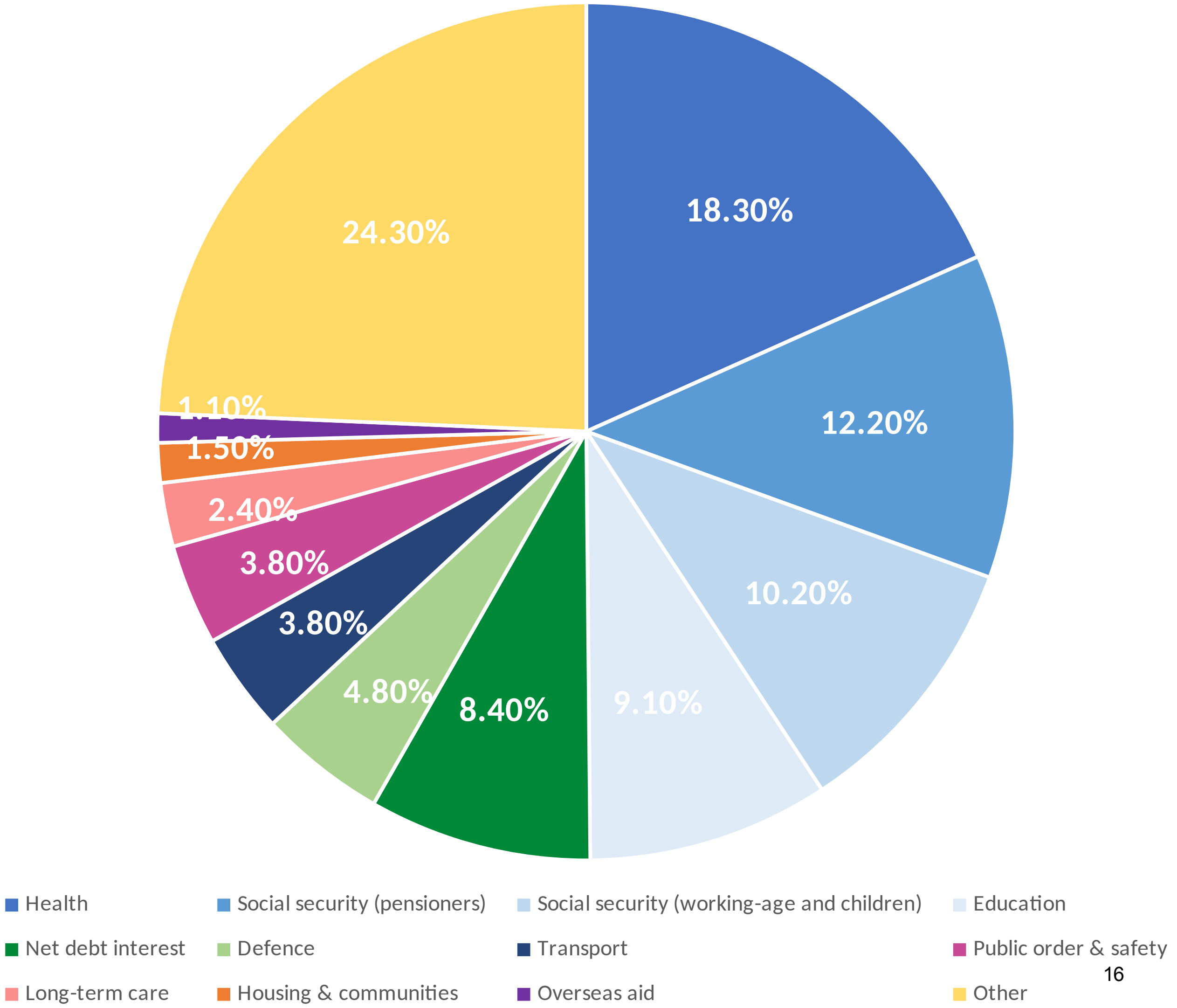


Government spending

Government revenue, 2023–24 forecast (£1.1tn)



Government spending in 2022–23 (£1.2tn)



30th October Budget – Raising Taxes

The government has already promised not to raise a range of taxes, which collectively deliver over 70% of tax revenue, meaning that the 30th October budget's tax raising is expected to focus on capital taxes and pension relief

"There's a Budget coming in October and it's going to be painful. Those with the broadest shoulders should bear the heavier burden."
Prime Minister Sir Keir Starmer

"The new Government is under no illusion as to the scale of the challenge we have inherited after more than a decade of low economic growth and a £22bn black hole in the public finances."
Chancellor of the Exchequer Rachel Reeves

Tax	Potential Saving (per annum)	Likelihood
Winter fuel allowance	£1.5bn	Very High
Fuel Duty	£2bn	High
Pensions	<£15bn	Medium
Capital Gains tax	<£9bn	Medium
Inheritance Tax	<£6bn	Medium
Council Tax	?	Low

Other Ways to Increase spending

- Break ‘red lines’ by increasing VAT, NICs or Income tax
- Borrow more money – (not currently possible whilst adhering to fiscal rules).
- Create new forms of tax – wealth tax?
- Falling interest rates – reduces the debt burden, thus increasing headroom.
- Amend the fiscal rules
- Use a different definition of debt – to exclude the losses made by the BoE from quantitative tightening – the FT estimate this could add £17bn to the headroom.

Any questions?