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ECONOMIC RESEARCH – MARCH 2025

INVESTMENT INSIGHT UK

- ✓ **Economic weakness continues into 2025**
- ✓ **Uncertainty does not support the British economy**

ATTRACTIVE BOND YIELDS

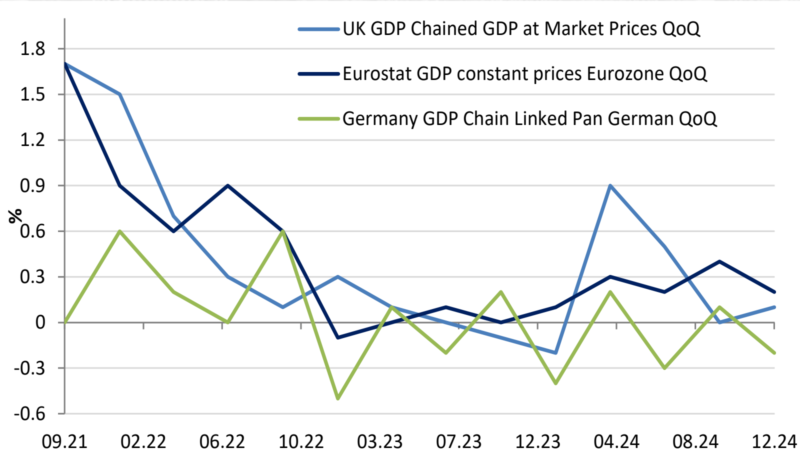
Unexpected economic contraction

The UK economy unexpectedly contracted by -0.1% in January, a notable reversal after a positive December. This decline marks the fourth monthly contraction in seven months, signaling a continued trend of economic uncertainty. The drop in manufacturing and construction output was partly due to difficult weather conditions, but these sectors are expected to rebound as conditions improve, potentially providing a temporary boost to the economy.

Weak domestic drivers and public spending reliance

Recent GDP figures for the fourth quarter of 2024 have also confirmed a significant slowdown in momentum. The annual GDP growth was a modest +1.4% (revised to +1.5%), essentially propped up by a substantial +0.8% rise in public spending. While the UK successfully avoided a technical recession, the underlying data remains a source of serious concern for observers. Both household consumption and private investment have shown persistent weakness, with consumption recording a third consecutive month of decline and investment falling by -0.9% after a positive contribution in the preceding quarter. These figures underscore the lack of robust, self-sustaining domestic drivers for growth as we move into the first quarter of 2025.

Quarterly GDP growth-United Kingdom



Sources : Bloomberg, BBGI Group

Escalating global uncertainty

Global political and trade uncertainty is casting a significant and palpable shadow over the British economy. The initial weeks of the new US administration, marked by a radical and surprising change in tone towards its economic and political partners, have unsettled market sentiment and heightened the risk of a global trade war. This climate of uncertainty presents a particular challenge for the UK, which has already found itself in a difficult position regarding its foreign trade since its departure from the European Union. While the British economy received some support from public spending at the end of the year, this is not a trend we anticipate to be a continuous factor in the months ahead.

Monetary policy and potential for rate cuts

The Bank of England's (BoE) recent monetary policy decisions reflect this cautious and complex economic outlook. Following a rate cut of 0.25% in January, the BoE opted to hold rates steady in March, a decision that came despite a slight uptick in inflation. This pause was likely influenced by core inflation figures, which came in better than anticipated and, in our view, provide the BoE with the necessary room for maneuver to potentially resume its rate-cutting cycle at its next meeting, scheduled for May 8th. This strategic move would be aimed at stimulating the economy without unduly reigniting broader price pressures.

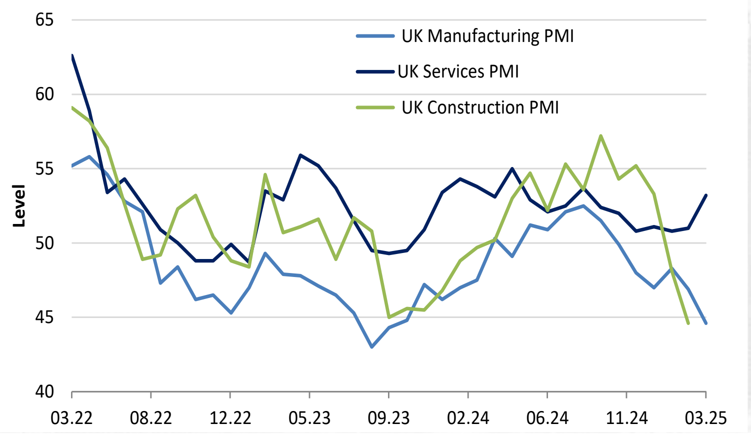
Moderate growth with external dependencies

Looking ahead to the remainder of 2025, the trajectory of UK economic growth will be more heavily and unpredictably influenced by international factors than domestic ones. The evolution of US trade policy under the new administration, particularly regarding tariff implementation, will have a direct impact on UK exporters and supply chains. We maintain our forecast for the British economy to follow a path of moderate growth, at around +1% for the year. This is a conservative yet realistic projection given the persistent challenges and the fact that domestic growth drivers remain subdued.

Persistent risks to economic stability

The overall economic environment remains fraught with risk, with the probability of a recession in the next twelve months still considered significant at 35%. The lack of supporting factors for a robust domestic recovery in the first quarter of 2025, as evidenced by a continued lull in household consumption and investment, underscores this fragility. A materialization of the growing risks of recession in the USA would also have profound knock-on effects for the UK's dynamic. This constant threat of contagion from a major trading partner presents a continuous risk that could undermine any tentative progress.

PMI indicators (manufacturing, services, composite)



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