Economic snapshot

by David Fenton, TSB's Chief Economist

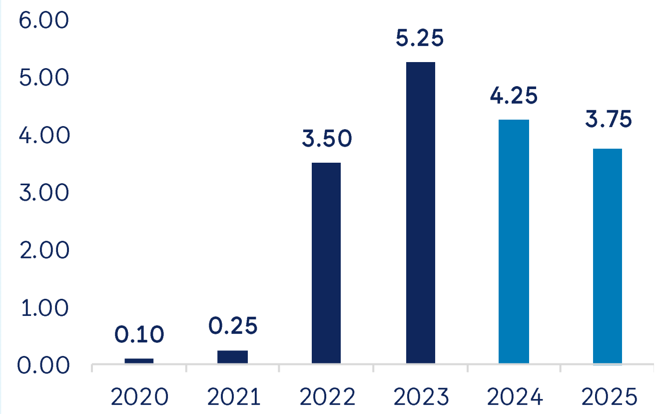
For many households, the festive season can be a time for managing expectations. The Bank of England (BoE) faced a similar challenge at its December meeting. Market expectations for rate cuts have led to a decline in swap rates, which are a key determinant of fixed-rate mortgage pricing. That's good news for borrowers but means that financial conditions are loosening at a time when Governor Bailey thinks there is "still some way to go" before inflation hits the 2% target. The BoE attempted to rein in expectations by reiterating its message that Bank Rate would need to be kept high for "an extended period of time".

Interest rates

5.25%

- The BoE left the policy rate on hold for the third meeting in a row, which reinforces the belief that it has peaked at $5\frac{1}{4}$%. The central bank said that the decision had been "finely balanced",. Indeed, three members of the Monetary Policy Committee voted for a quarter-point hike.
- Markets expect four rate cuts in 2024 (to 4.25%), with another two in 2025 (3.75%). The longer-term picture has fluctuated, but forward rates presently imply that the policy rate will ultimately settle around the 3% mark.

Market implied outlook for Bank Rate (year end)



Housing market

- Against all odds, it looks like house prices might end up posting a small increase in 2023 on the Halifax index. After back-to-back increases in October and November, prices are now somewhat higher than they were at the end of last year. We won't know for sure until we get the December data next month.
- The resilience of prices is consistent with what surveyors are saying about the balance of supply and demand in the market. The sales-to-stocks ratio has fallen, but is not especially low, and nowhere near the levels that have been associated with previous corrections.

Prices and inflation

4.6%

- Inflation fell "substantially" in October, as last year's steep rise in energy costs was followed by a small reduction in the price cap this year. Food prices and hotel prices were also a downward influence. The 4.6% reading for October was the lowest since Oct-2021 and below market expectations and the BoE's forecast (both 4.8%).
- The BoE said inflation would remain near its current rate in November and December. It flagged the possibility of an increase in January, due to base effects in the services sector, before resume its downward trend.

Jobs and earnings

- The official jobs data are still on hiatus, pending the introduction of a new and improved labour market survey next year. But the Office for National Statistics said there was a "largely unchanged picture", with the unemployment rate steady at around 4.2%. Vacancies continue to decline but remain high by historic standards.
- Wage growth is easing. The headline rate fell to 7.2% in October. That's higher than inflation, so wages are rising in real terms. The BoE remains vigilant about wage growth and the underlying tightness of labour market conditions

Economic activity

- GDP shrank by 0.3% in October, with the ONS saying that activity declined in the three main sectors of the economy (manufacturing, construction and services). A leading business survey showed a welcome improvement in November. S&P's PMI survey attributed this to two factors: "relief" at the pause in rate hikes and a "clear slowdown" in inflation.
- Even so, S&P suggested that Q4 is shaping up to be another period of stagnation for the UK economy. The BoE expects GDP growth to be "broadly flat" in Q4 – and to remain so in 2024.

TSB's economics snapshot summarises key data developments in the UK economy including growth, inflation, jobs, house prices and interest rates.
Data sources are BoE, ONS, Halifax, RICS and S&P Global. Interest rate outlook represents market forward rates as of 14th Dec 2023, inferred from SONIA via Bloomberg.