

Weekly Analysis

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BOE TO CUT KEY RATES IN AUGUST

The UK is already out of recession. Weaker growth in Q2. Inflation nears BoE target. Key interest rates to be cut soon. Positive outlook for bonds, real estate and equities.

Key points



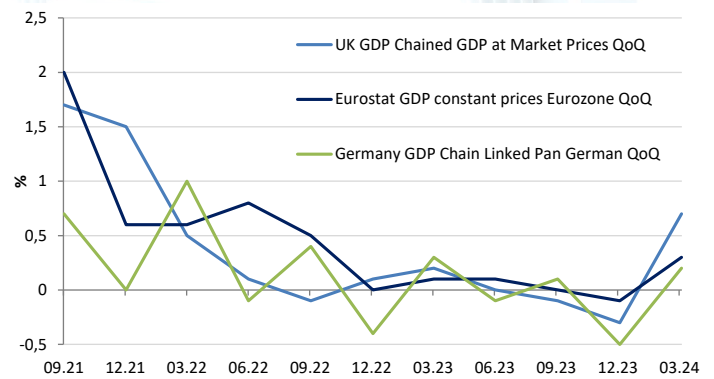
- The expected economic rebound is underway
- A probably weaker 2nd quarter
- Leading indicators continue to improve
- Falling tensions in the job market
- Household confidence continues to grow
- Inflation nears BoE target
- BoE soon in a position to cut rates
- Attractive yields and capital gains prospects for sterling bonds
- Limited prospects for pound appreciation
- It's always a good time to bet on securitized real estate
- Weak earnings growth expected for the FTSE100

The expected economic rebound is underway

After two quarters of moderate decline in UK GDP, we were expecting more positive developments and an upturn in activity at the start of 2024, based in particular on positive real wage growth and a more favorable trend in household purchasing power. Reported GDP growth for the 1st quarter was indeed more encouraging, coming in at +0.6%, well above consensus expectations of a slight +0.4% rise. Year-on-year, GDP thus went from negative growth of -0.2% in December 2023 to an increase of +0.2% at the end of March 2024. The UK is therefore rapidly emerging from an extremely modest recession, as we expected immediately after entering it. If the upturn at the start of the year is maintained, the high expectations of key rate cuts in the context of a UK recession will be adjusted and probably postponed a little, depending on inflation trends. The United Kingdom surprised once again at the start of the year with a quarterly rebound that was also the strongest quarter since the end of the health crisis, when the British government eased Covid-related containment restrictions. GDP growth was underpinned by a clear upturn in investment (+0.9%), gross capital formation (+1.4%),

government spending (+0.3%), as well as a revival in household consumption (+0.2%). Manufacturing also made a positive contribution, while exports declined.

Quarterly GDP growth-United Kingdom



Sources: Bloomberg, BBGI Group SA

A probably weaker 2nd quarter

This stronger-than-expected Q1 GDP growth certainly marks the start of an economic recovery in the UK. This should be supported over the coming months by a slightly more favorable combination of factors, including a likely change in monetary policy by the BoE. That said, after such an upturn, economic momentum is likely to ease slightly in Q2, as already suggested in part by the stagnation of monthly GDP in April (0%), following a +0.4% rise in March. The production and construction segments recorded negative contributions, offset by the positive trend in services. The -1.4% fall in the manufacturing segment, as well as the negative trend in consumption, were partly due to exceptional weather conditions.

The 2nd quarter will undoubtedly see growth, but still-high interest rates should continue to hold back any acceleration in economic activity before the summer. Recovery will undoubtedly be gradual and fragile, but should be helped by encouraging developments on the inflation front. In May, the CPI index fell below the BoE's 2% target, surprising many forecasters.