

UK in Focus

Economics
United Kingdom

The fastest growing economy in the G7?

- ◆ Strong Q2 GDP growth masks weakness in the private sector
- ◆ Uncertainty over the upcoming Autumn Budget could weigh on sentiment and activity
- ◆ A looser labour market could help dampen inflation concerns

The fastest growing economy in the G7

GDP data published in August, for the second quarter, was a mixed bag. Strength in the government sector was partially offset by weakness in the private sector, where a 0.2% q-o-q contraction was reported. However, taken as a whole, economic growth in the first half of 2025 was robust relative to a backdrop of heightened global uncertainty, a large rise in labour costs, 'Awful April' for consumer prices, and a weakening jobs market.

Some déjà vu in the third quarter

So far data for the third quarter has provided a little optimism on the activity front. UK PMIs point to an improvement in momentum relative to Q2, and consumer confidence ticked higher alongside stronger growth in consumer credit. There is the prospect that the second half of 2025 will look similar to that of 2024 as the UK government finds itself again in the midst of speculation that the Autumn Budget on 26 November will require a combination of higher borrowing, spending cuts, and tax increases. Indeed, markets, business and consumers alike have become more concerned over future growth, and UK borrowing costs have continued to rise.

Higher debt servicing costs, alongside reversals in planned spending cuts, and possible downgrades to growth forecasts all contribute to the erosion of fiscal headroom. How the Chancellor chooses to respond is more uncertain; we see a few possible scenarios, but the key decision will be whether the fiscal can be kicked down the road or is there the political courage to reset the public finances onto a more sustainable footing.

Looser labour markets are yet to weigh on inflation

Fiscal woes have seen yields on government debt, globally, rise sharply in 2025 but for the UK more specifically, sticky inflation is also a concern. Headline CPI rose to 3.8% y-o-y in July, driven by services and food prices. We think that headline CPI will top 4.0%, double the BoE inflation target, in the coming months. If price growth continues to be broad-based, that may warrant a pause in the BoE's current one-rate-cut-per-quarter pace until there is greater certainty that price pressures have abated.

That will depend on labour market loosening translating into softer wage growth. The unemployment rate has risen to 4.7%, and we expect slack will continue to emerge. But, while employment intentions are subdued, official data point to continued growth in jobs; the lack of reliable employment data only adds to BoE cautiousness.

KEY UK DATA

▼ **0.3%**

GDP growth in 3M to June

▲ **3.8%**

Consumer Price Inflation, July y-o-y

▶ **4.7%**

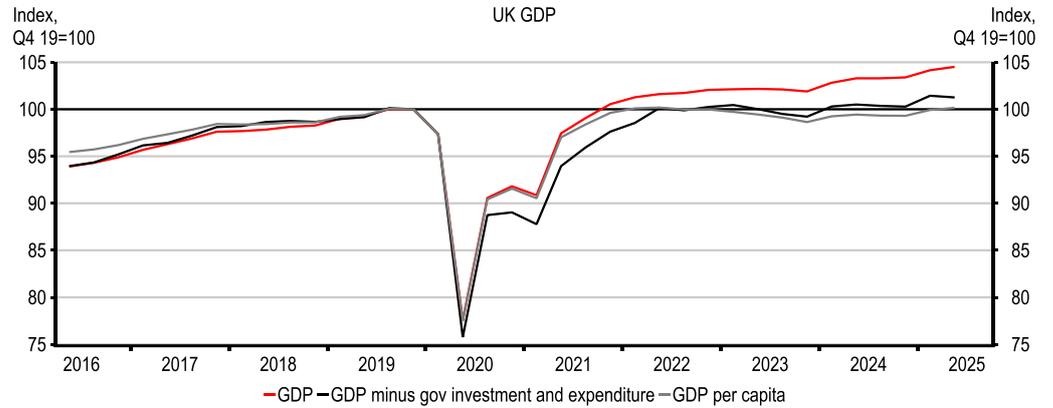
Unemployment rate, June

▶ **4.00%**

Bank of England Base Rate

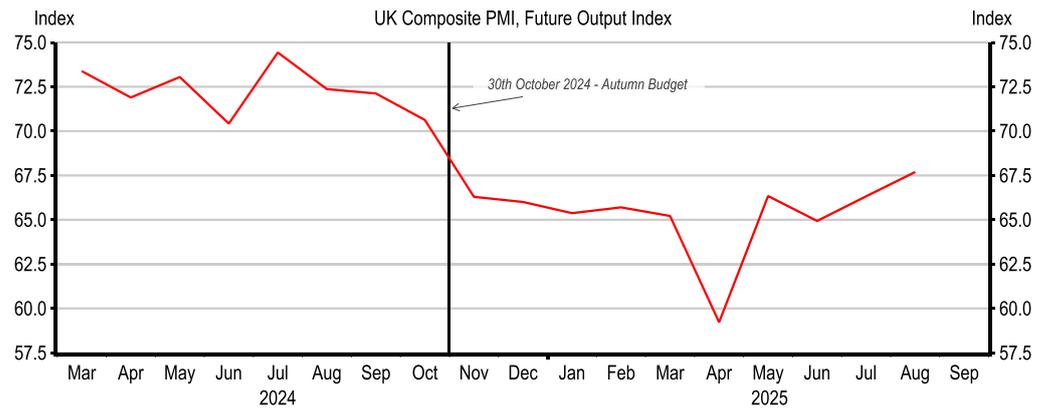
Source: HSBC

1. UK was the fastest-growing G7 economy in H1 2025, driven by the public sector



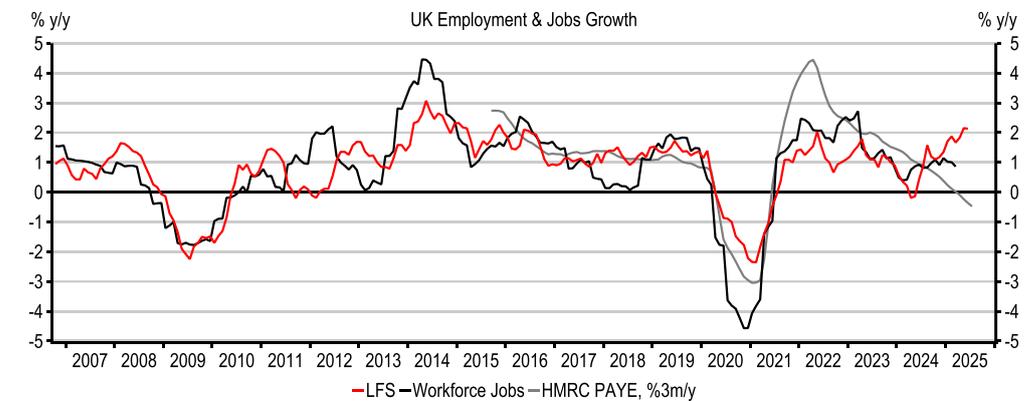
Source: Macrobond, ONS, HSBC calculations

2. Expectations of future output growth fell leading up to the 2024 Autumn Budget and haven't fully recovered ahead of the next Budget ...



Source: Macrobond, S&P Global

3. Contradictions across sources of labour market data add to policy uncertainty



Source: Macrobond ONS, HMRC

Disclosure appendix

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