

UK in Focus

Economics
United Kingdom

A better foundation for growth

- ◆ UK economic data showed a subdued environment in the run up to the Chancellor's Autumn Budget
- ◆ GDP growth slowed in Q3 while unemployment rose and pay pressures moderated
- ◆ The Autumn Budget left a more stable fiscal position but did little to bolster growth

Some greater stability gives a better foundation for growth

The months leading up to the UK Autumn Budget were clouded by high uncertainty and policy speculation, which appear to have contributed to a slowing in activity momentum. Indeed the PMI survey pointed to a slowing in growth in November with a notable downturn across the services sector, which reported a contraction in new order volumes. Notwithstanding that softness, against a backdrop of Budget uncertainty, activity surveys have been a less reliable signal of overall GDP growth, in fact, overestimating economic growth in Q3. The UK economy eked out a 0.1% q-o-q expansion in the third quarter as business investment fell, and despite a small uptick in household consumption, a slowdown in government spending, which has been a driver of growth in recent quarters, weighed on overall growth.

It's possible that the economy sees a 'bounce-back' in the coming quarters. With the majority of fiscal tightening backdated into future years, the near-term outlook is little changed. While greater 'headroom' against the Chancellor's fiscal targets should see a period of greater policy certainty, if that can translate into higher confidence, then the UK could see some upside news in Q1 2026. Following the 2024 Autumn Budget and a weak H2 2024, Q1 2025 growth was robust at 0.7% q-o-q. But let's be honest, given the low bar set in Q3 (and expected in Q4), some relatively more positive news early in 2026 shouldn't be too difficult.

Higher unemployment and slower pay growth

Elsewhere, a weak demand backdrop and higher unit labour costs have seen a continued softening in the labour market throughout 2025. The unemployment rate rose to 5.0% in the three months to September and more timely payroll and survey data point to further headcount reductions in Q4. Private sector pay growth slowed to 4.2% 3m/yr in September and given the slack building in the labour market, we expect more muted pay pressures into 2026. However, a further increase in the National Living Wage to around 66% of median earnings and over 70% in some regions is new territory for the UK economy, while firms' wage growth expectations have ticked higher in recent months, to 3.8%, up from 3.5%. Whether firms respond through headcount reductions or higher inflationary pressures, both are risks for the UK economy in 2026.

KEY UK DATA

▼ 0.1%

GDP growth in 3M to September

▼ 3.6%

Consumer Price Inflation, October y-o-y

▲ 5.0%

Unemployment rate, September

▶ 4.00%

Bank of England Base Rate

Source: HSBC

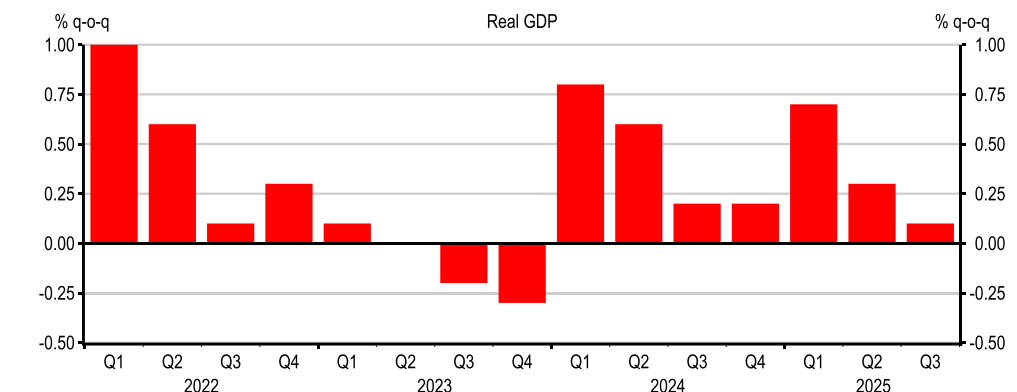
UK Autumn Budget: Economic need to know for businesses

From a macroeconomic perspective, there was very little in the Autumn Budget that was judged to bolster economic growth – the OBR went as far as explicitly saying so. As such, and despite higher government borrowing and expenditure in 2026, the OBR downgraded its annual 2026 GDP forecast to 1.4%.

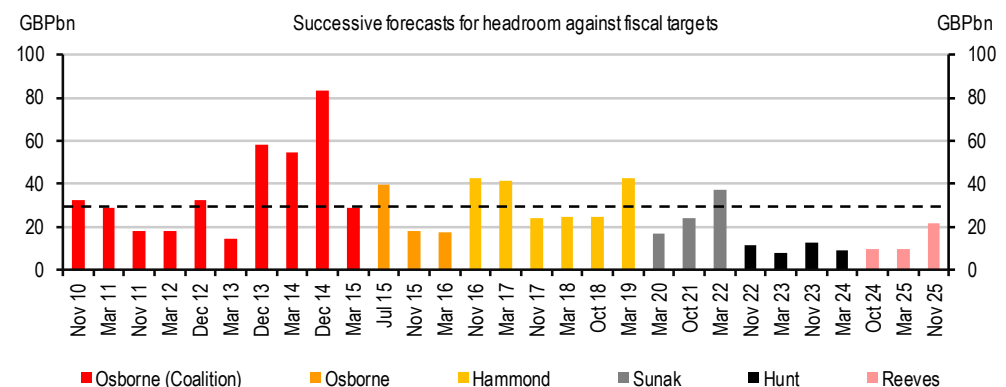
While a lack of substantial growth initiatives is a disappointment, the additional headroom against the main fiscal target to have the current budget balance in 2029/30 was welcomed. An increased margin of error from GBP9.9bn to GBP21.bn conditioned on a lower GDP growth path raises the bar for that headroom to be eroded and improves the resiliency of the UK to market or external economic shocks. Indeed, the market reactions in government bond yields and sterling have been positive.

However, the Budget did little to address the underlying challenges in UK public finances and therefore medium to longer term risks remain. Namely the prospect of further undershoots in the UK's economic performance. Notably, despite the downgrade to productivity growth to 1.0%, the OBR remains more optimistic than other forecasters and the historical average. Moreover, with tax rises and some real-terms departmental spending cuts pencilled in for 2029/30, it raises the risk of 'fiscal fictions', i.e. whether those measures will be enacted when the time comes. To address those concerns, the government has announced its intention to bring forward passing legislation on some measures: at the time of writing, the cap for pension salary sacrifice at GBP2,000 appears to be the focus, alongside updated business rate valuation – both additional costs to firms in the coming years.

1. UK activity growth has been weak, but we could see a post-Budget bounce



2. A larger amount of headroom should offer some policy stability, for now at least



Disclosure appendix

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