9 April 2026

UK in Focus

Economics
United Kingdom

A weaker but more uncertain outlook

- The latest energy shock points to an undesirable mix of higher inflation and slower growth…
- …but it's not like 2022, so the policy response will likely differ
- The bar to hike rates is high, in our view, but uncertainty is also very high

An energy shock weakens the outlook and brings greater uncertainty
The Middle East conflict and resulting energy shock has made the UK's narrow path to recovery in 2026 even narrower. The spike in energy prices in March, damage to energy infrastructure, and effective closure of the Strait of Hormuz, have created a less favourable mix of higher inflation and slower growth. In our base case scenario, the conflict is resolved relatively swiftly, oil prices fall back, inflation peaks at 3.4% in November, and rate cuts are delayed to 2027. However, uncertainty is high and how the conflict evolves will be crucial for the UK economy in 2026 and 2027.

That said, the interest rate policy reaction to the latest energy shock is unlikely to be comparable to that of 2022. Why? The size of the immediate energy shock is smaller, interest rates are already restrictive, widespread fiscal support is unlikely, and the economic backdrop is vastly different. That starting point matters. Unlike 2022, UK economic growth is below potential, unemployment has been rising, wage growth cooling, and price pressures in the broader economy are weaker. Indeed, consumer confidence has been subdued for some time, and the initial reaction in the March survey saw just a 2pt decline, although that may fall further as higher prices begin to pinch and there is less scope to rely on savings to smooth consumption.

Therefore, while we think that the risks to our inflation outlook are to the upside – given the degree of uncertainty and potential for a more protracted conflict than assumed in our base case – the bar for the BoE to hike, in our view, is high. That upside risk is reflected in the recent volatility of financial conditions. But policy makers at the BoE will not want to overreact to an energy shock and place undue pressure on an already weak economy.

Nonetheless, the BoE will be on high alert to signs that inflation pressures spread beyond the mechanical energy uplift, and lead to a de-anchoring of inflation expectations. So far, firms have not reported a significant rise in their own expected price growth and 3-yr CPI expectations remain stable. The prospect of weaker demand may be of greater concern to the services sector. Even if price pressures do begin to rise, limited pricing power may limit the pass through, notwithstanding the strain on margins and subsequently possible weaker investment and employment growth. In our view, unemployment will continue to rise over the next year.

KEY UK DATA

▲ **0.2%**
GDP growth in 3M to January

► **3.0%**
Consumer Price Inflation, February y-o-y

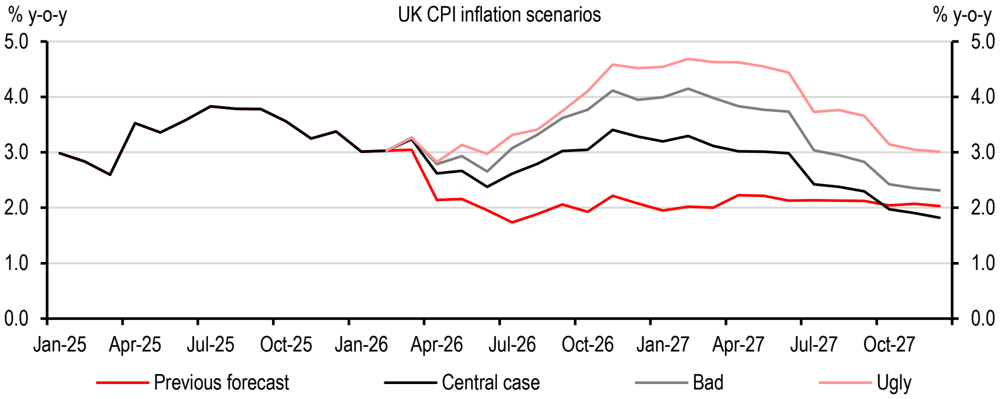
► **5.2%**
Unemployment rate, 3M to January

► **3.75%**
Bank of England Base Rate

Source: HSBC

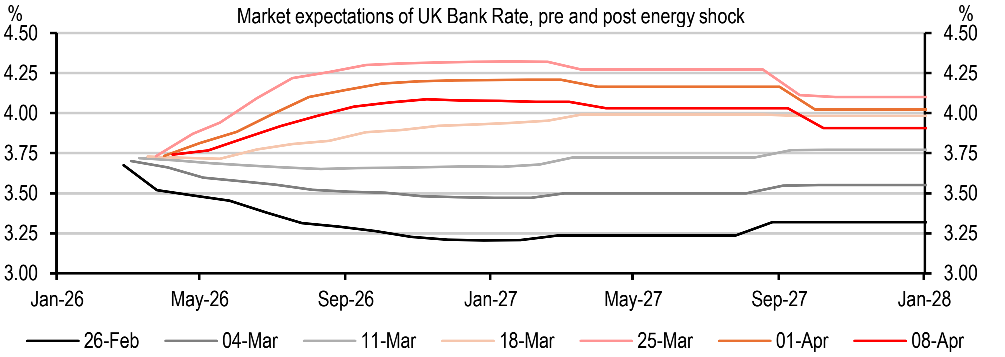
HSBC

1. UK inflation is set to accelerate in 2026, with upside risks to our central case



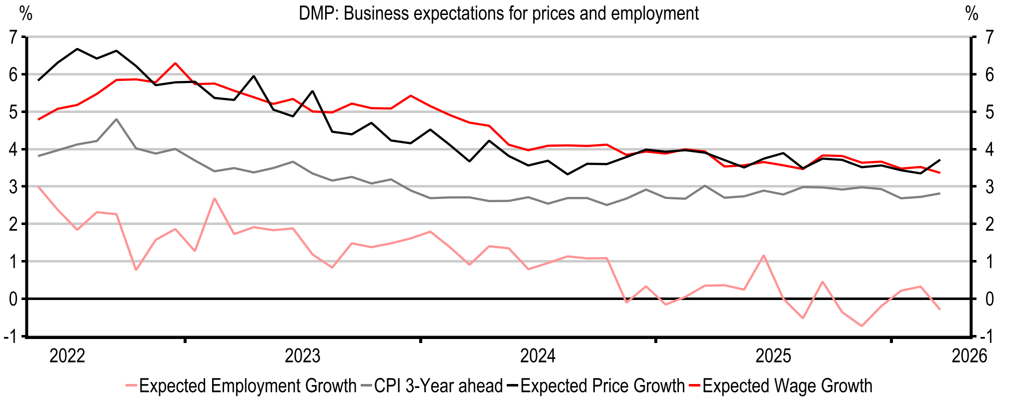
Source: HSBC forecast inflation scenarios as of 23 March 2026

2. Market expectations of UK Bank Rate has been volatile, as the probability of different inflation scenarios and BoE reactions have been considered



Source: Macrobond, Bloomberg

3. Firms expected price growth rose by 0.3ppts in March, but expected employment and wage growth fell



Source: Macrobond, BoE Decision Maker Panel, HSBC

Disclosure appendix

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