

*Market Monitor – United Kingdom*

**GDP Stabilises but Headline Inflation Edges Higher**



**GDP rises again in May, following upwardly revised figure for April**

The UK economy recorded better than expected 0.5% month-on-month growth in May, after an upwardly revised 0.2% decline in April. All the main economic sectors saw expansion in May, with the services sector recording month-on-month growth of 0.4% and manufacturing 1.4%. Output in the construction sector grew by 1.5% month on month in May, representing a seventh consecutive month of growth. The improvement in the services sector in May was mainly driven by more appointments at general practitioners and strong growth for travel agencies, while the rebound in manufacturing output may be an initial sign of an easing of supply chain bottlenecks.

**Headline inflation edges higher and BoE raises interest rate by 50 basis points**

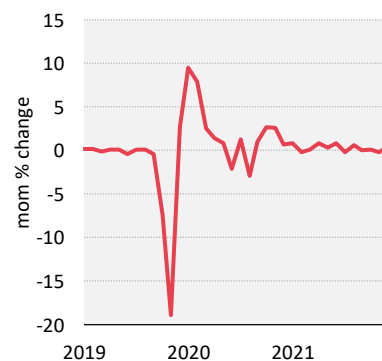
The UK labour market remains tight. The unemployment rate for March-to-May stayed unchanged at 3.8%. Meanwhile, wage growth eased in the three months to May, with average weekly earnings including bonuses rising 6.2% year on year (YoY) in March-to-May, down from the 6.8% YoY increase in February-to-April. This was mainly due to bonus payments returning to a relatively moderate level during the period. As international energy prices remain high amid the ongoing Russia-Ukraine conflict, inflationary pressure in the UK remains elevated. The consumer price index (CPI) registered a 9.4% YoY growth in June, up from a 9.1% rise in May. The core CPI also recorded YoY growth of 5.8%, only 0.1 percentage point lower than in the previous month. Consumer confidence remained weak as surging food and fuel prices, plus rising interest rates, continued to dampen the nation’s financial sentiment. The Gfk consumer confidence index stayed at a historic low of -41 in July. Against the background of weak consumer confidence, retail sales volumes fell 0.1% month on month in June, following a 0.8% drop in May.

**UK GDP sees renewed growth in May as services sector stabilises and manufacturing sector rebounds.**

**Consumer sentiment remains sluggish as Gfk consumer confidence index stays at historic low of -41 in July.**

**BoE raises Bank Rate by 50 basis points to 1.75% at its August meeting, the biggest hike in 27 years.**

**UK GDP**



Source: Bloomberg, data as of 22/7/2022

With inflation reaching a record-breaking level, the Bank of England (BoE) raised the Bank Rate by 50 basis points to 1.75% at its August meeting, the biggest hike in 27 years and accelerating from its previous 25 basis point pace. The BoE expects UK inflation rate to climb further to rise above 13% in Q4 2022, as the cap on energy bills will be set at about 75% higher. Meanwhile, the BoE projected that the UK economy would enter into a recession later this year with economic output declining from Q4 2022 to Q4 2023. Besides, the BoE laid out its plans for reducing government bond holdings in the Asset Purchase Facility (APF). It expects that a 12-month sales programme will begin in September 2022 and the stock of APF will decline by about GBP 80 billion in total, implying about GBP 10 billion sales per quarter after taking into account running off of maturing bonds during the period.

Looking ahead, the elevated inflationary pressure is going to be more persistent than previously expected, and the BoE is likely to continue tightening its policy at the remaining meetings of 2022. Household consumption, which accounts for about 60% of the UK's GDP, may grow at a slowing pace in the months ahead, as household incomes will be squeezed by higher inflation and tighter financial conditions. According to a Bloomberg survey in July, the UK's growth outlook is expected to drop to 3.4% and 0.7% in 2022 and 2023 respectively, 0.3 and 0.5 percentage points lower than its June survey. In addition, the BoE's latest forecast in August showed that the UK economy would contract by 1.25% in 2023, revised lower by 1 percentage point from May's projection. This implies that market may have room to further downgrade the economic outlook of the UK, if consumer sentiment further deteriorates.

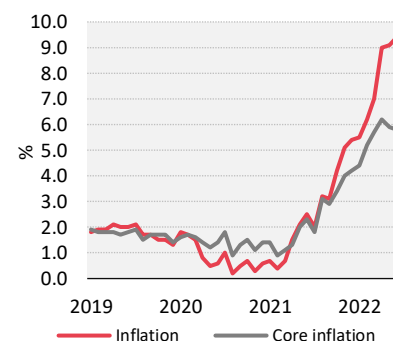
### Equity market rebounds mildly, pound has mixed performance, and bond yields edge downward

The UK equity market experienced a mild rebound in July after a significant correction in the previous month. This was mainly driven by monthly gains in the financial, consumer, and industrial sectors. As of 29<sup>th</sup> July, the FTSE 100 Index was about 3.5% higher than at the end of June.

In the bond market, UK government bond yields have edged lower in July after a surge in the previous month, mainly due to a gloomier local and global economic outlook amid high inflation, geopolitical uncertainty, potential disruption of energy and food supplies, and ongoing monetary tightening by major central banks. As of 29<sup>th</sup> July, the 10-year UK government bond yield stood at 1.864%, down 37 basis points from the end of June.

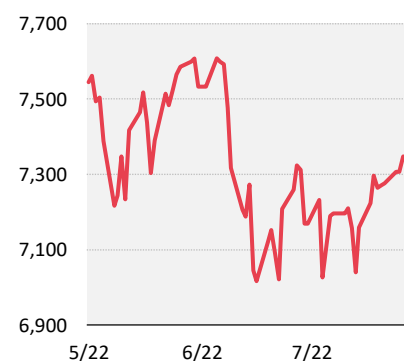
In the foreign exchange market, the British pound continued to weaken against US dollar but strengthened against the euro. As of 29<sup>th</sup> July, the British pound had depreciated by 0.1% against the US dollar but appreciated by 2.5% against the euro.

### UK Inflation



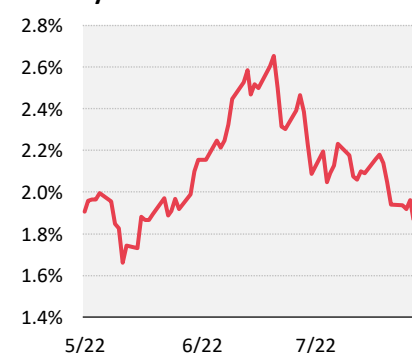
Source: Bloomberg, data as of 22/7/2022

### FTSE 100 Index



Source: Bloomberg, data as of 29/7/2022

### UK 10-year Government Bond Yield



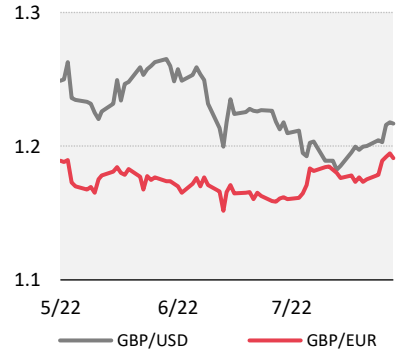
Source: Bloomberg, data as of 29/7/2022

## Economic Research

August 2022

Looking forward, the UK's financial markets will continue to be impacted by uncertainties stemming from the relationship with the European Union and domestic political issues such as the change of prime minister and the potential for a second referendum on Scottish independence. Any sudden change in investors' risk appetite will result in greater volatility for the UK financial markets.

**British Pound Exchange Rate**



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