



UK economy moving back towards EU orbit

Following several months of soft macro data, last week's UK GDP data suggest something of an upturn in activity of late and raises the question of whether the UK economy has turned a corner. Those GDP data showed a solid 0.7% gain on the quarter in Q1 2024, up 1.1% year-on-year.

What was a solid nascent recovery at the start of 2024 petered out in the second half of the year as both consumer and business sentiment surveys sunk following the gloomy rhetoric of the new Government, and the significant tax rises announced in the Autumn budget, particularly the hike to national insurance for employees. The uncertainty created by the Trump tariffs, and higher gilt yields also added to the general sense of malaise in the early months of 2025, culminating in the Chancellor announcing further spending cuts in the Spring Statement in April to meet her new fiscal targets. Following the Liberation Day tariffs, forecasters have also been trimming growth prospects for the UK and other European countries.

However, the UK was spared the worst of the reciprocal US tariffs, receiving a 10% baseline rate, while the framework trade deal announced by the US and UK in recent weeks suggests a willingness on the part of the Trump administration to move to a more favorable position with the UK, and at a faster pace than with the EU. While the UK is still worse off than the January 2025 baseline in terms of US tariffs, it did strike key concession for its steel and car industries.

More importantly, the rapprochement with the EU, including an emerging deal on alignment of food standards and fisheries access, could provide a basis for a closer relationship with its largest trade partner, using the cover of global trade uncertainty to undo some of the Brexit frictions. Nevertheless, the announced curbs on migration to the UK might offset some of the gains from a closer EU relationship, given the reliance on foreign labour to plug skills gaps across the economy.

Taken together, the near-term outlook is probably for continued modest growth, but if the Government can stay the course in deepening ties with its largest trade partner in the EU, and its growth agenda in infrastructure and regulatory reform, there may be some upside to the UK economy in the medium term.

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