

UK – Better growth, but watch for labour market weakness

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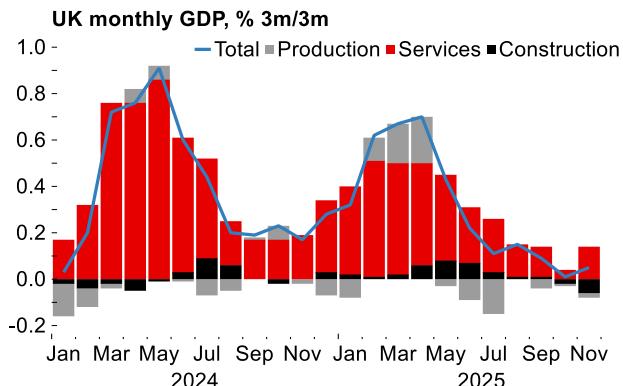
- Resilient services output combined with rebounding manufacturing activity to lift UK GDP growth to 0.3% M/M in November. We are now tracking growth at 0.2% Q/Q across Q4 as a whole, which would be decent enough in the context of Budget uncertainty.
- Looking ahead, we see annual average GDP growth at 1.2% this year. Meaningful disinflation and further BoE easing is likely to support activity. The obvious downside risk stems from the labour market which was limping into the new year. Redundancy data suggests that slack will continue to emerge – next week's data will shed more light.
- Today's activity data and perhaps an uptick in headline inflation next week could give the divided BoE some pause for thought. However, we continue to believe that a loose labour market and progress on wage growth could ultimately give policymakers the green light for the next cut as soon as March.

The economy looks to be carrying reasonable momentum into 2026

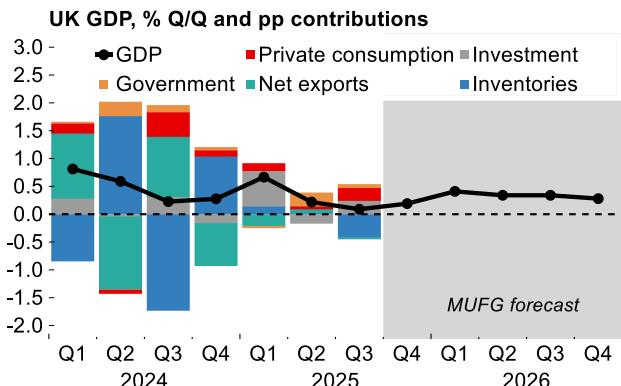
The UK economy looks to have been on a better footing than expected heading into 2026, despite the drag from Budget speculation in the autumn. GDP growth surprised to the upside in November at 0.3% M/M, the best single-month figure since last June. Strong services growth (+0.3% M/M) was especially encouraging. There was also a sharp rebound in manufacturing (2.1% M/M) as car production bounced back from the damaging cyberattack incident in September. The big blemish was construction output, which fell by 1.3% M/M. The dire [PMI](#) suggested a headwind from fiscal uncertainty (the December print was scarcely any better, however, and the government's ambitious construction [pledges](#) continue to look fanciful). Overall, these numbers support the wider theme of economic resilience in the face of tariffs and geopolitical uncertainty (see e.g. [here](#)).

That said, it's never wise to read too much into single-month GDP figures, volatile and prone to revision as they are. Indeed, there were some favourable revisions to the historical data, as previously flagged by the ONS in its quarterly accounts. The result is solid carryover into the Q4 figure which offsets the contraction recorded in October. Even flat growth in December would now correspond to a quarterly figure of 0.2% Q/Q, which is what we're tracking. It would be another case of growth fizzling out through the year, but in a quarter marked by heightened fiscal uncertainty it would be by no means a terrible outcome. The BoE expected flat growth (0.0% Q/Q) at the last policy meeting, pre-revisions to the historical numbers.

Services activity supports better growth momentum



We expect another decent start to the year in 2026



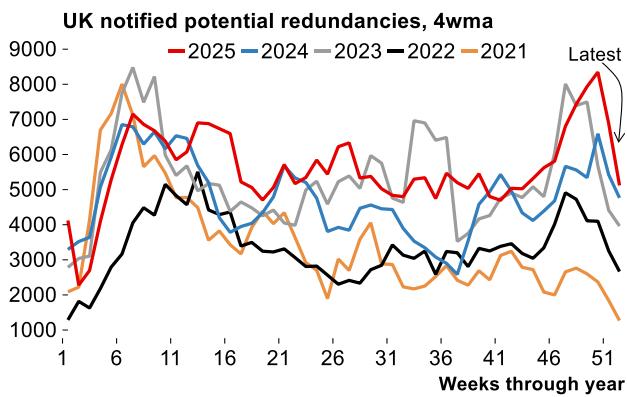
Disinflation and stimulus to come

Looking ahead, there are various supportive factors for activity in 2026. It is set to be a year of meaningful disinflation – we expect headline inflation rate will average 2.1% in H2 2026, down from 3.4% in Q4 2025, as base effects and government policy take hold. That is set to support real income growth and consumer confidence. We expect two more BoE cuts this year to 3.25% (with risks tilted towards more easing), which would further help activity. The mild fiscal loosening announced at the [Budget](#) will be an additional tailwind, and perhaps AI-related activity too.

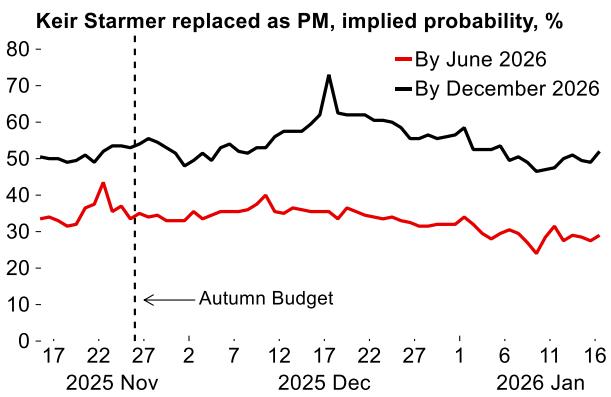
For Q1 2026, we've pencilled in growth of 0.4% Q/Q – not as strong as Q1 2025, which was helped by US front-loading, but supported once more by some post-Budget rebound in activity. [On an annual basis we look for growth of 1.2% in 2026](#), from 1.4% in 2025, with smaller carryover into the annual growth figure.

We judge that risks around our forecast are tilted to the downside. If the recent pattern of stronger UK growth at the start of the year is not repeated then sub-1% annual growth could suddenly look very plausible, and the mood music around the economy would likely worsen. There are several obvious risk factors. External conditions matter: a sharp slowdown in the US economy would weigh on the UK services sector. Domestically, political uncertainty could rise around the local elections in the spring. Prediction markets suggest it's 50-50 whether PM Starmer will last the year in office and alternative leadership would heighten policy uncertainty and, we suspect, raise fiscal risks.

Redundancy data points to continued labour market slack



Will domestic policy uncertainty increase?



Will evidence of labour market slack continue to build?

The risk of more abrupt labour market loosening will also remain in focus. The effects of restrictive monetary policy and regrettable government interventions are clearly weighing on the UK jobs market. The economy was shedding jobs at a steady clip last year – payroll employment was down 171k in the latest numbers for November. More recent data such as redundancy notifications points to a further increase in joblessness.

In that context, jobs and pay figures take on additional significance. Attention now turns to next week's labour market release. We expect to see further broad evidence of labour market slack: a slightly higher unemployment rate, another fall in payroll employment and slightly lower wage pressures. The following day could see headline inflation tick higher on food prices, however, which, combined with today's GDP beat, would be flagged by the MPC's hawkish contingent. As we [noted](#) after the last policy meeting, a cut in March is plausible but it is a close call and will likely require some clearer evidence of progress towards target-consistent pay growth (i.e. ~3%) in the annual settlement figures between now and then.

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