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Economic outlook 2024: what lies ahead for business

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Panel

Sam Fleming, economics editor, Financial Times
Catherine Mann, professor of the practice at Brandeis University and an external member of the Bank of England's Monetary Policy Committee
Lord Willetts, president, Resolution Foundation
Charlie Nunn, group chief executive, Lloyds Banking Group

In the latest event, Sam Fleming, the FT economics editor, moderated a panel discussion on the UK's economic outlook for the next 12 months. On the panel were Catherine Mann, professor of the practice at Brandeis University and external member of the Bank of England Monetary Policy Committee; Lord Willetts, president of the Resolution Foundation, and Charlie Nunn, group CEO of Lloyds Banking Group.

Here are the highlights.

Is the UK economy through the worst?

For Catherine Mann, the answer is yes, Britain is through the worst in relation to “the degree and extent of inflation as well as the extent of growth”. But “both have a very big ‘but’”. She said people should “be thinking of inflation as a rollercoaster: we ratcheted all the way to the top and now we’re coming down – but that doesn’t mean when you come down there are no bumps on the way”.

Putting numbers against her analogy, she said inflation was starting at 3.6% this quarter, will fall to 2.2%, rise again to 2.7% and then to 2.8%. “It’s a little bit of a rollercoaster for headline inflation.”

As regards growth in gross domestic product, she was most concerned about “the potential inflationary consequences [of] the limitations on supply”.

Lord Willetts said: “I think we are past the worst in the sense of the technical recession we just entered, but it’s all going to be pretty feeble stuff”. He said one issue facing the UK economy was the end of fixed-rate mortgages for as many as 1.5mn households.

He said research by the Resolution Foundation, the think tank of which he is president, found that the real cost of borrowing for mortgage-holders has been temporarily limited by their being on fixed rate deals. With many such arrangements coming to an end this year, mortgage-holders will have to move to more expensive packages, which will impinge on their disposable incomes.

Charlie Nunn was more optimistic. He believed the economy looked different depending on an individual or a company’s circumstances. While 20% of households “have really found the cost of living and inflation difficult, only below 1% can’t make ends meet”. He also said that while people on fixed-rate mortgages would find it costly to switch, they do “on average have twice the average income of the UK: £75,000” and may be able to adjust.

At the other end of the income scale, Nunn said the top 20% “have a much larger percentage of savings in the UK economy [and] have seen their savings grow over the last 24 months”. As a result their “spending on things like travel, hospitality and some discretionary items” are “at high levels, even on a real basis relative to pre-Covid”.

Nunn said the “mixed story” applied to companies too. Some sectors, notably hospitality, transport and commercial property, continue to encounter stress, he said. Small and medium-sized enterprises, “the lifeblood of the economy”, are facing challenges.

On the other hand he pointed to “the strongest business sentiment at the start of 2024 that we’ve seen since the start of 2016”. Companies have said that some of last year’s problems – employment costs, supply chain inflation and weak demand – are receding.

Why services are causing the Bank to be cautious over interest rate cuts

The Bank of England increasingly focused on the heterogeneous nature of the UK economy, Mann said. As a case in point, the Bank looked at “the decomposition in terms of goods versus services prices”.

She said that while “goods price inflation is almost zero on a three-month over three-month basis”, services prices remained “very, very sticky”. They were “one of the key elements the Monetary Policy Committee has put out there as an indicator of the persistence in overall inflation in the economy”. One reason for this stickiness is what she called “a lack of consumer discipline”.

Elaborating on this, Willetts pointed to “some significant Covid effects”. He said “Covid led to forced unanticipated saving by affluent people who couldn’t go out to the theatre and expensive restaurants”. They are now making up for lost time.

Boosting productivity: participation

Large numbers of people are not participating in the UK economy, in particular, older people who, as Willetts said, "exited the jobs market because of Covid" and have not returned. He suggested that the UK pensions system is one problem. "We have an unusually high proportion of pension incomes from funded pensions," he said, "and with funded pensions you can collect your income from as early as 55."

The Resolution Foundation has proposed that the government should raise the age at which pension holders can take funded pension savings so that people "can't withdraw from the workforce and access funded pensions in their mid-50s".

Boosting productivity: migration

Willetts said that "one of the factors which boosts our total growth, but not GDP per head, is the fact that it looks as if migration is pushing up the size of the working age population". He suggested that this trend may continue because new figures from the Office for National Statistics show "higher population projections".

Mann added a word of caution. She agreed that migration is "an important feature" but said: "I think we have to look at the composition [of the immigrant population]." She said many immigrants were students who "don't contribute to the supply side in the same way as people who come in with a job".

Boosting productivity: cities

Willetts said the UK economy had to become less London-centric. He cited a joint report from the Resolution Foundation and the London School of Economics. Willetts said it was "striking … how poorly our second cities perform". He said: "To put it crudely [Birmingham and Manchester] "aren't as big as they appear to be, and they aren't as big as they ought to be". He suggested that "one way of boosting productivity is to have bigger 'travel to work' areas in the midlands and the north".

Boosting productivity: investment

Nunn spoke about foreign direct investment and said that although the UK was "not as strong" as it was, it is "still strong on a relative basis to other countries". Having said this, he went on to argue that the UK FDI "is nowhere near where it could be".

What could boost FDI? He listed three things:

- Greater certainty over government policy for key industries
- Reform of "the mechanisms for getting things done" including the planning system, which is "particularly complex for infrastructure, green energy, and new buildings for manufacturing" and "connectivity to the national grid"
- More "patient capital" that can "absorb and support risk-taking in the economy". He said UK caution was "a huge factor slowing us down".

Why the UK should not read too much into the demand-driven bounce in the US

Mann acknowledged that US labour productivity numbers "look very attractive" but she warned that "we have to be very careful [with an evaluation]".

She said the picture in the US was complicated by the fact that President Joe Biden's administration is running a 7% budget deficit "designed to enhance the supply side of the economy, particularly on green industry". Harking back to the discussion on migration, she said that "just as students are not workers yet, construction isn't factories yet on the supply side". In other words the US is witnessing fiscally-driven demand, which is not the kind of demand that translates into higher living standards.

Questions from the online audience

How important is the turmoil in the Red Sea in terms of the inflation outlook?

Mann said it presented “a risk of an upward bias to inflation” not least because of “the higher shipping and insurance costs associated with that turmoil”.

Nunn took a different view. He said that the supply chain crisis that followed Covid forced companies into a rethink, reducing reliance on faraway suppliers and choosing suppliers at home and nearby. This process “created significant inflationary pressure, a couple of percentage points a year”. By contrast, the turmoil in the Red Sea is less inflationary. He said “most companies are saying it’s nowhere near as significant as the pressure on shipping during Covid”.

In what ways do you see the economic performance of the UK affecting the outcome of the general election?

Willetts, a Conservative peer, said Rishi Sunak, would like the economy to be a key feature of the electoral battle. The prime minister’s challenge is that the political agenda is constantly being diverted away from economic issues to what Willetts called “highly sensitive culture war issues”.

If the prime minister can focus on the economy, Willetts said he favoured actions designed to boost work: a cut in national insurance and “further structural measures that incentivise people to get into work”. He said Jeremy Hunt, the chancellor of the exchequer, might have found about £20 billion of fiscal “headroom” for the March 6 budget.

What will be the effect of generative AI on productivity?

Willetts said it could boost public sector productivity. Giving a couple of examples, he said generative AI might be able to free up time for police officers who currently manually redact documents sent to court and GPs who at present have to write routine referral letters to hospitals

Mann agreed that generative AI has “great potential but probably not for 2024”. She said that in the late 1990s she wrote a book on “how electronic commerce was going to revolutionise the delivery of government services”.

In the end there was no such revolution because “you have to have an awful lot of other things change within the system”. She added: “You can’t just drop technology in and expect it to transform the way businesses operate, the way government offices operate, the way people operate. There are many other factors that have to adjust.”

Nunn said generative AI would be “a fundamental part of the future” and that Lloyds Banking Group is “doing some scale pilots”. He urged companies and policymakers: “Don’t forget the rest of AI”. He said the banking sector “has been a leading sector using AI for over a decade”, and AI now “protects all our fraud systems. It’s had a massive impact on some of our core processes”.

Nunn agreed with Mann that deployment would take time. He talked about “the deployment curve” and observed that “this is going to take more than some of the hype is talking about today”.

He added that the effect of generative AI on productivity might even lag the deployment curve of the technology.