The UK economy seems to have exceeded expectations in the first quarter. Although GDP was flat in February, business and job surveys suggest March saw material improvements. Sure, headwinds do exist—stubborn core inflation, slowing wage growth, and tighter credit conditions globally. But this is the most optimistic the economic outlook has been in recent months. Does that mean we can wave goodbye to recession fears? Not quite yet. But don’t be surprised if we don’t end up seeing it this year.

Feb flatline. GDP was unchanged in February after starting the year with a solid 0.4% m/m growth. The reason? Industrial action in the public sector which depressed output in education, public administration, and defence – to the point that this masked gains made by the private sector of 0.2% m/m. Forward-looking surveys suggest that the private sector’s recovery continued in March, implying that a recession was most likely avoided in Q1. But it’s not all hunky dory. Credit conditions are tight, wage growth is slowing while inflation

remains in double digits, and the repayment burden for households have increased. Firms still must grapple with high borrowing costs and less generous government support. So, on balance, times remain tough.

Not just a blip. When business confidence bounced in February many thought it was too good to be true, but March's regional PMI data confirm that confidence has returned. Every region of the UK scored a reading of 50 or more, indicating that businesses are expanding, in contrast to January when all but one region was in contractionary territory. London, Northern Ireland, and Scotland lead the pack reporting greater inflows of new business and a firmer export environment. But it looks like a softening of pricing pressures is starting to ease the squeeze on business margins, bringing with it brighter expectations for the rest of the year. Encouragingly, that means firms are still keen to attract and retain workers, indicating that the labour market may yet continue to outperform through the first half of the year.

Upturn. Indeed, job surveys report that hiring conditions improved in March. According to the KPMG and REC Report on Jobs, the permanent staff placements index fell at its slowest pace since its decline began last October. But there is a clear shift from permanent to temporary staff, as economic uncertainty and tighter budgets are making firms cautious. The temporary billings index expanded more sharply last month, compared to February. But things are also looking upbeat on the supply side, as the overall supply of candidates increased for the first time since February 2021.

Bumpy Road Ahead. But BoE Chief Economist Huw Pill appears less cheery about the labour market outlook, going by his thinking about the future inflation path. He expects inflation to fall over Q2 as we pass the anniversary of last year's energy price hike, but the elevated core inflation rate remains a concern. He was arguably slightly less hawkish compared to last week's message of needing to 'get the job done.' That was due to emerging

signs of weakness in some areas of the labour market – the number of vacancies, job-churn and pay growth have all declined recently. On economic growth, the outlook, though improved, is still uncertain.

Unsurprising. The Bank of England’s recent credit conditions survey has shown largely expected results in the current climate. Within households, demand for all types of lending decreased in Q1, with credit cards down by c.10%, but is expected to rise in the following months. Borrowing defaults have increased across the board and lenders have decreased the interest-free periods on balance transfers and purchases potentially further squeezing households. On the brighter side, , large corporates is the only group of customers to not have experienced increased default levels.

A Rocky Road. After catastrophic hits from the pandemic and the Russia’s invasion of Ukraine, the global economy is on track for a gradual recovery, according to the IMF’s latest economic outlook. What’s helping? A growth rebound sparked by China’s reopening, an easing of supply chain disruptions and receding dislocatiosn to energy and food markets caused by the pandemic. That said, the IMF remained cautious in its outlook, citing inflation’s (so far) slow retreat and the significant, and synchronised, monetary tightening over the course of last year.

Watching. Indeed, the IMF thinks financial stability risks have increased since October, according to its latest Financial Stability Report, citing recent global banking turmoil. The key question: are those events a harbinger of more systemic stress, or just a flash in the pan prompted by tighter monetary and financial conditions? The answer is it’s tricky. Yes, the financial system is more resilient since the financial crisis. But there are concerns about hidden vulnerabilities, and Investors appear to be looking for stress points and fragilities that may have been underestimated or missed. Recent events are a reminder that funding can disappear rapidly, creating ripple effects through the financial system via loss of

confidence.

Mixed Messages. Getting inflation down is most central banks’ number one priority. The annual rate of US CPI eased from 6.0% in Feb to 5.0% last month — the lowest rate in almost two years. Good news surely? Not quite. Given that the core CPI measure, which excludes the more volatile consumer items of food and energy, ticked up to 5.5% y/y means the Federal Reserve will remain concerned. According to the latest FOMC minutes, several policymakers considered a pause in interest rate hikes in March given stress in the US banking system. While markets anticipate a further interest rate hike in May, that could represent the peak.

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