We are close to a turning point in monetary policy, but the full weight of rate rises to date have yet to be felt. And it might get worse for households in the near future. Firms have started cutting bonuses. And mortgage payments are going to shoot up. Any good news? The Bank of England is expecting the headline rate of inflation to show the first large drop this week, meaning prices would still be on the up, just not as rapidly as they have over the past year. Locally, another election is over. Back to porridge for the politicians. But back to Stormont?

Unwavering. This is how Andrew Bailey, the governor of the BoE, described its commitment to the 2% inflation target. But bringing it back to that level might not be easy. The spike in inflation was caused by external factors: sharp rise in the prices of globally traded goods, gas, and food. The rise in external prices has reduced our real national income and monetary policy can’t make it go away. But BoE has to take action to ensure that inflationary impulses do not cause persistent ‘second-round’ effects on domestic wage

and price setting. That is why the Bank have increased Bank Rate by nearly 4½ percentage points from December 2021, from 0.1% then to 4.5% now.

More to come. The BoE’s most recent rate hike of 25 bps marked the 12th successive rise. And, though the end of the tightening cycle appears in sight, the pain of higher mortgage repayments is far from over. The prevalence of fixed-rate deals means that two-thirds of the pain is still to come. Annual mortgage bills will shoot up by £2,300 on average for the 1.6 million households with expiring fixed-rate deals in the coming year. Further, younger and low-to-middle income mortgagors will face the biggest squeeze from higher interest rates.

Normalize it. Signs of slack are emerging in the labour market, but this is more a move towards normalisation than the start of fundamental weakening. The unemployment and redundancies rates are at historic lows, employment is still rising, and firms are still hiring. Though their cautiousness around high borrowing costs is leading them to cut costs in other areas – either by hiring more short-term staff than full-time/permanent positions or by cutting bonus payments by 3.7% in March. But even then, the demand-side picture is generally upbeat. What’s changing more materially is the supply-side story. Immigration flows and the reversal of the increase in early retirement seen during Covid is fuelling expansion of the workforce.

Turning point? The local labour market’s immunity to negativity could be starting to wane. The number of employees on Northern Ireland’s payrolls fell by almost 5,000 in April, more than offsetting March’s big rise. April’s decline represents the largest monthly fall since the initial reaction to Covid-19 in April 2020 (-11,210 jobs). Despite this decrease, the total number on payrolls are still over 32,300 above pre-pandemic levels. But with self-employment down by a similar amount, overall employment is just back to Q4 2019 levels. It is a similar story with the unemployment rate which, at 2.5%, is just a tad above its pre-pandemic rate. Redundancies are few and far between but Seagate’s recent announcement

of over 100 job losses highlights that this could be about to change.

Is The Tempest Over? UK businesses are mostly upbeat about June 2023, but clouds remain as the latest ONS survey shows. More than one in five (21%) businesses are expecting turnover to increase in June 2023, and 17% reported their overall performance increased in April 2023 compared with last year. However, the storm has not yet fully passed. Price pressure from goods and services bought remains, with 35% of businesses reporting an increase in April 2023. The highest proportion is in accommodation and food service activities sector where 68% saw an increase in prices bought in April 2023 compared to the previous month. Businesses have typically chosen to absorb costs (42%) or pass on the price increases to customers (27%).

Everything’s looking up? Consumers are feeling more optimistic, too. The headline UK confidence index rose to -27 in May from -30 in April – the highest since Russia’s invasion of Ukraine and the fourth straight month of rises. However, it is still well below the long-run average of -10, and consumer spending remains depressed in Q1 – still 2% below the level at the end of 2019. Expectations for the general economy over the next 12 months rose by 4 ppts despite 91% of the public remaining concerned about the cost-of-living, and 73% concerned about the economy. It remains to be seen whether confidence levels can keep climbing.

Going nowhere fast. Still absolutely no sign that the UK economy is able to generate the productivity growth needed to improve living standards. In Q1 output per hour worked was 0.6% less than a year before; the worst performance in a decade (excluding the pandemic). Perhaps that’s understandable amidst the cost-of-living squeeze. But zoom out and things only look worse. We produce a meagre 1% more each hour worked now than was the case five full years ago. Over 15 long years since the financial crisis, productivity gains have averaged a miniscule 0.3% p.a. Progress has stalled.

Inadequate. Clearly, the UK desperately needs a productivity boost. Trouble is, we're not doing enough to generate one. Take infrastructure. Good infrastructure reduces costs and eases friction, so we do more, from trade to travel. It therefore boosts growth and improves wellbeing. Yet in 2021 private sector infrastructure investment fell 2.8% to just £12bn. That's below replacement rate, so the capital stock fell to £337bn. Better news on the government side, where infrastructure investment rose by 15.2% to £23.8bn. But the share of government investment allocated to infrastructure is below the recent peaks of 2014-2017. Hopes of a productivity miracle without adequate investment are fantasy.

Draggin's Den. Start with persistently weak growth, add a high debt burden, mix in public spending cuts that have reached their limit and an ageing society with growing health and pension costs, what do you get? A higher tax burden. To that end, the UK government's current freeze on tax thresholds, which is set to last until 2028, is a powerful tool. Even more so with wages rising so quickly. As the Institute for Fiscal Studies has pointed out, 11% of adults were paying the higher rate of 40% in the last financial year. That's set to reach 14% by 2027-28, having only been 3.5% in 1991-92, meaning more than one-in-eight nursers can expect to be higher-rate taxpayers in five years' time. And more trade-offs await unless we grow the pie.

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