The UK is doing much better than you think and should avoid recession

L
et me confront those – not least of all people, the Governor of the Bank of England – who have written of the near certainty the UK falls into stagflation.

Indeed, such are the numbers of those predicting the UK's GDP numbers will tumble and bury the economy with them, one imagines they have clubbed together to pay for a pauper's headstone inscribed with the simple words *RIP UK economy*. Indeed, will try to calm such fears over *Recession, Interest rates and Prices* by invoking various reasons why the UK will actually rip.

Recessions do not 'just happen'. In basic terms, a downturn is induced when one of three key markets fails – namely labour, property or banks. And be in no doubt all three of these crucial elements of the UK economy are fundamentally sound. With over 1.3m vacancies, the labour market's problem is one to be envied. The UK's hiring backlog will progressively ease, not least as those who left the UK when COVID struck return, drawn back by higher wages (year-on-year growth of *c*10% this time in 2023). As for the sharp rise in energy and food costs, be in no doubt, their surge will result in a surge in new supply as nation after nation capitalises on selling price being so much higher than marginal cost of production to trigger a "Potato Cycle" supply surge. Now, rather than view rising wages as a threat, we should see them as delivering real wage growth; further supporting the UK's residential market, which, as of today, has never recorded a higher aggregate value (c£7trillion) and lower ratio of mortgage debt to value; over 8 out of 10 mortgages paying fixed rates, and all issued since 2008 stress-tested up to a 4% base rate. What of the banks? Well, they came into COVID in as macro prudentially good shape as they have ever been.

There is of course the rejoinder here could be that a recession can be induced by nothing more than the mere perception one is coming (The Keynesian Paradox of Thrift). Well, with the UK facing supply-channel shortages, any dampening of demand could actually be a good thing. A good thing as this would ease upward price pressures and so moderate the interest rate up-cycle.

Let me turn to concerns that lockdowns in China have made global supply shortage matters that much worse, not least in the UK, and so will bring about stagflation. The reality is that it is in Beijing's economic self-interest to get things restarted as quickly as possible. Be in no doubt then the huge commercial armada idling outside of China's ports will not *Rust In Pacific* waters. As to why one can be so sure, the PBOC has actively been moving its currency sharply down against the dollar to temper its trade weighted surge. This has been a strategy it has employed ahead of each big export push – in short do not expect global supply paralysis to persist.

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Regarding my *Rate of Interest Projections,* I expect the UK base rate to be c2% by New Year and reach a peak of no more 3.5%. As for the effect on the UK economy of such tightening, I am confident it can comfortably cope and indeed beat growth expectations (remember the pounds weakness is a form of monetary loosening).

Less we ignore the facto lock-downs meant UK households had savings enforced upon them of at least c£240bn on top of a surge in our saving post ’08. We need remember too that through Covid £1tn in additional housing equity was delivered in aggregate, and, as mentioned before, the UK’s residential market has never recorded lower LTVs, nor a higher proportion of fixed rate mortgages.

In terms of our behavioural change Peak *Retail Internet Penetration* will come in ahead of the 20% it seemed to be settling at pre-pandemic. As it heads to c30%, this will moderate inflation and drive employment, thanks to the huge operational gearing of logistics networks and their labour intensity. Such competitive pricing from on-line will in turn moderate pricing from physical premises.

To conclude, one is always confronted by the *Recession Infection Predicament*, as national economies are so interconnected. This said whilst It was once the case that the US or EU sneezing saw the UK catch cold, so much has now changed in the UK’s relationships near and far. Changed has happened too in relation to the internal workings of the UK economy, to make that adage redundant. One can draw upon a wide range of structural ways the UK economy has unshackled itself from the vicissitudes of the economies of the US and EU. For one, so much more of UK economic activity derives from within it. Whatever awaits the US and EU, Chinese and Indian students, tourists, and firms will continue to come to the UK; paying generously when here. Now, if matters turn for the worse across the EU – made worse by the crisis in Ukraine – we can be all the more confident that the EU nationals – up to 750,000 of them – who had been at work in the UK but left as COVID struck, will return. As for the UK’s traded goods sectors, whatever awaits the EZ, the UK will see reshoring of production to make a positive economic difference. In short, expect recession yes, but not in the UK, but in large swathes of the EU and the US.

Savvas is chief economist of Toscafund Asset Management