UK economy begins 2026 on a softer note ahead of energy price storm

Don't rule out UK growth picking up through the first quarter, despite a weak January. But the energy price spike risks a longer period of stagnation through 2026, as inflation rises, the jobs market keeps cooling and real wages fall back. We think the bar for a Bank of England rate hike is high

For the BoE to hike rates, we think oil prices would need to be sustained at 120 USD/bbl

January was weak

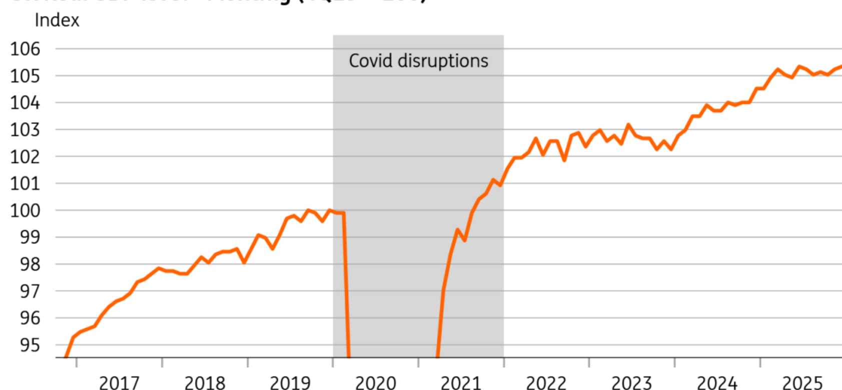
The UK economy had a lacklustre start to 2026, the latest monthly GDP figures reveal. January's output was unchanged relative to December, held back by a sharp drop in administrative/support services and hospitality.

These figures do have a habit of bouncing around, and realistically the economy is probably recording modest growth right now. Certainly, if you look at a three-month average of monthly GDP, the narrative looks a little better. Remember, too, that the UK growth figures have a suspicious habit of coming in stronger through 1Q than the rest of the year.

This is a trend that began in 2022, and we suspect is linked to the period of higher inflation and the tendency of price hikes to be geared towards the first half of the year, something which may not

be being fully adjusted for in the seasonal adjustment and/or deflation process. In other words, don't rule out a strong bounce back in February or March – this is exactly what happened last year after a similarly weak January.

UK monthly GDP over time



Source: Macrobond, ING

The bar for a BoE rate hike is high

Needless to say, all of this is a bit of a moot point given the rise in energy costs. The longer gas and oil prices stay at these levels, clearly the bigger the impact on growth. If the current level of prices persist, we're probably looking at a peak for headline inflation in late summer around 3.5%. That, at a time when private-sector wage growth is biased towards 3%. Real incomes are likely to fall.

This crisis also falls on a jobs market that is much, much cooler compared to when the Ukraine war began in February 2022. The vacancy rate is well below pre-Covid levels. Staff shortages aren't nearly as prevalent. Higher energy prices will likely add to the recent rise in unemployment.

For the Bank of England, that poses a dilemma. The 2022 playbook suggests it should tighten policy if the energy shock is enduring, in a bid to contain inflation expectations and the indirect fallout on services inflation. But with a weaker jobs market, that feedback mechanism is likely to be much more muted. This is something the Bank itself had begun to acknowledge at the recent February meeting, as it becomes clearer that last year's food inflation spike is unlikely to prompt a more widespread and longer-lasting period of price pressure.

We therefore think the bar for the Bank of England to hike rates is high. But the longer energy prices stay elevated, the longer the Bank is likely to stay on pause. The prospect of a March rate cut has all but evaporated.

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