



Economic Update September 2025

VISTAGE





Economic Update

Written by Roger Martin-Fagg, Behavioural Economist and Vistage Speaker

‘UK SME confidence remains optimistic but there are economic challenges ahead’

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Roger is an economist turned strategist. He began his career in the New Zealand Treasury, then moved into airline business planning and teaching postgraduates all aspects of economics. He designed and ran the postgraduate diploma in Airline Management for British Airways before joining Henley Management College in 1987, where for 21 years he taught senior managers macroeconomics and strategy.

Roger is an independent teaching consultant. He has been an external examiner to Bath University, worked with the Bank of England and three of the major UK clearing banks, and advised a major London recording studio for 15 years. Roger regularly talks to SME owners in the UK and Europe about economic trends, and is a visiting fellow to Ashridge, Warwick and Henley business schools.

Dear Vistage member, welcome to my update!

The purpose of the update is to act as a counterweight to the general economic commentary you get from the media. As many of you know I look at the economy through a behavioural lens. I focus on money and how it flows. As I explain in this update, this is missing in the mainstream models which are widely used by mainstream forecasters. Many of you have heard me say that these models and forecasts are precisely wrong. My approach is broadly right. It's your choice!

I am naturally optimistic (as most of you are!). As a consequence I tend to accentuate the upside and choose the data which supports my natural inclination.

If you are a pessimist there is a huge amount of analysis and commentary out there to support your mindset.

My optimism is always justified when I spend time with you. Vistage members are thinkers and doers simultaneously. Your adaptation to the reality of lockdown has been remarkable and I know many of you are producing financial results well above plan. As you are 60% of the economy my optimism is justified by your behaviour. Please continue to train, invest, innovate and lead. My forecasts will then prove correct!

Roger Martin-Fagg



I usually try and avoid politics. But economic performance and politics are inextricably linked. This update will begin with the economic outcomes of populist governments regardless of right or left.

In the 2023 American Economic Review economists at the Kiel Institute analysed how economies are impacted by populists in power. They found that after 15 years of populist leadership, real per capita GDP declines by more than 10% compared with a reasonable, non-populist government regardless of country or right or left. For example, Argentina, Turkey, Nicaragua.

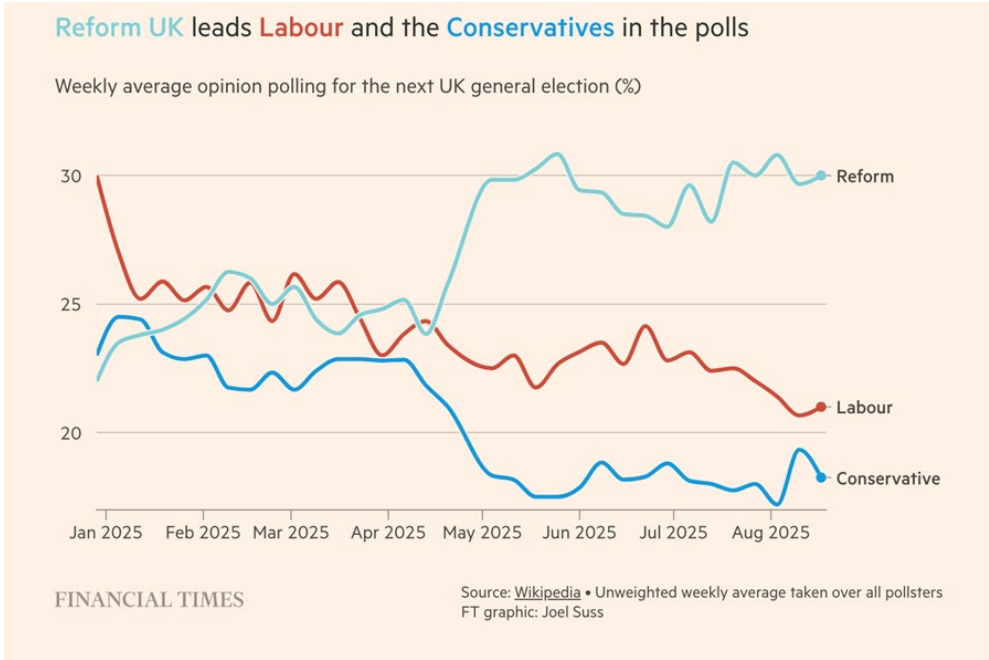
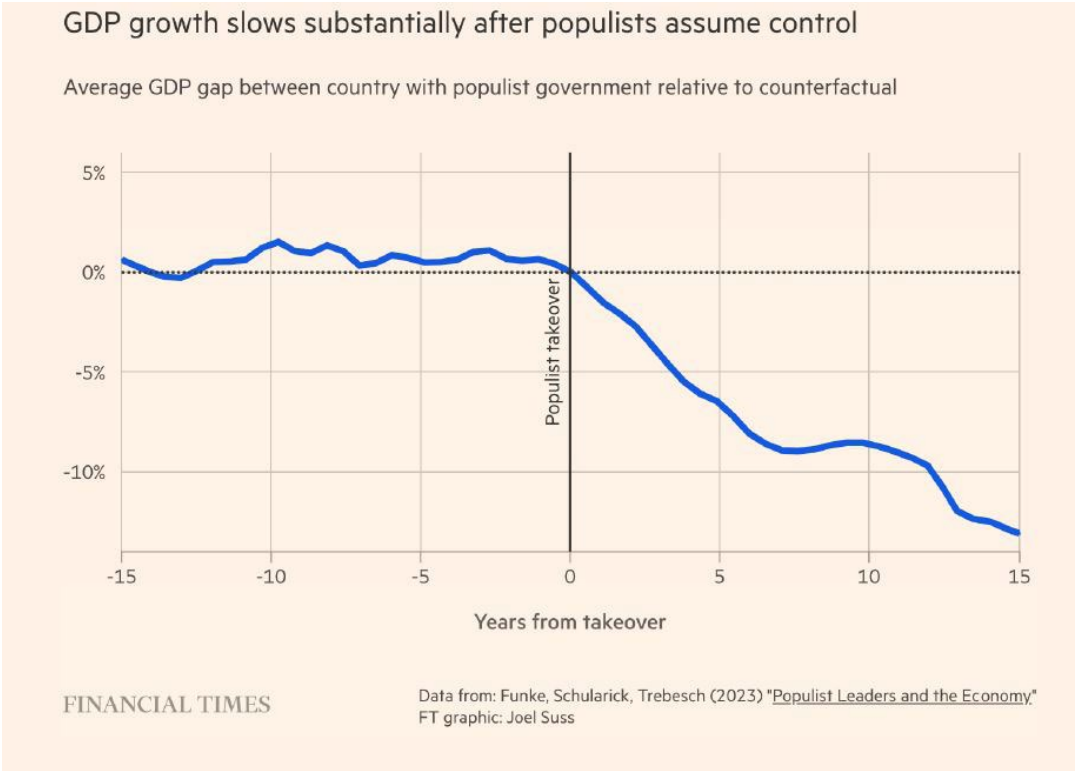
The reasons for the GDP decline are unsustainable fiscal debt, trade protectionism, and the erosion of judicial independence. However, the voter appears to accept these economic costs because populist governments on average last eight years compared to non-populist which last four.

The research results in the following advice to avoid populism.

Firstly, don't cause austerity, secondly avoid financial crises, thirdly recognise that every region and locality requires different economic solutions. Centralised governments are bad at assessing a region's particular needs. Local government is much better at assessing. It's an open question as to their abilities to implement.

Finally, and most importantly, communication is the most underappreciated and underemployed tool among mainstream politicians. But central to the success of populists is strong messaging from a charismatic and persuasive individual.

Thus we have Trump, Javier Milei in Argentina, Bibi Netanyahu, Putin, and Giorgia Meloni in Italy. Other contenders are Boris and Farage.



Opinions vary but currently the UK government is particularly bad at communication. Both the PM and the Chancellor fail to inspire. The opinion polls show it.

A significant part of my job is communication so I will do my best to communicate what the data tells us. I will not be using AI.

The UK outlook

A visitor from Mars with an economic education would look at the data for the UK and conclude that a number of key indicators are moving in the right direction.

The number one driver of economic activity is the money supply. It is the blood supply of any economy. Currently growing at 4%. Consistent with real GDP growth of between 1.5 and 2%.

Investment spending is 18% of nominal GDP and exactly in line with the average since 1950.

The visitor from Mars would look at the income data.

The average gross income of a UK household is £55,200. After tax this drops to £39.2k. The average tax take is 29% of income.

If you are in the top 20% of households your average gross income is £120k. After paying 41% in tax it leaves 70.8k to spend.

The concern is that per capita income has not grown since 2019. It can be explained by the considerable influx of new workers from abroad with their dependents. Since 2019 1.2 million of them.

The other concern is that households are saving 12% of their after-tax income. This is twice the historic norm. The reason for this is a combination of fear and ageing. A glance across mainstream media suggests unremitting gloom: everyone will pay more tax, the country is overrun with migrants who are rapists, there will be riots everywhere and the Prime Minister is a liar. In fact, survey data suggests the average Brit will forego meals to ensure they can have lots of holidays and leisure. And the baby boomers are skiing flat out (Spending the Kids Inheritance).

The visitor would question the reliability of employment data, would wonder why the retail sales data is delayed, would question the Bank of England selling off gilts at a £15bn loss. And also query the nonsense that the major taxes will not be increased when the ageing population and increasing longevity plus the triple lock are causing considerable budgetary stress.

On the plus side they would applaud the planned infrastructure spend and the greater freedom given to the regions to decide what they would value most.

They would applaud the building of bridges with the EU and rearmament. But would caution that rearming whilst good for growth is always inflationary.

They would note that the market for government debt is pricing in higher inflation both in the UK and the USA. And suggest that short-term interest rates will not fall any further. They would comment that with national debt close to £2.9tn and an interest bill of £100bn a year anyone who says government can and should reduce taxation is in cloud cuckoo land. Nevertheless, they would encourage government to double down on tax evasion, civil service head count, and generally wasteful spending and expect around £5bn to be saved. The least number of civil servants was in 2016. Since then, Brexit, Covid and illegal immigration have boosted head count by 32%.

They would give full marks to the Chancellor for raising NIC to a level which will ensure social care is funded from income not debt. But they would recognise that the increase in cost of employing people will result in more rapid introduction of AI plus the death of some businesses.

Transitional unemployment will increase. And the service sector inflation rate has always been higher than the manufacturing sector which historically has increased productivity at a much faster rate. AI might change this. They would note that all the indices of inflation show an uptick, some at 3.6%, others at 4.2%. Average weekly earnings growing at 5.2% before tax show real incomes are being squeezed but on average still growing.

Asda's monthly income tracker revealed the first decline in disposable cash for middle-income families in two years. In July, those on gross annual earnings of about £41,000 experienced a 1.6% year-on-year decline in their income.

Lower-income families were the hardest hit, as spending power slumped by 11%, resulting in a shortfall of £73 each week, according to the research carried out for the supermarket by the Centre for Economics and Business Research.

However, chunky increases in disposable income for the better-off meant that average disposable income rose by 2.4% in July compared with a year before to £255. I guess they shop at Waitrose or Booths.

Retail sales volumes are more erratic than usual: April posted a 5% increase on a year earlier, May a 1.2% decrease and June a 1.8% increase. Month-on-month volumes indicate a headache for retailers.

Since 2023, real disposable incomes grew strongly until May 2025. The decline is because inflation increased.

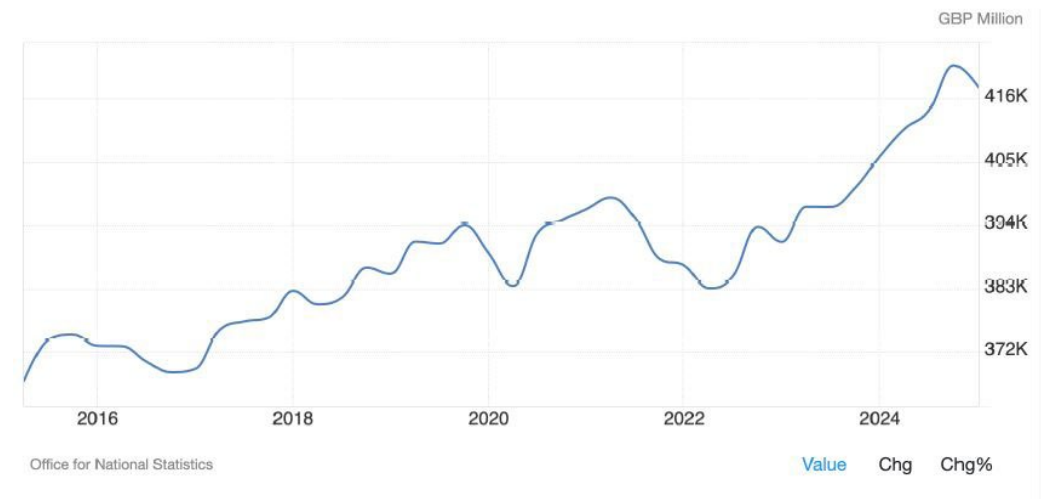
Paradoxically when inflation increases savings also increase. The logic is obvious: if saving for a deposit on a house and house prices are rising 5%, the purchasing power of the existing pot is falling by 5%.

Looking ahead, it's highly unlikely core inflation will fall. Global weather patterns are impacting harvests everywhere resulting in supply shortages and inevitable price increases. UK food inflation is likely to be 6% by the end of this year.

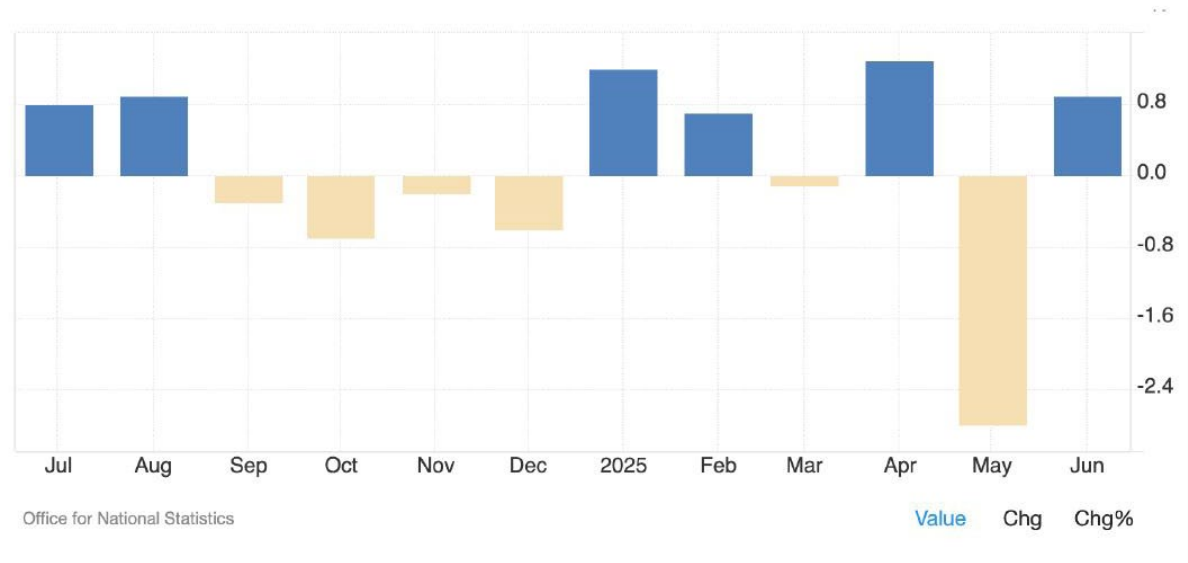
The chart shows UK and Scotland infrastructure spend as a % of GDP compared to the other 140 members of the OECD. The worst performer is the USA, then Germany, then the UK. In Germany the law to limit the Federal deficit to 60% of GDP in 2009 led to a significant drop in infrastructure spend.

It always makes sense to borrow to finance infrastructure. The economic and social gain will always exceed the rate of interest. The OECD econometrics show a GDP multiplier of 4. This means £1 spent generates £4 of new income over time. The IMF model has a multiplier of 3.

UK households real disposable income in billions



UK Retail Sales volumes month on month



Regular readers will know I believe the government's planned infrastructure spending will produce significant economic and social benefits. Here is why.

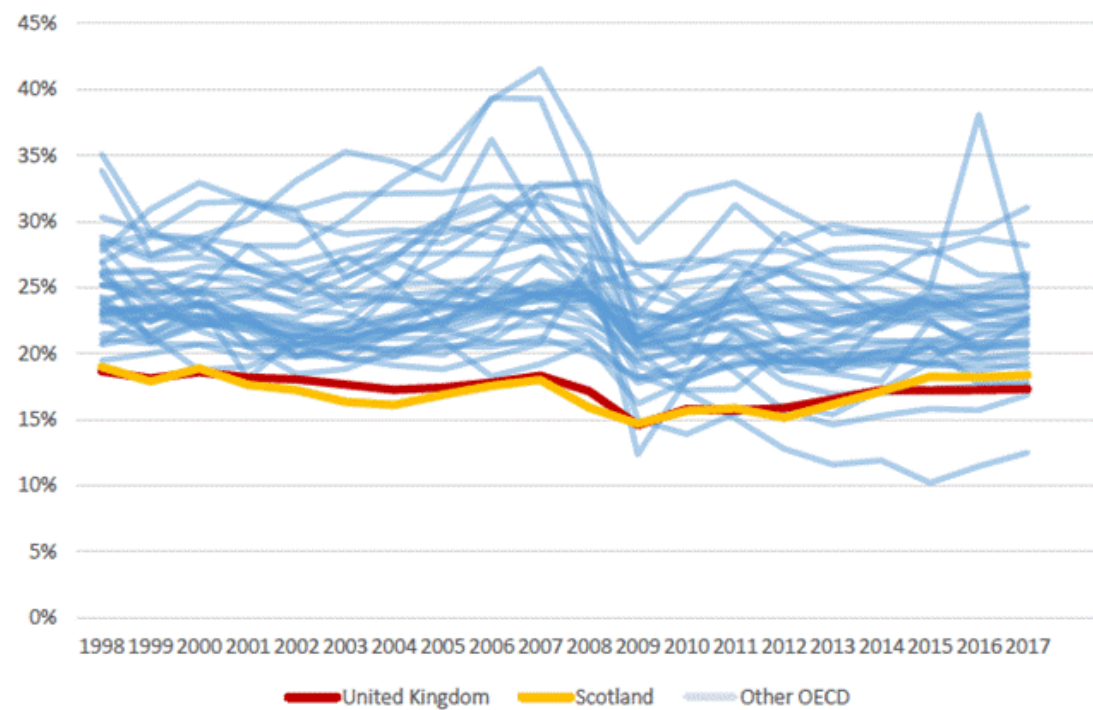
The ability for people to travel efficiently and quickly between cities is a key driver of the specialisation of labour, which in turn is key to productivity and income growth. One of the biggest drivers of economic growth in Asia was the Honda 50 moped which was launched in 1958. It allowed individuals to seek better paid work further afield than walking or cycling distance. We all know how much productive time is wasted stuck in traffic, or with delayed or cancelled public transport.

The analyses show smaller multipliers for high income countries. Indeed, the OBR thinks the UK multiplier is 1.5.

Their reasoning is that given the limited capacity of the UK, the spend quickly expands the economy to its capacity ceiling. At which point inflation takes off followed by significant interest rate increases dampening growth. Their model says this happens four years after the initial stimulus.

However, in the meantime our capacity to produce is increased due to productivity gains. Please note: none of this works if financed from current tax revenues, it has to be debt ie new money

Percentage of GDP spent on infrastructure for members of OECD



The Labour Market

The workforce stats are currently unreliable. However, the vacancy data is still ok. The increase in the cost of employing, the implementation of AI, and global economic uncertainty are combining to reduce the number of vacancies. Applicants with AI skills enjoy a 10% salary premium

The latest August Lloyds Bank survey of 20,000 SMEs shows that they are adapting quickly to the increase in their cost base. Hiring intentions have been increasing for the past four months. Business confidence in their trading prospects has hit the highest level since 2014. Retail confidence is at a five-month high. Manufacturing confidence is the highest for ten years. Construction confidence fell to a four-month low.

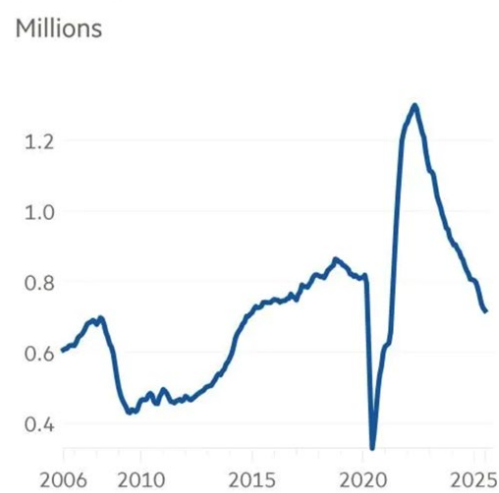
The housing market

Over the past few years many of the pundits have been consistently wrong. House prices have been barely affected by rising interest rates. In 2021 the bank rate was 0.1% rising to a peak of 5.25%. Over this period house prices were expected to fall. They rose 10%.

The reasons are clear. Over 80% of mortgages are fixed rate, more stringent regulation ensured people were better placed to deal with rising rates, there was a pool of savings to draw on after the pandemic, unemployment remained low, and wages grew strongly.

There have been regional differences. The North has seen prices increase between 6% and 14%, London and the SE decreases of 1%-2%.

Vacancies in the UK economy are declining



Source: Office for National Statistics

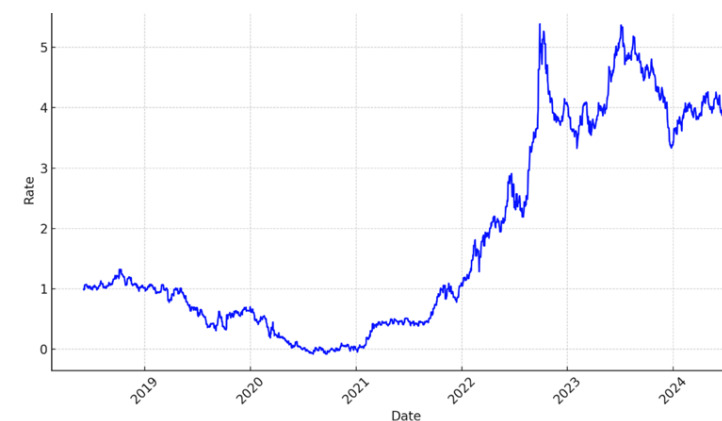
At this point we should note that the vast majority of economic journalists live in the SE. People in the SE tend to more highly leverage than elsewhere. The surge in demand for more rural larger houses has diminished. 20% of homes on the market were purchased during the pandemic. The return to the office mandates are clearly having an effect.

More people than ever own their house outright. Only 33% of households had a mortgage in 2023. More people are renting and 50% of 19-29 year olds live with their parents.

Over the next year the average rate paid on mortgages is set to rise as fixed rates are renewed.

Fixed rates are priced off the swap rate. The swap rate is always a bit below the bank rate.

5Y SONIA Swap Rate Card



The swap rate is the rate of interest banks pay for baskets of assets, usually mortgages, which they trade to manage their liquidity and risk.

As expected, the number of transactions has recovered after the rush and drop due to changes in the stamp duty threshold in April. July was 4% ahead of a year earlier at 95,580. And up 1% on June.

A cursory read of the media over August (known as the silly season) would suggest the UK is finished. There will be riots, significant tax increases, and Reform is likely to win the next election.

Research shows that people over 45 still get their news and insights from mainstream press. The Daily Telegraph claims 750,000 readers. Many of my friends read it. I stopped seven years ago due to declining standards.

Media sources are telling their journalists not to repeat DT stories because they are increasingly unreliable and full of inaccuracies.

Guy Dampier lives in Germany, Douglas Carswell in Mississippi, Isabel Oakeshott in UAE. All three have claimed insight into how middle England thinks and behaves and write about it. All have promoted the end of the UK and riots.

I receive a growing number of emails from individuals seeking an opinion on this and other matters based on something they have read. 80% is misinformation.

We live in an era of increasing amounts of (mis) information and less knowledge.

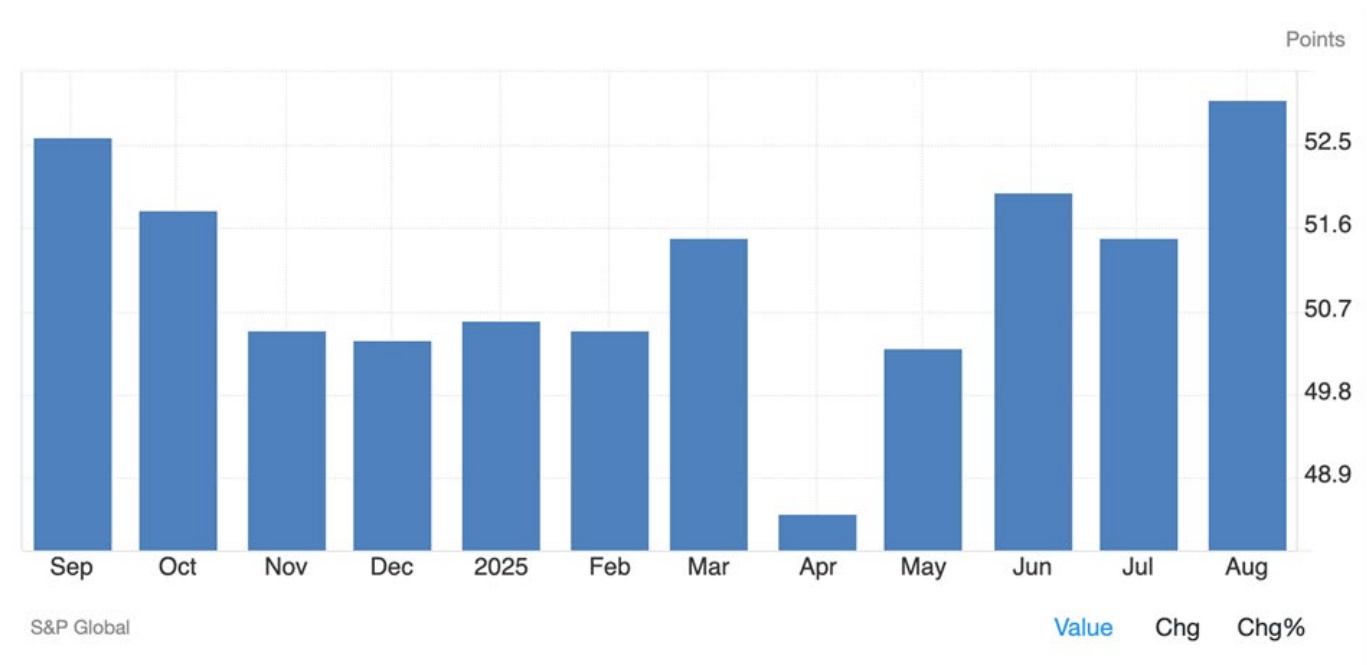
If the Treasury were ever to ask my advice, it would be this.

Immediately raise VAT by 10%. No parliamentary debate is required; all the Chancellor has to do is announce the date. Food and books are both zero rated. One only pays a great deal of VAT by buying expensive stuff or lots of less expensive stuff. So those with loads of money and who spend it pay more tax. It's a tax which can be minimised by reducing consumption. Of course the fiddles will continue, the demand for cash will increase. But everyone contributes to the Exchequer according to the amount they spend. Yes, the inflation rate will go up, but that would be a one-off increase. It would raise £20bn. And it would save all the time-consuming tinkering with wealth taxes.

It will NOT reduce growth. Denmark grew 3.7% last year, they pay 25% VAT with no lower rates.

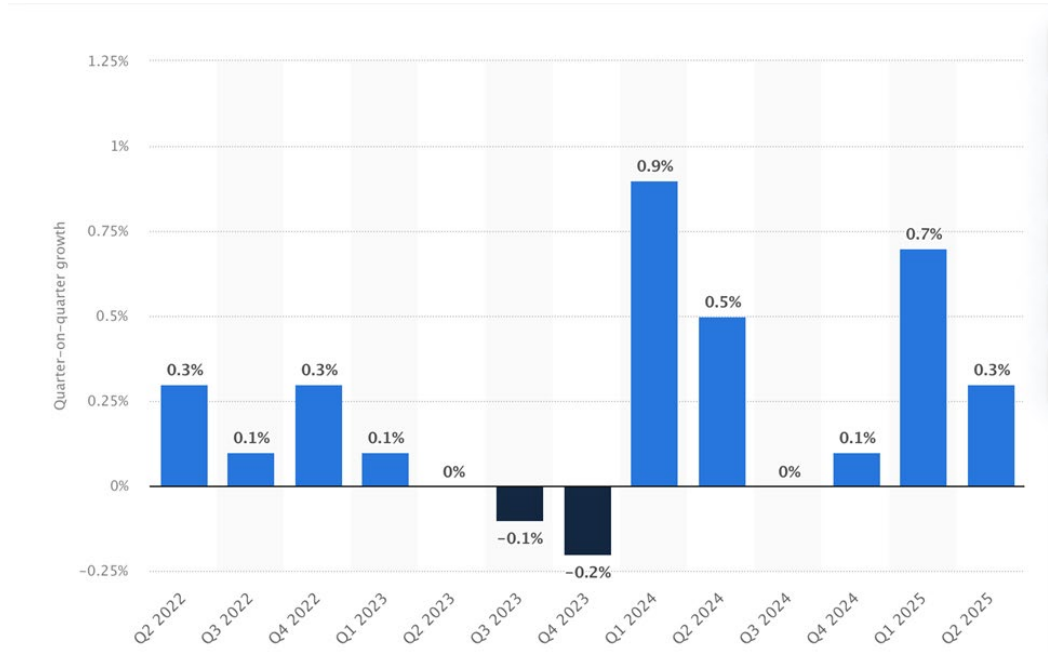
The Composite PMI and the data from the Lloyds Bank survey plus the data I have shared with you does not indicate an economy failing to grow. Despite the media mindset. Good news doesn't get clicks or sell papers. It's time for big business to stop whinging and get on with using AI to drive productivity.

The PMI index at over 52 is consistent with stable growth.



To conclude this section on the UK.

- The economy is growing. I expect full year growth to be 1.4% (the EU 1%)
- Inflation will remain above 3% but below 4%
- The exchange rate will hover around \$1.35, Euro 1.20
- The labour market has loosened a little but good people are still scarce
- House prices will continue to grow as will the number of transactions
- Bank rate will not fall again
- The cost of fixed rate mortgages might increase by 0.25%



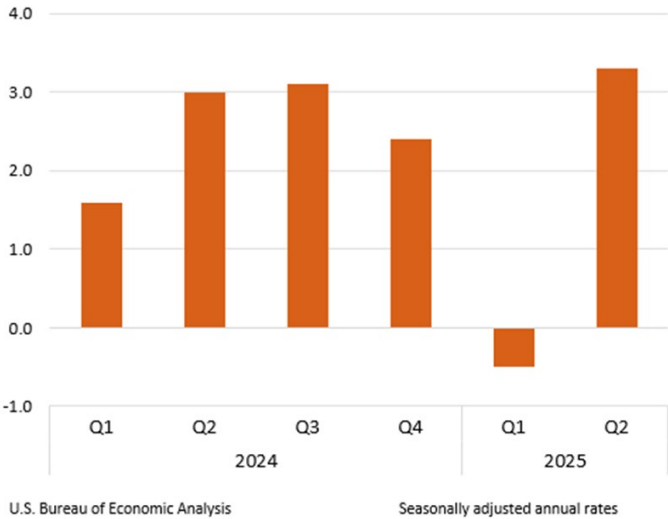
The United States

As the research has shown populism delivers lower growth. The cause of the GDP decline is unsustainable fiscal debt, trade protectionism, and the erosion of judicial independence. The USA currently is experiencing all three. So far it's impossible to ascertain a trend for GDP. Q1 and Q2 data points need explaining.

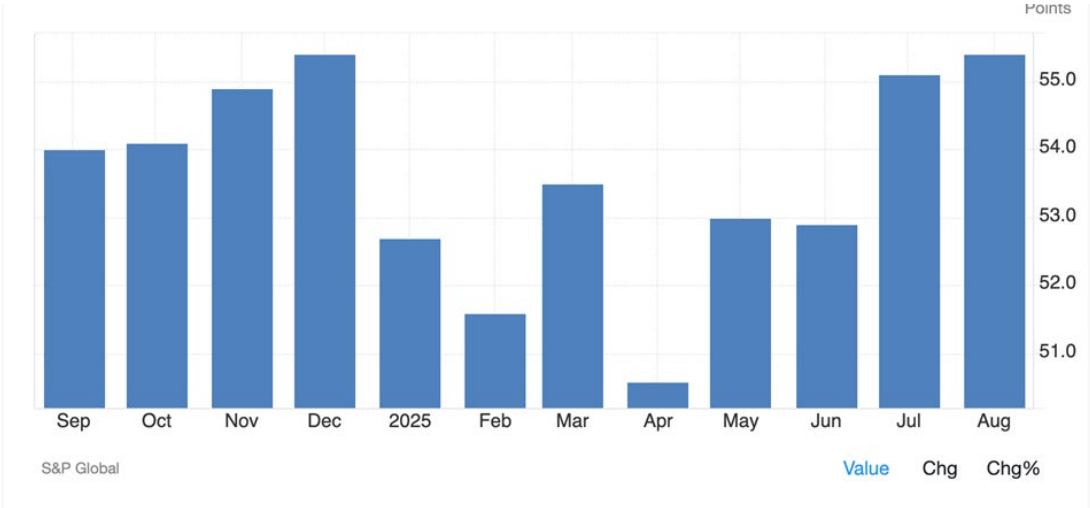
In the first quarter, real GDP decreased 0.5 percent. The increase in real GDP in the second quarter primarily reflected a decrease in imports, which are a subtraction in the calculation of GDP, and an increase in consumer spending. These movements were partly offset by decreases in investment and exports.

Unemployment has increased slightly due to government employee layoffs but it's still below 5% which is defined as full employment.

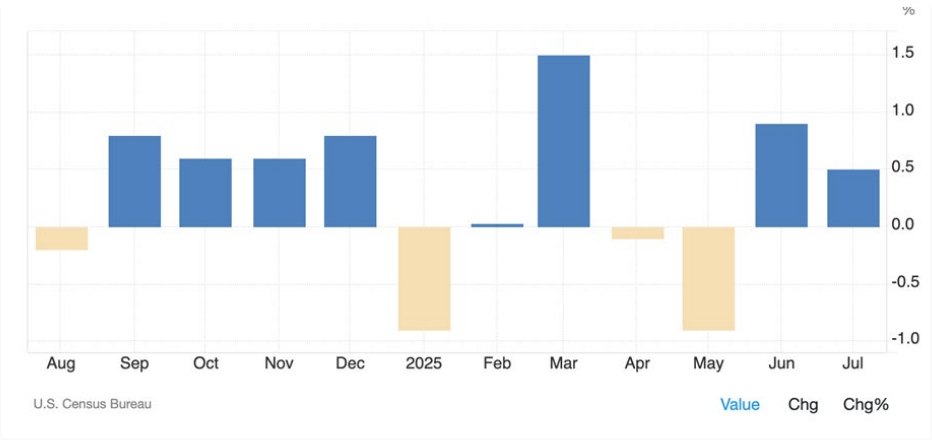
Real GDP, Percent Change from Preceding Quarter



The Composite PMI is looking good

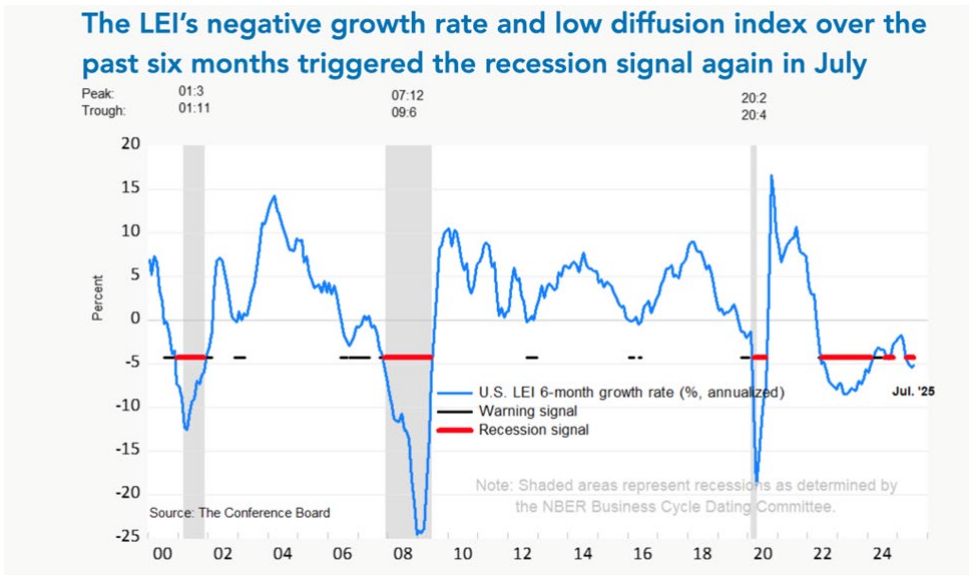


Retail sales month-on-month



So current data suggests stable GDP growth at around 2.8%

But the so called leading economic indicator (LEI) which looks ahead by a year is telling a different story. Please note that it indicated a recession in 2023 which never materialised.



So far then Trump can claim success. But it's early days. In my last update I focused on midwest farmers. And suggested that falling grain prices would trigger bankruptcies and the failure of the small local banks.

The soya bean price chart is replicated by oats, wheat and corn prices.



The chart shows prices are back at 2018 levels. But input prices ie fertiliser, machinery, labour are up 30%. Today the price of these commodities doesn't cover the cost of production. Midwest farmers incomes are currently falling as is their ability to meet debt obligations.

The chart is produced by the Midwest Federal Reserve dated August 29.

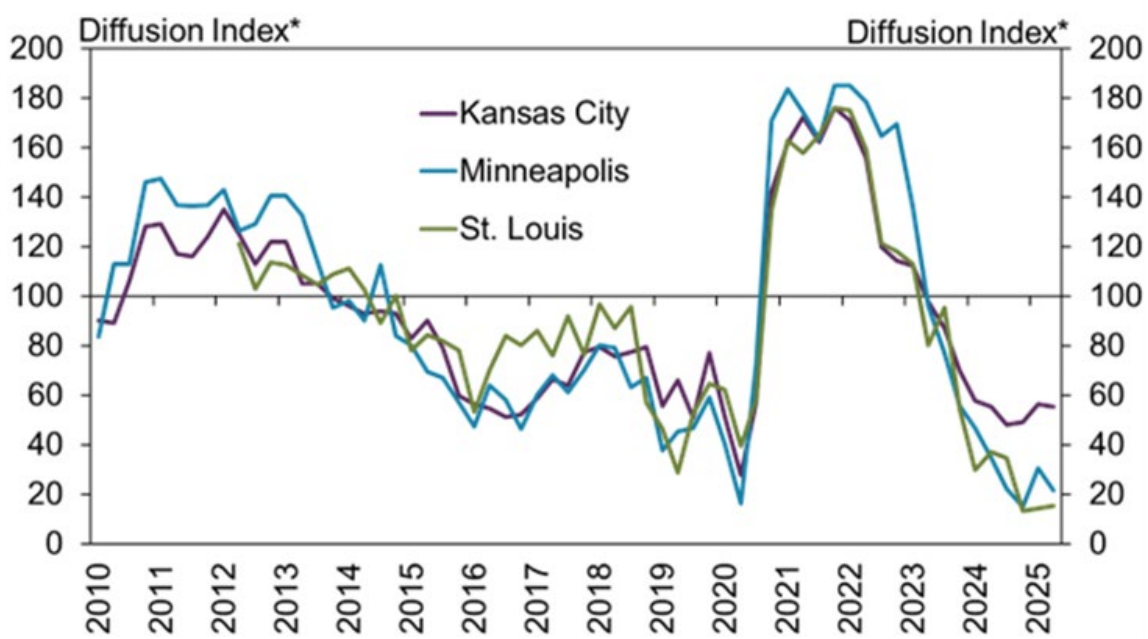
It supports my opinion. The next paragraph is a cut and paste from the internet.

"The US is currently experiencing a reduction in federal support for farmers, with actions taken by the Trump administration including imposing tariffs, ending climate and conservation programs, and dismantling programs that provided stable domestic markets through sales to schools and food banks. These policies are causing significant harm and instability for many family farmers across the country. 77% of them voted for Trump."

I am not optimistic that the USA will continue to grow at the current rate. Agriculture only provides 5.6% of USA GDP. But my concern is a financial crisis triggered by midwest bankruptcies along the lines of the savings and loan mess of the eighties and nineties.

We shall see.

Meanwhile international business has made significant promises to invest in the USA. This is to appease Trump. It will be interesting to see how much materialises.



Conclusion

The UK is suffering from an absence of effective leadership. If ministers do not know what the boss wants, they will work for the other boss, the electorate. But the electorate all want different things which makes government incoherent. There is a fundamental problem. The electorate always wants more but to have someone else pay for it.

The USA has a different problem. They have an autocratic boss who is inconsistent and will brook no challenge or indeed anything which suggests he might be mistaken. He is entirely transactional and has to win at any price. Such bosses are only fed good news when in fact the machine is failing. It's worth remembering that Trump tariffs on the world are 18%, the rest of the world has average tariffs of just 3% between themselves. The USA is only 15% of world trade. 85% of world trade remains largely free and frankly can manage well without US trade.

The core issue is the dominant role of USA as lender of last resort. If the Fed loses independence and non-bank US financial institutions continue to grow at their current pace there is a cocktail for a global financial crisis.

Long-term bond yields are now back at pre-pandemic levels despite the fact that government debt averages 92% of GDP globally. It was 65% in 2000. AI will affect 40% of the global workforce. Technological developments in crypto and stable coin will have important implications for the global monetary system.

Western rich country electorates have to understand that their governments cannot deliver pensions and healthcare without raising more revenue. Entitlement spending is growing at an increasing rate. Governments need to point out the reality and not fudge the issue. Either entitlements have to be reduced, or taxes have to increase. The populist argument that all government has to do is be more efficient to solve the problem is baloney.

It's a testament to the resilience of SME owners and their adaptability that the global economy has continued to grow despite all the uncertainties of the past six years. Depending on which source is used, they produce between 50 and 70% of global GDP. The global GDP is growing by 2.8%.

My opinion is that UK business will thrive despite our current leadership. After all, well run businesses have expanded under previous leaders who left a lot to be desired.

I have a question mark over the future success of the USA. It has significant momentum but even supertankers end up on the rocks. Only time will tell.

Finally, the UK in the first half of 2025 grew at 1.1%. This is top of the class for the G7 economies. It wasn't mentioned in the media.

Money supply and bank lending now normal at 4%pa
No interest rate change required



UK Household spending power growing at £8bn a month

