

Prospects for the UK economy

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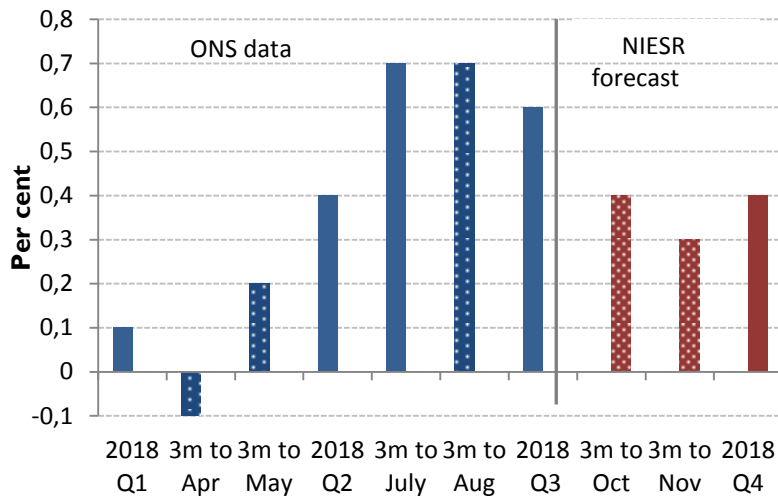
Plan

- Disconnect between *recent* economic performance and Brexit uncertainty
- Economic forecast update: hard + soft
- Thoughts on Budget 2018/fiscal policy
- Monetary policy outlook

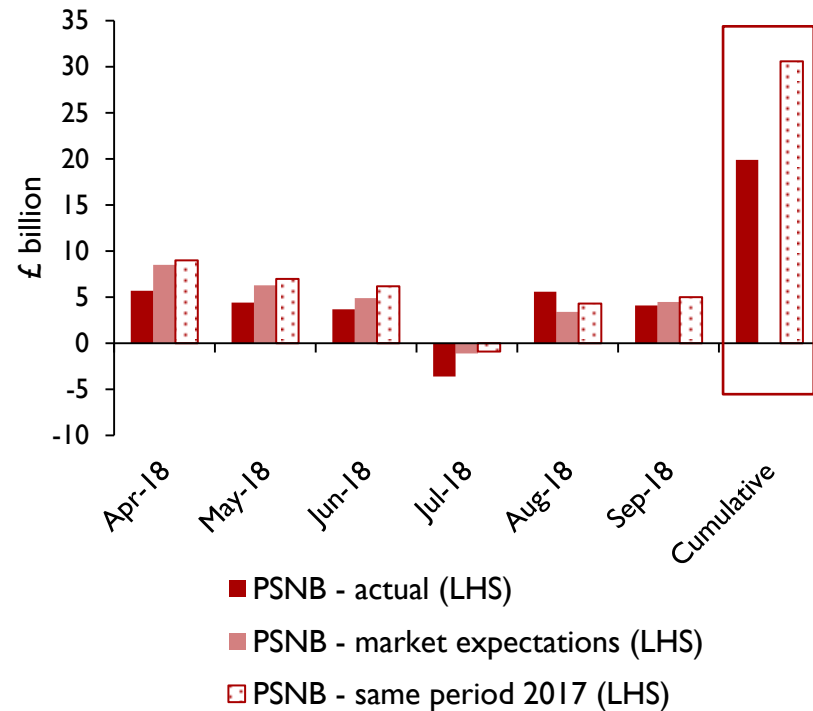


Disconnect: upside news

NIESR monthly GDP tracker

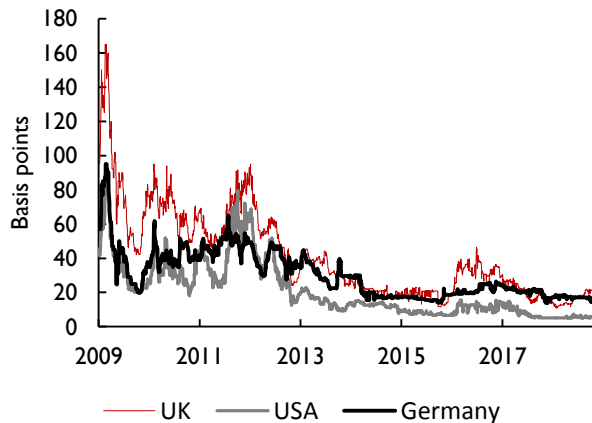


Surprises to public sector borrowing

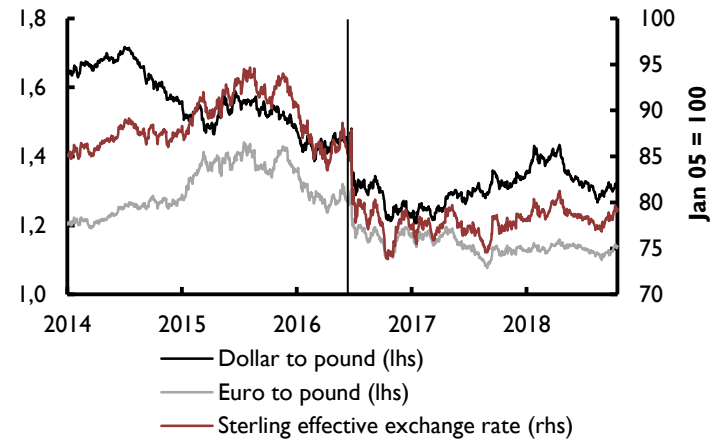


Disconnect: financial markets

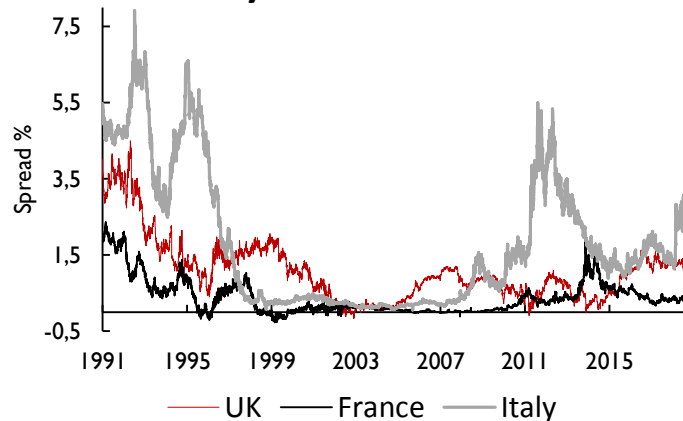
5 year CDS



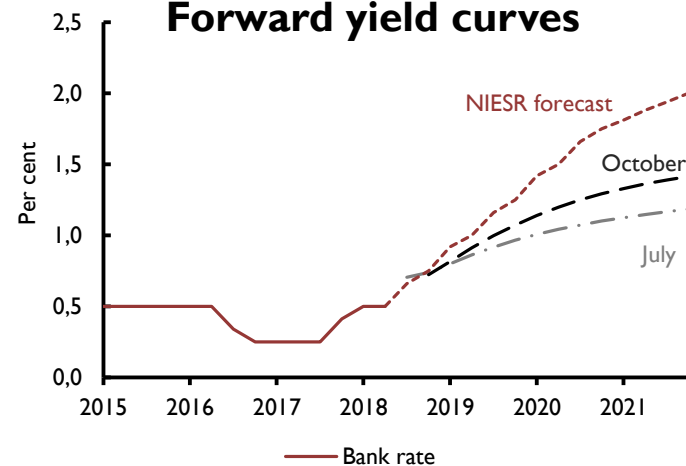
Sterling exchange rates



10 year Bund rate



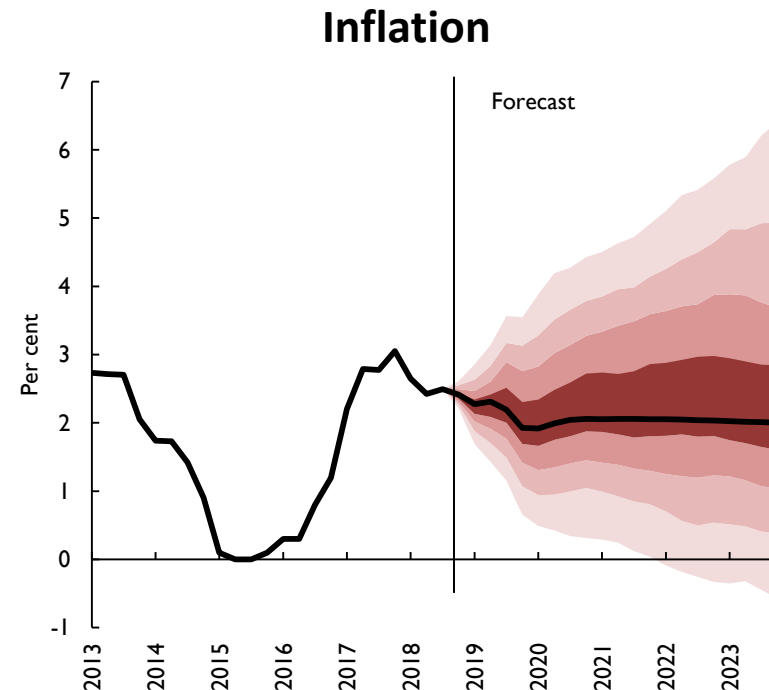
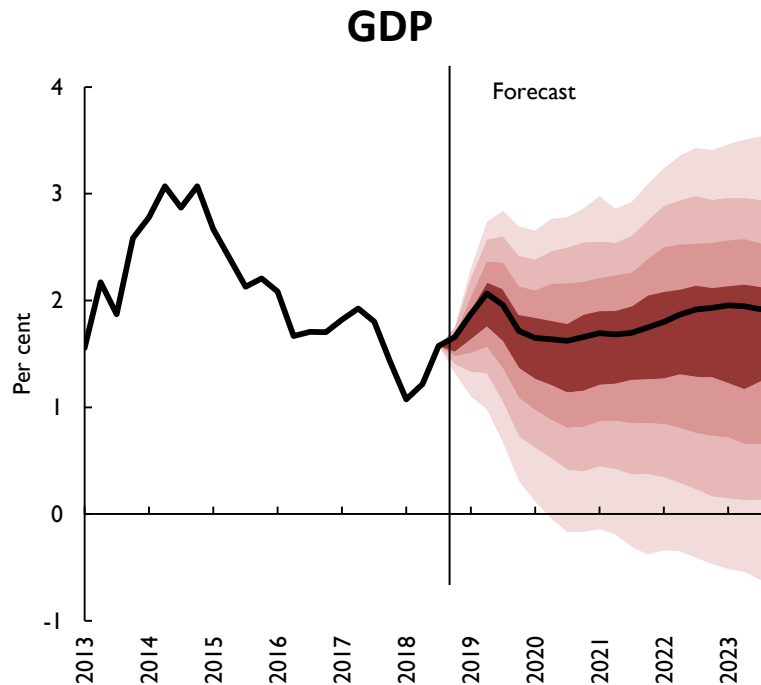
Forward yield curves



Forecast update

GDP growth at 1.4% this year and around 1.9% in 2019. Forecast based on a soft Brexit scenario. Risk to GDP tilted to the downside because of Brexit.

CPI inflation eases to the target level of 2 per cent by end-2019 under soft Brexit and the risks are skewed to the upside because of Brexit.

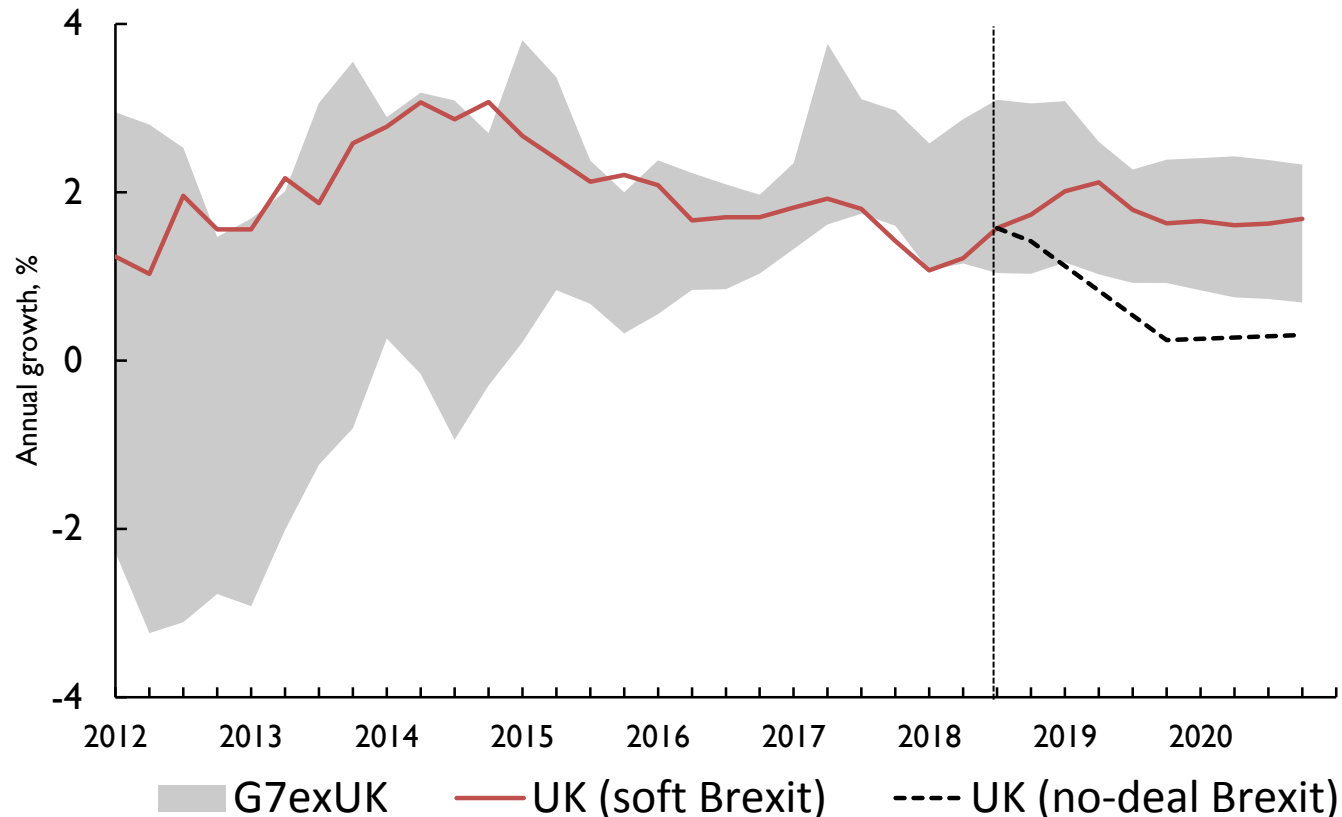


Source: NiGEM Stochastic simulation

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GDP growth: hard vs soft vs G7

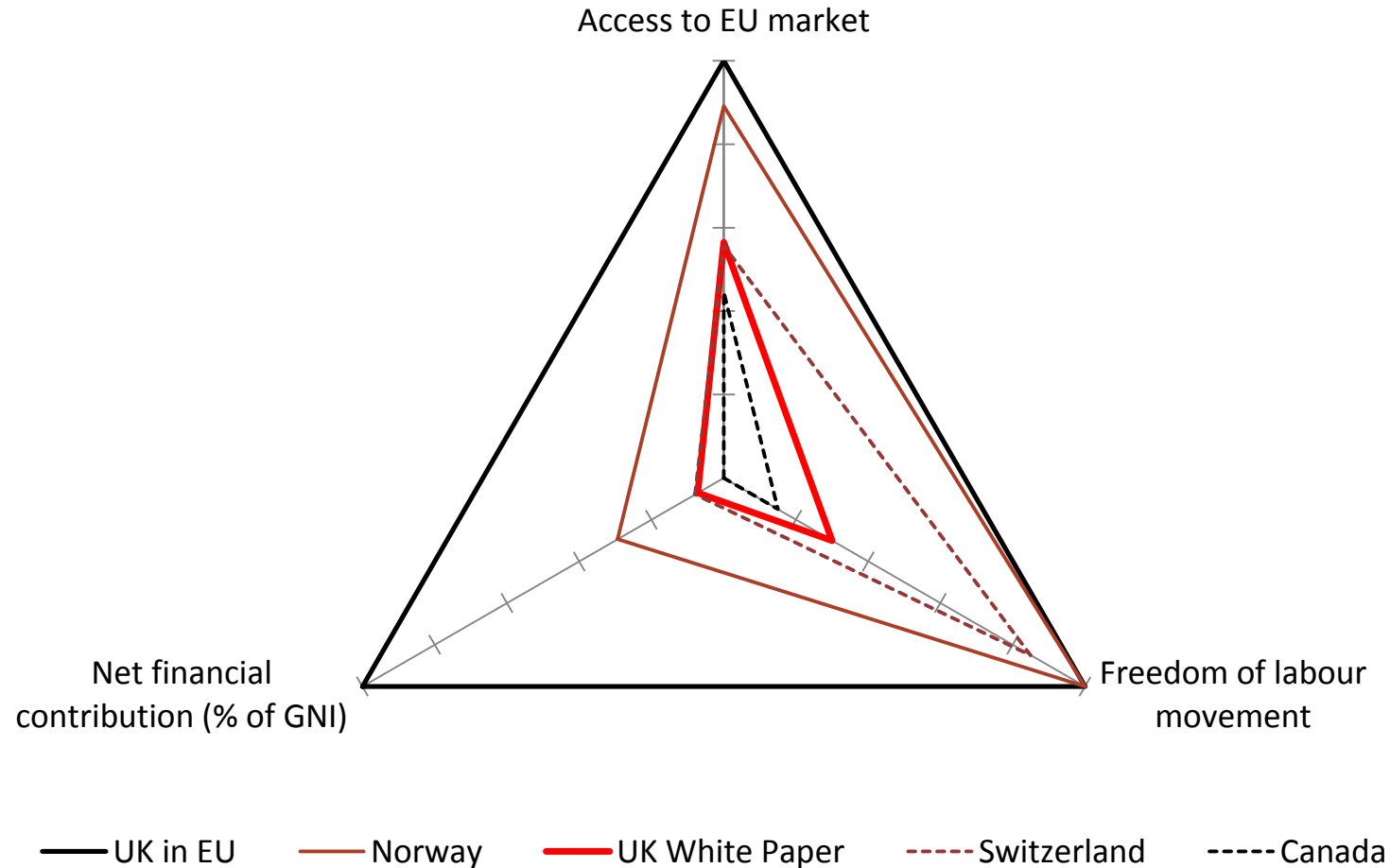
The UK will perform in line with other G7 economies under our soft Brexit scenario
The UK will be a notable underperformer under our *orderly* hard Brexit scenario



Source: NiGEM Stochastic simulation

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Brexit: engagement triangle



Source: NIESR, European Commission and World Bank.



GDP growth forecasts: OBR vs NIESR

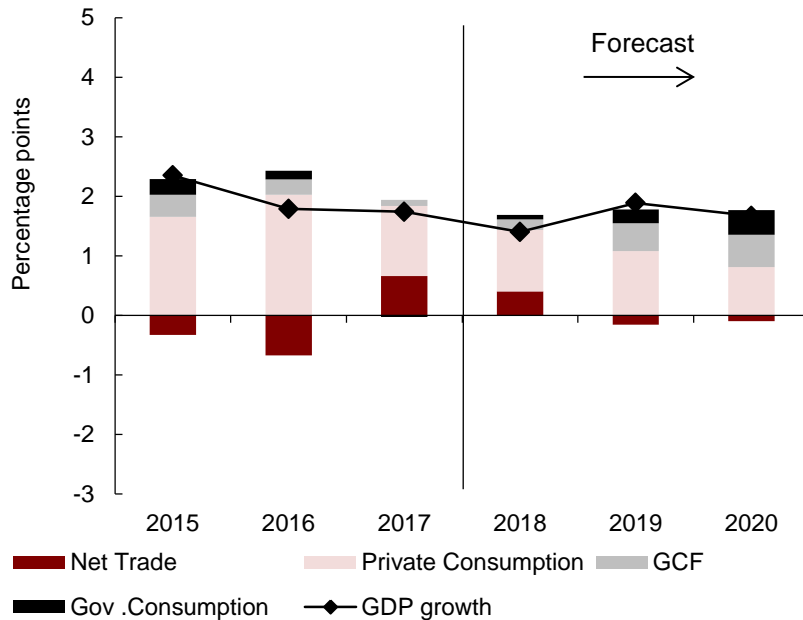
	OBR		NIESR	
	Spring	Budget	Baseline	WTO/No-deal
2019	1.3	1.6	1.9	0.3
2020	1.3	1.4	1.6	0.3
2021	1.4	1.4	1.7	1.4
2022	1.5	1.5	1.9	1.7
2023	1.6	1.6	1.9	1.7
Total Sum	7.1	7.5	9	5.4

Source: OBR, NIESR

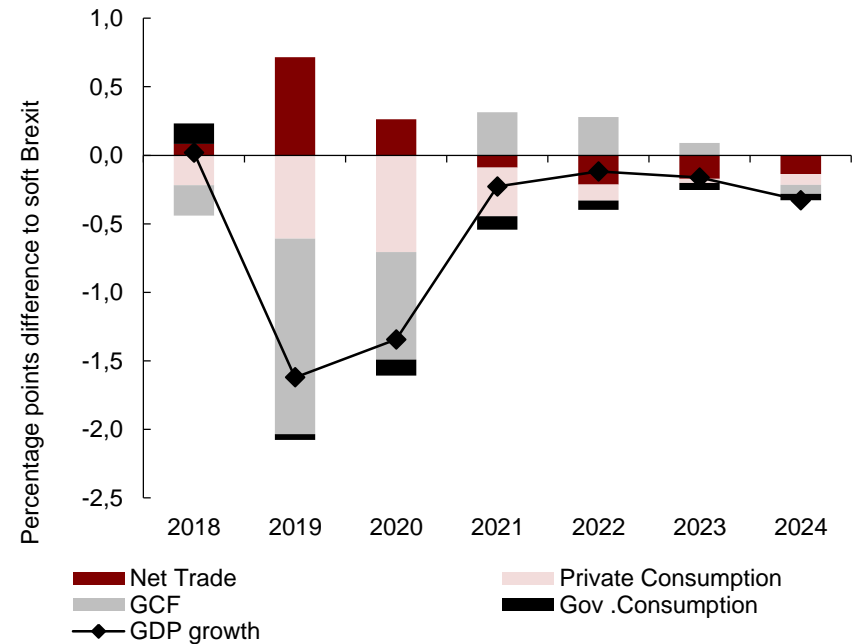


Contributions to GDP growth

Contributions to annual GDP growth



Differences in contributions under no deal



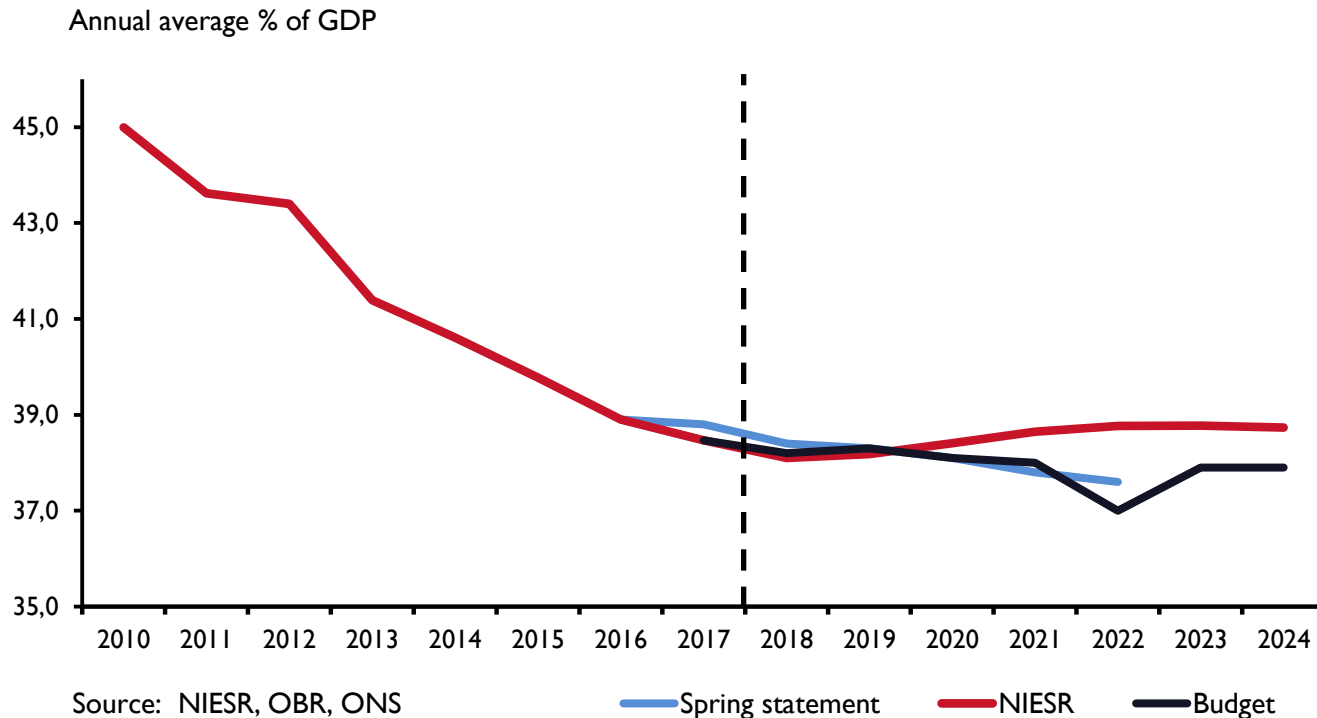
Source: NiGEM Stochastic simulation

Fiscal policy assumptions

- We have argued for sometime that ‘austerity fatigue’ has set in and that the government will have to increase the spending budget (Hantzsche and Young, May 2018 *Review*)
- In the Spring statement (**Budget 2018**) public spending as measured by the Total Managed Expenditure to GDP ratio fall by 1.2 (**0.6**) percentage points over the forecast horizon. We diverge from that and assume a flat TME/ GDP ratio



Total managed expenditure to GDP ratio



- What does that imply for the fiscal rules?



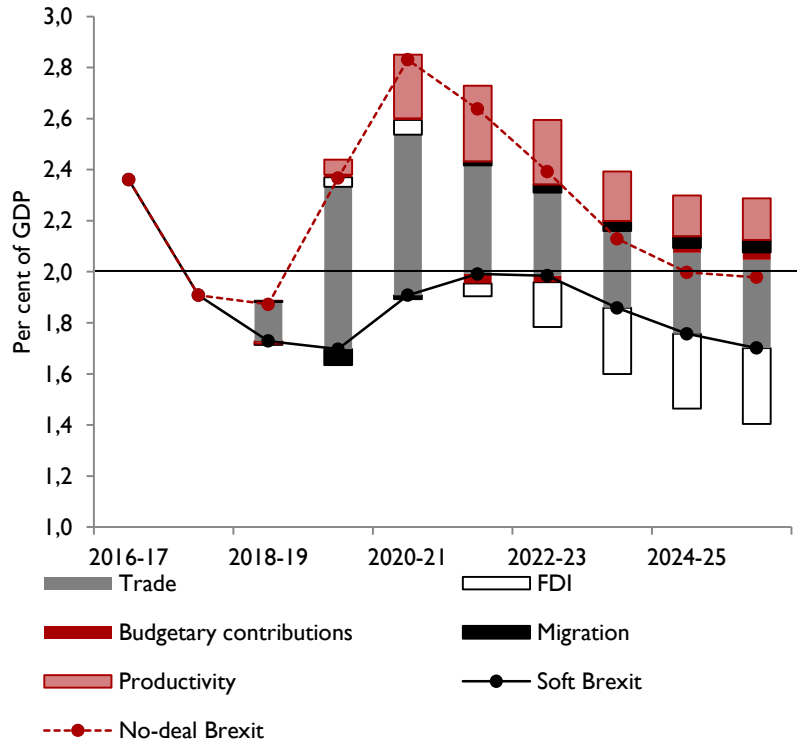
Fiscal targets and rules since the creation of the OBR

Year	Rule	Definition
2011	Fiscal mandate	Achieve cyclically-adjusted current balance by the end of forecast period (2015-16)
	Supplementary target	PSND as a % of GDP to be falling at a fixed date of 2015-16
2012	Fiscal mandate	Achieve cyclically-adjusted current balance at the end of the forecast period (2016-17)
	Supplementary target	PSND to fall as a % of GDP between 2014-15 and 2015-16
2013	Fiscal mandate	Achieve cyclically-adjusted current balance, five years ahead
	Supplementary target	Reduce PSND as a % of GDP in 2015-16
2014	Fiscal mandate	Achieve cyclically-adjusted current balance, five years ahead
	Supplementary target	Reduce PSND as a % of GDP in 2015-16
2015	Fiscal mandate	Borrow only to pay for investment- in the third year of the rolling five-year forecast period (2017-18)
	Supplementary target	Reduce PSND as a % of GDP in 2016-17
2016	Fiscal mandate	Achieve budget surplus in 2019-20 and beyond
	Supplementary target	PSND to fall as % of GDP each year
	Welfare cap	Spending below cash limits set in July 2015
2017	Fiscal mandate	Structural deficit below 2% of GDP in 2020-21
	Welfare cap	Spending below cash limit in 2021-22
	Supplementary target	Public sector net debt to fall as a percentage of GDP in 2020-21
	Fiscal objective	Achieve fiscal balance ASAP in next parliament (2022 or 2025?)

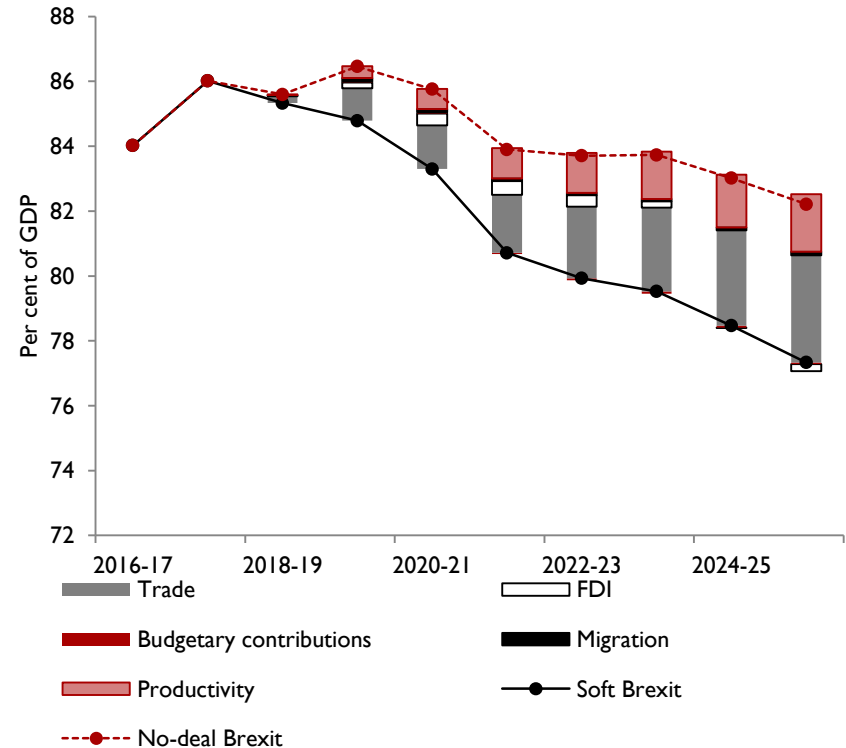


Fiscal deficit and fiscal debt forecast

Public sector net borrowing and Brexit variants

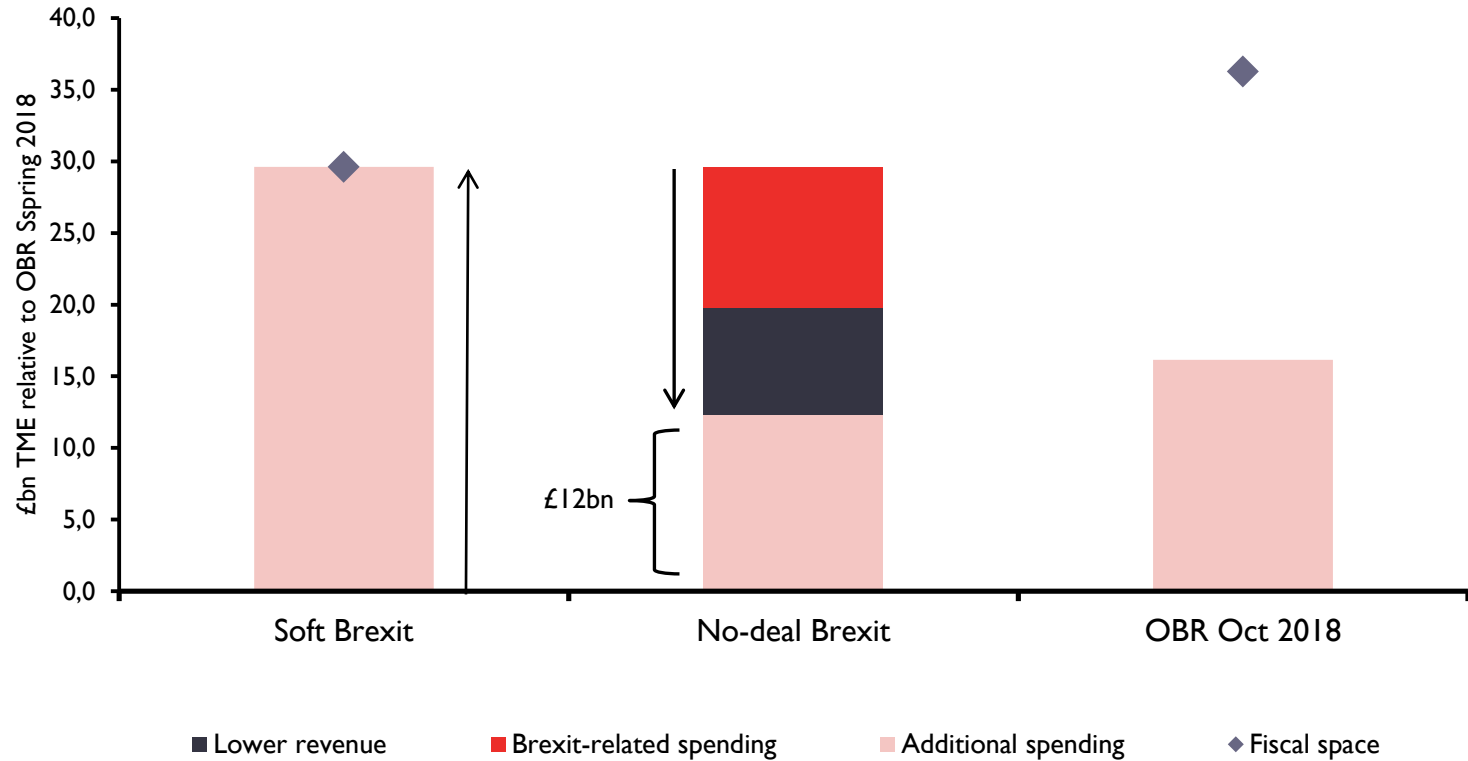


Public sector net debt and Brexit variants



Source: NiGEM Stochastic simulation

Fiscal space available under different scenarios



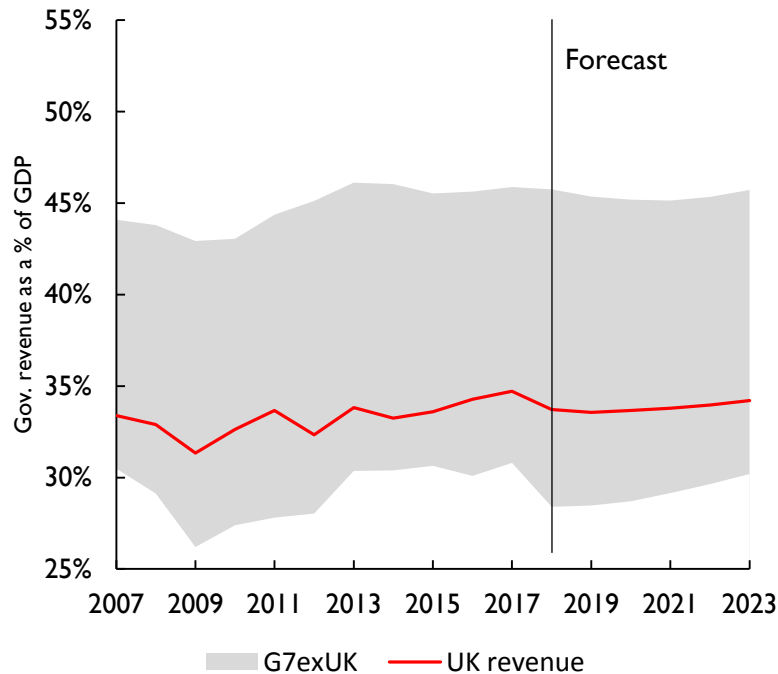
Fiscal rules checklist

	Soft Brexit		Orderly hard Brexit	
Spending compared with OBR Spring (average per annum, 2019-20 to 2022-23)	OBR Spring	OBR Spring plus £30 billion spending	OBR Spring	OBR Spring plus £30 billion spending
Fiscal mandate (structural deficit)		✓	✓	✗
Supplementary target (debt to GDP)	✓	✓	✓	✓
Fiscal objective (balanced budget)		✗	✗	✗

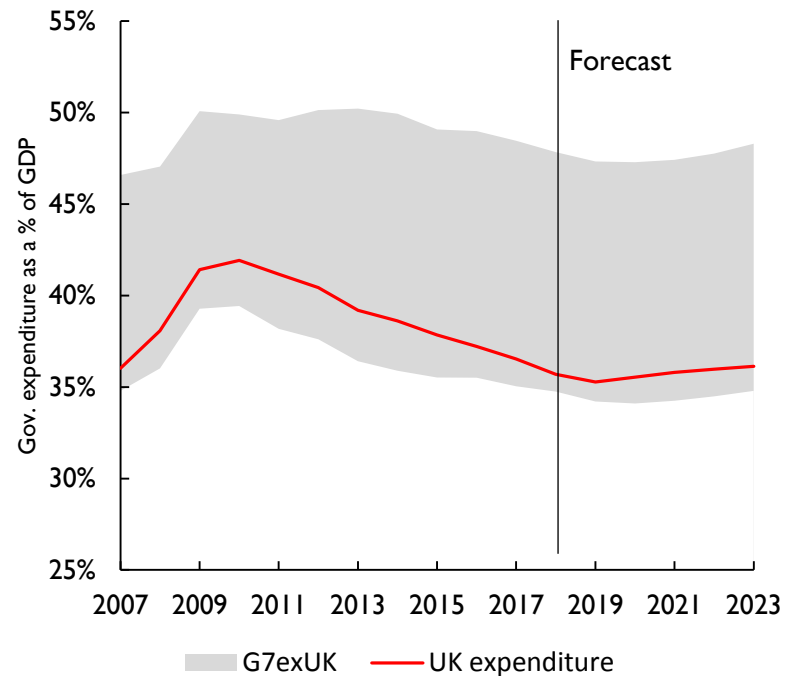


Expenditure and revenue, UK vs G7

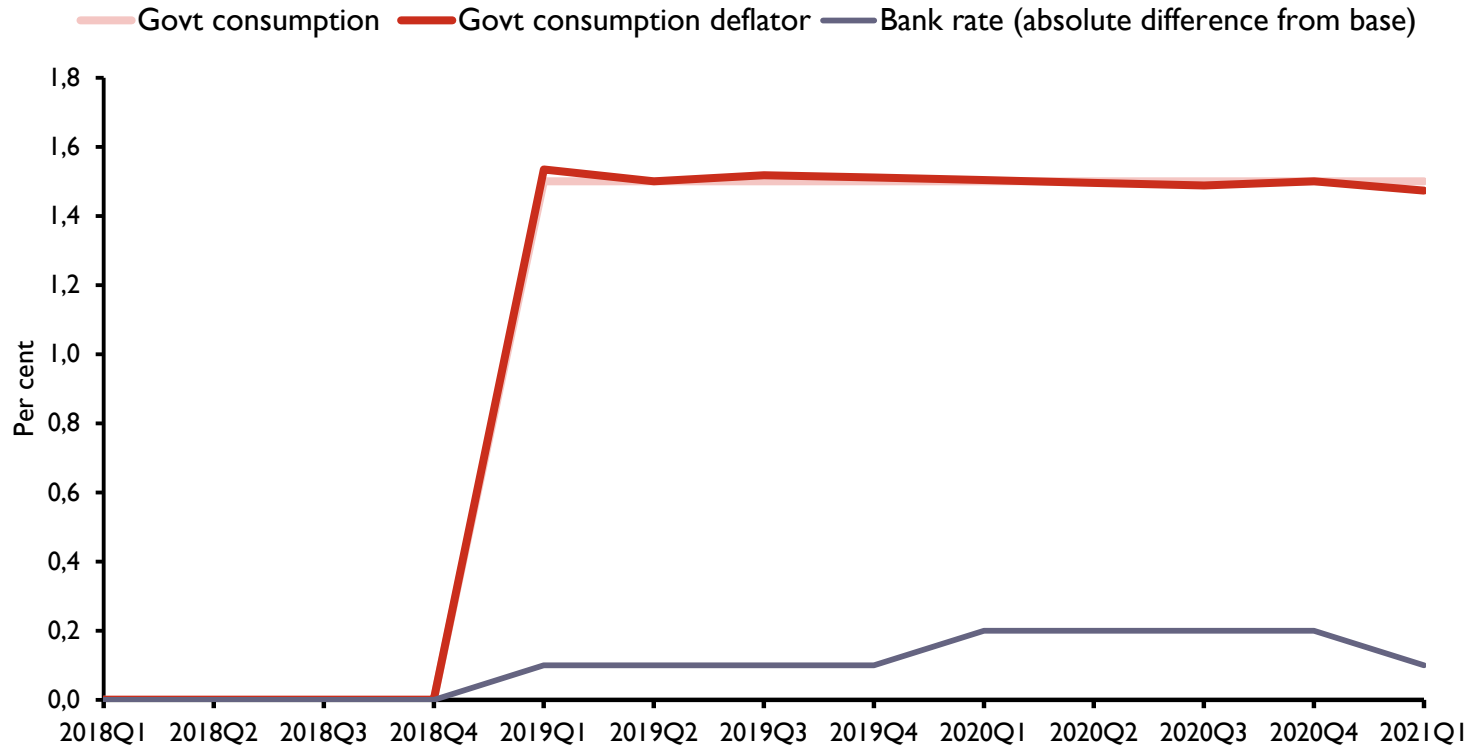
Gov. revenue as a % of GDP – G7 vs UK



Gov. expenditure as a % of GDP – G7 vs UK



Implications for monetary policy



Source: NIESR, OBR, ONS



UK forecast overview

Soft Brexit central case v no-deal Brexit scenario

	Real GDP growth	CPI inflation	Unem- ployment rate	Bank Rate	Current account balance (% of GDP)	<i>Per cent</i> PSNB (% of GDP)
2018	1.4 (1.4)	2.3 (3.0)	4.1 (4.6)	0.8 (1.0)	-3.1 (-3.5)	1.7 (1.8)
2019	1.9 (0.3)	1.9 (3.2)	4.0 (5.3)	1.3 (2.6)	-2.8 (-4.2)	1.7 (2.2)
2020	1.6 (0.3)	2.1 (2.6)	4.5 (5.8)	1.8 (2.5)	-3.3 (-4.0)	1.8 (2.7)

