

EMBARGO 00.01 hours 28 July 2010

Prospects for the UK economy

- GDP will grow by 1.3 per cent this year, and by 1.7 and 2.2 per cent in 2011 and 2012.
- The saving rate will remain above 6 per cent and per capita consumer spending will not reach its pre-recession peak until 2015.
- The announced increase in VAT will keep inflation above target until 2012.
- Public sector net borrowing will fall sharply reaching 2.8 per cent of GDP in 2015-16.
- The Emergency Budget has raised the probability of a decline in output in 2011 as compared to 2010 to 19 per cent.

Despite the very robust growth in the second quarter of this year, the economy will expand by just 1.3 per cent this year. Economic growth this year has so far been supported by government current and capital spending and a slowing pace of destocking. Disappointing net trade figures from the first quarter of this mean that net trade is a drag on GDP growth for the year as whole.

From next year the contribution of consumer spending will be less than in the decade before the recession. Per capita consumer spending will not recover its pre-recession peak until 2015. Growth will be more dependent on the contribution of net trade, while public spending will pose a drag on economic growth for longer than had previously been expected. Public sector spending cuts will subtract from economic growth in every year from 2011 to 2015.

Consumer price inflation will average 3 per cent this year and 2.7 per cent in 2011. The increase in the standard rate of VAT at the start of next year will keep the rate of inflation above target through next year. It is only in 2012 when the rate of inflation will fall below target, to an average of 1.4 per cent per annum.

The coalition government's more aggressive fiscal consolidation programme will result in public sector net borrowing falling more sharply than on our previous forecast. Net borrowing will moderate from £153 billion (10.9 per cent of GDP) in fiscal year 2009-10 to £51.3 billion (2.8 per cent of GDP) in 2015-16.

Tax and spending plans in the *Emergency Budget* will reduce the economic growth rate by 0.4 per cent in 2011. This has raised the probability of a decline in output in 2011 as compared to 2010 from 14 to 19 per cent.

Given the current plans and outlook for the economy it is more likely than not that the Chancellor's *Fiscal Mandate* will be met. But considerable risks to the outlook remain and the Chancellor will need to keep a watchful eye on the public finances. He has some headroom before any action would need to be taken.

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Notes:

The forecast for the UK economy is published in the National Institute Economic Review, no. 213, July 2010

For a full copy of the UK Economy forecast, please contact the NIESR Press Office:
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