

**NATIONAL INSTITUTE OF ECONOMIC AND SOCIAL
RESEARCH:
PRESS CONFERENCE
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Opening remarks by the Director**

Good morning. Welcome to the National Institute of Economic and Social Research for the release of our quarterly *Economic Review*. This morning we will concentrate on the outlook for the World and UK economy, which are perhaps showing signs of a divergence with below par growth in the UK and growing signs of a robust recovery in the rest of the World.

A theme of the Review is the question of policy normalisation and how it ought to be managed, explained and brought about some 10 years after the start of the financial crisis. The Review publishes a number of important papers that help us understand the ongoing impact. The financial crisis started ten years ago when BNP Paribas closed three funds in August 2007, temporarily as it turned out, when they argued that it was no longer possible to value accurately the portfolios of assets and liabilities. From that date interbank markets froze and to some great extent are still in the midst of an Ice Age. Liquidity between private agents was severely restricted and the public sector was asked to step in and provide financial support. That early shock, like the fall Credit-Anstalt in 1931, triggered a sequence of events from which 10 years after we can still observe the repercussions. In this special issue we examine many of the resulting debates for monetary, fiscal and financial policy. Papers by Sinclair (Birmingham) and Allen (NIESR), McMahon (Warwick), Barwell (BNP Paribas), Chadha, Kara and Labonne (all NIESR) and Aksoy (Birkbeck), Basso (Bank of Spain) and Smith (Birkbeck), as well as notes by Allen (NIESR) and Farmer (Warwick and NIESR) will provide an important source for researchers.

The forecast for world GDP growth in 2017 has been revised up to 3.6 per cent, which would be the fastest growth in six years. Growth projections for 2018 and the medium term are unchanged, at 3.6 and 3.4 per cent, respectively and inflation forecasts have nevertheless generally been revised

down slightly. In the Euro Area, stronger economic performance, together with reduced political uncertainty, provides an opportunity for action to complete the monetary union and reduce economic imbalances. But to avoid jeopardising the recovery, central banks in the advanced economies will have to manage policy normalisation with particular caution. Perhaps nowhere more so than in the UK.

The general election held on 8 June delivered an unexpected result. The Conservative Party was widely expected to gain parliamentary seats at the cost of the main opposition Labour party and solidify its hold over parliament. Instead, they lost seats and were forced to enter into a confidence and supply arrangement with the Northern Irish Democratic Unionist Party, raising the prospect of another early general election and all this just as the UK started formal negotiations for withdrawing from the EU. The British electorate has been asked to vote in each of the past four years, starting with the Scottish referendum in 2014, a general election in 2015, the EU referendum in 2016 and the early general election this year. It is hardly surprising then that the odds for another early general election stand at 80 per cent according to the average of the three largest betting companies.

The outcome of the general election has both raised and reflected political uncertainty in the UK, but the impact on the economy and financial markets is not entirely clear. There continues to be something of a disconnect between political outcomes and the economy. For example, GDP growth scenarios related to exit from the EU that were at the lower end of the distribution have so far proved to be too pessimistic, but also and more specific to the general election outcome, there is a perception that the new government will look to negotiate a ‘softer’ exit from the EU because it is now more dependent on constituencies that are in favour of a stronger link with the EU. One lesson to learn is that the average continues to mask a wide range of outcomes and opinions at the level of the household or region.

Our forecasts for GDP growth in the UK for this year and next remain unrevised at 1.7 per cent and 1.9 per cent, respectively. The economy has slowed each year since 2014 and according to our forecast, 2017 will mark the trough for GDP growth. Thereafter, we envisage a modest recovery that

takes economic growth to a level that is close to potential. Annual consumer price index inflation peaks at 3.0 per cent in the last quarter of this year before easing back to the target rate of 2 per cent in the final quarter of 2019. We have brought forward the timing of the rate hike from the second quarter of 2019 to the first quarter of next year. In our forecast, the fiscal deficit is eliminated in 2022 and the debt-to-GDP ratio peaks in 2018/19. We have brought forward the timing of the Bank Rate hike from the second quarter of 2019 to the first quarter of next year. Such a move would be the first policy rate increase in nearly eleven years. This rate increase should not be seen as a tightening in policy, but instead as a modest withdrawal of some of the additional stimulus that was injected into the economy after the 2016 EU referendum. Ultimately we think that the groundwork for a fuller normalisation of policy has yet to be laid.

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