

UK and Global Economic Outlooks



Summer 2023

Presenters

Opening Remarks

Stephen Millard

Outlook for the Global Economy

Barry Naisbitt

Outlook for the UK Economy

Leaza McSorley

Outlook for UK Regions and Households

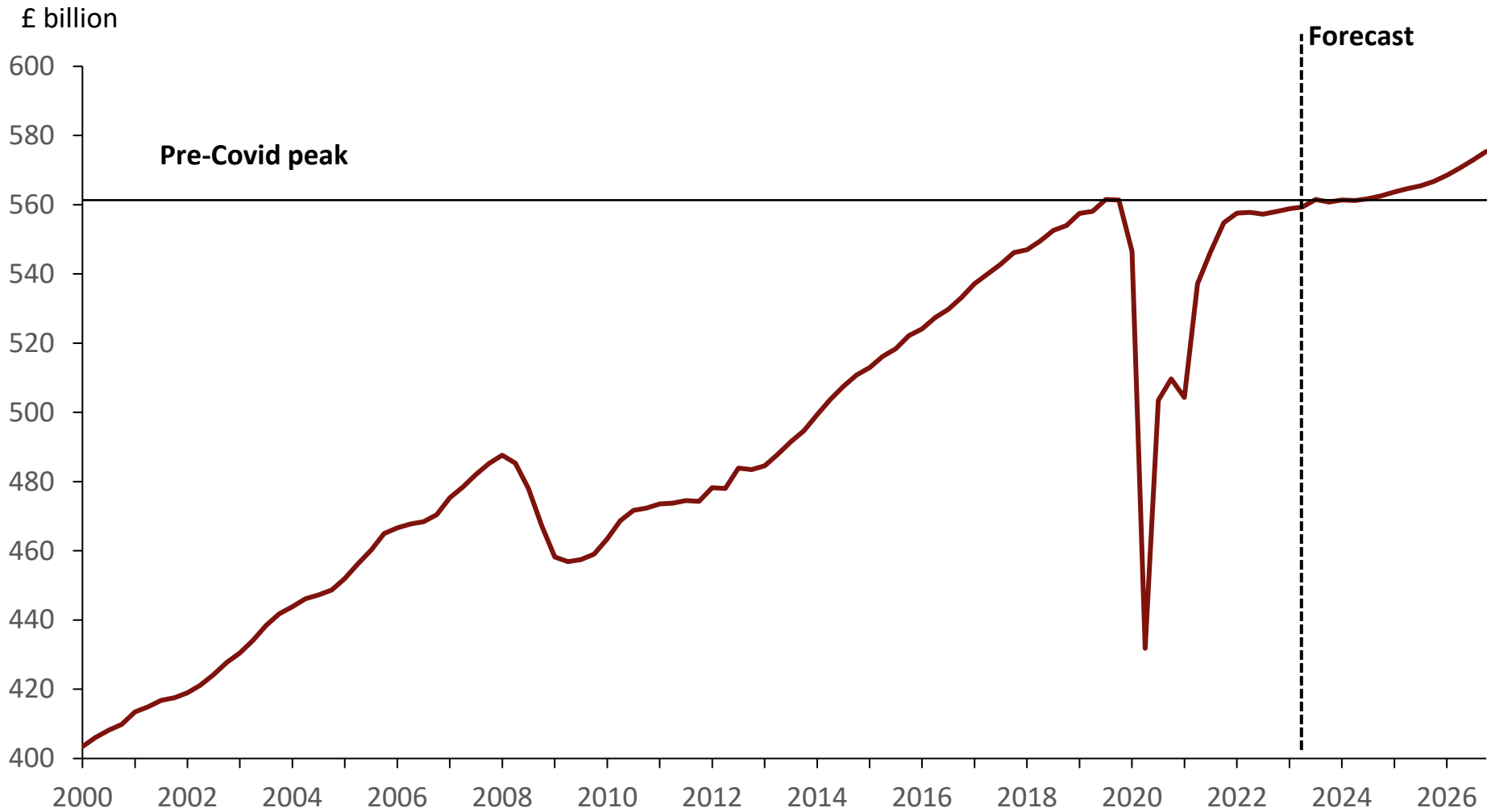
Arnab Bhattacharjee

Opening Remarks



Stephen Millard

The British Disease



Outlook for the Global Economy



Barry Naisbitt

Xuxin Mao, Ed Cornforth, Ian Hurst, Iana Liadze, Stephen Millard, Joanna Nowinska, Urvish Patel and Patricia Sanchez Juanino

Key Messages

- Inflation has peaked in the advanced economies...
- ...and forecast to return to target rates
- Heterogeneous inflation experiences in emerging economies
- GDP growth weak this year and next ...
- ... and likely to remain low relative to the recent past

The Rise and Fall of Inflation?

- Inflation driven up by two big shocks:
 - Covid and supply chain disruption
 - Russia's invasion of Ukraine
- Inflation has now peaked in the advanced economies
- How quickly will it come down?
- And will it stay there?

The Rise and Fall of Inflation?

Figure 8 Annual headline inflation

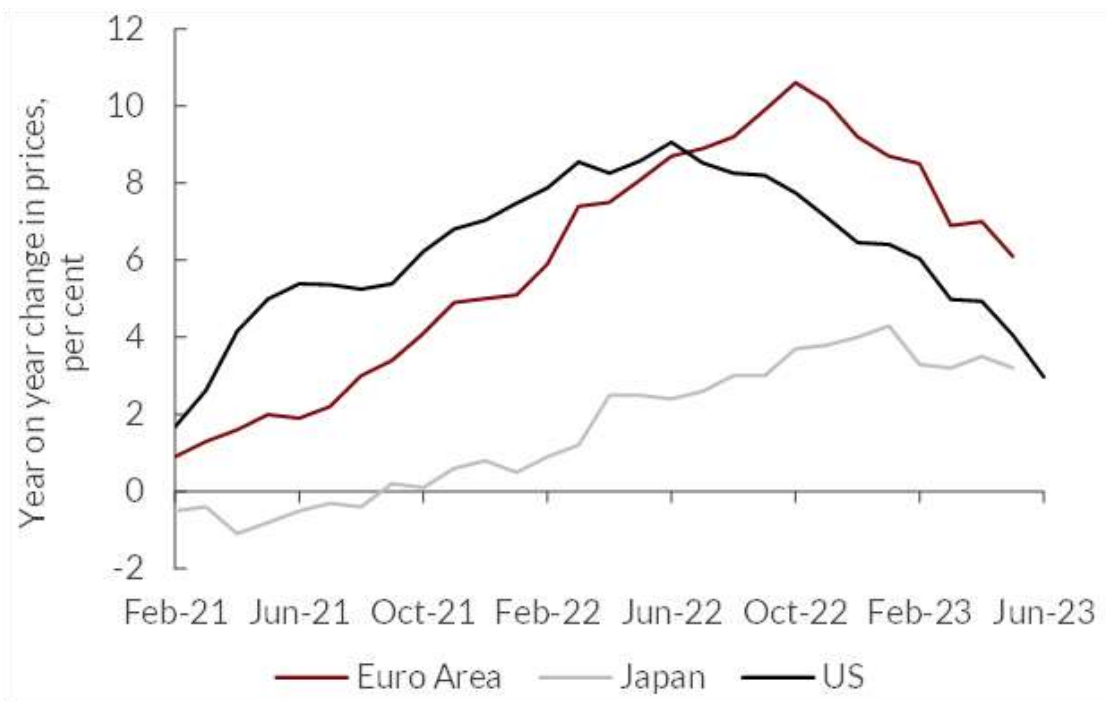
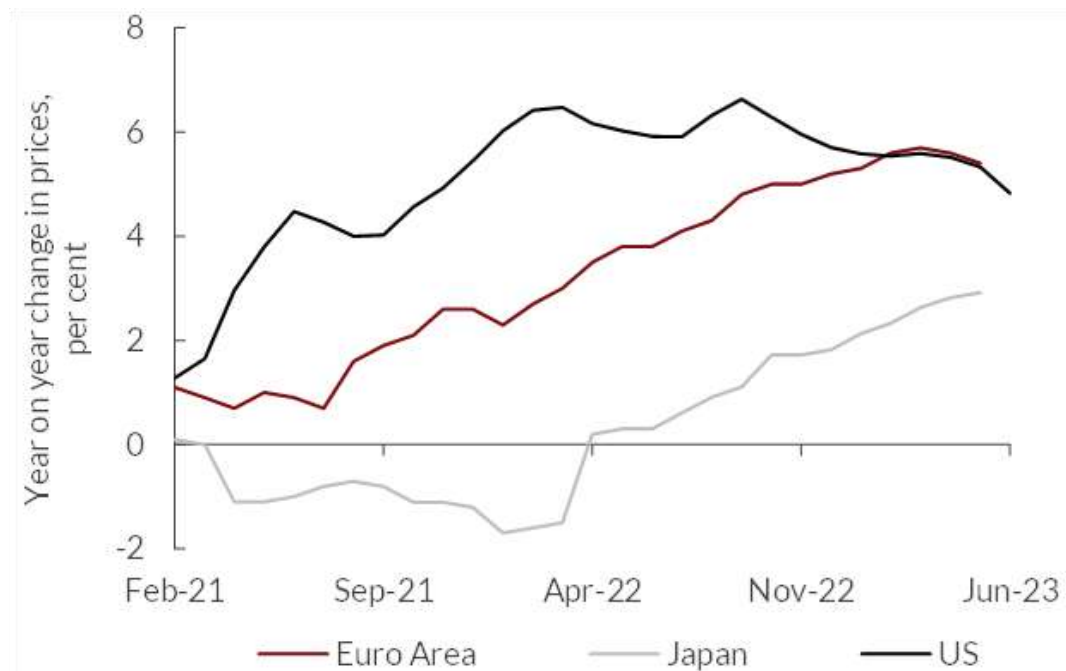


Figure 9 Annual core inflation



- Headline inflation in G7 looks to have peaked
- But core inflation still high
- So monetary tightening has continued

The Rapid Tightening Cycle is Ending

Figure 13: US policy interest rate tightening

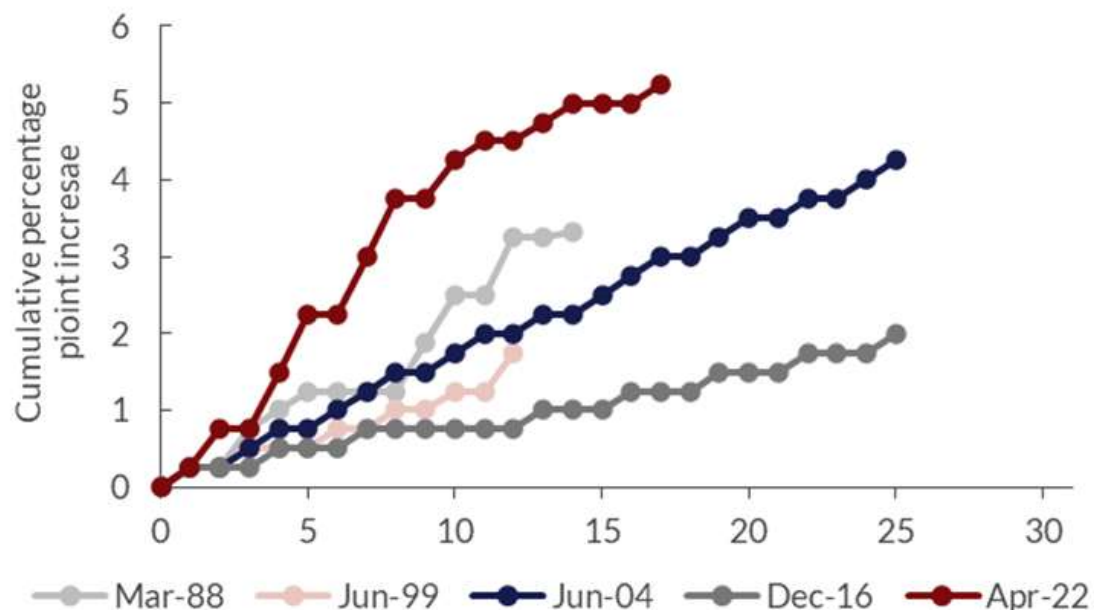
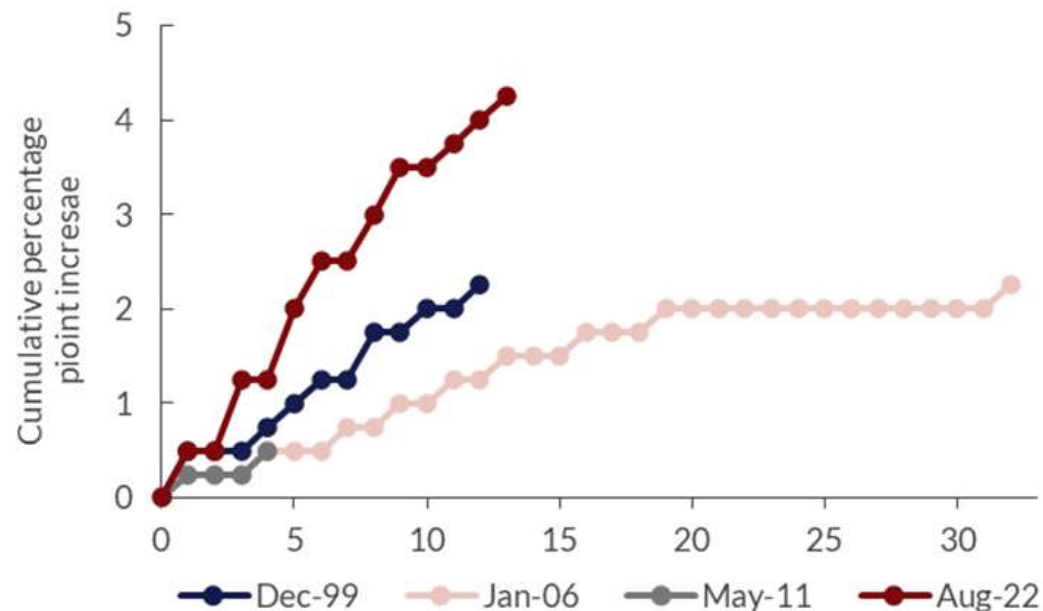
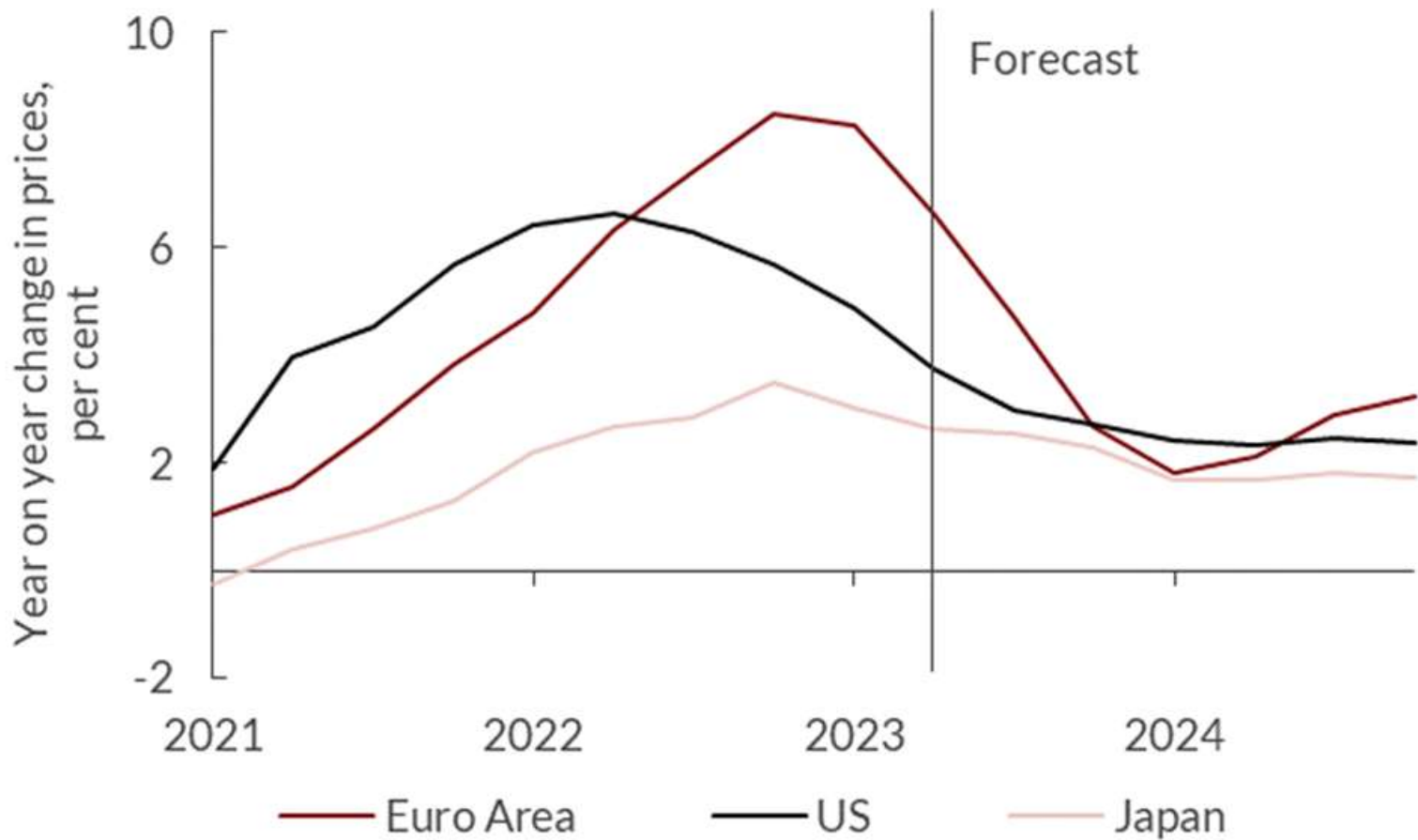


Figure 14: ECB policy interest rate tightening



- Have they done enough to get inflation back to target?
- Will the monetary tightening damage GDP growth?

Inflation in the Advanced Economies

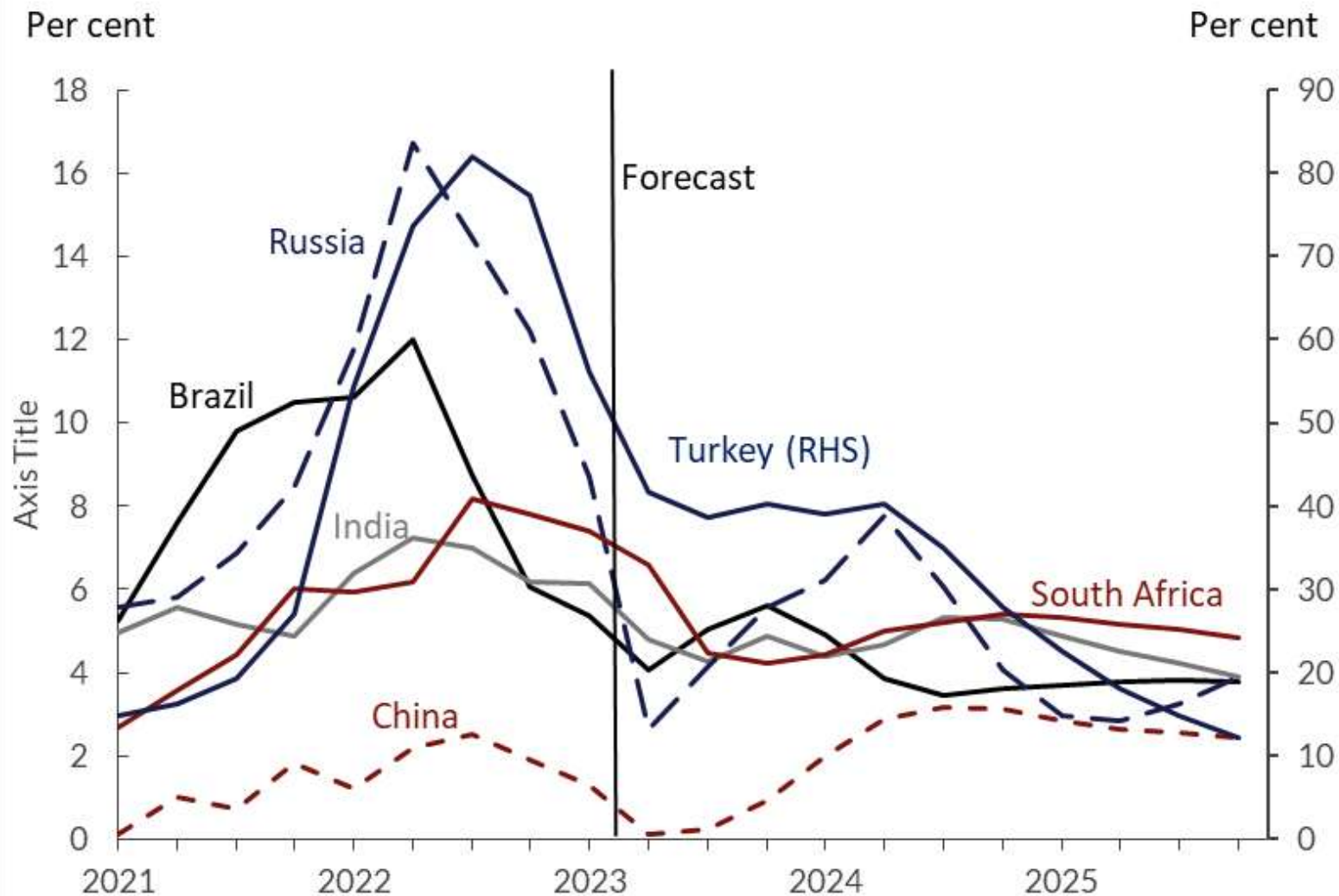


- Coming down to target relatively quickly
- But will it stay there?

Note: Consumer expenditure deflator

Source: NiGEM database and NIESR forecast

Inflation in Emerging Economies



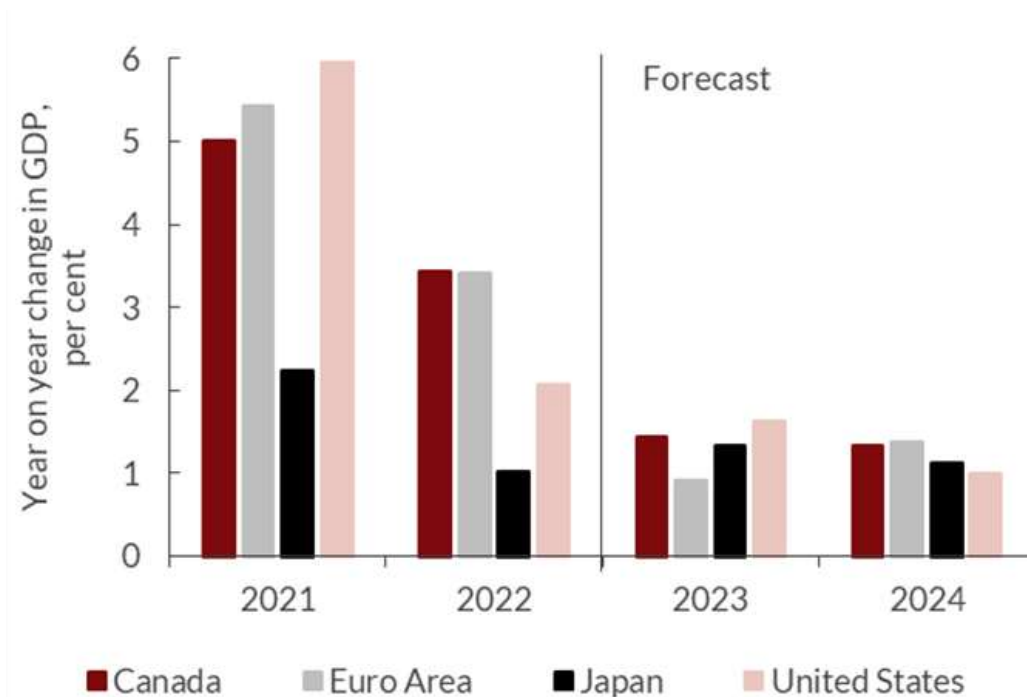
- No inflation spike in China and India
- Inflation returns to 2-6% (ex. Turkey)

Note: Consumer expenditure deflator

Source: NiGEM database and NIESR forecast

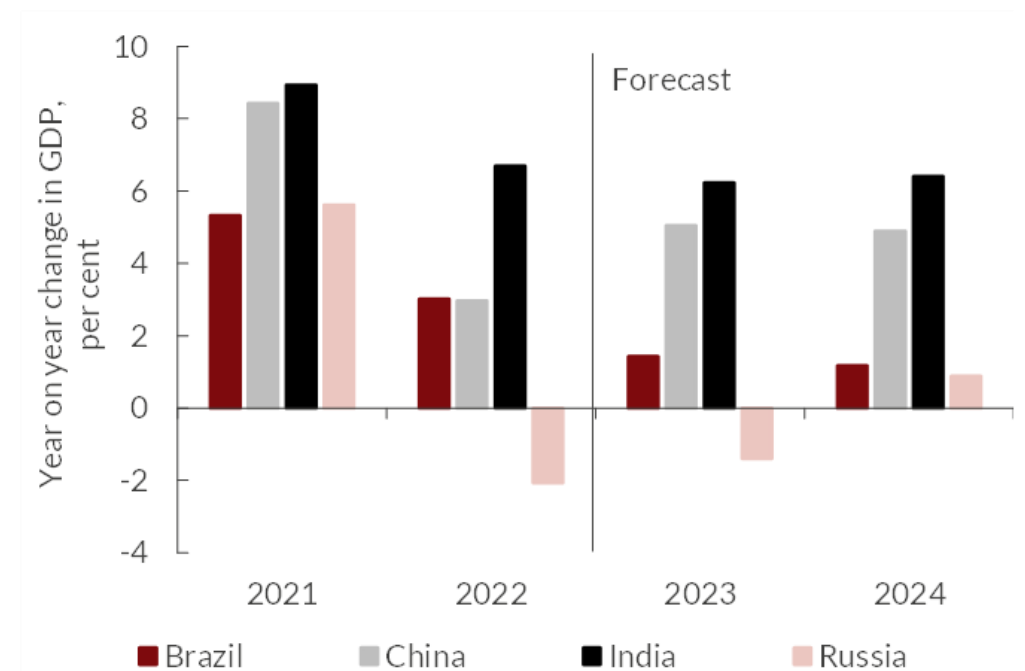
What About GDP Growth?

Figure 17 GDP growth in advanced economies



Source: NiGEM database and NIESR forecast

Figure 18 GDP growth in emerging economies



Source: NiGEM database and NIESR forecast

- Global growth below 3% in 2023 and 2024
- Apart from Covid-hit 2020, slowest growth years since the global financial crisis in 2009

Key Risk: Fragile Growth Prospects

Near-term

- Risk of a US recession
- Monetary policy may be tightened too much
- Inflation may not be sustained at target rates
- War in Ukraine is still continuing

Medium-term

- Growth in China will be moderate relative to the past two decades
- Advanced economies are likely to make a lower contribution to global growth

Forecast Summary

Table 2 Forecast summary percentage change

	Real GDP ^a												World Trade ^b
	World	OECD	China	India	BRICS+	Euro Area	USA	Japan	Germany	France	Italy	UK	
2021	6.3	5.7	8.4	8.9	7.7	5.4	5.9	2.2	2.6	6.4	7.0	7.6	10.4
2022	3.4	2.9	3.0	6.7	3.5	3.4	2.1	1.0	1.9	2.5	3.8	4.1	5.0
2023	2.7	1.4	5.1	6.2	4.2	0.9	1.6	1.3	0.1	0.7	1.1	0.4	2.4
2024	2.8	1.3	4.9	6.4	4.4	1.4	1.0	1.1	1.3	1.3	1.0	0.3	2.8
2025-2029	2.9	1.7	4.5	5.7	4.2	1.6	1.6	0.9	1.4	1.6	1.3	1.4	4.2

	Private consumption deflator									Interest rates ^c			Oil (\$per barrel) ^(d)
	OECD	BRICS+	Euro Area	USA	Japan	Germany	France	Italy	UK	USA	Japan	Euro Area	
2021	4.0	4.5	2.2	4.0	0.5	3.0	1.5	1.5	2.5	0.3	-0.1	0.0	69.9
2022	10.9	11.1	6.7	6.3	2.8	6.6	4.9	7.4	7.9	1.9	-0.1	0.6	97.2
2023	8.3	8.4	5.5	3.6	2.6	6.2	5.6	4.7	7.4	5.2	-0.1	3.8	79.7
2024	5.4	9.2	2.6	2.4	1.7	3.2	2.2	2.3	4.4	5.1	0.0	4.4	84.1
2025-2029	2.5	3.6	2.0	2.0	1.3	1.9	2.1	1.9	2.4	3.4	0.4	3.4	88.8

Notes: BRICS+ includes Brazil, China, Russia, India, Indonesia, Mexico, South Africa, Turkey. a GDP growth at market prices. Regional aggregates are based on PPP shares. 2017 reference year. b Trade in goods and services

c Central bank intervention rate, period average per cent. d Average of Dubai and Brent spot prices

Source: NiGEM database and NIESR forecast

Outlook for the UK Economy

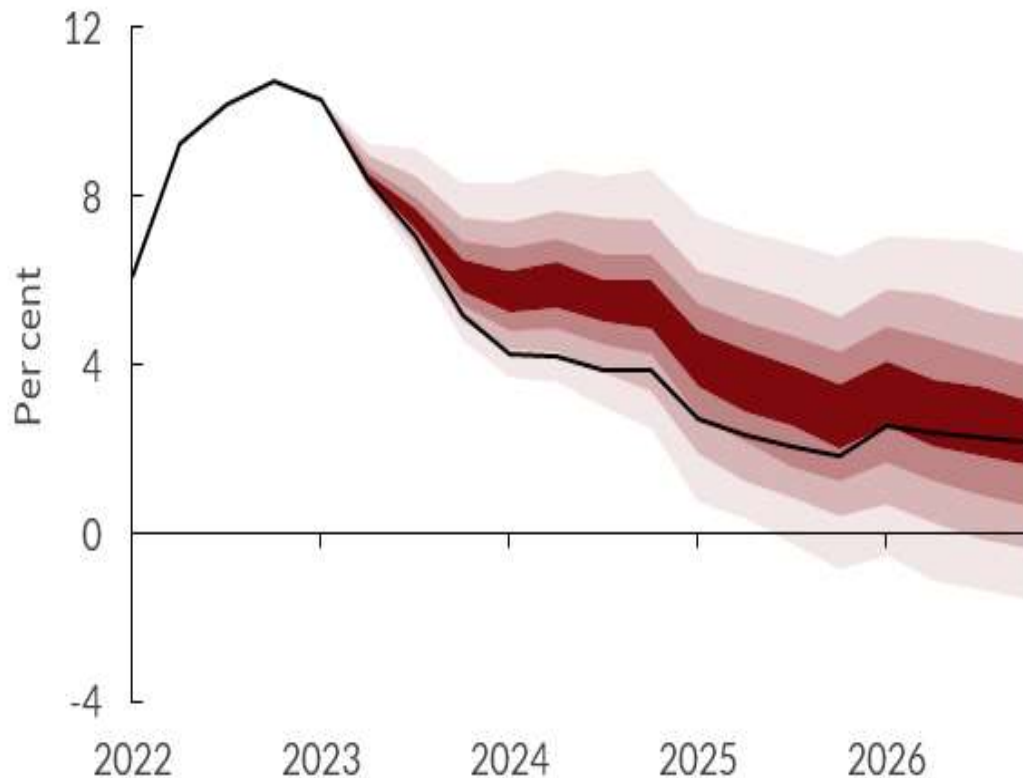


Leaza McSorley

Paula Bejarano Carbo, Hailey Low, Stephen Millard, and Kemar Whyte

Inflation

Figure 1.3 CPI inflation fan chart



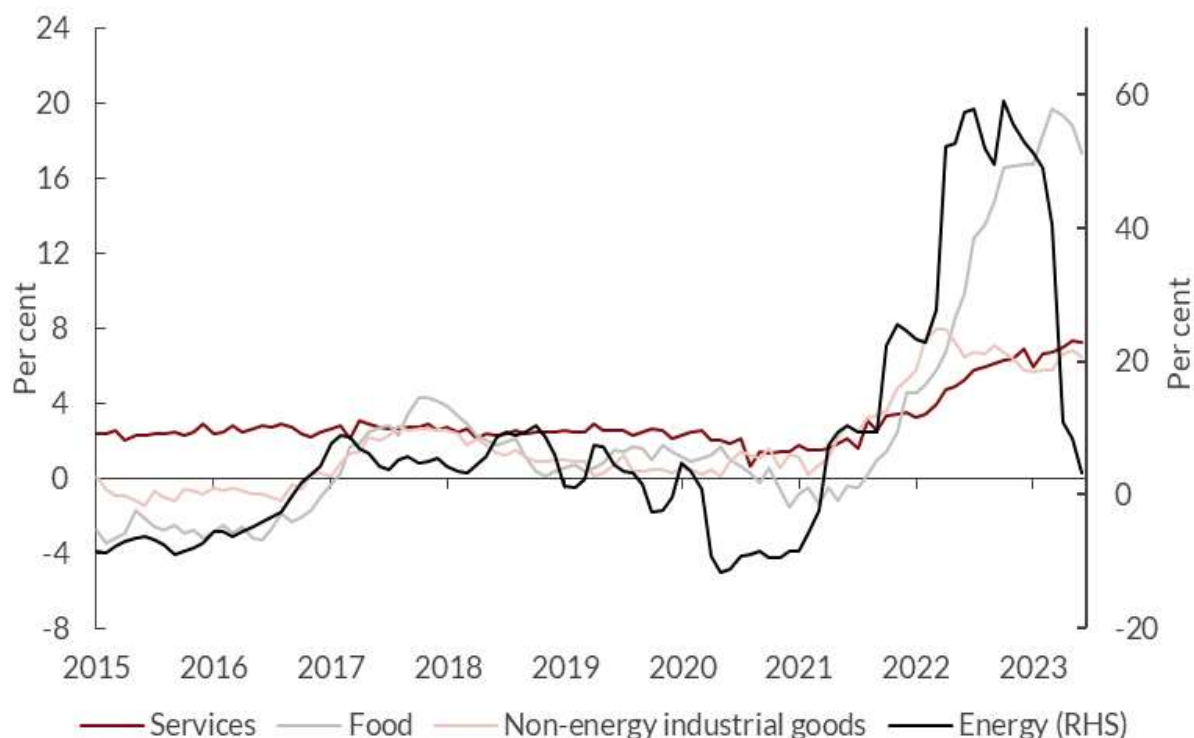
Note: The shades within the fan chart represent a 10 per cent chance that GDP growth will lie within the boundary of that shade. There is a 20 per cent chance that GDP growth will lie outside the shaded area of the fan.

Source: NiGEM database, NIESR forecast and NiGEM stochastic simulations.

- Twelve-month Consumer Price Index (CPI) inflation fell to 7.9% in June, down from 8.7% in May
- We forecast **CPI inflation to fall to 5.2% by the end of 2023 and to 3.9% by the end of 2024**
- Core inflation at 6.9% and other underlying inflation measures remaining high and reducing more slowly indicates potential second-round effects, which can indicate inflation persistence

Inflation

Figure 1.4 Annual inflation rates for elements of the consumer price index



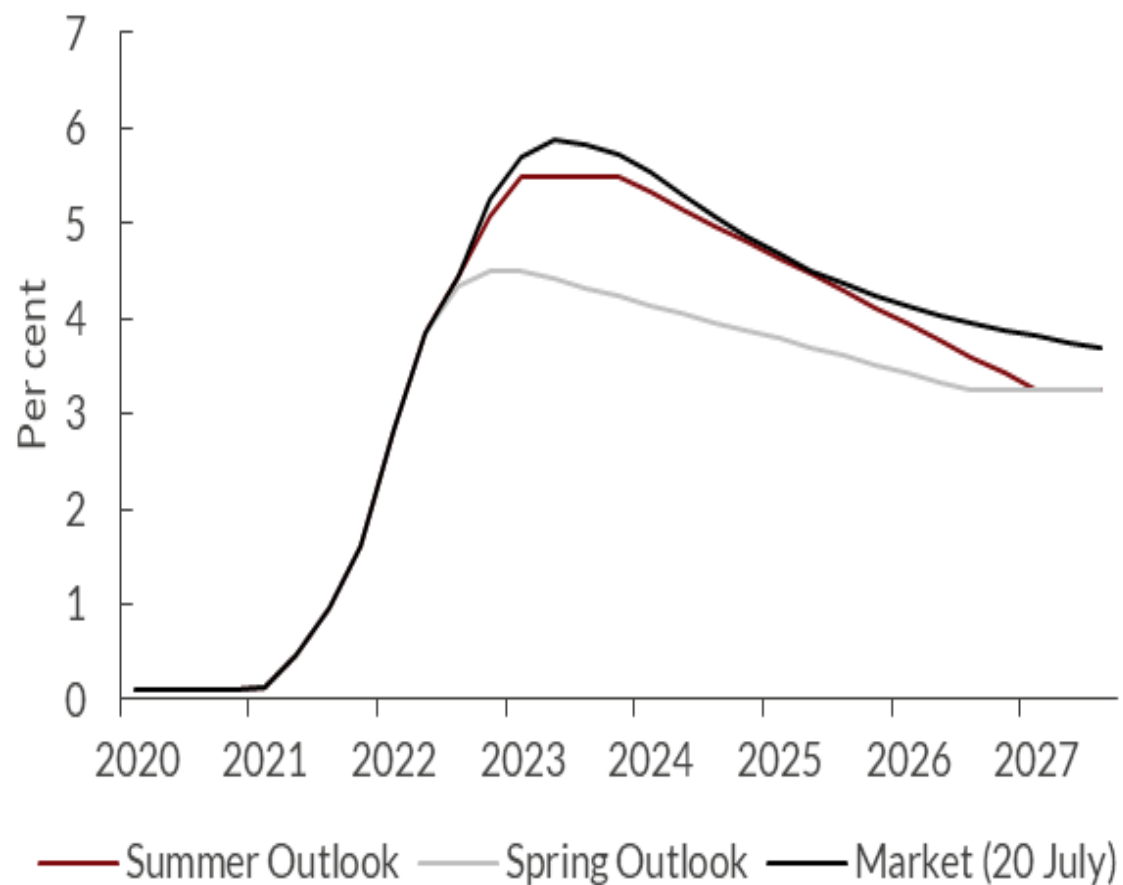
Note: Core CPI refers to CPI inflation excluding energy, food, alcoholic beverages, and tobacco. Trimmed mean inflation is measured by excluding 5 per cent of the highest and lowest price changes in the CPI calculation.

Source: NiGEM database, NIESR forecast

- With the large energy price rises ‘falling out’ of the CPI basket from April 2023 onwards, the drivers of inflationary pressures have shifted towards rising food, non-energy goods, and services prices
- Food inflation rose by 7.5% between June 2022 and June 2023
- Services and non-energy industrial goods inflation have plateaued around 7%

Monetary Policy

Figure 1.6 Bank Rate forecast comparison

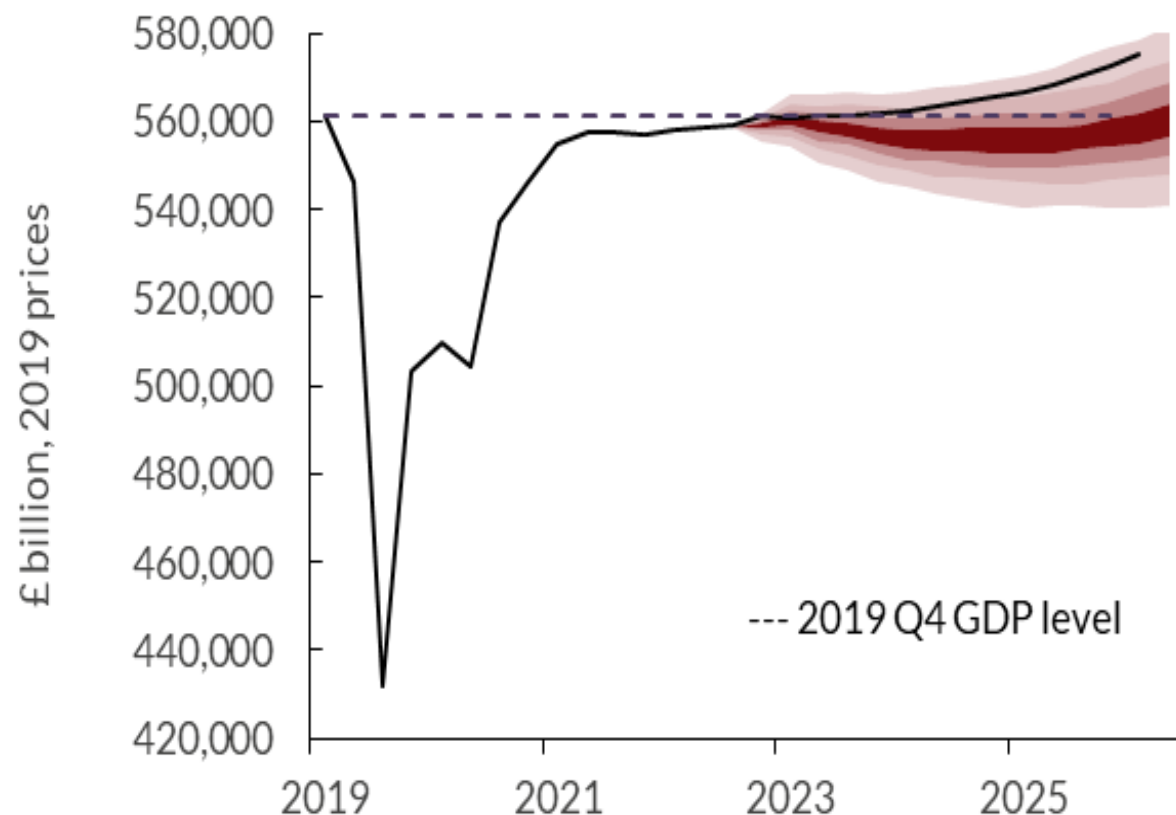


Source: Bank of England, NiGEM database

- Cumulative monetary policy action has tightened financial conditions
- **Our forecast is conditioned on the Bank Rate peaking at 5.50%.** It is notable that our Bank Rate projection lies below the market curve
- MPC may wish to make clear in its communication that, as monetary policy is forward looking, it has done enough to get in front of inflation, as it sets out its path towards target. Failing to do so may risk further market reaction

GDP

Figure: GDP level (£billion 2019 prices)



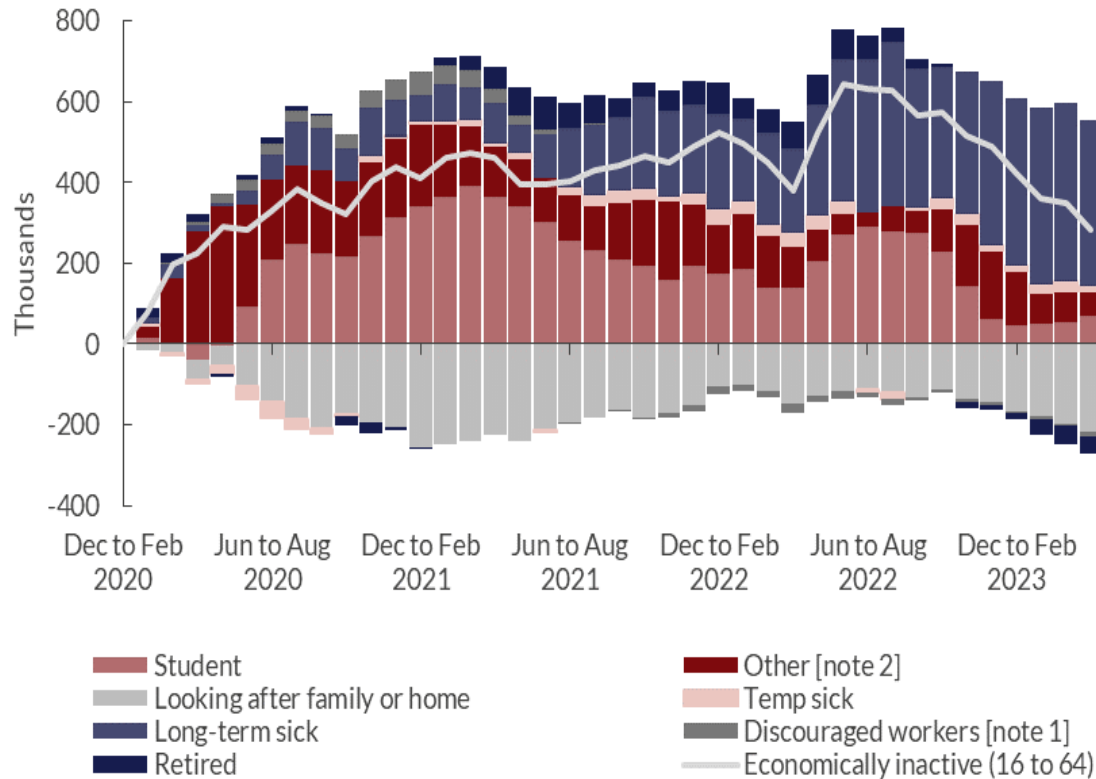
Note: The shades within the fan chart represent a 10 per cent chance that GDP growth will lie within the boundary of that shade. There is a 20 per cent chance that GDP growth will lie outside the shaded area of the fan.

Source: NiGEM database, NIESR forecast and NiGEM stochastic simulations.

- Against this background, the outlook for growth remains subdued with the longer-term view of persisting low economic growth in the United Kingdom
- **We expect GDP growth in this year and next of 0.4% and 0.3%, respectively**
- However, given continued monetary policy tightening these risks are skewed towards the downside

Labour Market Supply

Figure 1.21: Change in economic inactivity by category since Dec 2019 – Feb 2020

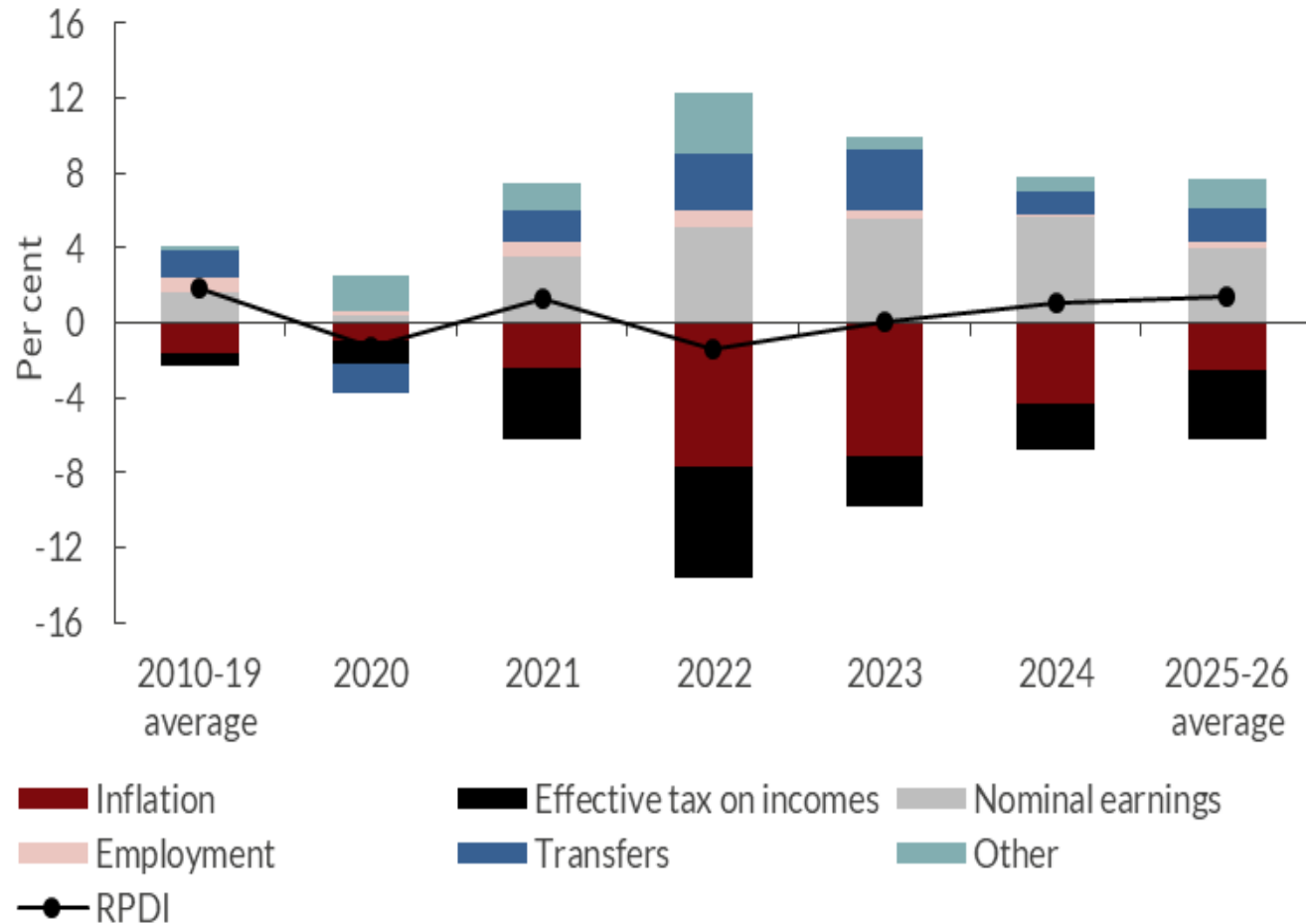


Source: ONS/NIESR

- Fall in the economic inactivity rate but the number of long-term sick remains high compared to pre-pandemic levels.
- Overall, the labour market has begun to loosen, with an uptick in unemployment and falls in vacancies, but remains tight
- **We forecast unemployment rate of 4.1% in 2023, 4.7% in 2024 and peaking at 5.1% in 2025.**
- **We expect wage growth to remain above 6% in 2023 and 2024**

Real Personal Disposable Income

Figure 1.10 Contributions to growth in real personal disposable income



- Real personal disposable income (RPDI) by 1.4% in 2022
- We now expect real personal disposable incomes to grow slightly in 2023 and 2024, by 0.1% and 1.0%, respectively, as inflation falls while nominal earnings growth remains at around 6%
- Over the medium term, we expect real incomes to grow by around 1.4%

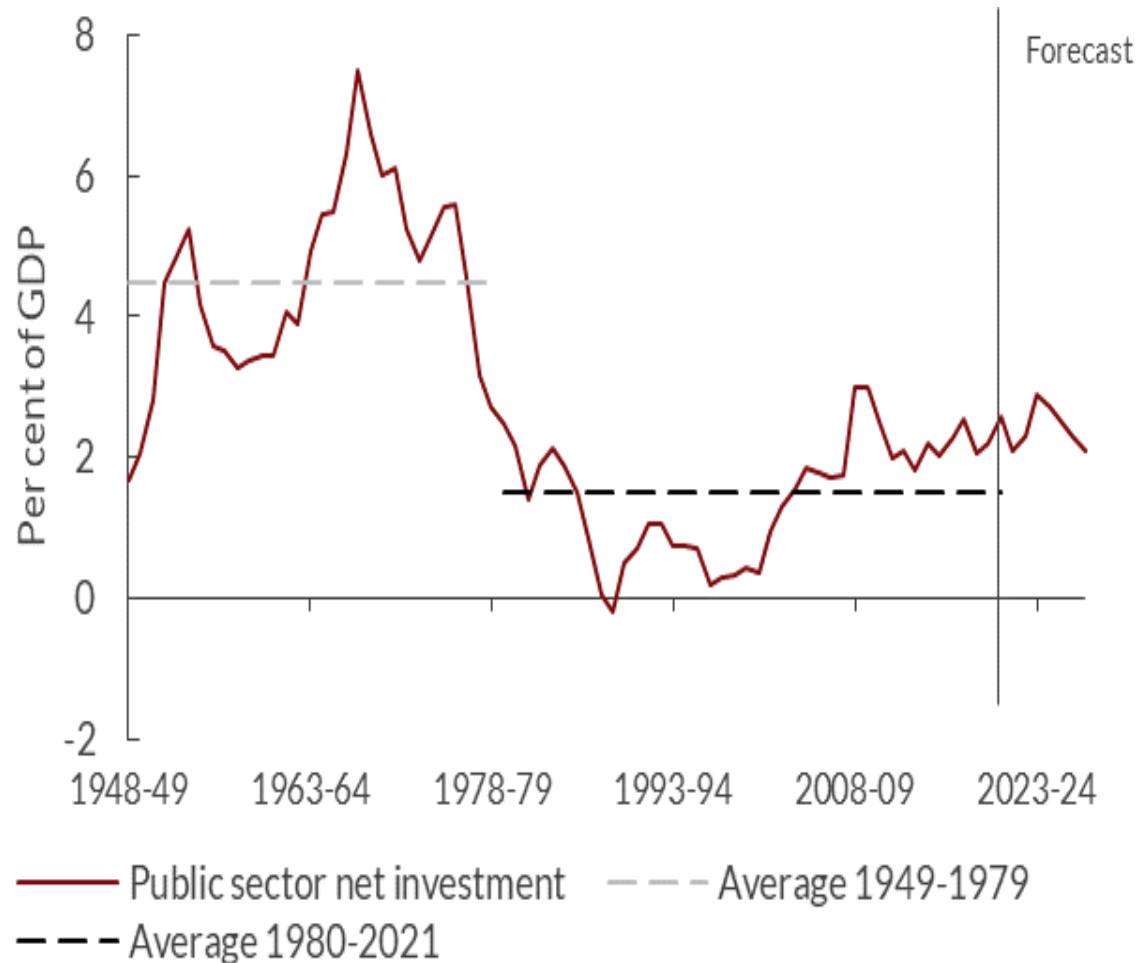
Source: NiGEM database, NIESR forecast

Fiscal Policy

- **Public sector net debt (PSND) was 100.8% of GDP in June**
- Surpassing the 100% of GDP mark represents a milestone moment, albeit one that was expected. This figure is 1.5% below the trajectory outlined in the Office for Budget Responsibility's (OBR's) March forecast, due to lower cash debt and higher GDP outturn
- However, **higher interest rates and inflation have increased government interest payments to 3.8% of GDP in 2022-23** and raised potential QT-related cumulative net losses

Fiscal Policy

Figure 1.8 Public sector net investment



- The OBR released its Fiscal Risks and Sustainability Report in July 2023
- Challenges to public finance highlighted were: inactivity and health, energy, and high debt
- NIESR has been arguing for some time now that the United Kingdom needs a **new fiscal framework that can provide enough flexibility and competence to respond to economic shocks while ensuring credibility is maintained and fiscal policy works for all.**

Source: OBR, ONS, NIESR calculations

Forecast Summary

Table 1.1 Summary of the Forecast (percentage change unless otherwise stated)

	2019	2020	2021	2022	2023	2024	2025	2026	2027
GDP	1.6	-11	7.6	4.1	0.4	0.3	0.6	1.2	1.7
Per capita GDP	1.1	-11.4	7.2	3.4	-0.1	-0.2	0.2	0.8	1.3
CPI Inflation	1.8	0.8	2.6	9.1	7.7	4.1	2.3	2.4	2.2
RPIX Inflation	2.5	1.7	4.2	11.5	8.5	4.4	2.8	3	3
RPDI	2.1	-1.3	1.3	-1.4	0.1	1	1	1.7	2.1
Unemployment, %	3.8	4.6	4.5	3.7	4.1	4.8	5	5.1	5
Bank Rate, %	0.8	0.2	0.1	1.5	4.7	5.5	4.9	4.2	3.5
Long Rates, %	0.9	0.3	0.8	2.4	4.1	4.2	3.8	3.5	3.4
Effective exchange rate	-0.5	0.5	4.7	-2.2	2.3	2.1	-1	-1	-0.6
Current account as % of GDP	-2.9	-3.1	-1.5	-3.8	-4.5	-4.9	-4.5	-3.7	-2.9
Net borrowing as % of GDP	2.5	15.3	5.7	5.3	5.4	3.4	1.3	0	-1.9
Net debt as % of GDP	82.3	101.6	99.7	99.3	98.8	98	93.3	89	82.9

Note: Numbers reported are yearly averages except for net borrowing, which is reported for the full fiscal year, and net debt, which is reported for the end of the fiscal year.

Outlook for the Devolved Nations, English Regions and UK Households



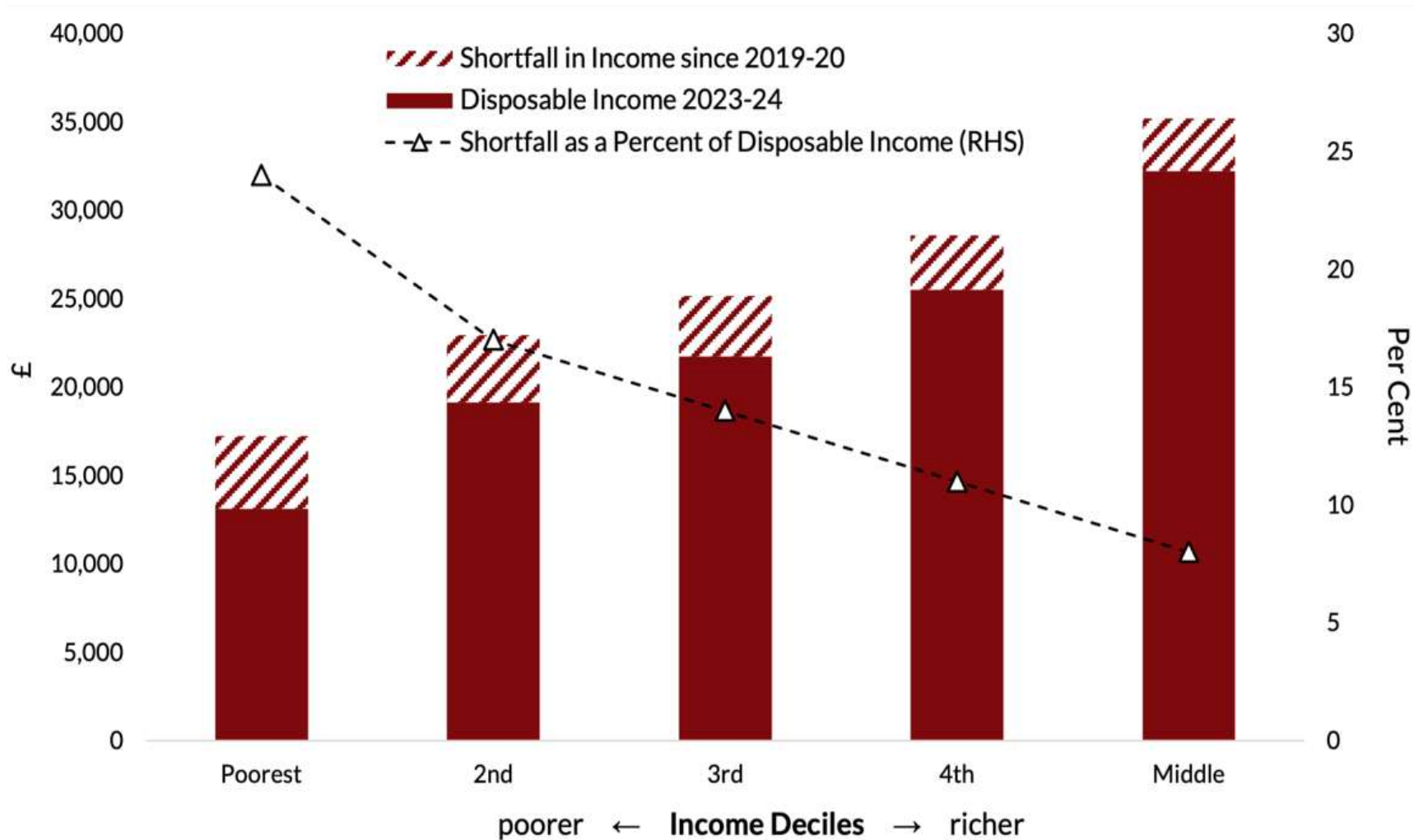
Arnab Bhattacharjee

with Max Mosley, Adrian Pabst, Robyn Smith and Tibor Szendrei

Key Messages on UK Households

- Widening disparities of income and wealth:
 - little real wage growth for low-income HHs
 - low or no savings
 - higher debt
 - elevated energy, food and housing costs
- A 17% shortfall in the disposable incomes of the poorest, compared with a 5% shortfall for the richest

Income Shortfalls in 2024 Relative to 2019



Source: LINDA

Return of the Squeezed Middle (Real Wages)

Table 2.1 Annual real wage growth for the lowest, median and highest earners

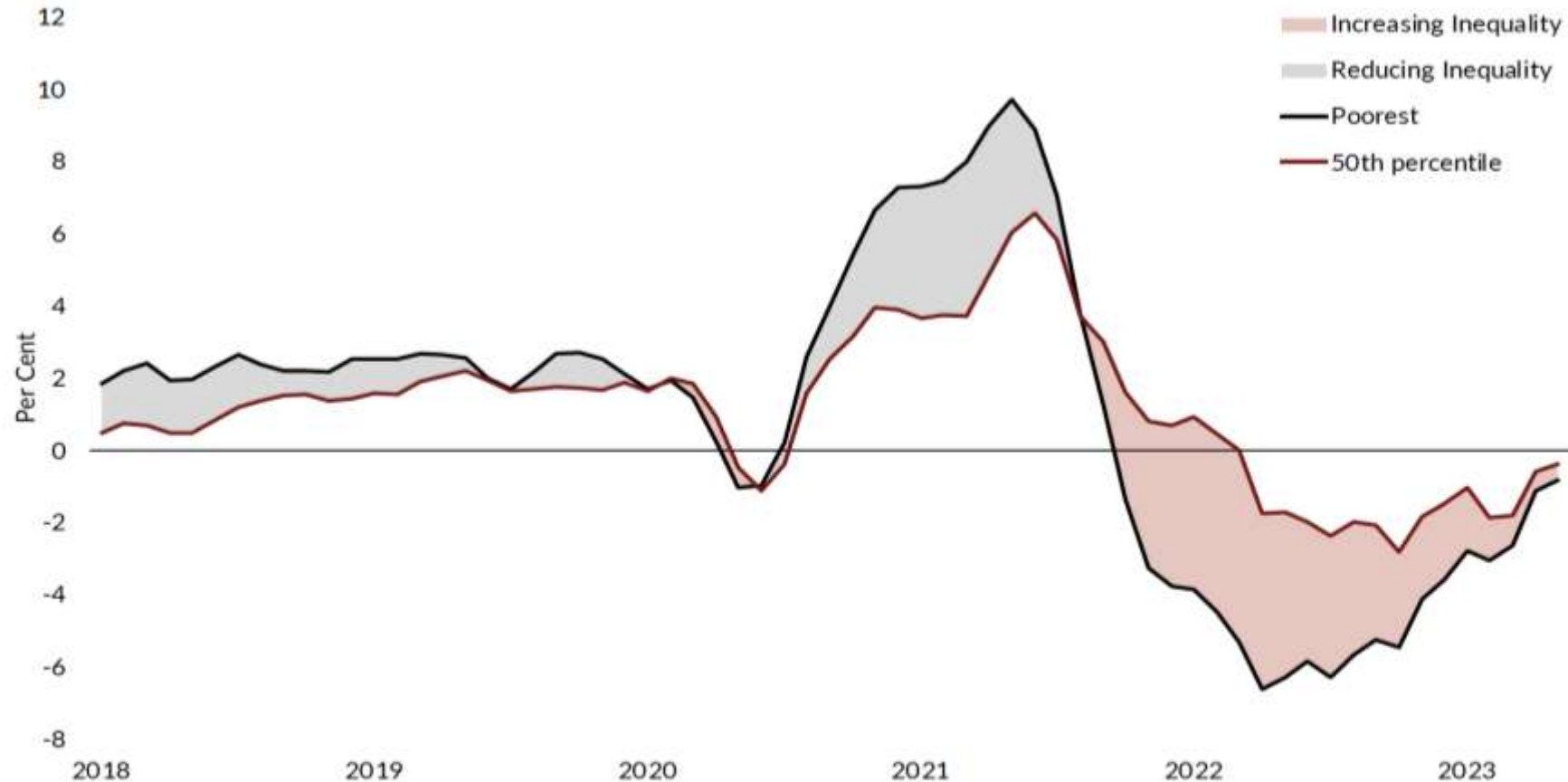
Date	Poorest (10th percentile)	50th percentile	Richest (90th percentile)
2018	1.1%	1.3%	3.3%
2019	2.4%	2.5%	6.0%
2020	-1.0%	0.2%	1.2%
2021	2.6%	2.3%	3.1%
2022	-1.6%	-3.6%	-0.1%
2023	-1.0%	-2.3%	2.8%
2024	1.7%	-0.1%	3.4%
2025	1.6%	0.3%	3.2%

Note: Figures for 2023, 2024 and 2025 are projections.

Source: NiGEM and LINDA.

Increasing Earnings Inequality

Figure 2.1 Year-on-year real earnings growth for the lowest and median earners



Notes: The chart shows the annual changes in real earnings (pay) for both the bottom 10 per cent and median earners. The trajectories track relative growth in labour income between the two categories of households, but not necessarily convergence in individual labour incomes.

Source: ONS PAYE Real Time Information (July 2023).

Regional Variation in Real Wage Growth

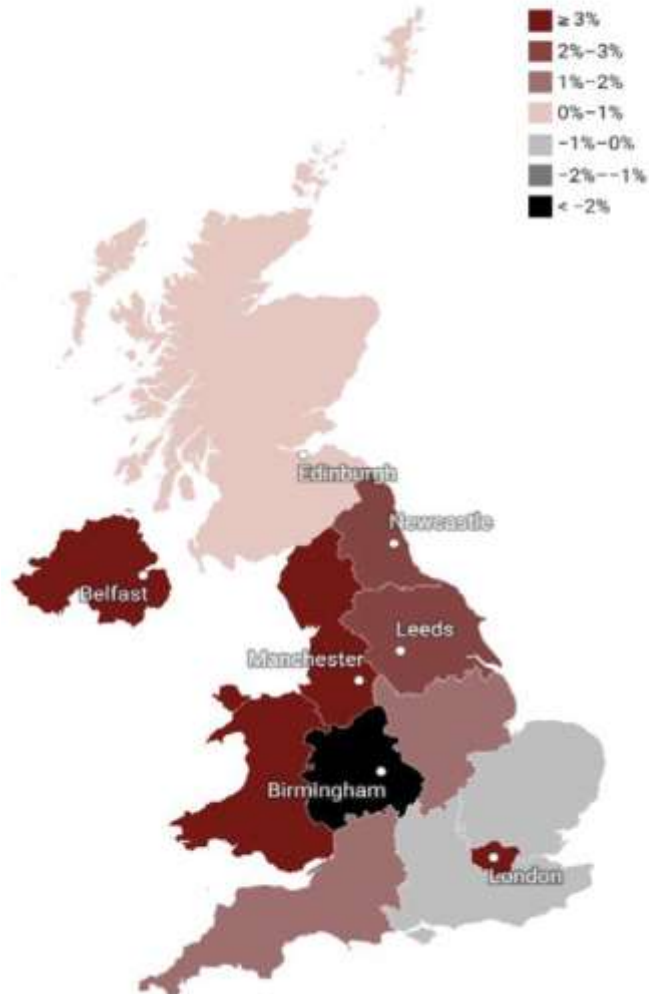
- Widening disparity between the prosperous and the poorer parts of the country
- In London real wages will have grown by up to 7% between 2019Q4 and 2024Q4
- In the West Midlands we are projecting a 5% fall in real wages over the same period

Regional Variation in Real Wages

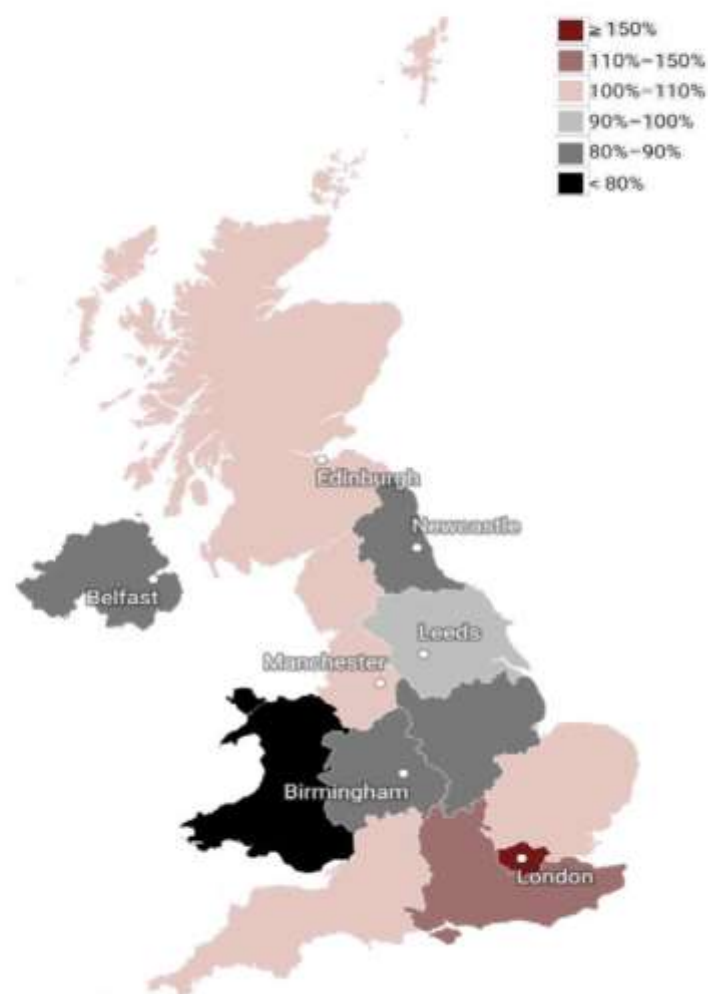
Date	Projected growth of real wages (2024Q4 over 2019Q4)	Projected median real wage levels 2024Q4 (relative to UK median)
North East	2.7%	81.8%
North West	3.1%	103.9%
Yorkshire and the Humber	2.5%	93.0%
East Midlands	1.1%	88.1%
West Midlands	-5.0%	84.7%
East	-0.5%	108.5%
London	7.2%	256.2%
South East	-1.0%	125.2%
South West	1.4%	105.1%
Wales	4.6%	79.4%
Scotland	0.8%	108.1%
N. Ireland	4.0%	87.4%

Regional Real Wage Projection

Post-Pandemic Growth
(2019Q4 to 2024Q4)



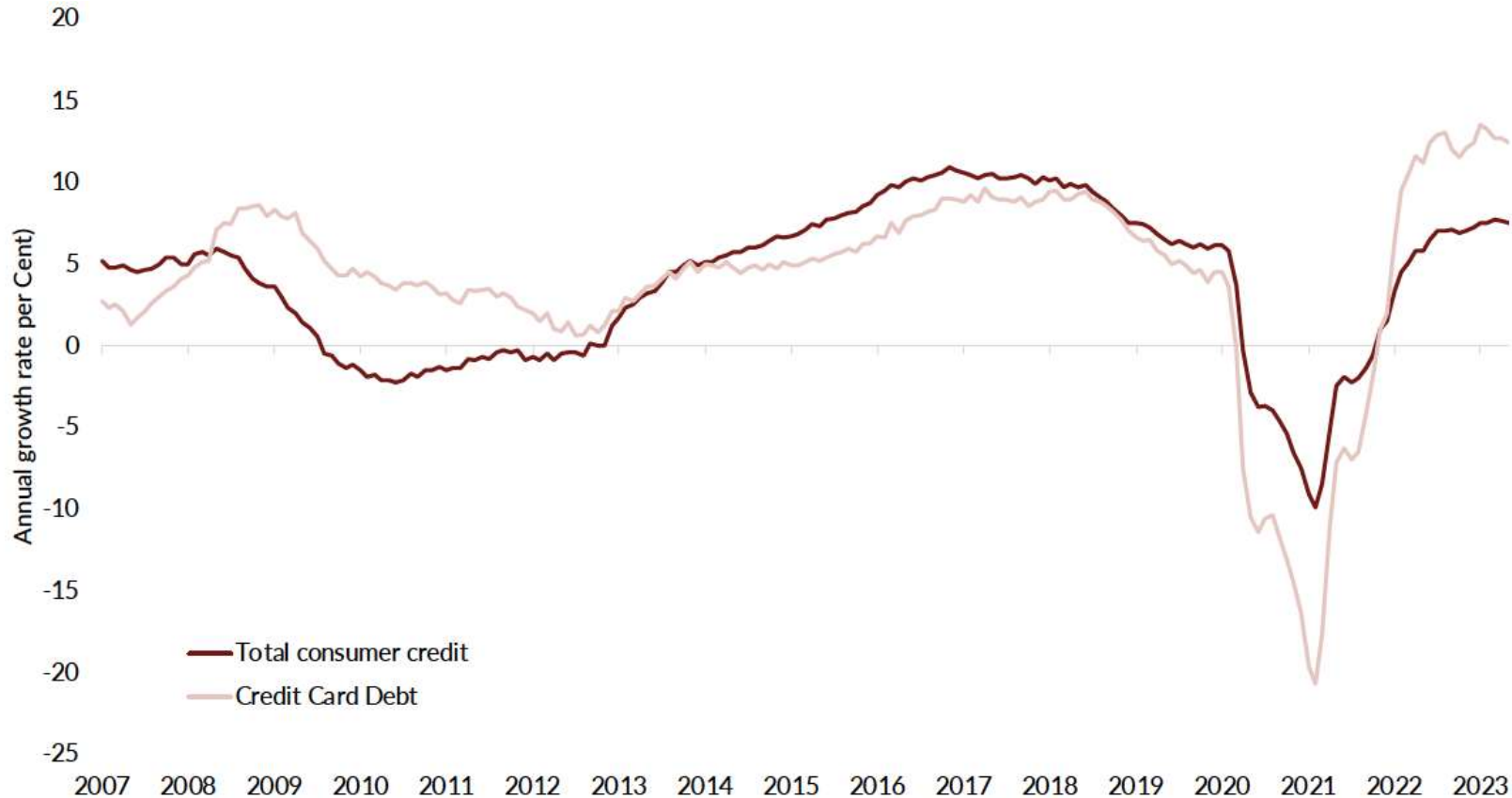
Median Real Wages in 2024
(Relative to the UK Median)



Source: NiGEM and LINDA

Unsecured Debt

Figure 2.4 Consumer credit growth rate

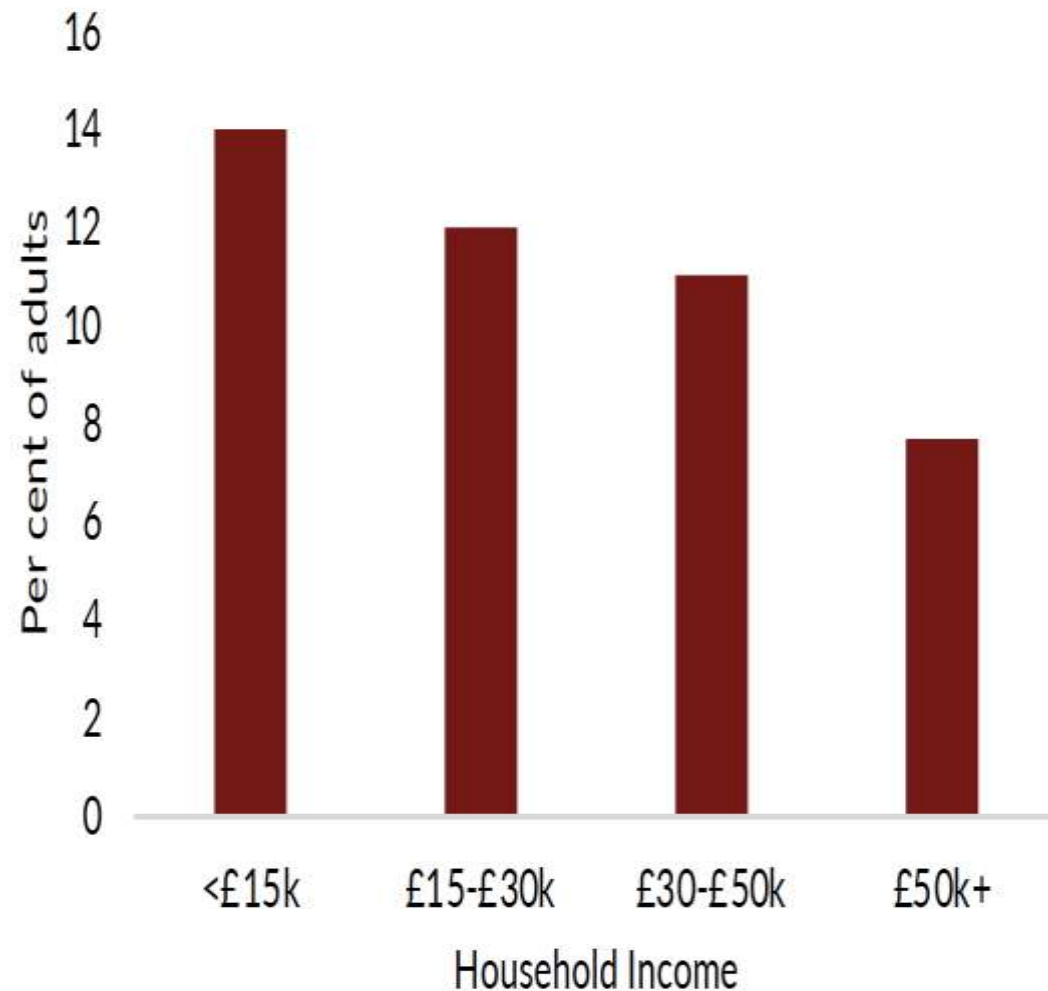


Source: Bank of England

- Total amount of unsecured debt is approx. £300 billion
- Average interest rate is around 20% for credit card debt, which covers around 30 per cent of unsecured debt
Payday loans – 110% !

Unsecured Debt

Figure 2.5 Use of high-cost credit



- 1.6 million low-income households hold high-cost loans
- They spend on average £3,200 per year (£267 per month) to pay back the debt and service interest rates averaging 76 per cent

Source: FCA Financial Lives Survey (2022)

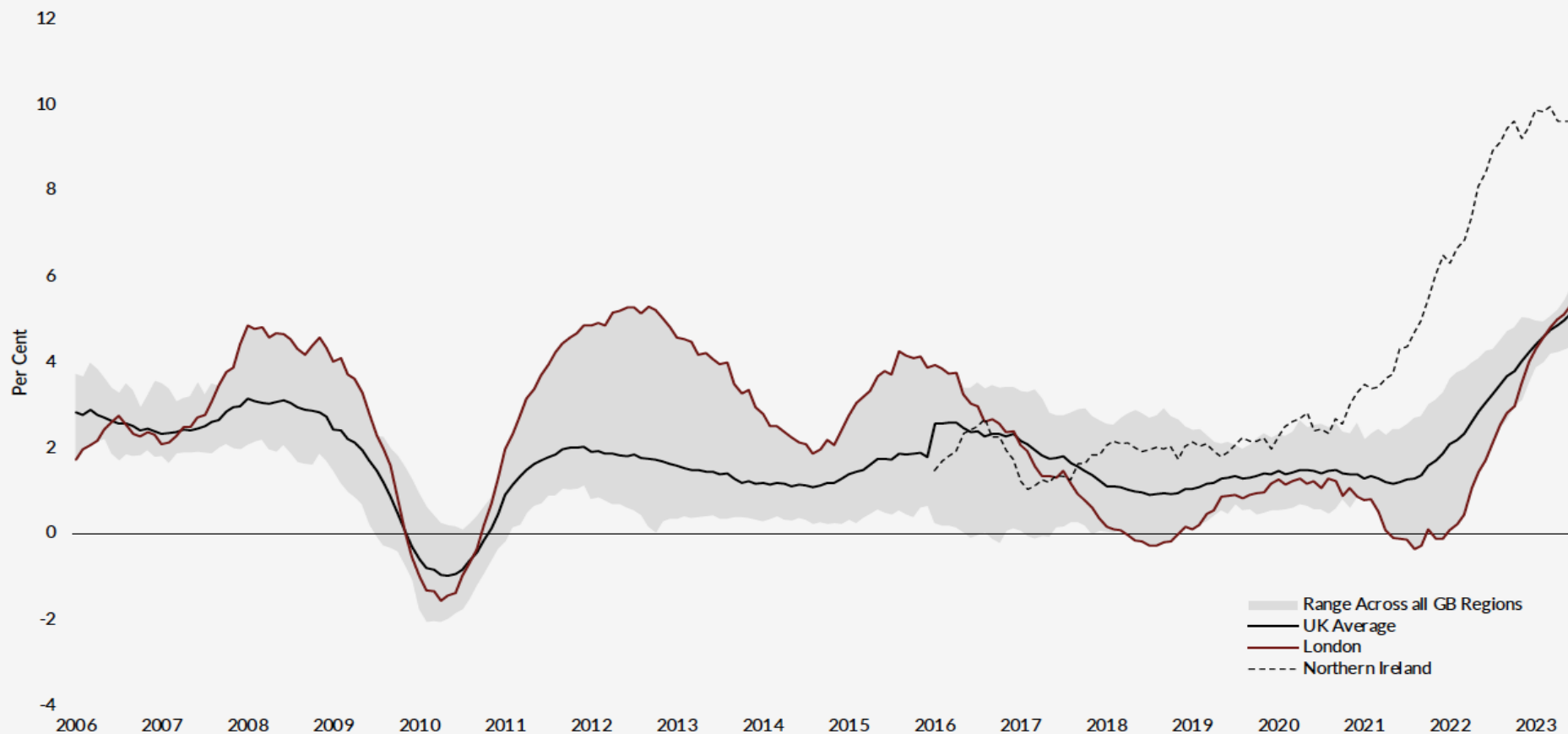
Spotlight on Housing Costs: Mortgages

- For 3 million households nearing the end of their fixed-rate deals, average mortgage interest costs have shot up since 2022

e.g., a household borrowing £300,000 on a 25-year mortgage would now face a 50 per cent rise in monthly repayments – from £1,200 to £1,800 – as a consequence of interest rates increasing from 2 per cent to now 5.25 per cent

Spotlight on Housing Costs: Rents

Figure S3 Annual percentage change in private housing rental prices across the UK



- Rents have risen by at least 5.1 per cent over the past year

Notes: The data is not seasonally adjusted. Wales is included in the UK average from 2010 onwards, Scotland from 2012 onwards and Northern Ireland from 2016 onwards. Northern Ireland data is not included for last two months because it is an outlier. The latest two monthly estimates are provisional and subject to revision in line with IPHRP's revision policy.

Source: ONS

Forbearance to Help Mortgage Holders

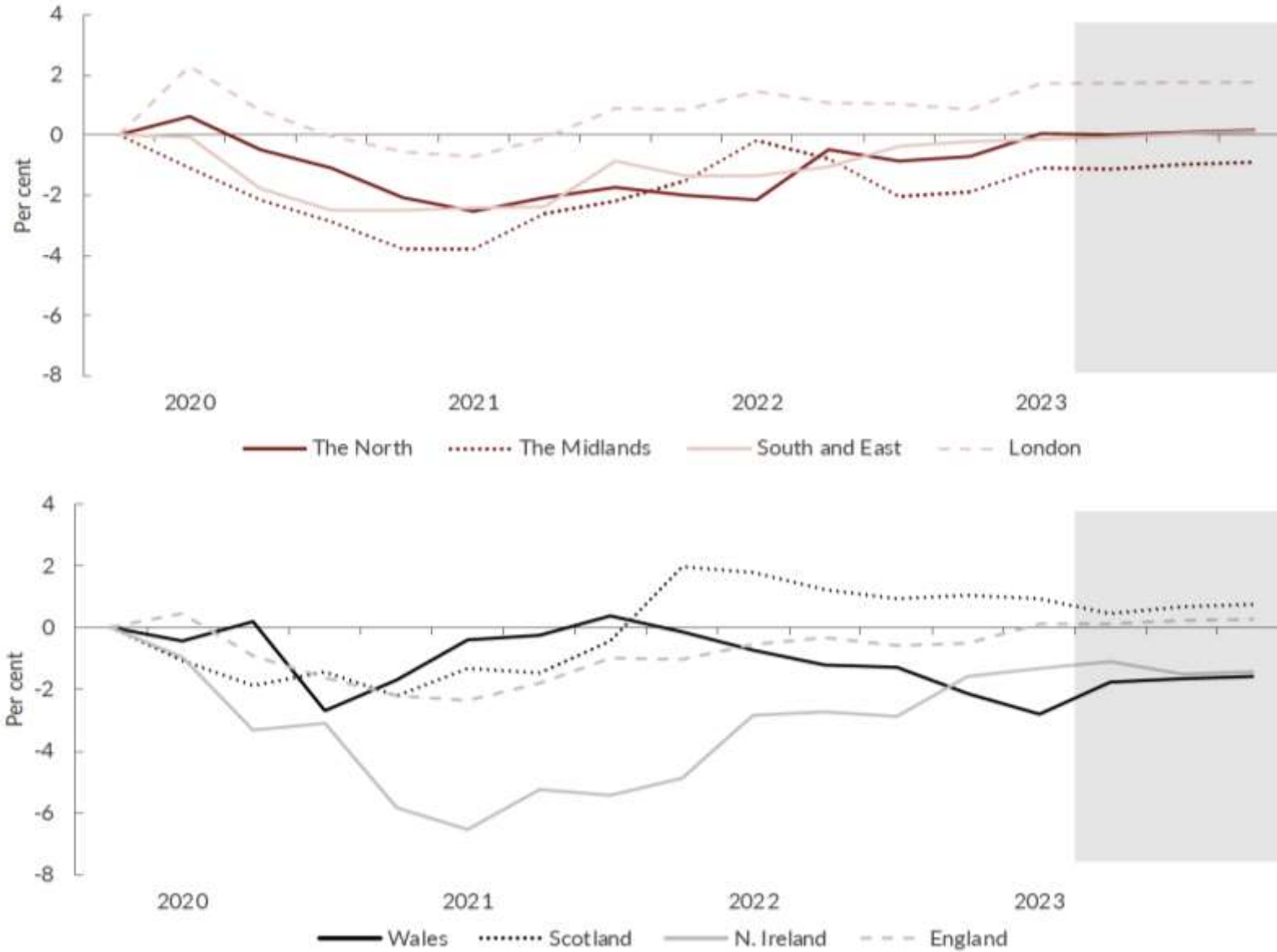
- Like inflation, fast-rising interest rates are a temporary phenomenon
- Mortgage holders are expected to withstand a 3-percentage point rise in the short-term, not a 5-percentage point rise
- Forbearance should be extended, for macroprudential reasons as much as for reasons of equity

Key Messages on the UK Regions

1. Divergence between prosperous and poor parts of the United Kingdom in terms of productivity
2. Despite a robust UK labour market, unemployment and inactivity are rising in Wales
3. Only Scotland and London are above pre-pandemic levels of employment
4. Unemployment is falling in Northern Ireland, the North East and Yorkshire and the Humber, but inactivity is higher almost everywhere

Regional Employment

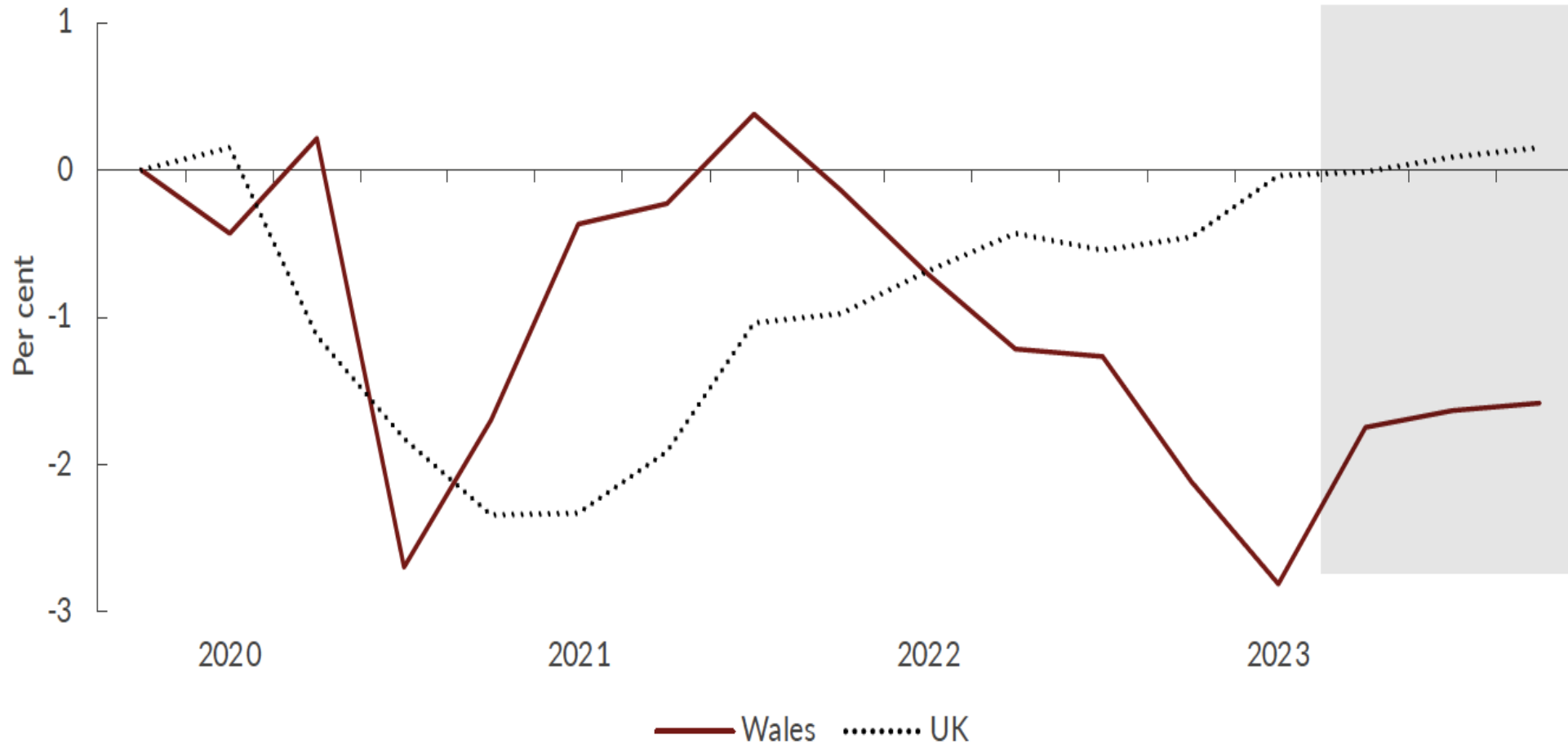
Figure 2.7 Employment levels relative to the fourth quarter of 2019



Source: NiReMS

Welsh Employment

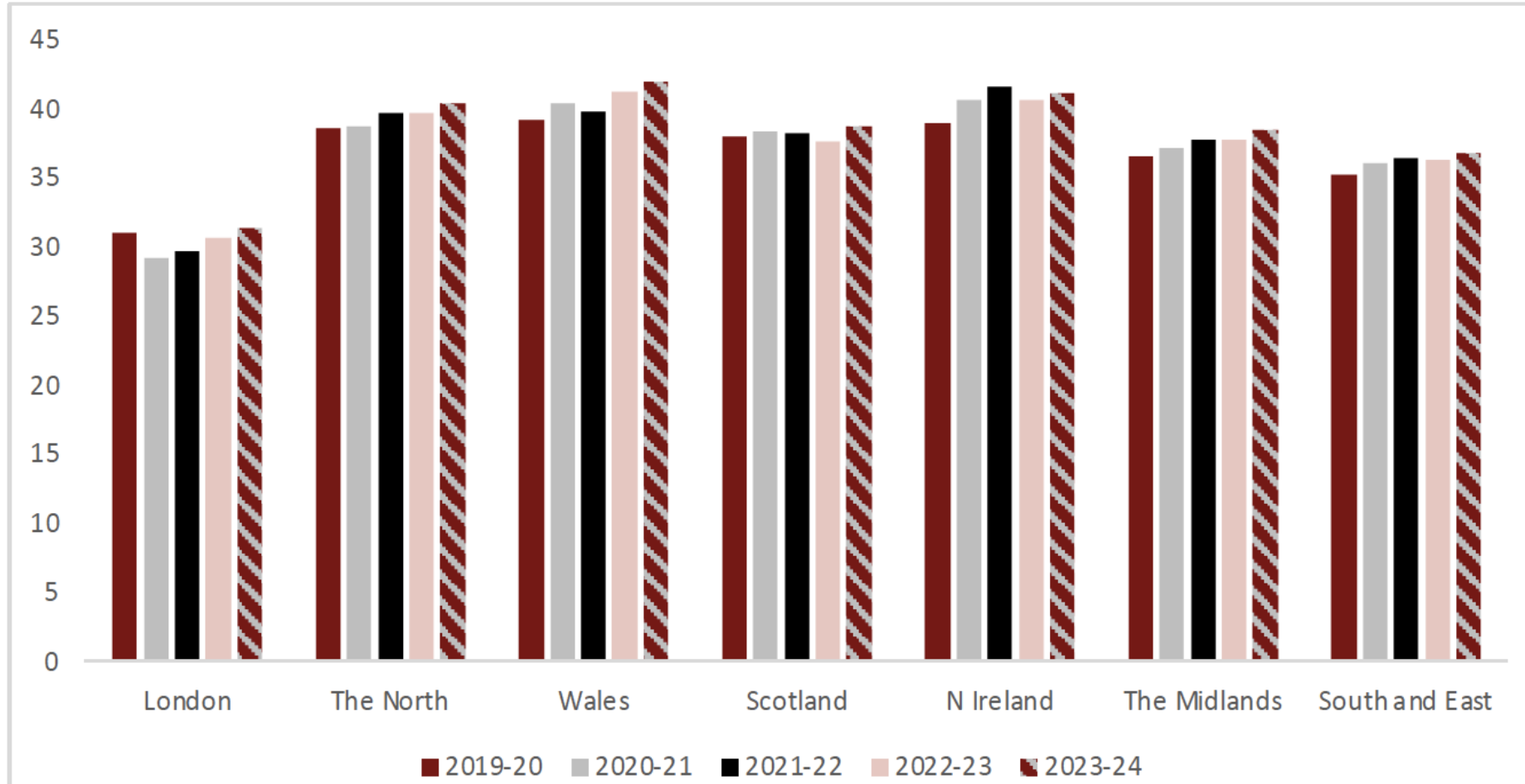
Figure 2.15 Employment in Wales relative to the fourth quarter of 2019



Source: NiReMS

Regional Inactivity

Figure 2.8 Devolved nation and regional inactivity rates

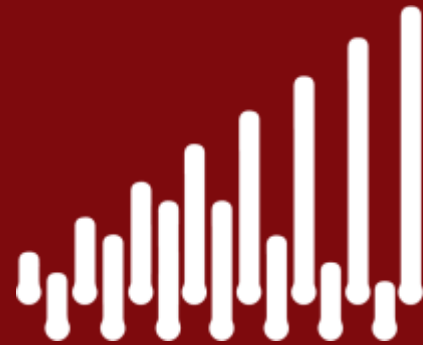


Note: Inactivity rate defined as labour force/population aged over 16.

Source: NiReMS.

Conclusion

1. Households in the bottom half of the distribution require sustained real wage growth
2. Housing costs are fast becoming a major burden, coupled with the rise in unsecured debt
3. Regional employment and inactivity require targeted intervention
4. Whither 'Levelling Up'?



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