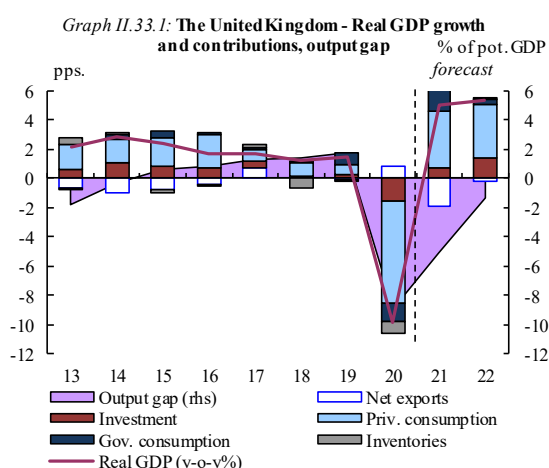


33. THE UNITED KINGDOM

After falling by 9.8% in 2020 as a consequence of the COVID-19 pandemic and the policy measures taken to contain it, UK GDP is projected to rebound in 2021 and 2022. While the first quarter of 2021 is forecast to be negative due to the lockdown, GDP is expected to pick up quickly in the second quarter as restrictions are eased and consumption rebounds. Slower but sustained growth is then projected over the forecast period, though the UK's departure from the EU is expected to weigh on trade and growth.

A subdued start in 2021

After falling by 19.5% in the second quarter of 2020 as a consequence of strict lockdown measures implemented to contain the first wave of the pandemic, UK GDP partially rebounded by 16.9% in the third quarter. To contain a second wave of the pandemic, another lockdown was introduced for the month of November, and GDP growth slowed to 1.3% in the fourth quarter of 2020. Overall, real GDP in 2020 fell by 9.8%, mainly due to a fall in private consumption.



After a sharp increase in the prevalence of COVID-19 cases in December 2020, the government tightened restrictions again significantly at the end of December. This third lockdown, which was only partially eased on 8 March with the re-opening of schools, weighed on output in the first quarter of 2021.

Shortly before the end of 2020, the UK and the EU signed the Trade and Cooperation Agreement (TCA). While the TCA provides for zero tariffs and zero quotas for all goods complying with the appropriate rules of origin, the UK leaving the European Union has inevitably created significant non-tariff barriers (NTBs). This became evident in early 2021 when UK trade volumes with the EU fell sharply. While some of these disruptions will

be temporary, as businesses get used to the new rules, UK trade is expected to remain permanently lower over the forecast period as compared to a situation with unchanged EU-UK trading relations.

Growth to pick up in 2021 and 2022

As the prevalence of COVID-19 cases falls, the restrictions imposed at the end of 2020 are being gradually eased. At the same time, the roll-out of vaccinations has progressed rather quickly; by end April, 51% of the population had received one dose of vaccine, and more than 20% were fully vaccinated. If cases continue to fall and vaccinations continue as planned, an almost full lifting of restrictions is foreseen for end June.

Private consumption is expected to pick up quickly as restrictions are being eased and pent-up demand is released, though an increase in unemployment when the furlough scheme finishes at the end of September 2021 is expected to temper private consumption slightly. Business investment is forecast to pick up more strongly in the second half of 2021 and in 2022, as uncertainties regarding the further evolution of the pandemic and the new EU-UK trade relationship fade away. In addition, the 'super-deduction' announced in the March 2021 budget, which allows businesses to offset 130% of eligible investment spending, is expected to have a positive impact on business investment over the forecast period. Government consumption is forecast to contribute positively particularly in 2021. Net exports are projected to be a drag on growth over the forecast horizon, as imports are expected to recover more quickly than exports. This would also cause the current account deficit to increase to around 5% of GDP over the forecast horizon. Overall, GDP is expected to increase by 5.0% in 2021 and by 5.3% in 2022. It is set to recover to pre-pandemic levels by the third quarter of 2022.

Unemployment to increase in 2021 as furlough scheme comes to an end

Government measures supporting employees and the self-employed are expected to keep unemployment relatively low until the third quarter of 2021. Unemployment is then expected to increase, as not all of the employees still on the furlough scheme are expected to return to their jobs. The unemployment rate in 2021 is projected to increase from 4.4% in 2020 to 5.6% in 2021 and to 5.9% in 2022.

Consumer price inflation is forecast to increase to 1.6% in 2021 and 1.8% in 2022. Reasons for this include higher energy prices and an increase in the tariff cap for natural gas and electricity; and higher service prices, as VAT cuts for food and accommodation services are gradually being phased out.

General government deficit to fall from record high as economy recovers

The general government deficit is expected to fall from 12.3% in 2020 to 11.8% of GDP in 2021 and to 5.4% in 2022 as the economy recovers. Government fiscal measures to deal with the consequences of the pandemic in 2020-2021 amounted to around 16% of GDP and include

income support for employees and self-employed workers, support for businesses and increases in welfare spending. The government also announced liquidity measures of about 16% of GDP, creating contingent liabilities. The main measures from the latest budget in March 2021 to be implemented in the forecast years are the previously mentioned 'super-deduction' and the freezing of the income tax personal allowance from April 2022.

The general government debt-to-GDP ratio increased to above 100% in 2020 as a consequence of the additional fiscal measures and the fall in GDP. It is expected to exceed 100% over the forecast horizon, at 108.1% in 2021 and 108.4% in 2022.

To support the economy during the pandemic, the Bank of England lowered its official Bank Rate to 0.1% in March 2020 and increased the total target stock of asset purchases to GBP 895 billion by November 2020. In February 2021, the Bank of England also instructed lenders to prepare for the possibility of negative interest rates as of autumn 2021, to broaden the monetary toolkit. However, given the economic and inflation outlook, monetary policy is expected to remain unchanged over the forecast horizon.

Table II.33.1:

Main features of country forecast - UNITED KINGDOM

	2019			Annual percentage change						
	bn GBP	Curr. prices	% GDP	01-16	2017	2018	2019	2020	2021	2022
GDP	2218.4	100.0		1.7	1.7	1.3	1.4	-9.8	5.0	5.3
Private Consumption	1420.3	64.0		1.9	1.1	1.4	1.1	-10.9	6.4	5.9
Public Consumption	423.1	19.1		2.0	0.7	0.6	4.0	-6.5	11.9	1.4
Gross fixed capital formation	399.5	18.0		1.7	2.8	0.4	1.5	-8.8	3.8	8.3
of which: equipment	81.1	3.7		1.6	0.9	-5.5	-2.6	-11.5	5.7	9.7
Exports (goods and services)	689.3	31.1		2.5	5.4	3.0	2.7	-15.8	0.9	5.8
Imports (goods and services)	716.7	32.3		3.1	2.6	2.7	2.7	-17.8	7.7	6.2
GNI (GDP deflator)	2203.0	99.3		1.6	3.0	1.2	2.1	-10.9	5.3	5.5
Contribution to GDP growth:										
Domestic demand				1.9	1.4	1.1	1.7	-9.8	7.3	5.4
Inventories				0.0	0.2	-0.6	-0.1	-0.8	0.0	0.0
Net exports				-0.2	0.7	0.1	-0.1	0.8	-1.9	-0.2
Employment				0.9	1.0	1.2	1.1	-0.3	-0.9	0.1
Unemployment rate (a)				6.0	4.3	4.0	3.8	4.4	5.6	5.9
Compensation of employees / head				3.1	3.0	2.6	4.2	1.7	0.9	2.8
Unit labour costs whole economy				2.2	2.3	2.5	3.9	12.4	-4.7	-2.4
Real unit labour cost				0.2	0.3	0.3	1.7	6.4	-5.5	-2.0
Saving rate of households (b)				8.9	5.7	6.1	6.5	15.7	10.6	5.8
GDP deflator				2.0	1.9	2.2	2.1	5.6	0.8	-0.4
Harmonised index of consumer prices				2.1	2.7	2.5	1.8	0.9	1.6	1.8
Terms of trade goods				0.4	-0.9	0.8	0.5	-2.6	0.0	0.0
Trade balance (goods) (c)				-5.5	-6.5	-6.4	-5.9	-5.4	-6.6	-6.3
Current-account balance (c)				-3.3	-3.8	-3.7	-3.1	-3.5	-5.0	-4.8
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-3.3	-3.8	-3.8	-3.1	-3.6	-5.0	-4.9
General government balance (c)				-4.7	-2.4	-2.2	-2.3	-12.3	-11.8	-5.4
Cyclically-adjusted budget balance (d)				-4.4	-3.1	-3.0	-3.3	-7.4	-9.0	-4.7
Structural budget balance (d)				:	:	:	:	:	:	:
General government gross debt (c)				59.9	86.3	85.8	85.2	102.0	108.1	108.4

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.