

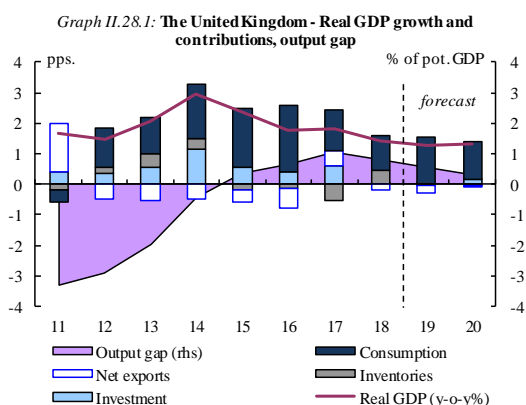
28. THE UNITED KINGDOM

Outlook remains subdued as uncertainty continues

UK GDP growth slowed markedly in 2018 and is forecast to remain subdued over the forecast horizon. Private consumption growth should find support from modest real wage growth but continuing uncertainty about the UK's future relationship with the EU27 means that business investment is likely to remain weak. With external demand moderating, net trade is not expected to contribute positively to GDP growth. Employment growth is expected to slow, leading to a broadly stable unemployment rate. Inflation should ease in 2019 before increasing slightly in 2020.

GDP growth slowed markedly in 2018

Annual UK GDP growth slowed from 1.8% in 2017 to 1.4% in 2018 due to a range of factors including falling business investment and slowing external demand. In 2018, business investment fell for four consecutive quarters – the first such instance since 2009, culminating in a year-on-year fall of 2.5% in 2018-Q4. Survey evidence suggests that this fall was largely due to the impact of uncertainty over the UK's future trading relationship with the EU.



While private consumption continued to make the largest contribution to GDP growth in 2018, it grew at the slowest pace (1.7%) since 2012 as the impact of subdued consumer confidence offset rising real wages. Net exports made a negative contribution (-0.2 pps) to GDP growth in 2018, as the impact of sterling's depreciation in 2016 faded and growth in the UK's export markets moderated, notably in advanced economies, which comprise a high share of UK exports.

Domestic demand to support modest GDP growth in 2019 and 2020.

Official GDP data for the first two months of 2019 indicate that GDP growth remained resilient in the first quarter of 2019. Evidence from a range of business surveys suggests that due to the

uncertainty over the timing and nature of the UK's exit from the EU, stockpiling by UK manufacturers supported growth in 2019-Q1. However, output growth in the second quarter of 2019 is likely to be constrained, as the elevated pace of inventory building is unwound.

Given the ongoing ratification process of the Withdrawal Agreement in the UK, projections for 2019 and 2020 are based on a purely technical assumption of status quo in terms of trading relations between the EU27 and the UK. This is for forecasting purposes only and has no bearing on future negotiations between the EU and the UK.

In 2019, moderate private consumption growth is projected to be supported by modestly increasing real wage growth and an expansionary fiscal policy. Acting against this, recent consumer confidence surveys suggest that savings intentions of consumers are high, reflecting weak overall consumer confidence. Consequently, over the forecast horizon, households are expected to maintain their savings at broadly constant levels. Business investment growth is projected to continue to fall as uncertainty persists over the UK's future trading relationship with the EU. However, the decline in business investment will be partly offset by strong public investment in 2019. The net exports' contribution to growth is expected to remain negative as external demand slows. Reflecting these factors and the technical assumption about UK trade relations with the EU27, GDP growth is forecast to remain weak at 1.3% in 2019.

In 2020, GDP growth is projected to be stable at 1.3% as the expected improvement in the contribution of net trade to growth, from negative to neutral, should be offset by slower government consumption growth. Private consumption growth is expected to moderate slightly as the effect of fiscal policy stimulus eases, while investment growth should recover but remain weak.

Employment growth to slow, inflation to remain stable

In 2019 employment growth is expected to slow in a context of subdued GDP growth and to stabilise in 2020. This is projected to lead to a broadly stable unemployment rate of 4.1% in 2019 and 4.2% in 2020. Consumer price inflation is expected to ease to 2.0% in 2019, from 2.5% in 2018, partly due to easing oil price inflation. Inflation is projected to rebound marginally to 2.1% in 2020 reflecting sustained wage pressures.

General government deficit to rise in 2019-2020

The UK's general government deficit is expected to rise to 1.5% of GDP in the 2019-2020 fiscal year, following several years of improvement in the budget balance. The deficit fell from 2.3% of GDP in 2016-2017 to 2.1% in 2017-2018 and is expected to have fallen to 1.3% in 2018-2019. The improvement in 2018-2019 was linked to both higher tax revenues and lower expenditure. Tax revenues, particularly income tax receipts, increased. Lower payments on inflation-linked bonds led to reduced interest payments on the government's outstanding debt. In line with the headline deficit, the structural deficit in 2018-2019

is expected to have fallen to around 1¼ % of GDP, from 2.7% in 2017-2018.

In 2019-2020, the general government deficit is expected to increase to 1.5% of GDP, before falling to 1.2% in 2020-2021. The rise in 2019-2020 is mainly due to policy decisions included in the 2018 Autumn Budget, which led to a net fiscal easing. This includes additional funding for the National Health Service, welfare spending, and an increase in the income tax personal allowance. Risks to the projected deficit are mainly to the downside, as pressures on public services have led to demands for increased spending. The structural deficit is expected to be broadly stable at 1¼ % of GDP for 2019-2020 and to fall to 1¼ % of GDP in 2020-2021. The general government debt ratio is projected to fall from 85.4% of GDP in 2018-2019 to 83.8% of GDP in 2019-2020 and to 82.7% of GDP in 2020-2021.

Table II.28.1:

General government projections on a financial-year basis

ESA10	Actual		Forecast		
	2016-17	2017-18	2018-19	2019-20	2020-21
General government balance-	-2.3	-2.1	-1.3	-1.5	-1.2
Structural budget balance	-2.8	-2.7	-1.7	-1.7	-1.3
General government gross debt	86.4	85.4	85.4	83.8	82.7

-APF transfers included

Table II.28.2:

Main features of country forecast - UNITED KINGDOM

	2017			Annual percentage change						
	bn GBP	Curr. prices	% GDP	99-14	2015	2016	2017	2018	2019	2020
GDP	2049.6	100.0		1.9	2.3	1.8	1.8	1.4	1.3	1.3
Private Consumption	1347.0	65.7		2.0	2.6	3.1	2.1	1.7	1.8	1.7
Public Consumption	375.2	18.3		2.3	1.4	0.8	-0.2	0.4	2.2	0.8
Gross fixed capital formation	351.3	17.1		1.5	3.4	2.3	3.5	0.2	-0.2	0.8
of which: equipment	87.4	4.3		2.0	5.2	2.0	-2.7	-4.5	-4.0	0.4
Exports (goods and services)	617.5	30.1		3.2	4.4	1.0	5.6	0.1	2.3	2.5
Imports (goods and services)	641.5	31.3		3.7	5.5	3.3	3.5	0.7	2.9	2.5
GNI (GDP deflator)	2026.1	98.8		1.7	2.1	1.5	3.2	1.3	1.3	1.3
Contribution to GDP growth:										
Domestic demand				2.2	2.9	2.6	1.9	1.2	1.5	1.4
Inventories				0.0	-0.2	-0.1	-0.5	0.4	0.0	0.0
Net exports				-0.2	-0.4	-0.7	0.5	-0.2	-0.3	0.0
Employment				0.9	1.7	1.5	1.0	1.2	0.8	0.8
Unemployment rate (a)				6.1	5.3	4.8	4.4	4.0	4.1	4.2
Compensation of employees / head				3.4	1.1	2.8	3.1	2.7	3.1	3.2
Unit labour costs whole economy				2.3	0.5	2.5	2.2	2.5	2.6	2.6
Real unit labour cost				0.3	0.1	0.4	0.0	0.6	0.7	0.6
Saving rate of households (b)				8.7	9.4	6.7	4.2	4.5	4.2	4.1
GDP deflator				2.0	0.4	2.1	2.2	1.9	1.9	2.0
Harmonised index of consumer prices				2.1	0.0	0.7	2.7	2.5	2.0	2.1
Terms of trade goods				0.3	-1.7	2.8	0.6	0.3	0.9	0.9
Trade balance (goods) (c)				-5.1	-6.2	-6.7	-6.7	-6.5	-6.7	-6.6
Current-account balance (c)				-3.1	-4.9	-5.2	-3.3	-3.9	-3.7	-3.4
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-3.1	-5.0	-5.3	-3.4	-4.0	-3.8	-3.5
General government balance (c)				-4.1	-4.2	-2.9	-1.9	-1.5	-1.5	-1.2
Cyclically-adjusted budget balance (d)				-3.8	-4.4	-3.3	-2.4	-2.0	-1.8	-1.4
Structural budget balance (d)				-	-4.4	-3.2	-2.4	-2.0	-1.8	-1.4
General government gross debt (c)				54.2	87.9	87.9	87.1	86.8	85.1	84.2

(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.