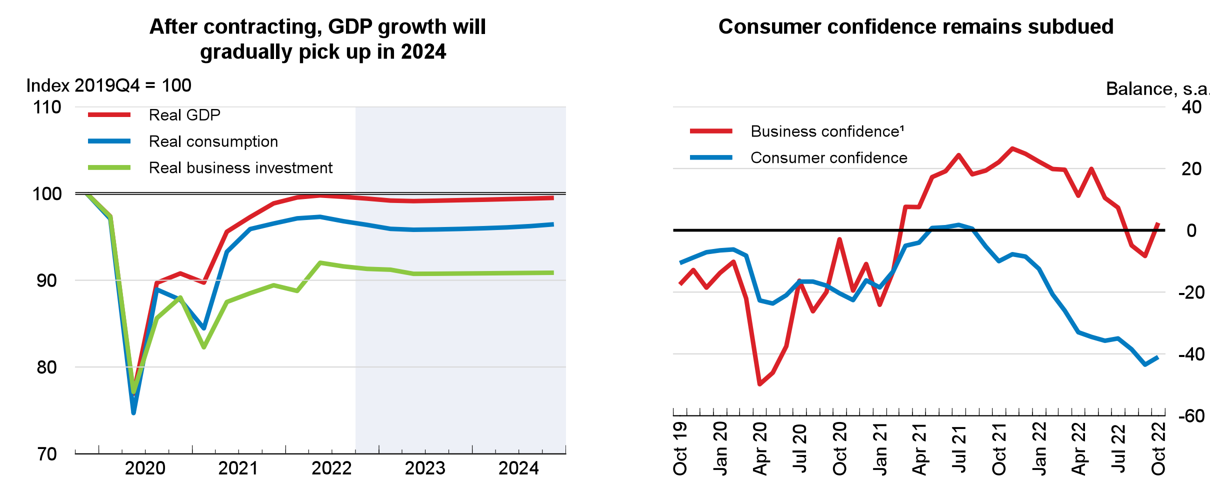
United Kingdom

Following a contraction of 0.4% in 2023, GDP is projected to increase by 0.2% in 2024. Consumer price inflation will peak at around 10% in late 2022 due to high energy prices and continuing labour and goods supply shortages, before gradually declining to 2.7% by the end of 2024. Private consumption is expected to slow owing to rising living costs, but will be aided by a 9.7% increase in the minimum wage and the usual uprating of welfare benefits and pensions in April 2023. Public investment is set to rebound in 2023 and 2024 as supply bottlenecks ease, in line with government plans. The unemployment rate is expected to rise to 5% by the end of 2024.

Complying with the fiscal plan and ensuring that future changes to fiscal targets follow a transparent and clearly defined process would maintain fiscal policy credibility and mitigate concerns about debt sustainability. The untargeted Energy Price Guarantee announced in September 2022 by the government will increase pressure on already high inflation in the short term, requiring monetary policy to tighten more and raising debt service costs. Better targeting of measures to cushion the impact of high energy prices would lower the budgetary cost, better-preserve incentives to save energy, and reduce the pressure on demand at a time of high inflation.

United Kingdom 1



1. Business confidence in the manufacturing sector.
Source: OECD Economic Outlook 112 database; and OECD Main Indicators database.

StatLink https://stat.link/cnz35u

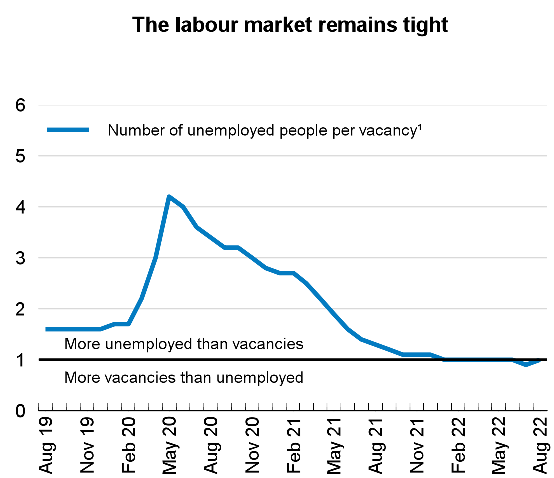
United Kingdom: Demand, output and prices

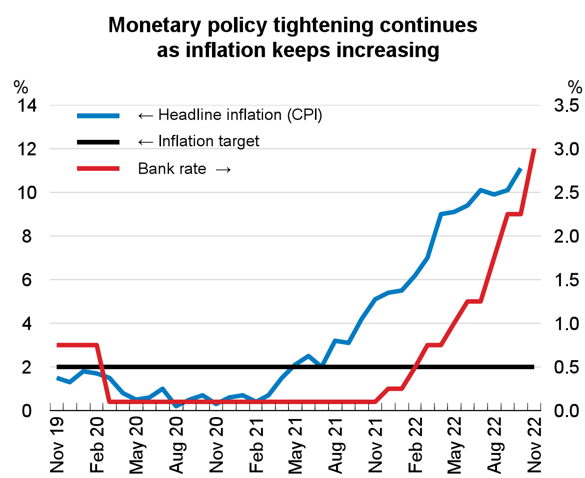
United Kingdom	2019	2020	2021	2022	2023	2024
	Current prices GBP billion	Percentage changes, volume (2019 prices)				
GDP at market prices	2 238.3	-11.0	7.5	4.4	-0.4	0.2
Private consumption	1 440.0	-13.2	6.2	4.7	-1.1	0.3
Government consumption	425.6	-7.3	12.6	1.6	2.3	0.6
Gross fixed capital formation	403.4	-10.5	5.6	5.6	1.0	1.3
Final domestic demand	2 269.0	-11.6	7.5	4.2	0.0	0.6
Stockbuilding[1]	5.5	-0.7	1.2	1.0	-2.2	0.0
Total domestic demand	2 274.5	-12.3	8.6	5.2	-2.1	0.6
Exports of goods and services	699.7	-12.1	-0.3	9.7	5.5	1.6
Imports of goods and services	735.8	-16.0	2.8	12.4	-0.5	2.5
Net exports[1]	- 36.1	1.5	-0.9	-0.9	1.9	-0.4
Memorandum items						
GDP deflator	_	5.9	0.4	4.8	4.7	2.5
Harmonised index of consumer prices	_	0.9	2.6	8.9	6.6	3.3
Harmonised index of core inflation[2]	_	1.4	2.4	6.2	6.4	3.4
Unemployment rate (% of labour force)	_	4.6	4.5	3.7	4.3	4.8
Household saving ratio, gross (% of disposable income)	_	15.8	12.5	7.9	7.6	7.5
General government financial balance (% of GDP)	_	-13.1	-8.2	-6.2	-7.6	-6.8
General government gross debt (% of GDP)	_	152.0	145.6	142.6	145.9	149.9
Current account balance (% of GDP)	_	-3.2	-2.0	-4.8	-3.5	-3.5

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/vzhcex

United Kingdom 2





1. UK vacancies excluding agriculture, forestry and fishing.
Source: ONS; OECD Economic Outlook 112 database; and Bank of England.

StatLink https://stat.link/yeopb9

Rising living costs weigh on economic growth

GDP growth has slowed and high-frequency indicators point towards a further deterioration in the outlook. Following growth of 0.7% in the first quarter of 2022 and 0.2% in the second, real GDP fell by 0.2% in the third quarter, as price growth outpaced wage growth, resulting in deteriorating household incomes. Annual CPI inflation reached 11.1% in October on the back of high energy prices and rising food prices and rising underlying inflation. Growth in average total pay picked up to 6% in the three months to September 2022, amidst labour market tightness, but real wages were down by 2.6%. In the third quarter, the unemployment rate of 3.6% fell below pre-pandemic levels, partially due to higher economic inactivity among 50 to 64 year-olds than before the pandemic. The number of vacancies remains high. Business sentiment picked up in October, following a period of deterioration driven by policy uncertainty and a worsening global outlook. Consumer confidence remained subdued after having fallen for several consecutive months amidst rapidly rising living costs.

The UK economy has limited direct trade linkages with Russia and Ukraine but is vulnerable to developments in the global energy market. Although Britain is not reliant on Russian exports, it imports gas and electricity from the continent during the coldest months. A particularly cold winter could risk supply disruptions, exposing the economy to rolling power cuts.

Monetary policy is set to tighten further but fiscal support is sizeable

The Bank of England has responded to rising inflation with monetary tightening, raising the policy rate from 0.1% in December 2021 to 3% by November 2022. It has also continued with quantitative tightening by no longer reinvesting the proceeds of gilt redemptions in new gilt purchases and gradually reducing its holdings of sterling corporate bonds until the end of 2023. From November 2022, the Bank of England started to sell government bonds to gradually reduce the GBP 838 billion stock that was built up since the global financial crisis. Monetary policy tightening is expected to continue, with the bank rate reaching 4.5% by Q2 2023 and remaining at that level throughout the projection period.

The government has introduced several support measures to help households and businesses to cope with rising energy prices. To protect households and businesses from high energy prices, the government introduced the Energy Price Guarantee and the Energy Bill Relief Scheme, which both are effective from October 2022 until end-March 2023. Households will benefit from the Energy Price Guarantee, which caps the cost per unit, with the government covering the difference to the market price. This new scheme, expected to cost about GBP 25 billion, will reduce the annual cost of electricity and gas for an average household with typical energy expenditure to around GBP 2 500 a year. On average usage, a household will save GBP 1 000 a year. Over the same period, gas and electricity prices will also be capped for businesses, charities and the public sector under the Energy Bill Relief Scheme, estimated to cost GBP 18 billion. This six-month long support for households and businesses together is estimated to cost about GBP 43 billion (1.9% of 2022 GDP). The government announced that for the fiscal year 2023/24, the cap of the Energy Price Guarantee will be raised to GBP 3 000 per year for the energy consumption of a typical household (worth about GBP 13 billion) and that the most vulnerable households will be aided with additional support to mitigate the rising cost of living. These measures for households and businesses come on top of support packages announced earlier in the year (worth GBP 37 billion) to help households, including a GBP 11.7 billion Energy Bills Support Scheme worth up to GBP 400 each for around 28 million households, as well as a GBP 150 disability cost-of-living payment and a GBP 650 cost-of-living payment for households on means-tested benefits. Moreover, the government reversed the 1.25 percentage points increase in national insurance contributions previously planned to take effect from November 2022. While most of the support package is debt financed, from April 2023, an increase in the corporate income tax rate from 19% to 25% and a decrease of the income threshold for taxation at the additional rate of 45% for higher earners from GBP 150 000 to GBP 125 140 will support the public finances. In 2023, the fiscal stance is expected to be slightly expansionary before tightening by 1.5 percentage points of potential GDP in 2024.

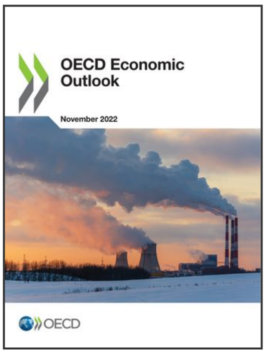
Economic activity will slow

Following a 4.4% expansion in 2022, GDP is projected to contract by 0.4% in 2023, and rise by just 0.2% in 2024. Inflation will remain above 9% into early 2023 before slowly falling to 4.5% by the end of 2023 and to 2.7% by the end of 2024. Reduced purchasing power and tighter monetary policy are expected to take a toll on consumer spending and rising long-term interest rates will lead to a slowdown in the housing market. Business investment will remain subdued over the projection period due to a higher cost of capital and lingering uncertainty. Continued tightness of the labour market is expected to push up wages, but wage growth is expected to remain below inflation over the projection period. Unemployment is set to gradually increase to 5% by the end of 2024 due to weaker demand. Public investment is expected to pick up from 2023 with planned spending increases on infrastructure and climate-related investment. The general government deficit is projected to decline from 7.6% of GDP in 2023 to 6.8% of GDP in 2024.

Risks to the outlook are considerable and tilted towards the downside. Higher-than-expected goods and energy prices could weigh on consumption and further depress growth. A prolonged period of acute labour shortages could force firms into a more permanent reduction in their operating capacity or push up wage inflation further. While households may seek to boost their real income by striking for stronger wage increases, they may also increase their labour supply either by returning from inactivity or by increasing working hours, which would be an upside risk. Further progress in trade deals could also support growth.

Raising productivity will be key to sustained growth

Fiscal support measures to help with high energy prices are warranted, but should ensure that incentives for energy reduction remain intact. Accelerating progress towards net zero is fundamental to enhance energy security and reduce dependence on fossil fuels. The policies in place are not yet sufficient to deliver the net zero target. The government can stimulate investment by being clearer about its approach to the transition to a net zero economy and developing an economy-wide plan with specific deadlines, policies and priorities, in line with a target-consistent emission pricing trajectory. To ensure sustainable growth, the government should also continue to implement its productivity enhancing “Plan for Growth” to support a shift towards greener and more inclusive growth through large-scale public investment in infrastructure, skills and innovation.



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