

# CBI Economic Forecast

- **UK GDP and the economic recovery** Our broad view of the UK economic outlook for 2010 is little changed since our September forecast. We still anticipate a fragile and weak recovery, with economic conditions remaining challenging going forwards, due to the absence of any strong driver of growth and the lingering impact of the financial crisis.

The recession is expected to end in the fourth quarter this year, as consumer spending rises in anticipation of the forthcoming VAT rise, but GDP growth subsequently falls back as a result early next year. By the second half of 2010 and into 2011, growth is expected to gradually gather pace. This reflects companies rebuilding their stocks, UK export growth improving with the strengthening global economic recovery, and household consumption also recovering.

Overall, we see UK GDP growth picking up from 1.2% in 2010 to 2.5% in 2011. However, despite two years of expansion, economic output will still not have return to its pre-recession level by the end of 2011, illustrating just how slow and anaemic the recovery is after such a deep recession.
- **Consumption** Levels of household spending will remain weak throughout 2010 due to rising unemployment, relatively weak wage growth, and the impact of households saving more and reducing levels of debt. Consumption is expected to recover over 2011, growing by 2.3%, as unemployment starts to fall back and income growth strengthens. Unemployment is likely come down fairly sluggishly however, after peaking slightly lower than previously forecast, at just over 2.8 million in the autumn next year.
- **Investment and Inventories** The prospects for capital investment continue to look weak over much of the forecast period. High levels of excess capacity and constraints on bank lending will inhibit expenditure by businesses. We forecast that business investment will fall a further 5.6% next year, before rising 2.7% in 2011.

Following the heavy rates of destocking this year, businesses will be rebuilding their inventories over the next two years, but at a very subdued pace initially, given concerns over the strength of demand and ongoing constraints surrounding access to finance.
- **UK Trade** The sizeable depreciation of sterling, coupled with a pick up in world demand will contribute to a modest rise in exports in 2010 and a stronger rate of growth in 2011, helping the current account deficit to shrink markedly over the forecast period.
- **Monetary Policy and Inflation** We continue to forecast that the Bank of England will start to raise interest rates in spring 2010, taking them up to 2% by the end of the year. This will withdraw some of the significant monetary stimulus currently in place, helping to lower the risks of undesirably high inflation in the medium term. However, we expect no further interest rates rises in 2011, as a retained degree of looseness in monetary policy will be needed to help sustain the economic recovery when the process of fiscal consolidation gets underway.

CPI inflation will rise sharply at the beginning of 2010 in response to the VAT increase, before easing back somewhat in 2010 and falling below target throughout 2011. The overall profile for CPI inflation has risen since our September forecast, mainly due to a higher oil price forecast. Indeed we now foresee prices nearing \$100 a barrel by the end of 2011, as global economic growth gathers pace in the face of relatively limited oil supply.

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12mth% unless otherwise stated	2009	2010	2011	2010 Q1	Q2	Q3	Q4	2011 Q1	Q2	Q3	Q4
<b>GROWTH &amp; CONSUMPTION</b>											
Real GDP	-4.5	1.2	2.5	0.1	1.0	1.7	1.8	2.3	2.5	2.5	2.6
Manufacturing output	-10.5	0.6	2.6	0.1	0.4	0.8	0.8	1.5	2.1	2.9	3.8
Household consumption	-3.1	0.4	2.3	-0.6	0.4	0.9	0.9	1.7	2.2	2.5	2.9
Government consumption	2.0	1.2	-1.4	1.9	1.3	1.1	0.4	-0.5	-1.7	-2.2	-2.2
Household savings ratio	5.2	6.4	5.9	6.2	6.5	6.5	6.4	6.1	6.0	5.8	5.9
<b>INVESTMENT</b>											
Fixed investment	-14.0	-3.7	2.9	-7.6	-2.4	-3.5	-1.0	1.1	2.0	3.6	5.1
of which:											
Total business	-18.8	-5.6	2.7	-14.9	-4.9	-1.6	0.5	1.9	2.3	2.9	3.7
General government	25.5	1.0	-21.3	17.9	9.7	-7.4	-12.6	-18.4	-21.9	-22.3	-22.8
Manufacturing	-20.2	-9.3	2.8	-24.3	-9.5	0.3	1.2	1.9	2.5	3.2	3.7
<b>EXTERNAL TRADE</b>											
Exports	-10.9	1.9	5.3	-0.2	2.0	2.4	3.3	4.3	5.0	5.7	6.3
Imports	-12.2	2.0	4.0	0.7	3.3	2.5	1.6	2.7	3.5	4.4	5.3
Current account (£bn)	-32.1	-28.1	-13.9	-7.4	-7.3	-7.0	-6.3	-5.4	-4.1	-2.8	-1.6
% of GDP	-2.3	-1.9	-0.9	-2.1	-2.0	-1.9	-1.7	-1.4	-1.1	-0.7	-0.4
<b>PRICES</b>											
CPI	2.1	2.3	1.7	2.7	2.3	2.0	2.0	1.9	1.5	1.7	1.8
RPI	-0.6	3.6	2.8	3.6	3.7	3.5	3.3	3.4	2.9	2.6	2.1
RPIX	2.0	2.7	2.2	3.7	3.0	2.4	1.8	2.2	2.1	2.3	2.4
Producer output prices	1.2	2.0	2.6	2.8	2.2	2.2	2.3	2.5	2.6	2.6	2.6
<b>LABOUR MARKET</b>											
Unemployment (ILO, mn)	2.45	2.77	2.64	2.68	2.79	2.82	2.78	2.73	2.66	2.61	2.57
Unemployment rate (%)	7.8	8.7	8.3	8.4	8.7	8.8	8.7	8.6	8.4	8.2	8.1
Unemployment (CC, mn)	1.58	1.81	1.74	1.76	1.83	1.83	1.80	1.78	1.75	1.72	1.70
Claimant count rate (%)	4.7	5.6	5.4	5.4	5.7	5.6	5.6	5.5	5.4	5.3	5.3
Employment (mn):	26.73	26.48	26.49	26.56	26.47	26.45	26.44	26.46	26.48	26.51	26.52
Average earnings inc. bonus	1.2	2.6	3.9	2.9	2.0	2.4	3.0	3.1	3.7	4.3	4.6
<b>PUBLIC SECTOR</b>											
Net borrowing (£bn)***	180.8	184.1	154.0								
% of GDP	12.8	12.5	10.0								
*** 2009/10, 2010/11, 2011/12											
<b>FORECAST ASSUMPTIONS</b>											
	2009	2010	2011	2010 Q1	Q2	Q3	Q4	2011 Q1	Q2	Q3	Q4
OECD GDP	-3.4	1.8	2.4	1.7	2.1	1.7	1.6	1.9	2.2	2.7	3.0
UK Bank Rate	0.65	1.25	2.00	0.50	1.00	1.50	2.00	2.00	2.00	2.00	2.00
Oil prices \$ per barrel	62.1	81.5	93.0	78.0	79.8	82.6	85.6	89.5	91.7	94.1	96.6
GBP Trade-weighted index	80.1	77.7	81.3	78.7	75.7	77.8	78.7	78.4	80.4	82.3	83.9
USD/GBP	1.57	1.60	1.64	1.62	1.58	1.60	1.61	1.61	1.63	1.66	1.68
EUR/GBP	1.12	1.09	1.14	1.08	1.08	1.10	1.11	1.11	1.13	1.15	1.17