

CBI Economic Forecast

- **Impact of the credit shock** The global economic outlook has deteriorated rapidly in the months since our November forecast, as the real economy impact of the banking crisis intensification post-Lehmans revealed itself to be far reaching and intense. A significant slowdown was already evident in the advanced economies, but this is being accelerated by dramatic falls in international consumer and business confidence, and the lack of available credit. Emerging market economies, which had previously shown a surprising degree of resilience, are now also suffering the effects of the global financial crisis and sharp downturn in demand. Industrial production has plummeted across many countries and world trade is falling rapidly too.

Economic prospects also look considerably weaker here in the UK, where access to credit has deteriorated further. A deep and prolonged recession is now expected. The stimulus measures implemented by the government and the Bank of England will take time to feed through, but will help the process of economic recovery which we expect to see next year.
- **GDP** Our new GDP forecast for 2009 is -3.3% compared with -1.7% in November. The quarterly profile shows six consecutive falls in output, with the UK economy contracting throughout this year. The cumulative fall in output is forecast to be 4.5%, which is far higher than in the early 1990s recession, but still below that of the early 1980s. A muted recovery in output growth is expected over the course of 2010 as the various stimulus measures take effect and credit flows are repaired.
- **Firms** Faced with rapid falls in demand and increased difficulties in accessing credit, businesses have been cutting back production and running down their stock levels. Firms are also scaling back their investment spending significantly and making heavy cuts to employment. We expect manufacturing output to fall steeply by 10.1% in 2009. We also forecast a 9.2% fall in business investment this year and a sharp rise in unemployment to just over 3 million by early 2010.
- **Households** The outlook for consumption has also weakened. We forecast a 2.7% fall in household spending in 2009 as unemployment rises and real disposable income declines. The household savings ratio is expected to rise throughout the forecast period in response to heightened concerns about job security and falling levels of wealth, caused by deflating asset prices.
- **OECD GDP and UK trade** The intensification of the global downturn has led us to lower our forecast for OECD GDP: we now expect it to fall by 2.2% this year. The sizeable contraction in our overseas markets is overwhelming the competitive gain from the recent significant depreciation in sterling. Consequently, the net trade contribution to GDP is forecast to be only very modestly positive this year.
- **Monetary policy and inflation** Since our November forecast the Bank Rate has been reduced from 3% to a record low 1%. Given the impaired nature of the monetary transmission mechanism we do not expect the Bank Rate to fall much further below this level. However, the Bank of England may need to undertake further, unconventional, monetary stimulus measures over the course of 2009 in order to tackle current deflationary forces. CPI inflation has already fallen back sharply from its peak in September, on the back of lower fuel prices and the December cut in VAT. We expect CPI inflation to fall further still, to a low of -0.1% in the third quarter of this year. The reversal of the VAT cut at the end of this year will push CPI inflation up again; however, we envisage that it will remain below the 2% target throughout the forecast period, mainly due to the sizeable build up of spare capacity and the resulting output gap.

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12mth% unless otherwise stated				2009				2010			
	2008	2009	2010	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
GROWTH & CONSUMPTION											
Real GDP	0.7	-3.3	0.0	-3.2	-3.9	-3.6	-2.3	-1.3	-0.3	0.4	1.3
Manufacturing output	-2.3	-10.1	0.7	-11.5	-11.7	-10.7	-6.3	-1.3	0.4	1.5	2.1
Household consumption	1.7	-2.7	-0.2	-2.1	-2.7	-3.3	-2.7	-1.7	-0.6	0.5	1.1
Government consumption	3.3	2.7	1.0	2.4	2.5	2.7	3.2	2.2	1.4	0.6	0.0
Household savings ratio	0.8	2.8	4.5	2.0	2.7	3.2	3.2	3.8	4.2	4.8	5.2
INVESTMENT											
Fixed investment	-4.1	-10.0	-2.5	-10.4	-11.5	-10.4	-7.8	-5.1	-3.3	-1.4	0.1
of which:											
Total business*	0.1	-9.2	-1.7	-7.2	-10.3	-10.9	-8.5	-5.4	-2.9	-0.2	1.9
General government*	16.7	10.0	-4.2	10.2	9.2	9.7	10.7	3.7	-2.1	-7.5	-10.3
Manufacturing*	-1.4	-8.8	0.7	-8.9	-8.8	-13.4	-3.7	-2.7	-1.3	2.9	4.2
* Exc. BNFL transfer											
EXTERNAL TRADE											
Exports**	0.9	-5.4	-1.3	-4.3	-5.3	-6.7	-5.5	-3.6	-2.1	-0.5	1.2
Imports**	0.9	-5.4	-0.8	-4.6	-5.2	-6.8	-4.9	-2.9	-1.3	-0.1	1.1
Current account (£bn)	-23.1	-24.3	-27.5	-5.1	-5.8	-6.5	-6.9	-6.7	-6.7	-7.0	-7.2
% of GDP	-1.6	-1.7	-1.9	-1.4	-1.6	-1.9	-2.0	-1.9	-1.9	-2.0	-2.0
** Inc. MTIC fraud											
PRICES											
CPI	3.6	1.0	1.2	2.5	0.9	-0.1	1.0	1.8	1.6	0.7	0.8
RPI	4.0	-2.9	1.7	-1.5	-3.6	-4.4	-2.2	1.6	2.2	1.3	1.6
RPIX	4.3	0.6	1.3	2.0	0.2	-0.8	0.9	1.6	1.5	0.9	1.2
Producer output prices	7.3	-0.2	2.0	2.8	-1.2	-2.1	0.1	0.7	1.2	1.4	1.6
LABOUR MARKET											
Unemployment (ILO, mn)	1.81	2.59	3.00	2.23	2.50	2.73	2.89	3.00	3.04	3.01	2.94
Unemployment rate (%)	5.8	8.2	9.4	7.1	7.9	8.6	9.1	9.4	9.6	9.5	9.3
Unemployment (CC, mn)	0.94	1.79	2.32	1.44	1.70	1.90	2.13	2.25	2.32	2.36	2.36
Claimant count rate (%)	2.8	5.5	7.2	4.4	5.2	6.0	6.6	6.9	7.1	7.3	7.3
Employment (mn):	27.32	26.56	26.04	26.84	26.63	26.47	26.30	26.14	26.03	25.99	25.99
Average earnings inc. bonus	3.5	1.7	1.8	2.5	2.0	1.1	1.3	1.3	1.6	2.0	2.5
PUBLIC SECTOR											
Net borrowing (£bn)***	88.7	148.7	168.1								
% of GDP	6.2	10.6	11.8								
*** 2008/09, 2009/10, 2010/11											
FORECAST ASSUMPTIONS											
	2008	2009	2010	2009	Q2	Q3	Q4	2010	Q2	Q3	Q4
OECD GDP	1.2	-2.2	0.7	-1.8	-2.4	-2.7	-1.8	-0.7	0.2	1.2	2.1
UK Bank Rate	4.63	1.04	1.00	1.17	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Oil prices \$ per barrel	97.4	43.8	56.3	40.0	40.0	45.0	50.0	52.5	55.0	57.5	60.0
GBP Trade-weighted index	91.0	76.1	84.9	76.5	75.4	75.9	76.5	80.5	82.9	86.3	89.8
USD/GBP	1.85	1.43	1.67	1.43	1.40	1.43	1.46	1.56	1.63	1.70	1.77
EUR/GBP	1.26	1.13	1.21	1.10	1.12	1.14	1.16	1.18	1.20	1.22	1.25