

CBI Economic Forecast

- **UK GDP**

After a particularly steep fall in output at the start of the year, the UK economy now looks to be stabilising, as many recent economic indicators have shown the pace of contraction diminishing markedly. Demand is no longer "falling off a cliff", firms have less need to run down their stocks as rapidly as before, and the confidence of businesses and consumers is noticeably less downbeat than a few months ago - when the economic outlook appeared extremely gloomy. With the process of stabilisation in the economy gaining traction over the months ahead, it is likely that we will see an end to the recession (i.e. GDP no longer falling) before the year is out - a little sooner than predicted in our April forecast.

However, the massive negative shock that we have had from the credit crunch will take time to dissipate, and it is difficult to see where there will be sources of solid and sustained demand growth in the economy over the next few quarters. Consequently we still believe that the economic recovery will not fully get off the ground until well into next year, and that it will be fairly slow and gradual. We forecast marginal quarterly growth at the start of 2010, with momentum building to around trend rate by the end of the year. For 2010 as a whole we predict modest GDP growth of 0.7%, following a GDP fall of 3.9% in 2009.
- **Firms**

Although demand in the economy is stabilising, it is doing so at a level that is considerably below that of a year ago, and many firms are faced with excess capacity. Business investment has already been cut back very sharply, but further falls are expected over the remainder of this year, albeit at much slower rates of decline. Business investment in 2009 is forecast to be down 12.4% on last year, and despite some modest quarterly growth in 2010, it is expected fall another 1.4%. The remarkable degree of flexibility in the labour market with regards to wage restraint (far exceeding anything seen in previous recessions) is likely to help limit the impact of the downturn on job losses. This has prompted us to lower our forecast for the peak in unemployment to just over 3 million in early 2010.
- **Households**

Weakness in household consumption is forecast to persist through 2009 in response to rising unemployment, downward pressure on earnings growth, and a preference for higher rates of saving than in previous years - as households seek to repair their balance sheets. A 2.9% fall in consumption is predicted this year. Consumption is expected to pick up a little next year, but with only very muted quarterly increases compared to the much stronger growth in spending that was achieved during the period of easy credit earlier this decade.
- **UK trade**

Exports and imports fell very sharply at the beginning of this year, when world trade was collapsing, and further falls are expected, such that double digit declines are forecast in 2009. Nevertheless, net trade is expected to contribute positively to GDP again this year, more so than in 2008. However, this is unlikely to last into next year, when consumer spending is gradually recovering along with demand for imports, and given the expectation of a further slight appreciation in sterling which will lower relative export competitiveness.
- **Inflation and monetary policy**

CPI inflation is now expected to fall below the Bank of England's 2% target in the third quarter this year, and less rapidly than forecast in April, mainly reflecting higher oil prices. However, we still predict that inflation will remain below target throughout the forecast period. In order to sufficiently bolster nominal demand for inflation to be close to target in the medium term, the Bank may need to further expand its quantitative easing programme from the current £125 billion in the coming months. Looking further ahead, as the economy is recovering next year, it is likely that the Bank will then be focussing its attention on how it retreats from such a highly accommodative monetary stance. We still expect that the Bank Rate will start to be raised from its 0.5% historical low early in 2010.

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12mth% unless otherwise stated	2008	2009	2010	2009 Q1	Q2	Q3	Q4	2010 Q1	Q2	Q3	Q4
GROWTH & CONSUMPTION											
Real GDP	0.7	-3.9	0.7	-4.4	-4.7	-4.1	-2.6	-0.3	0.3	0.9	1.7
Manufacturing output	-2.6	-11.6	1.4	-13.5	-13.6	-12.0	-7.2	-0.9	1.2	2.1	3.2
Household consumption	1.4	-2.9	0.5	-2.7	-3.3	-3.3	-2.3	-0.9	0.3	1.0	1.5
Government consumption	3.4	4.6	1.0	3.5	4.1	5.3	5.5	4.4	1.9	-0.1	-1.9
Household savings ratio	1.9	4.2	4.6	3.9	4.1	4.5	4.4	4.6	4.4	4.5	4.7
INVESTMENT											
Fixed investment	-3.1	-11.1	-0.5	-10.7	-12.5	-10.9	-10.3	-4.3	-1.0	0.8	2.7
of which:											
Total business	0.1	-12.4	-1.4	-9.2	-13.3	-13.8	-13.3	-5.6	-1.6	0.0	1.7
General government	21.1	1.5	2.0	-0.5	4.1	1.2	1.0	1.3	-0.7	2.3	5.3
Manufacturing	-1.8	-15.1	-2.4	-10.7	-14.0	-18.4	-17.4	-8.8	-3.3	0.8	2.3
EXTERNAL TRADE											
Exports	0.1	-11.1	0.1	-11.0	-11.9	-12.4	-8.9	-2.7	0.3	1.0	1.8
Imports	-0.6	-11.8	0.6	-13.1	-13.0	-13.2	-7.7	-1.2	0.4	1.3	2.0
Current account (£bn)	-24.5	-30.6	-41.3	-6.4	-7.2	-8.1	-9.0	-9.6	-10.0	-10.6	-11.2
% of GDP	-1.7	-2.2	-2.9	-1.8	-2.0	-2.3	-2.6	-2.7	-2.8	-2.9	-3.1
PRICES											
CPI	3.6	1.9	1.6	3.0	2.0	1.2	1.4	1.9	1.6	1.3	1.4
RPI	4.0	-1.2	2.1	-0.2	-1.6	-2.0	-0.9	1.2	2.0	2.2	2.8
RPIX	4.3	1.3	1.5	2.4	1.1	0.5	1.2	1.5	1.6	1.4	1.4
Producer output prices	7.3	0.9	1.1	2.9	0.1	-0.5	1.0	1.5	1.0	1.2	1.4
LABOUR MARKET											
Unemployment (ILO, mn)	1.82	2.60	3.00	2.27	2.51	2.72	2.90	2.99	3.03	2.99	2.97
Unemployment rate (%)	5.8	8.2	9.5	7.2	8.0	8.6	9.2	9.4	9.6	9.5	9.4
Unemployment (CC, mn)	0.94	1.76	1.99	1.46	1.73	1.90	1.96	1.97	1.98	2.00	2.00
Claimant count rate (%)	2.8	5.4	6.2	4.2	5.4	5.9	6.1	6.2	6.2	6.3	6.3
Employment (mn):	27.31	26.34	25.94	26.75	26.38	26.18	26.06	25.99	25.93	25.91	25.92
Average earnings inc. bonus	3.7	0.0	2.3	-0.4	-0.1	-0.2	0.5	1.7	2.2	2.4	2.7
PUBLIC SECTOR											
Net borrowing (£bn)***	86.7	172.3	182.2								
% of GDP	6.0	12.2	12.6								
*** 2008/09, 2009/10, 2010/11											
FORECAST ASSUMPTIONS											
	2008	2009	2010	2009 Q1	Q2	Q3	Q4	2010 Q1	Q2	Q3	Q4
OECD GDP	0.9	-4.3	0.6	-4.2	-4.9	-5.0	-3.0	-0.7	0.3	1.2	1.8
UK Bank Rate	4.63	0.63	1.25	1.00	0.50	0.50	0.50	0.50	1.00	1.50	2.00
Oil prices \$ per barrel	97.4	58.5	65.0	44.8	59.0	65.0	65.0	65.0	65.0	65.0	65.0
GBP Trade-weighted index	90.9	79.9	82.4	76.8	80.2	81.1	81.4	81.9	82.1	82.4	83.0
USD/GBP	1.85	1.53	1.62	1.43	1.54	1.56	1.58	1.60	1.61	1.62	1.63
EUR/GBP	1.26	1.14	1.21	1.10	1.13	1.15	1.17	1.18	1.20	1.22	1.25