UNITED KINGDOM

THE BRITISH LEAD THE WAY IN VACCINATION

Gambling has risks, but sometimes you win big. No stranger to risky gambles (Brexit, herd immunity to Covid-19...) the UK Prime Minister, Boris Johnson, can now claim that one of his wagers – betting early and big on vaccines – has allowed his country to be amongst the first to see the light at the end of the tunnel. Having been in strict lockdown since the beginning of the year, and whilst also suffering from a collapse in trade with the European Union, the economy now seems to have touched bottom; economic surveys and mobility reports promise better days ahead. Both fiscal and monetary policy will help support the recovery, before thoughts move to addressing the deficit, with the first turn of the screw expected in 2023.

Having been particularly hard-hit by Covid-19[1], the UK is now one of the countries vaccinating most rapidly. With 31 million vaccine doses given since the beginning of the year, coverage of the population has reached 45%, compared to just 17% in the European Union, where delays to the vaccination programme are piling up, as are frustrations with its British supplier. The result is that the pandemic is in retreat in the UK. With the death rate now down to 50 per day (from 1,500 at the peak of the epidemic in January) and the number of new cases at its lowest daily figure since the virus first struck, hope is finally starting to grow. Despite the double whammy of Brexit and the health crisis, the economy has even managed to find some stability.

In January, a strict lockdown and an unprecedented fall in exports to the EU – the result of the reintroduction of non-tariff barriers – caused a further fall in GDP of 3%, coming on top of the drop of nearly 10% in 2020. Since then, however, economic indicators have recovered. This is particularly true of surveys of purchasing managers, which look more optimistic, and the mobility reports from Google, which are showing some signs of movement. The recession in the first quarter is likely to prove less severe than expected, and then to give way to the beginning of a recovery during the spring.

GROWTH AND INFLATION (%)

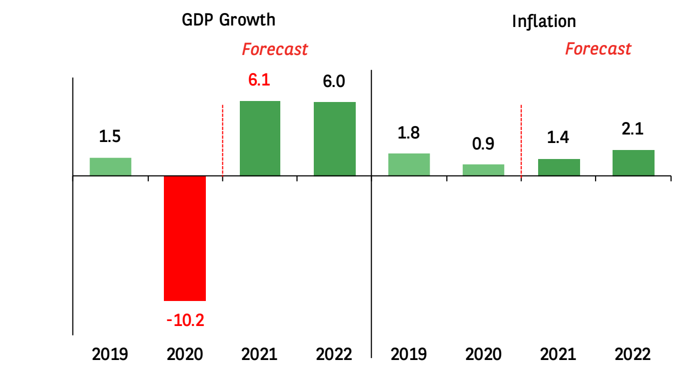

CHART 1 SOURCE: EUROPEAN COMMISSION, BNP PARIBAS

GOVERNMENT SUPPORT EXTENDED... FOR SOME TIME TO COME

The policy response will favour recovery over budget equilibrium for quite some time yet. As in most advanced economies where automatic stabilisers are weak, the health crisis has demanded a strong response from the authorities. The International Monetary Fund puts the UK government on the list of those that have done the most to tackle the depressive effects of the pandemic: 16 points of GDP have been engaged in the economy (excluding guarantees, loans and injections of capital), double the effort made in the European Union. As a result, the government deficit – at 16.9% of GDP in 2020, from less than 3% in 2019 – has seen unprecedented expansion.

In his budget, presented on 3 March, Chancellor of the Exchequer Rishi Sunak maintained a resolutely combative approach for the coming fiscal year (April 2021 to April 2022). He plans to devote a further GBP60 billion, or 3 points of GDP, to supporting economic activity, for instance by providing tax incentives for UK businesses to relocate[2]. This is a necessity. With Brexit, foreign direct investment has fallen to zero and has been replaced by net outflows for the first time in 35 years.

Monetary policy also promises to remain accommodating. In line with other major central banks, the Bank of England has supported government measures to tackle the pandemic by stepping up its asset purchase programme (raising target holdings from GBP475 billion to GBP895 billion by year end, or 42% of GDP). It has also brought its policy rate close to zero (0.1% since 20 March 2020). At its most recent meeting, on 17 March 2021, the Monetary Policy Committee noted the improvement in the economic outlook, but indicated that it would not change its policy. The end of "at whatever cost" (increases in business tax, the freezing of tax allowances and rates...) will come later... in 2023.

Completed on 2 April 2021

Jean-Luc Proutat
Jean-luc.proutat@bnpparibas.com

1 127,000 Covid-related deaths had been recorded by 2 April 2021, or 190 for every 100,000 inhabitants, one of the highest death rates amongst the members of the Organisation for Economic Cooperation and Development (OECD).
2 Over a two-year period, capital expenditure within the national economic territory can be deducted from taxable profit at a rate of 130%. Estimated annual cost of the measure: GBP12 billion. Source: Office for Budget Responsibility, March 2021.