

“WHERE THE ECONOMY WILL BE NEXT YEAR IS BLOWING IN THE WIND BUT THE STORY OF HOW WE ENDED UP IN RECESSION IS IMPORTANT TO RECOVERY,” SAYS SENIOR ECONOMIST

Alun Powell, senior economist from HSBC addressed local business people at the Bedford Breakfast Club on 19 May, in the wake of the announcement that the Budget would be broadcast on 22 June. Event sponsors Mazars, Woodfines Solicitors and HSBC invited local senior partners and directors from throughout the region.

“The past is important because it tells us how the economy ended up in a mess and it might give pointers how to get out of it. The future remains unpredictable,” were Alun’s opening words.

“In 2007, inflation rose, so the Bank of England increased interest rates which would normally slow growth if it was accelerating too fast. It did not work because growth was largely based on consumer borrowing,” explained Alun.

“In 2007 the debt-to-income ratio reached 160%, so the average consumer had approximately £160 of debt for every £100 earned. When interest rose, so did the cost of servicing debt, and spending naturally dipped in 2008,” explained Andy Mason, area commercial director at HSBC.

As manufacturers saw the economy begin to topple, they reduced production to clear their stocks and GDP fell.

“Destocking of around £20 billion took place in 2009. As this slowed, GDP started to increase at the beginning of this year. Service industries came out of decline early in 2009, manufacturers were a little later and recently the construction industry has followed,” said Alun.

“In 2001 property owners borrowed against their rising property valuations which bolstered their annual income. In 2008/9 they were seeking to reduce monthly costs by putting their own cash back into the property market in mortgage overpayments which consequently reduced disposable income,” added Valerie Findlay, senior associate at Woodfines Solicitors.

Unemployment has become another factor.

“Unemployment reached around half of the forecast levels because, unlike in earlier recessions, many took sabbaticals or worked part time rather than becoming unemployed. Although this suppressed unemployment rates, now people are underemployed. As the economy picks up employment is likely to plateau because companies do not have to recruit new workers. The June Budget will be interesting because if the public sector cuts costs, unemployment could grow,” commented David Birch, partner at Mazars.

“Inflation has also become a problem. Pay cuts and freezes have pushed earning growth rates beneath inflation rates, so people have even less money to spend,” explained Alun.

In the near future consumer spending is not going to be the driving force behind the economy that it has been in the past.

The prospect of tax increases from the next Budget has knocked investor confidence. The government is unlikely to support growth over the next few years. Current forecasts indicate that debt will reach 75% of GDP by 2014.

“The real issue is the speed at which we are reaching this level of national debt. Many who used to pay tax are now claiming unemployment benefits. This will take a long time to reverse,” explained Alun.

The Tories appear keen on cutting public spending but the Lib Dem's are more likely to increase taxes, so there is likely to be horse-trading on the run-up to the Budget.

“Large income tax hikes damage the economy in the long term. We will wait and see what the new coalition has to offer. It is going to be interesting,” commented Alun.

Weakened Sterling made British goods more affordable to the rest of the world. However, old trading habits die hard.

“We tend to export to developed countries, which are also struggling, which passes inflation from one region to another. British business should target rapid growth countries such as India, Russia, China and eastern Europe. This is a huge opportunity to increase sales but there appears to be a reluctance to take it.

“The Bank of England assumes that our inflation spike is temporary. If this assumption is incorrect interest rates will be forced upwards to bring inflation back under control,” Alun warned.

“Recovery will be drawn out. National growth forecasts range from 1.5% to 2.5%; however, the Bank of England is likely to think that it will be higher if exports and investments fare better than we think. There are probably 90 different views on where Britain will end up next year,” concluded Alun.

- ENDS -

Issued on behalf of Bedford Breakfast Club by Rachael Bonfield, Solution Factors Ltd.  
Email: [Rachael@solutionfactors.com](mailto:Rachael@solutionfactors.com)  
Tel: 01908 587793

#### **About Bedford Breakfast Club**

The Bedford Breakfast Club has, for many years, provided a friendly and informal environment where you can meet with a wide range of business, educational and professional finance people.

We meet every third Wednesday of the month starting at around 7.20am, finishing at 9am, with an average attendance of around 60+ people.

We provide breakfast, with an interesting speaker on topics all in a very pleasant location at the Bedfordshire Golf Club.

[www.bedfordbreakfastclub.co.uk](http://www.bedfordbreakfastclub.co.uk)