Economy expected to grow at modest pace throughout 2019

Economic growth has been volatile in the first half of 2019, due to pre-Brexit stockpiling and a surge in gold bullion pushing up imports growth. But further ahead, the economy is expected to grow at a modest pace, according to the CBI.

The UK’s leading business group now predicts GDP growth of 1.4% in 2019 and 1.5% in 2020. This is based on an orderly Brexit deal being ratified by October 2019, and the commencement of a smooth transition period thereafter.

A key driver of this growth is household spending (which grows by 1.7% in both 2019 and 2020), underpinned by a recent pick-up in real earnings. We expect living standards to remain reasonably firm over our forecast, giving impetus to household spending. However, growth is likely to remain below the average of recent years, as the ongoing weakness in productivity holds back earnings, partially offsetting the upward pressure on wages from a tight labour market.

In contrast to the firmness in household spending, Brexit uncertainty continues to bite hard on business investment, which remains very weak for this stage of the economic cycle. The CBI expects business investment to fall for much of the rest of this year (-1.3% in 2019, 0.9% in 2020). But under our forecast assumption that a Brexit deal is ratified, firms are expected to gradually resume capital spending projects, in particular on new technology such as artificial intelligence and automation. Nonetheless, growth in business investment is expected to remain modest, weighed upon by uncertainty around the end state of the UK-EU relationship.

Rain Newton-Smith, CBI Chief Economist, said:
"Looking through the volatility in growth over the last six months, our view of modest economic momentum ahead is largely unchanged.

"However, there is a lot going on underneath the surface and the make-up of growth in our forecast is more skewed towards consumers. It’s certainly positive that household spending has more punch, thanks to an improvement in living standards. But set against this, Brexit uncertainty is crippling business investment, which we expect to fall at the fastest pace since the financial crisis this year. It’s crystal clear that without a Brexit deal by October, we’re at risk of falling further behind our G7 competitors.

“Our forecast represents what could be in the event of an orderly Brexit – a decent foundation upon which we can take the reins and re-focus on vital domestic priorities that have been neglected. For example, pressing ahead with essential infrastructure projects such as HS2 and Heathrow expansion will enable the UK to better connect with and enter new global markets. These priorities will shift down the list in a no deal scenario, against the backdrop of damage to the UK economy, jobs and livelihoods.”

Meanwhile, global growth is expected to be slower this year, though to remain relatively decent. The global economy is forecast to grow by 3.0% in 2019 and 3.5% in 2020 (in purchasing power parity terms). However, the global backdrop has been hit by weaker world trade recently, in part due to the bilateral tariffs imposed between the US and China. As a result, the CBI expects slower UK export growth ahead. Coupled with the surge in imports in Q1, this means that no support to the economy is expected from net trade over our forecast.

The Bank of England continues to signal a gradual tightening in monetary policy ahead. While CPI inflation is around target at present, the Bank have their eye on growing domestic cost pressures, and the subsequent upward pressure on inflation over the medium-term. Brexit uncertainty is likely to keep the Monetary Policy Committee in check this year, but we expect two rate rises in 2020, of 25 basis points each.

Looking ahead, a “no deal” Brexit remains the biggest risk to the outlook, through its damaging impact on activity, sentiment and financial markets.