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Economic Briefing: November 2010

This paper summarises current economic conditions in Northern Ireland. It is intended to provide an overview of a range of economic indicators, including current growth projections, labour market and property market conditions, as well as the outlook for inflation / interest rates. Key data and messages are presented upfront in the Executive Summary in an attempt to provide an 'at a glance' synopsis of the NI economy.

Executive Summary

1. Economic Growth

Key Local Economic Indicators¹:

Gross Value Added (GVA)	NI (vs. UK)
GVA - 2009	-4.9% (vs. -4.7%)
GVA forecast – 2010	1.0% (vs. 1.7%)
GVA forecast – 2011	1.8% (vs. 2.1%)

Key Messages:

- Global economic recovery is underway; however, downside risks remain. Advanced economies, in particular, continue to be challenged by low levels of consumer confidence and reduced household incomes/wealth;
- It is estimated that the UK will grow at a rate considerably below the global economy in 2010 and 2011 (1.7% and 2% compared to 4.8% and 4.2%, respectively)². Forecasts for UK growth have remained relatively unchanged in the wake of the Spending Review 2010, since the scale of the cuts was broadly as anticipated³.
- NI faces a number of particular challenges to sustained economic recovery, including:
 - Impending cuts in Public Expenditure, particularly given disproportionate reliance on Public Sector;
 - Lack of confidence (generally and, more recently, in wake of 2010 Spending Review announcements), possibly leading to further drag on consumption and higher rates of precautionary saving⁴;
 - Relatively small private sector/export base;
 - High rate of economic inactivity;
 - Ongoing deterioration in labour market conditions (unlike rest of UK)⁵;
 - NI has associated reliance on welfare system and is thus particularly exposed to impending reforms;
 - Property market remains unsettled, with falling prices and lack of transactions still a feature;
 - Relationship with ROI and associated exposure to financial issues there, including bail-out by EU and International Monetary Fund (IMF);
 - Remaining constraints on availability/affordability of credit⁶ (particularly given specific nature of NI banking sector⁷);
- Accordingly, leading forecasts indicate that growth in NI will be below that of the UK at 1% in 2010 (vs 1.7% in UK) and 1.8% in 2011 (vs. 2.1% in UK);
- Growth projections for the NI economy presume strong performance in the Hospitality, Agriculture, Retail, Manufacturing, Health and Transport/Communications sectors. Sectors which are expected to contract further include Financial Services, Public Administration and Construction.

¹ Oxford Economics forecasts, as presented in Northern Bank/Oxford Economics, *Quarterly Sectoral Forecasts*, Q4 2010

² According to International Monetary Fund, October 2010

³ By the forecasters (as per *Quarterly Sectoral Forecasts*, Northern Bank, Q4 2010)

⁴ I.e. Consumers might further reign in spending, opting to save a higher proportion of incomes.

⁵ Claimant count numbers are continuing to rise in NI, whereas they have recently started to fall in UK

⁶ Anecdotal evidence suggests businesses are still encountering problems in accessing and/or affording credit. This is also supported by recent surveys conducted by the Institute of Directors on bank lending in NI

⁷ NI has a relatively concentrated banking sector, with four 'leading' banks, two of which are Irish owned and thus potentially exposed to the outworkings of NAMA, the EU/IMF bail-out, etc.

2. Labour Market Trends

Key Data⁸:

	Trend (Yr)	NI (vs. UK)
Employment (July-Sept 2010)	↑	66.1% (vs. 70.8%)
Number of Jobs - QES (June 2010)	↓	-
Unemployment (July-Sept 2010)	↓	7.0% (vs. 7.7%)
Claimant Count (Sept 2010)	↑	6.6% (vs. 4.5%)
Economic Inactivity (July-Sept 2010)	↓	28.8% (vs. 23.2%)
Redundancies (Oct 2010)	↓	-

Key Messages:

- Although official employment data indicates a slight improvement in conditions in the most recent quarter (July-Sept 2010), it is possible that rises in part-time employment are masking true trends. Indeed, the most recent data indicates that the proportion of males working part-time is at its highest on record.
- The Quarterly Employment Survey (June 2010), which measures the number of *jobs*⁹, in fact indicates a further deterioration in labour market conditions, particularly within the Services and Construction Sectors;
- Recent claimant count numbers also indicate an ongoing deterioration in labour market conditions. The level in NI is continuing to rise; this is contrast with the overall UK trend of falling numbers over the last year;
- Despite a slight improvement in most recent quarter, NI continues to have a particular problem with high rates of economic inactivity (this is largely attributable to a relatively high proportion of sick/disabled and students);
- There have been considerably fewer confirmed redundancies over the last 12 months, compared with the previous year. The largest number occurred in Belfast District Council area, and of all confirmed redundancies, 33% were in the manufacturing sector;
- The level of unfilled vacancies has fallen considerably since 2008, reflecting tighter labour market conditions.

3. Housing Market Trends

Key Data: NI House Prices

	Average House Price	Annual Change (vs. UK ¹⁰)
Nationwide (Sept 2010)	£131k	↓11.1% (vs. ↑8.3%)
Halifax (Oct 2010)	£128k	↓13.1% (vs. ↑8.3%)
University of Ulster (Nov 2010)	£148k	↓7.6% (vs. ↑8.3%)
Ulster Bank (Oct 2010)	£151k	↓18.8% (vs. ↑8.3%)
UK average	£213k	

⁸ NI Labour Force Survey, DETI, November 2010. Data is for the period from July-Sept 2010 unless otherwise indicated.

⁹ As opposed to persons in employment. The 'employment rate' does not reflect, for example, moves to part-time hours.

¹⁰ UK statistic based upon Department of Communities and Local government survey (as presented in Ulster Bank report)

Key Messages:

- NI's house price correction, from peak levels, has been more extreme than in other regions. However, it is important to acknowledge that this has occurred following a particularly large spike in local prices prior to the downturn;
- The specific data on the level of correction in local house prices is mixed; however, all sources indicate that, unlike the rest of the UK, the NI housing market is continuing to undergo price falls;
- The local market remains volatile, with a lack of confidence and a resultant lack of transactions.

4. Other considerations

- **ROI 'Bail-out' by EU/IMF:** The issues currently facing the Irish economy have potential economic implications for NI. The ROI accounts for a significant proportion of exports for local firms; thus the current situation may only create a further challenge for local companies in their ability to grow and enable sustained recovery in 2010 and 2011;
- **Bank Lending Levels:** It would appear that credit remains relatively inaccessible/unaffordable for local businesses and consumers, potentially impeding economic recovery in NI¹¹. It is not yet clear what the impact of the ROI bail-out may be upon the NI banking sector, (in particular upon the two Irish owned banks), however, it may serve to exacerbate existing conditions;
- **Business/Consumer Confidence:** Both consumer and business confidence levels remain low, and in the case of businesses, are continuing to deteriorate.
- **Inflation/Interest Rates:** Inflation remains elevated and risks to the upside¹²; remain (increase in VAT to 20% next year, pressure on food/commodity prices, etc). However, these pressures may be offset by public sector pay freezes and the degree of spare capacity (the difference between potential output and actual output) within the economy.

¹¹ As per local businesses' claims. Evidence produced by the Institute of Directors survey of bank lending is consistent with this.

¹² I.e. Risks to further increases in inflation rate

1 Economic Growth

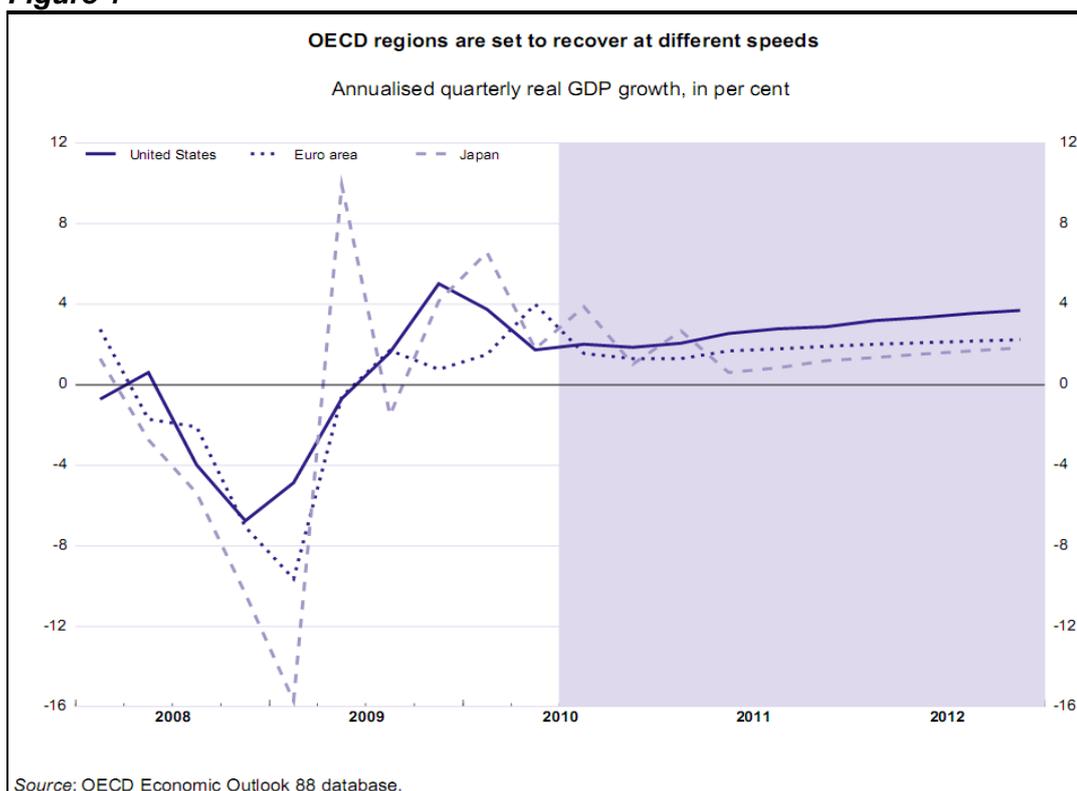
1.1 Key Data¹³

Gross Value Added (GVA)	NI (vs. UK)
GVA - 2009	-4.9% (vs. -4.7%)
GVA forecast – 2010	1.0% (vs. 1.7%)
GVA forecast – 2011	1.8% (vs. 2.1%)

1.2 **Global Context:** Global economic recovery is underway; during the first half of 2010, economic activity expanded at an annual rate of approximately 5¼%¹⁴. However, *advanced economies* remain particularly challenged by low levels of consumer confidence and squeezes on income/wealth¹⁵. Many consumers are now facing rising taxes and falling (real) wages, which may create a further drag on consumption and higher rates of precautionary saving.

1.3 **Global Outlook:** Most recent International Monetary Fund (IMF) estimates indicate that global activity will expand by 4.8% in 2010 and 4.2% in 2011, with a temporary slowdown during the second half of 2010 and the first half of 2011¹⁶. However, different regions are expected to recover at significantly different rates (as per OECD forecasts, Figure 1):

Figure 1



¹³ Oxford Economics forecasts, as presented in Northern Bank/Oxford Economics, *Quarterly Sectoral Forecasts*, Q4 2010

¹⁴ A surge in inventory and, more recently, fixed investment accounted for a dramatic rise in manufacturing and global trade World Economic Outlook, International Monetary Fund, October 2010.

¹⁵ Many emerging and developing countries are, in fact, experiencing strong growth – most did not experience major financial excesses just prior to the recession. <http://www.imf.org/external/pubs/ft/weo/2010/02/pdf/text.pdf>

¹⁶ World Economic Outlook, International Monetary Fund, October 2010, p. 1

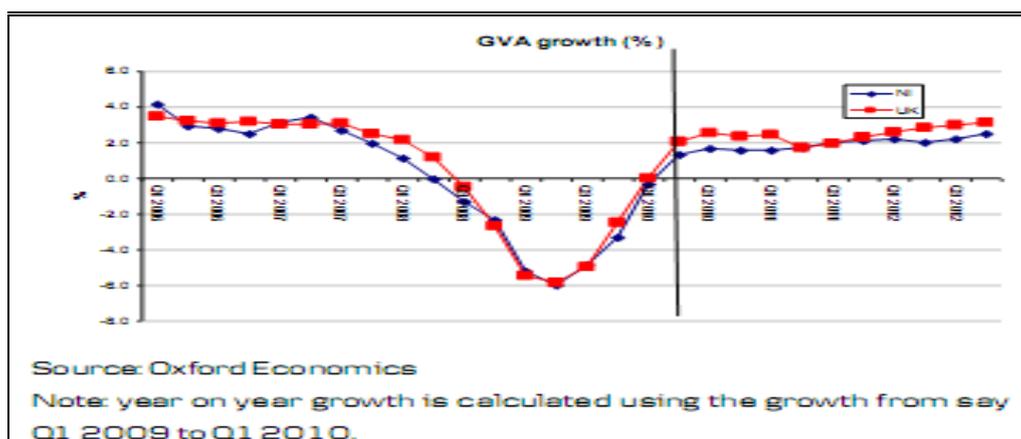
1.4 UK Outlook: The UK recovery should be bolstered by the considerable monetary policy stimulus (Quantitative Easing and cuts in interest rates) implemented to date, the expansion in world demand and past depreciation of sterling. However, in the wake of the bank bailouts, (with resultant impacts on consumer confidence and income/wealth levels, particularly in anticipation of Spending Review cuts), downside risks remain elevated. Both Oxford Economics and IMF projections indicate that the UK will experience growth rates considerably below those being projected for the global economy. As outlined in section 1.1, Oxford Economics currently estimates UK growth rates of 1.7% and 2.1% in 2010 and 2011, respectively. IMF estimates are broadly the same (1.7% and 2.0%).

1.5 NI Outlook: The Northern Ireland economy will face a number of particular challenges over coming months. It is arguable that the forthcoming fiscal consolidation will have a disproportionate impact on the NI economy, for the following reasons:

- NI has particular reliance on Public Sector (making cuts particularly painful);
- Lack of confidence (generally and, more recently, in wake of 2010 Spending Review announcements), possibly leading to further drag on consumption and higher rates of precautionary saving¹⁷;
- Relatively small private sector/export base;
- High rate of 'economically inactive';
- Ongoing deterioration in labour market conditions (unlike rest of UK)¹⁸;
- Associated reliance on welfare system and disproportionate exposure to reforms;
- Ongoing falls in house prices (unlike many other UK regions);
- Relationship with ROI and associated exposure to financial issues there;
- Reduced availability/affordability of credit¹⁹ (particularly given specific nature of NI banking sector²⁰);

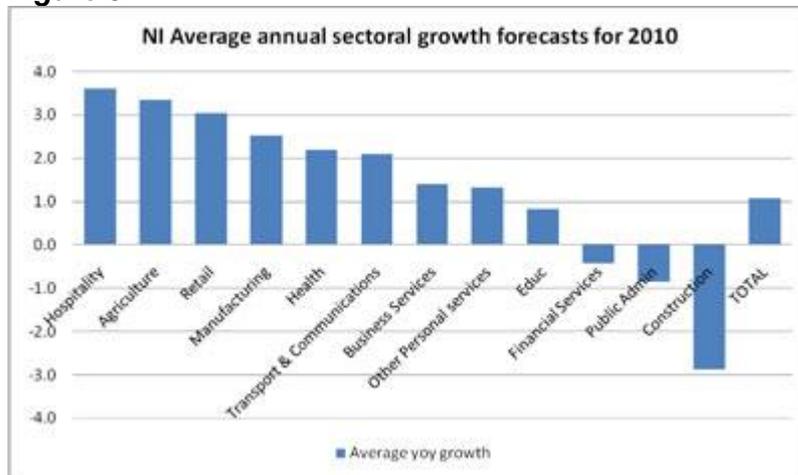
The outlook for the NI economy depends upon a variety of factors, including how the Executive decides to allocate/execute the spending cuts across departments. However, for the reasons outlined above, it is anticipated that NI will recover at a slower rate than the UK average (Figure 2). Oxford Economics thus indicates that GVA growth in NI will be 1% in 2010 (vs 1.7% in UK) and 1.8% in 2011 (vs. 2.1% in UK).

Figure 2: GVA Growth (%) in NI and UK



1.6 **Which Sectors Will Drive Recovery?** The projections for economic growth in NI are bolstered by assumptions of strong performance within the Hospitality, Agriculture, Retail, Manufacturing, Health, Transport & Communications and Business and other Personal Services sectors. It is anticipated that this growth will offset further contractions within Construction, Public Administration and Financial Services²¹, (Figure 3).

Figure 3



Source: Oxford Economics/Northern Bank Quarterly Sectoral Forecasts, Q4 2010

²¹ Quarterly Sectoral Forecasts, Oxford Economics/Northern Bank, Q4 2010

2 Labour Market Trends

2.1 Key Data²²:

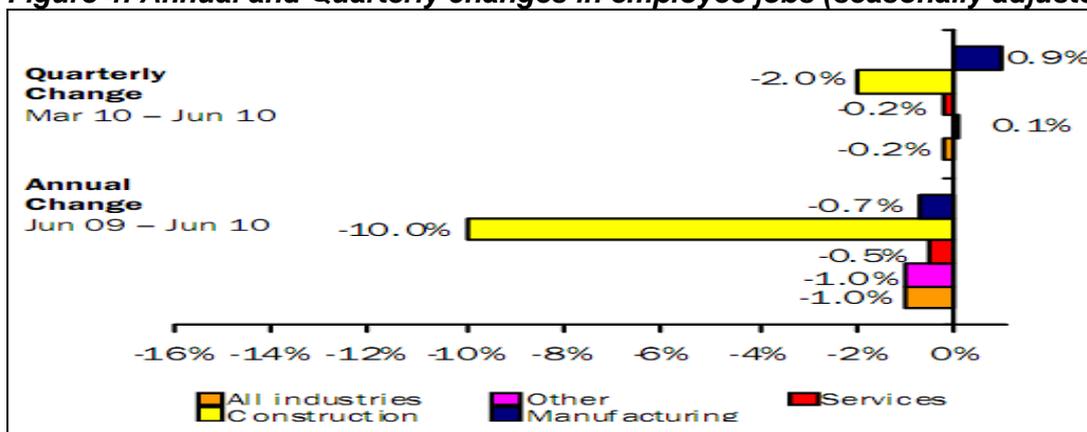
	Trend (Yr)	NI (vs. UK)
Employment (July-Sept 2010)	↑	66.1% (vs. 70.8%)
Number of Jobs - QES (June 2010)	↓	-
Unemployment (July-Sept 2010)	↓	7.0% (vs. 7.7%)
Claimant Count (Sept 2010)	↑	6.6% (vs. 4.5%)
Economic Inactivity (July-Sept 2010)	↓	28.8% (vs. 23.2%)
Redundancies (Oct 2010)	↓	-

2.2 Employment: The seasonally adjusted working age²³ employment rate (66.1%) has fallen by 0.2 percentage points over the quarter, but remains 1.8 percentage points higher than the same period last year²⁴. NI's employment rate remains well below the UK average (70.8%) and is the lowest of the 12 UK regions²⁵.

It is worth highlighting that higher rates of part-time employment may be bolstering employment data (potentially masking the true impact of the downturn upon the labour market); the proportion of males working *part-time* is currently at its highest on record, for example²⁶.

2.3 Quarterly Employment Survey (QES): This is an alternative measure of employment; it measures the *number* of jobs, as opposed to persons in employment. As such, it might be considered the preferred measure of change in employee jobs²⁷. In June 2010, the seasonally adjusted employee jobs total in NI was 699,230; (a decrease of 0.2% (1,120 jobs) since the March revised estimate and of 7,220 over the year). Decreases over the quarter occurred in the Service Sector (-1,090) and in Construction (-690), whilst increases occurred in Manufacturing (630) and Other Industries (30)²⁸.

Figure 4: Annual and Quarterly changes in employee jobs (seasonally adjusted)



Source: Monthly Labour Market Report, DETI, October 2010

²² NI Labour Force Survey, DETI, November 2010. Data is for the period from July-Sept 2010 unless otherwise indicated.

²³ Those aged 16-64

²⁴ According to DETI, the sampling variability of the employment estimates and change are +/-23,000 and +/-29,000, respectively

²⁵ Monthly Labour Market Report, DETI, November 2010

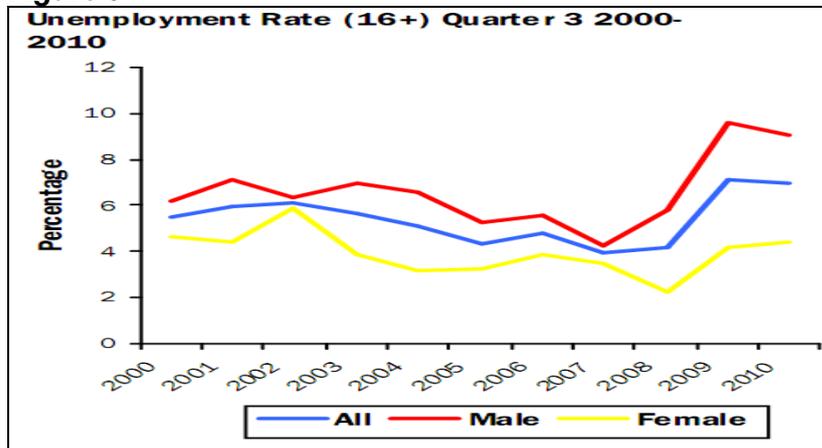
²⁶ NI Labour Force Survey, DETI, November 2010, p. 1

²⁷ Monthly Labour Market Report, DETI, October 2010, p. 3

²⁸ Monthly Labour Market Report, DETI, November 2010

2.4 **Unemployment:** In the period July-September 2010, the seasonally adjusted unemployment rate was estimated at 7.0%; up 0.3 percentage points from the previous quarter, but down 0.1% percentage points over the year (refer Figure 5). The unemployment rate remains below the UK average (7.7%) and is the fourth lowest amongst the 12 UK regions²⁹. The NI rate also compares favourably to those rates in the EU (9.6%) and ROI (13.9%) for August 2010³⁰.

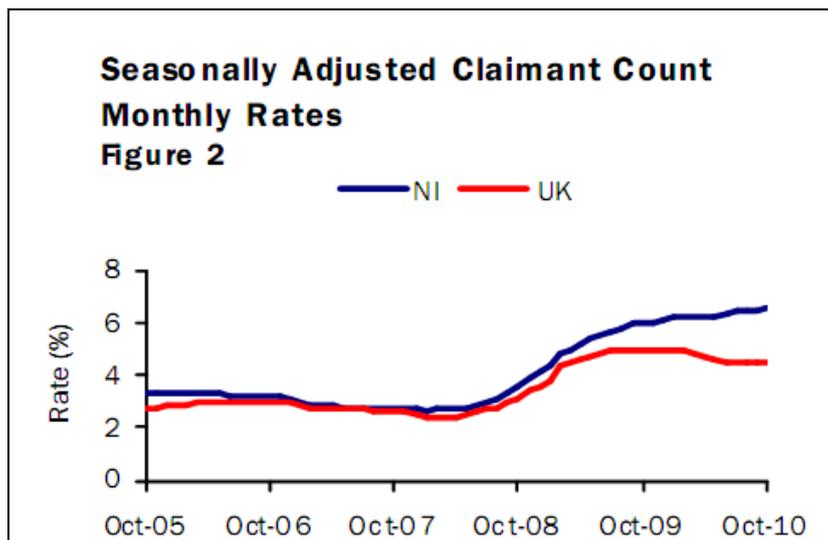
Figure 5



Source: NI Labour Force Survey, DETI, November 2010

2.5 **General Claimant Count:** Claimant count data paints a more negative picture of labour market conditions; the data is continuing to show signs of deterioration. The seasonally adjusted claimant count data (October 2010) increased by 400 over the month to 58,600 (this was the same as the rise in September 2010, thus there is no sign of a levelling off, as yet). The current (seasonally adjusted) rate of 6.6% is considerably above the UK average (4.5%) and is the second highest amongst the twelve UK regions³¹. Whilst claimant count levels in NI increased over the month to October 2010 (by 400 claimants, or 0.7%), the UK rate decreased by 0.3% (Figure 6).

Figure 6



Source: Monthly Labour Market Report, DETI, November 2010

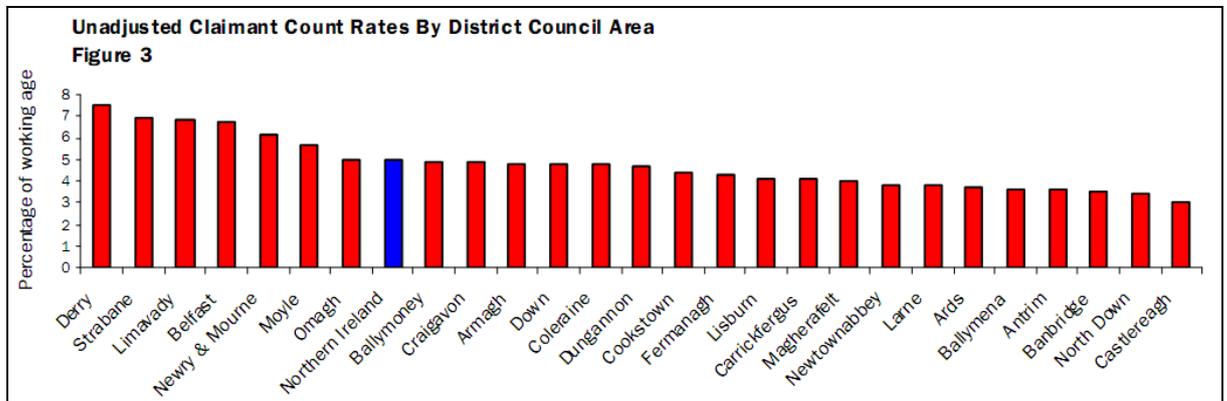
²⁹ NI Labour Force Survey, DETI, November 2010

³⁰ Monthly Labour Market Report, DETI, November 2010

³¹ Ibid

Within NI, the areas with the highest claimant count rates³² at October 2010 include Derry (7.5%), Strabane (6.9%) and Limavady (6.8%), (*Figure 7*). Those that showed the highest percentage increase over the year to October 2010 included Newry & Mourne (26.5%), Banbridge (24.5%) and Armagh (17.6%)³³.

Figure 7: Unadjusted Claimant Count Rates by District Council Area

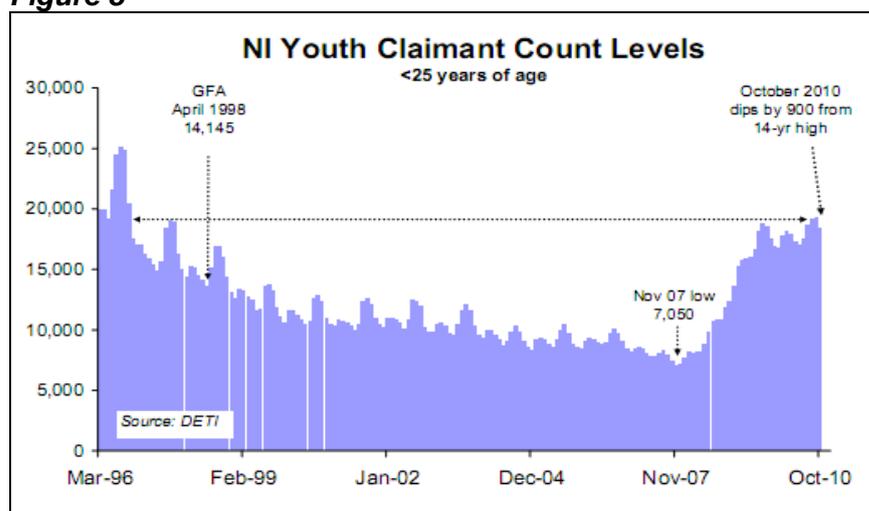


Source: Monthly Labour Market Report, DETI, November 2010

What is of particular concern is that, (as shown in Figure 8), there has been a marked increase in the level of *youth unemployment* (individuals under the age of 25) in NI since the November 2007 ‘low’. Over 2,220 individuals were added to the unemployment register over the four months to September 2010; however, there was a drop of almost 900 in October. This brought the total rate back below a 14-year high reached in September (the highest level of youth unemployment since October 1996)³⁴.

Despite a slight improvement in October, the rise in youth unemployment is concerning, and is likely to be exacerbated further by any freezes in public sector recruitment; a possible outcome of the Spending Review 2010. Furthermore, the collation government’s proposals in respect of increasing university tuition fees could also lead to further rises in the youth unemployment rate. The potential generational impact of these developments in labour market conditions is a worry.

Figure 8



Source: NI’s unemployment still rising in October, Ulster Bank, November 2010

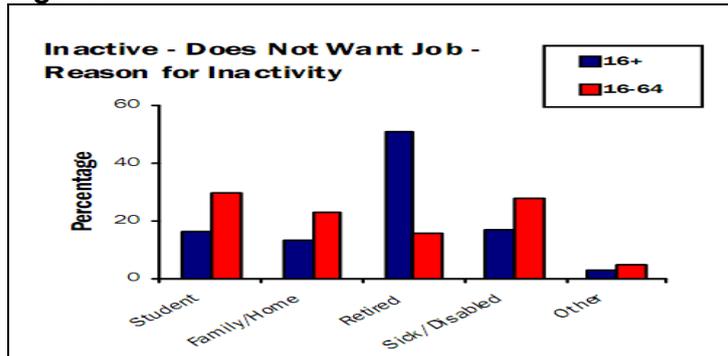
³² Unadjusted numbers as a percentage of the resident working age population

³³ Ibid

³⁴ NI’s unemployment still rising in October, Ulster Bank, October 2010

2.6 **Economically Inactive:** The unemployment rate in NI appears relatively healthy; however, this does not reflect the high rate of economic activity in NI. Although slightly improved in the current quarter, NI still ranks worst of the 12 UK regions in this respect; (28.8%, compared to UK average rate of 23.2%)³⁵. Unadjusted data shows that approximately 8% (47,000) of the working age-economically inactive wanted a job, but did not satisfy the criteria to be classified as ‘unemployed’ (being available for and actively seeking work). Amongst the (unadjusted) working-age inactive, there are a large proportion of students (27%)³⁶. However, there is also a relatively high rate of inactivity due to sickness/disability in NI (28.0% compared to UK average of 23.6%) – refer Figure 9³⁷.

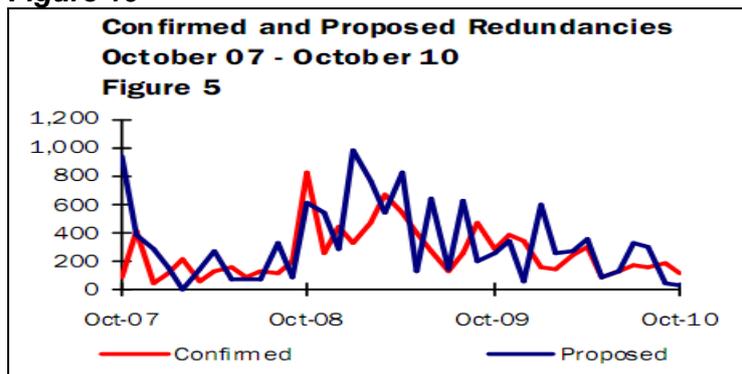
Figure 9



Source: NI Labour Force Survey, DETI, November 2010

2.7 **Redundancies:** The Department for Enterprise, Trade and Investment (DETI) was notified of 368 proposed redundancies between mid October and mid November 2010, compared to 50 in the previous monthly period. However, over the latest 12 month period there were a total of 2,480 confirmed redundancies; a decrease of 46% versus the same period in the previous year (4,576). The largest number occurred in Belfast District Council area (24.9% or 618 in total). Of all confirmed redundancies, 33% were in the Manufacturing sector. There are currently 1,085 ‘outstanding’ redundancies (proposed, but not confirmed), which is 39% lower than this time last year (1,787) (Figure 10)³⁸.

Figure 10



Source: Monthly Labour Market Report, DETI, November 2010

2.8 **Unfilled Vacancies:** As at 3 September 2010, a total of 6,891 vacancies remain unfilled; decreases of 2% on the total count in September 2009 and 36% on September 2008³⁹.

³⁵ NI Labour Force Survey, DETI, November 2010

³⁶ Monthly Labour Market Report, DETI, October 2010, p. 1

³⁷ NI Labour Force Survey, DETI, November 2010

³⁸ Monthly Labour Market Report, DETI, November 2010

³⁹ Ibid

3 Housing Market Trends

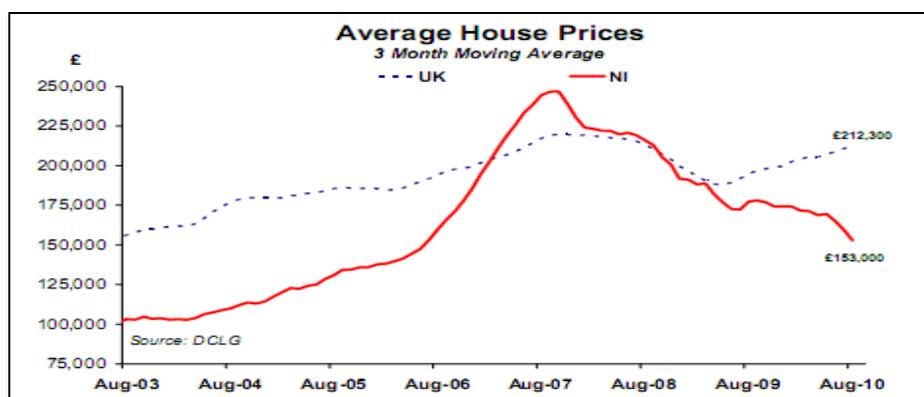
3.1 Key Data

	Average House Price	Annual Change (vs. UK ⁴⁰)
Nationwide (Sept 2010)	£131k	↓11.1% (vs. ↑8.3%)
Halifax (Oct 2010) ⁴¹	£128k	↓13.1% (vs. ↑8.3%)
University of Ulster (Nov 2010)	£148k	↓7.6% (vs. ↑8.3%)
Ulster Bank (Oct 2010)	£151k	↓18.8% (vs. ↑8.3%)
UK average	£213k	

3.2 **Trends in House Prices:** As is shown in the table above, there is a general consensus amongst the leading surveys that house prices in NI have continued to fall over the last 12 months; however, there are differing opinions with regards to the extent of the falls.

Ulster Bank claims that its survey is more reflective of market conditions as it is based on Department for Communities and Local Government (DCLG) data and, as such, includes the majority of lenders in NI (unlike separate Halifax and Nationwide surveys). Using a mix-adjusted index, Ulster Bank estimates that average house prices have fallen by 18.8% over the last year, (as opposed to a rise of 8.3% in the UK). The New Dwellings sector has experienced particularly sharp declines of approximately 26% (year-on-year)⁴². Overall trends since August 2003 are depicted in Figure 11.

Figure 11



Source: NI Housing Market Update, Ulster Bank, October 2010

The University of Ulster estimates a more moderate fall of 7.6% over the year⁴³. However, some regions have fared considerably worse than others; for example, the survey indicates that whereas the Belfast market has previously been relatively resilient, it has been less strong in the third quarter with an average fall of 21.7% over the year⁴⁴.

⁴⁰ UK statistic based upon Department of Communities and Local government survey (as presented in Ulster Bank report)

⁴¹ <http://www.lloydsbankinggroup.com/media/pdfs/research/Q3-2010/NorthernIrelandQ32010.pdf>

⁴² NI Housing Market Update, Ulster Bank, October 2010

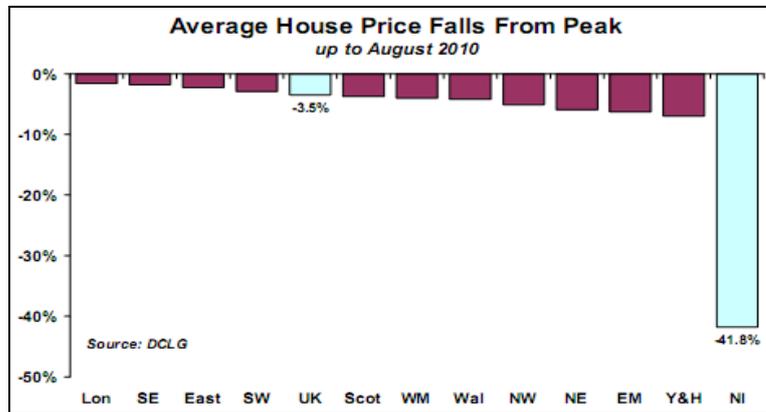
⁴³ Based upon weighted changes (this is the preferred measure according to UU survey and takes into consideration the price change and volume for each of six property types)

<http://news.ulster.ac.uk/releases/2010/5450.html>

⁴⁴ Ibid

3.3 **Price Corrections since Peak:** When average house prices are assessed relative to the peak (August 2007), it emerges that the NI housing market has fared particularly badly (Figure 12). It is important to acknowledge that NI property prices also underwent amongst the most extreme increases in the UK prior to this; however, the impact of such severe price corrections is considerable in terms of confidence levels in NI and is thus noteworthy in an economic context.

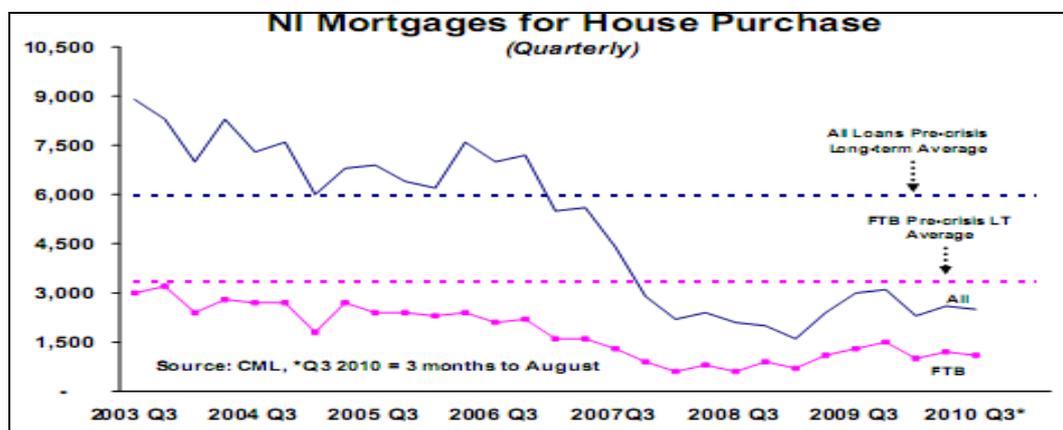
Figure 12



Source: NI Housing Market Update, Ulster Bank, October 2010

3.4 **Lack of Transactions:** Latest data from the Council of Mortgage Lenders confirms low levels of property market activity within the market⁴⁵. In the three months to August 2010, the number of mortgages released (2,500) was approximately 40% of the pre-crisis long-term average of approximately 6,000 (Figure 13).

Figure 13



Source: NI Housing Market Update, Ulster Bank, October 2010

⁴⁵ NI Housing Market Update, Ulster Bank, October 2010

4 Other Considerations

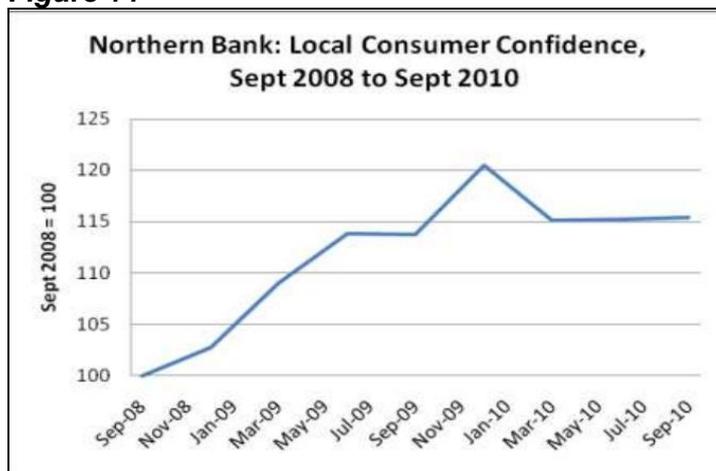
4.1 **ROI 'Bail-out' by EU/IMF:** As at 23 November 2010, the Irish Government has confirmed that it has formally requested financial assistance from the European Union. EU and euro-area financial support will be negotiated with the Irish authorities by the European Commission and the International Monetary Fund (IMF), in liaison with the European Central Bank (ECB)⁴⁶. The figure is being estimated at being in the region of 80 to 90 billion Euro⁴⁷. The Minister for Enterprise Trade and Investment has acknowledged the potential impact of this upon the NI economy; in particular, raising the concern about further job losses within the local banking sector should further amalgamations occur.

Minister Foster explained additional potential implications for the NI economy could arise from the fact that the ROI accounts for over 10% of sales by local manufacturing companies and 28.5% of exports. Accordingly, she re-iterated the requirement for local companies to become more out-ward looking and export orientated, in order that they may be able to drive growth in 2010/11⁴⁸.

4.2 **Bank Lending Levels:** It is important that healthy lending levels be restored to aid a recovery in the NI economy. There is anecdotal evidence to suggest that credit conditions in NI remain constrained, (refer to previous research paper for further details on banking issues in Northern Ireland⁴⁹). There also remains a relative lack of take-up, amongst local banks, of the government's schemes to enhance bank lending levels.

4.3 **Business/Consumer Confidence:** According to the Northern Bank Consumer Confidence Index for NI (Figure 14), in Quarter 3 of 2010, confidence levels remained unchanged on the previous quarter. The index reported a drop in confidence around expectations for future finances, and a decline in household's perception of their financial position relative to one year ago. However, the survey did reflect a, perhaps surprising, increase in perceived job security and spending expectations⁵⁰.

Figure 14



Source: Northern Bank

With regards to business confidence, the Ulster Bank Purchasing Managers' Index (PMI) indicated a further deterioration in conditions in October 2010, with activity decreasing at

⁴⁶ <http://www.eubusiness.com/news-eu/finance-economy.73i>

⁴⁷ Ibid

⁴⁸ Urgent Oral Question to Minister for ETI, NI Assembly, 22 November 2010

⁴⁹ <http://www.niassembly.gov.uk/researchandlibrary/2010/9710.pdf>

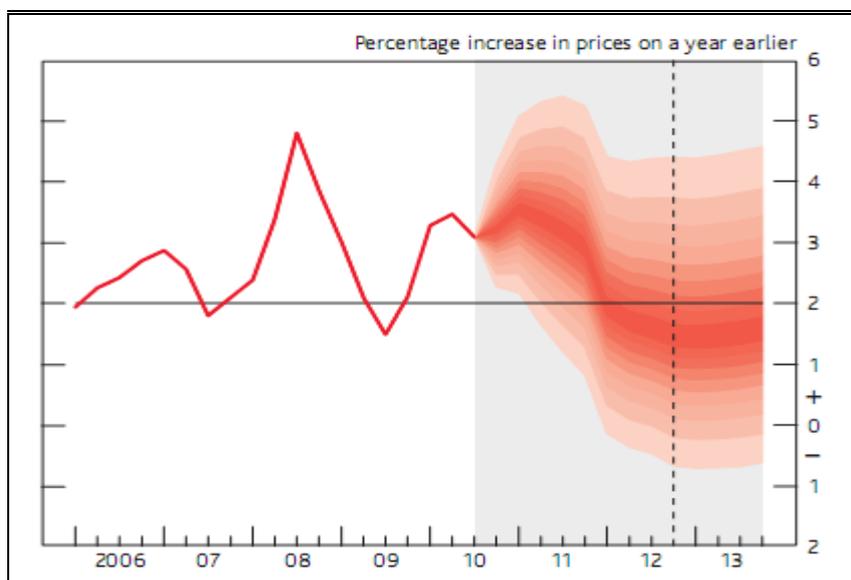
⁵⁰ <http://www.northernbank.co.uk/SiteCollectionDocuments/economic/2010/Northern-Bank-Consumer-Confidence-Oct-10.pdf>

the fastest rate in three months. Employee numbers also fell, as new business and backlogs of work levelled off. On the prices front, output charges fell further in October, despite strong cost inflation rates⁵¹.

4.4 Inflation/Interest Rates: The rate of Consumer Price Index (CPI) inflation was 3.1% in September 2010, (above the Bank of England (BOE's) target rate of 2%, thus necessitating another explanatory (or 'open') letter to the Chancellor). The elevated level of inflation is reflective of VAT having been restored to 17.5% as well as the past depreciation of sterling⁵².

With regards to the inflationary outlook, the most BOE Inflation Report (November 2010) indicates that the near term outlook for inflation is higher than previously expected (refer to Figure 15; the fan is reflective of the element of uncertainty in future trends) and is likely to remain above the 2% target for much of 2011.

Figure 15: CPI inflation projection⁵³



Source: Bank of England

It is likely that the forthcoming increase in VAT to 20% (2011) will put further pressure on prices. However, any freezes in public sector pay rates should mitigate this effect, as should the persistent margin of spare capacity within the economy⁵⁴.

The rate of inflation is an important consideration for NI, because it has implications for interest rates (with the Bank of England being more likely, all other things being equal, to increase interest rates should inflationary pressures persist⁵⁵). Higher interest rates would not be desirable, under current conditions, for local businesses or consumers.

Furthermore, the actual rate of inflation will determine the true impact of the forthcoming expenditure cuts across the UK. If inflation exceeds the rate forecasted in the Spending Review 2010, then real terms cuts in expenditure will be even higher than anticipated.

⁵¹ Ulster Bank Northern Ireland PMI, 8 November 2010.

⁵² Bank of England Inflation Report, November 2010

⁵³ Based on market interest rate expectations and £200 bn asset purchases

⁵⁴ The medium term outlook for inflation will also depend upon 'inflationary expectations'.

⁵⁵ This decision would be taken in the context of balancing the risks associated with inflation against the possibility of impeding economic recovery with higher interest rates.