

pbaaccountants
proactive business advice

Economic update: August 2014

This guide looks at key UK economic indicators and the economic prospects for the coming months.



Economic UPDATE

Following a period of faster than anticipated growth at the end of 2013, the economy has continued to strengthen with consistent growth throughout the first half of 2014.

Gross domestic product (GDP) increased 0.8% in the second quarter of 2014 and was around 3.1% higher than the same period in 2013. The economy has grown for 6 consecutive quarters, the longest period of progress since the start of the economic downturn in 2008.

This continued growth means Office for National Statistics (ONS) figures put GDP at 0.2% above its pre-recession high for the first time.

However, weak productivity in the workforce and population increases mean that output per person is not predicted to exceed pre-recession levels until 2017.

Industry growth

Services, which make up almost 80% of the entire UK economy, was the largest contributor to growth in Q2 2014, rising by 1% over the quarter and adding 0.77

percentage points to the increase in GDP.

Production output increased by 0.4% in Q2 2014 thanks to rises in manufacturing (0.2%) and energy supply (4.7%).

However, total production decreased by 0.7% between April 2014 and May 2014 including a 1.3% decrease in manufacturing. In the 3 months to June 2014, production was 11.3% below its Q1 2008 pre-downturn figure.

Construction output rose by 1.2% (£113 million) in the month to April 2014 and 4.6% over the year. New work increased by 4.9% compared with April 2013, which the ONS attributed to strong increases in new housing and private industrial work. However, construction output decreased 0.5% in Q2 2014 and remains 10.7% below its Q1 2008 level.

Investment growth

Since the end of the downturn, growth has been focused on household spending. However, in recent quarters investment growth has made a more significant

contribution to overall GDP. In the first 3 months of 2014, household spending and investment both added 1.4 percentage points to GDP growth.

The investment growth comes from a combination of business investment, which grew 10.6% in the year to Q1 2014, and investment in buildings such as houses.

Houses and mortgages

The Halifax Price Index reveals that house prices in the 3 months to June 2014 were 8.8% higher compared to the same period in 2013.

Looking at the longer-term picture, ONS figures show that house prices have recovered from the recession. In April 2014, the average house price was 6.5% higher than in January 2008.

However, these figures are affected by significant rises in house prices in London. House prices in the capital were 31.6% above their January 2008 level in April 2014. In the rest of the UK, prices were 0.2% below their pre-downturn level.



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Mortgage lending

The rise in house prices has led to a rise in the share of high loan to income mortgages.

The Bank of England's Financial Policy Committee (FPC) is concerned that if economic conditions change, this type of lending could potentially damage the banking system and jeopardise economic stability.

To protect against risky lending and a significant rise in household debt, the FPC has recommended:

- mortgage lenders should assess whether borrowers could afford to pay their mortgage if interest rates increased by 3 percentage points in the first 5 years of the loan.
- a 15% cap (as a percentage of all their new mortgages) on the number of mortgages lenders can give at more than 4.5 times the borrower's income.

Similarly, the Treasury has also announced that it will not include loans above 4.5 times the borrowers' income in its Help to Buy mortgage guarantee scheme.

Employment

Unemployment fell and the number of employed people increased comparing December 2013 to February 2014 with March to May 2014. There were 30.64 million people in work, up 254,000 compared to the previous 3 months.

Unemployment in the 3 months to May 2014 was 2.12 million - the lowest figure in nearly 6 years. The unemployment rate for March to May 2014 was 6.5% - below the Bank of England's 7% threshold for considering raising interest rates.

The increase in employment has not been mirrored by an increase in wages. The average weekly wage grew by 1.7%

between January and March 2014 compared with the same 3 months in 2013. However, for March-May 2014 pay including bonuses was 0.3% higher compared to a year earlier and pay excluding bonuses increased 0.7%. These are the lowest increases since 2009 and 2001 respectively.

Inflation

The Consumer Prices Index (CPI) measure of inflation increased by 1.9% in the year to June 2014, up from 1.5% in May. The biggest contributors to the rise came from clothing, food and non-alcoholic drinks and air transport.

The latest figures mean inflation has been below the Bank of England's 2% target for 6 consecutive months.

Interest rates

The interest rate has been set at 0.5% since March 2009 and the Bank of England has not raised the rate despite recent economic growth. In June 2014, Bank of England Governor Mark Carney said a rise in the rate "could happen sooner than markets currently expect". However, Carney has reassured businesses saying that eventual increases in the Bank rate will be "gradual and limited".

Contact us

We can help you to identify and take advantage of any opportunities to prosper over the coming months. Please get in touch to arrange a meeting.

We can advise you on your responsibilities and show you how you may be able to legally reduce your tax liability.

All figures are correct at time of going to press, 31 July 2014.

Business opportunities

Lending for exporters

Exporters can apply for government loans of up to £3 billion under the Direct Lending Facility.

Business rate relief

Business rate relief for business in enterprise zones has been extended until March 2018. Business that start up or relocate to an enterprise zone can claim up to 100% business rate relief for 5 years, up to a maximum of £275,000.

Tax relief on machinery

Businesses can claim tax relief on investment in equipment and machinery worth up to £500,000 a year. However, the limit will fall back to £25,000 from 31 December 2015.

Small Business, Enterprise and Employment Bill

The next session of parliament will introduce legislation to support small businesses by cutting bureaucracy and providing better access to government finance.

Funding for innovation

The government innovation agency, the Technology Strategy Board, has earmarked £400 million for 88 competitions designed to find and fund entrepreneurial ideas.