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The Economy: Recent Developments and Prospects to mid-1988

The following note and tables are adapted from the *Financial Statement and Budget Report 1987-88* (HMSO, March 1987)(Price £6.90):

Summary

The economy has been growing at around 3 per cent since last spring as exports have recovered strongly. For 1986 as a whole, recorded GDP growth was about 2½ per cent. A substantial rise in investment and non-oil exports is forecast for 1987, and GDP is expected to grow by 3 per cent, with manufacturing output rising slightly faster.

Employment has continued to grow, particularly since the middle of 1986. There has been a reversal of the previous rising trend in unemployment, and there are good prospects for a continuing decline this year.

Inflation fell last year to 3½ per cent, its lowest level for nearly 20 years. During 1987, inflation may rise temporarily to a little over 4½ per cent, as last year's movements in petrol prices and in mortgage interest rates affect the year-on-year comparisons. But it is expected to fall back to around 4 per cent by the fourth quarter.

Output in the major industrial countries has been rising by 2½—3 per cent a year since 1984, and is likely to continue at that rate in 1987. Imports by developing countries (other than oil exporters) should rise this year. Markets for UK exports of manufactures may grow a little faster in 1987 than in 1986.

Following the fall in oil prices a year ago, the current account of the balance of payments recorded a deficit of around £1 billion in 1986. Both export and import volumes rose sharply in the second half of last year. A further relatively modest current account deficit of £2½ billion (some ½ per cent of GDP) is forecast for 1987.

The forecast for the UK assumes that fiscal and monetary policies are set within the framework of the MTFS. It makes the conventional assumption of an oil price of $15 a barrel, as in last year's forecast, and assumes that the exchange rate will remain close to its current level.

Financial conditions

The dollar fell further during 1986, particularly against the deutschemark and the yen. These changes will, over time, help to reduce the size of the US current account deficit and the Japanese and German surpluses. As paragraph 2.10 above explained, Finance Ministers of six of the leading industrialised nations agreed last month to seek a period of stability in exchange rates. Sterling fell in the summer of 1986, in the wake of the fall in the oil price. It remained steady between October and mid-February, but has since strengthened.

Short-term interest rates in the UK, which rose to nearly 13 per cent in January 1986, fell last spring to around 10 per cent. But with sterling weakening in the summer and autumn and with M0 also indicating an easing of monetary conditions, interest rates were raised to 11 per cent in October; they remained around that level until early March, but have since fallen. Rates in several overseas countries have also been reduced in recent months. Longer-term rates in the UK followed the same broad profile as short-term rates during 1986, falling sharply in the spring and rising in the autumn. In recent weeks they have fallen again, to below 10 per cent.

M0 growth was below the centre of its 2—6 per cent target range in the early months of 1986—87. Its growth quickened from August onwards, reflecting both the falls in interest rates in the spring and the buoyant growth of personal incomes, and moved into the upper half of its target range. More recently it has fallen back again to the middle of its target range.

The growth of £M3 rose to 18 per cent in the early months of 1986—87 and has since remained at about that level. This is some 3 points above the top of its target range, which in turn was set well above the growth of money GDP. Holdings of bank deposits by companies and financial institutions have grown particularly rapidly. The wider aggregates that include building societies' liabilities have grown more slowly, although also at a rate well in excess of the growth of money GDP: the year-on-year growth of PSL2 has been about 13—14 per cent in recent months. Credit has continued to grow strongly, reflecting at least partly the pace of financial innovation and liberalisation.

The growth of broad money must be seen in the context of the strong growth of private sector wealth and strongly positive real interest rates that have made financial assets attractive to hold. Increased competition in financial markets has narrowed the margins between borrowing and lending rates and this has led persons and companies to build up both their liquidity and their borrowing. The considerable increase in liquidity since 1980 appears to have been willingly held, and has been accompanied by lower inflation.

World economy

The world economy has been strongly influenced by the fall in oil and other commodity prices, and by the substantial depreciation of the dollar. Lower import prices have helped to reduce inflation in the industrialised countries and stimulated faster growth in real domestic demand. But developing countries—and oil producers in particular—have suffered a sharp deterioration in their terms of trade.

Real GNP in the seven largest OECD countries grew by about 2½ per cent in 1986. Domestic demand grew rather faster, at 3½—4 per cent, with large rises in household incomes and consumers' expenditure. Inflation fell further; and average consumer prices in the seven major countries increased by only 2 per cent in 1986.

Despite the buoyancy of domestic demand in these countries, industrial production has grown only slowly. This has been largely a result of weak export demand, particularly from developing countries, and relatively sluggish growth in investment.

The changes in exchange rates over the last two years are already beginning to have significant effects on trade volumes; but these have not yet been enough to overcome the terms of trade effects (the "J-curve"). As a result, the trade imbalances between the major countries remain large. The surpluses in Japan and Germany have continued to grow, though more slowly; and there has been little sign yet of any substantial reduction in the US current account deficit.

Oil prices fell below $10 per barrel last summer, but rose in the second half of the year following the OPEC meeting in December. They have recently traded in a range of $15—$18 a barrel. Food and industrial materials prices also fell sharply through most of last year, although they recovered slightly in the autumn.

World import volumes are thought to have grown by more than 5 per cent during 1986. This is somewhat faster than in 1985, largely because of a rise in oil trade as the major oil companies rebuild their stocks. Developed countries' exports of manufactures rose by only 3 per cent as buoyant domestic demand in industrialised countries was partially offset by cuts in developing countries' imports.

The outlook for oil prices remains uncertain. The forecast below is based on the assumption that North Sea oil prices average $15 per barrel in 1987—88. Non-oil commodity prices may remain low, with food prices held down by the large surpluses of agricultural production. With rising activity in the major economies, industrial material prices may recover slightly from their current low levels.

Table 1 shows the forecasts for activity and inflation in the major seven industrialised countries, and for world trade. Inflation is expected to remain low, though it may rise a little from last year's level. In the US inflation may increase slightly as the effects of the fall in the dollar feed through, but the corresponding appreciation of the yen and deutschemark should mean that prices in Japan and Germany rise only very slowly, if at all.

Table 1 World economy

	Per cent changes on a year earlier			
		Estimates	Forecasts	
	1985	1986	1987	1988 H1
Major Seven countries [1]:				
Real GNP	3	2½	2½	3
Real domestic demand	3	3¾	3	3¼
Industrial production	3	1	2½	4¼
Consumer prices	4	2	2¼	2¾
World trade, at constant prices				
Total imports	3½	5½	3½	4½
Trade in manufactures [2]	4	2½	3½	4

[1] US, Japan, Germany, France, UK, Italy and Canada.

[2] Developed countries' exports weighted by UK markets.

These changes in exchange rates and inflation will affect domestic demand and output. In Japan and Germany they are likely to strengthen domestic demand but weaken export demand; in the US, the opposite effects are likely. In aggregate, domestic demand in the major industrial countries is likely to grow less strongly than in 1986. But GNP growth should be much the same, and industrial production should grow rather faster, helped by a recovery in exports.

World trade in manufactures is forecast to grow rather more quickly in 1987 than in 1986, though the pattern may be uneven. Import demand in the US is likely to slow down considerably, and oil producers are likely to cut back their imports further. But imports by Japan and Germany are expected to increase rapidly. Imports by non-oil developing countries seem likely to rise faster in 1987, after showing little change in 1986; despite continuing debt problems for some of these countries, commodity prices and hence export earnings are expected to strengthen during 1987. Growth in total world trade in 1987 is likely to be slower than in 1986, largely because the rebuilding of oil stocks is not expected to continue.

UK trade and the balance of payments

The UK's competitiveness improved markedly during 1986. Productivity rose fast and the growth of unit labour costs was only a little above that of our main competitors. As a result, the lower exchange rate was almost entirely reflected in improved competitiveness (Table 2). Most of the gain in competitiveness seems likely to be maintained over the year ahead.

Table 2 The exchange rate and competitiveness*

	Sterling index (1975=100)	Relative unit labour costs* (1980=100)
1984 Q4	75	80
1985 Q5	80	86
1986 Q4	68	72

*Ratio of UK manufacturing costs to those overseas.

Prices of most imports rose during 1986, as the effects of the depreciation of sterling more than offset generally weak world prices. Export prices also rose, as exporters took advantage of sterling's decline to improve profit margins. Excluding oil, the terms of trade for goods worsened slightly between 1985 and 1986. Little further change seems likely in 1987.

Table 3 Visible trade

	Per cent changes on previous year					
	All goods			Goods less oil and erratic items		
	Export volume	Import volume	Terms of trade*	Export volume	Import volume	Terms of trade*
1985	5½	3½	1½	7	4	1½
1986	3½	6	—5½	2½	6	—1
1987 Forecast	4	7	0	6	8	½

*The ratio of UK export average values to import average values.

The forecast for visible trade is summarised in Table 3.3

Exports of manufactures have been growing strongly in recent months. Growth had flattened in the final months of 1985 and exports fell briefly in early 1986, in common with those of other main manufacturing countries. But since then they have recovered strongly, and in the three months to January were 6 per cent above their level a year earlier. With rising world trade and the continued benefits of improved competitiveness, manufactured exports should show further strong growth in 1987. Exports of non-manufactures rose rapidly last year, mainly as a result of exceptionally high grain exports (demand for UK grain exports was strong, partly reflecting drought in Southern Europe); grain exports are unlikely to continue at these levels in 1987. Total exports should grow by about 6 per cent, compared with 2½ per cent in 1986.

UK manufactured export volumes appear to have maintained their share of developed countries' exports in 1986. This reinforces the previous evidence, that the declining trend in share of developed countries' exports over the decades up to 1981 has ended.

Non-oil imports were flat in the early part of 1986, but then rose sharply in the second half of the year. More recently, the rate of growth has moderated. Imports are likely to continue to rise in 1987 as domestic activity expands, though improved competitiveness should slow the rate of growth. Non-manufactured imports rose rapidly in 1986, partly reflecting increased imports of foodstuffs; this effect is unlikely to continue in 1987. In total, imports of goods other than oil are forecast to rise by 5 per cent between the second halves of 1986 and 1987.

Britain's surplus on oil trade halved from £8 billion in 1985 to £4 billion in 1986, reflecting the sharp fall in world oil prices and some decline in the volume of net oil exports. North Sea production in 1987 is likely to be somewhat lower than in 1986 and the oil trade surplus slightly smaller.

The surplus on invisibles rose in 1986. Net receipts of interest, profits and dividends (IPD) rose particularly rapidly as a result of the lower payments abroad by North Sea companies and an increase in the surplus on other earnings. The surplus on services fell in 1986, largely due to lower net earnings from tourism. The deficit on transfers was abnormally low last year, reflecting the size and timing of government transactions with the European Community.

The surplus on invisibles is forecast to show a further rise in 1987 with the pound's depreciation during last year helping to increase the sterling value of the earnings on the UK's large stock of foreign assets. The surpluses on services should also benefit from the improvement in UK competitiveness. These higher earnings should more than offset an increase in the transfers deficit to a more normal level.

The current account recorded a £1 billion deficit in 1986 following a surplus of £3 billion in 1985. Lower net oil earnings and an increased deficit on trade in manufactures more than offset an improvement in invisibles. The forecast for 1987 is for a current account deficit of £2½ billion. Details are given in Table 4.

Table 4 Current account

£ billion

	Manu-factures	Oil	Other goods	Invisibles	Current balance
1985	−3	8	−7½	5	3
1986	−5½	4	−7	7	−1
1987 Forecast	−8	4	−7	8½	−2½

The UK's stock of net overseas assets is thought to have risen by the end of 1986 to about £110 billion (equivalent to 28 per cent of GDP: its highest recorded level since the war) compared with £80 billion at the end of 1985. The increase in the sterling value of assets reflects both the strength of world stock markets and the depreciation of sterling last year.

Demand and activity

The UK economy continued its steady growth in 1986. But there are uncertainties over the precise estimates of the rate of growth, given the differences between the three separate estimates of GDP (based on measures of expenditure, income and output). The output figures—generally recognised as the most reliable short-term indication—show non-oil growth of over 3 per cent between the end of 1985 and the end of 1986, following a brief pause in late 1985.

As in other industrial countries, consumers' expenditure in the UK grew strongly in 1986 as inflation fell and real incomes rose. UK exports were weak in the first half of the year, but recovered strongly in the second half. Imports had been depressed in the first half of the year but also rose sharply in the second half as the economy gained momentum, with particularly marked rises in imports of capital goods. Output growth in the service industries exceeded growth of manufacturing output for the year as a whole; but manufacturing output rose by over 2 per cent between the two halves of the year as exports recovered.

Real personal disposable income is estimated to have risen by about 4 per cent in 1986, and consumers' expenditure by over 4½ per cent. This implies some further fall in the personal savings ratio which has been declining throughout most of the 1980s. One reason is that with lower inflation households have needed to make less provision for the erosion of their past savings. Another factor has been a decline in the growth of employers' contributions to pension funds as a result of the surpluses that many funds have been showing, reinforced by the provisions of the 1986 Finance Act: these contributions are treated in the national accounts as a part of personal income and saving. The buoyancy of consumers' spending may also owe something to the strength of the stock market. In spite of the fall in the savings ratio, higher asset prices and lower inflation have contributed to an increase of over 50 per cent in persons' net holdings of financial assets since the end of 1983.

Real personal disposable income is forecast to rise by around 3½ per cent in 1987. This is slightly less than in 1986 and reflects some narrowing of the gap between earnings growth and inflation. Though there may be some further decline in the savings ratio, consumers' expenditure is expected to grow more slowly than in 1986, at a little under 4 per cent.

The housing market was buoyant in 1986, and private housing investment, both in new dwellings and in improvements to existing dwellings, grew strongly during the course of the year. Private housing starts were about 8½ per cent higher than in 1985; in Greater London, where the largest increases in house prices have been recorded, private housing starts in 1986 were almost 40 per cent up on a year earlier. These higher starts should be reflected in completions and investment in new dwellings during 1987; private housing investment may rise by around 10 per cent in the year as a whole.

The rate of return earned by non-North Sea industrial and commercial companies (ICCs) continued to rise last year; gross trading profits earned in the North Sea fell by more than half. The outlook for companies is favourable, but further substantial rises in profitability will probably have to depend less on depressed world prices of inputs of materials and fuels, and more on firms containing the costs that are under their own control.

Company sector spending was relatively weak in 1986. North Sea investment has been falling in the face of sharply lower profits. Onshore business investment was affected by the bringing forward of capital spending into 1985 ahead of the final stage of the changes in capital allowances announced in the 1984 Budget.

The prospects are for investment to grow rapidly this year. The DTI investment intentions survey published last December pointed to growth in non-North Sea business investment of about 6 per cent, continuing into 1988. The latest quarterly CBI survey of industrial trends indicated a pick up in investment in manufacturing industry, and the forecast assumes that the DTI's intentions survey projections will be broadly realised. Table 5 provides details of the forecast for total investment and its components.

Table 5 Gross fixed domestic capital formation

	£ billion at 1980 prices	Per cent changes on a year earlier		
	1985	1985	1986	Forecast 1987
Business[1]	30.5	4	−3	4
Private dwellings[2]	9.3	−1	9	8
General government	6.6	−5	7	−1
Total fixed investment	**46.3**	**2**	**½**	**4**

1 Including investment by public corporations
2 Includes purchases less sales of land by persons, companies and public corporations, other than purchases of council houses.

The economy's stock output ratio fell in 1986 for the sixth successive year. It appears that manufacturers ran down stocks; and though distributors' stock levels rose, the increase was a small one in relation to the increase in the volume of sales. The latest quarterly CBI survey suggested that manufacturers may not now be intending to reduce their stocks of raw materials much further, possibly because of the firmer trend in raw material prices in recent months. An additional source of destocking in 1986 was the exceptionally high exports of grain which reduced the stocks held by the Intervention Board for Agricultural Produce (IBAP).

Stockbuilding is likely to make a positive contribution to growth in 1987, although the forecast is for only a small rise in stocks by the standards of most years in the 1970s, and there is likely to be a further fall in the stock output ratio for the whole economy.

The forecast is for a further year of steady growth in 1987. GDP is expected to grow by 3 per cent, around the rate at which it was growing in the latter part of 1986. Exports and investment are forecast to grow strongly, offsetting some slowing down in consumer spending. The prospects for demand and activity are summarised in Table 6.

Table 6 Domestic demand and GDP

	Per cent changes on a year earlier[1] (at constant prices)		
		Forecasts	
	1986	1987	1988 H1
Domestic demand	3	3½	3
Exports of goods and services	3 (3)	4 (5)	2 (4)
Imports of goods and services	6 (5½)	6 (7)	2½ (3)
Domestic production: GDP[2]	2½	3	2½

1 Non-oil shown in brackets.
2 Average measure.

The recovery in manufacturing output seen in the second half of 1986 is forecast to continue, helped by rising exports (Table 7). Construction output also rose quite strongly during 1986, and should benefit further from the expected strength of private investment in buildings during 1987.

Table 7 Real output

	Per cent changes on a year earlier		
		Forecasts	
	1986	1987	1988 H1
GDP	2½	3	2½
Non-North Sea output	2½	3½	3
Manufacturing output	½	4	3

Inflation

Both retail and producer output price inflation remain close to the lowest levels experienced since the 1960s. The RPI rose by 3½ per cent in 1986, compared to a rise of 6 per cent in 1985. The annual inflation rate reached a low point of 2.4 per cent in July and August: most of its subsequent rise has reflected changes in mortgage interest rates.

The rate of increase of producer output prices has also fallen significantly since the start of 1986, although it has started to edge up again recently, reflecting in part the fall in sterling that took place during the summer and early autumn.

Pay increases in the private sector have fallen slightly in recent months. Settlements in manufacturing industry recorded by the CBI have shown a fall of about 1½ per cent since 1985, although settlements in the private sector as a whole, including those outside manufacturing, may have fallen by less than this. This decline in pay settlements has not yet been reflected in lower recorded growth in average earnings. The current annual rate of growth of earnings reflects settlements made over the whole of the last year (the majority of them still dating from the period when settlements were running at a higher rate than they now are), and is also affected by overtime working, which has risen slightly since the second quarter of 1986.

In spite of the continuing relatively fast growth of earnings, unit labour costs in manufacturing have probably changed only a little since the first quarter of 1986 as productivity has risen sharply. Between 1985 and 1986 unit labour costs in manufacturing rose by about 5 per cent. For the first time since 1983 unit labour costs in manufacturing in the UK are expected in 1987 to rise no faster than those in the other major industrial nations.

The lower pay settlements recorded in recent months should lead to lower growth in earnings. Nevertheless employees will enjoy a further substantial rise in real earnings in 1987. The high rate of productivity growth currently being recorded should contain the growth in unit labour costs to below 4 per cent for the non-oil private sector as a whole, and to around 1½ per cent for manufacturing industry.

Table 8 Costs in manufacturing

	Per cent changes on a year earlier			
	Unit labour costs	Cost of materials and fuel[1]	Estimated total costs[2]	Output prices[1]
1984	3	8½	5	5½
1985	4	4½	4½	6½
1986	5	−10½	0	4½
1987 Forecasts	1½	3	2	4

1 Producer prices excluding food, drink and tobacco.
2 Including costs of bought in services.

The figures in Table 8 suggest that profit margins in manufacturing have widened markedly in recent years. It seems likely that industry will hold on to the gains it made last year with the help of falling input costs, and profit margins may widen further during 1987 given the forecast low growth in unit labour costs. In the longer run the higher level of profitability should lead to more investment, greater capacity, higher productivity, and hence lower inflationary pressure.

The year-on-year rate of inflation is likely to continue to edge up over the next few months, perhaps rising temporarily to a little over 4½ per cent. This will mainly reflect the relative movements in 1986 and 1987 of petrol prices (which fell during the first half of 1986 to a low point in July and early August) and mortgage interest rates. But inflation should then fall back in the second half of the year, to around 4 per cent in the fourth quarter (for details, see Table 9). The tax and price index (TPI) is expected to show a much smaller increase than the RPI during 1987, peaking at around 3 per cent during the summer, and probably falling to around 2 per cent by the fourth quarter.

Table 9 Retail price index

	Per cent changes on a year earlier			
		Forecasts		
	Weights in 1986	1986 Q4	1987 Q4	1988 Q2
Food	*18½*	3¼	2½	3
Nationalised industries[1]	*6*	3½	2	5
Housing	*14½*	7	9	7
Other	*61*	2½	3½	3¾
Total	*100*	3½	4	4

[1] Including water.

The GDP deflator measures the price of domestic value added—principally unit labour costs and profits per unit of output—and excludes import prices. It is sensitive to movements in North Sea profits, which may have fallen by more than half in the current financial year: as a result the deflator for GDP at market prices may have risen by only 3 per cent in 1986—87. Given the assumption of a $15 oil price and with the further rise in non-North Sea profits now foreseen, the GDP deflator may rise rather faster in 1987-88 than in the previous year, perhaps by around 4½ per cent.

Productivity and the labour market

Results from the 1984 Census of Employment became available in December. These showed that the change in the number of employees since the last Census in 1981 had been very close to provisional estimates based on the results of successive Labour Force Surveys. Results from the 1986 Labour Force Survey have led to minor upward revisions to figures for employees, and to a downward revision to the figure for growth in self-employment between mid-1985 and mid-1986. Growth since March 1983 in the employed labour force in Great Britain is now estimated at 1,040,000. Table 10 shows changes in employment over the last three years for which figures are available.

Table 10 Employment

	Thousands, change in GB seasonally adjusted				
	Employees in employment		Self employed	HM Forces	Total in employment
	Male	Female			
September 1983 to September 1984	− 23	+190	+235	+3	+406
September 1984 to September 1985	+ 47	+196	+ 90	− 2	+330
September 1985 to September 1986	− 25	+126	+ 38*	− 3	+136

* Figure for self-employment growth since June 1986 is a projection based on self-employment growth over the previous five years.

Growth in employment averaged only about 20,000 a quarter in the first half of 1986, reflecting the period of sluggish output growth at the end of 1985 and in early 1986. The third quarter saw employment growing at almost three times this rate as the economy quickened again. Recent monthly figures for manufacturing employment point to a further pick up in total employment growth in the fourth quarter.

While confirming earlier figures for the total number of employees the Census results show some differences from the previous figures in the composition of changes in employment. Full-time female employment has risen by much more, and part-time female employment by much less than previously estimated; employment outside manufacturing has risen more than previously thought while manufacturing employment has shown a corresponding greater decline. The estimate of productivity growth in manufacturing since the 1979 cyclical peak has been raised by about ½ per cent a year on average. Underlying growth in manufacturing productivity now seems to be back to the rate experienced in the 1960s.

Table 11 Output per head of the employed labour force

	Per cent changes					
	Annual averages					
	1964-73	1973-79	1979-86	1983 Q4 to 1984-Q4[1]	1984 Q1[1] to 1985 Q4	1985 Q4 to 1986 Q4[3]
Manufacturing	3¾	¾	3½	3¼	2¼	4¾
Non-manufacturing[2]	3	½	1¼	1¾	1¼	2¾
Whole economy	2¾	1¼	2	2	1	2½
Non-North Sea economy	2¾	½	1¾	2	1¼	2¾

1 Figures for 1984 Q4 are adjusted for the estimated effect of the coal strike.
2 Excludes public services and North Sea oil and gas extraction.
3 Partly forecast.

Seasonally adjusted adult unemployment in the United Kingdom fell by over 100,000 in the six months to January, the largest six month fall since 1973. The continued strength of the UK economy means that employment growth is likely to pick up further during the next year, and the outlook for a continuing fall in unemployment is promising. The training and counselling measures announced and implemented over the past year are helping the long-term unemployed in particular. A sustained major reduction in unemployment will continue to depend on moderation in pay settlements.

Forecast and outturn

Table 12 compares the main elements of the forecast published in the 1986 FSBR with the outturn or latest estimate:

Table 12 Forecast and outturn

	1986 FSBR forecast	Latest estimate/ forecast	Average errors from past forecasts
Total gross domestic product; per cent change between 1985 and 1986	3	2½	¾
RPI; per cent increase between the fourth quarters of 1985 and 1986	3½	3½*	1½
Money GDP, per cent change between 1985-86 and 1986-87	6¾	6	1¼
Current account of the balance of payments in 1986, £ billion	3½	−1*	3
PSBR, financial year 1986-87 £ billion	7	4	5

* Outturn

Inflation in the fourth quarter of 1986 was in line with the forecast made a year ago. GDP growth has probably been a little below forecast, although the data on which latest estimates for 1986 are based are still very uncertain. Non-oil tax revenues have grown faster than forecast, and the PSBR in 1986-87 is likely to turn out about £3 billion below last year's forecast. The largest error made last year was on the current account; the main factors here were that growth in UK export markets turned out well below what had been expected a year ago while the terms of trade worsened more than forecast.

This year's forecast is summarised in Table 13.

Risks and uncertainties

No forecast is complete without an indication of error margins. Table 13 sets out the average errors from past forecasts, alongside the forecasts themselves. These average errors provide an indication of possible errors in the current forecast. Those items which represent the relatively small balance between large flows in either direction are particularly subject to error. For example, the flows on either side of the PSBR, including the revenues of the public corporations, are about £200 billion; and for the current account of the balance of payments exceed £150 billion.

Table 13 The prospects: summary

	Forecast	Average errors from past forecasts[1]
A. Output and expenditure at constant 1980 prices	per cent changes 1986 to 1987	percentage points
Domestic demand	*3½*	*¾*
of which:		
Consumers' expenditure	*4*	*1*
General government consumption	*1*	*1*
Fixed investment	*4*	*2¼*
Change in stockbuilding (as per cent of level of GDP)	*½*	*¾*
Exports of goods and services	*4*	*2½*
Imports of goods and services	*6*	*2½*
Gross domestic product: total	*4*	*¾*
: manufacturing	*3*	*2*
B. Inflation		
Retail prices index	per cent changes	
1986Q4 to 1987Q4	*4*	*1½*
1987Q2 to 1988Q2	*4*	*2¼*
Deflator for GDP at market prices	per cent changes on a year earlier	
Financial year 1986-87	*3*	*¾*
Financial year 1987-88	*4½*	*1¾*
C. Money, GDP at market prices	per cent changes on a year earlier	
Financial year 1986-87	*6*	*1¼*
Financial year 1987-88	*7½*	*1½*
D. Balance of payments on current account	£ billion	
1987	− 2½	3
1988 first half (at an annual rate)	− 2	3½
E. PSBR	£ billion[2]	
Financial year 1986-87	4 *(1%)*	1 *(¼%)*
Financial year 1987-88	4 *(1%)*	5 *(1¼%)*

[1] The errors relate to the average differences (on either side of the central figure) between forecast and outturn. The method of calculating these errors has been explained in earlier publications and government forecasts (see Economic Progress Report June 1981). The calculations of average errors are based on forecasts made between 1975 and 1985. The errors are after adjustment for the effects of major changes in fiscal policy that were not allowed for in the forecasts.

[2] Per cent of GDP at market prices shown in brackets.

Table 14 Constant price forecasts of expenditure, imports and gross domestic product [1]

£ billion at 1980 prices, seasonally adjusted

	Consumers' expenditure	General government consumption	Total fixed investment	Exports of goods and services	Change in stocks	**Total final expenditure**	*Less* Imports of goods and services	*Less* Adjustment to factor cost	*Plus* Statistical adjustment	**Gross domestic product at factor cost**	GDP index (average estimate) 1980 = 100
1982	138.3	49.6	39.4	63.3	- 1.1	**289.4**	59.5	30.4	0.5	**199.9**	100.3
1983	143.6	50.5	41.7	64.7	0.7	**301.2**	68.2	31.5	- 0.2	**206.7**	103.7
1984	146.7	50.9	45.5	69.1	- 0.1	**312.1**	68.6	32.6	1.8	**212.7**	106.7
1985	152.0	51.0	46.3	73.1	0.6	**323.0**	70.7	34.0	1.4	**219.8**	110.2
1986	159.2	51.6	46.6	75.3	0.6	**333.2**	74.8	35.0	2.1	**225.5**	113.1
1987	165.2	52.1	48.4	78.4	1.4	**345.5**	79.4	36.3	2.4	**232.2**	116.5
1985 H1	75.0	25.5	23.3	36.7	0.4	**161.0**	35.2	16.7	0.5	**109.5**	109.9
H2	76.9	25.5	23.0	36.4	0.2	**162.0**	35.5	17.2	0.9	**110.2**	110.6
1986 H1	78.6	25.5	23.3	36.7	0.4	**164.5**	35.9	17.2	0.6	**112.0**	112.3
H2	80.6	26.0	23.3	38.7	0.2	**168.8**	39.0	17.8	1.5	**113.5**	113.9
1987 H1	81.9	26.0	24.0	39.0	0.6	**171.6**	39.3	18.0	1.2	**115.5**	115.8
H2	83.3	26.1	24.4	39.5	0.7	**173.9**	40.1	18.3	1.2	**116.7**	117.1
1988 H1	84.9	26.2	24.7	39.7	0.6	**176.3**	40.3	18.6	1.1	**118.5**	118.9
	Per cent changes										
1984 to 1985	*3½*	*0*	*2*	*6*	—	*3½*	*3*	*4*	—	*3½*	*3½*
1985 to 1986	*4½*	*1*	*½*	*3*	—	*3*	*6*	*3*	—	*2½*	*2½*
1986 to 1987	*4*	*1*	*4*	*4*	—	*3½*	*6*	*4*	—	*3*	*3*
1987 H1 to 1988 H1	*3½*	*1*	*3*	*2*	—	*2½*	*2½*	*3*	—	*2½*	*2½*

[1] GDP figures in the table are based on "compromise" estimates of gross domestic product, reflecting, for the past, average movements in constant price expenditure, output and income estimates of GDP. Percentage changes are calculated from unrounded levels and then rounded to half per cent. Figures for 1987 H1 and beyond are forecasts. Figures for periods up to the end of 1986 are based mainly on the national accounts published earlier this year (covering periods up to 1986 Q3) and incorporate some revised and later data and forecasts. A full set of national accounts, to end 1986, was published by the Central Statistical Office on 20 March.

Index of sources

Data given on page 5 may be more recent than that shown elsewhere in the publication.
United Kingdom balance of payments: National income and expenditure. In addition to the series indexed below, further detailed statistics are included in the regular quarterly articles (see inside back cover).