What’s the Matter with Britain?

Martin Wolf
Financial Times

01. Dec. 2022
Britain’s Zigzag course

- Asia focus: support of AIIB (against US, pro China)
- Brexit
- “Mini budget” – low tax growth model
  - Gilt yield scare LDI Pension fund

- Pragmatism: Traditional strength of UK
- Is there a battle for UK’s growth model?
Country Strategy

- Life science, IT, standard setter
- Green technology

- Tax haven
  Financial center focus

- European “bridge to Asia”
Country Strategy

- Life science, IT, ➡️ standard setter
  Green technology
     ➡️ cooperate with US (Europe)

- Tax haven
  Financial center focus
     ➡️ confront Europe, US

- European “bridge to Asia”
     ➡️ conflict with US (AIIB analogy)
Country Strategy - Geoeconomics

- Life science, IT, standard setter
  - Green technology
    - cooperate with US (Europe)

- Tax haven
  - Financial center focus
    - confront Europe, US

- European “bridge to Asia”
  - conflict with US (AIIB analogy)
Global Trade and Current Account Deficit

- Free Trade Champion
  Commonwealth connection
  for services: English language advantage

- Ongoing current account deficit
  - Vulnerability to currency as pound is not safe asset/reserve currency
    (no exorbitant privilege)
Gilt Yield Spike – Oct. 2022

- UK *fiscal* situation, *current account*, LDI-Pension fund *financial stability* issue

- 3-sided game of chicken ....
  - Monetary ■ Fiscal ■ Financial *Dominance*

- Monetary Dominance prevailed
  - PM Truss resigned
UK’s Resilience

- Ability to bounce back
- Adaptability, agility
  - Political transition
- Pragmatism, Realism
  - but “past empire thinking”
- Civil service
1. Will the UK rejoin the EU single market before 2030?
   - Yes or No

2. Will the Northern Ireland protocol be abandoned?
   - Yes or No

3. Can the UK recover the pre-financial-crisis growth rate of GDP per head?
   - Yes or No

4. UK growth strategy will be most successful if
   - Technology focused (Scandinavian)
   - Tax haven focused (Switzerland)
   - “Bridge to Asia” focused
   - Other focus
What is the matter with Britain?

Martin Wolf, Chief Economics Commentator, Financial Times

Markus’ Academy

30th November 2022
What is the matter with Britain?

1. Nothing much: it is just a declining great power:
   1. Its self-perception lags a generation or two behind reality
   2. It cannot recognise the weaknesses it inherited from past successes
   3. And it suffers from chronic nostalgia

2. Apart from all that
   1. It is still able to get rid of lousy prime ministers without bloodshed
   2. Politically at least, it is far healthier than the US
What is the matter with Britain? Politics

Trump's US lags behind other large high-income democracies

‘Freedom In the World’ aggregate score (0 = least free, 100 = most free), 2018

Source: Freedom House
© FT
What is the matter with Britain?

1. Now for the economic stuff:
   1. Long-run performance
   2. After the financial crisis
   3. What Brexit has done
   4. Challenges
   5. Conclusion
1. Long-run performance: productivity

The UK has not caught up with French or German productivity since 1979

Relative labour productivity (GDP per hour worked, % above/below UK level)

Source: Nicholas Crafts
1. Long-run performance: productivity

Falling productivity in developed economies

Average growth (output per hour) in each decade (% selected countries)

Countries ranked by 2010s’ growth
Source: The Conference Board
© FT
1. Long-run performance: investment

UK investment lags behind other big high-income countries

Source: IMF
© FT
1. Long-run performance: stagnation

The years before the pandemic saw very low growth in output per head and household incomes.

Growth rates over 15-year periods (%)
- Household income* - poorest 10%
- Median income*
- Household income* - richest 10%
- Real GDP per head

* Real non-pensioner household disposable incomes, after housing costs.
Source: Resolution Foundation analysis of data from BoE, OBR, DWP, IFS. © FT.
1. Long-run performance: inequality

The US and UK are league leaders in inequality

Inequality of household disposable incomes after taxes and cash transfers (2016)*

*Measure of inequality (0 = absolute equality, 1= absolute inequality)

Source: OECD
© FT
1. Long-run performance: low tax burden

The UK has a low tax burden relative to many of its peers

Sources: Dan Neidle/Tax Policy Associates, OECD
© FT
2. After the financial crisis: lost output

DEVIATION FROM 1980-2007 TREND GROWTH OF GDP PER HEAD (Actual minus exponential fitted trendline, as a percent of trendline)(Conference Board)
2. After the financial crisis: relative decline

UK incomes have fallen behind those of European peers

Median equilivalised disposable income, before housing costs (€ 000s)

- UK
- Germany
- France
- Netherlands
- Austria

* Adjusted for purchasing power parity
Source: Resolution Foundation, from Eurostat data
© FT
3. What Brexit has done: more decline

The UK has been among the growth laggards since Brexit

Growth in real GDP per head*, 2016 to 2022 (%)

- S Korea
- Netherlands
- US
- Australia
- France
- Sweden
- Italy
- Germany
- UK
- Canada
- Spain
- Japan

* at purchasing power parity
Source: IMF
© FT
3. What Brexit has done: after pandemic

The UK is the only G7 economy still below its pre-pandemic size

Cumulative growth in GDP, Q4 2019 to Q3 2022 (%)

Source: OECD © FT
3. What Brexit has done: weak currency
3. What Brexit has done: lost trade

Trade has been affected since the end of the transition period

Monthly imports/exports ($bn)

UK exports to EU

UK imports from EU

* Doppelganger UK: estimate based on UK remaining in the EU
Source: Jun Du, Aston Business School
© FT
3. What Brexit has done: investment

![Chart showing real business investment peaked at the time of the Brexit referendum.](chart)

Source: ONS © FT
3. What Brexit has done: shifts in migration

Taking back control over the borders has had rather surprising results

Net migration (000s)

- Non-EU
- EU
- British
- Total long-term net migration

Old data collection methodology

Covid-19

Source: ONS. Figures are year ending.
4. Challenges: the moron premium

Hunt & Sunak have removed the ‘moron premium’

UK 10-year gilt, spread over French 10-year bond (%)

Source: Refinitiv
© FT
4. Challenges: falling participation

The UK remains the only developed country in the world where the share of working-age people outside the labour force has kept rising after the initial pandemic shock.

Share of people aged 15-64 who are neither employed nor seeking work (%)
4. Challenges: an exceptional downturn
4. Challenges: inflation
4. Challenges: reliance on strangers
4. Challenges: rising public spending
4. Challenges: debt is not exceptional

![Graph showing net public debt in various countries]

Source: IMF
© FT
4. Challenges: productivity is the big one
4. Challenges: buyers’ remorse

<table>
<thead>
<tr>
<th>Pollster</th>
<th>Fieldwork Dates</th>
<th>Question Type</th>
<th>In EU</th>
<th>Out EU</th>
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</thead>
<tbody>
<tr>
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<td>27-28.10.22</td>
<td>Rejoin/Stay Out</td>
<td>59</td>
<td>41</td>
</tr>
<tr>
<td>Omnisis</td>
<td>3-4.11.22</td>
<td>Rejoin/Stay Out</td>
<td>58</td>
<td>42</td>
</tr>
<tr>
<td>Omnisis</td>
<td>10-11.11.22</td>
<td>Rejoin/Stay Out</td>
<td>57</td>
<td>43</td>
</tr>
<tr>
<td>Omnisis</td>
<td>17-18.11.22</td>
<td>Rejoin/Stay Out</td>
<td>61</td>
<td>39</td>
</tr>
<tr>
<td>Deltapoll</td>
<td>17-19.11.22</td>
<td>Rejoin/Stay Out</td>
<td>56</td>
<td>44</td>
</tr>
<tr>
<td>Omnisis</td>
<td>24.11.22</td>
<td>Rejoin/Stay Out</td>
<td>57</td>
<td>43</td>
</tr>
<tr>
<td>Poll of Polls</td>
<td>-</td>
<td>-</td>
<td>58</td>
<td>42</td>
</tr>
</tbody>
</table>
5. Conclusion

• The long story is one of relative decline
• The Thatcher revolution did not give lasting benefits
• The period after the financial crisis made this clear
• The Brexit referendum and its result was chickens coming home to roost allied to demagogic tomfoolery
• The economy has performed relatively poorly since Brexit
• The energy crisis is big and expensive, but manageable
• The challenges are renewing inclusive growth and resolving Brexit
• Politics will get in the way, because it is a field of nostalgic dreams