The Economic Consequences of the Pandemic

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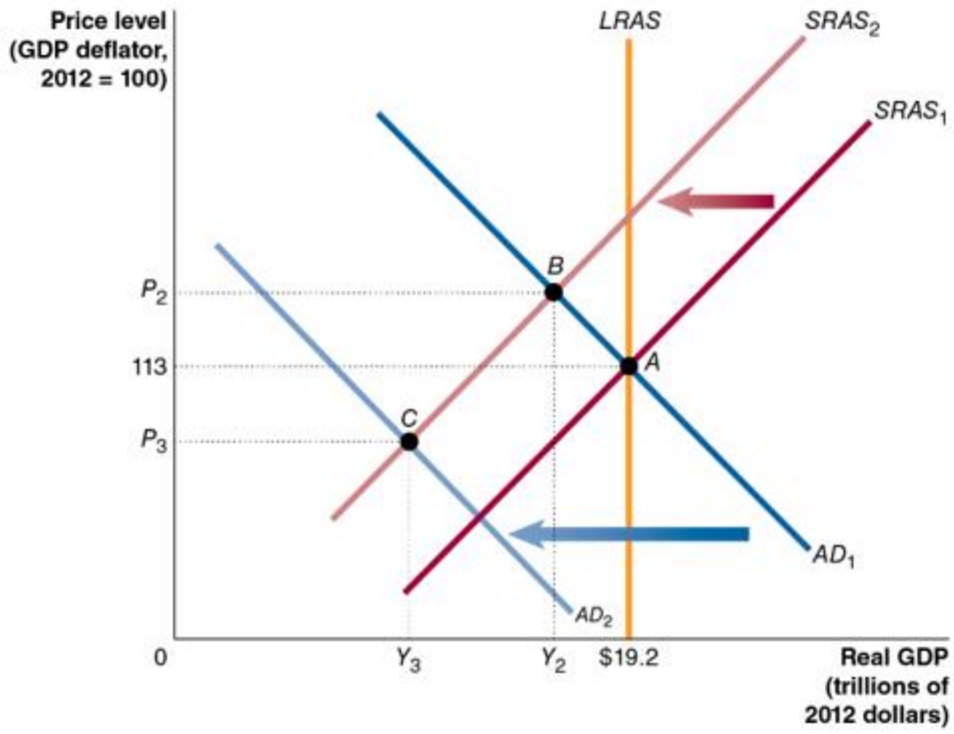
Introduction

- The affects of the pandemic on the economy and housing market.
- The policies adopted by the authorities to reduce the adverse effects of the pandemic.
- The future consequences of the pandemic.

How the economy has been impacted

- Output has fallen substantially.
- Prices have initially fallen, now beginning to rise.
- Financial markets have fallen but recovered recently
- Unemployment has remained stable
- This can be illustrated in a standard AS/AD model.
- House prices in the UK have risen sharply, by about 12% per annum since the pandemic, due to low interest rates and falls in stamp duty (Tax on buying a house).
- House prices have risen in rural parts of the UK faster than cities, such as London.

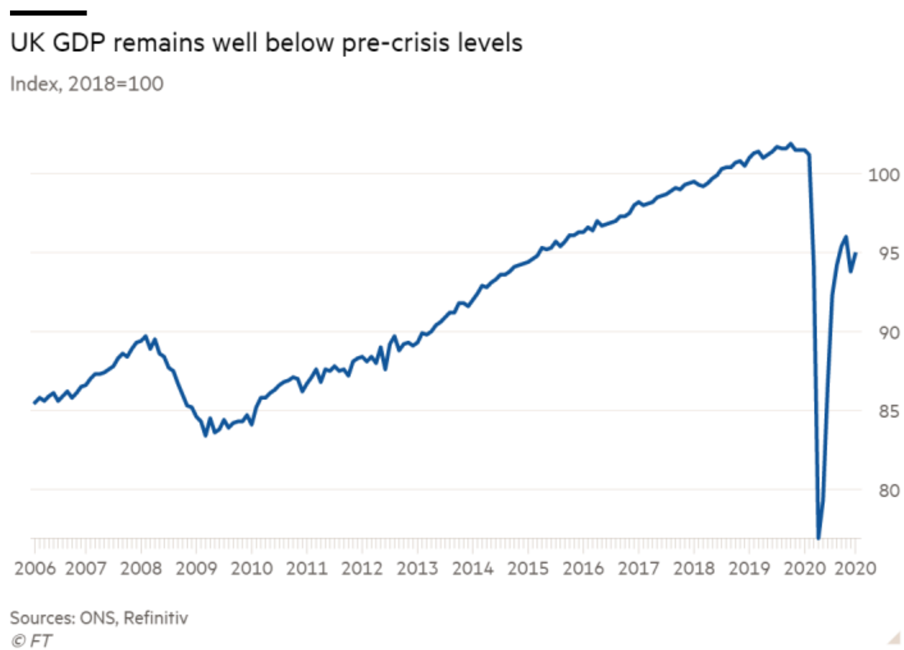
Aggregate Supply and Demand



GDP

- Following the move to lockdown in March 2020, there was initially a sharp fall in GDP, but this has gradually recovered.
- There was a fall of 10% in UK GDP in 2020 overall, the largest for over 300 years.
- UK is forecast to grow by approximately 5% in 2021, well above the trend rate of growth, but not back to the GDP levels pre-pandemic.
- Unemployment initially increased, but due to the various government schemes, it is now back to the pre-pandemic levels.

Fall in UK GDP



Reaction by the Authorities

- The UK government introduced the furlough scheme at the start of lockdown. This essentially involves the government paying most of the wages of workers that are temporarily unemployed.
- Since the scheme started 11.6 million workers have been furloughed for at least a part of the scheme’s existence.
- As of 31st July 2021, 1.6 million staff were on furlough.
- The scheme has been most popular with the travel and hospitality sectors.
- The scheme has cost about £70 billion so far.

Reaction by the Bank of England

- Interest rates have been cut to a historic low of 0.1%
- Quantitative Easing (QE) increased, now standing at approximately £900 billion of mostly government bonds bought by the Bank of England, having started in 2009.
- Next year it is expected that interest rates will rise slightly, perhaps to 0.5%. This will depend on the inflation rate.

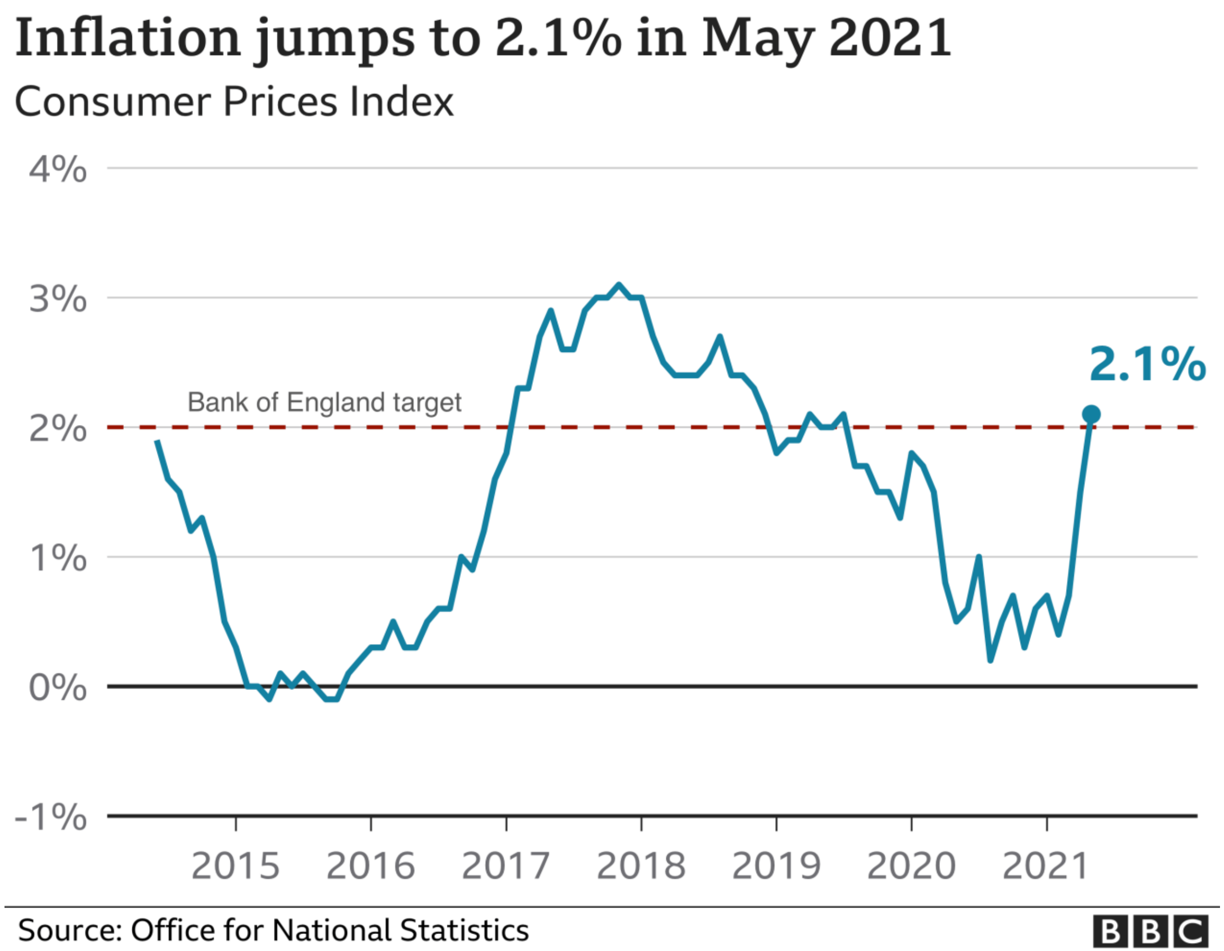
Government borrowing

- The pandemic has cost the government (taxpayer) about £350 billion so far.
- At the end of March 2021, UK government gross debt(borrowings) was £2,225 billion, 106% of annual GDP (ONS). This is the highest since the early 1950s.
- In the year to the end of March 2021, the budget deficit was £304 billion, or 14.5% GDP (ONS).
- The main purchaser of the extra debt has been the Bank of England.

The Future Prospects

- UK inflation is currently 3.2%, above the upper threshold of 3%.
- The Bank of England predicts it will rise to 4% by the end of 2021.
- The Bank of England believes this will be temporary and will then fall to below 3% by the end of 2022.
- In order to reduce inflation, QE needs to end and interest rates rise.
- House prices should stabilise around the UK.
- Also ripple éffect should return, where a rise in house prices in London then ripple out to the UK regions.

UK inflation



The Future Prospects

- Furlough ends in September 2021, unemployment is expected to rise thereafter.
- GDP is expected to recover over the next couple of years.
- However substantial rises in taxes could dampen this recovery.
- Budget deficit forecast to return to more balanced path in years to come.