

Britain: Economy hit by inflation and threat of recession

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There has been a host of statistics in the last few weeks that testify to the increasingly serious impact the financial crisis is having on the British economy and the living conditions of working people. The rise in the cost of living has outstripped pay increases for the first time since the 1990s—meaning that the average person is now officially worse off.

According to the Office for National Statistics, the annual inflation rate has doubled in the last six months, reaching 4.4 percent in July, the largest rise since this index, the Consumer Price Index (CPI), began in 1997. It was much larger than expected and more than double the Treasury's target rate of inflation, raising fears that the Bank of England will raise interest rates. The more broadly based Retail Price Index (RPI) went up by 5 percent in the 12 months to July.

As well as a 26 percent rise in petrol and oil, there has been a 13.7 percent rise in food costs, particularly meat, bread, cereals and vegetables, and a 16 percent rise in utility bills. The rise in the CPI will in turn trigger a 6 percent increase in rail fares next January.

The prices that manufacturers pay for their materials and fuel have risen by a colossal 30.1 percent in the last year. They have posted price increases on their domestic sales of 10.2 percent, the highest since 1982.

Yet the Bank of England had predicted last year that the CPI would reach 2 percent. It has been forced to revise its estimates, and expects inflation to reach 5 percent or more, later this year. Just last May, it had predicted a 3.7 percent inflation rate for the year. Now it recognises that even the 5 percent figure may be optimistic, as the risks are high, particularly if inflation leads to higher wages.

But even more importantly, the Bank has revised its forecast for the economy downwards. It expects zero growth in the economy for the next year, despite a boost from exports as consumer spending and investment tumble.

Mervyn King, the governor of the Bank of England, told a press conference, "There is no point pretending that what is happening is not happening in the world economy—that this unique combination of higher food and energy prices on the one hand and a sharp dislocation in the financial sector on the other—is going to do anything other than make the next year a painful adjustment for the UK economy."

King added that the country faced a period of stagflation. "The next year will be a difficult one, with inflation high and output broadly flat," he said. He noted that since employment prospects were not good, "labour market flexibilities" might offset inflationary pressures.

But he could not avoid pointing out that there was a risk that the economy would spiral downwards into a deep recession. King said that there were "bound" to be one or two quarters of falling output as a result of the credit crunch and rising commodity prices. Furthermore, house prices had further to fall due to the banking sector's inability to raise money in the capital markets and the consequent mortgage drought.

He made it absolutely clear that the Bank would "remain cautious"—code for refusing to lower interest rates to stimulate investment and the economy—despite the fact that wage growth was lower than inflation. "Wages do not make inflation," he said. "It depends upon what happens in firms." In other words, if companies believed that they could pass on their own cost increases onto their customers, second order inflation would appear.

The governor insisted however that "We will come through it; inflation will come down." When asked why he was so confident, King replied, "We will take the action necessary to see that it does."

What this means is that the Bank will raise interest rates to whatever levels are necessary and force the working class to bear the cost of adjustment.

Already unemployment has started to rise. The number

of people claiming unemployment benefit rose for the sixth month in succession, increasing to 864,700. Last month saw the number of new claimants rise at the fastest rate for 16 years. The unemployment rate now stands at 5.4 percent. Total unemployment, including those jobless for more than six months and thus not eligible for unemployment benefit, rose to 1.67 million.

Redundancies rose by 13 percent between April and June. This is likely to rise further with more than 10,000 layoffs announced in the building and financial sectors since the end of June. A number of high profile city centre developments around the country have come to an abrupt halt, while British Land has held off signing construction contracts for the prestige 47-story development for the City of London known as the Cheesegrater.

John Philpott, chief economist at the Chartered Institute of Personnel and Development, said that the rise in unemployment was “gaining worrying momentum.”

Total employment would have fallen had it not been for the increasing number of pensioners taking jobs. Pensioners have been hit by the failure of the state pension to cover even the most basic needs, leaving ever more of those above retirement age in poverty and forcing them to stay in or return to work. The number of pensioners in work has risen by more than two-thirds since 1997 to 1.33 million, meaning that the employment rate for pensioners increased from 7.9 percent to 11.7 percent.

There has been a 47,400 fall in the number of job vacancies to 634,900. The trends illustrate how the credit squeeze and inflation are affecting employment. Particularly hard hit have been vacancies in shops, restaurants and hotels, which fell by 18 percent in the second quarter of the year as consumers have reined in their spending. Vacancies in the construction sector fell by 12.6 percent and in the financial sector by 9.9 percent.

Last week, a report from the British Retail Consortium (BRC) found that the fall in the housing market was affecting the demand for household goods and furnishings on the high street. Annual like-for-like sales were down in July for the fourth time in five months. The BRC said that shoppers were reluctant to spend on non-necessities, and they now included clothes in the non-necessity category. The supermarkets were the only high street traders to report significant growth on July 2007.

With fuel and food prices rocketing, more and more people are falling behind with their mortgage payments and face losing their homes. According to Ministry of Justice figures released a week ago, the number of court

orders for mortgage repossessions rose to 28,568 in the second quarter of 2008, a 24 percent rise on the same period last year and the highest since the second quarter of 1992, when 30,587 court orders for repossession were made.

Adam Sampson, the chief executive of Shelter, the housing and homelessness charity, accused mortgage lenders of “still using repossession as the first, rather than the last resort, despite being urged not to.”

The Ministry of Justice also reported that the number of people facing bankruptcy rose from 17,847 percent in the first quarter of the year to 19,158 in the second quarter, an increase of 5 percent on a year ago. The number of creditor petitions—served by people who are owed money—jumped by 17 percent in the second quarter to 5,625. The number of debtor petitions—personal bankruptcies—climbed nearly 4 percent to 13,533.

According to Standard and Poor’s, the credit rating agency, UK credit card companies are seeing an increasing number of people walking away from the credit card debt. Companies have increased their charge-offs—defined as repayments of principal and interest which they no longer expect to receive—by an average of 6.9 percent in June, up from 6.62 percent in March.

The Bank of England’s warning of a recession sent sterling tumbling against the dollar and the euro. On Friday, the pound fell against the dollar for the eleventh day in succession to \$1.85, down 6.5 percent since July.

Prime Minister Gordon Brown, who used to boast as Chancellor of the Exchequer that he had abolished the cycle of boom and bust, has made it clear that public sector workers will see their pay rise by no more than 2 percent even as prices rise, and has encouraged private employers to similarly limit their pay increases.

While the Labour government has bailed out banks and mortgage lenders on the point of collapse due to their own semi-criminal and reckless policies, it has done and will do nothing to assist the millions of working people struggling with mortgages, rising bills and debt.



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