

## INFLATION AND JOB LOSSES ON THE HORIZON AS BUDGET INCREASES COSTS FOR UK COMPANIES

### *Firms axe investment and hiring plans*

The increase in employer National Insurance contributions and the National Living Wage, along with changes to employment law and increases in business rates are making many firms rethink their hiring and investment plans, with some even planning redundancies. For those in work the extra costs will mean lower wage rises, and some companies also plan to raise prices in order to cover the costs. The heavy and sudden burden is also causing some firms to shelve their investment plans, or shift them overseas, meaning even less job creation.

### *Inflation could go either way*

While muted pay growth, slower hiring and redundancies will all put downward pressure on inflation, some sectors plan to increase their prices. In addition, it is expected that the short run effect of extra government spending will temporarily boost demand, also causing upward pressure on inflation. At present the Bank of England also reflects this view that it is too early to tell which will be the greater effect. However, my view is that it leans more towards the downside. The burden on business is an onerous one and will stifle growth, meaning that demand for investment goods is lower, and muted wages mean that consumer demand is weaker.

### *Causing a threat to longer run growth via lower investment*

In the longer run however, lower investment means that the economy is less able to cope with any excess demand without putting upward pressure in inflation, because workers are less productive and need to work longer and therefore be paid more in order to produce more. This will put longer term upward pressure on inflation which could make it harder for the Bank to reduce interest rates.

### *Trump win may offer some hope, but also poses a risk*

Overall I feel that the outlook for the UK economy is not looking good, with growth prospects muted due to weaker demand for investment, and weaker employment growth leading to weaker consumption. One silver lining is that interest rates would likely come down if this risk materialises or looks likely to. One other ray of hope is that if the US economy holds up under the Trump administration then the UK could benefit from increased trade off the back of a stronger US economy. However, if he does go ahead with his proposed blanket tariffs then the UK could suffer a blow to its exports. Even if the tariffs were not applied to the UK, there are risks here too, as tariffs on other countries and some of Trumps' other proposed policies are inflationary such as decreasing the workforce by deporting illegal immigrants. Cuts to corporation tax should help however, and are already enticing some UK firms to invest in the US, which could see some revenue flowing back to the UK to help support their UK counterparts. However, all these measures are inflationary, which could mean slower rate cuts from the Fed, and may dampen demand from the US somewhat.

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