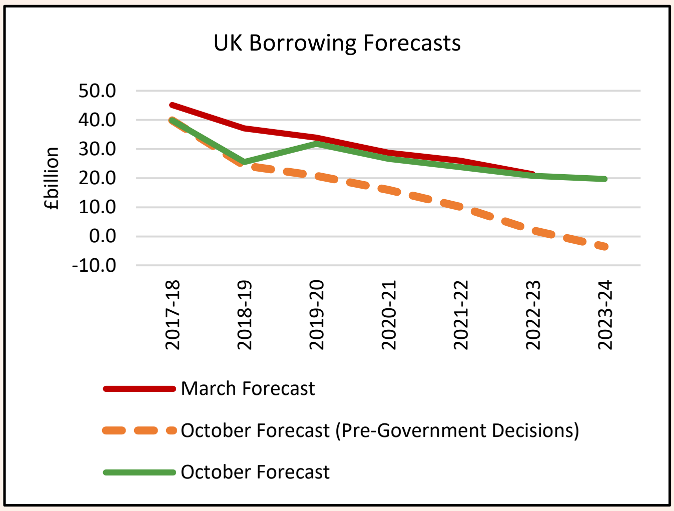
EZY ECONOMICS

THE WEEKLY 5

09/11/18

Here are the five economic stories which have caught our eye this week:

The End of Austerity:



Going into last week's budget, the word 'austerity' was put under the microscope as a result of Theresa May's bold claim that "austerity is ending".

Better than expected tax receipts of £13bn presented the Treasury with a policy dilemma – save the fiscal windfall to help balance the books or re-invest into the economy to fulfil domestic spending pledges.

Fortunately for the British people, the UK Chancellor seemed to respond with a Budget that, at first glance, appeared to loosen the public purse strings and commit to giving away more money to crucial public services such as the NHS.

The Chancellor committed to the biggest increase in fiscal spending since 2010 without accompanying tax rises. However, this came at a cost as government borrowing for the current fiscal year is projected to rise by £1bn and £11bn next year, before rising by as much as £24bn in 2023-24.

Assess the impact that increased spending on public healthcare in the UK is expected to have on its macroeconomic objectives.

A Gloomy Forecast Ahead:

	Bank of England Projections			
	2018	2019	2020	2021
GDP Growth	1.5%	1.7%	1.7%	1.7%
CPI Inflation	2.5%	2.1%	2.1%	2.0%
Unemployment	3.9%	3.9%	3.9%	3.9%
Output Gap	0	+ ¼	+ ¼	+ ½
Bank Rate	0.7%	1.0%	1.2%	1.4%

Last Friday, the Bank of England released their biannual inflation report that aims to assess the outlook for the UK economy in light of changing economic and financial conditions.

Like most economic publications these days, a cloud of Brexit uncertainty shrouded the projections and forecasts made.

The most surprising element of the Bank's publication was the statement that the Bank may continue their path towards tightening UK monetary policy (increasing rates) even in the scenario of a "no-deal" Brexit. Many see a Brexit outcome on WTO terms as potentially a scenario that could tip the economic scales of the UK towards a recession.

Using your knowledge of world trade, why might the Bank decide to increase interest rates even in the event of a no-deal Brexit?

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UK Energy Price Cap:

Energy Price Cap on Standard Variable Tariffs (SVT) up to 2020.

The energy regulator Ofgem confirmed this week the details behind an energy price cap that had been put forward by the UK Government in 2018.

The regulator confirmed that the cap will be brought in from the 1st of January at an initial level of £1,137 per customer. Any energy supplier that currently offers a default energy tariff above the cap will be forced to reduce their tariff rates.

The price cap has been brought in to focus on SVTs – the type of energy bills which have no fixed end date for the consumer and the price paid can fluctuate from month to month. It is estimated that 60% of all UK households are on this form of tariff.

However, the energy providers have criticised this move from the government as they expect it to reduce profits and innovation in the industry, as well as unleashing the unintended consequence of reduced competition.

Evaluate the view that the introduction of price caps in a market is an effective way of controlling monopoly power.

Ubernomics:

Since coming onto the scene in 2009, Uber has long been a fascination for economists not just because of the dynamic nature of their pricing model, but also because of the apparent economic costs and benefits that this service creates and provides. This week a study was produced by the University of Chicago that investigated this matter further.

The study reported that road accidents have increased by 3% for each year since the formation of popular self-riding apps such as Uber, due to heavy congestion in major cities. This has resulted in economic costs of up to $10bn a year due to lost wealth creation.

If you consider the associated economic benefits of lower fares for passengers and higher wages for drivers, it creates a compelling case for cost-benefit analysis.

Define the term ‘economic cost’.

Assess the effectiveness of a congestion tax on controlling some of the economic costs associated with self-riding apps.

Italy’s Rejected Budget Proposals:

The row between the European Union and Italy’s political leaders intensified this week over the coalition government’s expansionary budget plans.

The populist parties that make up the coalition have promised to deliver on a budget that introduces a basic minimum income for each citizen, a reversal in planned state pension ages, simplified tax structures and a cut in the VAT rate.

It is anticipated that these measures will result in the budget deficit in Italy rising to 2.4% of GDP, slightly below the 3% limit imposed by the EU, but significantly higher than planned by the previous Italian Government of 1.4%. The coalition believe that an expansionary budget is what is required to reduce the country’s debt stock of 131% of GDP.

Using an AD-AS diagram, assess how an expansionary budget plan, like this one, might help reduce a country’s national debt in the long-run.