IMF: UK Only G-7 Economy to Face Recession This Year

claudiodivizia/IStock/Getty Images Plus

Britain is poised to face the gloomiest two years of any major industrial nation, with a recession in 2023 and the slowest growth among its peers in 2024, a report from the International Monetary Fund (IMF) asserted.

The country will be the only Group of Seven (G-7) member whose economy will contract this year, shrinking by 0.6 percent, the IMF said.

The Washington-based institution revised its outlook by a considerable 0.9 percentage points from October, stating that higher interest rates and taxes together with government spending restraints will worsen cost-of-living challenges.

This latest IMF forecast reflected the difficulties that Prime Minister Rishi Sunak's government has to tackle prior to the next election. Yet the Chancellor of the Exchequer Jeremy Hunt opined that the economy is likely to fare better than the IMF posited.

"The governor of the Bank of England recently said that any UK recession this year is likely to be shallower than previously predicted," said Hunt.

"We are not immune to the pressures hitting nearly all advanced economies. Short-term challenges should not obscure our long-term prospects."

In 2024, the economy will recover only slowly, growing at 0.9 percent — aligning with Japan and Italy at the bottom of the G-7 league table for growth.

The IMF forecast expects the first British recession, excluding the Covid-19 outbreak, since the financial crisis in 2009. During the two years before the deadline for Sunak to call an election, the economy will basically slow down — expanding just 0.3 percent.

Notably, the IMF did not downgrade any other G-7 economy in 2023 as it increased its global growth forecast from 2.7 percent to 2.9 percent.

The prolonged and escalating conflict in Ukraine or a health catastrophe in China as Covid-19 spreads could undermine the world economy, the IMF said in its World Economic Outlook update. Nonetheless, "adverse risks have moderated since October."

The downgrade to British growth is notable as the IMF's October forecast was prepared before the £45 billion unfunded tax giveaway in last year's September budget during the transient Liz Truss premiership. At the time, the fund claimed that the fiscal splurge would have fuelled growth. Since then, financial restrictions have increased, leading to escalating borrowing costs for businesses and households.

The Bank of England has raised rates from 2.25 percent to 3.5 percent, and markets now anticipate rates to settle around 4.5 percent. Moreover, the IMF said its downgrade showcased a "tighter fiscal" policy. Nevertheless, based on Treasury figures, fiscal policy is looser this year than at the last forecast.

October last year witnessed the IMF lambasting Britain's massive spending spree, saying that fiscal and monetary policy should not be used at cross purposes and that the government had to better manage public finances.

IMF chief economist Pierre-Olivier Gourinchas reiterated the warning. In a blog post, he wrote that many countries are being too magnanimous with their energy support, which is "costly and increasingly unsustainable."

Rather, countries should "adopt targeted measures that conserve fiscal space, allow high energy prices to reduce demand for energy, and avoid overly stimulating the economy," he claimed.

Subsequently, he encouraged central banks, such as the Bank of England, to proceed with rate rises even if such moves would cause more strain to cash-strapped households.

"Where inflation pressures remain too elevated, central banks need to raise real policy rates above the neutral rate and keep them there until underlying inflation is on a decisive declining path," said Gourinchas.

"Easing too early risks undoing all the gains achieved so far."

The same IMF report put Britain's expected performance at a level that was even lower than sanctions-hit Russia, which is projected to expand by 0.3 percent after contracting 2.2 percent in 2022.

Among the other G7 nations, the IMF's 2023 GDP predictions depict growth of 1.4 percent in the United States, 0.1 percent in Germany, 0.7 percent in France, 0.6 percent in Italy, 1.8 percent in Japan, and 1.5 percent in Canada.

The IMF stated that although the outlook for other G7 members had been enhanced or remained the same since October, the forecast for the U.K. looked bleaker owing to rising interest rates and taxes. Furthermore, the government's spending restraint is expected to add fuel to the fire.

"Tighter fiscal and monetary policies and financial conditions and still-high energy retail prices weighing on household budgets" have eroded the country's GDP, the IMF said.

Meanwhile, the IMF reviewed upwards its estimate of Russian economic development, projecting GDP to grow by 0.3 percent this year, and 2.1 percent in 2024.

The fund's World Economic Outlook update stated that Russia's GDP fell by 2.2 percent last year. In its October forecast, the IMF claimed that the decline was expected to be 3.4 percent. For this year, the fund hitherto predicted a drop of 2.3 percent, and for 2024, a 2.1-percent decline.

Observers have pointed out that the IMF's estimates have started to align with Russian forecasts.

"Indeed, the Russian economy is confidently overcoming the sanctions and barriers of unfriendly countries. In 2023, greater economic recovery will hinge on the improvement of consumer demand, as well as policies to facilitate the rise of corporate and consumer lending," the IMF's Ministry of Economic Development stated.

Earlier in January this year, Russian President Vladimir Putin announced that the Russian economy is in better shape than previously expected, and is on track for further stabilization.

Putin elaborated that the Western sanctions and international pressure have failed to severely weaken the economy, saying inflation in Russia in 2022 was 11.9 percent, which was also lower than forecasts, including those of the country’s central bank.

To boot, Putin urged for a “tangible increase” in the salaries for Russian citizens in 2023, stating that rising prices have direct repercussions on the incomes of consumers.

“This is fundamentally important both for the real incomes of citizens and for the economy as a whole,” he stressed.

Alluding to Russian gas producers, Putin stated that they had a good year in 2022.

“At the same time, I note that world gas prices have risen significantly due to the actions of Western countries, and as a result, Russian gas producers and exporters have made a good profit for the past two years and significantly increased payments to the country’s budget system,” Putin said.