UNITED KINGDOM 2021-2022 OUTLOOK

BRIGHTER OUTLOOK THANKS TO THE VACCINE ROLLOUT

22 April 2021

Slavena NAZAROVA

WORKING EVERY DAY IN YOUR INTEREST AND FOR SOCIETY

GROUP ECONOMIC RESEARCH

CONTENTS

SUMMARY OF OUR SCENARIO

BRIGHTER OUTLOOK THANKS TO THE VACCINE ROLLOUT

We have revised upwards 2021 growth (to 5.6% from 4.5% previously) thanks to stronger-than-expected GDP at the turn of the year and faster-than-expected vaccination rollout. The easing of public health restrictions in line with the Government's 22 February Roadmap should permit a rebound in consumption and output from Q2. We expect the easing plan to proceed as planned and do not factor in another Covid wave, which could trigger a renewed lockdown later in the year. Domestically and globally, businesses and consumers have increasingly adapted to public health restrictions. In the UK, GDP in Q4 managed to grow despite the November national lockdown that was put in place in England and the social distancing measures that prevailed during the whole quarter across the country. Government support to businesses and consumers has been extended to September and strong fiscal incentives for this year and next have been announced in favour of business investment.

Consumer and business confidence suggest a sharp rebound in consumption and activity in the coming months. We expect still a partial recovery in Q2 as the lockdown is eased gradually, followed by a peak of growth in Q3 as the Government aims for an end of all social restrictions. In our scenario, GDP recovers to its pre-crisis level in Q122.

We expect activity to contract by 1.6% QoQ in Q1 (against -4% QoQ expected by the BoE). In January, GDP came in higher than expected (-2.2% MoM) despite the government implementing a strict national lockdown similar to the one put in place in Q220 and despite acute post-Brexit trade frictions that led to exports to the EU plummeting in January (-45% MoM in volume terms). Activity rebounded by 0.4% MoM in February as the services sector returned to growth thanks to a slight pick-up in wholesale and retail trade.

Risks to the recovery seem more balanced than before but still biased to the downside. To the upside, there is a risk that households resume normal spending behavior earlier than expected and might decide to run down a greater proportion of their accumulated savings. To the downside, risks from Covid-19 remain substantial: delays in the vaccination programs globally, emergence of vaccine-resistant variants of the virus and a possibility of further periods of restrictions on economic activity. Besides Covid, Brexit remains a source of uncertainty as the private sector continues to adapt to the new barriers to trade amidst persistent tensions between the EU and the UK. The Scottish parliamentary election on 6 May represents another idiosyncratic risk for the UK as it will likely result in a pro-independence majority with the SNP confirming its first place in the Scottish parliament.

Against the background of largely positive news regarding the near-term outlook, the BoE has shifted its stance and now appears more as positioning itself at the hawkish spectrum of global central banks. While it was still contemplating the possibility of negative interest rates at the end of last year it now appears confident in its plan to reduce the pace of asset purchases as soon as this year. **Therefore, we no longer expect more QE to be announced in May when the next MPC meeting will take place.**

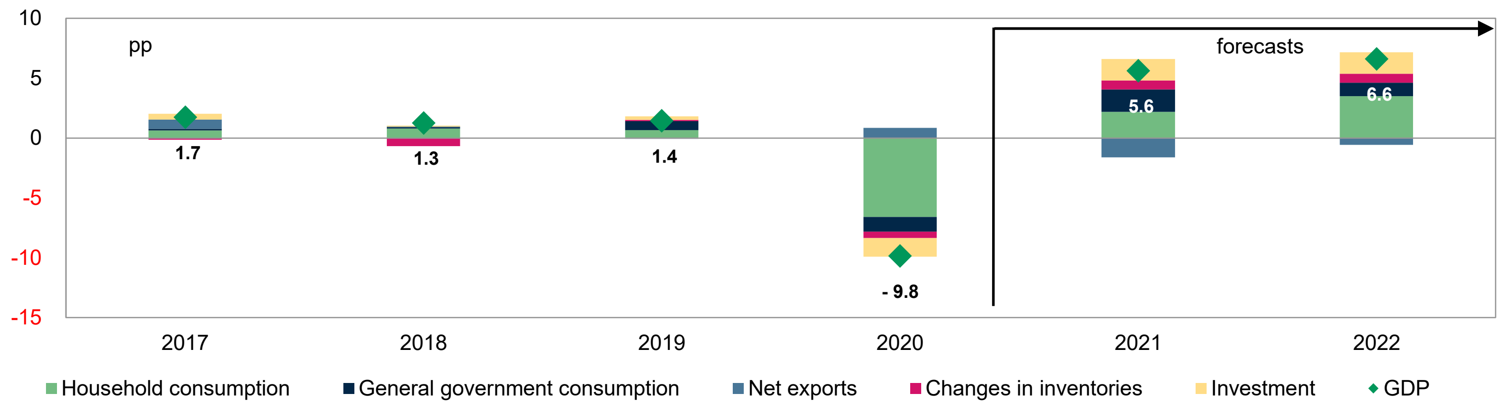
The BoE is currently reviewing its exit strategy, which may be announced in the coming months. This is likely to involve an unwinding of the QE program before an increase in rates, representing a reversal of the current forward guidance.

However, we still see the risks tilted towards a further extension of the QE later in the year, especially if growth disappoints. Indeed, if the BoE sticks to its current QE plan (stock of purchased gilts at GBP875bn at the end of 2021), it will need to almost halve the pace of purchases after the May meeting (from GB4.4bn per week to GBP2.3bn per week) or cut them even further later on. This could result in unwarranted tightening in financial conditions, which in turn will weigh on prospects for CPI inflation (which, for the time being, the BoE continues to see close to 2% at the two-three year horizon).

SUMMARY OF OUR SCENARIO

FORECASTS

Contributions to annual GDP growth



Sources: ONS, Crédit Agricole SA/ ECO

United Kingdom	2019	2020	2021	2022	2020				2021				2022			
					Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
GDP (%)	1.4	-9.8	5.6	6.6	-2.8	-19.5	16.9	1.3	-1.6	2.0	3.9	2.5	1.4	0.5	0.5	0.4
household consumption	1.1	-10.6	3.6	5.8	-2.6	-20.8	19.7	-1.7	-1.9	2.6	2.6	2.5	1.2	0.5	0.5	0.3
public consumption	4.0	-6.5	9.5	5.6	-1.8	-17.3	15.8	6.7	-2.0	3.0	3.0	1.0	1.0	1.0	1.0	1.0
investment	1.5	-8.8	9.9	9.5	-1.2	-20.7	19.0	4.4	0.0	2.0	3.0	3.0	2.0	2.0	2.0	2.0
change in inventories*	0.1	-0.5	0.7	0.7	0.1	-0.7	0.5	1.4	-0.8	-0.2	1.2	0.0	0.2	0.0	0.0	0.0
net exports*	-0.1	0.8	-1.6	-0.6	-2.5	3.4	-4.4	-1.5	0.7	-0.4	-0.1	0.2	-0.1	-0.3	-0.4	-0.4
Unemployment rate (ILO)	3.8	4.6	5.5	5.7	4.0	4.3	4.9	5.1	5.1	5.2	5.5	6.2	5.9	5.8	5.6	5.4
Inflation (CPI, YoY%)	1.8	0.9	1.4	2.0	1.7	0.6	0.6	0.5	0.6	1.5	1.5	2.0	2.0	2.0	2.1	2.0
Core CPI (YoY%)	1.7	1.4	1.5	2.0	1.6	1.4	1.3	1.3	1.1	1.5	1.5	1.8	1.9	2.1	2.1	2.0
Current account (% GDP)	-3.1	-3.5	-5.3	-4.6	-3.5	-3.0	-2.6	-4.8								
General gov. balance, % GDP	-2.3	-14.2	-9.3	-4.1	na	na	na	na	na	na	na	na	na	na	na	na
Public debt % GDP	85.4	102.2	107.6	103.6	na	na	na	na	na	na	na	na	na	na	na	na
Bank rate**	0.75	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Target of BoE's asset purchases (bn £)	435	895	895	895	645	745	745	895	895	895	895	895	895	895	895	895

** Contributions to GDP growth*

*** End of period*

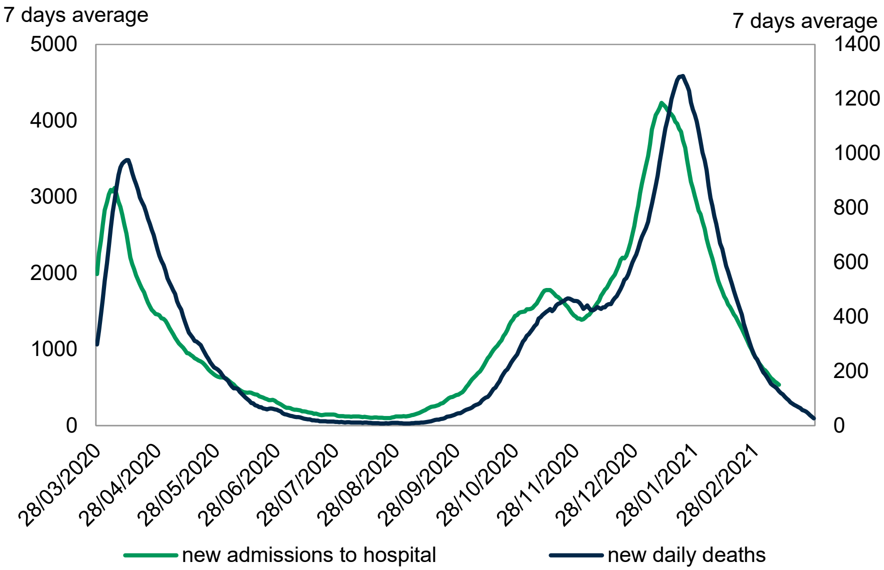
Source: ONS, BoE, Crédit Agricole S.A.

CONTENTS

HEALTH SITUATION

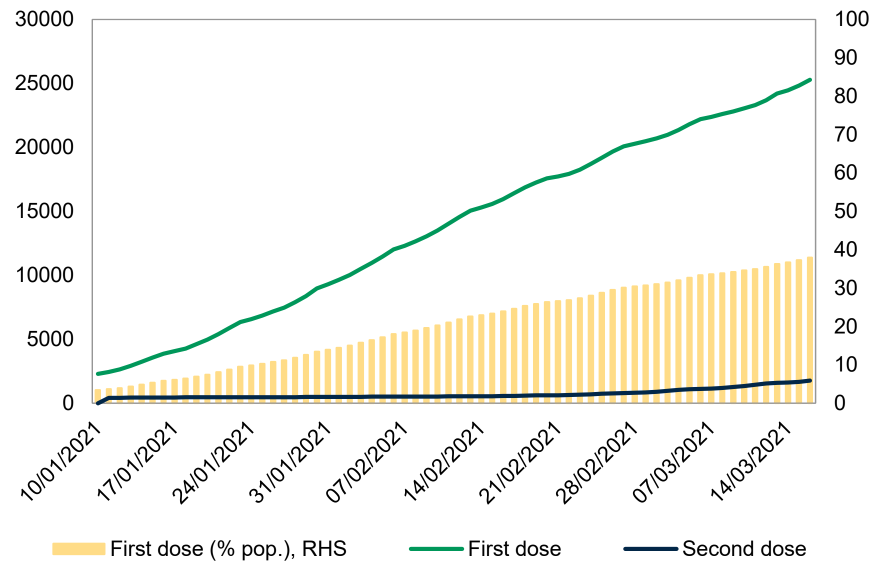
THE PUBLIC HEALTH OUTLOOK REMAINS CONSTRUCTIVE

The health crisis has been brought under control



Source: gov.uk, Crédit Agricole SA / ECO

More than 30 mn persons (45% of total population) have received one dose of vaccine



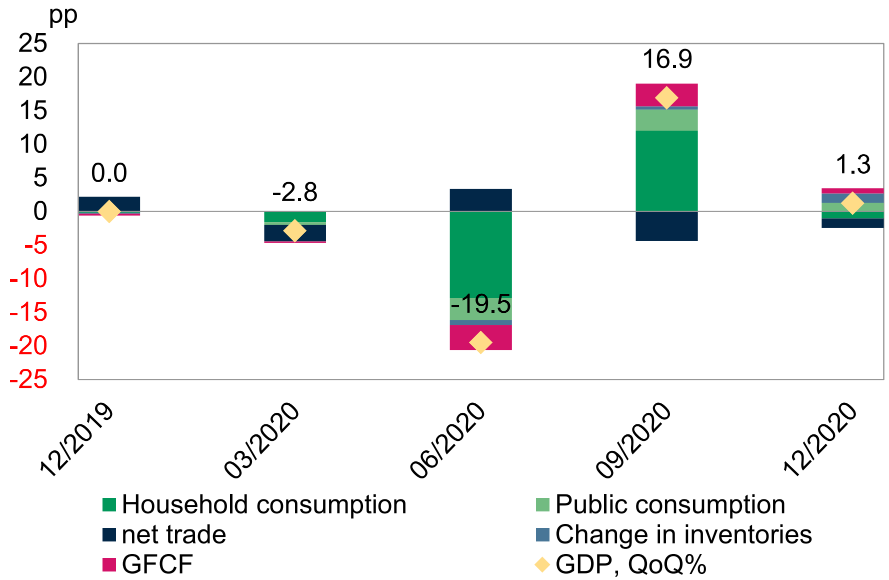
Source: gov.uk, Crédit Agricole SA / ECO

The government announced a prudent lockdown easing plan in January. It started on 8 March with the reopening of primary schools and colleges. Another series of restrictions followed on 12 April including the reopening of non-essential shops, outdoor hospitality and personal services. The earliest date for any further easing is 17 May concerning indoor hospitality and some international travel. The government's easing plan aims for full reopening of the economy on 21 June at the earliest. Covid case numbers and hospitalisations in the UK are now at a similar level to early September after continued reductions in recent weeks. **The vaccination programme is proceeding apace: 32 million adults have now received one dose (including all over 50s) and 7.5 million have been fully inoculated with both doses. The government aims to offer a first dose to all adults by the end of July.** As the economy reopens, case numbers are likely to climb again. However, we expect the easing plan to proceed as planned and do not factor in another Covid wave which would trigger a renewed lockdown later in the year.

LATEST ECONOMIC TRENDS

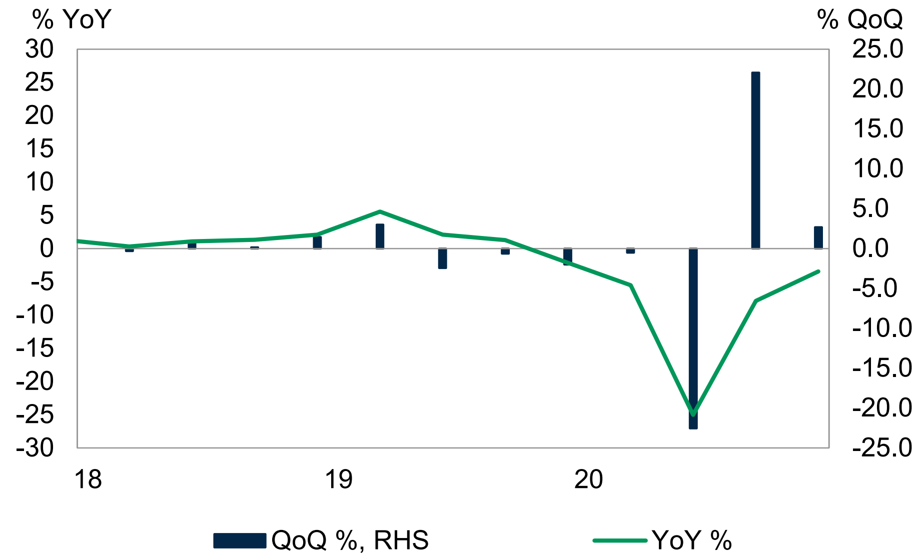
DOMESTIC DEMAND MORE RESILIENT TO COVID-19 RESTRICTIONS

Contributions to quarterly GDP growth: expenditure breakdown



Sources: ONS, Crédit Agricole SA / ECO

Growth of domestic demand



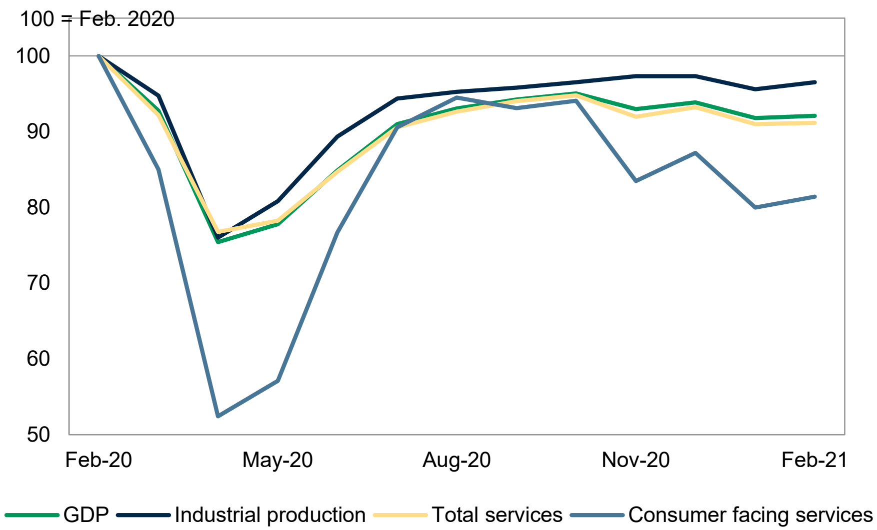
Sources: ONS, Crédit Agricole SA / ECO

GDP growth was stronger than expected in Q4. Despite the national lockdown that was put in place in England in November and the strict social distancing measures that prevailed in the whole UK during Q4, GDP growth remained positive. **Initially estimated at 1% QoQ, Q4 growth was subsequently revised upwards to 1.3%.** Q4 saw resilience in household consumption (-1.7% QoQ), an unexpectedly strong rebound in business investment (5.9%), a huge stock rebuilding ahead of the end of the transition period (contributing for 1.4 pp to GDP growth) as well as very strong public consumption (6.7% QoQ). Net trade contributed negatively (-1.5pp) owing to stronger import growth (+11% QoQ) than export growth (+6.1 QoQ). GDP growth was also more resilient than expected in January (-2.9% MoM) despite the third lockdown announced on 4 January which was of similar degree of stringency as the Q2-2020 lockdown. Schools were closed until 8 March and non-essential stores until 12 April. **The relative resilience of domestic demand, suggests that consumers and businesses have adapted to social restrictions and the UK will probably experience a more limited contraction in Q1 than initially feared.** We expect -2.4% QoQ but a higher number would not come as a surprise.

LATEST ECONOMIC TRENDS

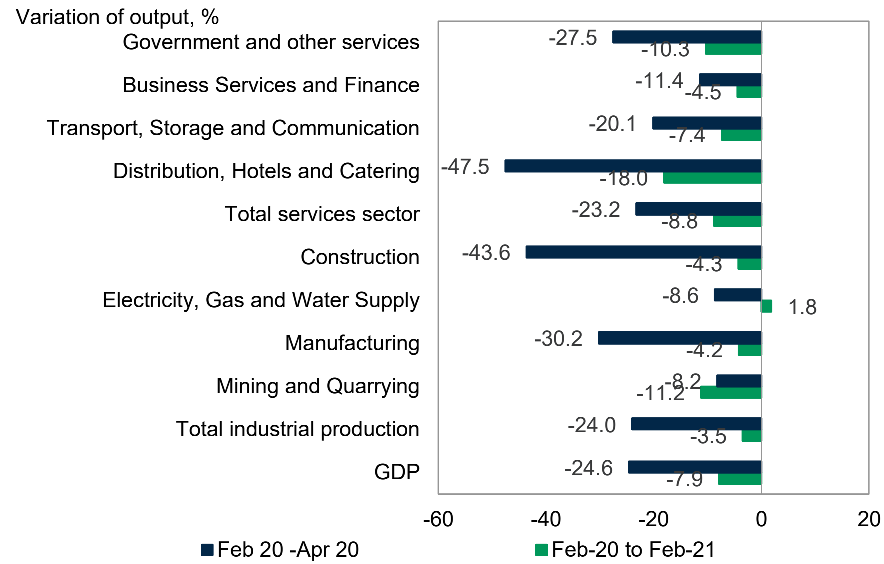
ACTIVITY RETURNED TO GROWTH IN FEBRUARY WHILE THE LOCKDOWN REMAINED IN PLACE

Output growth weighed down by consumer-facing service industries



Sources: ONS, Crédit Agricole SA / ECO

All main sectors remains below their pre-pandemic peak



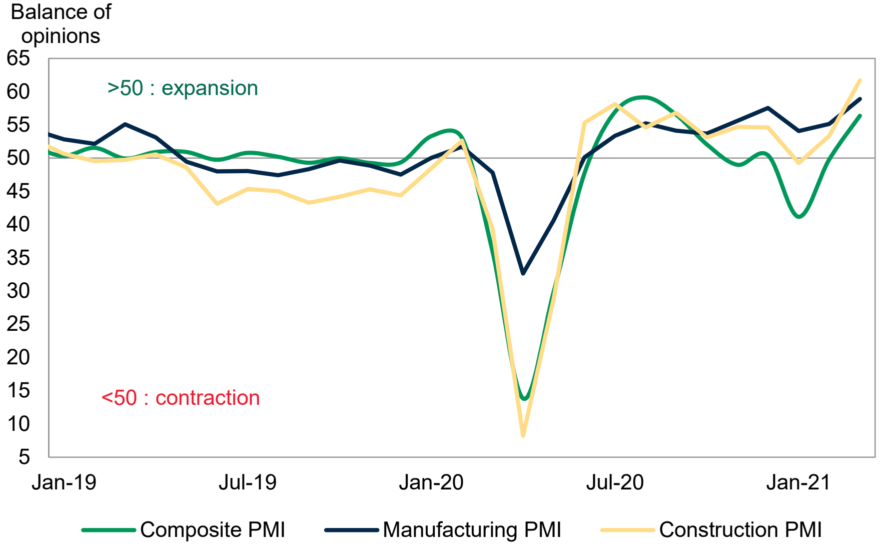
Sources: ONS, Crédit Agricole SA / ECO

GDP grew by 0.4% in February 2021 following a revised fall in January at -2.2% MoM. GDP was 7.8% below its level seen in February 2020 and 3.1% below levels seen in October 2020, the initial recovery peak. Output in the services sector grew by just 0.2% MoM in February as COVID-19 restrictions remained largely unchanged; this follows negative 2.5% growth in January 2021. The largest contributor to growth in services output in February 2021 was wholesale and retail trade as sales picked up slightly. **One year on, output in consumer-facing service industries (retail trade, food and beverage serving activities, travel and transport, and entertainment and recreation) remains almost 20% below pre-pandemic levels.** Overall, all main sectors of GDP remain below their pre-pandemic (February 2020) levels, but only services remain notably lower than the initial recovery peak in October 2020 (-3.9%). Industrial production is flat relative to October 2020, as a 1.8% MoM contraction in January was followed by a 1% MoM rebound in February. .

LATEST ECONOMIC TRENDS

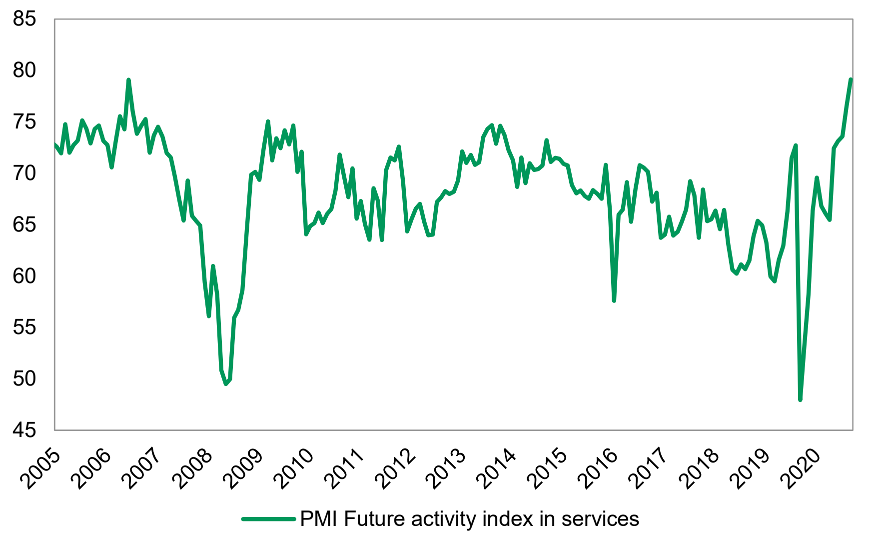
STRONG REBOUND IN BUSINESS CONFIDENCE AHEAD OF PHASE 2 OF LOCKDOWN EASING

PMI surveys firmly in expansion territory in March



Sources: IHS Markit, Crédit Agricole SA / ECO

In the services sector, optimism rose to its highest level since December 2006



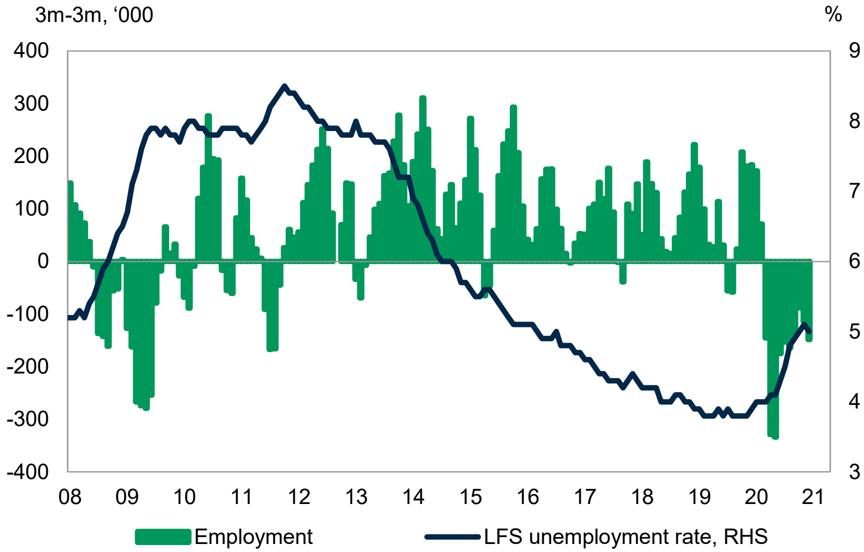
Sources: IHS Markit, Crédit Agricole SA / ECO

The services sector reported a strong rebound in business conditions during March, with activity, new orders and employment all picking up as England was preparing for phase 2 of the lockdown easing road map (reopening of outdoor hospitality, non-essential businesses and personal care services on 12 April). At 56.3 in March, up sharply from 49.5 in February, the headline UK services PMI Business Activity Index posted above the 50 no-change mark for the first time since October 2020. Renewed job creation in March represented the first overall expansion of staffing numbers across the service sector since the start of the coronavirus pandemic. Output expansion was the strongest for seven months. New orders picked up sharply despite a sustained reduction in export sales. **According to IHS Markit, subdued orders from abroad were typically attributed to either international travel restrictions or Brexit issues with sales to EU customers.** Nevertheless, the forthcoming easing of government stringency measures contributed to another improvement in business expectations for the year ahead. This Future Activity index signalled the strongest optimism since December 2006.

LATEST ECONOMIC TRENDS

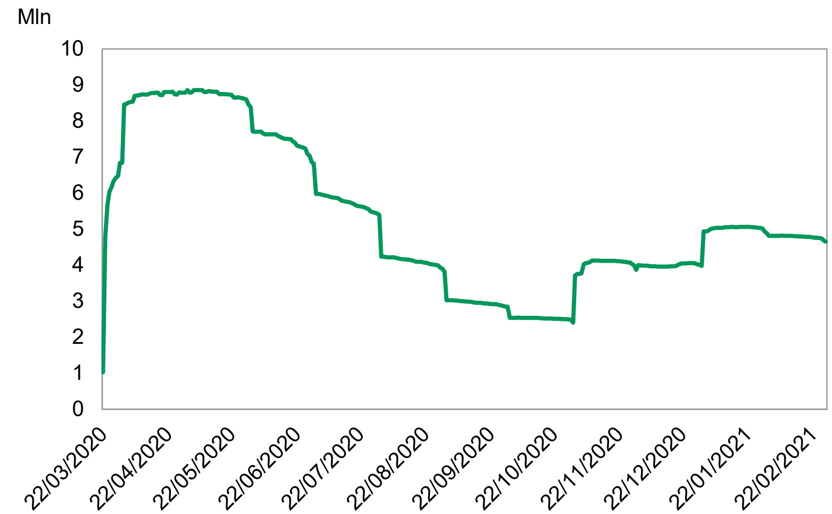
LABOUR MARKET CONDITIONS: STABILISATION

Employment variation and unemployment rate



Sources: ONS, Crédit Agicole SA / ECO

Number of jobs furloughed



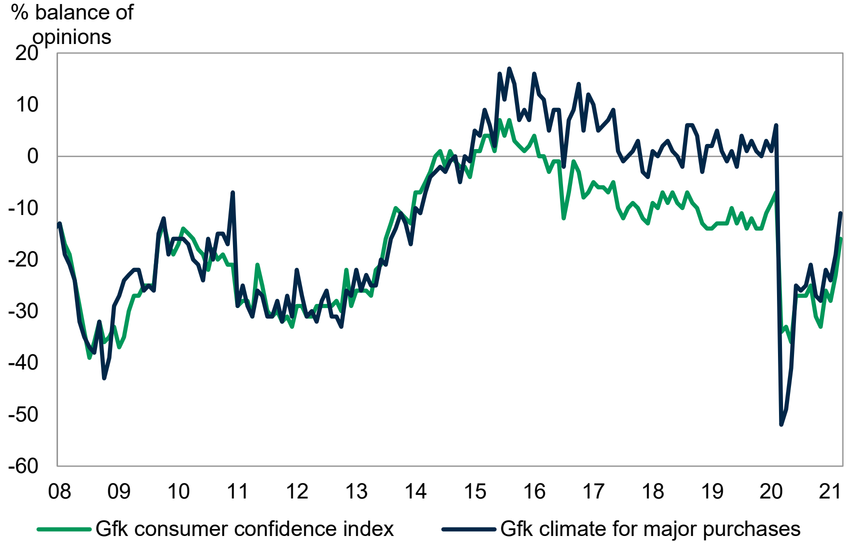
Sources: HMRC, Crédit Agricole SA / ECO

The extension of the government's employment support schemes to the end of September 2021 implies that the near-term rise in LFS unemployment is likely to be more moderate than expected previously. We now expect the unemployment rate to peak to 6.2% un Q4-21 from 5% currently (three months to January). As the BoE has pointed out, the support from the Government's employment schemes will still be available when the economic recovery is expected to be proceeding strongly. Therefore, the risk of currently furloughed workers not being reintegrated smoothly into the labour force was reduced. **Labour market slack remains substantial.** According to HMRC administrative data, 4.9 million jobs had been furloughed at the end of January, higher than in 2020 Q4 (4 million), but lower than during the first phase of the pandemic last spring (peaking at 8.9 million in May). In February, expectations are for a similar level of the number of furloughed employees as in January.

LATEST ECONOMIC TRENDS

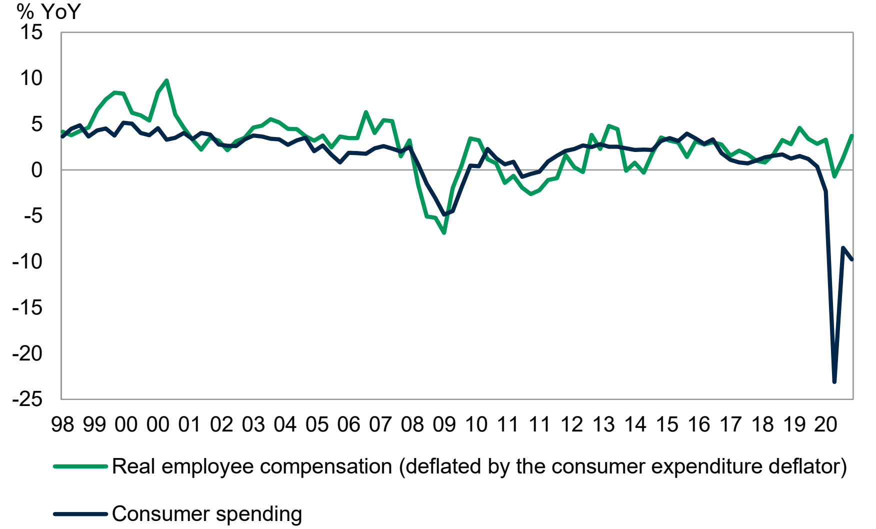
CONSUMER CONFIDENCE PICKED UP SHARPLY

Consumer confidence rises to its highest since the beginning of the crisis



Sources: Thomson Reuters, Crédit Agricole SA / ECO

There is a potential for a strong rebound in household consumption



Sources: ONS, Crédit Agricole SA / ECO

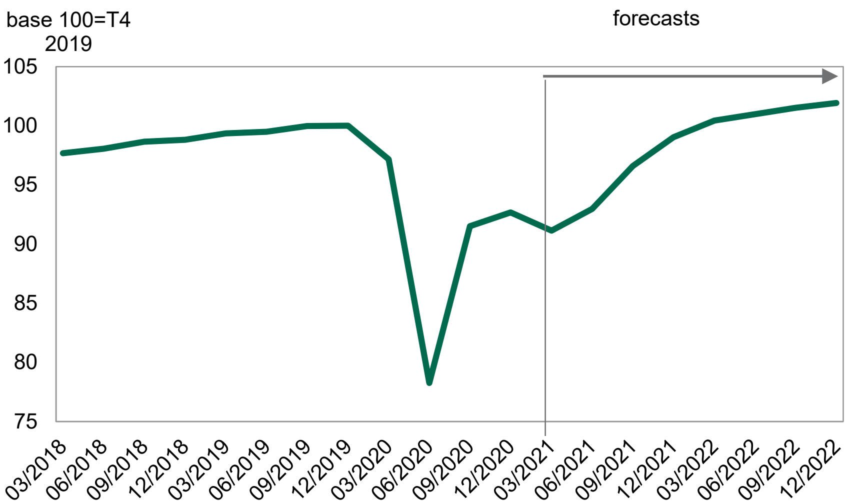
Household consumption fell by 1.7% QoQ in Q4 and we expect another sharp fall in Q1 of close to 2% QoQ, still much less pronounced than the fall registered in Q220 (-20.8% QoQ). Meanwhile, consumer purchasing power has remained positive with growth in real gross disposable income estimated at 0.8% YoY in Q420. **Positive real compensation growth alongside a very high savings rate suggest a potential for strong rebound in consumption in the near term.** Beyond the initial rebound triggered by the easing of health restrictions, we believe that some cautiousness will persist as the virus has not disappeared. **Hence, we expect the recovery in household consumption to be incomplete resulting in a saving ratio that remains above its pre-crisis levels.** After having fallen to 13.9% in Q3, the savings ratio rebounded to 15.6% in Q420 and is likely to increase further in Q1 as household consumption was restrained by the national lockdown. High savings may support consumption more than expected provided that confidence continues to improve.

CONTENTS

THE BASIS OF OUR SCENARIO

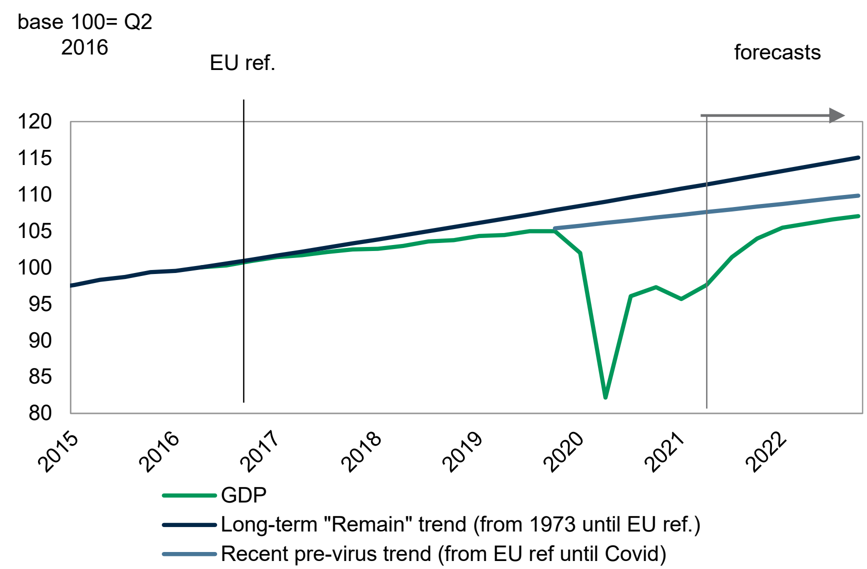
ACTIVITY GETS BACK TO NORMAL EARLIER THAN EXPECTED

GDP forecast to get back to pre-crisis levels in Q1-2022



Sources: ONS Crédit Agricole SA / ECO

But there is a permanent relative to trends prior to the EU referendum and prior to Covid-19



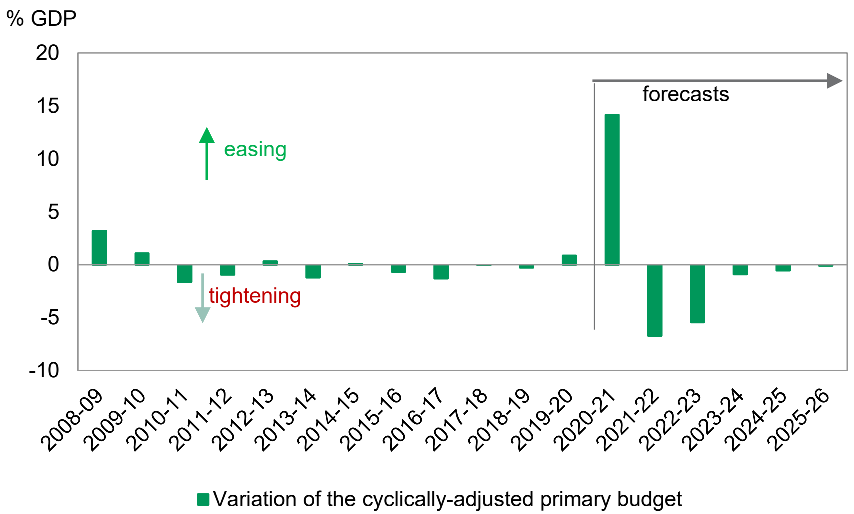
Sources: ONS Crédit Agricole SA / ECO

The rapid rollout of vaccines, the easing of public health restrictions and the extension of the budget stimulus is expected to fuel a more rapid recovery in output than in our December forecast. **GDP returns to its pre-pandemic levels early 2022, nine months earlier than previously expected.** After a contraction of around -1.6% expected in Q1, the recovery is likely to accelerate in the coming months, peaking in Q3 as social restrictions are lifted and the initial shock of Brexit dissipates. However, this does not mean a return to the pre-crisis normal. The supply capacity, the labour market, the corporate balance sheets and the public finances will be in a severely damaged situation. The unemployment rate is still expected to rise with a peak at 6.2% in Q421 (against 7.5% in Q2 expected in December). **This year, we expect the recovery to be led by consumers, the government (spending and investment) as well as business investment.** The latter is boosted by the strong temporary fiscal incentives announced in the March Budget. As per our forecasts, at end-2022, GDP would still be around 2.6% below its pre-Covid trend, and 7% below its long-term trend prior to the EU referendum.

THE BASIS OF OUR SCENARIO

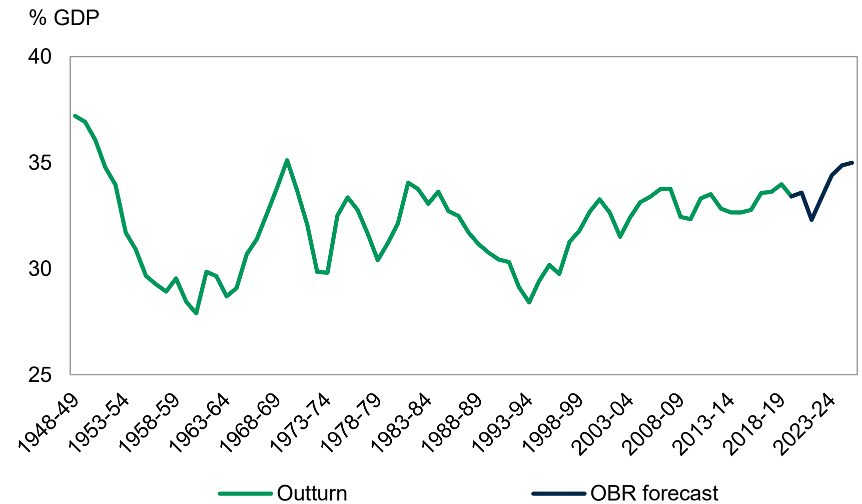
BUDGET GIVEAWAYS IN THE NEAR TERM, BUT TAX RISES ARE PLANNED IN THE MEDIUM TERM

Budgetary impulse becomes negative from FY 2021-22



Sources: OBR, Crédit Agricole SA / ECO

Tax as a share of nominal GDP set to rise to 35% in FY 2025/26, highest since the 1960s



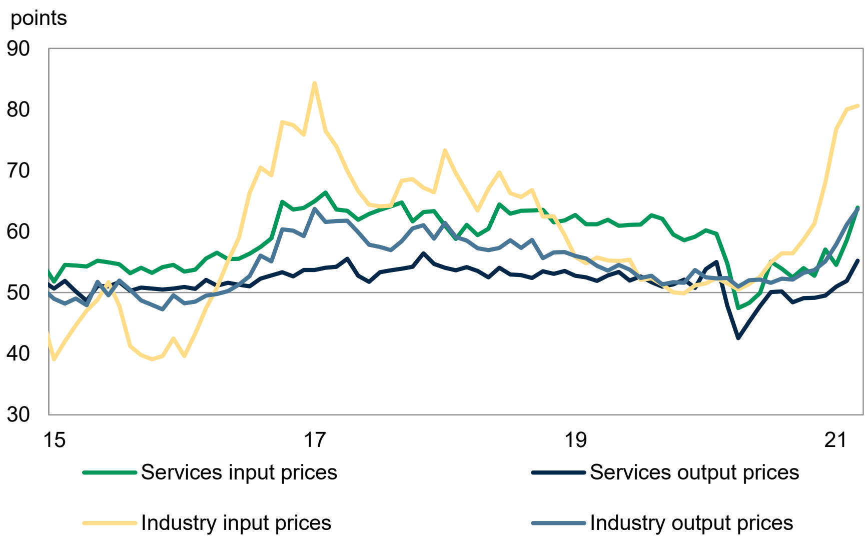
Sources: OBR, Crédit Agricole SA / ECO

The Budget on 3 March delivered three key things. First, **an extension of pandemic-related support to households, businesses and public services by a further GBP44.3bn, taking its total cost to GBP344bn.** Second, an investment-driven boost to the recovery, most notably through a temporary tax break costing more than GBP12bn a year that encourages businesses to bring forward investment spending from the future into this year and next. Third, a step to repair the damage to the public finances in the final three years of the forecast when the economy is expected to normalize, by raising the headline corporation tax rate (from 19% to 25% in April 2023), freezing personal tax allowances and thresholds (April 2022), and cutting departmental spending plans by GBP4bn per year to a total of GBP31.8bn in 2025-26. The pandemic has also pushed government borrowing up to a post-war high and debt to its highest level in sixty years. **In 2020-21, public sector net borrowing is forecast to reach 16.9% of GDP (GBP355bn), its highest level since 1944-45 and public sector net debt to rise to 100.2 % GDP, its highest level since 1960-61**. Most of the GBP298bn increase in borrowing this year is due to an unprecedented peacetime expansion in government spending, with the full-year cost of the Government's virus-related support to public services, households, and businesses reaching GBP250bn this financial year and GBP344bn in total.

THE BASIS OF OUR SCENARIO

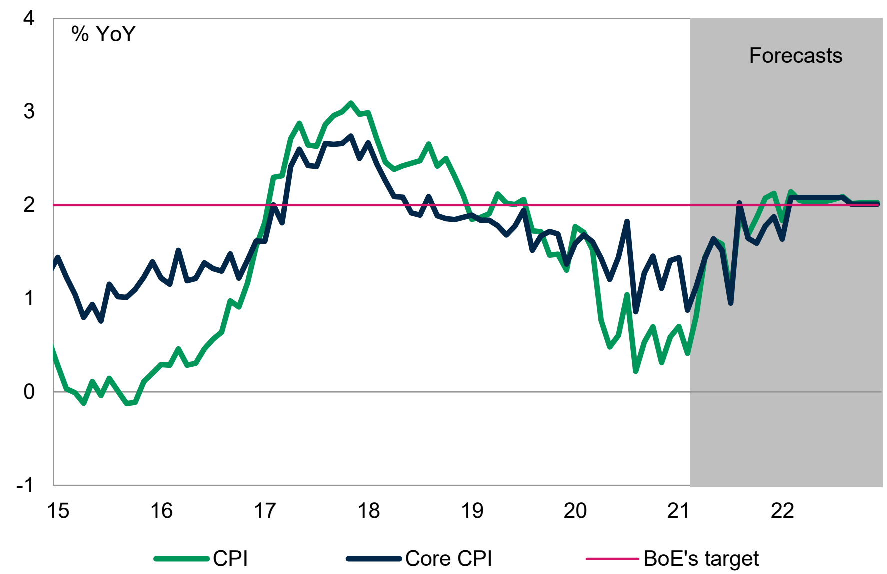
INFLATION: DOWNWARD REVISIONS, BUT STILL BACK TO TARGET BY THE END OF THE YEAR

PMI cost pressures



Sources: IHS Markit, Crédit Agricole SA / ECO

A volatile upward path towards target

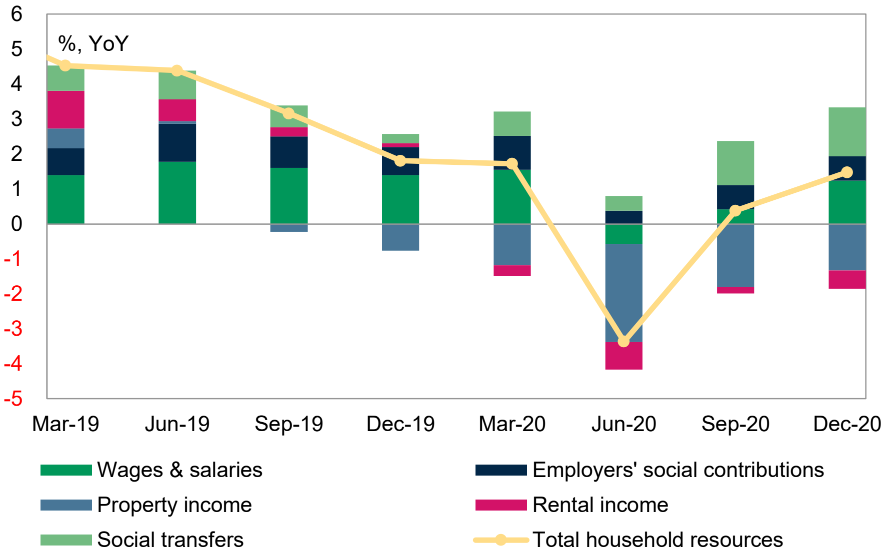


Sources: ONS, Crédit Agricole SA / ECO

CPI inflation was unexpectedly weak in February, dropping to 0.4% YoY from 0.7% YoY (consensus: 0.8% YoY) with core inflation falling to 0.9% YoY from 1.4% YoY in January. **Unusually weak prices of clothing and shoes for this time of the year (-5.7% YoY) contribute the most to the fall of inflation as well as a drag from recreation and culture.** These negative contributions more than offset the positive impact of moderating deflation of energy prices (-5.9% YoY). Going forward, we continue to expect a rebound in CPI inflation in Q2 due to rising energy prices, base effects related to the decline in oil prices last year and the revival in consumer demand with the reopening of the economy. However; **the near-term forecast is lower than before due to the downside surprise in actual data and the extension of the reduced VAT in the tourism and hospitality sectors.** The 5% VAT rate now runs until the end of September, rather than the end of March. Then, a 12.5% rate will apply until March next year. Headline inflation is expected to rise to 1.6% YoY in Q2 (compared to 1.9% YoY before) and to 2.1% in Q4 (2.3% previously). During 2022, we see inflation hovering around 2%.

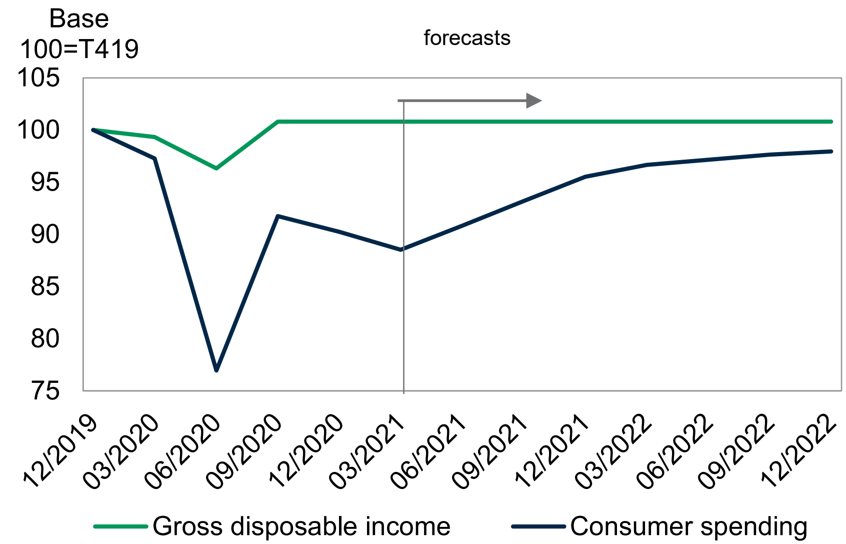
HOUSEHOLD CONSUMPTION: WE EXPECT AN INCOMPLETE RECOVERY BY THE END OF 2022

Social transfers have continued to shield incomes against weaker wage growth



Sources: ONS, Crédit Agricole SA / ECO

Household consumption and gross disposable income

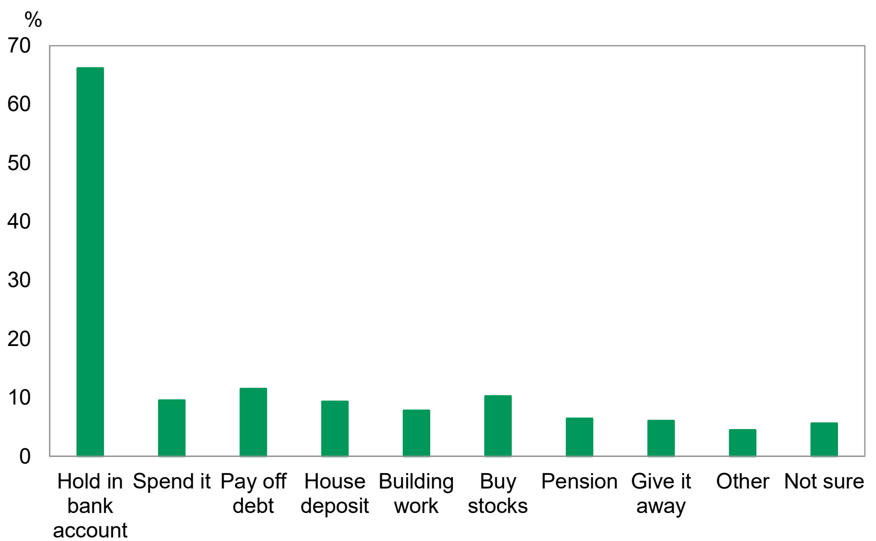


Sources: ONS, Crédit Agricole SA / ECO

We expect an incomplete recovery in household consumption over our forecast horizon (with a shortfall of 1.5% at the end of 2022 relative to Q419). It is true that the easing of social restrictions is likely to trigger a sharp rebound in household consumption in the near term. The rebound is likely to be led by the services sector. Unfortunately there have been growing concerns recently that the South African variant which is now spreading in the UK, is resistant to the vaccines. Indeed, there have been several reported cases of the South African variant among people who have received at least one dose of either the AstraZeneca or the Pfizer jab. The outbreak is likely to remain contained in the summer months, but a resurgence is possible next autumn/winter. Hence, even if the Government's 22 February Roadmap is implemented as expected and all social restrictions are lifted on 21 June, some social distancing is likely to persist, weighing on consumption in social services involving strong physical contact. In 2022, the prospects of tax rises and freezing in the income tax thresholds are likely to further weigh on consumer spending.

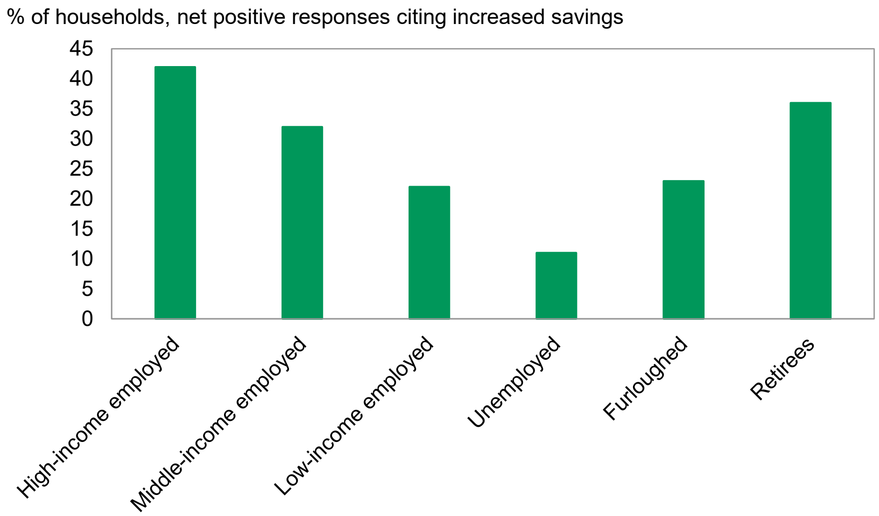
HOUSEHOLD CONSUMPTION: UPSIDE RISK FROM SAVINGS MAY BE OVERSTATED

What do households plan to do with additional savings built up during the pandemic ?



Sources: OBR, Bank of England NMG Survey, Crédit Agricole SA / ECO

The accumulation of saving has been concentrated among wealthier and less financially distressed households

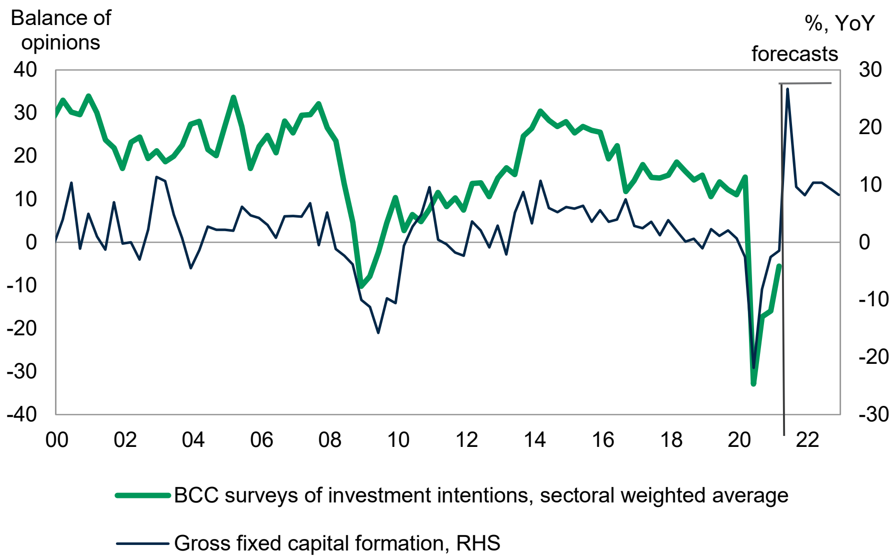


Sources: Bank of England, Crédit Agricole SA / ECO

There are upside risks to household consumption stemming from unprecedented high levels of accumulated savings during the crisis. BoE's data on household deposits suggest that between March and November 2020, consumers accumulated a stock of over GBP125bn in excess of normal times. This stock of savings is likely to rise further in Q121. The OBR expects it to reach GBP180bn by the middle of 2022, representing a potential boost of 6% to household consumption in 2021 and 2022, according to its estimates, were it to be spent in the next four quarters. That said, a substantial post-crisis rebound in household consumption can still be achieved without eroding the stock of savings, but by simply lowering the savings ratio from its current highs. Survey evidence shows that the large majority of households intend to keep their savings in their bank account. **The majority of households do not expect to increase their spending relative to pre-pandemic levels once restrictions are lifted.** Only just over 10% of households expect to spend more than before the pandemic began, according to the BoE. By contrast, over 25% of people expect to spend less once restrictions have been lifted than before the pandemic began. Moreover, the recent rise in savings has not been equally distributed across households. Evidence shows that it has been the result of high-income and mostly older households who already have sizable savings. They are unlikely to spend their extra savings but rather invest it in financial or housing assets.

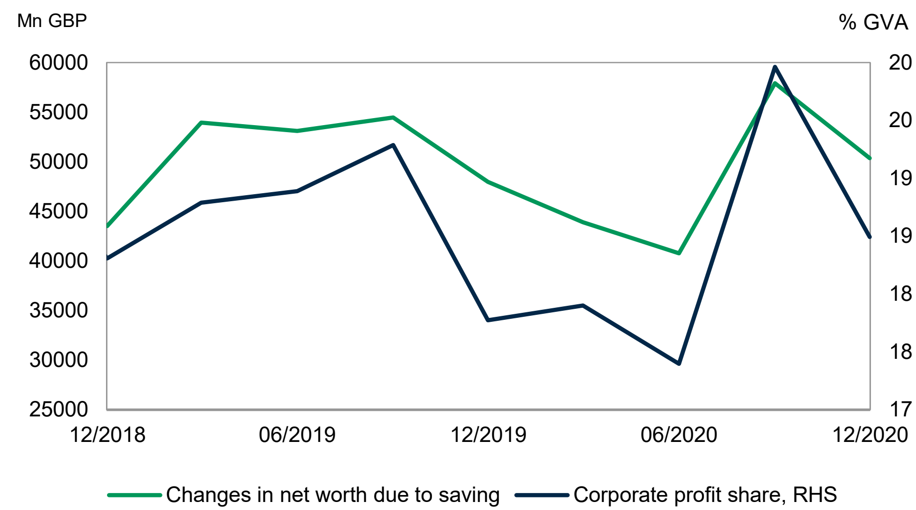
BUSINESS INVESTMENT: NEAR-TERM OUTLOOK BOOSTED BY STRONG TEMPORARY FISCAL INCENTIVES

We revised upwards growth in investment this year and next



Sources: BCC, ONS, Crédit Agricole SA / ECO

Businesses have accumulated savings on an aggregate basis since Q4-19

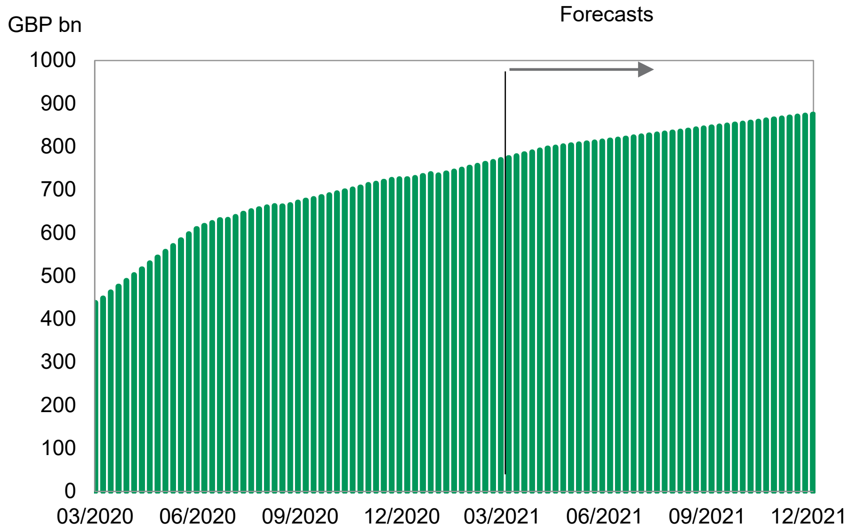


Sources: ONS, Crédit Agricole SA / ECO

We have revised significantly upwards our forecasts for investment thanks to better-than-expected actual data and strong fiscal incentives announced in the March Budget. After strong upward revisions by the ONS (Q3 business investment was revised upwards by 9%), business investment is estimated to have fallen by 10% in 2020. In Q4, business investment stood 7.4% lower than its pre-crisis level, a better situation than household consumption. Gross fixed capital formation represents an even smaller shortfall of 2.6%. Corporate investment intentions rebounded sharply in Q121 to record levels since the beginning of the crisis, likely due to the growing confidence in the medium term following the more-rapid-than-expected vaccination rollout. **The generous temporary uplift in capital allowances announced in the March Budget** (a 130% 'super deduction' available on most types of investment in plant and machinery) is expected to boost business investment significantly this year and next as companies bring forward investment from future periods. The OBR estimates that it could potentially raise the level of business investment by around 10% at its peak in the financial year 2022-23. In the medium term however there will be a reversal of the impact of the capital allowances. The substantial increase in the main rate of corporation tax in April 2023 will likely further weigh on business investment in the long run.

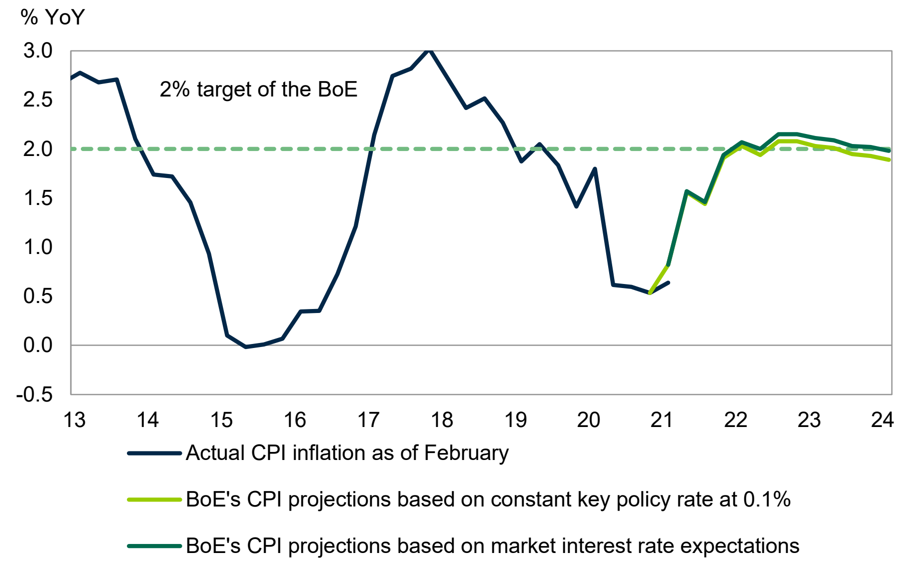
THE BANK OF ENGLAND PREPARES ITS EXIT STRATEGY, EVEN THOUGH RISKS ARE STILL BIASED TOWARDS MORE EASING

The stock of gilts purchased by the BoE is set to reach GBP875bn by the end of 2021



Sources: BoE, Crédit Agricole SA / ECO

The BoE sees CPI inflation back to target at the end of 2021 and close to it in the medium term



Sources: BoE, Crédit Agricole SA / ECO

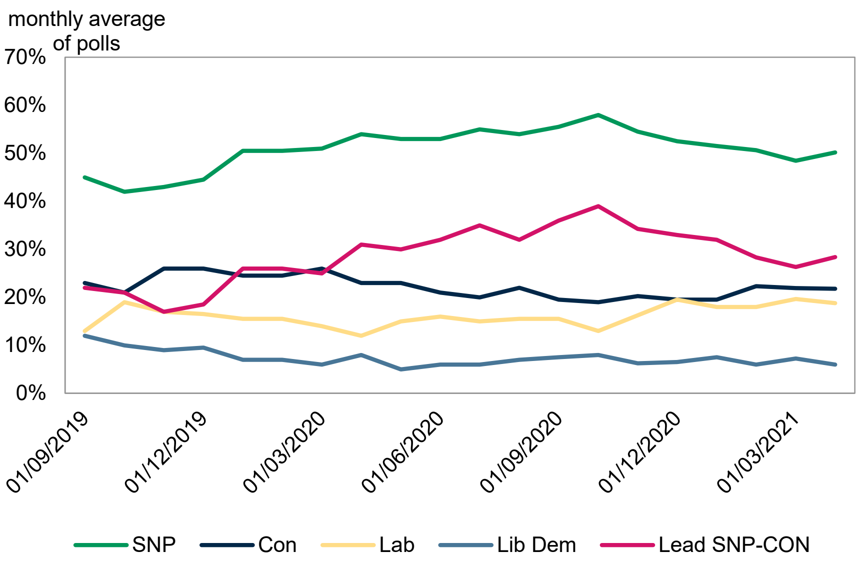
Against the backdrop of positive news regarding the near-term outlook over the recent months, the BoE has moved from the dovish side of central banks (contemplating the possibility of negative interest rates) towards the hawkish spectrum (suggesting a reduction of the pace of asset purchases as soon as this year). At the March MPC meeting it confirmed its intentions to complete its GBP875bn gilt purchase programme at the end of 2021. **Therefore, we no longer expect more QE to be announced in May when the next MPC meeting will take place.** The BoE is currently reviewing its exit strategy, and the new strategy may be announced in the coming months. This is likely to involve an unwinding of the QE programme before an increase in rates, ie, a reversal of the current forward guidance which sees the stock of purchased assets to be maintained "until Bank rate reaches a level from which it could be cut materially". **However, we still see the risks tilted towards a further extension of the QE later in the year, especially if growth disappoints.** Indeed, if the BoE sticks to its current plan, it will need to almost halve the pace of purchases after the May meeting (from GB4.4bn per week to GBP2.3bn per week) or cut them even further later on. This could result in unwarranted tightening in financial conditions, which in turn will weigh on prospects for CPI inflation (which, for the time being, the BoE continues to see close to 2% at the two-three year horizon).

CONTENTS

AFTER BREXIT, FOCUS ON THE SCOTTISH INDEPENDENCE RISK

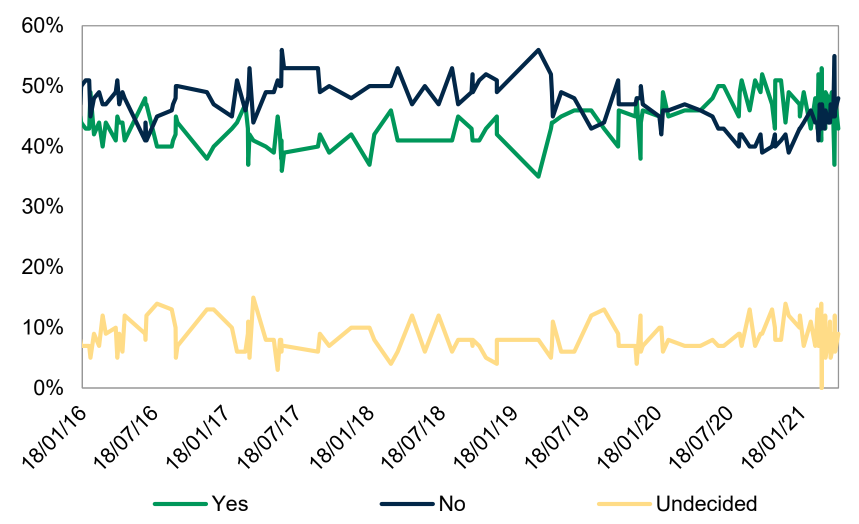
SCOTLAND'S MAY ELECTIONS WILL LIKELY RETURN A PRO-INDEPENDENCE MAJORITY

Scottish opinion polling for Parliament election: SNP ahead in the polls



Sources: Various polls, Wikipedia, Crédit Agricole SA / ECO

Support for Scottish independence has fallen back recently



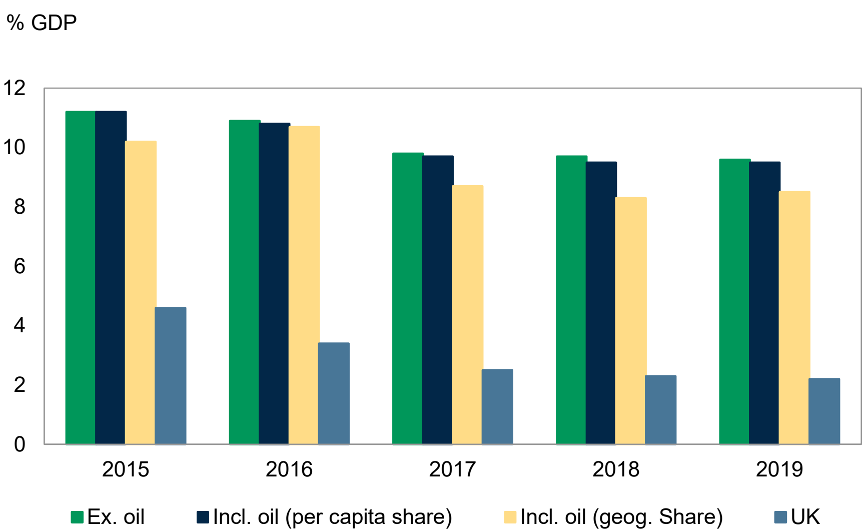
Sources: Various polls, Wikipedia, Crédit Agricole SA / ECO

The elections on 6 May for the Scottish parliament could involve a key risk for the future of the UK. The first minister Nicola Sturgeon is determined to ask for a referendum on Scottish independence if her party wins the election. Her pro-independence **Scottish National Party (SNP) is on course to be the largest group in the Scottish parliament after the elections, although it may struggle to secure an overall majority of seats, requiring 65 seats**. The newly created party by the former first minister Alex Salmond, the pro-independence party called Alba, could deprive the SNP of an overall majority. **Since the beginning of the year, opinion polls have shown a falling popularity of the SNP as well for Scottish independence.** The successive vaccine rollout by the Boris Johnson government and, more recently, the growing tensions within the SNP following the Salmond/Sturgeon affair, which have eroded people's trust in the leader of the SNP, likely explain that recent drift in voting intentions. Pro-SNP voting intentions have fallen to 50% in April, down from close to 60% at the beginning of the year. After having a solid lead during 2020, the support for independence has also become less pronounced this year. Polls in April have so far shown a lead of the No-votes.

AFTER BREXIT, FOCUS ON THE SCOTTISH INDEPENDENCE RISK

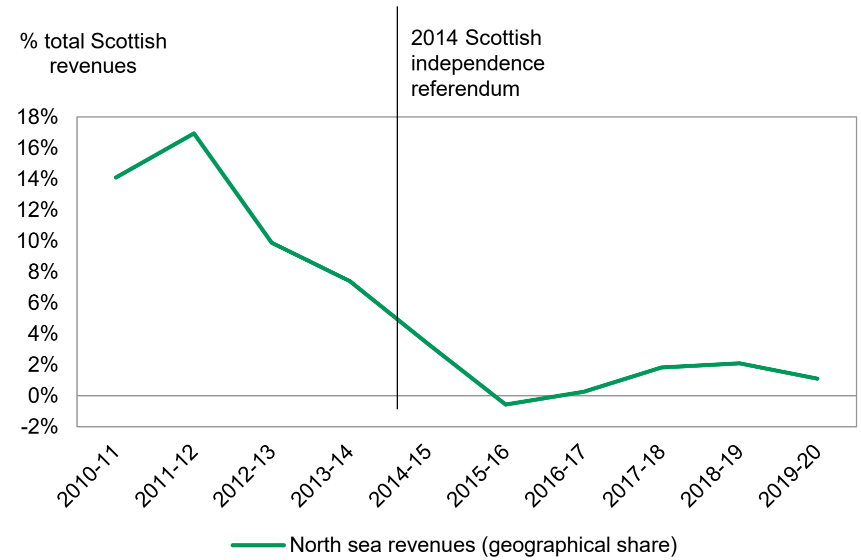
BUT OIL CAN HARDLY BE USED AS A PRO-INDEPENDENCE ARGUMENT NOW

Scotland has a much higher budget deficit than the UK



Sources: Scottish government, Crédit Agricole SA / ECO

Oil and gas extraction has become a negligible source of revenues since the 2014 referendum



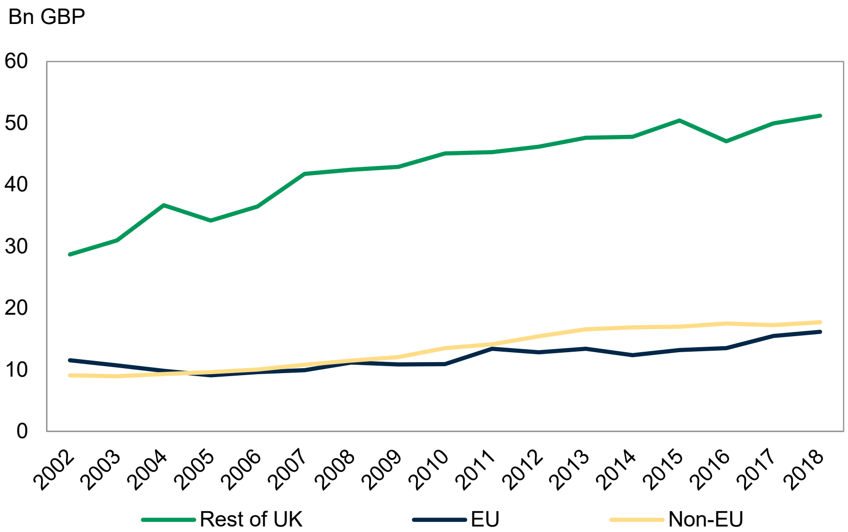
Sources: Scottish government, Crédit Agricole SA / ECO

An independent Scotland would be a much smaller economy relative to the UK. The Scottish population is almost 5.5 million (8.2% of UK total). Its GDP (including North Sea) is around 8% of UK GDP, 7.6% excluding North Sea GDP. Since the 2008 crisis, Scotland's deficit has been broadly stable at close to 9% of GDP, while the UK deficit has fallen steadily from close to 10% in 2008 to 2.3% in 2019. **This relative weakness in Scottish budget position is due to falling North Sea revenues and consistently higher government spending** (12% higher than for the UK per person according to the IFS). In 2020, the Covid-19 crisis and the associated rise in government expenditure and fall in oil prices will likely trigger a sharp rebound in fiscal deficits (estimated at around 26-28% of GDP in 2020/21 in case of Scotland). Brent crude oil prices have fallen from more than 60 USD per barrel on average in 2019 to 40 USD in 2020 (compared to more than 100 USD per barrel in the year preceding the 2014 referendum). **Oil prices will likely remain volatile in the coming months as the recovery in global demand remains uncertain and uneven across countries.** It would it make it even more difficult for the SNP to use North Sea revenues as a pro-independence argument.

AFTER BREXIT, FOCUS ON THE SCOTTISH INDEPENDENCE RISK

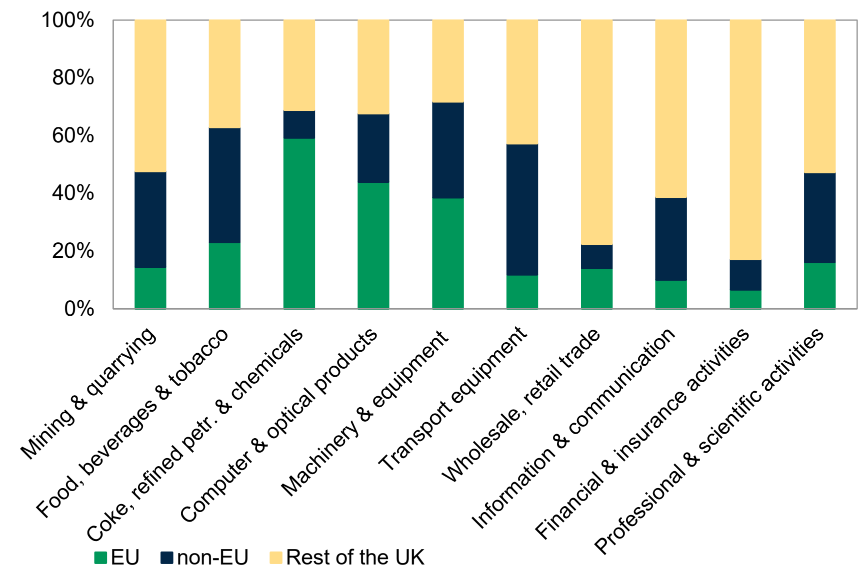
AND THE TCA MEANS EU MEMBERSHIP WOULD IMPLY A HARD BORDER WITH REST OF THE UK

Scottish exports by destination



Sources: Export statistics Scotland: 2018, Crédit Agricole SA / ECO

Scottish top 10 export industries, by destination



Sources: Export statistics Scotland: 2018, Crédit Agricole SA / ECO

The rise of support for independence since 2016 was undoubtedly the result of the Brexit referendum which took Scotland out of the EU against a substantial majority of its citizens (62% of the votes). The SNP wants Scotland to apply for EU membership if it gains independence from the UK. However, **as the UK is now out of the single market and the customs union, joining the EU would imply a hard border with the rest of the UK**, with whom trade is three times larger than trade with the EU (according to Scottish government trade statistics which are available up to 2018). Scottish exports to the EU were worth GBP16bn in 2018, compared to GBP51bn to the rest of the UK and GBP18bn to the rest of the world. An independent Scotland within the EU would be obliged to impose customs checks for trade with England and Wales, which would represent new additional costs for businesses trading across Great Britain. **As a member of the EU, Scottish trade with the rest of the UK would be done under the terms of the Trade and Cooperation Agreement (TCA) between the EU and the UK.** This would trade would be tariff-free but subject to rules of origin and full regulatory checks and controls.

CONSULT OUR LAST PUBLICATIONS

Date	Title	Theme
21/04/2021	France - Scenario 2021-2022: A light at the end of the tunnel	France
13/04/2021	World – Macroeconomic Scenario for 2021-2022: a (very) disorderly exit from the crisis	World
13/04/2021	Italy – Monthly News Digest	Italy
08/04/2021	Geopolitics, pandemic and contextual intelligence	Geopolitics
01/04/2021	Asia: the great divide?	Asia
26/03/2021	Services and tourism in emerging countries: one of the keys to the crisis	Emerging countries
17/03/2021	Behind the scenes of FinTech: superficial diversity	FinTech
17/03/2021	France – Covid-19 Crisis and the Labour Market: Initial Lessons and Future Uncertainties	France
10/03/2021	European recovery package: opportunities, constraints and risks	Eurozone
09/03/2021	Italy – Monthly News Digest	Italy
03/03/2021	Heat networks: backbone of the development of local renewable heat sources	Renewable energy
26/02/2021	What will be the legacy of this unparalleled crisis?	World
18/02/2021	Are you a Biden or a Bollywood?	Geopolitics
10/02/2021	Centring the rudder: Italy, vanguard of the decline of the anti-establishment in Europe?	Eurozone
03/02/2021	The promise of green steel	Mines & metals
02/02/2021	Italy – Monthly News Digest	Italy

Slavena NAZAROVA
+33 1 43 23 21 40
slavena.nazarova@credit-agricole-sa.fr

Completed on April 22 2021

THANKS FOR YOUR ATTENTION

YOU CAN SUBSCRIBE TO OUR PUBLICATIONS ON OUR WEBSITE :
http://economic-research.credit-agricole.com/

Access and subscribe to our free online publications:
application available in App Store and in Google Play

Crédit Agricole S.A. — Group Economic Research
12 place des Etats-Unis – 92127 Montrouge Cedex

Publication Manager: Isabelle Job-Bazille - **Chief Editor:** Armelle Sarda
Information centre: Dominique Petit - **Statistics:** Robin Mourier
Editor: Fabienne Pesty
Contact: *publication.eco@credit-agricole-sa.fr*