

Ten Years of Chancellor Gordon Brown

September 2006

Research Centre

Analysis

With Gordon Brown waiting in the wings for Prime Minister Tony Blair to finalise his plans for departure, Alliance Trust Research Centre takes a look at the real economic legacy of his ten years as Chancellor of the Exchequer. Brown and his party make extensive claims for the country's economic performance over the last ten years listing 'the lowest inflation since the 1960s', 'low interest rates' and 'the lowest unemployment in 29 years' among their top 50 achievements.

Our analysis of some key economic variables shows creditable progress in broad economic terms, with reasonable growth, relatively low inflation and a rise in GDP per head. While Brown's record has been positive on balance, there are several weak spots. Although the UK economy has expanded, its structure has changed because of sharp growth in the public sector over the last ten years. Government spending on this sector has far outstripped the increase achieved by other sectors. While employment has gone up under Brown, the bulk of new jobs were created in the public sector. Employment in some sectors, such as manufacturing, decreased. There are areas too where Brown's policymaking was not necessarily the reason for progress. Inflation has fallen back from the highs of the pre-Labour decades, but this was not unique to the UK. The effects of globalisation drove prices lower in many western economies.

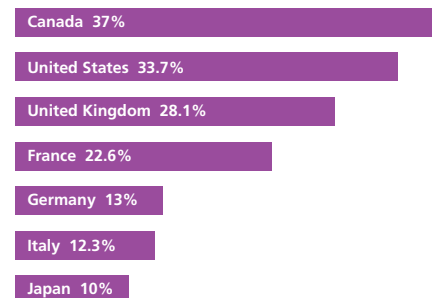
Some economic areas have deteriorated. The trade gap has widened sharply. In pensions, too, despite Labour's claim of 'record rises in state pensions', the economic policymakers could have done better. With homes run by pensioners suffering higher inflation than the average householder in recent years (as our research on Inflation and Age shows) limiting state pension rises to the headline inflation rate has left many worse off. While there have been some one-off payments and pensions credits to help compensate worse-off pensioners,

linking pensions to earnings, and not inflation, would have been a more straightforward way to help pensioners' income from falling behind.

Size of Economy

During the Brown years the UK economy grew 28%. At the end of 1996, the UK's gross domestic product was valued at £909bn. This had risen, in constant prices, to £1.168 trillion by the end of 2005. This performance ranks the UK in third place within the membership of G7, behind both Canada and the US but ahead of France, Germany, Italy and Japan.

GDP Growth (1996-2005)



Growth

The UK has achieved average growth of 2.8% over the 10 years in question, which compares with higher growth of 3.3% in North America, (US and Canada) but lower growth in Europe (2.2% in France and 1.3% in both Germany and Italy). Japan has also recorded a lower average rate of growth of just 1.2%.

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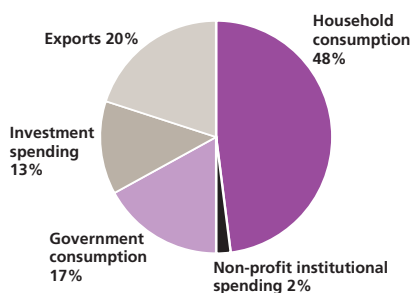
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Structure of the Economy

The composition of the UK economy has altered over the period in which Gordon Brown has been Chancellor. The major change has been the growth in the public sector. In 1996, government spending accounted for 15% of the UK's gross final expenditure, but this had increased to 17% by 2005. This was due to a rise in government spending of 80%, over the period in question. This increase far outweighed those achieved in other sectors of the economy. Investment spending rose 63%, maintaining its 13% share of gross final expenditure, and household spending rose 61%, maintaining its share of 48%. Spending on exports gained just 43%, which resulted in their share of gross final expenditure dropping from 23% to just 20% over the period in question.

Breakdown of Gross Final Expenditure 2005



Trade

The UK's trade position has deteriorated sharply over the last few years. At the end of 1996, the UK had a current account deficit of almost £7bn, but this has ballooned to a deficit of almost £27bn by the end of 2005. The trade deficit has also increased over the last 10 years.

GDP per head

GDP per head is a common measure of relative wealth, as it adjusts the total GDP of a country by the size of its population. The IMF estimates that the UK's GDP per head was £15,144 in 1996 and had grown by almost 24% to £18,764 by 2005. Among our peers in G7, only Canada has performed better, with growth in GDP per head of 25%, while the US has achieved an increase of 22%. Our European neighbours have not fared so well – France has achieved an increase of 17%, Germany 12% and Italy 11%.

Employment

Employment levels have increased during the Chancellor's term in office. In December 1996, total employment in the UK stood at 26.3 million and this had risen to 28.8 million by the end of 2005 – an increase of 2.5 million. However, the

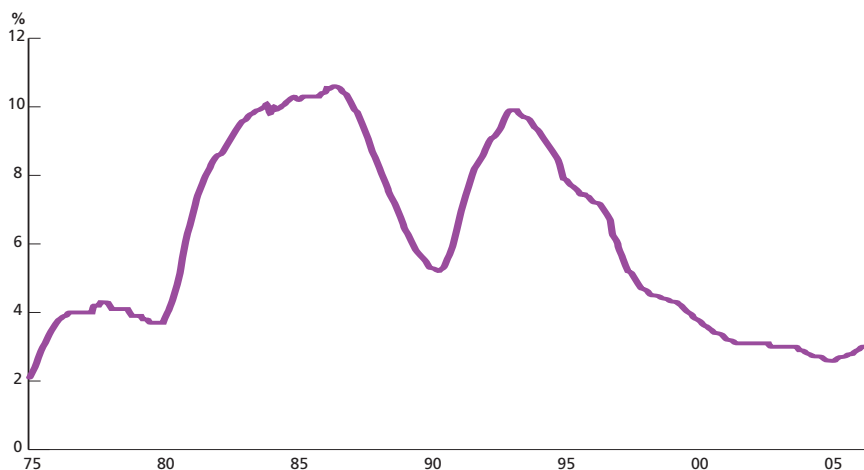
Change in employment since '96 (figures in millions)

	'96	'05	'96-'05 change
Total employment	26.3	28.8	+2.5
Public sector	6.6	7.9	+1.3
Manufacturing	4.5	3.4	-1.1

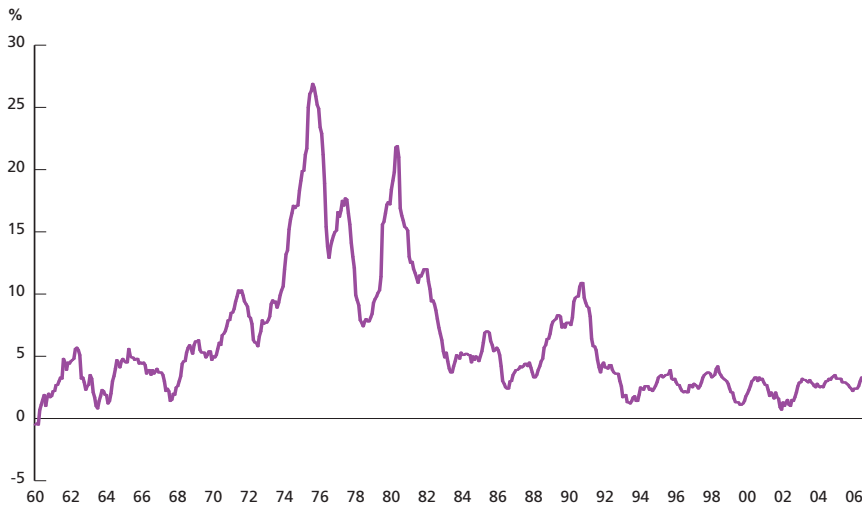
majority of this increase is due to the creation of public sector jobs. Employment in public administration, education and health rose from 6.6 million to 7.9 million, an increase of 1.3 million jobs. The manufacturing sector did not fare so well, employment in this industry fell from 4.5 million to just 3.4 million over the period in question, resulting in the loss of 1.1 million jobs.

The ninth of the Labour Party's list of top 50 achievements is 'the lowest unemployment in 29 years'. This did in fact occur, in January 2005, when the rate of those out-of-work and claiming benefits fell to 2.6%, the lowest since 2.5% was recorded in April 1975. However, this downward trend in unemployment actually began in 1993, five years before the Chancellor came to office. Unfortunately, unemployment has picked up again over the last year, and now stands at 3.0% on a claimant count basis (Aug 06).

Unemployment rate



Retail Price Index



Inflation

The Chancellor has prided himself on his good record on inflation, having granted the Bank of England independence over monetary policy decisions as soon as he entered office. The Labour Party's web site states the top 50 achievements since being elected and top of the list is 'lowest inflation since the 60s'.

This is generally true as inflation did fall back from the highs recorded in the 1970s and 1980s to reach relative lows in the early part of this decade. However, this was not unique to the UK as the forces of globalisation increased competition and drove inflation lower in many western economies.

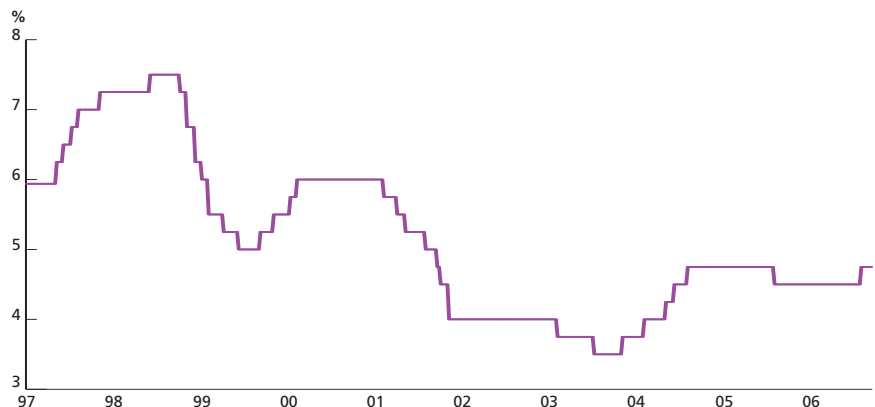
More recently, inflation has been increasing in the UK, pushed up by higher energy prices which utility companies have passed on to the consumer. The Chancellor switched the MPC's target rate of inflation from the Retail Price Index (ex mortgage interest

payments) to the Consumer Price Index in December 2003, setting a target of 2.0% with an allowable band of 1% on either side. Inflation is presently above the target (at 2.5% in Aug) and is expected to remain at an elevated level for some time due to higher energy and food costs.

Low Interest Rates

Second top in Labour's top 50 achievements is 'low interest rates'. As said, one of the Labour government's first moves in coming to power in May 05, was to grant independence to the Bank of England, charging it to set interest rates in accordance with the inflation target set by the Chancellor of the Exchequer. When the Monetary Policy Committee cut the base rate to 3.5%, interest rates reached their lowest level in 50 years. However, this was largely a global phenomenon, and not something achieved solely in the UK. Since that time, interest rates have increased once more, and now stand 1.25% higher, at 4.75%.

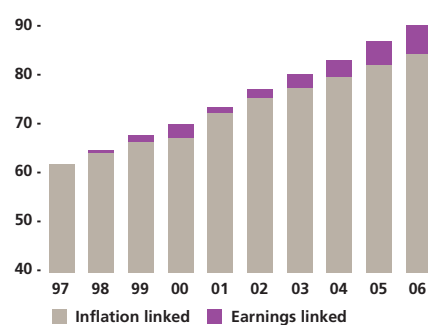
Interest rates



Pensions

Labour claims in its list of top achievements: 'record rises in state pension'. In 1997, the basic state pension was £62.45 per week. Under Labour this has increased to £84.25 per week for 2006, a 37% rise since 1997. However, pensioners would have benefited more, and kept pace with the rise in living standards of those in work, if the government had linked pensions directly to earnings, and not inflation. Because in that scenario pensions would be 7% higher than current levels, at £90 per week.

Pensions (£ per week)



Sources: IMF, ONS, Bank of England