

United Kingdom. Structure, problems, application

1.2% Real GDP growth 2025 (Q2 2026 +0.5% q/q)	£3.0 trn Nominal GDP 2025; 6th largest economy	~£43,700 GDP per head 2025; London £72k, NE £30k	~61% Household consumption % of GDP	-2.8% Current account % of GDP, Q2 2026
3.1% CPI Aug 2026; peak 11.1% Oct 2022	4.9% Unemployment May-Jul 2026; inactivity 20.9%	171,000 Net migration 2025; peak 900k+ in 2023	0.33 Gini 2024/25 before housing costs (0.37 after)	93.8% Public sector net debt % GDP, Aug 2026

STRUCTURE OF THE ECONOMY

	% OF GVA (2023)	% OF JOBS (APPROX.)
Services	80	~85
Manufacturing	9	~7
Construction	~6	~6
Energy, mining, farming	~5	~2

- **Deindustrialisation:** manufacturing ~17% (1990) → 9% (2023).
- **AD mix:** high C, low business investment, negative (X-M).
- **Trade (Q1 2026):** goods -7.6% of GDP, services +6.6%; deficit financed by capital inflows.

MAIN INDUSTRIES

- **Finance (City of London):** ~8% of output 2025; productivity well above average.
- **Business services:** law, consulting, accounting sold worldwide.
- **Creative, digital & education:** tech, film, games; students as service exports.
- **Life sciences & aerospace:** AstraZeneca, GSK, Rolls-Royce, BAE.
- **Cars & energy:** JLR, Nissan; North Sea decline; large offshore wind fleet.

GROWTH STORY: TURNING POINTS

1979-86 Thatcher: privatisation; "Big Bang" in the City	1997 Bank of England independence, inflation target	2008 Financial crisis: bank bailouts, QE, productivity puzzle	2016 Brexit vote: pound -15%, investment stalls
2020 Covid: GDP -10%; leaves EU; TCA from 2021	2022 CPI 11.1%; mini-budget gilt crisis	2023 Bank Rate 5.25%; growth 0.4%	2026 Oil shock (Iran war): CPI back to 3.1%; rate held 3.75%

Why growth is slow (~2.5% before 2008 → ~1-1.5%): weak investment and productivity, Brexit friction, inactivity.

EIGHT PROBLEMS

PROBLEM	EVIDENCE	SPEC LINK
Productivity puzzle	Output/hour 2.0% a yr pre-2008, ~1.3% since	LRAS, supply side
Current account deficit	-2.8% of GDP (Q2 2026)	BoP, exchange rate
Regional inequality	London GDP/head 2.4× North East	Inequality, immobility
Inactivity	~2.8 m long-term sick	Labour supply
Public debt	93.8% of GDP; interest >£100 bn	Public finances
Housing	Prices 7.6× earnings (England)	Inelastic PES
Energy shocks	Motor fuel +23% y/y (Aug 2026)	Cost-push, SRAS
Brexit friction	OBR: trade -15%, productivity -4%	NTBs

INEQUALITY & DEVELOPMENT

- Gini 0.33 before, 0.37 after housing costs (2024/25); above W. Europe, below US.
- GDP per head 2024: London £72,201; North East £29,957; Wales £31,484.
- Wealth far more unequal than income, mainly through housing.
- Tools: progressive tax, Universal Credit, National Living Wage £12.71 (Apr 2026).

Can the UK grow its way out? For: finance, life sciences, AI, planning reform. Against: low investment, ill health, Brexit friction, debt interest.

CLASSIC CHAINS USING THE UK

Interest rates: Bank Rate ↑ → mortgage costs ↑ → disposable income ↓ → C ↓ → AD ↓ → inflation falls, but only for demand-side and second-round pressures.

Energy shock: oil and gas prices ↑ → firms' costs ↑ → SRAS shifts left → inflation ↑ and output ↓ → policy conflict.

Current account: goods deficit → financed by capital inflows → if confidence falls, pound ↓ → imported inflation ↑.

A · DATA RECALL (1 MARK EACH)

1. Real GDP growth in 2025: _____
2. Services as % of UK output (GVA): _____
3. Peak CPI inflation (Oct 2022): _____
4. Bank Rate in September 2026: _____
5. Current account balance, % GDP (Q2 2026): _____
6. Year of Bank of England independence: _____
7. Public sector net debt, % GDP (Aug 2026): _____
8. Gini (before housing costs, 2024/25): _____

B · MATCH THE EVIDENCE TO THE ECONOMIC CONCEPT

UK EVIDENCE	LETTER	CONCEPT
1. Motor fuel prices up 23% in a year		A. Non-tariff barriers
2. Customs checks on UK–EU goods trade since 2021		B. Price inelastic supply
3. House prices 7.6× earnings despite rising demand		C. Cost-push inflation
4. Mining towns lose jobs that are never replaced		D. Financial account surplus
5. Foreign investors buy gilts and UK firms		E. Structural unemployment
6. Bank buys gilts to stop a pension fund fire sale		F. Lender / buyer of last resort

C · COMPLETE THE CHAINS

1. Bank Rate rises → _____ → consumption falls → _____ → inflation falls.
2. Inactivity due to long-term sickness rises → labour supply falls → _____ → _____.
3. Foreign investors lose confidence in UK policy → _____ → _____ → imported inflation rises.

D · EXAM-STYLE QUESTIONS

Extract. UK CPI inflation rose to 3.1% in August 2026, from 2.9% in July. Motor fuel prices were 23.0% higher than a year earlier after conflict in the Middle East pushed up oil prices. Services inflation was 3.4%. The Bank of England held Bank Rate at 3.75%, with three of nine members voting for a rise.

(5 marks) With reference to the extract, explain one cause of the rise in UK inflation in 2026.

(8 marks) Examine two reasons why the UK has a persistent deficit on trade in goods.

E · PLAN A 25-MARK ANSWER

(25 marks) Evaluate whether supply-side policies are the most effective way to increase the UK’s long-run rate of economic growth.

ARGUMENTS FOR (WITH UK EVIDENCE)	ARGUMENTS AGAINST / ALTERNATIVES
OVERALL JUDGMENT: IT DEPENDS ON...	

A · DATA RECALL

1. 1.2%
2. About 80%
3. 11.1%
4. 3.75%
5. About -2.8% (a deficit)
6. 1997
7. 93.8% (accept about 94%)
8. 0.33 (accept 33%)

B · MATCHING

1 → C · 2 → A · 3 → B · 4 → E · 5 → D · 6 → F

C · CHAINS

1. Mortgage and loan repayments rise / disposable income falls / saving more attractive → AD falls (smaller multiplier effect).
2. LRAS grows more slowly / shifts left → lower potential growth; also lower tax receipts and higher benefit spending.
3. Capital outflows / sales of gilts and sterling assets → pound depreciates → import prices rise.

D · EXAM-STYLE GUIDANCE

5 marks: Define inflation as a sustained rise in the general price level (1). Identify cost-push from the extract: motor fuel +23.0% after oil prices rose (1–2). Explain the chain: higher oil price → higher fuel and transport costs for firms → SRAS shifts left → price level rises (2). Use data: CPI 2.9% → 3.1%. Alternative: services inflation of 3.4% shows domestic pressure from wages. Must use extract data.

8 marks: Knowledge/application: deindustrialisation (manufacturing ~9% of output) means comparative advantage now lies in services; high consumption (~61% of GDP) and a high marginal propensity to import. Analysis: chain from each cause to imports > exports of goods. Evaluation (2 points for full marks): the goods deficit is largely offset by a services surplus (6.6% of GDP); low productivity and Brexit friction make it worse; a floating pound can partly correct it; it is a sign of specialisation, not necessarily weakness.

E · 25-MARK PLAN: POINTS TO LOOK FOR

For supply-side policy

- Problem is supply: productivity growth ~1.3% a year since 2008 vs 2.0% before.
- Shifts LRAS right: growth without inflation.
- Planning reform raises housing supply and labour mobility.
- Health and skills policy can bring back some of the ~2.8 m long-term sick.
- Infrastructure and R&D raise private investment.

Against / alternatives

- Long time lags; uncertain delivery (HS2 cut back).
- Fiscal rules and debt interest limit public investment.
- Demand matters: weak AD deters firms from investing.
- Trade policy: closer EU ties may add more than domestic reform.
- Market-based reforms (Thatcher) raised growth but widened inequality.

Judgment: supply-side policy is the only route to sustained long-run growth, but it works best alongside stable demand, credible public finances and lower trade barriers. Effectiveness depends on delivery and on private investment following.