UK: Economic challenges build, despite bold stimulus

The UK government's fiscal response has been well-designed, but with the details of some schemes only just emerging, the challenge now will be to channel the money effectively to businesses. An extension to the post-Brexit transition period looks likely

The UK's coronavirus crisis has yet to peak

The UK is at an earlier point in the coronavirus crisis than some of its European neighbours. But despite some hope that the rate of case growth may be stabilising, the unfortunate likelihood is that the crisis still has further to run. And this means the current period of lockdown, due currently to be reviewed in mid-April, is likely to be much longer-lasting.

If nothing else, the ability to test and implement more-widescale contact tracing will be key to reopening economies globally, and in the UK's case, it hasn't thus far been able to match the rate of testing seen in Germany and parts of Asia.

Logistics are the main challenge for the Chancellor

However, the UK's economic response to the crisis has undoubtedly been bold. Alongside a raft of

Bank of England easing measures, the Chancellor has introduced a large loan guarantee scheme for small businesses, and as well as a 'job retention' scheme designed to pay 80% of a firm's wage bill for furloughed staff.

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There are a range of other measures too, to protect firms' cashflows. But like we've seen in the US, the sheer speed at which the crisis is taking hold is alarming. The number of people signing up for unemployment benefits has soared, and that means the success of the Chancellor's crisis response will be judged just as much in the implementation, as in the design.

One challenge for Chancellor Rishi Sunak is that many of these new schemes are not part of the existing toolkit. Unlike other European countries for example, a job retention scheme hasn't been attempted before and as a result will take a bit longer to implement. Firms will receive the wage payments from the government from the end of April, with the hope that in the meantime employers will take advantage of the loan guarantee scheme to bridge the time gap.

However, the early evidence from accountants suggests around a fifth of small and medium-sized firms may not eligible for the loan guarantee scheme. There is also likely to be a chunk of firms that are too large to benefit from guaranteed loans, but too small (or not sufficiently credit-worthy) to benefit from schemes such as the Bank of England's commercial paper purchasing facility.

We'll have to wait for data on the take-up on the government's broader range of actions. But while the Chancellor's response has arguably been well designed, and the hope is it should still help foster a faster recovery at the end of all of this, there will still undoubtedly be a long-lasting impact on unemployment and the medium-term size of the economy.

An extension to the post-Brexit transition period looks likely

This all means that an extension to the post-Brexit transition period, beyond the end of this year, now looks inevitable. The timeline already looked tight to negotiate a free-trade agreement, and the current health-crisis undoubtedly gives the government some political breathing space to make an extension request.

A recent poll conducted on behalf of *Best for Britain* indicated roughly two-thirds of people were in favour.

Under the terms of the withdrawal agreement, the UK has until 30 June to negotiate a two-year extension. That would still require Britain to accept ongoing budget payments to the EU - a thorny issue - but in the end, we wouldn't be surprised to see an extension quietly announced over the next couple of weeks.

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