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Boris Johnson‘s economic legacy

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The new prime minister takes on a difficult legacy

Former Foreign Secretary Liz Truss is the new prime minister of Great Britain. This week she was appointed by the Queen to form a government. Truss had been preferred in the primary election for the chairmanship of the Conservative Party over former Chancellor of the Exchequer Rishi Sunak, who was considered more moderate.

With Liz Truss the more polarizing candidate won

Liz Truss is taking on a difficult legacy. Divided as a result of an emotionally contested Brexit referendum, Boris Johnson's polarizing government has failed to bring society back together. Liz Truss has also distinguished herself with a rather robust political style. In concrete terms, she stands for a hard line toward the EU, for example by unilaterally questioning the laboriously negotiated Northern Ireland Protocol. Her question as to whether the French president is "a friend or an enemy" of the United Kingdom is also symptomatic. Building bridges looks different.

The economy on the brink

Truss is therefore not ideally positioned to fill the deep political rifts - only a scant fifth of eligible voters have a favorable opinion of her. Yet a precarious economic situation poses even more urgent challenges.

The British economy in stagflation

The Bank of England's Monetary Policy Council spooked the markets after its meeting in August. It forecasts an inflation rate of 13% and a long and deep recession that is likely to last until the end of 2023. Another tight rate hike on September 15 is set. Due to high indebtedness of British households at variable mortgage rates that move in lockstep with key interest rates, this is likely to reduce purchasing power on top of the energy price shock. Of course, this is deliberate in order to squeeze inflation out of the system.

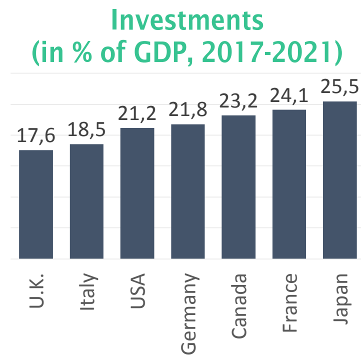
It's definitely going to be a tough winter for the British: The regulator just approved rate hikes that are likely to result in household energy costs nearly doubling. Further price increases are likely to come in January.

What role does Brexit play?

In the election campaign for the presidency, Liz Truss openly asked whether the mandate and, if necessary, the independence of the central bank (which, despite centuries of tradition, it only received in 1997 under Tony Blair) needed to be rethought. This sounds like another populist quick fix and fits into the Tories' Brexit worldview.

The extent to which Brexit is partly responsible for the current malaise of the British economy cannot be reliably determined in the confusing mix of pandemic, supply chains and energy crisis. What can be said, however, is that leaving the EU is unlikely to have helped. Of all the G7 nations, the UK has had the weakest export growth in the period since the referendum (2017-2021: minus 0.5%, Germany by comparison +1.8%).

In terms of the investment ratio, London has also held the red lantern since the decision to leave (17.6% of GDP, Germany 21.8%, see chart). If a Truss government simply muddles on along polarizing lines, hopes for a sustainable recovery of the economy and social climate are likely to remain illusive.



Investment activity paralyzed since Brexit