

Embargoed until 00:05 am Monday 15 February 2010

If the UK had been in the euro, we calculate that unemployment today would be 15% - whatever the failings of his other economic policies, Gordon Brown deserves credit for keeping us out



making business sense

The evidence of growing problems in the eurozone reminds us that cebr has consistently forecast that the diversity of performance would create problems eventually, though we found it hard to predict exactly when.

The problem states in the eurozone (which are all the southernmost states plus Ireland) have had major problems which go to the heart of the difficulty of creating a monetary union without harmonising other aspects of policy. Most European economies have found keeping up with a German inspired exchange rate a problem – Italian unit labour costs have risen 40% relative to Germany since the single currency came into operation on 1 January 1999 and as a result Italy has lost a third of its export market share over this period. For those European countries that have a propensity to borrow, a single interest rate, kept low by frugal Germany, was a step too far and they overborrowed. Ireland and Spain are the most spectacular examples, but Portugal and Greece also had interest rates that were far too low for their economic circumstances. But the fiscal crisis that is now emerging in all these countries is becoming a problem because the fiscal rules of the single currency zone are insufficiently robust to cope with the current economic crisis.

We have said consistently that there would be a bailout for Southern Europe first time round and it looks as though we will be right. But ultimately the Eurozone will have to choose between much greater integration and breaking up the currency. Predicting the timing of this is difficult. The Latin Monetary Union between Switzerland, France, Italy and Belgium (with some other countries also involved) in the mid nineteenth century essentially failed within 30 years. But things move much faster in the modern world and we could see the breakup before 2015.

Readers of the Forecasting Eye will know that we are not particularly enthusiastic about Gordon Brown's economics. His propensity to waste hard earned taxpayers' money on frivolous and wasteful public spending was thrown into relief in the past week when it was discovered that Parliament proposed to employ EIGHTY people to monitor the expenses of 650 MPs, a task that in the private sector would be handled by between 5 and 10 people. This seems typical of the public sector, taking about 10 times as many people as necessary to do a job.

But whatever Gordon Brown's failings, he deserves credit for preventing Tony Blair from taking the UK into the euro. We have used our model to carry out a simulation of what might have happened if Tony Blair has succeeded in taking the UK in in early 1998 when he could still walk on water electorally speaking.

This simulation shows that growth from 1998 to 2006 would have been very slightly higher but with inflation 0.6% higher but that post 2006 the slump would have been much greater – GDP last year might have fallen by 7% instead of 5% and unemployment now would be around 15%. Gordon Brown should be given credit for those things he has got right and this is the most important of them.

Douglas McWilliams *chief executive*
 centre for economics and business research ltd
dmcwilliams@cebr.com 0207 324 2860

This report is produced by centre for economics and business research ltd (cebr) as part of our macroeconomic trends, analysis and forecasting advisory membership service, the prospects service. This report and all associated material shall remain the property of cebr and are only made available to bona fide employees of organisations with a current and fully paid-up membership of the prospects service. Such materials may not be disclosed or transmitted to individuals or organisations outside the member organisation without prior written permission from a director of cebr. cebr is not licensed in the conduct of investment business as defined in the Financial Services and Markets Act 2000. Any client considering a specific investment should consult their own broker or other investment adviser. Any views on investments expressed by cebr, or on behalf of cebr, are intended to be generic only. cebr accepts no liability for any specific investment decision which must be at the investor's own risk. Whilst every effort has been made to ensure the accuracy of the material in this report, neither the authors nor cebr will be liable for any loss or damages incurred through the use of this report or associated materials.