

Economy 'strong' in election year

UK businesses are set to prosper during the next few months - but this could trigger more interest rate rises, according to a report.

Optimism is at its highest since 1997 and business will reap the benefits of a continuing rise in public spending, say researchers at BDO Stoy Hayward. The Bank of England is expected to keep rates on hold this week - but they could go up later in the year. Rates are likely to rise after the anticipated general election in May. The BDO optimism index - a leading indicator of GDP growth two quarters ahead edged up in January to 102.5, from 102.2 in October. The rise is due, in part, to an increase in public spending and increased merger and acquisition activity.

The only thing blighting business optimism this year will be uncertainties associated with the general election, BDO said. Its BDO's output index - which predicts GDP movements a quarter in advance - remained at 100.8 for January, implying GDP growth at 2.9% in the second quarter of 2005. However, the output index is being held back by recent interest rate rises, sterling's strength against the dollar and high oil prices, the group noted. Its inflation index, which has risen continuously over the last 8 months, climbed to 110.0 in January from 108.0 in October last year. "The UK is looking strong going into the general election, but businesses need to prepare themselves for a jolt ahead as the Bank of England reacts to growth and inflationary pressures," said Peter Hemington, partner at BDO Stoy Hayward. "Growth will probably slow by the end of 2005 and it is likely that we will see higher interest rates or a sharp drop in demand for products and services."