Northern Ireland Quarterly Sectoral Forecasts

Forecast summary

The Northern Ireland economy appears to have contracted in the third quarter of 2019, negatively impacted by local and national political uncertainty, low confidence and slower global growth. Throughout 2020, the economy is expected to continue relying on consumer spending to drive growth as uncertainty around the future trading relationship between the UK and the EU weighs on business investment and modest global growth constrains exports. We estimate that economic growth in Northern Ireland was a subdued 0.8% in 2019, with the rate of expansion in 2020 forecast to rise just slightly to 0.9%.

Economic output likely contracted in 2019 Q3…

The Northern Ireland economy appeared to experience a contraction in the third quarter of 2019, according to the latest quarterly indexes.

Production output in Northern Ireland contracted by 2.2% over the quarter to 2019 Q3, and was down 0.8% over the year. And services output, which in recent years has been the main driver of growth in Northern Ireland, also declined in 2019 Q3. Output decreased by 0.1% over the quarter, largely due to a 0.6% fall in the business services and finance sector. Although over the year, services activity increased by 0.6% thanks to previous gains.

The latest consumer and business surveys also back up this view of weakness in 2019 Q3. The Quarterly Economic Survey from NI Chamber of Commerce suggested a deterioration in economic health in the third quarter, with weak domestic and export sales. And the Danske Bank NI Consumer Confidence Index showed a further fall in consumer confidence as political uncertainties took their toll.

…with growth expected to remain subdued in 2020

We estimate that economic growth in Northern Ireland reached just 0.8% in 2019. In 2020 economic growth is expected to increase slightly, but to a still modest 0.9%. Lower inflation and reasonably high wage growth should continue to support household spending power as the economy remains reliant on consumer spending to drive growth. The UK is now expected to leave the EU at the end of January 2020, but continued uncertainty about the long-term trading relationship between the UK and the EU is likely to weigh on business investment. And the modest pace of global economic growth is expected to constrain exports.

Job creation surprised on the upside in 2019 Q3

The pace of job creation in Northern Ireland picked up again in 2019 Q3, according to the latest Quarterly Employment Survey. The total number of employee jobs rose by more than 4,200 compared with the previous quarter, up by 0.5% over the quarter and 2.0% over the year to 2019 Q3.

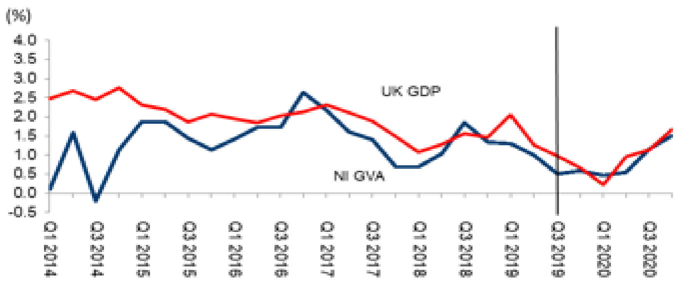
However, we do not expect this pace of employment growth to be maintained, particularly due to the low unemployment rate in Northern Ireland. In the August – October 2019 period, the unemployment rate fell to a new record low of 2.3%. We expect the rate to average 2.8% in 2019, and 3.3% in 2020.

Forecast summary (%)

	2019	2020
UK GDP growth	1.2	1.0
NI GVA growth	0.8	0.9
NI consumer spending growth	1.0	0.9
NI employee jobs growth	1.7	0.5
NI unemployment rate	2.8	3.3
UK CPI inflation rate	1.8	1.8

Source: Oxford Economics, Danske Bank Analysis

Economic growth (year-on-year)



Source: Oxford Economics, Danske Bank Analysis

Key factors in the outlook

Solid growth in household spending

A simultaneous pick-up in wage growth and a moderation of inflationary pressures led to household spending power remaining relatively strong over the past year. Looking into 2020, inflation is likely to remain relatively low and the labour market is expected to remain in reasonably good health, leading to continued strong real wage growth. Therefore, household spending power should remain solid throughout the year. We expect growth in spending to track gains in real incomes over the next few years, with consumer spending in Northern Ireland estimated to have grown by 1.0% in 2019 and forecast to rise by 0.9% in 2020. The pace of quarterly growth is expected to pick up steadily during 2020, paving the way for further growth in 2021.

Slower global growth and a weaker export enivronment

UK exporters have found life tougher of late, with the slowdown in global growth more than offsetting any gains from the weaker pound. Growth in world trade is expected to remain slow compared with 2018 as the impact of greater trade protectionism feeds through. This is likely to continue posing challenges for exporting businesses in Northern Ireland and across the rest of the UK.

Brexit uncertainty weighs on business investment

Although firms are in the most part in solid financial shape, they have been reluctant to spend – as of 2019 Q3, business investment was around 2% below its late-2017, post-crisis peak. Uncertainty around Brexit has been a key factor behind this. Following the outcome of the general election, the UK is now expected to leave the EU at the end of January 2020 and enter the transition period, during which trade between the UK and the EU will continue as it did previously. However, there is still a lack of clarity around the future, long-term, trading relationship between the UK and the EU, and around how trade between Northern Ireland and Great Britain will be affected by the updated Northern Ireland protocol included in the Brexit Withdrawal Agreement. As such, business investment is estimated to have had another weak year in 2019 and is forecast to remain subdued in 2020.

Interest rates unlikely to change in 2020

The Bank of England's Monetary Policy Committee continued to shift in a more dovish direction at its November meeting with two members voting for an interest rate cut. The minutes also suggested that a majority could vote for a rate cut if either global growth fails to stabilise or Brexit uncertainties remain entrenched. But we do not expect a rate cut to occur. Global growth is expected to be modest in 2020 but will likely be quite similar to last year. And while Brexit-related uncertainty is likely to remain a drag on the economy throughout 2020, the short-term risks are slightly lower now compared with the second half of 2019 when the chances of the UK leaving the EU without a withdrawal agreement had increased. Therefore, our baseline forecast assumes that Bank Rate remains unchanged at 0.75% throughout 2020.

Less restrictive fiscal stance

We estimate that fiscal policy exerted a 0.8 percentage point drag on UK economic growth in the fiscal year 2018-19. But the Chancellor announced a loosening of the fiscal stance in September's Spending Round, with real day-to-day spending set to grow by 4.1% in fiscal year 2020/21, a 15-year high. Furthermore, following the general election and the apparent public support for more government spending, the new Government will likely loosen fiscal policy more than its manifesto commitments imply. Overall, this means that the fiscal stance is expected to be modestly supportive of GDP growth in 2020.

Sectoral outlook

Modest economic outlook for Northern Ireland continues into 2020
The Northern Ireland economy lost momentum in the third quarter of 2019, and only minimal growth is expected in the final quarter of the year. We expect growth to remain subdued in 2020 as the weaker global economy, Brexit-related uncertainty and low confidence continue to negatively impact the economy. The estimated pace of growth of 0.8% in 2019 is expected to pick up slightly to 0.9% in 2020, with the **information & communication** and **professional, scientific & technical services** sectors leading the way. The **transportation & storage** sector also ranks in the top three fastest growing sectors, linked to its strong employment growth in the first half of 2019.

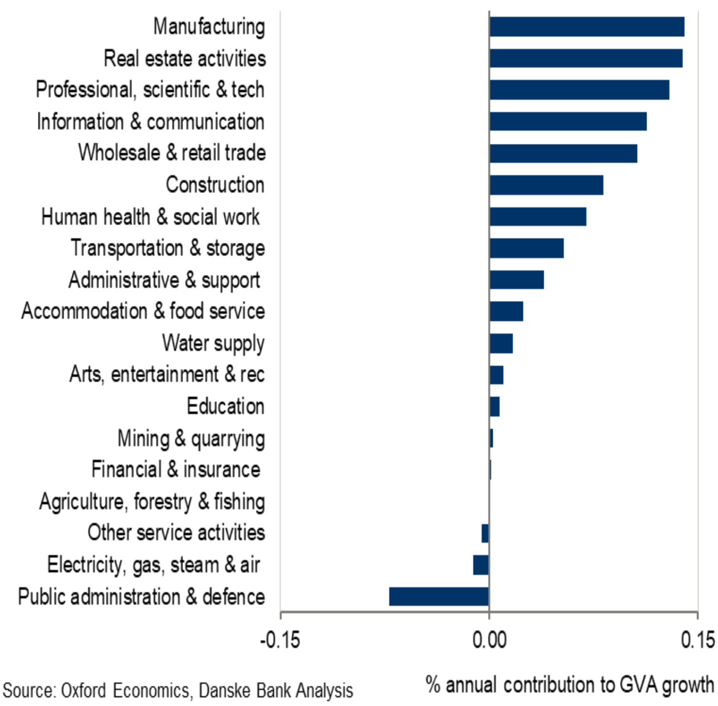
We have revised our forecast for growth in the **manufacturing** sector downwards to 1.0% in 2019 and 1.1% in 2020. Growth in 2019 looks set to be underpinned by the strength of the sector in the first half of the year, with a contraction in quarterly output estimated in quarter three and another one possible in the fourth quarter. The latest Index of Production data showed a decline in manufacturing output of 1.4% over the quarter to 2019 Q3, with the weakness potentially exacerbated by firms continuing to run down stocks that they had accumulated at the start of the year to guard against a potential 'no-deal' Brexit.

Expected output growth in the **wholesale & retail trade** sector has been revised down slightly to 0.8% in both 2019 and 2020. The latest Danske Bank Consumer Confidence Index showed a continuing drop in consumer confidence in 2019 Q3, again largely due to Brexit and the local political impasse. And the latest data from the Society of Motor Manufacturers and Traders showed the third consecutive annual fall in car sales in Northern Ireland, down almost 2% in 2019.

Output in the **construction** sector is forecast to rise by 1.2% in 2019 and 1.0% in 2020. While the latest Northern Ireland Quarterly Construction Bulletin implied a weakness in 2019 Q2 (with output falling by 5.6% over the quarter and 1.5% over the year), employment growth in the sector has remained strong, and increased in the five consecutive quarters to 2019 Q3.

Public administration & defence will likely continue to drag on growth, with output expected to contract by 0.8% in 2019, and by a further 0.3% in 2020.

Sector contributions to GVA growth in 2019



Source: Oxford Economics, Danske Bank Analysis

GVA (%)	2019	2020
Information & communication	3.2	3.3
Professional, scientific & tech	3.1	3.2
Transportation & storage	1.4	1.4
Administrative & support	1.3	1.2
Real estate activities	1.2	1.0
Construction	1.2	1.0
Water supply	1.0	1.0
Manufacturing	1.0	1.1
Mining & quarrying	1.0	0.6
Accommodation & food service	0.9	1.0
Arts, entertainment & rec	0.9	0.7
Wholesale & retail trade	0.8	0.8
Human health & social work	0.7	0.6
Education	0.1	0.4
Financial & insurance	0.0	0.0
Agriculture, forestry & fishing	0.0	0.2
Other service activities	-0.3	0.1
Public administration & defence	-0.8	-0.3
Electricity, gas, steam & air	-1.0	0.0
Total	**0.8**	**0.9**

Source: Oxford Economics, Danske Bank Analysis

Labour market outlook

Jobs growth in Northern Ireland surprised on the upside in 2019 Q3, but this pace isn't expected to continue
The labour market in Northern Ireland picked up pace in the third quarter of 2019, despite the weaker economic environment, with the latest Quarterly Employment Survey (QES) showing quarterly jobs growth of 0.5%, compared with 0.2% in 2019 Q2. However, we do not expect this pace of growth to be maintained – instead firms are likely to shift their focus away from recruitment and more towards productivity improvements, in part due to the little spare capacity left in the labour market. We are forecasting a slowdown in the annual rate of jobs growth in 2020, to 0.5% from an estimated 1.7% in 2019.

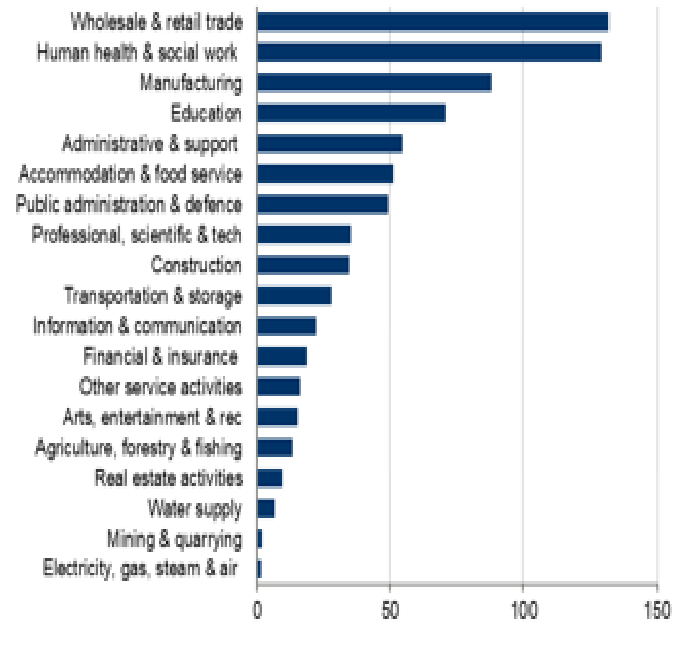
The **mining & quarrying** and **water supply** sectors are estimated to have experienced the fastest rate of employment growth in 2019, reflecting their strong performance as evidenced by the latest QES data. However, due to the small size of these sectors, their contribution to the expected overall number of new jobs in the economy is small. A 9.6% rise in mining jobs equates to only 175 new jobs, while the 8.7% rate of employment growth in the water supply sector represents just 550 jobs out of the total estimated 13,500 additional jobs in 2019.

The business services sectors have had a mixed year in 2019. Growth in the number of jobs in the **information & communication** sector has been revised upwards to 7.5% in 2019 and 1.3% in 2020, again reflecting strength in the latest data. The **professional, scientific & technical** services sector is also estimated to have grown above the national average, rising 3.2% in 2019, and remaining above average in 2020 at 1.3%. However, the **administration & support services** sector has been revised down, with jobs now estimated to have contracted by 1.1% in 2019, and subdued growth of just 0.2% expected in 2020. The latest data shows a 1.5% drop in jobs in this sector between 2018 Q3 and 2019 Q3.

Employment growth in **construction** has been revised upwards to 1.9% in 2019, reflecting continued quarterly rises in the latest data. However, this pace is not expected to be maintained into 2020, with growth forecast to slow to 0.6%.

The unemployment rate in Northern Ireland fell to 2.3% in the August – October 2019 period, a new record low. The rate was down by 0.6 percentage points compared with May – July (which was the previous record low), and 1.3 percentage points lower than August – October 2018. We expect the unemployment rate to average 2.8% in 2019 and 3.3% in 2020.

Employee jobs per sector in 2019



Source: Oxford Economics, Danske Bank Analysis

Employee jobs (%)	2019	2020
Mining & quarrying	9.6	0.7
Water supply	8.7	0.6
Information & communication	7.5	1.3
Transportation & storage	4.6	0.9
Professional, scientific & tech	3.2	1.3
Human health & social work	2.7	0.4
Manufacturing	2.3	0.8
Arts, entertainment & rec	2.0	0.7
Accommodation & food service	2.0	1.0
Construction	1.9	0.6
Education	1.5	0.4
Real estate activities	1.1	0.8
Wholesale & retail trade	0.9	0.6
Agriculture, forestry & fishing	0.4	0.1
Public administration & defence	0.0	0.3
Financial & insurance	-0.3	-0.1
Other service activities	-1.0	-0.3
Administrative & support	-1.1	0.2
Electricity, gas, steam & air	-9.7	-2.5
Total	**1.7**	**0.5**

Source: Oxford Economics, Danske Bank Analysis

Risks and uncertainties

There are several risks and uncertainties which may impact upon the Northern Ireland economy and the forecasts presented above. These include:

- **Brexit –** Following the Conservative Party's election win in December, ratification of Prime Minister Boris Johnson's Brexit withdrawal agreement and the UK's exit from the EU on January 31 looks highly likely. Where the greater uncertainty now lies is in the trade negotiations due to take place during the transition period. With the two sides starting in the rather unique position of regulatory alignment, the negotiations will be aimed at constructing a system to manage divergence. However, given the UK Government is unlikely to be enthusiastic about retaining very close alignment with EU rules or to want to accept much tighter restrictions on access to the EU market, we think agreeing a new free trade agreement will prove more complicated than expected. Indeed it would be highly unusual for a comprehensive trade deal of this magnitude to be completed within a year, implying that the Government will either need to soften its stance with regards to staying in close alignment with EU rules, attempt to agree only a very limited free trade agreement covering goods or extend the transition period (under the terms of the Brexit Withdrawal Agreement, an extension to the transition period needs to be agreed by 1 July 2020). However, it is worth noting that the Prime Minister has pledged that the future negotiations will not go on beyond 31 December 2020 and so another possibility is that a trade agreement is not reached in time and the UK goes into 2021 with no preferential trading relationship with the EU i.e. similar to a no-deal Brexit from a trade perspective. In addition, for businesses in Northern Ireland, while the new Brexit Withdrawal Agreement means that there will be no hard border with the Republic of Ireland, there is still a lack of clarity around what processes would need to be followed on trade between Northern Ireland and Great Britain once the transition period ends.

- **Local politics** – the restoration of the devolved institutions is undoubtedly a positive development for Northern Ireland's short and long-term economic prospects. After three years without a functioning Assembly and Executive, there are many challenges for the newly appointed departmental ministers to tackle, and the long-term economic problems of high inactivity and poor productivity will not be easy to solve. There is still some uncertainty around the size of the financial package which the Executive will receive from the UK Government and with a number of commitments agreed as part of the new deal, it is imperative that the Executive hits the ground running. If it is able to do so, then there should be a positive impact on both consumer and business confidence.

In addition, key global uncertainties include:

- **US and China trade tensions continue** – While the Phase 1 trade deal between the US and China has been accompanied by a wave of optimism, both historical evidence and more recent experience suggest caution. Over the course of the trade war, we've frequently seen a de-escalation in tensions followed by a re-escalation. And should tensions re-escalate again, this would have stark implications for the US and Chinese economies, with negative spill over effects for the global economy.

- **Global growth slowdown likely to continue into early 2020 –** Business surveys remained soft in 2019 Q4. The global manufacturing PMI remained a touch above the no-change score of 50 for a second month running in December and the services index nudged up. But the latter remains far weaker than at the beginning of last year. The year-end sluggishness implies that global GDP growth may weaken further around the turn of the year. Notably, the US economy is experiencing slowing momentum and continuing trade tensions; the Eurozone is seeing output slow as weaker employment growth and uncertainty hit the domestic economy; and China's growth is moderating further amid external headwinds and a modest impact from policy stimulus.

- **Volatility in global oil markets –** Recent volatility in global oil markets, including attacks on oil-processing facilities in Saudi Arabia earlier in the year and heightened geopolitical uncertainty in the Middle East, has led to vulnerability in the sector. Any exogenous shock to oil supply remains a genuine risk to the global growth outlook.

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