

Northern Ireland Quarterly Sectoral Forecasts

Forecast summary

The Northern Ireland economy grew strongly in the second quarter of the year as many of the coronavirus restrictions were gradually eased. The economy is also likely to have expanded in the third quarter though probably at a slower rate as the large gains from the initial reopening have now passed and businesses have begun to encounter disruption within their supply chains. Consumers appear to have reacted positively to the increased opportunities to spend on both goods and services and while we still expect consumer spending to be a key driver of future growth, some cautious spending behaviours are likely to persist. Given the latest data and some of the challenges that have emerged over recent months we have revised our forecast for economic growth in Northern Ireland downwards to 5.8% in 2021, which would still represent a strong rate of expansion. For 2022, we have slightly increased our growth projection to 4.7%.

Economic growth returned as restrictions were eased with further rises in activity levels expected

The latest data indicates that the Northern Ireland economy returned to growth in 2021 Q2 as the coronavirus restrictions were gradually eased.

The Index of Production showed that output increased by 1.1% over the quarter to 2021 Q2. The Index of Services showed an even sharper rise in overall activity levels of 5.5% with particularly strong quarterly growth of 13.9% for the other services sector and 8.3% for the wholesale, retail, accommodation and food services sector.

We expect the economy to have grown again in 2021 Q3 and to keep expanding throughout the rest of this year and into next year as the recovery from the impacts of the pandemic continues. We are forecasting that economic output in Northern Ireland will increase by 5.8% in 2021, down from the 6.2% we had projected in our previous report. This downward revision reflects the supply chain disruption that has emerged, our expectation of some cautious consumer spending behaviours persisting and the trends evident in the latest national and local economic data. However, it is important to note that growth of 5.8% would still represent a strong rate of expansion and encouraging progress towards economic recovery. We expect the economy to grow by around 4.7% in 2022, slightly higher than the 4.5% we previously projected as the downward revision to the 2021 forecast pushes some more of the recovery in output into next year. Under these forecasts, economic activity in Northern Ireland returns to its pre-pandemic level in the second half of 2022.

Encouraging signs around labour demand, but unemployment is still expected to rise

The latest labour market data has contained some positive signs. The Quarterly Employment Survey showed that the number of employee jobs continued to rise in the second quarter of the year, up by 0.2% when compared with the first quarter. The employment rate for the May-July 2021 period increased to 71.2%, and the HMRC PAYE data for August 2021 showed that the number of payrolled employees increased by 0.5% compared with the previous month.

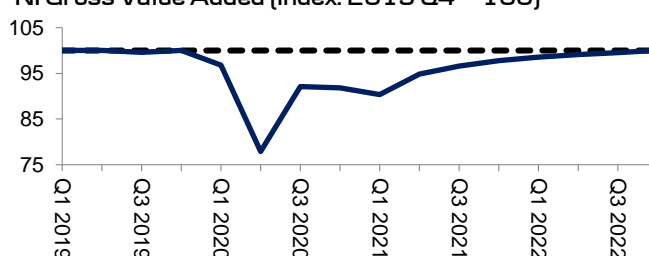
However, the unemployment rate also increased to 4.0% in May-July 2021. Given the fall in the economic inactivity rate, part of this rise in unemployment can likely be attributed to people re-entering the labour force and therefore becoming unemployed rather than inactive while they search for work. However, the unwinding of the Coronavirus Job Retention Scheme is also likely to have played a role. We expect to see some further job losses after the scheme ends on 30 September 2021.

We are forecasting that the annual average number of employee jobs will decline by around 0.6% in 2021, with employment growth returning in 2022 at about 1.0%. We also expect the unemployment rate to average 4.1% in 2021 and 4.4% in 2022.

Forecast summary (%)			
	2020	2021	2022
UK GDP growth	-9.8	6.5	5.4
NI GVA growth	-10.2	5.8	4.7
NI consumer spending growth	-11.0	3.8	6.0
NI employee jobs growth	-0.4	-0.6	1.0
NI unemployment rate	3.0	4.1	4.4
UK CPI inflation rate	0.9	2.2	2.7

Source: Oxford Economics, Danske Bank Analysis

NI Gross Value Added (Index: 2019 Q4 = 100)



Source: Oxford Economics, Danske Bank Analysis

Key factors in the outlook

Most coronavirus restrictions have now been lifted, facilitating a rise in economic output



The majority of coronavirus restrictions in Northern Ireland have now been eased, enabling a rise in economic activity levels. For example, the reopening of non-essential retail, hospitality and close contact services provided an outlet for pent-up demand during the second quarter of the year, facilitating a rise in local consumer spending. The UK GDP data for the second quarter of the year also showed an expansion in business investment, although the rate of growth was more modest than that of consumer and government spending. The higher number of positive coronavirus cases observed during quarter three is a cause for some concern. However, our forecasts assume that the rollout of the coronavirus vaccine programme will avoid the economy entering further periods of full lockdown.

Developments in the economic policy environment



Fiscal policy has been highly stimulative throughout the pandemic in order to lessen the adverse economic impacts, but many of the schemes are now drawing to a close. For example, the Coronavirus Job Retention Scheme, which has been one of the most significant fiscal support measures, comes to an end on 30 September 2021. However one local fiscal measure – the High Street Scheme – which will provide a £100 voucher to people in Northern Ireland is likely to provide a boost to local businesses during the final quarter of the year. In terms of monetary policy, the Monetary Policy Committee (MPC) voted to maintain Bank Rate at its historic low of 0.1% at its September 2021 meeting. The MPC believes that inflation will rise further over the months ahead, but expects the above target rate of price increases to prove temporary. As such, and given that the recovery is still ongoing as well as the MPC noting the uncertainty around the future outlook for the labour market in its meeting minutes, we expect Bank Rate to remain unchanged throughout the rest of 2021.

Supply chain disruption is contributing to higher rates of inflation



Disruption to supply chains is becoming an increasingly significant challenge for businesses and has the potential to act as a headwind to future rates of economic growth. As well as constraining business activity, supply shortages are also one factor contributing to higher inflation in the UK alongside rising fuel and energy prices as well as strong base effects. These factors combined to push the rate of headline CPI inflation up to 3.2% in August 2021. A further sharp rise in the energy price cap in Great Britain, the reversal of the VAT cut for hospitality and rising global goods prices are set to push CPI inflation up further towards the end of the year. However, we expect the rise to be temporary and believe that inflation will gradually start to move back towards its 2% target as we move further into next year. We are forecasting that inflation will average 2.2% in 2021 and 2.7% in 2022.

Confidence increased in 2021 Q2, but some cautious behaviours are expected to continue



The Danske Bank Northern Ireland Consumer Confidence Index showed that consumer confidence improved in the second quarter of the year as the coronavirus vaccine programme continued to be rolled out. Business confidence also improved according to the 2021 Q2 Quarterly Economic Survey published by the *Northern Ireland Chamber of Commerce* and *BDO*. At an aggregate level, we expect consumer spending to be a key driver of economic growth over the rest of this year and into next year. We are forecasting that it will rise by 3.8% in 2021 and around 6.0% in 2022. However, we are still likely to see some cautious behaviours persisting, as above-target inflation, higher coronavirus case numbers and Brexit-related uncertainty negatively impact sentiment. These concerns could also impact businesses, with some firms deciding to prioritise adding to their cash reserves or paying down debt rather than spending on new investment projects.

Extra trade frictions due to Brexit



Firms in Northern Ireland and across the UK are continuing to face new trade processes following the UK's exit from the European Union. The UK-EU Trade and Co-operation agreement has introduced new customs and regulatory trade barriers that may weigh on export competitiveness. In addition, the Northern Ireland Protocol has caused an extra hurdle for local firms when purchasing certain goods, although businesses have been adjusting to the changes. Political uncertainty related to these new trading arrangements remains elevated, and it is likely to take some time before firms fully adapt to the new processes.

Sectoral outlook

Economic output returned to growth in 2021 Q2 as coronavirus restrictions were eased

The Northern Ireland economy returned to growth in 2021 Q2 as the easing of coronavirus restrictions enabled an increase in economic activity. Consumers, while still showing some signs of caution, reacted positively to the reopening of non-essential retail and hospitality. However, the biggest output gains are now likely behind us. We expect the economy to have grown again in the third quarter of the year and that economic output will continue to increase over the final three months of this year and through 2022, albeit with the quarterly rate of expansion moderating over that time. Overall, we are forecasting that the Northern Ireland economy will grow by 5.8% this year and around 4.7% next year.

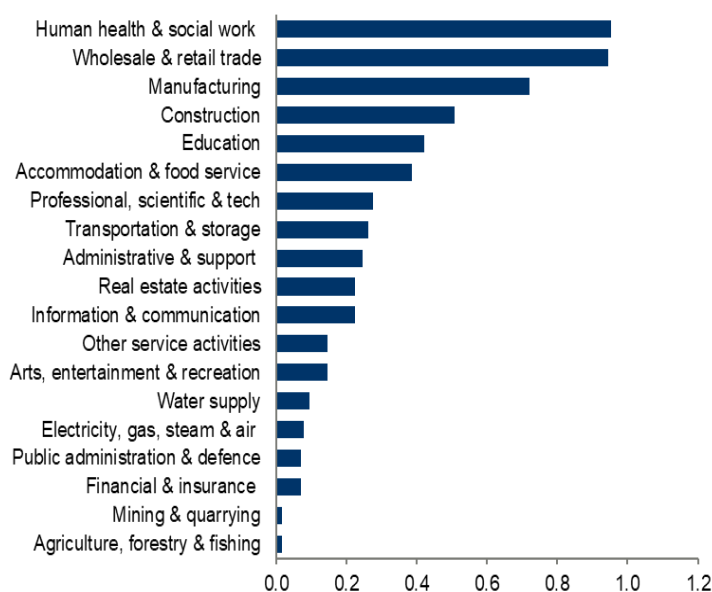
As the sectors hardest hit by the coronavirus restrictions in 2020, the **accommodation & food services** and **arts, entertainment & recreation** sectors are projected to experience the fastest rates of output growth, both this year and in 2022, as they rebound from the impacts of the pandemic.

Output in the **wholesale & retail trade** sector – which was less impacted by the lockdown periods than the other consumer-focused parts of the economy given that essential retail remained open and some firms began to sell goods online – is expected to rise by 6.8% in 2021. This is ahead of the average for total GVA given that wider activity in the sector has been spurred on by consumer spending following the easing of restrictions. The improvement in consumer sentiment in the second quarter of the year, shown by the Danske Bank Northern Ireland Consumer Confidence Index, likely stimulated activity in these sectors and should support further spending.

We have revised our forecast for growth in the **manufacturing** sector in 2021 from 6.7% in our previous report down to 5.6%. Manufacturing output did increase in the second quarter of the year but input price rises, difficulties related to the availability of raw materials and labour and Brexit-related challenges are negatively impacting the sector. These issues may also affect the **construction** industry and as a result we have also reduced our forecast for growth in this sector down to 6.7%.

We expect the **professional, scientific & technical services** and **information & communication** sectors to grow by around 6.2% and 6.1% respectively in 2021, slightly faster than the average for the overall economy. Output in the **administrative & support** sector is forecast to rise by 8.2% this year and by a further 9.7% in 2022 as it recovers from a relatively large drop in 2020.

Sector contributions to GVA growth in 2021



Source: Oxford Economics, Danske Bank Analysis % annual contribution to change in GVA

GVA (%)	2021	2022
Accommodation & food service	18.7	20.9
Arts, entertainment & recreation	14.6	14.7
Human health & social work	8.6	3.9
Other service activities	8.2	10.1
Administrative & support	8.2	9.7
Education	8.1	7.9
Transportation & storage	7.2	9.1
Wholesale & retail trade	6.8	5.0
Construction	6.7	5.4
Professional, scientific & tech	6.2	5.1
Information & communication	6.1	5.8
Mining & quarrying	5.8	4.2
Water supply	5.6	3.0
Manufacturing	5.6	4.1
Electricity, gas, steam & air	5.2	1.9
Financial & insurance	2.0	1.0
Real estate activities	1.9	0.4
Agriculture, forestry & fishing	0.9	1.4
Public administration & defence	0.9	0.3
Total	5.8	4.7

Source: Oxford Economics, Danske Bank Analysis

Labour market outlook

The number of jobs rose in 2021 Q2, but unemployment is still projected to increase

The latest data from the Quarterly Employment Survey showed positive employment growth continuing into the second quarter of the year, as demand in the labour market firmed in line with the easing of restrictions. The number of employee jobs in Northern Ireland rose by 0.2% over the quarter to June 2021. However, we do expect to see some job losses as government support unwinds. Overall, we are forecasting that the average annual number of employee jobs in Northern Ireland will decline by 0.6% in 2021, before returning to growth of around 1.0% in 2022.

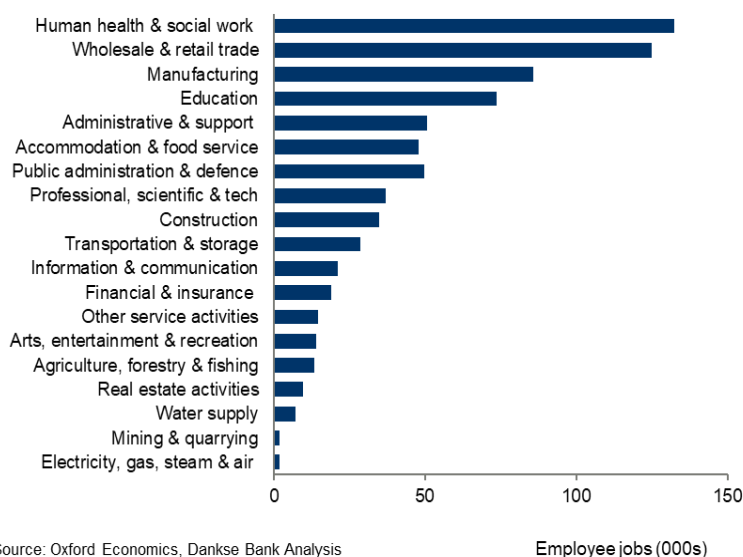
The consumer-focused sectors are forecast to experience the largest annual falls in employee jobs in 2021, as lockdown restrictions stifled demand at the start of the year and these sectors had relatively high uptake rates of the Coronavirus Job Retention Scheme. The **arts, entertainment & recreation** and **accommodation & food services** sectors are projected to experience the largest declines in the number of jobs this year, of around 5.1% and 4.0% respectively. However, this annual outlook is driven in large part by sharp falls in the number of jobs at the start of the year. The latest Quarterly Employment Survey showed that the number of jobs in the accommodation and food services sector increased by 3.0% in 2021 Q2. We expect the number of jobs in the arts, entertainment & recreation sector to have increased in the third quarter of the year. These two sectors are expected to experience the fastest annual employment growth next year as the recovery continues.

We are forecasting that employment in the **manufacturing** sector will decline by 0.8% in 2021 due to a fall in the number of jobs in the first quarter of the year, current difficulties in recruiting staff and other challenges facing the sector including input shortages. In the **construction** industry, the annual average number of employee jobs is projected to fall by 1.5% this year. Both sectors are forecast to experience rising employment levels in 2022.

The 0.6% fall in total employment expected this year is partly driven by the sectors mentioned above, but almost half of Northern Ireland's sectors are projected to experience annual jobs growth in 2021. The **information & communication** and **professional, scientific & technical services** sectors are forecast to experience the largest employment gains, with the number of jobs rising by 1.9%.

While employment continued to increase in 2021 Q2, so too did unemployment, with the rate in May-July rising to 4.0% as the Coronavirus Job Retention Scheme began to unwind and people re-entered the labour force and moved from being categorised as inactive to unemployed. Between the start of April and the end of July, the number of furloughed jobs in Northern Ireland fell by almost two-thirds to around 36,000. Once the scheme comes to an end, we expect to see a further increase in unemployment although we are hopeful that some of this will be very short-term, as people then begin to fill other employment vacancies. Overall, we are forecasting that the unemployment rate will average 4.1% in 2021 and 4.4% in 2022.

Employee jobs per sector in 2021



Source: Oxford Economics, Danske Bank Analysis

Employee jobs (%)	2021	2022
Information & communication	1.9	1.0
Professional, scientific & tech	1.9	0.6
Education	1.1	0.2
Human health & social work	1.0	0.7
Mining & quarrying	0.9	0.1
Real estate activities	0.8	0.1
Public administration & defence	0.7	0.1
Agriculture, forestry & fishing	0.6	0.2
Electricity, gas, steam & air	0.6	0.1
Administrative & support	0.2	0.6
Manufacturing	-0.8	0.4
Transportation & storage	-1.5	1.8
Construction	-1.5	1.1
Water supply	-1.8	0.7
Financial & insurance	-2.1	1.5
Wholesale & retail trade	-2.4	1.7
Other service activities	-3.2	1.5
Accommodation & food service	-4.0	3.4
Arts, entertainment & recreation	-5.1	4.1
Total	-0.6	1.0

Source: Oxford Economics, Danske Bank Analysis

Risks and uncertainties

While there is always uncertainty around economic forecasts, the extent of the risks and uncertainties around these projections is still considered to be more elevated than is normally the case. The main sources of uncertainty include:

- **Coronavirus** – Despite the easing of most restrictions, the coronavirus pandemic remains the most significant risk facing the economy. Throughout the second quarter of the year, the majority of restrictions were lifted in Northern Ireland, although some rules remain in place. Coronavirus case numbers have been high during the third quarter of the year when compared with the previous quarter, but the continued rollout of the vaccine programme provides hope that further lockdowns will be avoided. However further rises in case numbers, new coronavirus variants, or a return to some form of restrictions do remain as significant downside risks to the economic outlook.
- **Supply chain disruptions continue** – Ongoing disruption to supply chains threatens to constrain the pace of the economic recovery in Northern Ireland and across the wider UK. The shortages and higher input prices currently being experienced by firms are expected to be temporary, but it's not immediately clear for how long they will persist. A prolonged period of disruption could have adverse impacts on output levels across the economy, potentially slowing the pace of the recovery. It could also add to the cost pressures currently facing firms and feed through into higher and more sustained inflation rates, which would squeeze consumer spending power and create a more uncertain monetary policy environment.
- **Uncertainty surrounding post-Brexit trading arrangements in Northern Ireland** – Challenges relating to the implementation of the Northern Ireland Protocol are continuing, particularly with regards to the new checks and processes required when moving some goods from Great Britain to Northern Ireland. The 2021 Q2 Quarterly Economic Survey published by the *NI Chamber* and *BDO* showed that 32% of firms are experiencing difficulties resulting from the new arrangements, but this was down from 41% in the Q1 survey. Two thirds of respondents also said that the arrangements could present opportunities for Northern Ireland. However, the current situation is fragile and political uncertainty regarding the future implementation of the Protocol remains elevated. The extension of the grace periods, which had been due to end at the start of October, will hopefully provide the time needed for the UK and EU to continue engaging and reach agreement on a way forward. But until a consensus is agreed, these post-Brexit impacts are likely to remain a significant source of uncertainty for businesses.

In addition, a key global uncertainty relates to:

- **An uneven recovery from the pandemic-triggered downturn** – The global economy is continuing to recover from the pandemic-induced recession. However, this has not been the case everywhere with case numbers, vaccine availability and uptake, and restrictions differing across countries. Ongoing coronavirus-related disruption occurring in different countries runs the risk of escalating with spillover effects on global trade flows. There is also the risk that the pandemic will have longer-term scarring effects on economies around the world, with unemployment running at higher rates and firms and households taking a more cautious approach to spending for a longer period of time.

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