Northern Ireland Quarterly Sectoral Forecasts

Forecast summary

The Northern Ireland economy expanded again in the third quarter of 2021 but the pace of growth slowed. Growth is also expected to have slowed in the fourth quarter as supply side issues continued and the emergence of the new Omicron coronavirus variant likely stifled activity in the consumer-focused sectors. The new coronavirus variant and the rise in positive Covid-19 case numbers have increased the likelihood of consumers behaving more cautiously at the beginning of 2022 and more people having to self-isolate is also likely to weigh on activity levels. In addition to this, high inflation and supply chain disruption are continuing to pose challenges for consumers and businesses. We now estimate that the Northern Ireland economy grew by 6.2% in 2021 and have revised our forecast for growth in 2022 down to around 4.0%.

Pace of economic growth likely slowed in second half of 2021

Following strong economic growth in the second quarter of 2021, the latest data showed that the rate of economic expansion in Northern Ireland softened in the third quarter of the year.

The Index of Services showed that output increased by 2.8% over the quarter to 2021 Q3 (a slowdown from the 5.5% rise in quarter two). Activity in the other services sector rose by 4.8%, with the business services and finance sector experiencing a 4.0% rise in output. However, the Index of Production showed no change when compared with the previous quarter after having grown by 1.8% in 2021 Q2. Manufacturing, which is the largest component of the index, did experience a modest 0.3% increase in activity in quarter three, but other production sectors such as electricity, gas, steam & air conditioning and mining & quarrying saw declines in output.

We expect the Northern Ireland economy to have experienced a further slowdown in the pace of growth in the final quarter of the year, as supply-side factors continued to have an impact on output and the emergence of the Omicron coronavirus variant likely contributed to more muted consumer activity. Overall, and after taking account of the latest national and local data, we estimate that economic output in Northern Ireland increased by 6.2% in 2021 and are forecasting growth of around 4.0% in 2022, lower than the 4.7% in our previous report.

Employee jobs now projected to have increased in 2021, with unemployment also remaining relatively low

The latest data from the Quarterly Employment Survey showed a 1.0% quarterly rise in the number of employee jobs in Northern Ireland in 2021 Q3. The rate of expansion was the strongest since the final quarter of 2017 and follows on from more modest jobs growth in the first two quarters of the year.

The Coronavirus Job Retention Scheme finished at the end of September 2021 but the labour market data published to date suggests that unemployment did not rise sharply once this support came to an end. HMRC PAYE data for November 2021 showed that the number of payrolled employees increased by 0.7% compared with the previous month to a record high of 771,000. The number of people on the claimant count declined by 3.4% in November 2021. The unemployment rate also fell over the quarter to 3.6% in the August-October 2021 period, significantly below the historical 20-year average of 5.4%.

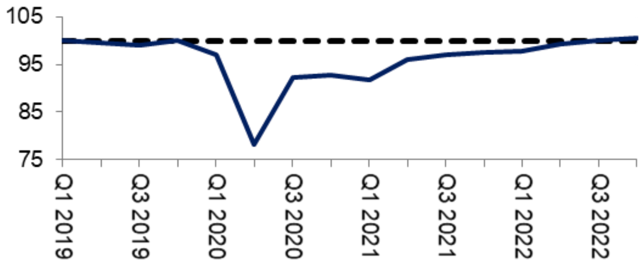
Given the recent strength of the labour market, we now estimate that the average annual number of employee jobs increased by 0.2% in 2021, and are projecting a further rise of around 1.4% in 2022. We also expect the unemployment rate to average 3.8% in 2021 and 3.9% in 2022.

Forecast summary (%)

	2020	2021	2022
UK GDP growth	-9.4	7.2	4.2
NI GVA growth	-9.7	6.2	4.0
NI consumer spending growth	-10.8	5.0	5.0
NI employee jobs growth	-0.4	0.2	1.4
NI unemployment rate	3.0	3.8	3.9
UK CPI inflation rate	0.9	2.6	4.5

Source: Oxford Economics, Danske Bank Analysis

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



Source: Oxford Economics, Danske Bank Analysis

Key factors in the outlook

Omicron coronavirus variant and high Covid-19 case numbers present new obstacles to recovery

The emergence of the Omicron coronavirus variant, and the sharp rise in the number of positive Covid-19 cases, represent further challenges to the recovery of the Northern Ireland economy. At this stage, the restrictions that have been implemented are not as stringent as those in place during the first quarter of 2021, when economic activity declined. However, there is considerable uncertainty around whether further restrictions aimed at limiting the spread of the virus may yet be necessary. Even in the absence of formal restrictions, higher Covid-19 case numbers are likely to lead consumers to behave more cautiously, particularly with regards to social consumption activities. The increase in the number of people required to isolate due to having contracted the virus and therefore unable to go to work is expected to weigh on activity levels, and there is also the potential that the ongoing supply chain disruption could be further exacerbated.

Supply chain disruption contributing to higher rates of inflation and weighing on activity levels

Higher fuel and energy prices, combined with global supply chain disruption, have contributed to a sharp rise in the rate of inflation in the UK. In November 2021, CPI inflation reached 5.1% - the highest it has been since September 2011. We think inflation will peak in the second quarter of 2022 before gradually starting to decline. However, it is expected to remain above its 2% target at the end of the year and we are forecasting that it will average around 4.5% in 2022. We continue to think that this period of higher inflation will prove temporary and that inflation will gradually move back towards its target as the pandemic-driven inflationary impacts begin to dissipate. But while inflation remains high it will put pressure on real wages and erode households' purchasing power, weighing down on the rate of growth of consumer spending. It's also important to note that while supply chain disruption is having inflationary impacts, it is also holding back output growth as activity levels at goods-based firms are restricted by shortages of, and delays in receiving, the materials they need to do business.

Changes to monetary and fiscal policy

At its December 2021 meeting, the Bank of England's Monetary Policy Committee responded to the rise in inflation by increasing Bank Rate to 0.25%. While this higher inflation is expected to be temporary, the rate of price rises is expected to remain above its 2% target throughout 2022. We think that 2022 will see a further tightening in monetary policy, with one or two further rises in Bank Rate by the end of the year. Fiscal policy is also set to change with the extent of coronavirus support to consumers and businesses now more limited, freezes in the 2022/23 income tax thresholds and the increase in National Insurance contributions.

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, with a further strengthening of customs rules in Great Britain taking effect from the beginning of January 2022. The implementation of the Northern Ireland Protocol has also led to new processes for local firms when purchasing certain goods. Negotiations are underway regarding the future implementation of the Protocol, with both the UK and EU having submitted proposals during 2021, but the path towards reaching agreement is not straightforward. For now, uncertainty remains elevated and this may impact consumer and business confidence.

The labour market appears to be in a relatively strong position

The labour market in Northern Ireland appears to be in a stronger position following the end of the Coronavirus Job Retention Scheme than had previously been expected. The number of payrolled employees reached a record high in November 2021 and the unemployment rate for the August – October 2021 period was just 3.6%, well below its long-term average. Indeed, the most pressing labour market issues are around skills shortages and recruitment difficulties. However, the relatively strong labour market data shows that many people are still in work and that demand for labour remains robust. The strong labour market could also give some support to consumer spending at a time when other factors, such as high inflation, are likely to hold it back.

Sectoral outlook

Economic growth slowed in 2021 Q3, and the Omicron coronavirus variant has likely dampened growth further
The Northern Ireland economy continued to grow in the third quarter of the year, but the pace of expansion slowed as most of the large, initial post-lockdown gains had already been realised. The emergence of the Omicron coronavirus variant likely contributed to lower-than-expected consumer activity in the final quarter of the year and this is also expected to be the case in the first quarter of 2022, while supply-side issues such as supply chain disruption and labour shortages are continuing to weigh on output. We have revised our forecast for economic growth in Northern Ireland down to 4.0% in 2022, following an estimated increase of 6.2% in 2021.

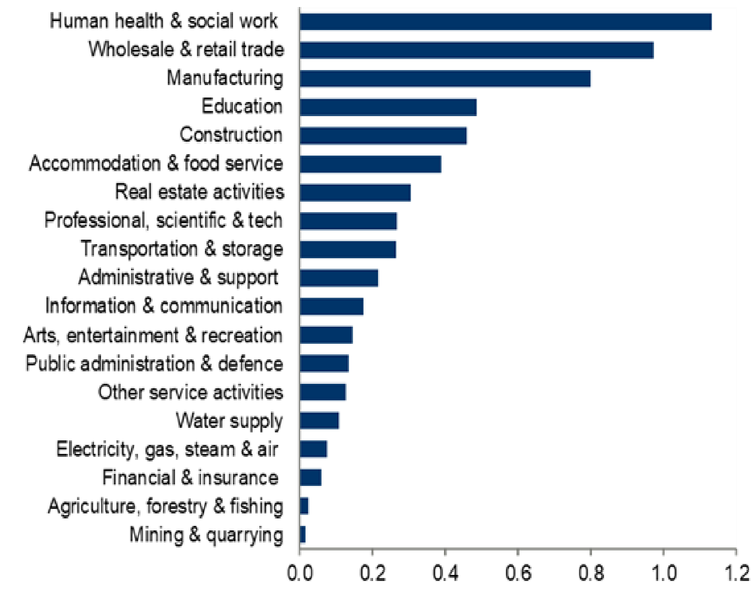
We estimate that the consumer-focused sectors, namely **accommodation & food services** and **arts, entertainment & recreation** experienced the fastest rates of growth in 2021, of around 18.7% and 14.5% respectively. We expect these sectors to post the strongest growth rates again in 2022 as their recovery from the large annual drops in output in 2020 continues. However, this expansion is likely to be at a slower pace than previously forecasted given the potential for a subdued start to the year resulting from the emergence of the Omicron coronavirus variant.

Output in the **wholesale & retail trade** sector is estimated to have risen by 7.0% in 2021 but the squeeze on household purchasing power, supply chain disruption and deteriorating consumer sentiment, as evidenced by the fall in the Danske Bank Northern Ireland Consumer Confidence Index in 2021 Q3 (before the emergence of Omicron), may lead to both demand and supply challenges in this sector. We are forecasting output growth in this industry of 4.2% in 2022.

Our forecast for growth in the **manufacturing** sector in 2021 is slightly lower than that for the overall economy at 6.0%. Output growth slowed in the sector in 2021 Q3, with the latest Index of Production reporting a 0.3% quarterly rise in activity. The data showed that the largest rise in activity in the third quarter occurred in the chemical & pharmaceutical subsector, most likely driven by coronavirus-related demand but there were falls in output in other areas, notably in the basic metals and fabricated metal products subsector. Ongoing supply constraints and upward price pressures for raw materials, energy, and wages are negatively impacting the sector. We are forecasting that manufacturing output will grow by around 3.9% in 2022. Some of these issues may also affect the **construction** industry and as a result we now expect activity in this sector to grow by about 4.6% in 2022, following projected growth of 6.3% in 2021.

We estimate that activity in the **professional, scientific & technical services** and **information & communication** sectors grew by around 6.2% and 5.5% respectively in 2021. In 2022, we expect output growth in these industries to be above that for the overall economy as these sectors, which were traditionally strong performers prior to the onset of the pandemic, continue to grow relatively strongly. We are forecasting expansion in both sectors of around 4.9%.

Sector contributions to GVA growth in 2021



Source: Oxford Economics, Danske Bank Analysis

GVA (%)	2021	2022
Accommodation & food service	18.7	17.7
Arts, entertainment & recreation	14.5	11.7
Human health & social work	10.0	4.1
Education	9.1	5.9
Administrative & support	7.5	7.9
Other service activities	7.5	7.9
Transportation & storage	7.3	7.2
Wholesale & retail trade	7.0	4.2
Water supply	6.8	3.2
Mining & quarrying	6.4	4.6
Construction	6.3	4.6
Professional, scientific & tech	6.2	4.9
Manufacturing	6.0	3.9
Information & communication	5.5	4.9
Electricity, gas, steam & air	4.7	1.6
Real estate activities	2.6	0.5
Public administration & defence	1.6	0.3
Financial & insurance	1.4	0.8
Agriculture, forestry & fishing	1.2	1.2
Total	**6.2**	**4.0**

Source: Oxford Economics, Danske Bank Analysis

Labour market outlook

We now estimate that the number of employee jobs increased in 2021, with further growth expected in 2022
The latest data from the Quarterly Employment Survey showed strong labour market growth in the third quarter of 2021, with the number of employee jobs rising by 1.0% over the three-month period to September. The timelier HMRC PAYE data also supports the view that the labour market is in a relatively strong position, with the number of payrolled employees in November 2021 rising at a monthly rate of 0.7%. As a result of this data, we have strengthened our labour market outlook and now estimate that the annual average number of employee jobs in Northern Ireland increased by 0.2% in 2021, and are forecasting further growth of around 1.4% in 2022. This would represent an above trend rate of expansion in employee jobs in 2022.

While we estimate that there was an overall rise in the average number of employee jobs in 2021, there were large variations in performance at a sector level. The **information & communication** sector is estimated to have experienced the largest annual rise in employment of 5.0% in 2021, and the **professional, scientific & technical services** sector is also projected to have seen strong jobs growth of 3.4%. However, not all business services sectors experienced growth – the **financial & insurance services** sector is projected to have experienced a decline in employment of 2.2%. However, we expect the number of jobs in the sector to rise by around 0.9% in 2022.

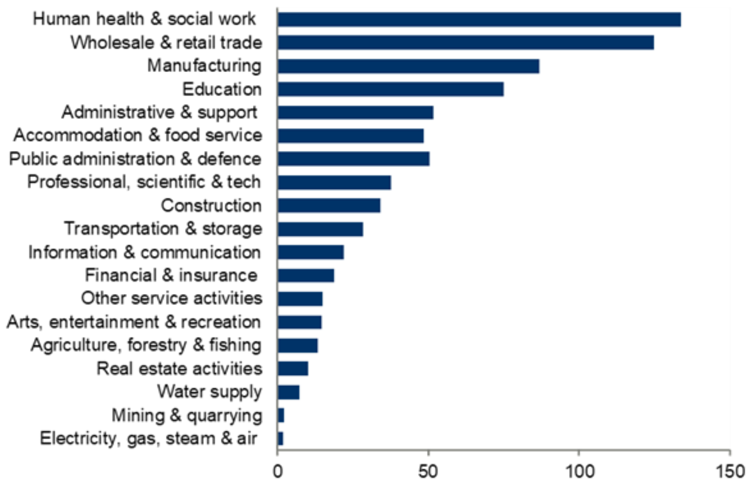
The **public administration & defence**, **human health & social work** and **education** sectors are also likely to have experienced above average employee jobs growth in 2021, but we are forecasting a slowdown in employment growth in these sectors in 2022.

We estimate that employment in the **manufacturing** sector rose by 0.4% in 2021, an upward revision from our last report based on the strong jobs growth in 2021 Q3. In contrast, employee jobs in the **construction** sector fell by an estimated 3.6% in 2021 – the sharpest fall out of all the sectors. We are forecasting a rise in the average number of employee jobs in both sectors in 2022, of around 1.0% and 2.2% respectively.

The annual average number of employee jobs in the **arts, entertainment & recreation** and **accommodation & food service** sectors is estimated to have declined by 3.5% and 2.5% respectively in 2021. While these sectors achieved the fastest quarterly rates of increase in quarter three, we do not expect that this pace of growth continued into quarter four as the biggest gains following the easing of coronavirus restrictions had already been realised, labour shortages were widespread and the Omicron coronavirus variant likely stifled consumer activity. However, these sectors are forecast to achieve relatively high rates of job growth in 2022, of 3.4% and 2.6% respectively, as their recovery continues. Similarly, **wholesale & retail trade** is forecast to experience a 1.8% rise in employment 2022, following an estimated contraction of 2.6% in 2021.

The unemployment rate in Northern Ireland fell to 3.6% in the August-October 2021 period. We are forecasting that the unemployment rate in Northern Ireland will average around 3.9% in 2022, similar to our 3.8% estimate for 2021.

Employee jobs per sector in 2021



Source: Oxford Economics, Danske Bank Analysis

Employee jobs (%)	2021	2022
Information & communication	5.0	2.2
Mining & quarrying	4.0	1.0
Professional, scientific & tech	3.4	1.2
Education	2.9	0.5
Electricity, gas, steam & air	2.5	0.9
Real estate activities	2.3	0.5
Administrative & support	2.2	1.8
Public administration & defence	2.0	0.9
Human health & social work	1.8	1.1
Agriculture, forestry & fishing	0.8	0.5
Manufacturing	0.4	1.0
Water supply	-1.9	0.7
Financial & insurance	-2.2	0.9
Other service activities	-2.2	1.8
Accommodation & food service	-2.5	2.6
Wholesale & retail trade	-2.6	1.8
Transportation & storage	-3.2	3.6
Arts, entertainment & recreation	-3.5	3.4
Construction	-3.6	2.2
Total	**0.2**	**1.4**

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** – The emergence of the Omicron coronavirus variant and the sharp rise in the number of positive Covid-19 cases has created considerable uncertainty around the economic outlook. At this stage, the restrictions that have been introduced to limit the spread of the virus are not as severe as those observed at other times during the pandemic, but there is the potential for further restrictions to be introduced. Our forecasts do not assume that a lockdown or a long period of more stringent restrictions is imposed but nevertheless, coronavirus-related factors are expected to weigh down on the pace of growth in the first quarter of 2022. It is also worth noting that any adverse impacts from a fall in social consumption activities will be felt most in the consumer-focused and tourism-based businesses, many of which had just started to regain momentum in the second half of 2021. The emergence of this new variant also highlights the global vulnerability to further strains of Covid-19, meaning coronavirus-related factors are likely to remain a source of significant downside risk to the performance of the economy in 2022.

- **Supply chain disruption and price pressures intensify** – 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 ultimately expected to be temporary, but it's not immediately clear for how long they will persist. If they continue for a long period of time, the supply chain disruption could have prolonged adverse impacts on output levels and further erode household spending power as higher costs are, at least in some part, passed on to consumers.

- **Prolonged uncertainty around the implementation of the post-Brexit trading arrangements** – Negotiations around the future implementation of the Northern Ireland Protocol are underway but reaching an agreement will not be straightforward. For now, challenges will continue in relation to the current arrangements, particularly with regards to the new checks and processes required when moving some goods from Great Britain to Northern Ireland. While there is the potential for the arrangements to present opportunities for Northern Ireland, this will take time to materialise. The current situation is fragile and remains a significant source of uncertainty for consumers and 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 downturn. However, this has not been the same 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. Higher case numbers across a number of countries could subdue activity levels and governments could continue to unwind support policies. 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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Contact details

Conor Lambe
Chief Economist
Email: conor.lambe@danskebank.co.uk
Twitter: @ConorLambe
LinkedIn: Conor Lambe