April 2020

Northern Ireland Quarterly Sectoral Forecasts

Forecast summary

Northern Ireland is expected to experience a staggering decline in economic growth in 2020 due to the impact of the coronavirus pandemic. Consumer spending is set to slump as restrictions on people's movement lead to lower discretionary spending and business investment is expected to fall as many firms will face cash flow and revenue challenges. We expect the shock to the economy to be concentrated in the first half of 2020 and that activity will begin to recover gradually in the second half of this year and into 2021, with government policy measures supporting the recovery. We are forecasting that the Northern Ireland economy will contract by around 7.5% in 2020 and then grow by about 5.0% in 2021. It is important to note that these forecasts are provided in a climate of high uncertainty and increased sensitivity to future events, with risks to the numbers weighted towards the downside.

The latest official data pointed to a pick-up in economic activity at the end of last year…

The Northern Ireland economy appeared to experience a slight pick-up in output in the final quarter of 2019, according to the latest data. The Northern Ireland Composite Economic Index showed that the local economy expanded by 0.2% over the quarter and by 0.6% over the year to 2019 Q4. But the coronavirus pandemic has changed the economic dynamics.

…but the short term outlook has been significantly impacted by the coronavirus pandemic

Our projections are based on the assumption that the current restrictions, which include the closure of most educational facilities, non-essential shops, restaurants and leisure facilities, remain in place until somewhere between the end of May and the middle of June. We then assume that the lockdown is gradually lifted but some social distancing measures remain in place for a longer period of time. Under these assumptions, we are forecasting that economic output in Northern Ireland will decline by around 7.5% in 2020.

The contraction is expected to be limited to the first two quarters of 2020, with the fall in economic activity in 2020 Q2 projected to be between 10%-15%. Assuming a gradual lifting of the restrictions combined with expansionary government policies, we believe that the second half of the year should see the beginning of a recovery, with the economy returning to growth in both 2020 Q3 and 2020 Q4.

This gradual recovery should then continue into next year and we expect the rate of economic growth in 2021 to be around 5.0%. However, total economic output may not return to its pre-coronavirus level until late in 2022 or into 2023.

Employment is set to fall, but government intervention should limit the number of job losses

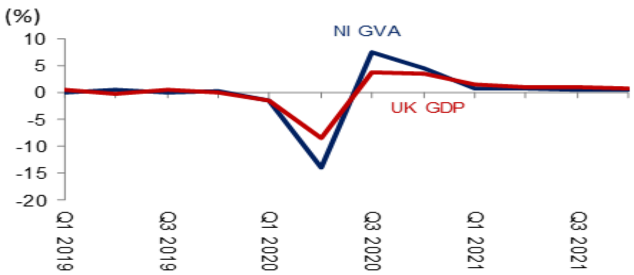
We believe that policy measures, such as the Coronavirus Job Retention Scheme, will help to minimise the number of job losses as a result of the pandemic. However, employment is still expected to fall this year. We expect the number of employee jobs to fall by around 2.3% in 2020 and the annual unemployment rate to increase to about 5.0%. However, we do expect to see some recovery in the labour market in 2021 with the number of jobs rising by approximately 1.2% and the unemployment rate coming down to around 4.5%.

Forecast summary (%)

	2020	2021
UK GDP growth	-7.0	5.0
NI GVA growth	-7.5	5.0
NI consumer spending growth	-8.0	5.5
NI employee jobs growth	-2.3	1.2
NI unemployment rate	5.0	4.5
UK CPI inflation rate	0.8	1.5

Source: Oxford Economics, Danske Bank Analysis

Economic growth (quarter-on-quarter)



Source: Oxford Economics, Danske Bank Analysis

Key factors in the outlook

Key factors underpinning the fall in output in the first half of 2020:

Lower discretionary spending by households
Consumer spending is expected to fall sharply due to a combination of social distancing measures, more precautionary consumer behaviours and subdued confidence levels. In addition, lower incomes for those who have been furloughed (and are receiving 80% of their usual salary), or who have become unemployed will also depress spending. We may instead see an increase in savings as households look to rebuild savings pots that they have had to run down in recent weeks or to increase their savings as a safety net against potential unemployment. We are forecasting that annual consumer spending in Northern Ireland will fall by about 8.0% in 2020.

Sharp drop in business investment
The coronavirus pandemic has already had a severe negative impact on business in Northern Ireland. A recent survey from the Northern Ireland Chamber of Commerce and BDO revealed that 75% of firms have seen a significant fall in revenue, while a survey from Belfast Chamber, Causeway Chamber, Londonderry Chamber and Newry Chamber showed that over 40% of businesses are currently closed. With businesses facing significant short-term challenges, and uncertainty about the depth and duration of this crisis particularly elevated, many firms are expected to postpone capital spending decisions. As such, business investment is expected to contract sharply in 2020.

Lower working hours
A reduction in hours worked is also expected to reduce economic output. Many businesses classed as 'non-essential' are temporarily closed if staff cannot work from home. The closure of schools for the majority of children means that many working parents have had to reduce their hours. Working hours are also expected to be reduced by people taking time off work due to having contracted Covid-19.

Key factors impacting the recovery in economic activity from 2020 Q3:

Government policy initiatives providing support to businesses and employees
The UK Government has launched a number of policy initiatives to support firms and workers that are negatively impacted by the coronavirus pandemic. These measures include the Job Retention Scheme, the Self Employment Income Support Scheme, the Coronavirus Business Interruption Loan Scheme and deferring VAT payments. In Northern Ireland policy measures have included grants to small businesses, grants to hospitality, tourism and retail firms and a three month business rates holiday. While the pandemic will still lead to a rise in unemployment and some businesses becoming insolvent, these policy measures are expected to limit the number of job losses and business closures, and support firms to start trading again from 2020 Q3 onwards.

Loose monetary policy facilitating a return to economic growth
In March, the Bank of England's Monetary Policy Committee (MPC) cut Bank Rate to its effective floor of 0.1% and restarted quantitative easing with £200bn of asset purchases, consisting of gilts and private sector securities. The MPC's decision to hold rates at 0.1% at its meeting ending on 25 March 2020 was unsurprising, but the committee made it clear that it is not out of monetary policy ammunition. We do not expect any further changes to interest rates during the rest of this year, or in 2021, but there is scope for further expansion in the asset purchase programme if the economy appears to be in need of additional stimulus.

Changes to consumer and business behaviours
As a result of the pandemic, consumers are visiting those shops that remain open less frequently and are trying to avoid crowded areas. It is likely that this will persist to some extent once the lockdown is lifted as people continue to behave somewhat cautiously. Some businesses may also behave prudently with regards to how quickly they revert from having staff work from home or in their investment decisions. This shift in consumer and business attitudes is likely to dampen the speed of the recovery.

Sectoral outlook

Coronavirus pandemic to cause short, sharp recession in 2020, but gradual recovery to begin later this year
Prior to the outbreak of coronavirus, economic growth in Northern Ireland was subdued – even accounting for the slight pick up towards the end of 2019. The introduction of the current lockdown measures and widespread social distancing in response to the pandemic will have a large impact on the already sluggish economy. Official data on the economic impact of the coronavirus pandemic is not yet available. But the available early indicators such as new car sales data, which provides some insight into consumer spending trends, suffered a major hit with a 56% drop in the year to March. We are forecasting that economic output in Northern Ireland will contract by 7.5% this year but expect a gradual recovery to start in the second half of the year as lockdown measures are slowly relaxed. We expect the economy to grow by around 5.0% in 2021, although it is important to note that total output may not return to its pre-coronavirus level until late in 2022 or into 2023.

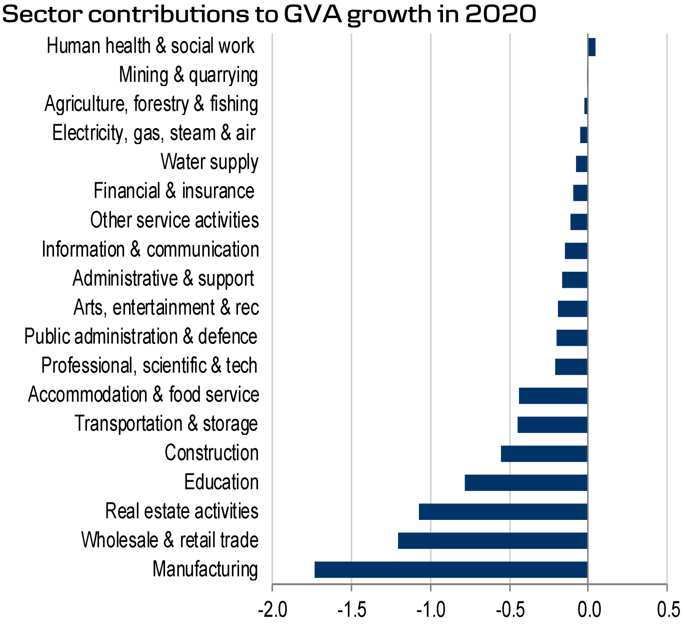
With the aim of slowing the spread of coronavirus, the Government has introduced a range of social distancing measures. Currently, people are only permitted to leave their homes for a limited number of reasons and most schools, non-essential shops and leisure facilities are closed. Our forecast assumes that the current measures remain in place until somewhere between the end of May and the middle of June before being gradually lifted, but that some social distancing measures remain in place for a longer period of time. As a result of the lockdown and social distancing, the **accommodation & food, arts, entertainment & recreation** and **education** sectors are forecast to experience the largest falls in output this year.

The **wholesale & retail trade** sector has seen a sharp fall in activity in recent weeks and we are now forecasting that the sector will experience an annual fall in output of 8.5% in 2020. A significant proportion of consumer spending occurs in crowded retail areas and we expect that this will experience a drastic reduction under social distancing rules. However, continued spending on essential items and online orders may somewhat offset this, meaning that the industry isn't expected to be quite as severely impacted as the other consumer-focused sectors.

Both **manufacturing** and **construction** are expected to experience sharp declines in output, with falls of around 12.0% and 7.7% in 2020 respectively. Extensive shutdowns, in addition to steep falls in orders, are impacting both sectors. And, given the global nature of this pandemic, there is a risk that supply chain issues may impact their recovery once the local economy begins to get moving again.

Human health & social work is the only sector expected to experience an annual increase in GVA this year, due to the increased demand being placed on the sector. We are forecasting an increase in activity of 0.4% this year and a further 0.4% in 2021.

Sector contributions to GVA growth in 2020



Source: Oxford Economics, Danske Bank Analysis

GVA (%)	2020	2021
Human health & social work	0.4	0.4
Agriculture, forestry & fishing	-1.5	0.8
Mining & quarrying	-2.4	1.6
Public administration & defence	-2.4	1.2
Financial & insurance	-2.6	1.1
Information & communication	-4.1	4.3
Water supply	-4.3	3.4
Electricity, gas, steam & air	-4.5	3.9
Professional, scientific & tech	-4.9	3.7
Administrative & support	-5.4	2.4
Other service activities	-6.5	2.4
Construction	-7.7	5.3
Wholesale & retail trade	-8.5	5.7
Real estate activities	-9.5	6.0
Transportation & storage	-11.5	8.5
Manufacturing	-12.0	8.6
Education	-14.2	12.5
Arts, entertainment & rec	-16.8	13.0
Accommodation & food service	-17.0	12.6
Total	**-7.5**	**5.0**

Source: Oxford Economics, Danske Bank Analysis

Labour market outlook

Job losses are expected, but government support schemes should limit the long-term impacts
The labour market in Northern Ireland will also be negatively impacted by the coronavirus pandemic, with the average number of employee jobs expected to fall by around 2.3% in 2020 compared with 2019. This forecast accounts for the expectation that government support schemes will help to limit the number of job losses, and therefore also reduce the long-term impacts on the economy. The schemes (the Job Retention Scheme and Self Employment Income Support Scheme) enable firms to avoid lay-offs by providing 80% of employees' salaries up to £2,500, and for self-employed people to receive a similar benefit. The uptake of these schemes is high – the NI Chamber of Commerce and BDO survey showed that 80% of firms intended to furlough some, or all, of their employees when the scheme was rolled out, and just 17% didn't intend to furlough any staff. We expect the labour market to recover somewhat in 2021, with the number of jobs rising by 1.2%. We are also forecasting that the average annual unemployment rate will increase to 5.0% in 2020, though it is likely to reach higher levels in the second and third quarters of this year, before falling to an average of 4.5% in 2021.

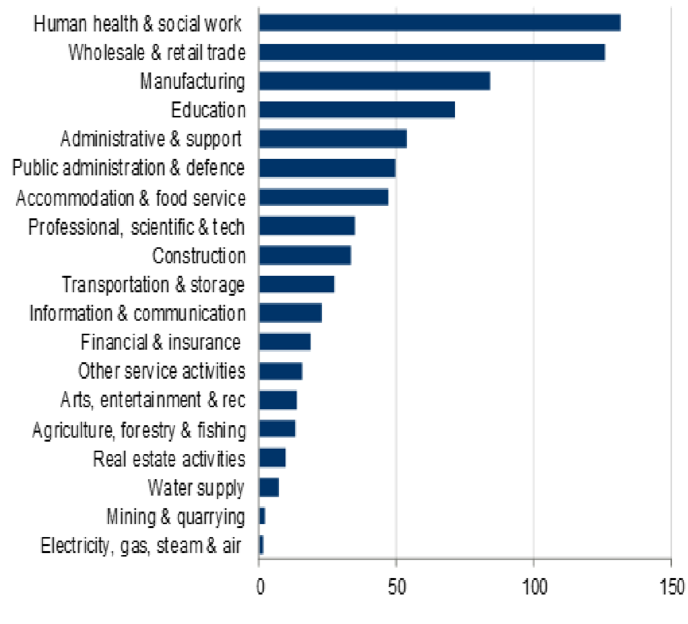
Given the nature of recent events, the public sector has the strongest forecast for employee jobs growth this year, with **human health & social work** and **public administration & defence** expected to experience increases in employment of 0.9% and 0.5% respectively. These sectors are likely to see increased demand in the short-term to provide additional public services during the pandemic. **Education** is expected to see only a small fall in the number of jobs, as the temporary school closures are unlikely to lead to large scale job losses.

The business services sectors are forecast to experience declines in employment this year. The **information & communication, professional, scientific & technical services** and **administration & support services** sectors are expected to see job losses, but at a less sharp decline than the average for the overall economy. We expect employment in each of these sectors to return to growth in 2021.

Despite the government's best efforts to minimise redundancies, we still expect there to be significant job losses in the consumer-focused sectors in 2020. **Accommodation & food services** and **arts, entertainment & recreation** are forecast to experience contractions in employment of 9.2% and 8.1% respectively but could regain some of those jobs in 2021.

Similarly, both **construction** and **manufacturing** are also set to experience job losses this year, as non-essential factories and sites are closed temporarily. But we expect that the total number of jobs in both sectors will increase in 2021.

Employee jobs per sector in 2020



Source: Oxford Economics, Dankse Bank Analysis

Employee jobs (%)	2020	2021
Human health & social work	0.9	0.1
Public administration & defence	0.5	0.1
Agriculture, forestry & fishing	-0.2	0.1
Electricity, gas, steam & air	-0.2	0.2
Education	-0.3	0.1
Water supply	-0.3	0.1
Mining & quarrying	-0.5	0.1
Financial & insurance	-0.5	0.1
Other service activities	-0.6	0.3
Information & communication	-0.7	0.8
Professional, scientific & tech	-1.1	0.7
Real estate activities	-1.2	0.4
Administrative & support	-1.6	0.6
Construction	-3.9	1.4
Wholesale & retail trade	-4.0	1.2
Transportation & storage	-4.3	1.6
Manufacturing	-4.5	2.1
Arts, entertainment & rec	-8.1	6.1
Accommodation & food service	-9.2	7.2
Total	**-2.3**	**1.2**

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 much more elevated than is normally the case. In addition, we would note that the risks around this set of forecasts are weighted more towards the downside. The main sources of uncertainty include:

- **Coronavirus –** The coronavirus pandemic is currently the most significant issue facing the economy. Our assumption is that the current restrictions on people's movement and temporary business closures will remain in place until somewhere between the end of May and the middle of June. We then assume that the lockdown is gradually lifted but some social distancing measures remain in place for a longer period of time. We expect the short-term economic shock to be concentrated in the first half of 2020 and that economic activity will begin to recover from the second half of this year onwards. One potential risk to this assumption is that aggregate demand in the economy does not recover as quickly as we expect and that financial conditions tighten further, both of which would limit the extent of the rebound in economic activity. This could happen if, for example, large numbers of firms go out of business and there is a sharp rise in unemployment. There is also the risk of lockdown measures continuing into the second half of 2020, or having to be reinstated later in the year, or indeed in 2021. In addition, the effects of the lockdown could lead to even greater changes in consumer and business behaviour towards more precautionary spending habits than we have assumed, which would mean it would take a longer period of time to return to the spending and investment levels seen prior to the pandemic.

- **Brexit –** the UK formally left the EU on 31 January 2020 and is now in a transition period during which trading arrangements between the two economies remain unchanged from what they were previously. During this period, which is due to last until the end of 2020, the UK and EU are attempting to negotiate the terms of their future relationship, including specific arrangements related to the movement of goods to and from Northern Ireland. For local businesses, there are still many sources of Brexit-related uncertainty. These include what goods coming into Northern Ireland from outside the EU will be liable for tariffs, what paperwork firms will need to complete when moving goods, to what extent local businesses will or will not benefit from any third country trade deals agreed by the UK and how services firms will trade with the EU once the transition period ends. These talks were always likely to be complex, particularly given the short period of time available in which to conclude them. But the subsequent disruption caused by the coronavirus pandemic and the resulting switch of political priorities means that concluding a deal by the end of this year is now even more challenging. The deadline for agreeing an extension to the transition period is 1 July 2020, but government policy is still that the transition period will not be extended and will conclude at the end of this year. If a new long-term trading agreement between the UK and the EU is not reached and the transition period is not extended, then economic output will be even lower than we are currently forecasting.

In addition, key global uncertainties include:

- **Prolonged global recession –** While we anticipate a short, sharp recession globally as a result of the coronavirus pandemic, there is a risk that the short-term economic costs from shutdowns and wider disruption are larger and more drawn out, or that such losses are exacerbated by spill-overs to the real economy from tighter financial conditions. There is also the risk that the pandemic will have long-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, thus prolonging the duration of the recession and the amount of time needed for economic output to return to its pre-coronavirus level.

- **Vulnerability in global oil markets –** Global oil prices have plummeted amid the unprecedented fall in demand resulting from the coronavirus pandemic. Production cuts may limit further price falls, but it is possible that there will still be a large surplus of oil in the market. This could prove challenging for some oil producing economies that may not be in a position to effectively handle both the costs of the pandemic and a period of lower oil revenues.

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