UK Outlook

July 2022

Economic Update

Bank of Ireland

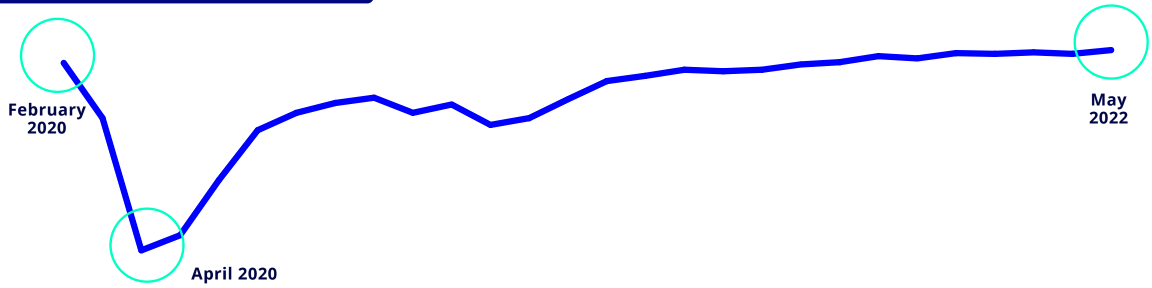
Cost of living squeeze slows growth

The fallout from Russia's invasion of Ukraine is taking a toll on the UK economy. GDP growth moderated through May and high-frequency indicators point to more slowing since. While the lifting of public health restrictions earlier this year is helping some sectors claw back ground lost during the pandemic, the consequences of the war are weighing on overall activity. Elevated energy prices have contributed to an increase in the cost of living resulting in a drop in consumer confidence to a multi-decade low. Business optimism is also flagging amid supply chain disruption, high costs and uncertainty about demand. Moreover, financing conditions have tightened as the Bank of England has steadily raised interest rates. In light of all this, we have again lowered our forecasts for growth while lifting those for consumer price inflation. GDP is now expected to increase by 3.5% in 2022 (-¼ percentage point from April's update) - this is consistent with the economy grinding to a halt after a solid first quarter performance - and by 0.6% in 2023 (circa -1 percentage point), with inflation averaging 9.2% and 6.0% respectively (+1¼ and +1½ percentage points). High inflation is exerting a significant drag on household incomes and, even though the Government's 'cost of living' supports will ease the burden somewhat, consumer spending is expected to slow sharply. Weaker demand will dampen business investment and exports, with political uncertainty and tensions between London and Brussels additional headwinds in this regard. The economic outlook remains subject to considerable risks, related inter alia to the path for energy prices and the degree of monetary policy tightening needed to return inflation to its 2% target.

Economic Overview

Recent Developments

GDP has rebounded



Post-restrictions tailwinds

Job gains
2.1%
YoY March-May 2022

Inflation
@ 9.4%
YoY June 2022

Cost of living supports

Composite PMI
@ 52.8
Flash July 2022

Uncertain global outlook

BoE interest rate
to 1.25%
at June 2022 meeting

£ narrow range versus euro

Outlook

	GDP	Consumer Spending	Investment	Exports	Employment	Unemployment Rate	Inflation
2021	7.4%	6.2%	5.9%	-1.3%	-0.3%	4.5%	2.6%
2022f	3.5%	3.8%	6.0%	5.3%	1.2%	3.9%	9.2%
2023f	0.6%	0.6%	3.0%	3.8%	0.5%	4.1%	6.0%

Fallout from the war taking a toll

Inflation and rising interest rates a drag

GDP slowing but recession narrowly avoided

Risks

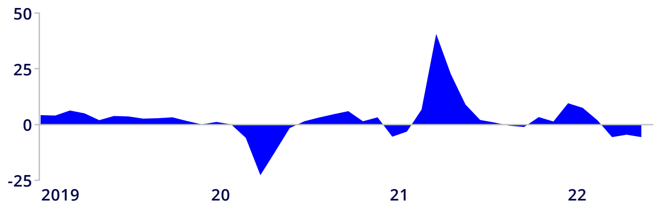
- Geopolitics
- Policy missteps

Sources: Bank of Ireland, ONS, HM Government, Bank of England, Bloomberg, S&P Global / CIPS, IMF

Consumer

Spending softening

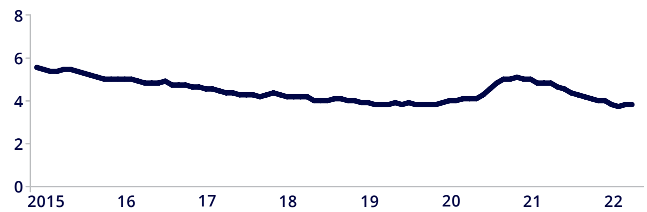
Consumer spending started off 2022 on a solid footing, increasing for a fourth consecutive quarter in Q1, but has lost momentum recently with retail sales falling by 5.5% year-on-year in the April-June period.



■ Retail Sales (annual % change, volume)
Source: ONS

Employment gains

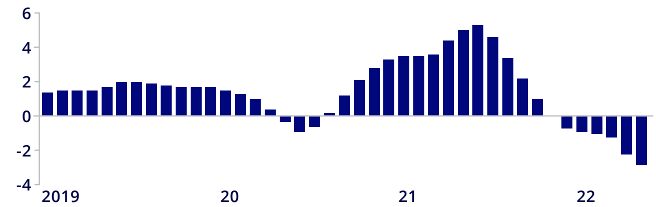
The jobs market remains a bright spot with the numbers in work increasing by 2.1% year-on-year in the three months to May and the unemployment rate running at 3.8%, in and around its pre-pandemic level.



▬ Unemployment Rate (%, 3-month moving average)
Source: ONS

Earnings pressured

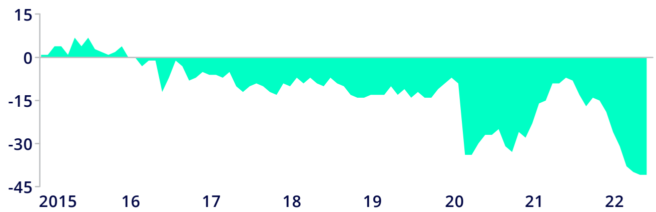
Elevated inflation is taking a toll on real earnings which are still falling on an annual basis, albeit the Government has put additional measures in place to support household incomes.



■ Real Average Weekly Earnings Excluding Bonuses (annual % change, 3-month moving average)
Source: ONS

Sentiment plunges

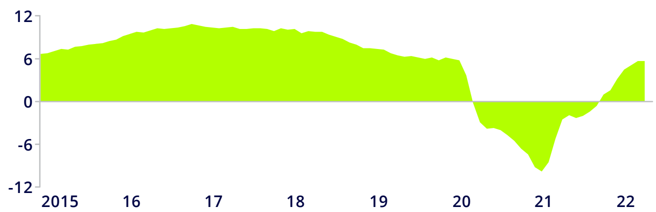
The increased cost of living as well as concerns about the general economic situation are weighing heavily on consumer confidence, which remained at a multi-decade low in July.



■ Consumer Confidence (net balance)
Source: GfK

Credit expanding

There has been a pickup in consumer credit growth recently, suggesting increased borrowing should provide some support to spending, as should the savings accumulated by households during the pandemic.



■ Consumer Credit (annual % change)
Source: Bank of England

Modest increase in prospect

With consumers clearly nervous and feeling the pinch from higher prices and interest rates, more modest growth in spending is now forecast for 2022 and 2023 than previously expected.

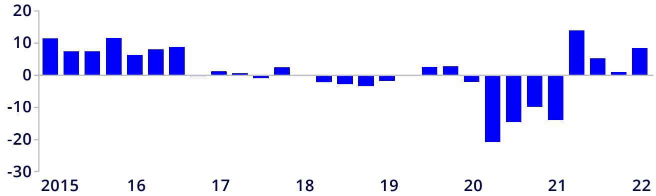
6.2%	3.8%	0.6%
2021	2022f	2023f

● Consumer Spending (annual % change, constant prices)
Source: ONS & Bank of Ireland

Business

Business investment subdued

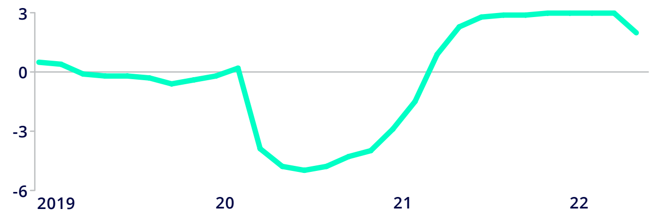
Capital spending by businesses was down 0.6% quarter-on-quarter in Q1 2022, though it was well ahead of the corresponding period in 2021.



■ Business Investment (annual % change, constant prices)
Source: ONS

Intentions ease

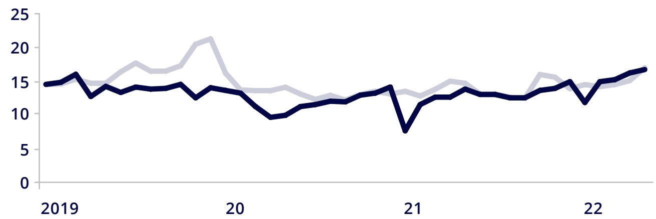
Supply chain disruption and high costs continue to constrain current investment, while firms' intentions have slipped as the war in Ukraine clouds the outlook, with domestic politics now also in flux.



Investment Intentions Next 12 Months (score)
Source: Bank of England

Exports perk up

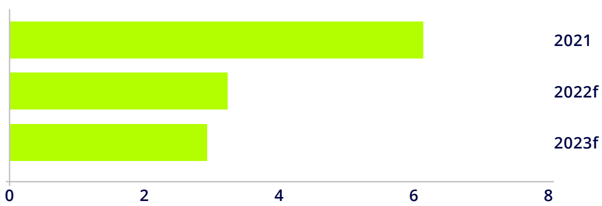
After falling in 2020 and 2021, exports have rebounded during the course of this year with both goods and services increasing year-on-year in volume terms over the five months to May.



Goods Exports (£bn, value) EU Non-EU
Source: ONS

Global situation

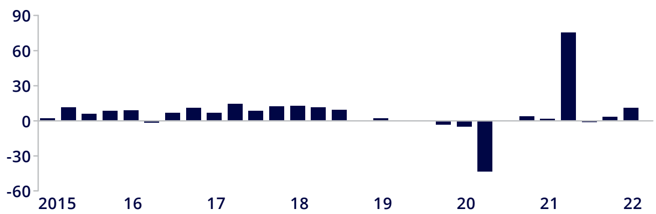
While the UK has limited direct trade links with Russia and Ukraine, the consequence of the war will be a weakening of the world economy with the IMF again lowering its forecasts for GDP growth in 2022 and 2023.



■ Global GDP (annual % change, constant prices)
Source: IMF

Housing headwinds

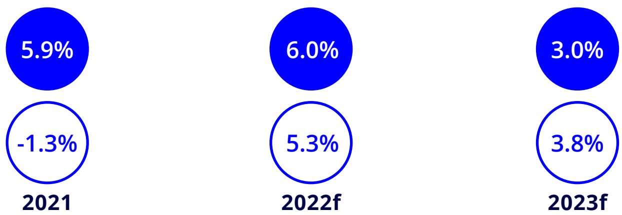
Private sector housing output increased in Q1 and house price growth has been robust if easing somewhat, though high construction costs, labour shortages and rising interest rates may weigh going forward.



■ Private Sector Investment in Dwellings (annual % change, constant prices)
Source: ONS

Slower growth ahead

Investment and exports are projected to rise in 2022 and 2023, but with political uncertainty at home added to the mix and the external backdrop weaker, the pace of expansion is set to ease.

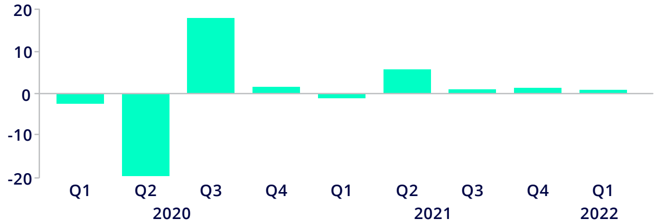


● Investment ○ Exports (annual % change, constant prices)
Source: ONS & Bank of Ireland

Overall Activity

Loss of momentum

GDP increased by 0.4% in the three months to May 2022 after rising by 0.8% in the three months to February, while the annual rate of growth slowed to 4.5% from 8.7% over the same period.



GDP (quarterly % change, constant prices)
Source: ONS

Softer outlook

The ongoing fallout from the geopolitical conflict has resulted in a further downward revision to forecasts for GDP growth this year and next, with the economy expected to only narrowly avoid recession.

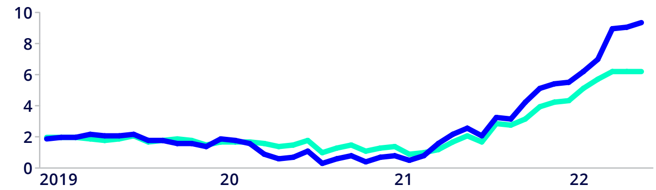
7.4%	3.5%	0.6%
2021	2022f	2023f

GDP (annual % change, constant prices)
Source: ONS & Bank of Ireland

Policy & Markets

Inflation up again

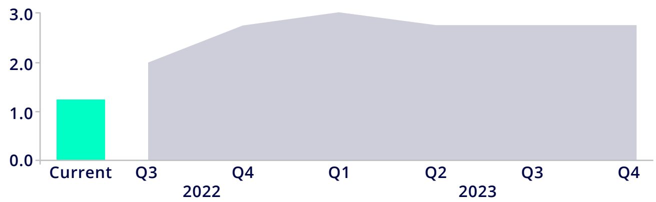
Reflecting higher energy prices, the annual rate of consumer price inflation rose further in June to 9.4%, though the ex-energy measure came in at 6.2% for a third month running.



Consumer Price Index Excluding Energy (annual % change)
Source: ONS

BOE still hiking

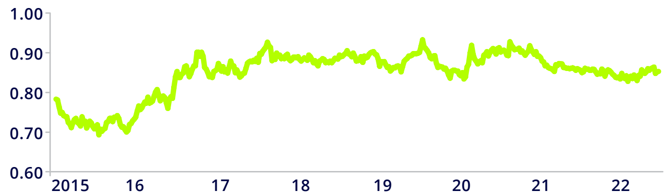
The Bank of England raised interest rates to 1.25% in June, bringing the cumulative increase since last December to 115 basis points, and said it is prepared to 'act forcefully' if necessary in response to 'persistent inflationary pressures'.



Bank Rate (%) Market Expectations
Source: Bank of England & Bloomberg

Sterling steady

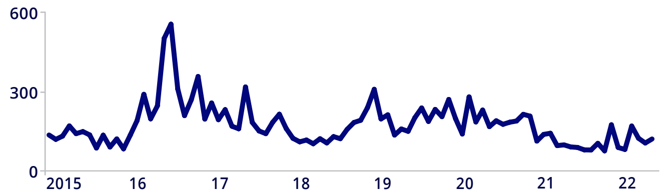
Though relations with the EU have deteriorated as the Government proceeds to unilaterally override large parts of the Northern Ireland Protocol, sterling has continued to trade in a narrow range against the euro.



€/£
Source: Bloomberg

Fresh uncertainty

The resignation of Boris Johnson as Tory party leader and Prime Minister has added to uncertainty, with the race to succeed him between Rishi Sunak (former Chancellor) and Liz Truss (current Foreign Secretary).



Economic Policy Uncertainty Index
Source: Baker, Bloom & Davis

Forecasts

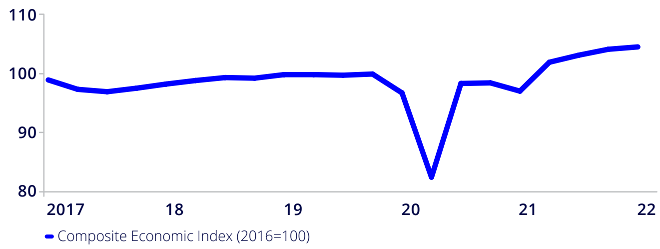
	2021	2022 (f)	2023 (f)
Personal Consumption	6.2%	3.8%	0.6%
Government Consumption	14.3%	3.0%	2.0%
Investment	5.9%	6.0%	3.0%
Exports	-1.3%	5.3%	3.8%
Imports	3.8%	10.0%	3.8%
GDP	7.4%	3.5%	0.6%
Employment	-0.3%	1.2%	0.5%
Unemployment Rate (Average)	4.5%	3.9%	4.1%
CPI	2.6%	9.2%	6.0%

Assumes Bank of England Bank Rate of 2.5% at end-2023
Annual % change unless otherwise stated; personal consumption, government consumption, investment, exports, imports and GDP are in constant prices

Northern Ireland

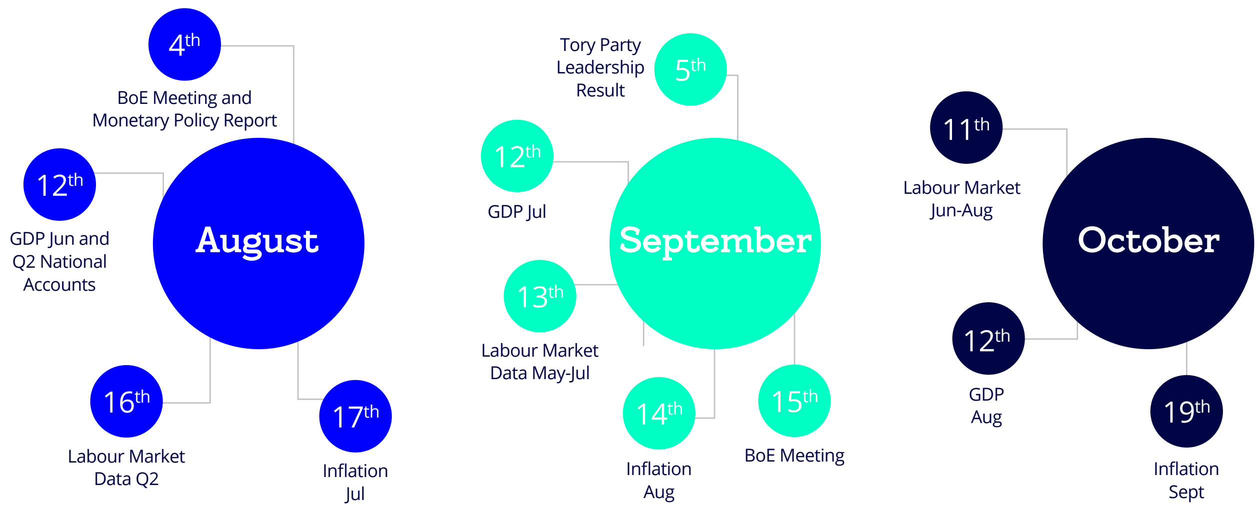
Political stalemate

The economy has rebounded from the pandemic, but tensions over the Protocol and a standoff between the political parties means the Assembly remains suspended following recent elections.



Source: NISRA

Upcoming Events



Contact Us

economics@boi.com
+353 1 250 8900

Dr. Loretta O'Sullivan
Group Chief Economist
ext. 44267

Michael Crowley
Senior Economist
ext. 44268

Conn Creedon
Senior Economist
ext. 35134

Alan Bridle
UK Economist & Market Analyst
+44 77 3636 2138

Mark Leech
Head of Media Relations
+353 87 905 3679