Making Business Sense

The Prospects Service

LEADING ECONOMIC ANALYSIS, FORECASTS AND DATA

UK Prospects, May 2020

GDP forecast for 2020 downgraded as post-lockdown bounce back likely to be limited

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- With lockdown measures still in place and businesses set to face various disruptions even after the lockdown is eased, the UK's economic outlook has deteriorated further since we published our last UK Prospects Service report in April. **We now expect the UK economy to shrink 7.0% this year. This means that even with a return to growth of 4.7% in 2021, UK GDP will not reach its Q4 2019 level until the second half of 2022.**
- **In March, retail sales volumes fell by 5.1%, the largest drop since the series began.** This was mainly caused by non-essential store closures which were made compulsory in the lockdown announcement on 23rd March. Textile, clothing and footwear stores saw a 35% monthly decline in volumes. In contrast, food stores experienced an increase in demand (10% up on February), as consumers increased their spending on groceries.
- **The annual rate of inflation on the CPIH measure declined to 1.5% in March, from 1.7% in February.** Clothing and transport costs were the biggest drivers of the decline. In the near term, the dramatic fall in aggregate demand paired with historically low commodity prices will generate considerable disinflationary pressures.
- **We expect inflation to hit a low of 1.1% in 2020 with an average of 1.8% for the year. Further ahead, inflationary pressures will be boosted by a pick-up in demand as restrictions ease (more so for restaurants, mini breaks etc than for big ticket items) and by the government's stimulus measures. In 2021, we expect inflation to peak at over 3%.**
- The unemployment rate edged up to 4.0% in the three months to February, 0.1 percentage points higher than the previous quarter. Cebr expects the true impact of the 'great shutdown' on employment to only become evident in the coming months and quarters as it is unclear how many of the people which are currently on the government's furlough scheme will become unemployed once the scheme comes to an end. **We expect the unemployment rate to average 7.7% over 2020.**
- **Following the Monetary Policy Committee's (MPC) latest announcement on 7 May, the Bank Rate remains at 0.1%.** Contrary to market expectations, we think interest rates are likely to gradually begin to rise in late 2020 and throughout 2021 in response to higher inflation. We see the Base Rate reaching 1.75% by the end of 2021.

Forecast summary

- With many shops closed, people's incomes looking less certain and consumer confidence hitting record lows, household consumption will experience a substantial hit in 2020. Consumer spending will be 8.0% lower in 2020 than in 2019. We expect a rise of 1.2% in 2021.
- Cebr anticipates exports to grow 0.5% in 2020, down from 4.8% in 2019. Growth is then set to rebound to 8.8% in 2021.
- Import growth is also set to slow this year, from 4.6% in 2019 to -0.7% in 2020. Since imports are a subtraction to GDP, this will reflect positively on the overall rate of economic growth.
- Business investment is set to tumble 15.5% over 2020. Measures will need to be taken to encourage investment for the post-2020 outlook to look less bleak.

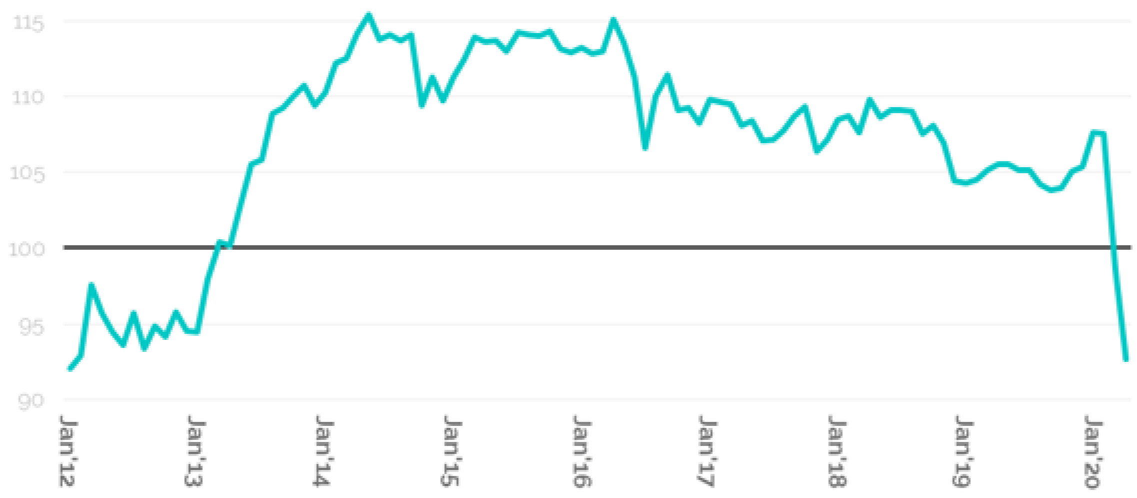
Industry outlook

- We expect real output in the wholesale and retail sector to grow by just 1.5% in 2020. The lowest annual growth figure since 2012. The outlook for the sector is challenging as non-essential stores remain shut. Grocery stores on the other hand have been reporting a strong performance and will prevent an outright contraction in the sector as a whole.
- Our 2020 forecast for real output growth in construction is -5.0%, down from 2.3% in 2019. While some construction is continuing throughout the 'great shutdown', the drop-off in investment and an expected housing market slowdown will weigh on construction activity this year. The shift to remote working has been accelerated by the coronavirus and will impact the demand for office space even in the longer term.
- We expect real manufacturing output to contract 12.9% in 2020, in response to stifled domestic and international demand and as a results of temporary factory closures. Numerous manufacturers have fully stopped production in light of the pandemic, and some of them may never reopen.
- Market turmoil and the wider economic slowdown have created a series of challenges for business services and finance. We expect a contraction of 5.5% in 2020 followed by growth of 5.2% the year after.

Leading indicators – consumer confidence

- Consumer confidence was in freefall in April, dropping 5.9 points to 92.7. This is the third consecutive monthly drop and puts the index at its lowest point since January 2012.
- Six of the eight constituent metrics fell during April. Respondents believed that their personal household financial situation had worsened over the last 30 days, with the measure falling 7.3 points to 78.6, and their estimates for the coming year also sliding 3.4 points to 83.
- Britons were equally pessimistic about house prices, with estimates of value over the last month declining 10.8 points to 93.9, and for the coming year by 13.4 points to 96.6. Both measures are now in negative territory for the first time in years.
- Respondents were increasingly pessimistic about their job security over the past month, with the measure falling 4.6 points to 80.8. However, the outlook for the coming 12 months rose fractionally by 0.5 points to 109.3, remaining firmly in positive territory.
- Surprisingly, given that these surveys were conducted after the Government imposed lockdown conditions, business activity estimates over the last month only slipped 10.2 points to 87.7. Estimates for the coming year even rose 2.3 points to 111.8. But these small glimmers of hope do little to balance the overwhelming average falls in sentiment.

Cebr/YouGov Consumer Confidence Index



Economic risks over the coming 12 months

	Risk likelihood	Comment
Many businesses permanently close as a result of the pandemic, preventing a rapid post-lockdown recovery	High	Despite the government's efforts, some businesses will never re-open following their mandatory shutdown. This may be as a result of running out of cash or the fact that the lifestyle changes brought about by the pandemic mean there is no longer sufficient demand for their products or services. Should this happen on a large scale, any post-lockdown recovery will be only gradual.
Consumers avoid leaving their homes for non-essential reasons even after they are allowed to do so	Medium	Various consumer surveys (e.g. from YouGov) suggest that many people are fearful of using transport, visiting pubs, dining out or doing other activities outside of their home. Following, many weeks of government messaging that it is dangerous to go outside, it will not be easy to change people's mindsets even as the rules on social distancing are relaxed. This may mean that even as some businesses re-open they may find themselves with few customers.

Focus On: Economic costs of the lockdown – a regional picture

Below we present the results of an analysis examining the impact the lockdown is having on each UK region. The analysis uses industry data in the UK's national accounting framework.

- Although London has the largest absolute GVA loss per day (£575m), our results show that is experiencing the lowest proportional loss. An estimated 28% of London's GVA has been lost due to the lockdown measures in comparison to 34% for the UK as a whole. This is due to the concentration of financial and professional services within the capital. These industries are largely able to work remotely and have been less affected by falls in consumer demand.
- Given the policy of self-isolation, many sectors have faced a significant demand slump. Restaurants, hotels and retail have all faced a reduction in footfall and consumer spending given the lockdown restrictions. This feeds through into other sectors, namely manufacturing; the lack of demand for final products means that the demand from factories has also fallen. This has significantly impacted manufacturing regions such as the Midlands and North.
- Scotland, Wales and Northern Ireland also have a higher proportion of their service GVA attributed to accommodation, food and beverage serving activities, arts, entertainment and recreation occupations. These roles require face-to-face interactions and hence have been most affected by the lockdown restrictions.
- Moreover, the specific lockdown restrictions are largely under the jurisdiction of the regional assemblies. This has led to slight differences in the exact nature of the lockdown between UK nations. For instance, Scotland, Wales and Northern Ireland have closed all construction sites. The generally stricter lockdown measures outside of England has also meant slightly higher falls in GVA.

GVA loss per day across the UK regions

Region	Total Loss per day £m	Total % Loss
London	575	27.7%
South East	393	34.7%
South West	185	36.3%
East of England	241	35.5%
East Midlands	164	39.7%
West Midlands	245	39.5%
North West	279	36.7%
North East	71	34.3%
Yorkshire and the Humber	170	36.6%
England	2,323	33.9%
Scotland	214	35.7%
Wales	79	36.5%
Northern Ireland	49	38.4%
UK	2,665	34.1%

- Cebr has also explored how well different regions were positioned for a large share of the labour force to start working from home.
- People in the South were more likely to have already been working from home before the crisis, meaning that they have been able to continue their usual working patterns.
- However, residents in Southern cities are likely to have less space in their homes in which to set up an office from their residence.

The full regional analysis was conducted in partnership with Irwin Mitchell and is available here.

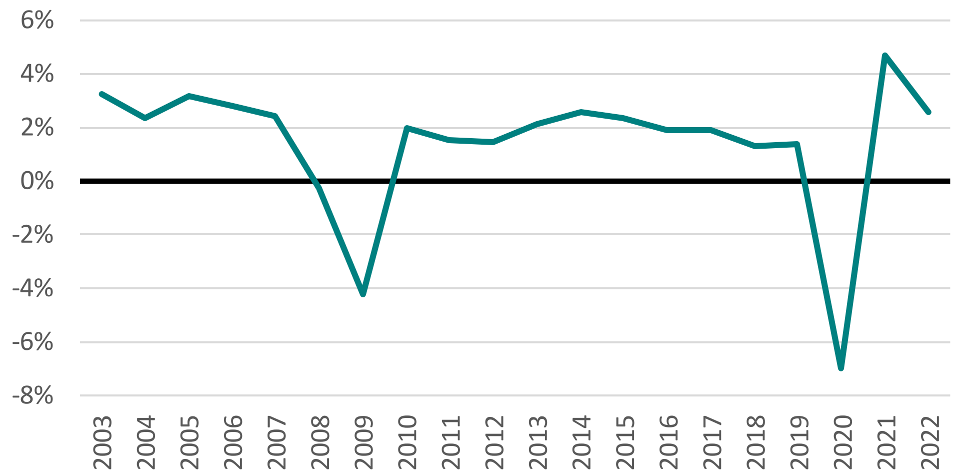
Forecast tables

Year-on-year change, unless otherwise indicated	2016	2017	2018	2019	2020	2021	2022
GDP	1.9%	1.9%	1.3%	1.4%	-7.0%	4.7%	2.6%
Consumer spending	3.8%	2.3%	1.6%	1.1%	-8.0%	1.2%	2.0%
Household disposable income	0.3%	1.3%	2.3%	1.3%	-3.4%	1.4%	1.3%
Business investment	4.3%	2.9%	-1.5%	0.6%	-15.5%	-2.8%	5.3%
Imports	4.4%	3.5%	2.0%	4.6%	-0.7%	-2.2%	2.9%
Exports	2.7%	6.1%	1.2%	4.8%	0.5%	8.8%	2.8%
Unemployment rate (%)	4.9%	4.4%	4.1%	3.8%	7.7%	7.0%	6.4%
Average gross employee earnings (incl bonuses)	2.4%	2.3%	3.0%	3.4%	-1.1%	1.8%	2.5%
CPI inflation	0.6%	2.7%	2.5%	1.8%	1.8%	2.7%	2.3%
Bank rate	0.40%	0.29%	0.60%	0.75%	0.28%	1.08%	2.06%
$/£	$1.35	$1.29	$1.34	$1.28	$1.27	$1.31	$1.34
€/£	€ 1.22	€ 1.14	€ 1.13	€ 1.14	€ 1.15	€ 1.17	€ 1.18
UK 10 year gilt yields, %	1.3%	1.2%	1.5%	0.9%	0.6%	0.7%	1.0%
Real output, manufacturing	0.2%	2.3%	0.9%	-1.7%	-12.9%	4.4%	1.5%
Real output, construction	3.9%	6.5%	0.0%	2.3%	-5.0%	3.0%	2.3%
Real output, financial & business services	2.7%	1.0%	1.8%	0.7%	-5.5%	5.2%	4.1%
Real output, wholesale & retail	4.2%	2.5%	3.2%	2.9%	1.5%	5.5%	2.0%

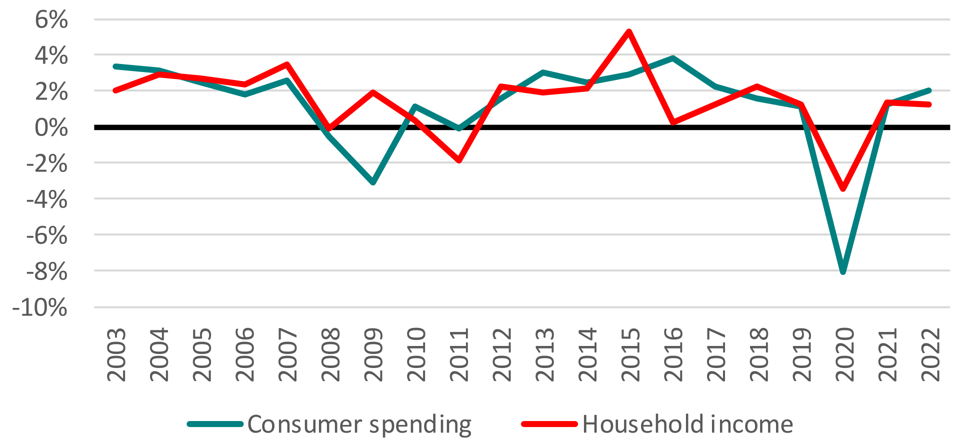
More UK forecasts can be found by accessing the Cebr databank: https://cebr.com/prospects-databank/

Key charts

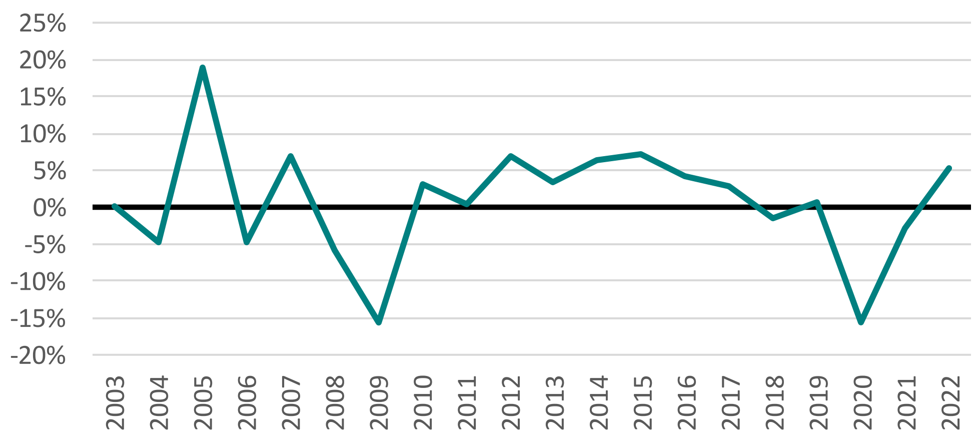
UK real GDP – annual % change



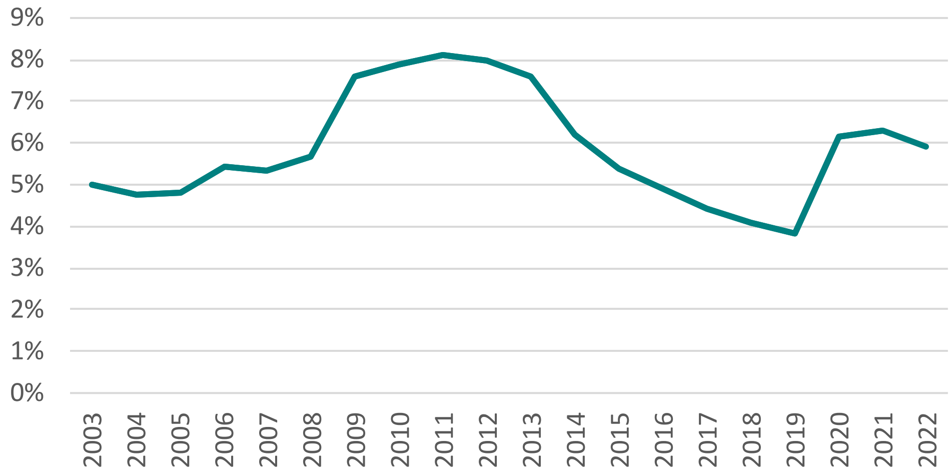
Total real consumer spending and household disposable income, annual % growth



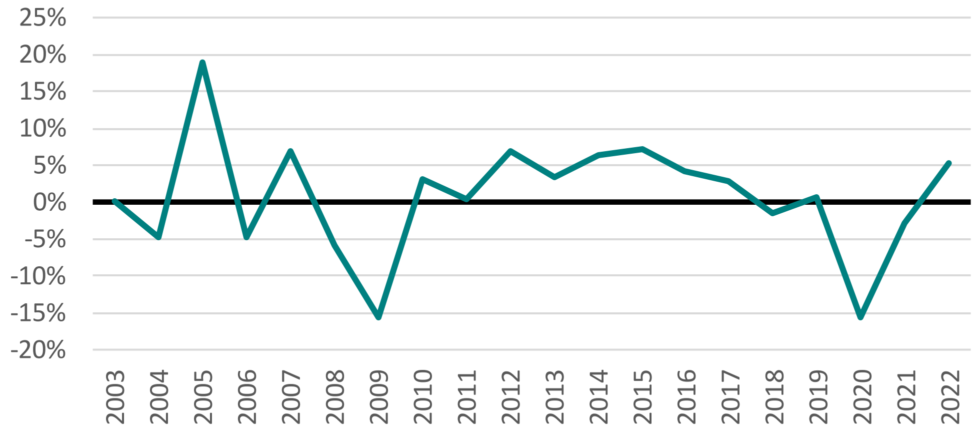
Real business investment, annual % change



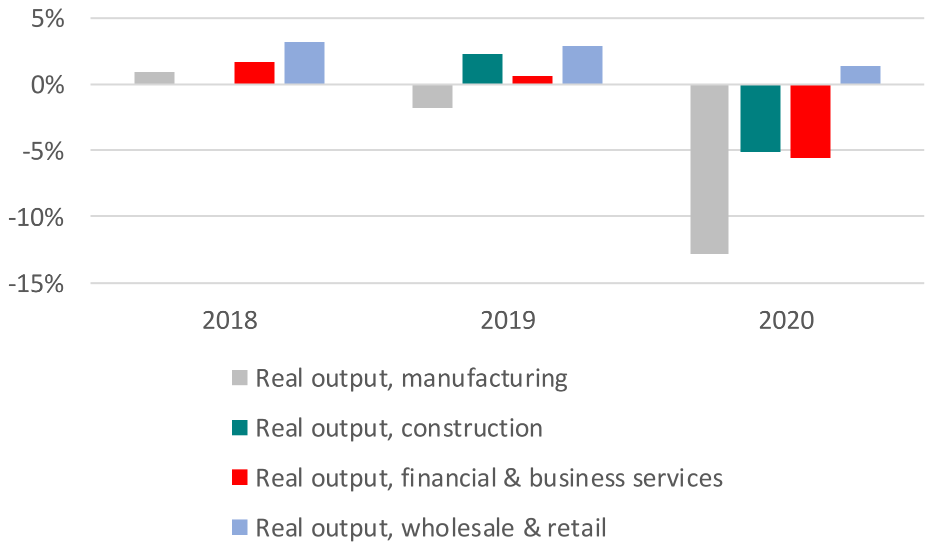
UK unemployment rate, %



Average gross employee earnings (incl bonuses), annual % change

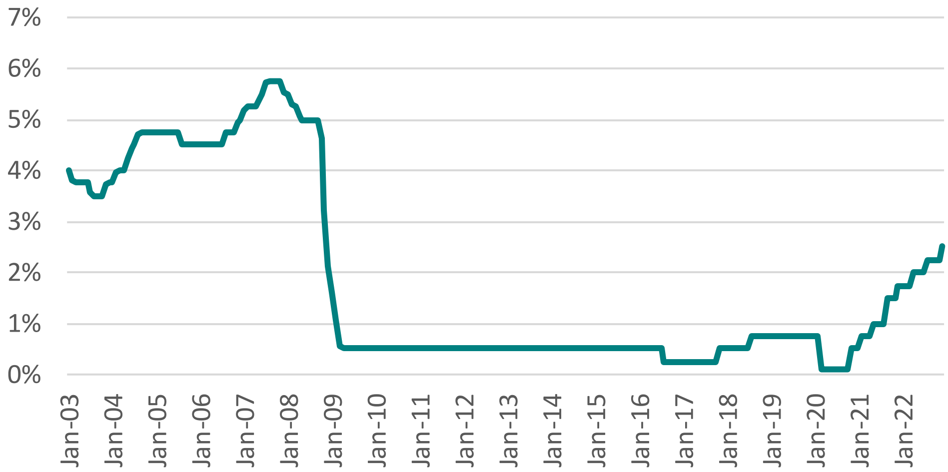


Real output, annual % change, by industry sector

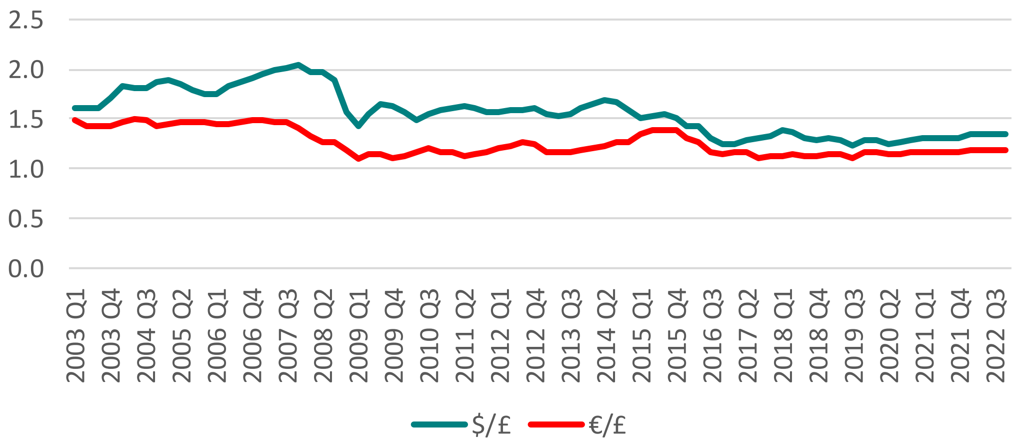


Consumer price inflation, annual % change

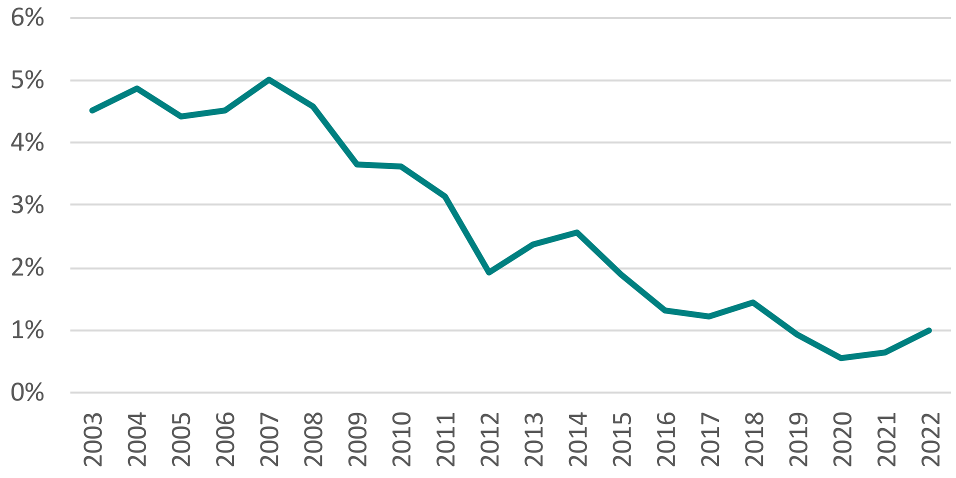
Bank of England base interest rate, %



Sterling exchange rate versus US dollar and euro



UK 10 year gilt yields, %



More UK forecasts can be found by accessing the Cebr databank: https://cebr.com/prospects-databank/

For more information, please contact…

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