Northern Ireland Quarterly Sectoral Forecasts

Forecast summary

The UK and Northern Ireland economies have displayed a degree of resilience so far this year and are both estimated to have expanded in the first quarter of 2023. Looking forward, the economic outlook remains challenging and uncertain given the persistence of inflationary pressures and the accompanying tightening in monetary policy. We are now forecasting that the Northern Ireland economy will grow by around 0.2% in 2023, an upward revision from our previous report. However, we have revised our projection for output growth in 2024 downwards and now expect the Northern Ireland economy to expand by about 0.6% next year as price pressures and the tighter policy environment weigh on growth.

The economy has proved resilient during 2023 but the outlook remains challenging

The UK and Northern Ireland economies have displayed a degree of resilience during the first half of 2023. The UK economy grew by 0.1% in the first quarter of the year, the same rate of growth as in 2022 Q4. In Northern Ireland, the economy is also likely to have expanded in quarter one with the Composite Economic Index posting a rise of 1.2%.

Looking forward, the economic outlook remains challenging and highly uncertain. Given the stronger than anticipated economic data and the expectation that some of the resilience displayed by households and businesses will persist, annual economic output is projected to expand modestly this year. However, inflation is proving stubborn and continuing to adversely impact household purchasing power. In response to these persistent price pressures, monetary policy has tightened and is likely to weigh down on spending, investment levels and consumer and business sentiment both over the rest of this year and into next year as monetary policy changes take time to fully impact the economy.

While continuing to note the high level of uncertainty around the economic outlook, we are now forecasting that the Northern Ireland economy will grow by around 0.2% in 2023, an upward revision from the 0.3% contraction in output we had projected in our last report. We expect the economy to grow again in 2024, by around 0.6%, but this is lower than the 0.9% expansion we expected previously.

The labour market remains in a strong position but some softening is expected

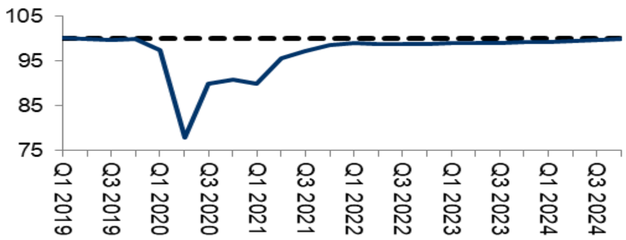
Northern Ireland's labour market has continued to perform strongly despite the challenging economic conditions. The Quarterly Employment Survey for the first quarter of 2023 showed a 0.6% rise in the number of employee jobs, the eighth consecutive quarterly increase and a new series high. However, the rate of jobs growth slowed for the second consecutive quarter, potentially signalling that the labour market is beginning to lose some momentum. The more timely HMRC Pay As You Earn data similarly points to a slight softening in hiring, with the number of payrolled employees falling over the month in April and then again in June. However, the unemployment rate in Northern Ireland remains low and stood at just 2.5% in the March – May 2023 period.

Although the labour market has remained robust, it tends to lag wider economic developments and so given the challenging economic backdrop, we expect the performance of the labour market to be softer over the rest of this year. However, given the strength in the rate of employee jobs growth in recent quarters, we have revised our forecast for 2023 upwards. We are now projecting that the annual average number of employee jobs in Northern Ireland will increase by around 1.6% this year but that the rate of jobs growth will slow to about 0.2% in 2024. We are also forecasting that the unemployment rate in Northern Ireland will rise to an annual average of around 2.8% this year and 3.2% in 2024.

Forecast summary (%)	2022	2023	2024
UK GDP growth	4.1	0.3	0.7
NI GVA growth	3.7	0.2	0.6
NI employee jobs growth	3.8	1.6	0.2
NI unemployment rate	2.7	2.8	3.2
UK unemployment rate	3.7	4.1	4.3
UK CPI inflation rate	9.1	7.4	2.8

Sources: ONS, NISRA, Oxford Economics, Danske Bank Analysis

NI Gross Value Added (Index 2019 Q4 = 100)



Sources: Oxford Economics, Danske Bank Analysis

Key factors in the outlook

Inflation expected to fall but take time to return to target

Inflation in the UK has fallen from its peak of 11.1% last October to 8.7% in May 2023, however the pace of decline has been relatively slow. There was an unexpected rise in the annual rate of inflation in February and the May figure was unchanged from April, when inflation was also 8.7%. In addition to the stickiness of the headline inflation figure, there are other signs of persistent price pressures across the economy. The annual inflation rate was above the headline 2% target rate for 11 of the 12 main consumer spending categories in May, with transport the only one where the rate of price growth was below the headline target. Food and non-alcoholic beverages was the spending category which experienced the highest annual inflation rate at 18.3%. Core inflation – which excludes energy, food, alcohol and tobacco prices and is considered one measure of underlying price pressures – increased in April and then again in May to 7.1%. We expect the headline rate of CPI inflation to continue to fall, as large base effects caused by last year's rise in energy prices affect the annual inflation calculation and the impact of falling wholesale energy prices feeds through to household bills. However, the decline in inflation back to its target rate is expected to take time and we are forecasting that the rate of inflation will average around 7.4% this year and about 2.8% in 2024.

Tighter monetary policy

The Bank of England's Monetary Policy Committee (MPC) increased Bank Rate by 0.5 percentage points to 5% at its June policy meeting, which was the thirteen consecutive rise in the base rate. As well as the increase in core inflation, the latest wage growth figures could also indicate that the headline inflation rate may continue to prove stubborn. The annual rate of growth for employees' regular pay in Great Britain was 7.3% in the March – May 2023 period. Strong rates of wage growth could support demand levels in the economy and as such, contribute to price pressures for goods and services persisting for longer. Given the rates of headline and core inflation being observed and the strong rate of wage growth, we expect the MPC to tighten monetary policy further and think that Bank Rate could rise to around 5.5% before the end of this year. However, with uncertainty around the outlook for inflation particularly elevated, the possibility of Bank Rate rising above this can't be ruled out. The tight monetary policy environment is likely to weigh on spending and investment levels, as well as consumer and business confidence. It's also important to note that Bank Rate rises take time to fully impact the economy and so the monetary policy environment is likely to weigh on activity levels throughout the rest of 2023 and during 2024.

Tighter fiscal policy

Following on from the end of the pandemic and energy-related fiscal support measures, and a range of tax increases which have recently been implemented, fiscal policy is currently planned to tighten over the coming years. When combined with tighter monetary policy, the economic policy environment is likely to weigh on aggregate demand levels and the pace of overall economic growth.

Household spending power likely to remain under pressure

The combination of elevated rates of inflation and higher interest rates are likely to result in household spending power remaining under pressure during the rest of 2023 and into 2024. In Northern Ireland and the wider UK, consumer spending accounts for a significant share of overall economic activity and with consumer spending likely to remain subdued, the pace of overall economic growth is expected to remain modest.

Resilient labour market continuing to provide some support to consumer spending

While high inflation is continuing to put household finances under strain, the robustness of the labour market may keep giving some support to aggregate spending levels. The unemployment rate in Northern Ireland has been at or below 3% since the first quarter of 2022, considerably below its long-term average, with the wider UK also experiencing low unemployment at present. While we expect unemployment to gradually edge upwards, its peak is still expected to be relatively low when considered against the challenging economic backdrop. While the strong labour market is unlikely to fully offset the squeeze on spending power, it should give aggregate household expenditure some support.

The outlook for the UK economy

After growing modestly and therefore avoiding a technical recession in the fourth quarter of 2022, the UK economy continued on its path of slow but positive growth in the first quarter of 2023 when GDP expanded by 0.1%. Within **private consumption**, real household expenditure was flat in 2023 Q1 as high inflation continued to weigh down on consumers' spending power. Total **investment** rose by 2.4% but **government consumption** declined by 1.8%. **Exports** and **imports** both declined in the first quarter of 2023, by 6.9% and 3.8 respectively.

The monthly GDP data showed that UK output levels expanded by 0.2% in April, following a fall of 0.3% in March. This was mainly driven by a rebound in the **services** sector, which recorded growth of 0.3% after a 0.5% contraction in the previous month. Meanwhile, the **production** and **construction** sectors both reported contractions in output of 0.3% and 0.6% respectively.

Regarding 2023 as a whole, we have revised our forecast for annual UK GDP growth upwards by 0.5 percentage points to 0.3% to reflect the resilience evident in the latest economic output data. However, the slower decline in inflation and tighter monetary policy have contributed to us revising our forecast for GDP growth in 2024 down to about 0.7%, from 1.0% in our last report.

We are forecasting that aggregate **private consumption** will fall by around 0.1% this year amid the ongoing squeeze on consumer spending power from higher prices, before growing by about 0.2% next year. The combination of higher interest rates and the uncertain economic outlook makes for a difficult backdrop for **investment**, which we expect to expand by a modest 0.1% in 2023 before declining by about 1.2% in 2024. **Government consumption** is projected to grow by around 0.1% this year then by about 1.6% next year.

The UK labour market remains in a relatively robust position. The number of employee jobs increased by 1.0% in the first quarter of the year. The employment rate increased over the quarter to 76.0% in the March – May 2023 period and the economic inactivity rate fell while the unemployment rate increased by 0.2 percentage points to 4.0%. Job vacancies have continued to trend downwards, falling to 1.03 million in the April to June period, potentially suggesting that demand for workers is softening.

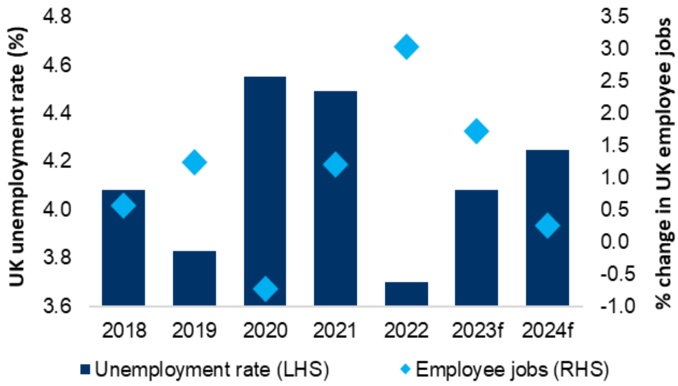
We have revised our forecast for the annual average rate of **employee jobs** growth in 2023 upwards to 1.7%, partly to reflect the resilience observed in the quarter one data. We then expect the pace of annual jobs growth to slow to about 0.3% next year. We are also projecting that the UK **unemployment rate** will increase moderately and average around 4.1% this year and 4.3% in 2024.

UK CPI **inflation** has proved persistent in recent months, having only fallen to 8.7% in April and then remained at that rate in May. Given the latest headline inflation data and the recent increases in the rate of core inflation, we have revised our forecast for the annual average CPI inflation rate in 2023 upwards to 7.4%, from 6.3% in our last report. Looking to 2024, we expect inflation to average about 2.8% over the year.

UK GDP forecasts (%)

	2022	2023	2024
UK GDP growth	4.1	0.3	0.7
Private Consumption	5.6	-0.1	0.2
Investment	8.6	0.1	-1.2
Government Consumption	1.8	0.1	1.6
Exports of Goods and Services	9.9	-2.5	2.5
Imports of Goods and Services	13.3	-5.0	3.5

Sources: ONS, Oxford Economics, Danske Bank Analysis



Sources: ONS, Oxford Economics, Danske Bank Analysis

Northern Ireland sectoral outlook

Projected 2023 output growth revised upwards, but the economic outlook remains challenging

The Northern Ireland economy is estimated to have expanded in the first quarter of 2023 and has displayed a degree of resilience so far this year. The Composite Economic Index posted a quarterly rise of 1.2% with services activity estimated to have grown by 2.2% but production output falling back by 0.4%. Given the resilience observed within both the output and the labour market data to date in 2023, we have revised our annual forecast for economic growth this year upwards and now expect the Northern Ireland economy to expand by about 0.2%. However, with high inflation persisting and monetary policy tightening we have revised our forecast for the annual rate of economic growth in 2024 down to 0.6%.

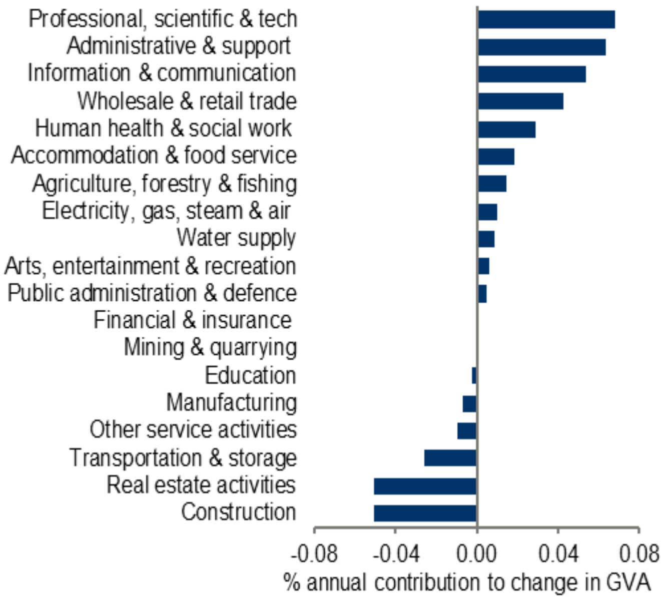
Despite the pressure being exerted on household spending power by high inflation, the consumer-focused sectors of the economy have displayed considerable resilience. The Northern Ireland Retail Sales Index increased by 3.3% in the first quarter of the year. The Quarterly Employment Survey for 2023 Q1 also showed that the number of employee jobs in the wholesale and retail trade, accommodation and food services and arts, entertainment and recreation sectors all increased in the first quarter of the year. As a result, we have revised our forecasts for the consumer-focused parts of the economy in 2023 upwards. We are now forecasting that output in the **wholesale and retail trade** sector will increase by around 0.3% in 2023. Activity in the **accommodation and food services** sector is projected to expand by about 0.6% this year, as is output in the **arts, entertainment and recreation** sector. In 2024, the sectors are expected to experience growth of around 0.8%, 0.7% and 0.7% respectively.

Annual output in the **manufacturing** sector is projected to be broadly flat in 2023. The Index of Production data for 2023 Q1 suggested that manufacturing activity increased by 0.4% at the start of this year but the weak outlook for investment is likely to weigh on the sector. We expect manufacturing activity to rise by about 0.5% in 2024.

Some sectors are still expected to experience a decline in output levels this year. The tighter monetary policy environment is expected to constrain activity in the **real estate activities** and **construction** sectors. The former is expected to experience a decline in output of around 0.4% this year. While the latter, which is also likely to be impacted by the expected weaker levels of investment activity, is projected to experience a decline in output of about 0.6%. Output in the transportation and storage sector is expected to decline by about 0.8% in 2023, in part reflecting the sharp drop in the number of employee jobs in the sector in 2023 Q1.

The outlook for the business services sectors is more optimistic. The **administrative & support services**, **professional, scientific & technical services** and **information & communication** sectors are expected to experience the strongest rates of growth this year, with output expanding by around 1.8%, 1.6% and 1.4% respectively.

Sector contributions to GVA growth in 2023



Sources: Oxford Economics, Danske Bank Analysis

GVA (%)	2023	2024
Administrative & support	1.8	1.1
Professional, scientific & tech	1.6	1.4
Information & communication	1.4	1.5
Agriculture, forestry & fishing	0.8	0.4
Electricity, gas, steam & air	0.6	0.4
Accommodation & food service	0.6	0.7
Water supply	0.6	0.4
Arts, entertainment & recreation	0.6	0.7
Wholesale & retail trade	0.3	0.8
Human health & social work	0.3	0.8
Public administration & defence	0.1	0.5
Financial & insurance	0.0	0.2
Manufacturing	0.0	0.5
Education	0.0	0.5
Mining & quarrying	-0.1	0.4
Real estate activities	-0.4	0.1
Construction	-0.6	0.6
Other service activities	-0.7	0.7
Transportation & storage	-0.8	0.6
Total	**0.2**	**0.6**

Sources: Oxford Economics, Danske Bank Analysis

Northern Ireland labour market outlook

Labour market continues to perform strongly with annual number of employee jobs expected to rise

The labour market in Northern Ireland has continued to perform relatively strongly despite the challenging economic backdrop. The latest Quarterly Employment Survey showed that the number of employee jobs increased by 0.6% in the first quarter of 2023, following growth of 0.7% and 0.9% in 2022 Q4 and 2022 Q3 respectively. Given this strong data, we now expect the annual average number of employee jobs to increase by around 1.6% in 2023. However, we expect the annual rate of jobs growth to slow to about 0.2% in 2024 as the challenging economic environment eventually leads to more modest rates of employment growth.

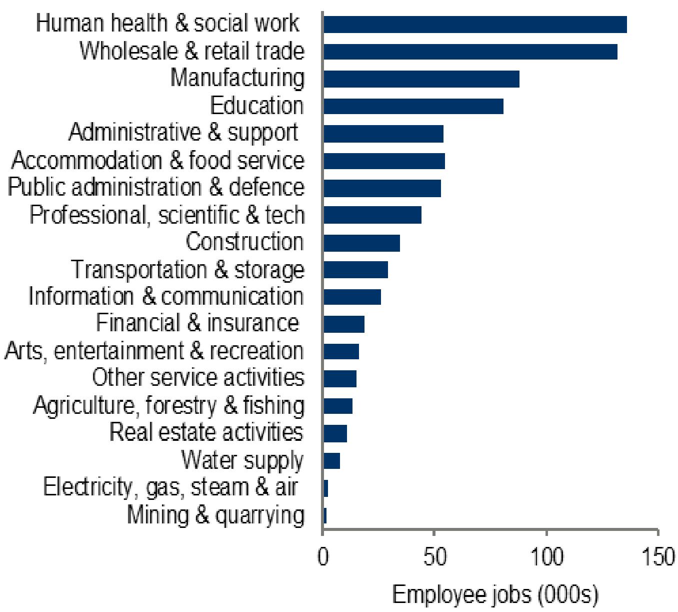
Employment in the consumer-focused parts of the economy has exhibited considerable resilience at the start of this year. The number of employee jobs in the first quarter of 2023 increased by 4.4% in the arts, entertainment & recreation sector, by 3.7% in the accommodation & food services sector and by 1.6% in the wholesale & retail trade sector. Given this strong quarter one data, we now expect the annual average number of employee jobs in 2023 to rise by 5.7% in the **arts, entertainment & recreation** sector, by 5.6% in the **accommodation & food services** sector and by 1.9% in the **wholesale & retail trade** sector.

Some sectors are expected to experience a decline in the average number of jobs in 2023, including **mining & quarrying**, **construction** and, to a lesser extent, **manufacturing**. All three industries experienced declines in employment in 2023 Q1 and their average employee jobs levels are projected to contract by about 4.0%, 3.8% and 1.0% respectively.

Despite a decline in the number of employee jobs over the quarter, the **professional, scientific & technical services** sector experienced a year-on-year increase in employment of over 14% in 2023 Q1. As such, the sector is expected to see the fastest rate of annual employee jobs growth in 2023 of around 6.4%. The **information & communication** sector is also expected to experience a strong rate of jobs growth in 2023, of about 5.2%.

Northern Ireland's unemployment rate in the March – May 2023 period was 2.5%, only slightly higher than the previous three-month period, and significantly below both its long-term average and the UK rate of 4.0%. We are forecasting that the unemployment rate in Northern Ireland will increase albeit to a relatively low level when considered against the challenging economic backdrop and average around 2.8% in 2023, before rising to an annual average of about 3.2% next year.

Employee jobs per sector in 2023



Sources: Oxford Economics, Danske Bank Analysis

Employee jobs (%)	2023	2024
Professional, scientific & tech	6.4	1.8
Electricity, gas, steam & air	5.8	-0.3
Arts, entertainment & recreation	5.7	0.5
Accommodation & food service	5.6	0.6
Information & communication	5.2	2.2
Real estate activities	3.9	-0.6
Public administration & defence	2.2	-1.7
Water supply	2.1	-0.9
Wholesale & retail trade	1.9	1.1
Administrative & support	1.7	1.7
Education	1.4	-0.8
Human health & social work	0.9	0.6
Agriculture, forestry & fishing	0.1	-0.8
Financial & insurance	-0.1	-1.3
Other service activities	-0.1	-0.1
Transportation & storage	-0.5	0.9
Manufacturing	-1.0	-1.3
Construction	-3.8	0.3
Mining & quarrying	-4.0	-1.3
Total	**1.6**	**0.2**

Sources: Oxford Economics, Danske Bank Analysis

Risks and uncertainties

While there is always uncertainty associated with economic forecasts, the extent of the risks and uncertainties around these projections is considered to be particularly elevated. The main sources of uncertainty include:

- **Persistent inflation** – Inflation in the UK remains stubbornly high – it came in at 8.7% in May, the same as April, and well in excess of the 2% inflation target. We now expect the rate of price rises to fall more slowly than in our previous forecast, averaging around 7.4% in 2023 and 2.8% in 2024. However, if inflation runs higher than forecast and falls even more slowly than anticipated, it has the potential to constrain economic activity even further. Factors which could see this come about include rising wages feeding into increased prices, businesses raising prices in response to higher costs or if commodity prices rise again. If inflation continues to run higher than expected, the Bank of England's Monetary Policy Committee may need to increase Bank Rate even higher than forecast to contain the rate of price rises and that could further dampen economic growth.

- **Prolonged political uncertainty** – Northern Ireland has not had a fully functioning Executive since early 2022, with issues around the implementation of the Northern Ireland Protocol the main factor preventing the re-establishment of the political institutions. The lack of an Executive has created uncertainty and challenges around policymaking in Northern Ireland and if this persists there is a risk that addressing key economic challenges will not progress as quickly as needed.

- **Skills shortages and recruitment challenges** – Across the economy, many businesses are still struggling to fill job openings with the skills that they require. In the *2023 Q1 Quarterly Economic Survey* published by the *Northern Ireland Chamber of Commerce and Industry* and *BDO* it was reported that 92% of the manufacturing firms and 82% of the services businesses that responded to the survey were facing difficulties when it came to hiring staff. While we expect unemployment to rise modestly, this competition for workers is one of the reasons that we think the extent of the increase may be lower than what might typically be assumed given the challenging economic backdrop. Skills shortages and recruitment challenges could weigh on economic output levels and taking steps to address this issue, alongside other labour market challenges such as low productivity and high levels of economic inactivity, should be policy priorities in Northern Ireland in an attempt to raise the economy's long-term growth potential.

In addition, a key global uncertainty relates to:

- **The war in Ukraine** – The economic consequences of the war in Ukraine on the UK and Northern Ireland economies have included higher commodity prices, in particular for oil and gas, and disruption to supplies of inputs from Russia and Ukraine. The war has also likely weighed on business and consumer confidence and the timing of an end to the war remains highly uncertain. However, if the war and the associated geopolitical tensions were to be particularly prolonged or to escalate further, in addition to the tragic human consequences that could ensue, the performance of the economy could also be negatively affected.

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The information in this document has been prepared in conjunction with Oxford Economics.

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