United Kingdom Outlook

Looking towards the post-furlough world

FOCUS

After the August GDP print, we lower our H2 21 forecast, and now see 2021 and 2022 growth at 7% (-0.3pp) and 4.2% (-0.1pp). Continued labour market recovery is welcome, but the post-furlough period is key, with initial survey data due next week. Earlier data suggest up to 600k still furloughed at the end of the scheme.

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August GDP soft; forecast revised down on accumulating headwinds

August GDP (0.4% m/m) printed slightly softer than the 0.5% expected by us and the consensus (read August GDP: summer lull, 13 October 2021). As expected, growth was driven by services, with hospitality and arts, entertainment and recreation key contributors to growth following the final set of reopenings on 19 July, while IP was boosted by the reopenings of oil fields previously closed for temporary maintenance. With the ONS significantly revising up past quarters in the final Q2 GDP release, GDP in August was within 1% of pre-COVID-19 levels (0.8% short of February 2020), but momentum has slowed over the summer months (Figure 2).

We downgrade our forecast from H1 21, as Q3 carry-over has barely reached 1.3pp meaning that September would have to print above 1% m/m to realise our previous quarterly forecast of 1.75% q/q. Lower momentum going into Q4 21, together with many headwinds (supply chains, labour shortages, end of policy support, energy prices, monetary and financial tightening), is eventually set to drag confidence (business and household) lower. We now forecast 7.0% (-0.3pp) growth in 2021 and 4.2% (-0.1pp) in 2022. These forecast are fairly close to the IMF's new forecast released yesterday (6.8%/5.0% for 2021/2022) but somewhat below consensus forecasts for next year (6.8/5.4% in 2021/22, see Figure 1). The IMF's estimate of economic scarring (the difference between pre-COVID-19 and post-COVID-19 GDP forecasts for the medium term) is somewhat larger than ours (3% vs 2%) and is the largest among their forecasts for G7 economies. It has become a relatively consensual view that the UK economy will suffer more permanent damage coming out of the COVID-19 crisis than peers. We believe Brexit and fiscal policy are key drivers behind the UK's expected relative underperformance.

FIGURE 1. Barclays vs IMF vs consensus forecasts

	2021	2022	2023
		GDP % y/y	
Barclays	**7.0**	**4.2**	**1.3**
Consensus	6.8	5.4	2.0
IMF	6.8	5.0	1.9
		CPI %y/y	
Barclays	**2.3**	**3.1**	**1.9**
Consensus	2.3	3.0	2.3
IMF	2.2	2.6	2.0

Consensus forecasts from Consensus Economics (as of 8 October 2021). IMF forecasts taken from October 2021 World Economic Outlook.
Source: IMF, Consensus Economics, Barclays Research

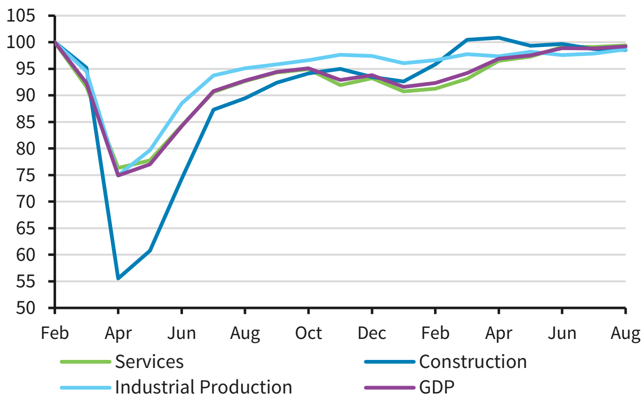
Labour market recovery continues, but still little clarity on post-furlough period yet

LFS data for the three months to August showed many of the features seen in recent prints, namely a continued gradual recovery in labour market conditions (read UK labour market chart book: continued improvement, 12 October 2021). Unemployment and inactivity continue to fall (albeit the latter's fall has been slowing), while total employment continued to increase but was still significantly lower than pre-COVID-19 levels (in the three months to August, employment, inactivity and unemployment were -657k, +622k and +146k relative to pre-COVID-19, respectively). In September, the number of people on HMRC PAYE payrolls (an alternative measure of employees) exceeded February 2020 levels for the first time in the pandemic, but given the possibility that a number of previously self-employed people may have re-classified themselves as employees through the pandemic, it is difficult to draw strong conclusions at this stage.

Critically, none of these data are for the post-furlough period. Timelier labour market data this week came from the preliminary BICS estimate of the proportion of people furloughed from 20 September to 3 October. It suggests that the fall in furlough numbers accelerated in the last couple of weeks of the scheme, albeit with c.500-600k people still on furlough by the end (Figure 3). This preliminary BICS estimate, based on a smaller sample of respondents, will be followed by the 'final' wave 41 edition of the BICS next Thursday (21st), but assuming few revisions, this means that in November, the MPC will be faced with the prospect that possibly up to 2% of the workforce was still furloughed when the scheme ended. The only October labour market data before the next MPC will be labour market indexes in the PMIs and consumer confidence prints (both released next week), as well as experimental fast data on online job vacancies for most of October, none of which will allow the MPC to take strong views (read The heat is on as sentiment cools, 1 October 2021).

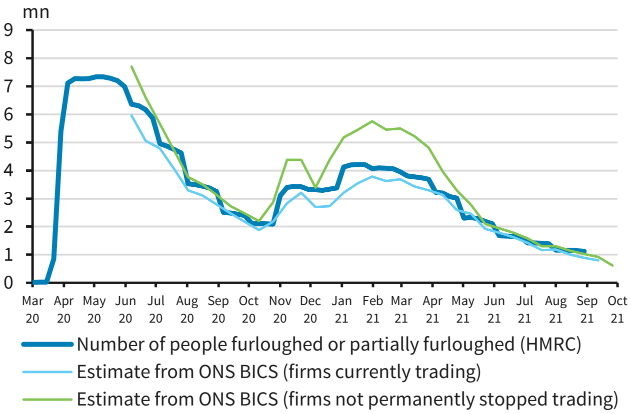
Furthermore, the paucity of data by the November meeting may have implications for the Bank's ability to hike in December, as historically it would want to avoid catching markets wrong footed. We think that a more plausible, alternative scenario is that the MPC uses the 16 December meeting to discuss a a February hike. The MPC will have early access to inflation and labour market data on Friday 10 December (publicly released only on 14 and 15 December respectively) and they will have new population projections by the ONS (to be released on 6 December), in addition to the usual batch of monthly data.

FIGURE 2. **GDP momentum slowed over the summer**



Source: ONS, Haver Analytics, Barclays Research

FIGURE 3. **Furlough fell faster towards the end of September, but up to c.600k were still on support**



Latest data point from ONS BICS (for the second half of September) is from the initial results of the Wave 41 edition of the survey, based on a smaller sample of respondents. The final print will be released on 21 October.
Source: ONS, HMRC, Haver Analytics, Barclays Research

Next week data heavy: September inflation and retail sales, October surveys

Next week, we forecast September CPI at 3.1% y/y (0.3% m/m), but see upside risks to this forecast stemming from continued supply chain disruptions. We will continue to watch whether high-inflation rates remain limited to a small number of sectors or whether strong price pressures have become more broad based. September will be the last month before the Ofgem price cap is increased in October by 12%, which will contribute 0.4pp to CPI; hence, headline inflation is set to jump following next week's print (we currently forecast October at 3.7% y/y).

We expect October consumer confidence to show a sharp deterioration (we forecast a print of -20) given the barrage of headwinds and negative headlines facing households (energy, food and fuel shortages, fiscal and monetary tightening, and the end of existing support schemes such as furlough and the universal credit uplift). This is likely to be driven by a fall in the future general economic situation index, albeit this index is particularly volatile - hence, a particularly sharp drop in sentiment in October may overstate the deterioration in underlying sentiment. We will be paying close attention to the unemployment expectations index given that this will be the first post-furlough print. If unchanged on the month in October, the index would be consistent with only a small rise in unemployment to around 4.6/4.7%.

We expect October PMIs to moderate, with services forecast at 54.5 (-0.9 points) and manufacturing at 55 (-2.1 points). While services are likely to have benefited from further normalisation in behaviours, particularly return to office, we expect this to be more than offset by lower household and business confidence stemming from many of the aforementioned headwinds. We expect manufacturing to fall by more than services, with output continuing to be limited by supply chain disruptions, particularly in logistics, as well as wavering demand, which PMIs suggest had already started in September. Again, the employment indexes will be of particular interest given that it will reflect the first month post-furlough.

Despite having sharply overshot pre-COVID-19 levels following the reopenings in spring, the decline over the summer as consumers rotated spending into services meant that retail sales in August declined to levels consistent with the pre-COVID-19 trend. This suggests that downside risks to next week's September retail sales are lower than in previous prints. Furthermore, heightened fuel consumption in the last week of September is likely to make a positive contribution (albeit it will likely be unwound later). However, sales may suffer from lower confidence among households as headwinds accumulated.