Office for National Statistics

Article

Quarterly economic commentary: January to March 2020

Economic commentary for the latest quarterly national accounts, prices and labour market indicators.

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1 . Main points

- UK gross domestic product (GDP) fell by 2.2% in Quarter 1 (Jan to Mar) 2020, the joint-third largest quarterly contraction on record, which reflects the imposing of public health restrictions and voluntary social distancing in response to the coronavirus (COVID-19) pandemic.

- There has been a marked uptick in the households saving ratio to 8.6% in Quarter 1 and an increase in the net lending by households in Quarter 1 2020, reflecting a fall in final consumption expenditures; there was a record increase in currency and deposits that were placed in financial corporations, in line with investors looking to acquire highly liquid assets.

- There have been pronounced cross-border financial flows in Quarter 1 2020 that were the largest quarterly flows since the global financial crisis, primarily in the more mobile forms of capital such as loans and deposits; this reflects the increase in demand for short-term highly liquid assets.

- Total actual hours worked in the three months to April 2020 fell by 8.9% when compared with the same period a year ago, while the number of vacancies is now 44% lower than the record high recorded in the three months to January 2019.

- The annual Consumer Prices Index including owner occupiers' housing costs (CPIH) has fallen to 0.7% in May 2020, the lowest it has been in four years, with lower petrol and diesel prices and further downward contributions from recreation and culture and restaurants and hotels.

2 . Gross domestic product

UK gross domestic product (GDP) is estimated to have fallen by 2.2% in Quarter 1 (Jan to Mar) 2020, revised from a preliminary estimate of a decline of 2.0%. This is the joint-third largest quarterly contraction in GDP. [1] This reflects the imposing of public health restrictions and voluntary social distancing in response to the coronavirus (COVID-19) pandemic. The decline in the first quarter largely reflects the large fall in output in March 2020, with widespread monthly declines in output across the services, production and construction industries.

More timely estimates[2] show that the UK economy fell by an unprecedented 20.4% in April, following a 5.9% contraction in March (Figure 1). This provides the clearest picture of the economic impacts so far, which were in effect from late March. These April figures showed the widespread collapse in economic activity, all of which were monthly records. There was a 19.0% contraction in services output, a decline of 20.3% in production output and a 40.1% fall in construction activity. Over the initial two-month period in which the effects of the coronavirus pandemic had been felt, the UK economy has contracted by around a quarter. [3] The industries most impacted by the response to the coronavirus pandemic have been retail, construction, manufacturing, accommodation and food services, and education, in line with where there were the largest falls in hours worked. More timely information imply that April is likely to be the low point for economic activity, including the official retail sales figures, which show a partial rebound in retail sales in May, though these remain well below their pre-pandemic levels.

Figure 1: The UK economy has contracted by 25% in a two-month period

January 1997 to April 2020

Source: Office for National Statistics – GDP monthly estimate, UK: April 2020

The more timely Business Impact of Coronavirus (COVID-19) Survey (BICS) shows that many businesses reopened in May and June. The latest BICS findings show that 86% of businesses were trading between 1 and 14 June 2020, the majority of which had been trading for more than that two-week period. That said, 64% of those businesses trading reported that their turnover was below normal expectations for this time of year. Of the 14% of businesses that had temporarily closed or paused trading, 3% intended to restart trading in the next two weeks.

Following the record declines in April, the latest Flash UK Composite Purchasing Manager's Index (PMI) suggests that there are some signs of a slower rate of contraction in June. It reports that "the easing of restrictions related to the coronavirus disease 2019 (COVID-19) pandemic had a favourable impact on economic activity" as well as reporting a pickup in expectations and confidence. That said, there was still evidence that underlying demand remained very subdued.

International

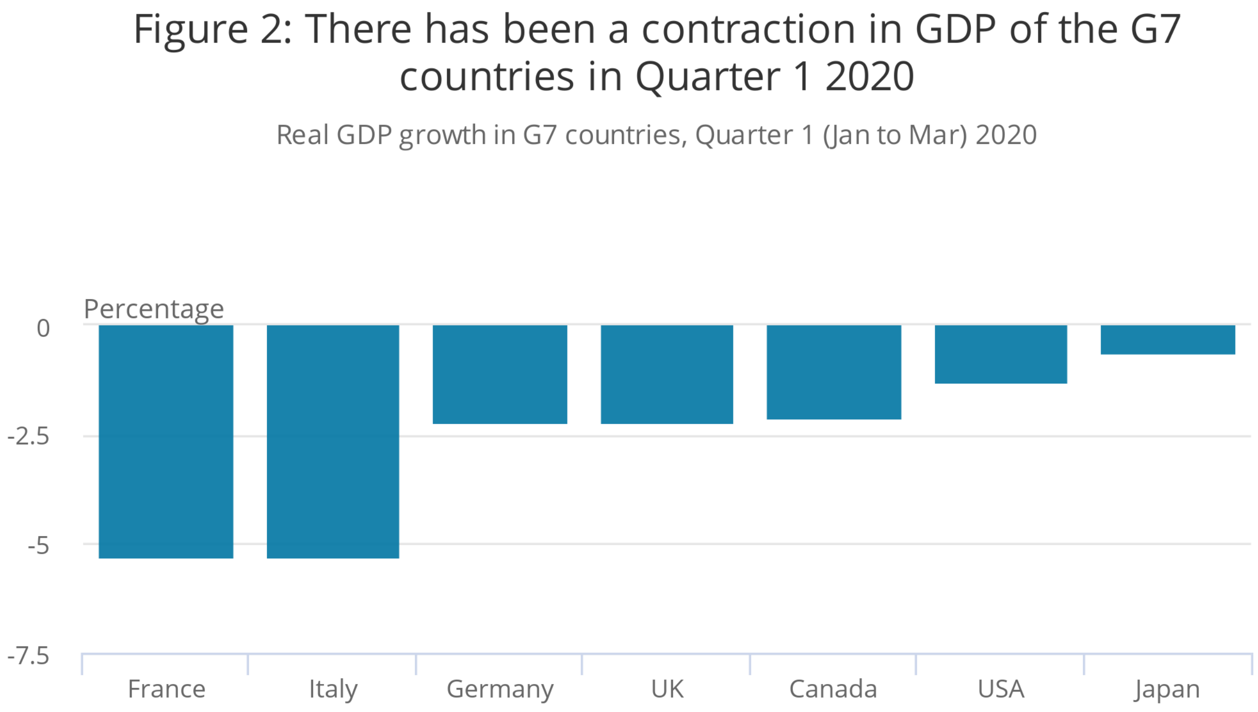
The coronavirus pandemic is having unprecedented impacts on the global economy. Restrictions to help contain the spread of the virus have been imposed on a worldwide basis, albeit some countries have implemented those policies at different times, leading to reduced economic activity in advanced and developing economies. Recent findings show that the stringency of these containment policies appears to be correlated with the size of the contraction experienced across countries.

Figure 2 shows how all G7 economies have experienced a contraction in Quarter 1 2020, while the economy of the EU contracted by 3.2% in Quarter 1. The expectations are for a larger global decline in Quarter 2 (Apr to June) 2020, as this is where the full impact of the shutdowns that have been imposed will be felt. This is corroborated in the more timely figures, which show a monthly fall in industrial production of 17.3% in which all member states experienced a contraction in output.

The outlook for the global economy is highly uncertain. It will depend on how restrictive the shutdowns are and how long these are in effect for, the pace at which these containment measures are lifted, the extent to which voluntary social distancing continues, and the possibility of a second wave of infections. Modelling of "single-hit" and "double-hit" scenarios by the Organisation for Economic Co-operation and Development (OECD) provides some indication of the impact on the world economy this year, in which global GDP is projected to contract by between 6.0% and 7.6%. The latest forecasts by the International Monetary Fund (IMF) are for the global economy to contract by 4.9% this year, underpinned by projections of weaker private consumption that reflect "a large adverse aggregate demand shock from social distancing and lockdowns, as well as a rise in precautionary savings".

Figure 2: There has been a contraction in GDP of the G7 countries in Quarter 1 2020

Real GDP growth in G7 countries, Quarter 1 (Jan to Mar) 2020



Source: Organisation for Economic Co-operation and Development and Office for National Statistics

Notes:

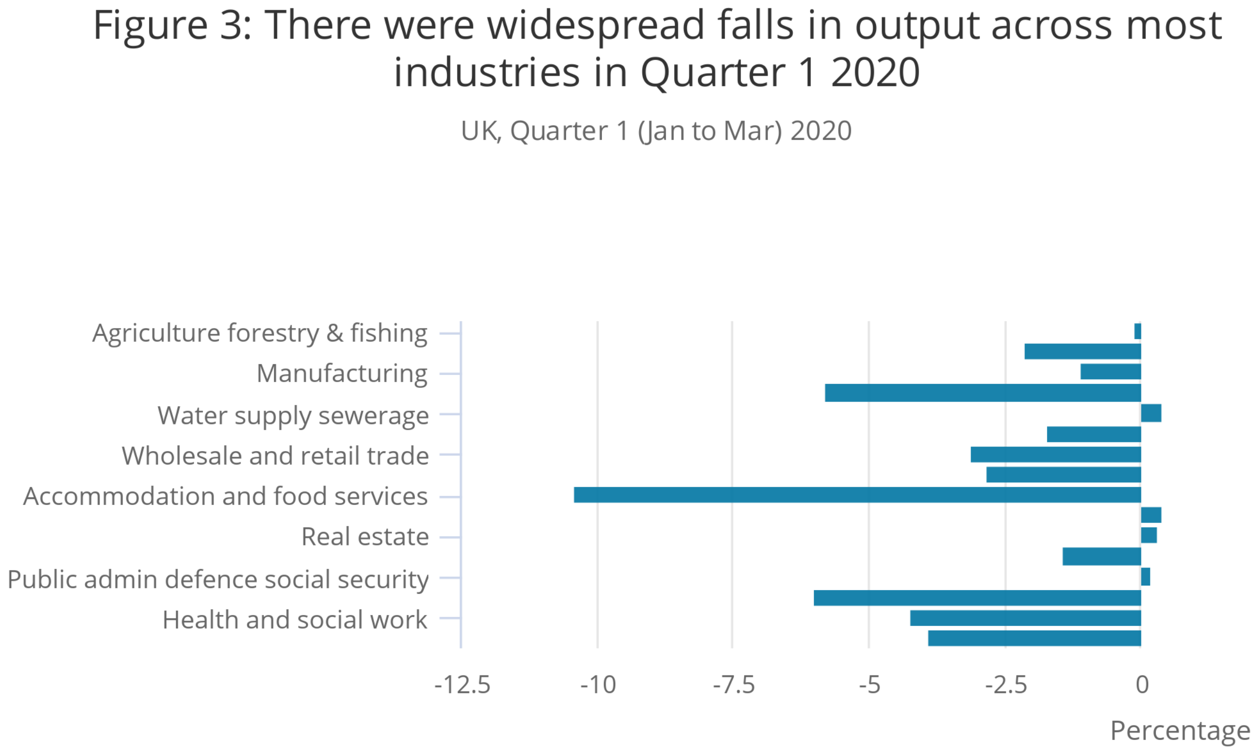
1. All Organisation for Economic Co-operation and Development (OECD) figures correct as at 23 June 2020.

Output

Public health restrictions and forms of social distancing have been imposed in response to the coronavirus pandemic, leading to lower levels of production and demand. The extent to which industries will be adversely impacted will reflect their exposure to these restrictions and their ability to respond. Those industries that require direct contact between consumers and service providers and/or those instances where there are enforced closures of those non-essential businesses will be most impacted, as will those where remote working is not feasible. Figure 3 shows the quarterly change in the production of each industry.

Figure 3: There were widespread falls in output across most industries in Quarter 1 2020

UK, Quarter 1 (Jan to Mar) 2020



Source: Office for National Statistics – GDP quarterly national accounts, UK: January to March 2020

Notes:

1. “Other Services” comprises of sections R, S and T of the Standard Industrial Classification (SIC) 2007.

Services output contracted by 2.3% in Quarter 1 2020, the largest quarterly fall on record, which were most notable in education; wholesale and retail trade and repair of motor vehicles and motorcycles; food and beverages; accommodation; and travel agencies. The Quarter 1 Bank of England Agents' summary of business conditions reported "a sharp decline in spending on consumer services and non-food goods", adding that the travel, leisure and hospitality sectors were the most affected.

The coronavirus pandemic has also affected the provision of services provided by government, specifically health and education. Health and social work output contracted by 4.2%, reflecting the postponement or cancellation of healthcare treatments as the NHS prepared to increase its critical care capacity in response to the pandemic. Education output fell by 6.0% in Quarter 1 2020, driven by the partial closure of schools from 23 March onwards as part of the response to the coronavirus pandemic.

There are some industries in the manufacturing industry that are integrated into global value chains. Given the closures of factory plants and the restrictions on international transportation, there is further potential for the production of those manufactured goods to be disrupted. Furthermore, in response to the heightened levels of uncertainty, there has also been a decline in demand for non-essential manufactured goods.

Manufacturing output fell by 1.1% in Quarter 1 2020, driven by declines in the manufacture of transport equipment, machinery and equipment, and textiles. This was partially offset by increases in the manufacture of pharmaceutical, chemical, and wood and rubber and plastic products in response to stronger-than-usual demand for medicinal products and for soaps and cleaning products in response to the coronavirus pandemic. The latest Confederation of British Industry (CBI) Industrial Trends Survey found that the volume of manufacturing output fell at the fastest rate on record in the three months to June, while total order books remained low by historical standards. The latest Agents' summary of business conditions showed that output continues to be weak and that social distancing and weak demand is expected to constrain manufacturing output over the next few months. That said, there has been a slight improvement as more manufacturing firms reopen.

Construction output fell by 1.7% in Quarter 1 2020. The March UK Construction PMI found that construction output declined at the steepest rate since April 2009 because of "stoppages of work on site and a slump in new orders". While the latest Agents' summary of business conditions reported that some sites were reopening, it also highlighted that the construction activity was still constrained by "social distancing measures as well as shortages of materials". There are also some concerns around the outlook, primarily reflecting how changes to working habits might impact the demand for commercial space.

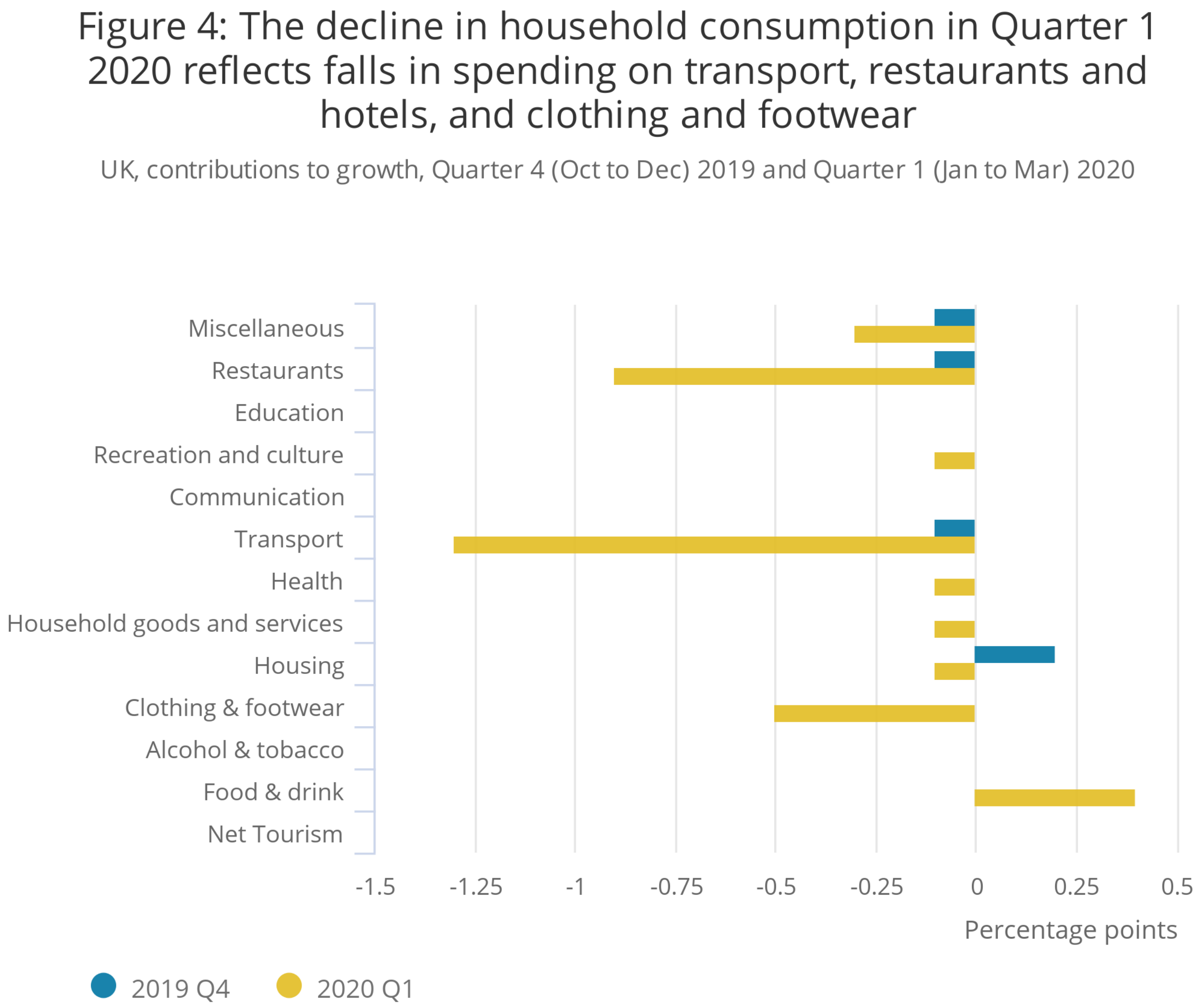
Expenditure

The Bank of England has highlighted how social distancing is likely to lead to some forms of consumption ceasing, particularly those that involve social interaction, including "eating out at restaurants and attending sports events, as well as spending relating to holidays such as hotels and air travel". There may also be an increase in precautionary savings resulting from heightened economic uncertainty and fear of job loss. Figures published by GfK show that there was a large decline in consumer confidence in late March and while the latest estimate points to an uptick of late, these remain low by historical levels. The Office for National Statistics (ONS) Opinions and Lifestyle Survey (OPN) found that 20% of employees and half of self-employed people reported reduced financial income in the period 3 April to 10 May 2020, in part because of reduced working hours.

Household consumption fell by a revised 2.9% in Quarter 1 2020, which is the largest fall since late 1979. The decline reflects falls in spending on transport, restaurants and hotels and clothing and footwear (Figure 4), in line with those expectations of where social distancing will likely have the most impact. The enforced closures of non-essential businesses and wider restrictions has had pronounced effects on the retail industry. Following a record monthly fall in April, there was a partial rebound in May as the volume of retail sales increased by 12.0% but was still down by 13.1% compared with February levels. This was in line with the reopening of household goods stores and the effect of some easing in travel restrictions on increased spending on fuel. The Bank of England has cited payments information that points to a recovery in the spending of "delayable goods", which include DIY goods, car sales, clothing and household goods. It also found that there has been an increase in work-related spending, including on motor fuels.

Figure 4: The decline in household consumption in Quarter 1 2020 reflects falls in spending on transport, restaurants and hotels, and clothing and footwear

UK, contributions to growth, Quarter 4 (Oct to Dec) 2019 and Quarter 1 (Jan to Mar) 2020



Source: Office for National Statistics – GDP quarterly national accounts, UK: January to March 2020

Notes:

1. Q1 refers to Quarter 1 (Jan to Mar) and Q4 refers to Quarter 4 (Oct to Dec). 2. Contributions represent contributions to overall household consumption growth. Contributions may not sum exactly because of rounding.

Government healthcare consumption fell by a revised 6.2%. There was increased activity in some areas, such as calls to NHS 111, but reduced activity in other areas (for example, elective operations and accident and emergency). Education fell by a revised 6.4% in Quarter 1 2020, reflecting school closures across the UK, except for vulnerable pupils or those whose parents are key workers. We include the education consumed by pupils who are learning at home using materials provided by teachers.

There is evidence that the lower level of sales and higher levels of uncertainty has led to the cancellation and postponement of investment projects. There was a fall in gross fixed capital formation (GFCF) of 1.1% in Quarter 1 2020, reflecting declines in government, dwellings and business investment. The latest BICS findings show that 43% of businesses continuing to trade said that capital expenditure had stopped or was lower than normal because of the coronavirus pandemic. The latest Decision Maker Panel survey found that firms in all industries are expecting to reduce their investment over the next year, particularly in consumer-facing services in line with those businesses experiencing "the largest and most persistent impact on sales".

The underlying figures show a substantial decrease in stocks being held by UK companies in Quarter 1 2020, led by a fall in the level of stocks held within the wholesale and retail trades. Respondent-led evidence points to the decline in the wholesale industry being largely because of firms facing increased difficulty obtaining stock from within the UK and abroad, while the falls in the retail industry were predominantly because of increased consumer spending on household goods and food and drink.

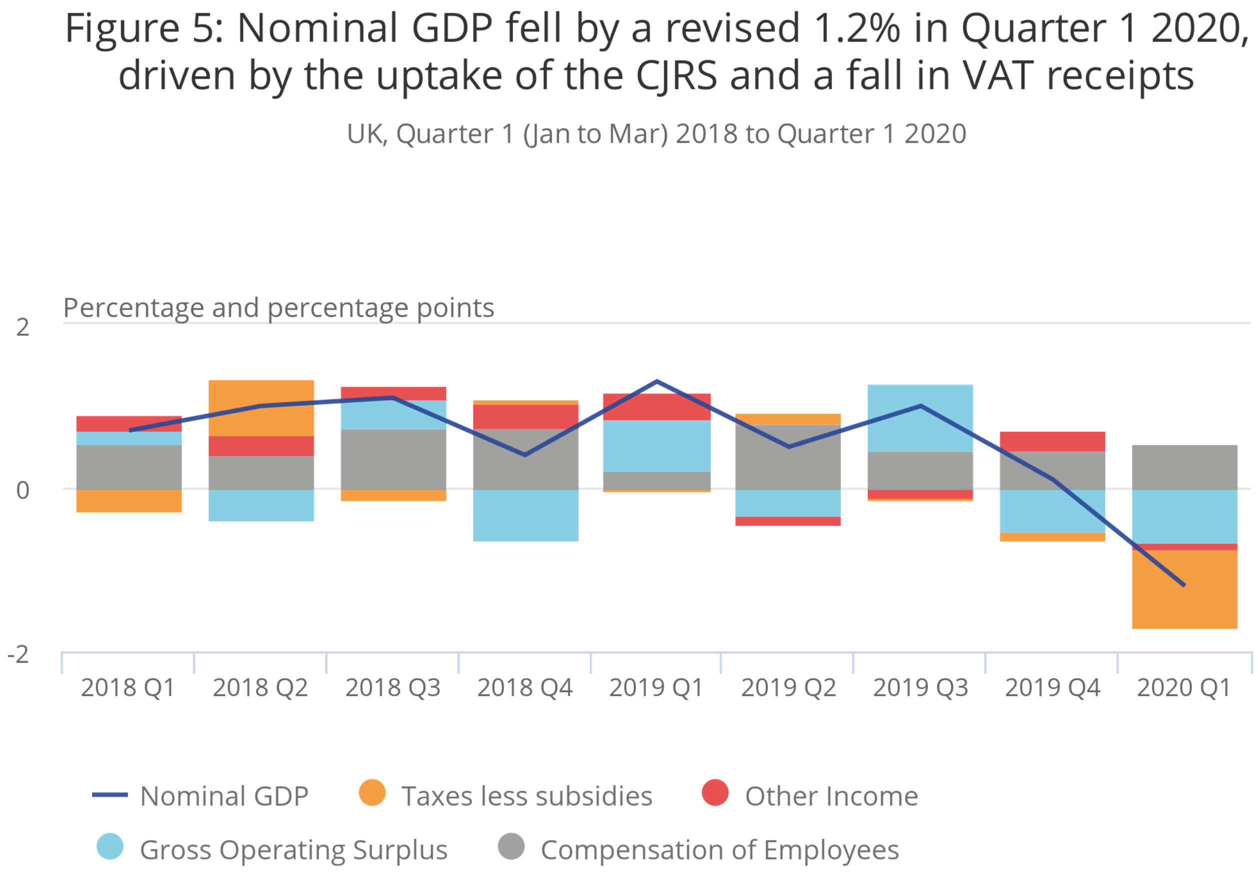
There were large falls in the volumes of exports and imports in Quarter 1 2020, reflecting declines in the international trade of goods and services. The coronavirus pandemic has led to a marked fall in domestic and global demand, while the disruptions to international supply chains might have impacted on the trade intensity of demand. The restrictions on many forms of travel and transportations is expected to impact on trade flows. According to the CPB World Trade Monitor, world trade volumes were 1.4% lower in March 2020 than in the previous month. The decline was particularly notable in Europe, though trade in China "rebounded in March, following a sharp decline in January and a consolidation in February".

Income

Nominal GDP fell by 1.2% in Quarter 1 2020, which is the largest quarterly fall in nominal GDP since Quarter 1 2009. Taxes less subsidies fell by 8.6%, reflecting updates to the Office for Budget Responsibility (OBR) coronavirus reference scenario and updated information on the extent to which Value Added Tax (VAT) receipts were impacted in Quarter 1 2020 (Figure 5). The latest HM Revenue and Customs (HMRC) weekly outturn figures point to a lower average grant per job than previously estimated because of an apparent concentration of furloughing among part-time and lower-paid jobs, so the OBR has revised down its estimate of the gross cost of the Coronavirus Job Retention Scheme (CJRS).[4]

Figure 5: Nominal GDP fell by a revised 1.2% in Quarter 1 2020, driven by the uptake of the CJRS and a fall in VAT receipts

UK, Quarter 1 (Jan to Mar) 2018 to Quarter 1 2020



Source: There was a sharp reduction in net borrowing by corporations in Quarter 4 (Oct to Dec) 2019, while the UK's reliance on external financing was at its lowest since 2011.

Notes:

1. Q1 refers to Quarter 1 (Jan to Mar), Q2 refers to Quarter 2 (Apr to June), Q3 refers to Quarter 3 (July to Sept) and Q4 refers to Quarter 4 (Oct to Dec).
2. Chart shows contribution to nominal gross domestic product (GDP) quarter-on-quarter growth.
3. Components contributions may not sum to total because of rounding.

Excluding the alignment adjustment, private non-financial corporations' (PNFC's) gross operating surplus (GOS) fell by 3.6% in Quarter 1 2020. According to the latest EY UK profit warnings, UK companies issued 301 profit warnings in Quarter 1 2020; this is a 238% increase from Quarter 1 2019 and more than double the previous high in Quarter 4 (Oct to Dec) 2001. The report highlighted that 77% of profit warnings cited the coronavirus, with travel and leisure being the most affected industry. Financial corporations' GOS increased by 7.8%, driven by an increase in net spread earnings, reflecting the extreme volatility in markets and elevated trading volumes in Quarter 1 2020.

Notes for Gross domestic product

1. There were larger quarterly contractions in Quarter 1 1974 (2.7%) and Quarter 2 (Apr to June) 1958 (2.4%). The UK economy also fell by 2.2% in Quarter 3 (July to Sept) 1979.

2. The latest official estimates of monthly GDP do not reflect the revisions that have been incorporated as part of the latest quarterly national accounts, released 30 June 2020. Fully consistent figures will be released on 14 July 2020. An indicative monthly path for Quarter 1 2020 has been made available.

3. For context, the monthly figures show that the peak-to-trough fall in GDP was 6.9% and took place over a 13-month period in the global financial crisis.

4. Further information on the recording of the CJRS is available in Coronavirus and the effects on UK GDP.

3 . Institutional Sector Accounts

The coronavirus (COVID-19) pandemic has also had an impact on the non-financial and financial transactions of households[1], corporations, the government and the rest of the world[2]. Non-financial transactions are those that relate to production, income, consumption and capital investment, which will be impacted by how the private and public sector responds. Financial transactions are those that capture the change of ownership in financial claims, which will likely be responsive to the uncertainty and volatility experienced in financial markets at the height of the coronavirus pandemic.

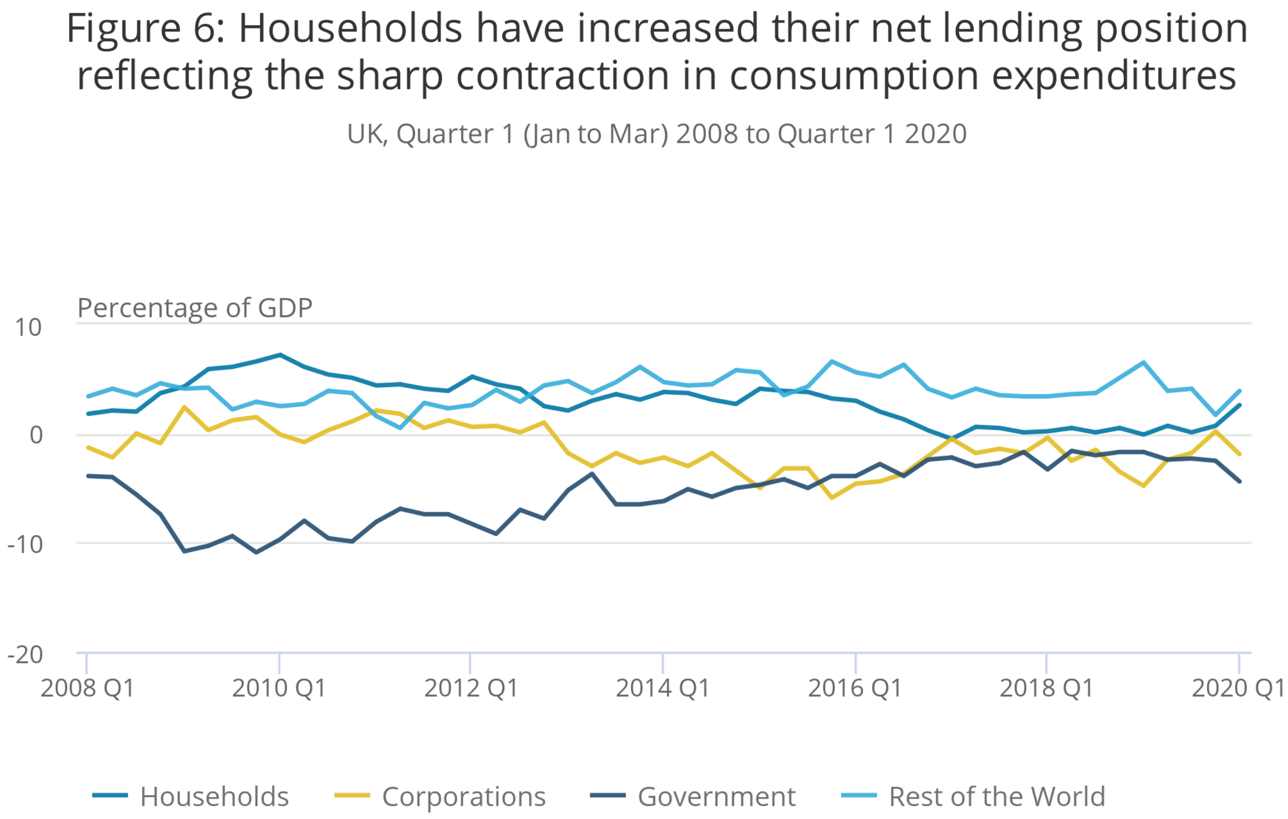
The paths of sectoral income and expenditure determine whether households, corporations, the government and the rest of the world are net lenders or borrowers. A net borrowing position must be funded by taking on further financial liabilities and/or reducing financial assets, while a net lending position is reflected in a net increase in financial assets and/or decrease in financial liabilities. As total borrowing must be matched by total lending, these financial positions must sum to zero across the institutional sectors in any period.

Figure 6 shows that there have been sizeable movements in the sectoral net lending or borrowing positions in Quarter 1 (Jan to Mar) 2020. There was a sharp increase in the net lending position of households to 2.6% in Quarter 1 2020, a contrast to the underlying trend of the previous four years, reflecting the sharp contraction in consumption expenditures. Figure 6 also shows that there has been an underlying improvement in the government net borrowing position over the previous 10 years. However, in Quarter 1 2020, there was an increase in net borrowing from 2.5% to 4.4%, primarily reflecting the cost of the fiscal policy response and the fall in tax receipts.

Non-financial corporations further increased their net borrowing requirements in Quarter 1 2020 (2.4%), reflecting a fall in gross operating surplus (GOS), while financial corporations reduced their net lending (0.5%). This included a record increase in currency and deposits, which might reflect the response of financial markets to the heightened uncertainty.

Figure 6: Households have increased their net lending position reflecting the sharp contraction in consumption expenditures

UK, Quarter 1 (Jan to Mar) 2008 to Quarter 1 2020



Source: Office for National Statistics – Quarterly sector accounts, UK: January to March 2020

Notes:

1. Q1 refers to Quarter 1 (Jan to Mar), Q2 refers to Quarter 2 (Apr to June), Q3 refers to Quarter 3 (July to Sept) and Q4 refers to Quarter 4 (Oct to Dec).

2. Net lending or borrowing positions may not sum to zero in later years because of unbalanced supply and use tables in the compilation of gross domestic product (GDP).

There was a marked increase in net lending by households in Quarter 1 2020. This primarily reflected a fall in final consumption expenditures. The imposition of public health restrictions on the UK economy helps explain the contraction in non-essential spending and/or those transactions that require direct contact between consumers and businesses. This has been evident in the large falls in expenditure on motor vehicles, restaurants and hotels, and clothing and footwear, likely reflecting the response of such examples of social consumption to the forms of social distancing that were in place towards the end of Quarter 1 2020.

There has been a marked uptick in the households saving ratio to 8.6% [3] in Quarter 1 2020, some of which might reflect a response to the increased levels of uncertainty. The Bank of England also highlighted that there might be a rise in precautionary savings in response to "actual or possible unemployment" or that the "constraints on spending during the lockdown" might lead to a rise in household savings. The Resolution Foundation showed that there was a large monthly increase in March in broad money holding, which includes "balances in bank accounts and other liquid assets, as well as cash itself", though it is not clear whether this reflected enforced or precautionary saving. The corresponding financial flows can be volatile, but households primarily financed the higher levels of net lending by reducing their loan liabilities and increasing the amount of currency and deposits placed with financial institutions.

General government was a net borrower in Quarter 1 2020 of 4.4% of gross domestic product (GDP). Early estimates of the public sector finances[4] show the fiscal impact of the coronavirus pandemic so far. Public sector net borrowing (PSNB) was £55.2 billion in May - the largest deficit recorded for any month and in line with the figure for all the 2019 to 2020 financial year in total. PSNB was £103.7 billion in total for the first two months of the current financial year, up by £87.0 billion on the same period in the last year.

This mainly reflects the cost of fiscal interventions so far - including the Coronavirus Job Retention Scheme (CJRS)[5] - and lower tax revenues, in particular lower Value Added Tax (VAT) receipts from the effects of a contraction in the economy. There was a sharp rise in public sector net debt (PSND) in May, reflecting the need for the extra funding required to support the government's coronavirus relief schemes combined with the fall in GDP[6]. PSND now stands at 100.9% of GDP, which is the first time that it has exceeded the size of the economy since the financial year ending March 1963.

Non-financial corporations increased their net borrowing in Quarter 1 2020. The coronavirus pandemic has led to lower levels of production and demand, reflecting how this is likely to have led to lower levels of demand and supply in the UK economy. This is likely to have been particularly pronounced in those industries where there have been enforced closures of non-essential businesses. The reduction in sales in response to these enforced restrictions has led to a fall in GOS, which explains the increase in the net borrowing requirements of non-financial corporations.

The latest Business Impact of Coronavirus (COVID-19) Survey (BICS) found that 64% of businesses trading between 1 and 14 June 2020 reported that their turnover was below normal expectations for this time of year. The Decision Maker Panel survey found that 42% of businesses expected their sales to be lower in Quarter 2 (Apr to June) 2020 in response to the coronavirus pandemic than it would have been otherwise. This has primarily been financed by a large increase in the issuance of loans. The latest Agents' summary of business conditions highlighted that there is still a continued high demand for credit to address "cash flow issues or finance working capital".

Financial corporations reduced their net lending in Quarter 1 2020, reflecting a large increase in gross capital formation. That said, this was because of an increase in their net acquisition of non-monetary gold. These cross-border flows have been particularly volatile in recent quarters, so these might not provide a useful indication of the underlying position of financial corporations. Financial flows are typically volatile, which was the case in Quarter 1 2020. The latest Bank of England Financial Stability Report explains how "a 'flight to safety' in financial markets became an abrupt and extreme 'dash for cash'" in which investors looked to acquire highly liquid assets. There was a record increase in currency and deposits that were placed in financial corporations.

Notes for Institutional Sector Accounts

1. For the purposes here, households include non-profit institutions serving households (NPISH) unless otherwise stated.
2. Further information is available in Coronavirus and the effects on the UK Institutional Sector Accounts .
3. This figure refers to households only. If NPISH are included, the saving ratio is 8.4%.
4. The PSNB and PSND cited here exclude public sector banks.
5. Further information on the recording of the CJRS is available in Coronavirus and the effects on UK GDP .
6. The monthly GDP estimates in estimating this ratio are highly provisional, being partly based on official estimates.

4 . Balance of payments

The coronavirus (COVID-19) pandemic is global and will have significant impacts on the UK and global economy. Most countries have imposed some form of restrictions to contain the spread of COVID-19, which has led to sudden contractions in gross domestic product (GDP). The latest estimates by the Organisation for Economic Co-operation and Development (OECD) point to a contraction of the global economy of around 3% in Quarter 1 (Jan to Mar) 2020 with a larger decline expected in Quarter 2 (Apr to June) 2020. It also highlights that there has been a contraction in world trade in Quarter 1 2020, while there was a sharp increase in financial market uncertainty around the start of the coronavirus pandemic. These effects are all expected to impact on the UK's international transactions with the rest of the world, including the gross and net transactions.

The UK has historically run a current account deficit, relying on overseas investors as a net lender to the UK. [1] This had raised concerns around whether this reliance on external financing was sustainable, particularly in response to the heightened economic uncertainty around the coronavirus pandemic, if there is a fall in the confidence of foreign investors and/or there is a shift in the global risk environment.

Figure 7 shows that the current account deficit was 3.8% in Quarter 1 2020. Recent quarterly movements have been volatile, particularly in the trade flows. This has largely reflected recent movements in non-monetary gold, which do not necessarily provide a true indication of the underlying external position. However, there have been some notable gross movements in the international trade of finished manufactured goods. The most recent Manufacturing Purchasing Manager's Index (PMI) showed how the rates of contraction in new export business were one of the fastest on record, while the latest Confederation of British Industry (CBI) Industrial Trends Survey found that export order books fell to a record low level. This is likely to reflect the fall in domestic and global demand and the disruptions to global value chains. There has also been a reduction in cross-border travel services and the imposition of physical restrictions that will impact on international travel. Higher-frequency indicators provide some further insight around the extent to which international travel has fallen over this period.

There has also been a steady decline in the UK's net investment income of late, in particularly on foreign direct investment (FDI). It is too early to comment on the impact of the coronavirus pandemic on these international income flows, though it is possible that some of the movements in Quarter 1 2020 reflect the lower interest rates that are now in place in many countries. There is also anecdotal evidence that the restrictions have had an impact on corporation profits, which businesses may be responding to through retaining a higher level of earnings and/or paying fewer dividend payments.

Figure 7: The current account deficit was 3.8% in Quarter 1, including lower levels of gross trade flows in the finished manufactured goods and travel services

UK, Quarter 1 (Jan to Mar) 2008 to Quarter 1 2020

Source: Office for National Statistics – Balance of payments, UK: January to March 2020

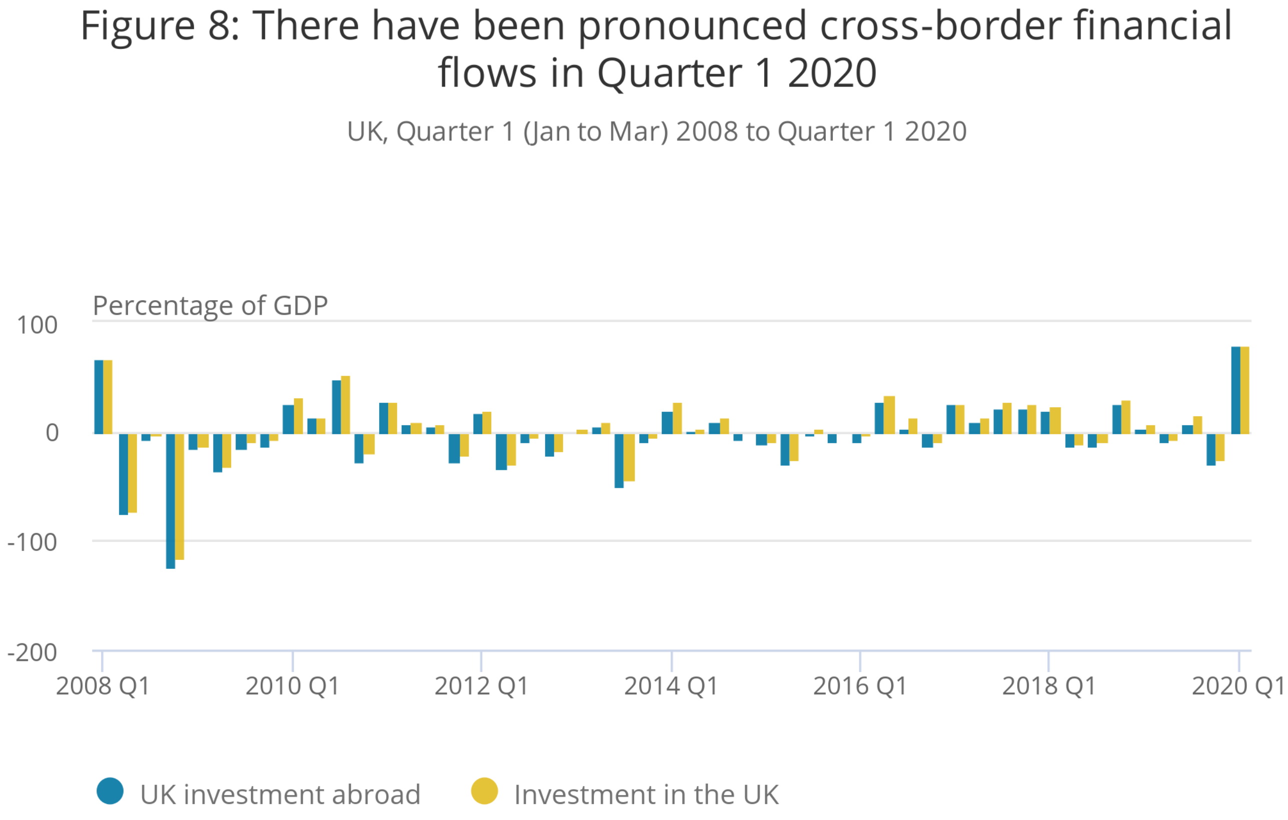
Notes:

1. Q1 refers to Quarter 1 (Jan to Mar), Q2 refers to Quarter 2 (Apr to June), Q3 refers to Quarter 3 (July to Sept) and Q4 refers to Quarter 4 (Oct to Dec).

A current account deficit must be financed by net financial inflows. This can be achieved by increasing external liabilities to the rest of the world and/or disinvesting in previously owned external assets. A reliance on net foreign capital inflows can leave a country vulnerable to a reduction in international investor appetite for those assets. These cross-border capital flows are prone to large swings, particularly for the more mobile forms of capital such as loans and deposits. This has been particularly marked in Quarter 1 2020 and reflected the largest quarterly flows since the global financial crisis (Figure 8).

Figure 8: There have been pronounced cross-border financial flows in Quarter 1 2020

UK, Quarter 1 (Jan to Mar) 2008 to Quarter 1 2020



Source: Office for National Statistics – Balance of payments, UK: January

Notes:

1. Q1 refers to Quarter 1 (Jan to Mar), Q2 refers to Quarter 2 (Apr to June), Q3 refers to Quarter 3 (July to Sept) and Q4 refers to Quarter 4 (Oct to Dec).

It is likely that these financial flows have reflected the response of financial markets around the start of the coronavirus pandemic, leading to a shift in the risk appetite of investors. The latest Financial Stability Report highlighted how the uncertainty around the scope and duration of the containment policies in place helps explain the increase in demand for short-term highly liquid assets, which was "underpinned by precautionary demand for liquidity in the real economy and financial markets". The most recent gross capital flows have been in other investment, as the UK increased its gross external assets and gross external liabilities in loans and deposits.

Notes for Balance of payments

1. There have been production challenges in producing a fully reconciled balance of payments at this time, as shown by the statistical discrepancy that brings together the current account, capital account and financial accounts. More information is available in Coronavirus and the effects on the UK Balance of Payments .

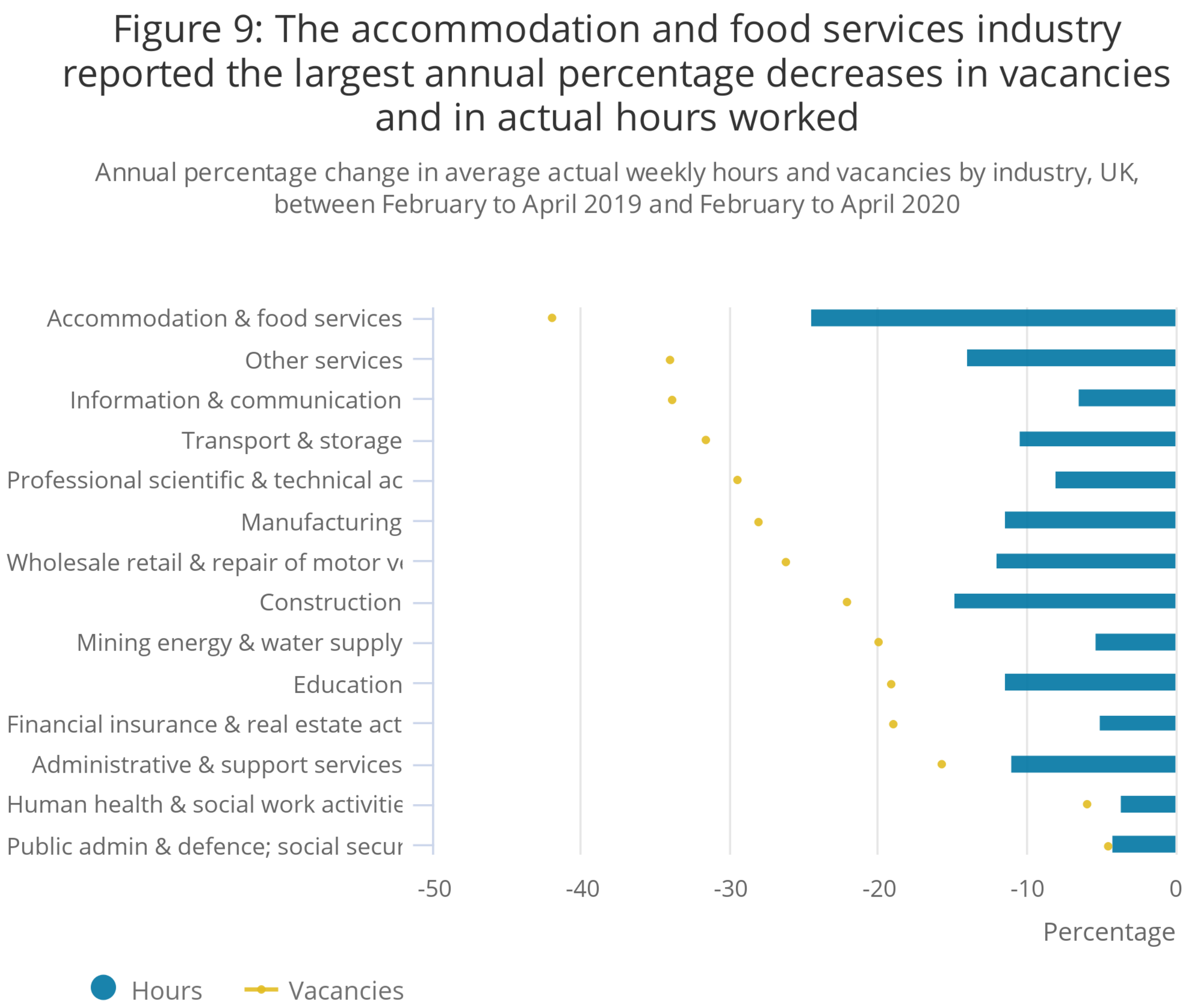
5 . Labour market

The impact of the coronavirus (COVID-19) pandemic is now showing up in the labour market. Given those individuals who have been furloughed through the Coronavirus Job Retention Scheme (CJRS) [1] and the Self-Employment Income Support Scheme (SEISS) are classified as in employment, the sharp contraction in the number of hours worked and vacancies provides a more insightful indication of the extent to which the labour market has been impacted.

Total actual hours worked in the three months to April 2020 fell by 8.9% when compared with the same period a year ago, the largest contraction on record. On the quarter, they fell by 8.7% in the three months to April 2020, the largest quarterly decrease recorded. All industries recorded a fall in hours in this period, with the most marked in accommodation and food services, construction, and other services, which includes the arts, entertainment and recreation industry (Figure 9). These are examples of the industries that might be expected to be most affected by the imposition of voluntary and involuntary restrictions. The impact on the UK labour market of the pandemic is also showing through changes in labour demand. Figure 9 also shows the comparable vacancies figures, highlighting the negative impact on hiring intentions.

Figure 9: The accommodation and food services industry reported the largest annual percentage decreases in vacancies and in actual hours worked

Annual percentage change in average actual weekly hours and vacancies by industry, UK, between February to April 2019 and February to April 2020



Source: Office for National Statistics – Labour Force Survey and Vacancy Survey

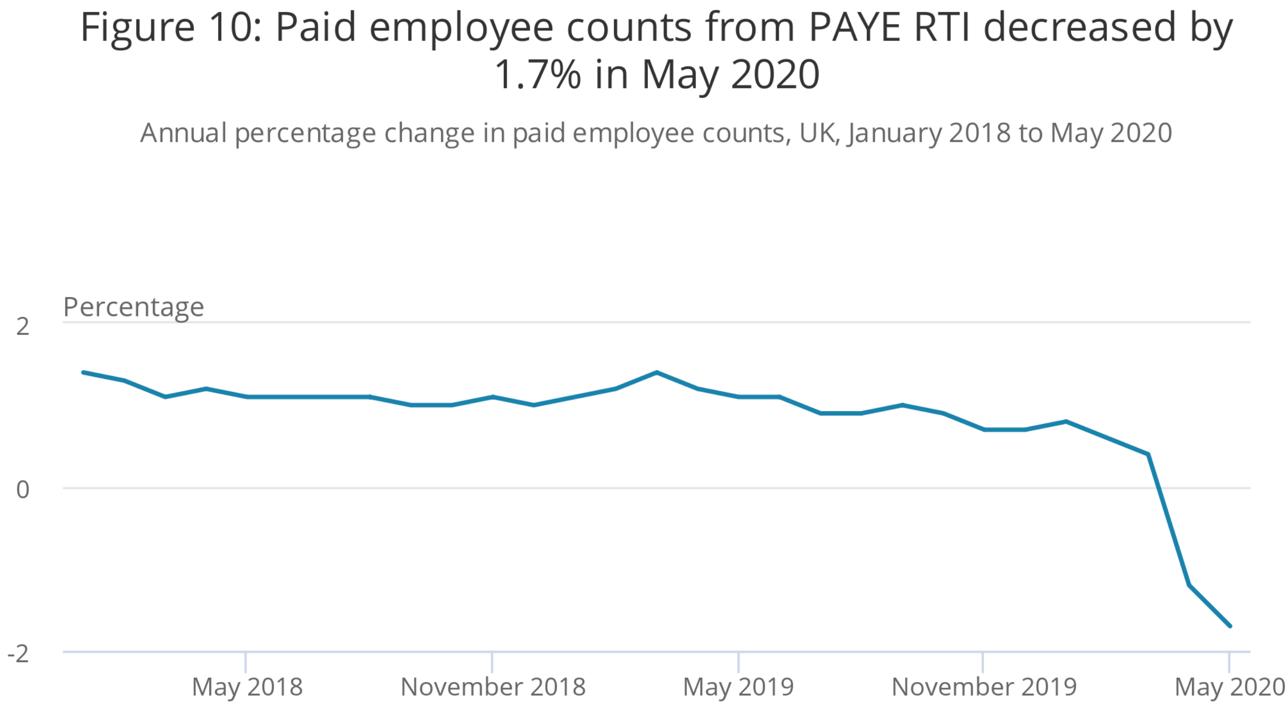
In its latest Report on Jobs, the Recruitment and Employment Confederation (REC) found a marked fall in demand for permanent and temporary workers in May 2020, citing how the coronavirus pandemic had led clients "to cancel or postpone recruitment plans until the outlook improved". The latest figures show that vacancies fell by 365,000 on the year and by 342,000 in the three months to May 2020 - the largest quarterly decrease on record. The number of vacancies is now 44% lower than the record high recorded in the three months to January 2019. The industries that saw the largest percentage decreases in vacancies in the three months to May were accommodation and food services (negative 71%), arts, entertainment and recreation (negative 57%) and construction (negative 54%). The experimental single-month estimates show that the number of vacancies fell by approximately 60% between March and May and are now at the lowest level on record.

The latest experimental Adzuna vacancies figures show that the volume of online job adverts is 53% lower than their 2019 average. That said, it is slightly up from where it was in early May, and there are some industries where the latest figures show a slight increase in the number of online vacancies, such as in wholesale and retail, that likely reflects the lifting of some of the restrictions on non-essential shops. The REC Jobs Recovery Tracker shows that the number of active job postings in the UK has risen slowly in the four-week period to early June, which might be a sign of "more companies starting to hire again since the lockdown measures have been eased, and that the recovery is starting to pick up speed".

The most recent figure for the three months to April 2020 shows that employment remains high, although the number of full-time self-employed workers fell by 142,000 on the quarter. That said, more timely Pay As You Earn (PAYE) figures indicate that the flash estimate for the number of payroll employees fell by 163,000 between April and May 2020. This follows a reduction of 449,000 between March and April 2020. Figure 10 shows the percentage change in the number of paid employees compared with the same month a year ago, implying that there is some weakness in the labour market.

Figure 10: Paid employee counts from PAYE RTI decreased by 1.7% in May 2020

Annual percentage change in paid employee counts, UK, January 2018 to May 2020



Source: HM Revenue and Customs - Pay as You Earn Real Time Information

Since January 2018, the annual growth in paid jobs has been slowing, which fell in the year to April. Claimant Count figures also support this, as the number of people who are claiming either Jobseeker's Allowance or Universal Credit for the purpose of searching for work increased to 2.8 million in May, a rise of 1.6 million (or 154%) compared with the same month a year ago.

The annual growth of nominal total pay slowed to 1.0% in the year to April 2020, which in part reflects the impact of lower pay for some furloughed employees. This slowing was most marked in industries where furloughing was most prominent, such as the accommodation and food service activities industry. The latest Agents' summary of business conditions reported a share fall in pay pressures, citing that "companies have deferred pay deals, cut pay or reduced working hours," as well as reporting declines in bonus and commission payments.

Notes for Labour market

1. The latest HM Revenue and Customs (HMRC) figures show that 8.7 million jobs have been furloughed on the CJRS as at the end of May 2020, with the higher levels in the wholesale and retail industry and accommodation and food services industry. A further 2.4 million of the potentially eligible population had claimed a SEISS payment by the end of May. The Labour Force Survey (LFS) figures show an increase in the number of people who were temporarily away from work had increased by over 6 million by the end of April, largely reflecting employees furloughed under the CJRS.

6 . Prices

The coronavirus (COVID-19) pandemic has had wide-ranging demand and supply effects on the UK economy, which will have implications for consumer price inflation. Business surveys tend to point to most firms expecting to cut their selling price. However, recent analysis has explained that headline consumer price inflation estimates will likely be a "noisy indicator" of how much inflationary pressure there is in the UK economy because of the temporary changes in relative prices and consumption expenditure shares. Furthermore, the Bank of England has also explained that the impact of spare capacity on inflation may be less than might be expected. This reflects that the higher levels of spare capacity have not been fully reflected in lower costs that are incurred by businesses and that incentive to lower prices is less in periods of weak demand.

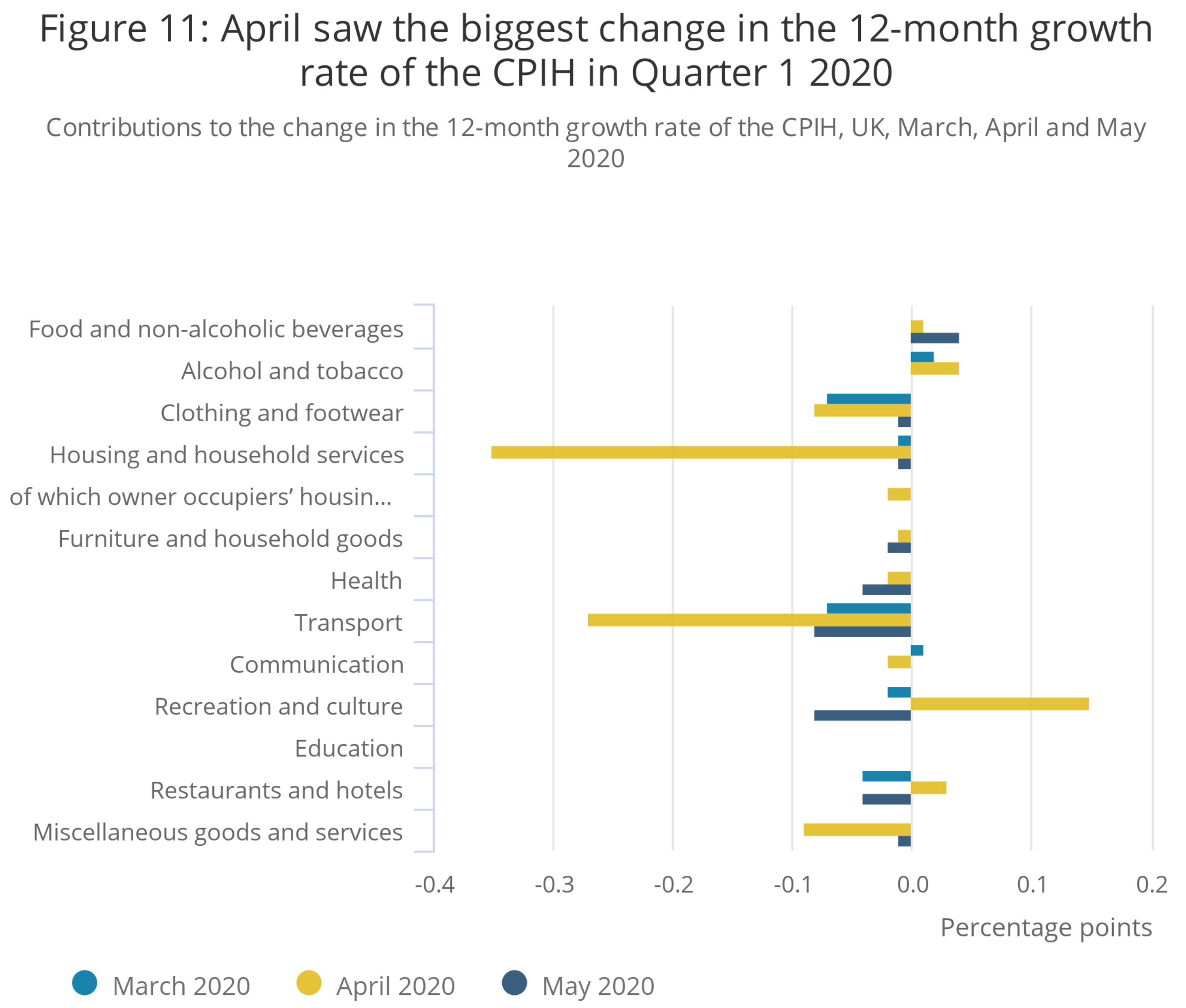
The annual consumer price inflation rate has fallen in each month of 2020 so far, from 1.8% in January to 0.7% in May 2020, as measured by the Consumer Prices Index including owner occupiers' housing costs (CPIH). The current rate of CPIH inflation is the lowest it has been in four years and is likely to be reflecting the effects of the coronavirus pandemic. Business price inflation has seen similar changes, with output prices falling each month since January 2020 and input prices falling on the year since February 2020.

Figure 11 shows contributions to the change in the 12-month CPIH rate. April shows the largest movements in contributions. The large negative contribution came from housing and household services and was largely driven by changes to the Office of Gas and Electricity Markets' (Ofgem's) energy price cap in April 2020. Electricity prices rose by 0.2% between March and April 2020, while gas prices fell by 3.5% on the month. This compares with price rises of 10.9% and 9.3% for electricity and gas, respectively, between the same two months a year earlier. The negative contribution from transport was driven by falling prices for motor fuels, which has continued into May. Petrol prices fell by 10.4 pence per litre between March and April 2020, the largest one-month fall since the current ultra-low sulphur or unleaded petrol was introduced into the basket in 1990, while diesel prices fell by 7.8 pence per litre.

Prices continued to fall in May, when petrol prices were at their lowest since April 2016, with diesel prices at their lowest since September 2016. Further downward contributions in May 2020 also came from recreation and culture and restaurants and hotels, which have been affected by restrictions on face-to-face interactions. [1] Prices for recreation and culture fell slightly on the month, compared with a rise between the same two months a year ago. The downward contribution from restaurants and hotels is because of prices rising by less than this time last year. This partly reflects price movements for items such as fast food and takeaways but is mainly driven by the effect of imputing prices for unavailable items.

Figure 11: April saw the biggest change in the 12-month growth rate of the CPIH in Quarter 1 2020

Contributions to the change in the 12-month growth rate of the CPIH, UK, March, April and May 2020



Source: Office for National Statistics – Consumer Prices Index including owner occupiers' housing costs

Prices for motor fuels tend to move broadly in line with global prices for crude oil. This has been by far the biggest driver of the easing of the input Producer Price Index (PPI) in recent months. Prices for the crude oil component of input PPI fell by 61.7% on the year to May 2020. Prices for crude oil reflect a range of factors, including geopolitical events. In recent months, there has been reduced global demand for crude oil as many countries imposed restrictions on work and travel, including widespread factory closures in China early on in the coronavirus pandemic, and excess supply as OPEC+ failed to agree to cut oil output in March and April. Oil prices have recently risen to above 42 American dollars per barrel as OPEC+ members agreed to cut production levels in the face of dampened demand amid the coronavirus pandemic. The latest [Agents' summary of business conditions] reported that input price inflation remained limited, as manufacturers cited "lower fuel, energy and commodity prices and little change in the cost of imported materials". It also found that there was little scope to raise prices because of uncertainty about demand.

Petroleum products in output PPI and fuels and lubricants in the CPIH have followed similar trends, although the feedthrough to both output PPI and the CPIH is more muted and has a slight lag. Consumer prices also include other costs, such as transport, duty and retail costs, as well as operating costs that must be met even when sales are low.

In response to the coronavirus pandemic, there have been challenges in how we construct our official estimates of consumer prices. We have had to impute prices to limit the impact that unavailable items have on the inflation rate. An alternative approach is to remove the unavailable items and rescale the weights for the remainder of the basket accordingly. Experimental figures have been produced for April and May 2020 and have shown lower annual inflation rates for this period (Table 1). This largely reflects the effects of transport, capturing the impact of prices for international travel being highly seasonal, broadly increasing in the middle of the year, peaking in the summer, and seeing smaller peaks around Easter and Christmas. Removing these items pulls the overall rate of inflation down, as prices for March 2020 were lower than those seen in April and May 2019. Increasing the weights for the remainder of the basket also has an effect, which amplifies the effect of the large fall in prices for motor fuels, pulling the overall rate down even further. That said, we recognise that this has not considered that expenditure on motor fuels is likely to have fallen during the lockdown.

Table 1: 12-month growth rates for the CPIH and CPI
Official, chain-linked and rescaled, percentages, UK, April to May 2020

		CPIH YoY%	CPI YoY%
	Official	0.9	0.8
April 2020	Chain-link	0.9	0.7
	Rescaled	0.8	0.6
	Official	0.7	0.5
May 2020	Chain-link	0.7	0.5
	Rescaled	0.6	0.4

Source: Office for National Statistics – Consumer Prices Index including owner occupiers' housing costs

Notes: Prices

1. There have been production challenges in compiling estimates of consumer price inflation. More information is available in Coronavirus and the effects on UK prices.

2. To introduce a new set of goods and services and a new set of weights, it is necessary to use a chain-link. This is the process of calculating the price change between the new month and an overlap month and then linking that movement on to the official CPIH and Consumer Prices Index (CPI) levels from March 2020.

7 . Conclusions

The coronavirus (COVID-19) is having pronounced impacts on the real and financial economy. UK gross domestic product (GDP) is estimated to have fallen by 2.2% in Quarter 1 (Jan to Mar) 2020, reflecting the impacts of imposing public health restrictions and voluntary social distancing. More timely estimates show that the UK economy fell by an unprecedented 20.4% in April, as the retail, construction, manufacturing, accommodation and food services, and education industries experienced large contractions. Early experimental information is also available on the impact of the coronavirus on the UK economy. The latest Business Impact of Coronavirus (COVID-19) Survey (BICS) showed that while businesses continued to return to trading, 64% of businesses continuing to trade reported that their turnover had decreased below what is normally expected for this time of year.

Public sector finances also showed the fiscal impact of the coronavirus pandemic so far, with a sharp increase in public sector net borrowing (PSNB) in May 2020. This reflects the cost of fiscal interventions so far - including the Coronavirus Job Retention Scheme (CJRS)[1] - and lower tax revenues, in particular lower Value Added Tax (VAT) receipts. Cross-border capital flows are prone to large swings, and these have been particularly marked in Quarter 1 2020, likely reflecting a shift in the risk appetite of investors and an increase in demand for short-term highly liquid assets.

The sharp contraction in the number of hours worked and vacancies shows the effects on the UK labour market, while more timely information shows a further fall in the number of payroll employees of late. Prices have continued to fall in May 2020, as petrol prices and diesel prices were at the lowest levels in four years. Further downward contributions in May 2020 also came from recreation and culture and restaurants and hotels, which have been affected by restrictions on face-to-face interactions.[2]

Notes for Conclusions

1. Further information on the recording of the CJRS is available.

2. There have been production challenges in compiling estimates of consumer price inflation. More information is available in Coronavirus and the effects on UK prices.