Office for National Statistics

Article

Quarterly economic commentary: April to June 2022

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

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1 . Main points

- Compared with Quarter 1 (Jan to Mar) 2022, there has been a slowing in the UK economy in the latest quarter in which gross domestic product (GDP) expanded by a revised 0.2%; real household disposable income has now fallen for four consecutive quarters reflecting the effects of higher price inflation.

- The UK continued to rely on historically high levels of net financial inflows in the first half of this year, in which the current account deficit stood at 5.5% of GDP in Quarter 2 (Apr to June) 2022.

- There was a further tightening in the labour market in the three months to July 2022 as the unemployment rate declined to 3.6%, although this was not because of an increase in employment but a further fall in labour force participation.

- Having reached a 40-year high in July 2022, there was a slight fall in 12-month rate of the Consumer Prices Index (CPI) inflation to 9.9% in August 2022, which reflected lower motor fuel prices.

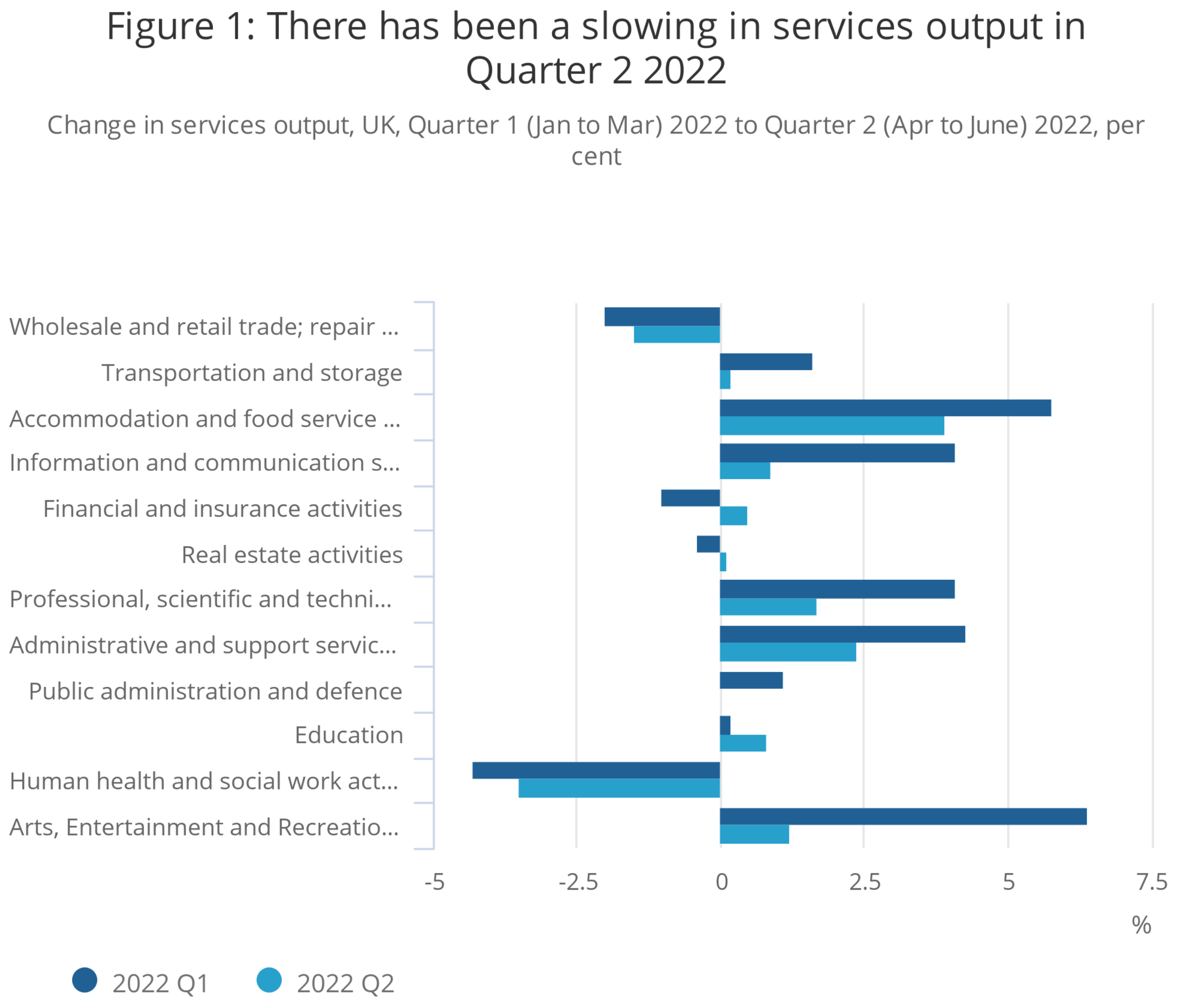
2 . National accounts

Gross domestic product (GDP) expanded by a revised 0.2% in Quarter 2 (Apr to June) 2022, where there has been a slowing in some services industries compared with Quarter 1 (Jan to Mar) 2022 (Figure 1). This reflects the effects of squeezed household incomes and labour and product shortages in some industries. Inflationary pressures reflected in domestic and international prices have fed through to nominal GDP, which increased by 1.4% in the quarter.

Monthly GDP was flat on the three months to July 2022. Consumer confidence has fallen to an historic low, reflecting concerns around the economy and finances from the effects of higher inflation. More timely figures show that the volume of retail sales continued to decline in August 2022.

Figure 1: There has been a slowing in services output in Quarter 2 2022

Change in services output, UK, Quarter 1 (Jan to Mar) 2022 to Quarter 2 (Apr to June) 2022, per cent



Source: Office for National Statistics – Quarterly National Accounts

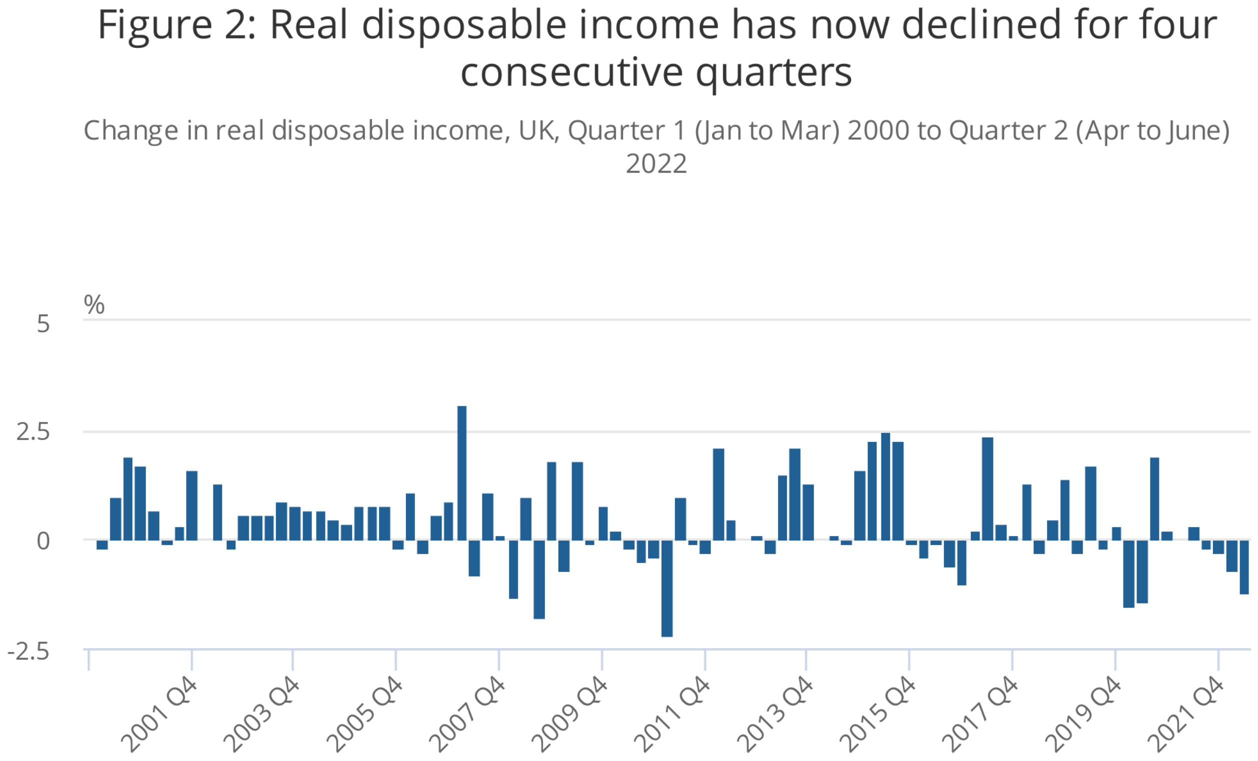
The latest independent forecasts for the UK economy expect a slowdown for later this year, while there is a subdued outlook for next year. The International Monetary Fund has revised down its forecast for the global economy for this year. This highlights the effects of higher-than-expected global inflation worldwide and tighter financial conditions, including further coronavirus (COVID-19) restrictions in China and the effects of the conflict in Ukraine.

There was a further decline in real household disposable income of 1.2% in Quarter 2 2022, which has now fallen for four consecutive quarters reflecting the effects of higher price inflation (Figure 2). This has weighed on the volume of household consumption expenditure. In response to higher prices, recent findings on the cost of living and household finances show that around a quarter of respondents are now unable to save money as usual, while around a fifth had to use savings to cover living costs.

"Forced" savings over the course of the coronavirus pandemic have led to higher levels of accumulated savings, which might give some more scope for consumption smoothing in response to this hit on real incomes. However, high rates of inflation continue to erode the real value of these accumulated savings. In Quarter 2 2022, the household saving ratio is now at 7.6%, which is higher than where it was prior to the pandemic.

Figure 2: Real disposable income has now declined for four consecutive quarters

Change in real disposable income, UK, Quarter 1 (Jan to Mar) 2000 to Quarter 2 (Apr to June) 2022



Source: Office for National Statistics – Quarterly Sector Accounts

Notes:

1. Inflation is captured by the implied price movements in household consumption expenditure.

Households increased the amount they deposited in Quarter 2 2022. More timely money and credit figures for July 2022 show that additional deposits were made in July. There was also an annual increase in all consumer credit, which was at its highest rate since March 2019, although these Bank of England figures show there were slightly lower levels of net borrowing of mortgage debt. However, there was an increase in mortgage approvals for house purchases, which is considered an indicator of future borrowing.

In Quarter 2 2022, private non-financial corporations (PNFCs) continue to be net borrowers, although slightly less so, primarily reflecting lower dividend payments paid out by UK businesses. There was an offsetting increase in underlying inventories, which might reflect the ongoing supply chain disruptions in the global economy.

There was also an increase in capital expenditure by businesses in Quarter 2 2022. Investment intentions continue to be positive, although there is some evidence that uncertainty about the economy and tighter financial conditions was leading to postponement in some capital expenditure. More timely money and credit figures show non-financial businesses made net repayments on loans in July 2022, including for large businesses who had been net borrowers in the previous month.

Public sector net borrowing (PSNB) was £11.8 billion in August 2022, lower than a year ago. Higher Value Added Tax (VAT) receipts reflect in part the effect of higher nominal spending, while Pay-As-You-Earn Income Tax receipts were driven by increases in payrolled employees and earnings over the last year. Higher compulsory social contribution receipts in part reflect the recent increase in the rates of National Insurance contributions. There was also a fall in subsidy payments on the year, mainly because the furlough schemes ended. PSNB was £58.2 billion in the financial year to August 2022.

There was another increase in interest payable on public sector net debt (PSND) over the last year. Many of these debt payments on UK government bonds are index-linked, so that the multi-decade high rates of annual change of the Retail Prices Index is feeding through into higher interest payable. Furthermore, the Office for Budget Responsibility's commentary on the public sector finances: August 2022 highlights that the Energy Price Guarantee is expected to "raise borrowing significantly through the second half of 2022 to 2023".

3 . Balance of payments

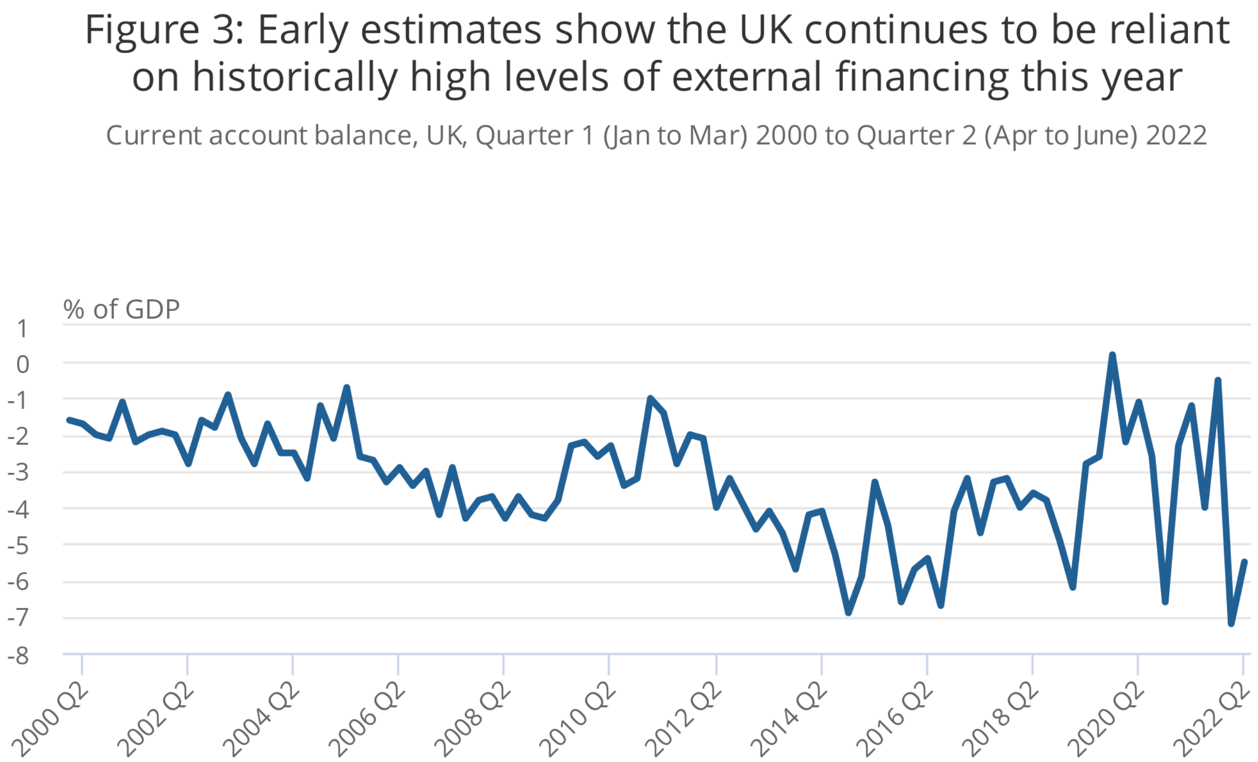
The UK continues to rely on historically high levels of net financial inflows in the first half of this year in which the current account deficit stands at 5.5% of gross domestic product (GDP) in Quarter 2 (Apr to June) 2022. This reflects a narrowing from a record high in the previous quarter, although is still high by historical standards (Figure 3).

This has been underpinned by a worsening goods trade deficit in recent quarters, particularly higher goods imports. This is most evident in the imports of oil and other fuels this year, reflecting the higher prices for these commodities which have increased further following the invasion of Ukraine. Recent evidence from the [Bank of England's Agents' summary of business conditions] highlights how businesses are responding to supply bottlenecks, including "building additional stocks, on or near-shoring production, redesigning products or diversifying supply chains" which might have some impact on international trade flows.

There was an improvement in the UK's net investment income flows in Quarter 2 2022, although the UK continues to pay more income to foreign investors on their holdings of financial assets in the UK. The improvement reflects an increase in net earnings on foreign direct investment, particularly in the holding of foreign assets in the oil industry, where returns have been higher in response to higher oil prices.

Figure 3: Early estimates show the UK continues to be reliant on historically high levels of external financing this year

Current account balance, UK, Quarter 1 (Jan to Mar) 2000 to Quarter 2 (Apr to June) 2022



Source: Office for National Statistics – Balance of Payments

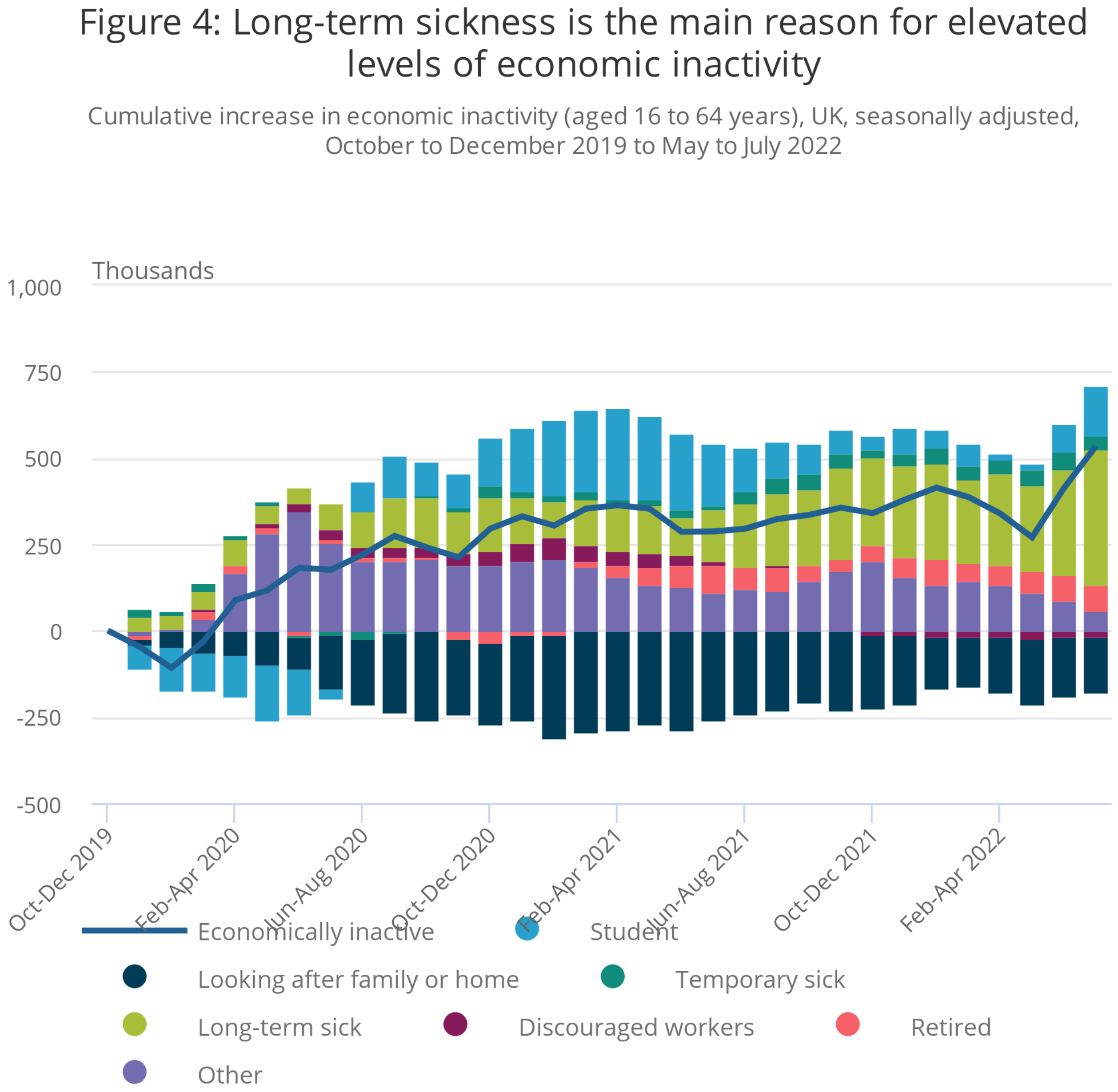
More recently, there have been historically large movements in the exchange rate reflecting domestic and global factors, potentially including some investor uncertainty around the economic outlook, although international financial flows tend to be volatile. In Quarter 2 2022, the UK's net borrowing from the rest of the world has primarily been financed by foreign investors increasing their holdings of portfolio investment in the UK, particularly in government debt.

4 . Labour market

Recent analysis of underutilisation in the UK labour market shows that there is limited spare capacity in the labour market, even if including the marginally attached and the underemployed. There was a further tightening in the three months to July 2022 as the unemployment rate declined to 3.6%, which is its lowest rate recorded since May to July 1974. However, this was not because of an increase in employment but reflected a further fall in labour force participation. Economic inactivity is still noticeably higher than it was prior to the coronavirus (COVID-19) pandemic. This has recently been driven by those aged 50 to 64 years. Those economically inactive because of long-term sickness is at a record high (Figure 4), which reflects the direct and indirect effects of the coronavirus pandemic.

Figure 4: Long-term sickness is the main reason for elevated levels of economic inactivity

Cumulative increase in economic inactivity (aged 16 to 64 years), UK, seasonally adjusted, October to December 2019 to May to July 2022



Source: Office for National Statistics – Labour Market Overview

There is still a strong unmet demand for labour, as the number of unemployed people per vacancy has remained at an historical low for the sixth consecutive month. This might be indicative of there being frictions in the matching efficiency of workers to those vacant jobs, although recent findings show that industry-level mismatch is not currently elevated by historical standards.

Worker shortages continue to be an acute problem for businesses, particularly in the health and social work industry. That said, there has been a fall in the number of vacancies from its record elevated levels which could be indicating some cooling in labour demand. There is some evidence that higher uncertainty and rising costs help explain the recent slowing in hiring.

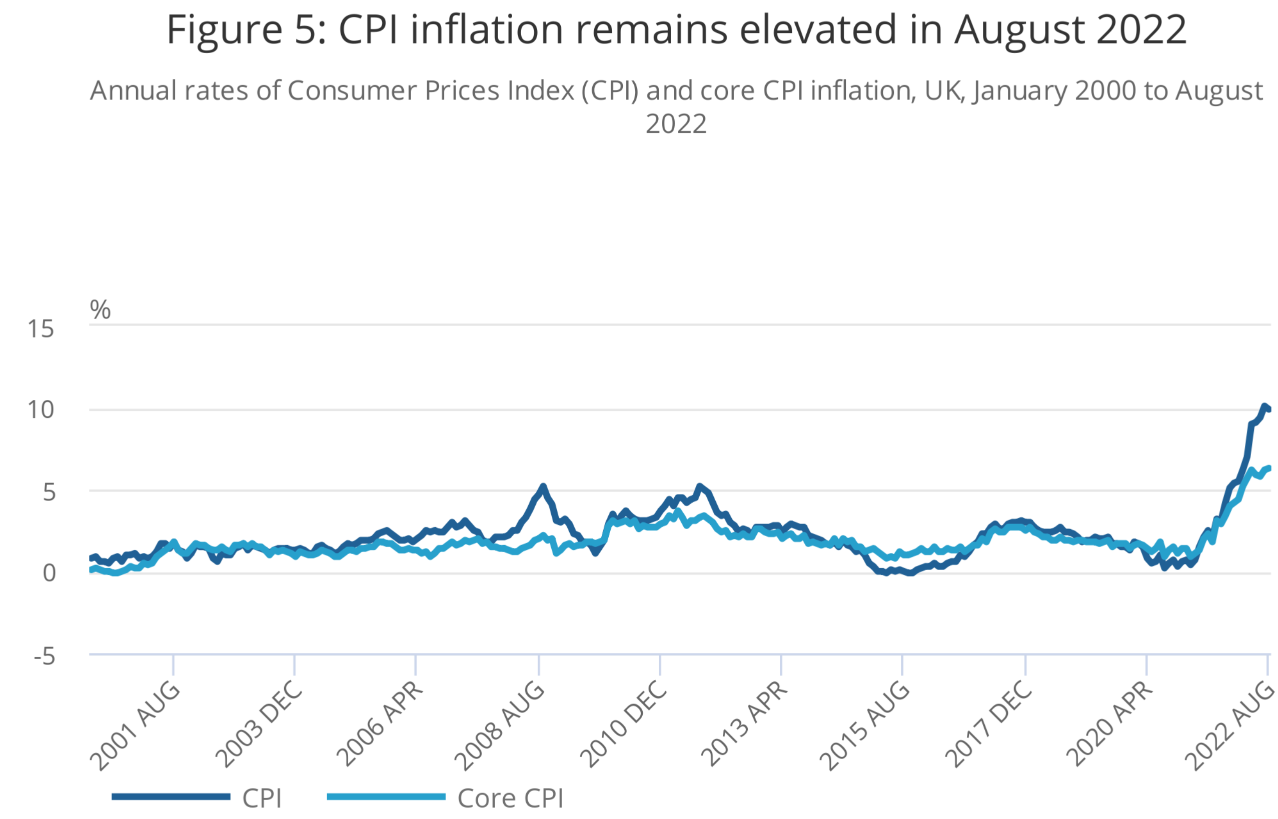
The tightness in the labour market has fed into the recent increases in regular nominal earnings, which increased by an annual rate of 5.2% in the three months to July 2022. However, the gap between public and private pay is at its largest on record, excluding the coronavirus pandemic period. Real regular earnings fell by 2.8% over the same period, reflecting current inflationary pressures. There is some survey evidence from the Bank of England that points to a further increase in expected average pay settlements over the next year, while more firms are offering one-off payments in response to the higher cost of living.

5 . Prices

Consumer price inflation remains elevated, which has primarily been underpinned by increases in global energy and tradable goods prices over the last year.Having reached a 40-year high in July 2022, there was a slight fall in 12-month rate of the Consumer Prices Index (CPI) inflation to 9.9% in August 2022. This easing reflected lower motor fuel prices, which more than offset the continued increase in food prices. There was an increase in the annual rate of core inflation in August, which is at its highest rate in over 30 years (Figure 5). Survey figures from the Bank of England show that one-year ahead inflation expectations have increased further, although there was a fall in the five-year ahead inflation expectations.

Figure 5: CPI inflation remains elevated in August 2022

Annual rates of Consumer Prices Index (CPI) and core CPI inflation, UK, January 2000 to August 2022



Source: Office for National Statistics – Consumer Price Inflation

Notes:

1. Core CPI inflation excludes energy, food, alcoholic beverages, and tobacco.

The annual rate of input price inflation remains high, which reached 20.5% in August 2022. Falling crude oil prices help explain the easing from the record high of 24.2% in June 2022.There was also a slowing in the annual rate of output prices to 16.1% in August 2022. As highlighted in our Business insights and impact on the UK economy: 22 September 2022 article, more than a quarter of trading businesses expect their selling prices to increase in October 2022, highlighting the impact of higher energy and raw material prices. Energy, pay, and the exchange rate underpin cost concerns.

Food and energy bills also help explain the experience of a higher cost of living. Reflecting the sharp increase in global wholesale gas prices as Russia has reduced its gas supplies to Europe, the Ofgem energy price cap had been expected to increase to £3,549 per year from October 2022. However, the Energy Price Guarantee (EPG) caps annual energy prices for the typical household to an average of £2,500 a year for the next two years from October 2022.

6 . Related links

Coronavirus (COVID-19)
Web page | Updated as and when data are available
Our latest data and analysis on the impact of the coronavirus (COVID-19) on the UK economy and population. This is the hub for all special coronavirus-related publications, including the fortnightly Business Insights and Conditions Survey (BICS).

GDP quarterly national accounts, UK: April to June 2022
Bulletin | Released 30 September 2022
Revised quarterly estimate of gross domestic product (GDP) for the UK. Uses additional data to provide a more precise indication of economic growth than the first estimate.

Balance of payments, UK: April to June 2022
Bulletin | Released 30 September 2022
A measure of cross-border transactions between the UK and rest of the world. Includes trade, income, capital transfers and foreign assets and liabilities.

Public sector finances, UK: August 2022
Bulletin | Released 21 September 2022
How the relationship between UK public sector monthly income and expenditure leads to changes in deficit and debt.

Labour market overview, UK: September 2022
Bulletin | Released 13 September 2022
Estimates of employment, unemployment, economic inactivity, and other employment-related statistics for the UK.

Consumer price inflation, UK: August 2022
Bulletin | Released 14 September 2022
Price indices, percentage changes and weights for the different measures of consumer price inflation.

7 . Cite this article

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