

Article

Quarterly economic commentary: January to March 2022

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

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1 . Main points

- The UK economy expanded by 0.8% in Quarter 1 (Jan to Mar) 2022, while the monthly decline in April was primarily driven by the end of the NHS Test and Trace programme.
- The current account deficit widened to a record 8.3% of gross domestic product (GDP) in Quarter 1 2022, although estimates of these international transactions are particularly uncertain at this time.
- There was a pickup in the annual increase in nominal total earnings in the latest three months, particularly in bonus pay; however, real regular earnings fell on the year at their fastest rate in over 10 years, highlighting the impact of higher inflation.
- The 12-month rate of Consumer Prices Index (CPI) inflation increased to a 40-year high of 9.1% in May, where the largest drivers over recent months have been housing and household services, transport, and food and non-alcoholic beverages, reflecting international movements in energy and commodity prices.

2 . National accounts

The UK economy expanded by 0.8% in the first quarter of this year, continuing its recovery from the coronavirus (COVID-19) pandemic. Gross domestic product (GDP) is now 0.7% above its pre-coronavirus Quarter 4 (Oct to Dec) 2019 level (Figure 1). There has been a slowing in momentum in recent months, including a 0.3% GDP contraction in April.

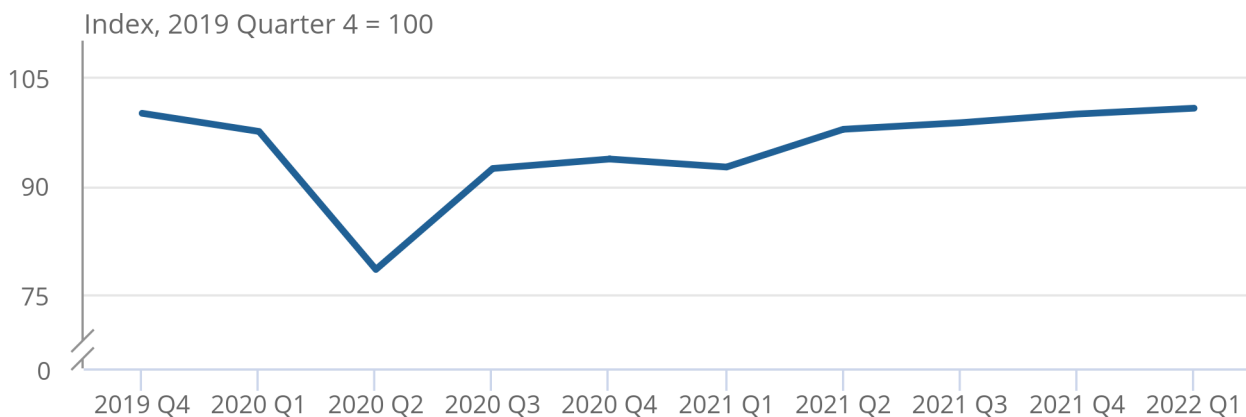
This was the first time that there were monthly declines in the output of all three main sectors -- services, production and construction -- since national lockdown restrictions were re-imposed in January 2021. The April decline was primarily driven by the end of the NHS Test and Trace programme rather than a fall in consumer-facing services. The effects of higher cost and price inflation have been reflected in a sharp decline in [consumer confidence](#). More timely figures show that the [volume of retail sales declined in May](#).

Figure 1: Real GDP is now 0.7% above its pre-coronavirus levels

Level of volume UK GDP, Quarter 4 (Oct to Dec) 2019 to Quarter 1 (Jan to Mar) 2022

Figure 1: Real GDP is now 0.7% above its pre-coronavirus levels

Level of volume UK GDP, Quarter 4 (Oct to Dec) 2019 to Quarter 1 (Jan to Mar) 2022



Source: Office for National Statistics – GDP Quarterly National Accounts

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. Index is referenced to Quarter 4 (Oct to Dec) 2019.

Recent forecasts produced by the Organisation for Economic Co-operation and Development show the [adverse impact of the conflict in Ukraine on commodity, trade and financial markets](#). The global economy is now forecast to slow this year to 3%. [Recent projections by the Bank of England](#) and [independent forecasts for the UK economy](#) also expect some slowdown this year.

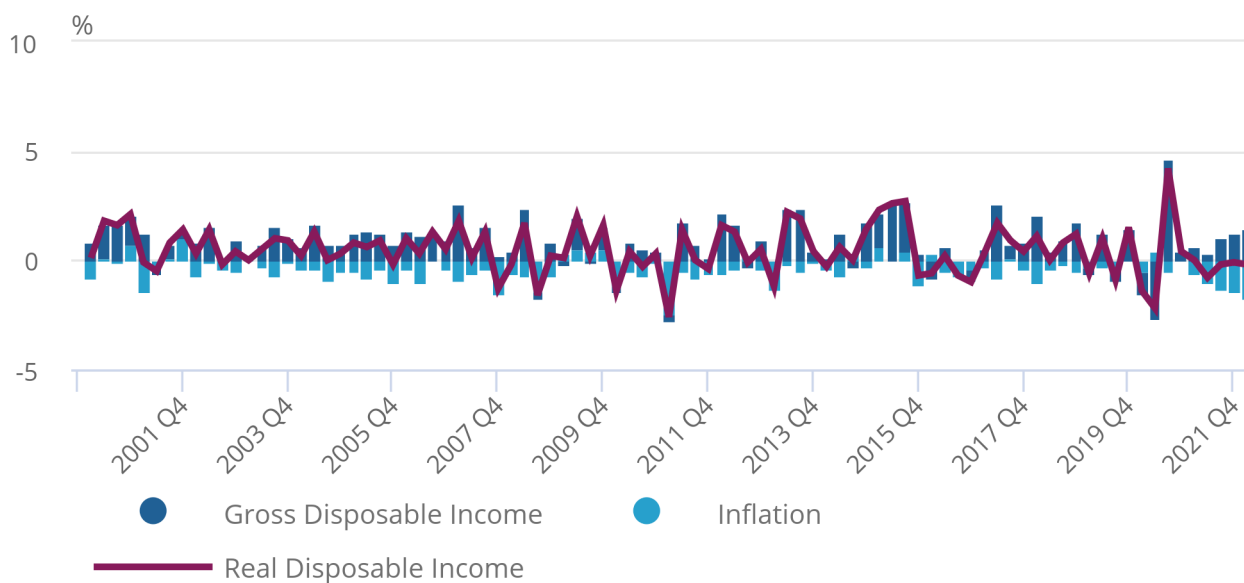
There was a decline in real household disposable income in Quarter 1 (Jan to Mar) 2022, reflecting the effects of higher price inflation more than offsetting the increase in nominal household disposable income (Figure 2). In response to higher inflation, the Bank of England reports that [households are most likely to save less and use existing savings to pay for extra spending](#). "Forced" savings over the course of the 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. In Quarter 1, there was a stabilisation in the household saving ratio at 6.8%, which is slightly higher than where it was prior to the pandemic.

Figure 2: There was a decline in real disposable income in the first quarter of this year

Change in real disposable income, Quarter 1 2000 to Quarter 1 2022

Figure 2: There was a decline in real disposable income in the first quarter of this year

Change in real disposable income, Quarter 1 2000 to Quarter 1 2022



Source: Office for National Statistics – Quarterly Sector Accounts

Notes:

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

Households reduced the amount they deposited in the first quarter of this year, which would be consistent with there no longer being "forced" savings in effect. There was an increase in the holdings of loan liabilities, particularly mortgage loans. More timely figures for April 2022 indicate [lower levels of net borrowing of mortgage debt](#), while there was also a slowing in mortgage approvals for house purchases. However, borrowing of consumer credit continued into April.

Private non-financial corporations (PNFCs) became net borrowers in Quarter 1 2022, primarily reflecting the large increase in underlying inventories. This might reflect the ongoing supply chain disruptions in the global economy as well as higher cost and price pressures. There was a slight decline in capital expenditure by businesses in the first quarter. [Investment intentions](#) continue to be positive, although there is some evidence that a shortage of materials, components and labour, and rising costs are a headwind to investment.

There is some evidence that [business uncertainty](#) has increased in recent months, while [cost inflation](#) remains a concern. This net borrowing was mainly financed by an increase in loans by PNFCs. Recent figures show a [further increase in net borrowing by large businesses from banks in April](#), although small and medium businesses continued to make net repayments to banks.

Public sector net borrowing (PSNB) was £14.0 billion in May 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 was 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 National Insurance contributions (NICs) rate. There was also a fall in furlough subsidy payments on the year.

However, there was a large increase in interest payments on public sector net debt (PSND) over the last year -- the £7.6 billion spending in May is the third highest in any month on record. Many of these debt payments on UK government bonds are index-linked, so that the multi-decade high rates in the Retail Prices Index is feeding through into higher interest payable.

3 . Balance of payments

The current account deficit widened to a record 8.3% of gross domestic product (GDP) in Quarter 1 (Jan to Mar) 2022 (Figure 3), although estimates of these international transactions are particularly uncertain at this time. This reflected very large movements in trade flows in the first quarter, particularly higher goods imports.

This was primarily in manufactured goods, such as machinery and transport equipment, while there were also increases in the imports of oil and other fuels, which might reflect the higher prices for these commodities over the quarter. There were also volatile movements in the trade of non-monetary gold. Recent evidence points to how [supply chain disruptions are expected to continue into next year](#), which might have some impact on international trade flows as businesses respond to minimise these impacts.

There was an unwinding in the UK's net investment income flows in Quarter 1, reflecting an increase in dividend income paid to foreign investors. These movements have been volatile of late, reflecting how there have been lower or deferred dividends through much of the coronavirus (COVID-19) pandemic. It might be that businesses are starting to distribute more of these profits, including to foreign investors.

Figure 3: Early estimates show a record current account deficit in Quarter 1 2022

Current account balance, UK, Quarter 1 2000 to Quarter 1 2022

Figure 3: Early estimates show a record current account deficit in Quarter 1 2022

Current account balance, UK, Quarter 1 2000 to Quarter 1 2022



Source: Office for National Statistics – Balance of Payments

International financial flows tend to be volatile. In Quarter 1, the UK's net borrowing from the rest of the world has primarily been financed by foreign investors increasing their holdings of other investment in the UK, which includes loans and deposits, and a reduction of the holding of equity investments owned by the UK. There were also large divestments of portfolio investment by UK and foreign investors.

4 . Labour market

Despite the headwinds of inflationary pressures, the UK labour market has continued to tighten in recent months. Survey indicators point to how [recruitment difficulties remain high](#), while there was a further increase in job vacancies to another record high in March to May 2022. The unemployment rate continues to fall and is now similar to the rates seen before the coronavirus (COVID-19) pandemic, while there are a similar number of vacancies as there are people in unemployment. This might be indicative of there being frictions in the matching efficiency of workers to those vacant jobs.

The latest insights [show that 15% of businesses were experiencing a shortage of workers in early June 2022](#), while the redundancy rate fell to another record low in the three months to February to April.

The tightness of the labour market also reflects the increase in the number of people that have become economically inactive in recent years, which is still above its pre-coronavirus level, with fewer people available to work. Some of this rise in inactivity reflects the retirement of older workers as well as those who are considered long-term sick, and so are not actively seeking work and/or not available to start work. There has also been an increase in those studying.

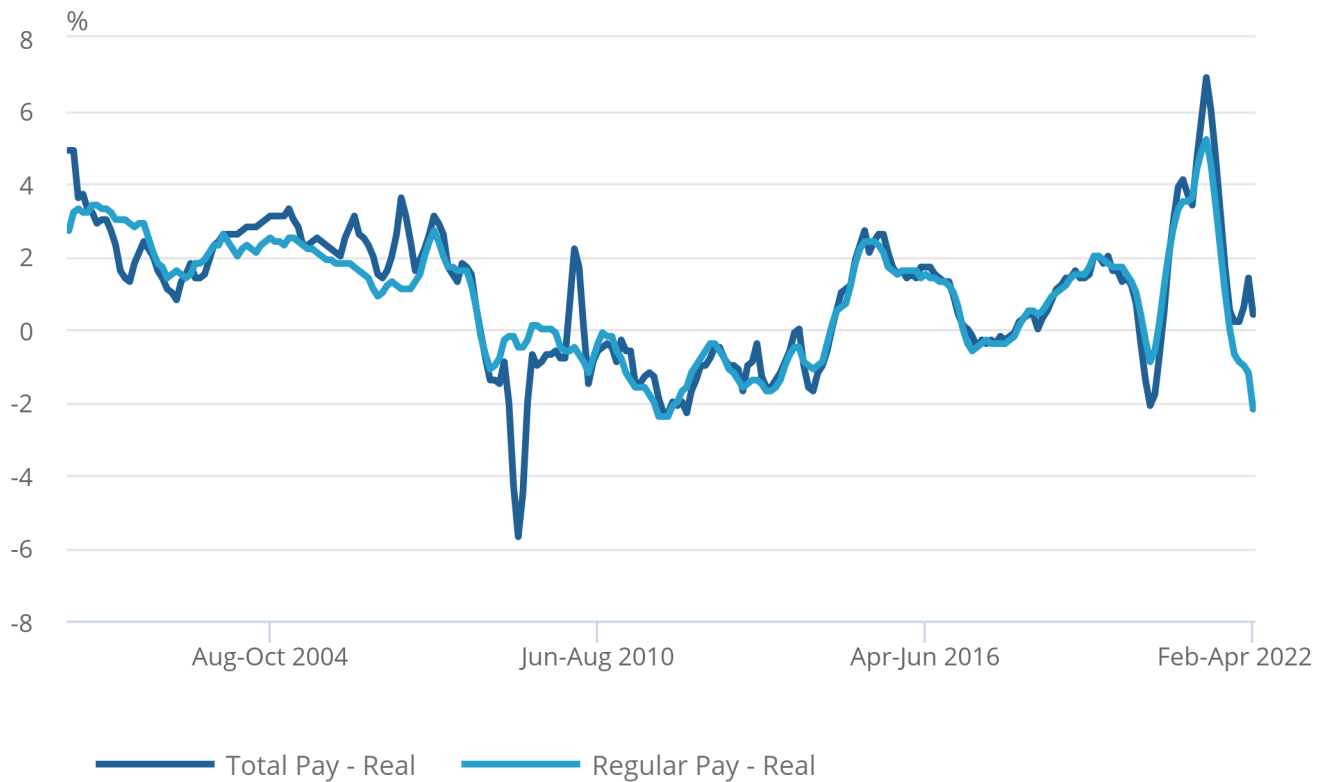
There was a pickup in the annual increase in nominal total earnings in the latest three months, particularly in bonus pay. The Bank of England found that [some companies are awarding one-off bonuses](#) to "compensate workers for higher inflation and to retain staff". However, Figure 4 shows that real regular earnings fell on the year highlighting the squeeze of higher inflation - the 2.2% decline on the year is the largest fall in over 10 years as inflationary pressures picked up.

Figure 4: The 2.2% decline in real regular earnings was the largest in over 10 years

Real and nominal total pay: UK, 2001 to 2022

Figure 4: The 2.2% decline in real regular earnings was the largest in over 10 years

Real and nominal total pay: UK, 2001 to 2022



Source: Office for National Statistics– Monthly Wages and Salaries Survey

Notes:

1. Real regular pay estimates based on the Consumer Prices Index including owner occupiers' housing costs (CPIH).

5 . Prices

Consumer price inflation has continued to rise sharply in recent months. The increases in global energy and other tradable goods prices reflects the demand and supply impacts of the coronavirus (COVID-19) pandemic, which have been reinforced by the effect of the conflict in Ukraine.

The annual rate of the Consumer Prices Index (CPI) including owner occupiers' housing costs (CPIH) hit 7.9% in May 2022 (Figure 5). Annual CPI inflation increased to 9.1% in May -- the highest annual rate in 40 years. There is some evidence that [inflation expectations](#) for the year ahead are also increasing.

Figure 5: The annual rate of CPI inflation increased to over 9% in May 2022

Annual rates of Consumer Prices Index (CPI) and Consumer Prices Index including owner occupiers' housing costs (CPIH), Jan 2000 to May 2022

Figure 5: The annual rate of CPI inflation increased to over 9% in May 2022

Annual rates of Consumer Prices Index (CPI) and Consumer Prices Index including owner occupiers' housing costs (CPIH), Jan 2000 to May 2022



Source: Office for National Statistics – Consumer Price Inflation

Producer prices have also continued to rise sharply with the annual rate of input price inflation reaching 22.1% in May 2022 -- the highest the rate has been since records began in January 1985. Output prices increased at their fastest annual rate in around 45 years.

Food products made the largest contribution to the 12-month rate in May 2022. [Around a quarter of businesses have cited input price inflation as their main concern](#) for July 2022, while survey evidence points to how [businesses in some industries are continuing to pass on these higher costs into prices](#).

The largest drivers of consumer price inflation over recent months have been housing and household services, transport, and food and non-alcoholic beverages, keeping in line with international movements in energy and commodity prices. The increase in wholesale gas and energy prices contributed to the rise in the Ofgem price cap that came into effect in April 2022. Forecasts expect CPI inflation to peak later this year, based on the expected higher wholesale energy prices, which would lead to a further increase in the Ofgem price cap.

The Opinions and Lifestyle Survey shows that [consumers are responding to price rises](#) primarily by reducing their expenditure on non-essential goods and services, using less gas and electricity, and spending less on food shopping and essentials. This also shows that some are using more credit than usual. Around a fifth report that they have had to borrow more money or use more credit in the last month compared with a year ago.

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: January to March 2022](#)

Bulletin | Released 30 June 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: January to March 2022](#)

Bulletin | Released 30 June 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: May 2022](#)

Bulletin | Released 23 June 2022

How the relationship between UK public sector monthly income and expenditure leads to changes in deficit and debt.

[Labour market overview, UK: June 2022](#)

Bulletin | Released 14 June 2022

Estimates of employment, unemployment, economic inactivity and other employment-related statistics for the UK.

[Consumer price inflation, UK: May 2022](#)

Bulletin | Released 22 June 2022

Price indices, percentage changes and weights for the different measures of consumer price inflation.