

UK: Covid presses pause on the economic recovery

Activity data has pulled back from recent highs amid rocketing Covid-19 cases. Thankfully hospitalisations and mortality have been much lower than past waves, and that means rules are set to be eased in coming days. The medium-term story still looks fairly solid despite some slower growth this summer. We expect a 1Q23 Bank of England rate hike



Source: Shutterstock

Covid-19 cases are rocketing but hospitalisations have stayed surprisingly low (so far)

The UK economy has had a remarkably good run over recent weeks. The recent reopenings and increased optimism will likely translate into growth above 5% in the second quarter. The size of the economy is probably around 2% below pre-virus levels, if we look at where monthly GDP data is likely to be in July.

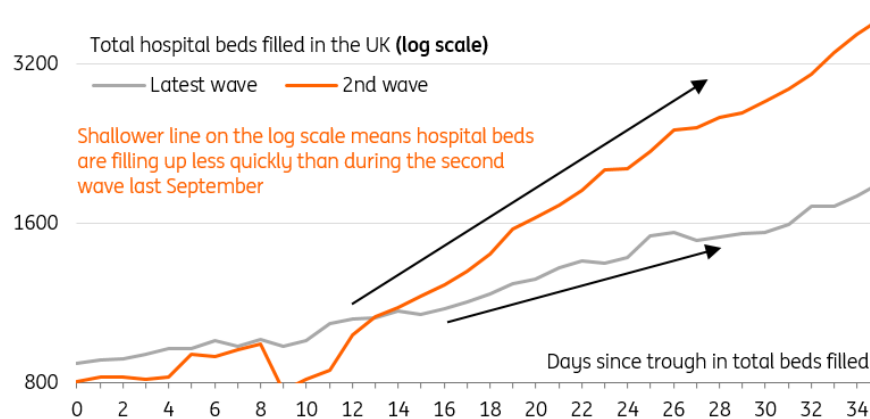
But Covid-19 cases are rising quickly again, and are showing few signs of slowing. With infection numbers doubling every 8-9 days, daily cases above 100,000 are entirely possible in the coming

weeks.

The encouraging news, at least, is that hospitalisations are running much lower than you'd expect given current case numbers. Vaccines are clearly working well, and that's reflected in the lower average age of cases but also lower mortality relative to the second wave. At the time of writing, there were 17 deaths on average over the past week, compared to over 400 when cases were at a similar level last year.

For that reason, the UK government is signalling it will press ahead with the removal of remaining restrictions on 19 July. This remains something of a calculated risk, in that rocketing case growth could in a worst-case scenario still result in hospitals being overwhelmed. But from an economic perspective, this signals that a return to business closures remains unlikely this side of winter.

Hospital beds have filled up more slowly than the second wave



Source: Gov.uk Coronavirus Dashboard, ING calculations

Trough after first wave: 2 Sept 2020. Trough after second wave: 27 May 2021

The recovery is paused - but crucially not cancelled

Still, the recovery is likely to be put on pause to some extent over the summer, and in fact, that's what the high-frequency data is already hinting at. Spending data and mobility have pulled back a little from recent highs.

Our main concern is that consumer confidence begins to decline once more. Admittedly a weekly survey of individuals doesn't yet point to increased Covid-19 concerns or reduced socialisation, but it's something we're keeping an eye on as case numbers rise.

Rising Covid-19 prevalence also means higher rates of contact tracing and self-isolation. These risks amplifying the current worker shortage in some of the consumer services industries, but could also see consumers reducing social contacts to mitigate the risk of having to stay at home for 10 days.

Having said all of that, it's important not to overstate the economic impact, relative to what's come so far in the pandemic. We're still looking at positive third-quarter growth in the region of 1.5%. And indeed assuming no new vaccine-evading variants arrive, the medium-term outlook still looks good.

But thinking about the Bank of England, the latest uncertainty is perhaps a reminder that market

pricing on the timing of the first-rate hike - in a little over a year - is probably getting a bit ambitious. Unlike the US, the UK is lacking a big fiscal impulse over the coming months, and inflation is likely to moderate by the middle of next year. For now, we're in the camp looking for a first-rate rise in early 2023.

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