

UK set for slow recovery after record second quarter economic decline

The UK economy is likely to experience a decent rate of growth during the third quarter, but importantly it will be at least a couple of years before all of the lost ground is recovered. Consumer caution, the unwinding of the Job Retention scheme and the end of the post-Brexit transition period are pose risks to the recovery



London Underground trains remain almost empty despite an easing of lockdown measures

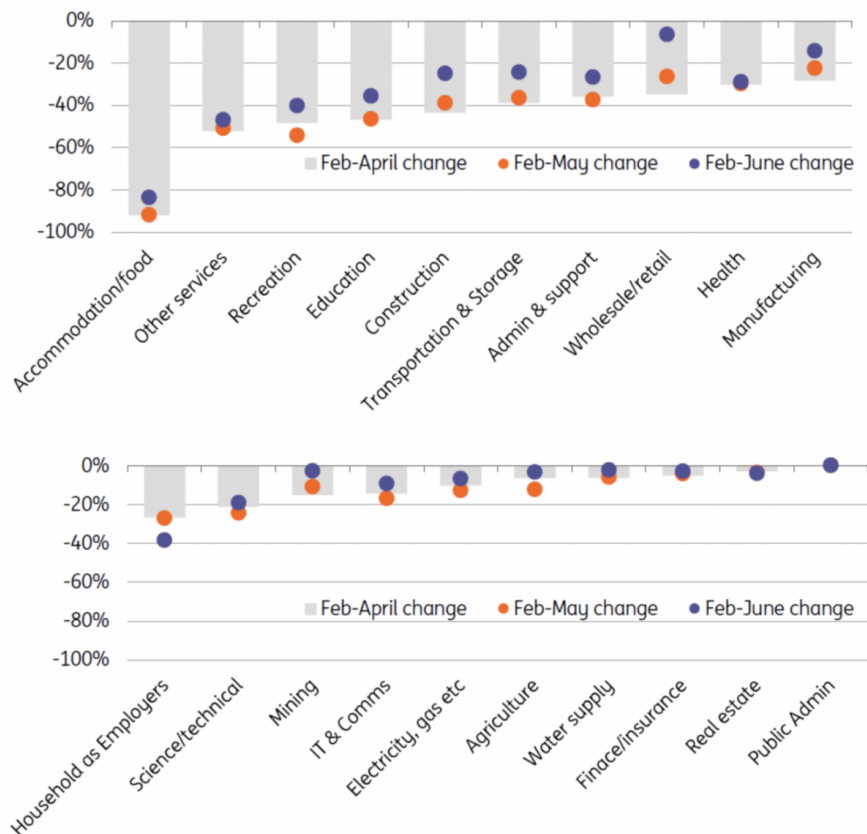
The 20.4% fall in UK second-quarter GDP will catch most of the headlines today. Britain's lockdown was more protracted than most others, and that unsurprisingly means that the overall slowdown in activity through the first half of the year (-22%) was more pronounced than that in the Eurozone as a whole (albeit this masks big variations) and the US.

More importantly though, the latest monthly GDP figures indicate that activity saw a much more solid rebound in June than the disappointing outcome for May. Activity was up 8.7%, and unsurprisingly the industry breakdown shows that a fair chunk of the rebound came from wholesale/retail trade as shops began to reopen. Retail sales, don't forget, are now essentially back to where they were before lockdown, although this partly reflects a big shift to online shopping.

We'd expect to see another decent bounce in GDP during July when a wider range of service-

sector businesses were allowed to open. And arithmetically, the timing of all of these changes (towards the end of the second quarter, or early into the third) probably means that the UK's third-quarter rebound is likely to appear larger than in many other economies. While we suspect the rebound may not be quite as large as the Bank of England's 18% third-quarter growth forecast, it might not be far off.

Change in UK (monthly) GDP by industry



Source: Macrobond, ING calculations

Of course, percentages can be misleading, and the reality is that the overall size of the UK economy is still likely to be almost 10% smaller at the end of the third quarter than when compared to pre-virus levels. We also suspect it will take at least another two-to-three years for the economy to regain all the lost ground, quite a bit longer than is being forecasted by the Bank of England (who assume a full recovery by the end of 2021).

Rising unemployment is probably the biggest threat to the recovery at the moment, and this is being linked to the gradual unwinding of the government's furlough scheme over the next few months. Many firms, particularly in the hardest-hit hospitality/recreation sectors are still struggling as a result of ongoing consumer caution and social distancing constraints.

Investment is also likely to remain a major drag, particularly in light of the forthcoming changes at the end of the post-Brexit transition period. Even if there is a trade deal agreed this year, businesses will encounter a wave of new costs across a range of sectors. We'd note that the sectors likely to be most heavily affected (eg manufacturing) by these changes are not necessarily going to be the same as those hardest hit so far by the Covid-19 crisis (which has most severely hit

consumer services).

For 2020 as a whole, we expect the UK economy to have shrunk by 9.7%.

Author

James Smith

Developed Markets Economist, UK

james.smith@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.