January 2021

# UK Economic Outlook

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# Summary of key points

1. The UK economy is following a kinked recovery profile. Following two consecutive quarters of negative growth in the first half of the year, quarter on quarter growth in Q3 stood at 16.0%. However, following a national lockdown in England in November and the introduction of tougher Tier 4 restrictions in England, we expect the UK to end the year with quarterly growth of -3.7% for Q4.

2. There has been a gradual slowdown in the monthly pace of the recovery since June, with growth further decelerating in October with the introduction of the tiered local lockdown system. We expect that month-on-month GDP growth contracted in November at -9.4% due to the second national lockdown in England.

3. Our projection of annual UK GDP growth for 2020 is -11.0%. We expect economic output to remain 12.0% below pre-pandemic levels by the end of the year.

4. We expect the UK's earlier than expected vaccination rollout will boost growth in 2021. However, there is still significant uncertainty over the pace and the path of the recovery, including the speed of the vaccine rollout and its effectiveness in limiting the spread of the new virus variants. Additional key risks include the possibility of a rise in COVID-19 cases after the Christmas period, the possibility of lockdown extension beyond February, the extent to which businesses adapt to new trading arrangements with the EU, the outcome of the US-UK trade negotiations, and the degree of economic scarring.

5. Under our 'slow recovery' and 'quick recovery' scenarios, the expected annual GDP growth rates range from around 2.2% to 4.8% in 2021, accelerating to around 5.1% to 6.3% in 2022 before slowing down to about 1.7% to 2.0% in 2023. Under the 'quick recovery' scenario we expect 2021 to be an important year in which most of the output loss caused by the first national lockdown would be recovered.

6. Our expectation is that the economy will recover to the pre-crisis levels by Q1 2023 under the 'quick recovery' scenario, and by the middle of 2024 under the 'slow recovery' scenario. These are two quarters slower than our previous forecasts made in November, due to the outcome of the UK-EU new trade agreements, the possibility of a lockdown extension and long term economic scarring which overshadow the earlier-than-expected vaccination programme.

7. We anticipate that most sectors will return to growth in 2021, including the hard-hit sectors such as accommodation and food services, as they recover from a low base in 2020. The health sector will be boosted by the vaccine rollout, while the financial services sector could face some challenges initially in 2021 as firms adjust to losing access to EU passporting. Although better prepared, the services sector would need to brace itself for additional non-tariff measures (NTMs) and services regulations from the new year.

8. We expect inflation to gradually pick up in 2021, as the economic recovery boosts demand and this feeds through to an increase in prices. We expect that inflation could average around 1.4-1.5% in 2021. However, an uptick in COVID cases post-Christmas, combined with the end of the furlough scheme in April, could mean consumers are less willing to spend, putting downward pressure on prices. The end of the transition period with the EU, on the other hand, will likely create upward pressure on domestic prices, as the cost of imports from the EU raises prices. We expect Brexit to result in an 10% increase in food prices.

# 1. UK economic prospects

## 1.1 Recent developments in the UK economy

The impact of the COVID-19 pandemic on the UK economy was first felt in March 2020, as a national lockdown forced the closure of hospitality and non-essential retail and required people to work from home where possible and avoid social places. Despite the lockdown only being in place for eight days in March, the impact on the economy was significant. Month on month growth stood at -7.3%, falling further to -19.5% in April as the first full month spent in lockdown.

There was a limited reopening of the economy in May, which accelerated in June and through to July and August. Growth was strongest in manufacturing and construction, where workers were able to return to factories and building sites.

The data for the three months to September showed the UK economy grew by 16.0% on the previous quarter, the highest quarterly rise ever recorded given the low base of GDP from Q2. The recovery occurred as more businesses, non-essential retailers and hospitality were allowed to re-open, while a reduction in the number of COVID cases over the summer reduced perceived health risks and boosted consumer and business confidence.

Pent-up demand helped the retail sector to recover to pre-pandemic levels by July. Consumer spending was further boosted by policies such as the 'Eat out to Help out' scheme, which helped output in the accommodation and food services sector recover from being just 13% of pre-pandemic levels in Q2, to 71% in Q3.

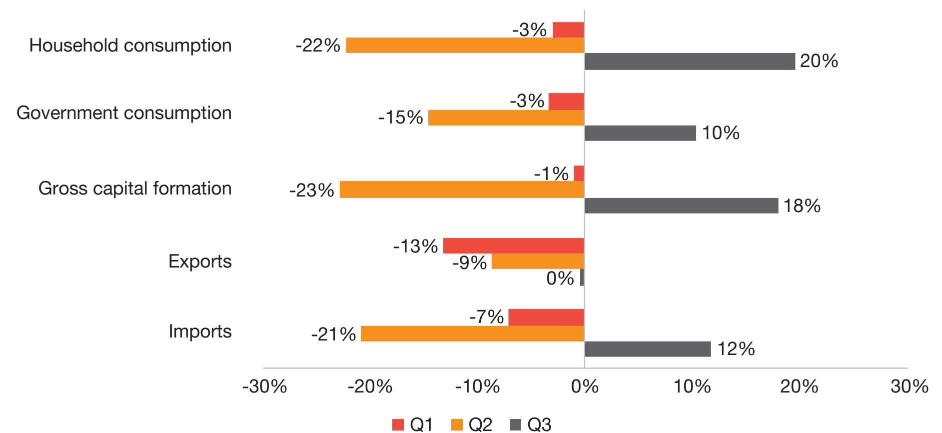
However, beneath the surface we find a slowdown in the monthly pace of the recovery. Month-on-month growth has gradually slowed from 6.3% in July, 2.2% in August, 1.0% in September, and 0.4% in October. This means more than 80% of the UK's recovery occurred in June and July.

**Table 1.1: Projected annual real GDP growth by scenario**

| Real GDP growth | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|
| Quick recovery scenario | -11.0% | 4.8% | 6.3% | 2.0% |
| Slow recovery scenario | -11.0% | 2.2% | 5.1% | 1.7% |

Source: PwC analysis

**Figure 1.1: Growth in GDP expenditure components, Q1 – Q3 2020**




Source: ONS

Household consumption grew by 20% in Q3 relative to Q2, driven by spending on restaurants and hotels as the economy gradually opened up, buoyed by the government's 'Eat Out To Help Out' scheme in August. Transport also played a part, due to higher spending on motor cars and fuels as normal activity and travel around the country resumed. Positive contributions were also made from clothing and continued growth in spending on furniture and household equipment. This corresponds with record quarterly growth of 17.4% in retail sales. Household consumption, however, remains 10% below levels seen in Q4 2019 as consumers continue to postpone some spending and build up their precautionary savings.

Government consumption grew 10% in Q3, driven by activity in healthcare, as elective surgeries and GP services resumed. The volume of healthcare consumption, however, remains 25% below Q4 2019 levels as coronavirus safety protocols continue to limit activity and patient capacity. With the reopening of schools in September, education consumption also picked up, but with lower attendance than usual.

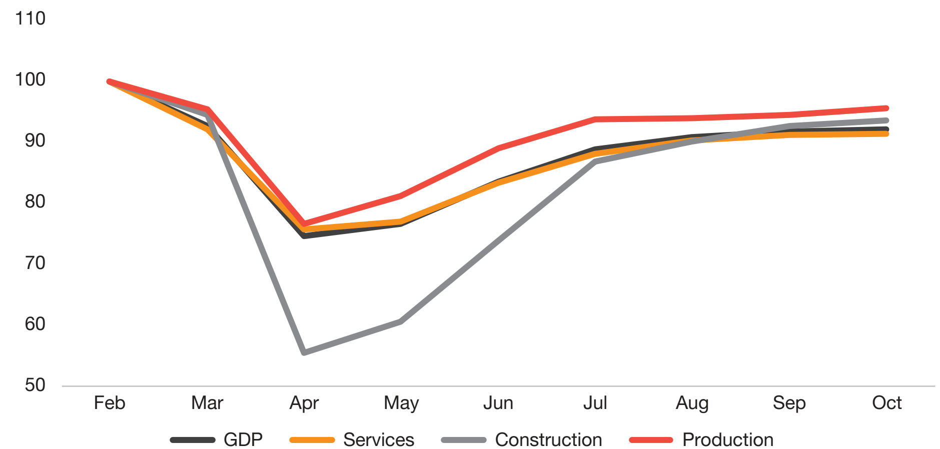
Growth in gross capital formation in Q3 was mainly driven by housebuilding (which grew by 70% q-on-q), as construction activity resumed, and business investment (which grew by 9% q-on-q), as firms make investments in ICT equipment and buildings. Business investment, however, stands at just 80% of its Q4 2019 levels, reflecting higher levels of economic uncertainty restraining the willingness of firms to undertake investment.

On net exports, a recovery in imports in Q3 reflects significant pent up demand and early stockpiling activities ahead of the end of the transition period. This boosted demand from UK consumers for international goods and services.

The latest official data for October revealed a further slowdown in growth of 0.4%, as the introduction of the tiered local lockdown system in England restricted economic activity. The key points from the latest data are as follows:

- The manufacturing sector contributed the most to October's monthly growth, with the healthcare sector being the second largest contributor due to a step-up in the volume of activity. Conversely, accommodation and food grew by -0.4%, as a result of heightened COVID measures in place from late September.
- Sectors such as air and rail transport, arts and entertainment, and travel agencies have recovered less than half of their pre-February levels of output. Construction has made one of the strongest recoveries; its change in GDP between the trough (April 2020) and October is almost 70%. This compares to just 21% for services.
- Much of the growth in the economy is coming from larger businesses, with smaller businesses the most adversely affected – particularly those that are customer facing and based in the service sector.
- As of October, around 23.4% of the lost output caused by the first national lockdown has now been clawed back, but economic output remains 7.9% below pre-COVID levels.

**Figure 1.2: Monthly output index of UK sectors (Jan 2020 = 100)**




Source: ONS

**The labour market**

The impact of economic shocks on the labour market typically lag behind the impacts on the wider economy. In the case of the COVID-19 pandemic, the government's job retention and job support schemes have further delayed the labour market impact as businesses have been able to retain workers despite the shocks to demand. As a result, unemployment has been kept relatively at bay over the course of the pandemic to date, compared to other recessions such as the global financial crisis. From 4% at the start of the year, the unemployment rate has risen gradually, to around 4.4% in the summer, and further to 4.9% in the three months to October in the latest data. The number of payroll employees in November is 2.7% below what it was a year ago; since February, 819,000 fewer people are in payrolled employment.

The most recent months of data, however, reveal that the labour market has begun to feel the pressure. In the three months to October, redundancies set a new record high – rising by a record 217,000 on the previous quarter to 370,000. These figures reflect the tightening of COVID restrictions in October, with the introduction of the tiered local lockdown system. This meant that certain sectors were shut down, like hospitality and non-essential retail, resulting in businesses adjusting to lower levels of demand by making workers redundant.

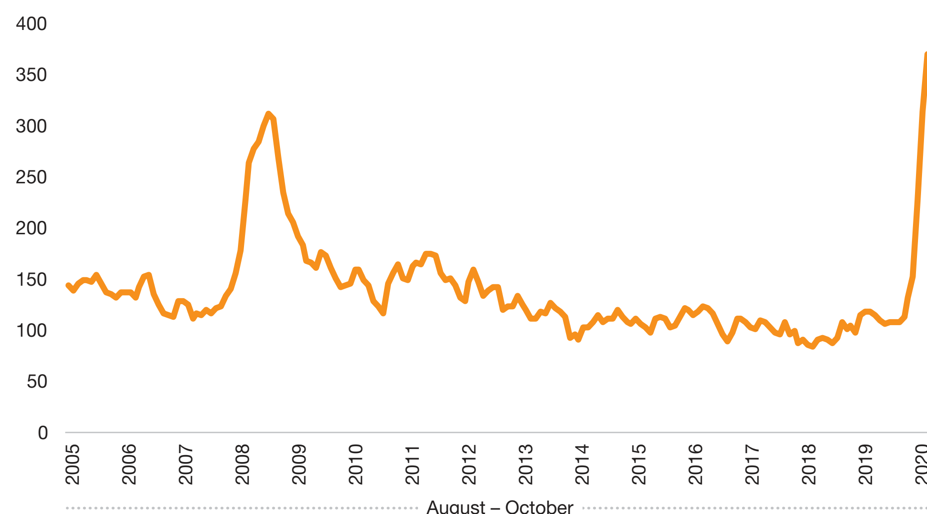
However, there are some tentative positive signs as well. Despite the tightening of restrictions in October, total hours worked continue to recover, increasing by 12% in the quarter. Vacancies also continue to increase. For the three months to November, there were 547,000 vacancies, representing a quarterly increase of 110,000. Levels do remain 32% below what we were seeing pre-pandemic, and this is most acute for larger businesses, for which vacancies are almost 40% below pre-COVID levels.

Despite record high redundancies and rising unemployment, the share of people who are economically inactive remains largely unchanged at 20.8% in October. Indeed, in September, there was a record flow of 215,000 people from economic inactivity to unemployment, which suggests that the gradual relaxation of social distancing measures and the opening of schools has encouraged workers to seek employment. It also implies that the rise in the inactivity rate observed in the previous months is likely to be a temporary rather than a permanent phenomenon, and that scarring in the labour market might be limited as long as demand levels in the economy return to pre-crisis levels.

The outlook for the labour market will depend on the impact of the second national lockdown in England in November, compared to the positive impact of the re-introduction of the more generous furlough scheme. The certainty of support for furloughed employees until the end of April, combined with the rollout of a vaccine in the UK, may provide businesses with the optimism and confidence to keep employees on the payroll, despite tighter lockdown restrictions causing another shock to demand. In a recent PwC survey, 19% of respondents stated that they expect to lose their job in the next 12 months.[1]

Just as the impacts on the labour market lag behind the wider economy in a recession, they will also lag behind in the recovery. So it may be some months before we see a recovery in the labour market, even if the vaccine stimulates an economic recovery in the new year. The end of the furlough scheme at the end of April is also likely to hinder any recovery; the OBR estimates that the unemployment rate could shoot up to around 7.5% in Q2 2021.

**Figure 1.3: UK redundancies (people aged 16 and over), not seasonally adjusted, thousands**




Source: ONS

## 1.2 The outlook for the UK economy

The UK economy is following a kinked recovery profile. Following two consecutive quarters of negative growth in the first half of the year, quarter on quarter growth in Q3 stood at 16.0%. However, following a national lockdown in England in November and the introduction of tougher Tier 4 restrictions in England, followed by the third national lockdown we expect the UK to end the year with quarterly growth of -3.7% for Q4.

We developed a Nowcasting model to estimate UK monthly GDP growth. A Nowcasting model is an econometric model which uses fast data indicators, such as Google mobility data, to provide more timely estimates of economic activity than official data. In our November UK Economic Update,[2] we presented the results of our model for the first time to estimate October's growth. Our prediction for month-on-month growth in October of 0.36% aligns to the ONS' subsequent official estimate of 0.4%.[3]

We then expect the UK economy to contract by 9.4% in November relative to October, due to the second national lockdown in England. This is a much smaller contraction than the first national lockdown caused, which led to month-on-month growth in April of -19%. There a number of reasons for this:

- The November lockdown did not impact as many sectors and to the same extent as in April. Sectors, such as construction, have had time to implement effective social distancing working arrangements, allowing them to maintain activity. Schools also remained open in November's lockdown, enabling the education sector to maintain activity.
- The investments in technology that many businesses have made since the first lockdown have enabled many workers to more effectively work from home and maintain activity and productivity in November, compared to April's lockdown.

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[1] PwC's QuantiBus is a weekly consumer survey in which we talk to 1,000 participants aged 18+ and is nationally representative by gender, age and region. Survey conducted w/c 7th December.

[2] https://www.pwc.co.uk/services/economics/insights/uk-economic-update-covid-19.html – **link**

[3] How to use nowcasting techniques to beat the queue in a world of fast data? – **link**

- Looking at fast data indicators, such as google mobility data, the impact of the lockdown has not been so significant. In April, mobility (an average of workplace, retail and recreation, and transit station mobility) fell by around 70% compared to a pre-COVID baseline. In November, the impact was around -45% compared to the same baseline.

The contraction in November is mainly driven by the shutdown in sectors such as non-essential retail and hospitality. A worsening of business and consumer confidence will drag on growth, as uncertainty around the pandemic and the extent to which tight lockdown measures will remain in place holds back spending and investment decisions.

The extension of the furlough scheme to the end of April will likely have helped to prop up confidence to some extent for the 2.4 million workers still on furlough (as of the end of September), but the risk of redundancy remains high as business grapple with the prospect of the tiered local lockdown remaining in place for some time. Redundancies rose again in October by 217,000 on the quarter.

We expect the UK to end the year with monthly growth of 2.8% in December, following November's contraction. Economic growth in December will be held back somewhat by the tiered local lockdown system, which has kept large parts of the country in lockdown under the highest alert level. We note that there is considerable uncertainty regarding our December nowcast, as more regions are moving into Tier 4 but data has yet picked up.

Our projection of annual UK GDP growth for 2020 is -11.0%. We expect that economic output will remain 12.0% below pre-pandemic levels by the end of the year.

**Outlook for 2021 and 2022**

Looking to 2021, there are a number of factors which will determine the pace of the UK's economic recovery. These include the following:

- The development of the COVID-19 pandemic and the prevalence of government measures to curb the spread. Specifically, there is a key risk that the Christmas period and new virus variants will contribute to an increase in the effective reproduction rate of the virus ('R') in January.
- The pace at which a critical mass is vaccinated against COVID-19 in the UK and the effectiveness of such vaccines at halting the spread of the virus.
- The extent to which economic scarring impacts the UK long-term recovery.
- The pace at which businesses adjust to new trading arrangements and regulations when trading with the EU.
- The outcome of the UK-US trade negotiations.

To reflect the range of likely outcomes across these various factors, we have designed two illustrative scenarios that capture the extent to which an early inoculation programme supports the resumption of normal activity in the economy, businesses adapt to the new UK-EU trade relationship and possible economic scarring.

**Under the 'quick recovery' scenario, we assume the following:**

- While the Christmas period and new variants could see hospital admissions subsequently rise in January, a fast vaccine roll-out and a March-style national lockdown could see R falling below one by spring and ensure the pandemic is kept under control over the course of the year. We assume that the tiered local lockdown system remains in place until at least the spring of 2021, with the number of regions in higher alert levels gradually decreasing. Details of our epidemiological scenarios are illustrated in Figure 1.4.
- There is limited long-term economic scarring, as various government support schemes assist the recovery of the economy as a whole and the labour market in particular.
- Under this scenario, we assume that most businesses are well prepared for the end of the transition period and adapt quickly to the new arrangements.
- The UK-US trade negotiations go smoothly under the new administration.
- Under this scenario, we expect that UK GDP would recover to its pre-pandemic levels by Q1 2023.

**Under the 'slow recovery' scenario we assume the following:**

- The Christmas period and the new variants drive up the hospital admission rate for COVID cases in the new year. Combined with a gradual vaccination programme, this results in the hospital admission rate remaining high and more regions entering higher tier alert levels over 2021. There is a possibility of a third peak of infection, but at a smaller scale and easier to control, resulting in a tightened tiered system until at least summer.
- Long term economic scarring is partially managed by various Government support schemes, but scarring remains significant especially in the labour market.
- Under this scenario, we assume that businesses take time to adapt to the new arrangements.
- The UK-US trade negotiations progress slowly but smoothly.
- UK GDP is assumed to recover much more slowly compared to the 'quick recovery' scenario, and will not reach the pre-pandemic levels until the middle of 2024.

In both scenarios, we assume a mass vaccination campaign during the first half of 2021, but this varies in speed and effectiveness. Generally, we expect the early inoculation programme to boost business and consumer confidence in the short run, supporting the UK's recovery in the new year. However, the effect may be short-lasting, as adjustment from the end of the transition period, weak global economic performance and possible economic scarring take their toll.

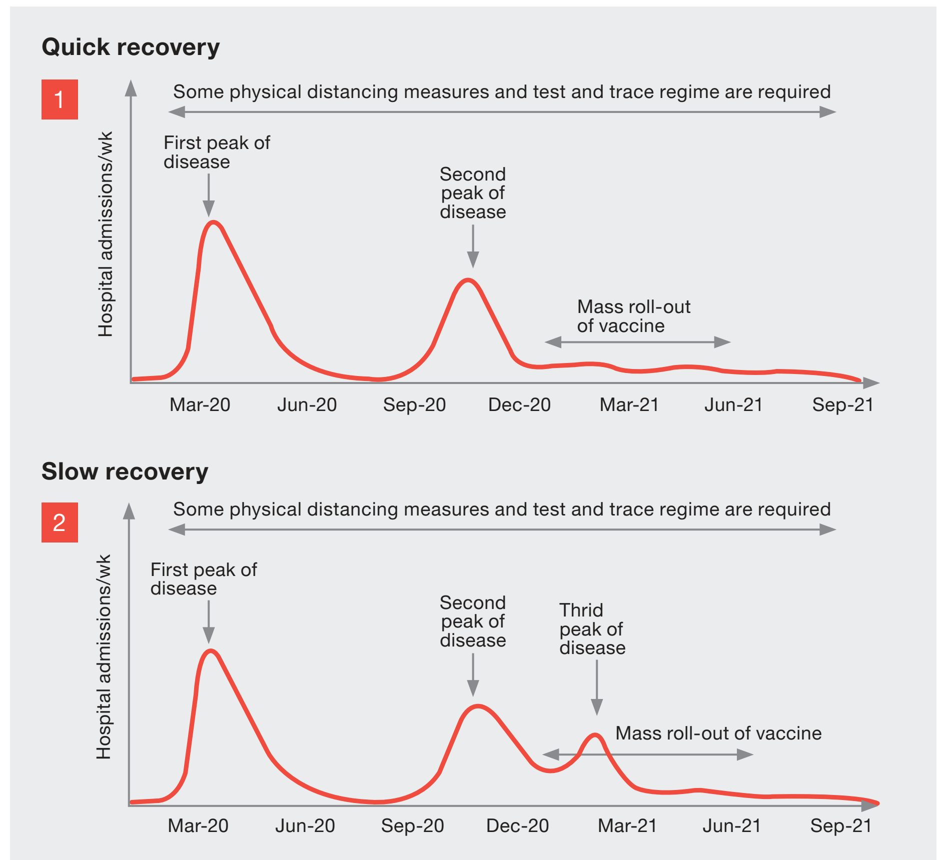
### Monthly GDP profile

We provide projections of GDP growth for the first three months of the year. Our projections have been developed using a hybrid approach, which uses our Nowcasting model, as well as other techniques, and varies by scenario. Beyond March, we provide quarterly projections.

Using our Nowcasting model, we expect UK GDP to drop by between 5.3% and 6.3% in January 2021. In real terms, this means the level of GDP is slightly below the November mark as the country enters its third national lockdown. However, we expect less disruption than during the March lockdown with businesses are better prepared and more safety measures are in place. Breaking down our nowcast by sector, we see that the construction sector is expected to grow the strongest in January. The service sector is expected to contribute the most (75%) to the January growth rate, mainly due to its size (it accounts for almost 80% of the economy).

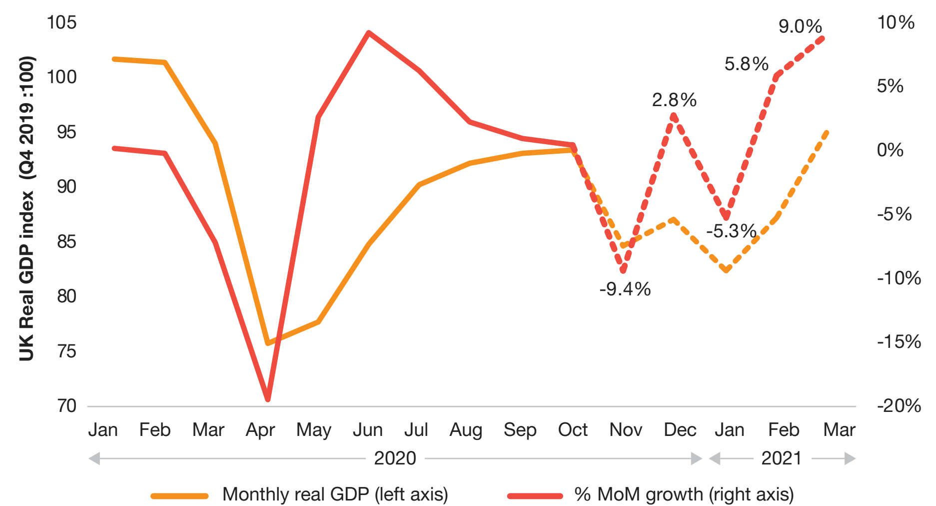
From February, we expect the economy to start recover from its low base, which sees February recovers to about the December 2020 levels. Within our quick recovery scenario, month on month growth in February is 5.8% and 9.0% in March, as the vaccine provides a boost to confidence, investment and activity. Under our slow recovery scenario, month on month growth in February is 5.7% and 8.9% in March, as businesses struggle to adapt to new UK-EU trading arrangements and tight restrictions to contain the pandemic remain in place.

**Figure 1.4: Epidemiological scenarios**




Source: PwC analysis

**Figure 1.5: UK Monthly Real GDP under the 'quick recovery' scenario (Q4 2019 = 100)**




Source: PwC analysis

## Quarterly GDP profile

In terms of our short to medium-term view, our quarterly GDP projections up until the end of 2023 show a 'W-shaped' recovery for the UK, with the second lockdown period being the second dip (see Figure 1.6).

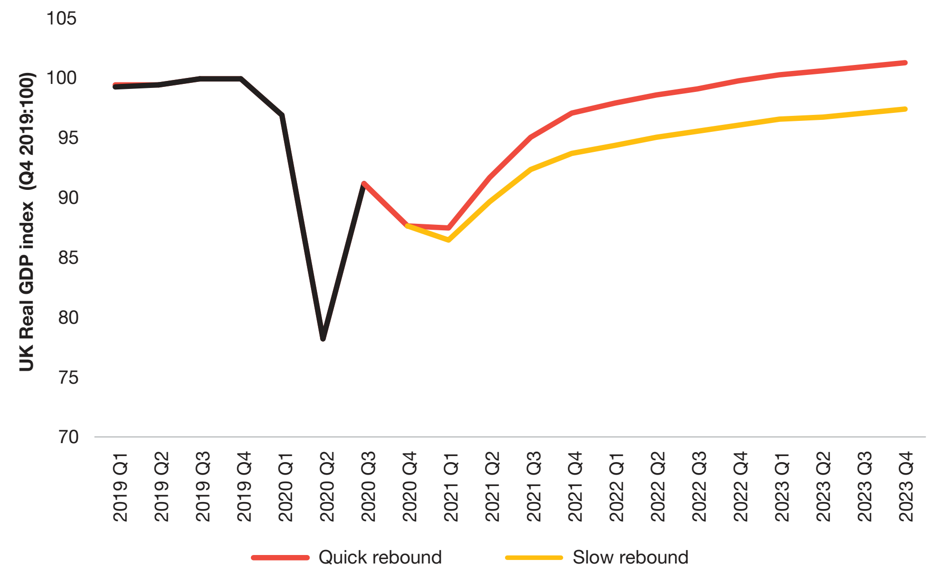
Under the 'slow recovery' and 'quick recovery' scenarios, the expected annual GDP growth rates range from around 2.2% to 4.8% in 2021. This means that most of the output loss caused by the first national lockdown would be recovered by the end of 2021 under the 'quick recovery' scenario and by the middle of 2023 under the slow recovery' scenario. The economy is expected to continue this trajectory, accelerating to around 5.1% to 6.3% in 2022 before slowing down to about 1.7% and 2.0% in 2023 as the UK economy begins to return to its pre-pandemic long-term growth trend.

Our expectation is that the economy won't recover to the pre-crisis levels until Q1 2023 under the 'quick recovery' scenario, and by the middle of 2024 under the 'slow recovery' scenario. These are two quarters slower than our previous forecasts made in November, due to the outcome of the UK-EU new trade agreements which would see additional NTMs being in place, the possibility of a lockdown extension and long-term economic scarring which overshadow the earlier-than-expected inoculation programme.

We have, therefore, revised down our projections for 2021 from between 3.4% and 6.0% under the 'slow recovery' and 'quick recovery' scenarios to between 2.2% and 4.8% to reflect their potential impact on the economic outlook in the medium term. These projections are broadly in line with other third-party projections (see Figure 1.7).

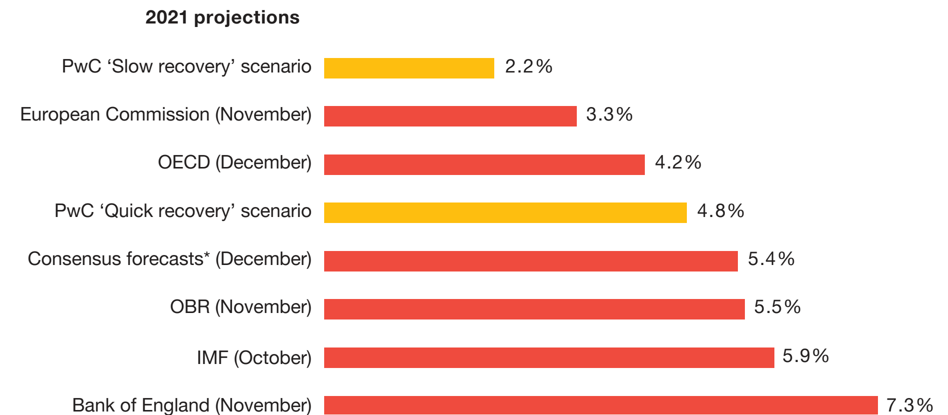
There will likely be some variation in the recovery in 2021 across regions in the UK, driven by the tougher local lockdown system. Regions in the North, the Midlands and London could remain the highest level alert systems into the new year if the Christmas and the new variants results in an uptick in COVID cases. This will restrain growth and hold back the recovery.

**Figure 1.6: UK Real GDP index (Q4 2019 = 100), quarterly levels in each scenario**




Source: PwC analysis

**Figure 1.7: Comparison of GDP growth projections, 2021**




(*): HMT comparison of independent forecasts (December 2020) – average of new forecasts made in last month

Sources: PwC, EC, OECD, HMT, OBR, IMF, BoE

## Sectoral outlook

We anticipate that the second and the third national lockdowns will be less disruptive to the economy than the first. The retail and hospitality sectors are again expected to be hit the hardest, with them being expected to contract in the fourth quarter of 2020 by -18.6% and -5.4%, respectively. Meanwhile, other sectors that were almost entirely shut down in the first lockdown have been able to continue operating at close to normal levels throughout the second lockdown, as a result of precautions made to improve customer and employee safety in the months following the first lockdown.

This includes sectors such as construction, which Boris Johnson confirmed was able to remain open during the second lockdown, where remote working is largely impossible.
This sector is expected to grow by 8.5% in the fourth quarter of 2020, compared to a contraction of -35.8% in the second quarter of 2020 when the first lockdown hit.

The outlook for 2021 is more positive, with most sectors expected to return to growth, except at different rates under the 'quick recovery' scenario. The hardest hit sectors, such as hospitality and transport, are projected to recover strongly, up from their low base in 2020.

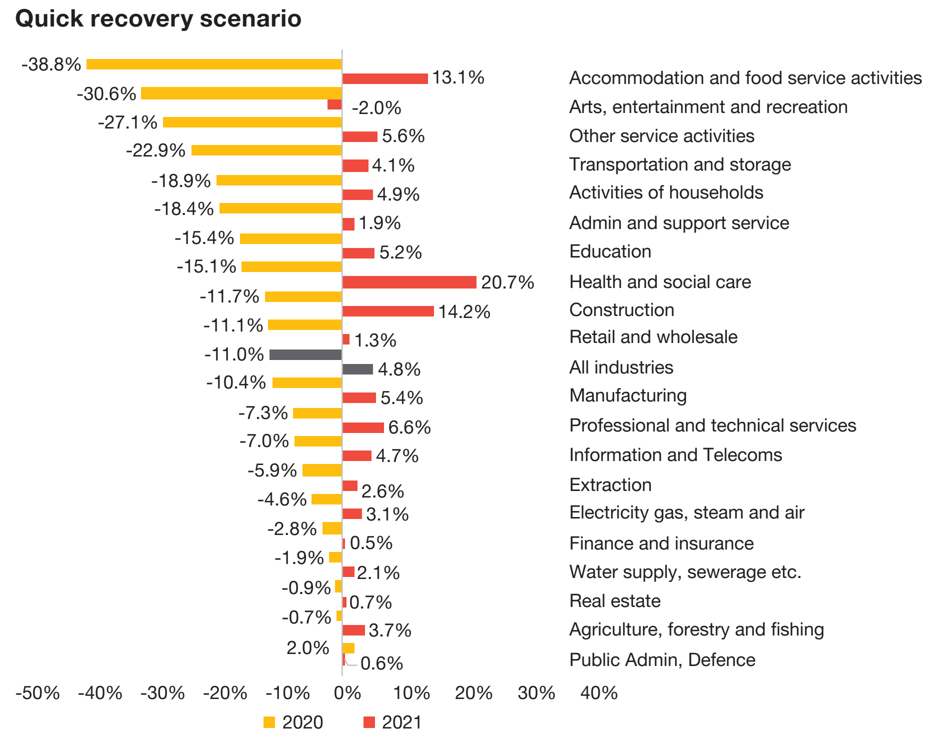
A fast mass rollout of the vaccine would front-load much of this recovery, with a loosening of social distancing restrictions in the first few months of 2021 allowing consumers to return to shops, pubs and restaurants across the country. Buoyed by the vaccine rollout, the health sector is also expected to grow strongly, as the sector attempts to vaccinate tens of millions of people against coronavirus in a matter of months.

Under the 'slow recovery' scenario, most sectors are still expected to grow in 2021 but their recovery is hampered by the extension of social distancing restrictions, due to a slower vaccine rollout, as well as businesses being slow to adapt to the end of the transition period. Under this scenario, we expect that the manufacturing sector will contract in the first quarter of 2021, as a result of the tightening of social distancing restrictions, before returning to growth towards the back-end of the year. Similarly, the recovery of the hospitality sector is halted, as more regions enter higher tier alert levels that limit the ability of the sector to fully reopen. Increased uncertainty over the severity and duration of lockdowns across different regions, with the regional tiers being reviewed every 14 weeks, will constrain business investment and innovation, which will have negative effects on future productivity growth.

Further to this, challenges in adapting to new trading arrangements with the EU would have an adverse impact on most sectors at the beginning of 2021. For production and manufacturing, no tariffs or quotas on goods under the new trading arrangements would likely to support exports and imports while additional red tape would challenge growth in the seemingly-better-prepared services sector. We expect that this would cause the financial services (FS) sector to contract in the first quarter of 2021, as UK-based FS firms lose access to the EU 'Passport', reducing their ability to trade cross-border[4]. However, this initial negative impact of Brexit will be tempered by adaptations made by businesses over the course of the year, as well as the gradual rollout of the vaccine, which enables social distancing restrictions to come to an end towards the end of the year.

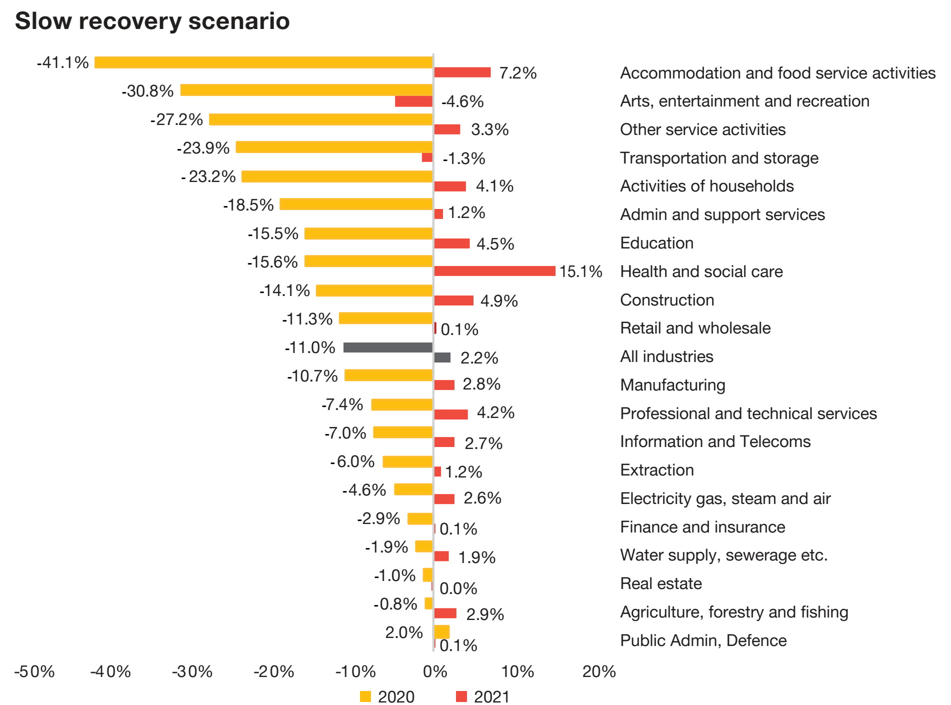
**Figure 1.8: Projected GVA growth rate by industry sector, % annual change in 2020 and 2021**

### Quick recovery scenario




Source: PwC analysis

### Slow recovery scenario




Source: PwC analysis

[4] For detail analysis of the impact of losing passporting rights on the UK and EU financial services sector, please see 'Leaving the EU: Implications for the UK financial services sector – **link** and Impact of loss mutual market access in financial services across the EU27 and UK – **link**

## 1.3 Outlook for inflation

The COVID-19 pandemic has exacerbated the downward trend in UK consumer price inflation (CPI). The combination of weak demand, excess capacity in the economy and suppressed wage growth have contributed to downward price pressure. Inflation began to pick up in July as shops and restaurants reopened, but quickly reversed in August due to the discounts on offer from the Eat Out to Help Out scheme and the VAT cut in the hospitality sector.

In the latest data, the 12-month CPI rate for November showed that consumer prices grew by 0.3%, a deceleration from 0.7% in October. The figures reflect the second national lockdown in England, which restricted activity and subdued demand for things like fuel and clothing. The largest drop in prices came from clothing and footwear as retailers discounted products for Black Friday.

We expect inflation to pick up in 2021, as the effects of spare capacity and weak demand unwind. As economic activity and consumer demand pick up, it will feed through to an increase in prices. As a result, CPI is expected to gradually increase. The end of the transition period with the EU will also create upward pressure on domestic prices, as the cost of imports from the EU raises prices. We expect Brexit to result in an 10% increase in food prices. We expect that inflation could average around 1.4-1.5% in 2021.

However, as set out in the preceding section, there are still considerable uncertainties regarding the path to recovery. Consumer confidence is to some extent dependent on their perception of health risks, which will in turn influence the level of household spending.

**Figure 1.9: CPIH and CPI, % change from previous year**

Source: ONS

A resurgence of cases following the Christmas period, combined with concerns of job security when the furlough scheme comes to an end in April, could make consumers less willing to spend and instead hold more precautionary savings. The uncertainty regarding the labour market, subsequent waves of the virus, and the end of the UK-EU transition period are all factors which risk keeping confidence and demand restrained into the first half of 2021, putting downward pressure on domestic prices.

On the other hand, while consumers may restrain their spending on non-essential goods and services, they will still spend money on food. And this is where some of the biggest effects of Brexit may be felt in terms of higher prices. This means that there is the potential for the upside risks to inflation to outweigh the downside, depending on how businesses respond to the new trading arrangements.

It is likely that monetary policy will remain accommodative at the start of the new year, as the Bank of England faces little pressure to raise rates with low inflation. This was more recently confirmed by the Bank of England's decision in December to keep the Bank Rate at 0.1% and maintain its existing bond purchasing programme.

# 2. Our predictions for 2021

## Summary of key points

1. **There could be fewer babies born in 2021 than in any year since records began.** We expect the health, social and economic effects of the pandemic to result in a 'baby bust', where the postponement of pregnancies during the pandemic translates into a dramatic decline in birth rates.

2. **London's population is expected to decline for the first time in the 21st century.** COVID-19 has fundamentally changed the way we view cities. We anticipate that in 2021, a shift away from city-living is likely to both increase the number of people moving out of the capital, and decrease the number of people moving in.

3. **Net migration with the EU could turn negative in 2021.** We expect that within the year, the number of EU nationals who leave the UK could be more than those who settle. This will be driven by the end of the transition period, and the disproportionate impact of COVID-19 on the sectors where EU migrants are highly represented.

4. **The UK's unemployment rate is expected to record its largest ever quarterly increase in Q2.** Despite tentative signs of an economic recovery in 2021, we expect to see the unemployment rate jump by a record 2.5 percentage points in the second quarter, as the government's furlough scheme comes to an end.

5. **Over 10m people could experience food poverty of some kind.** We expect that existing inequalities will be worsened by rising food prices, which could increase by as much as 10%, as well by projected increases in unemployment.

6. **Gender and ethnicity pay gaps are expected to increase in 2021, potentially reversing a decade of progress on the former.** We expect that the economic impact of the pandemic will be felt disproportionately by women and people from BAME backgrounds, as they are overrepresented in the sectors that have been most affected by social distancing restrictions.

7. **One in eight cars newly registered in Great Britain are likely to be electric or hybrid.** With the transport sector accounting for a third of all carbon dioxide emissions, the UK will have to transition away from petrol and diesel cars if it is to meet its target of net zero emissions by 2050. Following years of progress, the UK has the potential to see 1 in 8 new cars be electric or hybrid in 2021.

8. **By the end of 2021, the majority of electricity generated in the UK could be from renewable sources.** If it is to meet its net zero targets, the UK will need to transition away from fossil fuels and towards renewable energy sources. In the same year it is hosting the COP26, the UK could reach this historic milestone, showcasing its progress on the green agenda.

## Our predictions for 2021

2020 has been an unprecedented year. No one could have predicted the events that transpired and their impacts on the economy. As we enter the new year, there still are a considerable number of uncertainties. At the time of writing, the UK's future trading relationship with the EU remains undetermined, as does the possible UK-US trade deal. And of course, the UK could see a resurgence of the pandemic following the Christmas period.

But there is also a light at the end of the tunnel. The earlier than expected rollout of the UK's vaccination programme means that we expect the pandemic to be brought under control in 2021 and economic activity to return to some normality over the course of the year. The UK will host COP26, the UN's Climate Change Conference, in November, which should help to accelerate global efforts to move towards a sustainable future. And the Tokyo Olympics in August will bring the world together and provide a boost to morale across the globe.

In this section, we present our predictions for 2021. They reflect the short-term, and in some cases the long-term, implications of the COVID-19 pandemic on the economy, on the labour market and on society. They also reflect the expected impact of other major policy developments – namely, Brexit – and trends in the UK's sustainability agenda.

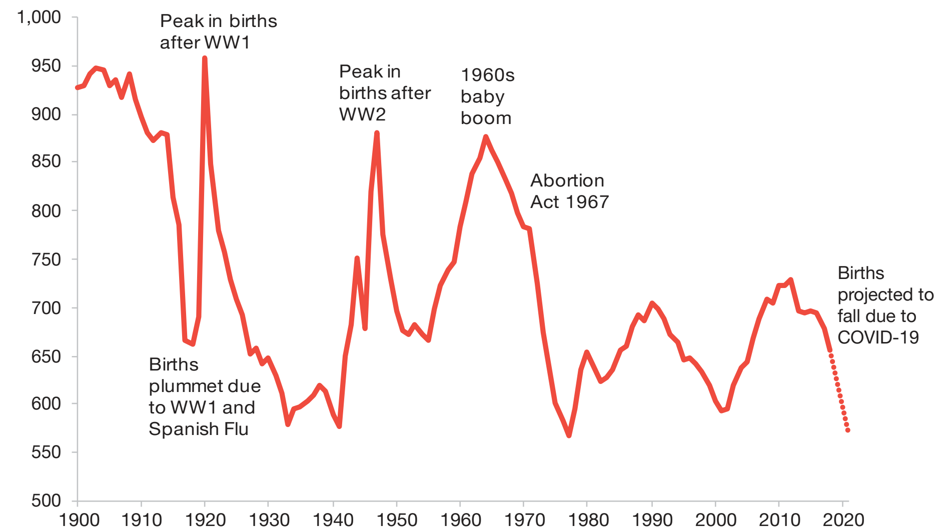
**There could be fewer babies born in 2021 than in any year since records began**

The COVID-19 pandemic has had a profound impact on our lives and plans for the future. For many individuals, it has significantly impacted the decision of whether or not to have a baby. Indeed, a survey conducted in April 2020 found that, of those who planned to have a child in January, 58% had decided to postpone pregnancy, while a further 19% had abandoned plans.[5]

There are many factors which influence a decision to have a baby. Job and income security play a big role. The unprecedented nature and size of the economic shock, as well as uncertainty regarding the duration and extent of government furlough support, will negatively impact family planning. Back in April 2020, 42% of people thought their household finances would get worse in the coming 12 months.[6] Nine months later, we expect that this will translate into fewer births in 2021. These uncertainties are likely to continue into 2021; in a recent PwC survey, 19% of respondents stated that they expect to lose their job in the next 12 months.[7]

Health concerns also play a role. While research has now confirmed the health risks of COVID-19 to pregnant women and newborn babies are low, anxieties will inevitably exist. Concerns over access to healthcare and GP services, as well as restrictions on partners being present at births may also have a negative impact on pregnancies.

**Figure 2.1: Live births, 1900-2021 (000's, projections from 2019)**




Source: ONS, PwC analysis

[5] Luppi, F., Arpino, B., & A. Rosina, The impact of COVID-19 on fertility plans in Italy, Germany, France, Spain and UK, May 2020 – **link**

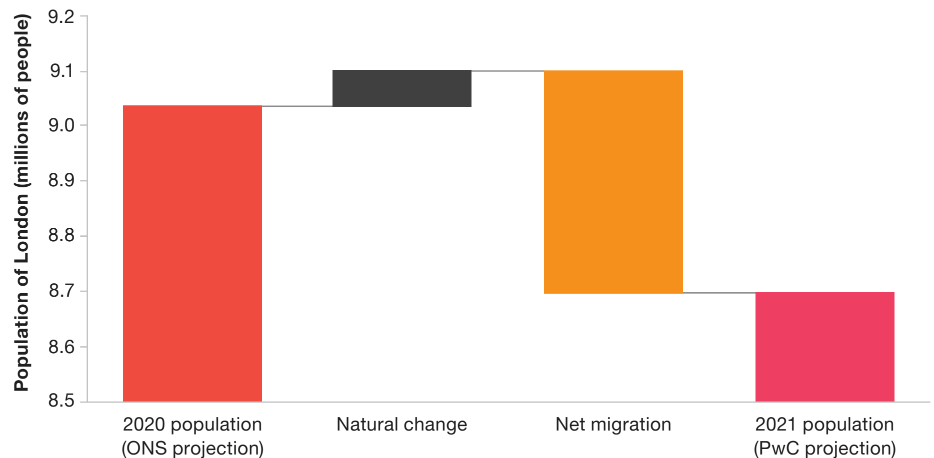
[6] ONS – Coronavirus and the social impacts on Great Britain – **link**

[7] PwC's QuantiBus is a weekly consumer survey in which we talk to 1,000 participants aged 18+ and is nationally representative by gender, age and region. Survey conducted w/c 7th December

The pandemic is also having an impact in other ways. IVF treatments have been delayed. 71% of UK weddings have been postponed, which may alter plans to start a family.[8] And it's not just the postponement of planned pregnancies – lockdown measures have prevented people from seeing their partners. According to a survey by YouGov, 45% of people who dated before the pandemic have stopped dating completely.[9] This reduces opportunities for unplanned pregnancies, which account for around a third of UK births.[10]

The combination of these factors could result in a 'baby bust' in 2021, where the annual birth rate in the UK has the potential to fall to its lowest level since records began. For some women, births will not just be delayed, but they will have a lower total number of children over their lifetime. A structural decline to the birth rate will depend on the level of scarring in the labour market and the pace of recovery. A longer recovery will reduce peoples' expectations of their lifetime income, which could result in women deciding to have fewer children. The effects of lower births won't be felt for decades. But if the pandemic causes a permanent decline in births, the long-term challenges associated with the UK's ageing population could be brought forward.

**Figure 2.2: Population of London ('000,000s) based on London Assembly survey results, projections from 2020**




Sources: PwC analysis, ONS, Public Health England, London Assembly

Notes: This includes excess death projections for 2021 based on data from Public Health England and the Institute for Health Metrics and Evaluation, University of Washington.

**London's population is expected to decline for the first time in the 21st century**

COVID-19 has fundamentally changed the way we view cities. City-dwellers are now rethinking their living situations in light of the pandemic, and re-evaluating the importance of larger homes, green spaces, and connections with the local community. We anticipate that in 2021, this shift away from city-living will mean that London's population could decline for the first time in the 21st century.

In an August 2020 survey conducted by the London Assembly, 4.5% of Londoners – or 416,000 people – responded that they would definitely move out of the city within the next 12 months.[11] Pre-COVID, the ONS predicted that London's population would grow by 56,000 people between 2020 and 2021. It would require just 14% of these respondents to actually move in 2021 to break even with this projection.

We also expect that we may see a decline in the number of graduates that arrive in the capital in 2021. Of graduates who move away from the city where they studied, more than 20% typically work in London within six months of graduation.[12] Primarily driven by job opportunities, this pattern of graduate migration may be disrupted in 2021 as jobs are harder to find. Especially as remote working becomes more prevalent – living in London may no longer be seen as a necessity for finding high-skilled, high-paid jobs.

Beyond COVID-19, migration out of London may also be influenced by wider concerns around the UK's economic and political standing. 16% of UK residents surveyed in November 2020 reported they would consider moving out of the UK some time within the next 12 months.[13] Among those considering to move, the main reasons cited were concerns about the UK economy (59%) and Brexit (53%).

[8] Hitched, New Study: 71% of Couples Are Postponing Their Wedding Due to COVID-19, October 2020 – **link**

[9] YouGov, Sex and dating under COVID-19, June 2020 – **link**

[10] Public Health England, Health matters: reproductive health and pregnancy planning, June 2018 – **link**

[11] London Assembly, Half of Londoners wanting to move home want out of London, August 2020 – **link**

[11] Centre for Cities, The Great British Brain Drain, November 2016 – **link**

[12] ONS, Coronavirus and the social impacts on Great Britain, 6 and 13 November 2020 – **link**

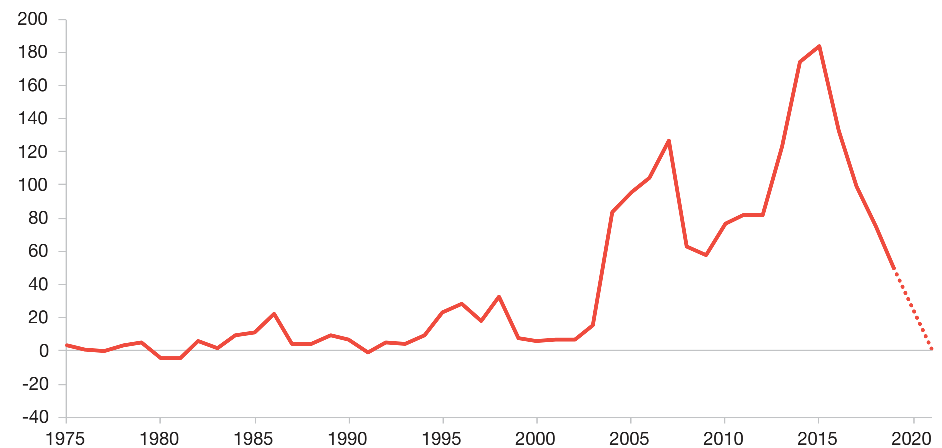
**Net migration with the EU could turn negative in 2021**

In 2019, net migration of EU citizens to the UK fell to 50,000 people, down from a peak of 184,000 in 2015.[14] In 2021, net migration with the EU has the potential to fall even further and potentially turn negative – meaning that within the year, the number of EU nationals who leave the UK could be more than those who settle. If so, this would be the first instance of negative annual net migration with the EU since its formal establishment in 1993.

COVID-19 and the end of the Brexit transition period will be the key drivers of this shift. The pandemic has disproportionately impacted sectors in which EU migrants are strongly represented, such as hospitality and transport.[15] Jobs will become harder to find and keep, discouraging migration that is enabled by, or for the purpose of, work in these sectors.

The end of the transition period also means that EU citizens currently residing in the UK will need to apply for settled or pre-settled status by the end of June 2021 in order to continue residence. Of the 3.8 million people eligible, around 200,000 have yet to be granted either status – 126,000 of which have yet to apply.[16] If at least a quarter of this group does not obtain leave to remain, that would be enough to turn net migration negative at today's rates of emigration and immigration – even without taking into account the potential effects of COVID-19.

**Figure 2.3: Net migration to the UK by EU citizens (thousands of people), projections from 2020**




Sources: ONS, PwC analysis

Fewer EU nationals entering the UK's workforce – and more leaving – is likely to exacerbate growing skills and occupation shortages. For example, there is a significant shortage of nurses in the UK, with an estimated 50,000 nursing vacancies in the UK's NHS alone.[17]
In January 2020, the EU accounted for 6% of all nurses, equivalent to 19,300 nurses in the NHS.[18] Nurses are the only health staff group to record a fall in the number of EU nationals since the 2016 EU referendum. If net migration with this group continues to fall, the occupational shortage could widen.

[14] ONS, Provisional long-term international migration estimates, August 2020 – **link**

[15] The Migration Observatory, Migrants in the UK Labour Market: An Overview, 2019 – **link**

[16] UK Parliament, The progress of the EU Settlement Scheme so far, April 2020 – **link**

[17] Royal College of Nursing, Staff safety at risk unless nursing shortages are addressed, September 2020 – **link**

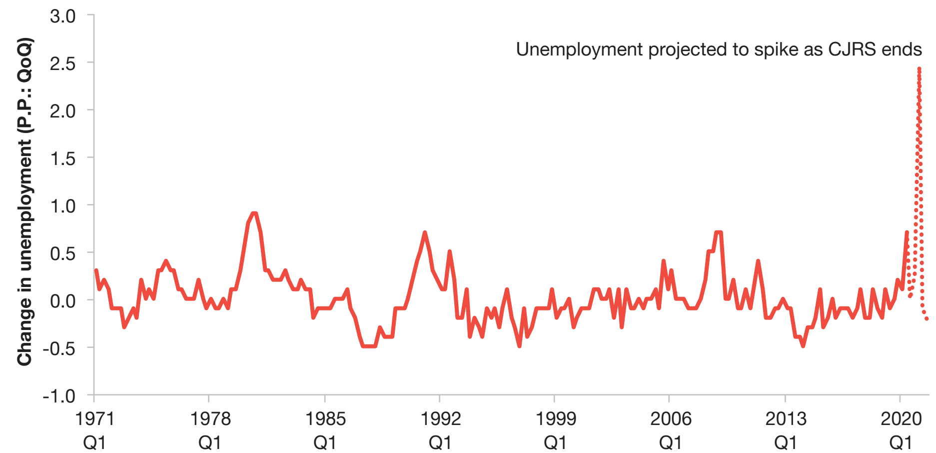
[18] UK Parliament, NHS staff from overseas: statistics, June 2020 – **link**

### The UK's unemployment rate is expected to record its largest ever quarterly increase in Q2

Unemployment is expected to soar in the wake of the government's Coronavirus Job Retention Scheme (CJRS) coming to an end next spring. The Office for Budget Responsibility (OBR) projects that the unemployment rate will increase by 2.5 percentage points between the first and second quarter of 2021.[19] This is more than twice the size of any other recorded change in the unemployment rate, with the second highest increase taking place in the early 1980s, at 0.9 percentage points (see Figure 2.4). This sharp increase will bring the unemployment rate to a peak of 7.5% in the second quarter of 2021. Equivalent to 2.6 million unemployed, this is a level that has not been reached since the aftermath of the 2008 financial crisis.

At present, there are around 2 million private sector workers that are still on furlough – we expect that many of these workers will not be able to return to their jobs once the furlough scheme comes to an end. This is largely because the scheme is coming to an end before demand returns to pre-COVID levels, with real GDP growth in Q2 2021 expected to be 8.8% below its pre-crisis trend in our 'quick recovery' scenario. Further to this, some jobs in the sectors hardest hit by the pandemic, such as hospitality and retail, are expected to be permanently lost. The government will need to support their transition to new roles with a focus on training and reskilling.

**Figure 2.4: Unemployment rate (p.p., quarter-on-quarter change, seasonally adjusted), projections from Q4 2020**




Sources: OBR, PwC analysis

Note: CJRS refers to the Coronavirus Job Retention Scheme

### Over 10m people could experience food poverty of some kind

COVID-19 is exacerbating inequalities. While higher income households have increased their savings by 5-15% as they postpone spending on recreation, lower income households have seen a decrease in their savings by 10-15% as earnings have fallen.[20] A consequence of the disproportionate impacts on lower income households has been a rise in food poverty. Historically, food poverty in the UK has been high compared to other European countries, especially for children.[21] Food banks saw unprecedented uptake in 2020, with the UK's two largest food bank networks reporting increases in need of 89% and 107% in April 2020 compared to the previous year.[22] Half of the people who used food banks in that month had never needed one before.

In 2021, two additional factors will be at play. Brexit could lead to an increase in food prices. The UK's exit from the single market is expected to raise the price of imports from some of the UK's key trade partners. We expect Brexit could increase food prices by around 10% in 2021. In general, we expect inflation to pick up this year, as the effects of spare capacity and weak demand unwind. At the same time, rising unemployment will lead to millions more people relying on government support for their income.

These combined effects on the food and labour markets could have a stark impact on the prevalence of food poverty in the UK. We expect that in 2021, over 10 million adults in Britain could struggle to put meals on the table – up from the 9.8 million already experiencing some kind of food insecurity in 2018.[23]

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[19] OBR, Economic and fiscal outlook, November 2020 – **link**

[20] Bank of England, How has Covid affected household savings?, November 2020 – **link**

[21] BMJ, Food insecurity in UK is among worst in Europe, especially for children, says committee, January 2019 – **link**

[22] The Trussell Trust, UK food banks report busiest month ever, as coalition urgently calls for funding to get money into people's pockets quickly during pandemic, 2020 – **link**

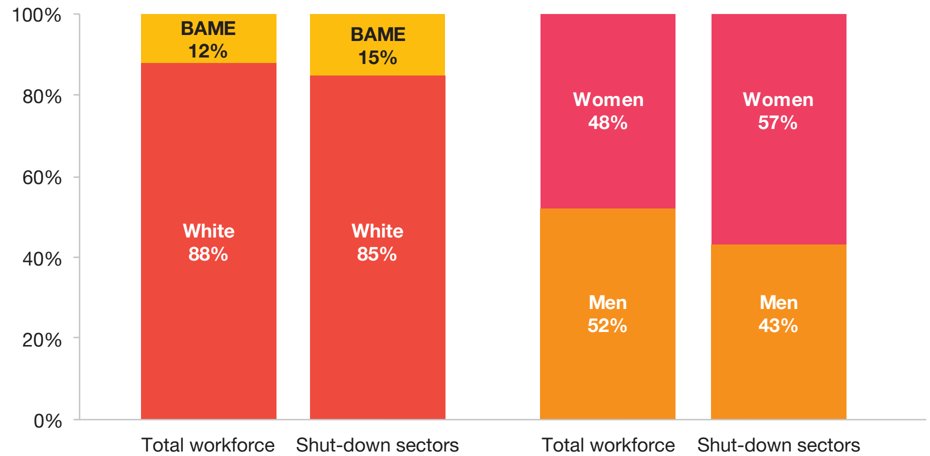
[23] Food Standards Agency, The Food and You Survey, 2019 – **link**

**Gender and ethnicity pay gaps are expected to increase in 2021, potentially reversing a decade of progress on the former**

The impacts of the pandemic have been felt disproportionately by women. Despite only making up 48% of the workforce, they account for 57% of employees in shutdown sectors. This is reflected in the greater share of women in total furloughed employees. In August 2020, there were 10% more women than men receiving Coronavirus Job Retention Scheme (CJRS) support. Indeed, a survey by the IFS and UCL revealed that mothers were 47% more likely than fathers to have permanently lost their job or quit, and 14% more likely to have been furloughed.[24] The government's public sector pay freeze will also disproportionately impact women, who account for two-thirds of the public sector.

The UK's gender pay gap has been steadily declining for decades, from 26% in 2000, to 19% in 2010 and to 16% in 2019.[25] However, there is evidence to suggest that this trend could be reversed in 2021. This is borne out in the survey data – 28% of women told us that their pay had decreased as a result of the pandemic, compared to 22% of men.[26] These disparities will only worsen when the CJRS comes to an end in April, which will disproportionately impact women as unemployment shoots up.

**Figure 2.5: Share of workforce by demographic (%)**




Source: House of Commons Library

These disparities have likely been worsened by the government's decision to exempt companies from filing gender pay data in 2019/20. As a result, only half did. This prevents the full impact of the pandemic on gender disparities from being known, reduces pressure on companies to take decisive action, and limits wide scale progress. Looking further ahead, there are hopes that a shift towards flexible working patterns will enable women and men to take a more equal role in childcare responsibilities, which may translate into a more equal playing field in terms of employment and pay.

In contrast to the gender pay gap, there is little evidence to suggest that the ethnicity pay gap has narrowed in recent decades.[27] We expect that the COVID-19 pandemic will only worsen these disparities. Despite only making up 12% of the workforce, BAME workers account for 15% of employees in shutdown sectors (see Figure 2.5). And in April 2020, people from BAME backgrounds were almost twice as likely as white Britons to report having lost income and jobs since the pandemic began.[28]

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[24] UCL, Parents, especially mothers, paying heavy price for lockdown, May 2020 – **link**

[25] OECD – Gender wage gap at the median. The gender pay gap is defined as the difference in gross median hourly earnings between men and women

[26] PwC's QuantiBus is a weekly consumer survey in which we talk to 1,000 participants aged 18+ and is nationally representative by gender, age and region. The survey was conducted on the week of the 14th December 2020

[27] A Bank of England study found that the ethnicity pay gap – defined as the difference in gross median hourly earnings between the 'White' ethnic group and the 'ethnic minority' ethnic group – has fluctuated between 2.5% and 7.5% over the past 20 years

[28] BMG poll for the Independent

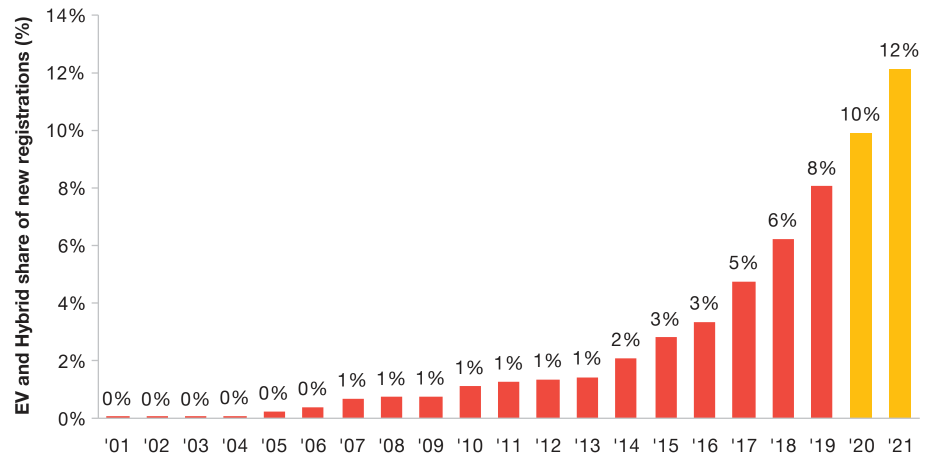
### One in eight cars newly registered in Great Britain are likely to be electric or hybrid

In 2019, the UK parliament passed legislation requiring the government to bring all greenhouse gas emissions to net zero by 2050. With the transport sector accounting for a third of all carbon dioxide emissions, the transition away from petrol and diesel cars will be critical. To this end, the UK government recently announced a ban on the sale of petrol and diesel cars from 2030.

Over the past decade, developments in battery technology and reductions in their cost have driven demand for electric vehicles. Average battery energy density – the amount of energy stored in each battery per unit volume – is currently increasing at around 4-5% per year. Further to this, over the past decade, the price of lithium-ion batteries has fallen by 87% globally.[29] As electric vehicles have become cheaper, the share of all cars registered in the UK that are electric or hybrid has risen from around 1% in 2010 to 8.0% in 2019 (see Figure 2.6).[30] Projections by Bloomberg suggest that electric vehicles will reach price parity with equivalent petrol or diesel cars by the mid-2020s.

Charging infrastructure also plays a big role in purchase decisions. In 2020, the UK government announced its Rapid Charge infrastructure plans, which include a vision to have at least 6 charge points at every motorway service area in England by 2023. These investments will encourage purchases.

**Figure 2.6: Share of all cars sold in Great Britain that are hybrid of electric (%), projections from 2020**




Source: ONS, PwC analysis

In a recent PwC survey, 29% of respondents indicated that they would consider buying an electric or hybrid car in the next three years.[31] In 2021, car sales are likely to be boosted by the pent up demand that has accumulated over the year as consumers have delayed purchases. We expect that one in every eight cars that are newly registered in 2021 could be electric or hybrid.

However, it should be noted that the emissions from the use of electric vehicles can only be as clean as the power supply that is used to charge them. This means that, in order for the government to achieve its net zero targets, the UK will also need to increase the renewable share of electricity generation. The UK's progress on this front is considered in our next prediction.

[29] BloombergNEF, Electric Vehicle Outlook, 2020 – **link**

[30] Figures presented are for GB as UK data is only available from 2015. However, the picture in the UK is similar – in 2019, 8% of all cars registered in the UK were electric or hybrid.

[31] PwC's QuantiBus is a weekly consumer survey in which we talk to 1,000 participants aged 18+ and is nationally representative by gender, age and region. The survey was conducted on the week of the 14th December 2020.

**By the end of 2021, the majority of electricity generated in the UK could be from renewable sources**

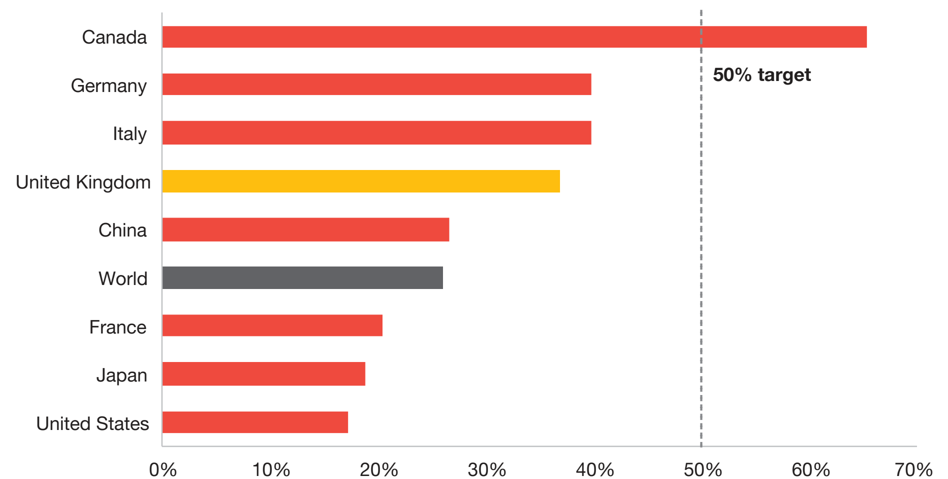
If the UK government is to achieve its net zero targets by 2050, the country will have to transition away from its reliance on fossil fuels and towards renewable sources of energy, such as wind and solar.[31] In recent years, sharp falls in the cost of renewable energy sources have rapidly increased the renewable share of electricity generated. If recent trends prevail, the UK has the potential to reach an important milestone in 2021 – by the end of the year, more than half of all electricity generated could be from renewable sources.

The share of electricity generation from renewables has increased eight-fold over the past decade. In the first quarter of 2020, 48% of all electricity generated was from renewable sources, up from 6% in the first quarter of 2010. This has been accompanied by equivalent falls in greenhouse gas emissions from electricity generation, which in 2019 were 72% lower than their 1990 levels. These trends have been driven by falls in the cost of renewable energy, particularly in wind. In 2019, the price of offshore wind was almost a third of that in 2015, falling from £120/MWh to around £40/MWh.[32]

The UK's progress on this front has made it one of the global leaders in decarbonisation. In 2019, 37% of electricity generated in the UK was from renewable sources, compared to a global renewable share of 26% (see Figure 2.7). By contrast, over the same period, only 17% of electricity generated in the US was from renewable sources, reflecting the country's continued reliance on gas and coal.

Over the coming decades, electricity is expected to account for an increasing share of our energy use, as we use it to heat our homes and power our cars. Recent analysis by BEIS even suggests that total electricity demand could double by 2050. Reaching this milestone in 2021 could act as a strong signal to businesses and households to more effectively engage with the green agenda.

**Figure 2.7: Share of electricity generation from renewables, 2019**




Sources: Our World in Data, BP

[32] Renewable energies include tidal, offshore wind, onshore wind, solar PV, hydro and bioenergy. It does not include nuclear energy – though this is a low-carbon energy source

[33] This is the offshore wind prices in renewable Contracts for Difference auctions (BEIS, 2020)

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