

Northern Bank Quarterly Economic Overview Q3 2011



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Summary of Quarter 3 2011 and economic outlook:

Global: Quarter 3 was probably the most challenging period so far this year for the global economic environment. Markets continued to look for a resolution to the Euro crisis but politicians in Europe procrastinated until things came to a head in early August when global markets experienced a temporary meltdown. By September there was still no resolve with debt and demonstrations dominating the economic landscape in many advanced economies. A degree of relief to the Quarter 3 problems only arrived in October by way of the Euro Summit (Oct 26th) when agreement was finally reached on recapitalisation for European banks, a 50 percent haircut for Greek bond holders and there was agreement that the European Financial Stability Fund should be boosted.

In the US GDP data was strong in Quarter 3, with a reading of 2.5% (seasonally adjusted annual rate) - a notable improvement from 1.3% in Quarter 2 and only 0.4 percent in Quarter 1. There was better-than-expected private consumption data in September (increasing by 2.4 percent) and US retail sales surprised positively in the same month. The overall signals in the latest quarter suggest that the US is not heading for a new recession, although the economy still faces major headwinds. For example, the US housing market is far from recovered and the government is still running a deficit of 10 percent.

In Asia, the Chinese economy saw weaker than expected Quarter 3 growth (at 6.7% qoq); the Chinese economy saw a notable improvement at the end of quarter and the expectation is for a much stronger performance in Quarter 4 of roughly 8.5% qoq. In Japan however there are some signs that the recovery is losing some steam. The Bank of Japan recently expanded its Quantitative Easing programme driven by fear that the appreciating yen would derail the recovery.

Quarter 3 also took its toll on Emerging Markets (EM) and a number of EM central banks (Brazil, Turkey, Russia and Poland) took pre-emptive measures to add liquidity to foreign exchange markets to reduce overall volatility. However, the overall recovery trend appears to be intact in emerging economies despite the significant slowdown in global activity levels. Policy makers will without doubt remain on stand-by as they observe the impact of the Euro summit on world markets in the months ahead.

United Kingdom:

Provisional results from the Office of National Statistics estimate that the UK economy grew by a mere 0.5 percent in Quarter 3. During the quarter, unemployment hit 8.1 percent, the highest rate since 1996 and inflation continued to head upwards (and is

expected to peak in the last quarter of the year]. Despite the fact that negligible growth is expected in Quarter 4; it is anticipated that the UK will experience solid growth in medium term (2013-2015). The medium-term outlook holds not only substantial upside potential for both private consumption and retail sales but also for investments and industrial production. Without doubt the UK has been scarred by the 2008-09 crisis, but it should be remembered that the country is still in relatively good shape compared with the average EU country.

[Northern Ireland:](#)

Undeniably the global economic upheaval during the summer months had an impact upon local confidence and investment levels during Quarter 3. The local unemployment rate rose to 7.6 percent in the three months to August and households felt a further strain coming from high energy and food prices. Confidence levels dipped again in September with local households indicating that their spending would continue to decline and a full 41 percent of those surveyed anticipated that their financial position would get worse in the year ahead. With disposable incomes squeezed, the local retail sector continued to experience very tough trading conditions. The latest Northern Bank/Oxford Economics quarterly forecast report suggests that the local economy remained largely stagnant during quarter 3. However political efforts to resolve the European debt crisis in October have the potential to improve sentiment levels locally for both households and investors. In addition, if inflation decreases rapidly in the first half of 2012, real wage growth should turn positive towards the end of next year and the local economy should see a rebound in private consumption levels in the medium term.

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Chief Economist

Nov 1 2011

Table 1: Economic Summary		2009	2010	2011
Output	Northern Ireland GVA growth Annual Growth	-3.8%	1.1%	0.9%
	National annual GDP growth Annual growth	-4.6%	1.7%	1.2%
Employment rate [June-Aug]		748,000 64.0%	778,000 66.3%	799,000 67.3%
Unemployment	ILO rate [June-Aug]	56,000 7.0%	58,000 7.0%	65,000 7.6%
	Claimant count [Sept]	53,200 6.0%	57,900 6.5%	60,900 6.9%
Inflation [CPI Q3] (y/y change)		1.5%	3.1%	4.7%
Interest Rate [Bank of England official rate March]		0.5%	0.5%	0.5%

1. Gross output estimates

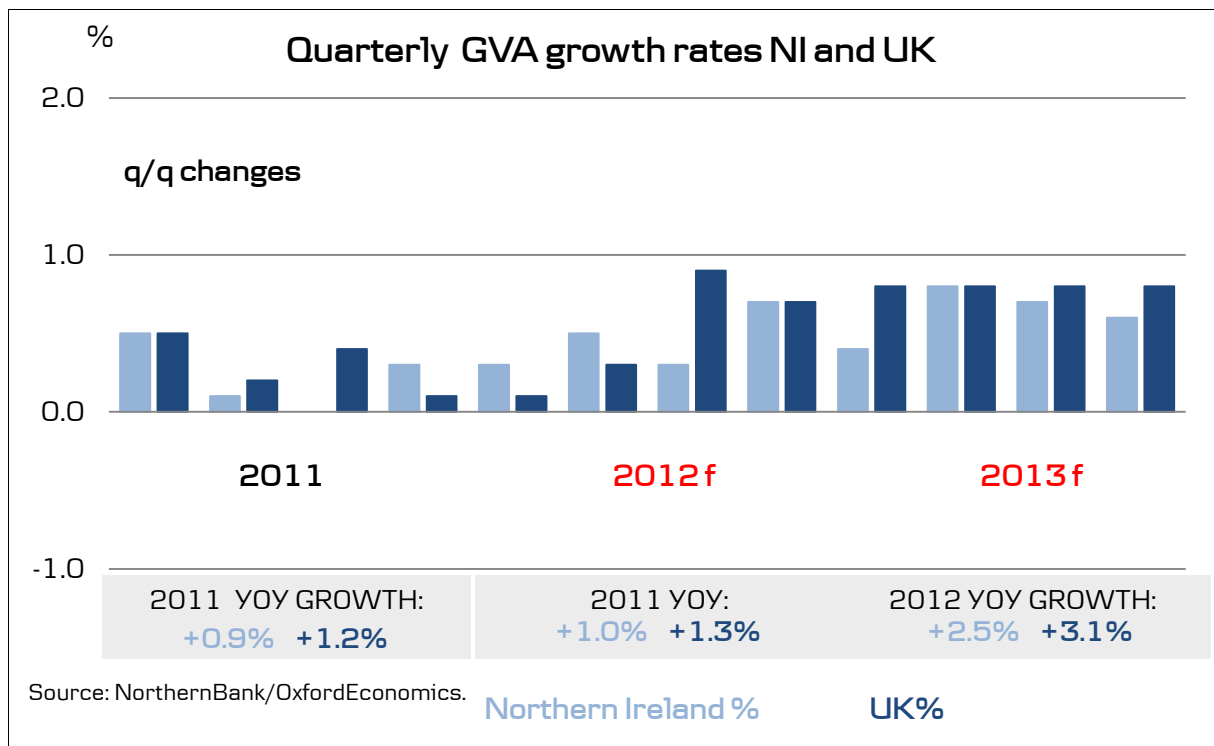
GDP United Kingdom

Provisional data from the Office for National Statistics (ONS) show that the UK economy grew by 0.5% in the Quarter 3 2011, following growth of only 0.1% in the previous quarter. The latest Oxford Economics / Northern Bank, Sectoral Forecast report estimates that the annual growth rate for the UK economy in Quarter 3 2011 was 0.4 percent over the quarter and annual growth in 2011 is estimated at 1.2 percent.

Economic Growth forecast for Northern Ireland

The Northern Bank/Oxford Economics Quarterly Sectoral Forecast report (October 2011) estimates that the local economy experienced no growth in during Quarter 3 and will grow by a mere 0.9 percent over 2011 [see *Figure 1*].

Figure 1.
Oxford Economics Q3 estimates and forecast of GVA growth in Northern Ireland and UK. (2011 - 2013).



N.B.: Data for Northern Ireland output are available in the form of GVA (Gross value added), where GDP = GVA + Taxes - Subsidies on products (the latter two items are available only at a national level).

2. Labour market

Employment

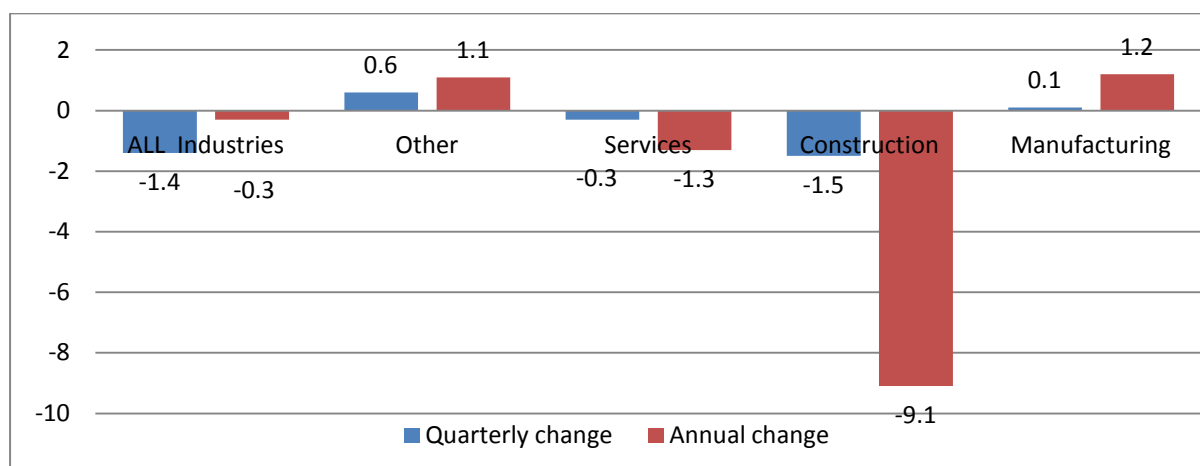
The latest *Monthly Labour Market Report* from the Northern Ireland Statistics & Research Agency (NISRA) shows that the number of people in employment in Northern Ireland during the three-month period June to August 2011 was estimated to be 799,000, equal to 67.3% of people aged 16-64. This represented an decrease of 3,000 over the quarter and 21,000 over the year.

The Northern Ireland employment rate (67.3%) remained lower than the UK average (70.4%) and was the second joint lowest of the twelve UK regions.

Sectoral employment data (published in October) for the March to June 2011 period showed that the local manufacturing sector employed 70 more people over the quarter and a further increase 110 people were reported to be working in the “Other Industries” sector. The Construction and Services sectors saw quarterly employment contractions of 500 and 1,520 respectively.

Over the year manufacturing sector employment rose by 1.2%, while construction employment shrank by 9.1 percent. [see *Figure 2*].

Figure 2.
Employee jobs in Northern Ireland: Annual and quarterly changes by industry.
(June 2011).



Vacancies

The level of unfilled vacancies reported to the Department of Enterprise Trade and Investment (DETI) in the period ending 5th August 2011 was 3,457, a decrease of 12 per cent relative to the same period last year, when vacancies stood at 3,910.

Labour Market Inactivity

The seasonally adjusted number of economically inactive persons (who are of working age) in Northern Ireland in the period June-August 2011 was estimated at 312,000. The Department of Finance and Personnel noted that 40 percent were male (124,000) and 60 percent were female (188,000).

The working-age economic inactivity rate for Northern Ireland stands at 27%, significantly higher than the UK average (23.3%) and the second highest of the twelve UK regions.

Unemployment

- **Claimant Count (September 2011)**

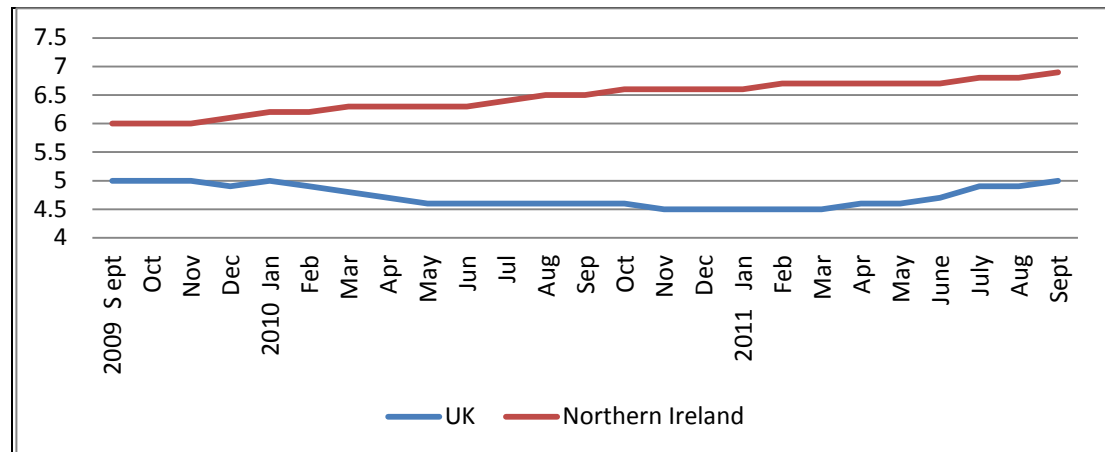
NISRA has reported that the seasonally adjusted claimant count in NI increased by 500 over the month of September 2011, it now stands at 60,900. The local claimant count rate was 6.9% of the workforce up 0.4 points over the year, representing an increase of 3,000 people. [see *Table 2*].

In the UK, the claimant count rose by 17,500 in the month of September 2011 and now sits at 1.6 million. The UK claimant count rate in September stood at 5.0%, up by 0.4 percentage points from a year earlier.

	Level Sep-10	Monthly change (level)	Annual change (level)	Rate % Sep-11	Rate % Sep-10
Northern Ireland	60,900	500	3,000	6.90%	6.50%
UK	1,600,000	17,500	129,200	5.00%	4.60%

Source: ONS

Figure 3. :Claimant count rate in Northern Ireland and UK (Sept 2009 - Sept 2011).



Source: DFP and ONS Labour Market Statistics, various issues

- ILO Quarterly Unemployment Rate (March-May 2011)

The International Labour Organisation (ILO) seasonally adjusted unemployment rate for Northern Ireland was 7.6% in the three-month period June to August 2011. This represents a rise of 0.5 percentage point over the quarter and 0.6 percentage points over the year. [see [Table 3](#)].

The Northern Ireland ILO unemployment level was estimated to be 65,000 in June to August 2011, this was up 4,000 over the quarter and up 7,000 over the year.

The ILO unemployment rate for the UK was higher at 8.1% in the same period. The number of jobseekers at the national level fell by 26,000 over the quarter to reach 2.45 million.

	Level June-August 2011	Quarterly change (level)	Annual change (level)	Rate % June-August 2011	Rate % June-Aug 2010
Northern Ireland	65,000	+4,000	+7,000	7.6%	7.0%
UK	2,570,000	+114,000	+113,000	8.1%	7.8%

See [Figure 4](#) below for the long-term trend in quarterly unemployment rates for both Northern Ireland and the UK as a whole.

Figure 4.
Historical unemployment in Northern Ireland and UK (June-August rates 1996-2011)

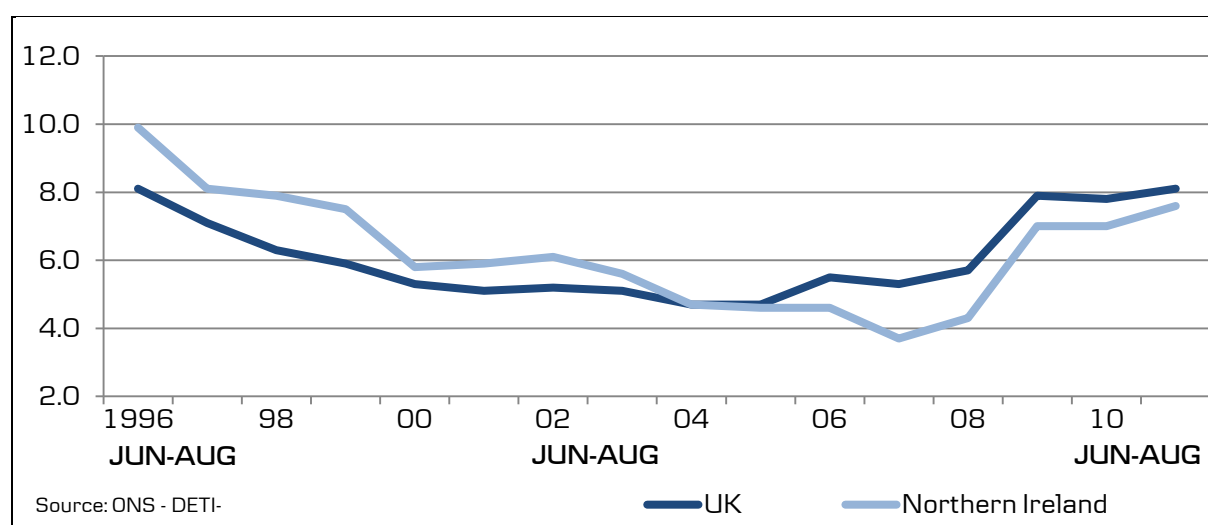
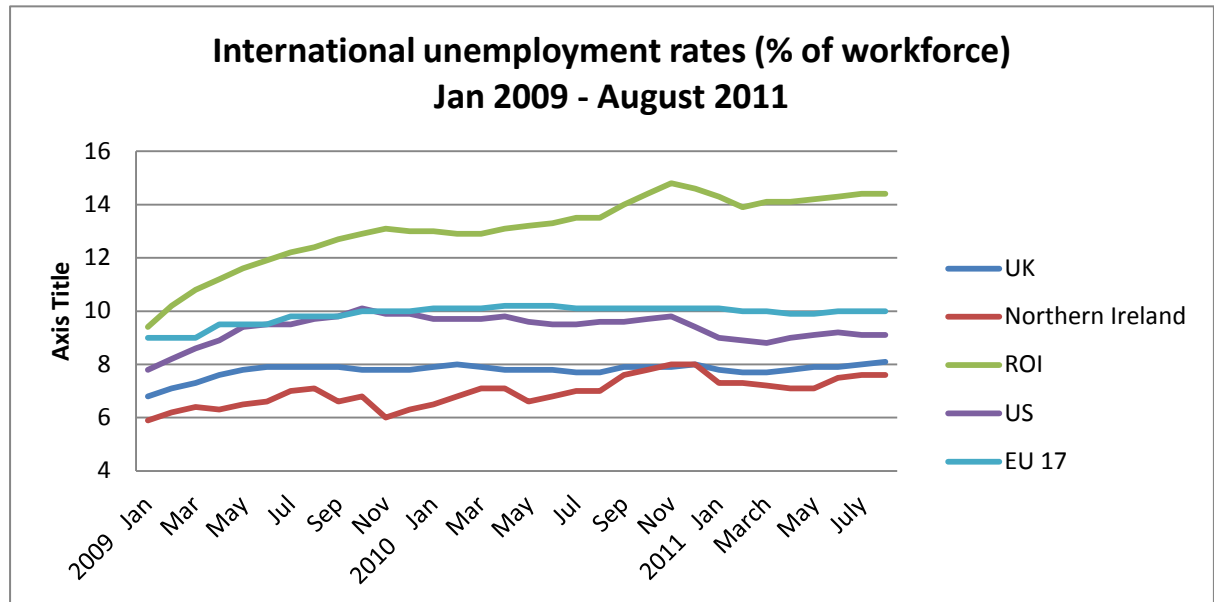


Figure 5 below shows the Northern Ireland and UK monthly ILO unemployment levels from 2008 onwards. Current levels remain well below levels in the USA, Eurozone and the Republic of Ireland.

Figure 5.
ILO Unemployment in Northern Ireland, UK compared to international comparators. (Jan 2008 - August 2011).



Source: Central Statistics Office ROI, ONS UK, DFPNI, Bureau of Labour Market Statistics US and Eurostat (various issues).

Redundancies

The Department of Enterprise, Trade and Investment (DETI) was notified of 65 confirmed redundancies in the month of September, compared with 191 in the same month one year earlier. Quarter 3 saw the Department being notified of 353 confirmed redundancies, which was a fall of nearly 34 percent from the previous quarter. (See Table 4)

There have been a total of 1294 confirmed redundancies from January 2011 to September 2011, a decrease of 26.2% for the same period in the previous year (1,753).

When examined at the District Council level, the majority of redundancies during 2011 have occurred in the Belfast District Council area (640), Newry and Mourne (147) and Derry (135) District Council areas.

Table 4 below shows a breakdown of redundancies by industrial sector during Q3 2011 compared with Q3 2010.

Industrial sector	Q3 2011		Q3 2010	
	number	%	number	%
Manufacturing	21	5.9	164	30.7
Electricity, Gas, Air Conditioning supply	6	1.7		
Water supply, sewerage, waste management				
Construction	10	2.8	44	8.2
Wholesale and Retail Trade	25	7.1	67	12.5
Transport	28	7.9		
Hospitality (Accommodation and Food service)				
Information and Communication	28	7.9	9	1.7
Financials and Insurance	19	5.4	27	5
Real Estate activities	22	6.2		
Professional, scientific and technical activities	21	5.9		
Administrative and support service activities	56	15.9	92	17.2
Public Administration			1	0.2
Education	117	33.1	131	
Health and Social Work	2			24.5
Total	353	100%	535	100%

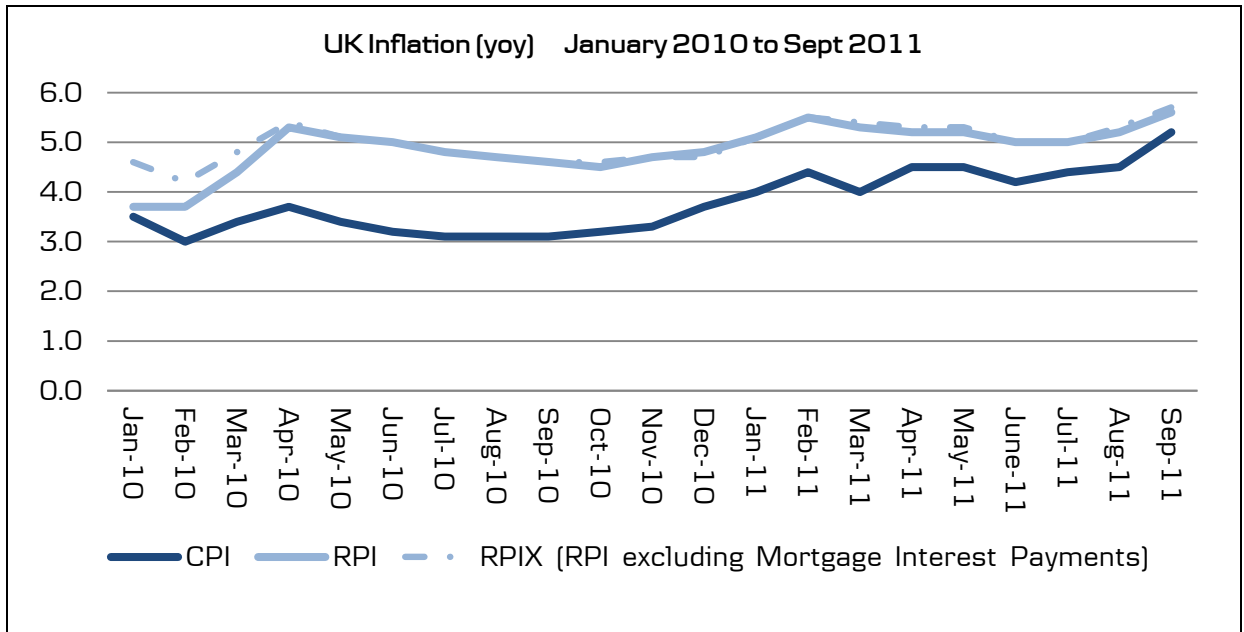
3. Inflation

Consumer price indices

In Quarter 3 2011 UK inflation levels remained well above the Bank of England's target averaging 4.7% y/y, with the September figure sitting at +5.2% [see *Figure 6*]. This compares to the average inflation rate of 3.1 percent in Quarter 3 2010. The elevated inflation rate reflects the temporary impacts of three factors: the increase in VAT to 20%; higher energy prices and higher import costs.

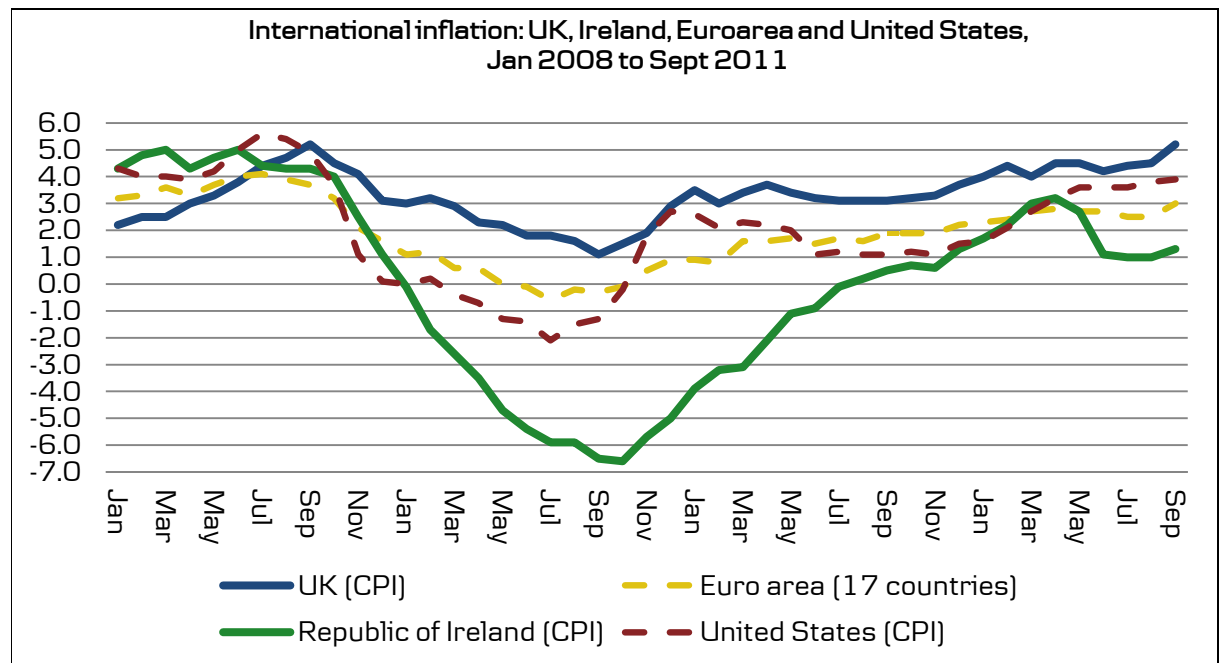
The RPI and RPIX indices (the latter excludes mortgage interest payments) both averaged 5.3% in Q3 2011, - a level similar to the previous quarter. The two indices have both maintained this elevated trend since 2010.

Figure 6.



Source: ONS (Sept 2011)

Figure 7 presents an international comparison of year on year rates of inflation since 2008.

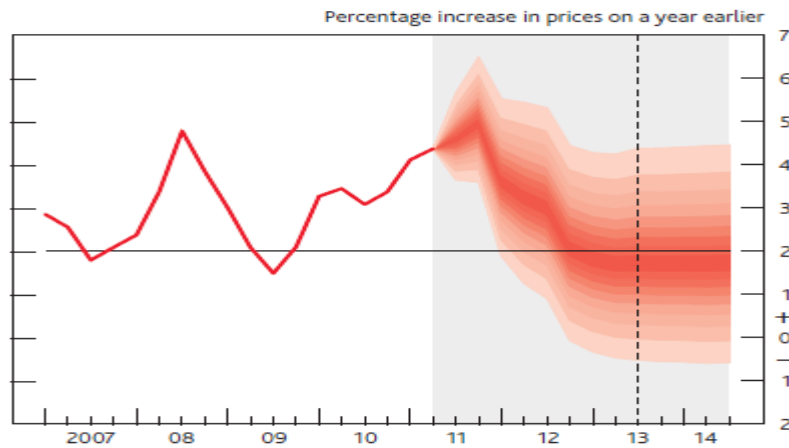


Source: ONS UK, Eurostat, CSO Ireland, US Bureau of Labor Statistics (various issues)

Inflation forecast

According to the Bank of England's *Inflation Report* published in August 2011, UK inflation rate will most probably peak in the last quarter of 2011 and should start to fall back in 2012 as the VAT hike falls out of the year on year comparison and downward pressure from spare capacity persists. The precise timing of that fall is however uncertain. [see *Figure 8*].

Figure 8.
Bank of England inflation projections. (up to Q2 2014).



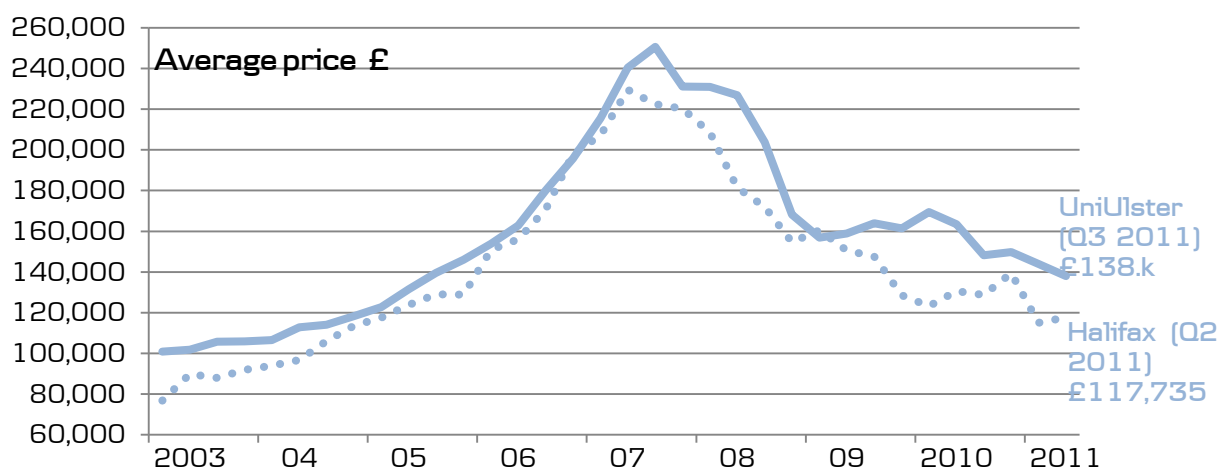
N.B.: BoE projections are made under the assumption of that the Bank Rate moves in line with market rates and the asset purchase programme remains steady at £200 billion.

4. Housing market

Northern Ireland

The University of Ulster Index examined house prices in Northern Ireland during Quarter 2 on the basis of a sample of 1062 open market transactions (compared with only 925 in Q1 2011). The results for the latest quarter show that although activity was up, the average house price in Northern Ireland had fallen to £137,814 (from £143,918 in the previous quarter). The latest price represents a fall of 4.2 percent since Quarter 1 2011, and represents a fall of 15.7 percent from the same period one year earlier.

Figure 9.
Northern Ireland House Price Indices.
(Q1 2003 - Q2 2011).



Source: University of Ulster / Halifax House Price Index

Oxford Economics: House Price Forecast

The Oxford Economics outlook for house price growth in Northern Ireland is shown in *Table 5* below. Due to exceptionally low confidence levels and the weak economic recovery, positive growth is now not expected to return until 2014.

Table 5. Oxford Economics House prices forecast Oct 11 - Growth %.

	2011	12	13	14	15	16	2017
Northern Ireland	-4.8	-4.2	-2.4	+3.4	+6.1	+5.1	+4.2
UK	-1.4	-3.0	-1.0	+4.5	+6.6	+5.5	+4.8

Source: Oxford Economics

United Kingdom

According to the Halifax house price index, house prices at the national level rose in Quarter 3. The marginal rise of 0.1percent from the previous quarter was the first quarterly rise recorded since Q1 2010.

Republic of Ireland

The traditional ESRI House Price Index for the Republic of Ireland has been discontinued and the Central Statistics Office (CSO) in the Republic has now launched a new national Residential Property Price Index. The latest index (published on October 25th) shows that house prices in the RoI continued to fall throughout Quarter 3 and in September 2011, the year on year change was -14.3 percent. House prices in Dublin are now 49 percent lower than their peak level in early 2007. The rest of Ireland has experienced a

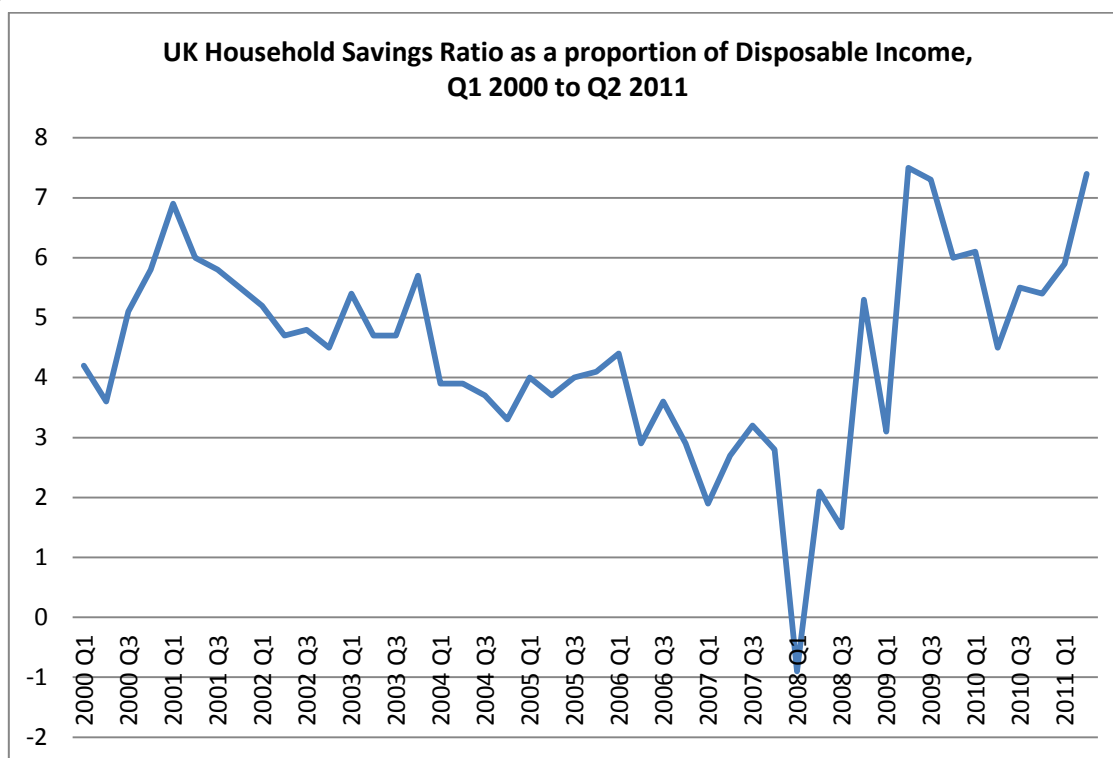
fall of 40 percent from peak. Overall, the national index is 44 percent lower than its highest level in 2007.

5. Households and consumers

Households' resources

According to figures from the Office of National Statistics (published on October 25th), Real Household Disposable Income rose by 1.2% during Quarter 2 2011 following a fall of 1.7% in Q1 [see *Figure 10* below]. The household saving ratio was 7.4 per cent in quarter 2, compared with 5.9 per cent in the previous quarter. The long-term average for the savings ratio is around 5 percent.

Figure 10

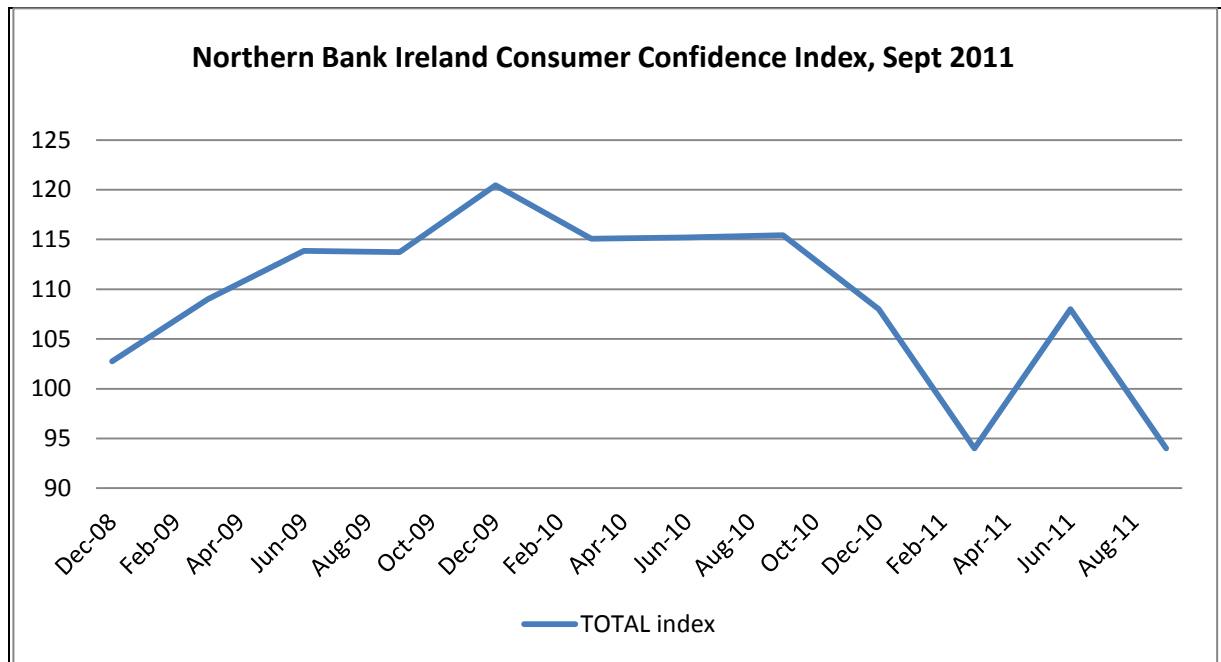


Consumer Confidence

Northern Ireland's Consumer Confidence index fell back to alarmingly low levels during Quarter 3 2011. The survey which was carried out in early September saw overall confidence fall in all aspects of the index bringing sentiment levels back to its historical low point of 94. The latest confidence data revealed that 'expectations for finances in the year ahead' and 'spending expectations' experienced the largest declines. Of the 1,000 people

surveyed, only 9 per cent believed that their household finances would improve, while 41 per cent felt that their financial position would get worse. A total of 47 per cent of households said that their financial position was worse relative to the previous year, up 3 percentage points from the last survey.

Figure 11.
Northern Bank Consumer Confidence Index for Northern Ireland.
(Sep 2008 - Sept 2011).



N.B.: The Northern Bank Consumer Confidence Index is compiled by surveying around 1,000 people in five key areas in Northern Ireland.

UK Consumer Confidence indices (Nationwide and GfK)

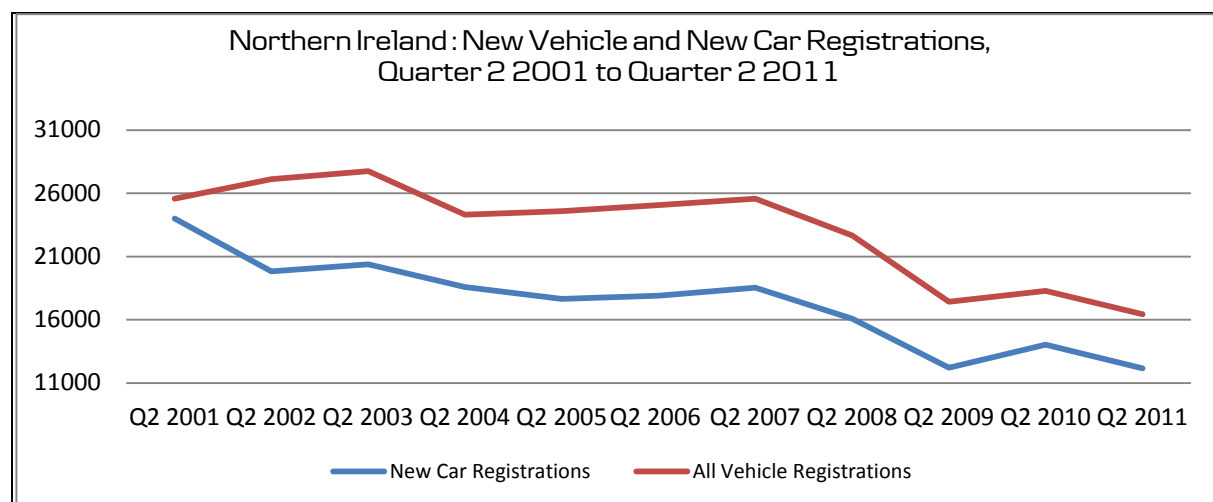
According to the GfK survey, UK consumer confidence levels dropped in September 2011 with the overall index score decreasing to -30. The Nationwide confidence index dipped for the fourth month in a row (to 45 points) in September. The Nationwide Index now sits ten percentage points below where it stood in September last year.

New Vehicle Registrations

Data on new vehicle registrations in Northern Ireland were published by the Department of Regional Development in October. The new figures for Quarter-2 2011 show that 16,440 new *vehicles* were registered - the lowest level for this quarter for ten years. In the same quarter new *car* sales amounted to 12,164 down by 15 percent from the

same period last year and down 16 percent on the ten-year average for Quarter 2 (around 16,700).

Figure 12: New car registrations and all newly purchased vehicle registrations in Northern Ireland. (Quarter 2 period 2001 2011).

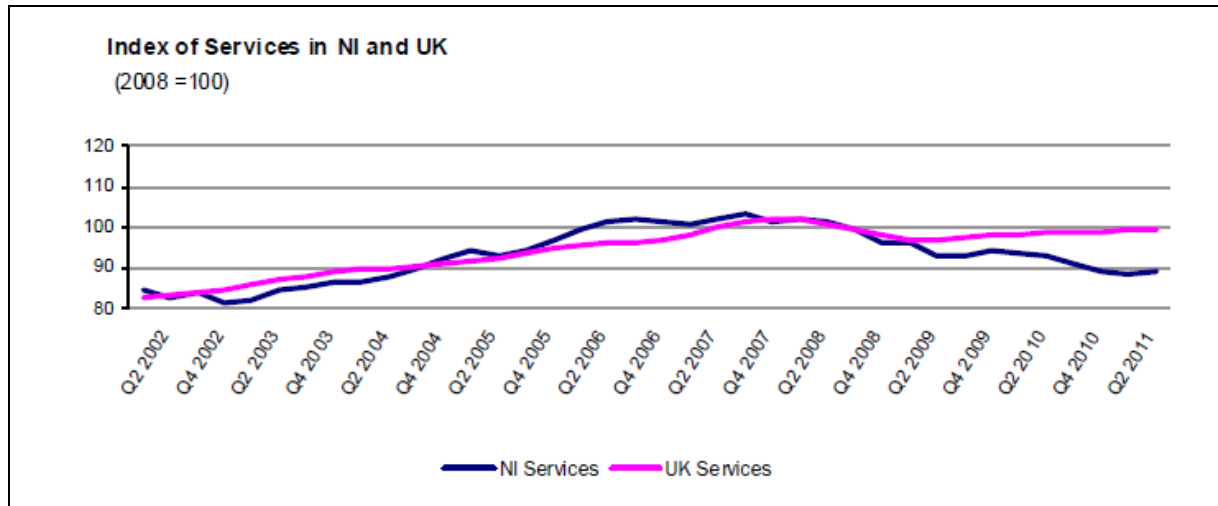


Source: DRDNI, October 2011

6. Business Environment

NI Index of Services Q2 (+0.6%)

The Q2 Index of Services (which draws on a sample of 1,900 companies) released by DFP on October 10th, shows that local output levels in the private service sector rose by 0.6% over the quarter (provisional data). This is the first quarter on quarter growth since Q4 2009. The IOS bulletin reported that growth in 'business services and finance' and in 'transport, storage, information and communication' worked to offset falls in the 'wholesale and retail distribution' and 'accommodation & food service' activities as well as the 'other services' sectors. The local index remains some 13.5 percent below the peak recorded in the third quarter of 2007.



Source: DFP, October 2011

NI Index of Production Q2 [-4.1%]

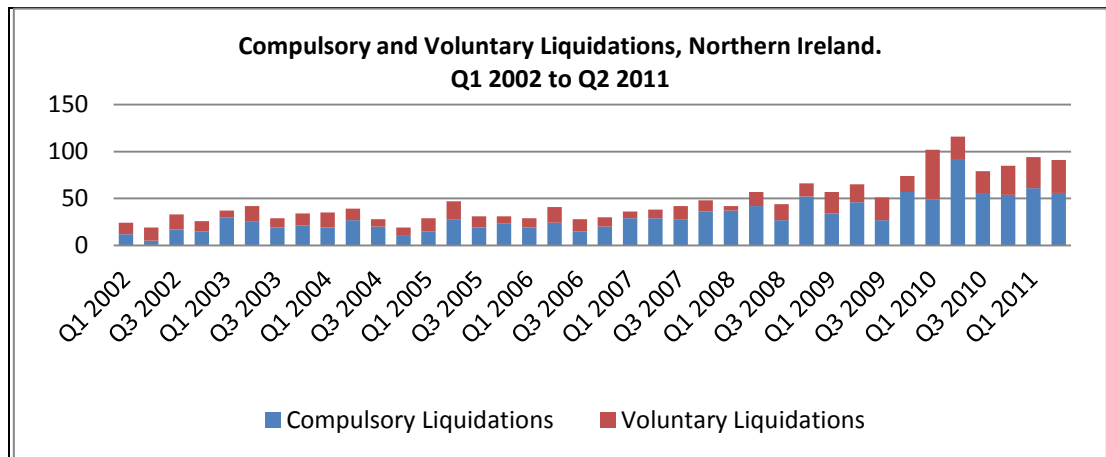
The DETI Index of Production, (published on 12 October 2011) for the second quarter of 2011 shows output levels in Northern Ireland decreased by 4.1% compared to Quarter 1. This compares with a slight decrease [-1.2%] for the UK as a whole over the same period. The NI index remains some 18.9% below the peak recorded in Q4 2007, whilst the UK Index is reported to have fallen by 10.6% in the same period.

Company liquidations Q2

Data from the Insolvency Service of the Department of Enterprise Trade and Investment (DETI) show a total of 91 company liquidations in Northern Ireland in Quarter-2 2011.

Compulsory liquidations decreased marginally in Quarter-2 relative to the previous quarter and voluntary liquidations were marginally up. In terms of total liquidations, the figure for Quarter2, although well above its long-term quarterly average, [see *Figure 13*] was down 21.6% compared with the same period one year earlier.

Figure 13: Company liquidations Northern Ireland. (Quarterly data from 2002 to Q2 2011).



Bank of England: Agents' Summary of Business Conditions.

Annual growth in nominal spending on consumer goods and services had slowed to a very gradual pace.

- Subdued activity in the housing market reflected continued difficulties of first-time buyers to secure a mortgage and households' rising concerns about incomes.
- Investment intentions had softened in recent months. Some capital spending that had been resumed after the recession had now been completed, and some plans had been put on hold because of increased uncertainty about the outlook.
- Manufacturing exports continued to grow steadily, although the Agents' score had fallen back from recent highs, due to less-favourable base effects and a slowing in orders.
- Manufacturing output for the domestic market continued to grow, although the rate of expansion had declined in recent months.
- Business services turnover growth remained modest, with some niche service providers raising fees, and firms in the transport sector passing on higher fuel prices.
- Construction output was broadly flat compared to a year earlier, and slowing public sector orders and early indicators of private sector demand pointed to a contraction in activity over the coming year.
- Employment intentions in the private sector pointed to further growth in employment over the coming year. But the pace of recruitment was expected to slow somewhat, reflecting both past hiring, and downward revisions to the outlook for demand.
- There was reported to be little upward pressure on private sector total labour costs, in part because of employees' rising fears about job security.
- The annual rate of increase in raw materials costs continued to flatten off, but higher energy prices were still feeding through as fixed-term contracts expired.

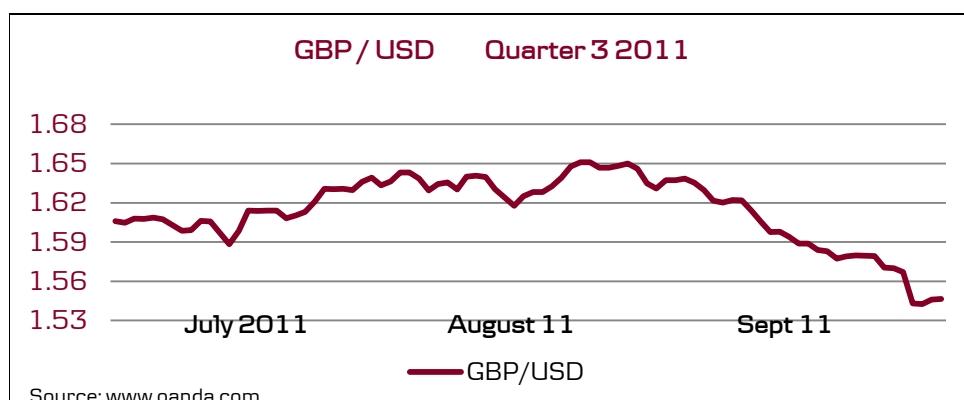
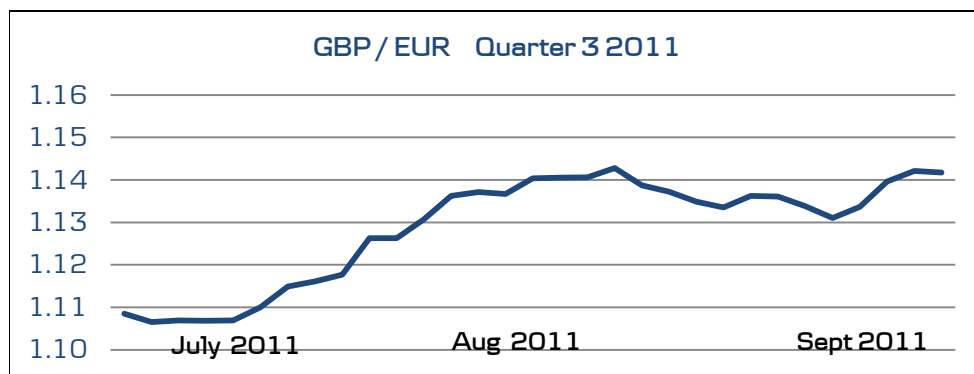
- Increased materials costs combined with higher labour costs in some emerging market countries continued to push up on the price of imports of finished goods.
- The pace of inflation in manufacturing output prices had slowed a little in recent months, while fees for services gradually edged upward.
- Annual inflation in the price of consumer goods and services remained elevated.

Exchange rates and interest rates

Quarter 3 Exchange rates: £/€ and £/\$

Anxiety around the euro crisis was a key driver of £/€ foreign exchange movements during Quarter 3. As the euro crisis peaked in early August we saw some flows into sterling as investors moved away from the more risky single currency (although it should be noted that the overall gains made by sterling were not significant in the Q3 period). Markets calmed in September as a politicians weighed in behind moves to support the euro and sterling's temporary attractiveness declined (but could re-emerge as and when euro debt problems resurface) . During Q3 the pound lost some ground to the dollar as economic data in the two regions diverged (with the States showing improvement and the UK data in Q3 remaining largely unimpressive) a low of 1.54 was reached in late September.

Figure 14.
Exchange rates: GBP/EUR and GBP/USD. (Quarter-3 2011).



Source: www.oanda.com

Interest rates.

The Bank of England Rate is maintained at 0.5% since March 2009 and it is expected to remain at this level until the latter part of 2012 at the earliest. The 3-month LIBOR interbank rate (at which banks borrow funds from each other) averaged 0.87% throughout Quarter-3, whereas the 1 year LIBOR averaged 1.63 %

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