

BRITISH CHAMBERS OF COMMERCE

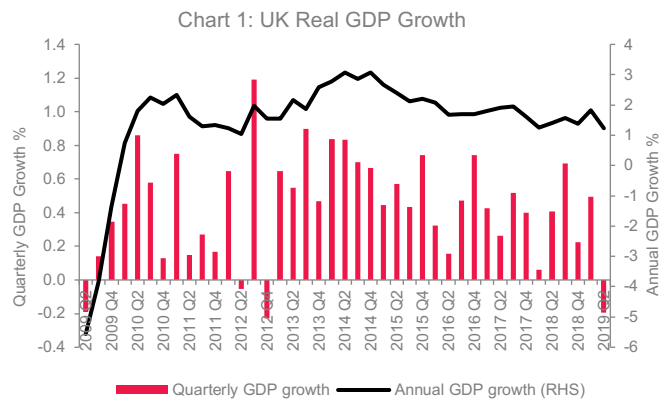
MONTHLY ECONOMIC REVIEW September 2019

Monthly headlines:

- UK economy contracts in Q2 as industrial and construction output falls
- UK employment reaches new record high as productivity falls
- Germany close to recession as US GDP growth is revised down

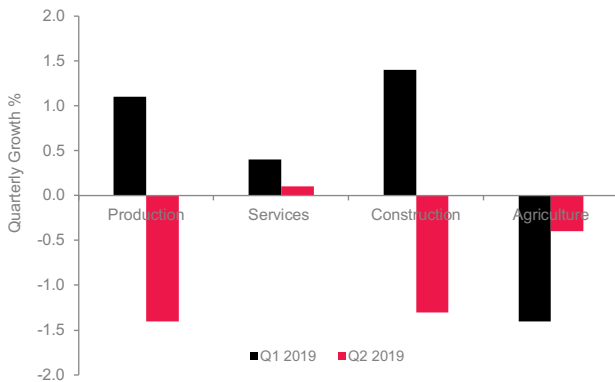
UK economy contracted in Q2...

The UK economy contracted by 0.2% in Q2 2019, the first decline since Q4 2012 and down from growth of 0.5% in Q1 (see Chart 1). In annual terms, the UK economy grew by 1.2% in Q2, the weakest outturn in seven years. Monthly GDP growth was flat in June 2019, down from growth of 0.2% in May. Overall, the latest figures suggest that the unwinding of heightened levels of stockpiling, growing anxiety over the prospect of a no deal exit and moderating global growth is increasingly weighing on economic activity.



Source: ONS UK GDP estimate, June 2019

Chart 2: UK GDP Growth by Sector



Source: ONS UK GDP estimate, June 2019

...as industrial and construction output falls...

The contraction in UK GDP growth in Q2 was largely driven by falling output from the industrial and construction sectors. Industrial sector output fell by 1.4% in Q2 (see Chart 2), with output from the manufacturing sector, which accounts for around 10% of UK economic output, dropping by 2.3% in the quarter. Construction sector output fell by 1.3% in Q2. While the dominant services sector was the only positive contributor to GDP growth in the quarter, growth in services output was still subdued at 0.1%, the weakest growth since Q2 2016.

...and business investment contracts...

The latest UK GDP data also revealed that business investment in the UK fell by 0.5% in Q2 2019, down from growth of 0.4% in Q1 (see Chart 3). Business investment has now fallen in five out of the last six quarters and is further confirmation that it remains a weak point for the UK economy. **Declining business investment is a concern as it limits innovation and productivity, stifling the UK's growth prospects.** In contrast, household spending increased by 0.5% in Q2 2019, boosted by the recent pickup in real wage growth. Government consumption increased by 0.7% in the quarter.

Chart 3 UK Business Investment



Source: ONS UK GDP estimate, June 2019

Chart 4: UK's Net Trade Position



Source: ONS UK Trade, June 2019

...as the UK's trade deficit narrows...

The UK's trade deficit in goods and services narrowed by £16 billion to £4.3 billion in Q2 2019 (see Chart 4). The improvement was driven by a marked decrease in the UK's trade deficit in goods as goods imports declined by 13% in the quarter, which more than offset the 1.5% drop in goods exports over the same period. The improvement in Q2 may well be a one-off with Brexit uncertainty, including the absence of clarity on trade conditions after October 31st, and a slowing global economy likely to increasingly weigh on the UK's net trade position over the medium-term.

...while the UK jobs market remains strong...

In the three months to June 2019, the number of people in employment rose by 115,000 to 32.8 million, a new record high. However, the number of people out of work also increased by 31,000 over the same period. The increase in both UK unemployment and employment was at least partly due to a rise in people looking for work as the UK's economic inactivity rate dropped to 20.7%, a joint-record low (see Chart 5). Average weekly earnings (excluding bonuses) growth increased to 3.9%, the highest rate since 2008. The number of vacancies dropped by 20,000 to 820,000, the sixth successive decline and suggests that demand for labour is moderating.

Chart 5: UK Economic Inactivity Rate



Source: ONS Labour Market Overview, August 2019

Chart 6: UK Productivity (Output per hour worked)



Source: ONS UK Productivity, Q2 2019

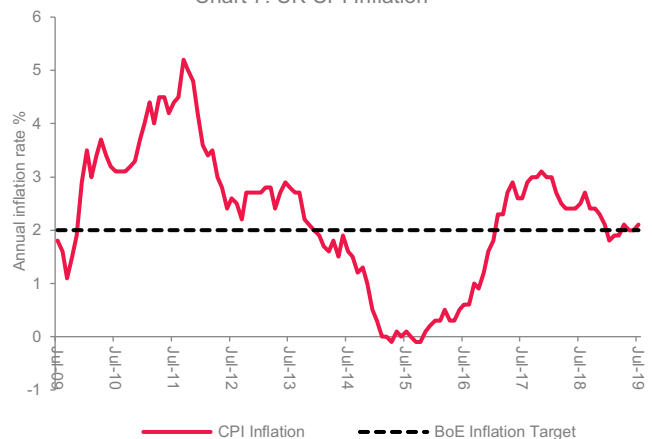
...but productivity weakens...

UK labour productivity, as measured by average output per hour, dropped by 0.2% in Q2, the second successive quarterly decline. In annual terms, UK productivity fell by 0.6% in Q2, the fourth successive quarter that productivity has fallen on an annual basis (see Chart 6). The decline in productivity in Q2 reflected both a rise in total weekly hours worked and weakening economic output. The UK's productivity performance continues to be weighed down by the failure to address the longstanding issues facing the UK economy, from growing skills gap to underinvestment in infrastructure and weak business investment.

...as inflation moves back above target...

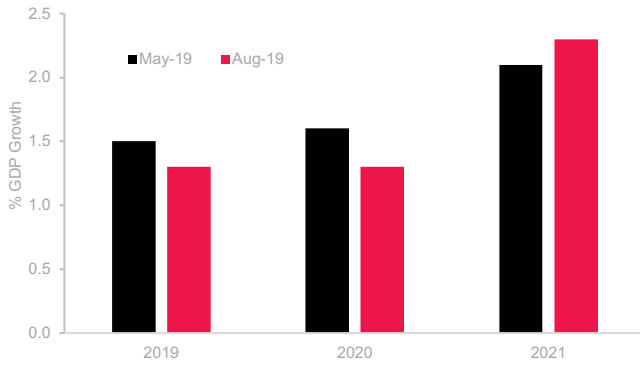
CPI inflation in the UK stood at 2.1% in July 2019, up from 2.0 in June and is the first time since April 2019 that inflation has been above the Bank of England's 2% target (see Chart 7). The largest upward pressure came from rising prices from a range of items, including clothing. There are signs that supply-chain pressures are rising with the growth rate of prices for materials and fuels at 1.3% in the year to July 2019, up from 0.3% in June. While consumer prices may drift higher in the coming months, the UK's weakening economic outlook should ensure that any increase in consumer prices is temporary.

Chart 7: UK CPI Inflation



Source: Consumer Price Inflation, July 2019

Chart 8: Bank of England UK GDP Growth Forecast Revisions



Source: Bank of England

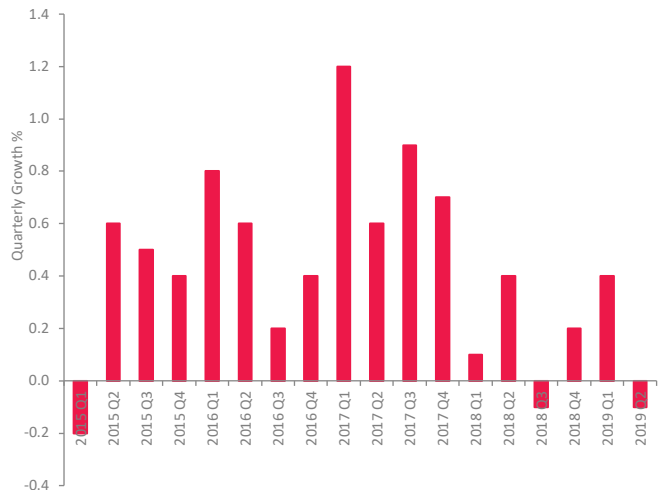
...as UK's growth outlook is downgraded...

In its latest inflation report, the Bank of England downgraded its UK GDP growth forecast for 2019 to 1.3%, from 1.5%, for 2020, from 1.6% to 1.3%, but upgraded its forecast for 2021 to 2.3%, from 2.1% (see Chart 8). The central bank cited growing concerns over Brexit and a deteriorating global economy as key drivers behind the forecast downgrades. Against this backdrop, it was unsurprising that the Monetary Policy Committee voted unanimously to keep interest rates on hold at 0.75%. If the UK economy slows further, then interest rates could remain on hold for some time to come.

...as Germany's economy contracts...

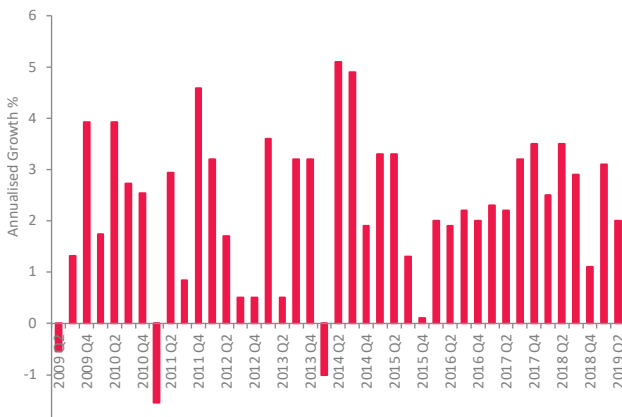
Germany's economy, the largest in the Eurozone, contracted by 0.1% in the second quarter of 2019 (see Chart 9). In annual terms, Germany's economy grew by just 0.4%. While household and government spending increased in quarter, this was more than offset by a marked deterioration in its net trade position. The continued China-US trade war and weakening global economic conditions has weighed on export activity, an important driver of German GDP growth. It is increasingly likely that the factors that drove the contraction in the second quarter will continue to weigh on the Germany GDP growth over the near term and could well push the country into a technical recession.

Chart 9: Germany Real GDP Growth



Source: Federal Statistical Office

Chart 10: US Real GDP Growth



Source: BEA

...US GDP growth revised downwards...

The second official estimate of US GDP revealed that the US economy, the world's largest, grew at an annualised rate of 2.0% in Q2 2019, down from the previous estimate of 2.1% and lower than the growth of 3.1% recorded in the previous quarter. The downward revision reflected downward revisions to government spending, exports and business investment that were partly offset by an upward revision to consumer spending. Continued trade tensions with China weighed on US GDP growth in Q2 with net trade a drag on growth, knocking 0.7 percentage points off US GDP growth in the quarter.

Bottom line:

Taken together, last month's data releases suggest that the UK economy is stalling amid growing anxiety over the prospect of a no-deal exit and moderating global growth. Against this backdrop, it is vital that the government goes all out to avoid a messy and disorderly exit from the EU and do more to boost the UK's growth trajectory by delivering the transformative infrastructure projects needed to secure the UK's economic future.

ECONOMIC SUMMARY CHART

Deteriorating ■ No change ■ Improving ■

Sector	Indicators (sources)	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	Jul-19	Aug-19
Household	Retail Sales (ONS)	■	■	■	■	■	■	■	■	■	■	■	■	■
	Consumer Confidence (GfK NOP)	■	■	■	■	■	■	■	■	■	■	■	■	■
	House Prices (Halifax)	■	■	■	■	■	■	■	■	■	■	■	■	■
	New car sales (SMMT)**	■	■	■	■	■	■	■	■	■	■	■	■	■
	Mortgage approvals (Bank of England)	■	■	■	■	■	■	■	■	■	■	■	■	■
Business	Business confidence (BCC)***	■	■	■	■	■	■	■	■	■	■	■	■	■
	Business lending (Bank of England)	■	■	■	■	■	■	■	■	■	■	■	■	■
	Service sector output (ONS)	■	■	■	■	■	■	■	■	■	■	■	■	■
	Production output (ONS)	■	■	■	■	■	■	■	■	■	■	■	■	■
	Investment intentions (BCC)**	■	■	■	■	■	■	■	■	■	■	■	■	■
Labour market	Employment (ONS)	■	■	■	■	■	■	■	■	■	■	■	■	■
	Unemployment (ONS)	■	■	■	■	■	■	■	■	■	■	■	■	■
	Earnings (ONS)	■	■	■	■	■	■	■	■	■	■	■	■	■
	Economic Inactivity (ONS)	■	■	■	■	■	■	■	■	■	■	■	■	■
Government	Public sector net borrowing (ONS)**	■	■	■	■	■	■	■	■	■	■	■	■	■
	Public sector net debt % of GDP (ONS)**	■	■	■	■	■	■	■	■	■	■	■	■	■
	Tax receipts (HMRC)**	■	■	■	■	■	■	■	■	■	■	■	■	■
	Current Budget Deficit (ONS)**	■	■	■	■	■	■	■	■	■	■	■	■	■
External	UK trade balance (ONS)	■	■	■	■	■	■	■	■	■	■	■	■	■
	Export Sales (BCC)***	■	■	■	■	■	■	■	■	■	■	■	■	■
	Export orders (BCC)***	■	■	■	■	■	■	■	■	■	■	■	■	■
Financial	Exchange rate (Bank of England)	■	■	■	■	■	■	■	■	■	■	■	■	■
	Equity Prices (Bloomberg)	■	■	■	■	■	■	■	■	■	■	■	■	■
	10 year Government bonds (Bloomberg)	■	■	■	■	■	■	■	■	■	■	■	■	■

*Colours indicate an improvement or deterioration of each indicator and refer to monthly changes unless stated. For example, an improvement in employment refers to an increase, while an improvement in unemployment refers to a fall. Also, a depreciation in the exchange rate refers to an improvement and an appreciation in the exchange rate refers to a deterioration. Dates refer to the release dates for each indicator.

Annual changes. *Quarterly changes. ****Latest figures are estimate.