BCC ECONOMICS

BRITISH CHAMBERS OF COMMERCE

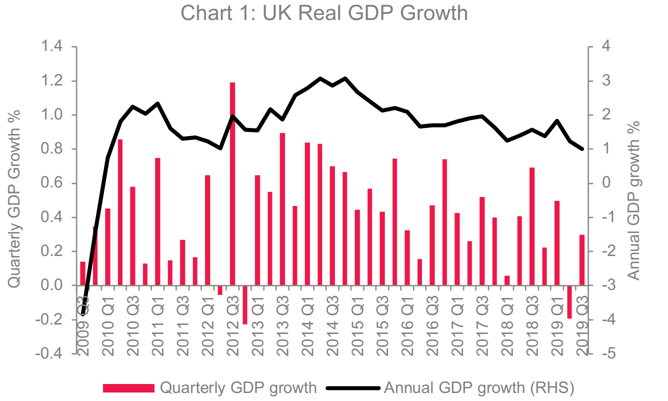
MONTHLY ECONOMIC REVIEW December 2019

Monthly headlines:

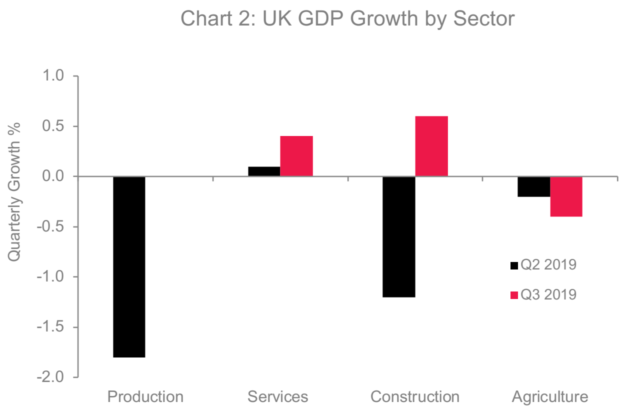
- UK economy returned to growth in Q3 amid strengthening service sector output
- UK inflation drops to 3-year low as labour market conditions continue to moderate
- Germany avoids recession in the third quarter as Japan's economy slows

UK economy returned to growth in Q3...

The UK economy grew by 0.3% in Q3 2019, up from a contraction of 0.2% in Q2 **(see Chart 1)**. In annual terms, the UK economy grew by 1.0% in Q3, the weakest outturn since Q1 2010. While there was welcome confirmation that the UK avoided recession in Q3, **the stronger headline figure masks a marked slowdown through the quarter.** Following a relatively strong July reading (+0.3%) on the monthly measure, UK GDP contracted in August (-0.2%) and September (-0.1%), the first successive monthly declines since the end of 2013.



Source: ONS UK GDP: Q3 2019



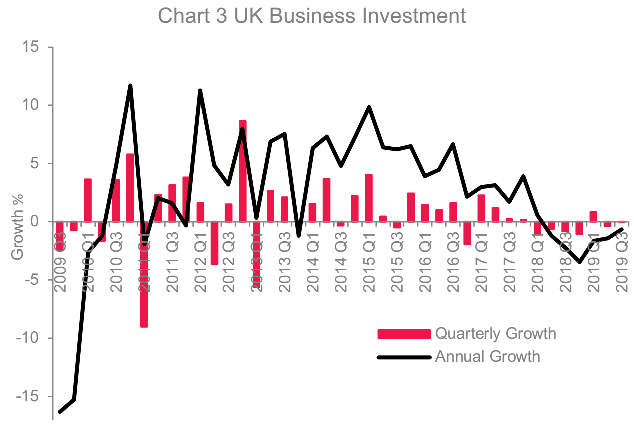
Source: ONS UK GDP, Q3 2019

...reflecting stronger services sector output...

The service sector, which accounts for around 80% of UK economic output, was the main driver of UK growth in Q3 2019, growing by 0.4% in the quarter, up from growth of 0.1% in Q2 **(see Chart 2).** Construction output rose by 0.6% in third quarter. Industrial production recorded zero growth in Q3 and agricultural output contracted by 0.2%. On the monthly measure, output fell in the industrial (-0.3%), construction (-0.2%) and agriculture (-0.2%) sectors in September, while output from the services sector was flat in the month.

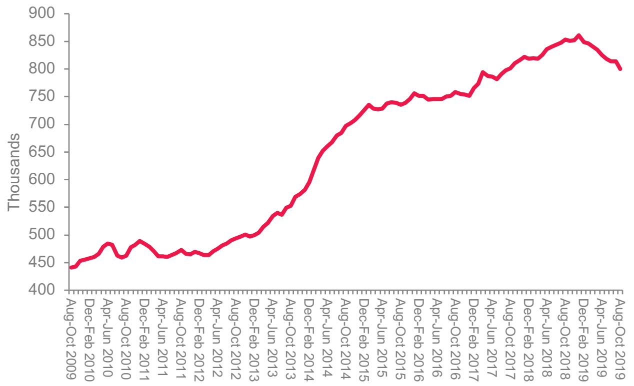
...but business investment remains weak...

The first official estimate of Q3 2019 UK GDP also revealed that household expenditure, a key driver of the UK economy, rose by 0.4% in the quarter, unchanged from the previous quarter. Government spending increased by 0.3% in Q3. In contrast, there was zero growth in business investment in Q3 **(see Chart 3)** and means that **UK business investment has grown in just one of the past seven quarters**. In annual terms, business investment was down by 0.6% in Q3. Anaemic business investment is a drag anchor on the economy as it limits UK productivity.



Source: ONS UK GDP, Q3 2019

Chart 4: Job Vacancies



Source: ONS Labour Market Overview, November 2019

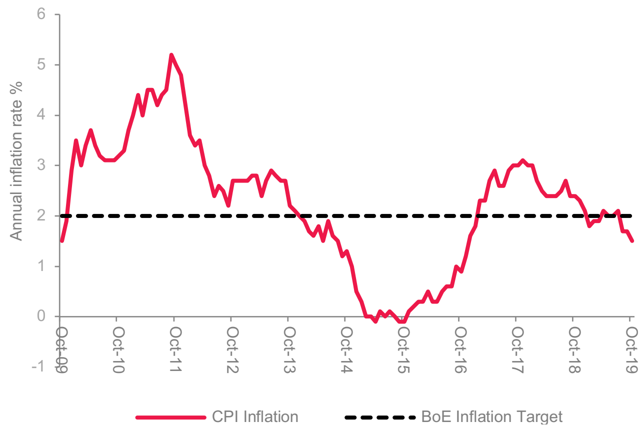
…labour market conditions moderate...

In the three months to September 2019, the number of people in employment fell by 58,000. UK's unemployment rate eased from 3.9% to 3.8% over the same period. **The number of job vacancies dropped by 18,000 to 800,000, the ninth successive decline (see Chart 4)**. Average weekly earnings growth (excluding bonuses) slowed from 3.9% to 3.6%. Although the UK's unemployment rate remains very low by historic standards, falling employment and job vacancies is further evidence that the labour market is starting to toil under the weight of a subdued economy, rising cost pressures and unrelenting uncertainty.

...as inflation continues to slow…

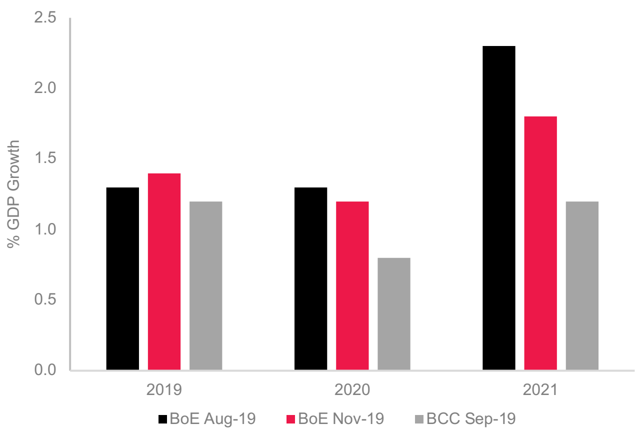
CPI inflation in the UK stood at 1.5% in October 2019, the weakest rate since November 2016 and down from 1.7% in September **(see Chart 5)**. The largest downward pressure on UK consumer prices in October 2019 came from fuel price drops amid a lowering of the energy price cap by Ofgem. **The current trajectory for UK inflation remains subdued with supply-chain price pressures continuing to weaken** - prices for materials and fuels fell by 5.1% on the year to October, following a drop of 3.0% in September. Slowing consumer price growth means that the gap between pay and price growth is still significant by recent standards, despite slowing wage growth.

Chart 5: UK CPI Inflation



Source: ONS Consumer Prices, November 2019

Chart 6: UK GDP Growth Forecasts



Sources: BCC, Bank of England

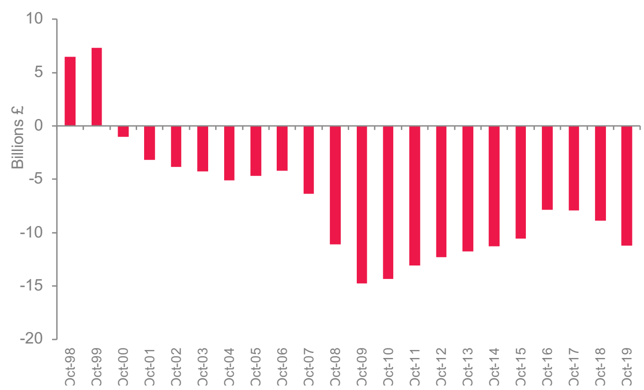
…UK's growth outlook remains subdued…

In its November 2019 Monetary Policy report, the Bank of England upgraded its UK GDP growth forecast for 2019 to 1.4%, from its previous estimate of 1.3%. However, the central bank's forecast for GDP growth in 2020 has been downgraded to 1.2% (from 1.3%) and to 1.8% (from 2.3%) in 2021**. The downgrades have been driven by a weaker global backdrop and the assumed impact of the government's current Brexit plans.** While the central bank's latest UK GDP growth forecast is more optimistic than the BCC's latest growth projections **(see Chart 6)**, they continue to indicate that UK GDP growth is set to remain weak for some time to come.

…UK government borrowing at 5-year high...

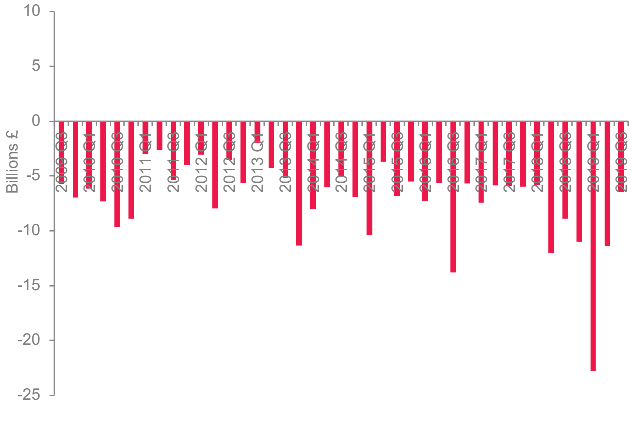
UK public sector net borrowing (excluding the public sector banks) stood at £11.2 billion in October 2019. This was the highest October outturn since 2014 and £2.3 billion higher than in October 2018 **(see Chart 7)**. In the current financial year-to-date, government borrowing rose by £4.3 billion to £46.3 billion. **Public sector net debt stood at 80.4% of UK GDP in October 2019, more than double the pre-financial crisis average.** The UK's fiscal position is likely to come under increasing pressure in the near-term if UK economic growth weakens as expected, further limiting the extent to which public spending can be significantly boosted from current levels.

Chart 7: UK Government Borrowing



Source: ONS Public Sector Finances: October 2019

Chart 8: UK's Net Trade Position



Source: ONS UK Trade, September 2019

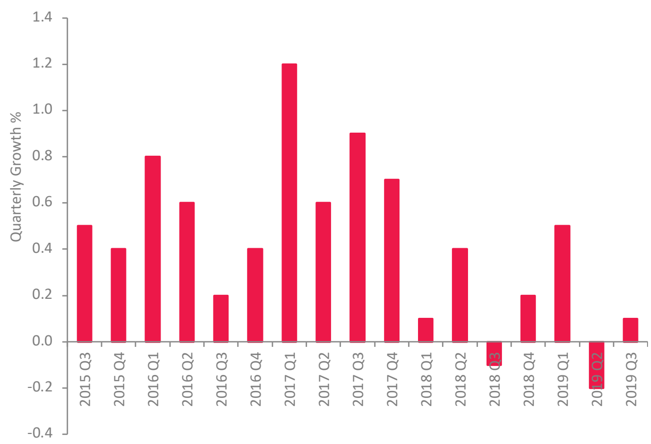
...as the UK's trade deficit narrows...

The UK's trade deficit in goods and services narrowed by 5.0 billion to £6.4 billion in Q3 2019 **(see Chart 8)**. **The improvement was driven by a 6.3% increase in services exports and a 5.0% uptick in goods exports.** However, the longer-term measures point to an underlying weakness with the UK's total trade deficit widening by £18.9 billion to £51.6 billion in the 12 months to September 2019, mainly because of the UK's trade deficit in goods increasing by £13.9 billion to £152.7 billion. Brexit uncertainty and subdued growth prospects in some of the UK's key export markets are likely to weigh on trading conditions for exporters for some time to come.

...as Germany avoids recession…

Germany's economy, the largest in the Eurozone, grew by 0.1% in the third quarter of 2019 **(see Chart 9)** following a contraction of 0.2% in the previous quarter. This meant that Germany avoided entering a technical recession. GDP growth in Q3 was largely driven by an increase in household (+0.4%) and government spending (+0.8%). In annual terms, Germany's economy grew by 1.0%. Despite avoiding recession, the near-term outlook for the German economy remains weak with **deteriorating global economic conditions and heightened trade tensions likely to continue to stifle exports, a key driver of the German economy**.

Chart 9: Germany Real GDP Growth



Source: Destatis

Chart 10: Japan Real GDP Growth

Source: Cabinet Office

...Japan's economic growth slows.

Japan, the world's third-largest economy, grew by 0.1% in Q3 2019, the weakest growth since Q3 2018 and down from growth of 0.4% recorded in the previous quarter **(see Chart 10)**. Japan's economy grew at an annualised rate of just 0.2% in the third quarter. **The slowdown was largely driven by growth in consumer spending** (which accounts for almost two-thirds of Japanese GDP growth) **slowing to 0.4% in Q3,** down from growth of 0.6% in the previous quarter. There was also a 0.7% drop in exports in Q3, reflecting slowing global growth and mounting global trade tensions, including worsening trade relations with South Korea.

Bottom line:

Although there was welcome confirmation that the UK avoided recession in the third quarter, November's data releases suggests that economic conditions remain sluggish. Against this backdrop and as outlined in: *2020 and beyond: business priorities for the next UK government*, avoiding a no-deal Brexit and delivering an urgent confidence boost through action on infrastructure, immigration, skills and business costs must be at the forefront of the next government's agenda.

ECONOMIC SUMMARY CHART

Deteriorating (red) No change (yellow) Improving (green)

Sector	Indictors (sources)	Nov-18	Dec-18	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	Jul-19	Aug-19	Sep-19	Oct-19	Nov-19
Household	Retail Sales (ONS)	Deteriorating	Improving	Deteriorating	Improving	Improving	Improving	No change	Deteriorating	Improving	Improving	Deteriorating	No change	Deteriorating
	Consumer Confidence (GfK NOP)	Deteriorating	Deteriorating	No change	Improving	Improving	No change	No change	Deteriorating	Improving	Deteriorating	Improving	Deteriorating	Deteriorating
	House Prices (Halifax)	Improving	Deteriorating	Improving	Deteriorating	Improving	Deteriorating	Improving	Improving	Deteriorating	Deteriorating	Improving	Deteriorating	Deteriorating
	New car sales (SMMT)**	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Deteriorating
	Mortgage approvals (Bank of England)	Deteriorating	Improving	Improving	Deteriorating	Improving	Deteriorating	Deteriorating	Improving	Improving	Improving	Deteriorating	Improving	Improving
Business	Business confidence (BCC)***	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating
	Business lending (Bank of England)	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Deteriorating	Deteriorating	Deteriorating	Improving	Deteriorating	Improving	Improving	Improving
	Service sector output (ONS)	Deteriorating	Improving	Improving	Deteriorating	Improving	Improving	Deteriorating	No change	No change	No change	Improving	Deteriorating	No change
	Production output (ONS)	No change	Improving	Deteriorating	Deteriorating	Improving	Improving	Improving	Deteriorating	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating
	Investment intentions (BCC)**	Improving	Improving	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating
Labour market	Employment (ONS)	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Deteriorating	Deteriorating
	Unemployment (ONS)	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Improving	Improving	Improving	Improving	Deteriorating	Improving	Deteriorating	Improving
	Earnings (ONS)	Improving	Improving	Improving	Improving	Improving	No change	Deteriorating	Deteriorating	Improving	Improving	Improving	Improving	Deteriorating
	Economic Inactivity (ONS)	Deteriorating	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Deteriorating	Improving	Improving	Deteriorating	Deteriorating
Government	Public sector net borrowing (ONS)**	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Improving	Deteriorating	Deteriorating
	Public sector net debt % of GDP (ONS)**	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving
	Tax receipts (HMRC)**	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Deteriorating
	Current Budget Deficit (ONS)**	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Improving	Improving	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Deteriorating
External	UK trade balance (ONS)	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Improving	Improving	Improving
	Export Sales (BCC)***	Deteriorating	Improving	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating
	Export orders (BCC)***	Deteriorating	Deteriorating	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating
Financial	Exchange rate (Bank of England)	Improving	Deteriorating	Improving	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Improving	Deteriorating
	Equity Prices (Bloomberg)	Improving	Deteriorating	Improving	Improving	Improving	Deteriorating	Deteriorating	Improving	Deteriorating	Deteriorating	Improving	Deteriorating	Improving
	10 year Government bonds (Bloomberg)	Deteriorating	Improving	Improving	Deteriorating	Improving	Deteriorating	Improving	Improving	Improving	Improving	Deteriorating	Deteriorating	Improving

*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.