RESEARCH

UK ECONOMIC OVERVIEW JANUARY 2019

The UK's gross domestic product slowed 10 bps from the prior period to 0.3% in the three months to November 2018, dragged down by widespread contraction in the production sector (-0.8%), despite strong growth in the summer of 2018. The service sector (+0.3%) and construction (+2.1%) underpinned the three-month growth figure.

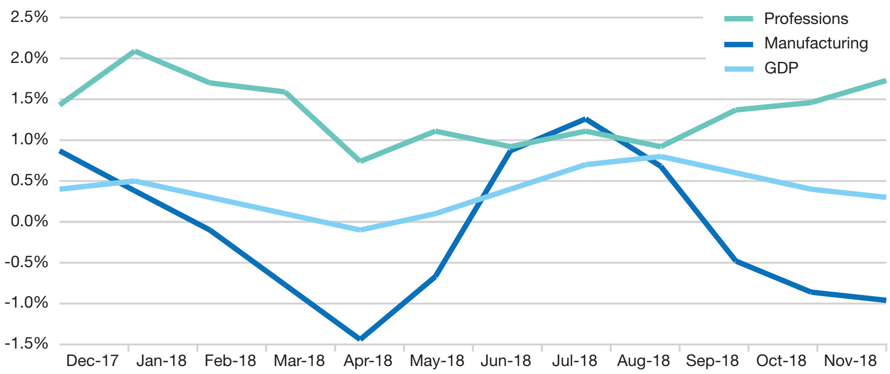
Service sector output in the three months to November 2018 increased by +0.3%, driven by prevailing growth in the professional, scientific and technical activities sector, which was driven by accounting and auditing activities (+4.7%). The retail sector was the largest contributor to month-on-month growth in November thanks to a boost from Black Friday sales. Services output increased by +1.8% since the three months to November 2017.

Meanwhile, UK manufacturing output fell -0.8% in the three months to November 2018. The monthly decrease of -0.4% in manufacturing output owes much to the weakness in transport equipment stemming from shutdowns in October and reduced production in November 2018. The manufacturing Purchasing Managers' Index, however, is standing at a six-month high of 54.2, where a reading above 50 means expansion. New business has increased steadily since October, with stocks of purchases increasing and contributing to growth in the sector. Much of this rise in activity stems from businesses stockpiling raw materials and goods to mitigate potential supply chain disruptions resulting from Brexit.

Retail sales grew +2.7% year-on-year in December 2018. Compared to the +2.0% annual growth in 2017, this might seem encouraging, but remains low considering the +4.7% annual growth recorded in December 2016. December's -0.9% month-on-month decline in retail sales was driven by a fall in the purchase of non-essential items.

FIGURE 1

UK GDP – Downbeat manufacturing data was offset by robust growth in the professional services sector



Source: ONS

CPI inflation's 12-month growth rate was +2.1% in December 2018, down from +2.3% in November 2018, largely because of reduced contribution from increased transportation prices and falling motor fuel prices. The UK unemployment rate in November remained unchanged at 4.0% on the quarter.

141,000 people entered employment in the three months to November and wages grew 3.3% on the year – the biggest rise since 2008.

The 10-year gilt yield in December 2018 decreased to 1.27% from 1.44% in November. The IPD equivalent yield remained unchanged at 5.81% in December, increasing the arbitrage from 4.37% in November to 4.54% in December.

The sterling has hit a 2019 high against both the euro and the greenback as the mechanics of how Brexit can be delayed, or stymied altogether, has become clearer, leading traders to believe that the threat of a 'no deal' Brexit is becoming a less likely outcome on March 29. This has pushed the pound to euro exchange rate up, touching €1.16 highs and hovering around €1.15.

While the diminished demand for the 'safety' of the US Dollar now means an exchange rate of $1.31 for a pound.

Key points

Consumers pulled forward their Christmas shopping last year to take advantage of Black Friday sales, leading to a slower festive season for retailers in December.

Self-employment accounted for two-thirds of the 141,000 jobs created in the three months to November. Employers may have been hiring contractors rather than full-time staff amid Brexit related uncertainty.

UK inflation slowed 20 bps month-on-month to 2.1% in December 2018, leaving the Bank of England under no pressure to raise interest rates any time soon.

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