

BRITISH CHAMBERS OF COMMERCE

MONTHLY ECONOMIC REVIEW March 2020

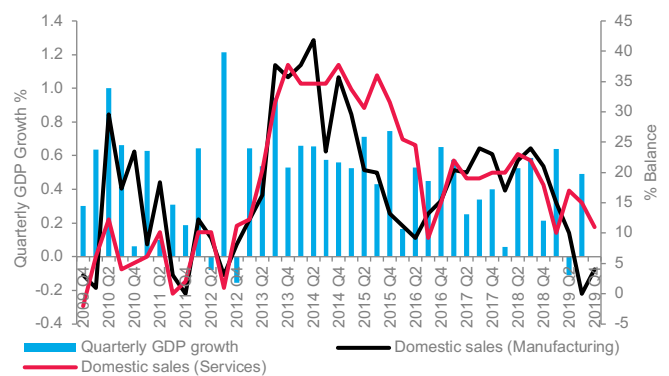
Monthly headlines:

- UK economy stalled in Q4 as industrial production contracts and service sector output slows
- UK labour market remains robust as inflation picks up
- Japan's economy close to recession as German GDP growth stalls

UK economy stalled in Q4...

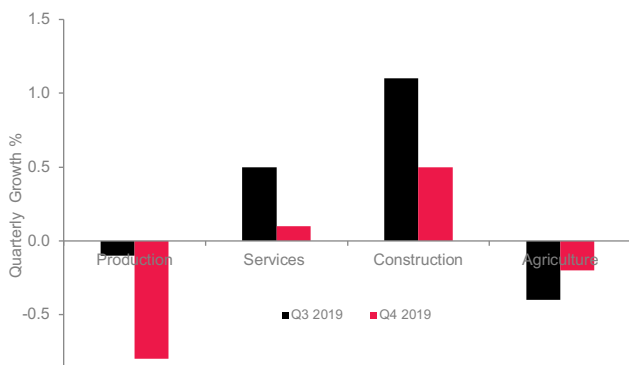
The first official estimate of UK GDP revealed that the UK economy recorded zero growth in the final quarter of 2019 (see Chart 1), down from growth of 0.5% recorded in the third quarter. This mirrored the results from the latest BCC Quarterly Economic Survey which found protracted weakness across most indicators of economic health in the final quarter of 2019. For 2019 as a whole, the UK economy grew by 1.4%, up slightly from growth of 1.3% in 2018. On the monthly measure, UK GDP rose by 0.3% in December 2019.

Chart 1: Real GDP and Domestic Sales



Source: ONS UK GDP, December 2019

Chart 2: UK GDP Growth by Sector



Source: ONS UK GDP, December 2019

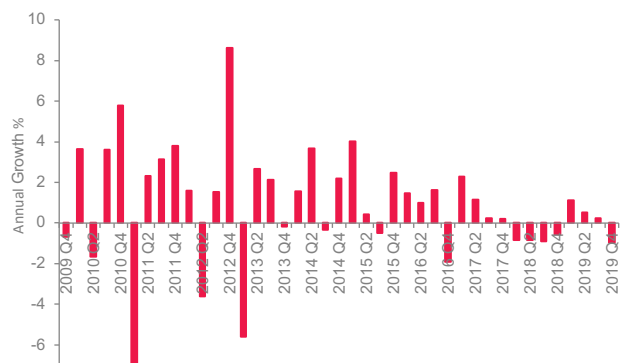
...as the industrial sector contracts...

Industrial production contracted by 0.8% in Q4 (see Chart 2), with output from the manufacturing sector, which accounts for around 10% of UK economic output, dropping by 1.1% in the quarter. The services sector, which accounts for around three-quarters of UK economic output, grew by 0.1% in Q4, down from growth of 0.5% recorded in the previous quarter. Construction sector output rose by 0.5% in Q4. On the monthly measure, output from the services (+0.3%), construction (+0.4%) and industrial (+0.1%) sectors all increased in December.

...and business investment weakens...

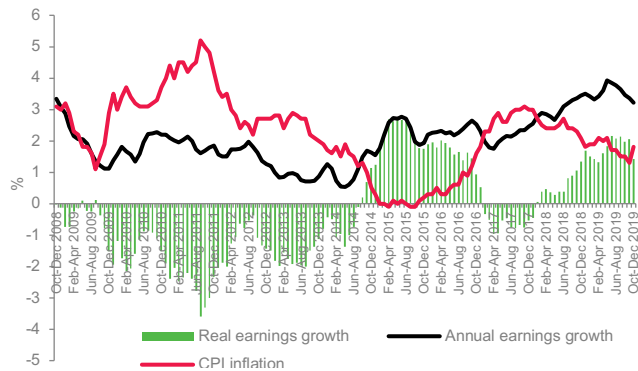
The latest UK GDP data also revealed that business investment in the UK fell by 1.0% in Q4 (see Chart 3), the largest decline since Q4 2016. However, due to upward revisions to earlier quarters, business investment grew by 0.3% for 2019 as a whole. Although this was up from a decline of 1.5% in 2018, it was well below the long-term average growth rate of 2.0%. Household consumption increased by 0.1% in Q4, down from 0.4% growth in Q3. For 2019 as a whole, household consumption rose by 1.4%, the weakest outturn since 2011.

Chart 3 UK Business Investment



Source: ONS UK GDP, December 2019

Chart 4: UK Real Earnings Growth



Source: ONS UK Labour Market Overview, December 2019

...UK labour market remains robust...

In the three months to December 2019, UK employment rose by 180,000. The number of people out of work decreased by 16,000 over the same period. However, the strong headline figures mask underlying problems. **Lingering economic uncertainty has often led to companies hiring staff rather than investing in new technology, weakening productivity.** Average earnings growth (excluding bonuses) slowed to 3.2% (see Chart 4), from 3.8% as a weak economy, low productivity and high employment costs continues to limit increases in pay settlements.

...UK inflation picks up...

CPI inflation stood at 1.8% in January 2020, the highest rate since July 2019 and up from 1.3% in December (see Chart 5). However, UK inflation was still below the Bank of England's 2% target. The upward pressure on inflation largely reflected a 4.7% increase in fuel prices (the biggest rise since November 2018) and airfares falling by less than a year ago. Although the UK's inflation current trajectory remains subdued amid a sluggish economy, **a sustained disruption to global production and supply chains due to the coronavirus could increase the upward pressure on consumer prices in the medium term.**

Chart 5: UK CPI Inflation



Source: ONS Consumer Price Inflation, January 2020

Chart 6: UK Government Borrowing



Source: ONS Public Sector Finances, January 2020

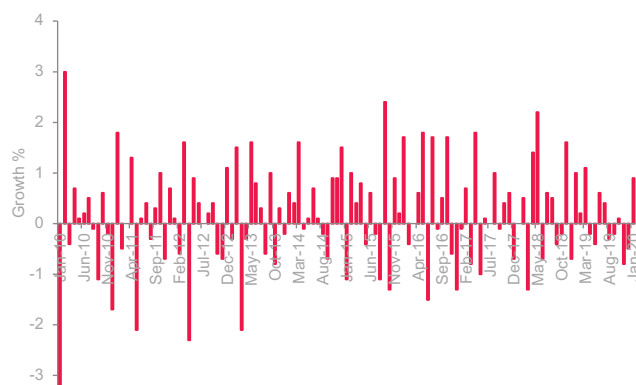
...public finances likely to undershoot target...

UK public sector finances (excluding public sector banks) recorded a surplus of £9.8 billion in January 2020 (see Chart 6). **January is typically a month where the public finances are in surplus due to the timing of self-assessed income tax receipts.** In the current financial year-to-date, government borrowing stood at £44.8 billion and suggests that UK government should undershoot the OBR's forecast of £47.6 billion. With a slowing economy likely to weaken tax revenue and government spending expected to increase, achieving meaningful deficit reduction is likely to prove increasingly challenging.

... retail sales increase in January...

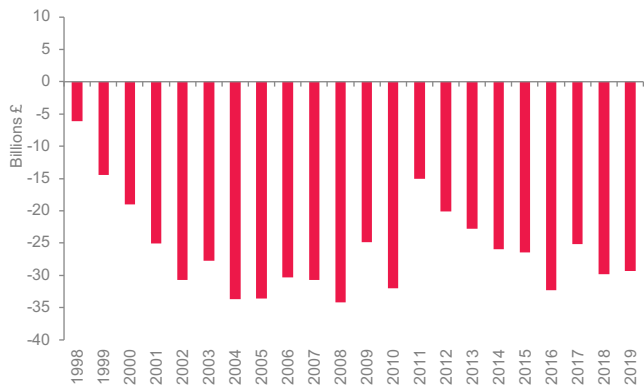
Retail sales rose by 0.9% in January, the largest monthly increase since March 2019 (see Chart 7). The monthly improvement reflected a 1.7% rise in food store sales and a 1.3% increase in non-food sales. However, despite the improvement in January, **retail sales still decreased by 0.8% on the 3 month on 3 month measure – a better indicator of the underlying trend – with sales in all sectors declining in the period.** Slowing wage growth (see Chart 4) and subdued consumer confidence are likely to limit consumer spending over the near term, maintaining the pressure on the retail sector.

Chart 7: UK Retail Sales



Source: ONS Retail Sales, January 2020

Chart 8: UK's Net Trade Position



Source: ONS UK Trade, December 2019

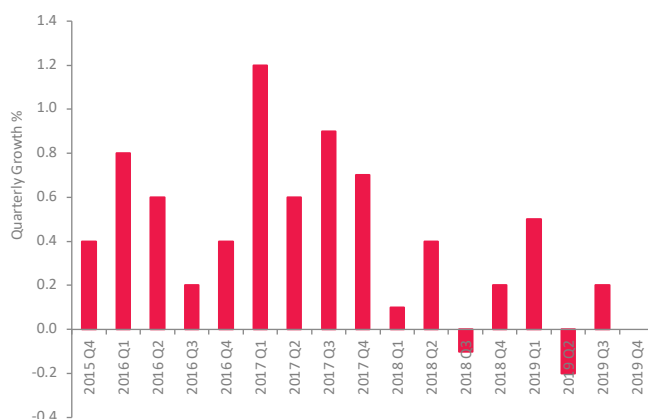
...the UK's trade deficit narrowed in 2019...

The UK's trade deficit in goods and services widened by £4 billion to £6.5 billion in Q4 2019. The deterioration was driven by a £5.1 billion narrowing in the UK's trade surplus in services as exports fell by £4.3 billion. The weakening in the UK's services trade surplus was partly offset by a narrowing of the trade in goods deficit. **The UK's trade deficit narrowed by £0.5 billion to £29.3 billion in 2019 as a whole (see Chart 8),** with a £9.7 billion narrowing of the trade in goods deficit, more than offsetting a £9.2 billion decline in the UK's trade in services surplus.

...as German GDP stagnates...

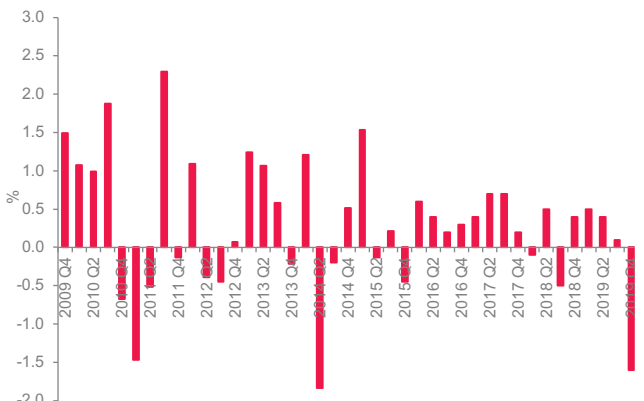
Germany's economy, the largest in the Eurozone, recorded zero growth in the final quarter of 2019 (see Chart 9), following growth of 0.2% in the previous quarter. In annual terms, the German economy grew by 0.3% in Q4, down from growth of 1.1% in Q3. The stagnation in GDP growth in Q4 was largely driven by weakening household and government spending and a deterioration in Germany's net trade position. For 2019 as a whole, the Germany economy grew by 0.6%. The near-term outlook for the German economy remains weak with a **subdued global economy and the impact of Covid-19 likely 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 economy contracts.

Japan, the world's third-largest economy, contracted by 1.6% in Q4 2019, the weakest outturn since Q2 2014 (see Chart 10). The contraction was partly driven by consumer spending (which accounts for almost two-thirds of Japanese GDP growth) declining by 2.9% in Q4, as a VAT hike and typhoon Hagibis weighed on activity. On an annualised basis, Japan's economy contracted by 6.4% in the final quarter of 2019, the biggest contraction in five years and down from growth of 0.5% in Q3. The possibility of Japan dropping into recession is relatively high with impact of Covid-19 likely to weigh heavily on Japan's economy in Q1.

Bottom line:

Taken together, the latest data releases indicate that economic conditions remain challenging. Against this backdrop, it is vital that the focus of policymakers should be on taking swift and tangible steps to boost growth and productivity across the whole of the UK, including incentives to release investment and easing upfront business costs.

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ECONOMIC SUMMARY CHART

Deteriorating ■ No change ■ Improving ■

Sector	Indicators (sources)	Feb-19	Mar-19	Apr-19	May-19	Jun-19	Jul-19	Aug-19	Sep-19	Oct-19	Nov-19	Dec-19	Jan-20	Feb-20
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.