ESSENTIAL READING

UK DEMAND & OUTPUT MONTHLY

December 2015

UK Team

GDP and latest nowcasts

	ONS 2nd estimate	UK Team expectation	Consensus	Latest backcast
Q3	**0.5%**	**0.5%**	**0.5%**	**0.6%**
	Latest nowcast		Last month's expectation	
Q4	**0.6%**		**0.6%**	

This month's data at a glance

Expenditure growth (%qoq)	2015 Q3	Nov IR	Contrib. to error*	2015 Q2	2015 Q1
GDP	0.5	0.6**	0.0	0.7	0.4
Consumption	0.7	0.8	0.0	0.9	0.8
Govt consumption	1.3	0.0	0.3	0.4	1.1
Investment	1.8	1.3	0.1	0.2	1.4
- Business	2.2	1.2	0.1	1.6	2.4
- Housing	-0.5	2.3	-0.1	-2.7	0.8
- Government	4.5	0.0	0.1	2.7	0.8
Net Trade*	-1.5	-1.2	-0.2	1.4	-0.6
- Exports	0.9	1.1	-0.1	1.9	-1.2
- Imports	5.5	5.0	0.2	-2.7	0.6
Other (inc. stocks)*	0.9	1.0	-0.2	-1.6	-0.1

*Contributions may not sum due to rounding

**Backcast

Monthly Output Indices	Sep	Aug	Jul	Jun	May
Index of Services	0.5	0.0	0.1	0.6	0.2
- PNDS	0.6	0.0	0.1	0.8	0.3
- Distribution	0.6	-0.3	0.3	1.0	-0.2
Index of Production	-0.2	0.9	-0.4	-0.2	0.3
- Manufacturing	0.8	0.4	-0.8	0.2	-0.9
Construction output	-0.2	-3.4	-1.2	2.4	-0.7

Trade and Retail Sales	Oct	Sep	Aug	Jul	Jun
Retail sales vols (inc fuel)	-0.6	1.7	-0.4	0.6	-0.2
Retail sales vols (exc fuel)	-0.9	1.5	-0.7	0.9	-0.3
Goods imports	n/a	-2.6	-0.4	4.8	11.2
Goods exports	n/a	0.4	5.8	-7.2	10.0

Survey Measures	Nov	Oct	Sep	Aug	Ave
CIPS Services*	-	54.9	53.3	55.6	55.1
CIPS Manufacturing	55.1	57.9	53.4	53.1	53.4
CIPS Construction	55.3	58.8	59.9	57.3	54.7
GfK Consumer Conf	0.5	2.4	1.9	4.3	-9.2

*CIPS Services data are confidential until the 3rd December.

CBI Service Sector Survey	2015 Q4	2015 Q3	2015 Q2	2015 Q1	Ave
Business optimism	18	33	29	17	3
Employment: next 3 months	22	12	34	31	11
Inv. Intentions: vehicles, plant & machinery	11	4	11	11	-6

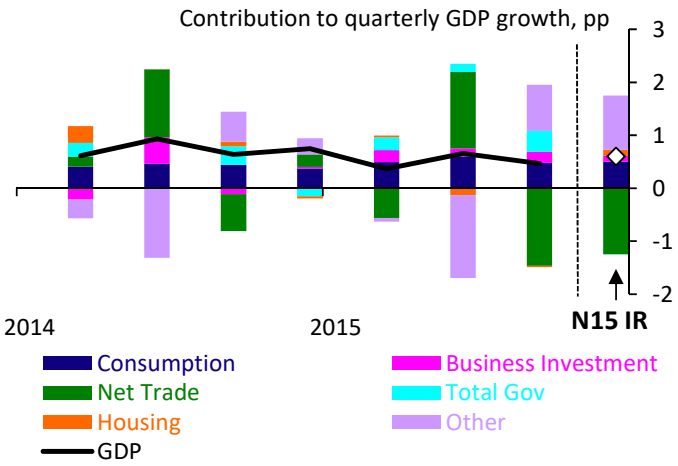
Our Q4 GDP nowcast remains at 0.6%, reflecting very little news this month

Q3 GDP growth was unrevised at 0.5%, in line with our expectation. We still expect it to be revised up to 0.6% eventually.

There has been no significant data news this month. The official output releases for September were broadly in line with the Q3 prelim GDP estimate, while the expenditure split was similar to the November IR. Movements in the most recent survey indicators have been mixed.

Our Q4 nowcast remains at 0.6%.

Chart 1: Expenditure contributions to GDP growth



Q3 GDP growth was unrevised at 0.5%

Q3 GDP growth was unrevised at 0.5% in the second estimate (Chart 1), in line with our expectation for the release. That is 0.1pp below the November Inflation Report (IR) forecast, but we continue to expect an upward revision to 0.6% in the future, as the estimate matures.

The quarterly growth picture across the output components is virtually intact from the preliminary Q3 GDP release last month, as we anticipated, despite new monthly production, construction and services figures. Services output grew solidly in Q3, by 0.7%, in line with its historical average. Production growth was a touch weaker (0.2% down from 0.3%) due to lower manufacturing output. Meanwhile construction output is still recording a surprisingly sharp 2.2% fall, but we think the extent of the construction output weakness is likely to be overstated in the official data (see Analytical 7281839 for more details).

There was also relatively little news in the expenditure split. Government spending (consumption and investment) and business investment were stronger than expected in the

Chart 2: Real net trade contributions to GDP growth

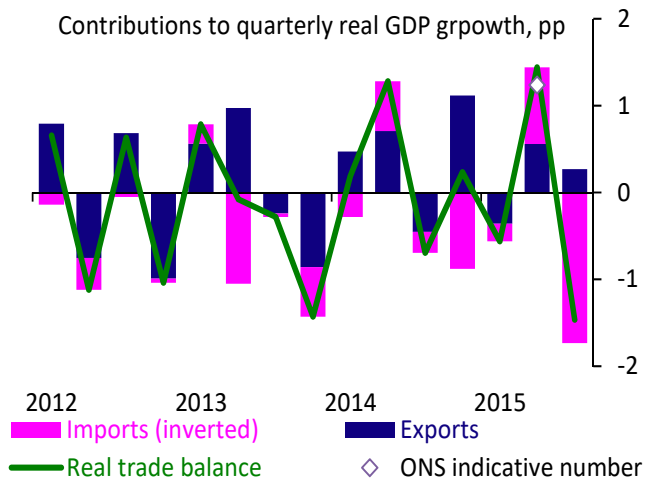


Chart 3: Monthly economic uncertainty indicator

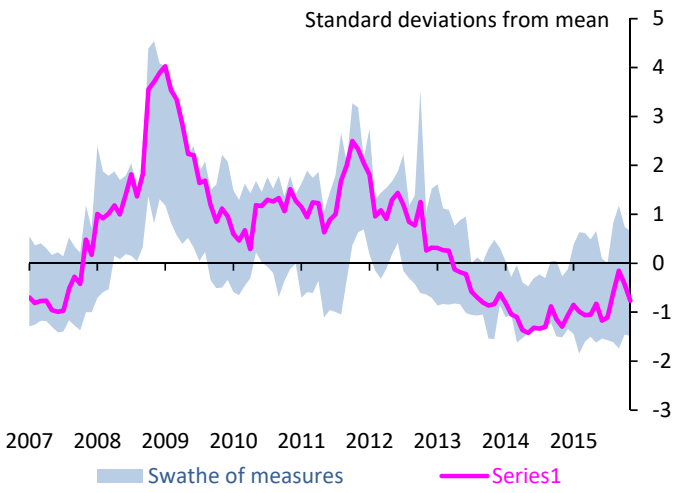
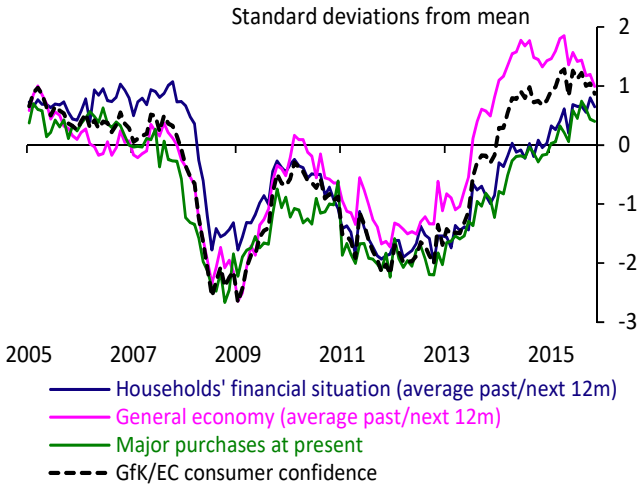


Chart 4: GfK/EC consumer confidence



November IR, broadly offset by weaker housing and net trade (Chart 1). We had anticipated the net trade revision ahead of the release, based on the monthly goods data.

Revisions to the goods trade data should shrink the real net trade drag to GDP growth in Q3

The Q3 GDP second estimate recorded an unusually large drag to growth from net trade: -1.5pp was the weakest since 1979, unwinding a similarly large positive contribution in Q2 (Chart 2). But we know not to take these data at face value, given the discrepancies between the implied goods trade deflators and the underlying price indices from 2014 Q1 onwards, which were acknowledged by the ONS last month (see Analytical 7266944 by Matt Corder and Chris Hackworth for more details).

The ONS have indicated that the Q2 2015 real trade deficit may be £0.9bn larger, based on some initial analysis of the data issues. But that would still suggest a large positive net trade contribution to Q2 GDP growth (the white diamond in Chart 2). No equivalent figure has been provided for Q3; but the ONS will publish revised goods trade data next week, in which the data issues should be resolved.

Housing investment disappointed in Q3, whereas business investment was better than expected

In the November IR, we expected housing investment in Q3 to reverse most of its sharp decline in the previous quarter. That occurred for dwellings investment but not for total housing investment, which fell for the second quarter in a row. That decline was entirely due to a 12.4% fall in the costs of ownership component, which is at odds with strong growth in both mortgage approvals and housing transactions. We're currently following this up with the ONS to better understand the data, but it would not be unusual to see heavy revisions in this component.

In contrast, quarterly business investment growth in Q3 was somewhat stronger than we had expected (2.2% vs 1.2%). The latest CBI Service Sector Survey (SSS) investment intentions data ticked up this month, suggesting that solid business investment growth could be maintained into Q4.

Uncertainty fell back further from its September high

Our monthly indicator of economic uncertainty has fallen back over the past two months from its 29 month high in September (Chart 3). That reflects movements in two of the six underlying components: lower equity market volatility and fewer media citations. We can't directly observe whether the uncertainty measure has been affected by the Paris attacks in mid-November. But more broadly, based on the experience of past terrorist attacks, we expect financial and macroeconomic spillovers to the UK to be limited and short-lived (see Analytical 7289906 for more details).

Elevated consumer confidence falls back further

The November GfK consumer confidence survey period closed soon after the Paris attacks, so is unlikely to fully capture that event. Nonetheless, our preferred seasonally adjusted GfK/EC measure did fall back, but that looks to be

Chart 5: CBI Service Sector Survey & ONS PNDS

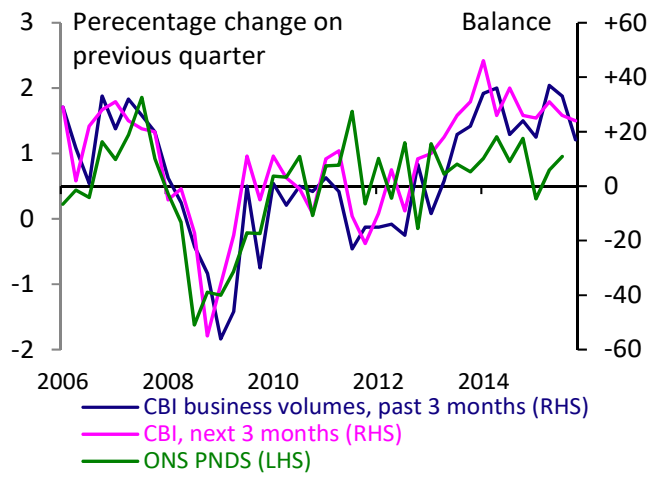


Chart 6: Monthly manufacturing export indicators

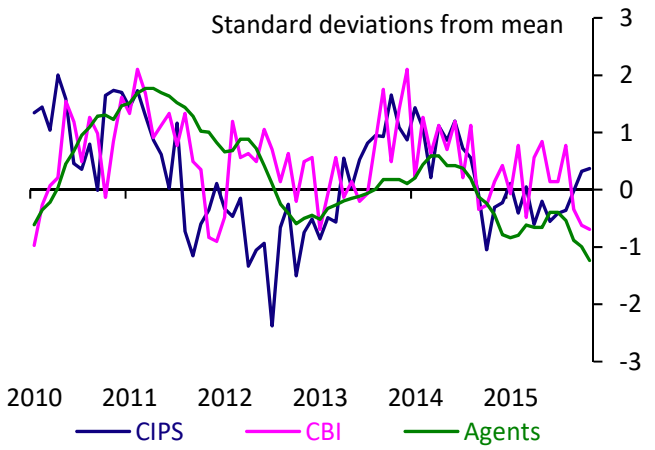
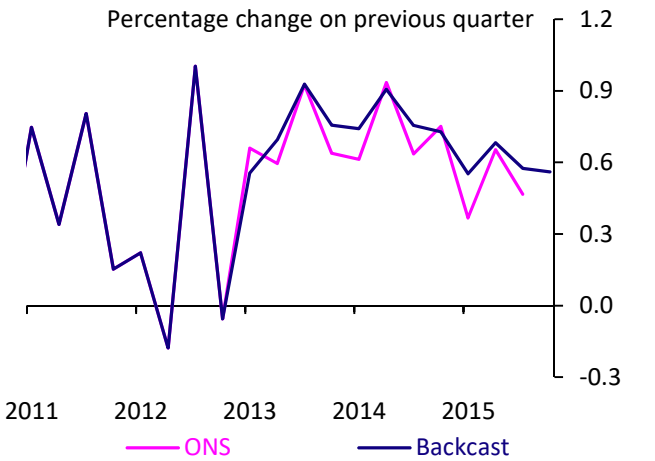


Chart 7: UK GDP growth and UK team backcast



consistent with the gradual downward trend over the past seven months, following the 12 year high in April (Chart 4). That reflects elevated household perceptions of the general economy (for both the past & next year) which have receded further. In contrast, perceptions of household finances are holding up well, consistent with improving income growth; for example, year-on-year growth in compensation of employees picked up to an average 4.6% over Q2 and Q3, broadly in line with its post-1997 average.

It's too soon to assess the impact of Black Friday

Black Friday retail discounts this year have been more drawn-out than last year's frantic one-day reductions, as retailers have sought to better manage the flow of sales. However, there does appear to have been a sales lull beforehand: for example, the Agents cited some delay in electrical goods purchases. Meanwhile, the November CBI Distributive Trades Survey retail sales balance fell to a nine month low (the survey closed well ahead of Black Friday), but expectations for December are strong.

Weaker CBI Service Sector Survey results reflect weaker business & professional firms, while consumer-facing firms are still doing well

Volumes for consumer-facing services firms were little changed in the November CBI SSS, while expectations eased back further, but both remain very strong by historical standards. That suggests a continuation of the solid consumption growth we've seen since mid-2013.

However, the total reported CBI SSS business volumes balance fell back sharply after elevated levels in May and August, due to a swing in the performance of business & professional firms, with expectations more stable in comparison (Chart 5). Overall, the SSS indicates weaker quarterly Private Non-Distribution Services (PNDS) growth in 2015 than last year, which is consistent with the trends in both the Markit/CIPS PMI survey and official services data.

Near-term construction outlook looks positive

Despite a sharp fall in November, the Markit/CIPS PMI construction output index has now been above its historical average for seven months and presents a much more positive picture of the industry than the official data. Taking all the indicators together, including the Agents' score, we think the near-term construction outlook is positive.

Manufacturing indicators have been more mixed

The Markit/CIPS PMI manufacturing output index also remains above its average after falling back from October's 16 month high, in contrast to the latest monthly CBI survey and the Agents' score which are more in line with their averages. That contrast is even starker when we compare the manufacturing export indicators (Chart 6).

No change to our Q4 0.6% nowcast

In light of little data news this month and hence no meaningful movements in our updated nowcast models, our Q4 GDP growth nowcast remains at 0.6% (Chart 7).