

# UK Economic Review

**MAY 2017**

*Based on April 2017 data releases*

**Bedfordshire Chamber of Commerce**

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- UK economic growth slows in Q1 as output from consumer-focused industries weakened
- UK consumer price inflation holds steady, but wage growth slows further
- US GDP growth weakens as the outlook for the Eurozone continues to improve

## UK Economy

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### UK GDP growth slows in Q1 2017...

The UK economy grew by 0.3% in Q1 2017, slower than the growth of 0.7% recorded in Q4. In annual terms, the UK economy grew by 2.1% in Q1, up from the growth of 1.9% recorded in Q4. UK economic output is now estimated to be 8.8% above its pre-recession peak in Q1 2008. Overall, **the first estimate of UK GDP for Q1 2017 supports our view that growth in the UK economy is becoming more subdued.** The BCC is currently forecasting growth of 1.4% for 2017 as a whole and if realised it would be the weakest rate of growth since 2012.

### ...driven by weaker service sector output...

Weakening GDP growth in Q1 was mainly due to growth in service sector output, which accounts for over three quarters of UK economic output, slowing to 0.3% in Q1, from 0.8% in Q4 2016. **This slowdown reflected declines in output from consumer-focused industries** such as retail sales and accommodation services. However, the service sector was still the main driver of the economic activity in the quarter, with industrial production (+0.3%), construction (+0.2%) and agriculture (+0.3%) output adding little to overall UK growth.

### ...as inflation continues to bite...

UK CPI inflation stood at 2.3% in March 2017, unchanged from February but still above the Bank of England's 2% target. Rising prices for food, clothing and footwear were the main upward contributors to change in the rate. However, this was offset by a 23% fall in air fares in March which reflected the shift in the timing of Easter from March to April compared to last year. However, as both the latest QES and official data confirms, **the continued strength in costs at the factory gate suggests that consumer prices will resume their upward trend in the coming months.**

### ...increasing the squeeze on earnings...

In the three months to February 2017, the number of people in employment rose by 39,000. UK unemployment declined by 45,000 over the same period and the UK's unemployment rate stood at 4.7%, down from 5.1% for a year earlier. Annual earnings growth, excluding bonuses, slowed from 2.4% to 2.2%. With consumer price inflation currently holding steady at 2.3%, **prices are now growing at a faster rate than pay growth for the first time since 2014**. If this trend continues it will increase the squeeze on consumer spending, a key driver of UK growth.

### ...and stifling consumer spending...

Retail sales fell by 1.8% in March. On the rolling three month-on-three-month measure – a more reliable indicator of the underlying trend – retail sales dropped by 1.4% in Q1 2017, the biggest decline since Q1 2010. Increasing prices have largely driven this slowdown with average store prices rising by 3.3% on the year, the biggest increase since March 2012. The largest contribution to the rise in store prices was a 16.4% increase in fuel prices. **The latest retail sales figures suggest that the pressure from rising inflation and subdued wage growth are starting to weigh on consumer spending.**

### ...as the UK's trade deficit widens...

The UK trade deficit widened by £0.7 billion to £3.7 billion in February 2017. This was driven by a £0.3 billion rise in imports and a £0.4 billion decline in exports. However, in the three months to February 2017, the trade deficit did narrow by £0.3 billion to £8.5 billion. **Trading conditions for UK exporters are likely to improve over the near term** as weaker sterling and an improving global economic outlook boost demand for UK goods and services. However, the extent of the improvement is likely to be limited by the rising cost of imported goods and raw materials.

### **...US growth weakens to three-year low...**

The first estimate of US GDP revealed that the US economy, the world's largest, grew at an annualised rate of 0.7% in Q1 2017, the slowest rate of growth since Q1 2014 and just a third of the growth of 2.1% recorded in the previous quarter. The slowdown was largely driven by consumer spending, which accounts for two-thirds of US economic output, growing by just 0.3% in Q1, after a 3.5% increase in Q4. Despite the weaker GDP figures in Q1, **the outlook for the US economy remains relatively strong and the IMF currently expect that the US will be the fastest growing economy in the G7 this year.**

### **...as Chinese growth picks up in Q1...**

China - the world's second-largest economy - grew by 1.3% in Q1 2017, over four times the growth of 0.3% recorded in the UK over the same period. **In annual terms, the Chinese economy grew by 6.9% in Q1, the fastest rate of growth since Q3 2015** and above the Chinese government's GDP growth target of 6.5%. However, while China's economy has enjoyed a reasonable start to the year, the near-term outlook looks a little more uncertain with concerns over debt levels and the financial sector likely to weigh on their near-term growth prospects.

### **...and the Eurozone sees solid Q1 growth.**

The first estimate of Eurozone GDP had growth at 0.5% for Q1 2017, unchanged from Q4, but stronger than the UK GDP growth recorded over the same period. In annual terms, the Eurozone economy grew by 1.7% in Q1, down slightly from the growth of 1.8% recorded in Q4. However, France, the Eurozone's second largest economy, grew by 0.3% in Q1 2017, down from growth of 0.5% recorded in Q4. **The outlook for the Eurozone has improved notably over the past year, boosted by less austerity and the European Central Bank's (ECB) stimulus programme.**

### The bottom line...

*The latest data releases suggest that the UK economy is entering a more challenging period with rising inflation a key risk for both consumers and businesses. While it is important to get a good Brexit deal, more must be done to address the longstanding domestic issues, including the escalating burden of upfront business costs.*

