

# Monthly Economic Review

**JANUARY 2018**

*Based on December 2017 data releases*

**Bedfordshire Chamber of Commerce**

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- Annual UK GDP growth revised up and the UK's current account deficit narrows
- UK inflation rises above 3% as household spending outstrips income
- Japan records the longest stretch of unbroken GDP growth in over 20 years

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## Annual UK GDP growth revised upwards...

The third official estimate of UK economic output (GDP) recorded growth of 0.4% in Q3 2017, unrevised from the previous estimate and up slightly from the growth of 0.3% recorded in Q2. However, partly due to upwards data revisions to GDP growth in the second half of 2016, the UK economy grew by 1.7% in annual terms in Q3, up from the previous estimate of 1.5%. Similarly, **UK GDP growth for 2016 as a whole was also revised up from 1.8% to 1.9%**. UK economic output is now 10.2% above its pre-recession peak.

## ...as household spending outstrips income...

Household spending, which accounts for around two-thirds of UK economic output, grew by 0.5% in Q3. The latest data also indicates that consumers are drawing down savings or borrowing to help fund spending. While real disposable incomes grew by just 0.2% in Q3, household net borrowing increased by 70%. **UK households have now been net borrowers for four successive quarters, the longest period since records began in 1987. Similarly, the households' saving ratio fell to 5.2% in Q3 2017, the second lowest rate since 1999.**

## ...while Black Friday boosts retail sales...

**Retail sales rose by 1.1% in November, more than double the 0.5% rise in October.** The increase in the month was mostly driven by a 2.9% rise in sales of household goods as 'Black Friday' played a key role in boosting activity. On the rolling annual three month-on-three-month measure – a better indicator of the underlying trend – retail sales rose by 1.6% in November, down from the growth of 1.7% recorded in the previous three-month period. With pay growth continuing the lag to behind price growth consumer spending is likely to remain under pressure in near term, squeezing retail sector activity.

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## ...inflation drifts above 3%...

**CPI inflation in the UK stood at 3.1% in November 2017, the highest rate since March 2012.**

The largest upward contribution to change in the rate came from air fares. Inflation is now more than 1% above the Bank of England's 2% target, triggering a letter of explanation from Mark Carney to the Chancellor. While inflation is expected to remain elevated in the short-term, it is likely to moderate this year as the impact of the post-EU referendum slide in sterling fades. However, inflation is likely to outpace earnings until 2019, squeezing consumer spending, a key driver of UK economic growth.

## ...UK job vacancies rise to record high...

In the three months to October, the number of people who are in employment fell by 56,000, the second successive decline. However, the number of people out of work fell by 26,000 over the same period and the jobless rate remained at 4.3%, the joint lowest since 1975. **The latest UK jobs data confirms that the UK labour market continues to face a number of key challenges.** There is further evidence of the growing skills shortage with the number of job vacancies rising by 45,000 over the past year to 798,000, the highest since comparable records began in 2001.

## ...and rebalancing is still a major challenge...

The UK's current account deficit (the gap between what the UK earns and spends) narrowed to £22.8 billion in Q3 2017, from a deficit of £25.8 billion in Q2. **The UK's current account deficit is now equivalent to 4.5% of GDP**, down from 5.1% in Q2. The improvement in the current account deficit was mainly driven by a rise in income from UK owned assets overseas, including foreign direct investment by UK firms. However, despite the improvement, the UK's current account deficit in Q3 was more than three times the long-term average of -1.4% and confirms that the weakness in the UK's external position remains with rebalancing the UK economy still a major challenge.

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### **...as does cutting the deficit...**

Public sector borrowing (excluding the public-sector banks) stood at £8.7 billion in November 2017, £0.2 billion lower than in November 2016. In the current financial year-to-date (April to November 2017), Public sector net borrowing stood at £48.1 billion, the lowest year-to-date net borrowing since 2007. **The UK's fiscal position in the month was boosted by a 4.5% rise in income tax receipts.** While government borrowing for this financial year is likely to undershoot the OBR's forecast, subdued GDP growth and productivity is likely to increase the pressure on the UK's fiscal position in the near term.

### **...as the IMF downgrades UK outlook...**

The International Monetary Fund (IMF) has downgraded its outlook for the UK economy. The IMF cut its GDP forecast for 2017 to 1.6%, from its previous forecast of 1.7%. However, the IMF's latest outlook remains slightly more optimistic than the latest BCC growth forecast for this year of 1.5%. The IMF forecast for UK growth in 2018 was unchanged at 1.5%, also above the BCC's latest GDP growth forecast for the year of 1.1%. Overall, **the IMF's latest forecasts of UK GDP reinforce our own view that the UK economy is set too slow further in 2018.** This is in marked contrast to an improving growth outlook for the global economy.

### **...while US tightens monetary policy...**

**The Federal Reserve raised interest rates in the US by 0.25% percentage points in December to a target range between 1.25% and 1.5%, the third rate rise in 2017.** The move reflected an improving outlook with the US economy growing by a healthy annualised rate of 3.2% in Q3 2017, according to the third official estimate. Further rises in US interest rate are likely in 2018 which will place further downward pressure on the value of sterling. However, we still expect the next increase in UK official interest rates, to 0.75%, will occur in the second half of 2019.

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## ...Japan's GDP growth revised up in Q3.

Japan, the world's third-largest economy, grew by 0.6% in Q3 2017, double the previous estimate of 0.3%. Japan's economy has now grown for seven straight quarters – the longest stretch of unbroken growth since 1994. In annual terms, Japan's economy grew by 2.5%. While consumer spending remains weak amid subdued wage growth, rising exports driven by an improving global economy and strong investment have helped to boost growth. **Overall, the latest Japanese economic growth data suggests that 'Abenomics' (combining monetary and fiscal stimulus with structural reform) continues to have a positive effect on Japan's economy.**

## The bottom line...

*Taken together, December's data suggest that the UK economic growth is set to remain underwhelming in 2018. With economic conditions likely to become more sluggish over the near term, it is vital that more is done to support firms looking to recruit and grow their business, including tackling the high up-front taxes and costs of doing business in the UK.*

