Monthly Economic Review

September 2016

(Based on August 2016 data releases)

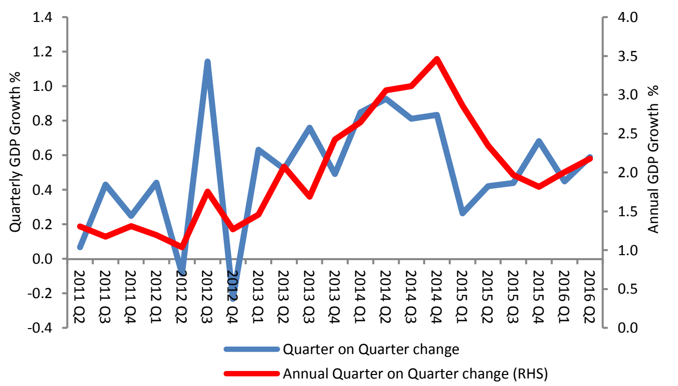
Monthly headlines:

- UK GDP growth unrevised in Q2, with consumer spending driving growth in the quarter
- UK set for a prolonged period of rising inflation, as the jobs market continues to strengthen
- US interest rates likely to rise by the end of 2016 despite downward revision to growth

UK GDP growth in Q2 unrevised at 0.6%...

The second official estimate for Q2 2016 growth in UK GDP was unrevised at 0.6%, compared to the 0.4% rise in Q1. This is the 14th consecutive quarter of positive growth **(see Chart 1)**. The UK economy grew by 2.2% in Q2 2016, compared to the same quarter in 2015. While UK economic output is now 7.7% above its Q1 2008 pre-recession peak, GDP per head is still just 1.2% above its pre-recession peak. Overall, **the latest GDP figures provide further evidence that the UK economy expanded at a solid rate in the run-up to the EU referendum.**

Chart 1: Real GDP Growth

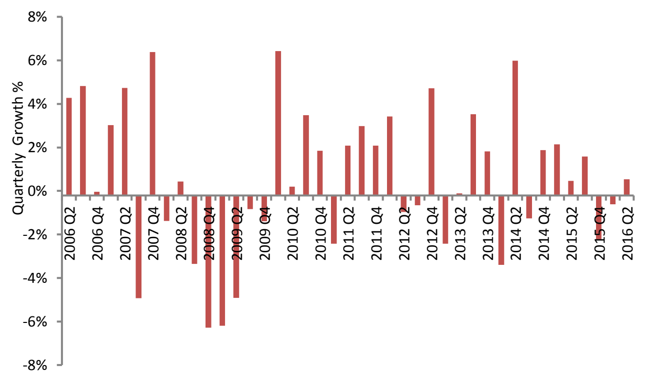


Source: ONS GDP second estimate, Q2 2016

...as consumers continue to drive growth...

The latest Q2 2016 GDP estimate revealed that business investment grew by 0.5% in Q2. In annual terms, business investment was 0.8% lower than in Q2 2015 **(see Chart 2)**. The latest BCC Quarterly Economic Survey (QES) revealed that investment intentions improved in Q2 among services firms, but declined among manufacturing firms. However, despite the pick-up in business investment in Q2, consumer spending, which accounts for around two-thirds of UK economic output, grew by 0.9% in Q2 and was the main driver of growth in the quarter.

Chart 2: UK Business Investment

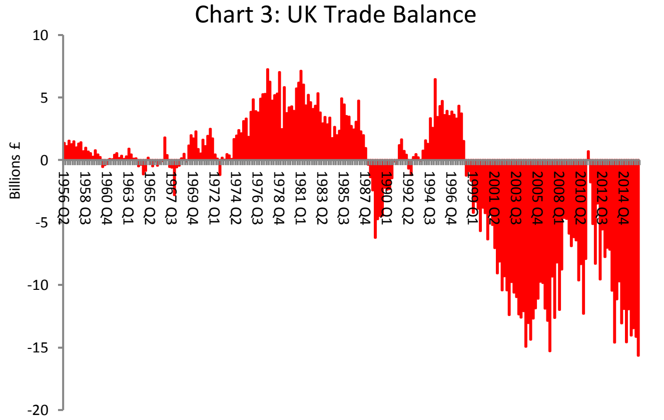


Source: ONS Business Investment, Q2 2016

...trade remains a drag on growth...

The UK's trade deficit widened from £14.1 billion in Q1 2016 to £15.7 billion in Q2 2016, the biggest deficit on record **(see Chart 3)**. This was driven by a 1% rise in imports in Q2, ten times the 0.1% increase in exports over the same period. As a consequence, net trade was a drag on GDP growth in the quarter, knocking 0.3 percentage points off Q2 growth. Overall, **the latest GDP figures confirm that rebalancing the UK economy away from consumer spending and towards exports remains a major challenge.**

Chart 3: UK Trade Balance



Source: ONS GDP second estimate, Q2 2016

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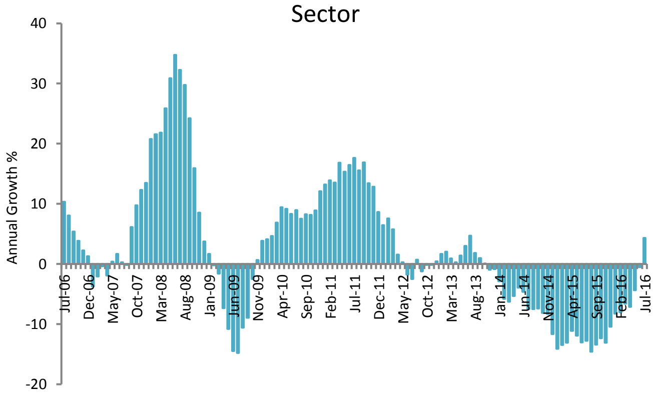
…inflation in the UK is set to rise…

CPI inflation rose to 0.6% in July 2016, the highest rate since November 2014 and up from the 0.5% rise recorded in July. The increase was mainly driven by rising fuel, alcoholic drinks and hotel room prices. **There are signs that we could see a prolonged period of increasing inflation** with input prices faced by manufacturers rising by 4.3% in the year to July. This was the first increase since September 2013 **(see Chart 4)** as the post-EU referendum slide in sterling pushes up the cost of imports. However, if economic growth slows as many expect, then the extent of the price rises is likely to be limited.

Chart 4: Total Input Prices, Manufacuturing Sector

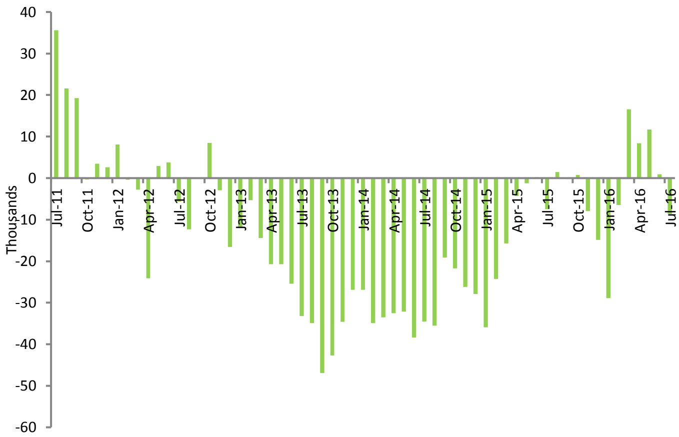


Source: ONS Producer Prices, July 2016

…UK jobs market continues to strengthen…

In the three months to June 2016, UK employment rose by 172,000 compared with the previous three months. The number of people who are unemployed fell by 52,000 over the same period. This mirrors the latest QES survey data which showed that before the EU referendum, businesses were confident enough to recruit despite a slowing economy. The claimant count, the first post-referendum labour market data, fell by 8,600 in July **(see Chart 5)**. However, labour market indicators tend to lag behind the wider economy so **it is likely to be some time before the full post-referendum employment picture emerges.**

Chart 5: UK Claimant Count

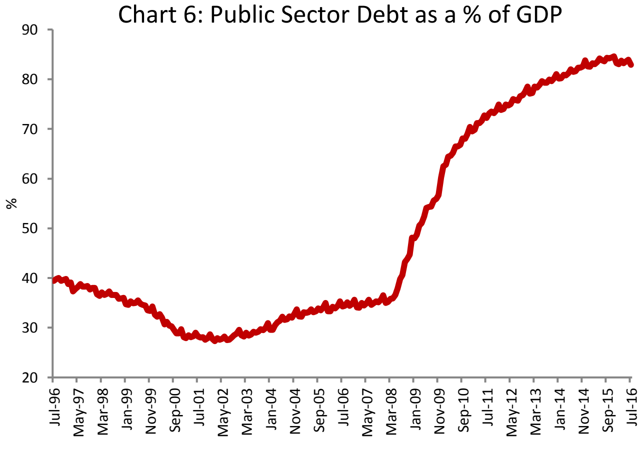


Source: ONS Labour Market Data, August 2016

…deficit reduction proving a real challenge.

The UK's public sector finances (excluding public sector banks) recorded a surplus of £1 billion in July 2016, down by £0.2 billion from July 2015. July is typically a month of surplus for the public finances, due to the timing of corporation tax payments and self-employed tax returns. However, the UK's public sector net debt currently stands at 82.9% of GDP, more than double pre-crisis levels **(see Chart 6). If economic growth slows in the coming months, the government is likely to face an increasingly uphill task to generate the tax receipts needed to make meaningful progress in cutting the deficit.**

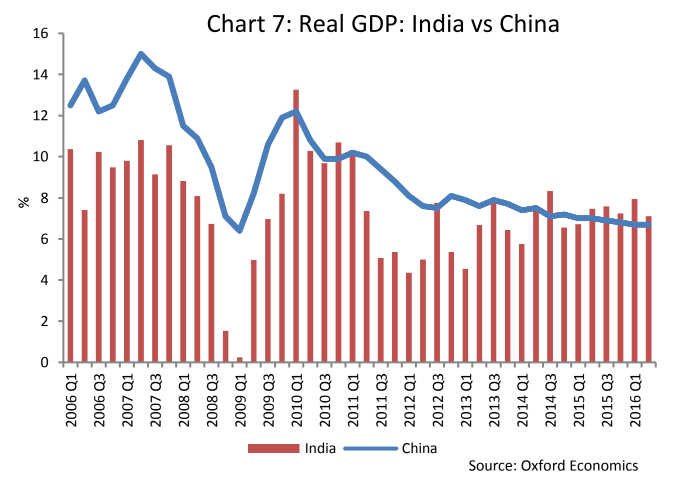
Chart 6: Public Sector Debt as a % of GDP



Source: Public Sector Finances, July 2016

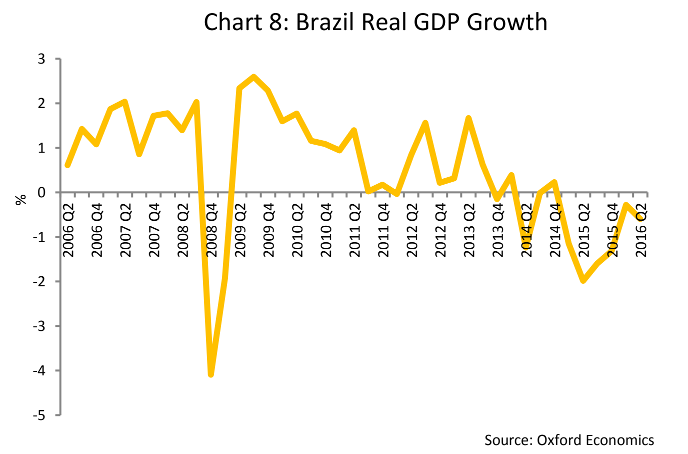
India's economy slowed in Q2...

India's economy, the world's seventh-largest, grew by 7.1% in annual terms in Q2 2016, the slowest rate of growth since Q1 2015 and down from the growth of 7.9% recorded in the previous quarter. **Weaker consumer demand was only partly offset by rising exports and government spending.** However, despite the slowdown, India continues to outpace China which grew by 6.7% in the quarter **(see Chart 7)**. With consumer spending, a key driver of India economic output, likely to continue to be supported by a growing middle class, the outlook for India's economy remains relatively good.



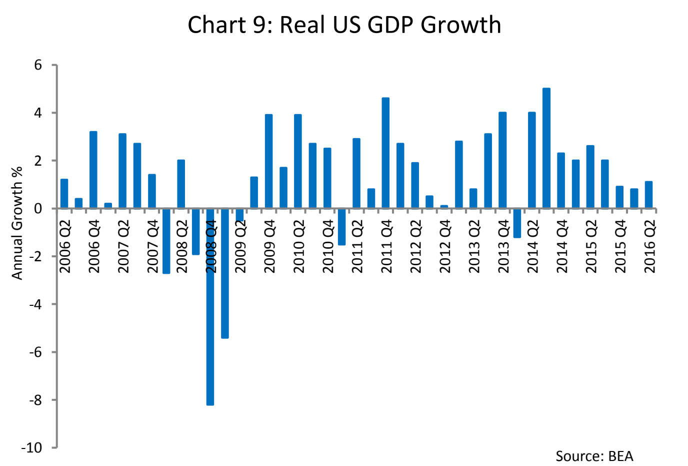
...as Brazil's recession deepens...

Brazil, the largest economy in Latin America, contracted by 0.6% in Q2 2016, the sixth successive quarterly decline **(see Chart 8)**. In annual terms, Brazil's economic output was 3.8% lower compared to Q2 2015. **Brazil's economy continues to be hampered by high inflation and unemployment as well as weakening commodity prices and significant political unrest.** However, there are some emerging bright spots for Brazil with fixed investment growing for the first time since Q3 2013 and exports increasing for the third successive quarter.



...and US growth is revised downwards.

The second estimate of US GDP for Q2 2016 revealed that the US economy grew by 1.1% in Q2 2016, compared to the same quarter in 2015 **(see Chart 9)**, lower than the previous estimate of a 1.2% increase, but up from the growth of 0.8% recorded in the previous quarter. The downward revision mainly reflected weaker state and local government spending and an upward revision to imports. However, **despite the subdued growth picture for the economy for the first half of this year, US interest rates are still likely to rise again before the end of the year.**



***Bottom line**: UK economic growth remains unbalanced with too great a reliance on consumer spending. If household spending is squeezed in the coming months as inflation rises, it is vital that the upcoming Autumn Statement is used to support other areas of the economy, including greater support for firms looking to invest.*

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Economic summary chart

Deteriorating (red) | No change (yellow) | Improving (green)

Sector	Indictors (sources)	Aug-15	Sep-15	Oct-15	Nov-15	Dec-15	Jan-16	Feb-16	Mar-16	Apr-16	May-16	Jun-16	Jul-16	Aug-16
Household	Retail Sales (ONS)	Improving	Improving	Improving	Deteriorating	Improving	Deteriorating	Improving	Deteriorating	Deteriorating	Improving	Improving	Deteriorating	Improving
	Consumer Confidence (GfK NOP)	Improving	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Deteriorating	No change	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Improving
	House Prices (Halifax)	Deteriorating	Improving	Deteriorating	Improving	Deteriorating	Improving	Deteriorating	Deteriorating	Improving	Deteriorating	Improving	Improving	Deteriorating
	New car sales (SMMT)**	Improving	Improving	Improving	Deteriorating	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Deteriorating	Improving
	Mortgage approvals (Bank of England)	Improving	Improving	Deteriorating	Improving	Improving	Improving	Improving	Improving	Improving	Deteriorating	Improving	Deteriorating	Deteriorating
Business	Business confidence (BCC)***	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating
	Business lending (Bank of England)	Improving	Improving	Deteriorating	Improving	Deteriorating	Deteriorating	Improving	Improving	Deteriorating	Deteriorating	Improving	Improving	Improving
	Service sector output (ONS)	Improving	Improving	No change	Improving	Improving	Improving	Improving	Improving	Improving	Deteriorating	Improving	No change	Improving
	Production output (ONS)	Deteriorating	Deteriorating	Improving	Deteriorating	Improving	Deteriorating	Deteriorating	Improving	Deteriorating	Improving	Improving	Deteriorating	Improving
	Investment intentions (BCC)**	Deteriorating	Deteriorating	Improving	Improving	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating
Labour market	Employment (ONS)	Deteriorating	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving
	Unemployment (ONS)	Deteriorating	Deteriorating	Improving	Improving	Improving	Improving	Improving	Improving	Deteriorating	Improving	Improving	Improving	Improving
	Claimant count (ONS)	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Improving	Deteriorating	Improving	Improving	Deteriorating	Improving
	Earnings (ONS)	No change	Improving	Improving	No change	Deteriorating	Deteriorating	Improving	Improving	Deteriorating	Deteriorating	Improving	Deteriorating	Improving
	Economic Inactivity (ONS)	Improving	Improving	Deteriorating	Improving	Improving	Improving	Improving	Improving	Improving	Improving	No change	Improving	Improving
Government	Public sector net borrowing (ONS)**	Improving	Deteriorating	Improving	Deteriorating	Deteriorating	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Deteriorating
	Public sector net debt % of GDP (ONS)**	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Improving	Deteriorating	Improving	Deteriorating	No change	Improving	Improving
	Tax receipts (HMRC)**	Improving	Improving	Improving	Improving	Improving	Deteriorating	Improving	Improving	Improving	Improving	Improving	Improving	Improving
	Current Budget Deficit (ONS)**	Improving	Deteriorating	Improving	Deteriorating	Deteriorating	Improving	Improving	Improving	Improving	Improving	Improving	Improving	Improving
External	UK trade balance (ONS)	Deteriorating	Deteriorating	Improving	Improving	Deteriorating	Deteriorating	Improving	Deteriorating	Improving	Improving	Improving	Deteriorating	Deteriorating
	Export Sales (BCC)***	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating
	Export orders (BCC)***	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Improving	Improving	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating
Financial	Exchange rate (Bank of England)	Improving	Improving	Improving	Improving	Improving	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating
	Equity Prices (Bloomberg)	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Deteriorating	Improving	Deteriorating	Improving	Improving
	10 year Government bonds (Bloomberg)	Improving	Improving	Deteriorating	Improving	Improving	Improving	Improving	Deteriorating	Deteriorating	Improving	Improving	Improving	Deteriorating

*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 estimates.