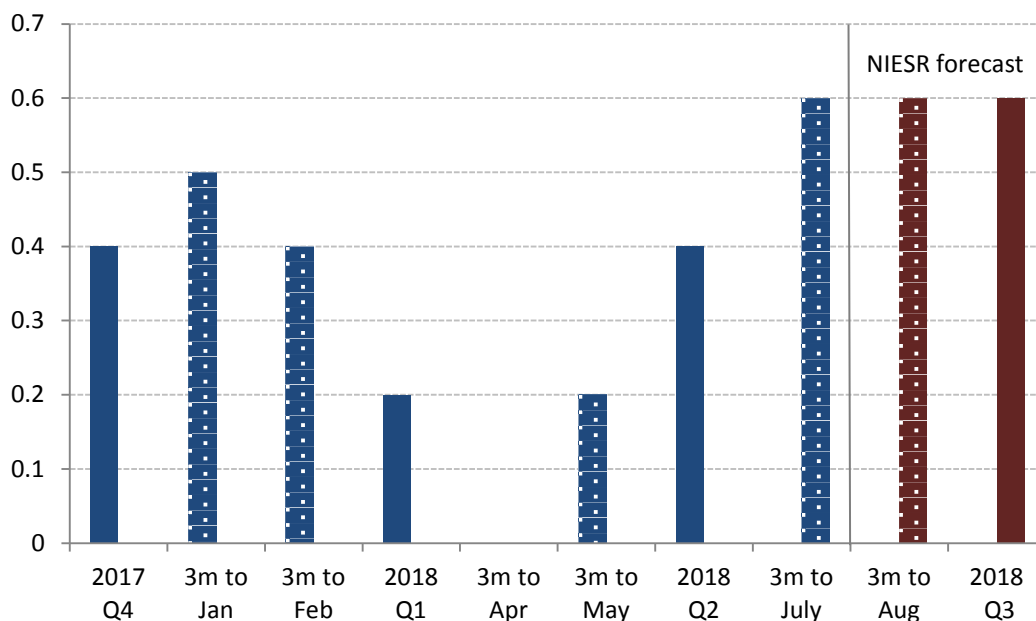


Press Release

NIESR MONTHLY GDP TRACKER: September 2018

UK economic growth gathers momentum

Figure 1: UK GDP growth (3 months on previous 3 months, per cent)



Source: NIESR, ONS

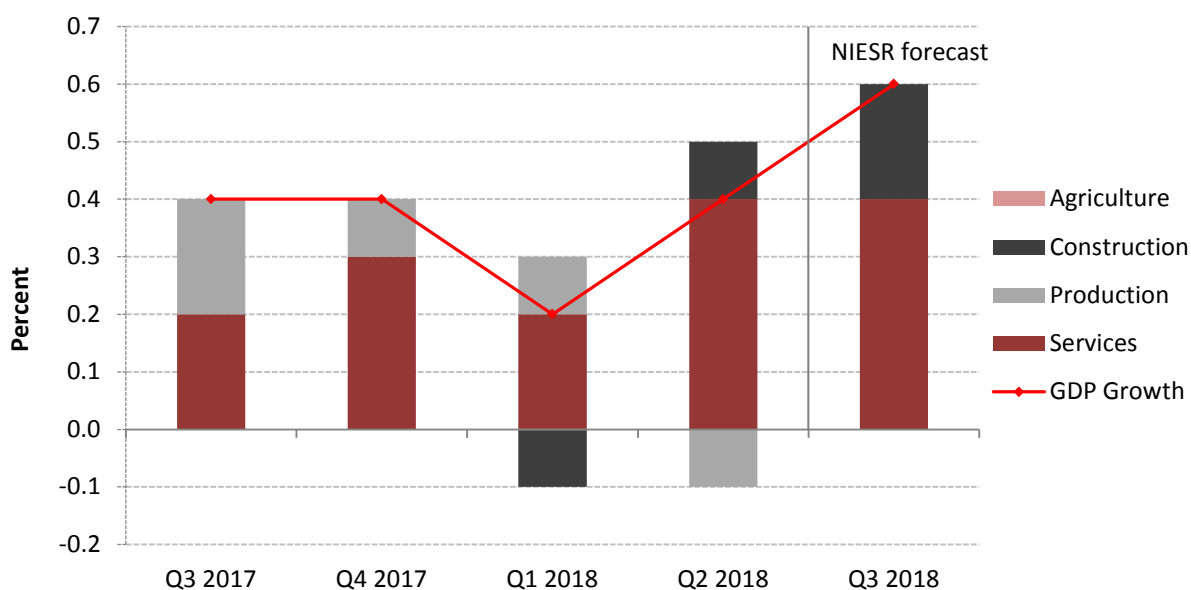
Note: the solid bars show the 3m/3m growth rate for complete calendar quarters and the shaded areas show rolling 3m/3m growth rate for the intervening months. There may be inconsistencies in the growth rate arising from rounding

Main points

- Latest economic data confirms that the UK economy has recovered from a soft patch earlier in the year and is now growing at a pace that is above potential.
- According to new ONS statistics published this morning, the UK economy expanded by 0.6 per cent in the three months to July compared with the previous three months after growing by 0.4 per cent in the second quarter (three months to June). The outturn was slightly higher than the 0.5 per cent monthly GDP forecast that we published last month for the same period. **Building on the official data, our monthly GDP Tracker suggests that the economy is set to maintain the 0.6 per cent pace for the remainder of the third quarter.**
- The official data for July shows that retail sales responded strongly to recent warm weather and the football World Cup as did construction sector output which has recovered after a lacklustre performance at the start of 2018. Growth for the third quarter as a whole is likely to be driven by the service and construction sectors.

Amit Kara, Head of UK macroeconomic forecasting, said *“The economy gathered momentum in the three months to July after rebounding from the weather-related disruption in the first quarter and is now growing at a speed that is faster than our estimate of potential. Looking ahead into August and September, we see the economy maintain the 0.6 per cent three-month-on-three-month growth rate driven mainly by growth in the services and construction sectors.”*

Figure 2: Contributions to quarterly GDP growth (percentage points)



Production (14 per cent of GDP)

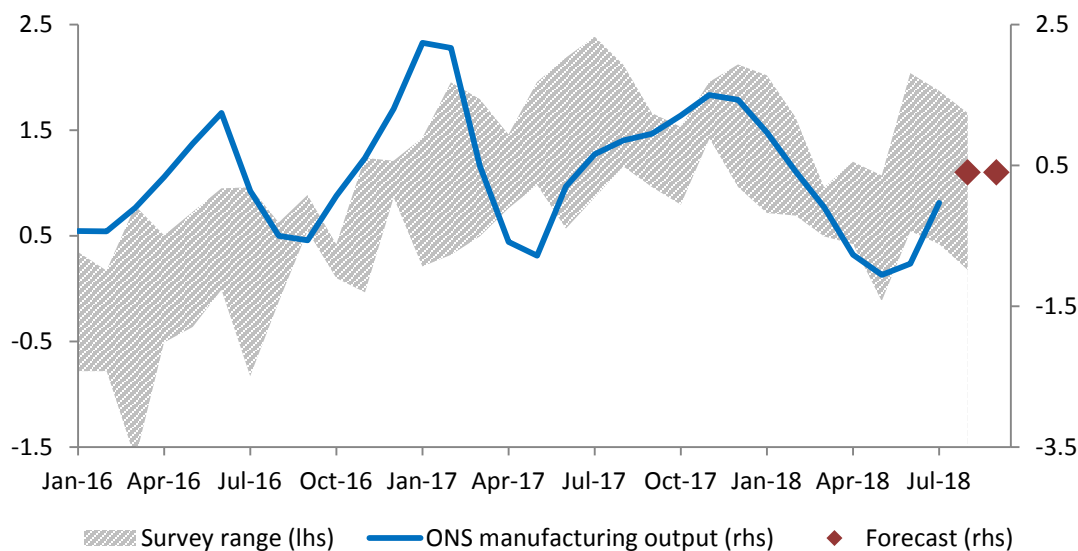
The production sector comprises of the manufacturing sector, mining and quarrying; electricity gas, steam and air conditioning; water supply and sewerage; and oil and gas extraction. Production sector output fell by 0.5 per cent in the three months to July compared with the previous three months mainly because of a 4.5 per cent fall in electricity and gas supply. This drop is primarily because of warmer-than-usual average temperature in May to July.

According to the ONS, the dominant manufacturing sector suffered a notable slowdown in the first half of this year. Output has bounced higher since then and is set to expand by 0.4 per cent in the third quarter according to our latest forecast.

Recent UK survey data points to a modest expansion in manufacturing sector output (Figure 3) with mixed signals from the major business surveys. For example, the JP Morgan global manufacturing PMI composite balance shows that the sector lost momentum in July and August with the latest outturn registering a 21-month low. Consistent with that, the analogous UK balance fell to a 25-month low mainly driven by a slowdown in export orders. The CBI Industrial Trends Survey, by contrast, suggests that the growth is broad-based and also at a speed that is faster than the long run average.

Mining and quarrying is a small and erratic component of the industrial production sub-component. According to the ONS, the oil and gas extraction rose by 5 per cent in July mainly because of an end to planned maintenance work that was carried out in June.

Figure 3: Manufacturing sector surveys and ONS manufacturing sector growth (3 months on previous 3 months, per cent)



Source: ONS, CBI, Markit, Bank of England Agents, NIESR

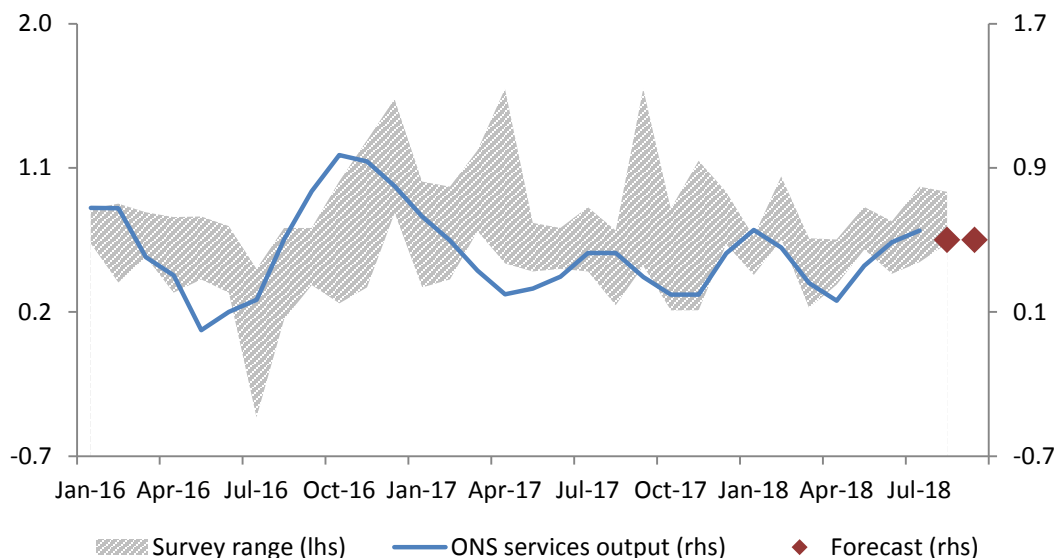
Services (80 per cent of GDP)

Growth in the dominant service sector recovered from 0.3 per cent in the first quarter of this year to 0.5 per cent in the second quarter and to 0.6 per cent in the three months to July. The outturn for the three months to July was slightly faster than our 0.5 per cent forecast that was published last month and the upside surprise is explained by the strength in retail sales. Retail trade performed strongly in the three months to July with a growth rate of 4.5 per cent.

Some of that strength in retail sales is likely to be temporary as the effects of the warm weather fade and the influence of the football World Cup drops out. According to results from surveys such as the BRC-KPMG the retail sector lost momentum in August whereas the quarterly CBI Distributive Trades survey indicates an above-average pace of growth.

Turning to the service sector as whole, business surveys concur with the healthy growth rate that is evident in the official data (Figure 4). The PMI-Markit Service sector survey not only points to a pick-up in business activity, the survey also indicates that incoming business increased in August. Likewise, the latest CBI quarterly Service Sector Survey suggests a steady pace of growth in business volumes. The outlook further out however, appears somewhat more cautious with the business optimism component of the PMI-Markit survey nudging lower in August to a five month low mainly because of Brexit-related uncertainty.

Figure 4: Service sector surveys and ONS manufacturing sector growth (3 months on previous 3 months, per cent)



Source: ONS, CBI, Markit, Bank of England Agents, NIESR

Construction (6 per cent of GDP)

The construction sector has rebounded in the second quarter with growth of 0.9 per cent compared with a 0.8 per cent fall in the first quarter. According to official data, output continued to expand in July with the three month growth rate at 3.3 per cent. The latest July outturn was slightly lower than our forecast of 3.4 per cent that we published last month. Some of that recent strength in construction output is likely to reflect a catch-up after the weather-related disruption earlier in the year.

Looking ahead into August and September, the latest reading from the IHS Markit/CIPS construction PMI survey signals a loss in growth momentum as the catch-up effect fades.

Outlook for the whole economy in 2018

NIESR publishes a comprehensive global and UK macroeconomic forecast each quarter. Under the central scenario of our August forecast, which was conditioned on a soft Brexit, we see GDP growth of 1.4 per cent in 2018. Our monthly GDP tracker broadly confirms that view. We emphasised in August that the risks to that forecast were tilted to the downside because of economic and political uncertainties related to Brexit negotiations. This uncertainty continues to act as a drag on investment spending and also a key risk going forward according to the Bank of England Decision Maker Panel. At the global level, there are some very early signs in business surveys that the risk from an escalation in protectionism and a more hostile international trading environment is holding back investment and activity more generally. Input costs for businesses are also rising.

Our next full UK and global forecast will be published in November.

Health warning:

NIESR's short-term predictions of monthly GDP growth are based on bottom-up analysis of recent trends in the monthly sub-components of GDP. These predictions are constructed by aggregating statistical model forecasts of ten sub-components of GDP. The statistical models that have been developed make use of past trends in the data as well as survey evidence to build short-term predictions of the sub-components of monthly GDP. These provide a statistically-based guide to current trends based on the latest available data. Each month these predictions will be updated as new ONS data and new surveys become available.

It is important to stress that the timelier NIESR guide to quarterly GDP growth will be less reliable than the subsequent ONS data releases as its data content is lower, particularly for estimates of the current quarter which in some months will be based only on forecasts rather than hard data. To mitigate this issue, NIESR will provide a guide to average errors based on past performance. NIESR will also each month provide clear guidance on how the latest news has caused its estimates of GDP growth in the current and preceding quarter to change and thereby quantify how the short-term outlook is being affected by recent data releases.

As we have adopted a new bottom-up methodology for producing estimates of GDP growth for the current and preceding quarters, we do not yet have a track record of estimates produced by the new approach. Nevertheless we would expect our estimates for GDP growth in the quarter prior to publication to be at least as reliable as those using the old methodology. Using the old methodology, the root mean square error of NIESR's early estimates of GDP for complete calendar quarters was 0.188% point for the period 1999Q3 – 2015Q4 once a noticeable outlier in 2010Q4 is excluded.

Forecast Error Analysis: Quarterly GDP growth (%)

Quarter	ONS first estimate	ONS latest estimate	NIESR estimate made in next quarter (early)	NIESR Prediction made in same quarter (very early)	Error in early estimate	Error made in very early estimate	ONS latest – first
2016Q4	0.6	0.7	0.5	0.7	0.1	-0.1	0.1
2017Q1	0.3	0.4	0.5	0.6	-0.2	-0.3	0.1
2017Q2	0.3	0.2	0.3	0.4	0.0	-0.1	-0.1
2017Q3	0.4	0.4	0.4	0.4	0.0	0.0	0.0
2017Q4	0.5	0.4	0.6	0.4	-0.1	0.1	-0.1
2018Q1	0.1	0.2	0.2	0.5	0.1	-0.4	0.1
2018Q2	0.4	0.4	0.4	0.0	0.0	0.4	0.0
Average absolute error					0.07	0.16	0.07

To check how our methodology would work in real time we have gone back to late 2016 to produce judgement-free forecasts of GDP growth in future months based on the monthly data series available for the components in November 2016 (this is the earliest

vintage currently available on the ONS website) and in each subsequent three months. We can then use these projections to calculate the forecast quarter-on-quarter growth rates for the current quarter and can compare these to the ONS first estimates of quarterly growth. The average absolute error for the 7 quarters that we have calculated was 0.16 % points. The largest error was for 2018Q1 when our GDP tracker had initially expected growth to be 0.5%, 0.4% points higher than the ONS first estimate of GDP growth that was published in April 2018.

Notes for editors: For further information please contact the NIESR Press Office or Paola Buonadonna on 020 7654 1923/ p.buonadonna@niesr.ac.uk

National Institute of Economic and Social Research
2 Dean Trench Street
Smith Square
London, SW1P 3HE
United Kingdom

Switchboard Telephone Number: 020 7222 7665
Website: <http://www.niesr.ac.uk>

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Table 1: Summary Table of GDP growth (2016=100)

2016=100	GDP index	Index of Services	Index of Services - Components				Index of Production	Index of Production - Components				Index of Construction	Agriculture
			Business services and finance	Government and other services	Distribution, Hotels and Restaurants	Transport, Storage and Communications		Manufacturing	Electricity, gas, steam and air conditioning	Mining and Quarrying	Water Supply, Sewerage and Waste Management		
Latest weights	1000	793	334	220	133	106	140	101	12	17	10	60	7
Jan-18	103.1	102.7	103.3	100.2	102.7	106.1	103.3	104.3	98.1	102.6	103.4	107.7	102.1
Feb-18	102.9	102.5	102.9	100.2	102.8	105.4	103.6	104.1	101.5	100.6	105.0	107.2	101.6
Mar-18	102.9	102.7	103.2	100.5	101.9	106.2	103.3	103.7	103.0	97.2	105.7	105.3	101.4
Apr-18	103.1	103.0	103.5	100.7	102.9	106.8	102.6	102.5	100.4	104.2	105.0	105.2	101.6
May-18	103.4	103.2	103.4	100.6	104.1	107.2	102.3	103.2	96.8	99.4	106.8	108.2	101.8
Jun-18	103.5	103.2	103.1	100.7	103.8	108.0	102.8	103.6	97.1	98.9	108.5	109.8	101.6
Jul-18	103.8	103.5	103.7	100.5	104.6	107.7	102.9	103.4	97.3	102.1	107.8	110.3	101.4
Aug-18	104.0	103.7	103.9	100.5	104.7	108.2	102.8	103.5	97.6	100.4	107.9	111.0	101.3
Sep-18	104.2	103.9	104.2	100.5	104.8	108.6	103.0	103.7	98.3	98.9	108.3	111.2	101.4
Percentage change, 3 months on previous 3 months													
Apr-18	0.0	0.2	0.2	0.4	0.0	0.0	0.1	-0.8	1.9	4.0	1.9	-2.1	-1.1
May-18	0.2	0.4	0.3	0.4	0.4	0.5	-0.4	-1.1	-0.3	4.7	1.8	-1.7	-0.5
Jun-18	0.4	0.5	0.2	0.4	1.1	1.4	-0.8	-0.9	-2.7	0.7	2.0	0.9	0.0
Jul-18	0.6	0.6	0.2	0.1	1.6	1.4	-0.5	0.0	-4.5	-0.5	2.3	3.3	0.1
Aug-18	0.6	0.5	0.2	0.0	1.4	1.2	0.1	0.4	-2.7	0.2	2.1	3.9	-0.2
Sep-18	0.6	0.5	0.6	-0.2	1.1	0.8	0.3	0.4	-0.4	-0.4	1.2	2.9	-0.3
Percentage change, month on same month in previous year													
Apr-18	1.5	1.6	2.4	0.2	0.9	3.2	1.9	1.1	3.8	5.6	2.6	-1.3	-1.0
May-18	1.5	1.5	1.6	0.2	2.3	3.6	1.2	1.6	-1.4	-0.2	3.9	1.5	-0.8
Jun-18	1.3	1.2	1.1	0.3	1.4	3.4	1.2	1.5	-0.1	-4.4	5.3	2.3	-1.2
Jul-18	1.6	1.6	1.7	0.3	1.9	3.6	1.0	1.1	-1.4	-0.8	5.2	3.6	-1.7
Aug-18	1.5	1.6	1.7	0.1	2.1	3.8	0.8	1.1	-1.8	-1.4	5.8	2.6	-2.2
Sep-18	1.7	1.9	1.9	0.4	2.7	3.8	0.2	0.4	-2.2	-4.4	7.4	3.8	-2.3
Percentage change, month on previous month													
Mar-18	0.0	0.2	0.3	0.3	-0.9	0.8	-0.3	-0.4	1.5	-3.4	0.7	-1.8	-0.2
Apr-18	0.2	0.3	0.3	0.2	1.0	0.6	-0.7	-1.2	-2.5	7.2	-0.7	-0.1	0.2
May-18	0.3	0.2	-0.1	-0.1	1.2	0.4	-0.3	0.7	-3.6	-4.6	1.7	2.9	0.2
Jun-18	0.1	0.0	-0.3	0.1	-0.3	0.7	0.5	0.4	0.3	-0.5	1.6	1.5	-0.2
Jul-18	0.3	0.3	0.6	-0.2	0.8	-0.3	0.1	-0.2	0.2	3.2	-0.6	0.5	-0.2
Aug-18	0.2	0.2	0.2	0.0	0.1	0.5	0.0	0.1	0.3	-1.7	0.1	0.6	-0.1
Sep-18	0.2	0.2	0.3	0.0	0.2	0.4	0.1	0.2	0.7	-1.5	0.3	0.2	0.0

Note: There may be inconsistencies in the growth rates arising from rounding.