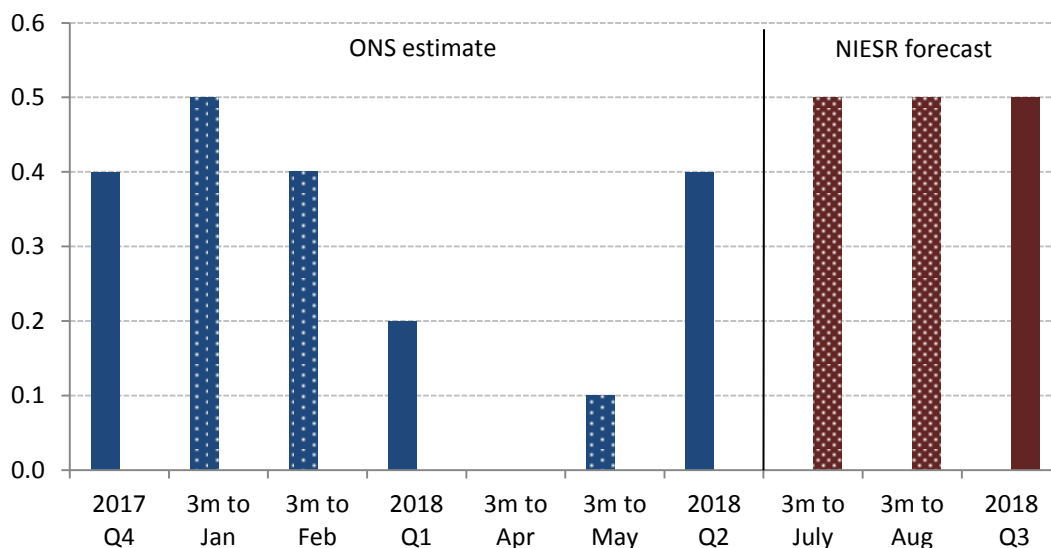


Press Release

NIESR MONTHLY GDP TRACKER: August 2018

UK economic growth back on track

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



Source: NIESR, ONS

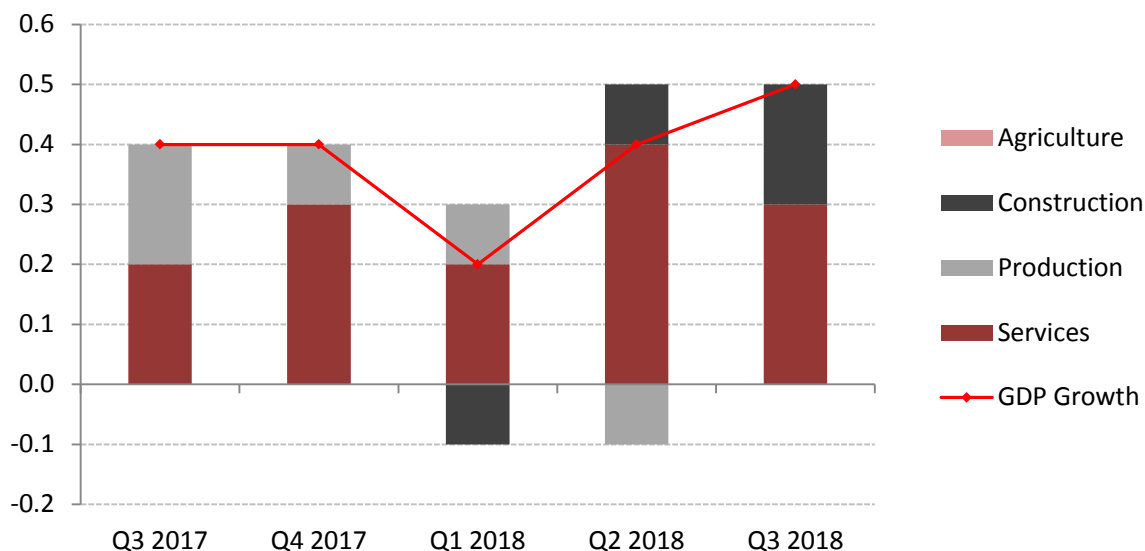
Note: the solid bars show the 3m/3m growth rate for complete calendar quarters and the shaded areas show rolling 3m/3m growth rate for the intervening months. There may be inconsistencies in the growth rate arising from rounding

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 at or slightly above potential.
- According to new ONS statistics published this morning, the UK economy expanded by 0.4 per cent in the second quarter. The outturn was in line with the monthly GDP forecast that we published last month for the same period and is close to our estimate of potential growth rate. **Building on the official data, our monthly GDP Tracker suggests that growth is set to nudge higher to 0.5 per cent in the third quarter.**
- Recent survey evidence suggests that the manufacturing and construction sectors are recovering after a particularly weak start to the year and the dominant services sector is set to maintain a similar rate of growth in the third quarter.

Amit Kara, Head of UK macroeconomic forecasting, said “*The economy recovered in the second quarter after the unexpected slowdown in the first quarter. Growth is now close to our estimate of potential. Looking ahead, there is some evidence to suggest that services sector output has stabilised while the relatively small construction sector continues to gather momentum. GDP growth is expected to strengthen to 0.5 per cent in the third quarter.*”

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



Production (14 per cent of GDP)

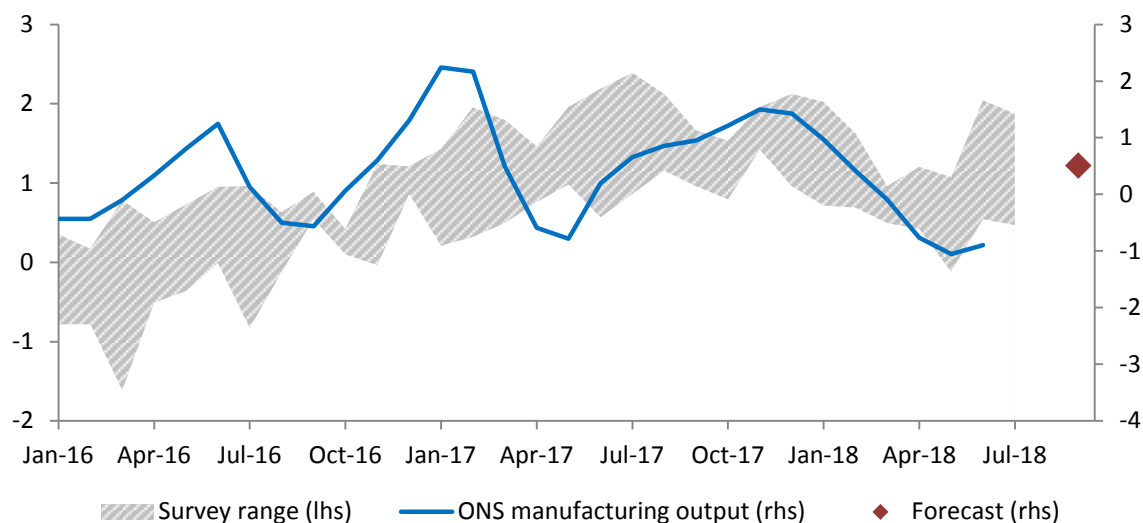
According to the ONS, the manufacturing sector suffered a technical recession in the first half of this year mainly because output fell in the first four months of this year. Output has however, bounced higher in May and June and is set to expand once again in the third quarter. Some of that earlier weakness is related to extreme weather conditions in the UK, but the slowdown was evident in other countries as well and export turnover was also lower.

Recent survey data points to a muted recovery in manufacturing output (Figure 2). One reason for that is tepid global manufacturing sector growth; for example the JP Morgan global manufacturing PMI survey shows that the sector lost momentum in July. That said there is evidence to suggest that the drag on manufacturing sector output from the inventory build-up in the first quarter has more or less fully reversed in the second.

On the basis of the most recent information, particularly a stronger performance in May and June, we expect manufacturing output to grow by 0.5 per cent in the third quarter after falling by 0.9 per cent in the second.

Mining and quarrying is a small and erratic component of the industrial production sub-component. According to the ONS, output in mining and quarrying output fell by 0.5 per cent in June due to planned maintenance work in the oil and gas extraction sector.

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

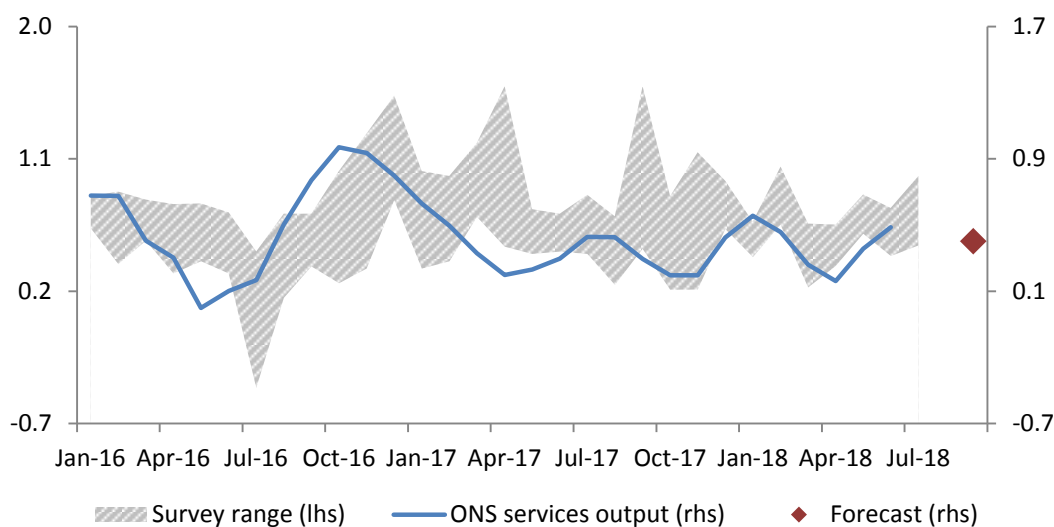
Output of electricity and gas, another small component in industrial production, fell in the second quarter mainly because of lower gas supply. This drop is primarily because of warmer-than-usual average temperature across the quarter and the demand for gas is likely to stay low at least in the first month of the third quarter because of the heat wave in July.

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. The second quarter outturn was marginally lower than the 0.6 per cent forecast that we published last month. Looking ahead into the third quarter, we see service sector output of around 0.4 per cent, which is unchanged from our previous forecast.

Within services, retail trade performed strongly in the second quarter with growth of 2.1 per cent. The rebound is explained by better weather conditions. More recent surveys, such as from the BRC-KPMG, suggests that warm weather and the football World Cup helped boost food and drink sales in July, but retail sales as a whole have been weak. Moreover, forward-looking indicators, such as those from the CBI Distributive Trades survey, suggest that retail sales volume growth is likely to be subdued in the near term. There is also evidence in surveys such as the latest PMI-Markit Service sector of delays in decision making and general caution because of Brexit.

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. The second quarter recovery is driven by an increase in repair and maintenance work. That strength in output is likely to persist in the third quarter according to the latest IHS Markit/CIPS construction PMI survey which has signalled a rise in confidence with companies reporting an increase in job creation and a build-up of new orders.

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 Sarah Stevens on 020 7654 1907/ press@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	103.7	103.4	103.3	100.7	104.0	108.3	102.7	103.5	96.8	99.9	108.0	110.5	101.3
Aug-18	103.9	103.6	103.5	100.7	104.2	108.7	102.8	103.6	97.4	98.8	108.1	111.2	101.0
Sep-18	104.1	103.8	103.8	100.7	104.4	109.2	102.8	103.7	98.0	97.8	108.4	111.4	100.9
Percentage change, 3 months on previous 3 months													
Mar-18	0.2	0.3	0.5	0.2	0.1	0.1	0.4	-0.1	1.4	2.5	1.7	-0.8	-1.5
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	0.1	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	0.5	0.5	0.1	0.2	1.4	1.6	-0.5	0.0	-4.6	-1.3	2.4	3.4	0.0
Aug-18	0.5	0.4	-0.1	0.1	1.0	1.5	0.0	0.4	-3.0	-1.1	2.3	4.0	-0.3
Sep-18	0.5	0.4	0.2	0.1	0.6	1.3	0.2	0.5	-0.7	-2.0	1.3	3.0	-0.6
Percentage change, month on same month in previous year													
Mar-18	1.3	1.2	1.6	0.3	0.0	2.5	3.1	2.5	12.0	-3.9	1.7	-1.1	-1.2
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	1.5	1.5	1.3	0.5	1.2	4.2	0.8	1.2	-1.9	-3.0	5.4	3.8	-1.9
Aug-18	1.5	1.5	1.3	0.3	1.7	4.2	0.7	1.2	-2.0	-2.9	6.0	2.7	-2.5
Sep-18	1.6	1.8	1.6	0.6	2.2	4.3	0.0	0.4	-2.5	-5.4	7.6	4.0	-2.8
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	0.2	0.2	0.2	0.0	0.2	0.3	-0.1	-0.1	-0.3	1.0	-0.4	0.7	-0.3
Aug-18	0.2	0.2	0.2	0.0	0.2	0.4	0.1	0.1	0.6	-1.0	0.1	0.6	-0.3
Sep-18	0.2	0.2	0.3	0.0	0.2	0.4	0.1	0.1	0.6	-1.1	0.3	0.2	-0.1

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