Office for National Statistics

Article

Monthly economic commentary: August 2017

Provides analysis of the latest estimate of GDP and economic commentary for prices, short-term indicators and labour market indicators to complement theme day economic commentary.

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1 . Main points

- The second estimate of gross domestic product (GDP) shows that the UK economy grew by 0.3% in Quarter 2 (Apr to June) 2017, unchanged from the preliminary estimate of GDP published on 26 July 2017.

- Growth in private consumption slowed to 0.1% in Quarter 2 2017, the slowest rate of quarterly growth since Quarter 4 (Oct to Dec) 2014.

- The contribution to nominal GDP growth from wage income (compensation of employees) slowed to 1.7 percentage points in Quarter 2 2017 compared with the same quarter a year ago; this is lower than the 2.1 percentage points recorded in each of the previous 3 quarters.

- The 12-month growth rate in the Consumer Prices Index including owner occupiers' housing costs (CIPH) and the Consumer Prices Index (CPI) both remained stable at 2.6% in July 2017, although inflation in the UK remains higher than in the EU and US.

- The rate of unemployment fell to 4.4% in the 3 months to June 2017, its lowest level since 1975, while real wages fell 0.5% in the 3 months to June 2017 compared with the same 3 months a year ago.

2 . Statistician's comment

"Gross domestic product (GDP) growth has slowed markedly in the first half of the year with relatively robust services growth, partly thanks to a booming film industry, offset by weak performances from manufacturing and construction in the second quarter (April to June 2017).

"Household spending grew weakly, with the lower-value pound hitting household budgets, while business investment showed no growth at all."

Darren Morgan, Head of Gross Domestic Product, Office for National Statistics

3 . Summary

Estimates of growth in the economy remain unchanged from the preliminary estimate of gross domestic product (GDP) published in July 2017. While growth in the UK economy has slowed during the first half of 2017, activity remains 9.0% above its pre-downturn peak. The services sector continues to be the main driver of recent economic growth in the UK, contributing 0.4 percentage points to quarterly GDP growth in Quarter 2 (Apr to June) 2017 and 1.9 percentage points to the 1.7% growth seen over the past year.

The trade deficit in Quarter 2 2017 remained broadly unchanged compared with Quarter 1 (Jan to Mar) 2017, widening by £0.1 billion to £8.9 billion. Output from the production and construction industries both fell and together detracted around 0.1 percentage points from GDP growth in Quarter 2 2017.

Consumer price inflation remained stable in the UK in July 2017, while the labour market continued to strengthen in the 3 months to June 2017.

More detailed theme day economic commentary is available for:

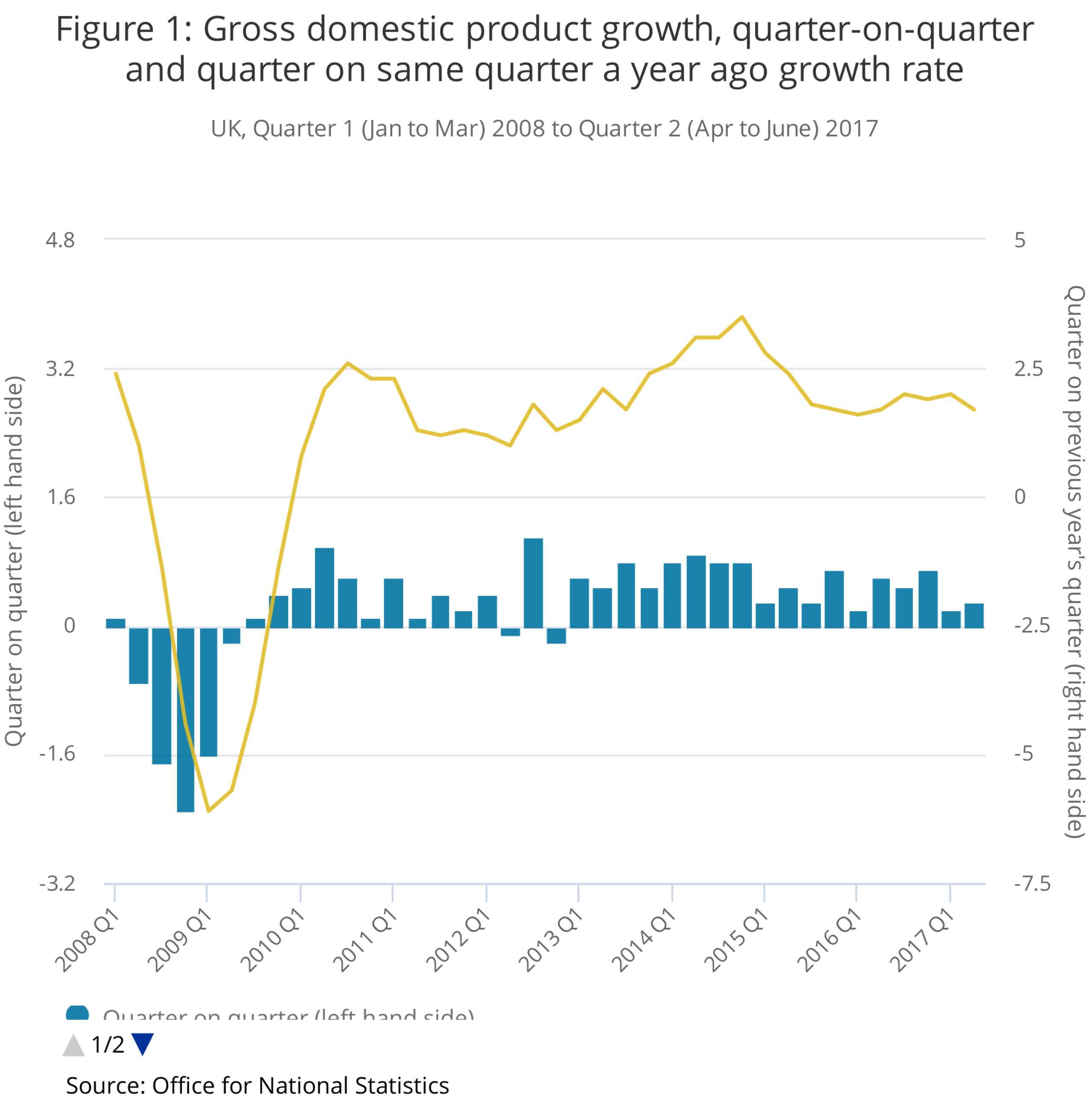
- Short-term indicators
- Prices
- Labour market

4 . The UK economy grew by an unrevised 0.3% in Quarter 2 (Apr to June) 2017

Today's Gross domestic product (GDP) release estimates that UK economic growth was unchanged from the preliminary estimate at 0.3% for Quarter 2 (Apr to June) 2017, following growth of 0.2% in Quarter 1 (Jan to Mar) 2017.

Figure 1: Gross domestic product growth, quarter-on-quarter and quarter on same quarter a year ago growth rate

UK, Quarter 1 (Jan to Mar) 2008 to Quarter 2 (Apr to June) 2017



Source: Office for National Statistics

Notes:

1. Q1 refers to Quarter 1 (Jan to Mar)
   Q2 refers to Quarter 2 (April to June)
   Q3 refers to Quarter 3 (July to Sept)
   Q4 refers to Quarter 4 (Oct to Dec)

Today's GDP figures, which provide a complete year of data since the EU referendum vote in June 2016, show that the UK economy grew by 1.7% compared with Quarter 2 2016, though there has been a slowing of growth in the first two quarters of 2017. Over the longer-term, GDP has grown 16.4% since the trough of the economic downturn in 2009 and is currently 9.0% higher than the pre-downturn peak level of output recorded in Quarter 1 2008.

5 . Services industries drive growth in Quarter 2 2017

In addition to the second estimate of gross domestic product (GDP), new data on services output in June 2017 have been published.

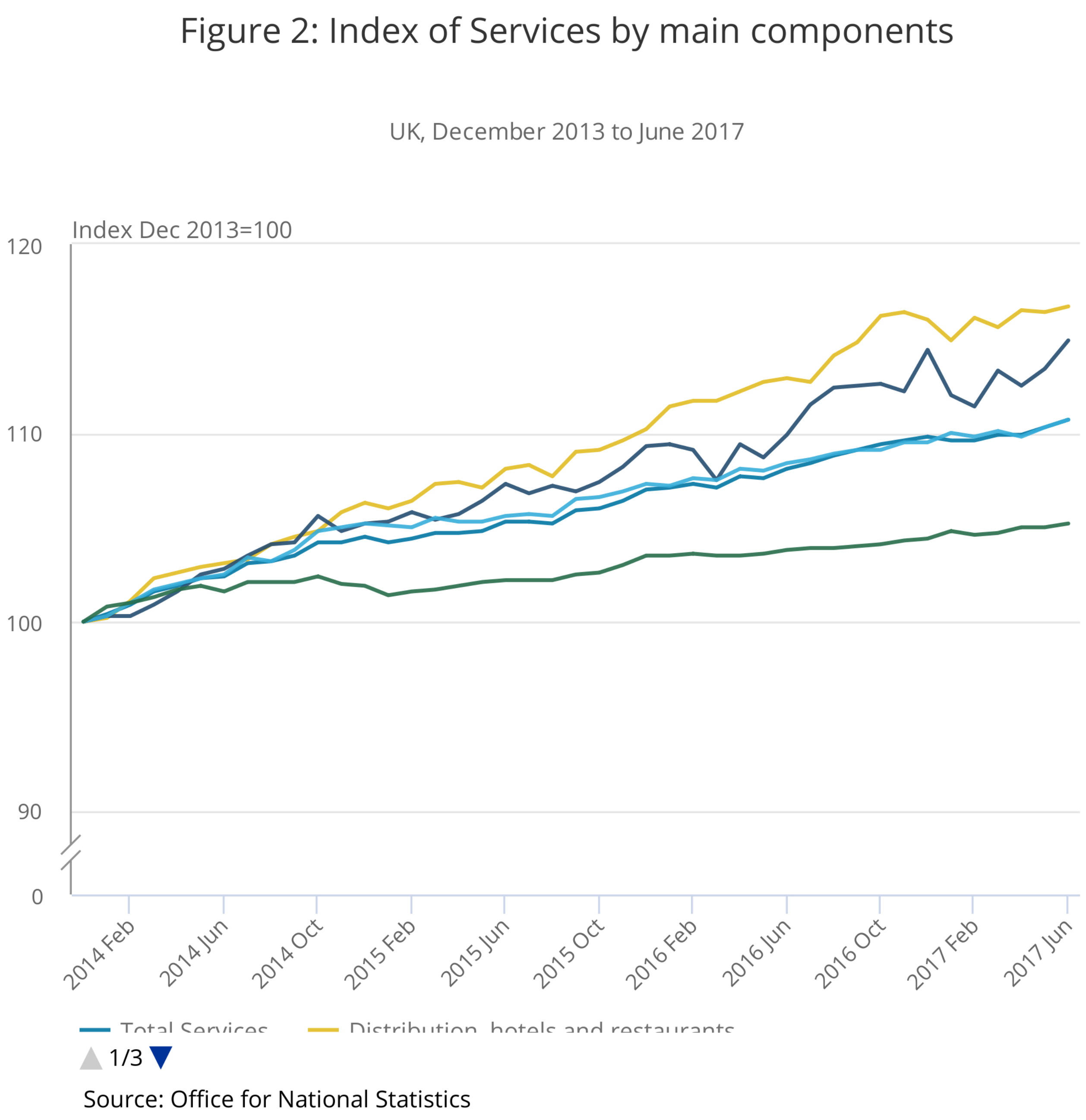
Output in the services sector saw a pick-up in Quarter 2 (Apr to June) 2017, increasing by 0.5% following modest growth of 0.1% in Quarter 1 (Jan to Mar) 2017. The services sector has been the main driver of recent economic growth in the UK, contributing 0.4 percentage points to quarterly GDP growth in Quarter 2 2017 and 1.9 percentage points to the 1.7% growth seen over the past year. However, services activity has slowed in 2017, with growth in the first two quarters of the year below the average quarterly rate of 0.7% seen in 2016.

Of the main components of services, the transport, storage and communications sector made the largest contribution to quarterly services growth (0.1 percentage points), with growth of 1.2% in Quarter 2 2017. Previous analysis highlighted strength in the motion picture industry within this sector, with the industry recording 6.7% growth in the latest quarter.

Looking at the monthly path, services output grew by 0.4% in June 2017, following 0.3% growth in May and a flat outcome in April. The rise in June 2017 reflected increases across all four main services sectors (Figure 2), with transport, storage and communications again being the largest contributor to growth, contributing 0.2 percentage points towards total monthly services growth and growing 1.3% on the month. Meanwhile, both the business services and finance sector, and the distribution, hotels and restaurants sector grew by 0.3% in June 2017, slightly stronger than the 0.2% growth recorded in government and other services.

Figure 2: Index of Services by main components

UK, December 2013 to June 2017



Source: Office for National Statistics

Notes:

1. Using 2013 weights, distribution, hotels and restaurants is 13.6% of total services, transport, storage and communication is 10.6%, business services and finance is 40.3% and government and other services is 29.0%.

6 . Production and construction detract from growth in Quarter 2 2017

While services industries supported growth in Quarter 2 (Apr to June) 2017, production and construction both fell and together detracted around 0.1 percentage points from gross domestic product (GDP) growth.

Production activity continues to be weaker following high levels of output in December 2016, with both total production output and manufacturing output decreasing in Quarter 2 2017. The 0.3% quarterly fall in total production output was almost entirely driven by a fall in manufacturing activity (down by 0.6%) and in particular, the production of motor vehicles, trailers and semi-trailers (down by 5.8%). However, the monthly picture for June 2017 was stronger for production, with growth of 0.5%. The mining and quarrying sector accounted for virtually all of the monthly growth (contributing 0.5 percentage points), with an unexpected rise in production due to the absence of usual summer maintenance in the North Sea oil rigs.

Construction output fell by 0.1% in June 2017, following a 0.4% and 1.1% fall in May and April respectively. Despite the monthly contraction in overall output, new private housing output grew by 5.1% to reach record high levels in June 2017, making the largest positive contribution towards monthly total construction growth (1.1 percentage points). The monthly path reflects the quarterly picture with construction output in Quarter 2 2017 contracting by 1.3%, with the largest negative contribution coming from public other new work, which contributed negative 0.5 percentage points.

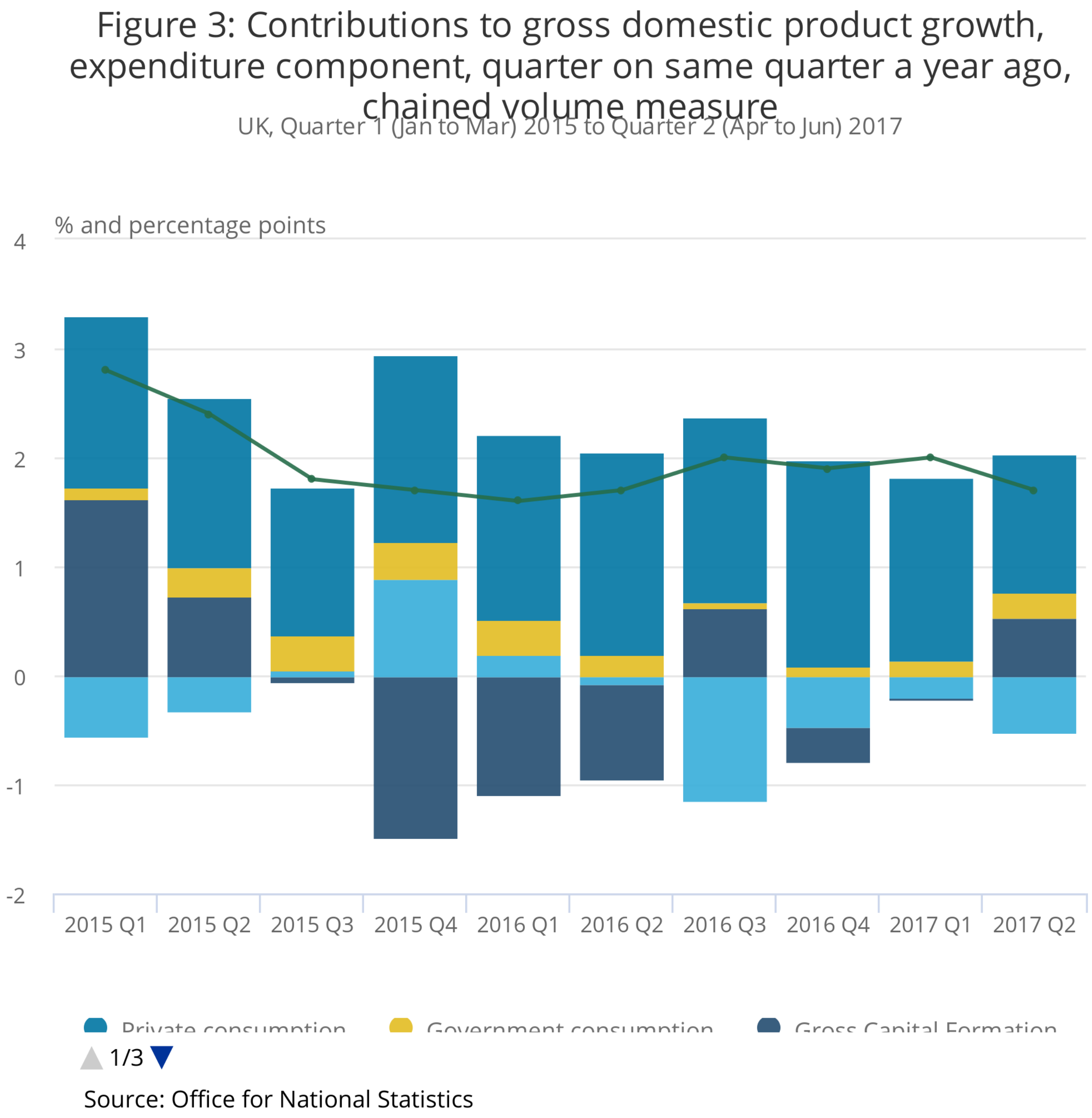
7 . Household consumption growth remains subdued

The second estimate of gross domestic product (GDP) includes a detailed picture of expenditure in Quarter 2 (Apr to June) 2017 and shows that private consumption, government consumption and gross capital formation all contributed positively to GDP growth, while net trade continued to detract from growth.

Growth in private consumption (expenditure of households and non-profit institutions serving households) slowed to 0.1% in Quarter 2 2017, the slowest rate of quarterly growth since Quarter 4 (Oct to Dec) 2014. While private consumption has increased by 1.9% compared with the same quarter a year ago, its contribution to quarter-on-year GDP growth has gradually declined from 1.9 percentage points in Quarter 4 2016 to 1.3 percentage points in Quarter 2 2017 (Figure 3). This slowdown in private consumption in 2017 is consistent with the latest independent forecasts published in August 2017, with the average independent forecaster predicting only 1.8% private consumption growth in 2017, considerably lower than the 2.8% outturn for 2016 [1].

Figure 3: Contributions to gross domestic product growth, expenditure component, quarter on same quarter a year ago, chained volume measure

UK, Quarter 1 (Jan to Mar) 2015 to Quarter 2 (Apr to Jun) 2017



Source: Office for National Statistics

Notes:

1. Components may not sum to total gross domestic product due to rounding and loss of additivity in data prior to open period. The statistical discrepancy is also not displayed.

2. Q1 refers to Quarter 1 (Jan to Mar)
   Q2 refers to Quarter 2 (April to June)
   Q3 refers to Quarter 3 (July to Sept)
   Q4 refers to Quarter 4 (Oct to Dec)

Meanwhile, gross capital formation (GCF) contributed to growth on a quarter on same quarter a year ago basis compared with recent periods (Figure 3), despite business investment, its largest component, experiencing flat growth. This is only the second positive contribution from GCF to quarter-on-year growth in GDP since Quarter 2 2015. The growth in GCF was offset by the UK's negative trade balance, which widened by £2.4 billion from Quarter 2 2016 to Quarter 2 2017. This can be attributed to growth in imports outpacing exports on a quarter on same quarter a year ago basis for the fourth successive quarter, despite the depreciation of sterling since June 2016.

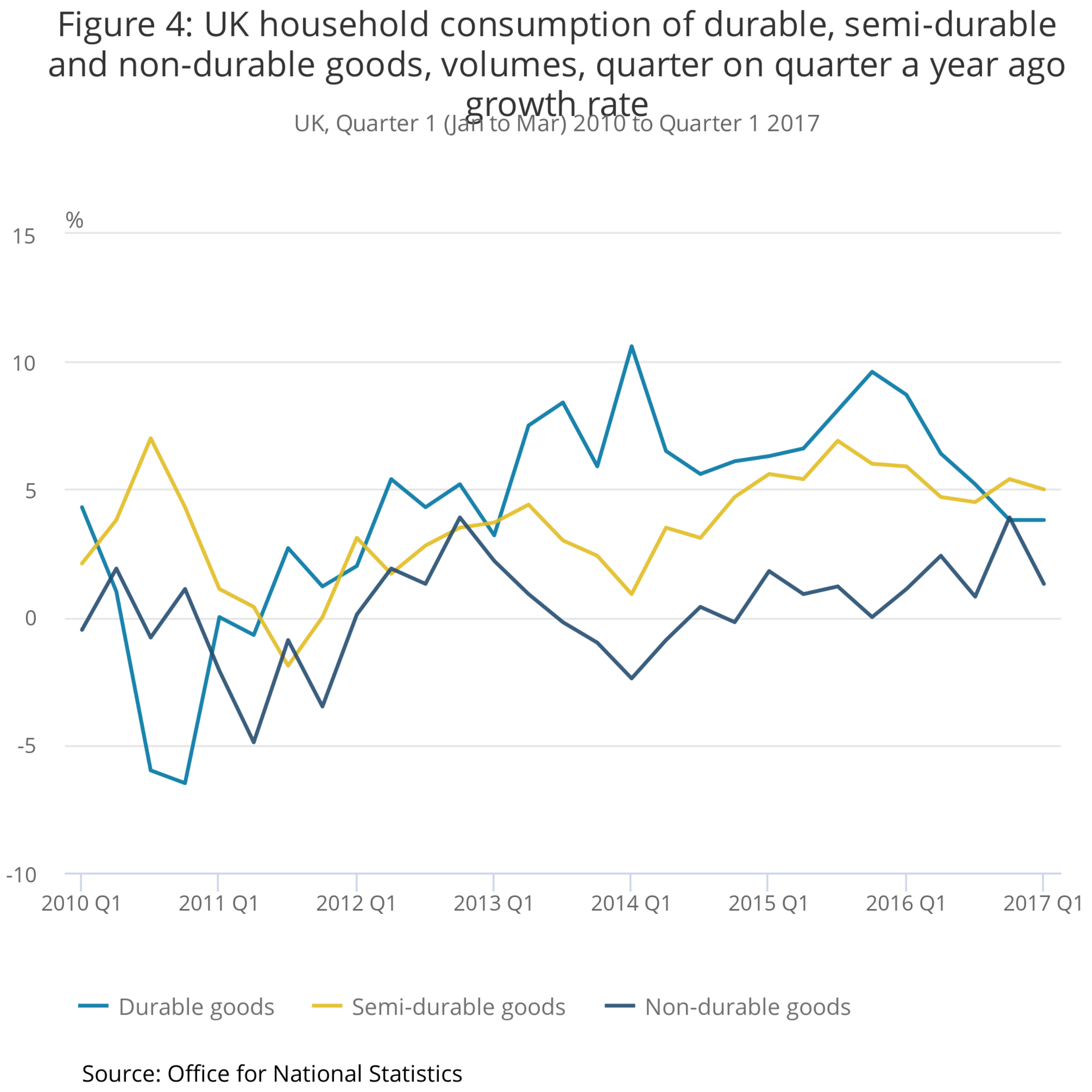
There is some evidence to suggest that the slowdown in private consumption has partly been driven by households choosing to delay their purchase of discretionary items, such as cars or "big ticket" household items, as factors such as the squeeze on real wages and the weaker value of sterling weigh on household spending decisions.

Within household consumption, goods may be classified as durable (such as cars or furniture), semi-durable (such as clothing) or non-durable (such as food). Spending on durable goods – those that can be used repeatedly or continuously over a period of more than a year – is generally thought to be more discretionary in nature, as consumers can more easily delay their purchase. It is therefore expected that expenditure on these items might slow during periods of lower real income growth or heightened uncertainty about the future.

Figure 4 shows recent underlying trends in durable, semi-durable and non-durable goods consumption, comparing quarter on quarter a year ago growth rates for each category (in volume terms)[2]. It highlights a declining trend in the consumption of durable goods, with the quarter on quarter a year ago growth rate falling from 9.6% in Quarter 4 2015 to 3.8% in both Quarter 4 2016 and Quarter 1 (Jan to Mar) 2017 – the lowest rate since Quarter 1 2013. Meanwhile, growth in the consumption of semi-durable and non-durable goods has remained relatively flat over the past 2 years.

Figure 4: UK household consumption of durable, semi-durable and non-durable goods, volumes, quarter on quarter a year ago growth rate

UK, Quarter 1 (Jan to Mar) 2010 to Quarter 1 2017



Source: Office for National Statistics

Notes:

1. Q1 refers to Quarter 1 (Jan to Mar)
   Q2 refers to Quarter 2 (April to June)
   Q3 refers to Quarter 3 (July to Sept)
   Q4 refers to Quarter 4 (Oct to Dec)

The downward trend in durable goods consumption is corroborated by recent retail sales figures, which show a relatively subdued picture in retail for 2017. In particular, figures have shown an underlying trend of slowing sales growth for household goods stores[3]. Compared with the same quarter a year ago, retail sales volumes for household goods stores rose by only 0.7% in Quarter 2 2017, down from a recent peak of 10.8% in Quarter 4 2014. The latest data on new motor vehicle registrations from the Society of Motor Manufacturers and Traders (SMMT) also add to signs of consumer caution, with the number of registrations falling in July 2017 compared with a year earlier for the fourth consecutive month (down by 9.3%).

Notes for: Household consumption growth remains subdued

1. However, this 2.8% growth for private consumption in 2016 was stronger than initial post-referendum forecasts of only 2.3% growth for the year.

2. Data for Quarter 2 2017 for durable, semi-durable and non-durable goods consumption are not published in the second estimate of GDP and will be available in the UK Quarterly National Accounts, released on 29 September 2017.

3. Household goods retailing includes furniture and lighting, electrical household appliances, hardware, paints and glass, and music and video recordings and equipment.

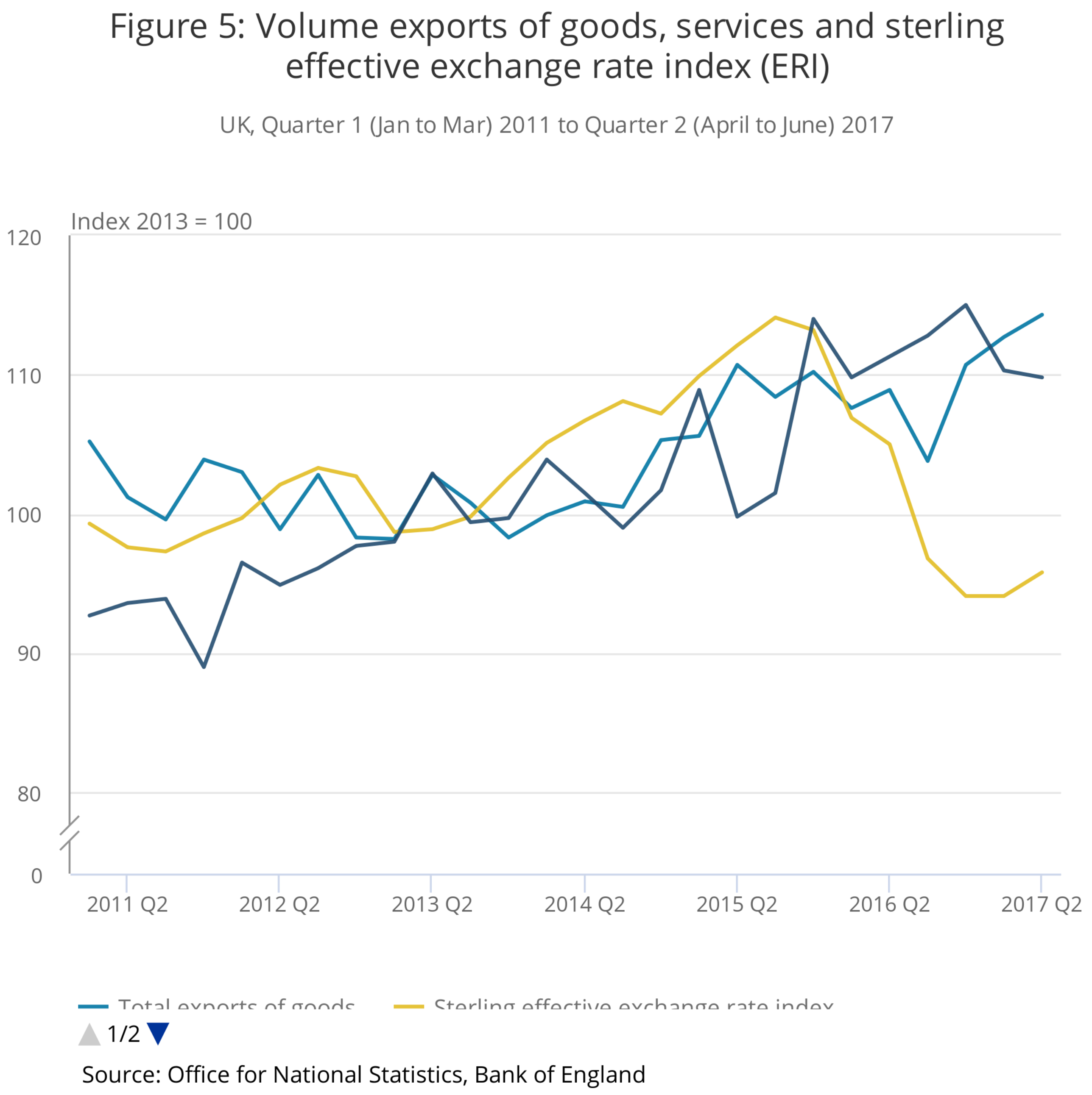
8 . The UK's trade balance remains broadly unchanged in Quarter 2 2017

The total trade deficit (goods and services) widened by £2.0 billion in June 2017[1], which is the largest monthly widening in the trade deficit since June 2016. Despite this, the trade deficit in Quarter 2 (Apr to June) 2017 remained broadly unchanged compared with Quarter 1 (Jan to Mar) 2017, widening by £0.1 billion to £8.9 billion.

In terms of prices, goods export prices increased by 8.2% in Quarter 2 2017 compared with the same quarter a year ago – less than the 8.7% depreciation in the sterling effective exchange rate (ERI) over the same period. The volume of goods exports rose by 1.5% in Quarter 2 2017 (Figure 5) to be 5.0% higher than a year ago. However, this has been a more muted export response to the weaker sterling than expected by some commentators. Possible reasons for this are highlighted in recent analysis on the impact of sterling depreciation on trade.

Figure 5: Volume exports of goods, services and sterling effective exchange rate index (ERI)

UK, Quarter 1 (Jan to Mar) 2011 to Quarter 2 (April to June) 2017



Source: Office for National Statistics, Bank of England

Notes:

1. Q1 refers to Quarter 1 (Jan to Mar)
   Q2 refers to Quarter 2 (April to June)
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   Q4 refers to Quarter 4 (Oct to Dec)

Notes for: The UK’s trade balance remained broadly unchanged in Quarter 2 2017

1. Section 4 of the UK Trade bulletin shows the UK total trade monthly balance including and excluding erratic commodities.

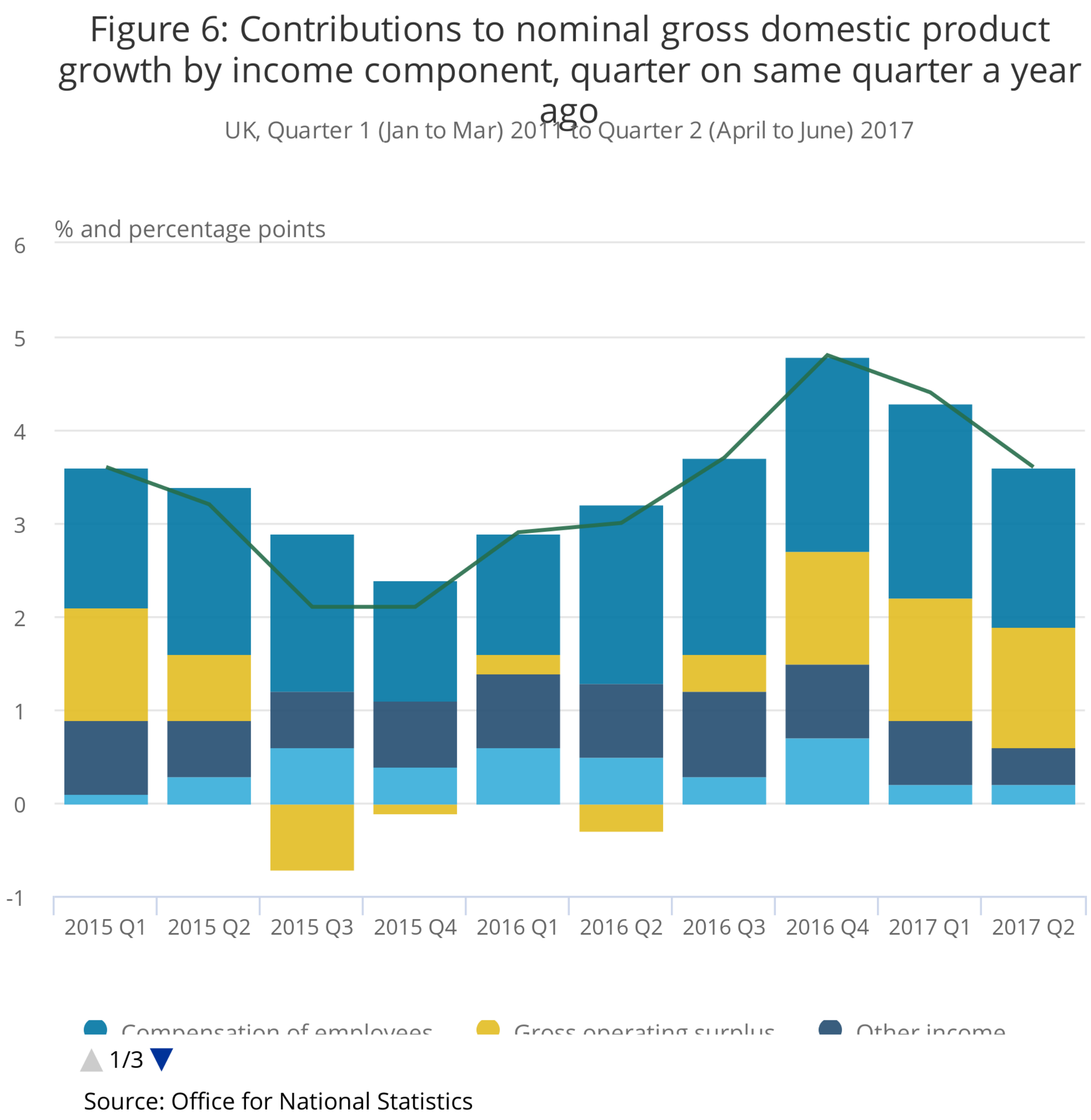
9 . Compensation of employees drives nominal GDP growth in Quarter 2 2017, while profits remain broadly stable

Nominal gross domestic product (GDP) increased by 0.8% in Quarter 2 (Apr to June) 2017, following growth of 0.7% in Quarter 1 (Jan to Mar) 2017. Growth in the latest quarter was predominantly driven by compensation of employees (COE), which increased by 1.2% in the quarter and 3.3% compared with Quarter 2 2016. However, the strength in COE was partly offset by a fall in gross operating surplus (GOS), which made zero contribution to nominal GDP growth in the latest quarter, compared with 0.9 percentage points in Quarter 1 2017. This is the weakest quarterly growth contribution since Quarter 3 (July to Sept) 2015 and is on the back of a 0.8% fall in private non-financial corporations' (PNFC) profits, with financial and public corporations both recording profit growth in Quarter 1 2017.

Figure 6 shows contributions of income components to quarter on same quarter a year ago growth in nominal GDP. While COE contributed 1.7 percentage points in Quarter 2 2017, this is lower than the 2.1 percentage points recorded in each of the previous 3 quarters. This, along with a decreased contribution from other income (0.7 to 0.4 percentage points) meant that quarter-on-year growth in nominal GDP slowed from 4.4% to 3.6% between Quarter 1 and Quarter 2 2017, the largest decrease in the quarter-on-year growth rate since Quarter 3 2015. The growth contribution from gross operating surplus remained unchanged in the latest quarter at 1.3 percentage points.

Figure 6: Contributions to nominal gross domestic product growth by income component, quarter on same quarter a year ago

UK, Quarter 1 (Jan to Mar) 2011 to Quarter 2 (April to June) 2017



Source: Office for National Statistics

Notes:

1. Contributions may not sum due to rounding.

2. Q1 refers to Quarter 1 (Jan to Mar)
   Q2 refers to Quarter 2 (April to June)
   Q3 refers to Quarter 3 (July to Sept)
   Q4 refers to Quarter 4 (Oct to Dec)

10 . The UK continues to see higher consumer price growth than the EU, driven by a range of goods and services

Data for July 2017 show that the 12-month growth rate in the Consumer Prices Index including owner occupiers' housing costs (CPIH) remained stable at 2.6%.

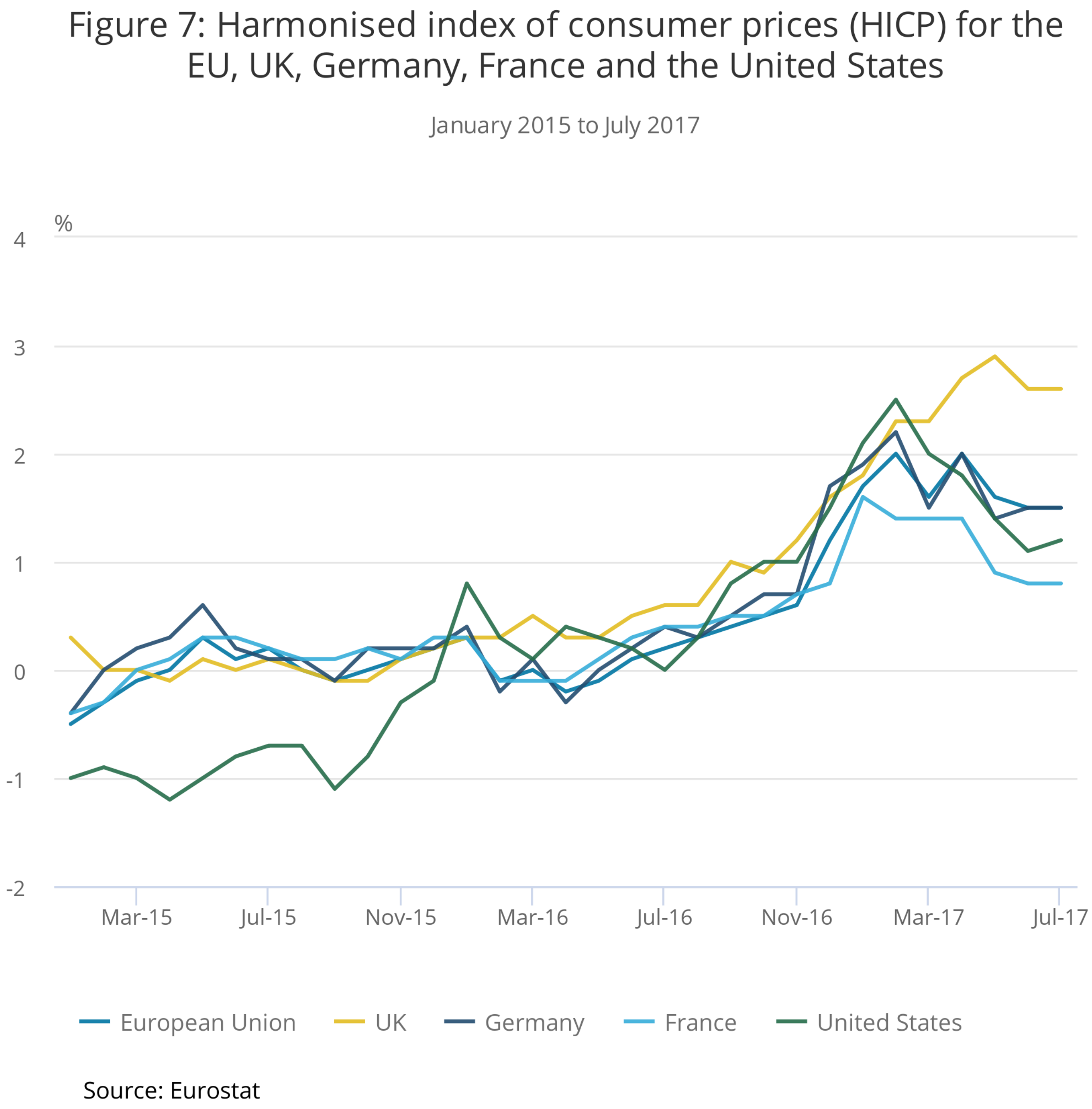
Figure 7 shows consumer price inflation rates on a consistent basis across the EU and selected European countries using the Harmonised Index of Consumer Prices (HICP) and for the US between January 2015 and July 2017. A proxy HICP is available for the US. The HICP is equivalent to the Consumer Prices Index (CPI) in the UK and allows for international comparisons to be made on a consistent basis.

These data show that inflation rates have risen from a very low base across selected countries in the EU and US in the second half of 2016 but have mostly fallen back during the first 7 months of 2017, apart from in the UK. Previous analysis has shown that the UK had among the lowest rate of HICP inflation for goods of selected EU countries and the EU as a whole during 2015 and 2016, but this has since picked up alongside services price inflation.

The HICP inflation rate for the EU as a whole was 1.5% in July 2017, unchanged from June 2017. While the inflation rate in the UK was also unchanged from June 2017, the UK HICP rate was 2.6%, that is, 1.1 percentage points higher than the EU as a whole. France and the US have the lowest rates of inflation in July 2017 at 0.8% and 1.2% respectively.

Figure 7: Harmonised index of consumer prices (HICP) for the EU, UK, Germany, France and the United States

January 2015 to July 2017



Source: Eurostat

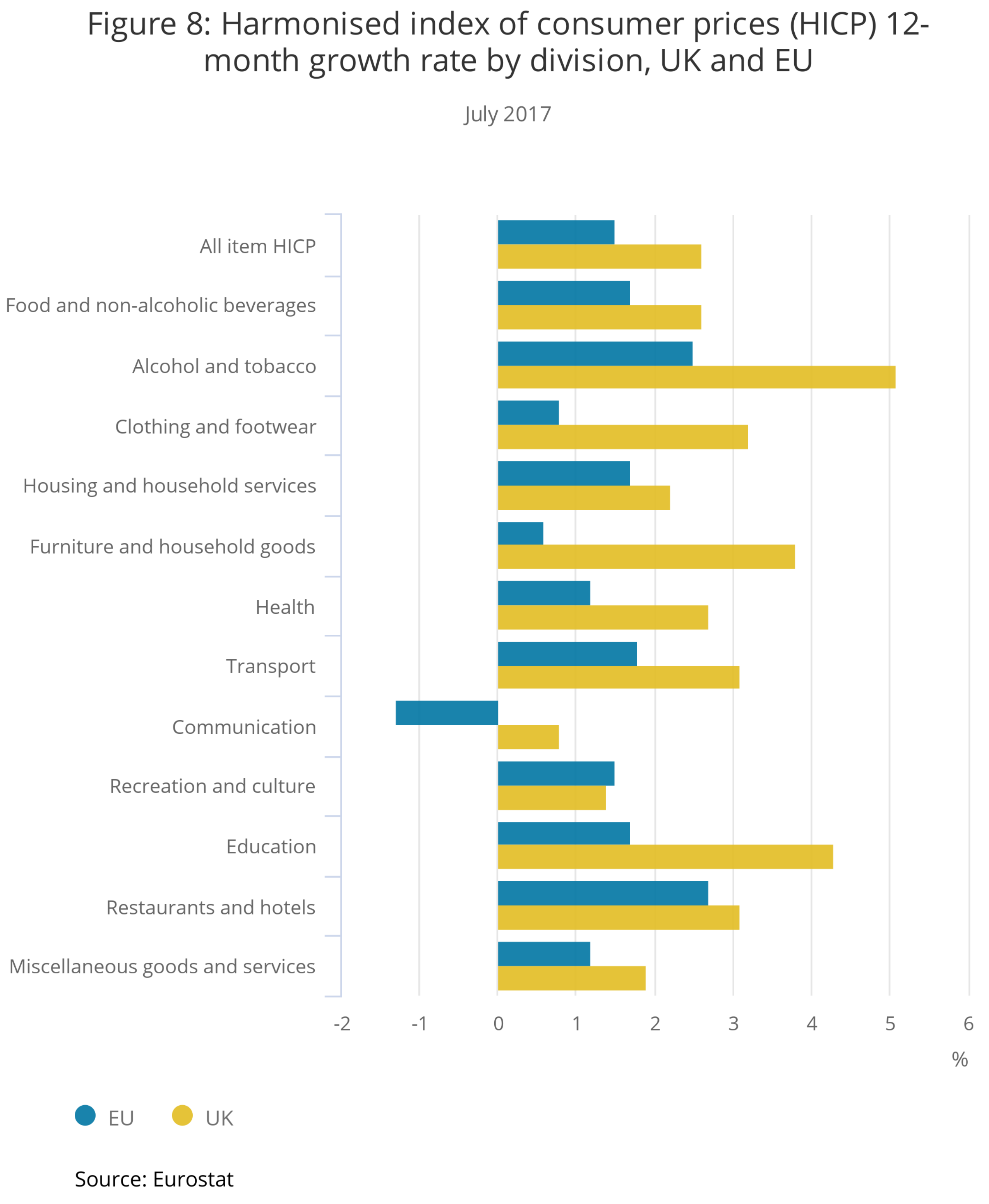
Notes:

1. A proxy harmonised index of consumer prices is available for the USA and is shown in the chart.

To consider the reasons behind the UK's higher rate of inflation than the EU as a whole in July 2017, Figure 8 shows the 12-month HICP inflation rates for the UK and EU for each division of goods and services and all-item HICP, and Figure 9 shows the weights of each division.

Figure 8: Harmonised index of consumer prices (HICP) 12-month growth rate by division, UK and EU

July 2017



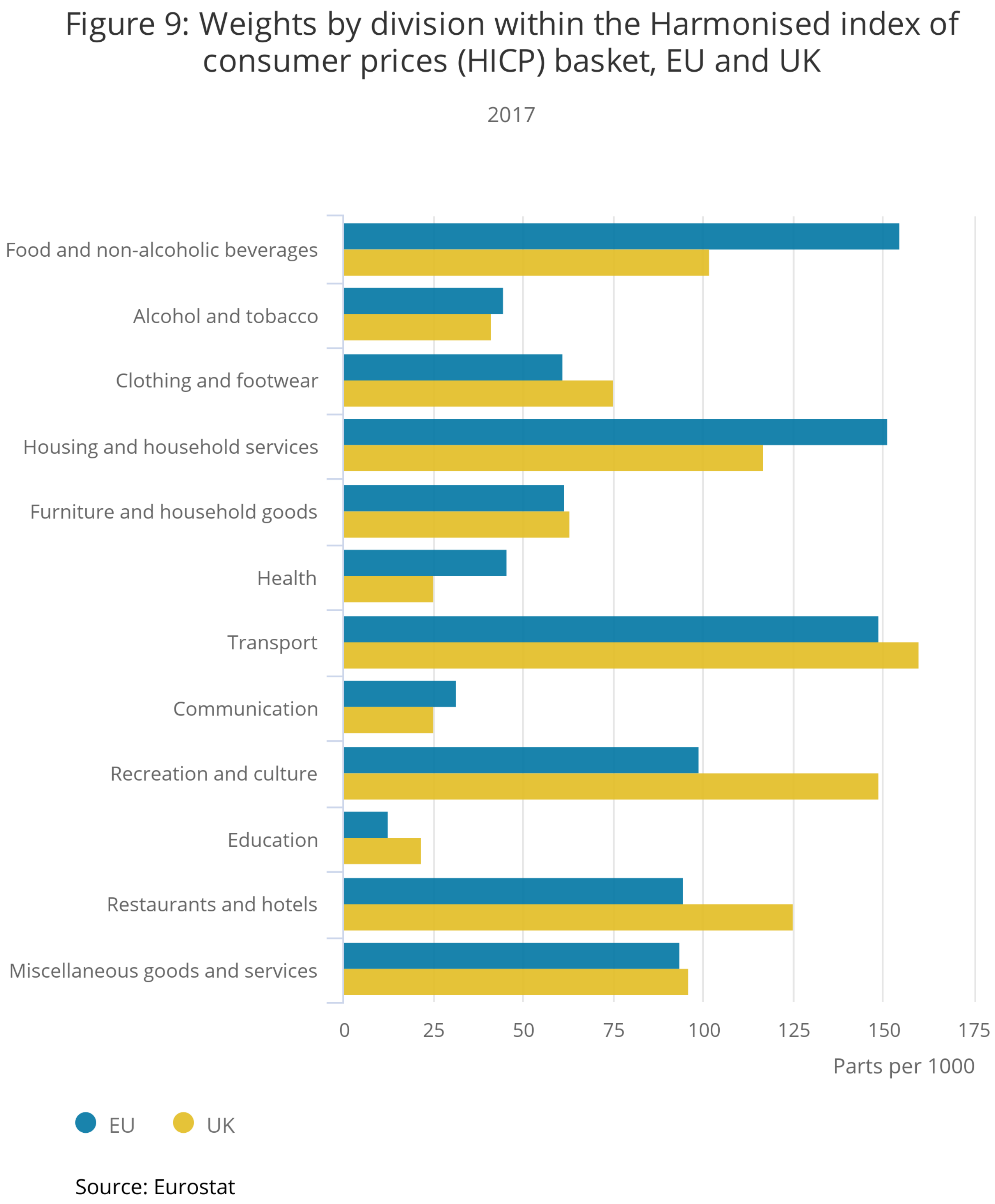
Source: Eurostat

Figure 8 shows that the UK currently has higher rates of price growth in all but one division in the HICP basket (recreation and culture). Differences are particularly noticeable for alcohol and tobacco, clothing and footwear, furniture and household goods, transport and education.

These differences, combined with the different weights between the EU and UK for the divisions of goods and services in the overall HICP basket shown in Figure 9, can provide an insight into the main drivers between the different overall inflation rates between the EU and UK. For example, the top three largest weights in the EU HICP basket differ from the top three largest weights in the UK. While transport is common to the top three most important divisions in both the UK and EU with a weight of 160 (parts per 1,000) in the UK and 148 (parts per 1,000) in the EU, the other two highest weighted divisions differ. In the EU, food, and housing and household services are the two other largest weights; but recreation and culture, and restaurants and hotels are the other two most important divisions for the UK.

Figure 9: Weights by division within the Harmonised index of consumer prices (HICP) basket, EU and UK

2017



Source: Eurostat

So, even where price growth rates are similar for divisions comparing the UK with the EU as a whole, such as recreation and culture, the higher weight for this division in the UK will lead to a greater contribution to overall inflation growth. Similarly, where the weights are similar comparing the UK and EU as a whole, for example, for alcohol and tobacco, the higher price growth in the UK for this division will also lead to a larger upward contribution to overall UK inflation than in the EU as a whole.

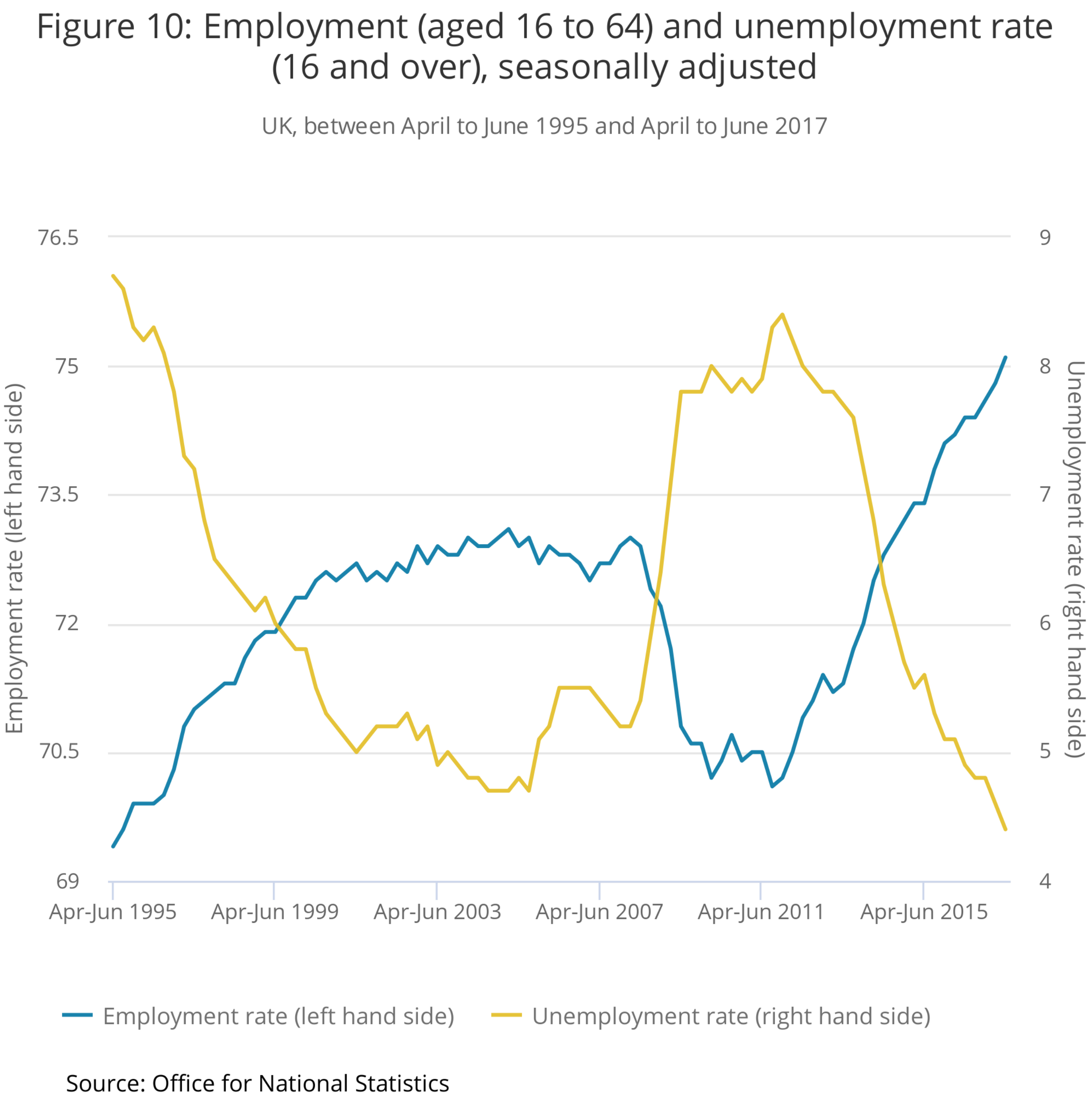
11 . Employment rate reaches a new record high in the 3 months to June 2017

The latest labour market statistics show that there were 32.07 million people in work, 338,000 more than for a year earlier and 125,000 more than for January to March 2017. There was an increase in full-time employment (up 91,000) to a record high of 23.58 million and part-time employment (up 34,000) to 8.49 million compared with 3 months ago. There was an increase in the number of people in self-employment (up 21,000) since the 3 months to March 2017.

By age category, there were increases in the number of employees for three age groups: 25 to 34 years, 35 to 49 years and 50 to 64 years; while the level of employment decreased for three age groups: 16 to 17 years, 18 to 24 years and 65 and over. The employment rate was 75.1% in the 3 months to June 2017, the highest since comparable records began in 1971 (Figure 10).

Figure 10: Employment (aged 16 to 64) and unemployment rate (16 and over), seasonally adjusted

UK, between April to June 1995 and April to June 2017

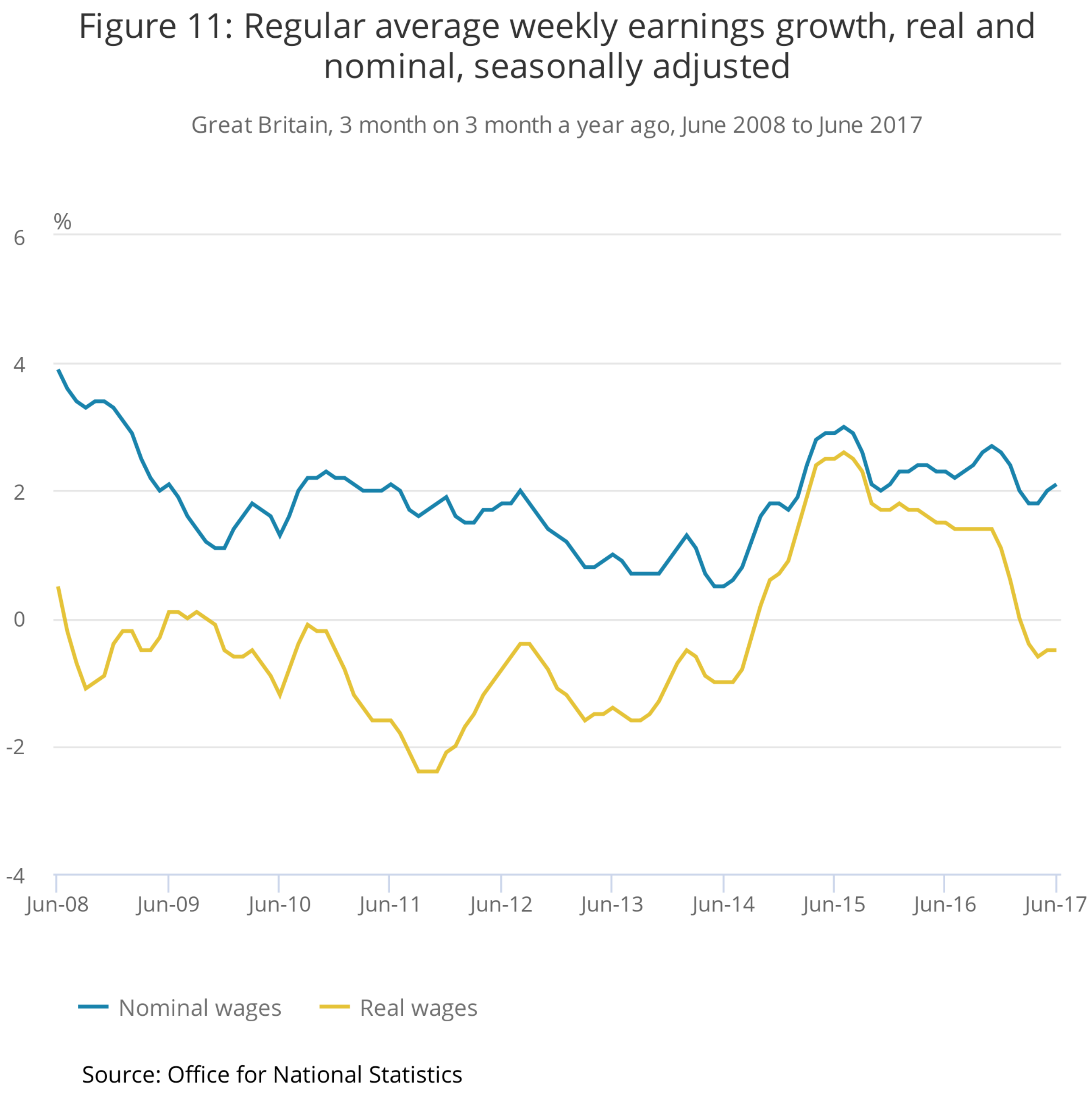


Source: Office for National Statistics

Figure 11 shows rates of nominal and real wage growth over a 9-year period from June 2008. These data show that regular weekly earnings for employees (excluding bonuses) in Great Britain increased by 2.1% compared with a year earlier. Once adjusted for inflation (measured using the Consumer Prices Index including owner occupiers' housing costs (CPIH)), average weekly earnings fell by 0.5% (excluding bonuses) over the year. Average total pay (including bonuses) also rose by 2.1% in nominal terms, and fell by 0.5% in real terms over the same period.

Figure 11: Regular average weekly earnings growth, real and nominal, seasonally adjusted

Great Britain, 3 month on 3 month a year ago, June 2008 to June 2017



Source: Office for National Statistics

UK unemployment rate falls to its lowest since 1975

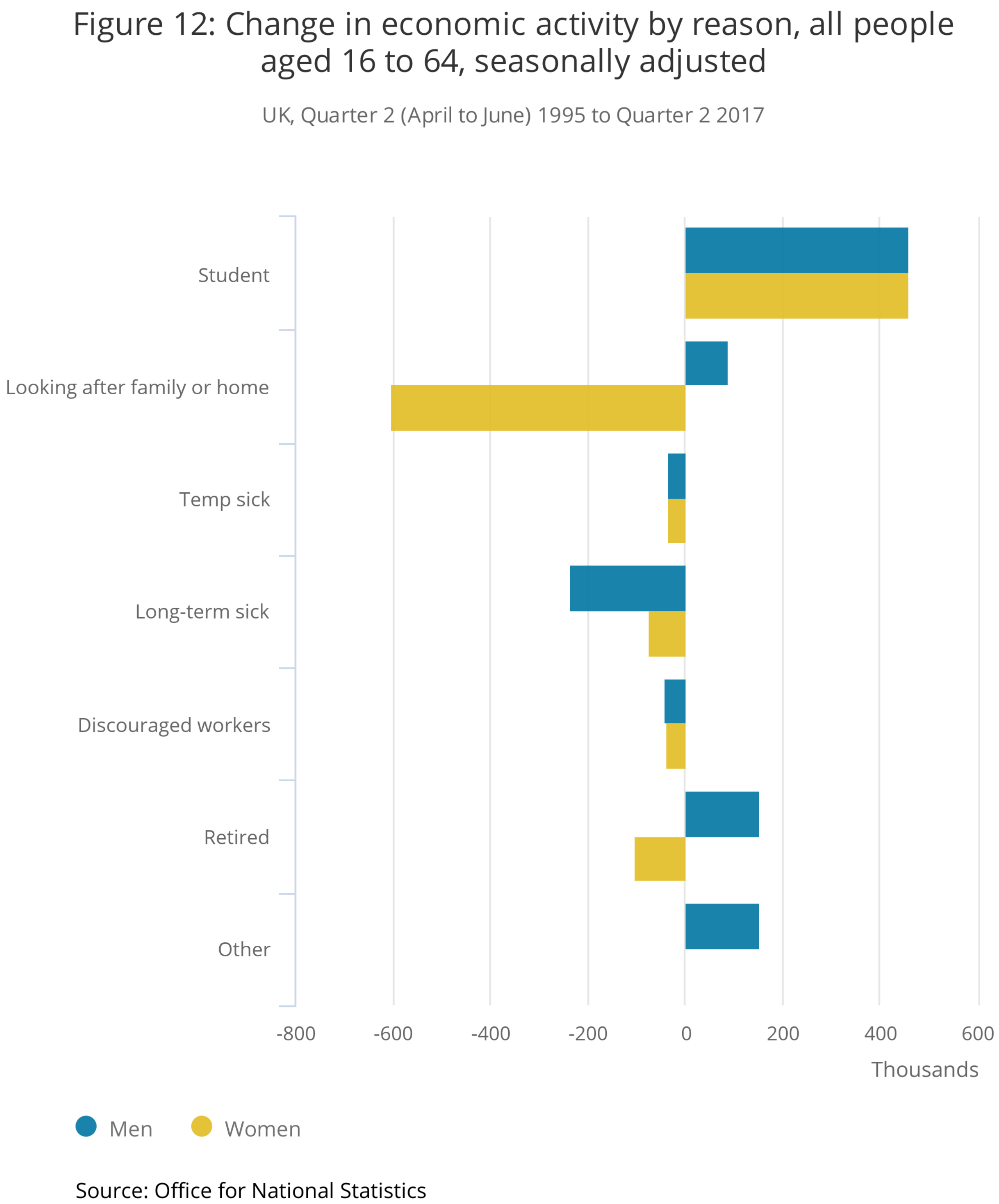
The unemployment rate declined by 0.2 percentage points in the 3 months to June 2017 compared with the 3 months to March 2017, falling to its lowest since 1975, at 4.4% (Figure 10). The total unemployment level decreased by 57,000 compared with January to March 2017 to 1.48 million. Unemployment decreased for three age groups: 16 to 17 years, 25 to 34 years and 35 to 49 years; while it increased for three age groups: 18 to 24 years, 50 to 64 years and 65 and over. A fall in unemployment was accompanied by a fall in inactivity. Total inactivity level decreased by 64,000 since the 3 months to March 2017 to 8.77 million; the inactivity rate for 16 to 64 year olds decreased by 0.2 percentage points since the 3 months to March 2017 to a record low of 21.3%. Inactivity decreased for three age groups: 18 to 24 years, 25 to 34 years and 35 to 49 years; while it increased for three age groups: 16 to 17 years, 50 to 64 years and 65 and over.

Recent analysis examined longer-term trends in economic inactivity. The overall inactivity rate has remained fairly stable over a long period until 2011. More recently, however, there has been a decline. The inactivity rate was 23.9% in Quarter 2 (Apr to June) 1995 but was down to 21.3% in the same quarter in 2017. The total economic inactivity rate masks different patterns among men and women over time. For women, the rate shows a reduction from 32.7% classified as inactive in the 3 months to June 1995, to 26.3% compared with the same period in 2017, but the proportion of men who are inactive has risen from 15% in the 3 months to June 1995 to 16.3% compared with the same quarter in 2017.

The main three reasons for economic activity were studying, looking after family or home and long term sickness. The overall proportion of the economically inactive that were students has been rising over the years, whereas the proportion of the economically inactive who were either looking after family or home or in long-term sickness has been falling (Figure 12). Looking just at men, since the 3 months to October 2009, those who were long-term sick or disabled have been overtaken as the largest group by those classified as students. For women, there has been a sharp decline in the proportions looking after the family and home accompanied by increases in the proportions in the student group since Quarter 2 1995.

Figure 12: Change in economic activity by reason, all people aged 16 to 64, seasonally adjusted

UK, Quarter 2 (April to June) 1995 to Quarter 2 2017



Source: Office for National Statistics