

UK growth beats estimates on strong service sector

The latest UK growth figure suggests the economy ended 2017 on a high note, but the surprising acceleration in services doesn't tally with the consumer slowdown



Source: Bank of England

0.5%

UK fourth quarter growth

(QoQ%)

Better than expected

Unexpected service strength

At 0.5%, UK fourth-quarter growth suggests that the economy performed a little better than feared at the end of 2017. We get relatively few details at this stage. But as the monthly flow of data has been suggesting, the manufacturing sector continued to flourish as global growth accelerated - although the overall production figures were held back to some degree by the North Sea pipeline outage back in December.

What is more surprising is the unexpectedly strong contribution from services, which grew at the

fastest rate since the end of 2016 (0.6% QoQ growth). This doesn't really tally with what we've seen in the consumer sector, with evidence that households continued to hold back on non-essential purchases in the fourth quarter (particularly around Christmas). Of course, the service sector encompasses much more than just the consumer sector, but it is nevertheless a key driver. It's also worth saying that only 45% of this GDP estimate is based on actual data, with the remainder calculated by a model, leaving some scope for a possible downward revision later on.

But whatever the case, given that the GDP data is already fairly outdated at the point of release, the key question now is, "what next"? Well, in the short-term at least, we see few catalysts for a further acceleration in UK growth. The outlook for consumer spending looks relatively bleak, even though the rate of inflation is starting to ease. Consumer confidence is the lowest since 2013, which is pretty stark when compared to the Eurozone and US, both of which are seeing sentiment at the highest levels since the early-2000s. And whilst an agreement is likely to be reached on a post-Brexit transition period this quarter, there is still plenty of Brexit-related uncertainty for firms to contend with.

What it means for interest rates

Admittedly, today's fourth quarter growth reading is better than the Bank of England had predicted at the time of the November inflation report. But if the UK economy does indeed struggle to move up a gear over coming months, the Bank will likely have to tread carefully when deciding whether to raise rates again this year. We don't expect any change in policy from the BoE in February, but a rate hike at the May meeting is an increasingly close call.

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