

UK growth slows considerably in the third quarter

Don't read too much into the latest slowdown in UK GDP. The figures look volatile and consumer-facing services – a key barometer of economic health – have been growing more quickly and consistently over the summer. Expect modest growth over the winter and a boost next year from the latest budget, though the health of the jobs market remains a key risk in 2025



We think the Bank of England is set to stay much more closely focused on services inflation than the disappointing GDP figures we've been seeing as of late

The latest figures don't look great, but...

For all the post-budget excitement about the prospect of faster UK growth, the latest GDP figures appear to provide a bit of a cold shower. Activity fell in September, and that meant that GDP growth across the third quarter was a pretty lacklustre 0.1%. That's a far cry from the 0.7%/0.5% quarter-on-quarter growth figures we saw in the first and second quarter respectively.

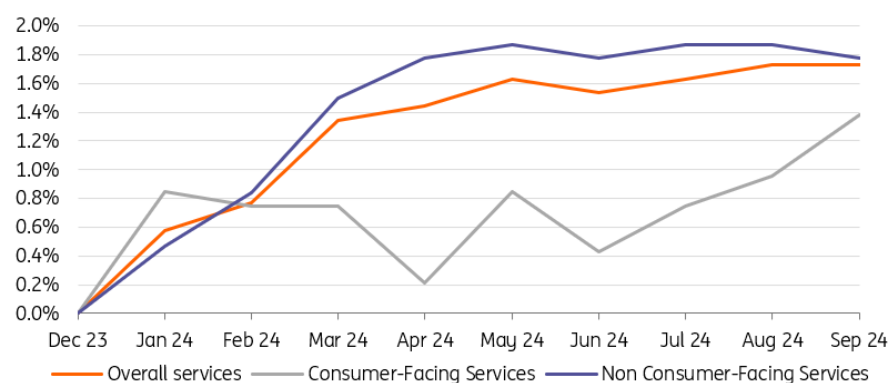
Figures can be deceiving, however, and that's been true of these GDP figures all year. That first half strength was particularly concentrated in two months (January and March), and in sectors that are typically described as non-tradable, or less correlated to underlying economic fundamentals.

Just look at "consumer-facing services" – retail, hotels, restaurants etc. Growth was considerably slower in these categories through much of the first half than it was in those non-consumer

sectors. But unlike that weaker overall third-quarter GDP figure, these consumer sectors actually saw pretty strong 0.5% growth over the summer. Instead, much of the recent weakness has been exaggerated by volatility within industry, particularly manufacturing.

Therefore, we shouldn't overthink the GDP numbers we've been getting recently. The Bank of England has made it abundantly clear that it's not putting much weight on them. Its latest [quarterly report](#) shows that GDP growth has been smoother and less extreme, based on the high-frequency survey data.

Breakdown of UK service-sector output (cumulative % change from Dec 2023)



Services inflation is more important for the Bank of England

Instead, officials are still laser-focused on services inflation, the next batch of which is due next week. Progress has been improving here, though we agree with the Bank that it's likely to stick in the 5% area for the next few months before turning lower again from the spring. Barring any downside surprises, we think the next move in December is a pause, before another rate cut in February.

As for growth, we think we're likely to see quarterly readings in the 0.2-0.3% range over the winter months. Real wage growth is still decent; wage growth is likely to stay above 4.5% for now, which is materially faster than inflation, even if that is set to pick up to 2.7% by year-end (from 1.7% now). Meanwhile, we estimate that roughly 80% of the mortgage squeeze has fed through to households. Our growth forecasts are a little lower than the Bank of England's in the near-term though partly because of our weaker global outlook.

The latest budget will boost growth through next year, though we are still sceptical that spending will rise quite as quickly as the government's plans suggest. Remember the OBR roughly estimates a £60bn increase in spending next year, relative to March budget plans, around a third of which is investment. We're not convinced all of that extra capital spending can be deployed speedily.

The main risk to all of this comes from the jobs market. The picture is blurred by reliability issues in the data, but [company payroll data](#) points to a 0.8% fall in employment this year once government-heavy sectors are excluded. For now there's little sign of that being driven by an increase in layoffs, but that there's a risk that this changes. And if it does, that will heavily dampen growth through 2025.

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