

Three takeaways from UK third-quarter growth figures

While the UK is being kept out of recession by surprisingly resilient consumer spending, the outlook for investment continues to look challenging as we move into 2020. We don't expect rate cuts from the Bank of England just yet, but that could change if the jobs market markedly deteriorates as we move into 2020



Source: iStockphoto

The UK economy grew by 0.3% in the third quarter, although the ongoing distortions of Brexit continue to make the figures hard to read. Here are our three main takeaways:

1 Inventories were a bigger drag than we'd expected

Firms ramped up stockpiling activity ahead of the original March Brexit deadline to insulate themselves against a possible 'no deal' scenario. Since then the jury has been out on exactly what firms have done with all of this excess stock.

These latest growth figures suggest there was a sizable drawdown in inventory during the third quarter, despite the revised Brexit deadline fixed at the end of October. It's possible that firms built up the buffers to some extent again in October, although with warehousing space in short-supply and some existing stock presumably still held, we suspect this effect will be fairly modest.

Ultimately, this is essentially noise and makes extracting the underlying growth trend trickier. It also means that the trade data should be taken with a fairly large pinch of salt.

2 Investment better than hoped, but still disappointing

So what is the underlying trend growth rate? Well the starting point is business investment, which had fallen in every quarter since 2018, with the exception of 1Q19 when accounting changes saw an artificial increase. The good news is that it didn't fall further during the third quarter (it was flat), although we expect the challenging investment backdrop to persist for some time to come.

Even if the Conservatives win a majority at the forthcoming election – and the deal is swiftly ratified – focus will quickly turn to the transition period. This standstill phase lasts until December 2020, and almost certainly will require extending. Until it is, there remains a risk of the UK (excluding Northern Ireland) leaving the single market and customs union at the end of 2020 – a scenario not dissimilar from 'no deal' for most firms.

3 Consumers have kept the UK out of recession

One of the more surprising features of this year's economic performance is the resilience in consumer spending. Admittedly, the pace of consumption growth has been fairly unexciting – spending contributed 0.25% to the overall growth performance. But the performance over the first three quarters of 2019 has been fairly consistent, and indicates that unlike firms, consumers have been less fazed by the twists-and-turns of the Brexit story.

However amid the challenging investment backdrop, there are early signs that the glut in new orders is translating into weaker hiring demand (including in the dominant services sector). Vacancy numbers have fallen modestly, while the latest PMIs spoke of redundancies in some areas. If this story deteriorates further in 2020, this would be negative for consumer activity.

Don't forget that while reduced purchasing power saw retail sales growth slow in 2017/18, the fact that it didn't collapse was partly because employment continued to grow.

All in all, we think the economy is probably growing at a pace of roughly 0.2% per quarter. For now, we think the Bank of England will probably avoid cutting interest rates in the near-term, although a lot depends on Brexit, and whether the jobs market deteriorates further.

Author

James Smith

Developed Markets Economist, UK

james.smith@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.