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Kallum Pickering, Senior UK Economist | Kallum.pickering@berenberg.com | +44 203 465 2672

## UK GDP GROWTH GAINED FURTHER MOMENTUM IN Q4 2017

### Berenberg Macro Flash

#### GDP (a), qoq %, Q4 2017

Actual	0.5
Previous	0.4
Consensus	0.4
Berenberg	0.5

**The UK economy gained pace towards the end of last year.** After a soft patch in H1 2017 where quarterly growth softened to a subdued 0.3%, real GDP growth accelerated in H2, driven by resilient domestic spending and the improving global backdrop. Real GDP expanded by 0.5% qoq in Q4, in line with our own estimate but above the consensus call of 0.4%. The Q4 pace is probably a little above what the UK can sustain outside of the EU in the long-run (0.4-0.45%). Along with the upside surprise to wage growth in the labour market data published earlier this week, the improving growth momentum makes the BoE's ultra-accommodative policy even stance harder to justify – expect a 25bps rate hike in Q2.

**The UK economy expanded by 1.8% yoy in 2017.** While this is below the 2% annual average for the post-Lehman period, it is well above the market's depressed growth expectations at the end of 2016 of 1.2% in 2017 (22 December 2016 Bloomberg consensus) and above our own above-consensus call of 1.5% (22 December 2016). That is, however, not to say that Brexit did not hurt. The UK missed out on the global upswing as Brexit uncertainty weighed on economic activity. Without Brexit, the UK would have probably expanded by c2.5% in 2017.

**Stable domestic demand, stronger external demand:** Looking across the sector data that make up the first estimate of GDP: Domestic oriented services expanded by 0.6% qoq, the strongest growth rate in a year. Despite the temporary real wage shock due to the Brexit-related import price surge in 2016/17 households are holding up well, utilising their balance sheets to smooth their consumption until real wage growth returns in cQ2 this year. Industrial production grew by 0.6% qoq, driven by strong growth in manufacturing – 1.3% qoq – thanks to the solid global backdrop and helped a bit by the competitive boost from the weaker sterling. Even though construction contracted for the third quarter in a row (-1.0% qoq), annual growth in 2017 was a solid 5.1%, after the strong start to 2017. But the sector continues to suffer under the Brexit strain. As expected, economic agents are cautious of making long-lived commitments in uncertain times.

**Brexit hurts already – the odd one out:** While the short-term risks to demand since the Brexit vote have not materialised in a serious way, the outlook for the UK would be much better without Brexit. Until 2016, the UK had one of the strongest post-Lehman recoveries of all advanced economies – Chart 1. While we are above consensus for 2018 and 2019 at 1.8% and 1.9%, respectively (26 January 2018 Bloomberg consensus is 1.4% for 2018 and 2019), because of Brexit uncertainty and the hit to real incomes from the weaker sterling, the UK is set to miss out part of the global upswing. Meanwhile, growth in the UK's major trading partners such as the US and the Eurozone is set accelerate to well above the average of the last few years – Chart 2. However, with the risk of a hard Brexit falling compared to last year - we currently see a 20% chance of a hard Brexit – less uncertainty tilts risks to the UK outlook to the upside. If UK firms, households and markets become less worried about the risk that the UK could crash out of the EU in March 2019 without an agreed framework for future trade with the EU, they will turn less risk averse, further boosting demand.



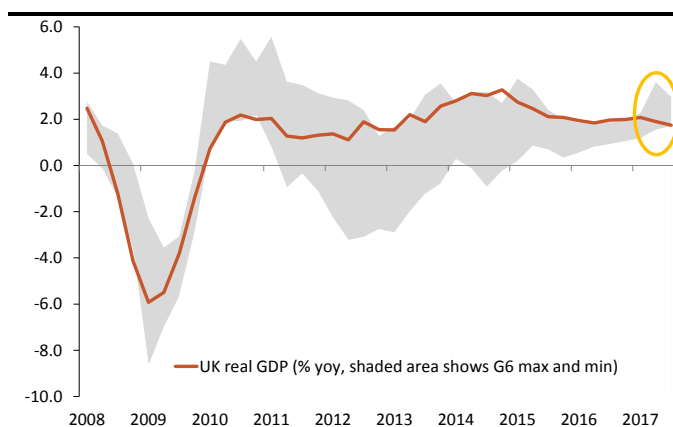
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## MACRO NEWS

Please see '[UK: 8 questions for 2018](#)' for a detailed overview of our key UK calls for 2018.

**Chart 1: UK real GDP versus G6 range (yoy, %)**



Quarterly data. Source: ONS, Bureau of Economic Analysis, Statistics Canada, Eurostat, Cabinet Office of Japan, Berenberg calculations

**Chart 2: The odd one out – UK growth lower after the Brexit vote**

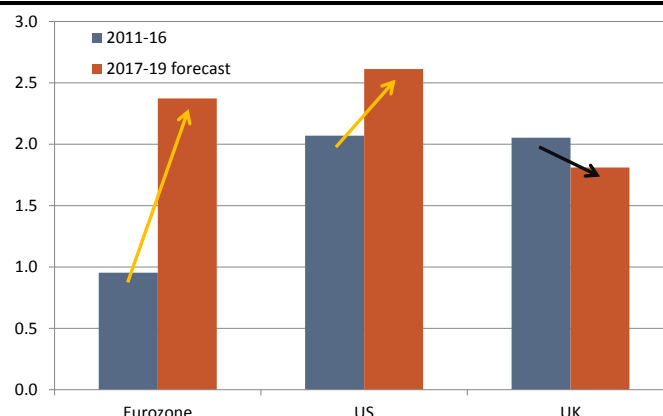


Chart shows average annual real GDP growth in %. Source: Eurostat, Bureau of Economic Analysis, Office of National Statistics, Berenberg calculations and forecasts

qoq %	Q4	Q3	Q2	Q1 17	Q4	Q3	Q2 16
GDP	0.5	0.4	0.3	0.3	0.7	0.5	0.5
Services	0.6	0.4	0.4	0.1	0.6	0.8	0.3
Production	0.6	1.3	-0.1	0.4	0.8	-0.5	2.1
Construction	-1.0	-0.5	-0.3	2.4	3.2	1.2	1.6

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Joh. Berenberg, Gossler & Co.  
 KG  
 60 Threadneedle Street  
 London EC2R 8HP  
 Phone +44 20 3207 7878  
[www.berenberg.com](http://www.berenberg.com)  
[Kallum.pickering@berenberg.com](mailto:Kallum.pickering@berenberg.com)