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UK RETAIL SALES: SOLID TREND DESPITE DECEMBER CORRECTION

Berenberg Macro Flash

Dec	UK, retail sales (ex. auto fuel)	
	yoy	mom
Actual	4.9%	-2.0%
Previous	6.4%	0.2%
Consensus	7.5%	-0.4%
Berenberg	7.5%	-0.4%

THE CONSUMER IS KING

UK consumers are enjoying life, helping the economy to cope with the Brexit shock. Unfortunately, this may not last much longer. The solid growth in retail sales of 1.4% qoq in Q4 (1.9% qoq in Q3) suggests the UK economy ended 2016 on a stable footing. The ten year average quarterly growth rate is 0.5%. Retail sales provide the timeliest official indicator of household demand and spending which makes up two-thirds of GDP. The modest slowdown in the quarterly growth rate supports our call that GDP growth slowed to around its trend rate of 0.5% qoq in the final quarter of last year from 0.6% qoq in the third quarter. *The first estimate of Q4 GDP will be published next Thursday.*

BROAD BASED CORRECTION ON A MONTHLY BASIS BUT ANNUAL GROWTH REMAINED STRONG

On a monthly basis, retail sales ex. fuels declined by 2.0% following gains in the previous two months. Keep in mind, monthly data is volatile. We should not look too much into the larger-than-expected monthly correction. Household spending was strong in the second half of 2016, as shown in the quarterly statistics. Apart from textiles, clothing and footwear, which, remained broadly stable on an annual basis, all categories of sales expanded yoy. On a monthly basis the correction was broad based across all major categories with the largest declines occurring in household goods (7.3% mom) and textiles, clothing and footwear (-3.7% mom). According to the Office of National Statistics, the strong Black Friday sales in November may have exacerbated the drop in December.

BREXIT HEADWINDS SET TO BLOW A LITTLE HARDER IN 2017

In the long-run, the major drivers of real spending are employment, real wages and households' appetite for debt. During the past two years, solid gains in real incomes and rising employment have led to above-trend growth in real consumption. Looking ahead, headwinds from the Brexit vote may begin to blow a little harder. We expect real consumption growth to slow from an average rate of 2.6% yoy in 2015 and 2016 to 1.7% in 2017 and 2018 as real wage gains are eroded by rising inflation (2.5% in 2017 and 2.4% in 2018). Slowing job gains now that the labour market has reached full employment could further reduce demand momentum.

RISKS TILTED TO THE UPSIDE

The recent surge in consumer credit growth to a decade high – in part induced by the aggressive BoE easing in August – shows that households' appetite for debt is rising again. While the return to old habits of excess borrowing may herald a return of the cyclical dynamics of boom-bust, it creates upside risk to our calls for growth over the medium-term. If households raise borrowing a little more than last year and continue to draw down on savings, they could easily sustain the current high growth rate of household con-



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sumption. That nominal wage growth started to accelerate toward the end of 2016 further adds weight to the case for continued strong household spending over the medium-term.

%	DEC	NOV	OCT	SEP	AUG	JUL
UK retail sales (ex. Change auto fuel), yoy	4.9	6.4	7.5	4.1	6.1	5.3
UK retail sales (ex. Change auto fuel), mom	-2.0	0.2	2.1	-0.1	0.1	2.0

Source: ONS

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