

# UK economy

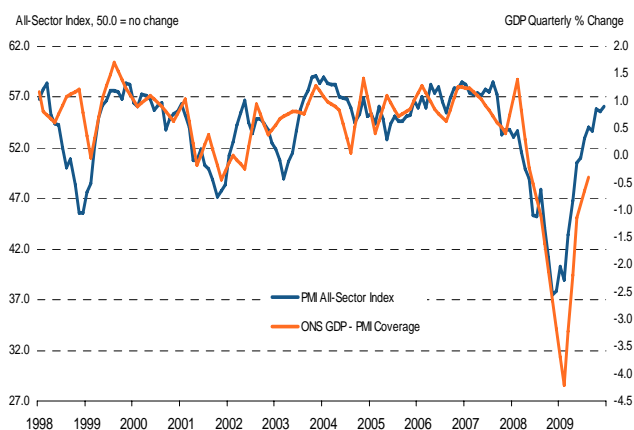
## PMI data signal strong end to 2009, but outlook for 2010 remains cloudy

- **UK economy expanded again at year-end and over Q4 as a whole.**
- **Recovery set to be subdued in 2010.**
- **Data show further rise in inflation.**

December's PMI data indicated growth of the UK private sector extended into an eighth month. The 'All-Sector' Output Index, which is a weighted combination of the Output Indices from the three UK PMI surveys<sup>1</sup>, reached a 27-month peak of 56.1.

December's data marked the end of a year in which the All Sector Output index recovered sharply from November 2008's all-time low. The All-Sector Index has in fact recovered most of the ground lost since the previous peak of 58.5, achieved in August 2007. The data remain consistent with quarterly UK growth in the final quarter of 2009, with the private sector as covered by the PMI surveys<sup>2</sup> on course to deliver expansion of around 0.8% q/q.

### All-Sector PMI and Private Sector Output



Sources: Markit, ONS

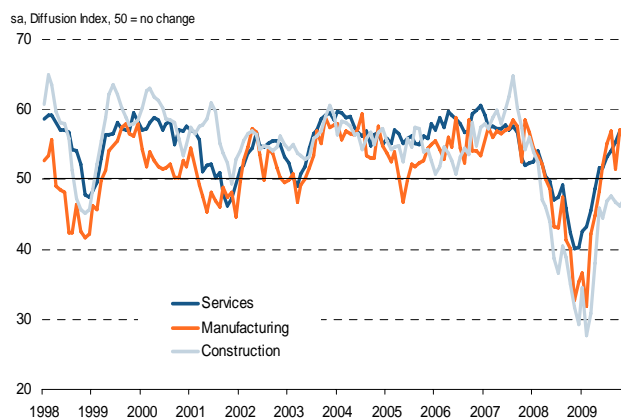
The PMI data show that the services and manufacturing economies both expanded throughout the second half of last year. Service sector activity

<sup>1</sup> Weights determined by each sector's relative contribution to the UK economy according to GDP data.

<sup>2</sup> Private sector output refers to those industries covered by the UK PMIs. Coverage is around 58% of the UK economy.

grew at a rate close to October's two-year peak in December, while manufacturing output rose at the strongest pace for 25 months. Construction remains a laggard, with output declining throughout 2009, albeit to a much lesser degree in recent months.

### PMI Output Data by Sector



Source: Markit

### Uncertain path for economy in 2010

While the PMI data provided both advance warning of the slide into recession in 2008 and an early signal of recovery in 2009, there remain a number of risks relating to the strength and sustainability of the economy in 2010.

A major headwind to economic performance in 2010 will be the expected austerity in the public sector, particularly post-election as the government grapples to regain control of the national debt. It seems inevitable that this will have some adverse impact on the economy, and expected belt-tightening by the government was a factor cited by UK service providers in December as a reason for a caution when assessing the outlook.

Furthermore, while the economy improved markedly towards the end of last year, growth was aided by an inventory bounce, the impact of which will (by definition) fade. Harder evidence of a self-sustaining recovery, ideally underpinned by exports and investment, is likely to be required before policymakers

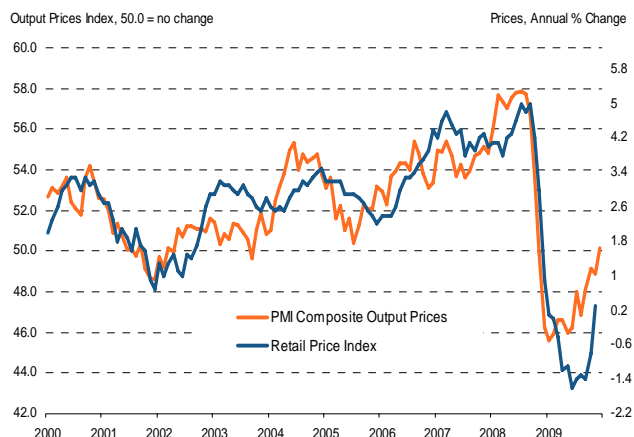
embark on an exit strategy from their current ultra-stimulatory stance. In this respect, the PMI surveys showed manufacturing exports and production of investment goods to have remained largely unchanged in December.

### Inflation continues to rise

December's PMI data also highlighted continuing pipeline price pressures. Input costs in manufacturing increased at the strongest rate for 15 months, while output charges rose for the second successive month. Companies reported that low stock at vendors and higher fuel prices were the main drivers of cost rises in December.

A resulting concern is that the Bank of England may be swayed into an early policy tightening by an increase in inflation. The Bank has anticipated a short-term spike in inflation, but the data need to be watched carefully for any longer-lasting price pressures.

### UK Composite Output Prices & Retail Price Index



Sources: Markit, ONS

### Paul Smith

Senior Economist

Markit

Tel: +44 1491 461 038

Email: [paul.smith@markit.com](mailto:paul.smith@markit.com)

For further information, please visit [www.markit.com](http://www.markit.com)

The intellectual property rights to this report provided herein is owned by Markit Group Limited. Any unauthorised use, including but not limited to copying, distributing, transmitting or otherwise of any data appearing is not permitted without Markit's prior consent. Markit shall not have any liability, duty or obligation for or relating to the content or information ("data") contained herein, any errors, inaccuracies, omissions or delays in the data, or for any actions taken in reliance thereon. In no event shall Markit be liable for any special, incidental, or consequential damages, arising out of the use of the data. Markit is a trademark owned by the Markit group.