

UK Economy

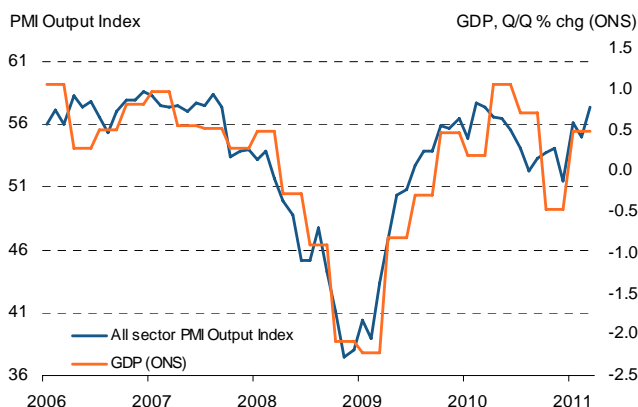
Economy shows feeble rebound in Q1 as construction slumps

- **GDP rose 0.5% in Q1.**
- **Manufacturing and services rose 1.1% and 0.9% respectively, but construction slumped 4.7%.**
- **Without the fall in construction, growth would have been 0.8%.**
- **Weak picture set to persist in Q2.**

According to initial official estimates of gross domestic product (GDP) data, a surprise 0.5% contraction in the final quarter of 2010 has been followed by a modest 0.5% rebound in the first quarter of 2011.

The first quarter GDP growth was in line with consensus and our [recent PMI-based estimate](#), but represents a disappointment for the Bank of England and Office for Budget Responsibility, with both having anticipated a 0.8% increase. We had also hoped that the PMI surveys may have understated the rebound from the final quarter of last year, and had hoped to see a 0.8% increase.

All sector PMI and GDP

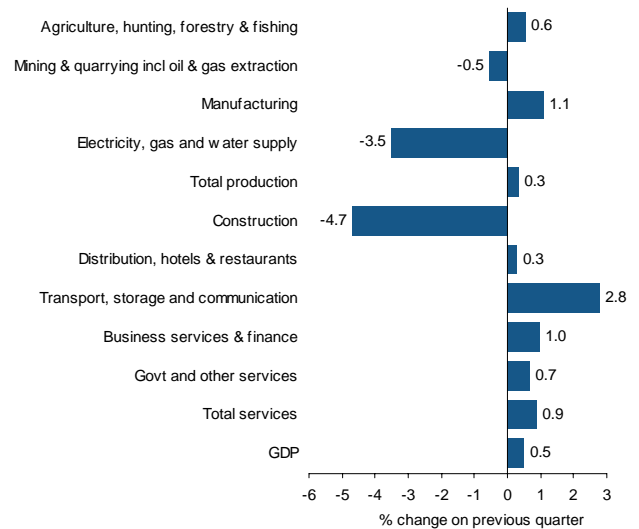


Not as bad as it looks on first sight

Looking at the detail, however, the situation is perhaps not as bad as the headline numbers suggest. Importantly, both manufacturing and services grew strongly in Q1 – expanding by 1.1% and 0.9% respectively. This is broadly in line with the PMI

surveys (though the manufacturing growth is somewhat weaker than the PMI survey indicated), and suggests that the bulk of private sector activity grew at a decent clip in the past three months. The principal area of weakness is the construction sector, which contracted by a startling 4.7%. We find this hard to reconcile with the business survey evidence, and maintain our belief that the sector probably rebounded from the bad weather at the end of last year. Note that **even if construction output had remained unchanged on the snow-affected level seen at the end of last year, GDP would have risen 0.8% in Q1** instead of 0.5%, which is in line with the Bank of England's and OBR's forecasts.

GDP growth by sector in Q1



Weakness likely to persist

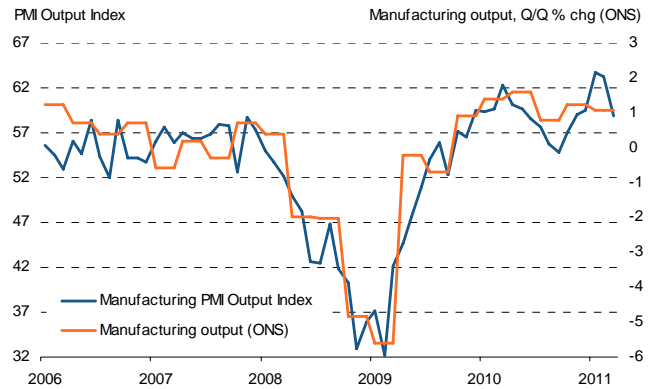
Irrespective of whether these official numbers are accurate or not, the weak pattern of growth indicated by the official data over the past six months should be sufficient to worry policymakers at the Bank of England and encourage them to delay any rate hikes until the recovery can be clearly seen to be on a sound footing. That may take some time. The data we have seen so far for April – such as the disappointing CBI survey of manufacturing and the increasingly downbeat surveys

of consumer confidence – suggest that growth in the second quarter will be modest at best.

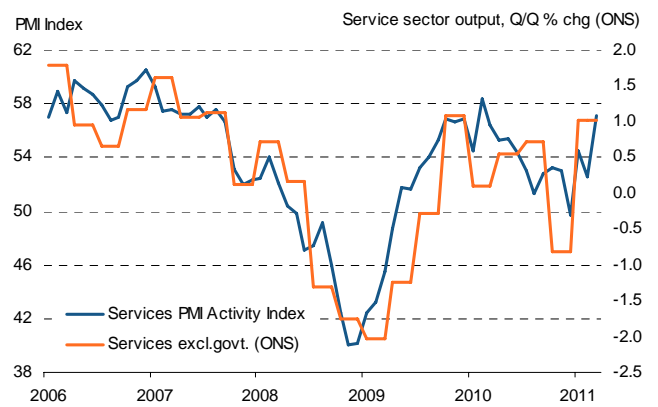
Furthermore, government and 'other' services grew by 0.7% – the largest increase for four years. As we described in our [note of 5 April](#), it appears that budgets were being used up prior to the financial year-end to a greater extent than usual in the first quarter, perhaps due to the impending closures of government departments and projects. This boost to growth is therefore likely to fade as the year proceeds.

It therefore looks like the economy will struggle to grow this year by even the recently downgraded forecast from the Office for Budget Responsibility of 1.7%.

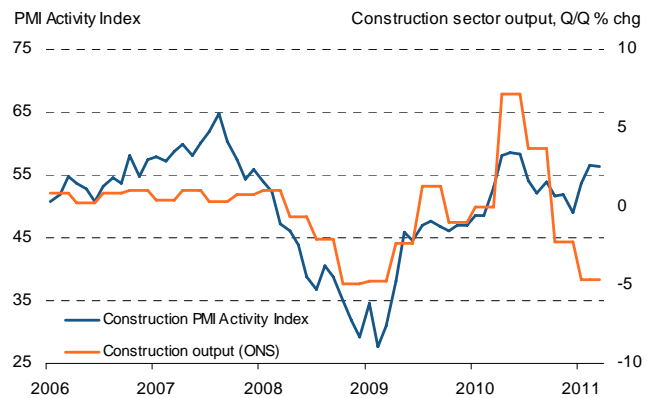
Manufacturing output



Service sector output



Construction output



Sources for all charts: Markit, ONS.

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