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Markit Economic Research

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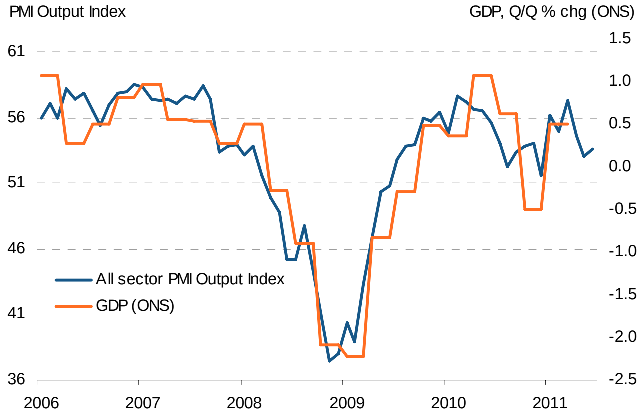
UK Economy

Uplift in PMI™ surveys for June fails to halt Q2 growth slowdown

- **All-sector PMI™ signals quarterly GDP growth of just 0.3% in Q2.**
- **PMI consistent with looser policy.**
- **Broad-based Q2 slowdown.**

The three Markit/CIPS UK PMI™ surveys collectively signalled a faster rate of economic growth in June, but the improvement failed to lift the average pace for the second quarter close to that seen in the first three months of the year. The data suggest that the economy, as measured by gross domestic product, will have expanded by 0.3% at best in the second quarter as a whole, down from 0.5% in the first quarter.

All sector PMI and GDP

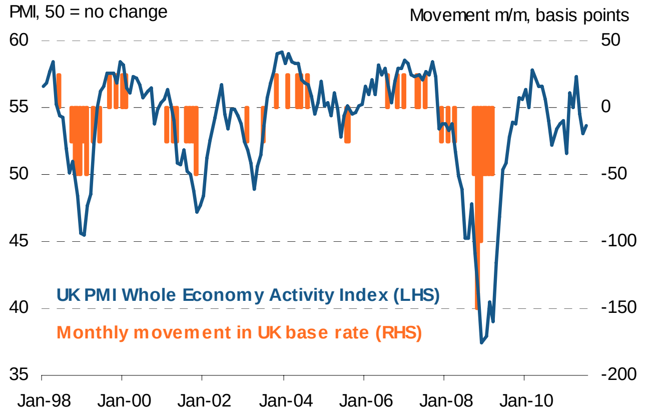


Need for looser policy signalled

The All-Sector PMI Output Index rose from 53.1 in May to 53.6 in June, but the average of 53.8 for the second quarter remained markedly lower than the average of 56.1 seen in the opening quarter.

While the strong survey data in the first quarter of the year added to the prospect of an imminent hike in interest rates by the Bank of England, the recent lower survey readings take the index to a level which is no longer consistent with tighter policy. Judging by historical comparisons, recent PMI data are now in fact more consistent with a further easing of monetary conditions rather than tighter policy.

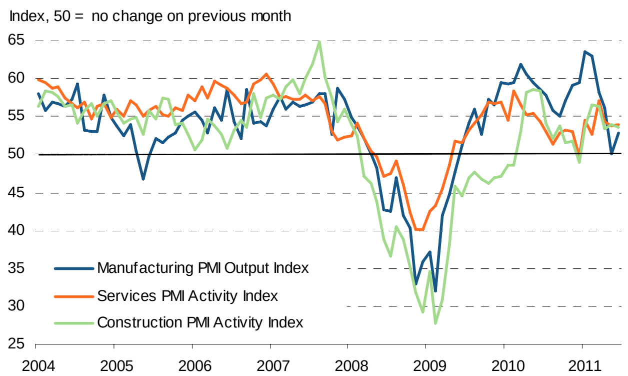
PMI and Bank of England rate setting



Economic growth rate weakens in Q2

Despite the modest upturn in all-sector growth during June, the PMI surveys are clearly pointing to a broad-based slowdown in the construction, manufacturing and services sectors over Q2 as a whole compared to the rates seen in the opening quarter.

PMI Output Indices



The upturn in growth in June was anyway largely expected (see our note from last month) and mainly reflects the removal of temporary factors such as extra public holidays and supply chain disruptions emanating out of Japan that many companies reported to have adversely affected activity levels in May.

Growth may therefore weaken again in July, and the third quarter as a whole, given the temporary nature of the uplift in June and downturns in the forward-looking indicators from the PMI surveys. In particular, manufacturing new orders fell for the second month running in June, and growth of new business levels slowed to five- and four-month lows in construction and services respectively. Measured across all three sectors, new orders rose at the slowest rate for six months. Business optimism also showed signs of weakening, dropping to six- and eight-month lows in construction and services respectively.

Manufacturing could act as drag to Q2 growth

Manufacturing has seen the steepest deterioration in the pace of growth since the start of the year. Despite a 2.7 point rise in June, the Output Index remains almost 11 points below its January near-record peak.

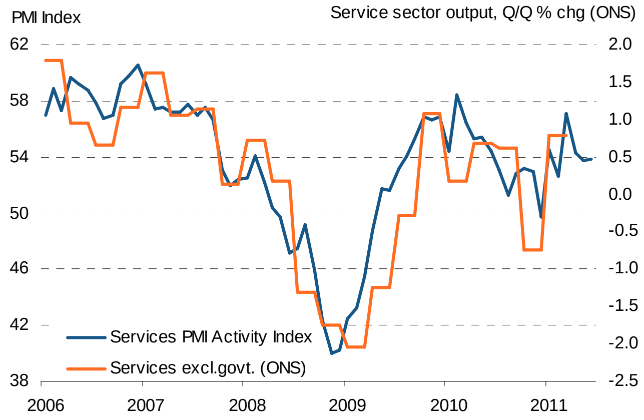
The Output Index is consistent with the official measure of manufacturing production falling at a quarterly rate in excess of 0.8% in June. The sector could therefore act as a drag on GDP growth in Q2, with a decline in manufacturing output of approximately 0.3%-0.5% signalled by the PMI survey. The decline contrasts with the (downwardly revised) 0.7% increase seen in Q1.

Manufacturing output

Services to expand by just 0.5%

In services (excluding government activity), the PMI data suggest that the quarterly rate of growth has slowed from 0.8% in Q1 to around 0.5% in Q2. If public spending cuts accelerate, growth in the service sector as a whole, including government spend, could be even weaker.

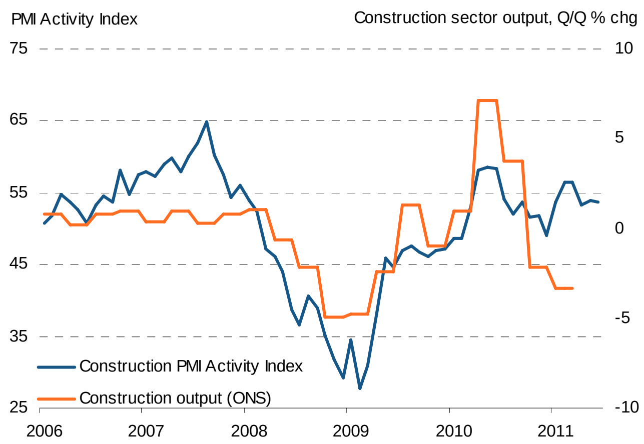
Service sector output



Construction 'recovery' sustained in Q2

The construction PMI data have diverged significantly from the weakness depicted by official estimates of output in the sector. Recent official estimates suggest that construction output fell 3.4% in Q1 (the previous estimate was a decline of 4.0%). The PMI, by contrast, registered growth in Q1, with the Output Index for the sector averaging 55.5 as building rebounded from the weather-related disruptions seen at the end of last year. In Q2, the average fell to 53.6, but still signalled ongoing reasonable growth of the sector.

Construction output



Sources for charts: Markit, ONS, Ecowin, Bank of England.

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