UK economy bounces back in August

October 2023

The UK economy expanded by 0.2% in August, returning to growth but failing to make up for the ground lost by a significant downturn in July (-0.6%), as an expansion in the services sector offset declines in production and construction. However, the poor start to the quarter coupled with a sharp drop in retail sales in September suggests growth in Q3 as a whole is likely to be close to zero. Labour market data also points to softening activity, though assessing current conditions has been made harder as the ONS transitions to a new methodology for its labour market statistics. The latest labour market release nonetheless points to a cooling labour market, with the employment rate and vacancies falling, and unemployment and inactivity rates ticking up. But confidence in the reliability of this data is low. Meanwhile, the Bank of England has expressed concern about the quality of the official data on wage growth, adding complexity to its next interest rate decision in November.

Summer blues?

A 0.4% m/m expansion in the services sector rescued the UK economy from two consecutive months of declining GDP as strength in the professional services, education and information & communication sub-sectors offset a drag from arts & entertainment (with an unwinding of July's #Barbenheimer effect on cinema ticket sales possibly playing a role). Services activity offset falls elsewhere as a contraction in nine out of 13 manufacturing sub-sectors weighed on production, while heavy rainfall in August led to fewer new construction projects.

New experimental data on the labour market suggest a further slight rise in the unemployment rate and a slight fall in employment in June – August compared with the previous three months (75.7% vs 76.0%). The ONS have only one date point (July – September) to compare the experimental against the previous methodology: the experimental data shows an employment rate of 75.7% vs 75.5% for the old methodology, for example. This is consistent with concerns that the LFS may be understating the strength of employment, given trends in payroll data, for example. Further doubts have recently been expressed about the reliability of the ONS wage data, with the Bank of England noting that business surveys have recently been pointing to more modest wage growth. Understanding conditions in the labour market is fundamental for judging the extent to which the economy is slowing and, therefore, whether the Bank need to apply the brakes harder.

provided experimental estimates for the last two rolling quarters from July, which do show some slight differences from the previous estimates The total employment rate fell slightly to 75.7% in the three months to August (down by 0.3pp compared with the three months to May). The unemployment and inactivity rates ticked up by 0.2pp to 4.2%, and 0.1% to 20.9%, respectively. Nonetheless, the picture of a gradual easing of labour demand is also reflected in a decline in the total number of vacancies, which have fallen for 15 consecutive rolling quarters to 988,000 in the three months to September, down from over 1.3 million in the three months to May 2022.

The ONS's latest earnings statistics show that year-on-year regular wage growth remains elevated. Private sector wage growth increased by 0.1pp compared with the three months to May to 8% in the three months to August (close to the fastest rates outside of the pandemic era). Public sector wage growth was also strong, boosted from one off payments to NHS staff and civil servants, which pushed the annual rate to 6.8%, the highest figure since records began in 2001. Taking inflation into account, real regular pay has turned positive in recent months, rising by 1.1% in the quarter to August (when adjusting for CPIH) or 0.7% (using our preferred CPI measure). Looking ahead, CBI surveys expect wage growth to ease over the next 12 months (from 5.9% in the year to September versus 4.5% in the 12 months to September 2024) suggest that salary pressures are softening, meaning that the Bank of England's Monetary Policy Committee (MPC) is likely to keep interest rates at 5.25% at its next meeting on 2 November.

Altogether, recent indicators paint a picture of an economy that is slowing. Despite revisions to GDP data over the past three years which show the economy is substantially larger than we previously thought, they don't alter the picture of a fairly subdued economic performance since the beginning of 2022. The latest GDP figures suggest that the economy is set to stagnate (or even shrink marginally) during the third quarter as September needs to see a robust expansion to keep GDP above its end-Q2 level (0.5% m/m or higher, barring any significant revisions).

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Further details

Increased services activity drives 0.2% GDP growth in August

- **UK GDP rose by 0.2% month-on-month (m/m) in August** following a fall of 0.6% in July (revised from -0.5%). This matched with consensus expectations, with a rebound in output in the services sector offsetting declines in both production and construction.
- On a rolling 3-month basis – a better gauge of underlying growth **– GDP grew by 0.3% in the 3-months to August** (which includes June's strong outturn of 0.7%).
- These are the first monthly numbers to include both the ONS' recent "Blue Book" revisions for GDP growth in 2020 and 2021, and revisions to national accounts which found **the economy is 2.1% larger than before the pandemic in February 2020** (compared to 0.2% larger under previous monthly estimates).
- The increase in GDP in August was driven by services activity growing 0.4% m/m, which saw increased output in professional services, education (which rebounded from teachers' strikes in July) and IT sub-sectors.
    - Output in consumer facing services fell by 0.6% in August, reflecting weakness in art & entertainment, food services, and travel agencies. Consumer-facing services remain 4.3% below their February 2020 levels.
- Services activity offset a decline of 0.7% m/m in the production sector as manufacturing output fell by 0.8% with nine out of 13 sub-sectors seeing contractions. The construction sector also saw a decline (0.5% m/m) as a contraction in new work offset an increase in repair & maintenance.
- ONS referenced anecdotal evidence they've received from businesses across the UK economy that industrial action had impacted operations, with the health sector (junior

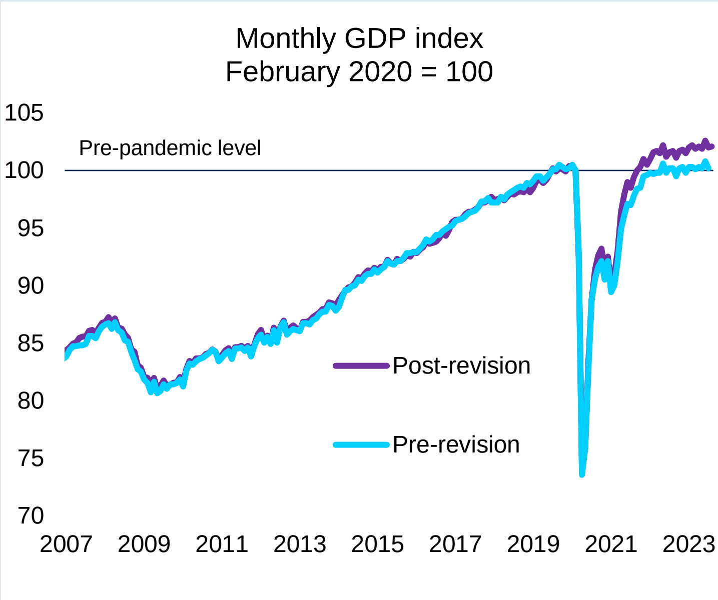
and senior doctors), rail network and parts of the transport network (buses and airports) all seeing industrial action in August which affected activity.

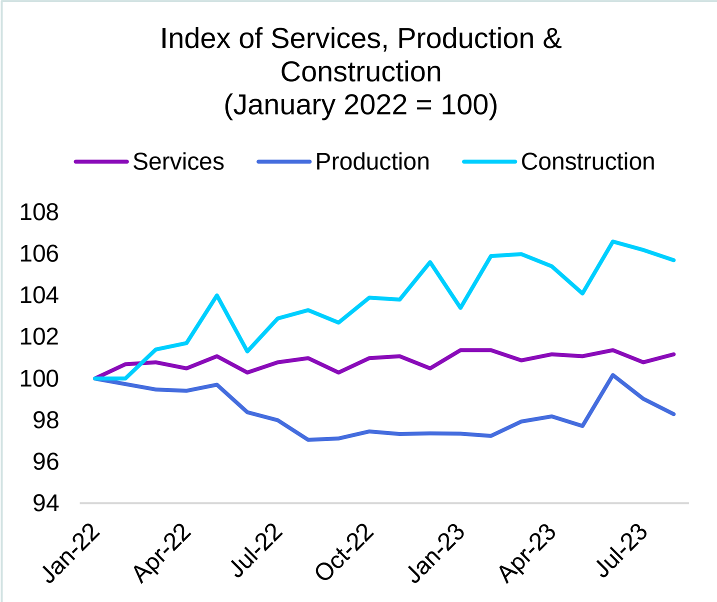
Experimental data shows unemployment and inactivity ticking up

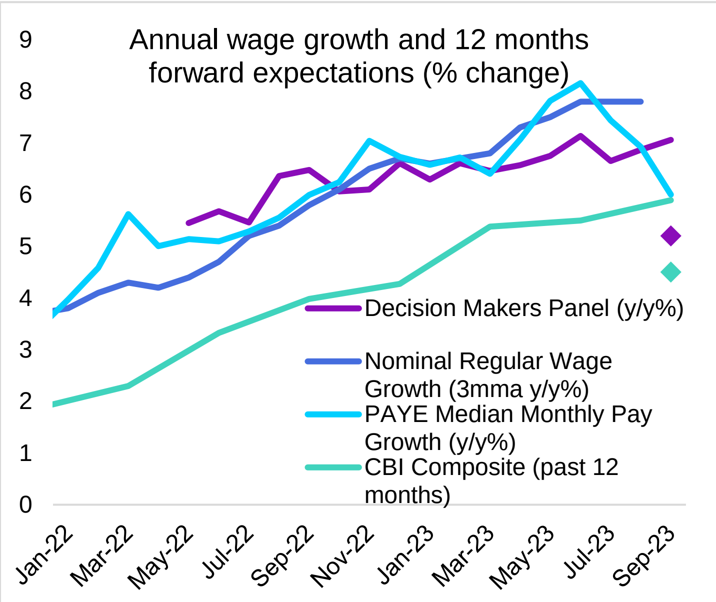
- The ONS is transitioning to a new methodology in the publication of its labour market surveys, so detailed estimates of employment, unemployment and inactivity are unavailable. This is primarily because response rates to the ONS' surveys have been steadily falling in recent years. Between now and Spring 2024, the ONS will only be publishing *experimental* estimates of labour market data The numbers below represent these new estimates for the last two quarters.
- The employment rate stood at 75.7% in the three months to August, a 0.3pp decrease from the three months to May.
- The unemployment rate stood at 4.2%, up 0.2pp from the previous quarter.
- The inactivity rate increased 0.1pp from the previous quarter to 20.9%
- The labour market continues to loosen, though remains historically tight, as the number of vacancies fell for the 15th consecutive rolling-quarter to 988,000 in the quarter to September (though vacancies are still 20% above pre-pandemic levels).

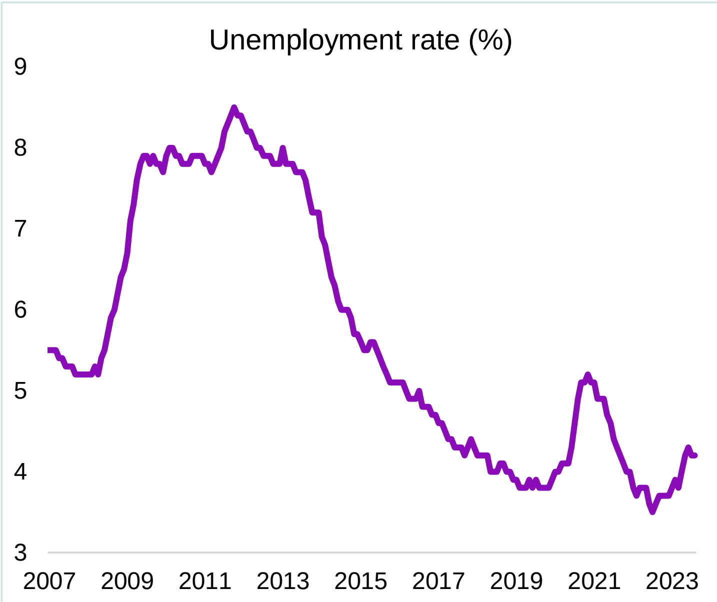
Wage growth accelerates in the public sector, with real wages growing for the first time in nearly two years

- Nominal regular pay (excl. bonuses) rose by 7.8% over the year to June-August 2023, posting three consecutive rolling-quarters for the fastest rate of growth seen since records began in 2001.
    - Nominal regular pay growth stood at 8% in the private sector, accelerating slightly from 7.9% in the three months to May, and one of the fastest rates outside of the pandemic period. Nominal pay growth accelerated in the public sector as one-off payments to NHS staff and civil servants boosted growth to 6.8%, the highest figure since records began.
    - Finance & business services saw the fastest wage growth by sector (9.6%, the highest since records began), followed by manufacturing (8%), wholesaling, retailing, hotels & restaurants (6.6%), and construction (5.7%)
- Adjusting for CPIH inflation, real regular pay across the economy rose by 1.1% in the year to June-August, following a 0.6% fall in the March-May period. Whereas adjusting for CPI (our preferred measure of inflation) real regular pay rose 0.7% in the three months to August.









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