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Markit Economic Research

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United Kingdom

Construction sector booms, Bank of England raises prospect of 2014 rate hike

- **Construction grows 1.2% in April after revised 1.5% gain in Q1**
- **Q1 GDP could get revised higher**
- **Data follow hawkish comments from Bank of England**

A booming construction industry, faster-than-previously-thought economic growth at the start of the year and hawkish remarks from the Bank of England's Governor Mark Carney point to interest rates starting to rise later this year.

Data from the Office for National Statistics confirmed survey evidence of surging growth in the construction sector so far this year, with output rising 1.2% in April compared to March. The construction data follow news that the manufacturing sector was also booming in April, suggesting the economy is on course for another spell of strong growth, perhaps 0.8%, in the second quarter.

The release also included major revisions to growth of construction activity in the first quarter, which means that GDP for the first three months of the year may get revised higher. While the ONS pencilled-in just 0.6% construction output growth in the first quarter, this has been revised up to 1.5%, more than double the prior estimate. The upward revision brings the official data more into line with the PMI survey evidence, which has signalled a booming construction sector since last summer. Assuming data for other sectors were unchanged, this would push GDP growth in the first quarter up from 0.8% to 0.9%, the strongest expansion since the second quarter of 2010.

Note that this is not just a housing market upturn. Although private sector housing activity was 2.5% higher in April compared to March, private sector industrial work rose by 3.8% and infrastructure building grew 0.6%.

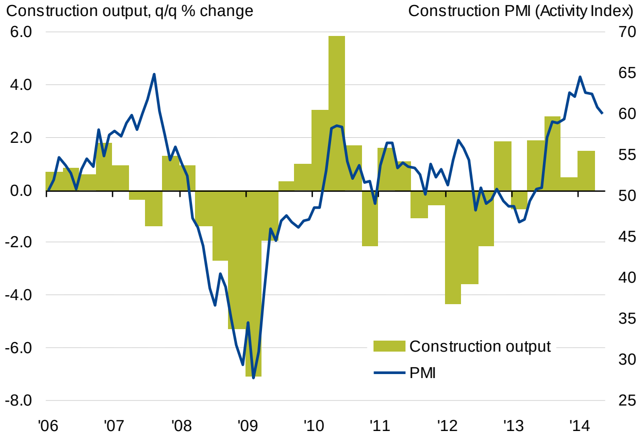
Carney hints at rate rise later this year

Mark Carney's Mansion House speech last night meanwhile gives the impression that discussion among the Bank of England's Monetary Policy Committee heated up at the June meeting. It's likely that there's a growing call among the Committee members for an earlier rate hike than spring 2015, which is when the markets and the Bank have been suggesting we should be looking for a tightening to start. Clearly, the housing market is a key concern and the Bank is increasingly worried of the possibility that so-called 'macro-prudential tools', such as limits on borrowers' mortgage-to-salary multiples, may not be sufficient to cool the housing market unless accompanied by higher interest rates.

It is also likely that the recent batch of strong labour market data is tilting the policy discussion towards the need for higher interest rates. The rapid recovery of the labour market has taken the Bank by surprise and has been the principal cause of the Bank needing to revise its estimates of when rates will start rising.

In his speech, Carney stressed that the first rate rise 'could happen sooner than markets expect', noting "when you hear the thunder of the falls, it is wise to get off the river". November seems a distinct possibility, as that is when the Bank updates its forecasts in its quarterly Inflation Report. However, perhaps we should also not rule out a hike when the August Report is published, if the economic data continue to surprise to the upside in coming months, especially in relation to wages.

UK construction output



Sources: Markit, ONS.

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