

# United Kingdom

## Official data confirm second quarter economic growth spurt

- GDP rose 0.6% in Q2, up from 0.3% in Q1
- Growth led by services, though manufacturing and construction also expanded
- Policymakers likely to focus on GDP being still 3.3% below pre-crisis peak

The UK economic recovery gained momentum in the second quarter. Initial estimates from the Office for National Statistics showed the economy grew 0.6%, twice the rate seen in the first three months of the year. The rise was in line with expectations following increasingly buoyant business surveys in recent months.

Excluding last summer's boost from the Olympics, the rise was the strongest for almost two years.

Prospects look good for a continuation of the recovery in the third quarter, with consumers and businesses both helping drive the upturn. There are even signs that exporters will see improved sales, helping drive the long-awaited re-balancing of the economy.

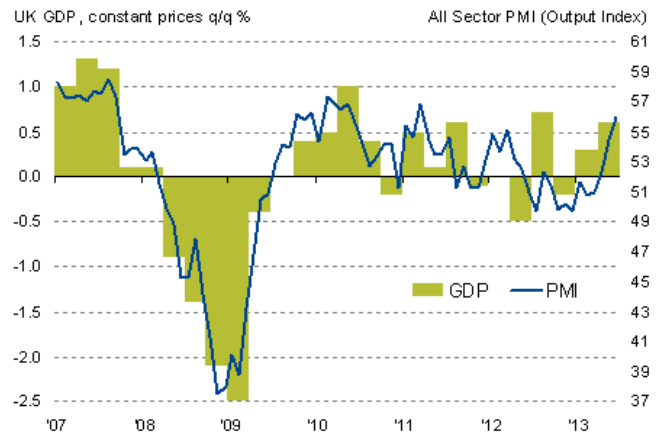
If this really is the start of a robust and sustainable improvement in the economy, it begs the question of how long can ultra-loose policy be justified for.

Data from the [Office for National Statistics](#) showed that growth was led by the vast service sector, which expanded 0.6%. Manufacturing output rose 0.4% and construction output jumped 0.9%.

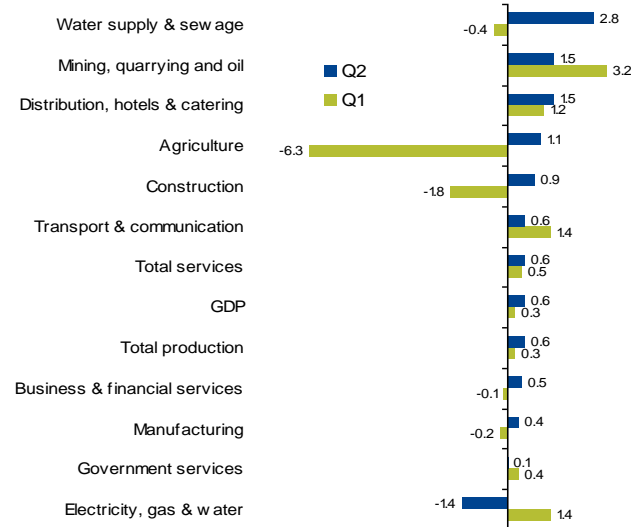
### Good third quarter prospects

The broad-based upturn mirrored the message from the business surveys, which also suggest that the pace of growth looks to have accelerated towards the end of the second quarter. The three PMI surveys showed a [triple-whammy of strengthening growth](#) in manufacturing, construction and services in June, suggesting that the economy not only gained momentum at the end of the quarter but that the acceleration was reassuringly broad-based. The strongest growth of business activity for two years was in itself encouraging enough, but the accompanying

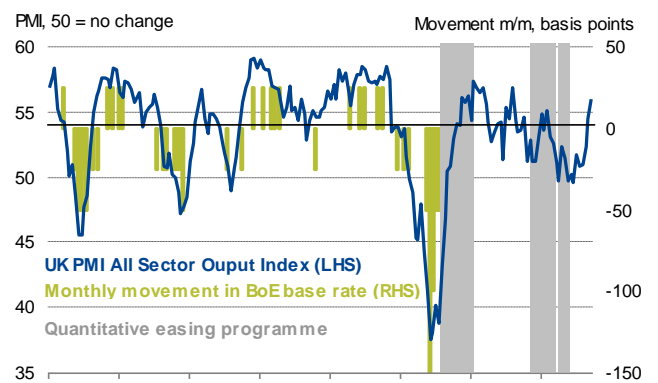
### GDP and business surveys in sync



### GDP by sector, ranked by quarterly % change in Q2



### PMI and Bank of England policy



news from the PMIs that employment and new orders rose at the fastest rates for almost six years added further optimism that the recovery is looking different to the false dawn we saw in 2010.

### Brighter households

The mood among households has also brightened, which helped boost consumer spending in the second quarter. With Markit's [survey of household finances](#) hitting a record, post-crisis high in July, the upturn in spending is likely to have persisted at the start of the third quarter.

There's some doubt as to how sustainable this increase in spending is. In particular, there's a fairly widespread acceptance among economists that strong growth is unlikely to persist if real wages continue to fall, as they have been doing for almost four years. However, wage growth is showing signs of picking up again, and inflation looks set to ease, which means this income squeeze should ease as we move towards the end of the year and could act as less of a drag on consumption.

### Improving export climate

At the same time, there are signs that the UK's largest export market, the eurozone, is finally pulling out of recession. A [return to growth in the eurozone](#) should help the plight of UK exporters as well as buoy global business confidence, which has been dented by worries about the single currency area since the Greek crisis erupted in 2010.

Fears of a US slowdown also look overplayed, with signs of the manufacturing sector and consumer confidence picking up again in July.

It therefore looks likely that we will see further robust growth in the third quarter, which would make this by far the best period of expansion since the economy pulled out of the 2008-9 recession.

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## Chris Williamson

### Chief Economist

Markit

Tel: +44 207 260 2329

Email: [chris.williamson@markit.com](mailto:chris.williamson@markit.com)

[Click here](#) for more PMI and economic commentary.

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

### How long can policy stay ultra-loose for?

However, there's no doubt that risks persist to the outlook: there's still a long way to go to fix the problems of the euro area, economic growth has slowed in China and other emerging markets, and there's great uncertainty about how markets and economies will respond to the eventual withdrawal of central bank stimulus.

In the latter respect, the Bank of England will be pleased to see the economy improving in line with their expectations, though policymakers are likely to place emphasis on the fact that GDP remains some 3.3% below its peak reached in the first quarter of 2008, highlighting the disappointing recovery relative to past recessions and other major economies.

We therefore wait for August 7<sup>th</sup> to see how policy will be shaped under new governor Mark Carney, including how "forward guidance" will work in practice. However, it is becoming increasingly unlikely that a prolonged, two-to-three year, period of record-low interest rates can be justified if this really does mark the start of a sustainable, robust upturn, especially if inflation remains stubbornly high.