4th floor
Ropemaker Place
25 Ropemaker Street
London
EC2Y 9LY
United Kingdom

tel +44 20 7260 2000
fax +44 20 7260 2001
www.markit.com

Markit Economic Research

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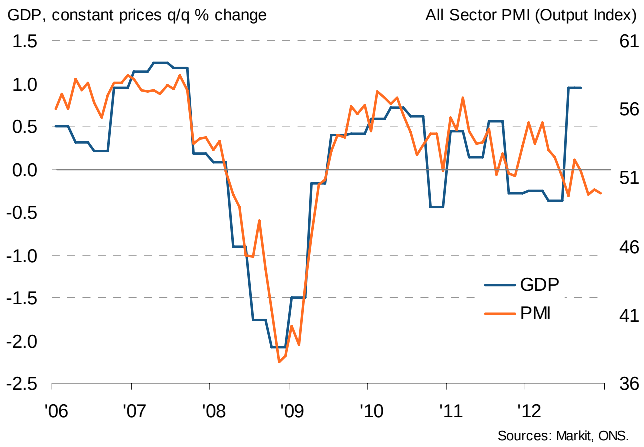
United Kingdom

Renewed weakness in December PMI surveys rounds off worst quarter for three-and-a-half years

- **All sector PMI falls back below 50.0 no change level in December**
- **Improvement in manufacturing offset by worsening picture in services and construction**
- **New orders fall at fastest rate since April 2009**

The UK saw a renewed bout of economic weakness at the end of 2012. The all-sector Output Index from the three PMI surveys fell below the 50.0 no change level for the second time in three months in December, dropping from 50.1 in November to 49.9. Over the fourth quarter as a whole, the PMI surveys have signalled the worst performance since the second quarter of 2009, suggesting that the underlying health of the economy deteriorated towards the end of the year.

GDP and the PMI

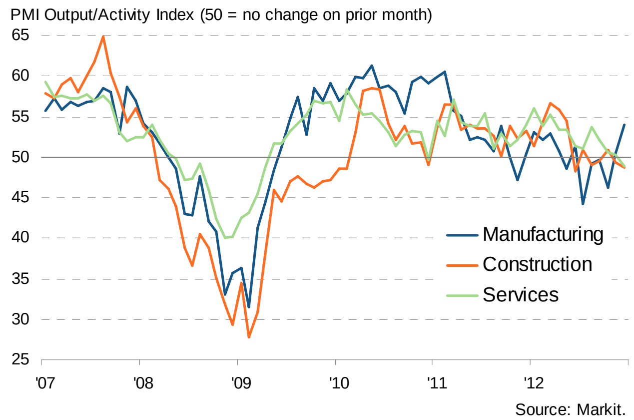


Historically, the PMI is consistent with GDP falling by approximately 0.2% in the fourth quarter, representing a marked turnaround from the 0.9% expansion seen in the third quarter. However, comparisons between the PMI and recent official gross domestic product data have been difficult as the latter have been distorted by extra public holidays hitting growth in the second quarter, and then the Olympics and working day effects boosting growth in the third quarter. So far the monthly flow of official data has pointed to a flat picture for the fourth quarter at best.

Very divergent trends are apparent by sector, according to the PMIs. Whereas both construction and services saw lower levels of business activity in December, the latter having shown particular weakness compared to the strong growth seen earlier in the year, manufacturing enjoyed the largest monthly increase in production since April 2011.

Other PMI indicators showed new orders falling across the three sectors for the second successive month, declining at the fastest rate since April 2009. The weakness of demand prompted firms to cut employment for the fourth month in a row, though only marginal declines were seen in all three sectors.

Sector output trends compared

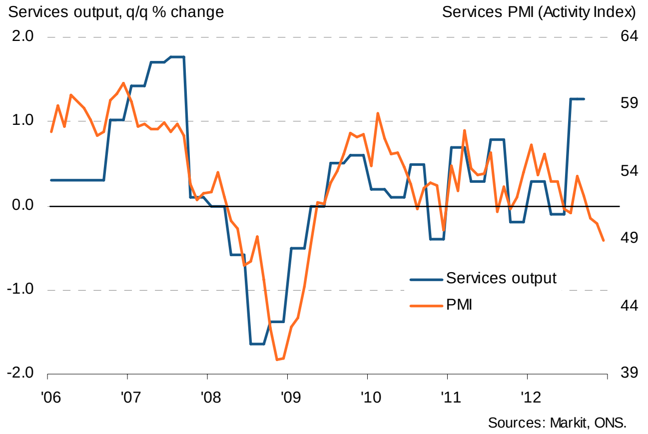


Service sector activity falls

The principal area of weakness in December was the service sector, where the Business Activity Index fell from 50.2 in November to 48.9, pointing to the first monthly fall in activity since the heavy snowfall of December 2010 and the largest monthly decline since April 2009.

Over the fourth quarter as a whole, the Business Activity index averaged 49.9 compared to 52.3 in the third quarter, the lowest quarterly average since the first three months of 2009. Having provided a major impetus to the economic expansion seen in the third quarter, growing some 1.3%, the service sector could see output fall slightly in the final quarter of 2012.

Services

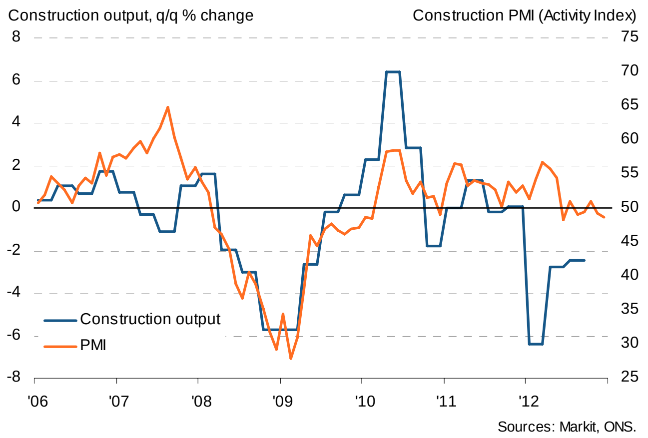


Construction slips further into decline

Business activity in the construction sector also fell in December. With the exception of last June, when activity was affected by the additional public holiday, the latest drop in activity was the largest since February 2010, though remains far weaker than the downturn seen in 2008-9. Nevertheless, with the Construction PMI Activity Index averaging 49.6 in the fourth quarter, down from 49.8 in the third quarter, the sector looks likely to have acted as a drag on the overall economy in the closing months of 2012.

Furthermore, with new business falling at the fastest rate since April 2009 in December, activity in the construction sector looks likely to remain in decline at the start of 2013.

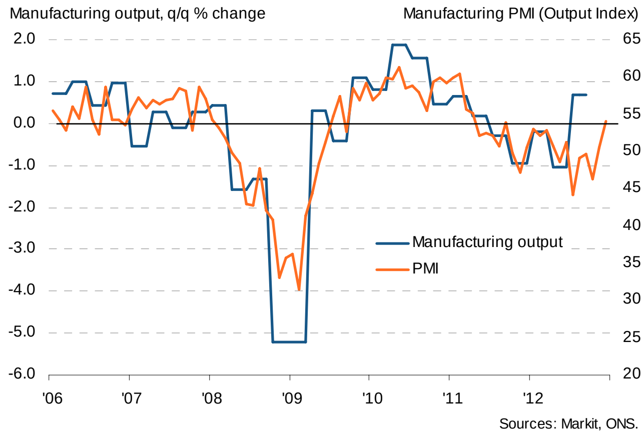
Construction



Manufacturing output growth hits 20-month high

In contrast to the renewed downturns seen in services and construction, the manufacturing sector's performance improved in December. The PMI Output Index rose from 50.5 to a 20-month high of 54.0. The upturn pushed the average index reading for the fourth quarter up to 50.3 compared to 47.7 in the third quarter. Historical comparisons of the PMI against official data suggest that the improvement in the PMI in December may be insufficient to prevent the manufacturing sector contracting in the fourth quarter. However, the gain in momentum seen towards the end of the year bodes well for the first quarter of 2013.

Manufacturing



Chris Williamson

Chief Economist

Markit

Tel: +44 207 260 2329

Email: chris.williamson@markit.com

For further information, please visit www.markit.com