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Markit Economic Research

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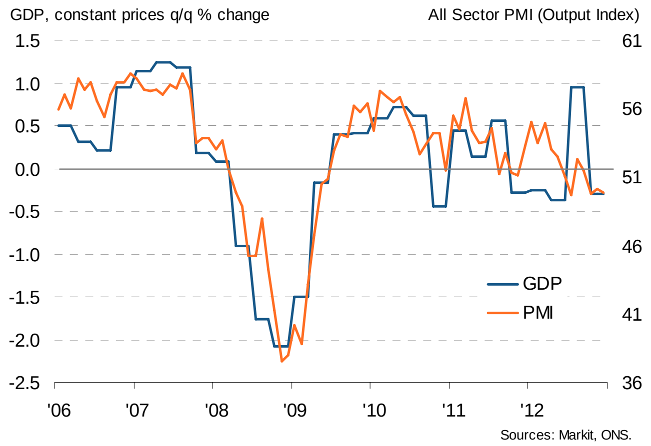
United Kingdom

Official data confirm fourth quarter economic contraction

- **GDP falls 0.3% against expectations of -0.1%**
- **Large part of decline due to disrupted North Sea oil production, but underlying weakness evident**
- **Data raise risk of triple-dip recession**

The UK economy contracted more than expected in the final three months of last year according to official data, confirming earlier signs of weakness from the business surveys. The disappointing numbers bang another nail in the coffin of the UK's AAA credit rating as the country faces the growing risk of a triple-dip recession.

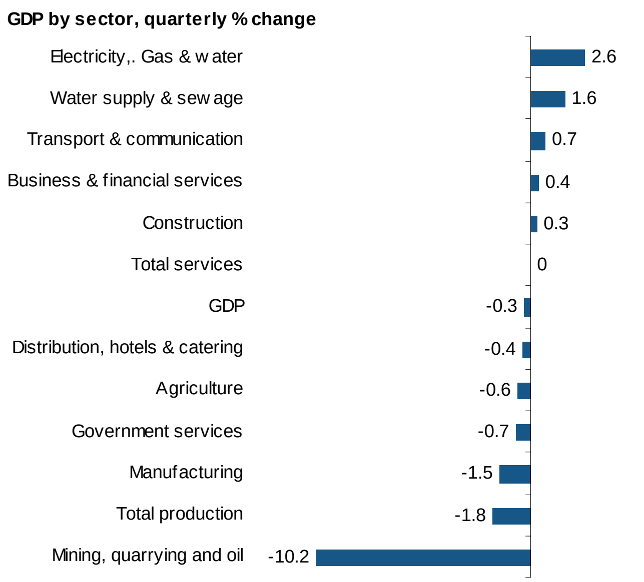
GDP and the PMI compared



The first estimate of economic growth in the final quarter of last year showed the economy contracted by 0.3%, its largest decline since the second quarter of last year. After a strong performance in the third quarter, reflecting an extra working day compared to the second quarter and a boost from the Olympics, some pay-back was always expected, and part of the weakness reflected disruption to North Sea oil fields, which was estimated to have accounted for just over half of the total decline. The underlying situation is therefore perhaps not as disappointing as the headline number suggests.

However, there were signs of broad-based weakness throughout the economy. Manufacturing output fell by 1.5% and the service sector stagnated. Bad weather is likely to have contributed to a 0.6% decline in agriculture, leaving construction as the only major part of the economy managing to eke out any growth, expanding 0.3%.

Fourth quarter GDP change by sector



Snow-blurred picture for first quarter

Looking ahead, there is great uncertainty about the first quarter, as different parts of the economy are moving in different directions. While the more domestically-focused service sector is weakening, contracting at the fastest rate for two years in December according to the PMI, the manufacturing sector appears to be gaining growth momentum, buoyed by rising demand from the US, Germany and emerging markets in particular.

The question is whether the smaller manufacturing sector can help drive a return to growth in the wider economy, or whether weak domestic consumer and business confidence will mean a downturn in services and retail offset any expansion of the goods-producing sector.

A bright light is that the Eurozone crisis - which has been widely blamed as one of the key causes of the weaker-than-expected UK recovery to date, is showing signs of easing. At the same time, the Funding for Lending Scheme is showing signs of helping boost credit availability. However, adverse weather, including heavy snow and freezing conditions, will inevitably put a toll on the UK economy and raise the risk of a further contraction in the first quarter.

At the moment it remains too early to tell if the economy will triple-dip, but today's numbers have greatly increased the risk of a new recession and a downgrading of the UK's AAA credit rating. As such, the data pile ever more pressure on the Chancellor to seek ways to revive the economy in the March Budget.

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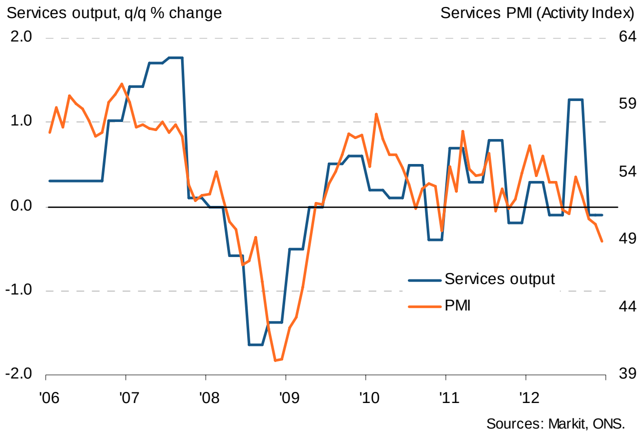
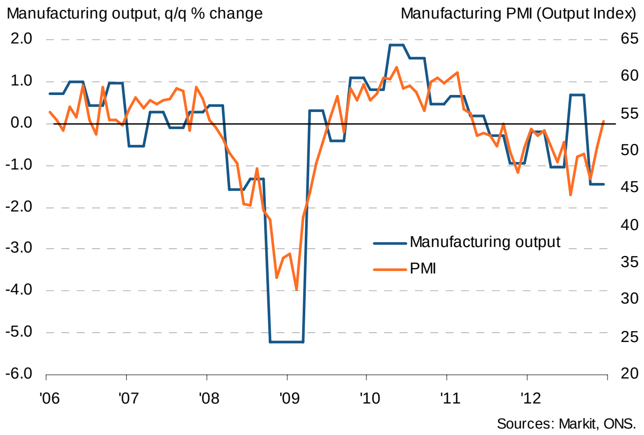
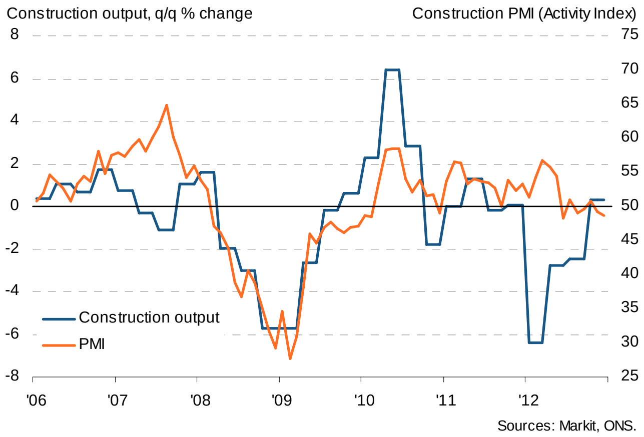
Services



Manufacturing



Construction



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