

United Kingdom

Retail sales show strongest annual rise in nine years

- **Retail sales beat expectations in December.**
Rise of 2.6% compared with expected 0.3% rise
- **Annual growth was the largest for nine years**
- **Fourth quarter growth remained weaker than prior quarters despite the December rise**

UK retail sales smashed through expectations in December. Despite the rise, sales over the fourth quarter as a whole slowed compared to the previous quarter, suggesting growth in the wider economy may also have weakened, but the strength of the latest upswing bodes well for a continuation of strong economic growth as we move into 2014.

Sales volumes rose 2.6% in December, even after accounting for seasonal influences, according to the Office for National Statistics, registering the largest monthly rise since February 2010. Growth rarely gets stronger than this. Sales were some 5.3% higher than a year ago, indicating the fastest rate of year-on-year growth since late 2004.

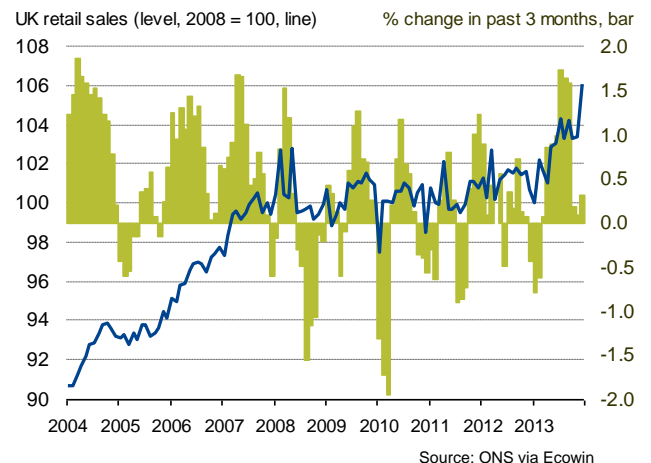
Sales values also rose 2.6%, up 6.1% on a year ago, dispelling fears that volumes may have risen purely due to heavy discounting.

The strength of the latest increase raises suspicions that we could see a big pay-back in January, as shoppers see their credit card statements and the hangover sets in. On the other hand, it seems more likely that the latest rise is primarily a rebound from the weakness in prior months.

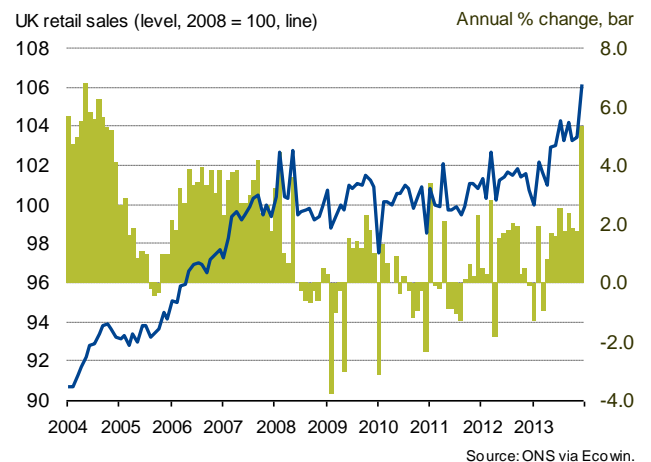
Sales have been volatile in recent months, and the 2.6% increase in December follows disappointing data in prior months. Sales were up just 0.1% in November and had fallen 0.9% in October.

Sales in the latest three months were just 0.4% higher than in the previous three months as a result, suggesting the retail sector made a much weaker contribution to the economy in the fourth quarter than in previous quarters. The 0.4% fourth quarter rise compares with 1.6% in the third quarter and 1.0% in the second quarter (periods when GDP rose 0.8%).

Retail sales



Core retail sales



The retail data therefore add to signs that the official data are coming in weaker than the business surveys, suggesting GDP growth may have slowed slightly in the fourth quarter, perhaps to 0.7%.

The increase in sales also corresponds with a number of factors that have buoyed households' spirits about their financial situation, which also bodes well for sales to continue to expand in coming months. Consumer confidence has improved in recent months, fueled by improved job security as the labour market picks up, the better economic news flow in the media and lower inflation. At the same time, more people are in employment, which naturally boosts consumer spending as more people are earning. However,

wages are also starting to rise, according to survey data.

With inflation down to its lowest for four years and wage pressures beginning to build, we should see wages start to rise in real terms by mid-year, which should help drive a sustained increase in household well-being and spending.

A big uncertainty is interest rates. In particular, it will be important to see how households react to the prospect of higher interest rates, given recent signs that the Bank of England may need to tighten policy sooner than previously thought if the economy continues to improve at the pace we've seen in recent months.

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