Office for National Statistics

Compendium

National accounts at a glance

An examination of recent trends and movements within the UK economy, focusing particularly on how the economy has evolved since the EU referendum in June 2016.

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1 . Introduction

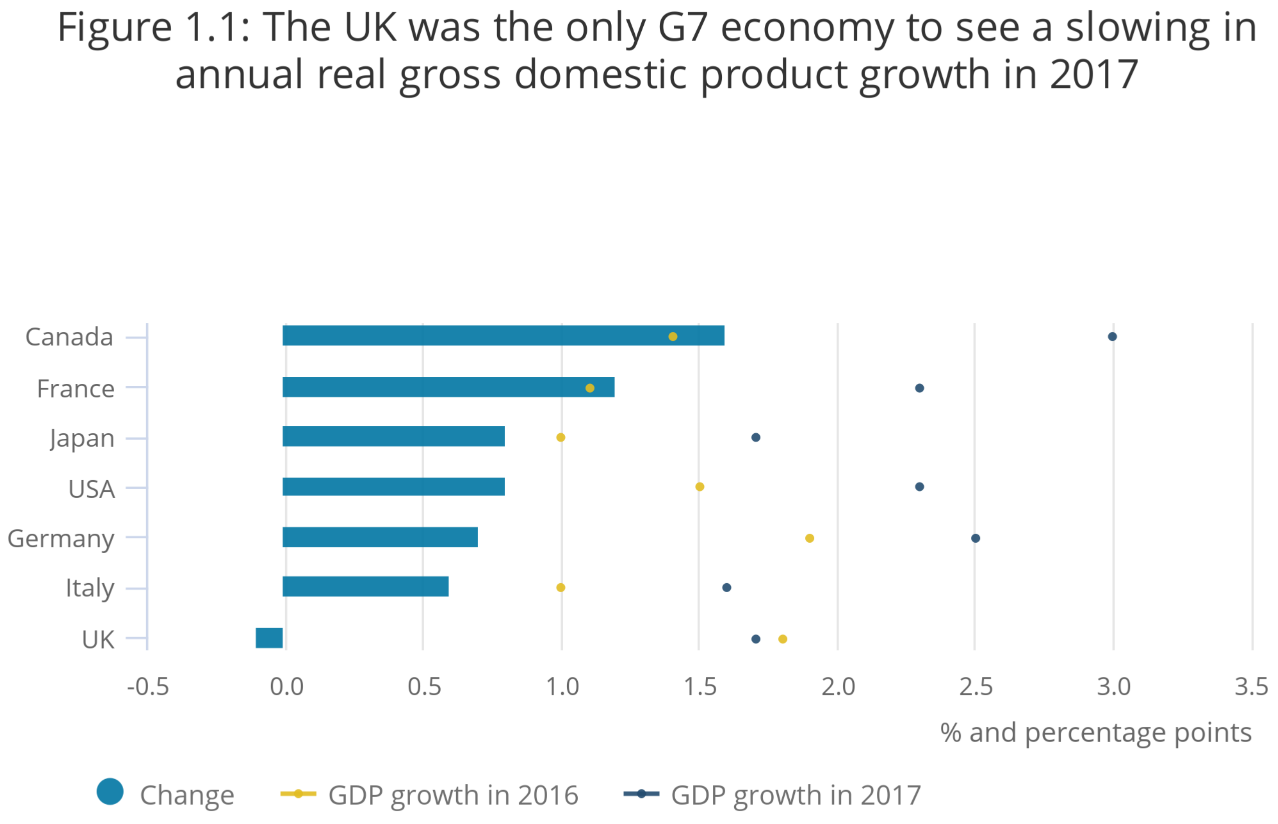
This section of the UK National Accounts, The Blue Book: 2018 edition provides an examination of recent trends and important movements for a range of information contained in a number of the subsequent Blue Book chapters. It will focus particularly on how the UK economy has evolved since the EU referendum in June 2016. All UK data referred to in this section are consistent with the Blue Book 2018.

2 . GDP and the headline economy

This section provides information on the headline economy, including the latest estimates of UK gross domestic product (GDP), which records how much output was produced in the UK in any given year. The UK economy grew by 1.7% in 2017 in volume terms, which followed growth of 1.8% in 2016. This marked the third consecutive year in which UK economic growth has slowed in annual terms.

The UK was the only G7 economy to see a slowing in 2017, with all other countries recording marked pickups (Figure 1.1). The latest IMF estimates show that global growth strengthened to 3.7% in 2017, which was the strongest pickup in activity since 2011 . Having experienced the second-fastest rate of growth in 2016, the UK was only the joint fifth-fastest growing economy in the G7 in 2017, ahead of Italy.

Figure 1.1: The UK was the only G7 economy to see a slowing in annual real gross domestic product growth in 2017

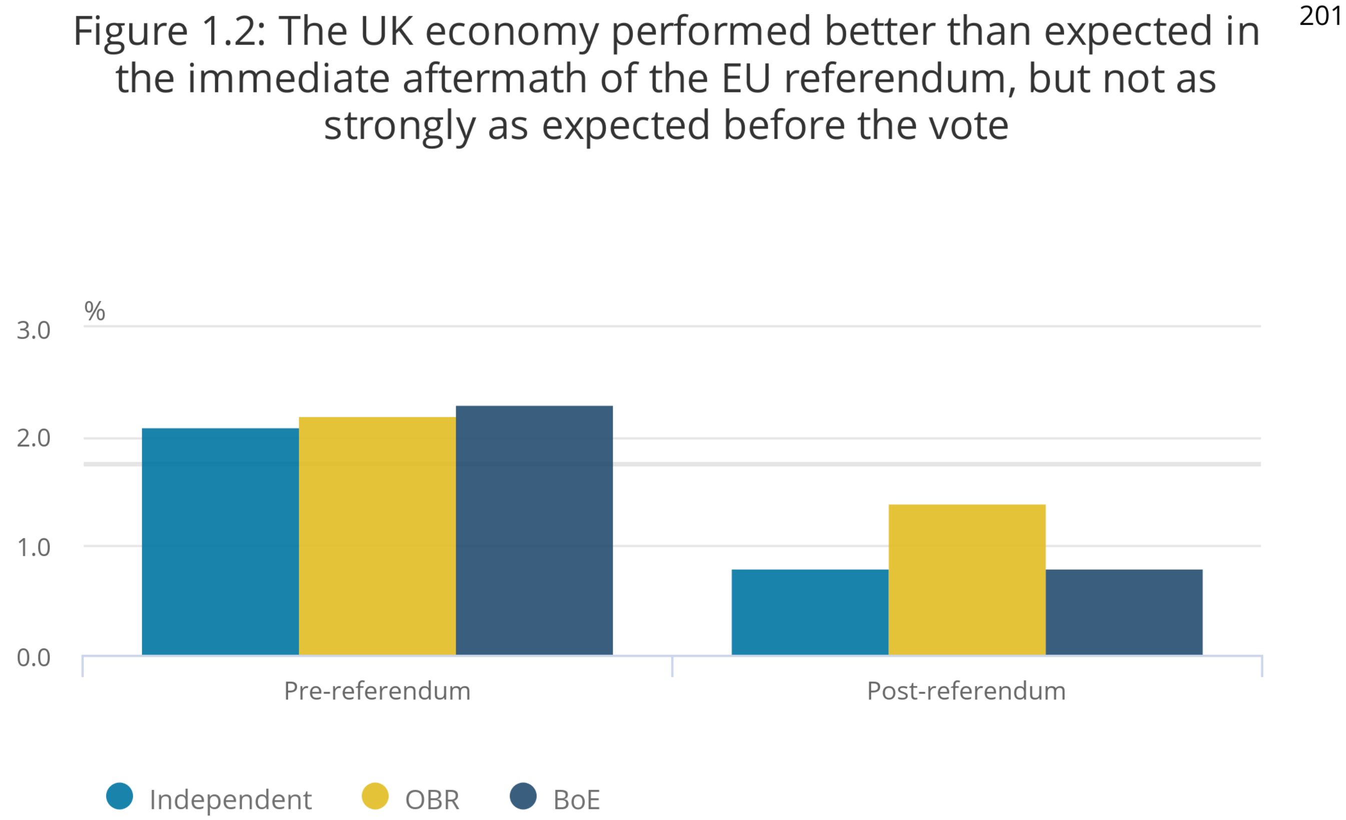


Source: Office for National Statistics and Organisation for Economic Co-operation and Development

However, UK growth has been more resilient than was initially expected immediately following the EU referendum in June 2016. Figure 1.2 compares the 2017 outturn with forecasts by the Bank of England (BoE), the Office for Budget Responsibility (OBR) and the consensus of independent forecasters, both before and after the vote.

Before the referendum, these forecasts had been conditional on the UK voting to remain in the EU. Figure 1.2 shows that these were subsequently revised down, based largely on the view that a weaker sterling would push up import prices, squeezing consumer budgets and spending, while heightened uncertainty would weigh on firms' decision to invest. While the UK economy did slow in 2017, the 1.7% growth recorded was not as weak as many had forecasted. In part, this was due to consumers initially spending more than had been predicted, with global GDP growth picking up since early 2016.

Figure 1.2: The UK economy performed better than expected in the immediate aftermath of the EU referendum, but not as strongly as expected before the vote



Source: Office for National Statistics, HM Treasury, Office for Budget Responsibility and Bank of England

Notes:

1. Pre-referendum forecasts refer to the last published figure before the EU referendum vote– June 2016 for independent forecasts, May 2016 for the BoE and March 2016 for the OBR.
2. Post-referendum forecasts refer to the first published figure following the EU referendum vote– July 2016 for independent forecasts, August 2016 for the BoE and November 2016 for the OBR.

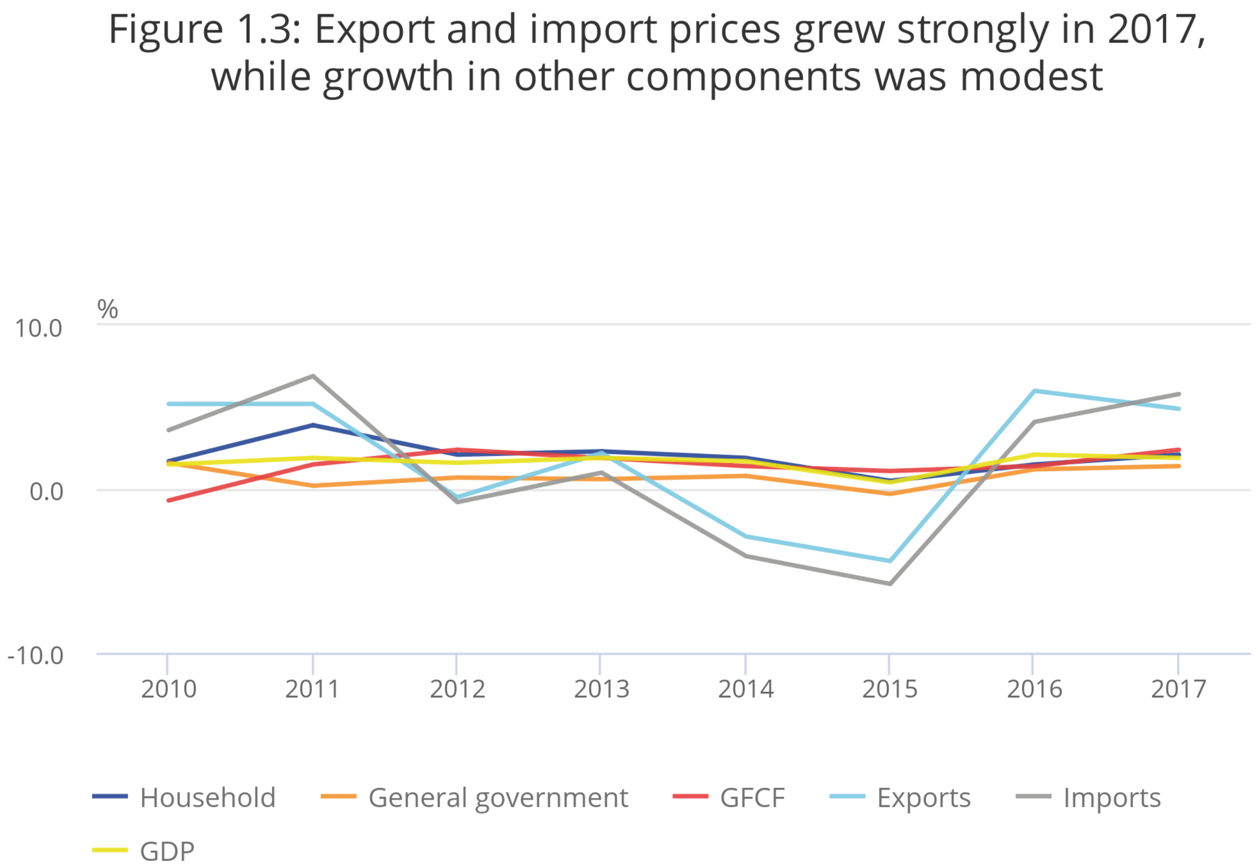
Meanwhile, growth in the implied GDP deflator – which measures changes in the price of all goods and services that comprise GDP – slowed to 1.9% in 2017. Despite this slowing, it was slightly stronger than its five-year average rate of 1.6%. Reflecting these price movements, nominal GDP growth in the UK economy was 3.6% in 2017, slightly below its five-year average annual growth rate of 3.8%.

The increase in the implied GDP deflator in 2017 reflected strengthening price growth across all expenditure components except for exports (Figure 1.3). Following a sharp rise of 6.1% in 2016, growth in UK nominal export prices eased to 4.9% in 2017. Meanwhile, nominal import price growth strengthened to 5.8% in 2017, the highest annual growth rate since 2011.

It is important to note that both export and import prices are based in sterling for the UK. While export prices have risen in sterling terms, it is possible there may have been no change in the price in foreign currency terms.

Movements in sterling export prices also reflect both exchange rate movements and changes in the price charged by the UK exporter, and there are a number of reasons why prices may be sticky in the short-term. Overseas firms that have agreed to pay a fixed price for UK exports may not be able to renegotiate the terms of those contracts in the short-term. Should prices be flexible, a domestic firm's choice to alter prices also depends on the price elasticity of demand of their products. For example, UK exporters may have the incentive to not pass through the full effect of an exchange rate appreciation to preserve market share and may not pass on the effects of a depreciation to increase profit margins.

Figure 1.3: Export and import prices grew strongly in 2017, while growth in other components was modest



Source: Office for National Statistics

Price growth across all other components of expenditure strengthened modestly in 2017. The household consumption deflator rose by 2.1%, following growth of 1.5% in 2016. The fall in the exchange rate following the EU referendum led to an increase in UK import prices, which was then passed through to consumer prices.

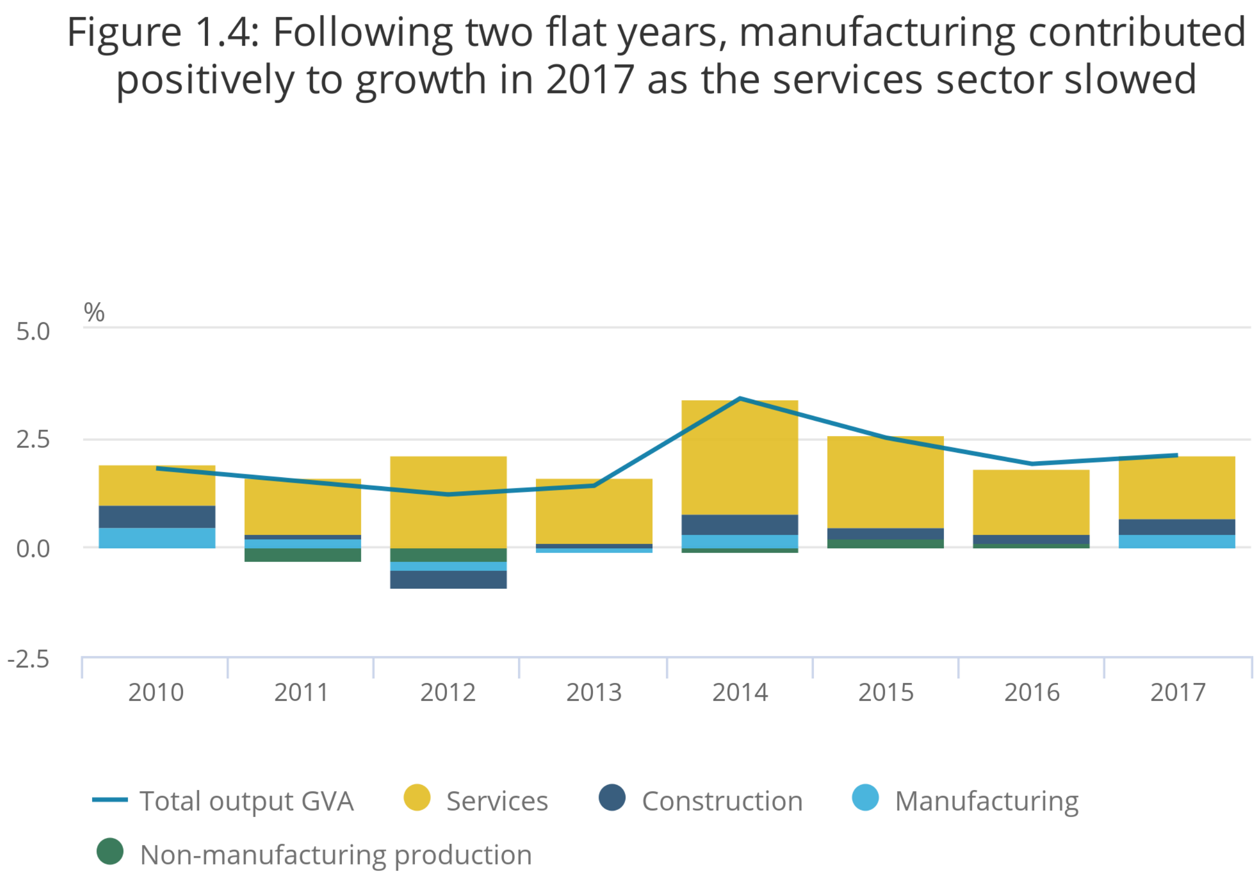
This was driven by particularly robust price growth in food and drink, and household goods and services. Food and drink prices rose by 2.4% in 2017 following a 2.3% fall in 2016, which was the sharpest annual uptick on record. Growth in the prices of household goods and services saw a similar record increase, rising by 4.0 percentage points in 2017 following two flat years. This is in line with the slowdown seen in household expenditure and output in consumer-focused service industries in 2017.

3 . How have different industries fared since the referendum?

While headline gross domestic product (GDP) slowed in 2017, the output approach to measuring GDP strengthened slightly from 1.9% to 2.1% (Figure 1.4). This increase was driven by manufacturing, which grew by 2.5% and contributed 0.3 percentage points, following two flat years.

Construction output increased by 7.1%, which contributed 0.4 percentage points. Meanwhile, services output increased by 1.8%, with its contribution falling slightly in 2017 to 1.4 percentage points. This was a continuation of a longer-term trend, with the services industry on a gradual deceleration since 2014.

Figure 1.4: Following two flat years, manufacturing contributed positively to growth in 2017 as the services sector slowed



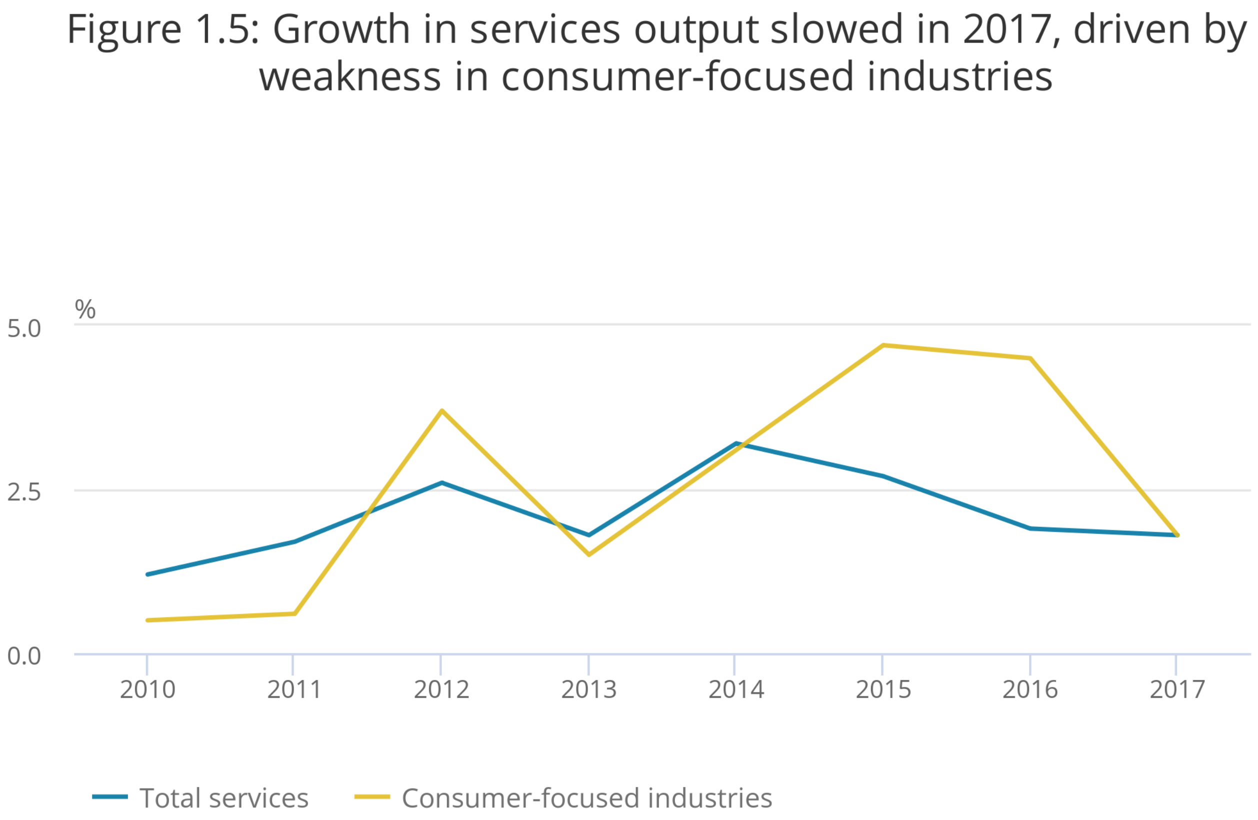
Source: Office for National Statistics

This slowdown in services can be attributed to weakness in consumer-focused industries, which saw a decline in their annual growth rate from 4.5% in 2016 to 1.8% in 2017 (Figure 1.5). In 2017, the distribution, hotels and restaurants sector – which includes retail trade and makes up a large proportion of consumer-focused industries – grew at its weakest annual rate since 2012 (2.1%).

This weakness in consumer spending reflects the squeeze on household purchasing power, with real incomes squeezed by rising inflation following the sterling depreciation that followed the outcome of the EU referendum. In the months following June 2016, the 12-month growth rate of the Consumer Prices Index including owner occupiers' housing costs (CPIH) increased sharply, from 0.8% in June 2016 to a peak of 2.8% in late 2017.

In other service sectors, business services and finance was the largest contributor to total services growth in 2017. This is in line with external evidence (PDF, 712KB), which indicates that professional services firms across law, accountancy and consultancy have experienced robust demand for advice related to the acquisition of UK assets and from EU clients on the establishment of UK operations to retain market access.

Figure 1.5: Growth in services output slowed in 2017, driven by weakness in consumer-focused industries



Source: Office for National Statistics

Notes:

1. "Consumer-focused" services defined here include retail trade (Standard Industrial Classification (SIC) 2007 codes 45 and 47), food and beverage (SIC code 56), publishing, audiovisual and broadcasting activities (SIC codes 58 to 60; including motion pictures), and arts, entertainment and recreation (SIC codes 90 to 93).

There is mixed evidence as to whether the result of the referendum has had a discernible impact on output in the construction industry. Construction output rose by 7.1% in 2017, following a rise of 4.1% in 2016. Although output subsequently fell by 0.8% in Quarter 1 (Jan to Mar) 2018 – the sharpest decline since Quarter 3 (July to Sept) 2012 – this fall was off a historically-high level in Quarter 4 (Oct to Dec) 2017 and output levels remain well above their pre-downturn peak in Quarter 1 2008.

Construction new orders have also remained broadly flat compared with pre-referendum levels. This is despite some survey evidence (PDF, 493KB) suggesting that Brexit-related uncertainty has impacted on firms' willingness to spend, weighing on new orders growth.

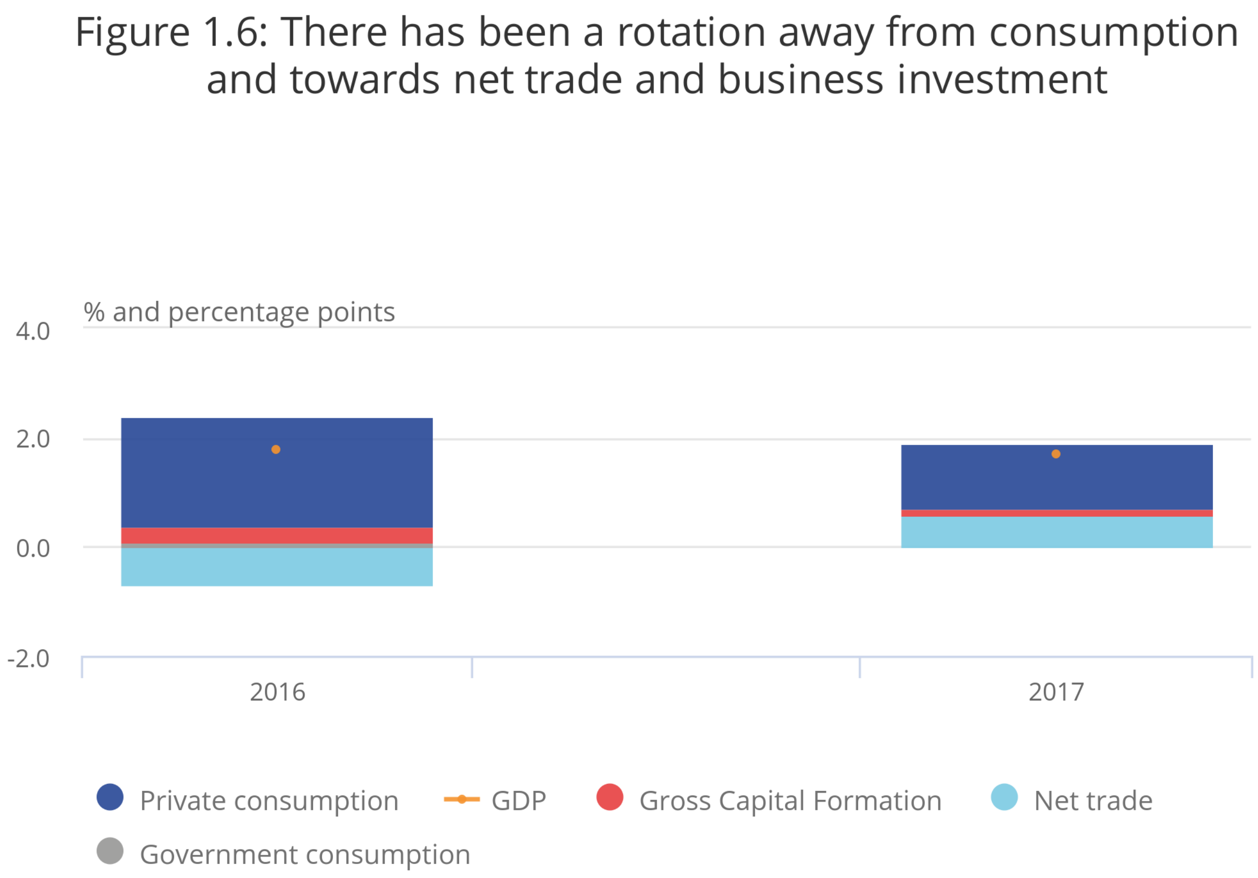
In the production industries, output rose by 1.8% in 2017 – its strongest annual growth rate since 2010. This was almost entirely driven by a 1.8 percentage point contribution from manufacturing, which expanded solidly to end 2017 on a run of seven consecutive months of growth. The Bank of England reports (PDF, 441KB) that manufacturers involved in export supply chains were benefitting from the fall in sterling and stronger global demand as the growth in their export volumes of manufacturing goods picked up.

In other sectors, growth in waste management in 2017 was offset by a decline in energy supply, while mining and quarrying made no growth contribution.

4 . How has spending in the UK economy changed since the referendum?

Looking at how the expenditure components of gross domestic product (GDP) have evolved since the referendum, there has been some evidence of a rotation in demand in response to the depreciation in sterling and pickup in global demand. Figure 1.6 shows a notable shift away from private consumption and towards net trade and business investment in 2017.

Figure 1.6: There has been a rotation away from consumption and towards net trade and business investment



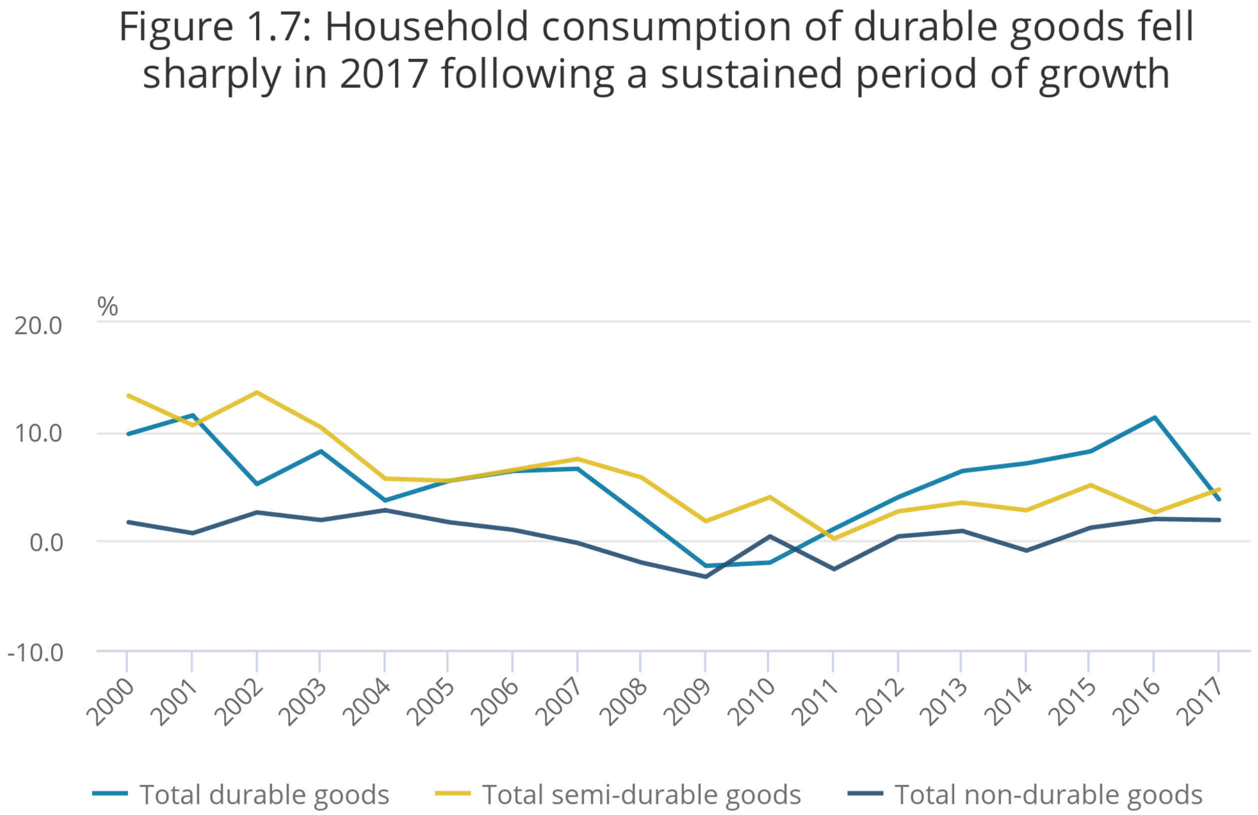
Source: Office for National Statistics

Growth in household consumption slowed to 1.9% in 2017, down from the 3.2% recorded in 2016. This is the weakest annual rate since 2012, consistent with the weakness seen in consumer-focused service industries. The slowdown in household spending has been driven by the erosion of household purchasing power and stagnating real wage growth following the depreciation of sterling. Real household disposable income fell by 0.5% in 2017, the weakest annual rate since 2011.

Spending on durable goods – those that can be used repeatedly or continuously over a period of more than a year – is generally thought to be more discretionary in nature, as consumers can more easily delay their purchase. It is therefore expected that expenditure on these items might slow during periods of lower real income growth or heightened economic uncertainty.

Figure 1.7 shows a striking decline in the growth of durable goods consumption, which increased by only 3.8% in 2017, following seven years of strengthening growth. This is the weakest annual rate since 2011 and was driven primarily by reduced purchases of motor vehicles, which fell by 5.0% in 2017 – the first annual decline since 2011. Meanwhile, growth in the consumption of non-durables – which comprises around half of total goods consumption and grows at relatively lower rates – remained broadly stable in 2017.

Figure 1.7: Household consumption of durable goods fell sharply in 2017 following a sustained period of growth



Source: Office for National Statistics

Figure 1.8 shows that the main drivers of the consumption slowdown in 2017 were net tourism, transport, and recreation and culture.

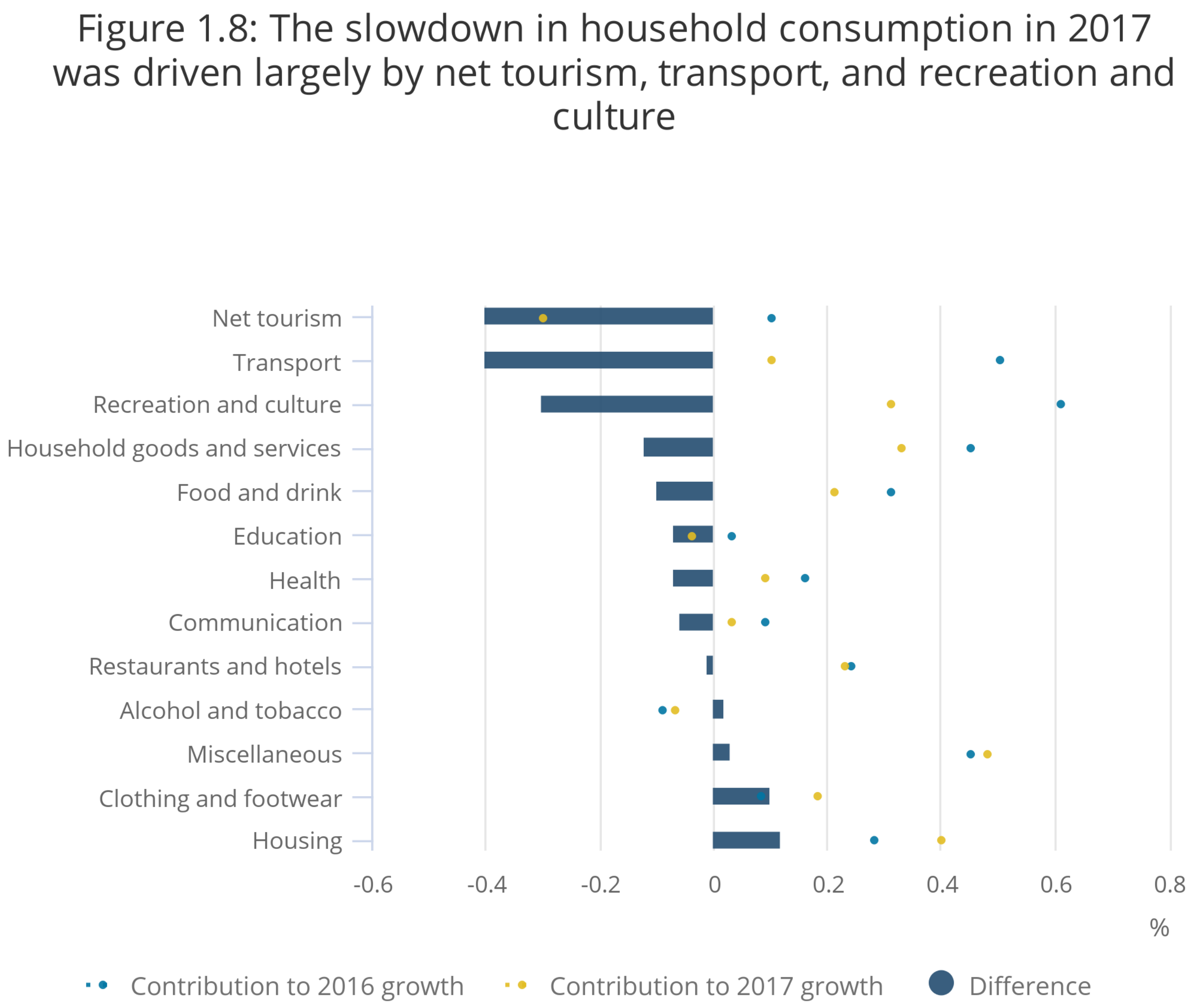
Net tourism[1] was the largest negative contributor to household consumption growth in 2017. Exchange rate movements are expected to have a relatively quick pass-through to the tourism industries, with such movements having more of an immediate impact on the purchasing power of UK travellers abroad, which is likely to have reduced expenditure.

Travel services are also less likely to be constrained by long-term contracts and be relatively price elastic due to their discretionary nature and, while imperfect, the availability of domestic substitutes (travel within the UK).

While recreation and culture was the largest growth contributor to household consumption in 2016, growth in this category more than halved in 2017, from 6.6% to 3.2%. This sharp slowdown was driven primarily by cultural services (such as theatre and museum visits), recreational and sporting services, and newspapers.

Clothing and footwear (which makes up almost half of semi-durable goods), and restaurants and hotels have also both seen a notable slowdown since the second half of 2017. Together, these consumption patterns corroborate the slowdown seen in consumer-focused service industries.

Figure 1.8: The slowdown in household consumption in 2017 was driven largely by net tourism, transport, and recreation and culture



Source: Office for National Statistics

Business investment grew by 1.6% in 2017 following a 0.2% decline in 2016. This pickup may in part reflect the strengthening global economy, with both exporters investing to meet stronger overseas demand and domestic facing firms benefitting from import substitution expanding capacity. Investment by manufacturing firms picked up in 2017, consistent with the strength seen in manufacturing exports.

Business investment growth in 2017 was also supported by stronger investment in construction and other production (predominantly in mining and quarrying), while services investment slowed.

Despite the pickup in 2017, growth in business investment remained relatively muted, particularly in the context of stronger global activity and supportive financial conditions. Investment levels remain subdued compared with recent years. Survey evidence (PDF, 493KB) suggests that this is likely to reflect the impact of Brexit, with the associated political and economic uncertainty weighing on firms' decision to invest. Estimates from the Bank of England's Decision Maker Panel (DMP) Survey (PDF, 99KB) suggests that Brexit-related uncertainty lowered nominal investment by around 3 to 4 percentage points in the year to the first half of 2017.

Notes for: How has spending in the UK economy changed since the referendum?

1. Net tourism is included in UK National household final consumption expenditure, which measures final consumption expenditure by UK households in the UK and abroad. It is not included in UK Domestic household final consumption expenditure, which measures expenditure in the UK by UK and foreign households.

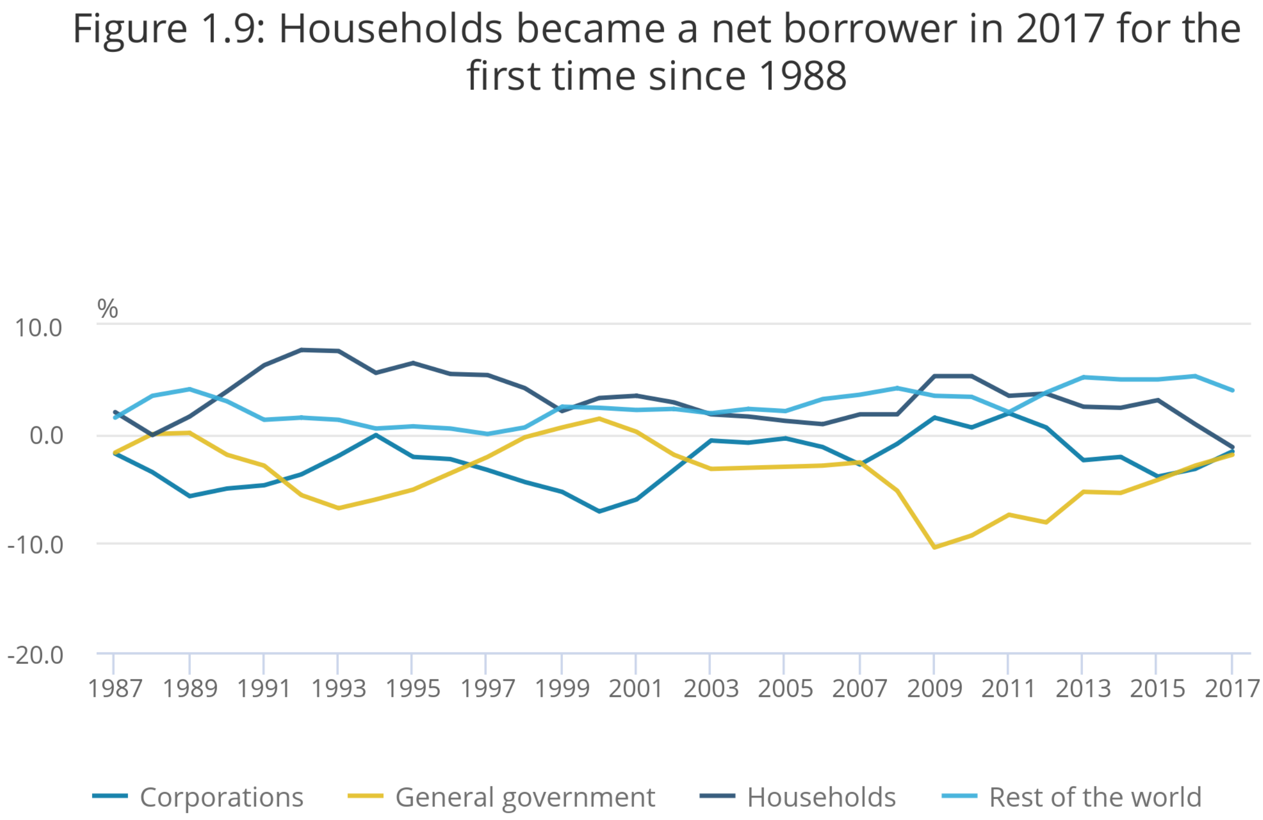
5 . Sector and financial accounts

The Blue Book also allows for an examination of activity by institutional sector. This includes the net lending or borrowing position of each domestic sector in the UK and the rest of the world. Net lending (borrowing) occurs when savings (investment) exceeds investment (savings). The net positions of each of these sectors must sum to zero, as there must be a pound lent for each pound that is borrowed.

Each of the domestic sectors in the UK – households (including non-profit institutions serving households (NPISH)), corporations and government – were net borrowers in 2017 (Figure 1.9). This is the first time on record that this has happened, with the UK reliant on external borrowing to help finance these net borrowing positions, running a current account deficit of 3.9% in 2017.

In recent years, the current account deficit has widened to historical highs, but there was a marked narrowing in 2017. This is likely to have reflected the effects of the recent sterling depreciation on competitiveness as well as the pickup in the global economy. These factors may also explain the improvement in the net rate of return on foreign investments by the UK.

Figure 1.9: Households became a net borrower in 2017 for the first time since 1988



Source: Office for National Statistics

Most strikingly, households (excluding NPISH) were a net borrower in 2017 for the first time since 1988 – borrowing 1.2% of GDP to finance its spending and investment. Households financed this borrowing by acquiring more liabilities, although at a slower rate than in recent years.

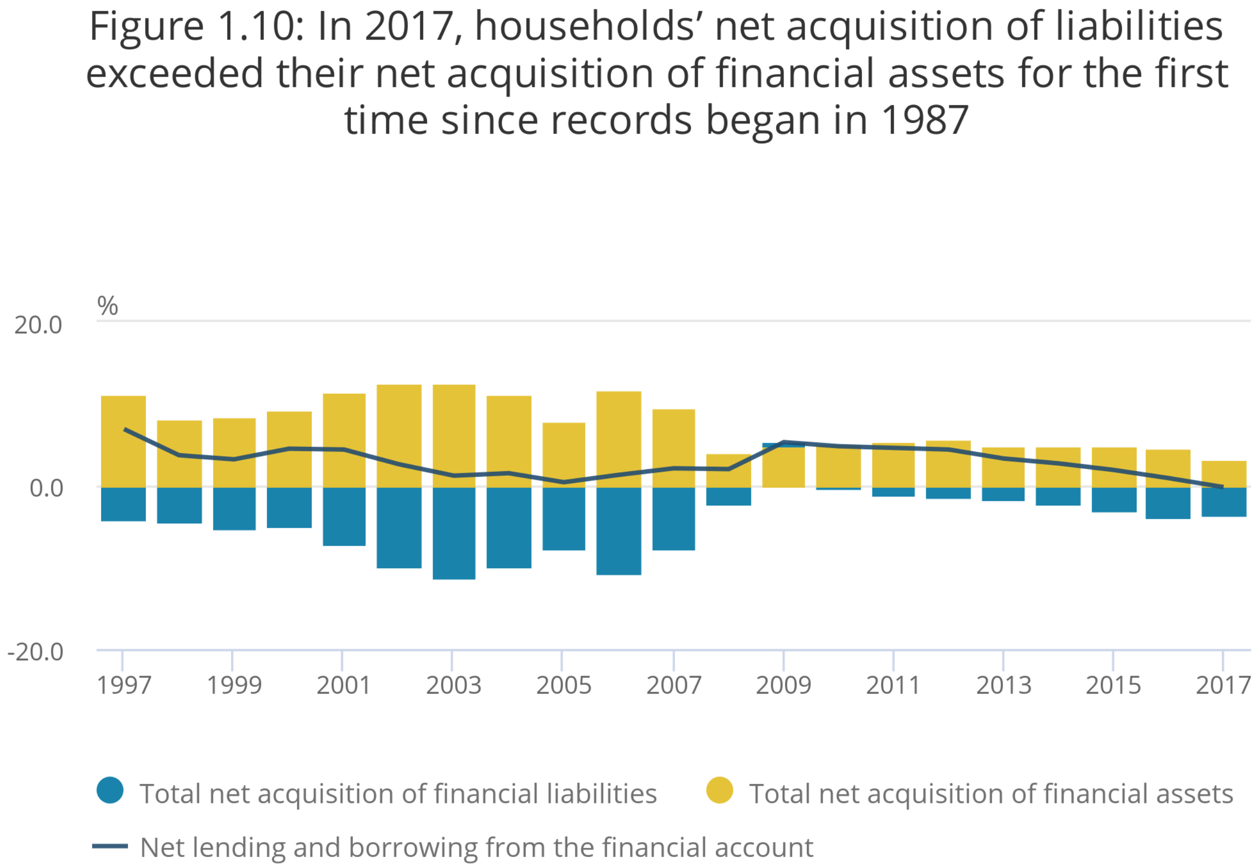
Household net acquisition of liabilities fell as a share of gross domestic product (GDP) in 2017, for the first time since 2009. As Figure 1.10 shows, households markedly reduced their net acquisition of financial liabilities in 2008 and 2009, corresponding with the impacts of the downturn on the cost and availability of credit. In particular, acquisitions of long-term loans secured on dwellings fell sharply as households undertook a process of deleveraging. Since then, households have been increasingly taking on more liabilities, although net financial liabilities had not yet exceeded net financial assets until 2017.

Acquisitions of long-term loans secured on dwellings continued to account for most of the increase in liabilities in 2017, although growth in these types of loans slowed considerably from the previous year. Household net acquisition of short-term loans fell by £3.5 billion to £8.9 billion in 2017, the first annual fall since 2012.

Households also continued to acquire more financial assets in 2017, although at its slowest rate since 2008 – household net acquisition of financial assets fell to 3.4% of GDP in 2017. Driving this slowdown was a large decrease in deposits with UK monetary financial institutions, which was partly offset by a reduced disposal of equity and investment fund shares.

Meanwhile, the government budget deficit continued to narrow in line with government policy and was 1.9% of GDP in 2017 – the lowest since 2002. Similarly, corporations remained a net borrower with their net borrowing position narrowing to 1.6% of GDP in 2017.

Figure 1.10: In 2017, households' net acquisition of liabilities exceeded their net acquisition of financial assets for the first time since records began in 1987



Source: Office for National Statistics

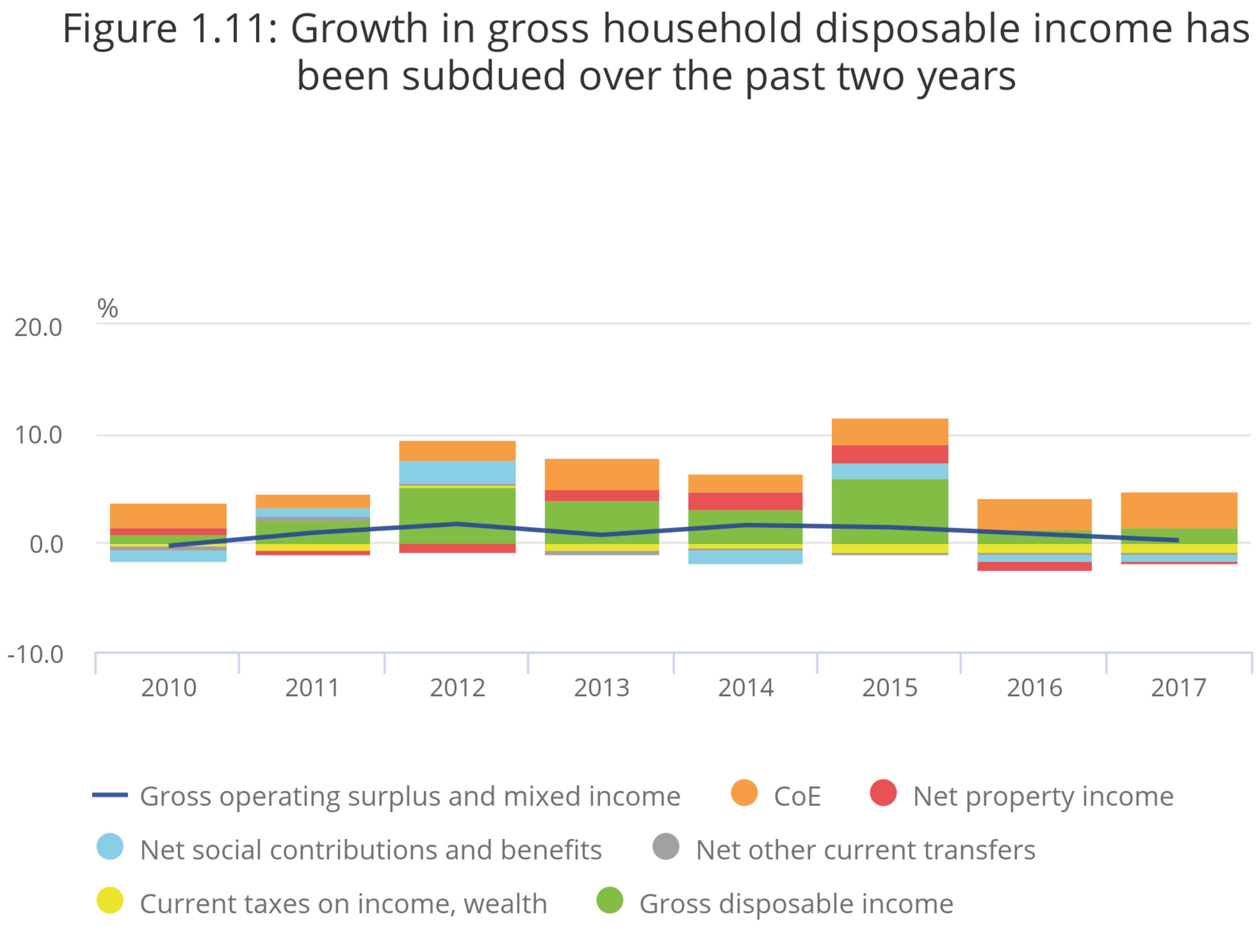
The household net borrowing position in 2017 largely reflects relatively subdued growth in household disposable income in both 2016 and 2017. As Figure 1.11 shows, there has been a marked slowdown in the growth of gross household disposable income (GHDI) compared with the preceding period. GHDI rose by 1.3% and 1.6% in 2016 and 2017 respectively, considerably weaker than the 10-year average annual growth rate of 3.0%. This slowdown was driven primarily by falls in net property income (earnings from interest on savings and dividends from shares) and net social contributions and benefits (Figure 1.11).

The slightly stronger growth in GHDI in 2017 was almost entirely driven by a 4.1% rise in compensation of employees (CoE), with employers' social contributions growing at their fastest rate since 2010 (9.9%) and wages and salaries also growing by a solid 2.9%. However, the contribution of wages and salaries to GHDI growth has fallen over the past two years, while the contribution of employers' social contributions has increased.

Looking at the impact of inflation, prices grew at a faster pace than gross disposable income in 2017 with the result that real household disposable income (RHDI) fell by 0.5% in 2017 – the second consecutive annual fall. The household consumption deflator increased by 2.1% in 2017, following the effects of the fall in the exchange rate. This inflationary squeeze on household spending power was the driver of slowing consumption growth in 2017.

The subdued growth in household income over the last two years is also reflected in historically-low levels of household savings, with the households' saving ratio hitting a record low of 4.1% in 2017. This reflects a reduction of gross savings by households, as growth in spending, although slowing, continued to outstrip growth in disposable income. As previous analysis showed, household spending slowed in 2017 but not as sharply as expected before the EU referendum.

Figure 1.11: Growth in gross household disposable income has been subdued over the past two years



Source: Office for National Statistics

Figure 1.12 shows the net worth of households as a share of nominal GDP, decomposed into financial and non-financial assets as well as financial liabilities. The value of total assets continued to increase in 2017, albeit at a slower pace, rising to £12.3 trillion (or 604.4% of GDP).

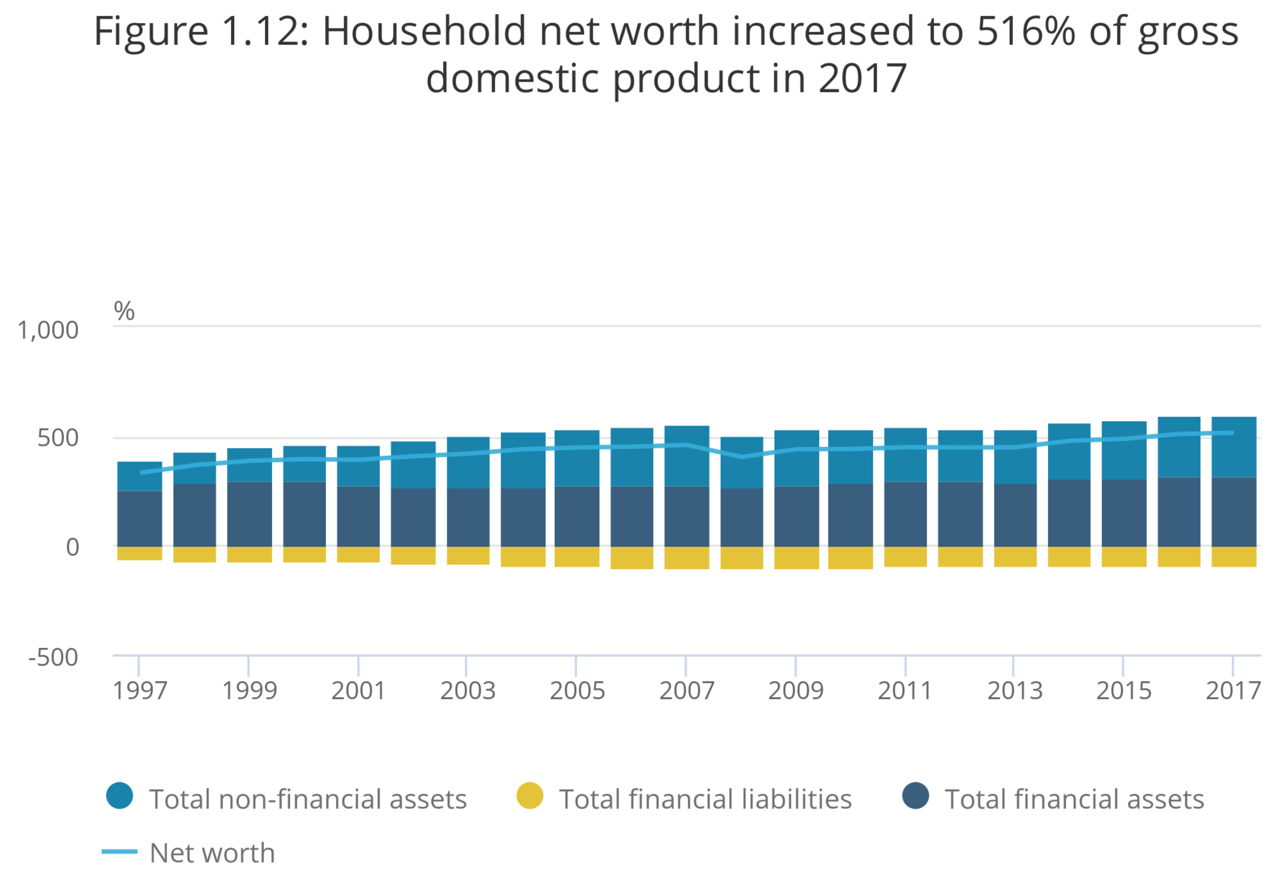
Within these assets, the value remained relatively evenly split between financial and non-financial assets – as it has been over the past 10 years. However, growth in the value of financial assets slowed in 2017, driven by insurance and pension entitlements, which increased by a modest 1.4% following a sharp 11.1% rise in the previous year (which was due largely to revaluations). Consistent with the reduction in household savings, growth in currency and deposits also slowed to its weakest annual rate since 2011.

On the non-financial asset side, growth continues to be driven by increases in the value of land, which contributed 5.6 percentage points to the 6.6% growth in the total value of household non-financial assets in 2017. Land held by households now accounts for over 40% of the UK's total net worth.

Meanwhile, the value of household financial liabilities increased to £1.8 trillion in 2017, but remained broadly stable as a share of GDP. Household liabilities as a percentage of GDP has been on a steady decline since 2009, falling from 100.4% of GDP to 88.4% in 2017. This decline has been largely driven by a considerable slowdown in long-term loans secured on dwellings – the value of these types of loans averaged double-digit growth in the years leading up to the financial crisis, but has averaged only 1.6% since 2010.

With the rise in the value of total household assets more than offsetting the rise in the value of liabilities, household net worth as a share of GDP increased to 516.1% of GDP in 2017. While all domestic sectors except non-financial corporations saw an increase in net worth in 2017, it was the households sector that continued to be the driver of growth in total UK net worth, contributing 4.9 percentage points to the 5.1% growth in total net worth. Total net worth in the UK rose by £492.4 billion to 502.0% of GDP in 2017.

Figure 1.12: Household net worth increased to 516% of gross domestic product in 2017



Source: Office for National Statistics