

The NewsLine

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UNITED KINGDOM

It's downhill from here for the UK economy

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The preliminary Q4 growth estimate seems to underline the British economy's resilience 18 months after the Brexit vote. However in our view it's downhill from here for the UK economy with the slow-burning growth deceleration that is already underway set to become more pronounced in 2018.

In the three months to December GDP growth came in at +0.5% q/q – slightly above consensus and the rate observed in the previous quarter (+0.4% q/q). In contrast to positive growth contributions from the service and production sectors, the construction sector contracted for the third consecutive quarter. No breakdown of components is available yet, but higher frequency data suggests that private consumption – albeit weakened – was the main engine of growth in the fourth quarter. For 2017 as a whole, UK GDP growth now stands at +1.8%. While only a slight dip compared to the +1.9 per cent expansion seen in 2016, this is the lowest growth rate for the British economy since 2012 when the continent found itself in the grip of the Eurozone debt crisis.

Today's growth data is a moment of 'as good as it gets' and we expect the strength of the UK economy to wane over the course of 2018. While the Brexit vote did not trigger the much feared doom and gloom scenario, the UK economy is already experiencing a clear – albeit slow-burning – slowdown which has been masked to some extent by the favourable global economic backdrop.

Relatively weak domestic demand will be key driver of the slowdown. Brexit uncertainty looks set to have a dampening impact on investment in particular while the consumer squeeze will continue in 2018 in the context of inflation outpacing wage growth and weakening house prices. British exports are currently profiting from the favourable global growth outlook but hopes of a

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pronounced and lasting export boom following the sharp depreciation of Sterling are in our view misplaced. After all exporters have increased prices to protect margins in light of the high import content of their goods. In any case the modest growth contribution from the external sector will not prove strong enough to offset the expected slowdown in domestic demand.

Over the past 18 months, the UK economy has been increasingly struggling to keep up with its European peers and we expect it to remain an economic laggard this year: While the Eurozone economy looks set to expand by a further +2.2% in 2018 after +2.5% last year, we expect UK GDP growth to reach just +1.4 per cent this year – one of the lowest growth rates across the EU.

The cooling economic backdrop is unlikely to make a crucial year for Brexit negotiation any easier for Prime Minister Theresa May who will have to seal a divorce agreement as well as a deal on the principles underpinning future EU-UK relations by the end of the year.

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