THE WEEKLY **U.K.** ECONOMIC MONITOR

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SAMUEL TOMBS, CHIEF U.K. ECONOMIST

Steady growth in real spending in Q4 and January's jump in retail sales show consumers aren't panicking.

Wage growth should remain solid in 2019, supported by labour shortages and another hefty rise in the NLW.

Pension contributions will jump again in April, but the rise in the personal allowance will cushion the blow.

Steady Growth in Consumers' Spending will Keep GDP Edging Up

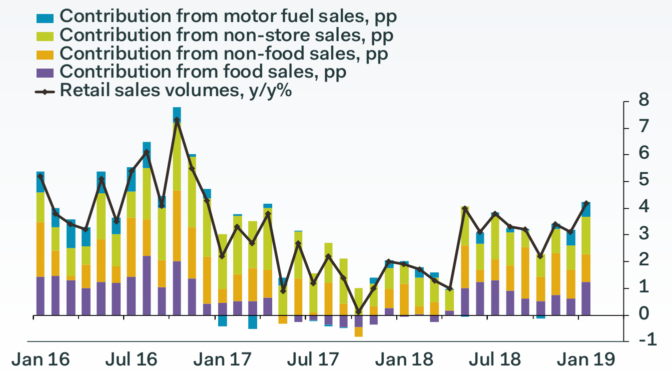
We became more confident last week in our call that GDP growth will hold up better than widely feared in the first half of 2019, following signs that consumers have maintained their happy-go-lucky mentality, despite the ongoing political crisis. Quarter-on-quarter growth in households' total real spending held steady at 0.4% in Q4, while January's retail sales volumes jumped by 1.0% month-to-month, exactly matching our above-consensus forecast.

Admittedly, consumers' confidence undeniably has been shaken by the Brexit impasse in parliament, and it usually leads households' spending by around three months. What's more, January's jump in retail sales volumes was driven by a 1.2% month-to-month rise in food store sales and a 2.1% surge in clothing sales, which reportedly were both driven by discounting. Recent rises in domestic producer and import prices suggest that food retailers will need to hike prices again over the coming months.

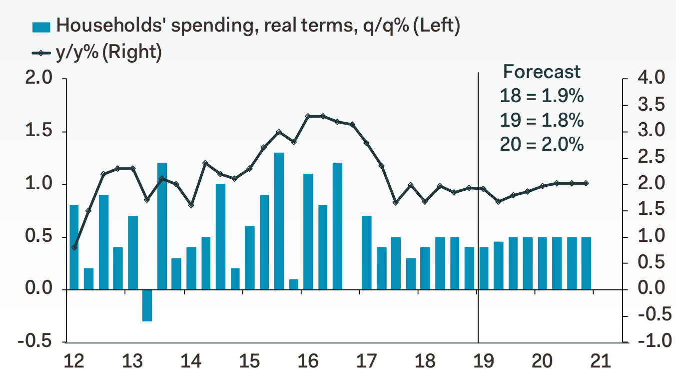
Nonetheless, consumers' confidence tends to give a misleadingly downbeat steer when, like now, it is depressed by political uncertainty; see here for our analysis. Consumers likely will hold back from buying cars, booking holidays and moving home, but will continue to increase their spending on low-value items sold on the high street.

The fundamentals continue to look solid for consumers. Out third chart shows that the pick-up in growth in retail sales volumes has been underpinned by the upturn in real wages. Granted, CPI inflation

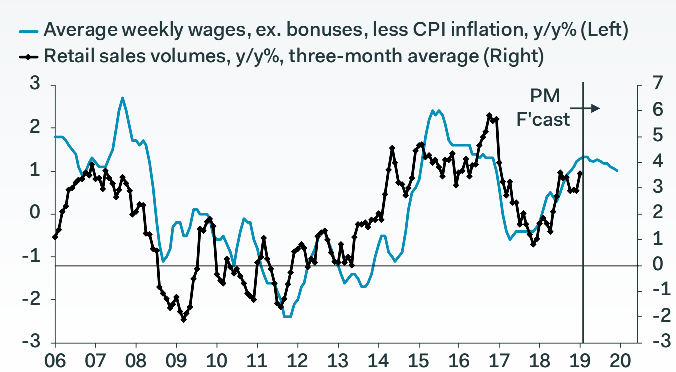
JANUARY RETAIL SALES DATA BEAT CONSENSUS EXPECTATIONS...



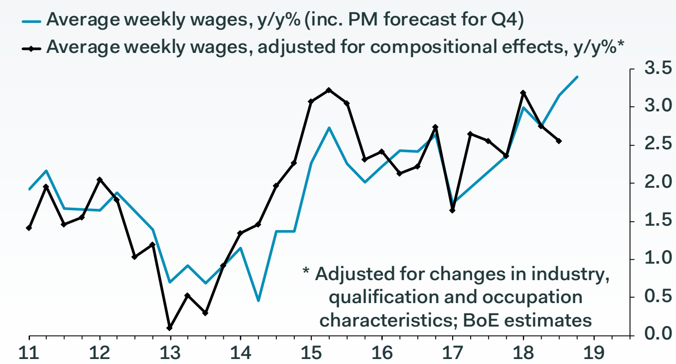
NO SIGN OF BREXIT RISKS HITTING CONSUMERS' OVERALL SPENDING



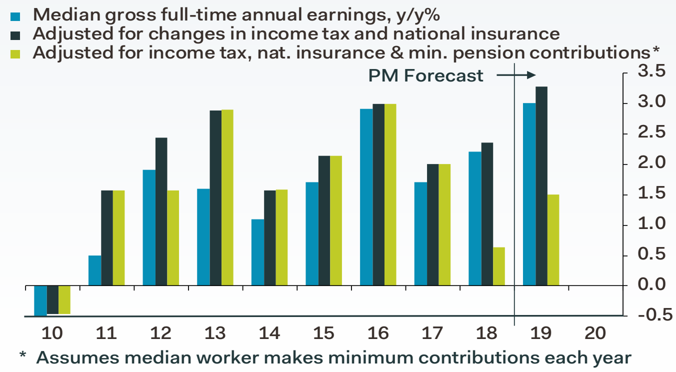
...AND ARE SUPPORTED BY SOLID INCREASES IN REAL WAGES



THE COMPOSITIONAL BOOST TO WAGE GROWTH WILL FADE SOON



TAKE-HOME PAY GROWTH WILL PICK-UP FOR MOST PEOPLE THIS YEAR



likely won't fall further from January's 1.9% rate this year. And wage growth probably is close to its peak, for now. We expect December's labour market data, released on Tuesday, to show that the headline, three-month average, rate of year-over-year growth in AWE excluding bonuses rose to 3.5%, from 3.4% in November. But our chart above shows that 0.5pp of the recent acceleration has reflected compositional changes in the workforce, which likely won't remain so supportive. In addition, pay settlements might weaken a little this year, because many are based off RPI or CPI inflation in the previous year.

Nonetheless, the labour market now is very tight and job-to-job flows have trended up over the last two years. In addition, the main rate of the National Living Wage will rise to £8.21 per hour in April, from £7.83. This 4.9% increase is bigger than last year's 4.4% rise. What's more, 10% of workers currently earn between £7.80 and £8.20, exceeding the 8% whose pay was directly impacted by the previous year's increase. ***Accordingly, we expect average weekly wages to rise by a still-solid 3.0% this year, generating a 1.0% increase in real wages.***

Growth in households' take-home pay, meanwhile, will be supported by the £650 increase in the income tax personal allowance to £12.5K in April, the biggest increase since 2013. *The increase in the threshold means that a 3.0% rise in pre-tax pay for the median worker will equate to a 3.2% gain in post-tax pay, the biggest this decade.*

Admittedly, the minimum proportion of "qualifying earnings" that employees must make to their workplace pensions in order to maintain employer contributions will jump to 5%, from 3% at present. For the median full-time worker who currently only makes minimum contributions, annual pension contributions will jump to £930, from £539. Take-home pay for these individuals will rise by only 1.5% this year, *below* the CPI rate of inflation.

Nonetheless, we estimate that only around half of all workers will have to increase their pensions contributions in April. A third of workers don't have a workplace pension, and 15% of those that do already made contributions above the new 5% minimum in 2017; this proportion likely has risen since then. *Even for those paying minimum contributions, growth in take-home pay will be stronger than last year, thanks to the jump in the personal allowance.*

Accordingly, we expect year-over-year growth in households' real disposable incomes to pick-up to 2.0% this year, from 1.3% in 2018. Provided precautionary saving does not suddenly rise—it didn't in Q4, when nominal spending and employees' compensation grew at the same rate—consumption should grow broadly in line with incomes. ***So, with households' spending accounting for 63% of GDP and business investment just 9%, the downturn in capex would have to be enormous to drive the overall economy into a recession this year.*** We expect quarter-on-quarter GDP growth to hold steady at 0.2% in Q1 and then to pick up to 0.4% in Q2.

Samuel Tombs **+44 (0)203 744 7430**
samuel@pantheonmacro.com

THIS WEEK IN BRIEF

Note: "**D**" prefix denotes Datanotes for these releases.

Monday, February 18

- **No significant data released.**

Tuesday, February 19

- **D: Labour market data (12)/09:30 GMT**

The headline, three-month average, unemployment rate likely held steady at **4.0%** in December. Admittedly, upside risks seem strong; November's unrounded rate was 4.046%, and employment surveys have deteriorated. But the departure of a cohort from December's sample that consistently has reported a high unemployment rate in previous months should push down the headline rate by a hefty 0.05pp. Meanwhile, we expect the headline rate of year-over-year growth in average weekly wages, excluding bonuses, to increase to **3.4%** in December, from 3.3% in November. But a further acceleration in 2019 doesn't look likely, given that many pay settlements are linked to a lagging rate of RPI inflation and compositional changes in the workforce explain some of the recent pick-up in wage growth. **Consensus: Unemployment 4.0%, wages 3.4%.**

Wednesday, February 20

- **D: CBI Industrial Trends Survey (2)/11:00 GMT**

We expect the total orders balance to drop to **-5** in January, from -1 in December, bringing it in line with the Markit/CIPS manufacturing PMI, which has indicated that output is flatlining. **Consensus: -5**.

Thursday, February 21

- **D: Public Finances (1)/09:30 GMT**

We expect a surplus on the PSNB ex. borrowing measure of **£11.5B** in January, better than last year's £9.3B. Past movements in the RPI suggest accrued interest payments will be about £0.7B lower than in January 2018. In addition, nearly all self-assessment and capital gains tax receipts are collected in January. Both will refer to income and capital gains generated in the 2017/18 fiscal year, when asset prices picked up. **Consensus: £10.0B**.

- **D: MPC member Haldane speech published/12:00 GMT**

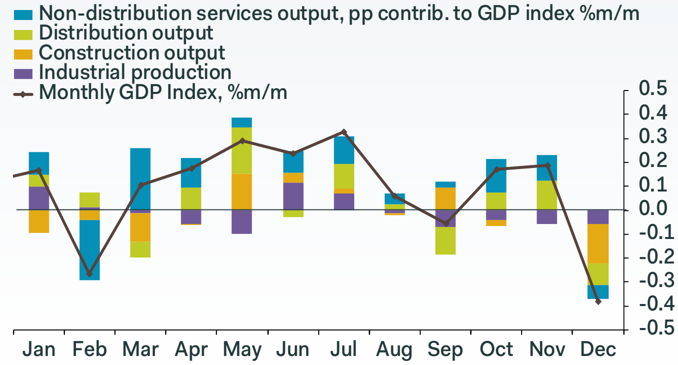
A transcript of a speech on innovation delivered on November 22 will be published. We do not expect any news on the outlook for monetary policy.

Friday, February 22

- **D: CBI Distributive Trades Survey (2)/11:00 GMT**

We expect the reported sales balance to rise to about **+10** in February—close to last year's average level—from zero in January. Although Brexit uncertainty has hit consumers' confidence, improving growth in real incomes should keep retail sales on an upward trend. **Consensus: +5**.

CHART OF THE WEEK: DECEMBER GDP DIP DRIVEN BY NOISY SECTORS



PANTHEON'S FINANCIAL FORECASTS

		End-month:				
	5pm Fri.	Mar	Jun	Sep	Dec	Dec 20
Bank Rate	0.75	0.75	0.75	1.00	1.00	1.50
3m Libor	0.87	0.90	1.00	1.10	1.20	1.70
12m Libor	1.13	1.20	1.30	1.40	1.60	2.00
2-year Gilt	0.74	0.90	1.20	1.40	1.60	2.00
10-year Gilt	1.16	1.40	1.60	1.80	2.00	2.40
30-year Gilt	1.68	1.80	2.00	2.20	2.30	2.50
FTSE 100	7237	7000	7200	7400	7600	8000
USD/GBP	1.29	1.35	1.36	1.38	1.40	1.40
EUR/GBP	1.14	1.23	1.24	1.25	1.27	1.27
Sterling TWI	77.2	83.7	84.3	85.6	86.8	86.8

PANTHEON'S ECONOMIC FORECASTS

	Period average:						
	Q1 19	Q2 19	Q3 19	Q4 19	2018	2019	2020
GDP, q/q%	0.2	0.4	0.5	0.6	-	-	-
GDP, y/y%	1.5	1.4	1.3	1.8	1.4	1.5	2.0
Employment, y/y%	0.8	0.9	1.0	0.9	1.1	0.9	0.9
Unemp. rate, %	4.1	4.0	4.0	4.0	4.1	3.9	3.6
Wkly earnings, y/y%	3.4	3.2	2.9	2.6	2.9	3.0	3.2
CPI, y/y%	1.9	2.2	1.8	1.9	2.5	1.9	2.1
RPI, y/y%	2.7	3.0	2.7	2.7	3.4	2.8	3.1
PSNB FY, £B	-	-	-	-	27	32	38
Cur. acc't., % GDP	-4.5	-4.6	-4.8	-4.9	-4.1	-4.7	-5.0
House prices, y/y%	1.9	1.7	1.3	1.2	3.3	1.5	2.5