



**PANTHEON**<sup>™</sup>  
MACROECONOMICS

INDEPENDENT • INCISIVE • ILLUMINATING

---

# **OUTPERFORMANCE ENDING AS FISCAL DRAG BUILDS** ...BUT FIRING LABOUR COSTS WILL REQUIRE MPC TO ACT

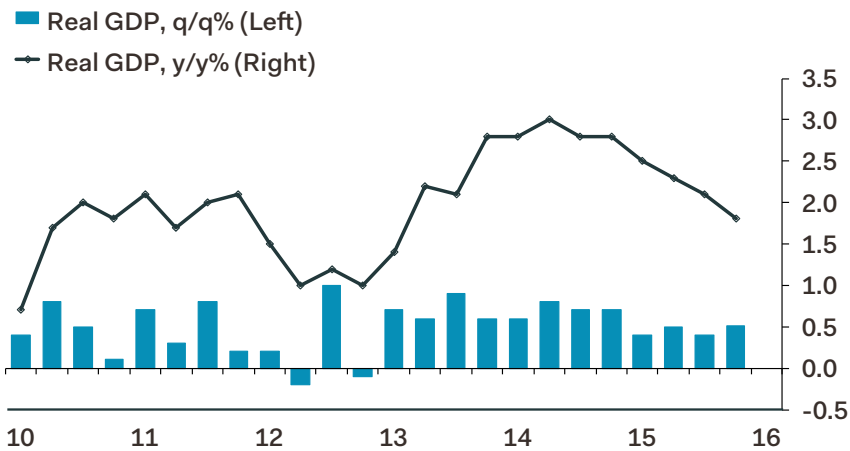
## **U.K. ECONOMIC CHARTBOOK, FEBRUARY 2016**

DATA AS AT FEBRUARY 18TH | SAMUEL TOMBS, CHIEF U.K. ECONOMIST  
[WWW.PANTHEONMACRO.COM](http://WWW.PANTHEONMACRO.COM) | +44 203 744 7430

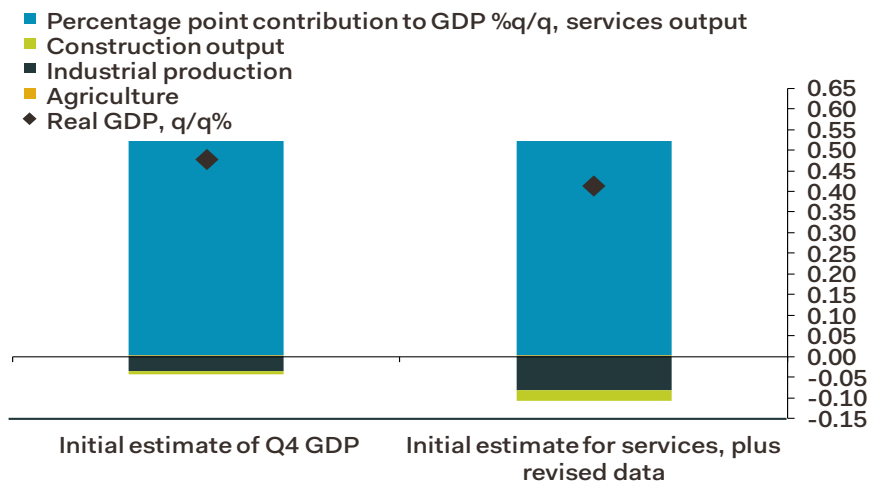




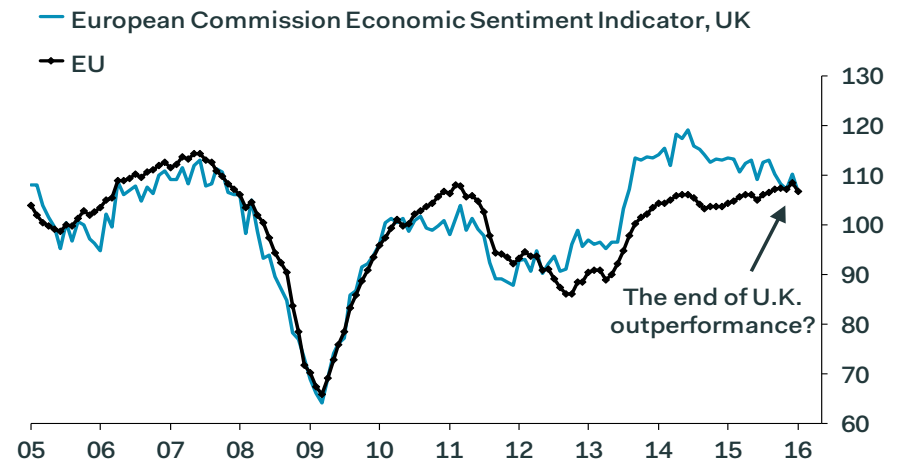
**1. THE U.K. RECOVERY HAS BEEN LOSING MOMENTUM SINCE EARLY 2015**



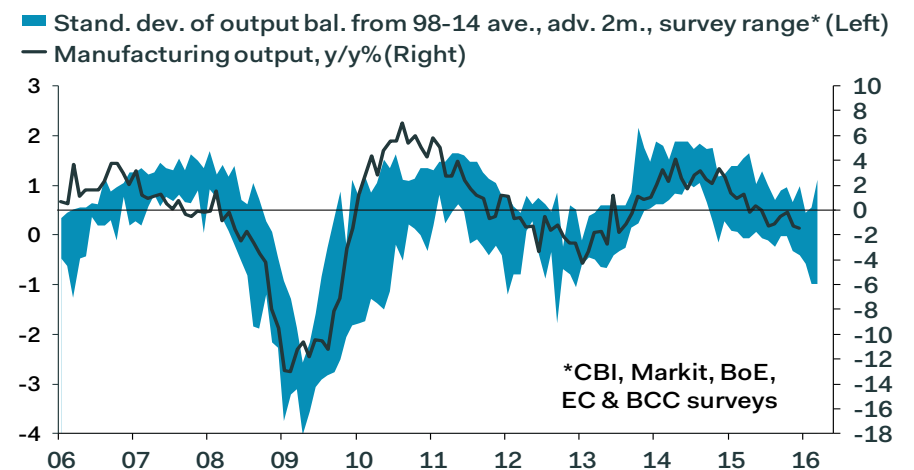
**2. THE INITIAL ESTIMATE OF Q4 GDP IS LIKELY TO BE CUT TO 0.4% FROM 0.5%**



**3. CONFIDENCE IS CONTINUING TO DRAIN AWAY**

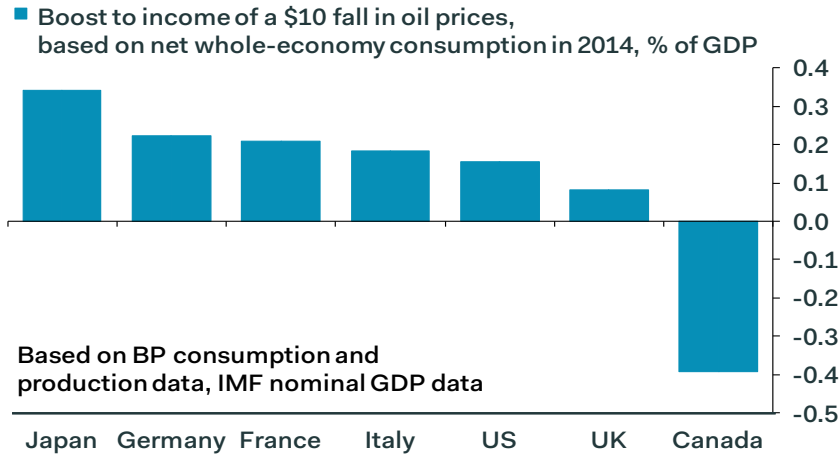


**4. MOST SURVEYS SUGGEST THE MANUFACTURING SLUMP IS DEEPENING**

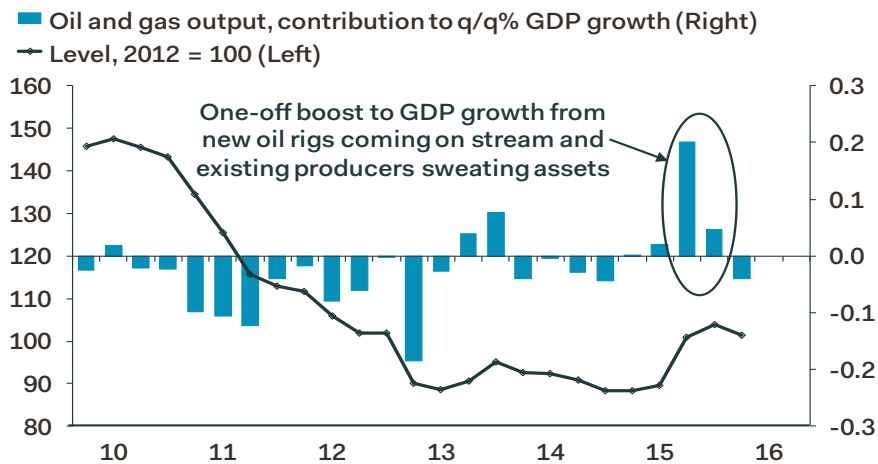




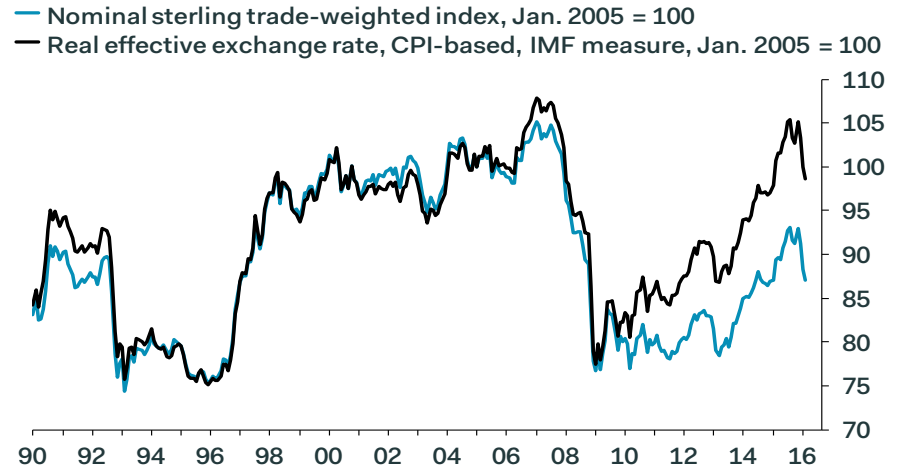
5. LOWER OIL PRICES ARE A NET POSITIVE FOR THE U.K., JUST



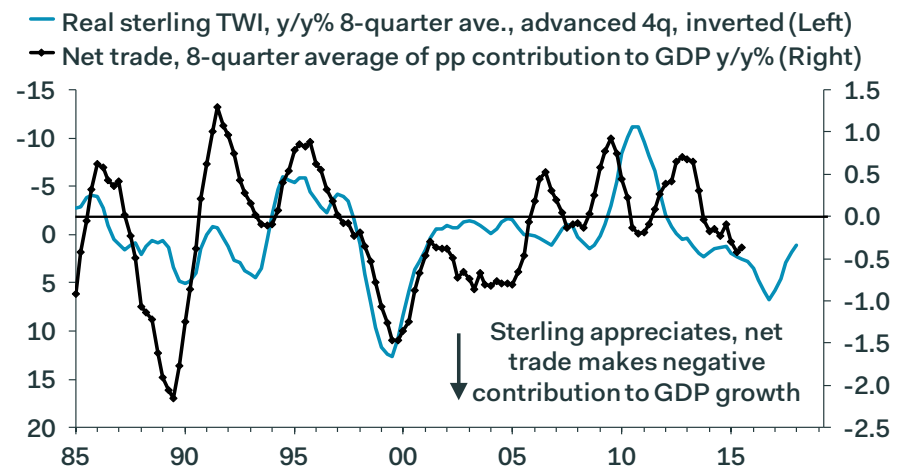
6. ...BUT THE SHAKE-OUT IN NORTH SEA OIL OUTPUT IS YET TO COME



7. STERLING REMAINS UNCOMPETITIVE, DESPITE ITS RECENT PLUNGE...

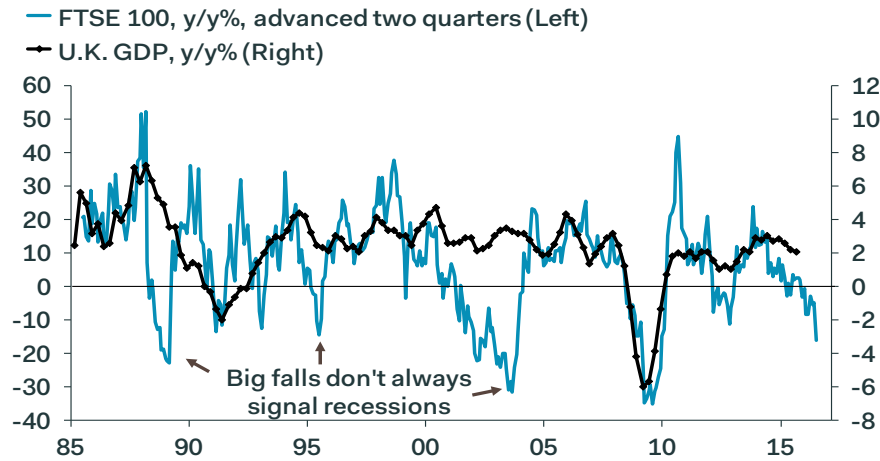


8. ...LAGS MEAN THE NET TRADE DRAG WILL BUILD IN EARLY 2016

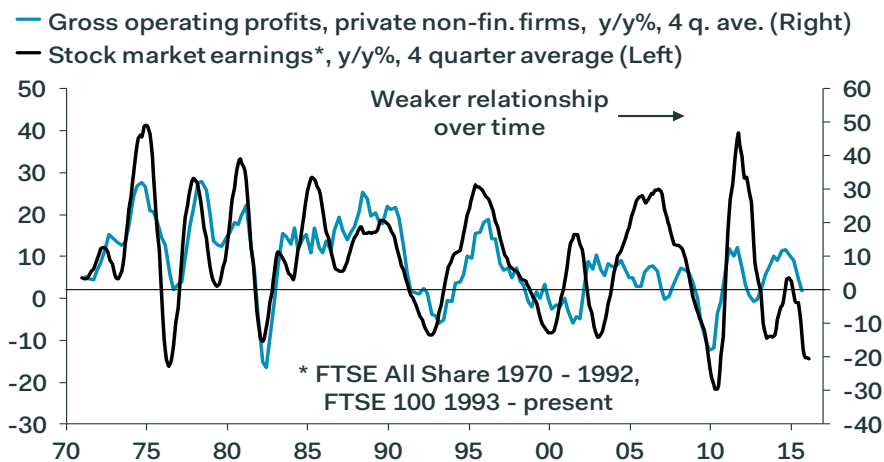




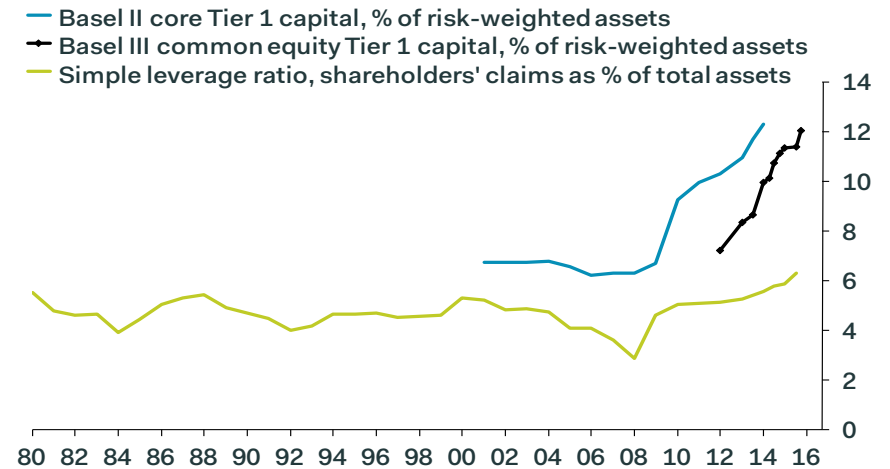
**9. EQUITY BEAR MARKETS DON'T ALWAYS SIGNAL RECESSION**



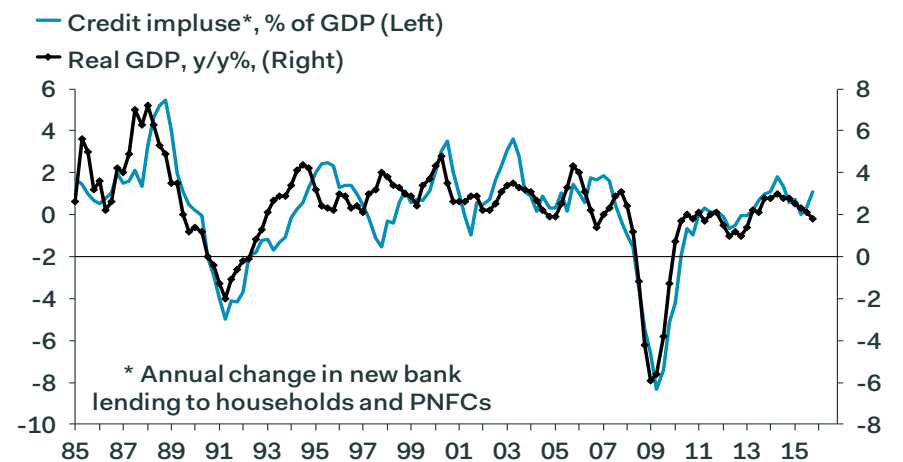
**10. FTSE 100 EARNINGS NO LONGER REFLECT DOMESTIC PERFORMANCE**



**11. BANKS ARE WELL-PLACED TO ABSORB LOSSES...**

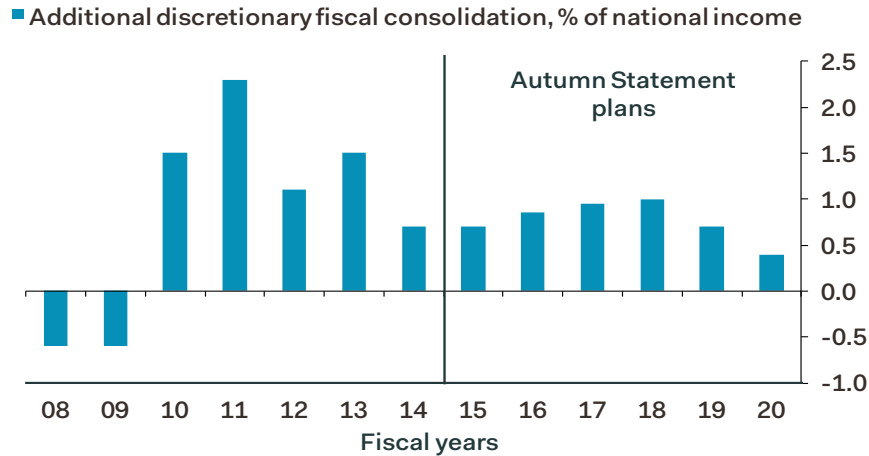


**12. ...AND STILL MAINTAIN CREDIT FLOWS, SUPPORTING GROWTH**

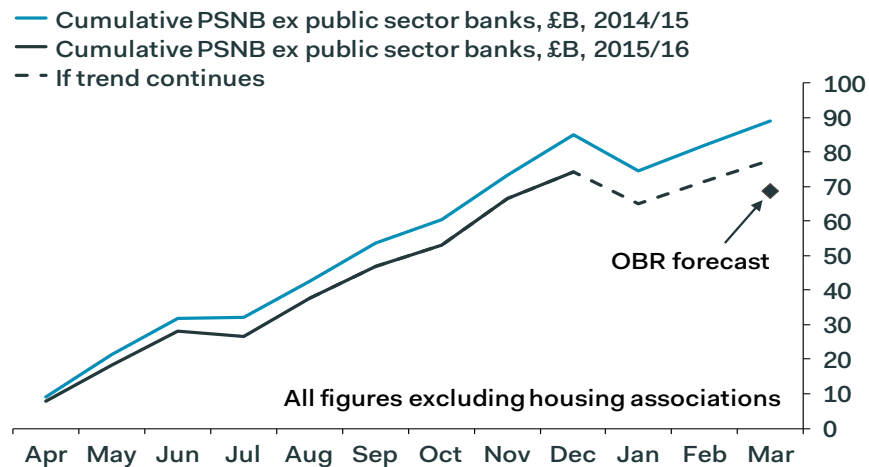




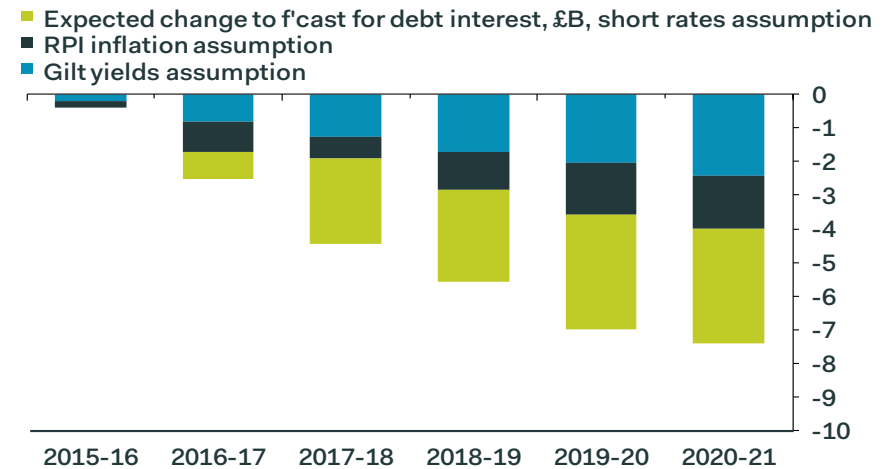
**13. THE FISCAL SQUEEZE IS SET TO INTENSIFY**



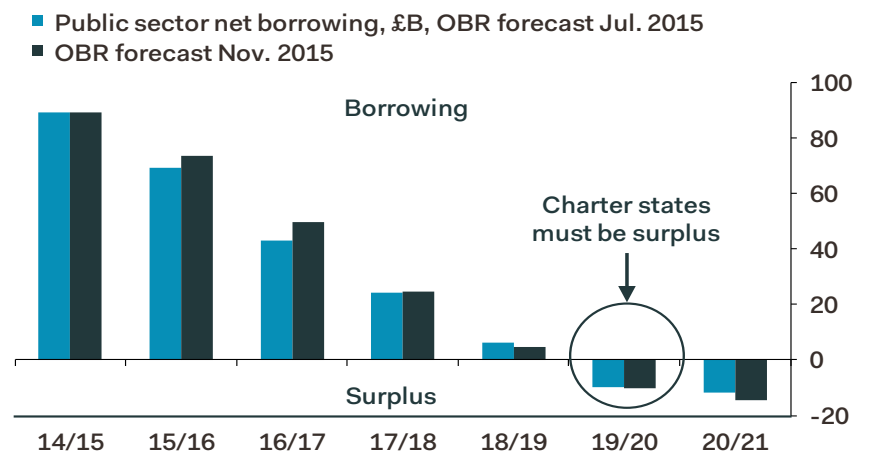
**14. AND BORROWING IS OVERSHOOTING THE PLANS, AGAIN...**



**15. LOWER DEBT INTEREST FORECAST WILL HELP IN THE MARCH BUDGET**



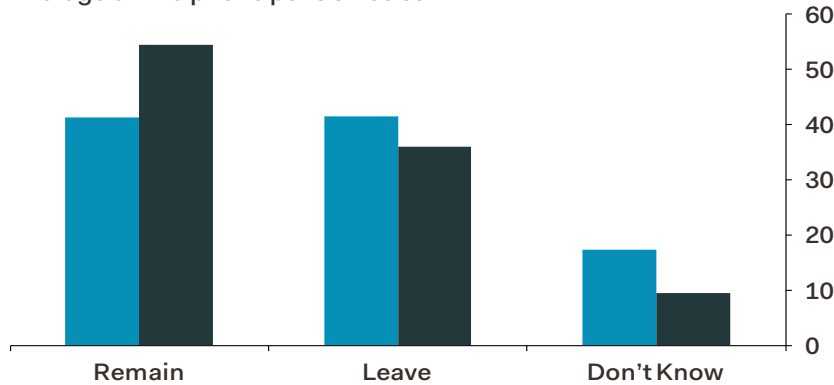
**16. BUT EXTRA AUSTERITY MAY BE ULTIMATELY NEEDED FOR A SURPLUS**



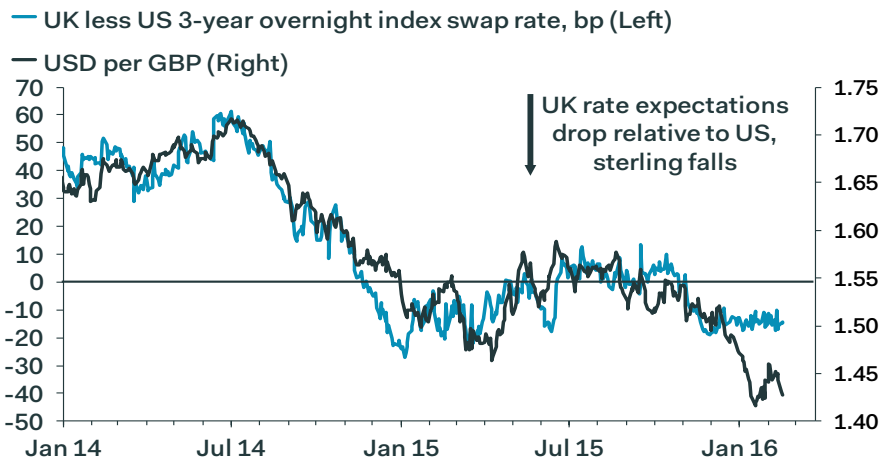


**17. BREXIT IS A 50:50 RISK, IF YOU BELIEVE ONLINE OPINION POLLS**

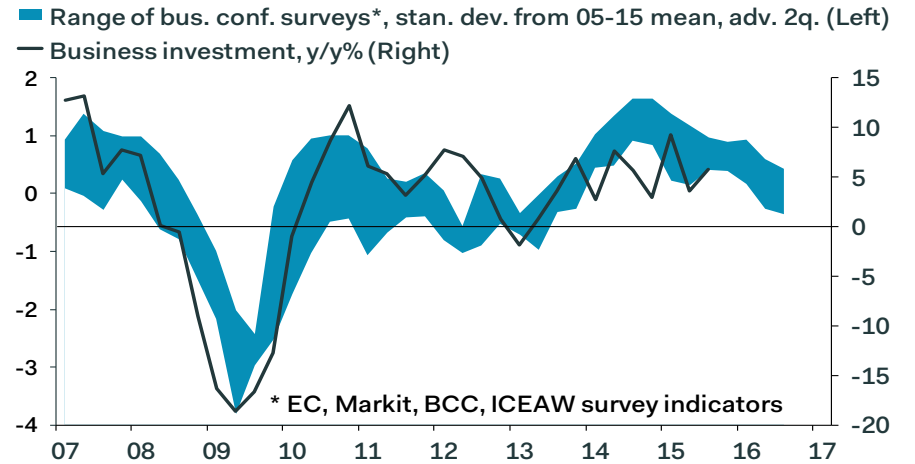
- E.U. Referendum voting intention, %, ave. of 10 online polls since Jan 1
- Average of two phone polls since Jan 1



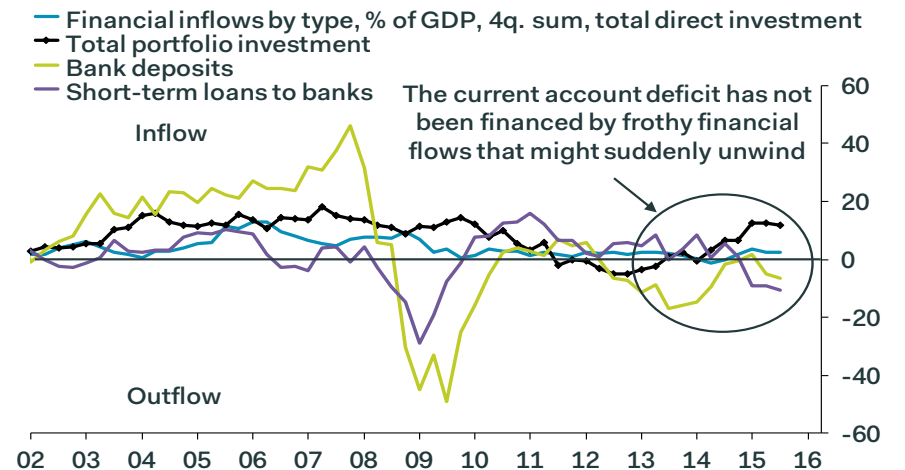
**18. MARKETS HAVE BEGUN TO PRICE-IN SOME DOWNSIDE RISKS...**



**19. ...WHILE BUSINESS CONFIDENCE APPEARS TO HAVE BEEN HIT TOO**



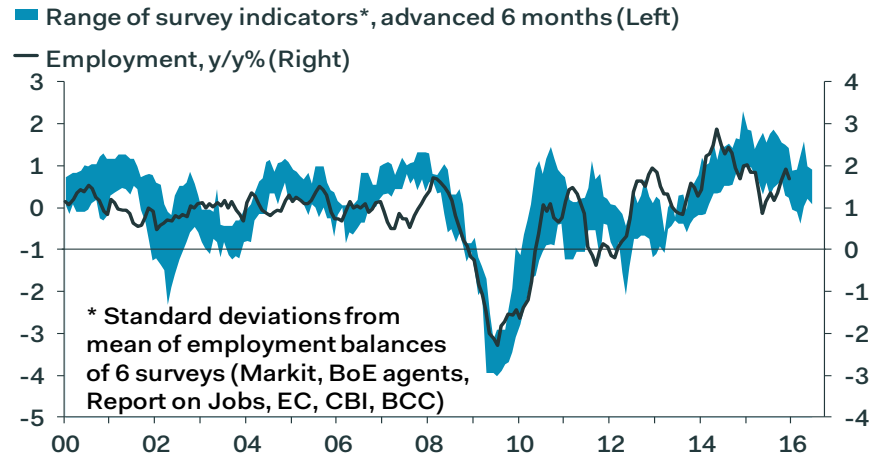
**20. BUT RAPID CAPITAL FLIGHT LOOKS UNLIKELY, PROVIDED NO BREXIT**



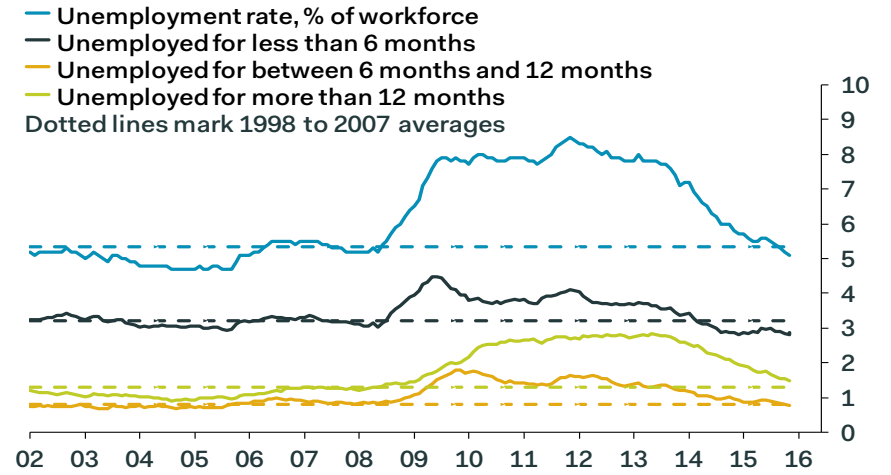




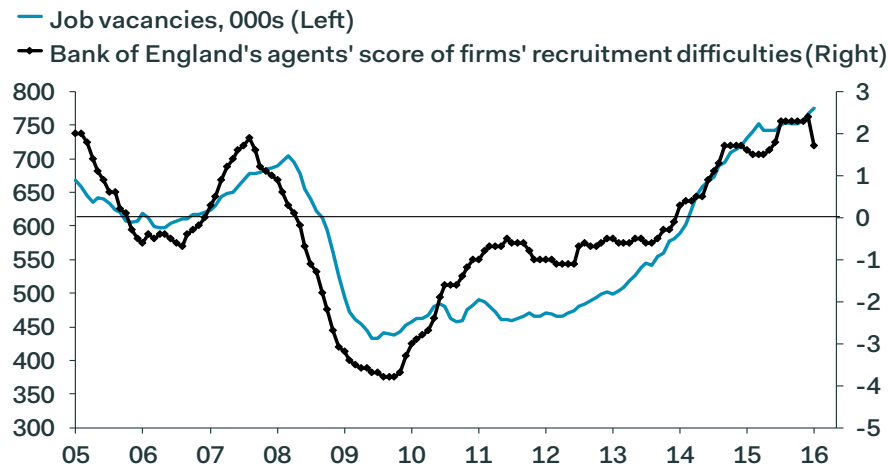
**21. SURVEYS INDICATE THE JOBS BOOM WILL LOSE SOME STEAM...**



**23. THE POOL OF SURPLUS LABOUR IS RUNNING DRY**



**22. ...BECAUSE FIRMS ARE STRUGGLING TO FIND SUITABLE CANDIDATES**



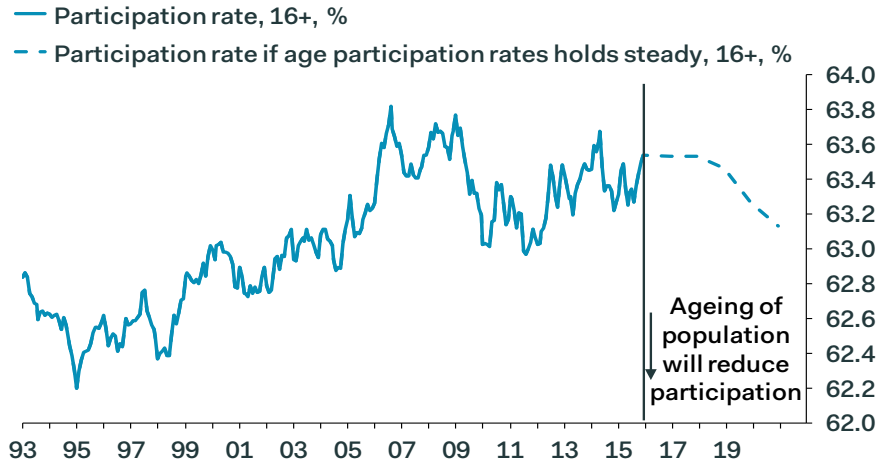
**24. PEOPLE WHO WANT WORK BUT ARE INACTIVE ARE SCARCE TOO**



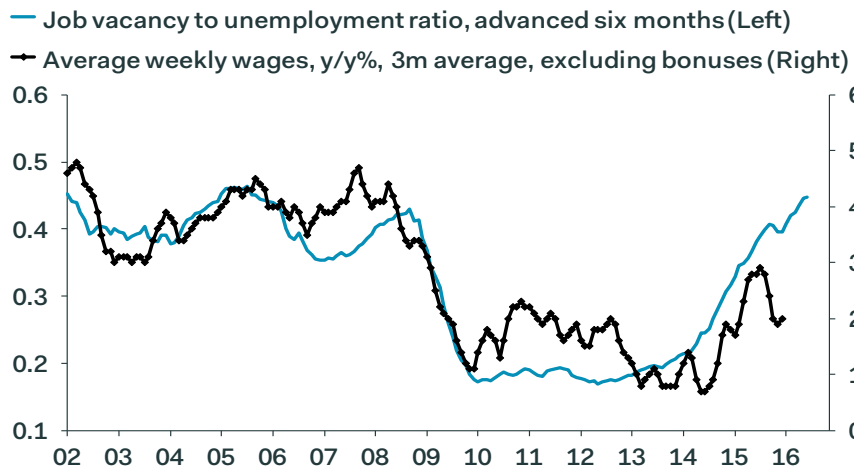




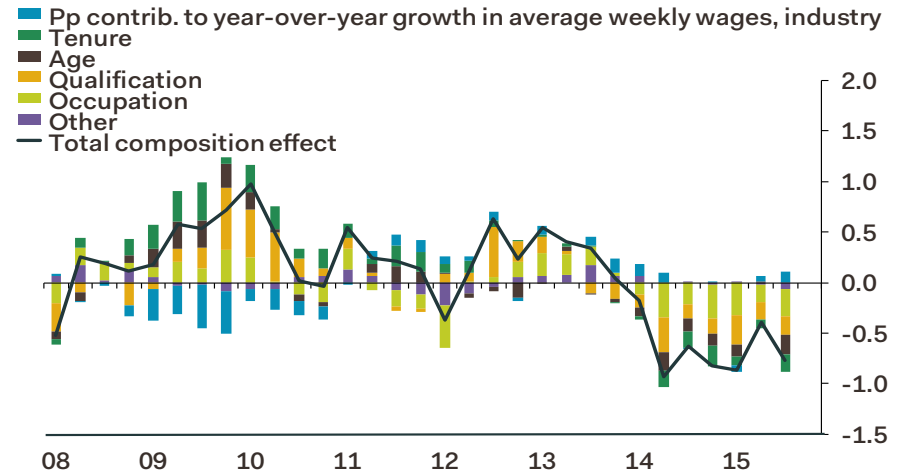
**25. PARTICIPATION WILL STRUGGLE TO RISE IN SECOND HALF OF DECADE**



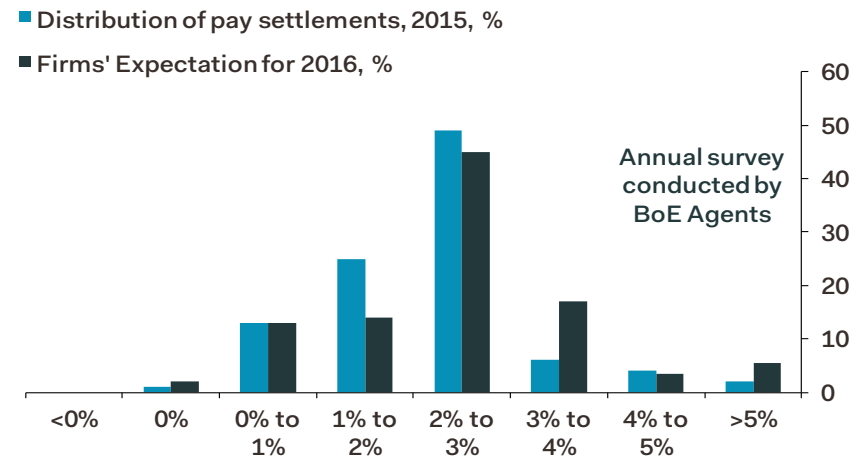
**26. WEEKLY WAGE GROWTH HAS EASED, FOR NOW**



**27. COMPOSITIONAL EFFECTS HAVE TEMPORARILY DEPRESSED WAGES**

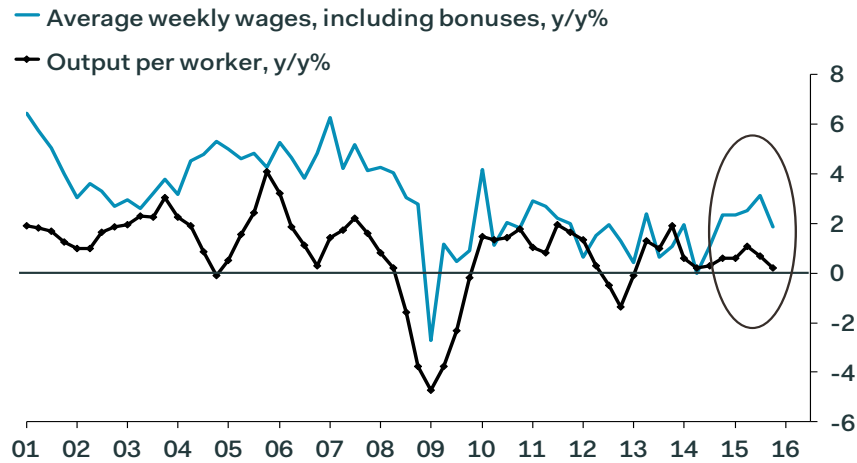


**28. PAY SETTLEMENTS, WHICH LAG WAGE GROWTH, ARE PICKING UP**

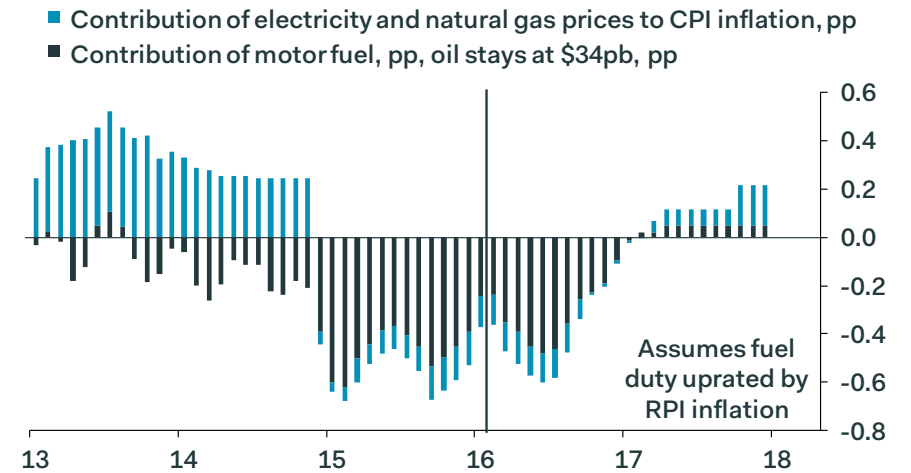




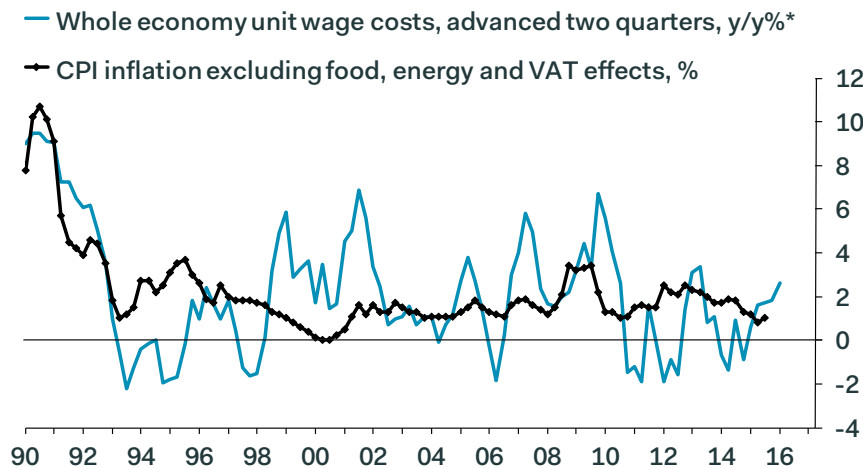
**29. WAGES STILL AREN'T BEING SUPPORTED BY PRODUCTIVITY GAINS...**



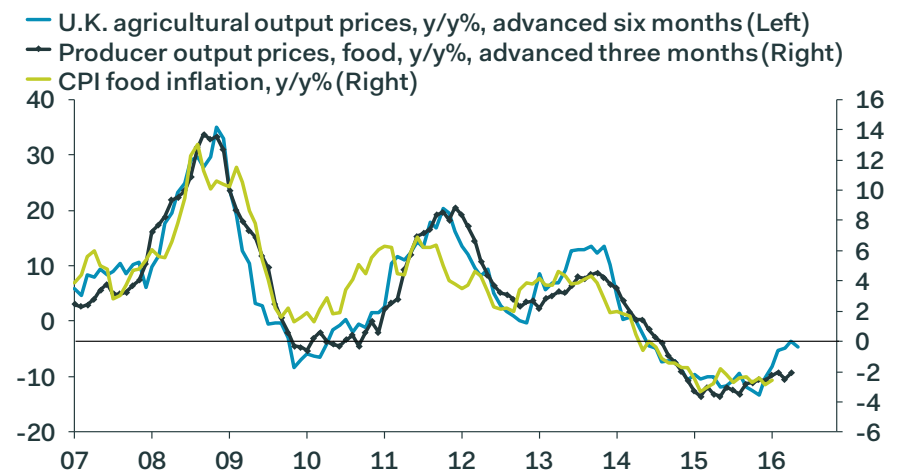
**31. THE DRAG FROM LOWER OIL PRICES WILL LINGER UNTIL LATE 2016...**



**30. ...SO UNDERLYING PRICE PRESSURES ARE INCREASING**

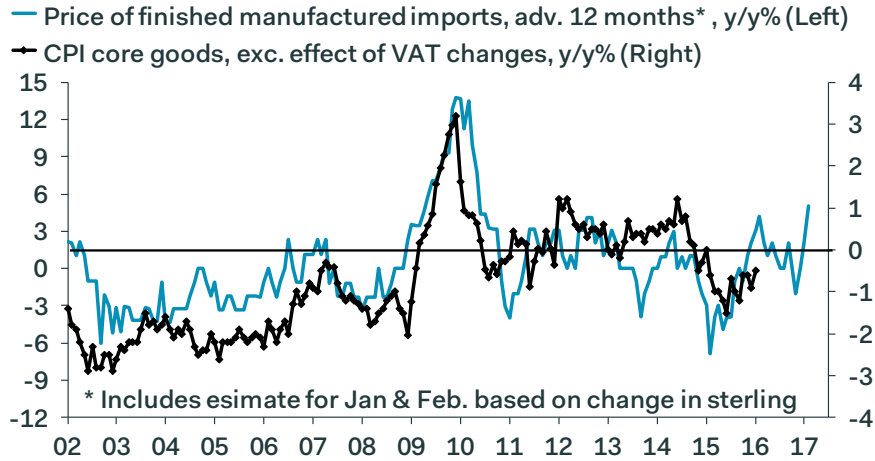


**32. ...BUT FOOD PRICE DEFLATION WILL EASE SOON**

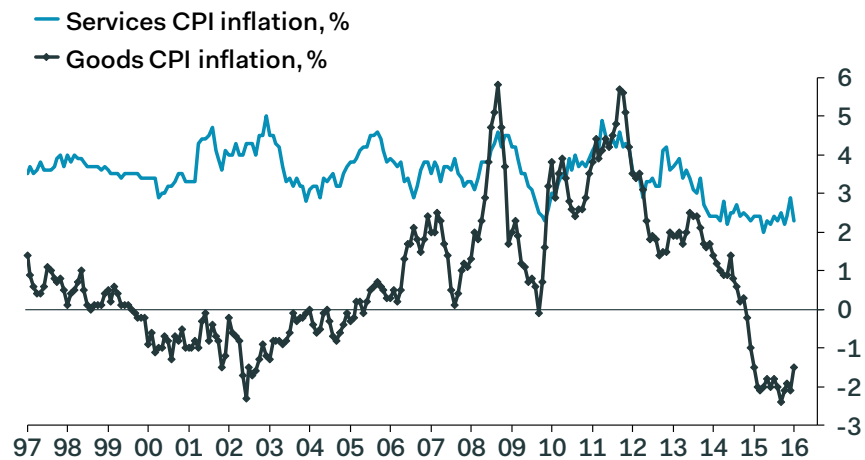




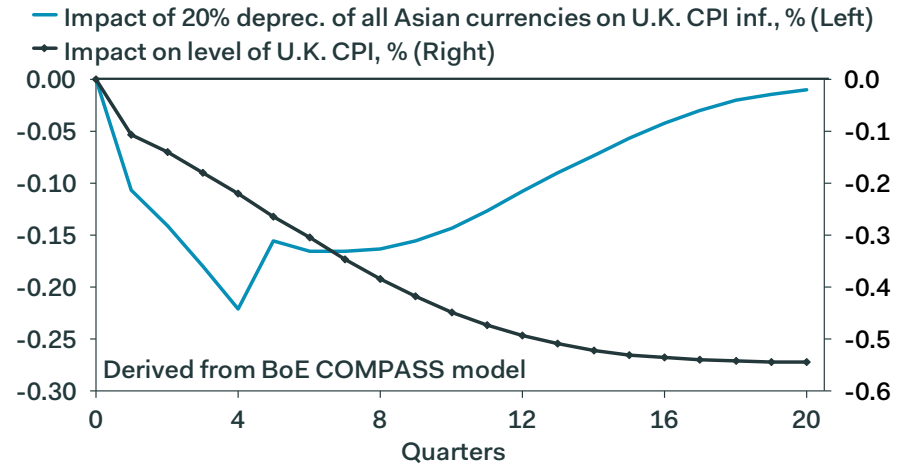
**33. THE DRAG FROM LOWER IMPORT PRICES ON CORE WILL FADE**



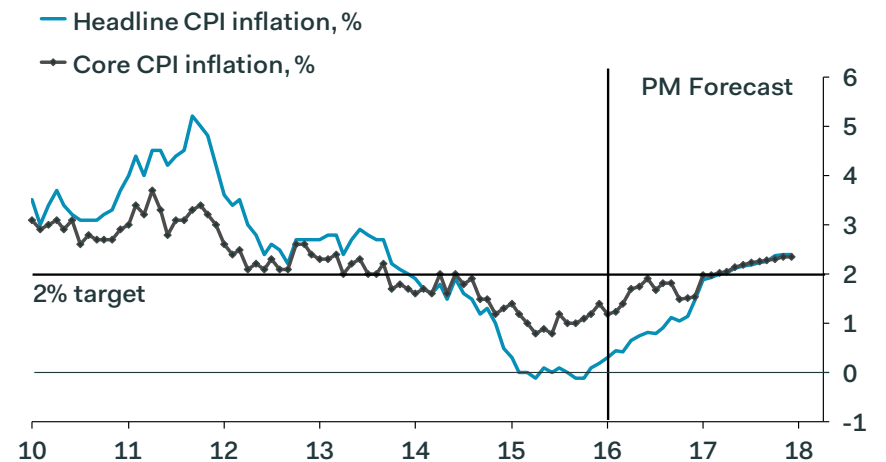
**34. STILL NO SIGN OF DEFLATIONARY PRESSURES SPREADING**



**35. A CHINESE DEVALUATION WOULD NOT UNLEASH A DEFLATION WAVE**

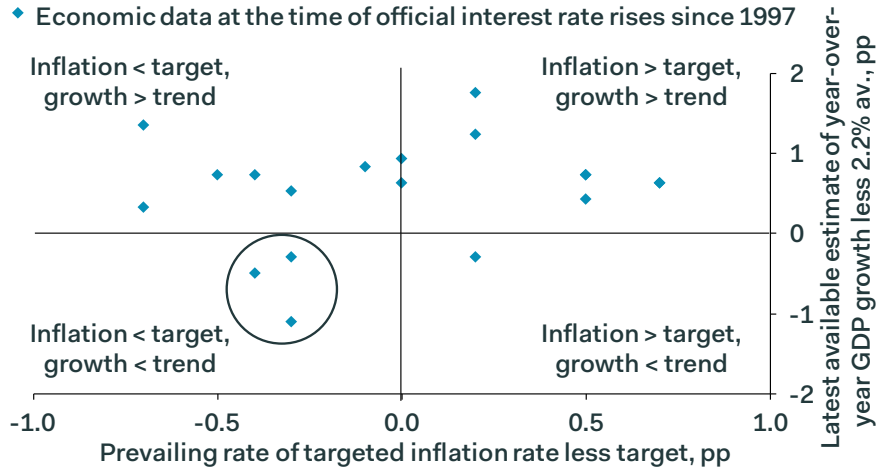


**36. SO CORE INFLATION IS SET TO NUDGE THE 2% TARGET THIS YEAR**

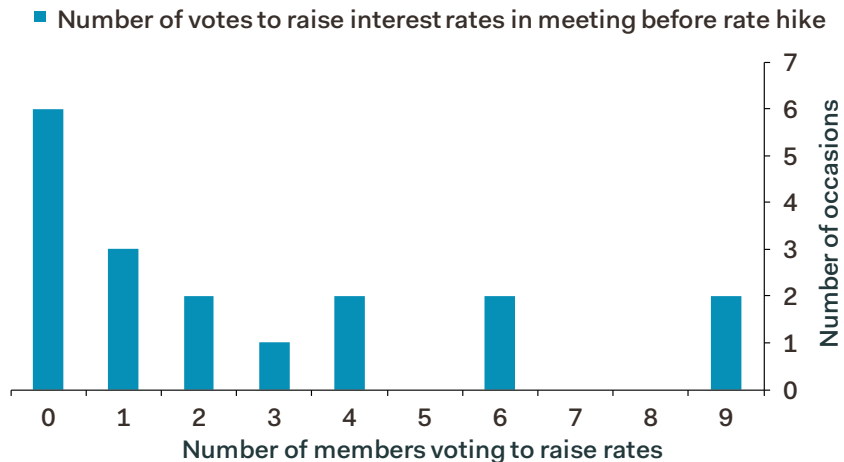




**37. THE MPC HAS HIKED WITH GROWTH SLOW AND INFLATION SOFT**



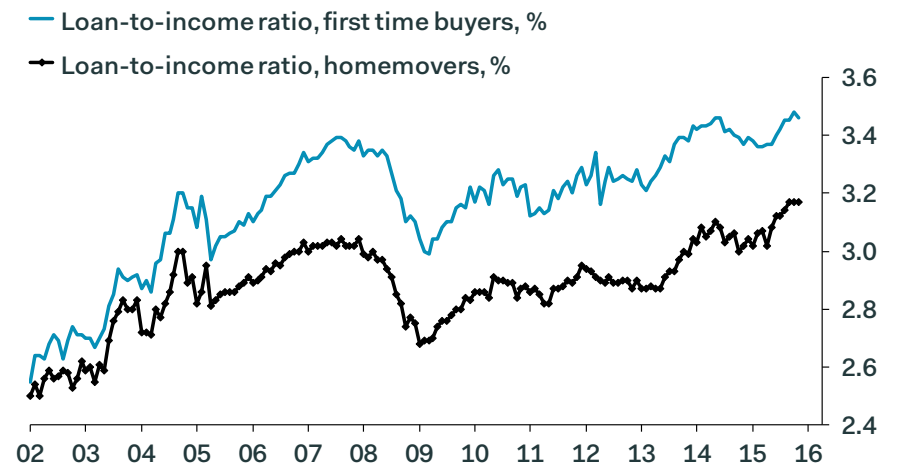
**38. RATE HIKES HAVE OFTEN COME WITH LITTLE FOREWARNING**



**39. RENEWED HOUSE PRICE MOMENTUM BOLSTERS THE CASE TO HIKE**



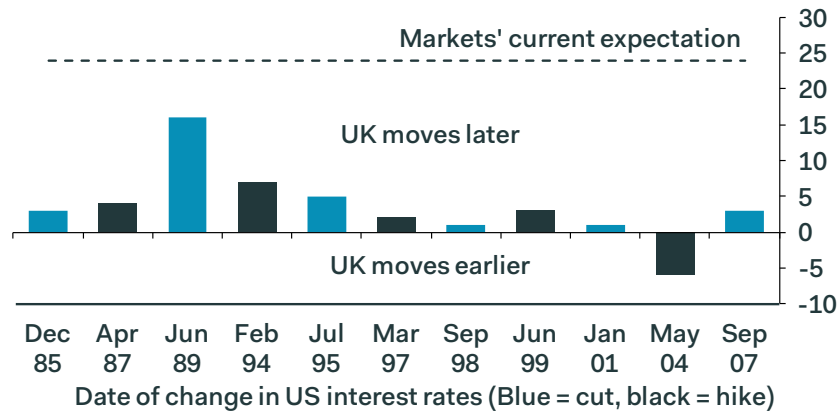
**40. LOAN-TO-INCOME RATIOS ARE NOW AT A RECORD HIGH**





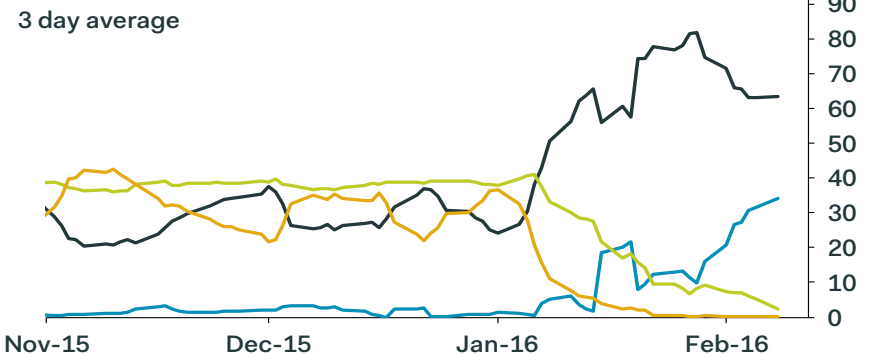
**41. U.K. RATES QUICKLY FOLLOW U.S., DUE TO IMPACT ON STERLING**

■ Months between change in direction of US interest rates and UK rates



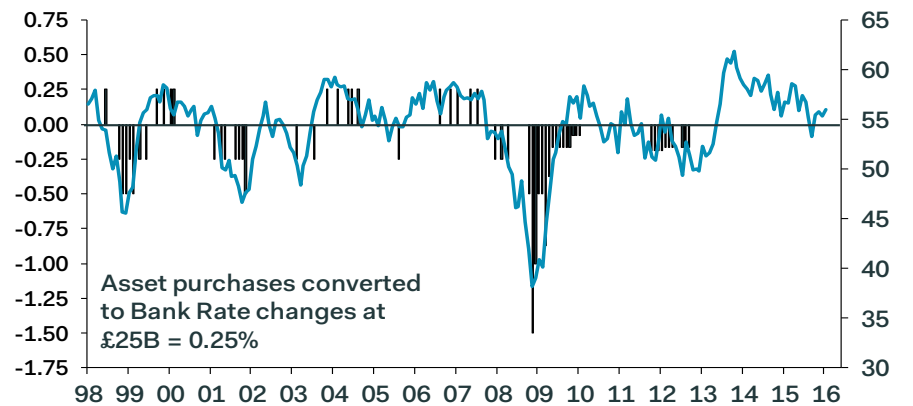
**42. MARKETS ATTACH A 0% CHANCE TO ONE 2016 HIKE; WE EXPECT TWO**

— Implied % probability of overnight int. rates in Dec. 2016, 0.25% or less  
 — 0.50%  
 — 0.75%  
 — 1.00% or more



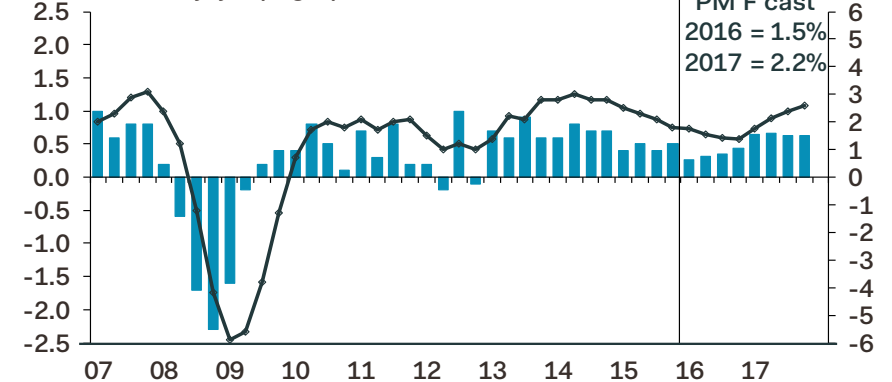
**43. THE U.K. WOULD HAVE TO FLIRT WITH RECESSION FOR A RATE CUT**

■ Change in Bank Rate, inc. QE decisions\*, pp (Left)  
 — U.K. Markit/CIPS composite PMI (Right)



**44. FISCAL AND EXPORT HEADWINDS SUGGEST SLOW, NOT NO, GROWTH**

■ Real GDP, q/q% (Left)  
 — Real GDP, y/y% (Right)





<b>Economic Activity (year-over-year, %)</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
Household spending	1.9	2.6	3.0	2.5	2.2
Fixed investment	2.6	7.3	4.4	3.0	4.0
Government spending	0.5	2.5	1.7	1.0	0.5
Inventories, cont. to GDP growth	0.7	0.2	-0.6	-0.2	0.1
Domestic demand	2.6	3.2	2.4	1.9	2.2
Exports	1.2	1.2	5.4	0.5	2.0
Imports	2.8	2.4	5.9	2.0	2.0
GDP	2.2	2.9	2.2	1.5	2.2

**Labor Market, Costs and Prices (year-over-year, %, year average unless stated)**

Output per worker	1.0	0.7	0.8	0.5	1.5
Employment	1.2	2.3	1.5	1.0	0.7
Unemployment rate (%)	7.6	6.2	5.4	5.0	4.8
Average weekly wages	1.2	1.3	2.4	3.0	3.5
Unit wage costs	-0.1	0.6	1.6	2.5	2.0
CPI	2.6	1.5	0.0	0.8	2.2
Core CPI	2.1	1.6	1.1	1.6	2.2
RPI	3.1	2.4	1.0	2.1	3.5
House prices, Nationwide measure (end year)	8.2	7.1	4.4	8.0	4.0

**Other**

Current account, % GDP	-4.5	-5.3	-4.1	-3.9	-3.3
Budget deficit, £B, FY	98.5	89.2	75.0	55.0	40.0
Budget deficit, % GDP, FY	5.7	4.9	4.0	2.8	1.9
Bank Rate, December	0.50	0.50	0.50	1.00	2.00
Asset Purchase Facility, £B, December	375	375	375	375	375
10-year gilt yields, Q4 average	3.02	1.76	1.96	2.50	3.50
30-year gilt yields, Q4 average	3.67	2.51	2.67	3.40	4.00
\$ per £, Q4 average	1.66	1.56	1.47	1.42	1.40
€ per £, Q4 average	1.20	1.29	1.36	1.41	1.40
FTSE 100	6749	6566	6242	6200	6500