UK: Industrial output plunges in August

Tue Oct 6, 2009 3:59pm BST

By Fiona Shaikh and Kylie MacLellan

LONDON (Reuters) - Industrial output plunged unexpectedly in August and at its sharpest monthly pace since January, according to official data on Tuesday, denting hopes for an economic rebound in the third quarter of this year.

The Office for National Statistics said manufacturing output fell 1.9 percent on the month, confounding analysts' expectations for a 0.3 percent rise. July's increase was revised down to 0.7 percent from 0.9 percent.

The wider measure of industrial output, which includes power generation and resource extraction, fell by 2.5 percent on the month, also the sharpest drop since January and against forecasts for an increase of 0.2 percent.

August's falls in output more than offset the gains recorded in the previous two months, and, although industry accounts for just 17 percent of the economy, lessened the chance that Britain has emerged from recession after more than a year in decline.

Analysts now reckon GDP will barely enter positive territory in Q3 and even then only if services output recovers strongly.

"August's dismal industrial production figures will dampen some of the recent optimism about the economy's apparent bounce-back," said Vicky Redwood of Capital Economics.

"Accordingly, a return to positive overall GDP growth in Q3 now looks less certain," she added.

The National Institute for Economic and Social Research said the economy probably did not grow at all in the third quarter of this year, after a modest expansion of 0.1 percent in the three months to August, an outturn it described as "disappointing."

The pound fell to a 1-week low against the euro and gilt futures hit a contract high as investors scaled back their expectations for a quick recovery and bet that monetary policy would have to remain loose for some time yet.

"This is a bit of a reality check on the status of the UK economy," said Philip Shaw, economist at Investec.

Bank of England policymakers have expressed concern about the strength of any upturn in the economy and Tuesday's data will reinforce their view that Britain is in for a long, hard slog back to growth, even though some forward-looking indicators have improved in recent months.

The central bank is unlikely to alter its monetary stance at its rate-setting meeting this week, however, and is seen keeping rates at a record low of 0.5 percent and leaving its 175 billion pound quantitative easing programme intact.

But some analysts said the unexpected weakness in manufacturing raised the chance the BoE would increase its stimulus to the economy next month to shore up demand.

"While we stick with the view that policy will be left unchanged at this week's October meeting, the chance of more QE in November has gone up significantly," said Allan Monks, economist at JP Morgan.

WIDESPREAD FALLS

The ONS said the drop in manufacturing output was broad-based, with all 13 categories recording falls in August. It noted there were particularly large declines in paper and publishing, electrical and optical equipment and food and drink.

But part of that may have been due to factories pausing production in August, and some of July's strong rise in output may have been the result of firms ramping up output before the summer break, the ONS said.

In addition, oil and gas output was hit by plant closures due to annual maintenance work, leaving production down 7.7 percent on the month -- the steepest decline since October 2008.

Analysts said there was still some chance of a rebound in September.

"We cannot write off positive GDP growth in Q3 altogether," said Colin Ellis, economist at Daiwa Securities. "Today's fall could prove erratic and reverse in September -- in which case production in Q3 would be down just marginally from the second quarter."

Indeed, other data on Tuesday painted a more upbeat picture of the economy.

The Society of Motor Manufacturers and Traders said car sales jumped 11.4 percent on the year in September, partly due to the government's car scrappage incentive scheme.

And the figures raised the prospect that this component of manufacturing could yet improve after August's 2.6 percent decline in motor vehicle production on the ONS measure.

"Hopefully, the manufacturing sector will increasingly benefit from sharply reduced stock levels, and from the relatively weak pound making UK manufacturers more competitive in both overseas and domestic markets," said Howard Archer, economist at IHS Global Insight.

(Editing by Chris Pizzey)

http://uk.reuters.com/article/idUKTRE5951O320091006?sp=true