theconstructionindex

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Weekly Economic Update

31st January 2010

Summary

UK GDP data were disappointing last week, with the economy expanding by merely 0.1% in the final quarter of 2009. The obstacles to a sustained UK economic recovery appear clear: indebted consumers looking to reign in spending and the urgent need for Government to reduce public debt in the near future.

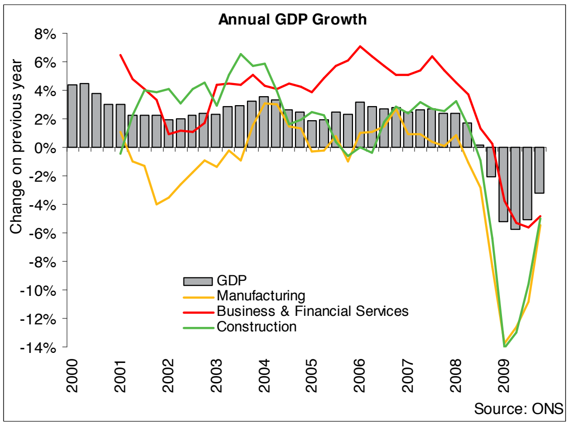
Statistics

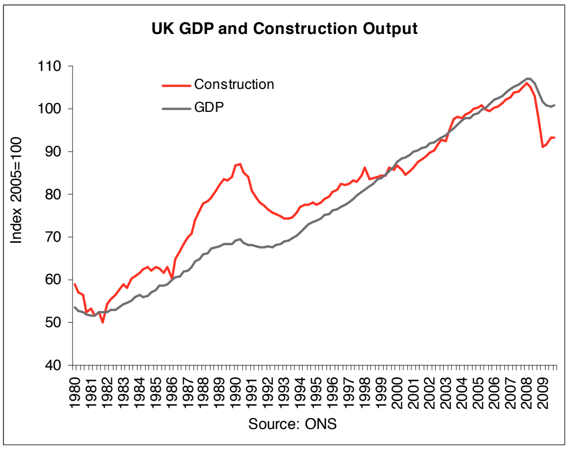
Economy

- According to official data, Britain's 18-month recession is technically over, but the recovery is disappointing, with GDP increasing just 0.1% in the 4th quarter of 2009. Overall, the **UK economy** shrank 4.8% in 2009, while the total decline in GDP from the peak in the first quarter of 2008 to the trough in the third quarter of 2009 was 6.1%.

  The **services sector** expanded by 0.1% during the 4th quarter, following five quarters of decline. Services output was still down 2.7% year-on-year in the 4th quarter and contracted 3.7% overall in 2009. Within the sector, business services and finance output was unchanged during the 4th quarter and still down 4.8% year-on-year. **Manufacturing output** expanded 0.4% during the quarter, but remained down 5.5% on a year ago and contracted 10.8% during 2009 as a whole. **Construction** output was unchanged during the 4th quarter compared to the preceding three months, but fell 4.9% year-on-year. Overall construction contracted 10.5% in 2009. The decline since the 1st quarter of 2008 now stands at 12%.

  The recovery in the UK remains very sluggish relative to the US and Euro area, despite the unprecedented loosening of financial and monetary conditions over the past 12 months. Most analysts predict the Bank of England to halt its £200bn asset buying programme next month, but the weak figures underpin expectations that a monetary policy tightening is still some way off.

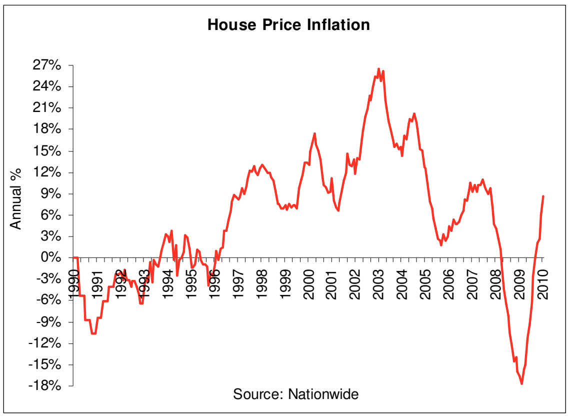




- **Consumer confidence** rose in January for the first time in three months, according to the GfK Consumer Confidence Index, as consumers became more optimistic for the economy's prospects. The index of consumer sentiment advanced from -19 to -17. The gauge of expectations for the economy in the next year rose from -6 to -2. In the 4th quarter, service industries and manufacturing expanded only enough to outweigh other sectors to get the economy growing again. The return of the consumer confidence is welcome as private consumption is essential in supporting the recovery.

- In contrast to the Gfk Consumer Confidence Survey, the **CBI Distributive Trades survey** shows that high street sales in January fell at their sharpest annual rate for five months. Among the retailers being surveyed, 28% said sales had risen while 36% said they had dropped. The CBI attributed the fall in consumer demand to the rise in VAT and the cold weather. The disappointing survey reinforces the heightened concerns over the strength and sustainability of the UK recovery. Household are still facing very challenging conditions, notably high unemployment, low earnings growth, high debt levels and the prospect of fiscal tightening ahead that will possibly include tax hikes.

- **House prices** rose by 1.2% in January and annual growth jumped to 8.6%, according to the Nationwide. The average price of a typical UK property now stands at £163,481. The revival in house prices since February 2009 is a consequence of sharply reduced mortgage interest rates and a lack of supply in the market. Additionally the stamp duty threshold of one per cent moved back down to properties costing £125,000 from £175,000 in January, which may have created a rush to buy before year end.



- **Commodity prices** extended their falls last week, amid mixed economic data. The price for Brent crude oil fell below $73 a barrel, after data showed an increase in US inventories. Metal prices also slipped back, as Chinese attempts to take the heat out of their economy continued.

Commodity Prices (29th January 2010)				
	Price	Weekly change	Monthly change	Annual change
"Brent" Oil ($/ barrel)	72.49	-2%	-3%	61%
Copper ($/tonne)	7,041	-3%	1%	113%
Aluminium ($/tonne)	2,125	-3%	-6%	56%
Nickel ($/tonne)	18,125	-2%	-2%	54%
Global Steel Price (Index 04/1994=100)	159.78	0%	7%	1%

Source: FT, LME, Cruspi

- The **Pound** gained against the Euro, rising 1% to £/€1.154, amid ongoing concerns about Portugal's budget and continuing Greek problems. The Euro also fell to a 6-month low against the Dollar. The Pound rose against the Dollar earlier last week, but gains were lost after ratings agency S&P said that Britain had no longer one of the most stable and low-risk banking systems in the world. Overall the Pound ended the week unchanged against the Dollar at £/$1.612.

Looking ahead

- The Bank of England's Monetary Policy Committee will have a challenging February meeting this week. Weak GDP growth in the 4th quarter, sharply higher consumer price inflation and still tight lending conditions will leave the committee pondering whether or not to extent the quantitative easing program. **Interest rates** will probably be kept at 0.5%. Bank of England data is expected to show **mortgage lending** edged higher in December as the number of mortgage approvals for house purchase continued to rise from the troughs of late 2008. orms. **Consumer borrowing** is forecast to have fallen for a 6th consecutive month.

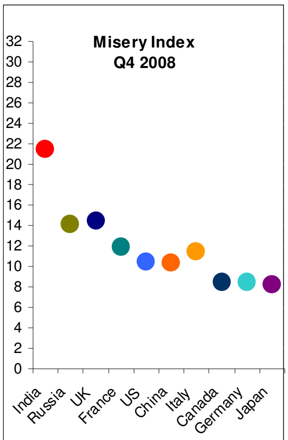
  The **construction PMI** is likely to show that sector activity continued to decline in January, with the commercial sector particularly weak. In the near future, the construction sector will be hit by the government's need reduce public expenditure on infrastructure and public buildings. The **service sector PMI** is forecast to indicate that activity expanded for a 9th successive month in January, but at a modestly reduced rate, because of the bad weather's effects and an increase in VAT. The **manufacturing PMI** is expected to stay in positive territory in January, though the index could show that the industrial recovery struggles to sustain momentum. **Producer input prices** are likely to have risen further in January due to a surge in commodity prices. **Output prices** should therefore have risen too as producers look to ease some of the pressure on their profit margins.

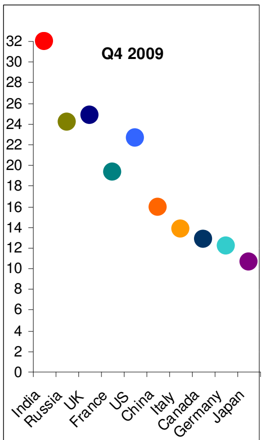
Focus on…Recovery hopes, but challenges ahead

Global leaders met at the annual World Economic Forum in Davos last week. The mood was certainly better than last year, when policymakers fretted about the depth of the global economic recession. This year, policy makers debated how strong the global recovery will be in 2010, though concern over public indebtedness dampened optimism. Indeed, the IMF warns that 2010 may prove to be a tumultuous year for sovereign debt issuers.

IMF - World Economic Outlook	(Annual % change)			
	2008	2009	2010	2011
World output	**3**	**-0.8**	**3.9**	**4.3**
United States	0.4	-2.5	2.7	2.4
Euro area	0.6	-3.9	1	1.6
Germany	1.2	-4.8	1.5	1.9
France	0.3	-2.3	1.4	1.7
Japan	-1.2	-5.3	1.7	2.2
United Kingdom	0.5	-4.8	1.3	2.7
Russia	5.6	-9	3.6	3.4
China	9.6	8.7	10	9.7
India	7.3	5.6	7.7	7.8
Middle East	5.3	2.2	4.5	4.8

Following the deepest global downturn in recent history, record-low interest rates, significant fiscal stimulus measures, major support for the banking sector and improved global trade and economic activity on the back of **emerging market resilience** have helped the **advanced economies to return to growth** over the latter half of 2009. The IMF's published its latest **global growth forecasts**. It revised up its predictions, now expecting global growth of 3.9% in 2010 and 4.3% in 2011. Like other forecasters, the IMF predicts the growth recovery to be uneven, with the advanced economies underperforming, due to few signs of non-stimulus related private sector demand. Growth in emerging and developing economies is expected to be relatively swift, largely driven by buoyant internal demand. The IMF projects the US economy to grow 2.7% in 2010, the Eurozone 1%, Japan 1.7%, 10% for China and 7.7% growth for India.

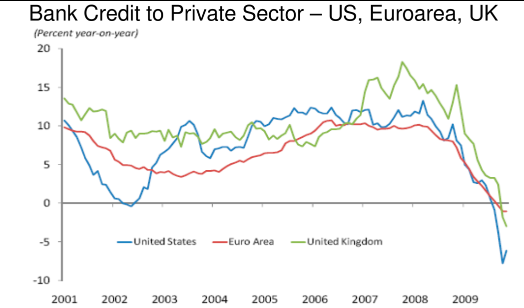




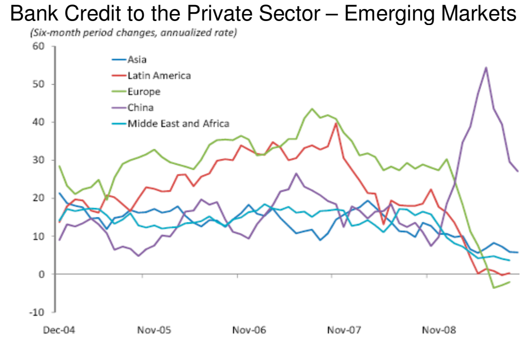
Misery index: sum of inflation rate, ILO unemployment rate and budget deficit in % of GDP. Selected countries only. Latest available data, dates vary

It has been well recorded that the **UK has been the laggard in the global recovery race,** being the last G20 economy to exit from recession in Q4 2009. The UK has climbed up the **"Misery Index"** over the last year, as GDP slumped and public debt increased sharper than many of its peers. India, despite having one of the strongest growth rates in 2009 continued to lead the index, due to weak government budget and high inflation. The US is also suffering from a sharp increase in the budget deficit and high unemployment. In the UK, the return to growth is certainly welcome, but it is unlikely to prompt a widespread sigh of relief. The **UK economy's headwinds** to a significant recovery in activity remain: the need to reduce household debt, high unemployment and the prospect of a substantial fiscal tightening.

Bank Credit to Private Sector – US, Euroarea, UK



Bank Credit to the Private Sector – Emerging Markets



Source: IMF

In its latest **Financial Market Stability Report**, the IMF argues that **systemic risks in global financial markets continue to subside.** Risk appetite has returned, equity markets have improved, and capital markets have re-opened, as the worst fears of investors about a collapse in economic and financial activity have not materialised. However, despite improvements, financial **stability remains fragile** in many advanced countries and some hard-hit emerging market countries. Credit channels have not yet normalised and losses from commercial real estate exposures are expected to increase markedly. **Capital inflows into some emerging market countries** are beginning to raise concerns about asset price and exchange rate pressures. One the main topics this year will be **sovereign debt,** as public policy support has come at the cost of a significant increase in public debt burdens, which could raise risks for financial stability in the future. The challenge for policymakers is now to judge the timing, pace, and sequencing of exit policies, both from the monetary and financial policies, as well as starting to implement a medium-term strategy for fiscal consolidation and debt reduction.

Market Watch

Share prices	Market Cap, £mn	Week	Month	Year
	Friday 29th January 2010			
FTSE100		-2.2%	-4.6%	23.8%
Real Estate				
British Land	3,790	1.4%	-5.2%	19.2%
Hammerson	2,660	-1.8%	-7.2%	43.9%
Land Securities	4,860	-1.6%	-3.0%	11.7%
Liberty Intl.	2,850	-0.7%	-10.5%	34.8%
Shaftesbury	863.4	-0.6%	-0.9%	82.7%
Great Portland Est.	888.6	-1.5%	-3.8%	66.7%
Derwent London	1,340	-1.9%	2.5%	120.2%
Segro	2,330	-1.3%	-8.6%	15.6%
Quintain Estates & Development	304.3	-3.3%	-2.5%	398.5%
St. Modwen Properties	388.1	-3.0%	-0.7%	89.3%
TR Property Investment Trust	574.3	-0.3%	-1.1%	40.1%
Unite Group	455.7	3.6%	-0.6%	322.5%
Workspace Group	247.1	2.3%	-3.3%	30.1%
Minerva	115.2	3.6%	-6.5%	279.0%
Average**		***-0.8%***	***-5.0%***	***48.0%***
Contractors				
Balfour Beatty	1,800	-3.6%	3.3%	-14.2%
Carillion	1,180	-1.2%	-1.4%	29.5%
Morgan Sindall	235.2	-2.0%	-12.6%	-3.5%
Kier Group	366.8	-3.7%	-7.5%	0.1%
Lend Lease Corp*	2,267	-4.1%	-8.4%	42.0%
Average		***-3.2%***	***-3.5%***	***17.7%***
Material Suppliers				
Wolseley	3,860	-2.2%	9.9%	95.0%
SIG	673.6	-5.6%	0.5%	11.7%
Marshalls	162.4	-3.4%	-0.6%	37.8%
Kingspan	866	-6.1%	-3.7%	118.7%
BSS	318.9	-7.0%	3.7%	-4.5%
Average		***-3.4%***	***6.2%***	***82.0%***
House Builders				
Persimmon	1,310	-4.4%	-5.8%	50.4%
Taylor Wimpey	1,240	-2.7%	3.1%	234.5%
Barratt	1,170	-5.9%	1.4%	163.6%
Bovis Homes	544.1	-5.2%	-2.1%	8.0%
Bellway	899.9	-1.0%	-3.5%	31.4%
Berkeley	1,080	-1.8%	-4.3%	4.0%
Average		***-3.5%***	***-1.8%***	***93.7%***

*Lend Lease Corporation Limited is listed on the Australian and NZ stock exchange
**Sector averages are weighted according to current market capitalisations

The UK equity markets remained under pressure last week, as Standard & Poor's expressed concerns over the UK's credit worthiness amid economic difficulties. S&P issued a negative outlook on the UK's AAA rating, citing apprehensions over its ability to reduce current debt levels and the condition of its banking industry, which has been driven to the brink by the global financial crisis and economic downturn.

The FTSE 100 stood at 5,188.5 on Friday, down 2.2% over the last week. With only a few exceptions, real estate companies, building contractors, material suppliers and housebuilder all ended the week in the red.