

ECONOMIC UPDATE: LEEDS CITY REGION, SEPTEMBER 2017

Key points at glance

This report presents the latest assessment of the Leeds City Region economy. It sets out the recent developments in the world's leading economies, along with trends and forecasts for global growth. It analyses the recent economic performance of the UK, before considering in more detail the latest developments in Leeds City Region.

National and international headlines

- **Global activity is strengthening amid rising confidence and a pick up in trade**, according to the World Bank.
- **The UK economy grew by 0.3% in Q2 2017, a slight increase from 0.2% in Q1**, but lower than other major economies and below levels seen in 2016.
- The World Bank's forecasts for global growth remain largely unchanged from their January projections. Their **outlook for the UK has been revised up slightly**, though growth is still expected to slow a little from 2016.
- **The UK employment rate has surpassed 75% for the first time since records began**, with full-time, permanent positions driving this growth.
- **Inflation remained elevated at 2.6% in July**, unchanged from June but down slightly from May's 2.7% peak. Meanwhile regular pay growth has risen to 2.1%, so whilst **real pay growth remains negative**, the gap between wages and inflation has narrowed slightly.

Key City Region and local developments

- **Yorkshire & Humber is the fastest growing region of the UK in terms of business activity**, according to the Markit/Lloyds Bank Regional PMI for July. The region's PMI of 58 is higher than any other region.
- **The number of new business bank accounts opened in Leeds City Region so far this year is broadly in line with 2016 activity**. There have been around 1% fewer accounts opened so far this year than at the same point in 2016 compared to a 2.2% fall nationally.
- The Chambers of Commerce QES found **increasing confidence among service sector firms** in Leeds City Region, though key measures of **manufacturers' confidence fell to their lowest levels in almost four years**.
- There are 28,500 more people in work in Leeds City Region than a year ago. This **2.1% increase in employment is higher than in any other northern LEP area, and is 2nd only to Greater Birmingham & Solihull among core city LEPs**. The employment rate has increased to 73.5%, up from 73.1% in the previous quarter.
- **Export activity continued to expand in Q2 2017 according to the QES**, though there was a divergence in trends with service sector firms outperforming their manufacturing counterparts.
- **Average house prices in Yorkshire & Humber grew by 4.9% between June 2016 and June 2017** – the same growth rate as the UK as a whole. Within LCR, York saw the fastest increase, up 7.6% on a year earlier, whilst Calderdale and Barnsley also saw prices increase faster than the national average.

Key conclusions and outlook

- In headline terms, the UK economy's continued expansion, with growth picking up slightly in Q2, is positive news. However, **the UK growth rate is now substantially below that in other major developed economies**, suggesting uncertainty stemming from Brexit negotiations is having an impact on UK GDP growth.
- The **service sector appears to be outperforming the rest of the economy**, with a tailing off of export growth contributing to a slowdown for manufacturers.
- Whilst the UK labour market continues to strengthen, **the City Region has outpaced national averages in terms of job creation of late**. This has helped to narrow the gap to the national average on key indicators including employment rate and the proportion who work full-time, but there is still some way to go to close this gap. On other indicators, the City Region economy appears to be at least maintaining pace with the UK.
- The fact that **inflation has abated, and wage growth has picked up slightly**, is encouraging and the Bank of England now has more scope to delay interest rate rises.
- The recent increase in business lending suggests **companies may be thinking of taking advantage of low borrowing costs to increase investment** as labour becomes more expensive and harder to come by.

These issues are explored in greater detail in the remainder of this document.

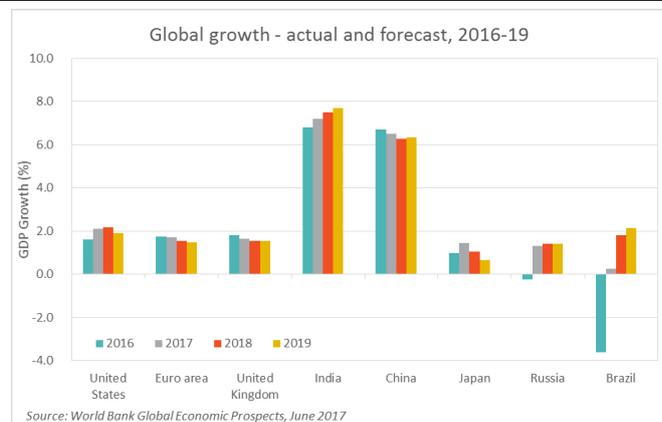
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Introduction

- This report presents the latest assessment of the Leeds City Region economy. It sets out the recent developments in the world's leading economies, along with trends and forecasts for global growth. It analyses the recent economic performance of the UK, before considering in more detail the latest developments in Leeds City Region.
- New data available includes updated global economic forecasts from the World Bank, whilst new official UK data is available on the labour market and international trade to June 2017.
- For Leeds City Region, data on business bank accounts is available up to July, along with the Chambers of Commerce Quarterly Economic Survey for Q2 and labour market data for Q1 2017.
- Initial headlines are also included from the Leeds City Region Business Survey. Whilst full results won't be available until further into the autumn, some early headlines provide valuable additional context.

Global context and forecasts

- Global activity is strengthening amid rising confidence and a pick up in trade, according to the latest Global Economic Prospects report from the World Bank. The World Bank expect global growth to reach 2.7% this year and 2.9% in each of the next two years.
- The World Bank's growth forecasts remain largely unchanged from their January projections, though the UK's outlook has been revised up slightly. They now expect growth of 1.7% this year (up from 1.2% in January), and 1.5% growth in 2017 and 2018 (both up from 1.3%). This still reflects a slowdown from growth of 1.8% in 2016.
- In the 2nd quarter of 2017, the US economy grew by 0.8%. This is up from growth of 0.3% in Q1 2017, thanks to higher personal consumption and increased export activity.
- The Eurozone recorded growth of 0.6% in Q2 2017, up slightly from 0.5% in Q1. This is the fastest growth rate seen in the single currency area since 2011, driven by solid growth in major economies such as Germany, France and Spain. Survey data suggests that Eurozone manufacturing growth continues to accelerate. Service sector expansion has plateaued somewhat, but remains robust.
- Japan's economy expanded by 1% in Q2, far outpacing expectations of 0.6% growth and up from 0.4% in Q1.
- Chinese growth also exceeded expectations in Q2, expanding at an annual pace of 6.9% thanks to strong growth in industrial activity. The world's 2nd largest economy continues to be supported by accessible credit conditions, and concerns remain about growing debt as the nation attempts to refocus growth on consumer activity.
- Output in India is expected to recover slightly in Q2, growing at an annualised rate of 6.6%, up from 6.1% in Q1. Activity is still subdued by the government's demonetisation policy in early 2017, but is expected to return to trend in the second half of the year.
- The strong performance of the European economy has helped strengthen the Euro, taking sterling to an eight year low against the single currency. The pound has performed better against the dollar, which has itself been under pressure amid concerns about tensions between the US and North Korea, as well as domestic political issues. However the pound/dollar rate remains well below the pre-referendum level, with concerns about Brexit talks weighing on sterling.
- Oil prices have remained relatively stable of late at around \$50 a barrel, with the recent OPEC cut in production being largely offset by rising output in nations not party to the agreement. Commodity prices more generally have also remained fairly stable so far this year, though prices for some foods have risen.



Global economy summary: Most major economies are experiencing solid growth with the Eurozone enjoying a prolonged period of expansion for the first time since the economic crisis. America has recovered from Q1's apparent blip, though there remain significant uncertainties in the US, the impact of which would be felt widely if realised.

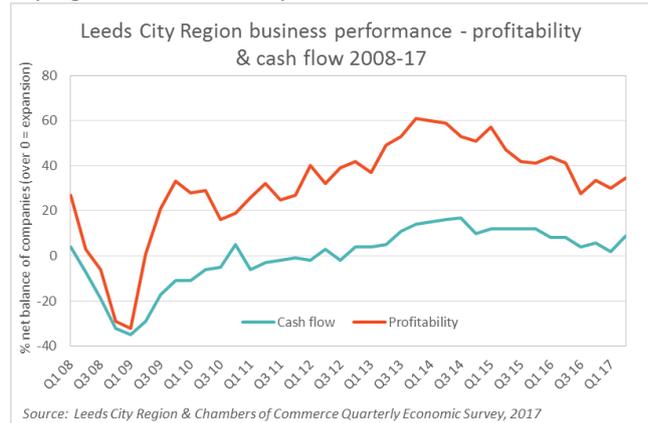
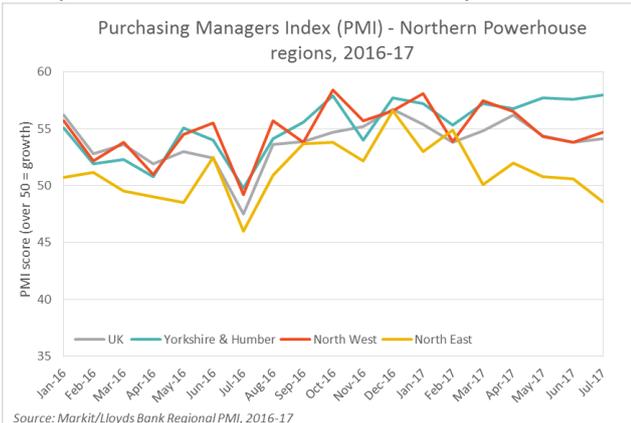
UK economic performance

Indicator	Latest position	Chart	Trend
Economic headlines	<p>The UK economy grew by 0.3% in Q2 2017, a slight increase from 0.2% in Q1. The service sector was again the main driver of growth, with output up by 0.5%. Manufacturing output decreased, however, (down 0.6%), as did construction (down 1.3%).</p> <p>The latest GDP data also confirms the slowdown in consumer spending. Household expenditure increased by just 0.1% in Q2, its lowest level for two and a half years. Business investment also slowed.</p>	<p>Source: Office for National Statistics, 2017</p>	
Confidence and sentiment	<p>Activity in both the manufacturing and service sectors accelerated in July, according to data from the Markit/CIPS PMI, with employment increasing. Optimism among service sector firms remains dampened by Brexit-related uncertainty, however.</p> <p>The construction sector also recorded growth, albeit at a reduced pace from June. Cost pressures remain a concern across the economy, but are most pronounced among construction firms with prices rising at their fastest pace for five years.</p>	<p>Source: Markit/CIPS PMIs, 2016-17</p>	
Labour market	<p>Total employment in the UK has risen past 32 million in June, up 125,000 compared to March 2017 and up 338,000 over the past year. The employment rate has surpassed 75% for the first time since records began. 381,000 more people are working full-time than a year ago, whilst the number working part-time has declined by 43,000.</p> <p>The unemployment rate has also reached a new record, falling to a low of 4.4% down from 4.9% a year ago. There are now 1.48 million people out of work, down 157,000 over the past year.</p>	<p>Source: Office for National Statistics, 2017</p>	
Trade and exports	<p>Retail sales volumes increased by 0.6% in the three months to July. This growth was driven by food sales, with all other categories seeing volumes fall between June and July.</p> <p>The UK's trade deficit (the difference between exports and imports) stood at £8.9bn in Q2 2017, broadly unchanged from Q1. Exports increased by £0.8bn over that time, with imports up £0.9bn.</p>	<p>Source: UK Trade, ONS 2017</p>	
Inflation and wages	<p>Inflation remained at 2.6% in July, unchanged from June but down slightly from May's 2.7% peak. Falling fuel costs helped keep prices in check despite increases in prices for food and clothing.</p> <p>Meanwhile regular pay growth has risen to 2.1% in June, having been falling since late 2016. Whilst real pay growth remains negative, the gap between wages and inflation has narrowed slightly.</p>	<p>Source: Office for National Statistics, 2017</p>	

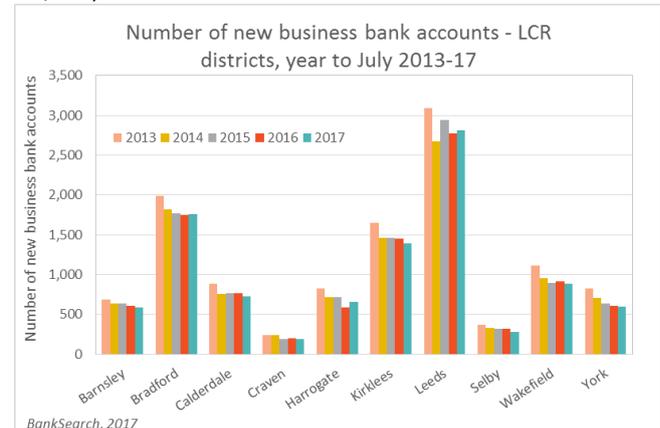
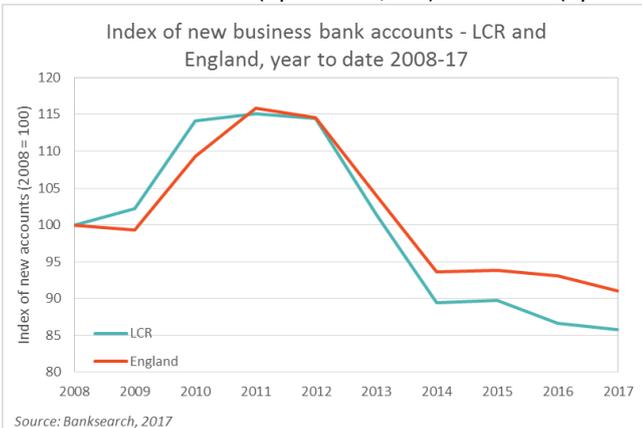
UK economy summary: UK growth remained below recent trends, and below other major economies in Q2. It also remains highly dependent on the service sector. With jobs, and particularly full-time jobs still being created a strong pace, the amount of slack in the UK labour market is lessening. This has helped to boost wage growth, though inflation remains relatively high.

Leeds City Region – Business Performance and Confidence

- Yorkshire & Humber is the fastest growing region of the UK in terms of business activity, according to the Markit/Lloyds Bank Regional PMI for July. The region's PMI of 58 is higher than any other region, overtaking the West Midlands since June (a reading of above 50 represents growth).
- The Quarterly Economic Survey (QES) with the Chambers of Commerce for Leeds City Region for Q2 2017 showed a rebound in service sector activity from Q1. Both domestic sales and export activity increased at a faster pace. The pace of growth slowed among manufacturers, but nonetheless remains in positive territory.
- This is reflected in business confidence, with the QES finding manufacturers' expectations of increasing turnover and profitability both falling to their lowest levels in almost four years. Conversely, service sector respondents were more optimistic on these measures than they had been in Q1, helping to sustain overall performance.



- 1,330 new business bank accounts were opened in Leeds City Region in July, a fall of 5% on June but broadly in line with 2016 activity, according to data from BankSearch. There have been 9,885 new accounts opened in LCR so far in 2017 – around 1% fewer than at the same point in 2016. The number of new accounts opened across England as whole so far this year is down 2.2% on 2016.
- Most districts of Leeds City Region have seen small falls in the numbers of new business bank accounts opened so far this year. However, Harrogate has seen the largest increase in percentage terms, up 11.6% on 2016 to 655 new accounts. Bradford (up 1% to 1,760) and Leeds (up 1.3% to 2,800) have seen more modest increases.



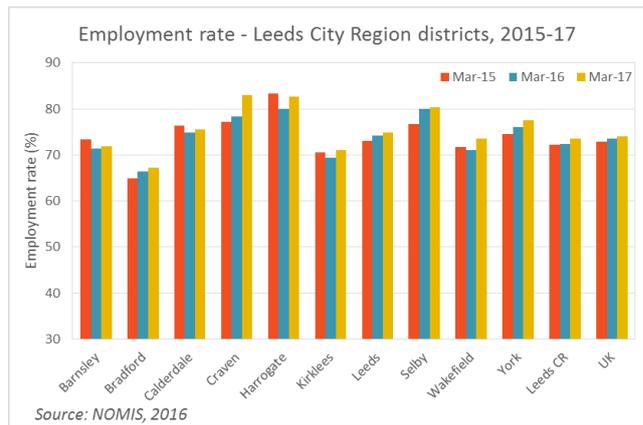
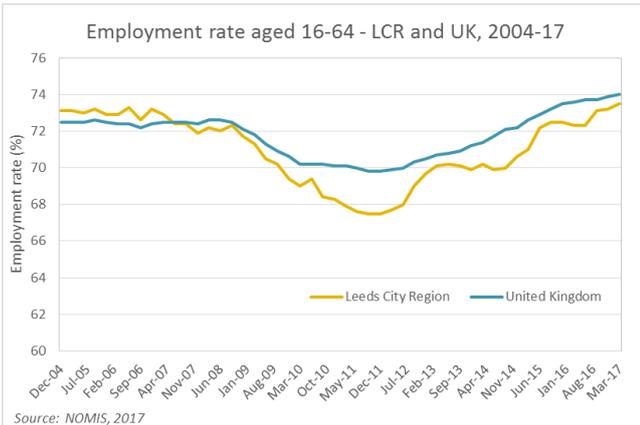
- Initial headlines from the Leeds City Region Business Survey suggest a small decline in business performance and confidence since the survey was last conducted in 2015. 38% of firms said overall performance has improved in the past 12 months, whilst 16% said it had worsened. This compares to 2015, when 46% said performance had improved, and 14% said it had deteriorated.
- Looking ahead, 34% expect to see improvement in performance of their business the next 12 months, down from 51% in 2015.

Summary: The regional PMI suggests that Yorkshire businesses are more optimistic than their counterparts elsewhere in the country, and particularly in the north. As with the national picture, service sector firms have seen their position strengthen of late, whilst the export-driven expansion of manufacturing seems to have slowed somewhat.

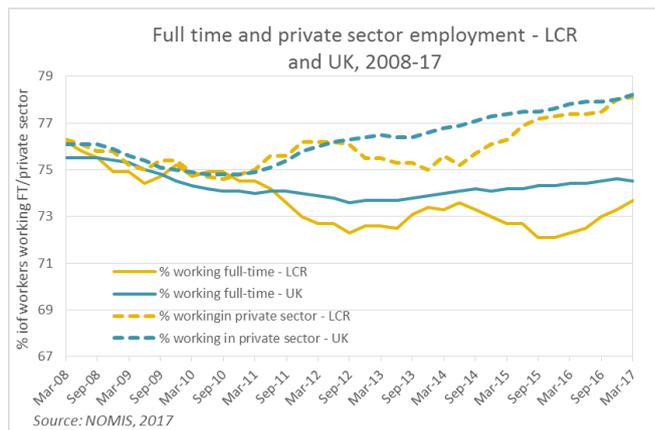


Leeds City Region – Labour Market

- There are 8,700 more people in work in Leeds City Region in Q1 2017 than in Q4 2016. There are 28,500 more people in work than there were a year ago. This 2.1% increase over the past year is higher than in any other northern LEP area, and is 2nd only to Greater Birmingham & Solihull among core city LEPs.
- The City Region’s employment rate has increased to 73.5%, compared to 73.1% in the previous quarter. The employment rate is now higher than at any point since 2004, though it remains slightly below the UK rate of 74.2%.
- At a district level, Kirklees, Craven, Calderdale, Leeds and Barnsley have seen increases in the employment rate in the past quarter. The employment rate in Leeds has moved above the national average this quarter, joining the North Yorkshire districts and Calderdale in outperforming the UK, though it should be noted that there can be significant fluctuation in these numbers.



- The number of people unemployed in Leeds City Region has fallen to 67,500, down 22,000 over the past year. The unemployment rate of 4.6% is below the comparable UK rate of 4.9%, though the unemployment rate remains above the UK average in Bradford, Kirklees, Wakefield and Barnsley.
- The employment rate for young people aged 16-24 in Leeds City Region currently stands at 53.5%, a level consistent with the position seen over the past 18 months. The UK rate has been similarly consistent and currently stands at 53.8%.



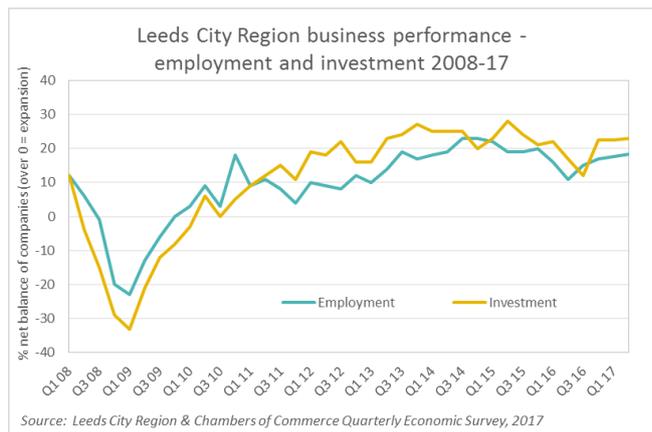
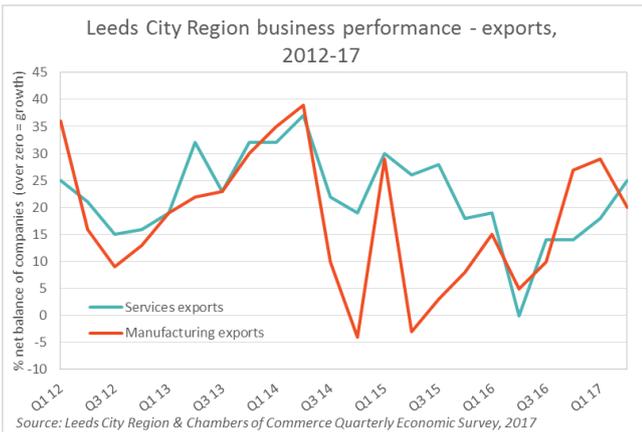
- Recent jobs growth has focused on full-time work, with the proportion of Leeds City Region residents who are working full-time increasing to 73.7% compared to 72.3% a year ago.
- Data from the QES suggests recent employment growth has continued in recent months. The survey found a net balance of 18% of firms had increased their headcount in Q2, a figure consistent with the previous two quarters.
- Initial findings from the Leeds City Region Business Survey suggest that 21% of firms increased their head count over the past 12 months, compared to 12% reporting a decline. Only 4% of firms expect staffing levels to fall over the next year.

Summary: Job creation in Leeds City Region has outpaced the UK average and that of other major cities, helping to narrow the employment rate gap to the UK. Survey data suggests this trend continues, with the majority of new posts being full-time positions. There do however remain substantial differences in performance across the City Region.

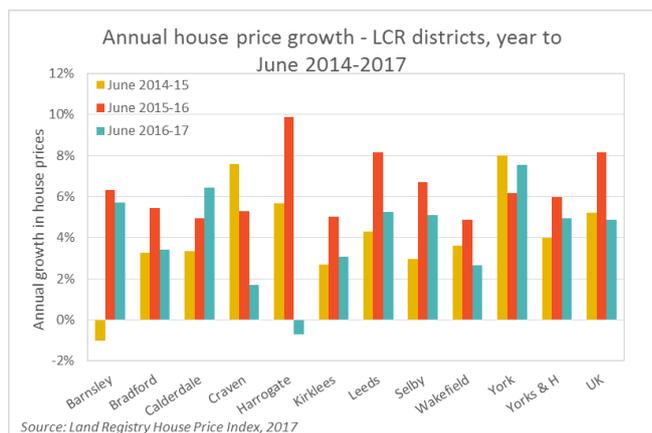
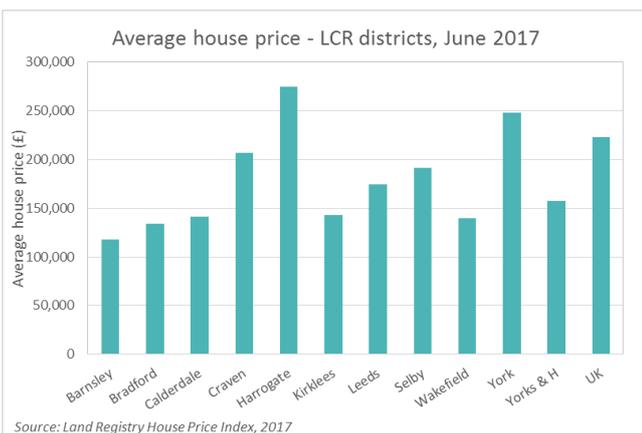


Leeds City Region – Trade, exports and investment

- Export activity continued to expand in Q2 2017 according to the Chambers' Quarterly Economic Survey, though there was a divergence in trends between service sector firms and their manufacturing counterparts.
- The service sector in Leeds City Region continued its recent recovery with the net balance of firms saying export sales had increased in the past quarter rising from 18% in Q1 2017 to 25% in Q2. This is the sector's strongest export performance since mid-2015.
- In contrast, the net balance among manufacturers declined from 29% in Q1 to 20% in Q2. This still signifies solid expansion, and compares favourably to recent performance prior to the previous two quarters. It does however suggest that the recent strong growth in export activity reported by manufacturers may have peaked.



- Both manufacturing and service sector firms continue to increase capital investments, with a net balance of 23% of firms increasing spend this quarter. This trend continues with regard to training investment among manufacturers, though service sector firms saw a small dip on this measure this quarter.
- Initial results from the Leeds City Region Business Survey suggest businesses continue to invest at a similar rate to when the survey was last carried out in 2015. 35% of firms have increased investment in the past year, whilst 8% have decreased investment. Marketing, training and ICT infrastructure were the main focuses of investment
- Similarly, the survey suggests that the proportion of firms engaged in exporting has also remained steady since 2015, at around 15%.



- House prices in Yorkshire & Humber grew by 4.9% between June 2016 and June 2017 – the same growth rate as the UK as a whole. Within Leeds City Region, York saw the fastest increase in average prices, up 7.6% on a year earlier. Calderdale (6.5%) and Barnsley (5.7%) also saw prices increase faster than the national average.
- Harrogate saw a small decline in prices over the past year, down 0.7%, though the district still has average prices substantially higher than elsewhere in the City Region, and higher than the UK as a whole.

Summary: Firms in Leeds City Region continue to report solid growth in export activity, though growth in the service sector has overtaken that in manufacturing on this measure. Despite suggestions elsewhere that uncertainty is inhibiting growth, survey data suggests companies in Leeds City Region continue to invest in their businesses and their people.



Conclusions and outlook

- In headline terms, the UK economy's continued expansion, with growth picking up slightly in Q2, is positive news. However, there are a number of apparent divergences from previous trends which offer some cause for concern.
- Internationally, the UK growth rate is now substantially below that in other major developed economies, such as the US, Japan and the Eurozone. This is in marked contrast to recent post-financial crisis trends. Whilst this could in part be attributed to the fact that the UK experienced stronger growth more quickly after the crisis, it also suggests that uncertainty stemming from Brexit negotiations is having an impact on UK GDP growth at a time when other major economies are cementing their post-recovery growth.
- Domestically, much of the official data points to a divergence between the performance of the service sector and the rest of the economy. Services was the only area of the UK economy to record GDP growth in Q2, with output declining among manufacturing, construction and the wider production industries. Whilst some survey data, such as the Markit/CIPS PMIs, suggests that manufacturing continues to expand, this has not been borne out in official statistics.
- Other survey data, including the Leeds City Region Quarterly Economic Survey, support the view that manufacturing activity is still expanding, although the pace of expansion appears to have peaked. Weaker export growth, which has been facilitated by the falling value of sterling, is a key factor in this slowdown.
- On wider measures the City Region economy appears to be at least maintaining pace with the UK, and in some cases closing the gap. Whilst the UK labour market continues to strengthen, the City Region has outpaced national averages in terms of job creation of late. This has helped to narrow the gap to the national average on key indicators including employment rate and the proportion who work full-time, but there is still some way to go to close this gap, and in some cases exceed it as was the case before the economic downturn.
- Other indicators such as new business formation also point to an economy slightly outpacing the nation as a whole, whilst surveys suggest the region's businesses are among the most positive in the country. All of this supports the view that the City Region's businesses are focused on the immediate task ahead of them, and are not too concerned about wider issues further down the line.
- More broadly, one of the more negative impacts of the depreciation of sterling, higher inflation, has eased a little of late. The relative stability of the pound against the dollar has contributed to this, as has more benign growth in commodity prices.
- At the same time, the pace of consumer lending has slowed, easing concerns that consumers were becoming overly reliant on cheap borrowing to maintain spending. Combined with the stabilising of inflation, this has lowered the pressure on the Bank of England to increase interest rates – a move which some were concerned would increase the strain on household budgets – in the short term at least.
- The Bank of England will also hope that the upturn in wages reported above persists and helps incomes to grow at a faster rate than inflation. At present, with inflation outstripping wage growth, real incomes are falling. This is in part fuelling the growth in consumer debt back close to levels seen before the 2008 crash. Stronger wage growth could mitigate the expansion of credit and provide the Bank with greater flexibility to respond to any change in economic circumstances in the coming years.
- Another period of strong performance in the labour market increases the likelihood of stronger wage growth. With the employment rate now above 75% for the first time, and with more people who want full-time able to find it, the pool of available labour is diminishing and workers' bargaining positions are strengthening. The recent fall in net migration will also help in this regard.
- Businesses could also look to increase investment in new equipment and technology to help improve productivity as labour becomes scarcer. Whilst official data suggests that there has been no upturn in business investment as yet, the Bank of England suggest that business borrowing has increased. This could be a prelude to increased investment, or could be a sign of firms insulating themselves from potential future interest rate rises.

This briefing has been produced by the Regional Economic Intelligence Unit. Any comments or queries can be addressed to reiu@westyorks-ca.gov.uk