West Yorkshire Combined Authority

Leeds City Region Enterprise Partnership

ECONOMIC AND BREXIT MONITOR: LEEDS CITY REGION, AUGUST 2019

Key points at glance

This report presents the latest assessment of the Leeds City Region economy. It sets out recent national and international developments along with trends and forecasts for global growth. It considers in more detail the latest developments in Leeds City Region and the implications for the economy as the UK approaches its exit from the European Union.

National and international headlines

- Global growth has been subdued in recent months as a range of geopolitical tensions show signs of taking effect on investment, trade and demand, increasing fears of recession.
- UK GDP decreased by 0.2% in Q2 2019, the first quarterly contraction since 2012. The tailing off of Brexit-related stockpiling was a factor – this contributed to stronger than predicted growth in Q1 which tailed off thereafter. The UK employment rate picture remains strong however.
- The Eurozone economy grew by 0.2% in Q2 2019, half the growth rate recorded in Q1. GDP in Germany contracted by 0.1% in Q2, whilst US growth also slowed as the impact of trade tensions with China took effect in America, Europe and Asia.
- Given these issues many forecasters have revised down their outlook with markets concerned that recession may be possible in some countries in the near term.
- The IMF revised down its forecasts for the UK for this year and next. Both are 0.2% lower than its January forecasts, and both are predicated on the UK securing an orderly exit from the EU.
- The election of a new Prime Minister in the UK and the shortening time frame has increased the likelihood of the country leaving the EU without a deal at the end of October, according to the Institute of Government.
- As such, many businesses will likely be revisiting the contingency plans they had in place in February/March.

Key City Region and local developments

- The City Region employment rate increased from 73.4% in Q4 2018 to 73.8% in Q1 2019 – the highest on record. There are 6,100 (0.4%) more people in work than the previous quarter – a faster increase than many other comparator LEPs.
- Unemployment in the City Region fell by 1,700 (2.9%) last quarter.
- Businesses reported a slowdown in domestic and export activity in the Q2 Quarterly Economic Survey with the Chambers of Commerce, with many businesses holding stock following the Brexit preparations in Q1.
- The service sector exports net balance turned negative for the first time in a decade, signalling declining activity according to the QES.
- Yorkshire & Humber businesses exported goods worth £4.46bn in Q1 2019, a fall of 4.8% from the record high of Q4 2018 though exports remain higher than a year ago.
- The value of goods imported into the region increased by 5.5% between Q4 2018 and Q1 2019, to £9.56bn. This increase is significantly in excess of the 0.4% increase in national imports.
- House prices in Yorkshire and Humber increased by 0.9% in the year to June 2019, in line with the increase seen nationally.
- Sales volumes declined by 2.5% in Yorkshire in June 2019, compared to the same period last year. This is a relatively small decline compared to other regions, with national sales volumes down 7.2%.

Brexit implications and conclusions

- The global economy appears to be slowing and the risk of recession rising for major economies, and markets appear to be increasingly expectant of a downturn. The added challenges of Brexit are also contributing to the slowdown in the UK.
- This slowdown is an added layer of uncertainty for those businesses who have forward provisioned for the initial Brexit deadline and who may face cash flow challenges, particularly when faced with a similar set of circumstances ahead of the UK's prospective departure date in October. Implementing similar plans for a second time may pose practical and financial challenges for many businesses.
- The devaluation of sterling coupled with businesses reporting increased demand for (and therefore cost of) warehousing space, would suggest that the cash flow challenges posed by a second round of no deal planning could potentially prove more complex than the last.

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

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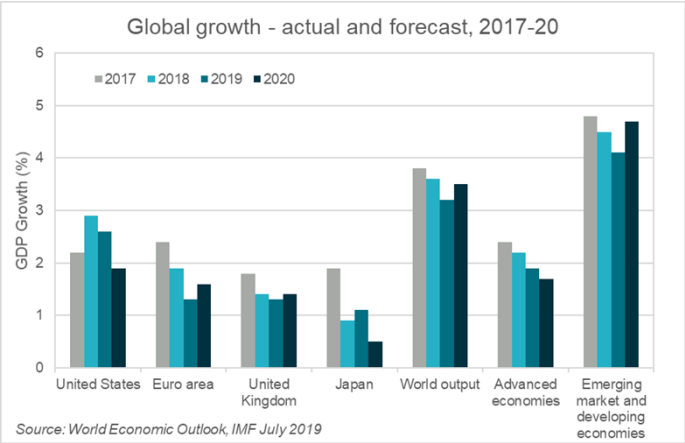
ECONOMIC AND BREXIT MONITOR: LEEDS CITY REGION, AUGUST 2019

Introduction

- This report presents the latest assessment of the Leeds City Region economy. It sets out recent global and national developments before considering in more detail the latest data for Leeds City Region and the implications for the economy as the UK approaches its exit from the European Union.
- New data available includes updated global economic forecasts from the IMF, whilst new official UK data is available on monthly GDP and the labour market for Q2 2019. There is also new official data on trade, inflation and retail activity and survey data on business sentiment.
- For Leeds City Region, the Quarterly Economic Survey with the Chambers of Commerce provides insight on business sentiment for Q2 2019. Labour market data from ONS for Q1 2019 and regional goods exports data from HMRC for the same period are also presented. Banksearch data on the number of new business bank accounts for Q2 2019 are also available.

Global economic and political developments

- Global growth has been subdued in recent months as a range of geopolitical tensions show signs of taking effect on investment, trade and demand, increasing fears of recession.
- The Eurozone economy grew by 0.2% in Q2 2019, half the growth rate recorded in Q1. GDP in Germany contracted by 0.1% in Q2, with the US-China trade war affecting its car industry.
- US growth also slowed. GDP increased by 0.5% in Q2, down from 0.8% in Q1. Again, the trade war is believed to be weighing on growth, though performance exceeded the expectations of many.



- China's economy faced similar issues, with growth slowing to annualised rate 6.2% in Q2, the slowest pace of growth since 1992. Chinese exports unexpectedly showed growth in July.
- The International Energy Agency has said growth in demand for oil has halved in the first five months of 2019, the weakest growth since 2008 as the global economy slides. Weaker demand has offset some of the upward pressures on oil prices from tensions in the Middle East seen recently, with prices falling from £67 per barrel in mid-July to £60 per barrel in mid-August.
- Given these issues many forecasters have revised down their outlook with markets concerned that recession may be possible in some countries including the UK and Germany where growth declined in Q2. In July, the IMF forecast global growth at 3.2 percent in 2019, picking up to 3.5 percent in 2020.
- Its forecasts for the UK were for growth of 1.3% and 1.4% this year and next respectively. Both are 0.2% lower than its January forecasts, and both are predicated on the UK securing an orderly exit from the EU.
- The election of a new Prime Minister in the UK and the shortening time frame has increased the likelihood of the country leaving the EU without a deal at the end of October, according to the Institute of Government.
- As such, many businesses will likely be revisiting the contingency plans they had in place in February/March. Rolls Royce has recently said it has spent £100m in planning for Brexit, but fears many in its supply chain are less well-prepared.

Global economy summary: A slowdown in activity across major economies is evident, with cyclical factors, trade wars and geopolitical tensions all contributing. This has led to a downward revision of growth trajectories and is raising fears about the threat of recession. The challenge is particularly acute in the UK as the ongoing Brexit uncertainty continues to weigh on growth.

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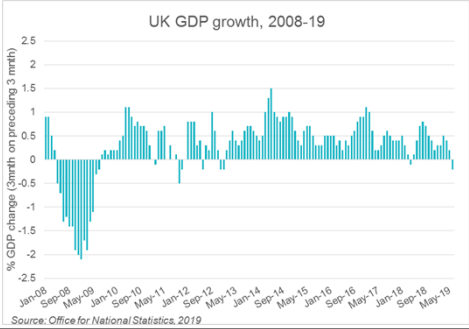
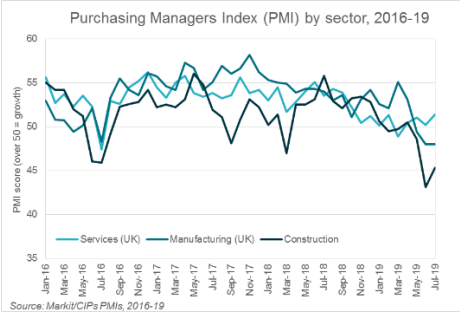
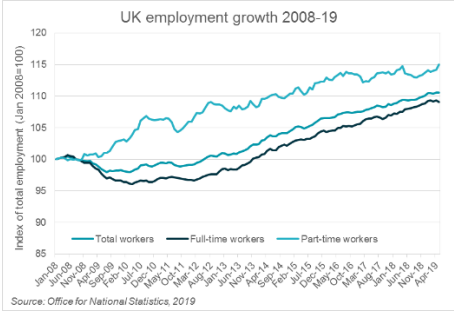
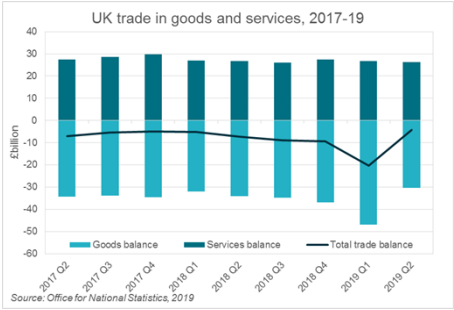
UK economic dashboard

Indicator	Latest position	Chart	Trend
Economic headlines	UK GDP decreased by 0.2% in Q2 2019, the first quarterly contraction since 2012. GDP fell by 0.5% in April, before recovering to some extent in May and June. The Brexit-related stockpiling was also a factor – this contributed to stronger than predicted growth in Q1 which tailed off thereafter. Over the quarter, the service sector was the only area of growth (+0.1%), with manufacturing (-2.3%) and construction (-1.3%) both seeing falls.		
Confidence and sentiment	Activity fell for the third consecutive month in the construction and manufacturing sectors in July, according to the IHS Markit / CIPS PMI surveys. A slowdown in new orders saw manufacturing production fall at the fastest pace for seven years. More positively, the service sector reported a slight improvement with modest expansion recorded for the 4th consecutive month but growth is still substantially below trend.		
Labour market	32.75 million people were in work in the three months to May 2019, up 28,000 on the preceding three months, according to ONS. The employment rate of 76% is down slightly from the peak of 76.1% - the first quarterly decrease in almost a year. Unemployment has fallen by 116,000 over the past year, to 1.29 million. The unemployment rate remains at a record low of 3.8%.		
Trade and exports	The volume of retail sales increased by 0.7% in Q2 2019 compared to Q1, a slowdown from an increase of 1.6% in the preceding quarter. The UK's trade deficit narrowed £16bn to £4.3bn in Q2 after widening in Q1. Total exports fell by 2.2% to £160.6bn, but imports fell more sharply – down 10.6% to £164.9bn.		
Inflation and wages	Inflation remains stable, in line with the government's target of 2% in May and June. Regular pay increased by 3.6% in the year to May 2019. Accounting for the effects of inflation, wages increased by 1.7%, up from 1.5% in April and the highest real terms increase since October 2015.		

Brexit implications: The first quarterly fall in GDP in seven years points to the fact that the UK economy is facing a challenging period. Whilst Brexit is undoubtedly a factor in this, with the unwinding of the stockpiling seen in Q1 weighing on growth along with the ongoing uncertainty over future arrangements, it is clearly not the only factor given the similar pattern in other nations. It does however mean that the UK is entering a critical period in Brexit decision-making with the global economic outlook appearing more challenging. Surveys suggest that businesses don't anticipate a sharp upturn in performance in Q3, though strong employment and wage growth remain positives.

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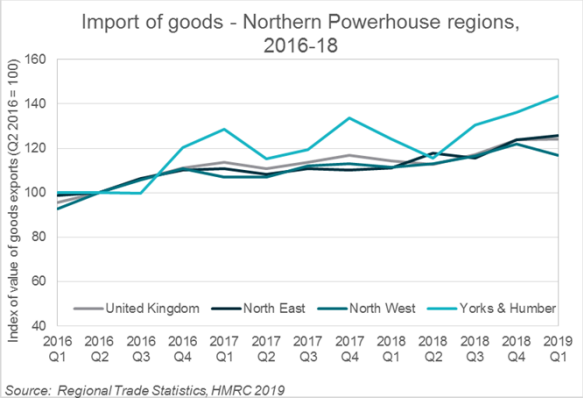
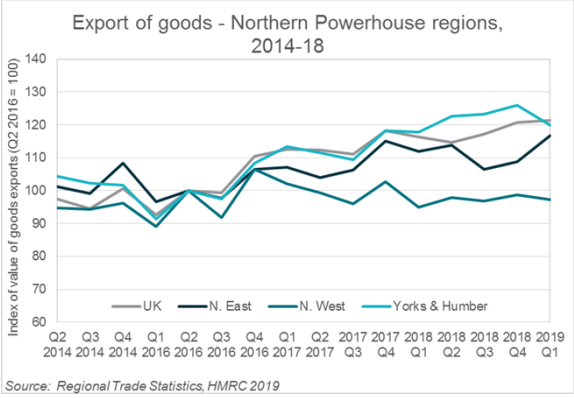
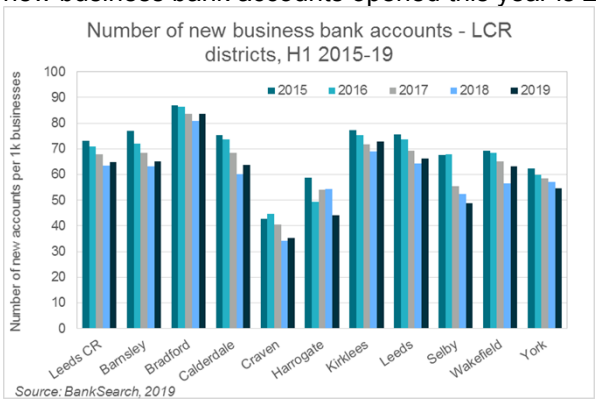
Leeds City Region – Business Performance and Trade

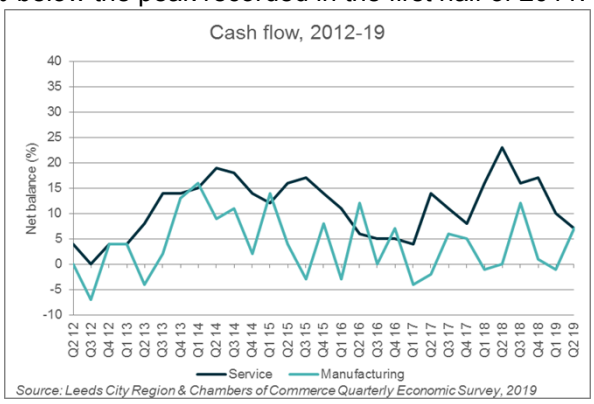
- Businesses reported a slowdown in domestic and export activity in the Q2 Quarterly Economic Survey with the Chambers of Commerce, with many businesses holding stock following the Brexit preparations in Q1.
- The service sector exports net balance turned negative for the first time in a decade at -3%, and though the net balance also fell among manufacturers, it remains close to its long run average at 20%.
- Business confidence continues to drop in the service sector in particular, with the fifth consecutive quarterly fall in profitability expectations. Cash flow shows a similar trajectory. Manufacturers are a little more positive, with an upturn in profitability expectations and an easing of cash flow concerns.
- Yorkshire & Humber businesses exported goods worth £4.46bn in Q1 2019, a fall of 4.8% from the record high of Q4 2018. Two other regions – the West Midlands and the South East – saw similar falls, though exports continued to increase elsewhere, most notably the North East (7.3%) and East Midlands (2.9%).
- The region's goods exports were 1.9% higher than in Q1 2018. Other than the West Midlands, which reported a 9.9% decline, this is the lowest growth rate of English regions over the past year.
- The value of goods imported into the region increased by 5.5% between Q4 2018 and Q1 2019, to £9.56bn. This increase is significantly in excess of the 0.4% increase in national imports. This appears to be driven by a 26% increase in imports from the EU, compared to a 5.5% increase nationally.
- Chemicals were the key driver of the increase at commodity level, with the value imported increasing by 107% to £2.59bn between Q4 2018 and Q1 2019. Whilst such trade in such commodities can be erratic, future data will have to be watched to assess whether this may reflect Brexit contingency planning or a similar one off event.





- 1,220 new business bank accounts were opened in June 2019 according to data from BankSearch, down from 1,380 in May but a similar level to June 2018.
- 8,150 new accounts have been opened so far in 2019, a 2% increase on the same period last year compared to a 0.4% increase nationally, which ranks Leeds City Region 14th out of 38 LEPs. The number of new business bank accounts opened this year is 28% below the peak recorded in the first half of 2011.





- Selby, York and Harrogate have seen falls in the number of new accounts opened so far this year. All other districts have seen increases, most notably Wakefield (9.8%), Calderdale (5.5%) and Kirklees (5.2%).
- Bradford has a higher rate of new business bank accounts opened, with 84 new accounts per 1,000 existing businesses so far this year compared to 65 across Leeds City Region and 67 in England.

Brexit implications: The issues facing the national economy in the first half of 2019 are replicated locally with businesses reporting falls in activity in Q2. Recent export growth also appears to be tapering, though imports increased markedly in Q1, perhaps reflecting businesses' preparations prior to the original Brexit deadline.

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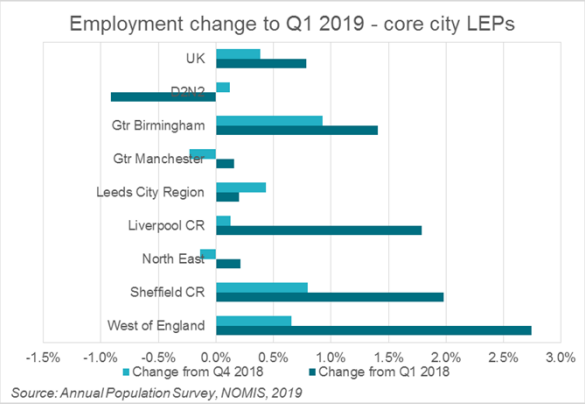
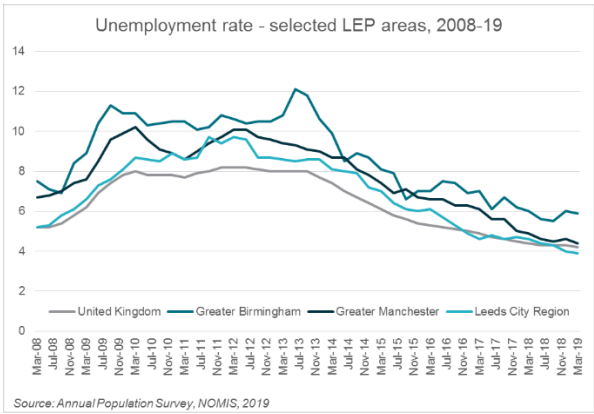
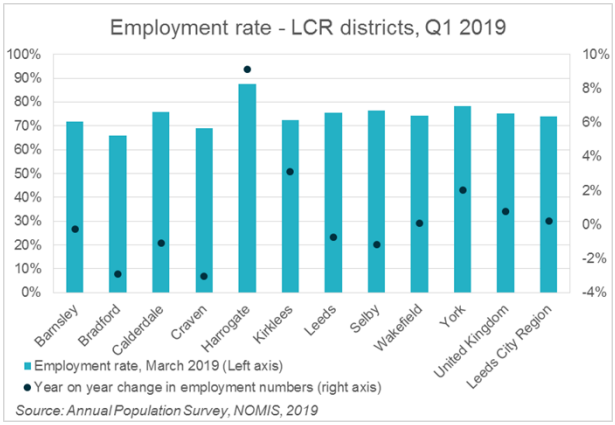
Leeds City Region – Labour Market

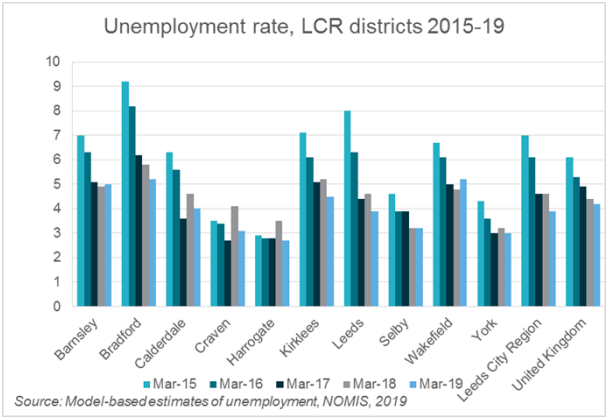
- Employment in Leeds City Region increased by 6,100 (0.4%) between Q4 2018 and Q1 2019. More than 1.41 million people are in work in the City Region, 2,800 (0.2%) more than a year ago. Local employment growth has exceeded that of Greater Manchester, Liverpool City Region, D2N2 and the North East LEPs over the past quarter. Whilst a number of core city LEPs have seen stronger growth over the past year, the City Region employment rate remains higher than most of these comparators.
- The City Region employment rate increased from 73.4% in Q4 2018 to 73.8% in Q1 2019 – the highest on record. It remains below the UK rate of 75.2% but among core city LEPs only West of England has a significantly higher employment rate (79.5%).
- Unemployment in the City Region fell by 1,700 (2.9%) last quarter. There are now 57,600 people unemployed, taking the unemployment rate to a joint record low of 3.9%. The unemployment rate is below the UK level of 4.2%. Only West of England and Liverpool City Region have lower rates (both 3.5%).
- 78.1% of Leeds City Region residents in work are employed in the private sector, a joint record high and up from 75% five years ago. This is comparable to the 78.5% nationally, and second only to Greater Birmingham among core city LEPs (80.5%).





- Whilst it is important to note that data at district level is based on relatively small sample sizes and is therefore prone to fluctuation, employment growth was most notable in Harrogate, Kirklees and Leeds this quarter, with these districts seeing around 2,500 more residents in work each. Calderdale and York both saw employment fall by around 1,500.
- Half of the districts in Leeds City Region have employment rates in excess of the UK rate of 75.2% - Calderdale (75.7%), Harrogate (87.4%), Leeds (75.5%), Selby (76.5%) and York (78.4%).





- The unemployment rate fell in 7 of the 10 City Region districts between Q4 2018 and Q1 2019, according to modelled estimates from NOMIS. It was largely unchanged in Barnsley and Selby, with only Wakefield seeing an increase (from 4.8% to 5.2%).
- With employment rates at a record high, businesses in the QES report challenges finding appropriately skilled staff. 44% of service sector companies, 61% of manufacturers and 80% of construction firms reported such difficulties in Q2.

Brexit implications: Recent growth in employment numbers has seen the Leeds City Region employment rate reach a new record high. This positive trend reflects the national labour market, though it appears to be exacerbating the recruitment challenges facing many employers.

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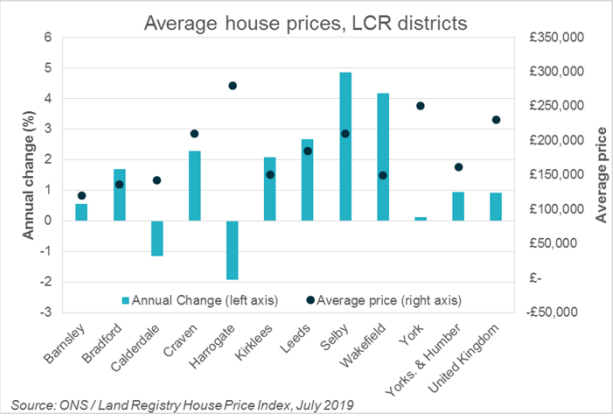
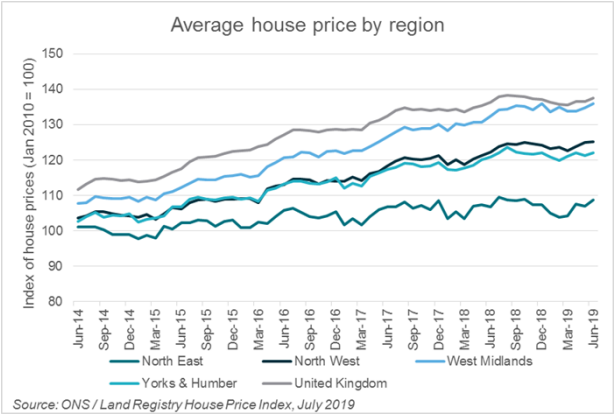
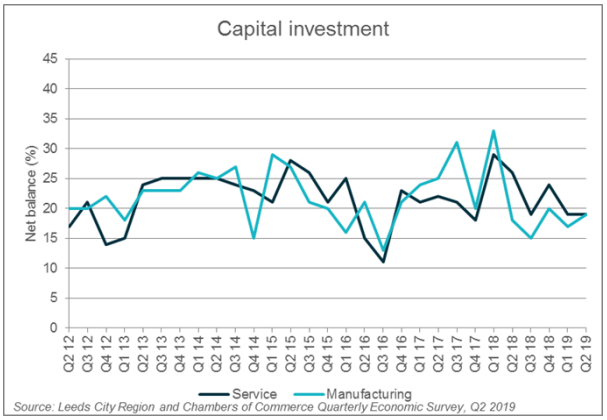
Leeds City Region – Housing, Property and Investment

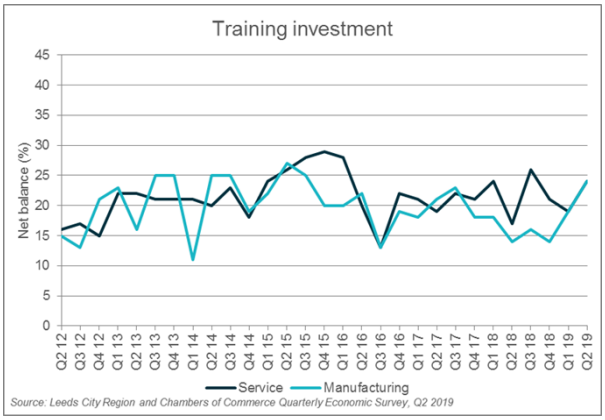
- House prices in Yorkshire and Humber increased by 0.9% in the year to June 2019, in line with the increase seen nationally. The average price also increased by 0.6% between May and June, reflecting the relatively static picture in the year up to that point. The average house price in the region is £162,000.
- Whilst local house price growth has followed national trends, other regions in the North have seen a more rapid increase over the past year, with North West prices up 2.4% to £164,000, and North East prices up 1.8$ to £130,300. The West Midlands has also seen a relatively high increase, up 2.6% to £199,000. All of these areas remain substantially more affordable than nationally, where prices average £230,300.
- Sales volumes declined by 2.5% in Yorkshire in June 2019, compared to the same period last year. This is a relatively small decline compared to other regions, with national sales volumes down 7.2%. Only West Midlands saw a smaller fall in activity than Yorkshire & Humber.





- Selby and Wakefield have seen the strongest increase in prices in the past year, up by 4.9% and 4.2% respectively. In contrast, prices have declined in Calderdale (-1.2%) and Harrogate (-1.9%).
- Most districts of the City Region remain substantially more affordable than the UK as a whole. Prices in most West Yorkshire districts are 60-65% of the UK average, except Leeds where prices are 80% of UK levels. North Yorkshire districts tend to be more expensive to buy, with prices higher than the national average in York (9% above UK levels) and Harrogate (22%).
- Average office rents in West Yorkshire increased to £24.86 per square foot in July according to data from EG Radius, up from £20 in May and £16 at the start of the year.





- Manufacturers reported an increase in investment in Q2 2019 across both capital and training according to the QES. The service sector also reported an upturn in investment in training this quarter, with the net balance at 24% and close to the long run average.
- Service investment in capital projects remained flatter however, with the net balance at 19% for both services and manufacturing – some way below the levels achieved in early 2017.

Brexit implications: As with last quarter, businesses remain hesitant to commit to capital investments though have at least appeared more willing to invest in training this quarter. Households remain similarly hesitant with further Brexit uncertainty on the horizon, though the impact on activity in the Yorkshire housing market is relatively low compared to other regions.

Conclusions and outlook

- The global economy appears to be slowing and the risk of recession rising for major economies, and markets appear to be increasingly expectant of a downturn. Germany and the UK appear to be at the forefront of concerns, given the two nations already saw output decline in Q2.

- Germany's challenges are reflective of those faced by other major economies, principally the impacts of a tariffs and trade tensions between the US and China affecting manufacturers and the automotive sector in particular, coupled with a cyclical weakening of demand.

- Whilst these challenges are also present in the UK, as evidenced by the ongoing weakening of its own automotive sector, the added challenges of Brexit are also contributing to the slowdown here. Whilst the pre-Brexit stockpiling may have helped to inflate activity in the first quarter of the year, the unwinding of the inventories built up through that process may have accelerated the slowdown seen in Q2.

- Although this means that the impact on growth may in some senses be seen as artificial, it is likely to pose real challenges to businesses faced with an excess of stock. Those who have forward provisioned for the initial Brexit deadline may face cash flow challenges, particularly when faced with a similar set of circumstances ahead of the UK's prospective departure date in October. Implementing similar plans for a second time may pose practical and financial challenges for many businesses.

- Anecdotal evidence from businesses in Leeds City Region confirms these challenges, particularly when aligned with a further devaluing of sterling which is feeding through into higher import prices. Coupled with businesses reporting increased demand for (and therefore cost of) warehousing space, this would suggest that the cash flow challenges posed by a second round of no deal planning could potentially prove more complex than the last.

- Other data point to a slightly more subdued level of activity in the local and regional economy this quarter, though in most cases performance remains at a similar or higher level than a year ago. This is true of both new business bank account activity, which has seen modest growth over the past year, and activity in the housing market which, although seeing a slight fall, has held up more strongly than in most other regions.

- Export growth has tailed off slightly, but the value of goods exported remains substantially above pre-referendum levels. Import patterns have been somewhat more erratic of late, though have been on an upward trend for Yorkshire & Humber for the past year.

- The spike seen in imports in chemicals and from the EU may or may not prove to be a one off event, possibly linked to Brexit preparations. It does however serve to further highlight the importance of the single market area to businesses in one of the region's key international trade strengths.

- The labour market continues to perform strongly, both locally and nationally with the employment rate reaching a new record high in Q1 2019 in Leeds City Region, and the unemployment rate reaching a joint-record low.

- This is perhaps related to the upturn in training investment shown in the Quarterly Economic Survey last quarter – as workers become harder to access, businesses can increasingly look to upskilling their own workforce. Whilst this clearly helps the business to meet its own skills needs, it is also of benefit to the individual and their own future career progression, which should be welcomed.

This briefing has been produced by the West Yorkshire Combined Authority Research & Intelligence team. Any comments or queries can be addressed to research@westyorks-ca.gov.uk