

ECONOMIC UPDATE: LEEDS CITY REGION, NOVEMBER 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

- **The recent upturn in global economic activity continues**, with most major economies seeing strong growth in the first half of 2017 compared to previous years.
- **UK GDP increased by 0.4% in Q3 2017, expanding at a similar rate to Q2.** Growth so far this year is around half of the average seen in the preceding three years. However, manufacturing returned to growth with output increasing by 1%.
- **The UK labour market remains strong.** The employment rate has now reached 75.1%, whilst the unemployment rate has fallen to 4.3%.
- The broad upturn in activity so far this year is reflected in the IMF's latest World Economic Outlook, which has **revised up its forecast for global growth** by 0.1% to 3.6% in 2017, an acceleration from growth of 3.2% last year.
- However, **the IMF expect UK growth to slow** from 1.8% in 2016 to 1.7% this year and 1.5% in 2018.
- **Inflation in the UK increased to 3% in September**, up from 2.9% in August to its highest level since 2012.
- Meanwhile **wage growth remains relatively low**, with average weekly earnings increasing by 2.1% in August. As such, pay fell by 0.4% in real terms (adjusted for inflation) between August 2016 and August 2017.

Key City Region and local developments

- The Quarterly Economic Survey (QES) with the Chambers of Commerce for Leeds City Region for Q3 2017 found **strong growth for both manufacturers and service sector firms**, on the back of solid expansion both domestically and in exports.
- Almost half of all service sector firms and a third of manufacturers **now expect profitability to increase over the next year**, both up 10 points on the previous quarter. Despite this, **concerns over cost pressures and exchange rates remain elevated.**
- Goods to the value of £8.35bn have been exported from Yorkshire & Humber in the first half of 2017, **an increase in exports of 17.5% on the same period last year.** This broadly mirrors national performance.
- Goods exports have averaged £4bn per quarter in Yorkshire & Humber in the year since the Brexit vote compared to an average of £3.5bn in the year preceding the referendum, suggesting **the fall in sterling post-EU referendum has helped to increase the value of exports.**
- There are 26,000 more LCR residents in work in Q2 2017 than a year earlier. **The employment rate stands at 73.4%, broadly unchanged** from the 73.5% seen in Q1.
- So far in 2017, 12,600 new business bank accounts have been opened in LCR, consistent with 2016. 2.6% fewer accounts have opened across England over that period. **Only 5 LEPs have seen faster growth in new business bank accounts than LCR so far this year.**

Key conclusions and outlook

- Globally, **the recent solid performance in major economies has continued with the US and Eurozone both posting strong growth in Q3.** In both cases, there is sufficient confidence that the long awaited recovery has enough momentum to begin planning to remove the stimulus programme in place since the recession.
- Whilst the moves towards the normalisation of monetary policy has been welcomed by many, others including the **IMF have voiced concerns that there remain a number of underlying issues in the global economy**, and have urged a cautious path with regard to withdrawing stimulus.
- Whilst **subdued wage growth is an issue across the developed world**, the low inflation problems seen in other major economies is not a problem shared by the UK, where inflation is running well ahead of the government's target.
- Despite these issues and increasing uncertainty related to Brexit, survey data suggests that **Leeds City Region businesses growing their operations and are optimistic about the year ahead.**
- Encouragingly, **LCR businesses seem increasingly willing to explore new overseas markets beyond the EU** in order to achieve their growth ambitions.

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

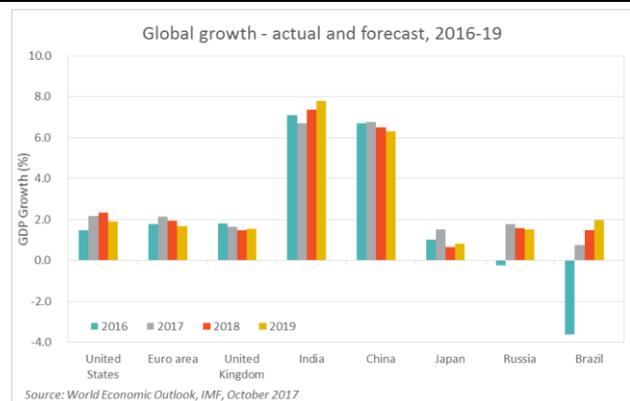
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Introduction

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- New data available includes updated global economic forecasts from the IMF, whilst new official UK data is available on GDP and international trade for Q3, and labour market data to August 2017.
- For Leeds City Region, labour market and export data is available for Q2 2017, along with the Chambers of Commerce Quarterly Economic Survey and data on new business bank accounts for Q3. Data is also presented comparing the 2017 Leeds City Region Business Survey with the last iteration of that survey in 2015.

Global context and forecasts

- The recent upturn in global economic activity continues, with most major economies seeing strong growth in the first half of 2017 compared to previous years.
- The broad upturn in activity so far this year is reflected in the IMF's latest World Economic Outlook, which has revised up its forecast for global growth by 0.1% to 3.6% in 2017, an acceleration from growth of 3.2% last year.
- The IMF expect UK growth to slow from 1.8% in 2016 to 1.7% this year and 1.5% in 2018, a slight downward revision from previous forecasts due to lower than anticipated growth in the first half of this year.
- However, the IMF also note that substantial challenges remain, particularly in advanced economies, that need to be addressed before central banks can begin to fully unwind accommodative policies such as quantitative easing.
- The Eurozone again reported strong expansion, with output increasing by 0.6% in Q3 and remaining close to the six year high of 0.7% seen in Q2. The single currency area has also seen unemployment fall to 8.9%, its lowest level since 2009.
- In the US, the economy grew by 0.7% in Q3, again close to the 0.8% seen in Q2. Strong consumer spending and business investment helped to sustain growth in spite of the widespread disruption caused by recent hurricanes.
- The Chinese economy also maintained strong growth, expanding at an annual pace of 6.8% between Q3 2016 and Q3 2017. Among the key drivers of growth were real estate spending and government financed infrastructure investment whilst private business investment struggled to keep pace, reawakening concerns about China's attempts to transition to a more service led economy whilst avoiding a house price bubble.
- The outlook for India continues to be dampened by the impact of changes to currency and the introduction of a new nationwide sales tax. Elsewhere, relatively subdued commodity prices continue to pose an issue for emerging nations reliant on the export of raw materials, though the upswing in global activity in major economies should help to sustain demand.
- Oil prices have hit a two year high recently of \$62 per barrel having averaged around \$50 a barrel in the first half of the year. Expectations that OPEC will maintain its recent cut in production, combined with political upheaval in oil producing states such as Iraq and Saudi Arabia, have pushed prices higher though this analysts expect the spike to be short-lived.
- Whilst commodity prices more generally saw modest growth in the early months of 2017, this has since tailed off with prices falling around 10% between February and June.



Global economy summary: The global recovery is becoming more sustained, prompting attention to turn towards removing some of the stimulus measures propping up the economy since 2008. There remain concerns about the underlying health of advanced economies however, with low inflation and wage growth a key issue.

UK economic performance

Indicator	Latest position	Chart	Trend
Economic headlines	<p>UK GDP increased by 0.4% in Q3 2017, expanding at a similar rate to the 0.3% growth seen in Q2. Growth so far in 2017 has averaged around half the 0.6% quarterly average seen in the preceding three years and is now below that of other G7 nations.</p> <p>Whilst this in part reflects a pickup in growth elsewhere, it also appears that factors such as Brexit-related uncertainty may be inhibiting UK growth.</p>	<p>UK GDP growth - 2007-17</p> <p>Source: Office for National Statistics, 2017</p>	
Confidence and sentiment	<p>Subdued activity in the construction sector is confirmed by the latest Markit/CIPS PMI, which found growth in housebuilding was largely offset by weaker civil and commercial activity.</p> <p>More positively, service sector firms and manufacturers reported more robust growth, with the former seeing the fastest expansion in six months. Optimism for the year ahead remains relatively weak, however.</p>	<p>Purchasing Managers Index (PMI) by sector, 2016-17</p> <p>Source: Markit/CIPS PMIs, 2016-17</p>	
Labour market	<p>There were 32.1 million people in work in the UK in the three months to August, up 94,000 on three months earlier and 338,000 on August 2016. The employment rate has now reached 75.1%, up from 74.9% in May. Unemployment also continues to fall, with the number down 215,000 over the past year to 1.44 million, an unemployment rate of 4.3%.</p> <p>Employment growth is being driven by an increase in full-time positions, with the number working full-time up by 346,000 in the past year and the number working part-time down 29,000.</p>	<p>UK employment growth 2008-17</p> <p>Source: Office for National Statistics, 2017</p>	
Trade and exports	<p>The volume of retail sales declined by 0.8% between August and September in a further sign that consumer activity is slowing. The more stable three month average still shows growth of 0.6%, however.</p> <p>The UK's trade deficit (the difference between exports and imports) increased from £6.5bn in the three months to May to £9.5bn in the three months to September. Imports increased by £3.2bn in the last quarter, whilst exports fell slightly.</p>	<p>UK balance of trade - 2007-17</p> <p>Source: UK Trade, ONS 2017</p>	
Inflation and wages	<p>Inflation in the UK increased to 3% in September, up from 2.9% in August to its highest level since 2012. Food & drink, household goods and transport costs were key drivers of inflation. The fall in sterling post-referendum is a key driver behind higher inflation in the UK than in other major economies.</p> <p>Wage growth remains relatively low, with average weekly earnings increasing by 2.1% in August. As such, pay fell by 0.4% in real terms (adjusted for inflation) between August 2016 and August 2017.</p>	<p>Wage growth and inflation, 2008-17</p> <p>Source: Office for National Statistics, 2017</p>	

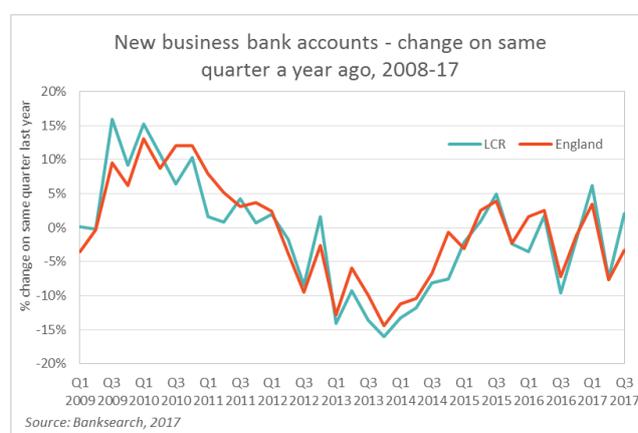
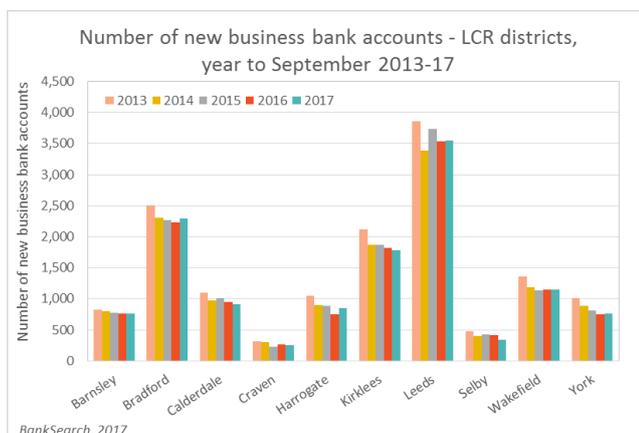
UK economy summary: The UK economy has continued at a similar pace to recent months, though growth remains a little below that of other major economies and below longer term trends. More positively, the manufacturing sector reported stronger growth and employment remains at record highs.

Leeds City Region – Business Performance and Confidence

- Manufacturers in Leeds City Region recorded strong performance in Q3 2017 according to the Quarterly Economic Survey (QES) with the Chambers of Commerce. The net balance of firms reporting increased domestic sales rose to 28%, up from 9% in Q2. This is consistent with official national data for Q3, which showed strong expansion in the manufacturing sector. Export sales also improved, expanding at their fastest pace since the recession.
- Service sector firms also reported positive performance in Q3. Whilst the number of firms reporting domestic sales growth slowed a little from its peak in Q2, it remains higher than at any point since early 2016 whilst export activity in the service sector increased back to its highest point since early 2015.
- This upturn in activity has resulted in increased business confidence. Almost half of all service sector firms and a third of manufacturers now expect profitability to increase over the next year, both up 10 points on the previous quarter. Despite this, concerns over cost pressures and exchange rates remain elevated.
- Manufacturers have also reported an increase in capital investment in Q3, with 31% of firms increasing investment.
- The LCR Business Survey supports the view that business investment has generally held up since 2015. A net balance of 27% said investment had increased in the past year, the same as in 2015. Access to finance remains the biggest barrier to growth according to the latest business survey, though the proportion citing this as an issue has fallen from 17% in 2015 to 12% in 2017.



- 4,100 new business bank accounts were opened in Leeds City Region in Q3 2017, a figure broadly consistent with Q2. The number of account openings is up 2% from Q2 2016, compared to a 3.5% fall nationally over the same period.
- So far in 2017, 12,600 new accounts have been opened in LCR, the same number as in the first three quarters of 2016. 2.6% fewer accounts have opened across England over that period. Only 5 LEPs have seen faster expansion in activity on this measure than Leeds City Region so far this year.
- Harrogate has seen a 12% increase in account openings so far this year, though this partly reflects the fact that account openings in the district in 2016 were lower than in other recent years. Bradford (+2.5%) and York (+2%) have also seen increases in account openings so far this year.

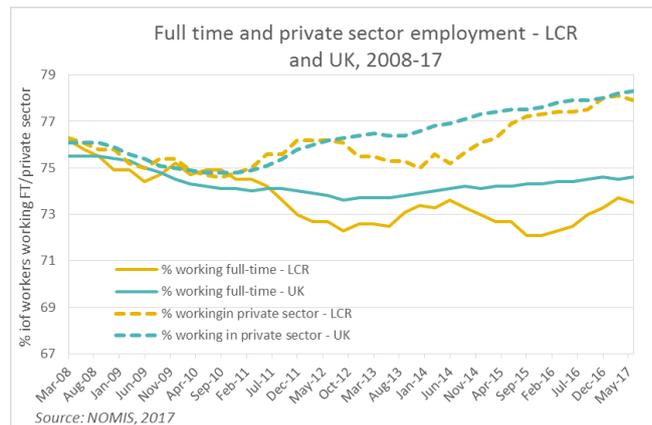
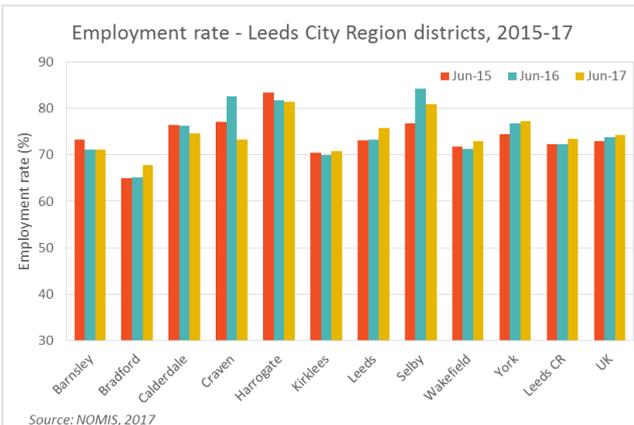


Summary: Business confidence rebounded in Q3 on the back of stronger domestic demand and export performance. Stronger data on new business formation compared to most other LEP areas, along with a recovery in manufacturers' investment plans, also reflect a degree of optimism in the local economy.

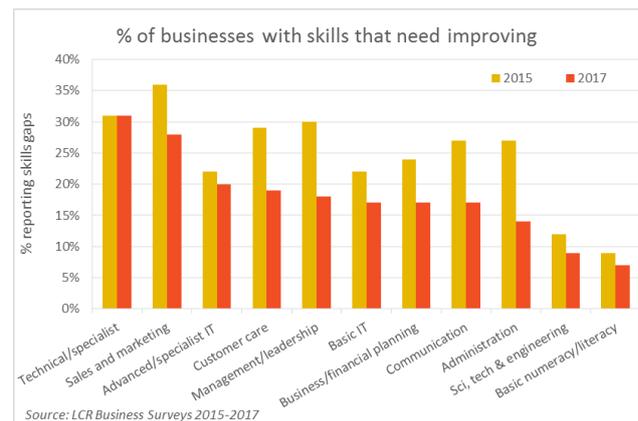
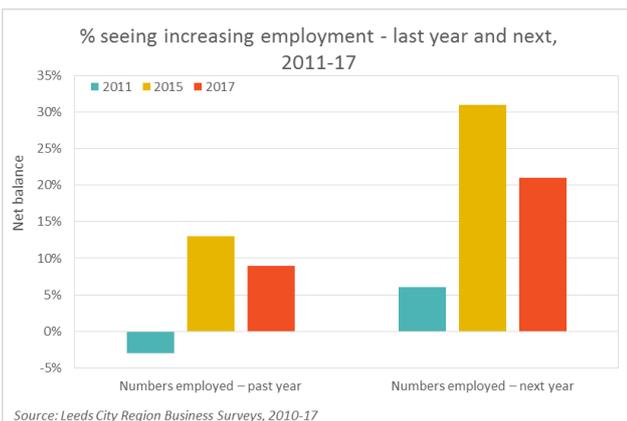


Leeds City Region – Labour Market

- There are 1.4 million LCR residents in work as of Q2 2017, 26,000 more than a year earlier though largely unchanged from Q1. The employment rate stands at 73.4%, broadly unchanged from the 73.5% seen in Q1 and slightly below the comparable national rate of 74.2%. It is also still above the pre-recession peak of 73.3%.
- Employment growth over the past year has been fastest in Bradford and Leeds, both of which have seen job numbers increase by 4% since Q2 2016, in excess of the 1.1% growth seen nationally. The employment rate is highest in Harrogate (81.4%) and Selby (80.9%), though it is above the national average in all of the North Yorkshire districts in LCR as well as Calderdale and Leeds.



- Unemployment increased slightly in LCR over the past three months, rising from 67,500 in Q1 2017 to 71,000 in Q2. Most districts saw relatively little change in unemployment levels, though increases of around 2,000 in Leeds and Wakefield offset a 1,300 fall in Bradford. The City Region’s unemployment rate of 4.8% is slightly higher than the 4.6% seen in Q1 but is down from 5.7% a year ago. The LCR rate remains similar to the comparable UK rate of 4.7%.
- The Leeds City Region Business Survey 2017 shows that more businesses expect their headcount in the coming year to increase than decrease. A net balance of 21% of firms said they expect employment in their organisation to increase over the next twelve months with a quarter of firms expecting employment to increase and just 4% expecting to see a decline (the remaining 71% either expected no change or were unsure).
- The proportion of firms expecting to see their headcount increase next year has fallen from 31% when the survey was last carried out in 2015 to 21% in 2017. This perhaps reflects the greater uncertainty in the economic climate, though optimism is still substantially higher than in the 2011 survey.



- The number of firms reporting that they have struggled to fill vacancies in the past year has remained consistent since 2015, at 20%. Technical/specialist or job-specific skills are by far the hardest to come by, with 63% of firms with hard to fill vacancies saying they had struggled to find suitable candidates with such skills.
- Technical/specialist skills are also the area where most businesses say they need to improve in the 12 months, with 31% of all firms saying they would need to improve their skills in this area to meet the organisation’s needs. Sales/marketing (28%) and digital skills (20%) were also frequently identified as needing improvement.

Summary: Though overall employment levels were largely unchanged in Q2, LCR businesses continue to create jobs and expect this trend to continue into 2018. They continue to face challenges in recruiting staff with the right technical and specialist skills, with these problems particularly acute in certain sectors.

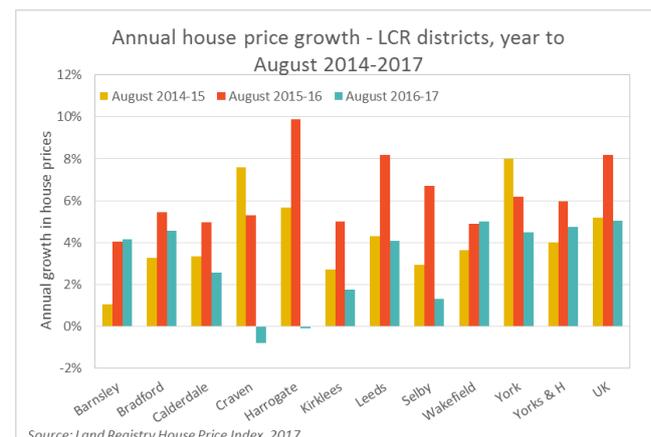
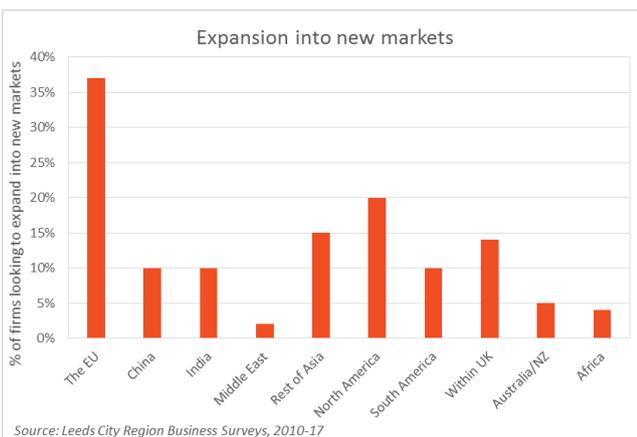


Leeds City Region – Trade, exports and investment

- Yorkshire & Humber businesses exported goods worth £4.2bn in Q2 2017, down slightly from £4.1bn in Q1 but higher than the £3.7bn exported in Q2 2016.
- Goods to the value of £8.35bn have been exported from Yorkshire & Humber in the first half of 2017, an increase of 17.5% on the same period last year. This broadly mirrors national performance, but growth is substantially higher than in other Northern regions, with North West exports up 6.8% and North East up 7.6%.
- The value of goods exported to the EU is 21% higher in the first half of 2017 than it was in the corresponding period last year. As such, the EU remains the primary destination for goods exported from the region, accounting for £4.8bn (58%) of value in the first half of 2017, up from £4bn (56%) in 2016.
- Looking over a longer period, goods exports have averaged £4bn per quarter in Yorkshire & Humber in the year since the Brexit vote compared to an average of £3.5bn in the year preceding the referendum. This pattern is repeated nationwide, suggesting the fall in sterling post-EU referendum has helped to increase the value of UK exports.
- This reflects the broader trend of increasing exports since the Brexit referendum, with the EU seeing an increase of 16.7% in goods exports from Yorkshire & Humber in the year since the referendum compared to the preceding year. Total goods exports from the region are 12.9% higher over that period, suggesting that whilst all markets (excluding Eastern Europe) have seen increased trade with Yorkshire & Humber over the past year the EU, as the nation's major trading partner, has seen the most significant uplift in trade.



- Looking ahead, 1 in 9 firms told the LCR Business Survey that they are looking at expanding into new markets in the year ahead. Of these, 37% were targeting the EU – more than any other market. The US is next most commonly targeted market, mentioned by 20% of firms, with China, India and other Asian markets also featuring prominently.



- House prices in Yorkshire & Humber grew by 4.8% between August 2016 and August 2017 – similar to the 5% increase seen nationally. House price growth is below the 6% seen in the region in the year to August 2016 but above the 4% seen in the same period in 2015.
- In commercial property, office vacancy rates in West Yorkshire have averaged around 7.8% so far in 2017, a similar level 2015 having increased slightly last year thanks to an increase in supply. The amount of floor space leased so far this year has exceeded the floor space brought to market.

Summary: The region has seen strong growth in goods exports in the first half of 2017 compared to last year. Businesses seem to be increasingly willing to explore new overseas markets beyond the EU in search of growth.



Conclusions and outlook

- Globally, the recent solid performance in major economies has continued with the US and Eurozone both posting strong growth in Q3. In both cases, there is sufficient confidence that the long awaited recovery has enough momentum to begin planning to remove or reduce the stimulus programmes in place since the recession.
- Whilst the moves towards the normalisation of monetary policy has been welcomed by many, others including the IMF have voiced concerns that there remain a number of underlying issues in the global economy, and have urged a cautious path with regard to withdrawing stimulus. Chief among these issues is that inflation remains markedly lower than the pre-recession period in most developed economies (the UK excluded). Low wage growth is acting to inhibit inflation, in spite of the strong recovery seen in headline measures of employment which would in usual circumstances lead to higher earnings.
- The IMF suggest that away from the positive employment growth, there remains a substantial amount of slack in labour markets with significant numbers underemployed in involuntary part-time work, or engaged in less secure temporary employment. Whilst actions such as labour hoarding may have limited the peak in unemployment during the downturn, these issues have exacerbated lower productivity growth which in turn limits firms' ability to increase wages.
- Whilst subdued wage growth is an issue across the developed world, the low inflation seen in other major economies is not a problem shared by the UK, where inflation is running well ahead of the government's 2% target. Whilst it is widely recognised that the key driver of higher prices in the UK is the fall in the value of the pound since the EU referendum, the Bank of England was still sufficiently concerned about rising inflation to increase interest rates for the first time in a decade. The move helped to shore up the value of sterling which may help ease some of the pressures businesses are experiencing through rising import prices.
- The interest rate move comes in spite of UK growth slowing compared to that of other G7 nations so far this year, and below the levels seen in the UK in the preceding three years. Whilst the economy has maintained growth since June 2017 and has performed particularly well in terms of job creation, it does appear that headline growth has is below trend, perhaps due to a combination of factors including subdued consumer activity and Brexit-related uncertainty.
- National reports suggest that there is increasing concern among the business community about the apparent lack of progress on Brexit negotiations, with the CBI urging the government to agree a transition deal by the end of the year to avoid businesses having to enact contingency plans for a "no deal" scenario early in 2018.
- Local data, particularly that from the Chambers' QES, suggests that local firms are still feeling the pressure from increased prices so from their perspective any moves by policymakers to help ease that will be welcome. Equally, HRMC's regional export data shows a strong upturn in exports from the region so far in 2017, suggesting that increasing international trade will offset some of the burden felt through increasing costs for those firms who are prepared to explore opportunities overseas.
- Locally however, both the QES and the LCR Business Survey suggest levels of investment are comparable to previous years, and businesses continue to create jobs at a solid pace. This, combined with BankSearch data suggesting new business formation here is keeping pace with previous years and outperforming other LEP areas, suggests that for the time being at they are focused on growing their operations and are optimistic about the year ahead.
- *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*