

ECONOMIC AND BREXIT MONITOR: LEEDS CITY REGION, NOVEMBER 2018

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

- The **IMF has recently revised down its forecasts for global growth** to 3.7% for both this year and next – down 0.2% from its forecasts in April. Recently announced tariffs and trade measures are key reason for this downward revision, which keep growth projections in line with 2017.
- The **IMF forecast growth in the UK to slow from 1.7% in 2017 to 1.4% and 1.5% in 2018 and 2019** respectively.
- **UK GDP increased by 0.7% in the three months to August.** This is substantially higher than the 0.1% growth in March-May. Warm weather was an important factor in this.
- **UK productivity increased by 0.5% in Q2 2018**, following a Q on Q fall in Q1. Productivity growth remains below the pre-recession trend.
- **Inflation fell to 2.4% in September**, down from 2.7% in August whilst **average earnings increased by 3.1%** in the three months to August, the highest annual growth rate since 2008. Real pay has increased by 0.7% in the past three months, with wage growth outpacing inflation for five consecutive months.
- **Total employment in the UK was largely unchanged** in the three months to August, according to ONS. The employment rate dipped to 75.5% from a record high of 75.7%. **Unemployment also fell.**

Key City Region and local developments

- The value of goods **exports from Yorkshire & Humber increased at a faster rate than any other English region** between Q1 2018 and Q2 2018. The region's goods exports increased by 3.4% in Q2, compared to a 2.2% fall nationally, according to HMRC data. The region has seen the joint fastest growth in goods export of any English region since the EU referendum in June 2016.
- New ONS analysis suggests **Yorkshire & Humber exported services worth £7.78bn in 2016**, an increase of 8.1% on 2015. This growth rate is third lowest among UK regions, and falls between North West (-0.9%) and North East (+14.3) at a northern level.
- **Business activity continued to expand across Yorkshire and Humber** through September according to the Natwest Regional PMI, albeit at a reduced pace.
- **Yorkshire businesses reported increased domestic and international demand in the PMI survey, and remain optimistic** that output will continue to increase over the next year.
- **Total employment in Leeds City Region increased by 4,000 (0.3%)** between Q1 and Q2 2018, taking the employment rate to a new record high of 73.7%. Employment increased faster than in the UK as a whole where it increased by 0.1%.
- **Unemployment in the City Region fell by 3,100 (4.5%)** in Q2 2018. There are now 65,200 people unemployed, the lowest level since 2005. The unemployment rate is 4.4%, also its lowest since 2005.

Brexit implications and conclusions

- There are signs that UK businesses are beginning to become increasingly alive to the uncertainty of Brexit negotiations and the perceived higher risk of a “no deal” outcome.
- At City Region level, the labour market remains relatively strong with employment increasing and unemployment decreasing. However, it is notable that some of the sectors that have seen strong employment growth of late are among those with reliance on EU workers which may pose a challenge to these industries in future, most notably logistics and hospitality sectors.
- The region's goods exporters continue to see the benefit of sterling's fall and have seen export activity expand strongly in the past two years. This may be a factor in the continuing levels of confidence among the region's businesses, who remain more optimistic than those in most other regions. The apparent fall in new business starts does however suggest a degree of hesitancy in some quarters.
- That same hesitancy is evident in the housing market, where sales volumes point to a slowdown despite rising prices. Many households, like businesses, appear to be waiting for clarity and confidence in future arrangements before making significant investment decisions.

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

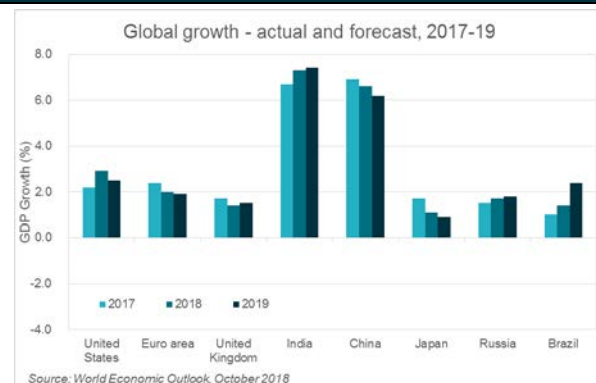
ECONOMIC AND BREXIT MONITOR: LEEDS CITY REGION, NOVEMBER 2018

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 up to August 2018. There is also new official data on trade, inflation and retail activity and survey data on business sentiment.
- For Leeds City Region, labour market for Q2 2018 and regional goods exports data from HMRC for the same period are also presented. Banksearch on the number of new business bank accounts and CoStar data on the commercial property market are available for Q3 2018.

Global economic and political developments

- A range of geopolitical and trade tensions have heightened concerns about the global economy of late, with a mixed outlook for near term prospects.
- US GDP increased by 0.9% in Q3 2018, a slight slowdown from Q2 but still a measure of robust growth.
- The Eurozone economy grew by just 0.2% in Q3, a slowdown from 0.4% in Q2.
- The Chinese economy grew by 6.5% in Q3, a slowdown from 6.7% in Q2. Growth is expected to continue to slow as tariffs begin to take effect. Growth in the next-largest emerging market, India, remains strong, driven by domestic demand.
- The price of oil has surpassed \$80 per barrel for the first time since 2015 in October. A range of issues are limiting supply, whilst diplomatic tensions with Iran and Saudi Arabia are also pushing up prices.
- The IMF has recently revised down its forecasts for global growth to 3.7% for both this year and next – down 0.2% from its forecasts in April. Recently announced tariffs and trade measures are key reason for this downward revision, which keep growth projections in line with 2017.
- The IMF forecast growth in the UK to slow from 1.7% in 2017 to 1.4% and 1.5% in 2018 and 2019 respectively. Poor weather in Q1 is a factor in this, though anticipated higher barriers to trade post-Brexit are also a factor in the medium term despite the IMF assuming that UK-EU trade remains tariff-free.
- UK public finances have performed better than expected so far this year, with public sector borrowing falling to its lowest level in 16 years to £19.9bn in the first half of the financial year.
- In recognition of the UK's low unemployment and improved financial position, the IMF suggest that some “modest tightening” of monetary policy may be warranted, for example through higher interest rates. However, the Fund also urged UK policy makers to remain flexible “in response to changing conditions associated with the Brexit negotiations”.
- There are signs that UK businesses are beginning to become increasingly alive to the uncertainty of Brexit negotiations and the perceived higher risk of a “no deal” outcome. A CBI survey suggested 1 in 5 businesses had already begun to implement contingency plans, with increasing numbers of companies planning follow suit if no certainty emerges before the end of 2018. Similarly, the Chambers of Commerce have reported lower levels of investment in their national survey for Q3.
- These trends are supported by statements made by major UK companies in recent weeks. The automotive industry continues to express concerns over the Brexit process, with Honda saying Brexit could increase costs by 10% and some manufacturers planning partial or temporary shutdowns to mitigate the risks of a no-deal Brexit and in response to falling sales, with new car sales down 20% in September. Meanwhile pharmaceutical company AstraZeneca has said it is stockpiling medicines in preparation, but is maintaining its freeze on new investment in UK manufacturing.



Global economy summary: Whilst the US economy continues to grow solidly, apparently as yet unaffected by tariffs imposed as part of a growing trade war, the picture is less positive in Europe. Concerns over a trade war are one of a number of concerns here, with Brexit and a slowing economy combined with budget challenges in Italy also posing challenges.

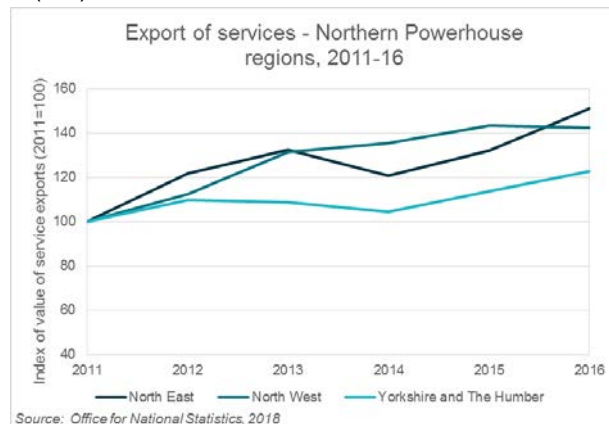
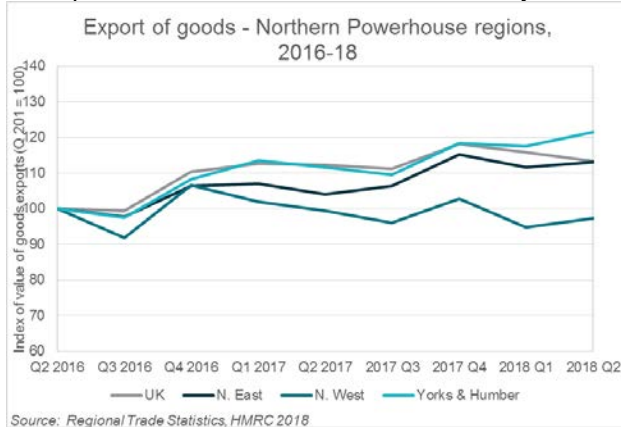
UK economic dashboard

| Indicator | Latest position | Chart | Trend |
|---------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------|-------|
| Economic headlines | <p>UK GDP increased by 0.7% in the three months to August. This is substantially higher than the 0.1% growth in March-May. Warm weather was an important factor in this. The service sector expanded by 0.5%, though this was outpaced by growth of 0.7% in production and 2.9% in construction.</p> <p>UK productivity increased by 0.5% in Q2 2018, following a QoQ fall in Q1. Productivity growth remains below the pre-recession trend.</p> | <p>UK GDP growth, 2008-18</p> <p>Source: Office for National Statistics, 2018</p> | |
| Confidence and sentiment | <p>Expansion continued across the manufacturing, services and construction sectors in October. The pace of growth slowed in the two former sectors, but quickened in construction.</p> <p>Domestic and overseas demand softened for manufacturers. Business optimism was dampened across all three sectors, with companies in all saying Brexit uncertainty was hindering demand, particularly in consumer sectors.</p> | <p>Purchasing Managers Index (PMI) by sector, 2016-18</p> <p>Source: Markit/CIPs PMIs, 2016-18</p> | |
| Labour market | <p>Total employment in the UK was largely unchanged in the three months to August, according to ONS. 289,000 more people are in work than a year ago. The employment rate dipped to 75.5% from a record high of 75.7%.</p> <p>Unemployment fell by 47,000 to 1.36 million, an unemployment rate of 4%. There was however a 100k increase in economic inactivity (neither in work nor seeking work) to 8.75m.</p> | <p>UK employment growth 2008-18</p> <p>Source: Office for National Statistics, 2018</p> | |
| Trade and exports | <p>Retail sales increased by 1.2% in the three months to September, though this was largely down to strong summer performance, with sales volumes down 0.8% between August and September.</p> <p>The UK's trade deficit narrowed by £4.7bn to £2.8bn in the three months to August. Imports increased by £2.5bn, but this was outpaced by export growth of £7.2bn.</p> | <p>UK retail sales, 2008-18</p> <p>Source: Office for National Statistics, 2018</p> | |
| Inflation and wages | <p>Inflation fell to 2.4% in September, down from 2.7% in August. Transport costs were the main driver of price increases, rising by 5.5%, whilst energy costs also increased.</p> <p>Average earnings increased by 3.1% in the three months to August, the highest annual growth rate since 2008. Real pay has increased by 0.7% in the past three months, with wage growth outpacing inflation for five consecutive months.</p> | <p>Wage growth and inflation, 2008-18</p> <p>Source: Office for National Statistics, 2018</p> | |

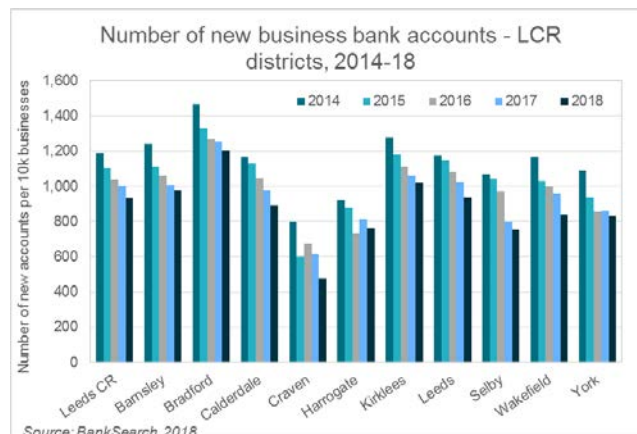
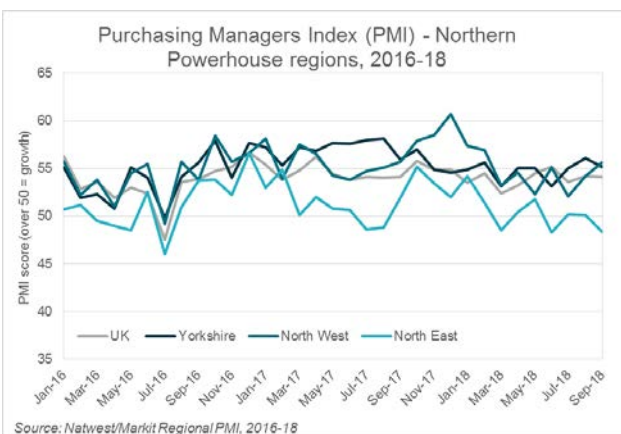
Brexit implications: At a headline level the UK economy remains relatively healthy. However, there are signs that the effects of a strong summer helped by good weather are still being felt and more recent data suggests a slowdown as the UK has headed into the autumn. Perhaps not coincidentally, surveys suggest that there is increasing recognition among businesses of the risks posed by Brexit uncertainty, with more businesses starting to enact their contingency plans in the event of a “no deal” scenario.

Leeds City Region – Business Performance and Trade

- The value of goods exports from Yorkshire & Humber increased at a faster rate than any other English region between Q1 2018 and Q2 2018. The region's goods exports increased by 3.4% in Q2, compared to a 2.2% fall nationally, according to HMRC data.
- Yorkshire & Humber has seen the joint fastest growth in goods export of any English region since the EU referendum in June 2016. Along with East Midlands, exports are 21.5% higher than Q2 2016.
- The European Union accounted for 60% of goods exports from Yorkshire & Humber in Q1 2018, higher than the 58% averaged across 2017. North America and Asia/Oceania accounted for 12.6% each.
- New ONS analysis suggests Yorkshire & Humber exported services worth £7.78bn in 2016, up 8.1% on 2015. The region has seen lower growth in service exports than other English regions in the past five years.
- Financial services accounts for a third of the region's services exports, a higher share than any other region. Another third is shared almost equally between manufacturing, professional services and transport.
- Yorkshire & Humber accounts for around 3% of UK services exports and 5% of goods exports. This in part reflects the dominance of London in service exports, though in both cases the region has a lower share of exports than its share of the UK economy would suggest (7%).



- Business activity continued to expand across Yorkshire and Humber through September according to the Natwest Regional PMI, albeit at a reduced pace. The region's PMI dipped from 56.1 to 55.2 from August to September (a reading over 50 indicates growth), though it remains the 3rd highest among English regions.
- Yorkshire businesses reported increased domestic and international demand in the PMI survey, and remain optimistic that output will continue to increase over the next year. As such, headcounts continue to expand.



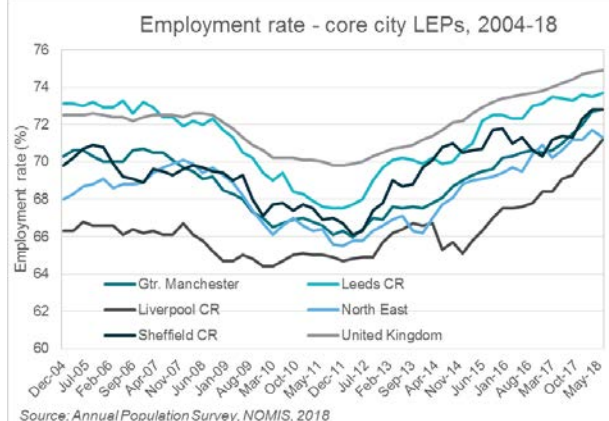
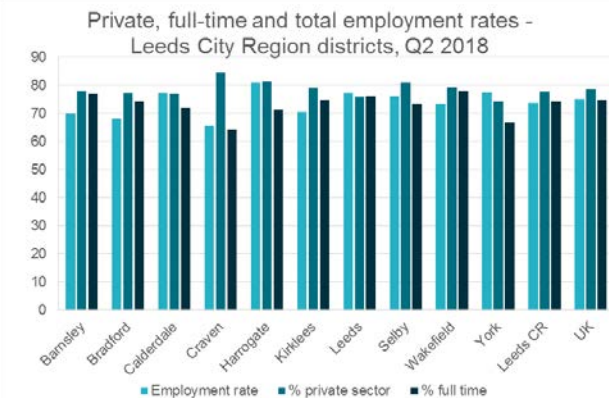
- 3,800 new business bank accounts were opened in Leeds City Region in Q3 2018 according to BankSearch, down from over 4,000 in Q2 and from 4,100 in Q3 2017. Over the first three quarters of 2018, the number of new business accounts opened is down 6.7% in Leeds City Region and 9.7% nationally.
- Barnsley saw the number of new account openings increase by 9.6% between Q2 and Q3, with Bradford up 1%. All other districts were either flat or saw declines.

Brexit implications: The region's goods exporters continue to see the benefit of sterling's fall and have seen export activity expand strongly in the past two years. This may be a factor in the continuing levels of confidence among the region's businesses, who remain more optimistic than those in most other regions. The apparent fall in new business starts does however suggest a degree of hesitancy in some quarters.

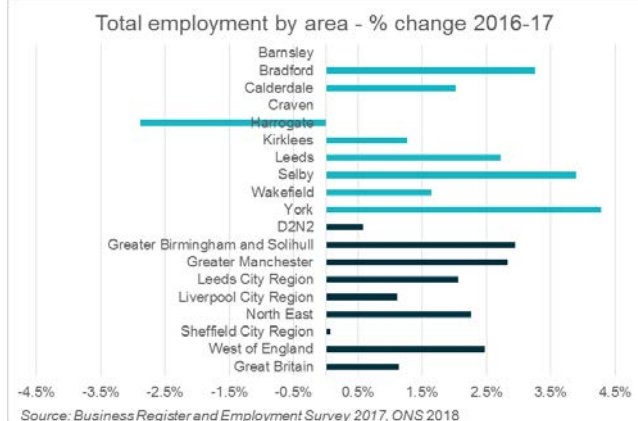
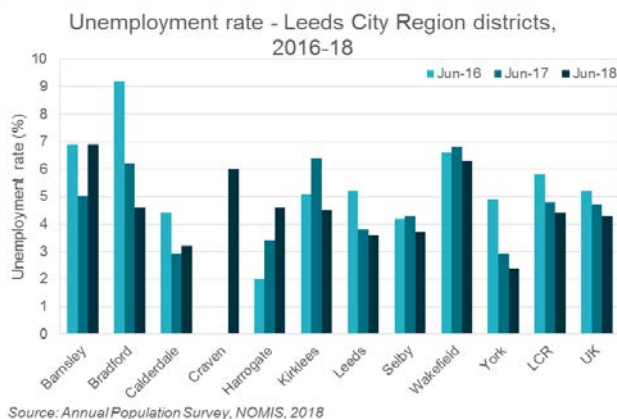


Leeds City Region – Labour Market

- Total employment in Leeds City Region increased by 4,000 (0.3%) between Q1 and Q2 2018, according to the ONS Annual Population Survey. There are now 1.42 million residents in work. Employment increased fast than in the UK as a whole where it increased by 0.1%.
- Leeds (+0.8%) and Kirklees (+1.6%) both saw total employment increase by over 3,000 last quarter, though this was partially offset by 4 districts seeing declines of between 500 and 1,800, though it should be noted that data can fluctuate between quarters. Harrogate (+2.2%) saw the biggest increase in percentage terms.
- Employment growth in the City Region was on a par with Greater Manchester, Sheffield City Region and Greater Birmingham last quarter. West of England and Liverpool City Region saw stronger growth, though D2N2 and North East LEP areas saw small declines.



- The employment rate for Leeds City Region has increased to 73.7%, up from 73.5% in Q1 to a new record high. The City Region's employment rate remains the third highest among core city LEPs, but behind the UK rate of 74.9%. The employment rate has increased to above 77% in York, Calderdale and Leeds.
- The proportion of people aged 16-24 who are in employment increased to 54.7% in Q2, the first time it has surpassed 54% since 2009.
- Unemployment in the City Region fell by 3,100 (4.5%) in Q2 2018. There are now 65,200 people unemployed, the lowest level since 2005. The unemployment rate is 4.4%, also its lowest since 2005. Only Bradford and Craven saw very small increases in unemployment this quarter, and in the former's case the unemployment rate is halved from 9.2% in June 2016 to 4.6% in June 2018.
- Other data recently published by ONS looks at the growth in the number of workers in a given area (as opposed to the residence-based employment measures above). This shows that the number of workers in Leeds City Region increased by 28,500 between 2016 and 2017, an increase of 2.1%. Employment increased by 1.1% across the UK over the same period.



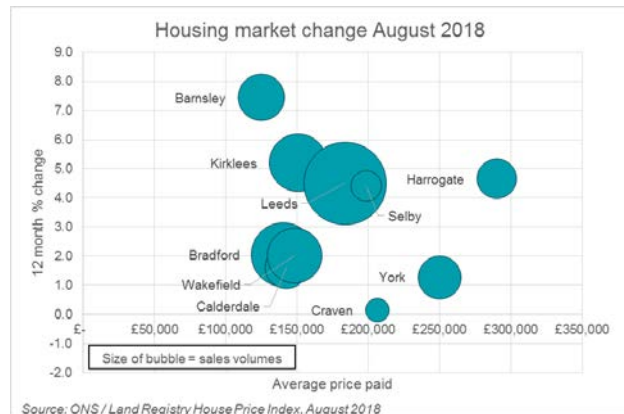
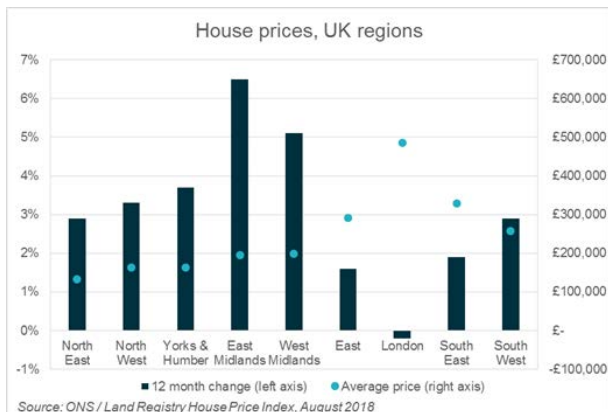
- Employment growth in 2017 was faster in Leeds City Region than in D2N2 and the Liverpool and Sheffield City Regions, but below that of other core city LEPs. Logistics, hospitality, and financial & professional services have contributed to employment growth in Leeds City Region of late.
- Most districts of Leeds City Region saw the number of workers increase in 2017, though the picture was flat in Barnsley and Craven and Harrogate saw a 2.9% decrease in the number of workers.

Brexit implications: At City Region level, the labour market remains relatively strong with employment increasing and unemployment decreasing. Some of the sectors that have seen strong employment growth of late are among those with reliance on EU workers which may pose a challenge to these industries in future.

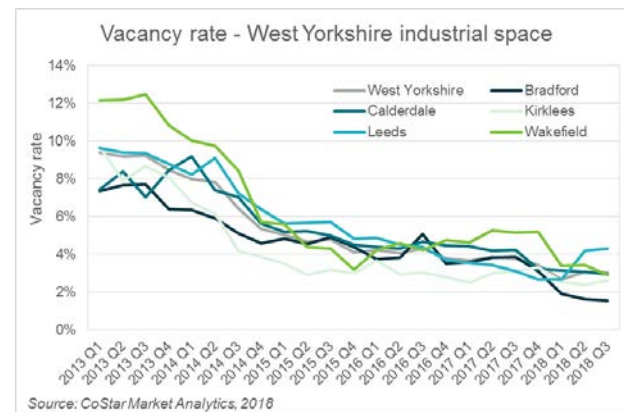
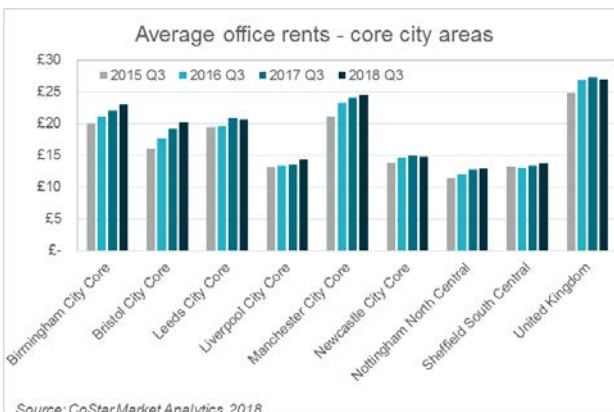


Leeds City Region – Housing, Property and Infrastructure

- House prices increased by 3.7% in Yorkshire & Humber in the year to August 2018. This is faster than regions in the south and north of England, but slower than the Midlands. London is the only area to see prices fall over the past year.
- Sales volumes are down 10.5% nationally and by 8.2% in Yorkshire & Humber in the first half of 2018 compared to the same period last year.
- The average property sold for £164,000 in Yorkshire & Humber in August. Northern regions remain substantially more affordable on average than other parts of England. There remains substantial variation across the region however, with average prices 35% higher in North Yorkshire than in South Yorkshire.



- Within the City Region, whilst all districts saw average prices increase over the past year this ranged from 7.4% in Barnsley to just 0.2% in Craven.
- Whilst prices increased in all districts, sales volumes fell in all areas. The number of transactions fell most sharply in Wakefield, down 17%. Craven saw the softest decline in sales volumes, down 3.4%. Transactions were down 10.7% across West Yorkshire as a whole.



- Average rents for West Yorkshire office space remain steady at £13.60 per square foot in Q3 2018, according to CoStar. Office rents have been little changed over the past year in most parts of West Yorkshire. Birmingham, Bristol and Manchester have seen office rents grow more sharply in the past year.
- The vacancy rate has fallen over the past year, from 7.9% in Q3 2017 to 6.2% in Q3 2018. The city core in Leeds has seen the fastest fall in vacancy rate, from 17.1% to 12.8% in the past 12 months.
- In the broader West Yorkshire market, a combination of robust occupier demand and several office-to-residential conversions caused office vacancy to fall sharply during recent quarters, reaching an all-time low near 6% in Q3. This is the 2nd lowest vacancy rate among major UK markets. CoStar expect the Leeds office market fundamentals to improve further once Channel 4 moves to the city.
- There is increasing pressure on industrial space in West Yorkshire, with vacancy rates falling 9% in 2013 to 3% in Q3 2018. The vacancy rate is just 1.6% in Bradford. As such, rental prices are increasing, up by an average of 1.6% over the past year though this is lower than the 6-7% growth seen in 2017.

Brexit implications: House prices in the region continue to rise, though a fall in volumes is indicative of a slower market. Many households, like businesses, appear to be waiting for clarity and confidence in future arrangements before making significant investment decisions. Whilst vacancy rates for commercial property suggest robust demand, relatively low rental growth may be indicative of fragile confidence.



Conclusions and outlook

- The global outlook has become more divergent and uncertain in recent months. Europe and China are being affected by a range of factors though the increasing threat of a trade war with the US is central to this. Other factors, such as the increasing nervousness around Brexit for many in Europe and rising oil prices and geopolitical risks more broadly have been behind major falls in stock markets in recent months.
- The US has so far bucked this trend and continues to report strong economic performance. This was expected to a large degree given recent tax cuts, and it remains to be seen if this is sustained in the medium term particularly if trade relations with China and the EU continue to deteriorate.
- These increasing tensions could be a factor in an apparent slowdown in the UK. Whilst headline economic data points to a strong summer driven by good weather, more recent intelligence from both surveys and harder data suggests that the picture has become more subdued through the autumn.
- Brexit does however to be increasingly central to businesses' thinking. It is notable that the issue was cited as weighing on sentiment across all sectors of the economy in October, regardless of performance. This suggests that businesses are becoming more conscious of the fact that their time to prepare and respond to any changes ahead of the March deadline is increasingly limited.
- Anecdotal evidence from conversations with businesses in Leeds City Region supports the findings reported here that many businesses have either already begun to enact their Brexit contingency plans or plan to do so by the end of 2018. For some, their business cycle is such that Brexit is now an operational issue and as such the response is already underway.
- Many City Region businesses cite uncertainty over import/export arrangements as a key concern which could impact on their operation as they don't have the capacity to stockpile or adapt to longer lead times. This is a critical issue for manufacturers, but also for sectors which have seen strong employment growth in Leeds City Region of late such as logistics. The sector has both a strategic reliance on the efficient movement of goods across borders and a high demand for EU migrant workers. As such future changes in this area will be critical to the sector.
- A lack of availability of workers is also a primary concern for businesses and some have suggested this is already having an impact, with recruitment becoming more challenging in recent months. This is likely to affect both high skilled roles and those sectors who are more reliant on lower skilled workers from the EU. The hospitality sector is one of these, and has also seen strong growth in Leeds City Region of late. With data suggesting weak consumer activity, this sector will be closely watched through the critical Christmas period.
- That said, for some businesses, particularly those for whom the US and Asia are already key import/export markets, Brexit is less of a concern and new trading relationships may prove beneficial in the longer term, though these importers continue to experience challenges from higher material costs.
- It is also clear from the data that our region has capitalised on the fall in sterling to accelerate export activity, with the value of exports growing faster here than in any other region since the EU referendum. Yorkshire & Humber has outperformed the UK on this measure of late and this is likely a key reason behind the region's businesses being consistently more optimistic than their counterparts elsewhere in the UK.
- The anecdotal evidence supports the wider data in that a tighter labour market is increasing demand for workers and helping to push up wages. This does not however appear to be feeding through into increased consumer activity, with many surveys and data sources suggesting that activity in this area has slowed of late. This is evident in slower retail sales and declining volumes in the housing market.
- Again, Brexit is likely to be a key factor here, as it is in the evident fall in new business starts and relatively low growth in commercial property prices. With the Article 50 deadline fast approaching, households and businesses alike delaying major investment decisions until there is greater clarity and confidence.

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.