Bournemouth University

Regional Economic Development

Business Intelligence Report 14: Summer 2018[1]

Summary

After a cold, wet first quarter of 2018, the second quarter of dry sunshine seemed to warm up the economy, a little – a pattern continuing into the third.

The pattern of growth is very uneven, however, with services providing the push and manufacturing and construction the drag. The UK's deteriorating trade balance is concerning, with exports down, (especially of cars), and imports up.

The renewed weakening of sterling may help trade in due course but it will boost costs first. Moreover, the inevitable negative effects of BREXIT and US mercantilism (higher inflation and lower growth) will not dissipate soon or quickly. With nervous supply chains, investment and consumption patterns are vulnerable to adverse outcomes.

Against this background, **Dorset retains some of its relative poise** because of its historical focus on a resilient spread of domestic markets. In the near term, this means local businesses continue to complain about the problems of success, (skills shortages and transport congestion), more than those of failure, (weak final demand and poor competitiveness).

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[1] This is the latest of a regular overview series of Business Intelligence Reports that BU produces for the Dorset and neighbouring business community and its partners.

In the longer term, however, the issue is still how to boost productivity, mitigating some of the constraining factors and providing a 'new' focus for growth: better investment, innovation, skills, entrepreneurship and competitiveness.

Intervention may be warranted to boost capacity and capability, encouraging collaboration to compete as well as more agglomeration and networking. Thereby, we may deliver the high value, 'sticky' supply chains we need.

The UK Economy

EVIDENCE

	Annual (2017)	Quarterly	Monthly
Real GDP (%ch 3m on prev)	+1.7	+1.2 (Q1)	+0.2 (Mar-May)
CPI inflation (%ch, yoy)	+2.7	+2.4 (Q2)	+2.4 (Jun)
LFS unemployment (%)	4.4	4.2 (Q1)	4.2 (Mar-May)
Current Account (£bn)	-78.9	-17.7 (Q1)	n.a.
Base rate (%)	0.29	0.5 (Q2)	0.5 (Jul)

Source: ONS

The UK economy (see table above and chart below) is meandering around a pattern of weak growth, firm inflation, low unemployment and persistent deficits. The consumer is constrained, investors are restrained and foreigners are selling a lot more to us than they are buying from us.

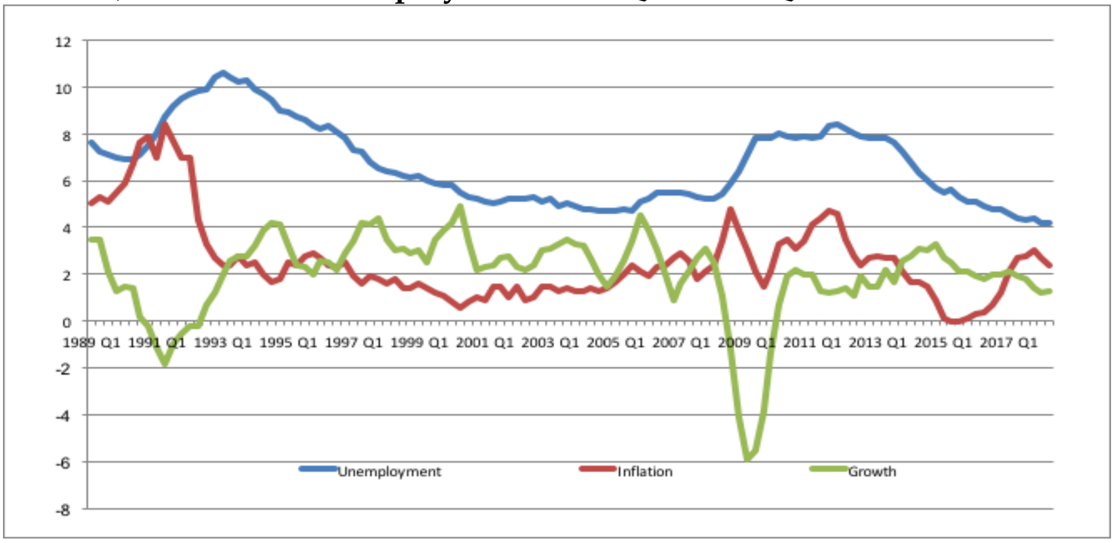
According to the first of the new monthly GDP releases, economic momentum remains modest, at best, and has moderated over the last year. The first of the new quarterly GDP series will emerge in August[2].

Meanwhile, recent performance has seen a modest retail and services rebound from the weather-affected first quarter. But, manufacturing and construction have been negative. The labour market is tight but productivity is low and growth potential is waning.

[2] Because of the change in ONS patterns of data release, the next BIR will be delayed until November and future issues will occur in sequence after that.

Whenever inflation rates are higher than growth rates (and both are softening), there is a risk of a weaker economy to come.

Growth, Inflation & Unemployment: 1989 Q1 – 2018 Q2



Source: ONS: Growth = real GDP % change year-on-year (yoy). Inflation = CPI % ch yoy. Unemployment = LFS % rate.

STABILISATION

World and UK interest rates are still low, signalling persistent economic weakness, excess money supply, and the potential for debt problems in the future. The monetary and fiscal overhang persists and macroeconomic policies are still offering little to help the economic cycle to be more robust.

With BREXIT uncertainty yet to be resolved and the global climate less conducive to economic acceleration, because of higher commodity prices and trade barriers, only moderate real growth can be anticipated - at least until or unless the world's savings glut is turned into a more active push for real investment.

For example, in its long-term outlook, **the OECD** recently (July 2018) forecast global real GDP growth falling from 3.5% per annum now to 2% a year by 2060. This is not inherently a good or bad thing. Partly, it reflects the maturing of markets in India and China to more sustainable growth rates. Nevertheless, with an ageing demography, new disruptive technologies and climate change, the world's economic 'future' is not the same as it was!

The latest **IMF** short-term update (July 2018) pointed to world output growth of 3.9% this year and next, with trade volume growth slowing from 4.8% to 4.5%. These rates represent a reasonable near-term outlook.

Importantly, however, the IMF said growth was becoming more uneven and fragile, especially for the United Kingdom. The balance of risks is thought to be more negative because of oil, trade and currency factors.

The IMF also said the 'Trump Trade Wars' could cost the world economy US$400-500bn and cut 0.5% per annum off growth by 2020. It called for greater efforts towards free and global trade, encouraging countries to undertake structural reform and prepare for "a rainy day".

Against this background, **central banks and national treasuries** cannot be relied on to dig the economy out of any cyclical holes. The policy levers are less effective. Strategic growth rather than stabilisation policies should come to the fore.

The United Kingdom, especially given uncertainty about the market and regulatory structural changes underway, will need to invest more in the dynamic chain of innovation that seems likely to arise through the 2020s.

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The Dorset Economy

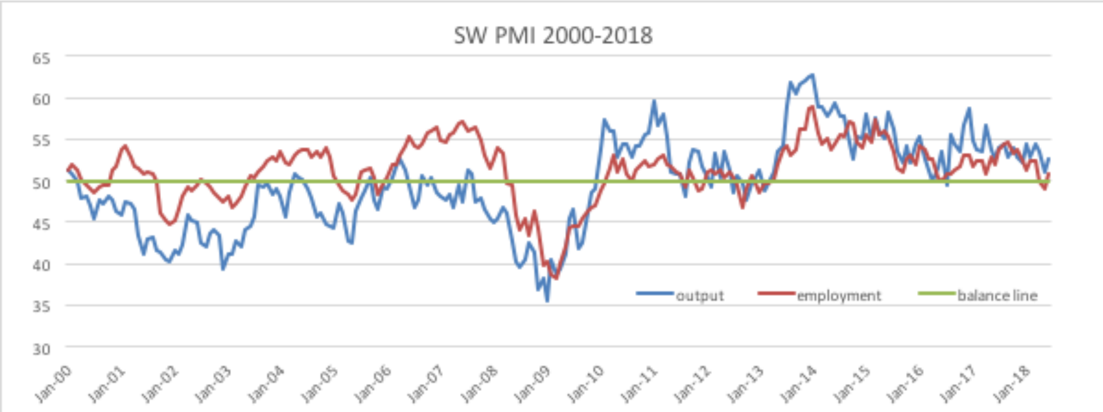
CONDITIONS

Dorset's economy is growing, albeit modestly. The first chart below indicates that SW activity and jobs are still above the PMI 50 balance line, suggesting continued expansion. But, net sentiment and momentum has been falling since the referendum 'blip' two years ago.

A couple of other second quarter surveys confirm this. First, the BCC survey reports sluggish growth: a "holding pattern" caused by high uncertainty. Second, the latest ICAEW survey saw more business confidence, but only compared with referendum lows - sentiment is not back to 2012-15 levels.

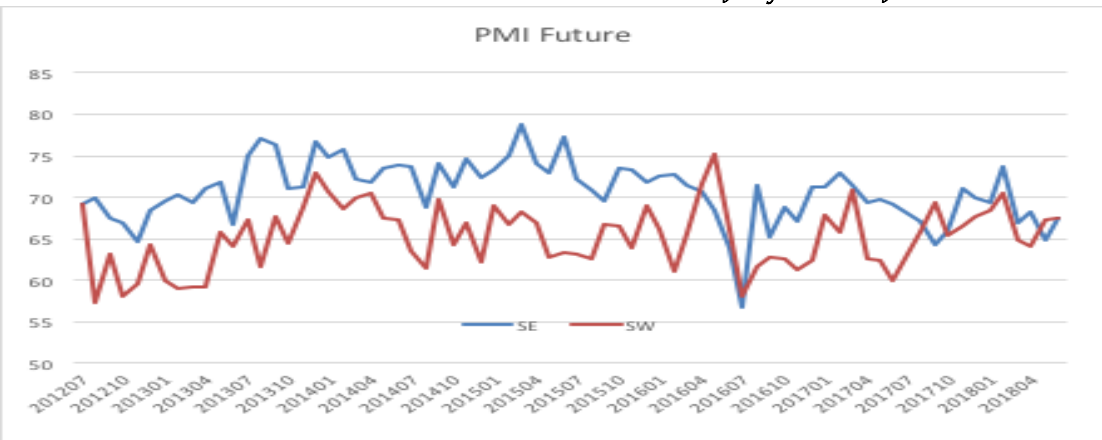
Generally, economic performance is not robust and is unlikely to be so through the second half of 2018.

Markit's SW PMI Activity & Employment Scores 2000-18



The second PMI chart shows SW and SE business respondents still fairly optimistic about the future. So, we can still hope for a 'bounce' this summer and autumn. But, given the overall easing of growth potential and the other anecdotal evidence just outlined, the possibility of occasional months of contraction cannot be ruled out.

Markit's SW & SE PMI Future Outlook balances: July 2012 - June 2018



The good news is that local labour markets are still robust. Claimant count rates are generally so low (0.6% or less in Dorset in June) that they are virtually irrelevant to predicting wider economic trends.

The Labour Force Survey shows the detailed local breakdown for the last twelve months available (i.e. year to March, as in the table below). These ratios are at historical highs (employment) and lows (unemployment) respectively and the usual patterns continue to prevail across the county and amongst our neighbours. With UK equivalent rates at 74.8% and 4.3% respectively, virtually all Dorset's figures are better than average and at, or close to, historical lows.

Despite this, earnings are rising at a very slow pace - basically flat in real terms. UK real earnings are still below levels of a decade ago and are not going to fuel a significant upturn soon.

Local Labour Indicators (April 2017 - March 2018)

	Emp %	Unemp %		Emp %	Unemp %
Bournemouth	75.2	4.1	Dorset	78.0	2.6
Christchurch	83.5	2.3	Somerset	76.5	3.9
Poole	76.3	3.2	Devon	79.3	2.7
East Dorset	81.5	2.3	Wiltshire	81.1	2.9
North Dorset	77.9	2.5	Southampton	74.7	5.0
Purbeck	76.2	2.7	Portsmouth	74.8	4.5
West Dorset	75.4	2.6	Hampshire	82.5	2.9
Weymouth & Portland	74.5	3.2	Isle of Wight	72.5	4.5

Source: ONS
employment 16-64 age groups, APS. unemployment 16+ economically active

The contrast between **macro sluggishness and micro dynamism** continues to play out. Within the general malaise, there are lots of examples of individual Dorset businesses or sectors doing well.

For example, Tech Nation recently reported that the local digital economy is globally competitive, with strong comparative growth in turnover per employee. Other local surveys suggest a relatively high rate of start-ups and good leisure spending in Dorset.

In contrast, some more well-established sectors, including motors and aerospace components and some consumer products, especially those sold in the high street, are less sanguine.

It is a mixed picture and, with the national economy's direction uncertain over the next couple of years, it is likely to remain so.

In such an environment, the disruptive effects of new technologies, demographics and other changes can be particularly important, perhaps heralding a period of shake-out, consolidation and re-growth in some industries in the years ahead. The nimble and efficient will survive and prosper. Others may not.

FEATURE[3]

In 2016, UK gross domestic household income (GDHI) was almost £1.3 trillion. SE and SW England generated almost a quarter of the total (15.8% and 8.2% respectively). The latter came from 8.4% of the UK population whereas the former was from £13.8%, underscoring an inter-regional 'gap' in wealth creation from east to west.

UK GDHI per head was £19,432, just 0.7% up on the year before. SE England reached £22,375 and SW England £19,077. Dorset's ratio fell in 2016 (see table below) but was still better than most of its neighbours.

Local LEP areas – ONS GDHI per head: 2016

	£ per head	% change on 2015
Enterprise M3	25,961	+0.2
Dorset	19,853	-0.4
Swindon & Wiltshire	19,752	+0.2
Heart of the SW	18,218	-0.1
Solent	17,395	+0.4

Within Dorset, highest GDHI per head was achieved in Purbeck and lowest in Poole (see next table). **All Dorset's parts suffered a decline in GDHI per head in 2016 but all, except Poole, were above the national average**.

Dorset – ONS GDHI per head: 2016

Bournemouth	19,448	-0.5	North Dorset	20,469	-0.2
Christchurch	20,560	-0.1	Purbeck	20,956	-0.2
Poole	18,534	-0.4	West Dorset	20,308	-0.6
East Dorset	20,555	-0.3	Weymouth & Portland	20,443	-1.1

Based on the proposed new unitary boundaries, 'City' Dorset had GDHI per head of £19,238 and 'County' Dorset £20,502 in 2016. The gap between the two has widened somewhat, especially after the Great Recession.

Nowhere in Dorset did well in 2016. Indeed, since the Great Recession (2008-9), the more urban parts of Dorset, in particular, have performed relatively weakly. Given all we know about the economy's path since 2016, **it is unlikely that 2017 and 2018 data will change this picture significantly.**

These GDHI trends underpin and reflect a loss of productivity growth over the last decade, with a resulting erosion of growth and earnings potential,

[3] For more detail, see our LEB24 document on Regional Incomes 2016.

despite good employment growth. They do not augur well for future living standards.

COMMENT

Without forecasting a near-term recession, it is sensible to retain some reservations about the local economy for the period ahead.

The negative risks about investment uncertainty probably outweigh the positive ones for the rest of the fiscal year.

A lot of uncertainty will need to be resolved, ideally before Christmas, if that outlook is to change.

If they are not resolved, a 'BREXIT recession' may loom for 2019/20.

Against this background, Dorset businesses have to take destiny into their own hands, planning investment in technical innovation, plant and machinery, workforce and skills, and market penetration.

Thereby, short term pessimism can give way to long term optimism.

Nigel F Jump, Professor in Regional Economic Development