Greater Manchester

Quarterly Economic Survey

Q4 2016

Greater Manchester
Chamber of Commerce
Connect. Communicate. Create.

OVERVIEW Christian Spence *Head of Research & Policy*

The Manchester Index™ made its first upward move in two years in the last quarter of 2016 with domestic demand rebounding from falls in the third quarter after the EU referendum result.

The latest data from the influential Greater Manchester Chamber of Commerce Quarterly Economic Survey (QES) shows a moderate improvement in UK trading positions in the final quarter of 2016 with some of the losses in the third quarter eradicated. The Manchester Index™ nudged up to 20.3 from 17.1 in the Q4 survey data with manufacturing businesses moving out of contraction and order book for 2017 strengthening. The service sector has regained much of its loss of momentum from the softer quarter three data and construction continues to expand, though at lower rates than the past three years.

The update to the Manchester Index™ indicates growth in Greater Manchester of around two per cent per year, commensurate with the UK economy overall. This strengthens our view that Greater Manchester's growth rate may have halved since its peak in 2014 and 2015.

Overall, the UK economy has weathered the months after the EU referendum in better health than many expected, though it should be remembered that policy under David Cameron's government was to serve notice to the EU under Article 50 on 24 June; this is now not expected before the end of March 2017. The latest economic forecasts from the Office for Budget Responsibility expect the UK economy to have grown by 2.1% in 2016 and show little expected Brexit-related effects in the longer term beyond 2018, though growth for 2017 is projected at 1.4%.

The latest data from the QES suggests that this may now be on the pessimistic side and, whilst there are undoubtedly some risks to the UK economy in the coming year, we believe that growth will be around 1.6% for 2017 and that risks of technical recession are now close to zero.

The formal notification of the UK's intent to leave the European Union under Article 50 contains for us a risk of a confidence shock to the economy in the second quarter of 2017 but, if government provides clarity over its position and strategy, we believe the economy will weather this over the year as a whole.

Domestic demand better than expected

The service sector which dominates the economy (81% of GM output) has recovered most of the weakening of growth it saw in the third quarter and order books for the first quarter of 2017 have also strengthened. Manufacturing demand has improved, moving from a contracting position to one of zero growth, showing the sector is still facing headwinds. Construction, whilst slightly softer in the latest data, continues to expand at rates above the pre-recession average.

Weaker Sterling is not a cure

The international picture remains soft for all sectors with the latest data showing either a flat or weaker picture. There is evidence that manufacturing order books for early-2017 may be improving, but the change is small.

It is a perpetual challenge to fight against the popular rhetoric that a weakening of Sterling is a boon for the UK economy. Whilst exporters see an short-term opportunity to either lower prices and gain a competitive advantage against other countries or increase margins, this is quickly eroded by higher inflation from the imported stocking cycle. The UK is an import-export economy with a net trade deficit; all things being equal, weak Sterling is likely to hurt more through imported inflation than it benefits in competitive pricing abroad.

Employment continues to expand

Employment levels remain buoyant across the sectors with manufacturing headcount increasing despite weak demand, likely caused by a combination of age and skills requirements. Growth in the service sector is slightly weaker than over the past year but remains healthy and expansion in the construction is still strong, though expectations for the beginning of 2017 suggest a slowing in growth.

Recruitment levels continue to show around half of all firms attempting to recruit (rising to 80% of construction companies who are also hiring much less temporary labour) but all sectors continue to report significant difficulties in filling positions with three-quarters of companies noting this.

Unemployment nationally is now below 5% - practically full employment – so companies recruiting will be looking to people already in work rather than from a pool of available labour.

Confidence and investment mixed

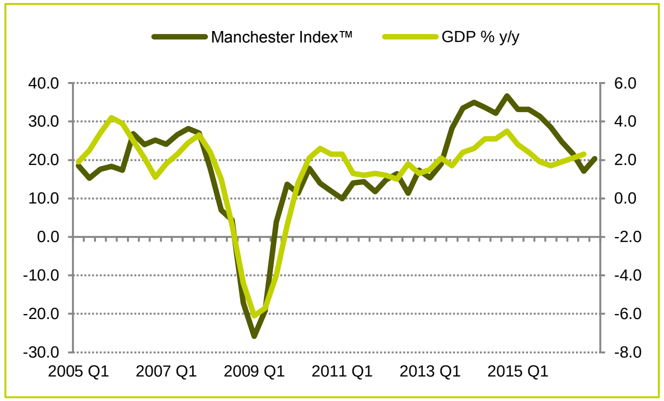
Service sector confidence has rebounded in the latest data with levels softening for construction and manufacturing, the latter particularly so for profitability (producer input prices are biting hard already with the currency shifts). A similar position is seen in levels of investment in both plant & machinery and in training, with improvements for services and construction, but further weakening for the manufacturing sector.

Inflation will be a key issue in 2017

The UK has become used to low levels of inflation, but the long-lived era of benign pricing is coming to an end. Driven by the falls in the exchange rate, prices of imported goods are accelerating quickly and are already making an impact on companies in the production sector; this will feed through to consumer prices across 2017.

Conclusion

Overall, the latest data is positive for the UK economy, ending 2016 stronger than expected last quarter. Inflation will make a return next year placing greater pressure on importers and consumers. We believe 2017 will be materially better than we expected six months ago, but a positive outcome will depend on a clear negotiating strategy from the UK government on the Brexit process. The challenge will be keeping them focus on the realities and not the politics.

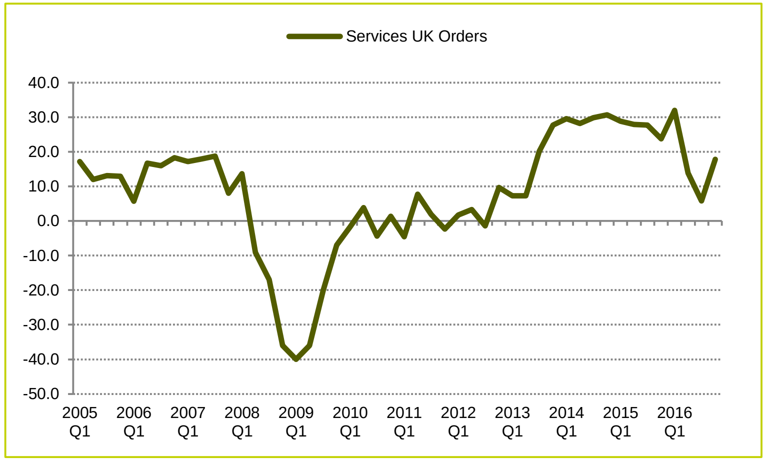


DOMESTIC DEMAND *All sectors show improvements …*

A small improvement in the overall broad manufacturing balance is echoed in the detailed data where core manufacturing has moved from contraction to flat whilst construction, whilst slightly softer, shows strong growth.

Service sector demand has rebounded strongly from last quarter's weak data, suggesting that, in line with official data, the third quarter was marred by a lack of confidence rather than an actual slowing of growth.

Order books look in better shape for the new year with both manufacturing and construction expecting a strengthening in output into the first quarter.



Similarly for services, an expectation of stronger growth for the first three months of 2017 is seen in the latest data, pointing to continued growth in the coming months.

... with expectations for 2017 stronger

INTERNATIONAL DEMAND *Exports weak this quarter …*

International demand for manufacturing and construction firms as softened in the latest data with manufacturing close to flat in the last quarter of 2016.

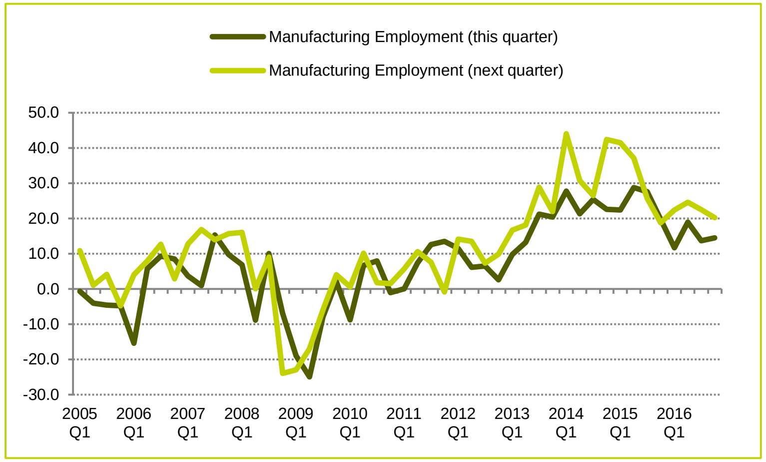
A further slow down for the services sector abroad this quarter with levels at their lowest for four years.

Order books for manufacturing are at their strongest for over a year suggesting that the start to 2017 may be healthier than this quarter.

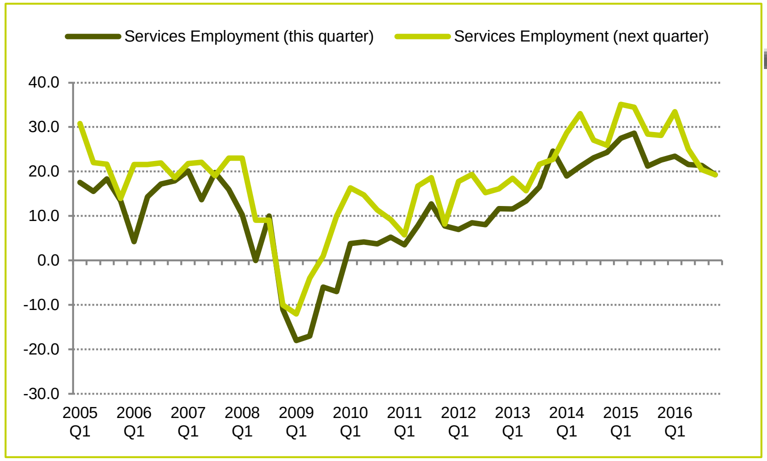
The weaker picture for service sector exports looks likely to continue with reports of order books looking close to flat for the first quarter of 2017.

... though manufacturing may improve into 2017

LABOUR MARKET *Employment growth continues …*

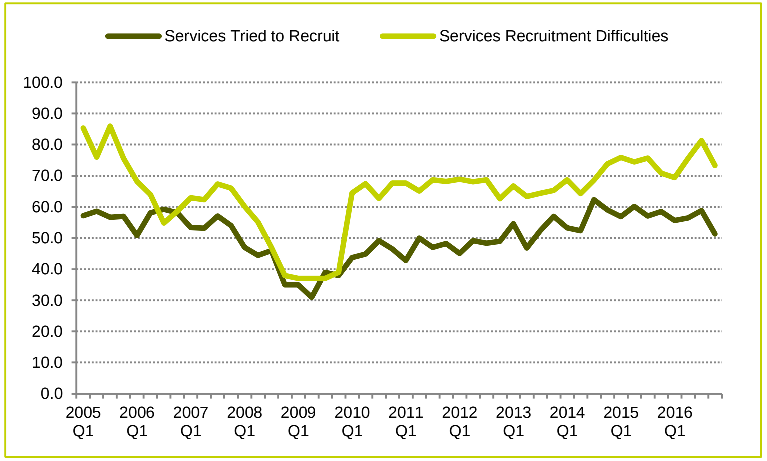


Employment growth remains strong in the last quarter of this year, though softer than at its peak in 2014. Both construction and manufacturing continue to increase their headcounts.



Service sector employment levels also continue to expand, though also at a lower rate than the past two years. Expectations for 2017 remain positive.

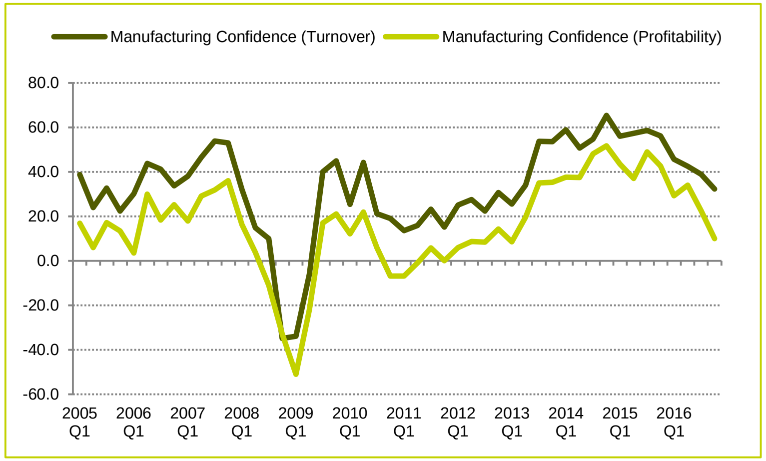
Recruitment difficulties remain high for manufacturing and construction in the face of strong recruitment drives.



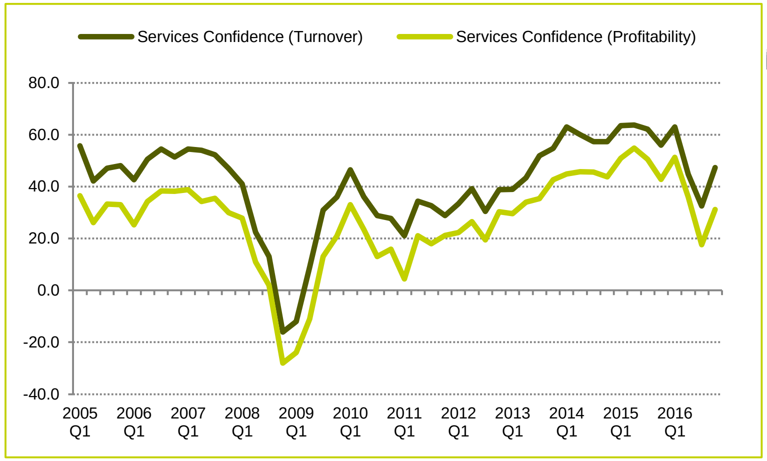
Recruitment levels in the service sector remain healthy, but slightly softer than last year; filling the vacancies is still difficult for many firms.

... but recruitment difficulties remain high

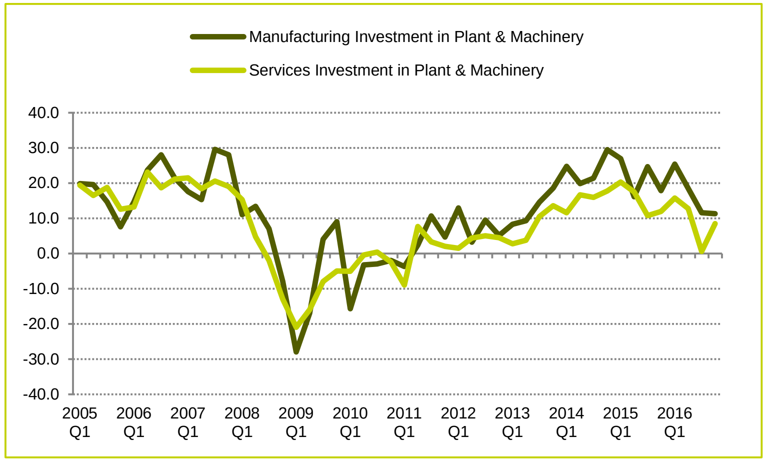
CONFIDENCE & INVESTMENT *Confidence softer …*



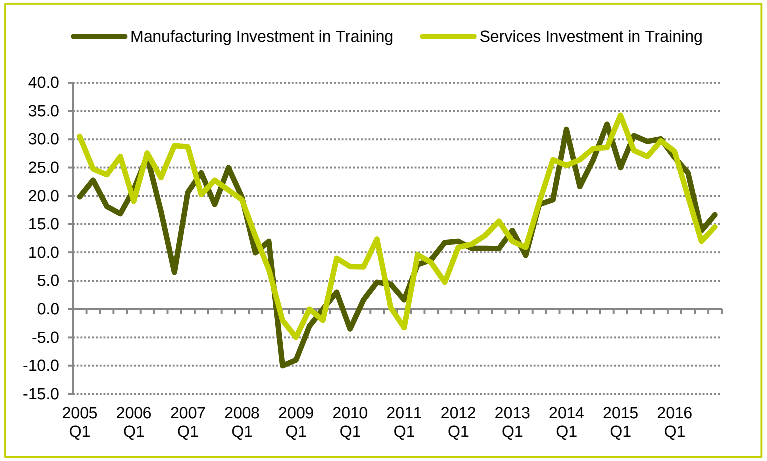
Confidence levels soften further this quarter to levels similar to those in 2010 for the manufacturing and construction sectors.



The service sector is more confident than last quarter, a rebound which gives us reason to expect a better outcome in 2017 than last quarter.



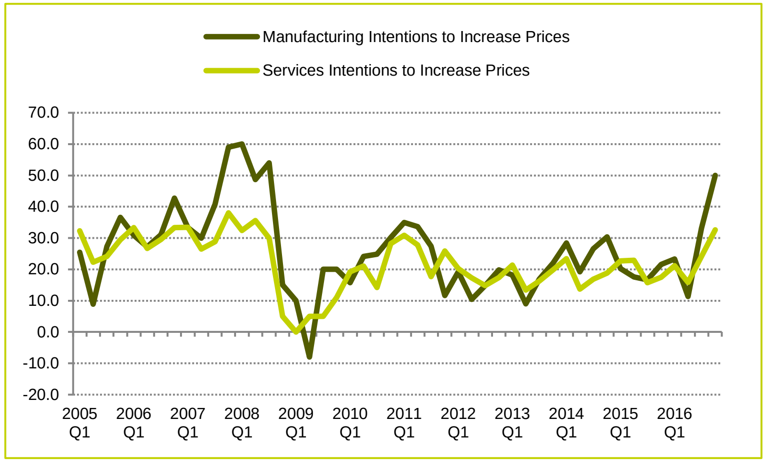
Capital investment levels strengthen for the services sector and for construction, but the manufacturing balance is held back by the core manufacturing sector whose intentions have softened further this quarter.



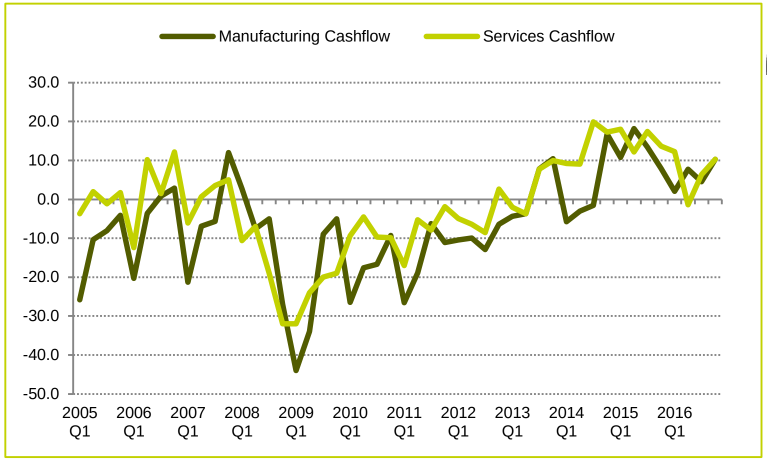
A small increase in the investment in training balance is, of course, welcomed, but at this low level it is uncertain that this is sufficient at a time when unemployment is so low.

... and investment in training weak

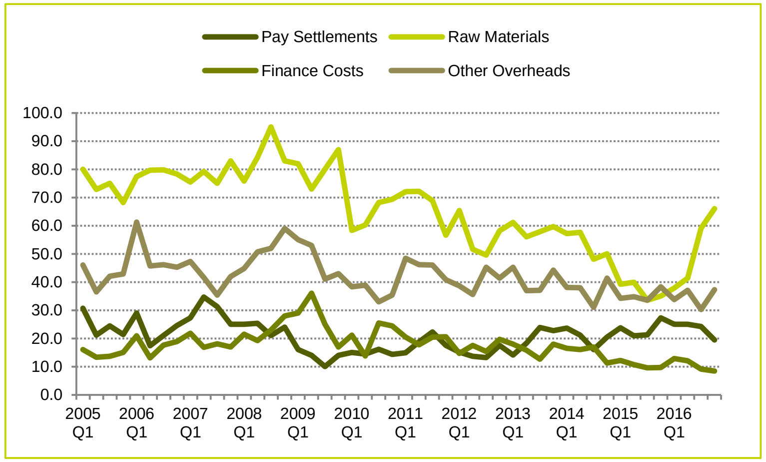
COSTS & PRICES *Inflationary signs are emerging quickly …*



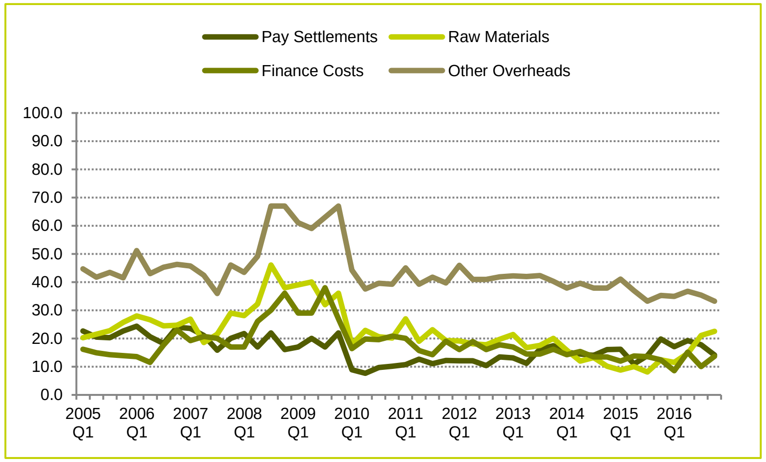
Inflationary intentions rise sharply in all sectors with manufacturing seeing the largest increase. Service sector inflationary expectations are now around the levels last seen before the recession.



Cashflow balances improve for the second quarter in all sectors and remain strong compared to historic averages.



In the manufacturing sector the impact of Sterling depreciation is seen clearly in raw material prices, most of which are imported, and will be feeding through to consumer prices over the coming months.



Raw materials also see a rise for the service sector as inflationary pressures begin to build in the system. It is of interest, however, that for all sectors the pressure on pay settlements has eased.

... with imported inflation likely to outweigh export benefits

BACKGROUND & METHODOLOGY

Greater Manchester Chamber of Commerce is the largest Chamber of Commerce in the United Kingdom, providing business support services to over 4,800 members who collectively employ over 400,000 people, around one-third of Greater Manchester's workforce.

Recognised as a leader in its field, Greater Manchester Chamber's reputation in government circles has grown locally and nationally. Serving the area of greatest economic intensity outside London and the South East, the Chamber is the primary body for business support, policy, representation and networking.

The aim of the Chamber is to support businesses and to help create the best climate for the region to prosper. This is achieved by ensuring that those taking decisions on key issues such as transport, taxation and business regulation hear the voice of our members. The representation of our members' views is central to the work of the policy team at the Chamber; these views are gathered in a range of ways including our local councils, policy committees, sector councils, the main Chamber council, focus groups, meetings with politicians, consultations and, of course, this Quarterly Economic Survey (QES).

Forming part of the British Chambers of Commerce's national survey, Greater Manchester is one of the single largest contributors to this important body of evidence. As the principal national business survey, and the first to be published in each quarter, its results are closely watched by both HM Treasury and the Bank of England's Monetary Policy Committee. Having been the first survey to call the last two recessions, the data revealed by it is timely, accurate and invaluable for anyone wishing to understand the subtle shifts in the economic climate for businesses in Greater Manchester and beyond.

The collection period for this survey was Monday 7 November to Wednesday 30 November 2016 inclusive. A total of 344 businesses, together employing 78,704 people responded to the survey.

This report has been researched, written and compiled by Christian Spence, Head of Research & Policy. If you require any further information about the production or detail of this report, please contact Christian on (0161) 393 4334 or email christian.spence@gmchamber.co.uk.

Net balance figures referred to throughout this report are determined by subtracting the percentage of businesses reporting a decrease in a factor from the percentage of businesses reporting an increase. The broad manufacturing definition includes the agriculture, energy and water, construction and manufacturing sectors.

Copies of this and previous reports can be downloaded from the Chamber's website at www.gmchamber.co.uk/qes with wider economic analysis from GM Chamber at www.gmchamber.co.uk/research.

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