

October 2002

SEEDA Economic & Business Bulletin

I am pleased to present to you a copy of the first SEEDA Economic and Business Bulletin.

We will be publishing further editions of this Bulletin every six months. Its purpose is to inform the development of business strategies in the private, public and voluntary sectors, by drawing together key economic and business information including short-term and medium to long-term outlooks.

I hope you find the bulletin useful. If you have any comments on how it can be improved, or would like more copies, please fill in the attached questionnaire or contact Rashid Bashir, email - rashidbashir@seeda.co.uk. The bulletin is also available on the website at www.seeda.co.uk.

Yours



Allan Willett CMG
Chairman



Economic and Business Bulletin

The South East Economy

Contents

Introduction	1
Executive summary.....	2
1 Key facts	3
1.1 Total output and industrial composition	
1.2 Population	
1.3 The labour force	
1.4 Employment	
1.5 Incomes and spending	
1.6 Budget 2002: Implications for the South East	
2 The short term outlook	5
2.1 Total output and sectors	
2.2 Employment and unemployment	
2.3 Incomes and spending	
2.4 The housing market	
2.5 Tourism in the region	
2.6 Inward investment	
3 The medium/long term outlook	8
3.1 Total output and sectors	
3.2 Employment and unemployment prospects	

Introduction

This report assesses the size and structure of the South East economy and its likely development in the short and medium term future. It is a first in a series of six-monthly reports that SEEDA will be issuing to help inform strategic decision making by businesses, public and voluntary sector organisations.

The report examines the prospects for economic growth, the labour market, income and spending, housing and inward investment, based on the analysis carried out by Business Strategies Ltd (Spring 2002).

If you have any queries regarding this bulletin or its contents, please contact Rashid Bashir, Strategy and Research Manager (01483 500719), e-mail: rashidbashir@seeda.co.uk

Executive Summary

Summary Points

Economic circumstances in the South East are now stronger than predicted at the end of last year, with low interest rates and high public spending helping to keep the UK economy stable and the South East sharing in that. However, employment growth has been slowing since 1996, and employment is likely to fall marginally in 2002 before rising again from next year.

- ▶ Manufacturing employment is set to fall sharply, declining by around 9,500 this year in the South East. Job losses are also occurring in other sectors, but the hotels and catering sector is seeing rising employment. The overall employment rise for 2003 is forecast to be 0.5%.
- ▶ A slowdown in economic activity is forecast, with regional growth declining from 3.2 % in 2001 to 2.4 % in 2002. But a recovery is predicted next year, with GDP growth rising to 3.6 %.
- ▶ At the sectoral level, it is expected that manufacturing will continue to struggle this year, especially those areas exposed to information and communication technology (ICT) and aviation. Overall, manufacturing output is set to decline, with a recovery in output forecast for 2003. In the service sector, output growth in the South East is likely to slow, especially in transport and communications.
- ▶ The region's ILO¹ unemployment rate is likely to increase again next year to 3.7 %. This rate will then decrease slowly over the next few years.
- ▶ Household income and spending growth are forecast to slow this year, but both will start to speed up again by 2004, with regional income recovering faster than spending.

Over the medium term it is expected that output and employment performance will improve in the South East, along with the UK economy as a whole. South East employment is expected to pick up at a faster rate than the UK.

¹*International Labour Organisation (ILO) Unemployment, the measure used by the Labour Force Survey. This records as unemployed, those who have undertaken no paid work in reference week (i.e. when they are interviewed), are starting, or are available to start work in the next fortnight and have actively sought work in the preceding four weeks. No account is taken of the individual's age, family status or eligibility for unemployment related benefits.*

1.1 Total Output and Industrial Composition

It is forecast that South East GDP will be £140 billion in 2002 (current prices), equivalent to about 15 % of total UK output.

Output per head of population is set to be £17,000 in 2002 (current prices), £1,750 higher than the national average.

Economic growth in the region has averaged just above 4 % a year over the last decade, well above the UK average of 2.8 %. This year, 2.4 % GDP growth is expected in the region.

The largest sector, financial and business services, accounts for just over a quarter of output in 2002.

Financial and business services, distribution, hotels and catering, engineering and transport and communications account for a greater proportion of regional output than nationally. The same is modestly true for construction, though this is more a consequence than a cause of the region's relative economic success.

1.2 Population

The South East population totals around 8.21 million, equivalent to 13.6 % of the UK. The population has grown by nearly 6.5 % in the last ten years, faster than the UK as a whole.

1.3 The Labour Force

The South East has a high economic activity rate across the regions, with 84.7 % of the population of working age either in work or seeking employment. Moreover, ILO unemployment (a more complete measure than the claimant count) of about 3.6 % is significantly below the UK rate of 5.2 %.

The South East labour force currently stands at around 4.31 million, equivalent to 14.4 % of the UK labour force.

About 47.6 % of all working age adults in employment in the region have attained NVQ² level 3 or above, similar to the average for Great Britain as a whole at 47.3 %.

1.4 Employment

For 2002, it is estimated that employment will be around 3.6 million, equivalent to 14 % of UK employment. This is lower than the region's output share because productivity in the South East is higher than the UK average (£29,400), at £31,000 per head (constant prices).

Employment growth has averaged 1.9% a year over the last decade, well above the UK average of 1.1%. This year, employment is expected to fall marginally followed by a small increase of 0.5% in 2003.

Other services (mainly public services), financial and business services and distribution, hotels and catering account for just over three quarters of all employment in the region.

² NVQ Level 3 is equivalent to GNVQ – advanced level, A level or equivalent (2 or more), RSA advanced diploma, BTEC national/ONC/OND etc., City and Guilds advanced Craft, Scottish certificate of 6th year studies (Scottish CSYS) (67%), SCE higher or equivalent (67%), AS-level or equivalent (4 or more), Trade apprenticeships (50%), Other qualifications (10%)

Key Facts

1.5 Incomes and Spending

Incomes in the South East are estimated to be £108 billion this year (household disposable incomes, current prices), equivalent to 15.5 % of UK personal incomes. Incomes have grown by 3.4 % over the last ten years, faster than the UK average (2.8 %).

Spending in the South East is set to reach £97 billion this year in current prices, equivalent to almost 16 % of UK spending. Spending has increased by 3.6 % over the last ten years, slightly faster than the UK average (3.5 %).

1.6 Budget 2002: Implications for the South East

The biggest implication across the UK will be the increase in National Insurance contributions for both employers and employees. This is expected to cost South East business about £560 million a year from 2003³.

Smaller companies received several tax relieves from the budget including:

- ▶ A cut in the small business tax rate from 20p to 19p
- ▶ No corporation tax for small businesses, down to zero from 10p
- ▶ VAT will now have a flat calculation rate to be extended to more businesses
- ▶ Capital gains tax has been cut

One real benefit for larger companies is a Research and Development tax credit set at 25% with the South East representing around 26% of UK R&D business expenditure. At present there appear to be relatively few risks to the continuation of modest to strong growth with low inflation.

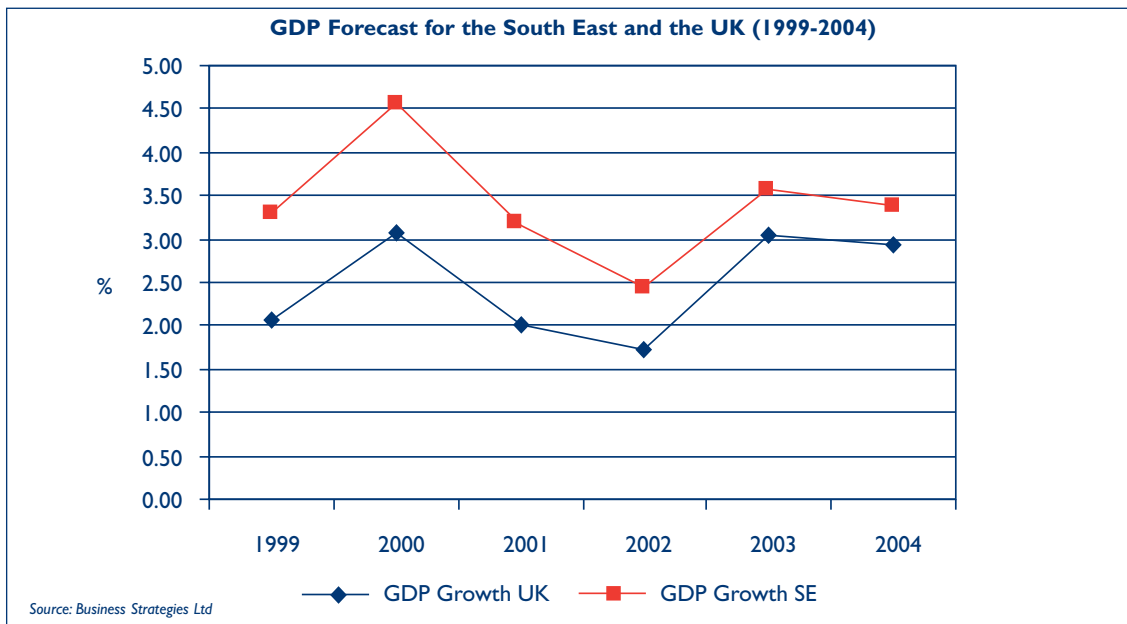
³This figure is based on Business Strategies' estimates.

2. The Short Term Outlook

2.1 Total Output and Sectors

The outlook for the South East is now rather better than was feared a few months ago, as the effects of September 11 have not been as severe as many anticipated. GDP growth for 2002 is expected to be 2.4 %, well above the UK average of 1.7 %.

The UK economy today is in better shape than it was ten years ago. Interest rates are at historically low levels, while public spending is strong, helping to support growth. The South East benefits from this. It is expected that growth in the South East will increase from 2.4 % in 2002 to 3.6 % in 2003.



Nevertheless, manufacturing is expected to continue to struggle this year, mainly due to a continuing slump in engineering. The latest CBI/Business Strategies Regional Trends Survey of local manufacturers shows that business confidence is still deteriorating, albeit at a much-reduced rate.⁴ However, it is predicted that there will be an upturn in 2003 in manufacturing overall. Non-manufacturing output increased last year and this is expected to continue in 2002 with around 3.6 % growth.

Service sector activity is also set to moderate, with the latest British Chambers of Commerce survey reporting that service firms have seen a significant fall in domestic and export sales in the last quarter.

In the service sector, other (mainly public) services and transport and communications are likely to see the lowest levels of growth.

⁴CBI/BSL Regional Trends Survey, February 2002

The Short Term Outlook

2.2 Employment and Unemployment

In the South East, employment growth has slowed significantly and employment is expected to level out this year, although in 2003 employment is forecast to begin a slow increase.

The decline in manufacturing employment is set to continue in the region this year with a drop of about 9,500, mirroring declines elsewhere. This trend is likely to continue over the next few years, although at a slower rate of decline.

A steep decline is forecast in the region's electrical engineering jobs this year, with a drop of almost 7%. Computer manufacturers worldwide have announced large-scale redundancies and a proportion of these are likely to affect the South East.

The airline sector is still suffering from the large-scale restructuring that took place after September 11 and further redundancies are expected in this sector. The first round of redundancies may only just be starting to take effect, with Gatwick and other regional airports being hit. These losses are also having a knock-on effect with aviation suppliers in the region. Companies in the aerospace industry have also been affected, with some companies issuing profit warnings and announcing thousands of redundancies.

The global Information and Communication Technology (ICT) industry slowdown has led many of the companies within the industry to reduce their headcount and delay expansion plans. Because of the size of the ICT industry within the South East this is likely to significantly affect ICT employment levels in the region.

Employment in financial and business services is forecast to remain broadly unchanged, with growth restricted by further consolidation and restructuring. This could particularly affect financial centres such as Milton Keynes, Basingstoke and parts of Surrey.

On the upside, employment in hotels and catering is expected to start to grow again after decreases in 2001. This is partly due to the end of restrictions that were put in place in response to the foot-and-mouth outbreak in 2001 and partly due to some recovery from September 11 problems (although events in the Middle East could still jeopardise that).

It is expected that the ILO unemployment rate will increase again in 2003 from 3.6% to 3.7%, then decrease slowly over the next few years.

2.3 Incomes and Spending

Consumer optimism has continued to hold up despite the background of international economic and political uncertainty. Optimism was higher in the first quarter of 2002 than it was a year earlier.

Strong confidence is reflected in strong consumer spending. National retail sales in February were 1.5% higher than the January figure, comfortably above the same time last year. Many retailers have reported strong sales recently. One supermarket has announced that sales volumes in the fourth quarter of 2001 financial year were the highest in five years.

2.4 The Housing Market

House price inflation has been running at double digits over the last couple of years. While a slowdown in this market is expected, and probably welcome, a meltdown is unlikely.

Survey evidence about house price movements has been mixed but the most recent Nationwide quarterly update of house prices indicates that house prices in the outer South East and other Metropolitan Area continued to increase in the third quarter to £114,586 and £148,546 respectively.

Table 1
House Prices (% change)

	1999	2000	2001	2002	2003
South East	11.1	19.7	9.7	8.6	1.4
UK	10.9	14.9	9.5	4.6	0.4

Source: Business Strategies

Overall, house prices are expected to increase by nearly 10% this year, and are likely to slow next year and the year after.

2.5 Tourism in the Region

Tourism is very important to the region. There is no official measure of the scale of the sector but some estimates indicate total annual revenue of around £3 billion⁵. The sector is clearly going through a difficult period, the latest Office of National Statistics figures show that the number of overseas visitors to the UK declined by 1% in the three months to February 2002, although total spending by overseas visitors to the UK increased by 3% in the same period. The number of overseas visitors to the UK is 10% down on the three months to February 2001.

In 2003 it is expected that hotels and catering employment in the South East (a broad proxy for tourism) will increase by about 1,250 to 226,000. Areas such as Canterbury, Brighton, Oxford and the New Forest continue to be popular with tourists and the region as a whole continues to be one of the main tourist destinations in the UK.

2.6 Inward Investment

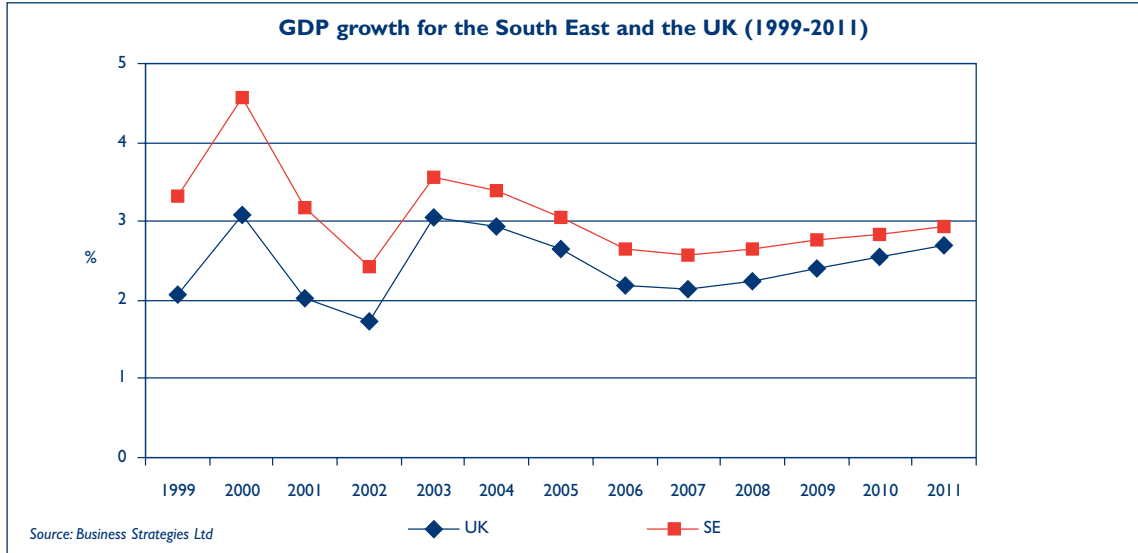
Invest UK's annual review (released July 2002) of inward investment into the UK for the 2001/02 financial year reported that despite the tough global economic conditions, the UK maintained its leading position as Europe's top investment location. Although the number of projects for the UK comprising new investments, expansions and acquisitions fell by 12%, the South East remained the most sought after investment location in the UK for international businesses outside London.

⁵Source: www.tourismsoutheast.com

3. The Medium/Long Term Outlook

3.1 Total Output and Sectors

Over the medium term it is likely that output and employment performance will improve, along with the UK economy as a whole. This is partly due to renewed optimism within the global economy, with more signs from the US that the downturn is not going to be as severe as initially expected. South East employment is forecast to pick up at a faster rate than the UK.



The South East will continue to benefit from a high concentration of fast growing sectors, notably financial and business services and distribution, hotels and catering. Apart from this year, business services will continue to have good rates of growth, although not as high as recent years. There will also be growth in manufacturing, although the sector's share of regional output will tend to fall, reflecting the strong performance from some of the service sectors.

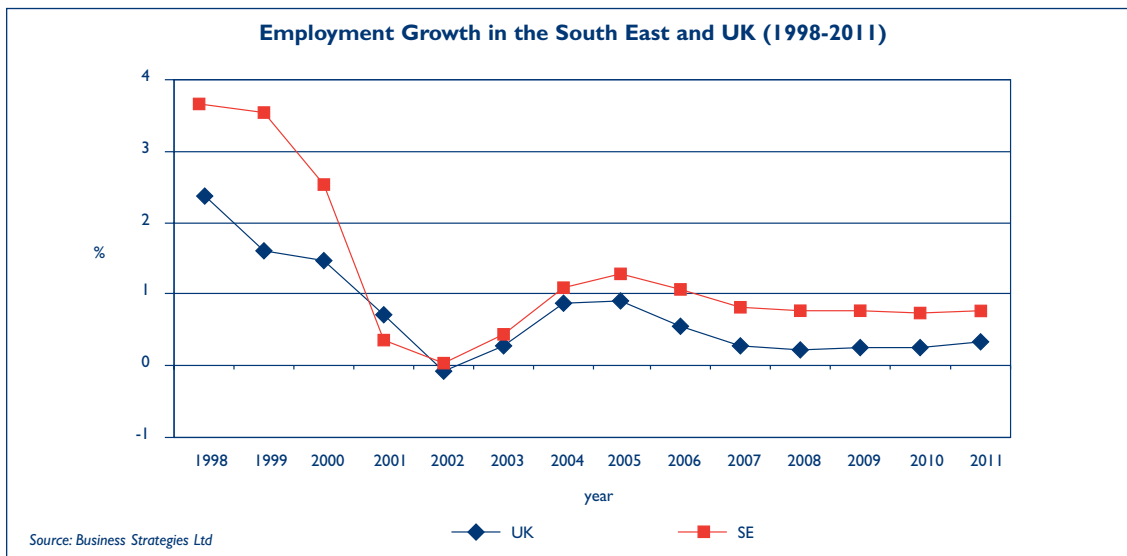
3.2 Employment and Unemployment Prospects

It is likely that employment will increase over the medium term, possibly by about 290,000 by 2011, pushing up the South East's share of UK employment to 14.6 %.

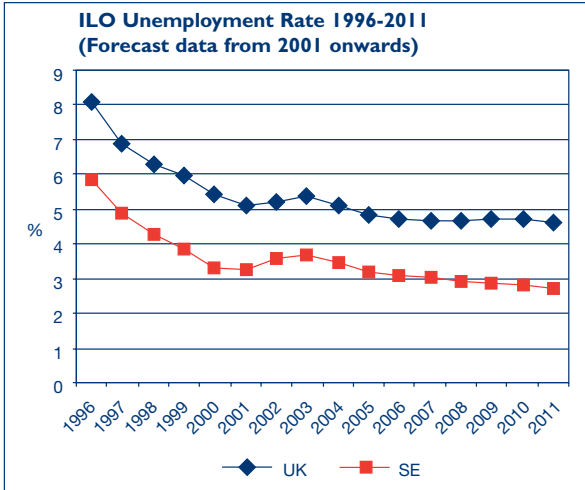
Most of these gains will be seen in distribution, hotels and catering, financial and business services and other services. Agriculture, mining and utilities, metals, minerals and chemicals, engineering, other manufacturing, construction and transport and communications will experience around 98,000 job losses, of which 69,000 will be manufacturing.

Engineering is expected to lose the highest number of jobs, followed by metals, minerals and chemicals and agriculture.

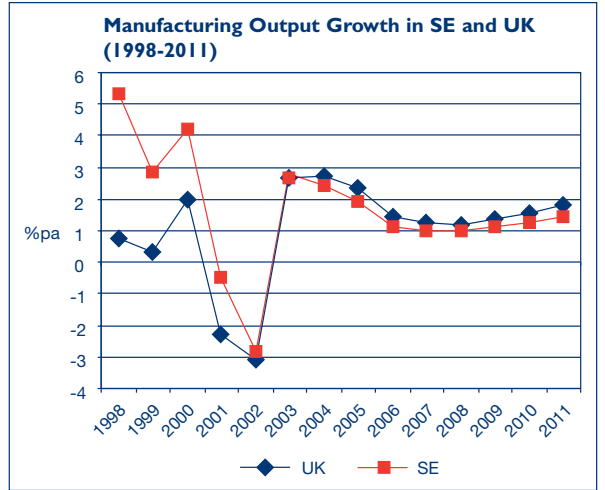
The ILO unemployment rate (a better measure than claimant count) is forecast to be around 3.6 % in 2002, dropping to about 2.7 % in 2011.



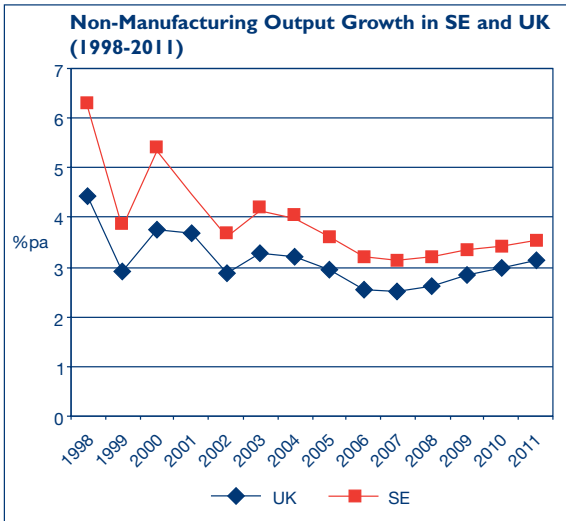
The Medium/Long Term Outlook



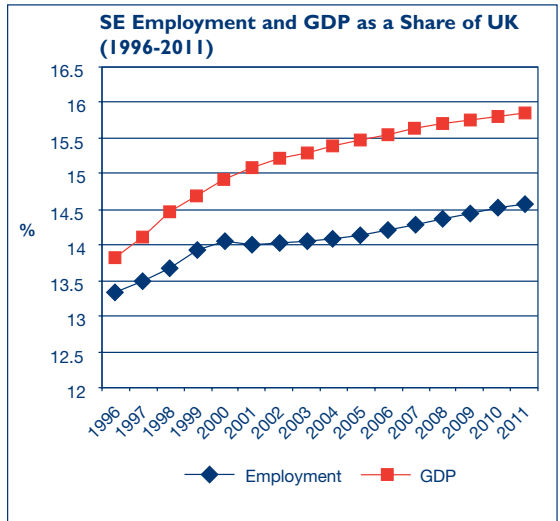
Source: Business Strategies



Source: Business Strategies



Source: Business Strategies



Source: Business Strategies