QUARTERLY

ECONOMIC REPORT
Summer 2009

Covering April to June 2009

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KEY POINTS

Local economic data confirm that the **Tyne & Wear** economy has entered **a deep recession**. Domestic (UK) sales and orders (for firms in TW) fell more steeply in the second half of 2008 and the first quarter of 2009 than in the early 1990s recession (§1); balances were around -25pp in Q1. Source: Chamber of Commerce quarterly surveys.

Export orders, perhaps surprisingly, are reported to have fallen less steeply than in 1998-2000 (mainly the Asian financial crisis of 1998). (Balances[1] fell -15pp or so in Q3, were hardly negative in Q4, before falling around -10pp in Q1).

This sharp Downturn in the real economy in TW **follows the earlier broad halving of house sales volumes**, which occurred in Q1 (of 2008) in the NE and TW (§2).

The **recession** is **clearly deeper than** in the **early 1990s** (which was less severe in TW than nationally), and appears more akin to the early 1980s – at least in terms of the speed of the Downturn. (For the UK, ONS data show that output fell by a record 2.4% in Q1 – reportedly the weakest performance in 50 years).

Note: since these data were recorded (up to March), nationally there have been **some positive signs**; Libor[2] has fallen, retail spending has held up better than some expected, and global commodity prices have risen. Since early March, the banking system has stabilised. The Bank of England said in a new April report that bank lending to companies does not clearly indicate they face a shortage of credit (§8).

NE exports fell by over 12½% in Q4 (over 2½ times as fast as in the UK). There was a slight *relative* improvement for the North East in Q1, with exports falling by 9.7% (compared to a sharp fall in the UK of 12.1%) (§3). The further sharp decline of the NE's major export markets in the EU is a particular concern; in Q1, German GDP shrank 3.8% the Netherlands by 2.8% - which are the NE's top export markets.

Caution: it is not clear to what extent the fall in NE exports was in chemicals and steel (from Teesside) rather than cars from Tyne and Wear.

Reported[3] **job gains exceeded losses by about 476** in Q2. This balance of reported job change is a marked improvement from a net loss of 1,100 in Q1 (§5) Caution: Many job changes are omitted from the press. The *actual* change in employment is almost certain to have been negative. More detail will be given in the TWRI Labour Market Report.

1 The balance is the difference in the proportion of firms who said the variable was rising minus those who said it was falling.

2 Libor is the rate of interest paid between banks.

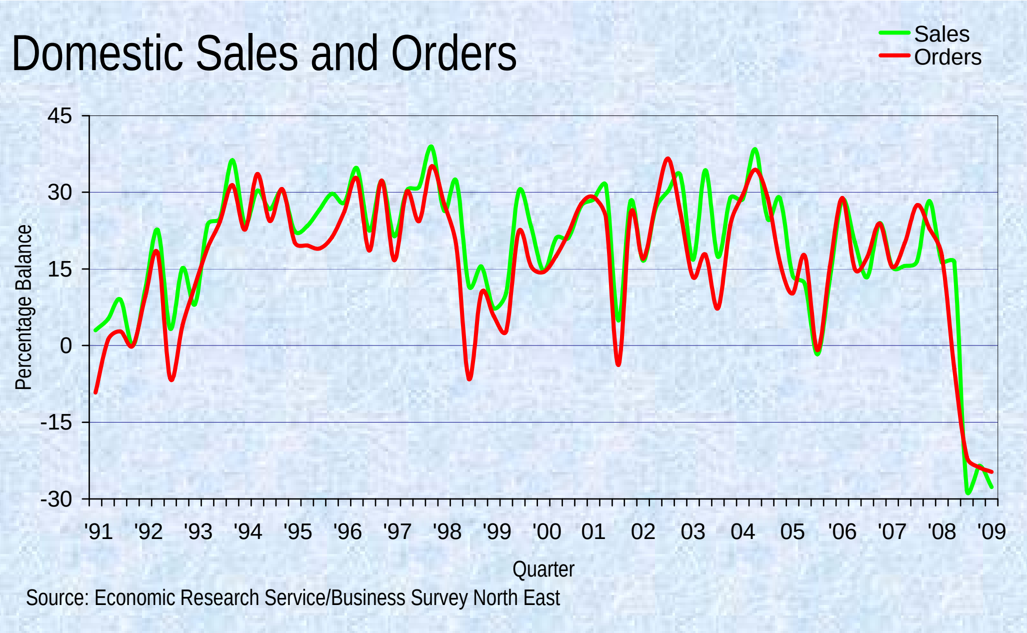
3 Caution: press coverage effectively omits many industries.

TYNE & WEAR ECONOMY

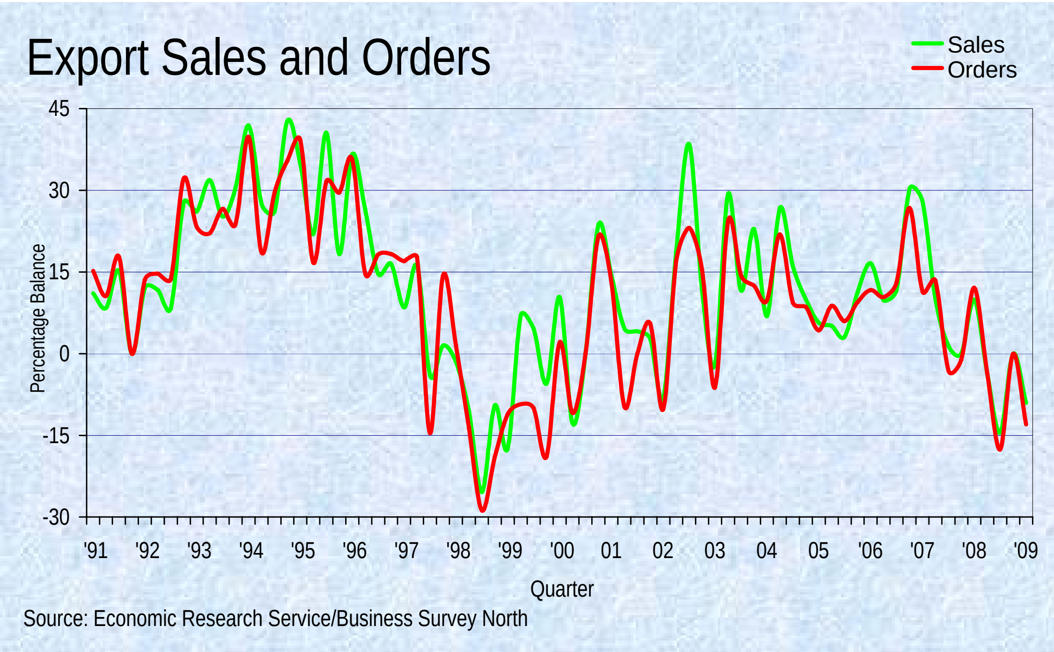
1. Indicators of Demand:

Domestic demand continued to fall in Q1, remaining at a lower depth than in the recession of 1992 (below). Balances have been around -25%, whereas they were no more than around -10% in the recession of 1991-92.

Note: these indicators of demand are from firms in Tyne & Wear (only).

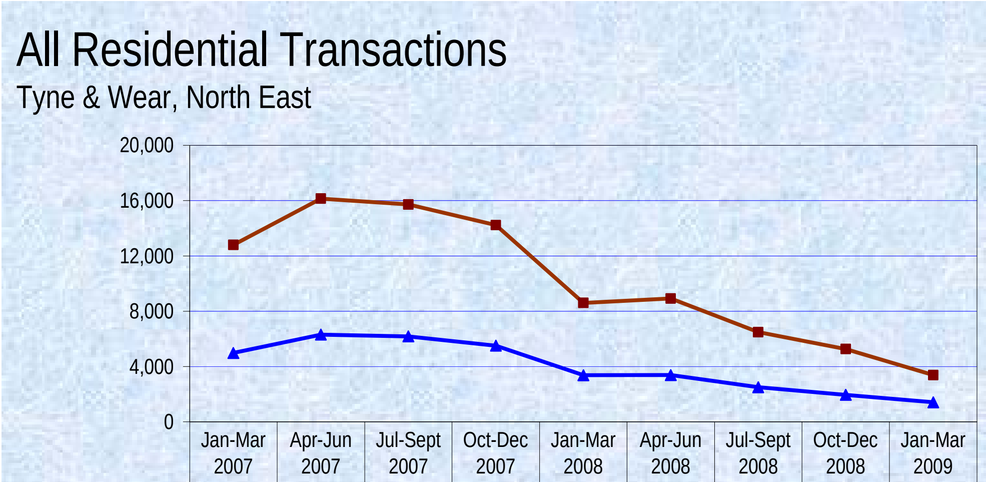


Export demand had fallen to a low level in Q3 (around -15% on the balance measure), but returned to around zero in Q4. However, in Q1 there was a further fall in export demand.



2. Housing Market

Housing market activity has fallen by around 60% beginning with lenders greatly restricting lending (from Q1, 2008). Activity continued to fall throughout 2008 and into 2009 in both the NE and Tyne & Wear (below). Sales in Tyne & Wear fell to under 1,500 in the first quarter; this is under a third of the volume two years earlier.

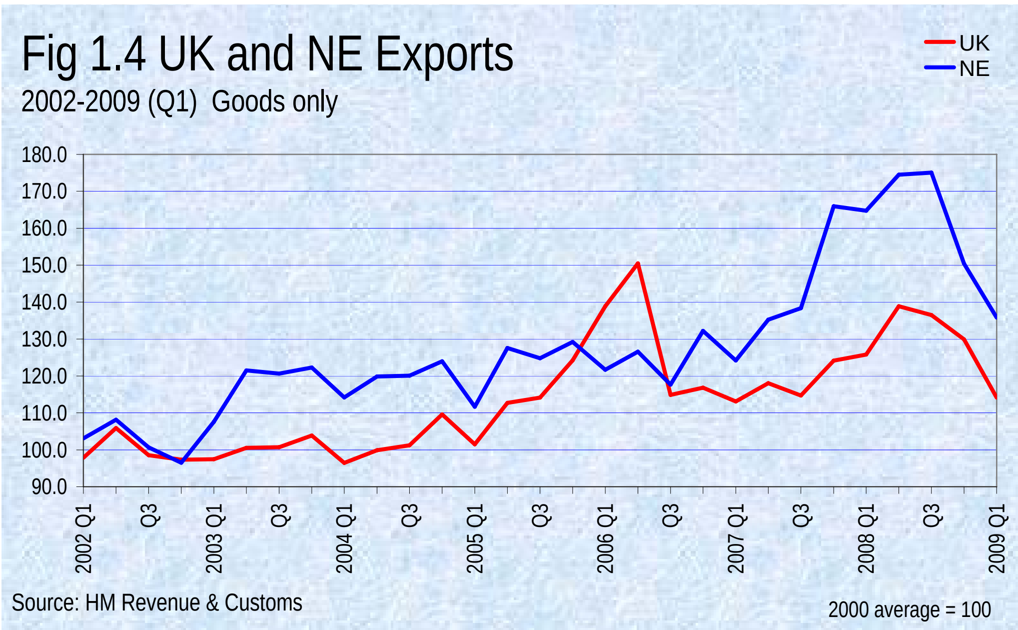


	Jan-Mar 2007	Apr-Jun 2007	Jul-Sept 2007	Oct-Dec 2007	Jan-Mar 2008	Apr-Jun 2008	Jul-Sept 2008	Oct-Dec 2008	Jan-Mar 2009
Tyne and Wear	4,985	6,311	6,185	5,513	3,372	3,390	2,504	1,953	1,409
North East	12,796	16,151	15,722	14,225	8,606	8,922	6,489	5,266	3,380

Source: Land Registry, TWRI.

3. Exports

Exports of goods from the North East[4] fell by 9.7% (by value) in **Q1 2009** (-£248m) to £2,307m. If this lower level remained for a whole year, it would equate to a loss of £0.99bn of exports **worth about 2% of NE GDP**. The silver-lining was that NE exports were still higher than in the first 2 quarters of 2007, because of the boom in exports in the intervening period.



Note: exports may be critical to economic recovery in the medium-term (say 1-5 years).

4 HMRC Tyne & Wear data are not available to TWRI.

The North East had been performing much better than nationally on exports. **NE exports rose by 17%** to **£11.2bn** in 2008. These goods exports are equivalent to about one-fifth of the region's GDP. [It would be good if ONE could provide indicators of international tourists coming to the NE.]

4. Aggregate Job Gains and Losses in TW (Apr-Jun 2009) – reported in the press:

There was a *reported* net job gain for TW of +476, a reversal of the net loss of -1,100 in Q1. The actual change is likely to have been a fall in employment.

The large job losses in Newcastle (900 gross loss from NPower) were due to the transfer of jobs to Sunderland (900 gross gain).

Summary of job gains and losses (announced in the press).

April 1st – June 30th 2009, for Tyne and Wear

District	Gain	Loss	At Risk
Gateshead	375	350	74
Newcastle	819	1,426	50
North Tyneside	465	209	180
South Tyneside	354	469	
Sunderland	1,010	-	
Unallocated*	70	163	
Tyne and Wear	3,093	2,617	304

* Note: Unallocated gains and losses are usually estimates at County level of regional change.

Source: compiled by TWRI from the Journal and other local media.

Caution: press reports are very incomplete. In particular, they essentially omit construction job change, small job losses in retailers and other service firms. Historically they have omitted major growth in public service employment in health and education. Nevertheless, the reported job changes give a strong sense of overall employment change.

Claimant unemployment has risen by about 15,600 in TW in the year to May; this suggests employment may have fallen by 15-20,000 (about 3-4%) in TW.

More details, including an itemised list of gains and losses, will be presented in the TWRI Labour Market Report.

5. Structural Change in the TW economy:

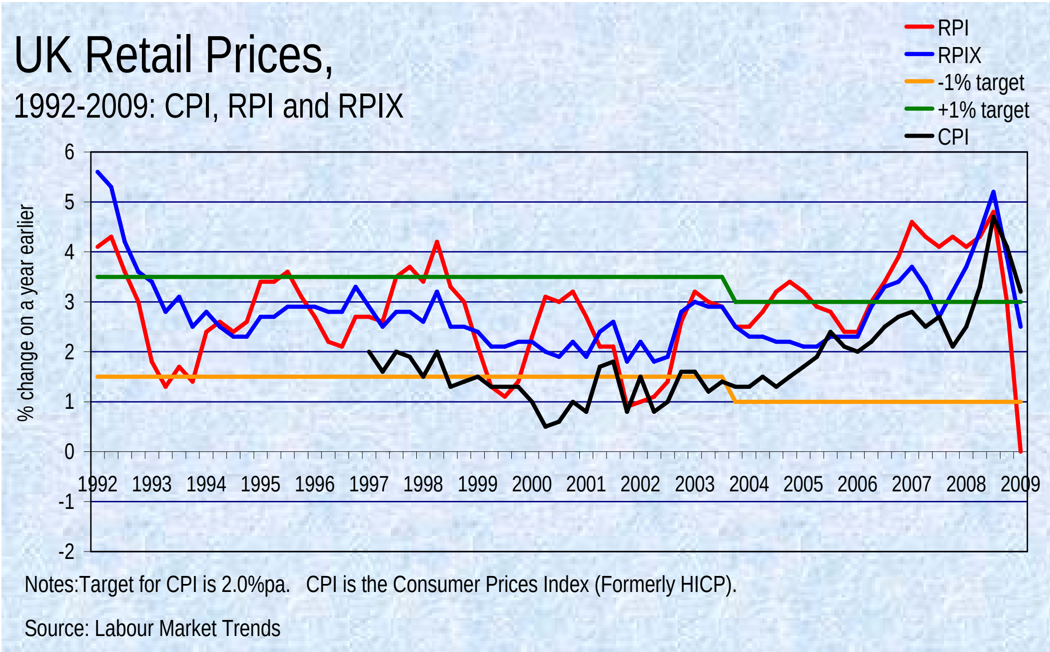
In June, Dairy Farmers of Britain (DFB) announced the closure of its dairy in Gateshead (at Blaydon). As it employs nearly 300 people, this is a major loss from the Food & Drink sector in Tyne & Wear.

In May and June, Nissan has been taking on hundreds of workers following the 1,200 job cuts in January. Competitor GM has been acquired from bankruptcy by a consortium led by Magna (a Canadian parts manufacturer with experience of contract car manufacturing for other car manufacturers). Competitor Chrysler (which makes Jeep, perhaps a substitute for Nissan's Qashqai) is being taken over by FIAT.

UK ECONOMY

6. Economic Context:

Inflation is no longer the problem, RPI inflation fell to zero in February, before falling further to -1.1% in May. CPI inflation was around 3% in February, before falling to 2.2% in May. The Bank of England says it expects inflation to remain below 2% for some years. Oddly, for now, CPI is stubbornly above 2%, despite the downturn.



7. Prospects:

Future UK Economic Prospects are for significant *negative* economic growth in 2009 and very low growth in 2010. Tyne & Wear's economic prospects (for at least the next year or so) are determined largely by the UK trajectory.

	2009	2010	Comments
Economic Growth	-3.7%	+0.7%	Severe downturn in 2009
Claimant Unemployment	2.00m (Q4)	2.28m by Q4 2010	A rise of almost 850,000 or 73%, compared with the December 2008 claimant count. Then a further 280,000 in 2010.
CPI inflation (Q4 in each year)	1.0% and RPI inflation to be -1.3%,	1.7% and RPI inflation to 2.5%,	Deflation is expected across the second half of 2009 (using RPI). But inflation returns in 2010.

Source: average latest revised UK forecasts from HM Treasury's survey of independent forecasts (June).

TW may fare somewhat worse than the UK because of its relatively large export-sector, and dependence on EU markets which have been declining steeply.

8. The Financial Crisis/Credit Crunch – recent developments

The Bank of England introduced a new monthly Lending Report in April. This is largely based upon a survey of the Big Six lenders.

Cautions: this source omits foreign banks which have reportedly largely withdrawn from new lending in the UK. Also, the report focuses on lending to companies, not small businesses. There are no data on lending to the local economy.

The June report states;

- The flow of **net lending**[5] **was negative** in April (-£5.4bn, from £1.3bn in March), the largest monthly fall in lending since June 2000.
- Since the start of the year, the major UK lenders have reported that a number of **companies have refinanced earlier** than usual by using 'forward start agreements'. Under these arrangements lenders agree, often well in advance, to extend a borrower's facility on its expiry.
- The major UK lenders report that the **average maturity of new lending** has **fallen** relative to before the crisis.
- Lenders have continued to report **subdued demand for new loans**, which they partly attribute to weak investment intentions. To some extent, companies may have reduced their investment plans because credit has become more expensive, or harder to obtain.
- **Gross mortgage lending** has **continued to weaken, largely because** of **weaker remortgaging activity**. The major UK lenders reported an increase in approvals for mortgages for house purchases in May. While there are tentative signs of increased mortgage availability, some lenders have pointed to various frictions that might delay the effect on completed housing market transactions and mortgage lending.
- Net flows of consumer credit have remained weak, particularly for unsecured loans – consistent with depressed spending on big-ticket items like cars. Effective interest rates on overdrafts and personal loans have fallen by much less than Bank Rate, and rates on credit cards have remained broadly unchanged, in part reflecting heightened credit risk.

Quantitative Easing

This programme is aimed to support activity in the economy, and remove the risk of failing prices. In May, the MPC voted to continue with its programme of asset purchases financed by the issuance of central bank reserves, and to increase its size by £50 billion to a total of £125 billion. Purchases of over £100billion have been made under this facility since its use for monetary policy purposes was first announced in March. The MPC expected that it would take until August to complete the programme, and it will keep the scale of the programme under review.

Trade Credit Insurance

On May 1st the Government introduced the trade credit insurance scheme. Suppliers will be able to purchase Government-backed insurance to either restore cover to the original level or double the amount they are able to obtain from the private sector up to the value of £1m (whichever is the lower). A maximum of £5bn of top-up cover for insurance will be available through the scheme.

[5] Official data covering lending by all banks and building societies.