

ECONOMIC POLICY CENTRE OUTLOOK SUMMER 2019



A challenging global environment

Much of the current economic data is positive, but the outlook remains cautious. The Northern Ireland jobs market continues to surprise on the upside, with approx. 8,000 jobs created in 2018, that's 78,000 net new jobs since the low point of 2012. In addition, the employment rate is now over 71%, the highest rate since LFS records began in 1992.

The UK economy is also performing reasonably well, almost 350,000 jobs created in the last year and real incomes on the rise. The fiscal position is also positive with tax revenues increasing strongly and a deficit for the year likely to be 1.2% of GDP (compared to 10% at its peak). This all suggests an economy in reasonably good health.

However, the issues are also significant. Nationally business investment remains low and globally the 2017/ 2018 story of growth synchronicity, where the US, China and the EU were all growing reasonably strongly at the same time, has ended. In an inter-connected world, that will have implications locally and nationally.

Key forecasts

Northern Ireland (NI)

	2018	2019	2020	2021	2022
GVA ⁽¹⁾ growth rate	1.2%	1.3%	1.2%	1.2%	0.9%
ILO Unemployment rate ⁽²⁾	3.7%	3.6%	3.5%	3.3%	3.1%
Employment growth	0.9%	0.2%	0.2%	0.6%	0.5%
House price growth	4.6%	5.1%	3.4%	3.2%	2.2%

United Kingdom (UK)

	2018	2019	2020	2021	2022
GVA ⁽¹⁾ growth rate	1.4%	1.7%	1.6%	1.6%	1.2%
ILO Unemployment rate ⁽²⁾	4.2%	4.3%	4.4%	4.3%	4.3%
House price growth	3.3%	4.9%	3.2%	2.7%	1.7%

Macro-economic variables

	2018	2019	2020	2021	2022
Interest rates ⁽³⁾ (end of year)	0.75%	1.00%	1.00%	1.00%	1.00%
Inflation ⁽⁴⁾ (annual average)	2.5%	2.2%	2.2%	1.4%	1.4%

Note 1: Gross Value Added (GVA) is the preferred measure of economic activity. It is similar to Gross Domestic Product (GDP) but excludes the impact of taxes and subsidies (most notably VAT)

Note 2: ILO unemployment rate is the measure of ILO unemployment as % of labour force

Note 3: Bank of England base rates

Note 4: UK Consumer Prices Index (CPI)

Good news overshadowed by global concerns

The economic data continues to give some reason for cautious optimism despite the constant gloomy backdrop. Nationally and locally the labour market continues to create jobs, with employment levels at record highs and unemployment levels correspondingly at or near record lows. The combination of a relatively tight labour market and inflation on a downward trend, has resulted in rising real wages which increased by 2% in Northern Ireland in 2018.

Reliance on consumer spending as a driver for economic growth has been a constant theme in EPC outlooks in recent years, and it remains a problem, but with more people in work earning higher wages, scope for continued growth in consumer spending may remain at least in the short term.

One further good news story is the UK fiscal position. Tax revenues are often overlooked as they have limited predictive powers, but they provide a very accurate picture of the recent health of the economy. VAT receipts were up by over 5%, Corporation Tax receipts increased by over 6% and income tax and capital gains tax up by 8%. The fiscal deficit for 2018/19 was approximately 1.2% of GDP, half the level it was in the last financial year.

It is important to recognise that after many years of Government spending restraint, the public finances are still in negative territory. However, their relative health provides the Chancellor with some fiscal ammunition to ease public sector pay pressures and other spending priorities if the need arises.

So why the doom and gloom?

Firstly, global economic growth is slowing, the IMF is forecasting lower growth for the US, falling from 2.9% in 2018 to 1.9% in 2020. Current strong growth in the US comes on the back of lower taxes but has also resulted in large budget deficits (4.2% of GDP in 2018 increasing to 4.7% in 2019). Deficits on this scale at this stage of the economic growth cycle raise significant concerns for longer term sustainability.

In addition, the risk of trade wars coupled with geo-political risks in the Middle East, Russia/ Ukraine and North Korea has resulted in the IMF projecting lower growth across all major economic blocks this year and next compared to 2018.

Looking closer to home, the UK Household savings ratio is currently 4.5%. It has been below 5% since Q4 2016 and has

not been this low on a sustained basis since before available records in 1963. This suggests the potential for weaker consumer spending growth in the medium term.

Looking forward

The current forecast remains broadly similar to previous outlooks and shows a slowdown in GVA growth. The trend of slowing job growth is likely to continue in the next few years with job creation slowing further in 2019/20, before increasing again in 2021. Our latest forecast estimates just over 39k net new jobs created over the 2018-2028 period, significantly lower than the 78k jobs created in the 2012-18 recovery period.

Importantly, the forecast assumes an orderly exit from the EU, which despite everything, still remains the likely outcome. However, given the heightened uncertainty, the UUEPC continues to publish upper and lower employment forecast scenarios. Typically scenarios are set around best and worst case outcomes, but we have attempted to present a range of more plausible outcomes which could occur depending on the outcome of a wide range local, national and global events.

The optimistic/upper case scenario is consistent with a move towards convergence with the current UK employment rate, which would see over 85k jobs created over the next ten years. In contrast a fall in consumer and business confidence linked to a more severe global slow-down and/or complications associated with Brexit and the absence of a local assembly could result in a squeeze in real incomes and employment growth over the next ten years fall to less than 5k.

TABLE 1:

Sectoral employment forecast 2018-28 across scenarios

	Lower Case (Pessimistic)	Central Estimate (Expected)	Upper Case (Optimistic)
Production & manufacturing	(4,100)	4,500	10,700
Construction	2,300	3,900	6,600
Public sector services	6,300	7,000	15,200
Private sector services	300	23,800	53,100
TOTAL	4,700	39,100	85,400

Temporary contracts and part-time working – more flexible or insecure?

The decade following the 2008 recession has been characterised by the growth in less secure types of employment. In particular temporary contracts, part-time working and self-employment. This has led to significant debate about the quality of jobs created over the same period.

The collective term for this group is ‘non-standard employment’ (any form of employment other than full-time employed). Over the period 2009 to 2017, growth in the numbers of people employed in non-standard employment represented 67% of the total employment growth. Chart 1 shows the increase in employment (in numbers and percentage terms) across each of these groups.

CHART 1: Change in non-standard employment and % increase, NI 2009-17



This trend of higher growth in non-standard employment is generally portrayed negatively, but further analysis suggests it may be that people are now making different choices.

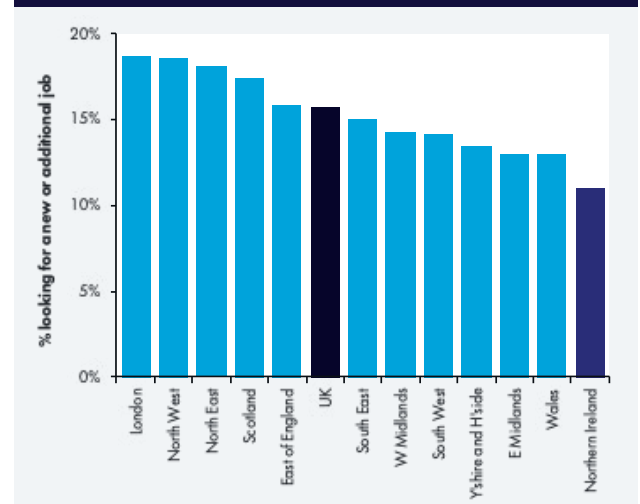
The self-employment rate in Northern Ireland is broadly equivalent to the UK average. However, self-employment is generally seen as an indication of entrepreneurialism and a dynamic economy. It is something to be promoted rather than discouraged and therefore this analysis focuses on temporary contracts and part-time working.

Temporary contracts – on the increase

Temporary workers as a proportion of total employees has increased from 5.6% to 7.2% in the last nine years, which is higher than the UK average but much lower than the OECD average of 11.2%.

The reasons for people taking temporary employment is revealing, 41% indicating that they could not find a permanent job. This seems high and may be a potential cause for concern, but further analysis shows that only 11% are seeking new or additional employment, the lowest in the UK (see Chart 2).

CHART 2: % of temporary workers seeking new or additional job, UK Regions, 2018



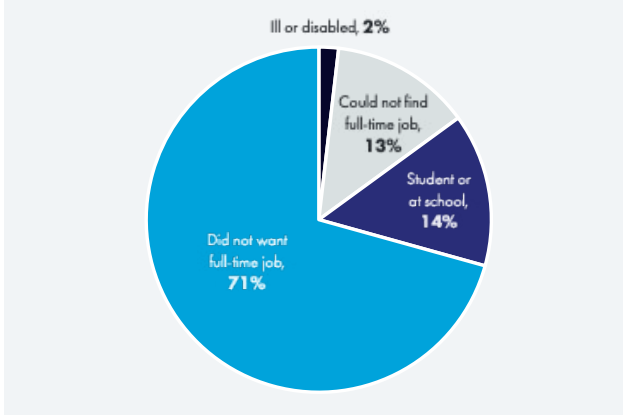
Although many workers find themselves on temporary contracts because they could not find a permanent job, only a small proportion are actively looking for new employment. The lower cost of living in NI is one potential factor but the North East of England also has a relatively low cost of living yet has a high proportion of temporary workers looking for new employment. These findings suggest a certain level of contentment with their current employment status.

Part-time working – a choice for most

Those in part-time employment make up 25% of total employment in Northern Ireland. This varies across council areas, Belfast City Council has the highest proportion of part-time workers at 30% (large numbers of retail and hospitality jobs) compared to the lowest, Causeway Coast & Glens at 22%.

Part-time working has played a very important role in the labour market over the last decade and in most cases, this has been through choice (see Chart 3). 71% of those working part-time did not want a full-time job and only 13% indicated that they couldn't find a full-time job.

CHART 3: Reasons for part-time working, NI (2018)

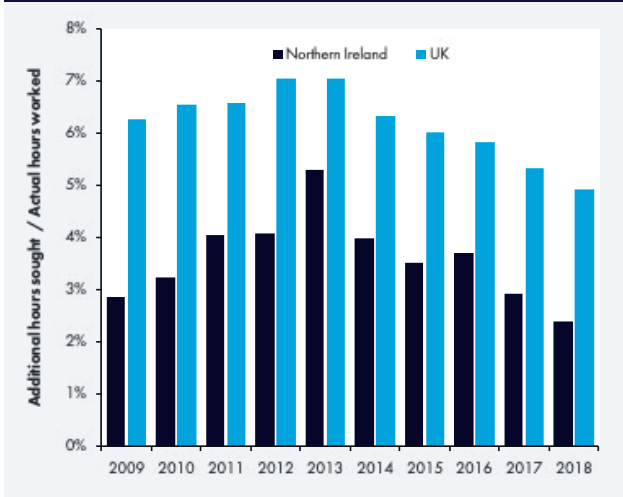


Although this is a positive story overall, there is an important gender perspective. The proportion of female part-time workers who did not want a full-time job is much greater than male part-time workers (76% female compared to just 53% male). This is most likely a legacy of the post-2008 recession, where large numbers of male full-time jobs were lost, for example in construction, and have not been replaced in the same industry.

Under-employment – less of an issue in NI

An under-employed worker is a person in employment working fewer hours than they wish. This is also less of an issue in NI, where only 6.5% of people in employment would want to work more hours, compared to an average of over 10% across the UK. This is also reflected on a standardised measure of additional hours sought (but not on offer from employers), which is 2.4% in NI compared to a UK average of 4.9% (see Chart 4).

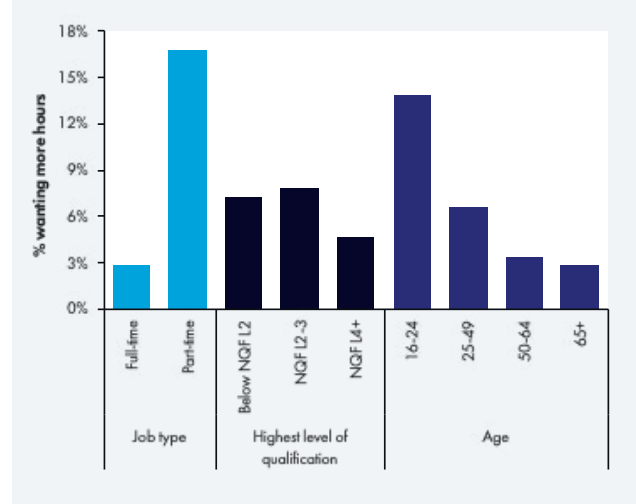
CHART 4: Additional hours sought as % of total hours worked



As economic growth increased from 2012 onwards, opportunities for additional work increased and therefore the level of additional hours sought, over and above actual hours worked, reduced. There has been a consistent gap between UK and NI over the period of this analysis.

However, levels of underemployment are not uniform across all groups in society. Those working part-time, those with lower level skills and young people are more likely to want to work more hours (Chart 5).

CHART 5: Proportion of workers wanting more hours



This is intuitively correct as young people are more likely to be in education and work part-time in sectors such as retail and hospitality which are more suited to part-time working. Conversely, other workers, particularly those with higher levels of skills are highly sought after in the labour market.

Is low wage growth the problem rather than non-standard employment?

It is important not to conflate general attitudes about low wage growth over the last 10 years with a changing trend in labour market contracts. Full-time permanent employment is no guarantee of wage growth, public sector workers have experienced real wage growth stagnation in the last decade, the majority of whom have full-time permanent contracts.

The way people are choosing to work has changed

The evidence would suggest that in most cases people have made a choice not to seek full-time employment and are taking advantage of increased flexibility. Furthermore, the scale of any issue is much smaller in NI than in other parts of the UK.

All that being said, there is a minority for whom the labour market is not providing a solution. In particular, the low skilled, young and male workers find it more difficult to find the employment they want in the modern economy. Even as we are experiencing an increasingly tight labour market, employers will not fill vacancies if applicants do not have the right skills. Therefore putting an onus on skills development and keeping people engaged in education and training is critically important.

Sectoral outlook

Manufacturing

Manufacturing remains the largest employment growth sector in the Northern Ireland economy since 2012, however, this growth appears to have stalled in the last year as a result of the job losses announced in the last few years. Within manufacturing, most jobs have been created in agri-food, up 3.5k since 2012, and most jobs lost in beverage and tobacco products (down 1k jobs in the same period). Unsurprising given the JTI closure, the last tobacco factory in the UK.

Looking forward, the PMI data for the sector is mixed, new business and future output expectations are positive, but employment has gone negative. Clearly the recent Bombardier announcement places a significant cloud over an important part of the sector and may take some time to resolve, but longer term we remain positive about the prospects for manufacturing overall.

Construction

The overall activity story is mixed. In the last year, 'repair & maintenance' grew by 6%, in contrast 'new work' growth was flat, suggesting some reticence in the market to start new projects.

Housing growth was strong, with activity up by over 10% on the year. Infrastructure activity in contrast did not experience any growth, new private infrastructure investment fell, but public infrastructure investment increased (ironically in the absence of an Executive) albeit from relatively low levels.

Looking forward, this mixed performance is likely to continue. House prices in Northern Ireland remain affordable by historic levels which provides a basis for resilience in more difficult economic times, but the bigger challenge is the absence of an Executive required to approve major public investment projects.

Private sector services

Overall, private sector services have been responsible for 48k of the 78k jobs created since 2012. There was a surprising stall in job creation in 2017, but growth returned in 2018. The big challenge for private sector services, is retail. It is the largest sector, employing over 140k, but has struggled to create jobs since the financial crisis. Furthermore analysis of the employee jobs numbers shows that when the sector does create jobs, it is more likely to be wholesale and motor trades, rather than on the High Street.

On a positive note, Professional Services continues to grow strongly, in particular in legal, accounting and management consultancy. The ICT story is similar, with almost all the jobs created being in computer programming and consultancy.

The trend towards more flexible working is confirmed in the Administration Services numbers, with most jobs created in 'Employment Activities' (or agency workers).

Taking a longer term, 10 year, view recent trends are likely to continue in terms of successful sectors, but overall the pace of job creation is likely to be lower.

Public sector services

Employment levels across the public sector have increased by only 8k since 2012, (approx.. 3% compared to a 13% increase in the private sector). As reported previously, the health sector has seen employment increase the most, Education has been broadly flat with reductions elsewhere.

Future levels of public sector employment in the medium to longer term will be entirely dependent on Government policy. These forecasts are based on the assumption of relative fiscal restraint as set out in the latest OBR forecasts. With Government tax revenues continuing to surprise on the upside, there is increased fiscal headroom for greater levels of Government spending which in turn could lead to higher levels of public sector employment.

TABLE 2: Sectoral employment actual and forecast (000's)

Industry	2008-12 (Recession)	2012-18 (Recovery)	2018-28 (Forecast)
Agriculture	0.7	-5.3	-1.1
Mining & quarrying	-0.2	0.1	0.0
Manufacturing	-11.2	17.4	5.5
Utilities	0.0	0.8	-0.1
Water supply & waste	0.4	1.1	0.2
Construction	-25.9	4.6	3.9
Retail	-13.2	2.5	0.6
Transport & storage	-0.6	0.6	1.0
Hospitality	-1.1	7.9	3.2
ICT	-1.0	3.8	4.4
Financial services	-1.5	0.3	0.7
Real estate	0.2	0.1	-0.1
Professional & scientific	-0.1	11.4	5.5
Administration services	-3.3	14.4	5.1
Public admin' & defence	-4.6	-5.5	-0.9
Education	-1.7	2.7	1.3
Health & social work	3.2	11.3	6.6
Arts and entertainment	0.1	3.1	1.6
Other services	-0.3	6.5	1.8
TOTAL	-59.9	78.0	39.1

Post-Brexit manifesto

While Government resources have been focused on negotiating the UK's exit from the EU, attention has been taken away from the development of economic policy in a post-Brexit world. The following ideas have been developed with a view to initiating debate on areas the UK Government and a Northern Ireland Executive may wish to consider to ensure continued economic growth and future prosperity.

Areas of policy consideration

- 1. Regional Migration Policy** – migration dependency and sensitivity to the issue varies significantly across the UK. Northern Ireland has amongst the lowest levels of migration in the UK and issues which may be more prevalent in other parts of the UK are less relevant here. Therefore a regional (i.e. NI-wide) migration policy may support local economic growth.
- 2. Regulatory reform** – reducing regulation and bureaucracy is often cited as a key benefit associated with leaving the EU. Therefore a review should be undertaken to identify regulations which could be amended to give the economy an advantage but maintains appropriate levels of protection, for example to workers and the environment.
- 3. Going global trade policy** – if EU markets are reduced as a result of the UK's exit from the EU, it will be essential that new export markets are exploited. Therefore addressing the barriers to increasing global trade and developing policies to maximise access to global markets should be identified and developed.
- 4. Developing a skills based policy environment** – as economies become more sophisticated and with increased automation, the emphasis on skills will become more important in order to thrive in the 21st Century. Incentivising education and training in economically critical subject areas will be increasingly important to ensure skills supply matches demand.
- 5. Enhancing links between Government, HE/ FE and business** – given the scale of challenges the economy faces, it is important that Government, the tertiary education sector and business work together to maximise the commercial benefit from research and keeping research economically relevant.
- 6. Developing the all-island economy** – how could this be done in a post-Brexit world and what might be the priorities – developing clusters, accelerating knowledge exchange, focus on the border region or the Belfast/Dublin Corridor.

About UUEPC

UUEPC is an independent economic research centre focused on producing evidence-based research to inform policy development and implementation. It engages with all organisations that have an interest in enhancing the Northern Ireland economy. The UUEPC's work is relevant to Government, business and the wider public with the aim of engaging those who may previously have been disengaged from economic debate.

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