North West Brexit Monitor

Key economic and policy developments

February 2018

Executive Summary

Headlines

- **Mixed signals on the state of the UK economy continued during late January and February. Whilst UK GDP was estimated to have grown by 0.5% in the fourth quarter (Oct-Dec) of 2017** (up from 0.4% in Quarter 3 and 0.3% expansion in Quarter 2) **annual GDP growth was estimated to have slowed to 1.8% in 2017**, down from 1.9% in 2016, and the lowest annual outturn since 2012.
- Finance and business services helped drive UK services growth. However**, squeezed real incomes are putting pressure on consumer facing industries**. The distribution, hotels, restaurants sector grew 0.5% year-on-year, compared to 5.2% in the comparable period in 2016. Manufacturing continued with a second straight 1.3% quarter-on-quarter rise, outpacing services for the first time in seven years.
- **The World Economic Forum meetings in Davos opened with the IMF reporting that world growth last year was the best for five years**, and will continue to strengthen throughout 2018/19. Growth of 3.7% is predicted for the world in 2018 with India heading at 7.4% and China growing at 6.6%. However, according to the IMF, the main 'improvers' are found in the 'slower-growing' developed world.
- **Euro Area growth is predicted to be 2.2%, ahead of the UK at 1.5%.** This has led to some economic commentators highlighting that growth in EU and global trade could shield the UK economy from a Brexit shock, and **emphasis should be placed on rebalancing the economy outside of the South East to capitalise on the UK's full potential.**
- Late January and February saw Brexit talks continuing to progress. **European Chief Negotiator for the United Kingdom Exiting the European Union, Michel Barnier reiterated the EU's position on transitional arrangements following the UK's exit from the EU on 29 March 2019**: Any transition period will last until 31 December 2020; during a transition all EU regulations and requirements would continue to apply to the UK, including any new EU rules enacted during this period; **and the UK will remain bound by the obligations stemming from all existing EU international agreements**.
- February also saw increased pressure on government to release **Brexit impact assessments** following a leaked government analysis indicating a pessimistic outlook for the economy post-Brexit. **The analysis concludes that alternative arrangements would likely reduce economic growth in the UK by between two to eight percentage points over the next 15 years compared with current forecasts**. However, **the analysis suggests that the impacts would be more acute in the North West**, with growth anticipated to be cut by between 2.5 and 12 percentage points, making it among the worst hit regions along with the North East, West Midlands, and Northern Ireland

Key sectors & business investment

- According to the **IHS Markit Regional Purchasing Managers' Index** (PMI), growth in business activity fell in the North West in January 2018, with the PMI dropping from a three-year high of 60.7 in December to 57.4 (above 50 = growth). This places the North West as third best performing region in the UK after the East Midlands (58.8) and Northern Ireland (58.7).

Executive summary

- **The IHS Markit/CIPS UK Manufacturing PMI® fell to 55.3 in January 2018 from December's reading of 56.2, indicating continued growth but at a slower pace (down from November's 51-month high of 58.2)**. It was the weakest pace of expansion in manufacturing since June last year. Meanwhile, jobs were added at a faster pace and the trend in new export orders strengthened, due to higher sales in North America, China, mainland Europe, Middle East and Japan. Input cost inflation also rose to an 11-month.
- **The IHS Markit/CIPS UK Services PMI® fell to 53 in January 2018 from 54.2 in the previous month,** the weakest pace of expansion in the service sector since September 2016, amid a loss of existing clients and concerns surrounding the UK's exit from the EU. However, despite slower growth, the rate of job creation rose on average in the UK to a four-month high. Input costs also rose at a robust pace amid higher prices for insurance, fuel, transport and food in particular.

Terms of trade, regulation & access to funding

- Prime Minister Theresa May has indicated she **will fight a proposal to give residency rights to EU citizens during the transition period** after Brexit, stating that there has to be a difference between those arriving after the UK leaves and those arriving before.
- **The EU has raised concerns over the possibility of Britain undercutting the continent's economy after Brexit by slashing taxes or relaxing regulation**. Brussels has described the UK economy as too big and too close to treat like a normal trade partner and wants to define new ways to enforce restrictions on taxation, state aid, environmental standards and employment rights.

Property investment, housing and planning

- **Housing data from the Land Registry continues to show that the vote to leave the EU has had little impact on house prices,** with average house prices in the North West rising by 7.3% on the level recorded in July 2016.
- **In 2017 the North West took up 4% of Grade A industrial and logistics floorspace in the UK**. This places the NW above the North East, Scotland, Wales, and Yorkshire & Humberside, but the West & East Midlands and the Greater South East still take the majority of grade A floorspace, together accounting for 85% of the UK total.

Economic inclusion

- **Unemployment in the North West has continued to grow above that seen prior to the referendum result – rising from 104,435 in June 2016 to 110,175 in December 2017 (latest).** January data on household finances also revealed a sharp squeeze on UK residents driven by continued rises in living costs and corresponding decline in cash available to spend, and rising demand for unsecured debt.
- **The seasonally adjusted Household Finance Index, which tracks Britons' sense of financial wellbeing, registered 43.0 in January**, below December's 43.7 (an index of below 50 signals deterioration in perceived levels). Moreover, December data revealed that household's expectations of future inflation reached a 47-month high.
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Macro-economic trends and developments

Macro-economy

- **UK GDP was estimated to have grown by 0.5% in the fourth quarter (Oct-Dec) of 2017**, which marks a slight acceleration from the 0.4% growth recorded in Q3 and a second consecutive quarter of improved growth following a 0.3% expansion in Q2. **Despite the uptick in economic activity in the second half of the year, annual GDP growth was estimated to have slowed to 1.8% in 2017**, marking not only a decline from the 1.9% recorded in 2016, but the lowest outturn since 2012.[(1)]
- **The services sector – driven by business services and finance – grew by 0.6% in Q4**, while production industries also grew by 0.6%, boosted by a second consecutive quarter of strong growth in manufacturing. However, this was offset by a decline in construction activity, as the sector contracted for the third quarter in a row.
- **The total UK trade (goods and services) deficit narrowed by £2.1 billion to £6.2 billion in the three months to November 2017**; excluding erratic commodities, the total deficit narrowed by £1.2 billion to £6.1 billion. This narrowing of the total trade deficit was driven by a narrowing of the trade in goods deficit, which came as a result of increasing exports.[(2)]
- **EU trade: The UK was a net importer from the EU in November 2017, with imports exceeding exports by £7.6 billion.** EU Exports for November 2017 were £15.1 billion, an increase of £0.6 billion (4%) compared with October 2017, and an increase of £1.3 billion (10%) compared with 12 months ago. EU Imports for November 2017 were £22.7 billion, a decrease of £0.4 billion (2%) compared with October2017, and a decrease of £0.2 billion (1%) compared with a year ago.
- **Non-EU trade: The UK was a net importer in November 2017, with imports exceeding exports by £5.3 billion**. Non-EU Exports for November 2017 were £15.2 billion, a decrease of £0.1 billion (1%) compared with October 2017, and a minimal decrease of 0.2% compared with a year ago. Non-EU Imports for November 2017 were £20.5 billion, a decrease of £1.1 billion (5%) compared with October 2017, but an increase of £0.8 billion (4%) compared with a year ago.[(3)]
- **The World Economic Forum meetings in Davos opened with the IMF reporting that world growth last year was the best for five years.** According to the IMF, the main 'improvers' are found in the 'slower-growing' developed world. **The US is forecast to grow by 2.7% in 2018, the Euro Area's growth predicted to be 2.2%, ahead of the UK at 1.5%.** This has led to some economic commentators highlighting that growth in EU and global trade could shield the UK economy from a Brexit shock, and **emphasis should be placed on rebalancing the economy outside of the South East to capitalise on the UK's full potential.**[(4)]

Consumer sentiment

- **The Consumer Prices Index including owner occupiers' housing costs (CPIH) 12-month inflation rate was 2.7% in December 2017, down from 2.8% in November 2017**. Following a steady increase from late 2015, since April 2017 the CPIH rate has levelled off, ranging between 2.6% and 2.8%.[(5)]
- **The volume of retail sales fell by 1.5% in December 2017 compared to November 2017, but rose by 1.4% compared with December 2016**. The underlying pattern in the retail industry in November 2017 (three-month on three-month measure) remains growth, with the quantity bought increasing by 0.4%. However, this was the **weakest quarterly growth since a decline of 1.2% in Q1 2017**.[(6)]

Key sectors & business investment

Business Investment

- According to the **IHS Markit Regional Purchasing Managers' Index** (PMI), growth in business activity fell in the North West in January 2018, with the PMI dropping from a three-year high of 60.7 in December to 57.4 (above 50 = growth). **This places the North West as third best performing region in the UK after the East Midlands (58.8) and Northern Ireland (58.7).**
- At the national level, all regions continue to see growth, with PMI Index for England at 54.0 in January 2018, down from 55.5 in December. **All regions saw a rise in private sector employment in January, with the North West and East of England leading with the strongest rates of job creation**. January's data however also indicated an increase in inflationary pressures, with the North West seeing the steepest rise in average prices charged for goods and services after Wales.(7)

CIPS UK Manufacturing PMI to end January 2018

- **The IHS Markit/CIPS UK Manufacturing PMI® fell to 55.3 in January 2018 from December's reading of 56.2, indicating continued growth but at a slower pace (down from November's 51-month high of 58.2)**. It was the weakest pace of expansion in manufacturing since June last year. Meanwhile, jobs were added at a faster pace and the trend in new export orders strengthened, due to higher sales in North America, China, mainland Europe, Middle East and Japan. Input cost inflation rose to an 11-month high (almost the highest on record) amid rising oil prices.(8)

CIPS UK Services PMI to end January 2018

- **The IHS Markit/CIPS UK Services PMI® fell to 53 in January 2018 from 54.2 in the previous month,** the weakest pace of expansion in the service sector since September 2016, amid a loss of existing clients and concerns surrounding the UK's exit from the EU. However, despite slower growth, the rate of job creation rose on average in the UK to a four-month high. Input costs also rose at a robust pace amid higher prices for insurance, fuel, transport and food in particular. The overall rise in costs was nonetheless the smallest since September 2016.(9)

Trade, regulation and access to funding

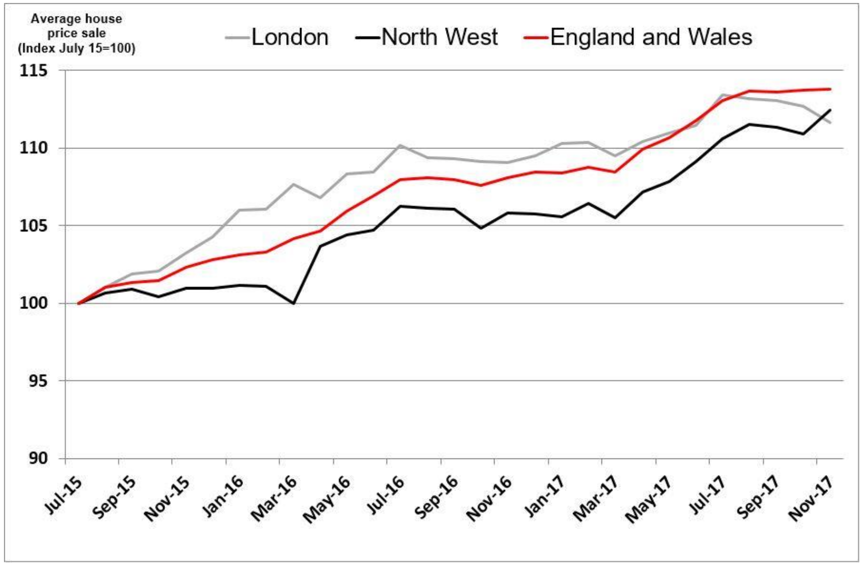
Trade, rules and regulatory developments

- **February saw increased pressure on government to release Brexit impact assessments following a leaked government analysis in January indicating a pessimistic outlook for the economy post-Brexit**. The paper, entitled *EU Exit Analysis — Cross Whitehall Briefing* and dated January 2018, looks at three of the most plausible Brexit scenarios: a "no deal" scenario, under which Britain reverts to World Trade Organization rules; a free-trade agreement with the EU; and a 'soft Brexit' option of continued Norway-style access to the EU single market through membership of the European Economic Area.
- **The analysis concludes that these alternative arrangements would likely reduce economic growth in the UK by between two to eight percentage points over the next 15 years compared with current forecasts**. However, **the analysis suggests that the impacts would be more acute in the North West**, with growth anticipated to be cut by between 2.5 and 12 percentage points, making it among the worst hit regions along with the North East, West Midlands, and Northern Ireland.(10) The analysis further suggests that Britain would suffer a larger hit to growth in the event of a so-called hard Brexit compared to a forecast produced by the Treasury before the 2016 referendum on EU membership**, with financial services, manufacturing, and retailing among the industries worst hit.**(11) A 'Norway-style' deal has been ruled out by prime minister Theresa May, while Downing Street has insisted Britain will not be part of a customs union with the EU, but has not clarified when it will move to new trading arrangements.(12)
- European Chief Negotiator for the United Kingdom Exiting the European Union Michel Barnier has reiterated **the EU's position on transitional arrangements following the UK's exit from the EU on 29 March 2019**, stating that "The EU position is very clear": The transition will last for 21 months, until 31 December 2020, during this limited period of time, the whole EU acquis will continue to apply to the UK. As well as the full EU supervision and enforcement framework, under the jurisdiction of the European Court of Justice, this will include new EU rules entering into force during this period. **As part of the transition, the UK will remain bound by the obligations stemming from all existing EU international agreements**, for instance on trade and aviation.(13)
- Prime Minister Theresa May has indicated she **will fight a proposal to give residency rights to EU citizens during the transition period** after Brexit, stating that there has to be a difference between those arriving after the UK leaves and those arriving before. The European Parliament's Brexit lead, Guy Verhofstadt, responded saying that Citizens' rights during the transition are not negotiable.(14)
- **The EU has raised concerns over the possibility of Britain undercutting the continent's economy after Brexit by slashing taxes or relaxing regulation**. Brussels has described the UK economy as too big and too close to treat like a normal trade partner and wants to define new ways to enforce restrictions on taxation, state aid, environmental standards and employment rights.
- **The negotiators said any deal on future relations had to "cater to the specificities" of the UK-EU relations — implying the "depth and breadth" of relations justifies tighter controls than those expected of the US, Japan or Canada**. Noting such strict curbs do not feature in standard trade deals, the EU paper argues innovative mechanisms will be needed to keep the UK in check, either through conditions in a trade agreement, or though separate retaliatory measures.(15)

Property and investment, housing, and planning

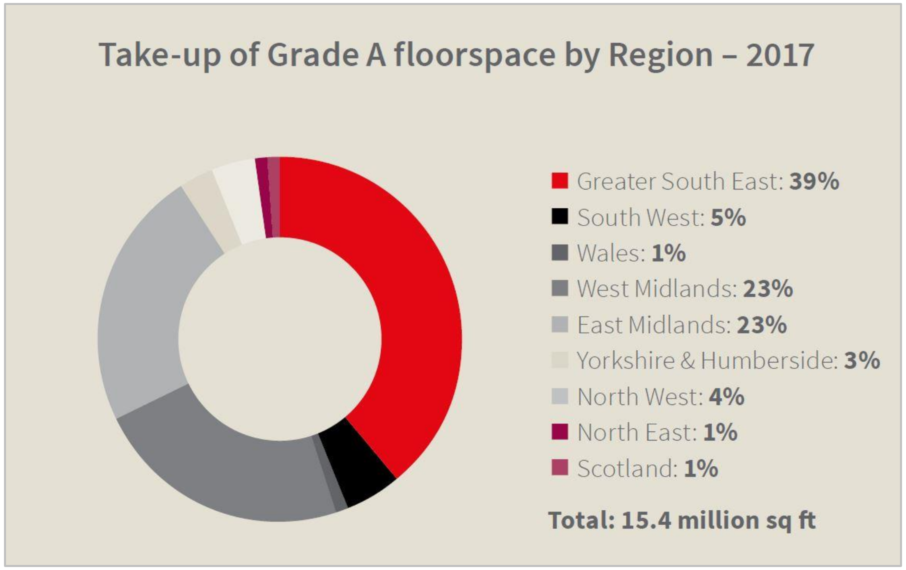
- **Housing data from the Land Registry continues to show that the vote to leave the EU has had little impact on house prices,** with average house prices in the North West in November 2017 (latest) rising by 7.3% on the level recorded in July 2016.
- **In 2017 the North West took up 4% of Grade A industrial and logistics floorspace in the UK**. This places the NW above the North East, Scotland, Wales, and Yorkshire & Humberside, but the West & East Midlands and the Greater South East still take the majority of grade A floorspace, together accounting for 85% of the UK total.

Average House Prices Sales (Index July 2015=100)



- **Housing Index** data from the Land Registry suggest the vote to leave the EU continues to have little impact on house prices, with moderate growth in average residential prices this period.
- **The latest house price data (November 2017) for the NW reveals an average price of £159,065**, an increase of 1.4% from the previous month, and growth of 6.2% from November 2016.(16)

Property Demand: Industrial & Logistics Grade-A Market

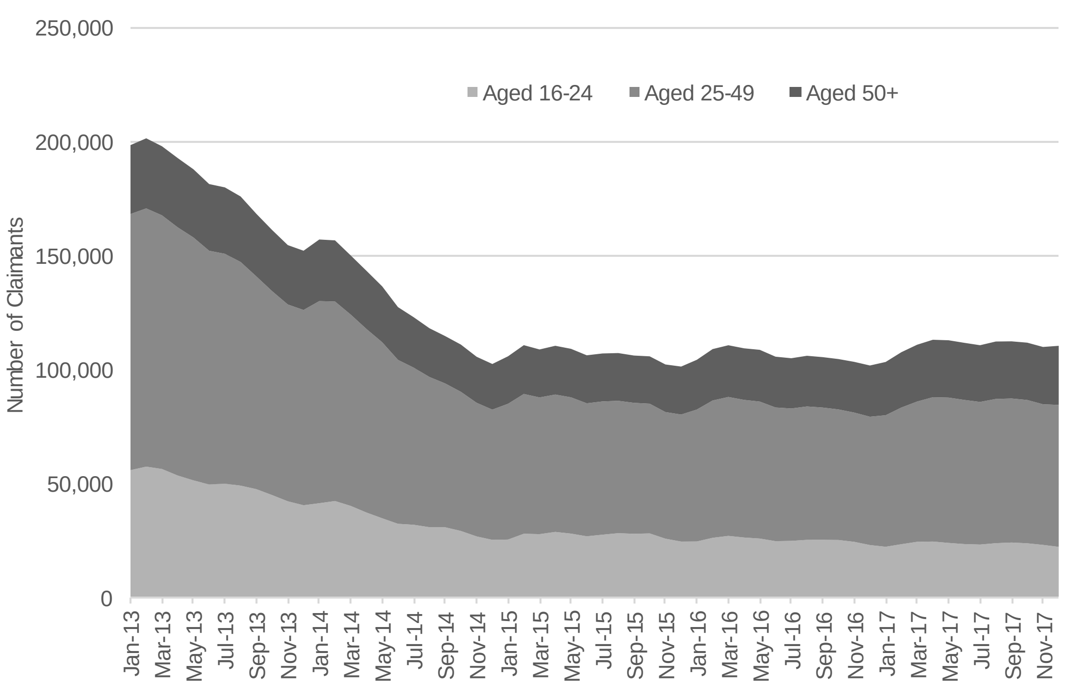


- According to JLL's UK Big Box Industrial and Logistics Market report, **out of a total of 15.4 million sq ft of Grade A industrial and logistics floorspace in the UK in 2017, the North West's take-up was 4%.** This Places the NW just above Yorkshire and Humberside and below the South West; and some way behind the Midlands.
- **Only the Greater South East, Wales, and the North East saw a rise in take-up in 2017** – however both Wales and the North East had seen no Grade A space taken-up in 2016.(17)

Economic Inclusion

- **Unemployment in the North West has continued to grow above that seen prior to the referendum result – rising from 104,435 in June 2016 to 110,175 in December 2017 (latest).** Unemployment as a proportion of the working age population has similarly risen from 2.3% in June 2016 to 2.4% in January 2018. Compared to the same month last year, **unemployment as a proportion of the working age population has increased marginally, rising from 2.2% in December 2016**. This roughly is in line with national trends across the UK, where unemployment has risen from 1.8% in December 2016 to 1.9% in December 2017.(18)
- January data revealed a squeeze on UK household finances, driven by continued rises in living costs and corresponding decline in cash available to spend, reflected in increasing demand for unsecured debt. **The seasonally adjusted Household Finance Index (HFI) – which tracks Britons' sense of financial wellbeing – registered 43.0 in January**, below December's 43.7 (an index of below 50 signals deterioration). Moreover, December data revealed that inflation expectations reached a 47-month high.(19)

Claimant count (JSA and out-of-work UC) in the North West by age group



Monthly Unemployment by age of resident

- As a proportion of working age residents, the **North West claimant rate for December 2017 (2.4%) remains above that of the UK (1.9%)**.
- **In December 2017, the total claimant count in the North West for the 16 to 24 age group fell by 3.7% (845) from November 2017.** In the 25 to 49 age group however, it increased slightly by 0.9% (580), and for the 50+ age group it increased more significantly, by 3.1% (775).
- The total claimant count grew by 0.5% (505) between November to December 2017.
- **Since the referendum result in June 2016, the number of claimants aged 50+ has increased by 16.3%** (3,635), although the number of claimants aged 16 to 24 has decreased by 10.2% (2,485). The number of claimants aged 25-49 has grown by 6.2% (3,620).(18)

Sources (1)

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