# Regional Monitor April 2018

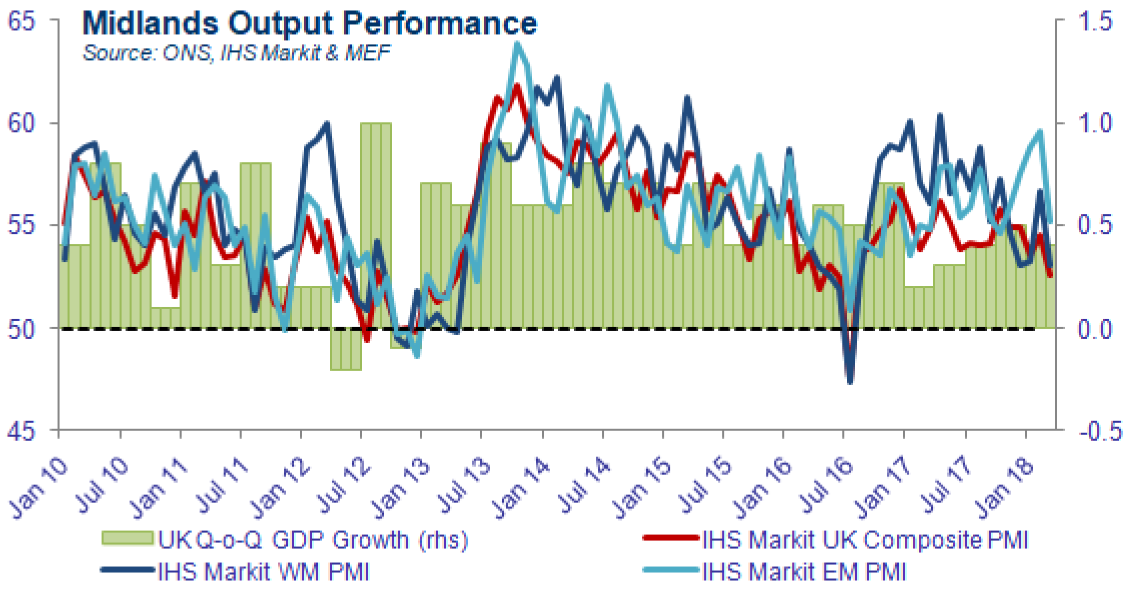
***Latest Global Trends, Regional PMI, Output Data, Trade Conditions & Brexit Update***

***Days since Article 50 activation: 379*** ***Conclusion of Negotiations October 2018***



- Midlands continues to outperform the UK, with the EM again recorded as the fastest growing region, although the rate is softening.
- EM PMI 55.2 from 59.6 in February, WM PMI 53.0 in March from 56.6 previously. UK composite PMI also softens from 54.5 in February to 52.5.
- Price pressures increase, notably in manufacturing.
- Employment demand in the Midlands continues to be stronger than elsewhere in the UK.
- Poor weather affected business output for the construction and services sectors in March.
- Transition deal parameters agreed with the EU, suggesting that the UK will remain in the EU until 2020.
- Election results in Hungary add pressure to the EU from the Visegràd group, possibly impacting the Brexit negotiations.

The EM saw a softening in growth in March, posting a PMI of 55.2 from 59.6 in February, although it remained the fastest growing region in the UK on a PMI basis. The WM PMI was also slightly lower from 56.6 in February to 53.0 in March. Nevertheless, growth in both the EM and the WM outpaced that in the UK overall, with expansion in new orders from new clients and for export, with the UK composite PMI down to 52.5 in March from 54.5 in February.




***Julian Beer, Deputy Vice-Chancellor at Birmingham City University** commented: "Output growth in the region remains locked in a growth trajectory. Nevertheless, a range of factors could dampen this performance, of which Brexit is only one. The marked shift in market demand from diesel is already impacting on local automotive manufacturing and concerns regarding the fragility of global growth could erode export demand. Most significantly however are the worsening tensions between the USA and Russia, and their respective allies. Market attention will surely focus on what, if any, exit strategy they can both agree on."*

The UK Manufacturing PMI sustained growth levels in March, slightly up to 55.1 in March from 55.0 in February. In particular, businesses noted a rise in new export orders, citing an improved exchange rate for the increase.

This trend was reflected in the ONS short term indicators, which showed growth of 0.6% in manufacturing in the three months to February, with basic metals and machinery & equipment being the two largest growth sectors. However, the overall production indicator showed a decline of 0.1% over the same time period, due to the closure of the Forties Pipeline System.

Notwithstanding the recent job losses announced at JLR, in the Midlands, manufacturers saw expansion in March with a rise in new orders for export reflecting the national data. Raw materials costs increased for manufacturers in the region, outpacing the growth in the UK as a whole, with the shortage of skilled labour also being a cost factor for businesses in the WM, as well as leading to a rise in backlogs of work. This may have contributed to a slight decline in optimism in the WM, but optimism increased in March for firms in the EM.

Unusually bad weather was cited as the main reason for the UK Construction PMI to fall to 47.0 in March from 51.4 in February, as it disrupted both work and the availability of staff. Nevertheless, job creation in construction remained at robust levels, and a lower value of Sterling led to the cost pressures on raw materials such as metal and insulation abating somewhat.

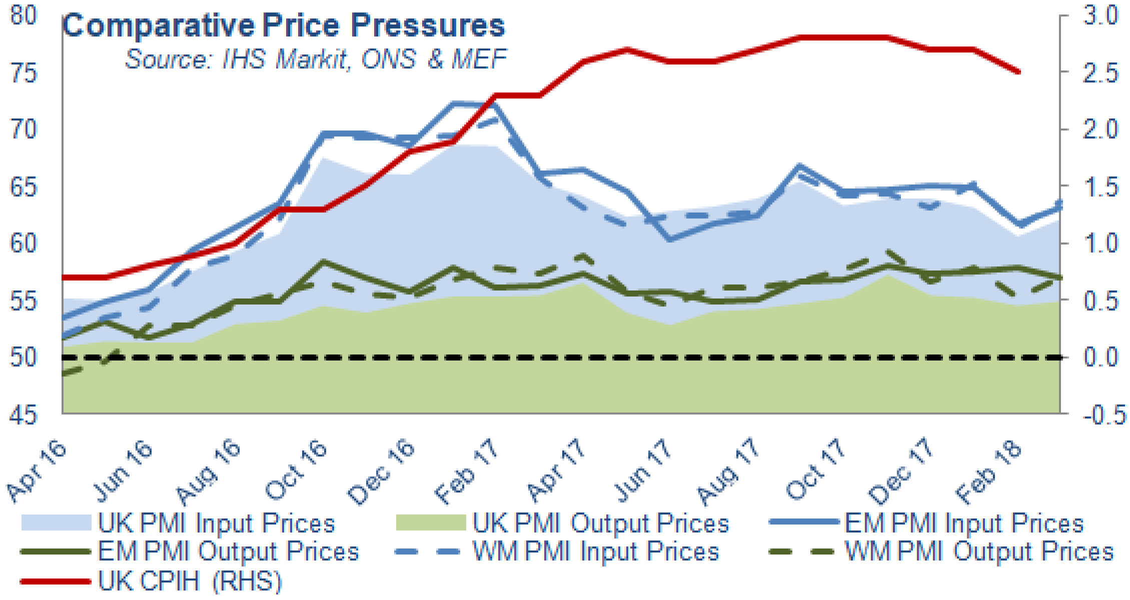


The recent unevenness of growth in the construction sector was reflected in the ONS Construction Output in the UK index, which fell by 0.8% in the three months to February. Once again, unusually bad weather acted as a dampener for growth, although private housing and infrastructure maintained modest growth levels.

Service sector firms were also impacted by bad weather in March, with the UK Services PMI falling to 51.7 in March from 54.5 in February, signalling that growth in the sector has slowed. Marginally lower consumer demand led to lower levels of new business, and recruitment increases were more moderate. Cost pressures remained acute, with utilities, salaries and food and drink costs all cited, and consequently, prices charged also rose in March.

In line with overall PMI data for the region, the service sector grew faster in the Midlands than in the UK overall. Demand from both existing and new clients led to increases in backlogs of work, and consequently employment demand was strong. In the WM, service sector firms also saw price pressures increase, but at a more moderate pace than for the manufacturing sector.

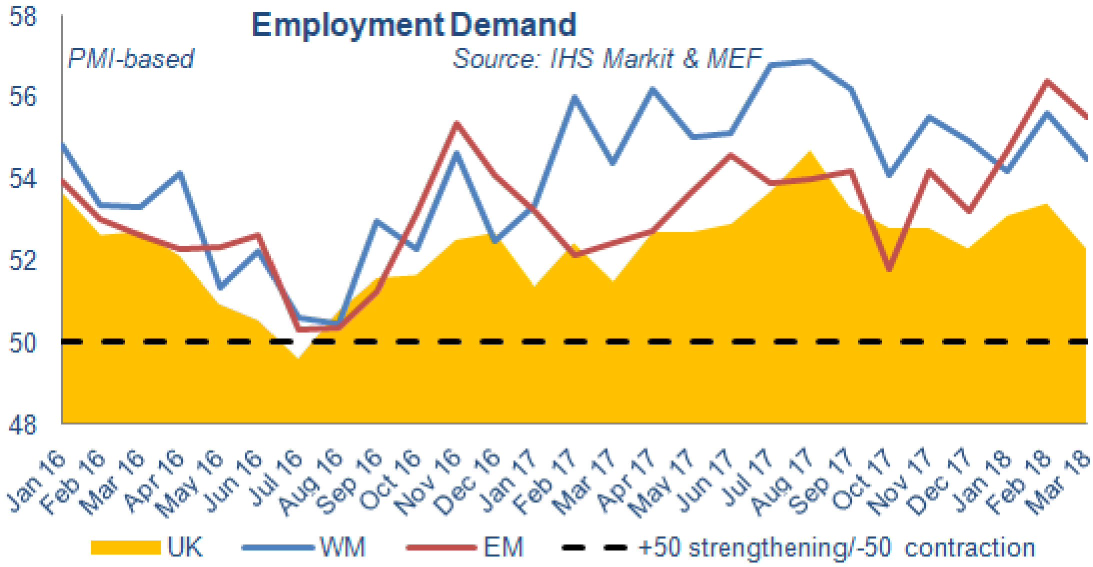
The Midlands saw expansion in the service sector in March, with firms retaining an optimistic outlook to the year ahead, and employment demand strong. However, there were some increases in price pressures and backlogs of work






Price pressures in the Midlands remain higher than in the UK overall, according to the latest PMI data, with manufacturers in particular facing higher raw material costs as well as higher wage burdens. This led to prices being passed on to customers and a rise in output costs. However, price pressures are not as great as they were in the second half of 2016, following the devaluation of Sterling in the aftermath of the Brexit Referendum.

Growth in job creation in the Midlands remained the strongest in the UK, although employment demand eased from February. Some firms, particularly in the manufacturing sector, reported a shortage of skilled labour.




Staff shortages, and in particular skills shortages, in the Midlands and the wider UK labour market show how workers need to be up-skilled in order to move them from lower paid, less productive jobs, into more productive jobs in other industries, at the same time reducing wage compression on these lower-skilled jobs. At the same time, this will require capital investment from these labour intensive industries in order to increase labour productivity.



## CBS Brexit Update

Brexit “negotiations” appear to have fallen back into their “Phoney War” phase, now that the EU have agreed to a Transition Period applying to the UK, whereby it remains in the Single Market and Customs Union until the end of 2020. At the time of writing, at least in terms of media coverage, current events have been dominated by Russia and the alleged use of chemical weapons in Syria by the Assad regime, and the already raised tensions in the area, which the US-led retaliation against Assad, involving French and British military forces looks set to heighten further and contribute to worsening of relations with Russia and Iran. Markets can be expected to be volatile until a resolution of the crisis become apparent.

Twelve months on from the enactment of Article 50, the uncertainty surrounding the likely impact of Brexit on key sectors continues. The Prime Minister has lauded this deal, but notably stated that life after Brexit is going to be “different”, given that current Government stance is still to exit the Single Market and Customs Union.

Hidden in the fine-print of this transition period “deal”, though, is that negotiations to secure a post-Brexit trade deal with the EU could fall through if agreement is not reached on the situation of the border of Northern Ireland (with agreement having ostensibly been reached on the status of EU citizens in Britain post-Brexit, and the size of the UK’s “divorce bill”). The EU’s backstop position on this is continued Northern Ireland membership of the Single Market and Customs Union, should the UK Government fail to come up with a “technological solution” to the Irish border problem. However, to date, no credible proposals have been put forward by the UK Government and this was indeed noted by a Parliamentary Committee including three DUP representatives. With only five months to go until October when a deal with the EU would need to be reached according to current Article 50 timelines, it is looking more problematic day-by-day as to how this seemingly intractable problem will be resolved, and the outlines of a future trade agreement be reached. In addition, the re-election of Viktor Orban in Hungary places additional pressure on the EU from the Visegràd group of Hungary, Poland, Czechia and Slovakia.



Turning to the rest of the world, the UK’s chances of securing a trade “deal” with the US have thrown up the stark choices facing us should we leave the EU Customs Union and regulatory orbit, with the Office of the President of the United States (Trade Representative) releasing a 400-page report last week (of which some 50 pages are devoted to the EU) detailing various “barriers” to trade for US producers. The report is notable in raising issues around phytosanitary standards, animal welfare, additives to milk, levels of pesticide use on crops, regulation of the price of medicinal drugs etc. that are all seen by the US Government as prohibitive.

The implication here is that any post-Brexit “trade deal” with the US by the UK Government would come at the price of realigning UK regulatory standards to match those of the US. As the recent furores over chlorinated chicken and hormone-treated beef have shown, there appears to be little “appetite” by the UK public for such products. However, the report comes on top of previous comments by senior US Government officials that the UK would be expected to drop its current food standards, and so paints a clear (if one-sided picture) as what would be expected to happen to realise such a deal. Couple this with rumours that the Trump administration is considering trying to repeal key elements of the Sarbanes-Oxley Act of 2002 (which amongst other things regulates corporate financial reporting standards and auditing, after the fallout from the collapse of Enron) and the concern is that US and EU regulatory frameworks will diverge further, forcing the UK to choose between one and the other.

For UK-based businesses the implication is clear, and that rather than waiting for Government clarification on what a “deep and comprehensive” (or Canada plus-plus) trade agreement means (assuming we get one), the need to start preparing for increased documentation requirements and customs checks (given the current stated positions of both major parties) starts now. The prospect of such measures (and decreased availability of EU workers given current migratory trends from the rest of the EU) should also prompt companies to reassess their supply chains – for some, reshoring to the UK might be an option, whilst for others, reduced worker availability might serve as a prompt to increased automation. Other companies might simply shift production to other EU states (as Jaguar LandRover have threated to do, for example, if the UK faces customs/regulatory barriers to the rest of the EU).

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**Notes to the Editor:**

**Birmingham City University: Centre for Brexit Studies**

The Centre for Brexit Studies (CBS) is an academic facility which supports and encourages the existing work on Brexit within Birmingham City University's schools and faculties. It promotes rigorous engagement with the multifaceted aspects of the "Leave" and "Remain" perspectives in order to enhance understanding of the consequences of withdrawing from the EU. Whilst CBS will have a national focus we will also specifically investigate the impact on Birmingham and the surrounding areas. The work of CBS is primarily undertaken by Birmingham City University staff and students, but we will provide collaborative opportunities with interested businesses, professional organisations and civil society. Our work will be accessible to the general public and we will hold conferences, workshops and seminars to disseminate knowledge and encourage discussion on Brexit. The Centre website will also reference member's publications on Brexit issues.



**Midlands Economic Forum:**

The Midlands Economic Forum is a neutral, independent forum bringing together representatives of the public, private and voluntary sectors to evaluate real trends in the local economy. Midlands Economic Forum is part of the West Midlands Economic Forum Group.