



Regional Monitor June 2018

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

Days since Article 50 activation: 438

Conclusion of Negotiations: October 2018

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- The Midlands was the fastest growing region in the UK in May, with the EM and WM recording the two highest PMIs respectively.
- Input price inflation accelerated in May, although this was largely passed on to customers.
- New business growth remained solid, although there was a slight weakening.
- A fractious G7 summit shows divides between the USA and Europe on Trade Policy.
- The proposed “backstop” plan from the UK is not seen as a viable solution by the EU Chief Negotiator Michel Barnier.

As the G7 met in Canada this weekend, the USA seemed to be at odds with the other nations on trade, with President Trump revoking his support for the joint communiqué via Twitter shortly after it was published. This comes as other G7 members move to make retaliatory measures against the tariffs imposed by President Trump on steel and aluminium imports to the USA. Trump’s call for “fair trade” and “America first”, as well as for Russia to rejoin the G8 (a move backed by the new Italian Prime Minister), mark a potential shift in global power structures, especially as the President is due to meet North Korean leader Kim Jong-Un in Singapore. With President Trump’s dislike of the WTO, and his delaying of the appointment of the US judges to the Appellate Body (the WTO’s Supreme Court) threaten to undermine the organisation’s ability to hear disputes.

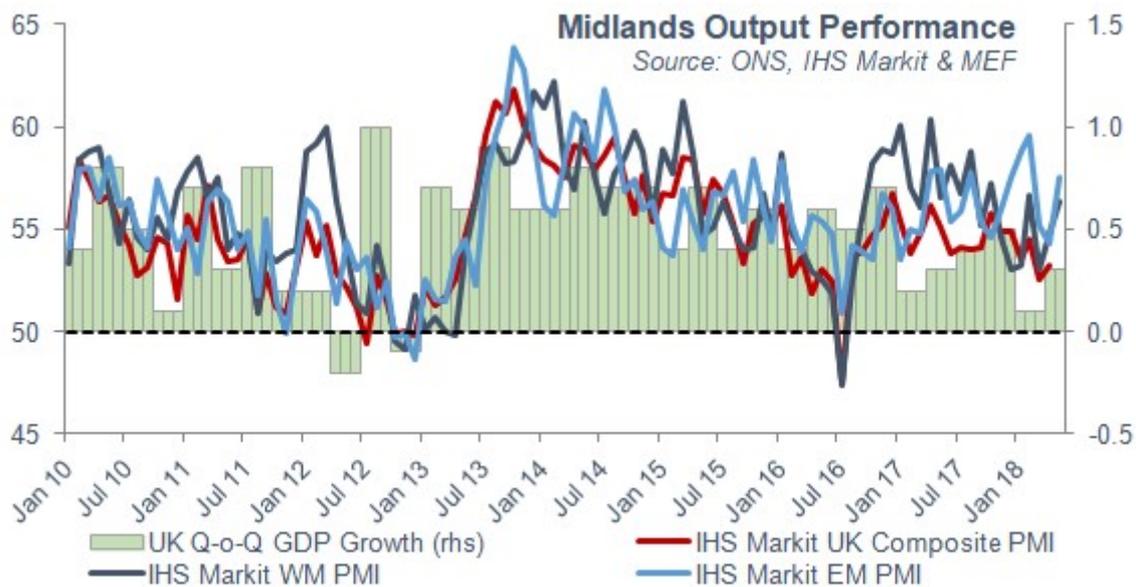
This comes as the EU-28 ambassadors sent an open letter to the USA highlighting the value of trade between the EU and the USA done under WTO rules, including that the EU was the largest destination for US exports in 2016, and that the EU invests more FDI in the USA than the USA does in Europe. This also highlights the value of the WTO to Britain after Brexit as a platform for free trade.



Although there was a united front at the G7 summit, the EU Chief Negotiator Michel Barnier has said that the UK government’s proposed temporary backstop solution does not offer a solution to the issue of the Irish Border. However, the EU faces other distractions, not least a potential trade war with the USA, but also the formation of a new populist government in Italy, which has already stopped a ship of migrants from docking on Italian soil, as well as the election of an anti-immigration party in Slovenia. There is unity on other fronts though, with the EU parliament revising the rules on posted workers after President Macron called for reform. The new Spanish premier has appointed several pro-EU members to his new cabinet, signalling a potential further divide between pro and anti EU sentiments in the EU.

In terms of the Global outlook in the Midlands, both EM and WM had a positive export climate indicator for May. There was increased activity in non-EU markets, notably the USA, China and Singapore, although output growth eased in some European markets such as Germany and France – potentially a sign of slightly weaker future export demand from these areas.

The NatWest PMI for the EM was 57.5 in May, from 54.3 in April, while the WM PMI rose for the second month running from 54.8 in April to 56.3 in May. Both regions continued to outperform the UK recording the two strongest PMIs in the UK in May.



Growth in the Midlands was seen across both the manufacturing and services sectors, accelerating from April. Business confidence in the East Midlands remained positive, with increased marketing, planned investment and the development of new



products buoying confidence. In contrast, despite increased growth, confidence in the WM weakened, and was below the UK average in May – although it remained at a robust level. There was some optimism, with firms anticipating new product launches and increased demand, although some firms reported concern about the low levels of consumer confidence.

Julian Beer, Deputy Vice-Chancellor at Birmingham City University commented:

“Despite the global uncertainties seen at the moment, the Midlands continues to be the powerhouse of growth in the UK, reporting the two strongest PMI figures for May. As market attention focuses on the outcome of the G7 summit, this could impact on future Midlands’ trade.”

This was reflected in the three sector PMIs for the UK, with the UK manufacturing and services PMIs reporting increases in growth and the construction PMI maintaining growth levels in May. Some of this expansion was due to firms being able to catch up on delayed work after the poor weather in Q1 of 2018. This reflected a slight increase in business confidence from manufacturers in May, as solid demand from export markets, new products and planned expansions buoyed confidence levels. However, construction and services firms reported a weaker business outlook, as Brexit and economic uncertainties weighed on client and consumer confidence.

In the Midlands, there was solid job creation, with an acceleration of growth in the Midlands, although both regions saw softer growth than in Q1 of this year. Businesses reported higher output requirements and increased demand as reasons for hiring.

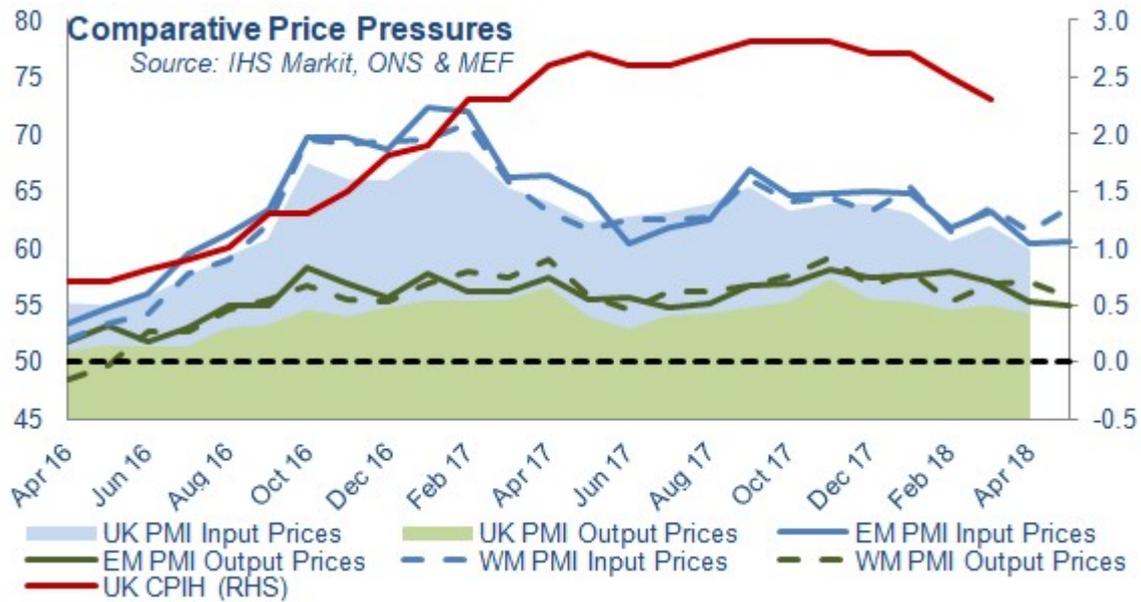
All three UK sector PMIs reported a slowing in job creation in May, with skills shortages and delays in filling vacancies cited as a key reason for this. This trend was reflected in the regional report on jobs, which showed the pace of expansion eased across the UK overall. However, in the Midlands the pace of expansion increased in April, continuing above the average for the UK overall. Despite the increased demand for candidates, there was a further decline in the pool of available candidates, in particular with regard to skills shortages. This in turn influenced starting salaries, with the Midlands seeing a sharp rise in April. This was also highlighted in the UK services PMI for April, which noted an increased pressure on



margins as pricing power was not strong enough to pass the increased costs onto customers in some cases.

In addition to increased labour costs, UK sector PMI respondents noted increased prices for raw material and fuels, in some cases exacerbated by shortages and supply chain delays – the latter most notably in the construction sector.

Manufacturers seemed largely to be able to pass these costs onto customers, but there was more difficulty with this in other sectors.

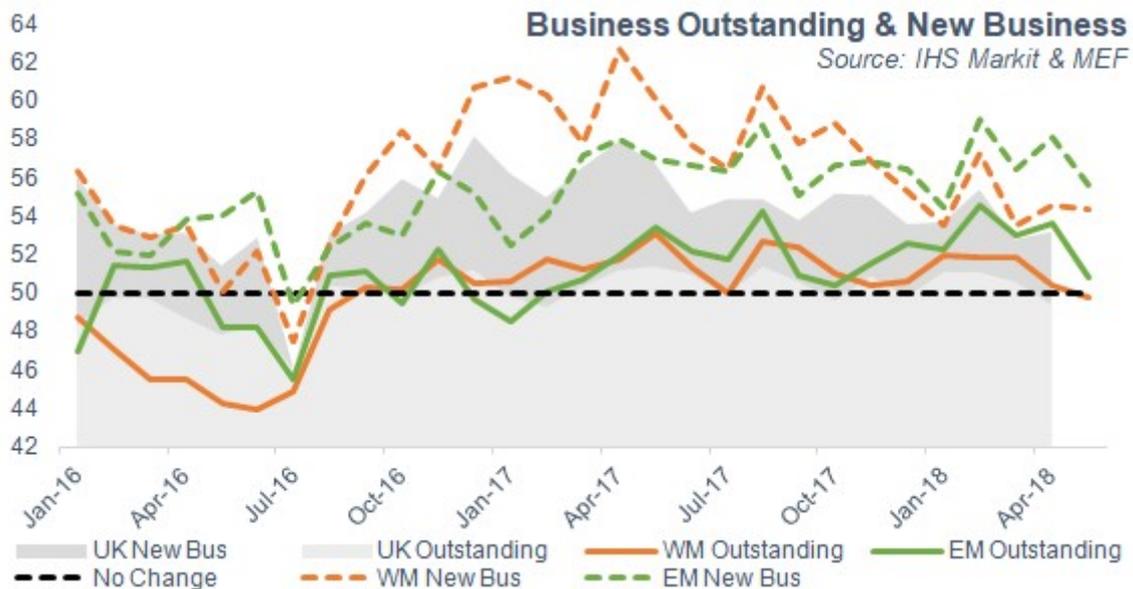


In the Midlands, price pressures increased, although they were not as acute as seen at the beginning of the year, they were above the UK level. Input price inflation was linked to greater demand for inputs, higher costs for fuels and raw materials, such as steel, and higher staff costs. Much of these costs were passed onto customers. In the WM, there was a difference between the manufacturing and services sectors, with manufacturers seeing sharper price rises.

New business growth in the Midlands was robust, although softer than in April. The increased demand was attributed to greater demands and increased marketing. In the WM, services firms saw a stronger increase in new business than manufacturers did. The WM saw a marginal fall in backlogs in May, particularly in the manufacturing sector. This reflected the UK trend, and the fall was smaller than the UK average. In the EM, there was a marginal increase in backlogs overall, with some firms attributing this to weaker demand easing pressure on capacity. However, some firms



also reported increased backlogs due to supplier delivery delays and difficulty sourcing raw materials.



This trend was not completely reflected in the three national sector PMIs; in the manufacturing sector, increased business output was due to a decrease in outstanding business and a build-up of finished products. Although the sector did still see a relatively solid increase in new business – notably in foreign markets - this could be an area for future concern. The construction and services sectors saw subdued new business in April, with political and economic uncertainty, as well as the troubles of the retail sector weighing on client confidence.

CBS Brexit Update

The past month has seen a number of Brexit-related developments. Most recently, in spite of agreeing an “end date” of the proposed “customs backstop” designed to ensure the absence of a hard border in Ireland, continued tensions within the Government over this issue remain apparent (BBC, 2018b). This is perhaps what lies behind Boris Johnson’s recent comments that imagining Donald Trump doing Brexit was a “very, very good thought” (BBC, 2018a). More problematically, it is difficult to envision EU agreement to a backstop that is time-limited. Indeed, events in Northern Ireland challenge the Government in more ways than one (Budd, 2018).

Of course, even with a customs agreement of some form with the EU, without continued adherence to the regulatory environment associated with the EU’s Single Market in goods it is difficult to see how a “frictionless border” can be achieved.



Moreover, Northern Ireland has not been the only challenge to face Westminster. The Scottish Parliament's vote to refuse to give consent to the UK's European Union (Withdrawal) Bill has also raised questions over the existing devolution settlement. Specifically, at present there are some 158 areas in which policy that would usually be the domain of devolved administrations is presently determined in Brussels. In 24 of these the UK government intends to repatriate policy directly to Westminster (at least for a period).

Although one can envisage compromise being found some of these areas are crucial for the UK's own internal market, including chemicals regulation, agriculture and fisheries policies for example, it is difficult to see a situation where English farmers are allowed to use certain products whilst their Scottish counterparts a few miles away are not (or vice versa) as being acceptable. In this vein, it is noteworthy that the Welsh Assembly voted to allow the UK government to repatriate powers. Nevertheless, repatriating such powers to Westminster could be construed as reversing aspects of devolution.

Whilst in the strictest terms this is of relatively limited constitutional importance – the UK government does not need the consent of the Scottish Parliament to introduce legislation – it raises thorny questions for a country that is deeply divided along regional lines. Indeed, it seems possible that the argument over the appropriate devolution of powers is something of a proxy for more fundamental disagreements. Although the UK ultimately voted by a relatively narrow margin (51.9% to 48.1%) to leave the EU, this masks highly divergent regional patterns in the vote. Whilst the Midlands, for example, voted decisively to leave (by 59.1% to 40.9%), Scotland voted heavily to remain part of the EU (62% of votes were in favour of remaining).

It raises thorny questions for the Government in Westminster – how should the UK reconcile the different wishes of various regions? The past 20 years have seen dramatic developments in the UK's constitutional and political landscape. One of the most centralised states in the world has engaged in a rather dramatic experiment with devolution, which is, in the Scottish case at least, widely seen as a resounding success. In light of this there is certainly a significant argument to be made in favour of greater devolution within England, although inter-regional tensions over Brexit are almost certain to remain. The coming week will see critical votes over Brexit taking place, with Parliament voting on the EU Withdrawal Bill on Tuesday. The



Government will attempt to reverse 15 amendments proposed by the House of Lords, which include, crucially, a series of deadlines as part of an attempt to ensure Parliament maintains meaningful control over the process. This week will certainly be one to watch in terms of how Brexit unfolds.

BBC (Producer). (2018a). Boris Johnson calls for more 'guts' in Brexit talks. Retrieved from <https://www.bbc.co.uk/news/uk-politics-44407771>

BBC (Producer). (2018b). Brexit: May and Davis 'agree customs backstop wording'. Retrieved from <https://www.bbc.co.uk/news/uk-politics-44391539>

Budd, L. (2018). Northern Ireland's Dance to the Music of Time of Brexit. Retrieved from <https://centreforbrexitstudiesblog.wordpress.com/2018/06/08/northern-irelands-dance-to-the-music-of-time-of-brexite/>



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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.

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