Regional Monitor September 2017

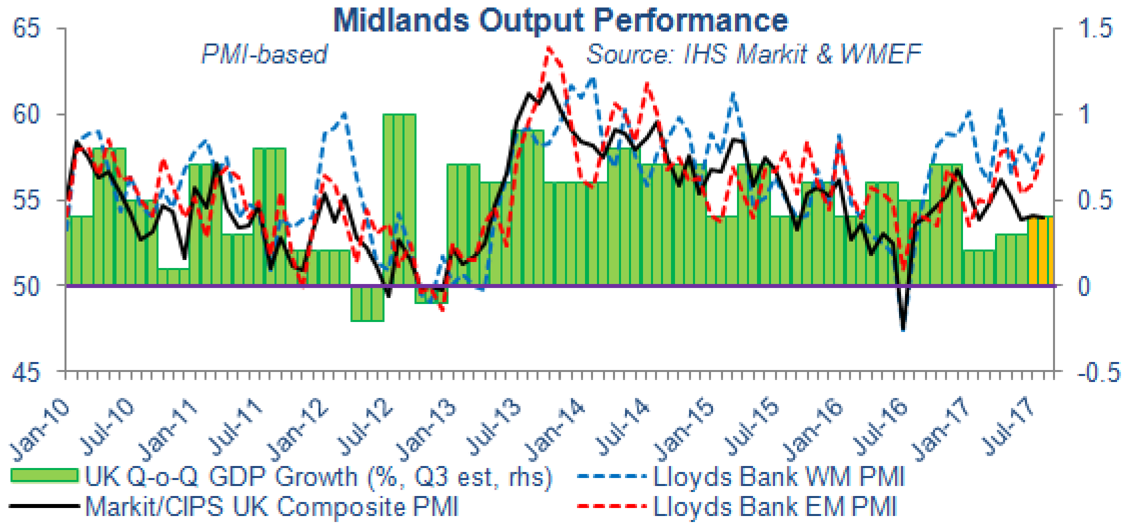
Latest Global Trends, Regional PMI, Output Data, Trade Conditions & Brexit Update

Days since Article 50 activation: 167 **Remaining Brexit Negotiating Days: 70**

- EM PMI records 57.7 for August, from 55.9 in July, while the WM is 58.6 from 56.7.
- WM and EM PMIs 1st and 3rd strongest performers in the UK, both outperforming the UK figure of 54.0.
- Nationally, recent Manufacturing performance has been robust, although growth in Construction and Services has been more muted.
- Price pressures are increasing, although in the Midlands they are lower than in the UK overall.
- Business Confidence is under pressure from Brexit-related uncertainty, although stronger in the Midlands due to robust Manufacturing output.
- £ has firmed against the US$ as cable comes under pressure, strong performance in the EU has led to € strengthening against £.
- Overall Global Commodity prices have remained largely flat, masking increases in metals and minerals.
- The Government has published its Great Repeal Bill, although there remains lack of clarity over their preferred options.
- The EU has indicated that the first round of talks may not be concluded until Christmas.

Midlands Output Performance

Business activity in the EM and the WM rose for the 13th consecutive month, according to the latest Lloyds Bank Regional PMI. The EM performance grew to 57.7 in September from 55.9 in July, and the WM recorded 58.6 from 56.7 previously. The WM and the EM ranked 1st and 3rd respectively, and both outperformed the UK figure of 54.0, which was down slightly from 54.1 in July.



Growth in the Midlands was driven by growth in new orders in both the manufacturing and the services sector, and was the fastest in the UK with the WM recording the highest growth and the EM second fastest. The growth in new business, which came from both domestic and foreign markets, has also led to an increased backlog of work. In the EM, backlogs accelerated at the fastest pace since December 2000. In the WM, backlogs increased more for service firms than for manufacturers.

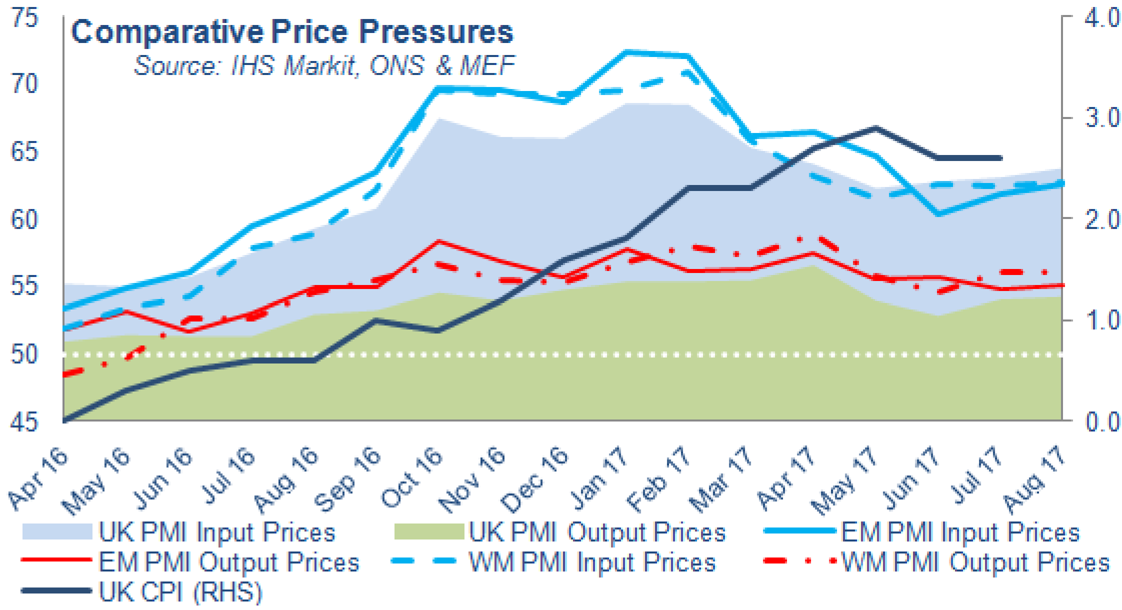
These trends were reflected in the three UK industry PMIs for August, with the August Manufacturing PMI at a three-month high, at 56.9, with production and new orders both up. Domestic markets were the main source for new orders, although there was also continued growth in new orders from foreign clients, especially Europe, the USA, China, and Australia. However, the ONS Production Index reported subdued growth in manufacturing in the three months to July, although they report that growth accelerated in July due to increased production in the automotive industry. The Services PMI also recorded robust growth, at 53.2, although there are some signals that expansion is softening, with new orders increasing at a slower pace than in H1 of 2017. The August Construction PMI reported continued slowing, recording 51.1, with civil engineering and commercial work stagnant or falling, but offset by moderate growth in residential building activities.

According to their respective PMIs, both Manufacturing and Services saw increases in employment in August, reflecting the growth in output and business in

Manufacturing, and increased backlogs in Services. In contrast, Construction employment slowed in August, with fewer new contracts for businesses to complete. Reflecting this, the Midlands saw an increase in jobs in August. The WM saw employment levels rise at the fastest rate since the beginning of 2015, and although the EM saw growth that was above trend, it was still slower than the UK overall. The increases in employment were largely due to increased new business and stronger client demand.

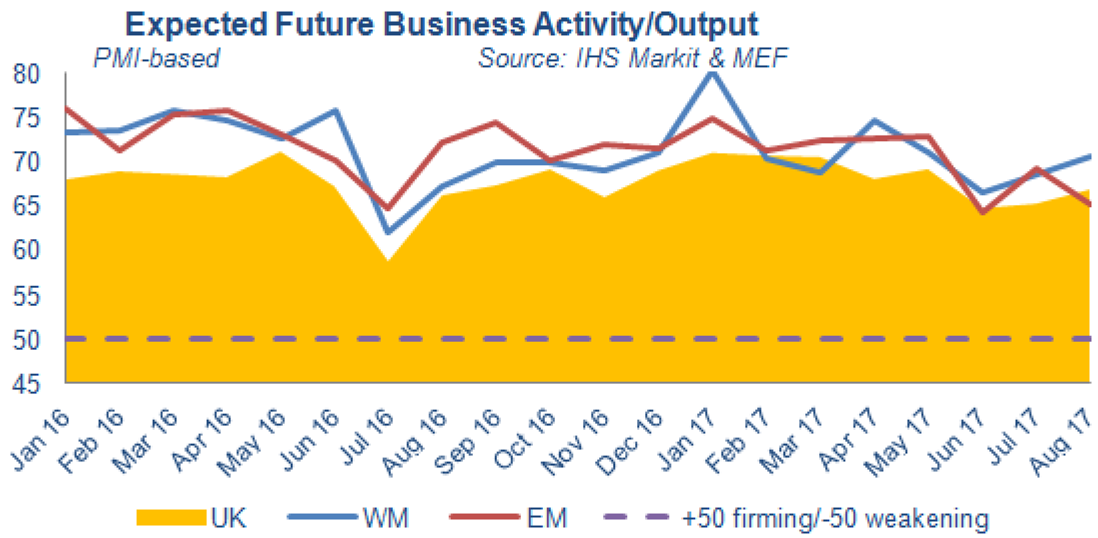
Professor Julian Beer, Deputy Vice-Chancellor at Birmingham City University comments: "Once again, the Midlands is showing strong performance compared to, and in some cases in contrast to, the rest of the UK. This strong performance of the region is despite regional infrastructure being at or near capacity in many cases, and skills shortages in some key regional industries. The fact that the region remains at the apex of global value-added supply chains bodes well for its success outside of the European Union, despite some challenges posed by Brexit."

In the Midlands, input price pressures continued to rise, although at a slower pace than nationally. In the EM, many firms cited the increased price of raw materials due to exchange rate fluctuations as a reason for higher input prices, whilst in the WM, input price rises were driven by increased employment costs in the services sector.



The Manufacturing PMI saw purchase price inflation increase for the first time in seven months, linked to rising prices in commodities, and in some cases exacerbated by shortages. Manufacturers' prices also rose, but at a slower pace in August. Construction cost pressures were softer in April; although some input prices were higher, softer demand from Construction businesses has reduced the upward pressure on prices. Services sector business reported some acute price pressures in August, although some of these were passed on to consumers, with output prices also rising.

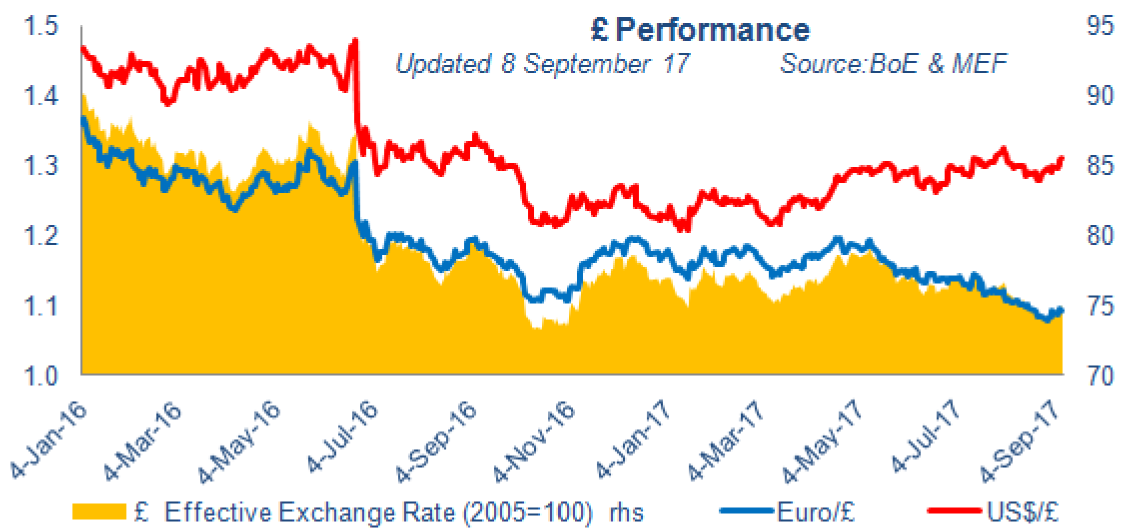
With the rise in output and new orders, the Manufacturing PMI reported an increase in business confidence in August. The construction sector reported a less positive outlook, largely down to reduced confidence in the economic outlook from clients, with many projects being delayed or scaled back. The Services PMI also reported weaker client confidence and delayed decisions on spending as reasons for lower business confidence in August.



This is partially reflected in the Midlands PMIs, with business confidence in the WM rising in August and remaining above that of the UK overall – perhaps reflecting its strong manufacturing base and the confidence within that industry. Brexit related uncertainty seemed to be less important for WM businesses, and a positive outlook for client demand and future sales provided a boost to confidence. In contrast, the EM saw more subdued business confidence; although it was still positive it was lower than in the UK overall. Increased demand from foreign and domestic markets was seen as the main driver of optimism.

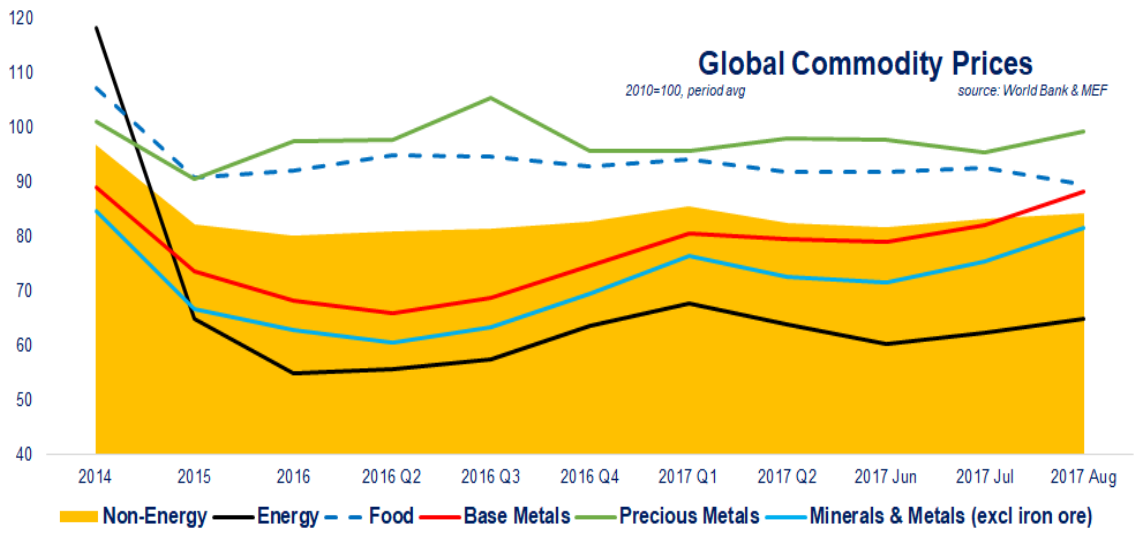
Global Trends

History is often described as unfolding first as a tragedy, and then repeated as a farce, although currently the farce is nuclear armed. With markets unable to discern a diplomatic resolution of US-North Korea imbroglio, further volatility can be anticipated, with the US$ under pressure - although the impact of the devastation wrought by hurricanes in the southern states and the Caribbean has also had an impact. This has contributed to the recent firming of £ above the US$ 1.20-1.30 trading range in has occupied since mid-October. Further destabilising factors have been expectations of US rate hikes, major shifts in the composition and subsequent policy of the Fed Board as Trump can now appoint up to 4 or 5 new Governors, as well as the continued Congressional impasse over raising the Federal budget debt ceiling.



In contrast, strengthening economic conditions in the EU has seen £ ease against the Euro, with parity now clearly on the horizon. Within this unsettled context, the unwinding of the various QE programmes could prove problematic. The CHF and JPN have both benefitted. Furthermore, in the post-Brexit trading environment, currency cross-rates, particularly of what are now regarded as more exotic cross-rates, are likely to receive the increasing attention of British business with market volumes hopefully rising.

With the US$ becalmed, safe haven flight has seen a firming of gold and precious metals prices (up 4% in August), with spot Gold reaching US$1,346.59 in Friday's trading. Nevertheless, although this is up from recent lows, there is evidence of some price acceleration in non-energy, non-food commodities according to World Bank data. Food prices have, however, been relatively flat, down 4% over the period Q2 2016 to Q2 2017, and in August food and beverages prices dropped 3.4% and 0.2% respectively. This was reflected in the comparatively weak increase of overall non-oil commodity prices, which masked the acceleration in metals and minerals prices which increased 8.2% last month, and especially base metals up 7.7%, with both rising by some 20% over the year to Q2 2017. Since falling from over US$114 pb in 2014 to less than US$50 pb in January 2015, the benchmark Brent blend oil price has trended in a range largely between US$40-US$60 pb. Thus, although energy prices rose 4.4% in August, and by 15% over the year to Q2 2017, Brent remains below US$60, closing at US$53.78 pb on the 8th September.



Brexit Update

Last week, the Government introduced its so-called Great Repeal Bill, which is intended to ensure legislative and judicial continuity after Brexit in April 2019, by incorporating all EU legislation into British law. Although there is some disquiet over the arrangements for subsequent legislative revision, the bill is broadly similar to previous British legal practice during past decolonisation processes. Of perhaps more concern, some 167 days after the activation of Article 50 and with only 70 formal negotiating days remaining before the Brexit agreement has to be concluded, is the continued lack of clarity over the Government's preferred options. Constructive Ambiguity is a difficult concept to quantify to enable effective forecasting or for strategic planning.

Publicly at least, the current status, whilst seemingly not acrimonious, appears far from cordial. Momentum toward an agreement seems to be slowing, and October's EU Council of Ministers, post German Federal Elections, will be crucial to revving impetus and common agreement is secured to move to formal trade discussions. What may prove significant, the EU has raised concern over IP issues, especially with regard to trademarks and geographic designations. This may reflect a key shift in EU positioning with the potential to unlock apparent deadlocks over a range of topics.

Last week the British government has launched a range of position papers:

- Continuity in the availability of goods for the EU & the UK
- Confidentiality and access to documents
- Northern Ireland and Ireland
- Ongoing Union judicial and administrative proceedings
- Nuclear materials and safeguards issues
- Privileges and immunities
- Safeguarding the position of EU citizens in the UK and UK nationals in the EU

In addition, the government has announced a series of partnership papers:

- Collaboration on science and innovation
- The exchange and protection of personal data

- Enforcement and dispute resolution
- Providing a cross-border civil judicial cooperation framework
- Future customs arrangements

The EU, through its various guises and representatives have published a range of responses to the British position, which in summary can be best described as less than favourable. There is evidence that there remains significant differences between the two parties, with the EU lead negotiator Michel Barnier now indicating that the first phase of talks may not be concluded until Christmas.

Ends

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Notes:

Birmingham City University:

Birmingham City University is a dynamic, business-engaged institution. As a substantial employer with over 2,000 staff and through the provision of graduate talent, research, and knowledge transfer, we contribute around £180 million to Birmingham's gross domestic product (GDP).

The university works with in excess of 5,000 businesses, regionally, nationally, and internationally, with our courses informed by Industry Advisory Boards, where information about business needs are reviewed and skills challenges are discussed. In 2015 we launched Advantage, the business growth service from Birmingham City University enabling organisations and individuals to get connected with knowledge, skills and money in business, innovation, and enterprise.

We have extensive sector linkages providing detailed intelligence and input into future innovation, driving thinking around smart specialisation, the creative economy, advanced manufacturing, and health-related life sciences. Through our work with partners such as the GBS LEP, WMCA, Science City, and Creative City Partnership, we take a lead on cross innovation, design, and climate change. Innovation is at the core of our work. Working in partnership is at the core of our approach to business.

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.