



Regional Monitor March 2018

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

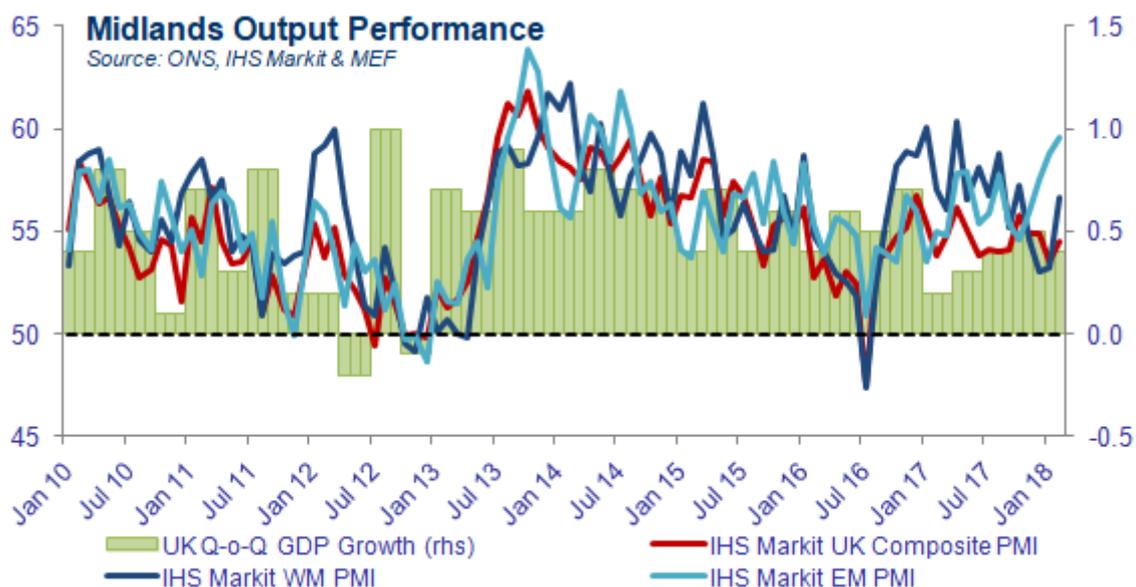
Days since Article 50 activation: 347

Conclusion of Negotiations October 2018

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- EM fastest growing region for second month running, while WM third fastest.
- UK growth increased, with the PMI posting 54.5 in February.
- Midlands reported the fastest increase in employment in the UK in February.
- Confidence levels remain robust, despite reports that the Midlands will be hardest hit by Brexit.
- Global demand for regional exports expected to remain robust in through to 2019.

The EM PMI increased further in February to 59.6, from 58.8 in January, while the WM PMI grew from 53.2 in January to 56.6 in February. In comparison, the UK PMI increased to 54.5 in February from 53.5 in January. This means that the EM was the fastest growing UK region for the second month running, while the WM was the third fastest growing after the North East.



Both EM and WM saw marked increases in new business in February, interestingly, this was driven by the services sector in the WM, although it was more broad based



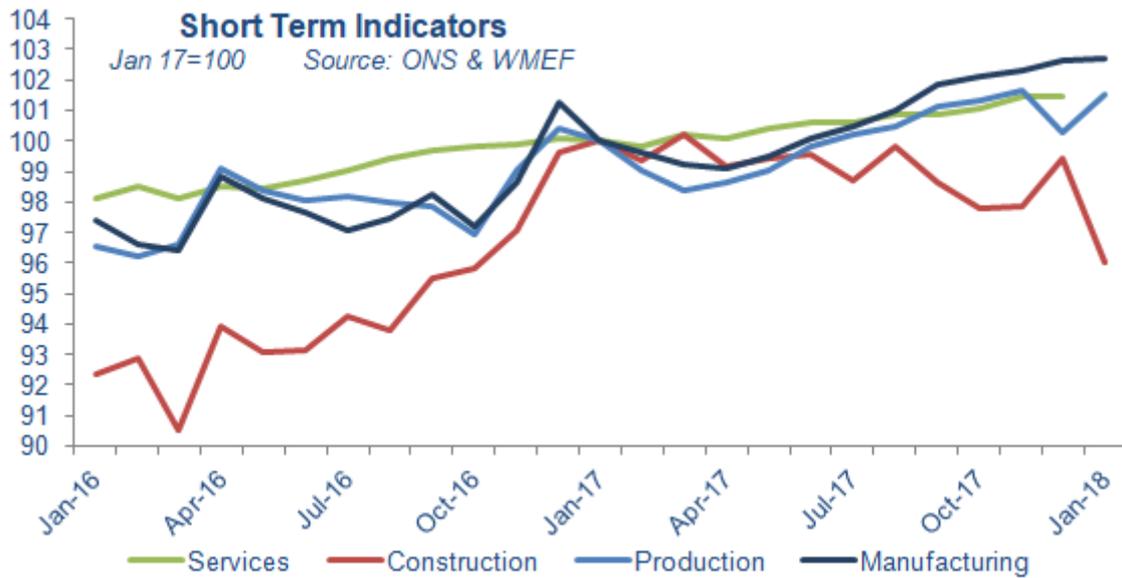
in the EM. The large increases in new orders led to increases in business outstanding, this was due to capacity pressures in the WM – which are more acute than in the UK overall, although both regions also reported some delays in supply chains. The increased pressure on firms and supply chains increased input costs, and these were largely passed on to customers, although the pace of both input and output price inflation has eased somewhat from previously, it remains above the levels seen in the UK overall.

The strength of regional performance reflects the robust growth levels seen in the manufacturing nationally – a key sector for the Midlands. The manufacturing PMI, at 55.2 in February, remained the highest UK sector PMI despite a slight softening in growth levels from January, and construction and services industries both reported increased growth rates.

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

“The Midlands continues to perform strongly compared to the rest of the UK, boding well for its ability to compete in a post-Brexit landscape. Critical, however, will be a deal that suits the whole of the UK, and not just certain areas and regions. Therefore, it is important that the Midlands has a voice in the Brexit process”

The ONS short term indicators, now published for the beginning of 2017, reflect the PMIs in showing a robust beginning to the year – notably in production and its largest component; manufacturing - although perhaps slower than the beginning of 2017. In part, this reflects the reopening of the Forties oilfield, after it unexpectedly shut in December. Construction data has also been affected by a fall in new orders, notwithstanding the large increase following the announcement of the HS2 contracts in Q3 of 2017. In the medium term, construction of HS2 will provide a boost to the construction industry in the Midlands and in the UK as a whole, as will preparations for the Birmingham Commonwealth games in 2022.



Looking ahead, the proposed steel tariffs by the Trump administration could pose issues for the Midlands economy, with the steel sector being a notable product source for exports from the region. Recent statements from the USA suggest a slight softening in the President's stance, and the final outcome remains to be seen.

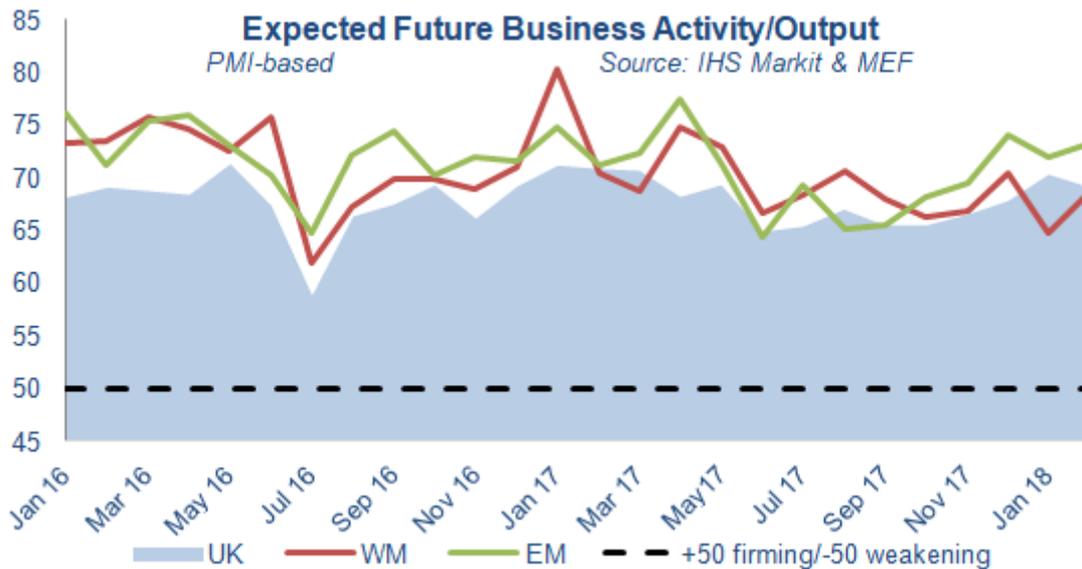
In addition, albeit slightly closer to home, the recent formation of a government in Germany might provide a new impetus to the Brexit negotiations. However, some distractions remain in Brussels, with the potential sanctions against Poland over rule of law, and the hung parliament result of last weekend's Italian Elections. The anti-EU Five Star Party won the largest proportion of seats, and the far-right Northern League also took 18% of the vote – making it the largest conservative party. Whilst in the PRC, one of the key regional export destinations, recent constitutional changes indicate shorter-term policy stability, but over a longer perspective could undermine the successful strategy adopted since Deng Xiaoping's reforms were adopted in the 1980s, and contribute to factional pressures amongst the leadership.

Nevertheless, the global outlook for the Midlands remains a fairly positive one, with robust growth levels in recent European and Global PMIs possibly signalling continued export demand for the Midlands. Indeed, the manufacturing PMI for February reported new business from the USA, Europe, China, Brazil and East Asia.

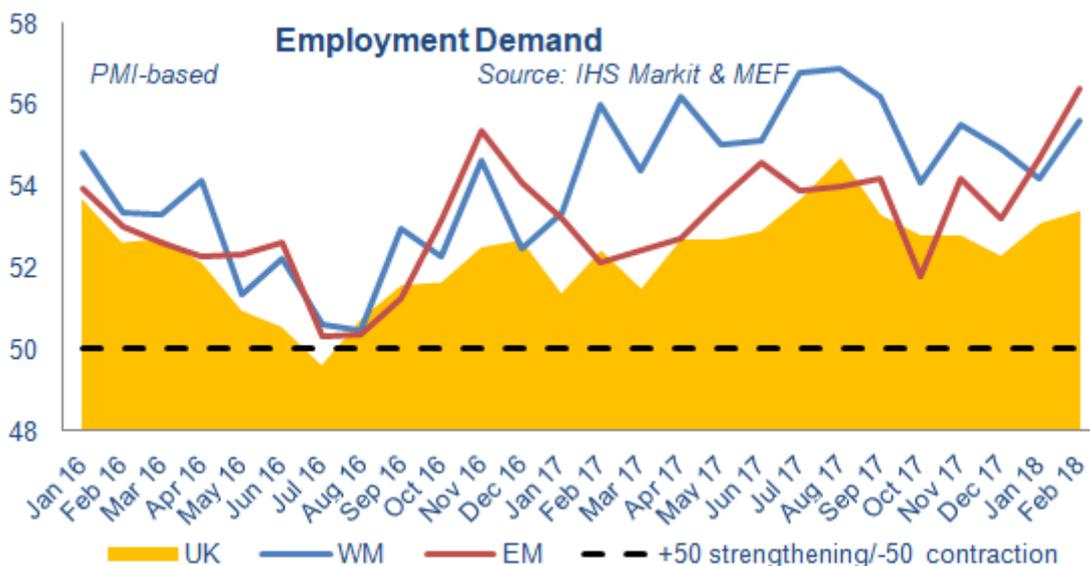
This global outlook feeds into confidence levels in the Midlands, with business outlook improving in February across the region. Businesses cited increased future demand – from both foreign and domestic markets – as well as investment in recruitment and new sales strategies as tentative reasons for a positive outlook. This



is in contrast to the recent leaked government analysis which shows that the Midlands will be one of the regions hardest hit by Brexit.



On a sector level, confidence in the manufacturing industry remained robust, with planned expansions, new orders demand and investment supporting the business outlook. In contrast, the construction and services sectors saw an easing in confidence levels, with Brexit related uncertainty contributing to some uncertainty, although the resilience of the UK economy and global conditions were also noted.



The quickest pace of job expansion in the UK was seen in the Midlands in February as firms increased staff levels in order to keep up with new business. This is reflected in the latest IHS Markit Report on jobs, where permanent placements rose at the fastest pace in the Midlands out of all the monitored regions. The industry



PMIs also reported an increase in jobs across the UK, with manufacturing, services and construction all reporting growth.

According to official data from the ONS, although the most recent data are from September 2017, it shows some of the recent dynamism in the Midlands labour market, with the EM having the largest growth in employment in the UK between July and September 2017, at 1.3%. Nevertheless, the WM had the highest official unemployment rate in September 2017, at 5.4%. This may be more of a reflection of the condition of employment statistics, but also shows the investment in skills needed in the labour market, as the IHS Markit report on jobs also found a further decline in the number of candidates available for positions in the Midlands.

CBS Brexit Update

February has seen a number of Brexit-related developments, although these have largely been rhetorical rather than concrete actions. Whilst negotiations are continuing behind closed doors, members of the cabinet have set out their Brexit 'vision' in a number of speeches. Other developments of note include Jeremy Corbyn laying out the Opposition's desire for a customs union and the EU's first attempt to draft a legally binding version of December's agreement.

Foreign Secretary, Boris Johnson, argued that Britain seeks a "liberal Brexit". Ultimately, his speech was grounded in questions of identity rather than economics, arguing that "only the nation can legitimate"^[1] obedience to laws. The remainder of the speeches were rather more pragmatic and in some cases showed genuine policy innovation. David Davis^[2] outlined several facets of the UK Government's Brexit agenda that had not previously been clearly elucidated. He reiterated that, "[t]he agreement we strike will not be about how to build convergence, but what we do when one of us chooses to make changes to our rules."^[2] The implication of this statement is clear: a future comprehensive economic agreement should look a lot like European Union membership. In essence, it appears that this most ardent of proponents for leaving the EU is now in favour of an arrangement that continues the *status quo ante* but with the ability to derogate from certain rules (including those not yet passed).

If this approach is to be adopted, the Government must explain, in detail, how such derogations might be managed and enforced. Inside the EU, conformity with trade



standards is enforced and the ultimate legal arbitrator is the Court of Justice. If Britain wishes to avoid being under the jurisdiction of said court, it needs to specify and explain precisely which authority is to oversee and adjudicate in the event of a dispute. Such an approach appears likely to conflict with Johnson's desire to repatriate sovereignty to the nation-state.

Davis's vision of close cooperation also appears to contradict the desires of many other proponents of Brexit within his party. The letter of the European Research Group^[3] suggests that for a significant minority within the governing Conservative Party, complete "regulatory autonomy" is a minimum requirement. The UK must make a decision as to where it stands – with Davis in his desire to maintain a substantial degree of regulatory alignment or with Johnson who wishes for a "retreat to the high seas" and wholesale shift in regulation.

Struggling with the same set of contradictions, Theresa May argued that any deal must "respect the referendum result". It is unclear what this means in practice, partly because of how the referendum question was framed: whilst a modest majority of voters voted against remaining in the EU, it is much less clear what, precisely, they were voting *for*. Migration was of paramount importance for many Leave voters but others would perhaps be content to remain within the European Economic Area and Customs Union for the purported economic benefits.

There appears to be an ongoing "blurring" of some of the UK Government's red lines, particularly regarding the role of the Court of Justice of the EU. It is thus far unclear whether the Prime Minister will be able to convince her European colleagues to support her vision of third-party arbitration. A fundamental question is what the UK would be able to offer in order to induce them to do so, although an "EFTA" style court seems the most likely option if agreed.

Policy has evolved in several areas, with the Government keen to retain membership of a variety of EU agencies. To a large extent this appears sensible and pragmatic – it is difficult to see how dropping out of the European Aviation Safety Agency or European Medicines Agency would be in the UK's national interests. Maintaining most elements of Open Skies is an obvious imperative. Similarly, the Government's acknowledgement of the importance of cross-border supply chains is very welcome.



Philip Hammond more recently argued that a deal could definitely be made to ensure broad continuation of the *status quo ante* in financial services. From the perspective of the Midlands, it is clear that whilst financial services are undoubtedly an important sector of the economy, they should not be prioritised to the exclusion of all else. In any event, the Government appears to have abandoned any hope of obtaining passporting rights for the financial services sector, instead relying on some form of equivalence and mutual recognition that has yet to be specified.

Jeremy Corbyn's recent speech purported to set out how a Labour government would approach the ongoing Brexit negotiations. He sought to drive a wedge between different factions of the governing Conservative party. Whilst domestic policy stood first and foremost, the flagship policy announcement of the speech was Labour's stated desire for a customs union as a matter of policy. A number of Conservative MPs are known to have a favourable view of such an option and it is likely such a policy has majority support within the House of Commons. This could cause considerable difficulties for Theresa May's government.

The broader ramifications of Labour's stated policy, if it were adopted, are likely to be felt in several areas. As with many aspects of the ongoing negotiations and future relationship, the devil is in the details and, fundamentally, Britain will be constrained by what the EU is prepared to offer. Labour appears to support withdrawing from the European Economic Area, as evidenced by Corbyn's statement that "Labour would not countenance a deal that left Britain as a passive recipient of rules decided elsewhere by others."

He wants the UK to have a joint say in any negotiations between the EU and other putative trade partners. Once again, the question is what Britain would be prepared to offer in exchange for a role in policymaking and trade arrangements. No country outside of the EU at present has this favourable position. Labour has ruled out membership of the EEA and the EU Customs Union (EUCU), preferring in favour a customs union with the EU (which is what Turkey has). Why would the EU be prepared to grant this to a third party?

Ultimately, however, in spite of the political optics there appears substantial agreement between both major parties on a number of issues. In particular, it appears that Labour and the Conservatives largely agree on citizens' rights, a



transition period and a desire to avoid a border on the Island of Ireland. Both support remaining in a number of EU agencies, including paying for continued membership. One distinction is over Euratom, which Corbyn would seek to remain part of but May has committed to leave. Ultimately, however, both parties are struggling to interpret the referendum result – leaving the EU can mean dramatically different things – and this has led to internal inconsistencies and contradictions.

1. *Johnson, B., Uniting for a Great Brexit: Foreign Secretary's Speech. 2018, Policy Exchange.*
2. *Davis, D., Foundations of the Future Economic Partnership 2018, Department for Exiting the European Union.*
3. *European Research Group, Letter to the Prime Minister, in Spectator. 2018.*

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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.



The Centre for Brexit Studies Annual Conference is on this Friday 16th and Saturday 17th March and a packed “full house” is expected. The conference will bring together leading academic and business figures, and politicians from both sides of the Brexit debate. The conference promises to provide some fascinating insights into how negotiations are expected to unfold over the next few months, what kind of “deal” the UK could expect, and the likely impact on business and jobs in the Midlands and beyond.

CBS is also pleased to announce it is providing commissioned research, for a world-leading client in data capture and management. This consists of a detailed sectoral impact analysis of the likely Brexit scenarios facing the automotive and aerospace sectors in the UK. We expect this research to have significant commercial impact, as well as contributing to the broader debate over sectoral and regional impacts of Brexit.

The Centre has also continued with its series of public engagement “town hall” meetings (the CBS Roadshow) to find out what people in constituencies that had a high Leave vote currently think about the Brexit process as it unfolds. Recent meetings have seen CBS visit Basildon, Great Yarmouth, Stoke on Trent, and Doncaster, amongst others. What has been striking about the findings is that perhaps contrary to some media depictions, the Leave voters we spoke to acknowledged that leaving the Single Market and EU Customs Union would entail a significant economic cost to the UK, but that this was “worth it” in order to repatriate sovereignty.

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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