

Brexit dashboard Q1 2018

12 March 2018

This is the first issue of the Global Counsel Brexit dashboard. 21 months on from the vote - and with just 12 months before the UK leaves the EU - we can now take the macro pulse of the economy, using a balanced set of 15 indicators, each quarter. We are not attempting to isolate the impact of Brexit from all the other factors affecting the economy, as that is near impossible. Instead, we are providing a health check, to see where the economy is faring better or worse, compared to the years before the vote.

Split screen

The headline message this quarter is of diverging fortunes and prospects for the British economy. While the services sector is struggling, industry is doing better. And while consumers and businesses are both feeling the squeeze, there are signs that the outlook for investment is now steadier.

Households saw real earnings fall during most of 2017, with only the first signs of a recovery in December. This has been matched by pressure on the high street, with sluggish retail sales and an even sharper drop in consumer durables spending. This bares an uncanny resemblance to the first years of the Cameron government, when household finances came under sustained pressure. The outlook for investment is better, with respectable growth in the second half of last year and signs that policy uncertainty may be falling.

Industry has been outperforming services since the middle of last year, which is a role reversal we have not seen in a sustained way since 2010. Growth in goods exports, helped by the fall in the pound and the brighter outlook for the global economy, helps explain this.

We also see a mixed picture for the people indicators we look at. We are now seeing a drop in both net migration and visitors from the EU, suggesting the UK may be less attractive as a destination. But we are only seeing early signs that this may be impacting on vacancies in the health and social work sector.

Snapshot of latest indicators | last available month or quarter

 Consumers	Last	Trend	 Investment	Last	Trend
 Real earnings	-0.3		 Economic policy uncertainty	256.5	
 Retail sales	1.4		 Business investment	2.1	
 Durable goods consumption	-0.1		 London house prices	-0.5	
 Industry	Last	Trend	 Services	Last	Trend
 Industrial production	1.4		 Services output	1.4	
 Manufacturing PMI	55.2		 Services PMI	54.5	
 Goods exports to the EU	3.9		 FTSE 350 Banks	66.5	
 People	Last	Trend	Legend		
 Visitor arrivals of EU residents	-2.3		 Above pre-referendum trend		
 Net migration of EU nationals	-45.4		 Within pre-referendum trend		
 Vacancies in health & social work	10.2		 Below pre-referendum trend		

For definitions, sources and more information, see technical notes at the end of this document.



Under pressure

Households are feeling the squeeze, with real wages falling by 0.3% in 2017, as the depreciation of the pound pushed up import prices, impacting on the cost of consumer goods on the high street.

Retail sales growth has fallen as a result, but remains positive. But there has been a bigger impact on consumer durables spending, suggesting households are cutting back on larger purchases. This may be due to the uncertain outlook, as consumer confidence has also fallen, although it is only a little below its long-term average.

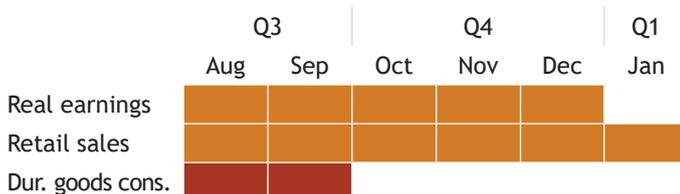
The past 12 months for consumers resembles the sluggish recovery during the first four years of the Cameron government, which saw real wages stagnant or falling.

The outlook for consumers partly depends on whether the changes in sterling and confidence will prove temporary. While the sterling effect is expected to ease, the prospects for consumer confidence are harder to call. This depends on how consumers see the general economic situation - including the Brexit outlook - as well as more immediate changes to their personal financial situation.

Data summary

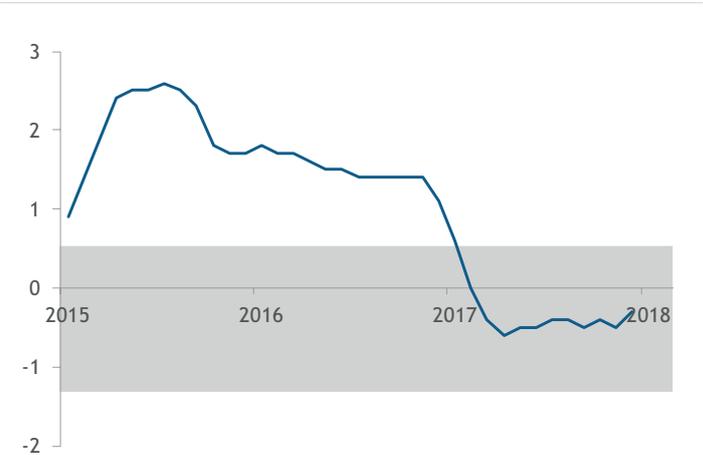
	Real earnings	Retail sales	Durable goods consumption
Last	-0.3	1.4	-0.1
Period	Dec 17	Jan 18	Q3 17
Previous	-0.5	0.9	-1.8
50% range	-1.3/0.5	0.5/2.9	1.6/7.3
Frequency	Monthly	Monthly	Quarterly

6-month heatmap



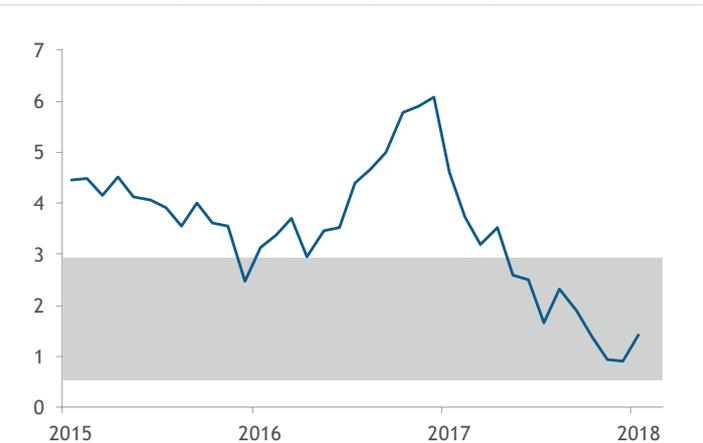
Real earnings

%-change year-on-year



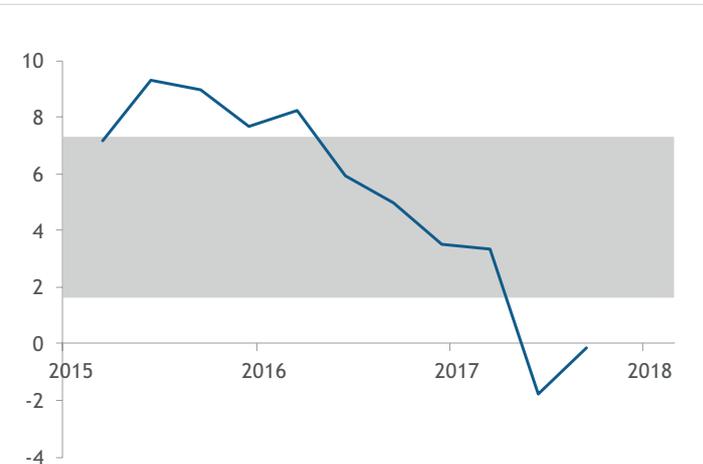
Retail sales

3-month moving average, %-change year-on-year



Durable goods consumption

%-change year-on-year





Slow recovery, uncertain outlook

Business investment has recovered from its 2016 trough and is now edging above the growth rate for the economy. However, the Bank of England recently observed that business investment is notably weaker than in previous expansions.

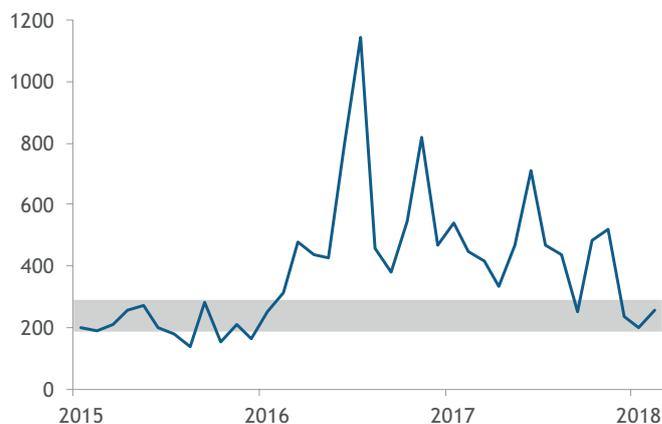
Financing conditions are favourable and global demand is high, but uncertainty in the UK outlook may be weighing on investment.

We have included an index of economic policy uncertainty in our dashboard. This is a crude measure of UK newspaper coverage of economic uncertainty, but it captures well the spike seen after the Brexit vote. While the picture has been erratic, the trend has been down since then, with a sharp drop at the end of last year when the phase one Brexit deal was reached.

We are using London house prices as an indirect indicator of foreign investor sentiment. Foreign demand is especially important at the top end of the London market and is one reason why the growth rate of prices has dropped over the past few years, turning negative in the third quarter of last year.

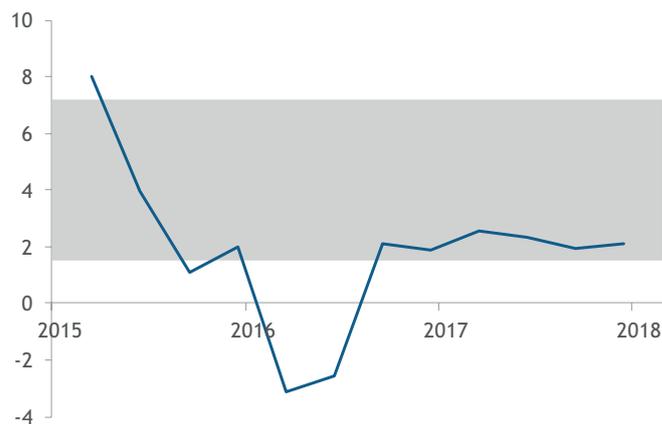
Economic policy uncertainty

Index based on newspaper articles



Business investment

%-change year-on-year

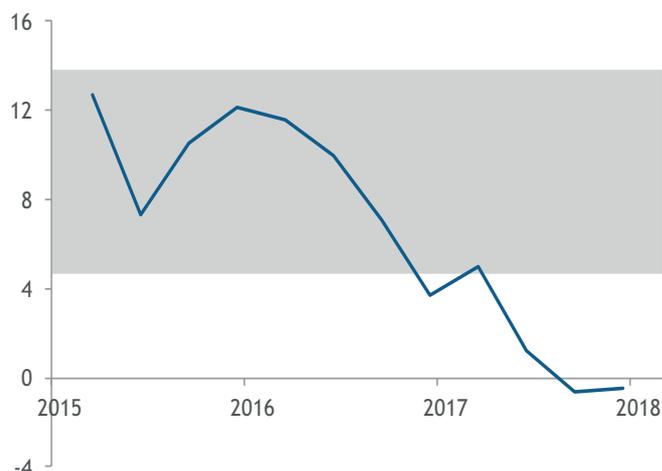


Data summary

	Economic policy uncertainty	Business investment	London house prices
Last	256.5	2.1	-0.5
Period	Feb 18	Q4 17	Q4 17
Previous	199.6	1.9	-.06
50% range	186.0/291.6	1.5/7.2	4.7/13.8
Frequency	Monthly	Quarterly	Quarterly

London house prices

%-change year-on-year



6-month heatmap

	Q3		Q4		Q1	
	Sep	Oct	Nov	Dec	Jan	Feb
Econ. pol. unc.	Dark Red					
Business inv.	Dark Red					
London house p.	Dark Red					



Holding steady

Industrial production tends to be volatile, which is why we use a 3-month moving average in our dashboard.

But the headline picture for producers over the past 12 months has been relatively benign. A more buoyant manufacturing sector in the second half of 2017 has helped to keep industrial production growth in positive territory.

UK goods exports performed strongly throughout last year, with the 3-month moving average for exports to the EU up 5.8% at the end of 2017.

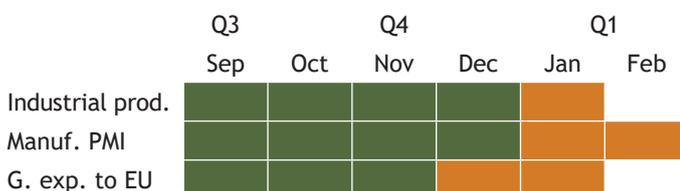
The stronger global economy has helped, but exports to the EU have also been boosted by the fall in the value of sterling.

Both factors have helped to boost manufacturing confidence, with the PMI rebounding from the sharp drop seen after the referendum and holding at a respectably high level. That confidence has eased back over the past few months, but remains well above the level consistent with an expansion in manufacturing output.

Data summary

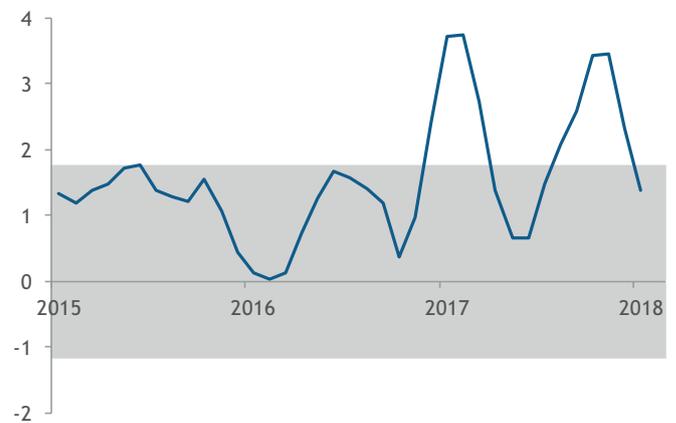
	Industrial production	Manufacturing PMI	Goods exports to the EU
Last	1.4	55.2	3.9
Period	Jan 18	Feb 18	Jan 18
Previous	2.3	55.3	4.2
50% range	-1.2/1.8	50.7/55.5	-1.7/6.9
Frequency	Monthly	Monthly	Monthly

6-month heatmap



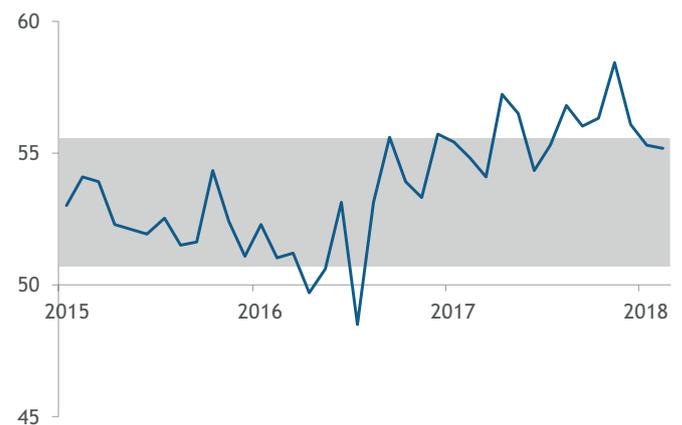
Industrial production

3-month moving average, %-change year-on-year



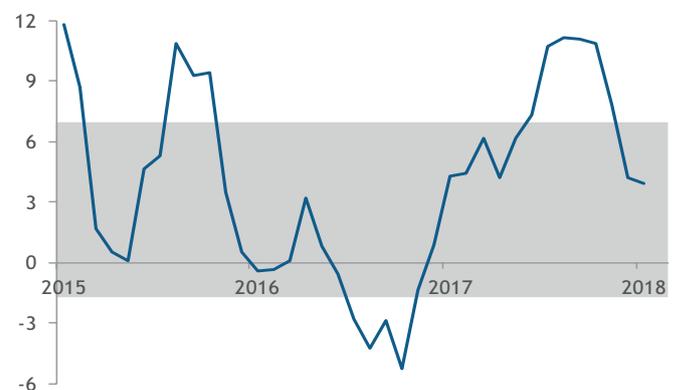
Manufacturing PMI

Above 50 indicates output expansion



Goods exports to the EU

3-month moving average, %-change year-on-year





A drag on growth

Growth in the service sector has been slowing down since the start of 2015. With the 3-month moving average advancing just 1.4% at the end of last year, the sector is as almost as flat as it has been at any time since the middle of 2010.

If anything, the outlook may be becoming tougher, with confidence in the sector slipping back in the final months of last year, although it still remains consistent with expansion.

As a rough rule, business-facing services are faring better than those with consumer-facing operations, as they tend to be more globally orientated and the fall in the pound has allowed them to boost exports.

We have included the performance of banking stocks relative to the market in our dashboard, as a crude proxy for how services may be expected to fare in the Brexit negotiation.

Banking stocks have underperformed since 2010, but have done relatively well more recently, so this indicator might be stronger than it first appears, with little sign that the sector is gripped by Brexit pessimism.

Data summary

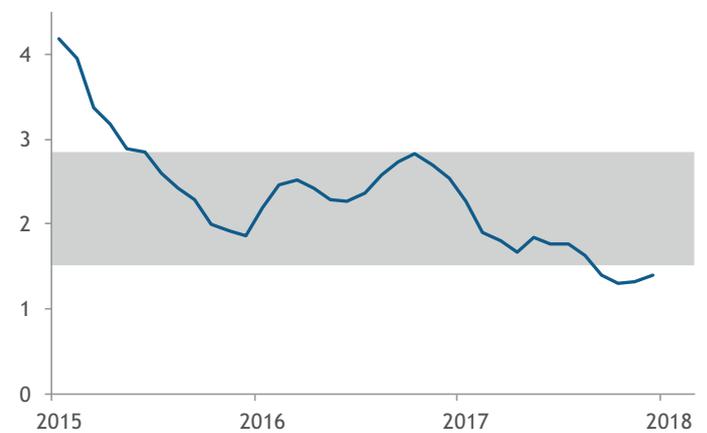
	Services output	Services PMI	FTSE 350 Banks
Last	1.4	54.5	66.5
Period	Dec 17	Feb 18	Feb 18
Previous	1.3	53.0	65.3
50% range	1.5/2.8	53.2/57.2	70.5/87.1
Frequency	Monthly	Monthly	Monthly

6-month heatmap

	Q3		Q4		Q1	
	Sep	Oct	Nov	Dec	Jan	Feb
Services output	Dark Red					
Services PMI	Orange	Orange	Orange	Orange	Dark Red	Dark Red
FTSE 350 Banks	Dark Red					

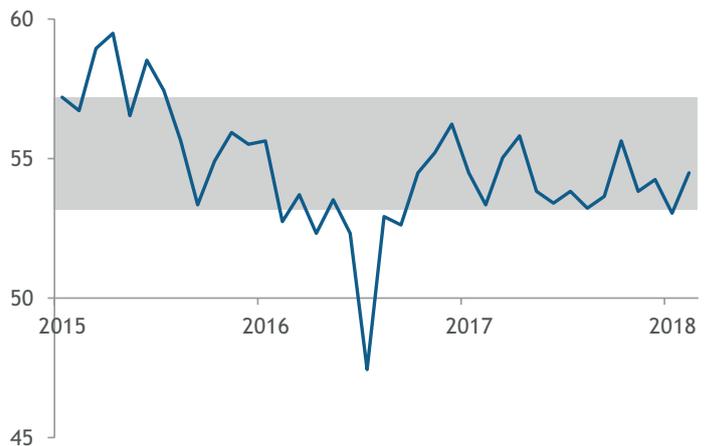
Services output

3-month moving average, %-change year-on-year



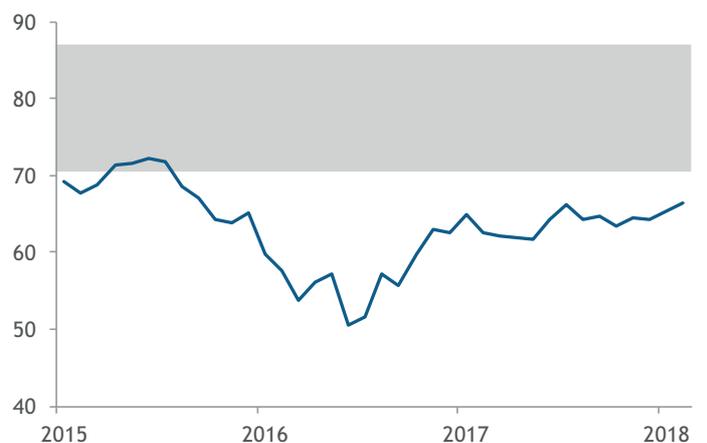
Services PMI

Above 50 indicates output expansion



FTSE 350 Banks

Relative to FTSE 350, Jan 2010 = 100





Less pull for EU nationals

Visitor numbers are highly erratic, but the 3-month moving average suggests an upward spike in the second half of 2016, most likely reflecting the fall in sterling.

This was followed by an equally sharp decline in the growth rate in the first half of 2017, with the growth rate of EU visitors turning negative for the first time since 2012.

Net migration from the EU is also in decline, although this predated the Brexit vote, with the net inflow peaking in 2013. The net outflow of 43,000 seen in the second quarter last year - the most recent quarter for which data is available - exceeds anything seen in recent years.

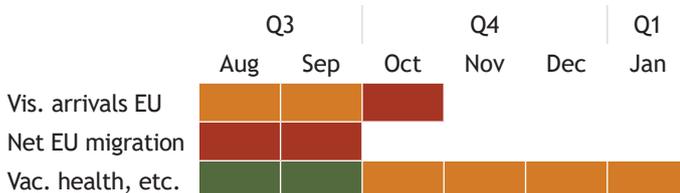
It is tempting to put this down to the UK losing its pull for EU nationals, but there is also likely to be less push, as the EU economy has strengthened over the past year.

The drop in migration does not yet appear to be seriously impacting on the health and social work sectors, which have only recently seen vacancies growing, and remaining well below the 30,000-plus level seen during much of 2014.

Data summary

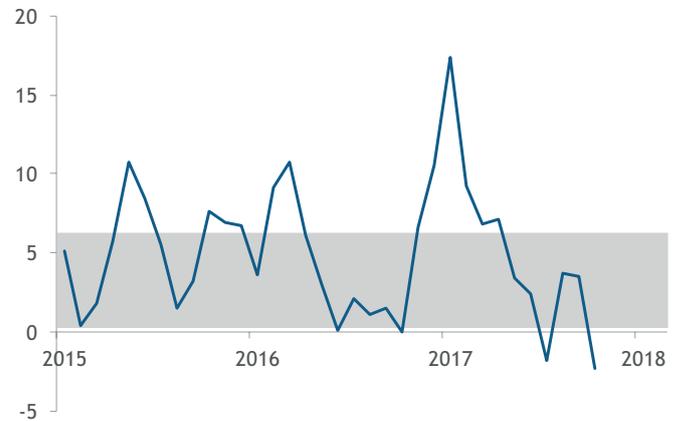
	Visitor arrivals of EU residents	Net migration of EU nationals	Vacancies in health & social sector
Last	-2.3	-45.5	10.2
Period	Oct 17	Q3 17	Jan 18
Previous	3.5	-43.4	5.9
50% range	0.2/6.3	4.4/37.9	1.2/21.9
Frequency	Monthly	Quarterly	Monthly

6-month heatmap



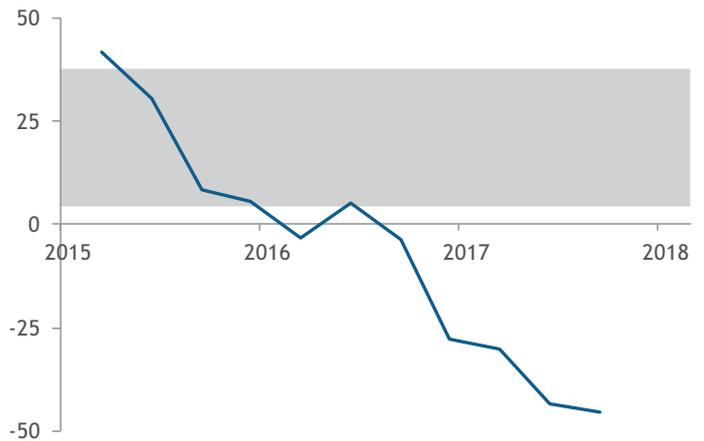
Visitor arrivals of EU residents

3-month moving average, %-change year-on-year



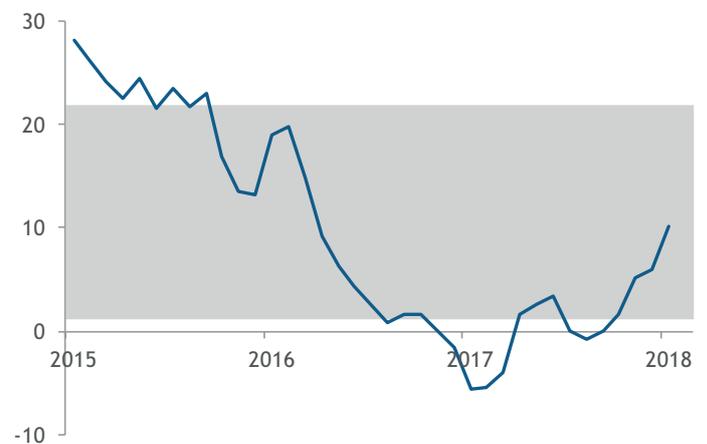
Net migration of EU nationals to the UK

4-quarter moving average, %-change year-on-year



Vacancies in health and social work

3-month moving average, %-change year-on-year



Technical notes

Global Counsel's Brexit dashboard seeks to take the macro pulse of the British economy, using a balanced set of 15 indicators each quarter. We are not attempting to isolate the impact of Brexit, from all the other factors affecting the economy, as that is near impossible. Instead, we are providing a health check, to see where the economy is faring better or worse, compared to the years before the vote.

We look at data in five areas, with three indicators each. These indicators are in most cases growth rates, which reflect the dynamics in the British economy. In some cases, the data is smoothed using moving averages to reveal the dynamics more clearly.

The dashboard indicates how well the economy is performing compared to the post-financial crisis, pre-referendum period from January 2010 to May 2016. For each indicator, we identify the range - shown by a grey band - within which we would expect to see half of all observations based on the data in the reference period and assuming each series is normally distributed, which may only be approximately correct for some of the data series. The width of the grey band is calibrated to 0.675 times the standard deviation in each case, so that it contains 50% of the probability distribution. This is the basis for the green, amber and red colour coding for the most recent observation, with amber used where the value falls within the grey band and green or red used for favourable or unfavourable values respectively outside the band.

The following provides a description of the data, the sources used and the reasons why the indicator is included in the Brexit dashboard. Data in many cases has been provided through CEIC Data.

Consumers

Real earnings, or real average weekly earnings, are recorded as part of the Office for National Statistics' (ONS) monthly wages and salaries survey and published in the UK labour market statistical bulletin. The indicator shows values for regular pay only. Real earnings provide an indication of how consumers' purchasing power is changing.

Retail sales are recorded in the monthly business survey - retail sales inquiry of the ONS. The data excludes automotive fuel. It is based on volumes and seasonally adjusted. It provides an indication of the overall level of consumption.

Durable goods consumption, or household final consumption expenditure on durable goods, is recorded as part of the ONS's quarterly national accounts. Figures are real (chain-linked) and seasonally adjusted. The decision of a household to purchase a durable good is similar to making an investment decision, which can be delayed under unfavourable conditions.

Industry

Industrial production is based on the Index of Production released by the ONS. It measures the volume of production for the manufacturing, mining and quarrying, energy supply, and water and waste management industries. Figures are seasonally adjusted.

Manufacturing PMI, or the Manufacturing Purchasing Managers' Index, is published monthly by Markit. It shows to what extent the sector is expanding, based on a survey of purchasing managers who have early access to data about company performance. This makes it one of the most important leading indicators for changes in output. Manufacturing is the largest industrial sector in the UK and considered to have high multiplier effects for the wider economy.

Goods exports to the EU are released monthly by the ONS in the UK trade statistical bulletin. Figures are real (volume-based). The indicator shows to what extent trade ties between the UK and the EU are being disrupted or deepened.

Services

Services output is based on the Index of Services released by the ONS. The data is real (chain-linked) and seasonally adjusted. It is an indicator of growth in the sector.

Services PMI, or the Services Purchasing Managers' Index, is published monthly by Markit. It shows to what extent the sector is expanding, based on a survey of purchasing managers who have early access to data about company performance. This makes it one of the most important leading indicators for changes in output.

FTSE 350 Banks shows the relative performance of the FTSE 350 Banks Index (which consists of the UK's major banks that are also part of the FTSE 350 Index) to the FTSE 350 Index, re-based to 100 in January 2010. The data is provided by the FTSE Group. Banks are considered especially exposed to Brexit.

Investment

Economic policy uncertainty is an index based on the number of articles in two of the leading British newspapers, The Times of London and the Financial Times, which mention economic policy uncertainty. The source is 'Measuring Economic Policy Uncertainty' by Scott R. Baker, Nicholas Bloom and Steven J. Davis. Data can be found at www.policyuncertainty.com. The level of uncertainty about a country's economic policy direction impacts on its business environment and is important for investment decisions.

Business investment is recorded as part of the ONS's business investment in the UK statistical bulletin. Figures are real (chain-linked) and seasonally adjusted. Investment signals confidence in the economy and is critical for current and future growth.

London house prices are recorded on a quarterly basis by Nationwide. It is one possible proxy for the UK's attractiveness as an investment destination.

People

Visitor arrivals by EU residents are recorded in the ONS's overseas travel and tourism statistical bulletin. It indicates how attractive the UK is for tourists, business travellers and other visitors.

Net migration of EU nationals to the UK is recorded in the provisional long-term international migration estimates published by the ONS on a quarterly basis. Based on the internationally recognised definition, a migrant is a person who spends at least a year in the UK, so that the country effectively becomes the new

country of usual residence. It shows how attractive the UK is as a country to work, study and live.

Vacancies in the health and social work sector, or vacancies in the sector of human health and social work activities, are recorded in the ONS's monthly vacancy survey, published as part of the UK labour market statistical bulletin. Figures are seasonally adjusted. The UK health sector is seen as above-average reliant on migrant labour.

For further information, please contact the lead authors of the report:

Dr Gregor Irwin, Chief Economist, g.irwin@global-counsel.co.uk
Thomas Gratowski, Senior Associate, t.gratowski@global-counsel.co.uk

A: 5 Welbeck Street, London, W1G 9YQ
T: +44 (0)203 667 6500
E: info@global-counsel.co.uk
www.global-counsel.co.uk
[@global_counsel](https://twitter.com/global_counsel)

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