

# Brexit dashboard Q3 2018

29 August 2018

*This is the third quarterly issue of the Global Counsel Brexit dashboard. More than two years on from the vote - and with just six months before the UK leaves the EU - we are taking the macro pulse of the UK economy, using a balanced set of 15 indicators. 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.*

## Cruising in the economic slow lane, for now

The economy bounced back in Q2, shaking off the effects of bad weather at the start of the year, and buoyed by a surge in retail sales as consumers enjoyed some sunshine, not to mention the World Cup. But when we look through the noise in the data it is hard to avoid the conclusion that the economy is cruising in the slow lane, motoring along for sure, but not at any great speed, and too slow to power a recovery in living standards after ten years of under-performance.

There are also signs that the economy may be at a turning point, as Brexit uncertainty rises and the deadline for a withdrawal deal nears. While our dashboard shows retail sales rising in Q2, spending on durables has fallen, suggesting households are nervous about larger purchases. And businesses appear equally cautious, with investment sluggish and Brexit uncertainty the biggest risk factor. Confidence in manufacturing and service is holding up - for now - but at levels that are underwhelming.

The big question for the coming months is whether the Brexit negotiations could upset this steady, if unspectacular progress. A deal that sets Britain on a course for a Brexit that is not too disruptive could encourage consumers to spend more and give businesses the urge to invest. But if there is no deal this could damage confidence and see the UK stuck on the economic hard shoulder.

Even in the best-case scenario there are long-term, supply-side concerns for policymakers. We are already seeing signs that net migration from the EU is no longer a pressure valve on a tightening labour market, constraining future growth. And even if investment picks up, it is unlikely to return to levels normally seen at this stage in the cycle, holding back productivity growth. The prospects for the economy moving into the fast lane look remote.

### Snapshot of latest indicators | last available month or quarter

Consumers	Last	Trend	Investment	Last	Trend
Real earnings	0.4		Economic policy uncertainty	218.0	
Retail sales	3.6		Business investment	2.0	
Durable goods consumption	-0.1		London house prices	-1.9	
Industry	Last	Trend	Services	Last	Trend
Industrial production	1.4		Services output	1.5	
Manufacturing PMI	54.0		Services PMI	53.5	
Goods exports to the EU	-2.8		FTSE 350 Banks	60.1	
People	Last	Trend	Legend		
Visitor arrivals of EU residents	-11.6			Above pre-referendum trend	
Net migration of EU nationals	-3.6			Within pre-referendum trend	
Vacancies in health & social work	12.6			Below pre-referendum trend	

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



### Split screen

The mixed signals on consumer spending need careful analysis. Real earnings continue to grow, although the rate of growth has fallen recently. With inflation expected to fall, partly as the effect of the 2016 depreciation on import prices washes out, real earnings growth is expected to pick up again in the coming months.

Consumer sentiment is another big driver of spending and here the survey indicators have also picked up in recent months, with an increase in the GfK measure for how households evaluate their personal situation. But there is now a noticeable split in actual spending by consumers by the type of purchase.

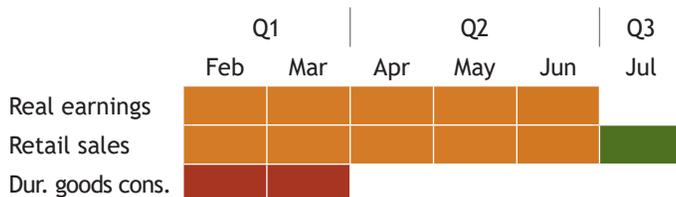
Our dashboard indicators show that retail sales jumped up in the second quarter this year, driven by online spending rather than sales on the high street. Just as some of the slowdown in the first quarter was temporary, due to bad weather, some of the increase in the second quarter may have been driven by the combination of the good weather and the World Cup.

This contrasts with our dashboard indicator for durable goods consumption, which has now stalled. This indicator is less timely but shows the most recent value for Q1 this year turning negative for the first time in several years, with consumers holding back on big-ticket purchases.

### Data summary

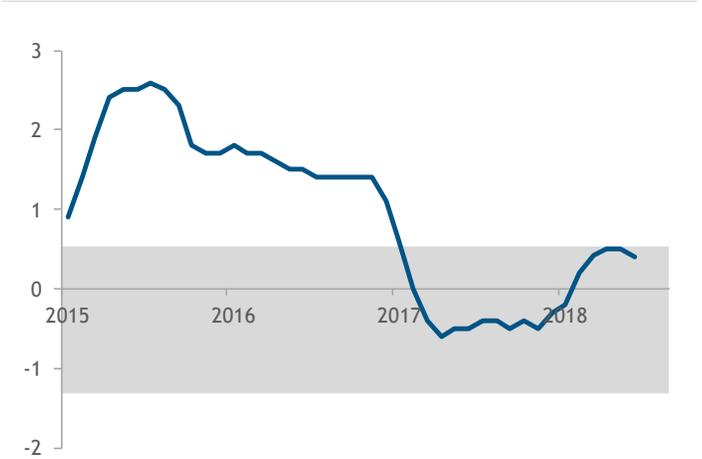
	Real earnings	Retail sales	Durable goods consumption
Last	0.4	3.6	-0.1
Period	Jun 18	Jul 18	Q1 18
Previous	0.5	2.8	3.0
50% range	-1.3/0.5	0.5/2.9	1.7/7.9
Frequency	Monthly	Monthly	Quarterly

#### 6-month heatmap



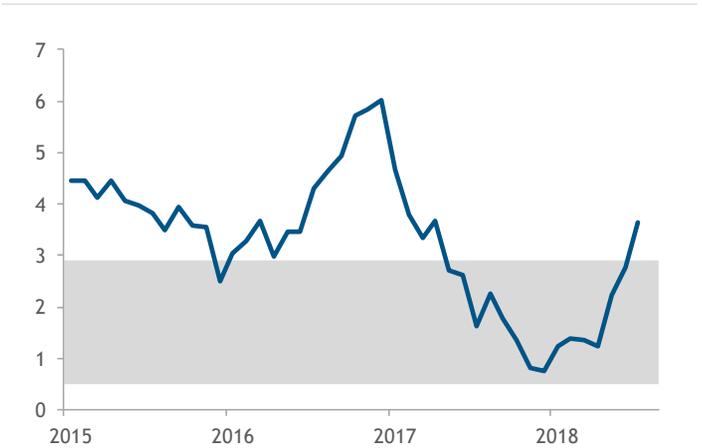
### Real earnings

%-change year-on-year



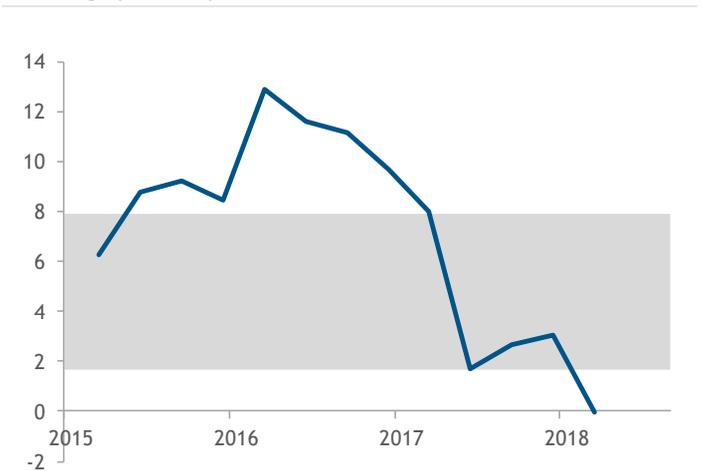
### Retail sales

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



### Durable goods consumption

%-change year-on-year





### Cautious and underpowered

Our dashboard indicator for economic policy uncertainty is now mid-range and still well below the post-referendum highs of mid-2016. This is surprising, given that uncertainty about the outcome of the Brexit negotiation is widely acknowledged to have increased. However, this may be because the focus is for now on the politics and the process rather than the potential consequences for economic policy specifically, which remain hard to assess.

Our dashboard shows that business investment remains sluggish. On a quarter-by-quarter basis, it fell by 0.4% in Q1 this year. This too may reflect the bad weather at the start of the year, as some of the decline was driven by a fall in investment in the construction sector.

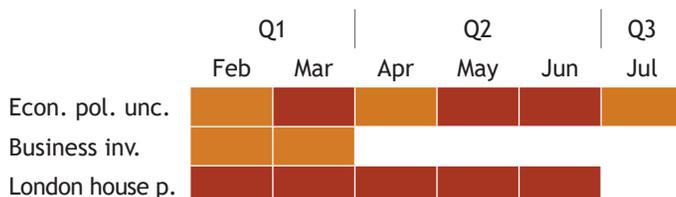
The Deloitte survey of CFOs in Q2 suggests that Brexit is once more the top concern for businesses, with a large majority of respondents expecting it will damage the business environment over the long term. What is clear is that at current levels business investment are unable to power a recovery in the economy and are another drag on labour productivity growth, which remains depressed.

London house prices continued to fall in Q2, suggesting that investment in new-builds is likely to remain restrained. This is also a broader indicator of weak sentiment.

### Data summary

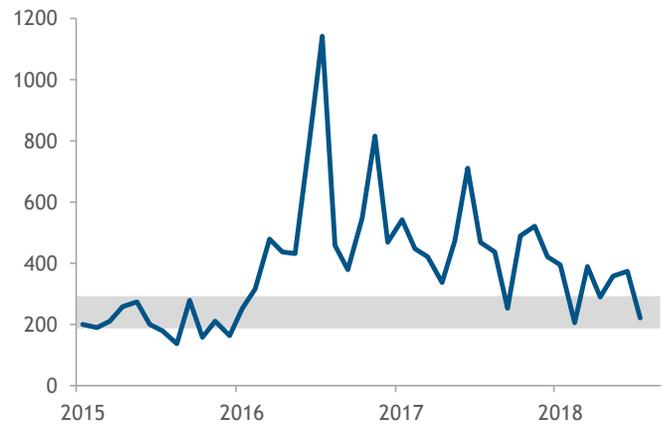
	Economic policy uncertainty	Business investment	London house prices
Last	218.0	2.0	-1.9
Period	Jul 18	Q1 18	Q1 18
Previous	371.7	3.1	-1.0
50% range	186.0/291.6	1.8/7.2	4.7/13.8
Frequency	Monthly	Quarterly	Quarterly

#### 6-month heatmap



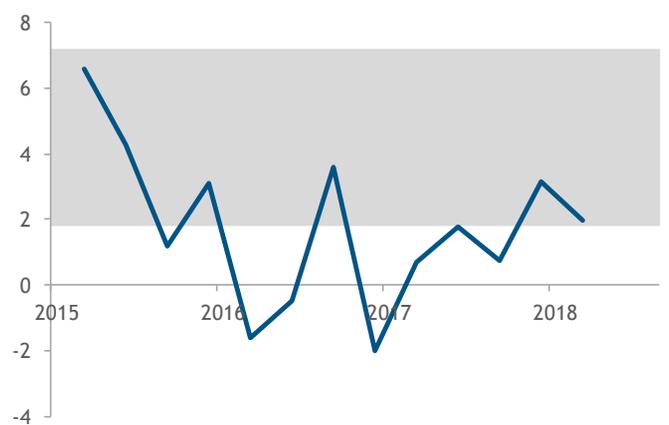
### Economic policy uncertainty

Index based on newspaper articles



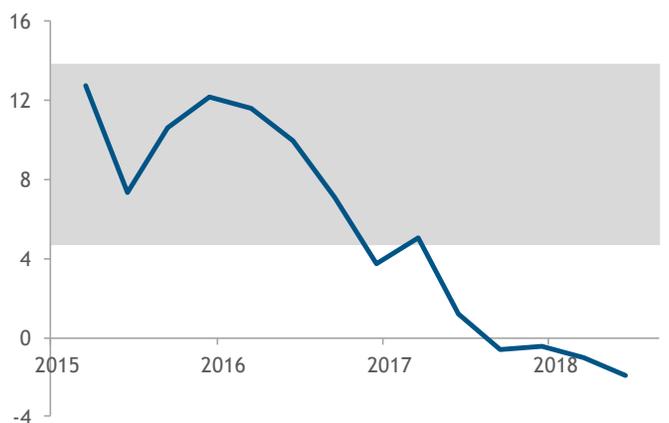
### Business investment

%-change year-on-year



### London house prices

%-change year-on-year





### Trending down

For some time, industry has been the relative bright spot for Britain's Brexit economy, but there are signs this is changing. Both manufacturing sentiment - shown by the PMI - and manufacturing activity, have been notably more subdued since the start of the year. The manufacturing PMI shown in our dashboard is now at 54, which is still consistent with expansion, but down from a high of 58.2 in November last year.

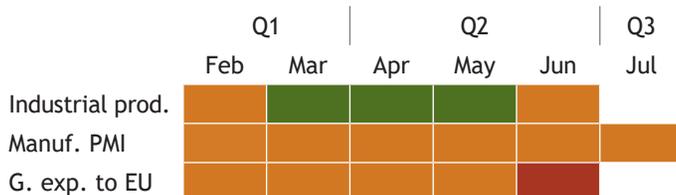
One reason for this is that net trade made only a modest contribution of 0.1 percentage points to growth in Q1 and is expected by the Bank of England to have subtracted as much as 0.6 percentage points from growth in the Q2, due to a fall in goods exports. While that reflects some temporary factors, the prospects for goods exports and the manufacturing sector remain tied to global economic prospects, which have become more uncertain, particularly in emerging economies.

Our dashboard shows that the growth rate of exports to the EU has been in a steady downward decline since the latter part of last year and is now firmly negative. It is hard to disentangle what effect, if any, the prospect of Brexit may be having from other factors. The growth rate of the eurozone economy fell in the first half of this year to just 0.4%, but that appears to reflect mostly temporary factors and slower demand for eurozone exports, rather than a fall in underlying domestic demand growth.

### Data summary

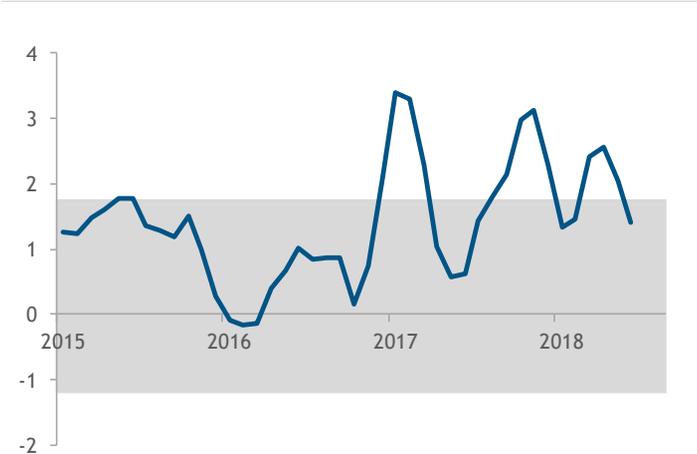
	Industrial production	Manufacturing PMI	Goods exports to the EU
Last	1.4	54.0	-2.8
Period	Jun 18	Jul 18	Jun 18
Previous	2.1	54.3	-1.2
50% range	-1.2/1.8	50.7/55.5	-1.5/5.5
Frequency	Monthly	Monthly	Monthly

### 6-month heatmap



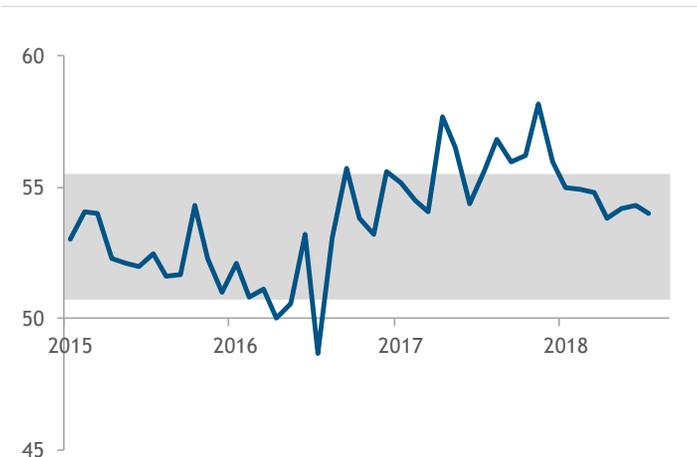
### Industrial production

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



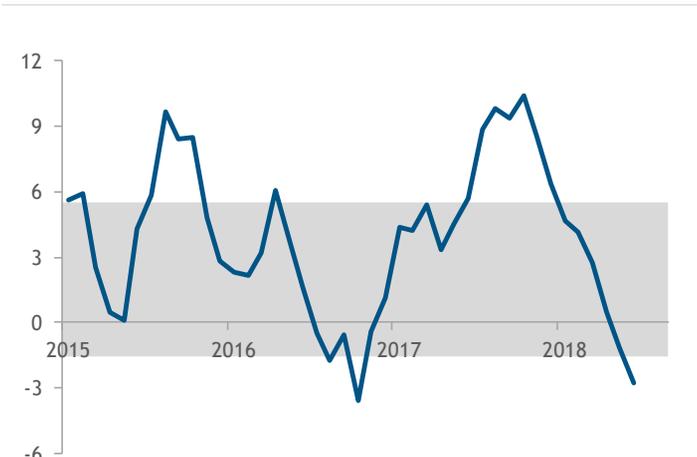
### Manufacturing PMI

Above 50 indicates output expansion



### Goods exports to the EU

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





### Still struggling

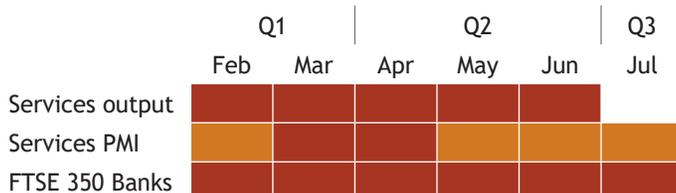
The services sector has never fully recovered from the shock of the referendum. The contrast with the industrial sector, and especially manufacturing, which benefited from the fall in sterling, is one of the defining features of the post-referendum data. This continues, with our dashboard showing output of services expanding by just 1.5% in the three months to June, compared with the year before. And while the PMI in July, at 53.5, is above the level consistent with expansion, it does not signal a significant recovery and remains below that for manufacturing, even as the benefits of the fall in sterling are losing their impact.

There have been important developments for services in the Brexit negotiation this quarter, with the UK's Chequers proposals prioritising market access for goods over services, in part because the government believes the costs of maintaining regulatory alignment for many services would be too high. That tension is greater for financial services, including banking, than just about any other sector. This month our dashboard shows the banking indicator falling back further into the red, with FTSE-350 banking stocks are performing worse than the composite index. There are many factors contributing to that, but Brexit is likely to be one of them.

### Data summary

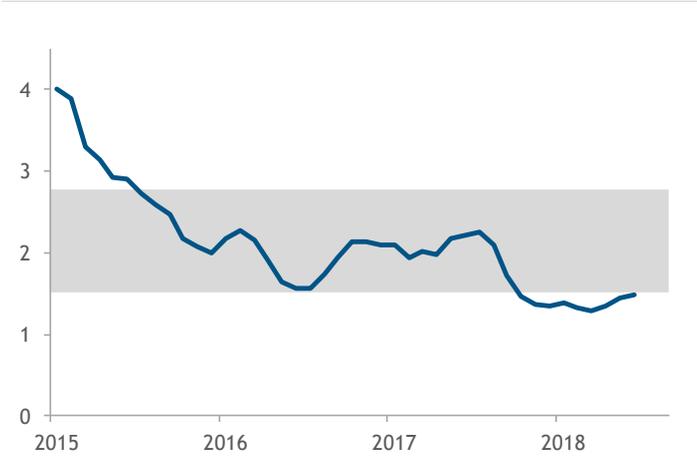
	Services output	Services PMI	FTSE 350 Banks
Last	1.5	53.5	60.1
Period	Jun 18	Jul 18	May 18
Previous	1.4	55.1	59.8
50% range	1.5/2.8	53.2/57.2	70.5/87.1
Frequency	Monthly	Monthly	Monthly

#### 6-month heatmap



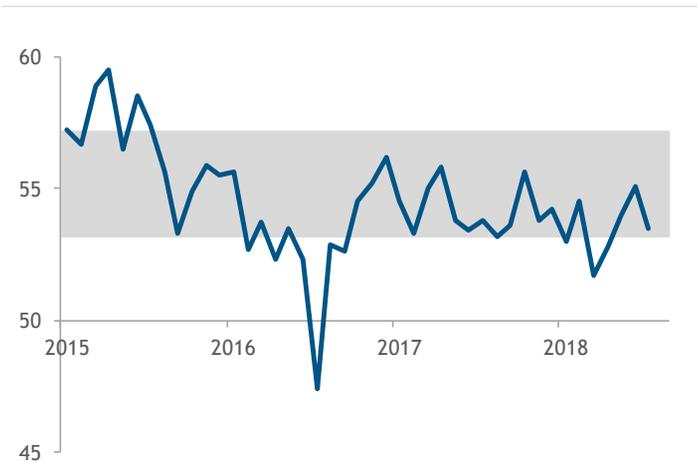
### Services output

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



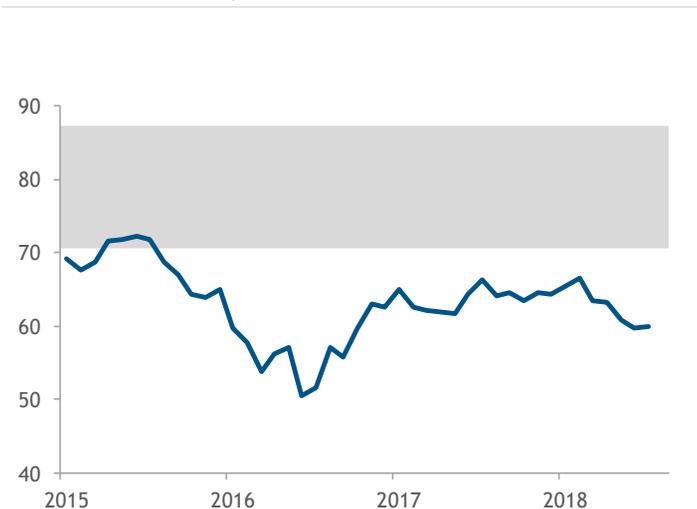
### Services PMI

Above 50 indicates output expansion



### FTSE 350 Banks

Relative to FTSE 350, Jan 2010 = 100





### Tightening labour market

Our dashboard shows the four-quarter moving average for net migration of EU nationals to the UK is now falling and is significantly below the rates seen in the run up to the 2016 referendum.

The actual number of EU nationals working in the UK fell by 86,000 to 2.28mn between April and June this year, which is the biggest drop in over 20 years. By contrast, the number of non-EU nationals working in the UK rose during this period, according to the ONS, possibly helped by a recent relaxation in Tier-2 visa rules.

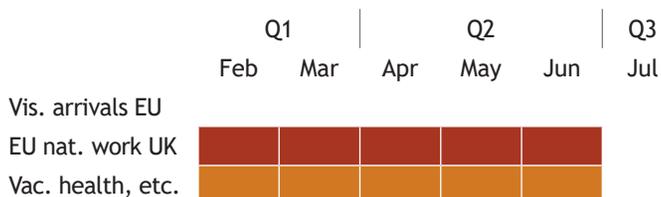
The flow of EU migrants is economically important because the UK labour market is now extremely tight by just about any definition. The unemployment rate is low, the participation rate is high, workers are on average satisfied by the hours they work and the number of people who would like a job, but who are not actively looking, has fallen sharply, according to the Bank of England. Moreover, the number of vacancies per person in the labour force is now above the pre-crisis average.

These labour market pressures are also beginning to manifest themselves in a manner that is politically sensitive, with our dashboard showing a faster increase in the number of vacancies in the health and social work sectors. Brexit is likely to be one factor driving this.

### Data summary

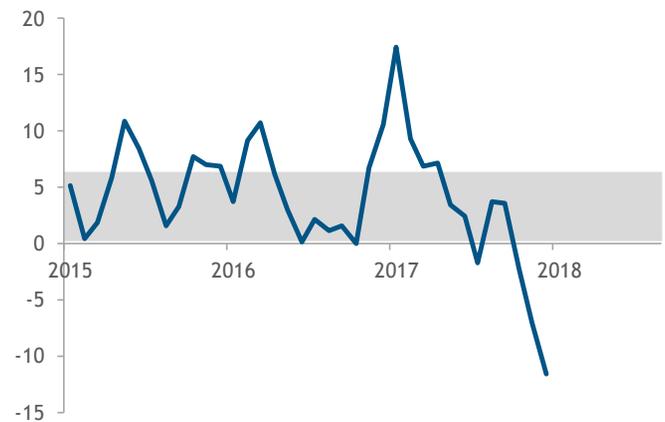
	Visitor arrivals of EU residents	Net migration of EU nationals	Vacancies in health & social sector
Last	-11.6	-3.6	12.6
Period	Dec 17	Q2 18	Jul 18
Previous	-7.1	-1.2	7.3
50% range	0.2/6.3	6.6/14.6	1.2/21.9
Frequency	Monthly	Quarterly	Monthly

#### 6-month heatmap



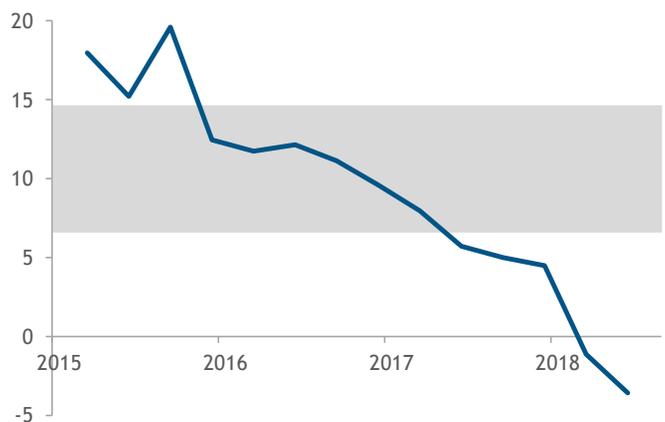
### Visitor arrivals of EU residents

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



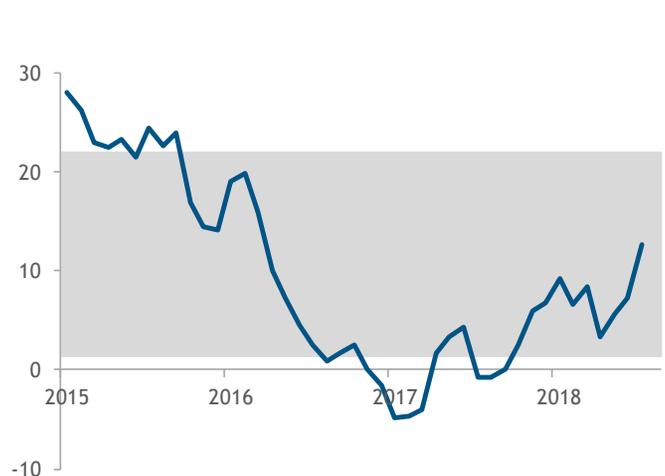
### EU nationals working in the UK

3-month 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.

### 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](http://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.

### 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.

### 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](mailto:g.irwin@global-counsel.co.uk)  
Thomas Gratowski, Senior Associate, [t.gratowski@global-counsel.co.uk](mailto: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](mailto:info@global-counsel.co.uk)  
[www.global-counsel.co.uk](http://www.global-counsel.co.uk)  
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