Quarterly Economic Briefing

January 2018

Contents

Introduction

Introduction

The purpose of this Quarterly Economic Briefing is to provide a focused quarterly assessment of a small number of key national and international economic trends to help inform future investment decisions and identify new opportunities.

The key economic indicators covered in this report are:

- GDP growth
- GDP forecasts
- Interest rates
- Inflation
- Unemployment
- Investment
- Productivity
- Exchange rates
- UK Trade
- Industry views
- Regional outlook

For each indicator we provide a short overview of the current trend along with a brief analysis of what it means for businesses. In addition to these indicators, we have also included an overview of the latest government and political situation at the front of the briefing to provide additional insight and context.

The next publication will be in April.

Headlines

Modest growth

GDP was estimated to have increased by 0.4% between Quarter 2 (April to June) and Quarter 3 (July to September) 2017. The UK Quarter 3 growth of 0.4% was some way short of the EU28 average of 2.6%

Interest rates rise

November's increase in the Bank Rate from 0.25% to 0.5% was the first movement in the Bank Rate since August 2016 when the rate was reduced from 0.5% to 0.25.

Weaker pound

The continued and prolonged uncertainty around the implications of leaving the European Union mean that a weaker pound is likely to remain for the foreseeable future, causing inflationary pressures on imported goods.

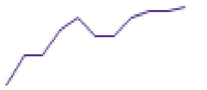
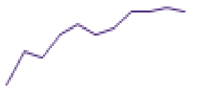
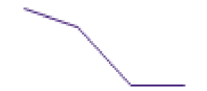
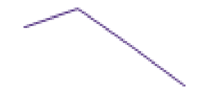
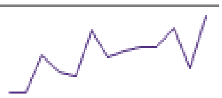
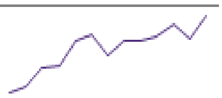
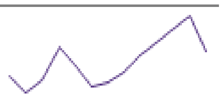
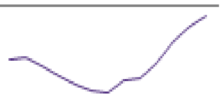
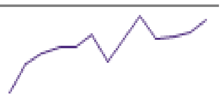
High Inflation

The Consumer Prices Index including owner occupiers' housing costs (CPIH) 12-month rate was 2.7% in December 2017. This fell slightly on November's rate of 2.8% which was the highest since March 2012 when it was 3.1%.

Low unemployment

The unemployment rate for August to October 2017 was 4.3%. The rate is the same as for May to July 2017 and is the joint lowest since March to May 1975.

Key indicators summary

Updated 2nd January 2018		Latest	12 month trend
Bank base rate	%	**0.50**	
3mo LIBOR	%	**0.52**	
10yr gilt	%	**1.32**	
USD:GBP	rate	**1.36**	
EUR:GBP	rate	**1.13**	
CPI	% y-o-y	**3.10**	
RPI	% y-o-y	**3.90**	
Unemployment	%	**4.30**	
GDP	% y-o-y	**1.70**	
FTSE 100	index	**7,648**	
FTSE 250	index	**20,681**	
Baltic Dry	index	**1,230**	
Oil	$/bbl	**66.4**	
Gold	$/oz	**1,313.1**	

Key indicators

The table to the left sets out the historic trend for the key headline indicators.

Government & political update

Brexit

We have seen some progress on Brexit negotiations, which provide a few points of assurance for organisations but equally shows how difficult it will be to reach a full agreement over the next year.

The EU and UK have now reached agreement on the basic 'divorce' settlement. Though neither side has confirmed or denied the scale of the figure, there is speculation that this could be between £35bn and £39bn. This includes

- **Assurance for EU citizens** working in the UK and their employers. EU citizens in the UK and UK citizens in the rest of the EU, plus their children and partners, have the right to stay. There is likely to be a process of applying for 'settled status'; further details should be available in the coming months.
- Some warm words for organisations operating across the **Ireland-Northern Ireland** border that they will be able to continue to operate pretty much as at present. The agreement provides the basis for further discussions; there is still lots to work out and negotiate before we have a clear plan for the border which organisations can action and there is still scope for this to come unstuck.

What happens next?

- The divorce settlement needs to be incorporated into a formal legal agreement.
- Once that is done, the negotiations will move on to phase two: agreeing **a transition** period and principles for future trade relationship between UK and EU. The basis for an agreement on 'transition' is fairly clear: a two year period from March 2019 during which we will be in the EU 'in all but name': continued membership of single market, customs union and subject to European Court of Justice (ECJ) but no voting rights in EU decision making. This should give many businesses greater certainty for the short to medium term.
- The earliest we are likely to see agreement on the transition arrangements is March this year; but this may well slip.
- Negotiations on the **future UK-EU trade relationship** are unlikely to start before March. The EU has expressly said that the UK needs to provide more clarity on what it wants before the EU will agree to start discussing this. That leaves very little time to agree the most difficult part of the negotiations. The EU has already made clear that they will not be able to agree a full detailed trade agreement with the UK before 'Brexit day' in March 2019. The talks this year will seek to agree a broad framework and set of principles for future UK-EU trade; the detail will then need to be hammered out after March 2019.
- We have made progress. But we now reach the more difficult part of the negotiations; the clock is ticking away; and there are many political tensions to be navigated to secure an agreement. Whether we have an 'orderly' or a 'chaotic' Brexit still hangs in the balance.

Business impact

The turbulent economic and political environment has continued to negatively impact business confidence in the past quarter. For more information see the overview of the ICAEW Business Confidence Monitor in the Regional outlook section.

It will be interesting to see if confidence returns as more certainty surrounding Brexit negotiations unfolds.

Government & political update (continued)

In other news…

Brexit dominates the UK political agenda and is crowding out the UK government's ability to do very much else. Nonetheless there were a number of significant announcements around the Budget in November:

- **Industrial Strategy:** the government set out a plan that covers skills, innovation, infrastructure, key sectors, and a focus on local strategies. This included 'sector deals' between government and industry to increase sector productivity. Four sector deals have been agreed: life sciences, construction, artificial intelligence and the automotive sector. More are in development including food and drink, creative industries and industrial digitalisation.
- **Housing:** the Budget provided additional investment which will support smaller as well as large house builders, combined with the Stamp Duty Land Tax relief for first time buyers, disincentives for keeping homes empty, planning reforms and encouraging landlords to provide longer term tenancies.

There are a couple of other areas to watch over the coming weeks and months:

- An **Immigration White** Paper is due imminently, setting out the government's proposals for a post-Brexit immigration policy.
- We expect government to publish draft regulations to implement some of their **corporate governance reforms**, including new requirements for companies to report on how they engage with wider stakeholders, large private firms to report on their governance arrangements and listed companies to report on pay ratios.

Business impact

The Brexit Secretary, David Davis, admitted in December of 2017 that the Government had not produced sector by sector impact assessments. While a letter sent to the Prime Minister by the Brexit Secretary in the same month, and leaked recently, reveals the lack of planning for a no deal scenario compared to those taken by the EU to warn industry of the consequences.

Businesses should continue to make contingency arrangements for a 'no deal' Brexit scenario. Planning should be made around:

- Skills shortages
- Cost base movements
- Inflation
- Impact of WTO tariffs

Businesses should explore what their sector is doing in relation to agreeing a sector deal and either understand the opportunities such a deal presents; or seek to influence the development of the deal so that it is fit for purpose and focused on the most pressing issues for businesses in the sector.

What to look out for in 2018

Positive Global Economic Outlook

Global economic activity is strengthening. Having seen the weakest growth since the global financial crisis in 2016 at 3.2%, global growth is projected to grow to 3.6% in 2017 and 3.7% in 2018. This outlook is not universal - upswings in the Euro area Japan, emerging Asia, emerging Europe and Russia are expected to offset downward revisions to growth expectations in the USA and UK

Political Developments

There will be a number of European developments that will set the context for 2018.

- As set out in the previous pages, the main challenge for the UK will be securing an exit from the European Union that has minimal cost by securing comprehensive free trade agreements with the bloc and other countries.
- In Germany, Angela Merkel will continue in her struggle to form a coalition government.
- In France, we will see how Macron's open view of the world (ie pro-European, pro-international, pro-trade) develops.
- 2017 saw a surge in populism in many countries. Could Italy continue this in 2018 with its anti-establishment movement in the upcoming parliamentary elections?

In the US President Donald Trump will deliver a State of the Union address to Congress on January 30th. The speech, typically given every year of a president's term except for the first, will report on the condition of the US and will allow the President to set out their legislative and other policy priorities.

November will see the mid-term elections for Congress and will be a key sentiment check for the Trump presidency. A Democrat majority would be the first since 2011 and would make it much more difficult for Trump to push through his agenda.

Elsewhere, Venezuela is set for presidential elections in February, Iraq will hold elections in May, Mexico is set for presidential elections in July and Brazil will hold presidential elections in October.

Sport

2018 holds two of the largest sporting events in the World Cup and Winter Olympics. While providing entertainment they also come at an interesting time politically for the two host nations. Russia hosts the World Cup shortly after the Presidential Election. While the Winter Olympics, hosted in South Korea comes at a time where tensions with its neighbour North Korea are rising. Both Russia and South Korea will be keen to broadcast a positive perception of itself.

Closer to home, it has been announced that Birmingham has been selected as host city for the 2022 Commonwealth Games. This could provide significant commercial and development opportunities for our clients in the coming years.

In this page we have set out a number of developments that are set to occur in 2018.

The points stated on this page are taken from a variety of sources, including the following:

The Economist – The World In 2018 as well as the thoughts of executive editor Daniel Franklin

Financial Times – The Year Ahead…

IMF – World Economic Outlook

Nesta – 10 Predictions for 2018

Consumer Technology Association – CES 2018

Wired.co.uk – Various

What to look out for in 2018 (continued)

Technology

Experts suggest a number of developments to occur in 2018.

- Changes to the collaborative economy. 2017 saw much scrutiny of the gig economy with workers perceived to be getting a bad deal. Could 2018 see collective action that will create new forms of the collaborative economy models that see a wider benefit to all.
- Drones to are to start operating on a much larger scale. With technological breakthroughs making drones cheaper and more technologically advanced, the sky is to become busier. Drones will be delivering parcels, supporting law enforcement and providing public services on a larger scale.
- At CES 2018, one the worlds largest business and consumer technology gatherings, Artificial Intelligence (AI) is an area of focus. From big data analytics and solutions, speech recognition, learning and decision making products to predictive technology, AI is increasingly seen as something that will shape the future of businesses. Both China and the US are investing large sums to lead the way in this technology, with the UK well placed behind them (according to the Financial Times).
- Elsewhere, 2018 is set to see SpaceX send tourists to the moon for the first time. The company owned by Elon Musk also plans to send its first spacecraft to Mars.

GDP growth

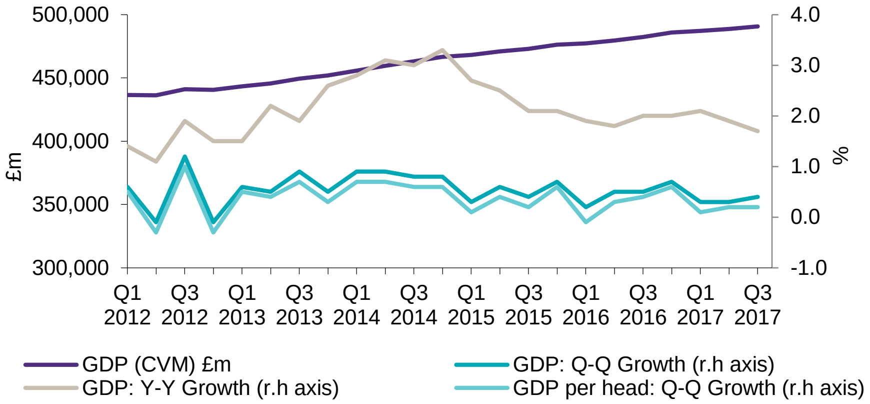
Change in Gross Domestic Product (GDP) is the main indicator of economic growth. Office for National Statistics data illustrates that UK GDP was estimated to have increased by 0.4% between Quarter 2 (April to June) and Quarter 3 (July to September) 2017. Services was the strongest contributor to GDP growth in Quarter 3 having increased by 0.4%.

In Quarter 3 (July to September) 2017, GDP per head grew by 0.3% compared to Quarter 2 (April to June). GDP per head is now 2.4% above the GDP pre-economic downturn peak in Quarter 1 2008, having surpassed it in Quarter 2 2015.

The UK Quarter 3 growth of 0.4% was some way short of the EU28 average of 2.6% and lower than other large economies such as France (0.6%), Germany (0.8%) and the US (3.2%).

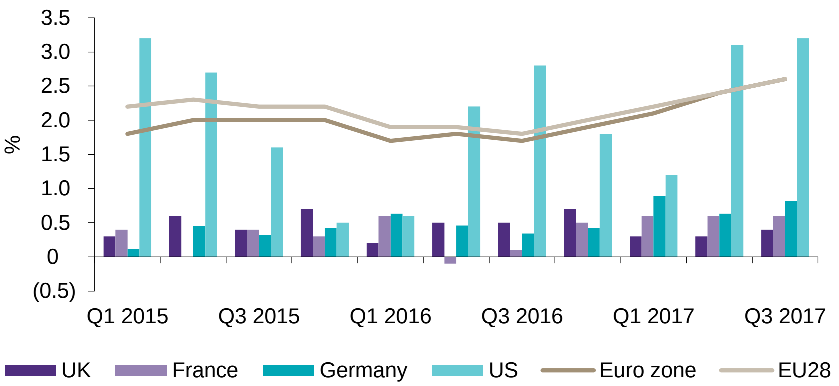
For more information see the latest ONS releases on Gross Domestic Product. The next ONS release on GDP is due 22nd February 2018.

GDP Growth



Source: ONS

Country GDP growth



Country GDP growth
Source: National Statistics offices

Business impact

Economic growth is important for all businesses in a variety of different ways. Over time a period of prolonged economic growth leads to major improvements in living standards, expansion of existing markets and opening of new ones. It sees the creation of new job opportunities and wage increases. However the converse is also true for a period of economic contraction.

This slow down, if prolonged, will therefore present both risks and opportunities. Therefore all business cases and investment plans should include a range of sensitives that assess both positive and negative GDP growth.

GDP forecasts

After a good growth performance in 2016, it slowed in the first half of 2017. The graph below provides a selection of GDP forecasts for the UK.

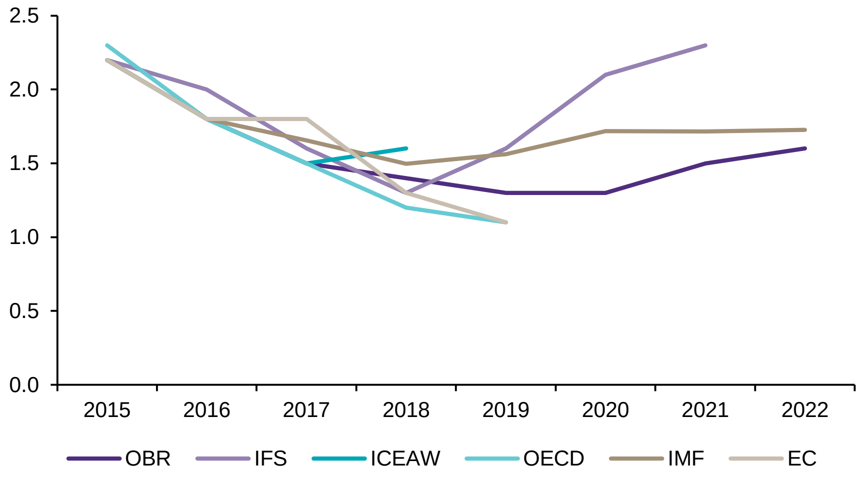
The OBR Economic and fiscal outlook (November 2017) announced that they have lowered their GDP forecasts in every year of their forecast. The primary reason for lowering this forecast is due a downward revision to potential productivity growth. They expect growth to average 1.4% a year over the next five years. Growth is expected to slow over the next two years as public spending cuts and Brexit related uncertainty weigh on the economy, before picking up modestly in the years after as productivity growth picks up.

The OECD Economic Survey for the United Kingdom (October 2017) anticipates projected growth to weaken. It notes that other advanced economies will continues to recover, but UK growth will be around 1.0% in 2018 under the assumption that the UK exits the European Union in 2019. They do highlight that the outcome of Brexit negotiations are difficult to foresee, and if more favorable than assumed, boosts to trade and investment could see growth increase.

The latest ICAEW UK Economic Forecast (Q4 2017) expects GDP growth of 1.5%, rising to 1.6% in 2018. With consumer spending expected to remain constrained, minor uplifts to exports and manufacturing, and little expected movement in fiscal and monetary policy, GDP growth will remain slow.

The IMF World Economic Outlook (October 2017) singled out the UK as the notable exception in the strong growth seen in major economies in the first part of 2017. They see growth of 1.7% in 2017 falling to 1.5% in 2018.

GDP Forecasts



Source: Various

Business impact

As noted previously the biggest implications of these forecasts is the uncertainty that they highlight. Therefore, all business cases and investment plans should include a range of sensitivities that assess both positive and negative GDP growth.

Interest rates

The Bank of England's Monetary Policy Committee (MPC) sets monetary policy to meet the 2% inflation target and help sustain economic growth and employment.

In the latest meeting on 13th December 2017 the members of the MPC voted unanimously to maintain the Bank Rate at 0.5%. This follows November's increase in the Bank Rate by 0.25 percentage points, from 0.25% to 0.5%. This was the first movement in the Bank Rate since the reduction from 0.5% to 0.25% that was made in August 2016.

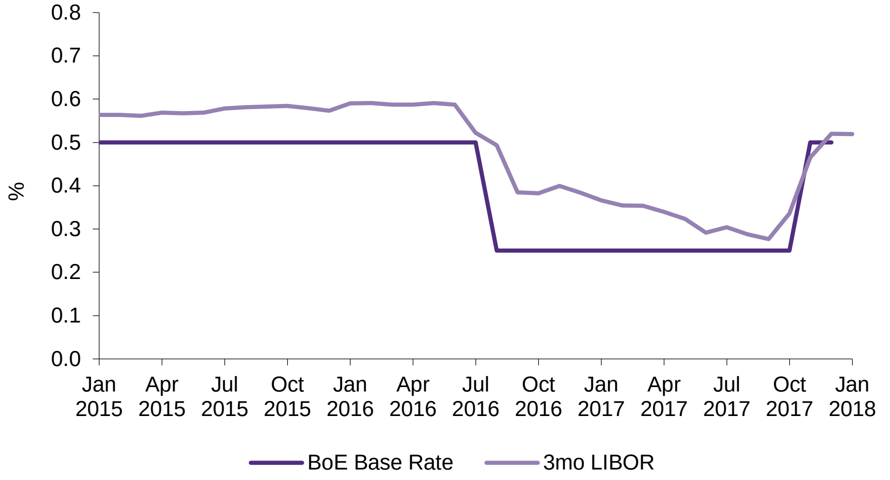
The MPC voted unanimously to continue the programme of Quantitative Easing by maintaining the stock of sterling non-financial investment-grade corporate bond purchases, financed by the issuance of central bank reserves, at £10 billion, and to maintain the stock of UK government bond purchases, financed by the issuance of central bank reserves, at £435 billion.

The Committee highlights that unemployment is at a 42 year low, the global economy is growing strongly, domestic financial conditions are highly accommodative and consumer confidence has remained resilient. As a result, the committee now considers it appropriate to tighten their stance on monetary policy in order to return inflation sustainability to the target.

The Committee acknowledges that there remain considerable risks to the outlook of the economy, which includes how households, businesses and financial markets respond to developments related to the EU withdrawal process. The MPC states that they will respond to developments in the economic outlook as they occur.

For more information see the Bank of England's latest Monetary Policy Summary and Minutes and Inflation Report. The next MPC meeting is Thursday 8th February 2018.

Interest rates



Source: Thomson Reuters Datastream

Business impact

Given the recent rate rise it will be interesting to see whether consumer spending reacts or whether further change is needed. With household real income squeezed in the near term, consumer spending is likely to remain sluggish.

Inflation

The Consumer Prices Index including owner occupiers' housing costs (CPIH) 12-month inflation rate was 2.7% in December 2017, down from 2.8% in November 2017. The 2.7% recorded in November was the highest rate since March 2012 when it was 3.1%.

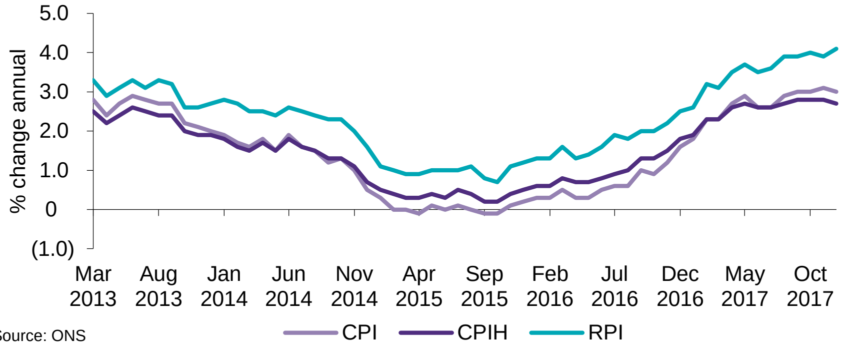
The downward effect came from air fares and a fall in a range of recreational goods, including toys and games. This was partially offset, by increases to tobacco prices due to duty increases that came into effect following the Autumn Budget, along with an increase in petrol and diesel prices.

The Consumer Price Index (CPI) 12-month rate was 3.0% in December 2017, down from 3.1% in November 2017.

The Bank of England's Monetary Policy Committee expects inflation to have peaked in the latter months of 2017 as the past depreciation of sterling and recent increases in energy prices continue to be passed on to consumers. It is then expected to fall over the next year as the effects of rising import prices diminish and wage growth recovers.

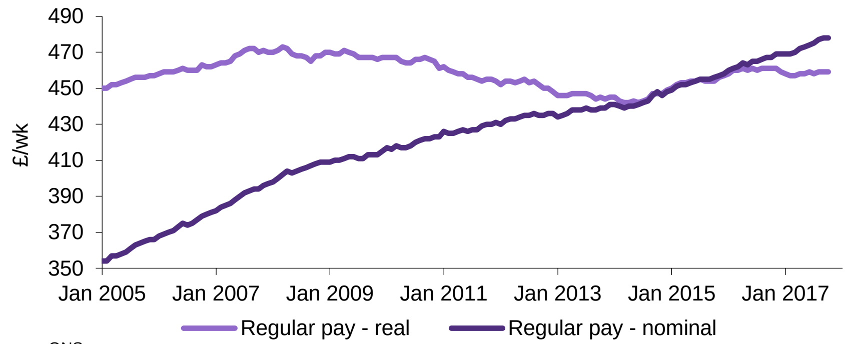
For more information see the latest ONS Inflation and Price Indices update and the Bank of England's Inflation Report. The next ONS release is 13th February 2018.

Inflation rates



Source: ONS

Average Weekly Earnings



Source: ONS

Business impact

One of the primary effects of inflation is the impact that it has on employees and the extent to which they are feeling 'squeezed'. This in turn impacts on salary expectations and demands. This is particularly true for companies that use inflation to set pay increases.

The knock on impact of 'squeezed consumers' is a reduction in consumer spending which will impact those businesses whose business model is B2C.

State benefits and many occupational pensions also rise in line with CPI so any changes will have further implications for both Government and individual employers.

Unemployment

Unemployment is a valuable indicator of the overall health of an economy and the extent to which prosperity and economic growth is filtering through the economy. The unemployment rate, measured by the Office for National Statistics, is the proportion of the economically active population (those in work plus those seeking and available to work) who are unemployed.

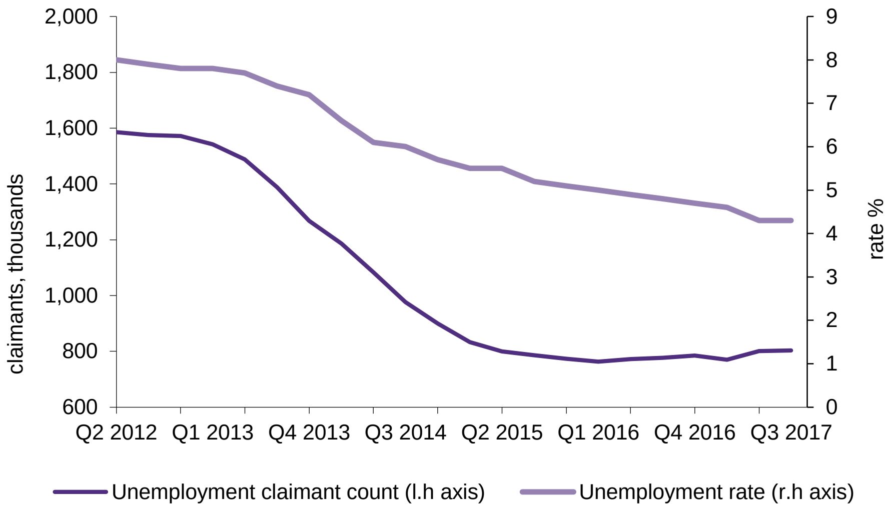
ONS estimates show that for August to October 2017, the unemployment rate (people not in work but seeking and available to work) was 4.3%. The rate is the same as for May to July 2017 and is the joint lowest since March to May 1975. There were 1.43 million unemployed people, 26,000 fewer than for May to July 2017, and 182,000 fewer than a year earlier.

The employment rate (the proportion of people aged from 16 to 64 who were in work) was 75.1% for August to October 2017. This is slightly up on the 75.0% recorded in July to September and the 74.4% for a year earlier. There were 32.08 million people in work, which was 56,000 fewer than for May to July 2017, but 325,000 more than a year earlier.

For August to October 2017, there were 8.86 million people aged from 16-64 who were economically inactive (not working and not seeking or available for work), 115,000 more than for May to July 2017 but 56,000 fewer than for a year earlier. The inactivity rate (the proportion of people aged from 16 to 64 who were economically inactive) was 21.6%, higher than the 21.2% recorded for May to July 2017 but down slightly than a year earlier (21.7%).

For more information see the latest ONS Unemployment update. The next data release for unemployment figures from the ONS is 24th January 2018.

Unemployment



Source: ONS

Business impact

With unemployment at record lows, getting the balance right between high employment and high productivity is a challenge for the United Kingdom, and it is one that businesses can play an important role in addressing. It is something that we see as critical in helping to create a vibrant economy, not least because of the clear link between improved productivity and improved prosperity.

A key issue for businesses is that with record levels of employment, skills gaps and hard to fill vacancies will increase – already an issue for many employers. This may be compounded by the perception – if not yet the reality – that government will reduce immigration in the near future. Businesses therefore need to think about how they develop and attract talent.

Should rising unemployment return as an issue, for many businesses this is less likely to impact on business decisions and operations. However, rising unemployment would have a number of important implications for organisations in the public and third sectors, many of whom would need to change policy or practice in order to respond to increasing levels of people out of work.

Investment

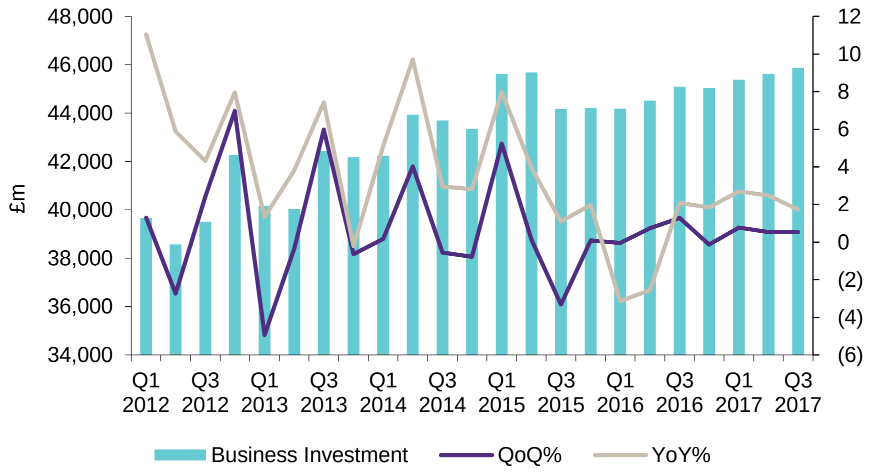
Investment in new equipment influences the productive capacity of the economy. It can also be seen as a measure of business optimism as to the future growth of the economy.

The ONS measure business investment as net investment by private and public corporations. This includes investments in transport, information and communication technology (ICT) equipment, other machinery and equipment, cultivated assets (such as livestock and vineyards), intellectual property products (IPP, which includes investment in software, research and development, artistic originals and mineral exploration), and other buildings and structures.

Business investment does not include investment by central or local government, investment in dwellings, or the costs associated with the transfer of non-produced assets (such as land).

Business investment has continued to grow positively in 2017 after a more mixed picture in 2016. Business investment was estimated to have increased by 0.5% to £45.9 billion in Quarter 3 2017 from £45.6 billion in Quarter 2 2017. The assets that contributed positively to business investment between Quarter 2 (April to June) 2017 and Quarter 3 (July to September) 2017 were intellectual property products (IPP) and other buildings and structures. For more information see the latest ONS release on Business Investment.

Business investment



Source: ONS

Business impact

The Bank of England, in its most recent Agents' summary of business conditions, stated that investment plans are being boosted by desire to increase efficiency to meet anticipated demand increases. However, uncertainty around the UK's future trading relationships are putting a drag on investment intentions.

Productivity

The first graph shows different measures of UK productivity over the past five years released by the ONS. Movements are shown for output per hour, output per job and output per worker. UK labour productivity, as measured by output per hour, is estimated to have grown by 0.9% from Quarter 2 (April to June) 2017 to Quarter 3 (July to September. This is the largest increase in productivity since Quarter 2 of 2011. Labour productivity in both Services and Manufacturing Industries by 1.0% on the previous quarter.

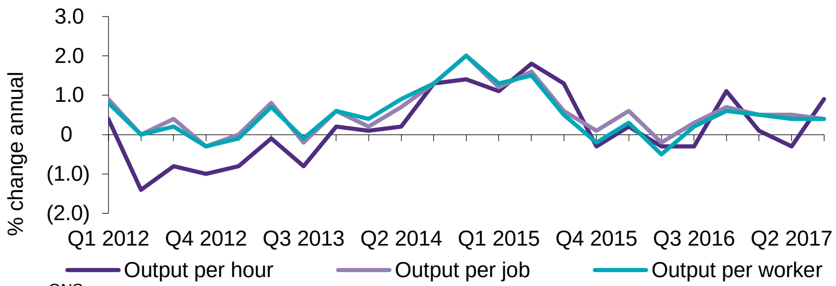
Over the longer term, labour productivity growth has been lower on average than prior to the economic downturn. The outlook for productivity also looks set to disappoint, with the OBR Economic and fiscal outlook lowering GDP forecasts due to downward revisions to future productivity growth reflecting post-crisis weakness.

The second graph shows historic and forecast productivity growth rates, as measured by GDP growth, for the OECD, France, Germany and the USA. In Quarter 4 of 2017 USA (1.40%) had the greatest rate of productivity growth, higher than Germany (1.34%), the OECD Total (1.08%), France (0.86%) and the UK (0.48%).

The latest OECD Economic Survey for the United Kingdom stresses that productivity gains have had no meaningful contribution to output performance since 2007, which has instead been driven by higher employment and hours worked by employee. As a result, output per hour is nearly 20% lower than it would have been had it continued to expand at pre-crisis trend growth. Stagnant productivity has held back real wages and real GDP per capita. Reviving labour productivity growth will therefore be key to ensuring higher living standards in future.

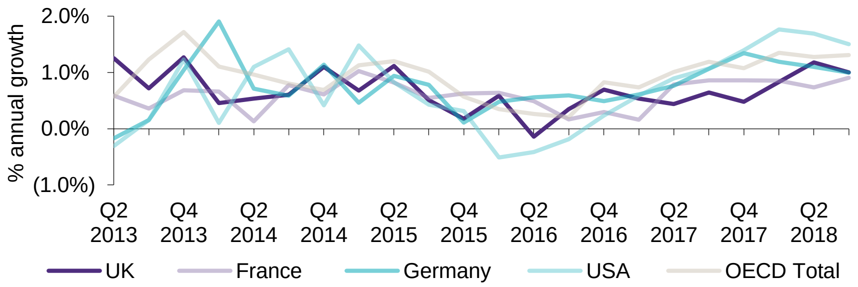
For more information see the latest ONS Labour Productivity update and OECD Productivity Statistics. The next ONS release is 6th April 2018.

UK productivity



Source: ONS

OECD Productivity inc forecast



Source: OECD

Business impact

Brexit could have further implications for UK productivity. The OECD highlights estimates that Brexit could reduce total factor productivity (ie the portion of output not explained by labour and capital used in production) by approximately 3% over the next ten years through diminished trade openness, weaker research and development intensity and a smaller pool of skills.

The extent that the labour market is kept open to foreign workers could be of critical importance.

In the Autumn Budget Government has announced plans to address the UK's productivity challenge, including: cutting corporation tax to support business investment; improving skills through increased numbers of apprenticeships and the introduction of T-levels; and, delivering infrastructure projects like the Mersey Gateway Bridge, the Northern Hub in Manchester and Crossrail.

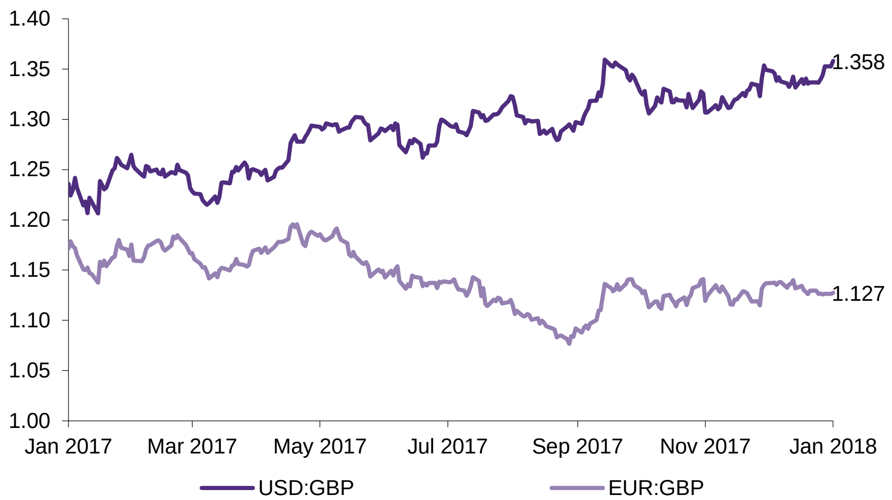
Exchange rates

Despite negotiations around Britain's exit from the European Union continuing notable uncertainty remains and in turn it is likely that a weaker pound will remain for the foreseeable future.

The latest ICAEW UK Economic Forecast highlights that since the European Union referendum the pound is now 10% weaker than the dollar and 14% weaker than the euro. Despite hopes of the weaker pound rebalancing the UK economy from services and consumption to manufacturing and exports, domestic demand remains fragile. Part of this may be down to lags in time as a result of the renegotiation of prices and increased cost of inputs. It will be interesting to see if exports see a boost in the future, especially with the manufacturing sector reporting more positive results in the latest PMI Index (See 'Industry Views' section).

The OECD Economic Survey for the United Kingdom also notes that persistence of currency weakness could reflect financial market expectation about the longer-term cost for the UK economy. In the near term, weaker sterling has propped up valuations of UK companies operating on foreign markets and reporting their profits in domestic currency. In contrast, the valuation of companies mainly selling on the local market has been subdued, as investors expect greater domestic consequences of Brexit.

Exchange rates



Source: Thomson Reuters Datastream

Business impact

Exchange rates have a direct implication for any international work and investment affecting both the cost of doing business as well as the potential profits that can be realised. Contingencies – positive and negative – should therefore be applied to any investment plans and business cases within this investment priority.

This is particularly the case for businesses who export goods and/or import raw materials.

For those that import raw materials, many of which are paid for in dollars, this change is likely to squeeze profits significantly.

For those that export there may be an increase in demand as products and services become cheaper. Although given the uncertainty and nervousness that exists within the Eurozone currently this demand may be tempered.

UK trade

UK trade shows import and export activity and is the main contributor to the overall economic growth of the UK.

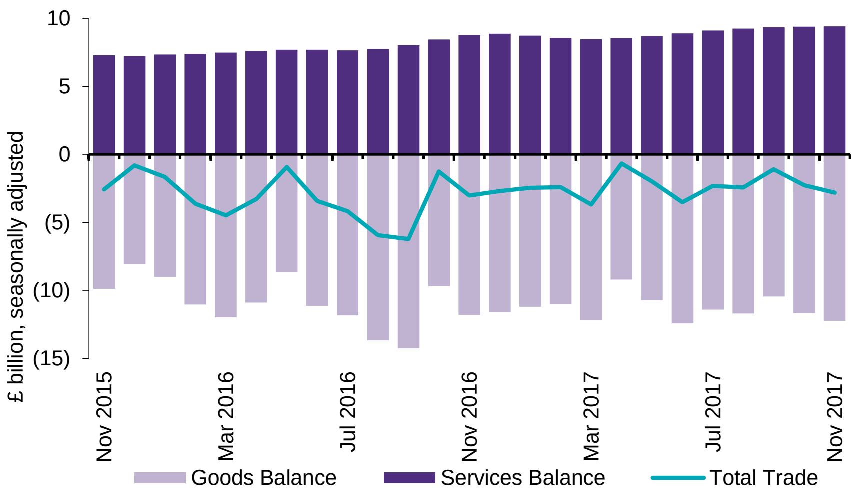
The Office for National Statistics stated that in the three months to November 2017 the total UK trade (goods and services) deficit narrowed by 2.1 billion to £6.2 billion.

This was mainly due to goods exports, which increased 2.6% (2.2 billion) to £87.6 billion. Unspecified goods (particularly non-monetary gold), machinery and transport goods were the largest contributors to this increase over the three month period.

Over the last year, the UK's trade deficit (goods and services) narrowed by £4.3 billion between the three months to November 2016 and the three months to November 2017. This was primarily due to increases in goods and services exports, by 10.6% (£8.4 billion) and 6.7% (£4.4 billion) respectively. Although imports of goods and services also increased, by 6.1% (£7.0 billion) and 3.7% (£1.5 billion) respectively, these increases were offset by the larger increases in goods and services exports.

For more information see latest ONS update on UK trade statistics. The next release is 9h February 2018.

Balance of UK trade



Source: ONS

Business impact

Despite hopes that the weaker pound would boost demand for British goods, exports remained subdued in the past two quarters.

There is optimism in the market that this might improve, with manufacturers stating that output has climbed to its highest level in over four years in the latest PMI Index (See 'Industry Views' section).

The outlook for export growth will also depend on any changes to the United Kingdom's trading arrangements and how companies anticipate and respond to these.

As noted previously the extent to which individual businesses are exposed to EU export and import markets will present both threats and opportunities to business growth.

Industry views

The first chart shows the Markit Purchasing Managers Index for the Construction, Services and Manufacturing sectors. The Index is based on survey responses from panels of senior purchasing executives who are asked to state whether business conditions for a number of variables have either improved, deteriorated or stayed the same compared to the previous month.

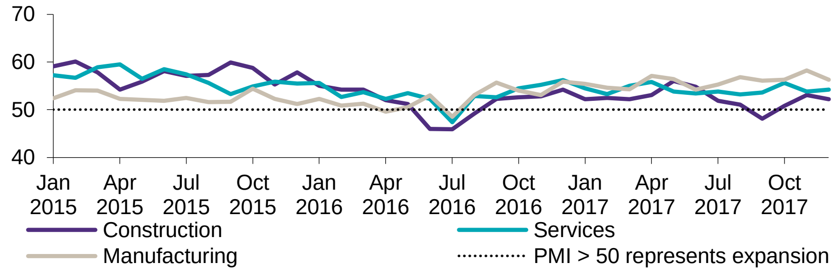
Service sector activity picked up in December. The index registered 54.2 in December, up from 53.8 in the previous month. Higher levels of business activity have now been recorded for 17 months running, which is supported by a more positive economic environment and rising consumer spending. Respondents highlighted rising operating expenses reflecting higher transport costs, staff salaries and utility costs in December. Business optimism is at a seven-month high with 43% of respondents expecting a rise in business activity in 2018, albeit low compared to the long-run survey average.

Construction output growth eased slightly in December. The index decreased slightly to 52.2 in December, down from 53.1 in the previous month. This was the third consecutive month where the index recorded a response above 50. Respondents reported an uneven recovery in business activity towards the end of 2017 with a rise in residential building and a fall in the number of commercial projects and stagnating civil engineering output.

Manufacturing growth remained solid at the end of 2017. The index posted 56.3 in December, slightly down from the 58.2 recorded in November, which was the highest level since August 2013. As a result, new orders and employment slowed in December from November's high, though all remained solid compared to long-run trends. Respondents maintained a positive outlook in December with nearly 54% reporting that they expect production to rise in 2018. For more information see the latest IHS Markit PMI releases.

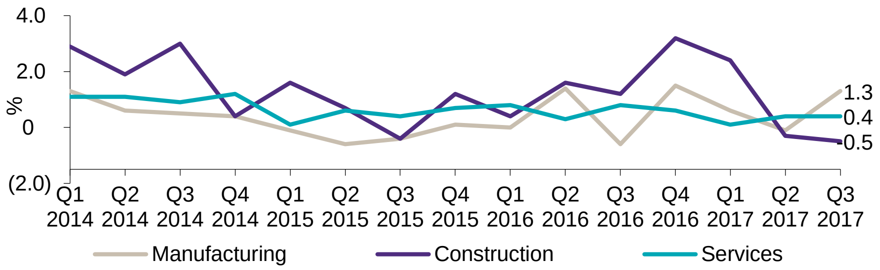
The second chart illustrates quarterly GDP growth across the three industries. Manufacturing activity increased by 1.3% in Quarter 3 2017, while Services increased by 0.4% and Construction fell by 0.5%.

Purchasing Managers' Index



Source: Markit /CIPS

GDP Growth Q-Q %



Source: ONS

Business impact

Business confidence directly impacts on business investment decisions. Continued levels of uncertainty over both the longer term with Brexit may limit levels of business investment and delay any major new investment from Government.

There are hopes that the weaker pound will boost demand for British goods in the near future. Conversely, the depreciation of the pound could lead to input price inflation for those who import. This was a factor raised by service sector respondents to the PMI who stated the depreciation against the euro would likely drive up costs in the near-term.

Regional outlook

The ICAEW Business Confidence Monitor is conducted every quarter, and gathers opinions on past performance and future perspectives for members' businesses, as well as investigating perceived changes in impact of factors such as availability of skills, government regulation and the tax regime.

In Q4 of 2017, business confidence was positive in just three regions – Wales, the South West and the East of England. For Wales and the East of England this is associated with improved performance in sales growth over the past year.

Despite none of the other regions showing positive confidence, none were strongly pessimistic. London was the most pessimistic, perhaps due to concerns about the potential impact that leaving the European Union may have on the capital's important banking sector. London and Scotland also had the highest proportion of firms reporting that regulation is a growing problem (54%); an issue generally felt most acutely in the Banking, Finance and Insurance sectors.

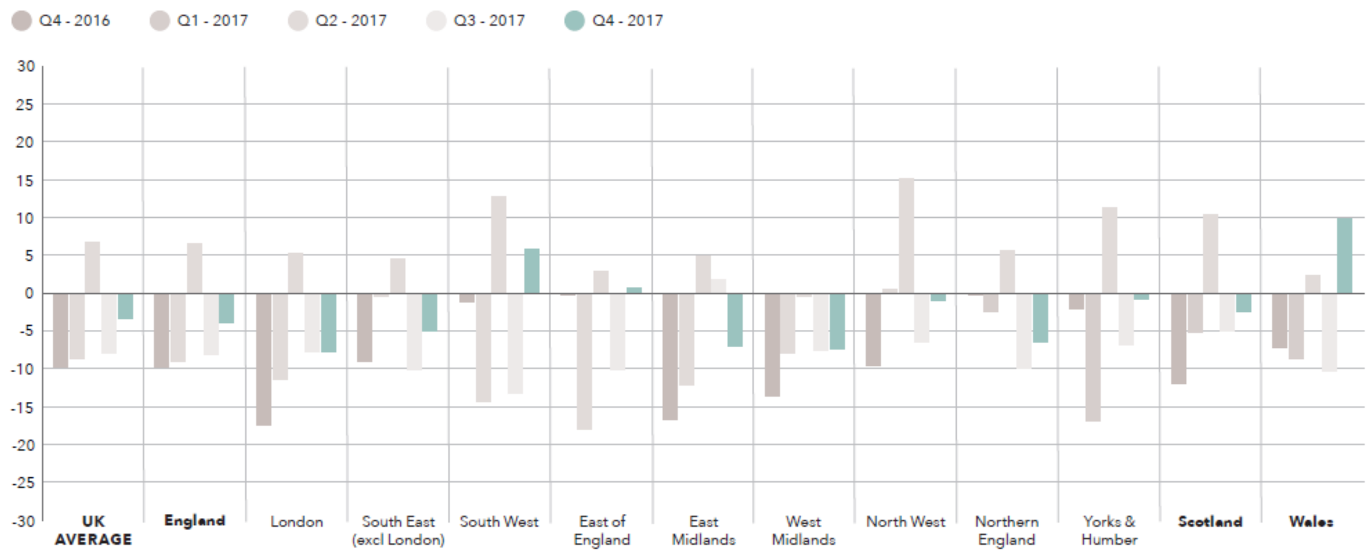
Two of England's manufacturing intensive regions – the East and West Midlands – have shown no improvement since the last quarter. The two regions also had the highest proportion of firms operating below capacity (64%).

For more information see the full ICAEW UK Business Confidence Monitor Report.

Business impact

In the context of government negotiations on the UK's exit from the European Union the ICAEW stresses the need for businesses to focus on maintaining their positioning and competitiveness in a growing global marketplace.

They also state that businesses are currently emphasising their focus on short term cost savings to deliver profit with the hope of increasing profit margins over the next 12 months.



Indicator glossary

Measure	What is it?	Why is it interesting?
Index of Services	Short-term indicator of services sector performance	Understand which service sectors are growing and what rates
Balance of Payments	Estimates about UK's trade, income and investment flows with the rest of the world	Trends in trade and also inbound and outbound overseas investment
Productivity	Output per hour, important for our economic performance in the long run	Productivity can be influenced by the structure of the labour market, investment and infrastructure, and the economic environment
UK Trade	Size of the import/export trade deficit on goods and services	Signs of change in the balance of exports compared with imports. The sharp depreciation in sterling post-referendum could be a key influence by making our exports cheaper and imports more expensive
Business Investment	Gross fixed capital formation and business investment	Look for change reflecting businesses' assessment of the economic and their financial situations post referendum
Index of Production	Early indicator of growth in the output industry	Manufacturing is dependent upon both upon domestic and overseas demand - changes will how UK trade is faring in the post referendum world
Retail Sales	Value and volume of retail sales	Indicates consumer confidence, prices and the overall financial position of households
Construction Output	Summarises ongoing and new construction work	Indicator of how confident enterprises and government are in investing in buildings and infrastructure, as longer term assets.
Inflation	Movements in prices of consumer goods and services	Reflects the degree of strength of domestic demand, domestic supply and changes in the UK prices of imports
Producer Prices Index	Factory gate prices and input costs	Changes could be due to changes in labour and energy cost; sterling depreciation could cause imported inputs to be more expensive
House Price Index	Change in house prices	An indicator of household's confidence in their financial situation
Labour Market Statistics	Employment, unemployment and average weekly earnings	Labour market trends will reflect changes to the overall economy
Public Sector Finances	Public sector net borrowing and tax revenues	Indications of the level of activity in the economy, changes in fiscal and BoE policy

Business impact

This table sets out the economic measures and data that are assessed in the economic briefing. This includes a brief explanation of what the measure is and why it is important to the health of the economy.

If you would like any further measures to be assessed in the next economic briefing, please get in contact with the one of the Insight & Analytics contacts on the following page.

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