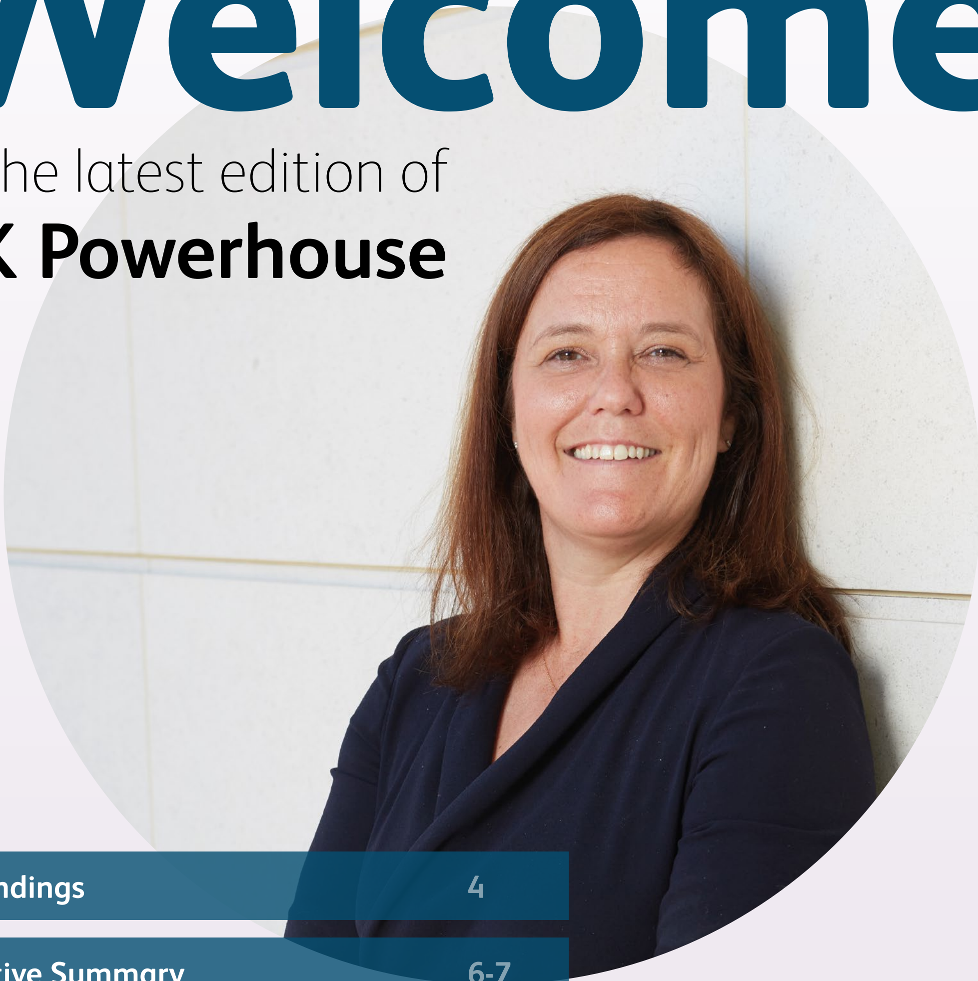
UK POWERHOUSE

Brexit Ready

February 2019

Welcome

to the latest edition of
UK Powerhouse



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I must say, it's quite a challenge writing an introduction to a report on Brexit, particularly at a point when there's still so much uncertainty about the specific terms of our departure.

When I write the foreword for our next UK Powerhouse report which comes out in April, I sincerely hope there'll be more clarity on what the future holds. This is Brexit, though, and it's hard to predict too much!

Having said this, at Irwin Mitchell we're determined to help our clients. This report is just one of the ways we're helping you prepare for the UK's departure from the EU.

This latest report builds on the economic forecasts in the previous study published last November. With the help of Cebr, it examines what the long-term economic future might look like over the next 15 years, based on three different Brexit scenarios.

There's also a shorter-term forecast on pages 14-21, which looks at how the 46 locations in our study are expected to perform in the third quarter of 2019 once we've officially left the EU.

In addition to this report, we'll continue to issue timely legal advice on important issues relevant to your business. I hope that these have been useful so far – please look out for future updates.

I also hope that you find this study interesting, and if you have any questions or require support about Brexit, please do get in touch with one of our experts. This insight will be incorporated into future reports and will also be available on our website.

Regards,

Vicky

Key Findings

Downside scenario

What will happen if no-deal is reached between the UK and EU, meaning that after the UK's withdrawal from the EU there would be no transition period guiding the parties to a new trading arrangement.

Central scenario

Based on a deal roughly in line with the Withdrawal Agreement. This would include outlines for a transition period, after which the UK and the EU would be "separate markets and distinct legal orders" following Brexit.

Upside scenario

Assumes that the UK and EU can agree on sufficient points to form a type of customs union that emulates the current trading arrangement, allowing some form of free trade with ease across borders.

In the downside scenario, GDP and business investment growth are both set to see sharp declines in the short term. At their lowest points, we expect GDP to contract 0.2 %, while real business investment falls by 8.4 % as firms move their business overseas.

The contraction of GDP in a downside scenario is driven by delays at borders and lengthier customs processes that will increase costs for business. As a result, businesses will reduce their output in the short-term.

After 2019, unemployment initially increases in all three scenarios. Even at its highest in the downside scenario, unemployment remains 1.8 % below its peak during the financial crisis.

Our indicators, which include GDP, population, consumer spending and unemployment, show a central scenario to be most stable, as the transition period gives time to pursue an orderly Brexit.

In a central scenario, business investment growth increases from -2.5 % in 2019 to 1.6 % in 2022, and remains steady from there.

The pound will perform strongly against the Euro and Dollar in an upside scenario as confidence in the economy increases. This sees the pound rise to between $1.48 and $1.53 between 2020 and 2034.

Executive summary

Irwin Mitchell's
Powerhouse Tracker

Official economic data sources for the UK's cities are often dated and fail to provide a reliable snapshot of the UK's localised economies – the last set of regional economic accounts corresponds to the economy in 2017. To more accurately estimate current economic activity, Cebr has utilised a range of more timely indicators to create a 'nowcast' of GVA and employment for a range of key cities across the UK. The latest outputs of this give us a picture of how the regional economies of the UK performed in Q3 2018. In this City Tracker report, we also develop a city forecast to Q3 2019, and provide forecasts and commentary on three Brexit scenarios.

Key Facts

- The UK economy grew by 0.6 % between Q2 2018 and Q3 2018 – the fastest quarterly growth since Q4 2016. One of the key drivers of this was increased household consumption.
- Cambridge, Reading, Oxford, Milton Keynes and Ipswich continue to feature as some of the fastest growing cities in the UK.
- No city sees growth of more than 2.3 % – well below the highest growth rates seen in previous quarters.
- The unemployment rate was 4.1 % on average across the UK Powerhouse cities in Q3. This was down by 147,000 year-on-year.
- London is set to see a rise in the Powerhouse tables for employment growth as it shows its resilience to Brexit. Outer London boroughs in particular are expected to perform well.
- A decline in car sales resulted in lower spending on transport but household consumption grew by 0.5 % over the quarter, with people spending more on various goods and services.
- Business investment decreased by 1.1 % from Q2 2018 to Q3 2018 – the third quarter-on-quarter fall in business investment.

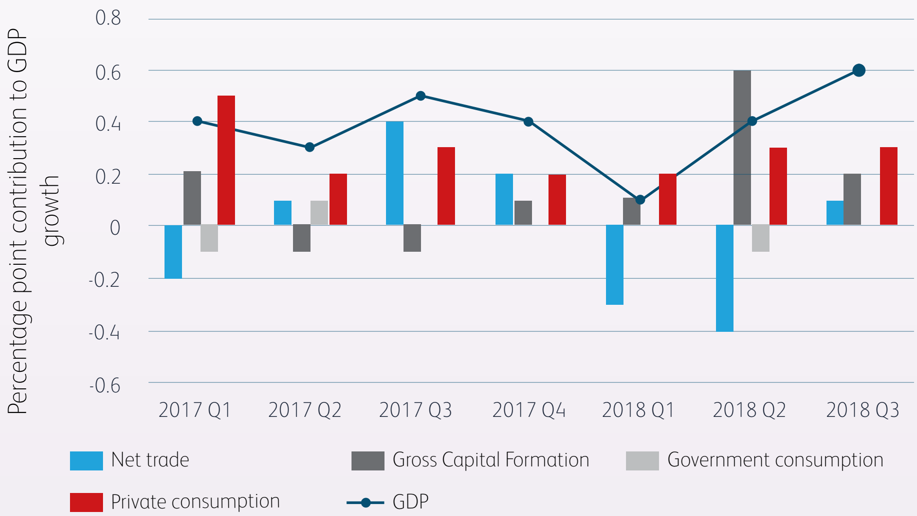
UK economy:

GDP growth continued to accelerate in Q3 but has slowed in Q4

Between Q2 2018 and Q3 2018, the UK economy expanded by 0.6 %, the fastest pace of quarterly growth since Q4 2016. Gross capital formation, net trade and private household consumption all provided positive contributions, with the latter offering the biggest boost. Private household consumption grew by 0.5 % in Q3, resulting in a 0.3 percentage point contribution to the headline GDP figure. One of the main drivers behind household spending was miscellaneous goods and services, particularly financial services. Meanwhile, one of the biggest downward pressures on private spending growth was a drop in household spending on transport, with fewer people buying cars.

In the months after Q3, the UK economy has slowed, with the three-monthly GDP growth rate falling to 0.3 % in November. Therefore, while the strong Q3 growth rate offers positive news for those concerned by Brexit uncertainty causing weakness in the economy, looking at the two quarters immediately before the March Brexit deadline, we can expect a slowdown in economic growth from the Q3 figures.

Figure 1 - GDP percentage growth (right-hand side); UK expenditure components percentage contribution to GDP growth (left-hand side), quarter-on-quarter



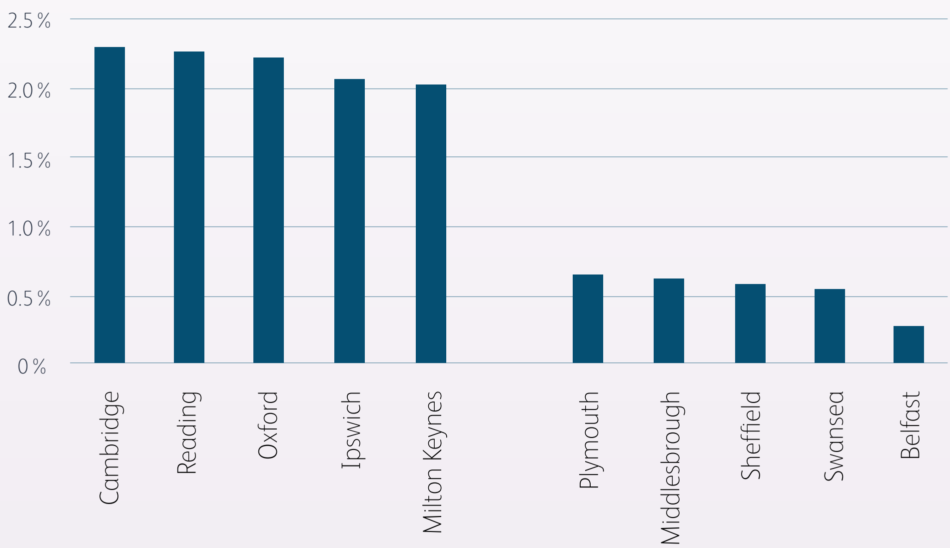
Source: Office for National Statistics, Cebr analysis

Turning to the labour market, in Q3 2018, the unemployment rate stood at 4.1 % in the three months to September, 0.1 percentage points higher than the previous quarter. The employment rate was 75.5 %, which is 0.5 percentage points higher than the rate for the same period last year, but unchanged from Q2 2018. The number of economically inactive people (those not working and not seeking work) stood at 8.74 million, largely unchanged from Q2 but down by 147,000 year-on-year. Earnings, excluding bonuses, increased by 3.2 % year-on-year – 0.5 percentage points higher than for the previous quarter – marking the highest rate of growth in regular pay since the final quarter of 2008.

GVA Growth

In Q3 2018, annual growth for the UK was 1.5 %, down from 2.0 % in Q3 2017. This slowdown across the country is reflected in a slowing of growth across many of the Powerhouse cities. While Cambridge, Reading, Oxford, Milton Keynes and Ipswich continue to feature as some of the fastest growing cities in the UK, no city sees growth faster than 2.3 %. This is well below the top growth rates observed in previous quarters.

Figure 2 - Top and bottom five cities by annual GVA growth, Q3 2018



Source: *Office for National Statistics, Cebr analysis*

Exeter was the fastest growing Powerhouse city in the South West in Q3 2018, with 1.4 % GVA growth, meaning the city ranks 13th on the Powerhouse table. This growth is expected to accelerate to 1.6 % in Q3 2019. Among the factors which make up Exeter's robust growth is the city's resilient high street. With a shop vacancy rate of just 8 % [1], Exeter has one of the lowest rates in the country – by contrast, some of the worst performing high streets, such as those in Hull and Southend, saw rates over 17 %. Exeter has a young working-age population, with the third highest share of the population aged 18-29 out of any UK city, at 28 %. This fuels economic activity in many areas of the city's economy, including the high street, but also leisure and service providers.

[1] https://www.centreforcities.org/blog/myth-1-all-high-streets-are-struggling/

Another high performing city is Norwich. While this city is somewhat overshadowed by its neighbours Cambridge and Ipswich in terms of GVA growth rates, it's still the seventh fastest growing Powerhouse city, with a growth rate of 1.8 % in Q3 2018. Despite growth being forecast to slow slightly to 1.7 % by Q3 2019, it's still expected to easily sit inside the top 10 fastest growing Powerhouse cities. Norwich has one of the highest shares of private knowledge intensive business services in the country, at 16 % in 2016 which provides a significant boost to GDP. Along with its neighbours in the East of England, Norwich is home to several organisations in the life science sector, which is a significant source of growth within the region.

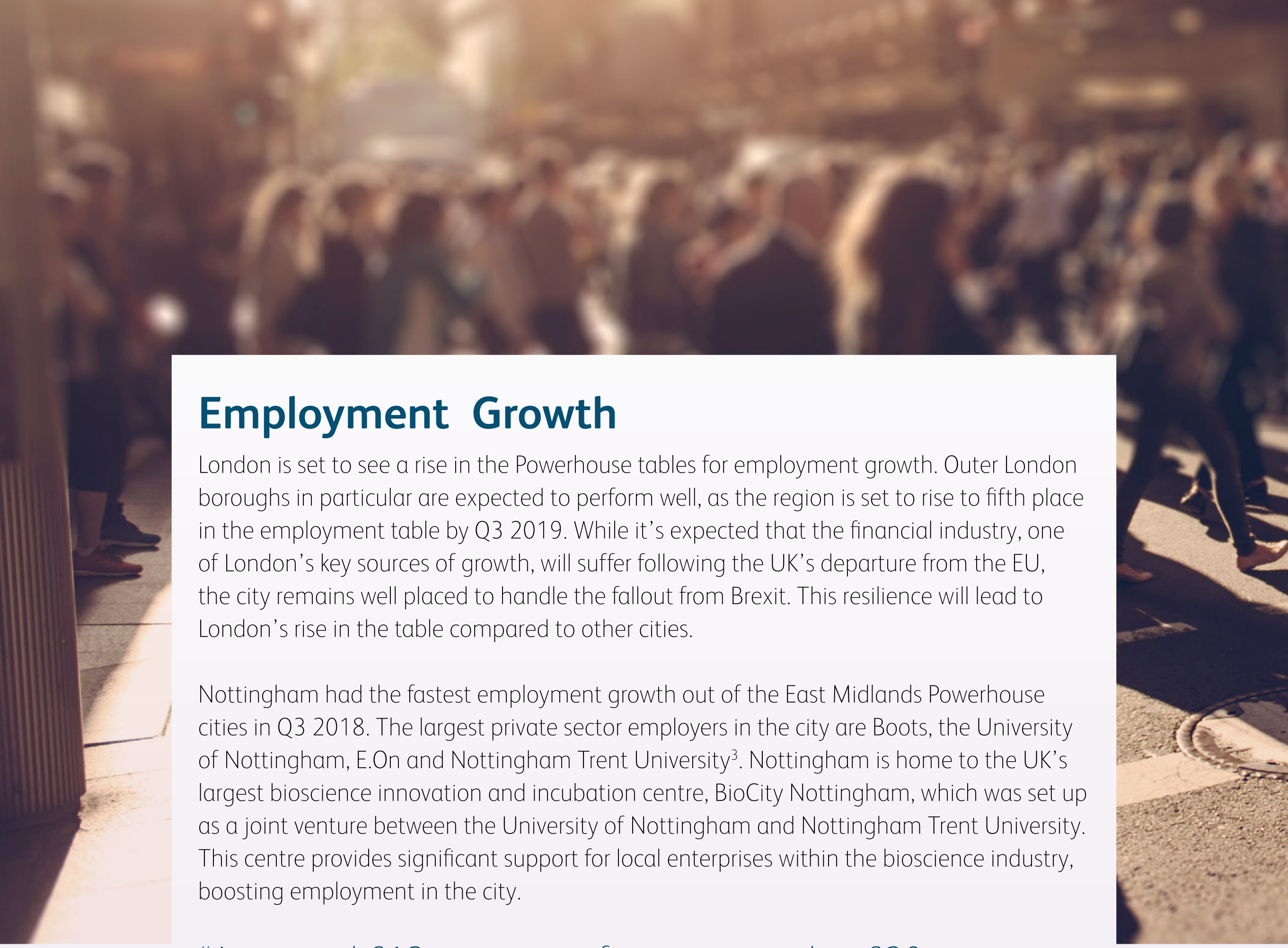
Portsmouth outperforms its south-coast neighbours Brighton and Southampton in terms of GVA growth in Q3 2018. By Q3 2019, however, Southampton is set to overtake. Portsmouth's economy is dependent on the defence and maritime sectors, with the Portsmouth Naval Base being one of the city's biggest employers. The University of Portsmouth also provides a boost to local enterprises and supports the city's growth. Similarly, Southampton benefits from the maritime sector, being home to one of the UK's biggest ports by value. Furthermore, Southampton is home to several thriving businesses including Garmin and P&O, while the city's hotels enjoy success from the large number of cruise ship passengers which pass through the city.

"Rotherham continues to see the fastest growth out of the Powerhouse cities in Yorkshire and the Humber"

Rotherham continues to see the fastest growth out of the Powerhouse cities in Yorkshire and the Humber, with 1.4 % annual growth estimated for Q3 2018, and 1.5 % forecast for Q3 2019. Several businesses have been investing in the area. Builders merchants James Burrell is set to open a £2 million new branch in the city[2] in spring 2019, while construction has begun on the £38 million Gulliver's Valley leisure development.

Manchester is the fastest growing Powerhouse city in the North West. While the North West economy as a whole has suffered from weakening of car sales and the manufacturing sector as a whole in 2018, Manchester is home to many businesses in the life science, healthcare, creative, digital and technology sectors, which continue to perform well. Established companies such as AO.com and Boohoo.com contribute to the city's success, while many new start-ups are also stimulating economic activity, with many businesses showing strengths in software development, IoT (internet of things), data analytics and IT services.

[2] https://www.jamesburrell.com/news/breaking-news-were-expanding-next-stop-rotherham



Employment Growth

London is set to see a rise in the Powerhouse tables for employment growth. Outer London boroughs in particular are expected to perform well, as the region is set to rise to fifth place in the employment table by Q3 2019. While it's expected that the financial industry, one of London's key sources of growth, will suffer following the UK's departure from the EU, the city remains well placed to handle the fallout from Brexit. This resilience will lead to London's rise in the table compared to other cities.

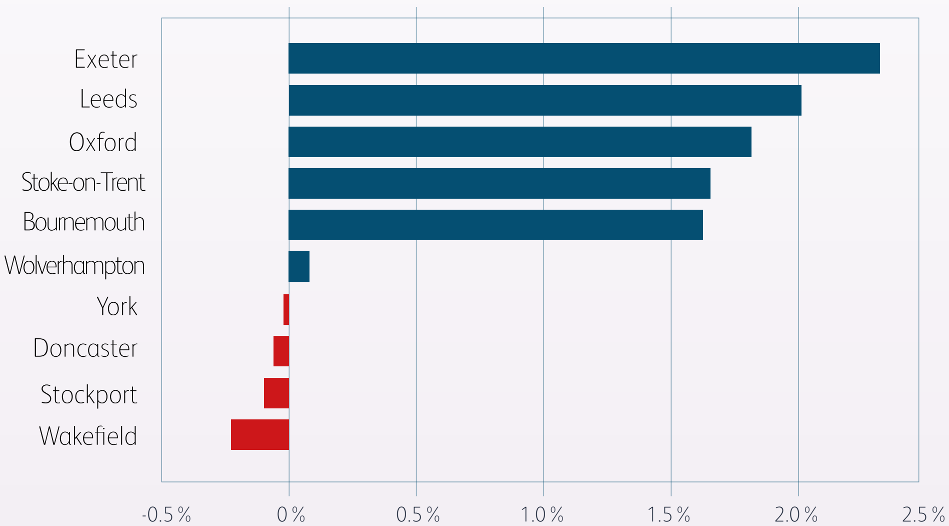
Nottingham had the fastest employment growth out of the East Midlands Powerhouse cities in Q3 2018. The largest private sector employers in the city are Boots, the University of Nottingham, E.On and Nottingham Trent University[3]. Nottingham is home to the UK's largest bioscience innovation and incubation centre, BioCity Nottingham, which was set up as a joint venture between the University of Nottingham and Nottingham Trent University. This centre provides significant support for local enterprises within the bioscience industry, boosting employment in the city.

> "At around £13 per square foot compared to £20 in Nottingham or £33 in Birmingham, Stoke is an attractive alternative location for many new businesses"

Stoke-on-Trent also performed well in terms of employment growth in Q3 2018, which is set to continue going into 2019. A major advantage the city holds is the availability of affordable office space. At around £13 per square foot compared to £20 in Nottingham or £33 in Birmingham, Stoke is an attractive alternative location for many new businesses looking to keep costs down.

[3] https://www.nottinghampost.com/news/business/biggest-20-employers-in-nottinghamshire-1992710

Figure 3 - Five fastest and slowest expanding cities by year-on-year employment growth in Q3 2018



Source: Office for National Statistics, Cebr analysis

Outside of London, Birmingham is the largest city economy in the UK, and is set to experience the sixth fastest employment growth out of the Powerhouse cities by Q3 2019. Birmingham is currently the subject of significant infrastructure investment, with the construction of HS2 and the Commonwealth Games in 2022. These developments have already begun to attract businesses to the area, with HSBC recently relocating the headquarters of their business bank to the city.

UK Cities in Q3 2018
Powerhouse Table

GVA

League table ranking		GVA Q3 2018, £millions (Annualised, constant 2013 prices)	Growth (YoY)
1	**Cambridge**	**8,900**	**2.3%**
2	**Reading**	**6,400**	**2.3%**
3	**Oxford**	**8,400**	**2.2%**
4	**Ipswich**	**4,400**	**2.1%**
5	**Milton Keynes**	**11,400**	**2.0%**
6	**Outer London**	**122,000**	**1.9%**
7	**Norwich**	**2,600**	**1.8%**
8	**London**	**388,400**	**1.6%**
9	**Peterborough**	**5,300**	**1.6%**
10	**Portsmouth**	**5,300**	**1.6%**
11	Inner London	266,500	1.5%
12	Brighton	7,200	1.5%
13	Exeter	4,700	1.4%
14	Southampton	6,000	1.4%
15	Rotherham	4,400	1.4%
16	Manchester	17,800	1.4%
17	Aberdeen	12,200	1.3%
18	Greater Manchester	60,200	1.3%
19	Hull	5,100	1.3%
20	Doncaster	5,000	1.3%

21	Nottingham	8,900	1.3 %
22	Wakefield	6,800	1.3 %
23	Birmingham	25,800	1.3 %
24	Bournemouth	4,600	1.2 %
25	Bristol	13,400	1.2 %
26	Newcastle	9,400	1.2 %
27	Leeds	21,500	1.2 %
28	Glasgow	17,700	1.2 %
29	Derby	6,600	1.2 %
30	Stoke-on-Trent	4,900	1.2 %
31	Sunderland	5,700	1.1 %
32	Coventry	8,100	1.1 %
33	Stockport	6,500	1.1 %
34	Swindon	6,600	1.0 %
35	Liverpool	10,500	1.0 %
36	Leicester	7,100	1.0 %
37	York	4,800	1.0 %
38	Edinburgh	21,300	0.9 %
39	Wolverhampton	4,500	0.9 %
40	Cardiff	10,100	0.8 %
41	Bradford	9,300	0.8 %
42	Plymouth	5,000	0.7 %
43	Middlesbrough	3,200	0.6 %
44	Sheffield	11,300	0.6 %
45	Swansea	4,400	0.6 %
46	Belfast	15,300	0.3 %

UK Cities in Q3 2018
Powerhouse Table

Employment

League table ranking		Employment Level, Q3 2018	Growth (YoY)
1	**Exeter**	**113,400**	**2.3%**
2	**Leeds**	**469,300**	**2.0%**
3	**Oxford**	**138,100**	**1.8%**
4	**Stoke-on-Trent**	**114,100**	**1.7%**
5	**Bournemouth**	**94,600**	**1.6%**
6	**Birmingham**	**581,000**	**1.6%**
7	**Cambridge**	**136,300**	**1.6%**
8	**Outer London**	**1,831,100**	**1.5%**
9	**Manchester**	**467,900**	**1.5%**
10	**Liverpool**	**312,700**	**1.4%**
11	London	5,154,100	1.4%
12	Sheffield	295,200	1.4%
13	Newcastle	224,300	1.3%
14	Southampton	163,000	1.3%
15	Brighton	159,800	1.3%
16	Inner London	3,323,000	1.3%
17	Reading	126,400	1.3%
18	Glasgow	437,500	1.2%
19	Portsmouth	127,700	1.2%
20	Peterborough	114,800	1.2%

21	Swindon	119,500	1.1 %
22	Middlesbrough	80,700	1.1 %
23	Rotherham	106,000	1.1 %
24	Greater Manchester	1,295,800	1.1 %
25	Milton Keynes	159,400	1.0 %
26	Belfast	134,400	1.0 %
27	Bradford	222,500	1.0 %
28	Nottingham	215,200	0.9 %
29	Plymouth	147,600	0.9 %
30	Hull	149,400	0.9 %
31	Bristol	337,300	0.9 %
32	Cardiff	223,500	0.8 %
33	Leicester	214,600	0.8 %
34	Edinburgh	358,200	0.8 %
35	Coventry	189,400	0.7 %
36	Aberdeen	181,000	0.6 %
37	Norwich	134,300	0.6 %
38	Sunderland	135,300	0.5 %
39	Ipswich	79,000	0.5 %
40	Derby	134,900	0.4 %
41	Swansea	114,200	0.3 %
42	Wolverhampton	116,700	0.1 %
43	York	109,800	0.0 %
44	Doncaster	125,200	-0.1 %
45	Stockport	117,700	-0.1 %
46	Wakefield	143,200	-0.2 %

UK Cities in Q3 2019
Powerhouse Table

GVA

League table ranking		GVA Q3 2019, £millions (Annualised, constant 2013 prices)	Growth (YoY)
1	**Milton Keynes**	**11,700**	**2.4%**
2	**Reading**	**6,600**	**2.3%**
3	**Cambridge**	**9,100**	**2.2%**
4	**Oxford**	**8,600**	**2.0%**
5	**Ipswich**	**4,500**	**1.9%**
6	**Peterborough**	**5,400**	**1.9%**
7	**Southampton**	**6,100**	**1.7%**
8	**Norwich**	**2,700**	**1.7%**
9	**Portsmouth**	**5,400**	**1.6%**
10	**Exeter**	**4,700**	**1.6%**
11	Wakefield	6,900	1.6%
12	Outer London	123,900	1.6%
13	Doncaster	5,100	1.5%
14	York	4,900	1.5%
15	Nottingham	9,100	1.5%
16	Brighton	7,300	1.5%
17	Rotherham	4,500	1.5%
18	Manchester	18,000	1.4%
19	Aberdeen	12,400	1.4%
20	London	394,000	1.4%

21	Swindon	6,600	1.4%
22	Birmingham	26,200	1.4%
23	Stockport	6,500	1.4%
24	Inner London	270,100	1.4%
25	Bournemouth	4,700	1.4%
26	Greater Manchester	61,000	1.3%
27	Coventry	8,200	1.3%
28	Stoke-on-Trent	5,000	1.3%
29	Glasgow	17,900	1.3%
30	Bristol	13,600	1.2%
31	Hull	5,100	1.2%
32	Leicester	7,200	1.2%
33	Sunderland	5,800	1.2%
34	Leeds	21,700	1.2%
35	Newcastle	9,500	1.2%
36	Liverpool	10,600	1.1%
37	Derby	6,600	1.0%
38	Bradford	9,400	1.0%
39	Sheffield	11,400	1.0%
40	Edinburgh	21,500	1.0%
41	Wolverhampton	4,600	1.0%
42	Cardiff	10,200	0.9%
43	Middlesbrough	3,200	0.8%
44	Plymouth	5,000	0.7%
45	Swansea	4,400	0.7%
46	Belfast	15,400	0.5%

UK Cities in Q3 2019
Powerhouse Table

Employment

League table ranking		Employment Level, Q3 2019	Growth (YoY)
1	**Exeter**	**116,000**	**2.3%**
2	**Leeds**	**478,700**	**2.0%**
3	**Oxford**	**140,500**	**1.7%**
4	**Stoke-on-Trent**	**116,000**	**1.6%**
5	**Outer London**	**1,860,300**	**1.6%**
6	**Birmingham**	**590,100**	**1.6%**
7	**Cambridge**	**138,400**	**1.5%**
8	**Manchester**	**475,000**	**1.5%**
9	**Southampton**	**165,400**	**1.5%**
10	**London**	**5,226,000**	**1.4%**
11	Liverpool	317,000	1.4%
12	Bournemouth	95,900	1.4%
13	Sheffield	299,200	1.4%
14	Newcastle	227,300	1.3%
15	Brighton	161,800	1.3%
16	Inner London	3,365,700	1.3%
17	Reading	128,000	1.3%
18	Milton Keynes	161,400	1.3%
19	Glasgow	442,900	1.2%
20	Portsmouth	129,200	1.2%

21	Swindon	120,900	1.1%
22	Peterborough	116,100	1.1%
23	Rotherham	107,200	1.1%
24	Greater Manchester	1,309,800	1.1%
25	Middlesbrough	81,600	1.1%
26	Plymouth	149,100	1.0%
27	Bradford	224,600	1.0%
28	Hull	150,700	0.9%
29	Cardiff	225,500	0.9%
30	Bristol	340,200	0.9%
31	Nottingham	217,000	0.9%
32	Leicester	216,400	0.9%
33	Edinburgh	361,000	0.8%
34	Coventry	190,700	0.7%
35	Belfast	135,300	0.7%
36	Aberdeen	182,100	0.6%
37	Sunderland	136,100	0.6%
38	Ipswich	79,400	0.5%
39	Norwich	135,000	0.5%
40	Swansea	114,600	0.4%
41	Derby	135,200	0.2%
42	Wolverhampton	116,800	0.1%
43	Doncaster	125,300	0.0%
44	Wakefield	143,100	-0.1%
45	Stockport	117,400	-0.2%
46	York	108,800	-0.8%

Economic impact of various Brexit outcomes

In November 2018, after almost two years of negotiations, UK Prime Minister Theresa May presented a 585-page Withdrawal Agreement to her cabinet. Despite several resignations, the deal was brought forward for a vote in Parliament, only to be postponed at the last minute due to the strong likelihood of its defeat – a fate it suffered just a few weeks later in the New Year.

The back-and-forth is illustrative of the hasty and unpredictable nature of the Brexit process so far. Brexit, or more appropriately the uncertainty surrounding it, has had a measurable impact on macro indicators in the UK. As business sentiment continues to fall, the Office for National Statistics estimates that business investment was down by 1.1 % to £46.9 billion between Q2 2018 and Q3 2018. This marks the third consecutive quarter-on-quarter fall in business investment, the first time this has happened since the economic downturn of 2008-2009.

"As business sentiment continues to fall, the Office for National Statistics estimates that business investment was down by 1.1 % to £46.9 billion between Q2 2018 and Q3 2018"

Turning to the consumer side of the economy, despite higher wages and falling inflation, consumers have been reluctant to spend. This is partially due to the need to pay off relatively high debt levels. The annual growth rate of consumer credit fell to 6.6 % in December 2018, down 0.6 percentage points from November. Another reason for subdued expenditure is the recent decline in consumer confidence. The YouGov/Cebr HEAT measure of consumer confidence hit a five-and-a-half year low in January.

All of these factors contributed to the slowdown in GDP growth in the three months to November 2018, the weakest rate since the three months to May.

As we approach the UK's formal departure date, the reality remains that there's still little certainty concerning what the future relationship with the EU will be. A number of scenarios remain possible. All of the possible outcomes stand to have a variety of impacts on the following macro measures:

- GDP
- Population
- Unemployment
- Consumer spending
- Business investment
- Exchange rates
- Bank of England rates

In this section, we explore the trajectory of these economic indicators under three distinct scenarios: downside, central and upside.

The three scenarios

Our downside scenario assumes that no deal is reached between the UK and EU, meaning that after the UK's withdrawal from the EU there would be no transition period guiding the parties to a new trading arrangement.

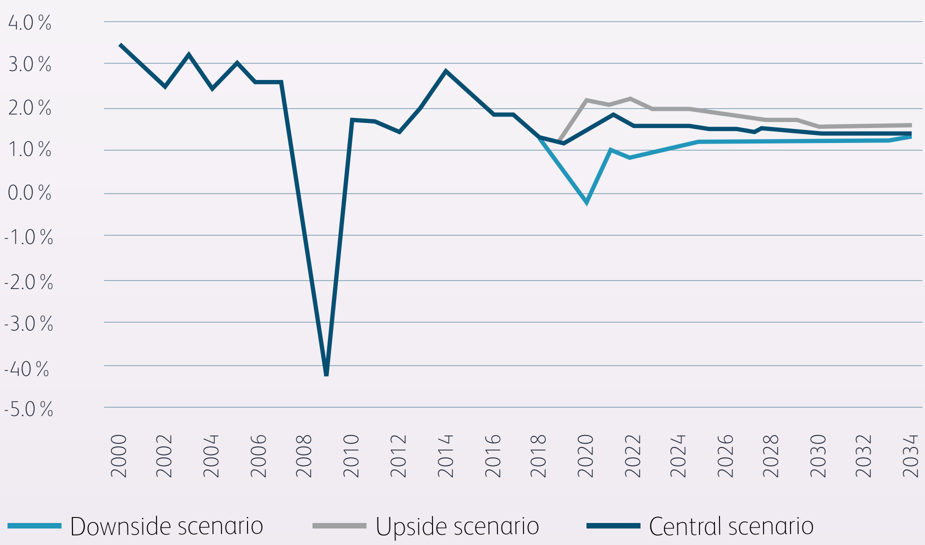
The central scenario is based on the assumption a deal is agreed that is roughly in line with the current Prime Minister's Withdrawal Agreement. This would include outlines for a transition period, after which the UK and the EU would be "separate markets and distinct legal orders" following Brexit.

The upside scenario assumes that the UK and EU can agree on sufficient points to form a type of customs union that emulates current trading arrangements. That is, the Withdrawal Agreement would be altered to allow some form of free trade that would permit, at the very least, the most important goods and services to be traded with ease across borders. In order to secure this, the UK would most likely need to accept free movement of labour, which the government has been very reluctant to compromise on. Any chance of implementing this arrangement would require negotiations over a lengthy interim period, perhaps following an extension to Article 50.

Downside Scenario

Trade stands to be severely disrupted under a no-deal Brexit. The boundary between the UK and the EU would become a customs border with immediate effect, with goods subject to increased checks and balances before being accepted on either side. This helps explain the immediate drop in GDP growth shown in Figure 4.

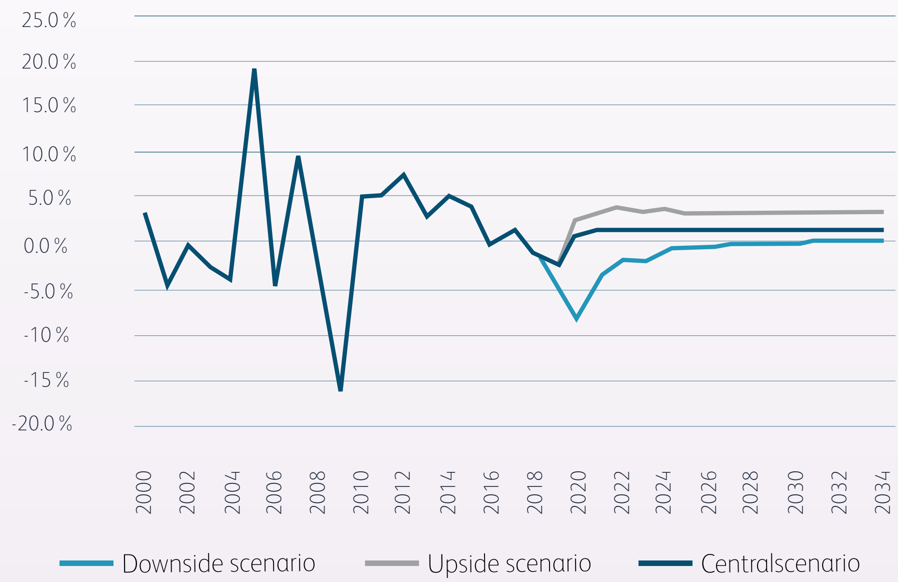
Figure 4 - GDP growth, percentage change



Source: *Cebr*

The sharp decline can be explained by a rise in delays, which in turn will increase costs for businesses. Faced with this, many firms are likely to make a choice to cut back on production and output in the short-term, as trade regulations are negotiated and settled.

Figure 5 - Real business investment, percentage change



Source: *Cebr*

This pattern is mirrored by the path of real business investment, which will initially decline as business confidence is dampened. Many international companies, will be adversely affected if the unrestricted access to the European single market is hindered – particularly those in the services sector who have chosen the UK as a 'gateway' to Europe. Some firms will be compelled to move their production sites overseas, if they have not started the process already. Real business investment is expected to contract by 8.4 % in 2020. As with GDP growth, however, from 2021 this measure is expected to recover in the long-term. This is as a result of the stability that will begin to materialise as businesses and consumers adapt their expectations in light of the new economic environment.

Weaker consumer spending will also hurt domestic firms and the services sector, with further repercussions for employment prospects in these industries. Latest figures show the unemployment rate was 4.0 % in the three months to November 2018, the lowest in decades. This would very likely be reversed in a no-deal scenario.

We anticipate that unemployment will pick up quickly as a result of the significant disruptions to existing trading relationships with the EU, and would peak at 6.6 % in 2028, 2.6 percentage points above the current level. However, the unemployment rate would still be 1.8 percentage points below its peak during the financial crisis[4], as the changing nature of employment encourages employees to work flexibly and take on part-time roles.

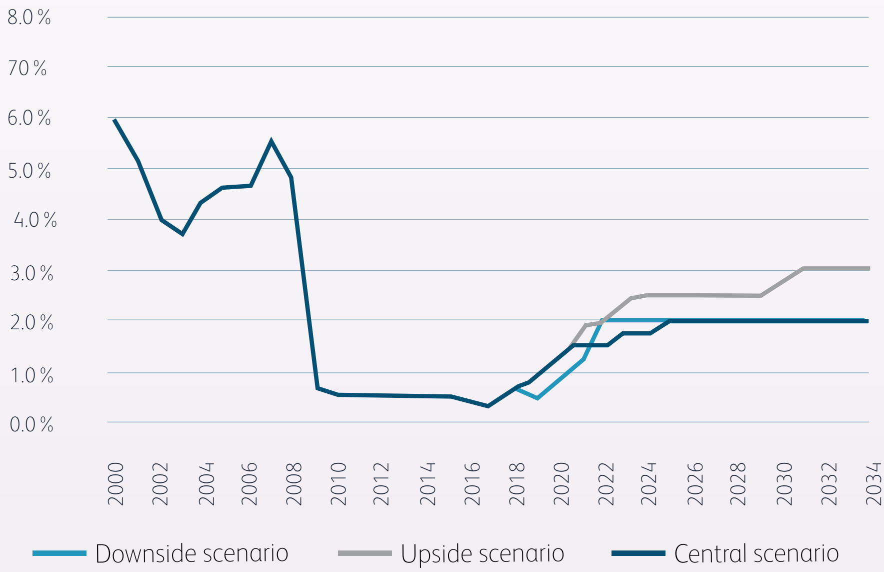
> “Unemployment will pick up quickly as a result of the significant disruptions to existing trading relationships with the EU”

After 2021, the unemployment rate begins to fall gradually to settle at 5.5 % in 2034. This is just 0.1 percentage point above the figure in the central scenario, and 0.7 percentage points above that in the upside scenario.

Under this scenario, real consumer spending growth falls sharply post-Brexit as confidence is severely damaged and inflationary pressures heighten. Not only will the higher trade frictions at the border drive up the cost of imports, but we forecast that the pound will weaken markedly against major currencies, worsening the foreign purchasing power of UK consumers.

[4] https://www.ons.gov.uk/economy/grossdomesticproductgdp/articles/the2008recession10yearson/2018-04-30

Figure 6 - Bank of England interest rate, %



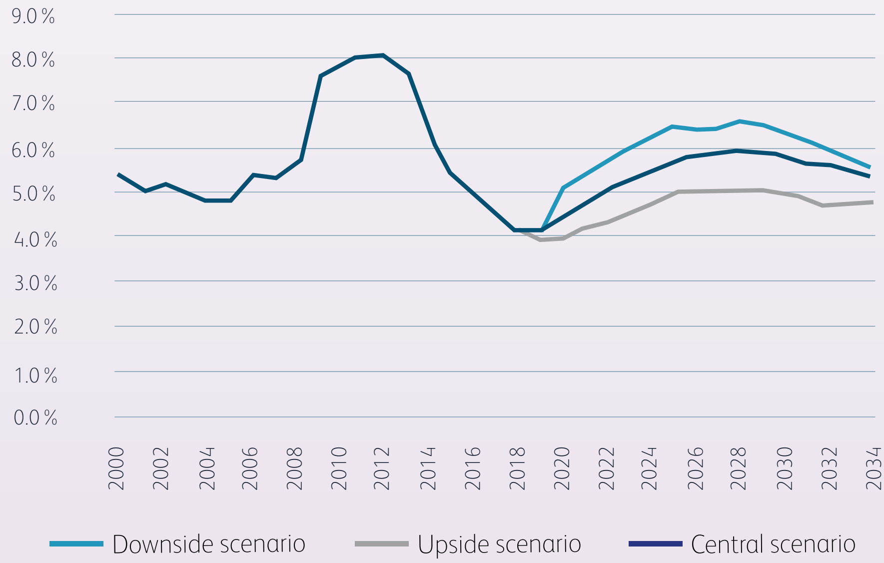
Source: *Cebr*

Perhaps most interesting in this case is the direction of the Bank of England's monetary policy. We anticipate that the Bank will initially cut rates in an attempt to boost GDP and consumer spending following a no-deal. The Monetary Policy Committee (MPC) will then need to quickly raise them in order to curb inflation from higher import prices. However, the interest rate ends its upward trajectory in 2022. From 2025, the interest rate in the downside and central scenarios move in tandem.

Central Scenario

Under the central scenario, we anticipate a more stable trajectory across most of the macro measures. GDP growth peaks at 1.8 % in 2021, before converging to 1.4 % in 2034. This is only 0.2 percentage points below the growth in our most optimistic scenario, and is supported by a steady path of business investment growth. As uncertainty lifts and growth rebounds to make up for lost opportunities, real business investment growth increases from -2.5 % in 2019 and stays steady at 1.6 % from 2022 onwards.

Figure 7 - Unemployment rate



Source: Cebr

Although inflation is currently at its lowest level in nearly two years, in the long-term, the Bank of England has remained committed to normalising monetary policy under an orderly Brexit. In this scenario, with a transition period that gives time to pursue an orderly Brexit, interest rate rises are still expected as the Bank works to keep inflation at its 2.0 % target.

The current low unemployment rate hides the prevalence of hard-to-fill vacancies in the economy. In autumn 2018, 70 % of employers with vacancies said that at least some of those were proving hard-to-fill compared to 51 % in spring 2017, according to the Chartered Institute of Personnel and Development (CIPD), the professional body for HR and people development.

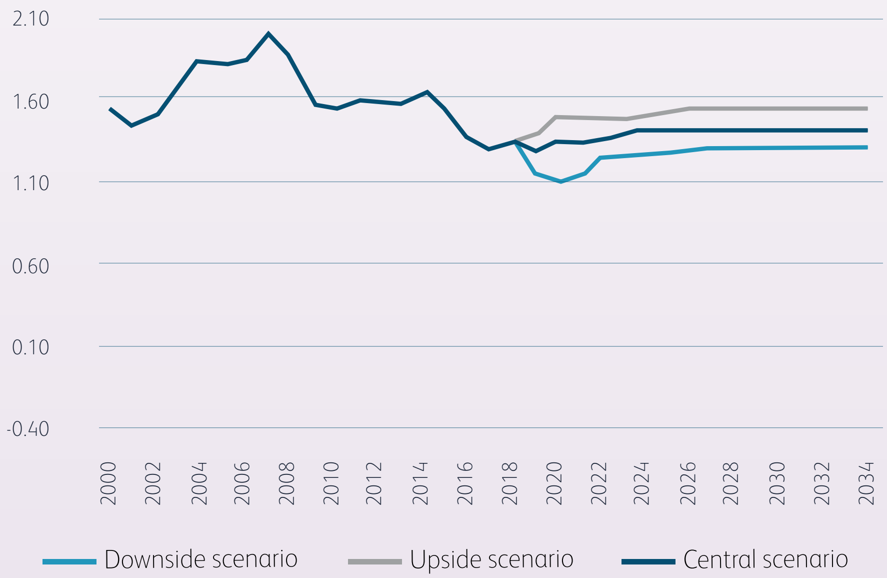
> "In autumn 2018, 70 % of employers with vacancies said that at least some of those were proving hard-to-fill compared to 51 % in spring 2017"

Increasing vacancies, coupled with low unemployment figures, suggests that on the supply side, there may be fewer workers with in-demand skills available. However, in the long-run, there is the opportunity for the labour force to obtain the right training and education required to meet the skills gap, allowing the unemployment rate to fall again after 2028.

Upside Scenario

In our upside scenario, the pound performs strongly against the dollar and euro, recovering the drop in value it experienced following the EU referendum. Between 2020 and 2034, the pound rises to between $1.48 and $1.53, as confidence in the UK economy boosts expectations and investors' demand for the currency.

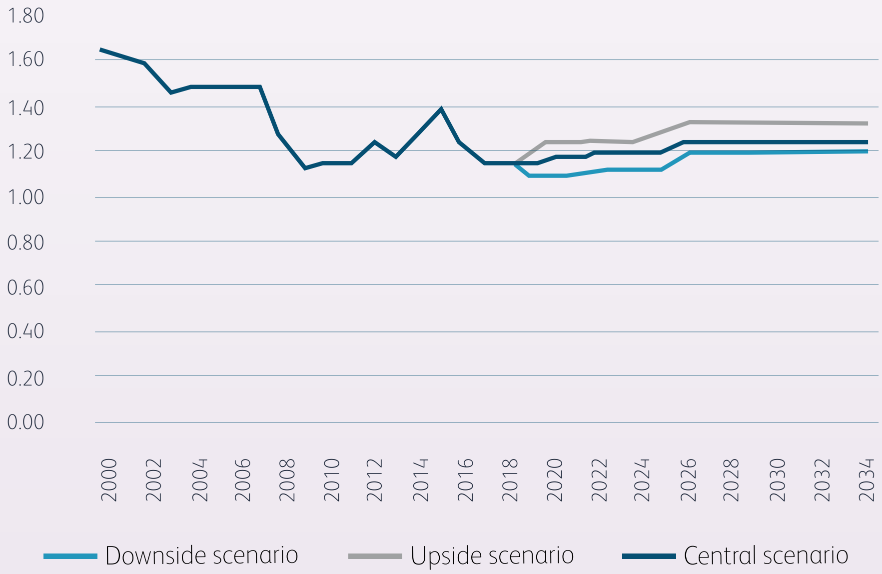
Figure 8 - $/£ exchange rate



Source: *Cebr*

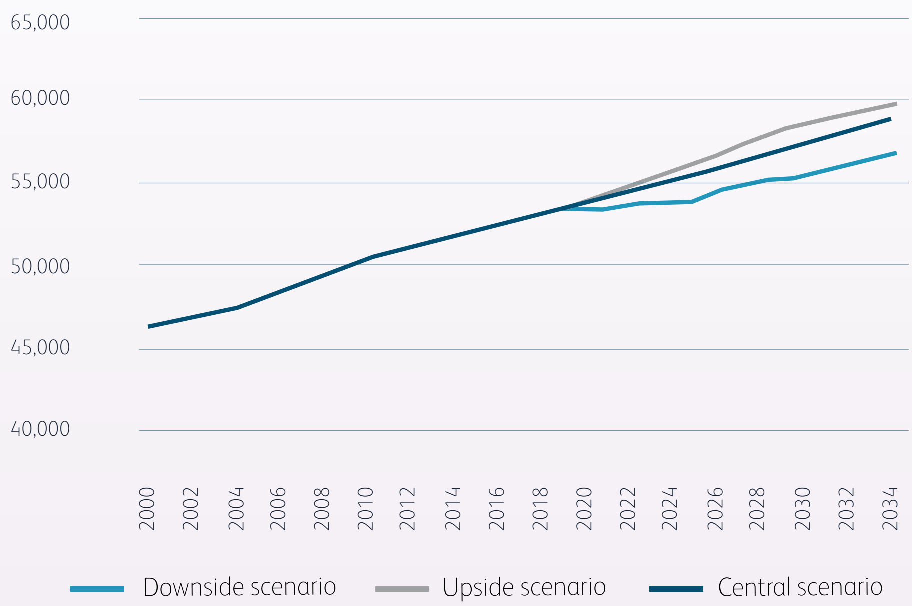
This outcome would be of particular benefit to international financiers, who rely on integrated markets and free trade to obtain higher returns on their investments.

Figure 9 - €/£ exchange rate



Source: *Cebr*

Figure 10 - UK adult population (16+), thousands

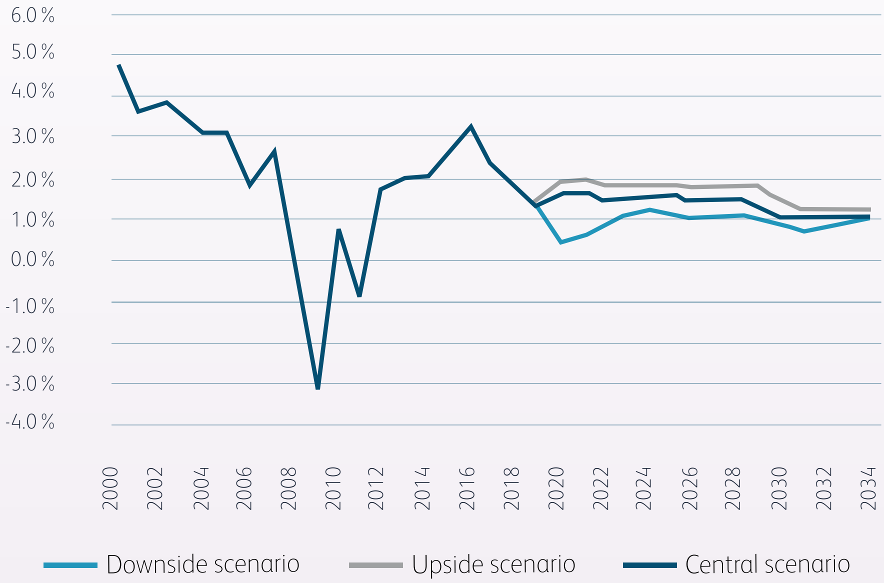


Source: *Cebr*

Turning to demographics, the UK adult population reaches its highest level in this scenario. Between 2019 and 2034, the adult population rises from 53.4 million to 59.9 million. This 12.2 % rise will likely fuel the growth in consumer spending as per Figure 11. However, the rise in real consumer spending growth does not continue indefinitely, with a projected fall in the percentage change of real consumer spending from 2029. This is in part due to its dependency on the Bank’s monetary policy.

When consumer spending increases, the MPC will adopt policy measures to counter the inflationary pressure. As such, the bank rate is likely to see a gradual increase, peaking at 3 % in 2031. The acceleration of interest rate rises between 2029 and 2032, corresponds to the decline in real spending growth as the Bank’s policy to cool inflationary pressures takes effect.

Figure 11- Real consumer spending, percentage change



Source: *Cebr*

Even in our most optimistic scenario, unemployment does begin to increase after 2019. This could arise as a result of some firms that reduce employment in the face of growing competition in foreign markets due to a strengthening pound. Also, the adoption of automation and technologies such as artificial intelligence, which is more likely to be supported by investment in the upside scenario, brings the promise of higher productivity, thereby reducing the need for staff at certain levels. However, the unemployment rate in the upside case is the lowest of all three scenarios. This is expected to reach a peak of 5.0 % , before falling to 4.8 % by 2034.

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A report for Irwin Mitchell

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The report does not necessarily reflect the views of Irwin Mitchell.

Methodological Note

Cebr's central forecasts are based on the assumption that the UK and the EU are able to form a compromise and sign a partial free trade agreement (FTA) covering at least the most important goods traded. It's unlikely that such an FTA can be agreed on in time, before the UK needs to leave the EU in 2019. We therefore assume that a transitional arrangement will be put in place that allows a continuation of the current relationship without any major disruptions until an FTA is agreed on around 2021. On the immigration policy, we rely on the lower immigration population estimates assuming that a visa system will be implemented for EU nationals, but that the requirements (e.g. the minimum salary, the NHS surcharge payment, the application fees etc.) would be more relaxed than they currently are for non-EU nationals requiring a visa.

As well as our central forecasts this report contained two additional forecasts for different scenarios. These are:

Upside scenario: A deal is agreed which is similar to the current PM's deal, but with added provisions on trade which emulate current trading arrangements.

Downside scenario: UK leaves EU with no deal and no transition period.

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