Date: 9th September 2016
Subject: Brexit implications for Greater Manchester and internationalisation
Report of: Sir Richard Leese

PURPOSE OF REPORT

This report updates members on work underway to understand the full implications of Brexit on Greater Manchester and develop an appropriate policy response.

RECOMMENDATIONS:

The GMCA/AGMA Scrutiny Pool are asked to:
- note the contents of this report and the GM Brexit Monitor and the matters which GM will want to consider as part of a policy response to Brexit; and
- indicate whether there are specific areas highlighted in the report on which the Pool requires further analysis and/or scrutiny.

CONTACT OFFICERS:

John Holden, Director of Research, New Economy
john.holden@neweconomymanchester.com

Simon Nokes, Managing Director, New Economy
simon.nokes@neweconomymanchester.com

Rebecca Heron, GM Strategy Coordinator
r.heron@agma.gov.uk
1. BACKGROUND AND INTRODUCTION

1.1 Following the result of the referendum on Britain’s membership of the European Union there is considerable uncertainty regarding both the process leading up to withdrawal and the impact that withdrawal will have on the UK economy.

1.2 The precise implications for access to markets and for labour movement and availability will depend on the terms of withdrawal that the British government is able to negotiate. It will be some time before the position becomes clear, particularly as the formal process for triggering withdrawal has not yet happened. Whilst the rapid appointment of a new Prime Minister and her government has meant that the process for the UK leaving the EU has started to be outlined, there is still considerable uncertainty around the detail of that process and the impact on the economy. Political uncertainty is compounded further by calls for a second Scottish independence referendum to protect Scotland’s position within the EU and a leadership contest in the Labour party.

1.3 The 2016 Autumn Statement is likely to be the point at which the new Government signals whether it will be promoting any changes in fiscal or economic management strategies, and whether it remains committed to re-balancing the national economy and to the Northern Powerhouse. Government has indicated that it is awaiting the publication of official forecasts in advance of the Autumn Statement before considering additional tax rises or spending cuts. The Autumn Statement is also likely to be the point when the first elements of the new national Industrial Strategy emerge.

1.4 Greater Manchester is determined to continue to drive strong growth in the economy as an internationally important city region. Although there are short term uncertainties, GM’s ambition to establish the city region as a financially self-sustaining city, sitting at the heart of the Northern Powerhouse with the size, the assets, the skilled population and political and economic influence to rival any global city remains unchanged. However GM must react to the challenges created by the uncertainty and potential economic consequences of Brexit.

1.5 To inform that response, at its July 2016 meeting the GMCA commissioned a comprehensive programme of work to consider the actions required in eight areas:
   - implications for access to European funding;
   - implications for changing rules, regulations and trading relations;
   - implications for key sectors;
   - implications for property investment;
   - implications for housing and planning;
   - implications for inclusion;
   - monitoring economic trends and developments; and
   - utilising GM’s relationships with key Central Government departments.

1.6 The purpose of this work programme is to identify:
   - the issues that Greater Manchester will be seeking the Government to address through the Autumn Statement; and
1.7 In addition to work being undertaken by GM and district officers, specialist third party support has been procured to support a detailed analysis of the likely impact of Brexit on Greater Manchester and the response required. The Resolution Foundation and Metro Dynamics have been commissioned, through Core Cities, to work with New Economy in providing analysis and advice on the role of the city regions, the implications for productivity and inclusive growth, a package of potential measures to support the economy, and potential changes to rules and regulations from Brexit negotiations. Leading economic experts at the Resolution Foundation, Volterra and Global Counsel will also be providing advice on GM-specific work.

1.8 This report provides members with a summary of the headline implications of Brexit for Greater Manchester and internationalisation and information detailing the latest intelligence on these issues.

2 IMPLICATIONS FOR GREATER MANCHESTER

2.1 The impact on city regions will depend in part on their economic make-up. Those UK cities reliant on the production of physical goods are likely to become less competitive if tariffs and quotas are imposed on goods for export into the EU, although the impact of such tariffs and quotas may be mitigated by a depreciation in Sterling. Restrictions on the free movement of people could have a negative impact on those cities with strengths in Research and Development and in Intellectual Property, as the ability to attract and retain highly trained talent is critical to success, although those cities that have already established global strengths in such sectors should remain strong. Restrictions on hiring EU citizens may also likely to have a negative impact on cities with a significant service sector, although the decision to leave the EU may improve the attractiveness of UK cities to some financial institutions as the UK would not be subject to certain EU legislation, such as Solvency II, which the sector has fought hard against which codifies and harmonises EU insurance regulations, primarily concerning the amount of capital that EU insurance companies must hold to reduce the risk of insolvency.

2.2 Brexit will also significantly affect the higher education sector, and as such will have a disproportionate impact on those cities with a strong university presence such as Greater Manchester. The decision to leave the EU will affect European students who study at UK universities and exercise significant spending power within the cities in which they live; it may affect the ability of UK universities to attract European researchers and students to contribute to universities’ research and development strengths, and it will affect the EU funding currently available to UK academic institutions and their ability to participate in international collaborations in the EU.

2.3 Whilst in the short-term there will be no change in the immigration status of current EU students, no change in the immigration or employment status for EU nationals currently employed by universities, no change to the fee status of EU students, and no change to existing EU-funded grants or collaborative
projects with other EU institutions it is impossible to predict the precise consequences of Brexit on the higher education sector until the terms of withdrawal become clear.

2.4 Whilst the medium and long-term impact of Britain’s withdrawal from the EU is difficult to assess at this stage, there are some immediate implications. It is clear that access to ERDF and ESF funding will end and that continued access to transnational funding will depend on the terms that Britain negotiates with Europe. There will be significant confusion and disruption amongst supported parties as a result of withdrawal at the mid-point of the current programme.

2.5 It is also clear that Britain’s decision to leave the European Union is already having a negative impact on investor and business confidence and we need to understand work is underway to analyse how this fall in confidence will affect behaviour in the short to medium term. Whilst the fall in sterling provides opportunities for some firms as UK exports become more competitive, initial intelligence indicates that firms and investors are delaying or cancelling plans to invest in capital or hire workers.

2.5 Government has a clear role to play in building economic stability and establishing a climate of confidence at both national and international level. Central to any strategy for creating a stable economic environment will be re-stating and reinforcing support for long-standing commitments that are of fundamental importance to the long-term success of the economy, including investment in critical infrastructure such as HS2 and the Northern Hub and investment to support globally-leading areas of excellence such as advanced materials and health research.

2.6 However, local leaders also have a critical role to play in building market confidence. In the weeks following the referendum result officers have been working on a programme of work to ensure that the GMCA is in a position to understand the likely impact of Brexit on Greater Manchester and in a position to take the action required to mitigate the worst impacts of withdrawal. That programme of work is being developed in conjunction with leading external economic experts, and in consultation with the GM business and investor community and is summarised below.

**Implications for Access to European Funding**

2.7 There has been a high degree of uncertainty on the implications of the vote on the 2014-2020 European Structural Investment Funds programme (ERDF and ESF) nationally and locally. Greater Manchester’s ESIF allocation for the programme period is €413.8m (approx £322m at January 2016 exchange rates), and Greater Manchester prudentially planned for two phases of ESIF projects 2014-2018 and 2018-2022.

2.8 The 2014-2020 ESIF programme had a slow start as a result of lengthy negotiations between HM Government and the European Commission. This delay has meant that only limited funding has progressed to contract before the referendum vote – c11% of GM’s ERDF allocation and c27% of ESF. With little correspondence from Government, there were significant concerns the majority of Greater Manchester’s ESIF funding programme was at risk.
2.9 On 13th August, a statement was released by the Chancellor of the Exchequer. This set out Government’s intention that in the short term all ESIF projects that can be under contract by the 2016 Autumn Statement (late November/early December 2016) will be fully funded. In the medium term, new arrangements will be put in place to consider ESIF projects post-Autumn Statement.

2.10 The August GMCA update paper on the European Structural Investment Funds set out that, although the statement initially appears positive, it is very concerning that Government are using date of the Autumn Statement as an arbitrary deadline for guaranteeing ESIF projects that are contracted by that date. A more logical approach would be to demonstrate spend by the end of 2018/9, not by constraining spend per se. This is not consistent with a fiscal stimulus requirement at a time when the national economy is slowing down - indeed given that we remain a contributor to EU till we leave, this policy is more consistent with a medium term policy of securing a rebate from the EU.

Implications for Changing Rules, Regulations and Trading Relations

2.11 Brexit will require a renegotiation of the trading relations between the UK and EU countries, as well as a renegotiation of access to any EU trans-national funding. In addition, leaving the EU could mean significant changes to the rules and regulations governing GM businesses and consumers in areas such as Health & Safety, Employment Law and Environmental Regulations.

2.12 The vast majority of EU rules and regulations have been embedded within UK law. Unless or until the UK Government decided to remove some of those – which would be likely to be a selective process given that there are tens of thousands of them – it is difficult to judge where GM would have an interest. One key area would be State Aid where repeal or replacement would change the parameters for GM’s services to businesses – with significant implications if areas start to compete against each other in an unrestricted way to attract companies and competitive pressures (a key driver of productivity) are reduced.

2.13 Looking forward, if the Fundamental Freedoms of movement in goods, services, capital and labour were ended or amended then that would change the parameters of future policy making in areas such as taxation. It is likely that some form of these Freedoms would need to be accepted by the UK in order to continue accessing EU markets, and although any negotiation around these is some way off, the UK government will have to decide its negotiating position quickly and therefore the window for influencing the direction of negotiations will close rapidly.

2.14 Analysis is being undertaken to identify the significant rules and regulations that GM may wish to influence, particularly in relation to particular sectors of relevance to Greater Manchester around trade, employment, investment, migration and energy/the environment to ensure we are able to input GM’s interests credibly into future national negotiations.
Implications for Key Sectors

2.15 There are already concerning signs for some of GM’s internationally significant key sectors, with the GfK consumer confidence survey suffering one of the largest falls in its history and the fall in the exchange rate indicating that investors may have reduced confidence in the UK as an investment location (although this may create opportunities for some businesses if it means they become more competitive in overseas markets).

2.16 The current Deep Dive analysis – GM’s in depth assessment of the opportunities and challenges facing sectors across the city region – is providing a rigorous evidence base, supplemented by the analysis of capabilities identified in the Northern Powerhouse Independent Economic Review. There are significant implications for the internationally-traded capabilities identified by that Review:

- Advanced Manufacturing is facing disruption as firms often rely on international supply chains and markets and requires high levels of capital investment which is threatened by uncertainty;
- Financial & Professional Services is one of the export strengths of the city region and the UK as a whole, but it is likely to be more difficult to negotiate new agreements around services, partly because they tend to require the free movement of people. GM will need to ensure that any negotiation around terms of trade to suit London’s financial market are also beneficial to the GM economy;
- Higher Education is at risk if uncertainty has an impact on the number of overseas students coming to study in GM and/or on EU funding streams and access to internationally leading research funding/programmes which GM institutions are able to access;
- Health Innovation requires high levels of international co-operation, investment by global businesses and the ability to access skilled workers from around the world;
- Digital requires collaboration across borders in order to keep at the cutting-edge of technological developments.

2.17 There will also be a range of implications for other sectors of the economy, including for some large employment sectors (and parts of the public sector) which have become dependent on a migrant workforce. There could also be particular implications for the tourism sector.

2.18 Manchester Growth Company (MGC) is gathering intelligence from GM businesses of all sizes, as well as inward investors through contacting its pipeline and Key Accounts. MGC is putting in place a range of additional support measures for companies initially focusing on informing and managing uncertainty. A new business ‘sounding board’ will provide ongoing advice and rapid feedback on developments. It will also be essential to understand in ‘real time’ any changing industry issues/confidence at a detailed sectoral level and to achieve far greater penetration into the GM business base, across the full range of sectors and sizes, than has been achieved to date.

2.19 MGC has therefore established an Advisory Board made up of representatives of MGC, IOD, Chamber of Commerce, EEF, FSB and others
to oversee the development and implementation of GM’s response to the issues faced by different sectors of the economy. Based on the intelligence gathered and analysis produced through engagement with businesses as outlined above, bespoke packages of support and specialised resources will be developed to ensure that GM business remain confident enough to continue to invest and diversify. This might include the need to strengthen the Sector Account Management activities within MGC to enable detailed engagement, analysis and support work within GM’s priority sectors to ensure that we not only have access to the latest information but also can respond in an integrated way with other business intermediary groups. Targeted trade interventions in selected countries as well as more general ‘open for business’ campaign (including investors, visitors etc) should also be considered.

2.20 The Hub is stepping up engagement with foreign-owned and large domestic companies, and adapting diagnostics and business engagement tools to ensure SME are building their resilience and taking advantage of any emerging opportunities. MGCs International Trade Team (UKTI) are engaging with exporting companies to explain that trading frameworks remain the same, and raising awareness of the GM Export Grant and Loan Fund.

2.21 In addition, analysis is underway to examine what opportunities may be created by Brexit for opening up to new markets outside the EU as well as the key issues for GM sectors around market access to the EU – assessing what the current barriers are and the extent to which these could be more easily tackled from outside the EU – or for adapting rules and regulations so that they work better for GM businesses (see above).

Implications for Property Investment

2.22 The commercial property market seems to be reacting quickly to Brexit, with evidence already that investment in slowing. Dialogue is continuing with property investors so that GM can make an ongoing assessment of the state of confidence with initial intelligence suggesting that investors, particularly those in North American markets, are nervous about making investments. Continuing investment will be crucial not only for driving productivity growth and maintaining the supply of well-paid and secure jobs, but also because the devolution of 100 per cent of Business Rates revenue means that a significant proportion of authorities’ spending is going to be dependent on the supply of business property which drives Business Rates revenue.

2.23 There is an immediate risk to property investment because current uncertainty of ERDF funding means that it is possible that we will not be able to access the funding required to extend the Evergreen Fund as originally planned. The timescales set out by the Chancellor may not give sufficient time to create and implement a meaningful fund. It is also possible that the Northern Powerhouse Investment Fund, supported by the British Business Bank will be in the same position. It is vital that GM is able to response to increasing demand for ‘pari passu’ or part-funded debt if confidence in the investment market is to be shored up, and this requirement has been reflected in Greater Manchester’s bid for Local Growth Funding and part of the Government’s Growth Deal process.
Implications for Housing & Planning

2.24 GMCA’s Preferred Growth Option, agreed by the GMCA at its August 2016 meeting, requires a significant uplift in the provision of new housing if we are to meet housing requirements over the coming decades. However, initial intelligence indicates that share values amongst housing developers have fallen by 25-30% since the announcement of the referendum result. Housing completion rates had recently reached 5-6,000 units per annum, from a low of 3-4,000 units per annum, but development rates will almost certainly decline again in light of the economic uncertainty we are facing. Urgent work is now required to examine options to maximise levels of housing development and investment.

2.25 National housing market policy has, to date, been driven by market developments in London and South East and many of the instruments available via HCA have not been effective in a GM context. Brexit is likely to exacerbate these problems. One-size-fits-all policy approaches which attempt to address the very different problems in London and the South East, at the same time as the North, have not been working. Government housing policies following recent downturns have also tended to attempt to stimulate demand, maintaining high prices in the South East, rather than directly providing more resources for building homes.

2.26 It is already clear that there is a gap in our toolkit, which means that many housing schemes are stalled not because of a lack of funding but because there is a viability gap arising from historic contamination, poor infrastructure and fragmented ownership. Traditional funding models and existing mechanisms for extracting value for land are insufficiently flexible or will not yield sufficient value to close that viability gap.

2.27 GM needs Government to take a long term view of infrastructure investment (including investment in brownfield sites to make them attractive to the market) and enable flexible place-based solutions relevant to the needs of an area, rather than national solutions. GM is therefore investigating this area further through joint work with Northern Core Cities and Government to develop new place based approaches in the light of Brexit. The growing challenge also means that there may be a case for looking again at the GMCA or Local Authorities carrying out direct development.

Implications for Inclusion

2.28 It is clear that Britain’s exit from the EU will have significant social as well as economic implications. Again, it is too early to understand the likely impact in any detail but initial analysis of voting patterns across the country show that there are correlations between specific characteristics and voters’ propensity to vote Leave as demonstrated by the Lord Ashcroft report issued shortly after the referendum. Urban city centres such as Manchester voted to remain in the EU but the degree of support for Remain decreases almost in direct proportion with the distance from the centre. This voting pattern correlates with the socio-demographic profile of city residents spatially, with educational attainment and earnings declining as the distance from the city centre widens.
More than two thirds of those in receipt of state pensions voted Leave, as did two thirds of council and housing association tenants. The referendum has exposed significant divisions in opinion across age groups, socio-economic classes, education levels and other classifications. The prominence of immigration in the referendum campaign has also raised issues around social cohesion with incidents of racial intimidation and hate crime being more widely reported. Short and long term strategies will be required to address these issues.

2.29 If the uncertainty caused by Brexit causes further stagnation of wages, rising prices, higher unemployment or less job certainty, then it will add further to the challenge of ensuring that everyone can contribute to, and benefit from, growth in GM. For example, the fall in sterling may well cause inflation to rise, hitting living standards by reducing real wages and benefits.

2.30 The programme of work set up by GM to feed in to the RSA Inclusive Growth Review, which is gathering evidence from around the city region, will focus on understanding the potential drivers of inclusive growth and the factors which can support resilience of communities to the economic implications of Brexit. This work will also develop options for policy responses which could help widen the opportunities for all communities to contribute to, and benefit from, future growth. These will be aimed at tackling the causes of stagnating living standards and the lack of opportunities for people to progress into work and higher paid secure jobs.

2.31 A key issue in the GM economy is the low wage, low skills, low productivity nature of the economy and the disconnection of some residents from economic growth. GM has previously undertaken research on the issues of Low Pay and Progression but working with Core Cities, expert external advice has been secured to investigate all these issues further and develop appropriate policy responses to drive productivity in all sectors, including our large employment sectors, rather than just focusing on our prime capabilities. By tackling some of these issues GM will be able to ensure it understands the problems (and how they might change post Brexit, including potential changes in migration) and that GM has the tools it needs to continue to drive inclusive growth even through the difficult economic conditions that might occur.

**Monitoring Economic Trends & Developments**

2.32 In each of these areas it is recognised that it is crucial that GM is able to respond to the latest developments. New Economy is monitoring economic trends and developments (see below), including in consumer and investor confidence, ongoing investment at a GM and national level, productivity growth, employment and population trends (including migration). Data will be assessed from national and local surveys and ONS releases, as well as studies by businesses, think tanks, academics and other groups and regular updates will be produced.

**Utilising GM’s Relationships with Key Central Government Departments**

2.33 Rapid changes in the national political situation and the approach of the newly re-structured Government departments will have implications across each of
the areas above. GM’s relationships with key Central Government departments, particularly HM Treasury, the new Department for Business, Energy and Industrial Strategy, the Department for Education (now including skills and higher education), CLG and Cabinet Office, are being used to get ongoing feedback on issues such as plans for policy programmes and investments and the potential priorities of the new government, including around devolution.

2.34 There could also be opportunities from using our relationships with other EU cities to encourage them to put pressure on the European Commission to negotiate a post-EU deal which works in the interests of GM.

3. GREATER MANCHESTER BREXIT MONITOR

3.1 Following the request from the GMCA for regular updates of the impact of Brexit to be produced, a Greater Manchester Brexit Monitor has been developed to consistently monitor economic and social trends and policy developments arising from the decision to leave the EU. The Greater Manchester Brexit Monitor will be produced monthly to track the impact of Brexit across the key themes below, which align with the work programme areas agreed by the GMCA. The first iteration of the monitor is attached to this paper. The themes being monitored are:

- Macro-economy trends and developments;
- Key sectors (including business investment);
- Rules, regulations and terms of trade & access to European Funding;
- Property investment, housing and planning; and
- Economic inclusion.

3.2 This first iteration of the Monitor captures the latest evidence available across each of the themes, recognising that the impacts in many cases are yet to emerge. It is too early to make any firm policy judgements at this stage but further editions will capture the implications for policy, changing rules and regulations as they unfold, as well as the work which GM is undertaking to inform the decision making process. Subsequent editions of the Monitor will be able to capture greater detail on the implications of Brexit as more data and analysis is released.

3.3 The Brexit Monitor, combined with the leading economic advice secured, will be used to advise the GMCA over the coming months on key implications for Greater Manchester and issues that GM will want to raise with Government either via the Autumn Statement or in the Brexit negotiations.

4. RECOMMENDATIONS

4.1 Recommendations are set out at the front of the report.

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