

## Déjà vu as Brexit stockpiling restarts ahead of October deadline

UK manufacturing took a hit during the second quarter as companies cut back on new orders, whilst they grappled with elevated stock levels. But where these firms have destocked, the latest PMI hints that they are beginning to resume the inventory building process as the October Brexit deadline inches nearer



Source: istock

Another month, another woeful UK manufacturing PMI reading. For the third month running, the index has slipped below the breakeven 50 level – and at 48.0, the PMI indicates the sector continued to contract in July.

Much – if not all – of this recent weakness is linked to pre-Brexit stockpiling. Having built inventory to insulate against possible supply chain disruption, firms have been cutting back on new orders while they grapple with what to do with all the extra stock.

But while the PMI points to a lacklustre start to the third quarter for manufacturing – driven partly by the global slowdown in demand – the Markit/CIPS press release suggests that the inventory story may be starting to evolve. The new 31 October Brexit deadline is drawing nearer, and firms

are once again ramping up preparations for a potential 'no deal' scenario. Stocks of finished goods inched higher in July – albeit more slowly than earlier in the year.

So what does this mean for growth in the second half of the year? Well a lot will depend on how far firms unwound stockpiles during the second quarter – and next week's GDP data will give us a clue. In some cases, firms will probably have had no choice but to try and work down their stock levels, given storage costs and working capital considerations. While we may not see a full correction, we're likely to see a reasonably sizable inventory drag during the second quarter, and overall growth will probably come in more-or-less flat.

The real challenge for those firms who need to rebuild stock in advance of the October deadline will be finding a place to store all the extra goods. The [UK Warehousing Association](#) suggests that space is already booked up ahead of Christmas. According to Markit, some firms are asking to delay delivery times – perhaps a hint that these warehousing constraints are already becoming an issue.

One way or another then, the UK growth numbers are likely to remain volatile for the rest of the year. But stripping away the inventory effect, the underlying story still doesn't look great. Investment is likely to continue falling over the summer as Brexit preparations draw resources away from capital spending, and limit appetite to expand. Consumer spending has also been fairly lacklustre, despite a modest improvement in real wage growth.

For the time being though, we think it's probably too early to be thinking about UK rate cuts and instead, we think the Bank of England will keep rates on hold for the rest of the year.

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