



BDO MONTHLY BUSINESS TRENDS INDICES

November 2013

INTRODUCTION

The BDO Monthly Trends Indices are ‘polls of polls’ that pull together the results of all the main UK business surveys. This edition of the BDO Business Trends Report gives the Index numbers for October, using the results from business surveys that were carried out between the first and last days of last month.

Summary and key findings

Index	Current reading	Movement in month	Index level
BDO Output Index	✓✓✓	▲	100.7 in October from 99.5 in September
BDO Optimism Index	✓✓✓	▲	101.7 in October from 100.7 in September
BDO Inflation Index	✓	▼	100.5 in October from 100.6 in September
BDO Employment Index	✓✓	▲	98.1 in October from 97.5 in September

KEY: ✓ = above 100; ✓✓ = (joint) highest in 12 months; ✓✓✓ = above 100 and (joint) highest in 12 months
 ✗ = below 100; ✗✗ = (joint) lowest for 12 months; ✗✗✗ = below 100 and (joint) lowest in 12 months

KEY FINDINGS

Business conditions continued to improve in October, as the BDO Output Index increased to 100.7, up from 99.5 the previous month. The last time the Index was higher was in June 2010. The economic recovery is now firmly entrenched in both the manufacturing and services sectors according to the BDO Output sub-indices, meaning the recovery is now present throughout the overwhelming majority of the UK economy. The services sector sub-index rose to 99.4 in October, up from 98.6 in September. The manufacturing sub-index rose to 106.5 in October, increasing from 103.6 in September. Markit/CIPS data indicate that export orders are contributing to the manufacturing sector recovery, with a slowly improving mainland Europe providing a boost. Overall, the BDO output Index suggests the UK economy is set for robust growth over the final quarter of 2013.

The Optimism Index reached 101.7 in October, up from 100.7 in September. The last time confidence was higher was in April 2010 and the Index suggests that UK economic growth will outperform its long-term historical trend over the coming six months. The services sector confidence sub-index rose to 99.9 in October; this is up from 99.2 in September and stands just below the 100.0 mark which indicates sectoral growth is at its long-run average rate. Improvements in the services sector have played a marked role in lifting the headline Optimism Index, as the services sector covers approximately three quarters of the economy. The manufacturing confidence sub-index also rose to 109.6 in October, up from 107.0 in September, demonstrating that the economic recovery is broad-based and suggesting economic growth may pick up speed going forward. New orders and increasing export demand are lifting sectoral confidence.

Inflation expectations for business input prices held steady over October 2013. In October, the BDO Inflation Index recorded a reading of 100.5, just down on the September reading of 100.6. This came after four consecutive falls in businesses' inflation expectations which now stand at their lowest level since January 2013. Holding down cost inflation, total wages were only 0.7% higher during June-August 2013 than one year earlier. This was the slowest rate of annual regular pay growth since January-March 2013. Wage growth is below the rate of inflation, meaning that *per employee* wage costs are falling in real terms. This has helped services firms, which are relatively labour intensive, to control costs. Input prices for UK manufacturers rose modestly, by only 1.1% over the year to September. The last time annual input price growth was slower was over the year to April 2013.

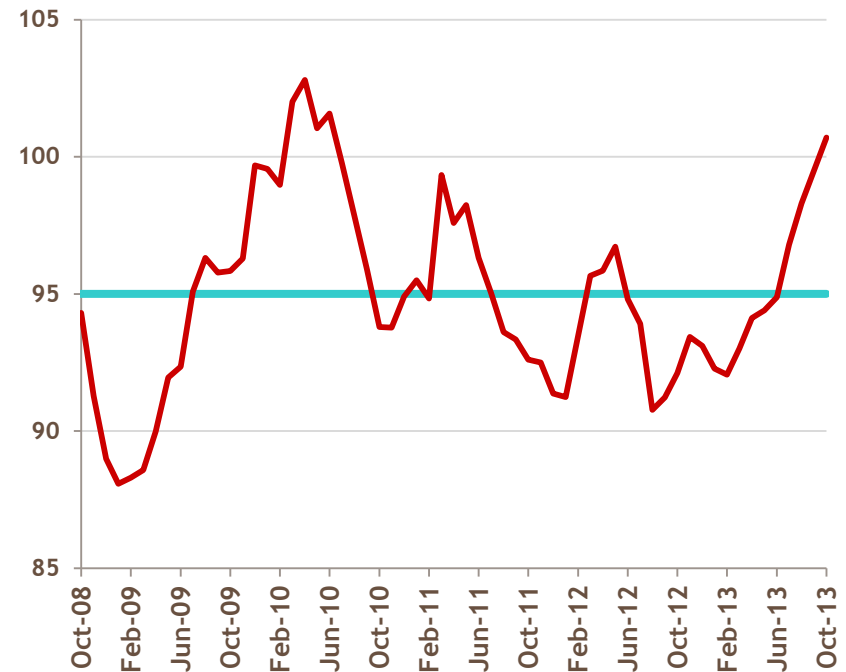
Hiring expectations increased modestly over October as the BDO Employment Index rose to 98.1, up from the 97.5 figure recorded one month earlier. The index is slowly approaching the 100.0 mark, the level at which UK private sector employment will be expected to grow at its long-term trend rate over the coming three months. Nevertheless, the index presently stands below the 100.0 level, tying in with slow declines in the UK unemployment rate. The headline unemployment rate stood at 7.7% over June-August 2013, just down on the 7.9% rate seen one year earlier. A risk to the unemployment outlook comes from the level of spare capacity remaining in the economy. Employers may move part-time staff them on to longer hours instead of hiring more. Moreover, relatively low productivity means firms have room to grow without hiring additional staff.

OUTPUT INDEX REACHES HIGHEST LEVEL SINCE MID-2010, INDICATING STRONG Q4 GROWTH

- Business conditions continued to improve in October, as the BDO Output Index increased to 100.7.
- This is up from the 99.5 reading seen in September and is the highest reading since June 2010.
- The BDO Output sub-indices indicate that the economic recovery is now broad-based and firmly entrenched in both the manufacturing and services sectors.
- The manufacturing sub-index rose to 106.5 in October, a rise from the 103.6 reading in September. In an encouraging sign for manufacturers and the wider UK economy, there is evidence that new export orders from the US, Asia, Europe and the Middle East contributed to this rise.
- The services sector accounts for over three quarters of the UK economy and the sectoral sub-index also rose to 99.4 in October, an improvement on September's 98.6 figure. This implies sectoral growth over the coming three months is expected to be just shy of its long-term trend.
- The BDO Output Index data suggest the broad-based recovery is gathering pace and that UK economic growth over Q4 2013 may be faster than the 0.8% seen over Q3 2013.

BDO OUTPUT INDEX

100 = average trend growth. Greater than 95 = positive growth



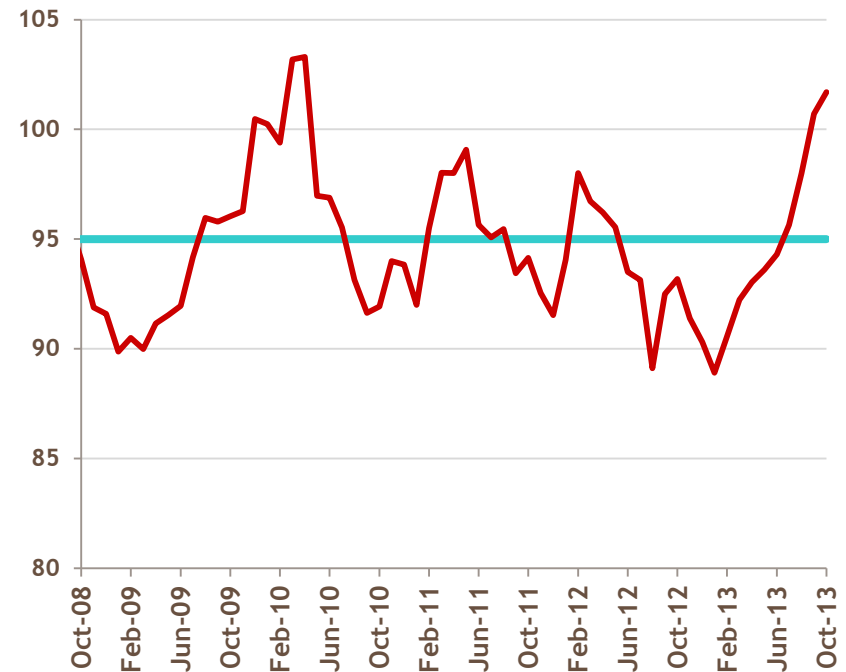
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

RISING BUSINESS OPTIMISM SUGGESTS ECONOMIC RECOVERY WILL REMAIN ROBUST

- The BDO Optimism Index rose noticeably in October 2013 and it stands at a level which suggests the economy will grow faster than its long-term trend over the coming six months.
- The Optimism Index reached 101.7 in October, up from 100.7 in September - confidence is now at its highest level since April 2010.
- The services sector confidence sub-index rose to 99.9 in October. It now stands just below the 100.0 mark which indicates services sector output is expected to grow at its long-run rate over the near term. Because the services sector covers roughly three quarters of the UK economy, improvements here have been vital in lifting the headline BDO Optimism Index.
- The manufacturing confidence sub-index also rose to 109.6 in October, up from 107.0 in September. Slowing input price growth and a recovery in new orders - even from struggling Europe - are lifting manufacturers' spirits.
- Overall, the Optimism Index is on a strong upward trend, suggesting economic growth may well remain robust over the next six months.

BDO OPTIMISM INDEX

100 = average trend growth. Greater than 95 = positive growth



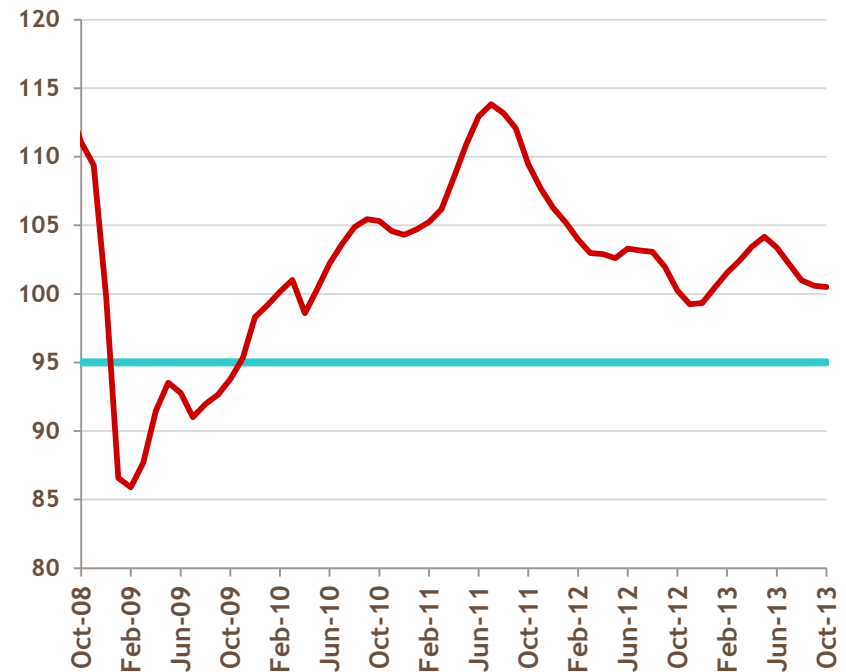
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

INFLATION EXPECTATIONS LOWEST SINCE JANUARY 2013

- Business inflation expectations stood on hold in October according to the BDO Inflation Index. The Index fell to 100.5 in October from 100.6. This follows four consecutive falls in businesses' expectations of price inflation over the coming three months.
- Falls in the Inflation Index now seem to have levelled off and the Index now stands at its lowest since January 2013.
- Keeping costs in check for labour-hungry services firms, total wages were only 0.7% higher during June-August 2013 than over the same period of 2012. This was the slowest rate of annual regular pay growth since January-March 2013.
- Moreover, because wage growth is below the rate of inflation, real *per employee* wage costs are falling.
- In a similar vein, input price growth for UK manufacturers has slowed significantly of late. Input prices increased by only 1.1% over the year to September. The last time annual input price growth was slower was over the year to April 2013.

BDO INFLATION INDEX

100 = average trend growth. Greater than 95 = positive growth



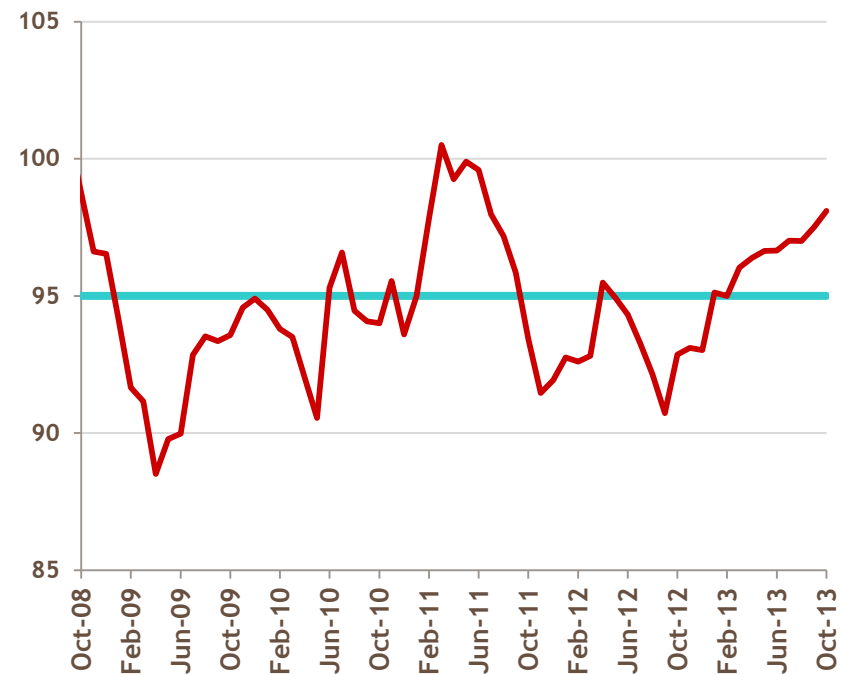
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

PRIVATE SECTOR HIRING INTENTIONS MAKE SLOW BUT STEADY PROGRESS

- Businesses' expectations for private sector hiring growth improved modestly over October as the BDO Employment Index rose to 98.1, up from the 97.5 figure recorded in September.
- The Employment Index is slowly approaching the 100.0 mark; this suggests that UK private sector employment growth is slowly approaching its long-term trend rate.
- Nevertheless, the official unemployment rate is still coming down only slowly. The rate stood at 7.7% over June-August 2013, just down on the 7.9% rate seen one year earlier.
- Despite strengthening hiring intentions, further public sector payroll reductions are likely, which could stop the UK unemployment rate coming down quickly.
- Moreover, a risk to the unemployment outlook comes from the level of spare capacity remaining in the economy. Many workers are still working part time. Employers may move them on to longer hours instead of hiring more staff. Relatively low productivity means firms have room to grow, perhaps getting more from existing employees without hiring additional staff.
- Overall, the unemployment rate may not come down as fast as the economic recovery suggests.

BDO EMPLOYMENT INDEX

100 = average trend growth. Greater than 95 = positive growth



Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

BDO INDICES TO LATEST MONTH

		Oct 2012	Nov 2012	Dec 2012	Jan 2013	Feb 2013	Mar 2013	Apr 2013	May 2013	June 2013	July 2013	Aug 2013	Sept 2013	Oct 2013
The BDO Optimism Index	Total	93.2	91.4	90.3	88.9	90.6	92.2	93.0	93.6	94.3	95.6	98.0	100.7	101.7
	Manuf.	89.2	85.9	91.9	95.2	94.5	88.2	88.3	88.5	89.0	91.4	99.6	107.0	109.6
	Service	94.2	92.8	89.9	87.3	89.6	93.2	94.1	94.8	95.5	96.6	97.7	99.2	99.9
The BDO Output Index	Total	92.1	93.4	93.1	92.3	92.1	93.0	94.1	94.4	94.9	96.8	98.3	99.5	100.7
	Manuf.	87.0	88.8	90.6	92.3	94.1	92.4	90.8	93.7	95.7	98.3	100.7	103.6	106.5
	Service	93.4	94.6	93.8	92.3	91.5	93.2	94.9	94.4	94.7	96.5	97.7	98.6	99.4
The BDO Inflation Index	Total	100.2	99.2	99.3	100.4	101.5	102.4	103.4	104.2	103.4	102.2	101.0	100.6	100.5
The BDO Employment Index	Total	92.9	93.1	93.0	95.1	95.0	96.0	96.4	96.6	96.7	97.0	97.0	97.5	98.1

FOR FURTHER DETAILS

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METHOD NOTES

The BDO Monthly Business Trends Indices are prepared on behalf of BDO LLP by the Centre for Economics and Business Research, a leading independent economics consultancy. Cebr has particular strengths in all forms of macroeconomic and market forecasting for the UK and European economies and in the use of business survey techniques.

The indices are calculated by taking a weighted average of the results of the UK's main publicly available business surveys. It incorporates the results of the quarterly CBI Industrial Trends Survey (and the CBI Monthly Trends Enquiry which is carried out in the intervening months); the Bank of England Agents' summary of business conditions; the Markit / the Chartered Institute of Purchasing and Supply's Surveys of Manufacturing and of Services; the DG ECFIN industrial and services confidence indices; the RICS construction market survey; the Manpower Employment Outlook Survey; and Eurostat's monthly business surveys.

Taken together the surveys cover over 4,000 different respondent companies, covering a range of different industries and of different business functions. Together they make up the most representative measure of business trends available.

The surveys are weighted together by a three-stage process. First, the results of each individual survey are correlated against the relevant economic cycles for manufacturing and services. This determines the extent of the correlations between each set of survey results and the relevant timing relationships. Then the surveys are weighted together based on their scaling, on the extent of these correlations and the timing of their relationships with the relevant reference cycles. Finally, the weighted total is scaled into an index with 100 as the mean, the average of the past two cyclical peaks as 110 and the average of the past two cyclical troughs as 90.

The results can not only be used as indicators of turning points in the economy but also, because of their method of construction, be seen as leading indicators of the rates of inflation and growth.