



BDO MONTHLY BUSINESS TRENDS INDICES

October 2015

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 at the beginning of October 2015, using the results from business surveys that were carried out between the first and last days of the previous month.

Summary and key findings

| Index | Current reading | Movement in month | Index level |
|----------------------|-----------------|-------------------|---|
| BDO Output Index | ✓ | ▽ | 104.3 in September from 104.5 in August |
| BDO Optimism Index | ✓ | △ | 102.2 in September from 101.9 in August |
| BDO Inflation Index | ✗ | △ | 96.1 in September from 95.9 in August |
| BDO Employment Index | ✓ | ▽ | 107.6 in September from 107.9 in August |

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

The BDO Output Index is down by 0.2 points compared to August's reading, having fallen from 104.5 to 104.3. Activity is still strong, showing the UK economy is not yet feeling the full effects of the global slowdown. That may change before long, as it spreads to more parts of the world. Europe is a rare example of a region where activity is speeding up, though this only modest and from very low levels. But for once the UK's strong links with the Eurozone could aid the economy's resilience.

The BDO Inflation Index remained on an upward path during September. This is largely due to firms' dominant cost of wages increasing. Very depressed prices in commodities, for example Brent crude oil at below \$50/barrel, offset the rises in wages to an extent. The level of the index indicates positive growth but significantly below the long-term trend rate.

The BDO Optimism Index has shown a slight rise for the first time in seven months. Sentiment among manufacturing firms is slightly less pessimistic than it had been, while confidence among service firms has only fallen marginally. Despite the improvement in manufacturing optimism, firms in the sector still expect to see a contraction over the next six months. The manufacturing sector is more globally linked, with confidence running correspondingly lower.

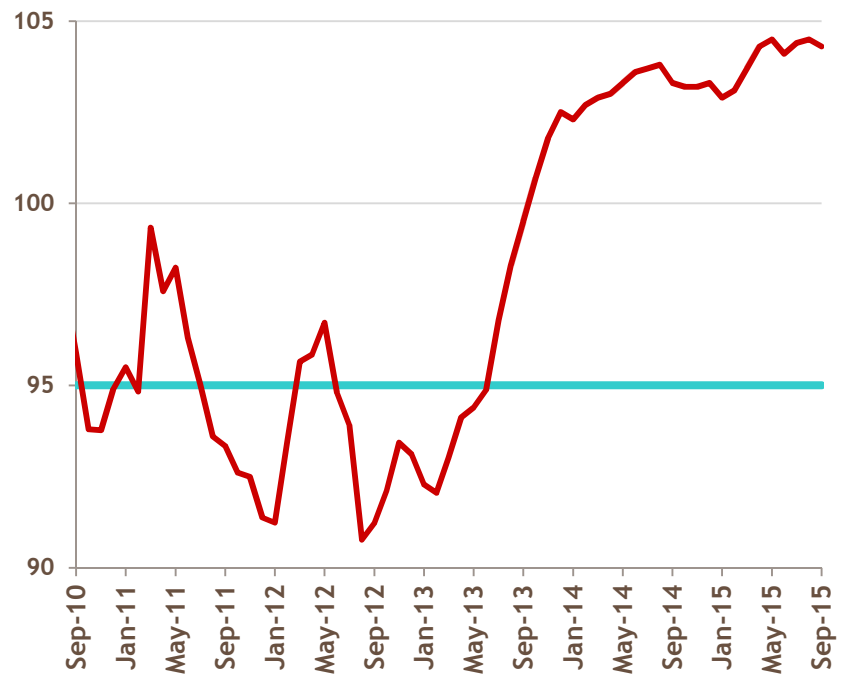
The BDO Employment Index has declined for the seventh month running. Since it is coming down from a very high level, the current figure of 107.6 still points to a strong labour market. Despite this, the gradual cooling in the rate of hiring is a factor behind the Bank of England's hesitation to raise interest rates above 0.5%.

UK FIRMS' OUTPUT HOLDS FIRM AMID GLOBAL SLOWDOWN

- The BDO Output Index showed a slight drop in September. It now stands at 104.3, compared to 104.5 in August.
- The index has plateaued in recent months, at a relatively high level. Firms still expect faster-than-average growth for the remainder of the year.
- This suggests that the UK economy, for the time being, has been somewhat insulated from a global slowdown starting to spread from China to other parts of the world. The US economy, also, has shown slowing activity recently. A modest acceleration in activity in Europe - the UK's largest trading partner - will be beneficial for business sentiment and demand for UK products.

BDO OUTPUT INDEX

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



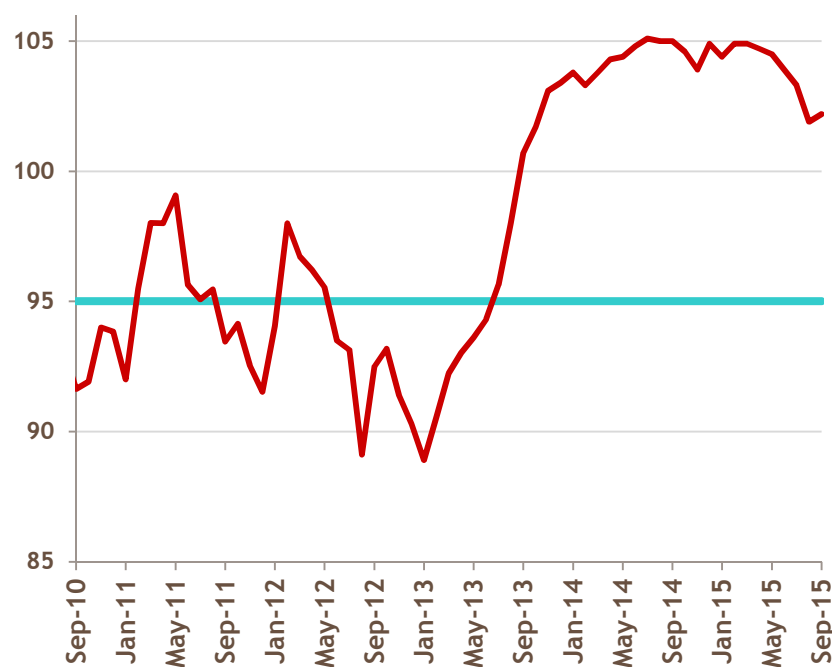
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

DOWNWARD TREND IN CONFIDENCE ARRESTED

- The BDO Optimism Index has risen slightly from 101.9 to 102.2, reversing a downward trend and marking the first positive change since February.
- Firms are expecting performance slightly better than the long-term trend, over a six-month horizon. There is a large discrepancy between services and manufacturing firms over their expectations.
- The implication from the Optimism Index's behaviour in recent months is that the high level of activity evident from the Output Index may well cool down before long.
- While encouraging, this month's move is a small rise. The main contribution came from manufacturing, the sub-index rising from 86.2 to 89.0. However, the sector remains well below 95, meaning firms are fairly pessimistic about the rest of the year.
- The manufacturing sector should be cheered by further falls in commodity prices, which are more important for industry than they are for service firms.

BDO OPTIMISM INDEX

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



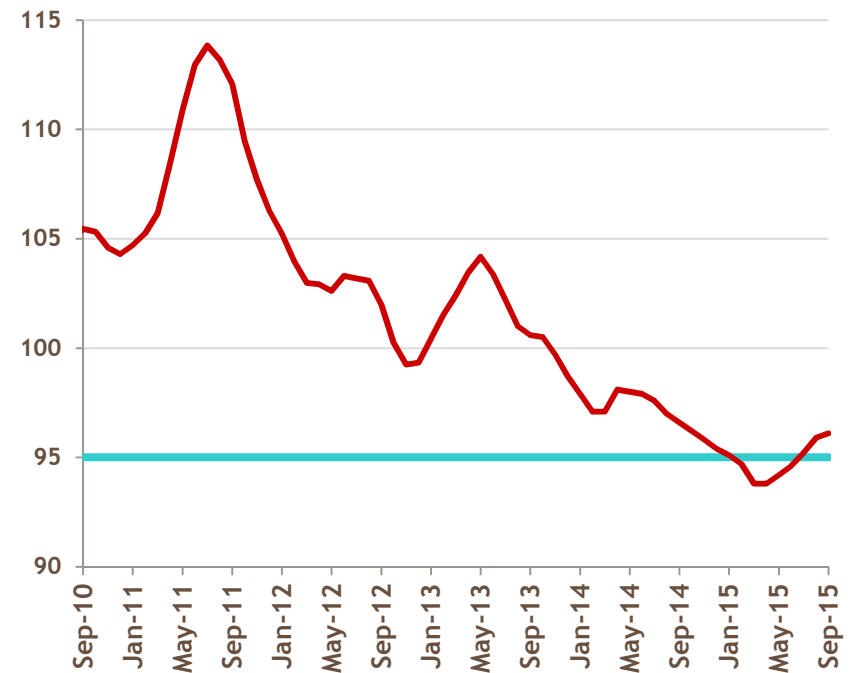
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

INFLATION INDEX POINTING TO GRADUAL COST RISES

- The BDO Inflation Index changed very little this month, creeping up from 95.9 to 96.1. Firms are now expecting to see gradually rising prices over a 3-6 month horizon.
- Commodity prices remain very low, with the key oil price down below \$50 per barrel. This applies to other many other input costs, with inputs for producers in general down by 1.8% in the year to August, as measured by the ONS producer price index.
- On the other hand, wages are up by 2.9% on the latest data. This is a more important cost for firms, and is starting to drive the inflation index upwards. The Index has now been on an upward path since April, which has been predominantly driven by wages rather than physical inputs.

BDO INFLATION INDEX

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



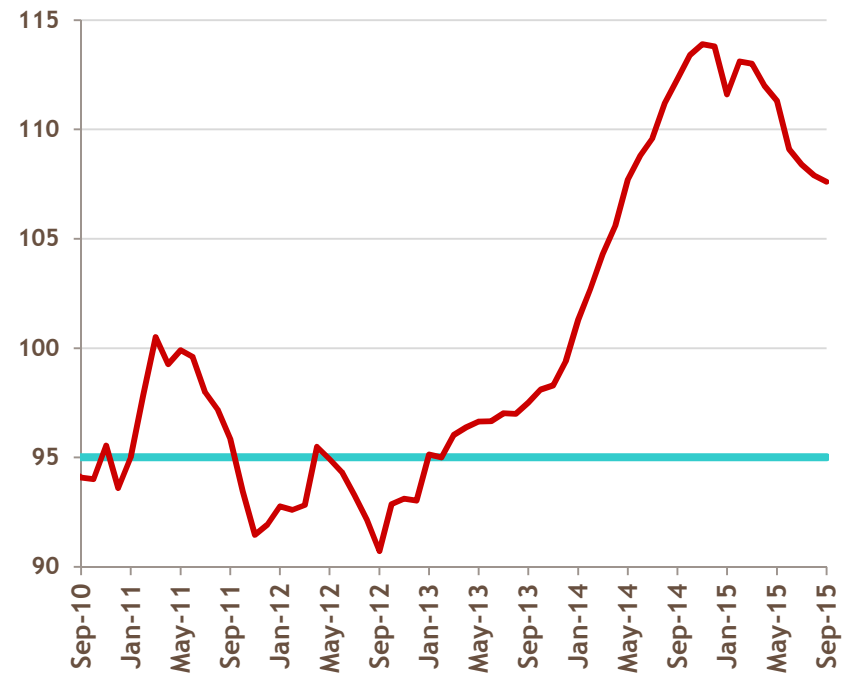
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

EMPLOYMENT PROSPECTS COOLING DOWN, BUT STILL STRONG

- The Employment Index remains strong at 107.6, marginally down on August's value of 107.9 but not seriously reduced.
- This continues a string of eight falls as the labour market returns to normality after a jobs-rich recovery.
- While the speed of hiring is slowing, other aspects of the labour market continue to show improvement. For example, earnings growth of 2.9% follows tighter conditions which mean employers have to raise offers. There have also been encouraging, consistent falls in the number of people working part-time who would prefer full-time work. Latest data show this is down almost 5% compared to one year ago.
- However, the Bank of England continues to hesitate rather than raise interest rates, based partly on evidence from the labour market. The recent cooling means the monetary policy committee sees little chance of a pickup in inflation.

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

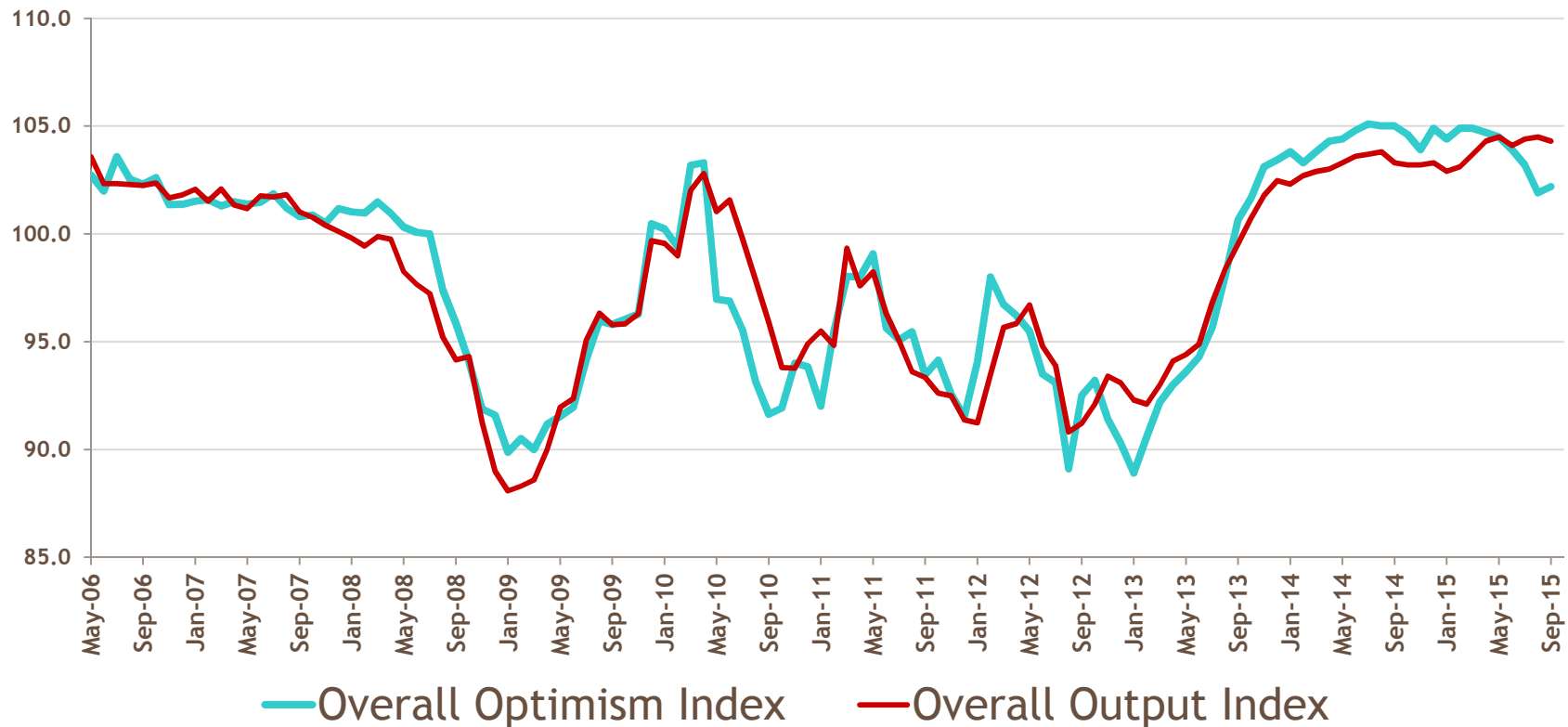
BDO INDICES TO LATEST MONTH

| | | Sep 2014 | Oct 2014 | Nov 2014 | Dec 2014 | Jan 2015 | Feb 2015 | Mar 2015 | Apr 2015 | May 2015 | Jun 2015 | Jul 2015 | Aug 2015 | Sep 2015 |
|--------------------------|--------------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|
| The BDO Optimism Index | Total | 105.0 | 104.6 | 103.9 | 104.9 | 104.4 | 104.9 | 104.9 | 104.7 | 104.5 | 103.9 | 103.3 | 101.9 | 102.2 |
| | Manuf. | 117.4 | 116.1 | 114.1 | 113.9 | 113.0 | 111.6 | 109.8 | 107.4 | 103.4 | 98.5 | 93.5 | 86.2 | 89.0 |
| | Service | 102.6 | 102.3 | 101.9 | 103.1 | 102.7 | 103.6 | 103.9 | 104.1 | 104.7 | 105.0 | 105.1 | 105.0 | 104.8 |
| The BDO Output Index | Total | 103.3 | 103.2 | 103.2 | 103.3 | 102.9 | 103.1 | 103.7 | 104.3 | 104.5 | 104.1 | 104.4 | 104.5 | 104.3 |
| | Manuf. | 111.6 | 110.1 | 109.1 | 108.0 | 107.3 | 107.1 | 107.7 | 108.8 | 109.0 | 107.8 | 106.8 | 106.8 | 106.5 |
| | Service | 101.7 | 101.8 | 102.1 | 102.4 | 102.1 | 102.3 | 102.9 | 103.5 | 103.6 | 103.4 | 103.9 | 104.1 | 103.9 |
| The BDO Inflation Index | Total | 96.6 | 96.2 | 95.8 | 95.4 | 95.1 | 94.7 | 93.8 | 93.8 | 94.2 | 94.6 | 95.2 | 95.9 | 96.1 |
| The BDO Employment Index | Total | 112.3 | 113.4 | 113.9 | 113.8 | 111.6 | 113.1 | 113.0 | 112.0 | 111.3 | 109.1 | 108.4 | 107.9 | 107.6 |

APPENDIX 1: UK FIRMS' OUTPUT HOLDS FIRM AMID GLOBAL SLOWDOWN

BDO OUTPUT AND OPTIMISM INDICES

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

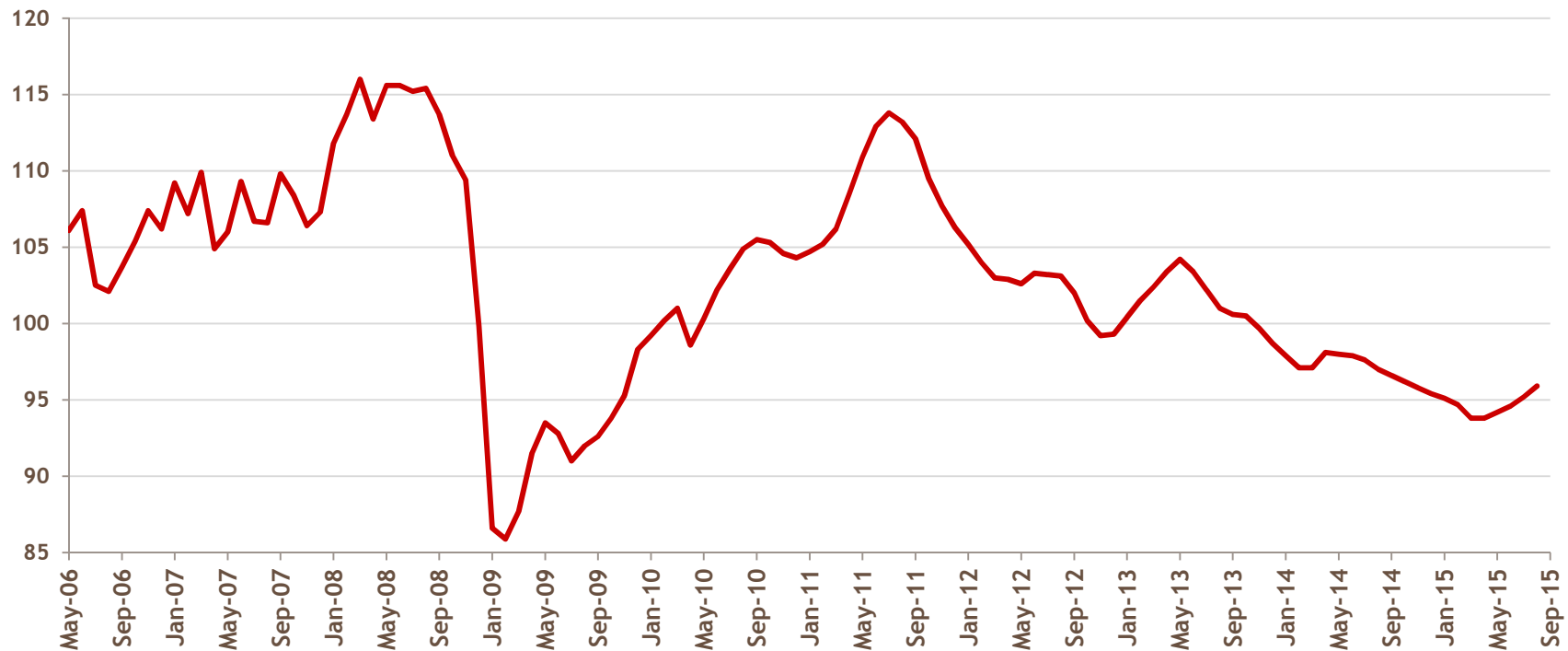


Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

APPENDIX 2: INFLATION INDEX POINTING TO GRADUAL COST RISES

BDO INFLATION INDEX

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



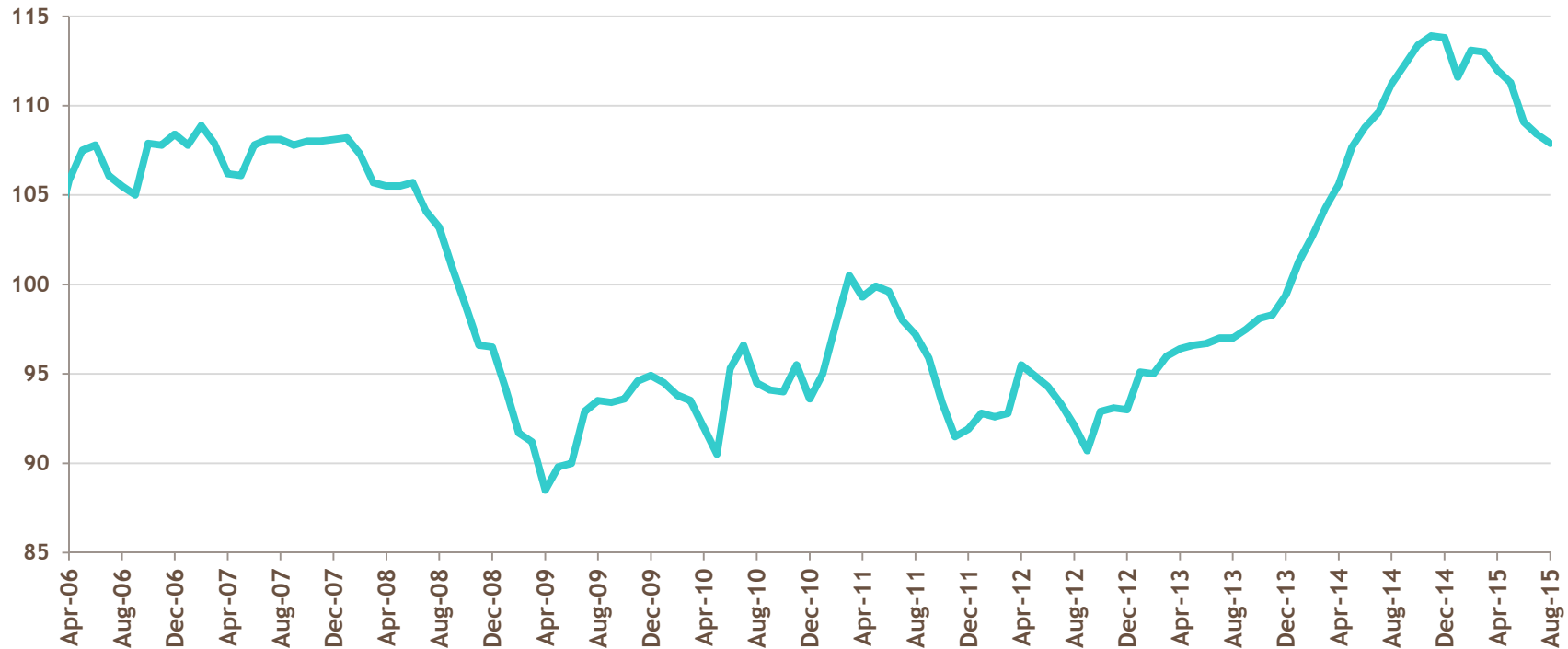
— BDO Inflation Index

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

APPENDIX 3: EMPLOYMENT PROSPECTS COOLING DOWN, BUT STILL STRONG

BDO EMPLOYMENT INDEX

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



— BDO Employment Index

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



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.