

BDO MONTHLY BUSINESS TRENDS INDICES

June 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 May, 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	x	▲	94.4 in May from 94.1 in April
BDO Optimism Index	✓✓	▲	93.6 in May from 93.0 in April
BDO Inflation Index	✓	▲	104.2 in May from 103.4 in April
BDO Employment Index	✓✓	▲	96.6 in May from 96.4 in April

KEY: ✓ = above 100; ✓✓ = highest in 12 months; x = below 100; xx = lowest for 12 months

KEY FINDINGS

There were further signs of strengthening business conditions in May, as the BDO Output Index rose to 94.4 from a previous reading of 94.1. This is the third consecutive increase and puts the Index at its highest in eleven months. The latest results are encouraging for the UK economy in 2013 and follow a confirmation from the Office for National Statistics of a 0.3% economic expansion in Q1 2013. However, as the Index still stands marginally below the 95.0 level that indicates growth three months ahead, it is likely that a continued cautious recovery is in store this year, with stronger growth remaining elusive for now.

Business confidence is continuing to rise, as the BDO Optimism Index reached in May its highest level in 12 months. The Index stood at 93.6, up from 93.0 in April after rising for four consecutive months. Stronger confidence suggests that the recent positive trend in business conditions, illustrated by the Output Index, is likely to continue until at least the end of 2013. However, the Index reading remains just below the 95.0 level that indicates economic expansion six months ahead, highlighting the continued risks to the UK outlook. Further real household income erosions are likely to constrain consumer spending growth this year, while government austerity is expected to take further effect and the Eurozone remains in recession, hampering UK export growth.

Inflationary expectations continued to rise in May, as the BDO Inflation Index climbed to 104.2 from a previous reading of 103.4. This is the highest that the Index has stood since January 2012 and highlights simmering inflationary pressures, following year-on-year cost declines for manufacturers in the latter half of 2012. Indeed, the Bank of England warns that inflation for consumers is likely to peak in Q3 2013 at over 3.0%. However, one factor restricting cost increases for businesses is pay growth; regular wages grew year on year in Q1 by just 0.8%, the slowest pace of growth since comparable records began in 2001.

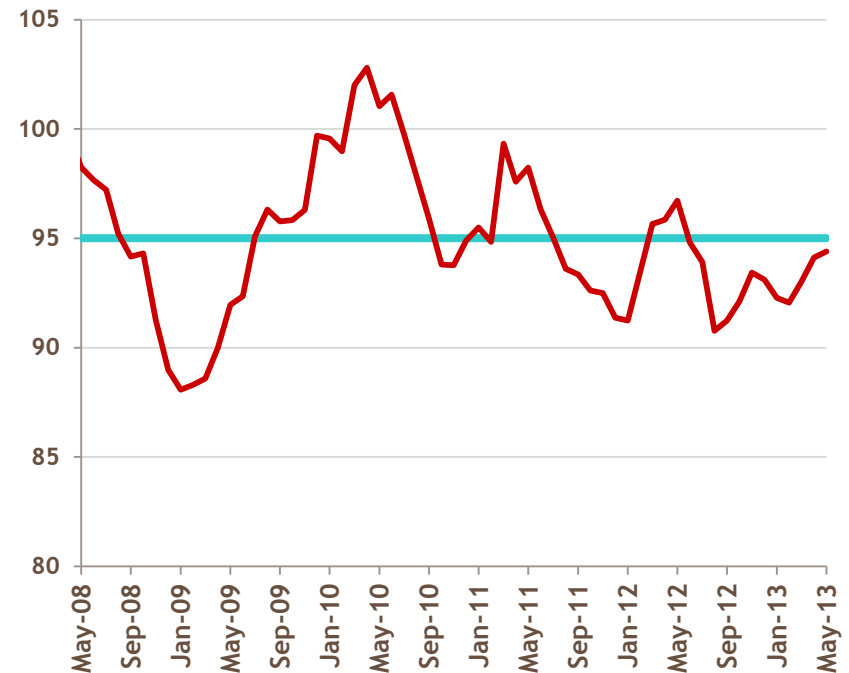
Low pay growth appears to be the price to pay for stronger job creation than the pace of economic growth justifies, as the BDO Employment Index rose again in May to a reading of 96.6, up from 96.4 the previous month. This is the third consecutive increase in the Index and takes the level to its highest since August 2011. Reflecting the recent strengthening of business hiring intentions, the number of out-of-work people claiming jobseeker's allowance fell back in May to its lowest since February 2012. Although the number of public sector employees is expected to fall back by 200,000 over the 2013/14 fiscal year, these latest findings showing rising private sector hiring intentions suggest businesses will be able to help offset falling government employment.

BUSINESS CONDITIONS CONTINUED TO STRENGTHEN IN MAY 2013

- The BDO Output Index rose again in May 2013 to a reading of 94.4.
- This is the third consecutive increase, up from 94.1 the previous month and the Index now stands at its highest level since June 2012.
- This upward trend in the Output Index points to stronger business conditions emerging in the UK economy, an encouraging sign following the 'zig-zag' growth path experienced in 2012.
- The latest Index reading follows figures from the Office for National Statistics, whose second estimate of UK output in Q1 2013 showed a 0.3% quarterly expansion, driven by consumer spending and a build-up of inventories.
- However, the Output Index continues to stand marginally below the 95.0 level that indicates positive economic growth three months ahead, suggesting that although a return to contraction is unlikely, the recovery will remain modest over the short term.
- Within the headline figure, the Output Index for Manufacturing climbed to 93.7 from a previous reading of 90.8, while the Index for the Services sector slipped marginally to 94.4 from 94.9.

BDO OUTPUT INDEX

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



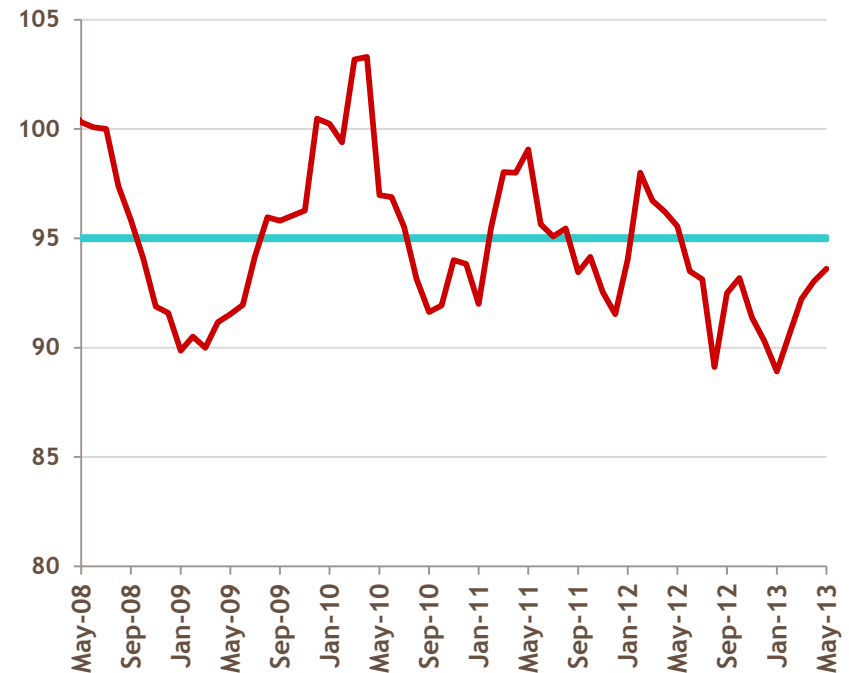
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

OPTIMISM LEVELS REACH A TWELVE MONTH HIGH

- The BDO Optimism Index increased to 93.6 in May 2013, up from a previous reading of 93.0.
- This is the fourth uptick in confidence levels in a row, bringing the Optimism Index to its highest score in twelve months.
- This continued upward trend in confidence suggests that the recent strengthening of business conditions is likely to continue into the second half of 2013, as the Optimism Index points to the economic environment six months ahead.
- Despite this good news, the Index continues to stand below the 95.0 mark that indicates expansion, highlighting the risks that do still remain to the recovery.
- Consumer spending is likely to face renewed pressure in real terms in the second half of 2013, as the effects of weak wage growth and the 1% cap in benefits uprating are felt alongside elevated inflation.
- In addition, government current spending is set to contract over 2013 as a whole and the UK's main export market, the Eurozone, remains in recession.

BDO OPTIMISM INDEX

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



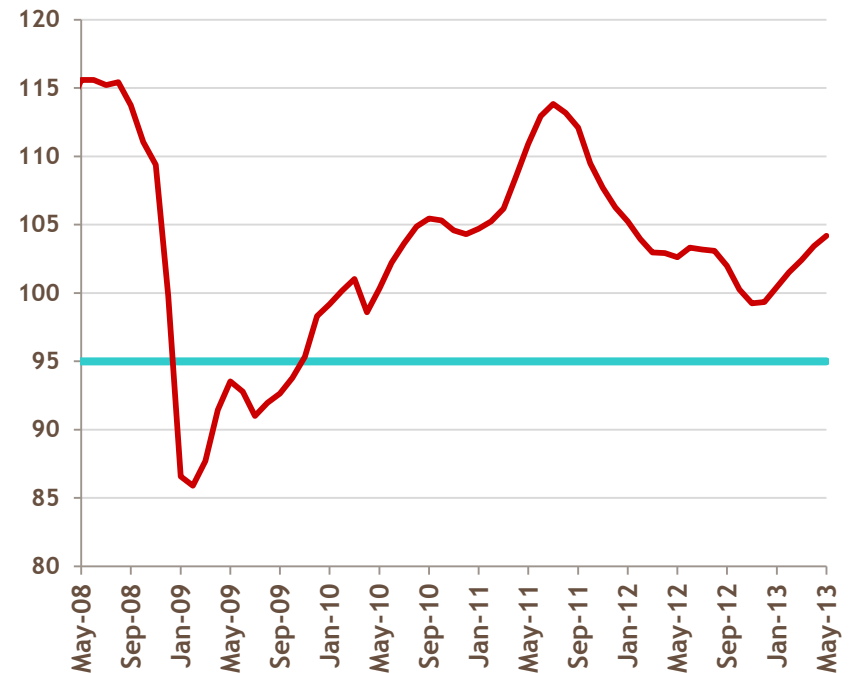
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

INFLATION EXPECTATIONS CONTINUE TO EDGE UP

- The BDO Inflation Index rose to stand at 104.2 in May, up from a previous reading of 103.4.
- This is the sixth consecutive increase in the Index and brings the level to its highest since January 2012.
- This latest finding reflects data from the Office for National Statistics, which shows that costs have started to climb again year on year for manufacturers, following input price annual deflation in the second half of 2012.
- In addition, although the rate of inflation on the consumer price index fell back in April to 2.4%, its lowest in seven months, this is expected to pick up again. Outgoing Bank of England governor Mervyn King suggested in his latest *Inflation Report* that the rate will peak at over 3.0% in Q3 2013.
- However, one factor unlikely to be playing into faster price growth for businesses is wage growth. Regular salaries increased year on year by just 0.8% in the first quarter of 2013, the slowest rate since comparable data records began in 2001. In addition, significantly faster salary growth is not expected this year.

BDO INFLATION INDEX

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



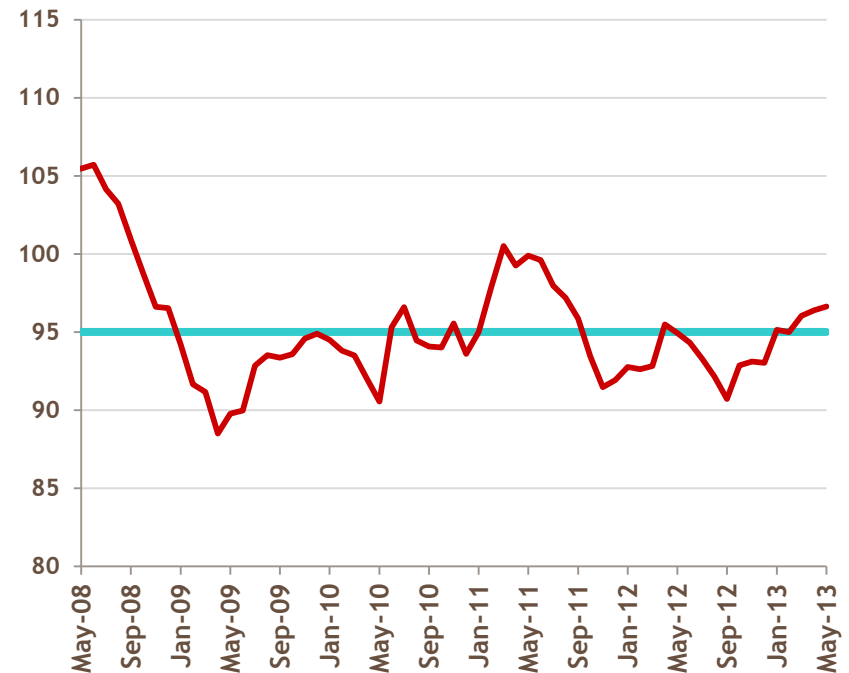
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

PRIVATE SECTOR FIRMS INCREASING THEIR HIRING INTENTIONS

- The BDO Employment Index rose to 96.6 in May, marginally up on the reading of 96.4 in the previous month.
- This is the highest at which the Index has stood since August 2011.
- Increased hiring intentions in the private sector are positive news for the UK's jobless. Although the Office for Budget Responsibility forecasts a decline in public sector employment over the 2013/14 financial year of 200,000, these latest results suggest that businesses may be able to support employment for some of these workers.
- The recent upward trend in the Employment Index is reflected in data on the claimant count, which showed dole queues shortening by 7,300 people in May.
- This is the lowest number of claimants since February 2012, with 67,800 fewer claimants than in the same month a year ago.

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

		May 2012	June 2012	July 2012	Aug 2012	Sept 2012	Oct 2012	Nov 2012	Dec 2012	Jan 2013	Feb 2013	Mar 2013	Apr 2013	May 2013
The BDO Optimism Index	Total	95.5	93.5	93.1	89.1	92.5	93.2	91.4	90.3	88.9	90.6	92.2	93.0	93.6
	Manuf.	92.2	83.8	90.5	80.5	90.2	89.2	85.9	91.9	95.2	94.5	88.2	88.3	88.5
	Service	96.4	95.9	93.8	91.3	93.1	94.2	92.8	89.9	87.3	89.6	93.2	94.1	94.8
The BDO Output Index	Total	96.7	94.8	93.9	90.8	91.2	92.1	93.4	93.1	92.3	92.1	93.0	94.1	94.4
	Manuf.	94.6	90.5	89.2	85.1	87.3	87.0	88.8	90.6	92.3	94.1	92.4	90.8	93.7
	Service	97.3	95.9	95.1	92.2	92.2	93.4	94.6	93.8	92.3	91.5	93.2	94.9	94.4
The BDO Inflation Index	Total	102.6	103.3	103.2	103.1	102.0	100.2	99.2	99.3	100.4	101.5	102.4	103.4	104.2
The BDO Employment Index	Total	94.9	94.3	93.3	92.1	90.7	92.9	93.1	93.0	95.1	95.0	96.0	96.4	96.6

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 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; Markit / the Chartered Institute of Purchasing and Supply's Surveys of Manufacturing and of Services; 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.