

BDO MONTHLY BUSINESS TRENDS INDICES

February 2013

INTRODUCTION

The BDO Monthly Trends Indices are ‘polls of polls’ that pull together the results of all the main UK business surveys. The Indices results in this February edition of the BDO Business Trends Report give the January Index numbers, 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	▼	92.3 in January from 93.1 in December
BDO Optimism Index	x	▼	88.9 in January from 90.3 in December
BDO Inflation Index	xx	▲	100.4 in January from 99.3 in December
BDO Employment Index	x	▲	95.1 in January from 93.0 in December

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

KEY FINDINGS

Business conditions remain challenging in the short term, as the BDO Output Index fell back to 92.3 in January, from a December reading of 93.1. This leaves the Index still below the 95.0 level that points to positive growth three months down the line, suggesting that 2013 will get off to a shaky start. The first estimate of UK output in Q4 2012 showed a quarter on quarter contraction of 0.3%, as broadly indicated by the Output Index readings earlier in the year.

Optimism among UK companies took a knock in January as the BDO Optimism Index fell back to its lowest reading since the index began in 1992. A reading of 88.9 was reached, down from December's level of 90.3. The Output Index points to the economic outlook for six months down the line and as such the latest results suggest that fragile conditions will continue well into 2013. This decrease was driven by service sector firms as optimism among manufacturers rose to its highest in nine months. With consumers still facing real income erosions, export growth under pressure from recession in the eurozone and government austerity yet to take full effect, plenty of downside risks still remain for the UK economy.

There were signs that some inflationary pressures are returning for UK businesses, as the BDO Inflation Index climbed to a four month high of 100.4 in January, up from a previous reading of 99.3. UK manufacturers experienced very low cost inflation for physical inputs in 2012, alongside slowing levels of global demand growth. However, the world economy is expected to pick up in 2013, which could provide upward pressure on commodity prices. In addition, consumer price inflation remains elevated above the Bank of England's target rate, pushed up by increases in the cost of home energy provision.

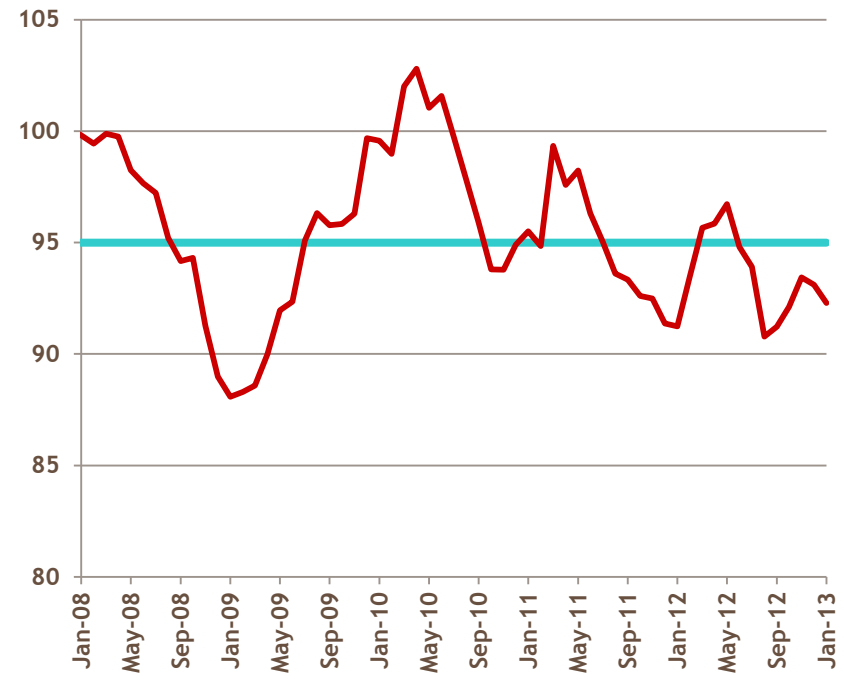
Despite the continued weakness in output growth, the latest BDO Employment Index results suggest that UK businesses are raising their hiring intentions. The Index stood at 95.1 in January, up from a previous reading of 93.0 and the highest reading since April 2012. These index results come alongside the latest figures from the UK labour market, which showed the unemployment rate falling back to 7.7%, down from 7.9%. Encouragingly, the latest employment increase came largely from full-time jobs. However, there are further public sector job cuts planned for the coming year and pay growth remains very low, so real income growth remains elusive for most households.

PRESSURE REMAINS ON BUSINESSES AS OUTPUT INDEX SLIDES BACK

- Short term business prospects weakened again in January, as the BDO Output Index declined to a reading of 92.3 from 93.1 the previous month.
- This takes the Index further away from the 95.0 level that indicates an output expansion three months down the line, suggesting that conditions are likely to remain tough across the first quarter of 2013.
- The latest figures from the Office for National Statistics showed the UK economy contracting in Q4 2012 at the quarter-on-quarter rate of 0.3%.
- Although this decline was driven in part by the distorting factor of an extended period of shutdown for maintenance at the North Sea's largest oil field, it serves to highlight the on-going sluggish recovery of the UK economy.
- This Q4 decline was indicated by the Output Index, which showed particularly low readings across August and September.
- The increase in the Index since then suggests that growth in Q1 2013 will still be weak, but not as much as at the end of 2012.
- Within the headline figure, the Output Index for manufacturers climbed to 92.3 from 90.6 and fell back to 92.3 from 93.8 among service sector firms.

BDO OUTPUT INDEX

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



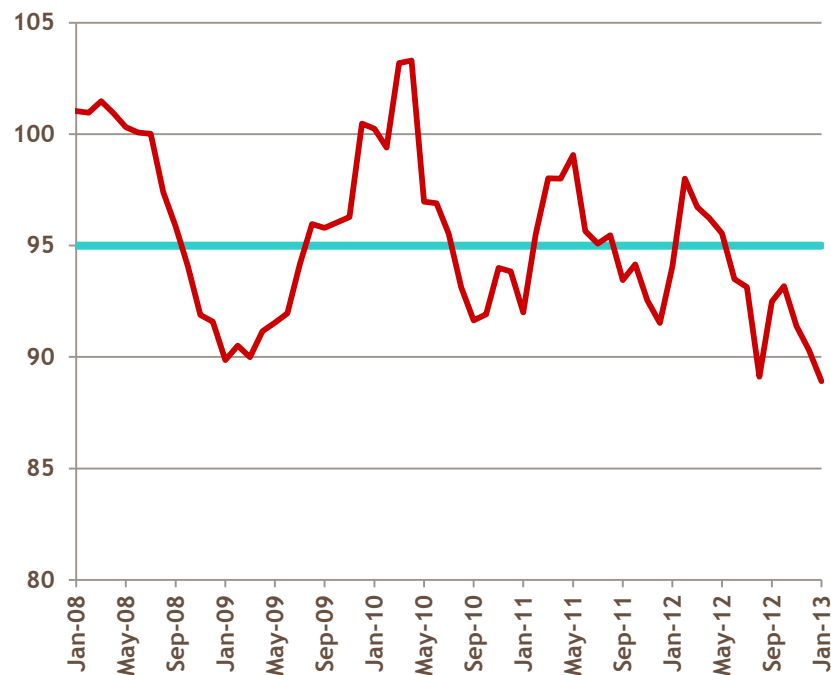
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

CONFIDENCE RECEDES AGAIN SUGGESTING CONTINUED WEAK ECONOMIC OUTLOOK

- Business confidence continued to slide back in January, as the BDO Optimism fell back for the third consecutive month to stand at 88.9.
- This is down from a previous reading of 90.3 and is the weakest confidence level recorded since the Optimism Index began in 1992.
- This is the eighth consecutive month that the Index has stood beneath the 95.0 mark that indicates negative growth in six months time, highlighting the continued fragility in the UK economy.
- With consumers continuing to face real income erosions, government austerity yet to take full effect and export growth weighed down by the recession-engulfed eurozone, there remain major challenges to the economic outlook.
- The latest findings suggest that the UK is unlikely to return to a sounder business environment until at least mid-2013.
- Within the headline figure, the Optimism Index for Manufacturers rose to 95.2, its highest since April 2012.
- However, optimism among service sector firms, with make up three quarters of the economy, fell back to 87.3, down from a previous reading of 89.9.

BDO OPTIMISM INDEX

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



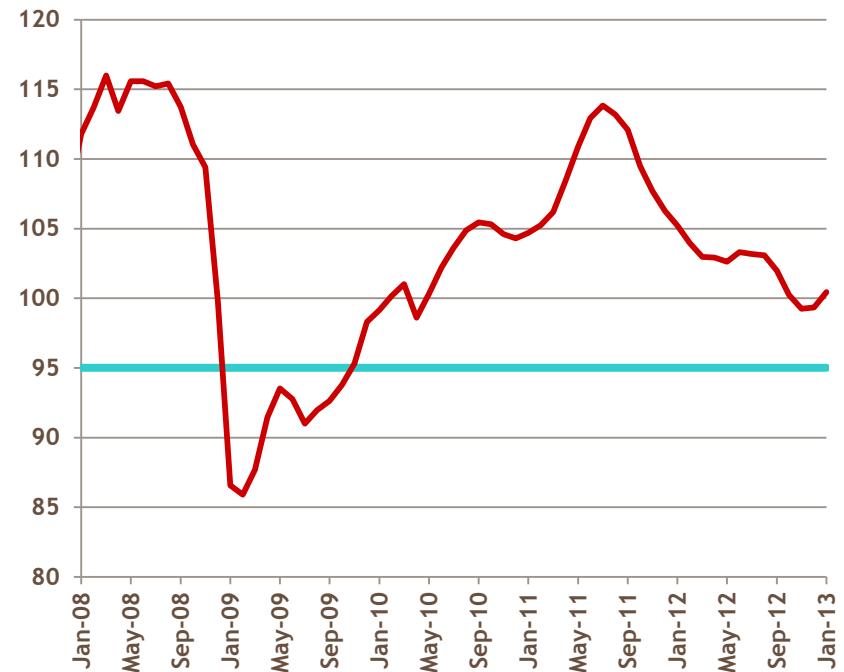
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

INFLATIONARY PRESSURES PICK UP SLIGHTLY

- Inflationary expectations started to pick again up in January, as the BDO Inflation Index climbed to 100.4.
- This is up from 99.3 in December and is the highest reading since September, suggesting that inflationary pressures are beginning to creep up.
- UK manufacturers have been experiencing weak cost inflation from their physical inputs over the past year; the last time that annual input price inflation was notably over 1.0% was March 2012.
- This is in part due to a global economic slowdown over 2012, dampening levels of demand.
- However the world economy is expected to grow slightly faster in 2013.
- Higher input price inflation is likely as a result, reflecting higher business expectations for inflation.
- In addition, consumer price inflation remains persistently above the Bank of England's target rate, standing on hold at 2.7% for the third consecutive month in December.
- On the upside, the inflation index remains much lower than the recent peak in mid-2011.

BDO INFLATION INDEX

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



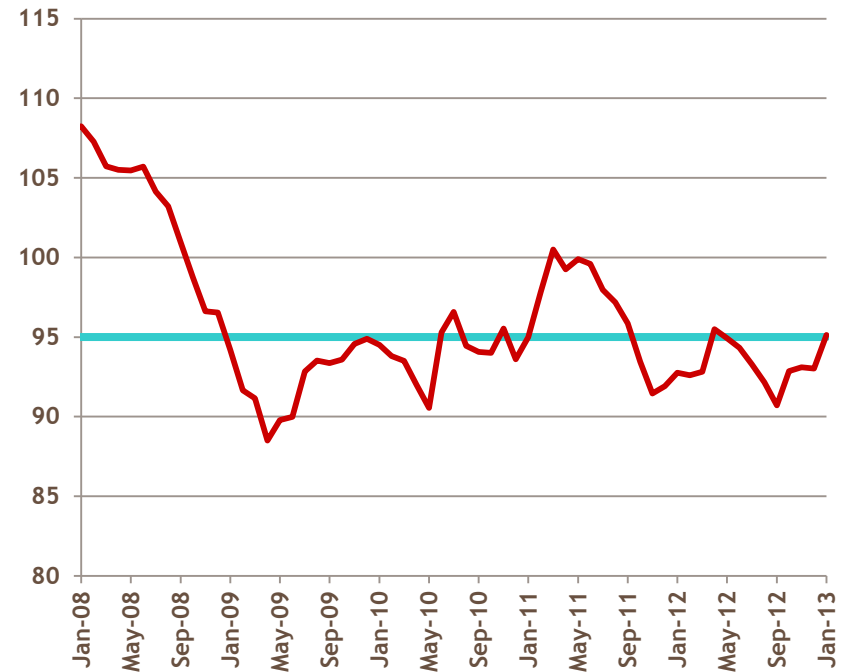
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

BUSINESSES HIRING RISES AS UNEMPLOYMENT FALLS TO 7.7%

- There are signs that businesses are raising their intentions to hire, as the BDO Employment Index rose to its highest level in January since April 2012.
- A reading of 95.1 was recorded, reaching just above the 95.0 mark that points to growing staffing numbers for the first time in 9 months.
- This finding comes as the latest labour market figures show the unemployment rate fell back to 7.7% in the three months to November, down from 7.9% in the previous quarter.
- In addition, the latest increase in employment was driven entirely by full-time work. The number of people in full-time employment rose by 113,000 on the quarter, while the number of those in part-time roles fell by 23,000.
- This movement helped to reduce the share of those only working part-time because they were unable to find a full-time role to its lowest since the three months to December 2011.
- However, the weak economy continues to hold back earnings growth. Total earnings, including bonuses, rose year on year by just 1.4% in the private sector in November, well below the rate of 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

		Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec	Jan
The BDO Optimism Index	Total	94.1	98.0	96.7	96.2	95.5	93.5	93.1	89.1	92.5	93.2	91.4	90.3	88.9
	Small	93.0	96.9	95.7	95.2	94.5	92.5	92.1	88.1	91.5	92.2	90.4	89.3	87.9
	Large	94.8	98.7	97.5	96.9	96.3	94.2	93.8	89.8	93.2	93.9	92.1	91.0	89.6
	Manuf.	91.3	96.9	94.6	96.5	92.2	83.8	90.5	80.5	90.2	89.2	85.9	91.9	95.2
	Service	94.7	98.3	97.3	96.1	96.4	95.9	93.8	91.3	93.1	94.2	92.8	89.9	87.3
The BDO Output Index	Total	91.2	93.5	95.7	95.8	96.7	94.8	93.9	90.8	91.2	92.1	93.4	93.1	92.3
	Small	89.7	91.9	94.1	94.2	95.1	93.2	92.3	89.3	89.7	90.6	91.9	91.6	90.7
	Large	92.5	94.8	97.0	97.1	98.0	96.1	95.2	92.0	92.5	93.4	94.7	94.4	93.5
	Manuf.	88.6	93.6	95.5	96.6	94.6	90.5	89.2	85.1	87.3	87.0	88.8	90.6	92.3
	Service	91.9	93.5	95.7	95.6	97.3	95.9	95.1	92.2	92.2	93.4	94.6	93.8	92.3
The BDO Inflation Index	Total	105.2	104.0	103.0	102.9	102.6	103.3	103.2	103.1	102.0	100.2	99.2	99.3	100.4
The BDO Employment Index	Total	92.8	92.6	92.8	95.5	94.9	94.3	93.3	92.1	90.7	92.9	93.1	93.0	95.1

FOR FURTHER DETAILS

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METHODOLOGICAL 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; 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.