

▶ A NEW ECONOMY
PUBLICATION

A red watering can is positioned in the upper left quadrant, tilted as if pouring. Four small, round terracotta pots containing various green succulents are scattered across the grey background. A vertical red bar runs down the center of the page, with a diagonal cutout at the top and bottom.

BDO MONTHLY BUSINESS TRENDS INDICES

June 2017

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 July 2017, 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	xx	▼	94.9 in June from 95.4 in May
BDO Optimism Index	✓	▲	102.9 in June from 102.8 in May
BDO Inflation Index	✓	▼	104.8 in June from 105.0 in May
BDO Employment Index	✓✓	▲	103.4 in June from 103.3 in May

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

KEY FINDINGS

In June, the BDO Output Index stood at 94.9, down 0.5 points from May. A reading of 95 represents zero-growth, and it is the first time the Index has indicated an output contraction for four years.

The decline was driven mainly by a service sector slowdown and bodes poorly for UK Q2 GDP growth. Many had been hoping to see a strong and immediate bounce-back following subdued GDP growth of 0.2% in Q2, but disappointing figures across the service sector imply it may be another poor quarter as consumer budgets are increasingly squeezed by falling real incomes.

However, while the service sector posted a decrease in both its Output and Optimism Indices from May to June, manufacturing fared better. Manufacturing Optimism rose to 120.2 in June, its highest level since May 2014. A large improvement in order book levels implies a strong uptick in manufacturing growth may be in the pipeline.

The improvement in manufacturing confidence drove an increase in the BDO Confidence Index to 102.9 over June, up 0.1 points from May. Prospects for UK manufacturers are boosted by the weak pound and the strong performance in European markets, with the Eurozone manufacturing PMI hitting a 74-month high in June according to IHS Markit/CIPS.

The BDO Inflation Index stood at 104.8 in June, down from 105.0 in May but still well above the long-term average. The recent consistency in the BDO Inflation Index indicates there may be little further acceleration in inflation in coming months. The latest data from the Office for National Statistics (ONS) showed that annual Consumer Price Index inflation including owner occupiers' housing costs (CPIH) stood at 2.7% in April.

Looking at the UK labour market, the BDO Employment Index stood at 103.4 in June, up from 103.3 in May to reach its highest level since March 2016. The improvement in the Index mirrors ongoing growth in employment seen in recent months, a trend that is likely to continue given strong vacancy levels. Unemployment in the three months to April remained at 4.6%, its lowest level since 1975.

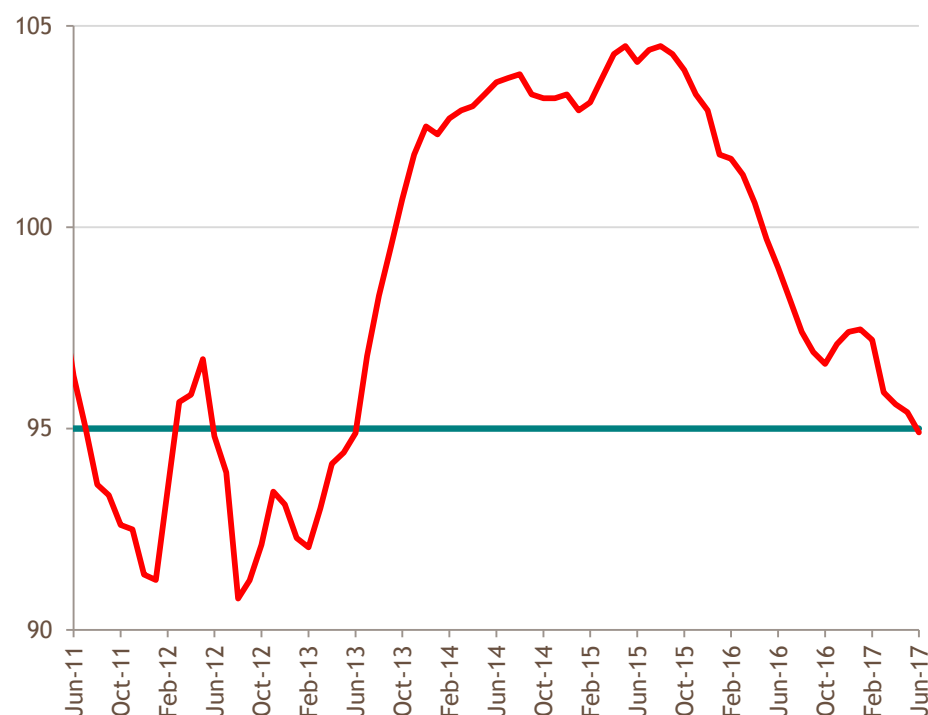
However, wage growth has cooled in recent months. Over the three months to April, annual income growth (excluding bonuses) was just 1.7%, its weakest level since the three months to January 2015. The combination of slowing income growth and high inflation is causing negative knock-on effects across the UK economy, from the deteriorating services sector to the falling retail sales.

SERVICES SECTOR IN CONTRACTION AS CONSUMERS COME UNDER PRESSURE

- The BDO Output Index stood at 94.9 in June, down from 95.4 in May.
- The fall was driven by declines in the Output Indices for both manufacturing and services. While manufacturing fell by just 0.1 points to 97.6, the services sector reading dropped from 95.0 to 94.4.
- The low reading in the BDO Services Output Index reflects a raft of disappointing data for the sector. UK GDP growth stood at a revised 0.2% over Q1, due to broad-based downward revisions within the service sector.
- In particular, consumer-dependent industries have suffered with inflation eroding household budgets. Over April, transport, storage and communication contracted 0.7% whilst business services grew by a modest 0.2% monthly. The index of services rose by just 0.2% monthly in April, within which key sectors performed especially poorly.
- Amid lower consumer demand, the retail sector is also struggling; in May, retail volumes bought increased by just 0.9% year-on-year, the weakest growth rate since April 2013.
- The fact that the service sector has weakened further this month is perhaps unsurprising given the continued deterioration in real wages, dampening hopes of a Q2 bounce-back.

BDO OUTPUT INDEX

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



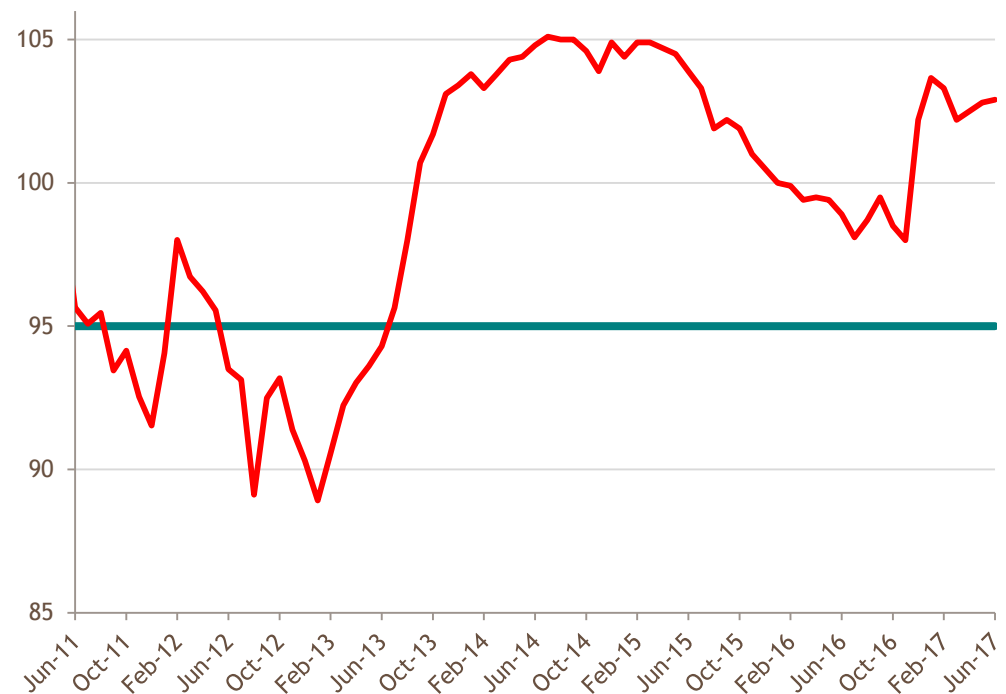
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

MANUFACTURING GROWTH LIKELY AS ORDER BOOKS PICK UP

- The BDO Optimism Index, which assesses firms' order books expectations over the next six months, stood at 102.9 in June, marginally up from 102.8 in May.
- By broad sector, service sector optimism declined in June to 99.6 down from 100.2 in May, with service industries facing tougher business conditions and reduced turnover expectations according to the latest surveys.
- In contrast, manufacturing confidence rose substantially from 116.4 in May to 120.2 in June. The BDO Manufacturing Optimism Index was last higher in May 2014.
- The rise in manufacturing confidence can be attributed to strong export expectations driving an uptick in order book levels. According to the Confederation of British Business (CBI), manufacturing order books are currently at their highest level for 29 years, underpinned by rises in 13 of the 17 sub-sectors, with strong rises in the food, drink & tobacco and chemicals sectors.
- While actual growth has been modest in recent months, the disparity between confidence and output levels in the manufacturing sector implies a significant uptick in output may be in the pipeline as order books feed through.

BDO OPTIMISM INDEX

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



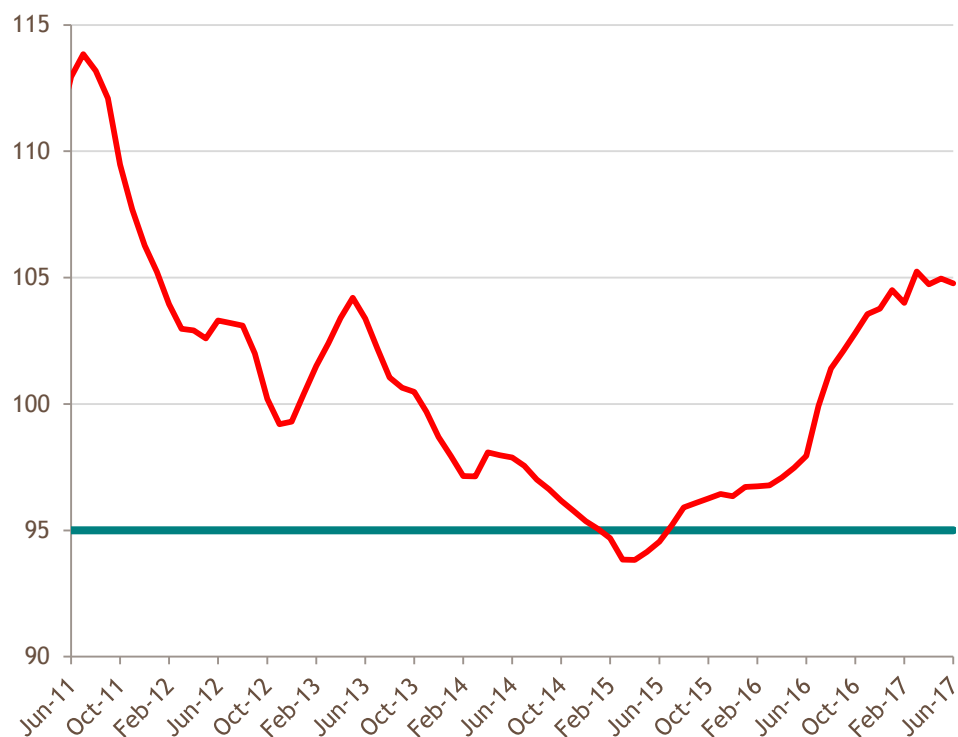
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

DESPITE SLIGHT FALL, INFLATION INDEX REMAINS HIGH

- Over June, the BDO Inflation Index stood at 104.8, down from 105.0 in May.
- The Inflation Index has remained fairly stable over recent months, currently sitting just above its average 2017 reading of 104.7. Yet, June's reading still represents a strong and significant level of inflation. Prior to 2017 the BDO Inflation Index has not been higher since January 2012.
- In the year to May, annual Consumer Price Index inflation including owner occupiers' housing costs (CPIH) stood at 2.7% in April, up from 2.6% in May. The chief drivers of the monthly increase in CPIH were higher prices for clothing, footwear and cultural goods and services.
- Consumer budgets are also being stretched by food prices, which rose by 2.5% in the year to May, the fourth consecutive month of positive food price inflation, after a prolonged period of food price deflation.
- While the current consistency in the BDO Inflation Index implies prices growth is unlikely to accelerate much further in 2017, rising prices for goods and services are significantly hampering the spending power of households, thus pressurising UK businesses.

BDO INFLATION INDEX

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



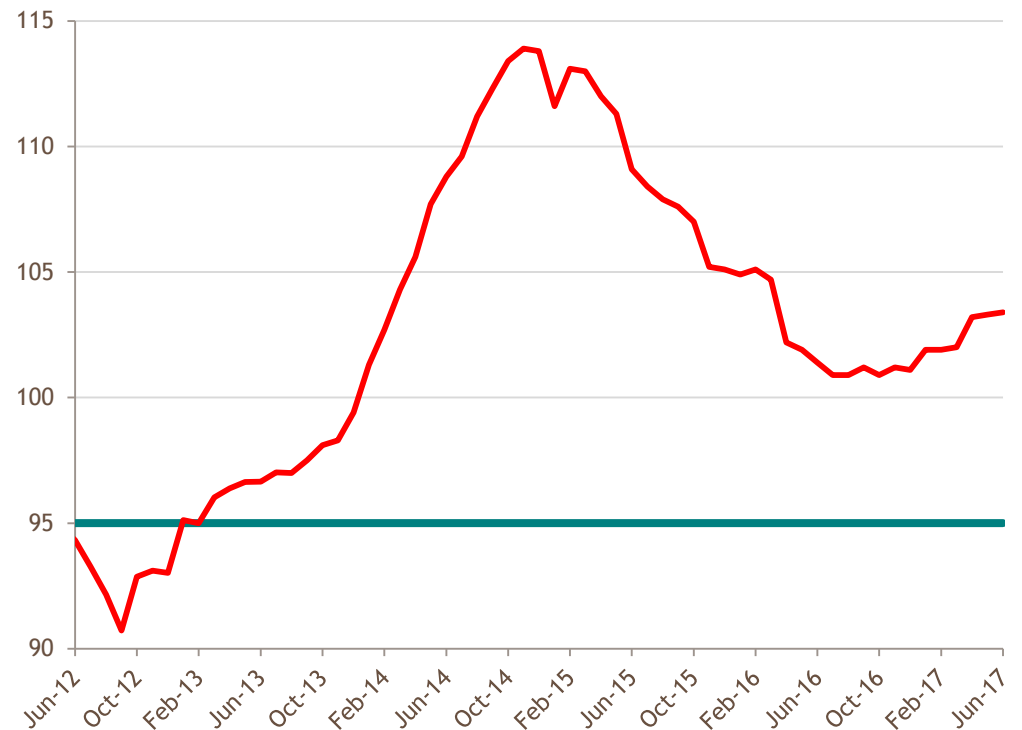
Source: Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

FIRMS CONTINUE HIRING BUT WAGE GROWTH COOLS

- The BDO Employment Index stood at 103.4 in June, a slight 0.1 point rise from May reaching highest level since March 2016.
- The improvement in the Employment Index indicates momentum in the UK labour market has continued over June.
- According to the latest ONS figures, in the three months to April, the share of those aged 16 to 65 stood at a joint-record high of 74.8%, with unemployment at a joint-four-decade low of 4.6%. Given strong vacancy levels, it is likely employment growth will remain robust over 2017.
- However, there remains a disparity between employment expansion and wage growth. Over the three months to April, the average weekly wage of £472 was just 1.7% than in the same period a year earlier, the weakest annual growth since the three months to January 2015.
- Such poor income growth is having a considerable effect across the economy. Household spending, normally a key driver of the UK economy, has faltered in 2017, and much momentum has ebbed from the UK property market.

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

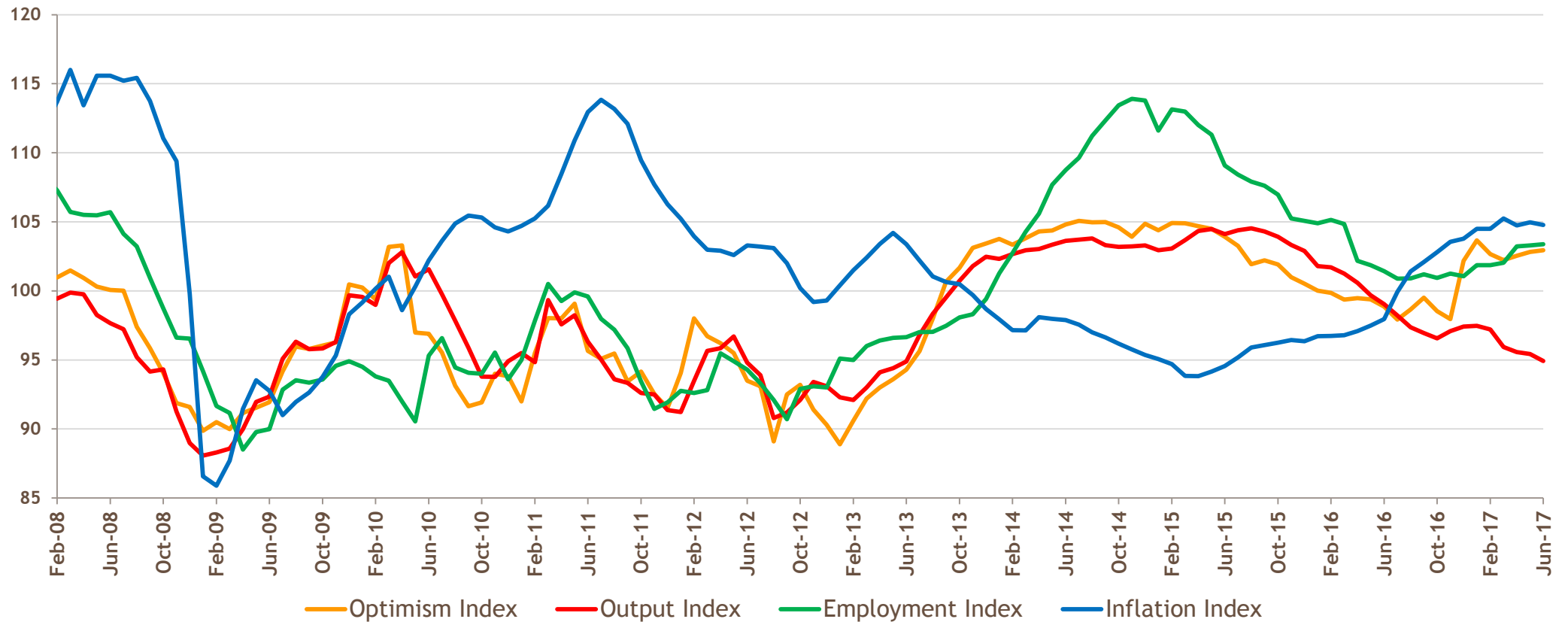
BDO INDICES TO LATEST MONTH

		Mar 2016	Apr 2016	May 2016	Jun 2016	Jul 2016	Aug 2016	Sep 2016	Oct 2016	Nov 2016	Dec 2016	Jan 2017	Feb 2017	March 2017	April 2017	May 2017	June 2017
The BDO Optimism Index	Total	99.4	99.5	99.4	98.9	97.9	98.7	99.5	98.5	98.0	102.2	103.7	103.3	102.2	102.5	102.8	102.9
	Manuf.	87.0	87.3	86.1	83.8	81.0	85.8	91.3	92.0	94.1	99.4	102.2	105.1	110.6	112.2	116.4	120.2
	Service	101.8	101.8	102.0	101.8	101.2	101.2	101.1	99.8	98.7	102.7	103.9	103.0	100.6	100.7	100.2	99.6
The BDO Output Index	Total	101.3	100.6	99.7	99.0	98.2	97.4	96.9	96.6	97.1	97.4	97.5	97.2	95.9	95.6	95.4	94.9
	Manuf.	96.0	94.4	95.9	95.8	95.4	93.9	95.1	94.1	94.9	97.4	96.4	97.7	97.2	97.1	97.7	97.6
	Service	102.3	101.8	100.4	99.7	98.8	98.0	97.3	97.0	97.5	97.4	97.7	97.1	95.7	95.3	95.0	94.4
The BDO Inflation Index	Total	96.8	97.1	97.5	97.9	99.9	101.4	102.1	102.8	103.6	103.8	104.5	104.0	105.2	104.7	105.0	104.8
The BDO Employment Index	Total	104.8	102.2	101.9	101.4	100.9	100.9	101.2	100.9	101.2	101.1	101.9	101.9	102.0	103.2	103.3	103.4

APPENDIX: OUTPUT CONTRACTS BUT PROSPECTS ARE BRIGHTER

BDO 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

FOR FURTHER DETAILS

PETER HEMINGTON

BDO LLP

55 Baker Street, London W1M 1DA

telephone: 020 7486 5888

fax: 020 7487 3686

email: peter.hemington@bdo.co.uk

JACK COY

Centre for Economics and Business Research

Unit 1, 4 Bath Street,

London EC1V 9DX

telephone: 020 7324 2864

email: jcoy@cebr.com

web: www.cebr.com

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 and 95 as the level dividing expansion from contraction.

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.