

BDO MONTHLY BUSINESS TRENDS INDICES

August 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 July, 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	✓✓	▲	96.8 in July from 94.9 in June
BDO Optimism Index	✓✓	▲	95.6 in July from 94.3 in June
BDO Inflation Index	✓	▼	102.2 in July from 103.4 in June
BDO Employment Index	✓✓	▲	97.0 in July from 96.7 in June

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

KEY FINDINGS

Business conditions continued to improve in July, as the BDO Output Index rose significantly to 96.8, up from 94.9 the previous month. The last time the index was higher was in May 2011. These encouraging results dovetail with recent positive economic data which show the UK economy grew by 0.6% over Q2 2013. The BDO Output sub-indices show that the economy is gathering strength across the board. The manufacturing sub-index rose to 98.3 in July, a significant increase on June's reading of 95.7. The all important services sector covers over three quarters of the economy and the sectoral sub-index rose to 96.5 in July, up from 94.7 in June. Both readings are above 95.0, indicating that near-term growth is expected for both these major economic sectors.

Business confidence is continuing to rise, as the BDO Optimism Index reached 95.6 in July, up from 94.3 in June. This is the sixth consecutive monthly increase and the last time the index was higher was in April 2012. Importantly, the index has broken through the 95.0 level which signals expansion. The confidence sub-index for the all-important services sector rose to 96.6 in July, up from 95.5 in June. The manufacturing confidence sub-index increased to 91.4 in July, up from a previous reading of 89.0. However, manufacturers still face significant risks, meaning the confidence measure remains subdued relative to their output measure. In particular, manufacturing exporters are struggling against weak demand from the Eurozone market where the unemployment rate held steady at a record high of 12.1% in June 2013. Manufacturers also came under pressure from input price rises of 4.2% over the year to June 2013, up from increases of 1.8% over the year to May.

Despite the cost pressures being faced by manufacturers, overall inflation expectations for business input prices eased slightly in July. The index recorded a reading of 102.2 in July, down from 103.4 in June. Weak pay growth is pulling down wages in real terms, allowing labour-hungry services firms to control their costs. Resource-hungry manufacturers have been less fortunate as input prices have risen in pound terms over the past year - oil prices alone increased by 4.4% over the year to July in sterling terms. The annual rate of consumer price inflation stood at 2.9% in June 2013, driven up by price rises for motor fuels, clothing and footwear. Combined with very modest wage growth, elevated inflation is continuing to squeeze consumers' living standards.

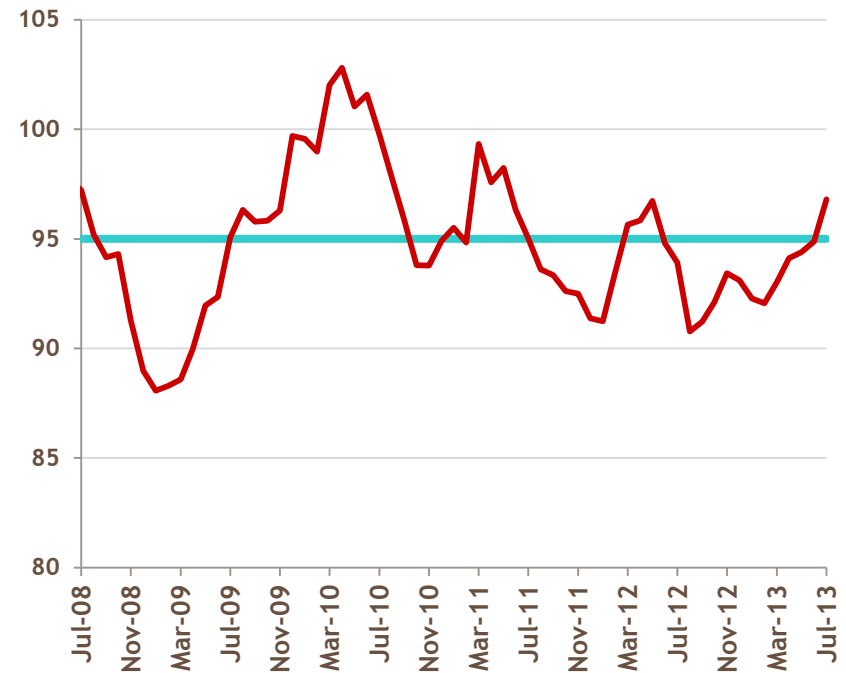
Hiring expectations increased modestly over July as the BDO Employment Index rose to 97.0 in July, up from 96.7 the previous month. This has continued an upward trend in hiring intentions which has been in evidence since late 2012. Reflecting this, the number of employees over March to May 2013 was 1.3% - or 313,000 jobs - higher than over the same period of 2012. However, on a more cautious note, the percentage of people who are economically inactive rose over the three months to May 2013 compared with the three months to February - signalling that some of the unemployed are becoming discouraged and simply giving up on their search for work. Employment has held up remarkably well given weak economic growth in the recent past. The cost of this has been falling real wages. Over the year to the three months to May 2013, regular pay rose by just 1.0% - well below the rate of inflation.

OUTPUT INDEX RISES SHARPLY

- Business conditions continued to improve in July, as the BDO Output Index rose significantly to 96.8, up from 94.9 the previous month.
- The last time the index was higher was in May 2011.
- These encouraging results dovetail with recent positive economic data which show the UK economy grew by 0.6% over Q2 2013.
- The BDO Output sub-indices show that the economy is gathering strength across the board.
- The manufacturing sub-index rose to 98.3 in July, a significant increase on June's reading of 95.7.
- The all important services sector covers over three quarters of the economy and the sectoral sub-index rose to 96.5 in July, up from 94.7 in June.
- Both readings are above 95.0, indicating that near-term growth is expected for both these major economic sectors.
- These data indicate that the UK's recovery is gathering speed and that the economy is likely to accelerate further in the third quarter of 2013.

BDO OUTPUT INDEX

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



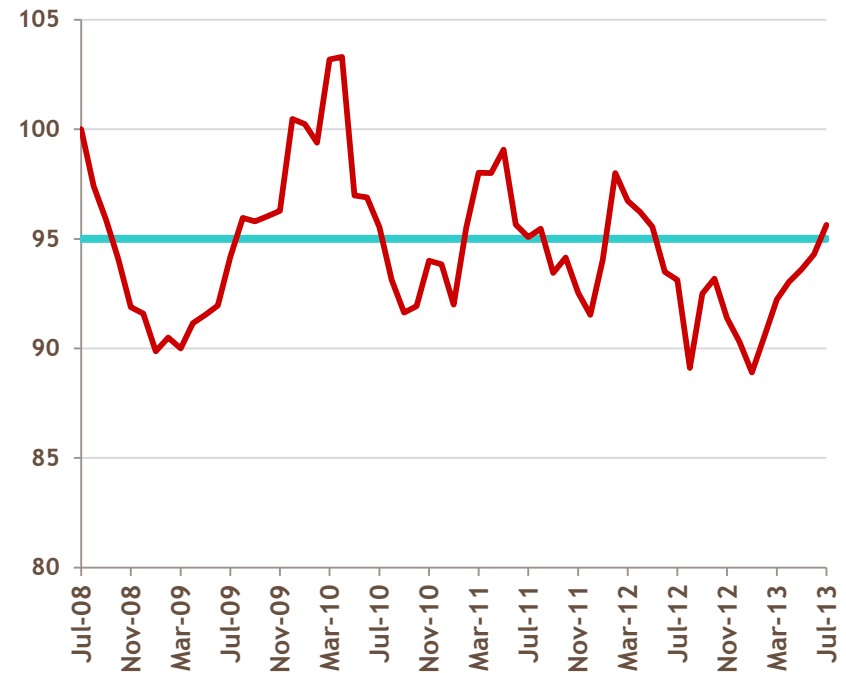
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

BUSINESS OPTIMISM PASSES CRUCIAL MILESTONE

- In line with improving business conditions and accelerating economic growth business confidence is continuing to rise, as the BDO Optimism Index reached 95.6 in July, up from 94.3.
- The index has just surpassed the 95.0 mark, signalling expansion six months down the line.
- The index has now been improving for six months and is at its highest level since April 2012.
- Confidence rose in both major economic sectors. For the all-important services sector, the confidence sub-index rose to 96.6 in July, up from 95.5 in June. The manufacturing sector confidence sub-index increased to 91.4 in July, up from a previous reading of 89.0.
- Manufacturing confidence remains subdued relative to the sector's output measure because of the ongoing challenges manufacturers face. Manufacturing exporters are having to battle against weak demand from the Eurozone and most manufacturers are having their margins squeezed by fast-rising input prices which rose by 4.2% over the year to June.
- Slowing economic growth in China and other major developing economies is also acting as a drag on demand for UK manufactured exports.

BDO OPTIMISM INDEX

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



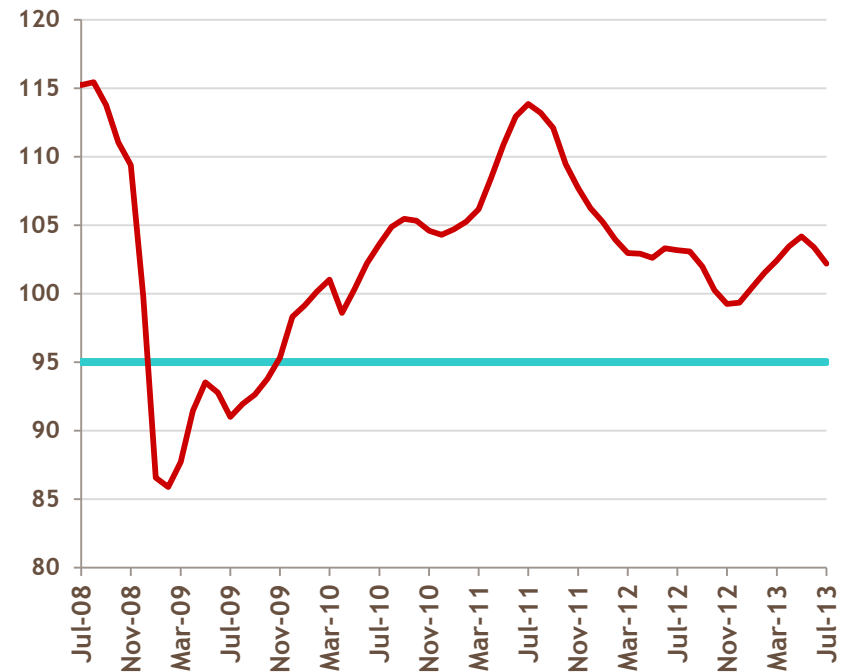
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

INFLATION INDEX CONTINUES TO DECLINE

- The BDO Inflation Index continued to decline in July - the second consecutive fall since a recent peak in May.
- The index recorded a reading of 102.2 in July, down from 103.4 in June. This indicates that near term inflation expectations are coming down from recent highs.
- The fall in the index was driven by weak pay growth, leading to declining wages in real terms. This has helped labour-hungry services firms control costs.
- By contrast, materials-hungry manufacturers have come under cost pressure.
- However, the input cost growth manufacturers will face may come in lower than expected. Oil prices may come down over the medium term as capacity increases and emerging markets slow. The development of exploitation of new hydrocarbon resources though fracking in the developed world may compound this.
- The prices of other inputs could also come down over the next two or three years as emerging market demand slackens amid slow economic growth.

BDO INFLATION INDEX

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



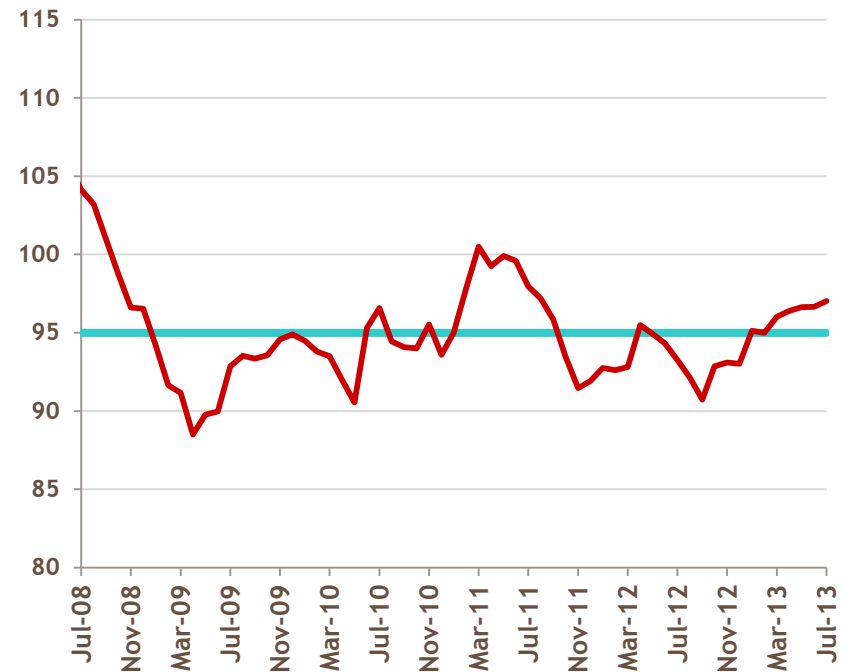
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

PRIVATE SECTOR HIRING INTENTIONS CONTINUE ON UPWARD PATH

- The BDO Employment Index rose modestly to 97.0 in July, up from 96.7 in June. Hiring intentions have continued on an upward trend which has been in evidence since September 2012.
- This dovetails with the 1.3% - or 313,000 - more jobs over March to May 2013 than during the same period in the preceding year.
- The fly in the ointment is that the percentage of economically inactive people rose over the three months to May 2013 compared with the three months to February. This signals that some of the unemployed are simply giving up on their search for work.
- Employment has held up well given weak economic growth in the recent past. Because the economy was struggling, this was only possible with declining productivity and real wages.
- Over the year to the three months to May 2013, total pay, which includes bonus payments, rose by just 1.7%. This is well below the rate of consumer price inflation and means real incomes are declining.

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

		July 2012	Aug 2012	Sept 2012	Oct 2012	Nov 2012	Dec 2012	Jan 2013	Feb 2013	Mar 2013	Apr 2013	May 2013	June 2013	July 2013
The BDO Optimism Index	Total	93.1	89.1	92.5	93.2	91.4	90.3	88.9	90.6	92.2	93.0	93.6	94.3	95.6
	Manuf.	90.5	80.5	90.2	89.2	85.9	91.9	95.2	94.5	88.2	88.3	88.5	89.0	91.4
	Service	93.8	91.3	93.1	94.2	92.8	89.9	87.3	89.6	93.2	94.1	94.8	95.5	96.6
The BDO Output Index	Total	93.9	90.8	91.2	92.1	93.4	93.1	92.3	92.1	93.0	94.1	94.4	94.9	96.8
	Manuf.	89.2	85.1	87.3	87.0	88.8	90.6	92.3	94.1	92.4	90.8	93.7	95.7	98.3
	Service	95.1	92.2	92.2	93.4	94.6	93.8	92.3	91.5	93.2	94.9	94.4	94.7	96.5
The BDO Inflation Index	Total	103.2	103.1	102.0	100.2	99.2	99.3	100.4	101.5	102.4	103.4	104.2	103.4	102.2
The BDO Employment Index	Total	93.3	92.1	90.7	92.9	93.1	93.0	95.1	95.0	96.0	96.4	96.6	96.7	97.0

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

CHARLES DAVIS, ROB HARBRON OR DANIEL SOLOMON

Centre for Economics and Business Research,
Unit 1, 4 Bath Street,
London EC1V 9DX

telephone: 020 7324 2850

email:

cdavis@cebr.com / rharbron@cebr.com / dsolomon@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, 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.