

BDO MONTHLY BUSINESS TRENDS INDICES

April 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 March edition of the BDO Business Trends Report give the February 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	▲	93.0 in March from 92.1 in February
BDO Optimism Index	x	▲	92.2 in March from 90.6 in February
BDO Inflation Index	✓	▲	102.4 in March from 101.5 in February
BDO Employment Index	✓✓	▲	96.0 in March from 95.0 in February

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

KEY FINDINGS

The BDO Output Index rose to 93.0 in March, up from 92.1 in February. While this improvement is notable and welcome, the index level is still low, continuing to stand below the 95.0 mark that indicates positive growth in three months' time and suggesting that robust business conditions will remain elusive. The Index rose to 93.2 for services firms, up from 91.5 in February. This is a welcome sign, as services constitute roughly three quarters of total output. By contrast, the Output Index stood at 92.4 for manufacturers in March, down on February's reading of 94.1, still signalling contraction in three months' time.

Businesses confidence amongst UK firms continued to improve in March, as the BDO Optimism Index rose to 92.2. This is up on February's Index reading of 90.6 is the highest reading since October 2012. However, confidence amongst manufacturers fell markedly, to 88.2 in March from 94.5 in February. Manufacturers have been impacted by a challenging export climate, as the UK's main trading partner, the Eurozone, struggles with the ongoing financial crisis. Recent sterling depreciation has pushed up the cost of manufacturing inputs while real wages have continued to fall, constraining consumer spending. By contrast, confidence amongst services firms rose to 93.2 in March up from 89.6 in February. The last time confidence was higher amongst services firms was in October 2012.

Business cost inflation is becoming more of a concern for UK firms as the BDO Inflation Index climbed to 102.4 in March, up from a February reading of 101.5. The last time the Index was higher was in August 2012. The fall in sterling against the dollar is keeping the cost of crude oil high, raising the cost of many inputs. Nevertheless, wage growth remains slow, limiting employee-related cost rises for all types of business. For consumers, the headline rate of annual inflation rose to 2.8% in February, up from 2.7% in January, remaining above the Bank of England's 2.0% target. Rising household energy bills, petrol and air transport costs contributed to the rise in inflation.

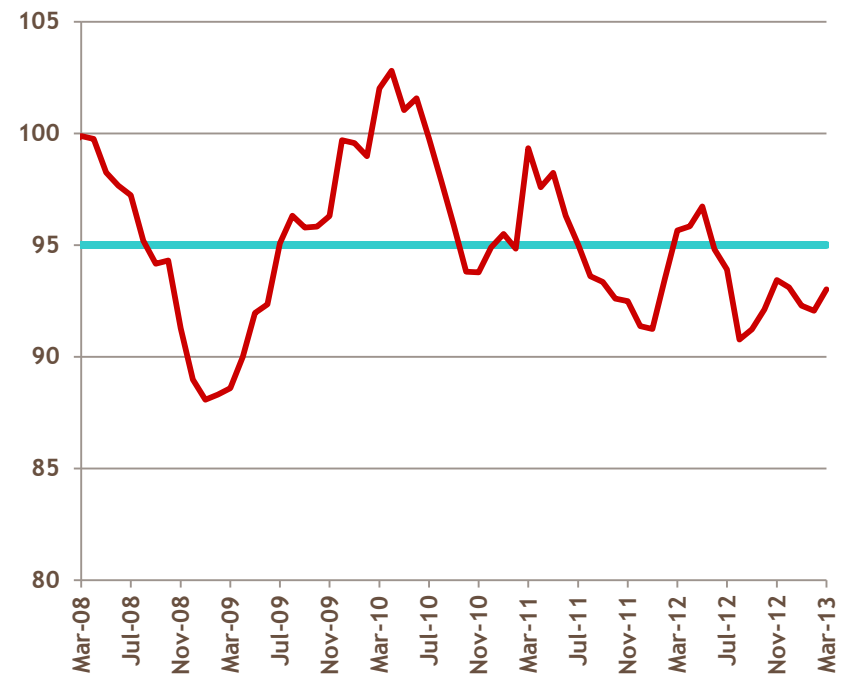
The BDO Employment Index stood at 96.0 in March, up from 95.0 in February. Crucially, the Employment Index now stands above the 95.0 level, suggesting that private sector employment will rise over the next three months. The last time the Employment Index was higher was in August 2011, so March's reading is a 19-month high. The UK unemployment rate stood at 7.8% over the three months to January, 0.5 percentage points lower than a year earlier. Total employment increased by 590,000 over the same period. The March Employment Index reading suggests firms could act to bring the unemployment rate down further over the next three months. Acting in the opposite direction, scheduled public sector headcount reductions mean private sector job creation must continue at a decent pace to prevent rises in the unemployment rate.

OUTPUT INDEX UP FOR FIRST TIME IN THREE MONTHS

- The three-month business outlook was up in March, as the BDO Output Index rose to a reading of 93.0, up from 92.1 in February.
- The index has been on a downward trend since November, so the March uptick represents the first increase since then.
- Nevertheless, the Index has now been below the 95.0 level (which indicates output growth in a quarter's time) since June 2012.
- The subdued Index level suggests economic conditions will continue to be tough until at least mid-2013, as the UK economy struggles to grow.
- The March Index level was 93.2 for the services sector, versus 91.5 in February. Services constitutes roughly three quarters of the UK economy, so this is a welcome sign. However, the services sub-Index still remains low, indicating the sector will struggle to expand significantly over the coming quarter.
- This low weak Index reading, combined with weak demand from the UK's key Eurozone export market, Government fiscal austerity and declining real wages which will limit consumer spending power, suggests economic growth will be lacklustre over the first half of 2013.

BDO OUTPUT INDEX

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



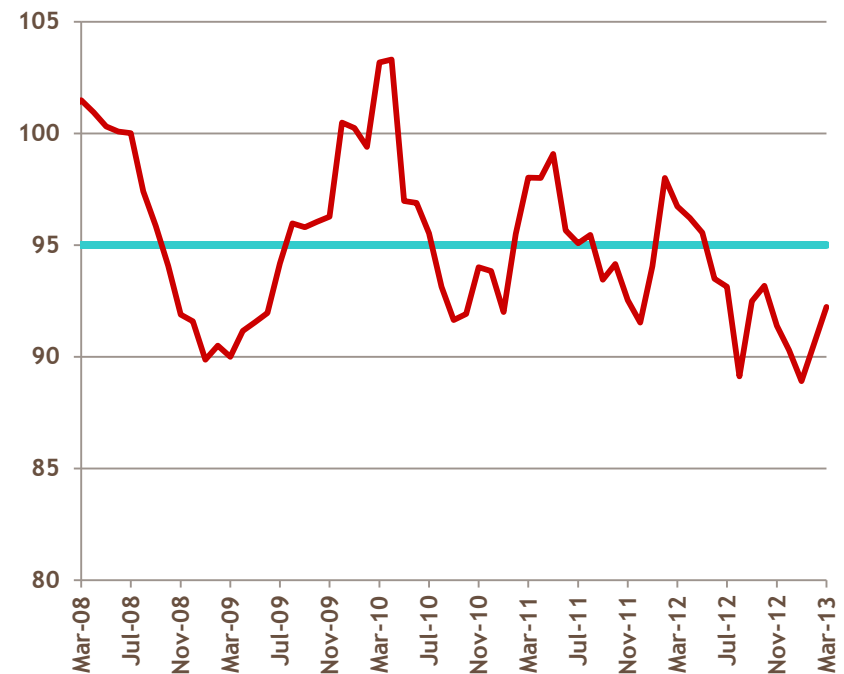
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

CONFIDENCE STRENGTHENS, BUT RISKS REMAIN

- Business confidence rose in March as the BDO Optimism Index reported a reading of 92.2. This is up on February's reading of 90.6 and the Index's all-time low recorded in January.
- The Index is now at its highest level since October 2012.
- Despite this improvement, the Index still remains at a relatively low level and March was the tenth consecutive month in which it recorded a level below 95.0, suggesting strong business growth conditions may still prove elusive six months down the line.
- The Optimism Index rose to 93.2 for the services sector in March, up from 89.6 in February. This sector is the largest chunk of the UK economy, so the pronounced rise in confidence is welcome.
- By contrast, the manufacturing sector Optimism Index fell significantly to 88.2 in March, from 94.5 in February. Sterling has depreciated since January which has raised imported business input costs, particularly in the energy-intensive manufacturing sector. Weak demand from domestic consumers and struggling Eurozone import partners are also likely to be weighing on confidence.

BDO OPTIMISM INDEX

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



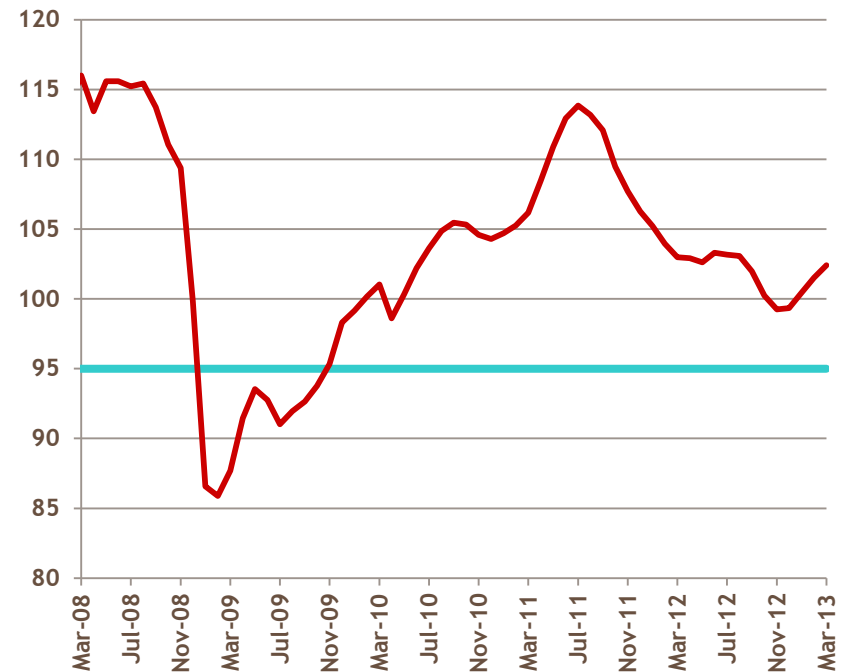
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

INFLATIONARY PRESSURES RISE AGAIN

- The BDO Inflation Index rose to 102.4 in March, up from 101.5 in February. The Index has now risen for four consecutive months and is at its highest level since August 2012.
- This high and rising index reading indicates cost pressures could limit businesses' profits over the coming three months.
- The pound has weakened markedly against the dollar since early January, driven down by the UK's weak growth prospects and loose monetary policy. This has raised import prices feeding into higher business costs.
- Manufacturing firms have been exposed to energy price increases which arose from sterling depreciation and earlier rises in the dollar oil price. February Producer Price Index data showed total manufacturing input prices rose by 2.5% over the year to February 2013, up from 1.9% for the year to January.
- By contrast, wage growth remains weak. Regular pay rose by just 1.2% over the year to the three months to January 2013. Wage growth has been persistently lower than inflation; this has helped to limit increases in business costs.
- Consumer price inflation rose by 0.1 percentage points to 2.8% in January. This was driven by household energy, petrol and air transport prices.

BDO INFLATION INDEX

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



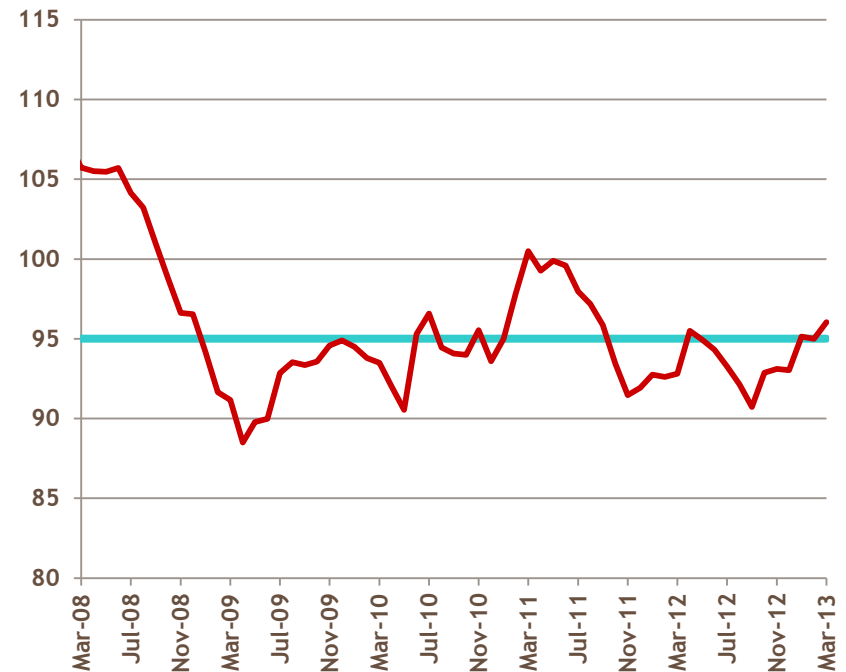
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

HIRING INTENTIONS STRENGTHEN AS EMPLOYMENT INDEX REACHES 19-MONTH HIGH

- Despite weak economic conditions prevailing in early 2013, March's BDO Employment index rose to 96.0. This is up from a reading of 95.0 one month earlier and indicates increased hiring intentions.
- The last time the Employment Index was higher was in August 2011, so March's reading constitutes a 19-month high.
- There were 29.73 million people employed over the three months to January 2013, up 590,000 from a year earlier.
- The UK unemployment rate was 7.8% over November 2012 to January 2013, down 0.5 percentage points on a year earlier. The March Employment Index data indicate businesses could act to bring this down over the coming quarter.
- However, planned public sector payroll cuts will put upward pressure on the unemployment rate over the coming years.
- Weak pay growth is decreasing employee wage costs in real terms. This could act as an incentive for businesses to hire going forward, helping to lower the headline rate of unemployment.

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	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec	Jan	Feb	Mar
The BDO Optimism Index	Total	96.7	96.2	95.5	93.5	93.1	89.1	92.5	93.2	91.4	90.3	88.9	90.6	92.2
	Small	95.7	95.2	94.5	92.5	92.1	88.1	91.5	92.2	90.4	89.3	87.9	89.6	91.2
	Large	97.5	96.9	96.3	94.2	93.8	89.8	93.2	93.9	92.1	91.0	89.6	91.3	92.9
	Manuf.	94.6	96.5	92.2	83.8	90.5	80.5	90.2	89.2	85.9	91.9	95.2	94.5	88.2
	Service	97.3	96.1	96.4	95.9	93.8	91.3	93.1	94.2	92.8	89.9	87.3	89.6	93.2
The BDO Output Index	Total	95.7	95.8	96.7	94.8	93.9	90.8	91.2	92.1	93.4	93.1	92.3	92.1	93.0
	Small	94.1	94.2	95.1	93.2	92.3	89.3	89.7	90.6	91.9	91.6	90.7	90.5	91.5
	Large	97.0	97.1	98.0	96.1	95.2	92.0	92.5	93.4	94.7	94.4	93.5	93.3	94.3
	Manuf.	95.5	96.6	94.6	90.5	89.2	85.1	87.3	87.0	88.8	90.6	92.3	94.1	92.4
	Service	95.7	95.6	97.3	95.9	95.1	92.2	92.2	93.4	94.6	93.8	92.3	91.5	93.2
The BDO Inflation Index	Total	103.0	102.9	102.6	103.3	103.2	103.1	102.0	100.2	99.2	99.3	100.4	101.5	102.4
The BDO Employment Index	Total	92.8	95.5	94.9	94.3	93.3	92.1	90.7	92.9	93.1	93.0	95.1	95.0	96.0

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

ROB HARBRON OR CHARLES DAVIS

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

telephone: 020 7324 2850

email:
rharbron@cebr.com
cdavis@cebr.com

web: www.cebr.com

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 Markit/CIPS Manufacturing and Services PMI data; 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.