

▶ A NEW ECONOMY
PUBLICATION

A red watering can is positioned in the upper left quadrant, tilted as if pouring. Below it, four small, round, terracotta pots containing various types of green succulents are arranged on a grey surface. 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

March 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 March 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	x		97.2 in February from 97.5 in January
BDO Optimism Index	✓✓		103.3 in February from 103.7 in January
BDO Inflation Index	✓✓		104 in February from 104.5 in January
BDO Employment Index	✓	-	101.9 in February from 101.9 in January

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

The BDO Output Index fell slightly to 97.2 in February 2017 having stood at 97.5 in January. While manufacturing posted a monthly rise of 1.3 points to 97.7, a fall in output in the proportionally larger services sector, from 97.7 to 97.1 in February, was enough to decrease the headline Output Index figure.

Manufacturing ended 2016 on a high note, helping an upward revision to UK quarterly GDP growth. UK GDP grew by 0.7% in the fourth quarter, above the 0.6% quarterly growth posted in both Q2 and Q3. Consequently, manufacturing confidence reaches its highest level since April 2015 this month. However, total confidence according to BDO's Optimism Index fell back 0.4 points to 103.3 in February, weighed down by a fall in optimism in the service sector. Yet, optimism stands above levels posted throughout 2016, with a robust UK performance highlighted by a range of macroeconomic indicators, including a record high employment rate in the fourth quarter of 2016.

The BDO Inflation Index stood at 104.0 in February, down from 104.5 posted in January, but still high. Excluding January, February's inflation reading is the highest figure since May 2013. Producer costs have risen sharply in recent months, due mainly to upward pressure from global oil price and weaker sterling. Consumer Price Index (CPI) inflation rose to 1.8% in January, driven by fuel and food price rises. We predict further increases to inflation, as rising producer costs continue to be passed onto consumers, constraining consumer spending in 2017.

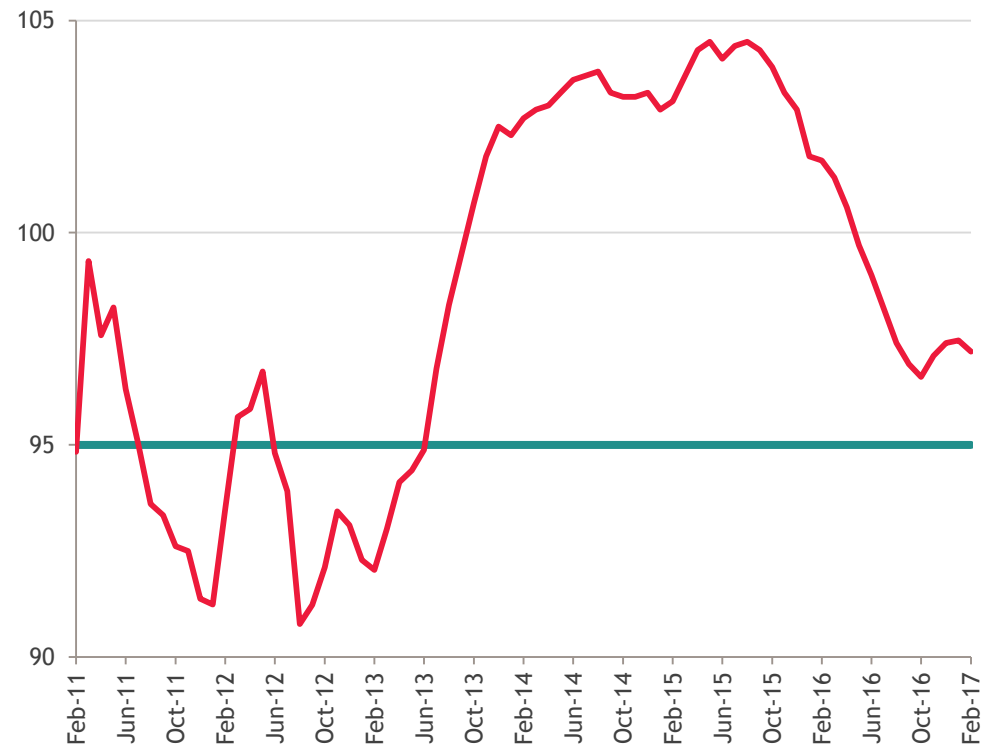
The BDO Employment Index held steady at 101.9 in February, unchanged from previous month to remain at its highest level since May 2016. With the employment rate at its highest level on record (at 74.6%) and the unemployment rate remaining at a low 4.8%, the UK labour market appears in good shape. However, the missing piece of the puzzle is earnings growth, which fell back to 2.6% in Q4 2016. The low rate of unemployment appears to be ineffective in stoking an uptick in earnings growth, as UK productivity fails to make meaningful progress.

OUTPUT INDEX TAKES SMALL STEP BACKWARDS

- Momentum had been building in the BDO Output Index after three months of consecutive increases, but the reading fell back slightly in February. The Index decreased to 97.2, down only marginally from 97.5 in January 2017.
- Despite the fall, short-term economic prospects are still in relatively good shape. Of the two sub-indices, manufacturing output grew from 96.4 to 97.7 in February. In contrast, services output fell from 97.7 to 97.1. These movements are mirrored by changes to the optimism readings for both sectors. With services comprising a greater share of total output, the fall in this sector outweighed rise in manufacturing in February.
- After a slight fall in January, the rise in output is promising for the manufacturing sector. This sub-sector finished last year on a high note, posting 1.2% annual growth in Q4, a key driver of UK production. Particularly strong industries, in terms of output growth remain the automotive and aerospace industries.
- However, long-term pressures on UK producers' input costs are mounting. January saw the sharpest annual increase in prices for imported goods and services since 2013 and higher international oil prices also put upward pressure on producers. Whether the weaker pound can offset this through an export boost remains to be seen.

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

STRONG END TO 2016 SPURS OPTIMISM

- After a stronger than expected end to 2016, the BDO Optimism Index stands at 103.3, a slight fall from 103.7 in January but above levels seen throughout 2016.
- UK GDP quarterly growth was revised up to 0.7% (thanks to a manufacturing boost) in the fourth quarter of 2016, outpacing the 0.6% expansions in both Q2 and Q3. Expansion in the services sector was the main driver of growth in Q4, with consumer-focused industries also faring well.
- The Optimism Index declined slightly in the service sector, 0.9 points to 103 in February, but rose significantly in the manufacturing sector. Manufacturing confidence rose to 105.1 in February, its highest level since April 2016.
- The competitive boost provided by the weaker pound may be acting as a boon to manufacturing confidence.
- Strength in international trade is also likely to improve UK export prospects. Eurozone growth hit a six-year high in February, according to Purchasing Managers' Indices. According to IHS, companies in the Eurozone are hiring workers at the fastest rate in almost a decade, with strong growth in the manufacturing and services industries. In particular, Germany is growing at its fastest rate since 2013.

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 STILL HIGH DESPITE MONTHLY DIP

- The BDO Inflation Index fell slightly to 104.0 in February, down from 104.5 in January.
- Despite the monthly dip, inflation remains considerably higher than levels seen in recent years; February's reading at its second-highest point since May 2013.
- The slight drop in February may be a result of the sharp price rises felt in January. Consumer Price Index (CPI) inflation rose to 1.8% in January, a 0.2 percentage point increase from December, with currency effects feeding through to firms' costs.
- The weaker pound is exerting considerable upward pressure on consumer inflation - prices for imported materials and fuels rose 20.5% annually in the year to January, the highest annual growth since 2008. These translate to higher consumer prices over time.
- Consumers are paying the price for higher international fuel prices at the pump. According to the AA, Brits now pay 18.2p more for a litre of petrol than they did a year ago.

BDO INFLATION INDEX

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



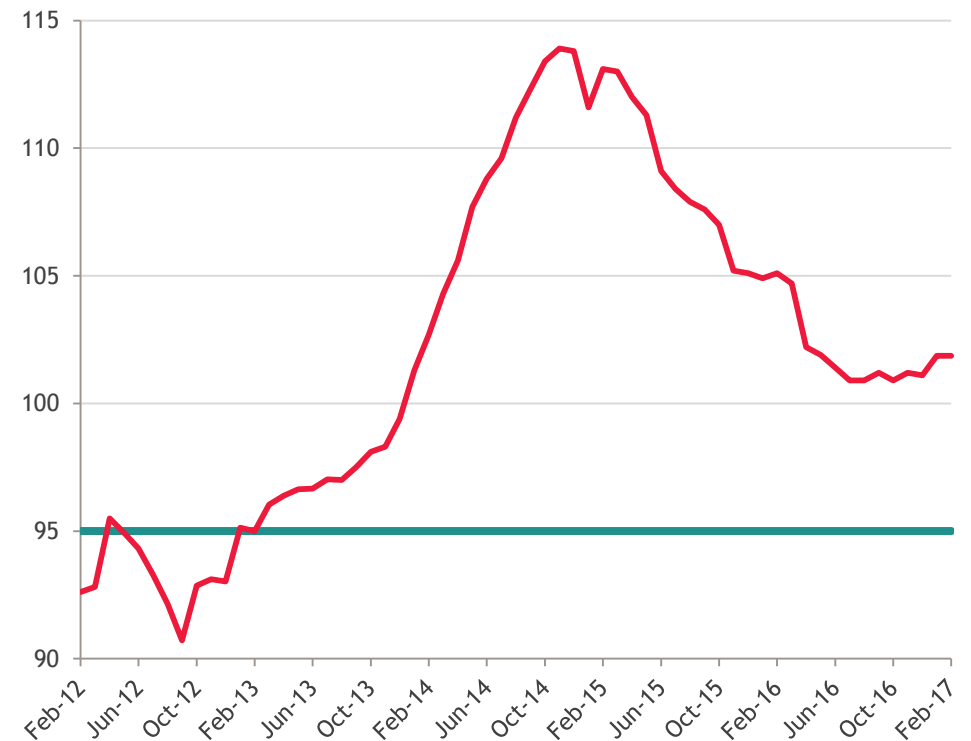
Source: Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

LABOUR MARKET REMAINS SOLID

- The BDO Employment Index stood at 101.9 in February, unchanged from the level posted in January, still at its joint-highest level since May 2016.
- The stability in the Employment Index reflects continued robustness in the UK labour market. In the fourth quarter of 2016, the employment rate (the proportion of people aged 16 to 64 in work) stood at a record high 74.6%. The unemployment remained once again at 4.8%, its lowest level since 2005.
- However, annual earnings growth (including bonuses) decelerated to 2.6% in the three months to December, down 0.2 percentage points from the three months to November. Typically, low unemployment is likely to spur higher earnings growth, but the Bank of England has suggested that unemployment may have to fall further still before an uptick in earnings growth, especially given weak productivity gains.
- Though currently robust, it is possible the job market could weaken in coming months. Cost pressures on businesses and economic uncertainty about the year ahead could cause firms to delay hiring, but vacancy levels increased in the three months to January, showing room to grow in the labour 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

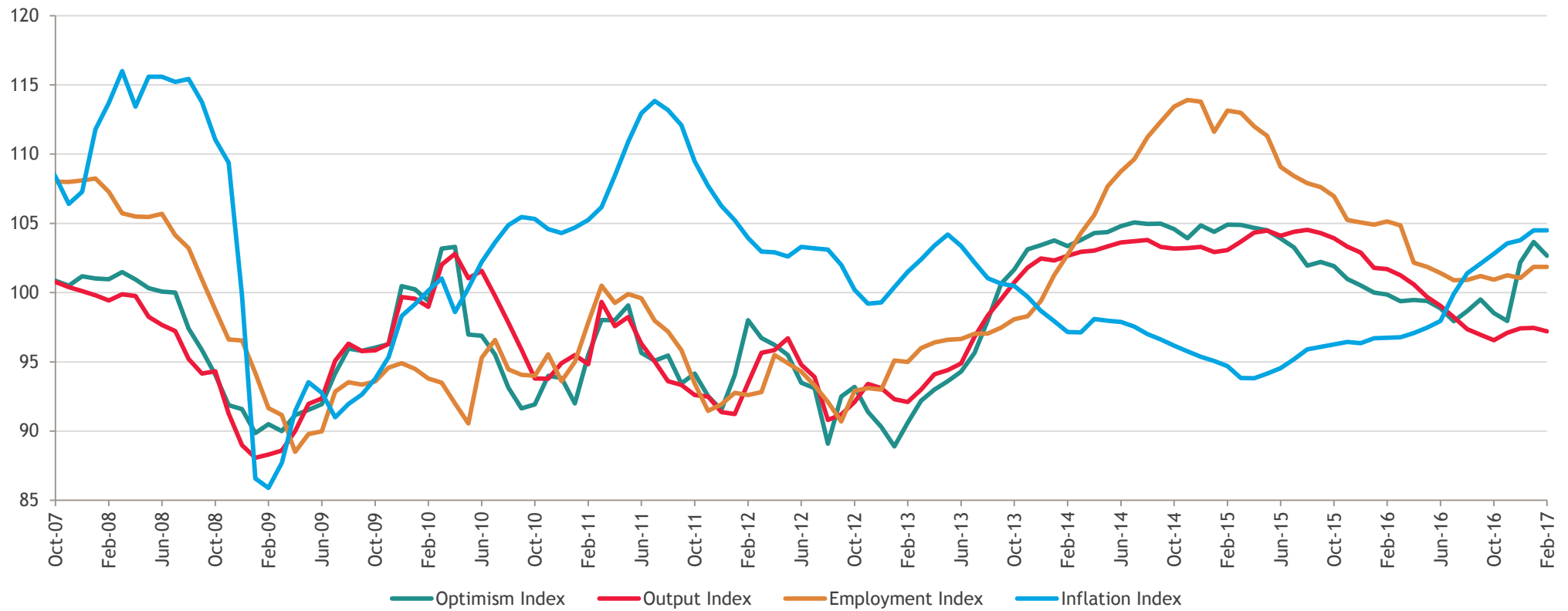
BDO INDICES TO LATEST MONTH

		Jan 2016	Feb 2016	Mar 2016	Apr 2016	May 2016	Jun 2016	Jul 2016	Aug 2016	Sep 2016	Oct 2016	Nov 2016	Dec 2016	Jan 2017	Feb 2017
The BDO Optimism Index	Total	100.0	99.9	99.4	99.5	99.4	98.9	97.9	98.7	99.5	98.5	98.0	102.2	103.7	103.3
	Manuf.	90.2	90.4	87.0	87.3	86.1	83.8	81.0	85.8	91.3	92.0	94.1	99.4	102.2	105.1
	Service	101.9	101.7	101.8	101.8	102.0	101.8	101.2	101.2	101.1	99.8	98.7	102.7	103.9	103
The BDO Output Index	Total	101.8	101.7	101.3	100.6	99.7	99.0	98.2	97.4	96.9	96.6	97.1	97.4	97.5	97.2
	Manuf.	94.7	95.0	96.0	94.4	95.9	95.8	95.4	93.9	95.1	94.1	94.9	97.4	96.4	97.7
	Service	103.2	103.0	102.3	101.8	100.4	99.7	98.8	98.0	97.3	97.0	97.5	97.4	97.7	97.1
The BDO Inflation Index	Total	96.7	96.7	96.8	97.1	97.5	97.9	99.9	101.4	102.1	102.8	103.6	103.8	104.5	104
The BDO Employment Index	Total	104.9	105.1	104.8	102.2	101.9	101.4	100.9	100.9	101.2	100.9	101.2	101.1	101.9	101.9

APPENDIX: OPTIMISM STARTS THE YEAR STRONGLY

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

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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 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.