

BDO MONTHLY BUSINESS TRENDS INDICES

July 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 June, 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	✓✓	▲	94.9 in June from 94.4 in May
BDO Optimism Index	✓✓	▲	94.3 in June from 93.6 in May
BDO Inflation Index	✓	▼	103.4 in June from 104.2 in May
BDO Employment Index	✓✓	▲	96.7 in June from 96.6 in May

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 June, as the BDO Output Index rose to 94.9 from a previous reading of 94.4. This is the fourth consecutive increase and the index now stands at a 12-month high. These encouraging results dovetail with recent positive economic data; official data showed the services sector (which covers over three quarters of the economy) grew by 2.0% year on year in April 2013. This recent sectoral data suggest the UK economy is poised to grow this quarter - building on the 0.3% growth seen in over Q1 2013. The manufacturing sector also supported the economy this quarter, as the manufacturing sub-index rose to 95.7 in June, up from 93.7 in May.

Business confidence is continuing to rise, as the BDO Optimism Index reached 94.3 in June, up from 93.6 in May. This is the fifth consecutive monthly increase and the index now stands at its highest level in over a year. Despite these sustained improvements, the index is still below the 95.0 level which signals expansion in six months time; although the economy has returned to modest growth, risks remain. Slow wage growth and elevated inflation mean that falling household disposable incomes continue to hamper consumer-facing firms in the UK. Moreover, exporters are struggling against a weak demand from the Eurozone market where the unemployment rate reached a new high of 12.1% in May 2013. Finally, the slowing pace of global monetary activism could raise businesses borrowing costs, weighing on profitability.

Inflation expectations for business input prices eased slightly in June, ending a string of six consecutive monthly increases in the inflation index. The index recorded a reading of 103.4 in June, down from 104.2 in May. Weak pay growth means wages are falling in real terms, helping labour-heavy services firms control their costs. Resource-hungry manufacturing firms have not been so lucky; the price of Brent Crude has risen by 7.1% in sterling terms over the year to June 2013. The annual rate of consumer price inflation stood at 2.7% in May 2013, driven up by price rises for transport and clothing. Combined with slow wage growth, above-target inflation means consumers' living standards are being squeezed.

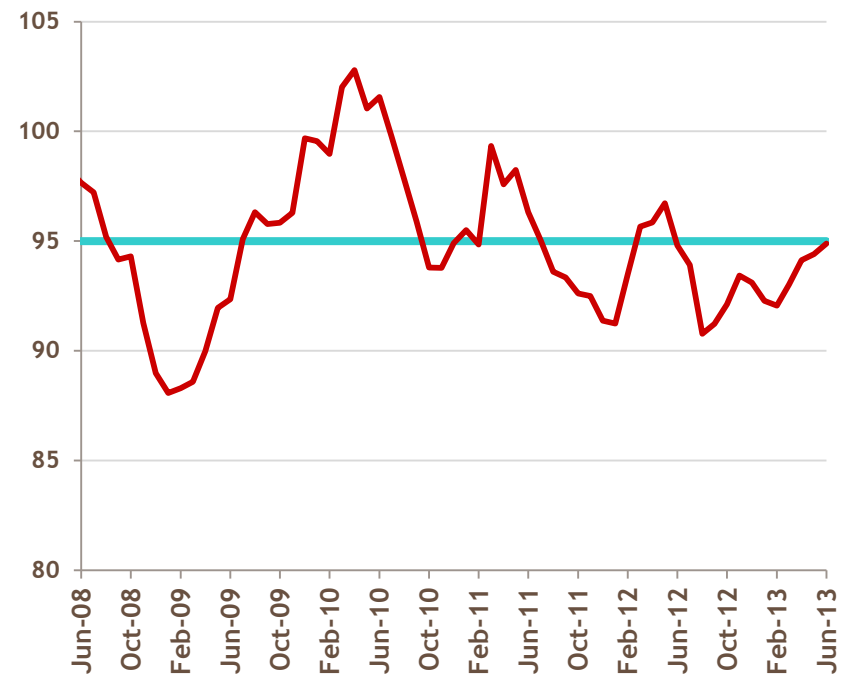
Hiring expectations held broadly steady over June as the BDO Employment Index rose marginally to 96.7, up from 96.6 in May. Hiring intentions have been on a broad upward trend since September 2012. Reflecting this, private sector employment increased by 3.2% - or 740,000 jobs - over the year to Q1 2013. This was more than enough to offset public sector payroll reductions over the period, leading to a net rise in employment. The labour market is holding up relatively well given the weakness of economic growth and potential pitfalls facing the recovery. Consequently, workers have had to endure meagre wage increases. Over the year to the three months to April 2013, regular pay rose by just 0.9%; this is well below the rate of inflation, meaning workers' real incomes are declining.

OUTPUT INDEX REACHES 12-MONTH HIGH

- The BDO Output Index increased to 94.9 in June, from a previous reading of 94.4, to reach a 12-month high.
- The index has now been on a broad upward trend since the start of this year as the economy has begun to return to growth.
- June 2013 is the first month that the index has been broadly at the 95.0 level (a reading above which signals expansion over the coming three months) since June 2012.
- These readings have been supported by the latest official data which indicated the services sector - covering over three quarters of the economy - grew by 2.0% year on year in April 2013.
- This was the fastest rate of services sector growth since January 2012.
- The CIPS/Markit Purchasing Managers' Index (PMI) also showed significant expansion in the manufacturing sector, which grew at its fastest pace for two years in June 2013.
- These data indicate that the UK economy is undergoing a modest recovery and is likely to grow in the third quarter of 2013.

BDO OUTPUT INDEX

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



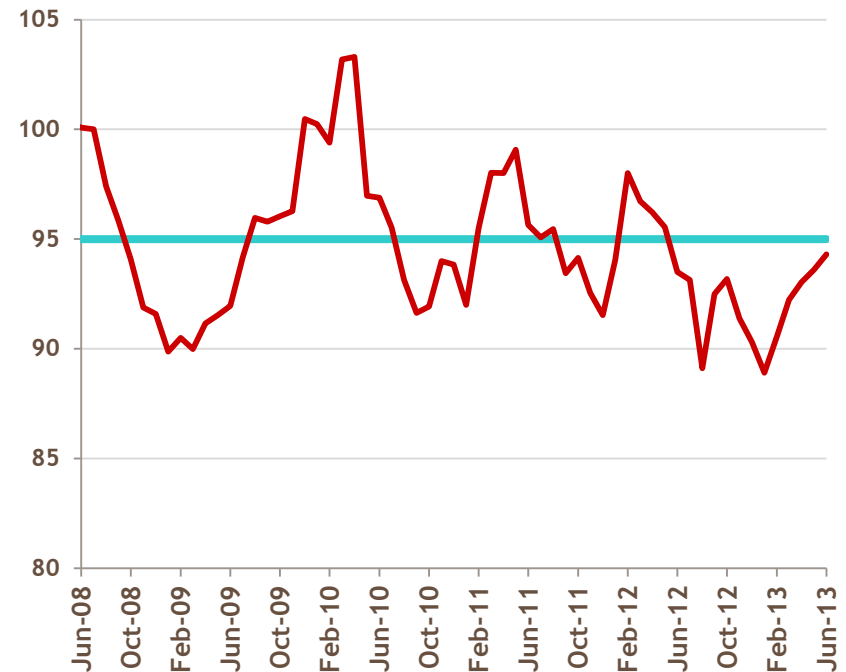
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

BUSINESS OPTIMISM CONTINUES TO RISE

- In line with improving business conditions and output, business confidence is also continuing to rise.
- The BDO Optimism Index reached 94.3 in June, up from 93.6 in May. The index has now increased for five consecutive months and stands at its highest level in over a year.
- Nevertheless, it still stands below the 95.0 level which signals expansion over the near term. Despite modest economic growth, significant risks remain.
- The US Federal Reserve signalled it could “taper” its monetary stimulus measures later this year. The suggestion of tapering has already led to significant declines in global stock indices, weighing on the UK financial sector.
- The slowing pace of global monetary activism could raise businesses borrowing costs, weighing on profitability.
- Real incomes are declining as consumer price inflation is outstripping wage growth. This is causing consumers to cut back on spending, weighing on consumer-focussed businesses.
- UK goods exporters - heavily reliant on the Eurozone market - are struggling as the bloc’s unemployment rate reached a new record high of 12.1% in May 2013.

BDO OPTIMISM INDEX

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



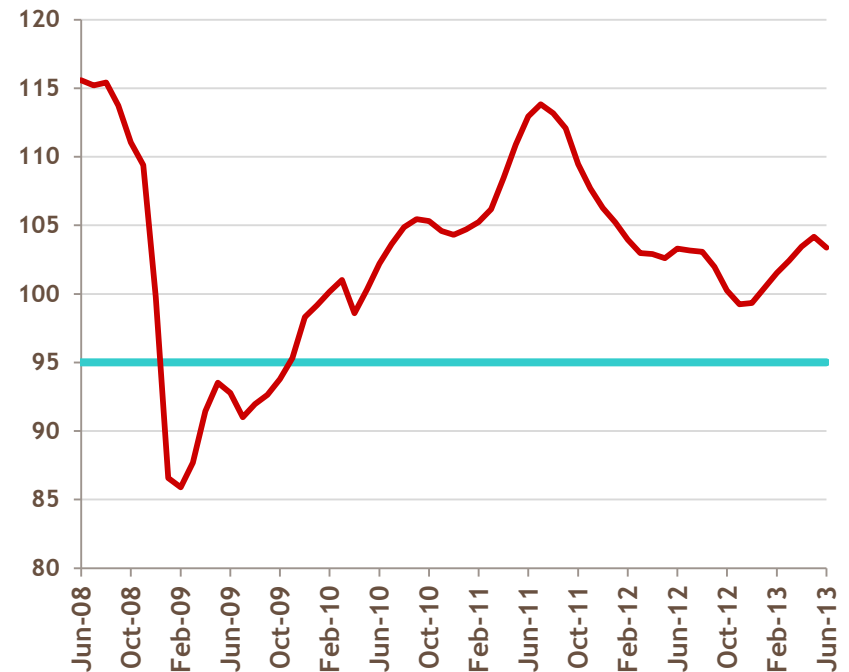
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

INFLATION INDEX COMES OFF RECENT HIGHS

- The BDO Inflation Index eased slightly in June, suggesting that near term inflation expectations are coming down from recent highs.
- The index recorded a reading of 103.4 in June, down from 104.2 in May. This downward movement broke a string of six consecutive monthly increases in the index.
- Regular pay (which excludes bonus payments) increased by just 0.9% over the year to the three months to April 2013. For labour-intensive services businesses, this has helped keep costs under control.
- Manufacturers, which are much more reliant on raw materials inputs, have been more exposed to commodity price increases.
- The price of Brent Crude has risen by 7.1% in sterling terms over the year to June 2013. This has pushed up energy prices - a major headache for energy-intensive manufacturers.
- For consumers, price rises for air transport and clothing led to price inflation of 2.7% over the year to May 2013 - up on 2.4% over the year to April. This inflation rate is noticeably higher than wage growth and is squeezing consumers' living standards.

BDO INFLATION INDEX

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



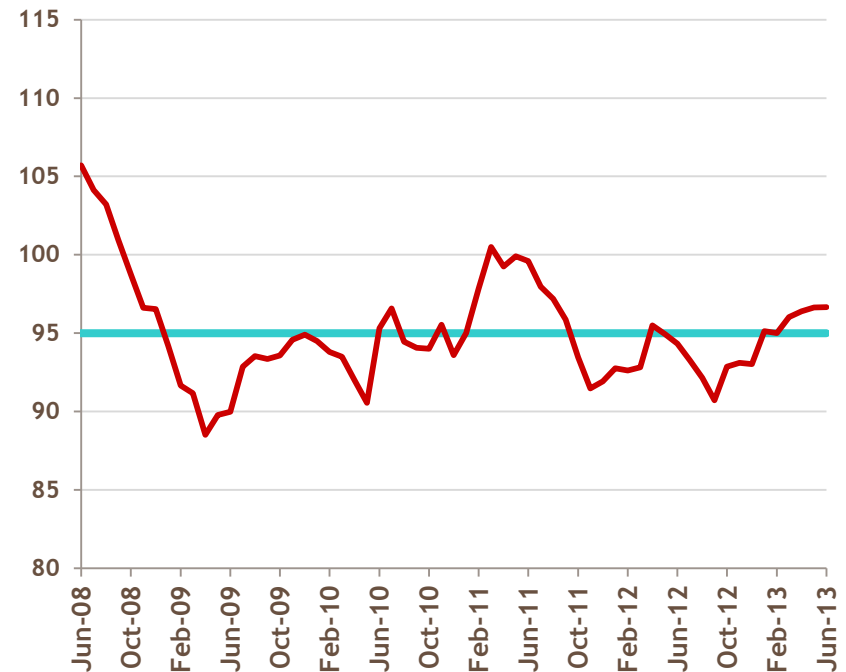
Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat, Office for National Statistics and Cebr analysis

PRIVATE SECTOR HIRING INTENTIONS HOLD STEADY

- The BDO Employment Index rose very slightly to 96.7 in June, up from 96.6 in May. This means that hiring intentions have effectively held steady over the month.
- Hiring intentions have been on a broad upward trend since September 2012. This ties with a 3.2% - or 740,000 jobs - rise in private sector employment over the year to Q1 2013.
- This was more than enough to offset public sector payroll reductions of 308,000, or 5.1% over the same period.
- Consequently, the headline number of workers rose by 432,000 - or 1.5% - over the 12 months to Q1 2013. This indicates the private sector is supporting the labour market in the face of public sector job cuts.
- Considering the slow pace of economic growth in the UK, the labour market is proving remarkably able to provide jobs. The sting in the tail is that productivity has fallen, going hand-in-hand with declining real wages.

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

		June 2012	July 2012	Aug 2012	Sept 2012	Oct 2012	Nov 2012	Dec 2012	Jan 2013	Feb 2013	Mar 2013	Apr 2013	May 2013	June 2013
The BDO Optimism Index	Total	93.5	93.1	89.1	92.5	93.2	91.4	90.3	88.9	90.6	92.2	93.0	93.6	94.3
	Manuf.	83.8	90.5	80.5	90.2	89.2	85.9	91.9	95.2	94.5	88.2	88.3	88.5	89.0
	Service	95.9	93.8	91.3	93.1	94.2	92.8	89.9	87.3	89.6	93.2	94.1	94.8	95.5
The BDO Output Index	Total	94.8	93.9	90.8	91.2	92.1	93.4	93.1	92.3	92.1	93.0	94.1	94.4	94.9
	Manuf.	90.5	89.2	85.1	87.3	87.0	88.8	90.6	92.3	94.1	92.4	90.8	93.7	95.7
	Service	95.9	95.1	92.2	92.2	93.4	94.6	93.8	92.3	91.5	93.2	94.9	94.4	94.7
The BDO Inflation Index	Total	103.3	103.2	103.1	102.0	100.2	99.2	99.3	100.4	101.5	102.4	103.4	104.2	103.4
The BDO Employment Index	Total	94.3	93.3	92.1	90.7	92.9	93.1	93.0	95.1	95.0	96.0	96.4	96.6	96.7

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 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; Markit / 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.