

BDO Monthly Business Trends Indices

August 2011

Introduction

The BDO Monthly Trends Indices are 'polls of polls' that pull together the results of all the main UK business surveys. The August Monthly Indices update the results in the 'BDO Business Trends Report' produced in July 2011. The latest results include new business surveys 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	↓	95.0 in July from 96.3 in June
BDO Optimism Index	x	↓	95.1 in July from 95.6 in June
BDO Inflation Index	✓✓	↑	113.8 in July from 112.9 in June
BDO Employment Index	x	↓	98.0 in July from 99.6 in June

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

Key Findings

The BDO Output Index dropped to 95.0 in July, falling from 96.3 in June. This latest move brings the Index level with the crucial threshold indicating economic expansion, indicating that growth over the next quarter is likely to be very slow. Within this figure, the manufacturing sector showed a contraction on the Output Index for the first time since October 2009, pointing to the tough conditions faced by the sector.

The BDO Optimism Index decreased in July to 95.1, down from June at 95.6, in a further move away from the average trend and broadly level with the important 95.0 mark. Manufacturing optimism remains low after last month's confidence dive but increased marginally to 93.5 in July, from 90.1, suggesting a weak outlook for the manufacturing sector.

The BDO Inflation Index highlights how inflation expectations have continued to grow to a thirty five month high of 113.8 in July, up from 112.9 in June. Despite the recent large dip in the price of oil as markets took a tumble, the cost of inputs remains high, with overall manufacturing input prices growing by 18.5% year-on-year in July according to official Office for National Statistics data. Energy suppliers' planned hikes in the price of electricity and gas in September mean inflation expectations are likely to persist at elevated levels.

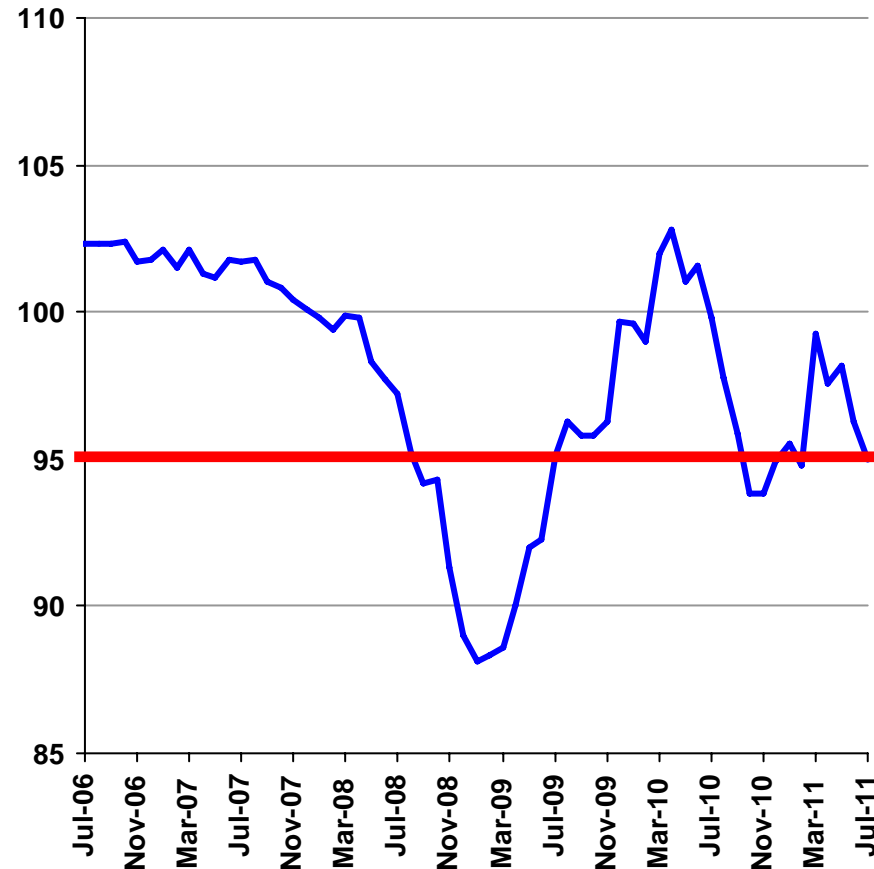
Prospects in the labour market continue to waver beneath long run trend, with the BDO Employment Index falling to 98.0 in July from 99.6 in June, as hiring intentions remain weak in both the manufacturing and services sectors. Reflecting this, pay growth continues to trail annual price inflation, at 2.1% year-on-year for regular pay between March and May; within this figure, manufacturing pay growth is even more fragile at just 1.0% over the same period.

The latest official growth data for the UK economy showed a quarter-on-quarter expansion in Q2 of just 0.2%, consistent with what the BDO Output Index suggested. This weak reading lends further support to the Bank of England's decision to keep rates on hold, despite soaring inflation. A rate rise is now unlikely before Q2 2012 as the Monetary Policy Committee waits for stronger growth figures.

Output Index points to contraction in manufacturing sector

- The BDO Output Index – estimating output over the next quarter – dropped to 95.0 in July 2011 from 96.3 in June, taking the index level with the crucial threshold that indicates positive output growth.
- This is a five-month low for the index, not having dropped beneath the 95.0 since February.
- The services sector continues to demonstrate fragility, as The BDO Output Index for Services fell in July to 95.3 from 96.0 in June – well below the average trend and only just indicating expansion.
- At the same time, the BDO Output Index for Manufacturing implies a contraction in the sector, reaching a low of 93.9 in July – down from 97.6 in June. This is a reading not seen since the depths of the recession in October 2009 and highlights how the manufacturing sector is under pressure from global factors, including supply chain disruptions from the Japanese tsunami, cooling global demand and commodity prices remaining persistently high.

BDO Output Index, 100 = average trend growth. Greater than 95 = positive growth

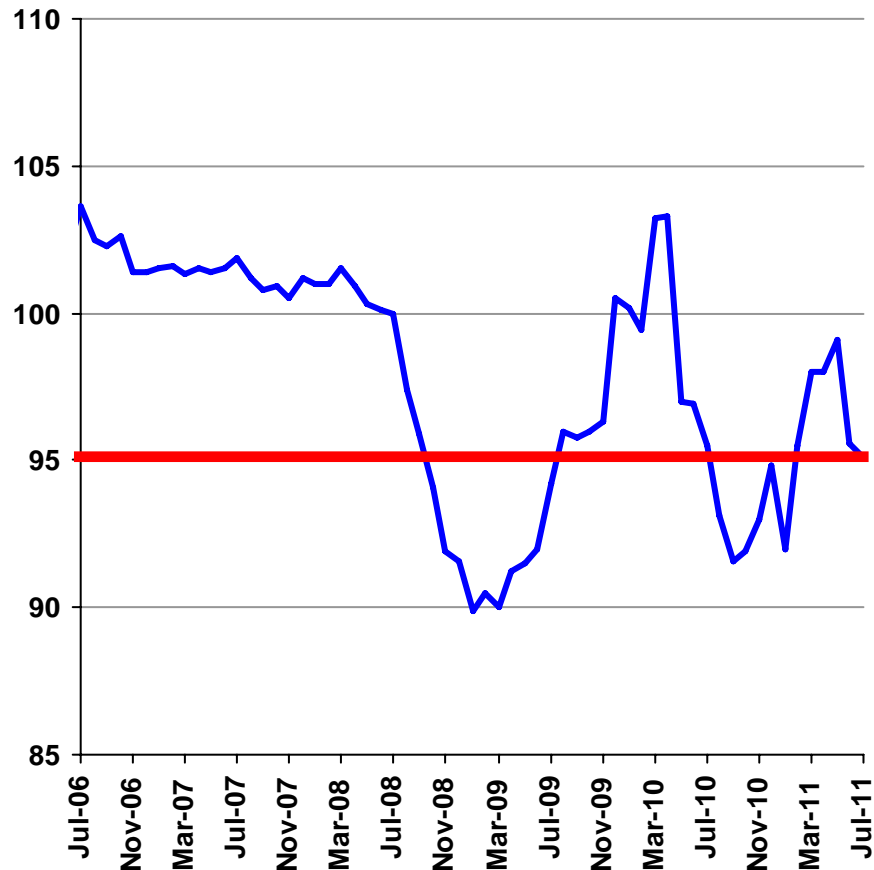


Source: PMI, Bank of England, CBI, Eurostat and the Office for National Statistics

Lowest business optimism levels in six months

- The BDO Optimism Index decreased marginally in July to 95.1, from 95.6 in June, in a further move away from the average trend level.
- This is the lowest confidence reading in six months, and as the index points to output two quarters ahead, suggests the outlook remains weak.
- Optimism in the services sector fell to 95.5 in July, down from 97.0 in June suggesting that growth in the sector remains frail. However despite the fall, this figure is higher than the 2010 average of 95.1.
- The manufacturing sector continues to suffer from blighted confidence, as the BDO Optimism Index for Manufacturing remained below the 95.0 trend level for the second month at 93.5 in July, although saw a rise from 90.1 in June. This is the longest period of below-trend optimism for manufacturing since June-July 2009, demonstrating the current tough conditions faced by the sector.

**BDO Optimism Index, 100 = average trend growth.
Greater than 95 = positive growth**

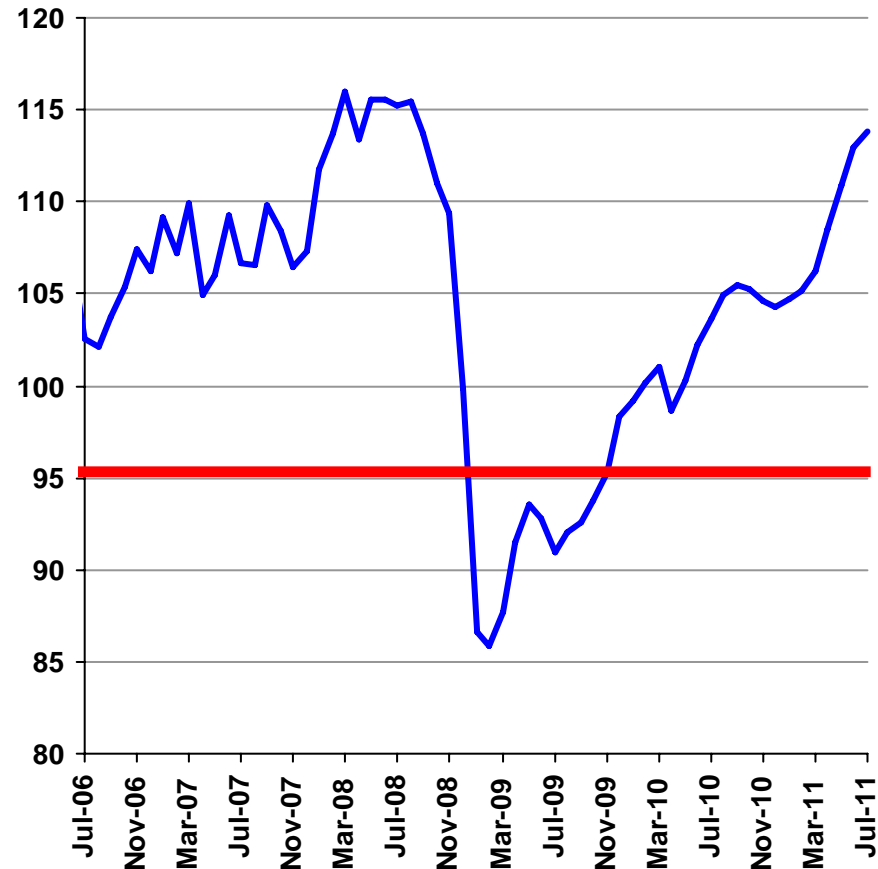


Source: PMI, Bank of England, CBI and the Office for National Statistics

Inflation expectations rise again to reach a thirty-five month high

- Inflationary expectations continue to rise, as the BDO Inflation Index grew again to 113.8 in July from 112.9 in June.
- This is the highest reading on the Index since August 2008, and is 9.9% above the level one year ago.
- Annual consumer price inflation fell back marginally in June to 4.2%, down from the 4.5% seen in April and May. While transport and, especially, fuel costs continue to keep inflation elevated, this decrease was largely due to discounting in the toys and hobbies category.
- Four out of the six large energy suppliers have now announced double-digit percentage price increases for their electricity and gas, due to take effect in September. Utility prices are therefore likely to be a key driver of inflation later in the summer, before inflation falls back in 2012.

BDO Inflation Index, 100 = average trend growth. Greater than 95 = positive growth

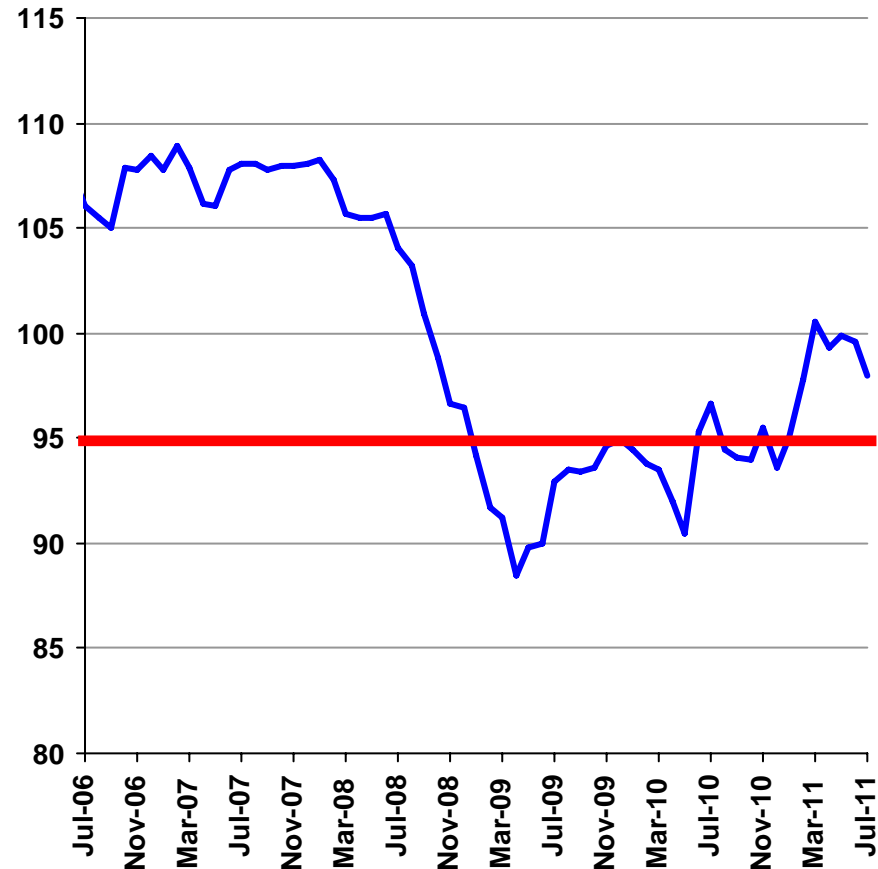


Source: PMI, Bank of England, CBI and the Office for National Statistics

Conditions in the labour market continue to quaver

- The BDO Employment Index shrank to 98.0 in July from 99.6 in June, marking a five month low in the index reading.
- No strong and clear upward or downward trend is emerging for labour market conditions – the Index continues to fluctuate just under the average trend mark.
- The official unemployment rate remains stubbornly high at 7.7% over March-May 2011, and despite the number of those unemployed falling since the previous quarter, the more timely claimant count measure showed dole queues increasing for the fourth consecutive month in June.
- Regular-pay growth remains weak in the whole overall at 2.1% year on year over March – May 2011. However within this figure, pay growth in the manufacturing sector is even weaker, at just 1.0% over the same period. This compares to a stronger 2.5% in the services sector.

BDO Employment Index, 100 = average trend growth. Greater than 95 = positive growth



Source: PMI, Bank of England, CBI and the Office for National Statistics

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BDO Indices to latest month

		Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	June	July
The BDO Optimism Index	Total	93.1	91.6	91.9	94.0	93.8	92.0	95.5	98.0	98.0	99.1	95.6	95.1
	Small	92.1	90.7	90.9	92.0	93.8	91.0	94.5	97.0	96.9	98.0	94.6	94.0
	Large	93.9	92.4	92.7	93.7	95.6	92.7	96.2	98.8	98.8	99.8	96.4	95.8
	Manuf.	101.7	97.7	98.4	99.7	106.6	106.2	116.4	112.7	102.9	97.5	90.1	93.5
	Service	91.0	90.1	90.3	91.3	92.1	88.4	90.3	94.4	96.8	99.5	97.0	95.5
The BDO Output Index	Total	97.8	95.9	93.8	93.8	94.9	95.5	94.8	99.3	97.6	98.2	96.3	95.0
	Small	96.2	94.3	92.2	92.3	93.3	93.9	93.2	97.7	95.9	96.6	94.7	93.4
	Large	99.1	97.2	95.1	95.0	96.2	96.8	96.1	100.7	98.9	99.6	97.6	96.3
	Manuf.	106.7	103.0	99.1	98.8	103.4	104.7	111.4	115.2	111.0	104.9	97.6	93.9
	Service	95.6	94.1	92.5	92.5	92.8	93.3	90.7	95.4	94.2	96.6	96.0	95.3
The BDO Inflation Index	Total	104.9	105.5	105.3	104.6	104.3	104.7	105.2	106.2	108.5	110.9	112.9	113.8
The BDO Employment Index	Total	94.5	94.1	94.0	95.5	93.6	95.0	97.8	100.5	99.3	99.9	99.6	98.0

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For further details

Peter Hemington:

BDO LLP,

55 Baker Street, London W1M 1DA

Telephone: 020 7486 5888

Fax: 020 7487 3686

E-mail peter.hemington@bdo.co.uk

Douglas McWilliams, Charles Davis or Rob Harbron:

The Centre for Economics and Business Research Ltd,

Unit 1, 4 Bath Street, London EC1V 9DX

Telephone: 020 7324 2850

E-mail dmcwilliams@cebr.com, cdavis@cebr.com or rharbron@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 Ltd., 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; and the Chartered Institute of Purchasing and Supply's Surveys of Manufacturing and of Services.

Taken together the surveys cover over 11,000 different respondents from companies employing approximately five million employees. The respondents cover a range of different industries and a range 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.