

Introduction

The BDO Monthly Trends Indices are ‘polls of polls’ that pull together the results of all the main UK business surveys. The January Monthly Indices update the results in the ‘BDO Business Trends Report’ produced in December 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	xx	↓	91.4 in December from 92.5 in November
BDO Optimism Index	xx	↓	91.5 in December from 92.5 in November
BDO Inflation Index	✓	↓	106.3 in December from 107.7 in November
BDO Employment Index	x	↑	91.9 in December from 91.5 in November

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

Key Findings

The BDO Output Index fell for the fourth consecutive month in December, highlighting on-going and worsening economic conditions in the UK. The Index dropped to 91.4 from a reading of 92.5 the previous month, pointing to a growing risk of a return to contraction. Within this headline figure the Index for the manufacturing sector declined to 87.4, a thirty-one month low. More crucially, the Output Index for the larger services sector fell to 92.4 in December, down from 93.5 and remaining for the fifth month beneath the 95.0 mark that points to contraction.

Business confidence resumed its downward trajectory in December, as the BDO Optimism Index slumped to 91.5 from 92.5 the previous month, the lowest reading since April 2009. Subdued confidence levels suggest that economic weakness is likely to continue well into 2012. Optimism among service sector firms dipped to 92.8 in December, the lowest reading since February and remained subdued at 86.6 among manufacturers, with the stumbling Eurozone economy likely to further weigh on confidence.

Persistently tough conditions in the UK labour market remain as the official unemployment rate stands at 8.3%, and the number of unemployed workers continues to rise. The BDO Employment Index highlights this, hovering well below the 95.0 threshold for the third consecutive month at 91.9 in December. The unemployment rate is expected to rise steadily over 2012, as stagnant hiring conditions in the private sector fail to make up for planned job losses in the public sector.

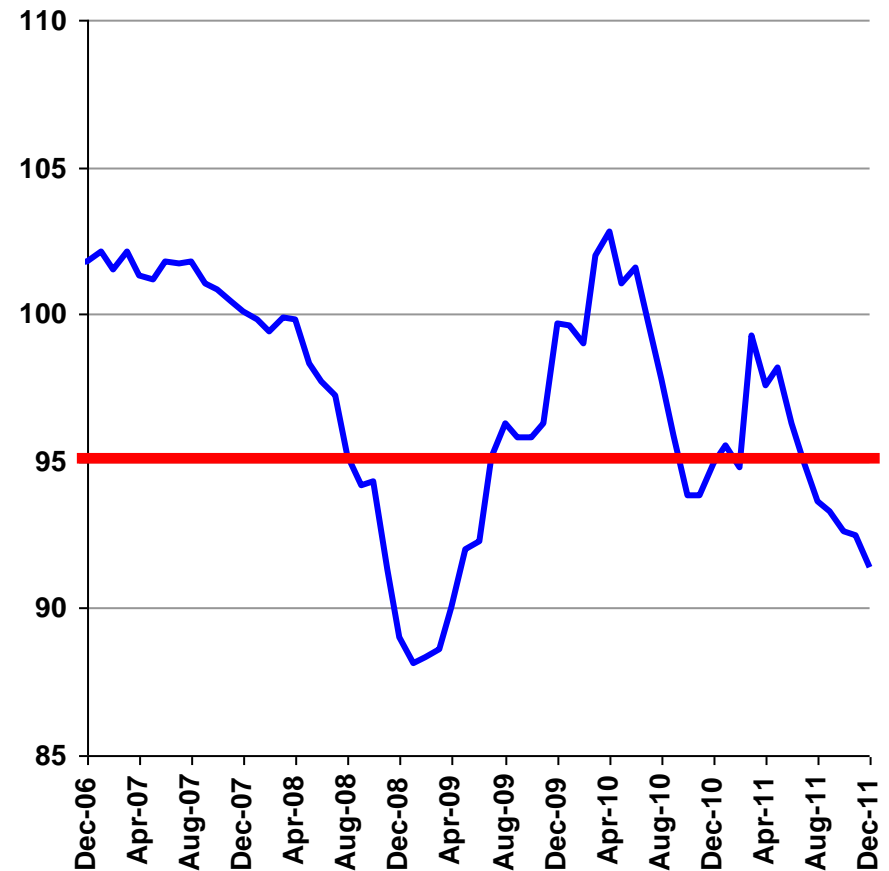
Inflationary pressures continued to slow in December, as the BDO Inflation Expectations Index fell to 106.3 from 107.7 the previous month. Easing commodity prices are helping to drive this and while inflationary pressures are likely to fall further, the stubbornly high price of oil remains a concern.

The coming year will see the UK sailing directly into strong economic headwinds. As the latest BDO Index readings suggest, growth is likely to be only slow for 2012 as a whole, and a real risk of a return to recession remains. Growth in the Eurozone is expected to slump over the next twelve months, acting as a drag on demand in the UK economy, and as such the Bank of England will face increasing calls to expand its program of quantitative easing in the first quarter of 2012.

Output Index slides again as economic headwinds continue

- The BDO Output Index suggests that business conditions are continuing to worsen, as it slid back for the seventh consecutive month in December.
- This latest movement takes the Index to a thirty-two month low with a reading of 91.4, down from 92.5 in November, and below the 95.0 mark that indicates contraction for the fifth month.
- The Output Index for the important Services sector resumed its downward trend in December, falling to 92.4 from 93.5 in November. This is bad news for output growth in the UK overall, as this sector comprises roughly three quarters of the economy.
- The factory sector also remains under pressure, as the Output Index for Manufacturing dropped again in December to 87.4 from 88.7 – its lowest reading in thirty one months.
- These latest readings point to very weak growth in 2012, with a real risk of return to recession.

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

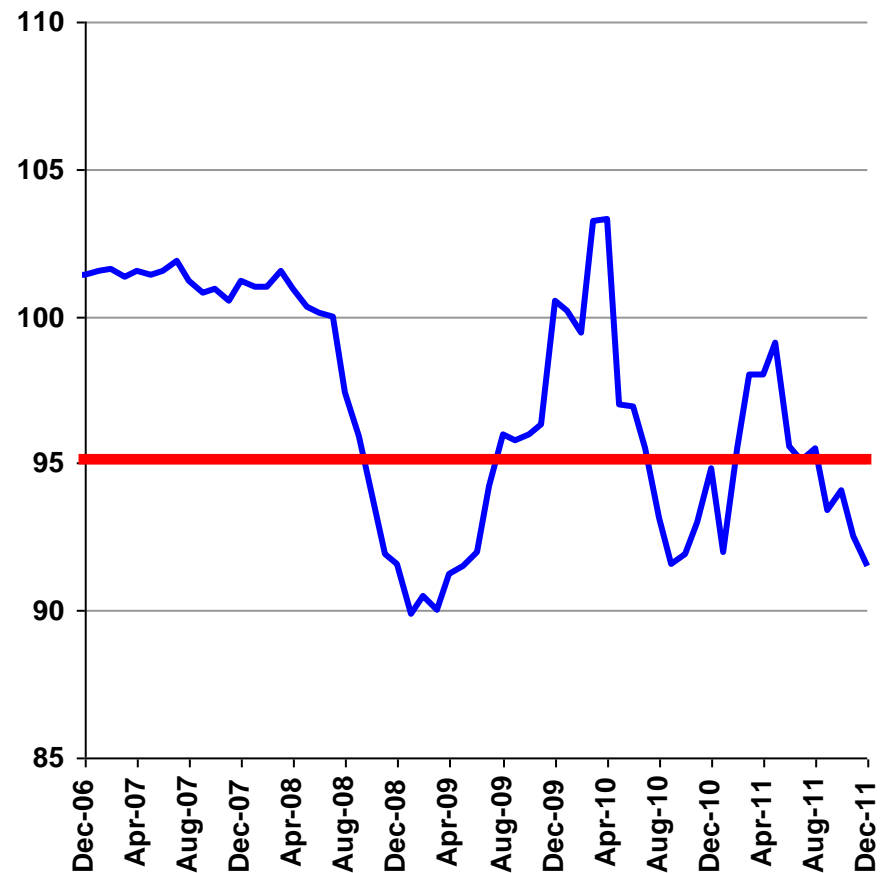


Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat and the Office for National Statistics

Business confidence in 2012 takes a further hit

- The BDO Optimism Index dropped in December to 91.5, down from 92.5 in November and continuing its general downward trajectory since May.
- As the Index points to output growth two quarters ahead, this latest slump in confidence highlights just how fragile economic conditions in the UK are likely to be over the coming year.
- The BDO Optimism Index for Manufacturers remained low in December at 86.6, only marginally from 86.2 the previous month. The Eurozone, which buys roughly half of UK manufacturing exports, is expected to fall back into recession in 2012 and likely to weigh further on confidence in the sector.
- Confidence among service sector firms slipped back again in December, as the BDO Optimism Index continued its sharp downward trend since at 92.8, the index reached its lowest reading since February.

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

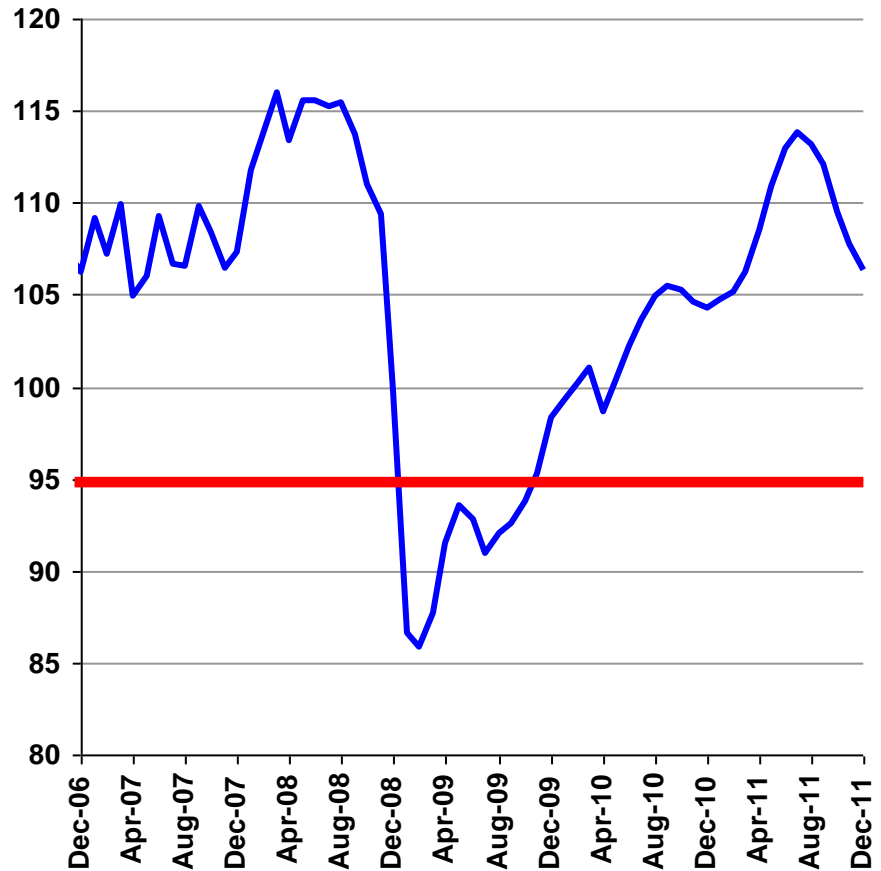


Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat and the Office for National Statistics

Inflationary pressures continue to ease

- Inflation expectations fell back for the fifth consecutive month in December, to 106.3 on the BDO Inflation Index. This is down from 107.7 the previous month, and from a high of 113.8 in July when inflationary pressures peaked.
- Expectations for inflation are now back in line with where they were in February. Easing commodity prices help contribute to lower inflationary pressures for UK businesses, although stubbornly high oil prices remain a concern.
- Annual consumer price inflation slowed again in November to 4.8% down from 5.0% in October, as fuel prices fell and food prices grew more slowly in November than the same month a year before.
- Expectations are now back largely in line with those seen in the more stable inflationary times before the recession of 2008-09. However if the current downward trend continues, inflation could fall below the Bank of England's target rate of 2.0% over the coming months.

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

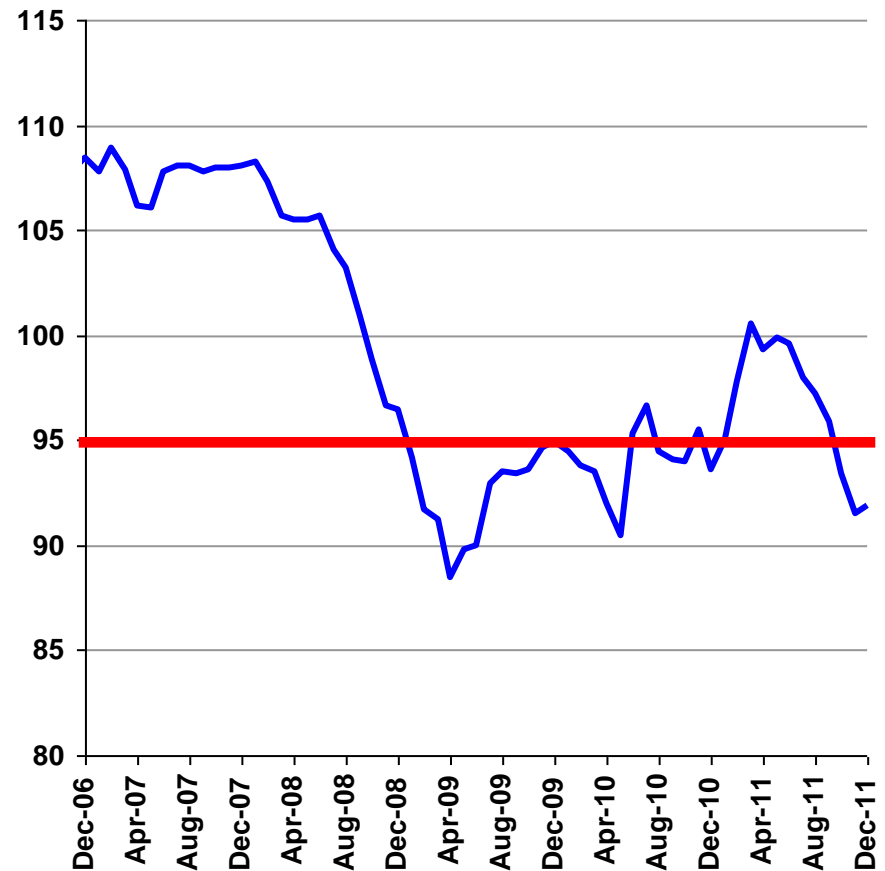


Source: Markit / CIPS PMI, Bank of England, CBI, Eurostat and the Office for National Statistics

Labour market conditions remain at low ebb

- The BDO Employment Index remained subdued in December, with a reading of 91.9 only marginally above November.
- The latest reading is the third consecutive month that the Index has remained below the 95.0 mark that marks contraction in the labour market. This indicates that employment conditions will continue to deteriorate over the coming months.
- Official labour market data shows the number of unemployed rising to its highest amount since September 1994. The unemployment rate stands at 8.3% and is expected to rise steadily over 2012.
- Businesses in both the manufacturing sector and the services sector report intending to reduce headcounts. Stagnant employment conditions in the private sector suggest the economy will struggle to make up for planned job losses in the public sector.

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



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

BDO Indices to latest month

		Jan	Feb	Mar	Apr	May	June	July	Aug	Sep	Oct	Nov	Dec
The BDO Optimism Index	Total	92.0	95.5	98.0	98.0	99.1	95.6	95.1	95.5	93.4	94.1	92.5	91.5
	Small	91.0	94.5	97.0	96.9	98.0	94.6	94.0	94.4	92.4	93.1	91.5	90.5
	Large	92.7	96.2	98.8	98.8	99.8	96.4	95.8	96.2	94.2	94.9	93.2	92.2
	Manuf.	106.2	116.4	112.7	102.9	97.5	90.1	93.5	90.1	88.2	94.3	86.2	86.6
	Service	88.4	90.3	94.4	96.8	99.5	97.0	95.5	96.8	94.8	94.1	94.1	92.8
The BDO Output Index	Total	95.5	94.8	99.3	97.6	98.2	96.3	95.0	93.6	93.3	92.6	92.5	91.4
	Small	93.9	93.2	97.7	95.9	96.6	94.7	93.4	92.0	91.8	91.1	90.9	89.8
	Large	96.8	96.1	100.7	98.9	99.6	97.6	96.3	94.9	94.6	93.9	93.8	92.6
	Manuf.	104.7	111.4	115.2	111.0	104.9	97.6	93.9	93.0	90.9	91.6	88.7	87.4
	Service	93.3	90.7	95.4	94.2	96.6	96.0	95.3	93.7	93.9	92.9	93.5	92.4
The BDO Inflation Index	Total	104.7	105.2	106.2	108.5	110.9	112.9	113.8	113.2	112.1	109.5	107.7	106.3
The BDO Employment Index	Total	95.0	97.8	100.5	99.3	99.9	99.6	98.0	97.2	95.9	93.4	91.5	91.9

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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; 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.