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Herefordshire and Worcestershire Chamber of Commerce

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# Q1 2015 Economic Review



## **SUMMARY**

“Following the strong growth in Q4 2014, the Quarterly Economic Survey for Q1 2015 shows that there is a slackening in the growth rate with weaker results for manufacturers and service sector firms across most indicators. Locally figures are positive in most key areas showing there is optimism and confidence.”

**Mike Ashton, Chief Executive, Herefordshire & Worcestershire Chamber of Commerce**

## **GENERAL NATIONAL OVERVIEW**

After strong results in Q4 2014, all the national domestic balances weakened in Q1 2015, for both manufacturing and services. In manufacturing, the domestic balances are now broadly similar to their pre-recession levels in 2007. In services, the domestic balances are still slightly higher than in 2007. The manufacturing sector's balance for domestic sales fell from +36% in Q4 2014 to +30% in Q1 2015, still seven points higher than in Q3 2014. The net balance for manufacturers' domestic orders fell from +38% in Q4 2014 to +27% in Q1 2015, still three points higher than in Q3 2014. The service sector's balance for domestic sales fell from +38% in Q4 2014 to +34% in Q1 2015, the lowest level since Q3 2013. The balance for service domestic orders fell from +33% in Q4 2014 to +28% in Q1 2015, the lowest level since Q2 2013.

Most national export balances weakened in Q1 2015. In manufacturing, one balance fell in Q1 and the other was unchanged. In services, both balances weakened in Q1, but one service balance fell only slightly. The manufacturing balance for export sales fell by seven points in Q1 2015, to +19%. The manufacturing export orders balance was +23% in Q1 2015, the same as in Q4 2014. The balance for export sales in services fell slightly by one point in Q1 to +21%, now the lowest level since Q2 2012. The service export orders balance fell by eight points in Q1 to +17%, the lowest level since Q3 2012.

All the national employment balances fell for both manufacturing and services in Q1 2015. For manufacturing, both the backward and forward-looking employment balances are still well above their average 2007 pre-recession levels. In services, one employment balance is marginally higher than in 2007 and the other is slightly lower.

The backward-looking manufacturing employment balance fell four points in Q1 to +32%, the same level as in Q3 2014. The forward-looking manufacturing employment expectations balance fell one point to +32%. The backward-looking service employment balance fell 12 points in Q1 to +20%, still marginally higher than in Q2 2014. The service employment expectations balance fell one point to +26%, the same level as in Q2 2014.

The national investment balances fell in Q1 2015, in both manufacturing and services. The balance of manufacturing firms that have revised upwards their plans to invest in plant & machinery fell four points in Q1, to +32%, still a higher level than in Q3 2014. The balance of manufacturing firms that have revised upwards their plans to invest in training fell six points to +33%, also a higher level than in Q3 2014. The balance of service firms that have revised upwards their plans to invest in plant & machinery fell two points to +19%, the lowest level since Q3 2013. The balance of service sector firms that have revised upwards their plans to invest in training fell two points to +24%, the level since Q2 2013.

The national confidence balances recorded mixed movements in Q1 2015. In manufacturing, the confidence balances were still higher in Q1 than their average 2007 pre-recession levels. But in the service sector, both confidence balances were lower than their average 2007 pre-recession levels. Confidence that manufacturing turnover will improve in the next 12 months fell from +62% in Q4 to +55% in Q1, the lowest level since Q2 2013. Confidence among manufacturers that profitability will improve in the next 12 months rose from +45% in Q4 +47% in Q1, but is still well below the confidence levels recorded in the first three quarters of 2014. Confidence among service firms that turnover will improve in the next 12 months dropped from +60% in Q4 to +50% in Q1, the lowest level since Q2 2013. Confidence that service sector profitability will improve in the next 12 months fell from +46% in Q4 to +41%, the lowest level since Q3 2013.

The cashflow balances worsened for both sectors in Q1 2015, and are now slightly lower than their average 2007 pre recession levels. The manufacturing cashflow balance fell four points in Q1 to +11%, the lowest level since Q2 2013. The services cashflow balance dropped nine points in Q1, to +12%, the lowest since Q2 2013.

Intentions to raise prices fell in Q1 2015, and in both sectors the balances are well below the 2007 pre recession levels. The balance of manufacturing firms reporting pressure to raise prices fell 10 points in Q1, to +11%, the lowest level since Q2 2012. The balance of service firms expecting to raise prices fell one point, to +23%, still slightly higher than in Q3 2014.

## **OVERVIEW LOCAL LEVEL**

The local Q1 results show that manufacturing and services firms have reported growth in many key areas compared to Q4 2014. The manufacturing sector has had increases in the balances for domestic sales, export sales and turnover confidence in Q1 compared with Q4.

Locally, the domestic balances for both manufacturing and services still remain at historically high levels.

However, the national employment balances fell for both manufacturing and services. A higher percentage locally expect there to be no change in their workforce. Professional/managerial positions are the most difficult positions to fill locally.

Locally, businesses believe that turnover and profitability will improve. This is for both the manufacturing and the services sector.

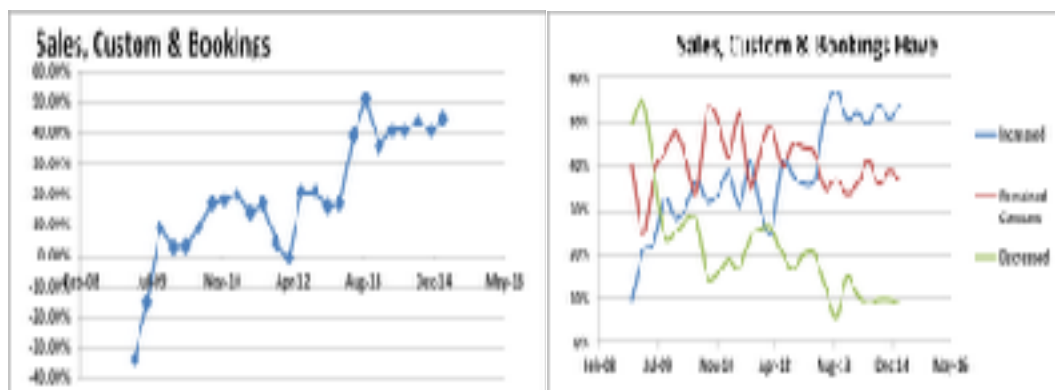
The main causes of price increase were raw material prices and other overheads.

Concerns locally are competition, corporation tax and business rates.

## DOMESTIC SALES

### SALES, CUSTOM AND BOOKINGS

The domestic sales balance is 45%, which is 4% higher than Q4. All the domestic balances remain at historically high levels in both sectors. Increased sales were reported by 54% of local businesses, 3% higher than the previous quarter. 37% reported their sales figures have remained constant which is down slightly on last quarter.



50% of local manufacturing saw an increase in sales (just down 2% from Q4). Nationally the manufacturing domestic sales fell. Figures for the local service sector show an increase of 54% (up 5% on Q4).

## ORDERS/ADVANCE CUSTOM AND BOOKINGS

Overall figures show a 51% increase for orders and advance bookings in the domestic market (which is up 3% from Q4). This shows positivity in orders and bookings. The balance is at 43% (Q4 the balance was 37%).

48% of local manufacturing saw an increase in orders, 2% lower than last quarter. Nationally, manufacturing domestic orders decreased further.

The local service sector figures show 50% reporting an increase in orders, 6% higher than Q4, 40% with orders remaining constant and 8% with decreasing orders over the last three months. Nationally, service domestic orders fell.



## EXPORT SALES

### SALES, CUSTOM AND BOOKINGS

49% saw export sales increase, which is 9% higher than the last quarter. Only 6% of companies saw a decrease in their overseas sales, custom and bookings, down 43% on last quarter.



Local manufacturers reported 35% increased sales, the same as Q4, 5% decreased sales and 31% experienced constant overseas sales which is 6% higher than Q4. Local service sector sales figures were lower at 27% increased sales, 3% decrease but with 26% remaining constant. Nationally, export sales fell slightly for both sectors.

## ORDERS/ADVANCE CUSTOM AND BOOKINGS

The balance for overseas orders has increased 14% to 42% in Q1 2015. There has been an increase in orders from 39% in Q4 to 47% in Q1.

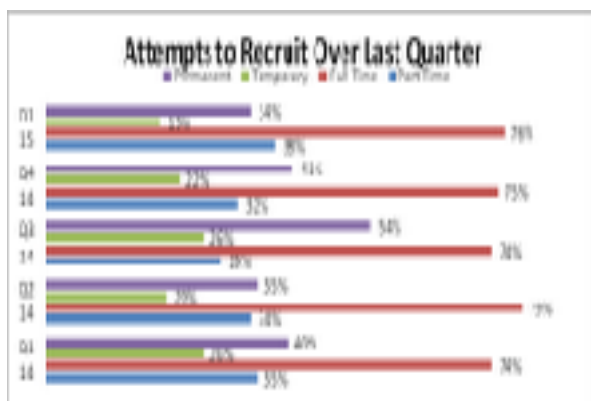


## OVERVIEW - EMPLOYMENT

### Changes to Workforce

The workforce change balance has decreased to 27% (28% lower than Q4). There was a 34% increase in workforce in Q1, 29% lower than Q4.

33% of companies responding reported plans to increase their workforce over the next three months (previous quarter was 29%), with just 3% with plans to decrease the workforce, just 2% lower than Q4.



## ATTEMPTS TO RECRUIT

76% have attempted to recruit full-time staff, an increase of 1% on the last quarter. Employing permanent positions has decreased 7% on the previous quarter. There is 3% decrease on last quarter for filling temporary positions. Taking a closer look at the local level we see that 60% of local manufacturers have attempted to recruit in

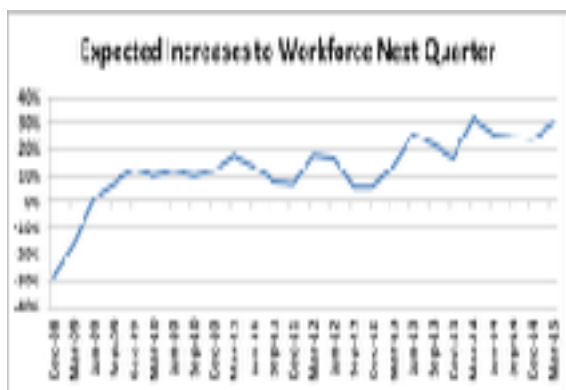
the last quarter which is 2% higher than the last quarter and 47% in the service sector, which is up 2% on Q4.

34% of local manufacturers have seen an increase in their workforce, which is a 2% decrease on Q4. Turning to the local service sector, 32% increased their labour force, which is a 6% increase on last quarter.

## RECRUITMENT DIFFICULTIES

Recruitment difficulties were experienced by 53% of businesses, the same as Q4.

39% of local manufacturers (an increase of 2%) and 23% of local services (an increase of 1%) have reported recruitment problems.



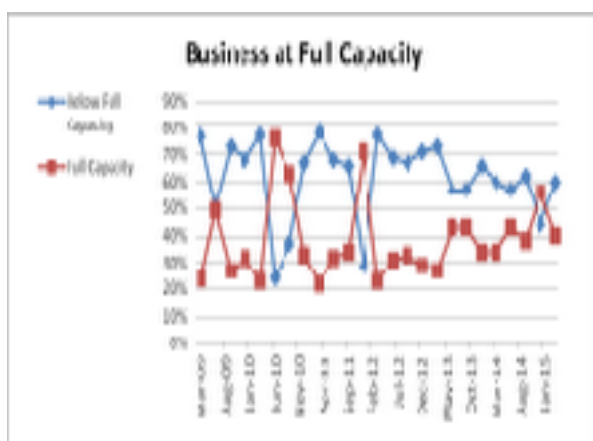
The key difficulty for manufacturer and service sector businesses alike was finding skilled manual/technical staff and also professional/managerial staff.

This follows a similar pattern to the last few quarters.

## EXPECTATIONS TO RECRUIT NEXT QUARTER

The balance for changes to workforce is 30%, a 6% decrease on last quarter.

A high percentage from the local manufacturing sector report that they expect their workforce to decrease over the next 3 months. In the local service sector businesses believe they will maintain their current staff levels. Nationally, employment expectations fell.



## CAPACITY CONSOLIDATION, CASHFLOW & INVESTMENT

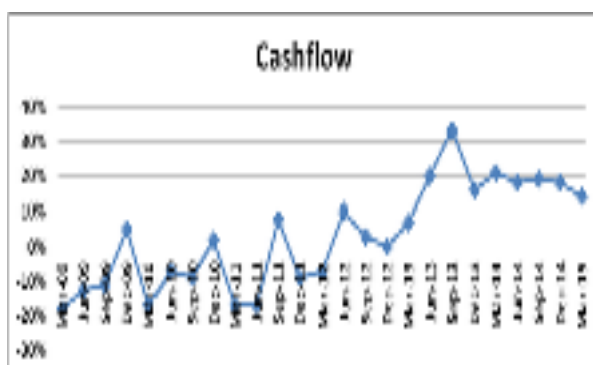
### Capacity

The full capacity balance has decreased from the last quarter to 40% by 16%.

60% of local businesses reported to be operating below full capacity, an increase of 16%. Turning to local manufacturers, 42%

stated over the last period they operated at full capacity and 55% reported to be operating below full capacity. Figures in the service sector show that 59% are operating below full capacity and 37% operating at full capacity.

## CASHFLOW



Regarding the cashflow balance this has decreased 4% to 14%.

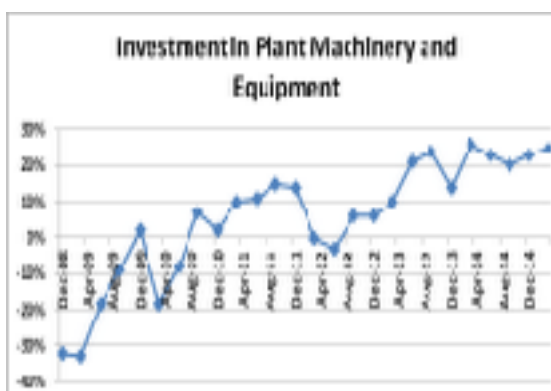
32% reported an improved cashflow experience, the same as Q4 and 50% stated their cashflow remained the same which is down just 2% from the previous quarter.

32% reported improved cashflow figures in the service sector and 29% reported improved cashflow in the manufacturing sector. Nationally, the cashflow balances worsened for both sectors in Q1.

## INVESTMENT

Overall the investment balance is -35%. Investment in plant machinery and equipment is up slightly to 25%. Investment in training is up 4% on last quarter.

61% of local manufacturer's have seen investment in plant machinery and equipment remain the same. 62% of local services have seen investment in training remain the same.



## EXTERNAL FACTORS

## PRICE PRESSURES





The balance figure for pressure on businesses to raise prices has decreased by 7% to 17%. 24% of companies surveyed experienced pressures to raise their prices, which is slightly lower than the last quarter.

7% reported they expect prices to decrease over the next quarter. 69% anticipate their price levels to remain unaffected, similar to

last quarter. 22% of local services and 26% of local manufacturing firms expect prices to rise.

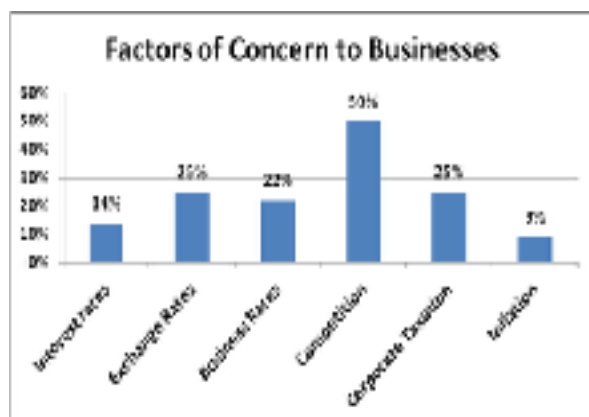
Overall, raw materials and other overheads were mentioned as main contributors to price increases. Factors of concern to businesses were competition, exchange rates, corporation tax and business rates.

### BUSINESS CONFIDENCE

The turnover balance has increased slightly but the profitability balance has decreased. Turnover confidence increased 1% to 73%. Confidence regarding profitability decreased to 61%.



73% of local manufacturers are expecting an increase in turnover, 4% lower than Q4 and 68% believe profitability will improve, just 1% lower than Q4. Confidence figures for the local service sector has increased for turnover as 76% believe they will see an improvement of turnover (5% higher than Q4) but expectations of profitability has decreased as 62% expect profitability to increase (this is 6% lower than Q4). Nationally, confidence balances for manufacturing were higher in Q1 than their average 2007 pre-recession levels. For the service sector confidence balances were lower than the pre-recession levels.



## FACTORS OF CONCERN TO BUSINESSES

The main factors of concern for businesses are, competition, exchange rates, corporation tax and business rates (50%, 25%, 25% and 22%).

Locally, the manufacturing and service sector also state that competition is a factor of concern.

## Summary 1<sup>st</sup> Quarter 2015

After very strong increases recorded in Q4 2014 the latest QES results are mediocre. Almost all the national balances, for both manufacturing and services, weakened in Q1. In both sectors, a number of key balances are now lower than their pre-recession levels in 2007. The only exceptions to the general pattern of lower balances in Q1 is a small rise in the manufacturing balance for profitability confidence and an unchanged balance for manufacturing export orders. While the Q1 results do not necessarily point to slower GDP growth, they highlight the major challenges facing UK businesses in key areas: exports; domestic markets; employment; investment and confidence. Intentions to raise prices fell sharply in manufacturing and slightly in services. The level of capacity utilisation eased in both sectors. The results of this quarter's survey supports our view that the UK recovery will continue in 2015, but growth must be nourished and supported in order to become sustainable over the longer term.

**Commenting on the results, John Longworth, Director General of the BCC, said:**

"It is not a huge surprise to see slightly weaker numbers at the start of the year, after a very strong fourth quarter for many firms. Crucially, our survey demonstrates that businesses remain optimistic, though they expect to grow at a slightly slower rate over the coming months.

"Our conclusions are by no means a cause for alarm, but they are a salutary reminder that the UK still faces obstacles on the path to sustainable, long-term growth. Unless support for exports and business investment is placed at the heart of any future government, consumption and government spending will continue to drive an economic recovery that is unbalanced and unsustainable.

“With these results in hand, our message to the politicians is simple: the national interest must come before short-term political point scoring. Given that all parties agree that the UK needs to strengthen its trade performance, and that we need to encourage our businesses to invest more, these should be issues that unite - rather than divide - the parties over the weeks ahead.”

**David Kern, Chief Economist at the BCC, said:**

“After unusually strong results in Q4 2014, almost all the national balances weakened in Q1 2015, for both manufacturing and services. **But** taking the QES results for the last two quarters together probably gives a more representative picture of the business outlook.

“It is disappointing that most Q1 balances recorded quarterly falls, and some are lower than the 2007 pre-recession levels, however the balances still point to solid economic growth continuing in 2015. While the national balances of our survey reflect accurately the overall momentum in economic activity, they do not necessarily replicate quarterly GDP movements as published by the ONS. It would not be surprising if the ONS reports an upturn in GDP growth, or at least an unchanged position, in Q1 2015.

“But the UK recovery remains unbalanced - growth is still too reliant on consumer spending and the current account deficit remains unsustainable. While a healthy consumer sector is vital for the economy’s wellbeing, much greater efforts are needed to increase the contributions of exports and capital investment to Britain’s growth. The Q1 2015 results show falling inflationary pressures, particularly in manufacturing, and easing pressures on capacity; this reinforces our view that the MPC must maintain interest rates at their current low level at least until early in 2016.”