BANK OF ENGLAND

Agents' summary of business conditions

November 2008

- Contacts painted a weak picture of most aspects of economic activity, with further reductions in the Agents' scores from the low levels reported last month.
- Demand for consumer services continued to shrink, and retail sales values were broadly unchanged relative to a year earlier.
- Investment intentions had been further reduced, with an increasing number of contacts citing tighter financing conditions as a factor in their decisions over and above the outlook for demand.
- Manufacturing output for domestic sales fell and a range of construction and business service activities also contracted.
- Growth in export orders had slowed sharply — after having been broadly stable across much of the year.
- Employment intentions were scaled back further across all sectors.
- Growth in labour costs remained subdued, with most contacts expecting next year's pay rises to be no larger than this year's.
- Annual input and output price inflation eased slightly.
- Retail goods and service price inflation also eased amidst reports of increased promotional activity.

This publication is a summary of monthly reports compiled by the Bank of England's Agents, following discussions with contacts in the period between late September and late October.
It provides information on the state of business conditions, from companies across all sectors of the economy. The report does not represent the Bank's own views, nor does it represent the views of any particular company or region. The Bank's Monetary Policy Committee uses the intelligence provided by the Agents, in conjunction with information from other sources, to assist its understanding and assessment of current economic conditions. A copy of this publication can be found at:
www.bankofengland.co.uk/publications/agentssummary/index.htm.

The Bank of England has Agencies for Central Southern England, the East Midlands, Greater London, the North East, the North West, Northern Ireland, Scotland, the South East & East Anglia, the South West, Wales, the West Midlands & Oxfordshire, and Yorkshire & the Humber.

The Bank's assessment of current monetary and economic conditions, and the outlook for inflation, are contained in the Inflation Report, obtained from:
www.bankofengland.co.uk/publications/inflationreport/index.htm.

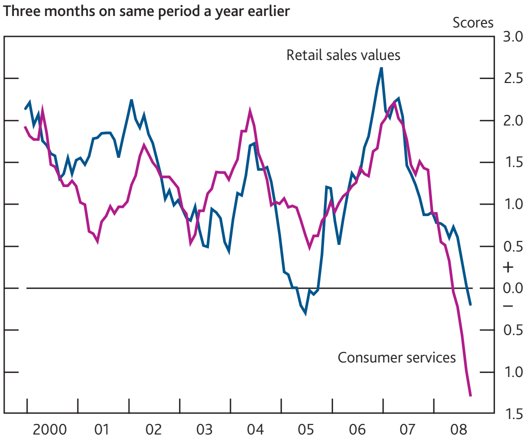
Demand

Consumption

The Agents' scores for retail sales values and consumer services turnover fell further in October (**Chart 1**).

Chart 1 Consumption values

Three months on same period a year earlier



Demand for a broad range of consumer services had continued to shrink. Consumption of housing-related services was contracting rapidly. Pubs and restaurants had seen reduced turnover as consumers cut back on discretionary leisure expenditure, with contacts flagging a continuing trend towards home consumption of food and drink. Domestic tourism remained an exception, with hotels reporting steady leisure bookings.

The value of retail sales was broadly unchanged on a year earlier, as the key drivers highlighted in recent months persisted. Consumers were shifting expenditure towards unbranded, or 'value' products in the face of budgetary pressures. Factory outlets and discount stores continued to gain market share. Sales of furniture and other big-ticket household items were still falling. More generally, discretionary expenditure was seen to be shrinking, with retailers reporting that fewer consumers were treating shopping as a leisure activity — reflected in reductions in both impulse spending and visitor numbers at major shopping centres.

Housing market

Activity remained weak. While there had been occasional reports of a pickup in viewings, contacts were not optimistic that these marked a sustained improvement in demand. Rather, the prevailing sense was that sales were largely limited to moves forced by job changes, repossessions, or changes in family circumstance.

Investment

Agents' scores for manufacturing and service sector investment intentions fell further in October. The slowdown in capital spending plans was widespread, affecting most industries. Many contacts reported that investment plans had been pared back to essentials — for example, to satisfy regulatory requirements. And where possible, firms were prolonging the use of existing assets. A number of contacts had, however retained projects aimed at securing energy efficiencies, some of which were large in scale.

The outlook for demand continued to be cited as a significant factor driving reduced investment intentions. Many contacts felt that demand uncertainties had risen in the wake of the financial turbulence experienced in recent months. However, there had also been an increase in the proportion of contacts citing financing concerns as an additional factor limiting investment.

Contacts reported a tightening in their own credit conditions since September. The all-in cost of finance had increased as set-up and management fees were raised and loans were increasingly priced relative to Libor rather than Bank Rate. Some contacts expected future cutbacks in facilities. There was also a wide-ranging perception that banks have become more active in responding to breaches in covenants.

Only a small number of October's contacts reported that their day-to-day business was immediately threatened by tightening external credit conditions. But concerns over the potential for future pressures on working capital had led some to cut back on internally funded investment plans. And there were also reports of investment plans being shelved as a result of doubts over the prospective availability of external funds.

Inventories

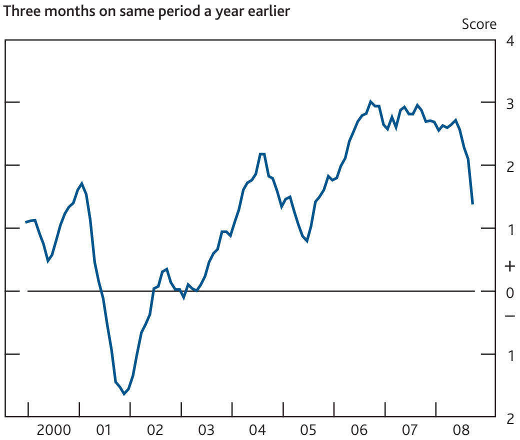
Actual and perceived pressures on working capital had led some contacts to cut back on planned inventories. And retail contacts reported some scaling back of orders in anticipation of a weaker-than-normal consumer demand around Christmas.

Overseas trade

The Agents' score for goods exports had been reduced significantly (**Chart 2**).

Chart 2 Manufacturing exports

Three months on same period a year earlier



Across much of the year, growth of export demand had been broadly stable. In recent months, however, contacts have reported a sharp slowdown in orders. The slowdown in orders largely reflected the pronounced weakness in demand in most developed countries. Orders from the euro area had shrunk as economic conditions had deteriorated — particularly in Ireland — and US consumer demand remained weak. However, contacts also reported some slowing of Middle and Far Eastern demand for capital goods. This reflected both the global effects of the credit crunch and overcapacity in some sectors.

A number of contacts cited trade credit and credit insurance as constraints on export sales. For many, trade credit and insurance had become harder to access and more expensive. For others, increased concerns over counterparty risk meant that insurance was seen to be more critical to trade than had previously been the case.

Volumes of imported consumer and capital goods continued to shrink. This had been reflected in declines in shipping activity. Some contacts reported plans to shift component supply back from China to domestic manufacturers.

Output

Business services

The Agents' score for business services turnover fell further (**Chart 3**).

Chart 3 Services turnover

Three months on same period a year earlier

A few isolated areas had seen increased growth in recent months — typically in countercyclical activities such as corporate recovery work and legal services related to employment law. But these were more than offset by shrinkage in activity elsewhere. For example, contacts reported a reduction in discretionary business expenditure on marketing and conference bookings. Reflecting the shrinkage in aggregate demand and output seen in recent months, a number of contacts also reported slowing demand for transport and logistics.

Manufacturing output

Manufacturing output had continued to fall in aggregate, though there was a broad dispersion of experience across different subsectors. On the downside, construction-related businesses had experienced a particularly marked slowdown in orders. And there were signs that cutbacks by building materials suppliers were having an impact further along the supply chain — for example, on the chemicals industry. On the upside, public and quasi-public transport investment programmes were generating significant demand for some firms. And firms supplying sectors that have so far been less affected by the downturn — for example, agriculture and pharmaceuticals — reported stable order books.

Construction

Construction output slowed further. Levels of house-building and commercial property activity remained sharply lower than a year earlier. The volume of land transactions had also slowed markedly. However, public sector projects continued to provide some support to construction output in all regions.

Capacity utilisation

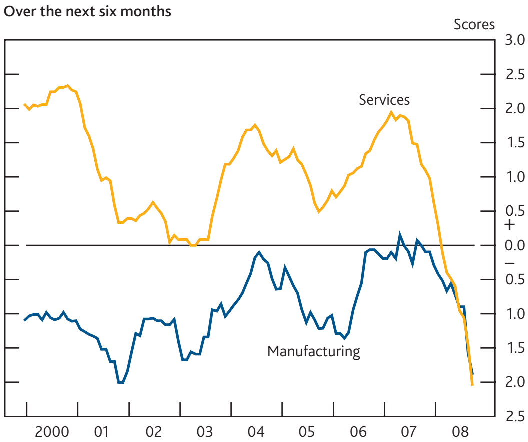
Capacity constraints had continued to decline. Weakening demand had led many contacts to cut output. But most businesses had retained capacity by cutting back on shift work and temporarily mothballing production lines. There were only infrequent reports of longer-term adjustments to capacity — for example through business closures or exiting aspects of business.

Employment

As in September, contacts reported declining demand for labour. The Agents' scores for employment intentions were reduced further across all sectors (**Chart 4**). In recent months, the scores for employment intentions in the services sector have been reduced particularly sharply and are now at their lowest level since Agents began scoring in 1997.

Chart 4 Employment intentions

Over the next six months



Fewer businesses were advertising for vacancies through Job Centres. A number of retailers had scaled back on their Christmas hiring plans. And construction companies continued to cut back on their demand for labour from sub-contractors. Moreover, reports of small-scale redundancies and plant closures had become more widespread. And more firms were entering redundancy consultations.

Costs and prices

Labour costs

The Agents' scores for labour cost growth were little changed in October. Most contacts expected next year's pay increases to be no larger than this year's. And some contacts reported wage freezes or postponement of settlements. As in September, a number of contacts felt that employee resistance to below-inflation settlements was lower than normal — reflecting heightened job insecurity.

Input and output prices

The Agents' score for materials cost inflation was cut in October, reflecting the sharp falls in spot commodity prices seen in recent months. However, input price inflation remained elevated relative to historic norms. In large part, this reflected long lags in passing through increases in energy prices earlier in the year. For example, many contacts were still locked into annual energy contracts set prior to the oil price rises experienced during the first half of 2008 and therefore anticipated price rises when contracts were renewed. Some contacts also reported that sterling's recent depreciation had dampened the impact of falling international commodity prices.

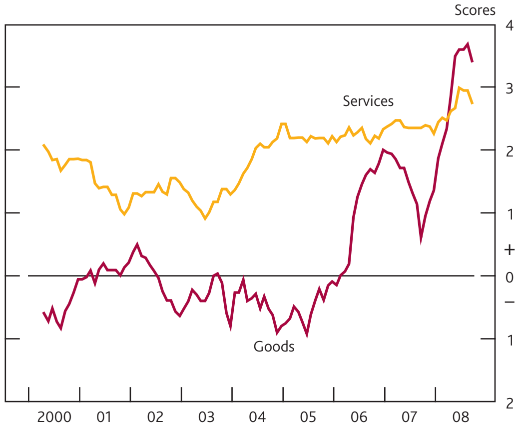
Manufacturers' ability to raise prices was limited both by the sharp slowdown in demand and by pressures to reduce stocks and hence preserve working capital. Wholesale food prices were stabilising. And contacts reported increased price discounting in sectors where discretionary corporate spending had weakened, including conference, corporate hotel and advertising rates.

Consumer prices

The Agents' scores for both retail goods and retail services prices were reduced slightly, though they remained elevated relative to historic norms (**Chart 5**).

Chart 5 Retail prices

Three months on same period a year earlier



Contacts reported faster than normal deflation in used car prices and increased promotional activity in both the retail and leisure sectors. Looking forward, the weakening outlook for demand was felt to have reduced the scope for consumer-facing firms to pass on cost increases. A number of contacts expected retail food prices to fall, under the combined impact of stabilising wholesale prices and an increase in price competition by supermarkets.