BANK OF ENGLAND

Agents' summary of business conditions

May 2015

- Consumer services and retail sales turnover had risen moderately.
- Housing market activity remained below that of a year earlier, with some contacts reporting a slowing in the run-up to the General Election.
- Investment intentions for the next twelve months were consistent with moderate growth overall.
- Business services turnover growth had remained robust and broadly based.
- Manufacturing output growth, both for the domestic market and for export, had edged lower.
- Construction output growth had continued to ease on a year earlier, but remained fairly robust overall.
- Corporate credit availability had improved further.
- Employment intentions had edged higher and were consistent with modest headcount growth overall.
- Recruitment difficulties had changed little, at a level somewhat above normal.
- Capacity utilisation had remained at broadly normal levels in manufacturing, but slightly above normal for services.
- Growth in total labour costs per employee had been steady.
- Materials costs and imported finished goods prices had remained lower than a year earlier.
- Output prices had fallen on a year earlier for manufacturers, although they had risen moderately for business services firms.
- Profitability growth had edged higher for services, but had fallen for manufacturers.
- Consumer price inflation had remained negative for goods. Retail service prices had continued to increase modestly.

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 March 2015 and late April 2015.
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/Pages/agentssummary/default.aspx.

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/Pages/inflationreport/default.aspx.

Demand

Consumption

Annual retail sales values growth had remained steady. Food prices had continued to decline but growth in sales volumes had increased. The patterns of growth had been mixed for non-food sales. A slowdown in the housing market and limitations in technological innovation were reported to have led to easing growth in household durable goods sales. However, consumers had been trading up in value terms, for example through shifting their purchasing towards aspirational brands. New car sales growth, supported by finance deals and manufacturers' incentives, had remained robust. Consumer services turnover growth had eased very slightly, but remained pretty robust. UK hoteliers reported a slight easing in occupancy rates — but that was probably a temporary effect from poor Easter weather. Forward holiday bookings in the United Kingdom were reported to be robust, as was trading by restaurants, coffee shops and internet-based service providers. Independent Financial Advisors had reported a sharp increase in demand for personal financial planning advice following recent reforms to pensions.

Housing market

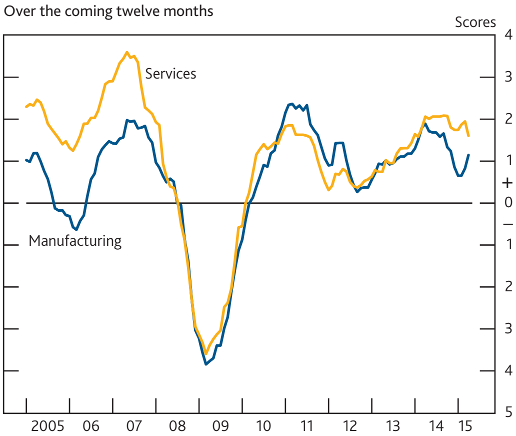
Housing market activity had remained below that of a year earlier. There were reports of a slowing in housing market activity in the run-up to the General Election, especially among potential sellers, some of whom were holding off from putting their property on the market in the expectation that conditions would be more buoyant in H2. That had exacerbated existing supply shortages in some areas. House price inflation had remained generally modest. The rental market had continued to expand, supporting growth in buy-to-let activity. There had been no evidence as yet that recent reforms to pensions had stimulated investment in property.

Business investment

Manufacturers' investment intentions had picked up modestly (**Chart 1**). In the main, manufacturing investment had been aimed at increasing efficiency and productivity, although there were increasing reports of spending to increase capacity. Services investment intentions had eased but pointed towards moderate growth. Spending on new IT had remained a frequent driver of growth, although growing numbers reported having completed the necessary catch-up in technology over the past year or so. In consumer services, the need to respond to changing buying habits, such as the popularity of coffee shops and smaller convenience stores, was often driving growth. On the whole, businesses had not delayed investment spending due to the General Election beyond those whose revenue was most dependent on public funding and potential policy changes.

Chart 1 Investment intentions

Over the coming twelve months



Exports

Manufacturing exports growth had remained stable but subdued. Conditions across markets were mixed, with weak euro-area demand and the appreciation of sterling against the euro having made exporting to Europe more difficult, offset by rising demand from the United States, aided by the depreciation of sterling against the dollar. Sales to Russia had been adversely affected by trade sanctions, unfavourable exchange rates and the general state of the economy. Services exports had continued to grow at a modest rate. Legal and commercial property services reported rising demand for advice from overseas clients seeking to invest in the United Kingdom. But overseas demand for advisory services related to the oil and gas industry had weakened. There had been increasing signs of services exports being affected by the appreciation of sterling against the euro.

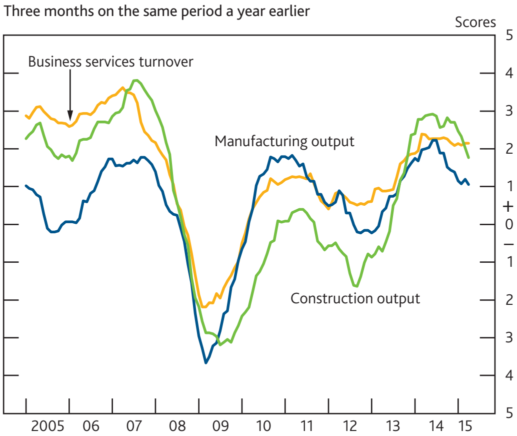
Output

Business and financial services

Turnover growth had continued to be robust (**Chart 2**). Strong corporate transaction and commercial real estate activity had increased demand for legal, advisory, accountancy, architectural and surveyors' services. Digital transformation

Chart 2 Activity

Three months on the same period a year earlier



across sectors was increasing demand for management consultants and IT activity. Some insurance companies reported that sales of additional cover to corporate clients were increasing. Distribution and storage firms reported strong volume growth. Recruitment agencies had remained busy, although some reported that the rate of growth was moderating. There were reports of strengthening corporate travel, conferencing and entertainment. But demand from the oil and gas industry for professional services had fallen.

Manufacturing

Manufacturing output growth had eased very slightly and remained modest (**Chart 2**). Demand had softened in aerospace supply chains, which contacts attributed mainly to the industry entering the 'de-stocking phase' of the product cycle. There were mixed reports from the automotive sector, mainly due to weakness in some export-related supply chains. Demand for operational equipment for the oil and gas sector had fallen, although orders of exploration equipment had held up. Manufacturers of capital equipment for the food sector reported increasing demand, although reports from food manufacturers about their output were mixed. Output of capital goods for the agricultural sector had declined further.

Construction

Construction output had continued to grow on a year earlier, although the rate of increase had eased (**Chart 2**). That slowing had reflected both self-imposed constraints, such as firms' desire to grow their margins rather than output and/or a reluctance to take on additional overheads, and constraints from skills shortages and rising build costs. Some public sector construction projects had been delayed in the pre-election period, although there were strong pipelines of work in many areas including infrastructure. Commercial construction had continued to grow overall, but the picture was patchy: for example, speculative building was limited to a few major cities and some energy-related schemes had been mothballed. In house building, the picture was mixed, but affordable house completions were reported to have picked up in March ahead of the end of the Homes and Communities Agency grant period and there were reports of a gradual increase in activity among small builders.

Credit conditions

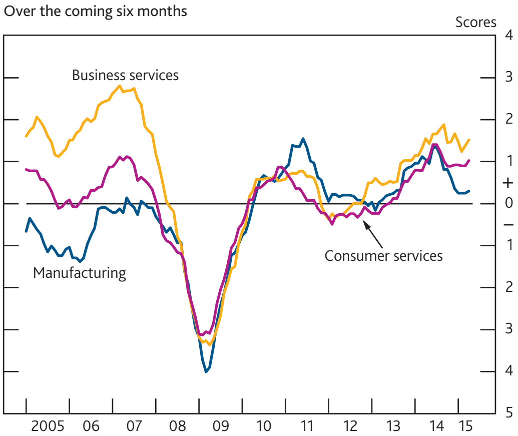
Credit conditions had improved further, with lending spreads coming under more downward pressure, loan tenors gradually extending and covenants easing slightly. The supply of non-bank finance, including from capital markets, had remained strong and at costs that were often reported as at record lows. Large corporates had been readily able to access funding from a range of sources, with banks reported to be competing aggressively for lending business. Medium-sized businesses had also increasingly benefited from greater competition among banks. Availability of funding had improved slightly further for small companies, but it had remained tighter than normal for some firms, such as for those involved in construction and property.

Employment

Employment intentions had edged a little higher, pointing to modest job creation over the next six months (**Chart 3**). Intentions were often strongest among business services contacts, particularly in the professional services and IT subsectors. Headcount growth in consumer services had been most evident in roles supporting online sales, or on the back of physical footprint expansion, partially offset by reductions in employment numbers among the major supermarkets. Manufacturing employment intentions were marginally positive. Recruitment difficulties had remained elevated for many contacts. Skill shortages still tended to be role or sector specific, but they had become more broad-based as economic activity had risen. Alongside this, attrition rates had picked up as employees had become more confident about moving jobs. Some contacts reported increasing difficulties in finding good quality candidates for lower-skilled jobs as the labour market had tightened. Migrant labour had continued to help fill gaps in unskilled and, in some cases, more highly skilled occupations.

Chart 3 Employment intentions

Over the coming six months



Capacity utilisation

Capacity utilisation had remained unchanged overall. Utilisation was around normal for manufacturing and slightly above normal in services. Within manufacturing, the effects of modest demand growth, recent investment and continuing productivity improvements meant that capacity utilisation was likely to remain marginally below normal levels for the next six months. In services there had been a notable reduction in utilisation for oil and gas related businesses. Utilisation across the sector overall had remained steady however as fixed asset utilisation was rising in other services, such as hotel occupancy and warehousing. Labour shortages were constraining output in some companies, in particular in professional services and construction.

Costs and prices

Labour costs

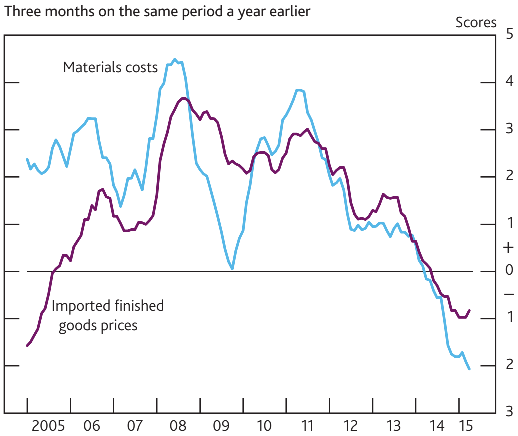
Growth in total labour costs had remained modest, but slightly faster in services than in manufacturing. Most settlements had remained in the 2%–3% range, although there had been some signs of manufacturing settlements tailing off a little in recent months, and pay freezes were reported in the oil and gas sector, and its supply chain, as the effect of lower oil prices fed through. Overall, upward pressures on wage growth from skills shortages had been balanced by downward pressures from low inflation, which was reported by some contacts to have allowed settlements to be lower than would otherwise have been the case, for example, where companies were struggling to afford pay rises.

Non-labour costs

Material costs had remained lower than a year earlier (**Chart 4**). Contacts linked substantial falls in agricultural commodity costs to high global stocks, following good harvests and a sharp decline in sales of produce from Europe to Russia. The decline in oil prices earlier in the year had fed through to plastics prices but had not been fully reflected in transport costs, due to offsetting increases in driver pay, and earlier forward purchases of oil. The rate of decline of imported finished goods prices had moderated a little (**Chart 4**). Although some importers reported lower prices from the euro area as a result of the decline in the euro, others who paid for their imports in sterling had seen no adjustment in prices. And some contacts reported upward price pressure from some European suppliers due to higher costs for dollar-denominated inputs. The cost of dollar-denominated imports from China had increased as a result of sterling's depreciation against the dollar and Chinese wage inflation.

Chart 4 Input costs

Three months on the same period a year earlier

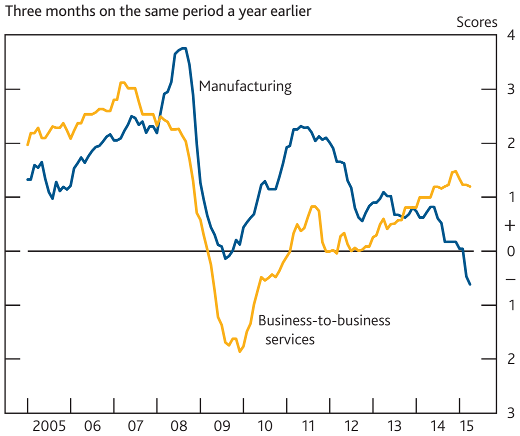


Output prices and margins

Manufacturing output prices had fallen slightly further on a year earlier (**Chart 5**). Although some firms reported being able to raise prices modestly year on year, many were coming under increased pressure from customers to reduce pricing as input costs had fallen. Business services output price inflation had been little changed (**Chart 5**). For many standardised services, there had been continued downward price pressure as contracts come up for renewal or procurement departments sought further year-on-year cost savings. Financial services prices were also under pressure because of increased competition. Elsewhere in business services, however, modest price increases were generally reported. Across the oil and gas sector supply chain, prices were falling significantly on a year ago as the lower oil price led to repricing. Overall, growth in manufacturing profitability had eased further, in part reflecting the effects of sterling's appreciation on exporters' margins. Service sector profitability growth had increased slightly, because of modest price increases and, in some cases, lower non-labour costs or moves away from lower margin work.

Chart 5 Output prices

Three months on the same period a year earlier



Consumer prices

Consumer goods price inflation had remained negative and little changed. Annual reductions continued to be focused primarily on food, fuel and energy with relatively little sign of price falls for other goods. Strong competition among supermarkets had continued to bear down on groceries inflation. Elsewhere, goods prices in high street or out-of-town stores had appeared broadly flat. In some cases, goods prices had risen at a slower pace than normal due to the pass-through of lower input costs and sterling's appreciation. But forecourt fuel prices had shown signs of creeping back up a little in recent weeks. Consumer service price inflation had remained positive but modest. For example, prices for some leisure and hospitality services had risen gradually alongside rising demand. Inflation in index-linked services prices, such as social housing rents and utility bills, had moderated over recent months.