



Agents' summary of business conditions and results from the Decision Maker Panel survey

2018 Q4

- Consumer demand softened, especially for major household purchases.
- Investment intentions continued to weaken, with Brexit uncertainty a restraining factor.
- Export growth eased slightly, following weaker demand from some emerging markets.
- Recruitment difficulties continued to intensify and constrained growth for some contacts; pay growth was slightly higher than a year ago.

Growth in the value of **retail sales** weakened. Uncertainty related to Brexit and subdued housing market activity weighed on demand, including for furniture and household appliances.

Business and financial services growth continued at a modest pace, though growth in hospitality and marketing weakened.

Growth in **exports of services** remained around average, helped by strong inbound tourism, which partially offset weaker demand for services related to goods exports and corporate transactions.

Domestic manufacturing output continued to grow at a steady pace, supported by robust demand in sectors such as electronics, aerospace, food and beverages. There were a few reports of contacts expecting to accelerate stockbuilding in 2019 Q1, but many contacts have not yet implemented contingency plans for Brexit, consistent with the recent Agents' survey on preparations for EU withdrawal.⁽¹⁾

Growth in **exports of manufactured goods** continued to ease from robust rates, as the boost from the past depreciation of sterling waned. There was some evidence of slower demand from some emerging markets.

Construction output continued to grow at a modest pace, with growth in private rental sector development and civil engineering and infrastructure projects partially offsetting slightly weaker housebuilding activity.

Investment intentions eased further, with a growing proportion of contacts putting new capital investment on hold until there is greater clarity around Brexit.

Demand for credit from corporates softened slightly, reflecting subdued investment intentions, and slower refinancing and mergers and acquisitions activity. Credit availability tightened for some contacts in sectors vulnerable to a potential slowing in demand such as construction, procurement and consumer-facing businesses.

Investor demand for **commercial real estate** was concentrated in warehousing and distribution, and demand from foreign investors for developments in UK cities remained solid.

Housing market activity weakened, partly due to increased uncertainty about the economic outlook.

Capacity constraints remained above normal in manufacturing and services, which some contacts attributed to labour shortages.

Consistent with that, **recruitment difficulties** continued to intensify and became more widespread. **Employment intentions** were mixed across sectors, however, and pay growth was only slightly higher than a year ago.

Consumer goods price inflation remained elevated, buoyed by higher fuel and energy prices than a year ago.

(1) Please see www.bankofengland.co.uk/report/2018/agents-survey-on-preparations-for-eu-withdrawal.

This publication includes a summary of economic reports compiled by the Bank of England's Agents between mid-October and late November 2018. It generally makes comparisons with activity and prices a year earlier. The report does not represent the Bank's own views, nor does it represent the views of any particular company or region. More information on the Bank's Agencies can be found at www.bankofengland.co.uk/about/people/agents. This publication also includes a summary of information gathered by the Bank's Decision Maker Panel survey. Further background is provided in Box 2 on pages 7–8.

Consumer demand

Over the past three months, annual growth in consumer goods values weakened, but was close to its long-run average (**Chart 1**). Demand for furniture and household appliances slowed, which contacts attributed to rising uncertainty related to Brexit and subdued housing market activity. There were some reports of falling demand for luxury foods, while grocery discounters continued to grow market share.

Contacts said early evidence suggested that 'Black Friday' sales had failed to meet many retailers' expectations. This was attributed to several factors. There was more discounting in early November. Some retailers limited their discounts to safeguard profits. The timing of the Black Friday weekend was earlier than usual. And consumers were more cautious, with average purchase baskets reported to be lower than a year ago. Some contacts thought the disappointing Black Friday sales could just indicate that less spending had been brought forward from December, although they were generally cautious about the outlook for sales over the Christmas period.

Growth in consumer services values remained somewhat muted, with weaker activity in housing-related services offset by modest growth in leisure services, albeit in lower price brackets.

Chart 1 Consumer goods values and consumer services turnover

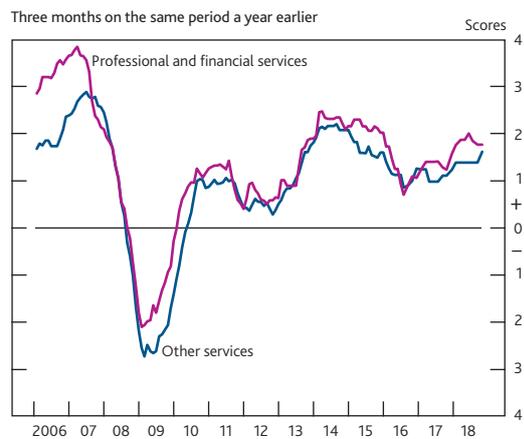


Business and financial services

Demand for business and financial services continued to grow at a modest rate (**Chart 2**). Contacts in sectors such as commercial property, recruitment and business advisory services reported that demand had been more resilient than they expected.

Mergers and acquisitions (M&A) activity continued to hold up, though there were some signs of slowing following a period of robust growth, and demand remained strong for IT services. But demand had weakened in sectors reliant on discretionary spending, such as hospitality and marketing.

Chart 2 Business and financial services turnover



A number of contacts warned that if Brexit uncertainty continued, activity could slow in Q1, potentially quite sharply, as businesses were likely to avoid completing large transactions close to the date of EU withdrawal.

Growth in services export values was steady and remained around its average over the past year (see Box 1). Most professional and financial services firms continued to report modest growth in demand from overseas clients, as did contacts in other business services, such as those related to oil and gas.

Companies in the IT sector, for example those specialising in gaming and animation, reported particularly strong growth. However, demand related to corporate transactions eased, and a few contacts said they had decided to cease providing some services to EU clients temporarily due to Brexit uncertainty. Overseas demand for services associated with outbound cargo and car volumes from UK ports weakened slightly.

Student numbers from the EU to UK universities were lower than a year ago. By contrast, intakes of students from outside the EU held up well, particularly from Asia. And inbound tourism continued to grow strongly compared with a year ago, notably from Asia and the US.

Manufacturing

Growth in domestic manufacturing output was broadly steady in the most recent period (**Chart 3**). Contacts in the electronics, aerospace and food and beverages sectors reported robust growth. A few contacts benefited from UK customers reshoring some production in order to manage their post-Brexit supply chains. There were a few reports of contacts expecting to accelerate precautionary stockbuilding in 2019 Q1. However, active contingency planning for Brexit tended to be concentrated among larger companies that generally had better access to working capital, and could therefore invest in planning and stockbuilding. Many contacts had not yet implemented contingency plans, consistent with the recent Agents' survey on preparations for EU withdrawal.

Box 1 New Agents' score for exports of services

The Agents have developed a new score to measure growth in services exports. This score is being published for the first time this month. Services exports account for around 45% of total UK exports, so the new score is a useful supplement to the existing score for exports of manufactured goods,⁽¹⁾ which has been published since 1997.

The services exports score covers the provision of both consumer and business services — such as professional and financial services, inbound tourism, IT and transportation services — by UK residents to non-residents. It measures the sterling value of total services exports in the past three months compared to the same period a year earlier.

Agents began scoring services exports in October 2017 and a short back-run of data has been provided alongside the other Agents' scores.⁽²⁾

The Agents' score indicates that services export values have been growing steadily over the past year at around long-run

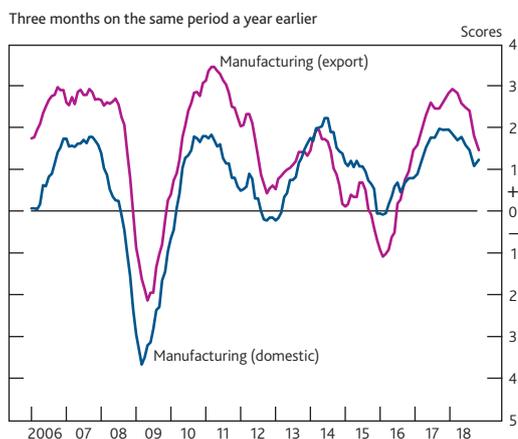
average rates. In contrast, growth in manufactured goods exports has weakened from robust rates in recent months (Chart A).

Chart A Agents' score points to continued growth in services exports



(1) Manufactured goods account for around 49% of total UK exports.
(2) See www.bankofengland.co.uk/-/media/boe/files/agents-summary/agentscores.xls.

Chart 3 Manufacturing output



Suppliers to the construction sector reported mixed demand. Some contacts reported continued growth in demand for construction materials for new warehousing, student accommodation and home improvements, but weaker housebuilding activity in some areas reduced demand for other materials.

In the automotive sector, declining output by some manufacturers fed through the supply chain, including to UK steel producers. And Brexit uncertainty weighed on demand for capital goods and consumer durables, as businesses and households became more cautious about committing investment and making large purchases.

Growth in the volume of manufactured goods exports eased to a modest pace (Chart 3). The slowdown reflected a combination of a waning boost from sterling's 2016 depreciation and weaker demand for diesel cars, rail and marine goods, notably from Asia. In addition, sales of construction equipment to some emerging economies slowed. There was some evidence of weaker demand from Turkey and Argentina. Growth in exports to the US was generally stronger than to the EU. That said, contacts reported steady growth in some exports to the EU, such as food, engineering and machine tools.

While EU clients have continued to source goods from the UK, contacts reported concerns about future prospects. This was partly due to Brexit-related issues such as tariffs and product approvals, but also amid concerns that China would seek to shift the focus of its exports away from the US towards the EU. Some contacts expressed concern that demand from the US could weaken, if US customers decided to source more domestically produced goods. A few contacts said that this had been experienced by their Chinese subsidiaries.

Construction

Output growth in the construction sector remained modest. Following a period of strong growth, there was a slight slowdown in housebuilding activity in some parts of the UK, particularly among larger housebuilders, who had become more cautious. However, this was partially offset by stronger demand for refurbishment and improvement work in housing,

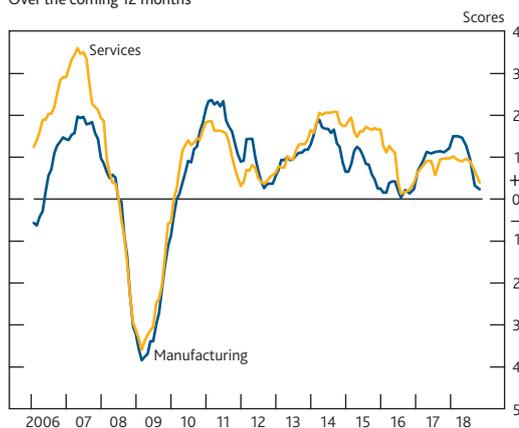
and for private rental developments. Construction of private non-residential property slowed, especially of retail premises and offices. Growth in civil engineering and infrastructure work held broadly steady, but contacts said larger projects remained vulnerable to delays, and contacts were concerned that some projects might be scaled back.

Investment

Investment intentions for the next 12 months continued to ease (Chart 4). Contacts reported a reluctance to commit to capital investment in the short term, preferring to wait for more clarity on the UK's future trading relationship with the EU. However, contacts continued to invest in projects aimed at increasing efficiency and productivity, particularly when faced with growing labour constraints and rising costs. There was increased investment in contingency infrastructure, such as warehousing, logistics and port capacity. And business and consumer services contacts invested in compliance-related IT upgrades.

Chart 4 Investment intentions

Over the coming 12 months



Corporate financing conditions

Corporate credit demand continued to soften, reflecting subdued investment intentions, and a slowdown in refinancing. There was some evidence of a slight softening in M&A activity, which had previously been boosted by activity being brought forward to avoid the period around Brexit. Contacts reported a general reluctance to increase borrowing, due to uncertainty about the economic outlook. However, some contacts expected to increase their working-capital and/or cash-flow borrowing to support stockbuilding.

Bank and non-bank credit remained readily available on the whole. However, the availability of credit and trade credit insurance continued to tighten for companies in sectors more vulnerable to an economic slowdown, such as construction, procurement and consumer-facing businesses. There were some reports that banks were asking more detailed questions about the anticipated impact of Brexit on businesses that applied for loans.

According to accountancy and insolvency practitioner contacts, restructuring activity and administrations ticked up in most sectors over the past three months, albeit from low levels, and could continue to rise in 2019. Companies in retail, casual dining, car dealership, further education and contract services continued to be vulnerable to distress. There were reports that delays to some construction projects were causing cash-flow difficulties in construction supply chains.

Property markets

Commercial real estate

Investor demand for UK commercial property remained modestly ahead of supply, reflecting a search for yield and the low supply of available stock in many areas. Investor appetite was weakest for retail properties, where vacancy rates continued to pick up, with demand most buoyant for distribution sheds and warehouses, in part reflecting the structural shift to online retail.

Contacts reported that investor demand for prime retail and office properties in London had held up better than expected. And demand from foreign investors for developments in major UK cities remained good. However, there were also growing concerns about the impact of Brexit on the commercial property market, and there were signs that development activity was starting to weaken, with some projects being delayed or put on hold.

Contacts in the property sector continued to report limited UK warehousing capacity for stockbuilding ahead of Brexit, though some capacity was likely to become available after Christmas. Some contacts reported rising rents for bonded warehouses and refrigerated storage in south east England.

Housing market

Estate agent contacts reported a general weakening in activity levels in the housing market, as the usual autumn pickup in activity failed to materialise in a number of regions. Although the stock of houses for sale remained low, contacts indicated that demand was also falling.

For example, there had been an increase in the number of purchases falling through due to uncertainty among potential buyers. More viewings were required before a sale could be achieved. And buyers were taking longer to reach a decision to purchase.

In addition, the difference between asking prices and offered prices had widened. Housing activity in southern England was muted, which contacts said was due to uncertainty among buyers and sellers, who were postponing transactions until after EU withdrawal.

Demand for new-build homes remained stronger outside London, although housebuilders reported having to offer more

incentives and undertake more viewings in order to complete sales. Labour shortages continued to constrain supply.

Mortgage activity was mostly concentrated in refinancing deals and homeowners moving from floating-rate deals to fixed-rate loans, with mortgage tenors often increasing to five years.

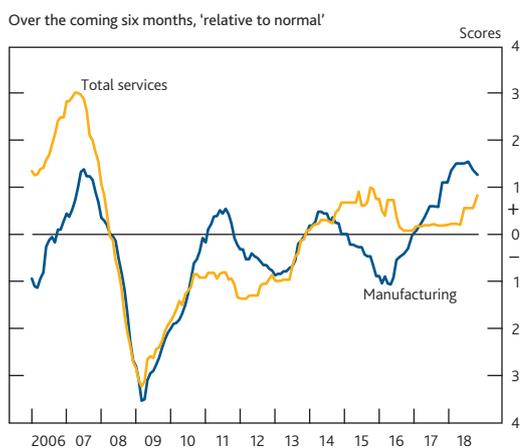
Contacts said that subdued demand for mortgages, combined with the entry of new lenders to the market, had resulted in intense competition. In turn, this has led to tighter pricing and improved availability of higher loan to value and loan to income mortgages, as challenger banks competed for higher-risk loans in order to grow market share.

Capacity utilisation

Capacity constraints remained above normal across the economy as a whole. Contacts reported that widespread labour shortages placed the biggest constraint on output. Constraints had eased slightly in manufacturing, but were tighter than in services, and remained above normal (Chart 5). Some food processors and packaging companies, for example, have had to increase shifts in order to meet demand. In contrast, there was excess capacity and staff cuts in parts of the automotive sector.

The slight increase in capacity constraints in services mainly reflected skill shortages within professional services and distribution, especially for drivers. There was very little spare capacity in warehousing and logistics. By contrast, contacts in consumer-facing services reported excess capacity.

Chart 5 Capacity constraints



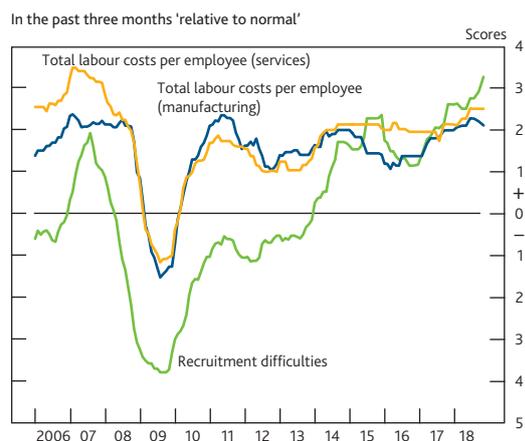
Employment and pay

Employment intentions were little changed in manufacturing. They picked up slightly in business services and weakened a little further in consumer services.

Recruitment difficulties intensified further (Chart 6) and became more widespread. Contacts in areas including IT,

professional services, construction, engineering, hospitality, health and social care and logistics reported that the inability to recruit sufficient numbers of staff was constraining output growth. They also reported that a lack of availability of EU migrant workers had exacerbated recruitment difficulties. In order to address the issue, companies were increasing intakes of apprentices and graduates, upskilling existing employees and investing in automation and technology.

Chart 6 Recruitment difficulties and total labour costs



Some contacts said that labour shortages had prompted them to be more selective about bidding for contracts, and to target work with higher margins. Staff turnover rates generally remained low, with employees cautious about moving jobs due to Brexit-related uncertainties. But there were reports that poaching of key staff and skills was becoming more prevalent in some sectors.

Pay settlements continued to be slightly higher than a year ago, and remained in a range of 2½%–3½%. Despite the tightening labour market, many contacts managed to contain pay bill growth by targeting pay awards at key skills or staff. The Agents' scores for total labour costs per employee held broadly steady (Chart 6).

Companies with a high proportion of low-paid staff concentrated pay increases on staff who were on or just above the National Living Wage. Alongside pay awards, many companies enhanced other elements of their overall packages, for example by offering flexible working and private healthcare. They did this partly to mitigate higher wage inflation, but also in response to employees' demands for improvements in their work-life balance.

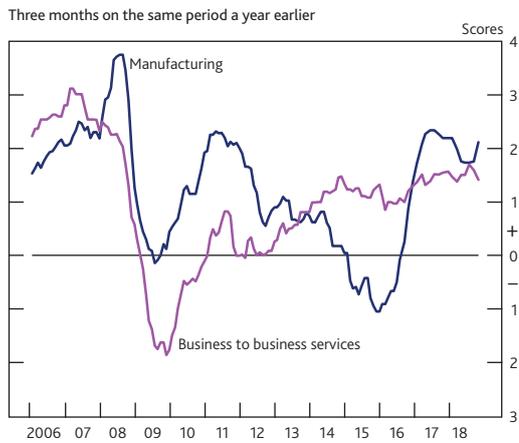
Costs and prices

Material cost inflation slowed for some commodities, including meat and dairy products. But it continued to rise for building materials and energy, where contacts reported increases of up to 25% when renewing two-year contracts. Costs of electrical components and paper continued to rise,

driven by strong global demand and restricted supply from European mills, respectively.

Manufacturers experienced less resistance to raising output prices to cover the rising cost of inputs, such as materials, labour and energy (**Chart 7**). However, suppliers of commoditised services continued to experience difficulty in implementing price increases. Many are seeking to stem the erosion of profit margins by focusing on higher-margin work, and taking measures to improve productivity.

Chart 7 Manufacturing and services prices



Consumer goods price inflation remained elevated relative to its historical average. Growth in fuel prices eased slightly but was still higher than a year ago. The pace of household electricity and gas price rises also picked up. Competitive pressures in food retail were likely to restrict the degree to which increases in producer prices would be passed through to consumers, with contacts expecting only modest inflation.

Consumer services price inflation was a little below average. Contacts reported modest price increases in sectors such as leisure facilities, tourist attractions, and social care. But often these increases did not fully cover rising labour and other costs.

Box 2 Results from the Decision Maker Panel survey

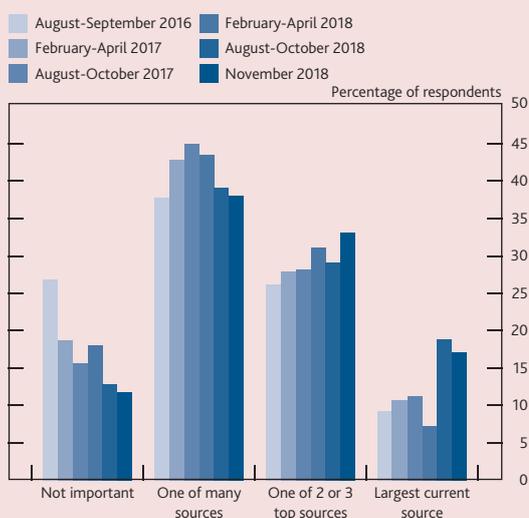
Overview

Together with academics from Stanford University and the University of Nottingham, the Bank has developed the Decision Maker Panel (DMP) survey to help monitor recent developments in the UK economy and to track businesses' expectations and the uncertainty surrounding them.⁽¹⁾ The responses from the DMP survey complement the intelligence gathered from contacts of the Bank's Agents.

The panel comprises Chief Financial Officers from small, medium and large UK companies operating in a broad range of industries. It is designed to be representative of the population of UK businesses. Around 6,600 businesses had agreed to be part of the panel at the time of the November survey. The survey runs monthly with panel members receiving one third of a quarterly questionnaire each month. The response rate has averaged around 45% in recent months. Aggregate-level data from the DMP survey are available on the Bank's website.⁽²⁾⁽³⁾

On 4 December, a summary of the latest DMP results relating to Brexit was published alongside the results of a survey by the Bank's Agents to coincide with the Treasury Select Committee hearing on the Bank's Brexit work.⁽⁴⁾ This covered a full set of quarterly data collected between August and October and estimates from November that were based on one third of the sample. The data showed that Brexit had created uncertainty for many businesses and that Brexit's importance as a source of uncertainty had risen further in recent months (Chart A).

Chart A Brexit as a source of uncertainty^(a)



Sources: DMP and Bank calculations.

(a) Question: 'How much has the result of the EU referendum affected the level of uncertainty affecting your business?'. Data for November 2018 are based on only one third of the sample.

This box provides some extra detail from the August to October surveys on the characteristics of firms that expect to

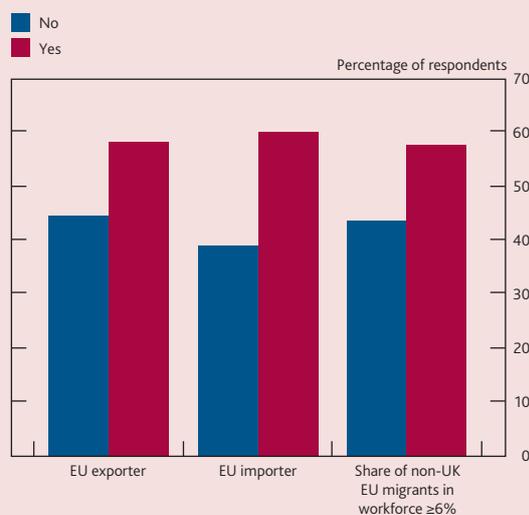
be affected by Brexit and summarises companies' views on the shorter-term prospects for their businesses.⁽⁵⁾

Characteristics of businesses affected by Brexit

According to the August to October DMP surveys, around 35% of companies reported that they export goods or services to other EU countries, while around 46% import some products from the rest of the EU. On average, exports to the EU made up 7% of total sales and EU imports accounted for 11% of costs in 2018 Q2 (of all firms, including those who do not export/import to/from the EU). Non-UK EU nationals made up an average of around 7% of the workforce among panel members.⁽⁶⁾

Businesses who are more exposed to the rest of the EU either through exporting, importing, or employing relatively more staff from other EU countries were more likely than others to view Brexit as an important source of uncertainty (Chart B). Within those who exported to or imported from the rest of the EU, uncertainty levels were higher for those who were more reliant on trade with the rest of the EU.

Chart B Firms who view Brexit as an important source of uncertainty, by exposure to the EU^(a)



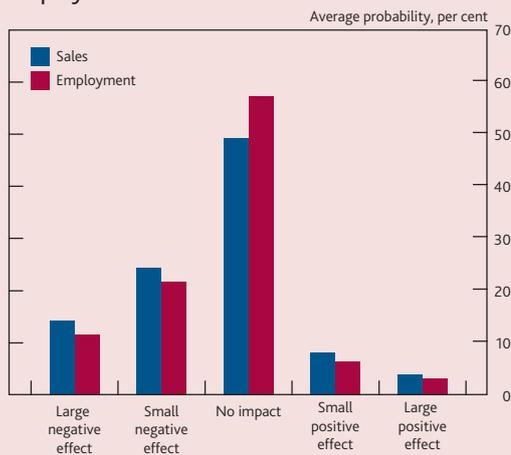
Sources: DMP and Bank calculations.

(a) Brexit uncertainty question is defined in the footnote to Chart A. Chart shows the percentage of firms who responded 'Largest current source' or 'One of 2 or 3 top sources'. Uncertainty data and information about whether a company exports or imports any goods or how many non-UK EU migrants it employs were collected between August and October 2018. If information about imports, exports, or the share of non-UK EU migrant labour was missing, responses from earlier surveys were used.

- (1) This project is supported by the Economic and Social Research Council (grant number ES/P010385/1).
- (2) For details on the methodology please visit www.bankofengland.co.uk/quarterly-bulletin/2017/q2/tracking-the-views-of-british-businesses-evidence-from-the-dmp. All results are weighted.
- (3) Aggregate data from surveys up to October and details on questions are available at www.bankofengland.co.uk/-/media/boe/files/statistics/research-datasets/dmp-results-december-2018.xlsx.
- (4) For details please visit www.bankofengland.co.uk/-/media/boe/files/agents-summary/2018/agents-survey-on-preparations-for-brexit.pdf.
- (5) For more in-depth analysis please visit <https://doi.org/10.1111/1475-5890.12179>.
- (6) Calculations are based on responses to the question 'Approximately what percentage of your employees were immigrants from the rest of the EU (...) in the latest quarter?'. Respondents could choose one of the following options: (a) Less than 1% (b) 1% to 5% (c) 6% to 10% (d) 11% to 20% (e) 21% to 50% (f) More than 50%; with the last two categories being merged into one. Values of 0.5%, 3.25%, 8%, 15.25%, and 27% were used as mid-points for the five categories and were multiplied by corresponding share of respondents to arrive at the average value.

As well as asking about the uncertainty created by Brexit, the DMP also asked panel members how they expected their sales and employment to be affected by Brexit over the longer term. No guidance was provided on what to assume about the form Brexit might take. On average, companies attached higher probabilities to Brexit eventually reducing their sales and employment than to increasing them (Chart C).⁽⁷⁾

Chart C Expected eventual impact of Brexit on sales and employment^(a)

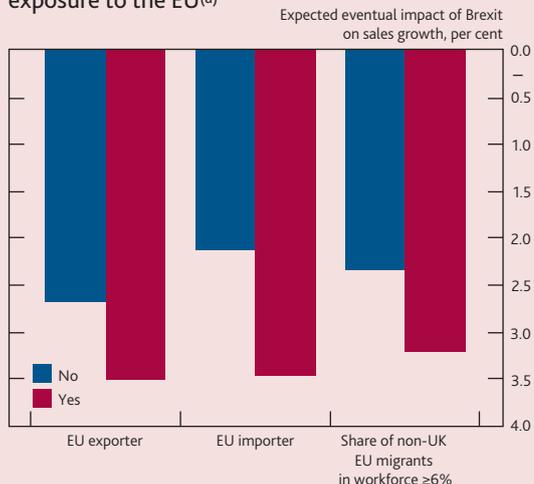


Sources: DMP and Bank calculations.

(a) Question: 'How do you expect the eventual Brexit agreement to affect your sales/employment once the UK has left the EU, compared to what would have been the case had the UK remained a member of the EU?' A large positive/negative effect corresponds to adding/subtracting 10% or more to/from sales/employment; a small effect is defined as less than 10%. Data are for August to October 2018.

Businesses who are more exposed to the EU through trade links or via their use of non-UK EU migrant labour expected Brexit to have a larger eventual impact on their sales and employment than those who are less exposed. Chart D illustrates this using some simple point estimates for the expected eventual impact of Brexit on sales.⁽⁸⁾ EU exporters, those who import from the EU, and firms who rely more on

Chart D Expected eventual impact of Brexit on sales by exposure to the EU^(a)



Sources: DMP and Bank calculations.

(a) Question about the impact of Brexit on sales is defined in the footnote to Chart C. Expected impact of Brexit on sales data and information about whether a company exports or imports any goods or how many non-UK EU migrants it employs were collected between August and October 2018. If information about imports, exports, or the share of non-UK EU migrant labour was missing, responses from earlier surveys were used.

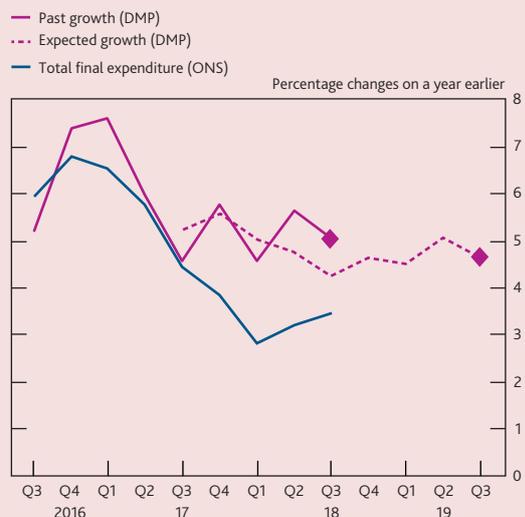
EU migrant labour all expected Brexit to have a larger impact on their sales in the long term than companies not in those categories.

The short-term outlook for sales growth

Over the past few quarters, companies' realised annual nominal sales growth appears to have held up and the short-term outlook for sales growth remains broadly unchanged.

Firms who responded to the sales questionnaire between August and October reported average nominal sales growth of 5.6% in the year to 2018 Q2, and those sampled in November reported slightly lower growth of 5.1% over the year to 2018 Q3 (Chart E). Firms who responded to the November survey expected sales growth to slow slightly to 4.6% over the year to 2019 Q3. In 2018, achieved and expected sales growth rates were relatively similar for exporters and non-exporters, whereas in earlier surveys exporters had reported higher sales growth.

Chart E Average expected and realised nominal sales growth^(a)



Sources: DMP, ONS and Bank calculations.

(a) Questions about sales refer to the last complete quarter. Realised data for 2018 Q3 and expected data for 2019 Q3 were collected in November and are based on data for one third of the sample only.

(7) Chart C shows data for August to October 2018. The sales question was also asked in November 2018. The 4 December report shows that the responses were little changed from August-October. The employment question was not asked in November 2018.
 (8) A point estimate for the expected eventual impact of Brexit on sales for each firm is constructed by multiplying simple mid-points for the five response categories shown on Chart C by the probabilities assigned to them. Values of ±20% are used for a large positive/negative impact and ±5% for a small positive/negative effect. Zero is used for no impact.