

# Summary

## 4th Quarter 2015

Although the key national balances remained positive in Q4 2015, pointing to continued growth, they confirm that the UK economy is facing challenges. In both the manufacturing and services sectors, most key balances were weaker in Q4 2015 than in Q3, with the manufacturing results suffering to a greater degree. The domestic and export manufacturing balances for both sales and orders are now well below their pre-recession levels in 2007. The sharp decline in the Q4 export manufacturing balances, to levels approaching stagnation, is particularly disturbing. However, there were some positive results in the Q4 survey, as the balances for investment in plant & machinery rose for both the manufacturing and services sectors. Capacity utilisation was high in both sectors, in spite of the falls in the domestic and export balances. The need to build new capacity, as labour costs increase, may explain the increase in Q4 investment balances at a time of slowing demand. Intentions to increase prices rose markedly in manufacturing and fell slightly in services. Both manufacturing and service firms also report sharply increased pressures for higher pay settlements.

### Domestic Market

The domestic balances fell in Q4 2015 for both manufacturing and services. In the manufacturing sector, the domestic balances dropped further below their pre-recession levels in 2007. The balance of manufacturing firms reporting improved domestic sales was +13% in Q4 2015, down from +20% in Q3 2015, and is now at the lowest level since Q1 2013. The balance for manufacturers' domestic orders was +10% in Q4, down from +18% in Q3, and is at the lowest level since Q4 2012. The service sector's balance for domestic sales fell from +36% in Q3 2015 to +32% in Q4 2015, the lowest level since Q3 2013. The service balance for domestic orders was +23% in Q4, down from +29% in Q3, the lowest level since Q2 2013.

### Export Market

The national export balances weakened in Q4 2015 for both manufacturing and services. The balance of manufacturers reporting improved export sales fell by nine points in Q4 2015, to +1%, the lowest level since Q3 2009. The manufacturing sector balance for export orders also fell to +1%. The service sector balance for export sales fell by three points in Q4 2015 to +15%, the lowest level since Q4 2011. The service balance for export orders fell by seven points in Q4 to +9%, also the lowest level since Q4 2011.

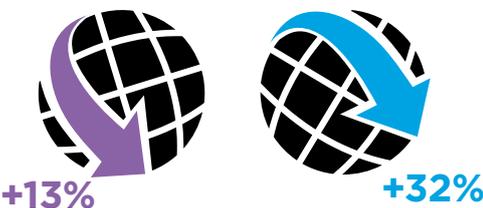
### Employment

The national employment balances weakened in Q4 2015 for both manufacturing and services. In the manufacturing sector, the balance of firms reporting an increase in their labour force over the last three months fell to +20%. The balance of manufacturers expecting their labour force to expand in the next three months fell five points to +17%, the lowest level since Q1 2013. In the service sector, the backward-looking employment balance fell one point in Q4 2015, to +23%. The forward-looking service employment expectations balance fell by three points in Q4 to +21%, the lowest level since Q1 2013.

### Investment

The balance of manufacturing firms that have revised upwards their plans to invest in plant & machinery rose by six points in Q4 2015 to +24%. The balance of manufacturers that have revised upwards their plans to invest in training rose by three points in Q4 to +23%. The balance of service firms that have revised upwards their plans to invest in plant & machinery rose three points in Q4 2015 to +20%. The balance of service firms that have revised upwards their plans to invest in training fell by one point in Q4 to +26%.

The domestic sales balance fell for both the **manufacturing** and **services** sectors



The balance of firms who increased their workforce in Q4 fell for both **manufacturers** (+20%) and **service firms** (+23%)



### Business Confidence

The national manufacturing confidence balances, after falling in Q3, were broadly stable in Q4 2015, recording very small divergent movements. The balance of manufacturing firms confident that turnover will improve in the next 12 months fell from +43% in Q3 to +42% in Q4, the lowest level since Q4 2012. The balance of manufacturing firms confident that profitability will improve in the next 12 months rose from +32% in Q3 to +33% in Q4. The balance of service sector firms expecting turnover to improve in the next 12 months fell markedly from +54% in Q3 to +45% in Q4, the lowest level since Q1 2013. The balance of service sector firms expecting profitability to improve in the next 12 months fell from +42% in Q3 to +41% in Q4.

### Capacity Utilisation

Capacity utilisation in Q4 2015 rose in the manufacturing sector and was unchanged in the service sector. The percentage of manufacturing firms operating at full capacity increased by five points in Q4 to 41%, joint highest level since Q4 2014. The percentage of service firms operating at full capacity was unchanged in Q4 at +48%, an all-time high for our survey.

### Cashflow

The balance of firms reporting improvements in cashflow recorded divergent movements in Q4 2015, rising for manufacturing and falling for services. The balance of manufacturers reporting improved cashflow rose from +9% in Q3 to +12% in Q4, still slightly lower than its average 2007 pre recession level. The balance of service sector firms reporting improved cashflow fell two point in Q4, to +14%, the same as the average 2007 level.

### Prices

Intentions to increase prices rose markedly in the manufacturing sector and fell slightly for service firms. The balance of manufacturing firms reporting an intention to raise prices rose by eleven points in Q4 2015 to +19. The balance of service firms expecting to raise prices fell two points in Q4 to +21%. Both manufacturing and service firms report sharply increased pressures for higher pay settlements.

## A view from BCC Chief Economist David Kern

Coming after relatively weak figures in our Q3 survey, the falling balances in Q4 highlight the risk that the pace of growth may slow further in the short term. The results also underscore the serious obstacles that the UK will face when trying to rebalance the economy towards net exports. While worsening global circumstances are the main impediment, the domestic drive towards boosting net exports is also inadequate. Though vibrant and resilient services will remain the UK's main growth driver, the Q4 results indicate that the service sector is also losing some of its momentum. However, the challenges facing manufacturing are much more serious. The fall in the manufacturing export balances to levels approaching stagnation are a stark reminder that designing a national exports strategy, and placing greater emphasis on promoting exports in services, must be major priorities. While we must not forget the strengths of the UK economy, with higher growth than in most G7 economies and a dynamic and flexible labour market, the recovery is still fragile. Given the global uncertainties, it is important to avoid unnecessary risks. Though wage pressures are rising, inflation is likely to remain below target over the next 18 months. The MPC should therefore keep interest rates at their current low for the time being.

The balance of **manufacturers** expecting prices to rise increased sharply to +19%



The QES balance for exports sales fell to +1% in the **manufacturing sector** and +15% for the **service sector**.

