



Agents' summary of business conditions

February 2016 Update

- Growth had eased a little in recent months, although remained solid overall. While services growth had remained relatively buoyant, manufacturing was contracting, reflecting subdued world growth, the earlier appreciation of sterling, and weak demand from extraction industries in particular.
- Consumer spending growth had been resilient. Some retail contacts suggested that purchases had been brought forward from December into November, because of Black Friday, or held back until the January sales. Retail contacts expected positive annual growth in sales during the first quarter.
- Employment intentions and recruitment difficulties had eased, although the latter remained above normal levels. In a survey, contacts expected a slight pickup in pay settlements in 2016, largely reflecting the introduction of the National Living Wage.

Annual growth in **consumer spending** had remained resilient (**Chart 1**). Some contacts reported that purchases had been brought forward from December to Black Friday, or held back to the January sales. Most contacts had positive expectations for retail sales values growth in the first quarter. Consumer services growth had eased a little.

Business services turnover growth had been firm overall, although remained somewhat stronger for professional and financial services than for other companies (**Chart 2**).

Manufacturing output growth was slightly down on a year earlier (**Chart 3**). Domestic output was broadly unchanged on a year earlier, but exports had declined, reflecting a slowdown in world demand, the earlier appreciation of sterling and weak demand for capital goods from the extraction sector in particular.

Construction contacts reported an easing in annual output growth, partly reflecting the strength of activity a year ago. Some house builders had become more cautious about prospects, partly reflecting concern over a lack of suitably skilled staff and rising costs.

Investment intentions were consistent with unchanged capital spending in manufacturing, but continued growth among services firms, mirroring the pattern of demand (**Chart 4**).

Competition among banks had continued to lower the cost of **corporate credit**, with some relaxation reported in covenants.

Occupier demand for **commercial real estate** had risen, particularly for warehousing and distribution facilities. There were, however, some reports of easing investment demand from the Middle East and China.

Housing market activity had remained subdued relative to pre-crisis levels, reflecting a lack of properties for sale. Many estate agents reported a persistent weakness in the pipeline for transactions.

Capacity utilisation was slightly below normal in manufacturing and slightly above normal in services.

Employment growth intentions had softened overall, as companies sought to increase productivity growth. The manufacturing workforce was expected to contract slightly over the next six months. **Recruitment difficulties** remained above normal (**Chart 5**) but had eased alongside softening employment intentions and as companies' efforts to increase training and apprenticeships fed through.

Labour cost growth had remained modest overall. A survey indicated that companies expected a slight pickup in settlements in 2016, concentrated among consumer services firms (see box on page 2). That was often reported to reflect the introduction of the National Living Wage.

Materials costs and **imported finished goods prices** had remained lower than a year earlier, with the annual rate of decline unchanged.

Manufacturing **output prices** were lower than a year ago, but modest price inflation among business services firms had continued (**Chart 6**). Companies generally reported difficulty in raising prices in a low inflation environment.

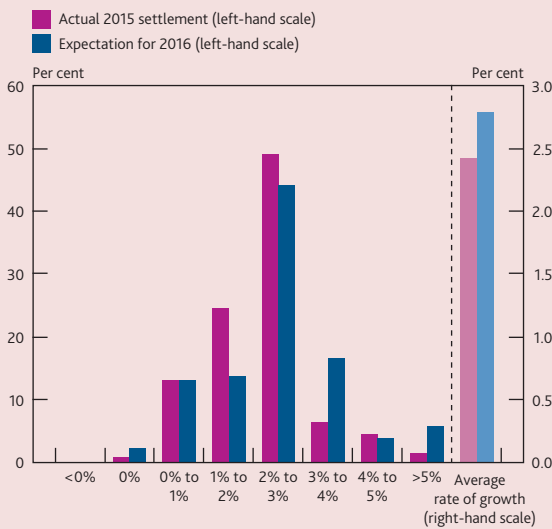
Consumer prices for goods remained lower than a year earlier, with further falls in petrol and food prices having helped sustain the annual rate of decline. Consumer services price inflation had remained modest.

Agents' survey on pay and labour costs

The Agents have conducted an annual pay survey since 1998, asking private-sector contacts about pay settlements in the past year, expectations for the year ahead, and the key drivers of any changes to growth in total labour costs per employee. This year 342 firms responded, with a combined employment of around 600,000 staff. The results of the survey have been weighted by employment and re-weighted by sectoral employment shares to adjust for differences in the composition of the survey compared with the economy as a whole.

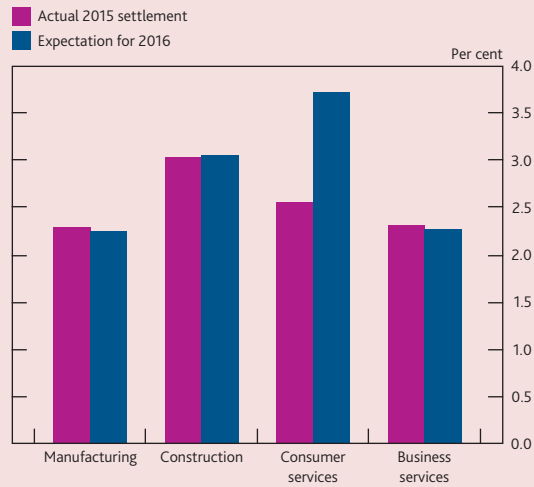
The average settlement was expected to rise in 2016, to 2.8%, from a reported average outturn of 2.4% in 2015 (**Chart A**). Looking at the distribution of responses, fewer settlements of between 1% and 3% were expected for 2016 than for 2015, with a comparable increase in the number of settlements over 3%. At a sector level, pay settlements for manufacturing, construction and business services firms were expected to increase at a similar rate to last year, but a big pickup was anticipated in consumer services awards, from 2.5% last year to 3.7% this year (**Chart B**).

Chart A Distribution and average rate of pay settlements



Broadly consistent with the expected pickup in settlements, a net balance of nearly 40% of respondents expected total labour cost growth per employee (a wider measure that includes regular pay, overtime payments, performance related pay, bonuses, employer pension contributions and employee benefits) to increase in 2016, compared with an equivalent figure of just over 20% in last year's survey. Expectations of increases in cost growth were strongest for construction and consumer services companies.

Chart B Pay settlements by sector



Looking at the factors driving changes in labour cost growth per employee, in last year's survey firms expected consumer price inflation and the ability to pass on cost increases to pull down cost growth in 2015. The near-zero balance for these factors in this year's survey (**Chart C**) indicates a similar expected drag on growth in 2016. In contrast, staff retention issues and changes in productivity were expected to exert further upward pressure on costs growth. The introduction of the National Living Wage was the single most commonly-cited factor driving up labour cost growth, however, with positive net balances of nearly half of consumer services firms and nearly 30% for business services and manufacturing businesses reporting upwards pressure from this source.

Chart C Influences on growth in total labour costs per employee, 2016 relative to 2015



Selected charts of the Agents' national scores

Chart 1 Retail sales values and consumer services turnover

Three months on the same period a year earlier

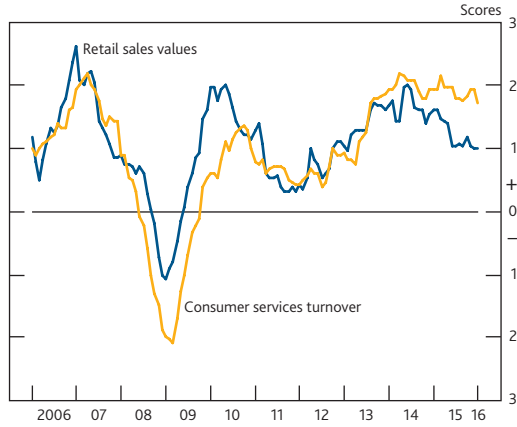


Chart 2 Business services turnover

Three months on the same period a year earlier

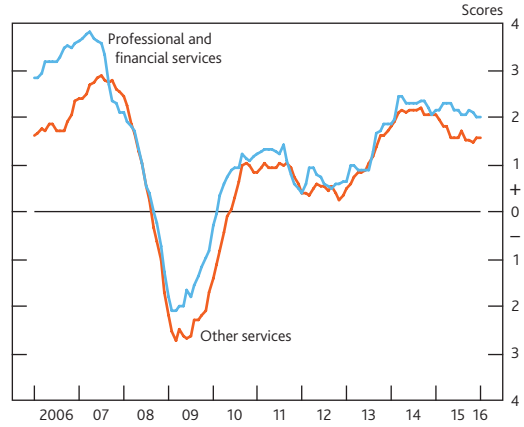


Chart 3 Manufacturing output

Three months on the same period a year earlier

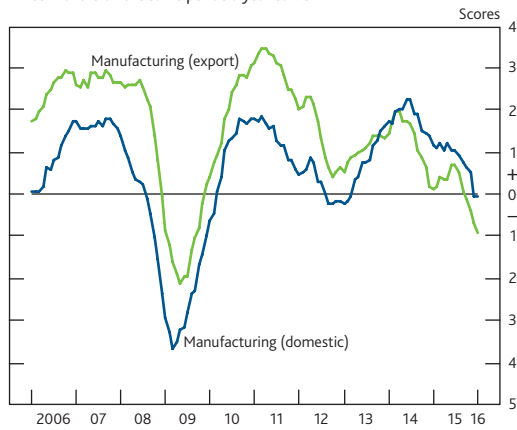


Chart 4 Investment intentions

Over the coming twelve months

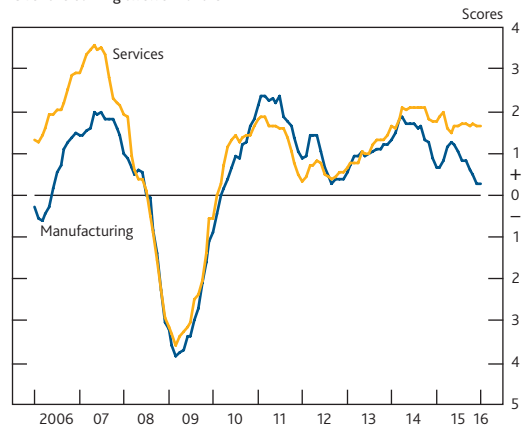


Chart 5 Recruitment difficulties

In the past three months, 'relative to normal'

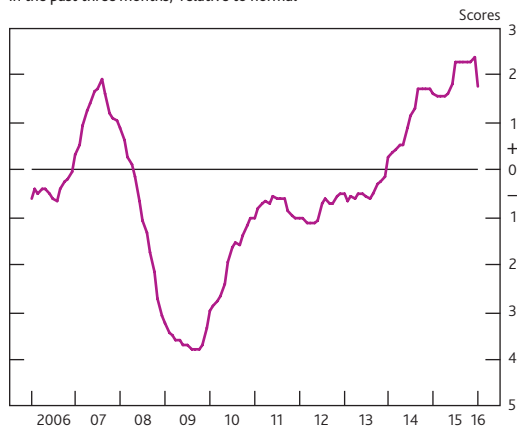
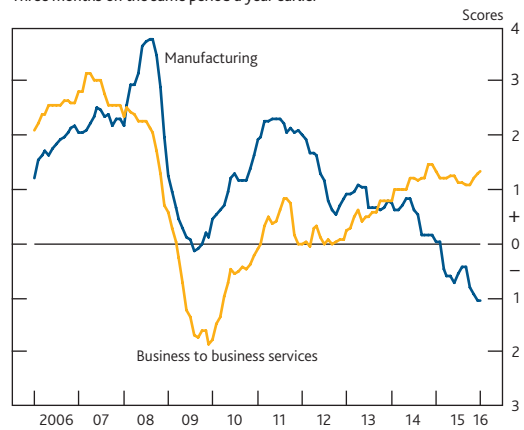


Chart 6 Output prices

Three months on the same period a year earlier



For data on the full set of Agents' scores see www.bankofengland.co.uk/publications/Documents/agentssummary/agentsscores.xlsx.