BANK OF ENGLAND

Agents' summary of business conditions

November 2016 Update

- Business sentiment had recovered further from its post-referendum fall, but remained relatively fragile alongside significant uncertainty around the longer-term outlook. Activity growth had remained resilient.
- A survey pointed to broadly stable or slightly lower investment spending over the coming twelve months (see box on page 2), with uncertainty concerning future demand and trading arrangements expected to drag on spending.
- Employment was expected to be broadly flat over the next six months and pay settlements were concentrated in the 1–3% range. Price pressures were building through supply chains following sterling's depreciation, but there had been limited impact on consumer prices to date.

Annual **consumer spending** growth had recovered further (**Chart 1**). Spending on luxury items had increased as overseas tourists took advantage of sterling's fall. Demand growth for new cars had continued to soften.

Business services turnover growth had increased a little since August, remaining modest (**Chart 2**). Contacts in the sector remained cautious about business prospects.

There had been a modest increase in **manufacturing output** growth for both domestic and export markets (**Chart 3**). Sterling's depreciation had aided manufacturing exporters and UK businesses competing against imports.

Construction output growth had eased (**Chart 4**), although sentiment had improved since the low levels of July.

A survey of **investment intentions** pointed to broadly stable or slightly lower investment spending in the year ahead (see box on page 2). Uncertainty concerning future demand and trading arrangements was expected to drag on investment. Current investment plans were focused on gains in productivity and efficiency that could be realised in the short term.

Credit availability and associated terms were little changed, while credit demand from businesses had remained subdued.

Investor demand for UK **commercial real estate** had continued to recover although sentiment remained fragile and transactions remained low by historical comparison. Rents had continued to rise in many parts of the United Kingdom.

Housing market activity had recovered since the weakness seen in the immediate aftermath of the referendum, but the extent of the pickup was variable across regions and price brackets.

Manufacturing **capacity utilisation** had remained a little below normal, but had picked up for exporters. In services, utilisation was slightly above normal but labour constraints in professional services had eased.

Employment intentions were consistent with stable private sector employment over the coming six months. Costs associated with the National Living Wage had been weighing on recruitment plans for some consumer services businesses. **Recruitment difficulties** had edged down a little further, remaining modestly above normal.

Growth in total **labour costs** had remained unchanged with most pay awards ranging between 1% and 3%, with slightly higher settlements in services than in manufacturing.

Sterling's depreciation had increased **input costs** in many sectors (**Chart 5**). Manufacturing **output price** inflation had turned positive and was expected to pick up further as foreign currency hedges and fixed-price contracts expired. Overall, corporate profit margins remained slightly lower than normal.

Consumer price inflation had started to rise, especially for goods (**Chart 6**). Pass-through of higher prices in supply chains to consumer prices had so far been limited, reflecting strong competition between retailers.

A change to Agents' scoring of profitability
Alongside this edition of the Agents' Summary, a change has been made to the published scores for corporate profitability, with the aim of providing a measure that is more relevant to how companies set prices. These scores will in future be published as profit margins relative to normal, rather than as changes on a year earlier, as has previously been the case. A year's backrun of the new measures are also provided, alongside the other Agents' scores, at www.bankofengland.co.uk/publications/Pages/agentssummary/default.aspx.

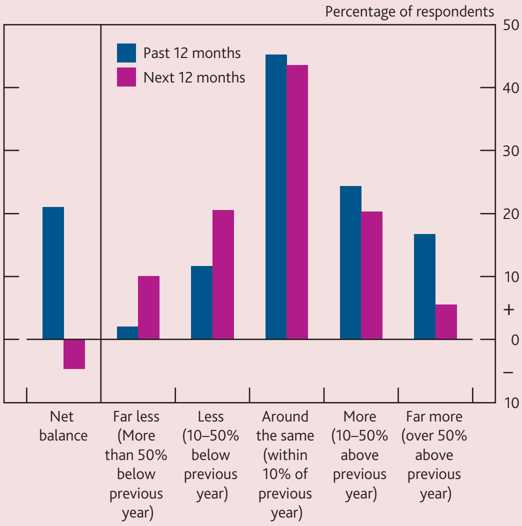
This publication generally covers intelligence gathered from business contacts between late August 2016 and mid-October 2016. It generally makes comparisons with activity and prices over the past three months on a year earlier.

Agents' survey on investment intentions

The Agents surveyed business contacts about changes to investment over the past twelve months and their plans for the twelve months ahead. The survey also asked how a range of factors were affecting these investment plans. In addition, firms were asked for information on criteria used to make investment decisions, and when and how these have changed. Around 340 businesses responded to the survey, accounting for 330,000 UK employees and £8.6 billion of UK capital spending. The survey results were weighted by employment.

Overall, firms in the survey reported expectations of broadly stable or slightly lower investment spending in the year ahead, after quite a significant increase in investment over the past year (**Chart A**).

Chart A Change in investment, past twelve months and expectations for next twelve months

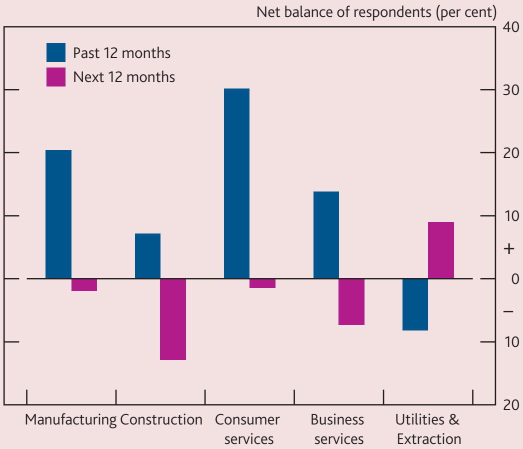


Notes for chart

(a) For this and subsequent charts, results are weighted by employment within the companies, and then re-weighted by sectoral employment shares in aggregate ONS data.
(b) When calculating the net balance of responses, half weight is given to those responding 'less' or 'more', and full weight is given to those that have responded 'far less' or 'far more'.

Looking across sectors (**Chart B**), expectations for investment spending growth in the coming twelve months were most negative for construction and business services, particularly among financial services companies. Expectations among manufacturing and consumer services companies were for broadly flat investment. By type of capital asset, investment plans were weakest for buildings and structures, which could explain the cautious outlook among construction firms.

Chart B Past and expected change in investment by sector



Among factors driving investment decisions, the most positive influences were the desire to achieve future efficiency gains and to provide capacity to meet expected demand (**Chart C**). Uncertainty about the demand outlook was the biggest drag on investment plans, particularly in manufacturing and construction. Uncertainty about future trading arrangements was the other main negative factor, especially for manufacturers. The results suggest that, in aggregate, pension deficits are not having a significant impact on firms' investment plans for the coming year.

Chart C Factors affecting investment in the next twelve months

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

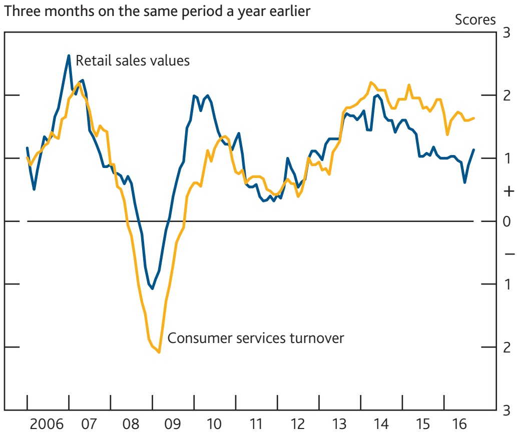


Chart 2 Business services turnover

Three months on the same period a year earlier

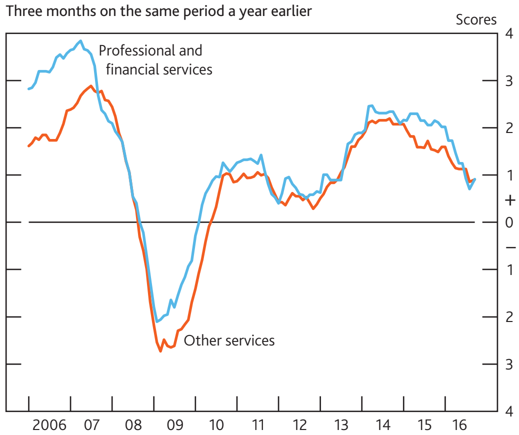


Chart 3 Manufacturing output

Three months on the same period a year earlier

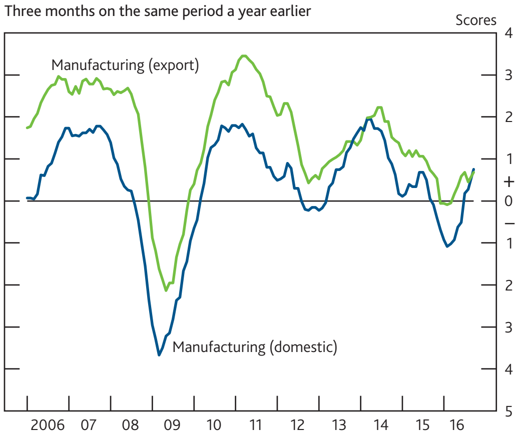


Chart 4 Construction output

Three months on the same period a year earlier

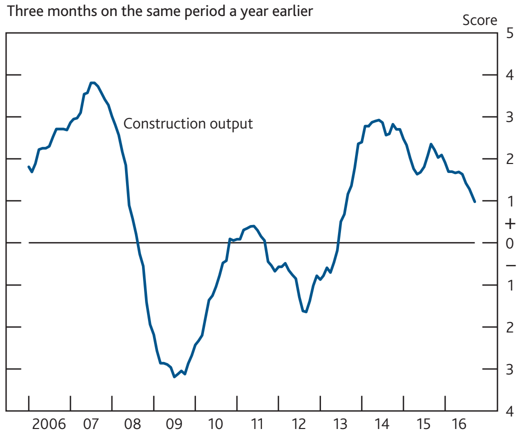


Chart 5 Materials costs and imported finished goods prices

Three months on the same period a year earlier

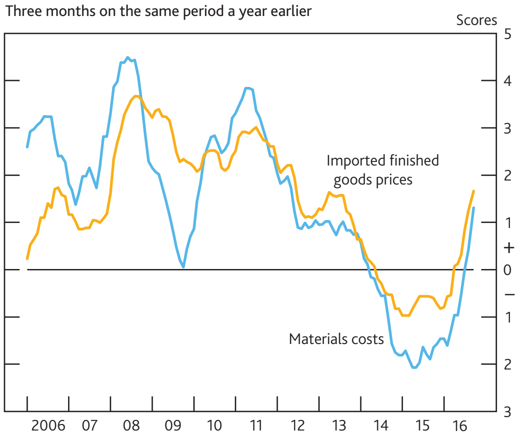
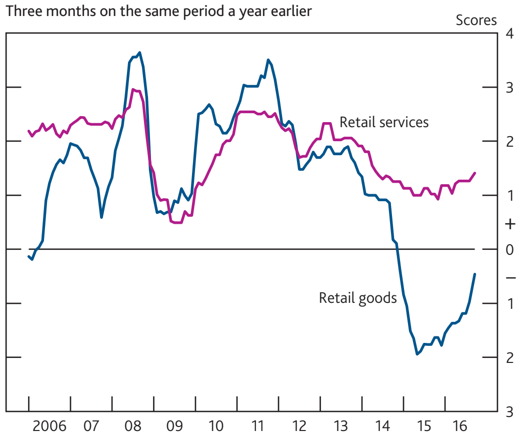


Chart 6 Retail goods and services prices

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.