QES LANCASHIRE QUARTERLY ECONOMIC SURVEY

Quarter 1, 2017

North & Western Lancashire Chamber of Commerce

In association with

Moore & Smalley
Trusted Thinking

About this Quarter's Survey

The Q1 2017 Survey was conducted by the North & Western Lancashire Chamber of Commerce, the Chamber of Commerce East Lancashire, and the Lancaster District Chamber in conjunction with Moore & Smalley Chartered Accountants and Business Advisors.

- The survey collection period was between 20th February and 13th March 2017.
- Responses were received from 279 companies across Lancashire employing 14,909 people.
- From the manufacturing sector, 111 business (40%) employing 8,108 people responded to the survey.
- From the service sector, 168 businesses (60%) employing 6,801 people responded to the survey.
- 182 companies (65%) were involved in exports.

NB: The net balance figures referred to throughout this report are calculated by subtracting the percentage of businesses reporting a decrease in a factor from those reporting increases. A figure above 0 indicates growth, while a figure below 0 indicates contraction.

Summary

This quarter's survey shows that Lancashire businesses are reporting solid growth and that business confidence is beginning to improve after a period of uncertainty in the aftermath of the vote to leave the European Union.

The Q1 2017 survey, compiled in association with Moore and Smalley Chartered Accountants and Business Advisors, shows that the manufacturing sector performed strongly in the first quarter of the year, particularly in the exports market, with the number of firms reporting improved sales and orders higher than in previous quarters.

The services sector continues to rebound from its initial shock in the months immediately after the EU referendum, and while growth has not yet returned to historic levels, it remains a key driver of the Lancashire economy.

The results also found that businesses are continuing to feel inflationary pressures. The percentage of manufacturers reporting raw materials as the key driver of increased prices remains way above the historical average, and in both sectors a significant proportion of firms anticipate having to raise their own prices over the next three months.

Inflation is a key risk to the UK's growth prospects, with businesses having to manage rising costs and the pressure to raise their prices. If higher inflation squeezes consumer spending as we expect, the current strength in business activity may not be enough to prevent a period of more muted economic growth.

Key Findings in the Q1 Survey:

- Overall, the figures for both sectors indicate continued expansion. While the services sector has not yet returned to historic trend levels, it is moving towards it

- The percentage balance of manufacturing firms expecting the price of their goods to increase over the next three months remains at historic highs, despite falling slightly from last quarter from +55% to +39%. In the services sector, the balance of firms expecting prices to rise eased from +44% to +37%

- 71% of manufacturers report an increase in the price of raw materials (down from 74%), while 28% of service businesses saw their raw material costs increase (down from 31%). 32% of manufacturers report an increase in the cost of other overheads (up from 23%), while 36% of services did (down from 39%)

- In the manufacturing sector, the balance for firms reporting increased domestic sales rose from +14% to +19%, and orders rose from +2% to +13%. The balance of firms reporting improved export sales rose from +15% to +25%, and the balance of export orders also increased from +12% to +21%

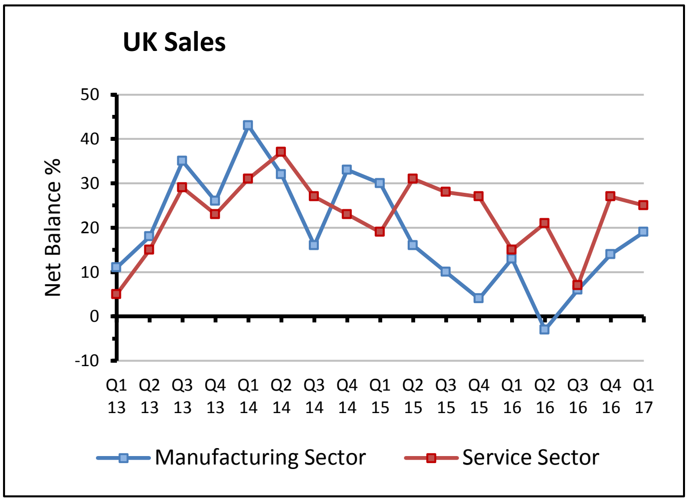
- In the services sector, the balance of firms reporting improved domestic sales fell marginally from +27% to +25%, and orders from +23% to +21%. Exports remained weak, with the balance for sales rising from +4% to +6%, and export orders falling from +4% to neutral.

- The percentage of businesses trying to recruit remained static in both sectors, standing at 58% in manufacturing and 44% in services. However, both sectors continue to experience high levels of recruitment difficulties, with the percentage standing at 56% in manufacturing (previously 46%) and growing to 63% in services (previously 59%)

- The balance of manufacturers confident that turnover would improve over the next 12 months rose significantly from +41% to +61%, whilst the manufacturing profitability balance increased from +23% to +29%. Confidence remains high in the service sector despite the turnover balance weakening slightly from +54% to +51%. The service sector profitability balance gained two points, increasing from +36 to +38.

+Positive number represents an expansion **-Negative number represents a contraction**

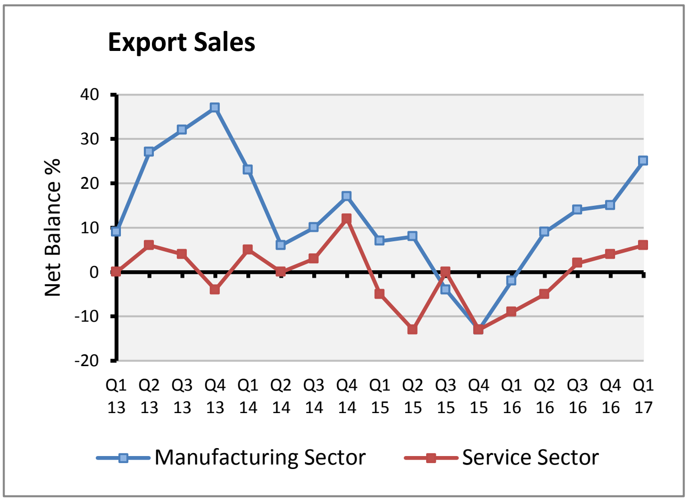
Domestic Market



The manufacturing sector enjoyed a third successive quarter of improvement in Q1, as the domestic sales balance gained five points on the previous quarter (+19, up from +14). This is the strongest quarterly sales balance since Q1 2015. The manufacturing orders balance also improved this quarter, up eleven points (+13, up from +2).

Despite a slight weakening in both domestic balances in Q1, service sector growth remains stronger than in manufacturing. The services domestic sales balance weakened slightly (+25, down from +27) but is ten points stronger than a year ago. The domestic orders balance also lost two points this quarter (+21, down from +23) but remains above its historical average.

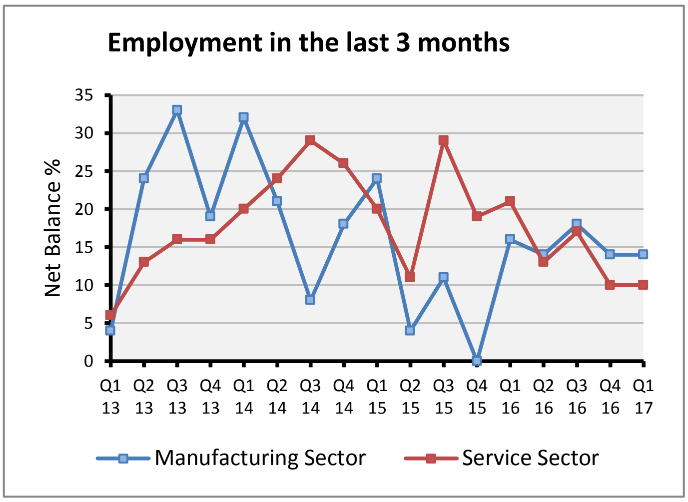
Export Market



From being in contraction a year ago, manufacturing export sales have continued to show signs of steady growth. The export sales balance was up ten points this quarter (+25, up from +15), its strongest position since Q1 2014. The manufacturing export orders balance gained nine points (+21, up from +12) and was also at its highest point for three years.

The service sector export sales balance improved slightly in Q1 (+6, up from +4) but continues to be historically weak compared to manufacturing. The services export orders balance weakened by four points to neutral.

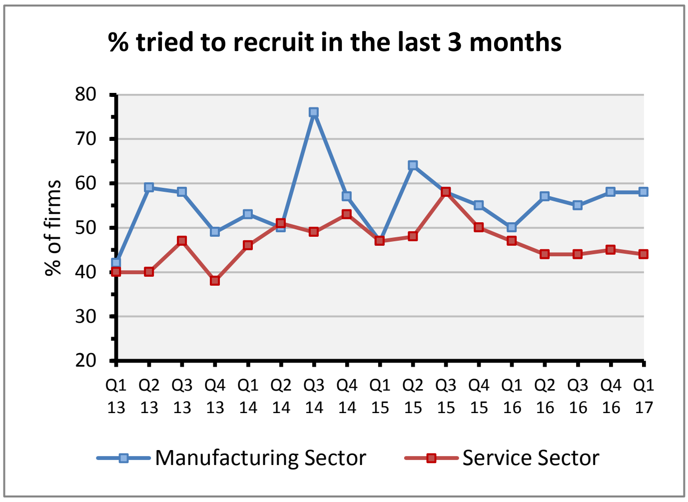
Employment



There was no change in either of the retrospective employment balances in Q1. The services employment balance held at +10; whilst the manufacturing employment balance was static at +14. In real terms, 24% of firms across both sectors reported that their labour force had increased in the past three months, whilst 12% reported a fall in numbers.

Looking at employment expectations over the next three months, the forward-looking employment balance for manufacturing gained five points (+27, up from +22); whilst the service sector balance was up six points (+29, up from +23). The figures are encouraging for the Lancashire economy and would support government data that unemployment is falling and numbers in work are increasing.

Recruitment

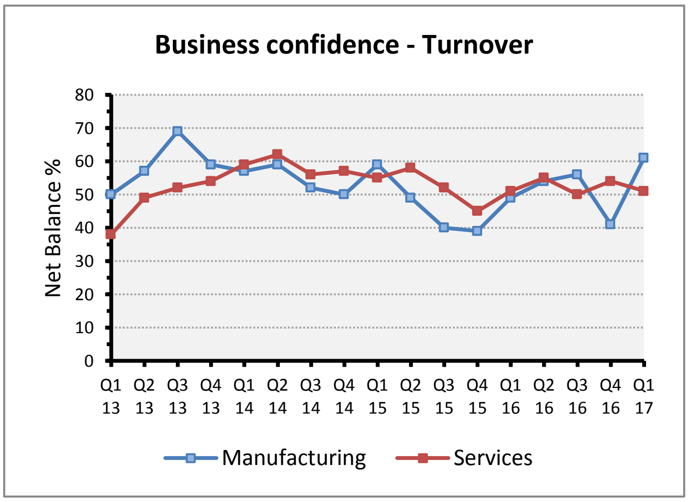


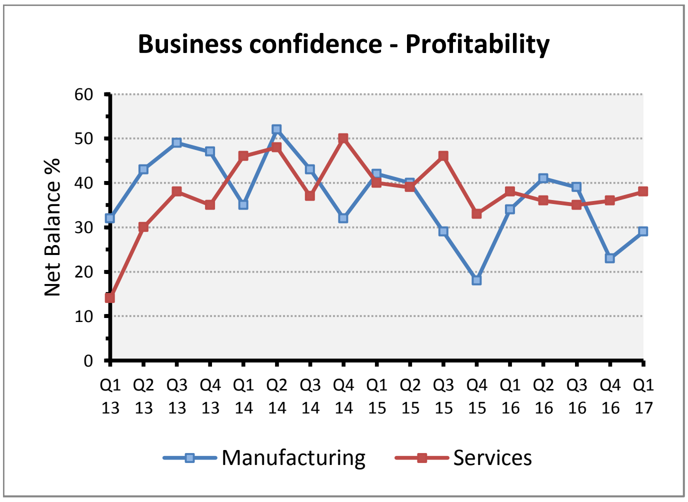
The overall percentage of firms attempting to recruit in the last three months remains unchanged from the previous quarter (49%). However, a greater percentage of manufacturing firms were attempting to recruit (58%) than their service sector counterparts (44%).

Of all firms attempting to recruit, 47% were seeking to fill permanent vacancies (unchanged), with 21% looking to take on temporary workers (down 1%). 78% of firms attempted to recruit for full-time positions (up 7%), whilst 25% were offering part-time roles (up 5%).

More than half of firms attempting to recruit said they experienced difficulties finding suitable staff (60%, up from 54%). For manufacturing firms, skilled manual and technical positions continue to be the most difficult to fill (65%, up from 56%). Service businesses found that professional/managerial positions were the most difficult for them to fill this quarter (51%, down from 56%).

Business confidence

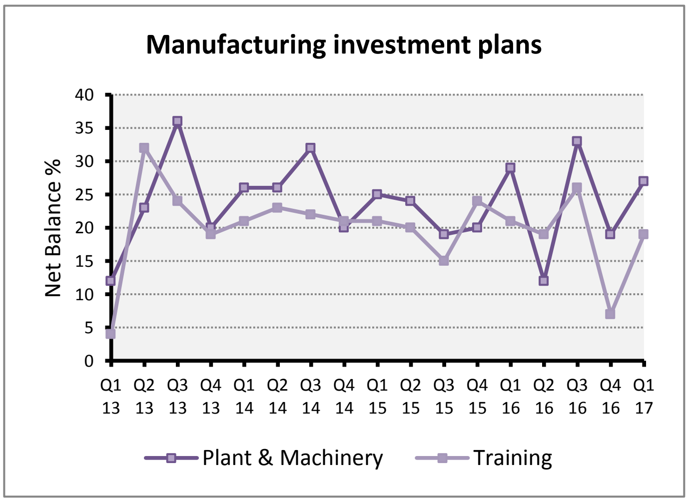


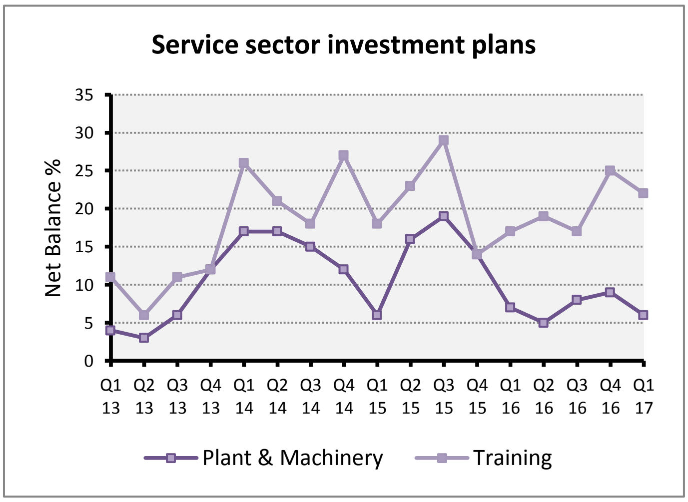


Looking at turnover and profitability expectations over the next 12 months, there is a notable improvement in business confidence amongst Lancashire manufacturers which appeared to have taken a dip towards the end of 2016 following the result of the EU referendum. The net balance of manufacturing companies expecting turnover to improve in the coming year was up twenty points (+61, up from +41), whilst the manufacturing profitability balance gained six points (+29, up from +23).

In the service sector, both measures of business confidence have held steady since Q1 2016. This quarter's survey is no exception with very little fluctuation in turnover and profitability expectations for the coming year. The net balance of service firms expecting turnover to improve was down three points (+51, down from +54) whilst the service sector profitability balance gained two points on the previous quarter (+38, up from +36).

Investment intentions

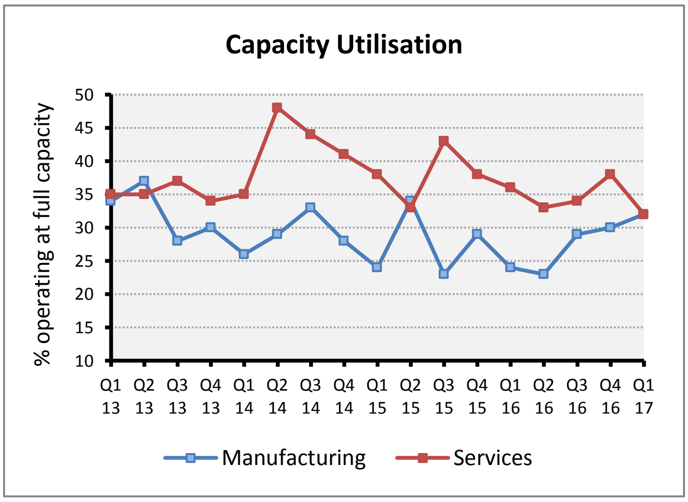


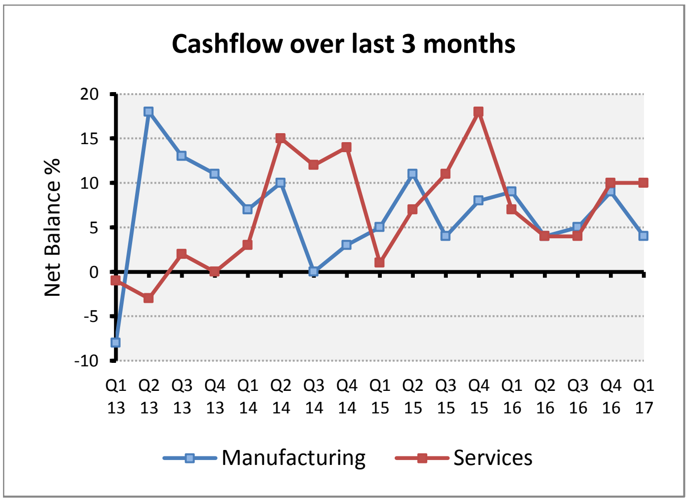


After a sizeable dip in Q4 2016, both of the manufacturing investment balances bounced back this quarter as more firms revised their investment plans upwards. The plant & machinery investment balance increased by eight points (+27, up from +19); whilst the manufacturing training investment balance gained twelve points (+19, up from +7).

There was a slight weakening in investment intentions amongst service businesses. The training investment balance lost three points (+25, down from +22), whilst the capital investment balance also lost three points (+6, down from +9).

Capacity Utilisation and Cashflow

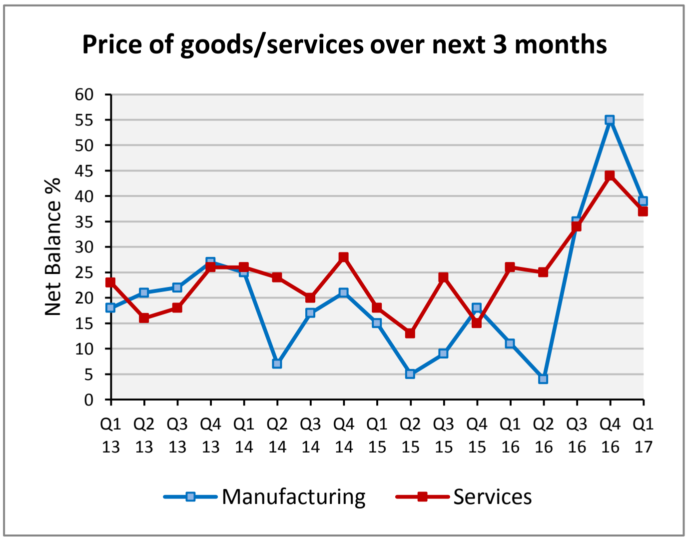


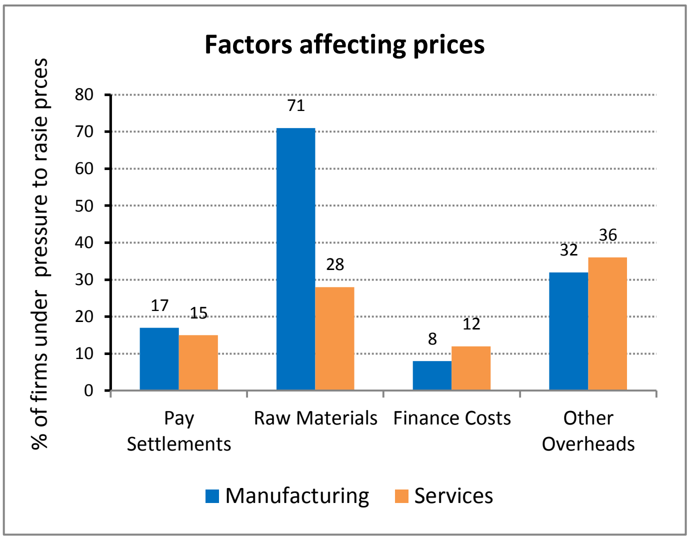


32% of firms in both sectors reported they were operating at full capacity (manufacturing up 2%; services down 6%)

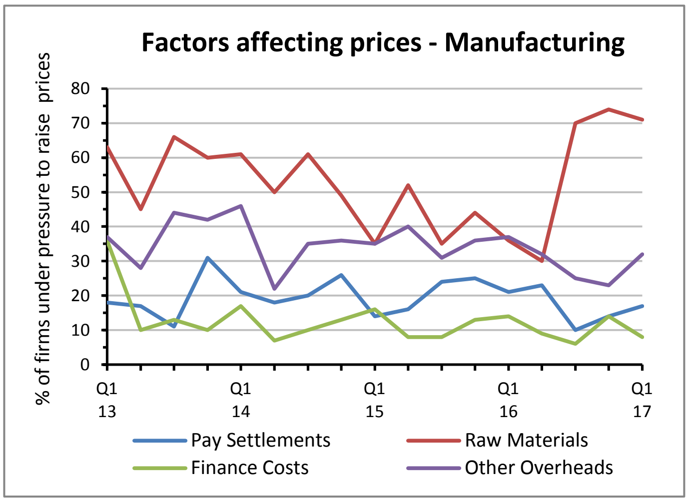
Over the past three months, the percentage balance of manufacturers reporting an improvement in their cashflow remained static at +10; whilst the services cashflow balance was down five points (+5, down from +10).

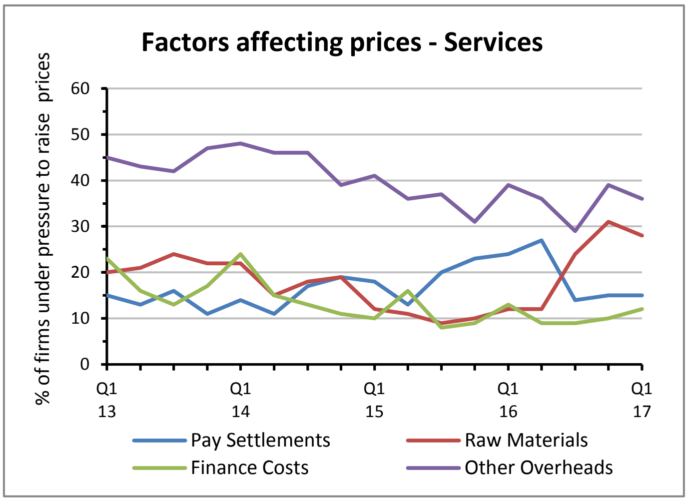
Prices





Ever since the UK voted to leave the European Union there has been significant pressure on firms to increase prices, mainly as a result of a weaker pound and increased costs of production. Q1 2017 has seen a slight weakening in the number of firms expecting to increase prices but the prices balance in both sectors remains well above the historical average. The net balance of manufacturing firms intending to increase prices fell 16 points (+39, down from +55); whilst in the service sector, the net balance of firms expecting to increase prices was down seven points (+37, down from +44).

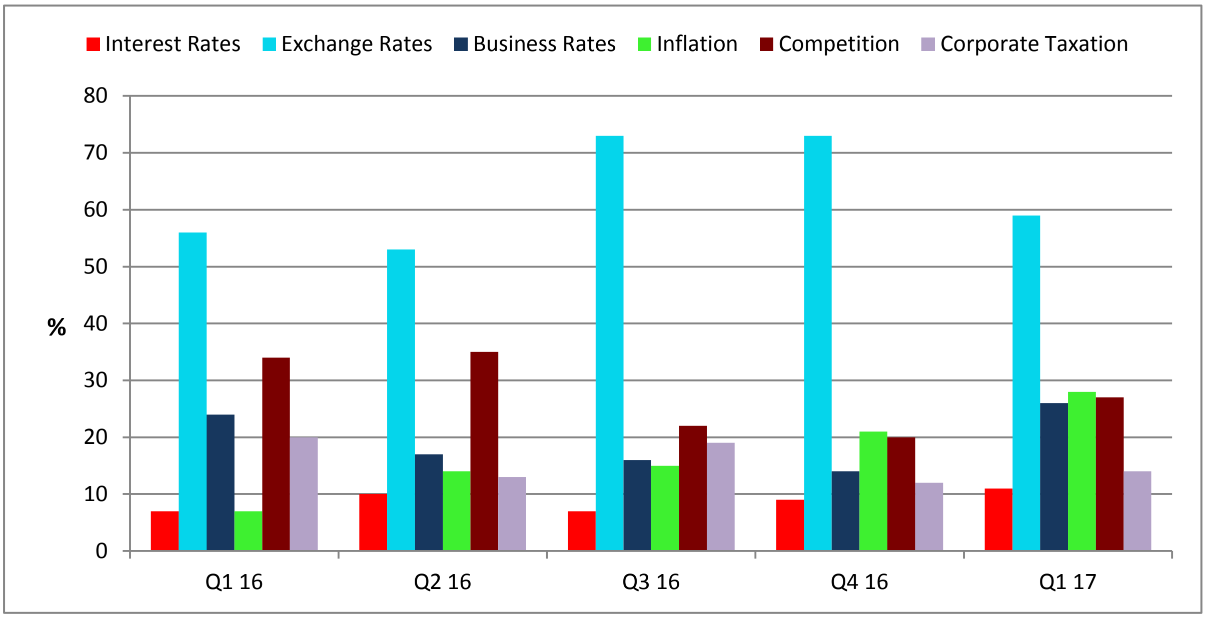




In terms of factors affecting the price of goods and services, almost three quarters of manufacturing firms (71%, down from 74%) said they were still under pressure to raise prices because of raw material costs. 32% of manufacturers said that they were under more pressure to increase prices as a result of other overhead costs (up 9%).

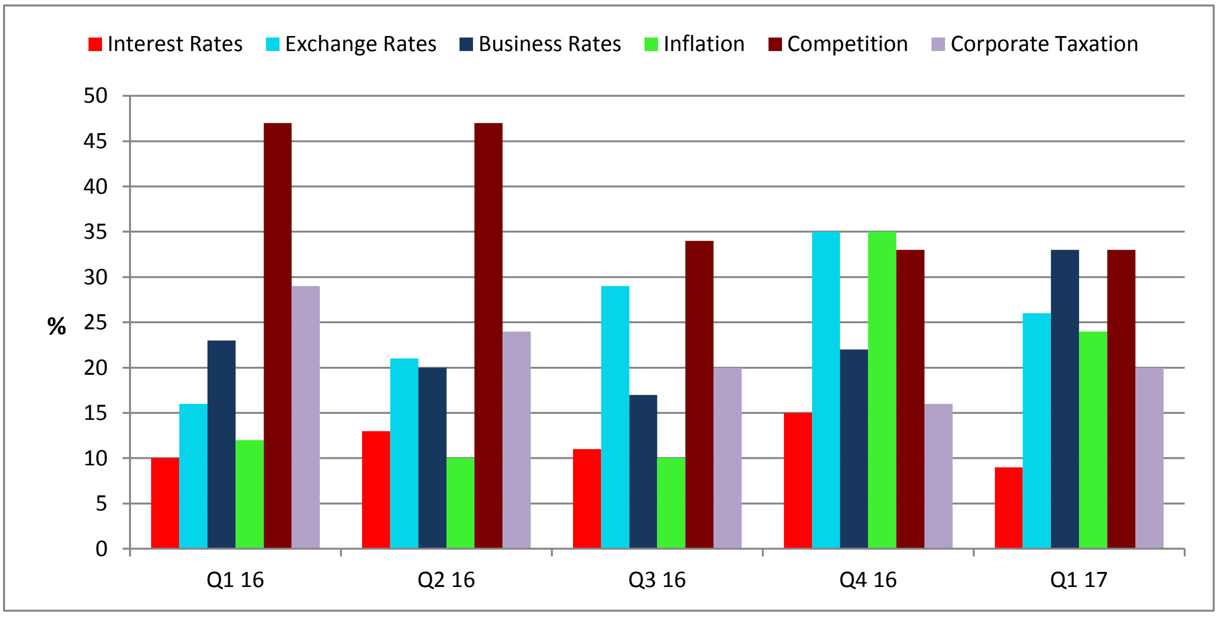
Prices in the service sector continue to be under greatest pressure from other overheads (36%, down from 39%), whilst pressure from the cost of raw materials also remains high compared with historical data (28%, down from 31%). Pressure from finance costs and pay settlements was relatively unchanged and remains weak.

Business Concerns (external factors) - Manufacturing



Exchange rates continue to be the biggest concern for manufacturing firms in the survey, although these concerns have weakened in Q1 2017 (59%, down from 73%). All other business concern measures have increased in Q1, with business rates (up 12%), competition and inflation (both up 7%) being the biggest concerns after exchange rates. Indeed, the percentage of manufacturing firms more concerned about inflation has risen 21% since the same period a year ago (28%, up from 7%).

Business Concerns (external factors) – Services



The recent revaluation of business rates has undoubtedly given many service sector firms cause for concern, with the Q1 survey showing that a third of all service businesses are more worried about business rates than three months ago (33%, up from 22%). 33% of businesses are also more concerned about competition (no change on Q4), whilst concerns about exchange rates (26%, down from 35%), inflation (24%, down from 35%)

BALANCE CHANGES

	Manufacturing		Services		Quarterly Change Manufacturing	Quarterly Change Services
	Q4 2016	Q1 2017	Q4 2016	Q1 2017	Q1 2017	Q1 2017
Domestic Sales	14	**19**	27	**25**	5	-2
Domestic Orders	2	**13**	23	**21**	11	-2
Export Sales	15	**25**	4	**6**	10	2
Export Orders	12	**21**	4	**0**	9	-4
Employment last 3 months	14	**14**	10	**10**	0	0
Employment next 3 months	22	**27**	23	**29**	5	6
% Tried to recruit	58	**58**	45	**44**	0	-1
% Part-time	10	**13**	28	**36**	3	8
% Full-time	69	**81**	73	**75**	12	2
% Temporary	31	**27**	16	**15**	-4	-1
% Permanent	50	**52**	45	**43**	2	-2
% Recruitment difficulties	46	**56**	59	**63**	10	4
% Skilled manual	56	**65**	36	**39**	9	3
% Professional/Managerial	36	**40**	56	**51**	4	-5
% Clerical	20	**20**	22	**41**	0	19
% Semi and unskilled	52	**38**	24	**18**	-14	-6
Cashflow	9	**4**	10	**10**	-5	0
Investment - plant/machinery	19	**27**	9	**6**	8	-3
Investment - training	7	**19**	25	**22**	12	-3
Confidence - turnover	41	**61**	54	**51**	20	-3
Confidence - profitability	23	**29**	36	**38**	6	2
% Full capacity	30	**32**	38	**32**	2	-6
Prices	55	**39**	44	**37**	-16	-7
% Pay Settlements	14	**17**	15	**15**	3	0
% Raw materials	74	**71**	31	**28**	-3	-3
% Financial costs	14	**8**	10	**12**	-6	2
% Other overheads	23	**32**	39	**36**	9	-3
External Factors of more concern than 3 months ago						
% Interest rates	9	**11**	15	**9**	2	-6
% Exchange rates	73	**59**	35	**26**	-14	-9
% Business rates	14	**26**	22	**33**	12	11
% Inflation	21	**28**	35	**24**	7	-11
% Competition	20	**27**	33	**33**	7	0
% Tax	12	**14**	16	**20**	2	4

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