

NatWest North East PMI®

North East achieves fastest output growth since January, but cost pressures intensify

Key Findings

Moderate rise in private sector business activity

New orders fall, but growth continues in manufacturing

Cost inflation picks up amid higher fuel and wage bills

North East Business Activity Index



Last six months NE v UK



May data from the NatWest North East PMI revealed a modest upturn in business activity across the private sector economy, suggesting a sustained recovery from the weather-related disruptions seen earlier in 2018. However, the latest survey indicated a setback for new order intakes, linked to subdued consumer spending. Employment numbers remained broadly unchanged, with rising input costs and a lack of pressure on operating capacity the main factors holding back staff hiring.

The headline North East Business Activity Index – a seasonally adjusted index that measures changes in the combined output of the region’s manufacturing and service sectors – registered 51.8 in May, up from 50.4 in April and the highest reading for four months. Sector data suggested that rising manufacturing production in the North East helped to offset subdued service sector business activity. That said, the overall rate of private sector growth in the North East continued to lag behind the UK as a whole (equivalent index at 54.5 in May).

Demand

In contrast to the stronger trend recorded for business activity, latest data highlighted a renewed fall in new work received by companies based in the North East. A number of businesses in the region cited stretched household finances and a corresponding moderation in consumer spending in May.

Manufacturing remained a bright spot for the North East, according to the latest survey data.

The upturn in order books at manufacturing firms was driven by improving business conditions in key export markets and rising global demand for capital goods.

Capacity

North East firms reported another sharp reduction in work-in-hand (but not yet completed) during May, which suggested a lack of pressure on existing business capacity. At the same time, staffing levels were virtually stagnant during the latest survey period, which echoed the subdued employment trends recorded across the UK as a whole.

Prices

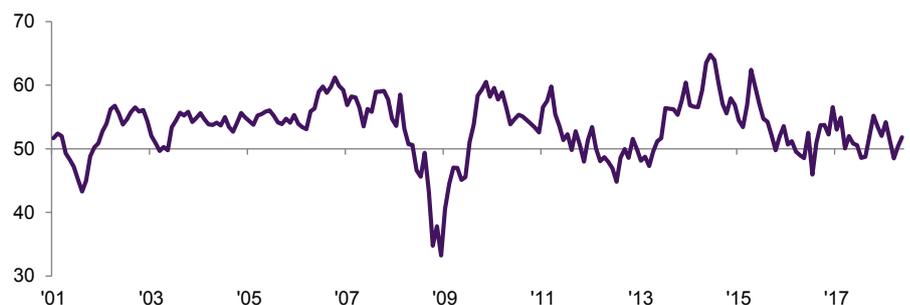
Average cost burdens increased at a sharp and accelerated pace in May. Moreover, the rate of input price inflation was stronger than the UK-wide trend. Survey respondents widely commented on rising fuel bills and greater staff wages, especially for employees close to the National Living Wage threshold. Despite higher costs, prices charged by North East firms increased at the slowest rate for seven months.

Outlook

The main positive finding from the latest survey was a rebound in North East business expectations to the highest since March 2016. Manufacturers cited new product launches and plans to boost export sales, while service providers noted hopes of improved operating efficiency and a rebound in consumer demand.

North East Business Activity Index

sa, >50 = growth since previous month



New Business Index



Total new work falls in May, but manufacturing remains a bright spot in the North East

North East private sector firms experienced a slight reduction in new business volumes during May, which represented the second fall in the past three months. The region has seen a soft patch for new work since early-2018, reflecting weaker sales across the service economy. Survey respondents cited subdued consumer spending and stretched household finances.

Meanwhile, manufacturers based in the North East achieved another robust upturn in new orders, underpinned by improving global economic conditions and greater demand for investment goods.

New Business Index

sa, >50 = growth since previous month



Outstanding Business Index



Sharp drop in unfinished work suggests lack of pressure on operating capacity

The seasonally adjusted Outstanding Business Index remained below the 50.0 no-change threshold in May, to signal a sustained decline in incomplete work at private sector companies. Another sharp drop in backlogs of work was linked to subdued sales volumes and suggested a general lack of pressure to boost operating capacity.

The latest depletion of work-in-hand (but not yet completed) was much faster than that seen across the UK as a whole.

Outstanding Business Index

sa, >50 = growth since previous month



Employment Index



Staffing levels stagnate across the North East private sector

May data revealed that private sector employment across the region was virtually unchanged over the month, which continued the largely stagnant trend seen on average in 2018 so far. Survey respondents generally noted that current payrolls numbers were sufficient to meet existing workloads.

Relatively subdued employment trends in the North East broadly mirrored the modest trend seen for job creation across the wider UK private sector in May.

Employment Index

sa, >50 = growth since previous month



Input Prices Index



Higher fuel costs contribute to stronger input price inflation in May

Input cost inflation accelerated sharply from the six-month low recorded in April. Moreover, the seasonally adjusted Input Prices Index signalled that average cost burdens at North East businesses continued to rise at a faster pace than across the UK as a whole.

Anecdotal evidence suggested that rising fuel bills were a key factor behind the steep increase in average cost burdens in May. A number of firms also cited higher salary payments.

Input Prices Index

sa, >50 = inflation since previous month



Prices Charged Index



Slowest increase in prices charged for goods and services since October 2017

May data pointed to greater pressure on operating margins at private sector companies. Despite facing stronger input cost inflation, the latest survey signalled that prices charged by North East businesses increased at the slowest pace for seven months.

There were widespread reports that strong competition for new work and subdued domestic demand had restricted firms' scope to pass on higher operating expenses to customers.

Prices Charged Index

sa, >50 = inflation since previous month



Future Business Activity Index



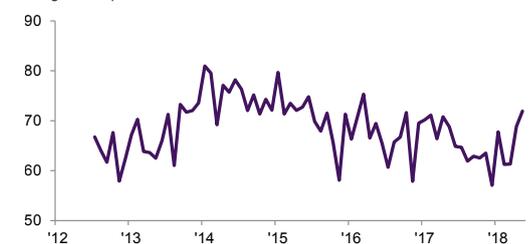
Business optimism rebounds to its strongest since March 2016

Despite a difficult month in terms of sales volumes and cost pressures, North East companies signalled a strong degree of optimism regarding the business outlook. Moreover, the Future Business Activity Index rose to its highest since March 2016 and pointed to a stronger level of confidence than the UK as a whole.

Manufacturers were particularly upbeat in May, reflecting forthcoming new product launches and planned extensions to plant capacity. Service providers cited efforts to improve efficiency, alongside hopes of a turnaround in consumer demand.

Future Business Activity Index

>50 = growth expected over next 12 months



North East Export Climate Index

Note: Export markets are defined as non-UK.



Last six months



Resilient demand conditions recorded in key North East export destinations

The North East Export Climate Index is calculated by weighting together national PMI output data according to their importance to the manufacturing exports of the North East. This produces an indicator for the economic health of the region's export markets.

At 54.7 in May, the North East Export Climate Index remained comfortably above the neutral 50.0 mark, thereby signalling a sustained and solid upturn in economic conditions across the region's export markets. That said, the rate of expansion slipped to a 16-month low, largely reflecting a loss of momentum in Europe.

The main positive developments were in North America, where business conditions improved at the fastest pace for just over three years in May (on a trade-weighted basis). There were also signs of a growth rebound in the Middle East, following the soft patch earlier in 2018.

Export Climate Index

sa, >50 = improving export climate since previous month



Top export markets, North East

Rank	Market	Weight	Output Index, May-18
1	Netherlands	11.2%	59.4
2	Germany	9.0%	53.4
3	USA	8.2%	56.6
4	Spain	6.9%	55.9
5	Italy	5.1%	52.8

North East Industry Specialisation

Location quotients (LQs) are useful measures of regional economic specialisation and offer a means to identify industry clusters at a local level. They are ratios derived by comparing the share of sector output (or gross value added) in regions with the national share of output in the same sector.

Focusing on the manufacturing and service sectors in isolation, a location quotient is calculated by taking a sector's proportion of regional output and comparing it with the UK-wide share of output in the sector. An LQ of 1.0 in a sector means that the region and the UK as a whole are equally specialised in that

sector. An LQ greater than 1.0 indicates that the sector has a greater economic footprint in the region than it does for the UK as a whole.

The tables below rank the location quotients for the North East, broken down by manufacturing and services sub-sectors. The UK Output Index for each sub-sector is also displayed.

Manufacturing specialisation: North East

Rank	Sector	LQ	UK Output Index, May-18 (3mma)
1	Machinery & Equipment	1.57	65.0
2	Chemicals, Rubber & Plastics	1.35	62.0
3	Metals & Metal Products	1.14	58.0
4	Wood & Paper	1.06	56.0
5	Transport Equipment	0.87	52.0
6	Electrical & Electronic	0.72	48.0
7	Other Manufacturing	0.71	47.0
8	Textiles & Clothing	0.69	46.0
9	Food & Drink	0.52	42.0

40 45 50 55 60 65 70

Services specialisation: North East

Rank	Sector	LQ	UK Business Activity Index, May-18 (3mma)
1	Transport & Communication Services	1.44	58.0
2	Hotels, Restaurants & Catering	1.21	54.0
3	Other Personal / Consumer Services	1.14	52.0
4	Business-to-Business Services	0.90	48.0
5	Financial Intermediation	0.70	45.0
6	Computing & IT Services	0.64	44.0

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UK Sector Focus: Hotels, Restaurants & Catering

Output Index



Last six months*



*3mma

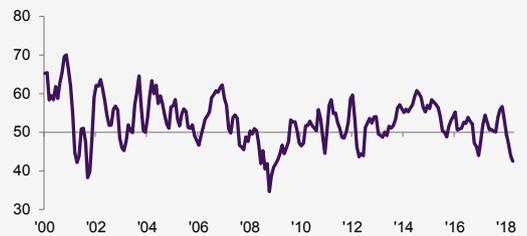
Subdued consumer demand continues to weigh on hotels, restaurants & catering sector

The consumer-focussed hotels, restaurants & catering sector was the UK economy's weakest-performing industry in the three months to May, having seen a further sharp decline in business activity. Furthermore, the rate at which activity fell continued to gather pace, reaching the quickest in nine years amid a decline in inflows of new work.

Latest data meanwhile showed sustained pressure on gross margins in the sector. The rate of input cost inflation was faster than anywhere else in the services economy in the three months to May, but a lack of pricing power meant that output charges rose far less by comparison. With higher costs often a reflection of wage pressures, firms in the sector continued to pare back staffing numbers, in line with the trend observed throughout the year-to-date.

Output Index

sa, >50 = growth since previous month (3mma)



Input Prices Index

sa, >50 = growth since previous month (3mma)



UK Regional Rankings

Business Activity

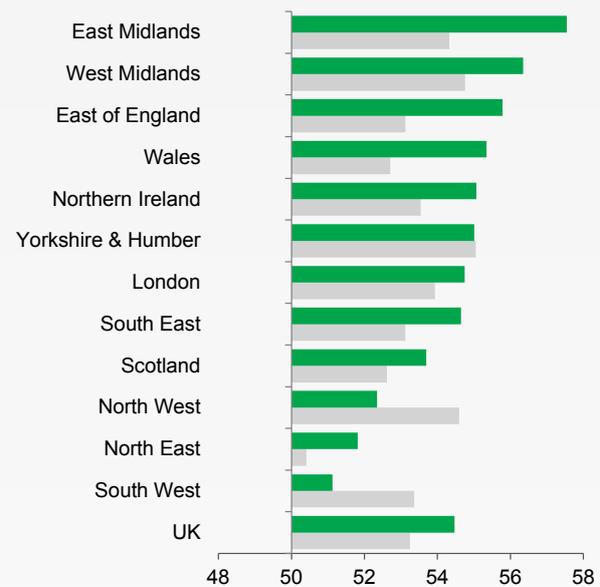
May saw business activity increase across all UK regions, led by strong and accelerated growth in the East and West Midlands. The former was the best-performing region for the fourth time in the past five months, re-taking the top position from Yorkshire & Humber. East of England and Wales also climbed the rankings in May having seen rates of expansion accelerate sharply from the previous month. At the other end of the table were the South West and North East, which both saw only modest increases in business activity.

Employment

Employment rose in 11 out of the 12 areas of the UK monitored by the survey in May, the only exception being the South West where staffing numbers fell for the first time in almost two years. The steepest rises in workforce numbers were recorded in Northern Ireland and Scotland respectively, with the latter recording the strongest rate of job creation for almost three-and-a-half years.

Output Index by region

sa, >50 = growth since previous month, May-18 (Apr-18)



Contact

NatWest

Jonathan Rennie
Regional PR Manager
07769 932 102
jonathan.rennie@rbs.co.uk

IHS Markit

Tim Moore
Associate Director
+44 1491 461 067
tim.moore@ihsmarkit.com

Joanna Vickers
Corporate Communications
+44 207 260 2234
joanna.vickers@ihsmarkit.com

Methodology

The NatWest North East PMI® is compiled by IHS Markit from responses to questionnaires sent to North East companies that participate in IHS Markit's UK manufacturing and services PMI surveys.

Survey responses are collected in the second half of each month and indicate the direction of change compared to the previous month. A diffusion index is calculated for each survey variable. The index is the sum of the percentage of 'higher' responses and half the percentage of 'unchanged' responses. The indices vary between 0 and 100, with a reading above 50 indicating an overall increase compared to the previous month, and below 50 an overall decrease. The indices are then seasonally adjusted.

The headline figure is the Business Activity Index. This is a diffusion index calculated from a single question that asks for changes in the volume of business activity (at service providers) or output (at manufacturers) compared with one month previously. The North East Business Activity Index is comparable to the UK Composite Output Index. It is sometimes referred to as the 'North East PMI', but is not comparable with the headline UK Manufacturing PMI figure.

Underlying survey data are not revised after publication, but seasonal adjustment factors may be revised from time to time as appropriate which will affect the seasonally adjusted data series.

For further information on the PMI survey methodology, please contact economics@ihsmarkit.com.

About PMI

Purchasing Managers' Index® (PMI®) surveys are now available for over 40 countries and also for key regions including the eurozone. They are the most closely watched business surveys in the world, favoured by central banks, financial markets and business decision makers for their ability to provide up-to-date, accurate and often unique monthly indicators of economic trends. To learn more go to ihsmarkit.com/products/pmi.html.

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Alongside a wide range of banking services, NatWest offers businesses specialist sector knowledge in areas such as manufacturing and technology, as well as access to specialist entrepreneurial support.

NatWest has been running MoneySense, an impartial financial education programme for 5–18 year-olds, for more than 21 years. By the end of 2018, NatWest will help another 1 million young people to understand and take control of their finances.

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