January 2009

Summary of economic conditions

- The latest evidence from businesses and business representative organizations points to **lower volumes of output and new orders** (in particular domestic orders) in the South East. According to the latest FSB Snap Poll Survey some 53% of small businesses in the region have seen a decrease in trade over the past two months.
- Largely anecdotal evidence shows that the **weak pound is contributing towards marginally higher volume of export orders** and higher volume of inward investment enquiries in some areas such as Milton Keynes.
- **Numbers employed are mostly lower** than last month. The latest ONS data points to a sharp fall in female employment in the region in the three months to November.
- Although the **volume of notified redundancies in the region increased by almost 60%** when compared to January last year, businesses in some sectors are still **trying to retain skilled employees** by seeking to reduce working hours rather than make redundancies.
- **Input costs remain high**, especially amongst businesses relying on imported raw material or equipment.
- With lower prices charged to customers and lower volume of trade, **profit margins and cashflow are lower** than last month.
- **Investment volumes** (including R&D investment) **are mostly lower** than the previous month.

Key challenges and hotspots

- The **cost of existing finance** has remained broadly flat for the majority of small businesses in the region with **higher cost of credit insurance and higher cost of new credit** being amongst the most significant challenges facing businesses. According to the latest FSB Survey over two thirds of small businesses in the region have seen an increase in the overall cost of new credit.
- **Investments in office space are put on hold** and there is evidence of buildings being demolished because of property tax on empty buildings.
- **Falling demand and a danger of financial markets deleveraging** too quickly which could reinforce the downturn.
- **Some instances of market power** being used, such as a large UK food processor imposing 90-day payment terms on equipment suppliers.
- There is a **perception that the banks are being slow in implementing the Enterprise Finance Guarantee**. Lenders at local level seem to be unaware of it and have received little instructions from their head offices.

Business specific intelligence / information on key questions

- The **overall picture has deteriorated across a broad range of sectors** with telecommunications, manufacturing, finance, construction and retail sectors facing the toughest trading conditions last month.
- See Annex for details.

Sectoral Overview

The overall picture has deteriorated across a broad range of sectors in the South East.

Manufacturing: in the first month of this year the outlook for manufacturing has taken a significant turn for the worse and trading conditions in 2009 are set to be some of the toughest for two decades. The Engineering Employer Federation (EEF)'s business survey shows that the picture has changed significantly since last summer because of the turmoil in the financial markets and the downturn is now widespread across most sectors and regions. However, some EEF members point out that weaker sterling has benefited exports across different sectors. At the same time, many manufacturing firms which are highly dependent on imports of raw materials, plant and machinery from abroad are suffering because of the strength of the Euro. Some manufacturers are considering redundancies alongside short-time working and possible pay cuts, in order to remain sustainable.

Business specific intelligence shows that **Eaton Aerospace** is to shed up to 100 of the 800 jobs at its fuel pumps and valves factory in Titchfield, Hampshire. **Edwards** is to shed 176 jobs at its vacuum equipment factory in West Sussex, and a further 1,000 will move to a four-day week.

Focusing on the automotive sector, world vehicle markets are sharply down in the wake of the turmoil on financial markets. Virtually all UK vehicle makers are cutting back, temporary contracts are not being renewed, and vehicle makers are starting to cut back on permanent employees. Suppliers are cutting back, and several long established companies are now in administration. Small companies in the South East supplying the automotive industry have been affected significantly by the current recession. Business specific intelligence shows that **UYS** is to shed a further 50 of the 180 jobs at its automotive exhaust systems factory in Oxford; **Gurneys**, the Oxfordshire-based Vauxhall car dealership with 38 staff, has gone into administration.

Retail: There is anecdotal evidence of strong Christmas trading, with footfall in January generally on a par with or higher than the previous year. However, of most concern in the short term is dwindling cash flow. Profit margins have been squeezed due to deep discounting over the Christmas period. Retailers of high-end or discretionary goods are suffering most. Lower employment levels are predicted for the first quarter of 2009. Major developments are on hold, including Westfield's Friary development in Guildford, which has been postponed for at least 5 years.

Business specific intelligence shows that **Marks & Spencer** is to close two high-street stores in Croydon and Woking and 25 smaller Simply Food stores, with the loss of 780 jobs and **Tesco** is to shed 50 of the 550 jobs at its distribution centre in Didcot, Oxfordshire. However, the business specific intelligence received also reports some positive news. For example, **Runnymede Council** is to consider plans from Albemarle Egham to invest GBP 35m in the development of a 20,000 sq ft Waitrose supermarket and 80-bedroom Travelodge hotel in Egham. Also, **Game** is planning to relocate the headquarters of its Gamestation software retailing business and up to 80 jobs from York to Hampshire.

Construction: mood in the sector remains downbeat as activity, particularly in the housing and commercial segments continues to slide. Government plans to bring forward spending have been largely welcomed by the industry. The sector is increasingly reliant on public spending which is crucial to the immediate outlook for the industry. Continued lack of credit and lack of confidence in the commercial property sector is leading to reduced activity. The commercial property sector is adopting a more flexible approach to renting/leasing arrangements in order to encourage retention and inward investment.

However, the business specific intelligence received also reports positive information. For example, **Highcross** has submitted plans for a 1m sq ft development at the Lakeside North

Harbour site in Portsmouth, including offices, a hotel, car dealership and conference centre. **The Foreign & Commonwealth Office** is planning to set up a 35,000 sq ft office at the Cornerstone building in Milton Keynes, with the relocation of staff from London and an existing office nearby.

Business services: anecdotal evidence shows that accountants, who were still doing quite well in December, have been affected by the current climate. Firms previously hoping to avoid redundancy are now either considering or implementing redundancies, many at the top end. Several senior partners in accountancy firms have already been made redundant. In particular, accountancy firms are experiencing a reduction in Corporate Finance work and some accountancy firms are reporting that their clients are having difficulty paying fees and are considering offering clients Feeplan options. In general, depending on their client base, other business services firms are struggling. Any company dealing with clients in estate agency, advertising, or retail of non-essential goods is more likely to be facing difficulties.

Financial services: Significant redundancies have taken place already, and more are expected in the New Year. Business specific intelligence reports that **Bank of Ireland** is to close its mortgage offices in Reading with the loss of 270, in order to transfer the work to its Bristol office.

Tourism / leisure: Higher end tourist businesses reported a significant drop in bookings, but expect higher demand in the summer as the weaker pound attracts more overseas visitors. Budget tourism businesses are still doing relatively well and are optimistic about the summer season. A number of hotels have already made redundancies and more are planned. The corporate and meetings business is particularly difficult at the moment with businesses down-scaling their requirements. However, the hotel industry is relatively confident that the weakness of the pound against the euro is bringing in more European customers, especially from the key markets of Germany, France and Italy. **Milton Keynes Leisure Complex** (Xscape) reported footfall down in December but up in the first week of January, with interest shown in three currently empty units within the complex.

Transport: The Dover Harbour Board reports that cross-channel freight and tourist trade is down by around 14% and shipping operators' forecasts for trade in 2009 range from 15%-25% down. All are reducing capital expenditure and taking ships 'off line'. Dover Harbour Board is shedding 3% of its staff in the next 3 months and outsourcing a further 190. However, there is some evidence that we are already seeing an increase in European visitors. For example, **LD lines** (ferry operator) reports that they noticed a recent surge in last-minute crossings being booked by French travellers, wanting to take advantage of the English sales at the end of 2008 and at the beginning of 2009. In fact, **LD Lines** has confirmed that it will start operating new ferry services from Dover to Boulogne and Dieppe next month, creating at least 20 jobs at the port. It is expected that at least another 40 jobs will be created with the addition of a second ship to the route from July 1st.

Flybe, Europe's largest regional airline and largest scheduled airline at Southampton, has reinforced the German market reports that this market remains robust. The strength of the Euro against the pound is creating better value for money.

Agriculture/Rural Businesses: Rural businesses are generally struggling to maintain sales volumes and margins while reducing costs. However, a survey of 100 rural businesses by the Country Land and Business Association revealed generally greater confidence in the rural economy than in the wider economy: 18% of rural businesses are quietly confident in the rural economy over the next few months, 61% are very confident, and only 5% are not confident at all. Farmers seem to be less affected by the problems of accessing credit than other sectors of the economy: less than 40% of NFU members surveyed in January had seen an increase in overdraft rates, and most of these increases had been modest. However, farmers will need significant increases in working capital this year to help them deal with higher input costs and infrastructure investments. Land based businesses in general are seen as being in need of gap finance, as they are often asset rich but cash poor.

Voluntary sector: a survey of 83 RAISE members in January showed that more than half of respondents had seen increased demand for their services – mostly a 6-10% increase – in the past 3 months. Nearly ¾ of respondents expect public funding of the sector to be reduced in the next 6 months, while less than 10% think it will increase. In the past 6 months, 42% of respondents have seen a drop in income (some by as much as half), 38% have experienced no change and 20% seen an increase in income. 13% of respondents have had to make staff redundant due to the financial crisis, although there has been limited impact on staff working hours. 42% of respondents have seen no change in the number of volunteers over the past 3 months, only 9% have seen numbers fall, while 39% have seen an increase – by up to 10% in some cases. Key challenges in the next few months include managing a similar or increased demand for services, ensuring stability and improving service quality in the face of uncertain or reduced funding levels.

Creative and media: In the creative and media sectors companies have reported lower volume of domestic orders, lower numbers employed, lower profit margins and lower cash flow. The volume of output, cost of production, prices charged to customers and staff costs have remained stable. Export orders and Research and Development have been higher this month compared to December 2008. Overall South East Media sees buyers/investors slowing down their decision making time. Smaller web and online companies are very busy but doing more for the same income. Enquiries for film production are still high probably due to exchange rate benefits. Orders for computer games developers are down by up to 10% and some redundancies (of the same order – up to 10%) are taking place or are being prepared for. However, the gaming sector in Brighton is reported to be faring well. Digital marketing is very active. Unfortunately a few companies are being affected by their parent companies and large clients such as Zavvi.

Redundancies: According to HR1 data[1], more than 6,100 redundancies were announced in the South East in January 2009, which is almost 60% greater than in the same period in 2008. Relative to their share of regional employment, the telecommunications, manufacturing, finance and construction sectors have seen the greatest increase in redundancies over the past month. These four sectors accounted for almost half of all notified redundancies in the South East over the past month. Retail and public sectors have also recorded an increase in redundancies in January 2009 (a fifth of all notified redundancies in January in the South East were in retail/public sector).

With one in ten notified redundancies in Milton Keynes, relative to its share of regional employment, Milton Keynes was affected by redundancies disproportionately more than other sub-regions. Berkshire and Oxfordshire also recorded disproportionately more redundancies than other sub-regions. For example, a fifth of all redundancies notified via HR1s in the past month were recorded in Berkshire, yet Berkshire accounts for less than 13% of employment within the South East.

Over the past month there was an increase in the proportion of redundancies in the South East due to lower demand. In January 2009 more than half of all redundancies in the South East were caused by lower demand against less than half in December 2008. In seven out of ten NUTS3 sub-regions in the South East lower demand accounted for at least half of all redundancies. In Berkshire, Buckinghamshire, Oxfordshire and Surrey lower demand accounted for between 60% and 70% of all redundancies.

[1] Note that this data only captures redundancies of more than 20 employees; some of the job losses are not scheduled to take place until later in 2009; and in some cases the redundancies are happening in another region but are registered in the South East because it is home to the company's headquarters.

Redundancy notifications by sub-region, volume and reason over the period 1 January – 31 January 2009 (Source: HR1 data via BERR / Job Centre Plus)