Regional Intelligence Snapshot for the South East

April 2010

Summary of economic conditions

- According to the latest South East Purchasing Managers Index (PMI), private sector **employment increased for the first time in twenty-one months** in April. The recruitment of new staff was generally linked to rising workloads, and centred on the manufacturing sector.
- **Business activity in the South East recorded another sharp rise in April**, albeit the weakest since February, according to the latest PMI. The rate of **growth of incoming new business remained substantial**, despite easing since March, and was well above the UK trend. New business rose at a sharper rate in manufacturing than in the service sector.
- **Labour market performance was broadly positive** in the South East: Claimant count unemployment in March 2010 was 156,000, 5,144 lower than in the previous month. The number of people in **employment in February increased by 6,000** on the previous three months.
- **More companies expect to take on new staff**: the net balance of small businesses in the South East expecting to increase employment in the next three months turned positive (+5%), according to the latest FSB-ICM 'Voice of Small Business' Panel (conducted end of March).
- The latest RICS Housing Market Survey (March) shows a positive net balance of surveyors reporting **rising house prices in the South East for the ninth consecutive month**, well ahead of any other UK region (apart from London). However, the net balance has been declining since its peak in November 2009.

Key challenges and hotspots

- **Cash flow and access to finance issues continue for some companies**, with 36% of businesses reporting that their application for new credit had been unsuccessful, according to the latest FSB-ICM survey.
- 'Late payers' are increasingly making cash flow difficult, according to Kent Economic Board. Analysis from Portsmouth & SE Hampshire Chambers' Quarterly Economic Survey also shows that cash flow has turned negative again in the first quarter of 2010. Manufacturers expect levels of **cash flow to fall back into negative territory** (balance of -8%), after positive levels in the last three months (balance of 3%), according to the EEF.
- The **gap between input and output prices appears to be widening**: average **input prices in April rose at the fastest rate since September 2008**, with manufacturing being particularly hit by higher raw material costs. However, the ability to pass on higher costs to customers remained limited in April, as a result of **strong competitive pressures**. According to Kent Economic Board, most manufacturers judge that their markets are not yet strong enough to pass on increased input costs.
- **Two thirds of small companies in the South East report operation below capacity**, and just over half expect activity to stay below capacity in the next three months, according to the latest FSB-ICM survey.

Business specific intelligence / information on key questions

- **Manufacturing continued to rebound in the first quarter of 2010**. Manufacturers across the South East and London were the **most upbeat of any English region**, according to the March 2010 EEF Manufacturing Outlook. The balance for output and orders in the past three months was positive for the second quarter in a row, and the strongest since early 2007.
- The number of **new business starts in the South East in the first quarter of this year increased** by 15% (compared to same quarter in 2009), according to BankSearch. Surrey Economic Partnership reports that **more enquiries are being received from individuals wishing to start their own businesses**. Numbers of individuals seeking to attend Business Link start up workshops are still increasing steadily.
- **Investment intentions remain the weak point, but there are some positive signs**. The latest EEF Manufacturing Outlook reports that nationally, the net balance of investment plans remains negative, but improved significantly during the last 18 months. According to Portsmouth & South East Hampshire Chamber of Commerce and Industry, investment in plant and machinery has recovered and is now marginally positive.

Sectoral Overview

Manufacturing

The latest figures from the Office for National Statistics (ONS) confirm that, at national level, manufacturing output continued to grow in the first quarter of 2010, in line with the UK GDP growth, although at a slightly slower rate. Manufacturing activity recorded a quarterly increase of 0.7%, compared with an increase of 0.8% in the previous quarter, and again made a positive contribution (0.1%) to GDP growth (0.2%).

The most recent South East Purchasing Managers Index (PMI) figures for April 2010 show that business activity eased further from February's twenty-nine month high, but remained above its long-run trend and the UK average. Sector data signalled that manufacturing output and workload continued to rise at a faster rate than service sector activity. This is corroborated by the latest EEF Manufacturing Outlook for the South East & London, which shows that the balance of responses on output (32%) and orders (35%) were again positive for the past 3 months and the strongest since early 2007. In line with other UK regions, more companies reported an expansion in export orders relative to domestic ones.

However, there are some concerns in the South East about the widening gap between input and output prices. According to the latest South East PMI, manufacturers recorded the fastest input price rise since September 2008, reflecting their greater exposure to rising prices for metals and chemicals (i.e. plastics and oil-related) as well as the weaker sterling exchange rate.

Looking ahead at sub-sectoral level, EEF expects the mechanical equipment industry to benefit from stronger export demand in Europe and Asia this year, with the help of a weaker pound. They project a growth of 0.4% this year, rising to 3.5% in 2011. Moreover, the pick-up in mechanical equipment activities should feed through to the metal products industry, leading to projected growth of 0.5% this year, rising to 3.8% in 2011. According to EEF, the electronics industry rebounded from recession in the middle of last year and should see strong quarter on quarter growth this year, expanding by 4.5% in 2011.

This is corroborated by business specific intelligence which shows that in the computer & electronics sub-sector **Motorola** has finalised plans to relocate its Swindon-based electronics factory and 500 staff to an 80,000 sq ft unit at Kembrey Park by late summer. Meanwhile, **Skye IT** is to create up to 20 jobs at a new headquarters for its technology business at West Malling in Kent.

A mixed picture is observed in the chemicals & pharmaceuticals sub-sector, where **Neolab** has secured £2m of venture capital from Maven Capital Partners to fund the expansion of its Hampshire-based pharmaceuticals licensing business. At the same time, it is reported that **Neuropharm**, the Leatherhead-based pharmaceutical research firm, is to go into voluntary liquidation.

The situation is quite different in the food & drink sub-sector where a leading firm is still facing cost-related difficulties. **Mars** has announced that it will be making further redundancies at its Slough factory and as a result 45 jobs could be lost from its 1,100 workforce. However, a spokesman stressed that the company remains committed to producing chocolate confectionery at its Slough factory. The company added that its recent plans to create a world class R&D facility is an example of the ongoing commitment to the Slough site.

Construction / property

The most recent official data from ONS shows that construction output in the UK fell by 0.7% in the first quarter of 2010, compared with a decrease of 0.9 % in the previous quarter. However, the sector recorded a slight increase of 0.2% in Q1 2010 when compared to the same period the previous year.

According to the latest Business Link Report for Surrey, the construction industry is reporting an increase in business, with a noticeable rise in new building projects throughout the south-west and east of the county. However, the property market is still struggling as a result of a shortage of stock.

These results are corroborated by anecdotal evidence from Kent Economic Board which suggests that civil engineering is currently faring better than residential development. Property developers point out that they are slightly less optimistic than a few months ago as lenders are now seeking a much higher level of security, which is effectively putting a brake on many projects in this sector. Additionally, they argue that future development in the rental sector in Kent is currently looking uncertain as there is doubt over the level of future funding available via the Homes and Communities Agency and Housing Associations.

Business specific intelligence from Kent also confirms the better performance of building over residential development projects. For instance, **Skanska** has been diversifying its portfolio over the past year, which now includes public sector projects such as the M25 and locally the A2 at Pepper Hill as well as the "building schools for the future" project. The firm is particularly interested in making linkages with micro businesses that could supply materials, technologies or services. Suppliers for the civil building sub-sector are, in turn, expanding their capacity as a result of higher demand. For example, **Pasquill** is to open four new timber processing branches in Abingdon (Oxfordshire), Bury St Edmunds, Leeds and North Wales this year, with the creation of up to 50 jobs.

Retail & wholesale

The latest figures from the ONS indicate that output in the distribution, hotels and restaurants sector at UK level fell by 0.7% in Q1 2010, compared with an increase of 1.9% in the previous quarter. The motor trade, retail and wholesale made the largest contribution to the decrease in Q1 2010, after having made the largest contribution to the UK GDP recovery in the previous quarter.

The picture in the retail sector is mixed across the South East. On the one hand, anecdotal evidence from Berkshire Economic Strategy Board indicates that Bracknell Forest still had, on average, a vacancy rate of retail units of 9.5% in March 2010. Car park figures for the same local authority were, on average, 0.3% lower than the same month in 2009. Newbury also saw car park figures falling by 10% in the first half of April, compared to the same period in 2009. However, their footfall figures were 10% higher for the same period of time. Business specific intelligence indicates that **Thorntons Chocolatiers** announced that it is due to close its store in the Nicholsons Centre, Maidenhead, during April.

On the other hand, anecdotal evidence from Guildford Borough Council shows signs of a pick-up in the retail sector locally, as **TKMaxx** opened a shop in the old Woolworths building on 24th April and **Primark** is moving into the old BHS store in the Friary Centre. The Council has invested heavily in the new entertainment venue, formally known as the 'Civic' and this is accompanied by investment from **Raddison Hotels** in a new four star hotel on the adjacent site which will open in 2011.

Transport & communications

Output in the transport, storage and communication sector nationally increased by 0.6% in Q1 2010 according to the ONS - unchanged from the previous quarter. The most significant positive contribution was from post and telecommunications. However, this was partially offset by a large drop in output in the land transport sub-sector.

South East business specific intelligence indicates that **CEVA Logistics**, the land transport company based in Kent, is to close its distribution depot in Mitcheldean in July, with the loss of up to 80 jobs, in order to transfer its Xerox equipment business to Daventry. However, other means of transport in the region have been performing better. **Patriot Aerospace**, the Redhill-based air transport company, has reached agreement to acquire Coventry Airport, and plans to restart commercial flights and secure up to 400 jobs. Similarly, **P&O Ferries** in Kent has announced it is to restart operations between the Port of Dover and the Belgian Port of Zeebrugge. The firm last operated between the ports in 2002 and from April 7th 2010 the company began running its dedicated freighter European Endeavour on the route.

Energy & Utilities

The latest UK GDP figures from the Office for National Statistics show that electricity, gas and water supply output increased by 2.5% in Q1 2010, following a sharp fall by -2.7% in the previous quarter, which is in line with seasonal variations. However, output in this sector is still -2.8% below the level reached for the same period the previous year.

Some encouraging signs of recovery in the industry are provided by business specific intelligence which indicates that, for instance, **Scottish and Southern Energy (SSE)** in Southampton is taking over a £225m contract to manage 250,000 street lights on the South Coast, creating 50 new jobs in Hampshire. To support the new contract, SSE has signed a 25-year lease on a new 60,000 sq ft regional depot in Hedge End. Around 150 staff will be based there, including existing street lighting and administration staff from SSE and the councils, as well as 50 new roles. Thirty-five of these are currently being recruited and the company expects to take on a further 15 before the end of the year.

Similarly, business specific intelligence from Kent reports that the **Kingsnorth Power Station** has progressed to the next stage of a government-funded competition to develop clean coal technology. **E.ON**, the energy firm that owns the plant, has been awarded funding by the Department for Energy and Climate change to carry out a study into the engineering and design of a carbon capture and storage unit at the power station in Hoo, Medway.

Agriculture / Rural

Agriculture, hunting, forestry and fishing activities in the UK saw a further decline of -1.1% in Q1 2010 for the seventh quarter running, according to the Office for National Statistics. Output in this sector also dropped by -5.9% for the same period compared to the previous year.

In the South East, anecdotal evidence from the Kent Economic Board suggests that the sector is recording lower profitability due to the rising costs of raw materials and other inputs. Fuel increases are reportedly impacting on agriculture, particularly arable, where input per ton of grain is now averaging £120 and yield is only £90 per ton.

The prospects for the agriculture sector are mixed across the South East. On the one hand, anecdotal evidence from the Kent Economic Board indicates that agricultural land values have risen – as a consequence banks appear to wish to lend to farmers, although increasingly not for diversification. On the other hand, a report from the Surrey LEADER team indicates that there are several small farms which qualify for funding under the LEADER scheme but are unable to secure match funding for these grants from banks.