THE ADECCO GROUP

Manufacturing Sector review

Q1 2017

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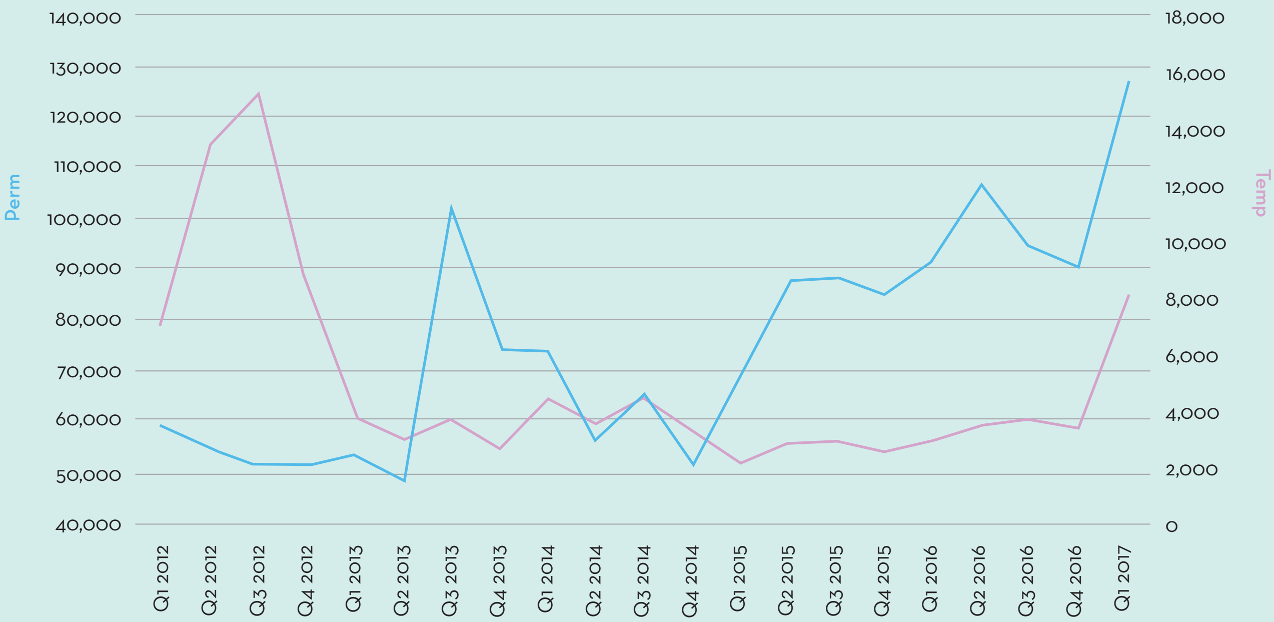
UK Manufacturing Vacancies by Quarter

(Source: Burning Glass)



The start of every year brings increased demand across all sectors and 2017 was no different in the manufacturing industry despite the uncertainty in the UK economy caused by the EU referendum.

The first quarter of 2017 has not even concluded at the writing of this report and there are already over 25% more vacancies than in the final quarter of 2016. More impressively there are also 20% more roles being advertised than during the first quarter of 2016 as well. To top this the final quarter of 2016 was also more buoyant than the previous year.

Short Term Confidence

This confidence is probably not surprising as whilst the EU referendum result has caused confusion and uncertainty it has, in the short term, created favourable market conditions for manufacturers that export.

On the day after the referendum Sterling suffered the biggest one-day fall since the era of free-floating exchange rates was introduced in the early 1970s (8%). It exceeds the largest falls for the other three major world currencies: Euro (-2.75%), US Dollar (-4.8%) and Japanese Yen (-6%, twice).

In the first quarter of 2017 sterling hit a 31-year low against the Dollar, at one point being only worth 1.211 for each dollar. It also fell to a six low against the Euro.

A survey from manufacturing body EEF suggests that growth in UK manufacturing is at a 3-year high with the falling pound allied to the recovery in core markets in Europe.

"The post-referendum wobble that defined UK manufacturing's performance in the second half of 2016 has been left firmly behind with manufacturers now rallying far more strongly than even they had predicted," EEF Chief Economist Lee Hopley said.

The EEF raised its forecast for growth in the sector to 1.0 percent this year, from a previous estimate of a 0.2 percent contraction, and it also increased its estimate for British economic growth as a whole to 1.8 percent from 1.3 percent.

Increased vacancies reflect the increased employment intentions of the sector from a balance of +17 in Q1 to +21 in Q2 2017. The figure represents the balance between those that are expecting to increase their workforce and those that are expecting to reduce it.

Two other surveys also point to short term confidence for the manufacturing sector. The Confederation of British Industry (CBI) reported the highest growth expectations in two-decades. Their rounded balance of +36% is the highest since February 1995.

The Purchasing Managers Index (PMI), compiled by the Chartered Institute of Procurement and Supply (CIPS) and Markit, reported a 30-month high in growth and the fastest rate of job growth for over a year. The survey suggests five consecutive months of employment growth.

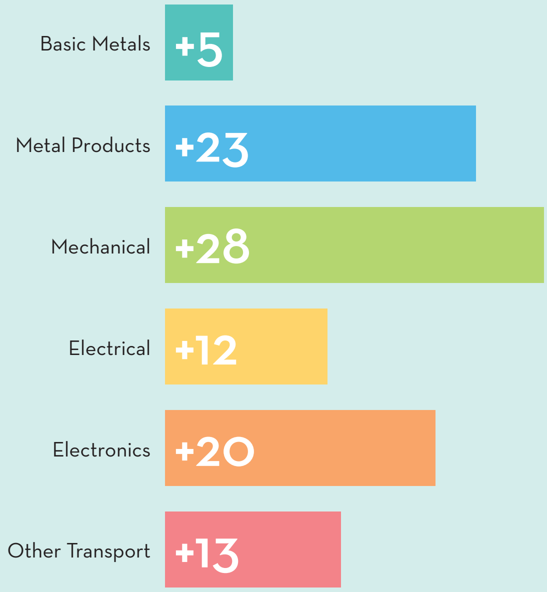
When looking for concrete evidence the UK automotive industry continued its recent strong performance by producing 153,041 cars in February 2017. This was the highest figure in 17 years, boosted by a 13% increase in sales to overseas markets.

Clouds on the Horizon?

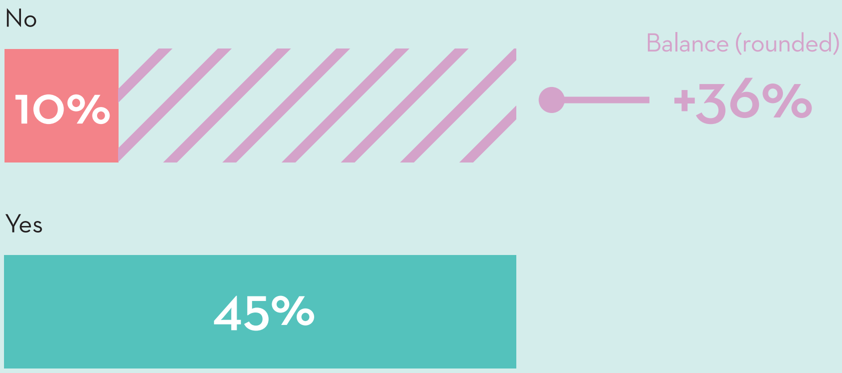
Despite all these positive figures there are things to be worried about for UK manufacturers. As CBI's head of Economic Analysis Ann Leach said: "The flipside is that cost pressure are widespread".

The country is braced for increases in inflation, which will push costs up for a sector which always has to watch the purse strings carefully. In the end the benefits from the deprecation of the currency are likely to be too modest

Employment Intentions Q2 2017
(Source: Manufacturing Outlook Q1 2017, EEF)



Do industrial companies expect to grow in Q2 2017?
(Source: CBI Industrial Trends Survey, March 2017)



to outweigh the costs of high inflation said Samuel Tombs, an Economist at Pantheon.

Higher inflation in will also cause a slowdown in domestic demand which will hurt the sector.

Howard Archer, Chief UK and European economist at HIS Markit believes that "soaring price remain a major concern" but also that overall stable orders point to a slowdown in domestic demand.

In the longer term businesses will also have to contend with the uncertainty of Brexit negotiations which CBI President Paul Drechsler recently called a "Pandora's box of economic consequences". For example, Britain's car manufacturers would face a 10% tariff charge under current World Trade Organisation (WTO) rules.

Mike Hawes, Chief Executive of the Society of Motor Manufacturers and Traders (SMMT) agreed that while the UK market has been more resilient than expected "we have not seen the full effects yet." He also said that the UK must avoid all barriers to trades as it would damage the UK's competitiveness.

The sale of Vauxhall to the PSA Group, makers of Peugeot and Citroen, is a very current example of both the dangers and complexity. The uncertainty around the post-Brexit economy might make the 4,500 jobs in the UK vulnerable to redeployment by the company's new owners.

Previously it seemed that Nissan, although unconfirmed by either party, received assurances that enabled it to commit to continue operations in the UK for the foreseeable future but whether the government is able to offer similar assurances to other manufacturers in far from clear.

Those that have already made announcements in this area include

Weetabix
Low single-digit percentage rise expected

Nescafe
14% rise already

Freddo
(Expected)

Premier Foods
(Mr Kipling & Bisto)
Considering mid-single-digit percentage rises

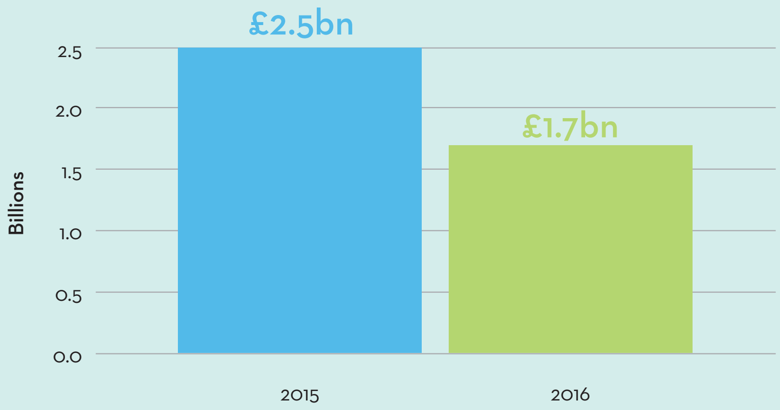
Birds Eye
12% expected

Marmite
12.5% rise already

Walkers
5p increase on most bags expected

Lego
5% rise already

The value of investment that car makers made in the UK fell from £2.5 billion in 2015 to £1.7 billion in 2016.



Rising Prices

Whilst exporters have fared well those importing supplies have seen the other side of the coin, with food manufacturers particularly in the firing line. In many cases they have been forced to respond by increasing prices, which may end up hurting them in the marketplace with consumers.

Additionally Mars has responded by reducing the size of Malteser packets by 15% whilst Toblerone increased the space between its triangles.

An open letter to the government signed by 30 food and drink industry bodies (including the Food and Drink Federation, British Retail Consortium and National Farmers Union) warned that if EU nationals were restricted from working in the UK then food prices would rise further.

The letter, published in the Guardian, says: "Workers from the European Union, some of whom are already leaving the UK, play a significant role in delivering affordable and high-quality food and drink." It says they provide "an essential reservoir of skilled, semi-skilled and unskilled labour."

What this means

The manufacturing employment market will be complicated and tough to predict for some time. Market conditions will play a significant factor in recruitment decisions and they may change both often and swiftly. The value of investment that car makers made in the UK fell from £2.5 billion in 2015 to £1.7 billion in 2016. This kind of uncertainty rarely encourages employers to invest in their workforce.

While market conditions remain favourable for exporters they are expected to increase their temporary workforce. Widespread increases in the permanent workforce for any area of UK manufacturing seem unlikely.

That said, according CV-Library manufacturing is the third largest growing sector in terms of vacancies advertised in the six months following the EU referendum, with 27% more roles than the same period the in 2015.

The status of EU nationals in the UK will have a big impact on the workforce, if large numbers were to leave for any reason then the sector would be forced to replace them. This sudden and largescale increase in demand could also see labour costs rise and also leave the sector far less able to respond to short-term increases in demand.

All employers in the manufacturing sector would be advised to review their current staffing levels and understand the potential impact and skills gaps that might arise from losing EU nationals.