THE ADECCO GROUP

Manufacturing Sector review

Q2 2017

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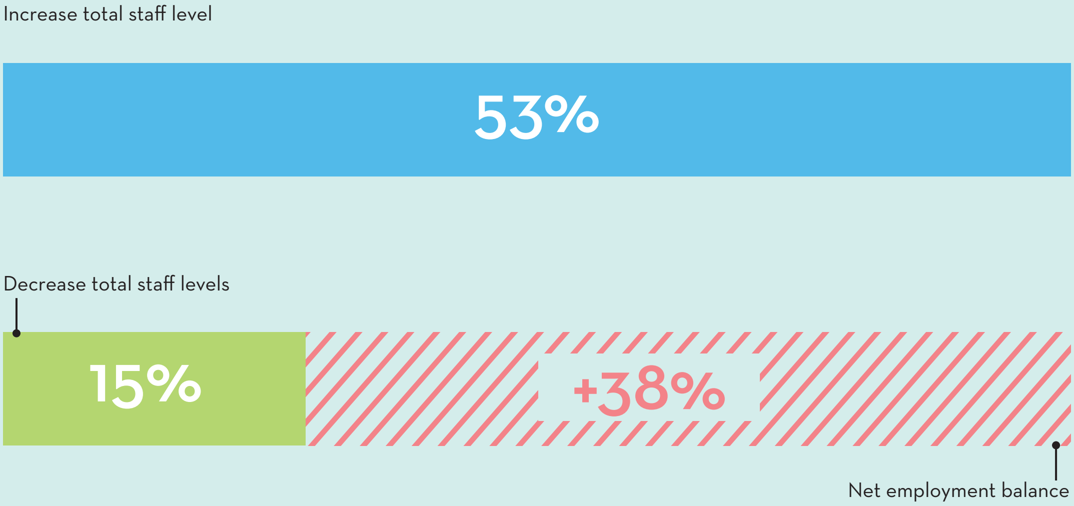
What will the overall effect of your recruitment policies be in the next three months?
(Source: Labour Market Outlook, CIPD/The Adecco Group UK&I, Spring 2017)



The second quarter of 2017 saw the manufacturing sector continue in the confident mood that it started the year in. Output is high and with it comes increased demand for talent.

The number of vacancies fell from the first quarter but this is not unusual in any industry but still remains higher than the year before and any other quarter in the last four years. This chimes well with the Purchasing Managers' Index (PMI) figures produced by IHS Markit which suggests that British manufacturers are enjoyed their fastest rate of expansion in three years during the month of April. Although the index slightly slipped the following month it still remained the highest since June 2014.

Recruitment intentions

The industry appears to be intent on continuing with the hiring boom at least for the coming quarter, according to the Labour Market Outlook report that the CIPD produces along with The Adecco Group UK&I. More than half of manufacturing and production firms expect to increase their workforce in the next three months compared to only 15% that expect it to decrease. This translates into a net employment score of +38% which is nearly twice the UK average (+20).

Manufacturing and production companies were at the same time less likely to be hiring and making redundancies in the next three months. Initially this seems at odds with the larger net employment balance but is likely to be linked to the slightly smaller size of firms in the sector – 55% are classed as small or medium organisations compared to just 41% for the overall sample. Smaller firms are just less likely to have vacancies in any given period that a larger one.

This probably feeds into the fact that companies in the sector currently have, on average, five vacancies, half the UK average.

Another example of optimism in the sector is that half of current vacancies are currently being described as newly created (as opposed to replacement ones), this compares to just 15% of roles across the UK that are newly created.

Reasons to be cheerful

The PMI was far from the only report to suggest that manufacturing was in rude health. Both the British Chambers of Commerce (BCC) and Confederation of British Industry (CBI) reported the strongest growth more than two years, the former in manufacturing exports and the latter in orders.

"The summer sun has come out early for Britain's manufacturers. Robust demand at both home and abroad is reflected in strong order books, and output is picking up," the CBI's Director of Economics, Rain Newton-Smith, said.

A lot of the reason for this continues to be the weakness of the pound whilst still being able to trade with the EU – something that HIS Markit called a 'sweet spot'. The surprise outcome of the UK election caused the pound to sink to a seven-month low against the Euro.

"Many firms tell us their short-term expectations are strong," said Adam Marshall, the BCC's Director-General.

The automotive industry continues to be the shining light, albeit in an industry that is now generally shinier, as it registered a 17-year high at the start of the quarter.

The sector has now been growing since the start of Q3 although the impact of the recent UK election and the subsequent hung parliament is yet to be determined. That said Dave Atkinson, UK Head of Manufacturing at Lloyds Commercial Banking said that employers did not seem worried by the outcome as it would still mean stability through until 2022.

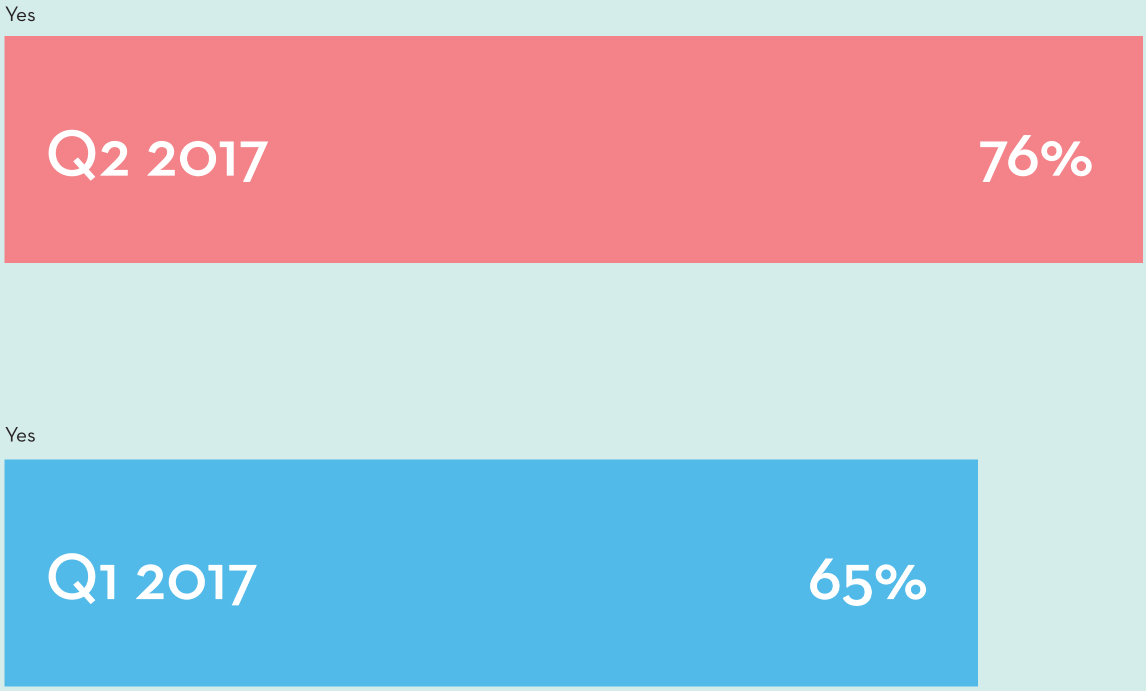
"On this basis, the sector should have sufficient momentum to see it through the uncertainty generated by the current unexpected general election and into the start of Brexit negotiations," IHS Markit Economist Rob Dobson said.

Rising Prices

"We cannot rely in the long term on the boost that exporters have received from a weak pound," said Mike Cherry, Chairman of the Federation of Small Business (FSB).

While the weak pound has been great for exports, the industry also knows this will import inflation which will even things out eventually. The Society for Motor Manufacturers and Traders (SMMT) have already warned on this with chief UK and European Economist Howard Archer suggesting that they might already have seen the peak.

Have raw materials become more expensive this quarter?
(Source: British Chambers of Commerce)



The BCC said raw material costs were having the biggest influence on prices since late 2011, and called inflation "a key risk to the UK's growth prospects". More than three-quarters of employers said raw materials were more expensive than three months ago.

Inflation now stands a touch under 3%, nearly a three year high and now above wage growth, whilst factory-gate inflation is only just below a five-year high at 3.7%.

Outlook for Pay Growth

Employers in this sector expect pay awards to be 2% in the coming year, this is higher than the UK average (1%) but in line with the average for the private sector (2%).

In fact, more than two-thirds of respondents suggested that they were expecting a pay award of 2% or more, with one in ten suggesting above 4%. Despite the apparent optimism within the sector it was not improved profitability that was driving this growth but more inflationary pressures (both current and expected) along with making up for the sluggish growth of recent years.

The ‘Brexit’ Effect

Despite the positive effect that Brexit has had for the industry it has been widely suggested it would be one that would, in the long run, be impacted most heavily. This commentary still continues, mostly in relation to the availability of the workforce.

The EEF became the latest organisation to call for a rethink of the government’s Brexit strategy during Q2.

The parliamentary Environmental, Food and Rural Affairs Committee (EFRA) recently warned that agricultural businesses are facing “considerable difficulties” in recruiting and retaining their workforce. This is because 30% of their workforce is not a British citizen.

This said the Labour Market Outlook Report (LMO) from the CIPD and The Adecco Group UK&I suggested that manufacturing and production firms do not demonstrate any higher employment rates for non-UK nationals than the rest of the UK. Just over half (55%) employ EU nationals with 80% of their workforce still being made up of workers from the UK.

The BCC says that 86% of UK manufacturing firms would like to expand but the majority can’t find the right staff.

It might be supposed that the skills gap is a reason why employers are targeting EU nationals but maybe not according to the LMO. The two biggest reasons for employing EU nationals were better work ethics and an inability to attract UK nationals to fill low-skill roles. Nearly one in four did mention better technical knowledge but not specifically qualifications.

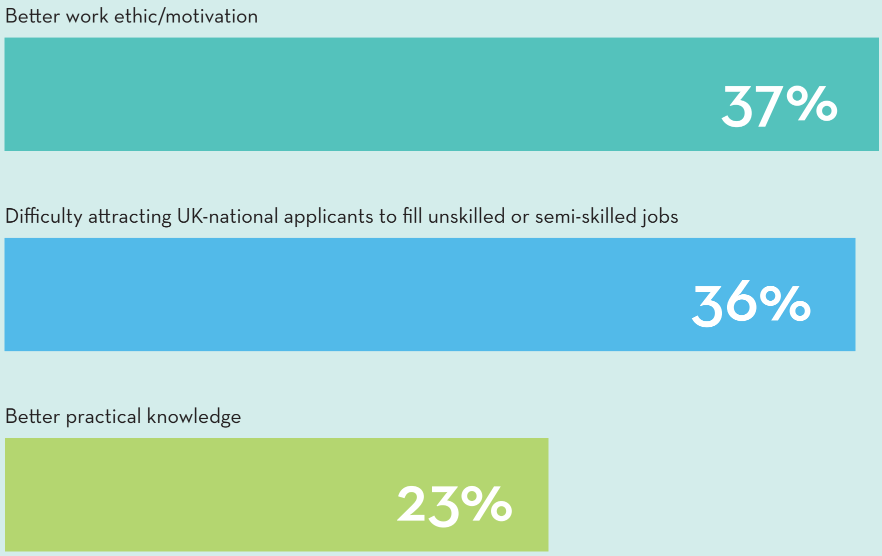
The result of the EU referendum has not affected the industry’s desire to recruit EU nationals; 77% report no change during the last 12 months.

What this means

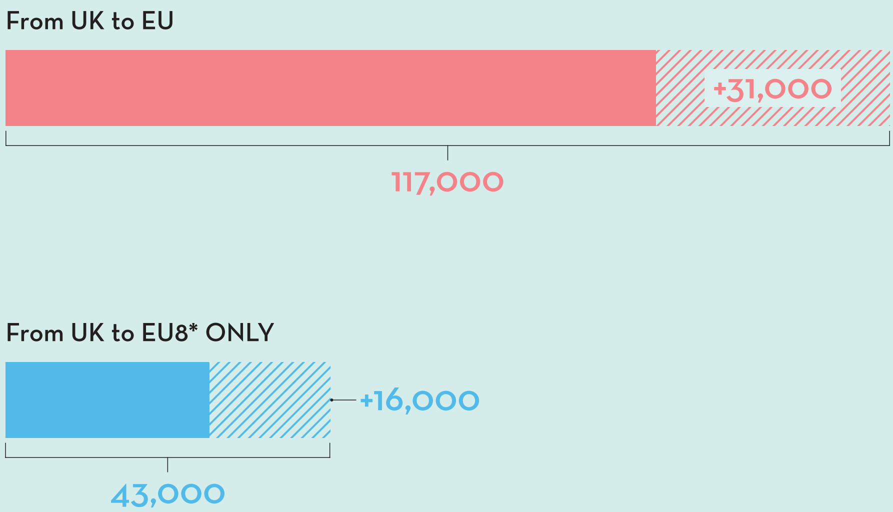
In the short term it seems that UK manufacturing will continue to try and grow and increase its workforce but there are two questions to answer.

The first is how quickly rising prices will start to filter through and impact demand. The European economy is fairly strong at the moment, recording

Why does your organisation employ EU Nationals? (Manufacturing & Production)
(Source: Labour Market Outlook, CIPD/The Adecco Group UK&I, Spring 2017)



Emigration from the UK in 2016
(Source: Migration statistics quarterly report: May 2017, Office for National Statistics)



*EU8 comprises Estonia, Latvia, Lithuania, Poland, Czech Republic, Slovakia, Hungary and Slovenia

the lowest unemployment since March 2009, this could help prolong the economic boom, certainly until the post-Brexit scenario is decided.

The second is whether they can actually find suitable candidates for the vacancies they wish to fill. Skills gaps have been widely discussed with the BCC identifying manufacturing as an area of concern.

The Office for National Statistics has also recently published data that suggests long-term migration to the UK is falling and emigration back to Eastern Europe is rising. This could just be a blip or the start of a longer term trend, if it is the latter then this may curtail the expansion of the sector prematurely – either they would hire less or increase wages to compensate which will further drive up costs.