

# UK Quarterly Industry Report

QUARTER 3 2016

November 2016



## INTRODUCTION

Dun & Bradstreet grows the most valuable relationships in business. By uncovering truth and meaning from data, we connect customers with the prospects, suppliers, clients and partners that matter most, and have done so since 1841. Nearly ninety percent of the Fortune 500, and companies of every size around the world, rely on our data, insights and analytics.

Growth is the lifeblood of business, and its most fundamental driver is the relationships a company fosters with prospects, customers and partners.

Over nearly two centuries of helping businesses understand this dynamic, we have honed the expertise of how data and analytics forge the relationships that lead to industry-leading performance. To activate these capabilities, we build – or co-develop with partners – solutions tailored to your role, whether you are in marketing, sales, finance, supply, compliance or information technology. And we deliver this content however you want to consume it.

Our platform's foundation is the world's largest commercial database, with over 280 million company records we derive from 30,000 data sources and update 5 million times per day. We integrate this insight into your core systems, workflows and cloud-based apps in ways that enhance their impact, and we also integrate with your existing data and third-party data sources. Our DUNSRight® process gives us the unmatched ability to turn an enormous stream of data into the high-quality information you need to grow your most valuable relationships.

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### WITHIN THIS REPORT YOU CAN FIND ANALYSIS OF THE FOLLOWING KEY TOPIC AREAS:

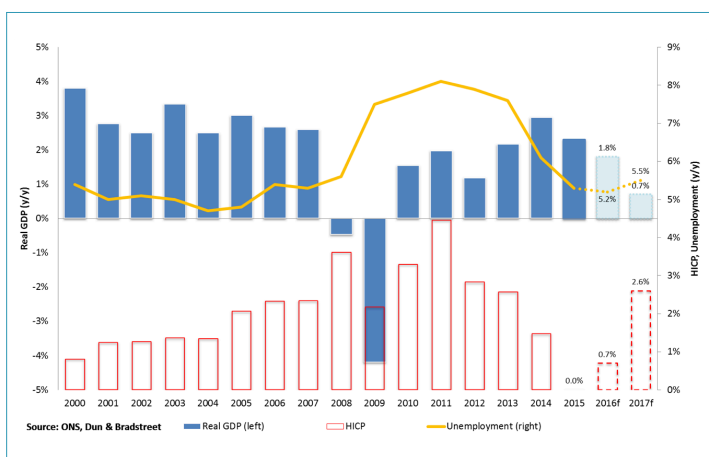
- 1.0 UK Economic Outlook
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We hope you find this report of use – please feel free to share it with others within your own organisation.

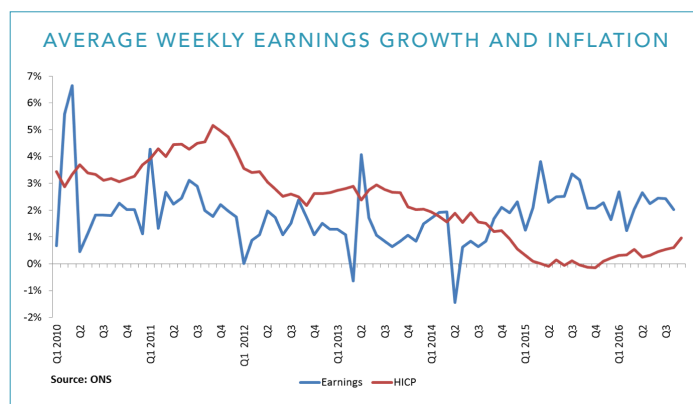
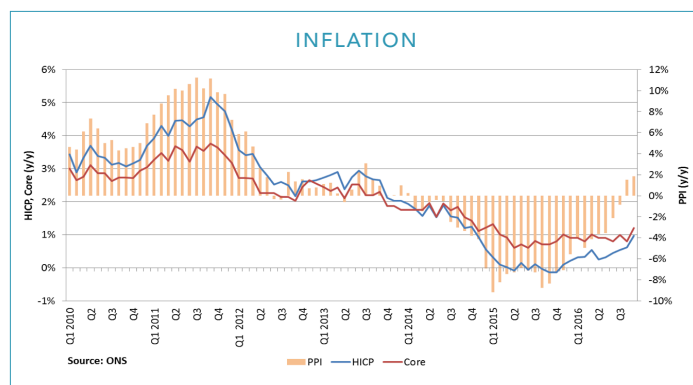
If you would like further information on the range of Dun and Bradstreet products and services that can provide an analysis of your own customer or supplier data, please see the final page in this document for more details.

## 1.0 UK ECONOMIC OUTLOOK

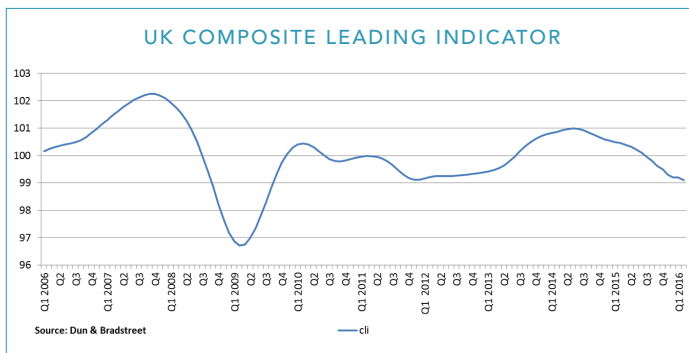
Recently published real GDP growth figures for July-September show that the British economy is yet to respond to the Brexit vote on a noteworthy scale (putting aside the impact on the exchange rate, see below). Overall, the economy grew by 0.5% quarter on quarter, down from the 0.7% seen in Q2 but above the consensus forecast of 0.3%. Meanwhile, recent Purchasing Managers' Index (PMI) figures compiled by Markit for the manufacturing sector create hopes that British industry can finish the year on a high. At 54.3 slightly down from September's 55.5, the PMI remains comfortably above the neutral 50-points line that divides expansion in sectoral activity from contraction; new order inflows – both foreign and domestic – expanded for the third straight month, while production levels continued to rise. Looking ahead, Dun & Bradstreet expects the economy to grow by 1.8% in 2016, not too far below the 2.2% seen last year. Nevertheless, we maintain our relatively pessimistic forecast for 2017, forecasting growth of just 0.7% as companies and consumers cut back on spending and investment in particular amid the unfolding Brexit.



While the sharply weakened British pound (which was down 21% against both the euro and the US dollar in the 12-month period ending 31 October) has shielded the domestic economy against the most adverse Brexit scenarios so far, it will lead to rising inflation rates. The 1.0% year-on-year increase in consumer prices in September (the highest inflation rate since October 2014) gives an idea of what to expect in the months ahead, especially once the important Christmas sales period for Britain's retailers is over. Overall, we expect inflation to reach 2.6% in 2017, overshooting the Bank of England's (BoE) inflation target of 2.0% for the first time since late 2013. Positively for FX risk, BoE governor Mark Carney has announced the extension of his contract by one year to Q2 2019 (keeping him in post until after Brexit – which we expect to occur in Q1 2019). This has eased concerns on FX markets that a change at the helm of the BoE in 2018 would adversely affect the British economy.



In the background to this, the UK fell by one position in the World Bank's recent *Doing Business 2017* report, slipping from 6th to 7th, thereby still outperforming most of its peers. Overall, 7 out of 10 sub-indices deteriorated and 2 stagnated. The only sub-ranking where the UK saw an improvement was 'paying tax'; the country rose from an already high 11th spot to 10th. Compared with the OECD average, it takes fewer payments (8.0 versus 10.9) and less time (110.0 hours versus 163.4 hours) to settle tax bills, with the total tax rate (as a percentage of profits) in the UK also comparing very favourably against the OECD average (30.9% versus 40.9%).



## BREXIT: SHORT-TERM GAIN FOR LONG-TERM PAIN?

Many critics of the UK's decision to leave the EU say the only reason people are not feeling any pain is because Brexit has not really started yet. Pending the invocation of Article 50, and with the UK economy posting stronger-than-expected GDP growth in Q3, an alarming underestimation of the negative long-term consequences of Brexit seems to have gradually superseded the bout of initial pessimism seen immediately after June's vote.

Some metrics of economic performance do indeed suggest that the fundamentals of the economy are solid: for example, domestic output expanded by 0.5% quarter on quarter in Q3. Although this was a little slower than Q2's 0.7% growth pace, it was still faster than the average forecast of 0.3%, defying experts' prediction of an economic recession following a Brexit vote. Furthermore, retail trade growth accelerated over the quarter, while inflation is also gradually picking up on account of a cheaper pound (albeit remaining well below the Bank of England's medium-term target of 2%). September's forward-looking indicators also bode well for future economic activity, with Markit's Purchasing Managers' Index (PMI) for the manufacturing sector rising to its highest level since mid-2014.

Notwithstanding the current economic bonanza, Dun & Bradstreet predicts that Brexit's medium- to long-term economic impact on the UK will be significant and negative. With the UK heading for a 'hard' Brexit, we have downgraded the country's risk rating from DB2c to DB2d (still just within the 'low risk' category). We are also maintaining our 'deteriorating' rating outlook. Prime Minister Theresa May's government intends to

prioritise immigration control and the supremacy of British law over EU legislation, making it increasingly unlikely that the UK will retain access to the EU's common market once Brexit is eventually completed. This will increase the economic cost of Britain's departure from the EU, with the UK being hit harder than the EU.

The possible loss of the passporting rights that currently allow UK-based banks to operate across the EU is a major source of concern. Anthony Browne, chief executive of the British Bankers' Association, recently claimed that Britain's biggest financial institutions are already planning to leave the UK in early 2017, while smaller banks are preparing to relocate before the end of this year. Goldman Sachs is allegedly making plans to transfer some 2,000 employees to a rival European city, and JPMorgan warned that as many as 4,000 jobs could be shifted out of the UK, according to its chief executive, Jamie Dimon. Nomura and Morgan Stanley are also among the companies that could move their operations out of the UK, although the latter recently denied a report that it had already decided to relocate 2,000 workers to either Dublin or Frankfurt.

While the domestic labour market and forward-looking indicators so far remain unimpressed by the looming hard Brexit, the pound is under pressure. In the 12 months ending October 20 the pound lost 18% against the euro, 20% against the dollar, and a stark 32% against the yen. EasyJet and Ryanair, together with several other UK-listed companies, are being affected by a weaker pound. EasyJet and Ryanair, together with several other UK-listed companies, are being affected by a weaker pound. EasyJet is expecting profits to fall by at least a mid-single-digit percentage in the second half of the year compared with the second half of 2015. Ryanair has released its first profit warning since autumn 2013, lowering its growth forecast for the year by five points to 7% in October. Both companies blame their troubles on the fall in the value of the pound since the Brexit vote.

Dun & Bradstreet doesn't expect the currency to recover until the UK's future relations with the EU are negotiated, something unlikely to be completed until the early 2020s. Until then, the battle of sentiment between optimism and pessimism looks set to continue.

## 2.0 GLOBAL ECONOMIC OUTLOOK: HEADWINDS ABATE SLIGHTLY

A series of political uncertainties into 2017 are weighing on the already weak global economic outlook. With resurgent nationalism and protectionism, in both goods and labour markets, impacting on election cycles globally, the November 2016 presidential election results in the US have set the tone for economic developments out into the medium term. Markets had failed to price in the chances of the Trump victory bringing an increase in populist trends into global political discourse. However, the shock of the Brexit vote in the UK had already showed that markets fail to price in political risk. In addition, parliamentary polls are scheduled in The Netherlands, France and Germany in 2017 (plus presidential elections in Austria in December 2016 and in France in Q2 2017). Thus, several key economies in Europe could see a change of government policies towards the economy and the EU itself in the next twelve months.

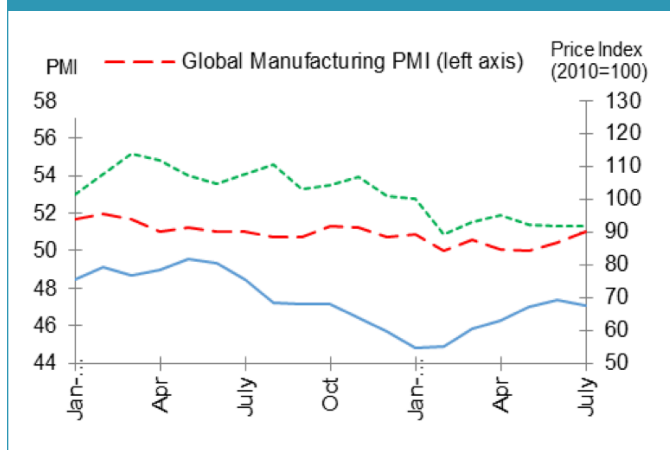
Meanwhile, Prime Minister Theresa May has announced that the UK will initiate Article 50, triggering the two-year period for leaving the EU, by end-Q1 2017. Worryingly, the indications are that the UK will adopt a strategy around a 'hard' exit restricting migrants, which is liable to increase the radical uncertainty for businesses into the medium term. Moreover, the threat from President-elect Donald Trump to withdraw the US from NAFTA has parallels with the 1930 'Smoot-Hawley' Tariff Act which impeded the recovery from the Great Depression.

### KEY RISK: POLITICAL COMPACTS CRUMPLE AS GROWTH VACUUM FEEDS INSTABILITY

The reversion to pre-crisis growth, inflation and interest rates has proved conspicuous by its absence. However, the continued optimism and use of ultra-loose monetary policy that was assumed would stoke inflation, have themselves damaged the sustainability of the macroeconomic trajectory for OECD economies, and emerging markets. Disappointing rates of gross fixed capital formation are likely into the medium term at least, as the false dawns of the post-crisis era have caused a build-up of excess capacity. Discussions in the OPEC cartel over production cuts, and the struggles within Chinese government circles over how quickly to cut capacity and deleverage, are parts of the same phenomenon of how to deal with a world of surplus investment on the verge of deflation.

Besides the unsustainable surge in demand from China in 2008-14, the global population in the rich world is ageing rapidly and taking with it the demand and savings that aided the boom period of 1985-2008. This demographic shadow as the 'baby boomers' retire and become smaller spenders is encroaching rapidly. However, only in recent weeks did one of the US Federal Reserve banks at last admit that the demographic factors at work at the macroeconomic level are real. This imminent negative demographic shock will add to populist pressures in national politics in OECD countries.

#### KEY GLOBAL GROWTH INDICATORS

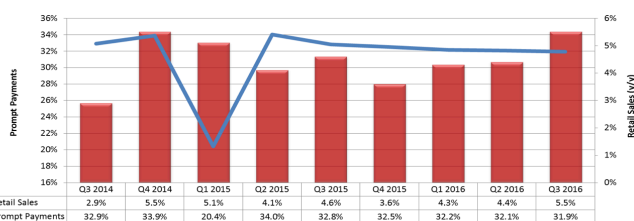


#### REAL GDP GROWTH (%)

	2015	2016f	2017f
World	2.4	2.4	2.7
Advanced economies	2	1.6	1.8
US	2.4	1.6	2.0
Euroland	1.6	1.6	1.5
Japan	0.5	0.5	1.0
UK	2.2	1.8	0.7
Emerging economies	3.4	3.4	4.3
Brazil	-3.8	-3.0	0.9
Russia	-3.7	-0.6	1.4
India	7.6	7.5	7.9
China	6.9	6.5	6.0

### 3.0 PAYMENT SNAPSHOT

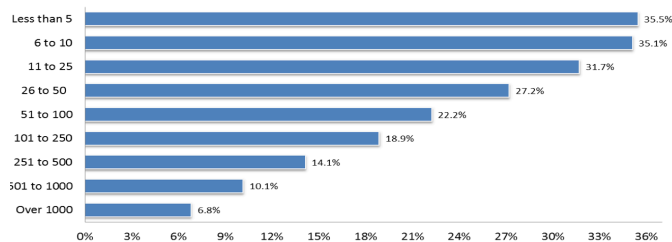
PROMPT PAYMENTS TRENDLINE – Q1 2014 TO Q3 2016



Source: Dun & Bradstreet; ONS

The chart above depicts how promptly all UK businesses have been paying their bills over the past nine quarters (blue line). Despite stronger-than-expected real GDP growth in Q3, a weaker pound, and robust retail sales, Dun & Bradstreet's data reveals that the proportion of prompt payments decreased slightly over the quarter, to reach 31.9% (from 32.1% in Q2). Such a deterioration could be partly explained by the uncertainty triggered by Brexit, which might have affected UK businesses' capacity (and/or willingness) to pay promptly. Looking ahead, we expect a further deterioration in prompt payments due to rising headwinds triggered by June's Brexit vote.

PROMPT PAYMENT BY EMPLOYEE SIZE FOR MARCH 2016

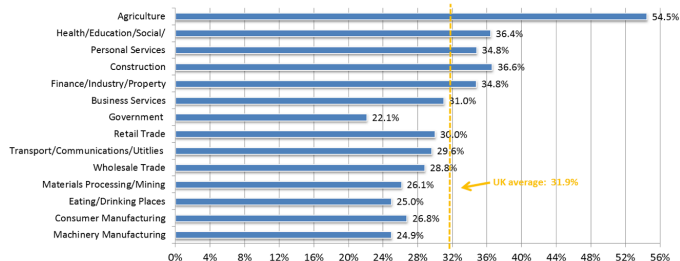


Source: Dun & Bradstreet

As the data in the chart above reflect, larger businesses continue to squeeze their suppliers by paying in a much slower manner than their smaller counterparts. The differential in payment habits between those companies employing 1,000 workers or more and those employing fewer than five is significant: 6.8% (it was 7.5% in Q2) as opposed to some 35.5% (from 36.6% in Q2).

Indeed, late payments remain a major problem for UK-based small and medium-sized enterprises (SMEs). While legislation is in place to assist small businesses with their struggle against late payments, most businesses, especially SMEs, elect to take no action for fear of alienating their larger customers. Indeed, according to the Association of Chartered Certified Accountants (ACCA), firms with fewer than 50 employees are typically twice as likely as larger businesses to experience late payment issues. Besides giving rise to tighter financial conditions and higher administrative, transaction and financial costs (external financing may be necessary to manage cash flows), late payments can cause insolvency and ultimately lead to bankruptcy.

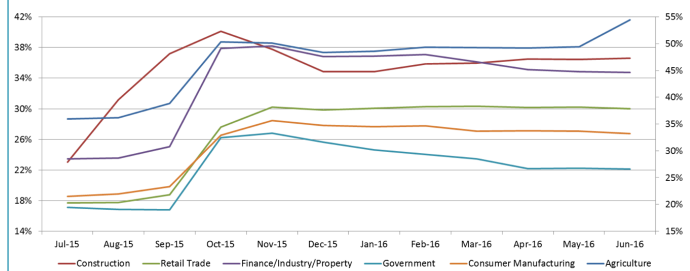
PROMPT PAYMENT BY INDUSTRY, SEPTEMBER 2016



UK average: 31.9%

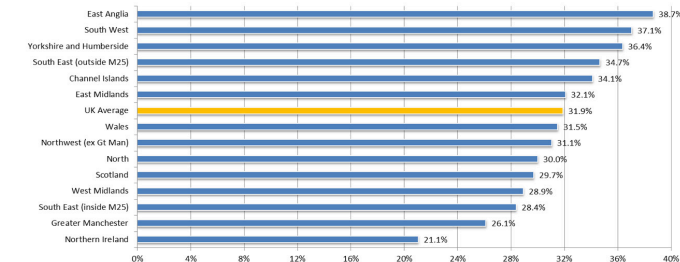
Dun & Bradstreet data show an overall deterioration in payment habits by industry on a quarter on quarter (q/q) basis in Q3 2016. The data, broken down by industrial sector, reveal that between Q2 and Q3 2016 the largest deterioration in payment habits was recorded in the 'Eating and Drinking places' sector, followed by the 'Finance/Industry/Property' and 'Government' sectors. 'Agriculture' and 'Construction' were the only two sectors recording an improvement in prompt payments, up by 5.2% q/q and by 0.6% q/q, respectively.

PROMPT PAYMENT EVOLUTION IN CRITICAL SECTORS (AGRICULTURE, RIGHT AXIS)



Source: Dun & Bradstreet

PROMPT PAYMENT BY REGION, SEPTEMBER 2016

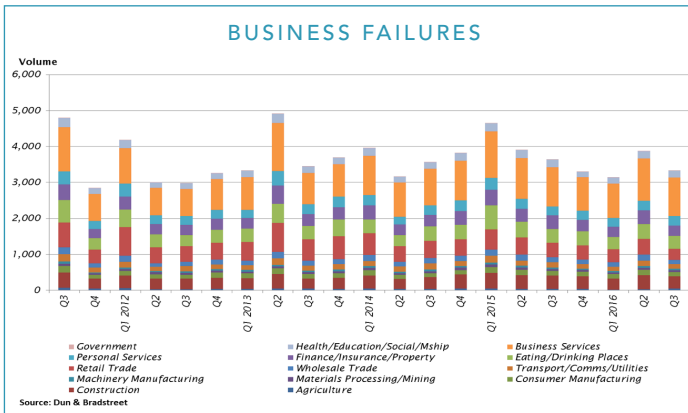


Source: Dun & Bradstreet

Dun and Bradstreet's Q3 data reveal that overall payment performance has (slightly) worsened in all regions, barring the West Midlands. In particular, the North's and North West's average prompt payments (as a percentage of total payments) dropped to 30 % and 31.1% respectively from 30.6% and 31.5% respectively in Q2. The Greater Manchester area and Northern Ireland continue to lag behind all the other regions, while East Anglia and the South West exhibit the best payment performance times (the former for the second consecutive quarter).

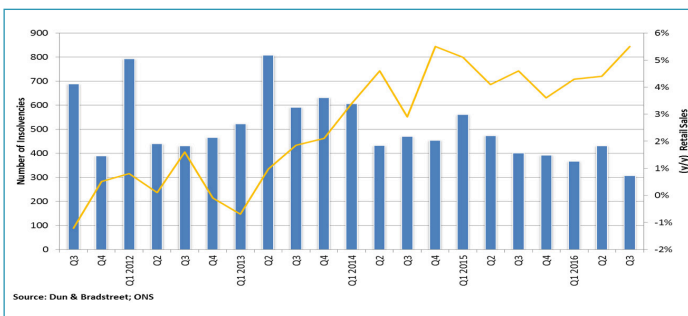


## 4.0 BUSINESS FAILURES



Dun & Bradstreet data for the third quarter of 2016 showed a drop in the amount of corporate insolvencies: some 14% lower than the preceding quarter, possibly tracking the resilience of the economy, which expanded more than previously anticipated in Q3. Between Q2 and Q3 2016, corporate insolvencies were down in almost all the sectors of the economy, with decreases of 35.5% q/q in 'Whole Trade' and 28.5% q/q in 'Retail Trade'. 'Government' and 'Agriculture' were the only sectors to see an increase in the amount of bankruptcies, up by 150% q/q and 84% q/q, respectively:

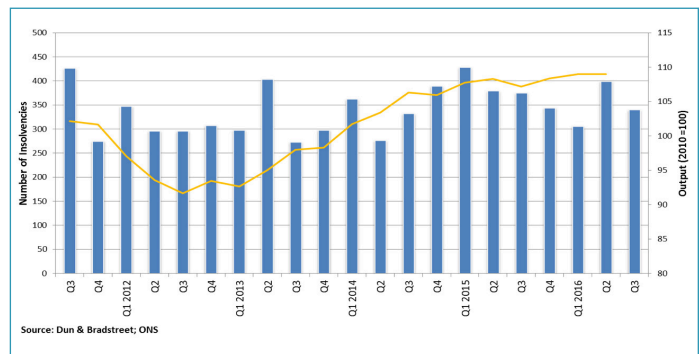
### BUSINESS FAILURES: RETAIL TRADE



The number of insolvencies in the retail sector (which accounts for almost 6% of the UK economy) decreased in Q3, tallying with the latest (post-Brexit vote) retail sales data showing a strengthening of momentum in household purchases. ONS seasonally-adjusted retail sales volume rose by a robust 5.5% y/y in Q3, following a 4.4% y/y increase in Q2. As we expect a slight increase in the unemployment rate on account of slower GDP growth, so we expect retail sales growth to decelerate in the quarters ahead. Lower sales growth could lead to a small rise in the number of bankruptcies in the coming quarters.

The ongoing decline in our recently compiled leading indicator for the UK economy supports this view, and suggests that a small rise in the number of bankruptcies is likely in the coming months. Against this backdrop, the uncertainty surrounding the retail sales outlook remains high, but risks to the upside and those to the downside are broadly balanced. On the upside, real wage growth and the still-low unemployment rate will continue to provide a boost to domestic sales volumes. On the downside, a slowdown in overall economic growth and Brexit could weigh on consumer spending.

### BUSINESS FAILURES: CONSTRUCTION

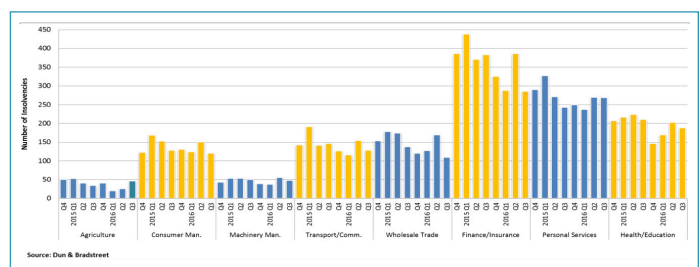


After falling for the previous four quarters, the number of construction companies going bankrupt rose again in Q2. In Q3, however, fewer companies went bankrupt than in the previous three months: 340, compared with 399 in Q2. The construction industry plays an important role in the UK economy. The entire sector contributes £90bn in gross value added to the UK economy and supports 2.9m jobs. Improved momentum in this sector is likely to bolster real GDP growth in the quarters ahead.

The latest seasonally adjusted Markit/CIPS UK Construction Purchasing Managers' Index (PMI) tallies with the implied strengthening of momentum in the sector. The PMI posted a reading of 52.6 in October, up from 52.3 in September and above the 50-point expansion threshold. Markit's report reveals that UK construction companies recorded a sustained expansion of overall business activity in October, driven by another robust increase in residential work. New order volumes also rose across the construction sector, but the rate of growth had eased since September and remained weaker than that seen prior to the summer.

Against this positive backdrop, October data on confidence in construction surprised on the downside. The confidence survey released monthly by the European Commission revealed that pessimism in the sector worsened to -5.6 points from -0.1 previously.

### BUSINESS FAILURES: OTHER SECTORS



The chart above shows the number of business failures in several critical sectors. Insolvencies dropped by some 14.5% q/q in 'Machinery Manufacturing' and by some 26.2% q/q in 'Finance and Insurance'. Bankruptcies rose in the 'Agriculture' sector by 84% q/q.

## 5.0 RISK OF FAILURE AND PAYMENT DELINQUENCY – INDUSTRY SECTOR COMPARISON

		RISK OF FAILURE	
		<b>RISK</b> (Rating 1,2,3) Minimal to above average risk	<b>HIGH RISK</b> (Rating 4)
RISK OF VERY SLOW PAYMENT	<b>HIGH RISK</b> (Delinquency Score $\leq 11$ )	<b>CASH CULTURES</b> UK AVERAGE – 13% RETAIL – 10% CONSTRUCTION – 13% Offer discount for prompt payment Charge interest on late payments Reset payment terms accordingly Improve relationship with client to induce prompt payment	<b>TROUBLE – LET YOUR COMPETITORS HAVE THEM</b> UK AVERAGE – 3% RETAIL – 3% CONSTRUCTION – 4% Increase prices to cover risk Reduce exposure - stop orders until paid Take guarantees Monitor vigorously Avoid new clients with this profile Up-front payment
	<b>RISK</b> Minimal to above average risk (Delinquency Score $\geq 10$ )	<b>IDEAL CUSTOMERS – CULTIVATE</b> UK AVERAGE – 69% RETAIL – 73% CONSTRUCTION – 84% Push for more sales Strengthen relationship with client	<b>MONITOR CLOSELY</b> UK AVERAGE – 1% RETAIL – 1% CONSTRUCTION – 2% Reduce exposure – minimise outstanding orders Monitor vigorously Take guarantees

Dun & Bradstreet's statistical analysis reveals that some 3% of UK businesses are deemed to be at high risk of failure and are highly likely to pay in a severely delinquent manner, while 69% offer a low risk of failure and of slow payment. Sales emphasis towards these latter businesses will enhance opportunities and enable suppliers to reduce risks of non-payment. Additionally,

some 7% of UK businesses fall within the lower risk categories (minimal to above-average risk) and are thereby less likely to fail; however, the payment habits they exhibit are somewhat slow, and while suppliers can be fairly secure in the knowledge that the business will not fail, payment may be somewhat protracted.



## DUN & BRADSTREET'S OVERALL RECOMMENDATIONS

- We have downgraded the country's risk rating from DB2c to DB2d (still just within the 'low risk' category). We are also maintaining our 'deteriorating' rating outlook.
- Count on the economy growing by 0.7% only in 2017, down from our pre-referendum forecast of 2.0%.
- Expect the government to invoke Article 50 of the Treaty of the EU (the legal basis for EU exit) in early 2017, setting the EU exit date for early 2019.
- In general we recommend that firms should adopt a wait-and-see approach, as it will take many more quarters until the full impact of the Brexit vote is completely felt.
- Expect the UK to lose full access to the EU's common market, although certain sectors should be able to trade more easily than others.
- The costs of Brexit will outweigh the benefits for the UK economy, at least over the medium term, with exporters to the country being hit the hardest.



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### ABOUT DUN & BRADSTREET

Dun and Bradstreet is the world's leading source of commercial information and insight on businesses, enabling companies to Decide with Confidence for over 170 years. Dun and Bradstreet's global commercial database contains more than 230 million business records in over 190 countries with nearly 700 million payment and bank experiences. The database is enhanced by Dun and Bradstreet's proprietary DUNSRight Quality Process, which provides our customers with quality business information. This quality information is the foundation of our global solutions that customers rely on to make critical business decisions.

Dun and Bradstreet provides solution sets that meet a diverse set of customer needs globally. Customers use Dun and Bradstreet Risk Management Solutions to mitigate credit and supplier risk, increase cash flow and drive increased profitability; Dun and Bradstreet Sales and Marketing Solutions to increase revenue from new and existing customers; and Dun and Bradstreet Internet Solutions to convert prospects into clients faster by enabling business professionals to research companies, executives and industries. For more information, please visit [www.dnb.co.uk](http://www.dnb.co.uk)

Dun and Bradstreet also have a team of economists dedicated to analysing the risks and opportunities of doing business across the world, monitoring 132 countries on a daily basis. For further details please contact Country Risk Services on 01628 492595 or email [CountryRisk@dnb.com](mailto:CountryRisk@dnb.com).