

## Summary of economic conditions

- According to the latest Purchasing Managers Index (PMI) Survey, **business activity in the South East increased in July for the first time since June 2008**. There was an **increase in new orders for the first time since April 2008**. Largely anecdotal evidence from businesses and business representative organisations bears this out, with a **slight improvement in business conditions in the region in August**. However, some firms are still experiencing falling output, orders and profit margins.
- The latest Federation of Small Businesses (FSB) Snap Poll Survey (August 2009) shows that **41% of small businesses in the South East have seen a decrease in trade in the past two months**. This is similar to the previous survey (42% in June) but significantly lower than in late 2008 and early 2009. **Rural businesses in the region performed slightly better on average than urban businesses**, with a higher proportion reporting increases in trade (27% compared to 22%).
- According to the PMI Survey, employment in the region fell for the 13<sup>th</sup> consecutive month in July. **Unemployment continues to rise in the South East**, to a greater degree than many other regions in the three months to June. The **number of Job Seekers Allowance claimants increased by 1,400 in July** to 153,600. **Redundancy notifications fell** from 2,200 in July to 1,300 in August. However, some parts of the region that had previously avoided large-scale redundancies are starting to see a slight increase in job shedding. In Berkshire, a Business Link survey in July found that one quarter of firms are considering cutting staff or changing employee hours – an increase on the April survey.
- The most recent Institute of Chartered Accountants in England and Wales (ICAEW) Business Confidence monitor shows that while business confidence rose in all regions over the past quarter, **businesses in the South East are amongst the most cautious in the country**, with significantly more firms remaining wary rather than confident about economic prospects. Confidence overall is up, but manufacturers and larger businesses remain cautious about their prospects for the future.

## Key challenges and hotspots

- **Credit conditions remain tight, but there are some signs that bank overdrafts and term lending are returning to a manageable level** for many small and medium enterprises (SMEs). The August FSB Survey showed that the proportion of businesses that had been refused credit fell over the past few months, to 14%. However, the cost of existing finance increased for 28% of FSB members in the region – up from 22% in June. Anecdotally, late or extended payment is still a problem.
- The Confederation of British Industry (CBI) reports that **many firms in the region's service sector are suffering heavy price competition**, which is driving down profitability. However, business and professional firms are reporting an increase in new business for the first time in over a year. In general, **prospects for business expansion and investment are the least gloomy they have been for some time**.
- Business **investment continues to fall sharply** and this is a major factor which could impact on the speed of the recovery.

## Business specific intelligence / information on key questions

- **There appear to be few signs yet of sustainable growth emerging in the South East**. In some sectors, destocking is continuing, but where output is on the increase it is too early to say whether this is the result of a genuine upturn in demand or simply a result of restocking. So far the recession has served to 'squeeze out' weaker businesses and those who were unable to obtain sufficient finance to fulfil orders. Those businesses that have survived remain cautious about prospects for sustained growth in the short-term.

## Sectoral Overview

**Manufacturing:** There are mixed fortunes for manufacturers in the region. According to the CBI's latest Industrial Trends Survey, which covered 560 manufacturers in the South East in late July and early August, demand is still weak, but expectations for the next three months are the least negative they have been since June 2008. However, Engineering Employers Federation (EEF) reports that the proportion of firms in the manufacturing sector implementing pay freezes rose for the eleventh consecutive month in August, to 78%. Fewer firms are requesting advice about redundancies compared to earlier in the year, but many companies are still reporting major redundancy programmes and cost cutting exercises. For example, **GE Aviation** is to shed 96 of the 898 jobs at its aerospace engineering factory in Hamble, Hampshire. Within the manufacturing sector, companies working in defence related fields are facing challenges because of uncertainty about the levels, nature and timing of future defence spending. However, a piece of positive news is that **BAE Systems** have won a torpedo support and maintenance contract up to 2019 (for the Royal Naval Spearfish and Sting Ray weapons). The contract will support 120 jobs in Portsmouth and over one-third of the contract value will go to sub-contractors in the UK.

**Automotive:** The scrappage scheme is generating some demand, but in some parts of the region there is a degree of scepticism as to how much of this is genuinely additional demand. There is still evidence of destocking by many car dealers. Larger, less economical cars are continuing to prove difficult to sell, but there is high demand for smaller, economical cars. **Suzuki** is opening new dealerships in Sittingbourne in Kent and Worthing in West Sussex in September 2009.

**High-tech engineering / IT / R&D:** Investment in many high-tech engineering firms is continuing, but cautiously. Businesses are aiming to continue to develop new or improved products and processes in order to remain competitive and to secure more orders. Some companies are reportedly also considering how to share resources with sister organizations in order to improve efficiency. High-tech firms are continuing to hire skilled workers where needed. There is significant movement of skilled engineers between businesses currently, due to redundancy and resultant recruitment drives. **Surrey NanoSystems** is looking to create hundreds of jobs at its East Sussex-based carbon nanotubes business over the next three years, having just secured £2.5m of funding that will create an initial 12 engineering jobs. Meanwhile, **Wolfson Microelectronics** is setting up a 17,000 sq ft office at Newbury Business Park in Berkshire.

A number of large businesses with research and development (R&D) units in the South East are looking to cut programmes that do not offer a short route to market, or to reposition R&D units as commercial profit centres, in order to reduce overheads. There is a danger that R&D units can be vulnerable when companies undergo restructuring processes, especially if this is driven by financial imperatives alone. Once a unit has closed, the skills and projects tend to be lost forever.

Some IT firms are finding that projects have been reduced in scope or split up into smaller projects by their clients, which is less cost effective as each separate project incurs start-up costs. There are continued problems with customers not paying on time, and many firms are continuing to cut costs – including reducing or stopping R&D work as greater investment is focussed on boosting sales.

**Construction / property:** The gestation period for construction projects is getting longer, with the result that it is more difficult to encourage clients to invest and to keep workers fully employed. It also means that the price agreed at the beginning of a project may not be enough to cover any increase in costs incurred during the life of project. More generally, fluctuations in the volume of work at the current time makes planning difficult for construction firms. Business specific intelligence shows that **Balfour Beatty** is considering plans to close its Mansell building operation in Ringwood, Hampshire, with the loss of up to 40 jobs, while **SIG** is planning to close six of its 12 interior building materials factories in the Midlands and the South East, with the loss of 300 jobs. On the positive side, **Costain**, the construction company with a head office in Maidenhead, Berkshire, is planning to

## **Regional Intelligence Snapshot for the South East (cont'd)**

recruit at least 200 extra people over the next year, including project managers, engineers and health and safety staff.

In the property market, many estate agents (and associated businesses such as providers of Home Information Packs) report strong demand for quality, realistically priced properties in some parts of the region, including Surrey. Demand is currently outstripping supply in this county. By contrast, there is an oversupply of properties in some sectors of the rental market – particularly one and two bedroom starter flats – with the result that rent yields are generally lower than landlords would prefer. Commercial property is “still in the doldrums” (Business Link Surrey), with continued low demand for space. Some businesses are looking to relocate to premises where rentals per square foot are less expensive, but only if this coincides with their current lease ending. Retail property continues to fare badly because of weaker consumer demand. In some cases ‘pre-pack administrations’ are being used as a way of preventing store closures by arranging lower rents. As an example, 51 of the 142 Allied Carpets stores were recently saved from closure in a pre-pack administration by the firm’s previous owners.

**Retail:** Generally larger retail centres are performing better than smaller ones, with footfall up in Brighton, Slough, Windsor and Reading in July compared to the same month in 2008. Retail voids are still increasing as businesses choose not to renew leases rather than close through liquidation. One or two retail units are closing per month in most Surrey town centres, with the exception of Guildford, where a scarcity of units prior to the recession has served to keep demand relatively high. Value retailers (such as Poundland) are reporting brisk business as customers look for bargains. **The 99p Store** chain is opening a branch in many former Woolworths’ premises across the South East. However, it is not clear whether the tight margins on which these businesses operate will survive the high rents and rates in areas like Surrey in the longer term. Traditional retailers (like Robert Dyas) have recently introduced ‘value’ lines to try to prevent customers switching to discount stores.

**Tourism / Hospitality:** Overall there is a mixed picture in this sector. Some businesses reportedly enjoyed their best ever trading weeks in July, while others say the situation is serious. The popularity of the ‘staycation’ has resulted in increased footfall at some local tourist attractions, but they are still finding it necessary to provide offers to attract price sensitive customers. The poor weather has badly affected admissions at some outdoor attractions, while ancillary spend in gift shops and cafes is under pressure. Many restaurants have experienced the usual relatively quiet August, but some sandwich and coffee shops have reportedly been forced to close because reduced demand earlier in the year has left them unable to cover the normal holiday season downturn financially, and because demand for corporate catering is down.

Lead times for booking business meeting and conference accommodation are still falling, but there are hopes that bookings will pick up in the autumn and winter after the traditionally quiet summer period, albeit with customers still seeking good deals. One concern now is that venues which have offered large discounts may struggle to restore their profit margins when the upturn comes, while those who have tried to maintain prices, while suffering in the short term, could be in a better position for the recovery. Despite generally slow business in the hotel sector in recent months, a number of hotel chains have announced plans to open new hotels in the South East. For example, **Jurys Inn** has raised £60m to fund the expansion of its chain of 21 hotels, with a new hotel due to open next year in Portsmouth. Meanwhile, **Premier Inn** has been given permission to build a new 121 bed hotel in the Medway Valley Leisure Park in Strood. Kent. It will be one of five new hotels built across the UK by the Whitbread-owned hotel group over the next five years.

**Energy / waste management:** Current challenges for the energy sector include the price of fossil fuels; higher input prices partially driven by the Euro exchange rate; and poor weather conditions for ground-works. However, there has been some positive news in the sector in the past month, with **Oxford City Council** planning to build a £3m wind turbine in Cowley. Some waste management

firms in the region are finding it challenging to respond to contract opportunities with their current reduced staff levels.

**Higher Education:** Some smaller companies are suspending their interest in Knowledge Transfer Partnerships due to economic uncertainty. However, some multinational partners at the University of Surrey are increasing their focus on innovation and R&D to prepare for the upturn. Student placements are still popular with companies, as they are seen as good value for money. Elsewhere, **The University of Greenwich** has decided to appoint nine specialist research staff to its School of Science, based in Chatham Maritime.

**Voluntary / community:** Two thirds of respondents to a survey in July by the umbrella group for the voluntary and community sector in the South East, Regional Action and Involvement South East (RAISE), had seen an increase in demand for their services (slightly up on the April survey), though this now appears to be reaching a plateau. Funding concerns are beginning to stabilize: around one third of organizations predict no change in public funding for the Voluntary and Community Sector (VCS) in the next 6 months, while 61% think spending will fall (less than in the April survey). The number of respondents seeing an increase in income is at its lowest level since January 2009. Two fifths of respondents have seen a decrease in income in the past 3 months and two fifths have seen no change. Public donations are lower than usual, and organizations who rely on income from Trust funds are suffering as the rate of return on deposits has fallen significantly.

The majority of respondents (86%) had not made any redundancies in the past 3 months (though this figure is slightly lower than 3 months before). Many organizations in Surrey are reportedly having to shed staff and cut back on all but core service provision. Several are considering how they can work more closely with other voluntary organizations to share costs. Some organizations in Hampshire are reportedly still recruiting staff, while others have had to make redundancies once contracts for particular projects have ended.

Key challenges for the voluntary and community sector currently include financial concerns (reduced or uncertain income); a need to adapt to increasing demand for services and changing client needs; and a need to demonstrate the value of the VCS to statutory funders in order to secure future funding. The main issues affecting local communities currently are increased debt and a lack of jobs or limited access to jobs. VCS organizations are finding it difficult to meet continuing demand for debt advice, requests for Debt Relief Orders and mortgage rescue advice.

**Redundancy Notifications:** According to HR1 data, the level of redundancy notifications fell again in August. There were some 1,300 redundancy notifications in the South East in August against 2,200 in July 2009.<sup>1</sup>

The service sector (excluding retail) continues to account for the greater proportion of redundancies, totalling 66% of all notifications in August. In comparison to the marked increase in retail notifications witnessed in July, for the first time this year there were no large redundancy notifications in this sector in August. As seen in the previous three months the number of redundancies in the construction sector fell again this month. A quarter of all notifications were in the manufacturing sector, although the total number fell in August compared to the previous month.

All sub-regions, with the exception of Milton Keynes and Surrey, saw a fall in the number of notifications and there were no large notifications in Buckinghamshire, East Sussex or West Sussex. Berkshire, Milton Keynes and Surrey continue to be affected by redundancies in the service sector, with Milton Keynes and Surrey experiencing a rise in the number of notifications compared to July.

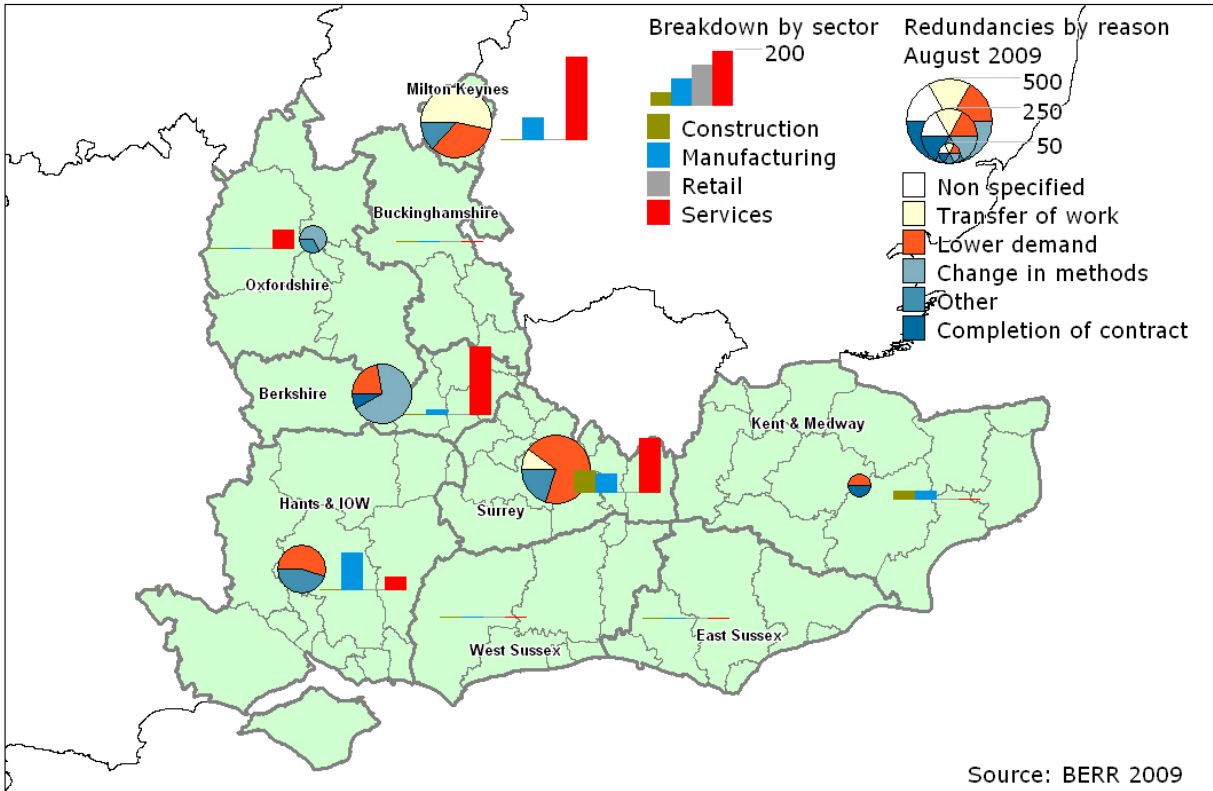
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<sup>1</sup> Note that this data only captures redundancies of more than 20 employees; some of the job losses are not scheduled to take place until later in 2009; and in some cases the redundancies are happening in another region but are registered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

**Regional Intelligence Snapshot for the South East (cont'd)**

A drop in the number of notified redundancies in the construction sector coincides with a fall in the number of notifications attributed to the completion of contracts. Lower demand is the reason cited for approximately 40% of all notifications across all sectors and the majority of redundancies in the manufacturing sector.

**Redundancy notifications by sub-region, volume, reason and sector  
August 2009 (Source: HR1 data via BERR / Job Centre Plus)**



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