ECONOMIC SURVEY

QUARTER 4
2022

IN ASSOCIATION WITH

North East England
Chamber of Commerce

Durham
University
Business School

FOREWORD

Even as we enter a recession, many of the indicators in this quarter's economic survey suggest that there are at least some signs of improvement over the previous outlook for business in the North East. The overall outlook continues to be one of concern, but this quarter's results do suggest that while inflationary pressures remain, some of the more extreme impacts are continuing to ease. These points of optimism are vital for businesses in our region, as the general decline across indicators of future activity and performance reflect how concerned organisations are about 2023.

Inflation, energy prices and staff costs all continue to trouble more businesses. However, the extreme increases that we have seen in these indicators through previous quarters has tapered off, with more measured growth in this survey. Interest rates and taxation have grown significantly as categories of concern for all businesses. It will be important to monitor how businesses respond to these evolving challenges through 2023.

This quarter's results also show services and manufacturing firms needs diverging significantly. Inflation and energy prices continue to represent the top concerns in both industries. However, manufacturing organisations are more concerned with taxation and exchange rates, while services organisations find staff costs and shortages more worrying.

This quarter's findings also reflect the culmination of a tumultuous period in politics. The data collection period for Q3 ended before the Truss government's mini budget and this quarter's window included the new Chancellor Jeremy Hunt's autumn statement. This survey therefore represents how businesses sentiment has changed through this period and provides a vital insight into how government policy has impacted the business environment in the North East.

Thank you to everyone who has contributed to the survey throughout 2022. As we navigate the year ahead it will be more important than ever that we as a Chamber represent your concerns regionally and nationally. Participating in this survey is a vital way that your voice can be heard. We will continue to use this insight to makethe North East stronger and fairer.

As ever, we are stronger together.

Andrew Haigh
Chamber president

OVERVIEW

The fourth quarter of 2022 was impacted by several geopolitical challenges and the cost-of-living crisis. While many indicators show a healthier business environment than in the last two quarters, this is not reflected in future indicators, with businesses clearly concerned about the future. This is not surprising as we notice that the UK economy, except for business investment, has also struggled to grow. The forecast from the British Chambers of Commerce (BCC) suggests that the UK economy will not return to growth until Q4 2023. Contributors to this are the fall in household spending because of rising energy costs and falling real wages. There also is a slight easing of inflationary pressure, in part due to the Government's energy price guarantee. This is likely to have an impact on the energy and production costs in Q1 of 2023, especially with the backdrop of pressure on employees seeking higher wages via industrial action.

In recruitment, while the workforce and future workforce indicators have decreased -18.6% and -16.5% respectively since last year, there is a shortage in some sectors that could lead to price pressures in 2023. At the UK level sectors like technology, health and services continue to struggle to fill vacancies which could potentially exacerbate the current inflation issue. Businesses are not optimistic about the future, as while the current workforce has increased by 2.3% in the last quarter, the future workforce has declined by 7.7%. Cashflow too is also still depressed, although less so than last quarter. Businesses are trying to mitigate this by continuing to invest in their training and plant plans.

Inflation and Energy costs are the two main business concerns and could potentially have an impact on inflation in 2023. The geopolitical situation in Europe remains highly uncertain and could have an impact on energy prices particularly if the government does not implement further energy price controls from April 2023. After a slight dip in most concerns in Q3 relative to Q2, percentages of businesses concerned about almost all issues (exception of competition and staff shortages) have either increased again or levelled off, suggesting that longer-term concerns are setting in for businesses. More businesses are concerned about all indicators except red tape than last year, reflecting the challenging business environment. Interest rates and taxation are the most significantly increased concerns relative to Q3.

Professor Kieran J Fernandes
Professor in operations management
Durham University Business School

KEY INDICATORS

INDICATOR	ALL COMPANIES	CHANGE ON LAST QUARTER	CHANGE ON LAST YEAR	MANUFACTURING	
UK Sales	9.5	-1.7 ▼	-9.8 ▼	11.1	8.7
UK orders	5.6	-0.7 ▼	-16.4 ▼	7.4	4.7
Export sales	10.9	2.7 ▲	9.7 ▲	10.7	11.1
Export orders	5.5	2.4 ▲	5.5 ▲	3.6	6.9
Plant investment plans	14.8	10.4 ▲	2.2 ▲	29.0	6.2
Training investment plans	15.4	5.4 ▲	3.0 ▲	14.1	16.1
Cashflow	-7.7	8.9 ▲	1.5 ▲	-6.9	-8.1
Current prices	42.3	-12.0 ▼	16.8 ▲	56.5	35.8
Future prices	48.7	2.1 ▲	3.5 ▲	58.9	44.2
Current workforce	16.1	2.3 ▲	-18.6 ▼	18.3	15.2
Future workforce	22.3	-7.7 ▼	-16.5 ▼	24.7	21.3
Future profitability	4.9	6.0 ▲	-14.3 ▼	16.4	0.0
Future turnover	25.9	-3.9 ▼	-27.4 ▼	31.5	23.6

The Economic Survey is carried out by the North East England Chamber of Commerce in partnership with Durham University Business School. This survey was conducted during November 2022 and is based on responses from 247 businesses. The Chancellor's Autumn statement took place near the middle of the data collection period on 17 November 2022.

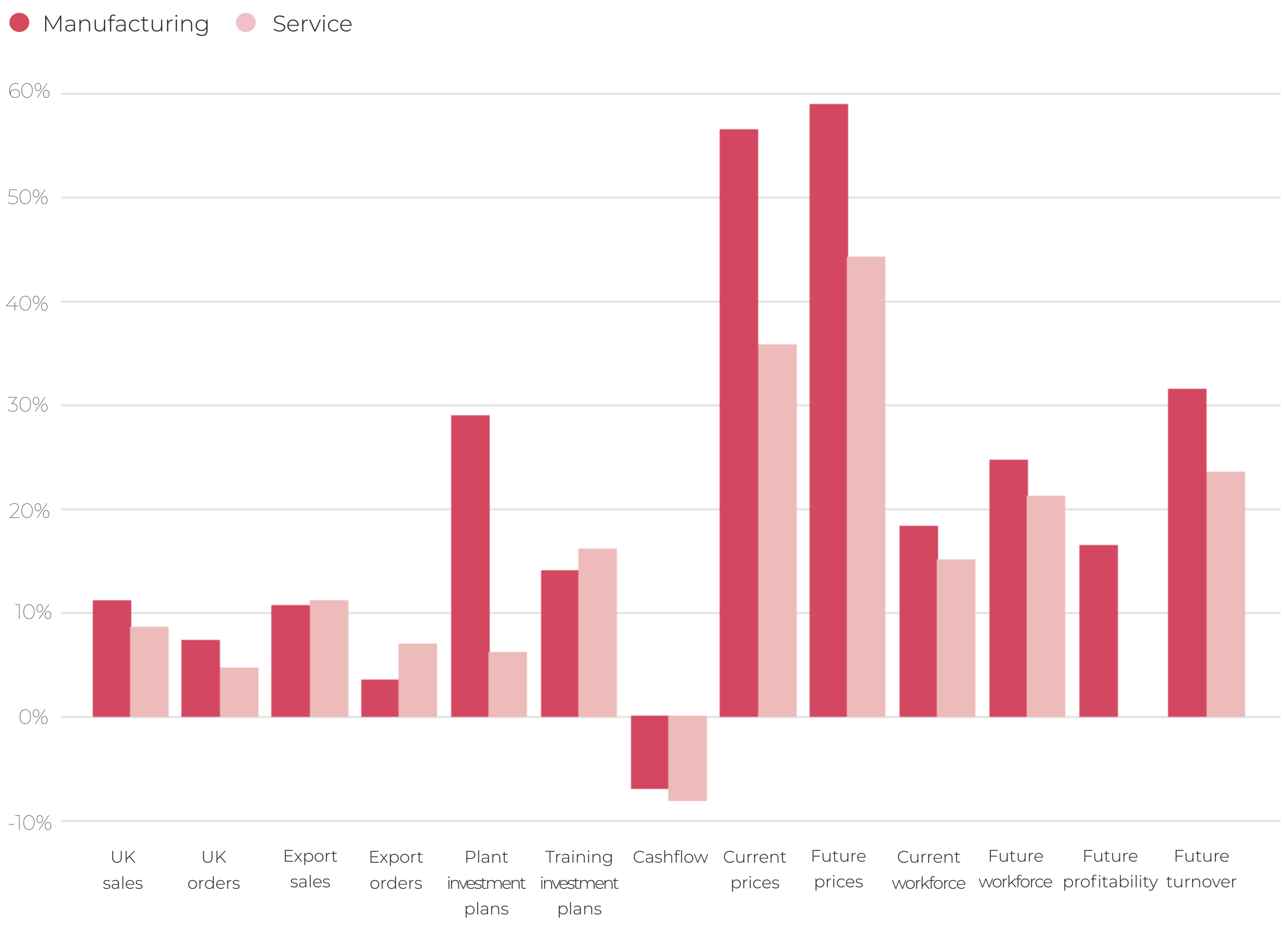
Methodology
Every quarter, we ask businesses about each of these key indicators. For current indicators (e.g. UK sales, cashflow), they are asked whether these have increased, decreased, or stayed consistent throughout the past three months. For the future indicators (e.g., future workforce, future turnover), they are asked whether they think these will increase, decrease, or stay consistent over the next three to 12 months. The values above are the 'balance' of the amount of 'increase(d)' and 'decrease(d)' answers we received. [1]

Key insights

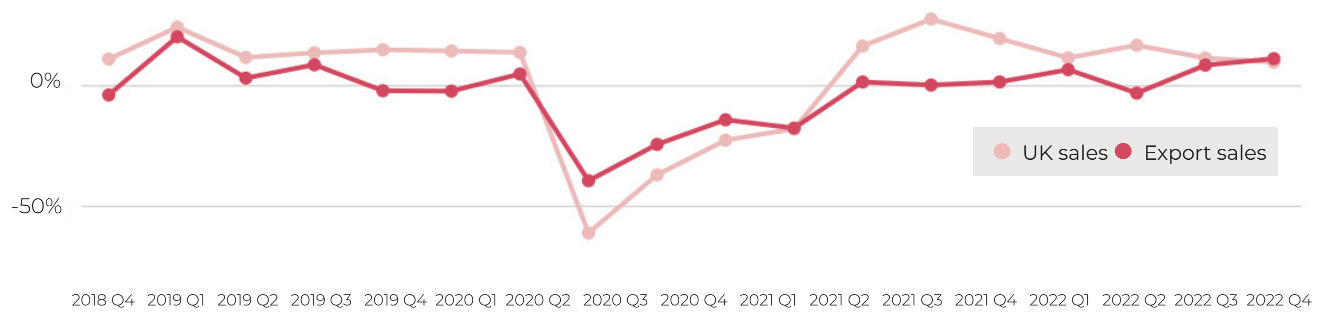
- After recovering slightly between Q2 and Q3, the overall picture of business conditions is more mixed in this quarter. There has been improvement in some areas, but a lack of business confidence remains. This is especially true in projections of future workforce needs, which have declined to 22.3% this quarter from 30.0% in Q3, and projections of future turnover which have declined to 25.9% from 29.8% in the same period.
- However, businesses are increasing investment in plant and training plans, a positive indicator of business health in difficult economic circumstances.
- There are some indications that the impacts of high inflation are easing slightly. Cashflow remains depressed at -7.7% but this represents a recovery from last quarter's result of -17.4%.
- Current prices are currently at 42.3%, considerably higher than last year when they stood at 25.5%, however also less than last quarter when they were 54.3%.
- All recruitment indicators are up on last year, with companies trying to recruit across all job categories and reporting increased recruitment challenges across all roles except for semi and unskilled positions. This suggests that the employment market remains generally tight.
- In this quarter, UK sales dropped to 9.5% from 11.2% in Q3 and 19.2% from Q4 2021. UK orders dropped to 5.6% from 6.3% Q3 and 22.1% in Q4 2021.
- Export sales have risen to 10.9% from 8.3% last quarter, and export orders have increased to 5.5%, from 3.1% last quarter.
- Businesses' top three concerns remain inflation (90.3%), energy prices (88.9%) and staff costs (74.4%), all of which have increased slightly since last quarter, approaching levels closer to those seen in Q2.
- Services firms are generally less optimistic about future business conditions than manufacturing firms.
- Services firms are considerably more impacted by staff costs and staff shortages, while manufacturing firms report higher concerns around issues such as exchange rates, business rates and taxation.

1 The number of businesses providing responses in the All Companies analysis is not necessarily equal to the sum of those providing responses for the two broad sectors of services and manufacturing, as not all respondents provide details of the industry in which they operate. Where data analysis involves more than two variables, and where three or less companies have provided information, data has been withdrawn from the survey in order to protect the anonymity of companies, and to provide accurate analysis.

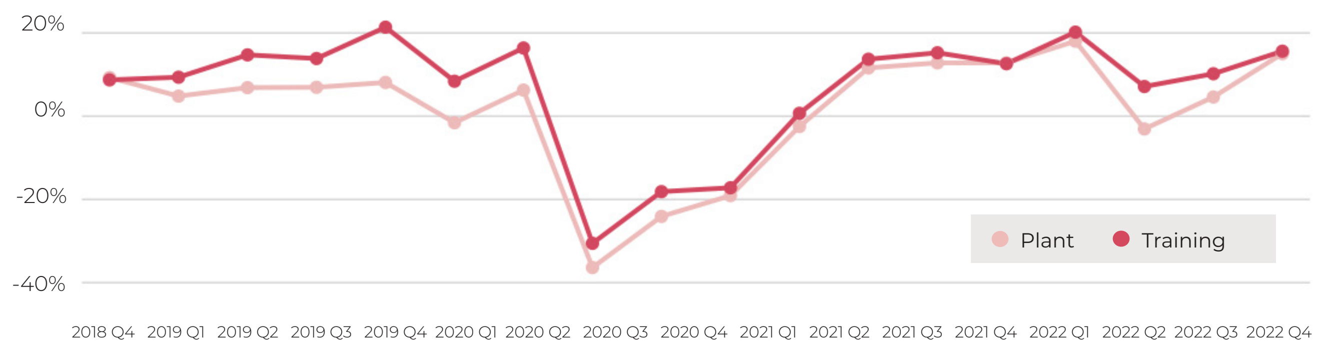
KEY INDICATORS



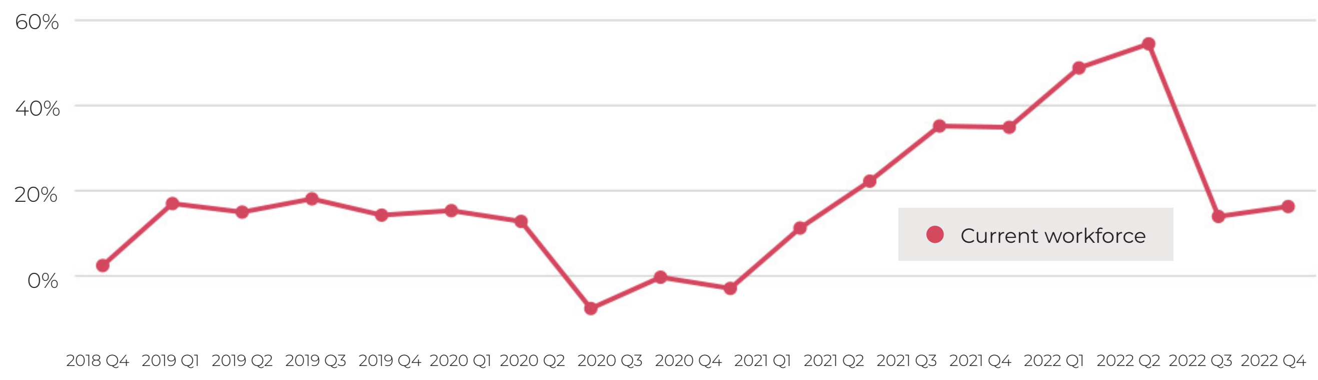
FIVE YEAR TREND - SALES



FIVE YEAR TREND - INVESTMENT



FIVE YEAR TREND - WORKFORCE



The impacts of extreme inflation are starting to ease, although price pressures continue to have the biggest impact across all sectors.

Recruitment
Businesses are not optimistic about future workforce needs. The current workforce indicator has increased by +2.3% to 16.1% this quarter, from 13.8% in Q3. The future workforce indicator has declined however by -7.7% to 22.3%, from 30.0% in the same timeframe. This suggests businesses are no longer preparing for workforce growth. Companies' current workforce and projections of the future workforce needs have decreased by -18.6% and -16.5% respectively since last year.

Within the quarter businesses have still been attempting to recruit across all job categories relative to both last quarter and last year. This suggests the tightness affecting the local labour market across 2022 has not yet eased. This is mirrored by the increased recruitment difficulties for clerical, professional and managerial, and skilled manual and technical roles relative to last quarter. Fewer companies are struggling to recruit semi and unskilled workers than in Q3.

After a relative slowdown in recruitment efforts for part time and permanent positions in the last quarter, growth in both areas has increased significantly. Companies trying to recruit part time staff have increased to 44.3% from 33.7% last quarter, and companies trying to recruit permanent staff have increased to 66.7%, from 58.9% last quarter.

The roles which have proved to have most depressed demand relative both to last quarter and last year are those in temporary positions. The lowest proportion of companies are trying to recruit for these positions at 33.5%, which has only risen from 31.0% last quarter and 29.6% last year. If we are to understand how the recession will impact those people in our region with the least secure employment it will be vital to monitor how this indicator changes next year.

Price pressures
The top three price pressures reported this quarter are labour costs (82.0%), utilities (81.0%), and fuel (69.6%). Among these most significant price pressures there are some interesting differences between services and manufacturing firms.

Amongst manufacturing firms, after seeing raw materials rise to the top of the list of pressures in Q3, utilities are once again the most significant pressure. 90.1% of all manufacturing companies responding reported increased price pressures in this area. Raw material costs are still the second most significant pressure for manufacturing firms at 86.1%.

For services firms, labour costs represent the most significant price pressure among respondents (81.4%). This is followed by utilities (77.1%). Concerns about price pressures are generally slightly lower among respondents in the services sector.

There are significant changes in price pressure concerns since last quarter, most notably around finance costs. This indicator has seen the largest quarterly increase of all indicators, rising from 41.4% in Q3 to 58.1% in Q4. Comparatively, utilities and fuel started from much higher points last quarter but saw smaller increases. Utilities rose from 79.3% in Q3 to 81.0% in Q4, while fuel rose from 67.6% in Q3 to 69.6% this quarter. Both remain in the top three price pressure concerns for businesses overall despite the government's significant levels of energy relief during the quarter.

CONCERNS KEY INDICATORS

INDICATOR	ALL COMPANIES	CHANGE ON LAST QUARTER	CHANGE ON LAST YEAR	MANUFACTURING	SERVICES
Crime	17.3	0.6 ▲	5.2 ▲	15.2	18.3
Congestion	22.7	6.4 ▲	1.4 ▲	25.8	21.2
Interest rates	68.0	20.2 ▲	27.4 ▲	56.3	73.2
Exchange rates	47.8	7.2 ▲	20.9 ▲	58.0	42.9
Business rates	53.9	6.1 ▲	20.8 ▲	55.1	53.3
Taxation	58.6	13.4 ▲	11.5 ▲	61.8	57.1
Competition	35.8	-2.3 ▼	5.2 ▲	28.4	39.2
Energy prices	88.9	0.6 ▲	8.3 ▲	87.7	89.4
Staff shortages	58.1	-0.3 ▼	5.6 ▲	46.5	63.3
Staff costs	74.4	1.3 ▲	14.3 ▲	56.9	82.6
Red tape	36.4	4.6 ▲	-9.9 ▼	33.8	37.6
Inflation	90.3	0.9 ▲	8.7 ▲	86.1	92.1

Businesses' worries are growing in all areas - but inflation and energy are still their top two concerns.

Perceptions
Perception scores reflect whether issues affecting members and their business activity are of greater concern now compared to last quarter. The scores above represent the proportion of respondents who indicated they were more concerned about these issues compared to last quarter.

Businesses' top three concerns are still inflation (90.3%), energy prices (88.9%), and staff costs (74.4%). Unlike in Q3 however, when concern dropped across those three areas, they have all risen in this quarter. Since Q3, concern about inflation has increased by +0.9%, concern about energy prices has risen by +0.6%, and concern about staff costs has risen by +1.3%. The consistency of these top three categories of concern for business across 2022 is significant.

In Q3, manufacturing and services firms were coalescing around the same main concerns. This trend has reversed in Q4, and gaps in concerns between services and manufacturing sectors around inflation, energy prices and staff costs have widened. Across these three indicators, manufacturing firms are registering similar or lower concerns compared to Q3. Services firms are more concerned across all three indicators than they were in the previous quarter.

Manufacturing firms are more concerned about energy prices (87.7%) than inflation (86.1%) with the reverse being true for services firms (inflation 92.1% and energy prices 89.4%), but these still represent the top two concerns for both sectors. The third and fourth concerns by sector are completely different, however. Manufacturing firms are more concerned about taxation (61.8%) and exchange rates (58.0%), while services firms are more concerned about staff costs (82.6%) and staff shortages (63.3%).

Concerns about staffing have dropped considerably among manufacturing firms this quarter, down to 56.9% from 72.7% in Q3 for staff costs and to 46.5% from 54.5% for staff shortages in the same timeframe. The reverse is true among services firms. 82.6% are concerned about staff costs this quarter compared to 73.1% in Q3, and 63.3% are currently concerned about staff shortages compared to 60.0% last quarter.

Interest rates and taxation have seen the most significant quarterly increases among all indicators. Data for Q3 was gathered before the mini budget, and this quarter's data collection period included the autumn statement, so these changes reflect the business communities' thoughts on the most significant fiscal policies of both Prime Minister Truss' and Prime Minister Sunak's administrations so far. Concerns about taxation among respondents across sectors is 58.6% this quarter, compared to 45.2% in Q3 and 47.1% last year. Concerns about interest rates stand at 68.0%, compared to 47.8% last quarter and 40.6% last year.

Other indicators which are registering levels of concern more than +5% higher than last quarter are exchange rates (47.8% in Q4, 40.6% in Q3), business rates (53.9% in Q4, 47.8% in Q3) and congestion (22.7% in Q4, 16.2% in Q3). The only indicators to have decreased in concern since last quarter are competition (35.8% in Q4, 38.1% in Q3), and staff shortages (58.1% in Q4, 58.4% in Q3). The only indicator to have decreased since last year is red tape (36.4% in Q4 2022, 46.3% in Q4 2021).

Energy usage
In Q4 2022, 88.9% of our respondents were concerned about energy prices, a slight increase of +0.6% from the previous quarter's result of 88.3% and an increase of +8.3% from the 80.6% recorded in Q4 2021. This reflects the implications of global prices which have continued to rise but may also reflect the uncertainty around the government's longer-term policy on commercial energy relief. The government is currently consulting on which vulnerable sectors will receive energy relief at the end of March 2023. By sector, 87.7% of manufacturing businesses and 89.4% of service businesses responding to the survey reported concerns about energy costs.

82.2% of businesses said they had taken action to try to reduce expenditure on energy compared to 73.0% in Q3, an increase of +9.2%.

Of those respondents:
- 84% were encouraging staff behaviour change to improve efficiency (an increase of +10% from 74% last quarter)
- 80% said they were reducing energy usage by turning off equipment (an increase of +4% from 76% last quarter)
- 41% were investing in new, more energy efficient equipment (an increase of +1% from 40% last quarter)
- 27% were investing in energy efficiency measures (e.g. insulation) (an increase of +7% from 20% last quarter)
- 22% were changing work patterns to reduce energy usage on site (an increase of +4% from 18% last quarter)
- 22% were switching tariff or provider (an increase of +2% from 20% last quarter)
- 19% were using local energy generation (e.g., solar panels)(an increase of +3% from 16% last quarter)

While short-term adaptation strategies are still common, the data suggests businesses are attempting to respond to high energy costs with longer term strategies for mitigation and energy efficiency. Changing working practices to reduce energy consumption and encouraging positive staff behaviours are still popular but compared to last quarter there has been a large increase in investment in energy efficiency measures to reduce consumption in the longer term. More firms are also reporting use of local energy generation techniques. This will be beneficial for the long-term energy security of the region. However, it is also possible that uncertainty around long-term energy prices and government policy may be limiting these investment plans, which require large initial outlays of capital.

Other responses further emphasise this need for both mitigation and adaption, with actions to reduce energy expenditure including:
- Energy reviews on existing contracts
- Car shares, encouraging more public transport use
- Encouraging remote working away from offices
- Investing in other energy efficiency systems including LED lights with movement sensors, new boilers, and new windows

The Chamber has used this insight and intelligence to inform our response to government's consultation on the commercial energy relief scheme available here.

We continue to welcome your feedback on this important issue for the region. To add your voice to that conversation please contact Thomas Lonsdale, knowledge and research executive, at **thomas.lonsdale@neechamber.co.uk**

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