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MANUFACTURING OUTLOOK

2024 QUARTER 4

With support from:

Scottish Engineering and Manufacturing NI

FOREWORD

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John Steinbeck's Pulitzer Prize winning novel The Grapes of Wrath, narrates the displacement of the Joad family as they are forced to give up their farm due to the challenges of the Great Depression and the environmental devastation of the Dust Bowl. In the family's struggles and financial challenges, Steinbeck captures the stark realities of economic hardship, as farmers once full of hope find themselves crushed by circumstances beyond their control. Their journey reflects how external economic forces can burden even the most resilient, hardworking people.

The Joads' saga captures the social and political dynamics of the time, but its sentiments speak to many farming families feeling battered by new fiscal burdens today. While most media coverage of the Autumn Statement has focused on British farmers, manufacturers too are grappling with external pressures and cost increases that threaten to pull them under. As this quarter's *Manufacturing Outlook* survey shows, family firms once buoyed by optimism, may find themselves struggling to stay afloat.

Though recruitment and investment intentions remain stable, the mood among companies has darkened markedly since the Chancellor's Autumn Statement. Confidence among UK manufacturers has dipped sharply to the lowest level in a year. That contrasts sharply with our previous Make UK/BDO survey when almost six in ten companies (58%) were looking ahead to a brighter future under a new government with its clear commitment to a modern, long-term, industrial strategy. Last quarter, optimism among manufacturers reached one of its highest levels in a decade. Overall conditions were beginning to improve, with output and order volumes gradually rebounding. The Budget put paid to that positivity.

The increase in payroll costs, in particular (employer's) National Insurance and the National Minimum Wage, coupled with capital gains and Inheritance Tax changes, as well as general pessimism about the state of the UK economy have all had an impact across the sector.

The budget was always going to involve tough choices. However, there is no escaping the fact that the surprising change in NICs thresholds, at a time of other cumulative increases in costs associated with the National Living Wage, Apprenticeship Levy and other policies is causing many to think twice about pay rises and investment in new equipment.

70% of manufacturers have already seen their cost base grow by a fifth this year. Almost one in ten (8%) saw them increase by up to a half. Now, almost nine in ten companies (86%) expect to see their payroll costs increase due to the Make Work Pay reforms, with almost half of companies (44%) saying this increase will be 'significant'. The cumulative effect looks likely to make investing in growth and the green transition much more difficult.

The Great Depression discussed in Steinbeck's novel was ended by President Franklin D. Roosevelt's 'New Deal'. The new UK Labour Government was elected with an offer of a new deal of its own. It promised to deliver supply-side reforms - deregulating planning, shouldering more of the risks to help invest in and grow British businesses, and providing the long-term policy and planning stability that manufacturers need to succeed - but, in return, business must increase investment in digitalisation and Net Zero, and respect the 'New Deal For Working People'. With domestic market demand relatively weak, and input prices being pushed up, there is an urgent need for Government to move forward measures to mitigate the negative growth manufacturing firms are now facing.

HEADLINES

Make UK's Q4 2024 *Manufacturing Outlook* report, in partnership with BDO, reports a return to stable growth for output and orders. However, growing signs of weakness in the domestic market continue to slow industrial activity as rising costs have impeded growth expectations. As a result of a mixed year, the manufacturing industry expected its gross value-added output to decline overall in 2024.

The latest balance of output reported at +20%, up from -2%, indicating that industry production expanded for a large share of businesses following the unexpected contraction last quarter. The last time output grew for this many manufacturers was the fourth quarter of 2023 which could suggest a return to regular growth during the festive periods. However, whether this rate of growth will continue into 2025 is far more difficult to predict given how the business cost environment will change next year. Manufacturers already predict that the balance of output will drop to +15% for the first quarter of 2025.

The sobering of future expectations could be a welcome change for the industry that has grown accustomed to overestimating its future performance. Albeit, as the expectations for production have been reduced, manufacturers expect their orders books to continue improving. In this latest chapter, the balance for total orders reported at +7%, unchanged from last quarter and a balance of +16% of manufacturers expect their orders to improve further in Q1 next year. However, it should be noted that these businesses have overestimated their order books for seven quarters in a row now.

is loosening. As it stands, it is unclear what the impact of higher employer's National Insurance contributions will be on recruitment plans. Investment intentions maintained a balance of +10%, adding to the view that economic stability and stronger policy incentives have supported productive investment decision-making.

The share of businesses raising prices is mixed for UK and export goods. The domestic market has reported a slight increase of the balance to +25%, indicating domestic inflationary pressures have accelerated. On the flip side, export price rises have reduced in balance to +21%, indicating easing inflationary pressures. However, margins have improved in both categories with a lower balance of manufacturers reporting contractions.

For the first three quarters of this year, confidence levels in both business conditions and economic conditions have consistently moved upward despite quarter-on-quarter turbulence. However, for the final quarter, confidence has dipped, suggesting a deterioration of expectations for the future, as is also reflected in manufacturers' output forecast. The standout change is that confidence in UK economic conditions has fallen at its sharpest rate since Q2 2020, declining by 1 point, or in other words 15% down, compared with the previous quarter. Despite this, confidence overall remains positive, but the contraction of this quarter may be a sign of more to come considering incoming rises in business costs in 2025.

INDICATOR	BALANCE	CHANGE	
Confidence	6.5	↓	Optimism slows for the first time since Q4 2023 but remains positive
Output	20%	↑	Output volumes rebound following dip
UK orders	0%	↑	Domestic market orders flat but improved
Export orders	10%	↓	Exports slow marginally
Employment	8%	↑	Employment contracts for the first time in four quarters
Investment	10%	↔	Investment intentions remain stable

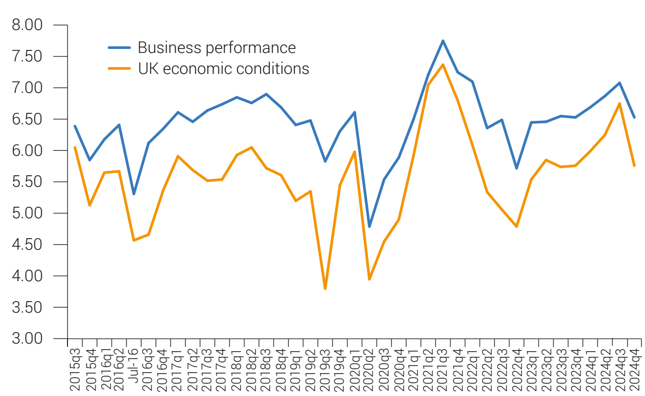
Source: Make UK Manufacturing Outlook Survey

The modest growth in total orders is primarily down to flourishing export orders that have supported the growth of businesses during turbulent times and reported a balance of +10% this quarter. However, the weakness in the domestic market has persisted now for six quarters in a row, reporting a balance of 0%, with limited signals of a recovery in 2025. The strength of any rebound will depend largely on several factors including the real impact of the Government's Autumn Budget, the movement of interest rates and inflation and the severity of returning President Trump's impact on global trade. The question now is for how long a strong export market can sustain the sector until the domestic market improves.

This quarter's employment and investment metrics are characterised by positive stability. Despite the former having indicated a decline in the third quarter, it was always within our expectations that recruitment would grow again, reporting a balance of +8%. Nevertheless, the number of live vacancies in the industry is returning to its long-run average indicating that the labour market

Manufacturer's optimism dips for the first time since Q4 2023.

Confidence in the next 12 months 1 = substantially worse, 10 = substantially better



Source: Make UK Manufacturing Outlook Survey

OUTPUT

Serving as somewhat of a saving grace for the sector's year average output performance, the output balance figure for the final quarter of the year brings about encouraging growth after a past year characterised by single-digit performances. Despite not quite reaching the heights of expectation that were set for this quarter's performance, performance in output hasn't been this positive since the same time last year.

The balance figure for order books was not particularly strong in the previous quarter, leading our analysis then to conclude that we would be less likely to see the kind of growth in output performance that we have, given there was little evidence of growing demand for the sector's products between Q3 and Q4. Nevertheless, those conclusions have been subverted by markedly impressive performance in the face of a pedestrian order performance throughout most of the year.

Despite this, the twin effects of sustained industrial confidence and the slow and steady loosening of monetary policy will have played their part. Over the past year, perhaps even two, there has been a degree of pent-up demand as the relative cost of capital remained elevated and was set against a backdrop of political uncertainty. Now, with those concerns mostly abated for the time being, activity has started gathering momentum once more.

This quarter's balance figure for output stands at +20%, a significant improvement over last quarter's -2%. Given the single-digit output performance we've observed throughout the year so far, this final quarter boost certainly helps to paint a prettier picture of the sector's year average, even though despite this last-minute boon it will remain insufficient to outperform 2023's output average, which saw double-digit output performance in three out of its four quarters.

The largest of companies, as proxied by turnover, have experienced the greatest uptick in output this quarter, with the middle market and small firms faring about equal.

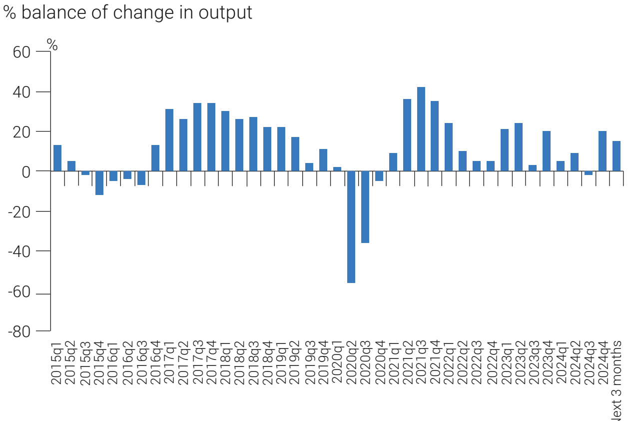
What is of particular note is the sector's next-quarter expectations. Followers of *Manufacturing Outlook* may have noted that the industry has exhibited demonstrable over-confidence in every quarter for just over a year, that is in the sense that the sector has expected output to grow in the future-3 month metric by significant degrees, although when the quarter comes to pass the exceptionally positive ambitions fail to materialise.

Now, with an expectation of a +15% balance figure for output in the first quarter of 2025, it would appear expectations have sobered, and perhaps become more grounded.

PAST THREE MONTHS	↑ 20%	NEXT THREE MONTHS	↓ 15%

Output volumes rebound following a contraction in the previous quarter

% balance of change in output



Source: Make UK Manufacturing Outlook Survey

Output summary

% balance of change

SECTOR	PAST 3 MONTHS	NEXT 3 MONTHS
Basic Metals*	–	–
Metal Products	20%	-9%
Mechanical	23%	34%
Electronics	10%	10%
Electrical	26%	13%
Rubber & Plastics	-18%	36%
TURNOVER		
£0-9m	9%	13%
£10-24m	10%	10%
£25m and over	21%	33%

Source: Make UK Manufacturing Outlook Survey
*insufficient sample this quarter

ORDERS

Following the sharp slowdown in order books in the third quarter of this year, there is a growing concern amongst manufacturers that demand will not return to anywhere near the levels seen in 2021. Furthermore, the return of President Trump presents the risk that seismic shifts in global trade flows could take place over the next year. The impact this could have on the UK is currently unknown, but the National Institute of Economic Research (NIESR) estimates that UK GDP could fall by 0.7% in 2025.

This would be problematic for the manufacturing sector which has been graced by robust demand from overseas, particularly from the European Union and North America regions. As UK market conditions have faced persistent uncertainty over the last twelve months, it is important for businesses to be able to rely on a diverse customer base to protect margins. This is challenging in the current policy climate following the reveal that several business taxes will increase, including employer's National Insurance and potentially Business Rates.

Total orders reported a +7 balance this quarter, a repeat of the result from Q3. This stable performance is largely related to a slight improvement in domestic market orders which was balanced by a slight slowdown in export orders. The latter remains the best performer of the two measures of pipelines.

The balance for total orders highlights an important relationship between domestic and international markets, and how critical supply chains are connected. In order to generate real material growth in the industry, it is imperative that both UK and export orders grow, rather than relying on contractions in one area to be offset by growth in another.

Additionally, manufacturers continue to overestimate their future total orders performance, reflecting the uncertain operating conditions many are working in. It is the seventh quarter in a row that manufacturers have underperformed on their expectations for new work. However, for the first time this year, manufacturers have forecast export orders to slow in the coming months suggesting businesses are factoring in geopolitical changes into their current expectations.

UK ORDERS	PAST THREE MONTHS	↑	0%	NEXT THREE MONTHS	↑	8%
EXPORT ORDERS	PAST THREE MONTHS	↓	10%	NEXT THREE MONTHS	↓	7%
TOTAL ORDERS	PAST THREE MONTHS	↔	7%	NEXT THREE MONTHS	↑	16%

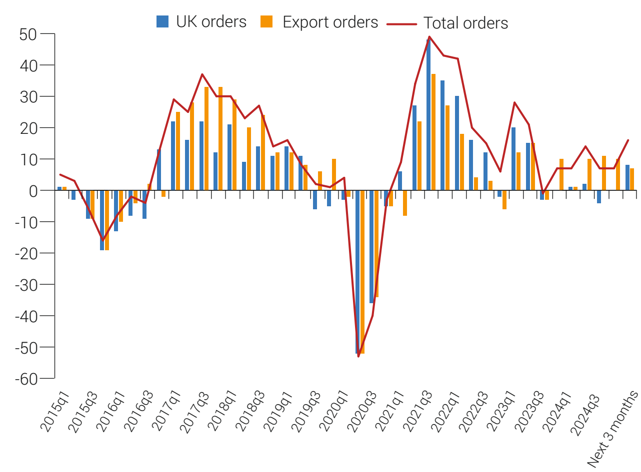
UK ORDERS

For the last six quarters in a row, the balances for UK orders have been concerningly poor. Albeit the flow of new work from domestic consumers is nowhere near the level of contractions experienced during the height of the pandemic, the lack of growth leaves something to be desired for a sector that is repeatedly being asked to invest more. The latest balance of 0% is an improvement on the previous quarter's -4%, though market conditions remain weak.

The results for the sub-sectoral breakdown for UK orders for some producers of intermediate goods are also worrying. The electronics subsector reported a balance of -30%, far more negative than the national average.

Domestic market performance flat as exports remain positive

% balance of change in orders



Source: Make UK Manufacturing Outlook Survey

Additionally, metal products also reported a negative balance. On a more positive note, rubber & plastics, electrical engineering and mechanical equipment all reported marginally positive balances which suggests industries such as construction may be experiencing growth.

EXPORT ORDERS

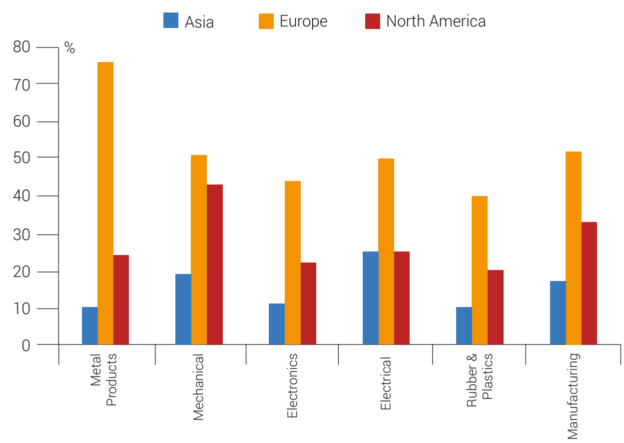
Exports continue to boost total orders for the manufacturing sector, reporting a balance of +10% for the quarter. However, this is a marginal slowdown from the +11% balance in the third quarter. The potential concern for the industry is that manufacturers expect exports to slow down further in the first quarter of next year, with only a +7% balance of manufacturers expecting growth in exports. This may reflect the impact that potential US tariffs could have on critical subsectors such as automotive.

Subsector-wise, of the manufacturing subsectors that are considered to be producers of intermediate goods, only the electronics industry reported a negative balance.

Finally, the survey finds that activity remains strong from the EU, with 52% of UK manufacturers reporting positive demand conditions from the region, slightly lower than last quarter's 55%. 76% of manufacturers in the metal products industry have reported strong demand conditions in the EU, whilst mechanical equipment is fairing quite well in both the EU and North America. The top three are completed by North America and Asia as expected.

Demand conditions for processed metal strong in Europe

% of companies reporting positive demand conditions by market



Source: Make UK Manufacturing Outlook Survey

Orders summary

% balance of change

	UK ORDERS		EXPORT ORDERS		TOTAL ORDERS	
SECTOR	PAST 3 MONTHS	NEXT 3 MONTHS	PAST 3 MONTHS	NEXT 3 MONTHS	PAST 3 MONTHS	NEXT 3 MONTHS
Basic Metals*	–	–	–	–	–	–
Metal Products	-2%	-5%	14%	-4%	11%	0%
Mechanical	8%	24%	8%	18%	15%	40%
Electronics	-30%	-10%	-14%	14%	-30%	0%
Electrical	5%	14%	21%	0%	9%	4%
Rubber & Plastics	9%	18%	0%	10%	36%	36%
TURNOVER						
£0-9m	-7%	4%	-6%	1%	1%	12%
£10-24m	-8%	2%	-9%	-4%	0%	11%
£25m and over	8%	25%	33%	29%	25%	26%

Source: Make UK Manufacturing Outlook Survey
*insufficient sample for export orders

EMPLOYMENT & INVESTMENT

The quarter's employment and investment metrics in the year's final *Manufacturing Outlook* are characterised by positive stability in both cases, but the implications of stability in investment intentions remain a disappointment. Employment has returned to growth following marginal negativity in the previous quarter, but the wider story lies in how aggregate vacancy figures in the sector continue to steadily cool back to their long-run average, indicating that the severity of the labour shortage for the sector is continuing to cool from the persistent labour market disruption that the pandemic brought about in 2022.

The employment balance figure this quarter stands at +8%. While an encouraging figure that isn't too expansionary, it reflects a change in pace from what we observed last quarter where it stood at -1%. Having been at similarly positive levels in the first and second quarters of the year as to what is reported in this edition, the third quarter negativity served as a blip that highlighted nervousness within the industry about cost control. A balance figure of -1 implies that, on aggregate, the sector's behaviour was tantamount to a hiring freeze. When we observe this and don't notice a significant drop in vacancies at the same time, we can surmise that there is not a proclivity to hire, at least in the short term, despite roles still being required by the sector in the medium term.

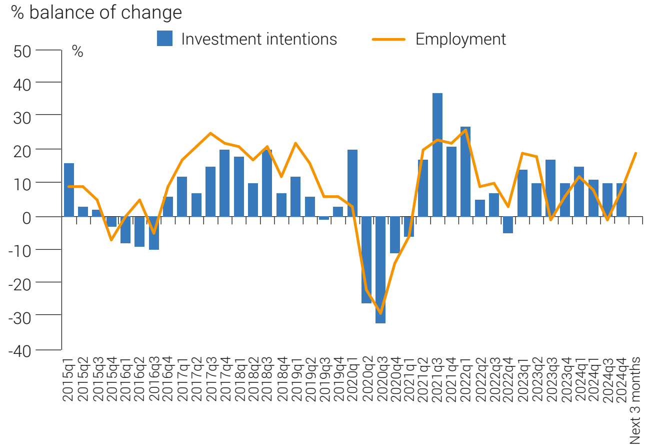
Looking forward, the sector has posted an expectation for an employment balance of +19% for the first quarter of next year.

While it is still a positive figure, and a double-digit one at that, there is still some nuanced negativity associated with that result.

The investment intentions balance has remained in this moderately positive position for five quarters now, deviating little from

Employment growth recovers as investment remains stable

% balance of change



Source: Make UK Manufacturing Outlook survey

EMPLOYMENT	PAST THREE MONTHS	↑	8%	NEXT THREE MONTHS	↑ 19%
INVESTMENT	NEXT TWELVE MONTHS	↔	10%		

Unlike other metrics in *Manufacturing Outlook*, the future-looking employment metric is typically representative of manufacturers' intention to hire, rather than their belief that they will render that employment growth in just three months. If anything, it more closely reflects the average severity of the labour shortage in the market over anything else.

As of October 2024, there were 56,000 live vacancies in the UK's manufacturing sector, a decrease from the 62,000 that were reported in the previous quarter's edition of this report. However, if we factor in ONS revisions in the intervening period, the revised figure for July is closer to 58,000, indicating a reduction of vacancies between the third and fourth quarter of the year by approximately 2,000. As a ratio, that is for every hundred jobs in the sector, 2.3 are vacant, down from 2.5 in last quarter's report, but down from 2.4 based on revised ONS data for the same time period.

The vacancy ratio data for the sector dates back to 2001, and the long-run average for the ratio, pre-pandemic (i.e. 2021), stands at approximately 1.8. Since the peak of 4.0 in late 2022, this ratio has been steadily reducing, albeit over a long period of time, lending strong evidence as to the easing of the severity of the industry's labour shortage. Nevertheless, it's important to acknowledge that this easing in the acute labour shortage exacerbated by the pandemic should not be conflated with the ongoing systemic challenge of skills shortages within the sector.

The investment intentions metric measures the sector's intentions to invest in the coming 12 months. This quarter's balance figure has come in at the same level as the third quarter of the year, at +10%. approximately +10%. Despite this, in this period the UK economy has seen a new government, the imposition of significant pro-business investment policies (e.g. full expensing) and the slow but steady reduction in the cost of capital as per the Bank's base rate. However, despite all these factors that would lead to the expectation of improved investment intentions, none have manifested, at least in the aggregate balance figure data as shown.

Employment and Investment summary

% balance of change

	EMPLOYMENT		INVESTMENT
SECTOR	**PAST THREE MONTHS**	**NEXT THREE MONTHS**	**NEXT TWELVE MONTHS**
Basic Metals*	–	–	–
Metal Products	4%	11%	14%
Mechanical	15%	31%	5%
Electronics	-20%	20%	0%
Electrical	9%	26%	22%
Rubber & Plastics	0%	9%	18%
TURNOVER			
£0-9m	11%	18%	11%
£10-24m	-11%	2%	-2%
£25m and over	13%	13%	28%

Source: Make UK Manufacturing Outlook Survey
*insufficient sample for export orders

PRICES & MARGINS

Across the first and second quarters of the year, the *Manufacturing Outlook* survey reported that, as per our price-setting behaviour metrics, inflation in manufacturers' supply side had been building. This was particularly alarming as it was set against a backdrop of steadily falling input price growth for the four quarters prior, coming down from the highest levels ever recorded in this publication's over thirty-year history. The peak came in the data in the first quarter of 2022, spurred on initially by a bounce back in demand following the pandemic, subsequently being sustained by the energy crisis that saw producer's input costs remain elevated.

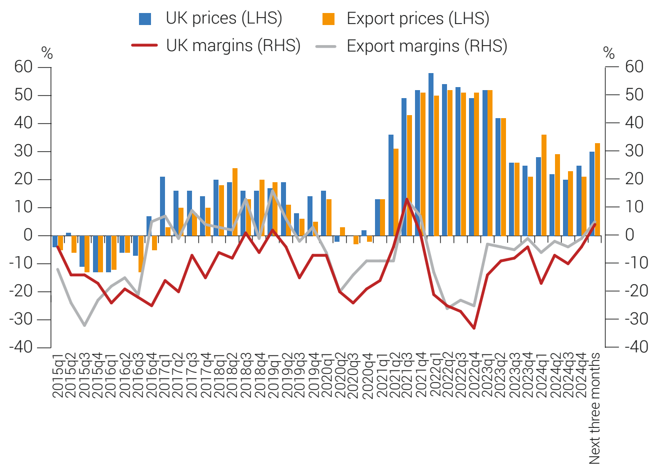
Since the first half of the year, namely in the third quarter, price-setting behaviour returned to a slower growth rate in line with the two-year trend. It's important to note that our data does not suggest prices are in absolute remission, rather they suggest that the rate of growth of prices is slowing. This quarter's data sees an increase in the balance figure for domestic prices compared to last, indicating a greater proportion of manufacturers have raised their prices this quarter. However, for export prices, the rate of cooling has continued, albeit more slowly than hoped.

The balance figures of UK prices and export prices are +25% and +21% respectively, an increase in UK prices by 5 percentage points and a decrease in Export prices by 2 percentage points relative to last quarter. While these aren't massive swings, they come at a time when the wider trading environment would suggest that prices should be cooling much faster, as is the trajectory of the Bank of England which has been steadily reducing the base rate, currently standing at 4.75%, throughout the year. These results could slow down the pace of base rate reductions in 2025.

balance figures for margins do turn positive in the next quarter, this would be the first time they have done so since the tail end of 2021. Alas, in recent quarters it has been all too common for the sector to suggest that margins will just tip into positivity in the coming quarter, but when the quarter comes the reality falls just short time and again.

Domestic inflation accelerates as business costs increase

% balance of change



Source: Make UK Manufacturing Outlook Survey

UK PRICES	PAST THREE MONTHS	↑	25%	NEXT THREE MONTHS	↑	30%
EXPORT PRICES	PAST THREE MONTHS	↓	21%	NEXT THREE MONTHS	↑	33%
UK MARGINS	PAST THREE MONTHS	↑	-4%	NEXT THREE MONTHS	↑	4%
EXPORT MARGINS	PAST THREE MONTHS	↑	-4%	NEXT THREE MONTHS	↑	5%

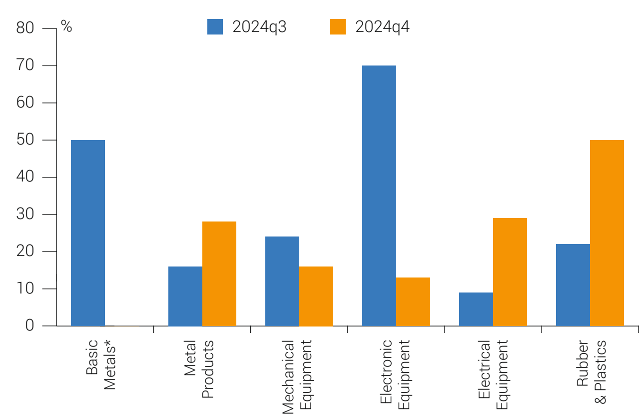
However, the data suggests that the elevated price rises have enabled an improvement in margins, despite them remaining in marginal negativity. The UK margins and export margins balance figures reported at -4% and -1% respectively. A 6 percentage point increase in the case of UK margins and a 3 percent increase in the case of Export margins.

There are expectations from the sector for growth in both prices and margins by the first quarter of the year, with bittersweet implications. In the first instance, manufacturers expect the UK prices balance figure to rise by 5 percentage points to +30%, and by 12 points to +33% for export prices. If price-setting behaviour does increase when we receive the data in the first quarter of next year, that would represent two consecutive quarters of acceleration in domestic price increases, indicating that the inflationary beast hasn't quite been put to bed, likely having bearish implications for monetary policy decisions in the first half of next year.

The 'sweet' is seen in the margins, as the sector expects margins to turn to positivity in the first quarter of 2025, with balances of +4% and +5% for UK margins and export margins respectively. If

Export prices for materials and construction rise

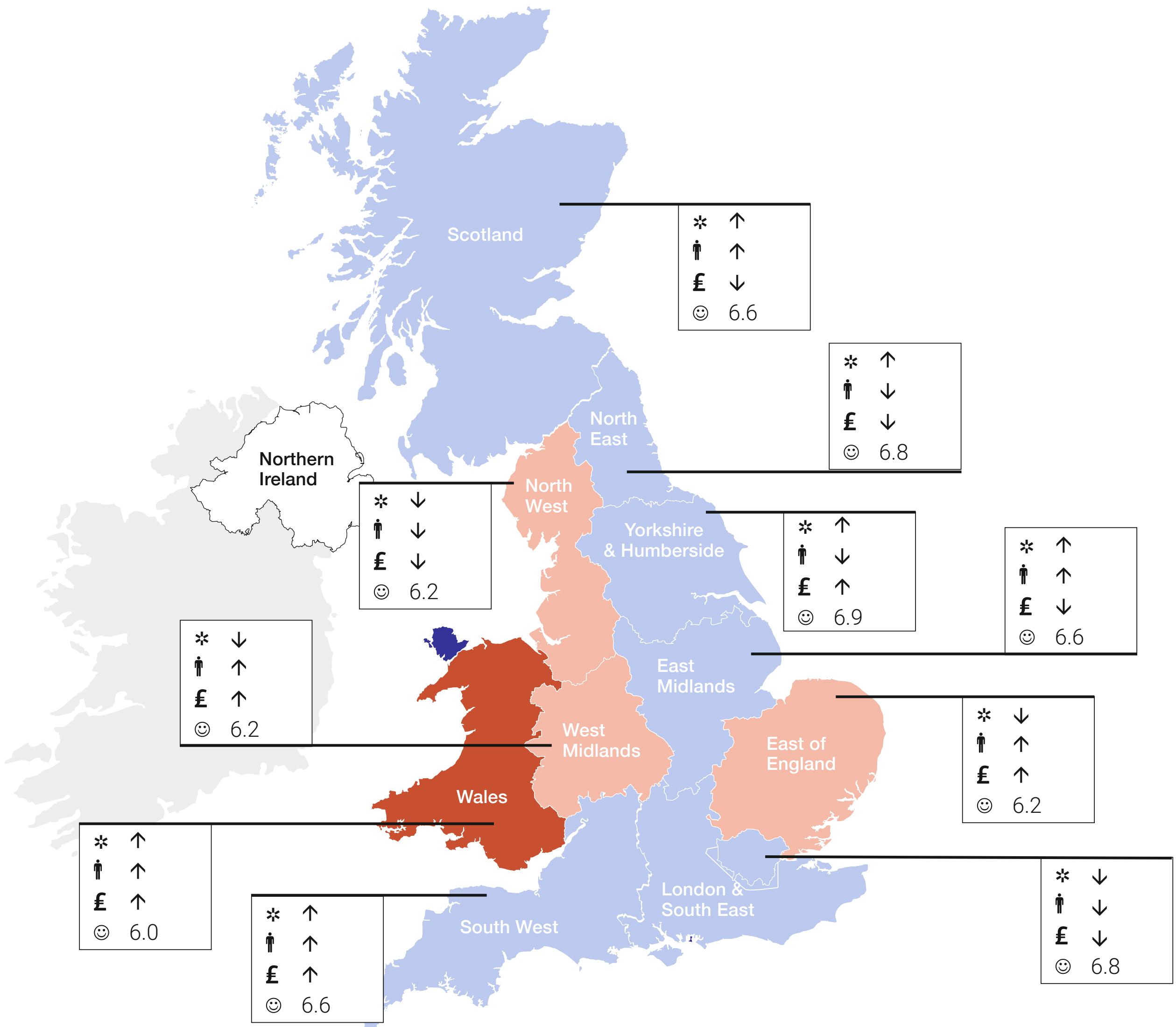
% balance of change in export prices in the past three months



Source: Make UK Manufacturing Outlook Survey
* insufficient sample for Q4

NATIONAL & REGIONAL

Since early 2021, manufacturers have continued to demonstrate resilience in their optimistic view of business conditions. Of the last seven quarters, business confidence has improved six times highlighting the sector's unshakable belief that things will be better in the future. This is unsurprising given the relative



KEY:

↑/↓ INCREASE/DECREASE ON PREVIOUS QUARTER
✲ OUTPUT
🕴 EMPLOYMENT
£ INVESTMENT
☺ BUSINESS CONFIDENCE

The map is coloured according to the business confidence levels difference from average UK business confidence

HIGH CONFIDENCE

LOW CONFIDENCE

Source: Make UK Manufacturing Outlook Survey

business conditions most companies are operating in today are far better than those experienced over the last few years, such as trading uncertainty, supply-chain disruption and astronomically high energy prices.

However, this persistent climb in optimism has unexpectedly reversed its trajectory for both business and economic conditions. This is an indication that expectations for the future could fall, which will undoubtedly impact investment given confidence is regularly highlighted as the number one factor in capital expenditure decision-making. Nevertheless, there is a possibility that investment could move in a different direction as the rising cost of employment could instigate a push towards greater automation and digitalisation. The likelihood of this happening will depend largely on the ambition and quality of implementation of the government's upcoming industrial strategy, *Invest 2035*.

Headline business confidence reported at 6.5, which is down from last quarter's level of 7.1.

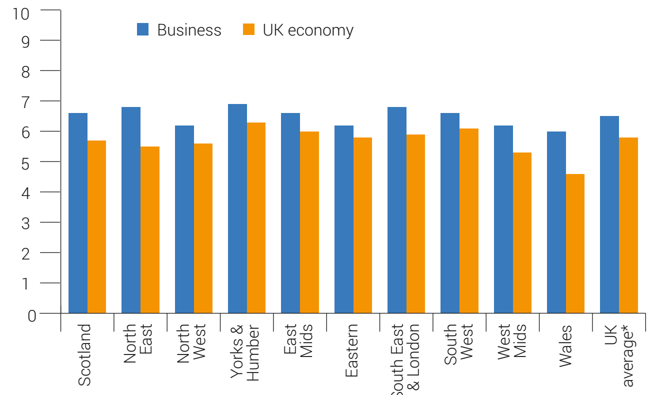
All regions and nations reported above the '5' inflexion point that separates positive and negative confidence. This indicates that on average, most manufacturers are relatively in line in terms of their optimism levels for the next 12 months. Across the nation, excluding Northern Ireland, seven regions or nations have reported a decrease in their business confidence.

Amongst the English regions, the largest improvement in business confidence was reported by the North East, which increased by 0.6 points to 6.8. However, the most confident region in the UK is Yorkshire & the Humber reporting a business confidence level of 6.9. The only other regions to report improved business confidence levels include the South West (up by 0.7) and East Midlands (0.2).

All other English regions reported declines in business confidence, the biggest contraction was reported by the South East & London region (down 1.2). This is followed by the North West which declined by 0.9. Outside of the English regions, however, Welsh business confidence dropped by a more significant 1.6 points. As a result, Wales also has relatively the lowest business confidence in the UK. It should be noted that despite the direction of change being primarily down, manufacturers generally remain optimistic about their own business conditions.

All UK regions and nations report positive business confidence

Confidence in the next 12 months 1 = substantially worse, 10 = substantially better



* Average =/= component parts due to instances of undeclared regionality

Source: Make UK Manufacturing Outlook Survey.

UK ECONOMY CONFIDENCE

Manufacturers' confidence in the overall UK economy reported at 5.8, this is a one-point decline from the previous quarter's level (reporting at 6.8). Relatively speaking, the sharpness of this negative change is unexpectedly the largest since the second quarter of 2020.

During the first half of the year, many businesses raised their expectations for the UK economy believing that growth would return. Many international forecasting bodies such as the IMF had raised their prospects for the economy due to tailwinds that put the UK in a competitively advantageous position. However, a rise in political uncertainty and the growing risks of higher business costs have likely spoiled manufacturers' hopes of achieving real growth. As a result, expectations for the UK economy appear to have declined at their fastest rate since the pandemic era.

Fortunately, the average confidence for the UK economy remains positive (above 5) but the impact of new legislations to employment rights and increased cost of employing staff could potentially hit investment and R&D activity.

Regional summary

% balance of change

	OUTPUT		TOTAL ORDERS		EMPLOYMENT	
REGION	PAST 3 MONTHS	NEXT 3 MONTHS	PAST 3 MONTHS	NEXT 3 MONTHS	PAST 3 MONTHS	NEXT 3 MONTHS
Scotland	10	17	-3	10	14	26
North East*	60	50	60	60	10	20
North West	-6	6	22	6	-11	17
Yorks & Humber*	47	53	27	67	0	20
East Mids	12	0	-6	-12	0	0
Eastern	5	15	0	10	-14	-5
South East & London	7	26	7	31	2	7
South West	13	0	7	0	7	-20
West Mids	0	5	0	33	14	29
Wales	86	-29	29	-29	43	-29

Source: Make UK Manufacturing Outlook Survey

* Sample size relatively low for these regions

ECONOMIC ENVIRONMENT

Halfway into the new Government's first year in power, the manufacturing sector has experienced a plethora of opportunities and challenges. The "mission" for growth is now firmly on the minds of every civil servant who are tirelessly formulating the right level of support for industry to restart the flow of investment whilst resetting the public purse to ensure the nation's financial health. However, this has put the Government in an inconvenient position as promises of long-term strategies to install confidence have been overshadowed by an increase in the business tax burden, driven by short-term needs.

Manufacturers remain resilient in the face of novel challenges, though the change in employer's National Insurance contributions (NICs) and adjustments to Capital Gains Tax and Inheritance Tax will be a difficult pill to swallow following several years of disruption and higher costs. There is hope that the background work ongoing for the industrial strategy, *Invest 2035*, will rebalance the scale in industry's favour.

The most recent string of GDP figures published by the Office of National Statistics (ONS) already suggests the UK economy had a difficult third quarter. Growth between August and September reported at -0.1%, driven by a decline in production and manufacturing whilst services and construction reported no growth. Across the quarter the UK's performance was flat following the immediate aftermath of the general election, suggesting the first change in government in 14 years did little to set ablaze consumer confidence. According to Oxford Economics, it is likely the UK will now achieve less than 1% growth overall in 2024 if the current trajectory continues. However, alternative bodies like the IMF are slightly more optimistic expecting the UK to grow by 1.4% this year.

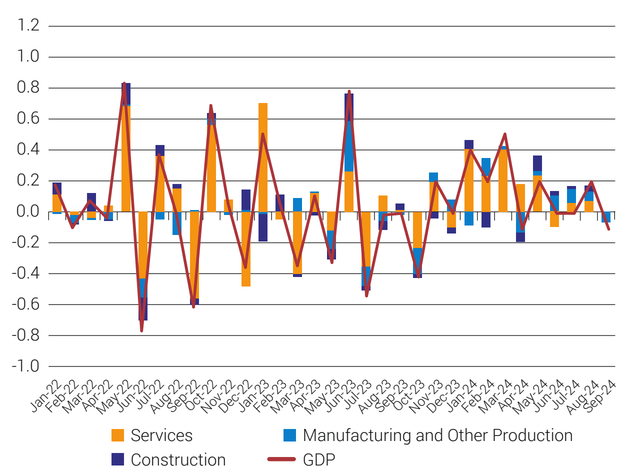
The positive note is that manufacturing has not been the main contributor to the poor GDP performances lately. Within the production sector includes the generation of electricity, gas, steam and air conditioning which contracted by 2.7% in the third quarter, whilst manufacturing grew overall by 0.2%. However, this is still a concerningly low level of growth for the industry. Our previous economic outlook indicated this was primarily down to a slowdown in domestic market orders that have negatively impacted the industry's prospects.

International forecasts highlight that two major economic nations, Germany and Japan, expect to contract overall in 2024, though likely for different reasons. Germany has faced major issues due to high energy costs negatively impacting the country's largest industrial sectors, such as automotive and capital equipment producers. Japan is experiencing persistent positive inflation for the first time in decades which has negatively impacted consumer confidence. The US continues to expect strong growth, though it is unclear currently how returning President Trump's tariffs will affect US businesses.

Despite the incoming rise in business costs, particularly due to the planned changes in employer's NICs and legislative changes in employment rights, manufacturers still hope to see interest rates fall in

GDP fell in September due to a slowdown in manufacturing

Contributions to monthly GDP, percentage points, January 2022 to September 2024



Source: ONS

2025 for balance. Higher rates have been highlighted as a significant barrier to investment since they were raised from their historically low levels in the last decade. However, the rate of consumer inflation, which the central bank targets at 2%, remains persistently higher than expected. The latest report of 2.3% inflation was unwelcome news to many consumers who are hoping for stronger signals of rate cuts in the next year, though the rise in prices is primarily down to Ofgem raising the price cap for energy bills. Producer inflation is on a downward trend, and reported a -2.3% decline for inputs in the ONS latest survey. Factory gate prices reported at 0.1%, which whilst small indicates manufacturers are raising prices to recoup lost margins.

The overall economic environment is a mixed one for manufacturers. The change in government presents an opportunity to renew hope across industries though not enough detail on strategies has been revealed to move the needle on investment decisions. Nevertheless, following the investment summit, which saw the CEO of Microsoft named as Chair of the Industrial Strategy Council (ISC), sends a strong message to the global economy about how the UK expects to evolve over the next decade. The future is inevitably going to centre on AI and the mass adoption of digital and automation technologies to close the productivity gap. Manufacturers will have a role to play in this transition but those businesses that fail to move in line with this progress may find themselves falling behind.

UK Economic Forecasts

% change except where stated

	2023	2024	2025
TRADING ENVIRONMENT			
Exchange rate (€/£)	1.15	1.2	1.2
Exchange rate ($/£)	1.27	1.26	1.27
Exports	-0.3	-1.9	1.9
Imports	-1.3	2.5	2.2
Current account (% GDP)	-2.6	-3.1	-2.8
OUTPUT			
Manufacturing	1.1	-0.2	0.7
GDP	0.3	0.9	1.4
COSTS AND PRICES			
Average earnings	7.4	5.0	3.5
Oil price (Brent Oil $/bl)	82	80	73
EMPLOYMENT			
Manufacturing (000s)	2,603	2,579	2,552
Rest of economy (000s)	36,689	37,094	37,338
Unemployment rate (%)	4.1	4.3	4.4

Source: Oxford Economics and Make UK

International Economic Forecasts

% change

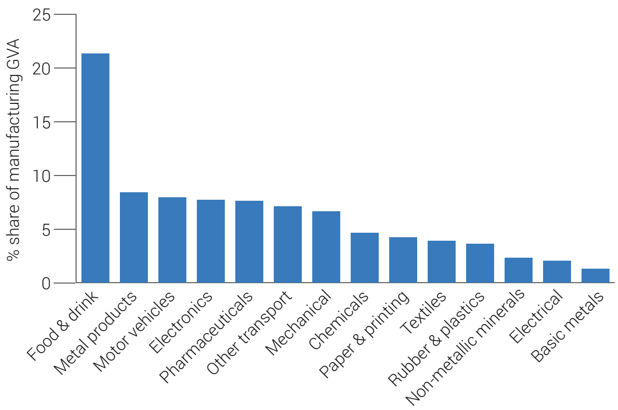
	GDP			INFLATION		
	2023	2024	2025	2023	2024	2025
US	2.5	2.8	2.6	4.1	2.9	2.4
Eurozone	0.5	0.8	1.2	1.9	2.3	1.6
France	0.9	1.1	0.8	4.9	2.0	1.3
Germany	-0.2	-0.1	0.6	5.9	2.2	1.2
Japan	2.0	-0.1	1.2	3.3	2.5	1.5
China	5.2	4.8	4.4	0.2	0.2	1.3
India	7.0	6.8	6.8	5.7	4.7	4.5
World (US$ weighted)	2.7	2.7	2.8	6.0	4.5	3.5

Source: Oxford Economics

SECTOR FORECASTING 2024 Q4

Q4 2024 manufacturing sector composition by GVA (% share)

Subsector share of Manufacturing Gross Value Added



Source: Oxford Economics

FOOD & DRINK

The **Food & Drink** subsector continues to dominate UK manufacturing, accounting for 21.3% of the total GVA, a figure increased by 0.1% from the previous quarter. Forecasts for output in 2024 remain robust at 2.9%, indicating that the subsector is maintaining its growth trajectory despite the gloomier outlook as illustrated by the manufacturing sector average growth expectation of -0.2% in the same period. Growth in 2025 is expected to be a more moderate 0.8%. Employment, however, presents a mixed picture. While relatively stable, it is forecast to decline slightly by -0.2% in 2024, followed by a sharper drop of -1.5% in 2025.

ELECTRONICS

The **Electronics** subsector is the only subsector that is forecast a perfectly flat growth expectation for 2024. Output growth in 2024 is forecast to remain at 0.0%, although relative to the average, this forecast is slightly ahead of the pack. For 2025, the subsector is expected to regain some momentum with a modest growth forecast of 0.9%. On the employment front, the subsector demonstrates consistency across output and employment, with a slight increase of 0.1% projected for 2024. However, this is subsequently expected to be followed by a decline of -1.7% in 2025.

BASIC METALS AND METAL PRODUCTS

The **Basic Metals** subsector remains under significant pressure, reflecting the disruption in global commodity markets, particularly that of demand cycles and geographic sourcing decisions. Output is forecast to decline by -2.2% in 2024. This contraction is set to continue in 2025, with output expected to fall sharply by -11.5%. Employment in the subsector mirrors this bleak outlook, with workforce reductions of -1.5% anticipated in 2024 and a dramatic -8.3% decline forecast for 2025. These figures highlight the subsector's vulnerability to macroeconomic headwinds and higher domestic marginal costs of production.

The **Fabricated Metals** subsector is now almost inverse to the Basic Metals subsector, despite their inherent linkage. The output forecast for 2024 is significantly above the sector average, with growth in output of 7% forecast, an improvement over last quarter's forecast. 2025's expectations are more tepid, yet still above the sector average, with 0.9% growth expected next year. Employment forecasts for the subsector remain positive but modest, with growth in headcount of 0.9% and 0.1% forecast across 2024 and 2025 respectively.

MECHANICAL EQUIPMENT

The **Mechanical Equipment** subsector, a key indicator of domestic capital investment trends, faced a contractionary year as investment appetite was insufficient to see the sector grow. Output is forecast to decline by -4.6%, reflecting the aforementioned subdued investment climate. However, the outlook for 2025 is improved, with output growth of 3.3% anticipated. Employment is set to decline by -3.0% in 2024, followed by a smaller drop of -2.0% in 2025. These figures suggest that the subsector expects to grow in 2025 but with a leaner workforce on aggregate.

TEXTILES

The **Textiles** subsector has endured negative growth projections for over three years now, with the final forecast for 2024 setting an expectation for an output contraction of -11.6% this year, the second most negative output forecast out of all subsectors this quarter. This outlook for the subsector's 2024 performance has worsened relative to last quarter where it was thought at the time the sector would shrink by -8% at the time. 2025's forecast expects this contraction to soften, to -2.3%. Employment is also expected to decline across both years, by -10.5% in 2024 and by a further -4.7% in 2025. This significant reduction in headcount in 2024 leaves the subsector as the most contracting this year in terms of employment.

PAPER & PRINTING

The **Paper & Printing** subsector has seen its output forecast for 2024 remain roundly consistent with the previous quarter's expectations. The latest expectation is that the subsector will contract in output by -1.7% in 2024, an ever so slight improvement on last quarter's forecast, but see little to no change in 2025 with growth of 0.2% forecast in the following year. The good news for the subsector and its employees is that previously forecast high levels of employment reduction have subsided from double digits to a new -3.2%, but this figure is expected to be sustained across about 2024 and 2025.

ELECTRICAL EQUIPMENT

The **Electrical Equipment** subsector has seen its forecast for output progressively worsen throughout the year. Now, in the final quarter, the forecast for output has settled at a contraction of -6.2% for the sector. Little solace or recovery of this loss of output is expected in 2025, with a flat forecast for growth of -0.2% expected next year. Conversely, employment in the subsector is expected to grow across both years, with an expansion of 3.3% in 2024, and a further 0.9% in 2025.

NON-METALLIC MINERALS

The **Non-Metallic Minerals** subsector is known as the subsector that supplies the construction market, providing products such as bricks, mortar, glass and other related products. This ties the subsector to the performance and appetite of the construction sector in the UK, which continues to see suppressed activity levels relative to expectations. In this quarter as it was last quarter, this subsector's output forecast for 2024 is the most contractionary out of all manufacturing subsectors and has been revised downward relative to the previous quarter. The final forecast suggests that output will decline in 2024 by -11.9%. 2025 performance expectations, albeit positive, don't hold much promise to claw back lost ground, with only growth of 2.1% expected. Somewhat surprisingly, Employment is set to grow, by 3.2% in 2024 and by 0.1% in 2025.

PHARMACEUTICALS

The **Pharmaceuticals** subsector, having enjoyed sustained growth during the pandemic, is now entering a period of normalisation. Output in 2024 is expected to contract slightly by -0.5%, reflecting a return to typical demand levels. In 2025, the subsector is forecast to recover with growth of 1.9%. Employment is projected to decline by 3.2% in 2024 but return to modest growth of 0.2% in 2025. These figures suggest that while the subsector remains a vital contributor to both the sector and the wider economy, it is settling back into a post-pandemic market reality.

CHEMICALS

The **Chemicals** subsector has received an upward revision to its 2024 output forecast in comparison to last. Previous expectations were for the subsector's growth prospects to contract by about 3%, but the latest forecasting suggests that this subsector will contract in output by a lesser -2.1% this year. 2025's forecast sees a flat expectation emerge, with a contraction of only -0.17% expected next year. Employment in the subsector is projected to remain roundly flat when averaging the coming two years. 2024's forecast sees the sector grow in headcount by 1.7%, but return to contractionary territory with a figure of -2.1% in 2025.

RUBBER & PLASTICS

The **Rubber & Plastics** subsector declined by -7.8% in output in 2023. Although negative, the subsector has not seen its forecast for output this year fall any further, despite already being moderately negative at -6.3%. Growth is forecast to return next year, however not to a commensurate degree. Output is forecast to grow by 2.4% in 2025. Employment is forecast to decline by -1.5% this year and grow by 1.3% in 2025.

MOTOR VEHICLES (AUTOMOTIVE)

As was the case last quarter, the **Motor Vehicles** subsector is the only one to be in receipt of a double-digit output growth forecast for 2024. A large driver of this growth is the remnants of 'catch-up' activity following a multi-year production suppression arising from the pandemic and subsequent market disruptions. So, even though the forecast for growth in 2024 stands at a whopping +10%, that isn't expected to continue into 2025, where in fact a slight contraction in output of -1.1% is forecast. Employment in the subsector will see a significant decline across this year and less so in the next, with a contraction in headcount across the subsector of -5.1% in 2024 and -2.7% in 2025.

OTHER TRANSPORT

The **Other Transport** subsector which is comprised of aerospace, defence, shipping and rail industries, is set to post strong growth for the second year in a row, which becomes clear now in the final quarter of the year. Having grown in output by 6.8% in 2023, the latest forecast for this year suggests it will grow in output by a further 6%, which is an improvement in the growth forecast by a whole percentage point in only the space of one quarter. Nevertheless, this sustained high growth is not to be seen into next year as a more modest 2.8% output growth is forecast for 2025, which is still twice the scale of the sector average for 2025. Employment is forecast to grow this year, by 2.6%, but decline by a modest -0.6% in 2025.

Sector growth rates and forecasts

% change

	OUTPUT			EMPLOYMENT		
	2023	2024	2025	2023	2024	2025
Basic metals	5.2	-2.2	-11.5	-8.5	-1.5	-8.3
Metal products	3.5	7.0	0.9	8.1	0.9	0.1
Mechanical	-3.9	-4.6	3.3	-1.2	-3.0	-2.0
Electronics	4.3	0.0	0.9	2.6	0.1	-1.7
Electrical	0.1	-6.2	-0.2	-0.1	3.3	0.9
Motor vehicles	18.9	10.0	-1.1	0.6	-5.1	-2.7
Other transport	6.8	6.0	2.8	4.0	2.6	-0.6
Food & drink	-0.2	2.9	0.8	-1.7	-0.2	-1.5
Chemicals	-9.1	-2.1	-0.17	-6.7	1.7	-2.1
Pharmaceuticals	9.9	-0.5	1.9	2.9	-3.2	0.2
Rubber and plastics	-7.8	-6.3	2.4	-4.8	-1.5	1.3
Non-metallic minerals	-10.2	-11.9	2.1	-2.5	3.2	0.1
Paper and printing	-5.4	-1.7	0.2	-3.1	-3.2	-3.2
Textiles	-8.7	-11.6	-2.3	-10.6	-10.5	-4.7
Manufacturing	**1.1**	**-0.2**	**0.7**	**-0.9**	**-1.1**	**-1.1**

Source: Oxford Economics

Source: Oxford Economics

BDO VIEWPOINT

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EU CARBON BORDER ADJUSTMENT MECHANISM (CBAM) - TAXING FUTURE CARBON EMISSIONS

In order to remain competitive and maintain margins, many manufacturers have historically sourced cheaper raw materials, parts, components and also finished goods from overseas where production and labour costs are cheaper.

Whilst this can lower the cost of manufacturing and procurement, it often comes with higher carbon emissions which is becoming an increasing environmental concern as the ESG agenda heats up.

The UK and EU governments' growing focus on the need to meet their net zero targets for carbon emissions domestically could, paradoxically, be adding to the problem. Importing cheaper goods – often from countries that have not imposed tougher emissions standards – could, in turn, result in exporting carbon emissions.

'Carbon leakage' caused by importing high-emission products is a well-established problem and needs to be addressed if net zero targets are to be achieved.

WHAT IS CBAM?

The Carbon Border Adjustment Mechanism is a piece of EU legislation which affects UK exporters. From 1 October 2023, the EU introduced rules to ensure that CO2 emissions created in the manufacture of goods imported into the EU are recorded and reported.

Although reporting requirements for the CBAM have been implemented, it won't be until 2026 that businesses will have direct costs under the scheme. Businesses will then have to purchase certificates under the EU Emissions Trading Scheme to cover the imports of such goods, effectively increasing their price and taxing the related emissions.

UK businesses exporting to the EU will be affected first, with the administrative reporting burden starting this year and either needing to provide this data to the EU importer or doing so themselves if they import directly. This will include appointing an EU-based reporting agent if the UK business has no establishment in the EU.

UK CBAM PROPOSALS

Following a consultation this year by the UK government to address future carbon leakage, they announced their approach to CBAM late October. UK CBAM will be introduced in January 2027, several years after the EU's regime and a year after the EU regime creates costs for importers.

UK CBAM will cover the aluminium, cement, fertilizer, hydrogen and iron and steel industries. The ceramics and glass industry will be included at a later point in time.

The regime will cover both direct (manufacturing emissions) and indirect emissions (those relating to the amount of electricity consumed in the production process) of CO2, with Perfluorocarbon PFS for the aluminium industry and NO2 Nitrous Oxide for the fertilizer industry also included.

CBAM rates for each covered good will be set and updated quarterly. Actual emissions will need to be reported but there will be a facility to use default values if they are not available to importers. UK importers will pay the difference between the UK set carbon price minus any carbon price paid in the country of manufacture.

Whilst the EU CBAM regime covers shipments greater than €150, the UK CBAM regime will cover imported goods that total over £50,000 in a rolling 12-month period. This means monitoring your imports will be essential for compliance.

HOW TO PREPARE?

UK manufacturers should already be monitoring their exports to the EU and assisting their EU customers or reporting CBAM goods in their own name.

Understanding the UK CBAM regime, affected products and the level of embedded emissions in goods currently imported into the UK by manufacturers should begin now. Ascertaining the carbon profile of your suppliers in advance is essential, as transitioning to other suppliers with better carbon profiles could take considerable time.

BDO's Customs Data Analytics Tool simplifies the process of analysing Management Support System data from HMRC to help you reduce the risk of customs duty assessments and civil penalties. Book your free demo here: https://store.bdo.co.uk/product/customs-data-analytics-tool

The Manufacturers' Organisation

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Make UK, The Manufacturers' Organisation, is the representative voice of UK manufacturing, with offices in London, every English region and Wales.

Collectively we represent 20,000 companies of all sizes, from start-ups to multinationals, across engineering, manufacturing, technology and the wider industrial sector. Everything we do – from providing essential business support and training to championing manufacturing industry in the UK and internationally – is designed to help British manufacturers compete, innovate and grow.

From HR and employment law, health and safety to environmental and productivity improvement, our advice, expertise and influence enables businesses to remain safe, compliant and future-focused.

MakeUK.org

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The data used in this survey have been provided by UK manufacturers including members of Scottish Engineering, Manufacturing NI, and Make UK. Contributing to our surveys helps to accurately reflect trends and behaviours that shape the UK manufacturing sector. If you would like to participate in future surveys, please contact our Information and Research team research@Makeuk.org

Accountancy and business advisory firm BDO LLP is the UK member firm of BDO International, which has more than 1,700 offices in 166 countries. We operate from 17 offices across the UK, employing 7,500 people offering tax, audit and assurance, and a range of advisory services.

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We provide real solutions to industry issues, utilising our capabilities in everything from sector-specific accountancy, tax and business advice to patent box and research and development claims and M&A opportunities to help our clients grow in the UK and overseas. We also provide manufacturing businesses and organisations with robust, independent audits.

We have an excellent understanding of the issues affecting UK manufacturers as an industry sector, but we also focus on specific sub-sectors to improve our knowledge and our service to clients. These include: advanced manufacturing, aerospace, automotive, building products, chemicals and pharmaceuticals, food and drink, electronics, industrials, test and measurement and technology.

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The Manufacturers' Organisation

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