Business Sentiment Report

Business confidence Q1 2013

Business confidence climbs to a series-high at the start of 2013

Business confidence improved strongly at the start of 2013, as the majority of indicators tracked in IBEC's Business Sentiment Survey climbed higher. Many recorded the highest reading in the history of the survey, which began at the height of the crisis in 2009.

CEOs' perceptions of the overall business environment in Ireland improved in Q1 2013, marking the first time since the survey began in 2009 that the indices have been close to neutral. The current conditions index rose to -6 from -13 in Q4 2012, while the three-month forward-looking index increased to -4 from -13 in Q4 2012. Managers' assessment of the current situation and future outlook for their own businesses also recorded robust improvement. The current conditions index rose to +19 from +15 in Q4 2012, while the index for the three-month outlook jumped to a series-high of +23, up from a relatively weak reading of +10 in the previous quarter.

The improvement in confidence likely reflects positive developments at government level: Budget 2013 did not bring about a major increase in labour costs and, along with the Action Plan for Jobs, contained positive measures for job creation and the business environment. Most importantly, however, business performance indicators – sales and order books in particular – are pointing towards growth.

Domestic sales expectations improved from -2 in the previous quarter to +7 in Q1 2013, the highest reading to date, while export sales expectations gained two points in the quarter to a reading of +35. In line with the improvement in sales expectations, the index for order books rose to +21 from +15 recorded at the end of 2012.

As a result of the improved outlook for company performance, the employee numbers index is now for the first time in the history of the series in the positive and one in four managers indicated they would increase employee numbers in the coming quarter.

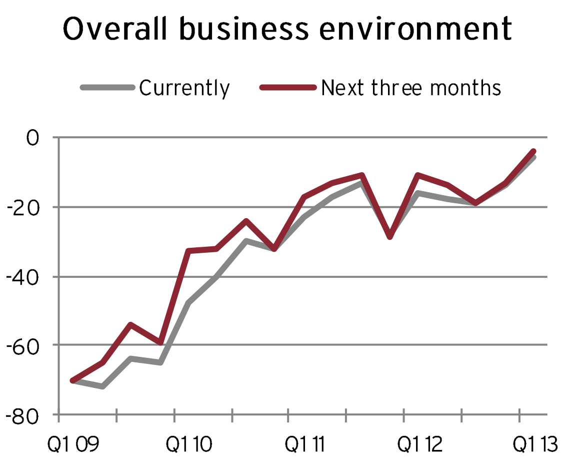
It now appears that sustained job creation in taking hold in the exporting sectors, and the index reading for these companies was +10. Last year saw an increase of 8,000 in the number of private sector employees. Given the positive reading from our employment index, which correlates well with official labour market data from the CSO (see Annex 1), we should see the trend of jobs growth continue and strengthen during 2013.

Indicator (balance of respondents)	Q2 2012	Q3 2012	Q4 2012	Q1 2013
Business confidence currently – overall	-18	-19	-14	-6
Business confidence 3 months' time – overall	-14	-19	-13	-4
Business confidence currently – own business	+5	+10	+15	+19
Business confidence 3 months' time – own business	+6	+6	+10	+23
Domestic sales	-9	-3	-2	+7
Export sales	+20	+12	+33	+35
Order books	+12	+12	+15	+21
Unit selling price	-11	-9	-16	-1
Profitability	-2	-11	-2	+6
Customer base	+18	+21	+21	+31
Employee numbers	-2	-9	-2	+4

Business confidence – overall business environment

Confidence indicators for the overall business environment in Ireland improved to series-highs at the start of 2013. The current conditions index rose to -6 from -13 in Q4 2012 and -16 in Q1 2012. The forward-looking index increased to -4 from -13 in Q4 2012 and -11 in Q1 2012. This is the first time since the survey began in 2009 that managers' perceptions of the business environment have been close to neutral.

Non-exporting companies reported a marked improvement in sentiment. The current conditions reading for non-exporters rose to -15 from -27 in the previous quarter, and the forward-looking index was -10, up from -29. Exporting companies continue to hold a broadly balanced attitude towards the business environment in Ireland, with a slight positive uptick in Q1 2013.



Business confidence – own business

Managers' confidence in their own businesses also improved in Q1 2013, marginally exceeding previous series-highs recorded in 2011. Sentiment in the current situation of the business rose to +19 from +15 in the previous quarter and +16 in Q1 2012. Confidence in the three-month outlook increased more sharply to +23 from +10 at the end of 2012 and +18 in Q1 2012.

As with overall business confidence, managers in exporting firms are more confident in the outlook for their companies than are managers in non-exporting companies. Both cohorts reported modest improvement on the current conditions index relative to the previous quarter, while the three-month outlook strengthened to +30 for exporters and +10 for non-exporters.

Domestic sales

CEOs' expectations of domestic sales for the coming three months increased to +7 in Q1 2013 – the highest rating since the series began in 2009. This is the first time the index is substantially in positive territory, pointing towards emergent growth; for most of 2011 and 2012 domestic sales expectations had hovered at close to balance, in line with the gradual stabilisation of the domestic economy. Q4 2012 and Q1 2012 both recorded a reading of -2.

Nonetheless, the positive headline indicator conceals sectoral variations. Confidence in wholesale/distribution, hospitality and electronic services was improved and positive. In contrast, the retail sector fell back into negative territory, highlighting challenges that remain before recovery in the domestic economy achieves sustainable momentum.

Export sales

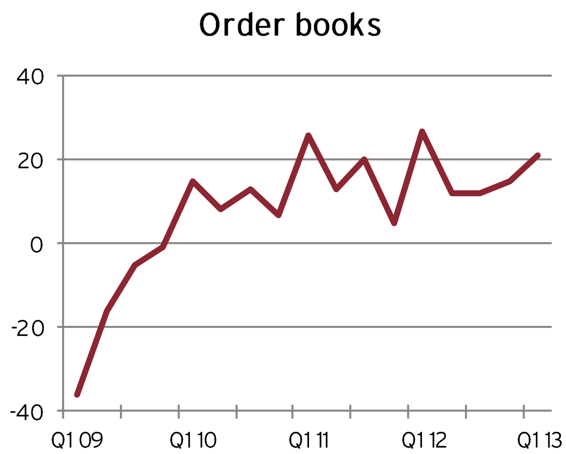
Managers' expectations on export sales improved marginally in Q1 2013 to +35 from +33 at the end of 2012, but remained below the reading of +43 recorded a year previously. At its current level the index points towards improving export growth in 2013, albeit at a somewhat slower pace than the 5% growth in 2011. Most CEOs expect a modest rather than substantial increase in exports, which will temper the growth rate somewhat.

In the food and drinks sector two-thirds of respondents expect to increase export sales slightly, despite the less favourable euro exchange rate this year. ICT and financial services had the most optimistic readings, highlighting the extent to which services are driving export growth at present. Of the modern manufacturing sectors pharmaceuticals and medical devices reported positive sales expectations, albeit with a slight moderation in medtech.

Order books

Expectations on order books improved again in Q1 2013 to +21 from +15 in Q4 2012, but remained below the Q1 2012 reading of +27, which is the current series high. The index is now above the four-quarter moving average, which has remained steady at close to +15 since the start of 2011.

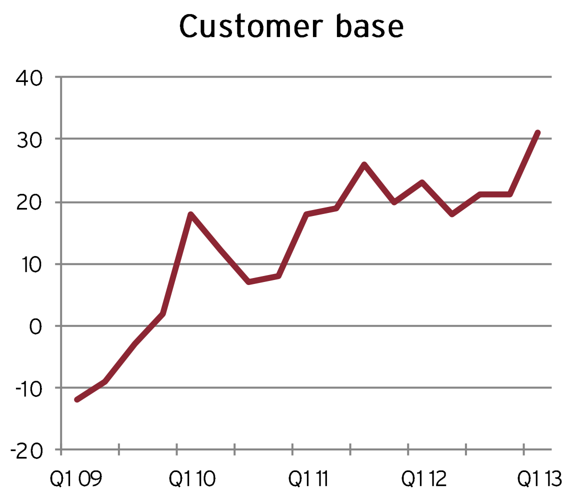
Exporters' expectations strengthened to +24 from +18 in the previous quarter. Of particular note is the improvement in order books expectations among managers in rubber and plastics and electronics manufacturing companies, marking the second consecutive quarter of improvement in these sectors and highest readings since 2011. However, metals and other manufacturing continue to feel the effect of a weaker eurozone economy and reported negative order books expectations.



Customer base

Expectations about customer base increased sharply in Q1 2013 to a series-high of +31. In particular, about four in ten managers expect to increase the firm's customer base, while only one in ten have pencilled in a decrease in the coming three-month period.

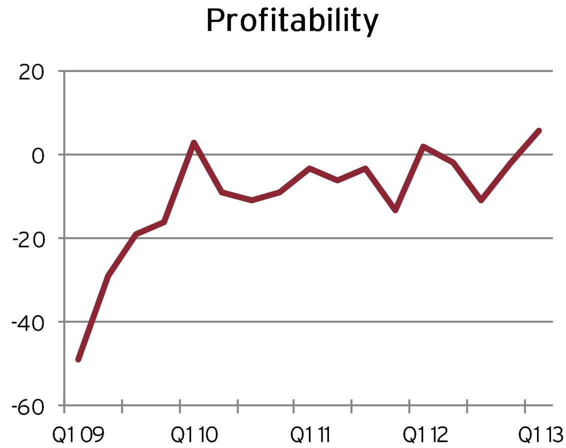
Of the major sectors, medtech, ICT and financial services held the strongest positive expectations about customer base. However, retailers and the food and drinks sector reported a deteriorating, though still positive, expectation about customer base. The negative outlook of the catch-all category other manufacturing highlights the challenges posed by a weaker eurozone economy.



Profitability

Managers' expectations about profitability improved in Q1 2013 to a series-high of +6 from a reading of -2 in the previous quarter and +2 in Q1 2012. Underlying the improved outlook is an uptick in price expectations, but also fundamental change at firm level: nearly half of managers expect to increase productivity in the coming quarter and one in three plans to invest more in R&D.

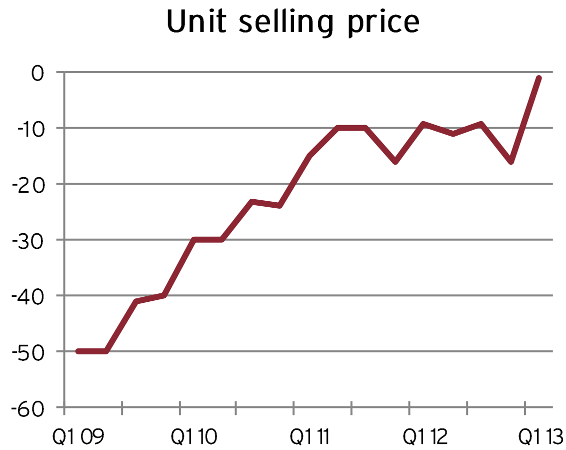
CEOs' assessment of profitability is typically the highest at the start of the year, so we may well see at least a partial reversal in the coming quarters. Nonetheless, the overall trend in the series points towards stabilisation, albeit with sectoral variation; retailers in particular continue to report expectations of deteriorating profitability, highlighting the challenges facing the sector.



Unit selling price

The outlook for unit selling price improved in Q1 2013 to -1 from -16 at the end of 2012 and -9 in Q1 2012. Managers in both exporting and non-exporting companies reported stronger price expectations. Among exporters, the index increased to +1 from -15 in the previous quarter, while domestically trading firms recorded a reading of -4, up from -13 in the previous quarter.

The food and drinks sector is likely to feel the effect of both a stronger euro, particularly relative to sterling, and weaker commodity prices and the sector now reports a balanced outlook on unit selling prices, where in the middle quarters of 2012 expectations had briefly turned more positive. Negative selling price expectations in medtech and ICT services show that even sectors with strong growth are not immune from price pressures.



Employee numbers

In one of the most encouraging developments this quarter, the indicator on employee numbers recorded the first positive reading since the survey commenced in 2009, rising to +4 from -2 in the previous quarter and -4 in Q1 2012. One in four managers indicated they would increase employee numbers in the coming quarter, up from one in five at the end of 2012.

It now appears that sustained job creation is taking hold in the exporting sectors, and the index reading for these companies was +10. Last year saw an increase of 8,000 in the number of private sector employees. Given the positive reading from our employment index, which correlates well with official labour market data from the CSO, we should see the trend of jobs growth continue and strengthen during 2013.

Annex 1: The IBEC Business Sentiment Survey and economic performance

The IBEC Business Sentiment Survey now consists of 21 quarters of data, which means that we can perform a simple investigation of how the sentiment indicators relate with the actual economic outturn recorded in the CSO's statistics. Three indicators in particular should correlate with real economic data. These are employment, domestic sales and exports.

Figure 1 shows the relationship between IBEC's employee expectations index and the annual percentage change in private sector employees from the CSO's Earnings, Hours and Employment Costs Survey. The correlation between the two strong at over 95% and the two series track each other quite well from the start in 2009.

The IBEC index is a leading indicator, with the best correlation occurring when the series is brought forward in time by one quarter relative to the CSO's data. This robust relationship exists despite a slight difference in the timing of IBEC's quarterly surveys and the calendar quarters used by the CSO.

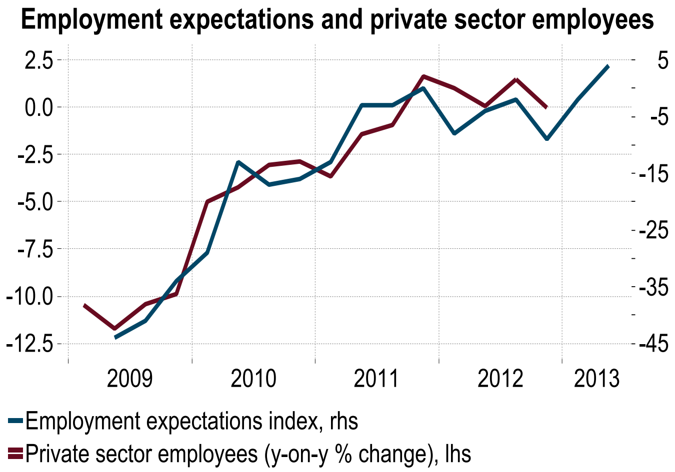


Figure 2 shows the relationship between IBEC's index of domestic sales expectations and the outturn for domestic demand (personal consumption, government consumption and investment) from the CSO's Quarterly National Accounts.

The relationship between IBEC's sentiment indicator and domestic demand is quite strong, with a correlation of 85%. The best correlation between IBEC's indicator and the CSO's data occurs when sentiment is brought forward by two quarters rather than one, which may be explained by the lags in placing an order, delivery of a good or service and payment of invoices.

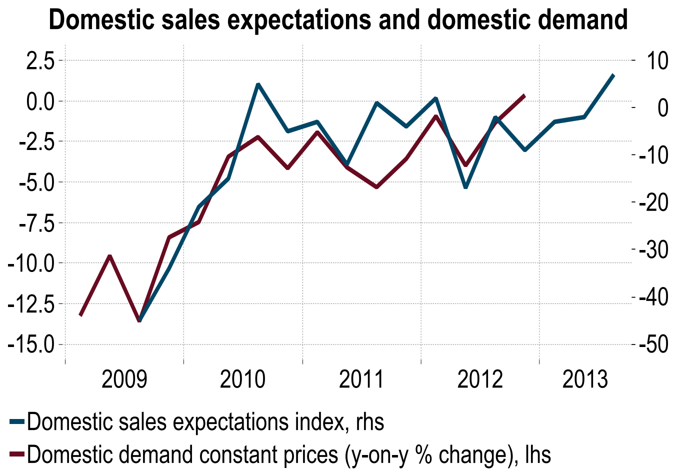


Figure 3 shows the relationship between IBEC's index of export sales and the outturn for the volume of goods and services exports from the CSO's Quarterly National Accounts. Irish exports are fairly volatile and fluctuating, but there is a good correlation between the IBEC series and actual export performance of close to 90% when the data are smoothed over two quarters.

However, the IBEC index does not appear to have predictive power, with the best correlation occurring with no time lags. It may be that development of export sales is more difficult to predict and managers instead rely on their current perceptions of the state of the business.

Methodological note

The Business Sentiment Report is based on a survey of manufacturing and services firms and presents the balance of respondents' sentiment for a series of indicators. Each quarterly sample consists of about 400 IBEC member companies.

The report findings are presented as simple balances of the difference between the positive and negative responses. A positive balance indicates that more firms responded positively than negatively to a particular question; for instance, a positive balance for order books means that a greater percentage of firms expect order books in the coming months to be higher rather than lower.

Four confidence questions ask firms to rate the overall business environment and their own business, currently and in the next three months. Possible answer options for each question are very good, good, average, poor and very poor.

Activity-based indicators ask companies to rate their expectations in three months' time on a range of indicators such as order books, profitability and employment levels. Possible answer options for each indicator are decrease substantially, decrease slightly, stay the same, increase slightly and increase substantially.

IBEC

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