

NI Manufacturing & Services Output – Q2 2011

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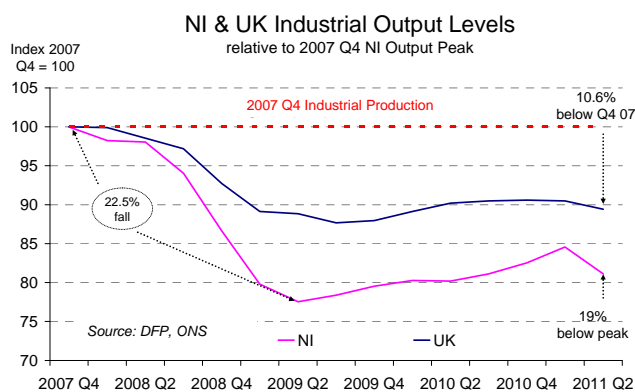
DFP's Index of Production / Manufacturing Output Q2 2011

NI's manufacturing recession was longer, deeper and recovery weaker than previously thought

Yesterday saw the release of a disappointing set of data from Northern Ireland's Department of Finance & Personnel (DFP) in the shape of its latest industrial production figures (*the vast majority of which is the manufacturing sector but also includes Mining & Quarrying and Electricity, Gas & Water Supply*) for Northern Ireland (NI). The latest figures are published for the first time using the Standard Industrial Classification 2007 (SIC07) basis, as opposed to a SIC03 basis. The data for Q1 2011 and earlier has been converted to approximate the SIC07 coverage and therefore are not strictly revisions. **The most significant impact from the changes is the scale of the peak to trough (PTT) decline is significantly greater than previously stated and the recovery has been somewhat weaker.** However, it is noted that the new methodology and coverage means comparing the new data with the historic series is not strictly a like-for-like comparison. The new approach also identifies the peak in industrial / manufacturing output as Q4 2007 and not Q2 2008 as previously estimated. The industrial / manufacturing downturn also lasted for six quarters as opposed to five quarters as identified previously.

Industrial Production posts hefty fall in Q2 2011

NI's industrial production fell by 4.1% in Q2 2011 relative to the previous quarter and compared unfavourably with a decrease of 1.2% for the UK. Despite this latest quarterly decrease, NI's industrial output in Q2 2011 was still 1.2% higher than the same quarter in 2010. Conversely, UK industrial output in Q2 2011 was 0.9% y/y lower. **The latest figures reveal that the scale of the peak to trough (PTT) fall in industrial output for NI is now a staggering 22.4% between the Q4 2007 peak and the Q2 2009 trough.** This is significantly greater than NI's PTT decline of 15.4% reported in July's Index of Production release. **It is now clear that that NI's PTT fall in industrial output was almost twice that experienced within the UK (-12.3%).** Since the recovery in the industrial sector began (Q3 2009), NI's industrial output has risen by just 4.6% (Q2 2009 to Q2 2011) which compares favourably with the UK +2.0%. However, this is due to the fact that NI's output has fallen much more than its equivalent sector within the UK. For example, despite a recovery in recent quarters, NI's industrial output in Q2 2011 was almost 19% below the pre-downturn peak in Q4 2007. This represents a significantly sharper contraction than the UK (-10.6%).



NI & UK Industrial Output

Service Sector Category	Q/Q Change Q2 2011		Y/Y Change Q2 2011		Change since peak 2007 Q4 - 2011 Q2	
	NI	UK	NI	UK	NI	UK
Manufacturing	-3.3%	0.2%	3.5%	3.2%	-20.8%	-6.2%
Electricity, Gas, Steam & Air Conditioning Supply	-6.8%	-1.7%	-5.9%	-4.9%	-0.6%	-26.5%
Water Supply, Sewerage & Waste Management	0.0%	-2.7%	0.3%	1.8%	3.4%	-6.7%
Mining & Quarrying	-7.2%	-6.6%	-20.2%	-16.9%	-31.5%	-30.4%
Total Production	-4.1%	-1.2%	1.2%	-0.9%	-18.9%	-10.6%

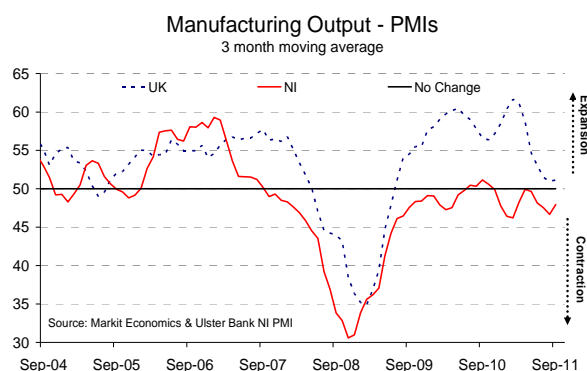
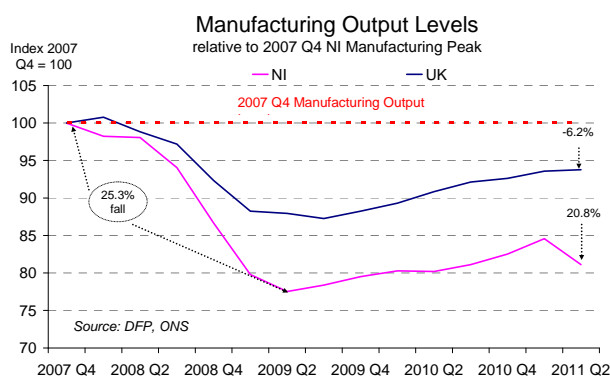
Source: ONS & DFP Index of Production

NI's Mining & Quarrying industry output down almost one third from peak

Within NI's industrial production sectors, Mining & Quarrying posted a hefty 7.2% q/q decline in output in Q2 2011 (UK=-6.6%). **The level of output in Q2 2011 represented a whopping 20% decline relative to the same quarter last year (UK= -16.9%).** It is now clear that the level of output within *Mining & Quarrying* in NI is back to output levels last recorded in 2002 Q4 and has shown no sustained recovery whatsoever. NI's Mining & Quarrying output is down almost one third (31.5%) relative to the 2007 Q4 peak (UK = -30.4% over the same period). This decline mirrors the steep decline in construction output which has also fallen by around one third. The construction output figures for Q2 2011 are due on 19 October. Given that the NI Executive has slashed its capital investment plans by 37% (*in real terms*) over the next few years relative to its recent peak the *Mining & Quarrying* sector is likely to record further declines in output (& employment) in the quarters ahead.

Northern Ireland's manufacturing output falls for the first time in 8 quarters

NI's manufacturing sector, which accounts for 83% of industrial production, recorded its first fall in output since Q2 2009 (8 quarters) in Q2 2011. This manufacturing recovery was actually longer than previously estimated and the strength of the recovery has been somewhat weaker. Local manufacturing output decreased by 3.3% q/q in Q2 2011 which compared with a rise of 0.2% q/q for the UK. Despite this recent decline, manufacturing output is still 3.5% higher than the corresponding quarter one year previous (Q2 2010). This compares with 3.2% y/y for the UK.



Northern Ireland's manufacturing recession was deeper & longer than previously estimated

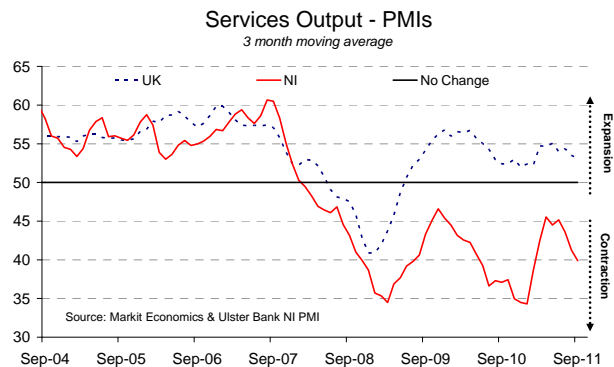
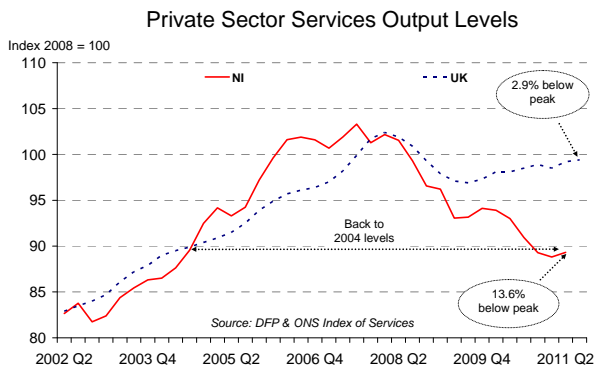
Yesterday's figures also reveal a steeper peak to trough (PTT) fall in manufacturing output than was previously estimated. Furthermore, there were six successive quarters of manufacturing decline, one more than previously estimated. NI's manufacturing industry saw output decrease by one quarter (25.3%) between Q4 2007 and Q2 2009. The PTT decline was previously estimated at 18%. By comparison, the UK's PTT decline in manufacturing output is almost half that of NI at 13.4% (2008 Q1 - 2009 Q3).

Northern Ireland's manufacturing recovery weaker than the UK's and earlier estimates

Since the manufacturing recovery first began in Q4 2009, NI's manufacturing output has risen by just 5.9% with output still almost 21% below the Q4 2007 pre-downturn peak. **Thus, NI's manufacturing industry has recouped just over one fifth of its lost output during the recession.** This compares with previous data that suggested just over half of the lost output had been regained. Meanwhile, UK manufacturing has recorded seven successive quarters of growth amounting to a cumulative increase of 7.5%. As a result, UK manufacturing output is just 6.9% below its Q1 2008 peak. **That is, UK manufacturing has recouped almost half the output it lost during the downturn.** The divergence between the UK and NI manufacturing recoveries has been apparent within the Ulster Bank / Markit Economics PMI surveys for quite some time. There is no manufacturing sub-sector data available at this stage but this will be released at a later date.

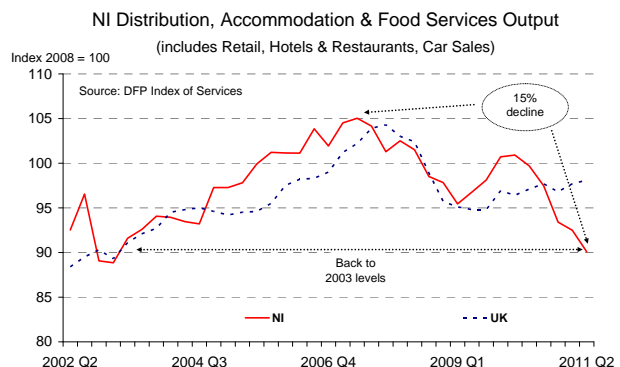
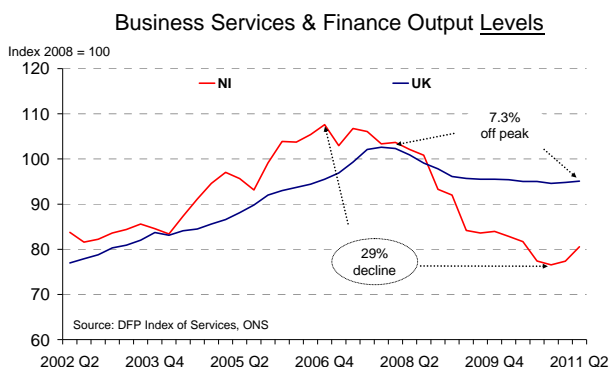
Private Sector Services Output (Index of Services) Q2 2011

The Index of Services Survey (IoS) released yesterday measures output within the private services sector. The latest survey incorporates a new methodology, as with the Index of Production, which means comparisons with previous data are not strictly on a like-for-like basis. One of the most significant impacts from the move to the new Standard Industrial Classification 2007 (SIC07) basis, from a SIC03 basis, is the peak of the index is now estimated to be Q3 2007 and not Q3 2006. This new peak is in line with the Ulster Bank / Markit Economics PMI for the services sector. Despite these methodological changes, it is clear that there remains a marked divergence in the performance of NI's service sector relative to the UK.



Private sector services output posts its first rise since Q4 2009

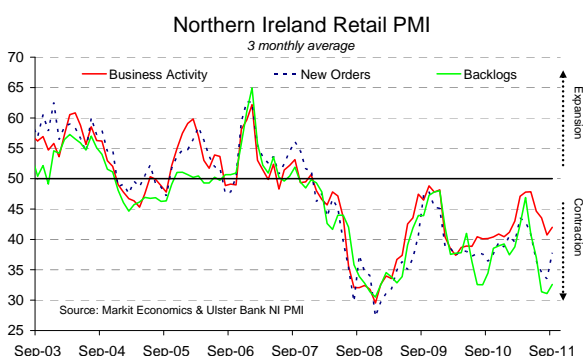
The latest IoS survey reports a 0.6% q/q rise in NI private sector services output in Q2 2011. This represented the first increase in output since Q4 2009. The UK's service sector posted a more modest rise of 0.2% q/q but this marked its fourth quarterly rise since Q4 2009. Despite NI's latest rise in output, service sector activity remains 13.6% below the Q3 2007 peak. Conversely, the UK services sector is just 2.9% below its Q1 2008 peak. This divergence in NI and UK service sector output has been evident within the Ulster Bank / Markit Northern Ireland PMI survey for quite some time. NI's private sector services output is now back at 2004 levels. By contrast, UK private sector services output is currently back at 2007 levels. This is of particular concern for NI given that the public expenditure cuts have yet to bite in any meaningful way. These will have a negative impact on both consumer sensitive sectors and business services. As is highlighted below these sectors account for almost three quarters of private sector services and they have already experienced steep falls before the impact of the public expenditure cuts is felt in the NI economy.



Business Services & Finance Output remains at extremely low levels

This is the largest category within NI's private sector services industry and accounts for 41% of output (includes banking, advertising, consultancy, solicitors, quantity surveyors, estate agents, recruitment consultants etc). Since its peak in Q4 2006, output within the Business Services & Finance (BSF) sector plummeted by 29% PTT in Q4 2010. By comparison the UK's BSF sector posted a PTT decline of 7.8%. NI's more pronounced property boom and bust is the main explanatory factor behind this extreme divergence in NI/UK performance. The latest figures for Q2 2011 reveal a 4.1% q/q increase (UK= +0.3%). This represented

the fastest rate of growth since Q1 2006 but this rebound is occurring from extremely weak levels. Going forward, however, the cuts in public expenditure will adversely affect a significant number of firms in this sector. For example, capital investment plans have been slashed and this will impact on those service industries linked to the construction industry. Furthermore, low levels of mortgage activity and a fairly stagnant housing market will remain major obstacles to a meaningful recovery in advertising, finance and legal activities. Although NI has announced recent inward investment and expansion within this sector through the likes of First Derivatives, Allen & Overy and PwC. Outside of BSF, the *Transport, Storage, Information & Communication* (TSIC) sector also posted a quarterly increase (1.6%). This followed three successive quarters of decline. The TSIC and 'Other services' sectors are the only services sectors to have higher levels of output in Q2 2011 relative to the peak in private sector services back in Q3 2007.



Consumer sensitive sectors have been hit hard and more challenges lie ahead

The new survey methodology now has a new category - *Wholesale, Retail, Repair, Accommodation & Food Service*. This amalgamates the previous *Distribution* sector alongside *Hotels & Restaurants*. This new sector accounts for 31% of total private sector services activity. Since the middle of 2010, this sector has experienced significant declines in output with five consecutive quarterly falls. Over this period the sector has experienced a hefty 10.7% decrease in output which compares with a rise of 1.8% for the UK. Clearly, this period partly reflects the fact that the influx of shoppers from the Republic of Ireland has eased substantially. To date, NI's *Wholesale, Retail, Repair, Accommodation & Food Service* sector has experienced a PTT decline of 15% since Q2 2007. By comparison, output within the corresponding sector for the UK is only 4% off Q2 2007 levels. The divergence in NI/UK performance in this sector is expected to continue. Inflationary pressures, further rises in unemployment and the impact from fiscal austerity (*tax rises and benefits / public expenditure cuts*) represent headwinds that are more significant to the NI's lower wage economy. More up to date consumer spending figures, such as new car sales and the Ulster Bank / Markit Economics Retail PMI, signal that the consumer sensitive sectors deteriorated further in Q3 2011.

NI & UK Private Service Sector Output

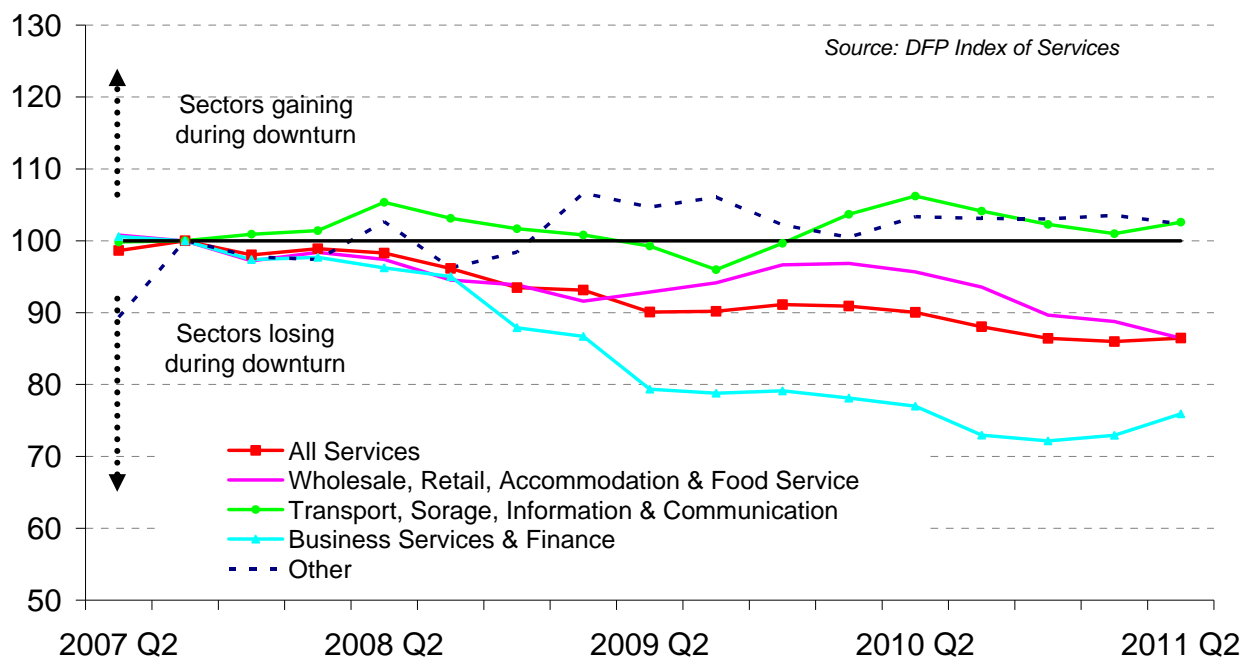
Service Sector Category	Q/Q Change Q2 2011		Y/Y Change Q2 2011		Change since peak 2007 Q3 - 2011 Q2	
	NI	UK	NI	UK	NI	UK
Wholesale, Retail, Repair, Accommodation & Food Service	-2.6%	0.4%	-9.6%	1.0%	-13.5%	-5.6%
Transport, Storage, Information & Communication	1.6%	0.0%	-3.4%	2.2%	2.6%	0.2%
Other Services*	-1.2%	0.1%	-1.0%	1.3%	2.4%	5.0%
Business Services & Finance	4.1%	0.3%	-1.4%	0.1%	-24.6%	-6.9%
Total Services	0.6%	0.2%	-4.0%	1.0%	-13.6%	-2.3%

Source: ONS & DFP Index of Services, *NI & UK have different coverage

NI Private Sector Services Output Levels

relative to 2007 Q3 service sector peak

Index 2007 Q3 = 100



Richard Ramsey,
13 October 2011

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