

Statistical bulletin

Profitability of UK companies: October to December 2014

The net rate of return on capital employed for UK private non-financial corporations related to their UK operations.



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1 . Main points

- Private non-financial corporations' profitability, as measured by their net rate of return, was estimated at 11.9% in Quarter 4 (Oct to Dec) 2014, down from the revised estimate of 12.3% in Quarter 3 (July to Sept) 2014
- Manufacturing companies' net rate of return was estimated at 12.0% in Quarter 4 (Oct to Dec) 2014, 1.7 percentage points higher than the revised estimate of 10.3% in Quarter 3 (July to Sept) 2014, but 1.4 percentage points lower than the estimate for Quarter 2 (Apr to June) 2014 (13.4%)
- Service companies' net rate of return was estimated at 16.9% in Quarter 4 (Oct to Dec) 2014, down from the highest recorded quarterly estimate of 18.4% in Quarter 3 (July to Sept) 2014
- UK Continental Shelf (UKCS) companies' net rate of return was 10.4% in Quarter 4 (Oct to Dec) 2014. This was the lowest estimated rate since the series began in Quarter 1 (Jan to Mar) 1997
- UK non-CS companies' net rate of return was 12.0% in Quarter 4 (Oct to Dec) 2014. This was down from the revised estimate of 12.3% in Quarter 3 (July to Sept) 2014. The highest estimated net rate of return for this series was recorded in Quarter 3 (July to Sept) 1997 (13.5%)
- In 2014, the net rate of return of private non-financial corporations was estimated at 11.9%, the highest recorded annual estimate since 1998 (12.4%)
- To see the above data in more context, data for earlier periods are shown at Tables 1 and 2, they are also presented in the graphs at Figures 1 to 4

2 . About this release

Understanding profitability:

Profitability, using the net rate of return calculation method, is a common way of measuring the economic success of a company or sector. The rate of return is calculated by expressing the economic gain, or profit, as a percentage of the capital used to produce it. See paragraph 2 of the Background notes for a more comprehensive definition.

All estimates in this statistical bulletin are consistent with the [Quarterly National Accounts Q4 2014](#) published on Tuesday 31 March 2015.

3 . Your views matter

We are constantly aiming to improve this release and its associated commentary. We would welcome any feedback you might have, and would be particularly interested in knowing how you make use of these data to inform your work. Please contact us via email: profitability@ons.gsi.gov.uk or telephone Stephanie Duff on +44 (0) 1633 456098.

4 . Net rate of return of private non-financial corporations

The net rate of return of all private non-financial corporations in Quarter 4 (Oct to Dec) 2014 was estimated at 11.9%. This compares with the revised estimate of 12.3% for Quarter 3 (July to Sept) 2014.

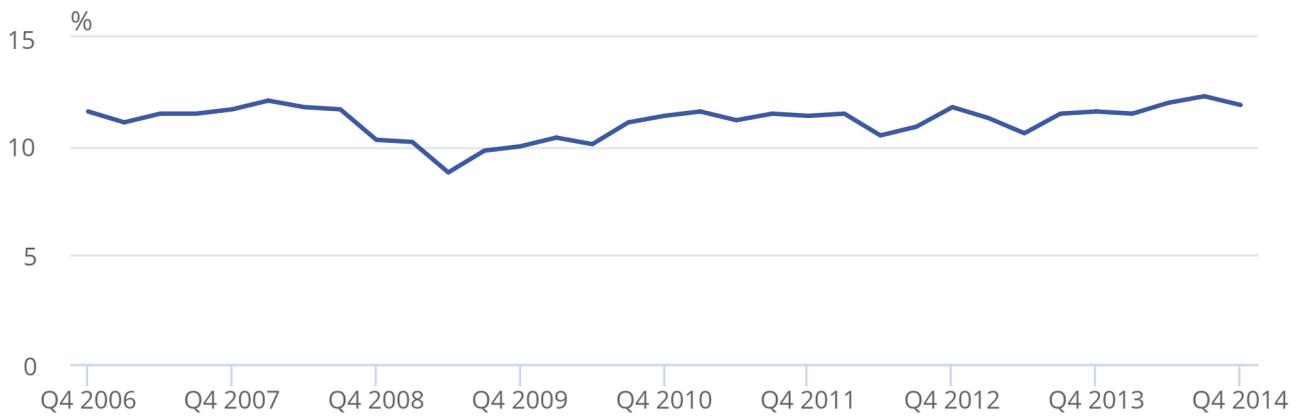
As figure 1 shows, the net rate of return for private non-financial corporations reached its highest point following the economic downturn, in Quarter 3 (July to Sept) 2014 at 12.3% and was at its lowest level in Quarter 2 (Apr to June) 2009 at 8.8%.

Figure 1: Net Rate of Return of private non-financial corporations, Quarter 4 (Oct to Dec) 2006 to Quarter 4 (Oct to Dec) 2014

UK

Figure 1: Net Rate of Return of private non-financial corporations, Quarter 4 (Oct to Dec) 2006 to Quarter 4 (Oct to Dec) 2014

UK



Source: Office for National Statistics

Table 1: Annual Net Rate of Return

United Kingdom

Net rates of return of UK Private Non-financial Companies (%)

	Total Manufacturing Services		UK Continental Shelf (UKCS)
1997	13.4	14.1	14.3
1998	12.4	12.0	14.0
1999	11.5	11.2	12.7
2000	11.4	10.4	11.7
2001	9.9	7.7	10.2
2002	11.1	9.0	11.7
2003	11.5	8.2	13.3
2004	11.8	10.0	13.1
2005	11.7	9.2	12.8
2006	11.8	8.7	12.6
2007	11.4	8.0	12.5
2008	11.4	8.1	12.6
2009	9.7	5.2	12.1
2010	10.8	5.6	13.1
2011	11.4	8.6	13.3
2012	11.2	7.0	14.4
2013	11.2	8.2	14.8
2014	11.9	10.9	16.7

Source: Office for National Statistics

Table 2: Quarterly Net Rate of Return

United Kingdom

Net rates of return of UK Private Non-financial Companies (%)

	Total Manufacturing Services			UK Continental Shelf (UKCS)
2007 Q1	11.1	9.7	11.6	28.0
2007 Q2	11.5	7.7	12.7	28.5
2007 Q3	11.5	7.9	13.2	34.5
2007 Q4	11.7	6.9	12.6	50.5
2008 Q1	12.1	9.4	13.2	46.7
2008 Q2	11.8	10.3	10.9	52.6
2008 Q3	11.7	6.4	13.0	44.1
2008 Q4	10.3	6.4	13.3	17.7
2009 Q1	10.2	5.7	12.7	30.7
2009 Q2	8.8	4.6	11.5	21.4
2009 Q3	9.8	5.2	12.4	29.7
2009 Q4	10.0	5.2	11.8	44.4
2010 Q1	10.4	5.7	12.7	34.5
2010 Q2	10.1	5.6	12.2	36.4
2010 Q3	11.1	5.6	14.1	41.2
2010 Q4	11.4	5.6	13.4	45.1
2011 Q1	11.6	9.2	12.9	45.4
2011 Q2	11.2	9.5	12.7	41.3
2011 Q3	11.5	8.0	14.2	39.1
2011 Q4	11.4	7.6	13.4	42.6
2012 Q1	11.5	7.3	13.9	38.0
2012 Q2	10.5	5.9	13.8	32.6
2012 Q3	10.9	6.1	15.5	29.9

2012 Q4	11.8	8.7	14.3	29.3
2013 Q1	11.3	6.1	15.0	27.5
2013 Q2	10.6	7.0	14.1	26.1
2013 Q3	11.5	9.3	15.9	26.5
2013 Q4	11.6	10.4	14.2	24.0
2014 Q1	11.5	7.8	16.0	20.6
2014 Q2	12.0	13.4	15.5	17.4
2014 Q3	12.3	10.3	18.4	12.4
2014 Q4	11.9	12.0	16.9	10.4

Source: Office for National Statistics

5 . Economic context

According to the Quarterly National Accounts, the UK economy grew by 0.6% in the final quarter of 2014, and by 2.8% over the 2014 calendar year as a whole. This was the highest annual growth rate recorded since 2006, and was accompanied by the highest annual net rate of return for UK companies since 1998, of 11.9%. This was an improvement of 0.7 percentage points on the previous year, resulting from gross operating surplus including the alignment adjustment – a measure of profits – growing at a faster rate than the amount of capital employed between 2013 and 2014.

Breaking down the aggregate measure in to its components reveals some notable features. Despite falling slightly in the final quarter of 2014, from 18.4% to 16.9%, the net rate of return in the services industry has generally risen steadily since the height of the economic downturn in 2009. In addition, the 2014 estimate of 16.7% was higher than in any year since comparable data were first produced in 1997. This coincides with strong growth in the services industry, which is the only headline industry to have surpassed pre-downturn peak levels of output to date. In addition, the Confederation of British Industry (CBI) Service Sector Survey reported strong growth in services profitability in the first three quarters of 2014, but a decline in the final quarter. Whilst the manufacturing net rate of return was not as strong as for services in 2014 (10.9%), it has also increased since 2012 (7.0%).

In contrast, UK Continental Shelf companies, which are mainly involved with the extraction of oil and gas from the North Sea, have seen a dramatic fall in the net rate of return between 2013 and 2014, from 26% to 15%. Although the profitability of these companies may have been affected by the recent decline in oil prices, they have seen their net rate of return decline since 2011, and therefore other factors may be relevant.

Despite the economy experiencing consistent economic growth over the past 8 quarters, other indicators related to profitability have shown mixed messages. Although business investment contracted by 0.9% in the final quarter of 2014, it grew by 7.5% between 2013 and 2014, the largest increase since the downturn. However, Ernst and Young have reported a surge in profit warnings, with 299 companies issuing profit warnings over the course of 2014, the highest since 2008. Many companies cited intense competition and over-capacity, but the strong value of sterling was cited as a potential factor.

6 . Manufacturing and service companies, Quarter 4 (Oct to Dec) 2014

Manufacturing companies

The estimated net rate of return for manufacturing companies in Quarter 4 (Oct to Dec) 2014 was 12.0%. This was 1.7 percentage points higher than Quarter 3 (July to Sept) 2014.

As Figure 2 highlights, the estimates of net rate of return for the manufacturing sector can be volatile. Variation from one quarter to the next usually reflects the fortunes of a number of the larger companies and is not necessarily an indicator of improving or worsening economic performance across the sector as a whole.

Service companies

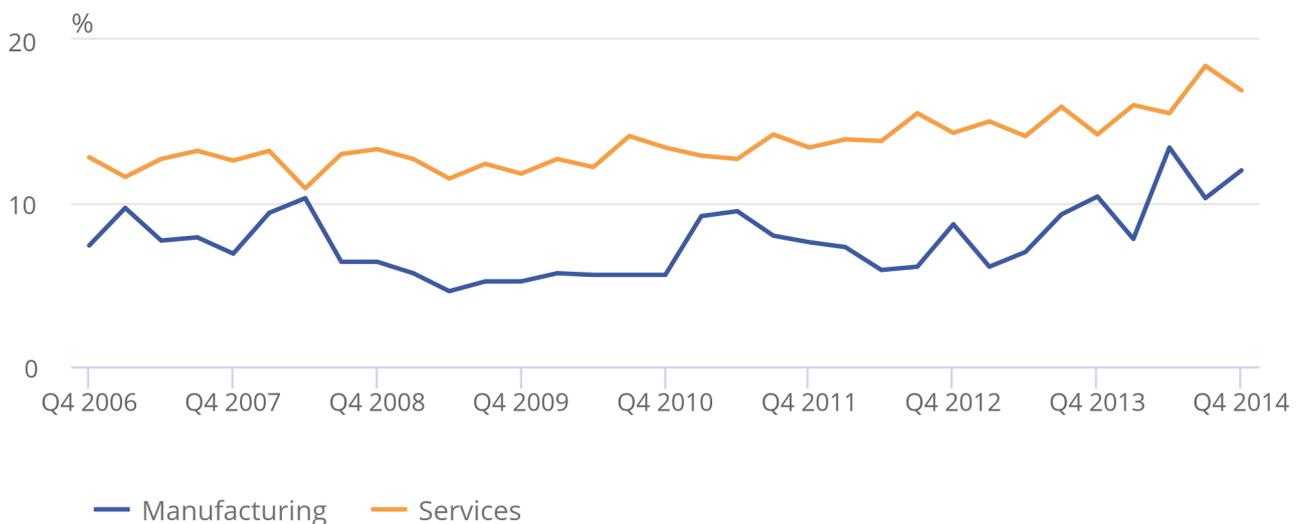
The estimated net rate of return for service companies in Quarter 4 (Oct to Dec) 2014 was 16.9%. This was the second highest estimated rate since the series began, the highest was the revised estimate of 18.4% for Quarter 3 (July to Sept) 2014. Figure 2 shows the net rate of return for service companies since Quarter 4 (Oct to Dec) 2006. The underlying trend in recent years reflects the improving economic recovery.

Figure 2: Net Rate of Return of Manufacturing and Services Companies, Quarter 4 (Oct to Dec) 2006 to Quarter 4 (Oct to Dec) 2014

UK

Figure 2: Net Rate of Return of Manufacturing and Services Companies, Quarter 4 (Oct to Dec) 2006 to Quarter 4 (Oct to Dec) 2014

UK



Source: Office for National Statistics

7 . United Kingdom non-continental shelf (UK non-CS) companies, Quarter 4 (Oct to Dec) 2014

UK non-CS companies comprise manufacturing, service and other UK non-CS companies (such as construction and power supply).

The estimated net rate of return for UK non-CS companies in Quarter 4 (Oct to Dec) 2014 was 12.0%. This was down 0.3 percentage points from the revised estimate of 12.3% in Quarter 3 (July to Sept) 2014.

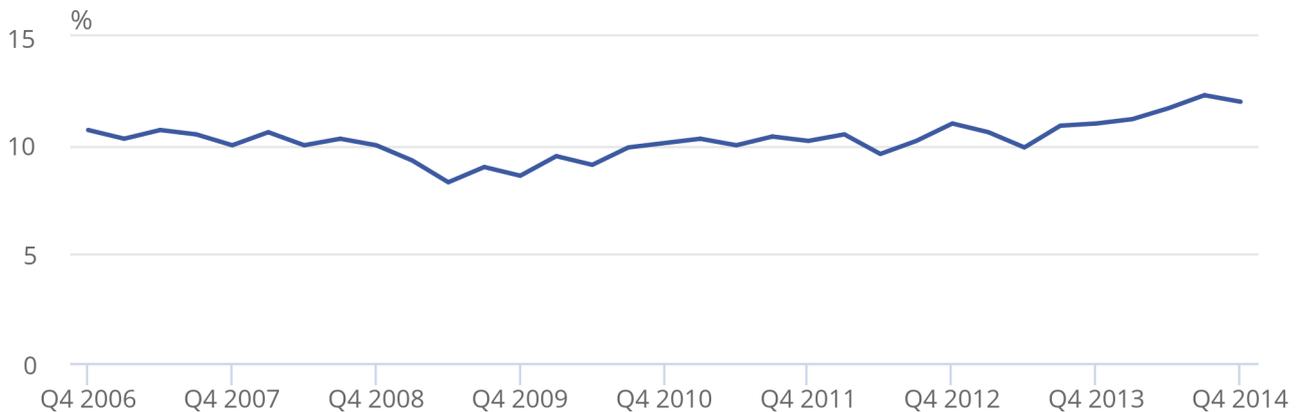
As the net rate of return of UK non-CS companies makes up the majority of private non-financial corporations, figure 3 shows a comparable picture to that of all private non-financial corporations (Figure 1).

Figure 3: Net Rate of Return of UK non-CS Companies, Quarter 4 (Oct to Dec) 2006 to Quarter 4 (Oct to Dec) 2014

UK

Figure 3: Net Rate of Return of UK non-CS Companies, Quarter 4 (Oct to Dec) 2006 to Quarter 4 (Oct to Dec) 2014

UK



Source: Office for National Statistics

8 . United Kingdom continental shelf (UKCS) companies, Quarter 4 (Oct to Dec) 2014

UKCS companies are defined as those involved in the exploration for, and extraction of, oil and natural gas in the UK. Due to the nature of the capital assets employed, net rates of return for continental shelf companies are not directly comparable with those for other industries.

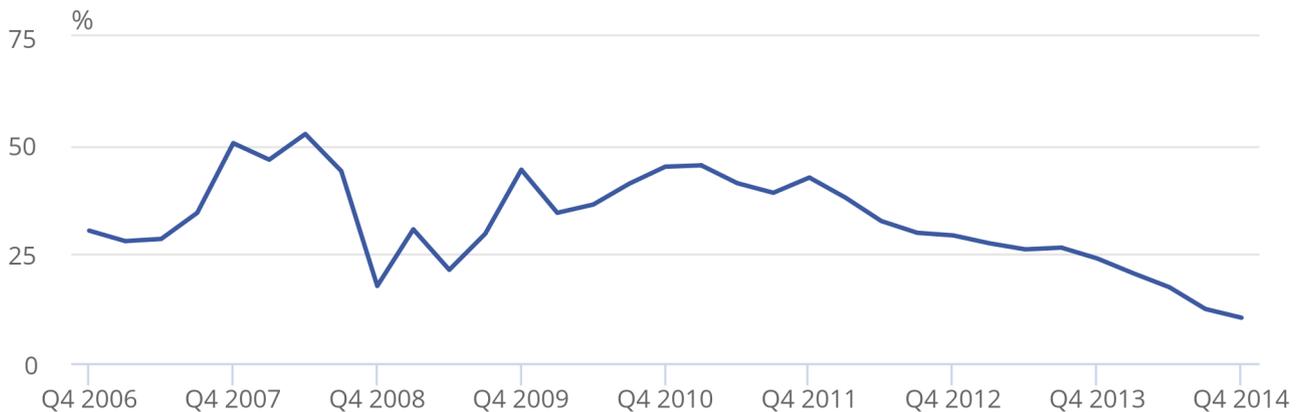
The estimated net rate of return for UKCS companies in Quarter 4 (Oct to Dec) 2014 was 10.4%, the lowest recorded estimated rate since the series began in 1997. This was the third consecutive lowest estimate and was 2.0 percentage points lower than the previous quarter. As described in the Economic Commentary this may be due to the recent decline in oil prices.

Figure 4: Net Rate of Return of UKCS Companies, Quarter 4 (Oct to Dec) 2006 to Quarter 4 (Oct to Dec) 2014

UK

Figure 4: Net Rate of Return of UKCS Companies, Quarter 4 (Oct to Dec) 2006 to Quarter 4 (Oct to Dec) 2014

UK



Source: Office for National Statistics

9 . International comparisons

Profitability is a relative measure of profit and what created it. This bulletin shows the rate of return on capital employed. Unfortunately, other countries use a range of different measures, making international comparisons difficult.

Eurostat show comparisons, across the European Union, of the aggregated national profit share defined as Gross Operating Surplus (GOS) plus Mixed Income divided by Gross Value Added (GVA) on a European System of Accounts 2010 (ESA10) basis. GVA is the difference between the cost of inputs (whether capital or labour) and the cost of the output. The difference in the cost is due to the value added by the use of labour and capital. GOS is the income earned from capital.

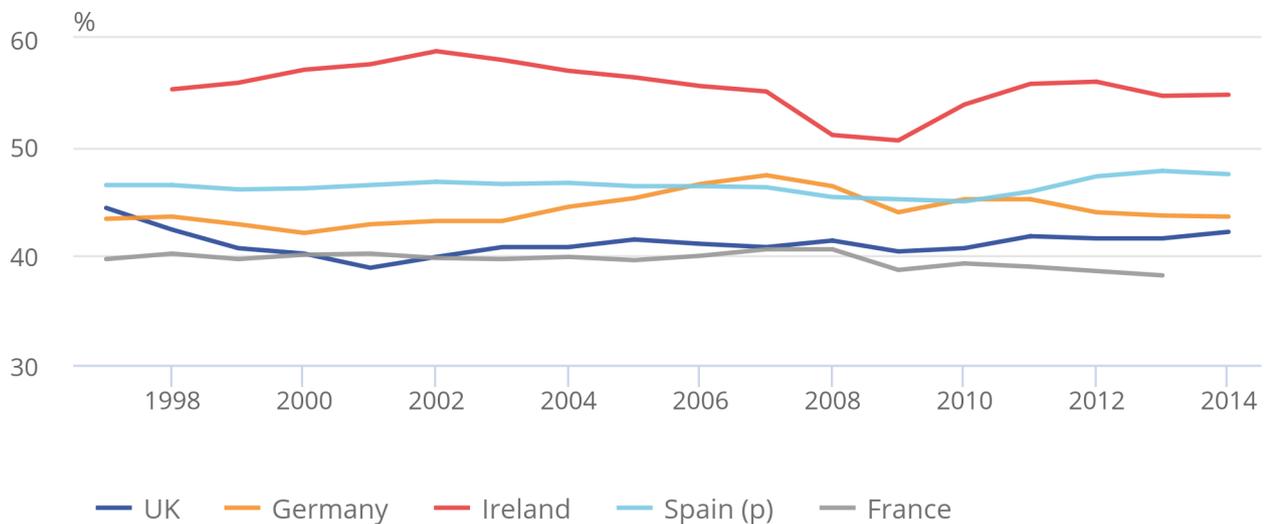
International data on an ESA10 basis are only available at the aggregate National level (Figure 5).

Figure 5: International Profit Share 1998 to 2014

International Comparisons

Figure 5: International Profit Share 1998 to 2014

International Comparisons



Source: Office for National Statistics, Eurostat

Notes:

1. Please note values for Spain are based on Provisional Eurostat data. Data for France for 2014 is currently unavailable.

The UK aggregated profit share in 2014 was 42.2%, up from 41.6% in 2013. Across the years, as shown in Figure 5, the UK aggregated profit share was comparable with that of France.

10. Background notes

1. What's new

Forthcoming changes

ONS has announced that Quarterly National Accounts data consistent with 2015 Blue and Pink books, originally scheduled for publication on 30 June, will now be published 30 September. ONS has released a [statement giving more detail regarding this change in publication dates](#).

Revisions

In this release, revisions to the net rates of return for PNFCs have been made back to Quarter 1 (Jan to Mar) 2014, and are consistent with [the UK National Accounts revisions policy](#). These incorporate revisions arising from the production of the [Quarterly National Accounts Quarter 4 \(Oct to Dec\) 2014](#).

2. Understanding the data

Interpreting the data

Private non-financial corporations (PNFCs) are comprised of UK Continental Shelf (UKCS), manufacturing, non-financial service sector companies and others (including construction, electricity and gas supply, agriculture, mining and quarrying). UKCS companies are defined as those involved in the exploration for, and extraction of, oil and natural gas in the UK.

The rates of return presented are ratios of operating surpluses compared to capital employed, expressed as percentages. The ratios measure the 'accounting' rates of return achieved in a particular period against total capital employed. The rates of return are on the basis of current replacement cost and relate to UK operations of PNFCs. The net rate of return uses capital estimates which are net of capital consumption, and is more widely used than the gross rate of return. Rates of return are published for quarters and for years.

The main components of the operating surpluses data used in the compilation of the rates of return are the profits data from the Quarterly Operating Profits Survey (QOPS) and provisional HMRC company profits data.

The underlying capital data used to calculate these rates of return are based upon capital stocks and capital consumption data.

Definitions and explanations

The gross operating surplus of PNFCs consists of gross trading profits, plus income from rental of buildings, less inventory holding gains.

Gross trading profits include only that part of a company's income arising from trading activities in the UK. It does not include income from investments or other means, such as earnings from abroad. Gross trading profits are calculated before payments of dividends, interest and tax. The gross trading profits figures used in the calculation of **gross operating surplus** exclude the quarterly alignment adjustments applied to UK non-CS companies' gross trading profits, as published in the Quarterly National Accounts.

Inventory holding gains are the differences in the change in the book value of inventories measured at replacement cost and historic cost. The holding gain is subtracted from profits because revaluations are not considered to be part of economic activity, as defined for National Accounts purposes.

Estimates of gross capital stock are a measure of the cost of replacing all produced capital assets held at a particular point in time. **Capital employed** is the value of fixed assets, plus the value of inventories. It measures the value at replacement cost of all fixed assets at the end of a calendar year. This includes all tangible assets and intellectual property products which have been produced and are themselves repeatedly or continuously used in the processes of production for more than a year. Tangible assets include buildings, plant and machinery. Intellectual property products include computer software and mineral exploration costs. For UKCS companies, capital employed includes mineral exploration costs and oil rigs, but not the oil and gas reserves that are classified as non-produced assets. Inventories include raw material and fuel that are used up in production. Book values are used for levels of inventories.

In the calculations for net rates of return, estimates of net operating surplus are net of capital consumption (depreciation). Capital consumption is derived from capital stock and covers the depreciation of fixed assets over their service lives. Estimates of net capital are net of accumulated capital consumption; that is, they are a measure of the written down replacement costs of fixed assets.

Use of the data

The underlying profits data used to calculate the rates of return are used within the [UK National Accounts](#). They are consistent with the [Quarterly National Accounts Quarter 4 \(Oct to Dec\) 2014](#) and the [UK Economic Accounts Quarter 4 \(Oct to Dec\) 2014](#), both published on 31 March 2015.

3. Methods

Sampling methodology

Details on the methods used for the Quarterly Operating Profits survey are available in the [Quality Methodology Information \(160.1 Kb Pdf\)](#) document.

Perpetual inventory method

Underlying estimates of capital stock and capital consumption are produced using the Perpetual Inventory Method. Further details are available in the '[Capital Stocks, Consumption of Fixed Capital 2014](#)', publication, which was published on 14 November 2014.

4. Quality

The net rate of return is defined as the ratio of the operating surplus compared to the capital employed, expressed as a percentage. The accuracy of the data in the numerator is likely to be high because the main component (profits) is benchmarked every six months to definitive, comprehensive, HMRC data. The accuracy of the data in this release for the denominator is likely to be more accurate than in previous releases due to the recent methodological changes.

The [Quality Methodology Information report \(118.8 Kb Pdf\)](#) for Profitability is available on the Office for National Statistics website.

The standard error of a series is a measure of the spread of possible estimates that might be obtained when taking a range of different samples of the same size. This provides a means of assessing the accuracy of the estimate: the lower the standard error, the more confident one can be that the estimate is close to the true value. Standard errors for quarterly profits, a key component of the numerator in the profitability data, are currently being developed and will be published in this bulletin in the near future.

Revisions

Table R1 accompanying this bulletin shows the revisions to the net rates of return made back to Quarter 1 (Jan to Mar) 2014. These revisions are consistent with the data published in the latest [Quarterly National Accounts Quarter 4 \(Oct to Dec\) 2014](#) statistical bulletin on 31 March 2015.

Estimates for the most recent quarters are provisional and, as usual, are subject to revisions in the light of updated source information consistent with the [National Accounts revisions policy](#). ONS has a web page dedicated to [revisions to economic statistics](#) which brings together ONS work on revisions analysis, links to relevant articles, revisions policies and key documentation from the Statistics Commission's report on revisions.

Further detailed information on all changes to National Accounts can be found here.

[National Accounts articles, Summary of ESA10 and BPM6 changes on Sector and Financial Accounts](#)

[United Kingdom National Accounts, the Blue Book, 2014 Edition](#)

[Capital Stock, Capital Consumption, Impact of the methodological changes to the estimation of capital stocks and consumption of fixed capital](#)

5. Relevant links

[Quarterly National Accounts](#)

[United Kingdom Economic Accounts](#)

6. Publication policy and Code of Practice for Official Statistics

Details of the policy governing the release of new data are available from the Media Relations Office. Also available is a [list of those given pre-publication access](#) to the contents of this release.

National Statistics are produced to high professional standards set out in the [Code of Practice for Official Statistics](#). They undergo regular quality assurance reviews to ensure that they meet customer needs. They are produced free from any political interference.

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7. Accessing data

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10. **Next publication:** 8 July 2015

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11. Details of the policy governing the release of new data are available by visiting www.statisticsauthority.gov.uk/assessment/code-of-practice/index.html or from the Media Relations Office email: media.relations@ons.gsi.gov.uk

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