Office for National Statistics

Statistical bulletin

Profitability of UK companies: July to September 2018

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

Contact:
David Summers
profitability@ons.gov.uk
+44 (0)1633 456602

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18 April 2019

Table of contents

1 . Main points

- Private non-financial corporations' (PNFCs') net rate of return was 12.6% in Quarter 3 (July to Sept) 2018, unchanged from the revised estimate for Quarter 2 (Apr to June) 2018.

- The net rate of return for manufacturing companies rose to 15.4% in Quarter 3 2018, up 1.1 percentage points from the previous quarter's net rate of return of 14.3%, after two consecutive periods of decline.

- Services companies' net rate of return was 17.1% in Quarter 3 2018, a decrease of 0.5 percentage points from the revised estimate of 17.6% in Quarter 2 2018.

- UK continental shelf (UKCS) companies' net rate of return increased to 18.9% in Quarter 3 2018, from a revised estimate of 13.5% in Quarter 2 2018; this follows the trend of increasing oil prices from $77.5 (US dollars) per barrel at the start of the quarter to $85 per barrel by the end.

2 . Things you need to know about this release

This bulletin provides estimates of the profitability of UK-based private non-financial corporations (PNFCs). PNFCs comprise UK continental shelf (UKCS) companies and other non-financial UK (non-UKCS) companies. Non-UKCS companies are further split into manufacturing companies, companies providing non-financial services and other industries (including construction, electricity and gas supply, agriculture, mining and quarrying).

UKCS companies engage in oil and natural gas exploration or extraction. This only includes companies operating on the UK continental shelf – the area where the UK claims mineral rights beyond the territorial waters. Owing to the nature of the industry, UKCS companies tend to be very capital-intensive and so require high levels of capital investment to operate. They also report high levels of depreciation of their fixed assets. For these reasons, the net rate of return for UKCS companies is not directly comparable with those for other sectors.

Revisions to the net rates of return for PNFCs have been made back to Quarter 1 (Jan to Mar) 2017 and are consistent with the Quarterly national accounts, published on 21 December 2018.

How do we measure profitability?

Net rate of return is used as the measurement of company profitability throughout this bulletin, except in the international comparisons section. The rate of return is calculated as the economic gain (profit) shown as a percentage of the capital used in production. "Net" refers to the rate of return after having accounted for the current value of capital consumed and capital stocks. Capital consumed refers to the decline in the current value in the stock of fixed assets (for example, due to depreciation). Gross rates of return are available in the Annex tables of this release.

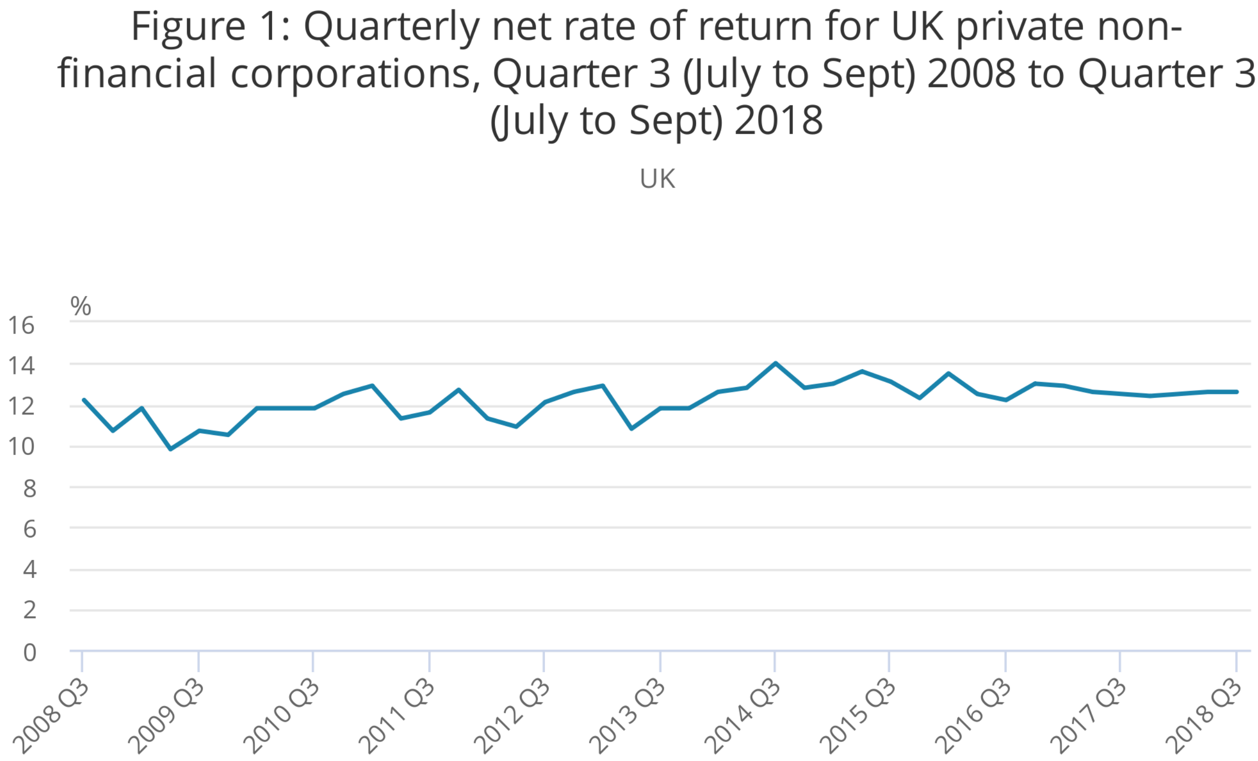
3 . Private non-financial corporations' net rate of return remained unchanged at 12.6%

The net rate of return for private non-financial corporations (PNFCs) remained unchanged at 12.6% in Quarter 3 (July to Sept) 2018 from the revised estimate of 12.6% in Quarter 2 (Apr to June) 2018 (Figure 1).

The zero growth in profitability is reflected in [Ernst and Young's Report]() of 68 issued profit warnings, showing an increase from the previous quarter, following a trend that has been present for the last six years. The Financial Times Stock Exchange (FTSE) sectors issuing the most profit warnings in Quarter 3 2018 were general retailers (8), travel and leisure (7), and support services (7). The most common reasons for the profit warnings were sales short of forecasts, increasing costs and competition.

Figure 1: Quarterly net rate of return for UK private non-financial corporations, Quarter 3 (July to Sept) 2008 to Quarter 3 (July to Sept) 2018

UK



Source: Office for National Statistics - Quarterly Operating Profits Survey

Notes:

1. Q1 refers to Quarter 1 (Jan to Mar), Q2 refers to Quarter 2 (Apr to June), Q3 refers to Quarter 3 (July to Sept) and Q4 refers to Quarter 4 (Oct to Dec).

4 . Manufacturing profitability rose after two consecutive periods of decline, whilst services fell from the previous quarter

Manufacturing companies

In Quarter 3 (July to Sept) 2018, the net rate of return for the manufacturing industries rose to 15.4% from the revised estimate of 14.3% in Quarter 2 (Apr to June) 2018 (Figure 2). This increase of 1.1 percentage points is the largest since Quarter 1 (Jan to Mar) 2017, following a similar trend as the Index of Production for the manufacturing industries, which rose by 0.6% compared with Quarter 2.

Services companies

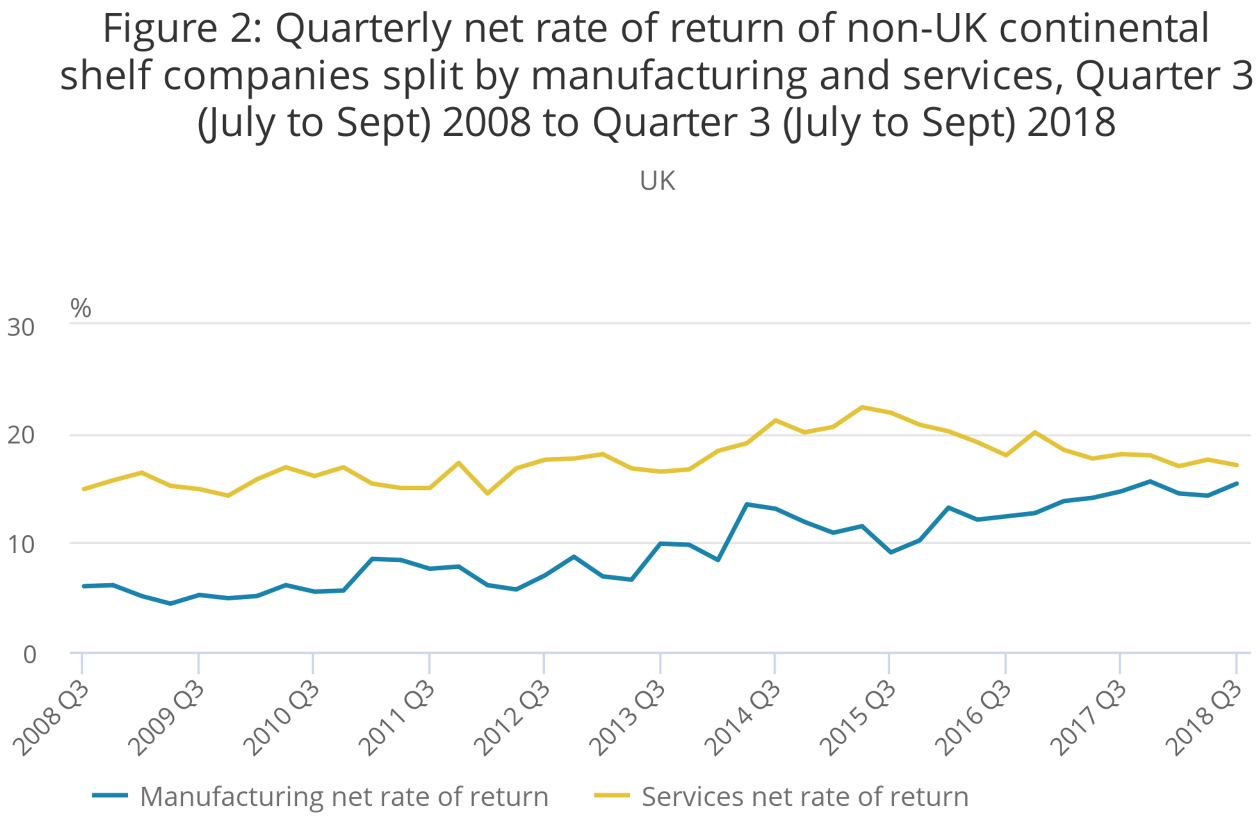
The net rate of return for the services industries fell from the revised estimate of 17.6% in Quarter 2 2018 to 17.1% in Quarter 3 2018 (Figure 2).

The Bank of England's Agents' summary report (PDF, 149KB) found that the boost of demand for seasonal items and activities was offset by the fall in demand for big ticket items such as new cars, white goods and homeware. The report also suggests business services saw a slowdown in growth after a period of elevated demand as corporate financing and mergers and acquisition activity declined.

The Ernst and Young's Report notes that the majority of profit warnings in this quarter were coming from the consumer side of the economy, a seven-year high in general retailers' profit warnings. This was not only due to the summer heatwave but growing domestic and global uncertainty has meant that investors have been hesitant in spending, reflected by a record fall in share prices.

Figure 2: Quarterly net rate of return of non-UK continental shelf companies split by manufacturing and services, Quarter 3 (July to Sept) 2008 to Quarter 3 (July to Sept) 2018

UK



Source: Office for National Statistics - Quarterly Operating Profits Survey

Notes:

1. Q1 refers to Quarter 1 (Jan to Mar), Q2 refers to Quarter 2 (Apr to June), Q3 refers to Quarter 3 (July to Sept) and Q4 refers to Quarter 4 (Oct to Dec).

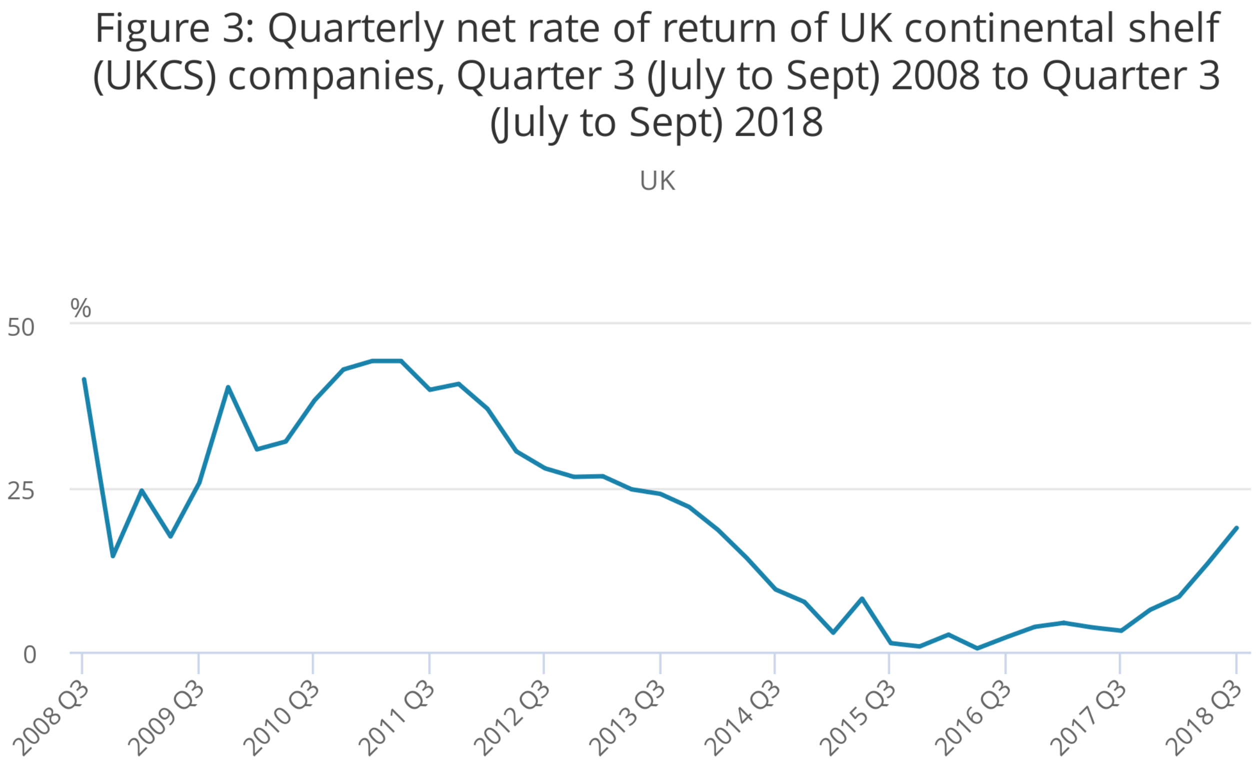
5 . UK continental shelf companies sustained strong growth as oil prices continued to rise

The estimated net rate of return for UK continental shelf (UKCS) companies in Quarter 3 (July to Sept) 2018 was 18.9% (Figure 3). This was up 5.4 percentage points from the revised estimate of 13.5% in Quarter 2 (Apr to June) 2018. It is the highest rate of return since Quarter 4 (Oct to Dec) 2013.

Growing global demand and the Organisation of Petroleum Exporting Countries (OPEC) restricting supply saw the price of oil rise from $77.5 (US dollars) per barrel at the start of the quarter to $85 per barrel by the end. This was the largest quarter-on-quarter growth since Quarter 3 2010, when similarly the price of oil rose from $74.5 (US dollars) per barrel at the beginning of the quarter to $84 per barrel at the end.

Figure 3: Quarterly net rate of return of UK continental shelf (UKCS) companies, Quarter 3 (July to Sept) 2008 to Quarter 3 (July to Sept) 2018

UK



Source: Office for National Statistics - Quarterly Operating Profits Survey

Notes:

1. Q1 refers to Quarter 1 (Jan to Mar), Q2 refers to Quarter 2 (Apr to June), Q3 refers to Quarter 3 (July to Sept) and Q4 refers to Quarter 4 (Oct to Dec).

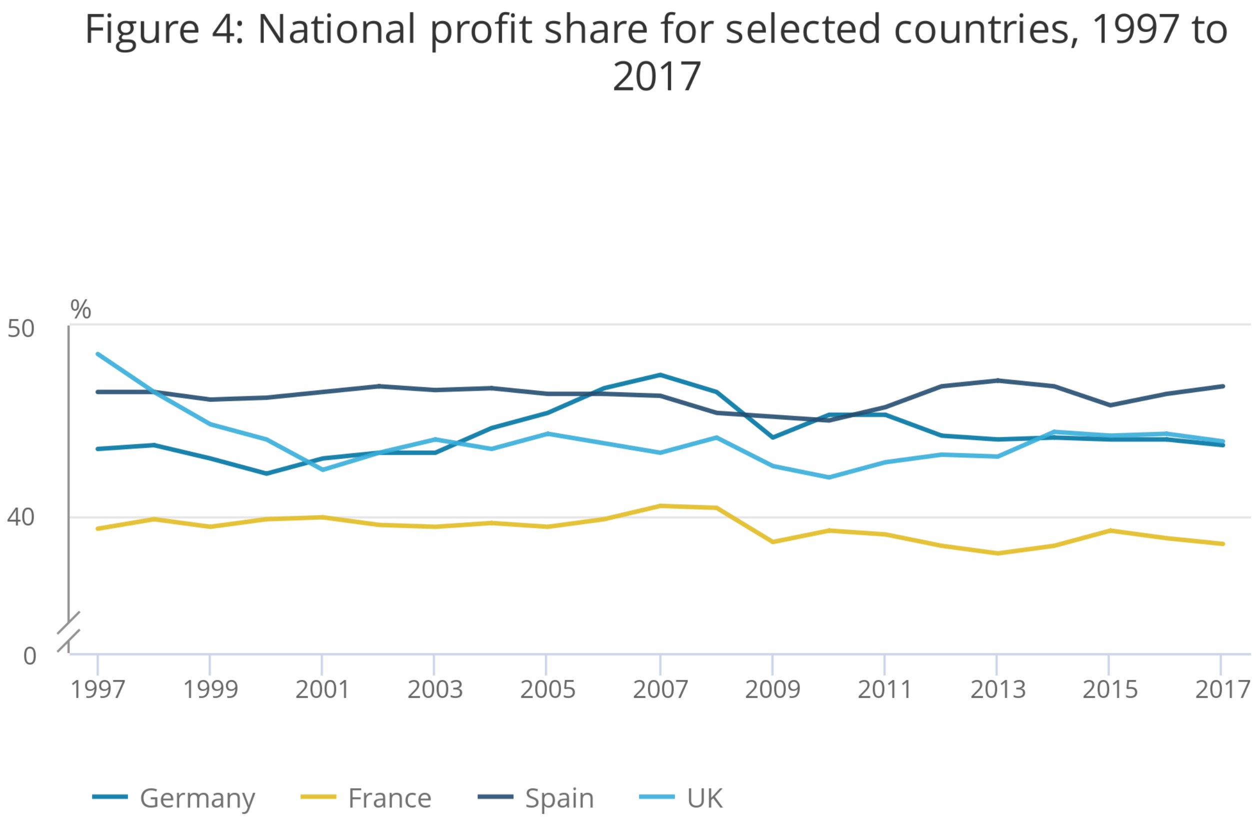
6 . How does UK profitability compare internationally?

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

It is possible to compare the aggregated national profit share, defined as gross operating surplus (GOS) plus mixed income (income made by the self-employed and other non-incorporated businesses) divided by gross value added (GVA) on a European System of Accounts 2010: ESA 2010 (PDF, 6.4MB) 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 using labour and capital. GOS is the income earned from capital. The national profit-share measure includes the activity of other profit-making sectors, such as financial corporations and public corporations, whilst the rest of this bulletin refers to the activities of private non-financial corporations (PNFCs) only.

International data on an ESA 2010 basis are only available at the aggregate national level, shown for selected countries (Figure 4).

Figure 4: National profit share for selected countries, 1997 to 2017



Source: Office for National Statistics - Quarterly Operating Profits Survey, Eurostat

Notes:

1. Calendar years are used for Figure 4.

While the UK, France and Germany experienced a decline in national profit share in 2017, Spain saw a second consecutive annual increase, rising by 0.4% to 46.8%. The UK saw the largest fall in profit share of the countries shown, as it fell to 43.9%, down 0.4% on 2016. This coincides with a period of slower growth in the UK, where gross domestic product (GDP) grew by 1.7% in 2017, which was 0.7% lower than growth experienced by the European Union (Source: Eurostat Tables).

7 . Links to related statistics

The gross operating surplus (GOS) of private non-financial corporations (PNFCs) is a component of the income approach to measuring gross domestic product (GDP). GOS consists of gross trading profits, plus income from rental of buildings, less inventory holding gains (changes in inventory value caused by price). See the Quarterly national accounts for a detailed breakdown of the components of GDP, as well as main sector accounts aggregates.

The Quarterly sector accounts includes estimates of national production, income and expenditure, UK Sector Accounts and the UK Balance of Payments.

We, like all government departments, ensure all of our outputs meet accessibility guidelines. As a result, from the Quarter 4 (Oct to Dec) 2017 (29 March 2018) release onwards we have no longer published a PDF file of the UK Economic Accounts (UKEA). The data contained in the current PDF file continue to be available within the UKEA datasets that are currently published.

8 . What's changed in this release?

Revisions to the net rates of return for private non-financial corporations (PNFCs) have been made back to Quarter 1 (Jan to Mar) 2017. This is consistent with the quarterly national accounts for Quarter 3 (July to Sept) 2018, published on 21 December 2018.

For more information, please refer to revisions to economic statistics, which brings together our work on revisions analysis, links to relevant documentation and revisions policies.

The estimates quoted in this international comparison section are the latest available estimates published by the respective bodies (referenced) at the time of preparation of this statistical bulletin and may subsequently have been revised. The data are sourced from Eurostat.

We welcome any feedback and are particularly interested in knowing how you use the data to inform your work. Contact us via email at profitability@ons.gov.uk or telephone David Summers on +44 (0)1633 456602.

9 . Quality and methodology

The Profitability of UK companies statistical bulletin reports the estimates for net rate of return on capital employed for UK private non-financial corporations (PNFCs) related to their UK operations.

The Profitability of UK companies and Quarterly Operating Profits Survey Quality and Methodology Information reports contain important information on:

- the strengths and limitations of the data and how they compare with related data
- uses and users of the data
- how the output was created
- the quality of the output including the accuracy of the data

Revisions

Revisions to rates of return have been incorporated in this release from Quarter 1 (Jan to Mar) 2017. The revisions to the time series are presented in Table R1 accompanying this bulletin.

For more information, please refer to our web page dedicated to revisions to economic statistics, which brings together our work on revisions analysis, links to relevant documentation and revisions policies.

The estimates quoted in this international comparison section are the latest available estimates published by the respective bodies (referenced) at the time of preparation of this statistical bulletin and may subsequently have been revised. The data are sourced from Eurostat.

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 and capital consumption QMI.

10 . Acknowledgements

The author, David Summers, would like to express his thanks to the following colleagues at Office for National Statistics for their contributions to this work: June Pupic and James O’Connor.