



*cutting through complexity*

# Tech Monitor

A most up-to-date source  
of UK tech sector data and  
analysis each quarter

Compiled for KPMG by Markit  
April 2014

# Tech Monitor/UK

/ flip page



// Recent falls in share prices of technology stocks have led some to question the health of the tech sector but all the data in this report point to a UK tech sector that is in rude health, and increasingly optimistic in its outlook on business activity and recruitment plans. //

Tudor Aw, Head of Technology at KPMG,

**A snapshot report for the tech industry,** giving an informative overview of market performance and expert insight on trends and outlook.







04 Overview

06 Tech growth

10 Employment trends

12 Economic context

14 Tech outlook

16 Methodology notes

# Tech sector job hiring plans hit post-crisis peak in Q1, with growth close to a 10-year high

## OVERVIEW

### Key points from the Q1 2014 data:



UK tech sector recorded **another steep rise in business activity**, with growth only slightly slower than the ten-year high seen in Q4 2013.

Current **job hiring** by tech companies is **close to its strongest for three years**, and faster than the UK private sector average.

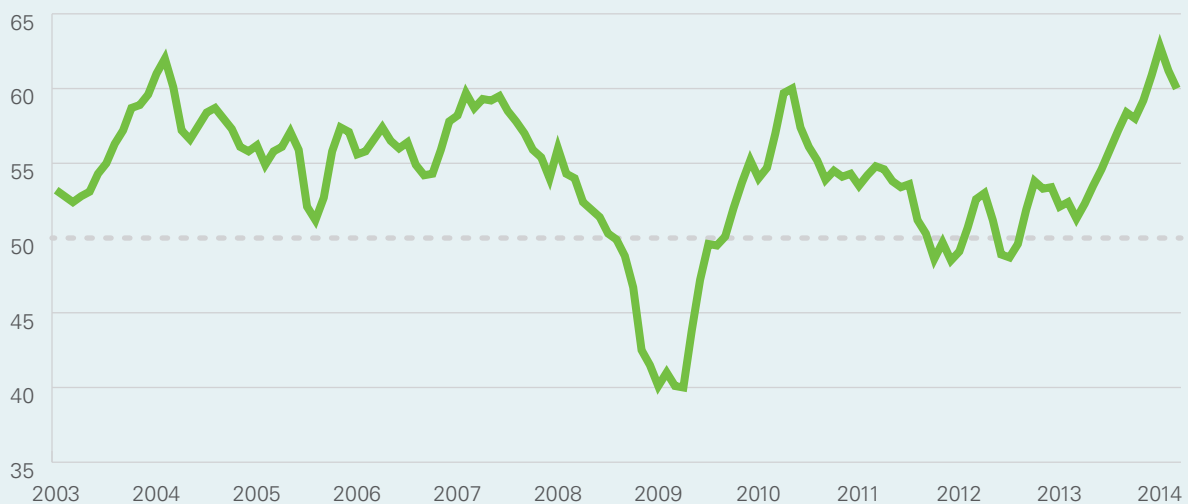
Around **58% of tech companies** expect their **business activity to rise** over the year ahead, compared with only 4% that expect a decline.

Almost **half of tech firms (49%)** intend to **recruit more staff** over the next 12 months, while only 11% anticipate a reduction.

At **+38.6%**, the net balance of tech companies expecting a **rise in employment is the highest since this series began in October 2009**.



**Tech PMI Business Activity Index, 50 = no change**



**Commenting on the latest Tech Monitor UK results, Tudor Aw, Head of Technology at KPMG, said:**

// Our data shows the positive impact the sector has on the UK's economic performance as a whole and the important role UK tech companies up and down the country play in the burgeoning recovery. It is time the sector gets the recognition and support it deserves. There are some fantastic advocates in government and business for the UK's buzzing start-up scene but we must not neglect the wider tech sector. We should ensure that the sector as a whole gets the profile and support that it needs such as focused government policies that help develop and encourage education in STEM subjects, and ease access to tech talent on a global basis.

With the increase in IPO activity, I would like to see the strong performance of UK tech companies translate to a mainstream technology company floating in London to help boost the sector and cement the UK's position on the map of global tech hotspots.



# Tech growth: Business activity growth moderates from 10-year high

## TECH GROWTH

Tech Monitor UK uses a specially selected panel of tech sector executives within the Markit UK Purchasing Managers' Index® (PMI®) surveys, to provide a unique and up-to-date assessment of the sector's economic performance. Growth and jobs trends are benchmarked against Global PMI® series and other key economic indicators.

### Main findings in Q1 2014\*

KPMG/Markit Tech Monitor UK data indicates that the tech sector remained on a strong growth footing at the end of Q1 2014, with both business activity and new work rising more quickly than has been seen over much of the past ten years.

Although output growth moderated in comparison with that recorded at the end of Q4 2013, the latest expansion was stronger than for the UK private sector as a whole, highlighting that tech companies continue to play a pivotal role in the domestic economic revival.

The headline index measuring UK tech sector business activity posted 60.0 at the end of Q1, down slightly from 60.9 in Q4 2013 but well above the 50.0 growth threshold. Higher levels of UK tech sector business activity have been recorded since

Q3 2012, and the current pace of expansion is close to the peak growth rates seen prior to the global financial crisis in 2008/09.

A steep pace of tech sector growth over the first quarter of 2014 was supported by a further sharp expansion of new order books.

Although new business growth has also lost some momentum since the turn of the year, the latest index reading still indicates an improvement in demand largely unsurpassed since the series began in 2003. Moreover, sustained rises in new orders and employment at the end of Q1 2014 provide confidence that the tech sector can maintain its historically strong pace of activity growth in the coming months (see Sections 2 and 4 for full details on employment trends).

70.0

60.0

50.0 neutral mark

40.0

30.0

20.0

10.0

00.0

Source: Markit/KPMG.

\*Index numbers vary between 0 and 100, with levels of 50 signalling no-change from the previous month. Readings above 50 signal an increase since the previous month, whilst postings below 50 indicate a decrease. The greater the divergence from 50, the greater the rate of change signalled by the reading.

Methodology notes can be found in section 6.

### Tech sector demand patterns

An improved domestic economic outlook, increased investment spending and buoyant client demand were all key factors behind the latest rise in tech sector business activity, according to survey respondents.

At 60.7, the index measuring new orders in the tech sector was well above the neutral 50.0 mark at the end of Q1 2014. The latest reading signalled a faster pace of new business expansion than was experienced across the UK private sector as a whole, as the equivalent index dipped to 58.2 during the latest survey period.

### Tech PMI Business Activity Index, 50 = no change



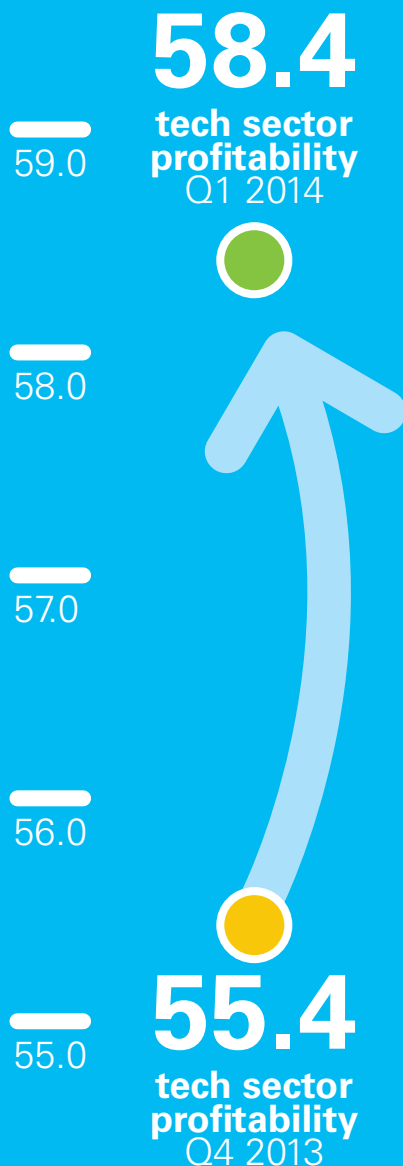
### Tech PMI New Orders Index, 50 = no change





# Tech growth: Profits supported by slowest cost inflation since late-2009

## TECH GROWTH



### Tech sector demand patterns cont...

Q1 2014 data indicated that tech sector firms continue to experience potential capacity pressures, with backlogs of work rising at rates unprecedented since the series began in 2003.

At 53.6, the index measuring backlogs of work signalled another solid rise in unfinished business across the tech sector at the end of the first quarter. This sustained increase in outstanding business volumes provides a further indication that companies will look to expand their operating capacity and boost payroll numbers over the coming months.

### Selling prices increase as demand rises

Stronger client demand and increased volumes of unfinished work placed upward pressure on prices charged by some tech companies.

At 51.4, the index measuring prices charged across the UK tech sector rose back above the 50.0 no-change mark, after posting 49.7 at the end of last year.

Although the latest survey signalled only a moderate rise in output charges, it was the quickest pace of inflation for just over three years. Moreover, it contrasted with marginal price cuts across the tech sector in the final quarter of 2013.

### Profitability improves as cost pressures ease and new business rises

Tech sector firms benefitted from a combination of higher selling prices, weakening cost inflation and rising new business volumes during the first quarter of 2014. This in turn supported a strong pace of profitability growth, according to the latest survey data.

The index measuring average input costs faced by tech sector firms posted 53.9 at the end of Q1. This was down from 56.2 at the end of 2013 and signalled the slowest rate of input cost inflation since late-2009.

At 58.4, the index measuring tech sector profitability was up from 55.4 at the end of 2013 and well above the 50.0 no-change value. The latest reading suggested that profitability growth is close to the pre-financial crisis peak seen in 2007.



**Tech PMI Backlogs of Work Index, 50 = no change****Tech PMI Input Price Index, 50 = no change****Tech PMI Profitability Index, 50 = no change**

Source: Markit/KPMG.

\*Index numbers vary between 0 and 100, with levels of 50 signalling no-change from the previous month. Readings above 50 signal an increase since the previous month, whilst postings below 50 indicate a decrease. The greater the divergence from 50, the greater the rate of change signalled by the reading.

Methodology notes can be found in section 6.

# Employment trends: Job hiring by tech firms is close to a three-year high

## EMPLOYMENT TRENDS

In this section of Tech Monitor UK we compare tech sector employment trends against equivalent indices from Markit's UK *Purchasing Managers' Index® (PMI®)* surveys, providing a timely barometer of tech hiring patterns in the context of overall UK private sector labour market developments.

### The main findings for Q1 2014\* are:

UK tech firms reported a further strong rise in employment at the start of 2014. Moreover, the latest KPMG/ Markit Tech Monitor UK data indicates that the pace of job hiring across the sector is back above the UK-wide average.

At the end of the first quarter, the index measuring tech sector employment hit 56.0, close to a three-year high and well above the figure recorded at the end of 2013 (54.1). Meanwhile, the equivalent index for overall UK private sector employment came in at 53.7, signalling the slowest rate of jobs growth since the end of Q3 2013.

Tech firms generally reported that additional staff had been hired in line with rising business activity requirements and ongoing company expansion plans. Others indicated that recruitment had been undertaken to support work on new product development.

Employment trends at tech firms have been stronger than the general UK pattern over most of the past seven years. While this gap narrowed as the wider economy started to experience faster growth towards the end of 2013, the latest figures suggest that the tech sector has remained a key driver of overall job creation so far this year.

Another factor supporting tech employment at the start of 2014 is rising backlogs of work. Outstanding business has increased continuously since last summer, with the rate of backlog accumulation picking up at the start of 2014 to around its fastest pace since the series began over ten years ago.

**54.1**  
tech sector  
employment  
end of 2013

**56.0**  
tech sector  
employment  
start of 2014

2013

2014

PMI Employment Index, 50 = no change



### Company size breakdown

The latest Tech Monitor UK survey indicates resilient growth of staffing levels among smaller tech firms (those with fewer than 50 employees), but the pace of job creation remains slower than the average for all tech companies.

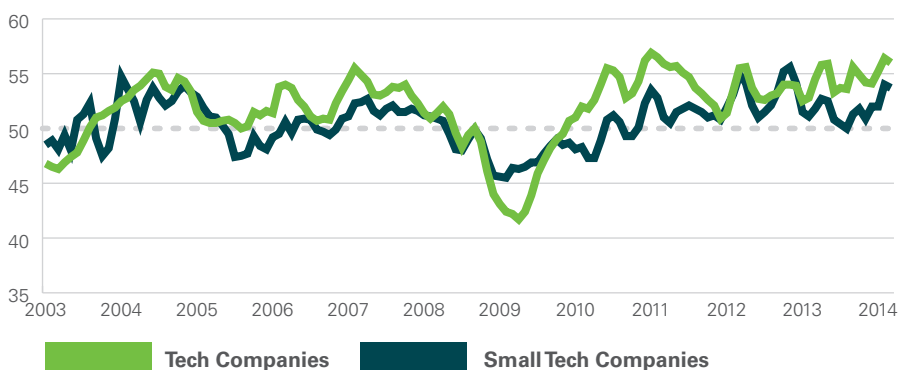
The index measuring employment at small tech firms registered 53.7 at the end of the first quarter. Although well above the 50.0 no-change value, the latest reading was below the equivalent index for all tech companies (56.0). This trend has been observed throughout much of the past four years.

Source: Markit/KPMG.

\*Index numbers vary between 0 and 100, with levels of 50 signalling no-change from the previous month. Readings above 50 signal an increase since the previous month, whilst postings below 50 indicate a decrease. The greater the divergence from 50, the greater the rate of change signalled by the reading.

Methodology notes can be found in section 6.

PMI Employment Index, 50 = no change





# Economic context: Tech growth helped by better economic conditions

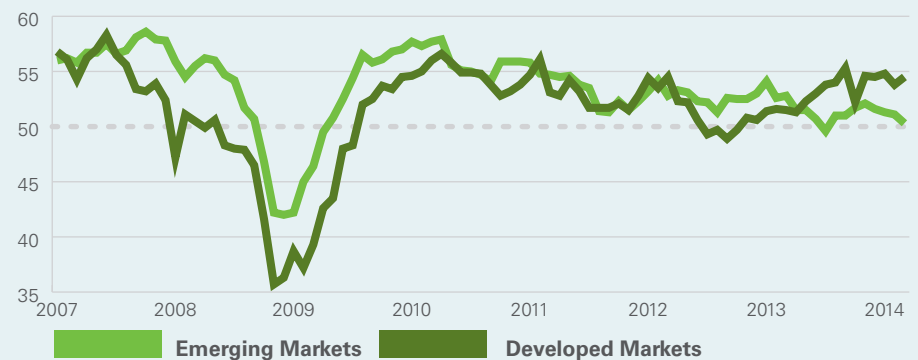
## ECONOMIC CONTEXT

This section examines recent economic developments and how they relate to the UK tech sector business conditions.

**2.9%**  
IMF forecast for  
UK GDP growth  
in 2014

### Developed and emerging markets growth

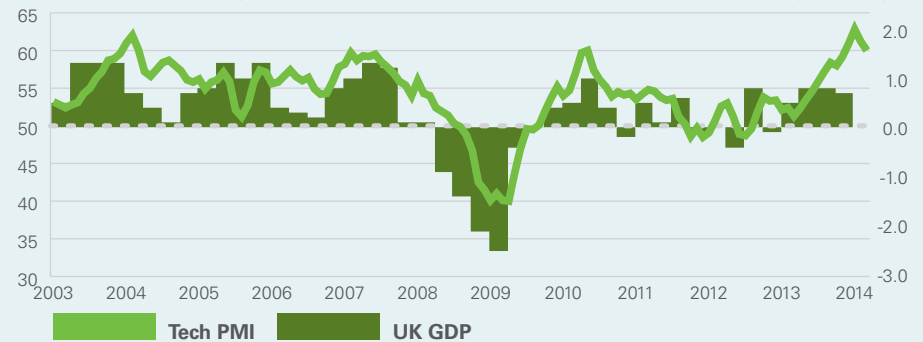
PMI Output Index (manufacturing and services), 50.0 = no change



### UK tech business activity mapped against UK GDP

Tech PMI, 50 = no change

UK GDP, q/q % change



### UK tech business activity mapped against the NASDAQ

Tech PMI, 50 = no change

NASDAQ yoy % change



#### Sources:

Global PMI® data sourced from JPMorgan/Markit.

UK GDP data sourced from the Office for National Statistics. At the time of writing, figures were available up to Q4 2013.

Stock market data sourced from Reuters EcoWin.



### Key developments in Q1 2014

Domestic economic conditions continued to strengthen in the first quarter of 2014, prompting the International Monetary Fund to further upgrade its forecasts for the UK economy.

The IMF's new forecast of 2.9% UK GDP growth in 2014 is the highest of all G7 nations and, given the strength of the survey data, the tech sector is well positioned to outperform this benchmark.

UK growth forecasts were also upgraded by the Office for Budget Responsibility (OBR) in the first quarter, with business investment expected to provide a particularly strong contribution (+8.0%). The OBR anticipate that unemployment will decline further in 2014, which will generate tailwinds to UK tech sector growth from both consumer and business spending this year.

The outlook for household purchasing power is starting to become more positive, reflecting low consumer price inflation and rising wage rates. This will provide a boost to consumer demand and, together with greater business spending, this should help offset any pressures on margins from tighter labour market conditions.

### Equity market correction

Following a rapid rise in 2013, the NASDAQ composite index, the benchmark for US technology stocks, has fallen back sharply in recent weeks, partly explained by analysts as a rotation out of growth stocks amid a shift in investor sentiment towards higher cash flow yield.

Tech Monitor UK, which measures actual changes in output and employment, shows a reassuringly positive sector performance over the first quarter. While historically strongly correlated with the NASDAQ, the survey can also provide a timely indication of broader market trends and perhaps be seen as a more stable bellwether of underlying business conditions among established tech sector companies in the UK.

### Global economy expands again in early 2014

UK tech firms can derive confidence from continued improvements in developed markets, especially Western Europe and the US. Better economic conditions are helping to offset the struggles of some emerging markets, where growth has tailed off to post-crisis lows.



# Tech outlook: Hiring intentions hit post-crisis peak, but growth forecasts slip

## TECH OUTLOOK

This section contains analysis of our survey data on UK tech firms' business expectations for 2014. Figures for future business activity are drawn from monthly PMI® surveys; those on employment and capex are based on Markit's tri-annual Global Business Outlook survey.

### The main findings for Q1 2014\* are:

UK tech companies continue to anticipate growth of business activity over the coming 12 months. However, the degree of confidence is weaker than that registered at the end of 2013.

A rise in activity is predicted by 58.4% of UK tech companies, compared with 3.9% that expect a decline. The resulting net balance is +54.4%, down from a reading of +56.9% at the end of Q4 2013.

Although tech companies are marginally more positive than those across all UK industry sectors, the gap has narrowed considerably in the latest quarter. At +54.0%, the index for all UK firms is up from +48.1% at the end of 2013.

Tech firms expect output growth during the coming year to be supported by improved marketing, new distribution channels, recent new product launches and stronger consumer confidence. There were also some reports from companies that past investments were starting to boost revenues.

### Brighter employment prospects

In contrast to the softening of activity expectations, tech firms' confidence regarding employment has risen since late-2013.

The latest survey, which was conducted in February 2014, showed that almost half of UK tech companies (49.1%) plan to raise employment over the next 12 months, compared with 10.5% that expect to cut jobs.

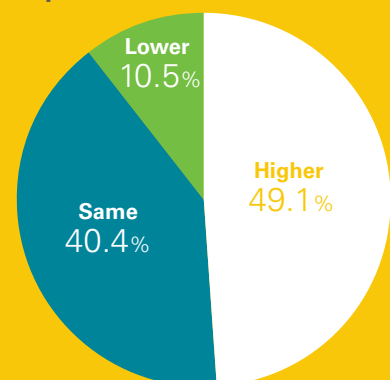
The resulting net balance is +38.6%, up from +36.8% when the previous outlook survey was conducted in October 2013. The latest reading is the highest since data was first available in late 2009.

Tech companies' hiring intentions are slightly stronger than the UK-wide average. The net balance for the latter is +35.7%, also a series-record high.

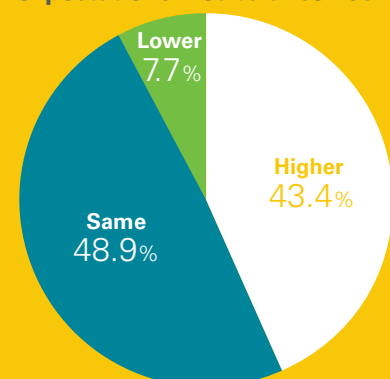
### Markit Business Outlook Survey February 2014

"Do you expect employment at your business to be higher, the same or lower in 12 months' time than the current levels?"

#### Tech companies employment expectations: net balance +38.6%



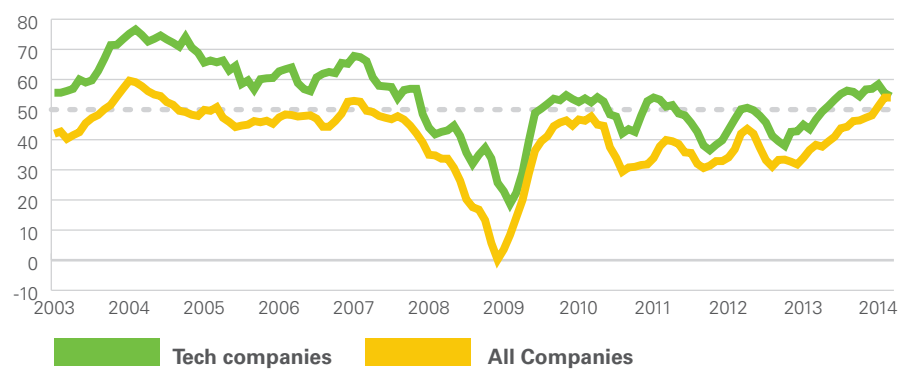
#### All companies employment expectations: net balance +35.7%



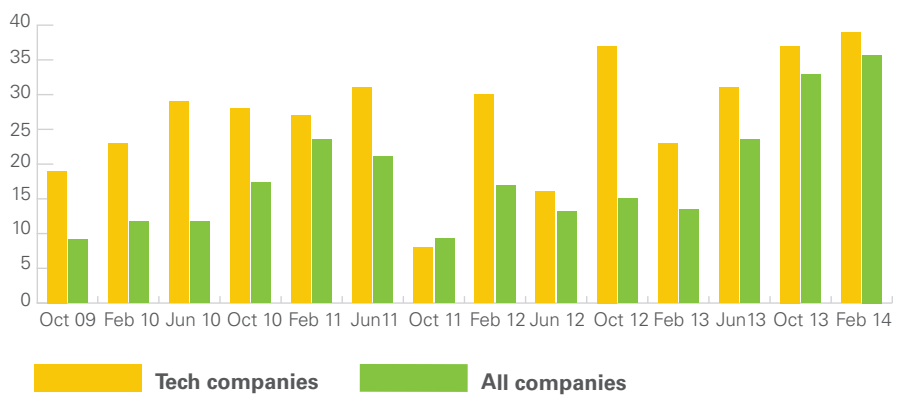




### Business activity expectations, (3-month average) net balance %



### Job hiring intentions, net balance %



Source: Markit/KPMG.

\* Methodology notes can be found in section 6.

# Tech Monitor UK: Methodology notes

## METHODOLOGY NOTES

### **UK Tech Sector Purchasing Managers' Index® (PMI®) survey data**

UK tech sector PMI data is derived from a representative sub-category of approximately 150 tech companies within Markit's regular PMI® surveys of UK manufacturers and service providers. Tech is defined in this report as technology software, technology services and manufacturing of technology equipment. All figures are seasonally adjusted and smoothed using a three-month moving average, to better highlight underlying trends in the data.

### **UK Tech Sector Business Outlook Survey data**

Business activity expectations data is drawn from the monthly PMI® surveys question on companies' expectations for their activity/output over the next 12 months. Prior to July 2012, only service sector companies were asked this question.

Employment expectations data is based on responses from UK services and manufacturing firms participating in Markit's tri-annual Global Business Outlook survey, which is based on the same panel of companies as the PMI® surveys.

### **'Technology Sector' industry groups:**

- Software publishing (SIC 582).
- Computer programming, consultancy and related activities (SIC 620).
- Data processing, hosting and related activities; web portals (SIC 631).
- Manufacture of computer, electronic and optical products (SIC 26).
- Manufacture of electrical equipment (SIC 27)



For more methodology details,  
see the October 2013  
**Tech Monitor UK report.**

**Tech Monitor UK**  
28 January 2014

**UK tech sector records best growth performance for almost a decade**

Almost 44% of UK tech firms plan to hire more staff over the next 12 months, while 7% expect to reduce their headcount, according to the latest Tech Monitor UK report. The report also shows that 10% of tech firms plan to increase their sales over the next 12 months, while 10% expect to reduce their sales. The report also shows that 10% of tech firms plan to increase their sales over the next 12 months, while 10% expect to reduce their sales.

**Commenting on the latest Tech Monitor UK results, Tudor Ayo, Head of Technology at KPMG, said:**

"These figures prove once more that the UK tech sector is going from strength to strength. The last quarter of 2013 saw the sector's best growth performance in almost a decade, with a steady increase in tech companies, a rise in new orders and an increase in profitability despite higher costs."

**Key points from the Q4 2013 data:**

- Strongest rise in UK tech sector business activity since early 2014.
- UK tech companies report fastest improvement in profitability for six years.
- Solid rise of tech sector job creation maintained at the end of 2013.

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### **Tudor Aw**

Partner, Head of Technology at KPMG

Tel: +44 (0) 20 7694 1265

tudor.aw@KPMG.co.uk

[\*\*in\*\*](#) contact Alwin on [\*\*Linkedin\*\*](#)

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Oliver Marketing for KPMG | OM016702A | April 2014