

Statistical bulletin

# Profitability of UK companies: October to December 2019

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

- The net rate of return for private non-financial corporations (PNFCs) stood at 9.3% in Quarter 4 (Oct to Dec) 2019, down from the revised estimate of 9.8% for Quarter 3 (July to Sept) 2019.
- The net rate of return for manufacturing companies fell to 9.4% in Quarter 4 2019, down 1.5 percentage points from the previous quarter's revised net rate of return of 10.9%.
- The net rate of return for services companies stood at 14.9% in Quarter 4 2019, a decrease of 0.2 percentage points from the revised estimate of 15.1% in Quarter 3 2019.
- The net rate of return for [UK continental shelf \(UKCS\)](#) companies fell to 1.8% in Quarter 4 2019, down from the revised estimate of 2.4% in Quarter 3 2019.

## 2 . Private non-financial corporations' net rate of return

The net rate of return for private non-financial corporations (PNFCs) fell to 9.3% in Quarter 4 (Oct to Dec) 2019 from the revised estimate of 9.8% in Quarter 3 (July to Sept) 2019 (Figure 1).

The net rate of return fell for the fifth consecutive quarter since its most recent peak of 10.5% in Quarter 3 2018. In Quarter 4 2019, a rise in the net capital employed coupled with a fall in the net operating surplus led to the downward movement in the net rate of return. The rise in net capital employed has been the cause of the continued fall since Quarter 3 2018.

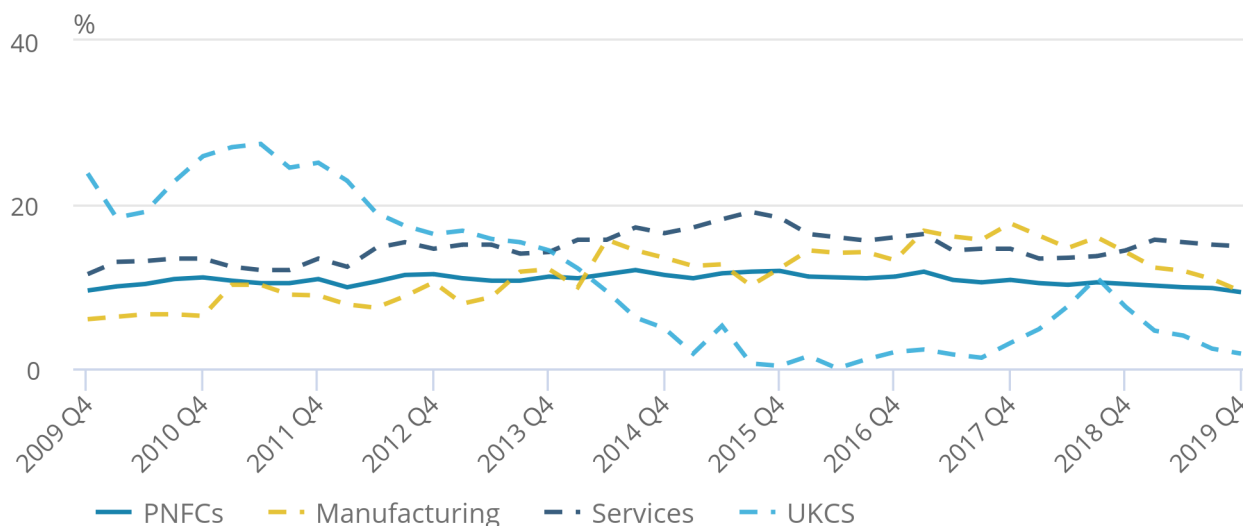
[Ernst & Young](#) reported the number of profit warnings in Quarter 4 2019 at 78. For Quarter 4 2019, 10 warnings were issued by industrial support services businesses and five by industrial metals and mining companies. On an annual basis, there were 313 profit warnings issued during 2019, a 9% increase on 2018. This is reflected in the annual decrease in the net rate of return from 10.3% (2018) to 9.8%.

**Figure 1: Quarterly net rate of return for private non-financial corporations has fallen for the past five quarters**

Net rate of return of UK private non-financial corporations, Quarter 4 (Oct to Dec) 2009 to Quarter 4 (Oct to Dec) 2019

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Net rate of return of UK private non-financial corporations, Quarter 4 (Oct to Dec) 2009 to Quarter 4 (Oct to Dec) 2019



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).

### 3 . Manufacturing and services

In Quarter 4 (Oct to Dec) 2019, the net rate of return for manufacturing companies fell to 9.4% from the revised estimate of 10.9% in Quarter 3 (July to Sept) 2019 (Figure 2). The net rate of return has now fallen for five consecutive quarters. This decline in the net rate of return is primarily caused by a fall in the net operating surplus, but there has also been a steady rise in the net capital employed.

The [British Chambers of Commerce \(BCC\)](#) reported that indicators in the manufacturing industry remain very weak by historical standards, showing export orders are negative for two consecutive quarters for the first time in around a decade.

The [Bank of England summary report for Quarter 4 2019](#) reports that manufacturing output fell, reflecting weaker domestic and global demand. It identifies Brexit uncertainty and subdued investment as the causes of this fall. However, it reported growth for premium food producers and evidence of a rise in domestic production to replace imports.

The [Purchasing Managers' Index](#) reported a value of 47.5 in December 2019, where a figure below 50 represents contraction. It goes on to say that production experienced its largest decline since July 2012 and incoming new work decreased for the eighth consecutive month.

The net rate of return for services companies in Quarter 4 2019 fell to 14.9% from a revised estimate in Quarter 3 2019 of 15.1% (Figure 2). There was a consistent fall in the net rate of return throughout 2019. Although there were quarterly variations in net operating surplus throughout the year, the net capital employed rose consistently and is the primary cause of the fall.

The decline in Quarter 4 2019 was caused by a fall in profits by the industry sub-group covering "real estate activities"; "professional, scientific and technical activities"; and "administrative and support service activities". This was partially offset by a strong quarter from "wholesale and retail trade; repair of motor vehicles and motorcycles" and "accommodation and food service activities".

The [BCC Quarterly Economic Survey for Quarter 4 2019](#) found that indicators for services industries worsened and remained well below their historical average.

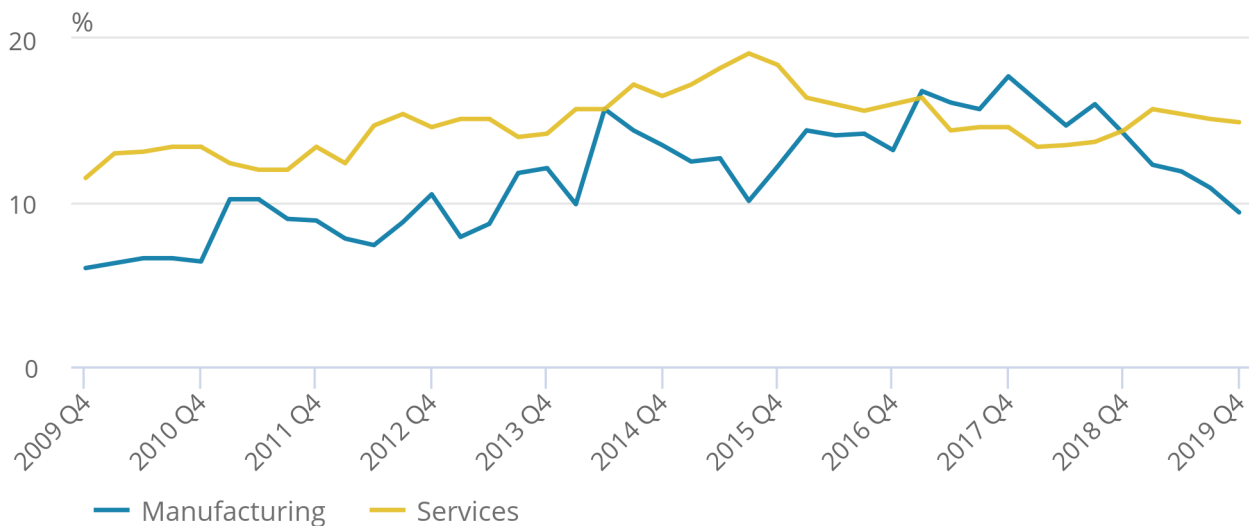
The [Bank of England summary report for Quarter 4 2019](#) reported that growth in business services weakened with uncertainty about Brexit and the General Election weighing on activity. Growth in consumption was muted as sales of major household goods, and new cars remained weak.

## Figure 2: Services have experienced a higher net rate of return than manufacturing for the past five quarters

Net rate of return of UK non-continental shelf companies split by manufacturing and services, Quarter 4 (Oct to Dec) 2009 to Quarter 4 (Oct to Dec) 2019

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Source: Office for National Statistics – Quarterly Operating Profits Survey

#### Notes:

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## 4 . UK continental shelf companies

The estimated net rate of return for UK continental shelf (UKCS) companies in Quarter 4 (Oct to Dec) 2019 fell to 1.8% (Figure 3). This was down 0.6 percentage points from the revised estimate of 2.4% in Quarter 3 (July to Sept) 2019. This is the fifth consecutive quarter of falling profitability.

When comparing with Quarter 4 2018, the wholesale gas prices fell markedly with the price per therm almost halving since Quarter 4 2018 (64.7p to 32.5p). This resulted in a sharp decrease in quarterly turnover against the same quarter last year.

As reported by [The Guardian](#), the fall in gas prices was caused primarily by very high imports from the US, Russia and Qatar. This record number of seabound cargoes arriving on UK shores kept gas market prices below 40p per therm.

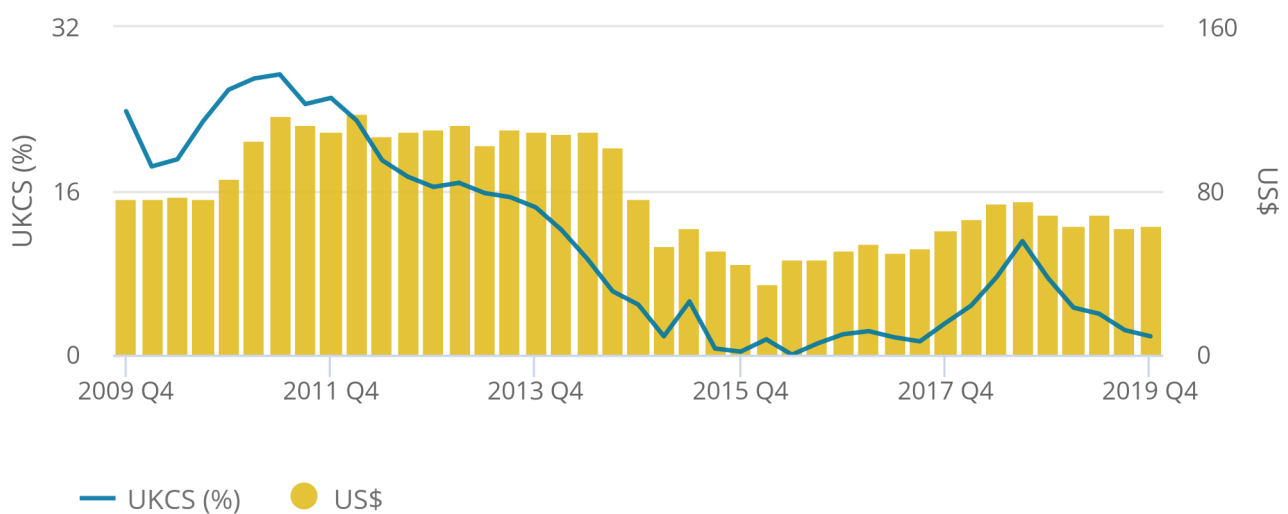
As can be seen in Figure 3, the UKCS companies' net rate of return follows a similar trend to the Brent Crude price of oil. However, the average price of Brent crude oil increased in Quarter 4 2019 to \$63.3 from a Quarter 3 2019 position of \$61.9. Therefore, the drop in the rate of return was primarily because of the fall in prices of wholesale gas.

**Figure 3: UK continental shelf companies' profitability follows a similar trend to the price of Brent Crude Oil**

Net rate of return of UK continental shelf companies and the average price of Brent Crude Oil in American dollars, Quarter 4 (Oct to Dec) 2009 to Quarter 4 (Oct to Dec) 2019

Figure 3: UK continental shelf companies' profitability follows a similar trend to the price of Brent Crude Oil

Net rate of return of UK continental shelf companies and the average price of Brent Crude Oil in American dollars, Quarter 4 (Oct to Dec) 2009 to Quarter 4 (Oct to Dec) 2019



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. International comparisons

Users should note that international comparisons of profitability can be problematic, as we discuss in the [Strengths and limitations section](#).

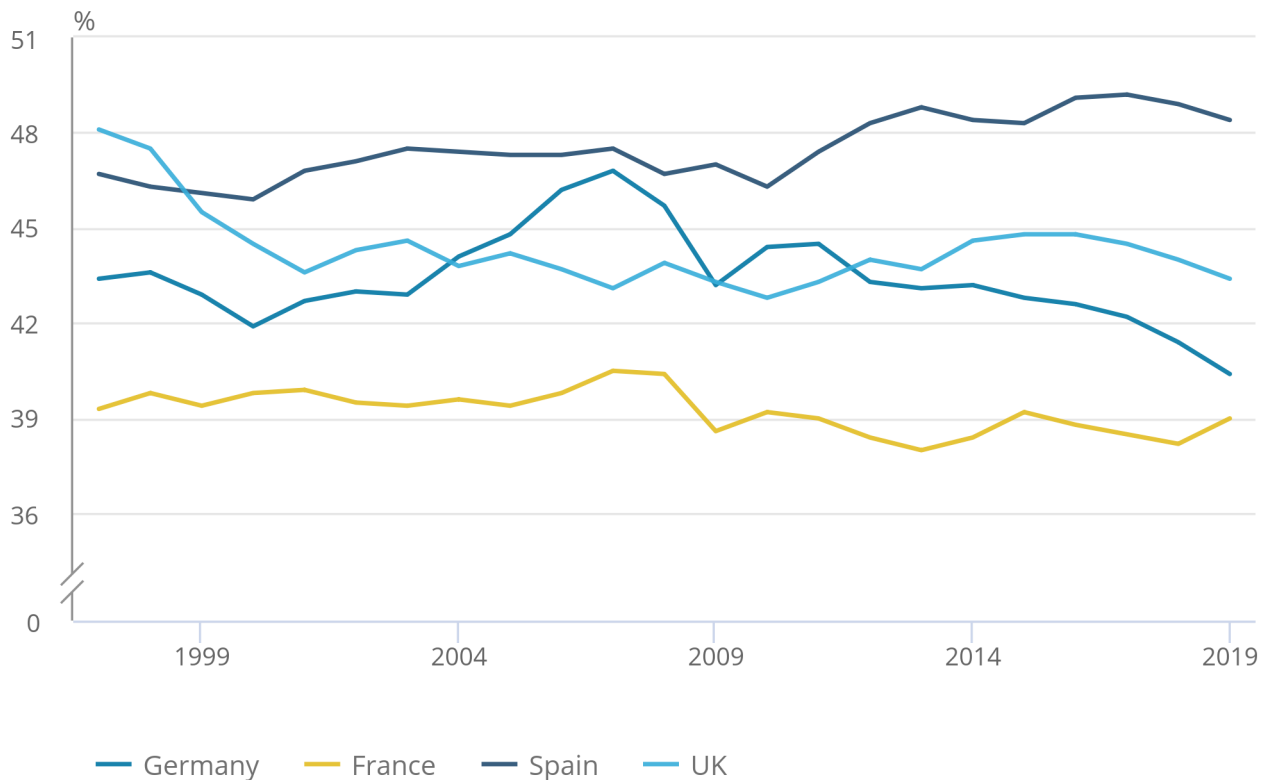
International data on a European System of Accounts 2010 (ESA 2010) basis are only available at the aggregate national level, which is shown for selected countries in Figure 4.

**Figure 4: The UK's national profit share fell for the third consecutive year**

National profit share of gross value added for selected countries, calendar years 1997 to 2019

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National profit share of gross value added for selected countries, calendar years 1997 to 2019



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

France was the only country to experience a rise in national profit share in 2019. For the UK, this was the third consecutive annual decrease. Germany saw the largest percentage fall in 2019, down 1.0%.

## 6 . Profitability data

[Profitability of UK companies - rates of return and revisions](#)

Dataset | Released 28 April 2020

Rates of return and revision tables of UK private non-financial corporations (PNFCs) by quarter.

[Profitability of UK companies time series](#)

Dataset | Released 28 April 2020

Annual and quarterly data for the latest profitability estimates of UK companies.

## 7 . Glossary

### Private non-financial corporations

Private non-financial corporations (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; and mining and quarrying).

### Net rate of return

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, owing to depreciation). Gross rates of return are available in the [dataset with this release](#).

### UK continental shelf

The UKCS is 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. The net rate of return for UKCS companies is not directly comparable with those for other sectors.

### Gross operating surplus

The gross operating surplus (GOS) of 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).

## 8 . Measuring the data

### Coronavirus (COVID-19)

During the coronavirus (COVID-19) pandemic, we are working to ensure that we continue to publish profitability of UK companies. The data collection for this quarter's publication has been largely unaffected. As this situation evolves, we are developing several solutions to meet potential scenarios depending on the amount of data that we can collect either through our in-house surveys or using other methods to ensure we are still able to produce the publication over the coming quarters. Our expectation is that, from the next publication in July 2020, we will move to publishing data tables only, rather than the bulletin with tables. This is to free up staff time to concentrate on other priorities.

The Office for National Statistics has released a [public statement](#) on the coronavirus and the production of statistics.

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.



More quality and methodology information on strengths, limitations, appropriate uses, and how the data were created is available in the [Profitability of UK companies](#) and [Quarterly Operating Profits Survey QMI](#).

The [Quarterly sector accounts statistical bulletin](#) includes estimates of national production, income and expenditure, UK sector accounts, and the UK Balance of Payments.

We have revised the net rates of return for PNFCs for previous quarters back to Quarter 1 (Jan to Mar) 2019. For total PNFCs, this is consistent with the [gross domestic product \(GDP\) quarterly national accounts](#) and [Quarterly sector accounts](#) released 31 March 2020.

The estimates quoted in the [international comparisons section](#) contains 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 fixed capital consumption QMI](#).

# 9 . Strengths and limitations

## Lack of international comparability

International comparisons of profitability can be problematic; the UK measures the rate of return on capital employed, while other countries use a range of different methods.

It is possible to compare the aggregated national profit share, defined as [gross operating surplus \(GOS\)](#) plus mixed income (that is, income made by the self-employed and other non-incorporated businesses) divided by gross value added (GVA) on a [European System of Accounts 2010 \(ESA 2010\)](#) 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 a result of 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, while the rest of this bulletin refers to the activities of private non-financial corporations (PNFCs) only.

# 10 . Related links

### [GDP quarterly national accounts](#)

Statistical bulletin | Released 31 March 2020

Revised quarterly estimate of gross domestic product (GDP) for the UK. Uses additional data to provide a more precise indication of economic growth than the first estimate.

### [Quarterly sector accounts](#)

Statistical bulletin | Released 31 March 2020

Detailed estimates of quarterly sector accounts that can be found in the UK Economic Accounts (UKEA).

