



# KPMG UK Tech Monitor

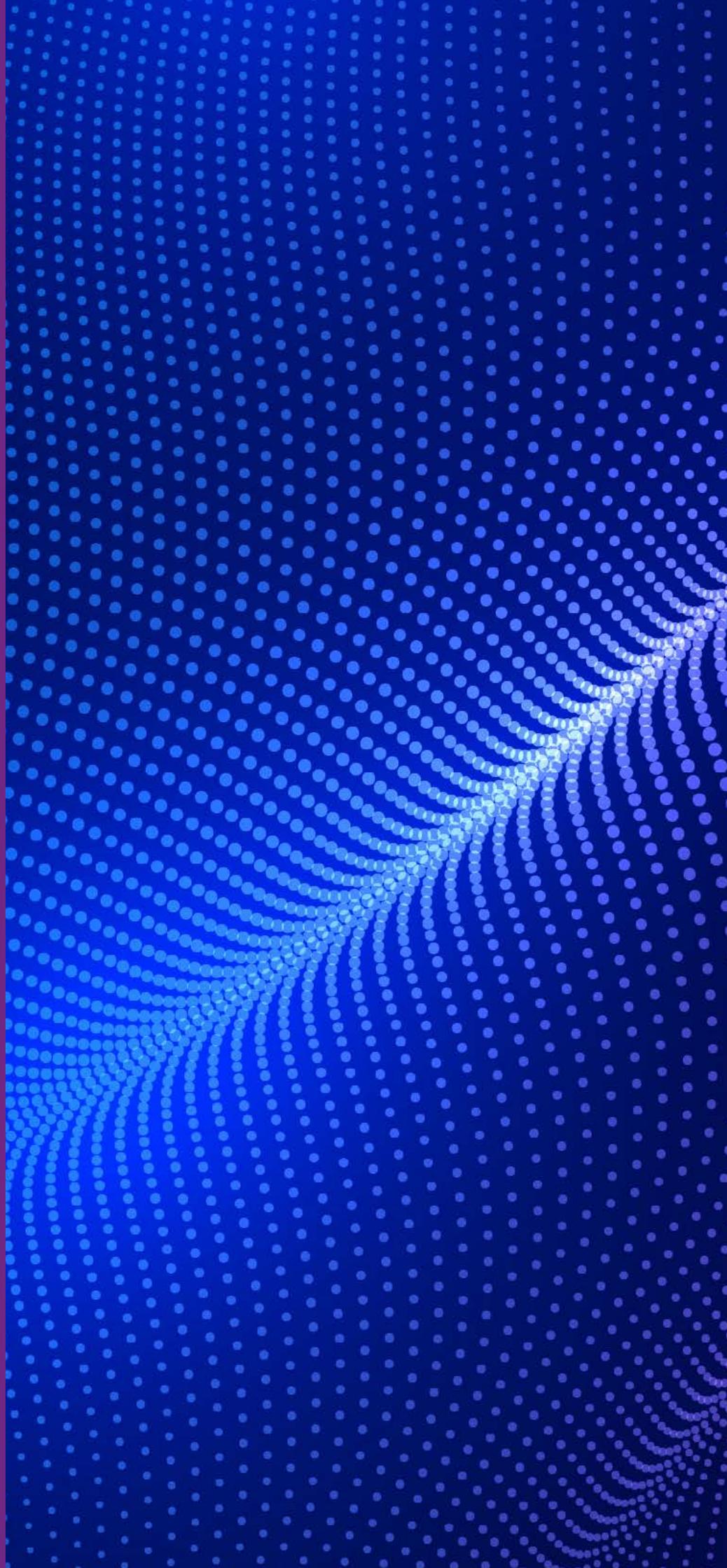
Tech sector activity surges and  
staff hiring hits record  
high in Q2



July 2021

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Chair, KPMG in the UK

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# Foreword

With the easing of COVID restrictions, the Q2 results reflect a rebound in business and consumer confidence driving accelerated growth and outlook for the tech sector. There are some very positive indicators that this vital part of the UK economy has bounced back from the pandemic and is powering ahead into strong growth.

Activity and investment levels have increased as businesses moved through Q2 with the rise in new orders, the quickest for six-and-a-half years. Greater sales volumes sustained a record rise in employment as businesses looked to expand capacity and meet rising customer demand.

But there are concerns for the sector as a shortage of electrical components more widespread than at any other time in the past 17 years, coupled with rising supply chain and staffing costs, stifle the ability of tech businesses and their customers to benefit fully from the growth opportunity.

Rising costs put huge pressure on margins with increases needing to be passed on to customers. It is an area that we will watch with interest; the sector can sustain a few more months of pressure, but if these issues continue longer term it could have a knock-on impact to the wider economy and hamper the UK recovery.



**Bina Mehta, Chair,**  
KPMG in the UK

# KPMG's Outlook

## People



The pace of change in the labour market is unprecedented, with new jobs being created whilst others become obsolete in the tech sector over faster cycles than we have historically seen. This is reflective of the scale of digital transformation that all organisations have been forced to undergo over the past 12-18 months and the trends show that large and smaller tech firms alike are benefiting from the sector wide boom with hiring on the rise. For this to be sustainable in the long run however, a diverse sourcing strategy is needed across the 5Bs to ensure that organisations remain responsive, 'talent light' and avoid peaks and troughs in their hiring plans.



**Anna Marie Detert**  
Partner, KPMG LLP (UK)  
Corporates People Consulting

## Pricing



Rapid increases in costs in the tech sector in 2021, along with intense competition, are leading to an increase in margin pressure on companies. The companies are therefore taking the opportunity to increase prices and restore profitability.

To illustrate, line rental and call packages have gone up by 4% and with further inflation on the horizon, we expect this upward price trend to continue.



**Shashank Dewan**  
Partner, KPMG LLP (UK)  
Pricing Strategy

## Supply Chains



Key challenges for manufacturers in the coming months will be navigating how the end of various Brexit grace periods impacts both their material supply and their route to market for exported products. Of particular concern for this industry will be the Rules of Origin changes and the conformity marking changes coming into force in Jan 22. Companies not only need to do their own planning for these new rules, but need to engage with their suppliers to verify they also have a robust plan to keep goods flowing post Jan 22.



**Maureen O'Shea**  
Partner, KPMG LLP (UK)  
Operational Transformation and  
Supply Chain

## M&A



The last quarter confirmed that we're in a golden era of technology investing, with a variety of actors seeking to capitalise on the secular trends of digitisation as well as the 'new ways of living and working' triggered by the pandemic. Valuation multiples continue to trend up, most recently also as a result of the boom in SPAC vehicles. If 2020 was the year of US SPACs, 2021 is when the action is spreading to Europe and in particular to the UK, which has the lion's share among SPAC vehicles. Sound value creation plans and faultless execution will be all the more important to underpin the aggressive entry prices and deliver satisfactory returns.



**Alfonso Marone**  
Partner, KPMG LLP (UK)  
TMT Deal Advisory Lead



## Key findings

- Business activity growth at tech firms hits six-and-a-half year high
- Tech sector employment expands at record pace
- Recovery accompanied by unprecedented rise in costs amid supply constraints



“With the lifting of COVID restrictions helping to ease business conditions, the tech sector is powering ahead with recovery and growth with new orders and recruitment hitting new highs. This is great news for the UK economy - as the tech sector is a major contributor to economic health and wealth.

“Against this positive outlook, there is continued pressure on margins and costs, partly due to increased supply chain costs as a result of Brexit and the impact of the pandemic on labour costs. There are some clouds on the horizon with a shortage of electrical components more widespread than at any other time in the past 17 years, which is hampering the ability of tech businesses and their customers to meet their recovery plans. This could have a knock-on impact to other businesses and their long-term growth plans, impacting the pace of the UK recovery.”

Bina Mehta, Chair,  
KPMG in the UK

# Welcome to the KPMG UK Tech Monitor Index

We have compiled the quarterly UK Tech Monitor Index by taking a representative sample of tech companies from IHS Markit's widely-watched Purchasing Managers' Index® (PMI®) surveys. The tech sector is defined in this report as technology software, technology services and manufacturing of technology equipment. Historical data is available since Q1 2003 and full details are in the methodology section.

## **Tech sector recovers strongly in Q2 as national lockdown measures ease**

The latest KPMG UK Tech Monitor Index survey showed a sharp rebound in activity at tech firms during Q2 2021 as national lockdown measures were eased. This followed a slight dip in output at the beginning of the year.

Monthly data showed that growth momentum built throughout the quarter as more pandemic restrictions were lifted and business investment picked up.

The upturn in output was supported by a substantial rise in new orders that was the quickest for six-and-a-half years. This recovery in sales volumes drove a record rise in employment as tech firms looked to expand capacity and meet rising customer demand.

## **Business activity expands at quickest rate since Q4 2014**

At 59.2 in Q2, the headline Business Activity Index rose from 49.2 in Q1 and was well above the neutral 50.0 level that separates expansion from contraction. Furthermore, the rate of output growth was the quickest seen since Q4 2014.

The rollback of lockdown restrictions, alongside improved business and consumer confidence helped to lift activity, according to survey respondents.

Similarly, business activity rebounded sharply across the rest of the UK economy during Q2. Overall growth was slightly faster than seen in the tech sector, largely due to the reopening of consumer-facing areas such as hospitality and leisure.

## **Fastest increase in new orders for six-and-a-half years**

Helping to drive the sharp upturn in business activity at tech companies was a renewed and rapid increase in total new

work. At 60.0 in Q2, the index measuring new order volumes rose from 48.9 in Q1 and signalled the steepest rate of growth since Q4 2014.

Improved order books were linked to the restart of delayed projects, greater willingness to spend among clients, and increased export sales.

## **Steepest rise in tech employment since the survey began in 2003**

A rapid rise in sales led to much greater pressure on operating capacity during the second quarter. The latest survey indicated that outstanding business rose to the greatest extent since the start of the index in Q1 2003.

Consequently, tech companies added to their payrolls for a third consecutive quarter. This index rose from 52.3 in Q1 to 58.1 in Q2, which marked a survey-record rate of job creation. Staff hiring among tech companies was also faster than seen across the UK private sector as a whole (index at 57.0).

## **Rapid increase in costs as wages rise and supply chains come under strain**

Latest data illustrated intense cost pressures at tech firms. The sector registered its steepest increase in operating expenses on record during Q2. The most commonly cited reasons for input cost pressures were Brexit and pandemic-related disruption. Survey respondents frequently cited higher staff costs, rising prices for critical components, and greater transport bills.

Higher costs were generally passed on to clients, with prices charged also rising at the fastest rate since the index began in Q1 2003.

## **Business confidence highest for over 14 years**

The easing of COVID-19 restrictions and successful vaccine rollout lifted business confidence across the UK tech sector in the second quarter. Optimism reached its highest since Q1 2007.

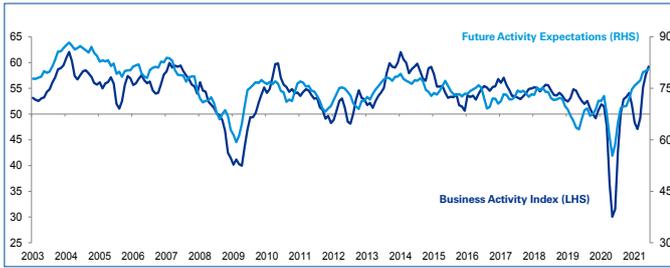
Around 67% of the survey panel forecast output growth in the year ahead, while only 6% expect a decline. Business investment in digital infrastructure, sustainable technologies, and AI innovation are all forecast to boost tech sector activity in the months ahead.



### KPMG UK Tech Monitor Index

Above 50 = business activity growth, seasonally adjusted

Above 50 = growth in the next 12 months



# Tech Sector: Demand and Capacity



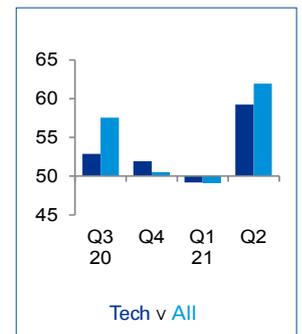
## Tech Sector Output: Business Activity Index

### Business activity growth rebounds sharply in Q2

After falling slightly during the opening quarter of 2021, tech sector business activity increased sharply in Q2. The respective index leaped 10 points from 49.2 in Q1 to 59.2, marking the steepest increase in output since Q4 2014. The upturn was linked to improved client confidence, strong business investment in response to easing pandemic restrictions, and the restart of previously delayed projects.

### Business Activity Index

Above 50 = growth, seasonally adjusted



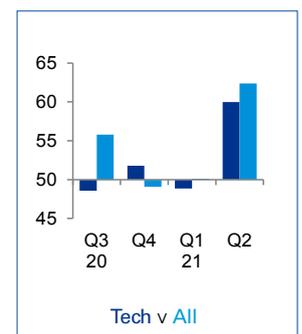
## Tech Sector Sales: New Business Index

### Steepest increase in sales since Q4 2014

Total new orders placed with tech sector companies rebounded strongly in the second quarter of 2021. At 60.0, this index picked up considerably from 48.9 in Q1 and signalled the fastest increase in sales volumes for six-and-a-half years. Survey respondents mentioned that the improving UK economic outlook, rising consumer spending and a swift recovery in business activity among clients had lifted demand. Tech firms also cited robust spending on ecommerce services and digital marketing, alongside strengthening sales across export markets.

### New Business Index

Above 50 = growth, seasonally adjusted





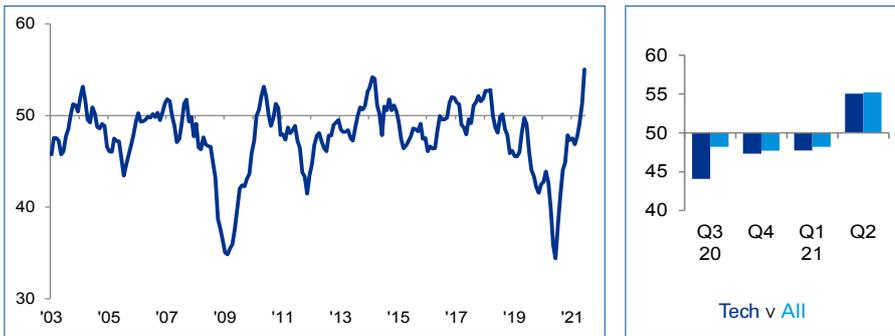
**Tech Sector Capacity: Outstanding Business Index**

**Backlogs increase at quickest rate on record**

The level of unfinished work at UK tech companies rose sharply in Q2, as surging sales placed pressure on business capacity. At 55.0, the index was up from 47.7 in Q1 and pointed to the first rise in backlogs since Q1 2018. Furthermore, the rate of accumulation was the sharpest seen since the series began in Q1 2003. Monthly data showed that pressure on capacity got more severe as the second quarter progressed, with panellists frequently commenting on supply chain delays, component shortages and difficulties in expanding capacity to meet new orders.

**Outstanding Business Index**

Above 50 = growth, seasonally adjusted



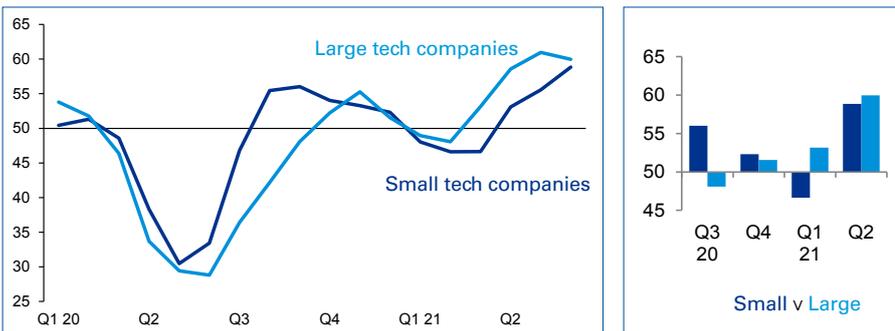
**Company Size Breakdown: Business Activity Index**

**Large tech companies outperform in Q2**

Small tech companies saw a faster recovery in business activity than large firms during the second half of 2020. However, this trend has reversed in the first half of 2021. At 60.0 in Q2, the index for large tech businesses was up from 53.1 in Q1 and comfortably above the equivalent reading for small firms (58.8). Large tech companies also signalled a much faster increase in backlogs than smaller businesses during Q2, driven by exceptionally strong pipelines of new work, which suggested that the outperformance will persist into the remainder of this year.

**Business Activity Index**

Above 50 = growth, seasonally adjusted



# Tech Sector: Jobs and Prices



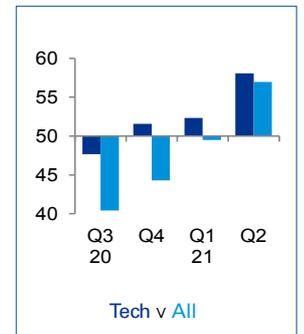
## Tech Sector Jobs: Employment Index

### Record increase in tech sector employment

Staffing numbers at UK tech companies expanded further in the second quarter of 2021. The rate of job creation was the quickest seen since this index began more than 18 years ago, with the latest reading climbing from 52.3 in Q1 to 58.1. Employment growth at tech firms also outperformed that seen for the UK private sector as a whole (index at 57.0). Reports from survey respondents indicated that companies added to their payrolls due to increased workloads and efforts to expand capacity.

### Employment Index

Above 50 = growth, seasonally adjusted



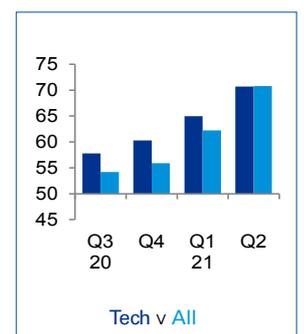
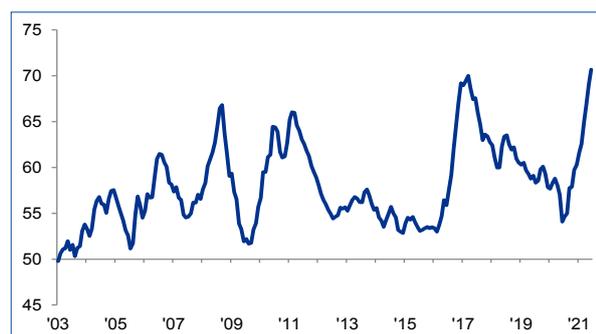
## Tech Sector Costs: Input Prices Index

### Cost inflation highest since the survey began in Q1 2003

Latest data showed that UK tech firms saw the steepest increase in input costs on record. At 70.7 in Q2, the respective index was up from 65.0 in Q1 and pointed to a rapid rise in expenses that was the fastest since the survey began at the start of 2003. Inflation was widely linked to higher staff costs, increased transport fees and supplier price hikes due to low stock availability (particularly for components such as semiconductors).

### Input Prices Index

Above 50 = inflation, seasonally adjusted





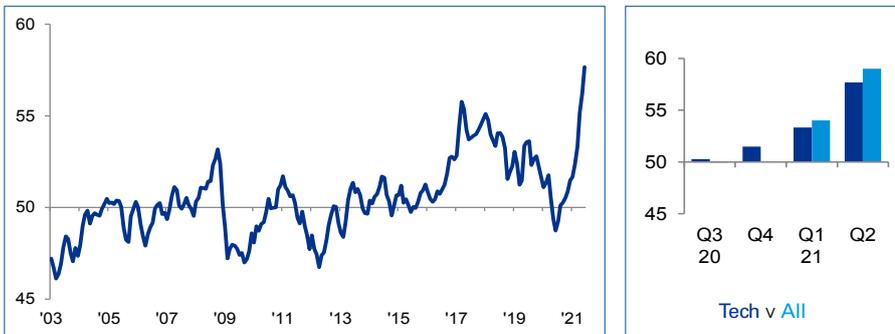
**Tech Sector Margins:** Prices Charged Index

**Selling prices rise rapidly in Q2**

Greater cost pressures and strong demand conditions led UK tech firms to raise their charges at a faster pace in the second quarter of 2021. The rate of inflation was the fastest since the series began over 18 years ago, with the index rising from 53.3 in Q1 to 57.7. That said, the increase was not quite as steep as that seen on average across the UK private sector (index at 59.0). Survey respondents often mentioned efforts to pass on higher raw material prices and transportation costs.

**Prices Charged Index**

Above 50 = inflation, seasonally adjusted



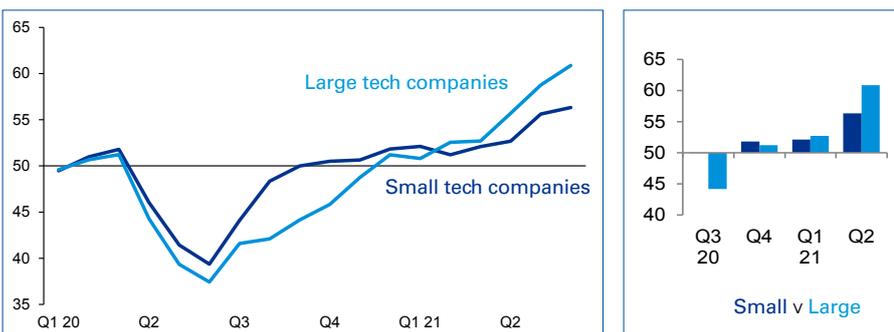
**Company Size Breakdown: Employment Index**

**Staff hiring at small tech firms hits record high**

At 56.3 in Q2, up from 52.1 in the previous quarter, the index measuring staff hiring at small tech companies was the highest since the survey began in 2003. The index also highlights that employment numbers returned to growth more quickly than at large tech companies after the pandemic began. That said, job creation gained considerable speed at large tech firms in Q2, with this index rising from 52.7 in Q1 to 60.9. This was the highest since Q1 2018 and above that seen among small businesses.

**Employment Index**

Above 50 = growth, seasonally adjusted



# Tech sector outlook



## Tech Sector Outlook: Business Activity Expectations Index

### Business confidence hits highest since Q1 2007

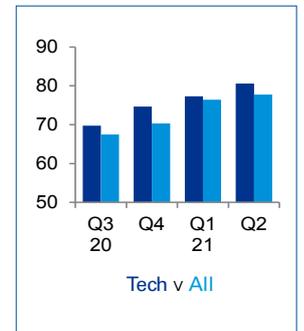
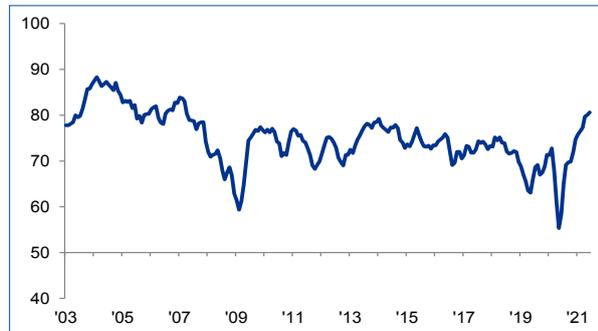
Around 67% of the survey panel anticipate a rise in output during the year ahead, while only 6% forecast a reduction. The resulting Business Activity Expectations Index indicated a high level of optimism among UK tech firms in the second quarter, with the latest reading rising from 77.3 in Q1 to 80.6. This marked the strongest degree of positive sentiment since Q1 2007, and tech businesses remained more confident about the outlook than other parts of the UK economy (overall index at 77.7).

The rollback of COVID-19 restrictions and rapid vaccine progress underpinned growth forecasts for the year ahead. Companies also stated that the release of pent-up demand and improved supply chain performance will support higher activity over the next 12 months. Investments in new technology were cited by survey respondents as helping to boost demand, with clients seeking to enhance their digital services, build better infrastructure for hybrid working, and meet sustainability targets.

However, lingering uncertainty about the trajectory of the pandemic, especially in relation to new virus strains and the re-imposition of restrictions, acted as a constraint on optimism at some tech companies in Q2. The prospect of further supply chain shocks and fewer EU clients following Brexit were also mentioned as factors that could limit the speed of recovery over the next 12 months.

### Business Activity Expectations Index

Above 50 = growth in the next 12 months



### How has the COVID-19 pandemic impacted tech sector prospects?

In this section, we assess the impact of the COVID-19 pandemic on the UK economy and tech sector prospects.

Service providers led the recovery in the UK economy during the second quarter of 2021, with this index pointing to the fastest growth for 24 years. Manufacturing production also expanded at a rapid pace, despite headwinds from supply shortages and stretched business capacity.

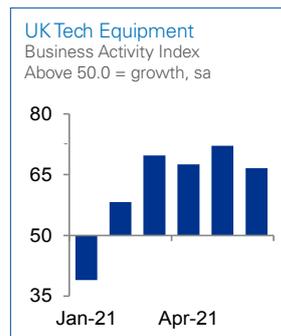
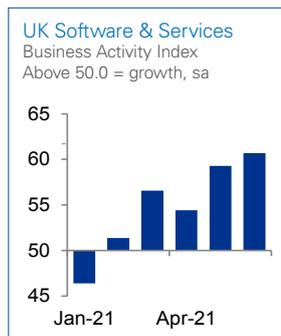
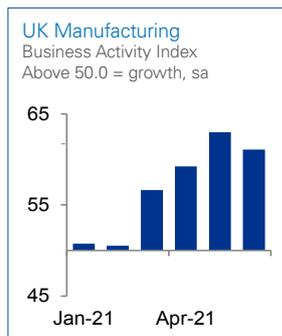
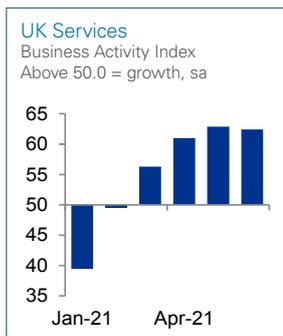
Monthly data illustrated that the Software & Services sub-sector gained momentum in June, which bucked a slowdown elsewhere in the service economy from May's peak. In fact, the latest rise in activity within this segment of the tech sector was the strongest seen in any month since January 2016.

Turning to production of Technology Equipment, latest monthly data highlighted that these tech companies experienced much faster growth than the rest of the UK manufacturing sector, which continued the trend recorded since the spring.

The outperformance of goods producers in the technology equipment sector was fuelled by exceptionally strong export order books. In April, survey data indicated the steepest rise in new business from abroad since this index began in 1998. Companies cited surging global demand for technology items and forward purchasing by overseas clients to secure critical components.

In contrast, lacklustre export volumes were reported in other parts of the UK manufacturing sector, such as Food & Drink and Automobiles & Auto Parts, where Brexit trade issues and disrupted supply chains held back sales in the second quarter.

### Business Activity Index



# Tech sector outlook

## Global semiconductor shortages hit record high in Q2

Worldwide shortages of semiconductors escalated during the second quarter of 2021 amid imbalanced demand and supply as economies recovered from the pandemic. As a result, the number of manufacturers citing a lack of electrical components reached a record high since 2004, according to data compiled from IHS Markit's Global PMI surveys. This index illustrated that reports of supply shortages for electrical items were nine times higher than usual in May, which led to particularly severe disruption at automotive plants.

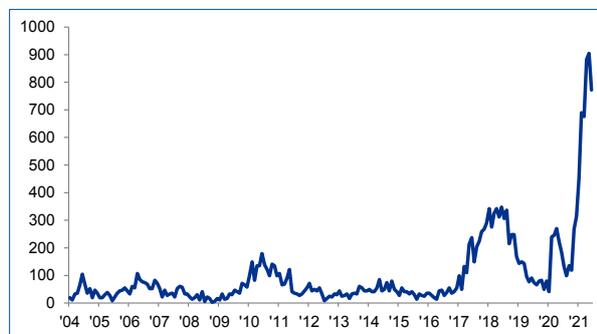
June data was slightly more encouraging, with the index dipping to a three-month low. However, this still meant that shortages of electrical items were still more widespread than at any other time in the past 17 years.

## Brexit and pandemic disruption pushes up costs at UK firms

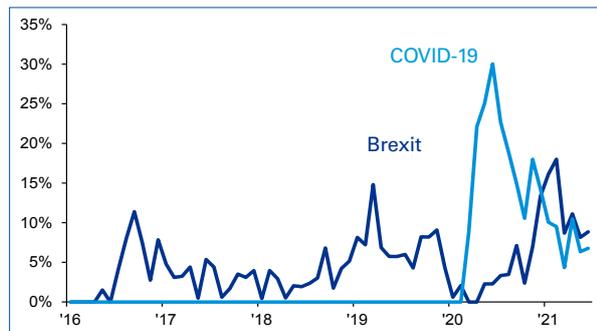
Disruptions to global technology supply chains added to cost pressures faced by UK businesses after the national lockdown. Survey data compiled by IHS Markit highlighted that Brexit and COVID were the most commonly cited reasons for higher input prices in the second quarter of the year, although both indices have eased since the start of 2021.

Staff shortages have emerged as a driver of cost pressures and constraint on growth. Record falls in candidate availability and an exceptionally strong rise vacancies were signalled in June by the KPMG / REC UK Report on Jobs.

**Global Supply Chains:** Short supply of electrical items (index, 100 = long-run average)



**UK Panel Comment Tracker:** Reason cited for higher input costs (percent of total comments)



# UK sector rankings

The release of pent-up consumer demand and higher levels of business investment spending helped to lift confidence across the UK economy in the second quarter.

Optimism improved since Q1 2021 in all six sectors monitored by the survey data, bolstered by the successful vaccine rollout and looser pandemic restrictions.

The strongest levels of confidence towards the year ahead were seen among manufacturers and those in the tech sector. This was driven by expectations of further steep increases in client demand and hopes that supply chain disruption will subside as extra capacity starts to clear bottlenecks. Tech companies often highlighted growth opportunities related to innovation in areas such as artificial intelligence, as well as electric vehicles and other investment in sustainable technologies.

Hotels & Restaurants were also highly upbeat regarding their prospects, with confidence in the sector bouncing back as restrictions on leisure, events and hospitality continue to ease over the summer.

Transport remained at the bottom of the rankings, as international travel restrictions were expected to persist.

## Business Expectations Index by sector

Above 50 = growth in next 12 months

	Q2 2021	Q1 2021
Manufacturing	81	77
Tech Sector	81	77
Hotels & Restaurants	80	79
Financial Intermediation	75	71
Business Services	73	72
Transport Services	72	67



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## About KPMG

KPMG LLP, a UK limited liability partnership, operates from 21 offices across the UK with approximately 16,000 partners and staff. The UK firm recorded a revenue of £2.3 billion in the year ended 30 September 2020.

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IHS Markit (NYSE: INFO) is a world leader in critical information, analytics and solutions for the major industries and markets that drive economies worldwide. The company delivers next-generation information, analytics and solutions to customers in business, finance and government, improving their operational efficiency and providing deep insights that lead to well-informed, confident decisions. IHS Markit has more than 50,000 business and government customers, including 80 percent of the Fortune Global 500 and the world's leading financial institutions.

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

UK Tech Monitor Index data is derived from a representative sub-category of approximately 150 tech companies within IHS 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 data

Business activity expectations data are 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, capex, profits and input cost expectations data are based on responses from UK services and manufacturing firms participating in IHS 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).

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