

Review of Scottish Business Surveys

Overall

The extent to which the recession is slowing down, or bottoming has been a popular theme in recent surveys, although, especially for the service sector, the timing of the Easter weekend (in the first quarter of 2008, but in the second quarter of 2009) and significant differences in the weather, should prompt caution as to drawing any firm conclusions between the first and second quarters, evidence of any significant changes in business trends and more generally in the current trends in the Scottish economy. In the retail sector the two latest Scottish Retail Sales Monitors suggest some improvement in April, albeit with considerable reservations, but some slowing down in May.

Nevertheless, there is an emerging consistency in the main manufacturing surveys (PMI, Lloyds TSB and Scottish Engineering anticipated for q 2 2009, and SCBS anticipated for q1 2010) that the pace of the recession is slowing down, especially after February, although from the current surveys it remains unclear as to whether these improvements are mainly the effects of restocking rather than recovery.

Oil and gas services

Offshore activities in the UK oil & gas sector continue to fall, and exploration operations within the UK Continental Shelf have decreased significantly (by some 78% over the past 12 months according to the Deloitte's North West Europe Review (published April 2009)). To an extent the credit issues affecting both the oil majors and the independents have led to a widespread downward re assessment of exploration and investment plans, and for the UKCS the issues of exploitation of marginal and ageing fields has become more significant.

Notwithstanding reduced demand for oil and evidence of current surplus stocks, the volatility in oil prices, a feature of the past years, has returned due to a combination of political uncertainty, some speculation in commodities, short term seasonal demand. The latest Cambridge Energy Research Associates reports suggest the upward cost pressures are still evident for oil firms, notwithstanding the current surplus capacity and stocks. The current upward drift in oil prices is likely to be replaced by a more general upward cycle for demand and hence prices in 2012/3, and the continuing shortages of refining capacity may lead to the return of significant rises in oil prices.

Lloyds TSB noted the steepest declines in the volume of business, turnover and export activity were in q4 2008, with the rate/spread of decline easing in q1 2009. Generally cash flow concerns were slightly less in q1 2009, but, and to a degree expected, concerns as to credit availability and late payment were thought to be more evident in the business conditions in the three months to end May 2009. The PMI noted 'operating conditions continuing to deteriorate during May, although signs of a slowing recession continued to emerge'.

Manufacturing

Results from the Lloyds TSB (February), PMI (April and May) and SCBS (March) suggest some signs of a slowing down in the rate of decline in activity. The PMI noted the weakest falls in production levels in April since June 2008, but noted little improvement in May, whereas the SCBS saw continued sharp declines in total, rest of UK and Scottish orders, but indicated some easing in the rate of decline in new orders in q 2 2009. The PMI (April) noted new orders have fallen for 12 months, but the rate of decline eased further, and noted a further weakening in the rate of decline in export orders, but this improvement seemed to level off in May. In contrast the SCBS export data indicated a less severe weakness, whereas the latest CBI and Scottish Engineering reports are more pessimistic reporting the weakest trends in orders for 10 years, but the Scottish Engineering Survey was the last to report entering the recession and its results seem to lag behind those of the other surveys, nevertheless, it anticipates some easing in the extent of decline in the second quarter.

The May PMI noted a continuation of the weakening trend in work in progress. The SCBS (q1 2009) noted average capacity eased to 66.4%, some 6 percentage points lower than in the previous quarter and 12 percentage points lower than a year ago, and over three-quarters of respondents reported capacity used was below preferred levels. Scottish Engineering reported capacity utilisation and output volume down sharply. The PMI, Scottish Engineering and SCBS noted pressures to raise prices, with the exception of finance costs, continuing to ease. However, the possibility of further price reductions is leading to some deferment of orders.

The SCBS evidence on investment trends noted that these eased again in q1 2009, and only 9% of respondents expect to increase investment, whilst 18.6% anticipate increasing their leasing of equipment over the coming year. Cash flow trends deteriorated further, and the anticipated trends in turnover and profitability over the next 12 months are the weakest recorded in the survey.

Both the PMI and SCBS noted the proportion of firms reducing staff increased significantly to February/March

and declining trends in hours worked and expenditure on training were reported. The April PMI data suggested the rate of decline in employment was easing.

Construction

Whilst house building and commercial work has been substantially reduced PPP funded work has continued, however this will go into decline by the end this of year/next year unless public sector work starts to emerge. There are some signs that some house building is picking up. Nationally there has been a slight increase in the number of approved mortgages, but from a very low base (across the UK approved mortgages were still 34% lower than in March 08 according the Halifax House Price Index), and public sector housing projects have been affected by credit issues.

The Scottish Chambers' Business Survey reported a widespread weakness in business confidence, and the trends in new orders remained at record lows, however some easing in the extent of these downward trends is anticipated in the second quarter, and 22% expect rising trends in the level of new work over the six months to September 2009. Nevertheless, a net of 64% (65%, 37% and 25% in the previous three quarters) anticipate declining turnover trends over the next year. A net of 78% (compared to a net of 3% in q1 2008) anticipate declining profitability over the next twelve months, and a net of 81% of construction firms anticipate declining tender margins over the next twelve months.

SCBS data suggests average capacity declined by three percentage points to 69%, the lowest figure recorded, and a decline of 19.7 percentage points over the year. Seventy-eight percent reported and 67% expect a declining trend in the level of work in progress, again the weakest trends in the history of the survey.

The decline in the construction sector has adversely impacted on the margins, fees, work, confidence and employment in the professional services allied to construction. Across the sector recruitment activity has declined to historic low levels and reductions in employment have been widespread.

The service sector

Wholesale distribution

Data from the SCBS suggests that concerns as to the business situation remained high amongst wholesale respondents in the first quarter of 2009 and 60% reported being less confident as to the general business situation. Declines in sales were widely reported and little improvement is expected through the second quarter, suggesting that restocking remains at a low level. The majority still anticipate turnover to decline over the next year, but margins not to be under considerable pressures.

Retail

Scottish Retail Sales Monitor reported sales up 4.3% compared to April 2008, but noted that Easter and better weather occurred in April 2009, whereas Easter was in March in 2008. However, the Scottish Retail Consortium noted that if the March and April figures are combined then the average increase over the year is 2.1% and factoring in inflation for food suggests that sales are relatively flat.

The Scottish Retail Sales Monitor noted that overall sales, allowing for increases in floor space, were up 8.2% over the year. It is unclear as to whether this reflects a drift from smaller and independent stores sales to those of the major multiple retailers, who have indicated further plans for expansion and employment this year.

The SCBS measures general sentiment by type of retailer and reflects concerns within the sector as to the pressures on the independent stores from the major retailers, a theme echoed in recent years by the Federation of Small Businesses. The SCBS results suggest business confidence continuing to fall, but at a reduced rate compared to Q4 2008, but more than 60% reporting falling sales and little improvement anticipated for the second quarter. Reflecting the situation of the smaller and independent retailers the SCBS survey noted a net of -52% of retailers anticipate declining turnover over the year to March 2010 (compared to -69% in the previous quarter), and a net of -73% (-72% in the previous quarter) anticipate declining profitability over the next year, suggesting further pressures on margins during 2009.

Tourism

The Visit Scotland Monthly hotel occupancy study suggested occupancy rates were some 2 – 3% down in February 2009 compared to the same month in 2008. However, by March the downturn appeared more modest with occupancy at 57% (one percentage point lower than in March 2008). April's data suggested average occupancy was marginally higher than in either 2007 or 2008. Occupancy rates appeared to have held up better in Edinburgh/Lothians and Glasgow/Clyde, rather than in other areas. This improvement may reflect a combination of Easter falling in the second quarter in 2009, rather than in the first quarter of 2008, the relative decline of the pound to the Euro, and more people holidaying at home rather than abroad. The PMI data to April 2009 was more pessimistic with demand falling but less so in March and April compared to February, but the latest PMI reported a further weakening in the rate of decline in business activity.

The Scottish Chambers' Business Survey (q1 2009) reported average occupancy (for hotels) at 54%, not too dissimilar than the averages for first quarters in previous years, however, the SCBS noted business confidence

remained very low and occupancy was being sustained by extensive cutting of room rates and with some pressures on margins. The SCBS data suggests discounting of room rates will figure widely in the second quarter, the PMI reported more extensive room rate cutting in March, compared to the period November 08 – February 09, but indicated slightly rising room rates/charges in its April survey. Other data suggests that the sector had recognised that 2009 would not be as good as 2007 and 2008 which had been good years, especially for the major tourist areas. One noticeable feature over recent quarters in the Scottish tourism sector has been the decline in the percentages of firms seeking to recruit staff, with the majority of SCBS respondents reducing both seasonal staff and hours worked.

Logistics

Data from the SCBS q 1 2009 reported widespread declines in business confidence as a net of respondents reported weakening business trends in all areas, especially long haul, storage and couriering activities, although, and in common with other sectors, an easing of these downwards trends is anticipated in the second quarter. Over the next year pressures on margins are widely expected, and turnover and profitably trends are expected to remain very weak.

Cost pressures

The SCBS noted cost pressures, except finance costs, continuing to ease across all sectors and expectations of price decreases were reported in manufacturing. Pressures on margins were widely reported in construction, and evident in tourism. In contrast over 70% of retailers anticipate price increases over the next three months. The latest PMI (May) noted some slight easing in the rate of decline in prices charged in the services sector, but the discounting of prices in manufacturing being more evident.

Pay and employment

SCBS data for the first quarter suggests the percentages of respondents increasing pay in the first quarter ranged from 8% of construction to 21% of manufacturing, and average pay increases ranged from 3.05% in manufacturing to 5.33% in retail. A net of firms in all sectors reported declining net trends in employment and hours worked/overtime levels. Recruitment activity in all sectors was low ranging from 8% in construction, 9% in retail to 38% in tourism and 42% in manufacturing.

Changes in the employment market seem still subdued – in latest PMI (May) 75% of manufacturers reported no change in employment and 77% of services no change in employment levels. In contrast in the earlier Scottish Engineering report (q1 2009) only 50% reported no change in employment.

SCBS data for the first quarter noted average capacity used in manufacturing has declined by 12.2 percentage points and in construction by 19.7 percentage points over the past year. In construction the proportion reporting working below optimum levels has increased from a net of 31% to a net of 86%. In tourism occupancy remained at the same level as in q1 2008, however, occupancy has been sustained only by widespread discounting.

Both the PMI and SCBS noted cost pressures, except finance costs, continued to ease across all sectors and expectations of price decreases were reported in manufacturing. Pressures on margins were widely reported in construction, and evident in tourism. In contrast over 70% of retailers anticipate price increases over the next three months.

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Current trends in Scottish Business are regularly reported by a number of business surveys. This report draws on:

1. The Confederation of British Industries Scottish Industrial Trends Survey April 2009;
2. Lloyds TSB Business Monitors for the quarters to February and May 2009 and expectations to August 2009;
3. Scottish Engineering's Quarterly Review for the first quarter 2009;
4. The Royal Bank of Scotland's Monthly Purchasing Managers' Index to end May 2009;
5. The Scottish Retail Consortium's Monthly Scottish Retail Sales Monitor for April and May 2009;
6. The Scottish Chambers of Commerce Quarterly Business Survey, reports for the first quarter of 2009;
7. Deloitte's North West Europe Review published April 2009);
8. The Lloyds TSB Halifax House Price Index;
9. Scottish Hotel Occupancy Survey to end April 2009.