

# Scottish Chambers' Business Survey

Strathclyde University's Fraser of Allander Institute in collaboration with the Scottish Chambers' of Commerce conducts the quarterly Chambers' Business Survey. In the present survey, which was conducted in September and early October, around 350 firms responded to the questionnaire.

## Business Performance

### Recent past and next three months

Business confidence was weaker in all sectors than in the first quarter. Nevertheless, confidence continued to rise in manufacturing and tourism, but turned downwards in construction and the decline strengthened in wholesale and retail distribution.

Rising trends in orders and demand were reported in manufacturing, construction, wholesale and tourism, however, the outturn in demand in all sectors was weaker than had been expected.

Manufacturing respondents reported an increase in the volume of work in progress and a slight decline in stocks of finished goods. Average capacity used eased to 77% and the percentage reporting working below optimum levels rose to 50%. Construction firms reported a slight easing in average capacity used, but stronger rising trends in work in progress, and expect these rising trends to strengthen further in the second half of 2005.

In the service sector wholesale respondents reported a modestly rising trend in sales. In contrast declining sales were again more widely reported by retail respondents, and little improvement is anticipated for the third quarter. Only 49% of retail respondents (compared to 75% a year ago) reported rising or level trends in sales. Tourism respondents reported good second quarter results, and expect rising visitor numbers from all areas in the third quarter, although demand from abroad remains weak.

The likelihood of price increases eased in manufacturing, wholesale and retail. The rising trend in room rates in the tourism sector was broadly the same as in the second quarter of 2004.

Concerns as to the levels of orders/sales and competition rose slightly amongst manufacturing and more significantly amongst construction respondents in the second quarter,

being cited by 42% of manufacturers, 70% of construction and 36% of tourist respondents.

Pay increases in the first quarter were slightly higher than in the previous quarter, and ranged from 3.2% in wholesale to 6.0% in construction. Recruitment activity was generally higher in the service and construction sectors than in manufacturing.

### Expectations for the next twelve months

Manufacturing respondents anticipate more modestly rising trends in orders, turnover and profitability over the next twelve months. Construction respondents expect rising turnover but more modest increases in profitability over the next year.

Retail respondents are again less confident as to the forthcoming year, and continue to expect declining trends in turnover and profitability. In contrast rising turnover, and more modestly profitability continue to be expected amongst tourism respondents.

## Manufacturing

### Optimism

The rise in business confidence, a feature of the last three months continued at slightly more modest levels.

### Orders and Sales

The rising trend in total orders continued at more modest levels, and the outturn was less than expected. Respondents now expect some modest easing of trends in the third quarter. Rising trends in orders from all areas were again reported in the first quarter. Expectations for the next twelve months, whilst positive, are now weaker than three months ago.

The rising trend in the level of work in progress continued at more modest levels and a further easing in the rate of increase is expected. A higher proportion (50%) reported operating at below optimum levels compared to quarter one (35%).

### Finance

The downward trend in cash flow ended, but firms downgraded their expectations as to the trends in turnover and profitability over the next year. Price pressures eased and concerns as to raw material costs remained widespread whilst concerns as to pay costs remained unchanged in the second quarter.

### Investment

48% reported revising investment plans for mid 2005 to mid 2006, and rising trends in investment and leasing were again reported. Investment in the current quarter was again

mainly directed towards increasing efficiency and for the replacement of equipment. Investment for R & D and to develop new markets/products, declined further.

### Employment

Employment continued to strengthen, and a higher percentage (58%) sought to recruit staff.

**Table 1 Manufacturing – key results**

	Q2 2005		
	Up	Level	Down
<b>Business Optimism</b>	28.9	48.1	23.0
Trends in actual orders			
Total new orders	42.8	30.9	26.3
Scottish orders	27.7	52.6	19.8
Rest of UK orders	27.4	48.3	24.3
Export orders [33.5% = N/A]	21.7	31.3	13.5
Trends in expected orders			
Total new orders	33.6	45.5	20.9
Scottish orders	21.5	61.0	17.6
Rest of UK orders	25.8	56.1	18.0
Export orders [35.1%= N/A]	20.9	32.7	11.3
<b>Av Capacity used</b>	77.3		
Invest in plant/equip.	31.2	52.1	16.7
<b>Cash flow past 3 mths</b>	22.9	56.6	20.5
Turnover next 12 mths	47.5	38.5	14.0
Profitability next 12 mths	38.2	32.7	29.2
Price change next 3 mths	23.4	72.0	4.6
Pressures to raise prices from			
<b>Pay settlements</b>	37		
Raw material costs	71		
Finance costs	12		
Other overheads	37		
Transport costs	43		
Employment trends			
Total actual employment	29.4	52.4	18.2
Total expected next 3 months	24.8	67.6	7.6
Average pay increase	3.7		

## Construction

### Optimism

Business confidence eased in the second quarter, notwithstanding rising trends in actual and expected orders and work in progress.

### Contracts

The rising trends in the value of new contracts continued, driven by both public and private commercial sector work. The level of domestic build work contracts eased and little improvement is forecast, but public orders are expected to increase. Firms continue to report rising trends in the level of work in progress and 35% expect the level of work in progress to rise over the next six months.

69% reported operating at or above optimum rates in the first quarter, however, average capacity used eased to 87%.

Respondents are more cautious as to future profit margins and now expect little change over the next year, and 60% expect building and other costs to rise in the year to mid 2006. Both turnover and profitability are again expected to strengthen over the next twelve months, but at more modest rates than had been estimated in the first quarter.

The level of new contracts, shortages of skilled labour, planning delays and the availability of contractors were seen as the four factors most likely to restrict activity over the next quarter.

### Investment

The rising trends in investment and leasing ended. Once again investment authorised in the second quarter was mainly for the replacement of equipment and to increase capacity.

### Employment

The rising trend in employment continued. 63% sought to recruit staff (76% in the previous quarter) and 41% reported increasing pay by an average of 6.0%.

**Table 2 Construction – key results**

	Q2 2005		
	Up	Level	Down
<b>Business Optimism</b>	7.4	70.4	22.2
<b>Trends in actual orders</b>			
Total new orders	40.7	44.4	14.8
Public sector orders	33.3	42.9	23.8
Private commercial	33.3	45.8	20.8
Domestic/house build	15.0	55.0	30.0

## QUARTERLY ECONOMIC COMMENTARY

### Trends in expected orders

Total new orders	33.3	48.1	18.5
Public sector orders	33.3	47.6	19.0
Private commercial	21.7	56.5	21.7
Domestic/house build	15.8	57.9	26.3

### Trends in work in progress

Actual	26.9	61.5	11.5
Expected	34.6	53.8	11.5

### Capacity used

87.1

Invest plant/equip.	14.8	66.7	18.5
Leasing plant/equip	8.3	58.3	33.3

### Employment trends

Actual employment	29.6	63.0	7.4
Expected next 3 months	20.0	80.0	0.0

### Average pay increase

6.0

Percent recruiting staff	63
Recruitment difficulties inc.	23

## Wholesale distribution

### Optimism

The decline in business confidence strengthened in the second quarter, notwithstanding slightly better than anticipated sales.

### Sales

A modestly rising trends in sales was reported; this increase is forecast to continue through the third quarter. The proportion reporting rising or level sales trends (72.7%) was little changed from the previous quarter (72.4%)

Once again the level of competition, along with business rates were seen as the factors most likely to restrict sales over the third quarter.

Expectations of price increases eased again, but still remain widespread. This may underpin the expectations as to slightly declining profitability trends over the next twelve months.

Concerns as to transport costs eased from the five year high reported in the previous survey. Nevertheless, transport costs together with raw material costs were the once again the most widely cited pressure on prices.

### Investment

Investment changes were at the margin, affecting only a third of respondents.

### Finance

A more modest rising trend in cash flow was reported and expectations as to trends in turnover improved for a further quarter. However, respondents are more cautious as to the trends in profitability over the next twelve months, and a slight net decline is now forecast.

### Employment

Rising trends in employment were reported as 42% sought to recruit staff. 27% increased pay by an average of 3.16%.

**Table 3: Wholesale distribution – key results**

	Q2 2005		
	Up	Level	Down
Business Optimism	21.2	45.5	33.3
Trend in actual sales	33.3	39.4	27.3
Trend in expected sales	39.3	28.6	32.1
Investment plans	18.2	66.7	15.2
Cash flow past 3 months	30.3	48.5	21.2
Turnover next 12 months	48.5	30.3	21.2
Profitability next 12 months	28.1	40.6	31.3
Price change next 3 Months	42.8	43.8	12.5
Pressures to raise prices from			
Pay settlements	18		
Raw material costs	54		
Finance costs	9		
Other overheads	24		
Transport costs	61		
Employment trends			
Total actual employment	12.1	78.8	9.1
Expected next 3 months	21.4	71.4	7.1
Average pay increase	3.16		
Percent recruiting staff	42		
Recruitment difficulties	40		

## Retail distribution

### Optimism

For a further quarter the declining trends in confidence continued and deepened, as sales trends were again weaker than anticipated.

### Sales

Declining trends in sales were widespread with 50% of respondents reporting declining sales, and 46% anticipating declining sales in the third quarter.

For a further quarter competition, business and interest rates were again identified as the three factors most likely to inhibit sales over the next quarter.

### Investment

Changes in investment plans were at the margin, affecting only a third of respondents, nevertheless, a slight decline was reported.

### Finance

The rising cash flow trends ended and a decline was reported. Overall, respondents are again more concerned as to profitability and turnover trends over the next twelve months, with 38.9% anticipating declining turnover and 49.4% declining profitability over the next twelve months, although expectations as to turnover and profitability were stronger amongst larger retailers. Price pressures were again most strongly anticipated by smaller firms.

### Employment

The slight decline in employment re-emerged, and this decrease is expected to continue through the third quarter. 46% recruited staff, and 47% reported difficulties in recruiting suitable staffs. 41% increased pay by an average of 4.12% (compared to 3.88% in the previous quarter).

**Table 4: Retail distribution – key results**

	Q2 2005		
	Up	Level	Down
Business Optimism	8.9	45.6	45.6
Trend in actual sales	13.5	36.0	50.6
Trend in expected sales	11.8	42.4	45.9
Investment plans	14.6	66.3	19.1
Cash flow past 3 months	12.4	61.8	25.8
Turnover next 12 months	22.2	38.9	38.9
Profitability next 12 months	19.1	31.5	49.4
Price change next 3 months	37.8	53.3	8.9

Pressures to raise prices from	
Pay settlements	28
Raw material costs	23
Finance costs	18
Other overheads	48
Transport costs	43

### Employment trends

Total actual employment	13.8	71.3	14.9
Expected next 3 months	5.1	80.8	14.1

**Average pay increase** 4.12

Percent recruiting staff	46
Recruitment difficulties inc	18

## Tourism

### Optimism

A rising trend in business confidence was reported.

### Demand

The outturn in demand was marginally weaker than anticipated, nevertheless, for a further quarter rising trends in demand were reported for total, rest of UK and Scottish demand, although demand from abroad remained weaker than a year ago. Average occupancy, at 70%, was at the same level as a year ago

Overall 34% of business was local trade [22% in quarter two 2004], 43% tourist trade [51% in quarter two 2004] and 32% business trade [31% in quarter two 2004].

### Finance

The rising trends in turnover and profitability continued, although at more modest rates than a year ago. The rise in room rates, continued, but was slightly less than had been forecast.

Concerns as to the lack of demand were generally lower than in the second quarters in previous years.

### Employment

Changes in employment were reported by 27% of respondents, and the increase was mainly in the increased employment of part time staffs.

### Recruitment

81% sought to recruit staff, and 31% reported that difficulties in recruiting staff had increased, overall 70% of those recruiting reported difficulties in recruiting suitable

staffs, most notably in the recruitment of chefs/cooks. 44% increased pay by an average of 5.7%.

**Table 5: Tourism – key results**

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	Q2 2005		
	Up	Level	Down
Business Optimism	32.4	41.2	26.5
Trends in demand/visitors			
Total demand/visitors	41.2	32.4	26.5
Demand from Scotland	30.2	52.4	17.5
Demand from Rest of UK	23.4	56.3	20.3
Demand from abroad	24.6	38.5	36.9
Business Trade	31.1	41.0	27.9
Trends in expected demand			
Total demand/visitors	35.4	43.1	21.5
Demand from Scotland	16.9	66.1	16.9
Demand from Rest of UK	22.4	63.8	13.8
Demand from abroad	28.8	45.8	25.4
Business Trade	21.1	49.1	29.8
Capacity used	70		
Investment	25.8	60.6	13.6
Turnover past 3 months	42.9	40.5	16.7
Profitability past 3 months	47.6	42.9	22.7
Average daily rate	35.4	50.8	13.8
Expected average daily rate	33.8	53.8	12.3
Employment trends			
Total actual employment	16.4	73.1	10.4
Expected next 3 months	14.5	82.9	1.6
Average pay increase	5.7		
Percent recruiting staff	81.4		
Recruitment difficulties	70		

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