

The Scottish economy

Forecasts of the Scottish economy

Economic background

There are now clear signs of recovery in the US although this is proving to be slightly delayed and relatively weak due to the fall in equity markets. The potential for conflict with Iraq has also increased tension and raised the degree of uncertainty in the world economy. Japan remains a problem but the rest of the Asia region appears to be recovering relatively well. The recovery in the Euro Area is still in the very early stages and both France and Germany are likely to perform less well than their neighbours.

The UK economy is relatively well positioned to pick up again next year with forecast growth of 1.6% this year and 2.6% next year. Inflation, interest rates and unemployment remain at historically low levels in the UK and macroeconomic policy has been stable but supportive. Consumption remains relatively strong in the UK although the recovery is expected to be export led. There are signs that business confidence, investment and profits will be more promising next year. The labour market has weakened slightly since the last quarter.

Both consumption and government spending remain important components of demand in Scotland. Tourist expenditure growth has improved slightly but it is expected that activity will accelerate further from 2004 onwards. The service sector continues to drive growth particularly financial services and real estate and business services. Both inward investment and transport and communication services could be slow to grow given the current uncertainty in the economy.

All economies are at risk from another significant stock market correction or from any conflict in the Gulf. The main problems are likely to be higher oil prices leading to increased inflation and a decrease in consumer spending as household wealth shrinks. Debt is unlikely to be a significant problem because the payback ratios remain high even though the level of debt has increased.

The forecast in detail

GVA

Our forecast for GVA is presented in Table 1. The Scottish Executive has revised the GVA index for 2001 with the result that growth was 0.84% compared to our forecast of 0.7%. Table 1 contains our forecasts for the period 2002 through to 2004. We are forecasting that GVA growth will be 0.7% in 2002, down from 0.9% in the last QEC. For 2003 we forecast growth of 1.4%, which is marginally up on our last forecast of 1.3%. In 2004 we forecast that GVA growth

will be 1.9% and this is substantially up on the 1.6% forecast last quarter. The outlook for the Scottish economy still remains relatively promising from 2003 onwards however we expect growth beyond 2003 to tail off slightly. The delayed recovery in the world economy may push more economic activity into 2004 rather than 2003. The main Scottish forecasts are presented in Table 1.

Table 1: Main forecasts of the Scottish economy, 2002-2004

	2002	2003	2004
GVA	0.7%	1.4%	1.9%
Agriculture	0.4%	0.3%	0.4%
Manufacturing	-2.9%	-0.1%	1.8%
Manufacturing (ex Electronics)	-2.0%	-0.7%	1.7%
Construction	-1.1%	1.6%	2.7%
Services	2.1%	2.0%	2.0%

Source: Fraser of Allander Institute, September 2002

Output

Our forecast for Agriculture is that there is unlikely to be any significant growth over the forecast period although we expect growth to be positive in each of the years in this sector. There still appears to be significant problems in the sector although there has been a vast improvement in the past two years. Construction is forecast to contract by 1.1% in 2002. We forecast growth of 1.6% in 2003 and 2.7% in 2004. Government investment is expected to make an important contribution to construction in 2003 and 2004.

Manufacturing continues to shed jobs and output has declined significantly. There is clear evidence of a two-speed economy when we compare the performance of the manufacturing and service sectors. Several sectors have had relatively poor output growth for some time now. A small number of sectors do actually perform very well. There are only a few signs of ICT demand increasing in the form of new and replacement investment. If this growth continues then this could be of considerable help to the Scottish ICT sector. We expect that the recovery in electronics will be long and slow. Our forecast is for positive growth to return to the sector in 2003. We also forecast that manufacturing will continue to contract in the next two years but positive growth is forecast for 2004.

As previously mentioned, services continue to drive growth in the Scottish economy. Both financial services and real estate and business services have experienced considerable growth. The forecast is for these sectors to outperform the other service sectors. Tourism does not appear to significantly stimulate demand until 2004. Services are forecast to grow at 2.1% in 2002 and by 2.0% in both of the following years.

Employment

Our forecasts of employment are given in Table 2 with the net employment change figure given in brackets. Total employment is forecast to increase from 2,185,300 in 2002 to 2,231,500 in 2003. A further rise to 2,255,000 in 2004 is also forecast. We are forecasting a net job loss of 5,800 in 2002 but thereafter we are forecasting significant job creation as economic conditions improve. Again employment growth is driven by the service sector.

The employment data has been recalibrated using the quarterly employment estimates. The preliminary indications are that manufacturing is likely to lose 13,700 jobs in 2002 and 3,300 in 2003. We are forecasting a net job gain of 5,000 in 2004 for manufacturing. Most manufacturing sectors are forecast to have job losses in 2002. Manufacturing employment is forecast to fall from 275,000 in 2002 to 271,700 in 2003. In 2004 we forecast that manufacturing employment will rise to 276,800.

Construction employment is forecast to be stable around 125,000 in 2002 and 2003. In 2004 it is forecast to increase to 128,000 following significant output growth in the sector. Agricultural employment is forecast to be stable around the 35,000 mark for the period of the forecast.

Table 2: Forecasts of Scottish employment and net employment change, 2002-2004

	2002	2003	2004
Total Employment (000s)	2,185.3 (-5,800)	2,231.5 (35,200)	2,255.0 (23,700)
Agriculture	34.5 (900)	35.4 (0)	35.5 (100)
Manufacturing	275.0 (-13,700)	271.7 (-3,300)	276.8 (5,000)
Construction	125.6 (600)	125.5 (-100)	128.0 (2,600)
Services	1,727.0 (10,800)	1,766.2 (39,200)	1,782.3 (16,100)

Source: Fraser of Allander Institute, September 2002.

Unemployment

Our forecasts of unemployment are presented in Table 3. ILO Unemployment is forecast to be 168,000 in 2002 or 6.6% and to fall to 159,600 (6.2%) in 2004. Claimant count unemployment is also forecast to fall across the forecast horizon. It is forecast to be 103,200 (4.2%) in 2002 but to steadily decline to 96,700 (3.9%). There are changes in the

labour market because there are considerable job losses in manufacturing but this is not leading to significantly higher unemployment as the service sector is providing many more job opportunities.

Table 3: Forecasts of Scottish unemployment, 2002-2004

	2002	2003	2004
ILO Unemployment (levels)	168,000	164,200	159,600
Rate	6.6%	6.4%	6.2%
Claimant Count (levels)	103,200	97,200	96,700
Rate	4.2%	3.9%	3.9%

Source: Fraser of Allander Institute, September 2002.

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