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# FRASER of ALLANDER INSTITUTE

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The Fraser of Allander Institute for Research on the Scottish Economy was established in the University of Strathclyde on 1 January 1975, as the result of a generous donation from the Hugh Fraser Foundation. Its principal function is to carry out research on the Scottish economy and its research programme includes the analysis of short term movements in economic activity. The results of this work, carried out in conjunction with the Department of Economics, are published in the Institute's Quarterly Economic Commentary. The Institute also publishes a series of Research Monographs and a series of Discussion Papers to provide an outlet for original research on medium term and long term aspects of the Scottish economy.

## Information for subscribers

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## Notes to contributors

The editor welcomes contributions to the Briefing Paper, Feature Article and Economic Perspective sections. Material submitted should be of interest to a predominantly Scottish readership and written in a style intelligible to a non-specialist audience. Footnotes and references should conform to recent issues of the Commentary. Contributions should be typed and two copies submitted to the Editor.

Editor: James Love

Editorial Assistant: Joan Bennett

Contributors: John Blackhall, Margaret Chalmers, Paul Draper, John Heeley, Iain Jenkins, Cliff Lockyer, Jim H Love, Jim McGilvray, Peter McGregor, Iain McNicoll, Mike McVey, Noreen O'Donnell, Jim Stevens, David Simpson, Elizabeth Tait and Jim Walker.

Graphics: John Blackhall

Production: Sheelagh Blackhall and Isobel Sheppard



The Fraser of Allander Institute  
Curran Building  
100 Cathedral Street  
GLASGOW G4 0LN

041-552 4400 Ext. 3958

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# QUARTERLY ECONOMIC COMMENTARY

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# Outlook and Appraisal

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The Scottish economy, like that of the UK as a whole, looks set to experience a substantial shift in the relative importance of the factors determining growth in the coming year. As discussed elsewhere in the **Commentary** (see **British Economy**), growth in the recent past has been driven mainly by the expansion of investment and exports. With the inter-related factors of sterling's strength and continuing high real UK interest rates operating against a background of some deceleration in the growth of world trade, the prospect is that these influences will be largely replaced by the re-emergence of consumers' expenditure as the principal determinant of growth.

Signs of this shift are already apparent in the results obtained from the **Scottish Business Survey**. After the pattern of cautious optimism detected among manufacturers in this year's three previous **Surveys**, the results of the October **Survey** indicate that this optimism has largely evaporated. Only limited increases in exports are forecast in the coming months, investment intentions remain largely unchanged and the manufacturing sector is operating with spare capacity. In contrast, the results for the service sector, and most notably retailing, suggest a far greater degree of optimism. Retailers report continuing sales growth and upward revisions to investment intentions to overcome the major constraint on their activity, that of insufficient floorspace. The strength of the underlying "consumer boom" is reaffirmed by the actual and expected growth in personal advances reported by Scottish financial institutions.

Differential performance across sectors has obvious implications for employment patterns and prospects. Over the past few years there has been a clearly discernible shift in Scotland to greater dependence on employment in services (see **Labour Market** section for relevant Scottish data). With the changing relative importance of the determinants of growth likely to reinforce the increasing importance of the service sector and with

the expansion of services the object of much policy concern in Scotland, it is appropriate to consider more closely the implications for the Scottish economy of the changing balance between manufacturing and service sector employment.

It is frequently contended that the increasing importance of the service sector is an inherent consequence of economic growth. The exact nature of this argument, however, has not been fully defined. In part, it seems to rest on the view that as economies grow an increasing proportion of resources is devoted to provision of services such as health, education and transport. Much of such provision in the UK tends to fall within the domain of the public sector. Given the incidence of constraints on government expenditure, however, this element of the argument holds little water in a Scottish context. Overall, services such as public administration and defence, education and health have contributed little to the recent net increases in service sector employment.

A second strand of the argument hinges on the significance of changing patterns of consumers' expenditure. As income expands, the share devoted to satisfaction of basic needs falls and that devoted to consumption of "luxuries" rises. At least implicitly, satisfaction of basic needs is equated with consumption of manufactured goods while satisfaction of "luxury" demand is equated with consumption of services. Three important observations must be made on this strand of the argument. First, it does not follow that manufacturing employment need fall in absolute terms. In the Scottish experience, however, the shifting employment balance is not attributable to increases in service sector employment against a background of simultaneous, but lesser, increases in manufacturing employment. Rather Scotland has experienced only modest increases in the former and a sharp decline in the latter. Secondly, the shift in the balance in Scotland has proceeded further than in the UK as a whole and has accelerated more

markedly in recent years than might be expected in the context of an argument framed in terms of secular income change.

Thirdly, it is often inappropriate to divorce consumption of manufactured goods and consumption of services. Undoubtedly, higher incomes generate increased demand for, for example, leisure and entertainment. The services desired may, however, be supplied in many cases by consumer durables. Much of the demand for leisure and entertainment spills over into the market for consumer durables such as video-recorders, home computers and televisions. The Scottish pattern is one in which such goods are increasingly produced elsewhere and Scottish demand for services therefore supports manufacturing jobs outside Scotland.

The extent to which the expansion of services can effectively replace jobs lost in manufacturing is a problematic issue. Given Scotland's small, open economy, past employment has depended heavily on the production of exportables. Typically, there is less scope for trade in services than for trade in manufactures. Certain banking, insurance and consultancy services can be traded internationally. However, even within the financial sector expansion of retail banking, for example, does not generate internationally tradeable services. This is self-evidently true also of much of the distribution sector. In terms then of Scotland's (non-oil) tradeable sector, the impact on Scottish employment of a greater dependence on imports of manufactured goods is unlikely to be offset by the employment effects of increased exports of services.

Moreover, domestically there is an inter-relationship between the manufacturing and service sectors. Services are supplied directly to manufacturing companies and also to customers whose income is derived from employment in manufacturing. Contraction of the manufacturing base, thus, also influences the service sector. Closure of the Ravenscraig complex, for example, would adversely affect suppliers of services, such as road haulage, and through the associated loss of income would affect suppliers of other services, as in retailing, in North Lanarkshire.

Given the decline of Scotland's

manufacturing base, it is difficult to deny the importance of employment expansion in other sectors of the economy. Much is made in official circles of the numbers of jobs created over the recent past and, indeed, since March 1984 successive quarters have shown increases in the total numbers of employees in employment in Scotland. These increases reflect lower employment in production and construction industries, including manufacturing, and increased employment in services. But tied in with this industrial composition effect there has been a substitution of part-time, and mainly female, employment for full-time male employment. The attraction to employers of part-time employment is that such employment provides greater flexibility of labour inputs. In large part that greater flexibility arises because part-time workers are cheaper to employ and lay-off. Setting numbers of part-time job gains directly against numbers of full-time job losses, however, overstates the extent of the increase in employment measured on a full-time equivalent basis.

As well as the distinction between numbers of jobs and their full-time equivalents, a distinction must be drawn between job creation and the creation of wealth. Much of the employment created is not only part-time but low-paid. This is particularly true of the distribution sector.

The pattern of employment creation in services also reinforces the structural change that has been taking place in the labour market. Creation of part-time employment absorbs workers, predominantly female, who previously were not registered as available for work. Expansion of services, thus, makes little impact on the rate of registered unemployment.

Rather than being symptomatic of a strong economy, the expansion of services in Scotland appears more as a sign of the continuing weakness of the manufacturing base. The outlook for employment prospects next year, with continuing high interest rates and the strong pound underpinning the changes in the pattern of growth, holds little promise of improvement.

14 November 1985