

## 3 Review of Scottish Business Surveys

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### Abstract

Business surveys provide a useful barometer of the investment and business intentions across the Scottish economy. The business surveys reviewed in this section provide an overview of key recent evidence in the Scottish economy. Up until recently, many surveys have been bullish but 2015 Q3 surveys suggest that the recovery has perhaps plateaued rather than beginning to slow. Since the start of 2015, businesses in Scotland have maintained positive confidence and output levels although the rates of increase have slowed. Nevertheless, key benchmarks are stronger than their long-term averages with many remaining at or above their pre-recession levels. Respondents, on balance, also continued to be positive about the prospects for the remainder of 2015.

### The Bank of Scotland Purchasing Managers' Index (PMI)

During September 2015 the The Bank of Scotland Purchasing Managers' Index (PMI) saw a broad-based contraction in the private sector as output in Scotland declined for the first time in six months – from 50.8 in August to 49 in September. Both the service and manufacturing sectors reported decreases in output. During August output moderated as the seasonally-adjusted PMI fell to 50.8 in August, down from 52.2 in July. During July, the data had signalled a further rise in activity at Scottish private sector companies, as highlighted by the index remaining above the 50.0 at a no-change level of 52.2. This was up from 51.2 in June and the index had seen its most marked rise in output since December 2014.

### The Bank of Scotland Business Monitor (SBM)

The latest Scottish Business Monitor (SBM) from The Bank of Scotland, reporting on results for June, July and August 2015 and expectations to February 2016, show the Scottish economy continuing to recover from the slowdown experienced at the start of the year. It reported that new business levels picked up strongly during the summer and that expectations for the next six months continue to signal moderate growth for the remainder of 2015.

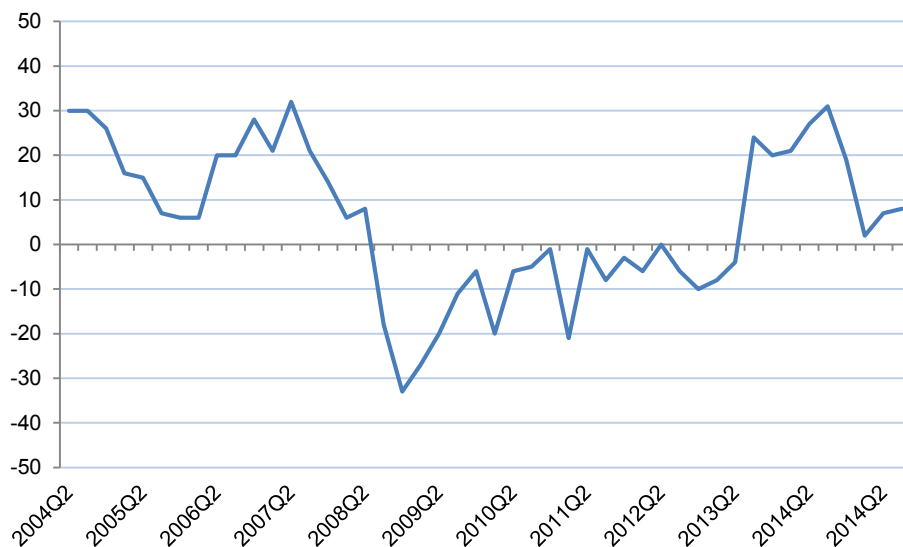
In the three months ending August 2015 a net balance of +8% (marginally up from the +7% of the previous quarter but well down from the +30% of the same quarter one year ago) reported a rise in turnover. Production firms reported a rise of +3% and service firms reported a rise of +11%. A net balance of +15% expect a rise in turnover in the period ending February 2016. Service firms remain more optimistic than production firms, with service firms showing an overall net balance for turnover for the next six months at +22% compared to +8% for production firms.

Volumes of repeat business improved slightly in the current SBM and the overall net balance of +2% was up slightly from 0% of the previous quarter (see figure 1), although worse than the +15% of the same quarter one year ago. Trends in the volume of new business were stronger with a net balance of

+17% compared to +3% of the previous quarter and close to the +23% of the same quarter one year ago.

Export activity continued to decline (-9%) in the current quarter but the rate of decline slowed from the -24% of the previous survey. During the next six months a net balance of -13% expect a fall in export orders - down on the -6% of last quarter and significantly worse than the +32% of the same quarter one year ago.

**Figure 1: Total volume of business Scotland, 2004-2015 (net balance of SBM respondents)**



Source: Bank of Scotland Business Monitor

## Manufacturing

According to the Quarterly Economic Indicator (QEI) produced by the Scottish Chambers of Commerce, in collaboration with the Fraser of Allander Institute a net balance of +12% of Scottish manufactures reported a rise in optimism – down from the +25% in Q2. A net balance of +11% of respondents to the QEI reported a rise in total orders. Rest of UK orders continued to rise for a balance of +17% of firms; however firms, on balance, reported a decline in domestic Scottish orders (-3.4%) during Q3 2015. However the decline is forecast to be temporary with a net of +18% forecasting a rise. For the fourth consecutive quarter the positive trends in exports continued in Q3 2015, with a net positive balance of firms reporting rises for both export orders and export sales revenue (net balances of +18% and +16% respectively). 67% of manufacturers expect orders to remain unchanged or increase, and +6% expect export sales revenue to be maintained or to increase.

Respondents to the Scottish Engineering Quarterly Review reported that optimism generally remained negative, especially for small and medium sized firms (SMEs). Total order intake remains negative with a net of +11% of reporting a decline. Small, medium and large companies all reported negative net balances and across manufacturing sectors there were no positive returns. Electronics (a net balance of

-9%), and fabricators (a net balance of -5%) were the least negative and mechanical equipment (a net balance of -26%) was the most negative. UK orders in general declined with small and medium companies reporting a net decline, although a net of large companies reported a rise. A net of +24% reported a decline in export orders compared to Q2.

Investment trends among QEI firms eased from previous quarters although fewer than 9% of businesses reduced total investment expenditure over the quarter, giving a net balance of +20%. A net balance of +12% of firms reported a rise in total employment levels, slightly lower than had been forecast by respondents in the previous survey.

For the first time since Q1 2010, Scottish Engineering Quarterly Review respondents reported that capital investment plans in general have dipped into a negative net balance (-1%). However only small firms reported a negative balance as both medium and large firms reported net increases (+8% and +33% respectively). Across individual sectors, metal manufacturing, non-metal products and transport reported positive results. Training investment plans in general remained positive. Employee levels generally remained unchanged for a net of firms and a small net balance are forecasting a rise in Q4 2015. Overall, output volumes remained negative. Small and medium sized firms, on balance, reported a decline while large companies reported a rise.

### **Construction**

According to the QEI the construction sector experienced continued growth in Q3 2015 with many positive key trends that are expected to remain positive throughout Q4 2015. A net balance of +20% of construction firms reported a rise in total contracts with this increase largely attributed to a rise in private sector commercial contracts, increasing for 40% of all firms. However results from public sector contracts remained depressed with a net balance of +5% of firms reporting a fall. 53.1% of businesses expect no change to the prices they charge during Q4 2015. Pressures to raise prices eased among construction firms in Q3 2015, although 47% remained under pressure to raise prices due to wage costs.

The latest Scottish Construction Monitor, the quarterly survey prepared on behalf of the trade body Scottish Building Federation (SBF), found confidence levels stood at +21 in the third quarter of the year down 14 points from a record high of +35 in the previous quarter. Respondents saw business confidence fall back to levels similar to those in the first half of 2014. The drop followed three consecutive quarters of rising confidence, although this was the ninth consecutive quarter in which confidence has been rated positive overall.

A net balance of +32% of QEI firms reported a rise in expenditure on investment, with positive trends reported for both training and capital investment with net balances of +34% and +23% respectively. Investment expenditure is expected to continue to grow in Q4 2015, with a net balance of +16% forecasting a further rise.

Fewer than 9% of QEI firms reduced employment over the quarter and the net balance of +33% is higher than at any other time since Q2 2007. Employment levels are expected to be maintained in Q4 2015 with 57% of businesses expecting no change and 35% anticipating an increase. Almost two thirds

of firms were actively recruiting staff during Q3 2015 and of these 48% had experienced recruitment difficulties.

## Retail

Sales revenue improved for a net balance of retail/wholesale QEI firms and a net of +20% expect a further rise in Q4 2015. Most businesses do not expect their prices to change in Q4 2015 (58%) although a net balance of +22% are forecasting a rise. A net of +5% reported an increase in profits compared to a net of -5% in the previous quarter.

The latest Scottish Retail Consortium-KPMG monitor reported that September 2015 was a more upbeat month for Scotland's retailers and that despite total sales being down again, it was the best performance since October 2014 (once Easter distortions were factored in). Like-for-like sales which exclude factors such as new store openings were down by -1.7% on September 2014 and worryingly the gap with the UK widened. Overall, sales were down -1.3% on last year but non-food sales grew slightly, with clothing, footwear, furniture and home categories driving sales; online sales performed reasonably well (up almost +2%). Food continued to struggle, as sales continued to decline in real terms as they have for the previous 22 months.

A net balance of +8% of QEI firms reported a reduction in total employment levels although no firms expect to reduce employment numbers in Q4 2015 and a quarter of firms expect to increase total employment levels.

## Tourism

A net balance of +31% of QEI firms reported a rise in optimism. Compared to the same quarter last year, a net balance of +63% of tourism firms reported that the total number of guests/customers had increased and fewer than 15% reported a decrease. The breakdown shows that a net balance of firms reported a rise in guests from all origins; from Scotland (+32%), rest of UK (+35%), rest of EU (+20%), and outwith of the EU (+31%). A net balance of +52% reported a rise in total sales revenue, with only 8% of firms reporting a decrease over the quarter.

A net balance of +39% of QEI firms in the tourism sector reported an increase in profits during Q3 2015 over the quarter, resulting in a positive net balance of +39% the highest level recorded in 2015. However, in keeping with seasonal trends this is unlikely to be sustained as 42% of firms are forecasting a decline in sales and 58% are expecting no change to the prices they charge.

A third of QEI tourism firms reported recruitment difficulties and skill shortages in this sector remain a significant challenge for businesses. More specifically, Chefs and front of house staff were the most frequently cited occupations that firms struggled to recruit. Employment levels increased with a net balance of +16% reporting a rise, although almost 40% of tourism businesses expect employment levels to decline in the next 3 months as they dispose of seasonal staff.

## Outlook

Generally, the overall economic picture is still positive but these surveys indicate that the speed of the recovery in the Scottish economy is perhaps starting to slow. Firms continued to report growth, but it was down on the previous quarter. However, expectations remain buoyant, suggesting the recovery will continue although here too the pace of increase is slowing. However, for some sectors trading conditions are still harsh, notably among exporters suggesting that aspects of the recovery remain fragile and policy action may be required to ensure that it is sustainable. The Scottish Chamber of Commerce survey noted a slowdown in investment trends for training and equipment which have dipped this quarter. These are typically indicators related to confidence and any drop in confidence should be a cautionary reminder. Confidence levels among Scottish businesses need to reach and maintain a point where firms have the confidence to invest for the longer term.

## References

Lloyds TSB [Business Monitor](#) Issue 71, June – August 2015

[Scottish Chambers' Commerce Quarterly Economic Indicator](#), Q3 2015

[Scottish Engineering Quarterly Review](#), Q3 2015

[The Bank of Scotland Market Economics Regional Monthly Purchasing Managers' Indices \(PMI\), August-October 2015](#)

[The Scottish Retail Consortium's KPMG Monthly Scottish Retail Sales Monitor](#), September 2015

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