

3 Review of Scottish Business Surveys

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Abstract

The business surveys reviewed in this section provide a barometer for the Scottish economy and outlined below is an overview of key recent evidence. These 2014 Q1 surveys suggest that the recovery evident from recent previous surveys has been cemented with growth across all main sectors gathering pace. Since the start of 2014 businesses in Scotland have maintained the positive confidence levels evident from previous surveys. Key benchmarks are stronger than their long-term averages with many now higher than their pre-recession levels. Respondents to many of the surveys, on balance, reported strong performances of the key indicators and also continued to be positive about the prospects for the rest of 2014. However, some warn that the recovery still remains fragile and may be at risk from domestic and foreign uncertainties.

Private Sector

The Bank of Scotland PMI - a single-figure measure of the month-on-month change in combined manufacturing and services business activity - for February 2014 was 56.2, indicating a further increase in the combined output of Scotland's manufacturing and service sectors. Employment rose at the fastest rate in the surveys history during February. In March 2014 the Index rose to 56.4, signalling improving business confidence and leading to increases in output, new business and employment. The March survey also highlighted an easing of inflationary pressures with the rate of increase of input/output prices slowing. The latest figure available is for April when the index stood at 54.8 showing continued growth albeit at a slower rate than in March. The gap between Scotland and the rest of the UK widened in April with the UK index rising to 59.2. However there was a further decline in new export orders, possibly fuelled by the strength of Sterling. The May PMI, at 54, was down on the April 2014 index and was also the lowest figure since April 2013, indicating a slowing in the rate of growth.

The Bank of Scotland group also produce a quarterly business survey, the Scottish Business Monitor (SBM) that analyses the production and service sectors. The latest issue showed Scotland's economy continued to strengthen at the start of this year, with improvements on both the previous quarter and on the same quarter one year ago. Both service and manufacturing firms showed signs of improvement.

Firms exhibited an optimistic outlook with a net balance of firms reporting increased turnover during the three months to the end of February 2014. The survey also found that expectations for the six months to August 2014 were at their highest level since before the recession in 2007. In the latest survey, 40% of Scottish production firms reported a rise in turnover while 24% experienced a decline and in the services sector 42% reported a rise and 22% recorded a fall (a net balance of +20%). This was a marked turnaround compared to the same period a year earlier where a net balance of -9% service sector firms reported a drop in sales.

Export activity improved and respondents are upbeat about export prospects in the six months to August 2014 as a net 42% of firms predict a rise. This highlighted a significant improvement from a balance of 21% forecasting a rise in exports in the previous quarterly survey. In the Q1 survey, 35% of producers reported a rise in export activity and 24% experienced a fall and among services companies, 29% recorded a rise and 15% reported a decline in export activity.

Manufacturing

During the first three months of 2014 business confidence continued to improve for a net of 18% of SCBS firms, a significant improvement from the 18.6% for Q1 2013. Only 11% of firms reported being less confident compared to Q4 2013. In general terms optimism levels also remained high among respondents to the Scottish Engineering Quarterly Review for Q1/14.

During Q1/14 the trend in total new orders improved markedly for SCBS firms (from a net balance of 13.1% to 30.5%) with 44% of all firms reporting a rise. Orders from all areas improved. Respondents continue to remain optimistic as to the trends in future orders during Q2/14 (+17.8%) with orders from all areas set to rise. Average capacity utilisation eased from 78.1% to 77% although was almost two percentage points higher than the Q1/13 figure. The manufacturers organisation, EEF in association with the accountancy firm BDO, reported that a net balance of firms reported a rise in orders and that a net of 31% expects a further rise, although disappointingly export orders fell short of expectations from the previous quarter survey.

Respondents to the Scottish Engineering Quarterly Review for Q1/14 reported that their total order intake increased. Small companies remained positive and appeared to be holding up the sector as medium companies reported a decline and large companies reported no overall change. Within the sector, electronics and machine shops and metal manufacturing were positive whereas fabricators reported no net change. Maintaining the pattern over the last 16 quarters UK orders in general remained healthy and this trend is expected to continue in Q2. Export orders in general declined for a net balance of 3% of firms although a net balance of 13% expect an increase in Q2.

Once again turnover and profitability are expected to rise for a net balance of Chamber of Commerce surveyed firms over the coming 12 month period. Both net balances are at their highest levels since 2007. The trends in investment in plant/machinery improved during Q1/14 for a net balance of SCBS manufacturing respondents (+15.7%). New investment continues to be directed towards replacement (29%) or to improve efficiency (36%) although a significant number are also reporting expansion as a reason (29%). Small and medium companies replying to the Scottish Engineering Quarterly Review are positive regarding investment intentions.

A net balance of SCBS firms reported a rise in total employment levels (+21%). Almost a third of firms increased pay during Q1 and the average increase remained at 3.3%. 52% (compared to 48% in the previous quarter) reported seeking to recruit staff, and almost half of these firms reported increased recruitment difficulties. Staffing levels in Q1/14 and forecasts for the next three months in general remained positive for Scottish Engineering firms.

Construction

The rising trend in business optimism among SCBS respondents continued into Q1/14 with a net balance of respondents reporting a positive net balance of optimism (+20.7%); only 13.8% reported a decline in business optimism. Following the rapid increase in Q4/13 the trend in total new orders dropped back but remained positive in Q1/14 and is expected to remain positive through Q2. Orders from all areas generally improved and all are expected to rise again in the three months to the end of June. Capacity utilisation eased from 82.3% to 77.6%.

Cash flow trends continued to deteriorate for a net balance of SCBS construction firms (-6.9%) although the decline eased from the previous quarter (-11.5%). Turnover is expected to increase for more than half of firms and a net balance now anticipate an increase in profits suggesting that the long term trend in pressure on margins may be beginning to ease. Indeed a net balance of firms reported that tender margins, in the next 12 months, are set to rise.

As forecast there was a net rise in total employment levels in Q1 among Chamber of Commerce respondents although most firms continued to report no change; a net balance (+7.7%) expect a further rise in Q2. Recruitment activity eased (from 46% to 31%) although recruitment problems increased with firms specifying problems attracting suitable professional and technical staff. Average pay increases decreased marginally from 2.9% in Q4/13 to 2.4%.

Latest Scottish Construction Monitor quarterly survey for Q1/14, conducted by the Scottish Building Federation suggests confidence in the construction sector has now returned to pre-banking crash levels. The latest Monitor found more than half – 51.6 per cent – of firms who responded in the first three months of the year are more confident about their prospects in the coming 12 months. This was the third consecutive report showing a rise in business confidence. The Scottish Building Federation however warned that while the survey results were encouraging, the outlook remained mixed across different sectors and that while there had been strong growth in infrastructure and private commercial activity, house building remained flat.

Wholesale distribution

The downward trend in business optimism amongst Scottish SCBS wholesalers continued, though eased, and more than two thirds continued to report no change. The downward trend in sales eased further from -5.6% in Q4 to 0%. Once again the net balance in sales was better than had been expected by respondents in the previous survey, and a net balance of +6.6% expect a rise in the first quarter of 2014.

Overall cost pressures appear to be easing, although more than half of SCBS respondents reported increased pressures from transport costs and other overheads and to a lesser extent, firms also remain under pressure from raw material costs (47%). More than half of firms (52.9%) expect to increase prices over the next three months. The long running downward trend in turnover ended with a net balance of 5.9% expecting a rise in the coming year whereas the downward trend in profitability continued, though eased in Q1. More than 80% of firms reported no change to investment plans although the remaining firms reported an increase.

SCBS wholesale respondents unexpectedly report a net increase in overall employment levels during Q1/14. Recruitment activity eased as did recruitment difficulties. The average pay increase in Q1/14 was 4.7% compared to 2.5% in Q4/13 (few than 20% reported an increase).

Retail distribution

Compared to the previous quarter business confidence eased in Q1/14 for a net balance of -5.5% of SCBS firms; despite the decline the net balance remained significantly higher than the balance in Q1/13 (-45.2%). Overall sales unexpectedly declined as a net balance of 18.5% reported a drop in sales in Q1, however a net balance of 4.4% expects a rise in Q2. This remains an improvement over the same period of 2013 when a net of 47.6% reported a decline in sales.

Cost pressures remain historically high and SCBS firms continued to cite raw material prices and utility costs. Pressures on margins appear to have increased slightly in Q1. A net balance of 12% expect a rise in turnover although a net of -14.6% expect a decline in profitability (compared to -2.1% in the previous quarter).

The trend in total employment remained flat for SCBS firms with more than 80% reporting no net change to total levels. A third of firms reported increasing pay, and the average increase eased from 6.5% to 4.4%.

Following a strong start to 2014 the Scottish Retail Consortium reported that in March 2014 total Scottish sales decreased by 2.5% compared with March 2013, when they had increased by 1.8% although argued that the timing of Easter this year distorted and exaggerated the decline in like-for-like spending figures. Like-for-like sales decreased by 3.8% on last March, when they had increased by 0.9%. Taking account of shop price deflation, March total sales were down 0.8% in real terms.

Tourism

The upward trend in tourism optimism continued with only 10% of SCBS hoteliers indicating that they were feeling less confident during Q1/14. Demand generally continued to improve and exceeded expectations with a net balance of 20.7% reporting a rise. There was however a net decline in demand from the rest of UK although this decline is expected to be temporary. More than half expect no change to demand levels in Q2. Demand from all areas is expected to improve in Q2.

Average occupancy eased from 65% to 56%, Q1 occupancy levels are normally low. During Q1 trends in bar/restaurant trade improved as did the demand for the use of conference/function facilities. A net balance (+7.7%) reported a rise in the average daily room rate and a net of 28.3% expect a rise in Q2.

Only 58% of SCBS firms (compared to 71% previously) reported the lack of tourist demand as the primary business constraint. Poor transport infrastructure and high fuel costs are becoming of increasing concern. Around half of hotels sought to recruit staff and recruitment problems are becoming more evident with a number of hotels reporting difficulties attracting suitable chefs/cooks, bar/waiting staff and managerial staff. Total employment trends declined although a rise is forecast for Q2.

Overall accommodation occupancy levels for January 2014, compiled by Visit Scotland generally recorded increases compared to January 2013. Hotel room occupancy for the month of January 2014

was generally down compared to January 2013. However they reported that growth in room occupancy was recorded in Fife, Glasgow & Clyde, Dumfries & Galloway, Edinburgh & Lothians, and Perthshire. Guest House and B&B room occupancy improved in Glasgow & Clyde, and Highlands. Self-Catering unit occupancy rose during January 2014, with the majority of areas recording growth.

Outlook

Generally, the speed of the recovery in the Scottish economy is continuing to gather pace and is becoming more broadly based. Expectations for 2014 are at their highest level since 2007, suggesting the recovery will continue and will become increasingly rooted. However, for some sectors trading conditions are still harsh suggesting that aspects of the recovery remain fragile and policy action may be required to ensure that it is sustainable. Growth is still, to an extent, reliant on household spending and in order to sustain growth over the longer term, an increase in investment and net exports as well as manufacturing and construction activity is needed. The recovery in Europe, where half of our exports go, remains fairly subdued therefore the challenge now must be to ensure that the recovery is sustainable in the longer term. Confidence levels among Scottish businesses need to reach and maintain a point where firms have the confidence to invest for the longer term.

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

Lloyds TSB Business Monitor Issue 65 December 2013 – February 2014;

Scottish Chambers' Business Survey Q1 2014

Scottish Engineering Quarterly Review Q1 2014;

The Bank of Scotland Markit Economics Regional Monthly Purchasing Managers' Indices (PMI) for February 2014 – May 2014;

The Scottish Retail Consortium's KPMG Monthly Scottish Retail Sales Monitor for March 2014

Visit Scotland Occupancy surveys for Q1 2014.

EEF and BDO Manufacturing Outlook Survey, Quarter 2 2014