



SCOTTISH CHAMBERS
OF COMMERCE

MEDIA RELEASE

Immediate Release

INTEREST RATE HIKES CAST SHADOW OVER GENERALLY POSITIVE OUTLOOK FOR SCOTTISH FIRMS

The Scottish Chambers of Commerce today released its Business Survey results for the second quarter of 2007. The long-established review, carried out on its behalf by the University of Strathclyde's Fraser of Allander Institute, reveals a continuing high level of business optimism, but the effects of five interest rate rises over the past year are causing concern among retailers, manufacturers and the tourist industry.

Liz Cameron, Executive Director of Scottish Chambers of Commerce, said:

"The results of our latest survey paint a largely positive picture of the Scottish economy, consistent with the healthy pattern of growth we have been experiencing since 2003. This is particularly true of the construction and tourism sectors, whilst optimism among manufacturers has shown a positive trend for the tenth consecutive quarter.

"However it is also becoming clear that the Bank of England's five interest rate rises over the course of the past year are impacting across a range of sectors. High exchange rates are worrying a number of businesses in the manufacturing industry, with the outturn in export orders weaker than anticipated and little improvement forecast for the next quarter.

"General optimism within the tourism sector must be tempered with recent feedback from our members on the ground that the strength of the pound is causing concern to a number of businesses. Although the larger hotels are enjoying robust trade this is not the case with many smaller businesses. A high exchange rate can be damaging to our tourism sector on two fronts. On the one hand, it can make Scotland a more expensive option for foreign tourists, whilst on the other it makes destinations abroad more attractive for UK residents. With this week's inflation figures sparking concerns of further interest rate rises, the Monetary Policy Committee of the Bank of England must keep in mind the potential effects on one of Scotland's most important industries when it next meets on 2nd August.

"It is important to ensure that the current positive investment trends in manufacturing, retail and tourism are sustained and not undercut by further interest rate increases and the strength of the exchange rate. The Bank of England's interest rate tool is double edged and must be used with very great care if we are to avoid damaging those industries which have the potential to take our growth up to the next level. It is important that all Scottish politicians, both in Holyrood and Westminster, are equally concerned if we are to sustain and increase the rate of economic growth in Scotland."

BUSINESS PERFORMANCE

Summary Points

Business confidence	Rising confidence was again reported in manufacturing, construction, and tourism. Business confidence declined for a net of wholesale and retail respondents, although within retail confidence rose amongst nationally based retailers;
Demand/sales	<p>In all sectors the trends in demand/sales were stronger than in the second quarters of 2006 and 2005. For a further quarter rising trends in total, Scottish and export demand were reported by a net of manufacturing respondents. Construction firms again reported rising orders;</p> <p>Rising trends in sales were reported among wholesale respondents, and in retail there were again marked distinctions between national/multiple retailers reporting strongly rising sales volumes and independent retailers reporting weaker sales trends. Overall in retail a slightly rising trend in the value of sales was reported. In the tourism sector strongly rising trends in visitor numbers/demand were reported, with strong demand for accommodation and rising trends in the use of restaurant/bar and function/conference facilities;</p>
Capacity/work in progress	Rising trends in work in progress were again reported by a net of manufacturing and construction firms;
Cost pressures	Concerns over raw material costs remained evident in the second quarter, being cited by 72% of manufacturing and 44% of wholesale and retail respondents. Expectations of price increases in the third quarter of 2007 ranged from 26% of manufacturing, to 52% of retail and 56% of wholesale respondents;
Pay	Pay increases in the second quarter ranged from 3.5% in wholesale distribution to 6.2% in construction, pay pressures were strongest where recruitment difficulties were most widely reported, namely in construction and tourism;
Outlook	Rising trends in demand in manufacturing, but some signs of an easing in the rising trends of work in progress, nevertheless, investment for expansion is stronger than last year. However, concerns as to the loss of jobs to lower cost economies remain. In construction optimism remains strong for the next twelve months, but concerns as to pressures on margins is more evident.

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 June 2007 to early July 2007, almost 300 firms responded to the questionnaire.

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MANUFACTURING

Optimism

Business confidence continued to rise in the second quarter, but at the lowest rate the 4th quarter of 2005.

Orders and Sales

The current rising trends in total, Scottish orders are the strongest reported for 10 years. Export orders continued to rise for a net of firms, although respondents commented as to the adverse effect of current exchange rates and the continued migration of jobs offshore. These rising trends are expected to continue through the third quarter. However, there are some signs that the rate of increase in work levels may be slackening, as rising trends in the level of work in progress were reported by 12% (compared to 32%, in the previous quarter). Average capacity eased to 78.1%, and 49% reported capacity used was below preferred levels. Expectations for demand and turnover for the next twelve months remain strong, but have eased compared to the end of March and concerns remain as to trends in profitability through 2007.

Raw material costs, reported by 72%, were again the most widely reported cost pressure on prices.

Investment

26% reported revising investment upward and 7% leasing plans for the coming year. Investment in the second quarter was mainly directed towards increasing efficiency, expansion and replacing equipment, and 16% reported investment in new products/new markets.

Employment

Employment rose for a net of firms, and 19% reported increased hours worked. 54% sought to recruit mainly skilled and other manual staffs.

	Q2.2007			Net Balances		
	Up	Level	Down	Q2/07	Q1/07	Q4/06
Business Optimism	21.4	57.5	21.1	0.3	6.6	17.6
Trends in actual orders						
Total new orders	46.5	33.2	20.4	26.1	22.8	15.9
Scottish orders	32.3	46.8	20.9	11.4	9.5	-2.6
Rest of UK orders	28.5	54.8	16.7	11.8	-4.9	8.1
Export orders [38.8% = N/A]	17.3	28.3	15.6	1.7	12.4	3.6
Trends in expected orders						
Total new orders	25.7	63.4	10.9	14.8	22.7	24.7
Scottish orders	19.1	70.5	10.4	9.3	15.1	11.9
Rest of UK orders	18.6	71.0	10.4	8.2	3.7	11.3
Export orders [39.5% = N/A]	11.9	38.1	10.6	1.3	13	8.9
Av Capacity used	78.1			78.1	79.2	77.3
Invest in plant/equip.	25.9	63.7	10.4	15.5	13.2	9.6
Cash flow past 3 moths	35.2	18.4	16.4	18.8	-19.3	2.1
Turnover next 12 moths	49.2	39.1	11.7	37.5	44.7	36.2
Profitability next 12 moths	33.1	41.9	25.0	8.1	6.3	26.4
Price change next 3 moths	26.3	68.2	5.5	20.8	30.4	49.0
Pressures to raise prices from						
Pay settlements	24.6			24.6	42.9	42
Raw material costs	72.1			72.1	72.5	77
Finance costs	11.8			11.8	18.5	12
Other overheads	35.2			35.2	37.1	55
Transport costs	32.8			32.8	51.5	48
Employment trends						
Total actual employment	24.5	56.2	19.3	5.2	-6	1.6
Total expected next 3 months	16.7	72.9	10.4	6.3	9.5	0.5
Average pay increase	3.83			3.83	4.7	4.66

CONSTRUCTION

Optimism

Business confidence rose reflecting rising trends in orders and work in progress.

Contracts

Rising trends in new contracts were widely reported in the three months to June and 58% (90% in the previous quarter) expect level or rising trends in the level of work through the next six months.

Average capacity used rose to 91.14%. Work in progress rose in the second quarter, although the trends were more modest than in the first quarter, and the rising trend in work in progress is expected to continue.

For a further quarter respondents remain confident as to rising trends in turnover and 45% (60% in the previous quarter) anticipate rising profitability over the next twelve months.

60% reported shortages of skilled labour, 50% the level of contracts and new work, 43% planning delays and 38% the availability of contractors as the factors most likely to restrict activity over the next quarter.

Employment

The rising trend in employment continued and strengthened, but overtime levels eased. Increased use of sub contractors is again anticipated over the next three months.

	Q2.2007			Net Balances		
	Up	Level	Down	Q2/07	Q1/07	Q4/06
Business Optimism	23.8	61.9	14.3	9.5	0	6.2
Trends in actual contracts						
Total new contracts	42.9	47.6	9.5	33.4	40	3.1
Public sector orders	31.4	42.9	25.7	5.7	37.5	8.7
Private commercial	29.4	61.8	8.8	20.6	23	4.0
Domestic/house build	30.6	50.0	19.4	11.2	14.3	0.0
Trends in expected contracts						
Total new orders	23.8	54.8	21.4	2.4	55.6	20.4
Public sector orders	24.2	45.5	30.3	-6.1	42.9	21.8
Private commercial	21.9	65.6	12.5	9.4	28.6	12.0
Domestic/house build	17.1	62.9	20.0	-2.9	57	-3.8
Trends in work in progress						
Actual	47.6	42.9	9.5	38.1	50	-3.1
Expected	35.7	50.0	14.3	21.4	40	26.6
Capacity used	91.14			91.14	88.2	81.4
Invest in plant/equip.					0	9.7
Leasing in plant/equipment.					-11.1	-3.3
Employment trends						
Total actual employment	45.2	47.6	7.1	38.1	30	15.6
Total expected next 3 months	32.5	67.5	0.0	32.5	20	6.5
Average pay increase	6.24			6.24	na	5.19
Percent recruiting staff	66.7			66.7	66.7	50.0
Recruitment difficulties increasing	23.5			23.5	12.5	43.5

WHOLESALE DISTRIBUTION

Optimism

Changes to business confidence were at the margin, being reported by 25%. Nevertheless, a declining trend was reported, as firms noted rising competition from larger firms.

Sales

The outturn in sales was more modest than had been anticipated, and firms are more cautious as to trading conditions in the third quarter of 2007, and anticipate only a level trend in sales.

Price pressures eased and 56% (70% in the previous quarter) anticipate price increases. 75% reported pressures to raise prices due to transport costs, 44% pressures from material costs and 25% pressures from pay settlements.

Only a quarter (50% in the previous quarter) anticipate rising turnover over the next year and a net of firms anticipate declining profitability over the next 12 months, suggesting pressures on margins will again be evident.

Finance

Changes to investment plans were limited, being reported by 25% and a declining trend in investment intentions was reported.

Employment

Changes in employment levels were again limited, affecting 40% of firms; nevertheless, the modestly rising trend in employment continued. 37.5% sought to recruit staff, and 12% increased pay by an average of 3.5%.

	Q2.2007			Net Balances		
	Up	Level	Down	Q2/07	Q1/07	Q4/06
Business Optimism	6.3	75.0	18.8	-12.5	0.0	-6.7
Trend in actual sales	31.3	50.0	18.8	12.5	19.0	0.0
Trend in expected sales	20.0	60.0	20.0	0.0	33.3	0.0
Investment plans	6.3	75.0	18.8	-12.5	-9.6	0
Cash flow past 3 months	18.8	62.5	18.8	0.0	-4.8	-6.7
Turnover next 12 months	12.5	62.5	25.0	-12.5	38.1	26.7
Profitability next 12 months	25.0	43.8	31.3	-6.3	-5	-6.7
Price change next 3 months	56.3	25.0	18.8	37.5	66.7	66.7
Pressures to raise prices from						
Pay settlements	25.0			25.0	33.3	46.7
Raw material costs	43.8			43.8	66.7	60.0
Finance costs	18.8			18.8	23.8	13.3
Other overheads	31.3			31.3	42.9	46.7
Transport costs	75.0			75.0	81	66.7
Employment trends						
Total actual employment	26.7	60.0	13.3	13.3	9.5	-6.7
Expected next 3 months	15.4	84.6	0.0	15.4	10.0	0.0
Average pay increase	3.5			3.5	4.55	3.8
Percent recruiting staff	37.5			37.5	52.4	46.7
Recruitment difficulties inc	25.0			25.0	20.0	18.2

RETAIL DISTRIBUTION

Optimism

Optimism remained strong and rising amongst national retailers but continued to decline for a net of independent shops. A number of respondents raised concerns as to the impact of recent interest rate increases on spending levels.

Sales

31% of independent retailers reported a decline in the actual value of sales in the second quarter, and 26% anticipate declining sales in the third quarter. In contrast, over 60% of national retailers reported and 56% expect increased value in sales.

Amongst all retailers competition (reported by 46%), legislation and regulation (reported by 34%) were identified as the factors likely to inhibit sales. Amongst smaller and independent stores concerns as to competition from larger, national retailers was reported.

48% reported utility and 44% material costs as to the two main cost pressures. Cost pressures were more widely reported by independent retailers.

Finance

More than 51% of independent retailers anticipate no changes to turnover, and 46% no change to profitability over the next year, however, 23% anticipate declining turnover and 26% declining profitability over the next year. In contrast 60% of the national retailers anticipate rising turnover and 80% rising profitability over the next year.

Employment

Changes in employment levels were reported by 19%. 33% sought to recruit staff.

	Q2.2007			Net Balances		
	Level	Up	Down	Q2/07	Q1/07	Q4/06
Business Optimism	16.4	57.4	26.2	-9.8	-22	21.6
Trend in actual sales	25.0	48.3	26.7	-1.7	-4	-11.7
Trend in expected sales	24.5	54.7	20.8	3.7	-8.9	-23.6
Investment plans	23.3	55.0	21.7	1.6	2	-1.7
Cash flow past 3 months	18.3	66.7	15.0	3.3	4.2	-8.4
Turnover next 12 months	35.0	46.7	18.3	16.7	6.1	0.0
Profitability next 12 months	41.7	38.3	20.0	21.7	-4.1	-15.5
Price change next 3 months	52.5	41.0	6.6	45.9	50.0	50.0
Pressures to raise prices from						
Pay settlements	32.8			32.8	40	23
Raw material costs	44.3			44.3	46	40
Finance costs	26.2			26.2	24	25
Other overheads	18.0			18.0	14	8
Transport costs	39.3			39.3	44	47
Utility costs	47.5			47.5	54	63
Regulation costs	34.3			34.3	40	30
Employment trends						
Total actual employment	10.2	81.4	8.5	1.7	-8.2	1.7
Expected next 3 months	12.2	77.6	10.2	2.0	4.5	-1.9
Average pay increase	3.97			3.97	3.34	4.18
Percent recruiting staff	33.3			33.3	38.0	35.0
Recruitment difficulties inc	17.2			17.2	32.1	50.0

TOURISM

Optimism

The net rising trend in business confidence remained marginally lower than a year ago.

Demand

A strongly rising trend in demand was reported, with rising trends in total numbers of visitors and rising demand from Scotland, the rest of UK and abroad stronger than for the past three years. 70% reported increased demand for accommodation, 46% increased numbers in restaurants and 31% increased demand. Average occupancy was reported at 77.4%.

Overall 43.8% of business in the second quarter was tourist trade, 28.2% local trade, and 28% business trade.

A net of 49% reported rising turnover and a net of 19% rising trends in margins.

Business constraints

45% (60% in the previous quarter) reported the lack of demand as the main business constraint in the second quarter, 39% the high exchange rates, 38% poor transport infrastructure and 27% the weak marketing of their area.

Employment

Changes in employment levels were again limited, being reported by 30% and with rising trends in full time, part time, and seasonal staffs. Falling levels of overtime working were reported by 32%.

Recruitment

82% sought to recruit staff, and half of those recruiting reported difficulties in recruiting suitable staffs, most notably in the recruitment of chefs/cooks and bar/restaurant staff. 29% increased pay by an average of 5.17%.

	Q2.2007			Net Balances		
	Up	Level	Down	Q2/07	Q1/07	Q4/06
Business Optimism	32.1	50.0	17.9	14.2	5.4	2.3
Trends in demand/visitors						
Total demand/visitors	63.6	23.6	12.7	50.9	5.6	0.0
Demand from Scotland	42.6	48.1	9.3	33.3	-2.9	-7.3
Demand from Rest of UK	52.7	34.5	12.7	40.0	0.0	-2.4
Demand from abroad	43.6	30.9	25.5	18.1	-39.4	-20.0
Business Trade	41.5	50.9	7.5	34.0	11.8	7.5
Trends in expected demand						
Total demand/visitors	51.9	34.6	13.5	38.4	41.2	7.5
Demand from Scotland	29.2	60.4	10.4	18.8	18.8	10.8
Demand from Rest of UK	37.5	52.1	10.4	27.1	18.8	0.0
Demand from abroad	36.7	40.8	22.4	14.3	9.4	-13.5
Business Trade	28.9	64.4	6.7	22.2	6.7	2.7
Occupancy	77.43			77.43		63.3
Average daily rate	43.4	45.3	11.3	32.1	11.1	15.0
Expected average daily rate	34.6	57.7	7.7	26.9	30.6	8.4
Employment trends						
Total actual employment	21.6	70.6	7.8	13.8	-17.6	-5.1
Expected next 3 months	26.0	72.0	2.0	24.0	31.4	-14.2
Average pay increase	5.17			5.17	3.1	5.35
Percent recruiting staff	82.1			82.1	48.6	64.3
Recruitment difficulties	49.0			49.0	37.5	50.0

Methodology

The Scottish Chambers' Business survey, in common with most national surveys, seeks evidence as to changing trends, and uses net balances as the key survey statistic. Most questions ask the respondent to indicate whether the trend, over the past three months, and expected for the next three months, is either 'up', 'level' or 'down'. The net balance for such survey questions is defined as the number of 'up' responses minus the number of 'down' responses to each survey question. Hence a positive net balance indicates a rising trend, and a negative net balance a declining trend. Net balances for the current quarter, together with those for the previous quarter and the quarter a year ago have been added to the usual results.

Size band analysis is based on the number of employees in manufacturing, construction and wholesale, on the number of rooms in tourism and on ownership and location patterns together with number of full time equivalents in retail.

This information is part of the data collected by the quarterly surveys, further information can be provided, but a charge will be made, depending on the time to organise and present the data.

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