

Quarter 1 2017

Quarterly Economic Indicator

Scottish Chambers of Commerce



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Methodology

The Quarterly Economic Indicator is owned and produced by the Scottish Chambers of Commerce Economic Development Intelligence Unit, in collaboration with the Fraser of Allander Institute of the University of Strathclyde.

This survey was conducted between 20 February 2017 and 13 March 2017. 470 firms responded to the Q1 2017 edition of the Indicator.

Results are reported as the “net % balance”, calculated by deducting the % of firms reporting a decrease from the % of firms reporting an increase.

E.g. If 50% of firms report an increase in profits over the quarter (compared with the previous quarter) and 49% report a decrease, the net % balance of firms reporting an increase in profits is $(50-49 = +1)$.

A negative net % balance generally indicates contraction and a positive net % balance expansion.

The Economic Development Intelligence Unit is available to be commissioned for a wide range of economic and business related research. For more information on the Unit, further information on the Quarterly Economic Indicator results, or details of sponsorship availability, please contact:

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Summary

In the first quarter of 2017, business performance in Scotland continued to be subdued, with signs of mixed expectations among firms. Profitability and cash flow remain challenging and pressures on prices continue to be high.

The construction sector reported a slight weakening in performance and optimism since last quarter and is significantly down on Q1 2016. Optimism is now at its lowest since Q3 2014, with employment also at its lowest trend level since Q4 2013. Despite this, a quarter of businesses are recruiting and they continue to report high levels of recruitment difficulties.

The financial and business services sector reported its highest levels of optimism since Q4 2014. This may reflect the fact that over a third of oil and gas businesses are now more positive about the future. Although cashflow and profitability are still in negative territory, investment is still growing and overall performance is much improved since Q1 2016.

The manufacturing sector is reporting growing optimism after a mixed year in 2016. Domestic orders and sales revenues are flat but performance has been boosted by the rest of the UK and export markets. There are positive signs for employment but, again, recruitment difficulties are increasing.

Retail and wholesalers have reported optimism back in negative territory, with sales revenues at their weakest since Q4 2015 and cashflow at its weakest since Q4 2015. Price change expectations at their highest since Q3 2011, when CPI inflation reached a peak of 5.2%.

Tourism businesses are reporting negative optimism for the first time since Q1 2016, with sales revenues down across the board for the second consecutive quarter. Overall investment is down for first time since we began measuring this in Q4 2014. Despite a fall in the number of EU and international guests, overall visitor numbers up and negativity in the sector at this stage may be as a result of seasonal factors and the impact of business rates increases.

Key Findings

CONSTRUCTION

Business Optimism

Although optimism remains in positive territory, it has been weakening since Q2 of 2016. There are positive trend balances for expected sales revenue and employment in Q2 2017. However, it should be noted that the net % balance of +2 is significantly lower than that recorded in Q1 2016, at +20.

Price Change

Generally, pressure to raise prices appears to have grown amongst businesses in the construction sector, with a higher percentage of firms citing upwards pressure from wages compared with Q4 2016. **42.9% of businesses expect to increase the prices they charge in Q2 and the net % balance of +43 recorded for expected price change is the highest reported since at least Q2 2016.** These trends reflect a rise in the UK rate of inflation over the quarter, as measured by the Consumers Price Index (CPI), at 2.3% in February and March, having risen from 1.9% in January.

FINANCIAL & BUSINESS SERVICES

Employment

Last quarter firms in the financial & business service sector generally said they expected to increase employment in Q1 2017, reflected by a net % balance of +12 recorded for employment expectations over the next three months. However, these expectations of increased employment do not appear to have been realised with the net % balance of -8 recorded for employment, the second consecutive quarter that trends in actual employment have been in negative territory. **Employment levels are expected either increase or remain the same in Q2 by 93.0% of businesses, as only 7.0% of businesses in the sector anticipate a decline in employment levels over the next three months.**

Profit

For the eighth consecutive quarter negative net % balances were recorded for both profits and cash-flow. This suggests an overall decline in profitability and cash-flow levels in the industry. Prices charged by firms are largely expected to remain unchanged (61% expect no change to the prices they charge) next quarter but more than half of firms (50.9%) expect sales revenue to increase. In all, this sector appears to be at a turning point, with many of the key balances improved.

Key Findings

MANUFACTURING

Optimism/Exports

Business optimism in the sector was strong at +11 – the highest trend balance since Q4 2015 and a significant pick up from +2 last quarter. Total export sales are strong at +24 and have been in positive territory for four consecutive quarters. The figures for Q4 2016 and Q1 2017 have been particularly strong, perhaps reflecting the stronger export potential in the light of the sustained weakness in sterling following the EU referendum.

Investment

The same number of firms reported an increase in total investment as those that reported a decrease, a net % balance of 0 firms. This is the lowest trend balance recorded since records began in Q4 2014. However, positive trend balances were recorded for capital and training investment of +6 and +4 respectively.

Profits/Cash-flow

The net % balances for profit levels returned to negative territory (-4), and although the balance was only marginally negative, this suggests an overall decline in profitability levels in the industry. Conversely, a positive net % balance was recorded for cashflow of +6.

RETAIL & WHOLESALE

Optimism

Over one third of respondents (36.8%) experienced a fall in business optimism in Q1 2017, giving a negative net % balance of -8 and marking a return to negative territory, which suggests an overall decline in the industry, and may explain the negative net % balance of -27 reported for cash-flow, as well as declines in sales employment, profitability and capacity.

Employment

Recent positive employment trends in the industry did not continue in the first quarter of 2017, with a net % balance of -8 reporting a decrease in staffing levels. However, only 10.3% of businesses anticipate a decline in employment over the next three months.

Approximately 41.0% of firms actively sought to recruit, lowest since Q1 2015, yet recruitment problems appear to have increased marginally over the quarter with 43.8% of firms recruiting indicating that they are currently facing difficulties.

Key Findings

TOURISM

Sales Revenue

For the second consecutive quarter, despite tourism firms reporting a positive trend balance of +13 for total guest/customers versus last year, sales revenue fell over the quarter, reflected in the net % balance of -13 recorded. This can be attributed to negative trend balances from domestic (Scotland), sales from the rest of the UK and online sales of -13, -10 and -4 respectively. However, expectations for sales revenue over the next quarter are positive with a net % balance of +32.

Investment

Total investment levels fell over the quarter with a net % balance of -2 recorded, this level is much lower than the +13 net % balance reported the same time last year. This trend is expected to continue in the second quarter of 2017 as a net % balance of -7 anticipate declining levels of investment expenditure over the next three months,

Employment

Over the quarter businesses in the tourism industry reported a decline in employment levels, reflected by a net % balance of -14. However, there has been growth in terms of the number of businesses currently recruiting in the sector (61.4%), which may in turn explain the positive trend balance recorded for employment expectations over the next three months, with 29.8% of respondents stating that employment levels were likely to increase in Q2 2017 (net % balance of +18). Yet, recruitment difficulties are still a major issue facing businesses in tourism sector, as stated by approximately 41% of businesses.

Construction

SALES REVENUE

The same number of businesses reported an increase in sales revenue over the quarter as those that reported a decrease: a net % balance of 0. This is the lowest net % balance recorded since the first quarter of 2015 and can be attributed to negative trend balances from domestic (Scotland) sales of -5.

CONTRACTS

Overall contracts grew in Q1 for a net % balance of +8 of firms. However, this was slightly lower than the level recorded last quarter. Additionally, there was a further fall in domestic/house build contracts, with a net % balance of -8. There was also a negative net % balance of -3 recorded for private commercial contracts.

PROFIT

Profits continued to fall, with 42.9% of businesses experiencing a decrease over the first quarter of 2017, giving a net % balance of -24- the lowest figure recorded since Q1 2015.

CASH-FLOW

More firms experienced a decline in cashflow than an increase in Q1 (net % balance of -24). This marks the second consecutive quarter the net % balance for cashflow has been negative.

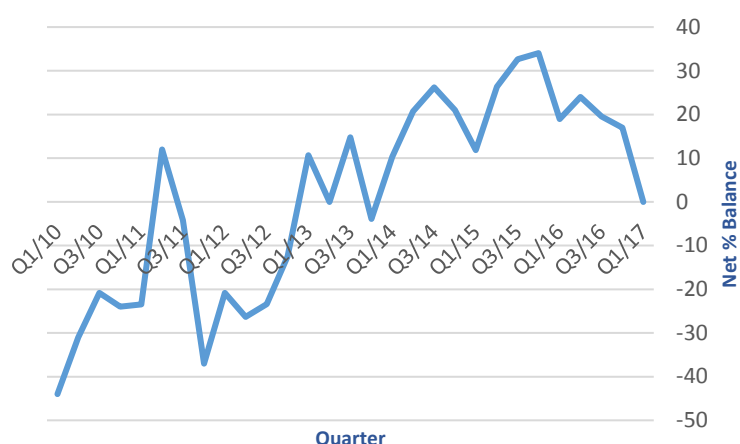
RECRUITMENT

The percentage of firms that tried to recruit last quarter and reported difficulties (61.5%) was higher than at any other time since the record for this began in Q4 2014.

EMPLOYMENT

52.4% of firms reported that employment levels were unchanged in Q1, giving a net % balance of 0- the lowest figure recorded since Q4 2013. Employment is expected to increase in Q2.

Employment



(balances may not add up to 100% due to N/A responses)				Q1/17	Q4/16	Q1/16
(figures given as % of respondents)	Up	Level	Down	Net % Balance	Last Quarter	Last Year
Business Optimism	26.2	50.0	23.8	2	4	20
Sales Revenue						
Total	24.4	51.2	24.4	0	8	26
Domestic (Scotland)	18.4	44.7	23.7	-5	6	21
Rest of UK	14.3	31.4	11.4	3	-2	9
Contracts						
Total	30.8	46.2	23.1	8	9	24
Public Sector	21.6	37.8	21.6	0	-7	6
Private Commercial	16.7	55.6	19.4	-3	9	6
House Building	5.3	34.2	13.2	-8	-2	2
Work In Progress	28.9	52.6	18.4	11	4	43
Investment						
Total	26.2	54.8	19.0	7	22	7
Capital	27.5	50.0	22.5	5	20	-3
Training	36.8	47.4	7.9	29	20	24
Cashflow	11.9	52.4	35.7	-24	-4	-2
Applied for Credit?				27	24	27
Profits	19.0	38.1	42.9	-24	6	11
Capacity Used (Ave. %)				79	83	83
Employment						
Total	23.8	52.4	23.8	0	17	19
Recruiting Staff			(yes)	63	56	68
Recruitment Difficulties			(yes)	62	43	58
Increased Wages?			(yes)	39	31	39
Average Pay Increase (%)				4.2	7	5
Expectations Next Quarter						
Price Change	42.9	57.1	0.0	43	33	46
Sales Revenue	41.5	39.0	19.5	22	6	53
Investment	23.8	50.0	23.8	0	-2	10
Employees	36.6	48.8	14.6	22	7	39

Financial & Business Services

BUSINESS OPTIMISM

Business optimism increased in Q1 for a net % balance of +16 firms, the highest net % balance recorded since Q1 2015, and follows a negative trend balance of -4 in Q4 2016.

SALES REVENUE

Over Q1 2017 total sales revenue increased for just over one third of businesses (38.2%). There was growth in export sales, a net % balance of +10 reporting an increase, the highest figure recorded since Q3 2014. There was also a positive trend balance of +2 for online sales. Domestic (Scotland sales) fell on balance (net % balance of -1), marking the 6th consecutive quarter for which the trend balance has been negative. The net % balance for sales revenue from the rest of UK was 0 – the first time since Q4 2014 that this has not been negative.

INVESTMENT

There was a slight slowdown in the growth of investment expenditure shown by a net % balance of +6 firms increasing investment in Q1 2017, compared to +7 in Q4 2016. The largest increase was in training investment expenditure, with a net % balance of +14. Conversely, capital investment was negative (net % balance of -1).

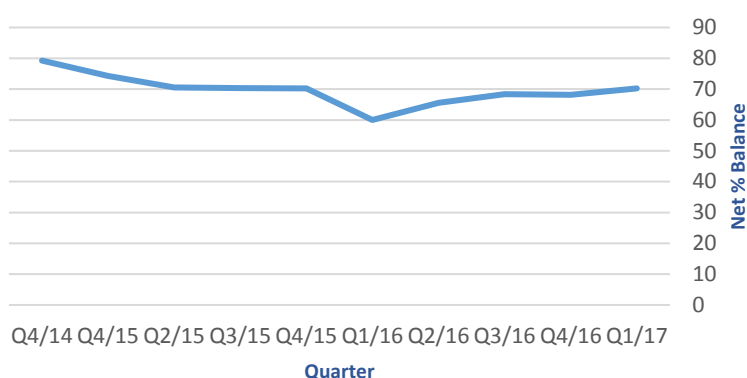
CAPACITY

The average capacity used for businesses in the financial & business services sector in Q1 was at its highest level (70.2%) since Q4 2015. Almost half of businesses (46%) said they were currently operating below optimum levels of capacity, but only 15.5% expect work in progress to decline next quarter.

EXPECTATIONS

Future expectations in term of sales revenue are positive as over half (50.9%) of firms expects sales revenue to increase in Q2 2017.

Capacity



(blank space indicates data not available)	(rounded up to nearest %)					
(balances may not add up to 100% due to N/A responses)				Q1/17	Q4/16	Q1/16
(figures given as % of respondents)	Up	Level	Down	Net % Balance	Last Quarter	Last Year
Business Optimism	36.8	42.7	20.5	16	-4	-14
Sales Revenue						
Total	38.2	31.2	29.4	9	1	-18
Domestic (Scotland)	28.9	33.1	30.1	-1	-3	-18
Rest of UK	16.7	34.0	16.7	0	-7	-12
Exports	19.5	18.9	9.8	10	-1	-22
Online	10.1	20.2	7.7	2	2	-11
Investment						
Total	22.4	45.3	16.5	6	7	-5
Capital	17.1	47.1	17.6	-1	-1	-8
Training	25.6	47.0	11.3	14	5	-2
Cashflow	19.9	42.1	35.1	-15	-7	-5
Applied for credit?			(yes)	7	9	9
Profits	26.8	37.5	32.7	-6	-6	-26
Capacity Used (Ave. %)				70	68	60
Employment						
Total	14.2	62.7	21.9	-8	-7	-6
Recruiting Staff			(yes)	34	38	46
Recruitment Difficulties			(yes)	29	28	33
Increased Wages?			(yes)	20	16	19
Average Pay Increase (%)				6.5	5	5
Expectations Next Quarter						
Price Change	34.3	60.9	4.7	30	18	1
Sales Revenue	50.9	29.6	18.9	32	16	7
Investment	23.1	53.3	13.0	10	4	-8
Employees	25.1	67.8	7.0	18	12	0

Manufacturing

ORDERS

The trend balance for total new contracts was positive over Q1 2017, with a net % balance of +13. Whilst there was growth in orders from the rest of the UK and exports over the quarter, with net % balances of +2 and +13 respectively; there was a net % balance of 0 for orders from Scotland, with the same number of businesses reporting an increase as those that reported a decrease.

DOMESTIC SALES REVENUE

There was a decline in domestic(Scotland) sales revenue in Q1 2017, with one quarter of respondents experiencing a fall (net % balance of -2). This is the first quarter that the trend balance has been negative since the same quarter last year.

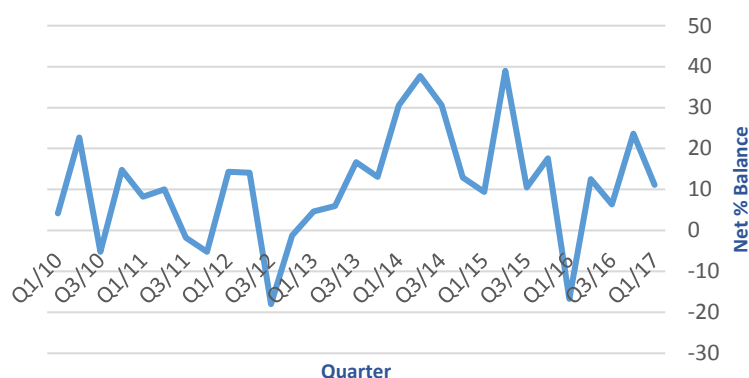
EMPLOYMENT

87.2% of businesses indicated that employment either increased or remained the same over the quarter. Approximately, 70% respondents stated that they were currently recruiting. However, 45.5% highlighted that they were currently experiencing difficulties. More specifically, technical/skilled staff were the most commonly cited by respondents as difficult to recruit.

PRICE CHANGE

The majority (57.4%) of businesses in the manufacturing sector expect to increase their prices in the second quarter of 2017.

Total New Orders



(blank space indicates data not available)	(rounded up to nearest %)					
(balances may not add up to 100% due to N/A responses)				Q1/17	Q4/16	Q1/16
(figures given as % of respondents)	Up	Level	Down	Net % Balance	Last Quarter	Last Year
Business Optimism	37.0	37.0	26.1	11	2	-10
Sales Revenue						
Total	38.3	36.2	25.5	13	22	-10
Domestic (Scotland)	23.9	43.5	26.1	-2	2	-15
Rest of UK	28.3	32.6	21.7	7	0	-8
Exports	31.1	28.9	6.7	24	28	-4
Orders						
Total	35.6	37.8	24.4	11	24	-17
Domestic (Scotland)	23.9	45.7	23.9	0	-7	-19
Rest of UK	23.9	32.6	21.7	2	6	-13
Exports	23.4	23.4	10.6	13	15	-15
Work in Progress	35.6	46.7	17.8	18	19	-8
Investment						
Total	23.4	46.8	23.4	0	16	21
Capital	29.8	38.3	23.4	6	15	15
Training	20.0	60.0	15.6	4	13	17
Cashflow	27.1	51.1	21.3	6	-15	-2
Applied for Credit?			(yes)	17	22	15
Profits	32.6	30.4	37.0	-4	0	-26
Capacity Used (Ave. %)				76	76	73
Employment						
Total	27.7	59.6	12.8	15	15	15
Recruiting Staff			(yes)	70	62	73
Recruitment Difficulties			(yes)	46	38	37
Increased Wages?			(yes)	14	24	15
Average Pay Increase (%)				4.9	4.5	2.6
Expectations Next Quarter						
Price Change	57.4	34.0	8.5	49	52	17
Sales Revenue	42.6	38.3	19.1	23	15	21
Investment	21.7	56.5	19.6	2	13	2
Employees	32.6	21.7	8.7	24	28	6

Retail & Wholesale

SALES REVENUE

A net % balance of -20 firms experienced a decrease in sales revenue in Q1, the lowest net % balance recorded since Q4 2015. However, this trend is not expected to continue in the second quarter of the year, with a net % balance of +20 anticipating an increase.

INVESTMENT

The same number of firms reported an increase in both total and capital investment as those that reported a decrease, resulting in a net % balance of 0 for both. However, the trend balance for training investment remained positive in Q1 2017 (+15).

CASH-FLOW

More firms reported a decrease in cashflow than an increase in Q1, a negative net % balance of -27. This was the 6th consecutive quarter of declining cashflow and the lowest trend balance recorded since Q4 2015.

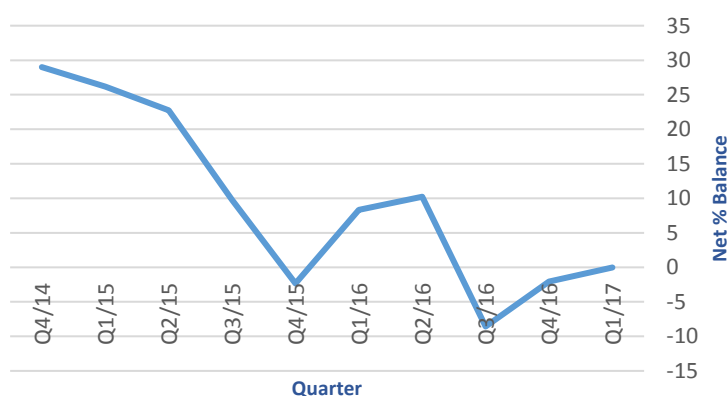
PROFIT

Q1 2017 was the 6th consecutive quarter where a net balance of firms in the sector reported a fall in profits, with a net % balance of -16.

PRICE CHANGE

The majority of businesses (67.5%) expect to increase their prices over the next three months. The most commonly cited price pressures included: raw material costs, wages, value of sterling and business rates. This is the highest level reported since Q3 of 2011, when CPI inflation reached 5.2%

Total Investment Expenditure



(blank space indicates data not available)	(rounded up to nearest %)					
(balances may not add up to 100% due to N/A responses)				Q1/17	Q4/16	Q1/16
(figures given as % of respondents)	Up	Level	Down	Net % Balance	Last Quarter	Last Year
Business Optimism	28.9	34.2	36.8	-8	2	10
Sales Revenue						
Total	25.0	22.5	45.0	-20	14	4
Domestic (Scotland)	26.3	23.7	28.9	-3	13	0
Rest of UK	7.9	13.2	18.4	-11	0	-7
Exports	5.4	2.7	0.0	5	11	4
Online	7.9	21.1	10.5	-3	4	19
Investment						
Total	15.4	41.0	15.4	0	-2	8
Capital	18.9	37.8	18.9	0	0	2
Training	20.5	41.0	5.1	15	8	2
Cashflow	16.2	32.4	43.2	-27	-6	-4
Applied for Credit?			(yes)	3	21	10
Profits	21.1	28.9	36.8	-16	-2	-4
Capacity Used (Ave. %)				72	75	74
Employment						
Total	10.5	63.2	18.4	-8	4	0
Recruiting Staff			(yes)	41	65	54
Recruitment Difficulties			(yes)	44	41	19
Increased Wages?			(yes)	36	30	35
Average Pay Increase (%)				4	4	5
Expectations Next Quarter						
Price Change	67.5	32.5	0.0	68	56	38
Sales Revenue	42.5	27.5	22.5	20	-2	25
Investment	25.0	45.0	12.5	13	2	11
Employees	15.4	74.4	10.3	5	10	6

Tourism

WAGES

Almost 30% of respondents increased wages over the quarter. Moreover, average wage increases continue to be higher than inflation, at 4.3%.

CASH-FLOW

More firms experienced a decline in cashflow than an increase in Q1, resulting in a net % balance of -21- the lowest figure recorded since record began in Q4 2014. A fall in cashflow levels may be explained by the number of firms experiencing a decrease in guests/customers from the rest of EU and outside the EU.

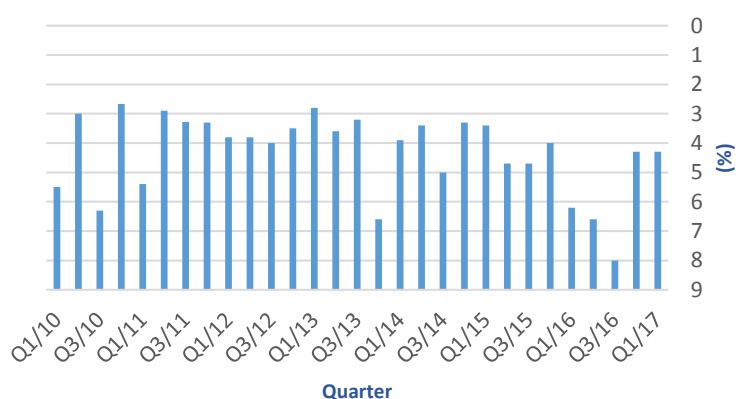
PROFITS

43.2% of respondents stated that profit levels were down in the first three months of 2017, giving a net % balance of -26. This is the lowest figure recorded since before records began in Q4 2014

EXPECTATIONS

Longer term expectations in the sector are positive, with a net % balance of +32 businesses expecting sales revenue to increase over the next quarter. However, a negative net % balance was recorded for future investment trends (-7).

Average Wage Increase



(blank space indicates data not available)				(rounded up to nearest %)		
(balances may not add up to 100% due to N/A responses)				Q1/17	Q4/16	Q1/16
(figures given as % of respondents)	Up	Level	Down	Net % Balance	Last Quarter	Last Year
Business Optimism (vs last quarter)	22.6	48.8	28.6	-6	3	-10
Sales Revenue						
Total	25.0	36.9	38.1	-13	-4	28
Domestic (Scotland)	21.4	33.3	34.5	-13	-4	25
Rest of UK	13.0	32.5	23.4	-10	-1	4
Online	15.9	29.3	19.5	-4	-7	17
Investment						
Total	22.0	43.9	24.4	-2	16	13
Capital	26.7	43.0	20.9	6	14	14
Training	20.7	50.0	11.0	10	17	10
Cashflow	15.5	44.0	36.9	-21	-15	-13
Applied for credit?			(yes)	19	8	27
Profits	17.3	32.1	43.2	-26	-18	-10
Employment						
Total	15.0	56.3	28.8	-14	-3	17
Recruiting Staff			(yes)	61	55	73
Recruitment Difficulties			(yes)	41	58	41
Increased Wages?			(yes)	28	29	28
Average Pay Increase (%)				4.3	4	6
Guests/Customers (vs last year)						
Total	39.0	34.1	25.6	13	24	17
From Scotland	31.8	35.3	29.4	2	8	23
From Rest of UK	28.9	38.6	22.9	6	4	0
From Rest of EU	14.8	43.2	24.7	-10	1	-10
From Outside the EU	19.8	33.3	24.7	-5	18	-3
Expectations Next Quarter						
Price Change	56.5	37.6	5.9	51	45	64
Sales Revenue	49.4	32.9	17.6	32	-12	40
Investment	19.3	49.4	26.5	-7	-1	20
Employees	29.8	58.3	11.9	18	7	34