

SCC QUARTERLY ECONOMIC INDICATOR: Q3 2018 REPORT

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SCOTTISH CHAMBERS OF COMMERCE SURVEY ILLUSTRATES ROBUST TRADING PERFORMANCE, BUT MANUFACTURING CONFIDENCE AND OVERALL INVESTMENT FALL AMID RISING MATERIAL COSTS AND UNCERTAIN POLITICAL ENVIRONMENT

The latest SCC Quarterly Economic Indicator Survey for Q3 of 2018 illustrates a broadly positive Scottish economy, but slowing investment across a range of sectors, and a challenging set of results for the manufacturing sector, suggest that the need for certainty on the UK's Exit for the European Union is paramount.

Driven by rising costs of raw materials, the manufacturing sector has posted its first negative result for optimism / business confidence since 2016, despite a reasonably strong set of financial results. Expectations in the sector for future revenue and investment both sit substantially lower than for the previous quarter.

The survey has also observed slowing investment trends generally throughout the third quarter, with all sectors bar retail experiencing a decline in investment relative to the second quarter.

Our results also show that external pressure continues to act as a challenge for some key sectors, with construction and manufacturing particularly impacted by the rising cost of raw materials. 63% of manufacturing firms indicated that rising raw material prices were acting as a growing cost pressure.

KEY FINDINGS / OVERALL NATIONAL RESULTS:

- Generally, robust financial results across sectors, but declining investment and expectations for the future.
- 21% of firms across the sample reported declining optimism, relative to 15% last quarter. This still suggests positive business confidence overall.
- 43% of firms reporting increased overall revenue, with only 17% reporting a decrease.
- 16% of firms reported declining business investment in this quarter, compared to 11% in Q2.
- On a sectoral basis: Construction, Business Services, Manufacturing and Tourism all report declining investment levels this quarter.
- Investment expectations for the future are slowing, with 27% of firms looking to increase investment this quarter, compared to 32% in Q2.
- On a sectoral basis: Investment expectations for the next quarter sit below average for Construction, Manufacturing, and Retail.

Commenting on the results, Neil Amner of Anderson Strathern and Chair of the Scottish Chambers of Commerce Economic Advisory Group, said:

“Our survey results for the third quarter of 2018 suggest that the Scottish economy continues to be resilient, but firms are becoming cautious as uncertainty grows around the future trading environment with the European Union. Investment in Q3 and future expectations of investment are beginning to show signs of slowing across many of the analysed sectors.

“Although optimism remains relatively strong throughout the national sample, levels of business confidence have also softened relative to the second quarter. It’s particularly concerning to see the manufacturing sector report a negative score for optimism. This is the first negative score reported since the third quarter of 2016, suggesting that the combination of rising material costs and continued uncertainty around future trading conditions are beginning to affect the confidence of businesses in this sector.”

Professor Graeme Roy, Director at the University of Strathclyde’s Fraser of Allander Institute said:

“This survey is further clear evidence of the importance of securing a smooth Brexit transition to protect Scotland’s economy. Whether you agree or disagree with the decision to leave the EU, it is essential that we have an orderly transition. The analysis undertaken by the Chambers of Commerce shows that it is vital that a deal is reached to enable firms to prepare and develop contingency plans. Crashing out of the EU in March next year threatens to severely impact on businesses right across the Scottish economy.”

On the UK’s Exit from the European Union, Neil Amner, said:

“A recent Chamber of Commerce survey illustrated that 62% of firms across the UK have not conducted a Brexit related risk assessment. This figure is higher in Scotland, at 67% of surveyed firms. Furthermore, 21% of firms across the UK intend to cut investment levels if a ‘no-deal’ scenario comes to pass. It’s difficult for firms, especially smaller businesses, to prepare without clarity on future arrangements. It is critical that the UK Government steps up to the plate to provide the certainty that business needs. Business communities need to see the UK Government working constructively with the whole of the UK and our EU partners to deliver certainty for business.”

On Investment, Neil Amner, continued:

“On investment, only the retail sector has observed a substantive increase in overall investment this quarter. Construction stands out as one sector which has seen substantive declines in investment figures, with the percentage balance figure for overall investment flat, and investment in capital now reported as negative for the first time since the first quarter of 2016. Based on reported investment expectations, the slowing investment levels observed this quarter appear on course to be replicated once more in the last quarter of the year. Pragmatic future arrangements with the EU, particularly a status quo transition period, must be confirmed in order to create a stable operating environment for future business investment.

“Furthermore, The Scottish Government must continue to do their part to encourage business investment at home. Policy in key devolved areas such as skills and non-domestic rates must provide certainty and focus on encouraging long term investment from businesses into their operations. A stable domestic environment will aid significantly in ensuring that investment levels persist throughout the Brexit negotiations.”

On Recruitment Challenges, Neil Amner, said:

“Recruitment difficulties continue to be a persistent business issue across all sectors. Almost 80% of businesses in tourism that attempted to recruit, found it a challenge to source workers, in part reflecting the increased tourism demand this quarter, and

perhaps also reflecting the reducing number of incoming migrants from the EU seeking work in the UK.”

ENDS

Notes to editors:

Scottish Chambers of Commerce’s Quarterly Economic Indicator engages with five of Scotland’s key business sectors: Construction, Financial and Business Services, Manufacturing, Retail & Wholesale, and Tourism.

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

This survey was conducted between September and October of 2018. 390 firms responded to the Q3 2018 edition of the Indicator.

SECTORAL RESULTS

CONSTRUCTION

- Optimism, contracts and revenue relatively positive.
- Investment in the third quarter lower across all recorded metrics (overall, capital, training).
- Positive profitability and cashflow results.
- Raw material prices increasing.
- Rising concerns around Business Rates + Inflation.
- Softening of recruitment difficulties despite stable number of firms recruiting.

FINANCIAL AND BUSINESS SERVICES

- Positive optimism results and broadly positive sales, although sales declined relative to Q2 2018.
- Recruitment difficulties at the second highest level on record for the sector.
- Cashflow and profitability positive, but down on the second quarter.
- Growing concerns around taxation, inflation and business rates.

MANUFACTURING

- First negative result for optimism since Q3 2016.
- Sales relatively strong, increased domestically and in the rest of the UK.
- Investment declined this quarter in all metrics, total investment back to lower levels observed in 2017.
- Cashflow and profitability returned to negative levels despite strong revenue figures.
- Raw material costs continued to act to drive up costs, with 63% of manufacturing businesses reporting this as cost pressure, similar levels as observed in Q2 2018.

RETAIL

- Strong optimism result, suggesting strong expectations for Q4.
- Sales less strong than in Q2, particularly in the Domestic market and Rest of the UK.
- Only sector with broad increases in investment this quarter, but driven from a low base in comparison with the second quarter when compared to other analysed sectors.
- Cashflow flat, but profitability substantially improved relative to Q2 and the Q3 2017.

TOURISM

- Optimism and revenue broadly sustained from Q2 2018, although a dip in revenue from the Rest of the UK.
- Very high levels of recruitment difficulties (79% of firms), perhaps reflecting the unique labour market needs and greater proportion of EEA labour traditionally in this sector.
- Intention to invest higher in Q4 2018, linked to seasonal investment focus in the tourism sector.
- Business Rates, Competition and Taxation growing as concerns for the industry. Softening concerns around inflation perhaps reflect increasing focus on EU and Non-EU guests.

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