Quarterly Economic Indicator

Scottish Chambers of Commerce

Network

in partnership with Fraser of Allander Institute

RESULTS: Q1 2023

CONTENTS

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Foreword

Uncertainty has increased in the outlook for the economy, as more positive economic news is mixed in with more worrying signs from the global banking system.

High inflation will be with us throughout 2023, and although we still expect it to come down as we compare to the much higher price levels of 2022, significant price rises are continuing to put pressure on consumer spending and therefore businesses.

And, while the approach of the Bank of England to interest rate rises may be softening, they are still showing that they will be prepared to raise rates further to deal with persistently high inflation. This measure will weigh on demand as we move through 2023.

All of this means that the outlook is exceedingly uncertain, and there are a number of risks to the forecasts – many of which are to the downside.

The outlook for the UK economy published by the Office for Budget Responsibility (OBR) which accompanied the Spring Budget was significantly more positive than in November. Given the uncertainty, and in particular, given the rise in energy bills households and businesses will experience from April, it feels a little premature to be celebrating that the UK has dodged a recession.

Whilst it may indeed be true that a technical recession will be avoided, it is still going to feel like a difficult time for the economy – with even the optimistic OBR thinking there will be a contraction in growth over 2023.

So, the overall feeling in the economy seems to be that things are not as bad as we feared a few months ago, but that the bar was pretty low. All of this is shown in the survey results today, with firms a bit more positive about the outlook for business, but much more negative about investment intentions.

This is concerning for the medium to long-term capacity of our economy to grow. The increasing uncertainty in the economy at the moment is unlikely to provide the environment to incentivise the investment that the economy needs.

Professor Mairi Spowage
Director
Fraser of Allander Institute

Introduction

Stephen Leckie
President
Scottish Chambers of Commerce

The beginning of 2023 has seen improvement in the prospects of some sectors of the Scottish economy, in line with recent economic data that has been more positive than previously expected.

While we see the construction, services and manufacturing sectors reporting better results, we must note that this comes from a very low bar set by the past few years of constant and seemingly never-ending challenges for business. We also see the retail and tourism industries continuing to struggle in the face of these headwinds.

The survey also indicates that many of the big challenges that faced firms in 2022 are continuing to persist in 2023. Cost pressures continue to rise alongside concern from energy bills, inflation, labour shortages, alongside growing uncertainty in the global economy.

There is a large in-tray of issues for the new First Minister and his cabinet to work with businesses to address, to help put the Scottish economy back onto a path towards unlocking growth and investment.

We are ready to work with government to bring care and focus onto these pressing challenges for the economy, that must come with agile and decisive action that supports firms through the uncertainty ahead.

One of the most consistent themes in the survey results is the high number of firms antidotally highlighting increased concern from current and or future regulatory burdens.

These include the deposit return scheme; short-term lets; alcohol advertising; tourism visitor levy; rent controls; to name but a few. Businesses will be looking for action on regulation very soon and we will hold the FM's pledge of an 'open door' for business to account.

While support for energy bills has helped business concerns and costs to an extent, there is still three-quarters of Scottish firms telling that this is still a problem and not going away any time soon.

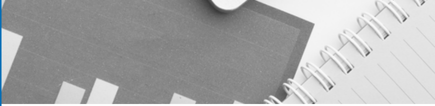
The painful reality for many is that energy support from the UK Government has now been scaled down and businesses will now soon see their standing charges shoot through the roof, which could be the final straw for many.

The UK Government should reconsider how it intends to support both firms and households in need throughout the year until wholesale energy prices have sufficiently cooled.

QUARTERLY ECONOMIC INDICATOR

Key Findings

Q1 2023



The Q1 2023 survey was conducted between February & March 2023. 320 firms responded to the survey.

Inflation Concerns Persist:

- Concern over inflation remains high among all firms and has seen little movement over the quarter, with around eight in 10 firms reported increased concern from it. On a sectoral level, financial and business services was the only sector surveyed where a lower number of firms reported less than at least eight in 10 at 77%.

Cost Pressures Remain High:

- 75% reported increased cost pressures from energy costs
- 70% reported increased cost pressures from labour costs, including salaries
- 55% reported increased cost pressures from fuels such as diesel and petrol
- 50% reported increased cost pressures from raw material prices

Cashflow & Profit Challenges:

- On balance, more firms reported a fall (43%) in cashflow than an increase (31%), reflecting the difficulties being faced by many businesses, notably in retail and tourism.
- Across the entire survey, the manufacturing sector was the only sector to report growth for cashflow and not a contraction. Similarly, the services sector was the only sector to report growth in profits.

Cautious labour market:

- Recruitment difficulties have seen a slight drop of five percentage points, from being reported by 52% of firms in Q4 to 47% for this quarter.
- Over half of all firms (57%) reported no staff changes over the quarter, with 57% again saying that they do not expect staff changes to change in Q2 2023.

Less firms planning to raise prices:

- The number of firms indicating that they intend to raises prices in the next quarter has fallen slightly compared to the previous quarter. This remains high with still over seven in 10 firms (73%) stating that they will raise prices in Q2 2023.

CONSTRUCTION

Business Concerns:
Cited by eight in 10 firms, concern over inflation remains high, albeit slightly down when compared to the average of 90% for 2022.

Cost Pressures:
Labour costs narrowly remain the leading cost pressure for construction firms, just ahead of energy costs and raw material prices

Work in Progress:
Seven in 10 firms are reporting an increase in work. The net balance of +30% is the highest recorded since Q3 2021.

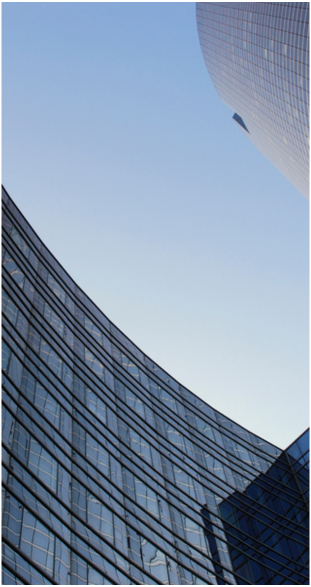
Contracts & Sales:
After a weak end to 2022 for sales and contracts, the new year has seen these trends rebound strongly and report positive net balances across the board.

Price Rises:
After a survey record 71% of firms anticipated raising their prices last quarter, that has eased to 50% of firms.

BUSINESS VOICE:

"Utility costs are a big worry. We are waiting on new electricity costs from our Landlord and expecting a high increase in our rates." - Construction firm in Dundee

FINANCIAL & BUSINESS SERVICES



Inflation:
Inflation concern has risen slightly to 77% of firms, just below the high average of 78% reported across 2022.

Confidence:
Q1 2023 has seen a return to the norm for the sector, reporting a healthy net balance of +25%, 10 percentage points higher than the Q1 average for the sector.

Sales Revenue:
Most sales trends have returned to positive net balances for the first time in two quarters. The main driver of the strong sales overall was an increase in domestic sales.

Cashflow & Profits:
Services firms have reported a fall in cashflow on balance for a third successive quarter. On the other hand, firms reported a positive net balance for profits.

Expectations:
Firms in the sector are generally positive for the next quarter with sales, investment and staff levels all forecast to grow on balance.

BUSINESS VOICE:

"Very unclear where the government is going with support for oil & gas and the whole energy transition strategy seems a mess. Increasing costs in hampering cashflow to enable growth - still very uncertain times." - Services firm in Aberdeen

MANUFACTURING

Inflation:
Concern from inflation has risen slightly over the quarter to nearly nine in 10 firms at 87%, close to the record highs reported in early 2022.

Cost Pressures:
As was the case through most of 2022, the leading cost pressures are from energy, labour costs and raw material prices. Around seven in 10 firms are being affected by these.

Labour Market:
Firms reported high difficulties towards the end of last year and that continues with still six in 10 reporting such challenges in Q1 2023.

Cashflow & Profits:
Firms in the sector have reported a positive net balance for cashflow for the first time in three quarters.In contrast, firms have reported a fall on balance for profits for a third successive quarter.

Confidence:
Manufacturing have generally reported positive levels of confidence for the past two years of the survey. That continues with a positive net balance of +12% to begin 2023.

BUSINESS VOICE:

"As a business we are trying to grow but this growth is throttled by the lack of a skilled workforce on a local and national level and the constant worry that the economy is stuttering and any short term gains will be wiped out by interest rate rises, rocketing energy costs. Some measures to create economic stability from Government would be welcomed to our business." - Manufacturing firm in the Highlands

RETAIL & WHOLESALE

Inflation:
Concern from inflation continues to far outpace other concerns and has increased slightly over the quarter, now being reported by 82% of firms.

Cost Pressures:
Utility All cost pressures have remained static or eased over the quarter, with energy costs and labour costs still the dominant trends.

Sales Revenue:
Spring sales have had a positive impact on the sector as it reported its first positive net balance (+8%) since Q3 2020.

Confidence:
Retail firms have started the year on a positive note after reporting their first positive net balance for confidence (+8%) for a year. This is 20 percentage points higher than the Q1 average.

Investment:
In a theme that has continued from 2022, retail firms are generally holding back or pulling investment out altogether from their businesses.

BUSINESS VOICE:

"The proposed bottle deposit scheme is unworkable, some of the guidelines for online retailers are impossible for me to adhere too. Additional it will create a barrier to trade outside of Scotland and therefore put my business at risk of closing as 90% of my revenue comes from outside of Scotland." - Retail firm in Renfrewshire

TOURISM

Business Concerns:
Concern over inflation remains close to record highs at 90%, while concern from taxation has seen a substantial increase up to 70%: a five-year record high for the survey.

Cost Pressures:
Most cost pressures have generally eased over the quarter but remain significant for tourism firms, particularly on energy and labour costs.

Investment & Sales:
The sector typically does not report growth in sales or investment in its 'off-season' and that is reflected in these results. Across all sales and investment trends, firms have reported falls across the board.

Cashflow & Profits:
In a similar vein to the end of last year, over half of firms have reported a fall in cashflow. Nearly seven in 10 (67%) reported falls in profits, resulting in negative net balances for both trends.

Expectations:
In keeping with the seasonal aspects of the sector, firms are forecasting sales and stuff to increase in Q2 but investment to stay flat.

BUSINESS VOICE:

"There is too much uncertainty, people are frightened to come out and spend. Utility prices are way too high, mortgage rates up, business rates now an issue due to drop in threshold. Way too much new regulations, STL, DRS, alcohol advertising, possible visitor levy. We need help not more pressures." - Tourism firm in the Highlands

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