

Quarterly Economic Indicator



Scottish
Chambers of
Commerce

Network

in partnership with
Fraser of Allander Institute

**RESULTS:
QUARTER 2
2022**

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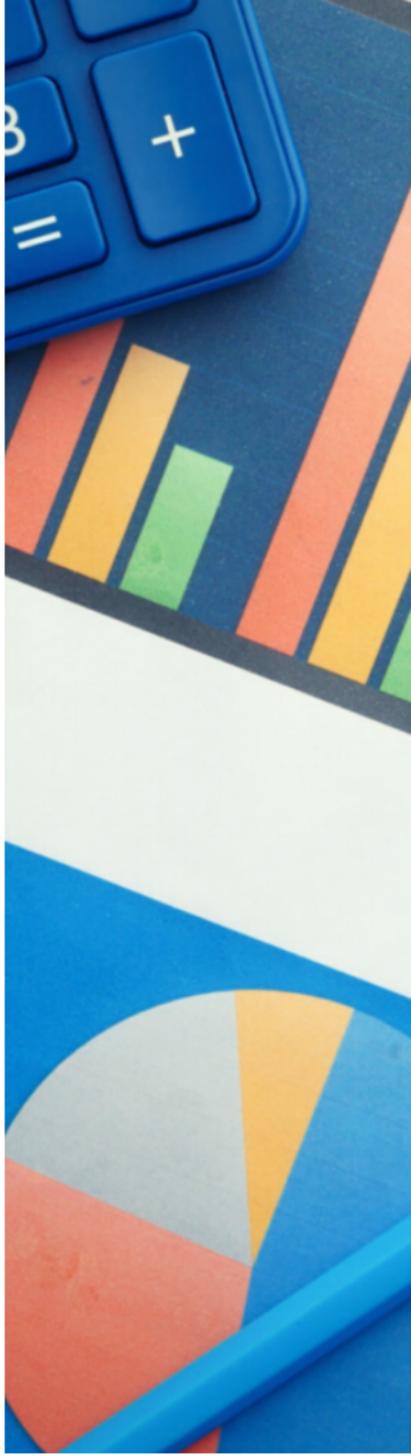
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Foreword

Mairi Spowage
Director
Fraser of Allander Institute



The consequences of rising inflation are being felt across the economy, with clear signs that consumer confidence is being dented and that people are cutting back on both essential and non-essential spending.

Alongside this, there is an increasing fear that high inflation will be more persistent than was first thought, with expectations now that it may be 2024 before we get back to more normal levels of inflation.

This has led the Bank of England to act to successively raise interest rates to manage inflation back down over the medium term. In the short term, however, this is likely to add to the pain for many households as it increases to cost pressures on mortgage and rent payments.

The Scottish economy recovered strongly in the first quarter of the year, with output now well above pre-pandemic levels. However, the data published last week for April shows the impact of current conditions across all sectors of the economy.

The latest GDP data for Scotland shows a contraction in the economy of 0.5%. There was minimal change in output across the production, construction, and agriculture sectors. Services, which makes up three-quarters of the Scottish economy, fell by 0.7% in the latest month.

However, this was not driven by consumer-facing services which actually grew by 1.1% in April. Instead, this contraction was primarily driven by health, education, and public services, as NHS scales back vaccination and test and trace activity.

This survey published today highlights concerns that businesses have about rising costs. Current data suggests that the experience of input price rises for businesses is running at 22%: still more than double the consumer inflation rate.

This may mean that these cost pressures may continue to feed through to prices experienced by consumers as more businesses face difficult choices.

Given this environment, It is not surprising in this latest set of results that we have seen a dip in confidence across sectors. Still though, it is heartening to see that most are optimistic about sales going forward.

It will be interesting to see how this positivity evolves as we progress through 2022.

Introduction

Stephen Leckie
President
Scottish Chambers of Commerce



The latest Scottish Chambers of Commerce business survey reveals that cost and inflationary pressures are deterring investment and forcing businesses with little choice but to make difficult decisions for business survivability.

These include holding back or in some cases pulling back investment, putting projects on hold due to supply chain disruption, and in extreme situations considering whether or not to have the heating and lights on or off.

Urgent action is needed now from the Scottish and UK Government if we are to reverse the tide of economic decline, restore confidence and put the economy back on the road to growth.

Cashflow and profit margins are taking heavy hits as cost burdens rise and businesses adjust to manage spiralling costs. As government loan repayments kick in and business insurances increase, firms are dealing with a whammy of surging cost burdens.

A record number of firms indicate that they expect to raise their prices to remain viable. With consumer discretionary spending suppressed due to the cost of living crisis and continuing supply chain disruption, this trend will continue unless support is forthcoming.

Firms are also telling us that this crisis is leading them to pull back or withhold investment decisions. The construction, retail and tourism sectors have reported significant cuts to investment over the last quarter, contributing to a slowdown in economic activity and any meaningful prospects for recovery.

The UK Government must act now and work with Scottish business ahead of the Autumn Budget to help firms weather this perfect storm. The immediate costs crisis is on energy prices and the UK Government must act on the calls from businesses to introduce an SME energy price cap and cut VAT on energy bills from 20% to 5%. This immediate support would shield businesses in a similar way to households.

Finally, the Autumn Budget must present solutions to the current economic challenges. But it must not stop there. The Chancellor must present a long-term economic plan developed in partnership between business and government focused on restoring business and consumer confidence, investment, and growth to the Scottish and UK economy.

Key Findings

Quarter 2 2022

The Q2 2022 survey was conducted between May and June 2022. 360 firms responded to the survey.

Record Concern Over Inflation:

- UK inflation has reached 9.1%, the highest in 40 years. Since April 2022, inflation has doubled and 9 in 10 Scottish firms across all sectors surveyed are continuing to report major inflationary pressures.

Cashflow Crunch & Profits Plummet:

- Cashflow and profits have generally fallen across the majority of the sectors. The sectors that saw the largest falls on balance of all the sectors, were the retail and tourism sectors.

Growing Cost Pressures:

- Businesses continue to be impacted by rising energy bills, 7 in 10 firms report that it is the largest contributor to their cost pressures. Fuel and labour costs, alongside raw material prices, are also significant concerns.

Consumer Price Rise:

- Over three quarters of all firms (77%) have indicated that they intend to raise prices next quarter. The sectors that reported the largest increases from the previous quarter were the financial & business services and tourism sectors.

Labour Market Pressures:

- Recruitment difficulties have seen a 10% increase from the previous quarter, with half of all firms reporting increased challenges hiring staff. The sectors that saw the largest increases from Q1 2022 were the financial and business services, manufacturing and retail sectors.

Investment Frozen:

- Decisions on investment have been held back with 50% of all firms reporting no changes to levels of investment in the next quarter. The construction, retail and tourism sectors have reported significant cuts to investment over the last quarter.

CONSTRUCTION



Inflation:

Concern over inflation (97%) has reached a successive record high for the survey.

Cost Pressures:

The most notable cost pressures highlighted by construction firms were utility costs (77%), raw material prices (74%) and labour costs (71%).

Cashflow & Profits:

For the second successive quarter, firms have reported falls on balance in levels of cashflow and profits.

Contracts & Sales:

All contract and sales remain consistently positive and robust, with the exception of domestic / housebuilding contracts which saw a fall on balance.

Investment:

All contract trends have reported positive net balances with most seeing significant improvement since the previous quarter.

BUSINESS VOICE:

"If business rates go up again, as alluded to in the Scottish Government's latest economic statements, this will have yet another negative impact on our local economy. Aberdeen suffers much worse than central belt equivalents." - Small Construction firm in Aberdeen

FINANCIAL & BUSINESS SERVICES



Inflation:

8 in 10 firms have reported increased concern from inflation. This is a record survey high and almost double the concern from last year's second quarter.

Cost Pressures:

The leading cost pressures for firms come from utility costs (65%) and labour costs (60%). All cost pressures have generally seen a significant increase since Q2 2021.

Sales & Orders:

All sales trends have remained at positive net balances for the third successive quarter since Q3 2021. Domestic sales continue to be the main driver, while export sales have seen little movement in the past year.

Labour Market:

Compared to Q2 2021, recruitment difficulties have increased by 12 percentage points to 54%. This is a record high in the survey's history.

Price Rises:

A record 55% of firms report that they intend to increase their prices in the next quarter. This has increased by 25 percentage points over the quarter.

BUSINESS VOICE:

"Current contracts are locked into 2021 rates and balancing the need to retain staff with pay rises and cost of business rates is reducing existing margins. The prospect of a national and global recession is a high risk to the services we provide and may result in redundancy in the latter part of the year if new business cannot be secured." - Services firm in Inverness

MANUFACTURING



Inflation:

Nearly 9 in 10 firms (89%) have reported increased concern from inflation since the previous quarter. This is only 2% lower than the record 91% recorded in Q1 2022.

Cost Pressures:

Over 8 in 10 firms have reported raw material prices and utility costs as their leading cost pressures.

Labour Market:

Recruitment difficulties have increased by 14 percentage points to 55% of firms. This is around 15 percentage points higher than the Q2 average.

Cashflow & Profits:

Firms have reported positive levels of cashflow for the second successive quarter and well above the Q2 average. After two successive quarters of reporting falls on balance in profit levels, firms also have reported an increase in profits.

Confidence:

Firms in the sector have reported a positive net balance for the seventh successive quarter.

BUSINESS VOICE:

"Challenging conditions due to input price inflation of around 20% and prices having to be increased to customers." - Manufacturing firm in Dundee & Angus

RETAIL & WHOLESALE



Inflation:

Over 8 in 10 firms (83%) have reported increased concern from inflation, a successive five-year survey high.

Cost Pressures:

Most cost pressures rose over the quarter, with utility costs (75%), labour costs (62%) and fuel costs (55%) the leading pressures.

Labour Market:

Recruitment difficulties have seen a sizable jump from Q1 2021, up to 57% of firms. This is the highest recorded in the past five years.

Confidence:

Retail firms have reported their lowest levels of confidence in two years. The negative net balance of -40% is the lowest reported since Q2 2020.

Cashflow & Profits:

Most retail firms have reported falls in cashflow and profit levels, resulting in significant negative balances of -44% for both trends.

BUSINESS VOICE:

"Generally domestic customers are feeling the pinch and not wanting to spend on non-essential items." - Retail firm in Edinburgh

TOURISM



Inflation:

Concern from inflation saw a large rise from the last quarter: 16 percentage points to 85% of firms, a successive survey record high.

Cost Pressures:

The leading cost pressures are utility costs (72%), labour costs (54%) and fuel costs (51%).

Price Rises:

A record 77% of tourism firms report that they intend to raise their prices in Q3 2022.

Cashflow & Profits:

For the third quarter in a row, tourism firms have reported falls in cashflow and profit levels on balance. Both trends sit well below their results from the same quarter in 2021 as well as the running five-year survey average.

Confidence:

8 in 10 firms reported either static or lower levels of confidence. The negative net balance of -22% is in stark contrast with the +14% reported in the same quarter last year and sits well below the running five-year survey average.

BUSINESS VOICE:

"There has to be some serious reform in the UK if businesses are to survive the next 18 months. The cost of living, fuel costs and inflation are going to have a devastating impact on millions of people in the UK. If there is no radical change these industries (leisure & tourism) will not survive." - Tourism firm in Stirling

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