

Royal Bank of Scotland PMI[®]

Scottish private sector nears stagnation in July

Key Findings

Manufacturing downturn deepens, almost offsetting service sector growth

Demand for services drives growth in total order books

Employment falls for first time in over two years

Scotland Business Activity Index



Last six months SC / UK



By sector	Jul-19
Manufacturing	46.5
Services	51.0

According to the latest Royal Bank of Scotland PMI[®], the private sector economy in Scotland approached stagnation in July, growing only fractionally. Order books increased for a second month running, however growth here was driven entirely by demand for services as manufacturing sales dropped sharply. Challenging conditions were also highlighted by employment declining for the first time since May 2017, while business confidence dipped to a 35-month low.

The seasonally adjusted headline Royal Bank of Scotland Business Activity Index - a measure of combined manufacturing and service sector output - posted 50.2 in July, down from 51.3 in June, signalling a fractional rate of growth in private sector output in Scotland at the start of the third quarter.

While a mild and slower expansion in business activity was registered at service providers, manufacturers reported a solid and quicker fall in production.

Demand

Latest survey data signalled back-to-back gains in new business at Scottish private sector firms in July. The pick-up in sales was driven by services, as manufacturing order books contracted sharply and at a quicker rate. New client wins reportedly lifted sales at service providers, but manufacturers mentioned uncertainty and softer underlying demand conditions as factors restricting new work inflows. Overall, aggregate order book volumes increased modestly, but at a slower

rate than seen on average.

Capacity

Relatively subdued demand conditions filtered through to hiring in July, with employment levels falling for the first time in over two years. The trend in Scotland diverged from the UK overall, where job creation was sustained. The drop in staffing levels was driven by goods producers, as workforce numbers were held broadly stable in the service sector. Meanwhile, a tenth successive monthly reduction in backlogs of work was recorded in Scotland, indicating spare capacity.

Prices

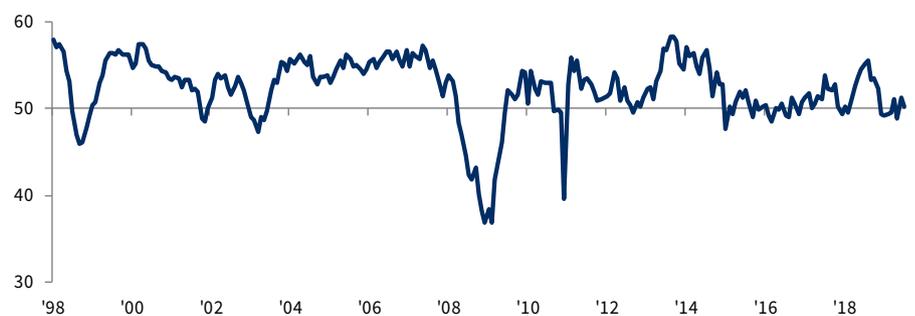
A broad-based softening of inflationary pressures was signalled by the survey data in July, with manufacturers and service providers both reporting slower rises to input costs and prices charged. According to anecdotal evidence, competitive pressures had reduced businesses' flexibility to pass on higher cost burdens to their clients.

Outlook

Looking ahead, private sector companies in Scotland expect output volumes to be higher than present levels in 12 months' time. That said, the degree of confidence was the lowest in nearly three years. Brexit uncertainty, slower global growth and concerns regarding the UK economy reportedly weighed on sentiment in July.

Scotland Business Activity Index

sa, >50 = growth since previous month



New Business Index



Back-to-back gain in new business in July

According to latest survey data, new business placed with private sector firms in Scotland increased in July, marking back-to-back gains in new workloads. Sector data indicated that the rise was driven by demand for services, as new orders at manufacturers declined strongly. Overall, the expansion lost momentum, easing since June and was weaker than that seen for the UK as a whole.

New Business Index

sa, >50 = growth since previous month



By sector

	Manufacturing	Services
Jul-19	43.6	53.2

Outstanding Business Index



Backlogs of work decline for tenth successive month

Private sector companies in Scotland continued to make inroads into backlogs of work in July, as signalled by the seasonally adjusted Outstanding Business Index recording below the 50.0 no-change mark. According to firms, recent softness in demand had enabled companies to allocate additional resources to freeing up capacity. Overall, the rate of depletion was moderate, gathering pace since June.

Outstanding Business Index

sa, >50 = growth since previous month



By sector

	Manufacturing	Services
Jul-19	44.8	47.9

Employment Index



Employment levels fall fractionally in July

Staffing levels in Scotland's private sector dipped at a fractional pace in July, thereby ending a 16-month sequence of rising workforce numbers. Employment was pulled down by the manufacturing sector, as services posted a broad stabilisation. Where job cutting was reported, panellists linked this to weak demand. However, trends between Scotland the UK as a whole diverged in July, as job creation was sustained for the latter.

Employment Index

sa, >50 = growth since previous month



By sector

	Manufacturing	Services
Jul-19	49.2	50.1

Input Prices Index



Input cost inflation eases to three-year low

Private sector companies in Scotland continued to face strong cost pressures in July. Higher prices for imported goods and greater charges from suppliers were mentioned by panellists. That said, a broad-based softening of input price inflation was recorded, leading the overall rise in operating expenses to slow to its weakest in three years.

Input Prices Index

sa, >50 = inflation since previous month



By sector

	Manufacturing	Services
Jul-19	54.7	59.2

Prices Charged Index

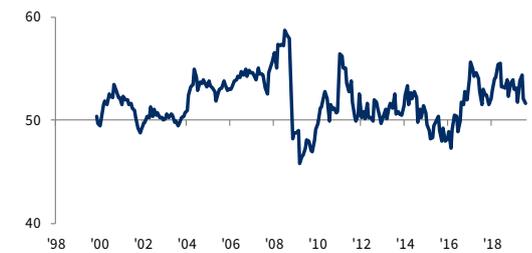


Selling prices increase at weakest rate since November 2017

Latest survey data pointed to another month-on-month increase in average prices charged by private sector businesses in Scotland. According to anecdotal evidence, selling prices were lifted in line with greater cost burdens. That said, the rate of output price inflation was only modest and eased to a 20-month low.

Prices Charged Index

sa, >50 = inflation since previous month



By sector

	Manufacturing	Services
Jul-19	50.4	51.9

Future Output Index

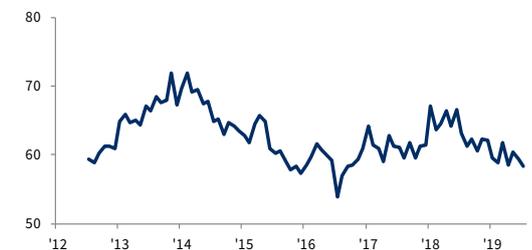


Business confidence dips to 35-month low

While firms still anticipate output volumes to rise over the coming 12 months, the degree of optimism weakened in July to the lowest in nearly three years. Concerns regarding Brexit, expectations of slower global growth and uncertainty towards the UK economic performance were mentioned as factors restricting sentiment. The only part of the UK to record weaker optimism than Scotland was Northern Ireland.

Future Output Index

>50 = growth expected over next 12 months



By sector

	Manufacturing	Services
Jul-19	59.7	58.0

Scotland Export Climate Index

Note: Export markets are defined as non-UK.



Last six months



Growth of key export markets eases to 74-month low in July

The Scotland Export Climate Index is calculated by weighting together national PMI output data according to their importance to the manufacturing exports of Scotland. This produces an indicator for the economic health of Scotland's export markets.

The Scotland Export Climate Index fell for a fourth successive month in July, indicating a softer rate of improvement in conditions at Scotland's key trading markets. Posting 51.2, down from 51.6 in June, the rate of growth signalled was only mild and the weakest in just over six years.

The softening of growth partly reflected a slowdown in Scotland's main destination for goods exports, the Netherlands, where growth eased to a 74-month low. Germany, France and Ireland also recorded weaker upturns. The US, which accounts for nearly 16% of total goods exported from Scotland, observed a stronger expansion than in June.

Export Climate Index

sa, >50 = improving export climate since previous month



Top export markets, Scotland

Rank	Market	Weight	Output Index, Jul-19
1	Netherlands	24.4%	50.6
2	USA	15.5%	52.6
3	Germany	10.7%	50.9
4	France	6.6%	51.9
5	Ireland	6.3%	51.8

Scotland Industry Specialisation

Location quotients (LQs) are useful measures of regional economic specialisation and offer a means to identify industry clusters at a local level. They are ratios derived by comparing the share of sector output (or gross value added) in regions with the national share of output in the same sector.

Focusing on the manufacturing and service sectors in isolation, a location quotient is calculated by taking a sector's proportion of regional output and comparing it with the UK-wide share of output in the sector. An LQ of 1.0 in a sector means that the region and the UK as a whole are equally specialised in that

sector. An LQ greater than 1.0 indicates that the sector has a greater economic footprint in the region than it does for the UK as a whole.

The tables below rank the location quotients for Scotland, broken down by manufacturing and services sub-sectors. The UK Output Index for each sub-sector is also displayed.

Manufacturing specialisation: Scotland

Rank	Sector	LQ	UK Output Index, Jul-19 (3mma)
1	Food & Drink	1.80	
2	Wood & Paper	1.18	
3	Textiles & Clothing	1.16	
4	Electrical & Electronic	1.04	
5	Chemicals, Rubber & Plastics	0.94	
6	Machinery & Equipment	0.93	
7	Metals & Metal Products	0.89	
8	Other Manufacturing	0.78	
9	Transport Equipment	0.35	

40 45 50 55

Services specialisation: Scotland

Rank	Sector	LQ	UK Business Activity Index, Jul-19 (3mma)
1	Hotels, Restaurants & Catering	1.27	
2	Financial Intermediation	1.06	
3	Other personal/consumer Services	1.05	
4	Transport & Communication Services	1.02	
5	Business-to-business Services	0.95	
6	Computing & IT Services	0.68	

45 50 55 60

UK Sector Focus: Financial Intermediation

Output Index



Last six months*



*3mma

Financial intermediation weighs on UK economic growth in the three months to July

In a complete reversal of the situation one year ago, financial intermediation was the UK's worst-performing services sub-category in the three months to July. That said, with the rate of decline in business activity in the sector slowing to a modest pace, its drag on economic growth continued to ease from a nadir in the three months to May.

Business confidence towards the year-ahead outlook for activity meanwhile remained close to the six-year low recorded in the three months to April, weighed on by ongoing uncertainty around Brexit. Nevertheless, hopes of future growth were reflected in a solid rate of job creation.

Margins across the sector meanwhile remained under pressure, as firms kept output charges broadly unchanged despite facing a sustained steep rise in costs.

Output Index

sa, >50 = growth since previous month (3mma)



Future Expectations Index

sa, >50 = growth over next 12 months (3mma)



UK Regional Rankings

Business Activity

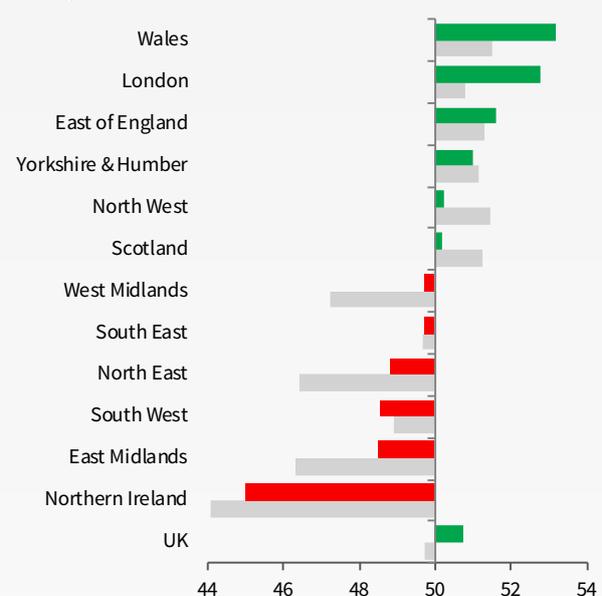
Wales stayed top of the rankings for business activity growth in July, having seen its pace of expansion accelerate for the second straight month to the quickest since February. London was ranked second overall and also saw a marked improvement in growth. The East of England and Yorkshire & Humber each posted a modest rise in output, while in the North West and Scotland marginal increases were recorded. Business activity fell in all remaining areas, with Northern Ireland again seeing the steepest rate of decline.

Employment

Yorkshire & Humber led job creation for the second month running in July, ahead of London. These were the only two regions where employment increased at a faster rate, with slower growth seen in the East of England, North West, West Midlands and South East. The steepest falls in workforce numbers were recorded in the East Midlands and Northern Ireland respectively. Modest job cuts were also seen in Wales and the South West, while negligible losses were recorded in both the North East and Scotland.

Output Index by region

sa, >50 = growth since previous month, Jul-19



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Methodology

The Royal Bank of Scotland PMI® is compiled by IHS Markit from responses to questionnaires sent to a panel of around 500 manufacturers and service providers. The panel is stratified by detailed sector and company workforce size, based on contributions to GDP.

Survey responses are collected in the second half of each month and indicate the direction of change compared to the previous month. A diffusion index is calculated for each survey variable, for the manufacturing and services sectors. The index is the sum of the percentage of 'higher' responses and half the percentage of 'unchanged' responses. The indices vary between 0 and 100, with a reading above 50 indicating an overall increase compared to the previous month, and below 50 an overall decrease. The indices are then seasonally adjusted. Comparable manufacturing and services indices are then weighted together to form a composite index, with the weights based on official value added data.

The headline figure is the Business Activity Index. This is a composite index calculated by weighting together the Manufacturing Output Index and the Services Business Activity Index. The Scotland Business Activity Index is comparable to the UK Composite Output Index. It is sometimes referred to as the 'Scotland PMI', but is not comparable with the headline UK Manufacturing PMI figure.

Underlying survey data are not revised after publication, but seasonal adjustment factors may be revised from time to time as appropriate which will affect the seasonally adjusted data series.

For further information on the PMI survey methodology, please contact economics@ihsmarkit.com.

About PMI

Purchasing Managers' Index® (PMI®) surveys are now available for over 40 countries and also for key regions including the eurozone. They are the most closely watched business surveys in the world, favoured by central banks, financial markets and business decision makers for their ability to provide up-to-date, accurate and often unique monthly indicators of economic trends. To learn more go to ihsmarkit.com/products/pmi.html.

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The bank has commitment to retain its close connections with the Scottish communities it serves.

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