

Royal Bank of Scotland PMI®

Scottish private sector remains in downturn in January

Scotland Business Activity Index



Aug '22 - Jan '23



Key findings

Private sector activity falls at a quickened pace in January

Downturn in new orders extends to seventh month

Marked drop in service sector new business

The Scottish private sector reported a further fall in total activity during January according to the latest Royal Bank of Scotland PMI® data. The Business Activity Index - a measure of combined manufacturing and service sector output - fell from December's five-month high of 48.3 to 47.1, signalling a quickened contraction in private sector output, and extended the current run of contraction to six consecutive months. The rising cost of living, supply chain disruptions and a slowdown in the housing market all contributed towards the latest downturn in activity.

At the sector level, January data revealed that service firms led the decline, registering faster rates of reduction in both business activity and new orders compared to their manufacturing counterparts.

Judith Cruickshank, Chair, Scotland Board, Royal Bank of Scotland, commented:

"The start of the year revealed that the downturn in Scottish private sector activity that began last August was extended into 2023. Moreover, the latest decline in private sector activity accelerated. It seems unlikely that the sector will bounce back anytime soon as services firms were severely impacted by the depressed demand conditions and the current economic climate."

"The step back in client activity has also resulted in firms trimming their workforce numbers for the second month running. Alongside an ongoing drop in the level of unfinished work, a further reduction in payroll numbers can be expected."

"However, the latest figures indicate that perhaps the worst of inflation has passed. Nonetheless, the current rates of input price and output charge inflation are still elevated and can be detrimental to the health of the Scottish private sector."

Scotland Business Activity Index

sa, >50 = growth since previous month



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About the Scotland PMI® report

The Royal Bank of Scotland PMI® is compiled by S&P Global 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.

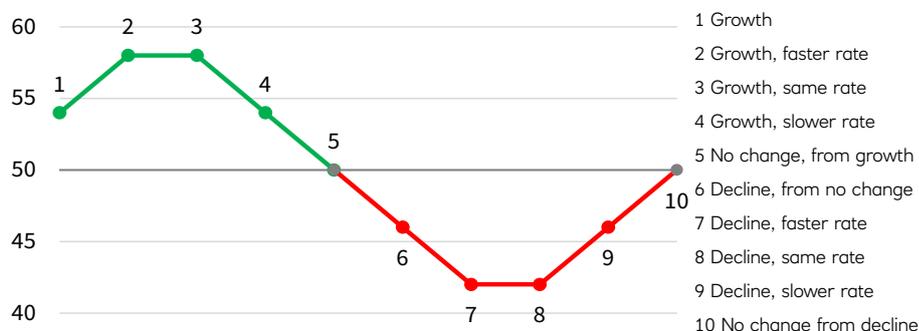
The headline figure is the Business Activity Index. This is a composite index calculated by weighting together the Manufacturing Output Index and the Services Business Activity Index. The Scotland Business Activity Index is comparable to the UK Composite Output Index. It is sometimes referred to as the '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.

Index interpretation

50.0 = no change since previous month



Demand and outlook

New business

New business received across the Scottish private sector posted a further contraction in January. Moreover, the pace of decrease quickened from December's three month low, signalling a sharp reduction in new work. The downturn was led by a faster fall in new business received at service providers, while goods producers reported the softest decline in eight months. A slow housing market, transport strikes and squeezed disposable incomes were all in part blamed for the drop in new orders.

Of the 12 monitored UK regions, Scotland registered the sharpest pace of contraction in incoming new business.

Business expectations

After weakening for the second month running, business expectations across Scotland improved during January and printed a six-month high. Optimism largely stemmed from anticipation of new projects and increased activity. That said, the latest reading continued to post below the survey average as worries over the war in Ukraine, energy crisis, slowdown in the real estate sector and the cost-of-living crisis weighed on growth expectations.

Additionally, business sentiment across Scotland registered the third-weakest in the UK, ahead of Northern Ireland and the North East of England.

Exports

Improvement in export market conditions for the first time in six months

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

The Scotland Export Climate Index printed above the 50.0 threshold in January to signal an improvement for the first time in six months. That said, the upturn was only fractional.

Only two of the top five export markets reported growth in output, with Ireland recording the stronger expansion, while softer growth was seen in the Netherlands. Germany, France and the US continued to record a downturn.

New Business Index 43.6
sa, >50 = growth since previous month Jan '23



Future Activity Index 58.4
>50 = growth expected over next 12 months Jan '23

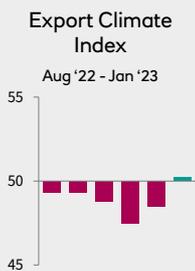
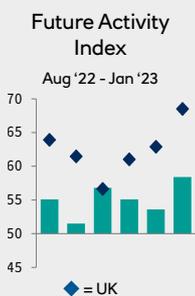
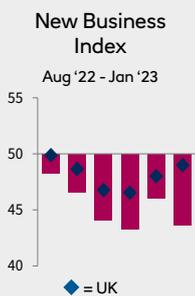


Export Climate Index 50.2
sa, >50 = growth since previous month Jan '23



Top export markets, Scotland

| Rank | Market | Weight | Output Index, Jan '23 |
|------|-------------|--------|-----------------------|
| 1 | Netherlands | 19.4% | 50.7 |
| 2 | Ireland | 13.5% | 52.0 |
| 3 | USA | 13.2% | 46.8 |
| 4 | France | 9.0% | 49.1 |
| 5 | Germany | 8.9% | 49.9 |



Business capacity

Employment

For the second month running, workforce numbers contracted across the Scottish private sector in January. The rate of job shedding was modest overall and only fractionally quicker than that seen in December. Where a drop in employment was noted, firms cited resignations, redundancies and retirements.

The drop in workforce numbers across Scotland contrasted with the no change seen at the UK-level.

Employment Index 48.8
 sa, >50 = growth since previous month Jan '23



Outstanding business

The levels of unfinished work fell during January across Scotland's private sector, thereby extending the current trend seen since last June. Moreover, the respective seasonally adjusted index ticked down from December's four-month high, signalling the fastest rate of depletion in the aforementioned sequence. According to anecdotal evidence, lower orders allowed firms to work through previous contracts.

The rate of backlog depletion across Scotland was the fastest of all the 12 monitored UK regions.

Outstanding Business Index 44.1
 sa, >50 = growth since previous month Jan '23



Prices

Input prices

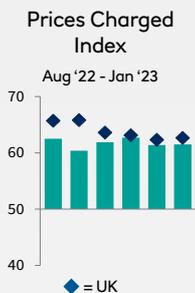
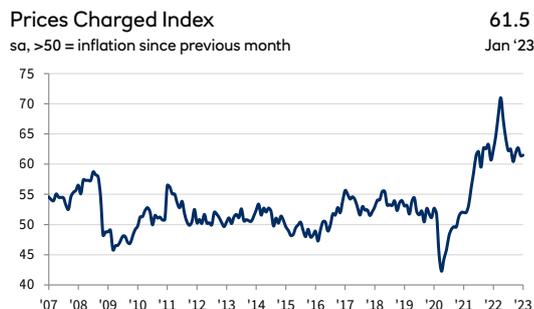
Firms across Scotland's private sector recorded a sharp rise in prices during January, thereby stretching the current run of inflation to 32 months. While the rate of incline measured the softest since May 2021, the latest upturn was still marked and historically elevated. According to anecdotal evidence, the incline in input costs was linked to higher prices for raw material, energy and transport, inflation and higher wages.

The pace of input price inflation across Scotland was the second-softest among the UK regions, behind the North West of England.

Prices Charged

Private sector firms across Scotland raised their charges for goods and services for the twenty-seventh month running in January. Though the pace of charge inflation slowed to a three-month low, it remained stronger in context of survey data. The rise in charges reflected increasing cost pressures.

Adjusted for seasonality, the Prices Charged Index for Scotland posted below the UK-wide figure.



UK Sector PMI

Sector specialisation: Scotland

Location quotients (LQs) are useful measures of regional economic specialisation and can 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. The UK Output Index for each sub-sector is also displayed.

Scotland specialisation: Manufacturing

| Rank | Sector | LQ | UK Output Index, Jan'23 ⁺ |
|------|------------------------|------|--------------------------------------|
| 1 | Food & Drink | 1.91 | 55 |
| 2 | Mechanical Engineering | 1.17 | 50 |
| 3 | Electrical & Optical | 1.08 | 48 |
| 4 | Textiles & Clothing | 1.06 | 45 |
| 5 | Timber & Paper | 1.05 | 40 |
| 6 | Chemicals & Plastics | 0.86 | 45 |
| 7 | Basic Metals | 0.81 | 48 |
| 8 | Other Manufacturing | 0.63 | 48 |
| 9 | Transport | 0.31 | 48 |

Scotland specialisation: Services

| Rank | Sector | LQ | UK Business Activity Index, Jan'23 ⁺ |
|------|--------------------------------|------|---|
| 1 | Hotels, Restaurants & Catering | 1.27 | 52 |
| 2 | Financial Intermediation | 1.10 | 48 |
| 3 | Transport & Communication | 1.04 | 45 |
| 4 | Personal & Community Services | 1.03 | 50 |
| 5 | Business-to-business Services | 0.94 | 50 |
| 6 | Computing & IT Services | 0.71 | 52 |

UK sector focus

Personal & Community Services

After seeing activity levels decline in the latter stages of last year, the UK's Personal & Community Services sector started 2023 on a more stable footing. Key to this was a renewed, albeit marginal, upturn in inflows of new businesses in the three months to January.

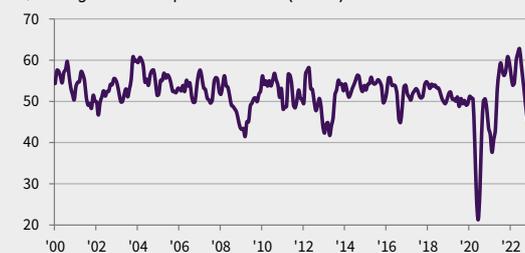
However, with survey data showing a lack of pressure on operating capacity, as evidenced by a marked and accelerated reduction in backlogs of work, firms reduced workforce numbers.

On the cost front, the rate of input price inflation eased only slightly and remained close to the record highs seen in 2022. Of the services sub-sectors mentioned, it was second only to that recorded by Hotels, Restaurants & Catering. Prices charged by Personal & Community Services firms meanwhile rose to the greatest extent since mid-2022.

Positively, expectations towards the year ahead improved, although they remained subdued by historical standards.

Output Index

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



⁺3-month moving average.



UK Regional PMI overview

Business Activity

London was alone among the 12 UK regions monitored by the survey in recording higher activity in January. The rate of growth in the capital remained only marginal, however. There were renewed downturns in output in both Wales and the North West, while the steepest decrease in activity was once again recorded in Northern Ireland.

Employment

Seven of the 12 regions and nations monitored posted a rise in employment in January, up from just four in December. Northern Ireland topped the rankings, registering its steepest rise in workforce numbers for six months, ahead of the West Midlands. The most marked fall in employment was in the North East, as had been the case in the previous survey period.

Future Activity

January data showed a broad-based improvement in business expectations. The greatest increase in confidence was recorded in the West Midlands, which also saw the strongest overall optimism. Sentiment in Northern Ireland turned positive for the first time in nine months, although it remained lower than in any other region or nation.

Business Activity Index

sa, >50 = growth since previous month, Jan '23



Employment Index

sa, >50 = growth since previous month, Jan '23



Future Activity Index

>50 = growth expected over next 12 months, Jan '23



* Coverage in Northern Ireland also includes retail and construction, alongside manufacturing and services.



Index summary

Composite

sa, 50 = no change over previous month. *50 = no change over next 12 months.

| | Business Activity | New Business | Export Climate | Future Activity* | Employment | Outstanding Business | Input Prices | Prices Charged |
|---------|-------------------|--------------|----------------|------------------|------------|----------------------|--------------|----------------|
| Aug '22 | 47.8 | 48.3 | 49.3 | 55.1 | 52.0 | 48.2 | 77.0 | 62.5 |
| Sep '22 | 48.0 | 46.6 | 49.3 | 51.5 | 52.1 | 45.5 | 72.8 | 60.4 |
| Oct '22 | 45.8 | 44.1 | 48.8 | 56.8 | 50.6 | 45.3 | 74.3 | 61.9 |
| Nov '22 | 43.9 | 43.3 | 47.5 | 55.1 | 51.0 | 45.4 | 75.4 | 62.7 |
| Dec '22 | 48.3 | 46.0 | 48.5 | 53.6 | 48.9 | 47.5 | 70.0 | 61.4 |
| Jan '23 | 47.1 | 43.6 | 50.2 | 58.4 | 48.8 | 44.1 | 69.1 | 61.5 |

Manufacturing

sa, 50 = no change over previous month. *50 = no change over next 12 months.

| | Output | New Orders | Future Output* | Employment | Backlogs of Work | Input Prices | Output Prices |
|---------|--------|------------|----------------|------------|------------------|--------------|---------------|
| Nov '22 | 44.5 | 41.5 | 51.8 | 51.6 | 42.2 | 72.8 | 63.0 |
| Dec '22 | 49.2 | 46.1 | 51.8 | 50.6 | 44.7 | 71.9 | 63.7 |
| Jan '23 | 49.9 | 47.1 | 58.2 | 50.1 | 47.3 | 67.1 | 63.8 |

Services

sa, 50 = no change over previous month. *50 = no change over next 12 months.

| | Business Activity | New Business | Future Activity* | Employment | Outstanding Business | Input Prices | Prices Charged |
|---------|-------------------|--------------|------------------|------------|----------------------|--------------|----------------|
| Nov '22 | 43.7 | 43.6 | 55.9 | 50.8 | 46.2 | 76.0 | 62.7 |
| Dec '22 | 48.1 | 46.0 | 54.0 | 48.6 | 48.1 | 69.6 | 60.9 |
| Jan '23 | 46.5 | 42.8 | 58.4 | 48.5 | 43.3 | 69.6 | 61.0 |

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About Royal Bank of Scotland

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

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