Quarterly Economic Indicator Q3 2018

Scottish Chambers of Commerce

Contents

Methodology

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.

Results are reported as the “net % balance”, calculated by deducting the % of firms reporting a decrease from the % of firms reporting an increase.

E.g. If 50% of firms report an increase in profits over the quarter (compared with the previous quarter) and 49% report a decrease, the net % balance of firms reporting an increase in profits is (50-49 = +1).

A negative net % balance generally indicates contraction and a positive net % balance expansion. For further information on the Quarterly Economic Indicator, please contact:

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Foreword

The Scottish economy has experienced a welcome pick-up in activity over the last 12 months, following a challenging couple of years.

The most recent figures show growth - whilst still below its long-term trend – is at its fastest rate since late 2014/early 2015. Indeed, during the first 6 months of 2018, the Scottish economy grew more strongly than the UK as a whole.

Overall however, the outlook remains highly uncertain.

The apparent lack of meaningful progress on the Brexit negotiations is increasingly showing up as a key risk for many Scottish businesses.

It is therefore not surprising that the latest Scottish Chambers of Commerce Quarterly Economic Indicator shows a slight rise in the percentage of firms who are less optimistic than before - an increase from 15% in the 3-months to June to over 20% today. Of particular concern is the relatively sharp decline in optimism amongst manufacturers, with the sector recording its worst performance in two years.

At the Fraser of Allander, we continue to remain cautiously optimistic about the outlook for the Scottish economy this year and next. However, this greatly depends on a broad-based agreement being secured between the UK and the EU which supports continued close economic integration post-March 2019.

Most economists have argued that a 'hard-Brexit' will act as a significant drag on Scotland's – and the UK's – economic potential.

However, it is the risk of a 'no-deal' scenario that is of most concern in the immediate term. Whether you agree or disagree with the decision to leave the EU the need for an orderly transition is vital.

Sleepwalking into a 'no-deal' outcome cannot be viewed as an effective economic plan. Now is the time for effective and strong leadership from all our political leaders.

Professor Graeme Roy
Director, Fraser of Allander Institute

Introduction

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.

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.

A recent survey from the British Chambers of Commerce 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.

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.

Neil Amner
Chair, SCC Network's Economic Advisory Group
Director, Anderson Strathern

Key Findings

OPTIMISM & BUSINESS CONFIDENCE

The third Scottish Chambers of Commerce Quarterly Economic Indicator of the year suggests that Scottish businesses are still broadly confident around the business environment, but optimism is weakening relative to the previous quarter in a number of key sectors.

Across the sample as a whole, before splitting the results by sector, 21% of firms reported that they were less optimistic about the business environment than in Q2 2018. This is in contrast to 15% of firms last quarter, suggesting declining optimism nationally.

Optimism is also declining on an annual basis, with 28% of firms stating that their optimism is lower. This compares to around 24% in the previous quarter. However, confidence is still generally stable, with 32% of firms reporting higher optimism than the same time last year, and 40% reporting that this is unchanged.

When we break down optimism by sector, the manufacturing sector provides cause for concern. At a percentage balance of **-4,** the sector has reported its first negative optimism figure since the third quarter of 2016.

Outside of this however, we've seen relatively strong results for the majority of other sectors in terms of business confidence. Tourism has observed a softening in overall optimism however, perhaps reflecting the traditionally quieter fourth quarter for the sector.

Reasons for optimism change

A range of reasons were provided by firms for their changes in business confidence.

For firms that reported higher levels than in prior periods, comments focused on a steadily improving environment for the Oil and Gas sector, larger infrastructure projects coming online, and steady consumer confidence.

For the minority of firms that reported a more pessimistic outlook, the UK's Exit from the European Union continued to act as a headwind.

Material prices in particular were also cited as as a concern, alongside exchange rate issues and the impact of additional tariffs between major economies.

INVESTMENT

Perhaps reflecting some of the underlying concerns affecting business confidence, we've observed a decline in total investment this quarter, with 16% of firms reporting lower investment across the third quarter.

This compares to only 11% of firms in the prior quarter. However, it's important to note that overall, 29% of businesses still increased their levels of investment in Q3.

On a sectoral basis, only the retail sector is looking to increase overall levels of investment relative to the previous quarter. Construction in particular has dropped to a percentage balance of **0** for investment, the lowest level in a number of years, alongside captial investment turning negative at **-6**, the first negative figure for this indicator since Q1 2016.

For the majority of sectors however, investment remains at positive levels despite an overall decline in net % balance figures.

At a national level, firms were increasing investment for a range of reasons, but the majority were doing so either to increase efficiency (38%), or to expand capacity (34%).

RECRUITMENT DIFFICULTIES

Recruitment difficulties, a persistent challenge of firms in the context of a tight labour market across Scotland and the UK, have been perhaps less consistently spread throughout our analysed sectors this quarter.

Sectors such as construction have observed a substantial softening of recruitment difficulties levels, with levels now comparable with figures seen in late 2016.

In comparison, Financial and Business Services (FBS) has seen a slight increase, up to approximately 44% of recruiting businesses reporting challenges in sourcing appropriate staff.

This is substantially above the third quarter average for the FBS sector, which stands at approximately 28%. Difficulties for this sector were also illustrated at an all time high for the UK in the latest Quarterly Economic Survey from the British Chambers of Commerce.

RECRUITMENT DIFFICULTIES

At a national level, recruitment difficulties have increased marginally over the prior quarter, from 48% of recruiting firms to 51% of businesses in the third quarter.

Despite recruitment difficulties continuing to act as a challenge to firms, the majority did not increase wages this quarter, with 68% of businesses maintaining wages at their previous levels. This trend has been observed across all sectors, with substantially fewer firms proportionally in each sector increasing wages than in the second quarter of the year.

Perhaps coupled with continually falling levels of EEA migrant workers, tourism also continues to be a particularly challenged sector with regards to recruitment, with 79% of actively recruiting businesses struggling to find the right people.

KEY FINANCIAL INDICATORS

Revenue

Nationally, the revenue profile for Scottish businesses remains strong with 43% of firms reporting increased revenue, and 40% stating that revenue remained constant. However, this is slightly down on the previous quarter, where 48% of firms reported an increase and 34% reported level figures. Nevertheless, the majority of firms reporting higher revenue suggests that the Scottish economy is continuing to display resilience despite some of the political headwinds.

Although the majority of sectors are observing slightly lower positive direction of revenues when compared to the previous quarter, all sectors have posted more positive results than at the same time last year, including in retail which reported a negative net % balance figure of **-5** in the third quarter of 2017, compared to **+20** for this quarter.

Despite the lower net % balances in comparison to Q2, the broadly sustained positive figures cross-sectorally for Q3 suggest that the business environment has been strong across the middle of 2018, and that the upswing in business sentiment we observed across the second quarter was not simply a recovery from the challenging first quarter and the "Beast from the East".

KEY FINANCIAL INDICATORS

Profitability and Cashflow

Cashflow and profitability results largely reflect those observed last quarter, in which around a fifth of firms expressed a decline in either metric. Firms continued to be most likely to report stability, with 49% of businesses across our whole sample stating that cashflow levels remain unchanged, and 42% maintaining similar levels of profitability.

Linked to stronger overall operating conditions, sectors such as retail and tourism have expressed substantive improvements in their cashflow and profitability levels.

However, manufacturing has returned to negative cashflow and profitability, with the positive levels observed in the second quarter of the year now reversed. On a trend basis, manufacturing often reports negative results in the third quarter on these metrics however, with the last positive Q3 result for cashflow expressed in 2015.

EXPECTATIONS

Expectations for the fourth quarter of the year appear somewhat muted across many of our analysed sectors.

Across our full sample of firms, a full third are planning to increase prices in the following quarter. This is in line with the sector quarter, with approximately 2/3rds of firms intending to maintain prices at current levels.

Investment also appears to trend towards maintaining the status quo at a national level, with 61% of businesses not looking to change investment levels in the coming quarter. Just over a quarter (27%), are intending to increase investment in Q4 of 2018.

When split by sector, manufacturing in particular displays some concerning results. Compared to the sample as a whole, 41% of manufacturing businesses are intending to increase prices, above the national trend, and investment intentions have decreased from **+31** in the second quarter to **+8** now. Our trend data suggests this is broadly in line with manufacturing in the third quarter, so Q4 results will be key to understand if the negative sentiment expressed by the manufacturing sector in this quarter will be maintained into investment intentions across Q4, which tend to be significantly higher on average.

Construction

BUSINESS OPTIMISM

Business confidence continues to be high in the construction sector, with a net % balance figure of **+20** the highest result observed for the sector since the second quarter of 2016. This is substantially above the average for Q3 in construction of approximately **+8**. The positive sentiment in the sector links to improved growth in the industry observed in both the UK and Scottish GDP measures.

CONTRACTS

The net % balance for overall contracts has increased to **+48**. Although this is a positive figure, with 2014 the last time that similar comparator levels of contracts were seen in the industry, however it's important to note that 43% of firms have seen no change in their overall levels of contracts.

WORK IN PROGRESS

91% of businesses reported that their level of work in progress either increased or remained the same in Q3, giving a net % balance of **+33**. This is broadly in line with last quarter, and above the Q3 average of approximately **+23**.

INVESTMENT

Levels of investment in the construction sector have fallen relative to the previous quarter, hitting negative levels for capital investment (**-6**) and falling substantially with regards to training investment (**+9,** from **+20** in the third quarter).

Although the net % balance for training is somewhat in line with the same time last year, capital investment figures have not been at similar negative levels since the first quarter of 2016. This may reflect firms focusing on margins for the final quarter of the year, as the highest level on record look to increase prices (**+50**), in concert with rising material prices.

CONCERNS + PRESSURES

Raw material prices, a growing concern amidst exchange rate pressures, continued political / supply chain uncertainty and wider use of tariffs, continues to be one of the construction industry's key cost pressures for this quarter, maintained at a level similar to Q2.

Aside from this area, there has been a softening of cost pressures across those monitored by SCC for the industry. Perhaps linked to challenging material costs, firms in the sector became more concerned with rising inflation.

(blank space indicates data not available)				(rounded up to nearest %)		
(balances may not add up to 100% due to N/A responses)				**Q3/18**	**Q2/18**	**Q3/17**
(figures given as % of respondents)	**Up**	**Level**	**Down**	**Net % Balance**	**Last Quarter**	**Last Year**
Business Optimism	40	40	20	**20**	14	16
Sales Revenue						
Total	40	46	9	**31**	23	3
Domestic (Scotland)	29	54	6	**23**	11	6
Rest of UK	14	14	10	**3**	9	-9
Contracts						
Total new contracts	52	43	5	**48**	23	9
Public sector orders	29	29	5	**24**	4	3
Private commercial	19	48	14	**5**	30	15
Domestic/house build	33	38	10	**24**	0	9
Investment						
Total	13	52	13	**0**	9	19
Capital	9	60	14	**-6**	3	14
Training	15	56	6	**9**	20	8
Work in Progress	43	48	10	**33**	32	28
Cashflow	29	56	15	**15**	**17**	-8
Applied for Credit?	10			**10**	**17**	24
Profits	32	50	18	**15**	**-6**	-3
Capacity used (ave. %)				**76**	**82**	83
Employment						
Total	29	68	3	**26**	**21**	14
Recruiting Staff			(yes)	**65**	**58**	57
Recruitment Difficulties			(yes)	**45**	**68**	55
Increased Wages?			(yes)	**26**	**32**	41
Average pay increase (%)				**5.6**	**3.8**	**3.0**
Expectations Next Quarter						
Price Change	50	50	0	**50**	**33**	35
Sales Revenue	50	38	13	**38**	**39**	34
Investment	21	50	11	**11**	**9**	19
Employees	33	67	0	**33**	24	32
Cost Pressures (%)						
Pay Settlements			(yes)	**14**	29	-
Finance Costs			(yes)	**17**	14	-
Raw Material Prices			(yes)	**44**	43	-
Other Overheads			(yes)	**31**	57	-
Concerns (%)						
Interest Rates			(yes)	**22**	23	-
Business Rates			(yes)	**28**	23	-
Competition			(yes)	**14**	26	-
Exchange Rates			(yes)	**8**	6	-
Inflation			(yes)	**28**	20	-
Taxation			(yes)	**19**	49	-

Financial & Business Services

SALES REVENUE

Although there has been a reduction in the percentage balance figures for revenue across some metrics, particularly exports, on the whole, revenue remains strong for the financial and business services sector.

At **+31**, Sales Revenue has outpaced the Q3 average for this quarter substantially (**+10**), and is almost 10 points higher than the previous year.

While it is concerning to see exports begin to slow, it's important to note that the majority of exporting businesses (28% of our FBS sample) are maintaining sales at similar levels to the previous quarter.

Domestically and for the Rest of the UK, revenues remain strong and higher than both the third quarter average, and the overall average percentage balance figures for sales for the Financial and Business Services sector.

EMPLOYMENT

The percentage of firms looking to recruit has steadily risen across the year, from 41% in the first quarter to 58% of firms in Q3.

In line with this, recruitment difficulties have once again begun to grow, with 44% of recruiting firms reporting difficulties in filling vacancies.

This is around 10 percentage points higher than the previous quarter, and is the second highest figure ever recorded for recruitment difficulties for the financial and business services sector.

INVESTMENT

Although Investment Expectations for the next quarter have risen, investment for this quarter was lower for FBS firms, with the exception of training budgets which have observed a very slight rise on the previous quarter.

Both overall and capital investment is now lower than the long term average for these metrics from 2014, but training percentage balances are higher, both on a quarterly and overall basis. This continues to reflect the challenging recruitment environment for FBS firms, driven by the record high employment rates observed across the UK.

CONCERNS

Concerns around general taxation have begun to grow for FBS firms, perhaps reflecting the upcoming Scottish and UK Government budgets, and the growing narrative around taxation targeted at services firms and online businesses.

(blank space indicates data not available)				(rounded up to nearest %)		
(balances may not add up to 100% due to N/A responses)				Q3/18	Q2/18	Q3/17
(figures given as % of respondents)	Up	Level	Down	Net % Balance	Last Quarter	Last Year
Business Optimism	44	40	16	**29**	27	14
Sales Revenue						
Total	46	37	14	**31**	38	22
Domestic (Scotland)	42	39	13	**29**	26	8
Rest of UK	24	39	9	**15**	17	7
Exports	13	28	15	**-2**	9	6
Online	18	22	9	**8**	13	4
Investment						
Total	27	43	11	**15**	22	20
Capital	16	57	10	**7**	15	20
Training	29	46	9	**20**	19	20
Cashflow	30	41	24	**6**	15	6
Applied for credit?	14			**14**	9	13
Profits	35	45	17	**19**	23	7
Capacity Used (Ave. %)				**73**	75	67
Employment						
Total	30	54	11	**18**	12	10
Recruiting Staff	58			**58**	47	52
Recruitment Difficulties	44			**44**	37	32
Increasing Wages	28			**28**	33	27
Average pay increase (%)				**8**	5	6
Expectations Next Quarter						
Price Change	26	73	2	**24**	17	21
Sales Revenue	52	34	14	**38**	32	38
Investment	29	52	9	**20**	8	22
Employees	24	72	4	**19**	16	21
Cost Pressures (%)						
Pay Settlements			(yes)	**13**	8	-
Finance Costs			(yes)	**10**	5	-
Raw Material Prices			(yes)	**17**	10	-
Other Overheads			(yes)	**24**	35	-
Concerns (%)						
Interest Rates			(yes)	**23**	16	-
Business Rates			(yes)	**25**	17	-
Competition			(yes)	**33**	36	-
Exchange Rates			(yes)	**17**	11	-
Inflation			(yes)	**27**	23	-
Taxation			(yes)	**29**	21	-

Manufacturing

ORDERS

Order levels in the Manufacturing Sector, similar to revenue, have been broadly strong this quarter, with domestic results in particular experiencing an upswing relative to the second quarter of the year.

Our results generally suggest a stronger order book for the manufacturing sector than at the same time last year, as despite rest of UK orders reporting as flat, this is stronger than the third quarter of 2017, in which this dropped to negative levels.

CASHFLOW + PROFITS

Unfortunately, despite a generally strong order book and revenue profile, this has not translated directly into cashflow and profitability figures.

For both cashflow (**-4**) and profit (**-3**) levels, more businesses have reported a decline than an increase, which also reflects the negative figures observed for these metrics at the same time last year.

Seasonally across our dataset, the third quarter trends towards negative results for manufacturers in both metrics. Profitability tends to be positive in the fourth quarter, so these results are important to understand the longer term outlook for the sector, as rising material costs continue to put pressure on margins.

CONCERNS + COST PRESSURES

In our second quarter survey, 62% of Manufacturing firms had highlighted raw materials as the main contributor to raising prices. The highest level of any of the sectors surveyed. This has risen slightly to 63% of firms this quarter, suggesting that the continued challenge of raw material costs is yet to subside in any meaningful way for manufacturers in Scotland.

This is reflected in substantially higher quarterly averages for future price changes, maintained at **+41** from the previous quarter, about 13 points higher than the Q3 average over the past few years of **+26**. The need for manufacturers to raise prices, and the price change measure itself, has risen substantially since the Brexit vote and in line with growing competition globally. For comparison, the average net % balance was **+23** from 2012-2015, compared to **+41** from 2016 to the present quarter.

EXPECTATIONS

Aside from price changes, our survey suggests a growing pessimism amongst manufacturers, reflected not only in their negative confidence result (**-4**), but also across future expectations for sales, investment and future recruitment, all down relative to the prior quarter.

(blank space indicates data not available)				(rounded up to nearest %)		
(balances may not add up to 100% due to N/A responses)				**Q3/18**	**Q2/18**	**Q3/17**
(figures given as % of respondents)	**Up**	**Level**	**Down**	**Net % Balance**	**Last Quarter**	**Last Year**
Business Optimism	30	36	34	**-4**	10	4
Sales Revenue						
Total	41	41	19	**22**	24	15
Domestic (Scotland)	38	41	16	**21**	12	9
Rest of UK	30	43	19	**11**	4	2
Exports	23	40	19	**4**	10	11
Orders						
Total	42	35	24	**18**	17	20
Domestic (Scotland)	29	49	14	**16**	8	7
Rest of UK	29	37	29	**0**	21	-2
Exports	21	40	6	**15**	15	11
Work in Progress	31	47	22	**8**	33	23
Investment						
Total	22	59	16	**5**	28	2
Capital	29	48	16	**13**	27	2
Training	27	59	11	**16**	22	9
Cashflow	25	46	29	**-4**	14	-2
Applied for Credit?	8			**8**	12	20
Profits	25	47	28	**-3**	10	0
Capacity Used (Ave. %)				**80**	77	75
Employment						
Total	40	47	13	**27**	27	22
Recruiting Staff			(yes)	**78**	87	78
Recruitment Difficulties			(yes)	**55**	49	31
Increased Wages			(yes)	**28**	40	28
Average pay increase				**3**	3	3
Expectations (next quarter)						
Price Change	41	59	0	**41**	41	43
Sales	33	47	20	**13**	36	45
Investment	22	64	14	**8**	31	7
Employees	9	70	22	**-13**	36	20
Cost Pressures (%)						
Pay Settlements			(yes)	**23**	18	-
Finance Costs			(yes)	**9**	8	-
Raw Material Prices			(yes)	**63**	62	-
Other Overheads			(yes)	**36**	40	-
Concerns (%)						
Interest Rates			(yes)	**14**	6	-
Business Rates			(yes)	**23**	14	-
Competition			(yes)	**32**	34	-
Exchange Rates			(yes)	**48**	40	-
Inflation			(yes)	**36**	24	-
Taxation			(yes)	**13**	20	-

Retail & Wholesale

OPTIMISM / BUSINESS CONFIDENCE

The retail sector has continued to observe relative high levels of business confidence, perhaps buoyed by the strong weather, and growing visitor numbers to Scotland acting to stabilise high street footfall.

This is the first time since the third quarter of 2013 that a positive net % balance figure has been observed in the retail sector, with the sector also now experiencing four positive net % balance results for the metric across the prior four quarters. This is the first time this has been observed in our dataset for the sector, which has generally trended towards a more negative outlook.

SALES REVENUE

Although the sector has continued to observe rising business confidence, revenue results are less positive in some areas, with declining levels of domestic and rest of UK sales.

Positively though, in a reversal of last quarter, online sales have now returned to **+16** from a negative figure in Q2, and now sit above the overall average of **+10**.

For domestic and rest of UK sales, the figures, while representing a decline relative to Q2, do trend above the third quarter average to date, suggesting that retail has continued to experience a period of general stability across the past few quarters.

PROFIT & CASHFLOW

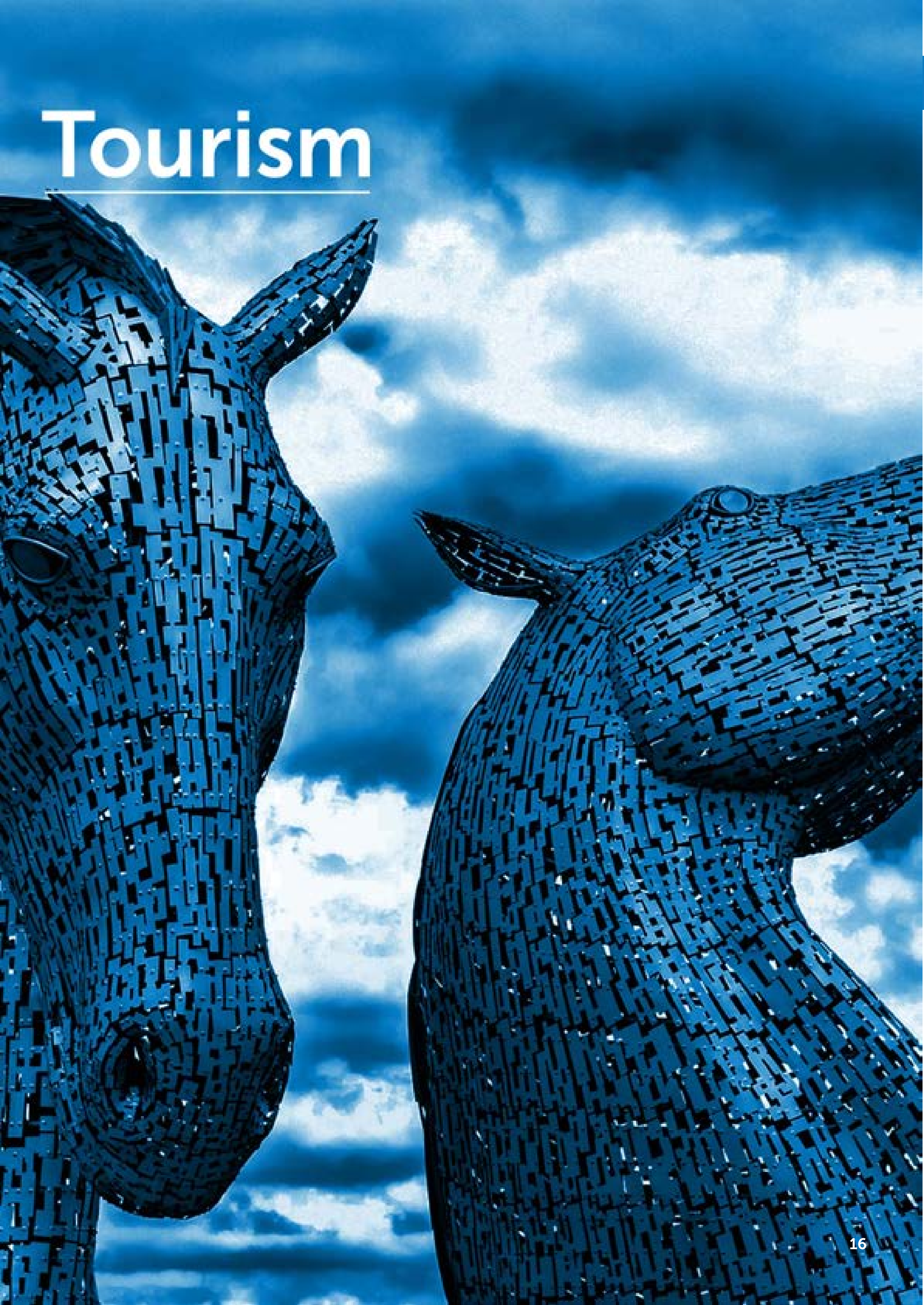
Linked to this generally positive outlook and revenue profile, the retail industry has also seen some improvement in other measures of business health.

At a net % balance figure of **+0**, cashflow appears to be broadly stable for the industry, with the half of all firms reporting that their cashflow has remained stable relative to the prior quarter. This does represent a decline from the positive result reported in Q2 however.

Profitability has reported a relatively high result, at **+14**. This is one of only five positive net % balance results for profitability seen from the end of 2014 to the present quarter, highlighting the shift in the sector which continues to experience profound structural change.

Expectations for the fourth quarter remain strong, with expected sales for Q4 (**+40**) the second highest result recorded for the sector. Interestingly, the prior quarter result of **+45** was the highest, linking in to the broadly increased levels of confidence in the sector across the past number of quarters.

(blank space indicates data not available)				(rounded up to nearest %)		
(balances may not add up to 100% due to N/A responses)				Q3/18	Q2/18	Q3/17
(figures given as % of respondents)	Up	Level	Down	Net % Balance	Last Quarter	Last Year
Business Optimism	41	47	12	**29**	16	-10
Sales Revenue						
Total	43	33	24	**20**	29	-5
Domestic (Scotland)	29	37	22	**8**	25	-13
Rest of UK	18	30	16	**2**	11	5
Exports	18	27	10	**8**	0	13
Online	28	37	12	**16**	-3	19
Investment						
Total	30	43	7	**23**	3	0
Capital	24	41	12	**12**	-3	5
Training	24	35	8	**16**	11	-5
Cashflow	23	50	23	**0**	3	-16
Applied for Credit?			(yes)	**20**	14	16
Profits	37	35	23	**14**	0	-15
Capacity Used (Ave %)				**1**	1	1
Employment						
Total	24	65	6	**18**	17	-5
Recruiting Staff			(yes)	**65**	48	50
Recruitment Difficulties			(yes)	**31**	71	37
Increased Wages?			(yes)	**29**	54	32
Average Pay Increase				**9.5%**	5.0%	3.3%
Expectations Next Quarter						
Price Change	43	53	4	**39**	41	39
Sales Revenue	48	42	8	**40**	45	13
Investment	22	44	15	**7**	28	-11
Employees	11	80	9	**2**	21	11
Cost Pressures (%)						
Pay Settlements			(yes)	**9**	13	-
Finance Costs			(yes)	**15**	6	-
Raw Material Prices			(yes)	**25**	35	-
Other Overheads			(yes)	**32**	55	-
Concerns (%)						
Interest Rates			(yes)	**21**	6	-
Business Rates			(yes)	**25**	35	-
Competition			(yes)	**30**	29	-
Exchange Rates			(yes)	**19**	19	-
Inflation			(yes)	**25**	39	-
Taxation			(yes)	**15**	29	-



Tourism

GUESTS/CUSTOMERS

For the most part, the tourism sector has maintained relatively strong sales and guest levels across the middle of 2018, with the third quarter continuing the trend of strong visitor numbers which are reflected in official data.

In particular, guests from the EU **(+27)** and Rest of the World / Non-EU **(+33)** continued to grow, with both figures substantially above the annual and quarterly averages across our dataset.

ONS data reflects this, with the rise attributed to the weaker pound.

INVESTMENT & EMPLOYMENT

Seasonal factors continue to influence the investment and employment behaviour of tourism businesses, with the quieter Q4 period leading to a rise in investment intentions for this quarter (**+18**), with the fourth quarter often seen as a period to improve premises as guest numbers fall.

Employee expectations are also flat, with the majority of firms not looking to increase their employee count at the end of the year.

Given the generally positive quarter and record number of visitors expressed across Scotland, this has been reflected in increased recruitment behaviour this quarter.

85% of firms tried to recruit, and 79% of these, the highest figure recorded since the second quarter of 2016, experienced difficulty in trying to fill these vacancies. Part of this challenge will be accounted for by the record high employment rate, but tourism and hospitality also employ a higher proportion of migrant workers than the majority of sectors, and falling numbers of EU migrants travelling to the UK seeking work will also act to put pressure on the industry.

EXPECTATIONS AND CONCERNS

Expectations are similarly in line with prior perceptions of the fourth quarter as a traditionally quieter period for the industry. Sales expectations in particular have decreased dramatically, from **+50** last quarter (referring to expectations for Q3), to **+3** now when businesses consider fourth quarter sales.

Business rates and general taxation continue to act as key pressures on this industry, and the sector will be one of many expecting continued progress on reform of the Business Rates system, as the Scottish Government looks to implement some of the key Barclay reforms.

(blank space indicates data not available)				(rounded up to nearest %)		
(balances may not add up to 100% due to N/A responses)				Q3/18	Q2/18	Q3/17
(figures given as % of respondents)	Up	Level	Down	Net % Balance	Last Quarter	Last Year
Business Optimism	44	38	18	**26**	32	11
Sales Revenue						
Total	50	39	11	**39**	42	37
Domestic (Scotland)	50	34	13	**37**	38	2
Rest of UK	23	33	17	**7**	33	14
Online	50	20	10	**40**	35	23
Investment						
Total	20	50	17	**3**	24	18
Capital	28	49	13	**15**	11	11
Training	15	62	8	**8**	14	8
Cashflow	49	41	10	**38**	34	33
Applied for credit			(yes)	**23**	18	23
Profits	53	37	10	**43**	16	19
Employment						
Total	23	67	8	**15**	30	10
Recruiting Staff			(yes)	**85**	76	77
Recruitment difficulties			(yes)	**79**	60	65
Increased wages?			(yes)	**38**	64	46
Average pay increase (%)				**4**	5	7
Guests/Customers vs last year						
Total	61	21	18	**43**	31	23
From Scotland	33	50	17	**17**	14	11
From Rest of UK	33	47	20	**13**	17	11
From Rest of EU	50	27	23	**27**	22	30
From Outside the EU	50	30	17	**33**	28	25
Expectations Next Quarter						
Price Change	30	62	8	**22**	31	29
Sales	31	41	28	**3**	50	-13
Investment	21	61	4	**18**	9	-2
Employees	17	66	17	**0**	12	-8
Cost Pressures (%)						
Pay Settlements			(yes)	**33**	42	-
Finance Costs			(yes)	**28**	21	-
Raw Material Prices			(yes)	**54**	47	-
Other Overheads			(yes)	**46**	50	-
Concerns (%)						
Interest Rates			(yes)	**18**	8	-
Business Rates			(yes)	**44**	32	-
Competition			(yes)	**46**	29	-
Exchange Rates			(yes)	**18**	24	-
Inflation			(yes)	**38**	50	-
Taxation			(yes)	**46**	39	-

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