Scottish Enterprise

Economic Commentary

April 2024
Insights and Economics

Economic Commentary: Highlights

Scottish Enterprise

SUMMARY

- The IMF is forecasting global GDP growth will remain ‘steady but slow’ at 3.2% over 2024 and 2025, the same pace as in 2023. Emerging and developing market economies are expected to grow much faster than advanced economies.
- Business activity continued to increase across all major global economies in March, although the pace slowed in both the US and UK. The euro area remains the weakest performer.

RECENT ECONOMIC DATA

- The UK economy grew in both January (+0.3%) and February (+0.1%). Although growth is weak, it does suggest that the UK recession has not extended into the first quarter of this year.
- Consumer price inflation fell to 3.2% in the year to March 2024, the lowest for two and a half years.
- Business activity in March rose in 11 out of 12 UK regions (including Scotland) supported by a general upturn in demand. Positively, UK manufacturing output returned to growth for the first time in five months. In Scotland, business activity growth was driven exclusively by the service sector, while manufacturing output continued to decline.

CURRENT BUSINESS SENTIMENT

- The Scottish economy grew by 0.6% in January, following +0.4% in December, significantly stronger than UK performance.
- 31% of Scottish businesses reported an increase in monthly turnover in February, an increase of 9pp on the previous month and the highest for almost a year.
- Scotland’s labour market shows signs of cooling - the unemployment rate increased 0.8ppts to 4.0% over the year to December - February, while the employment rate fell to 74.2%. Fewer Scottish businesses are reporting worker shortages and recruitment activity also slowed in March.

OUTLOOK

- SE customers are generally reporting strong order books, and becoming more optimistic as input price inflation eases, providing more certainty about future costs and helping build confidence to invest in growth opportunities. Main challenges are attracting skilled staff, availability of property and for some access to growth finance.
- The OBR is forecasting UK GDP growth to increase slightly to 0.8% in 2024 then to 1.9% in 2025.
- For Scotland, the Fraser of Allander Institute (FAI) is less optimistic with economic growth forecasts of 0.6% in 2024 and 1.1% in 2025.

SUMMARY

RECENT ECONOMIC DATA

CURRENT BUSINESS SENTIMENT

OUTLOOK

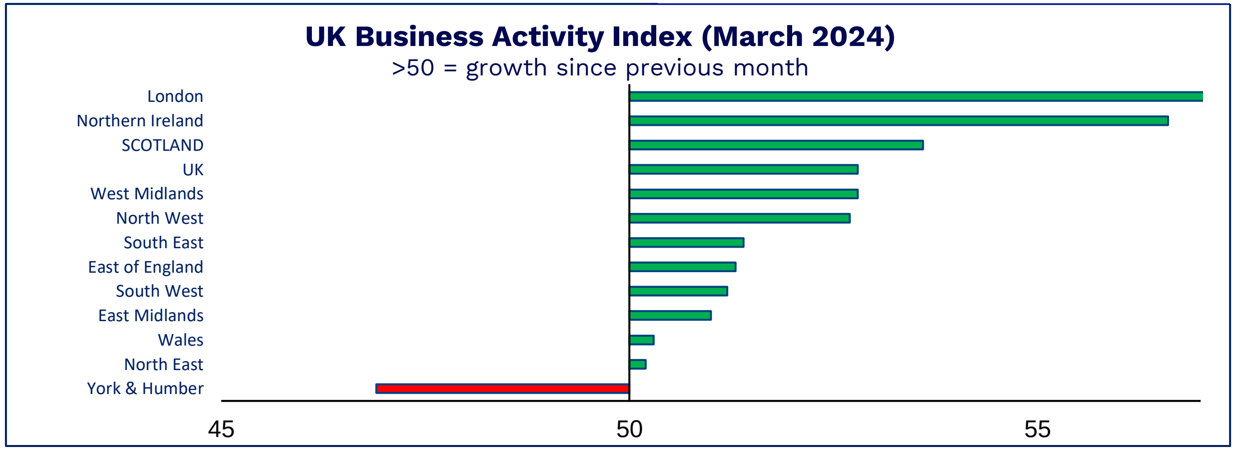
Global/UK

Business activity continued to expand across all major regions in March, though growth slowed in both the US and the UK. The euro area was the weakest performer. Globally, output expanded at its fastest rate since June 2023 for both the services and manufacturing.

UK business sector output rose across 11 out of 12 nations/regions in March, supported by a general upturn in demand. London continued to lead the way, followed by Northern Ireland then Scotland. Only Yorkshire and Humber reported a contraction. New order inflows also rose across most areas.

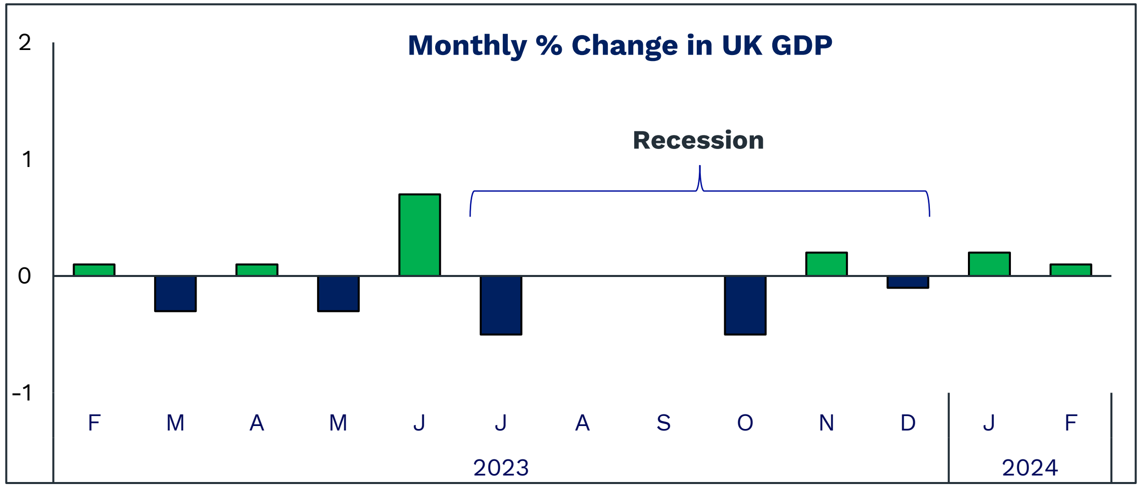
Business Activity Index (>50 indicates increase vs previous month)

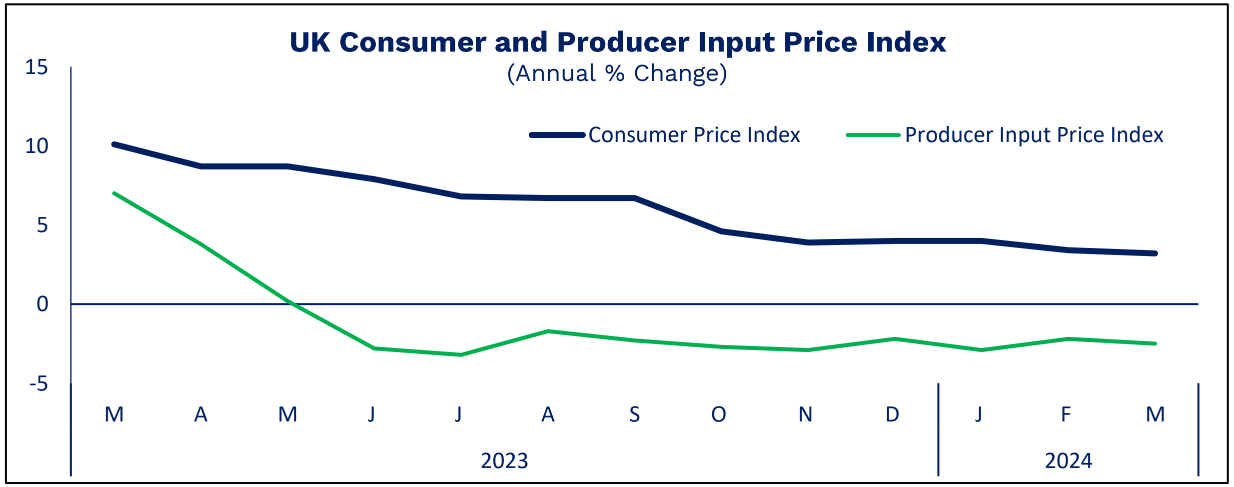
2023	Oct	Nov	Dec	Jan	Feb	Mar
Global	50	50.5	51.0	51.8	52.1	52.3
UK	48.6	50.1	52.1	52.5	53.0	52.8
China	50	51.6	52.6	52.5	52.5	52.7
US	50.7	50.7	52.3	50.9	52.5	52.1
Japan	50.5	50	50	51.5	50.6	51.7
Euro area	46.5	47.6	47.6	47.9	49.2	50.3



The UK economy grew by 0.1% in February 2024, down slightly from +0.3% in January. February's growth was driven by both services and manufacturing, with construction output contracting (poor weather a factor). Growth in January and February follows contractions in both Q3 and Q4 2023, suggesting the UK recession may be over.

Consumer price inflation was 3.2% in the 12 months to March 2024, down from 3.4% in February and the lowest for two and a half years. Core inflation rose by 4.2% over the year, down 0.3pp on the previous month. Producer input prices fell for the 10th consecutive month. Despite inflation slowing, it still remains above the Bank of England target of 2%.





SUMMARY

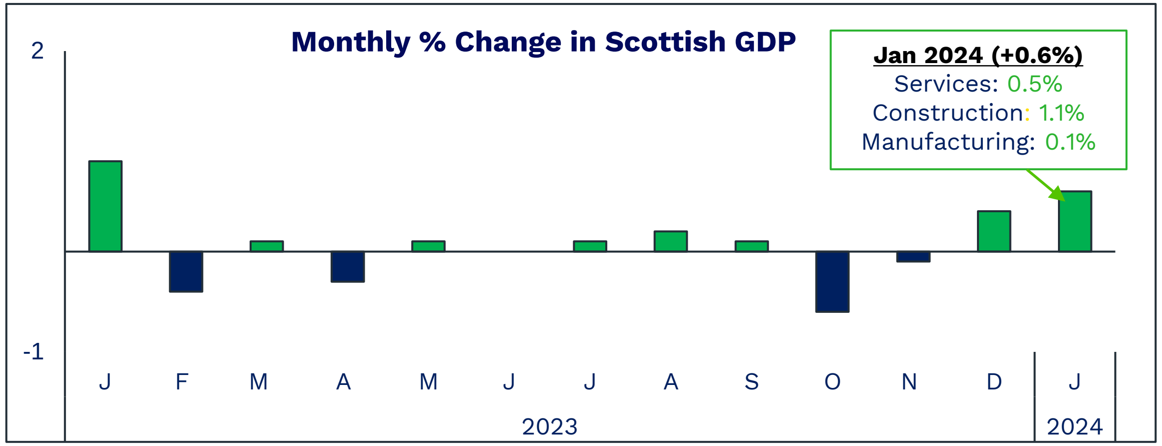
RECENT ECONOMIC DATA

CURRENT BUSINESS SENTIMENT

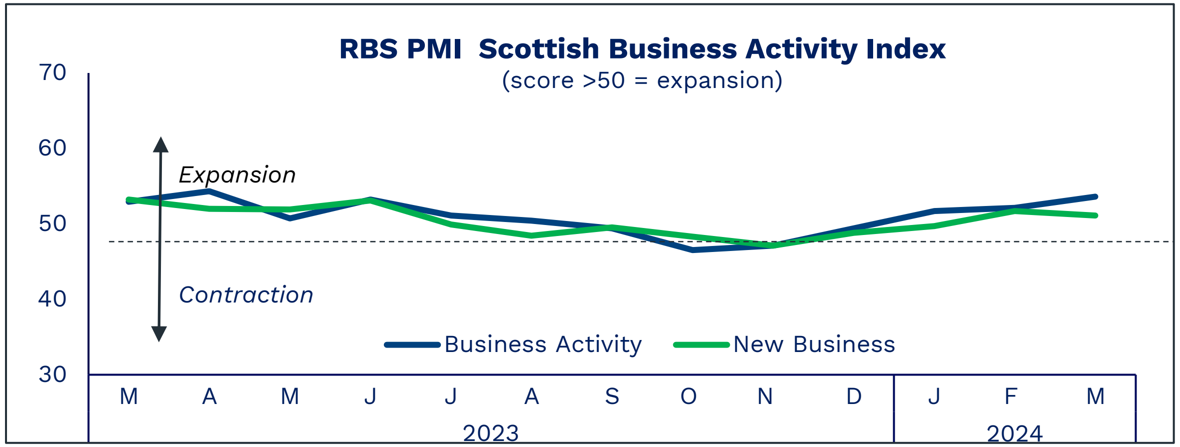
OUTLOOK

Scotland

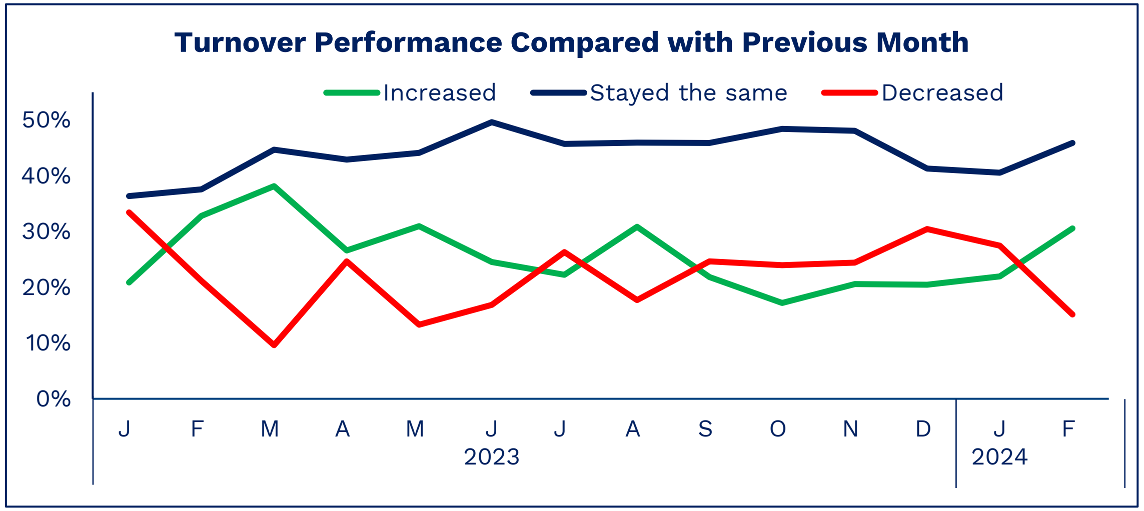
The Scottish economy grew in January 2024 by 0.6%, following +0.4% in December, far stronger than UK performance. Over 2023, the Scottish economy grew by 0.2%, slightly weaker than the UK average. Positively, Scotland's manufacturing output returned to growth in January for the first time since July 2023.



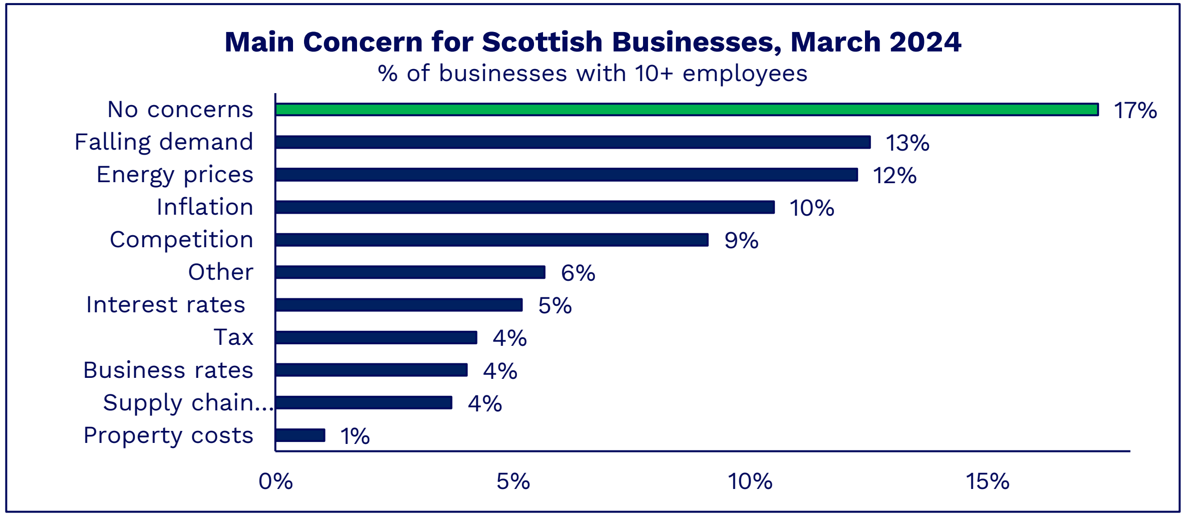
Scottish business activity rose in March for the 3rd consecutive month. Growth though has driven exclusively by the service sector as manufacturing activity contracted for the 9th successive month, and at a faster rate than February, contradicting signs of a manufacturing recovery across the UK.



31% of Scottish businesses reported a rise in monthly turnover in February, a significant increase (+9pp) on the previous month and the highest percentage for almost a year; 15% reported a decrease. The top three challenges to growing turnover are labour costs, cost of materials and economic uncertainty.



Excluding staffing issues, the main concern for businesses remains falling demand closely followed by energy prices. However, encouragingly, 17% of businesses reported no major concerns, down from 13% in April 2023.

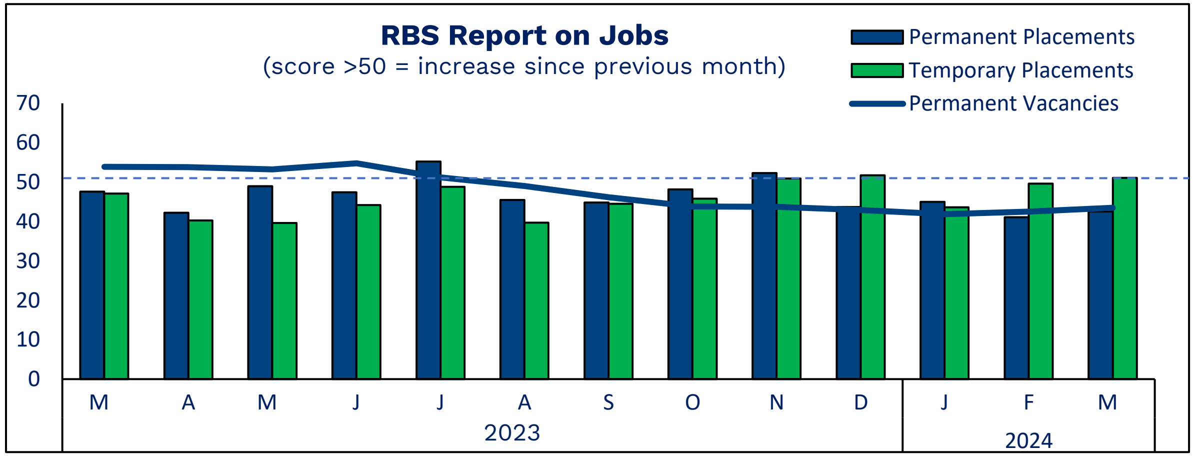


SUMMARY

Scotland

Scottish unemployment increased by 0.8ppts over the year to Feb 2024 to 4%, but was below the UK figure of 4.2%. The employment rate also fell by 0.9ppts to 74.2%, slightly below the UK's (74.5%). Economic inactivity has risen over the year by 0.2ppts to 22.6% (vs the UK's 22.2%), driven by an increase in long term sickness.

Recruiters reported further signs of an easing in the labour market in March as vacancies for both permanent and short-term workers fell for the 8th successive month. Uncertainty about the economic outlook and businesses looking to cut expenses impeded hiring. Pay pressures eased with both starting salary and hourly wage inflation below their long-run averages.

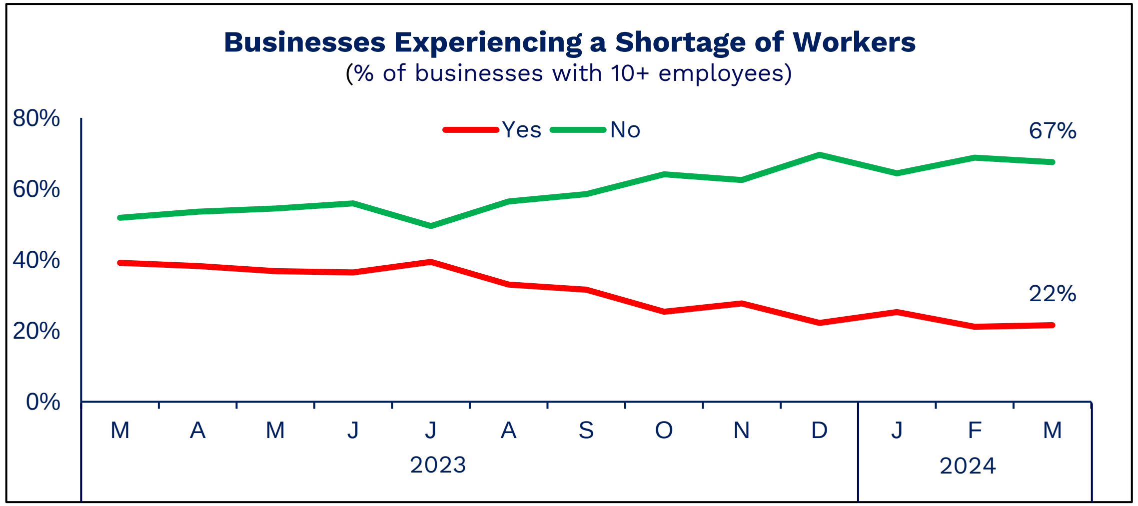


RECENT ECONOMIC DATA

	RATE (Dec 23 – Feb 24)	ANNUAL CHANGE
EMPLOYMENT (16-64)	74.2%	-0.9%pts
UNEMPLOYMENT (16+)	4.0%	+0.8%pts
ECONOMIC INACTIVITY (aged 16-64)	22.6%	+0.2%pts

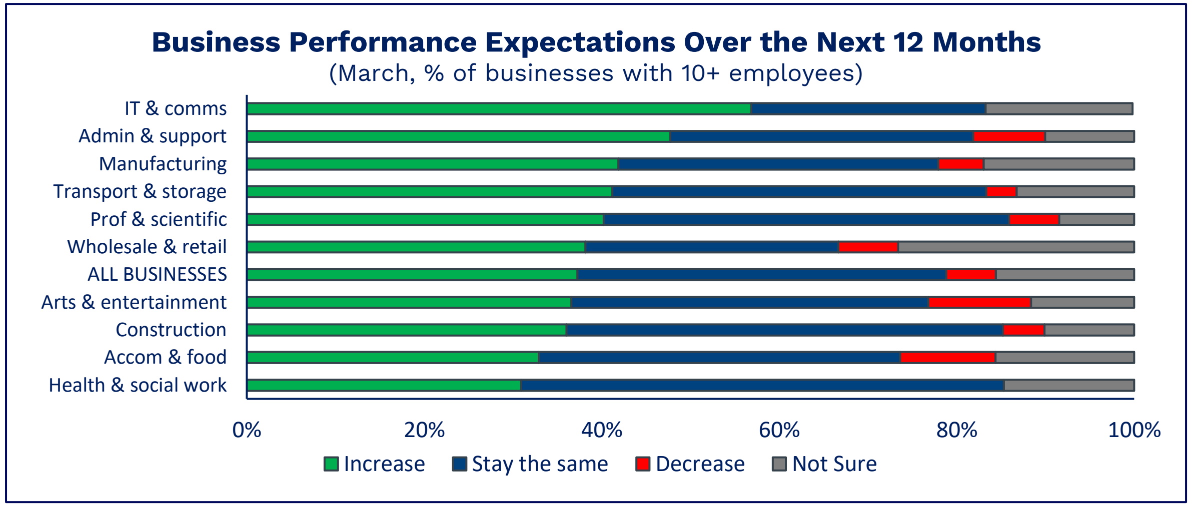
CURRENT BUSINESS SENTIMENT

22% of Scottish businesses reported worker shortages in March, down significantly from last summer. Some sectors are more affected than others, however, with 35% of Construction businesses experiencing shortages. 60% of those affected by worker shortages are increasing employee working hours, while 40% are unable to meet demand.



OUTLOOK

In March, 37% of Scottish businesses were optimistic about their performance over the next 12 months, with only 6% expecting it to worsen. The IT & Communications and Admin & Support sectors were the most optimistic, with Accommodation & Food and Health and Social Work the least.



Feedback from Scottish Enterprise Customers

General Sentiment

- Businesses are generally reporting **strong order books**, are **eager to invest** and explore growth opportunities, albeit for some in a cautious way. As input price inflation eases, this is providing more certainty about future costs.
- However, challenges continue with **staffing and recruitment** (high staff turnover and low numbers of applicants for jobs), **availability of property** and **access to investment funding** particularly for early-stage businesses.

Labour and Skills

- Recruiting **skilled labour** remains challenging for many businesses. Key issues include:
  - attracting suitable candidates for both **lower and higher-skilled positions.**
  - **rising** wage expectations due to inflation.
- Some businesses in lower margin sectors are concerned about the impacts on wage bills of April's increase in the **National Living Wage**.

Access to Finance

- While some businesses still rely on grants for funding, others are exploring financing options with banks. **Securing funding from banks** is no longer as challenging as it has been although businesses remain cautious about taking on debt.
- Some **early-stage** businesses are finding it challenging to raise finance, particularly at the **early seed and pre-seed stages**, prompting them to engage with funders **in the rest of the UK**.

Cost of Doing Business

- Positively, the cost of energy has decreased, but cash flow issues remain due to **higher material costs and wages.**

Exporting

- Post Brexit, many businesses continue to be cautious about exporting to the European market. **High transportation and administration time and costs**, both for exporting and importing, are factors.

Property

- Many companies highlight **difficulties finding suitable property** for expansion which reduces the capacity to take on additional work. This is especially the case for **smaller manufacturers**, where there is a lack of medium-sized, energy efficient units.
- The life sciences sector continues to face a **shortage of laboratory space**. For the space that is available, it often requires costly conversion making it uneconomic.
- Some businesses looking to expand their existing property or move to a new site report a **shortage of utility infrastructure** (water, waste and energy). This can add significantly to project build costs.

Innovation

- A small but growing number of businesses are starting to use **artificial intelligence (AI)** in their back-office activities (e.g. writing reports, preparing tenders). This helps reduce costs, address staff shortages and increase efficiency. However, some say the results (e.g. quality of outputs) can be mixed.

Supply Chain

- Supply shortages exacerbated by **long lead times** and concerns about **component quality** and **customer service**, are prompting some businesses to consider in-house production for greater supply chain resilience

Exporting

- Post Brexit, many businesses continue to be cautious about exporting to the European market. **High transportation and administration time and costs**, both for exporting and importing, are factors.

Net Zero

- Businesses are exploring **new approaches to increase efficiency and reduce emissions,** including **monitoring buildings** to identify ways of saving energy. Businesses are developing AI to support this.

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OUTLOOK

Economic Outlook

Global Forecasts

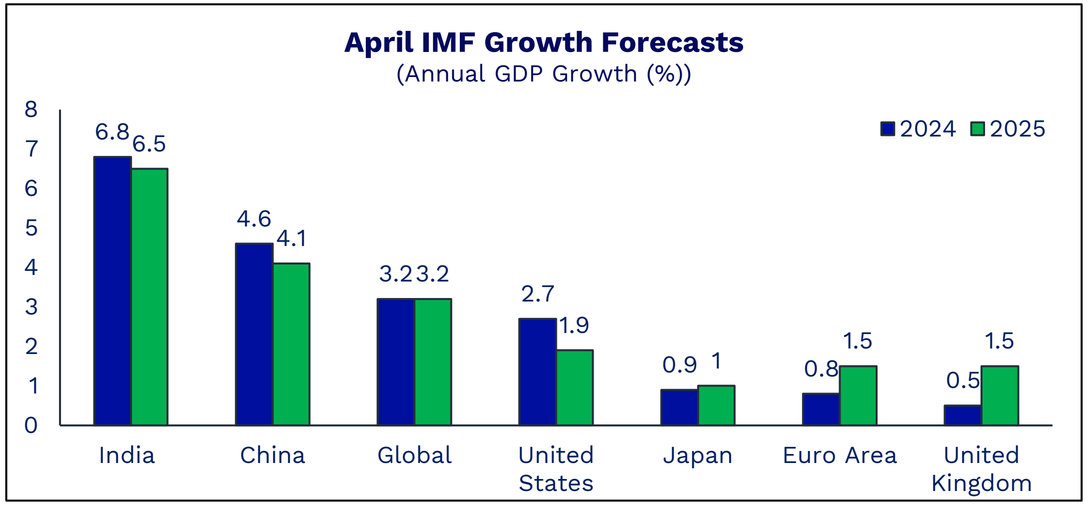
The IMF is forecasting global GDP growth to remain 'steady but slow' at 3.2% over 2024 and 2025, the same pace as in 2023.

Rates of growth differ across regions, however. Emerging and developing market economies (including China and India) are expected to grow by 4.2% this year, whereas 1.7% is forecast for advanced economies.

The UK is expected to be one of the weaker performers amongst advanced economies in 2024, partly due to higher interest rates. Growth is expected pick up to 1.5% in 2025, matching the euro area.

The IMF notes the following key risks to the global economy:

- price spikes and trade slowdowns stemming from geopolitical tensions, including those from the war in Ukraine and the conflict in Gaza and Israel.
- persistent core inflation resulting in high interest rates, putting extra pressure on household spending.
- falling economic growth in China damaging trading partners.



UK and Scottish Forecasts

In March, the OBR forecast UK GDP growth to increase slightly to 0.8% in 2024 rising to 1.9% in 2025 and 2% in 2026 as interest rates and real household incomes recover. The OBR noted:

- CPI inflation is expected to fall to an average of 2.2% in 2024 and 1.5% in 2025.
- Interest rates are expected to fall to 4.2% by the end of 2024.
- Nominal average pay growth is expected to halve in 2024 as inflation falls and the labour market weakens.
- Real household disposable income is expected to recover to its pre-pandemic level by 2025-26.

For Scotland, the Fraser of Allander Institute (FAI) forecast 'poor but improving' economic growth of 0.6% in 2024 and 1.1% in 2025.

FAI points to falling inflation and increasing consumer sentiment as positive drivers of GDP, but also note that most consumer sentiment indicators remain negative, emphasising the scale of the challenges the economy and households face.

Overall, the FAI note that forecast growth is *'fragile and may be blown off course by events, particularly given geopolitical uncertainty this year'.*