

Royal Bank of Scotland PMI®

Output declines further in January as business confidence falls

Key Findings

Manufacturing and service sector output declines

Demand for services rises, but falls for goods

Future output expectations hit 21-month low

Scotland Business Activity Index



Last six months SC / UK



By sector	Jan-19
Manufacturing	47.0
Services	49.6

According to the latest Royal Bank of Scotland PMI®, output across Scotland's private economy declined for a second successive month at the start of 2019, the first time since August 2016 that a back-to-back drop in activity has been recorded. New business also fell in January, enabling firms to clear backlogs of work. Output expectations were also pared back, with optimism easing to a 21-month low.

The seasonally adjusted headline Royal Bank of Scotland PMI posted 49.2 in January, a fraction below December's print of 49.3. Although this signalled only a mild reduction in private sector output in Scotland, it was the strongest in almost two-and-a-half years. As was the case in December, the downturn was broad-based across both manufacturing and service sectors. Anecdotal evidence indicated that heightened uncertainty and faltering consumer confidence had contributed to lower activity levels.

Of the 12 monitored UK areas, four recorded lower output in January and only London observed a faster decrease than Scotland.

Demand

Latest survey data signalled falling demand in Scotland, but the sector split revealed the drop was driven by manufacturers, as service providers recorded mild growth. According to goods producers, order intakes fell as a result of diminished client demand. Uncertainty was also mentioned by panellists as a factor impacting order book volumes. At the UK level,

private sector new order intakes decreased modestly and at a quicker rate than observed across Scotland.

Capacity

A solid decrease in manufacturing orders and just a mild rise in demand for services coincided with a further monthly decline in outstanding workloads in January. Both sectors reported reduced backlogs, but the rate of depletion was softer than in December in both cases.

Some panellists attributed lower volumes of incomplete work to increased staffing levels. Survey data pointed to further job creation in Scotland during January, extending the current upturn in recruitment to 11 months. This contrasted with the overall UK trend, where workforces were reduced.

Prices

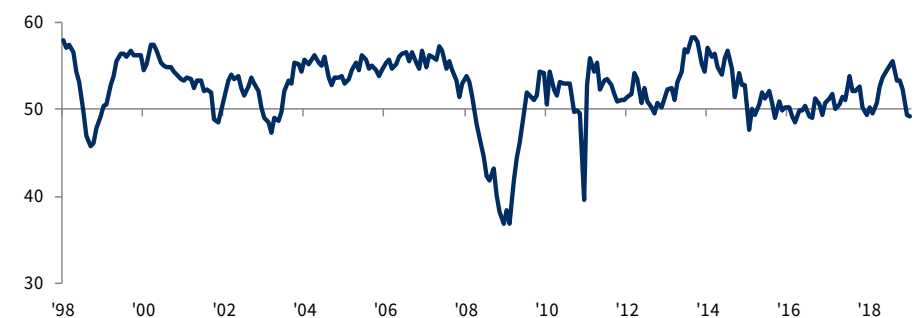
Inflationary pressures eased across Scotland in January, with both input costs and output prices increasing at slower rates. That said, operating expenses rose sharply amid reports of sterling weakness and increased raw material costs.

Outlook

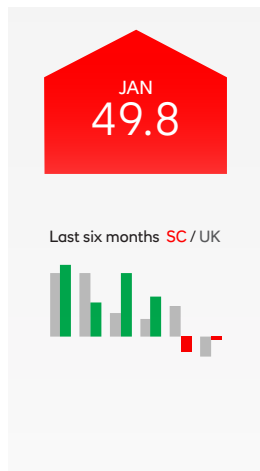
Lastly, business confidence dipped to a 21-month low in January, with economic uncertainty weighing on sentiment. That said, strategic changes, new product offerings and planned efficiency improvements were all cited as reasons to be optimistic overall.

Scotland Business Activity Index

sa, >50 = growth since previous month



New Business Index



Unfavourable demand conditions persist in January

Private sector firms in Scotland recorded a decrease in new workloads at the start of 2019, as was also seen during December. Weak consumer confidence, Brexit-related uncertainty and slowing demand contributed to the fall in new business, according to panel members. A strong downturn was seen in the manufacturing sector, where new orders fell at the sharpest rate in two-and-a-half years. Meanwhile, service providers registered mild growth. That said, the overall reduction was only marginal and softer than seen for the UK overall.

New Business Index

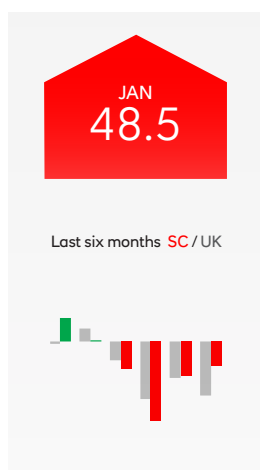
sa, >50 = growth since previous month



By sector

	Manufacturing	Services
Jan-19	46.1	50.7

Outstanding Business Index



Capacity pressures continue to alleviate

A fourth successive monthly decline in outstanding business was signalled by January survey data. Capacities at both manufacturing and service companies were relieved, with the former experiencing the stronger reduction in unfinished workloads. A combination of increased staffing levels and reduced inflows of new orders enabled companies to make further inroads to their backlogs. At the UK level, capacity pressures eased to a greater extent than in Scotland for a second month running.

Outstanding Business Index

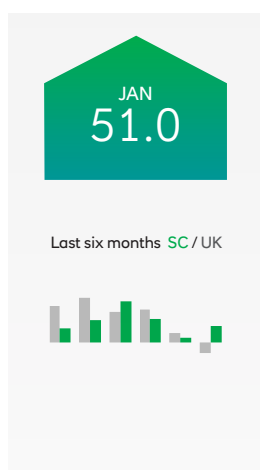
sa, >50 = growth since previous month



By sector

	Manufacturing	Services
Jan-19	44.0	49.6

Employment Index



Employment grows in Scotland, but falls across UK as a whole

Job creation in Scotland's private economy was sustained during January, marking an eleventh successive month of rising staffing levels. The expansion quickened from December, but was only mild. Furthermore, sector data revealed a broad-based upturn across both manufacturing and services. The employment trend in Scotland diverged from that seen for the UK as a whole in January, where recruitment declined for the first time since July 2016, the immediate month after the EU referendum.

Employment Index

sa, >50 = growth since previous month



By sector

	Manufacturing	Services
Jan-19	51.5	50.9

Input Prices Index



Costs rise sharply, but inflation rate eases to six-month low

Cost pressures remained elevated during the latest survey period amid reports of unfavourable exchange rate variation and increased energy, food, transportation and wage expenses. Although the rate of inflation eased to a six-month low, it was marked overall and broadly in line with the UK average. Industry-level data signalled a sharper increase at manufacturers than service providers.

Input Prices Index

sa, >50 = inflation since previous month



By sector

	Manufacturing	Services
Jan-19	64.5	60.6

Prices Charged Index



Selling prices rise moderately in January

Latest survey data pointed to a marked rise in prices charged for goods and services in Scotland. As was the case with input costs, the rate of inflation softened from December and was close to that seen for the UK overall in January. Panellists suggested that prices rises were part of efforts to share greater cost burdens with clients.

Prices Charged Index

sa, >50 = inflation since previous month



By sector

	Manufacturing	Services
Jan-19	58.3	51.9

Future Output Index



Business confidence dips to lowest since April 2017

Private sector firms in Scotland remained optimistic that output would increase over the coming 12 months. Strategic changes, new product offerings and planned efficiency improvements underpinned confidence. That said, the level of positive sentiment eased to the lowest in almost two years and was lower than seen for the UK overall, with Brexit uncertainty impacting expectations.

Future Output Index

>50 = growth expected over next 12 months

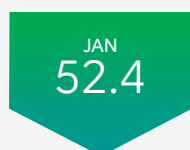


By sector

	Manufacturing	Services
Jan-19	57.6	60.0

Scotland Export Climate Index

Note: Export markets are defined as non-UK.



Last six months



Growth at key trading partners continues to ease

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 Export Climate Index fell for a fifth month running in January, dipping to 52.4 from 52.9 in December. Although in aggregate, Scotland's export markets are still growing moderately, the latest reading signalled the weakest rate of improvement in the Scottish export climate in just over two-and-a-half years.

A faster downturn in France was coupled with slower growth in China and the Netherlands during January, three of Scotland's biggest trading partners. A slightly faster expansion in Germany failed to offset slowdowns in other parts of Europe, while US growth was unchanged from December.

Export Climate Index

sa, >50 = improving export climate since previous month



Top export markets, Scotland

Rank	Market	Weight	Output Index, Jan-19
1	Netherlands	15.0%	55.3
2	USA	11.6%	54.4
3	Germany	9.7%	52.1
4	China	7.7%	50.9
5	France	6.3%	48.2

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, Jan-19 (3mma)
1	Food & Drink	1.80	55.3
2	Wood & Paper	1.18	54.4
3	Textiles & Clothing	1.16	52.1
4	Electrical & Electronic	1.04	50.9
5	Chemicals, Rubber & Plastics	0.94	48.2
6	Machinery & Equipment	0.93	48.2
7	Metals & Metal Products	0.89	48.2
8	Other Manufacturing	0.78	48.2
9	Transport Equipment	0.35	48.2

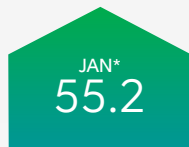
Services specialisation: Scotland

Rank	Sector	LQ	UK Business Activity Index, Jan-19 (3mma)
1	Hotels, Restaurants & Catering	1.27	55.3
2	Financial Intermediation	1.06	54.4
3	Other personal/consumer Services	1.05	52.1
4	Transport & Communication Services	1.02	50.9
5	Business-to-business Services	0.95	48.2
6	Computing & IT Services	0.68	48.2

45 50 55 60

UK Sector Focus: Computer & IT Services

Output Index



Last six months*



*3mma

Strong growth in UK tech services defies broader economic slowdown

As the UK private sector saw growth ease to near-stagnation at the start of the year, one area that continued to exhibit a robust rate of expansion was computing & IT services.

The increase in output during the three months to January was the steepest among all the broad service sectors monitored by the survey. And it was supported by strong underlying demand, with computing & IT firms recording the sharpest rise in inflows of new work since mid-2018.

Encouraged by growing workloads and a positive outlook for activity in the year ahead, firms in the sector continued to add to their staffing numbers. Moreover, the rate of job creation gathered pace and was one of the quickest seen over the past five years. This increased demand for staff was in turn reflected in sustained strong wage pressures across sector.

Output Index

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



Employment Index

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



UK Regional Rankings

Business Activity

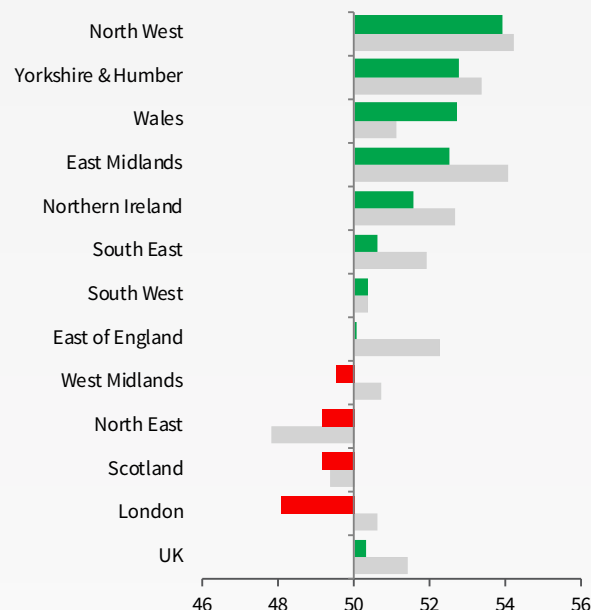
The North West saw the strongest business activity growth for the second month running in January, followed by Yorkshire & Humber and Wales. The latter was the only area of the UK where growth improved significantly from December, with performances deteriorating in most other parts. Notably, London and Scotland saw business activity drop to the greatest extent since July 2016 and August 2016 respectively. The West Midlands and North East also recorded contractions in output, while business activity in the East of England stagnated, to end a six-year spell of growth in the region.

Employment

The North West and Yorkshire & Humber jointly-led the regional rankings for employment growth in January, albeit at a rate that was only modest overall. A fall in employment was recorded in seven of the 12 monitored regions, the highest number since November 2012. The steepest decrease was seen in the North East, where a decline has been recorded in each of the past seven months.

Output Index by region

sa, >50 = growth since previous month, Jan-19 ■ (Dec-18 ■)



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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.

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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