

SCOTLAND Q3 2016 SMALL BUSINESS INDEX

Small business confidence in Scotland has declined further following the vote to leave the European Union. The Scottish Small Business Index stands at -18.8, down from +1.7 in Q3 2015, and from -5.5 the previous quarter – meaning that a significant majority of firms believe that the trading environment will deteriorate. Scottish business confidence continues to track behind the UK average. This is unsurprising, given that the Scottish economy saw zero growth in Q1 2016. Furthermore, for the three months to May 2016, Scotland was the only part of the UK to see a rise in the number of people unemployed compared with the same period a year ago.

Confidence across the small businesses community fell following June's referendum. The UK Small Business Index fell to -2.9 at the latest reading; the lowest figure since the final quarter of 2012. This suggests that growth across the UK economy will slow in the second half of 2016. Conversely, firms report improving on-the-ground conditions, with indicators such as export sales and capacity usage improving.

Unemployment in Scotland fell, despite economic growth stalling over the first quarter of 2016. The latest GDP data from Scotland shows that there was negligible economic growth in the first quarter of 2016. Year-on-year, the Scottish economy expanded by just 0.6% compared with 2.0% across the UK as a whole. That said, the latest labour market figures from the Office for National Statistics show that the rate of unemployment in Scotland between May and July had fallen to 4.7%. The Scottish rate is now below the UK-wide figure of 4.9% and is down from the 6.2% seen in the first quarter of 2016.

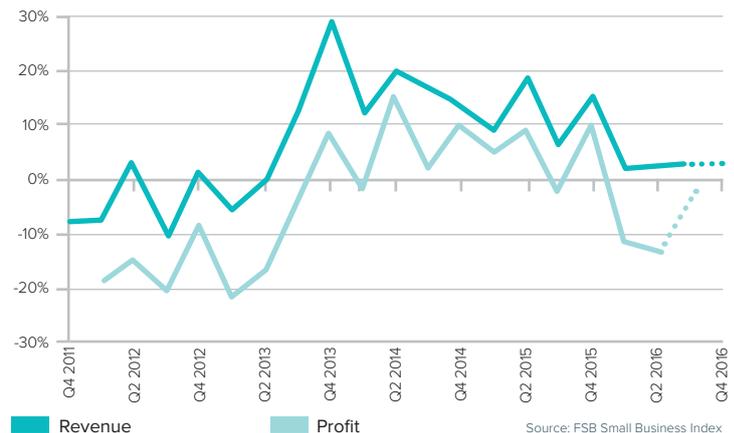
Revenue growth is steady across the smaller business community in Scotland, but business expectations have declined. This quarter, a net balance of 3% of small businesses in Scotland reported revenue growth over the past three months. This is a slight increase from the balance recorded in the first quarter of the year. However, while sales have held up in recent months, expectations for revenue growth over the next three months have fallen compared with the levels expected in previous quarters. In fact, with a net balance of 3% of firms expecting revenues to increase over the next three months, optimism over sales projections stands at its lowest level since early 2013.

Small Business Confidence



Source: FSB Small Business Index.

Net balance of small firms in Scotland reporting revenue/profit growth



Source: FSB Small Business Index.

Scottish small businesses have increased their headcounts.

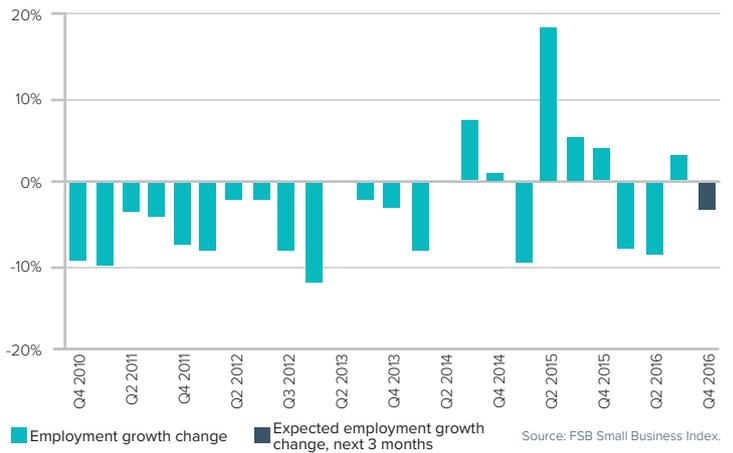
In line with the drop in Scottish unemployment, small businesses have increased staff numbers over the past three months, in contrast to the previous two quarters. However, with decreasing confidence in the market, together with economic and political uncertainty, a net balance of 3% of firms expect to cut back on staff numbers over the next three months. If this trend was replicated across the small business community as whole, it would place renewed pressure on the labour market.

Firms report increasing levels of concern regarding the domestic economy. Almost two thirds (63%) of small businesses report that the performance of the domestic economy is a barrier to growth, a figure much higher than the same time last year.

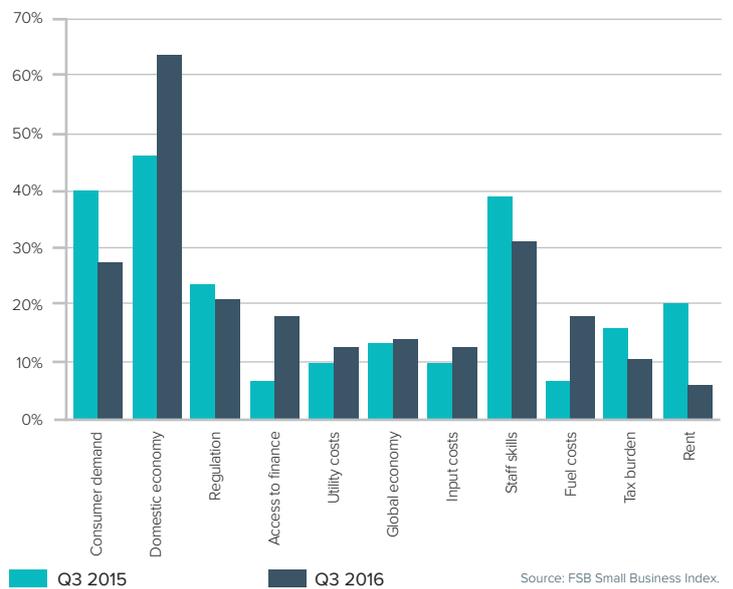
Business investment intentions are on the rise, despite the loss of confidence. A net balance of 24% of respondents expect to increase their capital expenditure over the quarter. After postponing investment decisions in previous quarters, a number of businesses are likely to push ahead with their investment plans. Additionally, improving credit markets are likely to be another supporting factor. The affordability of credit has improved, with 47% of firms reporting that credit is affordable, something that could be further improved by the Bank of England's decisions to cut its base rate to 0.25% at the beginning of August.

Overall, the latest Small Business Index suggests that Scottish small businesses believe that the second half of 2016 could be a challenging period. Whilst a range of indicators suggest that material conditions did not deteriorate substantially in the first half of the year, small business optimism has continued its downward trajectory in the wake of the referendum outcome. Some 47% of small businesses across the country expect conditions to worsen over the next three months, feeding through into less optimistic revenue forecasts. Still, similar to the UK as a whole, the latest figures do show some positive signs. The continued improvements in credit availability and affordability, for example, may be a key factor supporting positive investment expectations over the course of the next 3 months.

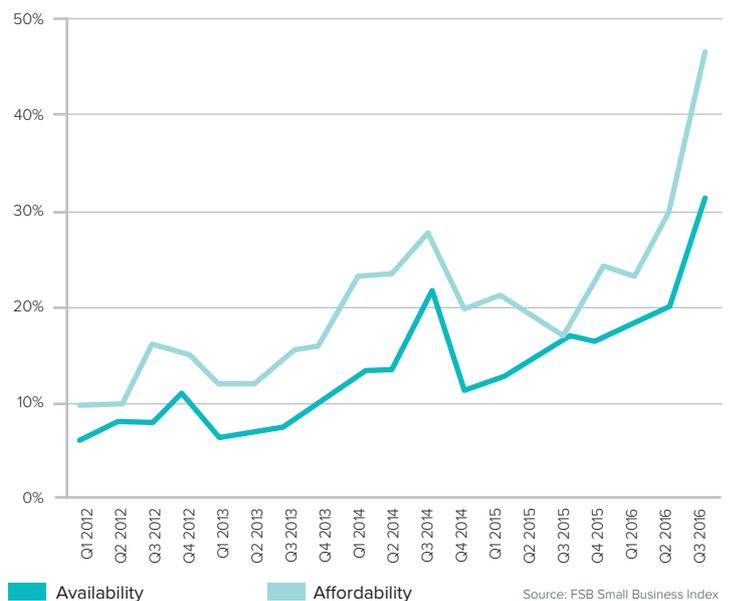
Net balance of firms reporting employment growth, Scotland



Share of firms reporting factor as perceived barrier to growth, Scotland



Share of firms reporting good availability/affordability of credit



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