

SCOTLAND Q1 2018 SMALL BUSINESS INDEX

Scottish small business confidence is improving but the economic outlook remains fragile. In the first quarter of 2018, the Scottish Small Business Index climbed to -17.8 points. However, Scottish small business confidence remains low and lags well behind that of the UK as a whole. This reflects the divergence of economic fortunes seen over the last year. The most recent available data show the Scottish economy is growing at half the pace of the UK as a whole, at just 0.2% quarter-on-quarter.

Scottish small businesses reported further decreases in revenue and profits in the first quarter of the year and continue to face tough market conditions. However, they are more positive about future revenue growth in the coming quarter.

The primary cause of concern was the state of the domestic economy. Consumer demand, a key factor, was also widely cited. Both are more frequently cited than they were a year ago, reflecting the pressure put on household and business budgets by inflation over the period. It seems that these heightened concerns are stifling investment intentions, which also declined at the start of 2018.

Small business confidence across the UK returns to positive territory. The UK-wide Small Business Index climbed from -2.5 points in Q4 2017 to +6.0 points this quarter. Previously, small business confidence had fallen in each quarter since Q2 2017. The UK economy expanded by 0.4% in the fourth quarter of 2017, taking GDP growth over 2017 to 1.7%, only slightly below the 1.9% recorded in 2016.

More Scottish small businesses see sales decline. In the first quarter of 2018, a net balance of 13.5% of Scottish small businesses reported a fall in revenues over the past three months. This is significantly worse than the 6.7% recorded in the third quarter of 2017. More small firms have seen sales fall than have seen them rise in each index reading since the start of 2017.

More positively, the findings suggest that revenues will recover – a net balance of 4.2% of small businesses anticipate that revenues will climb in the coming three months. Still, as consumer spending growth is expected to be weak this year, the outlook for Scottish small businesses remains uncertain.

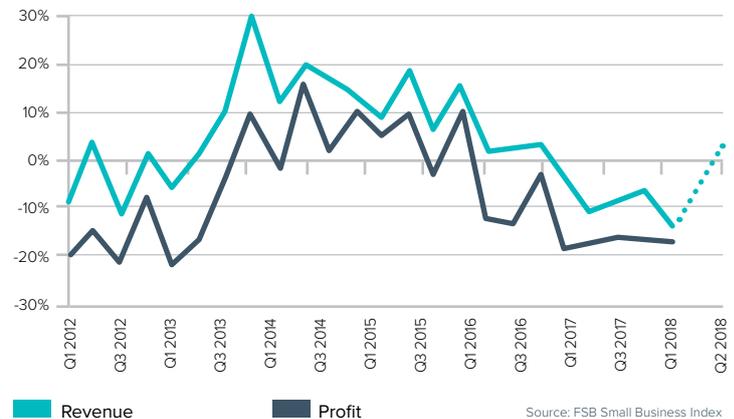
Small businesses report another quarter of reduced headcount. In the first quarter of the year, a net balance of 4.6% of small businesses in Scotland reported reduced employment levels. Although the overall direction remains negative, however, it should be noted that fewer businesses are reducing staff numbers.

This trend looks set to continue with small businesses expecting strong employment growth for the second quarter of the year. This will be welcome news given that figures from the Office for National Statistics (ONS) show the employment rate in Scotland declined by 0.2 percentage points between November 2017 and January 2018.

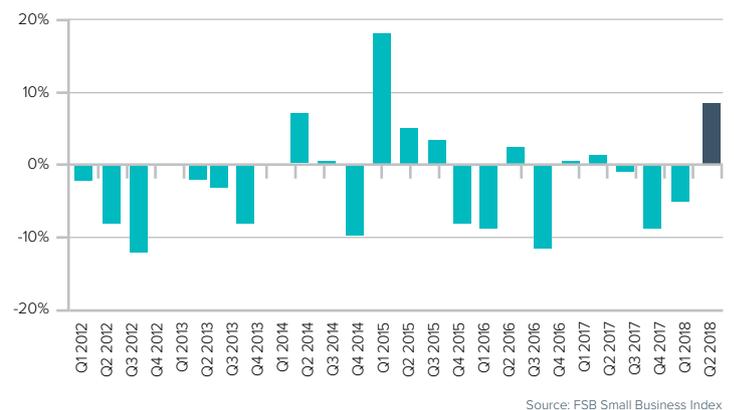
Small Business Confidence



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



Net balance of firms reporting employment growth, Scotland



The state of the domestic economy continues to concern Scotland's small businesses. Over half of Scotland's small firms (55.1%) cited the domestic economy as one of the top three barriers to growth. This figure has increased 2.6 percentage points on that reported in Q4.

With over three fifths of UK output linked to household consumption, it is unsurprising that consumer demand was the next most frequently cited concern. 2017 saw inflation accelerate as sterling's weakness made imports more costly. Real wage growth remains negative, falling 0.3% year-on-year in Q4 2017. Though wage growth is expected to return this year, households will still feel the pinch as they contend with depleted savings and higher interest rates.

Investment intentions are down, but remain positive. The net balance of firms intending to increase investment declined in Q1 2018, having reached a 15-month high in Q4 2017.

Last quarter's findings were supported by recently released GDP statistics which showed that business investment grew 1.1% quarter-on-quarter, having increased by 0.2% between Q2 and Q3.

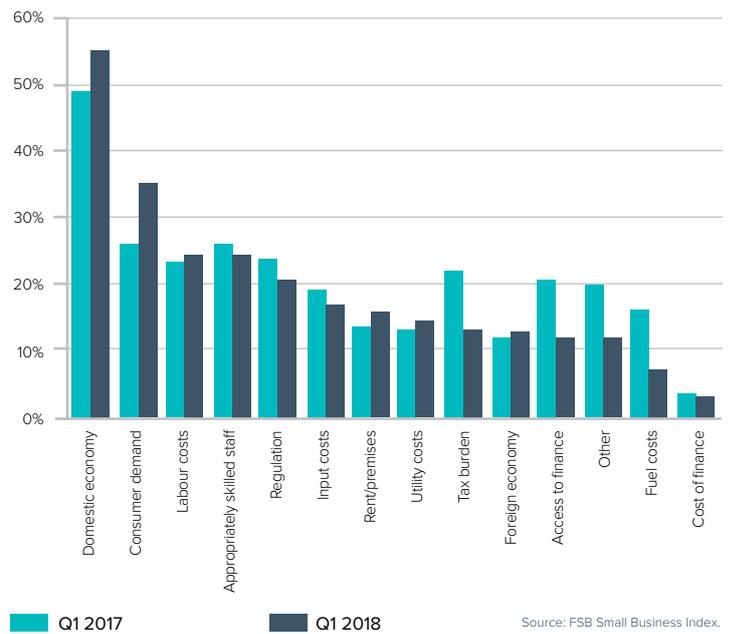
There is potential for business investment to pick up significantly over 2018 and 2019 if the Brexit negotiations deliver further clarity to firms regarding the UK's future economic position.

Small business confidence rebounds in Scotland. In the first quarter of 2018, the Small Business Index moved in the right direction with a rise of 3.6 percentage points. Nevertheless, confidence remains low and the index continues to be well below the average seen last year.

The confidence gap between small businesses in Scotland and the rest of the UK continues to be an issue for the Scottish economy. It is another worrying sign of varying economic performance between Scotland and the UK.

Providing stability and certainty to the small business community in Scotland will be vital if the Scottish Government is to match the greater GDP growth rates seen elsewhere in the UK. This may be a tall order, however, given current political uncertainties, rising costs and likely new regulatory burdens.

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



Net balance of firms with intentions to increase investment spending over next quarter

