

SCOTLAND Q2 2022 SMALL BUSINESS INDEX

The Small Business Index (SBI) in Scotland saw a marked fall in Q2 2022, dropping by 46.1 points to return to negative territory, at a reading of -31.8. The negative score means that the number of Scottish small businesses expecting their performance to improve over the coming quarter is outweighed by the number expecting their performance to worsen. This weakening sentiment came amidst the emergence of several headwinds affecting the UK economy, including significant price pressures for both consumers and businesses.

All UK regions saw a weaker SBI score in Q2 than in Q1. Scotland's fall was the third-largest in magnitude, only being surpassed by the East Midlands and London.

Scotland's SBI in Q2 was the weakest since the -69.0 reading in Q4 2020, when businesses had battled several bouts of Covid-19 containment measures and were facing the prospects of further restrictions.

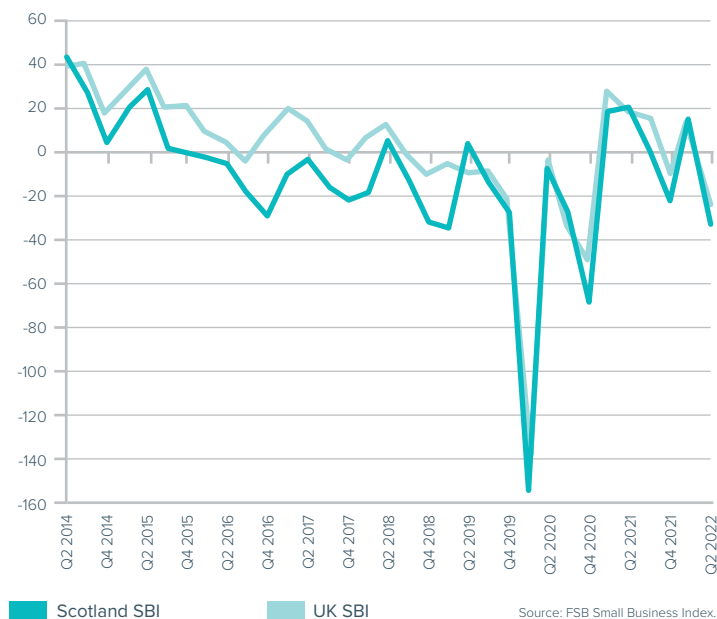
Reflecting the unanimous fall across all regions, the UK-wide SBI also fell in Q2, reaching -24.7. This marked a return to negative territory, having stood at 15.3 in Q1. The weakest reading since Q4 2020, this poor performance reflects the mounting pressures faced by small businesses across the country, as the economy grapples with input shortages, accelerating inflation, and widespread uncertainty.

A net balance of -14.2% of Scottish small businesses saw revenue increase in Q2, relative to Q1. The negative reading means that more respondents saw their revenue fall than increase during the most recent quarter. Scotland's performance on this measure was weaker than the UK-wide average, which stood at -6.0%. Within Scotland's net balance figure, just 27.0% of businesses reported their revenue increasing in Q2, the weakest share of any region.

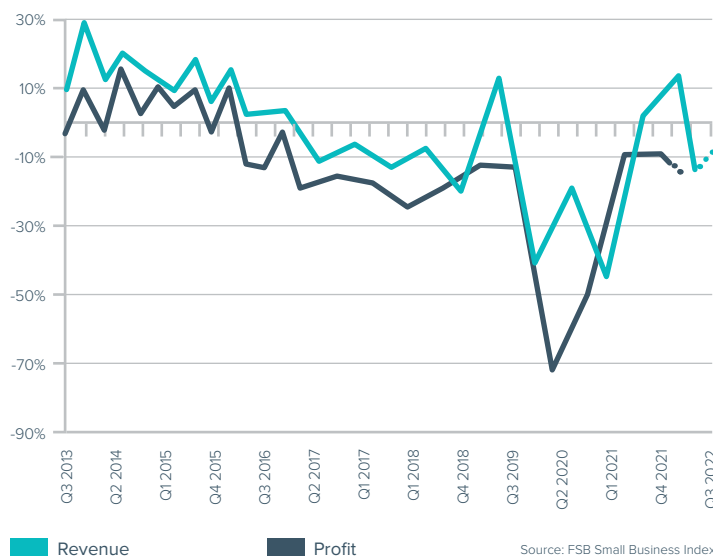
This weaker revenue performance likely reflects the slowdown in activity at the aggregate level, prompted by the headwinds outlined above. April's GDP showed the extent of pressures facing businesses at present, with UK-wide GDP witnessing a monthly fall of 0.2%. Scotland saw a more severe fall of 0.5%, corroborating the weaker revenue performance of Scottish businesses on this round of the SBI. Growth is set to have slowed across the UK as a whole in Q2, while a technical recession remains a risk for the UK economy in 2022.

This weaker outlook has translated into concerns about revenues. A net balance of -8.9% of Scottish small businesses expect revenue to increase in Q3, with the equivalent measure for the UK as a whole standing at -3.4%.

Small Business Confidence



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



A net balance of -4.7% of Scottish small businesses reported increased employee headcount in Q2. The negative net balance means that the number of firms reporting a contraction in their employee numbers outweighed the number of firms reporting an expansion, with this now having been the case for three consecutive quarters. Scotland's negativity was mirrored in the headline UK measure, which slipped below zero for the first time since Q3 2021, with a reading of -3.6%.

The employee headcount experience reported in this edition of the SBI reveals a different trend to that described by aggregate level labour market data. The most recent figures from the ONS, for instance, show that the employment rate in Scotland has increased by 1.0 percentage point on a quarterly basis. This suggests that the employment gains have been concentrated amongst larger businesses. Theoretically, these businesses have been better able to cope with certain economic challenges at present, such as labour shortages, due to economies of scale.

Looking ahead, small businesses are much more optimistic about their employee headcount. A net balance of 9.4% expect their headcount to increase in Q3. This reading is more positive than the UK-wide equivalent of 7.2%.

The share of Scottish small businesses reporting increased costs rose in Q2. 90.5% of small businesses in Scotland stated that their costs had risen in Q2, relative to the same period last year. This share is up even further on the 88.2% seen in Q1, highlighting the widespread extent of price pressures at present. Meanwhile, just 4.1% of small businesses in Scotland reported decreased costs relative to Q2 of last year.

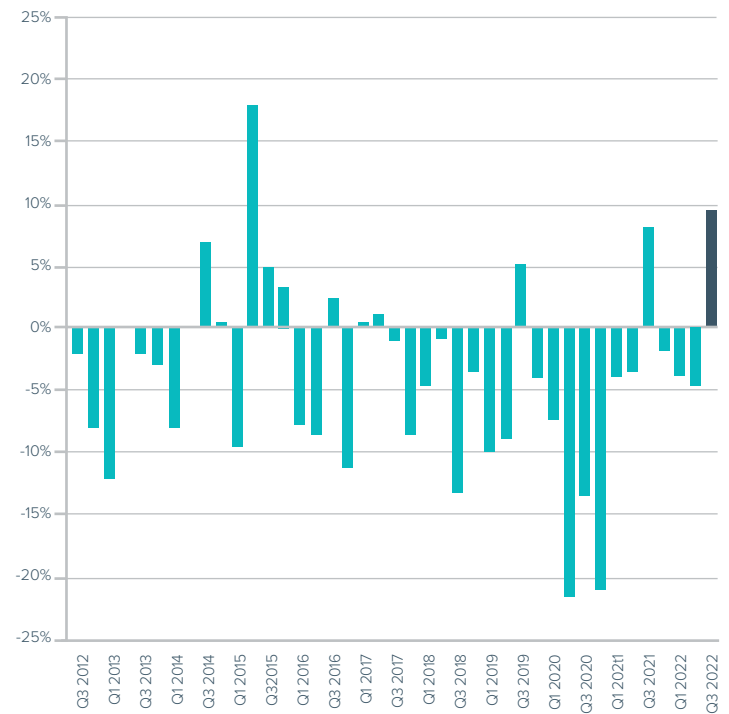
Due to a combination of global economic pressures, including supply chain disruption, input shortages, and geopolitical events, businesses have faced rising prices for some time. These price pressures have accelerated even further recently. The rate of input price inflation for producers reached a series high of 24.0% in June, for instance.

In Scotland, businesses were most likely to cite fuel and utilities as sources of rising prices, with this being the case for 72.9% and 67.1% of respondents, respectively. These categories have been particularly impacted by geopolitical events, specifically the rise in oil prices triggered by Russia's invasion of Ukraine.

There was a stark rise in the share of businesses citing the exchange rate as a source of rising costs. This picked up by 7.8 percentage points on a quarterly basis to reach 15.7% in Q2. Sterling has weakened in recent months, which makes imports more expensive, thus raising costs for businesses who rely on foreign inputs.

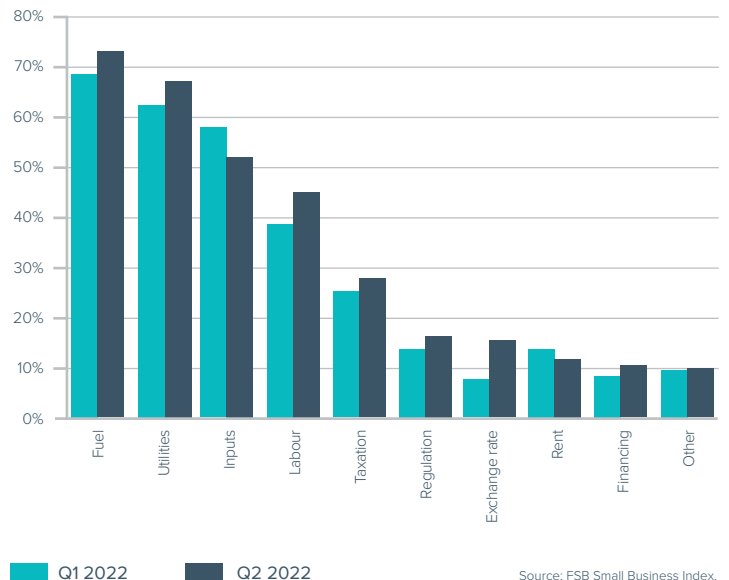
Labour was another category witnessing a large uptick in the share of firms citing this as a main cost pressure. This picked up by 6.4 percentage points on a quarterly basis, reaching 45.0% in Q2. The combination of labour shortages and heightened consumer price inflation has increased wage demands at the aggregate level, serving as additional costs for firms. Scotland has seen particularly stark labour shortages, with candidate availability – a proxy for labour supply – falling at a faster rate than the UK as a whole in recent months.

Net balance of firms reporting employment growth, Scotland



Source: FSB Small Business Index

Share of firms reporting factor as main cause of change in business cost, Scotland



Source: FSB Small Business Index.

FSB Scotland

Tel: 0141 221 0775
scotland.policy@fsb.org.uk
www.fsb.org.uk/scotland

 federationofsmallbusinesses
 @FSB_Scotland