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Survey shows Government needs to work harder to give business a 2005 better than 2004

“Businesses are ever optimistic that they can grow but they are entering 2005 fearing that enforced price increases are going to hit profitability, the message for Government in this election year is – we need economic development to be at the forefront of all policy making.”

The Scottish Chambers of Commerce today released the results of its Quarterly Business Survey for the fourth quarter of 2004, conducted in collaboration with the University of Strathclyde's Fraser of Allander Institute, showing businesses are remaining confident with orders regularly outperforming expectations across most sectors but with costs increasingly hitting profitability.

Commenting on the survey Liz Cameron, Director of Scottish Chambers of Commerce said:

“These results confirm SCC's view that business is feeling a cost squeeze, markets are no easier and no less competitive than last quarter or indeed last year yet the pressure to raise prices is increasing. Every sector is seeing pressures to raise prices, in particular from raw materials and transport. That's why we keep repeating our call to government and to the Chancellor for the urgent need for more consistent and supportive policies, not some of the time all of the time.”

“Looking to the next year the businesses are seeing the consequences of cost pressure as decreasing profitability. Scottish Chambers agree with the Executive that we need to see more of our businesses looking to research and development as core to their business. And we welcome the financial support from the Executive in this area. But when you are in the middle of a triple whammy of enforced rising costs, rising red tape and rising competition it is extremely difficult to put more money into long term R & D when next month is as far as your horizons are able to go.”

“Business needs breathing space and neither the market nor the government are giving it, we only have control over one and we call on the Chancellor to exert that control.”

Liz Cameron continued:

“On a more positive note the survey has highlighted that the tourism sector has again performed very well indeed, with optimism up, total demand up and most importantly we have turnover and profitability both up. Support from the Executive, like the Route Development Fund, have certainly helped and perhaps show that when you involve the private sector we do what works. The survey shows across all sectors the critical role of transport investment and infrastructure. We need to be building a efficient, effective and joined up transport system if Scottish businesses are to grow.”

BUSINESS PERFORMANCE

Summary Points – short term (past and next three months)

- Business confidence rose in construction and tourism but continued to decline in manufacturing, and in wholesale and retail distribution;
- Rising demand was reported by a net of respondents in all sectors except retail, although the outturn was weaker than anticipated in manufacturing, and retail distribution;
- Manufacturing respondents reported a slight easing in the volume of work in progress and some increase in stocks. Over 50% reported working below optimum levels. In contrast, construction firms reported rising trends in work in progress, and expect these to strengthen over the first half of 2005;
- In the service sector wholesale and smaller retail firms anticipate declining trends in sales, whilst larger firms expect modestly rising sales trends. Tourism respondents reported good fourth quarter results, but, as in previous years, expect a dip in visitor numbers in the first quarter;
- Price pressures strengthened in manufacturing in the fourth quarter and remain high in both wholesale and retail distribution;
- Concerns as to the levels of orders/sales and competition remain high in all sectors, being cited by 52% of manufacturers, 62% of construction and 47% of tourist respondents;
- Pay increases in the fourth quarter ranged from 3.2% in wholesale to 6.0% in tourism. Difficulties in the recruitment of skilled staffs were again especially evident in construction and tourism.

Expectations for the next twelve months

- Manufacturing respondents anticipate rising trends in orders, turnover and profitability over the next twelve months. Construction respondents expect strongly rising turnover and profitability, but in both sectors pressures on margins look to be more evident in 2005 than in 2004;
- Retail respondents again expect modestly rising turnover but declining profitability over the next year, suggesting further pressures on margins.

Strathclyde University's Fraser of Allander Institute in collaboration with the Scottish Chambers' of Commerce conducts the quarterly Chambers' Business Survey. In the present survey, which was conducted in mid December to early January, over 350 firms responded to the questionnaire.

Methodology

The Scottish Chambers' Business survey, in common with most national surveys, seeks evidence as to changing trends, and uses net balances as the key survey statistic. Most questions ask the respondent to indicate whether the trend, over the past three months, and expected for the next three months, is either 'up', 'level' or 'down'. The net balance for such survey questions is defined as the number of 'up' responses minus the number of 'down' responses to each survey question. Hence a positive net balance indicates a rising trend, and a negative net balance a declining trend. Net balances for the current quarter, together with those for the previous quarter and the quarter a year ago have been added to the usual results.

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MANUFACTURING

Optimism

The overall decline in business confidence eased, notwithstanding a weaker than anticipated outturn in orders and sales. Business confidence rose slightly for exporters who reported stronger trends in orders than non-exporters.

Orders and Sales

The trend in orders eased in the fourth quarter, although once again respondents remain optimistic as to rising trends in the first quarter. Expectations for the next twelve months are slightly stronger than three months ago.

The rising trend in the level of work in progress ended and the current decline is expected to continue with some increase in stocks of raw materials and finished goods. A slightly higher proportion (53%) reported operating at below optimum levels than in quarter three (50%).

Finance

The downward trend in cashflow continued and deepened but firms have again upgraded their expectations as to the trends in turnover and profitability over the next year. However, there are some signs of pressures on profit margins.

Price pressures increased and concerns as to raw material costs, other overheads, transport costs and pay costs all rose in the fourth quarter.

Investment

31% reported revising investment plans for 2005. Investment in the current quarter was again mainly directed towards increasing efficiency and for the replacement of equipment. Investment for R & D and to develop new markets/products remained low.

Employment

Employment eased slightly, 47% sought to recruit staff and 21% reported problems in recruiting skilled manual staffs.

	Q4 2004			Net Balances		
	Up	Level	Down	Q4/04	Q3/04	Q4/03
Business Optimism	21.7	53.8	24.6	-3	-15	5
Trends in actual orders						
Total new orders	29.8	47.1	23.1	7	10	11
Scottish orders	16.9	57.0	26.1	-9	1	-12
Rest of UK orders	20.5	59.2	20.3	0	2	2
Export orders [38.5% = N/A]	18.5	21.7	21.3	-3	2	12
Trends in expected orders						
Total new orders	28.9	56.7	14.4	14	12	7

Scottish orders	15.2	67.1	17.7	-2	2	-9
Rest of UK orders	19.2	71.6	9.2	10	2	0
Export orders [40.5 = N/A]	18.5	29.3	11.6	7	7	7
Av Capacity used	78.1			78.1	75.3	79
Invest in plant/equip.	20.0	58.8	21.3	-1	0	3
Cash flow past 3 mths	17.7	48.4	33.9	-16	-13	-22
Turnover next 12 mths	44.2	41.3	14.6	30	19	-13
Profitability next 12 mths	37.4	33.8	28.7	9	8	33
Price change next 3 mths	41.0	53.7	5.3	36	23	14
Pressures to raise prices from						
Pay settlements	32.2			32	14	34
Raw material costs	71.4			71	54	53
Finance costs	11.3			11	10	11
Other overheads	41.2			41	39	34
Transport costs	49.5			50	37	25
Employment trends						
Total actual employment	15.1	66.5	18.5	-3	11	-4
Total expected next 3 months	13.6	72.0	14.4	-1	4	0
Average pay increase	4.5			4.5	4.08	3.9

CONSTRUCTION

Optimism

The rate of increase in business confidence eased in the fourth quarter, notwithstanding rising, and better than anticipated trends, in the fourth quarter, and rising trends in the level of work in progress.

Contracts

The rising trends in the value of new contracts continued, driven by both public and private sector work. Some easing in the level of domestic build work contracts is expected in the first quarter, although respondents anticipate this will be offset by rising trends in public sector work. Firms continue to report rising trends in the level of work in progress and 40% expect the level of work in progress to rise over the next six months.

76% reported operating at or above optimum rates in the fourth quarter.

Respondents expect continuing pressures on tender margins through 2005, and over three quarters expect building and other costs to rise in 2005. Nevertheless, both turnover and profitability is expected to strengthen over the next twelve months.

The level of new contracts, shortages of skilled labour and to a lesser extent availability of contractors and business capacity were seen as the four factors most likely to restrict activity.

Investment

Rising trends in investment and leasing were reported, and once again investment in the fourth quarter was mainly for the replacement of equipment.

Employment

A rising trend in employment was reported. 56% sought to recruit staff and 17% reported increasing pay by an average of 3.8% [5.7% and 4.88% in the previous two quarters].

	Q4 2004			Net Balances		
	Up	Level	Down	Q4/04	Q3/04	Q4/03
Business Optimism	26.7	57.1	16.7	10	25	32
Trends in actual orders						
Total new orders	42.9	42.9	14.3	29	9	15
Public sector orders	28.6	46.4	25.0	4	-9	0
Private commercial	22.6	58.1	19.4	3	-11	-6
Domestic/house build	30.3	45.5	24.2	6	17	-7
Trends in expected orders						
Total new orders	25.6	59.0	15.4	10	-8	17
Public sector orders	34.6	46.2	19.2	15	-9	-4
Private commercial	14.3	75.0	10.7	4	-14	10
Domestic/house build	16.7	60.0	23.3	-7	-3	7
Trends in work in progress						
Actual	28.6	54.8	16.7	12	14	18
Expected	40.0	45.0	15.0	25	11	15
Capacity used	86.8			86.8	89.4	85
Invest in plant/equip.	16.7	71.4	11.9	5	5	18
Leasing in plant/equipt.	21.6	70.3	8.1	14	-6	-3
Employment trends						
Total actual employment	29.3	53.7	17.1	12	0	13
Total expected next 3 months	21.1	65.8	13.2	8	19	14
Average pay increase	3.8			3.8	5.7	4.4
Percent recruiting staff	56.1			56	64	55
Recruitment difficulties inc.	24.1			24	9	14

WHOLESALE DISTRIBUTION

Optimism

Business confidence fell in the fourth quarter, notwithstanding better than anticipated sales.

Sales

A rising trend in sales was reported, but an easing in sales is forecast for the current quarter.

Once again the level of competition, along with business rates were seen as the factors most likely to restrict sales over the first quarter.

Expectations of price increases again strengthened, and remain at their highest for more than five years, and concerns as to price pressures may underpin the expectations of declining profitability over 2005.

Transport and raw material costs were the most widely cited pressure on prices, being cited by over 60% of respondents.

Investment

27% reported rising trends in investment intentions, although the majority reported no change.

Finance

A rising trend in cashflow was reported, expectations as to trends in turnover and profitability over the next twelve months weakened further.

Employment

Rising trends in employment were reported as 41% sought to recruit staff. 36% increased pay by an average of 3.2% (compared to 4.15% and 3.19% in the previous two quarters).

	Q4 2004			Net Balances		
	Up	Level	Down	Q4/04	Q3/04	Q4/03
Business Optimism	5.9	64.7	29.4	-24	3	14
Trend in actual sales	38.2	32.4	29.4	9	0	-9
Trend in expected sales	18.5	51.9	29.6	-11	0	-6
Investment plans	27.3	57.6	15.2	12	-3	21
Cash flow past 3 months	18.2	75.8	6.1	12	-6	-17
Turnover next 12 months	29.4	50.0	20.6	9	19	31
Profitability next 12 months	26.7	33.3	40.0	-13	-10	11
Price change next 3 Months	61.8	35.3	2.9	59	58	34

Pressures to raise prices from						
Pay settlements	17.6			18	32	40
Raw material costs	61.8			62	48	34
Finance costs	5.9			6	26	23
Other overheads	29.4			29	32	43
Transport costs	64.7			65	71	46
Employment trends						
Total actual employment	12.5	71.9	15.6	-3	10	12
Expected next 3 months	7.4	88.9	3.7	4	-7	6
Average pay increase	3.2			3.2	4.5	4.1
Percent recruiting staff	41.2			41	42	35
Recruitment difficulties	62.5			62.5	35	67

RETAIL DISTRIBUTION

Optimism

Changes in business confidence were less widely based, and reported by a third of respondents. The declining trends in confidence continued and deepened, as sales trends were weaker than anticipated. Declining confidence was evident for both small and larger retailers.

Sales

Declining trends in sales were reported, and a further decline is forecast for the first quarter. Retailers employing more than 50 staff reported rising sales, whilst a net of those employing less than 50 reported and anticipate declining sales trends.

Competition, business and interest rates were seen as the three factors most likely to inhibit sales over the first quarter.

Investment

The downward trend in investment intentions continued in the fourth quarter.

Finance

The rising cashflow trends continued, although rising trends were only evident amongst larger firms.

Overall, respondents are again less optimistic as to profitability and turnover trends over the next twelve months. Larger firms anticipate rising trends in turnover and profitability, whereas a net of smaller firms anticipate level trends in turnover and declining profitability.

Cost pressures continued at a high level, with both smaller and larger firms being concerned as to the level of transport costs and to the implications of rising interest rates.

Price pressures remain high, but are most strongly anticipated by smaller firms.

Employment

A slight decline was reported and this is expected to continue through the first quarter. 34% recruited staff, and 32% increased pay by an average of 4.2%.

	Q4 2004			Net Balances		
	Up	Level	Down	Q4/04	Q3/04	Q4/03
Business Optimism	8.0	66.7	25.3	-17	-11	-25
Trend in actual sales	28.8	34.2	37.0	-8	12	-12
Trend in expected sales	12.3	58.9	28.8	-16	0	-19
Investment plans	10.7	72.0	17.3	-7	-10	8
Cash flow past 3 months	18.7	65.3	16.0	3	6	-7
Turnover next 12 months	28.0	52.0	20.0	8	14	-6
Profitability next 12 months	28.2	36.6	35.2	-7	-5	-10
Price change next 3 months	40.0	56.0	4.0	36	42	42
Pressures to raise prices from						
Pay settlements	30.7			31	24	28
Raw material costs	18.7			19	24	28
Finance costs	22.7			23	26	23
Other overheads	45.3			45	39	58
Transport costs	41.3			41	46	39
Employment trends						
Total actual employment	9.6	78.1	12.3	-3	1	0
Expected next 3 months	6.9	84.7	8.3	-1	3	-14
Average pay increase	4.2			4	3.6	4.3
Percent recruiting staff	33.8			34	38	40
Recruitment difficulties	37.1			37	41	48

TOURISM

Optimism

A rising trend in business confidence was reported, the strongest fourth quarter level for over 8 years.

Demand

For a further quarter rising trends in demand were reported for Scottish and rest of UK Visitors, and the trends from all areas were better than anticipated.

Overall 26% of business was local trade [17%, 22% and 31% in previous quarters], 39% tourist trade [58%, 51% and 46% in the previous two quarters] and 35% business trade [24%, 31% and 33% in the previous quarters].

Finance

Strongly rising trends in turnover and more modest increases in profitability were again reported. A level trend in room rates was reported, and, as in previous years some discounting of rates is expected in the first quarter.

Concerns as to the lack of demand were little different from previous fourth quarters.

Employment

Changes in employment were at the margin, affecting 28% of respondents, and the decrease was slightly stronger than had been anticipated.

Recruitment

65% sought to recruit staff, and 38% reported difficulties in recruiting staff had increased, overall 77% of those recruiting reported difficulties in recruiting suitable staffs. 67% increased pay by an average of 6.0% [4.95% and 4.91% in the previous quarters].

	Q4 2004			Net Balances		
	Up	Level	Down	Q4/04	Q3/04	Q4/03
Business Optimism	31.0	53.4	15.5	16	0	0
Trends in demand/visitors						
Total demand/visitors	38.6	33.3	28.1	10	39	-2
Demand from Scotland	26.9	53.8	19.2	8	16	19
Demand from Rest of UK	24.1	53.7	22.2	2	28	4
Demand from abroad	19.6	47.1	33.3	-14	16	-42
Business Trade	30.2	49.1	20.8	9	13	-34
Trends in expected demand						
Total demand/visitors	21.2	46.2	32.7	-12	-9	-14
Demand from Scotland	10.2	65.3	24.5	-14	-10	-4
Demand from Rest of UK	18.4	53.1	28.6	-10	-12	-7
Demand from abroad	14.6	47.9	37.5	-23	-29	-40
Business Trade	20.4	57.1	22.4	-2	-13	-24
Capacity used	55.5			56	74	42
Investment						
Turnover past 3 months	52.9	32.4	14.7	38	47	0
Profitability past 3 months	38.7	29.0	32.3	25		na
Average daily rate	24.6	50.9	24.6	0	2	-20
Expected average daily rate	26.4	45.3	28.3	-2	-24	3
Employment trends						
Total actual employment	7.5	71.7	20.8	-13	-6	-12
Expected next 3 months	5.9	70.6	23.5	-18	-10	-24
Average pay increase	6.0			6.0	4.95	4.8
Percent recruiting staff	69.7			70	65	56
Recruitment difficulties	76.9			77	73	81