

SCOTLAND Q1 2017 SMALL BUSINESS INDEX

Scottish small business confidence improved slightly this quarter.

The Scottish Small Business Index stands at -9.6 points for Q1, up from the six-year low of -28.9 points recorded at the end of 2016. Although the Index remains in negative territory, it rose for the first time in eighteen months. Small businesses in Scotland are amongst the least confident in the UK, with four in ten anticipating their overall business performance will deteriorate over the course of the next quarter.

Despite the weak pound, Scottish smaller businesses expect only a marginal improvement in export performance. Developments in the domestic economy remain a main threat to the business outlook. Moreover, around one quarter highlighted that skill shortages are an obstacle to future growth.

Official data from the Office for National Statistics (ONS) showed that Scotland's unemployment rate stood at 4.7% in the three months to January 2017, down 0.6% from the previous quarter, which matches the figure for the UK. Over the same period, employment levels increased by 0.4% to 73.7% – an increase of 16,000 jobs in Scotland.

Latest GDP data signalled that the onshore Scottish economy contracted by 0.2% in the fourth quarter of 2016, while the UK saw growth of 0.7%. This contraction was largely driven by declining output in the manufacturing and construction sectors and the lack of growth in the services sector. Looking ahead, the Fraser of Allander Institute forecast growth of 1.2% in 2017.

UK small business confidence improves further. The UK-wide Small Business Index continued to recover from the decline in Q3 2016 and rose from +8.5 points at the end of last year to +20 points this quarter – its highest level since Q4 2015. The index is now 11.4 points higher than a year ago, suggesting that the UK economy remains in good shape at the beginning of 2017. However, rising inflation paired with subdued wage growth will lead to lower household incomes, which could result in a slowdown in consumer spending and therefore hinder economic growth.

Scottish exports suffer a large drop despite weak pound. This quarter, the net balance of small Scottish businesses reporting higher exports compared to the prior quarter stands at -10.2%, highlighting that businesses' export performance on average deteriorated over the past three months. The data highlights that 17% saw a significant decline in the value of their exports compared to the prior quarter. Furthermore, firms anticipate marginal export growth over the second quarter.

Revenues decline at strongest rate for four years. Scottish smaller businesses' revenues declined during the opening quarter of 2017, with 43.2% reporting a fall. The resulting net balance of -11% is the poorest result in four years. Rising input costs – such as the cost of fuel and energy – are likely to have been partly responsible for this fall. Looking ahead, a third of firms anticipate a decline in revenues during the next quarter, while 37% project an increase.

Small Business Confidence



Source: FSB Small Business Index.

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



Source: FSB Small Business Index.

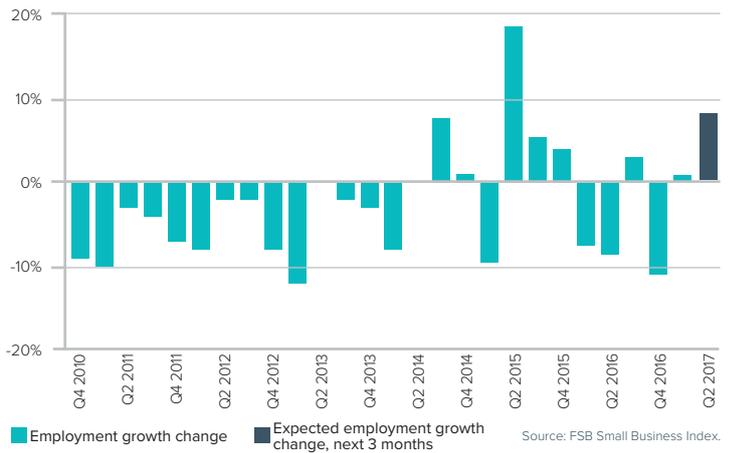
A very slight increase in firms reporting increased headcounts. A net balance of +0.3% of small businesses added to their workforce during the first quarter of 2017. Although a marginal increase, the jobs growth in the latest three month period contrasted with a substantial decline in the previous quarter, when 22.2% of small employers reported a shrinking workforce. That said, the overall subdued hiring picture points to a fragile labour market. Although a net balance of +7.8% of firms project employment growth over the second quarter, this compares with the corresponding UK figure of +11.3%.

Growth aspirations improve, but domestic economy perceived to be major threat to growth. Small businesses in Scotland anticipate turnover and sales to grow over the next year. While the net balance with positive growth aspirations has risen from +13.3% at the end of last year to +23.9% this quarter, this remains well below the overall UK average of +43.8%. In line with sluggish GDP figures, the domestic economy remains a significant problem, with almost half (49.2%) of all respondents identifying it as a barrier to growth. However, that is down from the figure of 57.7% in Q1 2016. Firms also identify consumer demand and the availability of skilled staff as problems for their operations. Over the last year, we've seen a large jump in the proportion of businesses highlighting the pressure from rising overheads. Fuel costs were mentioned by 16.2% (up from 1.5% in Q1 2016) while 19.2% (up from 7.2% in Q1 2016) made reference to input costs.

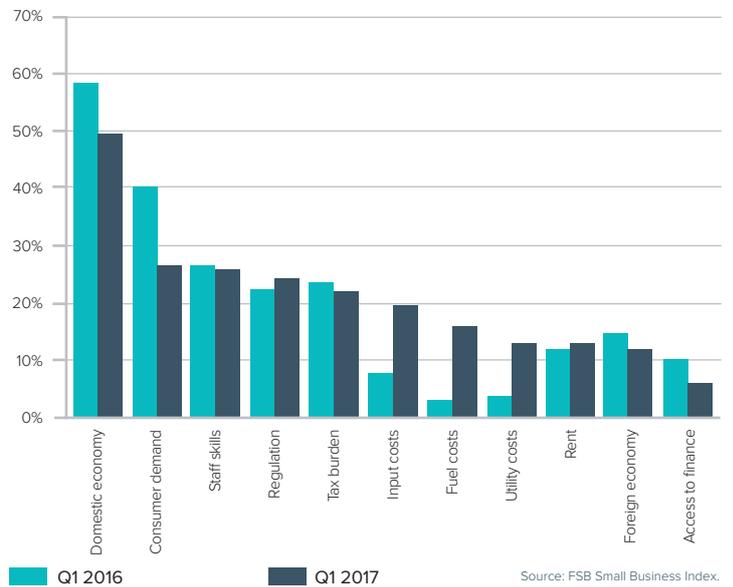
Investment intentions still positive despite overall fall in confidence. The net balance of small businesses expecting their capital expenditure to rise over the next three months has fallen from +19.2% in Q1 2016 to +13.2% this quarter. Weaker expectations regarding capital investment are accompanied by some signs of issues around business finance. The proportion of Scottish firms rating the availability of new credit as poor stands at 37.7% this quarter. This is down from 40% during the same quarter last year and broadly in line with the overall UK average of 36.4%. However, some small businesses still struggle to secure credit, with more than one-in-four companies highlighting unsuccessful applications.

The Small Business Index highlights ongoing challenges despite a slight improvement in confidence. Although it is encouraging that Scotland's SBI has improved since the previous quarter, the Index remains in negative territory for the seventh consecutive quarter – the lowest reading since the survey was introduced in 2010. Small businesses are concerned about the domestic economy and are increasingly feeling the impact of higher fuel and input costs. This data suggest Scottish economic growth will remain below trend in the immediate future.

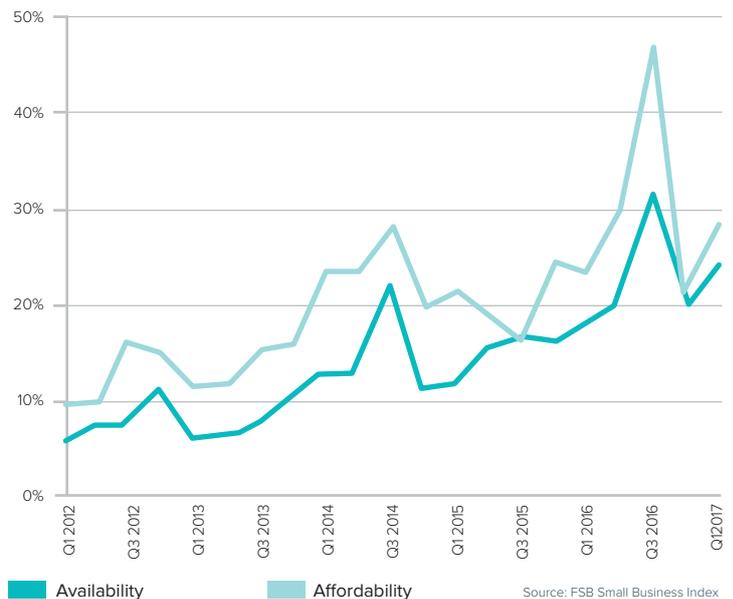
Net balance of firms reporting employment growth, Scotland



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



Share of firms reporting good availability/affordability of credit



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