

This is the Bank of Scotland PMI report. Compiled by Markit for Bank of Scotland, the report is based on data compiled from monthly replies to questionnaires sent to purchasing executives in around 600 private manufacturing and service sector companies. The panel has been carefully selected to accurately replicate the true structure of the Scottish economy.

NOT FOR BROADCAST OR PUBLICATION BEFORE 00:01, MONDAY 14 June 2010

BANK OF SCOTLAND PMI: SCOTTISH PRIVATE SECTOR ACTIVITY GROWTH GAINED MOMENTUM IN MAY

- Overall output growth the fastest in three months
- Fastest rate of job creation since October 2009
- Sharp rise in average input costs, with pace of inflation again faster than the wider UK economy

Latest data signalled that the recovery of the Scottish private sector economy gathered pace in May, following volcano-related disruptions to business operations in the previous month. The headline Bank of Scotland PMI – a seasonally adjusted index monitoring activity across Scotland's manufacturing and service sectors – rose to 53.1 in May, from 51.6 in April, pointing to a rise in private sector activity that was the fastest in three months.

The divergence between manufacturing and service sector performance moderated in May, with both output and new business in the service sector increasing for the first time since February. As a result, overall new business growth accelerated since April.

The latest rise in private sector activity extended the current period of expansion to eleven months. Anecdotal evidence suggested that output growth reflected higher intakes of new business, which rose modestly in May. Greater market demand and, in some cases, new product developments were cited by panellists as having supported total new business growth.

Private sector employment in Scotland rose for the fourth successive month in May. Although only modest, the rate at which companies added to their staff numbers was the fastest in seven months. Panellists reported that greater inflows of new business and company expansion plans had led to the latest rise in headcounts.

Despite further gains in new business, a moderate degree of spare capacity existed in the Scottish private sector during May, with backlogs falling for the thirty-third month running. The latest decline was broad-based across both services and manufacturing.

According to the latest data, average input costs continued to rise sharply in May, with the rate of inflation broadly unchanged since April. Higher prices paid for fuel and increased labour-related costs were the primary drivers of inflation.

Output prices set by private sector firms rose for the fourth consecutive month in May, increasing at a moderate rate that was the fastest since October 2008. Nevertheless, companies continued to find it difficult to pass on higher input costs to clients, with the overall rate of charge inflation relatively mild in comparison.

Donald MacRae, Chief Economist at Bank of Scotland, said: "Output growth is showing a welcome recovery, the fastest we have seen in the last three months. After a worrying two-month period of decline, service sector activity has returned to growth in May, reporting a promising rise in new business for the first time in three months. However the sharp rise in average input costs during May is of concern, with the pace of inflation again faster than that seen in the wider UK economy. The Scottish economy is slowly emerging from recession, although at a lower pace than the UK as a whole."

Bank of Scotland plc is registered in Scotland no. SC327000. Registered office: The Mound, Edinburgh EH1 1YZ.

Authorised and regulated by the Financial Services Authority.

As part of Lloyds Banking Group, Bank of Scotland is proud to be an Official Partner of the London 2012 Olympic Games and Paralympic Games.



Component Summary

Business Activity:

The Business Activity Index remained above the neutral 50.0 threshold in May, pointing to a further expansion of private sector output in Scotland. The rate of growth was moderate overall, but the fastest in three months. Service sector activity returned to growth in May, following a two-month period of decline, but the expansion was slower than that observed in manufacturing. Anecdotal evidence suggested that activity growth primarily reflected greater inflows of new business. Some panellists also mentioned higher client confidence.

New Business:

The level of new business received by Scottish private sector companies rose again in May, extending the current period of growth to four months. The pace of expansion was only modest, but faster than in the preceding month. Underlying the rise in overall new business volumes was a solid increase in manufacturing new orders, while the expansion in services was only slight. Where a rise in new work was signalled, respondents often linked this to greater client demand. There were also reports of new product development and the success of promotional activities.

Employment:

Data indicated that private sector employment in Scotland rose for the fourth month running in May, led by further job creation in the manufacturing sector. Although only modest, the rate at which firms added to their staff numbers was the fastest since October last year. In contrast to the previous month, the rate of employment growth was sharper than that seen across the UK as a whole. Those respondents that reported a rise in staffing levels linked this to greater market demand and, in some cases, company expansion plans.

Backlogs:

According to the latest data, outstanding business in the Scottish private sector fell for the thirty-third consecutive month in May. Nonetheless, the pace of depletion eased to the slowest since last November. Backlogs fell at broadly similar rates in both services and manufacturing. For the sixth month in succession, the overall decline in unfinished business was faster than in the UK economy as a whole. Survey participants reported that they had sufficient resources to deal with both forms of workloads, despite a further rise in new business.

Input prices:

Average input costs rose sharply in May, with the pace of inflation again faster than that seen in the wider UK economy. By sector, the average cost of manufacturers' purchases rose at a much faster rate than cost burdens faced by service providers. Evidence provided by the survey panel suggested that inflation reflected a combination of higher personnel and fuel costs. Some firms also mentioned exchange rate variations.

Output prices:

Output prices set by Scottish private sector firms rose in May. The rate at which companies raised their charges was moderate, and accelerated to the fastest since October 2008. Output price inflation, which has now been signalled for four successive months, primarily reflected higher prices paid for a range of raw materials. However, some firms reported that they were unable to pass on the full extent of cost rises due to high competition. The overall rise in input costs centred on the manufacturing sector, with only a fractional rise registered in services.

The Bank of Scotland PMI is compiled by Markit for Bank of Scotland and is based on data compiled from monthly replies to questionnaires sent to purchasing executives in around 600 private manufacturing and service sector companies. The panel has been carefully selected to accurately replicate the true structure of the Scottish economy.

Survey responses reflect the change, if any, in the current month compared to the previous month based on data collected mid-month. For each of the indicators the 'Report' shows the percentage reporting each response, the net difference between the number of higher/better responses and lower/worse responses, and the 'diffusion' index. This index is the sum of the positive responses plus a half of those responding 'the same'.

Diffusion indexes have the properties of leading indicators and are convenient summary measures showing the prevailing direction of change. An index reading above 50 indicates an overall increase in that variable, below 50 an overall decrease.

The Purchasing Managers' Index (PMI) survey methodology has developed an outstanding reputation for providing the most up-to-date possible indication of what is really happening in the private sector economy by tracking variables such as sales, employment, inventories and prices. The indices are widely used by businesses, governments and economic analysts in financial institutions to help better understand business conditions and guide corporate and investment strategy. In particular, central banks in many countries use the data to help make interest rate decisions. PMI surveys are the first indicators of economic conditions published each month and are therefore available well ahead of comparable data produced by government bodies.

Markit do not revise underlying survey data after first publication, but seasonal adjustment factors may be revised from time to time as appropriate which will affect the seasonally adjusted data series. Historical data relating to the underlying (unadjusted) numbers, first published seasonally adjusted series and subsequently revised data are available to subscribers from Markit. Please contact economics@markit.com.

About Bank of Scotland

Bank of Scotland is part of Lloyds Banking Group, the UK's largest retail bank and Scotland's largest financial services employer. Established in 1695, Bank of Scotland is the UK's oldest surviving clearing bank. Our goal is to be the best financial services provider in Scotland. We believe this means we must build a leadership position not on the basis of scale but on the foundations of reputation and recommendation.

About Markit

Markit is a leading global financial information services company with over 1,400 employees. The company provides independent data, valuations and trade processing across all asset classes in order to enhance transparency, reduce risk and improve operational efficiency. Its client base includes the most significant institutional participants in the financial market place. For more information, see www.markit.com.

About PMIs

Now available for 26 countries and key regions including the Eurozone and BRIC, Purchasing Managers' Indexes (PMIs) have become the most closely-watched business surveys in the world, favoured by central banks, financial markets and business decision makers for their ability to provide up-to-date, accurate and often unique monthly indicators of economic trends.

For further information, contact:

Zoe Redhead, Bank of Scotland Press Office
Tel: 0131 243 7005 / 07809 551491
Web: www.lloydsbankinggroup.com/media.asp

For technical enquiries, contact

Andrew Self, Markit economist
Tel: 01491 461 006
Email: andrew.self@markit.com

The intellectual property rights to the Bank of Scotland PMI provided herein is owned by Markit Group Limited. Any unauthorised use, including but not limited to copying, distributing, transmitting or otherwise of any data appearing is not permitted without Markit's prior consent. Markit shall not have any liability, duty or obligation for or relating to the content or information ("data") contained herein, any errors, inaccuracies, omissions or delays in the data, or for any actions taken in reliance thereon. In no event shall Markit be liable for any special, incidental, or consequential damages, arising out of the use of the data. Markit, PMI and Purchasing Managers' Index are all trademarks owned by The Markit Group.