

Compiled by Markit for Bank of Scotland, this 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 is carefully selected to accurately replicate the true structure of the Scottish economy.

NOT FOR BROADCAST OR PUBLICATION BEFORE 00:01, MONDAY 11 OCTOBER 2010

## BANK OF SCOTLAND PMI: PRIVATE SECTOR ACTIVITY DOWN FOR FIRST TIME IN FIFTEEN MONTHS

- Output fell in manufacturing and service sectors, following four months of growth
- New business levels rose for the eighth month in succession
- Job creation continues at a stronger rate than at the UK-wide level

The recovery in the Scottish private sector paused in September, as activity across the economy fell for the first time since June of last year. Nonetheless, at 49.8, from 53.0, the headline Bank of Scotland PMI posted a reading only fractionally below the 50.0 mark that separates rising from falling activity. Elsewhere, the survey pointed to continued recovery with new orders and employment both rising.

Activity levels at both manufacturing and service sector firms fell during September. This ended a four-month run in which both sectors had posted growth. The declines contrasted with the trend seen across the UK as a whole, where continued expansion was registered. In Scotland, panellists linked the fall to weakening new order values and lower activity at clients.

Meanwhile, the volume of new business received by private sector companies rose for the eighth straight month. However, a mild acceleration of growth in services new orders masked a fall in new business received by manufacturing firms (the first in the sector since January).

Despite recording the first fall in activity in fifteen months, panel members continued to raise headcounts in September. Although the latest rise was only fractional, it was the ninth increase in the past year, and at a stronger rate than that seen at the UK-wide level. Anecdotal evidence indicated that this may in part have reflected higher demand for temporary workers.

Latest data indicated that Scottish firms continued to deplete backlogs of work during September, extending the current sequence to thirty-seven months.

Higher raw material, wage and wholesale food costs were all reported to have contributed to another monthly rise in average input prices during September. Nevertheless, latest data highlighted a moderation in cost inflation to a nine-month low. In response to higher input prices, Scottish firms raised their average charges during September, as has been the case in seven of the past eight months. Nonetheless, the overall pace of output price inflation was only slight and considerably below that seen for average costs.

**Donald MacRae, Chief Economist at Bank of Scotland, said:** "The Scottish private sector economy has paused for breath after a slow but steady period of growth. While new orders and employee numbers remain on an upward trajectory, overall activity decreased during September.

"Scotland's manufacturing and service sectors, both critical to the economic recovery, were broadly flat last month. Rising raw material costs continue to increase pressure on businesses, however we are observing a moderation in cost inflation."

## **Component Summary**

### **Business Activity:**

For the first time since June last year, overall activity in the Scottish private sector decreased during September. Nevertheless, at 49.8, the seasonally adjusted Output Index posted a reading only marginally below the 50.0 level that marks the threshold between expansion and contraction. In contrast to the trends seen at the UK-wide level, falling output was recorded across both manufacturing and services. Survey respondents indicated that lower new business values had been the key reason for reduced output.

### **New Business:**

Latest survey data signalled a further rise in the volume of incoming new business received by firms operating in Scotland's private sector. The increase, according to respondents, was driven primarily through promotions and discounting, and centred on the service sector. Higher order levels have now been recorded in fourteen of the past fifteen months. Nevertheless, growth of new business was only modest. Where falling order levels were registered, panellists linked this to a deterioration in economic conditions and weaker activity at clients.

### **Employment:**

Despite recording the first fall in activity since June 2009, firms operating in Scotland's private sector raised employee numbers during September. Although sharper than the rise recorded at the UK-wide level, job creation in Scotland was only marginal. Rising employment has now been recorded in nine months of the past year. In September, some panel members indicated that rising flows of new business had driven the increase in employment, although anecdotal evidence indicated that this may have reflected rising demand for temporary workers.

### **Backlogs:**

Scottish firms continued to deplete their backlogs of work during September, indicating that spare capacity remained in evidence. The latest reduction in outstanding business was the thirty-seventh in a row, albeit at the weakest pace since November last year. Backlogs fell in both the manufacturing and service sectors, with the steeper depletion registered at goods producers. Compared with the UK as a whole, the reduction recorded in Scotland was relatively modest. Falling backlogs were linked by survey participants to a weak flow of new orders.

### **Input prices:**

Rising raw material, travel and wage costs all contributed to a further month of input price inflation during September. A number of panellists also mentioned that rising wholesale food prices had added to cost pressures. Although the seasonally adjusted Input Prices Index signalled a marginal deceleration of cost inflation across the private economy in Scotland, it was again stronger than that seen across the UK as a whole, as has been the case in each month since June 2008. By industry, it was again manufacturing firms which reported the stronger pace of cost inflation.

### **Output prices:**

For the seventh time in the past eight months Scottish-based companies raised their average selling prices during September. Nevertheless, the pace of charge inflation signalled by the seasonally adjusted Output Prices Index was only marginal. Service providers and manufacturers recorded divergent trends in September. Goods producers raised their factory gate charges at the fastest pace since June, while discounting was evident in the service sector. Where tariffs were raised, the need to pass on higher costs to clients was often commented on.

**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](mailto: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 1,900 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](http://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. To learn more go to [www.markit.com/economics](http://www.markit.com/economics).

#### **For further information, contact:**

Ross Keany, Bank of Scotland Press Office  
Tel: 0131 243 7195 / 07876 475815  
Web: [www.lloydsbankinggroup.com/media.asp](http://www.lloydsbankinggroup.com/media.asp)

#### **For technical enquiries, contact**

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