

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.

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BANK OF SCOTLAND PMI: JANUARY PMI SIGNALS FURTHER OUTPUT GROWTH IN SCOTLAND'S PRIVATE SECTOR

- Slight expansion in output reported by Scotland's private sector
- Job cuts evident amid falling backlogs of work
- Input prices unchanged, ending sequence of inflation which began in January 1999

The Scottish private sector remained in growth territory during the first month of 2016. Output expanded for the second successive month in January, albeit marginally, with the latest upturn driven by a faster rise in new business volumes.

However, firms continued to cut back on employee numbers, with the rate of job shedding accelerating to the fastest since July 2015. Despite a rise in new orders and business activity, volumes of outstanding business deteriorated for the thirteenth successive month.

The seasonally adjusted headline Bank of Scotland PMI - a single-figure measure of the month-on-month change in combined manufacturing and services output - scored 50.3 again in January, unchanged from December's 2015 reading. The latest weak expansion in output was led by Scotland's service providers, while goods producers reported a contraction.

Survey data for January indicated a modest increase in new orders in Scotland's private sector, as the rate of growth accelerated to a five-month high. Moreover, incoming new business in services has risen in every survey period since March 2015.

Scotland's private sector recorded a further contraction in employee numbers during January. The rate of job shedding quickened from December but was relatively weak. Job cuts were evident in both the manufacturing and service sectors with some panellists linking the fall to a combination of higher wage costs and the downturn in the oil industry.

Backlogs of work continued to decline during January, signalling ongoing spare capacity in the private sector of Scotland. While manufacturers reported a sharp depletion of outstanding business volumes, work-in-hand fell at a comparatively modest rate in Scotland's service sector.

Average cost burdens faced by businesses operating in the private sector of Scotland remained unchanged during January. This was the first time input prices had not risen since December 1998.

With input costs remaining unchanged, firms cut their average tariffs during the first month of 2016. There was evidence that lower output prices reflected competitive pressures in the sector.

Alasdair Gardner, Bank of Scotland Regional Managing Director Scotland - Commercial Banking, said, "Growth in Scotland's private sector remained in a low-gear during the first month of 2016 as service providers continued to outperform their manufacturing counterparts. Challenging market conditions in the oil and gas sector allowed for only a slight rise in incoming new business levels whilst job shedding accelerated to a six-month high. Firms reported a further lack of pressure on capacity throughout the private sector, yet this was not enough to halt the current upturn in the Scottish economy."

Component Summary

Output / Business Activity

Business activity in **Scotland's service sector** remained in growth territory during the first month of 2016. The rate of expansion remained relatively weak overall, having been unchanged over the past three survey periods. Meanwhile, January survey data indicated a further contraction in output in the **manufacturing sector of Scotland**. Production has declined in each of the past three surveys, with panellists linking the latest fall to the downturn in the oil and gas sector. The rate of decline was marginal, however, and little-changed since December.

New Business

Incoming new business received by **Scottish service providers** continued to grow during January, extending a trend that has been evident since March 2015. The rate of growth accelerated to the fastest in seven months, yet remained modest overall. Some panellists partly linked higher volumes of new work to an increase in social marketing. **Scottish manufacturers** received a lower quantity of incoming new work during January. This was highlighted by the seasonally adjusted New Orders Index posting below the 50.0 no-change mark for the fifth successive month. Despite the rate of contraction easing to the softest since October 2015, it remained relatively solid.

Backlogs

Despite a rise in new order volumes, **Scottish service sector** companies continued to work through their outstanding business levels in January. The rate at which backlogs of work deteriorated was the sharpest in five months. Meanwhile, the seasonally adjusted Backlogs of Work Index posted below the neutral 50.0 threshold for the twentieth consecutive month during January, signalling ongoing spare capacity in the **manufacturing sector of Scotland**.

Input prices

Scotland's service sector witnessed a further increase in average cost burdens during the first month of 2016. However, the rate at which input prices rose was the weakest in the survey's 18-year history. Anecdotal evidence suggested that the higher cost for inputs reflected pressures to increase average salaries in the sector. Firms operating in **Scotland's manufacturing sector** reported a lower price for their inputs in January. However, the rate of deflation was modest. There was some evidence that the drop in input costs reflected lower commodity prices, most notably for basic metals and oil.

Output prices

Survey data for January indicated a drop in average prices set by **service providers in Scotland**. Panellists have lowered their output prices in each of the last six surveys, although the latest drop was the weakest in three months. Companies that reported falling average tariffs linked this to competitive pressures, most notably caused by the declining price of oil. Meanwhile, a further fall in output prices was reported by **Scottish goods producers** in the first month of 2016. Moreover, the rate of deflation was the most marked since August 2009. Anecdotal evidence suggested the decrease in average tariffs was due to increased competition in the sector.

Employment

Job shedding was evident in the **service sector of Scotland** for the first time since July 2015. However, the rate at which staffing levels declined was slight, as highlighted by the seasonally adjusted Employment Index posting fractionally below the 50.0 no-change mark. There was some evidence that decreasing employee numbers reflected a combination of higher wage costs and the downturn in the oil industry. Further jobs cuts were observed at **Scottish goods producers** in the first month of 2016. The rate of job shedding was solid and quickened to the fastest in one year. Moreover, headcounts have been lowered in each of the past four survey periods.

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.

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