

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: GROWTH OF ACTIVITY REMAINED SOLID DESPITE ONLY MARGINAL INCREASE IN NEW BUSINESS

- Fall in new business at service providers due to lower demand
- Scottish employment growth moderated in June
- Cost pressures eased further, but remained elevated

Activity in Scotland's private sector economy expanded at a solid pace, increasing slightly since May according to the latest Bank of Scotland *PMI*. However, with new business increasing only marginally for the second consecutive month, job creation stalled. Meanwhile, cost pressures eased further, in part leading to the weakest rise in output prices so far this year.

Private sector output expanded in June for the sixth month in succession. With growth of activity picking up in both the services and manufacturing sectors since May, the headline seasonally adjusted Bank of Scotland PMI climbed to 53.3 from 52.2 in May, and was also above the long-run series average.

Despite reporting the first fall in new business for six months, Scottish service providers continued to expand activity solidly and at a slightly faster pace than their goods-producing counterparts. Growth of output in the manufacturing sector was only moderate, but above the long-run series average nonetheless. A marginal rise in new orders in manufacturing offset the fall in new business reported by the service sector.

Lacklustre demand resulted in only a marginal rise in employment in June. Furthermore, with the exceptions of Northern Ireland, Wales, and Yorkshire & Humber – where headcounts either decreased or were unchanged – Scotland saw the slowest rate of job creation of all surveyed UK regions. Nevertheless, employment has now been rising for five months in a row.

Reflecting trends in new business received, staff numbers in the service sector fell slightly in June, but increased in the manufacturing sector, albeit only marginally. This expansion of capacity enabled goods producers to reduce levels of outstanding business at a relatively solid rate, and faster than Scotland's service providers.

Input cost inflation cooled again in June, dipping to another low for the year so far. That said, growth of purchase prices in Scotland remained sharp and above the UK-wide average. According to anecdotal evidence, the key drivers of cost increases were fuel and utilities.

In line with slower cost growth, output price inflation eased further in the latest survey period. This primarily reflected only a modest increase in tariffs by service providers.

Donald MacRae, Chief Economist at Bank of Scotland, said: "June saw the sixth consecutive month of growth this year in the private sector of the Scottish economy with growth in both the manufacturing and services sectors. However, marginal growth in new business and job creation suggest business is going through a "soft patch" with subdued growth in the second quarter of this year decelerating below that of quarter one.

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"Input cost pressures are abating. However growth of purchase prices remained sharp primarily due to cost increases for fuel and utilities. Trends in the service sector changed little since May, with activity in business services and travel, tourism & leisure expanding, while financial services contracted for a second month running. Growth in travel, tourism & leisure was the strongest since August 2007."

Component Summary

Business Activity:

Activity in Scotland's private sector economy increased in June for the sixth month in succession. Moreover, after slowing in May, the pace of growth picked up and was solid. That said, activity in Scotland continued to expand at a slightly slower pace than across the UK as a whole. Output growth accelerated since the previous survey period for both manufacturing and services, but remained below the averages for Q1 in both cases. For the second month in a row, growth of service sector activity marginally exceeded that of the goods-producing sector.

New Business:

Growth of incoming new business eased for a second consecutive month in June and was marginal. Nevertheless, new work received in the Scottish private sector economy has now been increasing for six months running. Meanwhile, expansion of new orders for the UK weakened since May and was moderate. Underpinning the latest slowdown in Scotland was the first fall in new business at service providers since last December. The decline was, however, only marginal. In contrast, Scottish manufacturers reported a modest rise in new work received.

Backlogs:

Private sector companies in Scotland reported a further decline in backlogs of work in June. Broadly unchanged since May, the seasonally adjusted Business Outstanding Index indicated that the latest drop was only modest, and weaker than the UK private sector average. The rate of reduction of backlogs at Scottish goods producers quickened since May. At service providers, however, outstanding contracts decreased at a marginal pace that was the weakest in the current three-month period of contraction in the sector.

Input prices:

The seasonally adjusted Input Prices Index dipped for the fifth successive month in June to signal the weakest rate of cost inflation since last December. Nevertheless, input prices in Scotland continued to increase at a sharp pace, in excess of both the long-run and the UK-wide averages. Scottish manufacturers continued to face faster rates of inflation than their service sector counterparts, despite reporting the weakest month-on-month increase since December. Growth of input prices also slowed for service providers, but to a lesser extent.

Output prices:

Easing in June for the fifth month in succession, output price inflation in Scotland's private sector economy was the weakest since last December. Nonetheless, prices charged still rose solidly, and at a rate above the long-run series average. Manufacturing companies continued to lead the overall rise in tariffs, increasing output prices markedly and at an accelerated pace since May. In contrast, service providers increased charges only modestly, and at the weakest rate for six months. Output price inflation across the UK as a whole remained above that for the Scottish private sector.

Employment:

For the fifth month in a row in June, employment in Scotland's private sector economy increased. That said, the latest rise in headcounts was only fractional, and the weakest in the current sequence. A similarly marginal rate of job creation was reported for the UK as a whole – which was the slowest for six months. Reflecting a fall in new business received, Scottish services providers cut jobs, albeit only marginally. The pace of job creation at manufacturing firms slowed in June, but remained above the long-run series average.

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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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For further information, contact:

Zoe Redhead, Bank of Scotland Press Office
Tel: 0131 243 7005 / 07809 551491
Email: zoeredhead@bankofscotland.co.uk
Web: www.lloydsbankinggroup.com/media.asp

For technical enquiries, contact:

Phil Smith,
Markit
Economist
Tel: 01491 461 009
Email: phil.smith@markit.com

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