PRESS RELEASE

BANK OF SCOTLAND

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: PRIVATE SECTOR GROWTH REMAINED SOLID IN DECEMBER

- **Rates of output and employment growth solid and unchanged from November**
- **New business increases at faster rate**
- **Input price inflation eases to lowest since July 2009**

Scotland's private sector economy ended 2014 on a solid footing, according to December's *PMI* report from **Bank of Scotland**. Output increased at a solid rate that was unchanged from November, supported by faster growth in new business. The rate of job creation at businesses meanwhile remained strong amid growing backlogs of work. Elsewhere, data showed a further decrease in cost inflation to the lowest since mid-2009, and only a marginal rise in output prices.

The seasonally adjusted headline Bank of Scotland PMI – a single-figure measure of the month-on-month change in combined manufacturing and services output – was unmoved in December from November's 52.8. Although still pointing to a further solid expansion of private sector **output**, the index's quarterly average (53.3) was the worst since the first quarter of 2013. At the sector level, services firms continued to outperform their manufacturing counterparts.

Growth of **new business** at companies operating in Scotland rebounded in December, accelerating from the modest pace seen in November to the joint-fastest in the past five months. **New export orders** at manufacturers continued to fall, however, although the rate of contraction slowed and was only marginal.

As was the case with output, **employment** at Scottish businesses continued to rise at a solid pace that was unchanged from November, remaining among the fastest in the survey's 17-year history (bettered only twice in February and August 2014). Staff hiring was primarily centred on the service sector.

Backlogs of work increased in December following seven months of continuous depletion. However, the rate of growth was only modest.

December's survey showed a moderation of inflationary pressures north of the border. **Input costs** increased at the slowest rate since July 2009, with overall inflation weighed down by falling fuel prices. The principal factor leading costs to rise was higher staff remuneration, according to panel member reports.

Businesses passed on just a small proportion of the burden of higher costs to clients, with average **output prices** rising only marginally and at a slower rate than in November. The rate of inflation of output prices in Scotland was slower than the UK average, contrasting with the trend in input costs.

Donald MacRae, Chief Economist at Bank of Scotland, said: "December's PMI was 52.8 indicating solid growth in the final month of last year. Both manufacturing and services sectors employed more people and experienced welcome increases in the level of new orders. However, new export orders fell for the tenth time in 11 months confirming the challenges of exporting to the largely stagnant Eurozone economies. The Scottish economy continued to recover in the second half of 2014 and looks set to expand during 2015, but with growth easing compared to the high levels of the first six months of 2014."

Component Summary

Output / Business Activity

Scottish **services firms** recorded a rise in business activity in December, linked in part to better marketing and increasing inflows of new business. That extended the current sequence of growth to 48 months, with the rate of expansion in the latest period solid and unchanged from November. **Manufacturing** output continued to grow at a modest pace in December, in line with the trend throughout the final quarter. Production has now increased in 12 of the past 13 months, with a marginal decrease in September the only break in this sequence.

New Business

Latest data pointed to another increase in the level of incoming new work at **service providers**. Furthermore, the rate of growth was strong, having accelerated from the previous month. The level of new orders at **manufacturers** returned to growth in December, thereby ending a three-month sequence of contraction. Although only slight, the increase in new orders at the end of 2014 was in stark contrast to the rapid rate of contraction recorded in the penultimate month of the year.

Backlogs

December's survey indicated a greater degree of pressure on **services companies'** resources as a result of rising inflows of new work, with business outstanding increasing for the second time in the past three months. Moreover, the rate at which backlogs accumulated was the sharpest since April. In contrast, outstanding business in Scotland's **goods-producing sector** was reduced again during December, continuing a trend observed every month since June. Despite easing to the slowest since September, the rate of decline in work-in-hand was still solid.

Input prices

December data indicated a further decrease in the rate of inflation of input prices facing Scottish **services firms**, to the weakest since July 2009. While a number of businesses commented on higher labour costs, others mentioned a drop in fuel prices as a factor weighing on overall inflationary pressures. Input prices in **manufacturing sector** increased only marginally on average in December, with the rate of inflation the weakest in almost two-and-a-half years.

Output prices

Service sector output charges increased only slightly on average during December, with the rate of inflation slower than in November. December's survey likewise showed a slower and only marginal increase in average output prices for **manufactured goods**.

Employment

The jobs market benefited from rising business activity at **services firms**, with employment in the tertiary sector increasing at a sharp and accelerated rate. In fact, the degree to which staffing levels rose was the most marked since February. **Manufacturers** also added to their payroll numbers during December, extending the current sequence of net job creation in the sector to 23 months. That said, the rate at which employment at goods producers increased eased for the second month in a row to the slowest since December 2013, and was well below the highs recorded earlier in the year.

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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.

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

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