Monthly Economic Brief

July 2020

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Office of the Chief Economic Adviser

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Overview

This month's Economic Brief provides updated analysis for Scotland as the economy progressed through phase 1 of Scotland's recovery route map with the gradual easing of lockdown restrictions at the start of phase 2 in June, highlights risks going forward and presents new measures of economic activity.

The impact of the pandemic and lockdown measures on Scotland's economic output has been rapid and severe. GDP fell 18.9% in April, the first full month of lockdown, and around 23% over March and April combined. The speed and scale of this is unprecedented relative to previous economic crises, however the context is different as around one fifth of businesses had been required to close during this period with over 600,000 workers furloughed.

The latest business surveys have signalled that business output in Scotland has continued to fall sharply in May, though to a lesser extent than in April, with UK survey data also signalling stabilisation in June.

This is to be expected as lockdown restrictions have eased and businesses have begun to resume operations albeit in different circumstances. This pick-up in activity is particularly evident in the manufacturing and construction sectors to date while activity in the services sector, and particularly those in consumer facing industries, appears more gradual.

That said, it is clear activity is restarting from a very low base and that underlying demand in the economy remains extremely weak. New business and orders, domestic and export, have continued to fall, which presents ongoing significant risks to business balance sheets, debt levels and the labour market. Therefore recovery will remain protracted through this year and into 2021.

The Scottish Government's Monthly Business Turnover Index for May showed a further fall in business turnover across almost all industries (except for food retail) and in the first half of June, almost 40% of businesses reported having cash reserves of less than 6 months. Our sectoral viability modelling indicates the scale of the impact on profitability of sectors in Scotland and the extent to which Government support, particularly the Job Retention Scheme (JRS), has been essential for protecting businesses, income and employment across sectors of the economy.

The JRS has also kept the official headline unemployment levels relatively low, however challenges remain in the labour market as businesses transition to reopening and seek to reduce costs amid ongoing weak demand. The unemployment rate in the 3 months to April was 4.6%, however the claimant count almost doubled between March and May to a rate of 7.8%, signalling that unemployment has risen and incomes have fallen.

Alongside this, survey data signal that labour demand has continued to fall sharply in June, albeit to a lesser extent than in April and May, while a sharp rise in staff availability signals that redundancies have increased. Some form of on-going wage support will be required particularly for sectors re-opening into much weaker markets.

There is evidence also emerging that this has started to put downward pressure on earnings growth and starting salaries, which alongside higher unemployment and subdued consumer sentiment, is a key risk to a consumer led recovery.

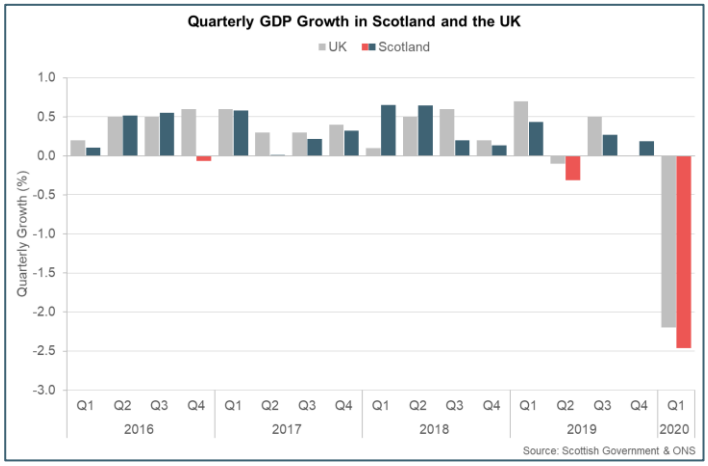
As we also move towards formally exiting the EU transition period (31 December 2020) uncertainty regarding future trade arrangements with key markets has the potential to impact already weakened business sectors and have a significant impact on economic activity, particularly if there is no deal.

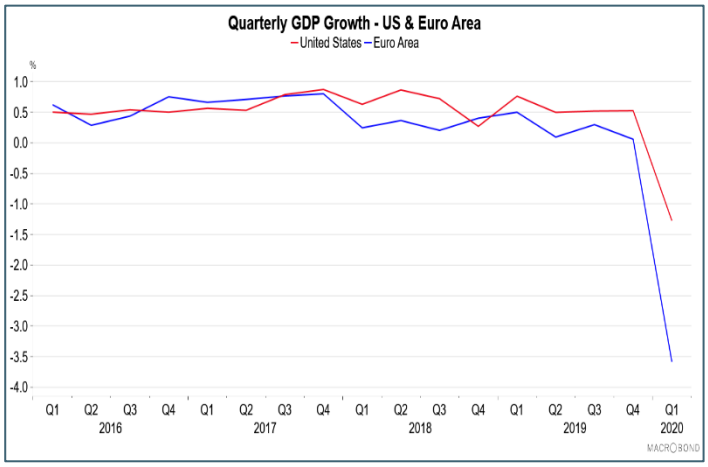
Finally, real time economic indicators remain critical for what continues to be a rapidly evolving global health and economic crisis. Next week, we publish monthly GDP data for May, the second full month of lockdown, while further business surveys provide new insights into how business and consumer activity is responding. In this report, we also provide details of a new Scottish economic index which we have developed to track and monitor impact. It is designed to capture forward expectations and is helpful for signalling changes in the economy using high frequency data. It signals recovery is happening in Scotland but at a gradual pace.

Output[1]

The coronavirus pandemic and the introduction of physical distancing and lockdown measures have had a rapid and severe impact on global and domestic economic output in 2020.

- Scotland's GDP fell by 2.5% in Q1 2020, driven mainly by a 5.0% fall in output in March as the spread of coronavirus and introduction of lockdowns slowed economic activity.
- This was evident across the UK as a whole with GDP falling 2.2% in Q1 2020 and internationally with US GDP falling 1.3% and Eurozone GDP falling 3.6% over the quarter.
- In April, the first full month of lockdown, Scotland's GDP fell by a further 18.9% over the month, similar to the pattern seen across the UK as a whole, in which GDP fell by 20.4%.
- Scotland's output fell by an unprecedented amount in nearly every industry of the economy in April. The most significant falls have been seen in sectors that have predominantly closed and in which working from home has not been possible; for example manufacturing, construction, and consumer facing services such as retail, accommodation and food services.
- When viewed across the two months of March and April, Scotland's GDP has fallen 23%.





Monthly change in Scotland's GDP across sectors
(April & May 2020)

Total GDP	March	-5.0%
	April	-18.9%
Production Sector	March	-4.6%
	April	-18.8%
Manufacturing	March	-4.2%
	April	-21.4%
Construction sector	March	-6.2%
	April	-39.8%
Services sector	March	-5.0%
	April	-17.6%
Accommodation & Food Services	March	-34.3%
	April	-77.2%
Arts, Culture & Recreation	March	-9.5%
	April	-46.1%

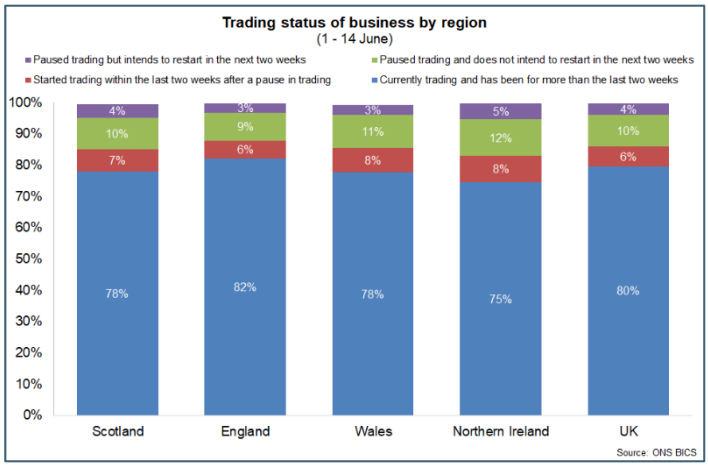
[1] Scotland: https://www.gov.scot/publications/monthly-gdp-april-2020/; https://www.gov.scot/publications/first-estimate-of-gdp-2020-q1/; UK: https://www.ons.gov.uk/economy/grossdomesticproductgdp/bulletins/quarterlynationalaccounts/januarytomarch2020; Eurozone: https://ec.europa.eu/eurostat/documents/2995521/10294996/2-09062020-AP-EN.pdf/8a68ea5e-5189-5b09-24de-ea057adeee15; US: https://www.bea.gov/data/gdp/gross-domestic-product

Business Activity

Business surveys are providing insights into the impacts that physical distancing and lockdown measures have had on business activity and cash flow in Scotland during May and the start of June.[2]

Proportion of business trading

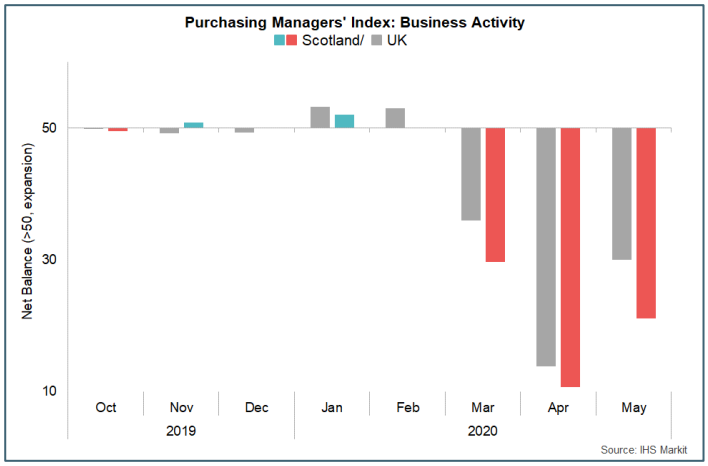
- Lockdown measures have required many businesses to close or scale down activity since March, either directly or indirectly, through a collapse in demand.
- In the first half of June, 14% of businesses in Scotland reported that they were temporarily closed (UK: 14%) and 85% reported that they were currently trading (UK: 86%).[3]
- The proportion of businesses reporting being temporarily closed has fallen from 19% in the first half of May. Latest data shows that 7% of businesses in Scotland had started trading again within the previous two weeks after a pause in trading.



- Further restarting of business activity was signalled at the start of June with 4% of businesses in Scotland reporting that they were paused trading but intending to restart in the next two weeks, however 10% reported that they did not intent to restart over the period.

Business activity

- The RBS Purchasing Managers Index (PMI)[4] reported that business activity across Scotland's private sector fell sharply in May (21.1)[5], however to a lesser extent than the survey record fall in April (10.7).
- The services sector continued to report a sharper fall in output than the manufacturing sector with both sectors strengthening from



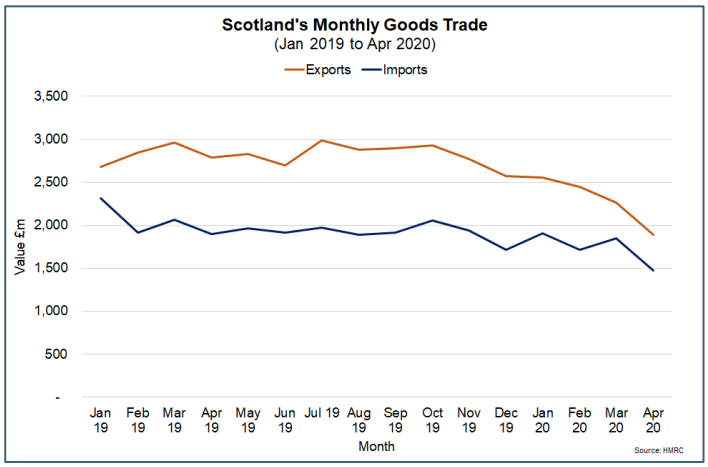
[2] The Scottish Government published its Coronavirus Route Map to changing lockdown restrictions 21 May. It started moving from Phase 1 into gradually introducing phase 2 changes to restrictions on 19th June. https://www.gov.scot/collections/coronavirus-covid-19-scotlands-route-map/
[3] ONS Business Impacts of COVID-19 Survey, Wave 7, 1 June – 14 June. https://www.ons.gov.uk/businessindustryandtrade/business/businessservices/bulletins/coronavirusandtheeconomicimpactsontheuk/latest
[4] IHS Markit, RBS Purchasing Managers Index, May 2020. https://www.markiteconomics.com/Public/Home/PressRelease/e6fdf6ec033249648c1f766cf506abb2
[5] The IHS Markit Purchasing Managers Index is between 0 and 100. Readings above 50 indicate an increase compared to the previous month, and below 50 a decrease.

April, but remaining below their levels in March. Businesses continued to link the fall in activity to temporary business closures and weak client demand.

- The UK PMI for June reported further stabilisation in business activity over the month with the UK index rising to 47.7 in June, signalling a notably softer fall in output than in the previous 3 months.[6] At a sector level, this was driven by the restarting of business activity in the manufacturing (and construction) sectors, while the services sector continued to report a fall in output with parts of consumer service and leisure activities remaining closed.
- While the business surveys signalled stronger activity as businesses restarted after being closed, underlying demand indicators remained more subdued with new orders/business stabilising at a slower pace, particularly export orders, while businesses also continued to reduce staffing levels while seeking to control costs amid weak demand.

Trade

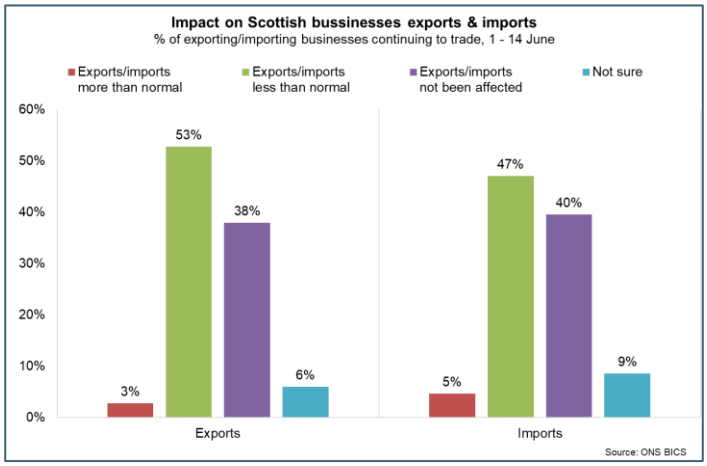
- On the back of significant global trade headwinds in 2019 and Brexit uncertainty, many businesses have faced further trade disruption in 2020 due to the pandemic and lockdown measures across countries.
- In April 2020 (compared to April 2019) the value of Scotland's goods exports fell 32% (UK: -31%) to £1.9 billion, while Scotland's imports fell 22% (UK: -32%) to £1.5 billion over the same period.[7]



- The decrease over the year likely reflects large decreases in the UK exports of key commodities for Scotland including whisky (-40%), salmon (-58%), oil (-49%) and gas (-74%).
- The changes in exports and imports over the past year have varied by destination/origin. In terms of trade with the EU, Scotland's goods exports to the EU decreased by 11% (UK: -32%) compared to April 2019, while imports from the EU decreased by 18% (UK: -39%).
- Scotland's goods exports to non-EU countries decreased by 46% (UK: -31%) compared to April 2019, while imports from non-EU countries fell 26% (UK: -24%).

[6] https://www.markiteconomics.com/Public/Home/PressRelease/77508f50614f4294907b785d0945b1ea
[7] https://www.gov.uk/government/statistics/regional-trade-in-goods-statistics-by-month-april-2020

- ONS data[8] suggests that subdued trade activity continued into the first half of June with 53% of Scottish trading exporters reporting that they were exporting less than normal and 47% of Scottish importers. This was broadly in line with the UK as a whole (52% of exporters and 44% of importers).



Real Time Economic Impact Index

COVID-19 has resulted in an economic crisis in Scotland, through the direct impact on the economy but also the secondary impacts on health and society from a weaker economy.

The impact of COVID-19 is not constant, and will be changing over time, depending on the prevalence of the virus and the severity of the restrictions required to protect against it. Most traditional measures of the economy do not provide a real time assessment, instead looking over longer periods such as a month or a quarter. They are therefore less useful when assessing the impact of the different phases of the virus.

In order to monitor the current level of economic impacts arising from COVID-19 we have developed a Real Time Economic Impact Index, which uses a set of high-frequency indicators to report on economic impacts by week. Any assessment of the economic impact of COVID-19 will be very uncertain, and to address this we look across a range of indicators in 3 broad groups[9]:

(1) Demand Indicators - measuring the changing demand across different sizeable sectors of the economy due to changing behaviours and restrictions:

- Electricity demand
- Non-residential real estate sales
- Consumer transactions

(2) Supply Indicators - measuring the disruption to supply chains and workforce participation:

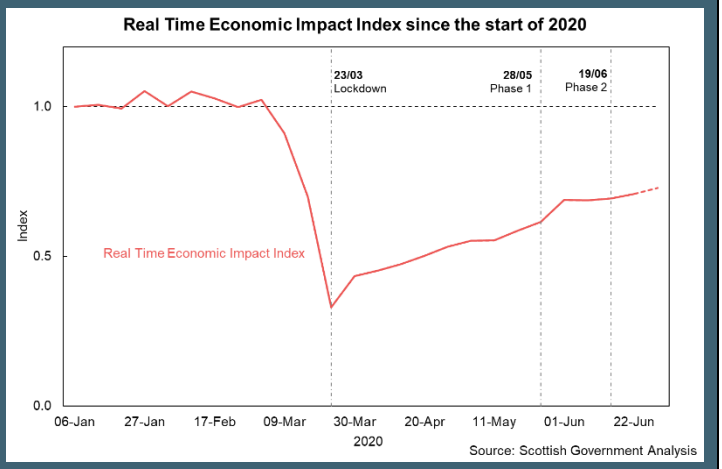
- New Universal Credit claims
- Heavy Goods Vehicle (HGV) traffic counts

(3) Forward looking Indicators - measuring levels of uncertainty and future expectations:

[8] ONS Business Impacts of COVID-19 Survey, Wave 7, 1 June – 14 June.
https://www.ons.gov.uk/businessindustryandtrade/business/businessservices/bulletins/coronavirusandtheeconomicimpactsontheuk/latest
[9] Relating to the frameworks presented in https://www.gov.scot/publications/state-economy-april-2020/

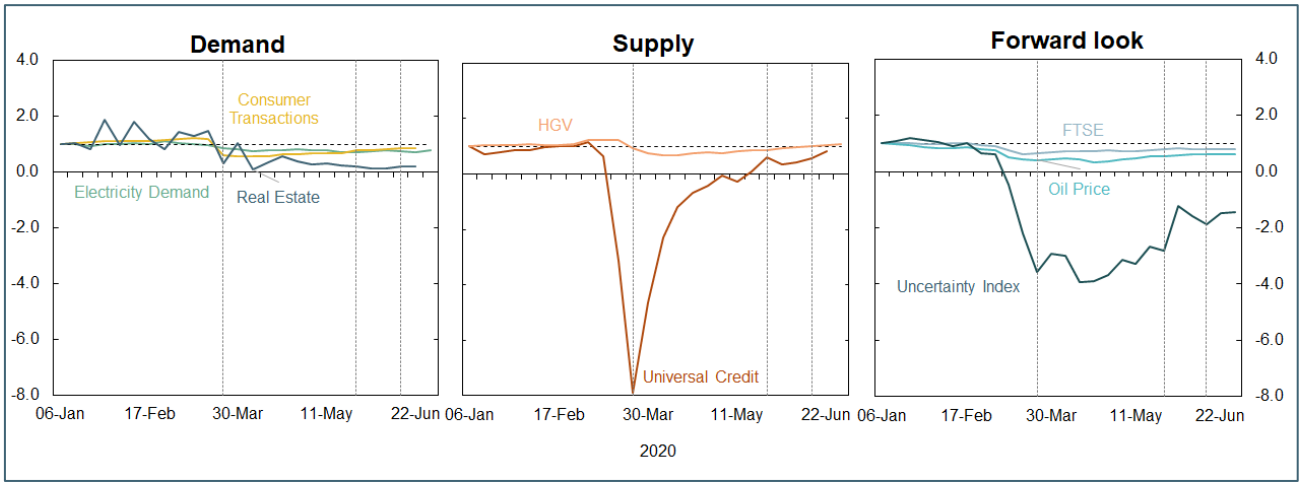
- FTSE250
- Brent Crude Oil Price
- UK Economic Policy Uncertainty Index

The overall index is derived by weighting each indicator according to their volatility since the start of 2019. When the index is below 1 economic impact is negative and when the index is at or above 1 the economy has returned to operating as normal (compared to January).



As can be seen, the Real Time Economic Impact Index deteriorated before lockdown was introduced, highlighting the importance of market expectations. It reached its lowest level of 0.33 in the week ending 29th March. However, it has been rising gradually since, reaching 0.71 in the week ending 28th June. It is forecast to increase further to 0.73 by the week ending 5th July. It increased slightly faster following the move to Phase 1, although there has yet to be a notable impact from the move to Phase 2. This may reflect that the restrictions in Phase 2 are being lifted gradually, and many shops had not reopened by the end of June.

Real Time Economic Impact Indicators since the start of 2020



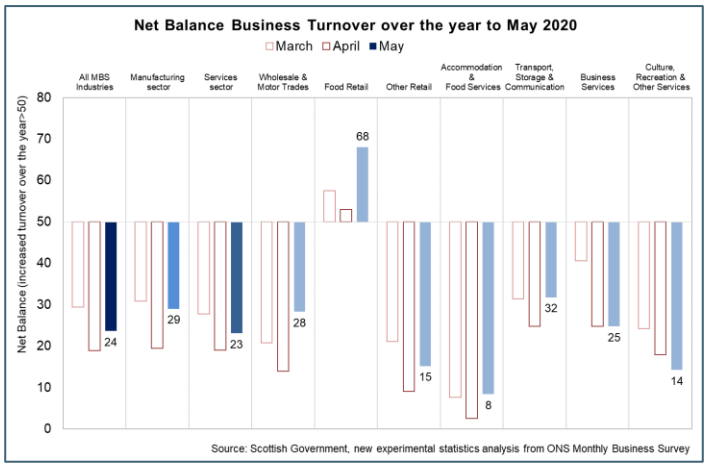
Looking across the different indicators it can be seen that the HGV index has returned to January levels, while non-residential real estate sales remain significantly down on January levels.

There is considerable uncertainty regarding the economic outlook and monitoring real time impacts is another approach to complement other economic data.

Business Turnover

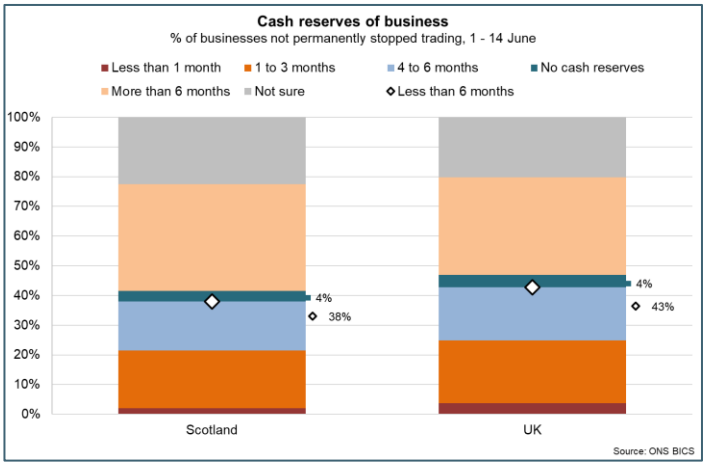
The closure, scaling down of business operations and fall in demand during lockdown has resulted in significant cashflow challenges for businesses.

Monthly Business Turnover Index[10]



- Over the year to May 2020, business turnover in Scotland fell sharply for most companies across almost all sectors. Furthermore, turnover decreased for the third consecutive month, albeit to a lesser extent than in April (24, up from 19).
- Business turnover continued to fall across both the manufacturing (29) and service (23) sectors in May, with the manufacturing sector strengthening by slightly more compared to April.
- Within the services sector, turnover continued to fall across all service industries except for Food Retail, in which turnover growth strengthened over the month. The Accommodation and Food Services continued to be the industry with most businesses reporting a decrease in turnover, followed by Culture, Recreation and Other Services, which was the only service sector industry to see turnover weaken compared to April.
- The slight improvement from April is in keeping with other business indicators signalling an increase in business activity as businesses started to plan for easing of lockdown measures. However, the broad based falls in business turnover continue to emphasise the precarious cashflow position that many businesses are facing.

Cash reserves of business



- The fall in turnover has resulted in businesses using their cash reserves to accommodate ongoing costs for the business.
- Of the Scottish businesses that had not permanently stopped trading in the first half of June, 38% of businesses reported having cash reserves to last between zero to six

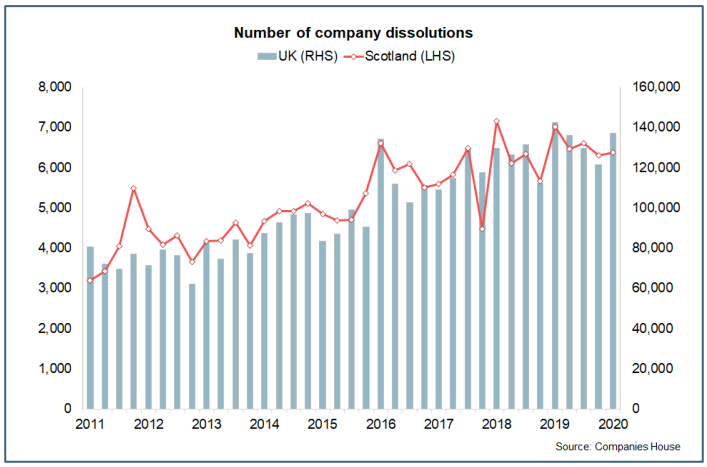
[10] https://www.gov.scot/publications/monthly-business-turnover-index-may-2020/ The Index is between 0 and 100. Readings above 50 indicate an increase compared to the previous year, and below 50 a decrease.

months (UK: 43%), while 36% of Scottish businesses had cash reserves to last more than 6 months (UK: 33%).[11]

- 4% of Scottish businesses reported they had no cash reserves (UK: 4%), which is slightly higher than reported in the first half in May (2.9%) and reflects the ongoing financial challenges facing businesses.

Business dissolution

- Quarterly Companies House data for Scotland reported a slight increase in the number of company dissolutions in Q1 2020.
- Between January and March 2020, there were 6,378 dissolutions in Scotland (UK: 136,978). Compared to Q4 2019, the number of dissolutions increased slightly by 1% (UK: +13%).



- Monthly data, which is only available for the UK as a whole, for March 2020 showed that the number of dissolutions increased by 7,453 (23%) compared to March 2019.

Sectoral Viability Modelling

COVID-19 has had a significant impact on economic activity in Scotland with the requirement to strictly close approximately 20 per cent of businesses during lockdown and the need for other sectors to restrict or change how they operate.

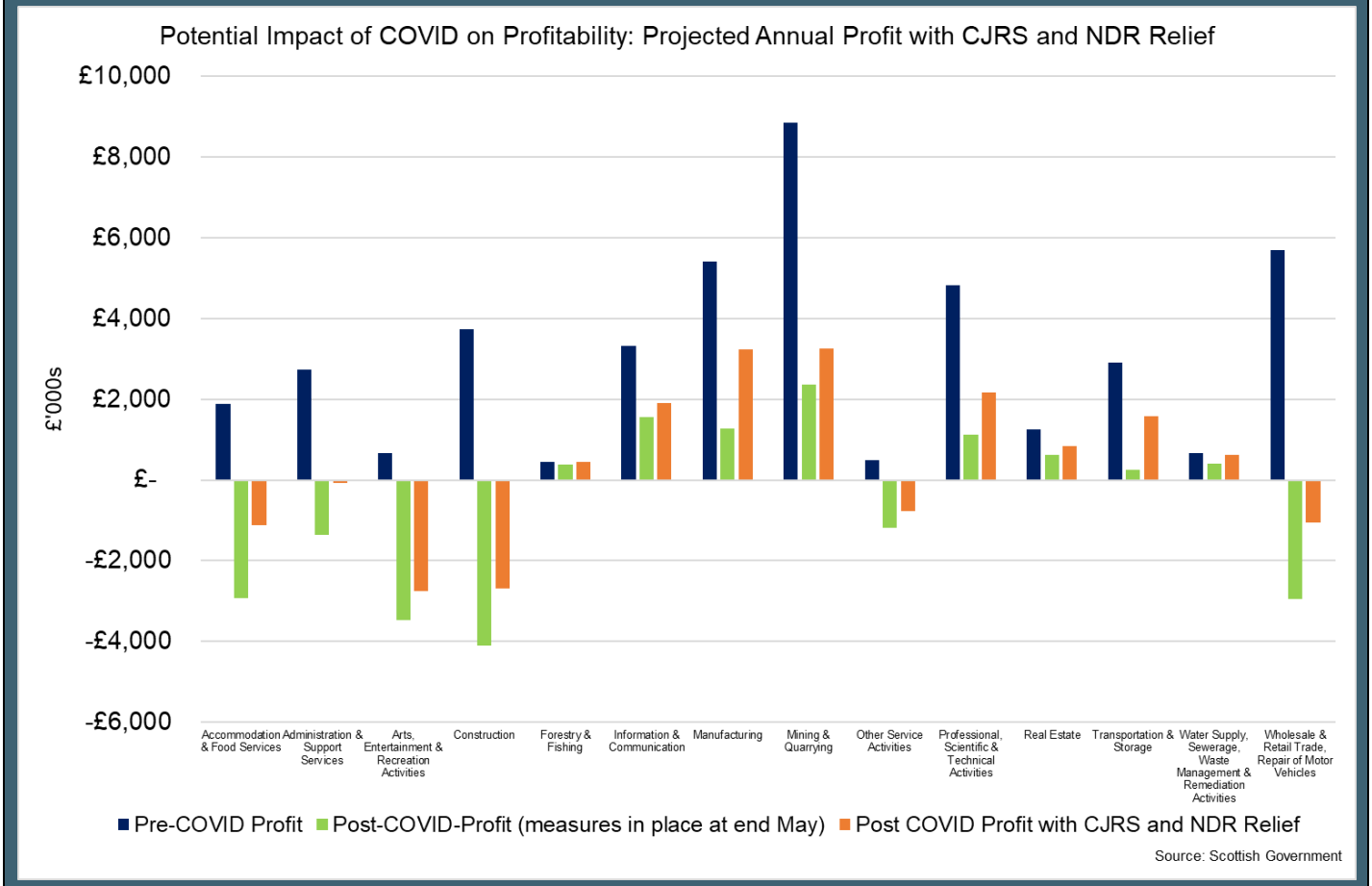
We know from the macro level analysis and the economic data published to date that output (GDP) produced in Scotland over March and April contracted by approximately 23%. We have also seen a rising number of redundancies across sectors with businesses restructuring (retail etc.) to reopen in different market circumstances.

Below the aggregate data, there are clearly different sectoral impacts with those most affected reflecting their ability to trade during the pandemic. For example, output for accommodation and food services was estimated to have contracted by nearly 80% in Scotland during April. Similarly, construction output fell by 40% while other sectors experienced much smaller contractions with the exception of food retail which increased.

[11] ONS Business Impacts of COVID-19 Survey, Wave 7, 1 June – 14 June.
https://www.ons.gov.uk/businessindustryandtrade/business/businessservices/bulletins/coronavirusandtheeconomicimpactsontheuk/latest

To better understand the sectoral impacts and the profitability and viability of sectors of the economy, OCEA has developed a framework for assessing how the pandemic and lockdown could affect business viability across different sectors of the economy. The model framework allows us to simulate the impact of lockdown directly on viability (turnover, cashflow, profitability and employment) and illustrate the impact of Government support such as rates relief, job retention scheme and related grants.

As an illustration, the chart below models the impacts on business profitability that the Job Retention Scheme and NDR Rates Relief has had across aggregate sectors of the economy.[12]



The initial results highlight both the importance of the immediate Government support to sectors of the economy, but also the risks that remain for those sectors not operating at previous levels. As the economy re-opens we will continue to monitor the impact on sectoral viability as turnover improves but also as the various government schemes are withdrawn or wound down. We will provide further updates on this analysis which links to our broader macro modelling work.

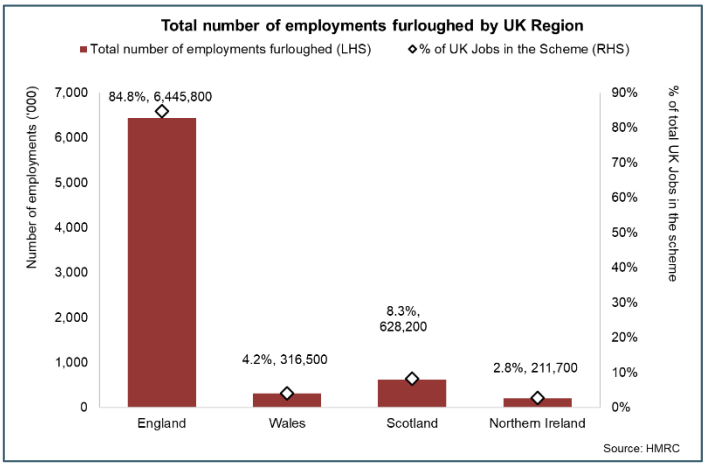
[12] Based on OCEA analysis of Scottish Annual Business Statistics and ONS Business Impacts of Coronavirus Survey.

Labour Market

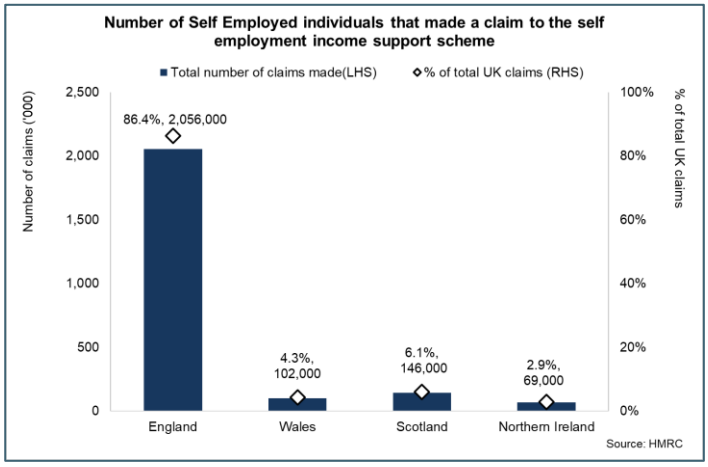
The impacts of the coronavirus pandemic on Scotland's labour market are only starting to emerge with the Coronavirus Job Retention Scheme supporting jobs and incomes during lockdown.

Coronavirus Jobs Retention Scheme (CJRS) and Self Employment Income Support Scheme[13]

- The CJRS has supported job retention and incomes during the lockdown phase as businesses have been required to close or significantly scale down business operations.
- At the end of May 2020 in Scotland, there were 628,200 jobs furloughed (8.3% of UK jobs in the scheme).
- Scottish Government estimates this is around 27.1% of employees in Scotland as being furloughed, broadly in line with other parts of the UK (England: 27.9%; Wales: 25.6%; NI: 29%).



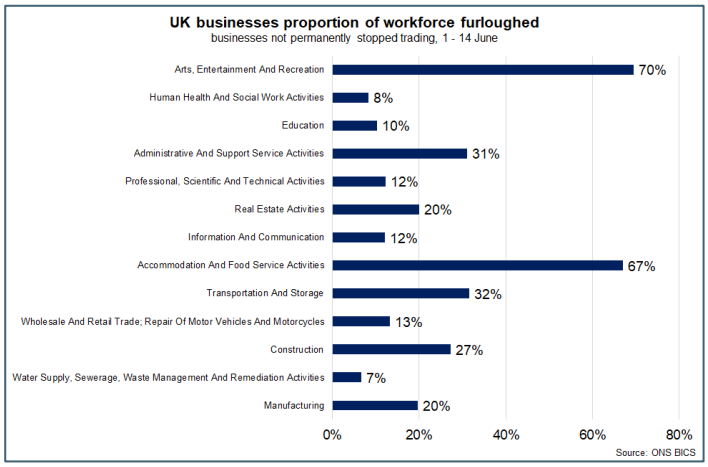
- Glasgow City (74,400) and Edinburgh City (58,400) were the local authorities in Scotland with the most claims, followed by North Lanarkshire (41,800).
- In terms of self-employed in Scotland, 146,000 (70% of eligible) self- employed individuals made a claim to the Self Employed Income Support Scheme (SEISS) up to the end of May. This was 6.1% of all claims across the UK and potentially reflects the lower level of self employed in Scotland.



- Glasgow (15,500) and Edinburgh (14,200) were the local authorities in Scotland with the most claims to the SEISS.

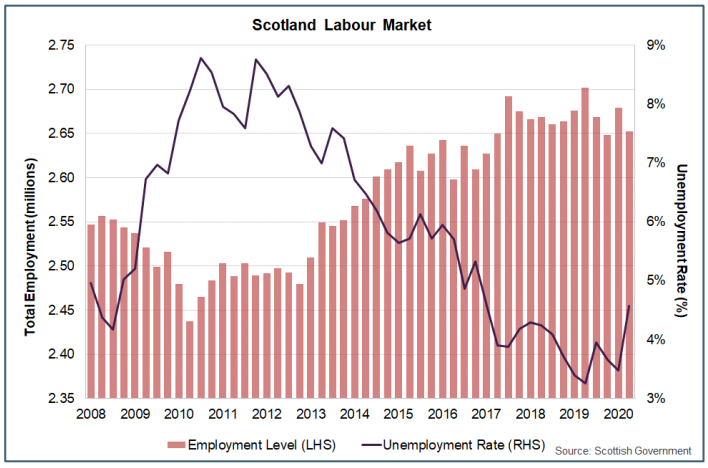
[13] https://www.gov.uk/government/statistics/coronavirus-job-retention-scheme-statistics-june-2020

- ONS data[14] show that the CJRS remained an important element of support for businesses in the first half of June, particularly for sectors that remained largely closed. At a UK level, of businesses that had not permanently stopped trading, 23% of their workforce was estimated to be on furlough leave. The arts, entertainment and recreation sector and the accommodation and food services sector had the highest proportions of furloughed workers – 70% and 67% respectively.



Official labour market statistics

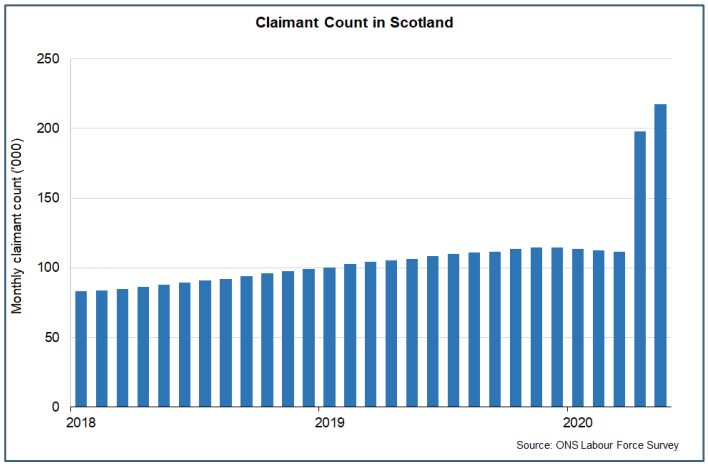
- The latest official labour market statistics for February to April 2020 record furloughed workers as employed, but temporarily away from work. Over the year to February to April 2020 the Labour Force Survey showed:[15]
- The employment level decreased by 50,000 and the employment rate fell by 1.7 percentage points to 74.3% (UK; 76.4%).



- The unemployment level increased by 36,000 and the unemployment rate increased by 1.3 percentage points to 4.6% (UK; 3.9%).
- The economic inactivity (those neither in employment or ILO unemployed) level increased by 22,000 and the inactivity rate increased by 0.6 percentage points to 22.1 (UK; 20.5%).

Claimant Count

- Scotland's Claimant Count[16] (the number of claimants of Job Seekers Allowance and Universal Credit 'searching for work' conditionality) has increased sharply since March signalling that despite the support provided by the CJRS, incomes have fallen and unemployment has risen.

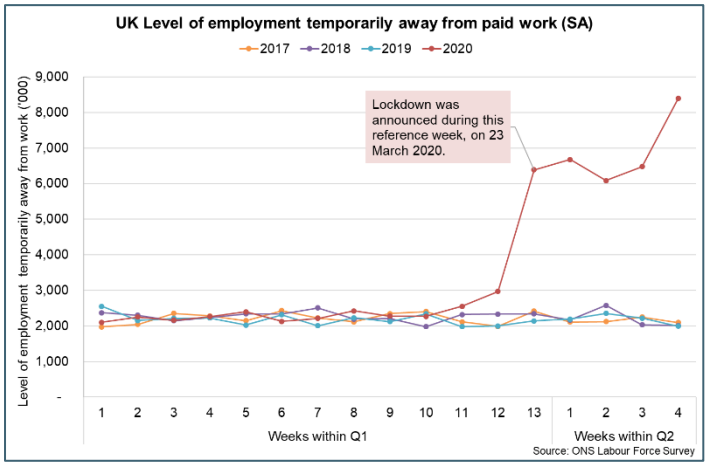


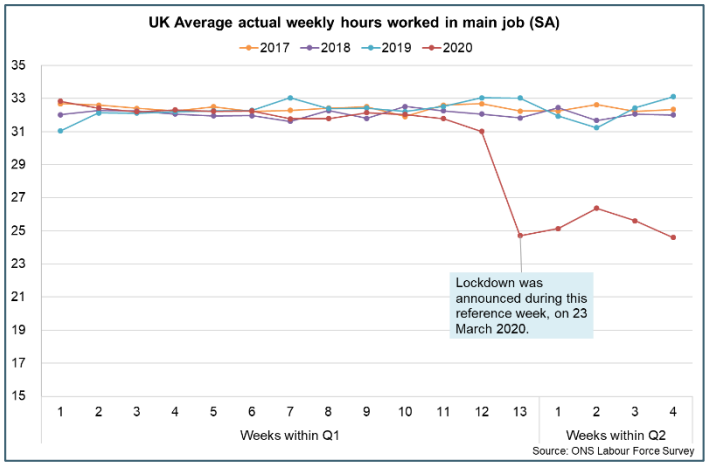
[14] ONS Business Impacts of COVID-19 Survey, Wave 7, 1 June – 14 June.
https://www.ons.gov.uk/businessindustryandtrade/business/businessservices/bulletins/coronavirusandtheeconomicimpactsontheuk/latest
[15] https://www.gov.scot/collections/labour-market-statistics/
[16] https://www.gov.scot/collections/labour-market-statistics/

- In May, the Claimant Count was 217,600 (a rate of 7.8%), up 20,000 over the month (10%) and over 100,000 since March (95%).

Hours worked

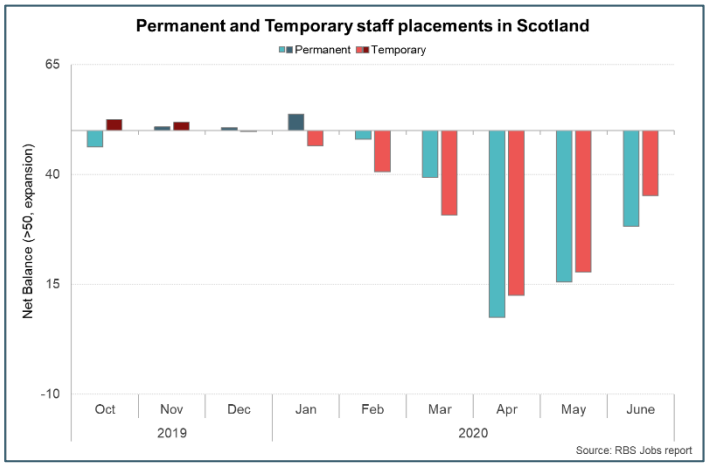
- Weekly ONS Labour Force survey data (published for the UK as a whole) showed a significant drop in hours worked and a sharp increase in the number of people temporarily away from work in the second half of March and throughout April, as lockdown measures were in place.





Demand for staff in Scotland

- The RBS Report on Jobs survey for June[17] reported further sharp falls in demand for permanent and temporary staff in Scotland, albeit to a lesser extent than in April and May.
- Staff placements and vacancies continued to fall sharply over the month reflecting that businesses continued to freeze or delay hiring activity.



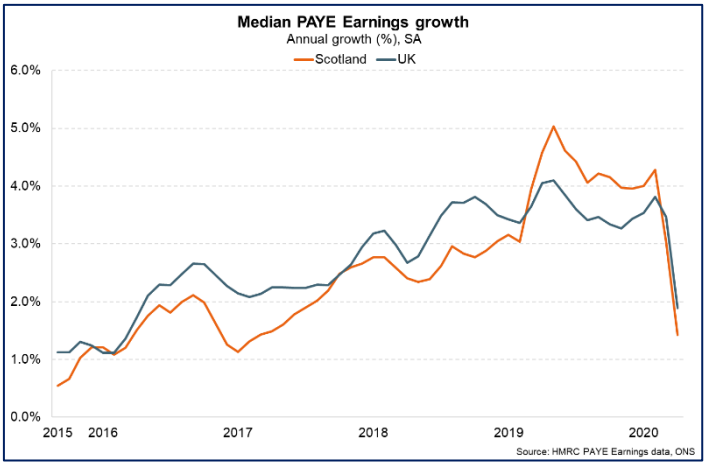
- Alongside this, candidate availability rose sharply in June suggesting a rise in redundancies, while emerging pay pressures were evident with salaries appointed to new staff falling at their sharpest pace in the survey time series.

Earnings

- The impact of the coronavirus on business activity and Scotland's labour market has started to feed through to a significant slowdown in earnings growth.

[17] https://www.markiteconomics.com/Public/Home/PressRelease/054118c564104d339eea711e43dcc686

- Pay As You Earn (PAYE) earnings data[18] reported a significant slowdown in nominal median earnings growth in Scotland over the year to April 2020.
- Annual growth in PAYE median pay in Scotland was 1.4% in the year to April 2020 (UK: 1.9%), significantly lower than earnings growth prior to the lockdown measures.
- Prior to the COVID-19 crisis, Scotland saw a pick-up in PAYE earnings growth in 2019 and at the start of 2020, with annual growth in the year to February 2020 at 4.3% (UK: 3.8%). This period of stronger growth followed relatively weaker earnings growth in 2017 and 2018.

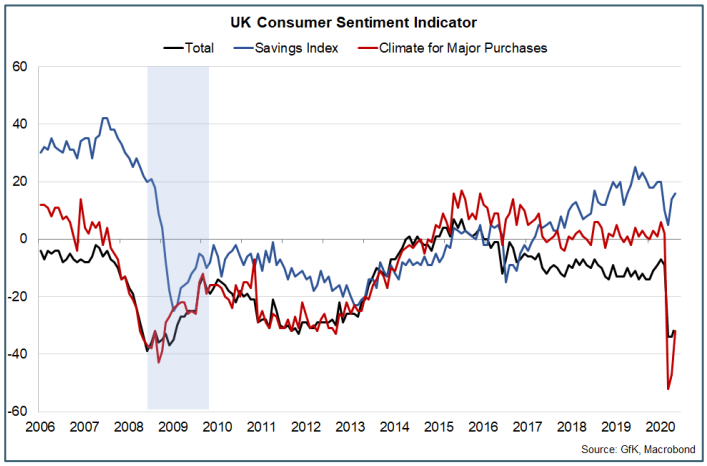


Consumption

Physical distancing measures, alongside more fragile household finances and weakening consumer sentiment is impacting demand in the economy and overall saving and consumption patterns.

Consumer sentiment

- UK consumer sentiment has fallen sharply since the end of March, reflecting weaker expectations about the performance of the economy and personal household finances.
- UK Consumer Sentiment for June[19] remained low at -30, and close to its level during the financial crisis.
- Compared to May, households in June reported small improvements in economic and household financial expectations for the next 12 months and a pick-up in attitudes towards savings and major purchases.
- UK Flash consumer sentiment[20] (collected 18 – 26 June) showed that UK consumer confidence continued to improve slightly in the second half of June, however, overall consumer confidence remained significantly lower than prior to the pandemic.



18 https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/bulletins/earningsandemploymentfrompayasyouearnrealtimeinformationuk/june2020
19 https://www.gfk.com/en-gb/press/UK-Consumer-Confidence-gains-six-points?hsLang=en-gb
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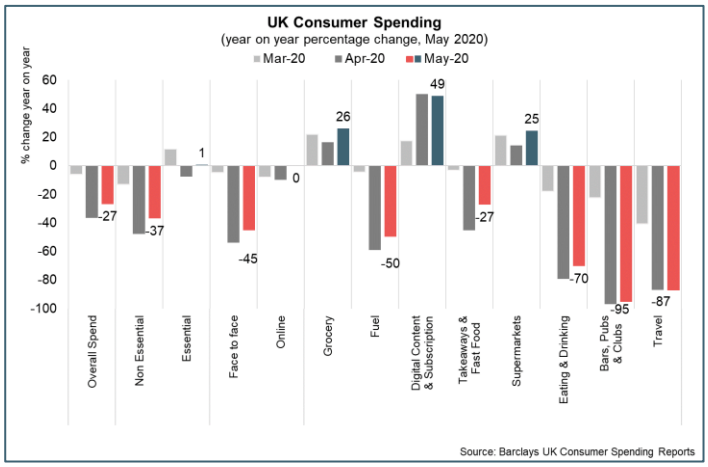
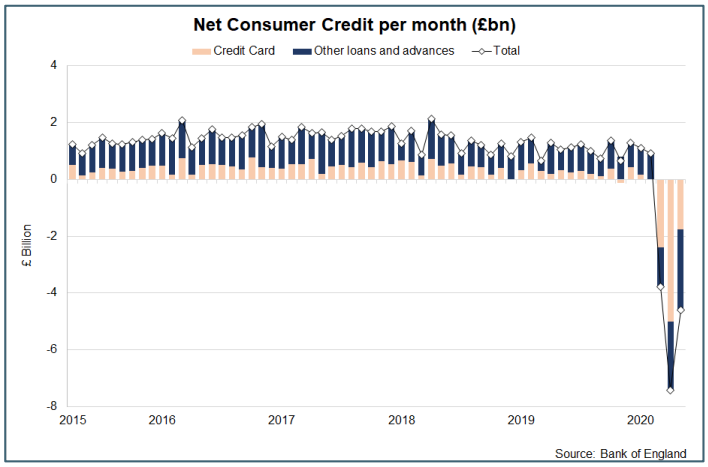
Consumer spending



- UK consumer spending data[21] showed a 27% fall in consumer spending over the year to May 2020 following a sharper fall of 37% in April.
- Spending on essentials grew slightly by 1% due to a 25% increase in supermarket spend, while non-essential spending declined by 37% driven by large falls in travel spend (-87%) and spending in bars, pubs and clubs (-95%).
- Digital subscriptions continued to increase in popularity with strong growth of 49% potentially reflecting increased demand through home working, learning and entertainment. Spending on Eating and Drinking saw a decline of 70% in May, up from the almost 80% fall in April, due to more pubs, cafes and restaurants offering take-away and delivery services.

Consumer lending and repayment[22]



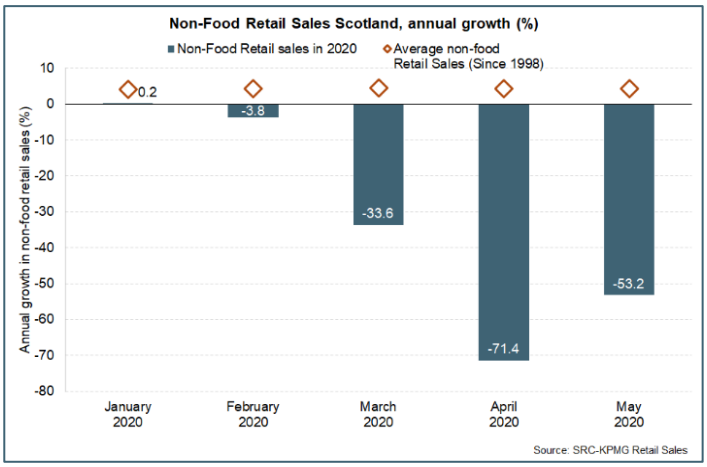
- While consumer spending has fallen sharply during lockdown, likely reflecting a combination of essential retail closure and weaker sentiment regarding the outlook, the CJRS has been supporting incomes of those not working. This has been reflected in consumers taking on less new borrowing and repaying more existing borrowing.
- Gross lending to UK consumers was £13.6 billion in May, up from £11.8 billion in April, but remained notably below the average of £25.5 billion average in the six months to February 2020.
- Repayments on consumer borrowing fell to £17.7 billion in May, from £19.9 billion in April, however more than offset new borrowing for the third month in a row.
- On net, consumers repaid £4.6 billion of consumer credit over the month, following net repayment of £11.2 billion over March and April.

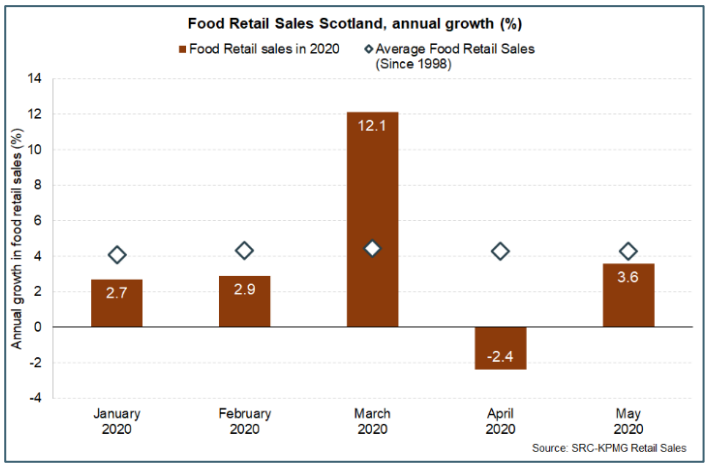
[21] Barclays UK Consumer Spending Report: https://www.barclays.co.uk/content/dam/documents/business/manage-your-business/UK_Consumer_Spending_Report_May_2020.pdf
[22] https://www.bankofengland.co.uk/statistics/money-and-credit/2020/may-2020

- Overall, the fall in net consumer credit continues to show that consumer spending remains weak, with the fall in the size of repayment over the month potentially reflecting a combination of gradual lifting of lockdown restrictions, stronger consumption and/or household cashflow challenges.

Retail sales

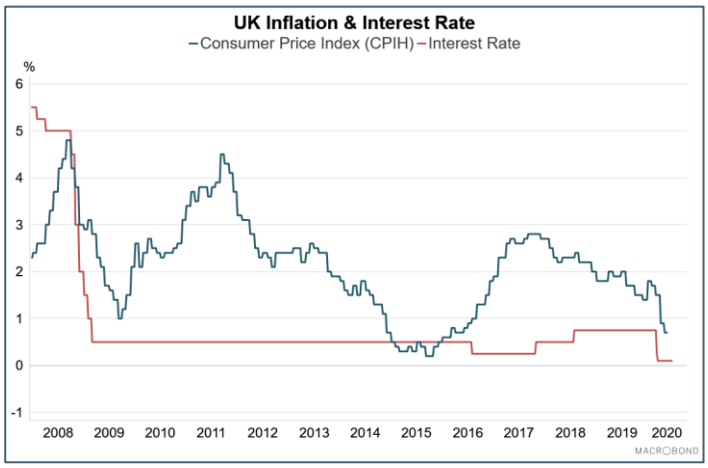
- Scottish Retail Consortium data[23] on retail sales for May reported an annual decrease of 27.5% in total retail sales in Scotland, easing from the record fall in April (-40.3%).
- The decline in retail sales in May was mainly driven by a fall in non-food retail sales. Over the year to May, non-food retail sales fell by 53.2%, while food retail sales increased by 3.6%.
- The combination of lockdown measures, increased pressure on incomes and weaker sentiment are likely impacting the overall fall in retail sales.





Inflation and interest rates

- The fall in demand, alongside the fall in oil price to record lows has placed downward pressure on inflation at the start of 2020.
- The Consumer Prices Index including owner occupiers' housing costs (CPIH) 12-month inflation rate was 0.7% in May 2020, down from 0.9% in April 2020.[24]



- Key downward contributions to the rate came from falling prices for motor fuels and a variety of recreational and cultural goods. The largest partially offsetting upward contributions came from a rise in foods and non-alcoholic drinks.

[23] Source: Scottish Retail Consortium.
[24] https://www.ons.gov.uk/economy/inflationandpriceindices/bulletins/consumerpriceinflation/may2020

- The Bank of England reduced the Bank Rate to 0.1% in March 2020[25] and in their current central scenario analysis project inflation to fall to 0.6% in 2020 and 0.5% in 2021 before picking up to target at 2.0% in 2022.

Sectoral Exposure Analysis

This box explores the challenges different sectors could face towards the end of this year and over the next 5-10 years, with businesses facing a double challenge of both recovering from the impacts of COVID-19 as well as facing the challenge of higher barriers to trade with the EU.

The end of the transition period represents an additional risk to the sectors already exposed to COVID-19, especially those with EU supply and demand chains or those whose labour supply will be affected by the removal of freedom of movement for workers.

Exposure to Trade Barriers

From the 1st January 2020, with no transitionary period extension, many sectors will see the introduction of new barriers on trade with the EU. This will primarily take two forms: tariffs and non-tariff barriers to trade (NTBs).

Tariffs on UK trade with the EU will depend on the form of EU exit. If no UK-EU trade agreement is agreed, UK exports into the EU would face EU Most-Favoured Nation (MFN) tariffs.[26] Under this scenario, agriculture and food products will face the majority of the high tariff lines, while generally smaller tariffs apply to manufacturing products. In addition to this, all sectors would also face tariffs on imports from the EU as detailed by the UK Government[27], where significant import tariffs would be faced across many agricultural and food product imports. In the event of a 'skinny' UK-EU trade agreement, the extent of tariff elimination is unclear, with the possibility of many of these tariffs remaining.

In addition to tariffs, firms will face NTB on EU trade. NTBs are defined as technical, regulatory, and administrative barriers to trade, including barriers relating to custom procedures and other at the border costs.

Some of the highest NTB would be seen in the categories of agricultural, food and drink products[28]. For example, food safety and animal and plant health checks[29] are used to ensure that imported goods are safe for health. This could take the form of additional administrative requirements for these goods, as well as checks at the UK-EU border. For manufacturing

[25] https://www.bankofengland.co.uk/news?NewsTypes=09f8960ebc384e3589da5349744916ae&Taxonomies=36308a372d1e44ee94e6b5915796c531&InfiniteScrolling=False&Direction=Latest
[26] https://www.wto.org/english/res_e/statis_e/daily_update_e/tariff_profiles/E28_E.pdf
[27] https://www.gov.uk/check-tariffs-1-january-2021
[28] For more detailed analysis, see: https://www.gov.scot/binaries/content/documents/govscot/publications/publication/2019/02/state-economy-february-2019/documents/brexit-scottish-sectoral-economic-impact-analysis/brexit-scottish-sectoral-economic-impact-analysis/govscot%3Adocument/00546072.pdf
[29] https://www.wto.org/english/tratop_e/sps_e/sps_e.htm

industries, another barrier in the form of technical barriers to trade would be faced. These barriers relate to compliance with manufacturing processes to ensure protection of human health and safety or protection of the environment.[30]

The context of COVID-19

Analysis on the sectoral exposure to COVID-19 were published in State of the Economy: April 2020[31]. This detailed the different domestic and international channels through which sectors have been exposed to lockdown restrictions around the world and found cumulative impacts across all economic channels to be greatest for manufacturing, construction, retail & wholesale, accommodation & food services, and arts, entertainment, and recreation.

Table 1: Sectoral Exposure to a no EU trade deal exit and COVID-19[32]

Sector	No EU trade deal	COVID-19: International Supply	COVID-19: International Demand	COVID-19: Domestic Demand	COVID-19: Labour Market Disruption
Primary/Manufacturing Sectors					
Agriculture, forestry and fishing	R	Y	A	Y	Y
Mining and Quarrying Industries	R	Y	A	A	Y
Manufacturing	R	R	R	A	R
Electricity, Gas & Water Supply	A	Y	Y	Y	A
Construction/Service Sectors					
Construction	A	Y	Y	R	R
Retail & wholesale	A	Y	Y	R	R
Transport & Storage	A	Y	Y	A	A
Accommodation & food services	A	Y	A	R	R
Information & Communication	A	A	Y	Y	Y
Financial & Insurance Activities	A	Y	Y	Y	A
Real Estate Activities	Y	Y	Y	Y	A
Professional, Scientific& Technical Services	A	Y	A	Y	A
Administrative & Support Services	A	Y	Y	A	R
Public Administration and Defence	Y	A	Y	Y	R
Education	Y	Y	A	Y	R
Health and Social Work	Y	A	Y	Y	R
Other Services	Y	Y	Y	R	R
Legend	Red [R]: Most Exposed				
	Amber [A]: Medium Exposure				
	Yellow [Y]: Least Exposed				

Table 1 combines trade barrier exposures faced by sectors in the event of a no UK-EU free trade agreement with aforementioned analysis on COVID-19 exposures to illustrate what sectors could face the biggest challenges.

The table indicates that some industries, such as agriculture, forestry and fishing who may be relatively less exposed to the impact of COVID-19 could be more exposed to EU exit trade shocks. It also suggests that a number of sectors can be expected to face a double hit. For example manufacturing industries are found to have a high exposure to the COVID-19 shock and to the EU exit trade shocks. Even sectors with relatively low direct exposure to trade such as

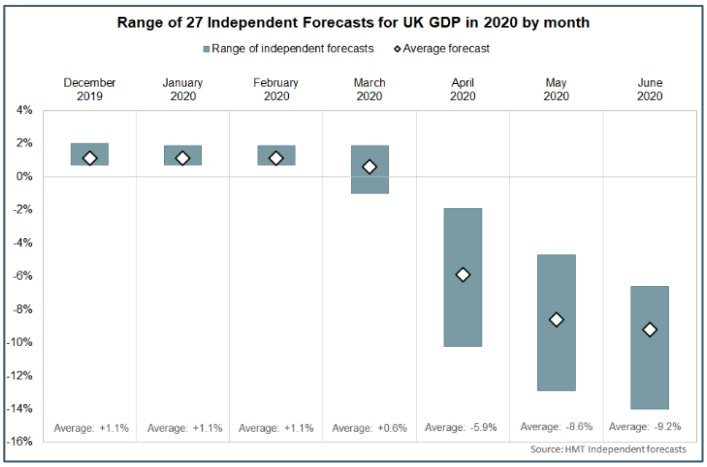
[30] https://www.wto.org/english/tratop_e/tbt_e/tbt_e.htm
[31] https://www.gov.scot/publications/state-economy-april-2020/pages/6/
[32] More detail on this can be found in a previous Scottish Government publication: https://www.gov.scot/publications/covid-19-case-extending-brexit-transition-period/

construction could also face a relatively high impact from leaving the EU without a trade deal due to the indirect impacts from the shock to the economy as a whole.

The UK economy will experience a change in its trading relationship with its biggest trading partner at a time when businesses are still recovering from the COVID-19 crisis. Companies already dealing with trading difficulties, increased indebtedness and restricted cash flows could face further disruption in the form of increased tariffs, customs declarations, border delays, and reduced access to EU workers. This highlights the importance of a comprehensive trade deal with the EU.

GDP Growth Outlook

The economic outlook for 2020 has deteriorated significantly as a result of the coronavirus pandemic and the necessary restrictions on economic activity to minimise the spread of the virus.



- The scale and duration of the economic impacts remains uncertain, however the degree of pessimism in forecasts has increased over the course of the year.
- At a global level, the latest IMF World Economic Outlook Update[33] projects a deeper fall in output in 2020 and a more gradual recovery than was previously estimated, with global GDP projected to fall by 4.9% in 2020.
- At a domestic level, as lockdown restrictions begin to be loosened across the UK, the economic data has started to show an increase in business activity as firms plan and restart operations. However, underlying demand remains weak with new orders/business not strengthening to the same degree and businesses continuing to reduce staffing levels.
- Scotland's scenario analysis published last month, suggests GDP could fall by 14% in 2020 and unemployment could rise above 10%, and that a gradual recovery in which output and employment doesn't get back to pre-crisis levels until 2023-24 is increasingly likely.[34]
- Scenario analysis from the Bank of England estimates UK GDP could fall by 14% over the year[35] while HM Treasury's monthly summary of independent GDP forecasts[36] reports UK GDP is forecast to contract by an average of -9.2% in 2020 (down from -8.6 in May 2020).

[33] https://www.imf.org/en/Publications/WEO/Issues/2020/06/24/WEOUpdateJune2020
[34] https://www.gov.scot/publications/monthly-economic-brief-2/
[35] https://www.bankofengland.co.uk/report/2020/monetary-policy-report-financial-stability-report-may-2020
[36] https://www.gov.uk/government/statistics/forecasts-for-the-uk-economy-june-2020

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