

Monthly Economic Brief

Office of the Chief Economic Adviser

June 2022

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June 2022**

Data up to 01 July 2022

Overview

This month's economic brief provides an update on data during the second quarter of the year, in which slowing output growth, rising inflation and tight labour market conditions are very much shaping current economic conditions. Furthermore, conditions are forecast to weaken over the coming year, presenting an increasingly challenging economic outlook for households and businesses.

During the first quarter of 2022, Scotland's output growth held up relatively well, growing 1% (UK 0.8%) as the economy transitioned through the Omicron wave and remaining Covid restrictions were removed. However monthly data indicates a gradual slowing in growth over this period with output falling 0.5% in April, the first fall in output since December 2021. Business survey data points to a further easing in business activity growth between April and May.

Over the period February to April 2022, Scotland's labour market has remained tight with unemployment at 3.2%, its joint lowest rate in the time series, while the payroll employee level continued to rise in May and is now 37,000 above its pre-pandemic level. Ongoing high vacancy rates however remain a key feature of the labour market with business survey data indicating that 38% of businesses were experiencing a shortage of workers in June.

Inflation has risen to 9.1% in May, the highest UK rate since 1982. The rise in inflation has been broad based with large increases in energy, fuel and food prices and continues to be exacerbated by the impacts of the war in Ukraine on global energy and commodity markets. Furthermore, latest projections from the Bank of England expect inflation to rise further later in the year to above 11%, largely as a result of rises in energy prices associated with the energy price cap.

This is presenting significant cost of living challenges for households with mean real PAYE earnings falling over the year in April. The impact on household incomes is very much reflected in Scotland's consumer sentiment indicator which has fallen sharply since the start of the year to its lowest level since March 2021 and highlights the risks to consumption growth going forward.

Business trading conditions also continue to be extremely challenging. While business survey data present some indications of improved cash reserves at an aggregate level, turnover continues to be impacted by the increased cost of materials, energy and labour, with 37% of businesses reporting that they are having to pass on increased costs to customers. Business sentiment has eased since the start of the year amid concerns that existing supply side challenges are accompanied by a fall in demand over the coming months.

Looking ahead over the next two year period, forecasters have upgraded their inflation forecasts and downgraded growth forecasts which means that the economic outlook is challenging.

Output

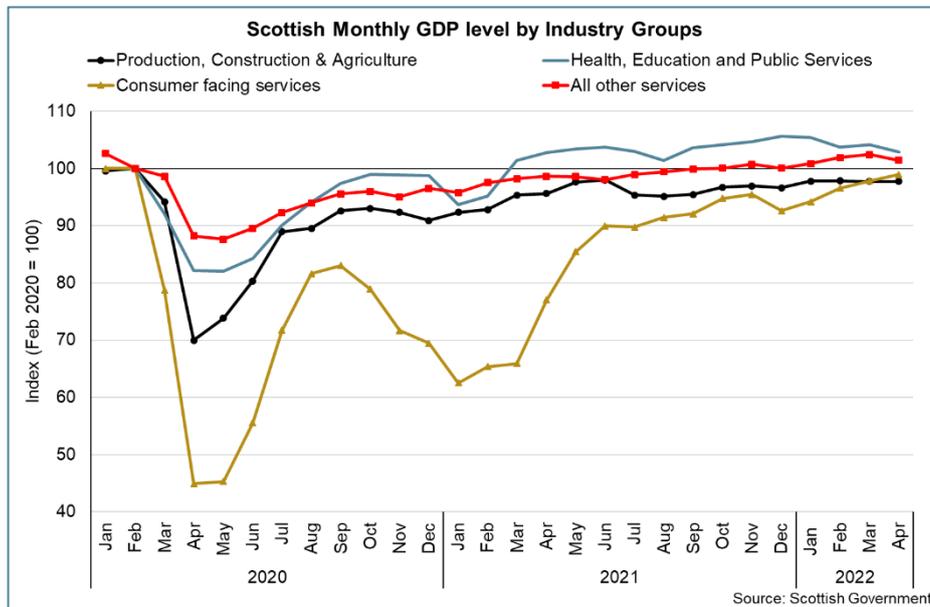
Scotland's GDP fell in April and output contracted across the UK as a whole in April.

- The start of 2022 has seen the removal of Covid restrictions from the Omicron wave as well as the remaining Covid legal requirements for businesses and services providers, while international travel restrictions for people coming to Scotland have also ended.
- In April, Scottish output fell by 0.5% (UK: -0.3%), it's first fall since December 2021, and GDP is now 0.6% above its pre-pandemic level in February 2020 (UK: 0.9%).¹



- In the three months to April, GDP is estimated to have grown by 0.8% compared to the previous three month period, with the pace of growth slowing compared to the first quarter of the year and compared to the second half of 2021 prior to the Omicron wave. This pattern of growth remains broadly in line with the UK as a whole.
- At a sectoral level, services output fell by 0.7% in April, while construction fell 0.2% and production grew by 0.1%.
- When looking at broad industry groups, within the services sector, the fall in April was driven by a fall in health, education and public services (-1.2%) and all other services (-1.0%); the latter including a 5% fall in professional, scientific & technical services. This was partially offset by growth in consumer facing services (1.1%).

¹ [GDP Monthly Estimate: April 2022 - gov.scot \(www.gov.scot\)](https://www.gov.scot/gdp-monthly-estimate-april-2022)



- Meanwhile, in the rest of the economy, output remained stable in the production, construction and agriculture group (0.0%). Within that, a significant decline over the month was noted in the manufacturing sector (-2.4%).
- Recovery in output back to pre-pandemic levels continues to vary by sector. Output in the production, construction and agriculture group remains 2.3% below its pre-pandemic level. In the services sector, despite contracting in the most recent month, the health, education and public services is 2.9% above while consumer facing services is 1.1% below its pre-pandemic level. Output in all other services was 1.4% above its pre-pandemic level.

Businesses

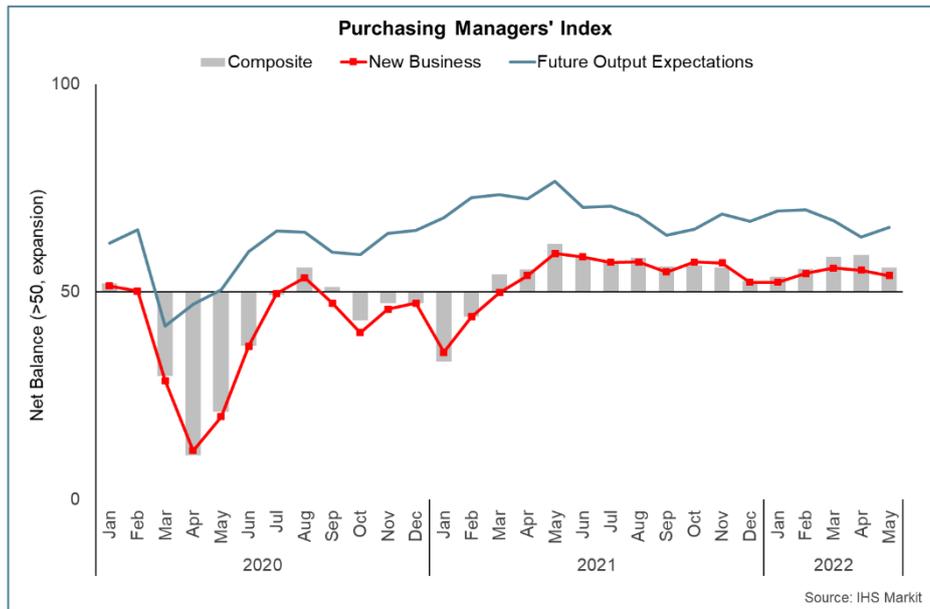
Businesses continue to face a range of supply side challenges, which coupled with the weaker outlook for demand, is weighing on growth expectations.

Business activity and expectations

- The Purchasing Managers Index (PMI) business survey signalled that Scottish business activity continued to expand in May, though at a softer rate than in March and April (55.9, down from 58.9 in April) with growth easing across both the manufacturing (50.6) and services sectors (57.1).²
- This partly reflected slower growth in new business, with inflows of new business/orders rising at the softest pace in five months, in part due to weakening demand through a renewed fall in new business for manufacturers.

² IHS Markit, RBS Purchasing Managers Index: [RBS UK regional PMI report for May 2022 | Royal Bank of Scotland](#)

- In May, Scottish business future output expectations remained positive with the composite index rising on April, however expectations have eased since the start of the year. Furthermore, flash UK PMI data for June indicated that business optimism of UK businesses fell further over the month and to its lowest level since May 2020 towards the start of the pandemic. This reflects the general weakening outlook for the economy over the coming year with businesses facing ongoing supply side challenges and inflationary pressures alongside concerns of a weakening in demand conditions from a fall in non-essential spending by households and businesses.³



Business turnover and input costs

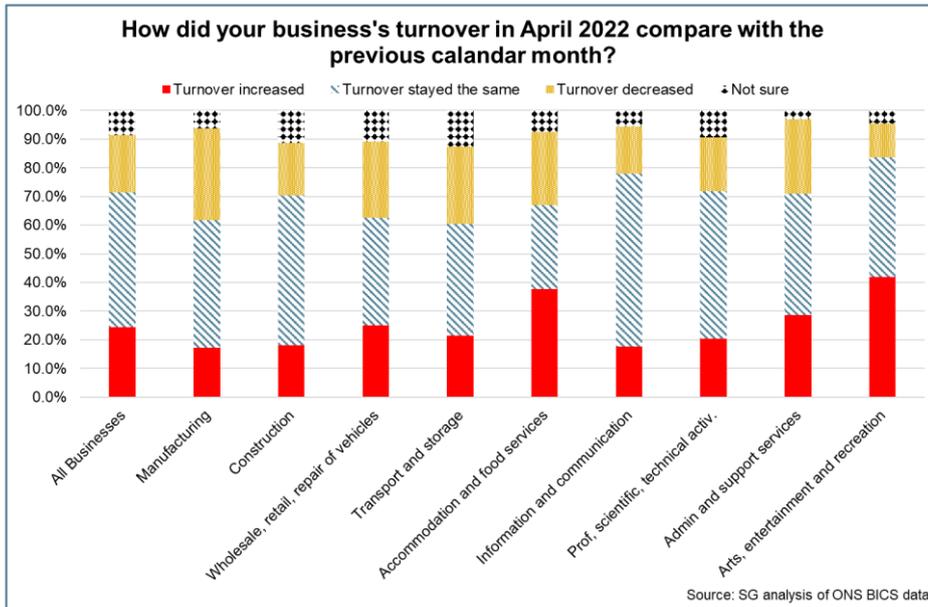
- The Business Insights and Conditions Survey (BICS)⁴ provides regular insight into business financial performance as the economy continues its recovery from the pandemic and in the face of current headwinds.
- BICS data up to the start of April indicates that at an aggregate level, business turnover has been improving as Covid restrictions on the economy have been removed with a declining share of business reporting that turnover has decreased compared to normal and a rising share reporting that turnover has increased.
- When asked how business turnover in April 2022 compares to the previous month, 24% of respondents reported that turnover had increased (down from 36% in March), 47% reported it had stayed the same (up from 46%) and 20% reported it decreased (up from 10%).⁵

³ S&P Global/CIPS, Flash UK Composite PMI:

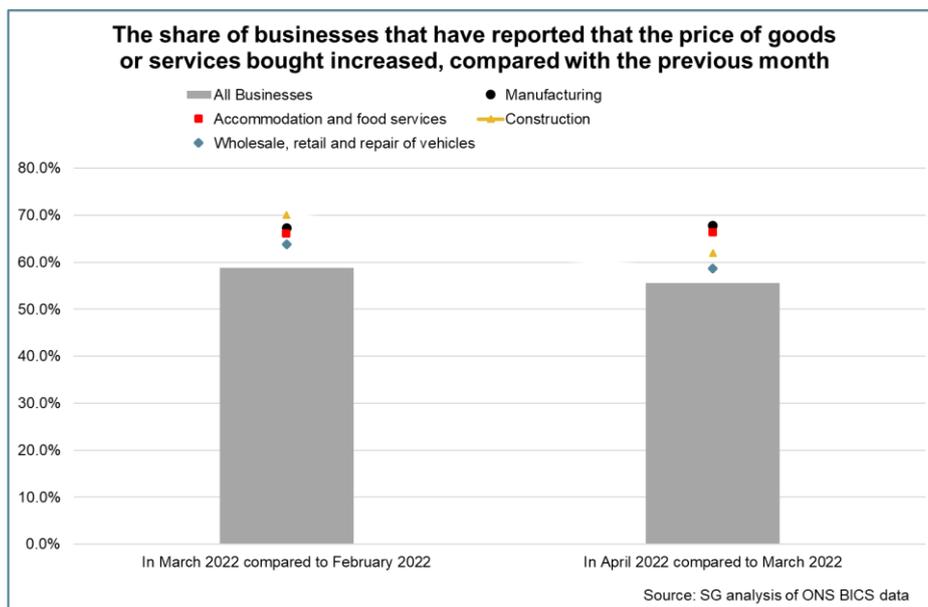
<https://www.pmi.spglobal.com/Public/Home/PressRelease/834511f716ac401a8c27e90d556d6a8c>

⁴ [https://www.gov.scot/collections/business-and-innovation-statistics/#businessinsightsandconditionssurvey\(bics\)](https://www.gov.scot/collections/business-and-innovation-statistics/#businessinsightsandconditionssurvey(bics))

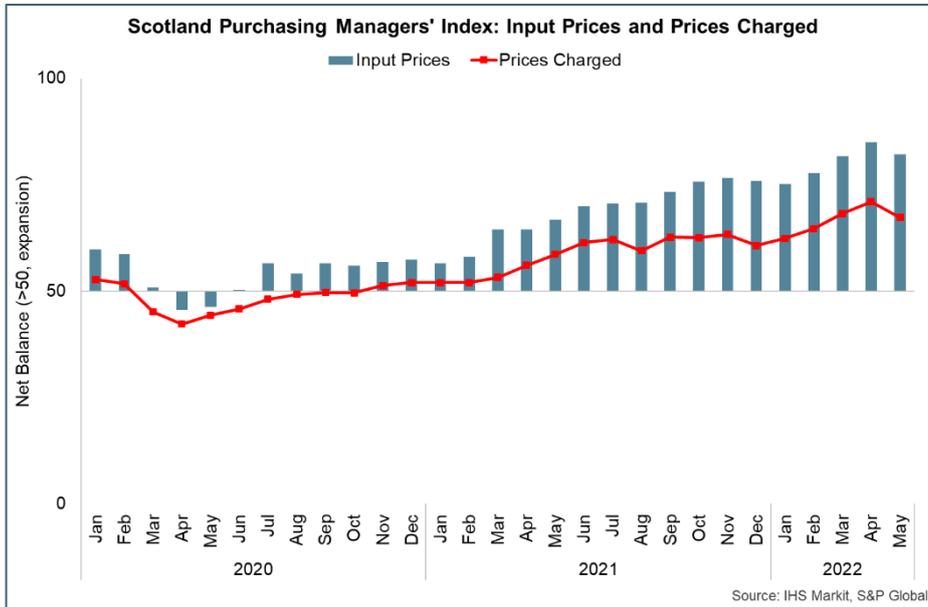
⁵ [BICS weighted Scotland estimates: data to wave 58 - gov.scot \(www.gov.scot\)](https://www.gov.scot/collections/business-and-innovation-statistics/#businessinsightsandconditionssurvey(bics))



- Parts of consumer facing services continued to have above average shares of businesses reporting a decrease in turnover (26% in the accommodation and food services sector), however, the sectors with the highest share of businesses reporting a decrease in turnover over the month were manufacturing (32%), transport and storage (27%), wholesale, retail, repair of vehicles (26%) and admin and support services (26%).
- Supply side challenges continue to be key factors impacting business activity with 36% and 28% of respondents respectively reporting that material costs and labour costs are impacting their business turnover.
- Intense input cost pressures continued in April with over half of all businesses reporting that prices had increased relative to March, (56%, down from 59% in March). Increased prices remained most widespread in manufacturing (68%), construction (62%), wholesale, retail and repair of vehicles (59%), and accommodation and food services (66%).



- In response to price rises, 50% of all businesses in May reported having to absorb costs, while 37% had to pass increased costs onto consumers. Scottish PMI data also indicated a further pass through of higher input costs to customers in May. Both the input costs indicator (82.1) and prices charged (67.3) eased back slightly from their series high levels in April, however remained elevated and reflected that firms are facing higher energy, materials and labour costs and have raised prices to offset the squeeze on margins.



- The ability of firms to absorb elements of costs has partially been supported by improving cash reserves. The BICS indicator for business cash reserves has been trending upwards since the beginning of the year, with 53% of all businesses reporting more than 6 months cash reserves at the beginning of May.

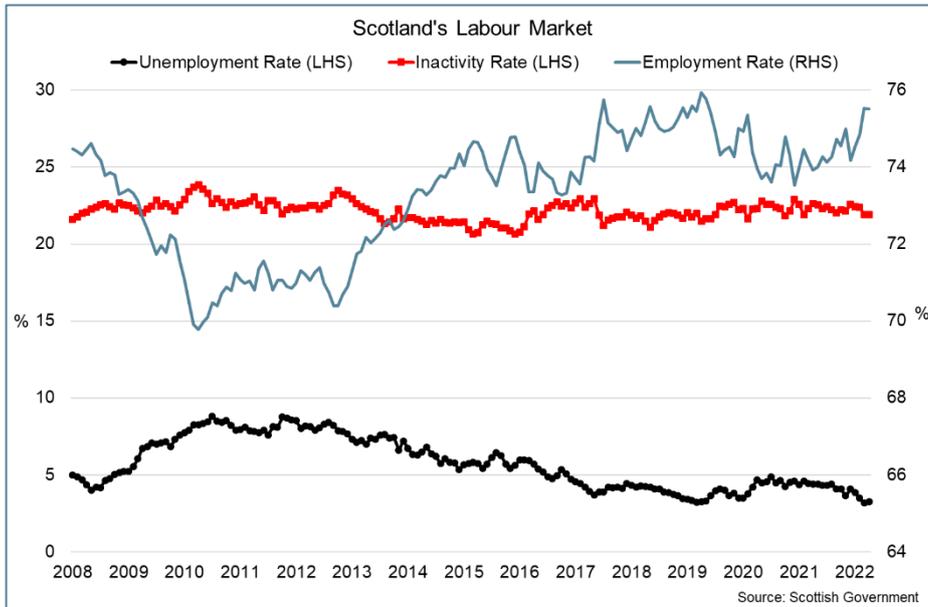
Labour Market

Scotland's labour market remains tight but there was further growth in payrolled employees in May.

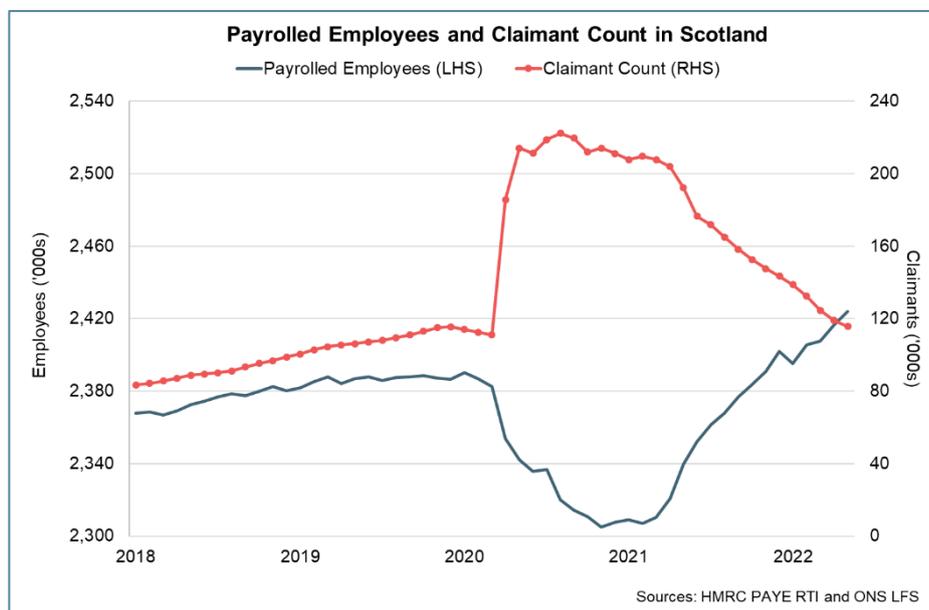
Official labour market statistics, payrolled employment and claimant count

- The latest labour market statistics for February to April 2022 in Scotland show there were 2.686 million people in employment (rate of 75.5%, up 1.6 percentage points over the year), 90,000 people unemployed (rate of 3.2%, down 1.2 percentage points) and 752,000 people economically inactive (rate of 21.9%, down 0.7 percentage points).⁶

⁶ [Labour Market Trends: June 2022 - gov.scot \(www.gov.scot\)](http://www.gov.scot)



- Pay As You Earn (PAYE) Real Time Information estimates indicate the number of payrolled employees in Scotland continued to increase in May, rising by 7,000 over the month to 2.42 million. The rate of growth over the month eased slightly to 0.3%, however remains in line with the average monthly rate of growth over the past year.
- The number of payrolled employees is now 47,000 higher than at the end of the Furlough scheme in September 2021 and 37,000 more than the pre-pandemic level in February 2020.⁷



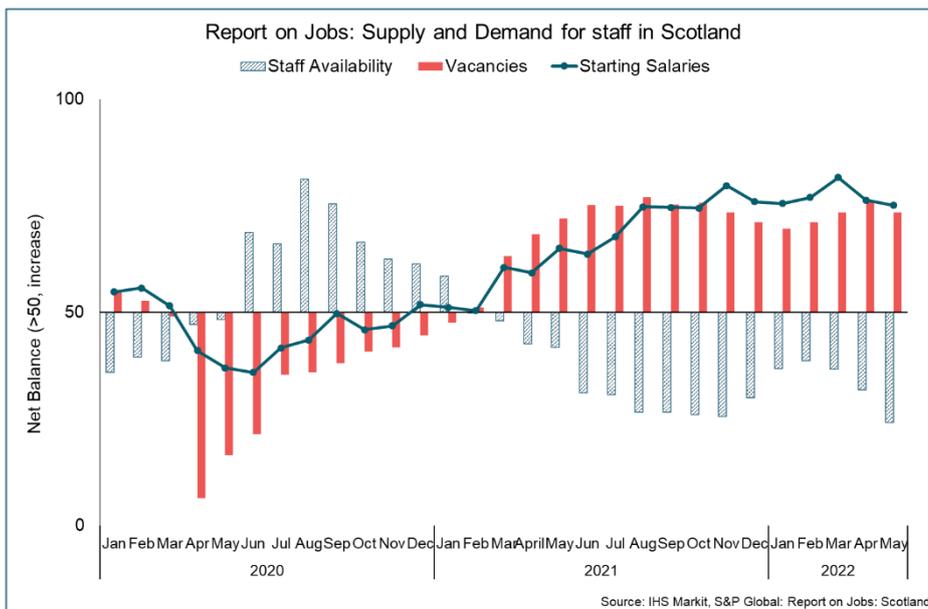
- Scotland's Claimant Count (the number of claimants of Job Seekers Allowance and claimants of Universal Credit claiming principally for the reason of being unemployed) also continued its downward trend in May, falling 2.8% over the month to 115,700; a claimant count rate of 3.8%.

⁷ [Earnings and employment from Pay As You Earn Real Time Information, UK - Office for National Statistics \(ons.gov.uk\)](https://ons.gov.uk/earnings-and-employment-from-pay-as-you-earn-real-time-information)

- Overall, the claimant count has fallen 48% from its peak in August 2020 and 26.9% since September when the furlough scheme ended. However, it remains 3,200 (2.8%) higher than its pre-pandemic level in February 2020.⁸

Demand and supply of staff

- Business surveys signalled that labour market tightness continues to persist in May with high vacancy rates and falling candidate availability.
- The latest Report on Jobs signalled that overall demand for staff (vacancies) continued to grow in May (73.4, down from 76.3 in April) and although the rate of expansion slowed over the month, it remained high compared to historical standards.⁹
- Supply side challenges in the labour market have also continued with candidate availability (labour supply) continuing to fall. The rate of contraction in May for permanent candidate availability was the fastest in the PMI time series for Scotland and faster than in the UK as a whole.



- More recent online vacancies data also signal that strong demand for staff continued throughout June, with weekly online job vacancies 34% higher than in February 2020. However, the volume of weekly online job postings fell consistently over the last month and to its lowest rate since the start of the year.¹⁰
- The strength in demand for staff, coupled with low unemployment, falls in candidate availability and challenges in recruiting the necessary staff, meant upward pressure on starting salaries

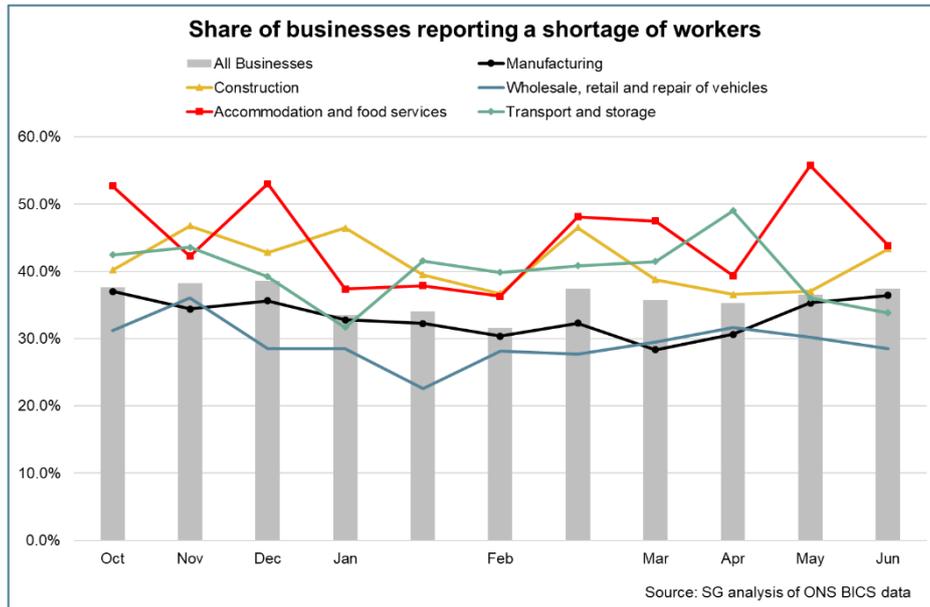
⁸ [Labour Market Trends: June 2022 - gov.scot \(www.gov.scot\)](http://www.gov.scot)

⁹ IHS Markit, S&P Global: RBS Report on Jobs for May: [0e2fba7138de425eac764302949b6c12 \(spglobal.com\)](https://www.spglobal.com)

¹⁰ [Online job advert estimates - Office for National Statistics \(ons.gov.uk\)](https://ons.gov.uk)

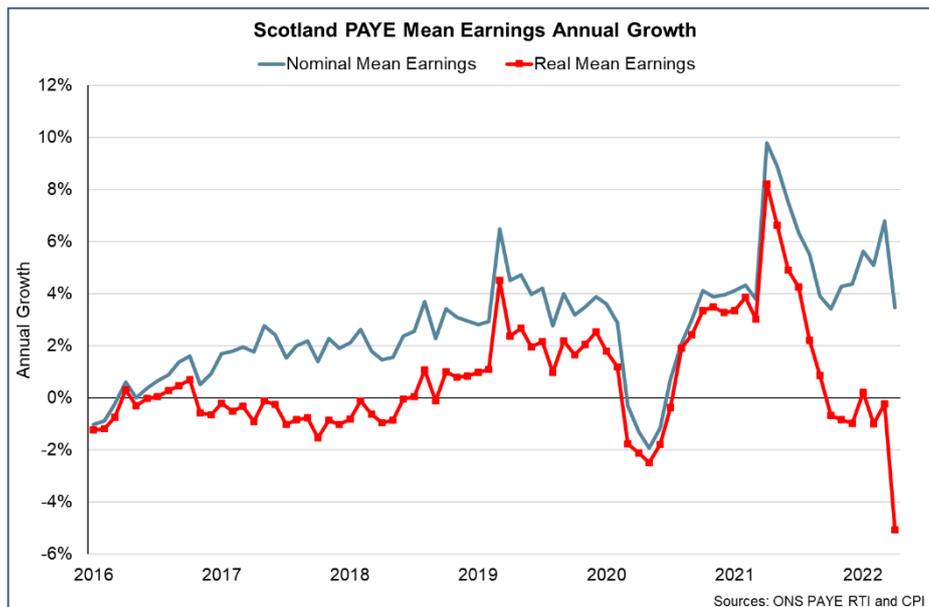
remained elevated in May, though the Report on Jobs salaries index eased back to its lowest rate since October 2021.

- Labour shortages continue to affect a range of sectors with 38% off all businesses experiencing a shortage of workers in June. The overall share has picked-up since the start of the year and remains most notable in accommodation and food services (44%), construction (43%), and the arts, entertainment and recreation (43%) sectors.¹¹



Earnings

- Nominal mean earnings annual growth has been on an upward trend since the end of the furlough scheme in September, following significant volatility during the pandemic.¹²



¹¹ [BICS weighted Scotland estimates: data to wave 58 - gov.scot \(www.gov.scot\)](https://www.gov.scot/data-to-wave-58)

¹² The rates of earnings growth during the pandemic need to be interpreted with caution as base effects, compositional factors and the furlough scheme have all influenced the data.

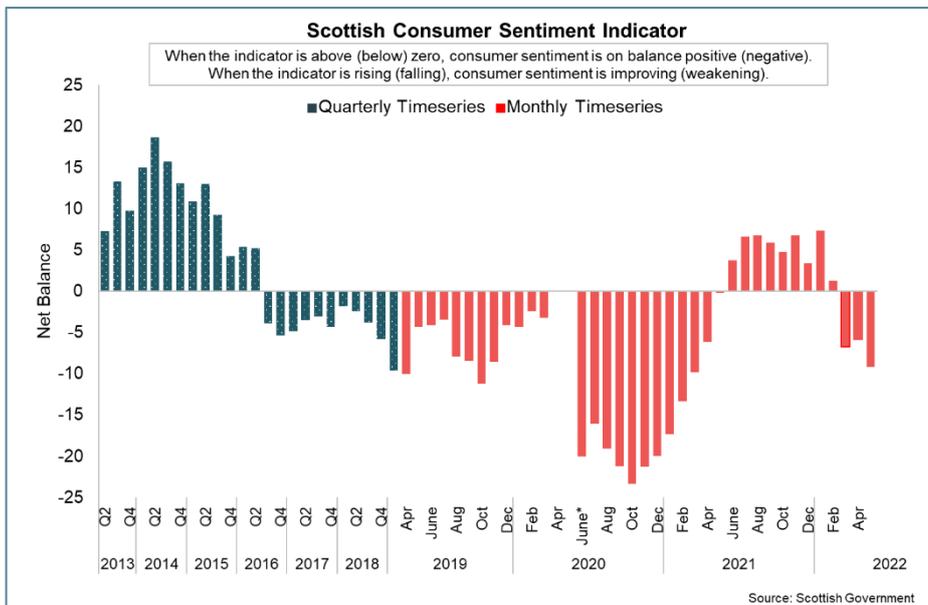
- Latest data show mean monthly nominal pay fell by 0.3% over the month in April 2022 (UK: -1.9%), and grew 3.5% (UK: 4.9%) annually to £2,596 (UK: £2,825).¹³
- The pace of annual nominal earnings growth in April was similar to annual growth rates in 2019. However, adjusting for inflation, which rose to 9% in April, real mean earnings fell 5.1% in April on an annual basis, the third consecutive month of negative annual growth.

Consumption

Consumer sentiment weakened significantly in May to its lowest level since March 2021.

Consumer sentiment

- Consumer sentiment indicators continue to be highly sensitive to the rapidly changing economic environment as the economy recovers from the pandemic while at the same time households and consumers are facing significant challenges from the sharp rise in inflation and cost of living.
- These challenges have intensified since the start of the year, which has been reflected in a sharp drop off in the Scottish Consumer Sentiment Indicator.
- Latest data show consumer sentiment declined considerably over the month from -5.9 in April to -9.1 in May. Overall, consumer sentiment has fallen 16.5 points since the start of the year and is at its lowest level since March 2021.^{14,15}

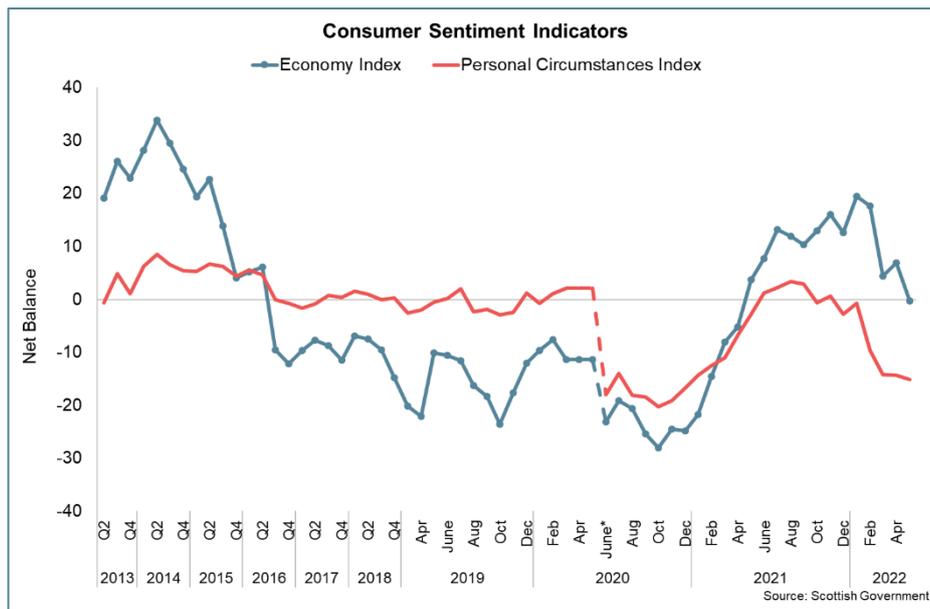


¹³ [Earnings and employment from Pay As You Earn Real Time Information, seasonally adjusted - Office for National Statistics \(ons.gov.uk\)](https://ons.gov.uk/earnings-and-employment-from-pay-as-you-earn-real-time-information-seasonally-adjusted)

¹⁴ The latest consumer sentiment survey was undertaken between 4 – 29 May 2022.

¹⁵ [Scottish Consumer Sentiment Indicator : Monthly Data - gov.scot \(www.gov.scot\)](https://www.gov.scot/scottish-consumer-sentiment-indicator-monthly-data)

- On the economy, respondents on balance consider current economic circumstances to be worse than last year (-11.8, down from -5.6 in April). Looking ahead, respondents expect the economy to improve over the coming year relative to the current situation (+11.3), although the level of optimism has been on a downward trend since July 2021 and is down significantly on April where it was 19.4.
- In terms of households personal finances, respondents on balance continued to report that their household finances are less secure than 12 months ago (-16.5, down from -13.0 in April). Looking ahead, sentiment towards expected finances remains negative (-0.1), though strengthened from -6.7 in April.
- Both the outlook for the economy and household finances influence the extent to which households are relaxed about spending money. Since the beginning of the year, households have been increasingly uneasy about spending money as inflationary and cost of living pressures have increased, with the indicator falling to -28.6 in May; its lowest level since December 2020.

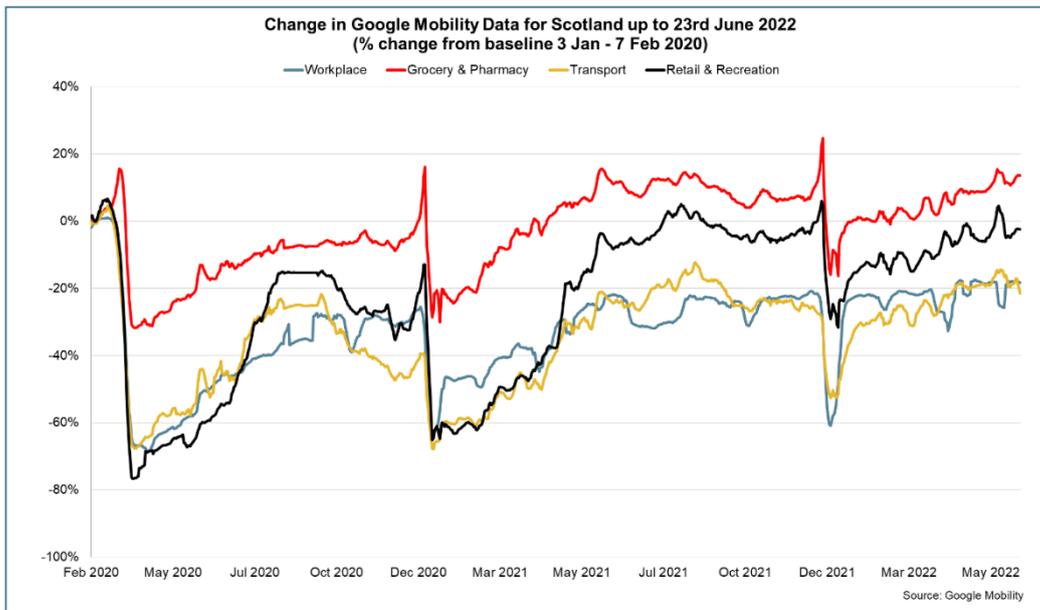


- Overall, the fall in sentiment since the start of the year has been driven by a combination of falling sentiment regarding the economy as a whole, and falling sentiment regarding personal household financial circumstances and personal relaxedness to spending money.
- This reflects the challenging economic environment households are facing and the risks to consumption growth over the months ahead.

Retail Sales and Google Mobility

- Google Mobility data indicates that movement around retail and recreation hubs is continuing to strengthen from the sharp fall in January during the Omicron wave and holiday period.

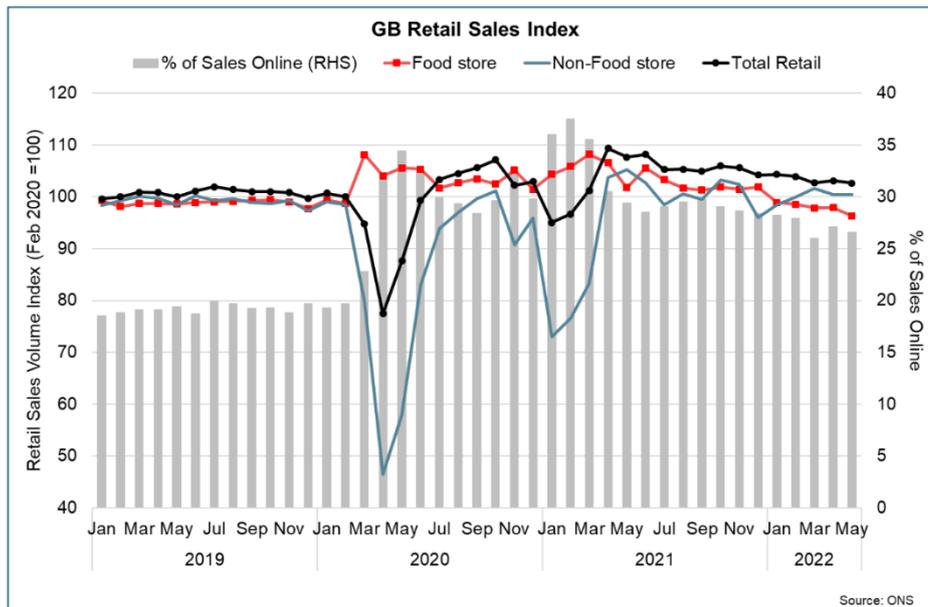
- Having fallen 30% below pre-pandemic levels in January, movement around retail and recreation hubs in June was back to around 3% below pre-pandemic levels.¹⁶



- Having remained stable across late 2021 and early 2022 (excluding holidays), visits to workplaces have marginally strengthened in recent weeks. Visits to workplaces in Scotland in the week to 23rd June were around 18% below their pre-pandemic level (compared to the average of 23% below across September 2021- April 2022, excluding holidays).
- However new working models, including hybrid working, will continue to influence the level of the visits to workplaces and use of transport indicators. Latest BICS data into June indicate that 27.4% of businesses intend to use increased homeworking as a permanent business model going forward (54.6% don't). This is particularly prevalent in the Information and Communication sector (79%) and Professional, Scientific and Technical Activities sectors (55%).
- Turning to retail, following growth of 0.4% in April, retail sales volumes fell by 0.5% in May 2022. In the three months to May, retail sales volumes fell 1.3% in comparison with the previous three months, a continuation of the downward trend since summer 2021.¹⁷
- Non-food stores sales remained stable over the month with increases in clothing (+2.2%) offset by falls in sales of household goods (-2.3%), and department stores (-1.1%). The ONS set out that feedback from retailers suggests that consumers are cutting back on spending due to increased prices and affordability concerns, however clothing likely increased over the month due to consumers planning holidays and buying new clothes.

¹⁶ Scottish Government analysis of [COVID-19 Community Mobility Reports \(google.com\)](https://www.google.com/covid19/mobility/) data published by google

¹⁷ [Retail sales, Great Britain - Office for National Statistics \(ons.gov.uk\)](https://www.ons.gov.uk/economy/retailandwholesale)

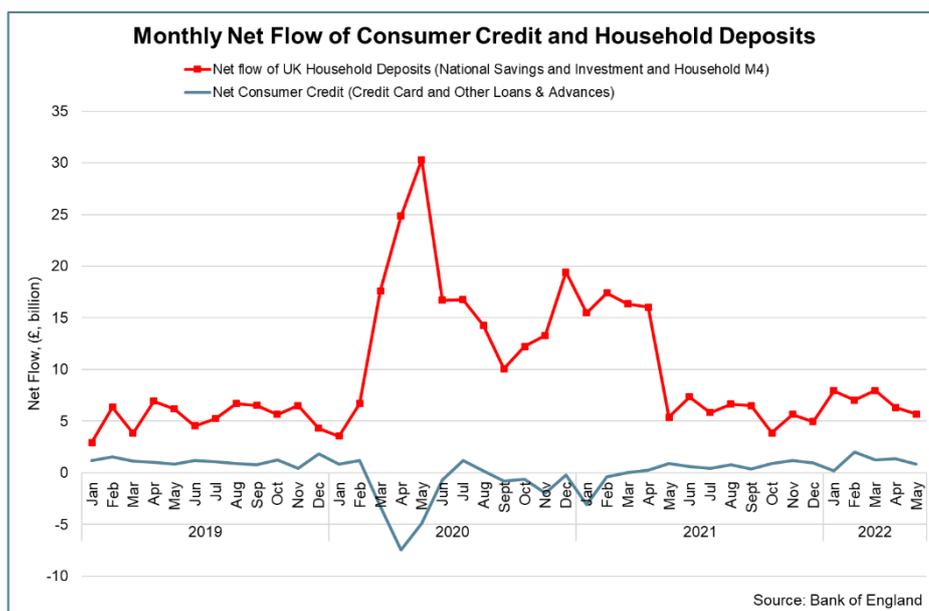


- Following growth of 2.6% in April, automotive fuel sales volumes rose by 1.1% in May. The ONS retail sales publication suggests that the strength in sales, despite rising costs, may in part be linked to the move to hybrid working and a shift away from working exclusively from home.
- Overall, retail sales have fallen 6.2% from their peak in April 2021, though remain 2.6% above their pre-pandemic level in February 2020.
- Online retail as a proportion of all retail sales, fell to 26.6% (down from 27.1% in April). This continues the wider downward trend since its peak in February 2021 (37.7%) though remains significantly higher than in February 2020 prior to the pandemic (19.7%).

Household Savings and Consumer Credit

- At an aggregate level, households increased their levels of savings during the pandemic and reduced net credit levels, due to a reduction in expenditure coupled with a rise in disposable income through the retention of earnings. More recently, saving patterns have returned to levels similar to prior to the pandemic while credit consumption has increased, particularly in the latter half of 2021 and early 2022.
- Bank of England data provides insights at an aggregate level of how savings and consumer credit flows have evolved as restrictions have been removed and economic activity has recovered alongside a rise in inflationary pressures.
- In recent months, at an aggregate level, net flows from UK households into deposit-like accounts have returned to a broadly similar position as they were prior to the pandemic. In May, net

inflows eased to £5.7 billion, down from £6.3 billion in April and in line with the pre-pandemic flows which averaged £5.6 billion in the year to February 2020.¹⁸



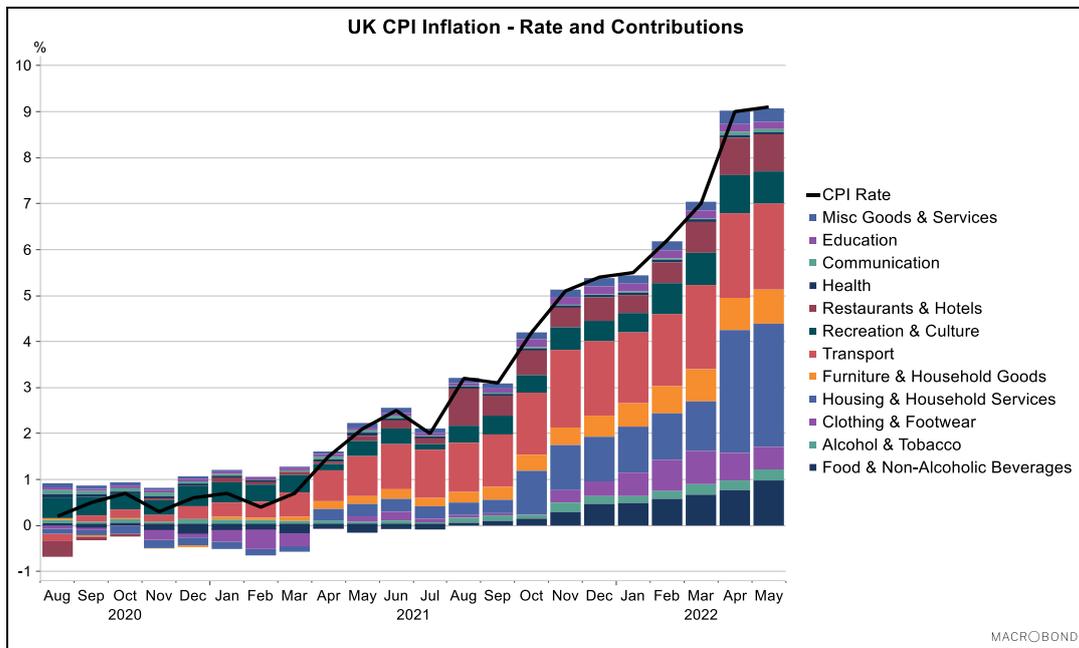
- Alongside this, net consumer credit fell significantly during the pandemic, however started to grow over the course of 2021. In May, consumers’ borrowed an additional £0.8 billion, following £1.4 billion of borrowing in April. This is slightly below the pre-pandemic average up to February 2020 of £1.0 billion.

Inflation

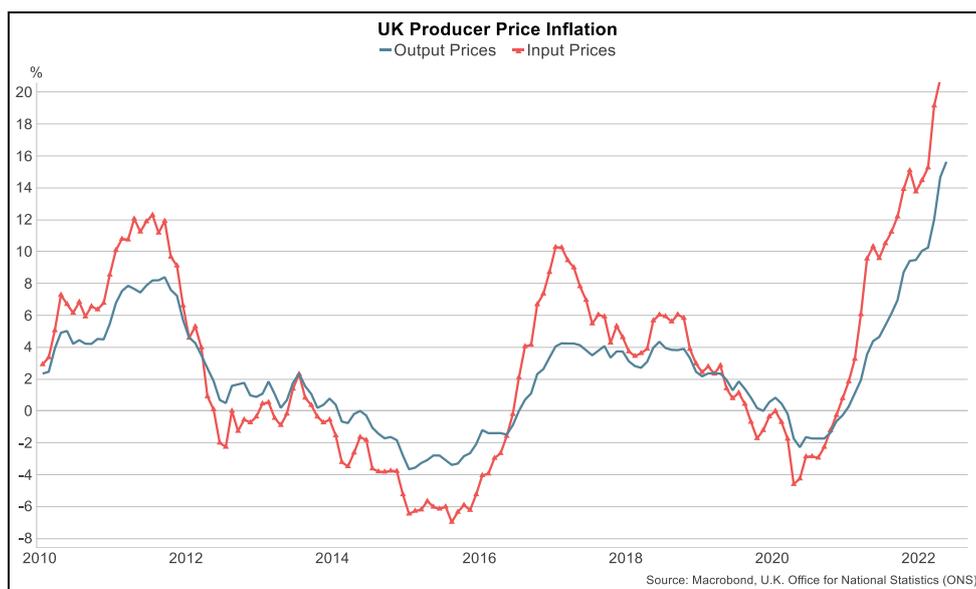
- UK CPI inflation rose to 9.1% in May 2022, up from 9.0% in April and has risen to its highest rate since 1982.¹⁹ Inflation rates have also continued to rise in the US (8.5%) and in the Eurozone (8.6%), in part reflecting rising energy prices over the past year.
- In May, UK consumer prices rose over the year across almost all goods and services monitored. Most notably there was large increases in electricity, gas and fuel prices (+69.9%), in transport (+13.8%, with large increases in motor fuels [+32.8%], second hand car prices [+23.4%] and passenger transport by air [+21.8%]) and in food and non-alcoholic beverages (+9.1%).

¹⁸ [Money and Credit - May 2022 | Bank of England](#)

¹⁹ [Consumer price inflation, UK - Office for National Statistics](#)



- Looking ahead, the Bank of England forecast inflation to rise to over 11% in October 2022, reflecting higher food, core goods and services price inflation and a prospective large increase in the Ofgem price cap, which are expected to intensify cost of living challenges.
- The pass through of higher energy and material prices from producers to consumers is an important aspect of this. Producer price inflation (changes in the prices of goods bought and sold by UK manufacturers, including price indices of materials and fuels purchased and factory gate prices) has risen over the past year and has remained elevated. In May input price inflation rose to 22.1% (up from 20.9% in April) and is at its highest rate since records began in January 1985, while output price inflation was 15.7% (up from 14.7% in April).²⁰



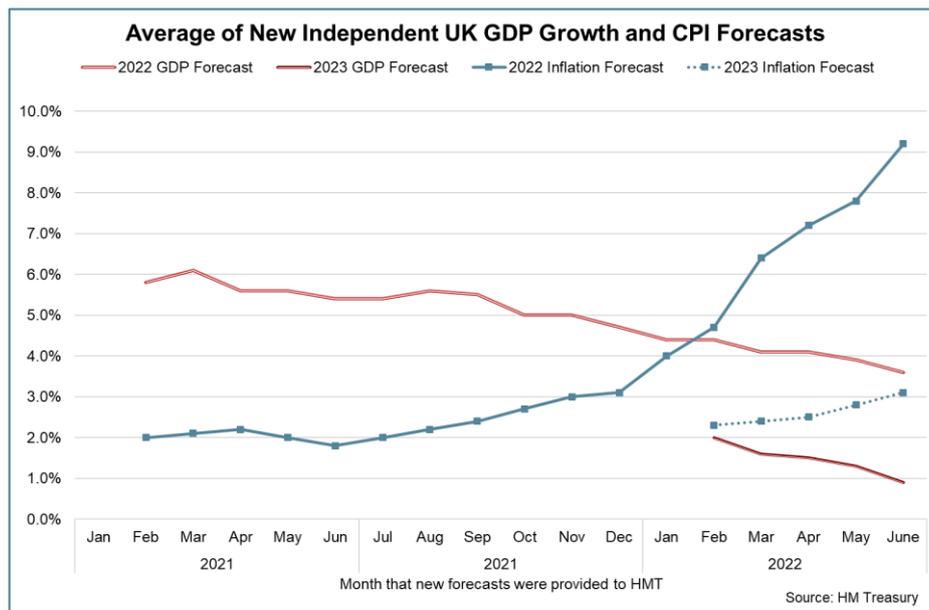
²⁰ [Producer price inflation, UK - Office for National Statistics \(ons.gov.uk\)](https://ons.gov.uk/producer-price-inflation)

- In response to the further rise in underlying inflationary pressures for the year ahead, the Bank of England's Monetary Policy Committee (MPC) increased the Bank Rate by 0.25 percentage points to 1.25% in June; its fifth consecutive rate rise since December and up from 0.1% over this period.²¹

Economic outlook

Latest output growth forecasts continue to be revised down as the inflationary outlook continues to sharpen.

- At a global and domestic level, the economic outlook has weakened significantly since the start of the year as rising inflationary pressures, exacerbated by the war in Ukraine, are expected to weigh on the GDP growth outlook over this year and next.
- At a global level, in June, the OECD revised down their GDP growth projections for 2022 and 2023 with global GDP growth of 3% forecast for 2022 (down from 4.5% forecast in December) and 2.8% in 2023 (revised down from 3.2%). Inflation projections have been revised up with inflation in OECD countries projected to reach 8.8% in 2022 (revised up from 4.5%), easing to 6.15 in 2023, resulting in intensifying cost of living challenges across countries.²²
- At a UK level, the average of new independent forecasts in June (published monthly by HMT) highlights the combination of the upgrades to inflation forecasts and downgrades to growth forecasts. UK GDP is forecast to grow 3.6% in 2022 (down 0.3 percentage points [p.p] over the month) and 0.9% in 2023 (down 0.4 p.p over the month).²³



²¹ [Bank Rate increased to 1.25% - June 2022 | Bank of England](#)

²² [OECD Economic Outlook](#)

²³ [Forecasts for the UK economy - GOV.UK \(www.gov.uk\)](#)

- In contrast, the average independent projected CPI inflation rates have been revised up to 9.2% in Q4 2022 (up 1.4 p.p over the month) and 3.1% in Q4 2023 (up 0.3 p.p). This points to current expectations that as inflation will potentially peak at the end of this year and start to ease back over 2023, the GDP growth outlook for 2023 and 2024 is notably weaker than for 2022. For example, the Bank of England project inflation to rise above 11% in October 2022 and for UK GDP growth to ease from 3.75% in 2022 to around -0.25% growth in 2023 and 0.25% growth in 2024. Similarly the OECD forecast UK growth to remain flat in 2023.
- Forecasts for Scotland's economy have followed a similar pattern. The most recent Scottish Fiscal Commission (SFC) forecasts in May forecast Scotland's economy to grow 4% in 2022, slowing to 1% in 2023. The SFC forecast CPI inflation to peak at 8.7% in Q4 2022 and forecast real average earnings to decrease by 2.7% in 2022-2023.²⁴
- Most recently in June, the Fraser of Allander Institute forecast Scottish GDP growth in 2022 of 3.8%, however in the face of higher and more persistent inflation, have revised down the growth outlook for 2023 to 0.5% (previously 1.5%) and for 2024 to 1% (previously 1.4%).²⁵

²⁴ [Scotland's Economic and Fiscal Forecasts – May 2022 | Scottish Fiscal Commission](#)

²⁵ <https://fraserofallander.org/publications/fai-economic-commentary-2022-q2/>



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