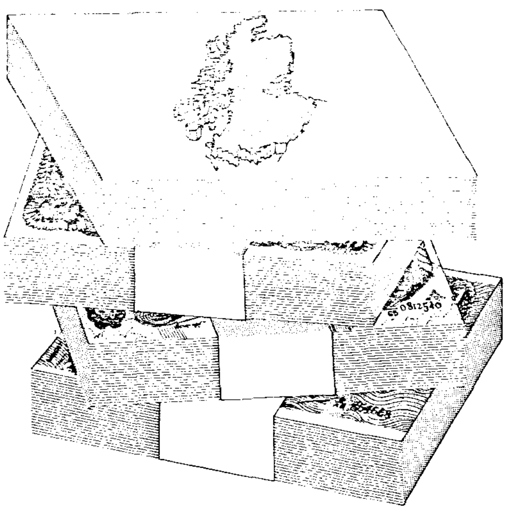
Industrial Performance



BUSINESS SURVEYS

With the inauguration of the quarterly **Scottish Business Survey** (SBS) in September 1984 there are now two regular up-to-date indicators of trends in the Scottish industrial sector. The combination of the new survey and the long-standing CBI **Industrial Trends Survey** provides a comprehensive assessment of trends in Scottish industry. The two data sources are essentially complementary, but there are important differences between them. While the **CBI Survey** provides information on trends by size of firm, the **Scottish Business Survey** provides a geographical breakdown of responses. Equally, the CBI provides information on sectoral employment trends, while the SBS distinguishes between male and female employment, and in some sectors between full-and part-timers. In addition, the number of respondents to the SBS is well over twice that to the CBI survey, and they cover not only manufacturing but also construction, distribution and financial institutions. The results from the new SBS are therefore capable of a greater degree of disaggregation than those from the CBI.

The results of the two surveys are first considered separately and their combined verdict on Scottish manufacturing trends is then summarised. Both surveys were conducted against a backdrop of a weakening of sterling's exchange rate against major European currencies and a strengthening of sterling against the dollar. The period since the last surveys was one in which nominal interest rates fell by 1.5%. The latest reduction which occurred on 18 April came after the closing date for both surveys so it will not have affected the replies of respondents. Most strikingly, the period was one in which oil prices declined steeply and this is bound to have had some influence on the results.

SCOTTISH BUSINESS SURVEY RESULTS

The SBS for April 1986 indicates that business optimism is continuing to improve. This reaffirms the strengthening of optimism which was observed in the January survey. For all manufacturing, a positive balance of 3% of respondents are more optimistic about their general business situation. In service activities too the outlook is generally bullish. Retail distribution and financial sectors both expect further improvements in their trading position, whilst the pessimistic outlook reported for respondents in wholesale distribution in the January SBS has been reversed, with a positive balance of 9% of respondents now viewing their prospects more favourably. Only in the construction sector does business optimism remain at a low ebb: the balance of respondents reporting reduced optimism

(4%) remains at the same level it was in the January SBS.

The expectation of an increase in the volume of orders for manufacturing in the first quarter of 1986 was realised. A balance of 10% of respondents reported an upward trend in orders over the period with growth in external orders in the rest of the United Kingdom and the rest of the world more than offsetting depressed orders within Scotland. Respondents expect this growth in orders to be maintained in the next three months. Trends reported for manufacturing sales follow closely those for orders.

Despite these improvements, capacity utilisation in manufacturing remains low by historical standards. On average, it is estimated that only 54% of capacity was in use over the three months to the end of March 1986. With virtually all new investment being motivated by either the need to replace machinery or to improve efficiency, the bleak prospects for employment shows no sign of abatement. In the next three months a negative balance of 13% of respondents expect to reduce their numbers in employment. Until such time as growth in demand for manufacturing output outstrips productivity growth retrenchment in manufacturing employment will continue.

Across the spectrum of manufacturing activity conditions are generally reported as being more buoyant in light manufacturing than in the older, more traditional industries. Chemicals, electrical and electronic engineering, food, drink and tobacco, paper and printing and miscellaneous manufacturing all record a positive balance of respondents who view their general business situation more favourably in the coming quarter. On the other hand, metals, mechnical engineering and other engineering respondents are all less sanguine about their general business situation. Whilst short-run factors will have undoubtedly influenced these responses, they also appear to reflect the nature of the more fundamental restructuring of economic activity which has been apparent now in Scotland for a decade. There is little indication that these trends can be reversed in the near future.

Recent SBS findings have consistently shown Textiles as enjoying an expansion of activity. Textiles is perhaps the only sector in which this expansion has percolated through to increases in employment and capacity expansion. It should be appreciated that the ascendancy of textiles in the past two years came only after a considerable restructuring of activity there. The April 1986 SBS findings are notable, therefore, because they suggest that optimism in the textiles sector may be waning. A large negative balance of 20% of respondents view their general business situation less favourably now than they did three months ago.

Inspection of the expected trends in orders and sales in the textiles sector and comparison of these trends with trends for the previous three months gives little clue as to why optimism has slackened so noticeably. If anything, orderbooks have expanded and only 8% of respondents expect a reduction in their sales in the coming three months. All other respondents expect sales to be maintained or improved. If it were not for the fact that expected employment looks set to fall in the next three months (a balance of 6% of respondents expect a downward trend) one might conclude that the indicator of general business confidence is aberrant.

One possible explanation for the reduced optimism in the sector is that it is being measured from an extremely high baseline. Over the past three months capacity utilisation in the sector has averaged 92%. Furthermore, there is some evidence that stocks of finished goods which have been accumulated over previous quarters now look set to be run down. If orders are to be met from existing stocks a slowdown would be expected in the rate of growth of activity levels and employment. The replies of respondents in the textiles sector are certainly consistent with this interpretation and with little indication of stocks of work in progress expanding it may be that the textiles sector is about to experience some retrenthment. The returns for the textiles sector will be monitored closely in the next quarter's SBS to see whether or not these indications of a slackening of growth are borne out.

The returns for other sectors in manufacturing will now be descsribed briefly. The growth in orders expected by respondents in the electronics sector reported in the last SBS is substantiated by the actual growth in orders experienced by these respondents over the last three months. This growth together with expectations of a further growth in orders, is of a sufficiently large magnitude that respondents also report actual and prospective increases in numbers employed. Noticeably, it is male employment which dominates the gains with female employment actually appearing to have fallen (a balance of 10% report a downward trend) over the last three months.

The setback in optimism experience by chemicals and food sectors in the last quarter of 1985 is reversed in the latest SBS. In chemicals 5% of respondents are more optimistic whilst in food, drink and tobacco 15% of respondents are more optimistic. This general trend is mirrored in the trend of orders. A balance of respondents in both sectors report a reduction in orders over the past three months but they are also confident that order books will expand in the coming quarter. The prospective expansion of orders in chemicals is sufficient to induce the respondents to believe that it will spillover into employment. A balance of 10% expect employment to increase in the next three months. In food, drink and tobacco, however, it appears that labour shedding is set to continue.

Those sectors where the outlook is most bearish are also those sectors where capacity utilisation has been at its lowest in the previous three months. In this respect, there has been little change over the findings reported in the last SBS. Capacity utilisation in metal manufacture and metal goods fell from 40% to 35% and in mechanical engineering a fall of 4% is recorded, from 30% to 26%. For the other engineering industries an expansion in capacity utilisation is recorded (from 28% to 37%) but nonetheless these figures provide little hope of a sustained recovery in the sector.

The position of the paper and printing and miscellaneous manufacturing sectors is much the same as previously. Both sets of respondents are more optimistic; both expect an expansion of orders and both expect to authorise more investment expenditure. Whilst previous gains in employment in other manufacturing are expected to be repeated, there is little prospect of employment growth in paper and printing, an industry in which the introduction of labour-saving technologies has been especially significant.

In summary, the SBS of April 1986 suggests that the growth in orders which has been experienced by manufacturing in recent months looks set to continue. For some sectors this growth has been of sufficiently large order to have stimulated actual and prospective employment but, on balance, manufacturing employment seems certain to slip further in the coming months. Elsewhere in the economy, service activity continued to show signs of expansion but construction activity remains, as before, very much depressed.

CBI SURVEY

The results of the April CBI survey for Scotland stand in marked contrast to those of the SBS. The strengthening of business optimism reported in the SBS is not echoed in the CBI findings which show a weakening of business optimism, with a negative balance of 5% of respondents being less optimistic about the general business situation in their industry. Underlying this depressed outlook is the expectation that orders books and output are likely to improve only marginally, if at all, over the next four months. In the SBS survey, the corresponding indicators suggest an unambiguous expansion of activity. There are, however, some similarities in the findings of the two surveys. Both concur that employment opportunities are likely to be further curtailed and that investment is motivated primarily by the desire either to replace worn out or obsolete equipment and/or to improve efficiency. They only bright note in the CBI survey is that export orders and deliveries look set to continue their recent expansion.

Not only do the CBI survey findings disagree with those of the SBS but they also suggest that respondents expectations, as reported in their January survey, have not been fulfilled. For example, in the January survey, a **positive** balance of 17% or respondents expected an increase in orders in the coming four months. The April survey reports, however, that a negative balance of 17% of respondents experienced a downward trend in the volume of new orders. Expectations of an expansion in output reported in the January survey also do not appear to have been realised by April, with a balance of 4% reporting a falling trend in output.

At the sectoral level, the CBI survey endorses the SBS findings for the textiles sector. Pessimistic expectations are underlined by a prospective contraction in orders, investment and employment. This confirms the trend which was predicted in the January CBI survey. Similarly, there appears to be broad agreement betwen the two sets of survey returns about actual and expected conditions in metal and engineering activities. Like the SBS, the CBI survey suggest firms here are unambiguously despondent about their general business situation. Only for the chemicals sector are the results of the CBI and SBS in conflict. The CBI survey reports depressed orders, output, investment and employment but suggests that orders are expected to pick up in the next four months. The SBS also reports that conditions were depressed in the first quarter of 1986 but indicates that a much stronger revival in activity will take place, so much so that the SBS expects employment to expand in the sector.

The overall CBI findings are heavily weighted by those of firms employing 500 or more employees. For these large firms the outlook appears to be very bleak indeed. Medium-sized and small firms, however, appear to be enjoying far more favourable business conditions and firms in these size classes are also more sanguine about their prospective business conditions. It is probable that to some extent these contrasts in response reflect differences in the economic fortunes of different sectors. Large firms, in terms of numbers employed, are typically found in traditional manufacturing activities such as metals and engineering. Smaller firms are usually engaged in lighter manufacturing activities.

It is possible that the differences in findings of SBS and CBI surveys reflect the large weight given to large firms in the CBI survey. Whilst large firms are, by virtue of the greater numbers they employ also given larger weight in the SBS it would appear that their effects on the overall manufacturing response is diluted by the very much larger sample size in the SBS survey. This larger sample size has the effect of giving greater weight to smaller and medium-sized companies than in the CBI survey.

AGRICULTURE

Agricultural surpluses are now a world-wide phenomenon. The closing of traditional grain markets such as India and China, coupled with expected increases in US farm exports, (encouraged by the new US Farm Bill and falling dollar), induced a further decline in the world market prices of many agricultural commodities. This will place still greater strain on European farmers and taxpayers, without much corresponding benefit to European consumers. Last year, the CAP failed to maintain our farm incomes (down 6% on average throughout Europe), failed to reduce its stocks of surplus products, and at the same time exhausted its budget.

Nevertheless, it seems certain that the European Commission will continue with its policy of cutting intervention prices paid to farmers in an attempt to reduce surpluses and diminish its expenditures. This policy can be expected to hit most severely the incomes of marginal farmers, and, in European terms, most of Scottish agriculture is marginal. This is so, not because of the size of the holdings or because of the skills or efforts of the farmers: it is because of the nature of the land and of the climate. If the tripartite objectives of European farm policy are to be achieved, then income maintenance expenditures must be separated from policies which are designed to balance market supply and demand. The kinds of policies required are illustrated by the deficiency payment schemes and capital grants schemes which operated before the UK joined the Community, and by such measures as the £38 million agricultural development programme of the Scottish Islands recently approved in principle by the Council of Ministers.

Although they share a common interest with many marginal farmers in Germany and in France (better land but smaller holdings), Scottish farmers are effectively without a political voice in Europe, since the British Government's view, promoted by Agriculture Minister Jopling is ~~wholeheartedly in~~ favour ~~of~~ price-cutting, and only price-cutting. ~~This~~ suits the very different farming conditions in the South of England. Much has been said to farmers ~~about the~~ need to respond to falling product prices by lowering their costs of production and improving the quality of their product. The fact is that most farmers have little influence over any of their important costs, and that the potential for further increases in productivity is now limited. Scotland is indeed well-placed to specialise in high quality products - indeed this has been the basis of much of its agricultural exports in the past. Scottish farmers do seem to have grasped the added significance which marketing has taken on in the new circumstances. The success of SQBLA in promoting sales of beef and lamb is an example. All these kinds of developments are indeed within the scope of farmers' self-help. However, much more fundamental changes are required if the destruction of the Scottish agricultural industry ~~is~~ to be avoided. And these changes require government initiative to bring them about.

~~The first~~ such change has already been mentioned - the need for an income maintenance scheme separate from the commodity price system. Secondly, there is a need for diversification into afforestation, tourism, conservation and other complementary land-use activities. Thirdly, there is the question of land-tenure. There is some evidence that the present system inhibits the changes which are needed to respond to continuously falling prices. It may be that security of tenure for tenant-farmers has outlived its usefulness. It can become an obstacle to change, can lead to unenterprising farming, and can create a new class of privileged heritors. On the other hand, those farmers who own the land they occupy find that most of their capital is tied up in an asset whose value is not directly related to its ~~product~~. Realising the value of the land, and injecting the money into the enterprise might yield a higher return.

Income maintenance, land use, and land tenure, are essential ingredients of any strategy for agriculture. Only the Government can take the initiative in bringing about necessary changes in these areas. Last month, Lord Gray, Minister of State at the Scottish Office, brushed aside the request of the NFUS for a new strategy for the countryside. In doing so, he illustrated once again that British agricultural policy under the present Government remains quite unmoved by Scottish farming interests.

FISHING

The total value of fish landed in Scotland by British and foreign vessels during 1985 was almost £220m (see Table 1.1) which represents an increase of more than 11% on 1984 figures. The total weight landed increased by a similar figure over the same period to over 610,000 metric tonnes. Trends varied according to species. For the demersal species, which accounted for 68% of the total value of landings, the 1985 figure represents only a 3% increase in quantity and an 8% increase in value. The value of shellfish landed, on the other hand, increased by 20% whilst quantity rose by only 5%. Finally, the figures for the pelagic species show an increase in volume and value in the region of 21%.

Table 1.1 Landings of fish at Scottish ports by British and foreign vessels

	Demersal	Pelagic	Shellfish	Total
Value of landings 1985 (£m)	148.9	29.8	40.4	219.1
% of total	68	14	18	
Increase over 1984 (%)	8	21	20	11
Quantity ('000 metric tonnes)	297.3	276.8	36.2	610.3
% of total	4.9	4.5	6	
Increase over 1984 %	3	21	5	11

Source: Department of Agriculture and Fisheries for Scotland

It was announced in March that the fish farming industry would in future be subject to more formal planning controls. The Crown Estate Commissioners, who have responsibility for the management of most areas of foreshore and seabed areas within territorial waters, announced the introduction of new consultative procedures designed to allow all interested parties to comment on any proposed development. This would allow an input from, amongst others, local environmental and conservation groups. It is also intended to limit the ability of the larger farming companies to acquire leases on land that they subsequently chose not to develop, by requiring that development on leased land must take place within a specific time period. It is hoped that this will improve the access to sites of smaller fish farming concerns.

The Scottish Fishermans' Federation has made a renewed attempt to secure Government compensation for loss of access caused by oil-related developments. They argue that compensation should be provided for both temporary and permanent loss of access. This approach is the first since a similar proposal was rejected by the Government in 1978.

CONSTRUCTION

Total activity in the construction industry in 1985 remained virtually the same as 1984. There was, however, a further shift away from public sector work into the private sector. Department of the Environment statistics record that the nominal value of new orers received from the public sector in Scotland rose by only 2.9% in 1985. This was effectively a real fall. In contrast new orders from the private sector rose by 11.9%.

The latest **Scottish Business Survey** indicates that this trend has continued into the first quarter of 1986. Considerably more respondents had suffered a reduction in orders from the public sector than the reverse. Orders from the private sector apparently remained static. The respondents to the survey were, however, more optimistic about future demand from the public sector. Their optimism is perhaps derived from the recent statement by Michael Ancram, Minister for the Environment at the Scottish Office, in which he announced that Scottish local authorities may spend £441.5m on housing capital projects in 1986/7. This amounts to a 14.5% increase over the previous year. For the first time councils will be allowed to carry forward any capital allowance left from last year, up to a maximum of 3.5% of this year's allocation. Within this total allocation the Scottish Office have allowed councils' capital spending on their own housing stock to rise by 16.9%. Council grants for improvements and repairs in the private sector have only been allowed an increase of 8.7%.

Although private sector construction in Scotland has been growing faster than public sector construction , the former appears to be lagging behind the rest of the UK. More than one indicator confirms this. The National House-Building Council (NHBC) recorded a 5.5% increase in the number of private dwellings started in 1985 in England and Wales. In Scotland the number of new starts in 1985 was 1% lower than in 1984. This trend has continued in the first quarter of 1986. In this quarter new starts in England rose by 2.7%, whereas in Scotland and Wales the number of starts remained the same as in the last quarter of 1985. In 1985 all areas of England and Wales recorded an increased turnover in builders merchants' sales, and sales throughout Britain increased by 9.6%. In contrast sales in Scotland were down by 4.3%. This difference in activity shows up clearly in the index for construction. In the third quarter of 1985 the Scottish index fell by 4.2 points, whereas the UK index declined by only 0.9 points.

Construction demand from the private sector is unlikely to improve in the near future. Demand from industry will be hit hard by two events. The fall in oil prices has already precipitated a severe cut-back in oil companies' exploration and development plans. This will soon hit the oil-related construction industry. Secondly, capital allowances for expenditure on industrial buildings were reduced from 50% in 1984 to nil from 1 April this year. The phasing out of this allowance will have encouraged many firms to bring forward plans for new buildings. We can therefore expect industrial construction to remain depressed in the foreseeable future.

ENERGY: OIL AND GAS

The oil and gas scene over the past few months has been dominated by the precipitous fall in crude oil prices. Faced by the continuing inability of OPEC members to agree on production cuts coupled with the expectation of slackening demand as the industrialised countries move into milder summer weather, the market drove the price of Brent crude below $10pb at one point before recovering to present levels of around $13-14pb. The prospect of oil prices falling below $10pb and remaining there is still taken seriously by many experts. Given that only six months ago crude was selling at $30pb, the sterling exchange rate is holding up remarkably well. Furthermore, the Chancellor seems to have been able to accommodate losses in oil tax revenues in his budgetary plans. Since UK non-oil related exporters should benefit from lower fuel and transport costs and increased foreign demand, it cannot be said that, in macroeconomic terms, the recent fall in oil price is necessarily 'bad' for the UK.

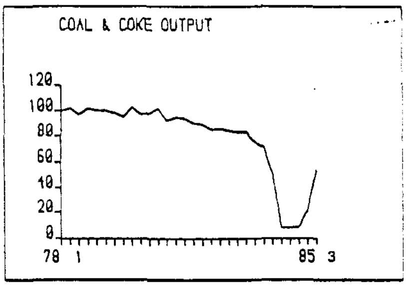
Whatever the net effects on the economy as a whole, low oil prices will adversely affect the rate of exploration and development in the North Sea, which, in turn, will adversely affect activity in the offshore supplies industry. Since this latter industry is concentrated in Scotland, any negative impact arising from a downturn in offshore-related activity will be felt disproportionately highly in the Scottish economy.

Already, it is becoming clear that oil operators are making downward revisions to their plans for exploration and development projects in the North Sea. In March, Britoil announced it was cutting £100 million from its exploration budget for 1986 and was shedding 250 white-collar jobs. Burmah also announced a halving of its exploration budget and the probable closure of its Aberdeen office. Shell/Esso, in April, abandoned plans to undertake a £2 billion development of the Gannet field complex and it appears that some operators are reluctant to fulfill their ninth-round drilling commitments.

However, even at current low crude oil prices some new North Sea projects will remain attractive. For example, Shell recently awarded a £52 million fabrication order to RGC Offshore for the Tern field platform. Redpath Engineering was awarded a £16 million contract to build an accommodation module for the same platform.

Latest figures from the Industry Department for Scotland indicate that in December 1985 there were almost 64,000 workers in Scotland wholly associated with North Sea oil, of which 80% were registered as employed in Grampian region. In view of the preceding discussion, clearly a significant fraction of these jobs could be at risk if the period of low oil prices is prolonged, and the effects on the Grampian economy could be particularly severe.

ENERGY: COAL, ELECTRICITY AND WATER



The index of industrial production for coal and coke in Scotland reached 66 in the third quarter of 1985. Although this is some way below 1980's base production level of 100 it is only 5 points short of the 1983 4th quarter and is swiftly approaching the pre-miners' strike figure of around 83. In the other energy and water supply industry the index jumped by 8% over the previous quarter to stand at 126 in the third quarter of 1985. This compared with the 129 figure for the UK as a whole (representing a 1% fall on the previous figure).

Events in the energy sector worldwide have displayed yet again the weakness of the Government's position on energy policy. Despite the fact that the coal industry has been performing extremely well since the end of the miners' dispute the fall in oil prices again seems to have brought pressure on the NCB to rationalise and cut costs. In effect, this means closure of some of the least efficient pits currently in production. The Scottish area is the second highest cost coalfield in the country, after South Wales, and as such is obviously in a very vulnerable position. This pressure from oil prices is exacerbated by the existence of cheap coal imports (not least caused by the appreciation of the sterling:dollar exchange rate). Imports of coal could be purchased at up to 30% below NCB prices by the CEGB and even with transport costs included imports have a 10% cost advantage.

The drop in oil prices is, however, the biggest immediate threat to the industry. With crude oil prices currently below $15 per barrel the existing pricing deals between the two main UK electricity generating boards, the two main UK electricity generating boards, CEGB and the SSEB, and the National Coal Board mean that coal is uncompetitive ie it would suit the electricity boards to bring on-stream their mothballed oil-fired generating plant. Indeed, to a limited extent this has already been happening. The coal industry and the country in general is faced with a dilemma. Either coal prices are cut to improve the industry's competitive position (which would increase its borrowing requirements just as it is about to reach a break-even point) or oil is allowed to replace coal in electricity generation and thus cause a reduction in demand for coal which will feed through to a reduction in production capacity ie pit closures and job losses. The dilemma is whether or not to allow either of these eventualities to occur. The Government's insistence on competitive viability forecloses the first option. The second is to let the market take its course, a strategy consistent with the Government's basic philosophy But this leaves the long-term possibility of the country facing higher fuel bills depending on a combination of factors outwith the UK's control.

If domestic coal production were to be cut in line with falling demand for coal as an electricity generating source and, say, within 3-5 years oil prices rose to $25 to $30 per barrel (thus making oil a wholly unattractive option) then our electricity boards would be forced to import more and more coal (since closed mines cannot be mothballed and then readily brought back on stream). The price of our energy would be extremely sensitive to changes in the exchange rate and prices on the world market for coal (an extremely limited market at the moment which might demonstrate a highly reactive price to large increases in demand). Thus our independence to set fairly low energy prices would be compromised.

Furthermore, the industrialised countries, mainly through the auspices of the International Energy Agency, have been trying, largely successfully, for the last decade to reduce their reliance on imported oil. It would be sad for the UK to demonstrate that it has learned no lessons from the two oil price hikes of the 1970s. The only option for the NCB and the Government at the moment is to maintain coal capacity at present levels and not to be driven by market reactions to possibly short-term fluctuations in the price of oil. It is essential that a policy be implemented which maintains the UK's self-sufficiency in energy sources.

Evidence that the NCB in Scotland is indeed thinking along the lines of further rationalisation of the industry came when a senior NCB official presented a paper at a recent conference in Glasgow. He stated that a 25% productivity improvement was required in Scotland to ensure long-term survival. The rationale for this was that the country already possessed enough nuclear and oil capacity in electricity generation to displace coal entirely. The target for Scottish coal production is £1.65 per gigajoule produced: current production stands at £2.14 per gigajoule.

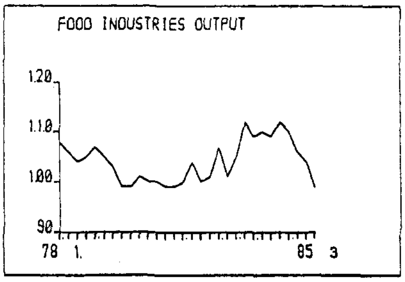
Another indication that a rethink on energy policy is required follows in the wake of the Chernobyl disaster. The Government is currently the driving force behind the CEGB's moves to undertake a construction programme based on the US-designed Pressurised Water Reactors (PWRs). The Chernobyl plant was a PWR as was that at Three Mile Island. While it is not being suggested that a "Chernobyl" would happen in this country, doubts must be raised as to the Government's motives for rejecting the British-designed advanced gas-cooled reactor (AGR) which it is commonly agreed is safer, cheaper to run and more efficient. Furthermore, the technology in the latter option is home grown, not imported.

All-in-all the lack of an identifiable Government energy policy is extremely worrying. Decisions appear to being made on short-term market considerations rather than with a view to the strategic needs of the country.

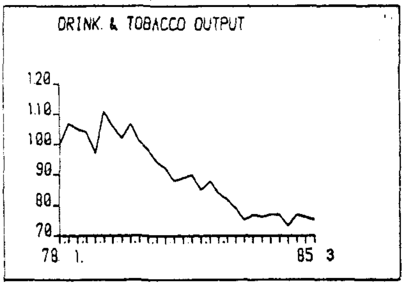
The inquiry into the European Demonstration Reprocessing Plant at Dounreay is currently underway. The debate over safety levels and emissions for the plutonium reprocessing facility for fast reactors is fraught with claims and counter-claims. What seems certain is that the Dounreay workforce and the people of Thurso are basically in favour of the project but the Orkney and Shetland Islanders are very much against it. The eventual economic outcome may well be evenly balanced regardless of the decision. Jobs will be saved at Dounreay if it goes ahead but seem certain to be lost in the fishing, agriculture and food processing industries as public opinion rejects products from this area which it believes, however wrongly, to have a high risk of contamination. On the other hand, if the project is rejected, within a few years the present Dounreay programme will be discontinued. A sensible solution to the dilemma would be the provision of alternative non-nuclear jobs for the Dounreay workforce. Unfortunately this simple option seems to have been overlooked by nearly all the parties concerned in the debate.

FOOD, DRINK AND TOBACCO

The food industry's index of production for the third quarter of 1985 stood at 105, 3% up on the heavily-revised figure for the second quarter but substantially below the corresponding quarter in 1984. As mentioned in previous **Commentaries,** so extensive are the revisions of the index for this sector that one wonders about its true value as an economic indicator.



The index of production for drink and tobacco fell from 76 to 75 in the third quarter of 1985, leaving output for the 12 months to September 1985 broadly unchanged from that recorded for the previous 12 months. These data make food and drink and tobacco the first and third worst performing sectors of Scottish industry respectively.



Despite this, the April 1986 **Scottish Business Survey** reveals that 28% of respondents in the Food, Drink and Tobacco industries were more optimistic than they were in January with only 13% less optimistic. This more optimistic outlook is reflected in the expected trend in sales over the next quarter. Excluding seasonal trends, 38% of respondents indicated that they expected sales to rise, with only 9% expecting a fall. The Survey findings for employment make much less optimistic reading, however. Almost half of the firms surveyed reported lay-offs in the preceding quarter, and 32% expect to lose staff before June ends. In the longer term, the fact that 19% of companies have revised their investment plans upwards since last year and only 4% downwards does seem to augur well.

The drinks industry is dominated by developments surrounding Allied-Lyons which has a substantial Scottish interest. News that the food and drink conglomerate was to buy the wines and spirits division of Hiram Walker was entirely unexpected. The move will give Allied a worldwide drinks portfolio which includes Canadian Club and Ballantines whisky as well as Courvoisier brandy and Tia Maria. Hiram Walker does, of course, have a major Scottish interest, owning ten Scotch whisky distilleries and a large blending and bottling plant at Dumbarton. At £1.25bn this is yet another of the multi-million pound takeovers which are currently prevalent in the food and drink business.

Much more modest at £23.5m is Allied's acquisition of the Haddow off-sales group from Stakis. Haddows shops will now carry the Victoria Wines name. Fourteen off-licences are included in the deal, most in the Central Belt of Scotland. This move was also rather unexpected because Stakis had themselves made some recent acquisitions. The hotel group has now effectively pulled out of the wines and spirits trade.

The Motherwell Food Park (which is actually located in Bellshill) moves from strength to strength. Kibun of Japan are soon to open a £3m fish processing factory creating 100 new jobs, and last month three new arrivals were announced by the SDA. They are: Sea Products (Scotland), a joint Danish-Scottish company processing shellfish; Mordic Poultry, chicken processors; and Bon Appetit who specialise in meat-based products for the retail market. The 22 new jobs to be created by these firms bring the total employment in the food park to 1,200.

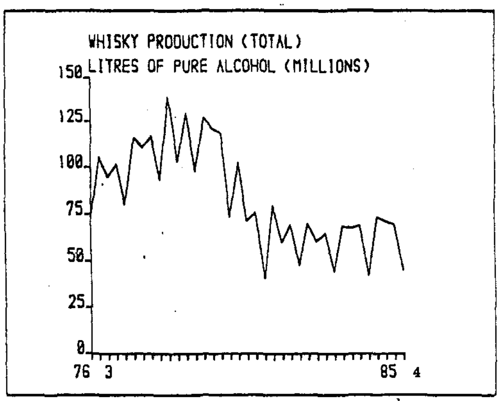
The SDA has consistently made much of the potential of the food industry in Scotland's economic recovery, although the STUC ignored the industry in its recently-published "Strategy for the Future". As a measure of its commitment, the Agency is to establish a £250,000 food centre at the Motherwell Food Park to provide research facilities and marketing and sales assistance.

The recently-announced half year results for Wm Low, the Dundee-based supermarkets group, do not make encouraging reading. Although turnover rose by £25m, operating profit fell by almost £400,000 to just over £3m. Most of the decline in profits comes from the Laws Stores in Gateshead, which has never really been profitable since being acquired two years ago.

WHISKY

Total whisky production for 1985 was 260.6 million litres of pure alcohol, 2.8% up on 1984. This is the second successive year in which total production has risen, an encouraging trend in an industry which has seen so many upheavals in recent years. To put this figure in perspective, it should be noted that the industry is now producing little more than half the total production of the boom years in 1978 and 1979. Given the current vogue for malt whisky it is not susrprising that malt whisky production rose 4.3% during the year, while grain whisky production rose only 1.3%.

A computer malfunction at HM Customs & Excise has caused problems with the figures for exports, and only total export figures for the first quarter of 1986 are currently available. At 53.8 million LPA exports are 3.8 higher than in the corresponding quarter in 1985. The only blot on the horizon in this respect is the possibility of "tit for tat" duty increases on Scotch by the USA in response to increases in Spanish import duties on American corn. The Scotch Whisky Association has been active in trying to dissuade the American authorities from such an illogical course of action.



The apparently endless and acrimonious battle for DCL has at last reached its conclusion, with Guinness emerging victorious. There can be no doubt that the emergence of the merged group has immense implications both for the whisky industry and for the Scottish economy. As recently as last summer Guinness had no direct whisky interests whatsoever. Now the brewers of the famous stout are by far the dominant party in the industry, owning one third of the working distilleries in Scotland and some of the most famous brands in the business, includindg Bell's and Johnnie Walker. In order to escape investigation by the Monopolies Commission several other brands including Haig and Crawfords will be sold to Whyte & Mackay, a move which will almost triple the Lonrho subsidiary's share of the UK market to 16% and do much to help its word-wide marketing effort.

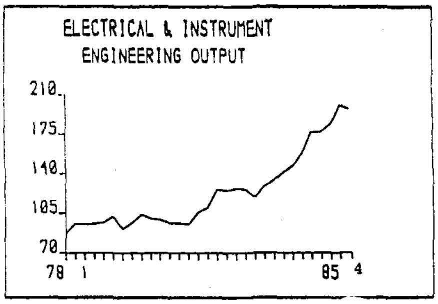
The supreme irony of Guinness's triumph is that the acquisition of the largest company in the industry by an Anglo-Irish concern may actually help to reverse the trend towards external control so prevalent in recent years. By the end of 1985 only 21 of Scotland's one hundred or so working distilleries were controlled from Scotland. The implications of this for the industry and for the Scottish economy have been discussed at some length in previous **Commentaries.** Although nominally Scottish, DCL was effectively run from London and could hardly be regarded as being in ultimately Scottish control. Guinness has always insisted that the headquarters of the merged group will be in Edinburgh, and that senior personnel will be based there as will the full panoply of service functions including research and development, finance and legal and marketing services. The emphasis on service functions is particularly interesting, since these are precisely the functions most frequently lost to Scotland during the process of external acquisition. Clearly Ernest Saunders learned from his wooing of the Scottish financial establishment during Guinness's bid for Arthur Bell.

Assuming Guinness carries out its promise to move to Edinburgh, ostensible control of a major part of Scotland's economy will revert to Scotland, even though Guinness plans to retain "a number of key corporate functions" in London. This will be a welcome development if the real power resides in Scotland. The long-run implications of the takeover remain uncertain, however, and most of the industry appears to be adopting a "wait and see" attitude.

Totally overshadowed by the DCL takeover, but of great importance for the industry, was the unexpected news that Allied-Lyons is to buy the wines and spirits division of Hiram Walker Resources. It is perhaps a measure of the extent to which a contested takeover can capture the attention of the media that an agreed merger worth £1.25bn can escape virtually without notice. Allied already owns Wm Teacher whose Teacher's Highland Cream has 13% of the UK market. However, neither this nor any other of Allied's whisky brands have sold well abroad, with the USA proving to be a particularly unprofitable market. The acquisition of major brands such as Canadian Club and Ballantines will make Allied a major force in the international drinks business, perhaps second only to the mighty Seagram. Hiram Walker's ten distilleries in Scotland will now join the two already owned by Allied.

Coupled with previous takeovers, the two major acquisitions mentioned above mean that no fewer than 66 of Scotland's working distilleries have changed hands at least once in the last ten years, an astonishing rate of change. What the industry really needs now is a period of relative stability in order to tackle the real problems of the relative and absolute decline in whisky's international fortunes in recent years. The reorganisation has occurred; now let the promised regeneration begin.

ELECTRICAL AND INSTRUMENT ENGINEERING



The index of industrial production for Scotland appeared to have taken a long time to reflect the world downward trend in the electronics industry in 1985. However, figures for the third quarter 1985 show a 1% drop from 198 to 195. A similar percentage fall affected the UK index which moved to 130 from 131 in the previous quarter. Nevertheless, the last four quarters reported for the Scottish index record an increase of 21% compared with the previous four quarters (9% for the UK as a whole) which still seems very high when the "rough ride" in the electronics industry over the last year is taken into account.

Just as the recession which swept the industry is appearing in the index of industrial production, signs of an upturn in the sector are now featuring strongly. There have been encouraging moves in the sales of semi-conductors, the part of the industry worst hit, and both National Semiconductor in Greenock and Motorola in East Kilbride are talking of re-recruiting laid-off workers or ending schemes which imposed short-time working on their labour forces. Furthermore, the April **Scottish Business Survey** displays a brighter performance in the electronic, electrical and instrument engineering sector than for quite some months. A net 15% of respondents were more optimistic about the general business situation than they were three months ago. In new orders and employment terms actual trends showed net increases in the participating firms of 16% and 14% respectively. Expected trends reveal even more optimism with a net 43% of firms expecting increases in new orders and 21% of firms expecting to take on more workers (with no firms expecting to reduce employment). Optimism about improving employment trends should be tempered, however, by the fact that capacity utilisation stands at only 66% - well down on 18 months ago. Companies will undoubtedly attempt to take up some of the slack in their businesses with existing workforces before moving into a phase of widespread recruitment.

In the wake of the semi-conductor recession a cartel has been mooted between Japan and the US (by US producers who are rapidly losing ground in competitiveness to the Japanese, particularly in the dynamic-RAM market). This would entail a global price fixing scheme which, although securing some stability for chip producers, would anger computer and systems manufacturers. Its effects on Scotland would not be harmful since all of our semiconductor firms are either US or Japanese owned. Further evidence that the electronics industry is emerging from the recession was contained in a statement by Murray Electronics, an offshoot of Murray Johnstone Investment Trust. They claimed in their interim report that semiconductor orders were rising faster than sales, a leading indicator often used to judge the health of the industry, but that growth was still slow.

There has been much activity in this sector since the last **Commentary.** In February OCLI Optical Coatings Limited announced an £8m investment in their Dunfermline facility's research and development operation. The company, which is involved in the optical components market, expects to create 80 new jobs spread over the next five years. Further job creation announcements were made by two indigenous companies, GL Group and Cruachem Limited. Despite difficulties over the last year the GL Group is expected to create 40 new jobs in the rationalisation programme developed for the company. It is going to concentrate its existing widespread operations on two units at Clydebank Enterprise Zone and one factory in Livingston. Currently the firm employs 200 workers. Cruachem Limited, which exports 95% of its products, is to move to the West of Scotland Science Park. It is the first major firm to do so and will create a further 30 jobs in effecting the move.

There have also been announcements of stabilitation in the workforce of some firms which have been experiencing difficulties either at home or abroad. Lattice Logic, the CAD software designer, has attracted an experienced electronics manager from Burr-Brown. His main aim is to improve the company's marketing techniques and thus improve performance. With this move comes the expectation of growth from a workforce of 43 to one of 50 in the next few months. Despite the massive profits reduction of £130m to £10m experienced by Wang in 1985, there is no forecast of job losses at the Stirling plant. In fact, the R and D budget at the facility is being increased and the plant is expected to increase sales from £30m, to £130m in 1986. This is seen as an indication that the European market for electronics goods is set to grow quickly in the next year or so.

Apricot, which has a production facility in Glenrothes, has divested itself of its American associate which made a £14m, loss on a turnover of only £2.7m last year. The company announced that there was no prospect of job losses in the UK because of this poor trading performance. Finally, STC Exacta has also issued a guarantee of stability of employment to its 450 staff following its £10m management buyout. The Borders firm is one of the largest producers of PCBs in Scotland. Not so sure of guaranteed employment levels in the near future is the much battered Time plant in Dundee. With the takeover of Sinclair Research by Amstrad, the 600 workforce will be under severe pressure to reduce costs. This is so because Amstrad has, in the past, preferred to assemble its computer systems in the cheap labour areas of the Far East. It has said that Sinclair's existing UK manufacturers will only maintain production contracts if "the price is right and quality requirements can be met".

Two initiatives linking the electronics industry and research in universities took place in March. First, Rank Xerox gave a £1m, grant to Edinburgh University for advanced computer equipment for research and teaching purposes and, secondly, the Scottish Electronics Technology Group (SETG) launched an initiative using venture capital (a shortage of which has often been cited as a major constrained on the growth of a truly indigenous electronics industry) to get research out of universities and into the market place.

Another new initiative designed to effect the same kind of liaison between industry and educational establishments has been set up by Strathclyde Regional Council. The Technology Agency Network (a scheme similar to one operating in the West Midlands but apparently not as dynamic or as far-reaching) is designed to bring together college graduates and teams from technology centres to set up firms to exploit their own ideas. It will also help existing businesses to introduce new technology on both the product and process sides.

TRANSPORT EQUIPMENT

Shipbuilding

The announcement by British Shipbuilders of 3,500 redundancies and the closure of three merchant shipyards comes as no surprise. Less than a year ago British merchant shipbuilders had enjoyed a shift in their fortunes, with total merchant orders up for the first time in many years. But this proved to be a brief respite in the long decline in merchant shipbuilding. Lloyds latest returns record a 6% fall in the world-wide gross tonage of new merchant orders for the quarter ended 31 December. UK merchant orders were down by 7.5%. One of the yards to close is Ferguson-Ailsa in Troon, although Ferguson-Ailsa's Port Glasgow facilities will continue to operate.

The Government argue that there is no alternative to cut-backs. They point to Japan and South Korea, which between them build more than half the ships in the world. Both countries are also suffering a severe decline in orders. New orders in Japan were down by 8.0% in the quarter ending last December. Korean orders were down by 6.6%.

There is no doubt that if the Government leaves the merchant shipyards to survive in the market that these redundancies are inevitable. There is a big difference, however, between the UK industry and Japanese and Korean yards. There is still enough capacity and skills for the latter countries to respond to a recovery in orders in the future. On the other hand, UK merchant capacity has now been reduced to a point of virtual no return.

The issue is whether the Government should aim for short-term savings or go for policies which put industry in a strong position to exploit any future up-turn in demand. The British Government is clearly taking the first option, but this route is not as inevitable as the Government implies. France and Italy have chosen to heavily subsidise their merchant yards. It is noticeable that these were two of the small number of countries which enjoyed a rise in new merchant orders at the end of 1985.

The privatisation of British Shipbuilders' warship yards has been completed on time. The deadline set by the Government was 31 March. One of the last yards to be sold was the Aberdeen yard of Hall Russell. Two weeks before the deadline the Government finally accepted an offer from a consortium headed by Mr Ian Phillip. They are now trading under the name of Aberdeen Shipbuilders.

The Government had delayed accepting the consortium's offer, possibly in the hope that with Hall Russell's shortage of orders the yard could be closed and the land sold off. At the last moment Hall Russel won a £5.75 million order from Balravie Offshore Shipping Limited of Aberdeen. The contract is to convert an existing hull into an offshore service vessel. With this order close to completion, there was no alternative but to agree the sale of the yard.

With this new order Hall Russell has managed to break away from the warship yard's traditional dependence on Government defence contracts. However, Hall Russell has only recently been designated a warship yard. In the past they have done a good deal of merchant shipbuilding, and still retain the capacity to take on merchant orders. The other warship yards will be much less flexible. Privatisation has still left them very much at the whim of the Ministry of Defence. The recent battle between Harland & Wolff and Swan Hunter to win an order for two naval oil replenishment vessels well illustrates this fact. Later this year four yards, including Yarrow, will be fighting over orders for two Type 23 frigates. Unless the losers in that battle can find substantial export orders there are certain to be heavy redundancies, if not closures.

The Government appears to have favoured management/employee buy-outs. Trafalgar House put in a strong bid for the Vickers/Cammell Laird yards, but the contract was recently awarded to a management/employee consortium. This leaves all the English warship yards (Vickers/Cammell Laird, Vosper Thornycroft, Swan Hunter and Brooke Marine) in the hands of management. In contrast, the two Scottish warship yards have been sold to external buyers (Yarrow was sold some time ago to GEC). The two Scottish warship yards had also discussed mounting a joint management/employee buyout. Although the Hall Russel workforce were in favour, the vast majority of the Yarrow workers voted against the scheme.

Privatisation of the management of the Royal Dockyard has proved much more troublesome than the sale of the warship yards. The Government has always claimed that putting the yards into commercial management will bring substantial savings. A recent internal report leaked from the Ministry of Defence suggested instead that it could cost £100 million more a year to run Rosyth and Devenport dockyards privately. The additional cost will mainly result from redundancy payments, the setting up of a private pension fund for workers, and the need to appoint additional supervisors within the MOD.

At a meeting of the Dockyards Services Bill Commons Committee in March, the Junior Defence Procurement Minister admitted that privatisation might add to the cost of running the dockyards. Even so, the Government continued to push through the Bill which passed its final reading on 8 April. The deadline for tenders is 1 August. This gives potential bidders very little time to prepare proposals on how they will run the very complex operation of a Royal dockyard. Inevitably none of those tendering will have previous experience of this kind of work. Already four groups have shown an interest in Rosyth. They are Northern Engineering Industries, Press Offshore, and two consortia, Babcock International/Thorn EMI and the Balfour Beatty/Weir Group.

Meanwhile, the Navy have just announced plans for a £220 million construction programme at Rosyth. Included in the project are two covered dry-docks, workshops, and storage. These are designed to make Rosyth ready to refit Trident submarines, which will be three times as long as the Navy's existing submarines. There will also be special accommodation for nuclear refuelling. Construction is expected to be completed in 1989.

Vehicles

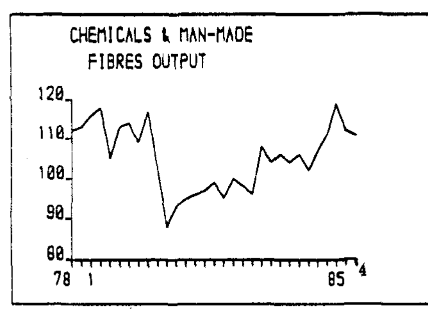
The long-expected closure of BL's truck division at Bathgate arrived in March. Hopes that an outside buyer might be found for the plant failed to materialise. Ironically the closure of the plant took place at the same time as the Government was hoping to sell the remainder of the BL trucks division to General Motors. This plan has now been shelved, but the indications are that the Government intends to continue to look for buyers for BL. The man who pushed through the privatisation of the warship yards, British Shipbuilder's Chairman Graham Day, has just been appointed Executive Chairman of British Leyland. Graham Day has no experience of vehicle manufacture, but he has considerable experience of selling-off public assets.

The closure of Bathgate closely followed the liquidation of the Glasgow sports car manufacturers AC Motors. This leaves only two vehicle manufacturers of any size in Scotland. They are Volvo Trucks in Irvine and the coach manufacturers, Walter Alexander, of Falkirk. For the moment both of these plants appear to be performing well.

CHEMICALS AND MAN-MADE FIBRES

The index of industrial production shows that output in the chemicals and man-made fibres industries fell by 1% over the third quarter of 1985. The index now stands at 111 (1980=100), registering a fall of 8 points since the start of 1985. However, in the four quarters to September 1985 output improved by 8% over the corresponding quarter a year earlier.

The results of the April Scottish Business Survey indicate that a balance of 5% of respondents in the Chemicals sector were more optimistic about the general business situation in the industry as compared to three months ago. Much of this is no doubt due to the expected trends in the volume of new orders over the coming three months. A balance of over 50% expects increased orders in each of the Scottish, rest of UK and foreign markets. This reverses the actual results of the past three months in home markets where the volume of new orders fell. The volume of new sales is expected to continue on its upward trend although with less dramatic increases expected in exports than were experienced in the past three months.

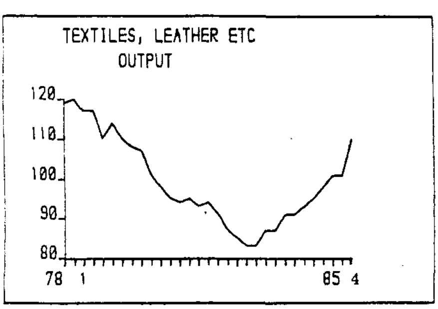


On the employment front, whilst a balance report a fall in actual employment over the past three months, the situation is expected to improve, especially with respect to female employment. This is to be accompanied by an increase in investment in plant and equipment.

It was announced in March that Fermentech, a biotechnology company, will be setting up a new production plant in Livingston that will provide employment for 60 people. The plant, costing between £2 and £3 million will manufacture Protein A,a substance that has a wide range of medical uses including the production of antibodies that help the body fight infection. Livingston Development Corporation faced heavy competition from England, Ireland and Belgium and were helped by a reported £600,000 grant to Fermentech from the Industry Department for Scotland.

The fall in oil prices and weak markets are amongst the reasons put forward to explain the disappointing first quarter results reported by ICI. Overall, turnover fell by 7% and net profit by 23% in comparison to the first quarter of 1985. In chemicals the lack of demand for plastics is blamed for the 4% fall in sales, whilst the downturn in agricultural chemicals is most noticeable in fertilisers and can be accounted for by the world food surplus. The dwindling oil price had two effects; first, in reducing the profits from oil production, compounding the effects of lower output (oil sales down 36%), and, secondly, on the value of stocks held. On a brighter note, there was some improvement in fibres, colours and polyurethanes.

TEXTILES, CLOTHING AND KNITWEAR



Statistics recently released by both the British Textile Confederation and the Scottish Woollen Industry confirm that 1985 was a good year for this sector in both domestic and export markets. The BTC report that UK clothing exports rose by 18% in value, and textile exports by 16%, reflecting increases in the volume of exports of 9% and 6% respectively. At the same time the volume of clothing imports remained unchanged, although the volume of textile imports rose by 5%.

The Scottish Woollen Industry, which represents most of Scotland's wool textile and yarn manufacturers, reported even better results. Exports were up by 30%, and the home market also showed strong growth. Most interestingly, this section of the industry recorded an increase in employment from 3,655 at the end of 1984 to 3,780 at the end of 1985. Although recent issues of the **Scottish Business Survey** have suggested that employment might have been growing in this sector, these are the first figures to confirm this trend.

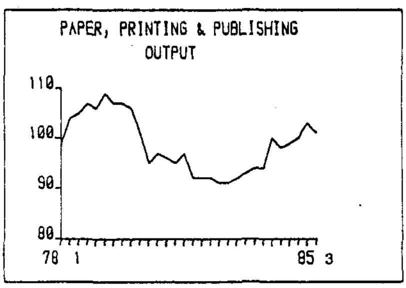
The growth in export sales by the Scottish Woollen industry has followed a similar pattern to that of the rest of the UK clothing industry. Sales to the US and most of Europe are well up, although purchases by West Germany have not shown the same growth. The weakening of the US dollar against other currencies, including sterling, does not yet appear to have squeezed demand for Scottish wool textiles. Sales to the US were up 27% in 1985.

After days of uncertainty the merger between Coats Paton and Vantona Viyella was finally confirmed. It is not long since Vantona merged with another major textileproducer,Nottingham Manufacturers. The new company, Coats Viyella, will have combined sales of £1.69 billion. This will make them the largest British textile and clothing manufacturers, even outstripping Courtaulds.

Coats Paton had initially agreed a merger with Dawson International, but at the last moment withdrew and accepted a higher bid of £717 million from Vantona. Both companies offered Coats the chance to dilute their heavy dependence on the earnings of overseas subsidiaries. Two thirds of Coats turnover is manufactured abroad. This is a potentially risky position to be in during these days of shifting exchange rates. The elimination of Dawson from the deal removed most of the Scottish dimension. Although Coats is nominally a Scottish firm, less than 1% of the employees are based in Scotland.

Negotiations on the Multi-Fibre Arrangement have now reached their final stage. The EEC Council of Ministers has agreed that the MFA should be renewed. Their exact position on the form that the new arrangement should take has remained secret, although almost certainly they will support a move to more liberal trade. The final agreement must be hammered out by GATT by the end of July. There is growing concern that if the EEC maintain their more liberal stance in the face of US determination to maintain firm limits on textile and clothing imports, the final form of the agreement may deflect imports from the US to Europe. On the other hand, if US negotiators do accept a more liberal MFA, the danger is that the Jenkins Bill (restricting clothing and textile imports into the US) will be re-activated. The last time the Bill was presented it was vetoed by the President. If the Bill wins more than a two-thirds majority next time, the President's veto will be invalid. In this case, the Border Knitwear industry, which relies heavily on US sales, could be hit hard.

PAPER, PRINTING AND PUBLISHING



According to the index of industrial production, output in Scotland in the paper, printing and publishing industries fell by three points over the third quarter of 1985 to stand at 99 (1980=100). This is in contrast to the recorded rise of 3% when the four quarters to September 1985 are compared to the previous four quarters. This figure was identical to that recorded for the UK as a whole. The index indicates that whilst the industry has recovered some of the ground lost during the recession, output is still significantly below the peak recorded in 1979.

The April Scottish Business Survey reports that a significant balance of respondents, 21%, were now more optimistic about the general business situation in the paper, printing and publishing industry than they had been three months before. New orders are expected to increase overall over the next three months although the healthy balance expecting an increase in orders from the rest of the UK and overseas is accompanied by a balance expecting a fall in new Scottish orders. This almost matches the actual trends reported over the last three months where new orders from the rest of the UK and export markets compensated for a fall-off in orders at home. Sales volumes arose in all markets over the past three months but this trend is expected to continue only in non-Scottish markets over the coming period.

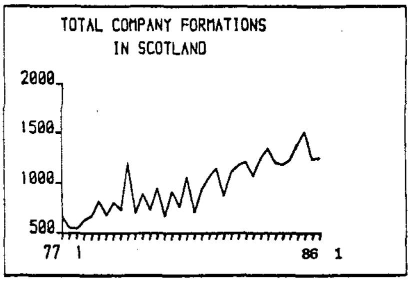
The trends in employment are very much downward although some increase in investment intentions is apparent. It is also clear that a major motivating factor behind new investment has been the desire to introduce new technology and to increase efficiency. This ties in with the joint statement issued by the print union SOGAT and the employers association, The Society of Master Printers in Scotland, in which they encourage the rapid introduction of advanced technology into the commercial printing industry. The statement provides for negotiations at individual company level and emphasises that both organisations have long recognised the need to adopt new technology in order to maintain the Scottish industry's competitive position. The agreement, however, does not extend to national daily newspapers.

On the subject of national dailies, there is continuing uncertainty surrounding the future of the workforce at the Daily Record and Sunday Mail plant at Anderston Quay. The dispute has run a complicated course and for more than three weeks in March and April the publication of both papers was halted. The papers reappeared on 3 April on the basis of an agreement by both sides to enter into negotiations leading to "cost cutting" job losses. A deadline of 30 April was set for the first set of negotiations but, at the time of going to press, these had yet to be concluded. Estimates of the expected number of jobs to be lost, out of an existing workforce of 1050 vary widely, but it is expected that whatever the figure agreed, it can be met by voluntary redundancy and natural wastage.

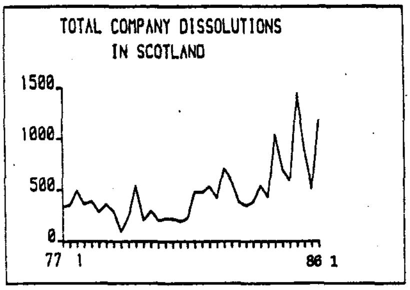
The Glasgow based publishing firm William Collins announced in March increased profits for 1985 with the prospect of even better performance in 1986 and 1987. The 1985 results show profits up by 11.5% to £131 million, a figure which would have been bettered had it not been for the adverse effects of exchange rate movements on the earnings from foreign subsidiaries. On the home front, Collins' Glasgow operations showed a healthy increase in sales of 9% over the year, with returns on capital employed also improving.

COMPANY FORMATIONS AND DISSOLUTIONS

At 1,502 company formations in Scotland in the first quarter of 1986 were up by 27% on the previous quarter, and up 8% on the corresponding quarter in 1985. This is the second highest number of formations ever recorded in a single quarter and indicates that the steady upward trend in formations continues.



Dissolutions for the quarter number 833, a fall of 43% over the correspoding figure in 1985. As noted in previous **Commentaries** this in no way reflects the actual level of business failures in Scotland.



Total business failures in the UK fell by 5.5% in the first quarter compared with the 1985 first quarter, according to Dun & Bradstreet. This is the first quarterly fall in the number of company liquidations since the survey began in 1980.

The Service Sector

FINANCIAL SECTOR

A number of theorists* have suggested that innovation in financial markets is driven by regulation. According to this view regulation often prevents firms from selling or providing particular financial services. The possibility of securing profit from meeting the unsatisfied demands of consumers induces firms to respond by introducing new products and innovations that circumvent the regulations. In turn, the regulators endeavour to plug the holes in their regulatory net with the result that further innovation is induced and a continuing spiral develops.

Although extreme in its predictions and not wholly satisfactory since it assumes that regulators cannot learn and amend their actions accordingly, the theory contains an element of truth, the evidence for which can be perceived in British financial markets, an obvious example being the continuing changes in the Business Expansion Scheme (BES). The recent Budget exempted BES shares from capital gains tax on first sale greatly increasing the attractiveness of this tax shelter for high tax payers. At the same time attempts were made for the third successive Budget to stop some of the abuses, most notably to prevent investment in less risky, asset (particularly property) based companies. In future shares will not qualify for BES relief if the value of a company's land and buildings exceed one half of the net value of its assets at any time during three years of the issue. Although desirable to prevent abuses, such rules may undermine the intentions of the scheme, not least because genuine risky investments often lose money during their early years. This provision could then penalise the very companies that the scheme is aimed at encouraging. One small crumb of comfort is that companies that fail the asset test will be able to issue up to £50,000 a year in new shares which qualify for BES relief. The BES tax concessions, it is to be hoped, will encourage further high risk investment with beneficial effects for the UK economy. Several BES schemes are managed from Scotland although the majority of their investments are South of the Border. Several managers have complained of a shortage of suitable investment opportunities in Scotland and it is to be hoped that the BES scheme, now continued indefinitely, will encourage more response from Scottish unquoted companies and entrepreneurs.

A second interesting example of the potential effects of regulation is provided by the mortgage market. One of the most important developments in the last quarter has been the entry of the American investment banking firm. Salomon Brothers, to the UK domestic housing market. The firm has set up a low cost mortgage operation to attract the larger, lower risk mortgage applications and offer a mortgage package, backed by suitable insurance policies, at a very attractive price. Salomon repackage the domestic mortgages it issues into large securities which are then sold to institutions as a low risk, secured floating rate bond. The attraction of the operation stems from the relatively high costs that most UK building societies incur as a result of their branch operations. In the absence of competition from similar schemes and provided that the advertising costs are not too prohibitive, Salomon should be able to earn a substantial profit and cream off the low risk, high value mortgages leaving the building societies the less desirable business. The consequences for the building societies could be dramatic. Loss of the better quality business would be a blow but as important could be the effect on their cost structure of a reduction in volume of business. Branch networks are expensive to maintain and require a considerable volume of funds to justify their continuance. For building societies already having to compete with much increased competition from the banks, the increase in the opening hours of the Bank of Scotland being an obvious example of the more competitive environment they are facing, the additional competition posed by Salomon Brothers, and if successful by a host of imitators, is an additional burden.

At the same time regulatory constraints continue to tie the hands of the more progressive building societies. The new legislation currently being debated by Parliament will improve their position, but in general the legislation is unduly restrictive and it is almost certainly a case of too little, too late. The Government will not uphold a true laissez faire stance and accept that all financial assets and institutions should compete on equal terms. Nor will it adopt a more rational, regulation-by- function approach, although in the marketing of investments the proposals of the Securities and Investments Board appear to represent a more even-handed approach. If the Government believes that the housing market should be treated differently, for whatever reason, the appropriate response is to lay down regulations to meet the desired objectives that affect all participants in the housing market. Any institution that is prepared to meet the particular conditions applicable to the market could then compete on equal terms. The present approach is unfair and discriminatory and has left the building societies exposed and unable to compete on equal terms with other institutions. The effect is almost certainly likely to lead to further mergers and branch closures. The outlook for smaller Scottish towns may well be the departure of many building society branches with consequent effects on employment, property demand and customer convenience.

The problems of regulation are not confined to building societies. The latest disclosure rules from the Marketing of Investments Board Organising Committee (MIBOC) indicates that self-regulatory bodies do not always act in the best interests of the public. MIBOC is prepared to allow insurance brokers exemption from disclosing the commissions which are deducted from clients' premiums. The Committee suggests that brokers should only have to declare that any commission they receive is in accordance with an approved industry scale. The justification MIBOC advances for this suggestion is based on the view that disclosure is only intended to ensure that a client is not sold a particular policy because it carried a higher commission than another. Having adopted a blinkered view of the purposes of disclosure MIBOC is then able to argue that given an approved industry scale sales aimed at maximising commission cannot happen and hence disclosure is not required. Similar arguments are made with respect to unit trust commissions despite the long-standing disclosure of charges that unit trust investors receive (and ignore). The MIBOC argument depends for its validity on its view of disclosure, a view that ignores the competition for saving from other investment vehicles as well as the differences in commission among policies within the life assurance industry. Informed investment requires information and the MIBOC proposals do nothing to foster better, more informed investment.

High commissions reduce the investment performance of the industry and in the long-term are unlikely to help its competitive position vis-a-vis other investment vehicles. Full disclosure may be a painful experience at first, with perhaps some dramatic changes in who receives new business and in the methods by which business is sold, but in the long-term it is important to the health of the life assurance industry. The tax advantages of the industry have been reduced and it is competing in a more competitive investment market. Hanging on to protective and restrictive practices is unnecessary and may well be self-defeating in the longer-term. The Scottish life offices should accept the challenge and lead the way by providing full information to potential clients. The Scottish offices are, with one exception, run after all for the benefits of their policy holders and not for outside shareholders. It is only reasonable that the owners should be provided with such important information.

The introduction of the Personal Equity Plan (PEP) in the Budget may be an important cause of lost business to the life offices in the future. Under the scheme investors will be able to invest up to £2,400 a year in ordinary shares quoted on any UK stock exchange. The funds must be held for at least one full calendar year to be free of both dividend and capital gains tax but trading will be allowed and the funds will remain free of taxes so long as the gains are re-invested. Investment trusts are included in the scheme providing a welcome boost for the investment trust industry and Scottish fund managers in particular.

The PEP offers a tax free, long-term saving plan. Combined with term assurance (which can be purchased at low cost), it can offer investors all the benefits of endowment policies and in addition provide them with flexibility over the desired time horizon of their investment, the possibility of choosing their investments and relatively low expenses since investors will be spared the selling expenses associated with endowment policies. The major difficulty for investors may be in securing adequate diversification,** although there is considerable evidence to show that a small number of investments provide adequate diversification. Inclusion of investment trusts and UK unit trusts in the allowable range of investments will also allow small investors to diversify by incorporating these investment vehicles into their portfolios. Investors in the more basic schemes may also lose the benefit of management expertise but since there is little evidence to show that any investors, institutional or personal, are able to secure above average returns for the risk assumed, except by chance, there is little to lose from its absence.

From a wider perspective one must question the wisdom of introducing another scheme that allows tax breaks to investors in order to correct the distortions in the market induced by existing tax shelters. Removing existing tax shelters on mortgages and possibly on pensions might have been a better way to proceed. In any event it remains to be seen whether the scheme entices new investors into the market. It is certain to attract existing investors but the important test is whether new investors will use the PEP scheme rather than the offerings of existing financial institutions. If investors are attracted then the life companies could find themselves facing increased competitive pressure from yet another quarter. As a matter of policy the Scottish life offices and other investment managers should be investigating the possibilities of offering PEP schemes that meet investors' needs. Swift response could allow Scottish investment teams to become well established in a new investment area before the market has grown and matured. The growth of life assurance and pensions has been due in large part to their attractiveness as tax shelters. It would be foolhardy to predict that similar growth will not occur for PEP schemes given the powerful stimulus that tax considerations appear to induce.

*See for example, Kane E J "Recent Structural Changes in the Capital Markets", **American Economic Review**, May 1983, No 2.

Recent examples for the UK are provided in Draper P, "The Advantages of Diversification through UK Equities", **The Investment Analyst January 1986, No 79.

DISTRIBUTIVE TRADES

The latest **Scottish Business Survey** (SBS) results suggest that first quarter performance in wholesaling was somewhat disappointing, with a net 10% of respondents reporting declines in sales. In spite of this, a balance of 24% of wholesalers expected sales to increase in the second quarter of this year.

First quarter employment trends in wholesaling followed the same general pattern as had been observed throughout 1985; that is, reported net increases in part-time workers were insufficient to offset net declines in full-time employees, with the result that a balance of 7% of respondents reported a fall in total employment. Survey responses indicate that wholesalers expected these employment trends to continue between April and June.

In marked contrast to those in the other Chamber of Commerce areas, Glasgow wholesalers emjoyed a buoyant first quarter sales performance (see Table 1). Indeed, according to the SBS returns, this was the third successive quarter in which Glasgow wholesalers had the best sales record among the areas covered. However, it will be noted that even in Glasgow actual and expected wholesaling employment is falling on balance.

Table 1 Geographical response to April 1986 Scottish Business Survey : wholesaling

		Balance of respondents in:			
		G %	E %	D %	A %
Overall confidence	UP	+31	+ 6	-20	+ 3
Actual sales	UP	+56	-35	-25	-27
Expected sales	UP	+80	+28	-26	+15
Actual employment	UP	-14	-22	+23	-14
Expected employment	UP	-14	-19	-50	-17
Investment intentions	UP	+ 7	+ 9	+46	+ 6

Key: G = Glasgow E = Edinburgh
D = Dundee A = Aberdeen

Perhaps surprisingly in view of the bad winter weather, Scottish retail respondents to the SBS survey continue to report healthy sales growth, with a net 51% reporting increased sales during the first quarter of 1986. This was a significantly better performance than had been expected by respondents in January. Furthermore, since a net 30% of retailers surveyed expect further sales growth in the second quarter, it is clear that the trade itself does not believe that the 'retail boom' has run out of steam.

As had happened in the last few months of 1985, retail respondents reported an overall increase in total employment in the first quarter of this year. However, in contrast to the pattern of last year where employment growth was entirely concentrated in part-time workers, the April SBS records gains in both full-time and part-time employees. Encouragingly, a balance of 18% of retailers expected employment to increase further in the second quarter.

Table 2 Geographical response to April 1986 Scottish Business Survey : retailing

		Balance of respondents in:			
		G %	E %	D %	A %
Overall confidence	UP	+ 3	+18	+15	- 8
Actual sales	UP	+74	-15	+21	+51
Expected sales	UP	+16	+28	+54	+ 1
Actual employment	UP	+42	-10	+ 9	-15
Expected employment	UP	+ 9	-11	+44	-23
Investment intentions	UP	+37	+ 9	+34	+ 9

Key: G = Glasgow D = Dundee
E = Edinburgh A = Aberdeen

Table 2 shows that, as in wholesaling, Glasgow retailers enjoyed a particularly good first quarter. On the other hand, as happened in the last three months of last year, Edinburgh retailers on balance reported actual declines in sales. It is interesting to note that while Aberdeen respondents had a good first quarter performance, they were considerably less optimistic about prospects in the immediate future. This almost certainly reflects concern over the prosperity of Aberdeen's offshore oil industry in view of recent substantial falls in the price of crude oil.

TOURISM

Since the publication of the last **Commentary**, two important decisions have been taken by the Government regarding Scottish tourism administration:-

- The rejection of the Trade and Industry Select Committee recommendation that the Scottish Tourist Board (STB) should be abolished. 1

- The rejection of the Scottish Affairs Committee recommendation that the Highlands and Islands Development Board's (HIDB) tourism marketing responsibilities should be transferred to STB. 2

The two decisions amount to a **retention of the status quo.** On 27 February, Lord Young took the unusual step of replying in advance to the Trade and Industry Select Committee on one aspect of its report, by giving a firm assurance as to the future of the Scottish Tourist Board and the other statutory national tourist boards:

> "We have concluded that, in the interests of effective promotion of tourism within the UK, we should maintain the existing structure of the statutory tourist boards and ministerial responsibility for them and to concentrate on continuing to improve liaison and co-operation between the boards."

Two months later came the Government's refusal to transfer the tourism marketing activities of the Highland Board to the STB, a reaffirmation of the view that support for tourism is considered by ministers to be an integral part of the HIDB's developmental remit. The Government have made it clear that in future it will expect these two quangos to co-operate more closely with one another in their efforts to expand Scotland's tourism sector. The Scottish Tourist Board is also being encouraged to articulate a policy to guide its promotional and development work. A memorandum 3 to the Trade and Industry Committee submitted by the Industry Department for Scotland in February 1985 revealed that STB had been asked "to produce a paper outlining its strategy and the objectives and targets of its individual programmes...." We await the Board's soon to be issued annual report for an indication of the scope and content of the STB's emergent strategy.

One important strategic issue that ought to be addressed is the extent to which there should be more effective co-ordination of the various financial assistance programmes designed to stimulate the development of new tourism plant. No less than five national government bodies are involved - STB, HIDB, the Scottish Development Agency, the Countryside Commission for Scotland, and the Department of Agriculture and Fisheries - and some form or other of inter-agency monitoring is essential to avoid waste and duplication and to deliver a desired pattern of new facilities and services. The Scottish Development Agency, in particular, has identified the development of higher quality tourist attractions as a major obstacle to the realisation of Scotland's tourism potential, and is energetically fronting major new initiatives in Glasgow and Edinburgh (see current **Perspective**), Greenock and Leith, and Dundee and Oban. In addition, the Agency has been the catalyst for smaller projects for other parts of the country (eg. the rejuvenation of Thirlestaine Castle as a visitor attraction). There is an acute sense in which these efforts ought now to be integrated with those of other agencies and interested parties to form a co-ordinated **national development plan for Scottish tourism.**

1. House of Commons Trade and Industry Committee, **Tourism in the United Kingdom**, HMSO, 1985

2. Scottish Affairs Committee, **Highlands and Islands Development Board**, HMSO, 1984

3. House of Commons Trade and Industry Committee Inquiry in Tourism in the UK, **Tourism Policy in Scotland**, Memorandum by the Industry Department for Scotland, 1985

The Labour Market

EMPLOYMENT

Table 1 shows the most recent data available on employment in Scotland. (The corresponding table was inadvertently omitted from the last **Commentary**). It shows an increase in total employment over the year to September 1985 of 17,000. This reflected the longer-term trends of declining male employment (-12,000 over the year) and increasing female employment (+28,000). The latter consisted primarily of part-time employment (+23,000), but, contrary to trend, full-time female employment also increased.

Table 1 Employees in employment in Scotland (000s) 1979-1985

	Male	Female All	Female Part-time	Total	Manuf (2-4)	Prod. and Cons. (1-5)	Services (6-9)
1979 June	1,205	897	332	2,107	606	837	1,222
1983 June	1,070	851	361	1,921	447	647	1,231
1984 Mar	1,407	861	375	1,908	436	636	1,232
June	1,048	882	386	1,930	437	634	1,255
Sept	1,056	878	387	1,933	436	635	1,255
Dec	1,045	885	396	1,931	434	633	1,260
1985 Mar	1,037	882	396	1,919	431	626	1,253
June	1,037	902	409	1,939	432	622	1,276
Sept	1,044	906	410	1,951	433	622	1,285

Source: Department of Employment Gazette

Table 2 presents employment estimates for those companies wholly-related to the North Sea oil industry onshore and offshore (but excluding employment on short-term oil-related projects). The employment data reflect the fact that significant oil production began in 1976 and increased by a factor of 2.5 times over the period to 1984. The geographic dispersion of wholly-related employment is as expected with over 80% of such employment being concentrated in the Grampian region (although this figure is exaggerated somewhat by registration of all offshore employment in Aberdeen).

At June 1985 employment in companies which are wholly-related to the North Sea oil industry accounted for only 3.3% of total Scottish employment. However, this measure considerably understates the contribution of the North Sea oil industry to Scottish employment since first, these data embrace only firms **wholly**-related to North Sea development. The activities of many other firms are at least partly, and directly related to the oil industry. Secondly, many Scottish firms are indirect beneficiaries of the North Sea oil industry's presence through, for example, the demand created as a consequence of oil-related employment.

The recent fall in the oil price is naturally likely to have an adverse impact on oil-related employment, and the Grampian region will obviously be hardest hit. Many existing operational fields, however, remain viable and profitable because the (variable) costs incurred in producing additional barrels of oil are still significantly less than the market prices of such oil. Consequently, for the foreseeable future those directly involved in oil production are unlikely to be particularly adversely hit by the oil price fall (except insofar as current production may be restricted in anticipation of higher future oil prices).

However, the development of new fields is likely to be severely curtailed, since this incurs very large set-up costs that may not be covered by ancitipated revenues at currently prevailing oil price levels. Table 3 suggests that, at least in terms of values of orders placed by the offshore industry, the development phase is particularly important (accounting for over 50% of the total value of orders).

Table 2 Employment in companies wholly-related to North Sea oil industry

	June							Dec	June	Dec	June
	1977	**1978**	**1979**	**1980**	**1981**	**1982**	**1983**	**1983**	**1984**	**1984**	**1985**
Scotland	28.63	33.99	41.76	46.34	49.61	58.32	63.29	66.75	64.05	60.98	63.76
Central and Lothian	0.62	0.55	0.62	0.86	1.99	0.15	0.86	0.62	0.98	0.75	0.52
Fife	0.81	1.38	2.26	0.81	1.09	1.25	1.57	1.35	1.41	1.70	1.30
Grampian	15.68	22.89	28.06	32.32	33.93	40.02	46.32	48.02	49.51	47.94	52.38
Highland	7.09	6.00	4.81	4.35	6.01	7.39	7.21	8.59	4.44	3.60	3.36
Strathclyde	1.92	0.50	0.77	2.73	3.07	3.80	2.83	3.52	3.38	3.49	2.40
Tayside	1.76	2.05	2.32	1.81	1.99	2.50	2.29	2.48	2.33	1.53	1.78
Islands	0.77	0.63	2.92	3.46	2.53	2.23	2.21	2.17	2.00	1.97	2.02

The table relates to employment in companies wholly-related to the North Sea oil industry onshore and offshore (but excluding employment on short-term oil-related projects.

Source: Scottish Economic Bulletin

Table 3 Percentage distribution of orders placed for goods and services for developments on the UK continental shelf

Sector	**1978**	**1980**	**1982**	**1984**
Exploration				
Surveying	0.70	0.84	1.99	1.55
Exploration and appraisal drilling	4.56	9.66	8.97	10.70
Sub-total	5.27	10.67	10.95	12.26
Development				
Production	25.46	29.86	17.62	26.68
Installation operations	9.34	3.45	9.19	7.18
Submarine pipelines	2.67	3.74	4.55	4.68
Development drilling	1.91	3.74	2.52	1.22
Terminals	14.74	16.64	4.15	2.14
Sub-total	62.52	67.16	48.01	54.02
Production				
Maintenance	4.64	3.40	2.61	2.52
Sub-total	4.64	3.40	2.61	2.52
General services				
Transport	13.09	7.14	12.46	6.41
Diving and under water services	1.91	2.02	3.18	2.44
Drilling tools and equipment	4.51	3.99	12.94	16.20
Support of personal offshore	4.26	2.94	5.21	3.22
Miscellaneous	3.81	2.65	4.64	2.94
Sub-total	27.57	18.74	38.43	31.20
GRAND TOTAL	100.00	100.00	100.00	100.00

Source: "Development of the Oil and Gas Resources of the United Kingdom", Department of Energy, 1979, 1981, 1983 and 1985.

If the current oil price is regarded as close to its longer-term level, then significant adverse employment effects would be implied. Indeed, caution may, at the very least, lead to postponement of developments even by those who regard the oil price as low relative to its likely future value. Any induced contraction in employment will be unevenly distributed across industries as Table 4 suggests.

Table 4 Employment in Scotland wholly associated with North Sea oil - December 1985

Summary by standard industrial classification

13	Extraction of mineral oil and gas	26,490
14	Refining	2
22	Metal manufacture	3
24	Manufacture of non-metallic mineral products	16
25	Chemicals	52
31	Miscellaneous metal goods	790
32	Mechanical engineering	14,012
34	Electrical and electronic engineering	1,355
36	Marine engineering	350
37	Instrument engineering	98
45	Clothing	43
47	Publishing	21
49	Miscellaneous manufacture	4
50	Construction*	5,667
61	Distribution and supplies	2,885
63	Commission agents	9
66	Catering	2,235
72	Road transport	40
74	Sea transport	1,267
75	Air transport	1,258
76	Supporting services and transport	1,267
77	Miscellaneous transport and storage serv.	1,102
79	Communications	23
83	Business and professional services	3,946
84	Renting of moveables	624
91	Public administration	17
92	Sanitary services	46
93	Education	79
95	Medical services	24
	Total employment	63,725

*This does not include temporary construction camps, only companies permanently involved in North Sea oil activity.

Source: North Sea Oil Information Sheet, February 1986

Development-related employment, which is likely to be worst affected by the oil price fall, is probably concentrated in the mechanical engineering and construction industries.

Over the longer term, a sustained decline in the oil price will lead to a sustained contraction in the Scottish oil industry. Lower oil prices are likely, however, to stimulate activity elsewhere in the Scottish economy. In particular, the reduction in fuel costs and the comparative decline in Sterling are likely to increase the competitiveness of the non-oil sector in Scotland. This in turn is likely to stimulate demand for the output of the non-oil sector, and (in the absence of binding supply constraints) stimulate output and employment in that sector.

Any beneficial effects of the oil price fall on the Scottish economy are likely to be much more evenly spread over industries and locations than the adverse effects.

UNEMPLOYMENT

Economists have traditionally defined the unemployed as those who, whilst not employed, are **actively seeking** employment at prevailing wage rates. The mere existence of unemployment in this sense is not necessarily regarded as a problem: in a dynamic mixed economy shifts in consumer demand among products imply a continuous need for the reallocation of labour and other resources across firms, skills and industries. There will always be some degree of "frictional" unemployment which is a manifestation of more or less temporary periods of unemployment as workers search the labour market in pursuit of the best employment opportunities and firms search for the best candidates to fill vacancies.

Whilst the existence of unemployment does not necessarily constitute a problem, there is widespread agreement that, presently, the **extent** of unemployment in Scotland and in the UK as a whole is "too high" in relation to some (usually ill-defined) notion of a "desirable" or

Table 5 Unemployment - seasonally adjusted (excluding school leavers)

	Number (000's)	Rate (percent)	Change since previous month (000's)	Average change over previous 3 months (000's)	Male Number (000's)	Male Rate (percent)	Female Number (000's)	Female Rate (percent)
1985								
March	327.5	14.5	+2.6	+1.5	227.6	17.8	99.9	10.2
April	333.7	14.8	+6.2	+3.0	227.6	18.2	101.1	10.3
May	333.2	14.8	-0.5	+2.8	232.2	18.2	101.0	10.3
June	333.3	14.8	+0.1	+1.9	232.2	18.2	101.1	10.3
July	333.2	14.8	-0.1	-0.2	231.8	18.1	101.4	10.3
August	332.8	14.7	-0.4	-0.1	231.5	18.1	101.3	10.3
September	332.0	14.7	-0.8	-0.4	230.8	18.1	101.2	10.3
October	334.0	14.8	+2.0	+0.2	232.3	18.2	101.7	10.4
November	332.7	14.7	-1.3	NIL	231.6	18.1	101.1	10.3
December	334.4	14.8	+1.7	+0.8	233.1	18.2	101.7	10.4
1986								
January	334.8	14.8	+0.4	+0.3	233.1	18.2	10.9	10.4
February	335.2	14.8	+0.4	+0.8	232.9	18.2	102.2	10.4
March	338.5	15.0	+3.3	+1.4	235.9	18.5	102.7	10.5

Note: Seasonally adjusted figures have been revised to take account of the change in the compilation of the unemployment statistics.

Source: Department of Employment

Table 6 Unemployment - unadjusted

	Number (000s)	Rate (percent)	Number (000s)	Rate (percent)	Number (000s)	Rate (percent)	Inflow (000s)	Outflow (000s)
1985								
March	242.7	19.0	109.2	11.1	351.9	15.6	34.1	38.8
April	245.8	19.2	108.9	11.1	354.7	15.7	39.2	35.6
May	241.9	18.9	106.1	10.8	347.9	15.4	35.4	42.8
June	239.9	18.8	105.7	10.8	345.6	15.3	37.9	40.7
July	241.6	18.9	110.7	11.3	352.3	15.6	46.0	39.3
August	240.2	18.8	109.9	11.2	350.0	15.5	36.8	39.7
September	243.9	19.1	111.8	11.4	355.8	15.8	44.2	46.0
October	243.6	19.1	109.7	11.2	353.3	15.6	44.3	44.8
November	242.8	19.0	108.7	11.0	353.2	15.6	37.3	35.2
1986								
January	256.9	20.1	114.3	11.7	371.1	16.4	36.5	23.7
February	253.6	19.8	113.6	11.6	367.2	16.3	37.7	42.1
**February	250.9	19.6	111.8	11.4	362.7	16.1	N/A	N/A
March	248.8	19.5	110.6	11.3	359.3	15.9	35.2	38.6

**Unadjusted unemployment figures for march 1986 onward are not comparable with previously published figures. Revised February figures are provisional and may be subject to amendment.

Source: Department of Employment

"acceptable" level of unemployment.

In the recent past John Prescott (Labour's employment spokesman) has claimed that the "true" level of unemployment in the UK is around 5m, whereas the official figure is around 3.28m. In contrast, Sir Michael Edwards has argued that the official estimate considerably overstates the extent of "real" unemployment which he estimates to be 1.5m (see, eg, Lipsey, 1985). In Scotland a **pro rata** distribution around the official figure of 334,000 (excluding school leavers) would produce a high estimate of well over half a million, an order of magnitude which Scottish trade unionists have often claimed and a low estimate of not much in excess of 150,000.

How is such an enormous disparity of estimates for an apparently straightforward matter of fact possible? Part of the problem may stem from discrepancies in the concept of unemployment among different groups, but most seem to have in mind something rather similar to the "economists" definition given above. Undoubtedly the major source of variation in estimates of unemployment is to be found in the condition that the unemployed should be "actively seeking" employment. At the operational level, this condition is open to a number of interpretations.

Before proceeding to consider which of the estimates is based on the most reasonable interpretation of the key criterion, however, we have to consider the effects of recent changes in the methods by which the official unemployment data are constructed. The official answer to "how much unemployment?" depends to a considerable degree on not only to whom the question was posed but also on when it was posed. The definitions on which estimates of unemployment are based have been subject to much change in the recent past. For example, the July 1985 issue of the Department of Employment's Gazette reports a new series for unemployment which is revised back to 1971 using the current official definition. This yields lower estimates of unemployment than previous definitions. One suspects that the public's perception of the unemployment problem is most closely related to the widely-reported official estimates. Whilst redefining official unemployment clearly does nothing to tackle the underlying problem, cynics maintain that it may do something to relieve political pressure on the Government.

On the face of it changes introduced since 1979 provide ample fodder for the sceptics. For example, in July 1980 those seeking part-time employment were counted separately. From the initial UK estimate of 41,000 the total had grown to 52,000 by September 1982 but no further figures are available. In July 1981, the registration requirements for the older long-term unemployed were relaxed, resulting in an estimated 30,000 leaving the UK register by May 1982. In July 1982 unemployment benefit became liable for tax and single parents were encouraged to claim (untaxed) supplementary benefit, which is not subject to the requirement that recipients must be "available for work". There is no estimate of the impact of this on UK unemployment. (Source of data on changes: eg IDS Report 456, September 1985.)

Undoubtedly, however, the biggest single change in the method of measuring official unemployment occurred in October 1982 when the system was altered from one based on a manual count of those registering to one based on the numbers actually in receipt of benefits. This had three main effects. First, and most importantly, those who were previously registered as unemployed but ineligible for benefits were removed from the register. This affected mainly married women and school leavers who cannot draw supplementary benefit within a specified minimum time interval. It was estimated that this reduced recorded UK unemployment by 161,000. Secondly, because the new system was computerised and the benefits system made more up to date, the delay between an unemployed person finding work and this being officially recorded was reduced. This was estimated to have reduced the official UK count by 108,000. Thirdly, the new system could not separately identify severely disabled people, so that around 23,000 were added to the total of unemployed. The net effect of these changes was to take 246,000 off the UK register. The corresponding figure in Scotland was 25,800 with disproportionate effects especially on female unemployment and, to a lesser extent, on the pattern of school leavers unemployment (see Bell, 1983).

There was a further change in the unemployment count in April 1983 which had the result of reducing measured UK unemployment by 161,800 (by August 1983). The change exempted some men aged 60 and over from the need to sign unemployment benefit office. It is estimated that the total effect on Scottish unemployment was a reduction of around 11,400.

The most recent change in the measurement of unemployment took effect in March 1986. From that date on the figures are compiled 3 weeks after the count date, whereas previously only a one week delay was involved. The additional two week period allows more claimants who ceased to be unemployed on or before the count date to be excluded from the count. Under the old system this information would not have reached the Unemployment Benefit Office in time. Consequently the new count provides a more accurate measure of those claiming benefit at a particular point in time.

The estimated average monthly effect of this change is to reduce measured Scottish unemployment as follows:

	Male	Females
Excluding school leavers	2,590	1,770
School leavers	110	100
Including school leavers	2,700	1,870
Total	4,570	

Source: Department of Employment Press Notice: 466/86)

In February 1986, these revisions caused the total male and female unemployment rates to fall by 0.2%. Tables 5 and 6 show that the underlying trend in (consistent estimates of) unemployment remains upward. The likely net effect of the oil price fall upon the Scottish economy as a whole, and therefore on unemployment is, as yet, difficult to establish.

The changes in the system of measurement were justified in terms of savings in administrative costs, in terms of increasing convenience for those exempted from registering under the modified rules and, in some instances, in terms of improved accuracy. These factors seem by and large to provide quite a reasonable rationale for change. However, sceptics might question whether cost saving exercises which would have increased the unemployment count would have been pursued with equal vigour, and whilst acknowledging the possible benefits of, for example, excluding older men from the need to sign on, they might worry that "forgotten statistics are often forgotten people as well" (IDS Report 456, p28).

Whatever the judgement on the changes in the system of recording, there seems little doubt that officially recorded unemployment departs in some respects from the criterion that workers should be "actively seeking" employment. John Prescott's estimate of 5m unemployed in the UK laid heavy emphasis on those excluded from the official count who perhaps should be included by this criterion. To the official figures were added three categories of individuals (Lipsey, 1985). The first category comprised the approximately 400,000 eliminated from the register as a consequence of changes in recording practices instituted by the present Government (especially the October 1982 and April 1983 changes). In Scotland the same adjustment would increase estimated unemployment by around 41,770 (or 11% of current Scottish unemployment levels). The second covered that group of workers, traditionally known as the 'hidden unemployed', who are seeking employment, but do not register as unemployed because they are not entitled to benefits. The 1984 Labour Force survey (discussed in the Department of Employment (DE) Gazette, October 1985) found that there were about 870,000 such individuals. A very crude **pro rata** adjustment (with total employment in December 1984 as the base) yields an estimate of around 79,000 for hidden unemployment in Scotland. Finally, the 600,000 workers on Government financed "job creation" measures (the most important of which is YTS) in the UK were added to official unemployment on the grounds that these are not "real" jobs. In Scotland there are currently estimated to be around 110,000 people covered by the various schemes.

The total additions to the official estimate of unemployment (3.28m) for the UK from these three sources is 1.87m, giving arise to an overall estimate in excess of 5m. For Scotland the comparable addition to the official estimate of 362,700 is 230,700 yielding an overall figure of around 593,470. This last estimate, however, should be regarded with even greater caution than its UK counterpart because the biggest single adjustment has been arrived at in a particularly crude fashion.

Do these adjusted figures get closer to the criterion of "actively seeking" work? Consider each of the adjustments in turn, beginning with that for changes in measurement made by the present Government. There seems little doubt that those married women and school leavers precluded from registering as unemployed by the October 1982 revision must be considered unemployed in the sense we use the term (161,000 in the UK). However the treatment of the impact of computerisation is more problematic, since, in itself, this led to downward revisions of unemployment estimates as a consequence of enhanced accuracy of measurement. The desire for a consistent series on "old" official measures would validate the adding back of this element, but our criterion does not. The severely disabled, included as a consequence of the changes, should clearly be taken out of unemployment altogether on our criterion. Together, these comments suggest a net upward revision to the UK figures of about 138,000. If the proportionate allocation of the net effect of all October 1982 changes to computerisation **per se** in the UK (44%) were applicable to Scotland, the net upward revision would be around 14,450.

The April 1983 modification which exempted some over 60s from registration could perhaps be rationalised on the grounds that they may be judged to be **effectively** retired. However, this judgement seems based on the implicit assumption that they will be **unable** to find work, and most likely has nothing to do with their willingness to do so. On that basis these individuals should be added into the unemployment estimates. The total net upward revisions to official estimates to counteract changes in the method of construction which operate against the spirit of the "actively seeking" criterion are 300,000 in the UK and 25,850 in Scotland. Considered in isolation, the most recent change can be regarded as improving accuracy of measurement (albeit of the wrong concept of unemployment) and does not, in itself, call for upward revision of new official estimates to meet the "willing to work" criterion.

Addition of those (primarily married women) "hidden unemployed" is clearly appropriate in the present context. However, it is often argued that many of those actually registered as unemployed are not actively seeking employment and so should be deducted from the official estimate. The recent (sample-based) Labour Force Survey (DE Gazette, October) estimated that some 940,000 of claimants did not actively seek work **in the reference week of the survey.** Of these, 200,000 said they had a paid job, although it is not clear whether such jobs violated the terms of registration. Of the remaining 740,000, 17% gave as the main reason for not actively seeking work the fact that they were long-term sick or disabled (a category we have already allowed for). A further 26% said that they were looking after the home (just over 50% of females gave this response), 8% were retired and 7% did not want or need employment.

The biggest proportion (28%) said that they had not searched in that week because they believed there were no jobs available. The remainder had either not yet started looking (3%) or gave other reasons/no reply (10%).

Among these categories there is little doubt that the sick and disabled, retired and those not wanting/needing a job should be excluded from the "unemployed" on an economist's definition of the term. However, it seems rather extreme simply to assume that the "hidden unemployed" and non-participants among the registered unemployed just offset each other. First, the question used to identify non-participants was particularly restrictive, focussing on the reference week of the survey only. Secondly, and very importantly, individuals' self-classification may well vary with their labour market experience. Indeed there is direct evidence of this in the survey response in that a large number of 'non-participants' gave a perceived absence of employment prospects as a reason for not actively seeking work in the reference week. Similarly those classifying themselves as "retired" or "looking after the home" may do so on the assumption that employment is simply not attainable. This dependence of individual's "tastes" on the general economic environment creates major problems the general economic environment creates major problems for Monetarist conceptions of a 'natural rate of unemployment' which is presumed to be (at least ultimately) independent of aggregate demand.

There are reasons for believing then, that the current official unemployment figures, of 362,700, probably represents a lower bound esimate of those actively seeking employment. The estimate obtained by application of the methods recently employed by the Labour Party in a UK context, ie nearly 600,000, on the other hand, can be regarded as an upper bound on the "true" level of unemployment.

INDUSTRIAL RELATIONS

The announcement, by the Secretary of State for Scotland, of the establishment of an independent Committee of Inquiry to examine education, effectively brought to an end nineteen months of industrial action by teachers. However, the emphasis in the terms of reference to make recommendations in the light of the requirement to "observe public expenditure restraint..... and in all respects the need to take account of what can be afforded" may reduce the likelihood of attaining a lasting settlement. Moreover, short-term problems remain. Strathclyde faces the prospects of having to close up to twenty primary schools and several secondary schools, which will severely test the effectiveness of retraining and other schemes. Elsewhere the public sector continued to dominate industrial relations issues in Scotland. Announcements of possible redundancies were made by Strathclyde Passenger Transport Executive (up to 600 jobs and the closure of two garages), and Greater Glasgow Health Board (up to 700 jobs in 1987 even though the Nursing Manpower Study noted that there was sufficient work to warrant 1,000 extra nursing jobs).

Uncertainties as to the placement of naval orders prompted renewed fears of insecurity at Yarrows, Govan Shipbuilders and Clark-Kincaid's marine engineering works at Greenock. The issue of redundancy also underlay the eight week strike at British Steel's Scottish Tube Works.

The national newsprint industry provided the major dispute in Scotland. Underlying the dispute involving employees at the Daily Record and Sunday Mail was Robert Maxwell's attempts to cut production costs (by extending the range of publications) and reducing the volume of journalistic work (by the introduction of five 'fax' machines at Anderston Quay which would receive made-up pages from the Mirror).

However, events at Anderston Quay tested the credulity of most observers. Over a two month period employees were sacked three times; faced with negotiations once and ultimatums twice, offered expansion and redundancies twice; heard proposals to introduce a North of England version of the Record, a northern version of the Mirror (provisionally called Record and Mirror) an Irish daily paper (Mirror Incorporated), and a Scottish Mirror. At various stages: phones were cut off, barbed wire erected and dismantled; guard dogs hired and dimissed; injunctions sought; and, new companies formed. Publication resumed in April following agreement to extend the working week and limited, but voluntary, redundancies.

The cause of good industrial relations in Scotland lost one of its ablest advocates with the death of James Milne, the General Secretary of the STUC. His eleven years as General Secretary witnessed a major decline in the Scottish manufacturing base, yet his efforts frequently ensured that action against closures became causes embraced by all. Despite declining membership, he maintained and even increased the influence of the STUC in Scottish life and affairs. Unfailingly courteous and polite, he wished continuously for the betterment of the people in Scotland. His abilities to bring consensus in awkward and complex disputes will be missed by all.

Regional Review

The seasonally adjusted rate of unemployment for Scotland rose by 0.2% (5,200) in the year to April 1986. However, due to changes in the compilation of the monthly unemployment statistics from march 1986, comparisons of current with past figures for the regions and travel to work areas (TTWAs) are no longer possible. It has been estimated that the effect of this latest change will be to reduce the reported unemployment rate by some 1.5%, or approximately 5,100, in Scotland.

Table 1 reports a very slight fall in the level of unemployment (unadjusted) in the month to 10 April 1986. The regions experiencing the largest falls were Highland, Borders and Dumfries and Galloway with rates of 6.9%, 5.3% and 5.3% respectively. Although unemployment rose in only three regions, Grampian, Fife and Central, it may be significant that the largest rise, of 2.3% came in Grampian perhaps reflecting the first effects of the recent collapse in oil prices and acting as a portent for the future. Overall, unemployment remains stubbornly high in most regions.

Turning to the sexual pattern of unemployment (Table 2), the male rate fell over the month in all but two regions, Grampian and Central, but generally by less than one percentage point. The pattern of change in women's unemployment is less clear with the rate falling in six regions, rising in four and remaining static in two. In every region with the exception of Highland, the change in the female rate was half of a percentage point or less. Although the changes between March and April are small in magnitude they appear to favour males slightly more than females.

As Table 1 adequately illustrates there is a considerable diversity of unemployment

Table 1 Unemployment by Scottish region

	Total Apr 86	Change since Mar 86	% rate Apr 86
Borders	3,689	- 196	9.7
Central	19,159	35	16.5
Dumfries & G/way	7,910	- 417	13.8
Fife	22,517	100	16.9
Grampian	19,091	446	8.7
Highland	13,274	- 919	16.1
Lothian	46,169	- 450	12.7
Strathclyde	195,79-	- 715	18.7
Tayside	25,682	- 409	14.8
Western Isles	1,831	- 50	18.8
Orkney	810	- 35	12.2
Shetland	754	- 32	6.4
Scotland	356,676	-2,642	15.8

Source: Department of Employment

Table 2 Unemployment rates: males and females

	% rate April 86		Change since March 86	
	Males	Females	Males	Females
Borders	10.7	8.3	- 0.7	- 0.3
Central	19.6	12.4	-	0.1
Dumfries & Galloway	15.2	11.9	- 0.8	- 0.5
Fife	19.5	13.4	- 0.2	0.4
Grampian	9.1	8.1	0.3	0.2
Highland	18.1	13.2	- 1.1	- 1.3
Lothian	16.1	8.7	- 0.2	- 0.1
Strathclyde	23.6	12.3	- 0.1	-
Tayside	17.6	11.4	- 0.4	-
Western Isles	23.4	12.6	- 0.7	- 0.2
Orkney	14.2	9.3	- 1.0	0.2
Shetland	6.3	6.5	- 0.3	- 0.3
Scotland	**19.3**	**11.2**	**- 0.2**	**- 0.1**

Source: Department of Employment

experience across the regions, from a rate of 6.4% in Shetland to one of 18.8% in the Western Isles. However, the spatial distribution of unemployment varies not only across regions but within regions. In order to illustrate this point Table 3 compares the TTWAs with the highest and lowest unemployment rates within each region. The unevenness of the distribution of unemployment is most glaring in Grampian where the Forres TTWA has an unemployment rate which is 3.9 times greater than that of Aberdeen. The intra-regional distribution of unemployment is also noticeably uneven in Dumfries and Galloway and Lothian where the highest figures exceed the lowest by factors of 2.5 and 2.1 respectively. The pattern of unemployment is more evenly spread in Central and Fife. Further evidence of the variations in unemployment rates within regions appears in the final column of Table 4 where the number of TTWAs within a region which exceed the region's own average unemployment rate are noted. In Grampian eight of the nine TTWAs exceed the region's average but the ninth and largest, Aberdeen, has a markedly lower rate and exerts a downward influence on the average. In a similar vein, five of the seven TTWAs in Dumfries and Galloway exceed the regional average with the Dumfries TTWA exerting a downward force on the average.

Table 3 TTWA with highest and lowest unemployment rates

		%	High - Low	Low - Low
Borders	H Berwickshire	15.6	7.5	1.9
	L Galashiels	8.1		
Central	H Alloa	18.0	3.8	1.3
	L Stirling	14.2		
Dumfries & G/way	H Cumnock & Sanquhar	26.6	16.0	2.5
	L Dumfries	10.6		
Fife	H Kirkcaldy	18.4	6.9	1.6
	L North East Fife	11.5		
Grampian	H Forres	27.1	20.2	3.9
	L Aberdeen	6.9		
Highland	H Skye & Wester Ross	21.3	9.5	1.8
	L Thurso	11.8		
Lothian	H Bathgate	21.3	11.0	2.1
	L Haddington	10.3		
S/clyde	H Irvine	25.7	12.1	1.9
	L Islay/Mid Argyll	13.6		
Tayside	H Arbroath	18.6	8.1	1.8
	L Perth	10.5		

Source: Department of Employment

Table 4 also emphasises inter-regional differences by reporting the number of TTWAs in a region in which the unemployment rate exceeds the Scottish average. A "high unemployment" region would be one like Strathclyde in which a large proportion of the TTWAs have unemployment rates greater than the Scottish figure. In the Strathclyde case ten of the twelve TTWAs have unemployment rates above the Scottish average while in Highland six of the eight TTWAs are in that position. In contrast, in none of the Borders TTWAs does the unemployment rate reach the Scottish average, while only two of the nine Grampian TTWAs and two of the seven in each of Tayside and Dumfries and Galloway exceed the Scottish

Table 4 TTWA in region with unemployment rates above Scottish and regional average

	No of TTWA	No above Scottish average	No above regional average
Borders	5	0	2
Central	3	2	2
Dumfries & Galloway	7	2	5
Fife	3	2	1
Grampian	9	2	8
Highland	8	6	4
Lothian	3	1	1
Strathclyde	12	10	5
Tayside	7	2	2

Source: Department of Employment

figure. Excluding the Island Authorities, Table 4 confirms that the last four mentioned are Scotland's relatively "low unemployment" regions.

The data provided thus far give little indication of the dynamics of the labour market, and in fact tend to convey the impression that little change is taking place. However, the relatively small net changes in the regions' unemployment rates do not necessarily imply small changes in the gross components. Tables 5 and 6 present the rates of flow to and from the register in the month to 10 April. Table 5 measures the rate of flow of people leaving the register, and if all unemployed people were alike this could be regarded as the probability of an unemployed person leaving the register in March-April. Thus in the period under review the probability of leaving the register was greatest in Borders, Shetland and Grampian. It need not be the case that people leave the register in order to take up employment - some may have withdrawn from the labour force but it is perhaps significant that the three regions with the highest off-flow rates are also those with the lowest unemployment rates. The off-flow rate is greater for women in six of the regions and for men in five. In Grampian the female off-flow rate is particularly high at 32.2%. In all but three of the regions, the on-flow rate to the register was greater for women than for men. The highest overall on-flow rate was recorded in Grampian, 23.6%. This rate is some 6.7 percentage points greater than any other region and, as mentioned above, may be due to the effects of falling oil prices.

In the case of both on-and off-flows the regions with the highest rates tend to have the lowest unemployment rates. This seems to suggest that the more buoyant regions not only have a greater proportion of people in jobs but also that there are greater amounts of job change and/or employment generation in these areas. The reverse of this phenomenon is to be found in a high unemployment area such as Strathclyde in which the off- and on-flows were only 10.9% and 12.0% respectively. It would appear that depressed areas experience not only high unemployment rates but also more sluggish change than the relatively better-off regions.

Table 5 (Off-flow)/stock March-April 1986 (%)

	Male	Female	All
Borders	21.2	20.6	21.0
Central	13.1	18.6	13.4
Dumfries & Galloway	12.8	16.9	14.0
Fife	12.5	12.5	12.5
Grampian	11.8	32.2	18.8
Highland	17.2	16.0	16.8
Lothian	12.4	16.0	13.5
Strathclyde	9.8	13.8	10.9
Tayside	15.0	11.5	13.1
Western Isles	14.9	15.1	15.0
Orkney	16.5	10.7	14.7
Shetland	20.1	19.9	20.0

Source: Department of Employment

Table 6 (On-flow/stock March-April 1986 (%)

	Male	Female	All
Borders	16.1	18.4	16.9
Central	14.2	15.7	14.7
Dumfries & Galloway	10.6	13.5	11.5
Fife	12.5	16.7	13.9
Grampian	24.4	22.0	23.6
Highland	13.1	15.7	14.0
Lothian	13.4	16.4	14.3
Strathclyde	10.6	15.3	12.0
Tayside	12.8	14.8	13.5
Western Isles	14.6	14.5	14.6
Orkney	11.0	12.6	11.5
Shetland	17.6	15.3	16.7

Source: Department of Employment