Scottish Engineering

Quarterly Review

DECEMBER 2009

ENGINEERING SECTOR SEES POSITIVE RISE IN OPTIMISM

- Order intake best for 18 months
- Optimism goes positive
- Output volume improving
- Electronic order intake stabilises
- Larger companies performing better

The last Quarterly Review figures from our member companies are the most encouraging for the past 18 months. While overall figures tend to remain negative, with the exception of optimism, we note that it is our smallest companies which are suffering most.

Indeed, most indicators from our largest companies have gone positive particularly in order intake and output volume while pressure remains on recruitment and capital investment projects.

The data confirms what members have been reporting directly to me in our latest round of District Meetings where there is an ongoing determination to keep a close watch on the cash flow being reflected in the continuing negative response to capital investment plans.

Within the engineering sector our machine shops are really feeling the pain with fabricators not far behind. This would appear to be resulting from larger companies retaining a larger proportion of their work in-house rather than sub contracting.

While we are delighted that the Westminster government has identified 10 potential sites for new nuclear build we are extremely disappointed that Scotland will lose out unless the Scottish Government moves from its continuing intransigent position on this vital issue. Failure to recognise that nuclear is a key element in providing a balanced, affordable, sustainable and secure energy supply alongside renewables will result in the loss of expertise and job opportunities in Scotland.

Bearing in mind the significant improvement in the data which we are reporting this quarter, I am sorry to end this article on a negative note, but it is vital that we continue to emphasise to the Scottish Government the importance of the nuclear contribution to our energy requirement.

DR PETER HUGHES, OBE FRENG
Chief Executive
Scottish Engineering

ANNUAL TRENDS

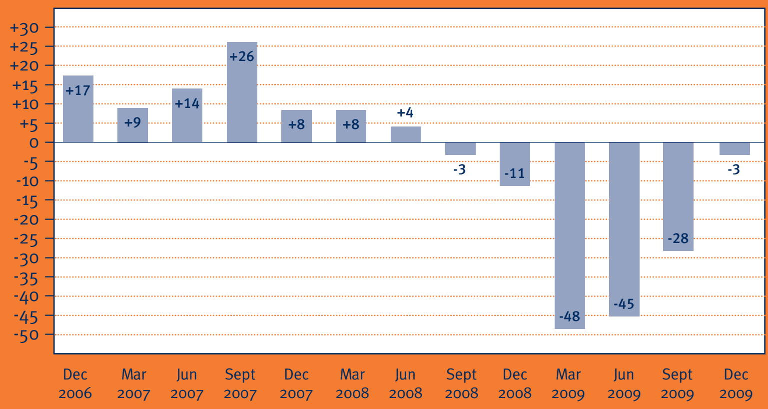
The general order intake figures are the best since quarter 3 2008 and have made a considerable improvement on the previous quarter.

Output volume has seen a great improvement since last quarter and is better than the whole of the previous year.

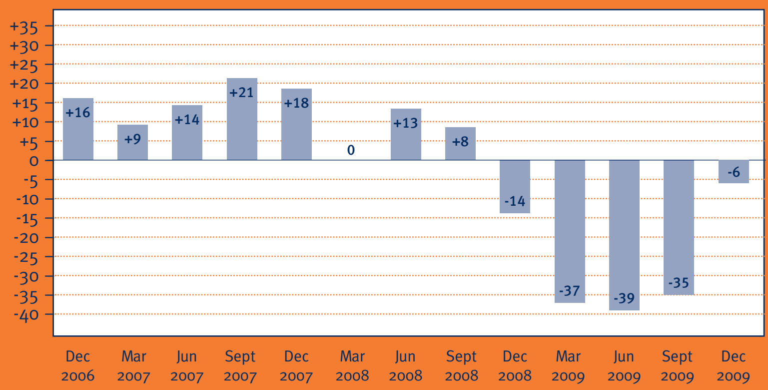
Similarly capacity utilisation has shown substantial gains over all figures in the previous year. Recruitment levels have also moved closer to being positive, again providing the best results for a year.

Training investment plans are not positive or negative but sit on the balance. Capital investment plans remain negative, having made a slight improvement on the last quarter.

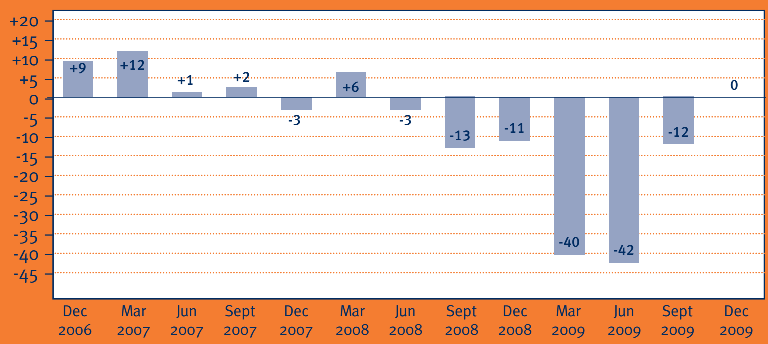
ORDER INTAKE



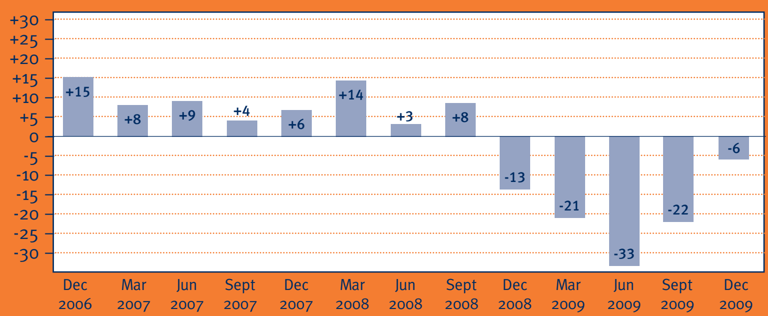
OUTPUT VOLUME



EXPORTS

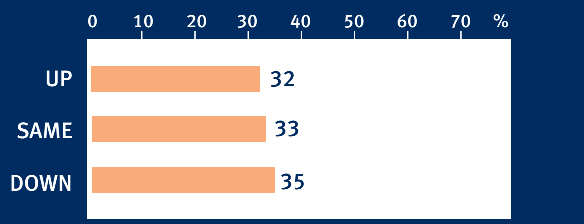


STAFFING

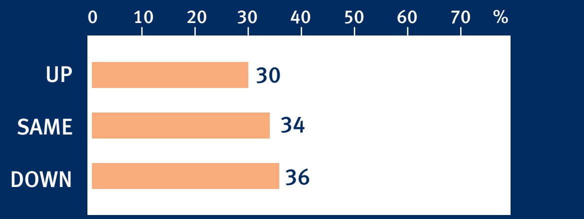


Balance between reports of increases and reports of decreases

ORDER INTAKE



OUTPUT VOLUME



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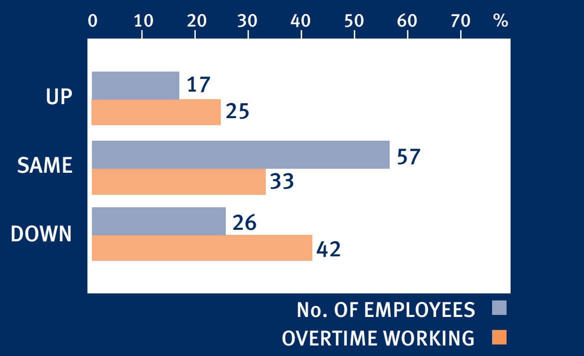
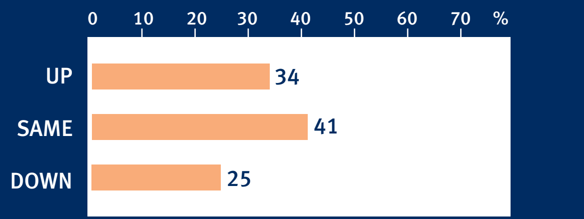
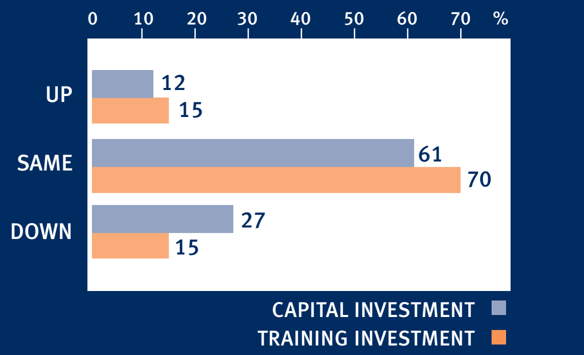


OPTIMISM



INVESTMENT



ORDER INTAKE

The overall level of orders is the best since 2008 with large and medium companies reporting positive figures.

OUTPUT VOLUME

Improvement is seen for large and medium sized companies while small companies continue to suffer. The electronic sector has reported a positive result.

STAFFING

Overall numbers of employees continue to decline but at a much slower rate. Overtime working remains negative in small and medium companies but is positive in large companies.

OPTIMISM

Companies are more optimistic than they have been since quarter 1 in 2008 across all sizes of company.

INVESTMENT

Capital investment plans remain under pressure as companies hold on to cash while training investment cut backs are only seen in small companies.

The rise in order intake and output volumes generally, though still remaining negative, is regarded as the reason there has seen an overall improvement in optimism. This final survey of 2009 – the most heartening of the year - sees improvements across a number of disciplines and sectors. While not quite taking the manufacturing sector out of negative figures it appears to be moving in the right direction.

Orders

The overall total order intake (32%up,33%same, 35%down) is the best figure for 18 months but is still negative. Only small (26%up, 36%same, 38%down) companies report negative figures while medium (36%up,31%same,33%down) and large companies (70%up,20%same,10%down) have moved into the positive area.

UK orders in general (23%up,44%same,33%down) have made improvements over the last quarter while still remaining negative as are small companies (23%up,38%same,39%down). Medium companies (22%up,56%same,22%down) have equal numbers of companies reporting increases as are reporting decreases. Large companies (30%up,50%same,20%down) have reported positive figures.

Mechanical equipment (27%up,48%same, 25%down) and fabricators (38%up,31%same, 31%down) have moved to a positive position, leaving behind machine shops (11%up,45%same, 44%down) and metal manufacturing (0%up, 11%same, 89%down).

Forecasts for the next three months show small companies (25%up,49%same,26%down) improving, medium companies (22%up, 49%same,29%down) falling back slightly and large companies (30%up,60%same,10%down) making further positive moves. Machine shops (33%up,56%same,11%down) are predicting a swing into positive figures.

Export orders in general (30%up,40%same, 30%down) show as many companies declining as are improving. Small companies (25%up, 41%same,34%down) remain negative, medium companies (30%up,40%Same,30%down) report an equal number of ups and downs while large companies (71%up,29%same,0%down) are in a positive position.

Mechanical equipment (29%up,45%same, 26%down) shows a robust export order intake as opposed to machine shops (0%up,50%same, 50%down) and metal manufacturing (12%up, 38%same,50%down) which are both negative.

Predictions for export orders for the next quarter in general (25%up,55%same,20%down) show an improvement which is reflected in small (19%up,62%same,19%down), medium (26%up,51%same,23%down) and large companies (62%up,26%same,12%down).

Prices and margins

UK prices in general (6%up,72%Same,22%down) continue to be negative as do small (6%up, 67%same,27%down) and medium companies (7%up,76%same,17%down) while large companies (10%up,90%same,0%down) are positive, although 90% of large companies showed no change.

In the next three months UK price forecasts in general (9%up,75%same,16%down) remain negative as do small (13%up,79%same,8%down) and medium companies (10%up,70%same, 20%down).

Export prices for the last quarter overall (9%up, 84%same,7%down) are positive as are small (11%up,83%same,6%down) and large companies (10%up,90%same,0%down) but medium companies (5%up,84%same,11%down) are unable to match this level and remain negative.

The forecast for the next three months in general (14%up,72%same,14%down) sees equal numbers of companies with prices rising as have prices falling. Small (13%up,79%same,8%down) and large companies (38%up,50%same,12%down) both hope to remain positive while medium companies (10%up,67%same,23%down) are predicting they will be negative.

Optimism

In general the levels of optimism (34%up,41%same,25%down) has returned to a positive situation after five consecutive negative quarters. All three sizes of company small (30%up,41%same,29%down), medium (39%up,43%same,18%down) and large (50%up,40%same,10%down) have all increased their optimism. Within the various sectors, electronics (56%up,33%same,11%down) and mechanical equipment (36%up,44%same, 20%down) are positive while fabricators (25%up,37%same,38%down) machine shops (11%up,45%same,44%down) and metal manufacturing (8%up,30%same62%down) are negative.

Investment

Plans for capital investment plans in general (12%up, 61%same,27%down) remain negative as companies continue to conserve cash. Overall training investment plans (15%up, 70%same,15%down) have a similar number of companies planning to increasing their training as plan to make cuts in their training plans.

Staffing

Staffing levels in general (17%up,57%same, 26%down) remain negative, though considerably less so that in the previous three quarters. This is mirrored in small (16%up,60%same,24%down). medium (16%up,58%same,26%down) and large companies (20%up,40%same,40%down).

Forecasts for the next three months in general (14%up,66%same,20%down) remain negative, but less so. Similarly this is the case in small (13%up,71%same,16%down), medium (14%up,60%same,26%down) and large companies (20%up,50%same,30%down).

Overtime working generally (25%up,33%same, 42%down) is down for another quarter which is true for both small (24%up,33%same, 43%down) and medium companies (26%up, 32%same,42%down) but large companies (40%up,30%same,30%down) are positive.

Output volumes

Overall output volumes (30%up,34%same, 36%down) remain negative as they are in small companies (23%up,34%same,43%down). However, medium (36%up,40%same,24%down) and large companies (70%up,10%same,20%down) show positive figures. Electronics (33%up, 45%same,22%down) and mechanical equipment (37%up,37%same,26%down) have similarly positive returns while fabricators (27%up, 20%same,53%down) and machine shops (0%up,33%same,67%down) remain negative.

The forecast for the next three months in general (29%up,41%same,30%down) is less negative. Small (31%up,44%same,25%down) and large companies (50%up,10%same,40%down) are predicting that they will be positive while medium companies (21%up,41%same,38%down) predict that they will remain negative.

The facts in this Review were acquired by a survey of Scottish Engineering's members and certain other electronic companies and foundries. The membership covers all sectors of the industry. The response rate was 35.9% of members. Companies are described as: Small (less than 100 employees), Medium (100-500) and Large (over 500).

Scottish Engineering

The Back Page

Owen Kelly
Chief Executive
Scottish Financial Enterprise

Looking back over 2009, it was a year in which the wider impact of the banking crisis became all too painfully apparent. The economies of many countries around the globe suffered, and we saw rising unemployment, falling property prices and the loss of some retailers and manufacturers of long standing.

Within the financial services industry itself, after the volatility of 2008, there was a return of greater stability, thanks, in large part, to the support of governments. As the representative body for financial services in Scotland, Scottish Financial Enterprise is acutely aware of the debt our industry owes to the UK taxpayer.

We also began the long process of learning lessons from the past. Government reports and parliamentary inquiries highlighted a mix of unacceptable risk-taking in some institutions; product innovations that in some cases exceeded the limits of understanding among those deploying them; an explosion of easy credit, and regulation that failed to see the full picture.

Companies, rightly, apologised for their mistakes, and relevant industry leaders were replaced.

Changes in regulation also followed. This process continues, as politicians decide on the best ways to tighten domestic regulation, while seeking to avoid setting UK companies at a competitive disadvantage internationally.

A third aspect of change is in financial services companies themselves. The most obvious impact has been on the banks which were in the front line of the crisis. Those banks, and others around the globe, have undergone major business and internal restructuring in the year, and this will continue into 2010.

Bank lending

One of the most difficult issues in the wider economy has been the impact on business lending. SMEs have been vocal in their criticism of banks, citing a reduction in willingness to lend, and a rise in the cost of borrowing.

Meanwhile the banks are clear that lending remains a core part of their business.

A few statistics - RBS has made an extra £3bn of funds available to SMEs through its regional SME funds initiative, including £250m for Scotland. The bank is approving the same level of applications for SME lending - 85% - as it did before the financial crisis.

Clydesdale Bank advanced nearly £3bn of new lending in the first nine months of 2009, with the pledge of a further £1bn as and when customers need it.

And both RBS and LBG have specific lending commitments through the Enterprise Finance Guarantee scheme (launched in January 2009) as part of the support they receive from government.

But we do acknowledge that the lending environment has changed. One of the reasons for that is the increased cost of funding for the banks themselves, which means they must in turn reflect that in their lending.

We must also acknowledge that the situation of many borrowers has changed. Collateral such as property has in most cases declined in value, sales projections may be down, growth expectations may well have been cut. So, the level of risk attached to lending to them has increased, leading to an increase in cost. If banks didn't recognise these changing risk profiles, they would be lending at risk and perhaps storing up problems for the future. To avoid a recurrence of the crisis, banks must ensure tighter scrutiny of borrowing propositions. This means pricing credit more accurately and that, in turn, suggests that it has been underpriced in the past.

Banks are in the middle of quite contradictory pressures, reflecting their central role in the economy. We are not complaining, but it is oversimplification to say that funding is being taken from the taxpayer and then hitting a bottleneck in banks. Indeed, the banks are clear that they are in the business of lending – it's what they do – and they will continue to work with customers to offer commercial loans, albeit in a difficult climate.

The year ahead

The focus on financial services has primarily been on the banks. That is understandable, but Scotland's financial services industry is much more diverse – we have great strengths in a wide range of sectors including insurance and pension, fund management and asset services.

The industry has a 300-year-old history in this country, and employs over 90,000 people. Even through the crisis we have continued to attract new business to Scotland from other parts of the UK and from overseas.

We owe it to those skilled employees to get through this period and restore our industry's reputation, particularly among our customers in other areas of commerce and manufacturing. My focus next year will be on working with companies, governments and regulators to do that.

The views expressed on 'The Back Page' are not necessarily those of Scottish Engineering.

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