State of the Economy

September 2019

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State of the Economy Office of the Chief Economic Adviser	September 2019

State of the Economy

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This report summarises recent developments in the global, UK and Scottish economies and provides an analysis of the performance of, and outlook for, the Scottish economy. Updates are provided on a periodic basis and the data and analysis in this edition are correct up to and including 18 September 2019.

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Overview

Growth in the Scottish economy has slowed through the first half of 2019 with continued Brexit uncertainty and a weakening in the wider UK and global economic environment impacting investment, sentiment and output. The analysis in this reports shows clearly the risks of a slowing economy, the continued impact of weak business investment on jobs and productive capital, which reflect the on-going Brexit uncertainty.

The contraction in output in Scotland in quarter 2, which reflects the unwinding of stock accrued by businesses in quarter 1, was not unexpected as the same pattern is evident in UK data (a contraction in quarter 2) and was widely anticipated.

However, the continued uncertainty relating to Brexit and the fact that business behaviour is still skewed to short term mitigation, rather than investment for growth or productivity, is impacting the economy more directly and weakening the overall resilience of businesses, which is a worrying trend and a risk to the economy. Updated analysis in this report considers the impact that this prolonged period of uncertainty could have and estimates that it could reduce or defer the level of business investment in Scotland by a further £0.5 billion by the start of 2020-21.

Scotland's labour market continues to perform strongly by historical standards, however the latest data shows a rise in unemployment in Scotland, albeit from record low levels. This, alongside continuing weak investment, the unwinding of business stocks, and subdued business and consumer sentiment, indicate that the economy is more vulnerable to an external slowdown and the risks of a No Deal Brexit from earlier in the year.

This contrasts with the position through 2018 in which the economy remained resilient, driven by continued strong domestic consumer demand, tourism and improvements in net trade. The latter reflects Sterling depreciation and new analysis in this report shows that Sterling depreciation may have had a greater impact on imports than on exports. However, more broadly, the slowdown in external activity, coupled with the continuing Brexit related risks, is now clearly impacting the economy in Scotland.

This makes predicting future growth more difficult as there is still no clarity on the form of Brexit - even in a No Deal scenario - and the extent to which there may be mini agreements or transition arrangements for parts of the economy. The independent forecasts for the Scottish economy reflect this uncertainty though most still assume some form of orderly EU exit and transition.

In contrast the recent Fiscal Risks report from the OBR (July 2019) suggests that the UK could contract through 2020 by around 1.4 per cent based on their most recent assessment, whilst the Bank of England suggest output lost to the economy could be as much as 5.5 per cent in the advent of a No Deal disorderly Brexit. It is our assessment that a No Deal Brexit would have an immediate dislocation for the economy and lead to a contraction in output in Scotland through 2020 and rising unemployment. The scale of the downturn could be potentially worse if external conditions continue to soften also and the economy continues to be weakened in the run up to any EU exit.

Global Summary

Global activity remains subdued in 2019.

- Global growth slowed over the year to 3.6% in 2018 and has remained relatively subdued in the first half of 2019.
- Slower growth over the year has been relatively broad based in Advanced and Emerging Market & Developing Economies.
- The IMF forecast global growth to slow further in 2019 to 3.2% before picking up to 3.5% growth in 2020.

Global trade activity has weakened in 2019.

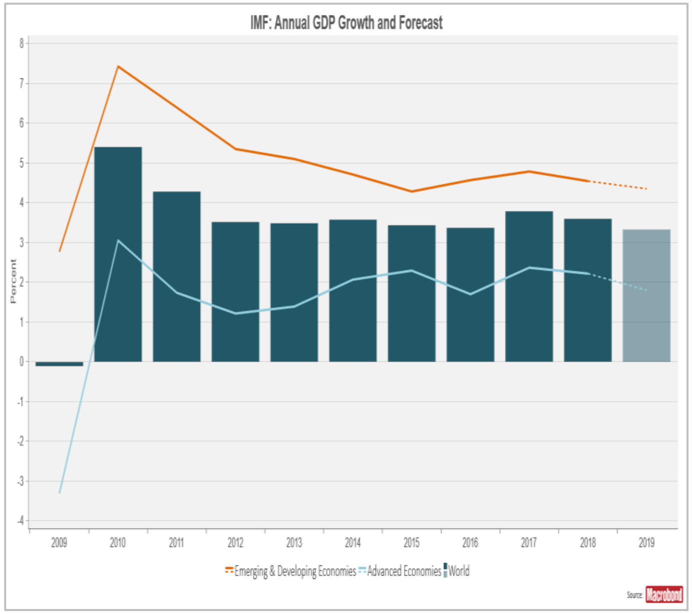
- Growth in world trade volumes has remained weak in 2019 amid heightened global trade tensions.
- The new Trade Uncertainty Index shows heightened uncertainty throughout 2019.
- Softening demand and trade has been reflected in global financial markets with equities growth easing during the year.

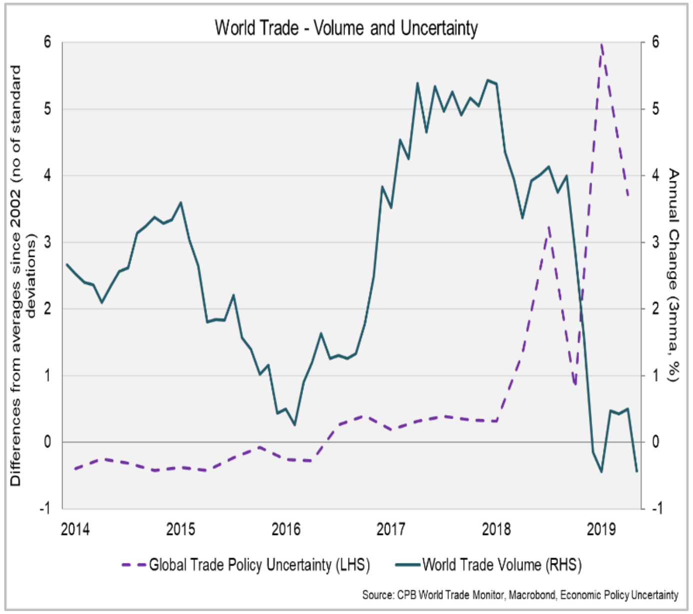
US economic growth slowed in Q2 2019.

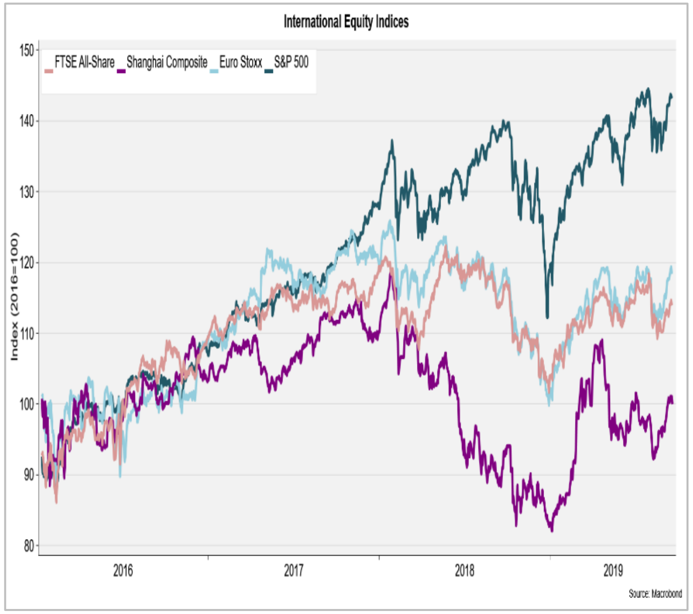
- US GDP grew by 0.5% in Q2 2019 (2.3% annually), slowing from 0.8% growth in Q1 2019.
- US unemployment is at historically low levels, remaining at 3.7% between June and August 2019.
- US CPI inflation eased to 1.7% in August (1.8% in July), having fallen from its recent peak of 2.9% in 2018.
- The IMF forecast US GDP growth to slow across 2019 and 2020 to 2.6% and 1.9% respectively.

Euro Area unemployment remains low as GDP growth slows

- Euro Area GDP growth slowed in the second quarter of 2019 (0.2%, down from 0.4% in Q1) and grew 2.3% over the year.
- Euro Area unemployment was 7.5% in July, unchanged over the month and at the lowest rate recorded since mid-2008.
- Euro Area inflation remained stable at 1.0% in August having fallen from 2.1% over the year.
- The IMF forecast Euro Area GDP growth to slow further in 2019 to 1.3%, before picking up to 1.6% in 2020.
- The ECB revised down their Euro Area growth forecast for 2019 to 1.1% and announced renewed monetary stimulus.







GDP Growth (%)	Estimate	Projections		Revisions from April 2019	
IMF WEO (July 2019)	**2018**	**2019**	**2020**	**2019**	**2020**
World Output	**3.6**	**3.2**	**3.5**	**-0.1**	**-0.1**
Advanced Economies	**2.2**	**1.9**	**1.7**	**0.1**	**0.0**
United States	2.9	2.6	1.9	0.3	0.0
Euro Area	1.9	1.3	1.6	0.0	0.1
United Kingdom	1.4	1.3	1.4	0.1	0.0
Japan	0.8	0.9	0.4	-0.1	-0.1
Emerging Markets and Developing Economies	**4.5**	**4.1**	**4.7**	**-0.3**	**-0.1**
China	6.6	6.2	6.0	-0.1	-0.1
India	6.8	7.0	7.2	-0.3	-0.3
Brazil	1.1	0.8	2.4	-1.3	-0.1
Russia	2.3	1.2	1.9	-0.4	0.2
South Africa	0.8	0.7	1.1	-0.5	-0.4

United Kingdom Summary

GDP contracted in Q2 2019 for the first time since 2012.

- UK GDP contracted by 0.2% in the second quarter of 2019 and grew 1.3% over the year.
- Manufacturing output fell 2.3% in Q2 2019, reflecting the unwinding of stock building ahead of the original Brexit deadline and widespread car firm shutdowns in April.
- GDP grew 0.3% in the month of July 2019 however remained flat over the 3-months with falls in manufacturing (-0.5%) and construction (-0.8%) output offsetting service sector growth (0.2%).

Employment rate at record high in May-July 2019.

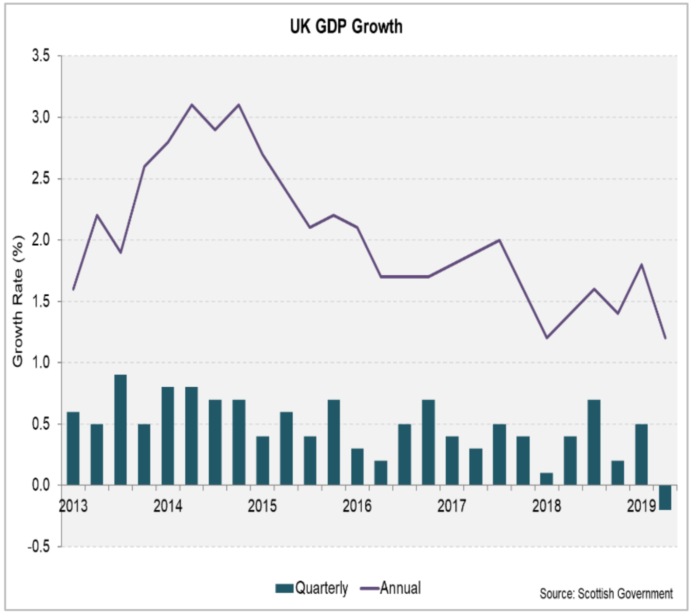
- UK employment rate rose over the year to 76.1%, its joint highest on record, with 32.8 million people in employment.
- UK unemployment fell to 3.8%, its joint lowest rate since 1974.
- The inactivity rate remained unchanged over the quarter at 20.8%, however has fallen by 0.5 p.p over the year.
- GB regular pay continued to strengthen into the second half of 2019 growing 1.9% over the year to July (up from 1.5%).
- Labour productivity fell by 0.2% over the year to Q1 2019; its third consecutive quarter of contraction.

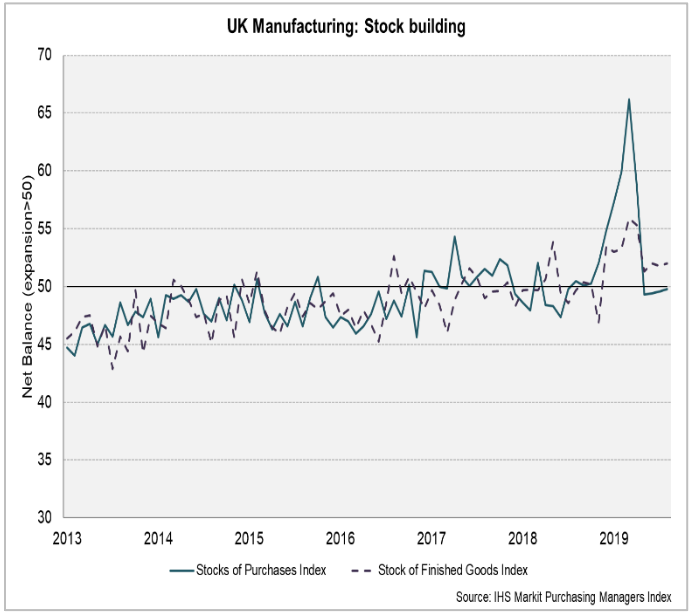
CPI inflation fell in August.

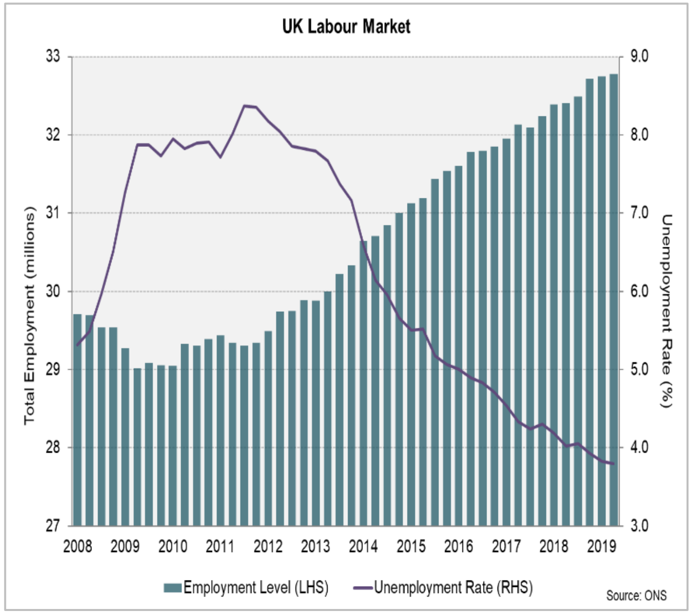
- Inflation edged up in recent months to 2.1% in July, however fell back to 1.7% in August.
- The fall in the rate was driven by a range of recreational and cultural goods and services, clothing and sea fares.
- The Bank of England (BoE) forecast inflation to remain above target at 2.1% and 2.2% in 2020 and 2021.

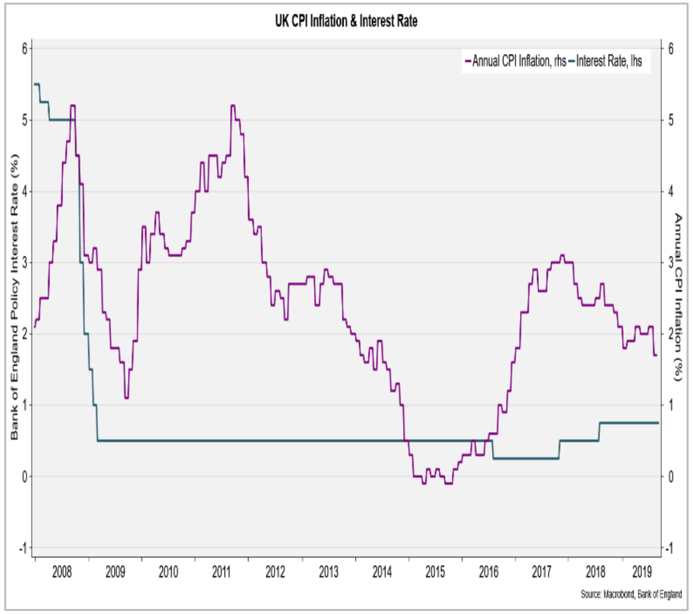
UK GDP growth is forecast to slow in 2019.

- The BoE forecast GDP growth of 1.3% in 2019, with weaker global growth and Brexit uncertainty weighing on investment.
- The IMF also forecast the UK economy to slow in 2019 to 1.3% before rebounding to 1.4% in 2020.
- Both forecasts assume a smooth Brexit transition.









Scotland Summary

GDP contracted in Q2 2019 for the first time since 2016.

- Scottish GDP contracted by 0.3% in Q2 2019 and annual growth slowed to 0.7%.
- Marginal growth in the services sector (0.1%) was offset by falls in production (-1.1%) and construction (-2.2%) output.
- The manufacturing sector contributed most strongly to the contraction, with output falling -2.5% reflecting the unwinding of stockpiling undertaken in Q1.

Labour market performing well by historical standards.

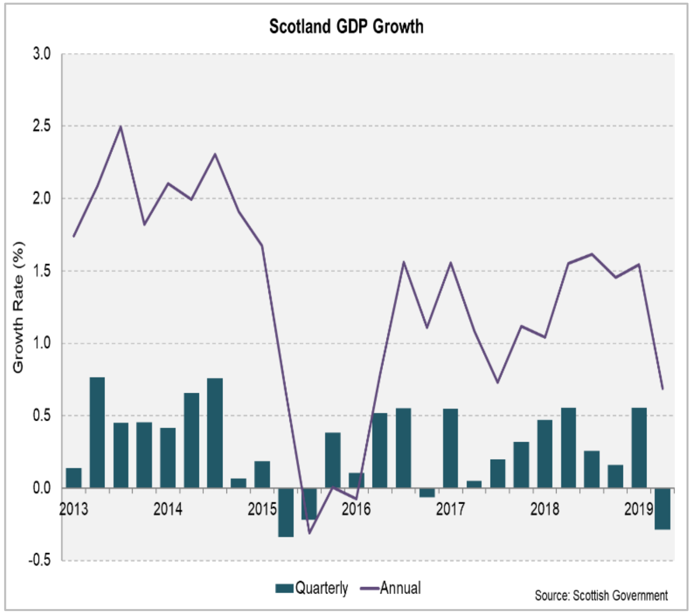
- Unemployment increased over the quarter to May-July 2019 to 4%, however has fallen over the past year and remains low by historical standards.
- The employment rate has fallen slightly over the latest quarter and year to 74.9%, with 2.7 million people employed.
- Full time employment rose by 47,000 over the year, more than offsetting a 40,000 fall in part-time employment.
- The inactivity rate rose over the quarter and year to 21.9%.
- Labour productivity grew by 0.4% in Q1 2019 and by 1.1% over the year.

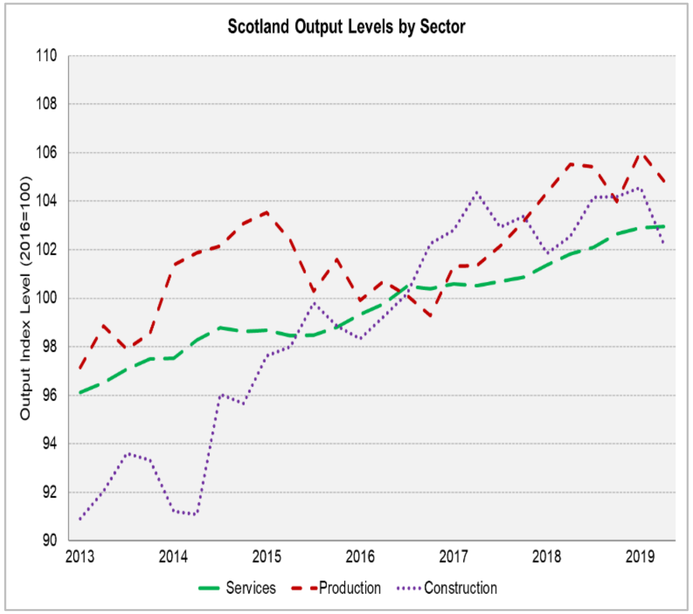
Business and consumer confidence remains weak.

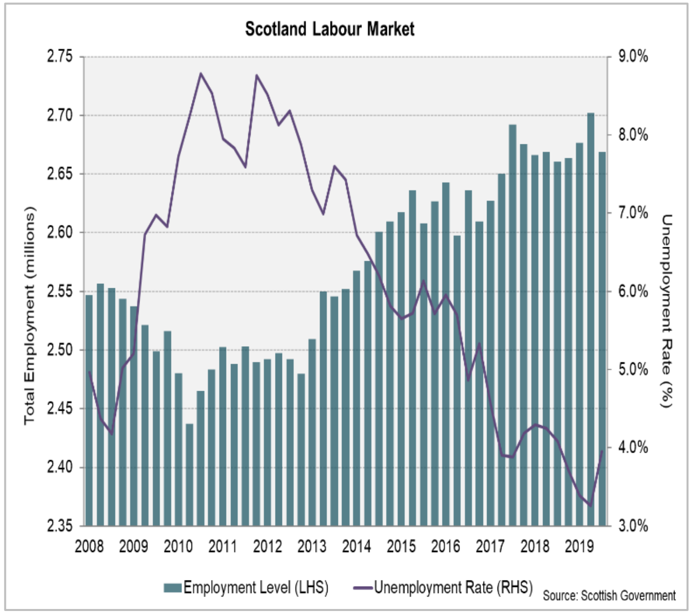
- The RBS Purchasing Managers Index reported marginal business activity growth in July and August while business confidence fell to its lowest level in over 3-years.
- Consumer sentiment in Scotland improved in Q2 2019, however remains negative and notably below the series average [see page 16]

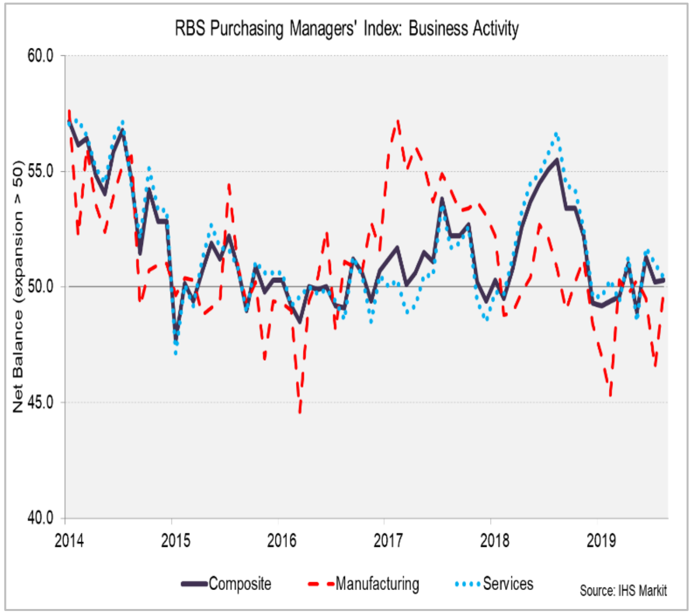
GDP growth is forecast to slow in 2019.

- Independent GDP forecasts estimate GDP growth to slow from 1.4% in 2018 to around 1% in 2019. [see page 17].
- Ongoing Brexit uncertainty is expected to continue impacting business investment and growth is generally expected to pick up in 2020 assuming a smooth Brexit transition.
- A no deal Brexit remains a downside risk to the economic outlook and risks pushing the economy into recession.



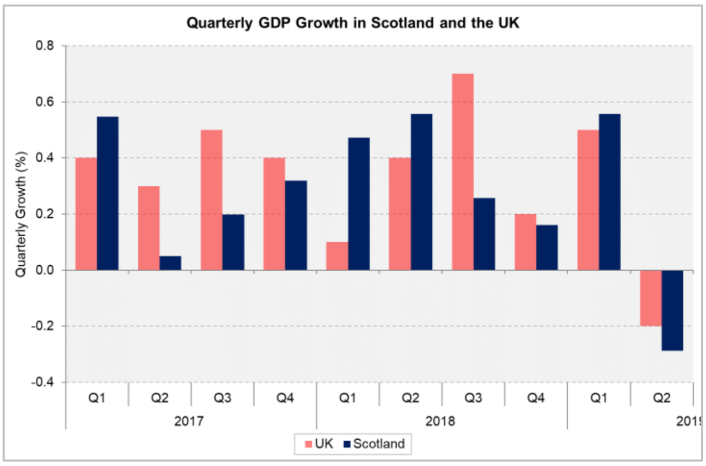






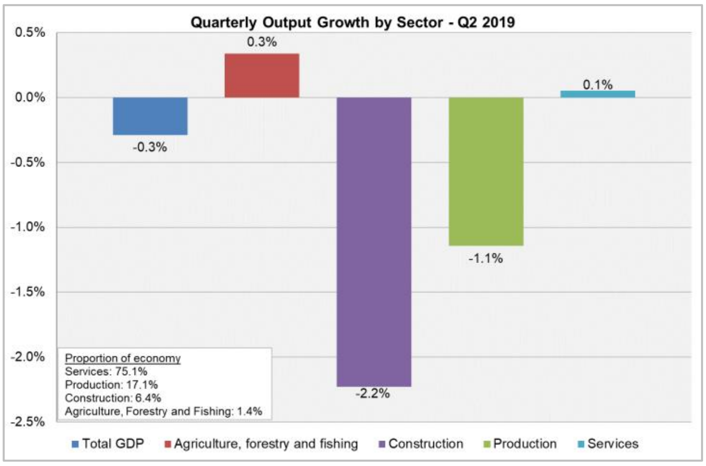
Scottish Economy Update

Gross Domestic Product



The first half of 2019 has presented a mixed picture for Scotland's economic output which reflects a combination of Brexit uncertainty and a weakening in the wider UK and global economic environment.

The latest GDP data for Q2 2019[1], provides insight into how Scotland's onshore economy performed in the 3-months following the original UK EU departure date at the end of March.



Over this period, the Scottish economy contracted by -0.3%, broadly in line with the UK economy as a whole which contracted by -0.2%. The key driver of the contraction was in the production sector (-1.1%), which alongside a contraction in the construction sector (-2.2%), more than offset marginal growth in the services sector (0.1%).

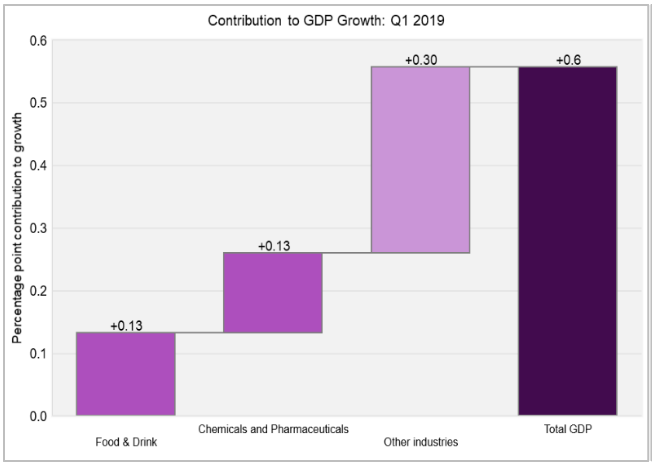
Over the year as a whole, the Scottish economy continued to grow 0.7%, however this was notably slower than annual growth of 1.5% in the first quarter of the year.

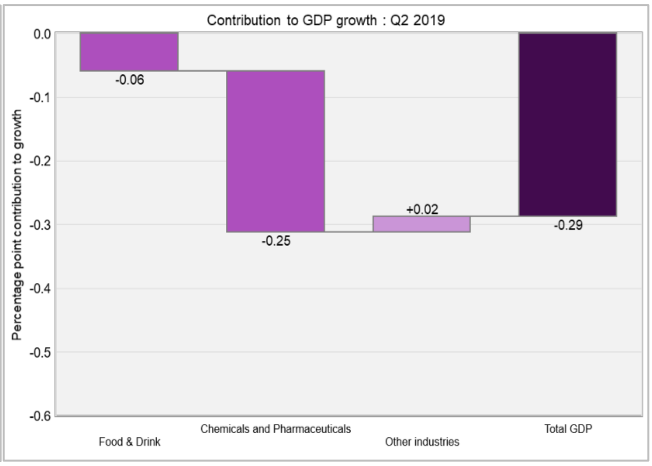
Service sector growth has slowed through the first half of 2019 compared to 2018, as it has in the UK as a whole, with Business Services and Finance slowing to 0.3% quarterly growth. Output growth from Distribution, Hotels and Catering (0.3%) and Transport, Storage and Communications (0.6%) picked up over the second quarter, however this was offset by a fall in output from Government and other Services (-0.5%).

The contraction in Q2 followed relatively robust growth of 0.6% in the first quarter. Around half of that growth came from the manufacturing of Spirits and Wines and Pharmaceuticals as firms stockpiled and moved to complete orders prior to the original Brexit deadline. The

[1] https://www2.gov.scot/Topics/Statistics/Browse/Economy/PubGDP/GDP2019Q2

June edition of State of the Economy, set out that these specific drivers were likely to be temporary as firms would subsequently unwind their stock levels.





The output data for Q2 shows that the same two manufacturing sectors that contributed most strongly to growth in the first quarter, contributed mostly to the subsequent fall in output in the second quarter and likely reflects the unwinding of stocks built up in Q1. This pattern of economic activity mirrors the findings from economic modelling presented in the October 2018 edition of State of the Economy[2]: the additional stockpiling in 2018-19 boosts growth initially but comes at a cost of growth in 2019-20 as companies allow their inventories to unwind.

The uncertainty regarding the nature and timing of the UK's EU departure is likely to continue generating volatility in the data. The response of businesses to the current October deadline may differ from the original Brexit deadline in March as the same sectors may not respond in the same way and may not stockpile again to the same extent. For example, the start of the festive trading period will impact firms' ability to prepare and stockpile for Brexit, while the ongoing uncertainty may reduce the willingness of firms' to incur the same degree of costs as in March.

The impact of prolonged uncertainty is considered in more detail in the box below. To set the context, the recent trend in private business investment is shown.

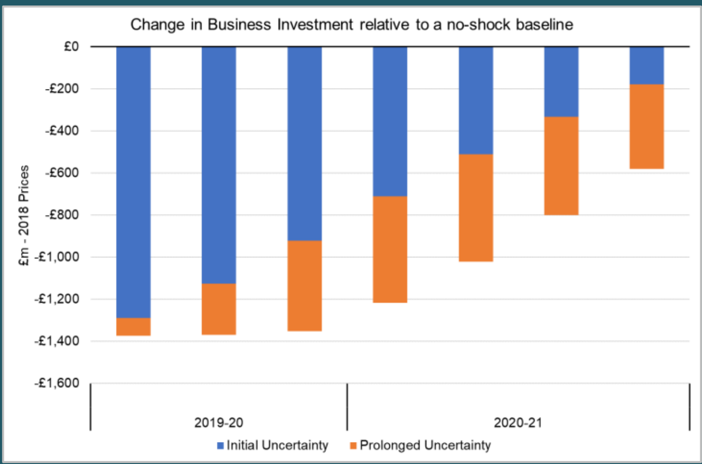
[2] https://www.gov.scot/publications/state-economy/pages/10/

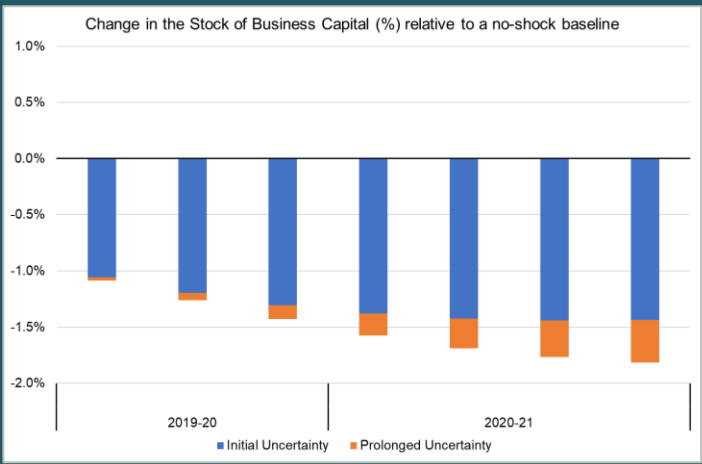
Estimating the impact of prolonged uncertainty from Brexit on the Scottish economy

In a previous State of the Economy Report in January 2018, we examined the impact that heightened levels of uncertainty from Brexit might have on the Scottish economy, in particular on business investment.

With uncertainty from Brexit now persisting, both around an EU Exit date and the form of future economic partnership with the EU, we estimate the impact that this prolonged period of uncertainty could have on the Scottish economy.

In our earlier analysis, the period of heightened uncertainty ran until the end of the second quarter in 2019. We now extend this period of uncertainty to persist until the end of the first quarter of 2020. In all other respects, the modelling approach is the same as in the previous analysis.[3]





The results show that the additional impact of this prolonged period of uncertainty is estimated to have reduced or deferred the level of business investment in Scotland by a further £0.5 billion by the start of 2020-21 than previously estimated.

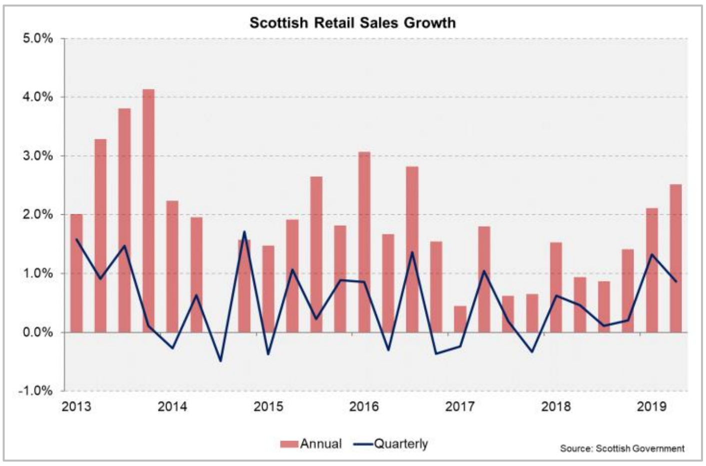
One of the main consequences of this lower or deferred business investment is that it reduces the stock of capital in the Scottish economy – for example, office buildings, new factories or manufacturing equipment.

The conclusion is that the prolonged period of uncertainty will have a more severe impact on business investment than previously estimated in the short term. In turn this is impeding growth of the capital stock by more than previously estimated and risks raising longer term challenges for productivity and growth in Scotland.

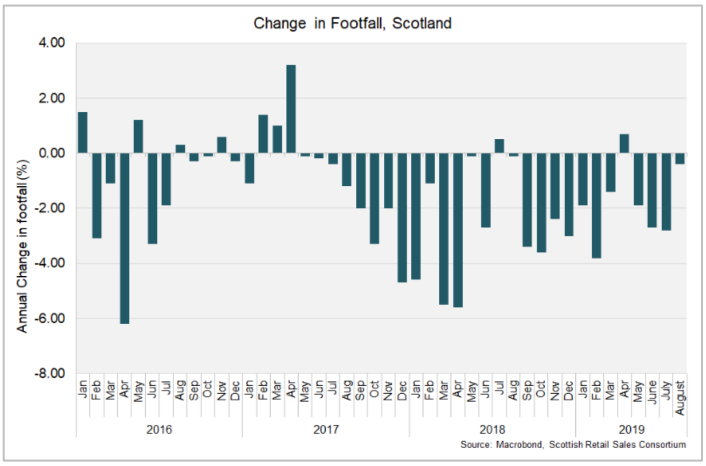
[3] The modelling is undertaken using the Scottish Government Global Econometric Model (SGGEM).

Retail Sales

Retail sales growth has supported service sector growth in the first half of 2019.



Over this period, there has been generally stronger growth in Scottish retail sales compared to the past two years[4]. However, the pace of growth slightly softened in Q2 2019, growing 0.9% over the quarter (2.5% annually), down from 1.3% growth in Q1 2019. This broadly reflected the movement in retail sales across Great Britain as a whole where growth slowed to 0.7% over the quarter.

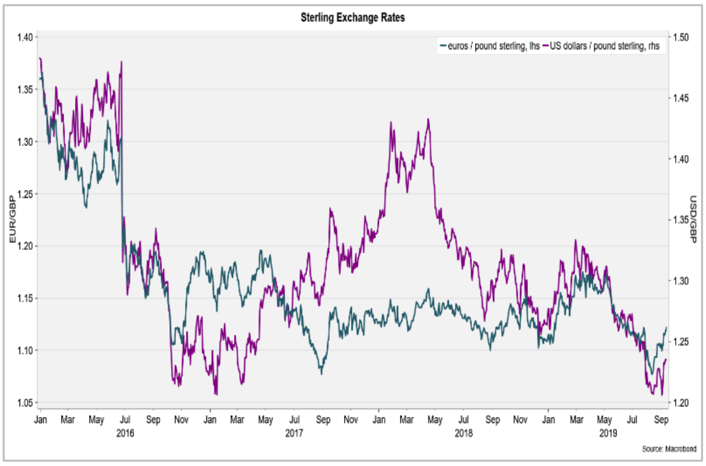


The latest data suggest that retail sales have held up despite Brexit uncertainty. However trading conditions remain challenging for the sector with retail footfall in Scottish town and city centre locations continuing to fall into the summer months.

While this has been driven by well documented structural changes in consumer behaviour, in particular the growth of online retail, this has implications for the profitability of many high street retailers. As such, Brexit uncertainty remains a key challenge for the sector and the ability of retailers to respond to any downturn in sales, or disruption to supply chains, as a result of continued Brexit related uncertainties.

Exports

The international trade environment has weakened and, as set out on page 2 above, has become more uncertain in 2019 amid ongoing trade tensions between China and the United States and a softening in global growth and trade over the past year.



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[4] https://www2.gov.scot/Topics/Statistics/Browse/Economy/PubRSI/RSIS2019Q2

Alongside this, Brexit uncertainty has continued to contribute to currency fluctuations with Sterling depreciating against the dollar and euro over the course of the year. The box below considers in more detail the relative impact that currency movements have on import and export growth.

In Q1 2019, Scotland's manufactured exports[5] grew by 1.4% over the quarter and 3.3% over the year; slightly slower than at the end of 2018. The largest contributor to the increase in the volume of manufactured exports was Food and Drink exports which increased 5.7% over the quarter and 16.9% over the year. Refined petroleum, chemical and pharmaceutical product exports also increased over the year (3.3%), while there was a fall in exports of engineering, machinery and metals (-6.9%) and other manufactured products (-4.3%).

More recent data from HMRC[6], a separate export survey, show that Scotland's goods exports (including oil and gas) increased in cash terms by £4.3 billion (14.5%) to £34.0 billion over the year to June 2019, compared to the previous year. This increase was driven by a rise in oil and gas exports, which to the EU increased by 25.8 percent to £9.4 billion and to non-EU countries more than doubled to £4.4 billion.

Exchange Rate Depreciation and the Trade Balance

Since the EU referendum, Sterling has depreciated by around 15% against the Euro and 17% against the dollar. Over that period, Sterling has been highly sensitive to Brexit signals and most recently the prospects of a no-deal.

Currency depreciations are usually expected to increase exports and hence to improve the trade balance. However, recent research by the IMF[7] shows that currency depreciation may lead to only a modest increase in exports, with improvement in a country's trade balance potentially driven by a reduction in imports.

This box explores this issue further for Scotland by undertaking the following analysis and modelling:

First, we present outturn data on Scotland's exports and imports and trade balance in the period since the EU referendum (2016 Q3). These are sourced from the Quarterly National Accounts Scotland (QNAS). Figure 1 shows what happened to exports and imports following the currency depreciation.

[5] https://www2.gov.scot/Topics/Statistics/Browse/Economy/QNA2019Q1
[6] https://www.uktradeinfo.com/Statistics/RTS/Pages/default.aspx
[7] https://www.imf.org/en/Publications/ESR/Issues/2019/07/03/2019-external-sector-report A 10 percent depreciation (vis-à-vis all currencies) improves a country's trade balance by about 0.3 percent of GDP in the near term, on average, with most of the effects coming through a contraction of imports.

Second, we model[8] what could have happened to the trade balance if the depreciation in Sterling had not occurred. This is done by holding the exchange rate at the 2015 Q4 pound to dollar rate until 2019 Q1.[9] Figure 2 shows what exports, imports and net trade might have looked like without the currency depreciation.

By comparing the two sets of figures we can illustrate how the trade balance has been affected by the currency depreciation.

Figure 1: Quarterly Growth Rates of Imports and Exports

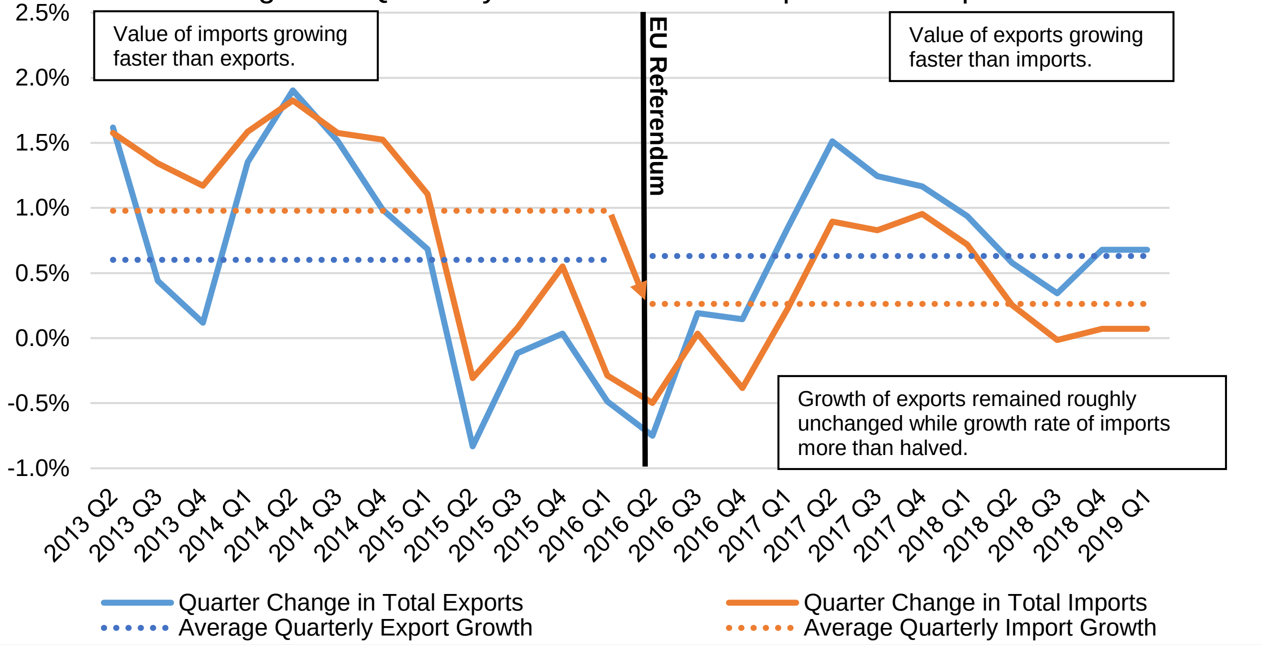


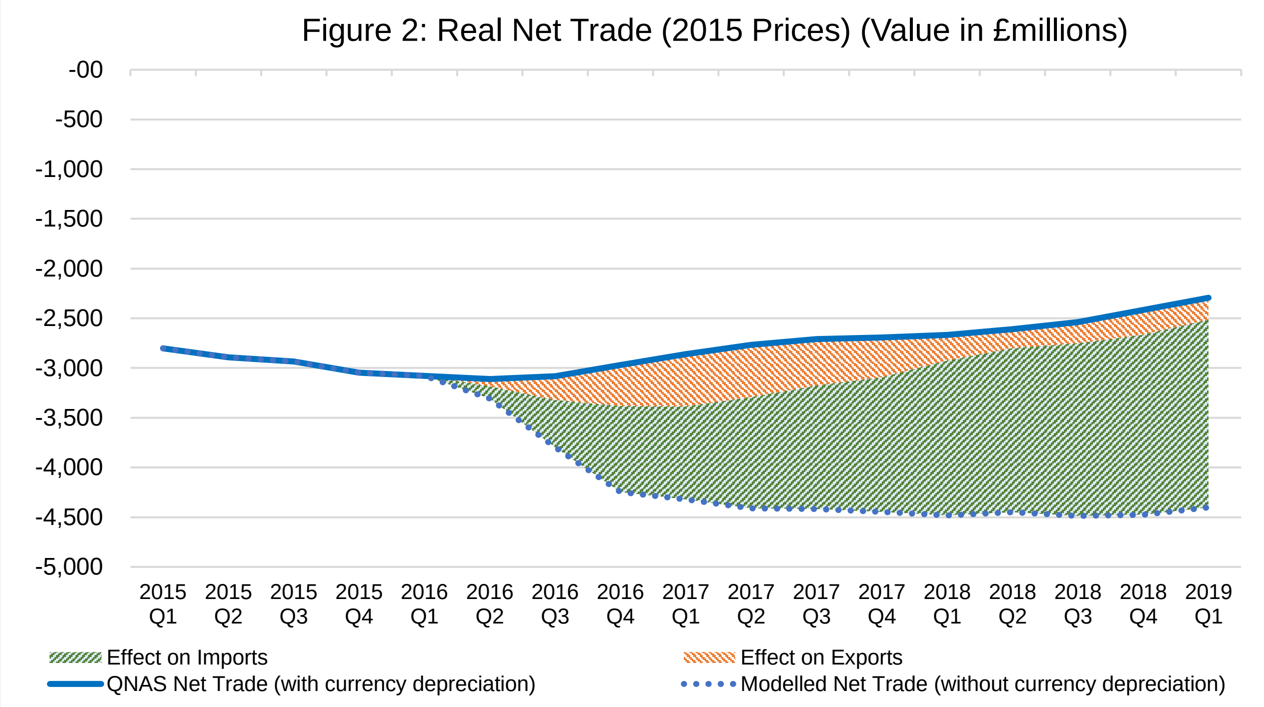
Figure 1 above plots quarterly growth rates of exports and imports from QNAS data. Since the EU referendum result and the fall in the Sterling exchange rate, Scotland's net trade balance has improved. Whilst exports have remained at approximately the same rate of growth, the rate of growth of imports has fallen resulting in an improvement of the trade balance. This suggests that imports have been relatively more sensitive to changes in the exchange rate than exports.

The fall in the value of Sterling following the EU referendum could be interpreted as one sign of wider political and economic uncertainty in the UK. The modelling considers only what might have happened in the absence of a currency depreciation - it does not attempt to show the impact of removing any wider uncertainty that has occurred since the EU referendum.

[8] The modelling is undertaken using the Scottish Government Global Econometric Model (SGGEM). This is one of several models that the Scottish Government is using to enhance its trade modelling capability. Further details on trade modelling can be found in the Scottish Government commissioned feasibility study (undertaken by the Fraser of Allander Institute with the National Institute of Economic and Social Research) published alongside this State of the Economy report.

[9] 2015 Q4 is used as the depreciation of the pound in 2016 Q1 indicates that a potential leave result was starting to be incorporated in exchange rates.

Nevertheless, the analysis supports the view that the improvement in net trade from the currency depreciation has been driven more by a fall in imports than by a rise in exports.



Labour Market

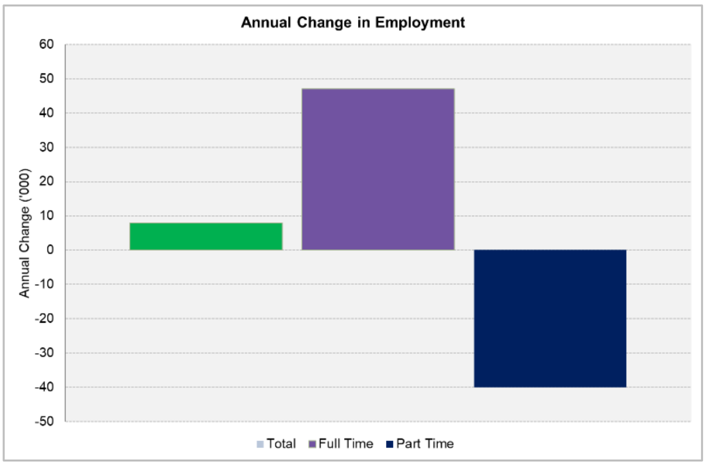
Scotland's labour market has continued to perform strongly by historical standards in 2019, however has softened slightly from the record performances in employment and unemployment achieved in 2018 and start of 2019.

Latest data for May to July 2019[10] show that while the unemployment rate remains lower compared to last year and compared to historical levels, it rose from 3.3% to 4.0% over the quarter.

SCOTLAND LABOUR MARKET STATISTICS (May-July 2019)			
RATES	Latest (%)	Quarterly Change (% p.t.)	Annual Change (% p.t.)
Employment*	74.9	-1.0	-0.1
ILO Unemployment**	4.0	0.7	-0.1
Economic Inactivity*	21.9	0.4	0.2
LEVELS ('000)	Latest	Quarterly Change	Annual Change
Employment (16+)	2,669	-33	8
ILO Unemployment (16+)	110	19	-3
Economic Inactivity (16-64)	754	14	5
*Denominator = Working age population (16-64)			
**Denominator = Total economically active			

[10] https://www2.gov.scot/Topics/Statistics/Browse/Labour-Market

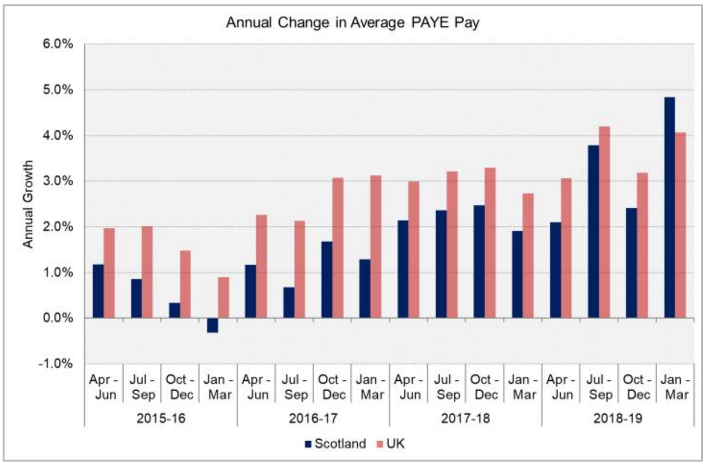
Alongside this, the level of employment has increased by 8,000 over the year, however fell by 33,000 over the quarter with the employment rate falling to 74.9%.



The rise in employment over the year was driven by an increase in full time workers (47,000) which more than offset a fall in part-time workers (-40,000).

Inactivity in Scotland – those neither in work or looking for work – has increased over the quarter and the year to 21.9%.

The slight softening in the labour market has also been reflected in business surveys[11], with firms reporting that permanent vacancy growth has eased in recent months to its lowest rate in over three-and-a-half-years, while temporary vacancies have increased. This recent shift towards temporary work may be for a variety of reasons including business uncertainty and the low cost of labour relative to capital. Businesses may also be hiring on a temporary basis given Brexit uncertainty.

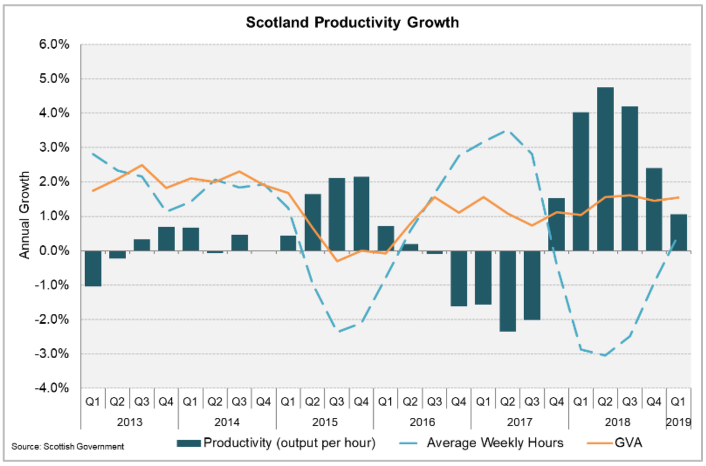


Despite a softer labour market, earnings growth has strengthened at the start of 2019. HMRC data for Scotland[12] show that average nominal PAYE pay in January-March 2019 was 4.8% higher than a year earlier, however real terms growth remains relatively subdued.

Labour Productivity

Labour productivity in Scotland has continued its recent pattern of positive growth at the start of 2019, albeit at a slower pace than in 2018.

In Q1 2019[13], labour productivity (output per hour worked) grew 1.1% over the



[11] https://www.markiteconomics.com/Public/Home/PressRelease/951e4e6734644a9cbcc205a3f6d4feaf

[12] https://www.gov.uk/government/statistics/uk-real-time-information-experimental-statistics

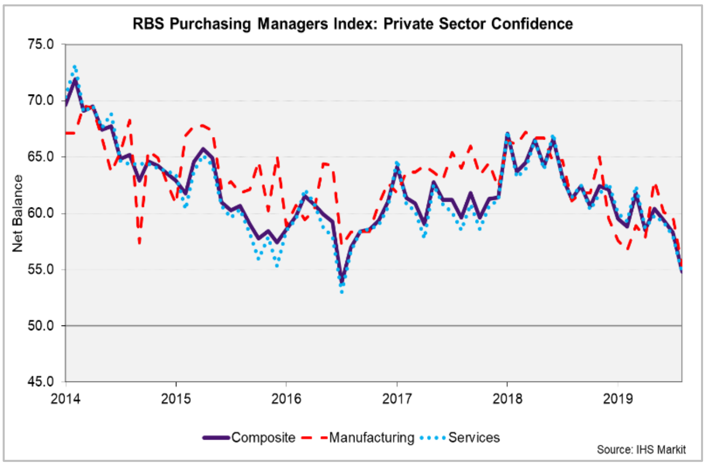
[13] https://www2.gov.scot/Topics/Statistics/Browse/Economy/PROD19Q1

year, down from the average annual growth rate of 3.8% during 2018.

Positive productivity growth reflects that output is growing more quickly than hours worked. The slower pace of productivity growth at the start of 2019 reflects that annual output growth has remained stable at around 1.5%, while growth in average weekly hours worked has strengthened, rebounding to 0.5% growth over the year following five consecutive quarters of contraction. This may reflect the increase in full-time employment relative to part-time employment over the past year.

Business Sentiment

Business and consumer sentiment data provide useful insight as leading indicators into the confidence and optimism of firms and households and how that may influence their economic activity in the short term.



The latest RBS Purchasing Managers Index survey for August 2019[14] reported that while businesses expect output to increase over the coming year, the degree of business confidence across both the manufacturing and service sectors has fallen to its lowest level in over 3-years.

The weakening in sentiment over the past year is also signalled in the engineering sector[15] in which optimism in August 2019 was reported as negative for the first time since 2016. The Scottish Chambers of Commerce Quarterly Economic Indicator[16] showed that while business optimism was positive across the sectors in Q2 2019, it was generally lower than the same period last year.

The fall in business confidence reflects in part the political and economic uncertainty associated with Brexit, which during the first half of 2019, has weighed on business investment and led to resources being diverted to short term stockpiling. Due to the prolonged period of uncertainty, this is likely to continue impacting business sentiment and investment intentions. In their latest Inflation Report[17], the Bank of England noted that UK underlying output growth is projected to be subdued in the near term reflecting more entrenched Brexit uncertainties.

The fall in business sentiment is also consistent with other factors that have been raised in latest business surveys such as weaker growth in business activity and output, weaker

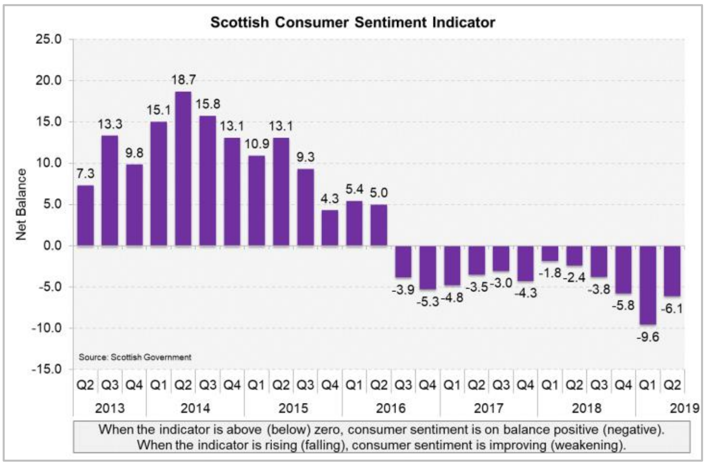
[14] https://www.markiteconomics.com/Public/Home/PressRelease/1af9bcb92d8d4bbbb05d106ddeffdad2
[15] https://app.emarketeer.com/resources/12144/My_Documents/QR_Q1_2019/1072_Scot_Eng_QR_0919.pdf
[16] https://www.scottishchambers.org.uk/press-releases/quarterly-economic-indicator/
[17] https://www.bankofengland.co.uk/inflation-report/2019/august-2019

growth in new orders and exchange rate fluctuations feeding through to input cost increases.

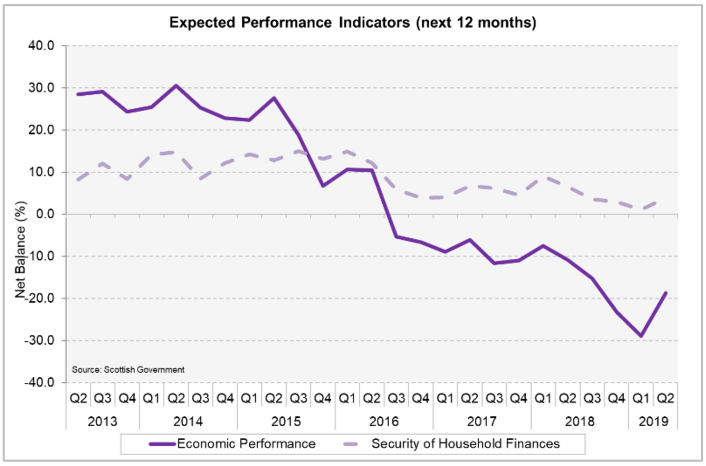
These factors, alongside stronger external headwinds, suggest a changing economic environment in which firms will be considering future investment and contingency planning ahead of the next Brexit withdrawal deadline.

Consumer Sentiment[18]

As with business sentiment, consumer sentiment in Scotland has remained weak in the first half of 2019. Having fallen to its lowest level in the time series in Q1, latest data shows consumer sentiment improved in the second quarter rising 3.4 points from -9.6 to -6.1. However the fact that the reading remains negative shows that more respondents continue to report a decline in sentiment than an improvement, as has been the case since Q3 2016.



Of the five elements that make up the Consumer Sentiment Indicator, respondents continue to be most pessimistic about the outlook for the Scottish economy over the coming year (-18.6). Alongside this, respondents continue to be most positive about the outlook for their personal household financial security which, on balance, they expect to improve (3.9).



While both indicators improved compared to Q1 2019, both remain notably below their series averages. The weaknesses in the forward expectation indicators are likely to reflect a range of macroeconomic issues such as the ongoing uncertainty surrounding Brexit, personal job security, wage growth and so on.

Looking ahead, the weakness in consumer sentiment presents a downside risk to the economic outlook as expectations may start to impact on real economic activity.

[18] http://www.gov.scot/Topics/Statistics/Browse/Economy/SCSI

Scotland's Economic Outlook

The Scottish economy is forecast to grow in 2019, however as with the UK and global economic outlook, the pace of growth is generally expected to be slower than last year (1.4%).

While the forecasts (where applicable) implicitly reflect the impacts of Brexit uncertainty so far on outturn data, they continue to assume some form of orderly Brexit transition, which would support a pickup in growth from 2020 onwards.

However, as we've set out in this report, the ongoing uncertainty arising from when and how the UK withdraws from the EU will continue to impact consumers and businesses sentiment and activity. Companies will continue having to divert resources to contingency planning and stockpiling rather than business growth and investment.

Until a Withdrawal Agreement is ratified or an extension is agreed, the economic risks associated with a No Deal Brexit remain live. As has been highlighted in Scottish Government Analysis, *No Deal Brexit – Economic Implications for Scotland*[19], such an outcome risks pushing the Scottish economy into recession with a corresponding sharp rise in unemployment.

For the UK as a whole, the recent Fiscal Risks report from the OBR suggests that the UK economy could contract through 2020 by around 1.4 per cent based on their most recent assessment, whilst the Bank of England suggest output lost to the economy could be as much as 5.5 per cent in the advent of a No Deal Brexit with a rise in unemployment to 7%.[20,21] The Fraser of Allander Institute reported that applying the Bank of England's scenario to Scotland could result in GDP in Scotland being £9 billion lower and unemployment rising to nearly double the current rate.[22] However, it is also the uncertainty over the nature of the UK and Scotland's long term relationship with the EU that persists.

The table below sets out a selection of independent forecasts and projections which, given their range in the short term, highlights the uncertainty of forecasting at this time.

Independent Scottish GDP Growth Forecasts (%)[23]						
	2019	**2020**	**2021**	**2022**	**2023**	**2024**
Scottish Fiscal Commission	0.8	0.9	1.1	1.2	1.3	1.3
Fraser of Allander Institute	1.2	1.4	1.5	-	-	-
EY ITEM Club	1.0	1.4	1.5	1.7	1.8	-
PWC	1.6	1.3	-	-	-	-

[19] https://www.gov.scot/publications/deal-brexit-economic-implications-scotland/
[20] https://obr.uk/frr/fiscal-risks-report-july-2019/
[21] https://www.bankofengland.co.uk/letter/2019/letter-from-the-governor-to-the-tsc-regarding-updated-brexit-scenarios
[22] https://fraserofallander.org/ Blog: What could No-Deal mean for the Scottish Economy? (9 September 2019).
[23] Scottish Fiscal Commission (http://www.fiscalcommission.scot/publications/scotlands-economic-and-fiscal-forecasts/scotlands-economic-and-fiscal-forecasts-may-2019/); Fraser of Allander Institute (https://www.strath.ac.uk/business/economics/fraserofallanderinstitute/publications/commentary/); EY ITEM Club (https://www.ey.com/Publication/vwLUAssetsPI/ey-scottish-item-club-summer-update-2019/$FILE/EY-Scottish-ITEM-Club-Summer-update-2019.pdf) PWC (https://www.pwc.co.uk/services/economics-policy/insights/uk-economic-outlook.html).

Alongside domestic challenges, external headwinds have also strengthened in 2019. Global growth is forecast to slow this year and the ongoing global challenges arising from trade tensions and heightened trade uncertainty, means that the external trading environment has softened relative to the last couple of years. Alongside Brexit uncertainty, these present a downside risk to the Scottish economic outlook.

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