University of Strathclyde Business School

Fraser of Allander Institute

Economic Commentary

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Foreword

A full year has passed since the UK went into its first nationwide lockdown.

No one knew what the next 12 months would hold this time last year. Some thought we would face a few weeks or months of restrictions, others believed we would be in this for the long haul. Either way, I am not sure any of us were prepared for the scale of economic and social disruption that has been caused by the pandemic – or the human cost.

As this quarter's Commentary notes, one of the defining features of this economic crisis has been the uneven impact on different sectors. For some industries, including science, technology, and information and communication, after some initial disruption, trading has remained steady at almost pre-pandemic levels.

This is in stark contrast to the experience of most businesses in sectors that rely on people leaving their homes and socialising together. Scotland's tourism, hospitality and retail industries have been hit hard, with restrictions on their operations extending beyond national lockdowns, making trading over the past 12 months almost impossible. This was echoed in Deloitte's latest Consumer Tracker analysis which found that year-on-year spend on eating and drinking out, in Scotland, declined by 49% and 41% respectively during Q4 2020.

While uncertainty remains as to what the future holds, with the vaccine deployment continuing at pace and the likelihood of looser restrictions in the coming months, there is reason to hope that our society will mobilise again and that businesses and the economy will begin to rebound.

As the Commentary points out, the private sector is an important cog in the wheel of Scotland's recovery and therefore business needs to come out of this lockdown in a position to grow and invest in order that a strong, sustainable, fair and green economic recovery can be attained. For the hardest hit sectors, such as tourism and hospitality, they will be hoping there is recognition of the months of turmoil that they have faced and for the new government to place a strong focus on rebuilding the economy.

As business leaders look to navigate their markets in the next 12 months, Deloitte's latest Human Capital Trends looks at the importance of a 'thrive' mindset, which recognises disruption as continuous, and an opportunity to create positive change and drive an organisation forward. A 'survive' mindset, on the other hand, treats disruption as episodic and expects a return to 'business as usual'. While we're still in the midst of this pandemic, its already clear that our society has fundamentally changed and, amongst many other things, old ways of working could be a thing of the past.

The response to COVID-19 has given us a glimpse of how work could, and should, change for the better with the adoption of new technologies and working styles. One of the defining aspects of the past 12 months has been the influence of lockdowns on daily life and the pivoting to, and normalising of, home working. While there is a mixture of opinions on the benefits of this both to employees and employers, as evidenced by this quarter's Commentary, there is no doubt that homeworking, to some extent, is here to stay for many sectors.

Another key finding from our Human Capital research is that those businesses that thrive must be distinctly human at their core, making sure that every issue and decision is considered from a human angle first.

Moreover, today's environment calls for a degree of courage, judgment, and flexibility that only people and teams led by humans can bring. A predictable world can be dealt with effectively by algorithms and equations. A messy world cannot, even in an age of increasingly intelligent machines.

To combine revenue growth and profit-making with respect and support for its environment and stakeholder network, an organisation needs to ground itself in a set of human principles: purpose and meaning, ethics and fairness, growth and passion, collaboration and relationships, and transparency and openness.

As spring approaches and the economy begins to open up again, businesses have an opportunity to embrace possibility. To be successful in a post-pandemic world, they should explore how they can draw energy from the pandemic's chaos and disruption in order to thrive in a post-pandemic world by designing the future of work.

Those businesses that use this disruption as an opportunity to embody human qualities will be in a strong position to capitalise on growth opportunities. Organisations that do not will quickly fall behind.

Gavin Hood
Partner and Head of Advisory Corporate Finance
Deloitte
March 2021

References

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2021 Global Human Capital Trends | Deloitte Insights

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For regular analysis on the Scottish economy and public finances please see

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Summary

We look ahead to a new future with hope that the vaccine programme will lead to a return to normality at some point during 2021. With furlough schemes now in place into the Autumn, it is clear that the economy will need support past the point at which restrictions are lifted.

Of course, the forthcoming economic recovery could take many shapes, and policymakers in all levels in government will have a role in shaping the recovery.

The Scottish economy has been through an unprecedented year: the contractions we have seen during lockdown periods are enormous by historical standards.

After a fall in GDP of 23% between February and April, we saw rapid growth through the Summer as the economy opened back up. The recovery flattened off during the Autumn as restrictions were re-imposed, and a fall moving into the end of the year as restrictions got even tighter.

The expectations for early 2021 are for further falls in output, before growth returns in the Spring as restrictions are able to be eased.

One of the features of this economic crisis has been the differential impacts on different sectors. Businesses which have been able to adapt quickly to do much of their business remotely have been much less harder hit, whereas those who rely on social spending and face-to-face interaction have been much more severely impacted.

With restrictions are likely to continue for some sectors for at least the first half of 2021, it is likely that this “twin-track” recovery will continue. Of particular concern are the impacts on the hospitality sector, which employs generally younger and lower paid workers.

Of course, Government policy interventions, in particular through the Job Retention Scheme, have protected millions of jobs throughout the period of the pandemic. Despite this, we know that thousands of jobs have been lost. Much of the impacts on employment are likely to manifest down the track as Government policy initiatives are rolled back.

All of this sets the scene for a very different election campaign come May.

It may be of relief to some that the doorstep canvassers will be absent. Social media will be more prevalent than ever before in the race to catch the voters’ eye. Postal voting will probably make up a greater proportion of votes cast, with perhaps less of a clamour to win votes in the days immediately running up to the election.

But none of this takes away from the importance of this election. As we have become accustomed to, the constitutional debate will be ever present, but there is plenty else to concern voter’s minds. The next parliament will see Scotland able to flex its fiscal policy muscle with much of the powers devolved from the 2016 Scotland Act in place and ready to go. And with some big reforms on the horizon, as well as the (hopeful) recovery from the largest recession in living memory, the next five years have a lot in store.

However, the economy is much more than a cursory glance at GDP numbers and unemployment statistics will tell you. A sustainable, sufficient, quality of life that is attainable for all of Scotland's population requires a lot of moving parts to be working together. The pandemic has shown us just how important some, often undervalued, parts of the economy actually are.

There is little doubt that getting the private sector back on its feet is an important cog in the wheel that will move us forward out of this crisis but there are other, perhaps less obvious, things that the next government will need to focus on to enable the recovery and to guide the economy onto a more sustainable footing.

Soon parties will be setting out (we hope) their vision for the new economy they hope to build. Some key issues that will likely feature big at this election include a 'green recovery' and business support.

Climate change is arguably the biggest threat facing Scotland bar none, and with COP 26 happening in Glasgow this year, there will be many eyes on Scotland. We expect that political parties will be putting forward policies which speak to the "green growth" agenda at this election as well as other plans on how to rebuild the economy after the pandemic.

In terms of supporting businesses, the Scottish Government has more limited powers than the UK Government, but there will be an expectation for the next government to have a clear strategy on how it helps business recover.

There are particular sectors, like hospitality, that will be looking for commitments of continued support, extending beyond the period of lockdown restrictions.

However, there are huge uncertainties around when physical distancing will end, the future of workplaces themselves, and the evolution of the behaviour of consumers.

Many businesses have adapted how they operate throughout the COVID crisis and it is uncertain how much of these homeworking practices will become the norm once the pandemic ends, and the impact that these new ways of working will have on productivity and growth.

Any future government activity in this area will need to be flexible and responsive and credibility and focus will be required in helping the private sector navigate its way out of this crisis with as many good quality jobs intact as possible.

Fraser of Allander Institute
March 2021

Outlook and Appraisal

Introduction

In this section of the commentary, we summarise some of the latest indicators covering the global, UK and Scottish economies.

There is a mountain of information that we could cover, so we do not try to replicate it all here. Our website – www.fraserofallander.org – provides a regular update and analysis of developments.

Instead we trace some of the key charts and commentary on economic activity, jobs, household incomes, and the latest thinking on the recovery.

The outlook for the next few months and years looks incredibly uncertain. Once again, given such uncertainties, we have avoided providing a specific point estimate or a central forecast for the next few years. Instead, we highlight different scenarios.

What do the scenarios tell us?

Since the last set of scenarios in our commentary in December, the profile for growth has changed: following the discovery of the new COVID-19 variants, and the post-Christmas lockdown, growth prospects for 2021 have been revised down due to likely contractions in quarter 1.

However, the vaccine rollout continues apace, and the prospects for the second half of 2021 look more bright.

The optimistic scenario sees the economy recovering fully by next summer. Given the drag on economic recovery that the current national lockdown is having on the Scottish economy, this is a few months later than previously thought.

However, the rollout of the vaccine so far has been fast, leaving room for some optimism still.

When the economy does open back up it will take some time before normality returns fully; some businesses may not be able to open back up at all. The central scenario reflects this.

The central scenario sees the economy recovering by Autumn 2022.

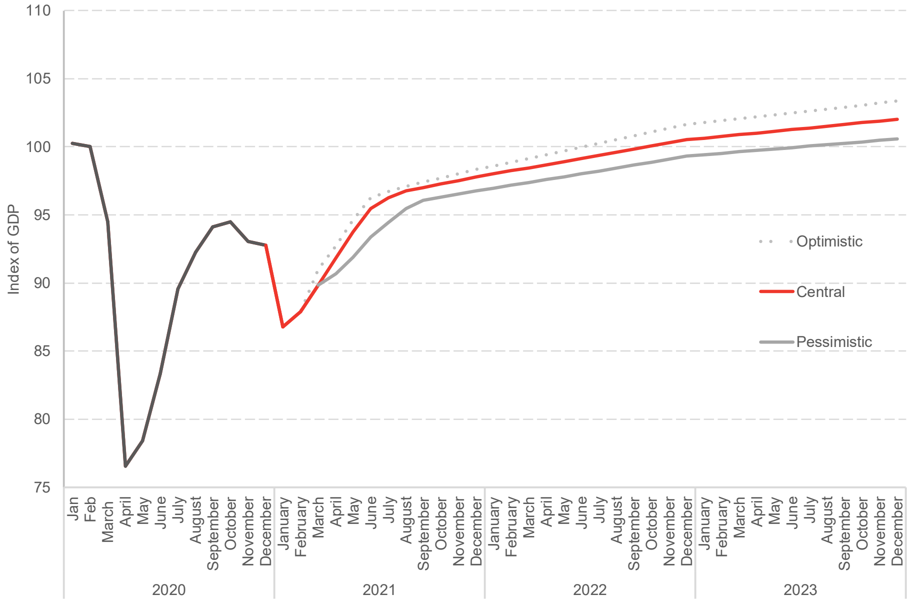
Finally, the immediate future of the Scottish economy is extremely uncertain. Whilst we hope that the current lockdown is the last, history has taught us not to underestimate the speed at which the virus can spread.

Additionally, once furlough ends in September it is uncertain how many furloughed staff will be welcomed back to their workplace and how many will be made redundant.

All of these factors will have an impact on Scotland's economic recovery and the pessimistic scenario reflects these challenges.

The pessimistic scenario sees Scotland recovering to its pre-pandemic levels by Summer 2023, over 2 years from now and over 3 years from the trough of this economic crisis.

Chart 1: Scottish Economic Growth scenarios: 2020 to 2025 based upon return to 'pre-crisis level'



Source: *Fraser of Allander Institute*

Table 1: Scottish Economic Growth scenarios: 2020 to 2025 based upon return to 'pre-crisis level'

	Trough	Return to pre-crisis level	Recovery time	2021 annual growth	2022 annual growth
Optimistic	Apr-20	Jun-22	2 years, 2 months	4.2%	5.9%
Central	Apr-20	Oct-22	2 years, 6 months	3.6%	5.6%
Pessimistic	Apr-20	Jul-23	3 years, 3 months	2.4%	5.5%

Source: *Fraser of Allander Institute*

Where are we now?

After some short-lived freedom over the summer months of last year, Scotland introduced a five-tiered restrictions system, with a third of Scottish local authorities in the strictest tier by the end of November.

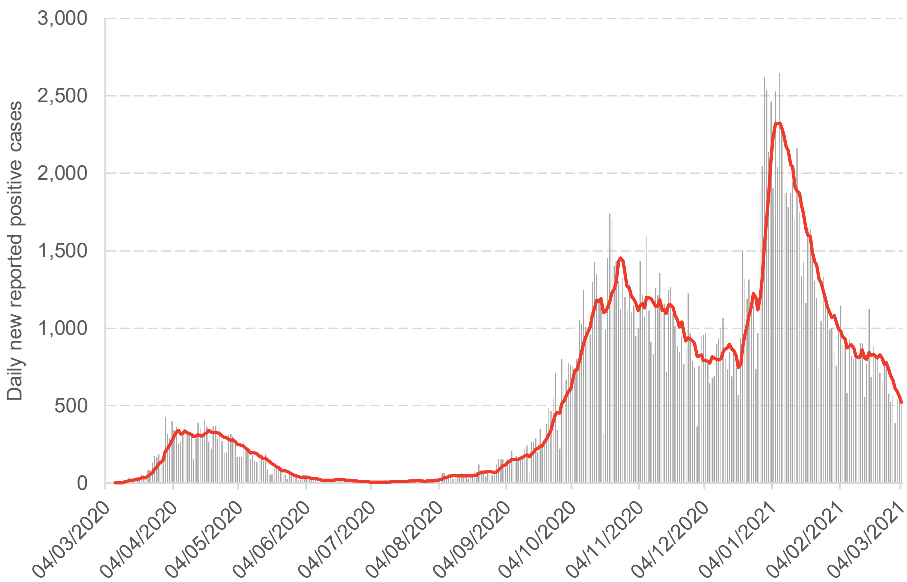
While families across Scotland were given the chance to mix in a group of a maximum of eight people from three households on Christmas day, Boxing day saw tier 4 restrictions imposed across Scotland; with the exception of some Scottish islands. The new year brought a national lockdown, with a stay at home message returning on the 5th January 2021 for the majority of Scotland.

Following the festive period, the number of daily reported new cases of COVID-19 hit all-time highs; however, it must be noted that the number of tests carried out are far greater now than they were last year during the first national lockdown.

However, since January, the number of daily cases reported have been falling and the rollout of COVID-19 vaccines has helped suppress the spread of the virus. Chart 2.

As of 25th February, in Scotland, first-dose vaccinations of over 75s have exceeded estimated population sizes and 98% of the estimated population of 70-74 year olds have been vaccinated with their first dose. The rollout of the vaccine is now reaching younger individuals and, as of late February, 85% of 65-69 year olds have received their first dose of the COVID-19 vaccine.

Chart 2: Number of reported daily new positive cases and 7-day rolling average, Scotland, 4th March 2020 – 4th March 2021



Source: *Scottish Government*

So, what impact has tougher restrictions following the festive period had on the Scottish economy towards the end of 2020?

Scottish GDP across all industries fell by 1.5% in November, followed by a 0.3% decline in the month of December. In December, the Scottish economy was 7.2% below pre-pandemic levels; this compares to 6.2% in the UK economy. Data published last week showed that the UK economy contracted by 2.9% in January 2021, meaning it is 9.0% below pre-pandemic levels. Chart 3.

However, as we have discussed in our previous commentaries, there has been an asymmetric hit to certain sectors, such as the accommodation and food services and arts, culture and recreations industries.

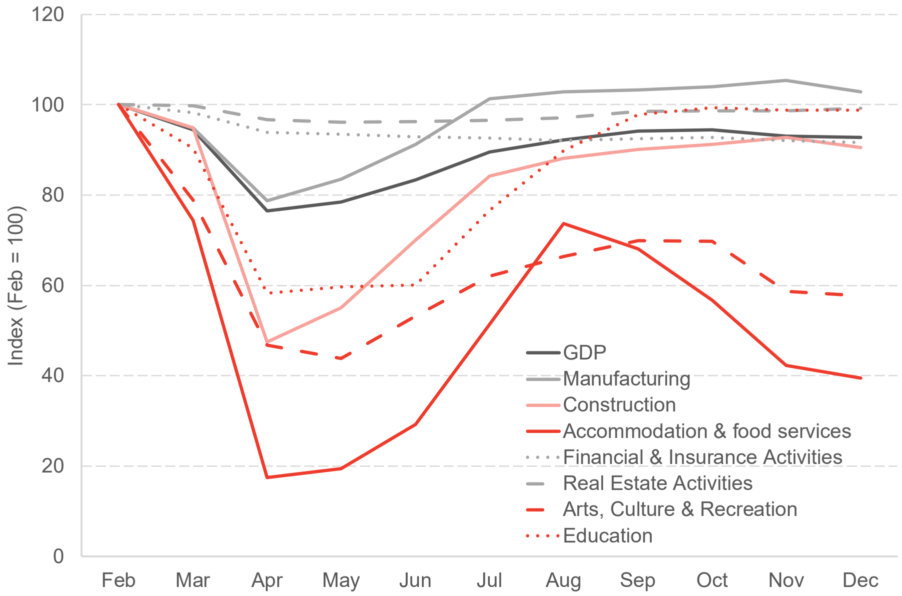
The hospitality industry in December was producing just 40% of its pre-pandemic output; levels similar to that in June/July of last year.

Despite tightening lockdown restrictions, the manufacturing sector remains above pre-pandemic levels and policies such as the Stamp Duty relief have kept industries like real estate close to pre-pandemic output levels.

Real estate activities actually experienced growth of 0.6% in December. Given that this sector makes up a significant 12% of the Scottish economy, it has been an important driver of economic growth in the economy.

The UK Budget, published this month, announced an extension of the stamp duty holiday until the end of June 2021 however, as stamp duty (Land and Building Transaction Tax (LBTT)) powers are devolved to Scotland, this holiday is still expected to finish at the end of this month; as announced in the Scottish Budget in January. This divergence in policy could result in some differentials in growth between Scotland and the UK in the coming months given the significance of the real estate sector to these economies.

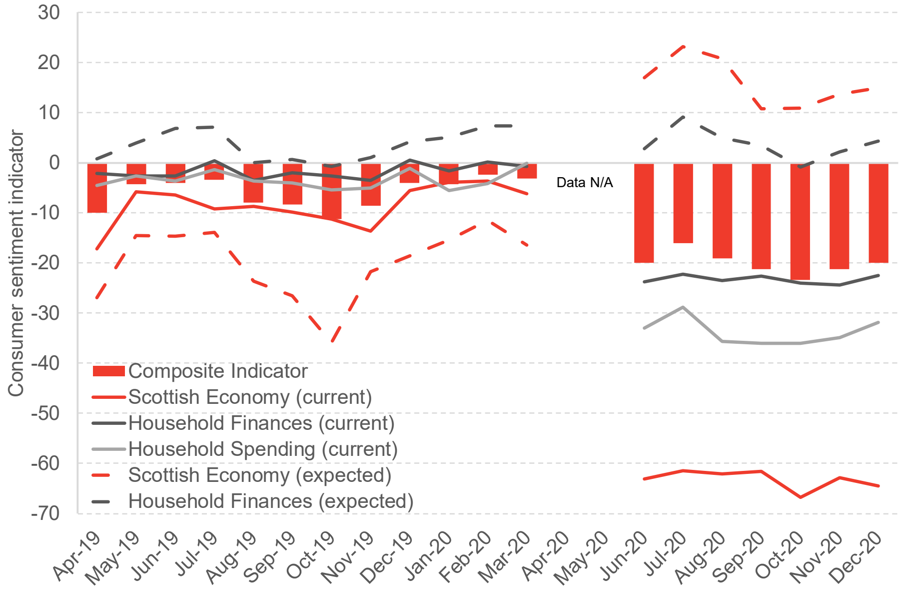
Chart 3: Monthly GDP index, Scotland, Feb – Dec 2020



Source: *Scottish Government*

However, although consumer sentiment remains at historic lows, expectations about economic development and household finances are now positive, with net balance responses for both indicators recovering from a fall in October 2020. Chart 4.

Chart 4: Scottish consumer sentiment indicator, April 2019 – December 2020



Source: *Scottish Government*

Real time indicators of Scotland's economic performance

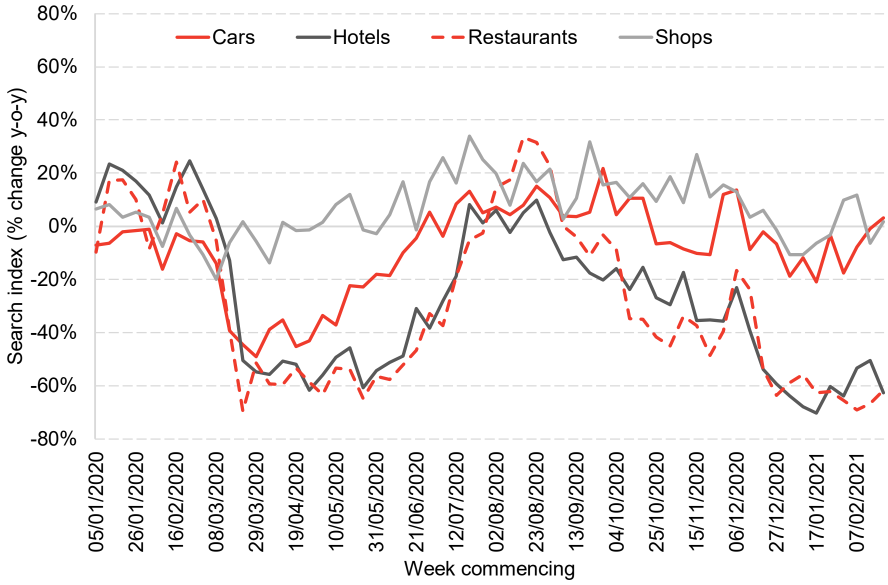
Traditional economic indicators such as GDP are often available with a lag. During fast developing crises, such as the COVID-19 pandemic, there is a need to track developments in the economy at a higher frequency. During the pandemic, the FAI has been tracking several real time indicators which are able to provide a timely picture about the state of the Scottish economy.

The indicators show that the winter wave of Covid-19 and associated lockdowns have taken a toll on economic activity. However, the magnitude of decline in activity has been less pronounced compared to the first wave.

Trends in Google searches are a useful indicator of consumer sentiment. They can also provide an indication about other macroeconomic variables such as demand for investment and credit.

In January and February 2021 searches for hotels and restaurants reached similarly low levels compared to the height of the first lockdown. However, searches for cars have remained more robust, suggesting that consumer confidence may not have fallen as much this time around. Chart 5.

Chart 5: Searches for different products and services, Scotland, week commencing 5th January 2020 – 21st February 2021

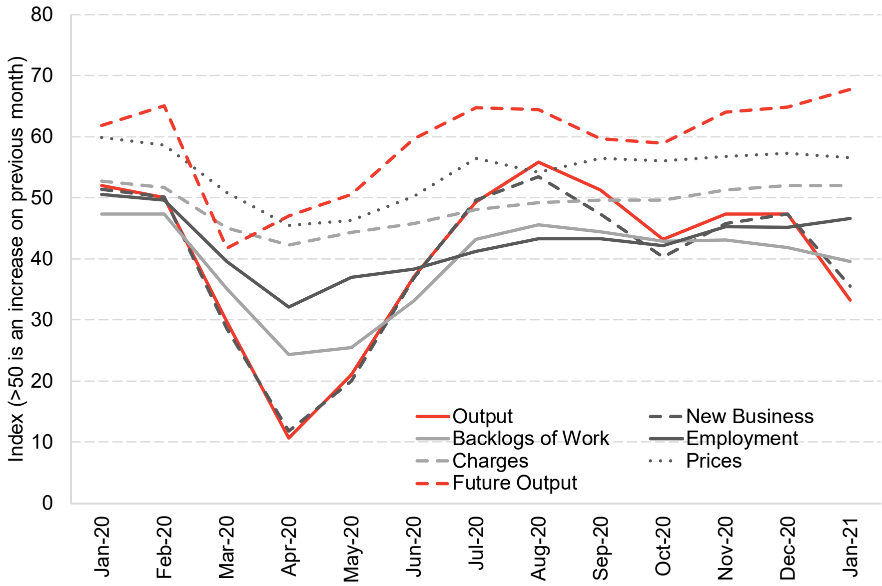


Source: *Google Trends*

The PMI index summarizes whether market conditions, as viewed by purchasing managers, are expanding, staying the same, or contracting.

Since October 2020, output, volumes of new business, backlogs of work, and employment have been falling. The decline intensified in January 2021 for output and new business due to the second lockdown. However, the month-on-month magnitude of this decline was smaller compared to April 2020. Prices, charges, and expectations of future output have remained positive over the past couple of months. Chart 6.

Chart 6: Composite PMI index, Scotland, January 2020 – January 2021

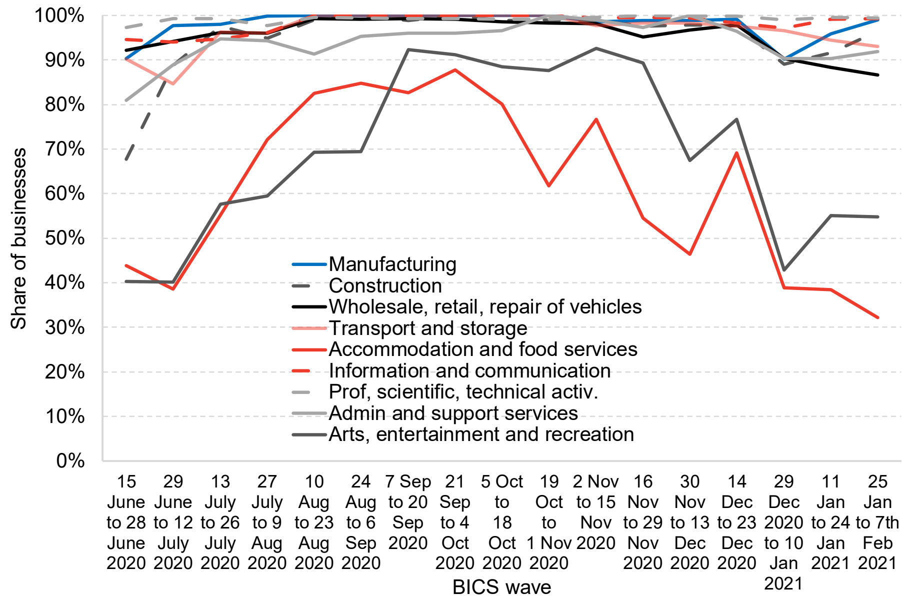


Source: *IHS Markit*

Business Impact of COVID-19 Survey (BICS) data on the share of businesses trading in Scotland highlights the varied impact of the crisis on different sectors.

Most sectors of the economy remain open, but accommodation & food services and arts, entertainment, & recreation had only 32% and 55% of businesses trading at the beginning of February. Chart 7.

Chart 7: Estimated share of businesses that are currently trading, broken down by industry, Scotland, 15th June – 7th February 2021.

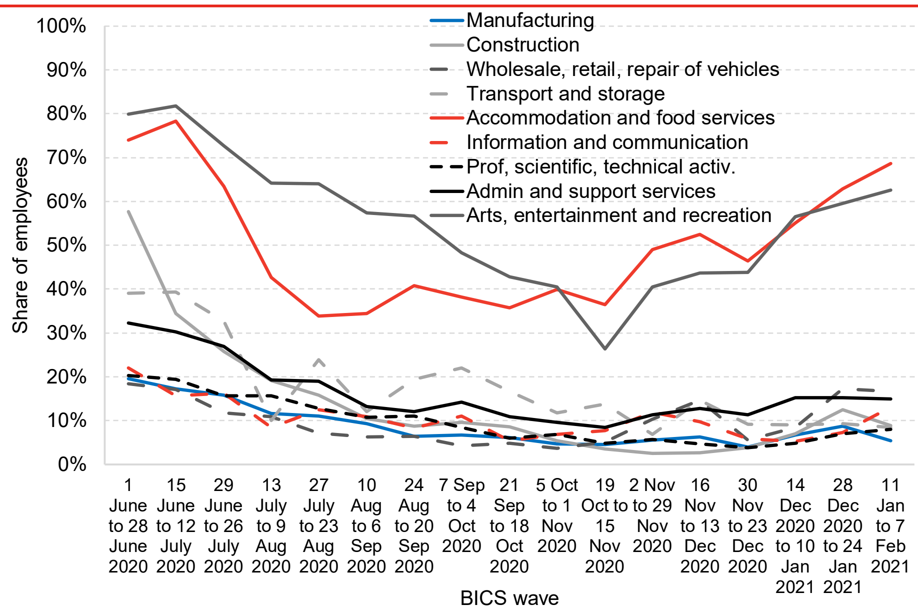


Source: *Scottish Government*

The closure of certain sectors of the economy and reduction in demand has led many businesses to put workers on furlough once again.

The furlough scheme has been most widely used by the sectors most affected by business closures – accommodation & food services and arts. As of the start of February, approximately 69% and 63% of employees in these two sectors were on furlough. This is slightly lower compared to the first lockdown. Other sectors of the economy have so far not seen significant increases in furloughing.

Chart 8: Estimated share of employees on furlough by sector, Scotland, 1st June 2020 – 7th February 2021

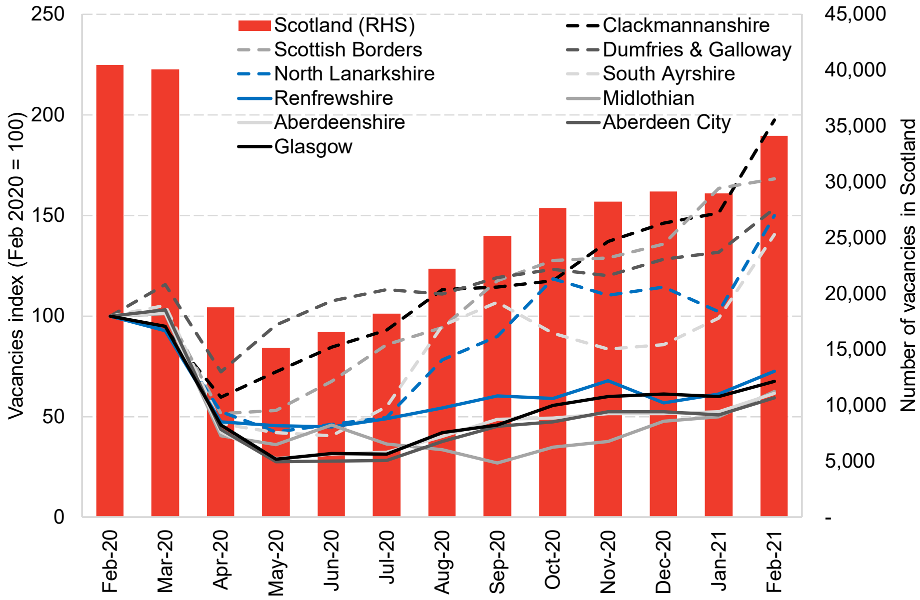


Source: *Scottish Government*

The number of advertised vacancies in Scotland rose from 28,960 in January 2021 to 34,110 in February 2021. However, this masks a wide degree of difference across Scottish local authorities.

Vacancies in Glasgow, Aberdeen City, Aberdeenshire, and Renfrewshire remain around 30 – 40% below pre-Covid levels. On the other hand, Clackmannanshire, Scottish Borders, North Lanarkshire, Dumfries & Galloway, and South Ayrshire have all seen growth in vacancies since May 2020; and are now 40 – 70% above pre-Covid levels. Chart 9.

Chart 9: Number of vacancies across Scotland, 'best' and 'worst' performing local authorities, February 2020 to February 2021



Source: *Adzuna Labour Market Stats*

Labour market

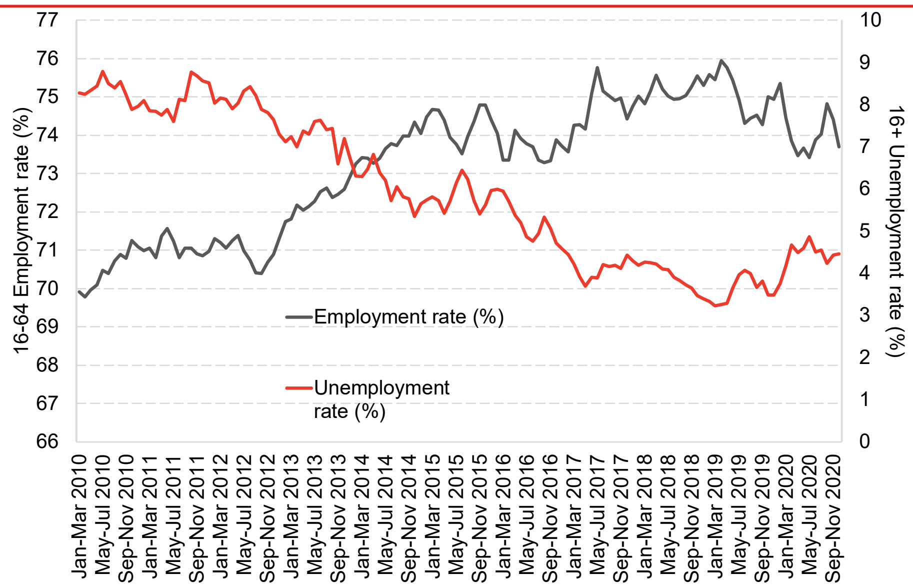
The extension to the UK's furlough support scheme announced in the Budget earlier this month will likely ensure that there remain modest movements in headline labour market measures through much of 2021. Chart 10.

Table 2: Headline labour market indicators, UK, Oct - Dec 2020

	United Kingdom	Wales	Scotland	Northern Ireland
16-64 Employment rate (%)	**75.0**	**72.2**	**73.7**	**69.4**
Change on year before	-1.5	-2.2	-1.3	-3.0
16+ Unemployment rate (%)	**5.1**	**4.4**	**4.5**	**3.6**
Change on year before	1.3	1.5	1.0	1.2
16-64 Economic Activity rate (%)	**20.9**	**24.3**	**22.8**	**28.0**
Change on year before	0.4	1.0	0.6	2.1

Source: *ONS; LFS*

Chart 10: Unemployment and employment rate, Scotland, Jan 2010 - Dec 2020



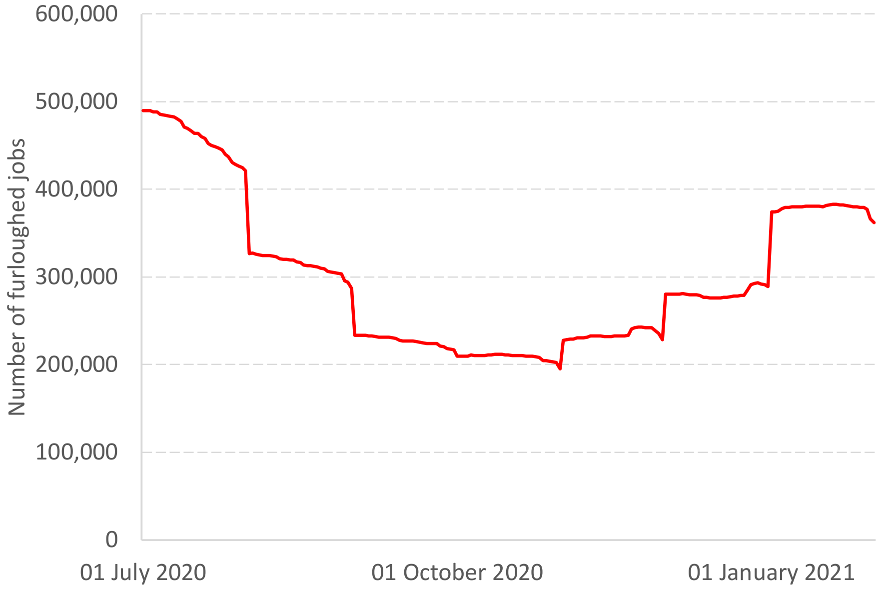
Source: *ONS; LFS*

The latest data have over 360,000 jobs in Scotland still furloughed at the end of January 2021. Chart 11.

Despite this furlough support, wider indicators of the health of the labour market continue to paint a worrying picture.

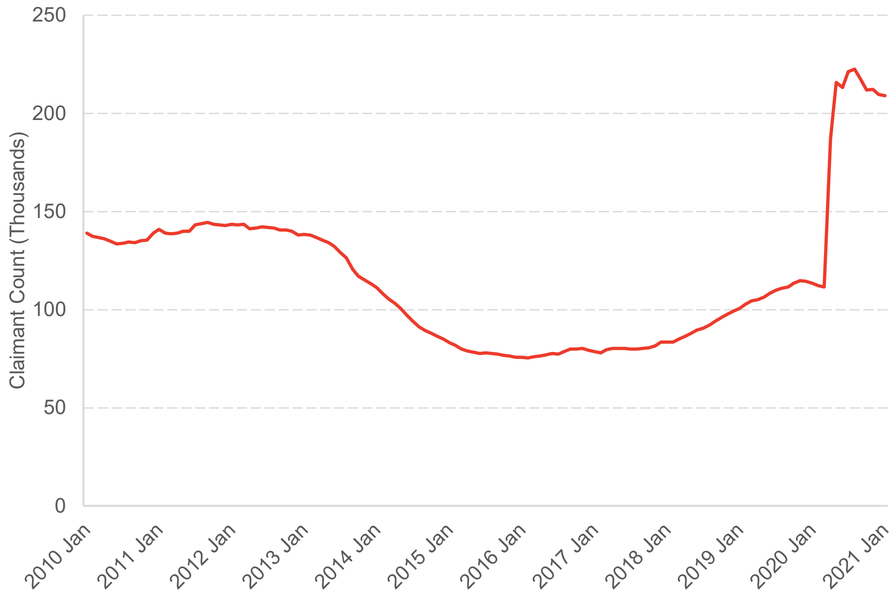
We've seen the number of people claiming unemployment related benefits in Scotland drop back slightly, and is now sits 87% higher than it was March 2020. Chart 12.

Chart 11: Number of people furloughed, Scotland, 1st July 2020 - 31st Jan 2021



Source: *HMRC*

Chart 12: Claimant count, Scotland, Jan 2010 - Jan 2021



Source: *ONS; LFS*

This represents an increase of over 97,000 people – and despite furlough support remaining in place.

UK wide data can provide timelier, and sometimes additional, indicators of labour market indicators than those available for Scotland.

From these data we can see that the recovery in hours worked witnessed since last summer began to taper off at the end of 2020.

There were still 7% fewer hours being worked in the UK economy at the end of 2020 compared to the same period in 2019.

Data on redundancies suggest that these have eased up slightly from the recent peak, but remain high and at a comparable rate to the peak during the 2007 – 08 financial crisis.

Meanwhile for those seeking work, the number of vacancies remains well below pre-pandemic levels.

At the end of 2020 there were over 200,000 fewer vacancies in the UK than there were at the end of 2019.

While there was a recovery in the number of vacancies in the second half of 2020, these remain over 25% down on the pre-pandemic period.

There is some evidence that pay has been growing again in the UK, with annual growth in total pay reached 4.7% at the end of 2020.

However, it is important to understand that part of this relatively robust rate of pay growth is being driven by changes in the composition of those in work.

Falls in employment in lower paid work combined with more stability in employment for those in better paid jobs is acting to drive up measures of average pay.

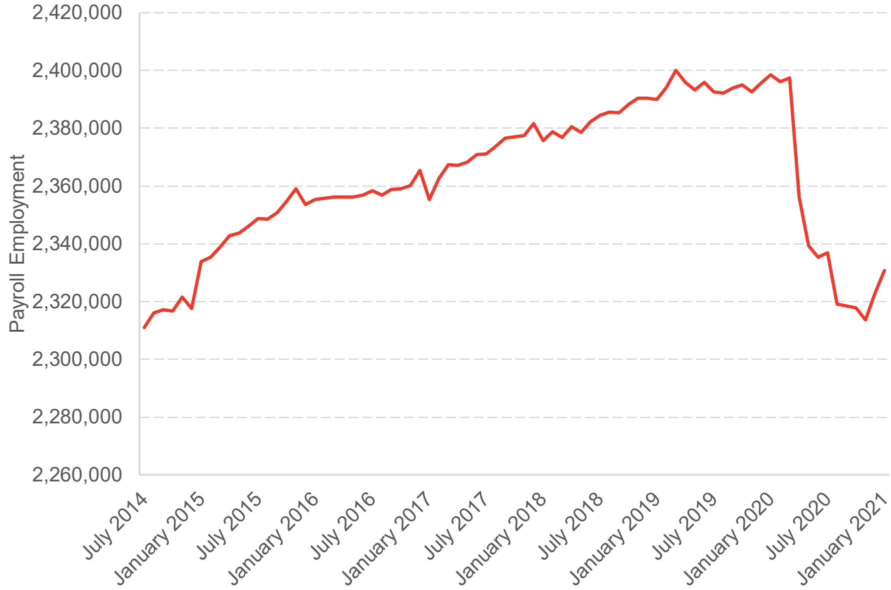
Since the onset of the pandemic we've been receiving some new experimental labour market data.

One of these is payroll data from HMRC – essentially data from the tax system tracking those registered for pay-as-you-earn (PAYE) taxes.

Two notable things can be seen looking at these data for Scotland.

The first is that we've seen more of a fall in payroll employment than the fall in the headline employment rate from the Labour Force Survey. Chart 13.

Chart 13: Payroll employment, Scotland, July 2014 - January 2021



Source: *ONS*

The second is that these data underline the differing economic experience of parts of Scotland through the pandemic.

Most notably the North East of Scotland which has endured a downturn in the Oil and Gas sector in the immediate period before the start of the pandemic.

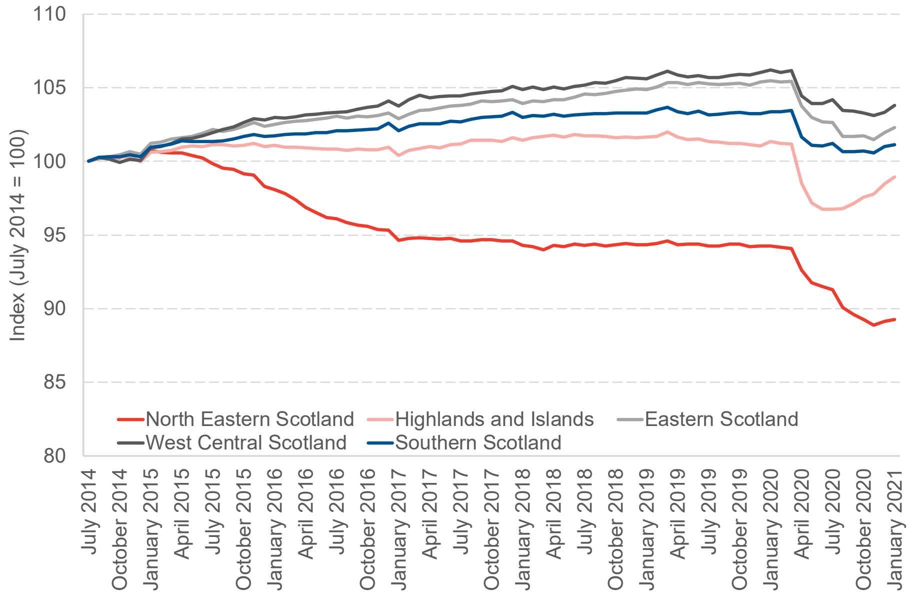
Payroll employment in the North East is down by nearly twice as much as it is for Scotland as a whole. Chart 14.

The outlook for the labour market through 2021 remains hugely uncertain.

On the one hand the rapid rollout of the vaccine across the UK should act to speed up the reopening of the economy, and in turn a rebound in employment.

On the other hand, it is only when we begin to restart the broader economy that the full toll that the pandemic has taken on the economy will become clear.

Chart 14: Payroll employment, NUTS2 Regions, Scotland, July 2014 - January 2021



Source: *ONS*

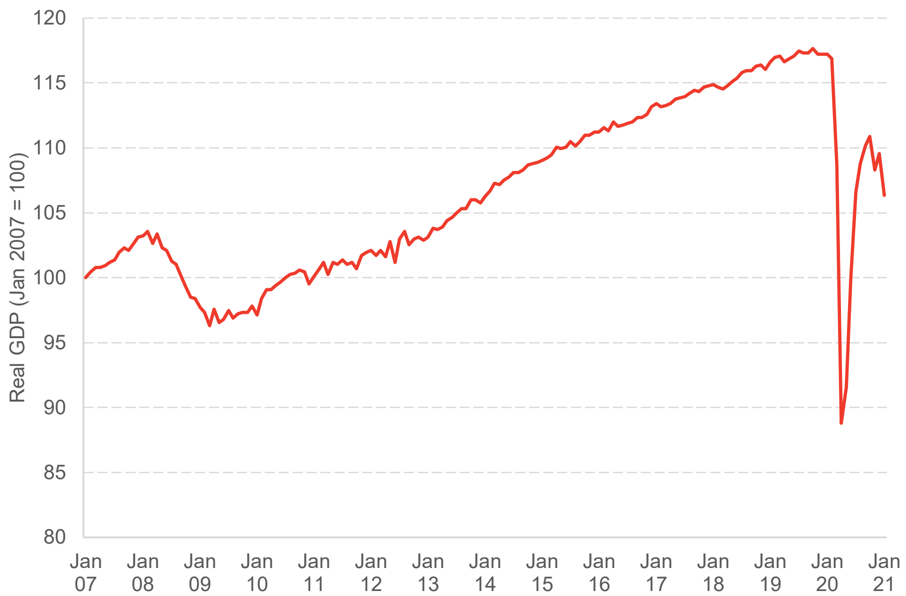
UK economy

UK GDP contracted by 2.9% in January 2021 after an increase of 1.2% in December. As discussed, UK GDP in January was 9% below February 2020, or 'pre-pandemic', levels. Chart 15.

Services drove most of the decline in GDP in January after contracting by 3.5%; education and wholesale and retail trade negatively contributed the most to overall GDP, following the tightening of restrictions across the UK at the start of the year. Services remain 10.2% below February levels.

Production contracted by 1.5% in December whilst construction grew by 0.9%; one of few positive contributors to GDP growth. Despite being severely impacted by the pandemic last spring, construction has bounced back relatively quickly and is just 2.6% below pre-pandemic levels.

Chart 15: GDP index (Jan 2007 = 100), UK, Jan 2007 – Jan 2021



Source: *ONS*

The Oxford COVID-19 Government Response Tracker (OxCGRT) tracks closure and containment policy responses of the UK's four nations to COVID-19.

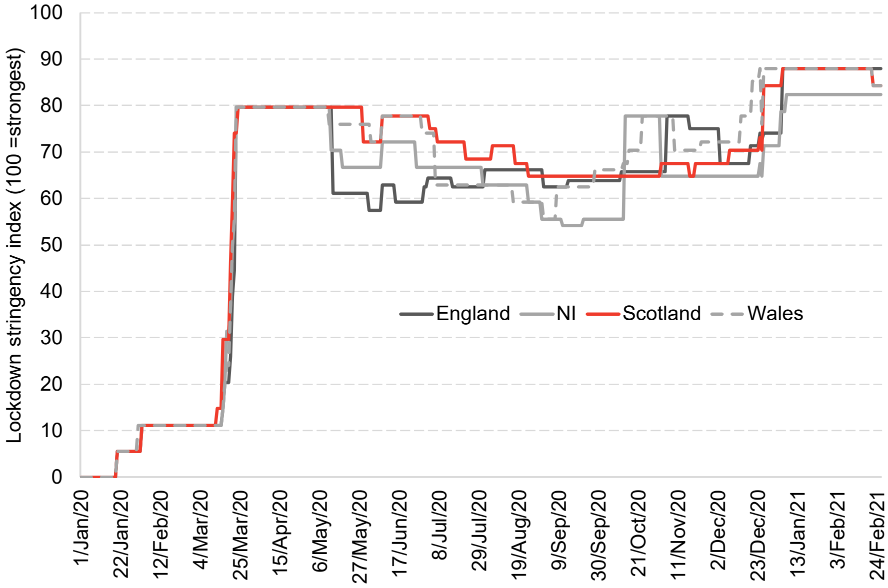
The UK's four nations have differed in their policy response to COVID-19 in terms of closure and containment policies.

Scotland has mostly maintained the strictest lockdown restrictions across the UK – with the exception of England's November national lockdown. Chart 16.

During the first lockdown UK nations followed a similar policy response however, approaches to containing the virus diverged in summer months as economies opened back up.

However, since the start of 2021 lockdown, restrictions across the UK have been more consistent - and similar to that seen in the first lockdown last spring - with a clear stay at home message from UK governments.

Chart 16: Lockdown stringency index, UK, 1st January 2020 – 26th February 2021



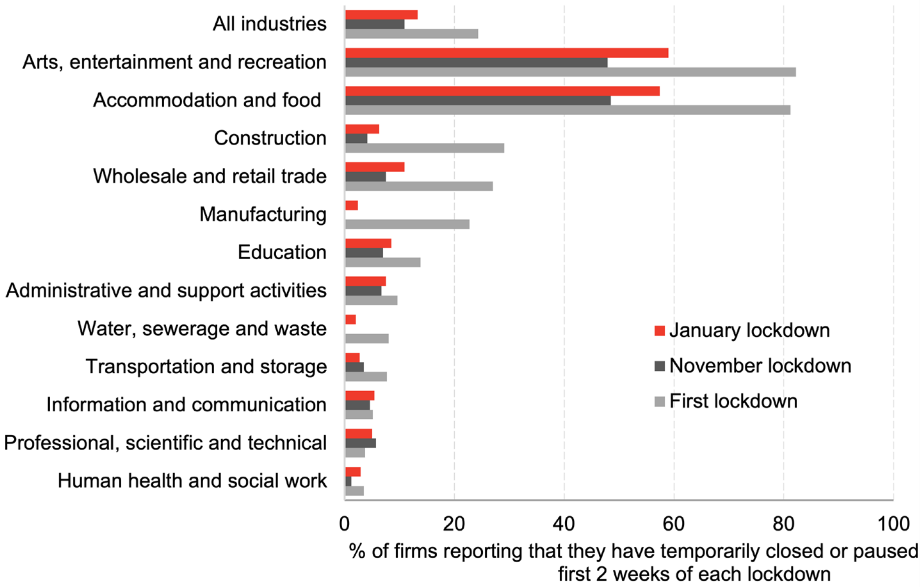
Source: *University of Oxford*

The ONS's Business Impact of COVID-19 Survey (BICS) shows that businesses experienced more widespread closures in the first lockdown in spring last year, with 24% reporting they had temporarily closed. This compares to just 11% and 13% in November and January respectively.

These figures highlight the adaptability of businesses throughout the past year – many businesses have implemented COVID-safe measures, i.e. plastic screens, social distancing markers, etc., which have allowed them to be better equipped to operating throughout a lockdown.

Accommodation and food services has been the most significantly impacted sector across the UK however, firms have been able to adapt and move towards takeaway services and contactless deliveries which have allowed more businesses to operate during the past two lockdowns compared to the first. Chart 17.

Chart 17: Share of firms closing or pausing trading at the start of each lockdown, UK



Source: *OBR; ONS*

Online retail experienced significant growth during the first lockdown which tapered off slightly as the economy began to open back up in summer months. During this period of reopening, footfall in stores began to increase, along with their sales.

The current lockdown has resulted in a similar pattern in retail emerging, with online retail sales expanding and store retail declining; however, not as much as the first national lockdown. Chart 18.

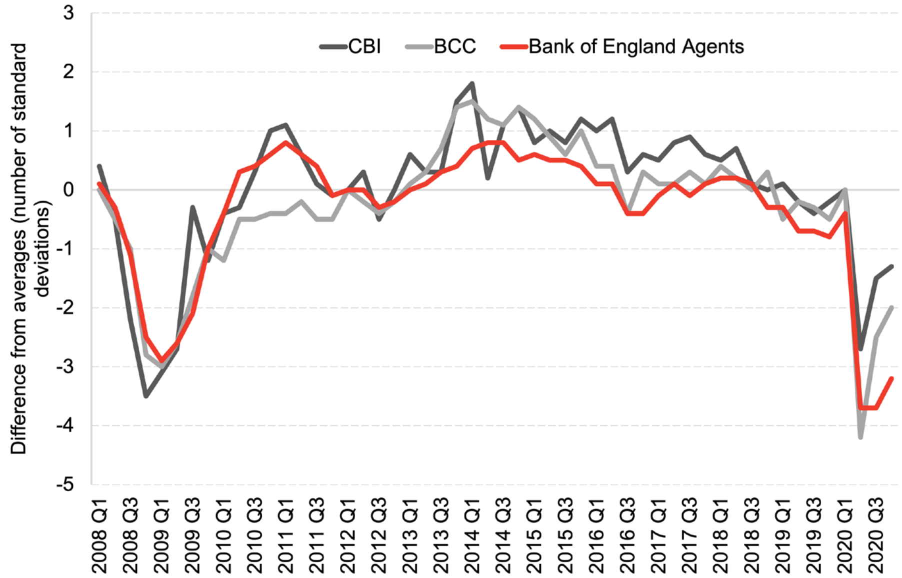
Chart 18: Retail sales index, seasonally adjusted (Jan 2020 = 100), Great Britain, Jan 2020 – Jan 2021

Source: *ONS*

Investment intentions remained weak in Q3 of 2020 however, it was up on the trough experienced in Q2. Chart 19.

Businesses cancelling or delaying investment plans has both short and medium term impacts on the economy, meaning that the impact of COVID-19 on the economy will persist for some years to come.

Chart 19: Survey indicators of investment intentions, UK, 2008 Q1 – 2020 Q4



Source: *BoE*

The UK Government's budget, published earlier this month, included a range of support for businesses and households. In particular, the budget includes a temporary tax break, worth £12bn a year, to stimulate business investment.

Given this month's budget, some forecasts of the UK economy are slightly more optimistic; economic growth projections for 2021 range from around 4-5%. Table 3.

Table 3: UK GDP growth projections, 2021 - 2023

	2021	2022	2023
BoE	5%	7.3%	1.3%
OBR	4%	7.3%	1.7%
NIESR	3.4%	4.3%	2.3%
IMF	4.5%	5%	-
Oxford Econ	5%	6.1%	-
ITEM club	5%	6.5%	-
IFS	4.6%	3.6%	2.4%
HM Treasury	4.4%	5.7%	-

Source: *BoE, OBR, NIESR, IMF, Oxford Economics, ITEM club, IFS, HM Treasury*

Global economy

Projections for the Global economy follow UK forecasts fairly closely with most institutions forecasting growth of around 4-5% in 2021.

While the UK is projected to grow by around 5-7% in 2022 and 1-2% in 2023, the global economy is forecast to experience growth of around 2-5% in 2022 and 2-4% in 2023.

While forecasts are broadly similar, the global economy is expected to see economic growth spread more evenly across the next few years while the UK economy is projected to have a strong 2022 and then a bit of levelling off in activity the following year.

Table 4: World GDP growth projections, 2021 – 2023

	2021	2022	2023
BoE	4.8%	5%	2.3%
OBR	5.5%	4.2%	3.8%
NIESR	4.4%	3.7%	-
EC	5.2%	3.8%	-
IMF	5.5%	4.2%	-
OECD	5.6%	4%	-

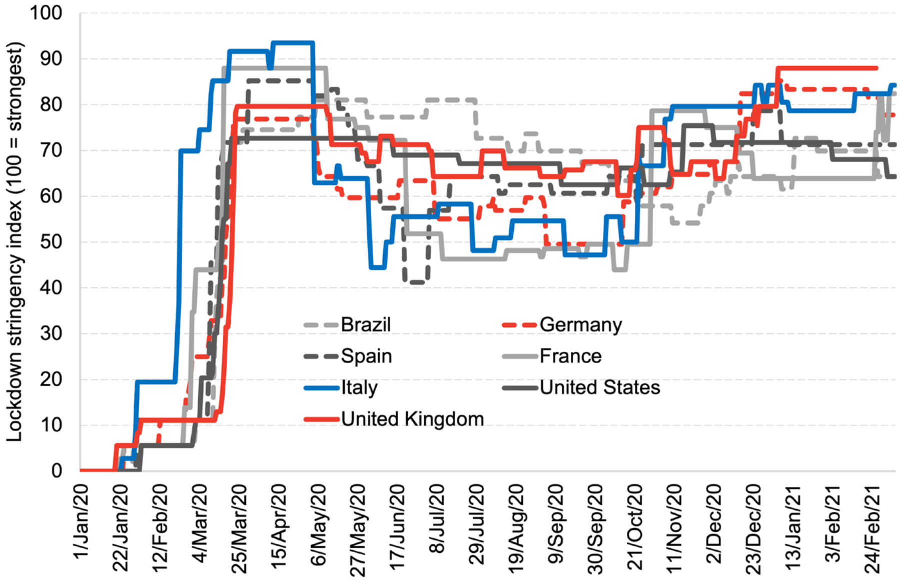
Source: *BoE, OBR, NIESR, EC, IMF, OECD*

The projected differentials in growth between the UK and the global economy is unsurprising if we look at lockdown restrictions in place worldwide.

The UK, like most countries, enforced a strict national lockdown last spring which eased in summer months. However, the current national lockdown in place across the UK is amongst the strictest of major economies. Chart 20.

The US has had more relaxed COVID-19 containment policies in place over the past year – relative to the countries in Chart 20 – however, it has remained at roughly the same level of restrictions since.

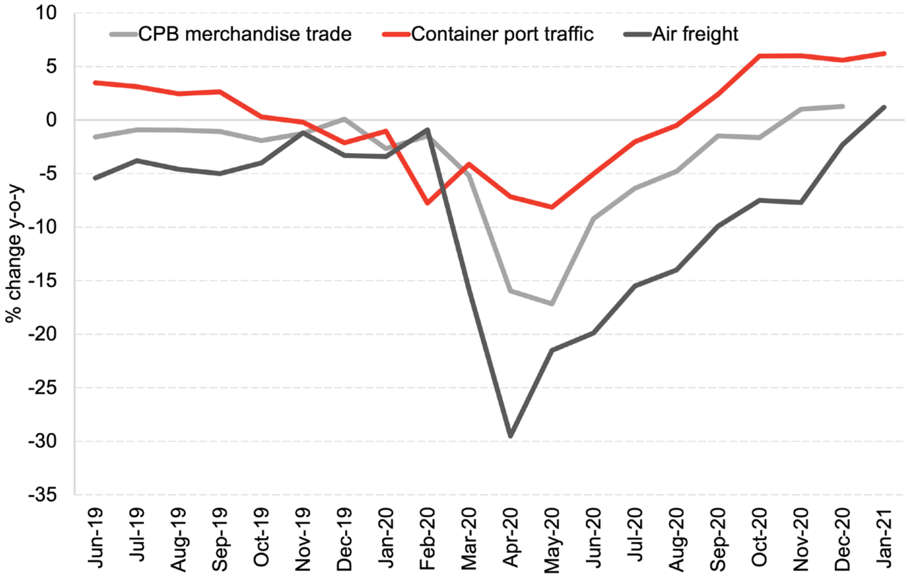
Chart 20: Lockdown stringency index, 1st January 2020 – 8th March 2021



Source: *University of Oxford*

Despite increasing lockdown restrictions globally in winter, global trade has been improving. Chart 21.

Chart 21: High frequency indicators of global trade, June 2019 – Dec 2020



Source: *OECD*

In terms of COVID-19 cases per one million of the population, the UK, Spain and, in particular, the US have been acutely impacted by the COVID-19 pandemic.

However, both the UK and US, alongside countries like Israel, are leading the world's vaccination race. Chart 22.

The UK has given first doses of COVID-19 vaccines to almost 24 million people in the population.

That is, around a third of the UK population have been vaccinated with their first dose so far.

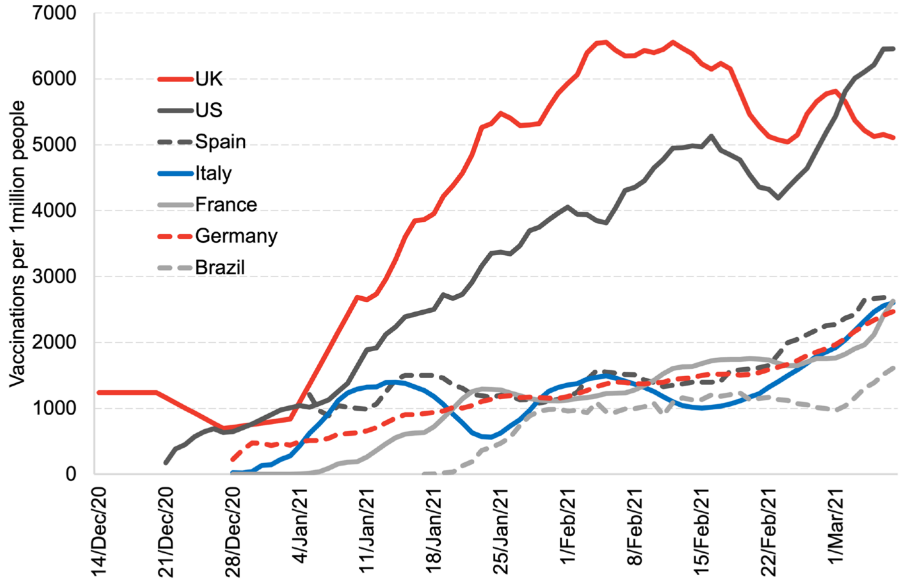
As the UK begins to vaccinate younger age groups within population, and provides second doses of the vaccine, in the coming months, this will support the reopening of the economy, allowing (hopefully) the economic recovery from this crisis to truly begin.

Although the winter has been difficult for many people around the world, there appeared to be some optimism across businesses and consumers in December; potentially driven by vaccine approvals that begun in December.

Confidence across OECD countries improved significantly towards the end of 2020, particularly among businesses. Business confidence has remained above pre-pandemic levels since August however, consumer confidence remains below February 2020 levels. Chart 23.

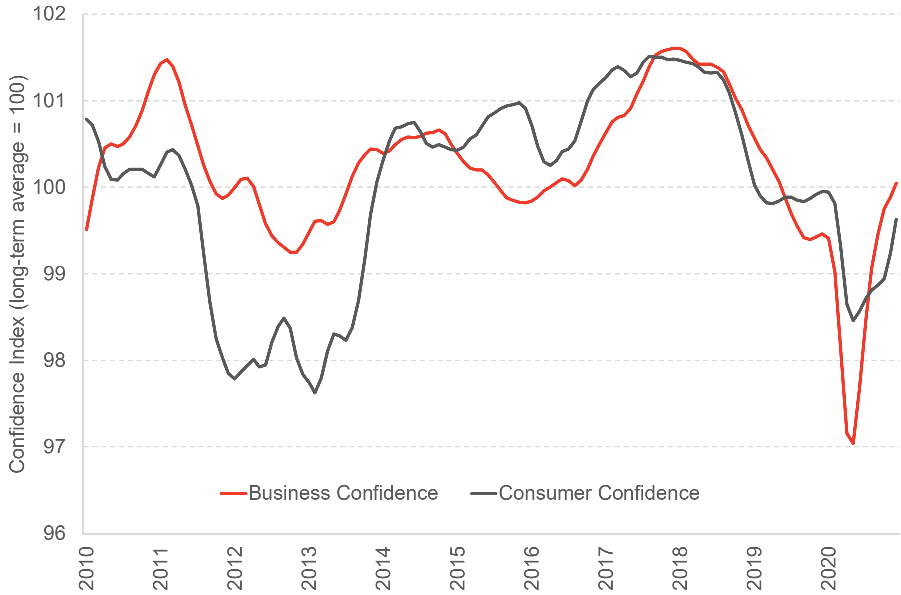
Despite a long winter, businesses have proven resilient and the rollout of COVID-19 vaccinations coupled with business adaptability provides optimism during a difficult time for households and businesses.

Chart 22: Covid-19 vaccinations administered per 1 million people, 14th December 2020 – 8th March 2021



***Source:** Our World in Data*

Chart 23: OECD business and consumer confidence indices, Jan 2010 – Dec 2020



***Source:** OECD*

Covid-19 impact on the Tourism and Hospitality Sector

While COVID-19 has had a significant impact on all sectors of the UK economy, some have been disproportionately affected by this health and economic crisis. In particular, tourism and hospitality suffered notable losses from the pandemic.

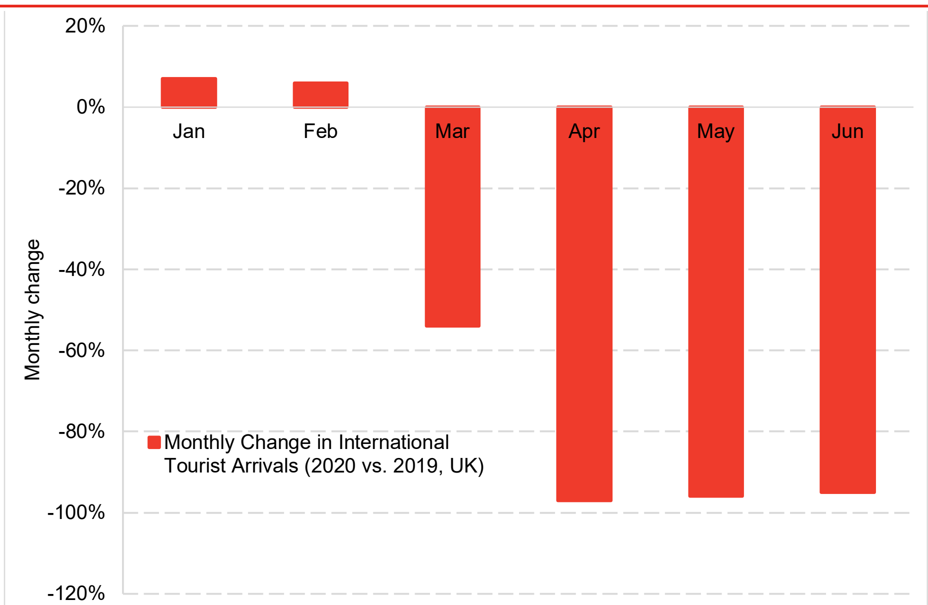
The COVID-19 pandemic led to an unprecedented simultaneous demand and supply shock to this part of the economy.

On the demand side, this was driven by travel bans, movement restrictions, curfews, and lost income.

Chart 24 shows the latest available data for international tourist arrivals to the UK in 2020 relative to 2019. The data shows a substantial decline in international tourist arrivals from March 2020 onwards.

This coincides with the introduction of lockdown restrictions globally as well as the national lockdown across the UK that came into effect in late March. During this period international tourist arrivals fell to record low levels, reaching -97% in April 2020 relative to April 2019.

Chart 24: International Tourism Arrivals in the UK, 2020 relative to 2019



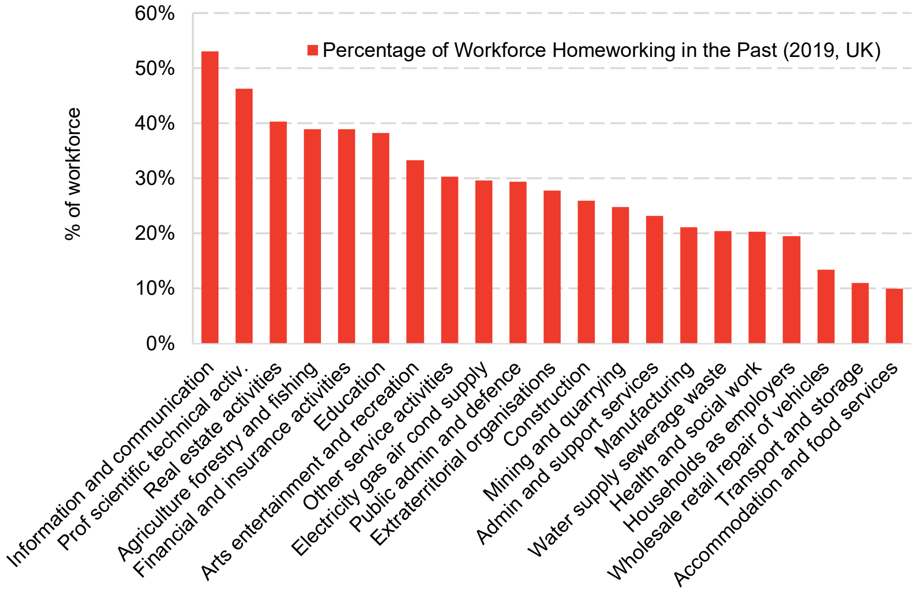
Source: *UNWTO*

On the supply side, many businesses across the tourism and hospitality sector have been forced to remain shut since the pandemic started. For instance, establishments selling food or drink were amongst the first to be closed to prevent the spread of COVID-19 and are expected to be some of the last to reopen completely.

Even when not forced to close completely, businesses in the sector had to follow strict social distancing guidelines, impacting their capacity limits and profitability.

In addition, tourism and hospitality businesses were often unable to adjust their operations to homeworking. This is unsurprising as accommodation and food Services, the largest subsector of tourism and hospitality, had the lowest share of workers that worked from home before the pandemic. As of 2019, only 10% of workers in this sector reported that they worked from home, compared to more than 50% in the information and communication sector. Chart 25.

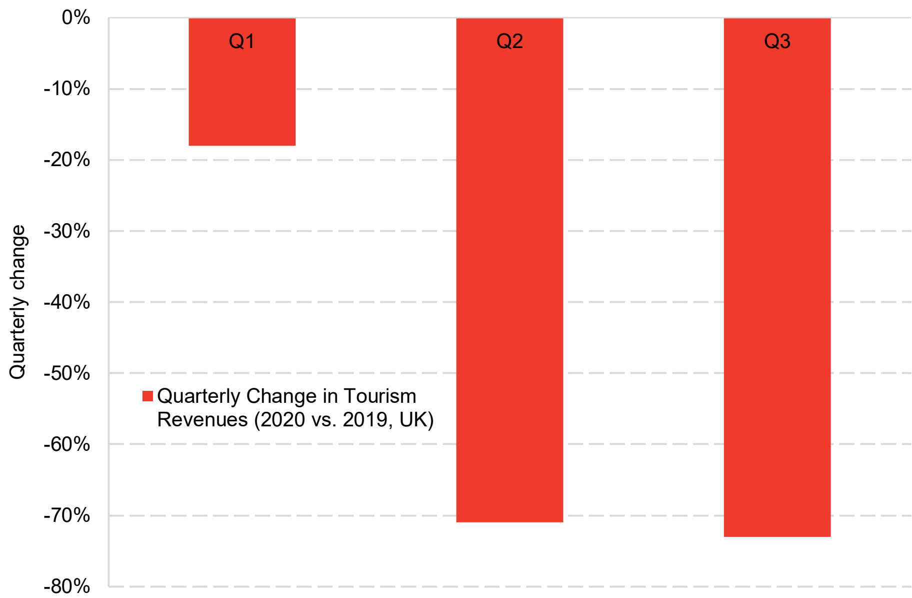
Chart 25: Percentage of people that ever worked at home, UK, 2019



Source: *ONS*

As a result of these supply and demand side shocks, revenues in the Tourism and Hospitality sector have taken a hit. Revenue for international tourism in the UK was down 73% in quarter 3 of 2020, compared to the previous year. Chart 26.

Chart 26: International Tourism Revenues, UK, 2020 relative to 2019



Source: *UNWTO*

The Scottish Hospitality Industry

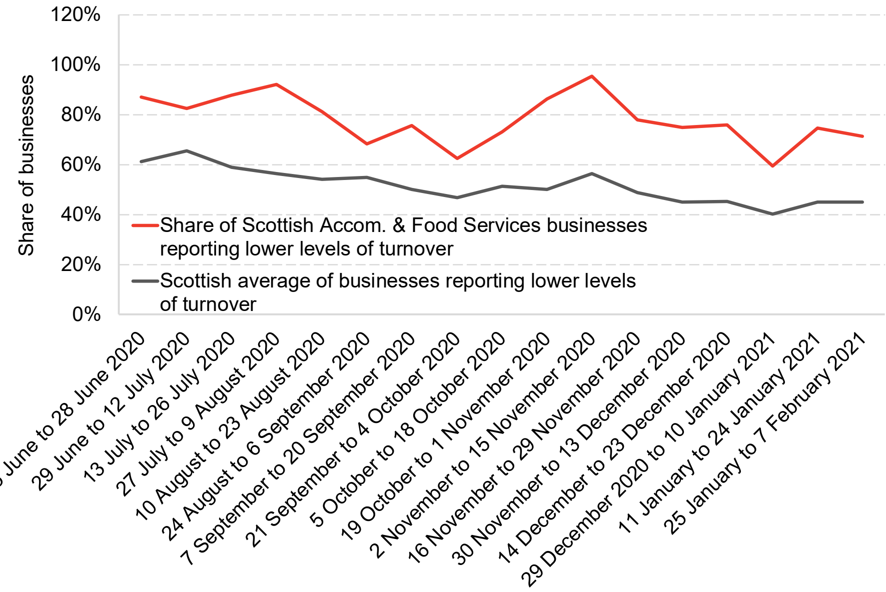
So, how has the pandemic impacted the Scottish hospitality industry?

Since June 2020 the share of operating accommodation and food services businesses reporting lower turnovers than usual was consistently above 60% and peaked in August and November 2020 above 90%.

The latest available data, covering late January and early February 2021, indicates no sign of a trend reversal with more than 70% of businesses in the sector reporting lower turnover than usual.

Comparing this number to the current cross-industry average of 45% shows how the sector is disproportionately affected by the pandemic.

Chart 27: Share of Scottish businesses reporting lower turnovers, 15th June 2020 - 7th February 2021



Source: *BICS Survey*

This figure may well underestimate the true impact on sector turnover, as it only covers operating businesses. The latest data indicates that currently only around one-third of food service and accommodation businesses are operating, compared to a cross-industry average of 80%.

This has a direct impact on employees: currently, 65% of the food services and accommodation workforce is on furlough and only 5% of the industry workforce is working from home. Table 5.

Table 5: BICS Survey results based on data from the 25th of January until the 7th of February, Scotland

Variable	Food Services and Accommodation	All Industries
Share of businesses currently trading	32.2%	80.9%
Businesses with staff on furlough	64.6%	61.0%
Workforce working from home	5.2%	26.4%

The Regional Impact on the Scottish Tourism and Hospitality Sector

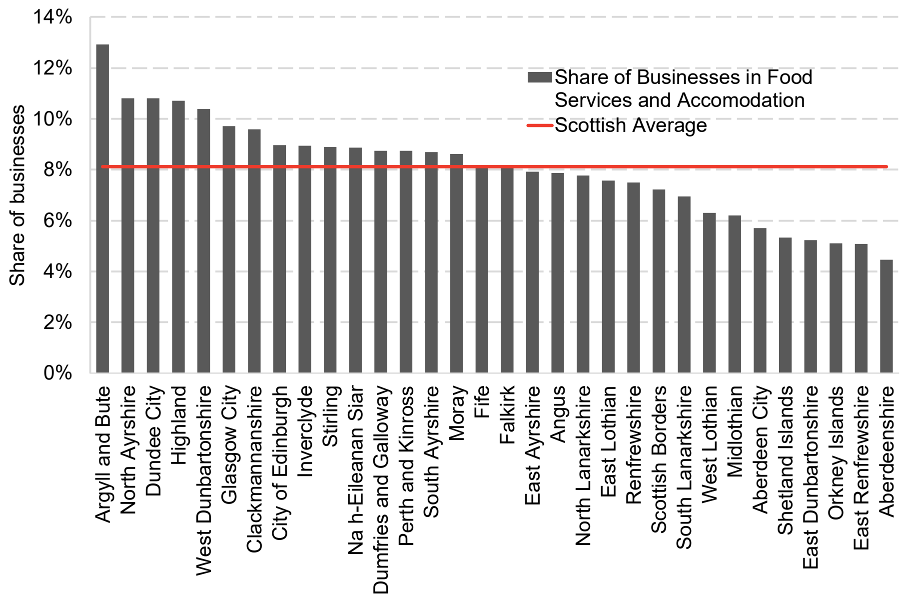
Previous commentaries showed that workers in the hospitality industry are younger, more likely to be female and earn particularly low wages. As a result, a shock to this sector threatens gender equality and income inequality more broadly.

To build on this analysis, one area we are focussing on in this commentary is the regional impact of this crisis to the hospitality sector.

Across Scotland, around 8% of businesses are in the hospitality sector. For some parts of the nation, such as the Highlands, North Ayrshire, and Argyll and Bute, this figure exceeds 10%. These areas are particularly reliant on tourism, making them more vulnerable to the economic impact of COVID-19.

Other parts of Scotland, such as Aberdeenshire have economies that rely much less on hospitality, making them more resilient to a shock in this area of the economy. Chart 28.

Chart 28: Share of Businesses in the Accommodation & Food Services industry, by region, 2020



Source: *Scottish Government and ONS*

Supply Chain and Demand Effects

Lastly, the crisis' impact on hospitality also has important supply chain and demand implications.

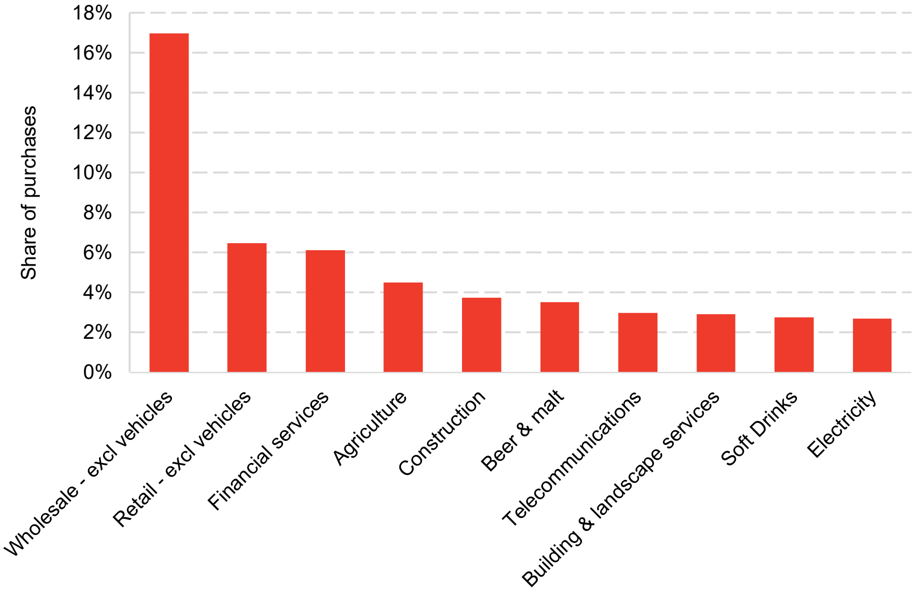
Chart 29 plots the largest suppliers to the accommodation and food services sector. We find that wholesale/retail, agriculture, and construction supply the most to this sector. These sectors therefore would have suffered indirect losses from the shock to hospitality throughout this pandemic.

But this crisis is not limited to the supply side.

Chart 30 shows the top 10 sectors by that purchase goods and services from the accommodation and food services sector.

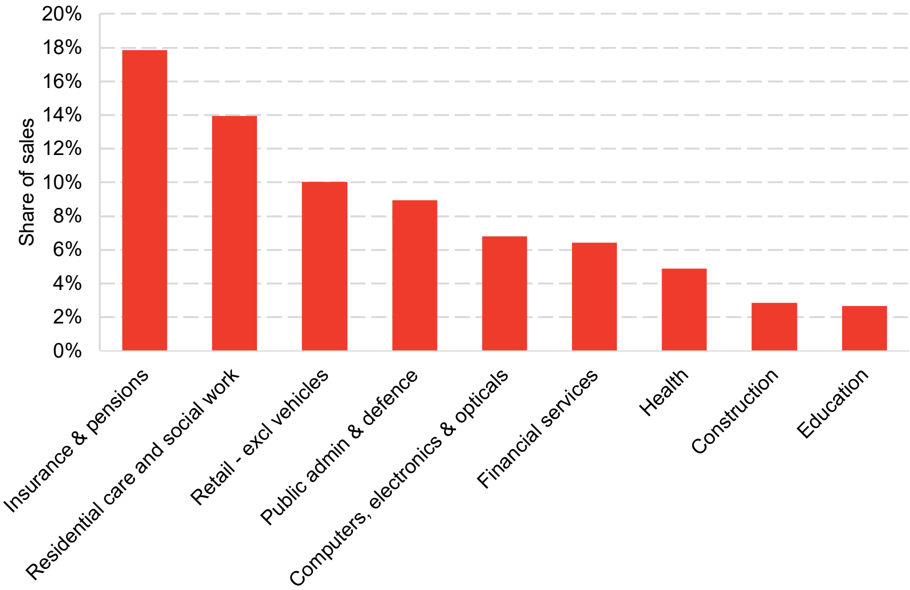
Insurance and pensions, Residential Care and Social Work, and Retail are the biggest buyers of services from this industry.

Chart 29: Biggest suppliers to Scottish Accommodation and Food Services Sector, 2017



Source: *Scottish Government*

Chart 30: Biggest sources of intermediate demand sectors from the Scottish Accommodation and Food Services Sector, 2017



Source: *Scottish Government*

The economic contribution of the accommodation and food services sectors to the Scottish economy

We have outlined what sectors supply to the hospitality sector in Scotland, and what sectors purchase from it. Therefore, it is evident that lockdown restrictions that have forced this sector to shut down would have had knock-on effects across the whole Scottish economy.

Although the national lockdowns have not resulted in complete shut downs of any industry, what would happen if the Scottish economy lost the hospitality sector?

Turning this question around, what is the economic value of the accommodation and food services sector to the Scottish economy?

In this section we model the economic contribution of the accommodation and food services sector to the Scottish economy.

This is carried out by hypothetically removing the accommodation and food services sector from the Scottish economy and estimating the size of the remaining economy - the difference between the original economy and the newly extracted economy is the contribution of the accommodation and food services sector to the Scottish economy[1].

The results highlight the direct, indirect and induced effects of the accommodation and food services sector. Figure 1.

Diagram 1: Direct, indirect and induced impacts

TOTAL IMPACT

Direct impacts
This measures the contribution from the actual spend and employment which underpins the accommodation and food services sector's own day-to-day activities.

+

Indirect impacts
This includes the economic benefits from the accommodation and food services sector's suppliers using the revenues from trading with the sector to, in turn, make expenditures on staff and other goods and services.

+

Induced impact
This includes the economic benefits from those employed directly by the accommodation and food services sector, spending their wages and salaries on goods and services across the Scottish economy.

Source: *Fraser of Allander Institute*

1 NB: this modelling does not assume that any other Scottish sectors are shut down nor is it done in a way to show the impact of COVID-19 lockdowns on the sector. Instead, it is hypothetically removing the sector from the economy using the Scottish Government's Input-Output (IO) tables from 2017 - before the COVID-19 pandemic - to highlight the importance of the sector to the Scottish economy.

Table 6 highlights the direct, indirect and induced impact of removing the accommodation and food services sector from the Scottish economy.

Table 6: Economic impact of the Accommodation and Food Services industry

	GVA (£bn)	Employment (FTE)
Total economic impact	7.6	200,700

Source: *FAI calculations*

The accommodation and food services industry contributes around £4.4bn in direct GVA to the Scottish economy.

However, when we add up the indirect and induced effects, the overall economic impact of the accommodation and food services sector to the Scottish economy increases to almost £7.6bn.

Across the Scottish economy the accommodation and food services sector supports over 200,700 direct, indirect and induced jobs. This total includes direct employment of over 153,600 in the accommodation and food services sector but also, thanks to spill-over effects, employment in other parts of the Scottish economy.

Conclusions

The hospitality sector has been asymmetrically impacted by the ongoing coronavirus pandemic and the subsequent national lockdowns and travel restrictions.

A large share of the sector remains shut down and a significant number of its workforce are still furloughed.

But, the impact of the closure of this sector is not limited to hospitality as its interconnectedness with other Scottish sectors means that there are spillover effects of shutting down this industry.

Our modelling suggests that, once knock-on effects are accounted for, the accommodation and food services sector supports -

- Almost £7.6bn in Scottish GVA; and,
- Over 200,000 FTE employment in Scotland.

This sector is a major contributor to the Scottish economy and work will need to be done in the future to ensure that this industry, and the employees working within it, are supported in Scotland's economic recovery from COVID-19.

Homeworking in Scotland

Back in December, we discussed homeworking and whether this new way of working was here to stay.

The opinions of businesses and employees were mixed at the end of 2020. For those in favour, it was the benefits to productivity and reduction in commuting times that were attractive.

But for those against homeworking, it was the reduction in office footprint that was noted as being a concern, particularly for businesses that rely on office footfall in cities.

This section provides an update to the analysis published at the end of last year, looking specifically at the opinions of businesses.

Homeworking in practice

Occupations

It is obvious that not all jobs can be performed at home.

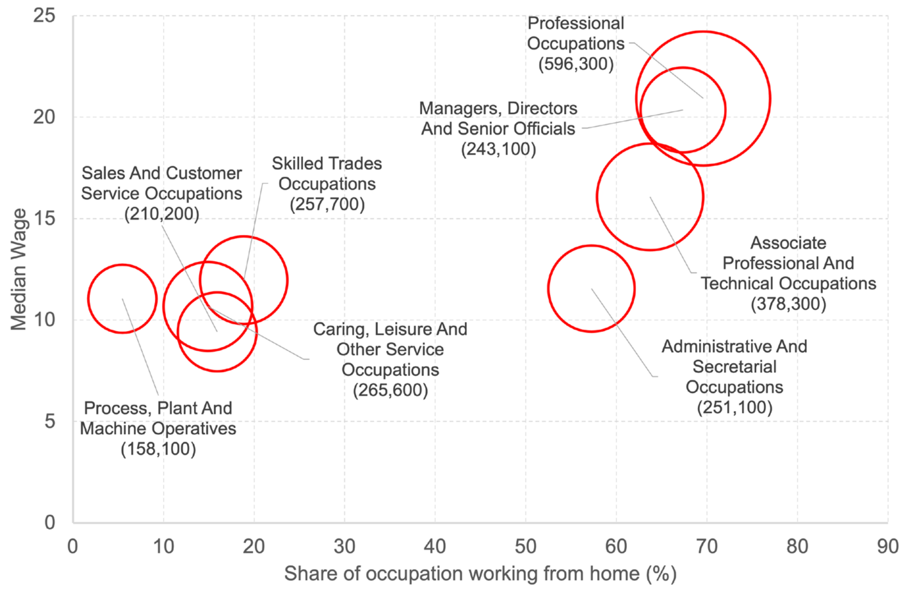
Yet, those jobs that can be done from home tend to not only demand higher wages but also make up a large part of Scotland's labour market.

Professional, Associate Professionals and Technical occupations account for around 41% of jobs in Scotland, and demand 1.5 times the Scottish median hourly wage. But these occupations have also had the highest share of employees working from home during the pandemic. Chart 31.

Yet when we compare this to those occupations in sectors affected the most by the pandemic, such as Sales and Retail staff - where median hourly wages are one third lower than the Scottish average - only 16% have been able to work from home.

The outlook for the inequalities gap in Scotland is therefore worrisome.

Chart 31: Proportion of responders working from home by occupation, UK, April 2020



Source: *ONS; ASHE; BRES*

Sectors

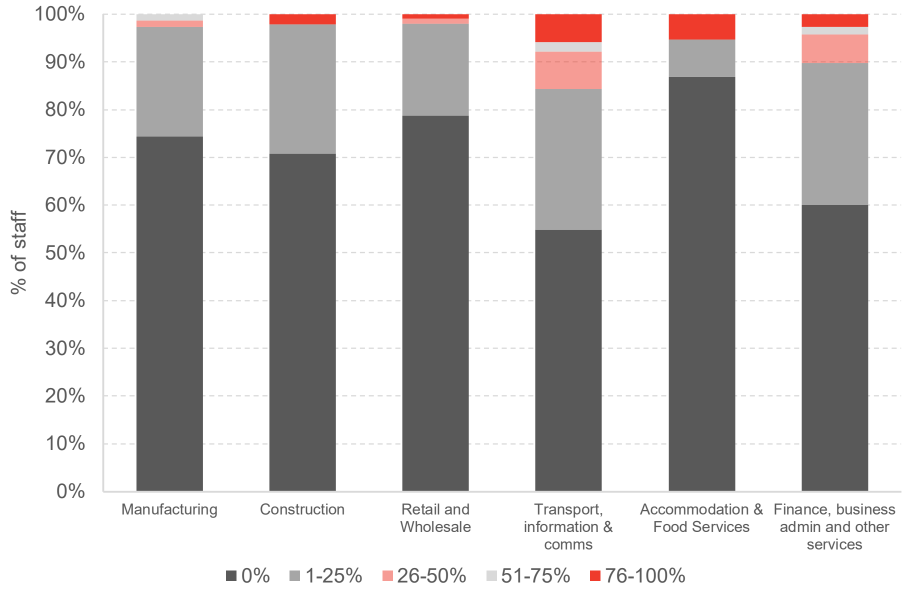
The defining feature of the current economic crisis has been how it has affected different sectors differently.

In particular, the hospitality and retail sectors have seen the majority of staff furloughed given the inability for many of these jobs to be done at home.

Whereas sectors in which homeworking is easier done, such as the financial and administrative sectors, have remained more resilient.

Chart 32 shows the proportion of staff working from at the end of 2020 compared to the same time one year before, highlighting the difference in the share of staff working from home in each sector.

Chart 32: What percentage of your staff are working from home currently, and worked from home this time last year? Q4 2020



Source: *Scottish Business Monitor*

Business Size

Work from home practices have also been a feature for businesses of all sizes.

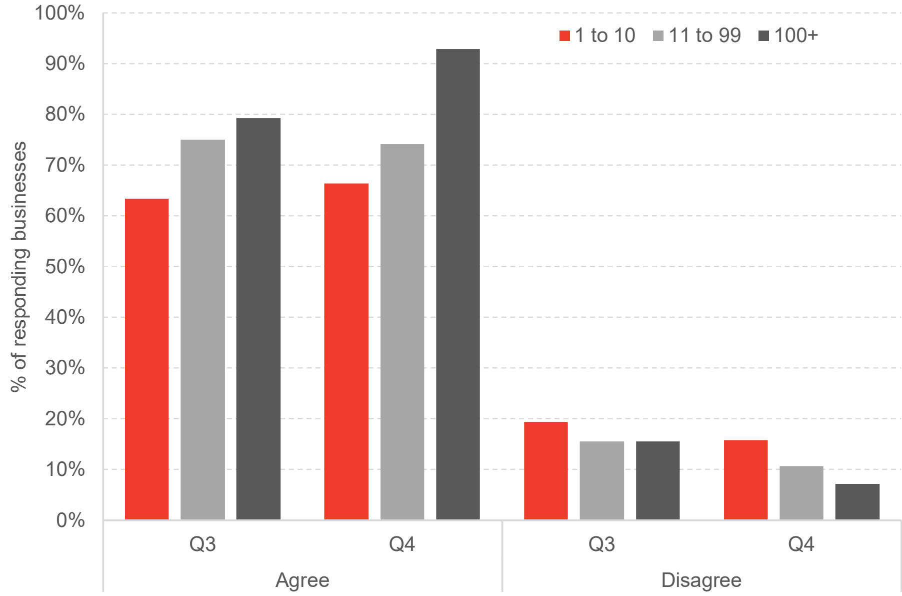
More than 1 in 2 businesses expressed that home working had increased in their organisation at the end of 2020.

This increase was the least prominent in small businesses, with just 66% agreeing that working from home had increased.

Large business saw the largest increases in home working. 93% of large businesses said that home working had increased, which represented a 13.5 p.p. increase on the previous quarter.

Only 10% of businesses said that homeworking had neither increased nor decreased at the end of 2020.

Chart 33: To what extent do you agree that staff home working in your organisation has increased? Q3 2020 - Q4 2020



***Source:** Scottish Business Monitor*

Implications and outlook for homeworking

As discussed, homeworking has pros and cons.

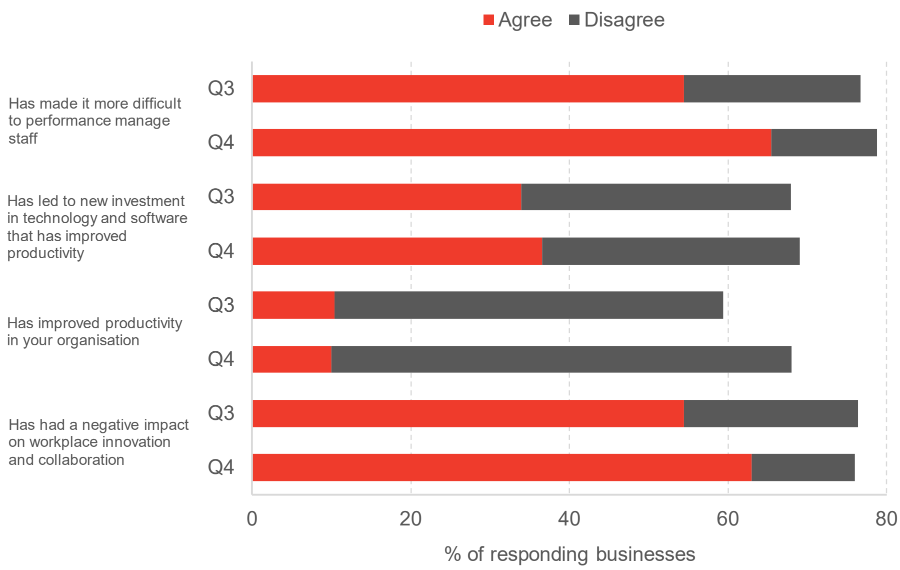
Whilst many argue that working from home has boosted productivity, some employers have argued that managing employee's performance has become more difficult.

Chart 34 highlights the feelings of businesses on a number of implications of homeworking.

Businesses feel that homeworking has made managing staff more difficult. They also feel that it has had a negative impact on innovation and collaboration in the workplace.

The majority of businesses also feel that productivity has not improved with homeworking.

Chart 34: To what extent do you agree that staff home working in your organisation has increased? Q3 2020 - Q4 2020



***Source:** Scottish Business Monitor*

Whilst the reviews on homeworking are mixed, the pandemic is far from over, meaning homeworking is here to stay in some capacity for the short-term.

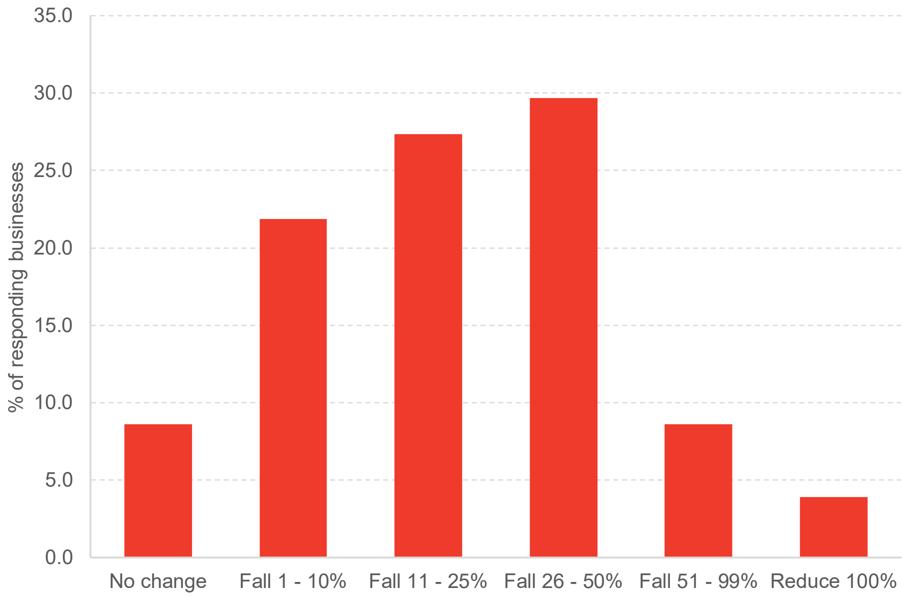
And whilst many employees look forward to a time with office parties and water-cooler chats, many are warming to the idea of never going back to an office environment.

This has sparked discussion around what this means for the future of cities, and those businesses that rely on office footfall.

In fact, only 9% of responding businesses thought their office footprint would not permanently reduce post pandemic.

With the average business expecting their office footfall to permanently reduce by 25-55%. Chart 35.

Chart 35: How much do you expect home working will permanently reduce your office footprint? Q4 2020



Source: *Scottish Business Monitor*

So, as we look forward to the future of working it appears as though a significant number of businesses will change the way they work when the economy opens back up. We may see a more flexible way of working with a blend between office and homeworking once this pandemic is over.

University of Strathclyde Business School

Fraser of Allander Institute
University of Strathclyde

The Fraser of Allander Institute (FAI) at the University of Strathclyde entered Scottish public life in 1975. Since then, it has become established as a leading independent economic research institute working with a wide range of clients on a variety of different topics.

What we do

For 45 years, the Fraser of Allander (FAI) has been monitoring and commentating on the Scottish economy. Our regular publications include:

- FAI Economic Commentary – Quarterly – First published in 1975, our quarterly Economic Commentary provides the authoritative independent assessment of economic conditions in Scotland, along with a wide range of economic and policy issues.
- Scottish Business Monitor – Quarterly – Since 1998, the FAI Scottish Business Monitor has been a key leading indicator of the Scottish economy. This survey of Scottish business sentiment provides vital insights into the Scottish economy well in advance of official statistics.
- Scotland's Budget Report – Annual – The Fraser of Allander Institute's analysis of the Scottish Budget and the choices, risks and opportunities facing the Finance Secretary.
- Our blog – Launched in 2016, and viewed over 200,000 times, our FAI blog is a keenly watched discussion platform on the Scottish economy. The blog publishes short reflections on economic developments as well as the policy debate.

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