SCOTTISH TRENDS

(Press Release - 23rd August 2017)

Analysis of latest Quarterly National Accounts for Scotland (QNAS) statistics for Quarter 1 of 2017 and of latest Government Expenditure and Revenues for Scotland (GERS) for 2016-17.

GDP Q1 2017

The following analysis looks at data relating to the Scottish economy's performance in **cash terms** and **including North Sea activity** (in contrast to the Scottish Government's quarterly GDP publication, which is in real terms and looks only at onshore activity).

Key points

- Latest data reveals **growth of 0.8% in Scottish GDP in the first quarter (Q1) of 2017.** This is in part due to the North Sea contributing to growth over the past year rather than significantly undermining it, as happened in the previous four years. However, Scottish GDP is only 1.5% its previous peak level, set in the 2nd Quarter of 2014, whereas the UK figure is now over 9% higher.

- **Scottish GDP per capita** (£7,485) in Q1 is only just above its peak level of 2 years ago and is slightly below the UK level (£7,538).

- The onshore **Trade deficit** has improved a little in Q1 but it is difficult to discern much in the way of a positive Brexit/exchange rate depreciation impact on recent Scottish Trade figures.

- The **Savings Ratio** for Scotland has been significantly revised upwards in the latest release and now stands at 4.5%, still a historically low figure.

Table 1: Economic growth comparison: Scotland and the UK, % change, cash terms GDP

	% change on Q4 of 2016		% change on Q1 of 2016		% change on Q2 of 2014	
	Scotland	UK	Scotland	UK	Scotland	UK
GDP						
- onshore only	0.8	-	3.1	-	6.0	-
- inc North Sea	0.8	0.7	3.2	4.4	1.5	9.3
- per capita (inc North Sea)	0.8	0.5	2.9	3.6	0.7	7.1

Sources: Scottish Government QNAS release (August 2017), ONS National Accounts

GERS 2016-17

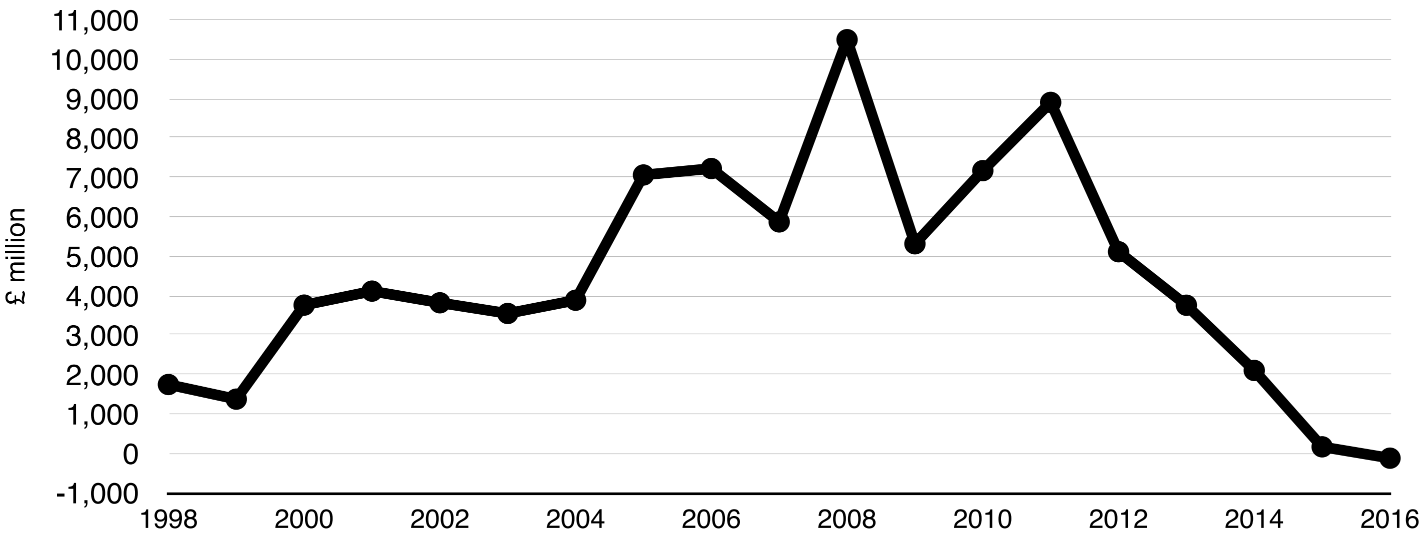
Key points

- Latest data reveals a Scottish overall (i.e. including the North Sea) fiscal deficit of £13.3 billion in 2016-17, equivalent to 8.3% of GDP and to £2,453 per person. The is slightly lower than the equivalent figure for 2015-16 (9.3%) but has barely changed (in % of GDP terms) from 2010-11 (8.2%).
- The UK fiscal deficit is £46 billion, equivalent to 2.4% of GDP and to £704 per person. The UK figure has been steadily falling, in both cash terms and as a % of GDP, in recent years.
- The key differential in the Scottish vs UK patterns is the demise of North Sea Oil Revenues (NSOR) from near £8 billion in 2011-12 to effectively zero in 2015-16 and now also in 2016-17.
- Income Tax (IT) is the biggest source of revenue, but Scotland's share of overall UK IT revenues continues to fall well short of its population share (7.3% to 8.2%).
- Future years (post 2016-17) are likely to show: (i) a slow improvement in Scotland's fiscal balance, in line with the UK's budget rebalancing; (ii) little change in Scotland's position relative to the UK, as the main element of variability (NSOR) has virtually disappeared and is not expected to return to any significant degree (see below).

North Sea contribution to Scottish Economy and Finances

- North Sea oil related tax revenues were trivial (£208 million). The rapid decline in recent years is highlighted in Chart 2. The recent decline contrasts with an 8 year period (2005-2012) of relative stability, when Scottish offshore oil revenues averaged around £7 billion a year and never fell below £5 billion in any single year, even though output was steadily declining.
- Unlike in earlier years, the chances of a revival in oil revenues are slim. While production levels have grown of late, North Sea output remains only a third of the level seen in 1999 and the recent upturn is expected to be short-lived. Meanwhile the oil price remains stuck in a range between $40-55 and the Scottish Government's latest projection (2015) estimates that, even if the oil price were to reach $100 a barrel again, the North Sea would contribute less than £3 billion a year of tax revenues for Scotland (up to 2019-20).
- The Scottish share of North Sea oil and gas revenues has been amended to be in line with the HMRC estimate, as opposed to previous editions of GERS where the share was based on analysis by Prof's Kemp & Stephen from the University of Aberdeen. The effect of this is to reduce the Scotland's share in most years.

Chart 2: Scottish North Sea Revenues (geographic share), £ million



Source: QNAS, August 2017

Going Forward

The annual publication of GERS may excite less interest now than in previous years but it remains highly relevant to any future discussion of a new fiscal arrangement, including independence. It acts as a starting point from which advocates of a different set-up need to build their case for a viable alternative.

This suggests that proponents of such an alternative arrangement would do best to publish an annual 'fiscal plan' update alongside GERS, showing what any adjustment phase would entail. This may be a big ask but then it is a big change that is being proposed.

At present, forecasts for future years are best done by extrapolating from GERS using the OBR's forecasts for the UK. Post the White Paper estimates made in 2013 (themselves providing only a partial pathway to a new arrangement) there is little information available on what any alternative path might look like. For example, the latest 'Oil and Gas Analytical Bulletin' from the Scottish Government was published over 2 years ago (June 2015).

Much has happened since 2013 (or even 2015) so that a new explanation for how a sustainable fiscal position might be reached is badly needed.

Adjusted Irish economics statistics in relation to Scottish economic data

One further point of interest in relation to both Scottish GDP and GERS data is the recent publication of a new measure ('modified GNI') for calculating Irish economic activity.

(Note: Gross Domestic Product (GDP) refers to what is produced in a country, while Gross National Income (GNI) refers to the net income accruing to the permanent residents of a country, i.e. it includes flows in and out relating to overseas ownership of activity, property etc. 'Modified GNI' further adjusts for the income of global firms redomiciling their headquarters to Ireland and the impact of mobile international assets in relation to depreciation on some R&D and aircraft leasing activities.)

Ireland already publishes data for GDP and GNI, but, despite this, still came up with clearly warped growth figures for 2015. The Irish government has now introduced 'modified GNI' to try and resolve some of these issues and to gain a better understanding of the underlying position of the economy.

This modified GNI measure is also used to better evaluate Irelands debt ratio and its debt sustainability as well as adjusting its Balance of Payments data.

Using the modified GNI measure methodology:
- the value of the Irish economy in 2016 fell from €275 billion (GDP) to €190 billion, down by almost a third;
- the (cash terms) growth rate fell from 25-35% in 2015 to 10%;
- the Irish headline debt level went from 73% of GDP to 106% of modified GNI;
- in addition, the Irish Current Account went from being a surplus to a deficit.

Scotland's position may not be as extreme as that of Ireland but significant, and currently unquantified, complications are likely to arise from the overseas ownership imbalances that exist and so additional, complementary, measures should be developed, starting with GNI.

Quotes:

"The recent upturn in the North Sea's fortunes continues to help the Scottish economy grow in cash terms.

However, the effective demise of North Sea revenues in recent years means that the latest edition of GERS highlights again the underlying difference between the Scottish and UK's fiscal balances. Scotland's is notably worse, by an amount roughly equivalent to £1,750 per person."

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