

Q1

FSB VOICE OF SMALL BUSINESS INDEX

QUARTER 1, 2020

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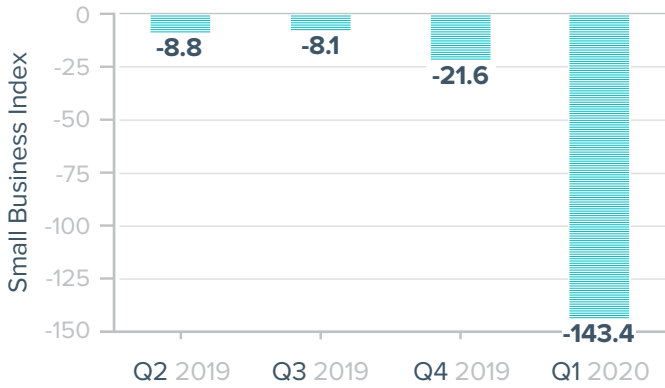
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Experts in Business

SBI Q1 2020

“**Coronavirus lockdown** takes its toll on the small business community”

Confidence crashes to all-time low



Firms plan closures amid coronavirus turmoil



9% intend to **sell, close** or **hand on** their business

Exports at all-time low

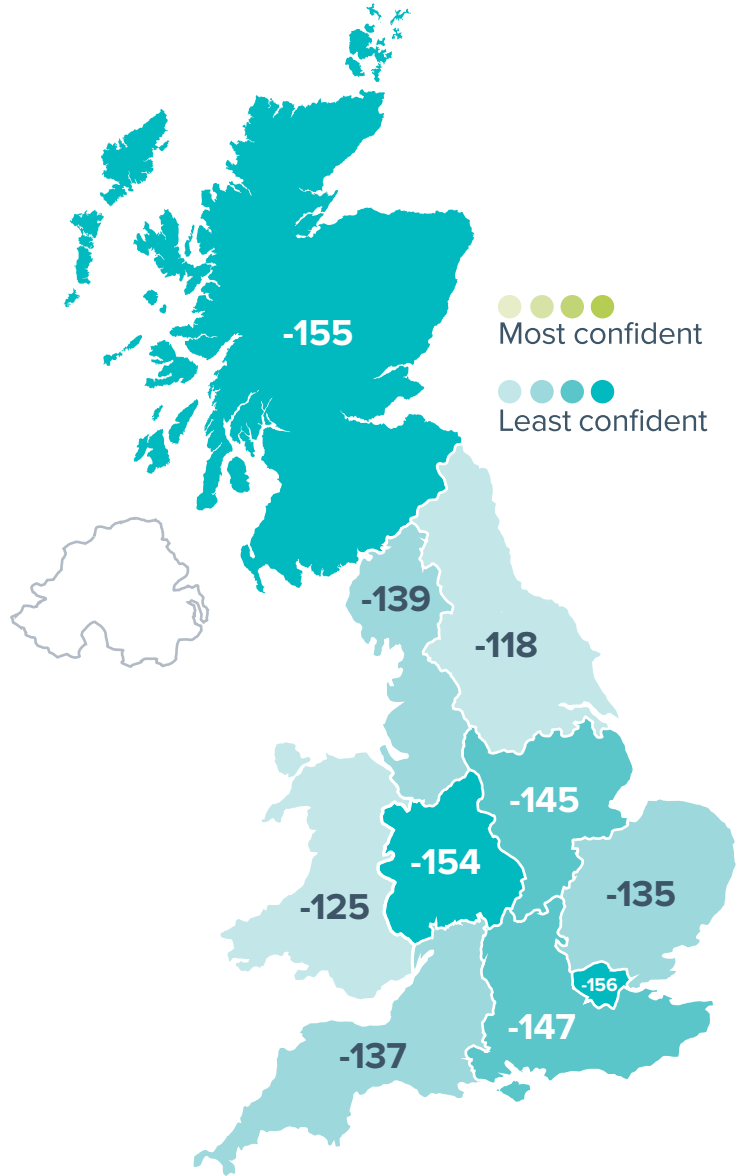


40% say **international sales** are **down** this quarter

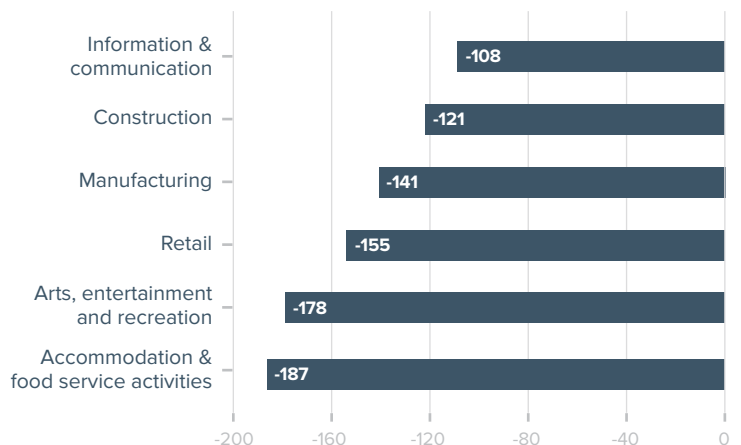
Employers plan to reduce headcounts



31% intend to **lower staff numbers** over next three months



Small business confidence by sector



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FSB FOREWORD

Small business confidence across the UK has collapsed in the face of unprecedented challenges created by the coronavirus crisis. FSB has engaged with government at the highest level to create support for UK small businesses that is as generous as possible, available to as many as possible, and deliverable as soon as possible. The UK Government has responded in kind with a fiscal reform package of enormity.

The Job Retention Scheme and the Self-employment Income Support Scheme will be, for many, the difference between surviving or folding. We welcome the extension of the Job Retention Scheme until the end of June. And as focus turns to recovery, it is important that the rules of the Job Retention Scheme are adjusted to ensure small businesses can stagger the return of furloughed employees given the predicted low levels of economic activity during the next quarter.

In the here and now, there is still much to do to help small businesses survive the crisis. Emergency loans and grants both have an important role to play. It is widely recognised the Coronavirus Business Support Loan Scheme (CBILS) has not reached enough SMEs quickly enough. And whilst we have welcomed government adjustments to the scheme, including the removal of personal guarantees for loans below £250K, the adoption of automated credit score processes for loans below £30K, and the removal of the requirement to first be offered a standard commercial product before a CBILS loan, there is clearly much more to do.

We want to see the Government guarantee on CBILS loans increase from 80% to 100%. In addition, we need much greater transparency regarding enquiries made about CBILS, particularly around what proportion of these are translating into applications, the application approval rate, and when funding is received by successful applicants.

Cash grants are the most effective mechanism through which to support small businesses at the current time. Therefore, cash grants of £10,000 for small businesses in receipt of small business rates relief/ small business bonus and rural rates relief are a lifeline. The same can be said of the £25,000 grants for eligible small businesses in the leisure, hospitality and retail sectors.

Much of the value of these interventions depends on the speed at which funding is received. Whilst some local authorities have stepped up and delivered, others have not. A razor-like focus on delivery is essential. Many small businesses across the whole of the UK, especially those on or adjacent to the high street, were struggling with business rates well before the coronavirus crisis. A one-year business rates holiday for businesses in the retail, leisure and hospitality sector (and in England – nurseries, estate agents and letting agents) is welcome. However, as forecasts about expected economic activity over the next quarter come in, the Government may need to look at this extending this holiday to a broader range of sectors.

Inevitably, in any wide scale programme of emergency fiscal intervention, there will always be gaps. In these instances, it is important that government looks creatively at how it can flex the rules of existing interventions to better support parts of the small business and self-employed constituency which are not directly helped by major interventions, and which may be ineligible for Universal Credit. This includes those who do not have premises and are ineligible for the Self-employment Income Support Scheme.

Small businesses will be at the forefront of recovery. Resilience and agility run through the DNA of the UK small business community. We have seen case after case of small businesses adapting their models to produce PPE, shift to online sales, and offer deliveries to customers, including the most vulnerable – providing free services and goods to our courageous key workers. Small businesses will adapt. However, just as the crisis has been unprecedented – so will be the size of the challenge faced by smaller businesses and the self-employed during recovery. Continued government support will be essential to ensure that those small businesses saved during the crisis can also survive, and ultimately thrive, during the recovery and, by doing so, help the UK economy to bounce back.



Mike Cherry,
National Chairman



Martin McTague,
Chairman,
Policy and Advocacy

ECONOMIST'S VIEW

The decline in this quarter's FSB Small Business Index (SBI) is so stark that it prompted those of us involved in compiling the Index to wonder if we had made a calculation error somewhere. Unfortunately, there was no error. Business confidence among small firms plummeted to -143.4 in Q1 2020 – the lowest level on record by a considerable margin. The previous record low was observed in Q4 2011 at -24.5.

The coronavirus pandemic is causing economic disruptions at a scale not seen in modern history. The government's unprecedented response to slow the spread of the virus also meant that the disruptions came about at an unbelievable speed. Businesses are now operating in an entirely different environment than a couple of months or even a couple of weeks ago. Of course, some of them aren't operating at all.

While confidence is low across all sectors, the picture is especially bleak for industries that rely on clients being able to participate in face-to-face interactions. The least confident sectors were wholesale & retail trade (-155.1), arts, entertainment & recreation (-178.5) and accommodation & food services (-186.9). The pessimism was slightly less pronounced among businesses in the information and communication sector (-108.4). Presumably this is because many in the sector are able to work effectively from home. The same is true for businesses in the professional services sector, which experienced higher than average confidence this quarter.

Looking at the regional picture, London was the least confident part of the UK, following a fall of 120.0 points to 156.4. Still the picture was downbeat across the country with even the most optimistic regions dipping deep into negative territory. Yorkshire and the North East and Wales were the two most confident regions, with scores of 119.7 and -125.4 respectively.

Cebr expects the UK economy to contract 4% over 2020 as government measures continue to partially or entirely prevent businesses from operating. This assumes that the current restrictions remain in place until late May and are gradually eased thereafter, leading to an economic recovery in the second half of the year. Some businesses will weather the coming months successfully and then see a surge in activity as pent up demand is released. However, for many, the repercussions will be long lasting. There are also those that won't make it through this crisis. Judging by the pessimistic views expressed by small firms in this report, many worry that they may be in one of the latter two categories.



Nina Skero,
Director and Head
of Macroeconomics,
Cebr

Q1

FSB EXECUTIVE SUMMARY

Key findings this quarter:

- **In Q1 2020 small business confidence collapsed to -143.4, its lowest ever level.** The quarterly fall of 121.8 points is the largest ever recorded by the FSB Small Business Index.
- **The level of confidence among small businesses fell in every one of the UK's constituent regions and countries for the second consecutive quarter.** The West Midlands saw the largest quarterly fall in confidence, with a decline of 138.4 points, while London (-156.4) was the least confident region of the UK.
- **The coronavirus outbreak was responsible for 87.7% of small businesses suffering a reduction in confidence in the first quarter of 2020.** Two thirds of businesses reported a significant reduction in confidence off the back of the spread of Covid-19, while only 4.2% saw their confidence improve.
- **Consumer-focussed industries saw confidence shattered in Q1 2020.** The worst-affected industries this quarter are arts, entertainment & recreation (-178.5) and accommodation & food services (-186.9), where enforced business closures and social distancing will hold back revenues for the foreseeable future.
- **Small businesses are reducing headcounts at the fastest rate since Q1 2012.** The proportion of small businesses reporting that their workforce has decreased in size rose by 2.9 percentage points to 15.4%.
- **More than four-fifths of small businesses expect revenues to fall over the next three months.** More than half (53.9%) of small businesses reported a decrease in revenues over the first quarter of 2020 with 84.1% of firms expecting sales to fall further in the coming quarter.
- **Over a quarter of small businesses expect to downsize their business in the next year.** The collapse in business confidence across the UK means 27.9% of business owners are now considering scaling back, closing, or handing on their business in the coming year – up from 11.5% in Q4 2019.

UK MACROECONOMIC OVERVIEW

Flatlining UK economy set to contract sharply in the face of the coronavirus outbreak

After a volatile 2019, during which Brexit negotiations and the US-China trade conflict dominated the economic and political news-cycle, sentiment among businesses started to improve in the early part of 2020. However, the arrival in the UK of the new coronavirus, which was first detected in China's Hubei province in December 2019, has now completely reversed this trend. With the Government's response escalating rapidly as cases of the virus multiplied, by mid-March the country faced the most drastic limitations on free movement ever seen during peacetime. In just two short months, the positivity growing among UK businesses as Brexit clarity finally began to emerge had completely evaporated in the face of collapsing demand and forced businesses closures.

But even at the start of the year the UK economy was by no means in perfect health. The economy recorded no growth in the three months to January 2020 compared to the previous three-month period. Growth of 1.4% in the construction sector was offset by a 1.2% decline in manufacturing. Meanwhile, the service sector flatlined and some of the strongest performing industries of recent years, such as information and communication and professional services, saw output falling according to the most recent data. Despite the stagnant economic performance towards the end of 2019, leading indicators had started to indicate the green shoots of recovery in early 2020.

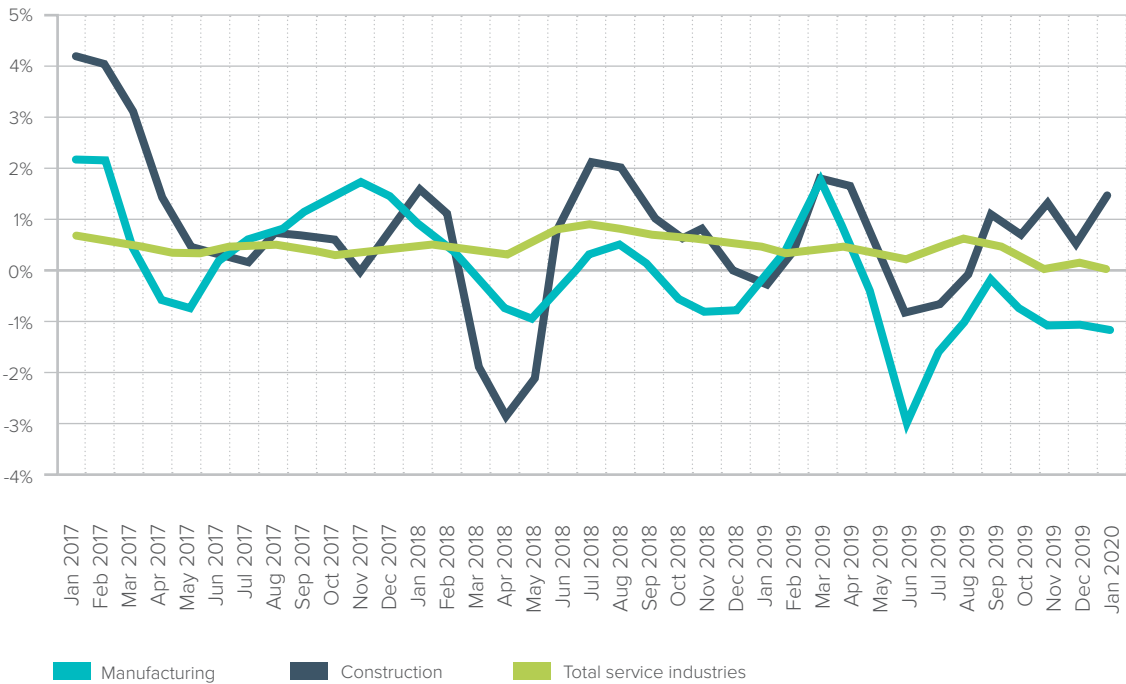
Once the General Election result had installed a majority Government, with the mandate to make genuine progress in Parliament on Brexit and other economic issues, business surveys began to indicate plans to increase production, reversing a long-run downward trend among manufacturers in particular. In a similar vein, the Cebr / YouGov consumer confidence index rose by 2.8 points to 107.6 in January 2020, and mortgage approvals climbed to their highest level in more than six years in February.

The increase in consumer confidence stood on the foundations of a record-breaking labour market. The employment rate reached its highest ever level in the three-months to January 2020, standing at 76.5%, the joint-highest estimate on record. This went hand in hand with an unemployment rate of just 3.8%, far below its long run average, and a record-low economic inactivity rate of 20.4%. Despite coming off their peak of 4.0% annual growth in June 2019, average weekly earnings continued to grow, recording an annual rise of 3.1% over the three-months to January.

But the coronavirus outbreak, and government interventions aimed at slowing the rate of infection, have immediately turned the tide on all of these cautiously positive trends. The initial advice to avoid socialising left many retail, leisure and hospitality businesses facing a demand shortage. As the guidance rapidly escalated from social distancing to total lockdown, the shortage of demand soon turned into enforced business closures and the loss of swathes of employees to self-isolation. The interaction between the loss of demand and restrictions on supply have had a devastating impact on the economy.

Despite the implementation of an unprecedented set of fiscal and monetary measures coordinated between the Treasury and the Bank of England, the number of new claims for Universal Credit hit 950,000 over the final two weeks of March. This suggests the unemployment rate is likely to have shot above 6% and, with many more staff temporarily furloughed, a massive fall in economic output is all but guaranteed until the lockdown conditions are relaxed. While the majority of businesses face a collapse in revenue that, for many, may be severe enough to threaten their survival, meeting the requirements of a wave of new home workers in the era of social distancing has thrown up opportunities and new ways of doing things.

Figure one: Monthly growth rates by sector of the UK economy, latest three months on previous three months
Source: Office for National Statistics.



SMALL BUSINESS INDEX

SBI crashes as coronavirus forces temporary business closures

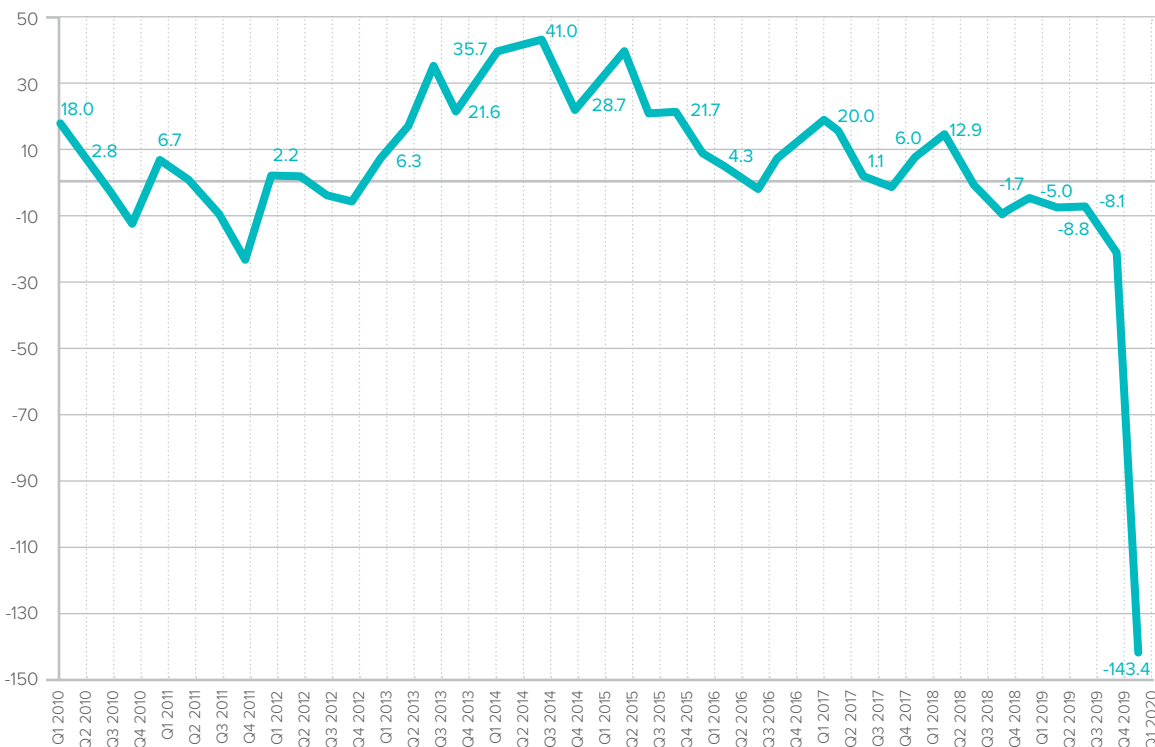
Business confidence among small firms plummeted to -143.4 in Q1 2020. This is the lowest level on record by a considerable distance, marking a quarterly fall of 121.8 points from the -21.6 recorded in Q4 2019. The coronavirus outbreak is a public health emergency of a scale not seen in the UK for a century, leading to an unprecedented government response to slow the spread of the virus. The enforced closure of businesses deemed non-essential, including pubs, restaurants and bars, has reduced economic activity on a massive scale.

Most survey data have indicated a negative outlook for UK businesses. The UK Purchasing Managers' Index (PMI) for the manufacturing sector fell by 3.9 points to 47.8 – any figure below 50 represents a contraction. The survey suggests that output in the sector has fallen faster than at any time since July 2012, and with the collection of results running from 12-26 March, as the Government's response escalated

rapidly, it is likely to underestimate the true impact. Comparable numbers from China released after the shutdown of Hubei province saw manufacturing PMIs fall to record lows as efforts to contain the virus took effect.

The official GDP growth data suggest the economy was growing slowly at the end of last year. In the final quarter of 2019, the economy was just 1.1% larger than in the same quarter of 2018. This coincided with an already poor showing on the FSB Voice of Small Business Index, which stood at -21.6. The latest plunge in the confidence of small businesses in the UK leave the score 119.0 points below its previous low of -24.5 recorded in Q4 2011. This suggests the economy is set for a sharp contraction over the coming months.

Figure two: The FSB Small Business Index¹: small business prospects over coming three months
Source: FSB - Verve 'Voice of Small Business' Panel Survey.



1. The Small Business Index is a weighted index of the responses to the question: 'Considering your overall business performance, and ignoring any normal seasonal variations at this time of the year, how do you view business prospects over the next three months, compared with the previous three months?' The share of firms reporting 'much improved' are given the following weightings: +2, slightly improved +1, approximately the same 0, slightly worse -1 and much worse -2; the Small Business Index is derived from the sum of these factors.

Figure three: Year-on-year change in the FSB Small Business Index.
Source: FSB - Verve 'Voice of Small Business' Panel Survey.

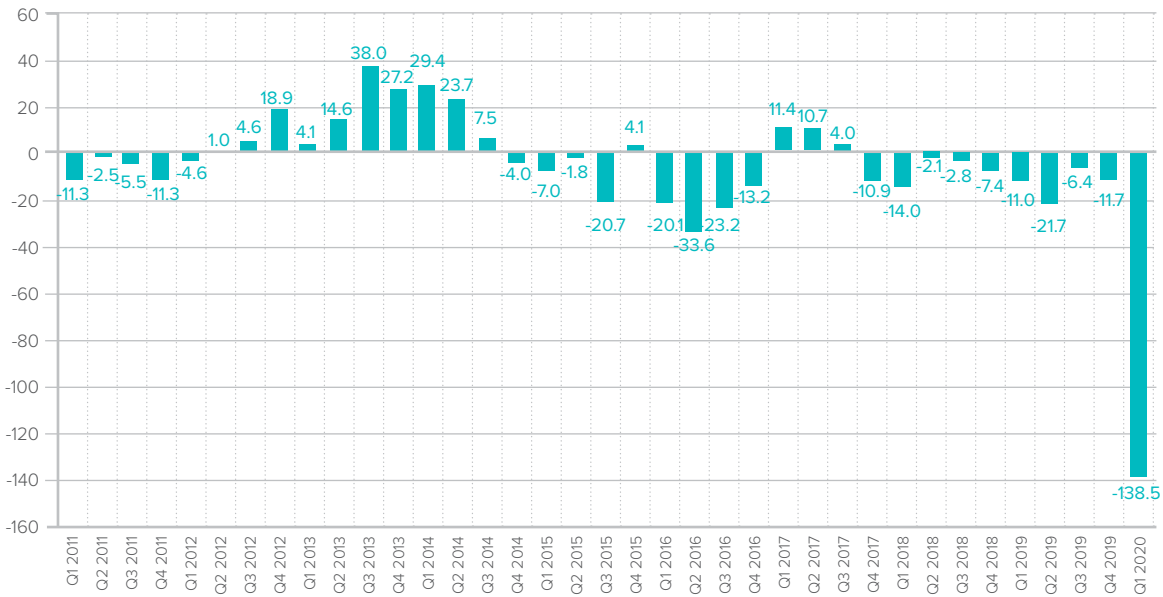
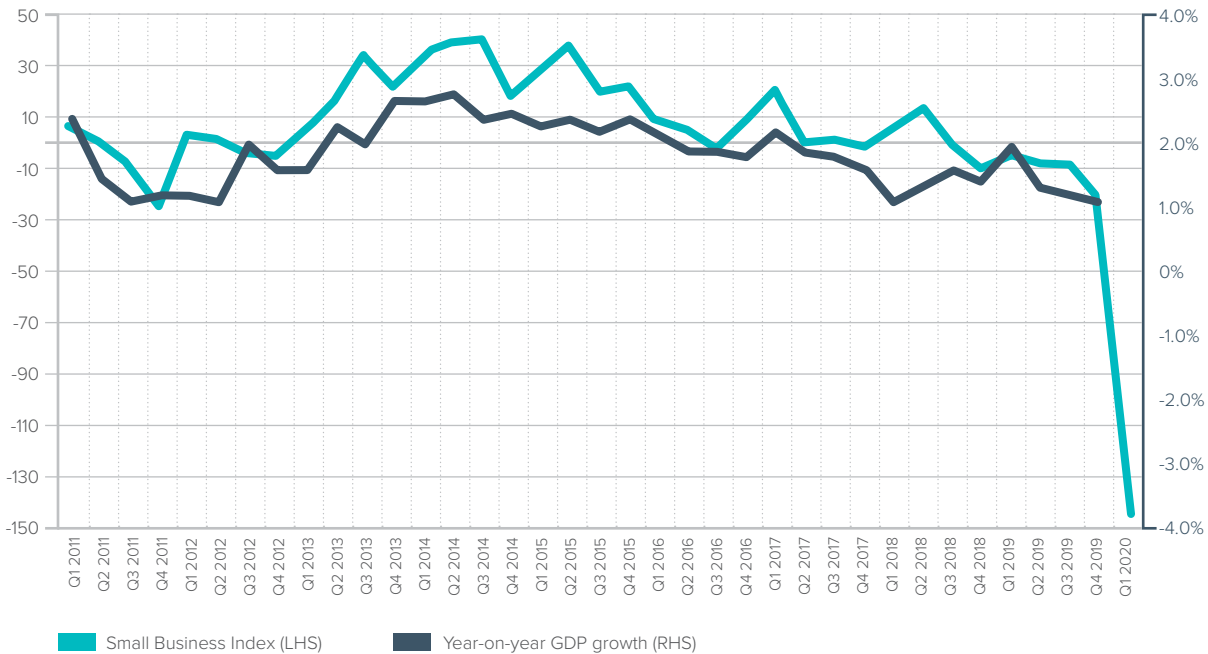


Figure four: UK SBI against year-on-year UK GDP growth.
Source: ONS, FSB - Verve 'Voice of Small Business' Panel Survey.



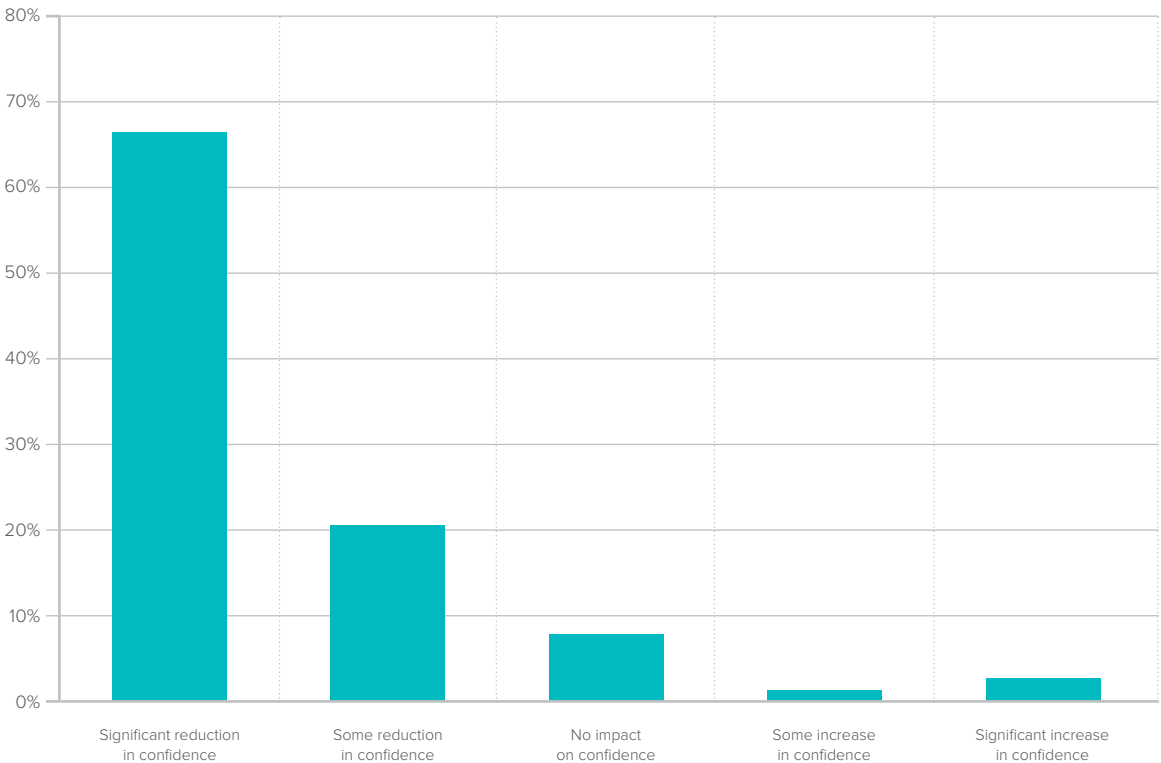
Two thirds of small businesses see a significant reduction in confidence as a result of coronavirus outbreak

The vast majority of small businesses have seen a reduction in confidence about their performance in the coming quarter specifically because of the coronavirus outbreak. Just over two-thirds (66.9%) of small businesses recorded a significant reduction in confidence as a consequence of the virus, with a further 20.7% experiencing a less severe hit to confidence. By contrast, only 4.2% recorded an improvement in confidence.

Among small businesses in the accommodation and food services industry, the share of firms recording a decrease in confidence was 95.0%, as practically all

of these businesses have been forced to close their doors to help combat the spread of the virus. Online and food delivery businesses have seen an increase in demand for their services due to the coronavirus, as more people work from home, avoid shopping trips and no longer have the option of eating out. This probably explains why a small proportion (1.2%) of businesses in the sector report a significant increase in confidence. Construction firms were more optimistic than average, with 6.2% recording an increase in confidence due to the impact of the coronavirus.

Figure five: Impact of coronavirus on small business confidence – proportion of respondents
Source: FSB - Verve 'Voice of Small Business' Panel Survey.



REGIONAL SMALL BUSINESS INDICES

A sea of red

COLLAPSING SMALL BUSINESS CONFIDENCE HITS ALL REGIONS AND COUNTRIES

Every one of the UK's constituent regions and countries recorded a huge collapse in small business confidence between Q4 2019 and Q1 2020. The West Midlands saw the largest quarterly fall in confidence, with a decline of 138.4 points, leaving the small business index for the region standing at -154.0. Meanwhile, London continued to be the least confident region of the UK following a fall of 120.0 points to -156.4 in the first quarter of 2020.

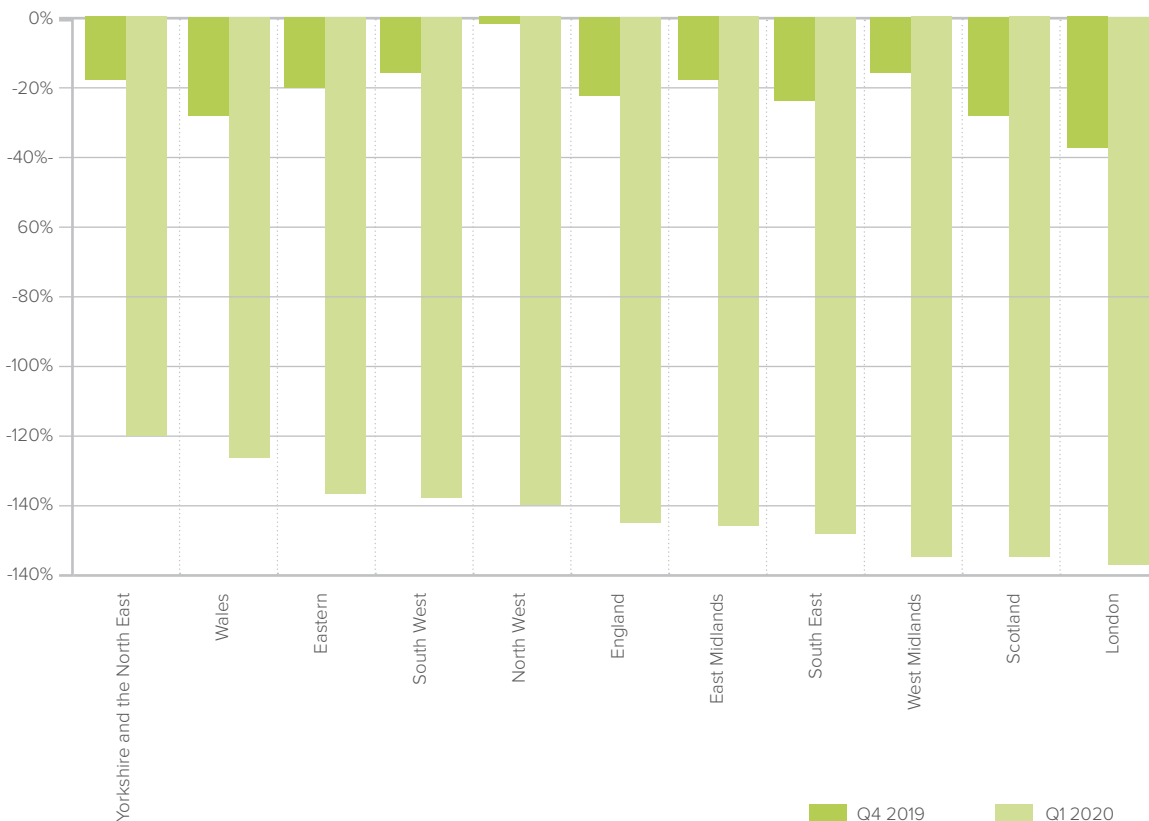
Even the most confident regions experienced unprecedented quarterly declines. Yorkshire and the North East and Wales were the two most confident regions, with scores of -119.7 and 125.4 respectively this quarter. Wales also experienced the smallest fall in confidence between Q4 2019 and Q1 2020, albeit the fall of 98.3 points would have still been the largest regional decrease ever recorded in any previous quarter.

After several years of Brexit, related volatility and Parliamentary deadlock, the general election in

December delivered an energised government with a clear mandate to enact Brexit. The subsequent passing of the Withdrawal Bill into law also avoided an immediate no deal exit through the implementation of a transition period. It also raised the prospects of a more coherent policy agenda, including ambitious plans for infrastructure investment and regional rebalancing. However, this momentum was soon eroded by the spread of the coronavirus outbreak. The impact ranged from disrupted supply chains in February, while Chinese factories were closed, to travel chaos as airlines closed routes, to total economic lockdown within two months. While the nature of the pandemic means businesses and regions that are most dependent on international trade would have been the first to be affected, the implications of a nationwide lock-down means small businesses in every region face a major economic squeeze in the months ahead.

Figure six: FSB Small Business Index – regional variation in small business prospects over coming three months

Source: FSB - Verve 'Voice of Small Business' Panel Survey.



SMALL BUSINESS SECTOR INDICES

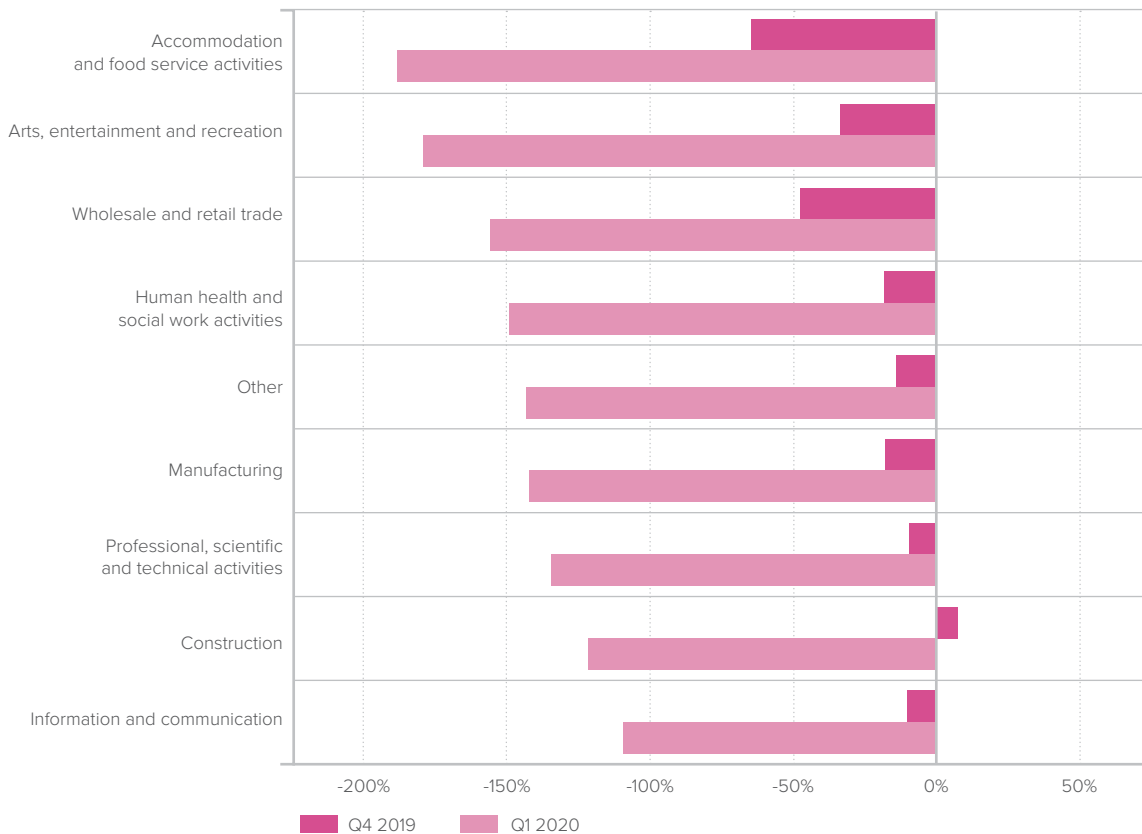
Closures take their toll

CONSUMER-FACING INDUSTRIES FACE NEAR TOTAL LOSS OF CONFIDENCE

Every sector of the economy saw confidence tumble in the first quarter of 2020. The extent of the economic shutdown aimed at slowing the spread of the coronavirus is so wide-ranging that no sector has escaped unscathed. The loss of confidence was slightly less severe among businesses in the Information and Communication sector where a fall of 98.2 points left the sector’s small business index standing at -108.4 in the first quarter of 2020. Many employees in information and communication businesses will have found it relatively easy to transition to working from home as the economic lockdown took effect. Similarly, businesses in the professional services sector that are also likely to maintain operations from home saw higher than average confidence this quarter, after falling by 124.2 points to -133.8.

The least confident sectors were wholesale & retail trade (-155.1), arts, entertainment & recreation (-178.5) and accommodation & food services (-186.9). These industries are typically dependent on face-to-face interaction which, with the exception of food retailing, run completely against government guidelines on social distancing. This will have reduced demand even ahead of the enforced closure of these types of business. With events cancelled and tourist attractions, pubs and restaurants all closed for the foreseeable future, revenues across these sectors are destined to fall. The bad news compounded a largely negative outlook in these industries in Q4 2019, when wholesale & retail trade (-47.3) and accommodation & food services (-65.0) were already the two least confident sectors.

Figure seven: FSB Small Business Index by sector – small business prospects over coming three months. Source: FSB - Verve ‘Voice of Small Business’ Panel Survey.



FINANCIAL PERFORMANCE

Sales hit all-time low

VAST MAJORITY OF SMALL BUSINESSES EXPECT REVENUES TO FALL

The net balance of small businesses reporting growth in revenues fell to -26.1% in the first quarter of 2020. Across the UK, more than half (53.9%) of small businesses reported a decrease in revenues over the quarter compared to just 27.8% reporting an increase. This was a decline in the net balance of 29.2% from the last time this question was asked in Q3 2019, bringing the net balance to its lowest ever level, and to below zero for the first time since Q2 2013.

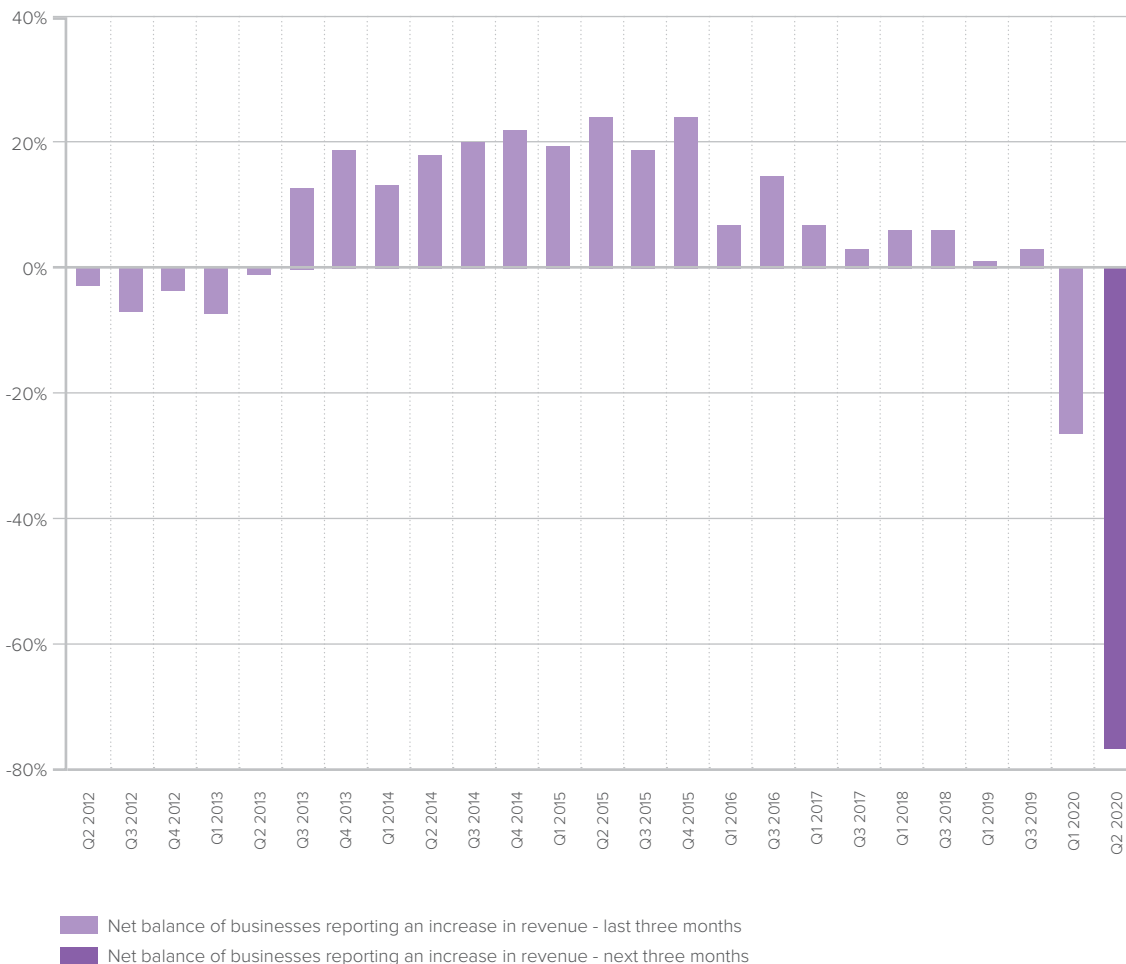
The net balance was lowest in the East of England (-36.7%), where a third (33.3%) of small businesses reported a significant fall in their revenues during the last quarter. Indeed, every region and nation in the UK reported a net balance of businesses experiencing falling revenues in Q1 2020. A net balance of -15.5% in the East Midlands was the

highest recorded in any region. Businesses in the accommodation & food services sector recorded the worst revenue performance of any sector in Q1 2020. Nearly four-fifths (78.3%) of businesses in the industry saw revenues fall, compared to just 8.5% in which revenues rose, resulting in a net balance of -69.8%.

The proportion of small businesses expecting their revenues to deteriorate over the next three months is 84.1%. This compares to just 7.8% of small businesses that expect to see an improvement in sales as the coronavirus outbreak grips the country. Notably the net balance for revenue expectations over the next three months is lowest in the East Midlands, suggesting the better than average performance in Q1 sales is indicative of a delayed coronavirus impact, rather than a greater level of underlying resilience.

Figure eight: Small business revenues, net percentage balance – proportion reporting/ expecting increase less proportion reporting/ expecting decrease.

Source: FSB - Verve 'Voice of Small Business' Panel Survey.



EXPORTS

International sales crash

EXPORT GROWTH HITS RECORD LOW

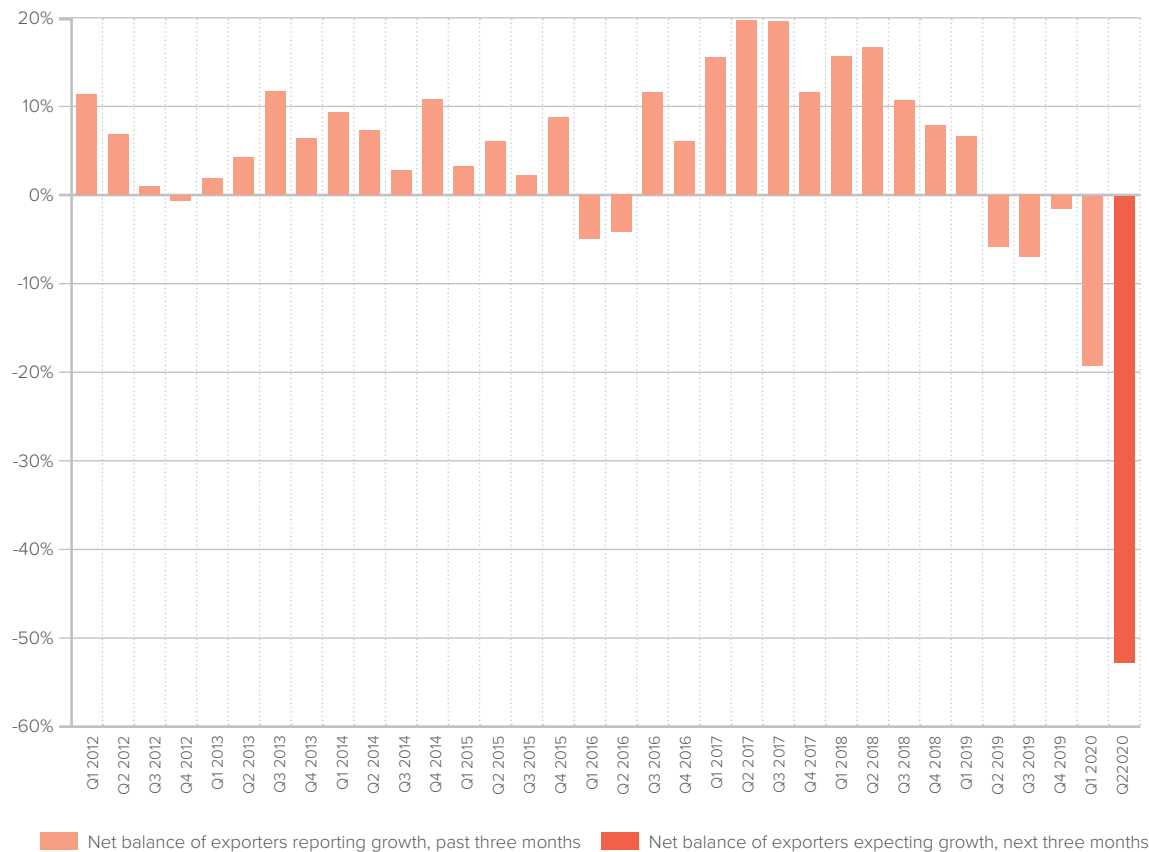
In the first quarter of 2020, the proportion of small businesses reporting a decrease in the value of their exports reached 40.4%, eight percentage points higher than in Q4 2019. Meanwhile, the proportion of businesses reporting an increase in export volumes fell by 9.6 percentage points to leave a net balance of -19.1%, an all-time low.

The latest official data show that, across the UK, the volume of exports (excluding erratic goods) fell by £4.2 billion in the three months to January 2020, a decline of 4.8% compared to the previous three-month period. This was accompanied by an even steeper decline of £9.5 billion in imports, causing the trade deficit to narrow by over £5.3 billion. This slowdown in total trade preceded the coronavirus outbreak and is likely indicative of a global phenomenon that was developing before said outbreak took hold. The US-China trade war had been driving trade volumes lower globally for some

time, while the risks associated with an unknown post-Brexit trade deal may have been driving some European firms to seek suppliers outside of the UK to maintain long-term stability.

At the end of January, the emergence of coronavirus in China led to a total shutdown of Hubei province, which quickly had knock-on effects on global supply chains that are still being felt. However, the spread of the outbreak to Europe will have far more serious implications for the ability of UK firms to trade in the months to come. As lockdowns and staff shortages create practical problems for trade, demand is also falling across major export markets due to the widespread closure of businesses. Consequently, the net balance of firms expecting an increase in exports in the next quarter fell by 42.9 percentage points to stand -52.5%. This was the second consecutive quarterly fall in the expectations indicator, which left the net balance standing at its lowest level on record.

Figure nine: Changes in value of exports – previous three months and expectations for coming three months; net percentage balance, proportion reporting increase less proportion reporting decrease.
Source: FSB - Verve 'Voice of Small Business' Panel Survey.



COSTS AND INFLATION

Drop in fuel prices brings
outgoings down

SMALL BUSINESS COST PRESSURES EASE

A net balance of 61.3% of small businesses reported an increase in operating costs during the past three months compared with the same period a year ago. Between Q3 and Q4 2019, the net balance rose by 1.5 percentage points, although it now stands 1.9 percentage points lower than in Q4 2018.

Labour costs continue to be the most frequently cited cause of rising costs for small businesses in the final quarter of 2019. The proportion of small businesses referring to labour as a source of cost pressure rose by 3.6 percentage points compared to Q3 2019, to stand at 43.5%. This is 0.8 percentage points higher than in Q4 2018. Rising wages, especially among some lower income workers, mean businesses in the accommodation & food services sector were

especially likely to be affected. While a net balance of 82.4% of businesses in the sector reported rising costs across all categories, two thirds (65.6%) of businesses reported labour costs as an issue in Q4. Notably, a high proportion of information and communication businesses (60.3%) also indicated that labour costs were rising, perhaps as strong growth in the industry has led to competition for skilled workers.

Compared to the final quarter of 2018, a much lower proportion of businesses have reported that fuel was driving costs higher. The net balance decreased by 11.4 percentage points compared to Q4 2018 as global oil prices have fed through to lower pump prices and fuel duty remained frozen at the last budget.

Figure 10: Small businesses reporting an increase in overall cost of operation over past three months, compared with the same period a year ago; net percentage balance.
Source: FSB - Verve 'Voice of Small Business' Panel Survey.

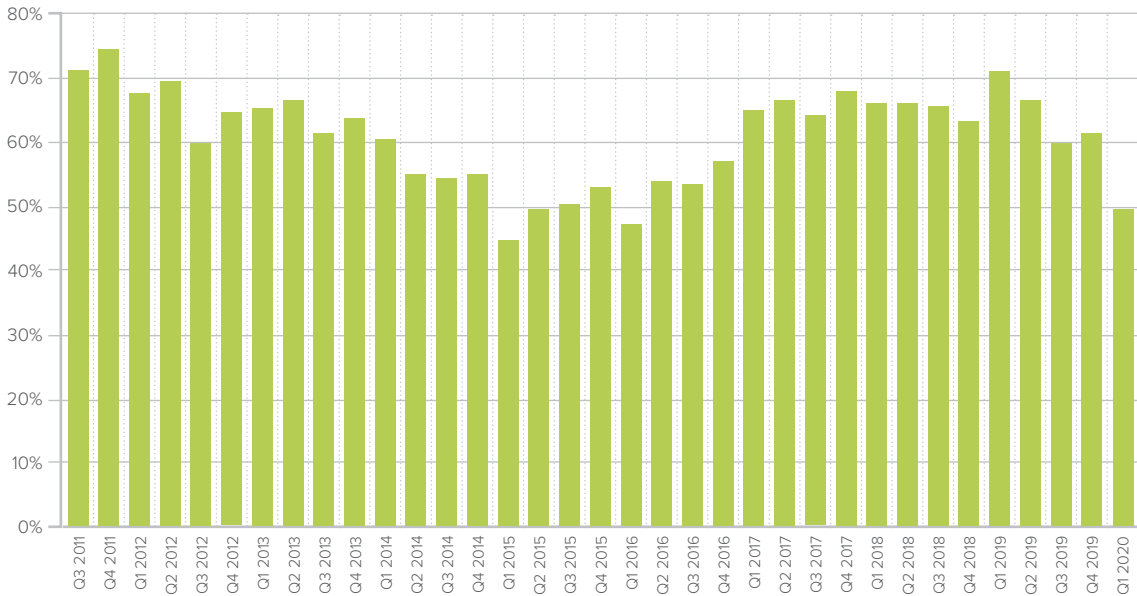
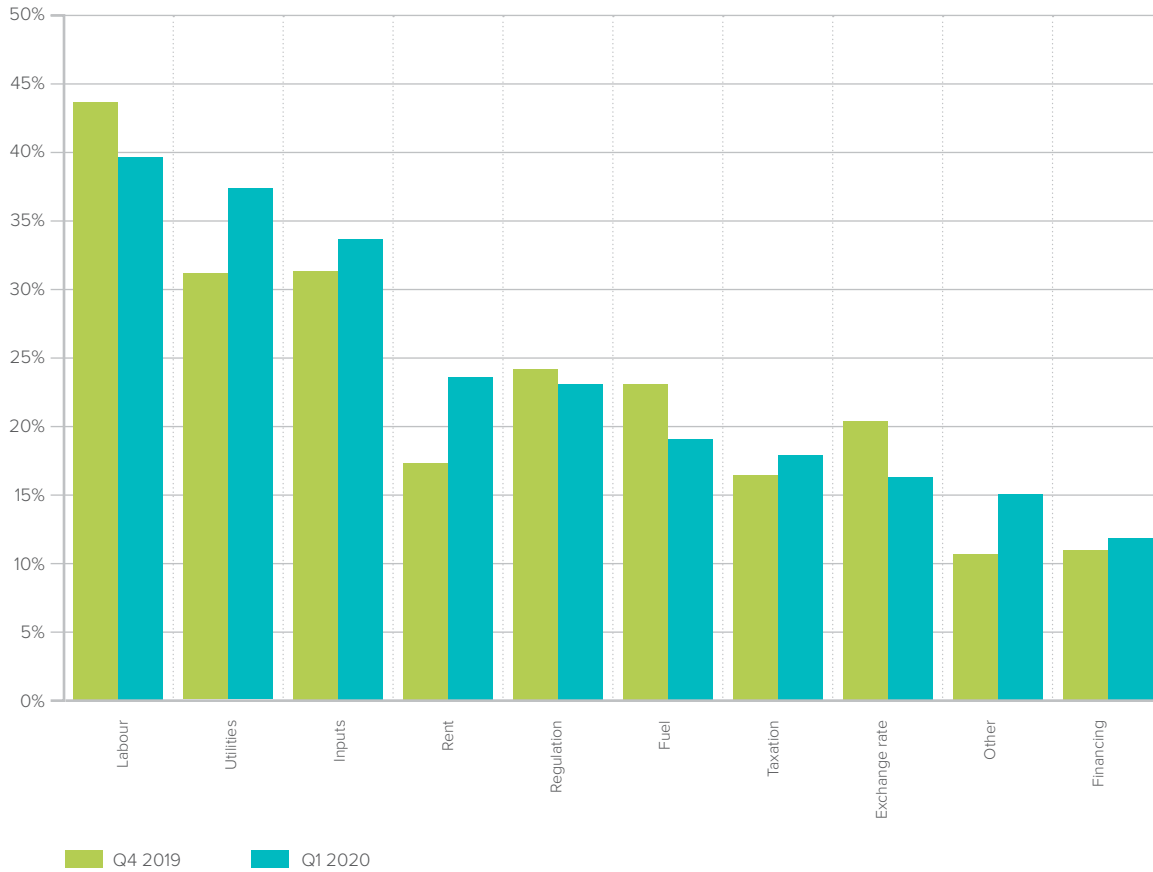


Figure 11: Main causes for changing business costs (firms may give multiple answers).
 Source: FSB - Verve 'Voice of Small Business' Panel Survey.



CAPACITY

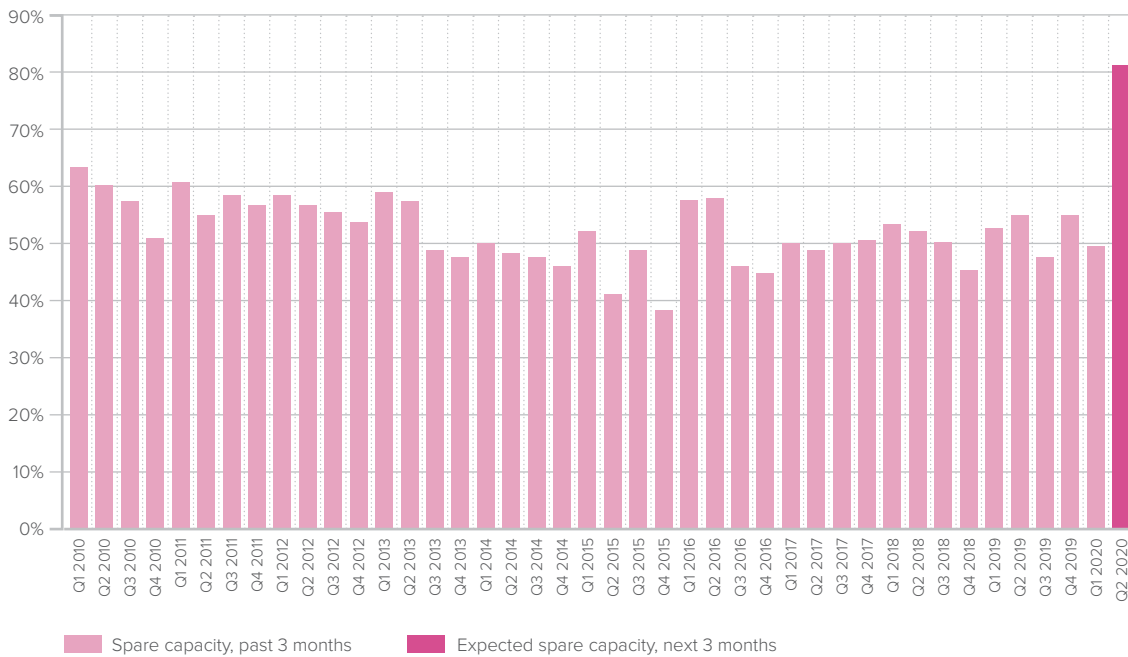
Fewer than half of firms firing
on all cylinders

EXPECTATIONS OF SPARE CAPACITY REACH RECORD HIGH

The proportion of small businesses reporting that they were operating below capacity fell from 63.2% in Q4 2019 to 57.5% in Q1 2020. With the proportion of businesses operating above capacity falling by a marginal amount to 8.3%, the excess capacity net balance fell by 5.1 percentage points over the quarter, a fall of 2.9 percentage points year-on-year. This defied the expectation held by businesses in Q4 2019 that spare capacity may rise slightly during the first three months of 2020 (expectations were for the net balance to reach 51.7%, its highest level since Q4 2012).

The outlook for the coming months is, however, far bleaker than the upturn in Q1 might suggest. The shutdown of the economy has forced businesses to close and change practices to ensure that social distancing takes place on a large scale. This has pushed the net balance of businesses that expect to operate with spare capacity in the next three months to 81.0% - its highest ever level. With so much spare capacity, many businesses may be driven to take up the Government's furlough scheme, whereby surplus workers are temporarily laid off to avoid redundancies while the spread of the coronavirus is brought under control.

Figure 12: Net percentage balance of businesses running below capacity: proportion below capacity less proportion above capacity.
Source: FSB - Verve 'Voice of Small Business' Panel Survey.



EMPLOYMENT

Staffing levels fall

SMALL BUSINESSES REDUCE EMPLOYMENT AT FASTEST RATE IN EIGHT YEARS

The proportion of small businesses reporting that their workforce has decreased in size rose by 2.9 percentage points to 15.4% in Q1. This measure was last higher eight years ago, when 17% of small businesses reduced their headcount over the first quarter of 2012. Meanwhile, the proportion of businesses increasing their employment level fell to just 7.8%, leaving a net balance of businesses increasing their employment of -7.5%. This is a quarterly decline of 6.0 percentage points. The situation is most severe in London where one in five businesses report reduced employment levels during the last three months.

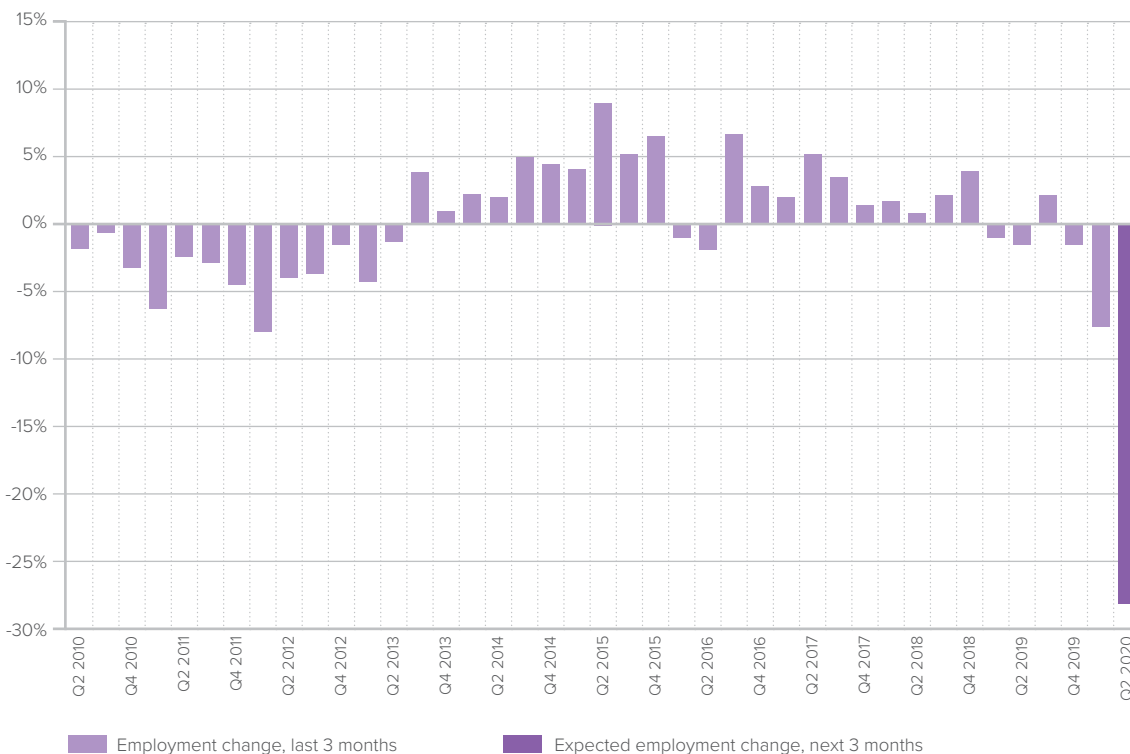
In times of economic stress, when lower demand is causing revenues to fall, businesses may often have to reduce their staffing to cut costs. Small businesses without large corporate debt facilities may be especially vulnerable to this type of pressure. Although signs were emerging that employment levels were starting to dip during 2019, the sharper decline in Q1 suggests that the reduction in demand

due to coronavirus has forced smaller businesses into lower staffing. The Government's job retention scheme, which allows businesses to temporarily lay off staff while extreme measures to slow the virus are in place, is likely to have contributed to a faster reduction in staff numbers as it allows businesses to cut their wage bill while maintaining headcounts and ensuring employee wellbeing.

In the three months to January 2020, the unemployment rate was well below its long-term average, standing at just 3.9%. Since the UK went into lockdown, many working in the worst-affected industries may have already been pushed into unemployment or financial distress, and the number of universal credit claims rose by 950,000 in the final two weeks of March. The worst may be still to come, however, as the net balance of businesses that expect to raise their employment levels in the coming three months fell by 31.5 percentage points compared to Q4 2019 and now stands at -28.0% - its lowest ever level.

Figure 13: Net percentage balance change in number of people employed – proportion reporting increase less proportion reporting decrease.

Source: FSB - Verve 'Voice of Small Business' Panel Survey.

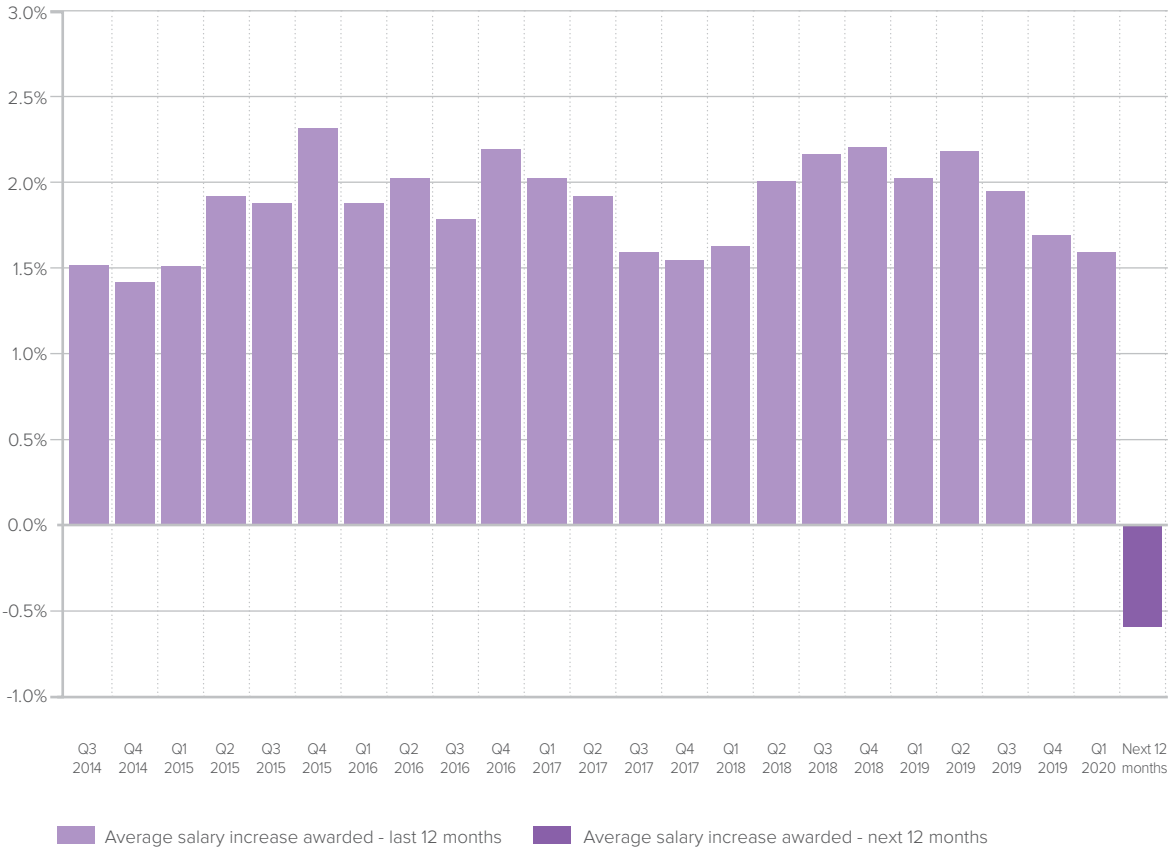


ONE IN FIVE SMALL BUSINESSES EXPECT TO CUT WAGE COSTS

In Q1 2020 the average annual rate of wage growth among small businesses fell by 0.1 percentage points to 1.6%. This was the third consecutive quarter in which the rate of pay growth slowed. Year-on-year, the rate of growth in average salaries was down by 0.4 percentage points from 2.0% in Q1 2019. This pattern fits with the national picture, where total average weekly earnings growth (which includes changes to the number of hours worked as well as changes in base pay) peaked in the three months to June 2019, at 4.0%. The latest data show this had slowed to just 3.1% in the three months to January 2020, as firms reined in their hiring and stopped competing for new staff so aggressively.

The slowing of the economy through 2019 meant the high cost of labour had been placing pressure on employers, with labour costs frequently seen as the biggest source of cost pressure. As coronavirus places a strain on revenues for most businesses, the ability to cut salaries in order to keep staff employed while protecting the viability of businesses is now seen as the only available course of action for many employers. Between Q4 2019 and Q1 2020, the proportion of businesses that expect to decrease average salaries has risen by 14.6 percentage points to 18.4%. With fewer than half of firms (42.5%) now expecting they will be in a position to raise salaries, the estimated average pay increase across small businesses for the next 12 months has fallen below zero for the first time, and now stands at -0.6%.

Figure 14: Average salary increase awarded, this quarter versus a year before.
Source: FSB - Verve 'Voice of Small Business' Panel Survey.



GROWTH ASPIRATIONS AND CHALLENGES

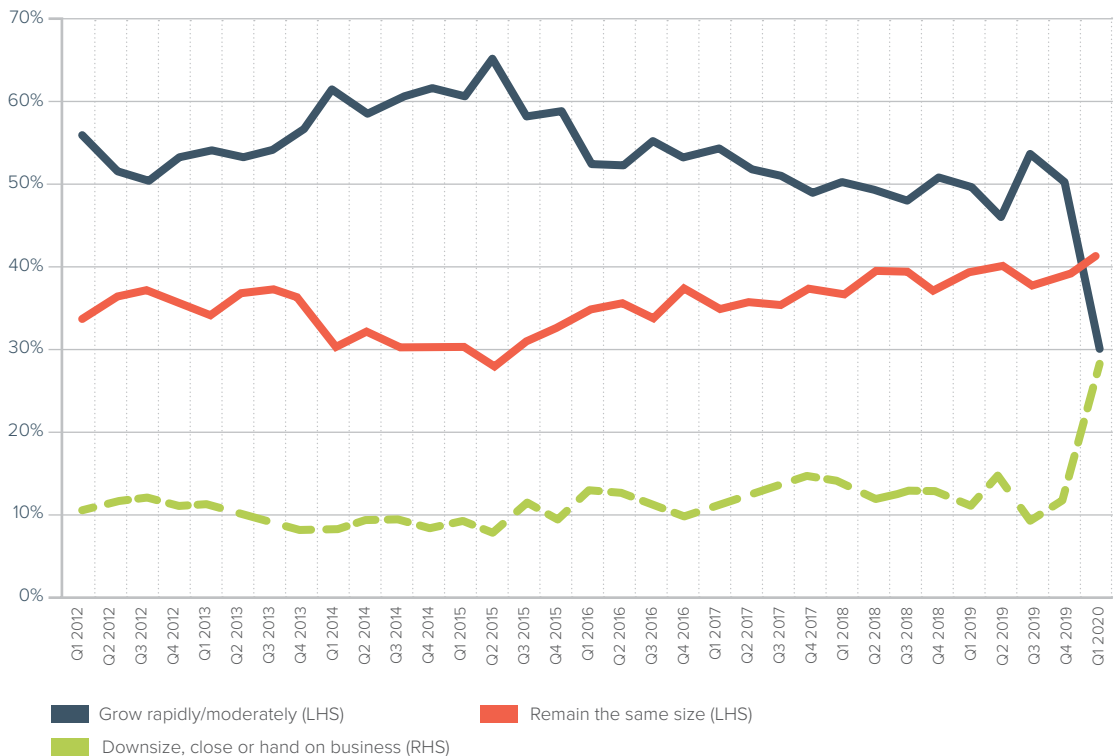
One in ten expect to
shut up shop

MORE THAN A QUARTER OF SMALL BUSINESSES PLANNING TO DOWNSIZE

The proportion of small businesses that aspire to grow over the course of the next 12 months fell for the second consecutive quarter in Q1 2020. While the decline was just 3.6 percentage points between Q3 and Q4 2019, the measure tumbled by a further 19.6 percentage points in the first quarter of 2020, and now stands at just 30.5%. More worryingly, the collapse in business confidence across the UK means a similar proportion of business owners (27.9%) are now considering scaling back, closing or handing on their business in the coming year. This is an increase of 16.4 percentage points compared to Q4 2019. While the economy faces severe restrictions in response to the coronavirus outbreak, many firms worry about the viability of their operations given the major demand shock and its impact on revenues.

Businesses in London (33.8%) are the most likely to consider scaling back over the coming year. By contrast only 20.6% of businesses in Yorkshire and the North East are expecting a contraction. Accommodation and food services businesses were also the most likely to report an intention to downsize. As one of the sectors that is most heavily affected by the closures required by the Government, it is unsurprising that many have scaled back their ambitions for the next 12 months.

Figure 15: Growth aspirations for next 12 months.
Source: FSB - Verve 'Voice of Small Business' Panel Survey.



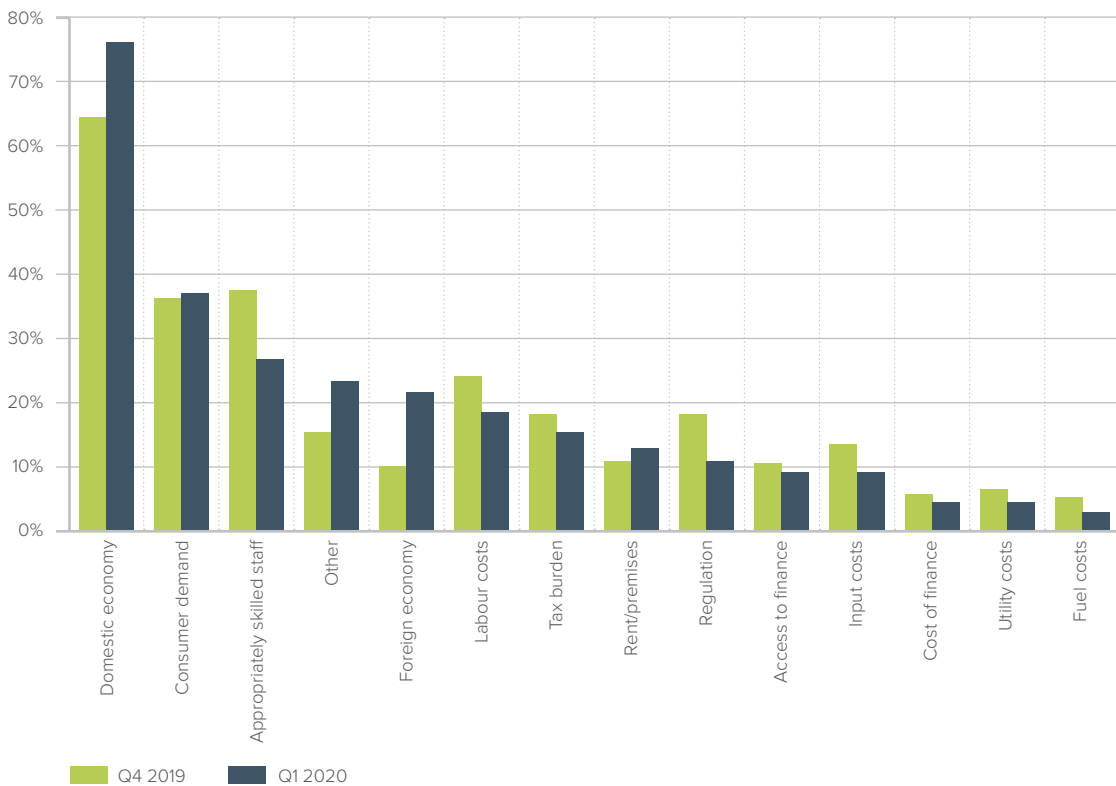
CONCERN OVER THE ECONOMY INTENSIFIES

The domestic economy remains the dominant concern among small businesses in the UK when it comes to growth aspirations. Following a 2.0 percentage point increase compared to the previous quarter, the proportion of firms citing the domestic economy as a barrier to growth was 64.4% in Q4 2019. The next most widespread cause for concern was finding appropriately skilled staff. A quarterly increase of 8.7 percentage points brought the share of businesses finding the recruitment of the right staff a barrier to growth to 37.2% - the highest level since this category was first included in the survey in Q4 2013. Concern over this issue is mirrored in rising labour costs, which 24.1% of businesses felt was a barrier to growth, up by 6.4 percentage points compared to the previous quarter.

With the unemployment rate dropping over recent years, competition for skilled staff has driven up wages across industries. Information and communication businesses were the most likely to face concerns over both appropriately skilled staff and labour costs, with 57.8% and 42.4% of firms flagging these issues respectively.

The international economy was considered less of a barrier in Q4 2019 - the proportion of firms concerned about non-domestic economic issues fell by 3.3 percentage points, to 9.8% - the lowest value on record. Lower global oil prices and a stronger pound seem to have reduced the burden of fuel costs on small businesses, and the proportion of businesses citing these as a barrier to growth fell by 2.6 percentage points over the quarter, to stand at just 4.7%.

Figure 16: Potential barriers to achieving growth aspirations – multiple answers possible.
Source: FSB - Verve 'Voice of Small Business' Panel Survey.

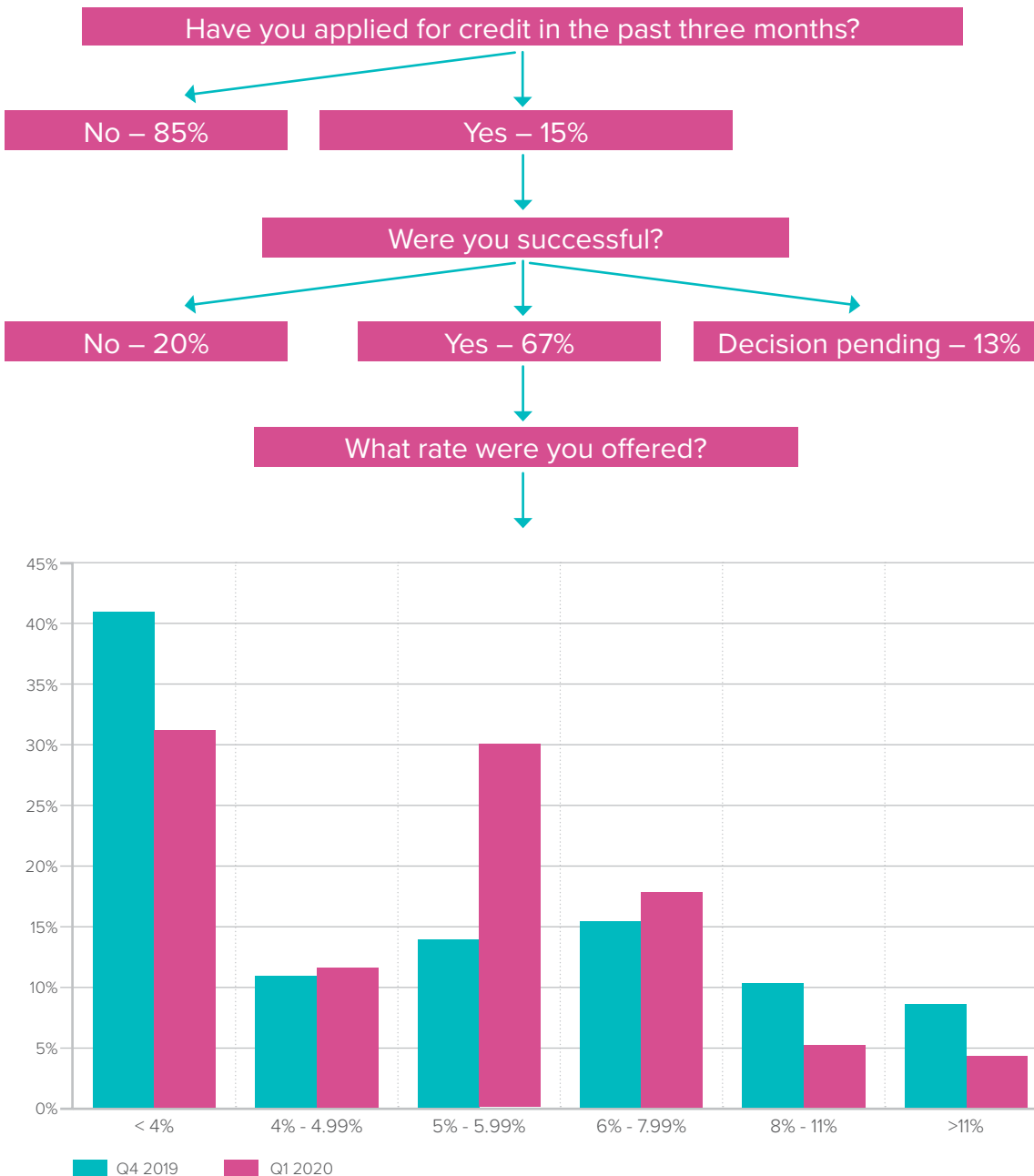


CREDIT

More firms seek finance

CREDIT APPLICATION SUCCESS RATE INCREASES

Figure 17: Credit applications and interest rates offered.
 Source: FSB - Verve 'Voice of Small Business' Panel Survey. Respondents were able to give multiple answers to this question.

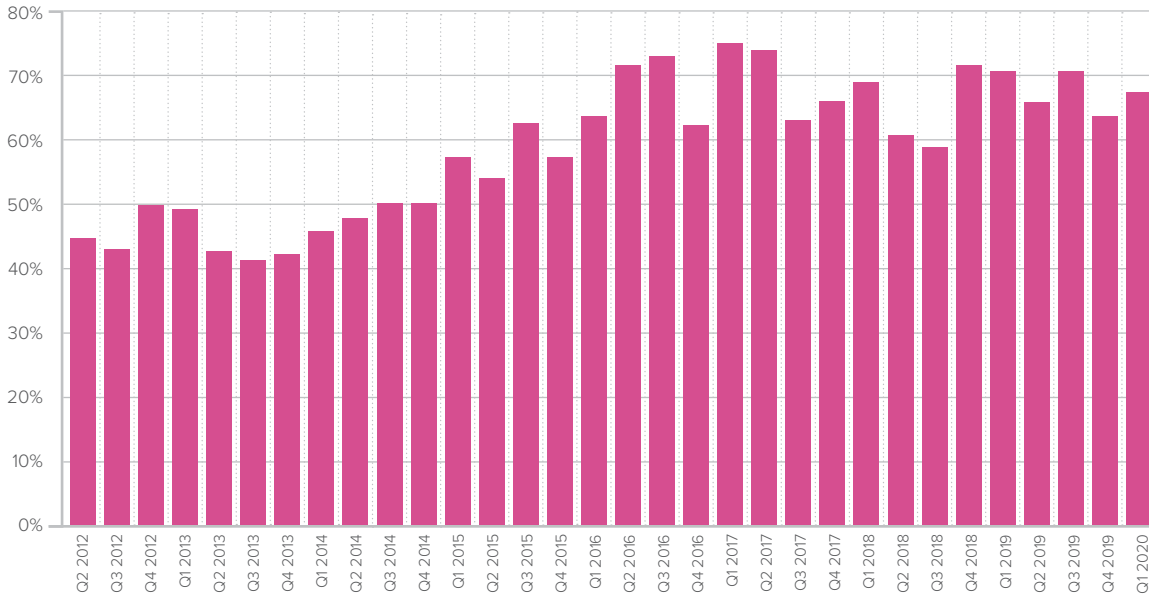


In the first quarter of 2020, the proportion of small businesses that applied for credit increased by 2.1 percentage points. The proportion of those applications that were successful rose by 3.6 percentage points compared to Q4, to stand at 66.9%,

although this was still down by 3.4 percentage points on Q1 2019. The proportion of businesses awaiting a decision was also up, by 2.8 percentage points to 13.3%.

For successful applicants the proportion that were offered an interest rate of less than 4% declined fairly significantly, however, dropping back by 9.7 percentage points compared to Q4 2019, to 31.1%.

Figure 18: Proportion of small businesses successful in their credit applications in the past three months.
Source: FSB - Verve 'Voice of Small Business' Panel Survey.



CREDIT AVAILABILITY AND AFFORDABILITY FALL BACK

The credit availability index fell by 5.2 points to -15.7 in the first quarter of 2020. Despite a higher success rate among small business applicants than the previous quarter, the success rate has fallen by 3.4 percentage points compared to Q1 2019. Meanwhile, the credit affordability index fell by 4.3 points compared to Q4, to stand at -15.6.

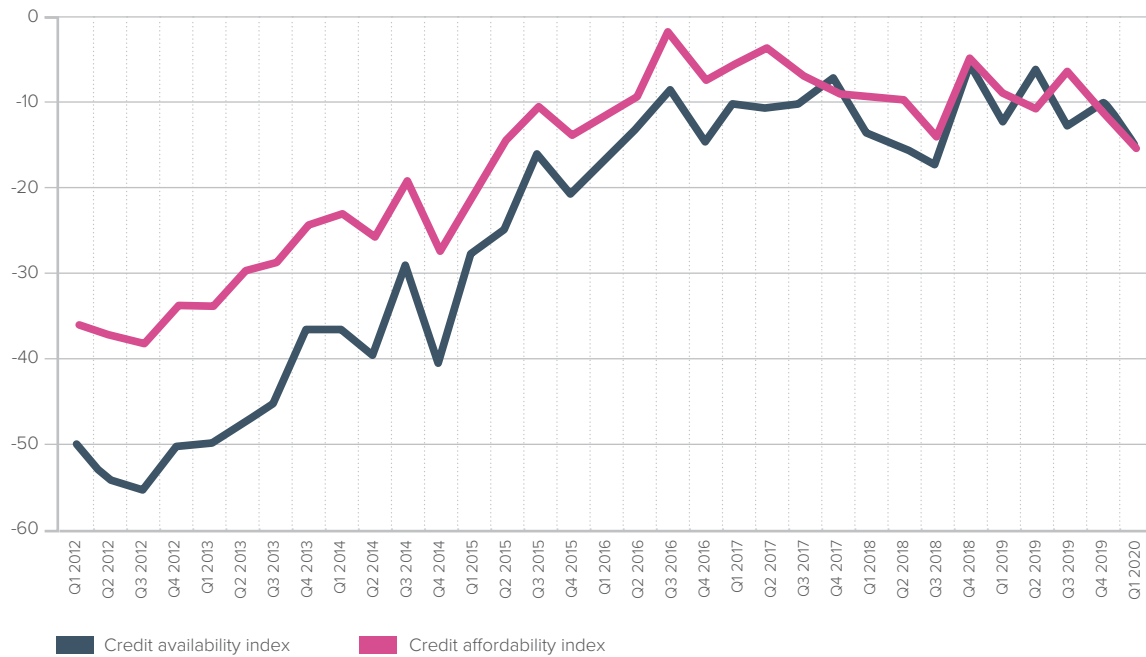
The Bank of England cut interest rates twice during emergency meetings held in March to leave the Bank rate at just 0.1% from 19 March, its lowest ever level. The rate cuts were combined with other measures aimed at maintaining the flow of credit to smaller businesses, with the intention of ensuring that the

reduction in interest rates is passed through to businesses. As revenues fall during an economic contraction, the risk of default rises which would typically see the cost of borrowing increase.

The sheer quantity of support that is being made available by the Bank of England is intended to avoid this issue altogether, ensuring that cheap credit is made available to all businesses while cashflows are diminished. By keeping businesses solvent during the crisis, this will boost their ability to rehire furloughed staff and ramp up output quickly once the restrictions on economic activity are lifted.

Figure 19: Indices of credit affordability/availability perceptions over time, a weighted net balance of those with negative responses subtracted from those with positive responses.

Source: FSB - Verve 'Voice of Small Business' Panel Survey.



INVESTMENT AND PRODUCTIVITY

Decision-making put on ice

SMALL BUSINESSES CUT BACK INVESTMENT PLANS

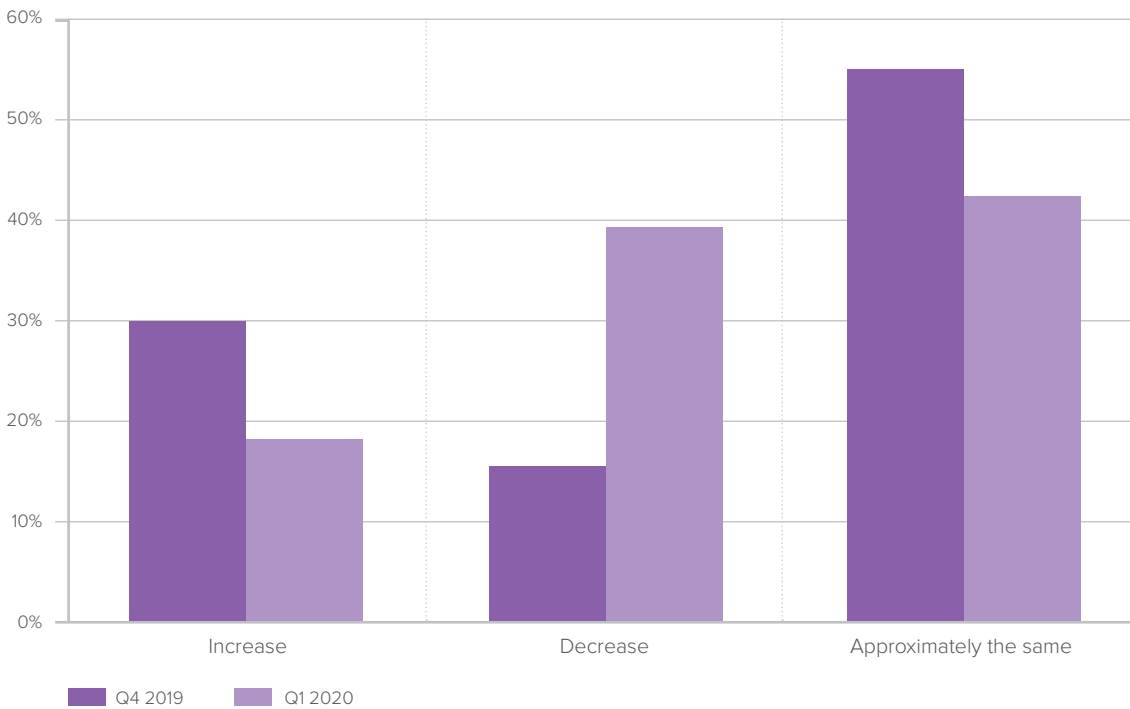
The share of small businesses expecting to decrease their capital investment over the next quarter increased by 24.0 percentage points compared to the previous quarter to stand at 39.3% in Q1 2020. This translates to a decline of 24.7 percentage points in investment intentions year-on-year as businesses focus their attentions on managing the impact of the coronavirus outbreak. The proportion of businesses planning to increase their investment activity over the next three months fell by 9.8 percentage points compared to the previous quarter.

Official statistics indicated that after falling every quarter throughout 2018 the tide may have turned on business investment as fears over a no-deal Brexit subsided leading to a small (0.6%) year-on-year

increase in business investment at the start of 2019. After the UK successfully left the EU at the end of January, and entered a 12-month transition period to negotiate a free trade deal with the EU, businesses may have started to feel more confident about the future and their investment plans. However, the rapid escalation of the coronavirus crisis will have moved most businesses into preservation mode as demand is cut off by the restrictions on economic activity enforced to slow the spread of the infection. For businesses that are still operational, there may be an incentive to capitalise on record low interest rates in order to invest, especially where additional home working technology is needed to increase resilience against an extended lockdown.

Figure 20: Percentage of small businesses expecting to increase and decrease capital investment over next quarter, compared with 12 months ago.

Source: FSB - Verve 'Voice of Small Business' Panel Survey.



METHODOLOGY

These tables are based on the March 2020 research survey of FSB members carried out by Verve. 5,849 Big Voice panel members (all Big voice members at time of survey) were invited to take part in an online survey as well as 28,000 wider FSB members from a sample list. Reminders were sent to all non-respondents. 1,558 responses were received, a response rate of 17% for the panel. The data are weighted by regional gross value added to match the profile of small businesses across the UK. The survey was undertaken between 13th March – 23rd March.

SUMMARY DATA TABLE

	Q2 2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	Q3 2019	Q4 2019	Q1 2020
Small Business Index	12.9	-1.7	-9.9	-5.0	-8.8	-8.1	-21.6	-143.5
Employment - previous three months	0.8%	2.3%	3.9%	-1.0%	-1.5%	1.9%	-1.5%	-7.6%
Employment - coming three months	8.2%	7.4%	5.1%	7.0%	10.2%	5.1%	3.5%	-27.9%
Exports - previous three months	16.5%	10.7%	7.6%	6.8%	-5.8%	-7.1%	-1.6%	-19.1%
Exports - coming three months	16.0%	17.8%	0.2%	-1.6%	11.4%	-4.1%	-9.5%	-52.4%
Credit availability - rated good or very good	21.9%	24.1%	30.2%	28.5%	28.9%	25.7%	27.5%	0.0%
Credit availability - rated poor or very poor	40.0%	42.5%	34.4%	39.0%	33.7%	39.4%	34.7%	0.0%
Credit affordability - rated good or very good	25.4%	23.7%	32.2%	27.9%	27.3%	28.1%	28.1%	0.0%
Credit affordability - rated poor or very poor	35.3%	41.7%	36.1%	37.9%	43.2%	33.8%	39.9%	0.0%

The Small Business Index weights strong responses (much improved or much deteriorated conditions) double and subtracts the weighted proportion of firms reporting deterioration in business prospects over the coming three months from the weighted proportion expecting an improvement.

The Employment and Revenue indicators are net percentage balances, with the proportion of firms reporting a decrease subtracted from the proportion reporting an increase.

Responses are also weighted according to regional gross value added.

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