Q1

FSB VOICE OF SMALL BUSINESS INDEX

QUARTER 1, 2022

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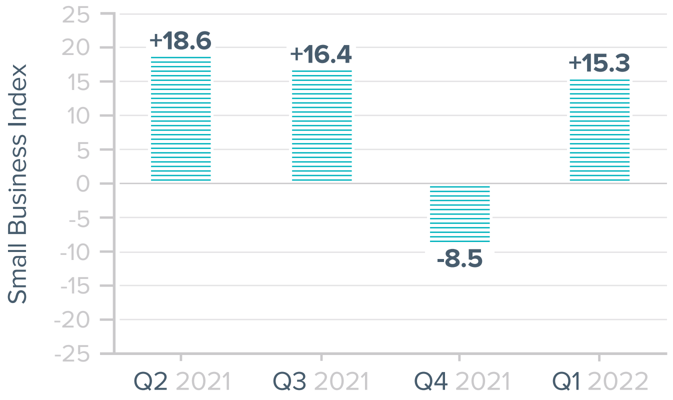
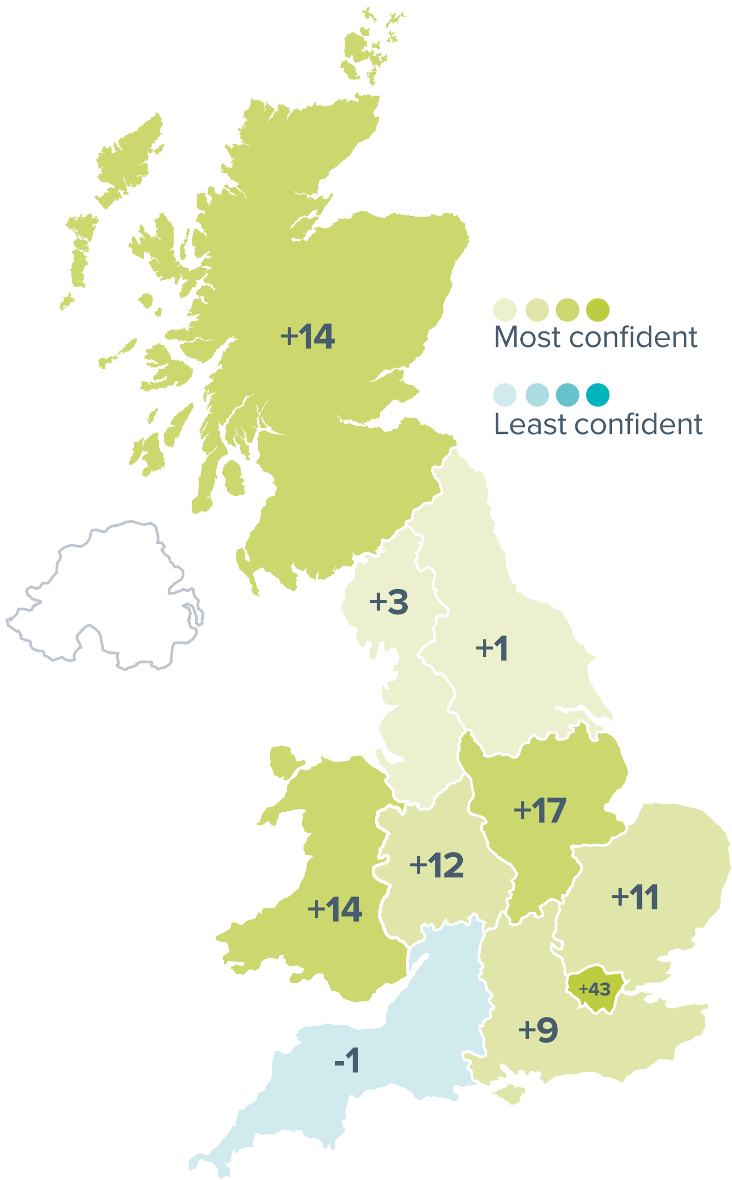
SBI Q1 2022

"Mixed fortunes for small firms as sectoral confidence gap widens"





Operating costs hit all-time high

87%

say **outgoings** are up

Poor payment practice holding firms back

61%

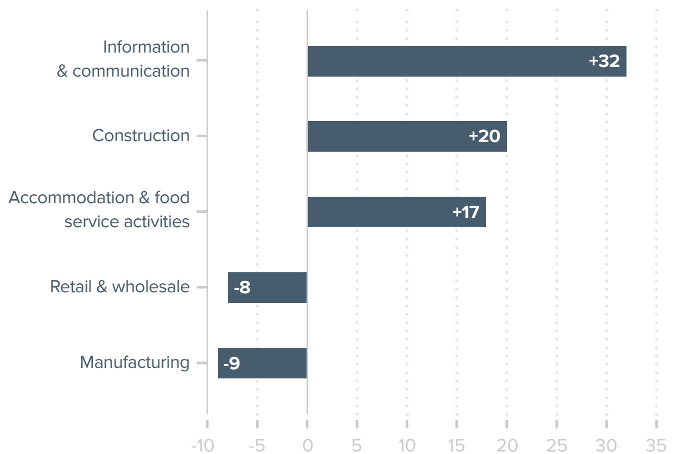
report **late payment of invoices**

Appetite for exporting wanes

77%

are **not making international sales**

Small business confidence by sector



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FSB FOREWORD

The first quarter of 2022 has been a study in contrasts. Just when small businesses had regrouped after the Omicron variant of Covid, any precious and precarious equilibrium which had been achieved was then rapidly undermined by a further increase in input prices, and energy and fuel bills. Adding to this uncertainty, the invasion of Ukraine has sent shockwaves through the geopolitical and business environments, along with the terrible humanitarian toll it has taken on the people of Ukraine.

Yet even against this tumultuous backdrop, with spiralling costs taking an especially harsh toll on firms, small business confidence in our headline measure has improved since the end of last year, when it was firmly in negative territory. This can be put down to small businesses being optimistic in nature, which helps them stay resilient in tough times, with half our respondents looking to expand in the near future. The Q1 2022 confidence reading of 15.3 is however some way below its level in the same quarter last year of 27.3; as far as starts to the year go, it could be worse, but it could be a lot better, and possibly presages more turbulence ahead, as do the still-negative readings in important sectors such as manufacturing and wholesale and retail.

The weakness in export growth continues, with this survey marking the twelfth quarter in a row in which the net balance of exports has been in negative territory. International trade remains precarious. While we welcome the news that a fresh round of import checks due in summer will now be delayed, small businesses looking to trade internationally still face considerable challenges.

Economic concerns among the public are high and still rising, as the cost of living crisis intensifies. With discretionary spending falling, and calls for more intervention from the Government to help alleviate the pressure on people's budgets, the performance of the domestic economy was the most commonly cited barrier to growth among respondents with aspirations to expand, at 58.6%. It is another cause for concern among many others, especially as the Bank of England predicts that inflation has some way higher to go, and could persist at elevated levels for even longer than initially feared. The devastation that inflation at 10% or more for a sustained period of time will cause to small businesses, compounding their input cost woes as already-high prices rise even further, shows the need for further action from policymakers.

Many small businesses find themselves caught in a pincer movement, with rising business and debt costs on one side and falling consumer demand on the other; microbusinesses and sole traders are particularly vulnerable, as they face a hike in the cost of everything from their mortgage to the cost of a tank of petrol, and their weekly supermarket shop. This survey was also undertaken before the impact of the 1.25 percentage point rise in all types of National Insurance contributions was felt by employers, employees, and sole traders. A big victory for small employers was included in the Spring Statement in late March, however, as FSB's lobbying led to a much-needed £1,000 increase in the Employment Allowance, giving small employers £5,000 of relief – it's vital that every small employer makes sure their payroll software has the right box ticked so they get this help.

Government can and should do more to target support at the smallest firms most in need: increasing the rateable value ceiling for small business rates relief, installing a sick pay rebate for small firms, and extending the support offered with energy costs through the council tax system to micro businesses via the rates system. It must also go further to eradicate a worsening culture of poor payment, too – eradicating this corporate scourge would come at no cost to the public purse and only massive gain to the business community and to society as a whole.

Martin McTague,
National Chair

Tina McKenzie,
Policy & Advocacy Chair

ECONOMIST'S VIEW

The Small Business Index saw a rebound in the first quarter of 2022, rising by 23.8 points to stand at 15.3, just 1.1 points below the Q3 2021 level. The improvement in the index is the result of a complex economic picture in the first quarter, with businesses in England welcoming the end of legal Covid-19 restrictions on 24 February. On the same day, Russia started its war in Ukraine, sending energy prices skyrocketing and adding to cost pressures in the UK.

The Omicron wave of the Covid-19 virus led to a spike in new infections across the country and caused the Government to implement stricter restrictions in December last year, contributing to the sharp fall observed in the SBI in Q4 2021. With the lifting of restrictions in February, certain parts of the economy saw a welcome return to consumer activity which lifted growth. In the accommodation and food services sector, for example, output expanded by 8.6% on the month in February. This is mirrored in the industry scores of the SBI where the hospitality sector recorded a 49.5-point gain between Q4 2021 and Q1 2022, lifting its score to 16.5 points. This was the strongest quarterly gain for any single industry, followed by professional, scientific and technical activities and the wholesale and retail sector which saw increases of 33.1 and 32.1 points, respectively.

Looking at the regional index scores, we note that London mounted a strong comeback in Q1 2022, with the score for the capital rising by 47.1 points to stand at 42.5. Given the importance of London's professional services sector as well as the large number of hospitality businesses within the capital, this result aligns well with the industry-specific scores discussed above. Beyond London, Wales and Scotland also recorded strong gains of 45.5 and 36.3 points, respectively. At the other end of the table, the West Midlands, the North West and the East Midlands could only record modest gains of 8.8, 7.3 and 2.3 points, respectively. Manufacturing, which plays a larger role in these regions, also saw only a small improvement of 2.9 points over the quarter and remained in negative territory at -9.1 points.

Despite the improvement in the SBI scores over Q1 2022, there remain some notable economic headwinds weighing on the growth outlook over the coming months. The war in Ukraine has come as a shock to many, and while the UK has only moderate direct exposure through trade with both Russia and Ukraine, the impacts of the war on global energy prices are clearly felt domestically. Businesses are feeling the pinch with fuel prices, as well as utility costs, rising dramatically over recent weeks. Indeed, fuel and utilities are the most commonly cited cost drivers among small businesses in the UK, followed by input prices. Overall, a record 86.7% of businesses surveyed stated that costs had increased over the past three months compared to the previous year, underlining the operational pressures faced by UK SMEs.

Unfortunately, the near-term outlook remains difficult due to a range of factors. Supply chain disruptions look set to remain a challenge for the remainder of the year, with the recent lockdowns in several key Chinese cities showing the continued vulnerability of complex international supply chains to the impacts of the Covid-19 pandemic. Meanwhile, the domestic economy is subject to a surge in price pressures with inflation having reached a 30-year high in March, a value that is expected to be exceeded again in April due to the adjusted Ofgem energy price cap. The emerging cost of living crisis remains a key concern for growth going forward, given that Government support so far has been limited and household disposable income is set to fall by as much as £2,500 per household this year. Moreover, tax changes which came into effect at the start of April, such as the 1.25 percentage point National Insurance increase, add to businesses' employment costs. As the impacts of the pandemic start to fade, there are numerous new challenges awaiting UK SMEs in the coming months.

Kay Daniel Neufeld,
Head of Forecasting and Thought Leadership,
Cebr

FSB EXECUTIVE SUMMARY

Key findings this quarter:

The Small Business Index (SBI) increased 23.8 points in Q1 2022, reaching 15.3. This marked a return to improvement, and indeed a return to positive territory, after the index had slumped to -8.5 in Q4 2021.

- **The majority of UK regions saw a positive reading on the SBI in Q1, marking a reversal of fortunes compared to Q4 2021, when most regions saw scores below zero.** Only the South West saw a negative reading in Q1, while London was by far the strongest performer.
- **There was a quarterly improvement in the SBI reading for all major industries in Q1 2022.** Nevertheless, some industries still saw negative SBI readings, notably manufacturing and wholesale and retail. The negativity in these sectors reflects several headwinds for the UK economy, including continued supply chain pressure and the cost-of-living crisis.
- **The net balance of small businesses reporting revenue growth over the previous three months stood at 11.1% in Q1.** This positive figure reflects the continued economic recovery at the aggregate level and subsequent impact on business revenues.
- **The net balance of exporting businesses reporting growth in the value of their exports stood at -5.3% in Q1.** This marked the twelfth consecutive quarter for which the net balance of exports has stood below zero. The fact that the net value of export growth remains in negative territory highlights the unfavourable conditions still faced by exporters.
- **Seven in eight businesses (86.7%) reported increased costs compared to a year ago in Q1, while just 3.0% reported a decrease.** Respectively, these figures represent a series high and a series low, highlighting the widespread nature of cost pressures at present. Businesses in manufacturing, which have been particularly exposed to mounting input prices, were the most likely to report upward cost pressures.
- **Price pressures are being driven by commodities, and this is reflected by the fact that fuel and utilities were the two most commonly cited sources of cost pressures amongst SBI respondents in Q1.** Three in five businesses (60.1%) selected fuel as a driver of costs in Q1, up from 45.6% in Q4 2021. Utilities were selected by 58.0% of respondents, up from 44.8% in Q4.
- **Growth aspirations were less widespread in Q1 than in the previous quarter (Q4 2021), with the proportion of firms seeking to expand falling from 54.1% to just 50.3%.** Nevertheless, the net balance of firms aspiring to grow is now roughly in line with pre-Covid levels, having initially slumped during the early stages of the pandemic, before seeing significant gains in 2021 upon the reopening of the economy.
- **The most commonly cited potential barrier amongst those aspiring to grow was the domestic economy, being reported by 58.6% of respondents.** This reflects the generally worsening outlook for the UK economy, with aggregate growth set to slow significantly on the year.
- **The proportion of small businesses applying for credit fell for a seventh consecutive quarter in Q1 2022.** Just 9.1% of respondents stated that they had applied for credit for business purposes in the past three months, the lowest share in the SBI's history. Credit has become less affordable and less widely available in recent months.
- **Businesses' investment intentions slipped in Q1 2022.** This likely stems from the weakening economic growth outlook as well as less favourable credit conditions.

UK MACROECONOMIC OVERVIEW

UK economic outlook weakens amidst cost-of-living crisis and Ukraine conflict

After the emergence of the Omicron variant brought some disruption at the end of 2021, the UK economy has returned to growth in early 2022, with output picking up in both January and February. Output now stands firmly above pre-pandemic levels at the aggregate level. There remains some sectoral variation, however, with the agriculture and production sectors still seeing output fall short of pre-Covid levels as of February 2022. Meanwhile, services and construction are seeing higher levels of activity than prior to the pandemic.

Despite the growth witnessed in the first months of the year, the medium-term outlook has taken on a more negative tone. Several emerging trends are presenting headwinds to the UK economy. Amongst these are global supply chain pressures, the conflict in Ukraine, and an expected real decline in household incomes. The last of these has been driven by mounting inflationary pressures, with price growth according to the Consumer Prices Index (CPI) measure having reached a 30-year high of 7.0% in March. This has prompted monetary action from the Bank of England, with the base rate having been raised on several occasions, reaching 0.75%. Collectively, these factors are set to put downward pressure on the rate of economic growth. Indeed, Cebr's forecasts for growth for 2022 have been downgraded several times since the turn of the year, with an annual expansion of 3.1% now expected.

The anticipated slower rate of growth is already evident in several data sources. The services and composite PMI readings stood at 58.3 and 57.6, respectively, in April. Both of these stand over 50, indicating expansion, yet are lower than the respective figures seen in March, indicating a weaker rate of improvement. Meanwhile, the emerging headwinds have prompted falls in other economic indicators. One example has been in the retail sector, with sales volumes having fallen in both February and March, illustrating the initial impacts of the cost-of-living crisis and the subsequent shift in consumer activity. Whether this trend continues, and indeed whether it spreads to other sectors, will be key to the economic outlook for the rest of the year.

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

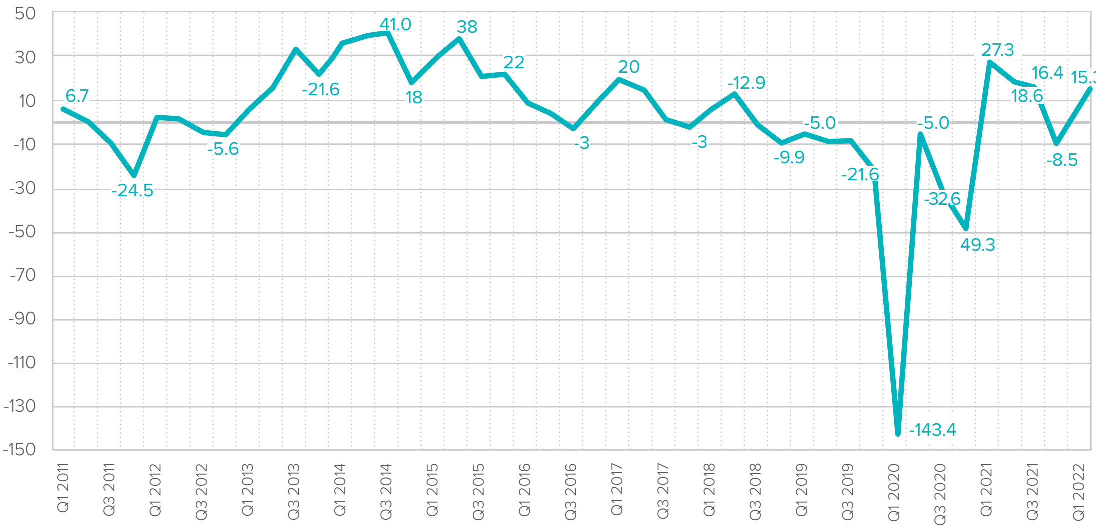
Small Business Index increases as Covid-19 disruption subsides

The Small Business Index (SBI) increased 23.8 points in Q1 2022, reaching 15.3. This marked a return to improvement, and indeed a return to positive territory, after the index had slumped to -8.5 in Q4 2021, prompted by the emergence of the Omicron variant. Q1's positive reading means that the proportion of small businesses expecting an improvement in performance over the coming quarter exceeded the proportion of firms expecting performance to worsen.

The improvement in the SBI in Q1 likely reflects the economy's return to growth in the early months of 2022 and the corresponding impact on business activity. The fall in Covid-19 cases and removal of restriction measures has improved the business landscape compared to Q4 2021, with positive SBI readings being seen across most major sectors. Manufacturing and wholesale and retail provided notable exceptions, however, with negative readings reflecting the emerging supply- and demand-side headwinds facing the UK economy.

Positivity was witnessed in the SBI readings across almost all UK regions, with only the South West seeing a negative score. This reading was barely below zero, however, at -1.1. This near-unanimous positivity reflects the broad nature of economic growth in the early months of 2022, and the expectation that this will continue in the coming quarter. Particular strength was seen in the capital, with London seeing an SBI reading of 42.5.

Figure two: The FSB Small Business Index[1]: 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

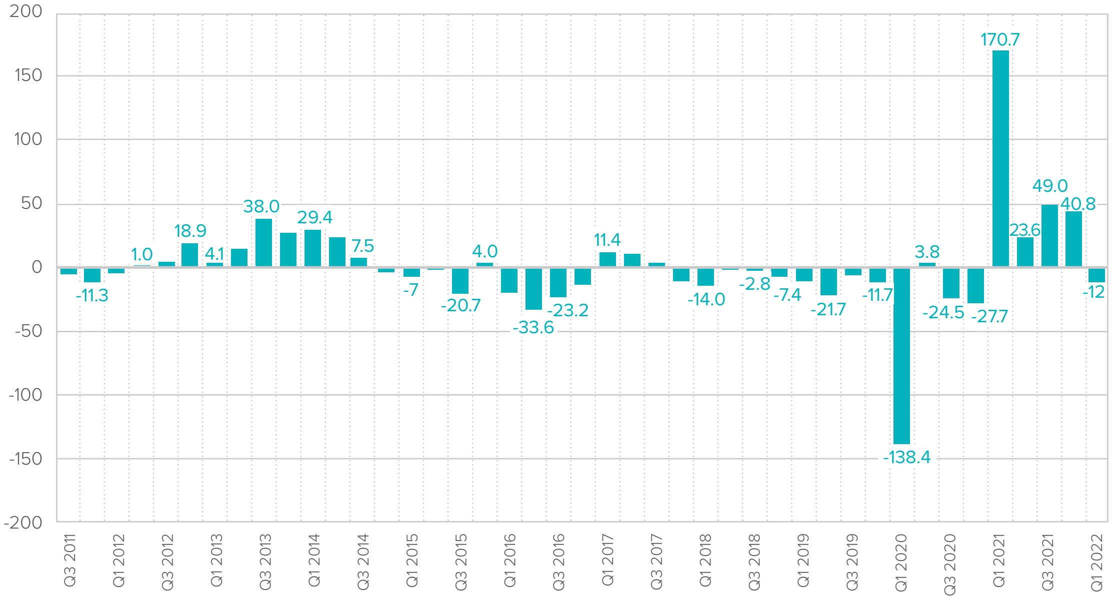
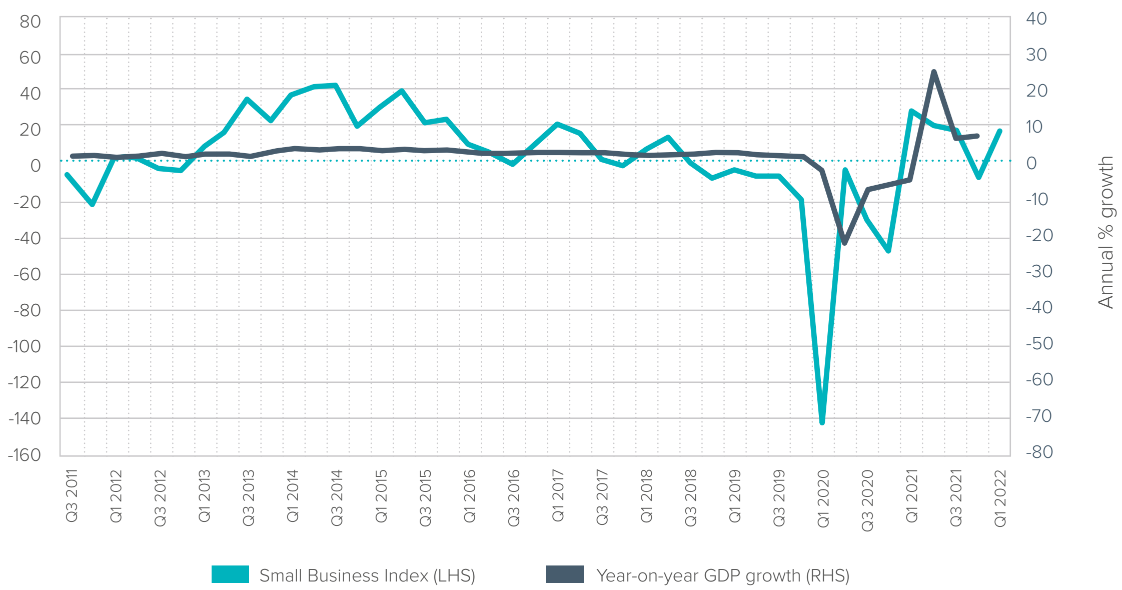


Figure four: UK SBI against year-on-year UK GDP growth
Source: ONS, FSB - Verve 'Voice of Small Business' Panel Survey



REGION AND NATION SMALL BUSINESS INDICES

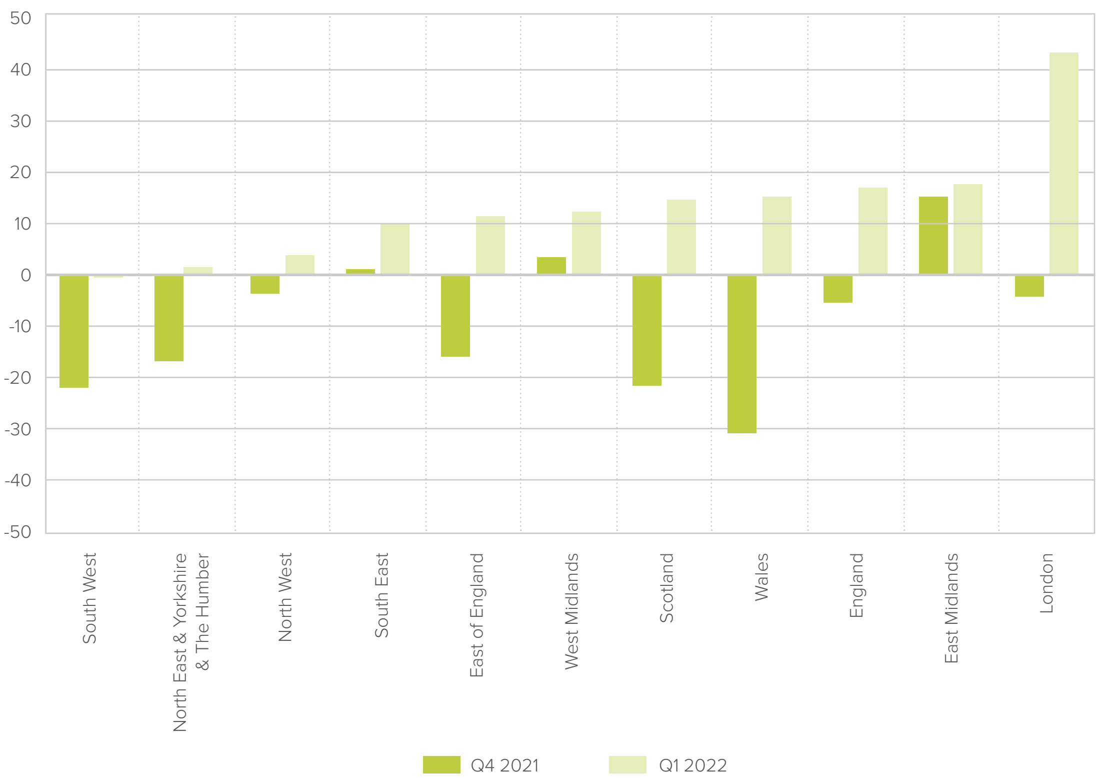
SMALL BUSINESS INDEX RETURNS TO POSITIVE TERRITORY FOR MAJORITY OF REGIONS

The majority of UK regions saw a positive reading on the SBI in Q1, marking a reversal of fortunes compared to Q4 2021, when most regions saw scores below zero. This shift reflects the improved optimism across the economy in the early months of 2022, fuelled by the return to growth.

The most optimistic region in Q1 looking ahead to Q2 was London, with an SBI score of 42.5. London has likely benefited from service businesses' gradual return to office-based working, with this having residual impacts on the large cluster of consumer-facing services in the capital. Meanwhile, London has also benefited from the prevalence of professional services and information and communication businesses, with these two sectors being the strongest performers on this latest round of the SBI.

At the other end of the scale, the South West was the only region to exhibit a negative SBI reading. Nevertheless, this was barely below zero, at -1.1. Two of the South West's main industries are tourism and transport and logistics. Both of these are set to be adversely affected in the coming months, going some way towards explaining businesses' general pessimism in the region. With consumers set to cut down on non-essential expenditure as a result of the cost-of-living crisis, tourism is likely to face some turbulence. Meanwhile, transport and logistics activity continues to be disrupted by issues with global supply chains and fuel prices.

Figure five: 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

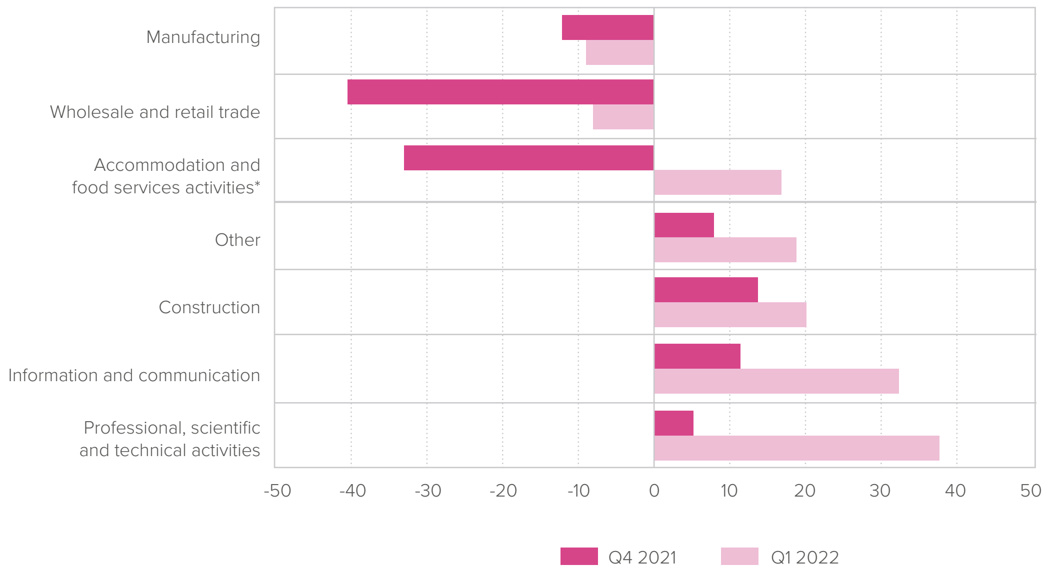
IMPROVEMENT ACROSS ALL MAJOR SECTORS, BUT PESSIMISM PERSISTS ACROSS MANUFACTURING AND RETAIL

There was a quarterly improvement in the SBI reading for all major industries in Q1 2022. This was witnessed to varying degrees, however. The largest quarterly improvement was seen amongst businesses in accommodation and food services, witnessing an uptick of 49.5 points to reach a reading of 16.5. A large improvement was also seen for businesses in professional, scientific and technical services, amounting to an increase of 33.1 points to reach 37.6, the highest SBI reading of any sector. Meanwhile, an increase of just 2.9 points was seen for businesses in manufacturing.

Manufacturing's SBI reading stood in negative territory for a second consecutive quarter in Q1 2022, with a reading of -9.1. As such, more manufacturing businesses expect their performance to worsen over the coming quarter than improve. This likely reflects a continuation of trends that have adversely impacted the sector in recent months. One key factor has been global disruption to supply chains, which has made sourcing inputs more burdensome for businesses. The sale of output goods has also been hindered, with logistics and export issues placing difficulties on manufacturers' shipping of finished products. These trends have collectively put significant cost pressures on manufacturers, as reflected in the record high levels of producer price inflation seen in recent months.

The retail sector also saw a negative SBI reading in Q1 2022, at -8.2. The sector has faced some turbulence in recent months. The emergence of the Omicron variant put downward pressure on sales volumes in December 2021, with consumer activity being discouraged amidst the faster spread of the virus. A partial recovery was then witnessed in January before two consecutive months of decline in February and March, taking retail activity to its lowest level in a year. This decline has been driven by the emerging cost-of-living crisis, with mounting consumer prices putting significant downward pressure on households' budgets. Cebr expects this trend to worsen over the coming months. CPI inflation is set to peak at 8.7% in the first half of the year, reducing real spending power even further. Insofar as this will also reduce consumers' propensity to spend, this outlook for inflation explains retailers' pessimism looking ahead to Q2.

Figure six: FSB Small Business Index by sector – small business prospects over coming three months
Source: FSB - Verve 'Voice of Small Business' Panel Survey



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FINANCIAL PERFORMANCE

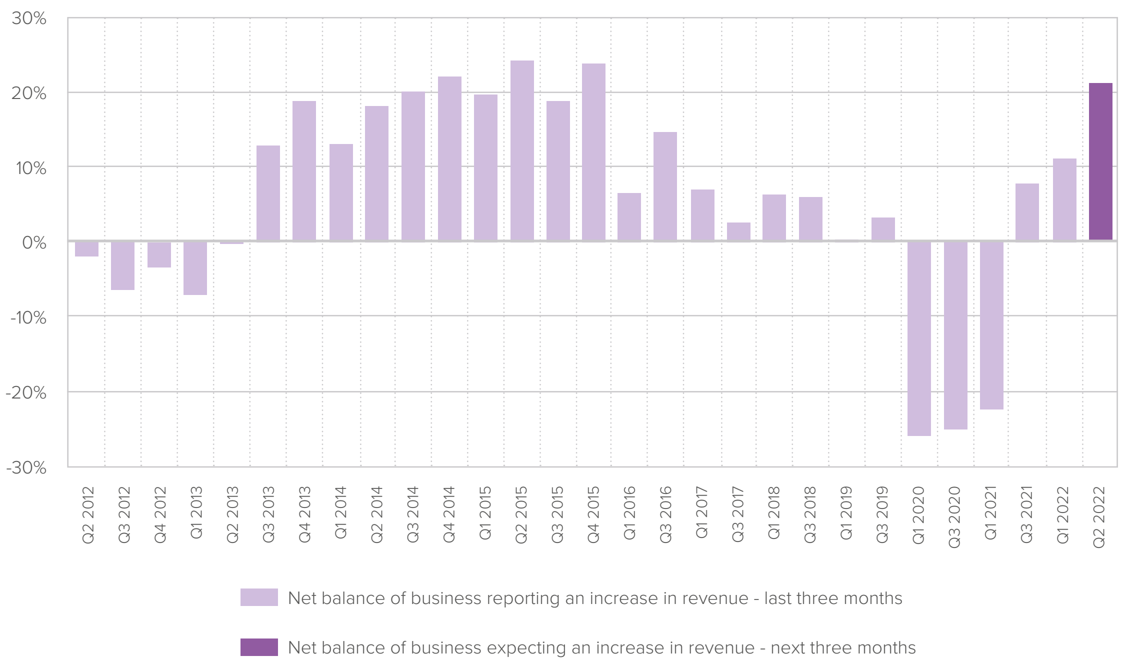
MAJOR SECTORS EXPECT REVENUE GROWTH IN Q2 DESPITE EXPECTED ECONOMIC GROWTH SLOWDOWN

The net balance of small businesses reporting revenue growth over the previous three months stood at 11.1% in Q1 2022. The positive figure means that the number of small businesses reporting an increase in revenue levels outweighed the number reporting a decrease. This net balance figure for revenue is the largest since Q3 2016.

Most major sectors recorded positive readings on this measure in Q1. The highest figure was seen for construction, with a net balance of 33.1% of small businesses reporting revenue growth during the quarter. The weakest positive figure was seen for accommodation and food services, at 10.8%. The near-unanimous positivity on this reading reflects the continued economic recovery at the aggregate level. Activity in Q1 2022 was firmly above pre-pandemic levels, with continued growth feeding into business activity and subsequently to revenues. Wholesale and retail recorded a negative net balance of -10.5%, with this aligning with the general downward trend in retail sales volumes in recent months.

Looking ahead, small businesses are more optimistic, with a net balance of 21.2% expecting their revenue to grow over the next quarter. The sectoral breakdown is broadly similar, with the construction sector seeing the highest net balance of all major sectors, at 38.0%, and wholesale and retail seeing the weakest, at 4.2%. As such, for all major sectors, more businesses expect their revenues to improve over the coming quarter than not. It remains to be seen how much of this will be dictated by increased sales volumes and how much will be a matter of rising prices, however. With the economy set to continue growing, albeit at a slower rate, and prices set to continue rising, revenue growth will likely reflect the combination of these factors.

Figure seven: Small business gross profit, net percentage balance – proportion reporting / expecting increase less proportion reporting / expecting decrease
Source: FSB - Verve 'Voice of Small Business' Panel Survey



EXPORTS

EXPORTERS OPTIMISTIC DESPITE CONTINUED SUPPLY CHAIN DIFFICULTIES AND UKRAINE CONFLICT

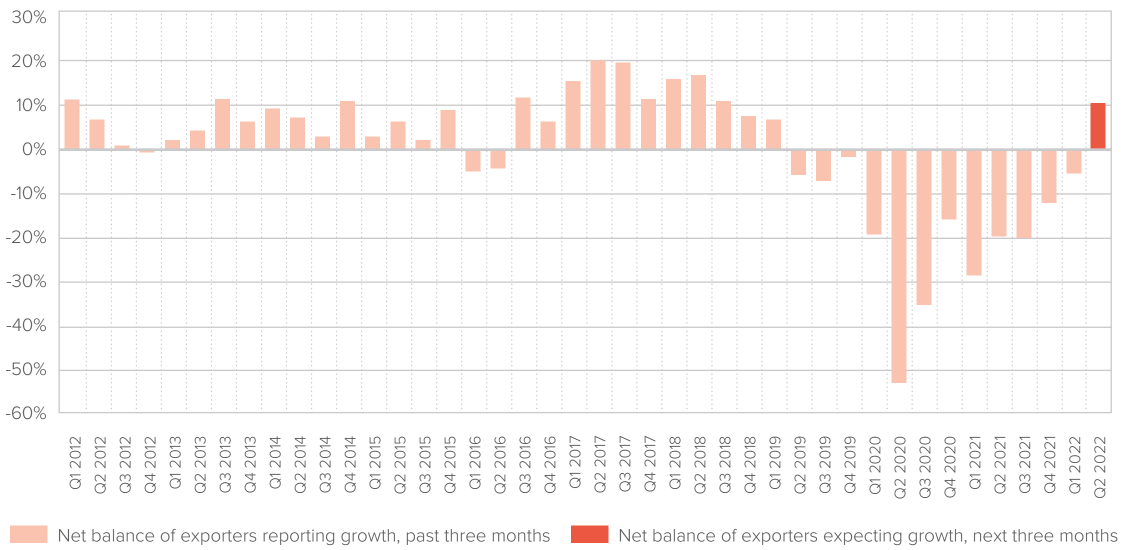
The net balance of exporting businesses reporting growth in the value of their exports stood at -5.3% in Q1. This marked the twelfth consecutive quarter for which the net balance of exports has stood below zero. Nevertheless, this marked the least negative reading since before the pandemic.

The exports measure last saw a stronger value in Q4 2019, when a net balance of -1.6% of small businesses reported growth in the value of their exports. As such, exporting businesses are seeing a weaker rate of decline that than they were during the depths of the pandemic, with the net balance of exporting businesses reporting growth in the value of those exports having reached a low of -52.8% in Q2 2020, before a further dip this time a year ago to -28.4% in Q1 2021. The fact that the net value of export growth remains in negative territory highlights the unfavourable conditions still faced by exporters, however. This has notably stemmed from continued supply-side issues, including disruption to the sourcing of input goods as well as to the channels for distributing finished goods. On the latter point, the continued uncertainty brought by the UK's withdrawal from the EU and subsequent trade frictions remain key.

Looking ahead to Q2, exporting businesses are more optimistic than pessimistic. This is reflected in the positive net balance figure of 10.4%, marking the first time this measure has stood above zero since Q2 2019, and which comes despite emerging trade disruptions that are likely to impact the export environment. Amongst these are the conflict in Ukraine and subsequent sanctions upon Russia, as well as the general slowdown in global economic growth. Small businesses in professional, scientific and technical activities exhibit the most optimism, with a net balance of 25.1% of respondents expecting the value of their exports to increase over the coming quarter. The services sector is less likely to be impacted by the trade frictions described above, partially explaining this greater optimism. This point also partially explains London's position as the most optimistic region when it comes to exports looking ahead to Q2, given the capital's cluster of professional services businesses.

At the other end of the scale, a net balance of -27.4% of exporters in wholesale and retail expect the value of their exports to increase over the coming quarter. As with retail revenues, this pessimism is being driven by the cost-of-living crisis and subsequent impact on consumer spending power. This trend is impacting other economies as well as the UK and is notably prevalent amongst key export partners, such as the US and Europe.

Figure eight: 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

SHARE OF RESPONDENTS REPORTING COST INCREASES REACHES SERIES HIGH

The net balance of small businesses reporting an increase in operating costs increased for the fourth consecutive quarter in Q1, reaching a series high of 83.8%. Within this figure, 86.7% of businesses reported increased costs compared to a year ago, while just 3.0% reported a decrease. Respectively, these figures represent a series high and a series low, highlighting the widespread nature of cost pressures at present.

The high prevalence of increased business costs reported in the latest Small Business Index aligns with trends seen at the aggregate level. Cost pressures for businesses had been mounting for some time due to disruption in global supply chains. The situation has worsened in recent months, however, with geopolitical events putting significant pressure on commodity prices and hence on input goods. The latest data from the Office for National Statistics show that the Producer Price Index for inputs grew by 19.2% year-on-year in March, marking a series high.

Businesses in manufacturing were the most likely to report increased costs in Q1, with this being the case for 95.9% of respondents. Due to the input-output nature of the manufacturing process, these businesses have been particularly exposed to pressures from commodity prices and supply chain issues in recent months. On a regional basis, rising costs were most likely to be seen in the East Midlands, where 90.9% of respondents reported rising costs relative to a year ago. The East Midlands is home to a cluster of manufacturing businesses, and will therefore also be susceptible to cost pressures from these channels.

The commodity-driven nature of cost increases is reflected by the fact that fuel and utilities were the two most commonly cited sources of cost pressures amongst respondents in Q1. Three in five businesses (60.1%) selected fuel as a driver of costs in Q1, up from 45.6% in Q4 2021. The prevalence of utility price increases saw a similarly-sized increase, with this category being cited by 58.0% of businesses in Q1, up from 44.8% in Q4.

Figure nine: 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

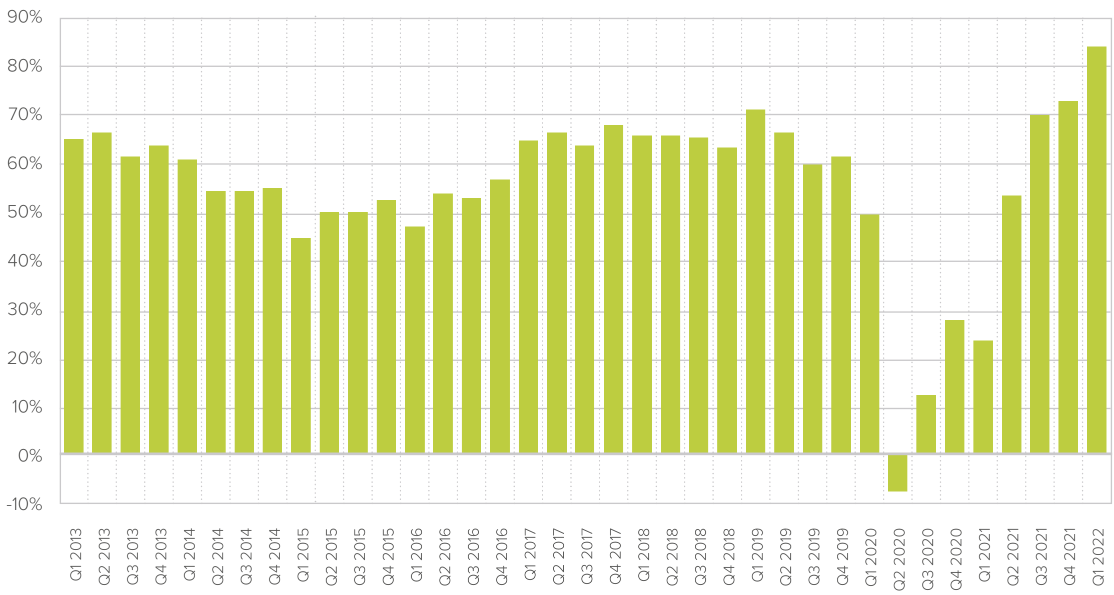
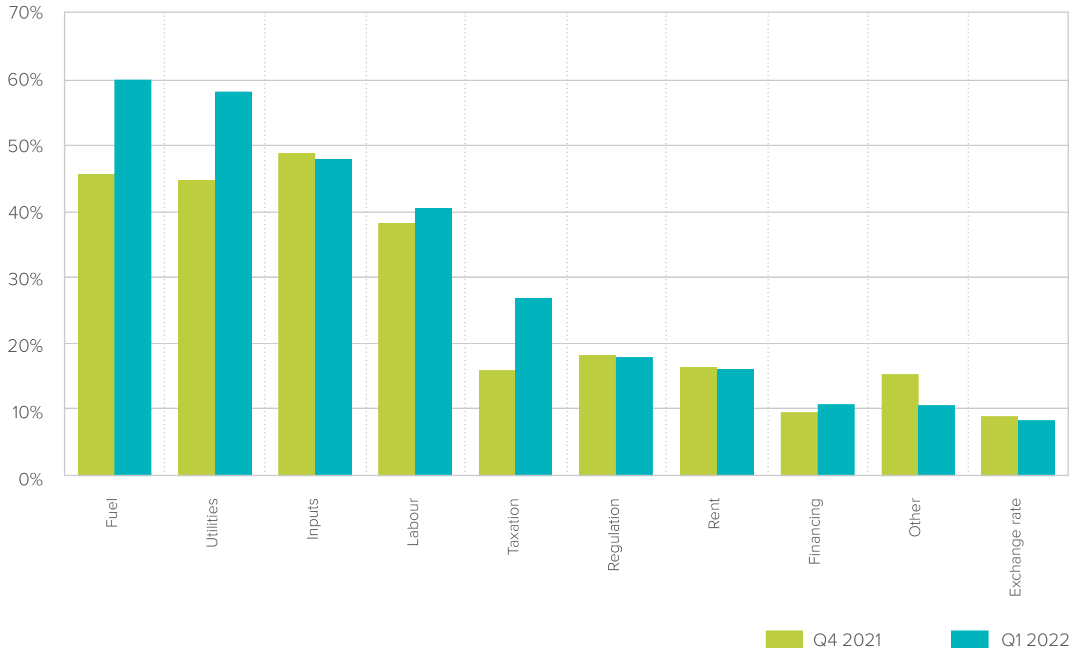


Figure 10: Main causes for changing business costs (firms may give multiple answers)
Source: FSB - Verve 'Voice of Small Business' Panel Survey



EMPLOYMENT

SMALL BUSINESSES REPORT CONTINUED GROWTH IN EMPLOYEE NUMBERS AMIDST STRONG LABOUR MARKET

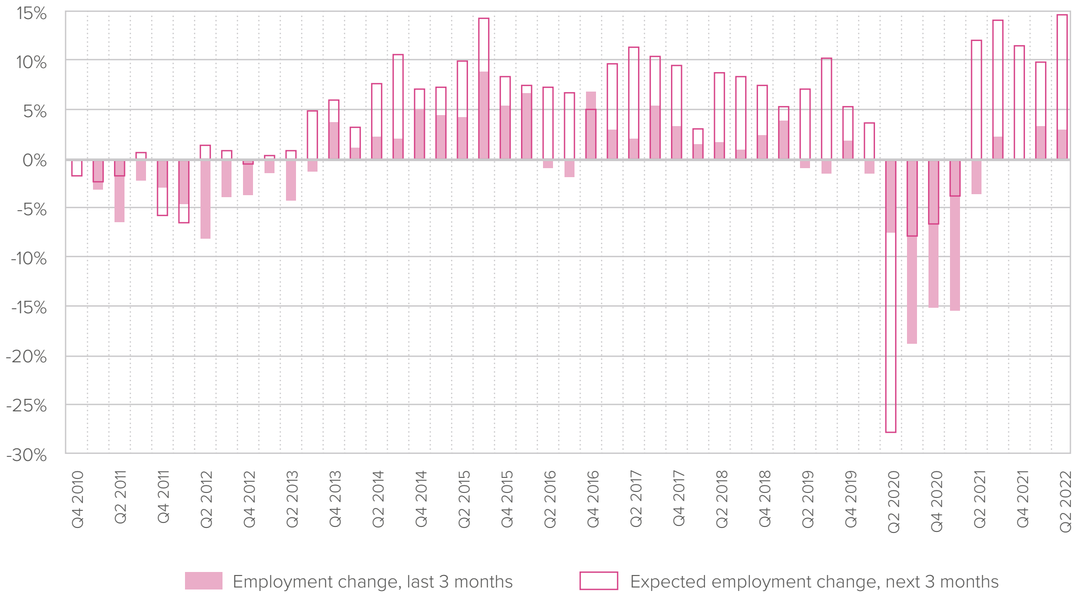
The net balance of small businesses reporting growth in employee numbers stood at 2.9% in Q1, down from 3.3% in Q4. The positive figure means that the number of businesses seeing their workforce increase in size outweighed the number of businesses seeing a contraction in employee numbers. Just 10.7% of respondents reported a contraction in the size of their workforce in Q1, the lowest share since Q2 2017.

The continued growth in employee numbers amongst small businesses aligns with labour market trends at the aggregate level. Recent months have seen a return to the pre-pandemic unemployment rate, with joblessness standing at just 3.8% in the three months to February 2022. Meanwhile, the hiring landscape remains active, with both vacancies and the number of employees on payrolls reaching record highs in recent months.

On a regional basis, small businesses in London were the most likely to report growth in employee numbers in Q1, with this being the case for 18.2% of respondents. London has likely benefited from the phased return to office-based working introduced by many services businesses. This increases residual demand for consumer-facing services and other businesses reliant on footfall, of which there are many within the capital.

Looking ahead, businesses are optimistic about further growth in employee numbers. A net balance of 14.5% expect to employ more people over the coming three months. This broadly aligns with Cebr's view of the labour market, with the unemployment rate set to remain low over Q2. However, there is some pessimism surrounding the medium-term outlook. Continued price pressures, the cost-of-living crisis, and the general slowdown in economic growth are expected to weigh heavily on businesses, and could increase businesses' prevalence to let staff go. As such, we would expect future rounds of the SBI to show falling employee numbers towards the end of the year.

Figure 11: 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



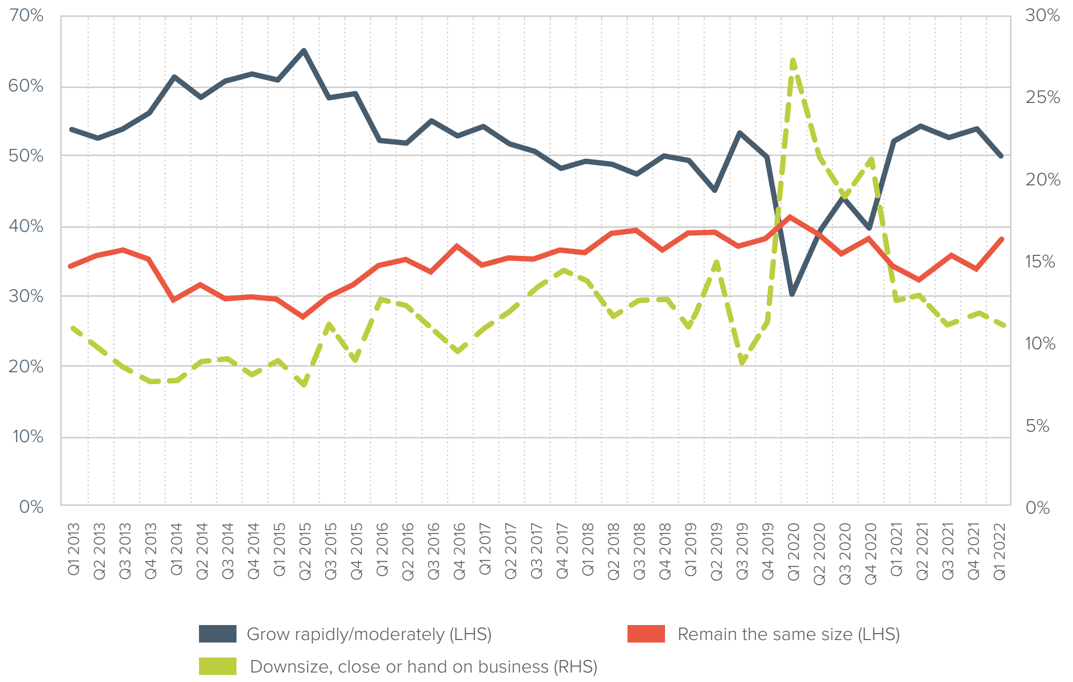
GROWTH ASPIRATIONS AND CHALLENGES

GROWTH ASPIRATIONS AMONGST BUSINESSES FALL, YET REMAIN ROUGHLY IN LINE WITH PRE-PANDEMIC TRENDS

The net balance of firms expecting to grow over the next twelve months declined by 3.1 percentage points in Q1, reaching 39.1%. This was mostly driven by a fall in the proportion of firms aspiring to grow, dropping from 54.1% in Q4 2021 to just 50.3%. The net balance of firms aspiring to grow is now roughly in line with pre-Covid levels, having initially slumped during the early stages of the pandemic, before seeing significant gains in 2021 upon the reopening of the economy.

On a sectoral basis, aspirations to grow were strongest amongst businesses in information and communication, where 60.6% of respondents expect to expand over the coming year. Businesses in this sector have been able to benefit from some of the behavioural shifts prompted by the pandemic, notably the shift to remote working and the growing importance of the digital economy, providing a strong basis upon which these businesses can grow looking ahead. The weakest growth aspirations were seen amongst businesses in accommodation and food services, with just 32.1% of businesses expecting to expand. These businesses were amongst the most adversely impacted during the pandemic, with revenues significantly hindered by restrictions on consumer activity. As such, these businesses are more likely to be focused on stability and survival than growth this year.

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



DOMESTIC ECONOMY A MORE COMMON POTENTIAL BARRIER TO GROWTH AMIDST WEAKENING AGGREGATE OUTLOOK

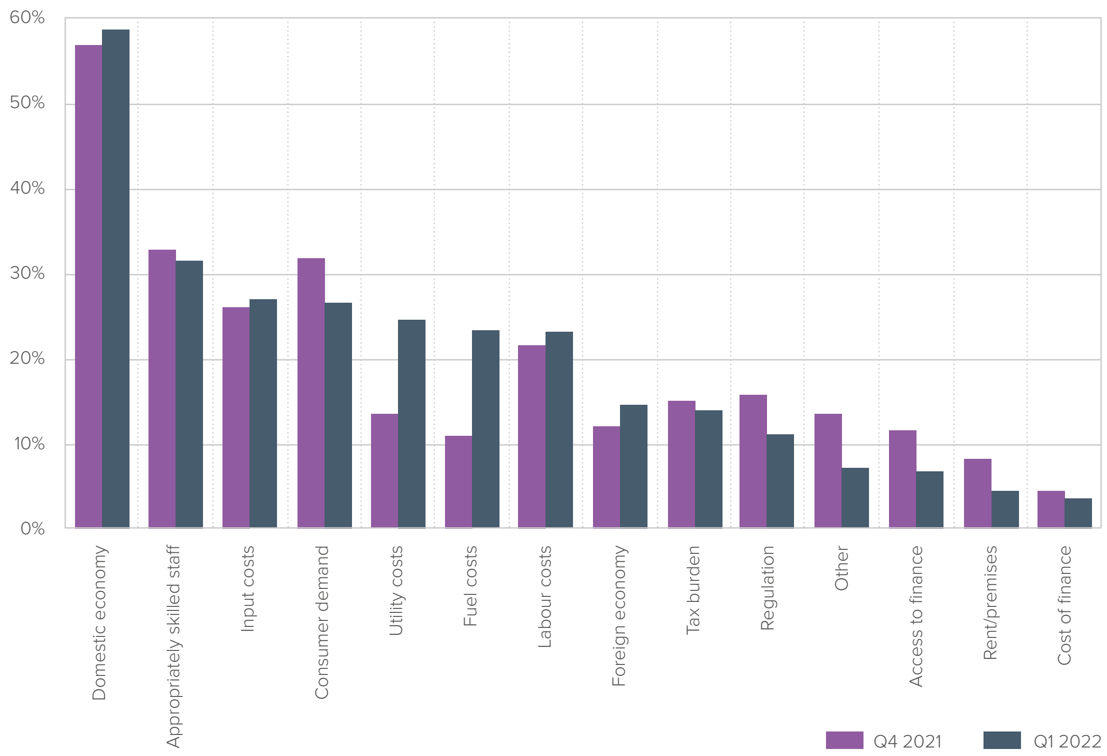
Amongst those aspiring to grow, the most commonly cited potential barrier to growth is the domestic economy. Nearly three in five respondents (58.6%) see domestic conditions as potentially disrupting their growth over the coming year, up from the equivalent share of respondents in Q4 2021, 56.7%. The outlook for the UK economy's growth has worsened in recent months, with supply chain pressures, tough consumer conditions, and global geopolitical conditions all acting as potential lags on growth.

Finding appropriately skilled staff was the next most commonly cited barrier to growth amongst small businesses. Three in ten respondents (31.3%) selected this option, down slightly on Q4 2021's value of 32.6%. Staff shortages have been evident in the UK for some time, with this trend showing little sign of easing. According to the Office for National Statistics, employment remains below pre-pandemic levels, while economic inactivity remains above. This goes some way to explaining staff shortages at the aggregate level.

Q1 saw significant jumps in the shares of businesses seeing utility and fuel costs as potential barriers to growth. In the case of utilities, 24.4% of respondents now see this as a potential barrier, up from just 13.3% in Q4 2021. For fuel, a similar share, 23.2%, now see this as a growth barrier, up from just 10.7% in the previous quarter. These trends reflect the mounting price pressures witnessed for these key input goods, which in turn stem from the commodity price volatility seen over recent months.

Price pressures have also been seen more generally, with the Producer Price Index for inputs being 5.0% higher in Q1 than in Q4 2021. This is reflected in the slight increase in the share of respondents citing input costs as a potential barrier to growth, reaching 26.8% in Q1, up from 25.9% in Q4.

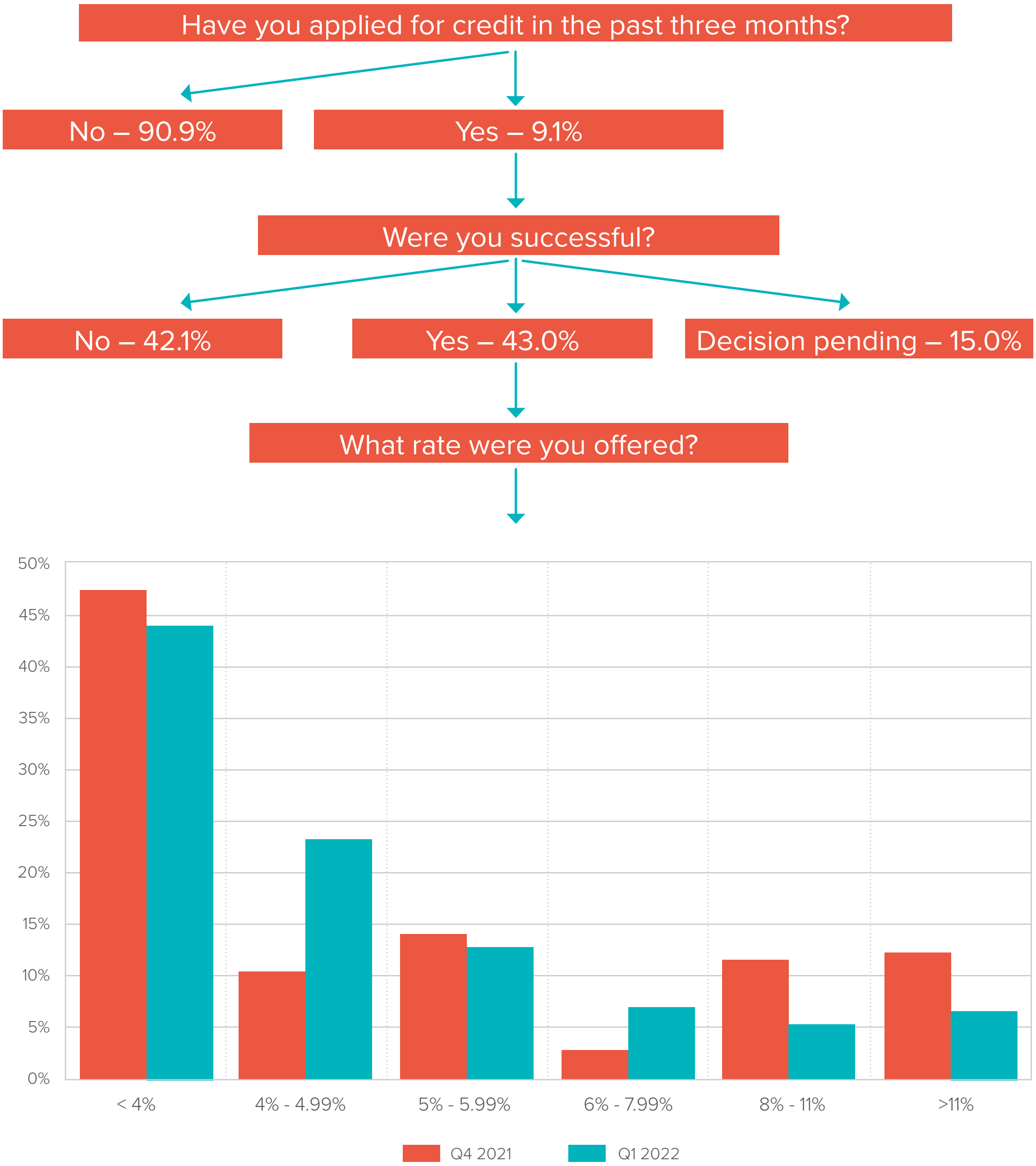
Figure 13: Potential barriers to achieving growth aspirations – multiple answers possible
Source: FSB - Verve 'Voice of Small Business' Panel Survey



CREDIT

RATE OF CREDIT APPLICATIONS DWINDLES TO SERIES LOW

Figure 14: 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.



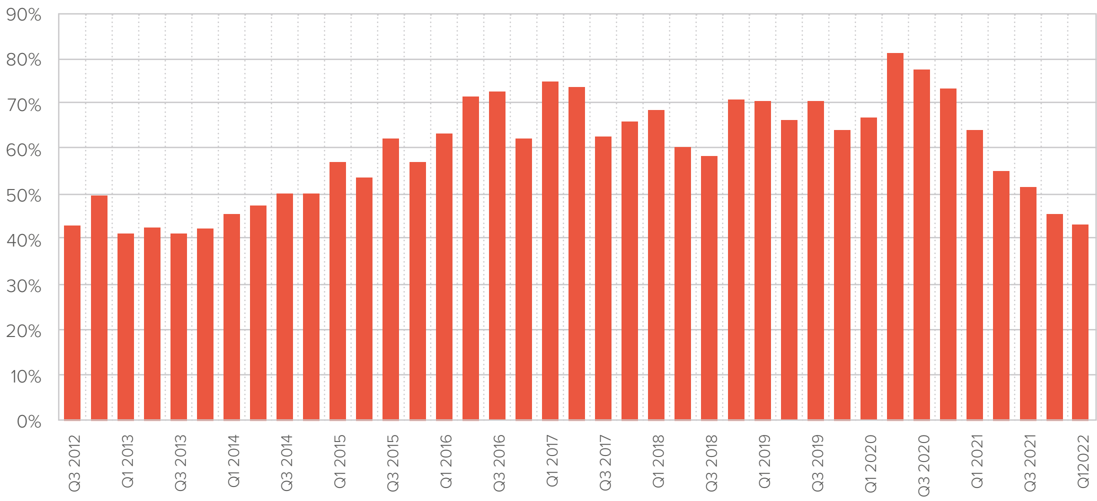
The proportion of small businesses applying for credit fell for a seventh consecutive quarter in Q1 2022. Just 9.1% of respondents stated that they had applied for credit for businesses purposes in the past three months, the lowest share in the SBI's history.

Investment hesitancy is likely one factor behind this further decline in credit applications. The economic landscape in 2022 so far has been characterised by volatility, making large financial decisions such as loan applications less palatable.

Moreover, borrowing costs have increased in recent months, with the Bank of England's rate rises feeding through into commercial lending markets. This is reflected in the significant fall in the portion of successful loan applicants being offered interest rates below 4%, and subsequent increase in the share being offered rates between 4% and 5%. All else being equal, higher rates make borrowing less attractive, acting as a further explanation for the falling rate of credit application.

The proportion of credit applications that were successful fell for a seventh consecutive quarter in Q1, reaching 43%, the lowest share since Q4 2013. This downward trend in part reflects the unwinding of pandemic support schemes, which had made it easier for businesses to access credit in the early stages of the pandemic.

Figure 15: Proportion of small businesses successful in their credit applications in the past three months
Source: FSB - Verve 'Voice of Small Business' Panel Survey



NEGATIVE VIEWS MORE PREVALENT ON CREDIT AVAILABILITY AND AFFORDABILITY

The proportion of small businesses with positive views on credit availability and affordability stood at 19.4% in Q1 2022. Meanwhile, 36.5% of businesses reported a negative view towards the availability and affordability of credit. The more pervasive negative sentiment towards credit also reflects the withdrawal of support schemes that had been in place to assist access to credit in the early stages of the pandemic. The recent rise in interest rates, making borrowing more expensive, will have also had an effect in this regard.

Figure 16: Indices of credit 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[2]

2 Due to methodological changes to the survey, the Credit Availability and Credit Affordability Indices have been superseded by a composite Credit Index, taking into account both of these factors.

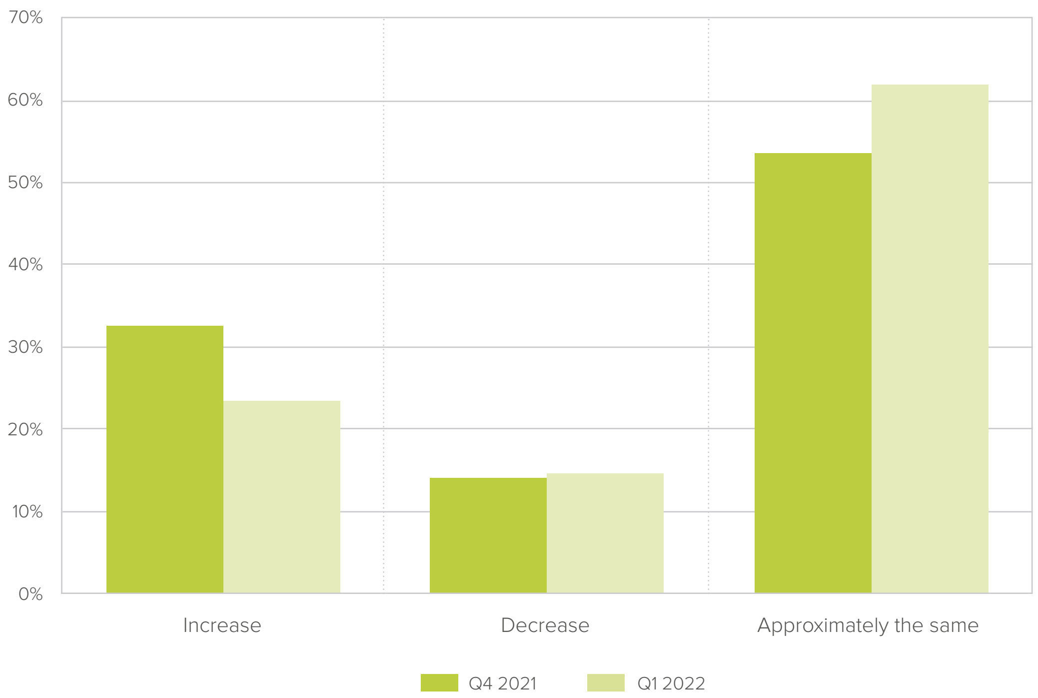
INVESTMENT

INVESTMENT AMBITIONS SLUMP AMID ECONOMIC UNCERTAINTY AND RISING BORROWING COSTS

Businesses' investment intentions slipped in Q1 2022, with just 23.4% of survey respondents expecting to increase their investment levels over the coming quarter. This marked the lowest reading since Q4 2020, when the economic landscape was still characterised by lockdown-induced uncertainty. Moreover, the proportion of businesses expecting to decrease their investment levels also increased in Q1 2022, reaching 14.4%. As such, the net balance of businesses expecting to increase their investment stood at just 8.9% in Q1, again the lowest reading since Q4 2020.

The fall in investment intentions in Q1 came amidst heightened economic uncertainty. Such uncertainty has been both international and domestic, with factors such as the conflict in Ukraine and mounting price pressures creating an unfavourable landscape for businesses. The decline in investment intentions also likely reflects the increased borrowing costs observed by businesses, as outlined in Section XIII, given that many small businesses fund their investment using credit. In terms of sectors, particularly weak investment intentions are seen amongst businesses in accommodation and food services, where just 17.1% of businesses expect to increase their investment levels over the coming quarter. These businesses have been amongst the most adversely affected over the two years of the pandemic so far and are thus less likely to have the funds with which to invest. The sector is also facing significant hurdles at present, notably in the form of labour shortages, so these businesses may be focusing on more immediate issues. Above-average investment intentions were seen amongst in the manufacturing, construction, and wholesale and retail sectors.

Figure 17: % of small businesses expecting to increase and decrease capital investment over next quarter, compared with previous quarter
Source: FSB - Verve 'Voice of Small Business' Panel Survey



METHODOLOGY

This report is based on the March research survey of FSB members carried out by Verve. 5,705 panel members were invited to take part in an online survey as well as through an open link shared with FSB members. Reminders were sent to all non-respondents. 628 responses were received, a response rate of 11% for the panel. The survey was then shared with the wider FSB members and received a total of 1,211 responses. The data are weighted by regional gross value added to match the profile of small businesses across the UK. The survey was undertaken between the 29th of March and 8th of April 2022.

SUMMARY DATA TABLE

	Q2 2020	Q3 2020	Q4 2020	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022
Small Business Index	-5.0	-32.6	-49.3	27.3	18.6	16.4	-8.5	15.3
Employment - previous three months	-19.0%	-15.2%	-15.5%	-3.5%	2.2%	-0.2%	3.3%	2.9%
Employment - coming three months	-7.9%	-6.7%	-3.8%	12.0%	14.0%	11.5%	9.8%	14.5%
Exports - previous three months	-52.8%	-35.2%	-16.0%	-28.4%	-19.8%	-20.0%	-12.3%	-5.3%
Exports - coming three months	-12.8%	-18.9%	-29.0%	-9.8%	-11.2%	-4.6%	-3.8%	10.4%
Credit availability - rated good or very good	38.3%	36.4%	29.3%	35.2%	30.0%	29.6%	26.4%	-
Credit availability - rated poor or very poor	34.9%	30.9%	30.5%	30.1%	35.0%	32.3%	36.0%	-
Credit affordability - rated good or very good	-	-	-	-	-	-	-	19.4%
Credit affordability - rated poor or very poor	-	-	-	-	-	-	-	36.5%

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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