Q4

FSB VOICE OF SMALL BUSINESS INDEX

QUARTER 4, 2023

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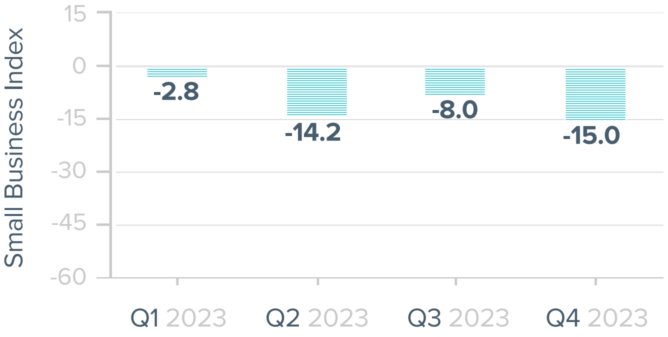
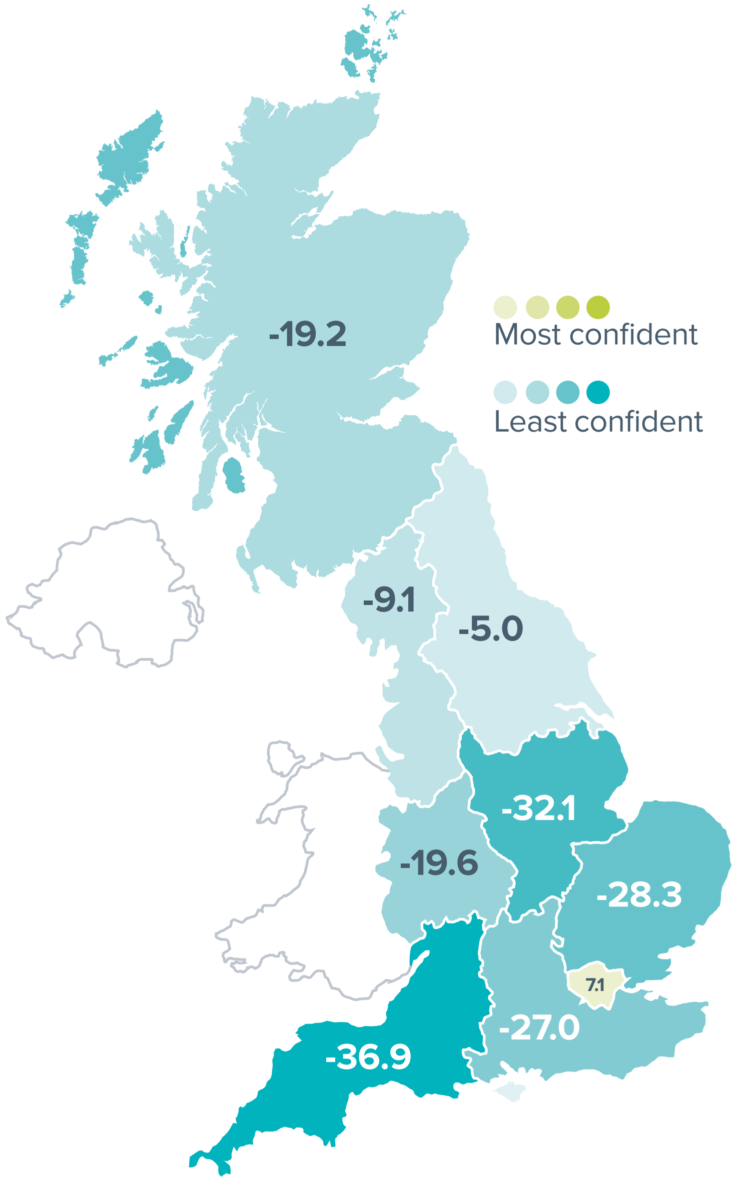
SBI Q4 2023

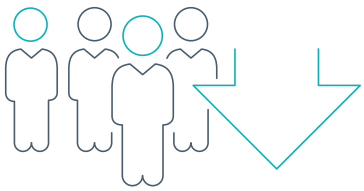
"Small business confidence slips back as economic momentum slows"





Please note: Sample sizes for Wales and Northern Ireland are insufficient for accurate reporting. The North East is combined with Yorkshire and the Humber to produce a combined region, due to low sample sizes for the former region.

Employment prospects fall for the next quarter



12%

of small businesses expect to **reduce employee numbers in Q1 2024**, while only **10%** expect to grow staffing levels

Concern as labour costs grow

27%

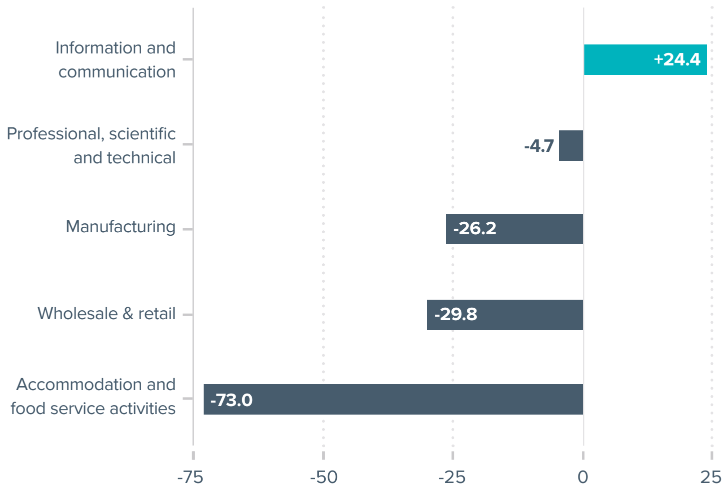
of small businesses say **labour costs are a barrier to their growth aspirations**, up **6.2%** from Q3

Revenue levels stagnated, despite 'golden quarter'

40%

of small businesses reported their **revenue levels decreased over the last 3 months** compared to **34%** reporting an increase

Small business confidence by sector



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FSB FOREWORD

It wasn't the end to the year that many small firms were hoping for. Small hospitality and retail businesses in particular pin their hopes on robust trading in the so-called 'golden quarter', which has traditionally given them enough of a cash buffer to make it through the leaner months at the start of the new year, when the festive season's bills hit and people tend to rein in their spending.

However, the ground which had been made up in terms of small businesses' confidence levels between the second and third quarters was lost once again in Q4. The final quarter's headline confidence measure of -15 points was on a par with the -14.2 points recorded in Q2, after Q3's recovery to -8 points. It's the seventh negative reading in a row, and the worst since the same quarter in 2022, when the energy price crisis was at its height.

The sectoral results show that accommodation and food services saw by far the largest drop in confidence among the major industries, going from -31.1 points in Q3 to a highly concerning -73 points in Q4, Retail also fell, although thankfully by a lesser amount, from -22.8 to -29.8.

It's disappointing that the tentative signs of stabilisation on some measures of small business performance in Q3 did not persist, by and large, into the final quarter. Measures including exports showed a higher net negative in Q4 than in Q3, with a modest rise in the proportion of small exporters reporting an increase in volumes (up from 24.4% in Q3 to 26.1% in Q4) more than offset by the proportion saying export volumes fell (36.9%, up from 26.9%).

Employment levels are another sign of contraction rather than the growth we'd like to see, with one in ten small firms (10.3%) expecting to grow employee numbers over the next quarter (down from 11.7% in Q3), but with over one in nine (11.5%) expecting to reduce staffing numbers (up from 9.1% in Q3). Labour costs also saw the largest increase in citations as a potential barrier to growth, mentioned by a fifth of firms in Q3 (21.2%), but over a quarter in Q4 (27.3%). Labour costs were also the second-most cited cause of cost increases between Q4 and the same quarter in 2022, up from 42.8% in the previous survey to reach 45.7%.

The growing cost of employment underlines the need for the Government to act at the Spring Budget to reduce the burden of costs which fall on employers, through an increase in the Employment Allowance. When it was first brought in following FSB's campaigning, it was designed to cover the National Insurance contribution costs to the employer of four full-time employees on the National Living Wage. However, the rise in the National Living Wage in April will leave it covering only three employees' NICs costs, if its current level is not increased.

Reported revenues were comparable to Q3, with a third (33.8%) of small firms saying their revenues increased over the period (Q3: 33.5%), while 39.8% noted a drop in revenues (Q3: 39.4%). However, given the heightened financial expectations placed on the 'golden quarter', this is one measure where we would have hoped to see an uptick, to allow small firms in consumer-facing sectors to build up something of a cash cushion to tide them over the traditionally frugal post-Christmas period.

It's not therefore unexpected for forward-looking revenue expectations to be more subdued than in the previous quarter, but it's still an indication of the precarious position many small firms find themselves in. Almost exactly the same proportion of small firms expect their revenues to grow over the first quarter of this year (31.6%) as expect them to decrease (32.0%), down from Q3's findings of over a third expecting higher sales volumes (35.4%), with three in ten (30.8%) bracing for a decrease.

Inflation fell over the final three months of the year, although the small increase between November and December is a warning sign that we are not yet out of the woods. This was reflected by a slight easing in the proportion of firms saying their cost of doing business was higher than in the same period a year ago, which was 82.5%, compared with 86% in Q3. Those saying their costs had increased significantly fell from 28.9% in Q3 to 24.7% in Q4 – an encouraging sign. Utilities are still the most-cited cause of cost changes, showing that the lingering effects of the energy price crisis are still very much a live concern, followed by labour costs, as previously noted, and inputs at 41.6%.

Tina McKenzie,
Policy Chair

The Bank of England's decision to pause its series of base rate hikes following the uplift to 5.25% in September has at least not made matters worse for small firms carrying index-linked debts, or those reliant on consumer spending. However, given that rates remain high, and 52% of small firms rate the availability and affordability of new finance as poor, we are looking to the Bank to cut the base rate sooner rather than later, especially given that the UK fell into a technical recession as of December 2023.. With the proportion of small firms predicting that they will shrink over the coming year going from one in eight (12.7%) in Q3 to over one in seven (15.0%) in the final quarter of 2023, the economic growth engine among small firms shows worrying signs of stalling.

Given this rather unencouraging picture, the Government needs to get serious about measures to spur investment and expansion among small firms. We've set out our vision for an overhaul of VAT – the frozen turnover threshold should go up to at least £100,000, from its current level of £85,000, to give more room to breathe for small firms approaching the threshold. As long-awaited import checks on EU goods roll out over the course of the year, small firms are vulnerable to increased margin pressures and supply chain disruption, underlining the need for the Government to step up efforts to help small firms adapt to the costs of international trade. We're also looking forward to the introduction of the Single Trade Window later this year, so small firms can benefit from a 'once and done' approach to the collection of the data they need to provide to export or import, while international visitors to the UK should be encouraged to splash out via the reintroduction of tax-free shopping.

Q4's Small Business Index is full of warning signs, but the overall situation is not catastrophic, and there is certainly scope for a turnaround in small firms' prospects. Getting the small business community back on the road to growth will be key to reviving the economic fortunes of the UK as a whole.

ECONOMIST'S VIEW

Our finding that the FSB Small Business Index deteriorated in Q4 is not surprising, but remains disappointing nonetheless. This quarter's data caps off a year of relatively shallow declines in expectations of small business performance. This aligns with the broader economic picture for 2023, which was one of gradual decline in momentum, taking us from sluggish growth to a recession in Q4.

The economic slowdown is partially a result of higher interest rates, a necessary action by the Bank of England to tackle the other main driver of the slowdown: high inflation. We are at least seeing restrictive monetary policy lead to reduced price pressures, with the lowest balance of small businesses seeing higher costs over the past three months in Q4 since Q1 2021.

While input and fuel cost pressures for small businesses continue to ease, labour costs are becoming an increasingly strong driver of overall cost growth. Nominal pay growth has peaked and is coming down, but the labour market remains tight by historical standards and that continues to apply upward pressure on pay.

With headcounts expected to continue to fall across small businesses in the coming three months, we expect only a marginal loosening of labour market conditions over this period of economic weakness. It is increasingly clear that, although labour shortages continue to ease, the UK economy faces a more severe structural problem post-covid than it did pre-pandemic. This will no doubt be a major barrier to growth for years to come.

Another issue that small businesses have raised as a significant barrier to growth is the tax burden. This is indeed the second most cited topic this quarter in relation to growth barriers, after the domestic economy/consumer demand. It is also increasingly cited as a main source of cost pressure. This is unsurprising given the impending increase in Corporation Tax, which comes on top of already stifling taxes like VAT, business rates and National Insurance. Despite some positive movements on tax in the Autumn Statement, this set of results makes clear that small businesses see the overall tax burden getting worse, not better.

One silver lining to the labour cost challenge is that it may lead to firms' willingness to invest more, particularly where it may help to improve worker productivity. Indeed, we find that small businesses expect to increase investment over the next three months on net, at the strongest rate since late 2022. Higher investment is a major contributor to higher productivity, which is the only sustainable way to improve standards of living in the long term. Therefore, it is great to see a quarter of small businesses point to plans to increase investment spending in early 2024.

This is one sign that further proves what we knew already: small businesses are resilient. Indeed, nearly half have ambitions to grow over the next year, with over a third more expecting to remain about the same in that time. And small businesses are right to feel confident in an improving economic picture over the current calendar year. With inflation easing gradually, the Bank should be able to start cutting rates from the middle of the year, allowing the economy to establish some positive momentum. Despite the ongoing risk of additional headwinds, both from a lack of progress in fighting inflation domestically or from geopolitical tensions abroad, small businesses can hope to end 2024 in better standing than they started.

Kay Daniel Neufeld, Head of Forecasting and Thought Leadership

Q4

FSB EXECUTIVE SUMMARY

Key findings this quarter:

- **The FSB Small Business Index (SBI) decreased to -15.0 in Q4 2023** from -8.0 in Q3, indicating that SMEs expect a faster decline in business performance than they did last quarter. This represented the SBI's seventh consecutive negative reading.
- These results are aligned with the downbeat picture for the wider UK economy. **With GDP having contracted in Q3 and Q4, the UK economy has formally entered a recession.**
- **The only UK region in which small businesses expected performance to improve over the next three months in Q4 was London.** Meanwhile, four regions reported a further deterioration in confidence levels, while the score for one region (the North West) entered negative territory in Q4.
- **Information and communication was the only sector in which the index improved in Q4,** moving into positive territory. Accommodation and food services and manufacturing were among the sectors in which performance was expected to deteriorate further over the coming three months.
- **Small businesses reported falling revenues in Q4, with a net balance of -6.0% in Q4 2023.** This is a slight deterioration from the -5.9% net balance in Q3 and marks the seventh consecutive negative quarterly reading. Small businesses broadly expect minimal change in their revenues over the next three months (-0.4% net balance).
- **The value of exports to SMEs also fell more sharply in Q4 (net balance of -10.8%) compared to Q3 (-2.6%).** This marked the nineteenth consecutive negative quarterly reading. SMEs expect a broadly flat performance over the next three months (0.8%).
- **In Q4, the net balance of small businesses reporting an increase in their operating costs fell to 79.0%.** This is the lowest reading for this metric since Q4 2021, reflecting the continued deceleration in inflation.
- **Small businesses reported falling employee numbers in Q4 (net balance of -4.5%) and expect a further decline over the next three months (-1.2%).** This is the seventh consecutive quarter that the small business employment numbers have been in negative territory. This is the first negative expectation in employment numbers over the next three months since Q4 2020.
- **The share of small businesses aspiring to grow over the coming year decreased for the second consecutive quarter to 48.2% in Q4,** signifying a broad reduction in confidence over the economic landscape.
- **A three-year high of 15.5% of small businesses reported that they applied for credit in Q4 2023.** This was up from 12.0% recorded in Q3 2023, ending three quarters of consecutive decline.
- Perceptions of credit affordability and availability continued to worsen in Q4. **The credit index remains deeply in negative territory at -32.0, the joint weakest value since the series began in Q1 2022.**
- **The net balance of small businesses expecting to increase their investment increased to 8.2% in Q4, up from 5.7% in Q3.** These changes come despite the Bank of England holding the bank rate at 5.25% since September 2023 and not being expected to cut the rate until Q2 2024.

UK MACROECONOMIC OVERVIEW

UK economy enters technical recession

The latest data from the Office for National Statistics (ONS) show that UK GDP fell by 0.1% in December. This marked a return to contraction following November's growth of 0.3%. Whilst monthly activity fell by 0.1% for December, GDP activity in the three months to December fell by 0.3%, bringing the economy into a technical recession.

The manufacturing sector has struggled over this period, declining by 0.9% in the three months to December. Manufacturing output has been curtailed by various supply-side headwinds, notably higher interest rates and continually elevated, albeit falling, input costs. Meanwhile, the construction sector witnessed a decline of 1.3% in the three months to December. In addition to experiencing headwinds similar to those in the manufacturing sector, construction has also contended with recently poor weather conditions, which have led to delays in planned work.

With the UK in a technical recession, it is clear that economic performance remains fragile, with limited scope for near-term growth. It is anticipated that growth will be similarly weak in 2024, as the economy continues to contend with various headwinds, including tighter monetary policy and lingering inflationary pressures. Further weak values on the Small Business Index (SBI) are likely as a result.

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

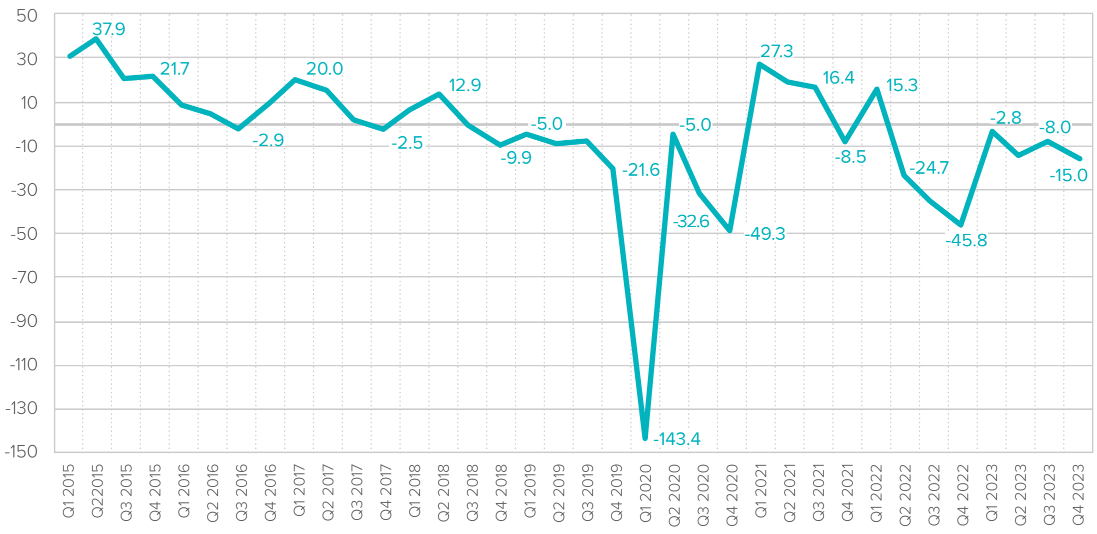
Small Business Index declines as net pessimism continues to prevail

The Small Business Index (SBI) decreased to -15.0 in Q4 2023. This marked a return to contraction, following an improvement in Q3. Amidst the quarterly fluctuations, the SBI has now recorded a negative reading for seven consecutive quarters. A negative score signifies that the share of businesses expecting their performance to worsen over the coming quarter outweighs the share expecting their performance to improve.

Continued negative readings of the SBI reflect broader macroeconomic vulnerabilities. Indeed, the persistent weakness mirrors the UK's recent weak growth trajectory, with output hampered by headwinds such as elevated interest rates and reduced household spending power. The near-term economic outlook is an anticipation for this trend to continue.

Official confirmation that the UK economy has entered a recession is likely to coincide with further negative values on th SBI.

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 are given the following weightings: 'much improved' +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

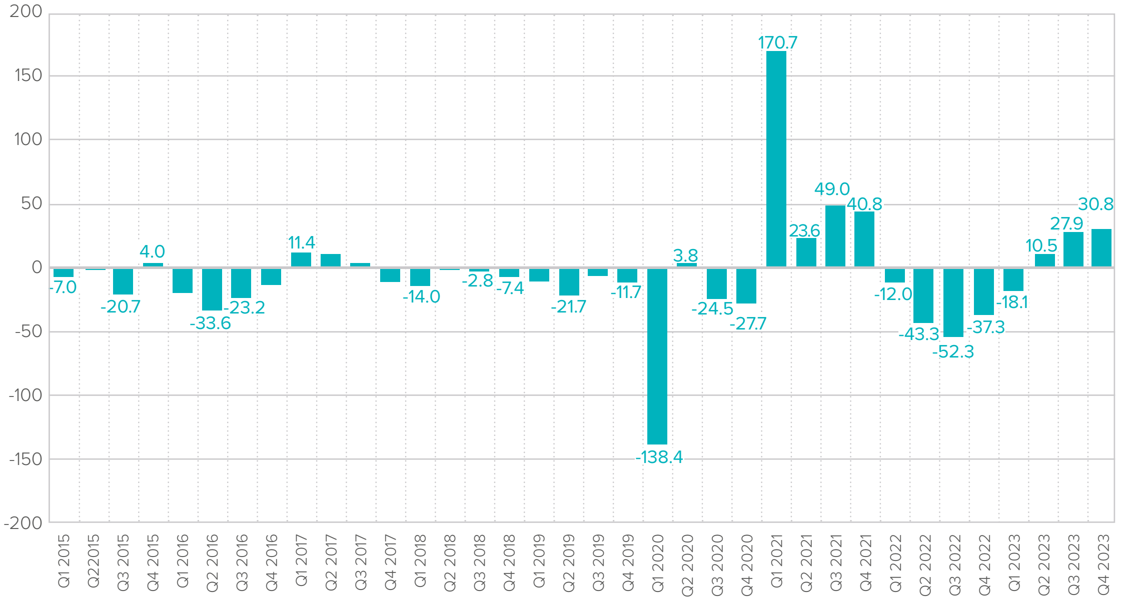
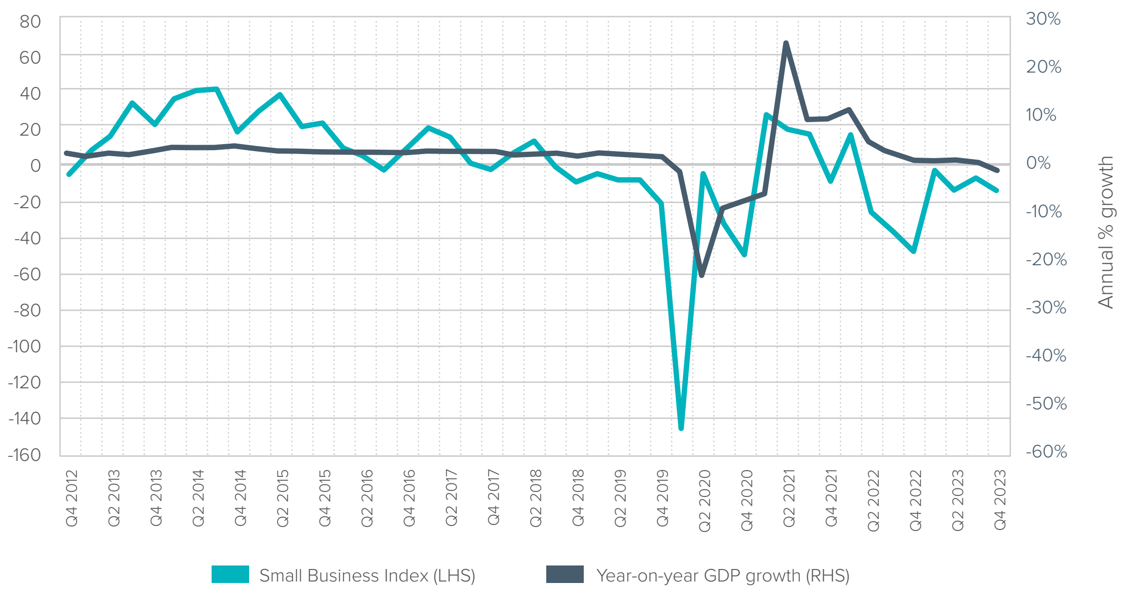


Figure four: UK SBI against year-on-year UK GDP growth
Source: ONS, FSB - Verve 'Voice of Small Business' Panel Survey



REGION AND NATION SMALL BUSINESS INDICES

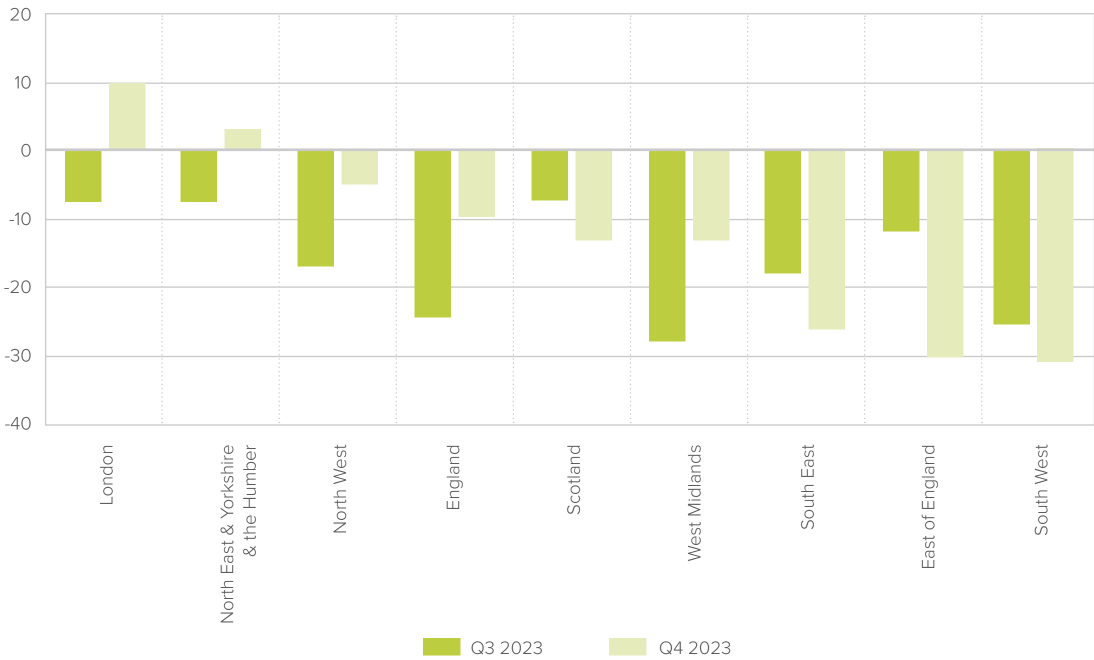
SMALL BUSINESS INDEX SCORES REMAIN NEGATIVE FOR THE MAJORITY OF REGIONS AND NATIONS IN Q4

Only one UK region saw a positive reading on the regional SBI in Q4 2023, while the remainder sat in negative territory.[2] This means that for all but one region the proportion of small businesses expecting a worsening in performance in the coming quarter still exceeds the proportion expecting an improvement. Six regions saw a worsening on the measure in Q4 when compared to Q3 2023.

The only optimistic region in Q4 was London, with an SBI score of 7.1. Notably, the two best performing industries on the sectoral SBI were information and communication, and professional, scientific and technical activities. London has a large concentration of businesses within both these sectors, partially explaining the positive outlook. Indeed, information and communication was the only major sector to produce a positive SBI score in Q4.

The most pessimistic region in Q4 was the South West, with an SBI reading of -36.9. A majority, 56.6%, of businesses in the South West expect their performance to worsen in Q1 2024 relative to Q3 2023. Further, the region had the lowest share of businesses expecting performance to pick up amongst all regions of the UK, at 19.7%. The East of England saw the next weakest SBI score in Q4, at -28.3. This was driven by 55.0% of businesses expecting performance to worsen, as well as a below-average share of businesses expecting performance to pick up.

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



2 Sample sizes for Wales, Northern Ireland, and the East Midlands are insufficient for accurate reporting. The North East is combined with Yorkshire and the Humber due to low sample sizes for the former region.

SMALL BUSINESS SECTOR INDICES

INFORMATION AND COMMUNICATION BUSINESSES ARE THE MOST OPTIMISTIC OVER THE COMING THREE MONTHS

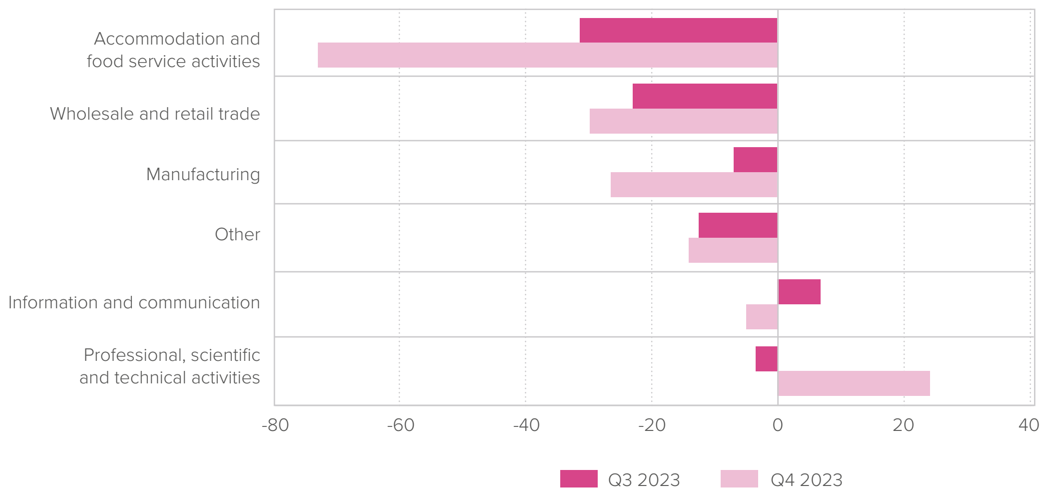
All but one major industry saw a worsening of their SBI reading in Q4 2023 relative to Q3, mirroring the trend observed in the headline SBI index. Further, only one major sector recorded a positive reading. The broadly negative set of scores demonstrates that businesses across most sectors are concerned about their performance over the coming quarter.

For a second consecutive quarter, the weakest sentiment was observed amongst businesses in accommodation and food services, with an SBI reading of -73.0. This score represented a notable worsening when compared to the already negative reading of -31.1 observed in Q3. Meanwhile, the wholesale and retail trade recorded the second-weakest sentiment amongst major sectors in Q4, with an SBI reading of -29.8. The continued negativity amongst both these industries largely reflects demand-side headwinds. Indeed, the disposable income of consumers has been hit particularly hard by the cost-of-living crisis and higher interest rates, which has consequently translated into weak consumer demand. With this trend set to continue in the near term, businesses in accommodation and food services, and the wholesale and retail trade, are broadly pessimistic about their performance over the coming three months.

Manufacturing recorded a similarly negative SBI reading in Q4, at -26.2. The score likely also reflects a downturn in consumer prospects, as well as a decline in business confidence.

Information and communication was the only major sector to record a positive SBI score in Q3, at 24.4. This comes on the back of the sector being a primary driver behind robust economic growth in November, and delivering a smaller but still positive contribution in December, according to the ONS.

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



FINANCIAL PERFORMANCE

SMALL BUSINESSES REPORT FALLING REVENUES FOR SEVENTH CONSECUTIVE QUARTER IN Q4

The net balance of small businesses reporting revenue growth over the previous three months stood at -6.0% in Q4 2023. The negative figure means that the number of small businesses reporting a decrease in revenue levels over the last three months outweighed the number reporting an increase. This marked the seventh consecutive negative reading for the revenue net balance figure.

On a sectoral basis, accommodation and food services recorded the weakest revenue net balance figure in Q4, at -31.8%. Meanwhile, wholesale and retail trade had the second most negative balance, at -8.1%. These scores likely reflect the demand-side constraints faced by both these industries, with reduced spending power impacting consumer activity. Manufacturing also had a negative net balance of -3.2%, reflective of the supply-side difficulties the industry has faced. In contrast, professional, scientific and technical activities, and information and communication were the only major sectors with positive net balances, of 6.3% and 4.1%, respectively.

Both these sectors are less affected by demand-side headwinds, given that businesses are less consumer facing. Further, supply-side constraints are less of a factor, given that such businesses tend to be less input intensive.

In terms of regions, the weakest net balances were observed for the South West at -19.5%. Only two regions recorded positive net balances: the North West and London, with scores of 9.0% and 7.1%, respectively.

Looking ahead, small businesses expect revenue to be broadly flat, with a slight net balance of -0.4% anticipating a revenue decline over the next three months. This downbeat outlook is reflective of the broader macroeconomic vulnerabilities facing the UK coming over the coming quarter.

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

EXPORT EXPECTATIONS BECOME GLOOMIER, REFLECTING SUBDUED GLOBAL ECONOMIC ACTIVITY

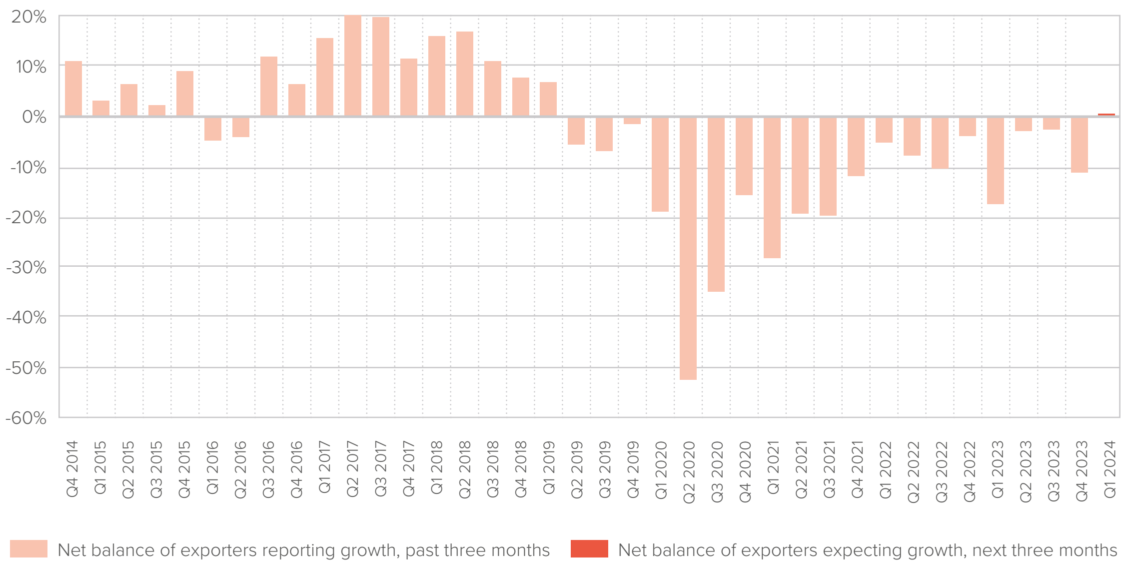
A net balance of -10.8% of exporting businesses said that the value of their exports increased in Q4 2023. This is a deterioration from the -2.6% net balance in Q3 and marks the nineteenth consecutive negative quarterly reading. Looking ahead, a net balance of 0.8% expect export value to grow in Q1 2024. However, optimism among exporters has diminished, as the current reading reflects a decrease from the previous quarter's forward-looking figure, which stood at 7.3%.

The latest official data show that the value of UK exports decreased by 1.4% in the three months to November compared with the three months to August. Whilst both exports of goods and services recorded a fall, the fall in exports of goods was higher than that of services. The overall weak global outlook, particularly in the EU which houses the UK's largest trading partners, has created subdued demand for UK imports.

The performance of sterling will have likely played an influential role in the net balance figure. Following a poor performance against the dollar in September, sterling has rebounded in the subsequent months. According to the effective exchange rate index released by the ONS, the pound is higher than it was a year ago in December. This positive trend is attributed to the slower-than-expected deceleration in inflation, creating a market expectation that a rate cut by the Bank of England in the short term is unlikely.

The overall subdued sentiment among exporters is rooted in the realisation of a slowdown in the global economy. This slowdown is a consequence of the impacts of co-ordinated monetary policy tightening campaigns across the world. There is a risk that geopolitical tensions will continue to mount, at the expense of world trade.

Figure eight: Changes in value of exports over the previous three months and expectations for the 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 BUSINESSES FACING INCREASED COSTS RISES HITS RECORD LOW

The net balance of small businesses reporting an increase in operating costs fell to 79.0% in Q4. This is the lowest reading for this metric since Q4 2021. This decline comes amidst an ongoing deceleration in inflation throughout 2023, ending the year at 4%, under half of where it was at the start of the year (10.1% January 2023).

The deceleration in inflation in October was driven by the fall in fuel and energy prices which recorded a price fall of 15.7% on the year. November continued the trend of deceleration with the price fall being driven by the transport category with transport prices falling by 1.5% on the year. The easing of price pressures in these categories is noticeable as the share of businesses selecting fuel as a main source of rising costs fell by 3.5% points from the previous quarter.

Utilities continue to be the most cited source of changing business costs, with the percentage of businesses selecting it as a main source of changing business costs increasing by 5.2 percentage points in Q4 to reach 62.5%. Labour comes in as the second most cited source, up 2.9 percentage points to 45.7%. This is reflective of tight labour market conditions. Despite there being a slowdown in average total pay, the growth rate remains high by historical standards. The path of wage growth will be vital for the path for price growth, and the Bank of England will be keen to see the broad trend of deceleration continue before cutting interest rates.

Financing has remained a notable source of cost pressure throughout the year. However, the number of businesses selecting this as a source of a changing business cost has been reducing. This is in line with the BoE holding its rates since its September meeting. Despite the sticky inflation, Cebr anticipates that the peak in the monetary policy tightening campaign has been reached, with the Bank of England likely to commence rates cuts in the middle of the year.

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

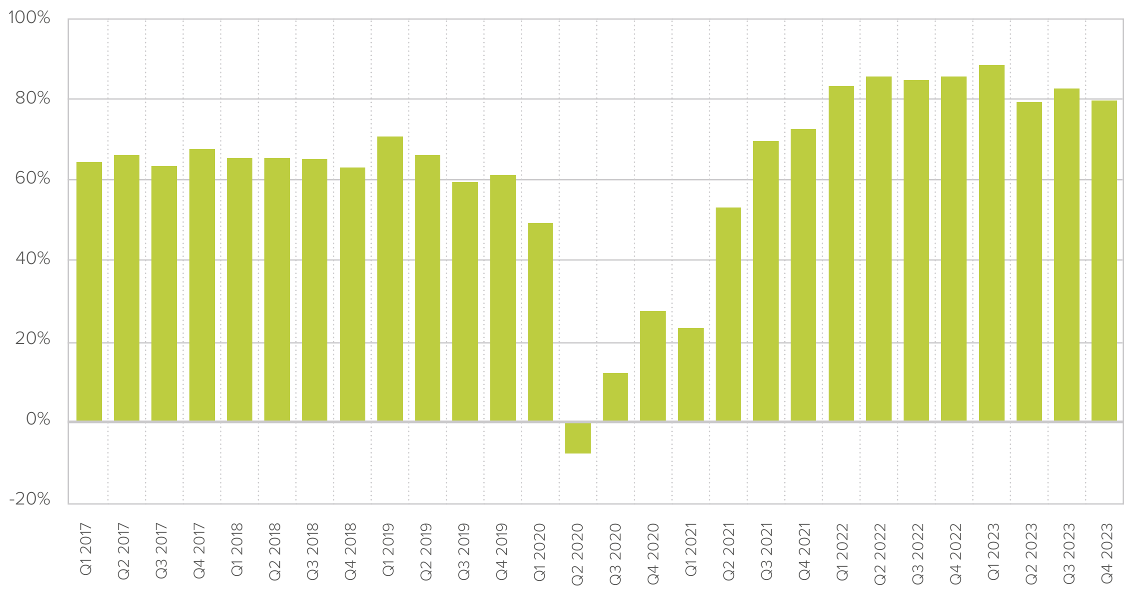
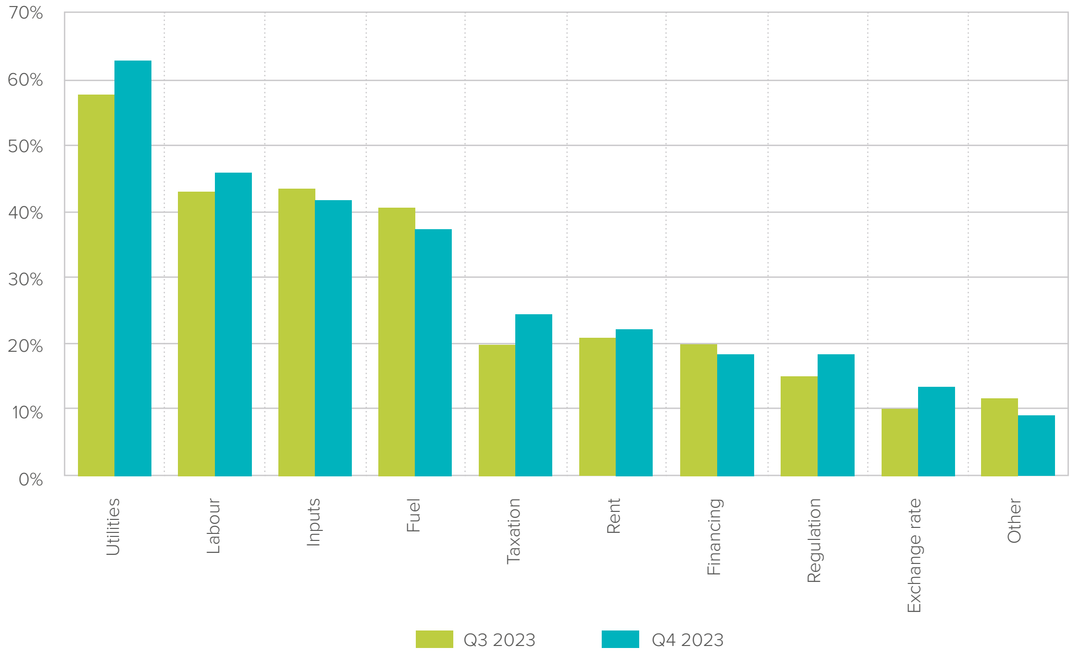


Figure 10: Main causes for changing business costs (Respondents could select multiple answers)
Source: FSB - Verve 'Voice of Small Business' Panel Survey



EMPLOYMENT

SMALL BUSINESS EMPLOYEE NUMBERS CONTRACT FOR QUARTER FOUR

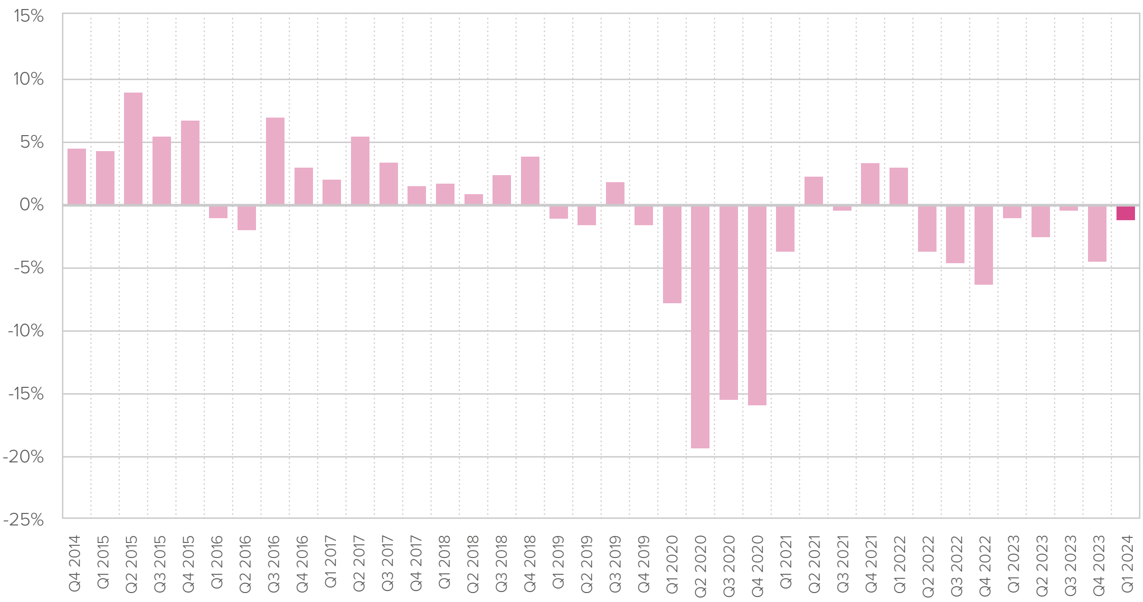
A net balance of -4.5% of small businesses reported growth in employee numbers in Q4. The negative reading means that the number of businesses expanding their workforce was outweighed by the number of businesses reporting a contraction in headcount. This marks a seventh consecutive negative reading on this metric.

The findings from the survey are in slight conflict with the latest ONS data which recorded an unemployment rate of 3.8% in the three months to December, a decline from the previous three months, and an employment rate of 75.0% in the three months to December, a slight fall of 0.8 percentage points relative to the previous three months. However, these are experimental labour market figures released in light of methodological uncertainties in the Labour Force Survey. The slowdown in the number of vacancies and wage growth is much more in line with the survey data as it signals an unwinding of the labour market.

The negative reading aligns with the slowdown in the overall economy. UK GDP recorded a contraction in output by 0.1% in Q3 and 0.3% in Q4, with negative or near-negative growth expected over the coming quarters. This ongoing slowdown is reflected in the employment metric. Negative headcount growth is expected to continue in Q1 2024, albeit at a slower rate, with a net balance of -1.2%.

On a sectoral basis, the worst net balance score was seen in accommodation and food services, at -27.3%. This sector continues to face the impacts of weaker consumer activity amidst a weak economic growth environment, which has reduced the demand for labour within the sector. In contrast, the sector with the strongest net balance score is the information and communication sector, at 14.3%. .

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

SMALL BUSINESSES ARE LESS OPTIMISTIC ABOUT GROWTH PROSPECTS OVER THE COMING YEAR

The share of small businesses aspiring to grow over the coming year decreased for the second consecutive quarter to 48.2% in Q4. The percentage who expected to shrink rose to 15.0%, from 12.7% in Q3. There was an above-average share of small firms planning to close their business in the next 12 months for the third consecutive quarter, at 3.4% (the average is 2.5%).

Looking at businesses by sector, those in information and communication continue to be the most upbeat, with 56.0% of the respondents hoping to grow over the next 12 months, possibly driven by the sector's aforementioned reduced dependence on consumer activity. However, this still represents a decline in aspiration levels from last quarter, when 66.2% of firms hoped to grow.

At the opposite end of the spectrum, businesses in accommodation and food services activities were the least optimistic about growth over the coming year, with only 31.6% of respondents expecting positive developments. The net balance for the sector in Q4 stood at –3.9%, indicating that the number of businesses expecting contraction outweighed those hoping for growth. Being heavily reliant on non-essential consumer activity, this sector is particularly susceptible to the impacts of a recession.

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

SMALL BUSINESSES FACE SEVERAL ECONOMIC HEADWINDS

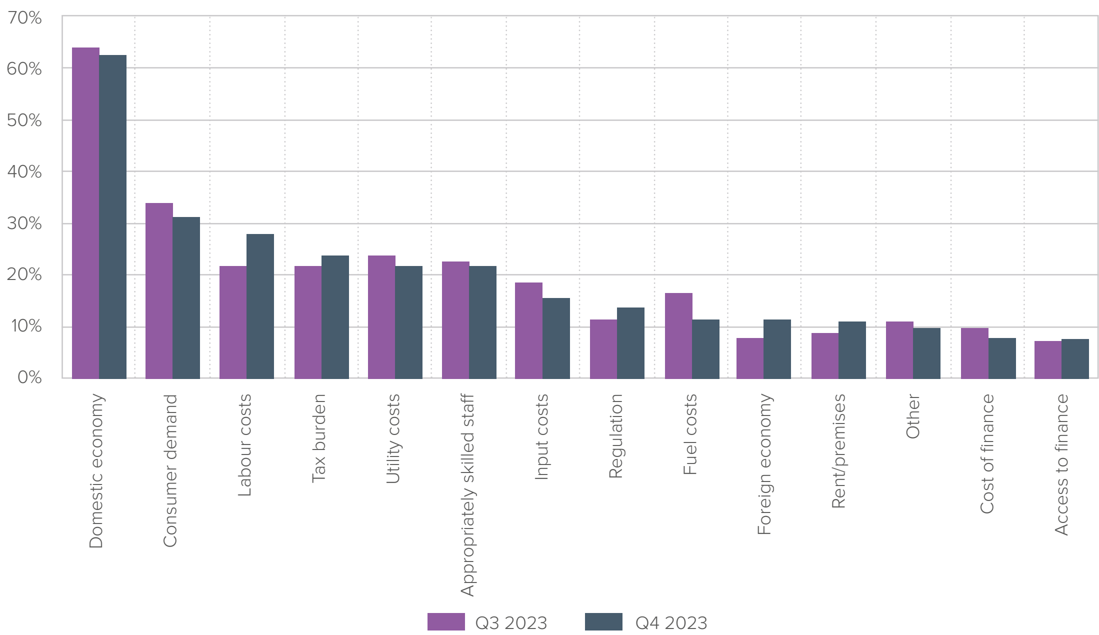
Among businesses expecting to grow over the next 12 months, the domestic economy was the most frequently cited potential barrier to such growth, selected by 61.8% of respondents. This aligns with the contraction of GDP in Q3 and Q4, and our macroeconomic view for the next twelve months.

Consumer demand was the second most chosen barrier to growth for the third consecutive quarter, with 30.7% of small businesses selecting it. However, this figure has slightly decreased from the previous quarter, when 33.3% of small businesses identified it as a growth obstacle. This decline perhaps reflects the impact of easing inflation and improving consumer confidence in recent months, coupled with elevated real wage growth which stood at 1.4% in the three months to December.

The selection of labour cost as a barrier to growth increased from the previous quarter, with 27.3% of respondents choosing it, up from 21.1% in Q3. This Q4 reading represents the highest number of businesses citing labour cost as a barrier since Q2 2019. Recent data from the ONS indicates a slowdown in UK wage growth in the three months to December with annual growth in total pay at 5.8%, compared to 6.5% in the prior three-month period. Nevertheless, these rates remain high by historical standards. Elevated labour costs pose a barrier to growth as they have the potential to contribute to second-round inflationary effects, leading to increased overall costs that could impede investment and growth. This aligns with more businesses citing labour costs as a factor influencing changing business costs as well.

The number of businesses citing foreign economies as a barrier to growth also increased from the previous quarter, reflecting the current unstable and troubling political climate. This is most likely to impact export-oriented businesses, but the trickle-down effects will have an overall effect on all businesses. Tax burden and regulations were also identified by more businesses as constraints to growth compared to the previous quarter.

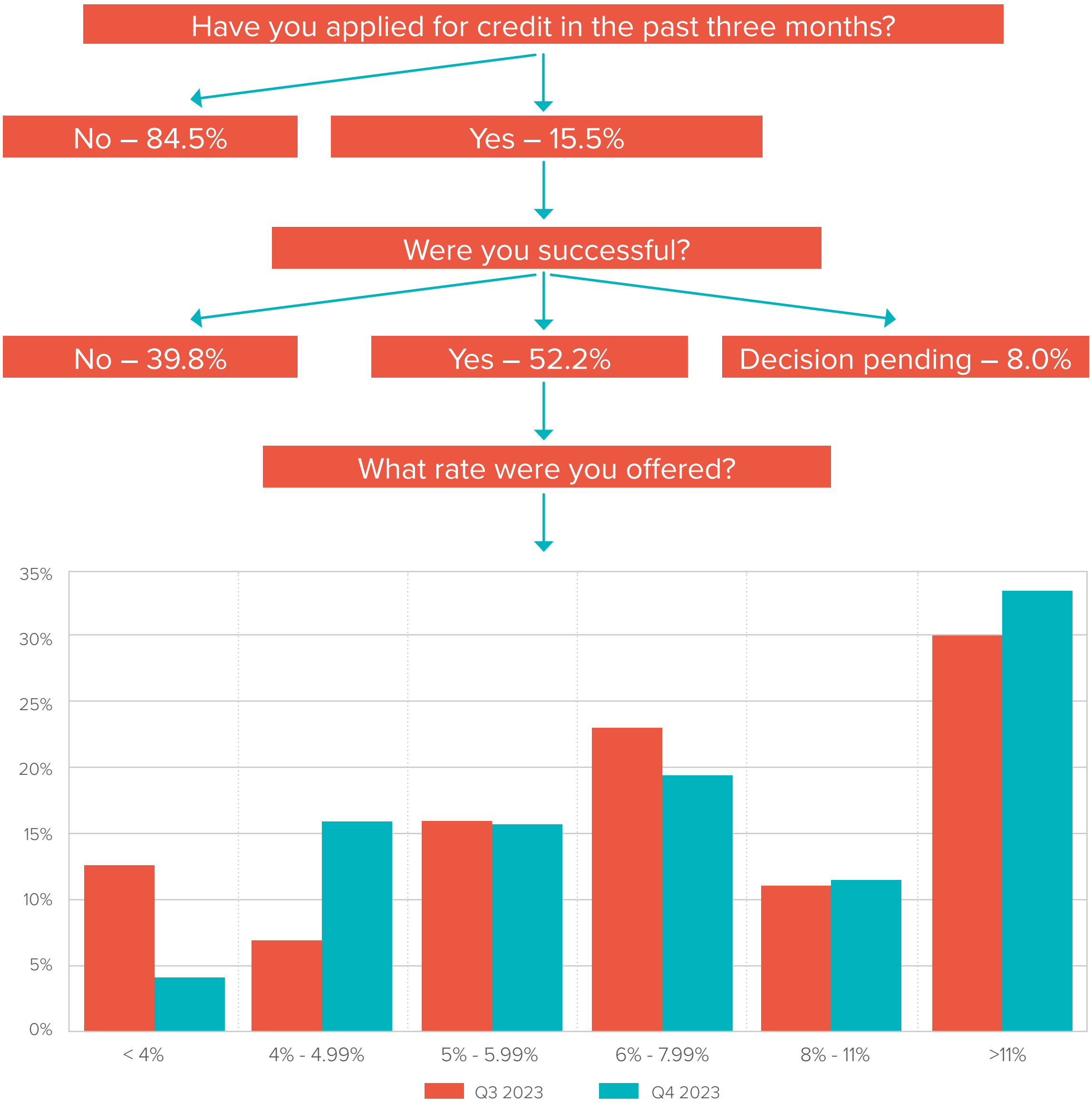
Figure 13: Potential barriers to achieving growth aspirations – multiple answers possible
Source: FSB - Verve 'Voice of Small Business' Panel Survey



CREDIT

SHARE OF SUCCESSFUL CREDIT APPLICANTS FALLS FOR THE FIRST TIME AFTER INCREASING FOR THREE CONSECUTIVE QUARTERS

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.



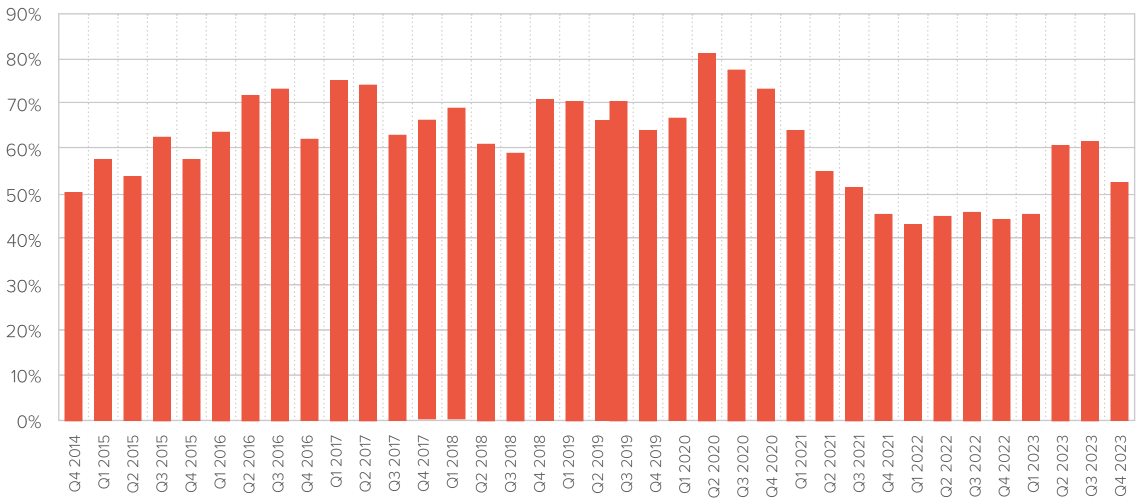
A three-year high of 15.5% of small business reported that they applied for credit in Q4 2024. This was up from the 12.0% recorded in Q3 2023. The uptick in the share of businesses reporting credit applications comes in the wake of the Bank of England's decision to hold interest rate increases since September.

However, the surge in applications has not translated into a higher success rate. The number of successful credit applications decreased to 52.2% in Q4, marking the first decline in this metric after increasing consecutively for three quarters. This may indicate increasing concerns over borrowers' ability to repay loans, which could be a sign of increased financial strain for small businesses.

Amongst sectors, businesses in wholesale and retail were the most likely to report credit applications in Q4, with this being the case for 16.8% of the respondents. At the other end, those in information and communication were the least likely to have made a credit application in Q4.

The share of successful credit applications being offered an interest rate less than 4% dropped drastically in Q4 to 4.2%, from 12.7% in Q3. Meanwhile, the share of successful applications being offered a rate higher than 11% increased to 33.4%, up from 30.1% in Q3, representing the highest value since the survey started in 2014.

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



BUSINESSES' PERCEPTIONS OF CREDIT AVAILABILITY AND AFFORDABILITY MOVES FURTHER INTO NEGATIVE TERRITORY

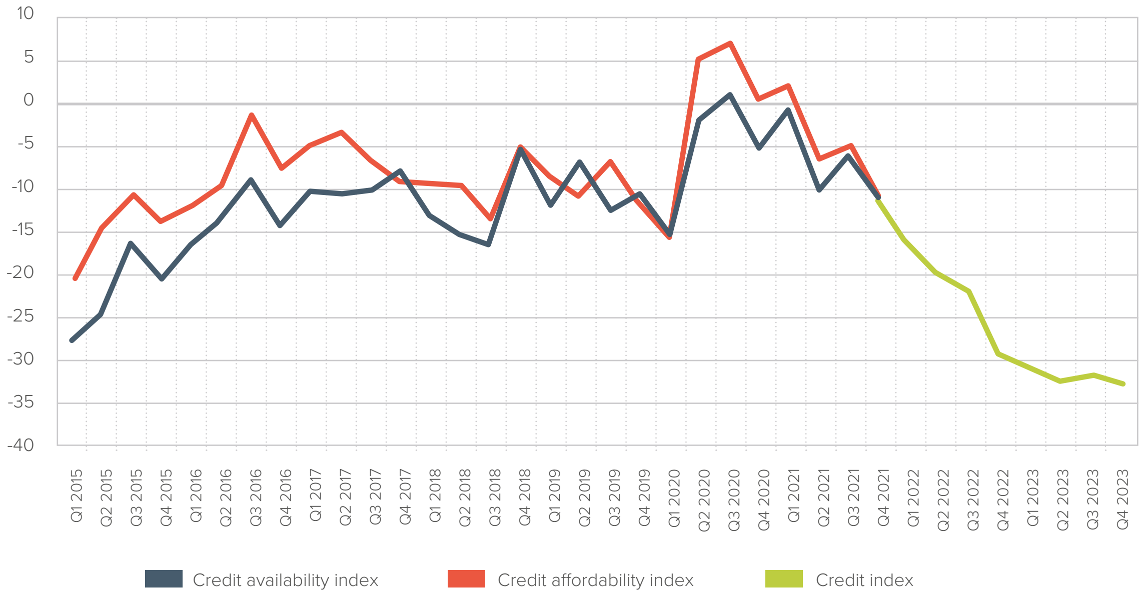
Perceptions of credit affordability and availability worsened in Q4. The credit index worsened by 0.7 points on the quarter, pushing the index deeper into negative territory. The index stood at -32.0 in Q4 – the weakest value on record.

The proportion of businesses expressing a 'positive attitude' on credit availability and affordability remained stable compared to the previous quarter. However, the share of respondents rating affordability and availability of credit as 'very affordable' dropped by 1.0 percentage points in Q4.

The proportion of small firms with a 'negative attitude' towards credit availability and affordability marginally decreased on the quarter. The negative attitude includes those who consider affordability and availability as either 'quite unaffordable' or 'very unaffordable'. The share of respondents rating affordability and availability of credit as 'very unaffordable' increased by 1.5 percentage points.

Therefore, while the overall positive attitude remained unchanged and the negative attitude decreased for the quarter, the shifts at the extremes of the spectrum are what led to a deeper decline of the overall metric further into negative territory.

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



3 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

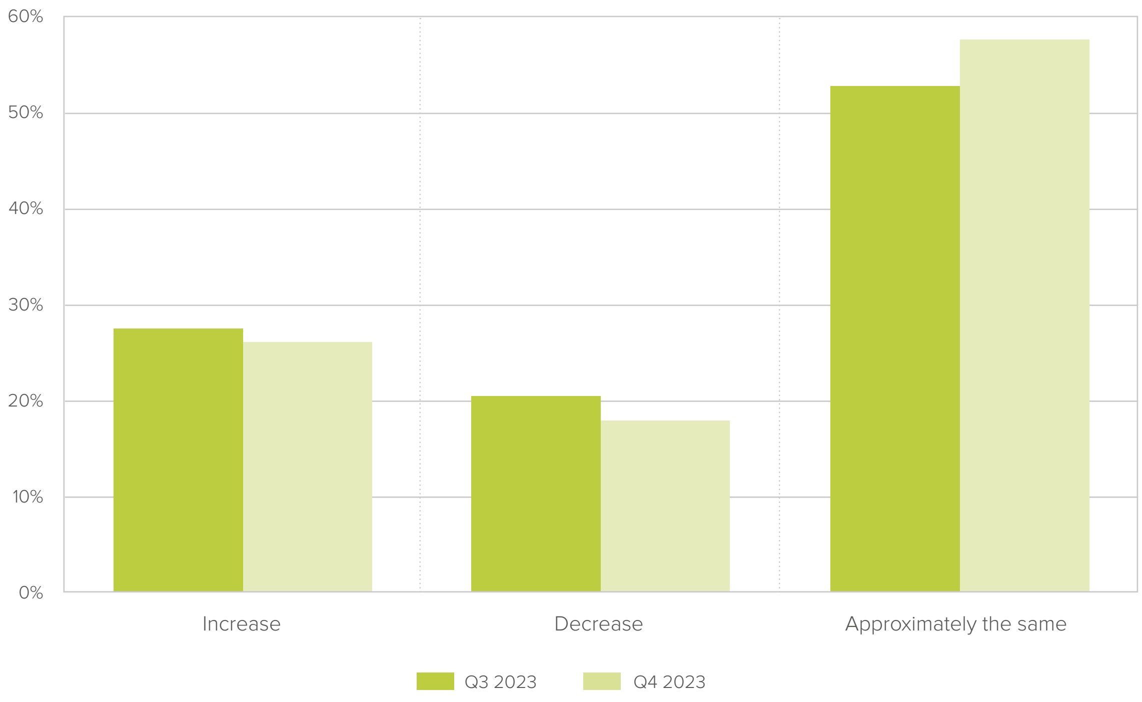
INVESTMENT AMBITIONS SHOW SLIGHT IMPROVEMENT, WITH THE BOE HOLDING RATES SINCE SEPTEMBER

The share of small businesses expecting to increase their capital investment over the coming quarter increased marginally in Q4, reaching 25.6%, but remains lower than the same metric a year prior of 28.3%. There was also a fall in the share of small businesses expecting to cut back on their investment, which declined to 17.4% in Q4, down from 19.4% in Q3. Overall, the net balance of small businesses expecting to increase their investment picked up to 8.2% in Q4, the highest result on this metric recorded for the year.

These changes come amidst the Bank of England holding the rate at 5.25% since September. The easing of inflation also raises optimism that the Bank will cut rates earlier this year than previously predicted. Cebr anticipates that the peak of the monetary tightening campaign has been reached, with rate cuts expected to commence around the middle of this year.

On a sectoral basis, businesses in accommodation and food services were the worst performers on this metric, with a net balance of -1.3%. However, they did show notable improvement on the net balance of -7.5% recorded in the previous quarter. Meanwhile, businesses in manufacturing were the most upbeat regarding their investment over the next quarter, with a net balance of 11.6% expecting to increase their capital investment compared to the previous quarter.

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 December 2023 research survey of FSB members carried out by Verve. 756 responses were received. The data are weighted by regional gross value added to match the profile of small businesses across the UK. The survey was undertaken between 13 December 2023 to 2 January 2024.

SUMMARY DATA TABLE

	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	Q2 2023	Q3 2023	Q4 2023
Small Business Index	15.3	-24.7	-35.9	-45.8	-2.8	-14.2	-8.0	-15.0
Employment - previous three months	2.9%	-3.6%	-4.4%	-6.1%	-0.8%	-2.4%	-0.2%	-4.5%
Employment - coming three months	14.5%	7.2%	2.7%	3.2%	8.3%	6.1%	2.6%	-1.2%
Exports - previous three months	-5.3%	-7.7%	-10.8%	-3.3%	-17.7%	-2.9%	-2.6%	-10.8%
Exports - coming three months	10.4%	1.4%	-4.3%	7.9%	-6.4%	-0.6%	7.3%	0.8%
Credit availability and affordability - rated good or very good	19.5%	17.6%	17.4%	14.7%	12.3%	11.8%	14.4%	14.4%
Credit availability and affordability - rated poor or very poor	36.5%	42.3%	44.1%	50.5%	50.9%	52.0%	53.1%	52.0%

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.

Q4

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