Q1

FSB VOICE OF SMALL BUSINESS INDEX

QUARTER 1, 2023

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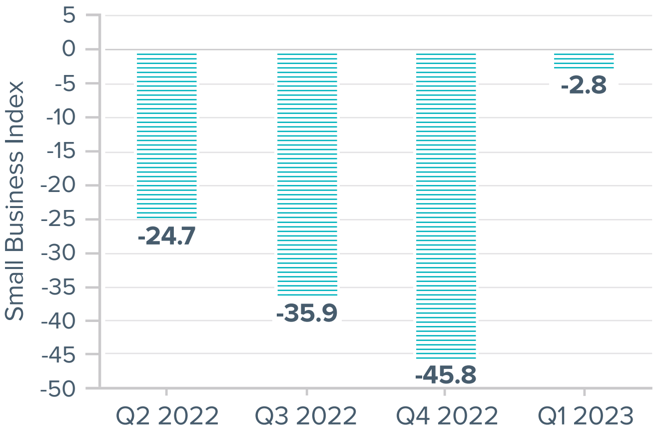
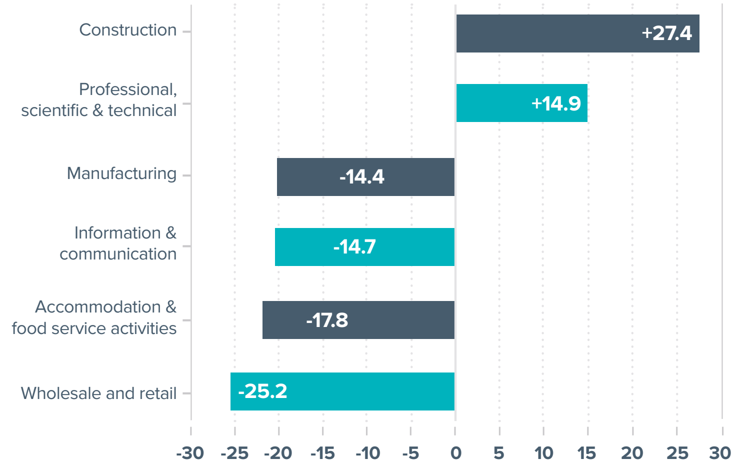
SBI Q1 2023

Small business confidence recovered strongly on the quarter but is still in lightly negative territory

Small business confidence improved by 43.0 points between Q4 2022 and Q1 2023, the third-largest improvement on record



Small business confidence by sector

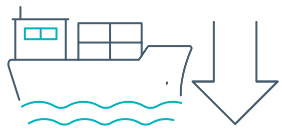


Costs set new record

92%

of small businesses report **higher costs** compared to a year ago

Exporters saw a fall in volumes



40%

of small exporters saw the **value of their exports fall** over Q1, while **37%** said they stayed around the same, and **22%** saw an increase

Two in five saw revenues fall

41%

of small businesses reported a **decrease in their revenues over Q1**, while **34%** said they increased

A third saw late payments worsen

34%

of small businesses said **late payments had increased** over the previous quarter

Finance more difficult to acquire

51%

of small businesses rate the **availability and affordability of finance** as ‘poor’ or ‘very poor’, and **18%** who have applied for finance are still **awaiting a decision from the lender** – a new record

CONTENTS

FSB FOREWORD

This latest Small Business Index (SBI) provides a measured yet encouraging indication of progress. Recovery was the third largest quarter-on-quarter rise in the history of the SBI. These figures illustrate potential to not only rebound to pre-pandemic levels, but also redefine our economy following a challenging period.

The panoramic view of progress across all sectors compared to Q4 2022 presents an interesting tableau, with strides of progress. The professional, scientific and technical sectors, for instance, saw a rise of 39.3 points, reaching a confidence score of 14.9 points, proving its robustness.

However, the wholesale and retail sector, despite a larger increase of 58.1 points, remains more negative at -25.2 points. This underlines the ongoing journey towards complete recovery.

Looking ahead, Q2 2023 presents promising prospects, with two in five small firms expecting to see an increase in their revenues. We are confident these upbeat forecasts will materialise, showcasing the steadfast drive of entrepreneurs and small businesses.

Growth aspirations, too, show a promising trend, with a slight increase from 45 per cent to 46 per cent of small businesses predicting they will grow in Q2. This aligns with a decrease in businesses expecting to downsize, sell, or close, dropping from 16 per cent to 13 per cent.

This is strong and positive, but there are still hurdles that lie ahead. Many small businesses have been impacted by increased costs, changes in finance availability, high energy and utility costs, and uncertainties surrounding exports. Employment levels also require careful scrutiny, with around one in nine firms increasing staff numbers and one in eight reducing their headcount in the last quarter. But these challenges aren't insurmountable, and we're steadfast in our commitment to addressing them effectively.

Despite finding the Spring Budget less supportive than expected, we will continue to press for an environment that encourages small businesses to grow, contributing to overall economic progress.

In line with this, FSB is now focusing on facilitating economic growth and fostering an environment conducive to new startups. We're shifting our perspective from past contraction towards future expansion, aiming to reinvigorate our community with fresh initiatives and strategies, particularly emphasising start-ups and women entrepreneurs.

It's clear that while there are challenges, there are reasons to be hopeful. The rising confidence is a promising sign, and we eagerly anticipate seeing the small business community thrive in the coming months. This is an opportunity to build stronger and better for the collective prosperity of all businesses.

Tina McKenzie,
Policy Chair

ECONOMIST'S VIEW

The first quarter of 2023 saw a substantial increase in the Small Business Index (SBI), rising by 43.0 points to stand at -2.8. This jump was the third largest since the inception of the index, only eclipsed by those in Q2 2020 and Q1 2021 as the UK economy emerged from periods of severe lockdown restrictions. While still net negative, small business confidence now stands at its highest since the start of 2022 before the energy price crisis unfolded and inflation skyrocketed.

The turnaround in small business sentiment, which follows an eight-quarter low recorded in Q4 2022, is reflective of a wider improvement in the UK economy's prospects in recent weeks. This is partly due to the sustained falls in wholesale energy prices witnessed since the start of the year, easing the cost pressure on businesses and consumers alike. Government intervention has also played a part, with the Energy Bill Relief scheme providing help with businesses' energy bills over the winter, and the Energy Price Guarantee, which was extended until the end of June, supporting households.

Aside from the extension of the Energy Price Guarantee, Chancellor Jeremy Hunt announced several other policies in his Spring Budget on 15 March focused on increasing employment rates across the economy, such as more generous childcare provisions for parents with small children and the removal of the pension lifetime allowance. Meanwhile, full expensing of qualifying investments for a period of at least three years was announced while the planned increase in Corporation Tax from 19% to 25% starting from the 2023/24 financial year is going ahead. Additionally, pubs and other licensed establishments will benefit from an increase in Draught Relief for qualifying beer, cider and wine products.

Looking at small business confidence by sector shows that all major industries recorded an increase in Q1, though only three out of the seven sectors analysed jumped into positive territory. Aside from businesses in the 'other' categories, wholesale and retail trade and the accommodation and food services sectors saw the largest increases last quarter at 58.1 and 53.6 points, respectively. The improvements in these consumer-facing industries supports our view that greater resilience in consumption spending is a key factor behind the wider uptick in small business sentiment.

Similarly, the regional breakdown of the SBI shows a general increase in confidence in the first quarter, with all regions reporting an uptick in their index score. In Scotland, the West Midlands, the South East, and London, more small businesses are optimistic about their business performance over the next three months than not. Meanwhile, the South West and the combined North East & Yorkshire and the Humber region saw the weakest net confidence scores at -23.2 and -15.6, respectively.

While the more positive outlook for the UK economy is to be welcomed, 2023 will nevertheless be a challenging year for the UK's small businesses. Headline inflation rates are expected to fall in the coming months, though rising costs will remain a key issue for business owners due to the expiration of the more generous Energy Bill Relief Scheme and increasing Corporation Tax bills. Moreover, the effects of tighter monetary policy will be felt throughout the economy, potentially further amplified by the turmoil in the banking sector in recent weeks. We can already see more signs of tighter credit conditions in this quarter's falls in the credit availability and affordability scores.

Kay Daniel Neufeld, Head of Forecasting and Thought Leadership

FSB EXECUTIVE SUMMARY

Key findings this quarter:

- **The Small Business Index (SBI) increased to -2.8 in Q1 2023.** This uptick follows three consecutive quarterly declines. The SBI is now at its strongest position since Q1 2022.
- **All UK regions saw an improvement on the SBI in Q1, relative to Q4.** Nonetheless, the SBI remained in negative territory in six of the UK's regions and nations.
- **All major industries saw an improvement in their SBI readings in Q1 2023.** Most remained in negative territory, however, with construction and professional, scientific and technical businesses recording positive scores.
- **The net balance of small businesses reporting revenue growth over the previous three months stood at -7.1% in Q1.** This marked the fourth consecutive negative reading on this measure, reflecting the pressures on revenue from high input prices and weaker consumer demand.
- **The net balance of exporting businesses reporting growth in the value of their exports stood at -17.7% in Q1.** This marked the sixteenth consecutive quarter for which the net balance of exports has stood below zero. This indicates exporters are still facing unfavourable conditions.
- **91.8% of businesses reported increased costs compared to a year ago in Q1.** This represents the highest net balance figure on this measure since data collection began, highlighting the widespread nature of cost pressures at present.
- **Utilities were the most commonly cited source of increasing costs, selected by 62.7% of respondents.** The percentage of respondents who attributed rising costs to labour saw an increase from 40.5% in Q4 2022 to 45.3% in Q1. This is likely a reflection of the combination of a relatively tight labour market and elevated inflation, with workers demanding higher wages in response to increases in the cost of living.
- **A net balance of -0.8% of small businesses reported growth in employee numbers in Q1.** This marks a fourth consecutive negative reading, though it was less negative than the preceding three quarters.
- **For the fourth consecutive quarter, just under half of small businesses expect to grow over the coming year.** However, this share was slightly higher in Q1 than in Q4 2022, at 45.9% compared to 44.7%. Weaker growth aspirations align with the general instability faced by the economy as a whole, which has experienced only marginal growth over the past quarters.
- **The domestic economy is the most commonly cited barrier to growth amongst small businesses, with 61.3% of respondents selecting the category.** Utility costs were the second-most selected barrier to growth amongst businesses in Q1, with 32.8% reporting this.
- **The environment of higher base rates, with the Bank of England raising the base rate twice in Q1, has fed through to higher commercial rates for small businesses.** The share of successful loan applicants being offered a rate of up to 4% declined starkly in Q1, reaching just 4.7%, having stood at 26.7% in Q4 2022. Accordingly, small businesses perceptions of credit availability and affordability worsened in Q1 of this year.
- **Q1 brought a decline in the share of small businesses expecting to increase their investment over the coming quarter.** This was the case for just 23.3% of respondents, down from 28.3% in Q4. Simultaneously, the share of small businesses expecting to cut investment over the coming quarter increased, reaching 21.2%, up from 19.0% in the fourth quarter of last year.

UK MACROECONOMIC OVERVIEW

UK economy on sluggish growth path at start of 2023

The latest data from the Office for National Statistics (ONS) show that UK GDP grew by just 0.1% in the three months to March 2023, relative to the previous three-month period. The UK economy is currently performing sluggishly, having witnessed very little growth since Q4 2021.

The 0.1% headline growth in the three months to March masked some divergence between sectors. The production sector, which covers manufacturing as well as some smaller sectors such as energy supply, grew by 0.1% following no growth in the previous three-month period. Meanwhile, the services sector grew at the same rate as the economy as a whole. Services output has been mixed, with consumer-facing services falling by 0.4% whilst other services increased by 0.2%. Construction output grew by 0.7% in the three months to March, supported by an uptick in activity in repair and maintenance work.

The UK economy remains on a relatively unstable footing, facing a variety of risk factors. As a result, Cebr is forecasting a small quarterly contraction in Q2 2023. Across the year as a whole, the economy is projected to grow by just 0.2%. It should be noted that this forecast has been upwardly revised recently, with economic conditions being less negative than was the case towards the end of 2022. This development is corroborated by the fact that the FSB Small Business Index has improved substantially on the quarter, though it remains in negative territory.

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 improves but net pessimism still prevailing

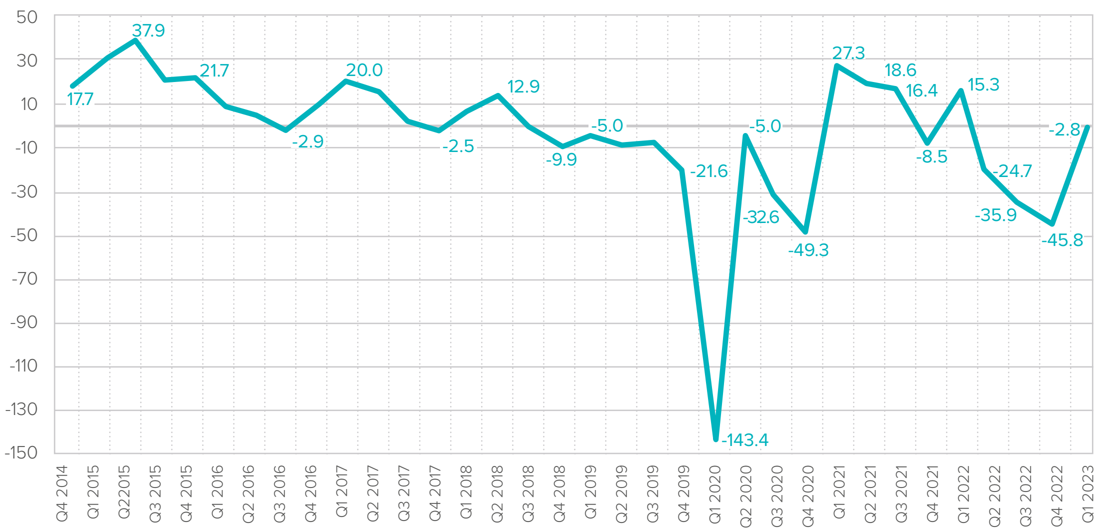
The Small Business Index (SBI) increased to -2.8 in Q1 2023. This marks a return to growth, following three consecutive quarterly declines. Despite the increase, the Index remains in negative territory, meaning that the proportion of small businesses expecting an improvement in prospects over the coming quarter is exceeded by the proportion of firms expecting prospects to worsen. Nevertheless, following the third-largest quarterly improvement on record the SBI is now at its strongest position since Q1 2022.

The improvement to the SBI is corroborated by wider macroeconomic evidence, which has shown stronger-than-expected performance at the start of 2023. As a result, many forecasts for the economy in 2023 have been upwardly revised. Such improvements in conditions have fed through to small businesses, as evidenced by the improving sentiment compared to Q4 2022.

The Index remains in negative territory, however, meaning there are more businesses expressing pessimism about the coming quarter than optimism. Cebr's forecasts corroborate this sentiment, with the economy expected to face a quarterly contraction in Q2.

With a return to growth anticipated in Q3, as pressure from energy bills and wider supply chain issues subsides, a return to positive readings on the SBI is seemingly on the horizon.

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

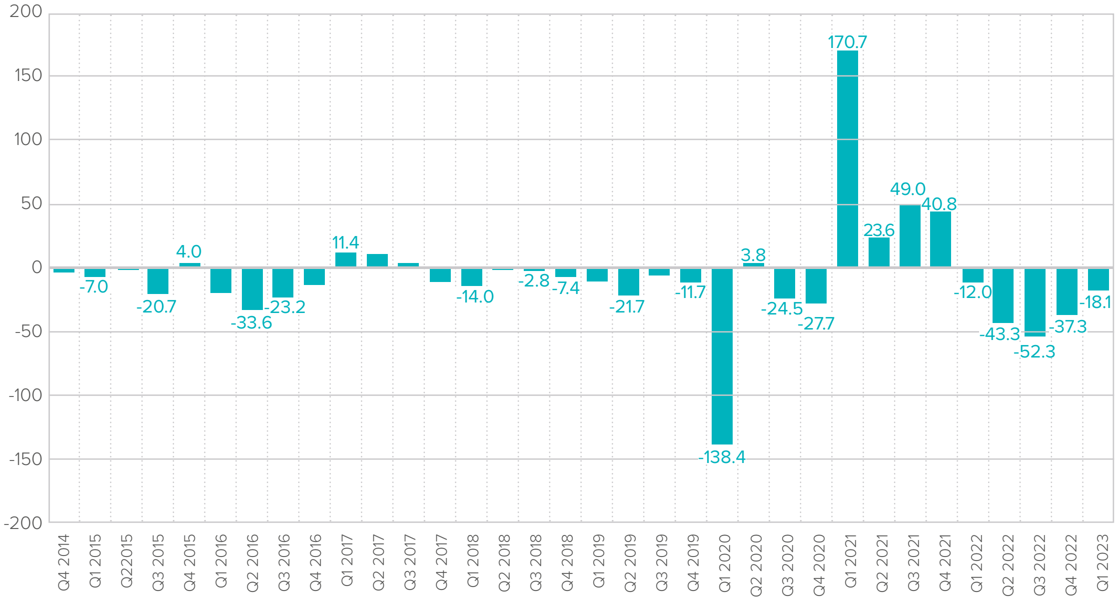
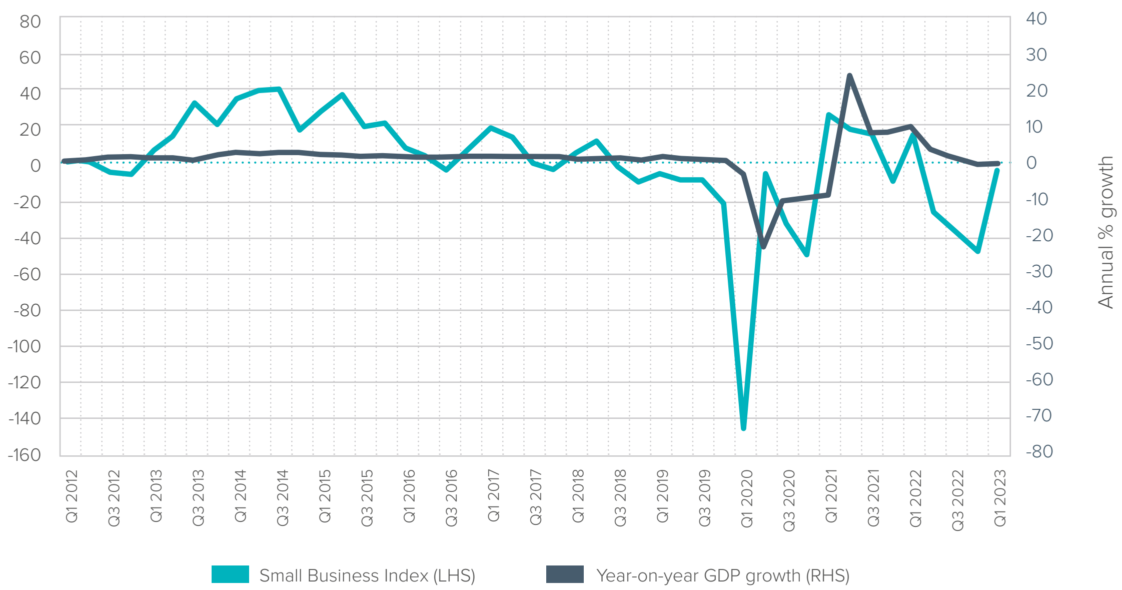


Figure four: UK SBI against year-on-year UK GDP growth
Source: ONS, FSB - Verve 'Voice of Small Business' Panel Survey



REGION AND NATION SMALL BUSINESS INDICES

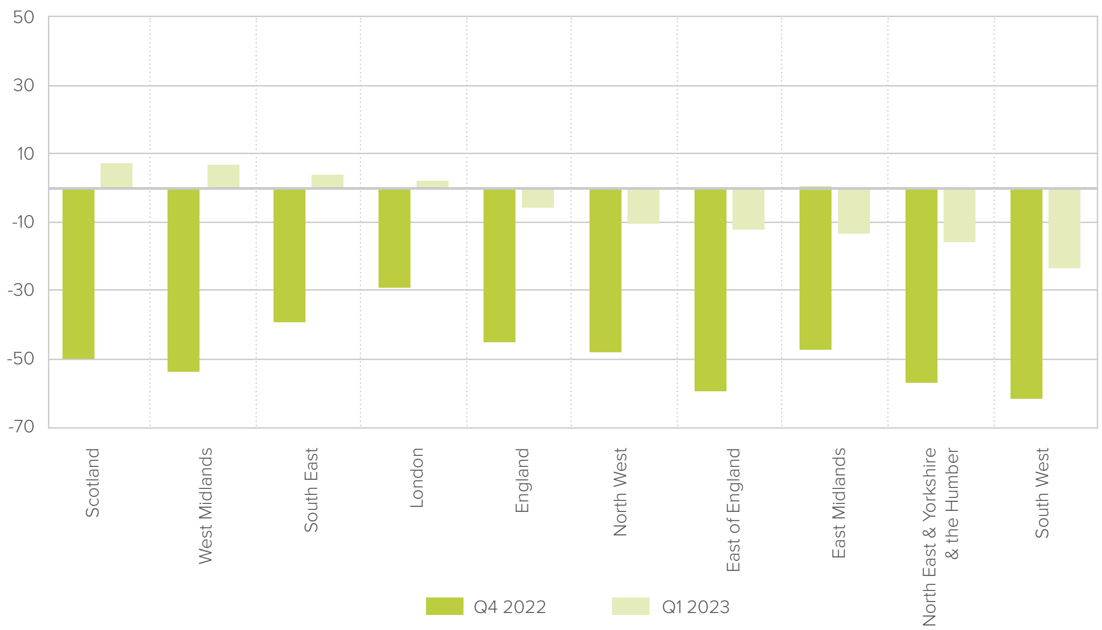
SMALL BUSINESS INDEX IMPROVES FOR ALL REGIONS AND NATIONS, THOUGH SCORES REMAIN NEGATIVE FOR THE MAJORITY IN Q1

Four of the UK regions and nations saw a positive reading on the regional SBI in Q1 2023, while the remaining six remained in negative territory.[2] All regions and nations saw an improvement in the measure in Q1 when compared to Q4 2022. This shift reflects improved optimism across the economy relative to the outlook towards the latter part of 2022, with the UK economy looking set to avoid a deep recession. However, for most areas the proportion of small businesses expecting a worsening in performance in the coming quarter exceeds the proportion expecting an improvement.

The most optimistic region in Q1 looking ahead to Q2 was Scotland, with an SBI score of 7.1 following a strong quarterly improvement of 57.1 points. London recorded a positive SBI score of 1.8. The large concentration of consumer-facing services in the capital means it has likely benefited from better-than-expected consumer activity during the start of this year.

The South West ranked the lowest in Q1, with an index score of -23.2. This was the third consecutive quarter in which the South West ranked as the lowest scoring region. Tourism is an important industry in the South West and this sector is facing significant challenges due to high inflation. With prices of essential goods rising, some consumers are forced to cut back on non-essential expenditures, which will include travel and leisure activities. The combined region of the North East & Yorkshire and the Humber was the second-lowest ranking region, recording a score of -15.6 in Q1.

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 Analysis for Northern Ireland and Wales is excluded due to insufficient sample size in the survey. Furthermore, results for the East Midlands, East of England and North West should be interpreted with care due to low sample size.

SMALL BUSINESS SECTOR INDICES

CONSTRUCTION AND PROFESSIONAL, SCIENTIFIC AND TECHNICAL BUSINESSES ARE MOST OPTIMISTIC OVER THE COMING THREE MONTHS

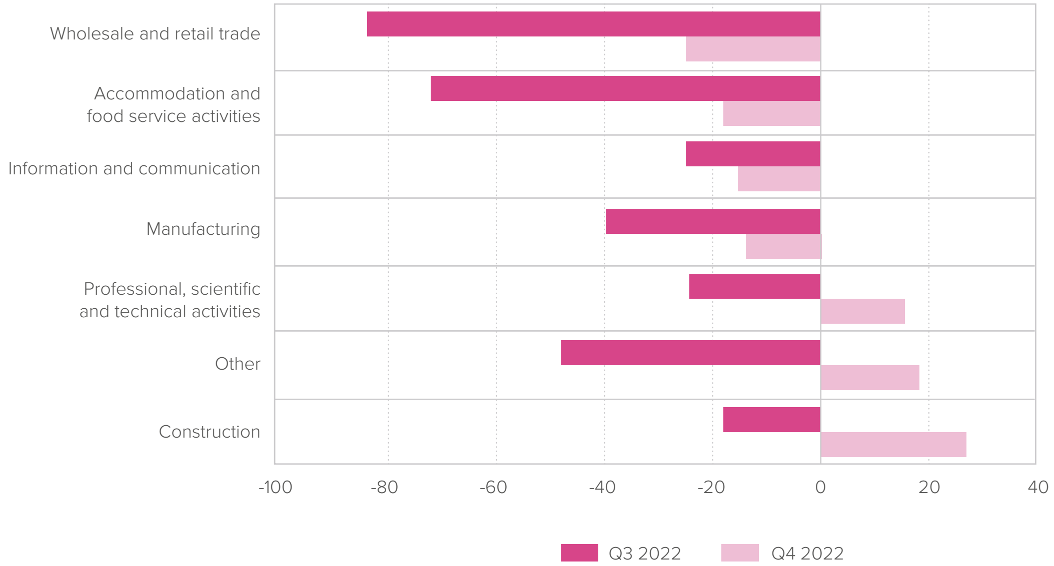
All major industries saw an improvement in their SBI readings in Q1 2023. Construction and professional, scientific and technical activities saw positive SBI readings in Q1 as a result, while manufacturing, information and communication, accommodation and food and wholesale and retail trade all remained in negative territory.[3]

Construction saw an increase in its SBI reading, up from -18.6 in Q4 of last year to 27.4 in Q1. An improvement was also seen for businesses in professional, scientific and technical services, amounting to an increase of 39.3 points to reach 14.9. A new government policy of 'full expensing' was announced in March, which allows companies to write off the full cost of capital expenditure including IT equipment against their tax bill. This will support businesses with more technical services.

The SBI reading for the wholesale and retail sector improved by 58.1 points to a reading of -25.2 in Q1. This reduction in pessimism in the sector likely reflects the fact that consumer spending has held up better than expected at the start of the year, as shown in recent retail sales data from the ONS. Nonetheless, this industry remains the most pessimistic of the major sectors monitored, and the cost-of-living crisis is still the main concern for its economic outlook. CPI inflation was 8.7% in April, reducing spending power for consumers.

The smallest increase in Q1 relative to Q4 was observed in information and communication, which remained in negative territory with a reading of -14.7. Although this industry is less exposed to lower consumer spending, high interest rates will impact businesses as the new technology associated with this sector often requires high levels of borrowing. Sentiment may therefore have suffered from the continued pursuit of price stability by the Bank of England, which raised its base interest rate to 4.25% during Q1.

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 FOURTH CONSECUTIVE TIME IN Q1

The net balance of small businesses reporting revenue growth over the previous three months stood at -7.1% in Q1 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. Q1 marked the fourth consecutive negative reading for the revenue net balance figure.

On a sectoral basis, wholesale and retail businesses recorded the weakest figure in Q1, with a net reading of -26.8%. For wholesale and retail in particular, decreases in revenue growth are a concern as businesses in this industry are acutely exposed due to their relatively lower profit margins. Accommodation and food services saw the second-lowest reading, with a net balance of -25.9% reporting revenue growth. This reflects the fact that businesses in this sector have been particularly exposed to the slowdown in consumer activity resulting from persistently elevated price pressure. Recent wage data from the ONS showed further falls in household disposable income, leading consumers to cut back on non-essential spending. Meanwhile, small businesses within the construction industry saw the largest positive reading for Q1, with a net balance of 19.5% reporting revenue growth. This improvement in activity is corroborated by the composite PMI for construction which averaged 51.2 across Q1 2023, its highest level for three quarters.

Looking ahead, small businesses are more optimistic with a net balance of 12.9% expecting their revenue to grow in Q2 2023. The largest positive net balances were seen in construction and professional, scientific and technical services, with readings of 59.2% and 24.3%, respectively. This corresponds to the rankings on the broader SBI measure, underscoring the connection between revenue performance and business confidence.

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

EXPECTATIONS FOR EXPORTS TURN LESS GLOOMY AS SHIPPING RATES FALL FURTHER AND FUEL PRICES EASE

The net balance of exporters reporting growth in the value of their exports fell in Q1 2023, with the figure standing at -17.7%, down from a net balance of -3.3% in Q4 2022. The latest reading means exporting small businesses have on balance seen negative export growth for the past sixteen quarters, though recent readings are well above the lows seen during the early pandemic lockdown periods. Looking ahead, a net balance of -6.4% anticipate export growth in Q2 2023.

The Baltic Index, which provides a benchmark for measuring the price of shipping costs, showed that shipping costs for a typical 40-foot container averaged £1,020 across Q1, down 29.4% from Q4 and 47.4% annually. This significant fall in shipping costs should support exporters in the period ahead.

Exports are also exposed to worsening demand prospects across the globe, however, high inflation has impacted demand across the world while rising global interest rates have a dampening effect on activity, with both factors potentially hurting export growth.

Swings in the value of sterling are important to exporting businesses, though a devaluing currency has both benefits and drawbacks depending on the nature of the business. According to the Bank of England's trade-weighted effective exchange rate index, sterling was 5.1% weaker in Q1 2023 than its level a year earlier. This could provide a boost to exports by reducing costs to other countries. For businesses relying on imported inputs, however, a weaker pound will lead to higher costs.

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 BUSINESSES FACING INCREASED COSTS HITS ANOTHER RECORD HIGH

In Q1 the net balance of small businesses that reported a rise in their operating costs reached an all-time high of 88.7%, up from the previous quarter's net balance score of 86.1%. This data marks a worrying trend for small businesses, as it demonstrates the continued financial strain due to the mounting pressures of rising costs. The last two quarters have recorded the highest net balance figures ever reported, demonstrating higher operating costs are still affecting businesses' bottom lines.

As was also the case in Q4 2022, the most commonly-cited source of changing costs was utilities, selected by 62.7% of respondents. Though energy inflation rates have decelerated in recent months from their June peak, prices are still rising at an elevated rate. Q1 marked the final quarter of the Energy Bill Relief Scheme, a Government initiative that shielded businesses from the full rise in energy costs. This policy was replaced by a less generous Energy Bills Discount Scheme from April, shifting support from a cap to a discount, meaning businesses are now more exposed to any potential future rises in energy prices.

Labour and rent costs were cited as a main source of cost increases by 45.3% and 25.3% of respondents in Q1, respectively, with both options seeing the joint-highest rise in share when compared to Q4 2022. This is reflective of the broader pressures in the economy, with workers demanding higher wages in the face of a cost-of-living crisis, while landlords are faced with higher borrowing costs and are increasing rents as a result.

Taxation was quoted by 22.8% of businesses as having a key impact on costs. It was announced in the Spring Budget in March that the Corporation Tax hike from 19% to 25% will go ahead this April. Although this will only impact businesses with profits over £50,000 per year, this is still a considerable policy shift, and, on top of the freeze in National Insurance thresholds announced in the Autumn Budget, raises costs for businesses. The rise in the Annual Investment Allowance to £1 million and a new policy of 'full expensing' will support businesses with tax relief on qualifying capital investment.

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

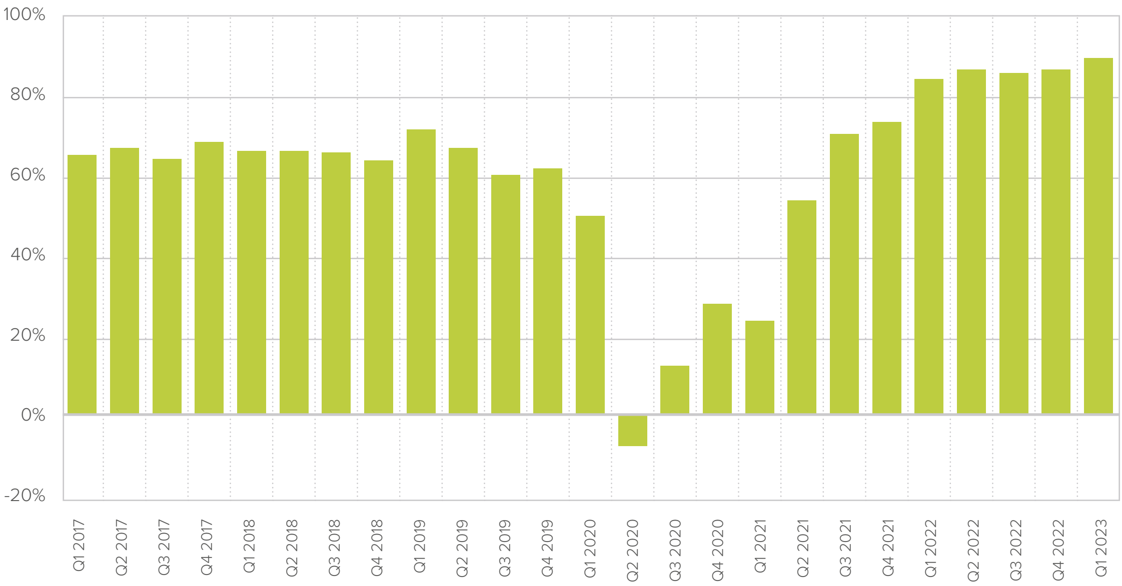
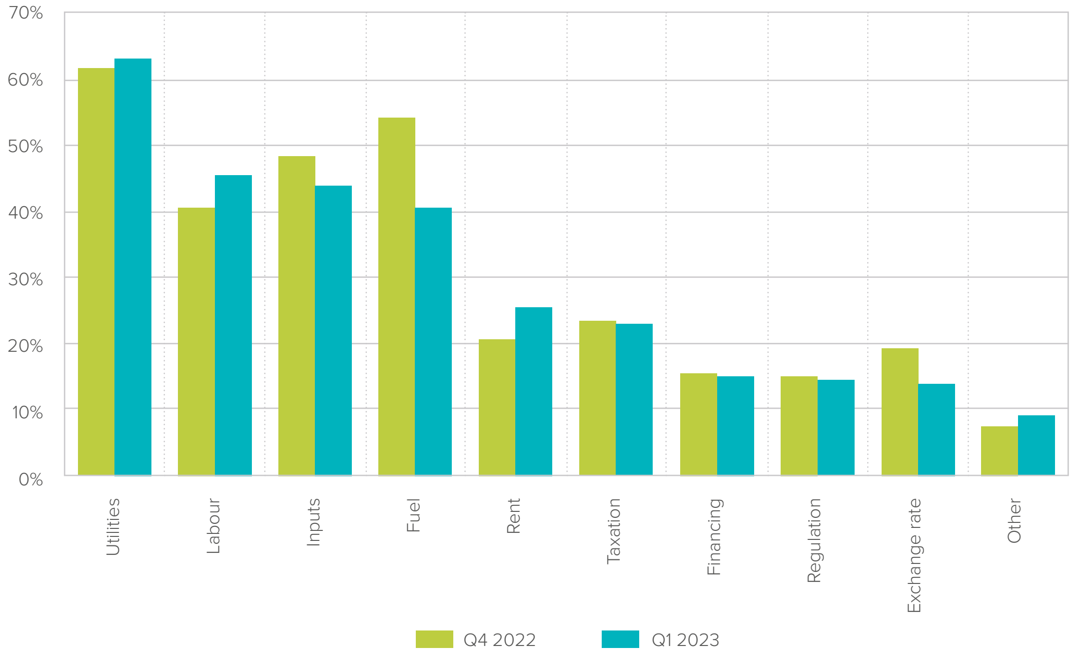


Figure 10: Main causes for changing business costs (firms may give multiple answers)
Source: FSB - Verve 'Voice of Small Business' Panel Survey



EMPLOYMENT

SMALL BUSINESS EMPLOYEE NUMBERS CONTRACT FOR FOURTH CONSECUTIVE QUARTER

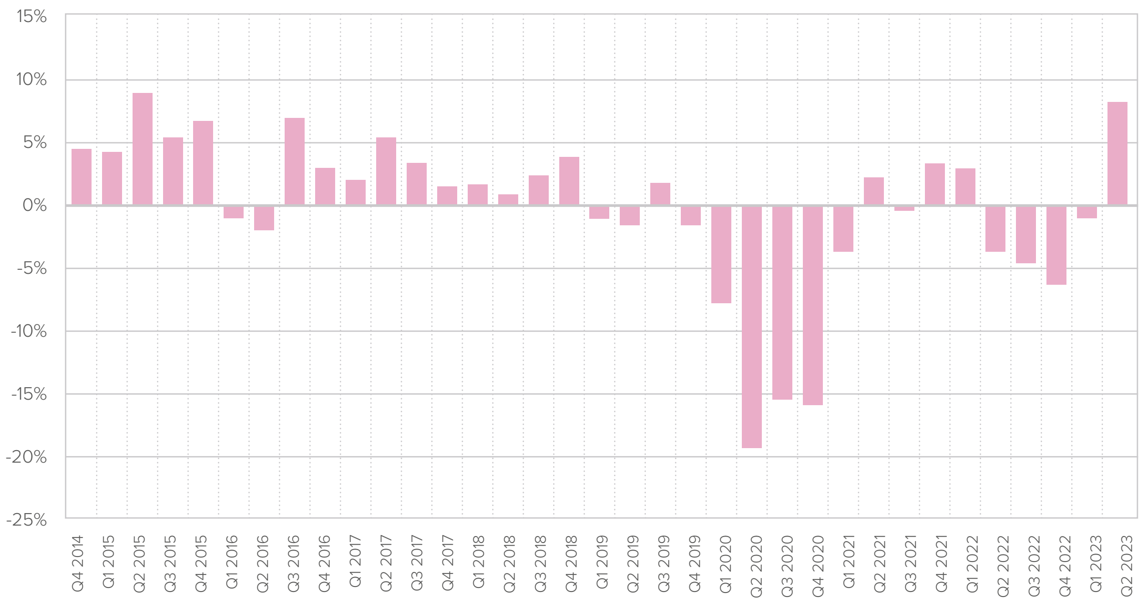
A net balance of -0.8% of small businesses reported growth in employee numbers in Q1. The negative reading means that the number of businesses expanding their workforce was outweighed by the number of businesses reporting a contraction in headcount. This marks a fourth consecutive negative reading, although one that was less negative than the preceding three quarters.

Official data from the ONS show that unemployment rose by 0.1 percentage point to 3.9% in the three months to March 2023, while vacancies were shown to have fallen for the tenth consecutive period. Lower consumer demand and elevated input costs mean businesses are likely seeking to reduce hiring intentions.

By sector, the worst net balance score was seen in manufacturing at -10.1%. This sector is especially exposed to soaring input costs which may be leading to reduced hiring intentions to cut costs elsewhere. Wholesale and retail and accommodation and food services were the other main sectors to see a negative net balance, recording -4.2% and -6.6%, respectively. These sectors are reliant on discretionary spending and have suffered due to consumers cutting back on spending due to the cost-of-living crisis.

Looking ahead, the net balance of expectations for the next three months stands at 8.3%, suggesting businesses expect employee numbers to grow in Q2 2023, in line with the improvement in economic conditions. Nevertheless, it is in contrast to Cebr's expectations of further increases in unemployment as a result of the aforementioned macroeconomic headwinds.

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

LESS THAN HALF OF SMALL BUSINESSES ANTICIPATE GROWTH OVER THE COMING YEAR

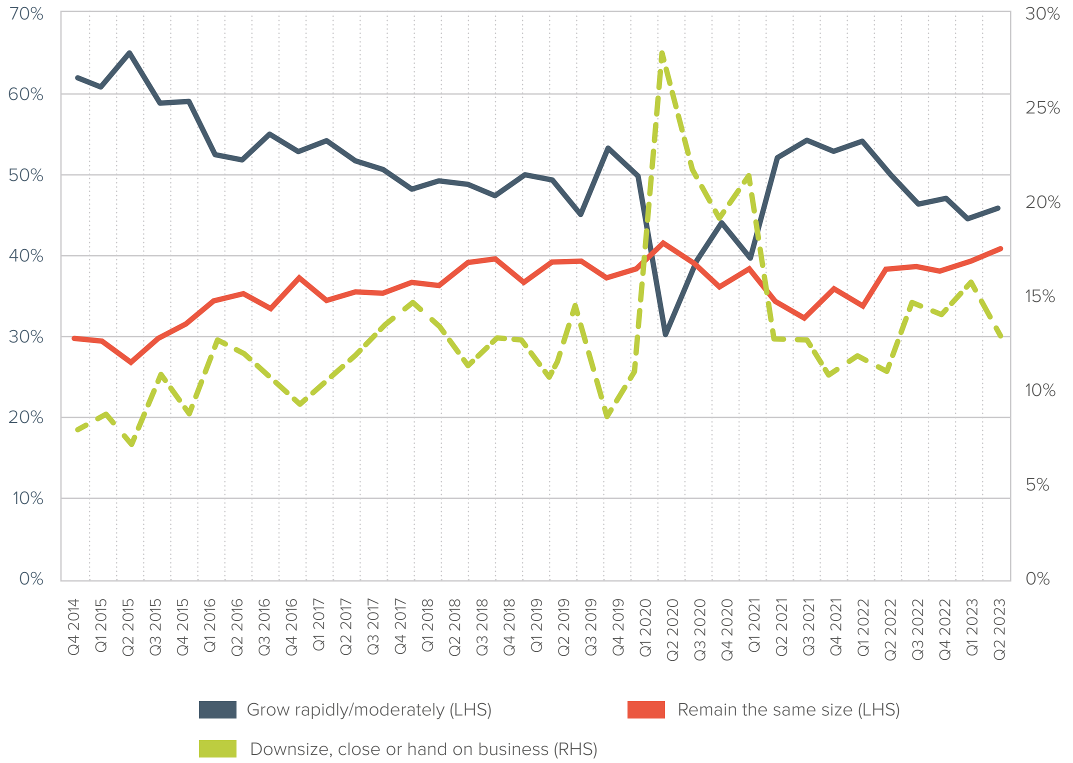
For the fourth consecutive quarter, only a minority of small businesses expect to grow over the coming year. However, this share was slightly higher in Q1 than in Q4 2022, at 45.9% compared to 44.7%. There was a simultaneous decline in the share of businesses expecting to downsize or close, from 15.7% in Q4 to 13.2% in Q1, the lowest share since the 11.2% recorded in Q1 2022.

Weaker growth aspirations align with the general economic uncertainty and low growth trajectory of the wider economy. Looking at businesses by sector, those in accommodation and food service activities are the least likely to anticipate growth over the coming year, with this being the case for just 17.8% of respondents. For the wholesale and retail sector, the net balance figure stood at 28.0%.

Both sectors continue to face pressure from weaker consumer activity amidst declining living standards. Nevertheless, the share expecting growth in wholesale and retail is greater than was the case in Q4 2022, when just 37.5% of small businesses in this sector expected to expand over the coming year. This highlights the shift in sentiment between these periods.

Information and communication businesses are the most likely to expect growth over the coming year. This is the case for 53.7% of such respondents. These businesses are less exposed to the current headwinds facing the economy, since they are less input-intensive and also less directly linked to consumer developments.

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



DOMESTIC ECONOMY AND UTILITY BILLS ARE THE MOST COMMONLY-CITED BARRIERS TO GROWTH FOR SMALL BUSINESSES

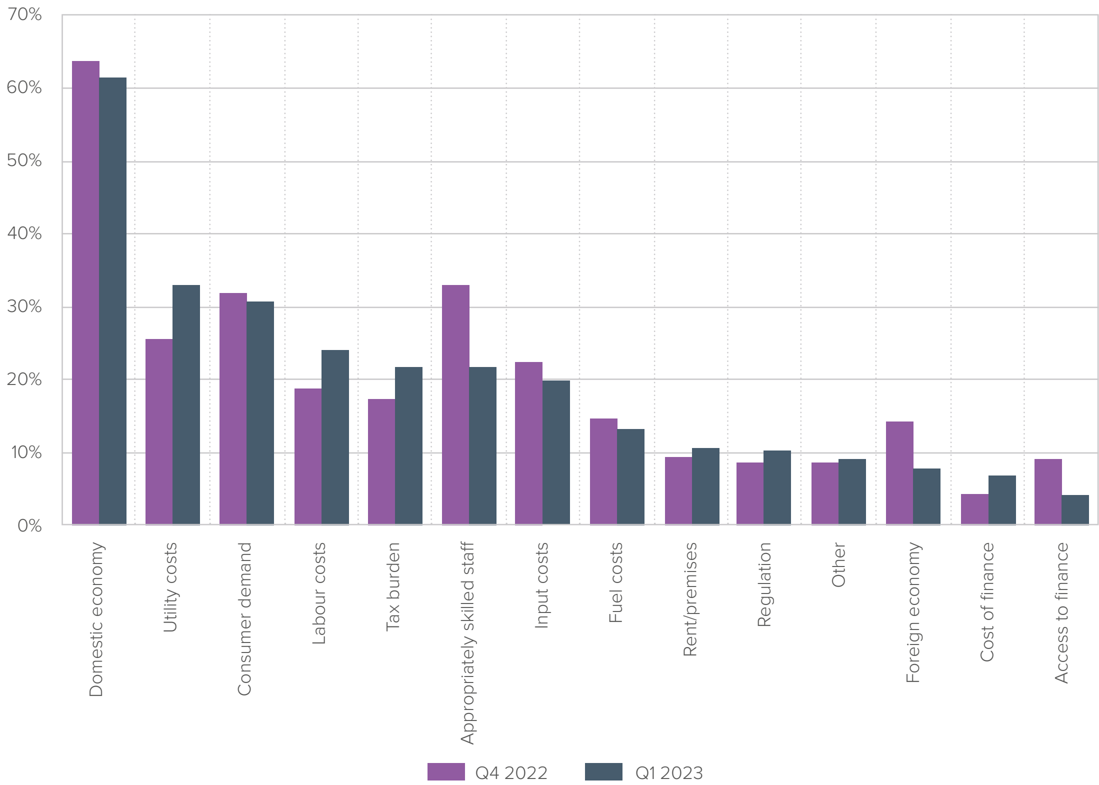
The domestic economy is the most commonly-cited barrier to growth amongst small businesses,[4] with 61.3% of respondents selecting the category. This highlights the continued weakness posed by current demand conditions. Nevertheless, this share is down on the 63.7% recorded in Q4 2022, reflecting the slight improvement in conditions between these periods.

Utility costs were the second-most selected barrier to growth amongst businesses in Q1, cited by 32.8%. This category also saw the largest increase in selection rate between Q4 and Q1, being up by 7.7 percentage points. After significant volatility in energy markets in 2022, prices are now on a general downward trajectory, but remain firmly above pre-crisis levels. Energy bills are therefore a more significant cost for many businesses at present.

Recent production cuts from the Organization of Petroleum Exporting Countries (OPEC) represent an upside risk to energy prices in the future.

There was a fall in the share of businesses citing finding appropriately skilled staff as a potential barrier to their growth. 21.4% of businesses selected this category in Q1, down from 32.7% in Q4. Though remaining tight by historic standards, the labour market has shown some emerging signs of slack in recent months, with the unemployment rate ticking up slightly. As a result of the expected recession, Cebr anticipates further increases to the unemployment rate. This should help to alleviate labour shortage issues that have impacted businesses for some time now.

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

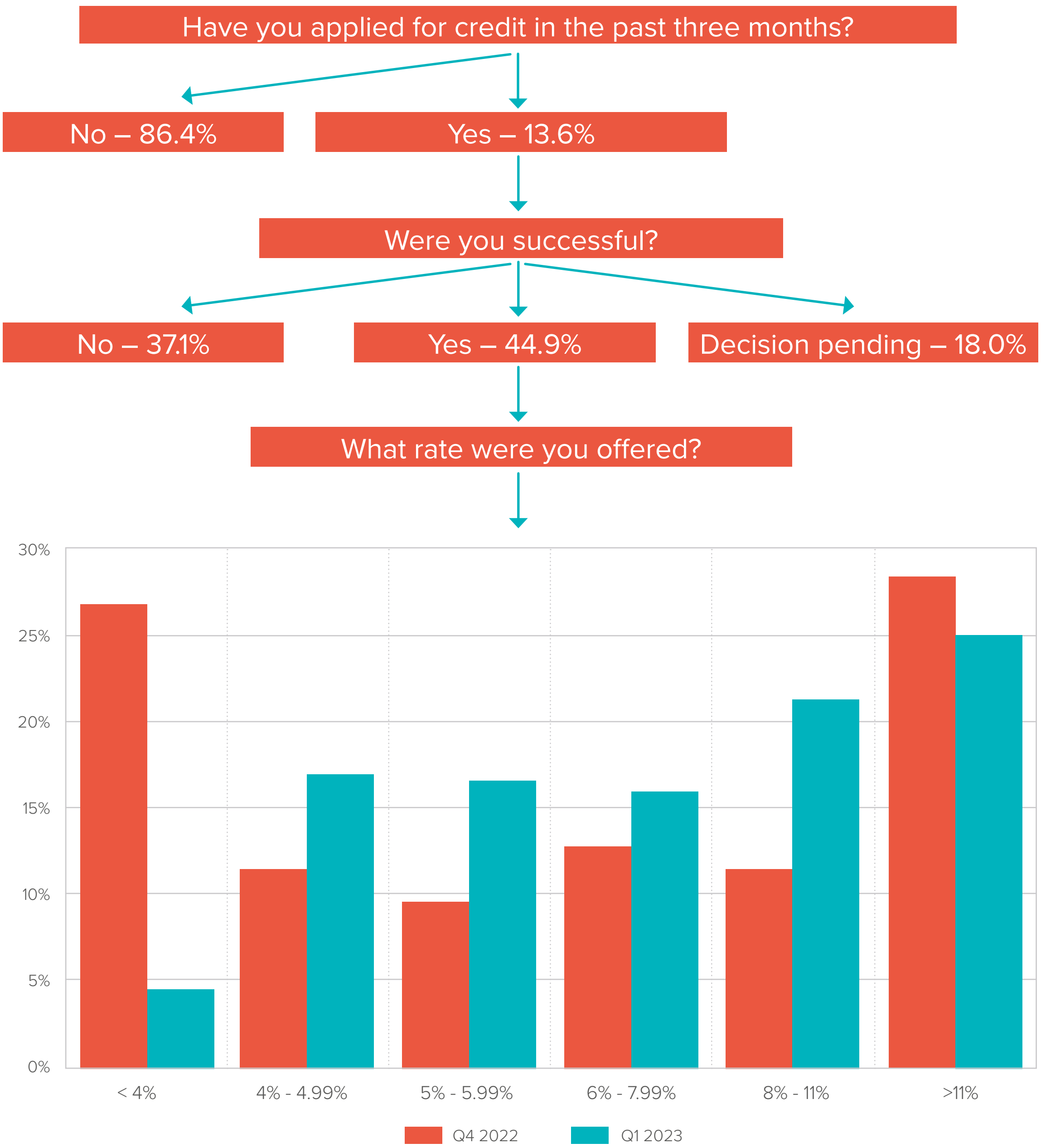


4 Please note that the Q4 edition of the Small Business Index posed the question of barriers to growth only to the subset of businesses expecting to grow over the coming year. The Q1 edition posed this question to all respondents.

CREDIT

SMALL BUSINESSES FACING HIGHER COMMERCIAL RATES AS MONETARY TIGHTENING FEEDS THROUGH

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.



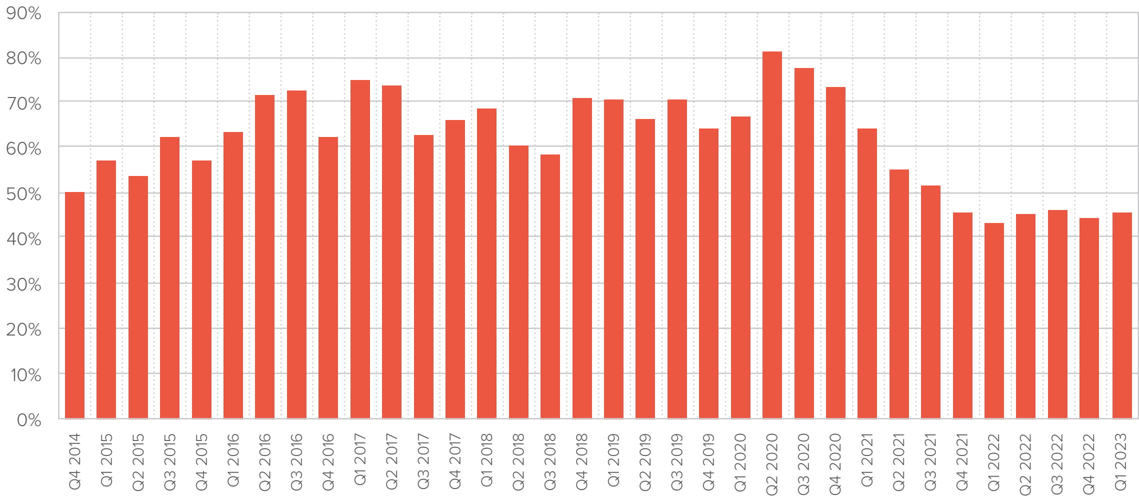
13.6% of small businesses reported that they applied for credit in Q1 2023. This was slightly down on the 13.8% recorded in Q4 2022, but remains above the three-year pre-Covid average of 13.2%.

The share of credit applicants reporting that they were successful in their application increased slightly on the quarter, reaching 44.9%, up from 44.1% in Q4. Despite this increase, this is still the third-lowest value since Q4 2013, highlighting the tight credit conditions faced by businesses at present.

Comparing across sectors, businesses in wholesale and retail were one of the most likely to have applied for credit in Q1, with this being the case for 18.8% of respondents. This highlights the troublesome conditions these businesses have faced in recent months, being particularly exposed to consumer pressures.

The Bank of England raised rates on a further two occasions in Q1. This environment of higher base rates has fed through to higher commercial rates for small businesses. The share of successful loan applicants being offered a rate of up to 4% declined starkly in Q1, reaching just 4.7%, having stood at 26.7% in Q4 2022. Meanwhile, there were simultaneous upticks in the share of successful loan applicants being offered rates of 5% and 6%. The share of respondents being offered a rate of 9% increased significantly on the quarter, reaching 15.1%, up from 3.2% in Q4.

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

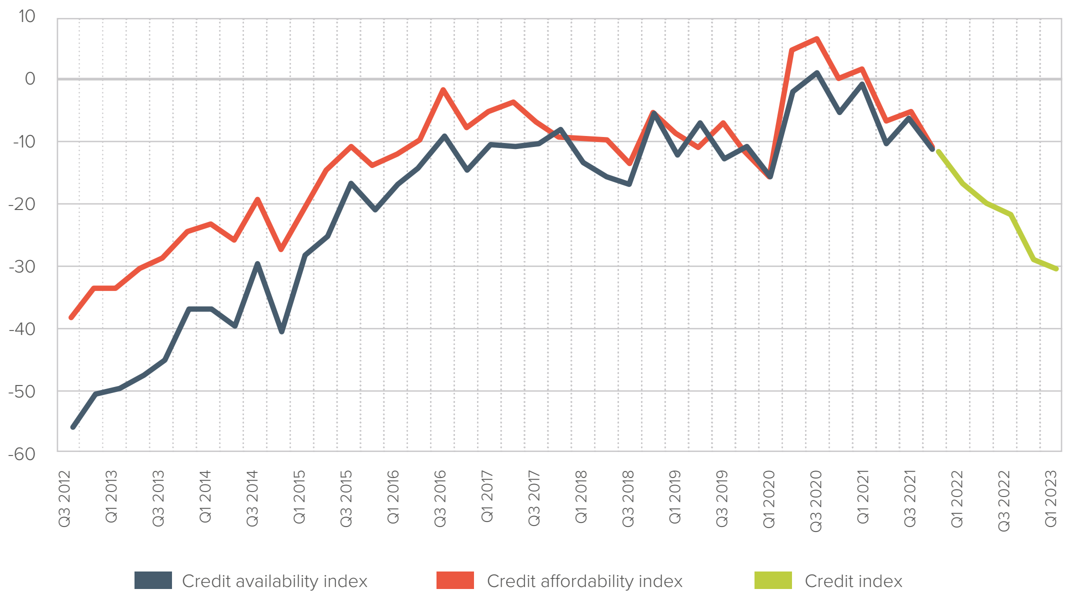


BUSINESSES' PERCEPTIONS OF CREDIT AVAILABILITY AND AFFORDABILITY WORSEN FURTHER

Perceptions of credit affordability and availability worsened further in Q1. The share of businesses with positive opinions on overall credit availability and affordability fell to 12.3% in Q1, down from 19.5% in the same quarter of 2022. Simultaneously, the share expressing negative views increased to 50.9% in Q1 2023, up from 36.5% in the same quarter of 2022. Businesses in London were particularly likely to express negative sentiment on credit availability and affordability, with this being the case for 56.3% of small businesses in the capital.

As a result of this changing sentiment, the credit index fell once more in Q1, reaching -30.5. This marks the worst reading since the credit availability and credit affordability indices were amalgamated in Q1 2022.

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[5]



5 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 WEAKEN AMIDST HIGHER BORROWING COSTS

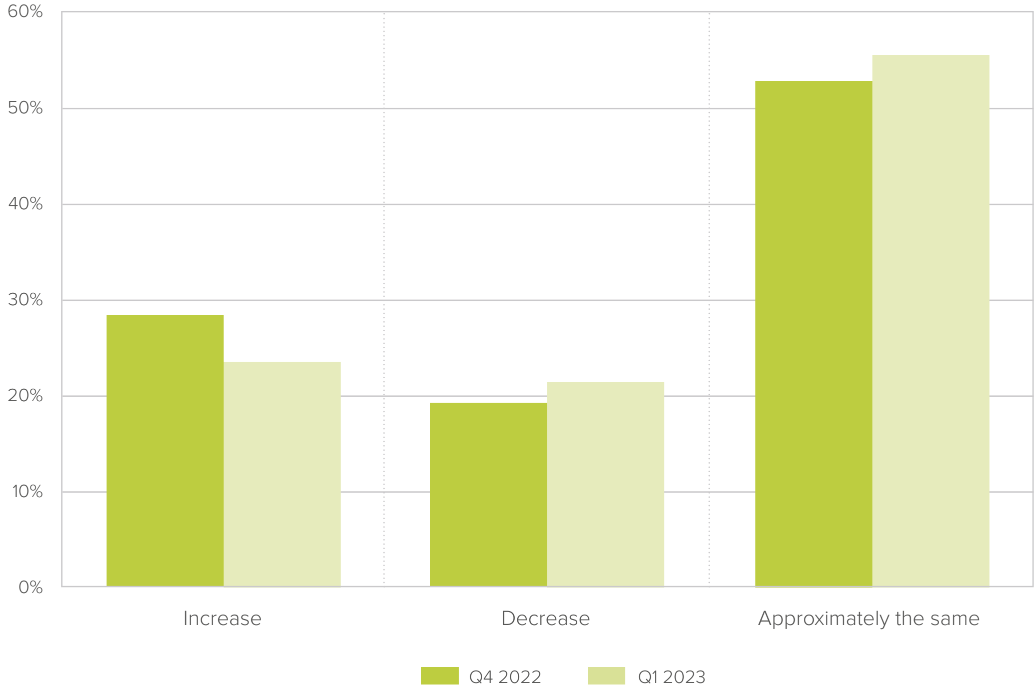
Q1 brought a decline in the share of small businesses expecting to increase their investment over the coming quarter. This was the case for just 23.3% of respondents, down from 28.3% in Q4. Simultaneously, the share of small businesses expecting to cut investment over the coming quarter increased, reaching 21.2%, up from 19.0% in Q4.

Consequently, the net balance of small businesses expecting to increase their investment over the coming quarter worsened in Q1, reaching just 2.1%. A decrease from 9.3% in Q4, this also represents the weakest net balance figure since the -0.6% recorded in Q4 2020, when businesses were facing considerable uncertainty from the Covid-19 pandemic.

The worsening of investment ambitions likely reflects the tighter interest rate environment, with borrowing costs now being significantly higher than in recent years. This increases the cost associated with investment, thus disincentivising businesses from making such plans. Continued economic uncertainty and relatively weak growth prospects are also likely dissuading businesses from putting funds towards investment.

Businesses in wholesale and retail were again one of the worst performers on this metric, with a net balance of -7.1% expecting to increase their investment over the coming quarter. These businesses are particularly exposed to consumer pressures at present and therefore subject to greater uncertainty. Interestingly, small businesses in information and communication recorded a weak net balance figure on this metric, at -12.6%, despite being some of the strongest performers on other elements of the SBI survey.

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 2023 research survey of FSB members carried out by Verve. 5,489 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. We received 681, a response rate of 7% 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 27 March and 11 April 2023.

SUMMARY DATA TABLE

	Q2 2021	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023
Small Business Index	18.6	16.4	-8.5	15.3	-24.7	-35.9	-45.8	-2.8
Employment - previous three months	2.2%	-0.2%	3.3%	2.9%	-3.6%	-4.4%	-6.1%	-0.8%
Employment - coming three months	14.0%	11.5%	9.8%	14.5%	7.2%	2.7%	3.2%	8.3%
Exports - previous three months	-19.8%	-20.0%	-12.3%	-5.3%	-7.7%	-10.8%	-3.3%	-17.7%
Exports - coming three months	-11.2%	-4.6%	-3.8%	10.4%	1.4%	-4.3%	7.9%	-6.4%
Credit availability and affordability - rated good or very good	-	-	-	19.5%	17.6%	17.4%	14.7%	12.3%
Credit availability and affordability - rated poor or very poor	-	-	-	36.5%	42.3%	44.1%	50.5%	50.9%

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

Q1

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