



SME CONFIDENCE TRACKER

SEPTEMBER 2022

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FOREWORD

SMES: AN URGENT PLEA OF THE NEW PRIME MINISTER

In our SME Confidence Tracker in April, I wrote about the challenges facing UK businesses in the wake of the conflict in Ukraine.

I also wrote about the rebounding sense of optimism following the Covid-19 pandemic. At that time, two-thirds of SMEs expected sales to increase over the coming months, with almost nine-in-ten planning to invest in 2022. It was seemingly back-to-business for many of the UK's SMEs.

Just a few months later, this optimism has retreated considerably. In its place has come widespread uncertainty and concern over the viability of many businesses (and households).

Our latest study finds confidence in short supply, with 79 per cent stating the current environment is worse than the pandemic. Today, just 49 per cent of firms believe sales will increase over the next six months.

So how have things changed so drastically in such a short period of time? Firstly, it is worth noting the already precarious position many small business owners find themselves in after two years of uncertainty. Supply chains were impacted by insolvency of customers and suppliers and the subsequent 'Great Resignation' shrank the UK labour market. In addition, already accelerating inflation due to raw materials shortages has now been

catapulted even further by an energy crisis not seen on such a scale in the 21st century.

While estimates vary, Citigroup believes inflation could reach a peak of 18 per cent by the start of 2023 - an astonishing figure demonstrating the scale of the cost of living crisis facing both individuals and businesses.

The self-fulfilling nature of inflationary cycles is borne-out in our latest research too. Two-thirds say they will be forced to pass on rising costs to customers, and a quarter say they will halt recruitment plans and impose salary rise freezes, further impacting 'real' income.

"Though our latest research reflects the stoic nature of SMEs, it is difficult to overstate the challenges facing them today."

Half say one or more of their customers has become insolvent in recent months and 30 per cent say they have experienced bad debt - non-customer payment.

This dire situation is unlikely to come as news to anyone. The warning signs have been in plain sight for months. However, the UK economy's hurdle towards recession has coincided with a leadership race in the Tory party, which saw Liz Truss triumphant in her quest to become Prime Minister.

More than two-fifths say a cut in VAT would help them to overcome challenges, and 30

per cent want the Government to consider increasing the allowance for energy grants.

As I write this, the new Prime Minister has unveiled a package of measures to support businesses and households through the energy price emergency. It includes a two-year freeze on domestic energy bills and the promise of a six-month cushion for businesses. However, what that cushion looks like is yet to be announced.

Undoubtedly, over the coming days and weeks, this will be a priority for the Prime Minister and her new team, and initial signs are encouraging. But businesses need imminent and wide ranging support now. Without this help, many SMEs are unlikely to make it to, let alone through the Winter months.

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UK MANAGING DIRECTOR,
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 Derek Ryan

HIGHLIGHTS FROM THE RESEARCH



Four in five believe the current economic landscape is worse than during the pandemic



Half would prefer lockdowns to further inflationary rises



Three quarters agree that the economic landscape is killing entrepreneurialism



Only one in ten SMEs is fully prepared for inflation-related challenges if inflation rises again



12% are making redundancies as part of their cost-cutting measures



63% say they will be forced to pass on inflationary pressure to customers in the form of price increases



37% of businesses are 'Just About Breaking Even' - 46% of female owned/run businesses say they are 'Just About Breaking Even', compared with 33% of their male peers.



THE DEATH OF ENTREPRENEURIALISM

Every economy relies on the innovation of a group of individuals driven by an aspiration to succeed. For many who start and run small businesses, there is a common desire to create an enterprise with a lasting legacy for future generations. A legacy that will provide long-term stable employment, and financial and social benefit to the local communities in which they operate.

By and large, these individuals share a common spirit of enterprise and a flare for spotting an opportunity backed by the energy, enthusiasm and skill to convert that opportunity into a successful business.

However, one of the starkest findings of our recent survey is that this drive to launch and build a new business is being seriously eroded. More than three quarters (76%) of respondents agreed or strongly agreed with the statement that today 'the economic landscape is killing entrepreneurialism'. This threat is felt most keenly in some of the country's most important sectors, such as construction, where the figure is 82%; and in certain parts of the UK, such as Wales, where 87% of respondents acknowledged the survey hypothesis.

The reasons behind these numbers are obvious. Today, historically high inflation and crippling energy costs are forcing a radical reappraisal of the underlying conditions for doing business. For 80% of respondents, the current economic climate is worse than during the thick of the pandemic, with this sentiment being particularly marked for smaller enterprises with fewer than 10 employees. Qualifying the scale of this issue, half of all respondents favour two more lockdowns over further inflation rises.

For an increasing number of SMEs, the challenges of keeping their heads above water and their businesses afloat are evidently tough. In certain cases, they may even seem insurmountable.

Asked to describe the status of their businesses, 37% claimed to be 'just about breaking even' (JABE). A more detailed review of the data shows pockets of deeper distress. Notably, there seems to be something of a gender split. Almost half (46%) of female owned businesses say they are 'JABEs', compared with 33% of their male peers. Results differ by sector, also. Looking across the UK economy, 44% of wholesale businesses and 38% of those in construction describe themselves as JABE. At a regional level, the greatest number of JABEs are in London (49%) and the West Midlands (44%).

Similarly, in total, nearly half (47%) of respondents do not describe themselves as a profitable business today, compared with 52% six months ago. In certain parts of the country, this sentiment is even more pronounced. London and the West Midlands both register the highest percentage (57%) of businesses to not consider themselves as profitable.

UK Plc is heavily dependent on its 5.6m SMEs to create jobs and expand the wealth of the country. Any hint that existing business owners - or those who might once have been motivated to set up a new company - are disinclined to continue with their ambitions, could be calamitous.

Such statistics are a clear indication of the urgent need for the Government to consider carefully how it might step in to alleviate the increasing burden for SMEs - especially to find effective ways to stem the tide of the mounting cost pressures witnessed by businesses over the past few months. The alternative would see a growing number of insolvencies and redundancies, at a time when we need to see UK SMEs firing on all cylinders.



COSTS, CUT-BACKS AND WANING CONFIDENCE

The current economic environment and prevailing mood of uncertainty have significantly dampened SME confidence. In a few short months, what many might have been hoping was a cautiously optimistic post-pandemic bounce seems to have rapidly lost much of its verve.

Taking sales as a proxy for both business activity and revenue, our survey indicates a noticeable deterioration since we conducted our previous survey in April. A quarter (25%) of SMEs say they've experienced a fall in sales volumes over the past six months. And even though 43% of respondents saw sales increase during the same period, this is notably lower than the 56% who reported an uplift in sales in the Spring.

Perhaps more worrying still, is a palpable sense of a deterioration in future expectations - a mood shift of the sort that has the potential to drive self-fulfilling prophecies. The evidence from SMEs in our survey may be echoing that of the many pundits signalling a coming recession.

While one third (32%) of survey respondents anticipate that sales will remain at current levels, 19% think sales will fall in the coming six months. Only 16% of SMEs believe sales will increase significantly. When we asked the same question in April, a surprising 67% expected to benefit from a 'slight' or 'significant' sales uplift between then and now.

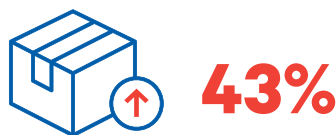
Addressing the key concern of rampant costs, SMEs are taking resolute action. Nearly half (47%) of our respondents are passing costs on to customers in the form of higher prices. Though likely a last resort, for many this will be the most direct, and possibly the only really effective means of minimising the burden in the short-term. Similarly, just over one in four SMEs (43%) are trying to find ways to reduce costs. A further 22% are re-evaluating their finances and funding sources, and 19% are deferring hiring. In what could be a significant blow to current levels of employment, 12% of SMEs are making redundancies as part of their cost-cutting measures, which could equate to approximately 672,000 potential lost jobs.

In the face of further inflationary rises - which it is estimated could reach 18% by the beginning of next year - SMEs plan to take even more drastic action. Cost management is a key factor for many in finding ways to remain resilient. A substantial 63% say they will pass on higher costs to their customers if inflation rises again. Arguably, of greater concern for the future economic prospects of the UK, 26% of respondents say they will freeze recruitment, salaries and promotions. Moreover, 23% of SMEs claim they'll curb any investment plans they may have had in the pipeline.

The gathering inflationary storm could exacerbate ongoing concerns many SMEs have in relation to managing their cashflows. Unsurprisingly, 17% of respondents say they'd be likely to require short-term lending to help them navigate these challenges. Others, exercised by the reality of having to service existing business debt facilities, are also searching for ways to reduce this strain. This means that 29% of SMEs are currently paying down existing government loan schemes by restructuring financing arrangements, and 6% will seek alternative finance to avoid defaulting on their loan repayment obligations in the future.



A quarter of SMEs say they've experienced a fall in sales volumes over the past six months



43% of respondents saw sales increase during the same period



One third of our survey respondents anticipates that sales will remain at current levels



A substantial 63% say they will pass on higher costs to their customers if inflation rises again

THE FIGHT FOR SURVIVAL



While most businesses aim to invest for growth, the current economic landscape is significantly weakening their ability to do so. For a substantial minority (41%), concerns over the spiralling costs of doing business lie at the root of their decisions to refrain from investing. For others, the adverse conditions simply mean it's a fight for survival. Our survey points to two principal roadblocks for all small businesses, whether they're struggling just to keep the doors open or to fulfil their growth ambitions.

In the first instance, SMEs are increasingly battling with the scourge of limited cashflow. For 36% of respondents there is insufficient cashflow within their businesses to provide the headroom for investment, or indeed, to even operate efficiently. Just over one in four (44%) female-run businesses don't have the cashflow required to grow or to manage on a day-to-day basis, versus 32% of their male counterparts.

Consequently, more than a quarter (26%) of all respondents say they will not invest in their businesses over the coming months. In the Spring, only 14% said the same thing. This comparison brings into sharp relief the extent to which attitudes have hardened over a relatively short timeframe.

Part of the diminishing revenue story could be explained by a demonstrable rise in the number of respondents' customers who have become insolvent. Again, around one in four (42%) SMEs explain that between one and 10 of their clients have failed within the last six months.

Furthermore, the proportion of businesses that have suffered from bad debt has risen from 28% in the Spring to 30%, with the average sum written off by SMEs standing at £11,712, up from £10,329. This represents increasing pressure on SME supply chains throughout the country. With increasing inflationary pressure and overheads expected to rise further over the months - despite government intervention introduced to offset these costs - SMEs should consider how they can insulate themselves from bad debt, be it through securing appropriate trade credit insurance or bad debt protection on offer by the private sector.

The second, and arguably more pernicious barrier to investment and growth, remains the prospect of yet higher inflation in the coming months. Only one in ten (11%) businesses are fully prepared for inflation-related challenges.

A look at the regional data splits reveals a more nuanced and, possibly more troubling, picture. In the South-West and Wales - the two regions with the lowest rates of inflation readiness - this figure drops to 5% and 3%, respectively.

It's a fair assumption that this situation will worsen before it improves, further limiting the potential of many SMEs to survive and grow.

However, there is clear evidence that in the face of strengthening headwinds, SMEs are planning to seek third-party funding to bridge the gap in their working capital. A third (33%) of respondents say the current economic environment makes them either 'significantly more' or 'more' likely to use external finance to support their businesses. For those that have invested in their companies since the cost of doing business crisis began, that figure rises to 60%. In general, a little less than half of SMEs seeking funding (45%) say that up to £100,000 would suffice to support their businesses for the remainder of this year. But for external financing to be effective, SMEs will need to know they can readily find and rely on funding sources that most effectively match their requirements.

SUPPORT FROM GOVERNMENT URGENTLY REQUIRED

Much of the data in our survey reinforce several consistent themes - an economy under severe strain, hard-working SMEs struggling to cope with mounting cost pressures and, consequently, an urgent need for more support from central Government.

During the Covid-19 pandemic, swift action was taken to provide safety nets for households and businesses alike. Initiatives, such as the Furlough Scheme, Coronavirus Business Interruption Loan Scheme and Bounce Back Loan Scheme, were broadly welcomed. The fact that they undoubtedly prevented many businesses - small and large - from going under, means they are probably some of the better-known interventions from government.

Given the dire circumstances facing many businesses today, what's perhaps surprising is that many SMEs are much less aware of - and /or have accessed - the raft of other Government packages from which they could benefit.

Under a quarter (22%) of respondents claim to be unaware of various sources of potential help (including: Gov.uk website, R&D tax credits, employment allowances, various loan schemes, Local Enterprise Partnerships, and national support programmes like Innovate UK). Across the nation, some regions are even less well informed, with this figure jumping to 30% in East Anglia.

Similarly, in terms of access, nearly a third (32%) of SMEs overall have never tapped into any of these initiatives and have thereby missed out on what could have been a vital boost in very challenging times. The two regions with the highest rate of non-access to Government initiatives are East Anglia and the South West (both at 42%). The construction sector has the greatest proportion of businesses who haven't accessed support at 39%.

What is strikingly evident from these numbers, and our broader conversations with clients, is that the Government needs to be much better at communicating what's available in terms of help for SMEs. Seemingly, it also needs to broaden the existing range of initiatives it provides, as well as making some of them significantly easier to access.

Our survey makes plain what type of assistance SMEs feel would be most effective. Providing an extension to the VAT cut is a favourite choice, selected by 44% of respondents. This is closely followed by increasing tax relief options (40%) and providing affordable financial support (36%). Unsurprisingly, given the current laser focus on costs, 30% of SMEs would like to see an increase in the allowance for energy grants. The new Government's recent proposal to introduce an energy price freeze that covers SMEs as well as households, will no doubt go some way to meeting this need. However, at this juncture, the devil of this headline-grabbing policy is still in the detail.

As a close partner to 7,000 SMEs in the UK, we back these suggestions wholeheartedly. We also invite those with the power to make a consequential difference to the long-term viability and success of SMEs to go further still. At the strategic level, we see a burning need to address underlying and long-standing systemic failures in the business environment.

Specifically, we would advocate that:



Over the long-term, the energy regulator, Ofgem, more effectively regulates and monitors the energy market in the UK.



The new Government carries out a root and branch review of fiscal policy in relation to business, including a reassessment of the extent to which measures such as Business Rates are still fit-for-purpose given the very diverse range of SMEs currently in business across the UK.



Both the public and private sector work more closely together to raise awareness of all forms of financial support available to SMEs, including finance options available from non-traditional sources.

SMEs demonstrated stoic resilience during the pandemic, in large part thanks to the Government's intervention, and the provision of loans, grants and furlough payments. But now they are on the brink of an even greater crisis without a lifeline. Government intervention alone, however, cannot fix this problem and it will involve true collaboration with SMEs from both the public and private sector alike.

METHODOLOGY

This study is based on a poll of 500 UK SME owners and decision makers across the manufacturing, construction, wholesale, transport and services sectors.

Research was conducted by independent specialists, Critical Research. The survey questionnaire was circulated to respondents between 11 and 17 August 2022.

ABOUT BIBBY FINANCIAL SERVICES

Bibby Financial Services (BFS) is a leading independent financial services partner to over 9,000 businesses worldwide.

We provide specialist and adaptable trade, asset and working capital finance, FX and insurance services helping businesses to grow in domestic and international markets.

Formed in 1982, BFS is part of the Bibby Line Group (BLG), a diverse and forward-looking family business delivering personal, responsive and flexible customer solutions for over 200 years.

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