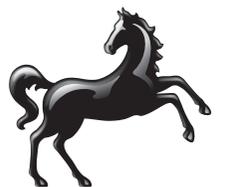


COMMERCIAL BANKING

Business in Britain

A survey of opinions and trends
49th edition January 2017

For your next step



LLOYDS BANK

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INTRODUCTION



Tim Hinton
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Welcome to the latest half-yearly Lloyds Bank Business in Britain survey, now in its 25th anniversary year, which offers insights on the recent performance and expectations of UK businesses, especially small and medium-sized enterprises (SMEs). Our survey is based on the responses of 1,500 firms, drawn from all sectors and areas of the country.

Since the survey started in 1992, the country has seen its fair share of economic and political shocks, from the recession in the early 1990s to the dotcom bubble in 2000 and global financial crisis from 2008. Last year was no stranger to important events, in which Britain voted to leave the EU and the US voted Donald Trump as the next President – results which commentators and pollsters did not expect.

We can expect more twists and turns to come in 2017 as businesses wait for further details of Britain's exit from the EU but in the meantime business owners are doing what they do best – taking growth opportunities when they arise and keeping an eye on external risks.

Our latest survey shows that business confidence has risen slightly since the last report, which was conducted shortly after the EU referendum result, but remains below the long-term average as firms cite economic uncertainty as the single greatest threat to their business. Nevertheless, it is important to put this into context, whilst sentiment has fallen it remains well above the lows of the financial crisis in 2008/09.

I hope you find the report useful. We look forward to supporting you with your strategic plans and wish you every success in 2017 and beyond.

EXECUTIVE SUMMARY

- The report's confidence index – an average of respondents' expectations of stronger sales, orders and profits in the next six months – rose to 14%, having fallen to 12% in the previous survey conducted shortly after the EU referendum outcome. It nevertheless remains below the long-term average and points to a possible slowdown of economic growth in the first half of 2017.
- The news for export prospects was more positive. The net balance* of firms anticipating stronger export sales in the next six months increased to 26% from 20%. Firms indicated that the exchange rate is the most favourable for their export sales since the last sharp depreciation during the global financial crisis.
- The weaker pound has also contributed to a rise in firms' pricing intentions. The net balance of firms expecting to raise their prices in the coming six months increased to 20% from 13% and is particularly high among importing firms (28%).
- Caution prevails with respect to hiring and capital spending prospects. The net balances of firms expecting to raise their staffing and investment levels in the next six months remained near zero. Firms reported a fall in recruitment difficulties, while a smaller proportion expect average pay levels to rise in the coming six months.
- In terms of the industry sectors, business confidence is highest among firms in manufacturing and hospitality and leisure, possibly reflecting the boost to competitiveness from the weaker exchange rate. Sentiment among construction firms is also relatively high, but it is lower in the remaining services sectors, including retail and wholesale and business and other services.
- From a regional perspective, business confidence is the highest in the North East, Scotland and the East of England. The South West also registered a significant improvement in confidence compared with the last survey. Confidence is the lowest in the West Midlands and London, which is also reflected in employment intentions in those regions.

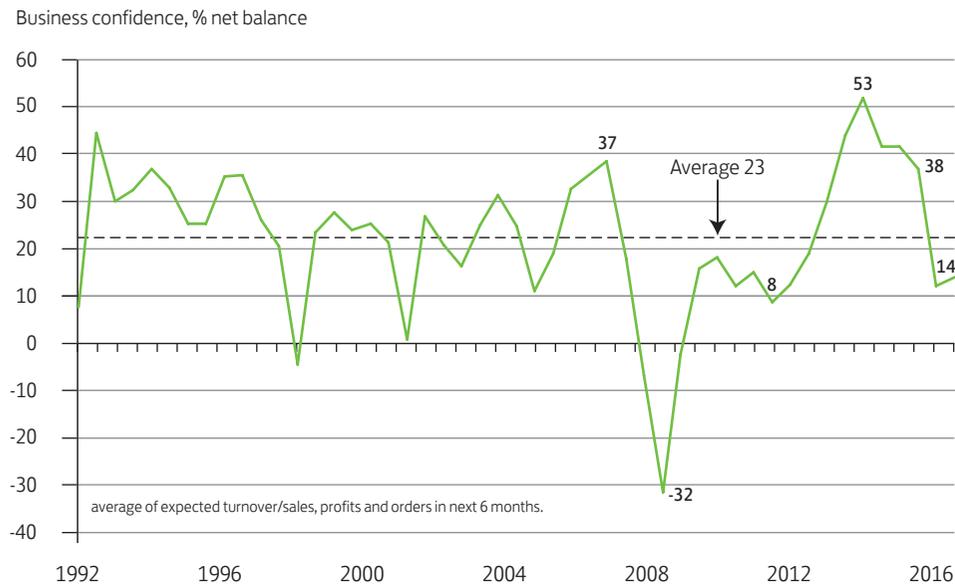
* The 'net balance' throughout this report is calculated as the difference between the percentage of positive responses and the percentage of negative responses, ignoring the middle ground. It can vary between 100% if all firms are positive and -100% if all firms are negative.



RECENT TRENDS IN THE SME MARKET

BUSINESS CONFIDENCE

OVERALL SENTIMENT STABILISES AFTER THE SHARP FALL IN THE LAST SURVEY

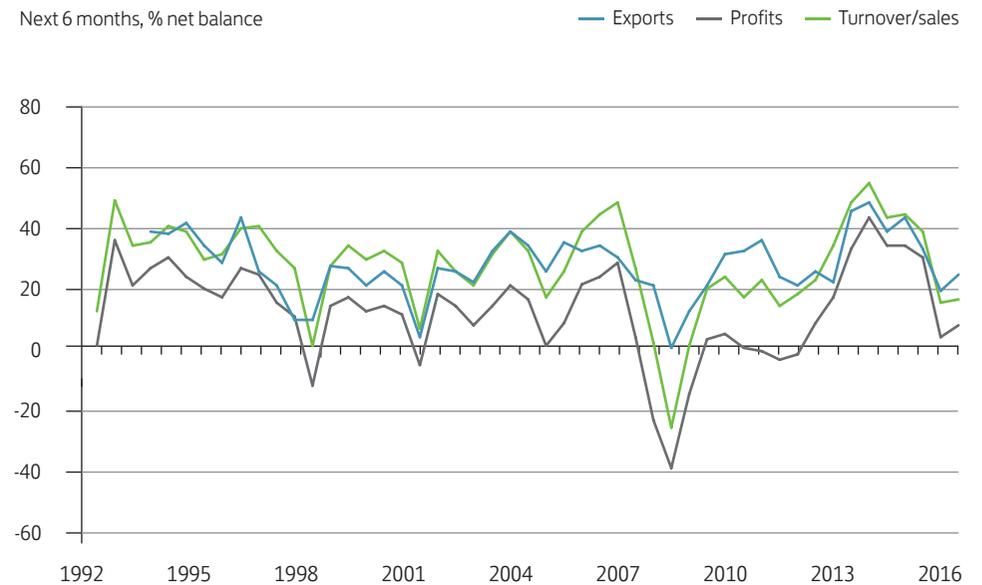


Overall **business confidence** rose slightly to 14%, following the sharp fall in the previous survey to 12% conducted shortly after the EU referendum outcome. It stays below the long-term average of 23%, however, and remains near the lowest level since 2012.

The read-across to economic growth is not precise, but it nevertheless points to a possible slowdown in economic growth in the first half of 2017.

SALES, PROFITS AND EXPORTS

EXPECTED SALES AND PROFITS STABILISE; EXPORT PROSPECTS IMPROVE



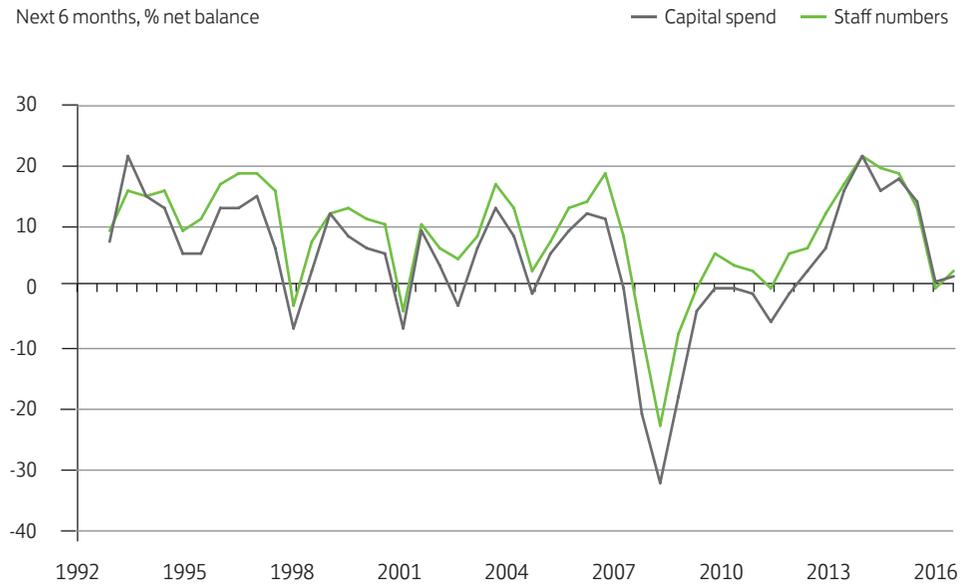
The net balance of firms reporting expectations of higher **turnover/sales** in the next six months increased marginally to 17% from 16%. It remains in positive territory, but is nevertheless the second lowest reading since 2011.

The net balance of firms reporting expectations of higher **profits** in the next six months rose to 8% from 4%, the first increase since 2014, but it remains somewhat weaker than in the previous three years.

The net balance of exporting firms reporting expectations of higher **exports** in the next six months increased to 26% from 20%. It suggests that external demand could be an increasingly important driver of overall growth, helped by the sharp fall in the pound over the past year.

STAFFING LEVELS AND CAPITAL SPENDING

HIRING AND INVESTMENT CAUTION PREVAILS



The net balance of firms reporting expectations of higher **staffing levels** in the next six months improved only slightly, rising back to positive territory to 2% from 1%. It remains consistent with a moderation in the pace of employment growth.

The net balance of firms reporting expectations of higher **capital spending** in the next six months edged up to 1% from 0%, stabilising near the weakest level since 2012. It continues to signal sluggish business investment prospects in the coming months.

RECRUITMENT DIFFICULTIES AND AVERAGE PAY

HIRING FRICTIONS AND PAY PRESSURES FALL



The share of firms saying they are experiencing **difficulties in recruiting skilled labour** fell quite sharply to 31% from 38%, a third consecutive decline to the lowest level since 2013. The decline may partly be related to weakness in firms' hiring intentions.

The share of firms saying they are experiencing **difficulties in recruiting unskilled labour** edged down to 14% from 15%, the lowest level since 2014.

Consistent with lower recruitment difficulties, the net balance of firms reporting expectations of higher **average pay** among its staff in the next six months fell to 12%, compared with 14% in the previous survey and 27% a year ago.

EXPORT SALES

EXPORTS EXPECTED TO IMPROVE ACROSS ALL MARKETS

Exports next 6 months, % net balance

— Europe — Asia-Pac — LatAm
— US/Can — Non Europe* — ME/Afr



The net balance of firms reporting expectations of higher exports in the next six months improved for **all markets**, most notably for the Asia-Pacific.

The highest net balances are for the **Asia-Pacific** and **US and Canada**, both at 18%, followed by Europe (14%), Middle East and Africa (9%) and Latin America (6%).

EXCHANGE RATE IMPACT

THE EXCHANGE RATE IS MORE FAVOURABLE FOR EXPORTS

FX impact on exports, % firms saying 'positive'

— Pound vs US Dollar — Pound vs Euro



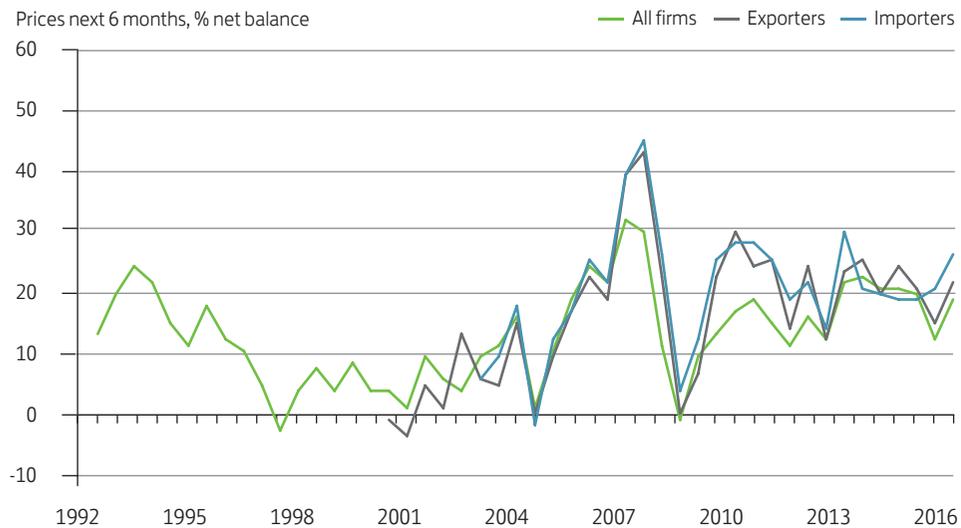
The share of exporting firms saying that the exchange rate against the **US dollar** is 'positive' for their exports increased to 44% from 38%. This is a higher share than after the last sharp depreciation of sterling in 2008.



The share of exporting firms saying that the exchange rate against the **euro** is 'positive' for their exports increased to 42% from 35%. This is the highest level since 2009.

PRICING INTENTIONS

A GREATER SHARE OF FIRMS EXPECT TO RAISE THEIR PRICES



The net balance of firms anticipating to raise their **prices** in the next six months increased to 20% from 13%, suggesting that domestic inflationary pressures are set to rise.

23%

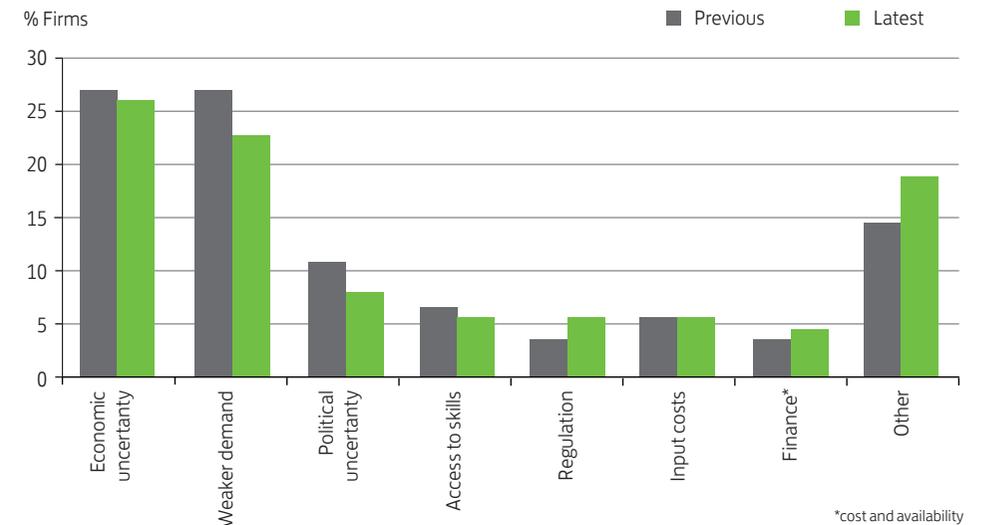
The net balance of **exporting firms** expecting to increase their higher prices in the next six months increased to 23% from 16%.

28%

The net balance of **importing firms** looking to lift their prices in the next six months increased to 28% from 22%, the highest level since 2013.

GREATEST THREATS

ECONOMIC UNCERTAINTY AND WEAKER DEMAND REMAIN THE GREATEST THREATS



Economic uncertainty was most commonly cited by firms (26%) as the single greatest threat to their business.

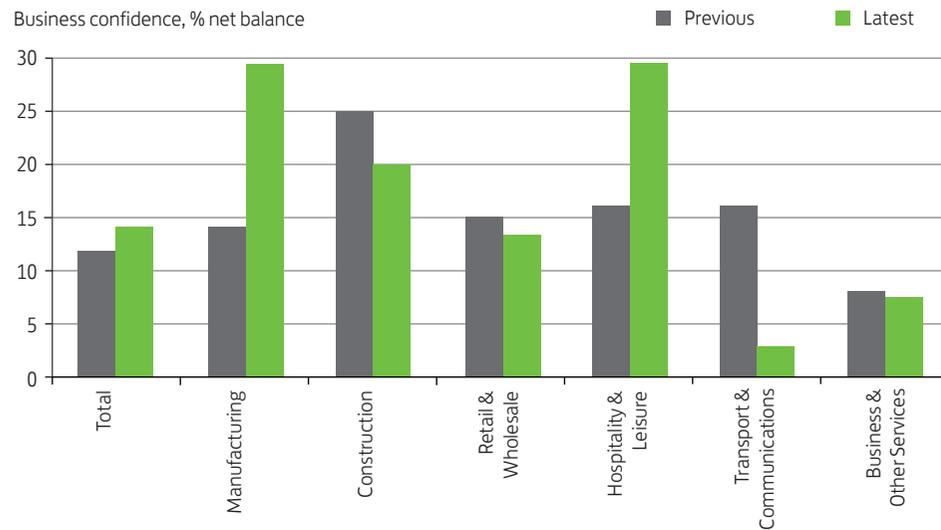
This was followed by **weaker demand** (both domestic and overseas), reported by 23% of firms, although it fell from 27% in the last survey. A smaller share of firms citing weaker overseas demand accounted for most of the decline.

Political uncertainty was cited by 9% as the greatest threat, followed by **access to skills** and **regulation**, both at 6%. The **cost and availability of finance** was given by 5% of firms.

THE SECTOR OUTLOOK

BUSINESS CONFIDENCE

SENTIMENT HIGHEST IN MANUFACTURING AND HOSPITALITY AND LEISURE



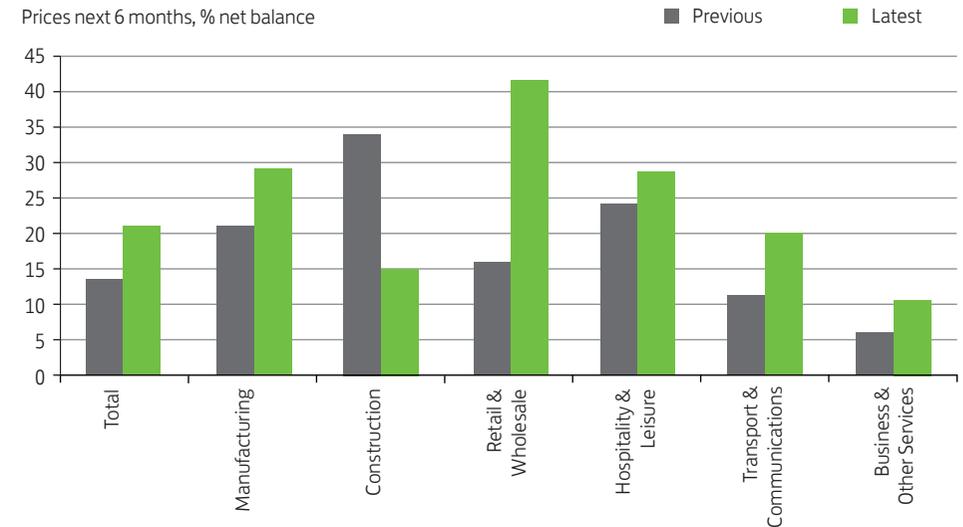
Manufacturing has seen a sharp rise in business confidence since the last survey. Confidence has risen strongly from 14% to 28%, possibly reflecting the boost to competitiveness from sterling's depreciation.

Confidence in the **hospitality and leisure** industries has also seen a strong gain from 16% to 28%, possibly due to expectations of a rise in foreign tourists helped by the fall in sterling.

For all other sectors, confidence has fallen, but the declines are generally small. The lowest confidence levels are for **transport and communications** and **business and other services**.

PRICING INTENTIONS

PRICE EXPECTATIONS RISE SHARPLY IN THE RETAIL AND WHOLESALE SECTOR



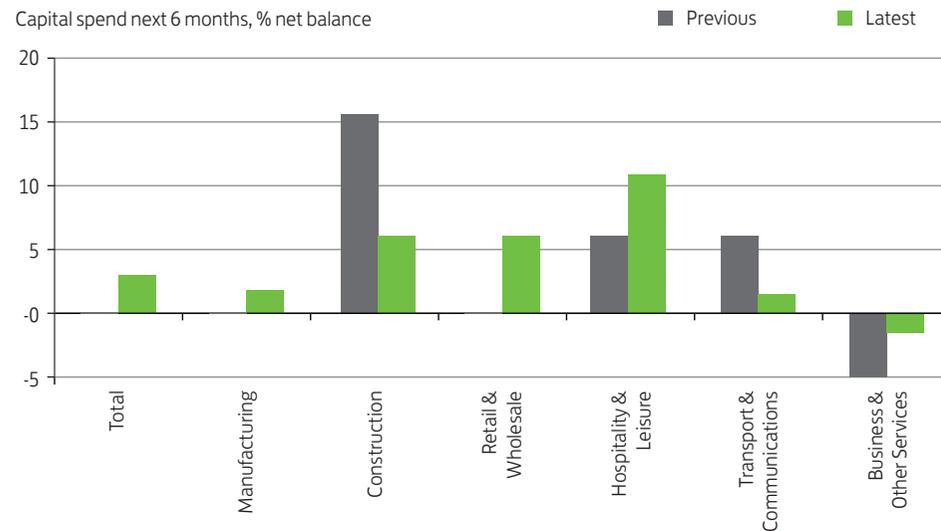
All sectors, apart from **construction**, reported an increase in the net balance of companies expecting to raise prices in the next six months.

The **retail and wholesale sector** has seen the net balance of firms expecting to raise prices rise to 40% from 17% previously, its highest level for almost five years, reflecting the impact of sterling's recent depreciation.

The net balance of **manufacturing** firms expecting to raise prices has risen to 29% from 20% previously. This is an indication that some firms in sector plan to use the competitiveness boost from the weaker pound as an opportunity to expand their profit margins.

CAPITAL SPENDING

CAUTIOUS INVESTMENT INTENTIONS ACROSS MOST SECTORS FOR NEXT SIX MONTHS



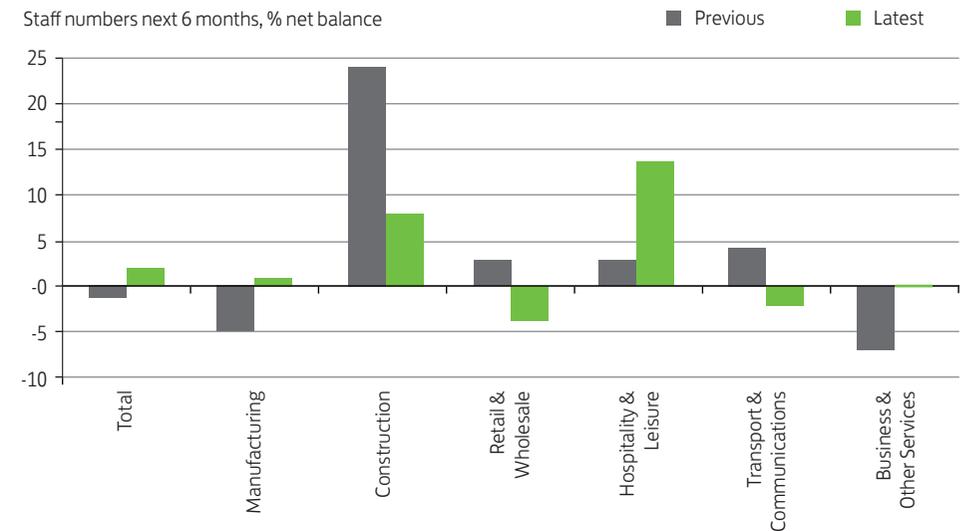
Most sectors still have relatively cautious investment plans. However, in all but one case, the net balance is higher than the previous survey.

Construction has seen a fall in the net balance to 6% from 15% previously, but that still leaves its investment balance above all but two other sectors.

Hospitality and leisure (10%) has the highest net balance, followed by **retail and wholesale** (6%). The higher plans of both may partially reflect an expectation of a boost to demand from foreign tourists.

STAFFING LEVELS

MOST SECTORS ARE ALSO CAUTIOUS ABOUT RAISING THEIR STAFFING NUMBERS



Employment intentions across sectors remain mixed, with three areas reporting a positive net balance, while three have a negative or zero net balance.

Hospitality and leisure has by far the highest net balance at 13%, up from only 3% in the previous survey.

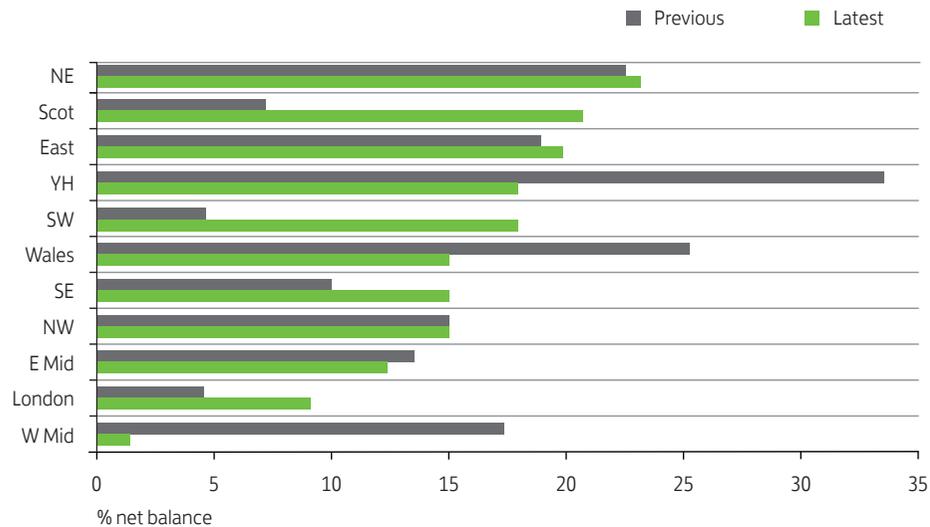
Construction also has a significant positive balance of 8%, but it fell significantly from 24% in the last survey.

Reflecting generally cautious hiring intentions, both the **retail and wholesale** and the **transport and communication** sectors have small negative net balances.

THE REGIONAL PICTURE

BUSINESS CONFIDENCE

BUSINESS CONFIDENCE UP IN MOST REGIONS

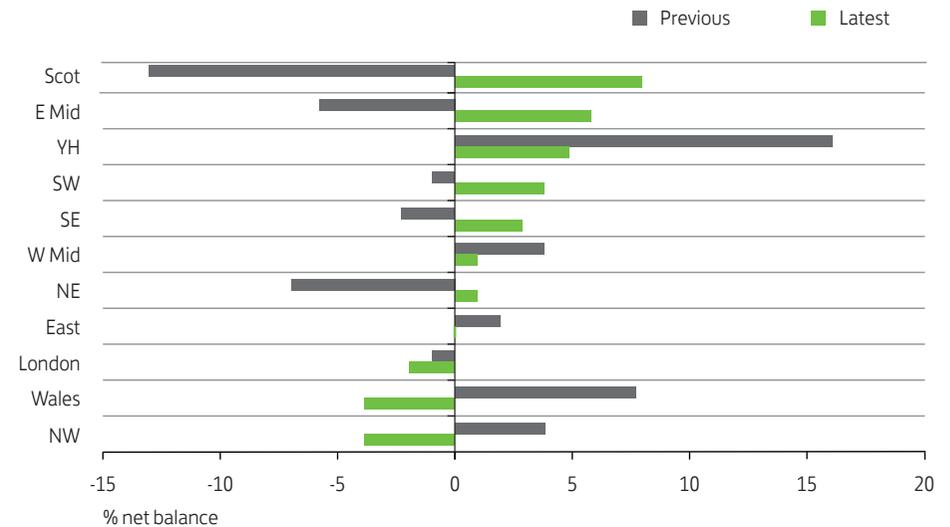


Overall **business confidence** is the highest in the **North East** (22%), followed by **Scotland** (21%) and the **East of England** (20%), all reflecting improvements compared with the last survey. The **South West** also showed a large rise in confidence (17%), though from a relatively low level previously.

The weakest levels of confidence are in the **West Midlands** (1%), London (9%) and the **East Midlands** (12%). Confidence fell particularly sharply in the West Midlands compared with the last survey. Confidence also fell sharply in **Wales** (15%) and **Yorkshire and the Humber** (17%), though from relatively high levels. Hence, their confidence levels are near the national average.

CAPITAL SPENDING

OUTLOOK REMAINS CAUTIOUS ACROSS THE REGIONS

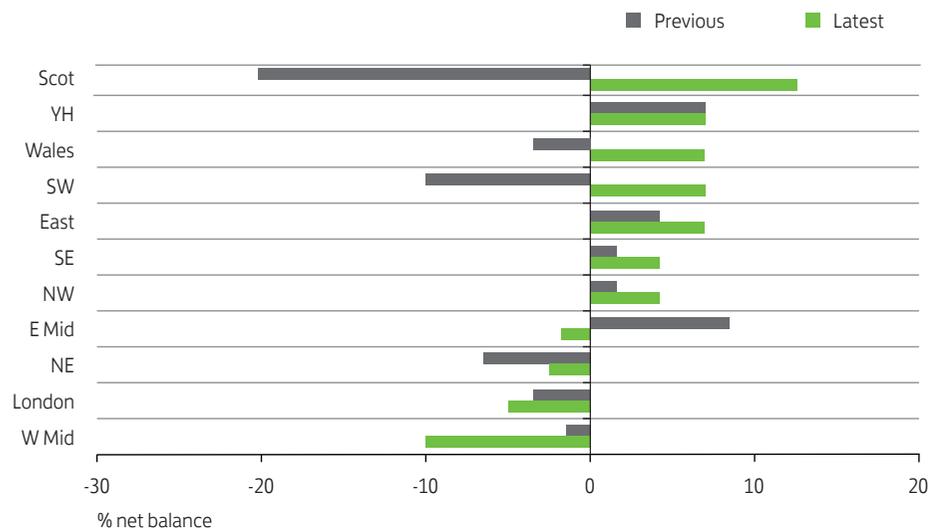


Firms across the regions remain cautious about their capital spending plans. The highest net balance of firms reporting expectations of higher capital spending are in **Scotland** (8%) and the **East Midlands** (6%). This is followed by **Yorkshire and the Humber** (5%), despite the decline compared with the last survey.

In contrast, negative net balance levels are reported in the **North West** (-4%), **Wales** (-4%) and **London** (-2%). All these regions reported lower net balances compared with the last survey. Despite weak overall business confidence, the net balance for the **West Midlands** (1%) is the same as the national average.

STAFFING LEVELS

EXPECTED STAFFING NUMBERS RISE IN MOST REGIONS

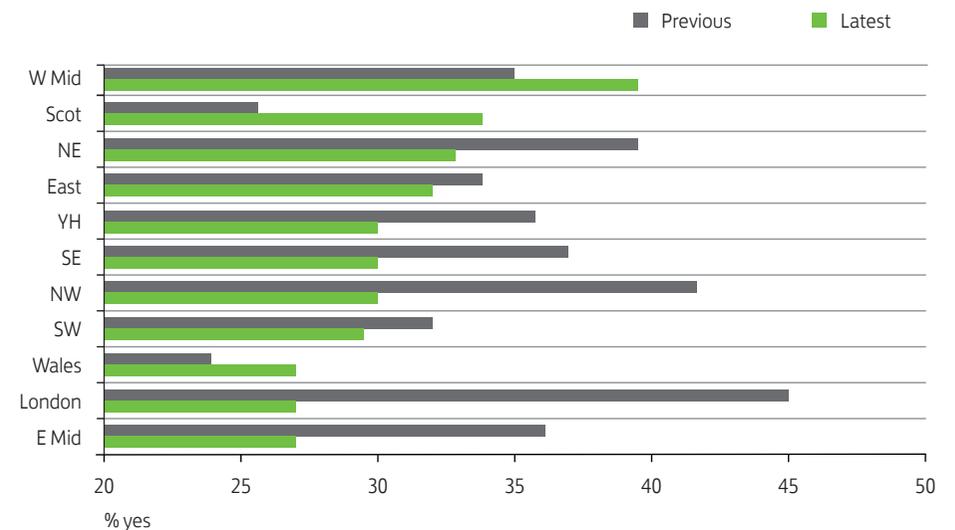


There is a significant turnaround in employment intentions in **Scotland**, where the net balance rebounded by 32 percentage points to 11%, consistent with the rise in overall business confidence. The next highest net balances are in **Yorkshire and the Humber, Wales, the South West and the East of England** – all at 6%.

Four regions reported negative net balances, including the **West Midlands** (-10%) and **London** (-5%) and the **East Midlands** (-1%), consistent with relatively low levels of business confidence in those regions. The net balance is also negative in the **North East** (-2%), despite strong business confidence.

RECRUITMENT DIFFICULTIES

RECRUITMENT DIFFICULTIES FALL SHARPLY IN LONDON



The share of firms saying they are experiencing **difficulties in recruiting skilled** labour fell in all but three regions. The largest declines are in **London** (down 18 percentage points), the **North West** (down 12 percentage points) and the **East Midlands** (down 9 percentage points).

Firms in the **West Midlands** (39%) reported the highest level of recruitment difficulties, yet firms in the region are the most negative about expected staffing levels.

Recruitment difficulties are also high in **Scotland** (34%), consistent with strong employment intentions.

In contrast, the lowest share of firms reporting recruitment difficulties are the **East Midlands** and **London**, both at 27%, consistent with weak expected staffing levels in those regions. Recruitment difficulties are also low in **Wales** at 27%, despite relatively strong expected staffing levels.

Find out more

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