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THE SME BAROMETER

QUARTERLY SMALL & MEDIUM SIZED BUSINESS INSIGHTS. AUTUMN 23.

ARE WE THERE YET?

THE YEAR SO FAR FOR UK SMEs

IN THIS ISSUE...

Business confidence hit by poly-crisis

New era of global trade

Start-ups transform the business scene

The challenges ahead

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FOREWORD

As the fight against inflation continues to heighten recessionary fears, the Bank of England's decision to hold interest rates in September amidst the unexpected fall in inflation sees SMEs racing for resilience as commentators predict the UK will avoid a recession, but the near-stagnation of the economy will mean it won't feel much different.

Constant hikes in the cost-of-borrowing have had a hugely detrimental impact on SMEs, and businesses will be giving a cautious welcome to the Bank of England's action to hold the base rate at 5.25%. The Monetary Policy Committee (MPC) voted five to four in favour of holding rates steady, with four members preferring a 0.25% rise to 5.5%. Additionally, MPC voted to reduce the amount of government bonds held under quantitative easing (QE) by more than 10% over the next 12 months.

"The vote to trim QE by some 13% will tighten monetary policy a touch, and that may have given some swing voters the space to hold rather than hike," comments Nicholas Hyett, Investment Manager at Wealth Club. "From here there's a strong argument for the Bank taking a prolonged pause. Fixed rate mortgages and a higher proportion of mortgage free owner occupiers mean higher rates don't feed through to the economy as quickly as they once did, and the full impact of past interest rate hikes hasn't been felt yet."

"The risk of the 'lag effect' on interest rate hikes means that the decision to hold rates may not be felt for another 9 to 12 months," agrees Giles Cognlan, Chief Market Analyst, HYCM. "As such, with economic growth already faltering and core inflation remaining high, there is the continued risk of overtightening the economy and inducing a period of stagflation further down the line."

Holding interest rates is good news for SMEs, but the story is far from over.

"

RISHI SUNAK AND JEREMY HUNT'S TARGET OF BRINGING INFLATION UNDER 5% BY THE END OF THE YEAR IS LOOKING INCREASINGLY OUT OF REACH,

and that will have implications on consumers, investors, businesses and the financial markets," warns Jatin Ondhia, CEO, Shojin.

PRISM research found the stability of the economic climate as the top concern cited by 92% of SME leaders with 46% saying they worry that the UK does not have the right balance of support for the SME sector.

Source: PRISM research

"With inflation proving more persistent than was previously expected, and more firms starting to experience the negative impact of rising interest rates, there is a greater sense of caution in the air than in the spring," says Kitty Usser, Chief Economist, Institute of Directors (IoD).

Following a sharp fall in core inflation in August and with signs that the labour market is cooling, the Bank of England has finally pushed the big red pause button, prompting a rush of relief for companies and consumers bearing the brunt of higher borrowing costs.

"The surprise drop in inflation over the year to August, despite the upwards march in oil prices, saw the Bank of England fast forward its decision to halt the relentless rise in interest rates," says Susannah Streeter, Head of Money and Markets, Hargreaves Lansdown. "The sharp fall in core inflation, stripping out volatile food and fuel prices, clearly took policy makers by surprise given that last month only one policy maker had voted for a pause."

For the SME sector, the cost of borrowing is cited as a major financial challenge by 74% of firms. (PRISM research). "The sharp increase in the cost of borrowing over the past year and a half has already left many SMEs in real difficulty, but hitting the stop interest rate button in a panic will not make an immediate economic turnaround," warns Nick Hood, Senior Advisor, Opus Business Advisory Group. "The reality is that the UK economy is bumping along the bottom and may be heading for a shallow recession as we move into 2024. Recent predictions by both the well-respected S&P Purchasing Managers Index and KPMG have warned about a downturn later this year and possibly throughout 2024."

"The economic signals are horribly mixed: unemployment is sharply up but job vacancies are down. GDP fell by 0.5% in July but was up 0.2% in the quarter to then. Worryingly, a survey by the British Chambers of Commerce of consumer-facing businesses reported that **61% were being negatively impacted by interest rates,** which may not go much higher but are already too much for some over-indebted companies to bear," says Hood.

"After GDP growth in June was boosted by the month having one extra working day compared with May and a rise in manufacturing output, July had seemed destined for a reversal. In practice, a 0.5% month-on-month fall in GDP that month was bigger than the consensus expectation of a 0.2% decline," adds Martin Beck, Chief Economic Advisor, EY ITEM Club.

"The sectoral breakdown showed a 0.5% fall in services output accounted for much of the fall. A steep decline in health output was the main culprit here, reflecting the effect of strikes (the total number of working days lost in July was at a three-month high and 75% more than in June). A drag from unusually wet weather on retail spending may have also exaggerated services' weakness. The wet weather probably also played a role in a 0.5% contraction in construction. Meanwhile, industrial output fell 0.7%, meaning all three main sectors shrank for the first time since June 2022."

"The role of erratic factors in July's weakness means the economy probably saw some bounce back in August. But it's now looking less clear that GDP will expand meaningfully in Q3," continues Beck. "Any growth is on course to be very modest, continuing the trend of near stagnation which has characterised the UK economy over the last 12 months – and the EY ITEM Club thinks that prognosis will remain broadly true over the rest of this year and into 2024."

"Companies need reassurance that decisions on interest rates are not knee-jerk reactions to the most recent inflation data," comments Shevaun Haviland, Director General of the British Chambers of Commerce (BCC). "We need clear direction from decision makers, creating a roadmap for business that really boosts confidence and investment."

The debt cloud continues to put SMEs at risk. Record levels of global debt has got much worst since the pandemic and the cost of raising finance has risen. Higher interest rates directly affect a company's ability to obtain lending, and whilst some companies had been fortunate in locking in abundant financing during the long stretch when rates were near zero, so they don't have to worry about refinancing in the short-term, others have not been so lucky, and debt burdens are getting heavier.

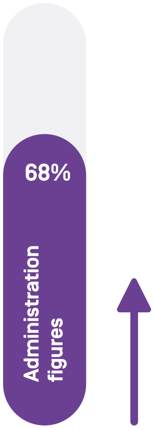
With company insolvency numbers now returned to and exceeding pre-pandemic levels, the month of August 2023 witnessed 2,308 company insolvencies compared to 1,941 for the same month the year before.

source: https://www.gov.uk/government/statistics/monthly-insolvency-statistics-august-2023/commentary-monthly-insolvency-statistics-august-2023)

With company insolvency numbers now returned to and exceeding pre-pandemic levels it is a bleak reminder of what is to come.

In August there were 1,880 Creditors' Voluntary Liquidations (CVLs), 544 more than the previous month, and 13% higher than in August 2022. "Corporate insolvency figures for August were their highest for this month in four years as a mixture of long-term economic issues, director fatigue and creditor pressure saw more companies enter an insolvency process in an attempt to resolve their financial issues or shut their doors," says Nicky Fisher, President of R3, the UK's insolvency and restructuring trade body.

"Creditors' Voluntary Liquidations remain high as more and more directors choose to wind down their firms, while compulsory liquidation numbers were at their highest this August for four years as creditors continue to pursue the money they are owed."



Administration figures for August 2023 are 68% higher compared to a year ago, and greater than those pre-pandemic. "August's administrations figures were the highest monthly figure we've seen since January 2019, which is a sign that more and more businesses are at a point where they are in need of specialist help to survive – and that a sale or a liquidation may be their only options," continues Fisher. "Our message to directors is simple: be alert to signs your business could be financially distressed and seek advice as soon as they show themselves. If you're having problems paying wages, staff, or suppliers, if stock is starting to pile up, or if you're worried about your business and its finances, that's the time to speak to a qualified advisor."

SMEs are being hit from every angle and each blow is damaging their chance of survival. "Nothing about the latest insolvency statistics for August 2023 is good. They were up a third on July and two thirds above the pre-pandemic figures for August 2019. At the current rate, which may well accelerate, we are heading for 26,000 business failures this year, the second largest annual total on record," says Hood.

"Digging down into the numbers, the sector most badly affected so far this year has been construction, the perennial winner in this grotesque beauty parade. It accounted for 18% of all corporate insolvencies. Next came two consumer-facing industries: hospitality at 15% and retail with 9%. This means that well over one in four failures have been directly affected by the cost-of-living crisis, when other sectors like leisure, sport, arts and entertainment are also taken into account."

Worries about economic uncertainty continue to impact SMEs with 40% of firms saying they are considering exiting their businesses citing 'director fatigue' as the main factor impacting on their mental health. This is surprising given that 72% of firms do not have an exit strategy.

Source: PRISM research.

According to the Funding Circle's Resilience in Small Business Report, prioritising wellbeing is vital if a small business is to flourish. Improving mental health through therapy sessions was popular amongst younger leaders, with one in five (21%) 18-24s having used therapy sessions compared to no one (0%) in the over 65 age bracket.

With research showing that 88% of SME leaders plan to focus on mental health in the next 12-18 months, the Funding Circle has teamed up with Thrive Mental Wellbeing, an app trusted by the NHS to help give small business leaders and their employees access to free help with their mental health.

source: https://www.fundingcircle.com/uk/resources/wp-content/uploads/2023/04/Resilience-In-Small-Businesses-Funding-Circle-2023.pdf).

Money worries impact both businesses and consumers. Slowing price rises have yet to reach consumers with any real meaning. Many popular brands are already suffering from shrinkflation and firms are reducing the size of products in a bid to curb passing on the rising raw material costs to consumers, but with prices already risen to a premium, consumers have yet to see a drop in household spend at the tills.

"Annual headline Consumer Price Index (CPI) inflation reached 11.1% in October last year, but it has since fallen by over 4 percentage points. August's data saw headline inflation surprise on the downside, printing 6.7% year-on-year (versus the consensus expectation of 7.0%). The Prime Minister's pledge to halve inflation this year, from 10.1% in January to approximately 5% in December, looks to be on track; economists expect inflation to average 4.5% in the fourth quarter of this year," says Rob Clarry, Investment Strategist, Evelyn Partners.

"A key threat, however, comes from the energy sector. The price of oil has increased in recent months as Saudi Arabia and Russia extended voluntary supply cuts to the end of this year. This comes on top of cuts agreed by OPEC+, a group of oil exporters, to the end of 2024. Higher oil prices typically take around one month to feed through to petrol prices, so we can expect to see higher prices in the coming weeks and months," warns Clarry.

"Another lingering source of inflation in the UK comes from rents, which have yet to peak. Having said that, we still expect inflation to ease in Q4; lower energy costs following the October change to the Ofgem price cap will help households across the country."

With Winter approaching charities are bracing themselves for the influx of demand as households continue to be hit by increase in mortgage payments and rent, high food bills, and the likelihood of even higher energy costs. Consumers may be spending less in a bid to drive down inflation, but the downside is – they are also spending less with SMEs.

As the Bank of England holds interest rates, the cry from the backseat is "Are we there yet?" As we continue to put 200 SMEs under the microscope, the answer is clear: there is still quite some way to go before the business community can revel in the stability and growth which it so desperately needs. In Q3 2023, SMEs will be under greater pressure, so buckle up – the ride is about to get awfully bumpy!

BUSINESS CONFIDENCE HIT BY POLY-CRISIS

A series of high-impact risk events – including ongoing economic volatility, a cost of living and cost of doing business crisis, the war in Ukraine and growing geopolitical turmoil, labour shortages and extreme weather events fuelled by the climate change – is creating a poly-crisis for SMEs.

According to the Chartered Institute of Internal Auditors latest 2023 Risk in Focus report

[source: https://www.iia.org.uk/media/1692515/risk-in-focus-2023.pdf],

SMEs need an unwavering focus on organisational resilience and need to work together to respond rapidly to the myriad of immediate and fast-moving risks businesses now face. Over 45% of businesses see the war in Ukraine and its impact on macroeconomic and geopolitical uncertainty as one of the top five risks impacting on their firm's financial liquidity and raising the risk of insolvency.

Not only are businesses readjusting to a changing customer landscape following the pandemic, but the UK is forecast to be heading towards five years of lost economic growth, according to the National Institute of Economic and Social Research (NIESR). "The triple supply shocks of Brexit, Covid and the Russian invasion of Ukraine, together with the monetary tightening that has been necessary to bring inflation down, have badly affected the UK economy."

The impact from overseas geopolitical events was cited by 81% of SMEs as having a knock-on effect on their firm's long-term strategic goal to access markets, as the lack of opportunity for developing overseas partnerships post-Brexit continues to hamper international trade for SMEs.

Source: PRISM research.

"UK GDP is projected to grow barely by 0.4% this year and by 0.3% in 2024, with the outlook remaining highly uncertain. There are, in fact, even chances that GDP growth will contract by the end of 2023 and a roughly 60% risk of a recession at the end of 2024," explains Professor Stephen Millard, Deputy Director for Macroeconomic Modelling and Forecasting, NIESR. "We forecast inflation to remain continually above target until 2025. More specifically we expect it to fall to 5.2% by the end of 2023 and to 3.9% by the end of 2024, as the effects of the rises in Bank Rate over the past year start to take effect. Nevertheless, with core inflation at 6.9%, and other underlying inflation measures remaining high, we see significant risks to our inflation forecast, which could result in inflation being higher than anticipated."

As a result, NIESR is expecting UK GDP to take to at least Q3 2024 before it recovers its Q4 2019 growth, indicating that addressing UK's poor growth performance remains the key challenge facing policy makers as we approach the next election.

Problems surrounding levelling up the country continue to impact SMEs.

CONTROVERSY SURROUNDING THE FUTURE OF HS2, THE HIGH-SPEED RAIL LINE 14 YEARS IN THE MAKING, CONTINUES TO THREATEN THE GOVERNMENT'S STRATEGY FOR LEVELLING UP THE COUNTRY.

The original plan of HS2 was to link London and the West Midlands, stretching to Birmingham, with a further phase extending to Crewe, Manchester and Leeds in the North and to be built at a cost of £35.5 billion. But the project has been beset with delays and spiralling construction costs, and is now forecast to cost the taxpayer around £180 billion with some parts needed to be funded by additional private investment.

Cost has been a major contributory factor in the Government's decision to announce the cancellation of the Northern leg of HS2, after 14 years in the making. With the knowledge that the line will fall short of its original destinations, businesses in the North who had been making plans for expansion and the opportunity to welcome new customers, must now rethink their strategy.

"SMEs will play a key role in future stability and as the economy stabilises, creating a healthy businesses environment will not only support the businesses within the UK but will make the country an attractive hub, bringing in overseas investors and promoting international relations. Business support must be high on the agenda and policy, investment and regulation to support business growth is now more important than ever," says Steven Mooney, CEO, FundMyPitch, a social investment platform that connects investors with investment-ready start-ups and established companies seeking funds.

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SEEING POSITIVE ECONOMIC PROGRESSION IS THE BOOST WHICH BUSINESSES THROUGHOUT THE UK NEED

to continue operations as usual and support the country's mission to grow. As the economy bounces back, businesses must be shown support from both the government and investors alike to grow, develop and innovate, allowing the country to beat the negative forecasts and unpredictable market conditions."

"The past year has thrown yet another curveball at businesses with economic disruptions, so it is positive to see signs of optimism with the recent economic growth in the UK. The pandemic highlighted that to weather external market forces, businesses should be open to change, be agile and flexible in their use – and, of course, fostering a culture of innovation should be at the core," comments Sridhar Iyengar, Managing Director, Zoho Europe.

"The recent turbulence has underlined the importance of SMEs being prepared to navigate turbulent times. Investing profits into research and development can position businesses as trendsetters, not just followers. The positive economic news should hopefully provide businesses with the confidence to fuel growth through innovation."

IN THE ABSENCE OF FURTHER SHOCKS, IT LOOKS LIKE THE BANK OF ENGLAND IS NOW AT, OR VERY CLOSE TO, THE END OF ITS HIKING CYCLE.

Although commentators are expecting the Bank will keep policy tight through 2024 as it continues to fight inflation, attention is now turning to when we can expect to see some rate cuts.

A continuation of its restrictive policy is supported by the empirical evidence. A recent paper by International Monetary Fund (IMF) analysed over 100 inflation shock episodes in 56 countries since the 1970s, warning that "most unresolved episodes involved 'premature celebrations', where inflation declined initially, only to plateau at an elevated level or re-accelerate". Whereby countries which had resolved inflation "had tighter monetary policy that was maintained more consistently over time, lower nominal wage growth, and less currency depreciation, compared to unresolved cases." The Bank of England and central banks will be taking note, wishing to avoid repeating the mistakes made by their predecessors by easing policy too early.

source: https://www.imf.org/-/media/Files/Publications/WP/2023/English/wpiea2023190-print-pdf.ashx)

Against this backdrop, there are shoots of positivity. "There remains cause for hope that the predicted recession may not be quite as harsh as predicted. Despite the numerous naysayers, the UK economy is continuing to fight to secure a positive index juxtaposed to the EU that appears to have stagnated to a flat lining standstill," says Paul Rowland, Senior Partner, Invictus Risk Solutions LLP.

"There is clear evidence of a contraction of investment, spending, and a falling business and consumer confidence across the UK. This has all been heightened by the burgeoning cost of living crisis and the Bank of England increasing the interest rates on a near monthly basis. There is clearly no soft landing on the horizon. While not actually disgruntled, the UK SME business community is certainly far from being gruntled by the Bank of England's programme. That said, if only the doyens within the hallowed walls of the Bank of England would advocate a programme of fiscal reform with equal tenacity and zeal, this would restore its credibility and ease the aggressively tightening and increasing weight of debt upon all sectors of British business, employment, and society."

THE GRADUAL EASING OF INFLATIONARY PRESSURE AND THE RISK OF OVERTIGHTENING LED TO A DOWNWARD TRAJECTORY FOR CPI WHILE OVERALL PAY PRESSURE ARE LIKELY TO EASE ACCORDING TO MANY FORWARD-LOOKING INDICATORS.

According to Swati Dhingra, External Member of the Monetary Policy Committee, Bank of England's annual report to the Treasury Select Committee, the total weekly earnings for business services (comprising of information, communication, professional, scientific and technical activities) increased by 11.3% in the three months to May, compared to a year ago. Whilst wage inflation across all other industries had been 5.3% implying a continued fall in real wages with an expectation of a further slowdown as the labour market continues to loosen.

source: https://www.bankofengland.co.uk/-/media/boe/files/news/2023/swati-dhingra-annual-report-2023.pdf)

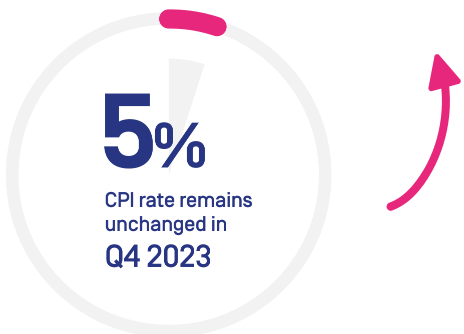
British Chambers of Commerce's (BCC) latest Quarterly Economic Forecast

source: https://www.britishchambers.org.uk/news/2023/09/bcc-economic-forecast-fragile-economy-stuck-in-first-gear)

reveals that economic activity is expected to remain very weak throughout 2024 and 2025. "We are expecting GDP to flatline over the next two quarters, leading to 0.4% growth for this year. Longer term growth is also expected to be less than 1% for 2024 and 2025," says David Bharier, Head of Research at the British Chambers of Commerce.

"CORE INFLATION IS PROVING STICKY.

But while BCC research shows inflation is the top concern for UK firms, fewer businesses now expect their prices to rise over the coming months. Therefore, the forecast for the CPI rate remains unchanged at 5.0% in Q4 2023."



Many SMEs are struggling to rebuild confidence following three years of economic shocks. "Prolonged inflation, skills shortages, and new trade barriers with the EU have fed into a climate of little or no growth," says Bharier. "A rapidly increasing proportion of SMEs are also now worried about interest rates, which have dramatically raised borrowing costs in many cases, and with further trade barriers looming, leading to higher import costs, and tightness in the labour market persisting, it is difficult to see how large-scale investment will be unlocked."

IT'S NO SECRET THAT SMES ARE FINDING THEMSELVES UNDER INCREASING PRESSURE TO CONTAIN COSTS WHILE INCREASING PROFIT AND GROWTH.

Pressure from their suppliers, pressure from their banks, pressure from their own organization – this in a world of increasing global compliance mandates and supply chain pressures, all while trying to find/retain talent and foster a culture of financial discipline within their organization," says Jody Derr, Business Development Manager, Esker Inc.

"Industry analysts point to inflation as being a primary cause for budget deficits with disruption to supply chains being a major concern. A sourcing solution, one enabling them to run RFx events, reverse auctions, etc., helps to mitigate these issues and provides standardisation of the process to ensure companies are receiving fair market value and drive their bottom line. For others, this evolves into highly strategic discussions around working capital. Again, the primary cause for this is not just inflation, but also the rising financing rates – not to mention the implications for having good credit."

source: https://www.esker.com/blog/technology-innovation/unlocking-business-potential-how-cfos-and-cpos-can-drive-profit-and/)

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NEW ERA OF GLOBAL TRADE

The economy remains in a precarious state. In the three months to July GPD grew by 0.2%, with a 0.5% decline in July itself. SMEs continue to battle against trade barriers with the EU.

"Understanding and navigating the new market landscape is becoming ever more important. The news of the UK Government Department for Business and trade (DBT) Secretary Kemi Badenoch's efforts in the USA gives further proof of the UK's post-Brexit new trade opportunities and the admiration in which the UK's robust service industries and supply chains are still held by the global business community. The UK SME business community can now plan to immerse itself in the opportunities arising from the UK Government Department for Business and Trade (DBT) Secretary Kemi Badenoch's closure of several significant deals in her current tour of the USA," says Paul Rowland, Senior Partner, Invictus Risk Solutions LLP.

"While in Jacksonville, Secretary Badenoch has astutely engaged the advisory services of the experienced trade officials within the Institute of Export and International Trade to secure a memorandum of understanding trade deal with the state of Florida that represents unfettered access to a massive £1 trillion GDP. This comes on the back of Secretary Badenoch and her team securing an eye-catching memorandum of understanding trade deal with Washington State that will enable UK companies to access the procurement and supply chain teams of major companies such as Amazon, Boeing, Microsoft, and Starbucks that contribute to a £725 billion GDP."

"Once the Florida deal is complete, the UK Government will have bypassed President Biden's partisan and publicly anti-British rhetoric to unlock access to £3.3 trillion GDP for British legal, financial, fintech, and manufacturing service industries via strategic trade deals with the USA states of Florida, Indiana, North Carolina, Oklahoma, South Carolina, Utah, and Washington – and there are more deals in the pipeline," continues Rowland.

"Our belief is that post-COVID the UK's SME business community can weather the future economic storm with confidence and survive by taking a long-term view on their risk appetite," comments Rowland.

> **SO, WHEN LIFE GIVES YOU LEMONS, RATHER THAN MAKING LEMONADE, WHY NOT ADD A LITTLE GIN AND TONIC!**

The UK domestic trade credit insurance market has always been an accurate barometer of our economy. "The current message coming from the experienced underwriters speaks of an expected slowdown across the last quarter of 2023 that will march into Q1 and Q2 2024. With this, they are expecting an increasing frequency, value and volume of non-payment, corporate insolvencies, and subsequent policy claims. Like their corporate insurance brethren, the trade credit insurance market can be seen to be implementing an industry wide policy of "pulling down and in" its industry exposures to lessen capacity and risk," continues Rowland.

"The positive message coming from the UK's trade credit insurance underwriting community is, of course, seeking to demand a better risk selection. However, the underwriters are doing so while also advocating for an expansion of its product and service portfolio such as an aggressive and refined debt collection service and non-cancellable insured credit limits to provide a deeper level of engagement and trust with its clients. This is particularly important for the banking and funding industry within the UK seeking the comfort that such a policy product can bring to their considerations of appetite and securitisation."

ALLIANZ TRADE

Over 51%

Aim for further market share in existing markets

Under 49%

Plan to diversify and target new countries

Allianz Trade, one of the world's leading trade credit insurance underwriters recently reported that post Brexit and post Covid "just over half (51%) of corporates aim for further market share in existing markets, while just under half (49%) plan to diversify and target new countries.

Source:
[https://www.tradefinanceglobal.com/posts/allianz-international-expansion-leveraging-trade-credit-insurance-post-brexit-post-pandemic-world.)](https://www.tradefinanceglobal.com/posts/allianz-international-expansion-leveraging-trade-credit-insurance-post-brexit-post-pandemic-world.)

For those UK SME's operating overseas, there are new commercial opportunities given the UK Government's success at executing post Brexit trade agreements with Australia, India, New Zealand, Singapore, and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) which is a free trade agreement between 11 countries in the Asia-Pacific rim region. "Of course, these exporters face the additional risks of "harder" markets vis-à-vis steep price increases to claw back previous losses, a tighter rigidity of policy cover terms and conditions to return the portfolio to profitability, and a volatile environment of shifting and turbulent socio-economic and geopolitical elements including an increasingly tempestuous post Brexit landscape."

> **CERTAINLY, OUR BRAVE EXPORTERS NEED TO REMAIN OBSERVANT, OPERATIONALLY ROBUST AND RESILIENT AT ALL TIMES BECAUSE JUST WHEN THEY FEEL THAT THINGS ARE GOING WELL FOR THEM, THE EU, OUR ECONOMY OR FATE WILL SNEAK UP BEHIND THEM AND CRACK THEM OVER THE HEAD WITH A PLANK OF WOOD!**

Comments Rowland.

"SME business in the UK should be aware that within the independent broking community there is a concern that insurers are seeking to apply coverage restrictions or reduce their exposure to risks through a defined peril approach. Of course, we understand the market dynamics of insurers needing to meet the challenges set by their regulators, shareholders, and other stakeholders. However, we are seeing insurers presenting new internal risk modelling tools, more stringent underwriting controls, and revised policy wordings as they seek to limit potential losses both in terms of scale and/or type of peril. This is not an easy or quick process as the underwriters need to align the risk profile of their existing client portfolios and new business targets with what their primary reinsurance partners are prepared to support going forward in terms of appetite, capital, capacity, and pricing."

"While we work with the underwriters and our clients to negotiate their way through less cover, restrictive policy limits and retentions (or the exclusion of risks), we are doing so with our placing broker and underwriting partners who can demonstrate clarity of cover and the competency in their risk management. We have taken a position and rule of engagement not to apologise for the corrections taking place within our insurance markets. After all, the right sort of client does not seek apologies, while the wrong sort will always seek to take a negative advantage of them," says Rowland.

There is an interconnectivity of climate change, commercial risk, cyber-attacks, economic crisis, energy supply disruption, inflation, and supply chain problems. All these elements are scalable and determined by the industry trade sector and turnover of a UK SME business.

"Our SME community leaders need to be focusing upon these elements and investing their energy, resources, and time to better analyse and understand the immediate and measurable potential impact upon their businesses in the not-too-distant future," warns Rowland. "With risk comes great worry but also a great opportunity to exploit for the UK SME business community with better, enhanced, and new products and services."

As the Government's flagship Electronic Trade Documents Act that gives legal status to electronic Bills of Exchange and Bills of Lading and other commercial documents finally comes into force, the British Chambers of Commerce (BCC) are urging businesses who want to boost their exports and reduce costs to quickly embrace a new era of digital trade.

IN ITS TRADE MANIFESTO, THE BCC HAD BEEN CALLING ON THE UK GOVERNMENT TO WORK WITH BUSINESS TO ENSURE.. 60% OF THE UK'S EXPORTS ARE CARRIED OUT DIGITALLY BY THE END OF THE DECADE.

Source: https://www.britishchambers.org.uk/news/2023/07/bcc-trade-manifesto-international-trade-vital-for-uk-growth)

"The introduction of the Electronic Trade Documents Act is a huge milestone. This new era is starting in the UK, but we can also act as a beacon, leading towards further digitalisation of trade across the world. We now need to see other governments accelerating their work to digitalise border processes," says Willian Bain, Head of Trade Policy, BCC.

"The whole Chamber Network has already risen to this challenge and has switched to using Digital Certificates of Origin for the UK. As more countries make the transition, we will be able to increasingly digitise our trade – making it much less bureaucratic and leading to big savings in both costs and time."

Exporting involves credit risk; credit risk affects collectability of sales; and delays cost dearly. Between order taking and cash receipt a raft of problems can arise. Across the entire supply chain, accuracy of data is paramount. “Data is the lifeblood of the modern SME. Gathering real-time financial data from various sources across the chain and integrating it seamlessly into solutions for budgeting, forecasting, and variance analysis help accelerate the decision-making process for SMEs, and provides valuable insights for key stakeholders,” says Sam Townsend, Head of Marketing for Northern Europe, Esker Ltd.

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AUTOMATION TOOLS ELIMINATE THE NEED FOR MANUAL INTERVENTION, ENSURING DATA CONSISTENCY AND ACCURACY.

BY IMPLEMENTING INTELLIGENT AUTOMATION SOLUTIONS WITH THE USE OF ARTIFICIAL INTELLIGENCE (AI), SUCH SOLUTIONS NOT ONLY HELP TO ENSURE THE BUSINESS COMPLIES WITH COMPLIANCE, FINANCIAL REGULATIONS, AND INTERNAL CONTROLS, BUT TECHNOLOGY IS NOW THE ENABLER THAT SEES BUSINESSES BECOME MORE AGILE AND DRIVES ORGANISATIONAL GROWTH.

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source: https://blog.esker.co.uk/unleashing-the-power-of-process-automation-transforming-the-office-of-the-cfo/]

SMEs trading overseas are coming to terms with the fact that in tapping export markets, specialist knowledge is vital. Export trade involves risk and costs which are, in many cases, higher than those which exist in the domestic market. Getting paid for exports can often be challenging and exporters learn the hard way not to try to compete with credit terms, nor lead a credit race or terms auction. For SMEs, sales competition should be all about price, delivery, and services – but never about cash.

GOVERNMENT BACK TRACKING ON NET ZERO

Government's announcement to ease the transition to heat pumps from gas boilers in homes is likely to be a vote winner with consumers already hit with the cost-of-living crisis, as is the news to push the banning of sale of new petrol and diesel vehicles back by five years to 2035 bringing the UK in line with the EU's plans to ban the sale of new fossil fuel cars.

However, the news was met with scorn by businesses who say that they have already made fundamental changes to their operations in their commitment to cut emissions, and they see the government's decision to ease the transition as bringing uncertainty and likely disruption to their own transformation efforts to meet the regulations.

A central pillar to the Government's Net Zero strategy to become neutral was the 2030 ban on new petrol and diesel vehicles. Car companies were quick to respond to the news that the government will soften several key policy commitments which are mainstays in the drive to achieve net zero emissions by 2050. Ford's chief executive Lisa Brankin pulled no punches saying,

"Three years ago the government announced the UK's transition to electric new car and van sales from 2030. The auto industry is investing to meet that change. Ford has announced a global $50 billion commitment to electrification, launching nine electric vehicles by 2025. The range is supported by £430 million invested in Ford UK's development and manufacturing facilities, with further funding planned for the 2030 timeframe. **This is the biggest industry transformation in over a century,** and the UK 2030 target is a vital catalyst to accelerate Ford into a cleaner future. Our business needs three things from the UK government: ambition, commitment and consistent. A relaxation of 2030 would undermine all three."

By now the government had been hoping to see greater availability of cheap electric vehicles, but the cost of EVs remains high, the charging infrastructure cumbersome, and the ability to charge speedily on route can mean journeys need greater planning and destination arrival times can be longer than expected.

source: [https://moneyweek.com/investments/energy/the-backlash-against-net-zero-begins]

Encouraging more drivers into EVs needs an attractive package of incentives to give consumers the confidence to switch. "Manufacturers will continue to put innovative new models on the market, but consumers need encouragement to buy more than ever," says Mike Hawes, Chief Executive, Society of Motor Manufacturers and Traders.

"As cost remains one of the biggest barriers to going electric, there's surely no reason why the Government can't help many more drivers into EVs by reintroducing a form of the plug-in car grant that incentivises the cheaper end of the car market," comments Simon Williams, Head of Policy, RAC.

source: [https://www.rac.co.uk/drive/news/motoring-news/uk-ban-on-new-petrol-and-diesel-cars-pushed-back-to-2035]

When it comes to meeting their own net zero agenda, 78% of SMEs say they are actively or plan to invest more in renewable technology in 2023 compared to 2022.

Source: PRISM research.

"It isn't just multinationals like Ford throwing their toys out of the pram when the Government flip flops on climate change. Tens of thousands of smaller suppliers into the industries most affected have had their investment plans turned upside down. The potential damage extends beyond motor manufacturers to the companies trying to build the EV charging infrastructure and so many more entrepreneurs committed to creating the brave new world post fossil fuels," says Hood.

"Add in the recent self-inflicted shambles over the bidding process for new offshore wind farms and a picture becomes clear of a commercial landscape, which is not safe for investors and lenders, never mind business owners and managers. Without adequate equity and readily accessible finance, few businesses can survive, never mind thrive. Studies on why the UK has such a lamentable record on business investment consistently call for greater certainty, particularly on government policy. What chance of that now, either under this government or another administration after the forthcoming election?"

The news that the North Sea Transition Authority (NSTA) has given approval for the development of the Rosebank project – the UK's largest untapped oil field – elicited strong reactions, with the Prime Minister Rishi Sunak insisting that the oil field development is "the right long-term decision for the UK's energy security", whilst Scotland's First Minister Humza Yousaf says he is "concerned that the majority of what is extracted from Rosebank will go overseas", and environmental groups begin protests outside UK government offices in Edinburgh.

Despite the softening stance, the Prime Minister says the Government remains committed to the legally binding target of reaching net zero emissions by 2050, but he felt it is right to protect the public from the "unacceptable costs" of going green, citing that he was changing policy because previous governments had moved too quickly to set net zero targets without securing the support of the public.

source: https://www.reuters.com/world/uk/uk-interior-minister-braverman-we-need-pragmatic-approach-net-zero-2023-09-20/)

"A week is a long time in politics and there appears to be a bit of flexibility and u-turning being built into the calculations with regards the actual year at which its greenhouse gas emissions will now be targeted at net zero for the UK. There will of course be considerable additional operational bureaucracy and costs attached to the UK SME business community to deliver the ambitious net zero target," says Paul Rowland, Senior Partner, Invictus Risk Solutions LLP.

"" THE UK GOVERNMENT IS SEEKING TO DELIVER A BLUEPRINT PROGRAMME OF ACTIVE COLLABORATION ACROSS A WIDE PANEL OF BANKS, COMPANIES, GOVERNMENT MINISTRIES, FUNDERS, AND STAKEHOLDERS TO DEFINE A ROADMAP AND THE STANDARDS NEEDED TO "GREEN" THE UK ECONOMY

alongside securing the necessary call to action and funding to deliver this. Our hope is that the UK Government, now and in the future, will also present the UK SME business community with a strategy of multi layered tax incentives which should prove to be a highly effective mechanism to trigger change and reward behaviour by encouraging green and environmentally positive investment."

With the UK creating only around 1% of the world's carbon emissions, the UK is unlikely to be the tipping point in cooling the planet. It does, however, have the potential to lead the way in the development of green technology and help other countries make the move as well.

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"In the dynamic realm of start-ups, SMEs and even Corporates, innovation and adaptability are the keys to success.

These enterprises are the heartbeat of our economy, injecting and kneading fresh ideas and entrepreneurial spirit into industries across the board.

As the CEO of our Boutique Strategic Consulting and Venture Capital firm, I believe that nurturing small ventures as well as ambitious corporates with strategic guidance and smart investments is not just a business strategy but a commitment to fostering growth and innovation in our ever-changing world. Together, we pave the way for a brighter future where small, medium-sized enterprises and big companies thrive together."

Andrea Maria Cosentino
Founder & CEO – Impact Fundry

START-UPS TRANSFORM THE BUSINESS SCENE

There are currently over 5,000,000 start-ups in the UK and with 793,000 new startup formations since the start of the year, new business creation continues apace.

Source: [source: https://profiletree.com/uk-business-startup-statistics]

Opus Business Advisory Group's recent market report on the hospitality sector reveals that there were 10% more food and beverage companies in September 2023 than in August 2022

source: https://opusllp.com/report/financial-uncertainty-for-the-hospitality-industry/)

"The question is whether this is bravery or foolhardiness. A start-up is not for the faint-hearted," says Nick Hood, Senior Advisor, Opus Business Advisory Group. "One particular challenge is raising finance. It's not just that the current economic climate makes investors and lenders extra cautious; the finance market has fragmented in recent years. Last year, business finance provided to SMEs by the 'challenger' banks and the crowd funding industry exceeded funding from traditional high street banks for the first time. All these new sources have their own, often distinctive risk assessment procedures and processes, meaning a hugely steep learning curve for borrowers."

"Another key issue is finding and even more importantly, keeping staff both initially and holding on to talent as the start-up grows. The labour market is extremely competitive, making hiring a nightmare and escalating staff costs a threat to many business models," continues Hood.

"Having a lack of business experience and a limited range of skills are problems for many start-up management teams. There are two immediate solutions, sadly too often ignored in the enthusiasm of starting a new venture. Having access to a mentor either as a non-executive or on a less formal basis is essential. A good mentor will never tread on an entrepreneur's toes, unless of course the business is seriously out of control. The other important resource is having good professional advisers. There's never any shame and usually plenty of upside in asking for expert outside advice."

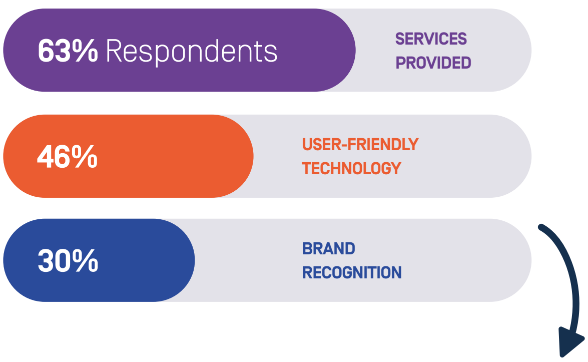
Fintech is leading the way in start-ups. A survey by iResearch Services conducted earlier in 2023 found considerable post-pandemic trust in financial providers, with 70% of UK and US respondents saying they believe their bank acts in their best interests. This is up from 63% in 2020.

source: https://www.iresearchservices.com/thought-leadership-report/leading-lights-focus-on-financial-services-fs1/).

"Our study also showed clear faith in fintechs, with 43% of respondents saying they were more inclined to use a challenger bank or fintech provider than a traditional bank," says Rachael Kinsella, Editorial and Content Director, iResearch Services.

"With this delicate balance of trust and credibility, any liquidity and stability concerns in the market will be keenly felt, particularly by small to medium-sized businesses that are already facing a raft of inflationary, economic and geopolitical pressures. When you add current supply chain and sustainability concerns into the mix, it's a perfect storm for SMEs. Their chosen partners and providers will have to go the extra mile to prove their customers' trust in them is not misplaced."

iRESEARCH SERVICES STUDY



According to the iResearch Services study in April 2023, 63% of respondents say the services provided by financial services or fintechs are the biggest reason when choosing their main bank, with a further 46% saying that user-friendly technology is an additional key motivator for them. While a further 30% say they take brand recognition seriously.

"Communication and alignment of purpose and values are vital in achieving this. SMEs are even more focused on purpose and their raison d'etre in the current climate because customers increasingly demand clear communication of purpose and values in all that the company says and does," continues Kinsella. "Ethical and environmentally conscious approaches are equally important for people and the planet: customers are far more likely to choose products and services based on how a company can demonstrate these credentials."

"The UK is well placed to take advantage of the opportunity as a leading digital economy and financial services country to leverage a position as one of Europe's leading fintech hubs. By driving entrepreneurial investment and growth into this trade sector, and by the UK Government fostering an environment of innovation, the UK can generate expertise and employment within a service industry that is advocating the ability of mobile phones and tablets to access "value added" distribution chains and channels to pay bills, to pay for goods and services, to receive wages, to take out loans, to make investments, and to send and receive money domestically and internationally," comments Paul Rowland, Senior Partner, Invictus Risk Solutions LLP.

"Given the availability of electricity and internet services, even for our most northward and remote islands of Orkney and Shetland, British society is able to continue to embrace Fintech services as new and fast-moving innovations and technologies are developed at an increasing pace to meet our demands.

The falling price and wider accessibility of smart phones and tablets will continue to drive investment into the internet-based solutions offered by the British fintech industry. All will be well, so long as our legal infrastructure keeps pace in terms of affordability, compliance, consumer choice, privacy and regulatory oversight."

Like every industry, fintech faces disruptors. Given the advent of commercial-usable AI potentially destabilising the market, and interest rates dampening investors' appetite, we may see an unusual number of fintech businesses teetering on the brink of failure so the sector will need to be ever watchful.

source: https://www.cityam.com/uk-fintech-funding-tumbles-as-interest-rates-dampen-investors-appetite/]

THE CHALLENGES AHEAD

SMEs will need to build resilience as we move into Q4 2023. As the Government faces calls for tax cuts, the Chancellor Jeremy Hunt is warning taxes won't be coming down anytime soon amid fears that a cut in taxation will fuel inflation.

For businesses already battling with weaker market demand and mounting costs a cut in taxation would have been particularly welcomed given the challenges facing SMEs. According to S&P Global's Purchasing Managers' Index (PMI) for September, the Index recorded a score of 44.3 from survey respondents, up from August's 39-month low of 43.0. Despite the rise, it is still ranked among the weakest reading seen over the past 14 years as pressures on costs are joined by other challenges including market uncertainty, the cost-of-living and cost-of-business crisis, couples with weak conditions in overseas markets.

source: https://www.pmi.spglobal.com/Public]

After strong activity in the service sector for Q2 2023, the S&P Global/CIPS UK Services Business Activity Index recorded a marginal drop to 49.3 for September, down 0.2 from the 49.5 figure for August as rising interest rates in the autumn squeezed disposable incomes, brought in fewer new business opportunities and slowed long-term business expansion plans leading to fewer job creation and the non-replacement of departing staff.

"Though the sector's shrinkage was marginal, the hesitation to commit is likely to be the landscape for the next few months as the UK economy becomes a riskier environment for domestic and overseas business alike and competition amongst service providers intensifies," says Dr John Glen, Chief Economist, the Chartered Institute of Procurement & Supply (CIPS).

> **AS BACKLOGS DECLINES, CAPACITY OPENED UP AT THE GREATEST LEVEL FOR THREE YEARS, SO STAFF HIRING WAS MORE MUTED, REDUCING JOB SEEKER OPPORTUNITIES AS PROSPECTS FOR THE UK ECONOMY BECOME COLDER.**

"After a modest recovery over the past six months, service sector businesses are now clearly feeling the impact of rising interest rates on client demand," adds Tim Moore, Economics Director, S&P Global Market Intelligence. "Worries about the broader business climate also dampened spending in August, with firms suggesting that faltering UK economic growth and sticky inflation were weighing on the outlook."

In his keynote address at the Conservatives Party Conference, Prime Minister Rishi Sunak reiterated that the Government is taking practical steps to help all enterprises and small businesses, including business rates relief for retail, hospitality and leisure firms, and reductions in employers' National Insurance bills, but warned there were some tough long-term decisions which will need to be made in order to deliver economic growth, and cutting taxes can only be done when the time is right.

It's a turbulent time for British businesses. In a recent iResearch Services Pulse survey 56% of respondents identified the international tax agenda as a significant medium-term concern for their business.

source: [https://www.iresearchservices.com/?s=pulse].

"Thousands of UK businesses will be released from EU reporting requirements following Brexit negotiations and these will in turn be replaced by UK laws and requirements. The Government must recognise that the process towards achieving this is driving a medium-term risk for businesses," comments Yogesh Shah, CEO, iResearch Services.

The impact of the cost-of-living crisis on staff remains a leading source of concern for 48% of Pulse survey respondents. "Many businesses are taking a short-term view where the cost-of-living crisis is perceived as the biggest threat to survival over the next few months," says Shah. "It's important that business leaders look beyond this at emerging medium-term risks and ensure there is a plan in place to manage these."

Nearly 50% of business leaders say they believe policymakers are sufficiently aware of the key challenges faced by their industry, with 62% saying they are confident that the challenges can be fixed.

source: [https://www.iresearchservices.com/?s=pulse].

ONE SUCH CHALLENGE IS THE LEVELLING UP OF THE COUNTRY, AND MANY SAW HS2 AS A MEANS TO ACHIEVING THIS.

After days of speculation that overshadowed other issues at the Conservatives Party Conference the Prime Minister's tough decision over the second phase of the project "to stop the construction of the HS2 high speed rail line to Manchester" instead

"REINVESTING EVERY SINGLE PENNY – £36 BILLION – IN HUNDREDS OF NEW TRANSPORT PROJECTS IN THE NORTH AND THE MIDLANDS, ACROSS THE COUNTRY" TO BE KNOWN AS 'NETWORK NORTH' HAS BEEN MET WITH CRITICISM.

"Network North may sound like a better use of the money with new lines promised and road schemes the simple fact is that irrespective of what it is called, we are still no nearer to getting the transport network that we needed years ago to unlock the north's potential. We have been promised a lot before and nothing has been done and this latest attempt from government will be treated with cynicism and scepticism by a lot of people," comments Chris Fletcher, Director of Policy, Greater Manchester Chamber of Commerce.

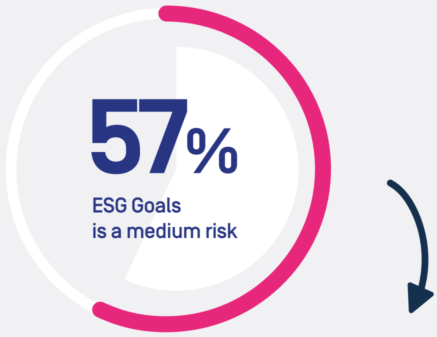
"HS2 was a major investment opportunity for the UK that would unburden a worn-out network already at over capacity; boost the country's net zero ambitions and open up labour markets and job opportunities on a scale like never before. Plus, it was also a cornerstone of Northern Powerhouse Rail. Network North must deliver all this, and more, and in a shorter timescale. If the scale of what the Prime Minister announced is to be realised, then there will have to be a huge investment in upskilling and training an army of workers for the challenge ahead," continues Fletcher. "At present, there are gaps and shortages in critical construction and engineering jobs, something HS2 has been good at resolving through apprenticeships and that will have to be stepped up unless we are to face yet more hold ups and delays in construction. We will be watching closely and waiting on further details of what will be delivered and, more importantly, when."

"THE CANCELLATION OF HS2 NORTH OF BIRMINGHAM AND THE NEGATIVE CONSEQUENCES ARE LIKELY TO HAVE AN IMPACT ON THE BRITISH ECONOMY AND ENVIRONMENT.

The dramatic improvements in connectivity in the North and Scotland that we would have seen cannot be delivered by alternative schemes and their economies will be significantly disadvantaged as a result," says Julian Worth, spokesperson and Chair of The Chartered Institute of Logistics and Transport's (CILT) Rail Freight Forum.

"The problem with HS2 is not that it is the wrong project, but that its costs have been allowed to escalate out of control. Other densely populated countries can control the cost of major infrastructure projects and rather than a 'bespoke UK' solution, consideration should be given to using specifications from existing schemes in Europe and beyond."

ESG GOALS



WITH THE CLIMATE CRISIS WORSENING BY THE YEAR, THE NEED TO DECARBONISE IS BECOMING GREATER AND MORE URGENT WITH 57% OF FIRMS SAYING MEETING ENVIRONMENTAL, SOCIAL, AND CORPORATE GOVERNANCE (ESG GOALS) IS A MEDIUM-TERM RISK.

source: https://www.iresearchservices.com/?s=pulse).

Almost all large companies now have clear carbon reduction strategies, but decarbonising long distance road freight movements remains extremely challenging. "Battery HGVs will carry out local and regional distribution, but decarbonising trunk haulage by road is much more difficult and, for this reason, modal shift to rail trunking is an attractive option for many companies. Rather than a significant allocation to road projects, a proportion of any money released from HS2 should be invested in modal shift by increasing capacity at key locations and electrifying missing links in the core rail freight network, 60% of which is already electrified," explains Worth. "Wiring 800 miles over the next 20 years at a cost of less than £2 billion would allow around 95% of rail freight to be electrically hauled with zero carbon emissions."

The announcement that capacity is to be increased on the vital freight route from Felixstowe to the Midlands and North, with investments at Ely and Haughley Junctions have been welcomed by CILT. "This route should also be electrified as key strategic investment for freight and logistics, supporting supply chains for businesses in the Midlands and the North. A series of investments in capacity on the West Coast Main Line are also required in lieu of the capacity that would have been released by HS2. These include 4-tracking between Colwich and Stafford plus between Winsford and Warrington, and it is essential that a significant proportion of the capacity released by HS2 Phase 1 continues to be earmarked for freight," says Worth.

"Providing certainty on such projects would help to encourage private investment in rail-connected logistics centres, which in turn supports the UK's move to decarbonise transport. This is private investment which may look outside of the UK if there remains uncertainty over when the projects replacing HS2 are due to be delivered."

In answer to the critics about HS2, the Prime Minister said, "The facts have changed and the right thing to do when the facts change is to have the courage to change direction."

SMEs already have that courage – despite the obstacles they face. SMEs are highly agile and quick to adapt to change. As we move into Q4 2023, and the impact of tough long-term decisions emerge, the agility of SMEs will help drive business confidence.

SO, IN ANSWER TO THE QUESTION, "ARE WE THERE YET?" NOT QUITE, BUT SMES HAVE THE COURAGE TO GET US THERE.

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