Business in Britain
A survey of opinions and trends
50th edition June 2017
For your next step
INTRODUCTION

Welcome to the 50th edition of the Lloyds Bank Business in Britain Survey, providing insight on the performance and expectations of UK businesses, in particular small and medium-sized enterprises (SMEs).

In my introduction to January’s report, I predicted more twists and turns in the political landscape, but I did not foresee a snap General Election! The responses which inform our June report were provided before the outcome of the election was known, but after it was called, and whilst firms acknowledge the threat of political uncertainty, we have seen a positive increase in business confidence since our last survey in January.

Business owners are optimistic, despite hurdles including challenges in recruiting both skilled and unskilled labour. They anticipate higher sales, increased profits, and staffing levels to rise.

Of course the outlook for the external environment remains far from clear, with details of Britain’s exit from the EU still to come; however firms appear to be taking this in their stride and demonstrating resilience during this uncertain period.

I hope you find the report valuable. My team and I look forward to working with you during the remainder of 2017.
EXECUTIVE SUMMARY

- In our latest half-yearly survey, companies were the most positive they have been about their overall business prospects since the EU referendum result. Business confidence increased significantly to 24%, from 14% in January and 12% immediately following the EU vote.
- The rise means that business confidence is now broadly in line with the long-term average.
- The recovery in business sentiment has become more broad-based across sectors. While confidence in the manufacturing sector remains positive, there has been a rebound in most service sectors, supported by improving domestic demand.
- The share of firms naming political uncertainty and weaker demand edged higher from January's survey, but are little changed from a year ago.
- Recruitment difficulties have increased across all sectors and regions, and are at a decade high. Despite that, the share of companies expecting to increase average pay rose only slightly. This may point to reluctance among some firms to raise average pay levels to secure employment. Expectations for staffing levels rose, but remain lower than levels seen in recent years.
- Firms' pricing intentions overall have remained steady. Price expectations in the retail and wholesale sector, however, have fallen and suggest that consumer inflation will remain relatively high, but may peak later in the year.
- Firms' capital spending plans improved for a second consecutive survey, but remain cautious despite stronger profit expectations and a large fall in economic uncertainty. However, concerns about weaker UK and overseas demand – along with input costs and extra regulation – have increased.
- Companies were more positive about export prospects, which rose to an eighteen-month high. Exporters regarded the value of the pound as positive for their activity, while importers saw it as negative, but sentiment between them has converged compared with the last survey. This suggests the pound is perceived as being nearer fairer value.
Overall business confidence* rose for a second consecutive survey to 24% from 14% in January. It had fallen to 12% immediately following the EU referendum outcome. Confidence is now broadly in line with the long-term average of 23% and is at an eighteen-month high.

The recovery in sentiment has also become more broad-based across the different sectors (see the sector outlook on page 10).

* Business confidence in this report is measured as an average of the net balances of firms anticipating stronger sales, orders and profits in the next six months.

The net balance* of firms reporting expectations of higher turnover/sales in the next six months increased to 24% from 17%. It is at the strongest level since January 2016. Firms in construction and manufacturing were the most positive about turnover prospects.

The net balance of firms reporting expectations of higher profits in the next six months rose to 18% from 8%, which is also an eighteen-month high. Profit expectations are the highest in the construction and transport and communications sectors.

* 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 therefore varies between +100 and -100.
The net balance of firms expecting to raise their staffing levels in the next six months increased for a second consecutive survey to 8% from 2%. It suggests that the pace of employment growth may improve, but hiring levels seem likely to remain lower than a couple of years ago.

The net balance of firms anticipating to increase capital spending in the next six months rose to 8% from 1%. The rise was strongest in construction and transport and communications.

The share of firms saying they have experienced difficulties in recruiting skilled labour in the past six months increased to a ten-year high of 52%, compared with 31% in January. Difficulties in recruiting unskilled labour also rose to 26% from 14%.

Despite this sharp increase, the net balance of firms reporting expectations of higher average pay in the next six months rose only slightly to 16% from 12%. The responses suggest that firms are taking a cautious approach to their hiring and pay policy.
The net balance of exporters reporting expectations of higher total exports in the next six months increased to 29% from 26%, the highest level since January 2016. Firms were most positive about their export prospects to North America, followed by the Rest of the World and Europe.

Since the last survey, the pound has risen against both the US dollar and the euro from post-EU referendum lows, although it remains significantly below levels prior to the vote.

The net balance of exporters saying that the pound’s value against the US dollar is ‘positive’ fell to 3% from 18%. Against the euro, the net balance declined to 5% from 13%.

The net balance of importers saying that the exchange rate against the US dollar and the euro is ‘positive’ increased to -3% and -9%. That compares with far more negative levels of -29% and -39%, respectively, in the last survey.
The net balance of firms expecting to increase their prices in the next six months remained unchanged at 20%.

The net balance of retail and wholesale firms expecting to increase their prices in the next six months fell back to 26%, after rising to 40% in the last survey. This suggests that consumer price inflation is likely to remain elevated, but could peak later this year.

There was a notable fall in the proportion of firms citing economic uncertainty as the single greatest threat to their business (down to 15%, from 26% and 27% in the previous two surveys). The share of firms naming political uncertainty and weaker UK demand edged higher to 11% and 18% respectively, but are little changed from a year ago.

There were more visible upward trends over the last three surveys in firms quoting weaker overseas demand (11%), input costs (11%), extra regulation (9%) and the cost and availability of finance (6%) as the greatest threats. Skills access remained steady at 6%, even though there was a sharp rise in recruitment difficulties.
The latest report shows a broad-based improvement in confidence about future conditions. Four out of the six sectors have noted an improvement in confidence since January, with the rise most significant in sectors that are primarily driven by domestic demand. This suggests that the lift is not merely due to the competitiveness boost provided by the weak pound.

Confidence is now highest in **construction**, where the net balance rose from 20% to 31%. **Transport and communications, business and other services** and **retail and wholesale** also recorded strong gains.

Even in the two areas which reported a fall, the level of confidence is well above the recent lows of last July. **Manufacturing** fell modestly from 28% to 27%, which still left it as the sector with the second-highest reading. Meanwhile, **hospitality and leisure** declined to 21% from 28% previously.

Readings on expectations for prices are more mixed than in January. This time only two sectors report an increase in the net balance of companies expecting to raise prices in the next six months. Nevertheless, as most sectors still have relatively high balances, there is little evidence here that inflationary pressures are waning.

**Construction** has seen the largest rise in the net balance since January, moving up to 22% from 15%. The increase may reflect a combination of rising raw-material costs due to higher import prices, alongside more leeway to pass these cost pressures on due the pickup in activity. **Business and other services** also saw a rise in its net balance from 11% to 17%.

**Retail and wholesale** recorded the biggest decline in its net balance to 26% from 40%. Nevertheless, that net balance is still the highest across all sectors, reflecting the sector’s exposure to rising import prices. **Hospitality and leisure** now has the lowest net balance, having fallen from 27% to 15%.
Despite the improvement in business confidence, most sectors still have relatively cautious investment plans. Nevertheless, net balances are higher in four out of the six sectors.

Construction has seen the largest rise in its net balance to 23% from 6% in January. Transport and communication also recorded a sharp rise to 13% from 1%.

Hospitality and leisure (1%) has the lowest net balance, followed by retail and wholesale (4%). Moreover, while manufacturing’s net balance has gone up to 5% from 1%, this is still well below the levels of a couple of years ago.

Employment intentions have risen across most sectors, with all but one sector reporting stronger intentions to increase staffing levels. However, the balances still remain relatively low across all sectors compared to a few years ago.

This may be in part due to a lack of available workers, as most sectors reported increasing difficulties in recruiting new staff.

Construction has the highest net balance at 12%, followed by manufacturing at 11%. Hospitality and leisure, which now has the lowest net balance at 3%, is the only sector to show a decline from January. However, both the retail and wholesale and the transport and communication sectors continue to report particularly low net balances at 4%.
Most regions report sizeable increases in business confidence. All but one area reported an improvement in business confidence, compared to January. Confidence is now highest in Wales (34%), followed by the North East (33%), the South East (28%) and the South West (27%).

Scotland (19%), which was the only area to show a drop, now has the lowest level of confidence. It is followed by London (20%), the East of England (22%) and the West Midlands (22%).

Capital spending plans vary markedly across regions. The capital spending balance has risen for all but two areas compared to January. However, while the overall net balance for the UK as a whole is still relatively low, it is much more elevated in some regions.

The highest net balance of firms reporting expectations of a pick-up in capital spending are in the North East (27%), the West Midlands (14%) and Wales (14%).

The lowest net balances are in the East Midlands (0%) and Scotland (2%). These are also the only two areas to report a decline from last time.

* Please note that inferences for Wales and the North East should be interpreted with care, due to small sample size.
Employment intentions have improved in all but three regions since January. **Wales** (16%) now has the largest balance, up 10 points from January. This is followed by the **North East** (15%), **Yorkshire and the Humber** (13%), and the **West Midlands** (13%).

Only three regions reported lower balances than in January. These are the **South West** (-4%), the **East of England** (5%) and **Scotland** (8%). **London** also has one of the lowest net balances at 7%, although this was a rise from January’s -5% recorded.

One potential reason for firms’ rather cautious plans for boosting employment is that many are already reporting recruitment difficulties. Those appear to have escalated since January, with all regions reporting an increase in the difficulty of recruiting skilled level. Firms in the **West Midlands** and the **East of England** (both 62%) report the highest levels of recruitment difficulties. This is followed by the **South West** (57%), and **London**.

Overall, more than half of firms in seven regions report difficulties in recruiting skilled labour, suggesting that this has become a particularly significant issue. **Wales** (32%) has the lowest net balance, followed by **Scotland** (45%). Even in those cases, however, the net balances have risen since January.
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