

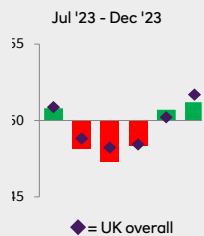
NatWest Sustainable Business Tracker

UK SME business activity returns to growth amid recovery in service sector performance

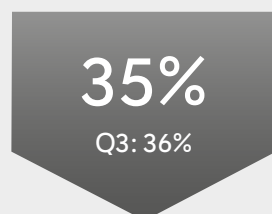
NatWest SME PMI



Business Activity Index



NatWest SME Sustainability PMI



Key findings

Fastest rise in overall UK SME output since May 2023

Service providers report growth rebound, but manufacturers see an accelerated decline

Business optimism among SMEs reaches highest level since March 2022

Cost inflation hits three-month high and is seen as the biggest obstacle to sustainability action in 2024

The NatWest Sustainable Business Tracker is a quarterly report, designed to monitor business performance and sustainability actions at UK enterprises with 1-249 employees. Results are compiled from responses to S&P Global UK Purchasing Managers' Index® (PMI®) surveys. The latest report includes a special feature on obstacles to sustainability plans in 2024.

Business activity at UK small and medium-sized enterprises (SMEs) expanded at the fastest rate for seven months in December, led by renewed growth in the service economy. Adding to signs of a steady turnaround in business conditions, new orders stabilised at the end of 2023, which ended a five-month period of reduced workloads.

The headline NatWest SME PMI® Business Activity Index registered 51.2 in December, up from 50.7 in November and the highest reading since May. This signalled a marginal overall increase in SME business activity, with growth in the service economy more than offsetting sustained declines in manufacturing and construction output. The latest fall in manufacturing production was the steepest since October 2022, reflecting weak demand in both domestic and export markets.

Survey respondents often commented on relief at the pause in Bank of England interest rate hikes last autumn, alongside a positive impact on business and consumer spending from lower borrowing costs and easing inflationary pressures. This contributed to an improvement in business activity expectations for the year ahead. Overall business confidence among SMEs was the highest since early-2022, helped by a marked improvement in service sector optimism at the end of last year.

Elevated wage pressures and squeezed margins meant that UK SMEs were wary about adding to their staffing numbers. Job creation

stalled in December, which ended a 33-month period of employment growth. A number of firms commented on the non-replacement of voluntary leavers due to spare capacity and efforts to contain business expenses.

Input cost inflation accelerated to its highest since September, which was overwhelmingly linked to greater salary payments. December data also signalled a robust rise in prices charged by SMEs, led by those operating in the service sector, largely in response to higher operating expenses.

Meanwhile, the latest NatWest Sustainable Business Tracker indicated that 35% of UK SMEs viewed sustainability action as a high priority for the year ahead, down from 36% in Q3 and the joint-lowest since the survey began in 2020. A slide in prioritisation was reported by both manufacturers and service providers, with survey respondents often commenting on the need to focus on rising business expenses and challenging economic conditions. In contrast, the proportion of large enterprises citing sustainability action as a high priority rose from 59% to 64% in Q4.

Finally, our special feature on obstacles to sustainability actions in 2024 illustrated that worries about higher business costs were by far the most prevalent constraint cited by UK SMEs. Around 60% of the survey panel noted that rising business costs was a major obstacle to becoming more sustainable in the next 12 months. Difficulties measuring carbon footprint were the second-highest ranked barrier, reported by 31% of SMEs in Q4.

Large enterprises also noted that rising business costs (59%) were the top ranking obstacle for 2024, while uncertainty about government regulation was the second-highest cited constraint on sustainability action (37%).

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Comments

“Small businesses are starting 2024 on a positive footing with confidence getting back to pre-energy crisis highs. Costs are clearly a concern and rising wages, especially the national minimum wage, means businesses are going to be working hard to find efficiencies this year. That may mean sustainability initiatives slide down the priority list for some, but investments in energy efficiency will make even more sense for others. The market’s expectations of interest rate cuts may also help lower financing costs, if the Bank of England builds more confidence that inflation is falling reliably.”

Sebastian Burnside
NatWest Chief Economist

“After a turbulent year for the economy, it is really encouraging to see that small businesses ended 2023 in higher spirits, with growth accelerating at the fastest rate since May. The services sector in particular has been buoyed by strong sales in the last quarter as borrowing costs have eased. With business confidence now at its highest level in over a year there’s a real sense of momentum as we start 2024.

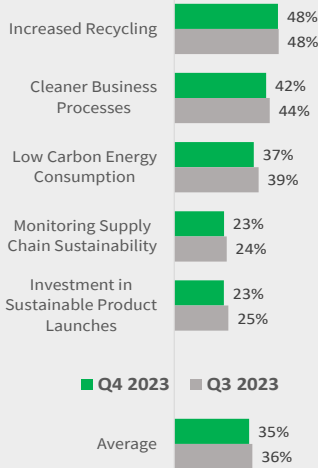
“For those businesses looking to improve their environmental sustainability, rising business costs remain the biggest challenge. At NatWest we have developed the tools to support businesses to understand where they can improve their energy efficiency and save money, so they can concentrate on the day-to-day running of their business.”

James Holian
Head of Business Banking at NatWest Group

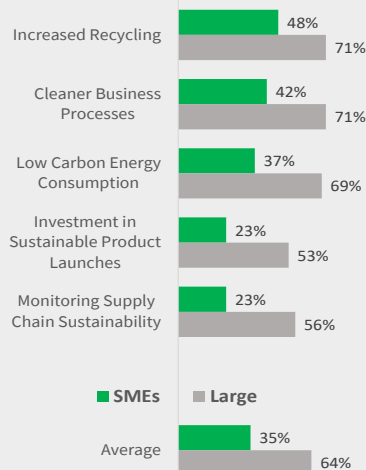
SME Sustainability PMI: Actions in the next 12 months

Which of the following actions, if any, is your company prioritising to improve environmental sustainability in the next 12 months?

UK SME Sustainability PMI: Actions
Percent reporting 'high priority'



SMEs vs. Large Companies (Q4 2023)
Percent reporting 'high priority'



Sustainability actions become less of a priority for UK SMEs, but large firms report a renewed rise

In this section we look at the actions on sustainability that UK businesses are prioritising during the year ahead.

NatWest Sustainability PMI data highlighted a slight fall in the prioritisation of sustainability action at SMEs, with the index for service firms hitting a survey-record low.

In contrast, large enterprises noted a rise in sustainability prioritisation since Q3.

Latest data revealed a renewed fall in the proportion of UK SMEs planning to prioritise environmental sustainability over the next 12 months. Dropping to 35%, from 36% in the previous quarter, the headline index reading was a joint record-low.

Meanwhile, a higher percentage of large companies planned to prioritise sustainability goals during 2024. At 64%, up from 59% recorded in the previous quarter, large companies were again much more inclined to prioritise sustainability actions compared to their small and medium-sized counterparts.

Four out of five types of sustainability action see a fall in prioritisation

UK SMEs downgraded their sustainability plans for four out of five monitored actions. The exception was Increased Recycling, which at 48% remained the highest priority for UK SMEs. However, this was the joint-lowest reading since the survey began at the start of 2020.

Survey-record-lows were registered for the prioritisation of Cleaner Business Processes and Monitoring Supply Chain Sustainability, while the percent of firms

prioritising Investment in Sustainable Product Launches slipped to the lowest for a year-and-a-half. Moreover, the latter two were also the joint-lowest ranking priority goals.

Low Carbon Energy Consumption saw the biggest downgrade from the previous quarter, with 37% of SMEs citing this as a high priority (compared to 39% in Q3). This was also down sharply from the peak seen in the second quarter of 2022 (51%).

Services SMEs continue to lag behind their manufacturing counterparts

In terms of prioritising sustainability goals by sector, SME services firms have now trailed behind their manufacturing counterparts for the past one-and-a-half years. In the final quarter of 2023, both the sectors downgraded their sustainability plans, with only 31% of services firms and 37% of goods producers planning to prioritise environmental sustainability over the course of 2024.

Increased Recycling remained the top priority for both the sectors, and by a considerable margin. Notably, Monitoring Supply Chain Sustainability registered as the lowest priority for SME manufacturers, with firms often finding it difficult to track the sustainability of their suppliers.

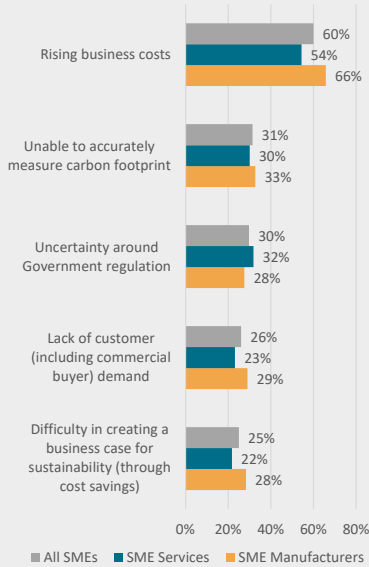
Investment in Sustainable Product Launches was the least prioritised sustainability action for SME service providers. Firms often noted that the weak demand environment and ongoing cost of living crisis had dissuaded customers from opting for greener products.

Special Question: Sustainability Obstacles in 2024

Which of the following are the largest obstacles to your business in becoming more sustainable in 2024? (Select all that apply*)

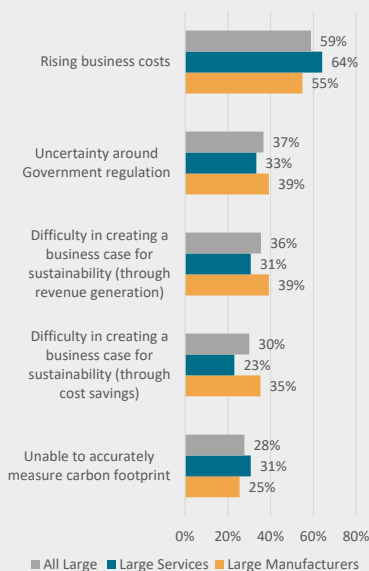
UK SMEs

Top five obstacles



Large UK enterprises

Top five obstacles



*The full list of obstacles listed by the survey were; rising business costs, lack of sustainable suppliers, shortages of skilled staff in sustainability, unable to accurately measure carbon footprint, lack of customer (including commercial buyer) demand, difficulty in creating a business case for sustainability (through revenue generation), difficulty in creating a business case for sustainability (through cost savings), lack of availability of investment/funding, uncertainty around Government regulation and environmental sustainability is not a priority for my business.

Rising business expenses cited as key barrier to progress on environmental sustainability in 2024

In this section, we look at the obstacles that UK SMEs face in becoming more sustainable in 2024.

Of the ten potential barriers covered by the survey, rising business costs were cited as the biggest challenge for SMEs when looking to improve their environmental sustainability. Six-in-ten SMEs noted this as the largest obstacle, with manufacturers more likely to report this as a constraint than services companies.

When assessing the major barriers to becoming more environmentally sustainable over the next year, rising business costs were by far the most widely cited factor among SMEs. The inability to accurately measure their carbon footprint and uncertainty around government regulation were meanwhile ranked in second and third place as obstacles to improving sustainability over the next 12 months.

Majority of SMEs see rising business costs as a barrier to improving their environmental sustainability

The majority of SMEs (60%) noted that higher business expenses were a large obstacle to pursuing sustainability plans in 2024. Manufacturing firms were more likely to see costs as a challenge than services companies (66% versus 54%).

Furthermore, the proportion of SMEs stating rising costs as a barrier was nearly double that recorded for the next biggest obstacle; the inability to accurately measure their carbon footprint (31% of all SMEs).

One-third of SMEs view difficulties measuring their carbon footprint as a barrier to sustainability action

UK SMEs cited an inability to accurately measure their carbon footprint as the second-biggest obstacle in making their company more sustainable in 2024.

Around 31% of SMEs noted challenges with measuring their impact on the environment, compared to 28% of large firms. A number of companies reported that suppliers, particularly those based overseas, were often unable to provide information on their carbon emissions, which made it challenging to calculate their companies' overall footprint.

A lack of customer demand for more sustainable products (26% of all SMEs) and difficulties in making a business case for sustainability in terms of cost savings (25%) were also key concerns.

Making a business case for more environmentally-friendly operations or products was a more widespread concern among large companies, however. Around 36% of large firms felt they may not be able to generate sufficient revenue from sustainability efforts, while 30% indicated that it could be a challenge to make a business case through cost savings.

Uncertainty around government policy more likely to hinder sustainability efforts of large firms

While rising business expenses were also the main concern among large companies when it came to future sustainability goals in 2024 (59%), uncertainty around government regulation placed second in the rankings of top obstacles.

Around 37% of large firms reported uncertainty around government policy as a constraint on sustainability plans for the year ahead, compared to 30% of SMEs.

There were widespread reports that insufficient government incentives and a lack of investment spending on green initiatives could constrain firms' ability to reduce their carbon footprint through 2024. Companies indicated that a wide range of policies could support their environmental plans, including spending on electric vehicle infrastructure, energy saving schemes, subsidies for the promotion of greener products, as well as clearer guidance on sustainability targets and carbon footprint measurement.

NatWest SME PMI[®]: Service Sector

Service sector activity revives

UK SME service providers signalled a strong end to 2023, with business activity rising for the second successive month. At 52.8 in December, the respective seasonally adjusted index picked up from 52.1 in November to indicate the strongest rate of expansion since last May. That said, growth momentum fell short of that seen for large companies.

The back-to-back increase in service sector output was supported by improved demand conditions, with companies often noting new client wins and increased activity at customers. Total new business likewise expanded for the second straight month in December, albeit modestly.

Companies remain cautious around staff hiring

Small and medium-sized services firms signalled a sustained rise in staffing levels during December. Employment has now increased in each of the past 34 months. However, the rate of payroll growth was the joint-slowest seen over this period and only marginal. Nevertheless, the upturn contrasted with a decline in staff numbers at large firms. Where higher staff numbers were reported, panellists generally linked this to ongoing and future company expansion plans. However, there were some mentions of firms choosing not to replace voluntary leavers amid the subdued economic climate.

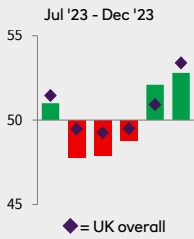
Input costs continue to rise at historically strong rate

Services companies with fewer than 250 employees continued to record higher input costs during December. At 62.8, the respective seasonally adjusted index picked up from 61.4 in November to signal a sharp rate of inflation that exceeded the series average. That said, the pace of increase was slower than the post-pandemic trend and not as rapid as that seen for large firms. Greater salary payments were cited as a key driver of inflation, though firms also noted that suppliers had often hiked prices due to the generally strong inflationary environment. As a result, prices charged by SMEs also rose sharply, albeit with the pace of increase softer than that seen for large companies.

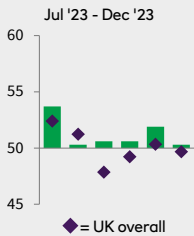
Business sentiment improves to 22-month high

Amid signs of firmer growth momentum and improved sales, SME services companies expressed greater optimism towards the year-ahead outlook for activity during December. The degree of positive sentiment was the strongest recorded in nearly two years. Firms widely anticipated that a recovery in economic conditions, new product releases and improved marketing will drive growth over 2024.

Business Activity Index



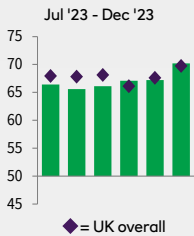
Employment Index



Input Prices Index



Future Activity Index

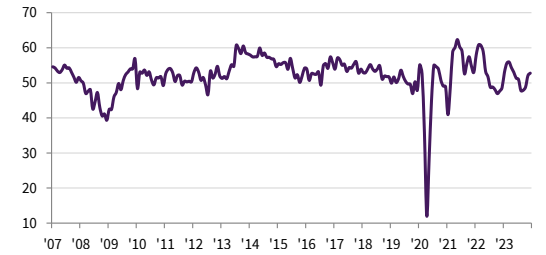


Business Activity Index

sa, >50 = growth since previous month

52.8

Dec '23

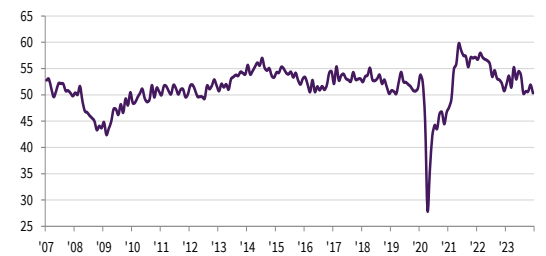


Employment Index

>50 = growth expected over next 12 months

50.3

Dec '23

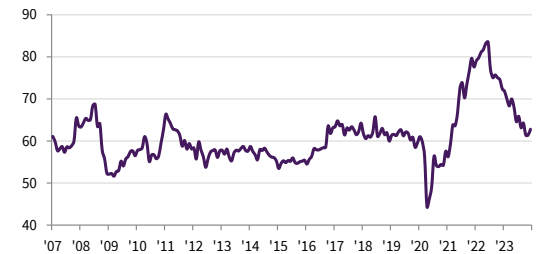


Input Prices Index

sa, >50 = growth since previous month

62.8

Dec '23



Future Activity Index

sa, >50 = growth since previous month

70.2

Dec '23



NatWest SME PMI[®]: Manufacturing Sector

Sharp drop in UK SME manufacturing output

UK SME manufacturers recorded a fall in production volumes for the fifth consecutive month in December, with the rate of decline picking up slightly since November. The respective seasonally adjusted index fell from 45.7 in November to 45.5, to signal the most pronounced contraction in output in 14 months. Large companies also pared back their output volumes, and at an identically sharp rate.

Central to the decrease in output was a further deterioration in overall demand conditions. New order intakes have fallen in each month since May 2022. The latest drop was sharp overall, despite easing to the softest in six months. Reduced market confidence and greater pressure on spending due to the higher interest rate environment were cited as having dampened sales.

Job shedding intensifies

Small and medium-sized manufacturers reduced their staffing numbers for the fourth consecutive month in December. The rate of job shedding quickened over the course of the fourth quarter, with the latest reduction the fastest since September 2020. Firms often mentioned adjusting their payroll numbers in line with lower business requirements, with some companies actively laying off staff or delaying hiring plans.

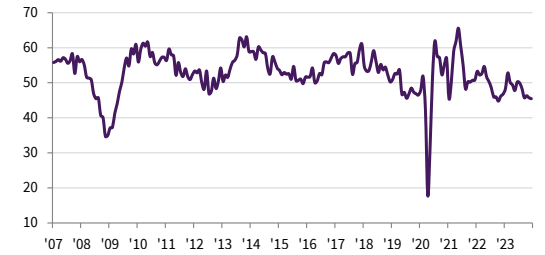
Fresh rise in average input costs

SME manufacturers in the UK signalled fresh increases in both input prices and output charges in December. This marked the first rise in expenses for eight months, albeit one that was mild, with firms often citing supplier price hikes (particularly for raw materials) and greater energy costs. Selling prices meanwhile rose for the first time in three months, and at a solid pace, as companies often sought to pass on additional expenses to customers.

Business optimism strengthens slightly in December

Although SME goods producers faced challenging market conditions, firms remained optimistic that output would rise in the coming 12 months. Moreover, the degree of confidence strengthened in December, and was broadly in line with that recorded for large companies. Hopes of new client wins, the launch of new products and increased investment underpinned growth forecasts. That said, overall sentiment remained softer than the survey average.

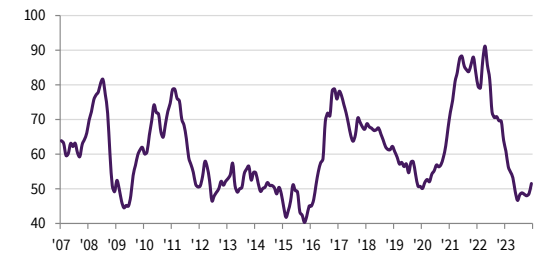
Business Activity Index
sa, >50 = growth since previous month
45.5
Dec '23



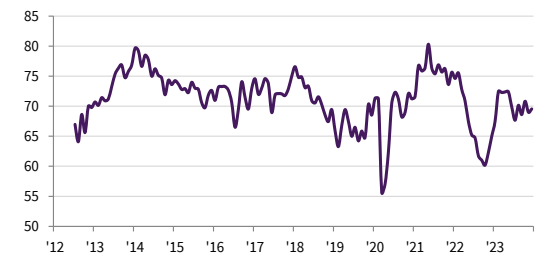
Employment Index
>50 = growth expected over next 12 months
47.2
Dec '23



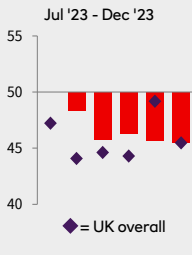
Input Prices Index
sa, >50 = growth since previous month
51.5
Dec '23



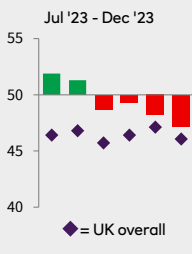
Future Activity Index
sa, >50 = growth since previous month
69.5
Dec '23



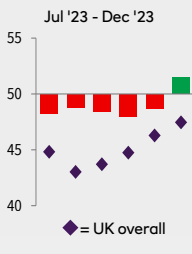
Business Activity Index
Jul '23 - Dec '23



Employment Index
Jul '23 - Dec '23



Input Prices Index
Jul '23 - Dec '23



Future Activity Index
Jul '23 - Dec '23



NatWest SME PMI[®]: Construction Sector

Sustained downturn in construction work

The seasonally adjusted Business Activity Index registered 47.3 in December, up from 47.0 in November but below the neutral 50.0 value for the fifth consecutive month. Lower volumes of SME construction output largely reflected a prolonged downturn in housing activity.

Survey respondents widely commented on cutbacks to major house building projects and headwinds to demand from elevated interest rates. The speed of the downturn in total construction output was nonetheless slower than seen for large enterprises throughout the final quarter of 2023.

Staff hiring maintained

SME construction companies continued to add to their payroll numbers at the end of 2023. At 51.6, the seasonally adjusted Employment Index was up from 50.9 in November and pointed to a twelfth consecutive monthly rise in staffing levels. The rate of job creation was the strongest since August, but only modest overall.

Suppliers pass on lower raw material costs

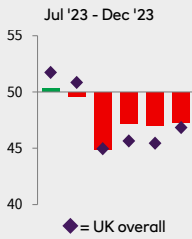
December data indicated a renewed increase in average cost burdens across the SME construction sector, following sharp declines in the prior two months. In contrast, large enterprises saw reductions in input prices throughout the final quarter of 2023. Large enterprises secured price discounts from suppliers due to lower raw material costs and negotiations in the wake of weaker demand conditions, according to anecdotal evidence.

Meanwhile, the latest survey indicated worsening supplier performance for construction SMEs, which partially reversed the improvements seen in the middle of last year. The seasonally adjusted Suppliers' Delivery Times Index was the lowest for nine months, but signalled only a modest lengthening of vendor lead times.

Positive business activity expectations for 2024

At 60.4 in December, the Future Activity Index indicated that SME construction companies remain upbeat overall about their growth prospects for the year ahead, although the degree of optimism was lower than for large enterprises. Survey respondents typically commented on hopes of lower borrowing costs and improving market conditions, although some cited elevated recession risks as a factor holding back optimism for 2024.

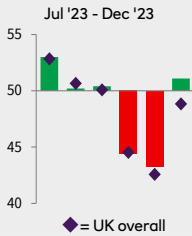
Business Activity Index



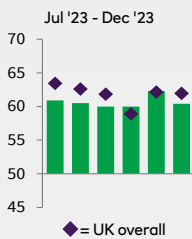
Employment Index



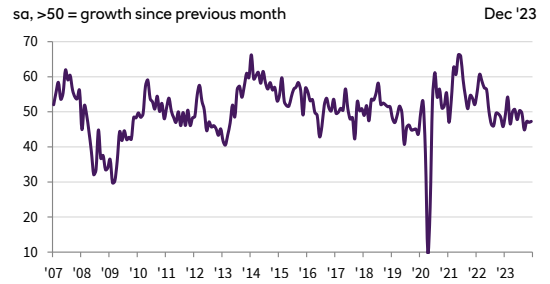
Input Prices Index



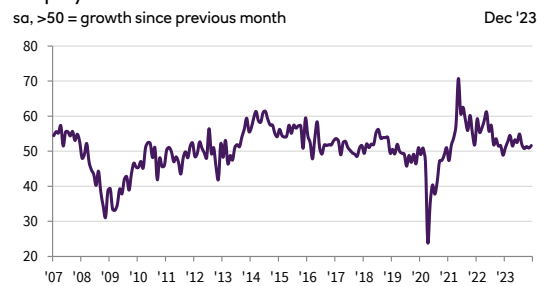
Future Activity Index



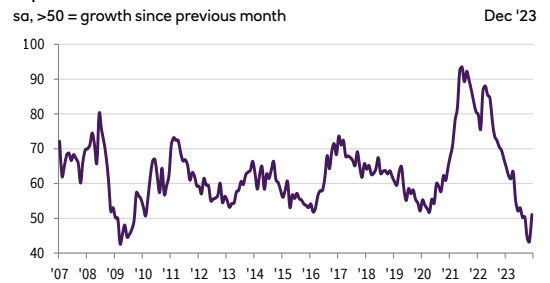
Business Activity Index



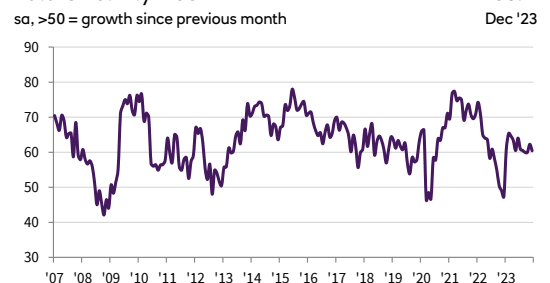
Employment Index



Input Prices Index



Future Activity Index



About the NatWest Sustainable Business Tracker

The NatWest Sustainable Business Tracker is a quarterly report designed to monitor business performance and sustainability at enterprises with 1-249 employees.

NatWest Sustainable Business Tracker is based on responses to questionnaires sent to companies with 1-249 employees that participate in monthly UK Purchasing Managers' Index[®] (PMI[®]) surveys compiled by S&P Global.

The panel of around 850 small and medium sized enterprises is stratified by detailed sector, based on contributions to GDP.

SME PMI[®] survey responses are collected by S&P Global in the second half of each month and indicate the direction of change compared to the previous month. A diffusion index is calculated for each survey variable. The index is the sum of the percentage of 'higher' responses and half the percentage of 'unchanged' responses.

The SME PMI[®] indices vary between 0 and 100, with a reading above 50 indicating an overall increase compared to the previous month, and below 50 an overall decrease. The indices are then seasonally adjusted.

Indices are compiled for a range of survey variables, including business

activity, new orders, employment, input costs, prices charged, outstanding business and future activity.

The SME PMI[®] data for September were collected 06 – 20 December 2023. Historical data are available from January 1998 for the All-Sector SME Business Activity Index.

Manufacturing data are available from January 1992, Services data from July 1996 and Construction data from April 1997.

SME Sustainability PMI[®] data are compiled on a quarterly basis. The latest survey was compiled in December 2023. Companies are asked about the sustainability actions they are looking to prioritise over the next year, and the results are compared against those seen for large companies. The latest survey also monitored obstacles to sustainability actions.

For further information on the PMI survey methodology, please contact economics@spglobal.com.

Index summary

NatWest SME PMI® data (All-Sector)

sa, 50 = no change over previous month. *50 = no change over next 12 months.

	Activity	New Business	Future Activity	Employment	Outstanding Business	Input Prices	Prices Charged
Jul '23	50.8	49.1	66.1	53.6	45.0	62.2	55.1
Aug '23	48.1	45.5	65.8	50.6	44.1	60.0	54.2
Sep '23	47.3	46.6	65.9	50.4	43.7	60.8	54.5
Oct '23	48.3	47.1	67.0	50.5	44.7	58.0	53.2
Nov '23	50.7	48.9	67.1	51.3	44.0	58.0	53.7
Dec '23	51.2	50.1	69.3	50.0	46.3	60.1	54.2

NatWest SME PMI® data (by sector)

	All-Sector Business Activity	Service Sector Business Activity	Manufacturing Business Activity	Construction Business Activity
Jul '23	50.8	51.0	50.0	50.3
Aug '23	48.1	47.8	48.4	49.6
Sep '23	47.3	47.9	45.8	44.9
Oct '23	48.3	48.8	46.3	47.2
Nov '23	50.7	52.1	45.7	47.0
Dec '23	51.2	52.8	45.5	47.3

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About NatWest

NatWest serves customers in England, Wales and Western Europe, supporting them with their personal, private, and business banking needs. NatWest helps customers from opening student accounts, to buying their first home, setting up a business, and saving for retirement.

Alongside a wide range of banking services, NatWest offers businesses specialist sector knowledge in areas such as manufacturing and technology, as well as access to specialist entrepreneurial support.

NatWest has been running MoneySense, an impartial financial education programme for 5–18 year-olds, for more than 21 years. By the end of 2018, NatWest will help another 1 million young people to understand and take control of their finances.

About S&P Global

S&P Global (NYSE: SPGI) S&P Global provides essential intelligence. We enable governments, businesses and individuals with the right data, expertise and connected technology so that they can make decisions with conviction. From helping our customers assess new investments to guiding them through ESG and energy transition across supply chains, we unlock new opportunities, solve challenges and accelerate progress for the world.

We are widely sought after by many of the world's leading organizations to provide credit ratings, benchmarks, analytics and workflow solutions in the global capital, commodity and automotive markets. With every one of our offerings, we help the world's leading organizations plan for tomorrow, today. www.spglobal.com.

About PMI

Purchasing Managers' Index™ (PMI®) surveys are now available for over 40 countries and also for key regions including the eurozone. They are the most closely watched business surveys in the world, favoured by central banks, financial markets and business decision makers for their ability to provide up-to-date, accurate and often unique monthly indicators of economic trends.

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