

COMMERCIAL BANKING



BUSINESS IN BRITAIN

A SURVEY OF BUSINESS OPINIONS AND TRENDS
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A Survey of Business Opinions and Trends

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Introduction

Welcome to the latest instalment of our twice-yearly Business in Britain survey. The survey offers invaluable, as well as timely, guidance on the recent performance and near-term expectations of domestic businesses, especially in the SME segment. The latest wave of the survey draws on the experiences and opinions of 1,501 companies covering all sectors and regions.

Against an improving economic backdrop, the survey indicates that sentiment about recent orders, sales and profits has improved significantly over the last six months. The increased expectations have been broad-based, covering all sectors and regions, and in some cases have climbed to levels not seen since the early 1990s. Exports to Europe and the rest of the world have also rebounded markedly.

These gains may help to explain the buoyancy of corporate confidence about the outlook for the next six months. Anticipated rises in demand and profits in the first half of this year have fed into strengthened plans for hiring and capital expenditure. The net balance of companies reporting difficulties in the recruitment of skilled workers rose for the third consecutive survey. In principle, this could put upward pressure on pay growth. However, the index remains well-below its pre-crisis readings which should contain wage pressures. Meanwhile the expected rise in capital outlays is underpinned

by a rise in the share of firms who report that they are operating at full capacity. If these plans are delivered, then this investment will provide a further fillip to sustainable economic growth.

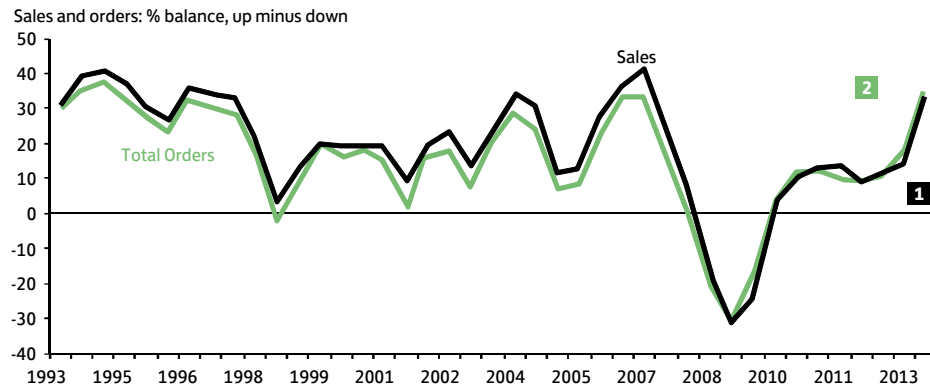
I would like to thank all the firms that have participated in the survey and provided valuable insights into UK economic developments. I would like to wish all businesses every success in 2014 and look forward to supporting your endeavours.

Stephen Pegge
Group External Relations Director
Lloyds Banking Group

Recent trends in the SME market

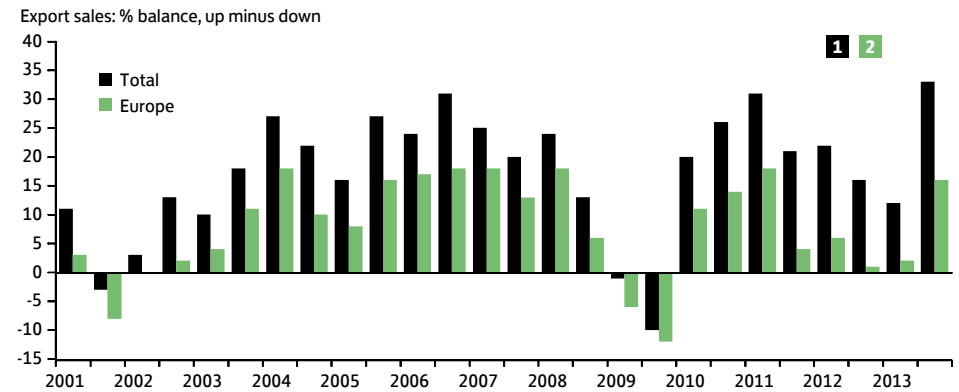
Sales and incoming orders point to a robust expansion of economic activity

Sales, orders and export sales balances over the last six months



1 The net balance for sales in the past six months rose by eighteen points to **33%**, which is the highest level since mid-2007. This is consistent with the firm economic recovery over the second half of 2013.

2 The net balance for incoming orders over the past six months also rose sharply from 18% in the previous survey to **34%**, with 47% of respondents reporting an increase in new business and 13% citing a decline. The index is now at its highest reading since 1994 and strongly suggests that the current robust pace of expansion is set to continue.



1 The net balance for total exports in the past six months has picked up by twenty-one points to **33%**, which is just short of its all-time high (34%) reached in 1995 and well above its long-run average.

2 Sentiment about shipments to Europe over the last six months is also up, with the net balance rising from 2% in the previous survey to a two-year high of **16%**. This recovery in European sales lines up with a rise in euro area demand as it emerged from recession in Q2 2013.

Sales and orders expected to increase over the next six months

| | 2014 H1 | 2013 H2 |
|----------------------|---------|---------|
| Expected Sales: Up | 60% | 50% |
| Expected Sales: Down | 9% | 14% |
| Balance | 51% | 36% |

| | 2014 H1 | 2013 H2 |
|-----------------------|---------|---------|
| Expected Orders: Up | 55% | 45% |
| Expected Orders: Down | 6% | 8% |
| Balance | 49% | 37% |

| | 2014 H1 | 2013 H2 |
|------------------------------|---------|---------|
| Expected Total Exports: Up | 54% | 33% |
| Expected Total Exports: Down | 6% | 10% |
| Balance | 48% | 23% |

| | 2014 H1 | 2013 H2 |
|----------------------------------|---------|---------|
| Expected Exports to Europe: Up | 40% | 23% |
| Expected Exports to Europe: Down | 9% | 13% |
| Balance | 31% | 10% |

The net balance for expected total sales over the next six months increased by fifteen points to **51%**, which it last touched on the eve of the 2008-09 downturn. The corresponding index for total orders rose by twelve points to **49%** - an all-time high since the survey began in 1992. Both indices point to a potential firming in economic activity over 2014H1.

The burgeoning optimism regarding sales and orders is also evident in foreign shipments. The net balance for expected exports over the next six months rose by twenty-five points to **48%**.

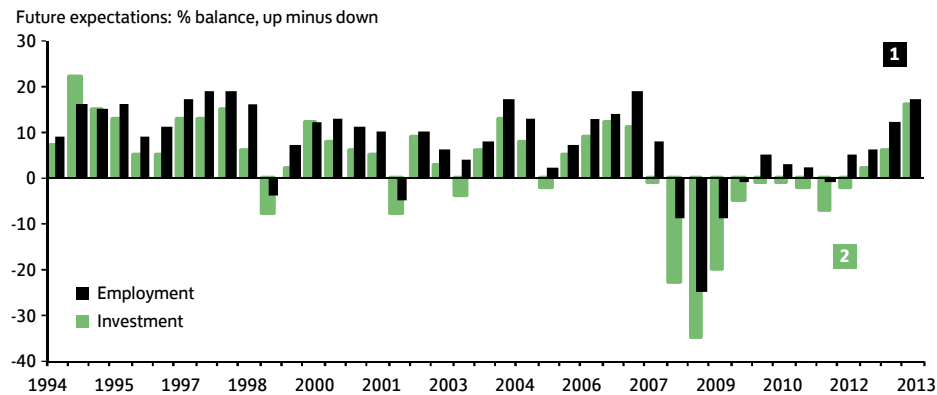
The net balance for exports to Europe in the next six months rose by 21 points to **31%**. Domestic companies are most confident about sales to Asia-Pacific (36%), Middle East/Africa (35%), Europe (31%), US and Canada (26%) and Latin America (23%).

Business activity set to firm further

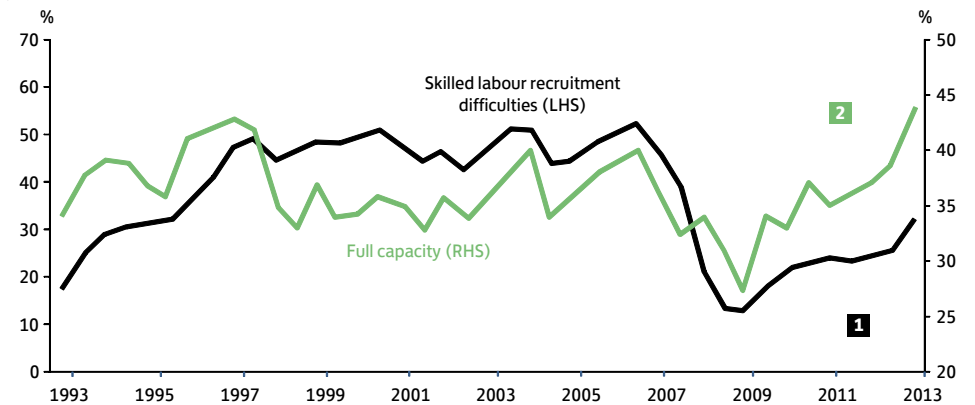
The improvements in the sales and new orders net balances over the past six months tally with the recovery in UK economic output since the start of 2013. Moreover, the strengthening of their corresponding forward-looking counterparts, especially orders, which have climbed to a record high, suggests that this upswing is set to continue into 2014H1. Survey respondents also envisage increasing their exports, with optimism highest for the Asia-Pacific and Middle East/Africa regions.

Hiring and investment plans strengthen further

Investment, employment and capacity trends



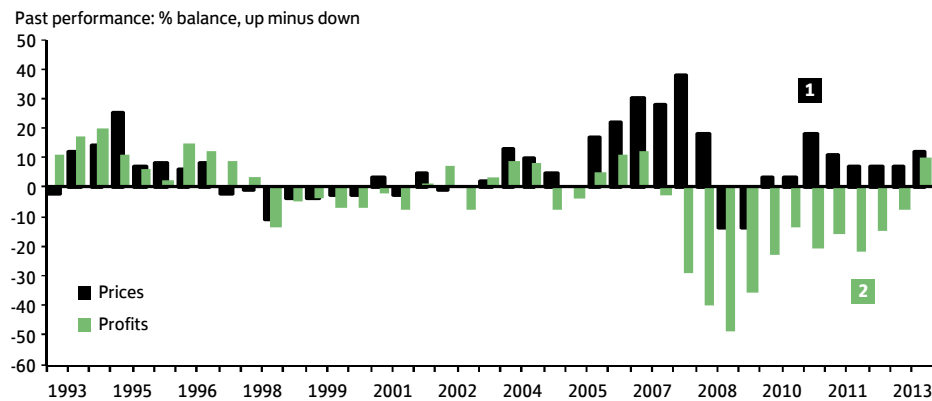
- 1** Firms continue to anticipate increasing their hiring over the next six months with the index of expected staff levels rising for the fourth consecutive survey. The five-point rise took the net balance to a six-year high of **17%**. This suggests that the recent rise in employment is set to continue as economic activity picks up.
- 2** Expected capital expenditure is also on an ongoing upswing with the net balance rising by ten points to **16%** which is the highest level since 1994. The net balance has been in positive territory for three consecutive months for the first time since 2006-07.



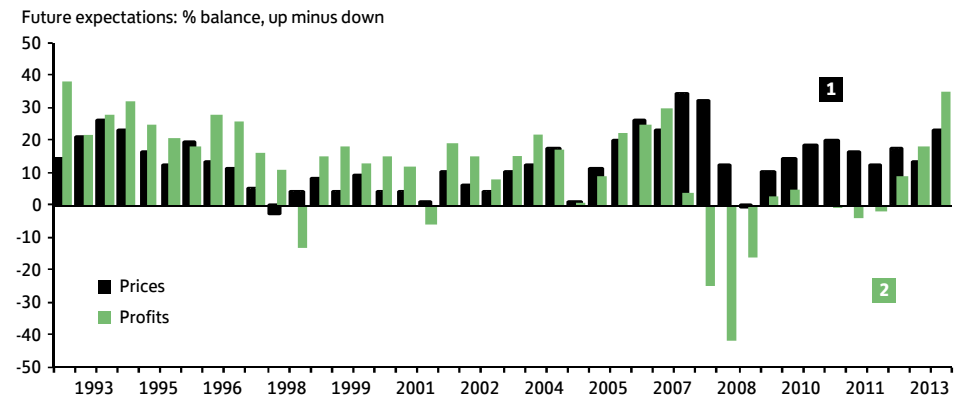
- 1** The share of companies reporting frictions in the recruitment of skilled workers continues its post-crisis recovery with a six-point increase to **32%**. The recent rises point to a gradual tightening in the market for skilled labour which could put upward pressure on pay growth, although the index is still well below its 1997-2007 readings, which averaged 47%.
- 2** The percentage of firms claiming to be operating at full capacity increased for the fourth survey in a row to **44%**, which is the highest score since the survey began in 1992. Eliminating any potential capacity constraints as growth strengthens may underpin the expected rise in capital expenditure.

Both prices and profits are expected to increase

Prices and profits: past performance and future expectations



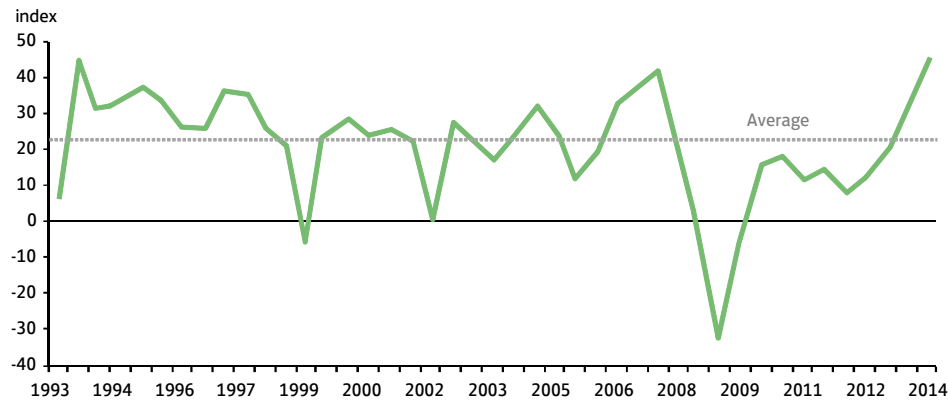
- 1 After remaining stable at 7% for three successive surveys, the net balance for prices charged in the last six months rose to **12%** which was just slightly lower than the outturn expected at the time of the last survey.
- 2 The net balance for profits over the past six months continued its recovery since 2009 with an eighteen-point rise to **10%**, the first positive balance since 2007.



- 1 Firms anticipate a greater scope for raising prices over the next six months with the net balance rising by ten points to **23%**, its highest score since 2008.
- 2 These higher prices may help to underpin corporate expectations of stronger profits over the next six months with the net balance rising for the fourth consecutive survey to **35%**. The index is close to the all-time peak of 38% seen in 1993.

Overall business confidence close to all-time peak

Business confidence



Our business confidence measure, which is based on the average of the net balances for expected sales, orders and profits over the next six months, has jumped by fifteen points to **45%**. This was the fourth consecutive increase in the net balance and it is now just short of its all-time high of 46% recorded in the early 1990s. The rise was driven by double-digit improvements in all of the underlying elements, led by profits and sales.

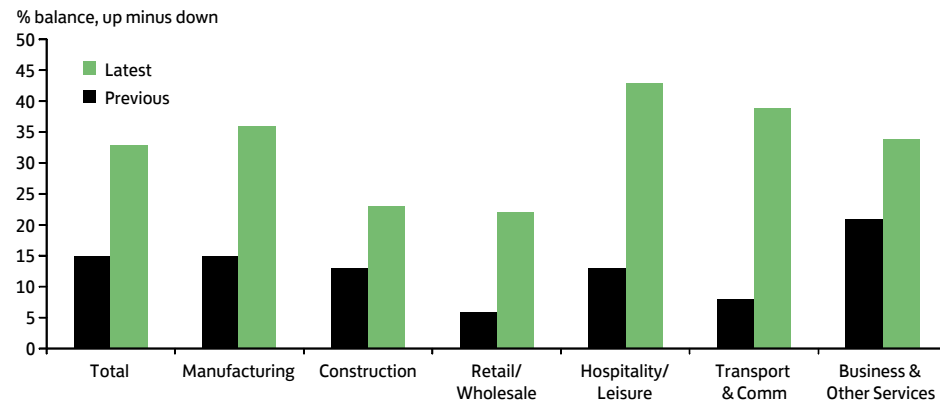
The economic outlook is strengthening

Our survey indicates that company optimism about the economic outlook and their own business prospects has become increasingly buoyant. These substantive rises in anticipated sales, orders and profits have fed into expectations of rising staff headcounts. These improvements, which suggest that the recovery is becoming increasingly entrenched and resilient, may also have helped to support an expected rise in corporate capital expenditures.

The sectoral picture

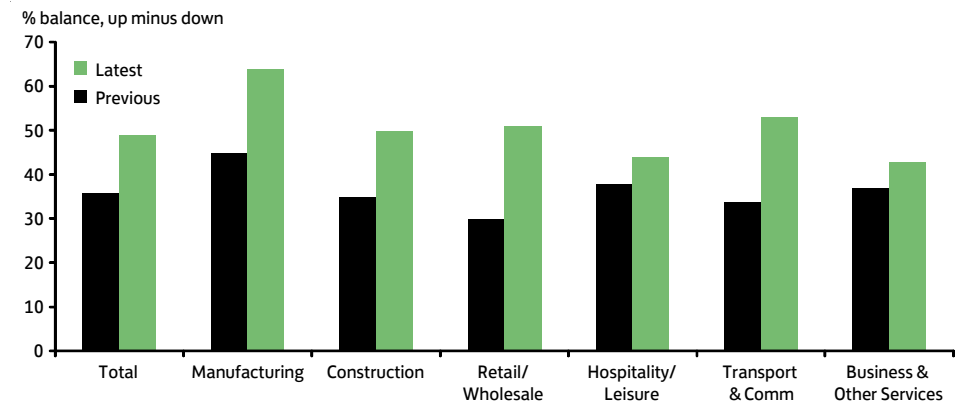
All sectors saw boost to sales and expected order books

Sales over the last six months



All the sectors saw notable rises in the net balance for sales over the last six months. These increases range from ten points in construction to thirty-one points in transport and communications. Hospitality and leisure report the highest net balance of 43%, followed by transport and communications at 39% and manufacturing with 36%.

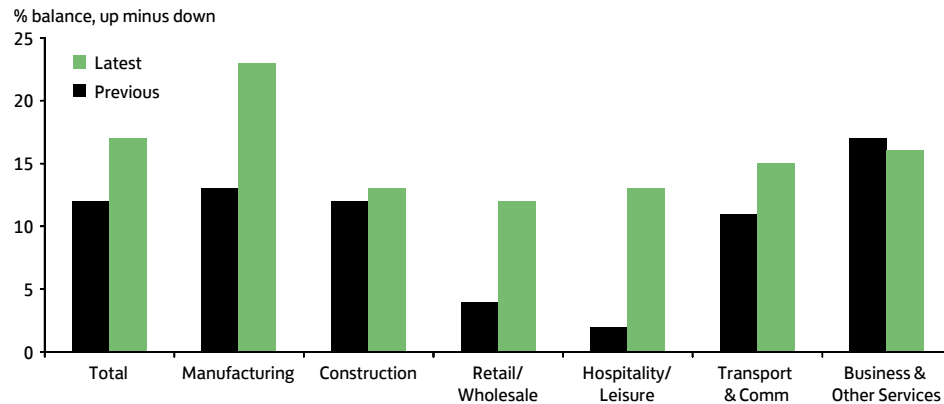
Orders over the next six months



The net balances for order book levels over the next six months also showed across-the-board increases. The retail and wholesale, manufacturing, and transport and communication sectors report the largest climbs in optimism with rises of twenty-one, nineteen and nineteen points to 51%, 64% and 53% respectively.

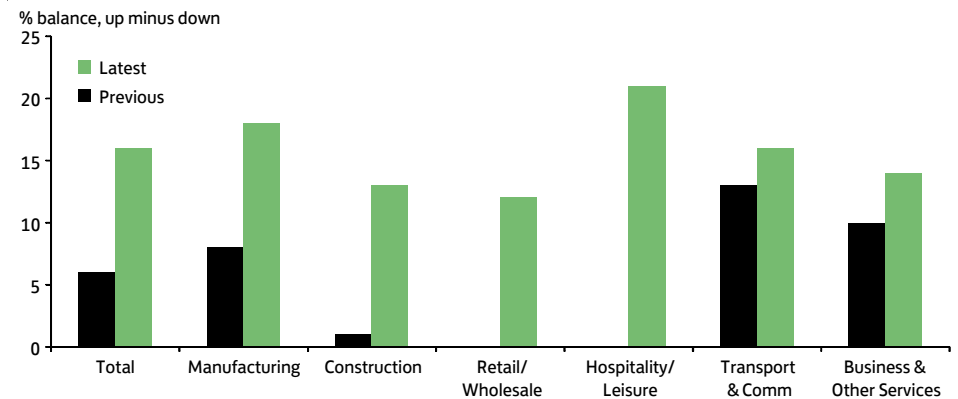
Employment and investment intentions firm

Employment in the next six months



All sectors expect an increase in headcount over the next six months with the exception of business and other services where the net balance has fallen by one point to 16%. The hospitality and leisure, and manufacturing sectors report the largest index rises of eleven and ten points to 13% and 23%, respectively, with the latter at all-time high.

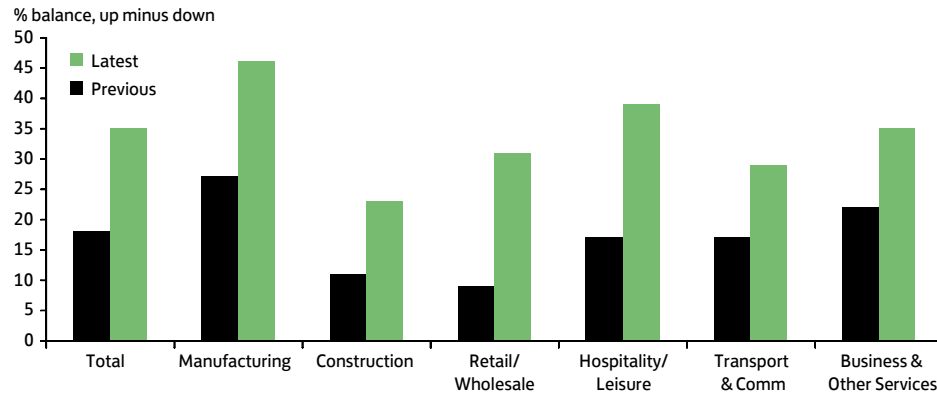
Capital expenditure in the next six months



The overall rise in expected capital expenditures over the next six months has been replicated across all the sectors, especially hospitality and leisure which saw a twenty-one point rise to 21%, and retail and wholesale, and construction, where the net balances increased by twelve points each to 12% and 13% respectively.

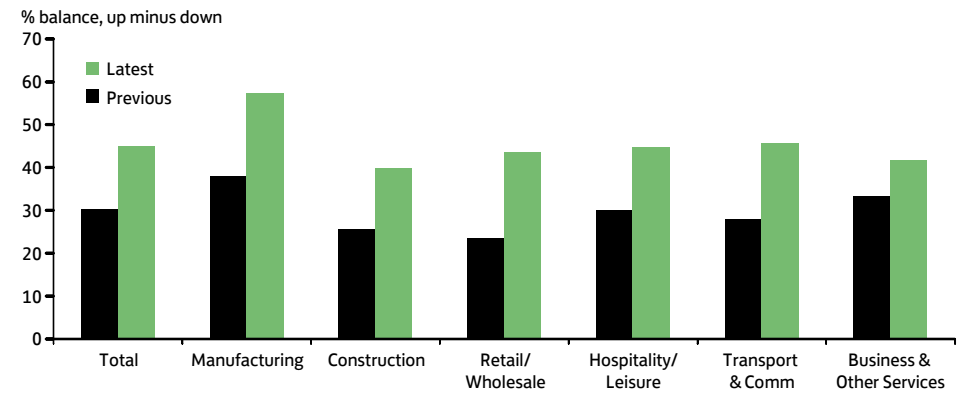
Profits and business confidence also up across sectors

Profits in the next six months



The net balance for expected profits over the next six months increased everywhere, especially in hospitality and leisure, retail and wholesale, and manufacturing, where it rose by twenty-two, twenty-two and nineteen points to 39%, 31% and 46% respectively. The net balance remains highest in manufacturing.

Business Confidence

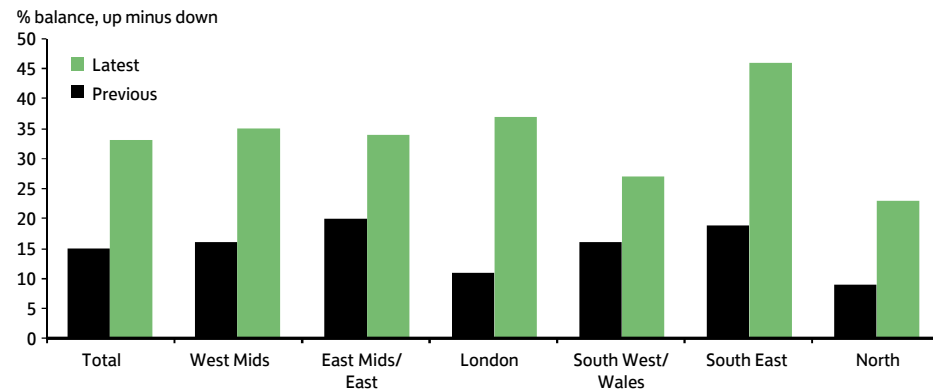


Overall business confidence increased across all the sectors for the third consecutive survey, again signalling a firming upswing. All segments reported double-digit rises, with the exception of business and other services which saw an eight-point increase. Retail and wholesale reported the largest improvement, with sentiment jumping by twenty points to 44%, followed by manufacturing, up nineteen points to 57%, and transport and communication with an eighteen-point rise to 46%.

The regional picture

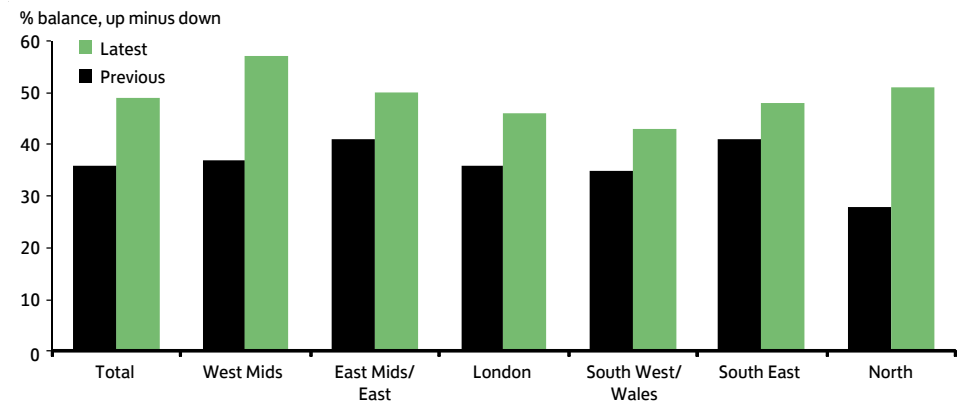
Total orders set to continue rising across all regions

Sales over the last six months



The net balance for sales over the past six months increased across all regions. The index rose the most in the South East and London, by twenty-seven and twenty-six points to 46% and 37% respectively, while the South West and Wales reported the smallest rise of eleven points to 27%.

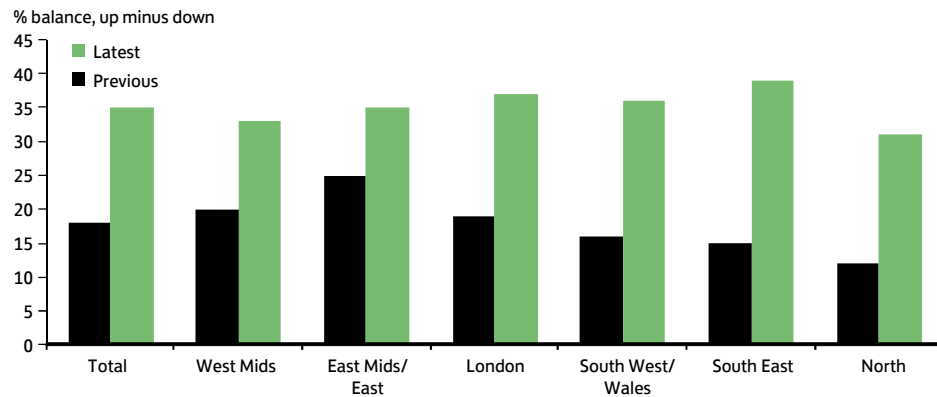
Orders over the next six months



All regions also posted an increase in the net balance for expected orders over the next six months which suggests that sales are set to remain strong. The North and the West Midlands recorded the largest rises of twenty-three and twenty points respectively to 51% and 57%. The smallest advances were recorded in the South West, East Midlands and East of England, and London.

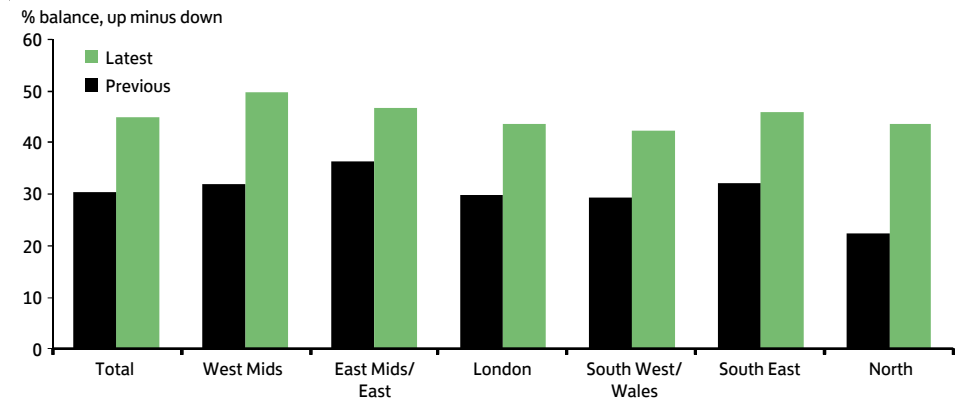
Business confidence jumps across the regions

Profits in the next six months



Firms across all regions also expect to see a rise in profits over the next six months. The South East, South West and Wales, and London reported the largest increases of twenty-four, twenty and eighteen points to 39%, 36% and 37% respectively. The lowest increase was in the East Midlands and East of England with a ten-point rise to 35%.

Business confidence

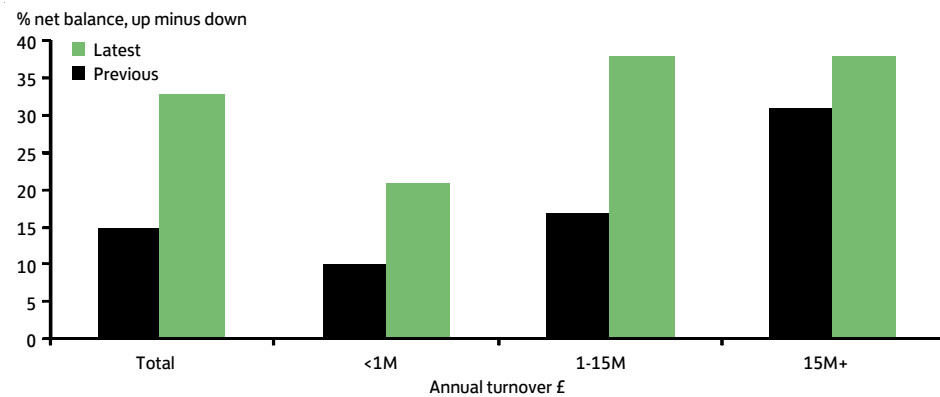


The broad-based regional gains in expected sales, orders and profits underpin similar outcomes for overall business confidence. The largest rises were in the North and West Midlands with rises of twenty-one and eighteen points respectively. The East Midlands and East of England saw the smallest improvement of ten points. The net balances all varied between 42% and 50%.

Analysis by size of firm

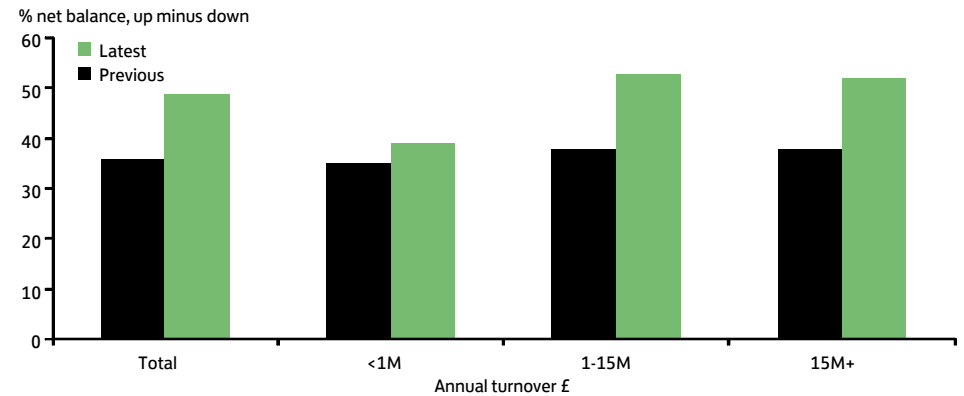
Orders expected to rise across all firm sizes

Sales over the last six months



A broad improvement in the net balance for sales over the last six months was led by firms with an annual turnover of £1m-£15m. These companies reported a twenty-one point increase in the index to 38%. Firms with sales of less than £1m scored an eleven-point increase to 21% while those achieving over £15m reported a seven-point increase to 38%.

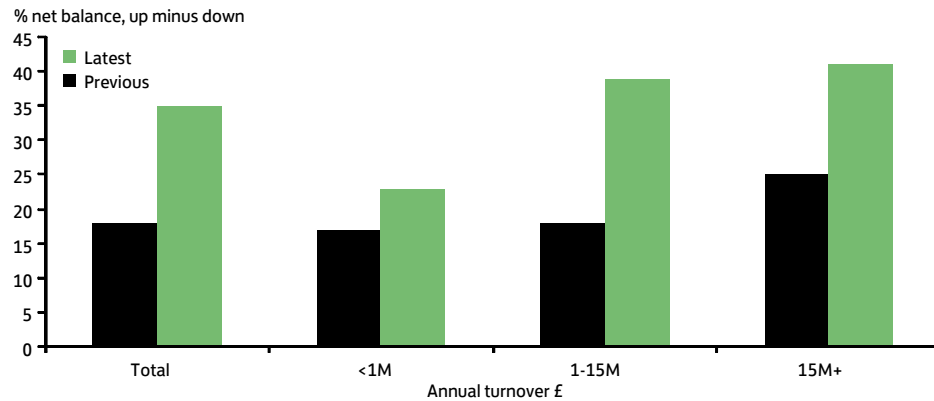
Orders in the next six months



Firms in all categories anticipate orders rising over the next six months, especially those in the £1m-£15m and above £15m bands whose net balances rose by 15% and 14% respectively.

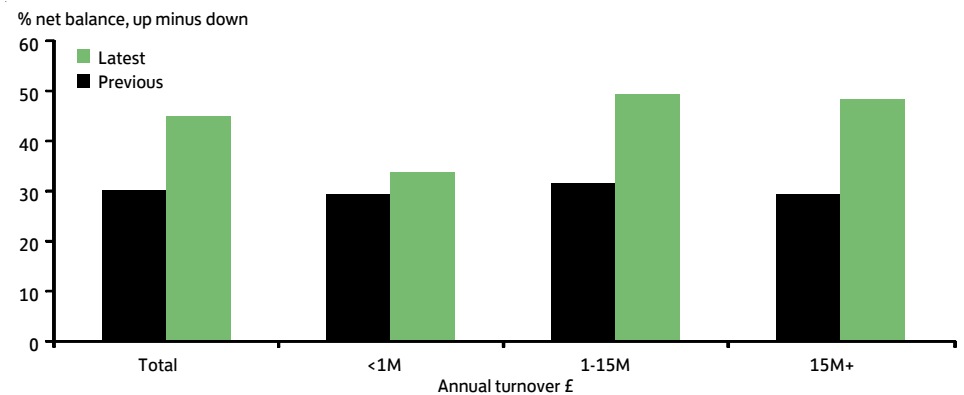
Business confidence increased the most for medium and larger companies

Profits in the next six months



Firms in the middle and upper end of the size distribution reported the largest net balance increases for profits over the next six months of twenty-one and sixteen points to 39% and 41% respectively. Firms with sales below £1m reported a six-point rise to 23%.

Business confidence



After being broadly equal across firms of all sizes in the last survey, confidence about the next six months rose by the most among companies with £1m-£15m and over £15m worth of sales whose net balances increased by eighteen and nineteen points respectively leaving them both on 49%. Smaller companies saw a rise in net sentiment of five points to 34%.

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