



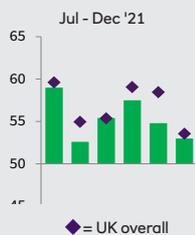
SME recovery trails behind large enterprises. Smaller firms less likely to prioritise sustainability action in 2022

NatWest SME Recovery PMI

52.6

Nov '21 54.1

Business Activity Index



NatWest SME Sustainability PMI

41%

Feb '20: 44%

Key findings

NatWest Sustainable Business Tracker highlights wide divergence between SMEs and large firms

Slower recovery from the pandemic has held back SME sustainability plans for 2022

Around 41% of UK SMEs cite sustainability action as a high priority, down from 44% in February 2020

A majority of large companies (60%) report sustainability action as a high priority, up from 57%

The NatWest Sustainable Business Tracker is a new quarterly report, designed to monitor business performance and sustainability actions at UK enterprises with 1-249 employees. Results are compiled from responses to IHS Markit's Purchasing Managers' Index® (PMI®) surveys.

Business performance among SMEs is tracked by our Recovery PMI, which monitors output, jobs, inflation and growth expectations.

Sustainability actions among small and medium sized enterprises (SMEs) are tracked by our Sustainability PMI, which monitors year ahead plans across five categories of action.

December data illustrated that SME business performance continued to trail behind large companies due to renewed COVID-19 stringency measures, rapid cost inflation and supply disruption.

SME sustainability plans have been adversely impacted by the need to make further progress on recovery from the pandemic. Survey data compiled for the NatWest Sustainable Business Tracker highlighted that UK SMEs have reduced their focus on sustainability action in comparison to the levels seen prior to the pandemic.

By contrast, large companies reported a considerable increase in their prioritisation of sustainability action in 2022, which extended the gap between plans among smaller businesses.

SME Recovery PMI

The latest SME Recovery PMI survey pointed to a slower expansion of overall business activity at small and medium-sized enterprises as the Omicron variant weighed on the UK economy.

At 52.6 in December, the All-Sector SME Business Activity Index fell from 54.1 in November and indicated weakest upturn in activity for four

months. Growth slowed across services (53.0) and construction (52.1), while manufacturing output expanded only slightly (50.8).

SMEs across all three sectors saw weaker increases in activity than large companies. The slowdown was partly linked to supply bottlenecks and challenges retaining staff.

SMEs also faced rapid increases in expenses, which in turn drove an unprecedented rise in selling prices during December. Nevertheless, firms remain highly optimistic about 2022 growth prospects, with confidence holding steady despite sharply rising COVID-19 cases.

SME Sustainability PMI

On average across the five areas monitored by the survey, around 41% of SMEs stated that sustainability action was a high priority in the next 12 months, down from 44% in February 2020. This compared with 60% of large companies, up from 57% prior to the pandemic. The latest survey was collected in September 2021 and referenced plans for the year ahead.

Comparing SME sustainability action plans for 2022 against those reported prior to the pandemic, the only increase was in low carbon energy consumption (41%, up from 40%).

SME manufacturers were much less likely to downgrade their sustainability plans than service providers. On average, 45% of SME manufacturers cited sustainability actions as a high priority in the next 12 months, down only slightly from 47% in February 2020. The equivalent for SME service providers was 37%, down sharply from 42% prior to the pandemic.

The biggest fall in SME manufacturers' action plans was prioritising investment in sustainable product launches (31%, down from 38%).

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Foreword



It's great to launch NatWest's UK Sustainable Business Tracker, new for 2022, which will review the progress that the UK's SME community is making in implementing sustainable and environmentally responsible practices. The quarterly Purchasing Managers Index (PMI) will reveal the latest green attitudes and priorities for the nation's businesses as well as general trends and focuses, including on prices, employment and investment. Building on the momentum from COP26, the UK Sustainable Business Tracker will shine a light on how best to support the UK's businesses in their transition to net zero.

Our first Sustainable Business Tracker shows that the sustainability experiences of SMEs and large businesses are diverging. Compared with early 2020, SMEs are now prioritising sustainability less (41% down from 44% in February 2020), whilst large businesses are doing so more (60% up from 57% in February 2020). This shift shows the pressures SMEs are under as they direct attention to their recovery as the UK transitions to living with Covid.

It's important that SMEs are aware that sustainability measures can boost their recovery, and even fuel their growth, for example through increasing efficiency, lowering energy bills and by future proofing their operations. [NatWest's Springboard to Sustainability](#) report, published in October 2021, found that 50% of the UK's carbon reduction ambition can be delivered by the SME sector. This could also unlock a £160 billion opportunity for them. Sustainability, recovery and growth go hand-in-hand and SMEs need to be supported to know how to make the most of the opportunities that lie ahead.

The reduced proportion of SMEs stating that sustainability actions are a high priority is due to the pandemic hitting SMEs harder than larger firms. Stretched supply chains and rising costs remain ongoing challenges for all businesses but appear to have limited

SMEs' sustainability plans in the short term, adding to challenges faced as a result of more limited resources and funding options than larger firms.

The widest gap in priorities between SMEs and large companies was in investment into low carbon energy consumption (41% of SMEs versus 70% of large firms stated this as a high priority) and supply chain monitoring (32% versus 58%). If, as expected, energy prices and inflation rise this year, this gap may widen further.

SMEs have taken swift action in other areas in the short term to aid their recovery; for example manufacturing and services SMEs have increased hiring staff at a greater rate than large businesses in the same industries, telling us that this recruitment attempts to safeguard against staff shortages and prepares them for a rebound in underlying demand.

SMEs continued to signal substantial price pressures in December. Input costs rose at the second-sharpest rate on record, behind only November's peak, and one that surpassed the average for large companies. Respondents reported higher prices for transportation, raw materials, fuel and utilities alongside greater wage bills.

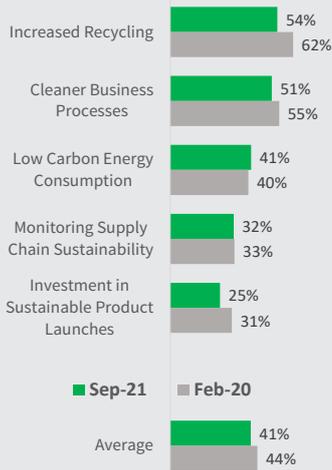
As the UK's largest business bank, to help support SMEs to take advantage of the growth opportunity that lies ahead, we've committed to lending £100 billion of Climate and Sustainable Funding and Financing by the end of 2025. We'll also continue to focus on advice, education, coaching and products that can help SMEs contribute to cutting the UK's carbon emissions by half; we encourage SMEs and business leaders who need support and guidance to go greener, to speak to one of our Relationship Managers or visit natwest.com to discover how we can help.

Andrew Harrison
 Head of Business Banking
 NatWest

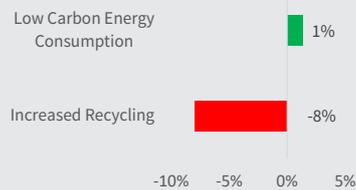
SME Sustainability PMI: Actions in 2022

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

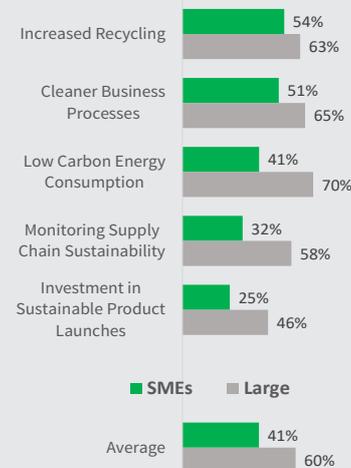
UK SME Sustainability PMI: Actions
Percent reporting 'high priority'



Top changes in percent reporting 'high priority'



SMEs vs. Large Companies (Sep-21)
Percent reporting 'high priority'



Scarring from the pandemic holds back SMEs action on sustainability

In this section of the report we look at the actions on sustainability that UK SMEs are prioritising in 2022, and results are compared against those for large companies.

NatWest Sustainability PMI data suggests that SMEs have reduced their focus on sustainability since the pandemic began.

The latest survey showed that SMEs are generally less likely to prioritise sustainability actions since the onset of the pandemic and subsequent challenging business environment. In September 2021, on average 41% of SMEs stated that sustainability actions were a high priority in the next 12 months, down from 44% in February 2020.

Sector data showed that both manufacturers and service providers downgraded their sustainability plans during the course of the pandemic. The average proportion of SME manufacturing companies stating environmental action as a high priority slipped from 47% in early-2020 to 45% in the latest survey, while for service providers the figure fell from 42% to 37%.

More than half of UK SMEs look to prioritise increased recycling in 2022

Increased recycling remained the top priority for UK SMEs during 2022, with over half highlighting this as a key long-term investment (54%), closely followed by cleaner business processes (51%). However, these figures were down from 62% and 55% respectively at the start of 2020, with efforts to improve recycling seeing the biggest downgrade of all monitored actions.

The proportion of SMEs that felt supply chain monitoring was a high priority over the next year fell only slightly, from 33% in February 2020 to 32% in September 2021. Sustainable product launches were the lowest ranked priority, with just a quarter

of SMEs reporting this as a high priority (down from 31% in February 2020).

The only area to see a slight improvement in investment plans was low carbon energy consumption, where the proportion of SMEs highlighting this as a high priority rose from 40% to 41% during the pandemic.

Large companies much more likely to pursue sustainability goals

When compared to large companies, SMEs have weaker intentions of prioritising sustainability actions in 2022. On average, 60% of large companies believed that actions to improve environmental sustainability were a high priority, compared to 41% of SMEs. The proportion of large firms stating actions on improved sustainability are a high priority was greater in September 2021 than before the pandemic (57%).

As was the case for SMEs, large manufacturers are more likely to pursue sustainability plans than large services companies (63% versus 57%). In contrast to SMEs, however, both sectors saw intentions improve since February 2020.

The widest gap in priorities between SMEs and large companies was concerning investment into low carbon energy consumption (41% of SMEs versus 70% of large firms stated this as a high priority) and supply chain monitoring (32% versus 58%).

The reduced proportion of SMEs stating that sustainability actions are a high priority is likely due to the fact that the pandemic has hit SMEs harder than larger firms, with plans instead orientated towards recovering from the widespread disruption of the pandemic.

Moreover, stretched supply chains and rising costs remain ongoing challenges for firms. Volatile price and supply appears set to limit SMEs' sustainability plans in 2022, adding to challenges faced as a result of more limited resources and funding options than larger firms.

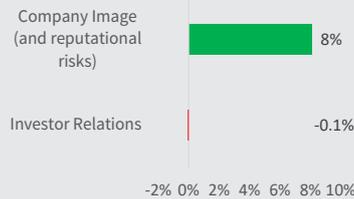
SME Sustainability PMI: Motivations in 2022

To what extent are the reasons below likely to influence your environmental sustainability actions in the next 12 months?

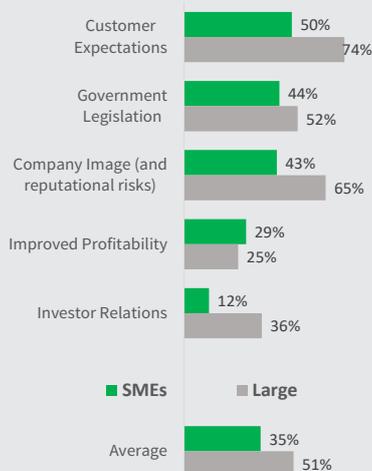
UK SME Sustainability PMI: Motivations
Percent reporting 'large extent'



Top changes in percent reporting 'large extent'



SMEs vs. Large Companies (Sep-21)
Percent reporting 'large extent'



Customer expectations are most likely to influence action on sustainability

This section looks at what has the biggest influence on SMEs' efforts to improve environmental sustainability.

The latest data indicated that overall motivation for prioritising green initiatives has increased over the pandemic, from 33% to 35% of UK SMEs on average. However, this remained lower than reported by large companies (51%).

Customer expectations had the biggest influence on SMEs sustainability actions, with half of all firms stating that this had a large impact on their plans, up from 46% in February 2020.

Government legislation was ranked in second place (44% of firms, up slightly from 43%), closely followed by company image and reputational risks (43%, up from 35%). The latter saw the biggest change in terms of motivation for environmental plans of all categories, underscoring the greater focus on environmental issues and increasing importance of green credentials.

Finally, the lowest ranked influence was investor relations, with only 12% of SMEs indicating that this had a large influence on their actions (unchanged from February 2020).

In contrast, more than one-in-three large companies (36%) cited investor relations as a considerable motivating factor for sustainability action in 2022.

Pressure to act on sustainability plans is greater at SME manufacturers

Both manufacturers and services companies within the SME sector reported increased motivation for action on sustainability compared to before the pandemic.

Motivation to pursue greener initiatives was greater at manufacturers overall, with an average of 39% of firms reporting

strong influences on sustainability plans, compared to 32% of services companies.

While customer expectations ranked as the top influence, the biggest change in motivation for both sectors was for company image and reputation risk. Around 45% of manufacturers and 41% of service providers stated that this had a large impact on their sustainability actions, up from 33% and 36% respectively in February 2020.

Large companies report much greater motivation to pursue environmental sustainability plans

There is still a wide margin between how motivated SMEs are to invest in sustainability actions compared to large companies.

Both SMEs and large firms stated that customer expectations remain the primary influence for action on sustainability. However, the proportion of SMEs that indicated customer expectations had a large influence on their plans was still notably lower than that seen for large firms (50% versus 74%).

Company image and reputational risk was also much more likely to drive environmental sustainability plans at large businesses than SMEs. Around 65% of large companies indicated that this had a large impact on actions, compared to 43% of SMEs.

The proportion of large firms citing investor relations as a big motivation (36%) was also notably higher (12% of SMEs).

Investor relations had the biggest upgrade in influence for larger companies of all five categories (rising from 20% in February 2020), likely due to greater public scrutiny about action on environmental sustainability and the pursuit of green credentials.

SME Recovery PMI[®]: Service Sector

Activity growth lags behind large firms

Services companies with less than 250 employees continued to record output growth at the end of 2021, taking the current stretch of expansion to ten months. However, the upturn was the slowest since August and weaker than among large firms. The respective seasonally adjusted index slipped from 54.8 in November to 53.0 in December.

Survey participants linked the rise in business activity to sustained increases in sales and successful marketing efforts. However, growth was reportedly constrained by the escalation of the pandemic, the reintroduction of restrictions, staff shortages and a lack of raw material availability.

Although new work intakes continued to expand in December, growth lost momentum. The increase was moderate and the weakest since August. Firms attributed the slowdown to heightened consumer uncertainty amid the fast spread of COVID-19.

Expectations of rebound in demand boost job creation

UK SME service providers expect Omicron disruptions to be short-lived, as evidenced by another substantial improvement in hiring activity. The upturn in employment was among the strongest seen in the series history and outpaced that registered among large enterprises. Companies associated job creation with efforts to safeguard against staff shortages, attempts to overcome tight labour market conditions and preparations for a rebound in underlying demand.

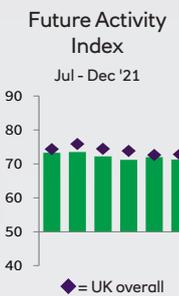
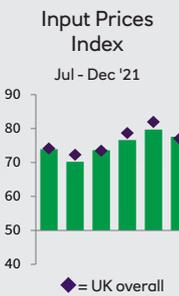
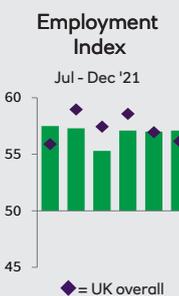
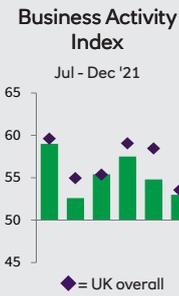
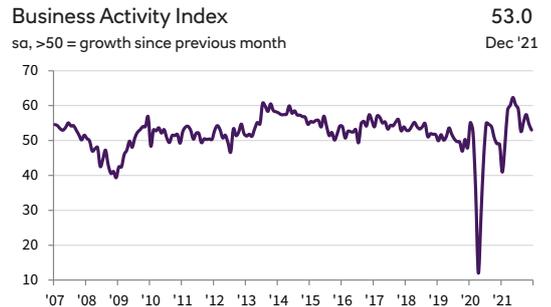
Intense inflationary pressures

Small- and medium-sized firms continued to signal substantial price pressures in December. Input costs rose at the second-sharpest rate on record, behind only November's peak, and one that surpassed the average for large companies. Panellists reported higher prices for transportation, raw materials, fuel and utilities alongside greater wage bills.

December data highlighted an unprecedented upturn in prices charged by small companies, as firms passed on ongoing rises in cost burdens to clients.

Optimism broadly unchanged from pre-Omicron level

SME service providers retained optimistic projections regarding the 12-month outlook for business activity, with the overall level of sentiment in December broadly similar to November. Optimism was pinned on hopes that the pandemic would recede, restoring consumer confidence and enabling the release of pent-up demand.



SME Recovery PMI[®]: Manufacturing Sector

Output growth held back by supply shortages

December data indicated another increase in manufacturing production among SMEs. At 50.8, little-changed from 50.7 in November, the seasonally adjusted Output Index was below its long-run average and consistent with a marginal rate of expansion. The figure was also considerably lower than the all-firm average (53.6).

Panellists indicated that ongoing increases in factory orders supported the upturn in production, but growth was stymied by shortages of staff and raw materials.

Although new orders continued to rise in December, the pace of expansion eased from November and was modest. Several companies stated that the upturn was constrained by subdued client confidence due to the rise in COVID-19 cases and the possibility of tighter restrictions. Many orders had been reportedly placed on hold or cancelled.

Job creation remains strong

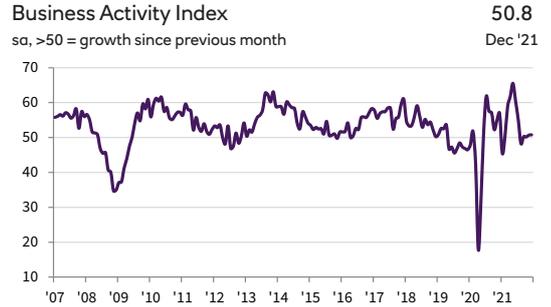
Small- and medium-sized companies signalled a further intensification of capacity pressures in December, which in turn led them to hire extra staff. The rate of job creation was marked, despite softening to a three-month low. Several panellists indicated that hiring activity was curbed by fierce competition for labour and skill shortages, while others found it challenging to retain staff due to more attractive pay and sign-on bonuses elsewhere.

Input cost inflation subsides, but remains elevated

After hitting a near-record high in November, input costs facing manufacturing SMEs rose at a slower rate in December. The increase was nonetheless sharp and among the fastest in the series history, as lingering supply-chain constraints and shortages continued to exert upward pressure on cost burdens. Higher energy, labour, raw material and transportation costs were reported. Similarly, charges increased at a substantial, albeit slower, pace. Rates of both input cost and output charge inflation were below the trends for large firms.

Optimism strengthens despite spike in COVID-19 cases

Companies revised up their assessments for output growth in the year ahead. Upbeat projections stemmed from predictions of reduced travel restrictions, new product launches, investment and demand resilience. However, the overall level of positive sentiment trailed behind large firms.



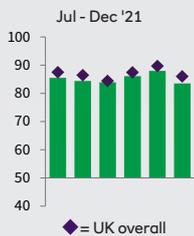
Business Activity Index



Employment Index



Input Prices Index



Future Activity Index



SME Recovery PMI[®]: Construction Sector

Construction activity rises at softer rate at year end

Small- and medium-sized UK construction firms signalled ongoing growth of output during December, but the rate of expansion softened. The Business Activity Index was down from 53.9 in November to 52.1, its lowest mark since September. Still, the latest reading took the current sequence of uninterrupted increases in output to 11 months.

Survey participants suggested that robust demand for construction work continued to boost activity. However, the postponement of on-site work, the pandemic and a lack of raw material availability curtailed growth.

Large construction companies continued to outperform their SME counterparts, despite also seeing a slowdown in growth at the end of 2021.

Employment increases at slowest rate in ten months in December

Construction companies with less than 250 employees continued to take on additional staff at the end of the year, stretching the current run of expansion to 11 months. That said, after reaching a record high in second quarter, the rate of job creation slowed throughout most of the second half of the year, down to the weakest in ten months in December.

Anecdotal evidence linked job creation to robust demand for construction work, although many firms reported difficulty retaining staff.

Slowest rise in cost burdens for nine months

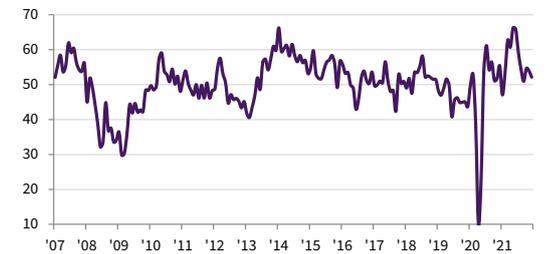
Small- and medium-sized UK constructors signalled a substantial upturn in input prices, but the rate of inflation softened to the weakest since March and was below that seen for large companies.

Inflationary pressures reportedly stemmed from supply-chain disruptions and associated raw material scarcity. Firms also mentioned increased prices for energy and fuel.

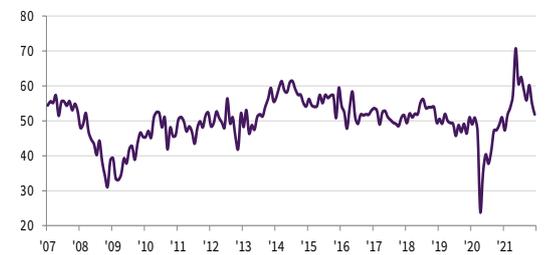
Business confidence ticks higher

SME constructors became increasingly optimistic towards growth prospects, with the overall level of positive sentiment strengthening to a three-month high in December. Companies foresee an improvement in economic conditions leading to a pick-up in demand. Some stated that they have projects due to commence, while others are waiting for planning permissions to be issued. Restructuring and marketing efforts were also seen as opportunities to the outlook.

Business Activity Index
sa, >50 = growth since previous month
52.1
Dec '21



Employment Index
sa, >50 = growth since previous month
51.9
Dec '21



Input Prices Index
sa, >50 = inflation since previous month
80.6
Dec '21



Future Activity Index
>50 = growth expected over next 12 months
70.9
Dec '21



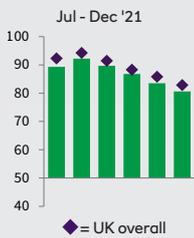
Business Activity Index
Jul - Dec '21



Employment Index
Jul - Dec '21



Input Prices Index
Jul - Dec '21



Future Activity Index
Jul - Dec '21



About the NatWest Sustainable Business Tracker

The NatWest Sustainable Business Tracker is a new 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 IHS Markit's monthly UK Purchasing Managers' Index[®] (PMI[®]) surveys.

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

SME Recovery PMI[®] survey responses are collected by IHS Markit 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 Recovery 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, suppliers' delivery times and future activity.

The SME Recovery PMI[®] data for December were collected 06 – 22 December 2021. 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 will be compiled on a quarterly basis in 2022. The SME Recovery PMI[®] data will be compiled on a monthly basis.

The latest SME Sustainability PMI data were collected in September 2021 and February 2020, to capture intentions both before and after the onset of the pandemic. In each survey, companies are asked what sustainability plans they are looking to prioritise over the next year, and the results are compared against those seen for large companies. The survey also monitors how SMEs are motivated to act on sustainability.

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

Index summary

NatWest SME Recovery PMI® data (All-Sector)

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

	Activity	New Business	Suppliers' Delivery Times	Future Activity*	Employment	Outstanding Business	Input Prices	Prices Charged
Jul '21	58.5	56.9	20.5	73.2	57.9	55.2	76.9	60.9
Aug '21	52.2	52.2	20.1	73.9	57.8	52.3	74.2	60.0
Sep '21	54.3	54.0	19.8	72.9	55.1	52.1	76.5	61.3
Oct '21	56.2	54.9	21.1	71.9	57.2	52.3	78.8	62.3
Nov '21	54.1	54.4	23.4	72.0	56.7	52.4	81.2	63.2
Dec '21	52.6	52.0	29.4	71.9	56.5	52.4	78.7	63.7

NatWest SME Recovery PMI® data (by sector)

	All-Sector Business Activity	Service Sector Business Activity	Manufacturing Business Activity	Construction Business Activity
Jul '21	58.5	59.0	55.1	59.2
Aug '21	52.2	52.6	48.3	54.4
Sep '21	54.3	55.4	50.2	50.9
Oct '21	56.2	57.5	50.2	54.6
Nov '21	54.1	54.8	50.7	53.9
Dec '21	52.6	53.0	50.8	52.1

Contact

Laura Blumenthal
Media Relations Manager
NatWest
+ 44 (0)7947974464
laura.blumenthal@natwest.com

Annabel Fiddes
Economics Associate Director
IHS Markit
+44 1491 461 010
annabel.fiddes@ihsmarkit.com

Joanna Vickers
Corporate Communications
IHS Markit
+44 207 260 2234
joanna.vickers@ihsmarkit.com

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 IHS Markit

IHS Markit (NYSE: INFO) is a world leader in critical information, analytics and solutions for the major industries and markets that drive economies worldwide. The company delivers next-generation information, analytics and solutions to customers in business, finance and government, improving their operational efficiency and providing deep insights that lead to well-informed, confident decisions. IHS Markit has more than 50,000 business and government customers, including 80 percent of the Fortune Global 500 and the world's leading financial institutions.

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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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