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Trend report:

Looking beyond the pandemic, what does recovery look like for UK SMEs?

Paragon Bank's report outlines six key trends that are impacting SMEs as they emerge from the Covid-19 pandemic



Business owners are in a good position to overcome obstacles and are utilising this period to transform and innovate, while focusing on boosting cashflow and maintaining cash reserves.



An introductory note from John Phillipou

Over the course of the last 18 months, UK SMEs have demonstrated incredible resilience and agility in the face of one of the biggest global crises of a generation.

At Paragon, we saw multiple examples of this through our own customer base – we witnessed businesses innovating at a staggering pace, taking their businesses in new directions nearly overnight, expanding into brand new sales channels and targeting new customer groups. The creativity and flexibility demonstrated by so many UK SMEs throughout this pandemic has been nothing short of astounding.

We wanted to gauge how business owners' outlooks for the future had evolved as we started to emerge from the third national lockdown and saw restrictions lifted. For some businesses and industries, this marked the first time they were able to operate at 'normal' capacity since the start of the pandemic.

To get the full picture, we conducted a large scale survey of 1,000 SMEs across the UK, covering a variety of industries. This was a follow-up to an initial survey we conducted in September 2020.

It was really pleasing to see a resounding sense of optimism across the SME landscape, with 92% of SMEs reporting a positive outlook. More than half also reported they were back to, or exceeding, pre-pandemic turnover levels.

Many factors have contributed to this rapid pace of recovery.

Firstly, it's clear that business support, from the Government, financial providers, trade associations and other groups, has been invaluable in helping businesses keep their head above the water during such a difficult economic crisis.

The financial Government support has been a lifeline for UK businesses, and we've seen a strong take-up of initiatives, such as the furlough scheme, across the board. UK businesses are also thinking about how they can use the Recovery Loan Scheme to power their long-term recovery, which is encouraging to see. Indeed, 35% of businesses reported that they had already used the scheme or were thinking of doing so, only seven weeks after launch.

We are also seeing businesses continue to demonstrate the skills and agility that gave them such an edge throughout the pandemic. UK SMEs are recognising the importance of innovation in keeping the momentum of their recovery and are prioritising this and putting money behind it, with the majority of businesses boosting their innovation budget post-pandemic. This focus on innovation is taking lots of different forms, from investment into IT infrastructure and expanding ranges and product lines, to marketing innovation or implementing flexible working models and more staff benefits.

The biggest challenge UK businesses will face in the upcoming months will be maintaining the pace of this recovery. However, it looks like business owners are in a good position to overcome obstacles and are utilising this period to transform and innovate, while focusing on boosting cashflow and maintaining cash reserves.

It is still difficult to predict exactly what the future holds for UK SMEs and there are still uncertain times ahead as we move towards Autumn. But it certainly looks like UK businesses are in good stead to weather any storms ahead.



John Phillipou
Managing Director
Paragon Bank SME Lending



Research summary

We conducted a survey of more than 1,000 UK SMEs, across a variety of different sectors including construction, manufacturing, agriculture and professional services, in order to paint a picture of the key trends driving post-pandemic recovery.

One of the most notable and positive findings of the survey was that despite a tumultuous 18 months, **UK SMEs are bouncing back at a very encouraging pace.** More than half (54%) of UK SMEs have recovered turnover in line with, or exceeding, pre-COVID performance, while more than nine in ten (92%) predicting positive business outcomes post pandemic.

It was clear from the results that SMEs have made great progress since our initial survey in September 2020 and are feeling very positive about the future. Our first SME survey was conducted between the first and second national lockdown, when many UK businesses were facing a very uncertain future, with a number of industries still not able to trade at normal capacity.

In that initial September survey, we saw **66%** of businesses report a negative impact on turnover, and **42%** of SME owners predicted that their business would struggle and couldn't predict a timeline around recovery – it's therefore very positive to see **84% of SMEs either fully recovered or on the verge of recovery.**

Delivering growth plans and managing cashflow top priorities for SMEs

The survey revealed businesses' biggest priorities as they continue to plan for their recovery.

UK SMEs named two leading priorities – the first was creating and delivering **growth plans**, which was a priority for 61% of SME owners over the next 6 months, and in close second, **managing cashflow** – a focus for 60%.

This highlighted that **cashflow** still remains a key focus for UK businesses, with **58% of SMEs impacted by this issue.**

Despite positive signs of recovery, a portion of UK SMEs (39%) **remain uncomfortable with their cash reserves.**

It is therefore no surprise that SMEs are keen to use **Government schemes** to boost cashflow. Indeed, this was the most popular reason listed by SMEs to use the Government-backed **Recovery Loan Scheme**, with more than half of businesses who have already utilised the scheme using it for that purpose.

UK SMEs happy with Government support during the pandemic

Our research highlighted that the majority of UK SMEs were happy with the business support provided by the Government throughout the pandemic.

Overall, the level of satisfaction increased by **15%** since SMEs were last surveyed in September – and 44% of SMEs considered the Government as their **main source of business support.** It looks like the Government's sustained support of UK SMEs between September and May, which included the introduction of the Recovery Loan Scheme in April to help power recovery, will likely have been key influencing factors in this increase. The extension of various initiatives including the furlough scheme, which was utilised by close to half (44%) of SMEs, will have also been a decisive influence on sentiment towards Government support.

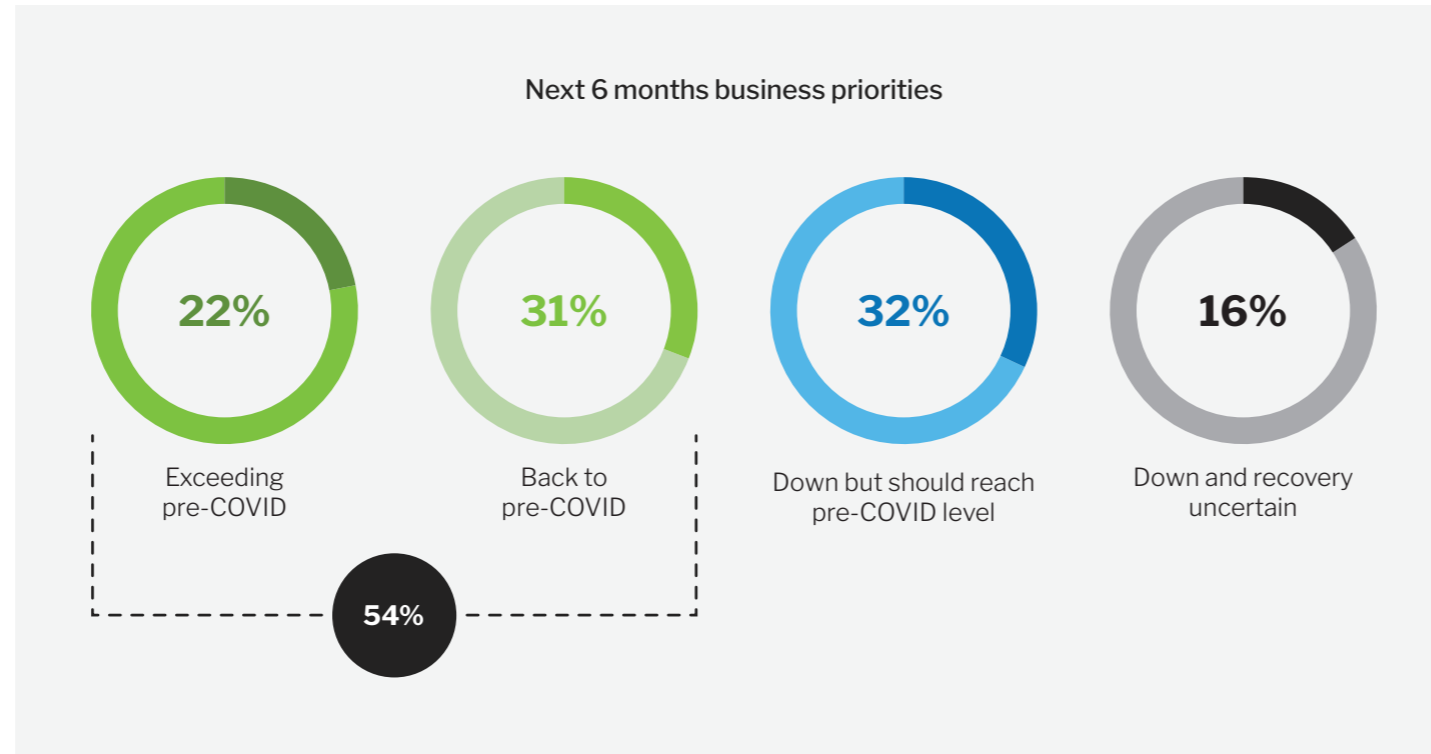
Trend
#1

24%
of SMEs predicted their business will be stronger post-pandemic than it was before COVID-19



Most UK SMEs are bouncing back at a rapid pace

The majority of UK SMEs are already seeing strong signs of recovery as we emerge from the Covid-19 pandemic.



More than one in six SMEs (22%) are seeing their turnover levels exceed pre-Covid levels, while another 31% reported being back to pre-COVID levels. Amongst the 48% of SMEs still working to get back to their pre-COVID turnover figures, 32% said they anticipated they would reach pre-COVID levels soon. Only 16% faced an uncertain path to recovery.

Smaller businesses seem to have bounced back the quickest with 64% reporting turnover to have recovered or exceeded pre-pandemic levels, compared to just 47% of firms with 100-249 employees

Turnover recovery is most visible amongst SMEs in **East Midlands and London**, with 67% and 63% respectively indicating that turnover is in line or above pre-COVID

These results are in stark contrast to the initial survey we carried out in September 2020 between the first and second lockdown, where 66% of businesses reported a negative impact on turnover in September 2020. In the first SME survey, 42% of SME owners predicted that their business would struggle and would recover to pre-pandemic levels 'eventually' – it's therefore very positive to see 84% of businesses either recovering or on the verge of recovery.

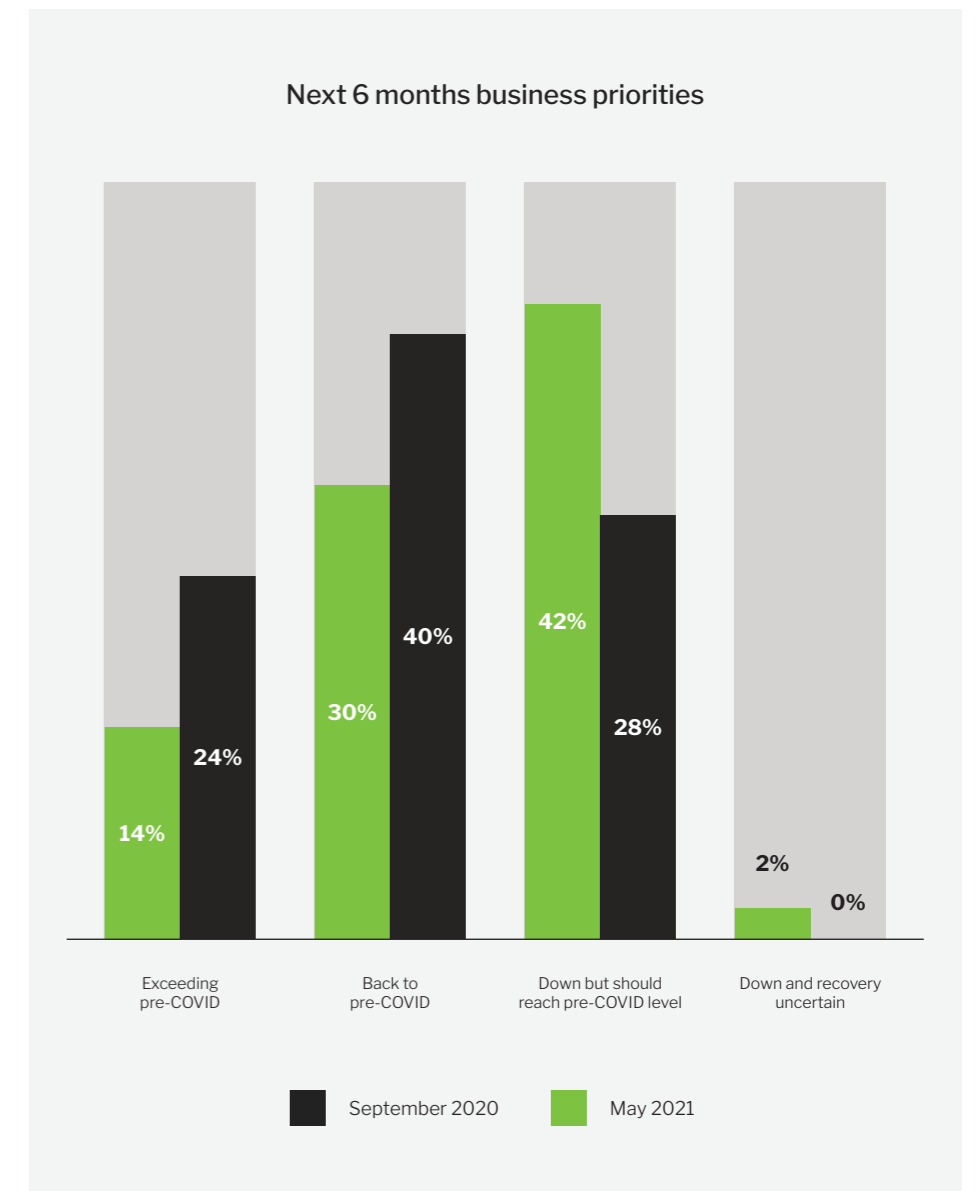
Optimistic outlook is on an upward trajectory

Amongst UK SMEs, 92% reported a positive outlook in May 2021, compared to 86% in September 2020.

Amongst those, 24% predicted that their business will be stronger than ever, compared to only 14% in September 2020. Another 40% said they would likely remain as strong as they were pre-Covid, compared to 30% in September 2020.

Those in the **agriculture industry** hold most optimism with 81% believing they will be stronger than before and 13% believing they will be as strong as before.

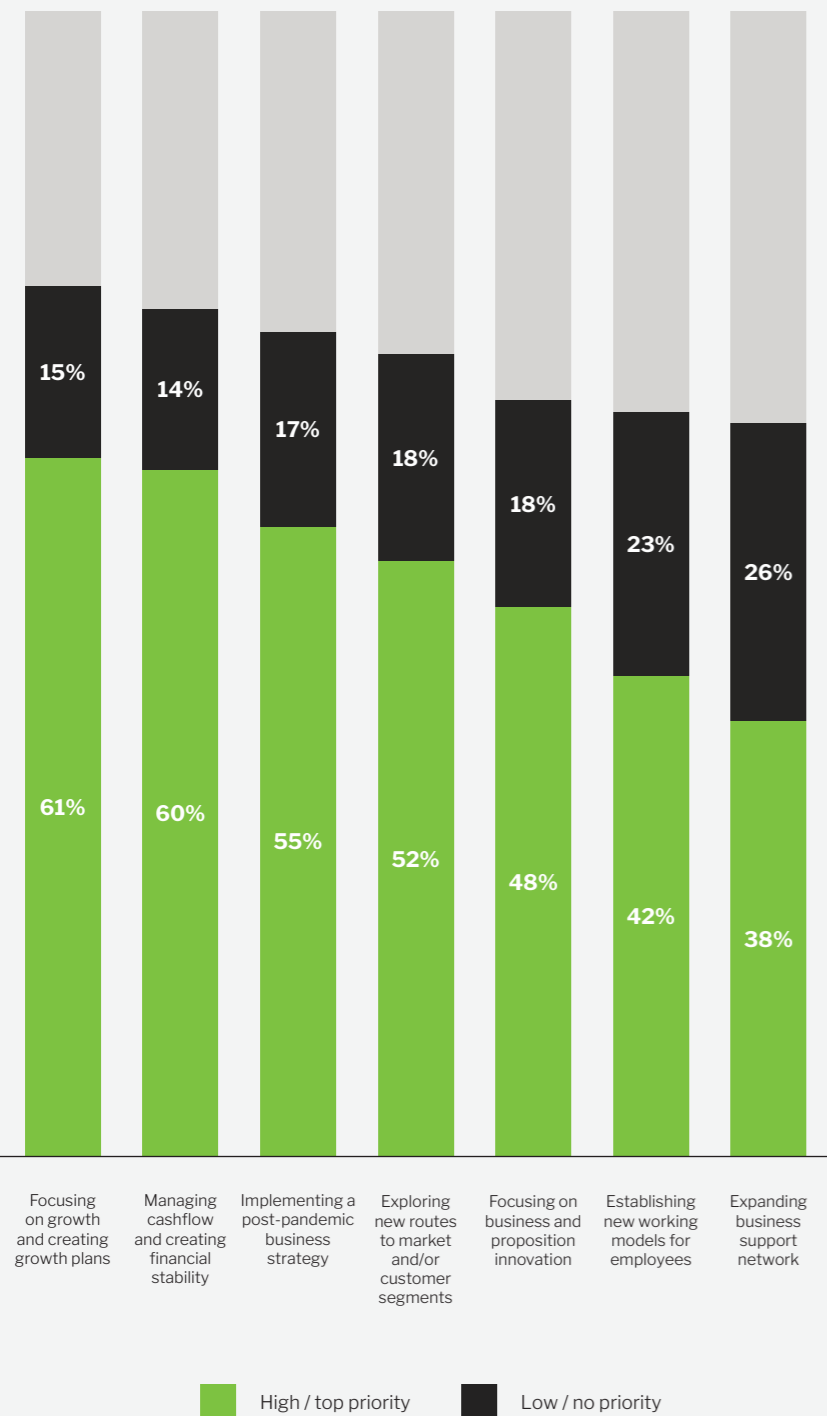
This positive outlook is also stronger amongst SMEs based in East Midlands, Scotland and London (79%, 76% and 70% respectively indicated that they will be as strong or even stronger than before vs 64% cross UK average)



Growth and stability are top priorities for UK SMEs

We asked UK SMEs to outline their top priorities as they plan for their recovery and found that growth and stability are the leading priorities for most.

Next 6 months business priorities



Trend #2



The biggest priority for SME owners was focusing on creating and delivering **growth plans** – this was a top priority for 61% of SME owners over the next 6 months.

In close second, **managing cashflow** was another key priority for six out of ten SME business owners.

Implementing a **post-pandemic business strategy** and exploring **new routes to market** were also key for more than half of SMEs, with 58% and 52% listing this as a priority respectively.

Expanding their business support network is the lowest priority at this stage, with only 38% of businesses prioritising and 26% saying it is low or not a priority at all.

The Midlands bucking the trend for post-Covid recovery

- The **West Midlands** is the only region where **growth** and **stability** don't top the priority list, instead the focus is on new routes to market and customer segments (a priority for 60% of SMEs in the West Midlands)
- Emphasis on **innovation** is also more apparent amongst businesses based in the Midlands, with 63% indicating this is high/top priority vs a national average of 48%
- Focus on **growth** as key priority rises above 70% for SMEs incorporated over 25 years ago and based in Northern Ireland (75%), North East (76%) and East Midlands (75%)
- Focus on **cashflow** is also stronger amongst SMEs based in **East Midlands, East of England and Northern Ireland** (71%, 71% and 75% respectively)



Implementing a post-pandemic business strategy and exploring new routes to market were also key for more than half of SMEs

SMEs are boosting their innovation budgets to drive their recovery

Innovation is a vital driver of post-COVID recovery for UK SMEs at both business and industry level.

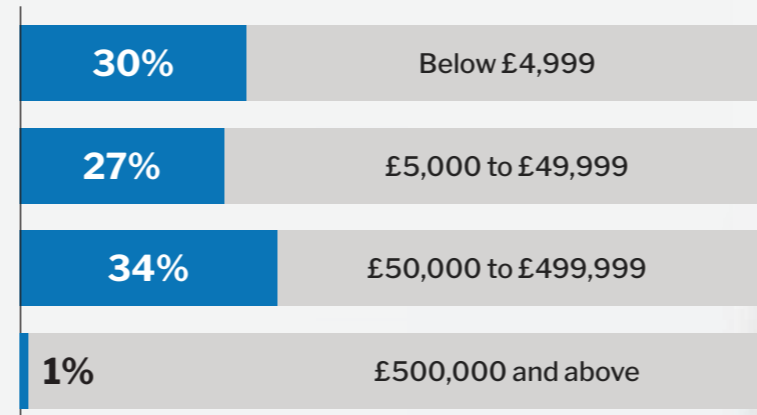
Eight in ten (79%) of SME owners think that **industry innovation** will be a key factor in powering post-COVID recovery, while 77% of SME owners deem this to be important for their own business

recovery. This focus is reflected in the amount of budget SME owners are assigning to innovation, with 61% of SME owners increasing their innovation budget post-COVID.

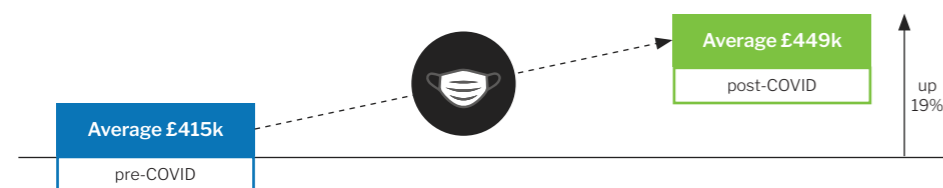
Prior to the pandemic, the average innovation budget was **£415,000** – this has risen by nearly a fifth to **£494,000**.

The majority of SMEs reported budgets of £50,000 or less. However, some respondents reported very high figures (over £10 million), which generated the overall average of £415,000.

Pre-pandemic innovation budget



Average £415k



Four innovation pillars

There is a fairly evenly spread distribution of budget across four key innovation pillars



Process innovation – a priority for 39% of SMEs

- Increasing efficiency through IT infrastructure was the leading priority for this innovation pillar, a focus for 61% of SMEs prioritising process innovation
- IT security was close second and was important for 60% of business owners within that group



Proposition innovation – a priority for 36% of SMEs

- Nearly three quarters (73%) of those prioritising proposition innovation are planning on introducing brand new product lines or services during the pandemic, while two thirds (67%) expanded existing product lines or services



Organisational innovation – a priority for 35% of SMEs

- Flexible working was the leading priority for those SMEs focused on organisational innovation, with 47% assigning budget to implementing a flexible working model
- Companies were also investing heavily into learning and development and employee wellbeing (40%)
- One in three also considered the planet and focused on implementing environmentally sustainable or amending processes to reduce emissions



Marketing innovation – a priority for 34% of SMEs

- More than 50% of SMEs prioritising marketing innovations were looking at expanding customer communication channels, targeting new audiences or creating/upgrading their website

Cashflow was the biggest concern for SMEs during the pandemic – and remains a focus during recovery

The majority of UK SMEs experienced cashflow issues during the pandemic, with 58% impacted by this.

Unsurprisingly, cashflow issues were most common amongst sectors that had to either shut down completely or reduce activity during lockdown, including **Accommodation, Food Services & Recreation (66%), Construction (66%), and Retail industries (66%).**

Cashflow issues have also been a particular problem for newer businesses in operation for less than 5 years (76%), those with a large turnover of £25m+ (73%), or SMEs based in North East (71%)

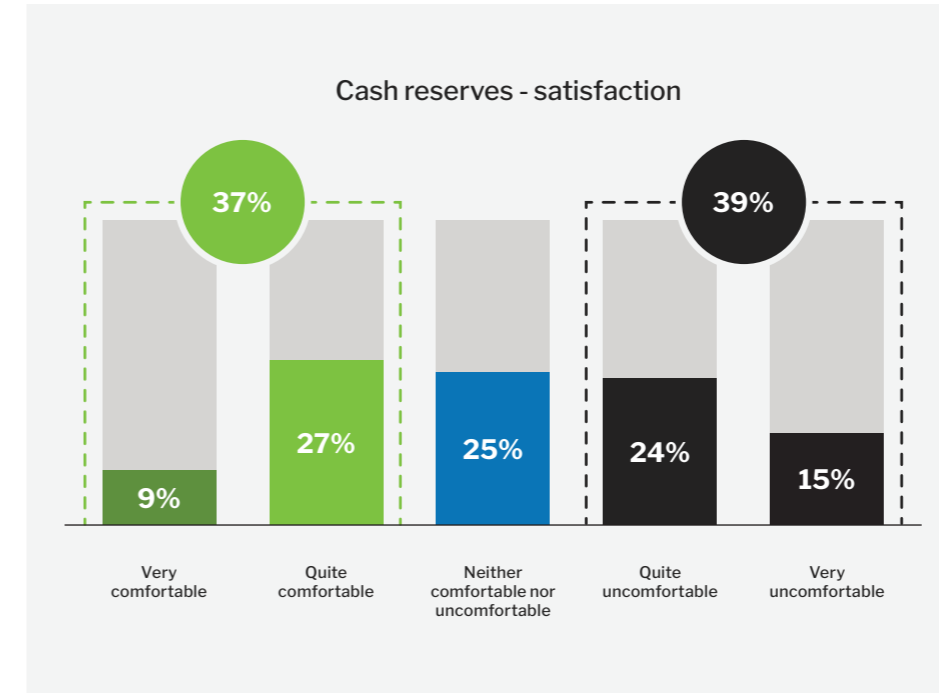
There was a wide range of contributing factors to those issues, with **loss of profit** the leading reason in 53% of cases. **Late payments from clients** was the second most common reason for cashflow disruption, impacting 34% of SMEs.



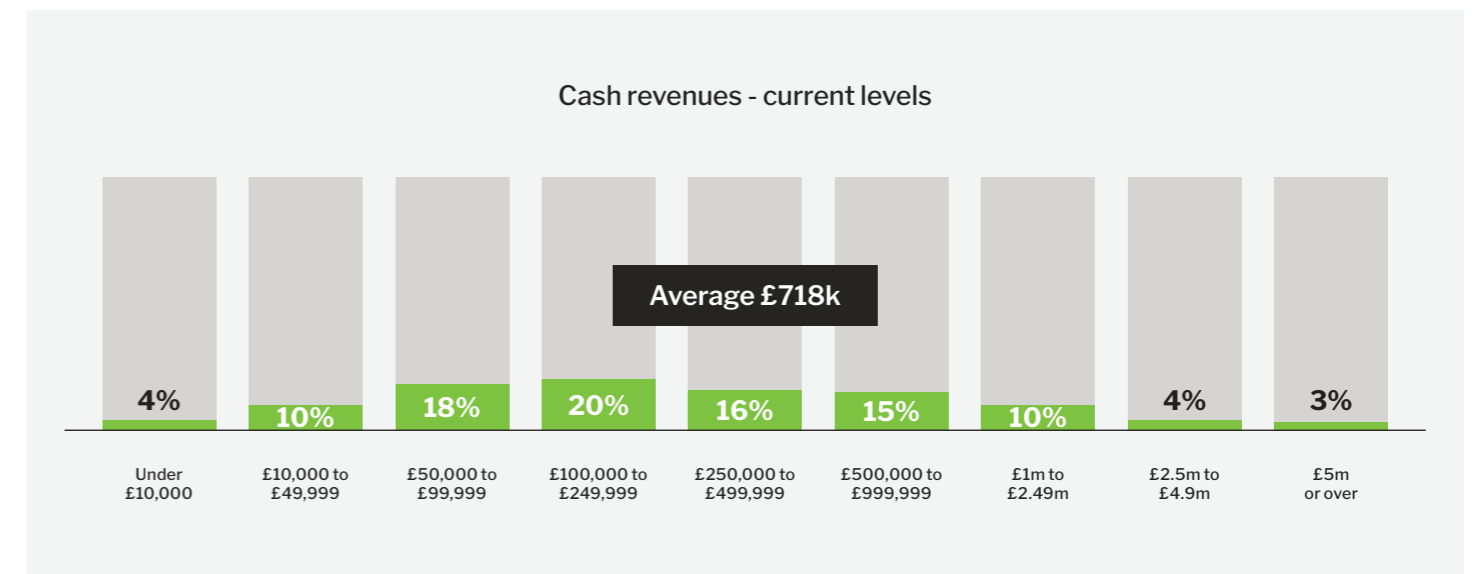
Four in ten SMEs still uncomfortable with cash reserves

Close to 40% of SME owners say they aren't comfortable with the amount of cash reserves currently held by their business.

However, there is a fairly even split amongst SMEs, as a similar proportion of business owners feel comfortable with the amount of money they have in the bank.



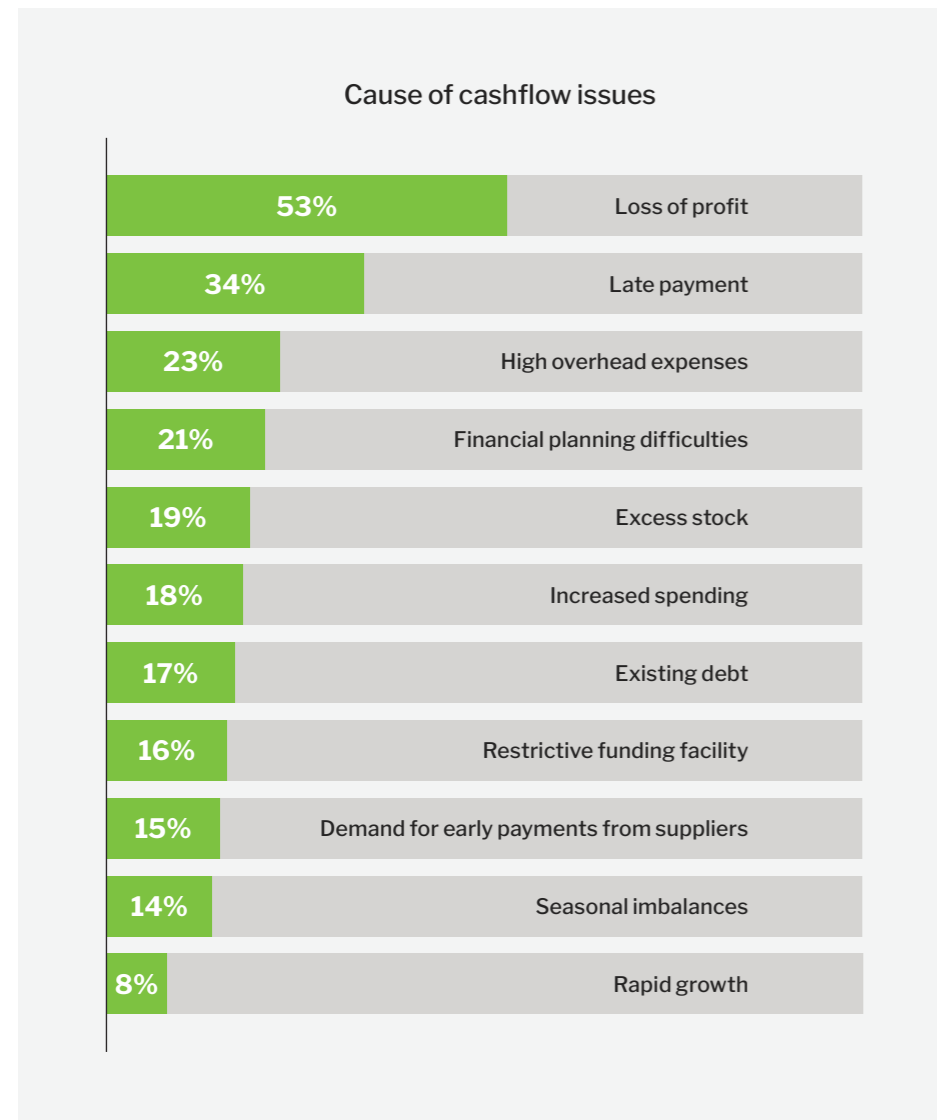
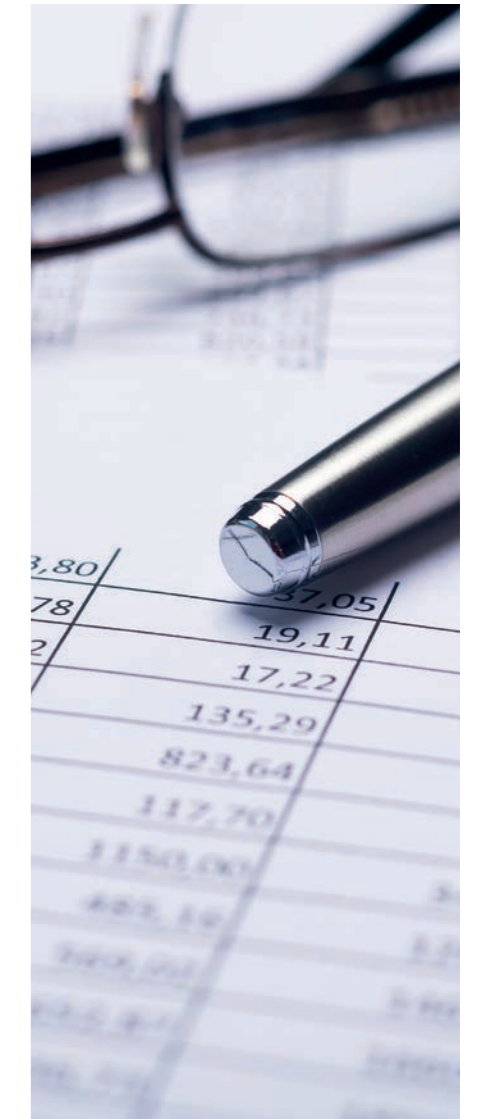
On average, SMEs hold £718,000 of cash reserves in total. Those uncomfortable with their cash reserves have 30% lower buffer than those who feel comfortable.



SMEs that felt very or quite comfortable with their cash reserve levels held an average of £955,000 in cash, while those that felt very or quite uncomfortable held an average of £683,000.

SMEs in **accommodation** and **agriculture** feel the most uncomfortable with their current levels (51% and 78% respectively). The average amount of cash reserves in the

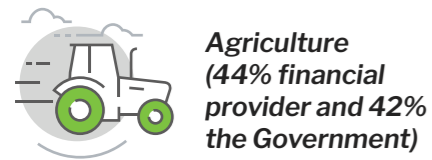
accommodation industry was £596,000 (38% lower than average), while the average for agriculture was £658,000 (31% lower than average).



Government support has been vital in powering SMEs forward

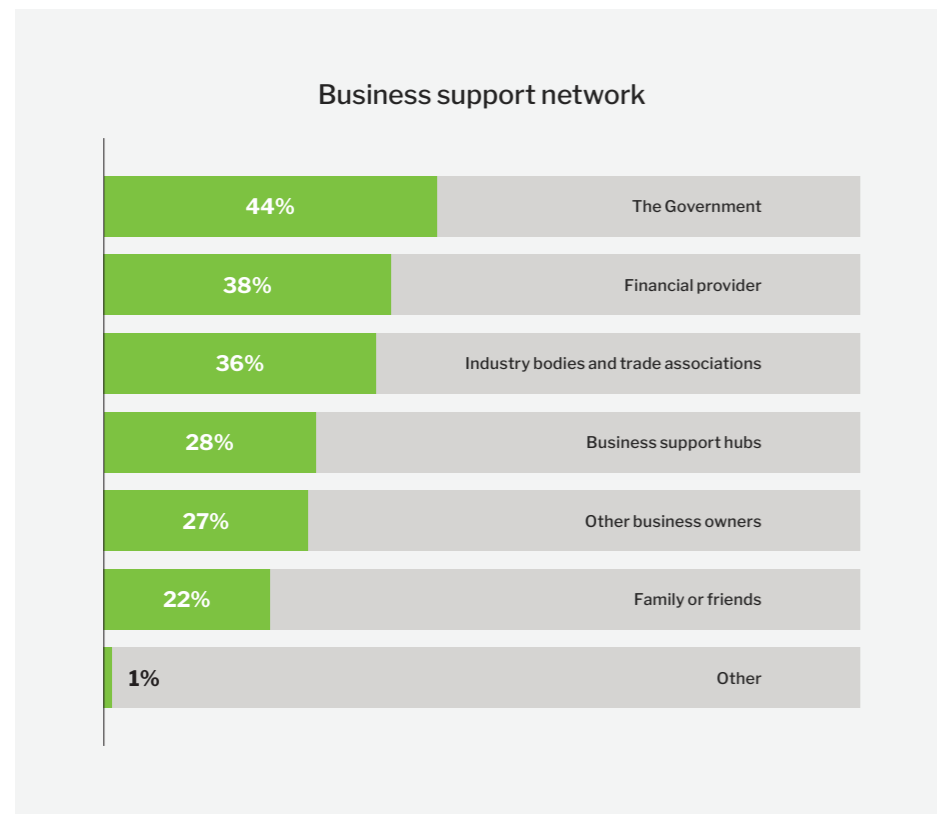
Government support has played an invaluable part in supporting SMEs during the pandemic – this is reflected in the fact 44% of SMEs see the Government as their main source of business support.

Financial providers and industry bodies/trade associations also played a key part in supporting SMEs and were named as a main source of support by 38% and 36% respectively. **Agriculture and construction** are two industries that bucked the trend, where SMEs relied more commonly on their financial providers than the Government:



Even during the pandemic, where many business support events and networking opportunities were put on hold or went digital-only, there is still a heavy reliance from SMEs on business support hubs and networks. This shows the importance of collaboration within the industry.

However, more than one in five SMEs (22%) still rely on family and friends for business support, while 1% included mentions under 'other' such as "fellow directors and senior staff" or "myself / stand-alone", which shows that there is still a portion of SME owners not utilising resources available to help aid their recovery.

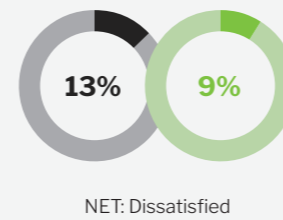
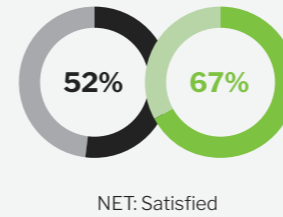


Trend #5



More than two thirds approve of Government support available

Satisfaction with Government support



September 2020 (N=250)
May 2021 (N=1,000)

Amongst SMEs, 67% confirmed that they were pleased with the amount of Government support available to UK businesses during the pandemic.

The level of satisfaction has increased by 15% since SMEs were last surveyed in September 2020, with factors such as the introduction of the Recovery Loan Scheme and the extension of various initiatives including the furlough scheme likely to be key influencing factors in this increase.

SMEs' satisfaction with the Government support rose to 73% amongst **smaller SMEs** (below 50 employees) and to 93% for SMEs in Agriculture.

Further support required by SMEs included clarification on the various ways businesses can be supported (29%), the provision of an easier application process (28%) and a relaxation of the lending criteria (21%). However, nearly one in three (32%) believe the Government has

Take-up of different Government support schemes

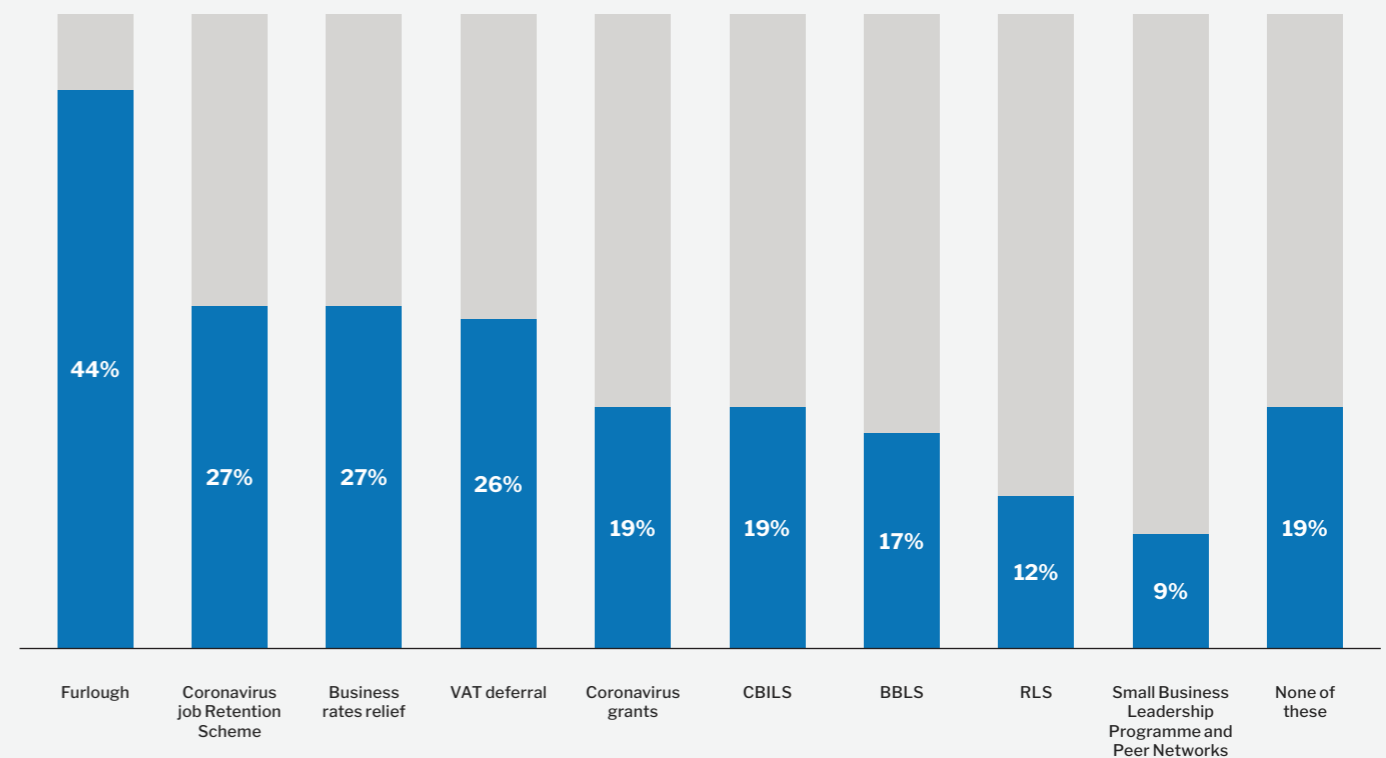
done enough and it can't do much more to help them.

The most commonly used Government support was by far the furlough scheme. This was used by more than four in ten SMEs (44%).

This was followed by the Coronavirus Job Retention scheme and Business Rates Scheme (both 27%).

Nearly one in five SMEs (18%) opted to use no support at all, while the Coronavirus Business Interruption Loan Scheme (CBILS) and Bounce Back Loan Scheme (BBLs) were used by 19% and 17% respectively.

Most used Government support schemes



The Recovery Loan Scheme

Launched in early April, The **Recovery Loan Scheme (RLS)** is designed to support access to finance for UK businesses as they grow and recover from the disruption of the COVID-19 pandemic.

Amongst UK SMEs, 12% had already used the Recovery Loan Scheme (RLS) within seven weeks of the scheme launching, with a further 23% confirming that they are either 'quite likely' or 'very likely' to use the scheme in future.

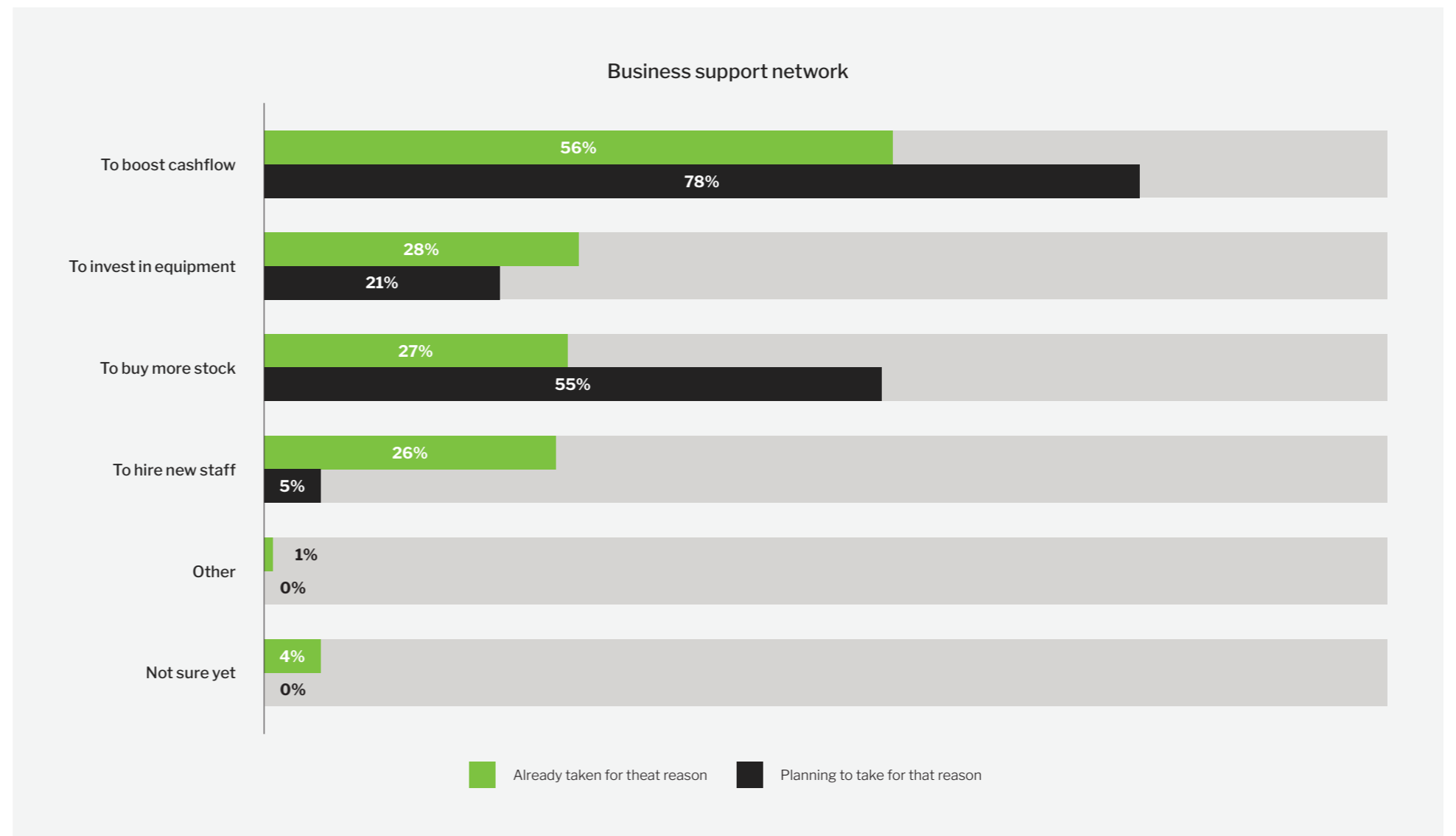


More than half of business owners planning to use RLS in the future

The most common reason for applying to use the scheme already was to **boost cashflow**, with 56% of SMEs using the scheme for this purpose. With cashflow named as the most common issue faced by SMEs during the pandemic, and money reserves still a concern for many business owners, it is expected that this would be the leading reason SMEs sought to use the scheme. Amongst SMEs planning to use RLS in future, cashflow was an even more dominant trend, which reflects that business owners anticipate this will continue to be a key focus in the upcoming months as we emerge from the pandemic.

The second leading reason was to **invest in equipment and assets**, with 28% of SMEs using the scheme to do this. The majority of those who used or will use RLS to buy new asset are investing in IT hardware and software, predominantly to enable or improve remote working.

More than half of business owners planning to use RLS in the future planned to **buy more stock**, which correlates to a high proportion of businesses innovating at a rapid pace in order to fuel their post-COVID recovery by expanding existing product lines or introducing new ones.



The Agricultural sector is flying the flag for post-COVID recovery

The agricultural industry is bouncing back from the Covid-19 pandemic quicker than any other sector surveyed.

SME owners within agriculture hold the most optimism, with 94% of business owners believing they will be stronger than before the pandemic.

A key driver of this positive outlook, which is considerably above the UK average, has been in the way the COVID-19 pandemic has impacted

the farming industry. This has been unique in comparison to many other sectors.

Whereas most SMEs struggled with lockdowns and saw activity grind to a halt, agricultural businesses often saw a significant boost in food supply demand. This was further driven by an increasing consumer focus on the 'farm to fork' journey and on food provenance.

There was a range of ways in which the agricultural sector stood out in terms of its post-COVID recovery:

- **SMEs in Agriculture show stronger recovery and are more optimistic about the future**, with 96% of SMEs in the industry reported turnover in line or exceeding pre-pandemic level vs only 54% on average. Post-COVID positive outlook was also resoundingly high within across the sector, reported at 94% against an average of 65%
- They were also **8% less likely** to experience **cashflow issues** during the pandemic compared to other industries. Those who did indicated excess stock as a main contributor to this, opposed to loss of profit
- When reaching out for **business support**, business owners in farming rely more on business hubs and their financial provider than the Government, whereas across other industries, the Government is at present the main source of support.
- The appetite for the **Recovery Loan Scheme** is stronger than average in the agricultural sector – one in three (31%) have already used the scheme and 20% are likely to use it in the future (versus an average of 12% and 23% respectively)
- Whereas **growth** (61%) and **financial stability** (60%) dominated short-term plans for all, **SMEs in Agriculture** did not indicate any major priorities and had an even spread across all.
- **Innovation** post COVID is undeniably important for Agriculture, both on industry (94% vs 79% average) and business level (93% vs 77%) and this commitment can be seen with **90% increasing their innovation budget**.
- However, the innovation budget in the industry is considerably smaller than average, growing from ££77,686 pre-pandemic to £100,324.



85%
felt that
government
support could
have stretched
further

Agricultural businesses call for more Government support

Of course, the sector was not immune to challenges, including labour shortage, transport and logistics disruptions, equipment shortages, manufacturing delays and shifts in consumer demand, to name a few.

Despite the rapid pace of recovery, SMEs within the agricultural sector had lower cash reserves than the cross-industry average, holding around £658,000 against an average of £718,000. They were also one of the sectors most likely to report being dissatisfied with their levels of cash reserves.

Farming SMEs were also the industry most likely to use a Government support scheme, with 99% of the industry using at least one scheme (against an average of 82%) – however 85% felt that Government support could have stretched further.

More than four in ten businesses (41%) surveyed would have liked to see further educational and non-financial support from the Government around issues such as managing the aftermath of Brexit. This is against cross-industry average of just 17%.

What further support or changes to the current approach would you like to see from the Government?

	Total	Agriculture, Forestry & Fishing
Base: all respondents	1000	101
N/A - I don't think the government can do much more	32%	15%
More clarity on current support available	29%	32%
Easier application process	28%	39%
Relaxation of lending criteria	21%	35%
Increase of loan limits	17%	30%
Further educational and non-financial support	17%	41%
Other	2%	2%





How agriculture is bucking the trend




	All	Agriculture
Average turnover	£8.8m	£20m
Turnover back to or exceeding pre-pandemic level	54%	96%
% of SMEs that experienced cashflow issues during pandemic	66%	58%
Main contributors to cashflow issues	Loss of profit (53%) Late payment (34%)	Excess stock (34%) Late payment (30%)
% of SMEs that are comfortable with cash reserves	37%	17%
AVG to Average	£718,000	£658
% of SMEs that want more financial Government support	47%	80%
% of SMEs that want more non-financial Government support	31%	77%
Top sources of business support	1. The Government (44%)	1. Business support hubs (44%)
	2. Financial provider (38%)	2. Financial provider (44%)
	3. Business support hubs (36%)	3. The Government (42%)
% of SMEs that have already used RLS	12%	31%
% of SMEs likely to use RLS in the future	23%	20%
% of SMEs satisfied with Government support	67%	93%
6-months top priorities	Growth	29%
	Financial stability	29%
Post-COVID positive outlook	64%	94%
% of SMEs that think industry innovation is important	79%	94%
% of SMEs that think business innovation is important	77%	93%
Innovation budget	£414,715	£77,686
% of SMEs that saw their innovation budget increase	61%	90%




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