

# **FSB Wales' response Economy, Trade and Rural Affairs Committee inquiry**

**Cost of Living**

**May 2022**

## About FSB Wales

FSB Wales is the authoritative voice of businesses in Wales. It campaigns for a better social, political, and economic environment in which to work and do business.

With a strong grassroots structure, a Wales Policy Unit and dedicated Welsh staff to deal with Welsh institutions, media and politicians, FSB Wales makes its members' voices heard at the heart of the decision-making process.

FSB Wales welcomes the opportunity to respond on the current cost of living crisis, and would urge that the committee take into account that a cost of living crisis is also a cost of business crisis. Given that many SMEs remain vulnerable following the Covid-19 pandemic, it is vital that we develop an economic strategic vision and ensure that all governments ensure that a post-Covid recovery is not thwarted at this critical time.

- **What are the likely economic impacts of the cost of living crunch?**
- **How are cost of living challenges impacting upon businesses and economic sectors, and how are businesses responding to these?**

SMEs form the overwhelming bulk of businesses in Wales. They are grounded and embedded in our communities and provide vital services and amenities, as well as jobs and prosperity. They form the foundation for local economic development and create value within our communities. It is vital that policy is shaped to respond to the current challenges in a way that places them at the centre of economic development.

April was a particularly difficult month for small businesses, as a host of costs kicked in:

- 100% business rates relief for retail, leisure and hospitality has been reduced to 50%
- VAT has increased from reduced rate of 12.5% to 20%
- Increase in the National Minimum Wage
- National Insurance contributions for employers have risen by 1.5%
- Soaring energy and fuel prices – with another rise expected in October
- Ongoing supply chain issues because of Brexit, the pandemic, and war in Ukraine

Cost of living is holding back growth, with a 0.1% GDP increase for February presenting a challenging economic horizon, particularly with inflation and rising costs. Rising inflation has left small businesses with little option but to increase prices: the rising cost of living starts with a cost of doing business crisis, and so it is imperative to take all measures to address the financial barriers of doing business and support our SMEs.

Many small businesses rely on discretionary spending. If households have constrained income, it will be these businesses that are likely to suffer first and may be less able to pass the price increases on. The cost of doing business is rising, which in turn will continue to have an impact on the cost of living.

While this restraint in spending will be felt across the economy, some sectors which were most impacted by the pandemic such as hospitality and retail may be particularly exposed in the months ahead.

Our research suggests increased fuel costs add over £1,000 per year onto SME's energy bills, with some sectors facing far higher bills.

For a typical commercial van, the increase is approximately £1139, with an average of 2648 litres of fuel used annually, at currently an additional £0.43 cost per litre.

SMEs have faced an average gas bill hike of more than 250 per cent in the last year with gas prices paid by some in the first three months of 2022 soaring by this amount when compared with the same period in 2021.<sup>1</sup> However, unlike domestic customers, firms have yet to see any dedicated Government support and with insecure contracts, the unstable energy market is also seeing suppliers withdraw tariff propositions at short notice.

Our latest Small Business Index suggests 80.4% of small businesses in Wales reported increased costs over this last quarter. This is likely to have an instant impact on small businesses, who may now see new and immediate salary expectations rising, along with inflation. This is a cost that will ultimately be passed on to consumers.

FSB are calling for banks to be supportive towards small businesses during this testing period, as the access to finance is likely to continue to be squeezed.

National Insurance is set to add to the costs of the 55,385 SMEs affected in Wales by £173m (at a median cost of £3,115 per business), as can be seen in the table below:

	Number of SMEs with employees	Total Employers NICs cost increase	Total Employers NICs cost increase, £m
United Kingdom	1,408,325	£4,386,778,300	£4,387
North East	40,900	£127,399,025	£127
North West	141,255	£439,993,871	£440
Yorkshire and the Humber	104,220	£324,633,898	£325
East Midlands	100,325	£312,501,399	£313
West Midlands	118,725	£369,815,386	£370
East of England	139,010	£433,000,942	£433
London	245,090	£763,428,536	£763
South East	208,105	£648,224,308	£648
South West	124,075	£386,480,051	£386
England	1,221,705	£3,805,477,417	£3,805
<b>Wales</b>	<b>55,385</b>	<b>£172,518,216</b>	<b>£173</b>
Scotland	94,770	£295,198,182	£295
Northern Ireland	36,460	£113,568,911	£114

<sup>1</sup> <https://www.cornwall-insight.com/businesses-facing-a-250-increase-in-gas-bills/>

Businesses remain in a vulnerable position after the Covid-19 pandemic. In February, corporate insolvencies in England and Wales more than doubled over the past year (+121%). Businesses are struggling already, and any recovery will require a resilient small business sector to be able to weather the continuing storms from the cost-of-living crisis as outlined.

- **How are cost of living pressures affecting the workforce, and how are different groups within the workforce being affected?**

Clearly, cost of living pressures will impact on the standard of living of the workforce, small business owners and the self-employed.

The trauma of Covid-19 will likely have a continued impact on mental health. FSB's recent survey of 1,000 business owners finds that a third (34%) of all small business owners state that their mental health declined over the course of the pandemic. Latest [Government figures](#) show that there are 5.5 million small businesses across the UK, indicating that 1,800,000 have suffered a mental wellbeing hit due to Covid. Across all respondents, one in four (24%) report that they currently have a mental health condition such as anxiety, depression or post-traumatic stress. Among disabled entrepreneurs, the figure rises to four in ten (43%).

As such, following two years of accumulating debt, care responsibilities for staff, as well as personal pressure, cost of living will add to mental health vulnerabilities and to these pressures.

The rise in cost of living will understandably lead to rising pressures on wages, with SMEs being in a difficult position of financial insecurity following the pandemic and disruption to business, and where SMEs are already reporting a rising cost of labour and skills shortages.

Our 'What we Value' report notes the leadership and pastoral care SME owners have, and the close relationships they have with their staff. They will feel responsibility to help where they can, but SMEs may themselves need support to weather the current storms themselves.

Where SMEs struggle on wages, they tend to look to provide better and more flexible terms and conditions and we will continue to encourage exploring such options as well as flexible or remote working where that may save money also and where they fit the company.

- **How are rural communities being affected by the cost of living crunch, and to what extent are the pressures they face different to urban areas?**

Rural areas already face greater costs in terms of fuel costs, and so the impact will be felt disproportionate in these areas.

Less disposable income could have an impact on the drive toward better local food systems, with advice to 'buy value brands' for example being at the expense and against a strategy to point to the value of quality local products. It also raises the costs of bringing perishable products to market and in terms of export.

Rural areas in Wales are more dependent on tourism and so less disposable income is likely to lead to issues in terms of the amount visitors can spend locally and fewer holidays taken. It is also likely to force business to raise prices for their services, pushing this into a vicious economic cycle whereby business costs go up, leading to pressures to raise prices, potentially leading to fewer visitors leading to less revenue.

We know that rural and coastal town high streets are already vulnerable due to factors outlined in our recent report 'A Vision for Welsh Towns'. With less 'strength in depth' of economic activity, low retail and hospitality spending may well have a disproportionate effect on these economies and Welsh and UK governments will need to look to measures to maintain the viability of operating businesses within these settings and supporting Welsh high streets.

It's also the case that where businesses may look to adapt to lower costs that this may be more difficult in rural areas. For example, there would be less by way of EV charging points if this was a way to lower costs either in personal car use, or in terms of freight and deliveries. Broadband and 5G infrastructure may make it more difficult to lower travel costs through tools such as remote working for example.

The discussions around mitigations for rural areas are therefore linked to infrastructure and economic development strategy that places value on rurality, on local supply systems and in terms of ensuring a level playing field for SMEs whatever their location in Wales.

- **How effective are the support measures that the Welsh and UK governments have put in place, and what further support might be needed over the coming months?**

FSB have encouraged firms to check what support is out there, such as the Employment Allowance, and to also check with local authorities where there may be unspent funds available. We would encourage local, Welsh and UK governments to proactively seek to provide support, ensuring information is widely disseminated or that support is provided automatically where possible.

We are calling for banks to be supportive towards small businesses during this testing period and would urge governments to apply pressure to ensure this too.

During the Spring Statement, FSB were pleased to see our calls for an increase in the Employment Allowance – a tax cut worth up to £1,000 for eligible businesses and a measure for which FSB campaigned, was included by the Chancellor. This measure, along with the fuel duty cut, may help some SMEs keep their head above the water.

While we are pleased the Chancellor is listening to our calls, government must go further to support small businesses with soaring energy costs. The rising energy costs are concerning, and while government was right to focus on domestic consumers, actions to support small businesses also need to be taken, otherwise we will start seeing the serious impact of the cost of doing business.

Any remaining funding, allocated by Welsh Government to be utilised in reaction to supporting businesses through earlier phases of the pandemic, should be reconsidered for redeployment within the context of the energy price crisis. It may yet be the case that Welsh and UK Governments will need to come up with further targeted support to help cushion the blow of higher costs for businesses to ensure that we don't stifle the recovery.

The business rates holiday in Wales was extremely helpful to our members in 2020-21 and 2021-22, and we welcome the continued relief of 50% this year for SMEs. However, this policy was put in

place ahead of the Omicron crisis, prior to the worst rises in inflation, fuel and energy costs, and ahead of the impact from the war in Ukraine. As such we would urge Welsh Government to revisit whether there is a means to lower the cost of business.

In general, we would urge governments to lower the cost of doing business where possible, and to ensure we secure the SME sector as the foundation to our economy and communities in Wales. Where possible, the support on cost of living to individuals should also apply to small businesses, to continue to mitigate the pressures to raise costs.