A tool for transformation

The power of capex in challenging times

HSBC UK

Foreword: Ambitions interrupted

The foot is down – but the brakes are on. In a nutshell, that is the predicament in which many businesses find themselves in 2022, according to the latest survey of capital expenditure intentions commissioned by HSBC Equipment Finance.

UK business has no shortage of ambition. Our research shows it is emphatically bouncing back from the doldrums of the pandemic years. It also has capital available to fund its plans: 45% of respondents told us their capex will rise this year.

However, businesses are being frustrated by a fresh set of external pressures. Soaring inflation, the fall-out of war in Europe and continuing obstacles in supply chains are among the interlinked factors challenging business and threatening to hold back their growth intentions.

The risk of stymied plans is that businesses find themselves stagnating. Those who seek out ways to continue strategic investments – if necessary, pivoting to alternative areas to the ones they originally favoured – will be better placed to expand and flourish beyond the current crises.

Shifting priorities

The survey also reveals some striking changes in business mindset. There has been a significant rise in the numbers who see digitisation and automation as priorities, for example. This suggests that with supply chains choked off or delayed, some firms are turning to business process transformation to gain efficiencies in a tough financial environment.

These issues are closely linked to another growing priority: securing the right workforce for the next phase of growth. This is partly about up-skilling staff in new technologies, but it is also influenced by the tight labour market. Staff availability is a current concern for two-fifths of our respondents. With the dearth of low-cost labour unlikely to change in the medium term, the case for investment in automation becomes more compelling.

Meanwhile, the survey provides conclusive evidence that the drive for sustainability is now being fully embraced by UK businesses – not as a side issue, but as a prerequisite for maintaining trust and winning new business.

Riding out crisis

At HSBC Equipment Finance, we support the capex needs of business in the round. That goes beyond financing itself, to include exploring the alternative investment options to realise your business aspirations, as well as helping to assess the benefits.

It is heartening to see how swiftly most firms have surmounted the existential threats of Covid-19 that prevailed a year ago. That resilience augurs well for UK business to ride out the current crises. Experience suggests those who continue to add value through investment will outperform their peers, and find themselves better equipped to thrive once conditions are brighter.

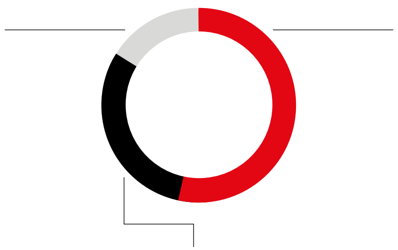
Sacha Balachandran
Head of HSBC Equipment Finance,
HSBC UK

Barriers to growth

Cost and supply uncertainty are making it hard for business to invest at the pace and volume they anticipated. Yet standing still is not a viable option.

Reasons for optimism

There is good news in this year's capex report. While the survey was taken in the spring, before UK inflation hit a 40-year high, it is clear that businesses now feel positive about Covid-19 recovery, which was the main preoccupation in last year's results. Most are also upbeat about the availability of capital to invest.



The number of businesses expecting their capex spend to increase through 2022 has risen significantly since last year, by 9 percentage points. Larger firms, and those trading internationally, are more likely to anticipate higher spend.

45% of businesses expect their capex spend to go up this year; **up 9% on 2021**

63% of corporates are positive about the availability of capital, **compared to 53% of SMEs**

Blocks on growth

However, businesses are being tested by a cocktail of challenges. Together, these threaten to hinder spending and hold back growth.

Soaring costs are causing the biggest concern. The volatile geopolitical scene is also high on the business agenda, and has compounded existing supply chain difficulties. Margins are being eroded and cashflow disrupted; in some cases, orders are going unfulfilled.

Manufacturing and production businesses are especially concerned about costs (83%) and supplies (75%). Retail and wholesale businesses are most likely to see the UK economic climate as a concern (60%). The business complexity and greater international reach of corporates makes them more vulnerable to some of these factors: for instance, 82% of corporates are negative about costs and 72% about geopolitics, while the figures for SMEs are 73% and 62% respectively.

At the same time, many are concerned about staff availability. A significant minority are also finding changed trading conditions with the EU to be a challenge.

Factors affecting business	Positive	Neutral	Negative
Availability of capital to invest	54%	31%	15%
Covid recovery	49%	37%	14%
Staff levels/availability	30%	30%	40%
UK economic climate	27%	26%	47%
Changes to trade conditions with EU	16%	47%	37%
Supply of materials/goods	15%	24%	61%
Business costs	11%	15%	74%
Geopolitical environment	10%	28%	62%

Creative solutions

These challenges make it tougher for businesses to pursue their planned courses of investment and growth, but our findings also suggest that creative solutions are being found by some respondents.

For instance, investment in technology and digitisation is ramping up, with a 15% rise over last year. Activity in automation, in particular, is notably stronger (43%) among those who are most concerned about staff availability, suggesting that some businesses are turning to long-term digital strategies partly as a way of resolving chronic workforce issues.

There is also a striking surge in those who see sustainability as a prime area for investment – up by 19% on last year. Reducing energy use and waste are the top areas of focus, but businesses also recognise that the benefits go far beyond cost efficiency: an overwhelming majority of those investing in this area expect to gain through customer reputation and new business wins.

19%

increase from last year in businesses who see sustainability as a prime area for investment

Alternative outlets

More generally, businesses may be adapting their capex planning approaches to identify useful area of investments that are less dependent on unpredictable supply pipelines.

"The biggest area of capex increase is on machinery and equipment – but supply issues mean this is likely to be hampered in many cases," says Sacha Balachandran, Head of Equipment Finance at HSBC. "With capital often on hand, the critical point is not to allow growth plans to be stifled.

If supply chain delays are impacting a specific investment, agile businesses will pivot to another area of development, whether that be enhancing sustainability, acquiring future workforce skills, or expanding into new markets.

Sacha Balachandran
Head of Equipment Finance,
HSBC UK

Multiple challenges

"Devastating. We have been unable to get products in since Covid. Some items are trickling in now but we still have long waits for many others – this has had a dramatic impact on our business"

- Retailer -

"Costs are creeping upwards, squeezing margins – but we've built up a good war-chest so are in a strong position to continue investing in growth"

- Wholesaler -

"Shortage of raw materials and consequential price increases are restricting cash flow and capital investment… we have mitigated some of this by investing in our stock holding and sourcing from European suppliers to diversify risk"

- Business services provider -

Green to the core

Sustainable operation is now a core purpose and an investment priority for UK businesses of all types.

Imperative to success
Environmental action has long been on the agenda: for some businesses, a genuine passion; for others, a useful way of driving efficiencies. But our survey eliminates any remaining doubt about the central position of sustainability in UK business strategy.

More than half of respondents see this area as one of importance for capital expenditure – up by 19% from last year. The number of those who do not see it as important to their business has almost halved.

51%

say environmental sustainability is an important area for growth **up by 19% on 2021**

2 in 3

businesses are **confident they can achieve their environmental goals**

Tangible benefits
While reducing costs remains a key areas of focus, especially for smaller firms, businesses increasingly have a clear view of the hard business benefits to be gained through sustainability.

Of those focusing on this area, the vast majority see it as critical to their reputation among customers, for example. And over three-quarters say it helps them win new business, while only 8% feel this is not the case. The corollary is also true: recent research suggests almost 60% of businesses lose work due to weak ESG performance.

only 8%

of businesses feel a **focus on sustainability does not help them win new business**

SMEs are more likely to see sustainability as a way of helping to reduce costs (81%, compared to 47% of corporates). However, SMEs too appreciate the wider benefits: 86% see reputational benefits while 73% believe it wins them new business. And 62% of SMEs are confident about the prospects for their own sustainability plans, compared to 56% of their larger counterparts.

How sustainability helps business	
Reputation with customers	88%
Community perception of business	82%
Win new business	78%
Boost staff morale	71%
Reputation with suppliers	67%
Reduce costs	63%
Reputation with shareholders	48%

88%

sustainability helps business with **reputation with customers**

82%

sustainability helps business with **community perception of business**

1 - https://dwfgroup.com/en/news-and-insights/press-releases/2021/11/59-of-businesses-lose-work-due-to-poor-esg-performance

Where investment is going
Given soaring fuel costs, it is unsurprising that energy efficiency is the most common theme being pursued by those with an environmental focus. Over half of these companies are focusing on vehicles, underlining the growing interest in electric power.

This focus makes sound sense in the context of strong government and city promotion of electric vehicle use – London alone has 17 relevant policies. From giant logistics players to local farm shops, businesses are investing in e-vans, e-trucks and e-cargo bikes in pursuit of their net-zero strategies.

Others are looking at wider associated EV infrastructure (eg charging) and beyond EVs: for heavy-duty transport, the high energy density of hydrogen makes it potentially more attractive than batteries for long distances. Meanwhile, far-sighted manufacturers are investing in R&D to explore alternative technologies to surmount the environmental risks linked to materials such as cobalt in battery manufacture.

Areas of environmental focus	
Energy	78%
Waste management	69%
Building efficiency	57%
Vehicles	56%

Future-proofing exercise
"Businesses are aware of the brand and reputational value of being a sustainable operation – and how this is now simply expected by customers, suppliers, investors and the wider public," says Sacha Balachandran.

"At the centre of our Group Sustainable Finance strategy is the aspiration to be a leading global partner in financing, managing and shaping the transition to a low carbon world. Within our revised Sustainability strategy announced last year (our 'Plan for the Planet') we are committing to working with customers to reduce carbon emissions from our overall portfolio of customers to net zero by 2050 or sooner.

"It's no coincidence that those who told us this was a key focus are significantly more likely to be optimistic about growth.

> **"Injecting capex into the pursuit of net zero goals is more than just the right thing to do. It's a hard-headed way to future-proof your business."**
>
> Sacha Balachandran
> Head of Equipment Finance,
> HSBC UK

Case study: Select Plant Hire

Leading the switch to electric

Select Plant Hire's (Select) investment in the latest sustainable plant innovations involves repeated "leaps of faith", but they are chances worth taking to maintain the company's leading role in transforming the construction industry.

While not a silver bullet for emission reduction, electrification has a strong part to play. By May 2022, one in eight new cars on UK roads was an EV[1], and many major companies are pledging to make their fleets all-electric within the decade.

The shift is well under way in construction too. New standards require smart, future-proofed buildings, and there is pressure for more sustainable construction methods and equipment. Post-pandemic, pent-up demand for new infrastructure is soaring. Select sees its role as helping the industry to meet that demand sustainably.

Select, part of the Laing O'Rourke group, is one of the UK's largest and most capable suppliers of equipment and services to the construction industry including: Lifting, Site Solutions, Specialist Plant, Test & Inspection, Logistics, and an industry renowned training academy. Over the last 30 years, Select has been involved in iconic projects that have shaped UK infrastructure, most recently including HS2, Hinkley Point C, Google King's Cross, and Stratford Olympic Park.

Replacing older plant to achieve energy efficiency is a big priority for the company. It has worked with a key supplier, Punch Flybrid, on an innovative energy-storage system for tower crane operation. It also makes continuous investments in new equipment to help shed the industry's traditional reliance on diesel.

1https://heycar.co.uk/blog/electric-cars-statistics-and-projections

Pushing boundaries
"For infrastructure jobs, we see a real appetite for sustainable assets," says Paul Griffin, Finance Leader. "We're really keen on pushing the boundaries, not only to reduce emissions and noise pollution on site, but to ensure sustainability for the people who will ultimately be using the completed infrastructure."

Select purchased the UK's first electric crawler crane, using a sustainable finance line from HSBC Equipment Finance, and has since funded a second. The business is now seeking to electrify other plant, and to install EV charging points at its head office and depots in support of its electric/hybrid company car policy.

Ramping up investment
Older, less sustainable equipment is likely to fall in value in the coming years, so the business has scaled up its capex plans to ensure it can continue to meet demand with new sustainable assets. "As cities start to tighten their own emissions constraints, older, less sustainable equipment will be obsolete for UK use," Paul says. "So to stay ahead of demand, we need to invest more, not at the same level.

"Electric assets new to the market are more expensive than the diesel equivalent. This is where it takes a leap of faith to buy new technology, both by us and by the bank supporting us. HSBC has been really supportive of our green agenda.

"You can only get better, more sustainable products if you start investing to drive demand, so that in turn the manufacturers invest in more. You have to believe that you're doing the right thing."

The best tech, the right team

Intertwined digitisation and workforce issues are preoccupying many businesses.

An inflection point
Driven by the expectations of prospective employees and younger consumers, and accelerated by the experiences of Covid-19, digitisation is an imperative for business leaders. Smarter, cleaner technologies are also central to the net-zero agenda.

Our survey underlines the transformative point at which UK business finds itself. In the drive to stay ahead of new ways of working and delivery, there is an increasing focus on investment in digitisation and technology. The proportion of businesses focusing on these areas has risen by 15% over the past year.

Interest in these areas goes well beyond traditional manufacturing and heavy asset industries – for example, two-thirds of professional and business services providers are focused on tech investment. Larger firms are especially engaged with tech: 59% of them are spending more this year on digitisation and IT, compared to 33% of SMEs.

55 %

see technology and digital as an important investment focus – **up 15% since 2021**

Preparing the workforce
At the same time, businesses of all sizes and sectors are concerned about getting people with the right skills in place for the next phase of growth. Two-thirds of respondents are focused on the future skills of their workforces. For many, this imperative is likely to be linked with the digital transformation drive and its associated recruitment and training needs.

67 %

of businesses see future workforce skills as an important area of investment

3 - https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1033698/ras-final-report-nov-2021.pdf

Shift to automatic
Automation is another priority area across a range of industries. Government research suggests industrial robots could boost value in the warehouse logistics sector by 14%, and in food and drink manufacturing by 3%, by 2035. In agriculture, boosting automation is also central to the government's recent food strategy.

Half of manufacturing and production businesses see automation as a focus, according to our survey. More surprising is the high proportion of all businesses who now see automation as important – 33%.

1 in 3 businesses see automation as an investment priority

Those who are most concerned about staff availability are more likely to have automation on their agendas (43%). This indicates that business leaders' minds are turning to automation in the context of the current tight labour market.

"The effects of Brexit and high vacancy rates mean low-cost labour will remain scarce for the foreseeable future," says Sacha Balachandran. "That makes automation a natural move for many businesses. While the investment cost is significant, it makes sense if for those with capital to deploy and finding hurdles to investment in other areas.

"Supply delays and difficulties also provide an opportunity to build automation improvements into your supply chain, setting you up to satisfy orders more quickly once things are running more smoothly again.

Sacha Balachandran
Head of Equipment Finance,
HSBC UK

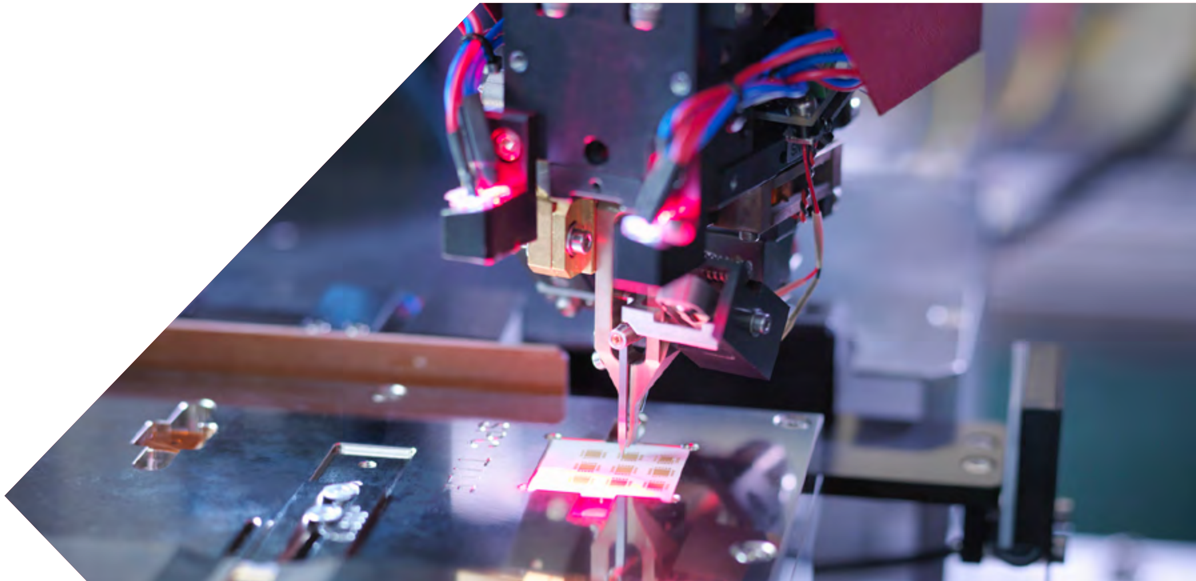
4 - https://www.gov.uk/government/news/tech-and-innovation-drive-to-boost-food-production-and-back-british-farmers

49% of manufacturing businesses put emphasis on automation – **up 16% since 2021**

Forward thinkers
"The recruitment scene is so tough at present that it's understandable if some businesses find it hard to think beyond the urgency of immediate vacancies," Sacha adds.

"But getting prepared with longer-term workforce skills is vital to ensure sustained growth and help attract new key talent. It's notable that businesses who are doing this are also more likely to be thinking hard about digitisation and other issues such as sustainability – suggesting a forward-looking mindset.

"With one in three businesses focused on automation and two-thirds concerned with future workforce skills, these are clearly areas that merit investment appraisal – a task with which we are well equipped to support our clients."



The next big thing?

The metaverse – where the physical world meets virtual and augmented reality – offers potential to simulate immersive worlds and bring new dimensions to digital interaction. For many, it remains a buzzword at best – but early adopters among UK businesses are thinking about how this development will transform their own sectors.

One in 10 of our respondents is prioritising plans to harness the metaverse to enhance customer experience, expand training and reduce costs. Smaller businesses are more likely to be in this group, capitalising on their agility to capture new trends.

Businesses with an active interest in the metaverse show an all-round willingness to prepare for change. For instance, 78% of them cite environmental issues as an investment priority, 85% digital and tech, and 94% future workforce skills.

"We want to integrate our products into a VR, to enable customers to visualise them on their homes"

- Production business -

"When the cost of fully immersive property viewings comes down, we will be able to save a lot of time in travel to viewings"

- Property firm -

"It could change the events business"

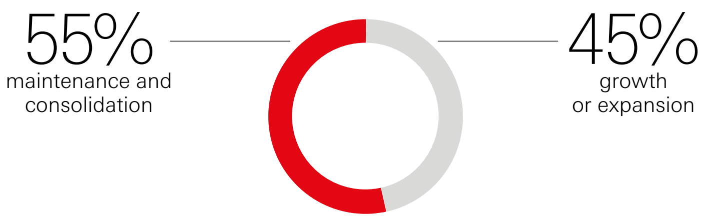
- Business services provider -

Investing to expand

While much capex is devoted to maintaining and consolidating business, almost half of spending is being channelled into growth.

Expansion plans
Larger businesses, and those trading internationally, are dedicating more to expansion efforts – around half of their spend. Overall, one in three businesses is devoting at least 60% of this year's capex to growth ambitions.

Capex spend



30%

of businesses are **spending 60%** or more of capex on growth

36% of firms will spend more this year on expanding into new markets. A similar proportion will invest more in diversifying their products or services, while 29% plan to boost research and development. Larger businesses are most likely to be focused on market expansion and R&D.

Percentage of businesses increasing capex spend	
Machinery and equipment	43%
IT/digital	38%
Expansion into new markets	36%
Land and premises	36%
Product/business diversification	35%
Environmental sustainability	33%
Research and development	29%
Vehicles	29%

An eye out for bargains
The survey also reveals a surge in potential M&A activity. Four in ten large businesses are actively seeking acquisition opportunities – up by 9% on last year.

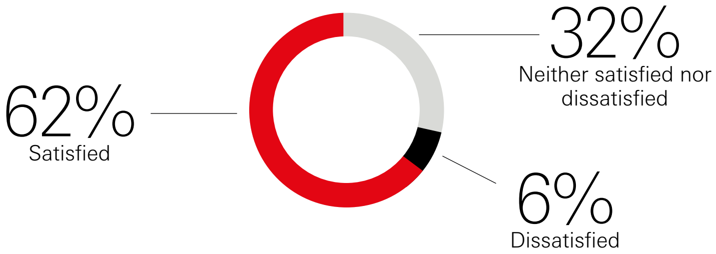
"With strong capital to hand, it makes absolute sense for corporates to be on the lookout for potential new purchases," says Sacha Balachandran. "In the current climate there are likely to be some good deals out there, and finding the right match can enable companies to extend their reach and achieve new business ambitions."

The practicalities

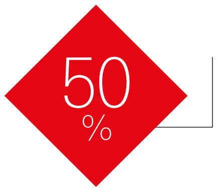
HSBC is here to help businesses invest in ways that allow them to stay competitive and seize the opportunities ahead.

How does capex perform?
Capital spending is generally fruitful. Few businesses doubt the value of the investments they make. Most (62%) are currently satisfied with the returns they are getting on their capex, with only a small percentage dissatisfied.

Business satisfaction with returns on capex



However, almost one in three firms admit they have no clear method of measuring those returns. Where that is the case, satisfaction is markedly lower. Provided at least one recognised method of measurement is used – for example, payback and accounting rate of return, discounted cash flow, risk measures and portfolio optimisation – satisfaction is generally good. But half of those who do not assess capex returns are dissatisfied.



of firms who do not assess capex returns are dissatisfied

"Following up spend with performance analysis is fundamental to the financial effectiveness of any business," says Sacha Balachandran. "Whatever the method, firms that do so establish a pattern of success. At HSBC we support clients who are new to this type of analysis, helping them understand potential and actual returns."

Where does it come from?
Around a third of businesses expect to use more cash for capex, while one in five will use more debt funding. Almost half of businesses do not plan to change the sourcing of their capex this year. Bigger businesses, and those in the manufacturing and agriculture sectors, are more likely to fall into the latter group.

How will capex be funded this year?

Explore the options
HSBC is committed to supporting the capex needs of all types of business, Sacha adds. "With our extensive global network, we are also well placed to support clients as they navigate through the current blockages – or to explore alternative capital allocations that will support their business ambitions."

Further reading and more information

To discuss your capital allocation plans in more detail, please contact your Relationship Director or visit our website.

To support you on your journey to Net Zero, we have created a number of guides, which you can find on our Sustainability Hub.

Report methodology

The survey was carried out between late March and mid-April 2022. 670 customers took part in the online survey.

24% of responses were received from businesses with turnover of £0-2m, 39% from businesses with turnover between £2-25m, and 16% from businesses with turnover of £25m+.

52% of businesses who responded trade domestically, and 48% trade internationally.