

Is business booming?

Chief economist's comment

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- Across several major economies, there has been a surge of new business startups as lockdowns have ended.
- These are small business startups. There may be a focus on retail and wholesale firms. It seems as if people have used lockdowns to explore their entrepreneurship.
- Data on business creation is better quality than survey evidence. This suggests that confidence in the economic outlook is higher than survey evidence is reporting.
- These new businesses may too small to provide the sole income stream for their owners—but they may form part of a person's portfolio of incomes in the gig economy. The risk is that economic data will overlook this and underestimate economic activity.

Financial markets often underestimate human resilience. People adapt in a crisis. One example is the fact that business creation is booming in many countries as lockdowns end.

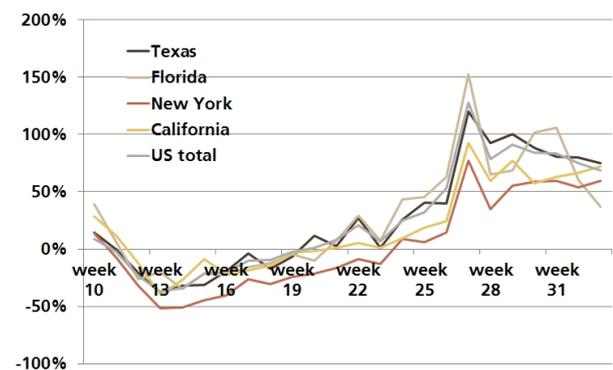
Business creation cannot be compared from country to country. Definitions of a new business are not the same. But business creation data is not a survey. People legally registered their business, and generally pay to do so. Business creation numbers have a degree of quality that survey evidence does not.

More than a bounce back

Business creation fell dramatically during lockdown. The UK, which has weekly data, shows the collapse in business creation the week lockdown started. US weekly data shows a rapid drop in business creation as the first states contemplated lockdowns. This was effectively a supply and demand problem. As government offices closed it became more difficult to register a business. As fear of the virus grew,

US business creation post-lockdown more than offset lost business creation in lockdown

Business creation growth % yoy, weekly from March (week 10)

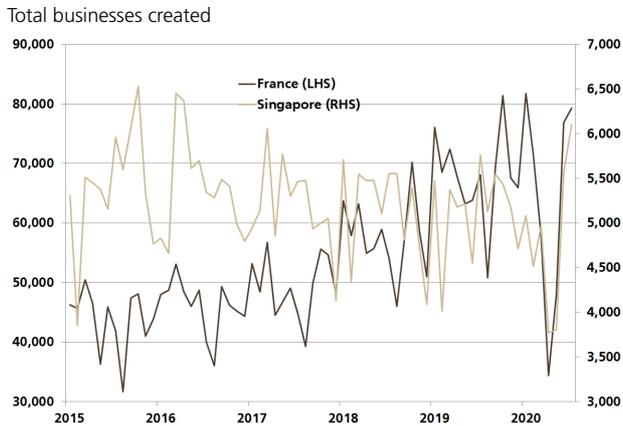


Source: US Census Bureau, UBS Calculations

uncertainty about the economic outlook reduced people's willingness to take the risk of starting a new business. As lockdowns have eased, there business formation has boomed. This is more than offsetting the weak business creation in lockdown periods. US business applications for 2020 to date are up almost 14% compared to the same period in 2019. UK business applications are noticeably higher than normal. France and Singapore have also seen post-lockdown surges in business creation. The numbers of Japan's sole-proprietor businesses have risen quickly as restrictions have eased.

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Business creation in France and Singapore recovers strongly



Source: Haver, UBS

What businesses are being created?

Details on business creation are often missing from high frequency numbers. However, most of the businesses being created are small. In the US the number of businesses intending to pay wages has risen, but the rise is nothing like the surge of overall business applications. That suggests single person businesses are being created.

In the UK the number of businesses registered at Companies' House has grown far faster than the number of businesses registered to administer VAT. VAT registration is only required for larger companies. In Japan, it is sole proprietorships rather than large businesses that have had a rapid growth in business creation. Singapore has had a surge of new companies (large and small), but sole proprietorships are being created at the fastest pace in three years.

There is very little evidence as to the sectors where businesses are being created. High frequency data from France and Singapore both show a bias to wholesale and retail business creation. There is likely to be a strong bias to online wholesale and retail businesses being created, given structural trends in the global economy and the sharp rise in online retail sales in most major economies.

What does this tell us?

The fact that businesses are being created does not deny that the pandemic will also cause a large number of business failures. But the fact that businesses are being formed does raise some economic possibilities.

Most obviously, business creation is a signal of economic confidence. Setting up a business requires some optimism about the future. Specifically, the number of small businesses being set up suggests that optimism is quite widespread. Individuals seem to have more faith in the economic outlook than they are prepared to admit in confidence surveys.

Details of business creation also suggest a link to economic confidence. Business creation coincides with areas that are more likely to have higher confidence levels. In the US, business creation in New York has lagged that of the rest of the country. New York was very badly affected by COVID-19 when fear of the virus was especially high. Although other states have seen high infection rates, this has taken place at a time when fear of the virus has apparently lessened.

Similarly, Spain has lagged the UK and France in business creation. Some of this may be due to the tourism bias of the Spanish economy. Tourism is a higher risk economic sector at the moment. Spain also had one of the worst economic performances in Europe. That will have increased economic fear.

Government policies do not seem to be behind this surge in business creation. The pattern is being repeated in different economies, which have offered different support schemes during lockdown. Generally speaking the businesses are too small to receive significant tax benefits. As a rule, government aid has been given to existing businesses, not to businesses created since the start of lockdowns.

The pattern of business creation suggests growth of the so-called gig economy. Online retail businesses have relatively low barriers to entry. They can be set up cheaply from home. Time spent at home in lockdown may have inspired people to act. Such businesses may not replace paid employment. Instead, they are likely to become part of a portfolio of different household income sources. Diversifying income sources was a trend of the fourth industrial revolution. A less secure labor market may have sped up the trend. There is a risk that this will not be properly captured in economic data, which may assume outdated patterns of working. If so, this means that the strength of the economic bounce back may be underreported in the initial data releases.

Appendix

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