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ERC *Insight*

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Contribution to Job Creation by High Growth SMEs

High-Growth Firms (HGFs) are a very small proportion of UK businesses population yet they have a disproportionate impact on job creation. We re-visit the issue to confirm that typically, over a three year period, high growth SMEs represent less than 1% of established businesses, but generate 20% of all job growth amongst established businesses which grow.

Following on from the publication of the ERC Insight Paper on HGFs in February 2014[1] we have been asked by the Department for Business, Innovation and Skills (BIS) to provide evidence on the contribution of SME HGFs to job creation within the wider population of all HGFs.

OECD High-Growth Firm Metric – a Reminder

The OECD High-Growth Firm (HGF) metric has a very precise definition. If we are measuring growth over a three year period, the first step requires that we consider only firms which, are born before the beginning of the three year period and are alive at its end. This implies that in each period we will have a 'balanced panel' of firms – the same firms are always present (often referred to as 'continuing firms').

In terms of the OECD definition a HGF is a firm in this balanced panel with at least 10 employees at the beginning of the period and which records an annual average growth of 20% in employment over the three year period. We define the HGF incidence rate as the number of HGFs divided by the number of firms (in the balanced panel) with 10+ employees. Starting with 1998, we have data on 14 overlapping 3-year periods: from 1998/2001 to 2011/2014.

[1] Hart, M and Anyadike-Danes, M (2014) "Moving on from the Vital 6%", ERC Insight Paper, February 2014

How many HGFs are there in the UK?

The results for the number of HGFs and the HGF incidence rate are plotted in Figure 1. In summary, the incidence rate of HGFs averaged 7.2% over the period between 2002-05 and 2007-10 and then dipped to an average of 5.9% in the period of economic downturn before 'bouncing back' to 6.6% in 2010-13, and edging up, again, to 7% in 2011/14. So HGF incidence is now firmly back to the level it was before the Great Recession. There were 10,929 HGFs in 2011-14, also back to pre-2008 levels.

Figure 1: Prevalence of HGFs in the UK 1998-2014

Source: ONS BSD (1998-2014)

HGFs and Job Creation

The composition of job creation by established businesses over the last decade and a half has changed, as Figure 2 shows. In particular, the share of non-HGFs has increased by about 10 percentage points since the mid-2000s (a by-product of a significant increase in small firm births). One constant though has been the share of SME HGFs: their contribution has been within one or two percentage points of the long-term average of 20% since 1998/01. Even the Great Recession made very little difference to this proportion. By contrast, the share of larger HGFs in job creation has shown a ten percentage point decline (roughly matching the increase in the non-HGF share).

Figure 2: HGFs and Job Creation

Source: ONS BSD (1998-2014)

Summary

What is clear from the evidence is that there are a very small number of firms in the UK which can be classified as HGFs using the OECD definition. Further, the HGF prevalence rates have remained largely unchanged since the late 1990s. Focussing specifically on SMEs we find that although high growth SMEs represent less than 1% of established businesses, they generate 20% of all job growth amongst established businesses which grow. Again this proportion has remained virtually unchanged since the late 1990s and was not affected by the Great Recession.

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Notes:

1. Here we consider the stock of established businesses which make up the 'balanced panel' -- alive at the beginning, alive at the end -- over a three year period. The earlier ERC Insight piece on HGFs included 'new' businesses -- born during a three year period -- in the analysis.

2. We divide the stock of established businesses into four groups:

   a. young, one year old at the beginning of a three year period.

   b. SME HGFs more than one year old, more than 10 but less than 250 jobs at the beginning of the period, and more than 20% annual average growth over a three year period.

   c. large HGFs more than one year old, more than 250 jobs at the beginning of the period, and more than 20% annual average growth over a three year period.

   d. non-HGFs more than one year old, less than 10 jobs at the beginning of the period, and/or less than 20% annual average growth over a three year period.