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EXECUTIVE SUMMARY

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An Investigation of UK SME Access to Finance, Growth and Productivity, 2015-2017

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Executive Summary

The study investigates UK SME access to external finance and its relationship to growth and productivity. Three research questions are addressed:

RQ1 – What are the characteristics of SMEs that determine their funding and discouragement?

RQ2 – What are the impacts of external finance on SME performance and productivity?

RQ3 – What are the implications for theory and policy?

Findings relate to a two-stage approach:

(i) Quantitative analysis of a panel of 4,165 surviving SMEs responding to the UK Longitudinal Small Business Survey (LSBS) baseline wave in 2015 and through two succeeding annual survey waves in 2016 and 2017;

(ii) Follow-up qualitative interviews to test the quantitative data findings with 6 expert business finance advisors working with innovative potential high growth SMEs in England, supplemented by 3 interviews with senior strategic managers from two business support organisations.

RQ1 – What are the characteristics of SMEs that determine their funding and discouragement?

Key characteristics of access to finance success

- The most successful SMEs applied every year and were significantly (<.001 level) larger SMEs (50-249 employees), more likely to use general business support and specialist access to finance advice and (<.05) to have more partner/directors, and better perceived ability to access finance.
- The smallest (self-employed) and youngest SMEs established up to 5 years were significantly (<.001) less successful in their applications.
- SME resource base is influential; fewer partner/directors and perceived poor finance access capabilities were significantly (<.01) associated with less success.
- Lower level innovative firms (referring to firm, rather than market level innovation) were less successful in accessing external finance (<.05).

Characteristics of Non-financed groups

- Happy non seekers were significantly (<.001) more likely to be self-employed, not seeking business advice, not having a business plan and not innovative.

- Discouraged non finance seeking SMEs were significantly (<.001) less likely to be large (50-249 employees) and more likely to possess poor perceived capabilities to access finance, have no business plan and be younger (5 years or less established; <.01).
- Those that sought finance, but did not receive any (2015-17) were significantly (<.01) more likely to be younger (up to 5 years established), innovative and have used specialist access to finance advice and general business support, but have no business plan.
- Known closures (n=552) were significantly (<.001 level) more likely to be established up to 5 years, family led with 1-2 directors/partners, possess poor capabilities to access finance, have no business plan and have declining employment, and (<.1) declining sales turnover and not be innovative.

RQ2 – What are the impacts of external finance on SME performance and productivity?

A caveat is that productivity data is constrained to a crude calculation of sales turnover divided by overall employment change between Autumn 2015 and Autumn 2017 for 2,896 SMEs.

Growth and Productivity

- There was no significant difference in the employment and sales growth of externally financed and non-financed SMEs. A high proportion of external finance was for premises, equipment, working capital and R&D unlikely to render shorter term changes. Productivity improvement (i.e. sales turnover per employee), for example from investment in more efficient machinery and working practices, may not result in shorter term employment increase.
- Half (50.8%) of all panel SMEs increased productivity between 2015-17; 8.9% remained static and 40.3% declined; median percentage growth was highest amongst successful finance seekers (5%) and lowest for contented non seekers (0%).
- Successful access to finance is correlated (<.1) to productivity growth, relating more to larger, more frequent applications by larger SMEs. Younger established SMEs (<10 years) exhibit higher productivity growth, notably aged 6-9 years.
- A crucial finding appears to be the overall indication that the smaller self-employed and micro SMEs struggle to exhibit productivity increase when externally financed,

whilst older SMEs (20+ years) exhibit least impact where finance is received and externally financed larger SMEs (50-249) do not increase their productivity as much as their non-financed larger SME counterparts.

Productivity regression analysis

Overall, whilst the descriptive analysis demonstrated that access to external finance can lead to improved productivity and that access to regular and substantial amounts of external finance was associated with higher productivity, and conversely poor management resources such as fewer managers and poorer perceptions about accessing external finance are associated with lack of external finance and poorer productivity growth, these factors are overridden by three main factors: establishment age, size and the balance between employment and sales growth. SME resource issues such as business planning, use of specialist finance advice and better perceptions of ability to access finance are associated with improved productivity performance (or at least with mitigating against poorer performance).

RQ3 – What are the implications for theory and policy?

- Whilst external finance can assist SME growth and productivity growth, such impacts are highly nuanced, appear strongly related to the employment size (larger SMEs perform better), establishment age (younger SMEs perform better), and the lag between employment growth and productivity growth. Ongoing, more frequent use of external business/finance support services can improve performance.
- Policymakers should be cognisant of the difference in objectives between employment and productivity growth, given that shorter-term changes – captured in the current study – demonstrate that smaller SMEs struggle to deliver productivity change (as they may have to take on more staff to undertake R&D and develop new skills) whilst larger firms may offer more rapid productivity change through equipment and work practice efficiencies, but at the expense (at least in the shorter term) of job creation and permanent job status.
- The study demonstrates that business finance advice is a key to SME development and is a significant factor in enabling timely access to appropriate types of finance. However, SME finance advice is likely to be most effective when it is ongoing, regular and integrated with mentoring and management skills development. This can enable optimal financial investment and management activities. In turn, this will provide greater access to follow-on funding, growth and business sustainability.