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SMEs as Social Enterprises: Regional Disparities, Access to Finance, Strategic Intentions, and the COVID-19 Pandemic

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ABSTRACT

This report presents new findings regarding the social orientation, geographic distribution, outreach and financing of UK social enterprises. Using data from the 2016-2020 Longitudinal Small Business Survey, the report describes the key characteristics of social enterprises and compares these to those of commercial SMEs. We observe that SMEs that are: smaller; exhibit growth ambitions; located in non-urban areas; female-led; minority ethnic-led and operating in the social/services sector are more likely to be social enterprises compared to commercial SMEs. We also find that Scotland, Northern Ireland, Wales, North East of England, Yorkshire & Humber are the regions where social enterprises are more likely to be located compared to London. Social enterprises are more likely to rely on government and local grants as source of funding, but less likely to use bank overdrafts, loans from mainstream financial institutions and peer-to-peer platforms, equity finance, factoring and discounting relative to commercial SMEs. Finally social enterprises seem to have been resilient during the pandemic. Compared to commercial SMEs, we do not observe any differences in their perception of the COVID-19 pandemic as to be considered as *major* obstacle for their business and in fact we find some evidence suggesting that operations were increased. In terms of future plans, social enterprises' future plans to increase skills of the workforce and potential capital investments do not seem to have been affected by the pandemic when compared to commercial SMEs. This suggests a certain degree of resilience and ability to respond and adapt to new conditions following sudden and significant exogenous shocks.

NON-TECHNICAL SUMMARY ¹

Social enterprises are unique organizations pursuing *economic, social and environmental goals*. Their respective commercial activities intersect with the significant social and environmental challenges facing society today. This report uses the 2016 – 2020 Longitudinal Small Business Survey as a main data source, given that it offers a unique and detailed classification of SMEs based on their financial, social and environmental goals, and consequently allows for a clear identification of social enterprises in the context of the UK small business population.

¹ In this report we use the ONS Business Population Estimates to estimate the number of social enterprises. In 2017, there were 5,687,230 SMEs (0-249 employees) operating in the UK. In 2019, the total number of SMEs was 5,860,085 (0-249 employees).

This report presents new evidence regarding the key characteristics of SMEs that operate as social enterprises, allowing also for systematic comparisons with commercial SMEs in terms of social orientation, geographic prevalence, access to finance, and future strategic plans following the COVID-19 pandemic.

Section 1 introduces the key aspects of the report and structure. Following this, Section 2 offers a discussion of the recent developments in the UK SME market with a special focus on the role of social enterprises and relevant literature in this area. Section 3 describes the Longitudinal Small Business Survey in detail and the methodology used to identify social enterprises. Although this report focuses on social enterprises, we acknowledge the existence of diverse organizational forms within the UK ecosystem, including, traditional non-profit SMEs and socially-oriented SMEs which are closely related to social enterprises. Therefore, we also provide comparisons to commercially-oriented SMEs. Detailed descriptive statistics and empirical models used in the report are also presented in this Section.

Section 4 presents the key results of the study, which illustrate the importance of financial and social/environmental goals for the whole UK SME population, but also in terms of specific characteristics of social enterprises with respect to business size, location, industry, their financial performance, and major perceived obstacles to success. An extensive descriptive and econometric analysis leads to the following insights:

- Using the representative sampling of the LSBS and extrapolating to the UK small business population in 2019, around 2.9% of SMEs (approximately 170,000 SMEs) consider social or environmental goals as their only concern. 9.3% of SMEs (approximately 544,000 SMEs) consider these goals as their primary concern. 26.7% (approximately 1.5 million SMEs) consider them to be equal to financial or other goals, while 38% (approximately 2.2 million SMEs) consider them to be secondary to financial or other goals.
- In 2019, 8.2% of SMEs (approximately 480,000 UK SMEs) met the LSBS definition of a social enterprise. This is slightly higher than the reported figure of 8% (approximately 455,000 UK SMEs) for 2017.
- Around 71.5% of social enterprises are formed by firms with no-employees, followed by micro firms (22.1%), small (5.5%) and medium-sized firm (0.9%).
- England has the higher proportion of social enterprises (89.3%), followed by Scotland (4.8%), Northern Ireland (3.3%) and Wales (2.5%).



- The majority of social enterprises operate in the education, health and social work, arts and entertainment, and other services sectors (Sector classification - PQRS).
- A high proportion of social enterprises generated a profit/surplus over the last year.
- The proportion of social enterprises in 2019 indicating that the following factors are major obstacles to business success are: obtaining finance (23.4%); taxation (33.4%); staff and recruitment (31.7%); regulations/red tape (32.4%); availability/cost of suitable premises (18.2%); competition in the market (35.3%); late customer payments (22.6%); and the UK exit from the EU (17.1%).

Following this, the report focusses on identifying the most influential factors behind different types of SMEs, comprising commercial SMES, traditional non-profit, social enterprises and socially-oriented SMEs. The following findings emerged specifically for social enterprises:

- Social enterprises are more likely to have growth ambitions.
- Social enterprises are less likely to be located in non-urban areas.
- Female- and minority ethnic-led SMEs are more likely to be social enterprises.

In terms of regional and industry prevalence:

- The North East of England, Northern Ireland, Wales, Yorkshire & Humber, and Scotland have a higher probability of hosting social enterprises compared to London.
- Within England (and relative to London as a reference category) and based on Local Enterprise Partnerships (LEPs); the Tees Valley, Worcestershire, Heart of the Southwest, York and North Yorkshire, Gloucestershire and Coventry and Warwickshire are more likely to have social enterprises.
- Social enterprises are more likely than commercial SMEs to be operating in social and service sectors compared to the production and construction sector.

In terms of access to finance, our main results for social enterprises suggest:

- Social enterprises are less likely to use bank overdrafts, equity finance, leasing and hire purchase, loans from a bank, building society or other financial institution and loans from peer-to-peer platforms compared to commercial SMEs.
- Social enterprises are more likely to use government or local authority grants as source of funding compared to commercial SMEs.



- Relative to commercial SMEs, social enterprises are less likely to apply for funding from commercial banks. However, social enterprises are more successful in securing funding via loans and credit cards compared to commercial SMEs.

Finally, in terms of strategic future intentions in the context of the COVID-19 pandemic, our results suggest that:

- Disruptions brought about by the COVID-19 pandemic and resultant government restrictions on trading are not perceived as a major obstacle to business success for social enterprises compared to commercial SMEs.
- Operations of social enterprises were increased during the lockdown restrictions compared to commercial SMEs.
- In terms of future plans, social enterprises' future plans to increase skills of the workforce and potential capital investments have not been affected by the pandemic when compared to commercial SMEs. This suggests preliminary evidence of a degree of business resilience and ability to respond and adapt to new conditions following sudden and significant exogenous shocks.

This report informs key stakeholders, government bodies and third sector on recent developments of social enterprises in the UK, and thus provides a basis for future in-depth discussions regarding specific policies to support the viability of these organizations and their actual and potential contribution to the society.

