

## Policy Briefing

# Exploring External Finance to Build Back Better a Green UK SME Economy

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This paper outlines key findings and policy implications from research exploring the link between external finance and SMEs becoming 'green' i.e., having a 'green mission' and adopting energy efficiency practices. The research was based on econometric analysis of data from the Longitudinal Small Business Survey (LSBS survey 2020, 2019 and 2017 waves), and builds on Cowling and Lui's (2021) work on Access to Finance for Cleantech Innovation amongst UK SMEs.

'Green mission' refers to self-reported importance of environmental issues and goals for SMEs. Improving energy efficiency refers to taking actions in the 12 months prior to the survey (e.g., installing a smart meter, improving insulation). The focus of the analysis was on identifying characteristics that were linked with a higher likelihood of being 'green'.

### Key findings

- Green SMEs make more use of external finance than their non-green SME counterparts and access a wider range of finance options.
- **SMEs that use government grants and loans are strongly linked to being green.**
- Green SMEs tend to be established (at least six years old), have more employees, and are concentrated in environmentally regulated sectors (e.g. primary, construction, manufacturing and retail).
- Green SMEs are more likely to be located in rural areas and greener UK regions i.e., those with a higher ratio of installed renewable capacity to GVA.
- Green SMEs are more likely to introduce new products and/or services; but are (at best) as likely to generate turnover growth or profits.
- Green SMEs tend to provide more external training to employees and are more likely to be ethnic minority-led.
- Almost half of SMEs are still unaware of government energy efficiency schemes, particularly smaller firms. However, there is a positive trend between 2019 and 2020, the proportion of business that were unaware of any such schemes decreased from 67% to 45%.
- Businesses in rented premises are less likely to undertake green energy efficiency measures, probably because this is under the control of their landlords.

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## Policy implications

**Recommendation 1.** There is a lack of consistency in data collection in LSBS on greenness of SMEs which limits further analysis. We recommend widening the survey to include questions exploring SME motivations and green actions including the adoption of innovative green business models and approaches. Crucially, the questionnaires should be kept consistent between LSBS waves to enable ‘deeper’ longitudinal analysis at the business level. An increase in the scale of the LSBS survey (at least to include full wave, rather than partial cohort data for energy efficiency practices) would enable improved analysis of external financing requirements.

**Recommendation 2.** The evidence suggests limited financial incentives for business to go green, however using government grants and loans is associated with being green. Therefore, consideration should be given to developing appropriate financial support mechanisms to incentivise and encourage SMEs going green, particularly for laggard SMEs. This may come in the form of grants, soft loans with low interest and repayment holidays, or other forms of inducement such as improved energy feeder tariffs, green R&D tax credits etc. Developing a clear and accepted definition of green SME will be required.

**Recommendation 3.** To address the *prisoner* effect of SMEs in rented accommodation who are unable to undertake energy efficiencies, government should give greater attention to landlord incentives and aggregating schemes to incentivise landlords and SMEs to work together to achieve green solutions.

**Recommendation 4.** Considering the relatively low (albeit improving) SME awareness of government energy efficiency schemes, there is further work to be done in increasing knowledge and understanding of support to meet Net Zero ambitions. Development and provision of widely accessible universal online support tools to nudge and assist SMEs to become greener is urgently required. For example, SME Net Zero champions could act as role models and mentor fellow SMEs on the way forward.

Full paper link:

<https://www.enterpriseresearch.ac.uk/our-work/publications/>