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EXECUTIVE SUMMARY

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The impact of flexible work on SME Performance: An analysis of flexible working arrangements, innovation and productivity in Scotland

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One out of three jobs currently advertised in Scotland offers flexible working (Timewise, 2023) and recent legislation — the Employment Relations (Flexible Working) Act 2023, effective from April 6, 2024 — grants employees the right to request flexible working from day one in a new job. This new legislation highlights the increasing demand for flexible work arrangements (FWAs), addresses the recruitment difficulties due to an increased level of economic inactivity post-pandemic, offers the possibility of a better work-life balance to workers while adapting to their needs, and potentially improves productivity and innovation as several studies have found around the world. However, the factors behind FWAs adoption and its impact on business performance for small and medium enterprises (SMEs) in the UK remain underexplored. Drawing on data from Scottish SMEs in the Longitudinal Small Business Survey (LSBS) between 2015 and 2022, this report provides a comprehensive evidence-based analysis of the determinants of FWAs adoption and its relationship with SME productivity and innovation. We do this by investigating both any FWAs as an aggregate and disaggregating FWAs into eight distinct types (flexitime, annualised hours contract, term-time working, job sharing, nine-day fortnight, four-a-half-day week, zero hours contracts and on-call working) in addition to a ninth type comprising any other flexible working hours arrangement. In modelling productivity and innovation, we control also for a set of other business characteristics like sector, age, location in rural areas, female ownership, exporting status, plans for the future and major obstacles to business success allowing a rich analysis of Scottish SMEs behaviour.

It is found that, overall, three out of four Scottish SMEs with employees offer some form of flexible working arrangements. The type of contract more likely to be adopted is flexitime, or flexible working hours, offered on average in the period 2015-22 by more than two out of three FWAs firms, and just over half of all Scottish SMEs with employees.

Other key findings reveal that innovation plays a crucial role in the adoption of FWAs among Scottish SMEs. Firms characterised by innovative practices are more likely to adopt flexible arrangements, such as flexitime and alternative work schedules. Additionally, the adoption patterns of FWAs vary across sectors. The primary and the construction sectors are less likely to offer any type of FWAs, while ITCs and the professional and scientific sector are more likely to offer flexitime, the hospitality and the healthcare and social sectors are more likely to offer zero-hours contracts, in the education sector term-time work is more prevalent and in the administrative and support services sector there is a higher chance of finding on-call working arrangements. Some of these sectoral differences in the adoption of FWAs are related to the

different prevalence of females working in them, as female-dominated roles are more prone to be offered flexible work contracts (Timewise, 2023). Location seems to matter for on-call working which is more likely to be offered by SMEs in rural areas. Also, business size matters for the adoption of FWAs. Medium-sized firms exhibit a stronger preference for FWAs. This indicates that policy initiatives should particularly target smaller firms to maximise the benefits associated with flexible work. We also shed some light on the differences in adopting two types of contracts used by businesses to manage their variability of demand for labour: on-call working and zero-hours contracts.

Considering SME productivity, the results indicate that the overall adoption of FWAs does not have a statistically significant impact on labour productivity, except for the nine-day fortnight working, which is positively associated with improved productivity and statistically significant, but it is also the least used flexible work contract among those adopted by SMEs.

Regarding innovation, we consider both actual innovation in the previous three years and the intention to innovate in the following three years. Our analysis shows that SMEs offering flexible working arrangements, particularly flexitime, are more likely to report innovation. This supports the argument that flexibility fosters a creative environment, enhancing product and process development as found in the literature. The results also indicate that different types of FWAs contribute to the intention to innovate, particularly flexitime and term-time working contracts. These findings highlight how flexible work models can be a win-win arrangement for workers and the firm, stimulating innovation plans and activities that help the firm compete and stay in the business.

Finally, we provide some policy implications of these novel findings in the UK context and suggest future research directions.