Institute for Public Policy Research

PERSPECTIVES ON SMEs AND PRODUCTIVITY IN THE NORTHERN POWERHOUSE

FINAL REPORT

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SUMMARY

By international standards, the UK's post-recession productivity performance has been poor. This 'productivity problem' is particularly acute in the north of England, and for the smaller businesses that make up over 99 per cent of the northern business population. Boosting the productivity of small businesses in the Northern Powerhouse could add as much as £23 billion per annum to the economy.

Policy for productivity must target both advanced industries and high-tech sectors, as well as the 'everyday economy' in which many small and medium-sized enterprises (SMEs) provide employment and support communities and places. This is important if productivity gains are to translate into higher wages and better living standards.

Northern SMEs are not a homogeneous group. They need support that is tailored to their local contexts and individual needs. This means strategically coordinated opportunities that are rigorously assessed for efficiency, relevance and effectiveness, delivered by experts and well-resourced. Signposting services are also essential to allow busy SME leaders to navigate what is inevitably a complex landscape.

SMEs need support to help them respond to wider challenges and opportunities in the UK economy. These include:

- skills shortages and models for skills provision
- connectivity: physical and digital
- the cost of running a business
- Brexit.

Business support should also make sure that SME leaders can apply well-evidenced productivity-boosting measures to their specific contexts and needs, such as:

- high-quality management and leadership skills
- digital and technological development, supported by appropriate employee skills
- innovation, both sector-specific and generic; this is relevant both to high-tech and advanced businesses and right across the 'everyday economy'
- opportunities for exporting and internationalisation
- employee health and wellbeing.

Funding for business support in recent years has been very modest, and may be further reduced as the UK loses access to key EU sources. In addition, the business support landscape is highly complex, and businesses' trust in the quality and relevance of some provision is cautious. Much support, including access to finance, is targeted at a small subset of 'high growth' businesses, meaning that SMEs which add different kinds of value can miss out on opportunities to grow and to work productively.

We recommend the following measures to boost northern SME productivity.

1. Funding should be increased for the British Business Bank and the Northern Powerhouse Investment Fund, commensurate with the size of the northern SME population and the potential gains from increased productivity. In the long-term, this should be developed into a full-scale regional investment bank structure.
2. Support for businesses that add value in ways other than 'high growth' should be improved, and small-scale support should be made more accessible.
3. Government should create long-term financial settlements for LEPs to fund growth hubs, increasing funding from £12 million per year to £60 million per year. Growth hubs should take on strategic responsibility for shaping local support landscapes.
4. Support should prioritise areas that are proven to support productivity, including management and leadership training and digital skills development. This should include face-to-face support and mentoring.
5. Northern Local Enterprise Partnerships should consider increasing small business representation in their decision-making.
6. Universities should be funded to develop and extend current good practice in knowledge transfer (to advanced *and* everyday sectors) and skills support, in ways that are relevant to SMEs.
7. Government should commit to a full redesign of business rates, alongside a review of how local government is funded.

INTRODUCTION

In the interim report of this project, we set out how the UK's 'productivity challenge' affects small businesses in the north of England. We found that:

- productivity among small and medium-sized enterprises (SMEs) in the North lags that of southern small businesses
- raising the productivity of northern SMEs to match the national average would be worth approximately £23 billion per annum, representing a 7.5 increase in northern GVA.

This report considers the role of business support for SMEs in the north of England. We explore the characteristics of SMEs and the barriers that they might face to improving their productivity. We outline the current landscape of support that is provided at both a national and local level, and set out recommendations for central and local government proposing how this might be developed and improved in order to boost the productivity of small firms throughout the Northern Powerhouse.

The government provides and funds a range of support for small firms. This includes both financial support such as loans and grants and non-financial support and advice on how to run a business through mentoring or consultancy, or help with specialist activities such as government procurement. Support is often, although not always, provided through a third party. Chapter five provides an appraisal of the current business support landscape.

In the north of England:

- 99.8 per cent of all businesses have fewer than 250 employees
- 21 per cent employ between one and nine people
- 74 per cent are 'sole traders'.

Like SMEs across the UK, these businesses tend to have lower rates of productivity than larger firms; companies that employ fewer than 10 people lag behind the national average rate of productivity by between 15 and 27 per cent.

The report is structured as follows.

Chapter 1 outlines the nature of the UK's productivity puzzle, and the role of SMEs in the north of England in relation to this.

Chapter 2 draws on learning from our fieldwork to outline a profile of small businesses in the North.

Chapter 3 explores the wider and structural factors that impact on SME productivity in the North.

Chapter 4 explores the firm-level factors that affect SME productivity.

Chapter 5 briefly describes the current landscape of business support, and current issues with it identified through our fieldwork.

Chapter 6 sets out our recommendations.

Research methods

We were keen to engage with expert stakeholders in the north of England, and to reflect their experiences and views. This report draws on findings from the following qualitative and quantitative data gathering and analysis.

- Two focus groups with SME leaders in the north of England.
- 12 interviews with expert stakeholders who work with SMEs on a day to day basis. This group included senior staff from the region's chambers of commerce, universities and local enterprise partnerships, the Federation of Small Businesses and Be the Business.
- A survey of SMEs in the north of England, to gauge their business ambitions, their support needs, and their hopes and fears for the future. A summary of key findings from the survey is included in chapter 2. The full breakdown of survey results is included alongside this report.

What is an SME?

The term 'small and medium-sized enterprise' (or 'SME') refers to companies with fewer than 250 employees. Because the experiences of businesses at different points on this scale vary quite considerably, SMEs are sometimes broken down further into:

- **micro-enterprises** with 0–9 employees
- **small enterprises** with 10–49 employees
- **medium-sized enterprises** with 50–249 employees.

There is some overlap between the category of 'micro-enterprises', sole traders, and the self-employed. Distinctions between these groups are not relevant to the main discussions in this report. For the most part, we focus on the needs of entrepreneurs who elect to manage their work as a business rather than a freelance endeavour. In addition, the position of people who are technically self-employed but whose working life in many ways resembles that of an employee (Taylor 2018) is not explored in this project.

1. SMEs AND PRODUCTIVITY: THE PROBLEM AND THE POTENTIAL

1.1 PRODUCTIVITY IN THE UK

The productivity of an economy is the relationship between its inputs and its outputs; how much value is generated for every hour worked? Productivity measures demonstrate the return on the resources that go into producing goods and services. One way to understand productivity is to think of it as the 'miles per gallon' that a company or an economy achieves. Another is to think of it as the scope that is available for raising living standards and making investments – two processes that are vital for an economy that is both prosperous and fair.

At firm level, SMEs generally have lower rates of productivity than larger businesses (see figure 1.2). However, they account for a large proportion of the economy, contributing around 52 per cent of private sector turnover in the north of England. Therefore, focussing on the specific issues that could increase productivity for smaller firms has the potential to make a major difference to productivity overall (as discussed above). In this report we consider how a reformed framework of business support at the regional level can support improved productivity in northern SMEs.

How is productivity calculated?

Productivity is defined as the *output* of a production process in relation to *inputs*. A wide variety of different inputs contribute to most production processes, and so methods for calculating productivity vary depending on which inputs are considered.

$$\textbf{Productivity} = \frac{\textbf{Outputs}}{\textbf{Inputs}}$$

It is not possible to observe productivity directly, and so most productivity measures are **derived statistics**, using different measures of inputs and outputs. Commonly used measures include:

- **total output:** the value of goods and services produced
- **gross value added (GVA):** the difference between the value of goods and services produced (total output) and the cost of raw materials and other inputs that are used up in production (intermediate consumption)
- **gross domestic product (GDP):** total economic activity – this may be measured as **production** (the sum of all the gross value added by all producers in the economy), **income** (total income generated through this productive activity), or **expenditure** (total expenditure on goods and services produced).

Because the key input into the production process is **labour**, many accounts of productivity refer to **labour productivity**, or the quantity of goods and services produced per unit of labour input. Labour input can be measured as the number of **jobs**, the number of **workers**, or the number of **hours worked**.[1]

Multifactor productivity is calculated using estimates for all inputs, including labour, capital, physical elements such as machinery or equipment, and intermediate inputs (OECD 2001). **Resource** productivity is “the efficiency of using natural resources to produce goods and services within the economy”; improving resource productivity can have a positive impact on GDP, and high resource productivity may also be linked to high employment (Stocker et al 2015).

Because regional data for the UK is largely calculated in terms of **labour productivity**, this is the measure used here unless otherwise stated. In general, where other measures are used, this is because labour productivity data is not available for the selected issues/geographies. However, in general, patterns will be broadly similar because of the importance of labour as an input factor.

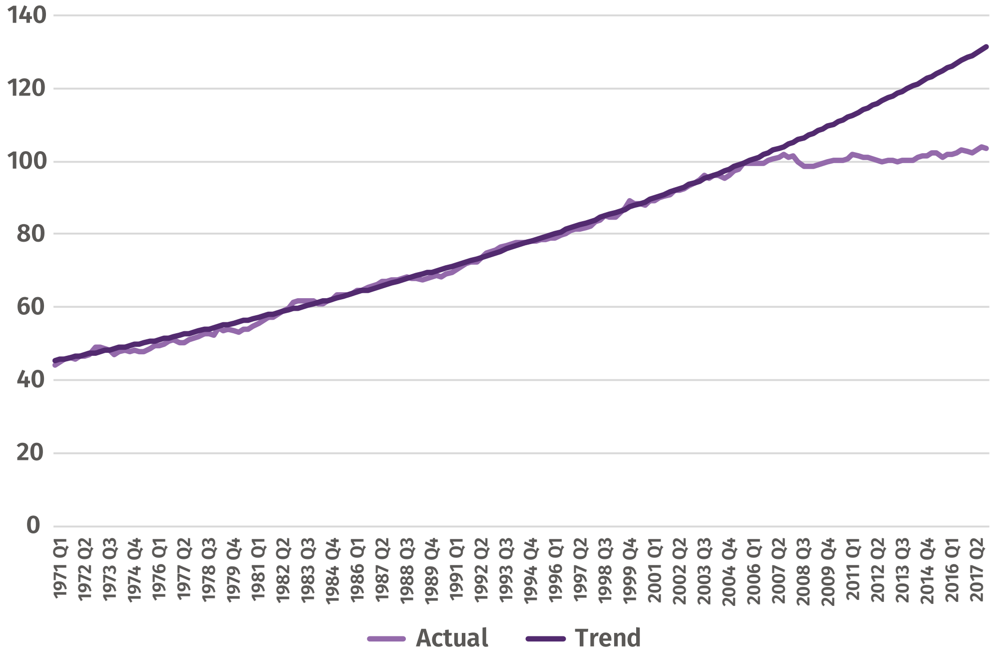
The UK faces three key challenges in relation to productivity.

The first is **a near-halt to productivity growth**, which has stalled since the financial crisis and failed to match pre-recession rates (figure 1.1; for discussion see McCann 2018 and Harari 2017). This follows a history of relatively ‘disappointing’ productivity performance over several decades (Crafts 2019). The rest of the developed world has seen similar patterns but they are markedly more acute in the UK (Wren-Lewis 2017).

1 Based on ONS 2016.

FIGURE 1.1

UK productivity growth since the 2007/08 financial crisis

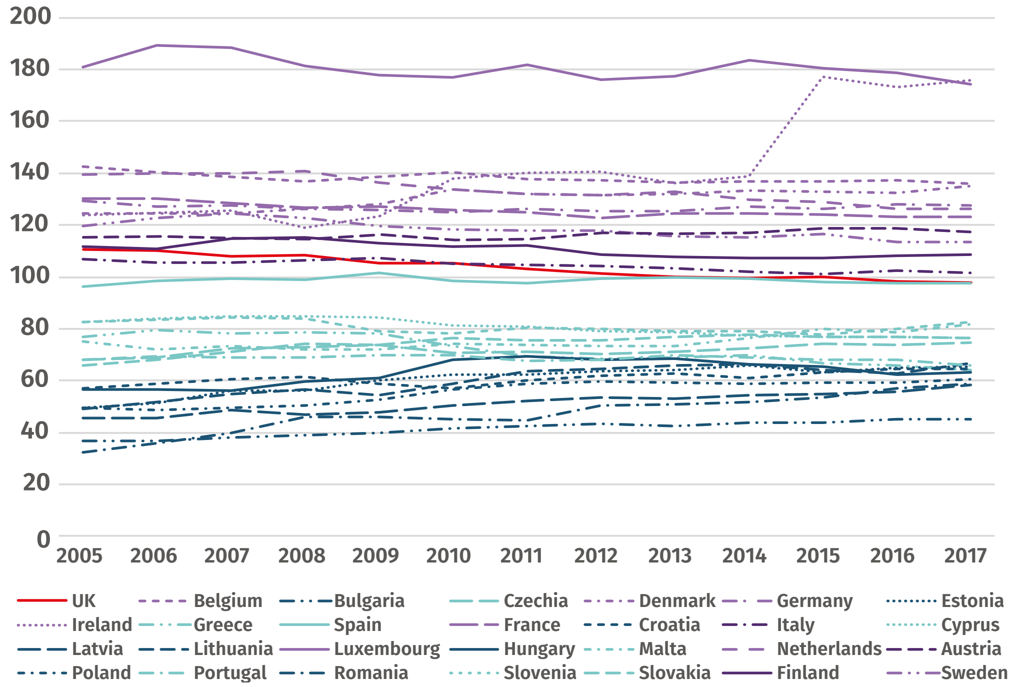


Source: IPPR analysis of ONS 2018g

In addition, both productivity levels and rates of productivity growth lag behind those of comparable developed countries. UK productivity was just below the EU average in 2017, falling from around 8 percentage points above in 2007 (figure 1.2). It lagged behind the G7 average by around 18 percentage points in 2006 (figure 1.3).

FIGURE 1.2

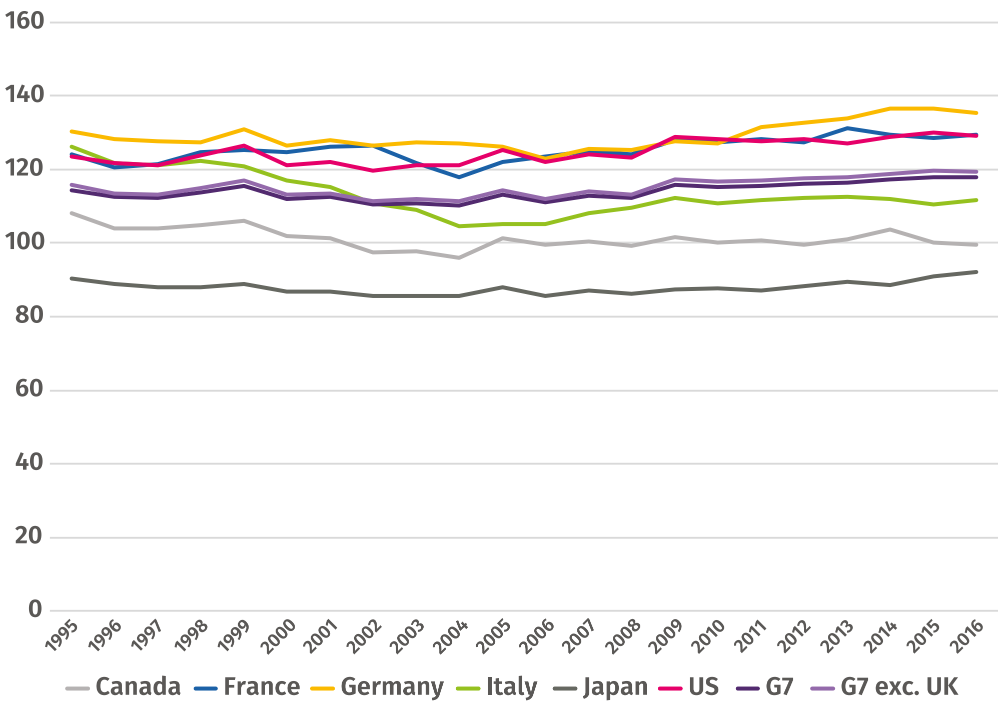
Nominal labour productivity per hour worked, EU (indices: EU28=100)



Source: Eurostat 2018

FIGURE 1.3

Current price GDP per hour worked, G7 nations (indices: UK =100)

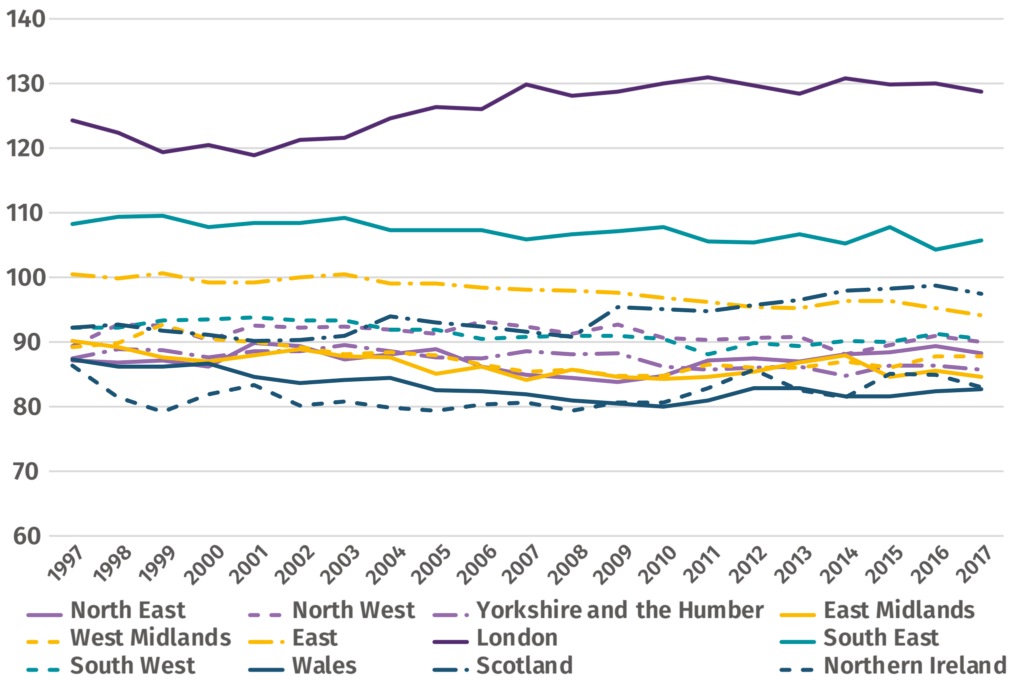


Source: ONS 2018a

Finally, the UK has long-standing and stark regional imbalances in productivity (figure 1.4; for discussion see Gal and Egelund 2018). These regional disparities are extreme by the standards of most other OECD nations (Coyle and Sensier 2018), and have changed relatively little since the recession.

FIGURE 1.4

Output per hour at current prices, UK nations and regions (indices: UK=100)



Source: ONS 2019a

Explanations of these trends are numerous and somewhat disputed (Gelauff et al 2008), presenting a 'productivity puzzle' whose sources are complex and intractable. In fact, the UK's levels of openness and connectivity are such that, if general global trends applied, productivity would be around 18 per cent *higher* than it is in reality (Haldane 2018). Economic modelling suggests that Brexit will have a negative impact on productivity, as a result of skills shortages and lower levels of competition and innovation; over the long term this might amount to a fall of between 1 and 1.6 per cent compared to a remain scenario (Hantzsche et al 2019).

In a review of *Eight Decades of Productivity Analyses*,[2] McCann (2018) traces the history of productivity studies and shifting assumptions about key drivers and risks. Prominent among these are the rising importance of access to knowledge and concentrations of knowledge; patterns of trade and globalisation; and the context of governance, politics and policy.

McCann's review proposes the following explanations of the UK's poor productivity performance.[3]

2 This document was produced for the 'Productivity Insights Network' (PIN 2018). Launched in 2018 and funded by the Economic and Social Research Council, this brings together experts from eight universities across England, Scotland and Wales along with an expert economic consultancy to develop new insights into the UK's productivity issues.

3 Adapted from McCann 2018.

- Low levels, per capita, of technology, research and development investment, skills training and advanced capital.
- Moderate to average levels of knowledge-investing and innovation dynamism, by comparison with OECD and EU competitors (which may have been masked for a decade pre-crisis by growth in financial services).
- Poorer quality management in many firms than is the case in competitor countries.
- Lower stocks and flows of human capital than in countries such as the US, and a recent marked fall in labour market churn.
- A trend, especially during a period of economic and political uncertainty, towards taking on more workers or increasing working hours rather than investing in technology or new business practices.
- Slow average rates of technology adoption (despite some very high performers), particularly since the recession.

Across these trends, the UK's productivity suffers from "the apparent deterioration or stalling of... knowledge diffusion and knowledge absorption processes". This 'stalling' is widespread, save at the 'technological frontiers' and in all but the most productive sectors and regions (McCann 2018).

In summary, productivity is driven partly by macroeconomic factors in the national and global economy which are outside the control of individual businesses and their leaders. However, within this context, individual businesses can act to improve their productivity. This, in turn, can generate the resources to raise wages and living standards.

In the next section, we consider how national productivity challenges play out for SMEs in different regions and sectors.

1.2 THE 'LONG TAIL' OF PRODUCTIVITY: FIRM SIZE AND SECTORAL TRENDS

Many analyses point to a 'long tail' of firms whose poor productivity lowers the overall average, despite a number of companies that perform well (Haldane 2017). This tail that includes many SMEs. Figure 1.5 illustrates recent trends in the distribution of firm-level productivity for firms of different sizes.

These figures show that a higher proportion of large businesses fall into the higher productivity categories, but also that it is possible for smaller businesses to achieve high rates of productivity. This is particularly true of medium-sized businesses; their density at the higher end of the productivity distribution is similar to that of large businesses. The lowest density of highly productive businesses is seen among those with 10–49 employees.

FIGURE 1.5

Distribution of real firm-level productivity by firm size band (less productive firms appear in the left-hand tail)

Source: ONS 2017a

While micro and small businesses have consistently had lower rates of productivity, the fall associated with the 2008 recession was less marked for these businesses than for larger organisations, and the smallest businesses have seen a stronger recovery. Over the same period, medium-sized enterprises have slightly higher productivity than large ones (figure 1.6).

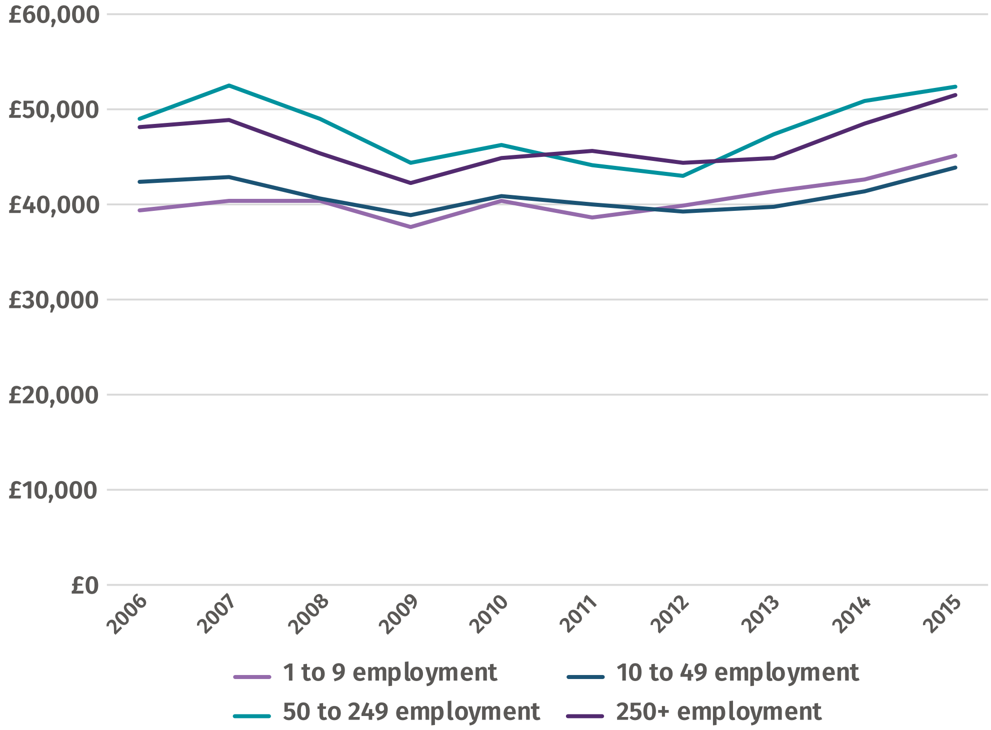
The very end of the 'long tail' – or the least productive 10 per cent of businesses – includes a disproportionately large number of micro-enterprises; they make up 91 per cent of this 'laggard' group compared to 88 per cent of the whole business population. However, size alone does not explain their poor productivity performance, and their presence in this least productive 10 per cent of firms fell slightly over the past decade. Very low productivity companies also include (ONS 2017a):

- a low proportion of knowledge-intensive services firms[4]
- a high proportion of businesses in low-knowledge-intensive services, with the distribution, hotel and restaurant industries accounting for around one-third of the group (an increase from just over one-fifth in 2003)
- a higher proportion of businesses based in Yorkshire and the Humber, the North East and Wales than the business population as a whole
- a higher proportion of 'young' companies that have been trading for less than five years
- single-site businesses.

4 Knowledge-intensive services firms are those in service sectors with a high share of employees educated to a university level. For a list of sectors see: https://ec.europa.eu/eurostat/statistics-explained/index.php/Glossary:Knowledge-intensive_services_(KIS)

FIGURE 1.6

Gross value added (GVA) per worker by firm size



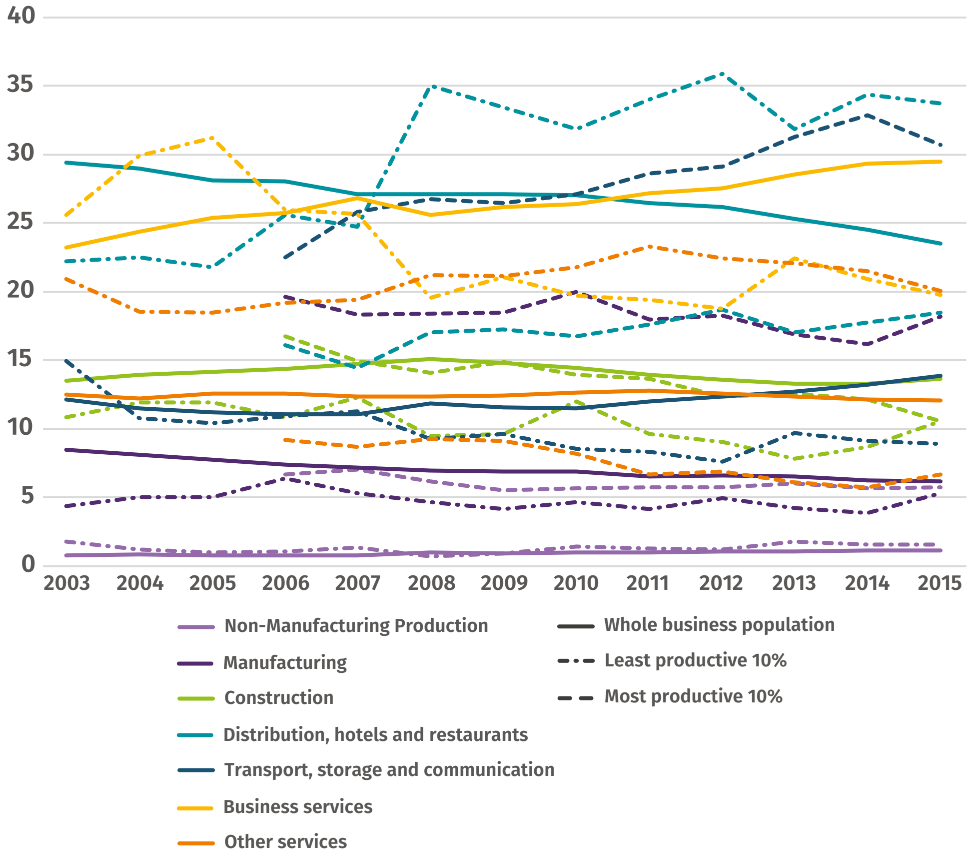
Source: ONS 2017b

Figure 1.7 shows the proportion of businesses from different sectors in the highest and lowest 10 per cent of firms for productivity, and in the general business population.

Some analyses argue that sectoral differences explain much of the productivity gaps between the UK and other nations. A country with a high proportion of firms in low productivity sectors will have lower average productivity. However, other commentators (such as IPPR 2018; Dolphin and Hatfield 2015) suggest that, in fact, the UK's productivity performance is generally lower than average in both low *and* high productivity sectors, despite the strong performance of a number of firms that hold their own internationally (figure 1.8; for caveats relating to these figures please see ONS 2017e). Sectoral differences arise both because of global trends and how these operate in national contexts, as well as factors that affect individual sectors (see Riley et al 2018 for discussion).

FIGURE 1.7

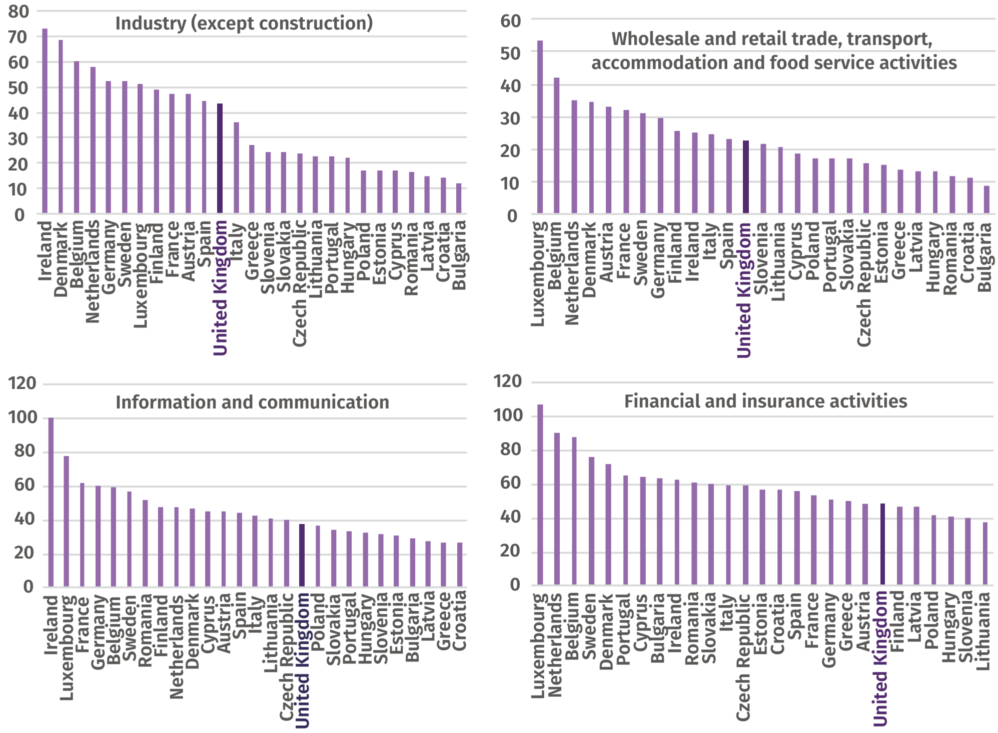
Proportion of firms from each sector in the highest and lowest 10 per cent of firms for productivity and in the general population



Source: ONS 2017a and 2017b; authors' analysis

FIGURE 1.8

Output per hour worked, selected industries, EU (€)



Source: ONS 2017c

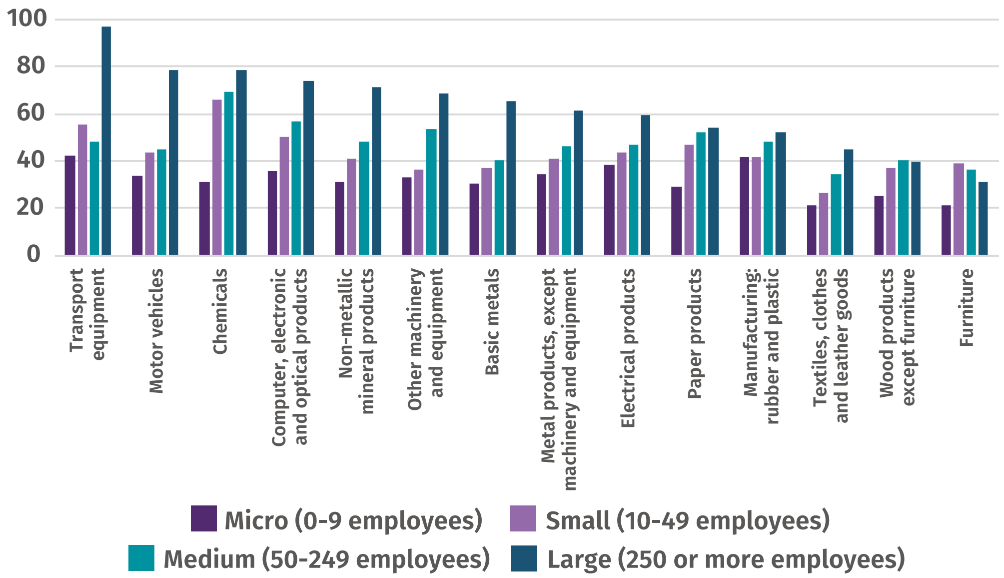
Within sectors, average productivity varies considerably for firms of different sizes. Figure 1.9 shows the median productivity for micro, small, medium and large-sized businesses in different sectors across the UK.

In manufacturing, median productivity is higher in large companies than in small or medium-sized ones. This is very marked for advanced manufacturing sectors, such as transport equipment, motor vehicles, chemicals, and computer and electronic equipment. However, the gap between firms of different sizes is smaller in most areas of manufacturing other than advanced and high-tech.

The 'large company advantage' in productivity is also marked in some areas of knowledge-intensive services, but it is by no means universal. In telecommunications, information services and computer programming, the most productive firms are also the largest. However, in architecture and engineering, the difference is fairly small. Across other sub-sectors, the most productive firms are those in the small or medium brackets. Microbusinesses tend to have the lowest median productivity.

FIGURE 1.9A

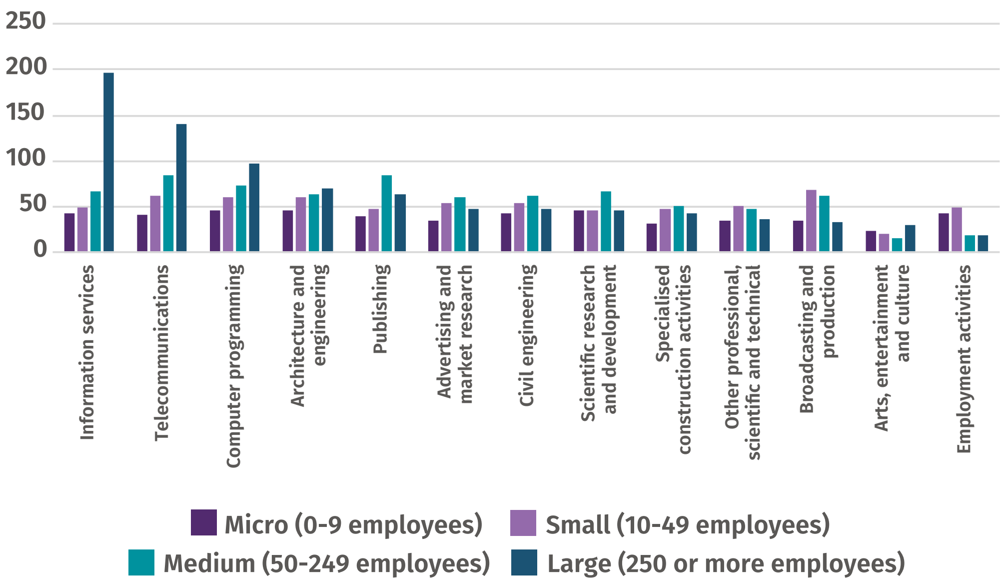
Median labour productivity by manufacturing sub-sector, employment weighted, constant price, 2017 (£000 per worker)



Source: ONS 2019b

FIGURE 1.9B

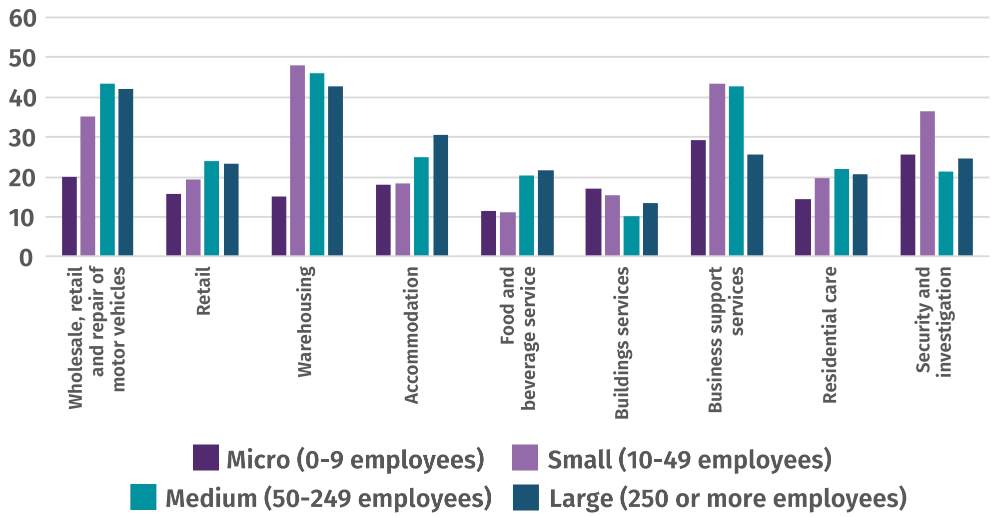
Median labour productivity by knowledge-intensive services sub-sector, employment weighted, constant price, 2017 (£000 per worker)



Source: ONS 2019b

FIGURE 1.9C

Median labour productivity by non-knowledge intensive services sub-sector, employment weighted, constant price, 2017 (£000 per worker)



Source: 2019b

The picture is mixed for non-knowledge intensive services. Large companies are the most productive in accommodation and food services, although – as noted above – their overall productivity is relatively poor. However, in retail, motor vehicle sales and repair and residential care, medium-sized businesses have the highest median productivity. And small firms are the highest performers in a further set of sub-sectors such as warehousing and business support services.

In the next section, we examine the SME population of the north of England.

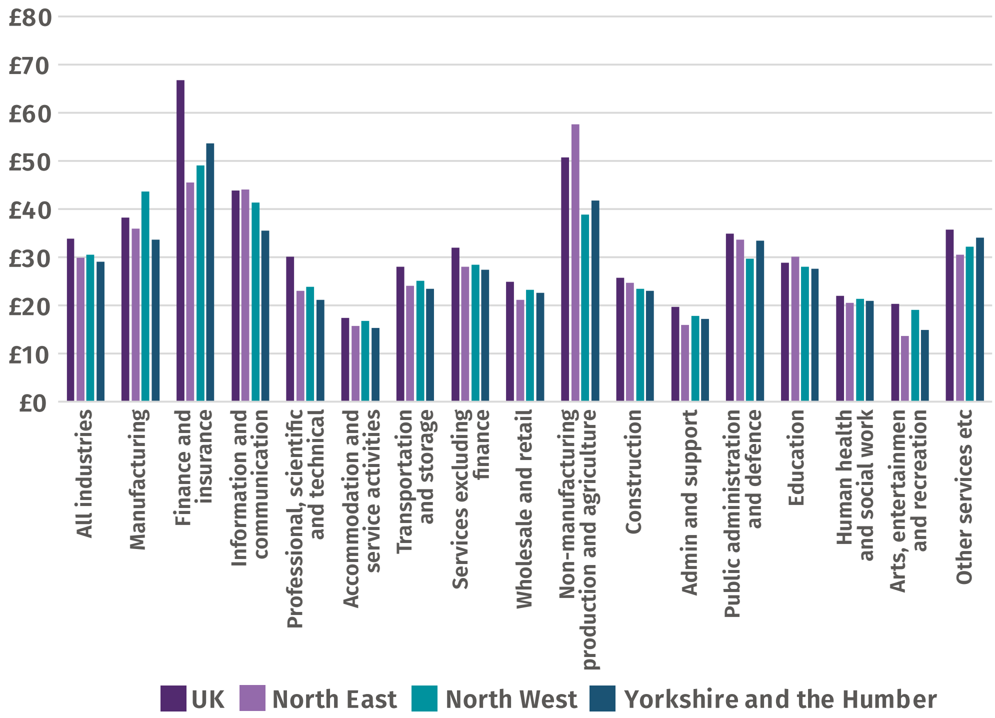
1.3 HOW PRODUCTIVE ARE SMES IN THE NORTH?

The productivity of different sectors varies markedly across the UK (figure 1.10), with productivity in the North generally, although not uniformly, lower than the national average. Some examples that illustrate this include the following.

- The North lags behind national productivity rates by a substantial margin in finance and insurance and in professional, scientific and technical businesses.
- The North lags behind national productivity rates by a smaller margin in various non-knowledge intensive services, transportation and storage, and wholesale and retail.
- In a number of sectors, certain northern regions perform well or even outperform national rates. For example:
  - the North West outperforms the UK average in manufacturing
  - the North East matches the UK average in information and communications
  - in human health and social work, productivity in the North is close to the UK average.

FIGURE 1.10

Output per hour (£), UK and northern regions, 2017



Source: ONS 2018c

However, these contrasts do not appear to reflect the internal composition of these sectors within the north of England. For example,[5] in the North West – where manufacturing productivity is above the UK average – the proportion of businesses engaged in transport equipment and motor vehicle manufacturing is slightly *lower* than it is across the UK (at 4.67 per cent of all business compared to 4.88 per cent), and the proportion of large manufacturing businesses in this sector is also lower (at 0.7 per cent of all business compared to 0.13 per cent). The proportion of North West firms engaged in manufacturing chemicals and pharmaceuticals is slightly above the national average (4.63 per cent compared to 3.76 per cent) but a relatively high proportion of those are micro-enterprises (2.91 per cent compared to 2.83 per cent).

It is true that, in some sectors where the North does comparatively well, it has a smaller proportion than the national average of companies of all sizes. For example, a smaller proportion of businesses in the North East than elsewhere fall into its high-performing information and communications sector – a total of 4.7 per cent, of which the majority are microbusinesses. Nationally, 7.8 per cent of all businesses belong to the information and communications sector. In the North West and Yorkshire and the Humber, 5.8 and 5.4 per cent of businesses fall into this sector, with the vast majority of those having just 0–9 employees.

At the less productive end of the spectrum, the North does have a slightly higher proportion of smaller firms in unproductive sectors. For example, 8.6 per cent of firms in the North East are in the accommodation and food services sectors, compared to 5.8 per cent nationally, 7 per cent in the North West and 6 per cent in Yorkshire and the Humber. And these firms are generally smaller: in the North East

5 All figures in this discussion are derived from ONS 2017d (authors' calculations).

6.6 per cent of firms are microbusinesses engaged in food and accommodation services, compared to 4.7 per cent in the North West, 5.5 per cent in Yorkshire and the Humber and 4.3 per cent nationally.

Overall, this confirms the view that sectoral mix is less important than trends within firms themselves (see ONS 2018b). A recent study found that firms of a similar size, sector and age in the North are less productive overall than comparable enterprises in London and South East (Tiwasing et al 2019). This may reflect local conditions, trading conditions, support and opportunities, as well as business clustering and infrastructure; for example, the North East's strong performance in information services could reflect the presence of a small number of global corporations, outstanding university departments, and strong informal networks (see Longlands et al 2018). For these reasons our recommendations include provision for a high degree of tailoring of business support to regional and firm-level contexts.

In chapter 2, we consider the reflections of individual SME leaders and experts on the experience of being a northern small business.

2.
CHALLENGES AND OPPORTUNITIES FOR NORTHERN SMEs

2.1 A PROFILE OF SMES IN THE NORTH

Small and medium-sized enterprises (SMEs) are the backbone of the Northern Powerhouse economy. As noted in the interim report of this project, SMEs make up over 90 per cent of its private sector business population, contributing hugely to employment, prosperity and innovation. In addition, small businesses play an important part in community cohesion and resilience (Steiner and Atterton 2014; Hunter 2019). Studies of entrepreneurial motivation show that community objectives and other non-economic outcomes are often as important as financial ones, if not more so (Douglas and Prentice 2019; Randolph et al 2019). The North needs a productive SME sector to support prosperity, raise living standards, and strengthen its places.

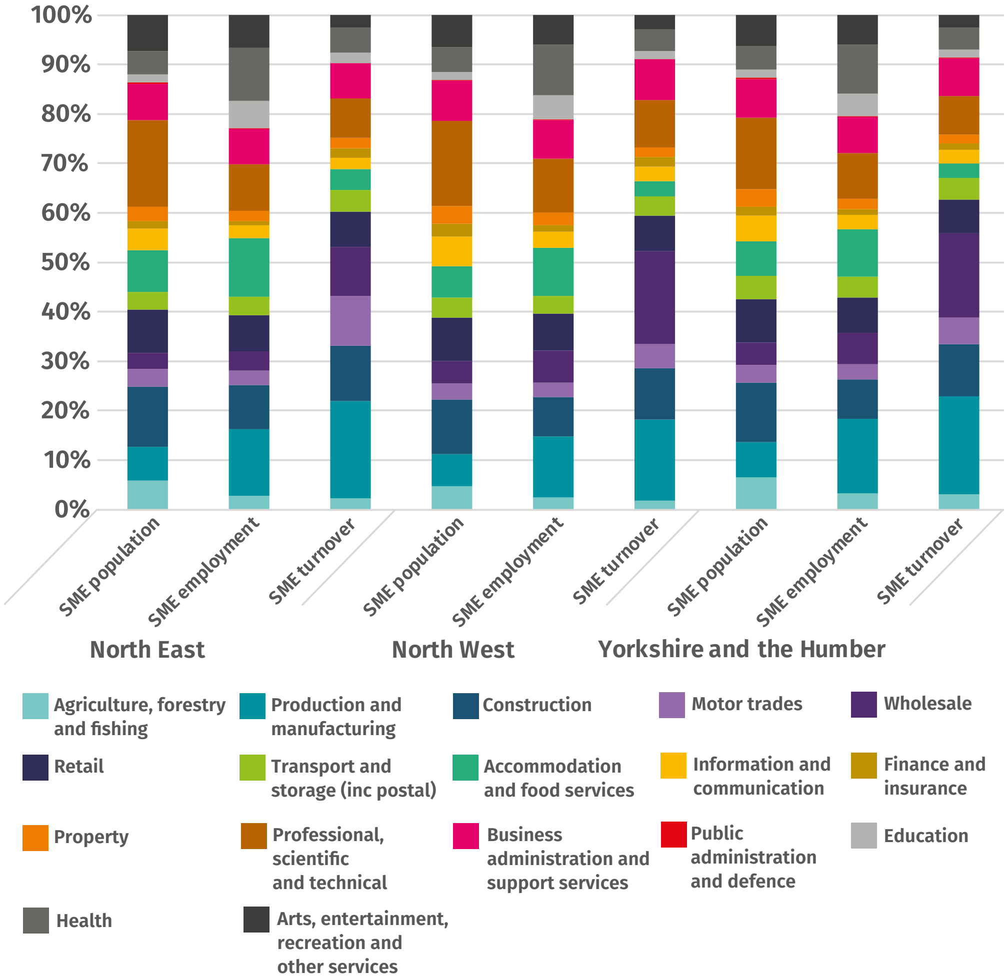
Figure 2.1 shows the composition of the SME population, employment and turnover in the northern regions of England. This varies considerably between the three main regions, and indeed there are even greater variations at the local level. For example, in the most rural areas almost 40 per cent of SMEs operate in agriculture, forestry and fishing; in others, manufacturing may employ a similar proportion of SME workers.

Some notable trends within this picture include the following.

- The 'headcount' of businesses in agriculture, forestry and fishing is high, but the overwhelming majority are microbusinesses; in the North, average employment per business in these sectors is around three people. Their contribution to turnover is relatively small, but their importance in maintaining the landscape and natural environment of rural areas is very substantial indeed (Cox et al 2017).
- Production and manufacturing, by contrast, account for a small proportion of SME 'headcount', but a relatively high proportion of both SME employment and turnover, amounting to almost one-fifth in the North East and Yorkshire and the Humber. This is particularly marked in the North East.
- The rate of employment and contribution to SME GVA by sectors identified as relatively unproductive (retail, accommodation and food services) is somewhat higher in the North East than the other parts of the North, as discussed above.
- Finance and insurance, information and communication, and professional, scientific and technical activities have a higher business headcount in the North West than in the North East or Yorkshire and the Humber. In particular the professional, scientific and technical population includes many microbusinesses, with an average employment count of around 3.5 per business.

FIGURE 2.1

SME population (businesses with fewer than 250 employees) of the north of England, by sector and contribution to business population, employment and turnover



Source: ONS 2018d

IPPR North survey of SMEs in the north of England

To better understand the profile of SMEs in the north of England, and the challenges they face, IPPR North commissioned a survey of small business owners and directors across the region. Fieldwork was carried out by Censuswide in May 2019.

Of the 501 responses, 15 per cent were from the North East, 60 per cent were from the North West and 24 per cent were from Yorkshire and the Humber. Across the North, 14 per cent of SMEs are based in the North East, 50 per cent in the North West and 36 per cent in Yorkshire and the Humber (ONS 2018d).

Larger SMEs were disproportionately represented. 43 per cent of responses were from sole traders, a further 25 per cent from micro enterprises (comprising businesses with fewer than 10 employees). For context, 95 per cent of northern SMEs are micro enterprises.

45 per cent of respondents were men, and 55 per cent were women. 92 per cent stated their ethnicity as 'White'. Across the North, 89.4 per cent of residents are white (Source: Annual Population Survey).

2.2 CHARACTERISTICS OF NORTHERN SMES

Our qualitative and quantitative research with SMEs identified the following broad trends.

A diverse population with diverse aspirations and needs

Northern SMEs are not a homogeneous group and they operate in very different local contexts. Policies that assume a 'one size fits all' approach to supporting or representing them are therefore unlikely to be effective. Variations in size, sector, place, and other factors such as business maturity and business mission lead to very different trajectories, and with these come different support needs.

This doesn't mean that it is impossible to provide SME support that is effective across a region or a sector. Rather, support needs to be flexible, with the option of close tailoring to the situations and needs of individual businesses. Those providing it need the ability, knowledge, time and mindset to get to know the businesses they work with and to plan support packages that correspond to their requirements and aspirations. Our recommendations (chapter 6) are designed to reflect and support this diversity.

- 18 per cent strongly agree that they would like to keep their business going "more or less as it currently is". A further 34 per cent somewhat agree.
- 18 per cent strongly agree that they'd like to build a national or international business, 29 per cent somewhat agree.
- 45 per cent say they have a detailed business plan for how they will achieve their priorities. However, 75 per cent of sole traders and 70 per cent of microenterprises say they do not have a business plan.

Source: IPPR North SME survey

Local identities

Interviewees suggested that many SME leaders have ambitions to trade and – to a lesser extent – develop networks outside their immediate locality. However their primary focus tends to be highly local or sub-regional when it comes to support needs and other day-to-day business activities. Our SME participants provided many examples of this approach. For example, they tend to network and use business services within a town, city, or at most a sub-region.

For services companies, however, trading ambitions are often national rather than northern – with many companies keen to expand their reach across the UK. In particular, business services firms in the North may be especially attractive to London clients because they offer high-quality services whose prices reflect the absence of the high overheads (rent, transport, higher salaries) for London-based firms. For companies that provide goods and products, there may be a greater focus on maximising opportunities within a smaller geography.

In general, the geographical ambitions of companies reflected the type of goods and/or services that they offered; for example, catering companies were highly focussed on a relatively small geography, while online business services firms often 'think globally'.

Expert interviewees noted that an important function of business support may be to challenge assumptions about *where* businesses can identify and exploit trading opportunities.

Informality

Several interviewees suggested that many SMEs have an informal management style, lacking strategic leadership. Microbusinesses in particular tend to fall into this category. Many people who start a small business do so because they want a career doing what they enjoy, or what they are good at. They may not necessarily be good directors or managers – and will often learn through experience how to run a successful firm.

For some, this may lead to a situation of living 'hand to mouth' or 'from day to day'. Too many SMEs exist in constant 'crisis mode', and as a result may struggle to take stock and act in their strategic best interests. Business owners who work in this way may find it hard to identify areas of their firm that need improvement. As a result, their adoption of new technology and new business practices can be sporadic and ad hoc.

SME leaders also have diverse business ambitions. A significant proportion have a clear plan for growing their business, but for many more growth is a general aspiration. Others have little or no growth ambition, and instead focus on maintaining their business in its current form. This does not always demonstrate a lack of ambition; they may prefer to keep the business small for various reasons (ease of innovation, community commitment, or lifestyle). Even without strong growth ambitions, however, SMEs can still benefit from improvements to their productivity.

For this reason we recommend (Chapter Six) that business support for SMEs include options for high-quality and tailored training in management and leadership skills.

3. PRODUCTIVITY CHALLENGES FOR SMEs IN THE NORTH OF ENGLAND

In this chapter, we consider factors in the wider northern and UK economies that will impact on SMEs. These are largely outside the control of individual businesses, but SME responses will have implications for their productivity. The recommendations in chapter 6 present proposals for how a new framework of business support can help SMEs to manage aspects of this context. In chapter four, we consider firm-level factors over which SMEs have more control and can take more direct actions.

- 47 per cent of respondents say they saw an increase in profits last year
- 20 per cent say that profits are down
- 55 per cent say costs of doing business (not including salary costs) have increased this year

Of the 'major' issues that SMEs face, the most frequently raised were:

- difficulties finding new customers – 27 per cent (an additional 42 per cent say it's a 'minor' issue)
- red tape and regulations – 17 per cent (38 per cent say it's a 'minor' issue)
- problems recruiting people with the right skills – 15 per cent (23 per cent say it's a 'minor' issue)
- lack of finance – 15 per cent (28 per cent say it's a 'minor' issue).

47 per cent have applied for finance in the past year, including 22 per cent who have used a credit card, 20 per cent who have used a bank overdraft, and 18 per cent who have used a bank loan.

Use of finance is less prevalent among sole traders (32 per cent have applied for any form of finance).

Source: IPPR North SME survey

3.1 WIDER ISSUES THAT IMPACT ON SMES

Skills

Skills are vital in boosting productivity (Rincón Aznar et al 2015; Konings and Vanormelingen 2010; Sasso and Ritzen 2018). All of our interviewees agreed on this point. Skills levels across the north of England are lower than for the UK as a whole, with particular challenges in sectors at Level 4 and above (Round 2018a).

Skills shortages in general are more acute for SMEs than for large businesses. In 2017, almost one-third (31 per cent) of vacancies in firms with fewer than five employees were 'hard to fill' because of difficulties in finding suitably-skilled candidates; this compares to just 16 per cent in firms with 250 or more employees (Winterbotham et al 2018).

Recruiting skilled workers is especially challenging in some highly-skilled fields. There was some perception that graduates may leave the region, believing it to be easier to build a career in the south of England. However, the quality of northern graduates and universities was praised. Short supply of high-level and graduate skills may result in salary inflation, which in turn raises difficulties for SMEs. Participants noted that it can be difficult to find very specific skills for certain roles or sectors, particularly in fields where technology is fast-moving. Examples included some areas of digital and construction.

Expert interviewees noted that some SMEs are unwilling to invest in staff training.[6] In 2017, 42 per cent of businesses with 2–4 employees trained some of their staff, as did 56 per cent of firms with 5–24 workers; by contrast over 60 per cent of staff were trained in establishments with 25–99 staff and 70 per cent in those with 100–249 (DfE 2018).

Barriers to engaging in training include anxiety that investment in training may mean that newly-skilled staff may choose to use their enhanced employability to change jobs, and even an unwillingness to "make up for the deficiencies of the school system", in the words of one interviewee. Training is often seen as an investment in the individual rather than the company.

Identifying skills needs, and the right training programmes to address them, also demands time and expertise. It is particularly hard to plan for skills needs that may become critical in the future. In addition, it depends on providers making clear and comprehensive information available, presented in a way that helps SMEs to match training with their needs. SMEs may find it difficult to navigate a fragmented landscape of adult learning provision, as may potential learners (Round 2018a). Training providers, seeking to maximise enrolment, may market primarily to established clients rather than reaching out to potential new markets.

It was suggested that certain sectors might struggle to recruit learners, and subsequently workers, because of a lack of interest in developing particular kinds of skill. Craft and technical skills were mentioned in this context. Interviewees also noted challenges in finding suitable 'upskilling' and retraining opportunities for SMEs with a relatively high number of older workers.

Priorities that emerged from these discussions included the following.

- A need both for 'generic' business skills – such as marketing, handling finances, growing a client base and managing time – and also sector-specific development, such as craft skills and specialised innovation.
- An urgent need to develop the co-investment and fund-sharing aspects of the apprenticeship levy, which allow large levy-paying organisations to transfer some of this funding to smaller organisations within their supply chain (ESFA 2019).
- A need for collaboration to support better skills opportunities for SMEs, particularly to allow the 'pooling' of training to meet needs within the local economy.
- A need for coordination between SMEs to facilitate outsourcing of certain functions (like marketing) rather than requiring all SMEs to upskill in order to 'do everything'.

6 This was not the case for any of the business leaders who spoke to us.

- The usefulness of 'bite size' training opportunities that let established workers upskill in key areas, and, for example, in order to help them apply generic knowledge to a particular company or sector. One area where this was seen as beneficial was digital skills development (see Round 2018b for a discussion of how this can benefit SMEs).

Access to finance

Investment is crucial to productivity; training, innovation and improvements to company infrastructure all involve a short-term cost for longer-term gains. Yet many SMEs report difficulties in gaining access to finance. In general, start-ups and potentially 'high growth' businesses have good range of options. However, things may be harder for more mature businesses looking to scale up after several years of successful operation, and for firms whose growth ambitions are more modest – but still of potential value in growing GVA and creating jobs.

Across the UK, considerable variation emerges between rates of bank lending to SMEs, and both awareness and use of equity finance remains concentrated in London and the South East (BBB 2019). In particular, access to money for relatively small-scale and 'unshowy', but crucial investment is a major problem for many SMEs. Potentially transformative investments in equipment, technology, skills, marketing and other areas may be outside the reach of many SMEs; even £5,000 or £10,000 is prohibitive for an owner who has already made a major commitment of personal funds. Small and accessible loans or grants, in particular those targeted towards firms that add community or innovation value, would be welcomed.

Transport and digital connectivity

Poor investment in physical and digital connectivity (Raikes 2018; Hunter and Longlands 2017) continues to create challenges for the northern economy as a whole, and for SMEs in particular. Deficiencies can damage access to current and potential markets, restrict opportunities to recruit skilled staff, and slow down or hinder essential business processes.

In our interviews with SME leaders and wider stakeholders, we frequently heard of several specific issues with regards to poor connectivity, including the following.

- Specific 'pinch points' and areas of isolation ("being away from the M6 is a big deal"). Unreliable public transport and poor-quality roads tend to affect rural SMEs most seriously; congestion is a major problem for goods manufacturers, especially in urban areas.
- Digital and broadband connectivity remain extremely problematic in many rural areas; these hamper both business-to-customer sales and opportunities to digitise business practices or use digital business-to-business services.
- Piecemeal and fragmented approaches to some transport issues and a lack of coordination; for example, clean air plans are not well integrated, which causes difficulties for businesses using transport across several different regions.
- Many of the SME leaders we spoke to were committed to public transport and decarbonisation opportunities, not least because they understood that these could reduce congestion and improve the mental and physical wellbeing of their employees.
- Digital capacity was considered low in the North by international standards. Even in the major cities, the reach and quality of broadband was felt to be lacking, and costs to be high for both businesses and households (who make up a major part of their customer base).

The costs of running a business

Interviewees were clear that no-one expects to run a business for free, and SME leaders expect to invest in their firms – often taking considerable personal financial risks. They were also clear that, for many SME leaders, making a lot of money is *not* a primary motivation – or even a motivation at all. Several stated that they would have been better off financially had they remained as employees, but that they were glad they had started a business instead.

Nevertheless, some cost issues present major challenges for these business.

- **Business rates**, which are particularly challenging for businesses in sectors where there is a major advantage to locating in a city centre. Serviced offices allow SMEs to reduce this burden, but raise other issues and costs; they also reduce autonomy and can be impractical as firms grow. Business rate relief for SMEs has been welcomed.
- **Non-wage payments:** Increases in pension and NIC contributions and other non-wage payments have created some issues, especially for relatively new businesses.
- **Tax:** Interviewees stressed their commitment to paying tax, but noted that recent falls in the sums that SME owners could earn tax-free, changes to VAT legislation and other developments have made it more burdensome both financially and bureaucratically. Several noted practical problems in dealing with HMRC. Interviewees described a sense that tax and other systems are set up for big companies, with scant attention to the practicalities of SMEs.
- **Late payments and payments not made:** Some SME leaders had experienced only limited problems with late payments or clients refusing to pay, but the majority had come across at least some clients who delayed payment for as long as possible, or simply did not pay SME suppliers what they are owed.

3.2 BREXIT

Just under one-fifth (18 per cent) of SMEs say Brexit represents a 'major' issue for the success of their business. A further 38 per cent say it's a 'minor' issue. 39 per cent say Brexit is not an issue.

Small firms were less likely than larger businesses to identify Brexit as an issue for them - 15 per cent of those with nine employees or fewer said that Brexit was a 'major' issue (compared to 25 per cent of larger SMEs), and 44 per cent say that Brexit is not an issue (27 per cent of larger SMEs).

Of those who stated that Brexit represents an issue for their firm, the main obstacles were:

- uncertainty about future regulatory changes - 43 per cent
- uncertainty about future access to EU markets - 43 per cent
- reduced customer demand - 44 per cent

Source: IPPR North SME survey

Brexit was the most frequently-discussed issue in our fieldwork, with participants mentioning the current uncertainty, the impacts of different eventual trade scenarios, and the possibility of a reduction of demand in the economy should Brexit be followed by lower growth.

The impact of Brexit on SMEs in the North

Our survey of SMEs found variation in how businesses across the North perceived the potential risks of Brexit (see above). This mirrors the findings of other research. For example, one large-scale study of SMEs across the UK found that, in 2017:

- 23.1 per cent viewed Brexit as a 'major obstacle' to business success. This was more marked for innovators, businesses in 'peripheral regions' (over 25 per cent), and exporters and importers (where the figures were 40 per cent and 43.5 per cent, respectively, and almost half for those trading with the EU).
- a higher proportion of medium-sized businesses than small or micro-enterprises felt that Brexit represented an obstacle to their success; the proportion who agreed with this statement increased with firm size. This may reflect the levels of innovation and engagement in exporting or importing (Brown et al 2019).

Figures from the annual Small Business Survey suggest a similar picture. In 2017, just over one-quarter of micro and small enterprises and one-third of medium-sized enterprises felt that Brexit was likely to be 'fairly' or 'very' detrimental to their businesses. A little over half felt that there was unlikely to any impact; around 10 per cent stated that they did not know what the impact was likely to be.

These concerns translate into active preparation for around 40 per cent of all firms, with a higher proportion of medium-sized enterprises than of smaller ones stating that they are 'very prepared'. On the other hand, around one-quarter feel that they are 'fairly' or 'very' unprepared (figure 3.4).

Brexit, SME performance and productivity

Interviewees suggested that businesses had 'taken their foot off the gas' because of the current uncertainty in a 'risk averse' environment. This has resulted in reductions to investment in capital and skills, decisions to delay business investments, and a preference for sticking to 'business as usual' rather innovation in business processes. Sectors such as construction have been especially hard hit. In theory, a period of uncertainty could provoke innovation, as businesses seek competitive advantage. However, this is unlikely to happen when there is no clear end to that uncertainty in sight (Bryson and Forth 2019).

Some potential consequences of Brexit could impact directly on productivity among small businesses. These include the following.

- **Loss of EU investment:** European structural funding to support innovation, skills and business development has benefitted many SMEs, and the level and format of its replacements remain unknown (see chapter 5). It has been particularly important in new industry sectors such as life sciences and food production (McCullogh 2018) and across innovative SMEs more generally (Brown and Lee 2018). The marked differences in the likely regional impacts of Brexit (Ortega-Argiles 2018; North East Brexit Group 2018) mean that a robust regional policy, including strengthened institutions and additional devolved powers, will be important in mitigating negative outcomes (Brown et al 2019).
- **Reduced private investment:** Foreign Direct Investment (FDI), which has been important in developing the northern economy, has fallen. Since the referendum result, inflows have seen the longest continuous decline since the data series began; the UK has now been overtaken by Germany as the major EU recipient of FDI and France is gaining ground. Services have been especially hard-hit (Serwicka and Tamberi 2018).
- **A lack of effective support and advice to help SMEs prepare for Brexit:** Instructions from government to 'prepare' are of limited value when it is not clear what one is preparing for. Support needs include business continuity planning, with advice both on business practices and knock-ons from impacts to customers, and locally-tailored resources. Many SMEs may 'not know what

they don't know' about some key issues; for example, non-tariff barriers and the implication of changes to regulatory frameworks.

- **Loss of access to skills**, particularly in sectors that rely on highly skilled migrants or on a large migrant workforce (such as hospitality, food and agriculture).
- A demand for businesses to **expend scarce resources of time and money on preparing for Brexit**, rather than investing these in measures to boosts productivity.

Rising costs as a result of the weak pound have produced what one interviewee called "a direct hit to productivity". This is exacerbated by pressures within supply chains, as larger businesses want more from smaller ones and resist costs being passed on. This leaves smaller businesses with limited resource for investment to drive up productivity, which – ironically – might make it easier to respond to precisely such demands. To improve productivity in these circumstances would be very difficult indeed. Businesses that are in the supply chains of companies relying on EU and international customers have also encountered difficulties.

One interviewee reported that some SMEs had described a nervousness about articulating their actual feelings over Brexit, because of a national narrative that it is important not to 'talk down' Britain or be overly negative about potential outcomes. We did not encounter any such reticence in our qualitative research, and it must be said that although we asked participants to consider positive impacts and opportunities, few chose to do so.

Several interviewees suggested that a major unknown is the potential impact of a downturn in demand and consumer spending as a result of Brexit, especially when it follows a long period of 'belt tightening' under austerity and stagnating wages. Where positives were noted, these tended to be 'side effects' of the need to plan for Brexit, rather than changes associated with leaving the EU. Examples included:

- greater awareness of supply chains and one's place within them
- a sense among some companies that they will be 'protected' because they are not involved in importing and/or exporting, or because they trade primarily outside the EU.

4. FIRM-LEVEL DRIVERS OF PRODUCTIVITY

This chapter explores the drivers of productivity at the level of individual firms. It reflects findings from our fieldwork, supplemented by wider research and data analysis. Our recommendations in chapter 6 propose how business support can help SMEs to respond effectively to these challenges, and boost their productivity through by investing in different ways of doing business.

The following needs were identified as 'high priority' by SMEs in our survey:

- 'developing new products or services' – 30 per cent
- 'improving the skills of our employees' – 28 per cent
- 'finding new overseas markets' - 15 per cent
- 'investing in new equipment, machinery and/or technology'– 21 per cent
- 'doing more online' – 36 per cent
- 'developing management and leadership skills' – 23 per cent
- 'increasing the social and environmental benefits' of their business – 23 per cent

Source: IPPR North survey of SMEs

Speaking the language of SMEs, what is 'productivity'?

The term 'productivity' is disputed even within the discipline of economics. Despite its importance for SMEs, some authors have identified what might be termed 'productivity illiteracy' (BEIS Committee 2018). For example:

- in one survey, around 15 per cent of SMEs did not know what productivity was, 29 per cent did not know how to measure it, and 37 per cent said that they did not have time to measure it
- a lack of understanding means that SMEs often don't know how they could act to improve productivity, and misjudge their own relative performance
- many SMEs are too strongly focussed on growth and profits to consider the issue (BEIS Committee 2018).

Research conducted by a team from the University of Gloucestershire found that, while SMEs were aware of the importance of productivity, this did not always translate into actions around business planning and company strategy (University of Gloucestershire 2017).

In this research, we found a mixed picture. Among the SMEs we spoke to, awareness of productivity was high and leaders were aware of actions to support this. However, our interviewees were a self-selecting group who had chosen to take part in discussions of precisely this topic. Our expert interviewees reported that, while some SMEs are focussed on productivity, others do not grasp its meaning or importance.

We found five core factors that influence firm-level productivity among SMEs.

1. Management and leadership skills

Strong research evidence suggests that a great deal of cross-firm variation in productivity relates to the nature of management practices (Bender et al 2016). Poor management has been identified as the leading cause of SME failure, blamed for 56 per cent of insolvencies (CMI 2015). Improved entrepreneurial leadership skills are important both in determining the fate of individual companies, and in developing and strengthening regional business ecosystems (Huxtable-Thomas and Hannon 2017).

However, SME leaders may not recognise their own skills needs, or realise that changes could have a major impact on their business. Even if they do, they may not be able to identify the right training, or be unwilling to take time away from their business to follow it. Interviewees (both SME leaders and others) described the dangers of ‘not knowing what you don’t know’.

Management skills are particularly important at certain points in SME development, particularly during periods of ‘scaling up’. One key issue is a lack of skills for *running a business* among people who are highly skilled in *doing what the business does*. This mismatch between skillsets can sometimes make it harder for SME leaders to diagnose their own management skills needs. Family businesses may face particular challenges in acknowledging the potential for better management practice to improve their productivity.

Good quality training is available; interviewees named several examples of short and extended programmes, provided by universities, banks and other private sector stakeholders, and dedicated training providers. One gap may be around guidance for scaling up of firms that are not ‘high growth’ or highly innovative, but nevertheless have the potential to grow steadily, providing employment and local economic and social benefits. Interviewees noted that, as well as some excellent provision, other courses are of limited value.

SME leaders may also need support to choose a programme that closely meets their needs. This is an area where tailored advice, supported with examples of the tangible benefits of learning, could be beneficial. Interviewees also felt that high-quality mentoring could improve management and leadership skills.

2. Adopting technology and digital innovation

Adopting technology across a wide range of applications has the potential to boost SME productivity. Yet technology adoption may be particularly slow in small and medium-sized enterprises (Haldane 2018). Digital technologies in particular can improve both the core activities and the management of SMEs, helping them implement more efficient business processes, reach new customers, and manage existing customer and supplier relationships. As more day-to-day business processes become ‘digital by default’, digital skills and systems will become important in building general business efficiency (see, for example, Tu et al 2017).

Once again, businesses may need support to diagnose their specific needs in technology and digital innovation. The vast majority of businesses can benefit from digitising at least some of their marketing and business processes. However, many miss out on getting the most from technology because of a lack of understanding and good-quality advice. The opposite problem arises when a business adopts ‘tech for tech’s sake’, rather than tailoring new investments to specific business goals. This is true both for digital and for sector-specific technologies.

Digital investment must ensure that businesses have both the right equipment (software and hardware) and the right skills so that employees can make the best use of these for the business. Neglecting one side or the other of this equation means that potential productivity gains will not be felt (Díaz-Chao et al 2015).

As noted above, businesses depend heavily on good quality digital infrastructure, which can be hard to access in rural areas. As a result, they may miss out on using certain digital services, as well as on accessing new activities and markets, such as exporting out of area or internationally.

3. Innovation

Innovation is widely recognised as a contributor to SME productivity. Many SMEs are created by entrepreneurs with the explicit aim of innovating, and larger businesses may effectively 'outsource' innovation to their supply chains. All SMEs can benefit from incorporating innovation into their processes, drawing on research and development from universities and other sources.

Such innovation thrives within strong regional networks that facilitate dialogue and interactions between innovators and potential beneficiaries. Universities have a key role to play as centres of excellence for research and the development of high-level skills (Montmartin et al 2018). A high degree of 'regional alignment' supports productivity growth because it promotes 'intimate and multiple connections' between innovation, technology and scientific advances and key social institutions. This promotes dialogue, collaboration and knowledge-sharing (Aghion et al 2009).

A focus on innovation is often associated with manufacturing and production, but interviewees stressed that it is also vital for services. They can benefit from support to identify and codify their intellectual property, and to develop it through research and testing of application to new cases or markets. Relationships with experts in research and in applying research are essential.

Interviewees described examples of how northern universities and their partners are becoming centres of excellence and expertise for knowledge transfer to SMEs. They gave examples of SMEs who had approached regional HEIs in order to access innovative ways to boost their growth and productivity. They also gave examples of ways in which access to university expertise, including research and development, has benefitted SMEs in sectors that are not obvious candidates for 'high tech' or cutting-edge innovation, but have problems which can be solved through the expertise that resides in universities. This relies on good quality facilitation and high visibility of the relevant university. In some cases, SMEs had approached the university to use a generic business support programme and then benefitted from further engagement.

Not all SMEs are aware of these opportunities in their region, or aware that they could benefit from them. Universities often do a good job of making links to research communities elsewhere, but the relevant teams are often small and their expertise – by necessity – relates primarily to their own institution and local economy.

4. Internationalisation

SMEs that export tend to be more productive (BBB/ERC/Goldman Sachs 2015). Entering an international market encourages scrutiny of business processes, engagement in 'lean' practices, and analysis of productivity and innovation. However, many SMEs miss this opportunity. Around 10 per cent of non-exporting firms are estimated to have the potential to become exporters, but despite this just one in five SMEs currently export outside the UK.

Interviewees identified a lack of support for SMEs that aspire to trade internationally. This reflected some preconceptions about who is a 'likely candidate' to export, with smaller firms and services companies particularly likely to be excluded as a result. Other barriers include a lack of understanding among SMEs about how exporting works, and some reductions in support for internationalisation, such as certain UKTI/DIT programmes (DTI/UK Export Finance 2018).

Exporting demands a high level of bespoke support, providing guidance that addresses specific opportunities for particular sectors and potential export partners. Key issues include market and cultural awareness, efficiency of process, and support with the administrative aspects of exporting, as well as how to expand beyond an initial experience of internationalisation. One interviewee noted that "There's a seminar on exporting in a few weeks' time" is of little use as advice to a business that needs to seize an export opportunity immediately. Several noted that exporting is an area around which mentoring is especially valuable, both as a source of candid advice and as a way to build confidence among new or expanding exporters.

5. Employee health and wellbeing

Employee health and wellbeing are crucial to firm productivity (see Black et al 2008). Key issues include approaches to workplace health and work practices,[7] and the physical environment of the workplace (Fisk 2012).

We encountered almost unanimous agreement among interviewees on this point. Leaders of SMEs with employees mentioned examples from their own firms, including practices to supported employee engagement, family-friendly working, stress reduction and good mental health, trust, worker autonomy, and tailored approaches to performance management.

Once again, we should be cautious about assuming that these SME leaders are representative of all small businesses. Both they and our other interviewees mentioned a broader lack of awareness of the importance of these issues to productivity: "when we need to do more on productivity we need to not make it difficult for people to contribute in the workplace", in the words of one participant. Similarly, participants felt that SMEs may lack a good knowledge of occupational health, beyond conventional 'health and safety'.

Current trends in employment practice could represent a possible productivity risk. Some analysis suggests that workplaces which have "increased their use of numerical flexibility in staffing" had, over the same period, seen a decrease in certain aspects of business performance, including productivity and quality of output (Bryson and Forth 2015). This suggests that some options for reducing input costs, such as casualisation and the use of highly flexible contracts, may not lead to the desired productivity impacts.

There is also evidence that minimum wages can operate as productivity drivers. For example, the introduction of the national minimum wage was associated with increases in productivity, because employers changed their practices and invested more in staff training. Research outside the UK suggests that minimum wages can increase worker effort (Owens and Kagel 2010) and reduce levels of job churn (Riley and Bondibene 2015).

In chapter 5, we discuss the business support landscape for SMEs in the north of England, and the ways in which it can help them to address the issues set out here.

7 See Round 2017 for a summary.

5.
BUSINESS SUPPORT FOR SMEs

This chapter briefly explores the current business support landscape in England, with specific reference to the North, and identifies areas where this could provide more effective provision to boost SME productivity.

72 per cent of SMEs agree that they "generally tend to do things on our own and without advice from others".

69 per cent say that they "know who to ask if I have a query regarding my business".

39 per cent agree that "support for businesses in my local area is relevant to firms like mine"

59 per cent of SMEs say they have had some form of support in the past year. There was a wide range of support mentioned:

- 13 per cent say they have accessed support from central government (eg GOV.UK)
- 7 per cent say they have accessed support from their local growth hub, local council or local enterprise partnership
- 12 per cent say they have got support from a business network
- 15 per cent have used an online training course.

Source: IPPR North survey of SMEs

What is business support?
Many SME owners have the ambition to grow their business and expand their customer base, but may lack some of the necessary skills, knowledge, capacity or finance to do this on their own. High-quality support and advice make a crucial difference.

Robust evaluations of business support programmes are relatively rare. Where these have been conducted, however, the majority show that they have a positive impact (What Works Centre 2016). SMEs, in recognition of their contribution to the economy, are offered a range of government-funded support. The EU also funds some provision, primarily through the ESF and ERDF.

Business support includes options such as direct coaching or signposting services. It may offer help with all of the issues discussed above, including:

- management and leadership skills
- business strategy
- access to affordable and targeted training (including digital skills development)
- advice on HR policies and support for workers, workplace health and staff retention
- export opportunities and new markets

- access to finance
- advice on using digital technologies and enhancing business practices through digital
- support for innovation (Round, Hunter and Longlands 2019).

To make the most of business support, SMEs need to know how to access it, and to trust that it will provide a worthwhile return on the money and time they invest in it.

5.1 THE BUSINESS SUPPORT LANDSCAPE

Government provides a range of financial and non-financial support to SMEs. This includes the following major schemes.[8]

The industrial strategy

The industrial strategy (HM Government 2017) has an explicit remit to boost productivity and growth through investment in businesses, skills and infrastructure. It includes national actions, led by the Department for Business, Energy and Industrial Strategy, and the local ones, primarily led by LEPs and combined authorities.

SME productivity is a key strand of the industrial strategy. It introduces a new Business Basics Programme (with £8 million of funding) to test new ways of encouraging SMEs to adopt technology and improve management practices in an effort to improve productivity. It also includes a 'Long Tail Productivity Review' to address the challenges discussed in sections 1.2 and 1.3 of this report (BEIS 2018).

Be the Business

The industrial strategy includes an announcement of government funding (£13 million over three years) to match private sector investment in Be the Business, an initiative to boost UK productivity and competitiveness. Be the Business delivers a range of programmes to enhance business performance. These include the following.

- **The 'Productivity through People' programme:** This SME education programme aims to enhance leadership and management capacity in small businesses. It brings together academic learning, input from industry leaders, and peer-to-peer support, as well as visits to leading national and multinational companies.
- **Business Collaboration Networks:** Place-based programmes that trial innovative peer to peer solutions to encourage the adoption of business improvements.
- **Mentoring for Growth:** This initiative pairs executives from leading businesses with SME owners. LEPs match mentors and mentees to achieve a good 'fit'.
- **Benchmarking:** A new online tool helps firms identify opportunities to improve their businesses, and provides links to examples of how other SMEs have implemented performance improvements.

The British Business Bank

The British Business Bank (BBB) is independently managed but fully owned by the government. It was created in 2014, with a remit to change "the structure of finance markets for smaller businesses (defined primarily as those with turnover less than £25 million), so these markets work more effectively and dynamically" (BIS 2015b). The BBB does not lend directly to firms, but works with other financial institutions, including banks, leasing companies and venture capital funds, to increase access to funding (for example by part-guaranteeing loans).

8 This list is not exhaustive.

The BBB works in three broad areas to raise the growth potential of the UK economy:

- **supporting scale-ups:** including a new £2.5 billion patient capital entity to co-invest, alongside private sector investors, into venture and growth capital funds
- **closing regional imbalances:** including a focus on regional imbalances in equity finance that heavily favour firms in London (BBB 2018)
- **raising awareness**: improving information in the market and fostering links between smaller businesses and finance providers to get the best match of provision to need.

EU schemes

The European Investment Bank (EIB) invests in infrastructure and also provides opportunities for UK SMEs to access funding. The European Investment Fund (EIF), of which the EIB is the majority shareholder, supports SME access to finance. Like the BBB, neither the EIF nor the EIB lends directly to SMEs. Instead, intermediaries provide finance, including both loans and equity capital. These intermediaries include private banks, investment funds and venture capital firms.

In addition, LEPs and growth hubs receive funding from the European Regional Development Fund (ERDF) and European Social Fund (ESF).

The future of these funding schemes after Brexit is highly unclear and the cause of considerable concern. The UK will no longer be a member of the EIB, and its €5.5 billion of paid-in capital will be repaid in 12 annual instalments starting in 2019.

In late 2018, the government announced **£20 million extra funding for the BBB in the year after Brexit,**[9] if no agreement is reached to extend the relationship with the EIB. A House of Lords report proposes that the government replace the EIB with a new national infrastructure bank.

Funding from both the EIB and EIF has already declined sharply (House of Lords 2019). The government has indicated its intention to replace the ESF and ERDF through the Shared Prosperity Fund. However, details of the eventual form of the SPF remain to be announced.

Northern Powerhouse Investment Fund and North East Finance

Announced in 2017, the £400 million Northern Powerhouse Investment Fund (NPIF) is designed to boost business growth in Yorkshire and the Humber, Tees Valley and the north west of England, by providing SMEs with access to finance via intermediaries. It is funded from several sources including the UK government, the EIB, the BBB and the ERDF. The fund will be managed by the BBB, in partnership with the ten LEPs in the regions covered.

NPIF provides commercial finance through three types of product: Microfinance, Debt Finance and Equity Finance. These are designed to plug common gaps in access to finance. A separate but similar fund, North East Finance, covers the North East LEP area. Both schemes are aimed primarily at SMEs – both start-ups and established firms – that can demonstrate growth potential.

Both schemes offer relatively modest levels of funding. The NPIF, for example, has directly invested £100 million in 385 northern-based SMEs, and also leveraged £84 million of investment from the private sector over two years.[10]

9 See: https://www.british-business-bank.co.uk/autumn-budget-2018/
10 See: http://www.the-lep.com/news-and-blog/npif-supports-%C2%A3184m-of-investment/

Innovate UK and Catapult Centres

A range of initiatives seek to support and develop innovative businesses. Innovate UK works to build links between businesses and potential partners, customers and investors, in order to encourage the development of commercially successful products and services. They also fund business–research collaborations to accelerate innovation and drive business investment in research and development. Analysis for Innovate UK states that they have helped 8,500 organisations create around 70,000 jobs, and added an estimated £18 billion of value to the UK economy.[11]

Innovate UK has established a national network of Catapult centres, which provide a physical base where firms can access technical expertise, equipment, and other resources required to develop innovative concepts into products. There are several Catapult centres in the north of England: the National Renewable Energy Centre at Blyth, Northumberland (part of the Offshore Renewable Energy Catapult); the North East/Tees Valley Digital Catapult; the Nuclear Advanced Manufacturing Research Centre and Advanced Manufacturing Research Centre in Sheffield; the Centre for Process Innovation in Redcar (part of the High Value Manufacturing Catapult); and the Medicines Discovery Catapult in Alderley Park, Cheshire.

Last year, the government announced £780 million additional funding for some of the UK's Catapult centres, as part of the industrial strategy.[12]

Help with exporting

In August 2018, the government launched a new export strategy (DIT/UK Export Finance 2018), which includes a commitment to better target SMEs with available support. This includes various policies and initiatives to support and encourage SMEs to export, including trade finance, overseas trade events and access to advice on export issues such as:

- financial incentives, and dedicated support, to SMEs to access emerging markets
- UK Export Champions who are themselves successful exporters
- a review of export support provided locally through LEPs and growth hubs
- improved digital access to export support, particularly for SMEs.

The Business Support Helpline and GOV.UK

Following the abolition of the Business Link network in 2011 (see box), the government set up a dedicated national helpline and website for business support. Initially, this used the Business Link branding; it was subsequently rebadged as the Business Support Helpline, with online support via GOV.UK. This support forms a key part of the government's offer to SMEs in England, providing trusted and joined-up information and signposting businesses to relevant support.

11 See: https://www.gov.uk/government/organisations/innovate-uk/about

12 See: https://www.gov.uk/government/news/billion-pound-backing-for-british-innovation

Business Link (abolished in 2011)

Until its abolition in 2011, the regional network of Business Link offices (delivered through Regional Development Agency Offices) was a key part of SME support.

Business Link was designed as a one-stop shop where businesses could access advice on starting-up, regulatory requirements, exporting, accessing finance for growth, and other issues. Services used an IDBT (information, diagnostic, brokerage and transaction) model. Regional Business Links ran events and workshops on topical subjects and general business skills, and offered face-to-face support delivered by regional business advisors. The aim was to improve the performance of small businesses.

Evaluations of the Business Link programme found an association between its services and positive employment outcomes (Mole et al 2009), and a significant employment effect on firms that received intensive face-to-face support (Mole et al 2008). Some tentative evidence also points to a positive impact on productivity (Roper and Hart 2003).

In 2011, the Coalition government ceased to fund Business Link.

Local enterprise partnerships (LEPs)

In England, public sector support for businesses at the local level is primarily organised through a nationwide network of 38 LEPs, which effectively replaced the regional development agencies with a public–private partnership model. LEPs are responsible for promoting local economic development within their local areas, each of which straddles a large strategic footprint corresponding to a functional economic areas.

LEPs submit strategic economic plans to central government in order to draw down funding from the Single Local Growth Fund. Originally created in the 2013 spending review, the fund has grown over time through additional rounds of funding such as growth deals; as of October 2018, £9.1 billion of growth deal funding has been allocated to LEPs (Ward 2019). LEPs have also been allocated money from the Growing Places Fund for infrastructure spending, and are responsible for delivering part of the EU Structural and Investment Funds for 2014–2020.

Business support is a key part of many LEPs' activities. Many have identified the promotion of enterprise, access to finance and business growth as strategic priorities and have developed schemes to address this as part of their growth deals (Pugalis and Townsend 2014).

Growth hubs

LEPs also manage growth hubs, each of which covers a LEP geography. Growth hubs bring together existing business support provision and provide signposting to help businesses access information and advice, simplifying what can be a confusing landscape of private and public sector provision. Growth hubs were created with the aim of ensuring that local business support is "simpler, more joined up and easier to access" (BIS 2016). They offer a locally-led replacement for the centralised Business Growth Service, which incorporated the Manufacturing Advisory Service (MAS) and the Growth Accelerator programme.

Local development and management means that growth hubs vary considerably in their design and scope. All have some online presence, as part of the LEP website or as a standalone, and most have a dedicated phone line for businesses seeking support. However, few offer face-to-face advice. Of the eleven northern growth hubs, only Greater Manchester (where the model originated) has a physical 'shop front' where SME representatives can drop in.

Central government funds LEPs to provide growth hubs. They were initially funded for a two-year period from 2014, with the expectation that they would become self-sustaining. However, between 2016 and 2020 the government has committed £12 million annually. The very low level of funding received by growth hubs has raised serious questions about their viability (BEIS Committee 2018).

The following sections note some issues with the current landscape for business support, using findings from our interviews with northern stakeholders and learning from IPPR North's analysis of support for small businesses in Lancashire and Cumbria.

KEY ISSUE 1: FUNDING AND AMBITION FOR STRATEGIC BUSINESS SUPPORT

Current initiatives are useful, but lack sufficient ambition to make a tangible difference

Over the past decade the government has introduced the significant national initiatives, described above, each with a strong local and/or regional element. These have great potential to improve SME productivity, but lack the ambition and scale to be truly transformational.

The industrial strategy represents a welcome acknowledgement of government's role in investment, and its explicit focus on SME productivity is also important. Expert stakeholders felt that it offers a major opportunity to boost SME performance, but noted a number of issues that must be tackled in order to maximise this.

Intermediaries are vital in translating industrial strategy benefits for SMEs. Awareness of the strategy among SMEs is low; this is not necessarily a problem in itself, but it creates a major task for 'intermediary' organisations, who will need to make sure that small business can access its benefits. Both members and representatives of such organisations accepted this, noting that they can help to make policies tangible and practical in local and sector contexts; expecting SMEs to engage directly with a large-scale government policy may not be particularly effective.

Local industrial strategies will also have a key role in coordinating activities across regional economies, making industrial strategy promises 'real' for businesses, and deriving opportunities for SMEs from initiatives such as the 'Grand Challenges'.

Regional fairness: some participants felt that the industrial strategy in its current form lacks a sense of place, which could result in uneven access to opportunities for development. Previous initiatives where funding has been disproportionately allocated to southern regions were noted.

Translating the industrial strategy to the everyday economy: innovation can be transformative not only for high-profile and cutting-edge industries, but also for SMEs on the peripheries of these (in construction, supply chains and business services, for example), and in sectors that are apparently unrelated. Implementation must embrace the full spectrum of businesses, to gain the greatest impact on productivity, employment, and living standards.

Adequate SME investment: SME funding via the Business Basics Programme is very low, and local industrial strategies will primarily coordinate existing local and national funding; they are unlikely to carry any additional money for local investment.

Growth Hub funding is also low and time-limited

£12 million a year across 38 growth hubs mean that this vital resource is spread very thin. The current allocation ends in 2020 and plans for legacy funding are unknown; in addition, many growth hubs rely on EU funding.

This combination of factors means they are poorly-positioned deliver a comprehensive package of support including, for example, the face-to-face advising that was a highly effective element of Business Link. It also limits their power to move proactively to shape the local business support environment – for example, by addressing gaps in the market (where this has happened it has often relied on EU funding). Low funds and short-term policies have left growth hubs with little option but to work reactively rather than strategically.

The visibility of LEPs and growth hubs is low among small business owners, and they are low on the list of support organisations for northern SMEs; some small businesses are even unaware that these exit (FSB 2017). SMEs are more likely to reach out to private sector providers, including banks, accountants and lawyers, as well as networks such as industry groups and chambers of commerce. To some extent, this may reflect a tendency to seek advice along with key business services; most SMEs will use a bank plus some accounting or legal advice.

Part of the solution is better funding for key coordinators such as growth hubs. This should be used, among other things, to develop a more collaborative and place-based approach to providing business support, offering a 'no wrong door' approach for local businesses.[13]

LEPs and growth hubs could also seek ways to collaborate to make better use of scant resources. Some specialist support services would be better delivered on a pan-northern basis – for example, generic advice on exporting, social enterprise, rural business issues and support for certain sectors such as arts and culture (FSB 2017).

The N11 group of northern LEPs has already agreed to work together to develop closer joint working arrangements where appropriate, including building and learning from best practice and exploring scope for greater collaboration and cooperation (Humber LEP 2018).

The British Business Bank has great potential but is comparatively poorly funded

The BBB was created to address market failures in the allocation of finance to SMEs. This is particularly relevant to the north of England, given evidence of a London bias in private sector lending to SMEs. For example, almost half of equity deals are in London, although the city is home to only around 20 per cent of high-growth firms (BBB 2019).

The BBB currently supports almost £6 billion of finance for around 82,000 smaller businesses. This sum is not inconsiderable, but it is very low for an initiative that seeks to effect real change in the economy. In 2012, for example, IPPR set out a possible initial design for a 'British Investment Bank' (with a similar role to the BBB) and proposed an initial capitalisation of £40 billion, with the expectation that it would build a balance sheet of over £140 billion within four years through capital markets (Dolphin and Nash 2012). The Labour Party has also published an independent report that calls for a **£250** billion investment bank, with a view to emulating the highly successful German system (Labour Party 2017).

13 See: http://data.parliament.uk/WrittenEvidence/CommitteeEvidence.svc/EvidenceDocument/Business,%20Energy%20and%20Industrial%20Strategy/Small%20businesses%20and%20productivity/written/80525.html

The government recently announced plans to inject £200 million of additional funds into the BBB, specifically to back businesses that are starting out and scaling up.[14] A previous IPPR report (Longlands et al 2018) suggested that the BBB might help 'fill the gap' in support for start-ups in the absence of European funds.

KEY ISSUE 2: A COMPLEX BUSINESS SUPPORT LANDSCAPE AND A LACK OF TRUST

The business support landscape is complex and confusing, and seems to shift constantly

SMEs are offered a wide range of government programmes and initiatives, alongside free provision offered by large businesses and sector bodies and various paid-for options. Some schemes are short-lived, and eligibility criteria are often highly specific. All of these factors create a hugely complex landscape for SMEs, LEPs and growth hubs to navigate. Business support in England is often described as a confusing landscape (BEIS committee 2018).

This complexity is acknowledged by government. Policies such as the creation of growth hubs have sought to simplify matters, but successive changes to central government policy, which have alternately swept away and introduced initiatives, have often had the opposite effect.

The huge diversity of SMEs means that a wide range of support options is desirable, in order to meet different needs. And schemes should be regularly reviewed to ensure that they are relevant to current contexts and provide good value for money. However, constant 'churn' risks making a complex landscape impenetrable. This, coupled with uncertainty over funding streams, makes it harder for businesses to take investment decisions to improve their productivity.

Businesses distrust the quality and value of current business advice

Although our interviewees had accessed some business support that they considered extremely helpful, they also expressed a lack of confidence in the quality and value of much of what is available. Criticisms included the very 'generic' nature of much provision, a lack of tailoring to the circumstances of individual organisations, and the role of some 'professional advisers' who lack engagement or experience in the world of running a SME. High-quality mentoring was viewed as a very useful option, but once again its potential variability was stressed.

This finding echoes previous work that found a lack of trust in much business advice, including both commercial and government options (for example, CEEDR 2011). The evidence base for current business support options is limited, with few or no evaluations "at the threshold for evidence that the programme has caused the reported impact" (NAO 2019); a NAO review is underway of BEIS schemes that seek to improve performance, productivity or business investment.

Some local areas have tried to develop a network approach to the provision of informal advice and support, including peer-to-peer support and mentoring. This potentially can help to overcome the trust barrier; however, SMEs may still lack the time and resource to create their own support systems. Support that is provided by banks was discussed in positive terms; this builds on an existing trust relationship, and also on established lines of contact.

14 See: https://www.ft.com/content/a62c82f8-6052-11e9-b285-3acd5d43599e

KEY ISSUE 3: TARGETED SUPPORT IS STRONGLY FOCUSED ON HIGH-GROWTH FIRMS

There is lots of government-backed assistance for businesses who have the potential to support job creation

Much business support policy is highly focussed on "intensive growth coaching aimed at a small number of self-selecting businesses with high growth ambitions". Government schemes reflect this tendency, while other companies must use far less bespoke services or pay the full costs of external advice (Thompson 2014).

However, being a 'high growth' SME is only tangentially related to increased productivity gains. Primarily it refers to a firm's ambitions and capacity to expand its operations and its workforce. High growth SMEs are important to the economy, but this is by no means the only kind of value that small firms provide. In addition, business ambitions can change significantly over time, depending on context and other factors (BIS 2015a). Our interviewees expressed a range of ambitions and motivations other than maximising growth; these included innovation, specialisation and community motivations, as well as lifestyle and personal factors. Many SME owners want simply to run a high-quality business and provide employment for their staff.

Firms for whom high growth is not a major, or realistic, priority may therefore find it hard to access and afford support. Even those with stronger growth ambitions may first require foundational support to develop their business, their workforce, and their business plan, in order to become one of the prized 'high growth' firms.

KEY ISSUE 4: DIFFICULTY ACCESSING FINANCE

For many SMEs, access to finance, including small-scale funds, remains difficult

As discussed above, access to finance remains a key issue for many firms. In particular, small-scale loans that can be used agilely for investments to meet immediate priorities may be hard to get, especially for SMEs that do not fall into the clearly 'high growth' category. This is a particular problem given the wide range of ambitions among SME owners, and the value for communities, innovation and employment of SMEs that are not focussed primarily on growth.

Many SMEs may need assistance to develop a funding application

Several interviewees stressed that availability of funds was not the only issue, or even the main one. SMEs also need the expertise, or support, to create an effective business case or funding application. This also was identified in our study of Cumbria and Lancashire (see case study).

Large financial providers such as banks are increasingly developing services for SMEs that offer more holistic support to those who are applying for – or who might consider applying for – finance. Interviewees noted that certain intermediaries, including some accountants, provide only limited help in this area. The closure of high street bank branches, particularly in small towns and rural areas, was also identified as an issue for firms in certain places.

Case study: Family business support in Cumbria and Lancashire

In February 2019, IPPR North was commissioned by Be the Business to conduct a landscape study of support for family businesses in Cumbria and Lancashire. Not all family firms are SMEs, and not all SMEs are family-run, but there is considerable overlap between the two. Including sole traders, just under 90 per cent of all businesses in the North are majority-owned by members of the same family (IFB Research Foundation/Oxford Economics 2017).

We used desk-based research and interviews with senior stakeholders in both LEP areas, business networks, and organisations that support the regions' SMEs. Key findings include the following.

- **There was a clear focus on growth acceleration and start-ups** across all geographies in the study. Stakeholders noted that to qualify for ERDF-funded business support, SMEs must demonstrate projected business growth as an output. They also identified pressure from BEIS that encourages a tighter focus on 'high growth' businesses.
- **'Foundational support'** (to help existing businesses with VAT, HR, marketing plans etc) is much harder to obtain. Consultees were not sure what foundational support existed, either because it is simply not available or because it is poorly promoted.
- **Support for training and upskilling of staff also seems limited**. This includes apprenticeships. Many current schemes depend on ESF (ie EU) funding.
- **EU funding restrictions limit support for some sectors.** For ERDF-funded support, sector restrictions exclude parts of the economy such as retail, the nuclear industry, agriculture, and primary production.
- **Communication and engagement are significant obstacles.** Stakeholders identified promotion of the local support offer as an issue. The LEPs and growth hubs are increasing their capacity to communicate with SMEs and advertise the available support. These efforts were generally thought to be successful, but stakeholders still felt that many businesses don't know they can ask and often don't even know to look.
- **Access to finance is a key issue.** In particular:
  - there are few funds for relatively small investments below £0.5 million
  - SMEs are often unprepared to access finance; they may wait until they are 'knocked back' by lenders or investors before seeking support, rather than getting advice on how to make an effective application in the first place. Problems often relate to foundational issues like credible business planning or presentation skills. SMEs often underestimate how long it takes to overcome these barriers
  - 'soft referrals' as a response to unsuccessful applications would help to signpost SMEs to effective support, and encourage them to use it. For example, those seeking finance could be automatically referred to Growth Hub advice. Making banks, accountants, and investors aware of the available support so they that they can direct SMEs towards this early in the process would be effective
  - match funding requirements (often a part of EU funding) present a further obstacle.

In the final chapter of this report, we set out our recommendations to support increased SME productivity, based on our learning from this research.

6. RECOMMENDATIONS

Few politicians hesitate to sing the praises of small businesses. This attention is undoubtedly warranted - small businesses make up a significant part of the economy, and play an important role in local areas up and down the country.

But the policy focus afforded to small businesses comes at a price – business support to SMEs has been characterised for years, if not decades, by sudden and substantial changes, nationally and locally. Many initiatives have been short-term and small scale, and targeted at only a sub-group of businesses. The outcome of this is a complex and shifting business support landscape, which increases uncertainty and makes it much harder for institutions to 'bed in'.

With this in mind, and conscious of the continued and substantial uncertainties posed by Brexit, we do not propose any radical redesign of the current system of business support. Instead, our proposals build on existing institutions and initiatives, rather than creating a portfolio of new policies. What is needed is for the government scale up existing initiatives by providing resource commensurate with the size of the North's SME population, and the potential economic gains from boosting SME productivity.

These recommendations draw largely on our primary research with regional SMEs and other stakeholders, reflecting common concerns and examples of good practice. They are designed to support increases in productivity for SMEs in the north of England, by:

- improving access to finance,
- strengthening regional business support networks, and
- creating a local tax regime that better supports SME needs.

IMPROVING ACCESS TO FINANCE

1. **As part of its industrial strategy, the government should substantially increase funding for the British Business Bank. Tony Dolphin and David Nash (2012) proposed a capitalisation of £40 billion over four years – we echo this recommendation.**

The British Business Bank (and, within it, the Northern Powerhouse Investment Fund) can help to boost SME productivity in the North by improving access both to finance and to wider support, either directly or by signposting. To achieve this, the following action should be taken.

- Government should increase BBB and NPIF funding by a significant order of magnitude and over the long-term, going well beyond replacement of current EU support.
- The BBB and NPIF should be tasked with an explicit focus on investment to boost productivity, particularly within the long tail of small firms, including those in the 'everyday economy'. The focus to date has been on 'high growth' firms.
- The BBB should be given a remit to develop a stronger regional presence. Over time the government should develop it into a full-scale network of regional investment banks.

2. **Small-scale support, including support with 'minor' financial costs should be a key part of business support.**

To promote this:

- the funding available from government sources should include accessible, small-scale grants and loans to support small-scale investments that can make a difference to business productivity and resilience
- state providers should make sure that this is offered alongside guidance on preparing funding applications *and* on the effective use of such funding; and growth hubs should provide guidance for other funders (such as banks) to make them aware of the local support offer, and to encourage them to refer SME applicants to support to develop their funding application, rather than rejecting them outright.
- stakeholders such as financial providers should be encouraged to provide 'in-kind' support that reduces costs and supports networking for SMEs, such as subsidised co-working spaces, technological support with networking, and 'bite-size' training.

STRENGTHENING REGIONAL BUSINESS SUPPORT NETWORKS

3. **The government should provide a long-term financial settlement for LEPs to fund growth hubs – and should increase the total funds available from £12 million to £60 million per year, which should be reviewed as growth hubs increase their size and capacity.**

£60 million is a tiny sum compared to the overall government spending through various channels to boost SME productivity – and, given the evidence of the potential gains to the economy through well designed business support, this investment is more than likely to pay for itself.

In addition, the NP11 group of LEPs, and their respective growth hubs, should continue to develop ongoing pan-regional collaboration in best practice and joint working and to formalise working arrangements into a 'Northern Business Hub'.

The Northern Business Hub would:

- identify and address unnecessary duplication in business support
- share best practice and develop peer challenge between growth hubs
- improve the visibility and accessibility of growth hubs in the North
- encourage and support individual growth hubs to develop a collaborative and place-based approaches to local business support, drawing on the direct and in-kind support available elsewhere, such as in universities, and by banks and independent providers
- encourage and support the use of co-investment and fund sharing mechanisms within the apprenticeship levy.

4. **Local leaders should develop a comprehensive gap analysis, via their growth hub, of the local SME support market to inform their local industrial strategy.**

This should include scoping out whether sufficient opportunities exist that are accessible, practical and tailored to needs in the following areas.

- management and leadership training for SMEs
- mentor support, with training and networking for mentors to ensure good matches and quality of provision
- support for exporters, including potential and expanding exporters, tailored to the local economy and its opportunities

- development of digital skills and the skills needed for embedding digital in businesses across the economy.

5. Northern Local Enterprise Partnerships should consider increasing small business representation in their decision-making

Increasing the representation of SMEs on LEPs would better reflect the size of the contribution of small businesses to their respective economies, their diverse profile and needs, and would help to ensure business support, and wider policies designed to boost economic growth, are targeted effectively. Measures to increase representation could include, for example, voluntarily increasing the number of SME representatives on LEP boards (LEPs are currently obliged to have a 'small business champion' on their boards), or creating a dedicated SME sub board or advisory group to inform the LEP's decision-making.

6. As part of its industrial strategy, central government should establish a 'Universities Business Support Fund', in order to resource universities to establish dedicated technology transfer and business support functions including facilitation expertise.

This should support two core functions.

- **Knowledge transfer hubs**, where expert facilitators identify how university research can help to address problems or seize opportunities among SMEs, and built relationships between SMEs and researchers in order to put this into practice.
- **Business support and training for SMEs in their region**. This should be well-publicised in collaboration with growth hubs, drawing on expertise within the university that can meet the sector-specific and generic needs of regional SMEs.

Knowledge transfer hubs should be networked across the UK, to facilitate opportunities and potential collaborations out of region, and partnerships between SMEs and larger businesses. The German Steinbeis Foundation (Steinbeis 2019) offers a possible model that could be adapted in the UK context.

CREATING A LOCAL TAX REGIME THAT BETTER SUPPORTS THE NEEDS OF SMES AND LOCAL GOVERNMENT

7. Government should commit to a full redesign of the business rates system, informed by an awareness of the importance of SMEs in regional economies including their contribution to GVA, growth, innovation, employment, quality of place and communities. In particular, this should take into account the costs imposed by business rates that put some SMEs off of locating in locations with high rateable values, including city centres. Any new system should also ensure a long-term and sustainable source of income for local government.

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