SME FINANCE MONITOR: THE SCALEUP PERSPECTIVE

JULY 2017

Acknowledgements

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Contents

Introduction
Irene Graham, CEO, ScaleUp Institute **4**

Insight
Rebecca McNeil, COO Barclays Business Bank and Chair, Commercial Product and Service Board, UK Finance **5**

Research
Shiona Davies, Director, BDRC Continental **6**

Insight
Keith Morgan, CEO, British Business Bank **18**

Insight
Toby Austin, CEO and co-Founder, Beauhurst **20**

Concluding Remarks
Marcus Stuttard, Head of AIM, London Stock Exchange **21**

Introduction
Irene Graham, CEO, ScaleUp Institute

The contribution of scaleup businesses to the health and dynamism of the UK economy is being increasingly realised. Scaleups matter because they are across sectors, in every area of the country and are generators of exports, jobs and growth in our local communities. They are a prime source of today's jobs and tomorrow's.

This document brings together new analysis of the independent SME Finance Monitor to provide further demographic insight into this vital segment of UK business. The snapshot also compares them with the wider national population of small and medium-sized enterprises.

This new analysis reinforces the fact that scaleups come from all business sectors and geographic regions and that they are more likely to be innovative and international in their business, than their counterparts, with greater ambition and plans for further growth.

Whilst the overall economic climate is not a primary concern for them this analysis reinforces that scaleups view the greatest barrier to growth as recruiting and retaining staff; followed closely by management/leadership skills, availability of relevant advice, access to prompt payment and options of finance.

The analysis allows us to better understand the makeup of these businesses and their overall attitude towards finance and growth. We see a driver of scaleup status is innovation in service, markets and products and often an owner/ manager under 50. Scaleups also tend to be more profitable.

Although scaleups are more willing to use external finance to help them grow, **four out of ten** choose not to access it. It demonstrates that scaleups require confidence and support to help them in their growth journey. There is a clear need to ensure that business leaders can access finance and understand their available options. It is important to increase the provision of education on growth finance so that scaleup leaders understand – and are aware of – all the available options so they can structure their companies appropriately.

There are some important and constructive points that can be drawn by the financial community from these latest findings: it shows that further thought should be given to the nature of the support that the financial community provides to scaleup businesses. Scaleups are not just looking for cash – they want smart money which brings knowledge and support along with it.

We are fortunate to have very many capable ambitious business leaders innovating to provide customers with better services than before. Growing pains in companies that are scaling are inevitable and we all have a role to play in breaking down the barriers that exist to allow their growth to flourish in every city and area of the country. This report gives key insights which we can act on. We hope it will be used by national and local financiers, policymakers, educators and industry in their work. As we consider the next steps of a modern industrial strategy and the Patient Capital Review, it is critical that we establish the right local and national frameworks to allow scaling businesses to flourish.

Insight from Banking Industry
Rebecca McNeil, COO Barclays Business Bank and Chair, Commercial Product and Service Board, UK Finance

The banking industry supported the independent development of the SME Finance Monitor which has provided comprehensive analysis of lending and the availability of external finance for the UK SME market since 2011. Its data and insights have enabled the industry to develop finance propositions that reflect the needs of modern SMEs.

This report gives us useful further indications about how the banking industry can interact with other players in the financial ecosystem to really "lean in" to help scaleups. The banking industry currently supports scaleups with a range of loan and debt finance products, as well as through the establishment of new finance vehicles such as the BGF, Venture Debt, British Business Bank etc. However, it is evident we can collaborate even more with equity finance providers and emergent fintech companies so that we can provide joined-up support for scaleups, as well as comprehensive and timely education about the finance options available to them.

This report has given us further insights to our scaling businesses which we can act on, including the importance of getting timely guidance which we will consider further as we evolve the mentoring services offered under Mentorsme.

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SME FINANCE MONITOR
SCALEUP INSIGHTS

Shiona Davies, Director, BDRC Continental

bdrc continental

Background and definitions

The SME Finance Monitor has been providing robust and respected data on SMEs since 2011. All respondents were SMEs interviewed on the SME Finance Monitor in 2015 or 2016. Within this data set, recent scaleups and "aspiring" scaleups were identified:

	Definition	Interviews
Scaleups	SMEs who report turnover growth of 20%+ in the previous year and in each of their preceding two years	2,202
Aspiring	SMEs who have grown by 20%+ in previous year but not in the prior two years, and who are planning to to grow by 20%+ in the next year	553
SMEs (comparison group):	All SMEs, excluding new starts, who have not scaled their business	32,030

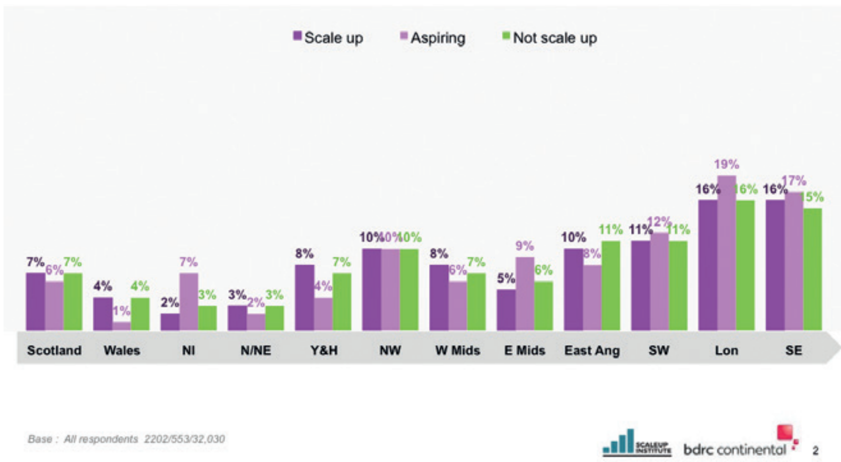
ABOUT SCALEUP SMEs

5% of all SMEs trading for more than 2 years meet the definition of a scaleup and a further 1% are aspiring scaleups. Scaleups are found across all regions and sectors. They are typically younger businesses, with younger owners. They are likely to be profitable and more likely to have employees.

Scaleups are across all areas of the country and there is little difference in regional profile between scaleups and other SMEs. Aspiring scaleups are somewhat more likely to be found in London or Northern Ireland:

There is little difference in distribution of scaleups across England and the devolved nations

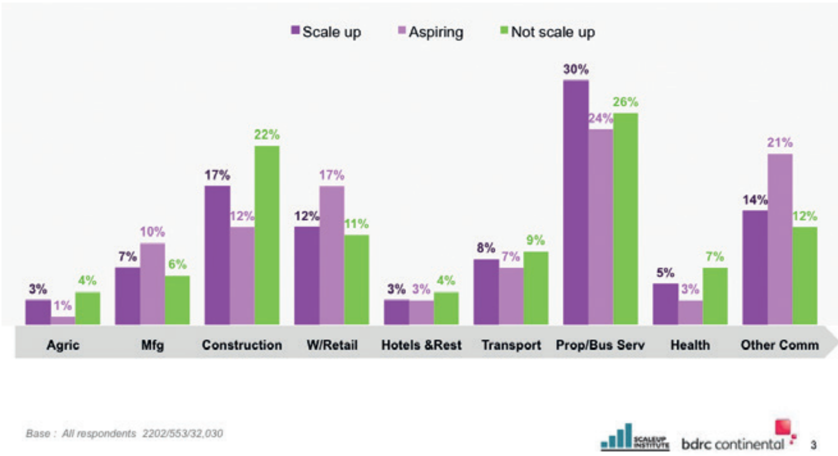
Region 2015-16



Scaleups are found across all sectors of the economy including property, manufacturing, agriculture, business and retail services:

Scaleups are somewhat less likely to be in Construction and more likely to be in Property/Business Services

Sector 2015-16

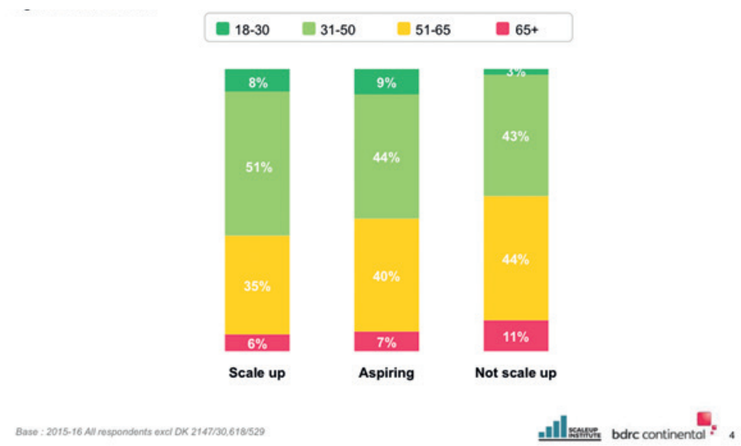


Scaleups are typically, but not exclusively, younger businesses. 6 in 10 (58%) have been trading for 2-9 years, compared to 4 in 10 (36%) of other SMEs. While the findings suggest that scaleup growth is more likely to occur earlier stages of a company's life, it should be noted that a **quarter of both scaleups and aspirationals have been trading for 15 years or more.**

Scaleups and aspirationals are also more likely to have a younger owner. 6 in 10 scaleups (59%) have an owner or MD under 50 compared to 46% of other SMEs:

Scaleups are also somewhat more likely to have an owner/MD under 50. Aspiring scaleups also somewhat younger

Age of owner 2015-16



Most SMEs are profitable, and this is slightly more likely to be the case for both scaleup and aspiring scaleup SMEs (89%) compared to other SMEs (82%). Scaleup and aspiring scaleup SMEs are also more likely to have employees (40% and 36% compared to other SMEs 29%) and to be family owned (26% and 24% compared to 19% of other SMEs).

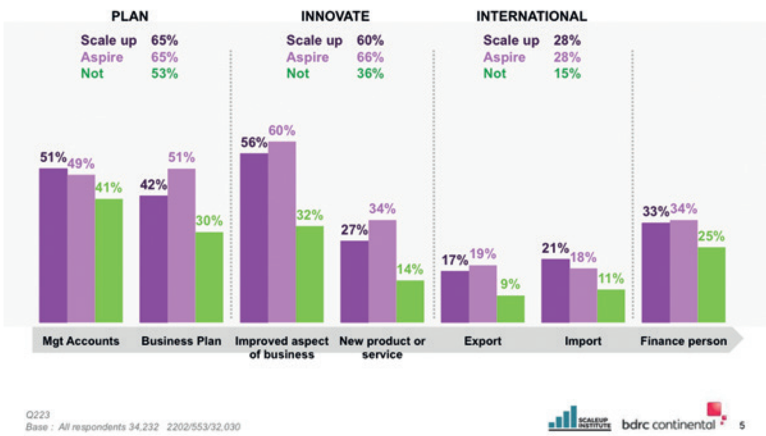
RUNNING A SCALEUP BUSINESS

Scaleups are more likely to plan, be innovative and be international

Innovation is a key determinant of being a scaleup (ie they have improved aspects of their business, and/or have launched new products or services).

Scaleups are much more likely to be innovative, international and plan than their peers, as are Aspiring scaleups

Business structure 2015-16



Scaleups are **twice as likely as their peers to have innovated** in the past three years (60% v 36%). Aspiring scaleups are the most likely to have been innovative (66%).

Scaleups and Aspiring scaleups are **twice as likely to be trading internationally** as their peers (28% v 15%).

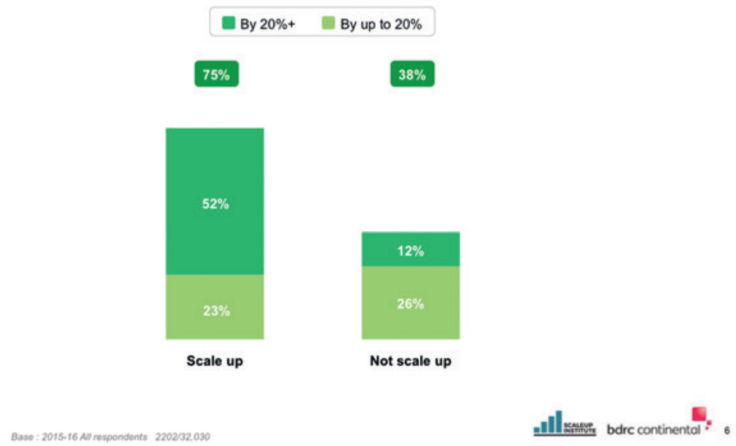
Scaleups and Aspiring scaleups are also **more likely to plan** (65% v 53%). They are more likely to produce management accounts and have a business plan than their SME counterparts.

Most scaleups are ambitious to continue to grow in the year ahead.

Scaleups have ambitions to grow their business further (by definition, all aspiring scaleups plan to grow by 20% or more).

Building on their scaleup growth, most scaleups expect to grow again in the coming year, with half planning to grow by 20% or more

Plans to grow 2015-16



Having already grown by 20% or more in the previous three years, more than half of them (52%) expect to achieve similar rates of growth in the coming year and 23% expect to achieve growth – but by less than 20%. This ambition compares to the SMEs where 38% plan to grow and just 12% plan to grow by 20% or more.

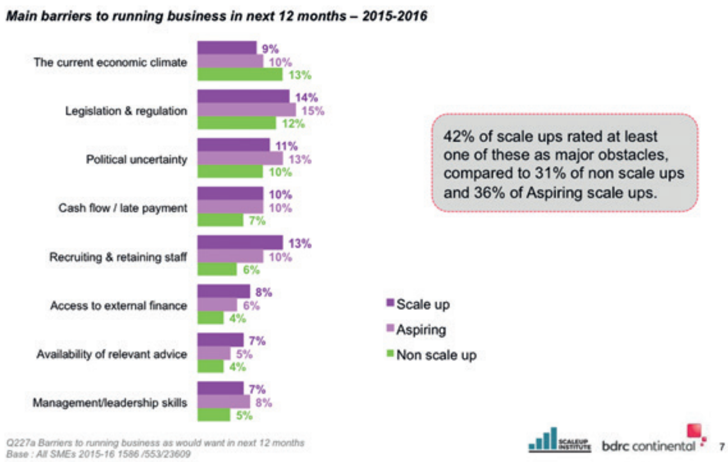
Amongst all those planning to grow, selling more in UK markets is the main way to achieve this (85% v 87%). Scaleups are somewhat more likely to say growth will come from new markets, either at home or abroad (31% v 25%).

Although they are ambitious, scaleups still identify barriers to their business. They are more concerned about recruiting and retaining staff.

Although they are ambitious, scaleups still identify barriers to their business performing as they would wish. 4 in 10 (42%) identified at least one major barrier compared to 36% of aspirational scaleups and 31% of other SMEs.

Scaleups are somewhat more likely to identify major barriers to running the business, notably recruiting and retaining staff

Main barriers to running business in next 12 months – 2015-2016



Scaleups are more likely to mention recruiting and retaining staff, cash flow, availability of advice and management/leadership skills as barriers. In 2016, 20% of scaleups rated at least one of these factors as a major barrier compared to 14% of other SMEs.

Regional barriers for scaleups

15% saw legislation/regulation as a barrier: 23% in the South West and 20% in the West Midlands

13% saw staff as a barrier: 19% in the East Midlands and 17% in London

10% saw cash flow and late payment as a barrier: 20% in NI and 19% in London

11% saw the political uncertainty as a barrier: 16% in the South West, 15% in London and 14% in the North East

9% saw the economic climate as a barrier: 19% in the South West and 16% in the North East

8% saw access to finance as a barrier: 15% in London, 14% in NI and 13% in the South West

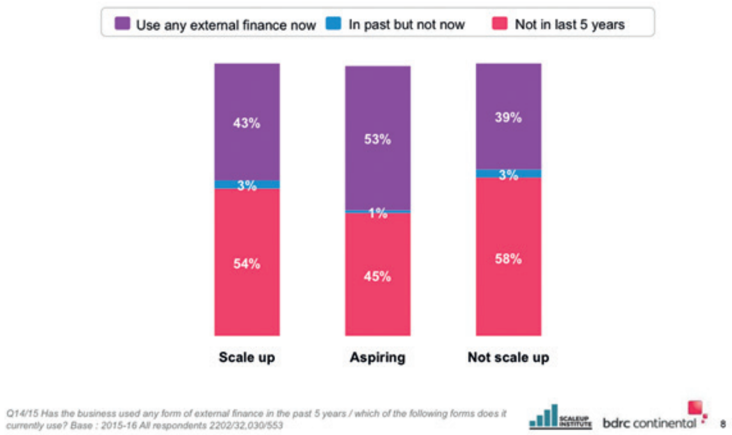
FINANCE AND SUPPORT

Scaleups are slightly more likely than SMEs to be using external finance and business funding. They are more willing, attitudinally, to use finance to grow but 40% are permanent non-borrowers.

Scaleups are slightly more likely to be using external finance, while aspirational scaleups are much more likely to be using finance.

Scaleups are slightly more likely to be using external finance, Wannabes much more likely

Use of external finance – now and in past 5 years 2015-16



One-third (32%) of scaleups and other SMEs are using one or more forms of core finance (loans, overdrafts and credit cards). Aspirational scaleups are more likely to be using these core forms of finance (41%), led by a higher use of overdrafts.

Adding in personal finance and trade credit results in 7 in 10 scaleups (71%) and aspirational scaleups (72%) using any form of "business funding" compared to 63% of other SMEs.

Permanent non-borrowers are those SMEs that are not using finance and have shown no appetite to do so. Almost half of non-scaleup SMEs meet this definition (46%), with scaleups slightly less likely to do so (39%).

Attitudes to finance amongst scaleups are not that different to their peers, with the exception of their willingness to use finance to help the business grow (55% v 42% of other SMEs). 50% of aspiring scaleups are also willing to use finance to grow.

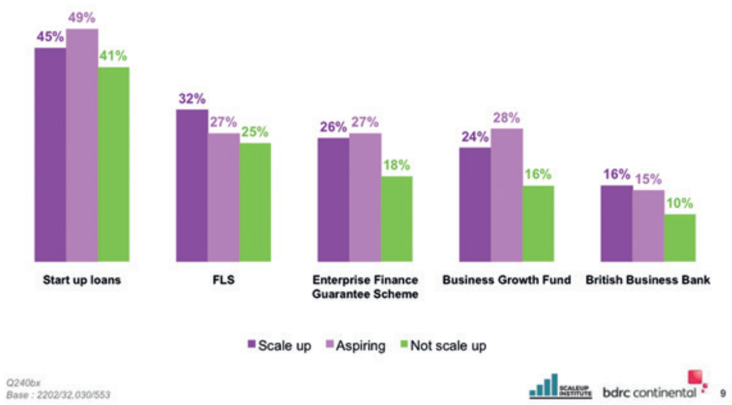
Scaleups have a stronger future appetite for finance and better awareness of various finance initiatives

Scaleups and aspiring scaleups are more likely to be planning to apply for finance (22% and 23% v 12% of other SMEs). They are less likely to be looking for funding for cashflow; instead they want funding for plant and machinery, premises or international growth. Scaleups are though somewhat less confident that their bank will agree to their future request (42% v 60% of other SMEs).

A range of initiatives are available to SMEs to support them accessing finance. 7 in 10 Scaleups and aspiring scaleups are aware of any of the initiatives tested compared to 6 in 10 other SMEs:

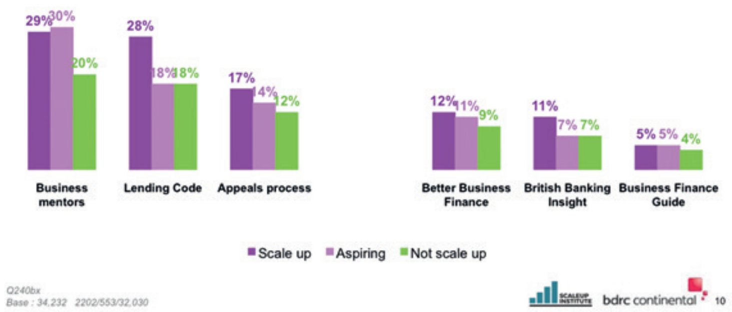
6 in 10 scaleups and aspiring scaleups were aware of one or more of these initiatives, compared to half of non-scaleups

Awareness of initiatives– 2015-16:



Scaleups and aspiring scaleups were also more likely to be aware of one or more of these initiatives

Awareness of initiatives– 2015-16:



Scaleups and aspiring scaleups are also more likely to at least consider using crowd funding or other peer to peer lending.

Larger scaleups

Larger scaleups (ie those with 10-249 employees) make up 7% of those identified on the SME Finance Monitor. Some of the differences between larger and smaller scaleups will reflect their being larger businesses, rather than being larger scaleups per se. This factor should be considered in this analysis.

Attitudinally, larger scaleups appear to be more engaged with finance. They are less likely to to accept a slower rate of growth rather than borrow to grow. They are less likely to say that their plans are based on what they can afford to fund.

LARGER SCALEUPS ARE MORE LIKELY THAN SMALLER SCALEUPS TO:

- Use business funding (86% vs 69%)
- Plan (85% vs 63%)
- Have a minimal/low risk rating (67% vs 22%)
- Be innovative (67% vs 60%)
- Use finance (63% vs 41%)
- Have been trading for 15+ years (48% vs 23%)
- Trade internationally (37% vs 28%)

THERE ARE MANY FACTORS TO WHICH LARGER AND SMALLER SCALEUPS GIVE SIMILAR RESPONSES.

- Making a profit (94% vs 89%)
- Aware of finance initiatives (72% vs 69%)
- Happy to use finance to grow (59% vs 55%)
- Planning to grow by 20% or more next year (53% v 52%)
- Aware of crowdfunding (both 46%)
- Having a borrowing event (28% v 22%)
- Planning to apply for finance in future (23% vs 21%)
- See recruitment/retention of staff as future barrier to growth (14% vs 13%)

Scaleups led by women

SCALEUPS ARE LED BY WOMEN AND ANALYSIS SHOWS THAT SUCH SCALEUPS ARE MORE LIKELY THAN THOSE LEAD BY MEN TO:

Plan (72% v 63%)

Innovate (65% v 59%)

Be a permanent non-borrower (50% v 37%)

See recruiting and retaining staff as a major barrier (16% v 12%)

Be in the health sector (12% v 4%)

As amongst women-led SMEs overall, women-led scaleups are less likely to be using finance (36% v 45%), and somewhat less likely to have applied for it (19% v 23%) or to plan to apply for it (16% v 23%).

Scaleup snapshot

SCALEUP INSTITUTE

5% of all SMEs trading for more than two years have achieved recent scaleup growth and a further 1% aspire to be a scaleup. Aspiring scaleups share many characteristics in common with those who have achieved scaleup growth

Scaleup SMEs are found across all regions and sectors

	Scaled up	Non scaled up
North England	21%	20%
Midlands	23%	24%
South England	43%	42%
Devolved Nations	13%	14%
Manufacturing	27%	32%
Retail/Distribution	20%	20%
Services	52%	49%

They are more likely to do the "good things"

	Scaled up	Non scaled up
Plan	65%	53%
Trade Internationally	28%	15%
Innovative	60%	36%

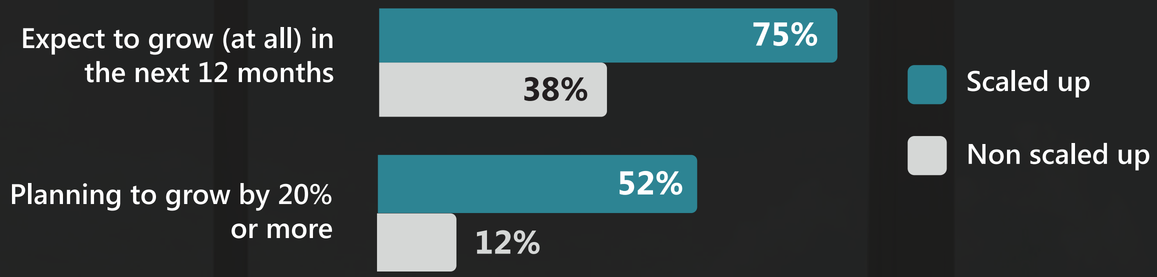
Scaled up

Non scaled up

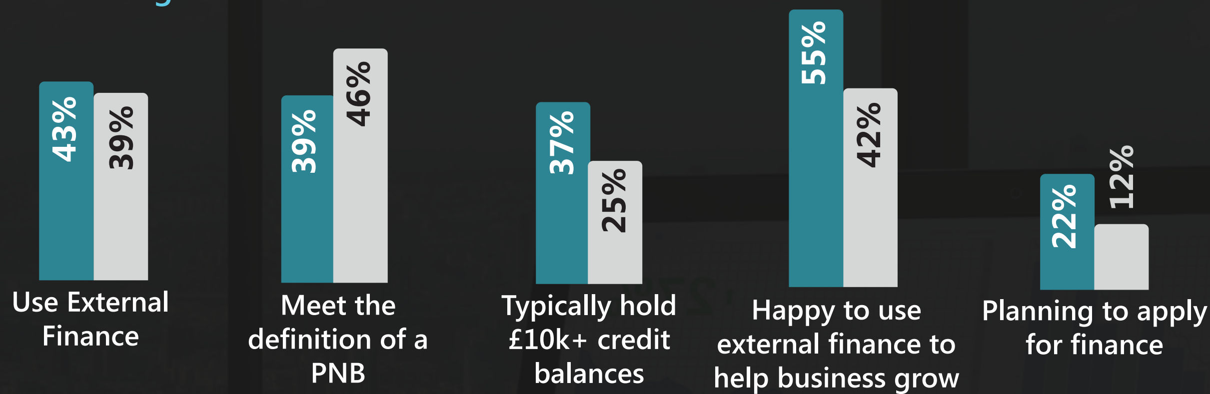
It's not all plain sailing...

	Scaled up	Non scaled up
More likely to identify at least one barrier to running the business	42%	31%
More likely to identify recruiting and retaining staff as an issue	13%	6%
More likely to identify cash flow or late payment as an issue	10%	7%
More likely to identify access to finance as an issue	8%	4%
More likely to identify availability of advice as an issue	7%	4%

They have not finished growing yet



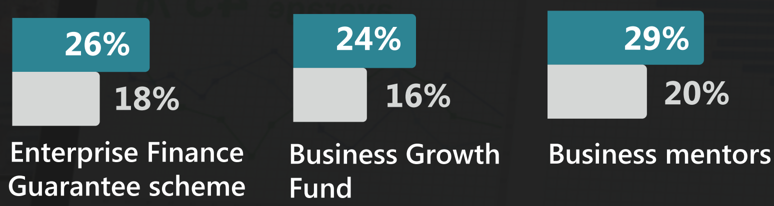
Despite all this growth they are not dramatically heavier users of external finance, but they are a bit more open to it – although a third managed to scale whilst being a Permanent non-borrower*



They do have better awareness of the various initiatives available to help businesses

69% were aware of any of the initiatives tested (v 60%)

Key differences:



Spotting a scaleup

Analysis shows that the following factors are more likely for scaleups:

- Being innovative
- Having a younger MD/owner
- Having £10k or more of credit balances
- Seeing recruitment and retention of staff as a barrier (but not the economic climate)

Data drawn from the BDRC Continental SME Finance Monitor 2015-16 which included 2202 interviews with SMEs that had scaled. Aspiring scaleups had grown by 20% or more in the past year and planned to grow by 20% or more in the following 12 months and 553 were interviewed in 2015-16. BDRC Continental has published this independent report since its launch in 2011 and it is used by banks, Government and industry bodies to inform the debate on access to finance for SMEs.

**Permanent non borrowers are those SMEs that by their answers indicate that they are not using, and have no immediate appetite to use, external finance.*

bdrc

Insight
Keith Morgan, CEO, British Business Bank

To better understand SMEs' attitudes to finance, particularly regarding their underlying needs and openness to receiving information, the British Business Bank has recently commissioned analysis using data from the SME Finance Monitor.

Two factors were used to interpret the statistical cluster analysis:

- SMEs' confidence in their own abilities, such as their confidence in assessing and applying for finance, and whether the person in charge of financial management has an appropriate qualification/training.
- SMEs' perceptions of opportunities and threats, relating to their level of need in terms of whether they are planning to grow or undertake innovative or international activity. It also considers whether they perceive any obstacles to their business and if they have previously been rejected by a bank.

The analysis has resulted in the British Business Bank concluding on four key SME segments of which scaleups feature in the 'savvy entrepreneurs' and 'quicksilver' categories. Going forward the BBB intends to put increased focus upon these segments when considering how to provide information on finance options to SMEs.

SME MARKET SEGMENTATION:

CONTENTED
62%

Undemanding and unworried. The least innovative and international, and with the lowest growth ambitions. Relatively financially confident, but not informed

FIGHTERS
12%

Trying to overcome obstacles and grow. Tend to be somewhat ambitious, international and innovative. Most likely to report obstacles to running their businesses, including those relating to cashflow, skills, politics, the economy and access to finance

SAVVY ENTREPRENEURS
10%

Innovative, international and formal. The most confident in their own abilities to assess finance options. Most likely to have a financial qualification

QUICKSILVERS
16%

Growing, successful, but somewhat vulnerable. The fastest-growing businesses with the most ambitious growth plans. Relatively international and innovative. Somewhat confident in their abilities to assess financial options and relatively more likely to employ someone with a financial qualification. Nevertheless, have had some issues with previous rejections by a bank.

British Business Bank, 2017

Companies that are “permanent non-borrowers” were excluded from the analysis, around half of SMEs.

BRITISH BUSINESS BANK

Insight
Toby Austin, CEO and co-Founder, Beauhurst

At Beauhurst, we track the UK's fastest growing companies by identifying those that meet triggers indicative of growth and the potential for further growth – these triggers include equity investment, graduation from accelerators, MBOs and, as of 2017, meeting the OECD criteria for scaleup firms.

In partnership with the ScaleUp Institute, we are currently researching all UK companies which meet the scaleup criteria. While this study is ongoing – 3270 scaleups have been analysed so far – several clear patterns are emerging and they are consistent with the findings of earlier research.

- Of the scaleups that have used equity finance, the greatest number are in London, the South East, and the North West.
- The next most populous regions for scaleups using equity finance are the East of England, Yorkshire & Humberside, and the South West.
- The top equity investor into scaleups is BGF followed by Index Ventures, Draper Esprit, Lloyds Development Capital, Notion Capital.
- Scaleups raised £1.7bn from equity investors in 2016.
- Scaleups are across all sectors of the economy and the majority are outside of pure technology sectors.
- Leading sector using equity is Software-as-a-Service.
- The percentage of scaleups using equity is circa 14% – so there is much more work to encourage others to consider it as an option for growth.

Beauhurst

Concluding Remarks

Marcus Stuttard, Head of AIM, London Stock Exchange

It is clear from this report that the UK's scaleups and aspiring scaleups are our innovators and exporters and businesses which plan to grow even further.

The increase in the overall number of SMEs in the UK economy is positive but, in order to help more of these companies to scale up, there is a need to package a suite of services to support their growth, alongside making sure that we help scaleups understand the benefits of growth capital and how to access it.

For many of our fastest growing businesses – and those with the potential to be high-growth – this means access to long-term patient equity capital, which enables capital to flow directly from investors to innovators.

The economic potential of patient equity capital is clear: when the Government made shares on AIM (London Stock Exchange Group's international growth market which has raised £100bn for over 3,700 high growth companies) eligible for ISA inclusion, more than £4bn flowed into these companies. The private sector finance community can also signal its support for scaling businesses beyond the provision of capital.

Scaleups do not just need appropriate growth capital for their success. They need mentorship and the networks and support systems that investors and intermediaries can offer. They also need to develop their leadership and management skills to enable them to make informed decisions to support them in growing their business effectively.

We believe there needs to be a stronger connection between the finance community and local areas, providing tailored solutions to businesses where they are based. That is why we have created the international business support and capital raising programme, ELITE and through a team of regional account managers in the UK work closely with local communities, including LEPs and business groups, as we seek to encourage the understanding and use of growth capital in its many forms.

Going forward we are committed to continuing to work closely with the finance community, the Government (including the export, finance and innovation agencies), and industry groups, to better join up finance options at a local level, as well as showcase scaleup success stories across the country through initiatives such as our annual 1000 Companies to Inspire Britain report.

Working together in a coordinated manner across the public and private sector will be key if we are to make sure that our scaling businesses thrive in the UK and international environment where they can reach their fullest potential. We must build on the success of what works today, as well as reduce the barriers that continue to exist.

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