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SMALL BUSINESS IN THE UK: A REPORT FOR NATIONAL WESTMINSTER BANK

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1. ECONOMIC BACKGROUND

The Country

The United Kingdom of Great Britain and Northern Ireland (UK) covers some 94,000 square miles (242,494 square kilometres). It consists of:

	Area (Square kilometres)	Population (1986)	Persons per sq. km
England	130,439	47,254,000	362.3
Northern Ireland	14,120	1,566,800	111.0
Scotland	77,167	1,566,800	66.4
Wales	20,768	2,821,000	135.8

Population

1986: 56,763,300

Population growth 1981-1986: 0.7%

Population projection 2001: 58,957,000

Government

The Queen is the constitutional monarch. In practice the Queen's role is purely formal. In all important matters she acts on the advice of her ministers.

Parliament - the legislature - consists of the House of Lords and the House of Commons. The House of Lords has over 1,000 peers of whom over 800 are hereditary. No new hereditary peers have been created since 1964. The functions of the House of Lords are:

(a) Legislation. Its role here is limited under the Parliament Acts.

(b) Debate.

(c) To act as the highest Court of Appeal (but only the 'law' lords take part in legal proceedings).

The House of Commons consists of 650 Members of Parliament (MPs). All MPs are elected to represent single member constituencies. The main function of the House of Commons is legislation, and its

importance in this area is paramount. A secondary function of the House is to scrutinise government activities through a complex structure of standing and select committees.

The executive work of central government is through the Prime Minister and other Ministers of the Crown. Control is exercised through the Cabinet which consists of ministers selected by the Prime Minister. The Cabinet assumes collective responsibility for government policy. Most Cabinet ministers are heads of government departments.

The policy of the government is administered by the Civil Service (a body of permanent officials).

Local government in the UK is created by Parliament. The structure is different in both Scotland and Wales from that in England. In broad terms, however, there are three levels of authority throughout. They are:

1st tier - County Councils.
2nd tier - District Councils and London Borough Councils.
3rd tier - Parish and Community Councils.

Economy

The UK economy in recent years has been characterised by a rising gross domestic product per person, rising average earnings and increasing levels of personal disposable income. At the same time the level of unemployment is at an unacceptable level. There is also a growing balance of payments crisis with the value of imports being greater than the value of exports. In order to stem these financial problems Government has raised interest rates in order to dampen down the demand for imported products.

Gross Domestic Product (expenditure based at factor cost: current prices)	
Total GDP 1986	£326,049 million
Growth total GDP 1985-86	6.4%
Total GDP per head 1986	£5,597
Growth in total GDP per head 1985-86	10.0%
Total GDP at 1980 prices in 1987	270.65
Growth in total GDP at 1980 prices 1987-86	3.6%

Annual Inflation Rate	
Annual consumer prices (1980=100) in 1987	152.5
Growth in annual consumer prices 1986-87	4.2%

Average earnings for all employees in employment 1987	£199.8
Growth in earnings 1986-87	7.8%
Real personal disposable income at 1980 prices in 1987	£ 180,759 million
Growth in real disposable income 1986-87	3.3%
Registered Unemployed October 1987	
Number	2,751,384
Rate	11.1%
Balance of payments	
Value of exports 1987	£80,089 million
Value of imports 1987	£94,016 million
Growth in unit value of exports (1980=100)	3.6%
Growth in the unit value of imports (1980=100) 1986-87	2.3%
Market exchange rate	
Exchange rate in 1987 (US $ per £)	$1.87
Exchange rate in 1981 (US $ per £)	$1.91
Lending rate 1987	9.63%
Lending rate 1981	13.25%

Income tax, primarily that on employees rather than sole traders and partnerships, generates almost 30% of tax revenue. Corporation tax generates only just over 4% of tax revenue and, even then, over a third of this represents advance corporation tax which is really a dividend withholding tax. There are three other important sources of tax revenue; social security, contributions by employers and employees (20%), value added tax (15%) and local rates (11%). Marginal rates of personal tax vary between 25% and 35%. Since the rate of corporation tax on small business (with taxable income below £100,000) is only 30%, it is generally better for businesses to incorporate at an early stage in their life. Associated with recent reductions in rates of corporate taxation there have been corresponding reductions in business allowances, primarily depreciation or capital allowances, that affect both sole traders and companies. The consequent effect has been to increase the effective taxation on sole traders and partnerships. One, unstated, objective of this shift in taxation is to encourage incorporation, with all the legal regulation and control that involves. Indeed the burden of administering the tax system generally falls disproportionately heavily upon small business. Small businesses have also to administer the pay-as-you-earn system for taxation and national insurance for all employees, and a national scheme for statutory sick pay

Sources: Annual Abstract of Statistics, 1988; International Financial Statistics, 1988; and Regional Trends 23, 1988.

2. BUSINESS REGISTRATIONS, DEREGISTRATIONS AND STOCKS

This section looks at trends in business registrations, deregistrations and stocks for different regions and industrial sectors. All data is based upon Value Added Tax (VAT) statistics published by the Business Statistics Office (Employment Gazette, 1987). Whilst this is the best data available for this purpose in the United Kingdom, it does have certain drawbacks. These are highlighted in Appendix 1.

Registrations and Deregistrations, 1975-1987

The number of businesses registered for VAT in the United Kingdom has increased consistently from 1975 to 1987, from 1.23 million at the end of 1975 to 1.51 million at the end of 1987, as illustrated in Figure 1. The size of these annual increases has varied considerably, as is shown in Table 1. Between the end of 1977 and 1978 the number of VAT registered businesses actually decreased by 6,000 which is in marked contrast to the 45,000 increase in 1987 which is the largest increase since 1979.

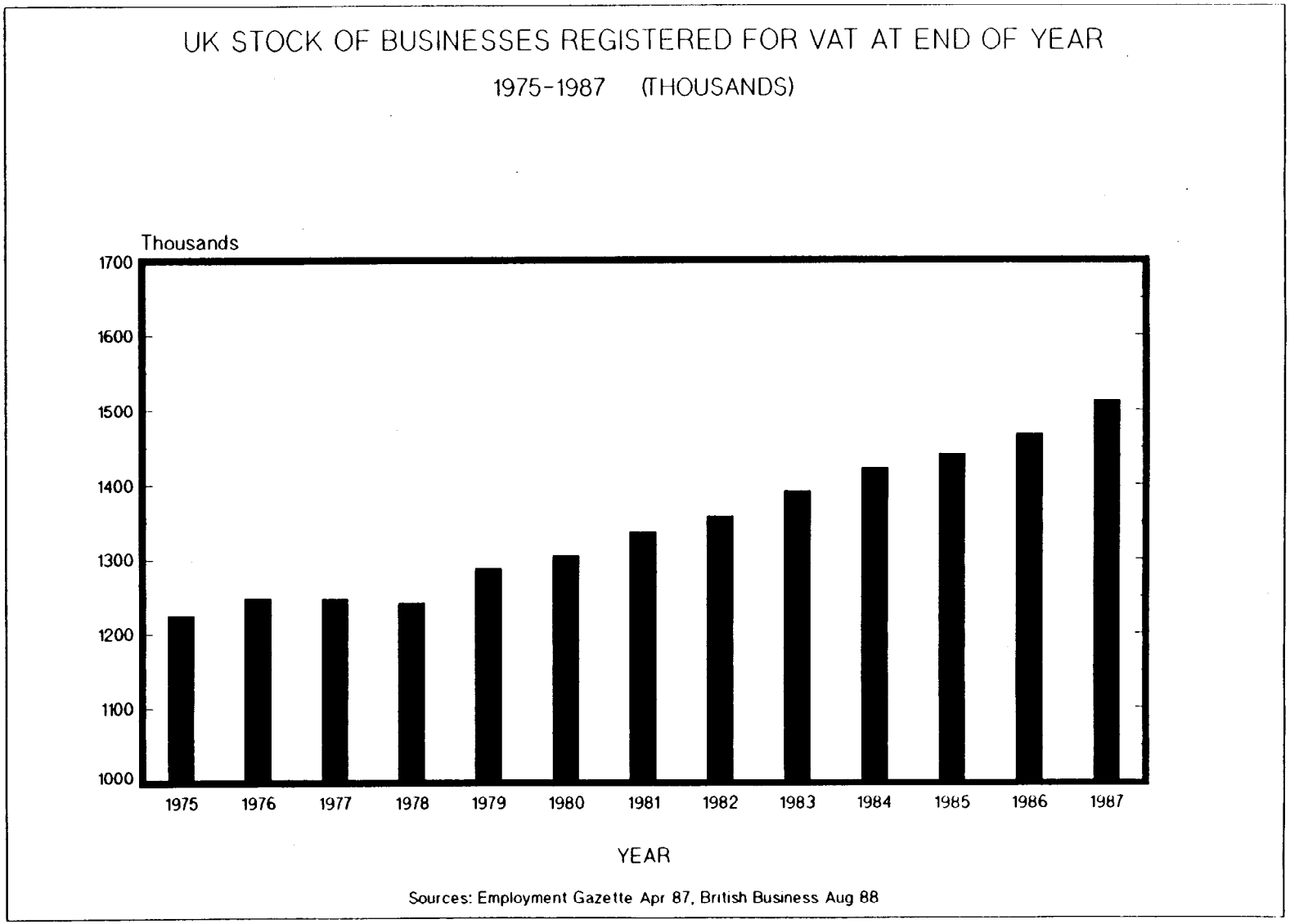
Insert Figure 1

Table 1 Business Registrations, Deregistrations and Stocks in the UK: 1980-1987 (thousands)

Year	Stock at start of year	Registrations	Deregistrations	Net change	Net change as a % of stock	Registrations as a % of stock	Deregistrations as a % of stock	Stock at end of year
1975	1,203.0	161.3	138.5	22.8	1.9	13.4	11.5	1,225.8
1976	1,225.8	169.0	146.0	23.0	1.9	13.8	11.9	1,248.0
1977	1,248.8	157.2	158.2	-0.1	-0.1	12.6	-12.7	1,247.8
1978	1,247.8	149.7	155.7	-6.0	-0.5	12.0	12.5	1,241.8
1979	1,241.8	171.8	125.3	46.5	3.7	13.8	10.1	1,288.3
1980	1,288.9	158.3	142.3	16.0	1.2	12.3	11.0	1,305.0
1981	1,305.0	152.1	120.3	31.8	2.4	11.7	9.2	1,336.8
1982	1,336.8	166.0	145.4	20.6	1.5	12.4	10.9	1,357.4
1983	1,357.0	180.0	145.0	35.0	2.6	13.3	10.7	1,392.0
1984	1,392.0	182.0	152.0	30.0	2.2	13.1	10.9	1,422.0
1985	1,422.0	182.0	163.0	19.0	1.3	12.8	11.5	1,441.0
1986	1,441.0	191.0	164.0	27.0	1.9	13.3	11.4	1,468.0
1987	1,468.0	205.0	160.0	45.0	3.1	10.9	10.9	1,513.0
1980-87	1,288.9	1,416.4	1,192.0	224.4	17.4			1,513.0

Sources: Employment Gazette, April 1987 and British Business, August, 1988.

Figure 1


UK STOCK OF BUSINESSES REGISTERED FOR VAT AT END OF YEAR
1975-1987 (THOUSANDS)
Thousands
1700
1600
1500
1400
1300
1200
1100
1000
1975
1976
1977
1978
1979
1980
1981
1982
1983
1984
1985
1986
1987
YEAR
Sources: Employment Gazette Apr 87, British Business Aug 88

Each increase is the net result of much larger numbers of registrations rather than deregistrations (Figure 2). The number of registrations increased substantially between 1985 and 1986, and again between 1986 and 1987 (Table 1). In 1987 the number of registrations of businesses was 205,000 compared to 160,000 deregistrations resulting in a net change as a percentage of stock of 3.1%. The number of deregistrations has remained relatively stable for the last three years.

Insert Figure 2

Table 2 shows for each year from 1974 to 1984, the proportion of those firms registered in that year which are still registered 6, 12, 18 months etc after the date of original registration. This table is therefore used to indicate the survival and failure rates of United Kingdom businesses. Three quarters of firms remain registered two years after their initial registration; one half after five years: and just under one third remain registered after 10 years, although this result can only be based on data relating to 1974 and 1975. While one may treat these results with some caution, since there is no guarantee that firms registering today will behave in the same way as those registered in earlier years the table shows a remarkable consistency in the pattern of survival from year to year. The most 'dangerous' period in a firms life - in terms of deregistration rates - is the second and third years, during which time the deregistration rate averages nearly 8% in each six month period or about 15% as an annual rate. As a consequence about one third of firms which survive their first year, subsequently deregister during the next two years. After this the deregistration rate falls away, but after ten years is still around 4%, or 8% at an annual rate. Data relating to firms which registered in 1973 suggests that the annual rate eventually steadies at around 6.7%.

Figure 2

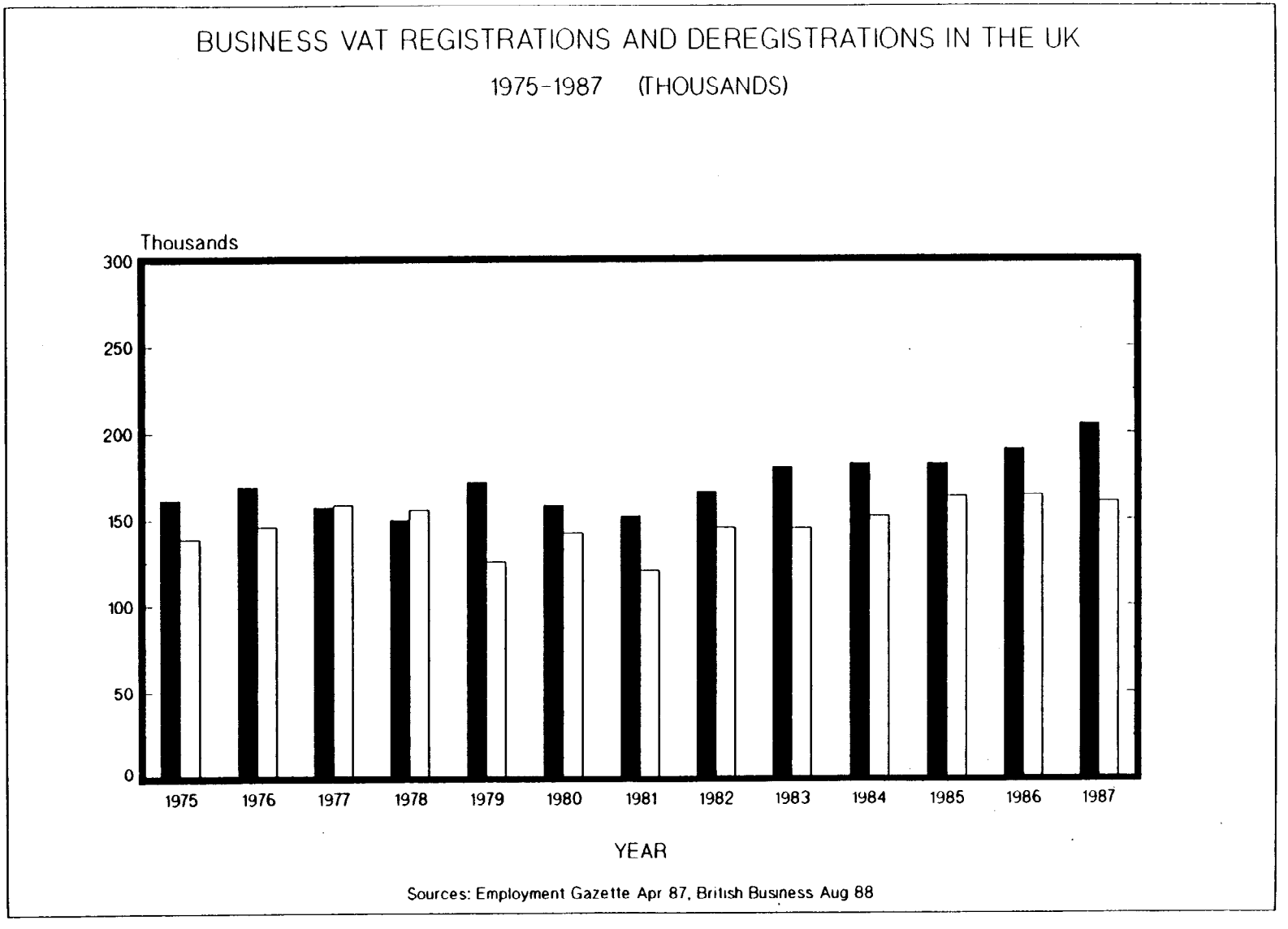

BUSINESS VAT REGISTRATIONS AND DEREGISTRATIONS IN THE UK
1975-1987 (THOUSANDS)
Thousands
300
250
200
150
100
50
0
1975
1976
1977
1978
1979
1980
1981
1982
1983
1984
1985
1986
1987
YEAR
Sources: Employment Gazette Apr 87, British Business Aug 88

Table 2 Survival of UK VAT Registrations

	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Total registrations (thousands)	148	161	169	157	150	172	158	152	166	180	182
% still registered after:											
6 months	95	96	96	95	95	95	94	95	95	95	95
12 months	88	89	89	88	89	88	88	88	88	88	88
18 months	81	82	81	80	82	80	82	81	81	81	81
24 months	74	76	74	73	76	74	75	74	74	74	
30 months	68	69	67	69	70	69	69	68	68	68	
36 months	62	63	63	64	66	65	64	63	63		
42 months	57	58	59	60	62	60	59	58	58		
48 months	53	55	56	56	58	56	56	54			
54 months	49	52	53	53	55	53	52	51			
60 months	46	49	50	51	52	50	49				
66 months	44	46	48	48	49	47	47				
72 months	42	44	45	45	46	45					
78 months	40	42	43	43	44	43					
84 months	38	41	41	41	42						
90 months	37	39	39	39	40						
96 months	35	37	37	37							
102 months	33	35	36	35							
108 months	32	34	34								
114 months	31	32	33								
120 months	30	31									
126 months	28	30									
132 months	27										
138 months	26										

Source: British Business, April 1987.

A summary of the lifespan of businesses by industrial sector is indicated in Table 3. Perhaps not surprisingly, agriculture stands out as being very different from other industries, with a much longer lifespan for registered firms. Almost two-thirds of agriculture registrations were still registered after ten years, about double the proportion in most other sectors. Among the non-agricultural industries, businesses in 'property, finance and professional services' tend to remain on the VAT register for longer than businesses in other industries (it took nearly six years before half had deregistered), while transport and retailing tend to be registered for below average periods (half of them being deregistered after about four years).

Table 3 Comparison Between Industries of Time on VAT Register

Industrial sector	Months until one quarter deregistered	Months until one half deregistered	Per cent still registered after 10 years
Agriculture	88	>120	62
Production	24	60	33
Construction	25	64	30
Transport	19	47	26
Wholesale	21	59	31
Retail	21	48	24
Property, finance and professional services	29	71	34
Catering	23	51	28
Motor Trades	20	52	30
All industries	24	60	30

Note: These estimates are based on the experience of all firms registering in the years 1974 to 1984.

Source: British Business, April 1987.

Regional Variations, 1980-1986

Between the end of 1979 and the end of 1986, there was a net growth in the number of registered businesses in each region of the United Kingdom. This is illustrated in Figure 3 which indicates that the South East has recorded an increase of 79,200 businesses which is a level of increase four times its nearest rival the South West (an increase of 17,400 businesses). Modest increases have been recorded in the peripheral areas of the United Kingdom such as the North, Wales and Northern Ireland. Each region showed an increase in each of the seven years, apart from small declines in Wales.

Insert Figure 3

Table 4 gives details of this net increase in registrations. In the South East the net increase of 79,200 businesses was made up of 470,700 registrations and 391,500 deregistrations. This represents an 18.9% increase in the stock of businesses - the largest increase in any region. The smallest increase, as a proportion of total stock, was the 7% increase recorded in the North West.

Figure 3

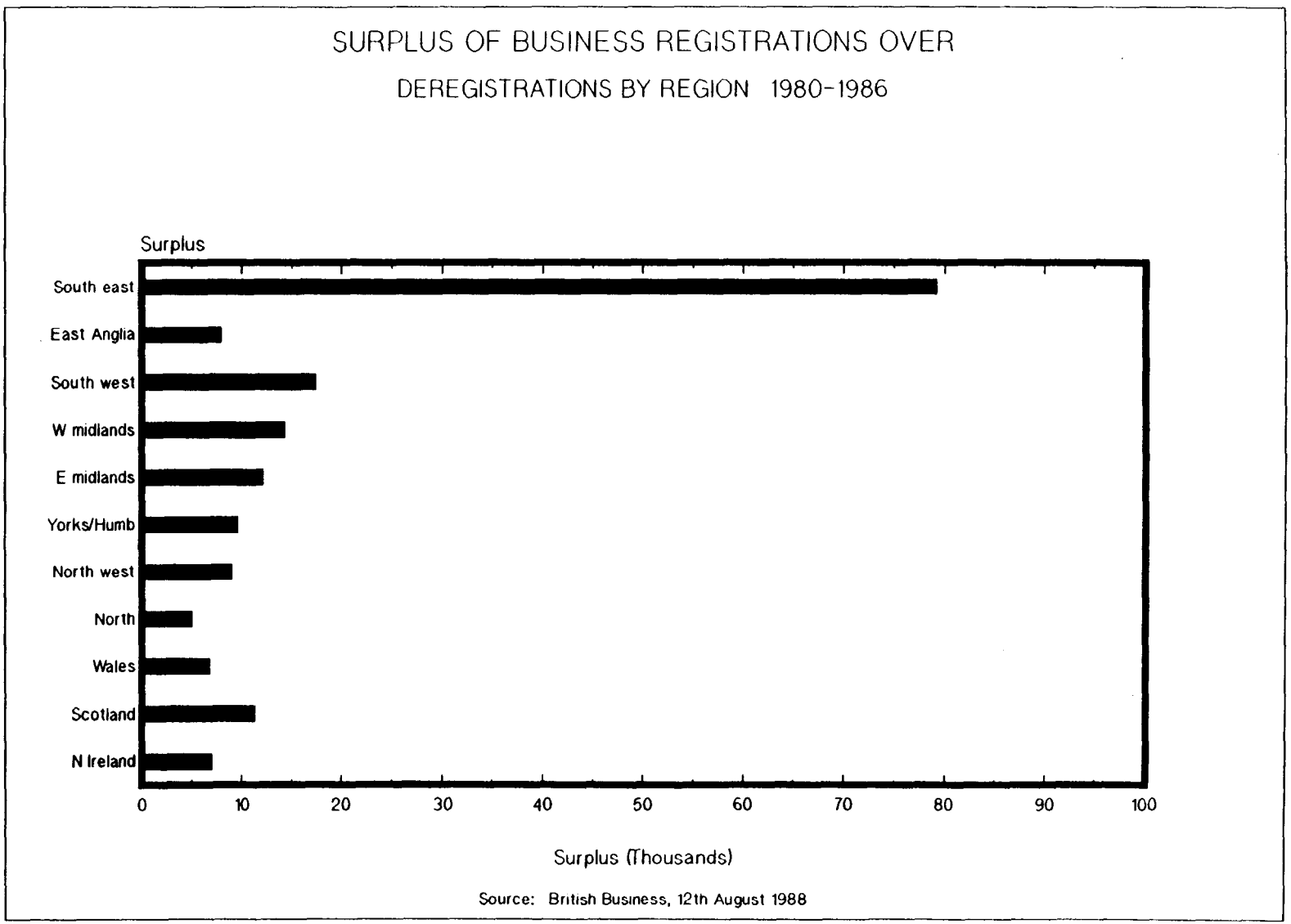

SURPLUS OF BUSINESS REGISTRATIONS OVER
DEREGISTRATIONS BY REGION 1980-1986
Surplus
South east
East Anglia
South west
W midlands
E midlands
Yorks/Humb
North west
North
Wales
Scotland
N Ireland
0
10
20
30
40
50
60
70
80
90
100
Surplus (Thousands)
Source: British Business, 12th August 1988

Table 4 **Business Registrations, Deregistrations and Stocks by Region: 1980-1986 (thousands)**

Region	Stock at start of year	Registrations	Deregistrations	Net change	Net change as a % of stock	Registrations as a % of stock (1)	Deregistrations as a % of stock (2)	Stock at end of year
South East	417.7	470.7	391.5	79.2	18.9	16.1	13.4	496.8
East Anglia	51.8	43.7	35.8	7.9	15.1	12.1	9.9	59.6
South West	123.0	104.4	87.0	17.4	14.2	12.1	10.1	140.5
West Midlands	111.5	103.2	88.9	14.3	12.8	13.2	11.4	125.8
East Midlands	87.8	77.8	65.7	12.1	13.8	12.7	10.7	99.7
Yorkshire & Humberside	103.1	90.3	80.7	9.6	9.3	12.5	11.2	112.7
North West	127.7	120.1	111.1	9.0	7.0	13.4	12.4	136.8
North	53.2	44.7	39.7	5.0	9.4	12.0	74.6	58.2
Wales	70.6	52.6	45.8	6.8	9.6	10.6	9.3	77.4
Scotland	99.0	78.9	67.6	11.3	11.4	11.4	9.8	110.3
Northern Ireland	43.7	25.2	18.2	7.0	16.0	8.2	5.9	50.6
United Kingdom	1,288.9	1,211.6	1,032.0	179.6	13.9	13.4	11.4	1,468.2

Notes: (1) (Number of registrations in Region i / Stock of units in Region i at the end of 1979) / Time period of analysis;
(2) (Number of deregistrations in Region i / Stock of units in Region i at the end of 1979) / Time period of analysis.

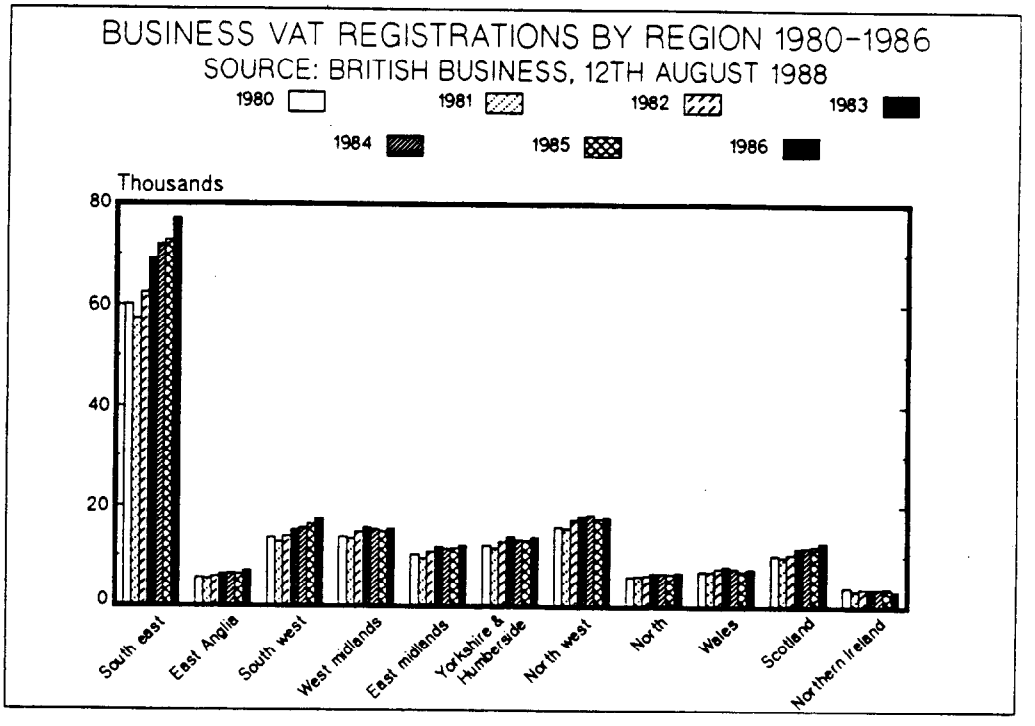
Source: British Business, August, 1988.

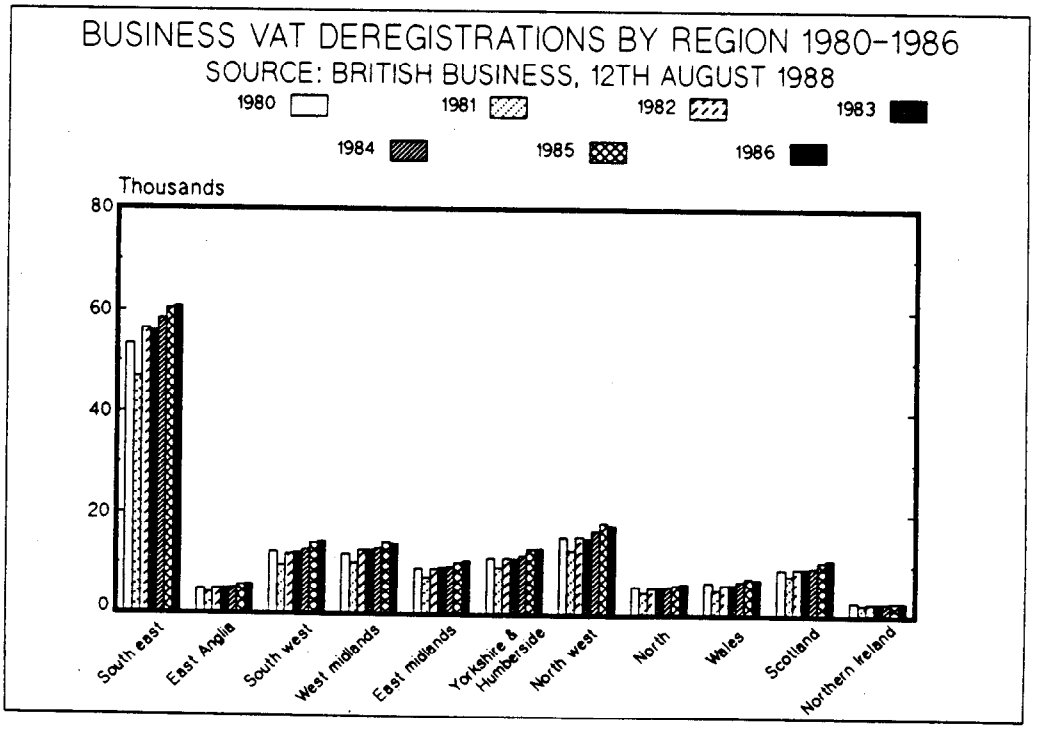
The dramatic increase in the number of VAT registrations in the South East since 1982 is clearly shown in Figure 4a in contrast to the less dramatic increases in business registrations in other regions of the United Kingdom. Moreover, Figure 4b indicates that the level of deregistrations has increased in the South East since 1981 but not at the same level as registrations. Modest increases in deregistrations over the 1980 to 1986 period have been recorded in the remaining regions of the United Kingdom, with the exception of the North West and Wales where deregistrations actually decreased between 1986 and 1987.

Insert Figures 4a & 4b

The overall rate of increase in any region is affected by the industry mix of the region. For example, the South East has a relatively high proportion of businesses in the 'property, finance and professional' and 'other services' sectors, which partly accounts for the high overall growth rate in this region. In fact, sector by sector, the percentage growth rates for the South East were not very different from those for the United Kingdom as a whole. Figure 5 illustrates the dramatic net growth as a percentage of end 1979 stock of businesses engaged in finance and 'other services' in each of the

Figures 4a & 4b





regions It is surprising at first sight that the rate of growth of finance ('financial, property and professional services') was lowest in the South East, but examination of the stock figures for 1979 suggests a possible explanation. At the end of 1979, this sector accounted for more than 10% of all registered businesses in the South East, proportionately more than twice as many as in any other region. To some extent therefore, other regions may have been going though a 'catching up' process. However, declines in the agricultural and retail sectors were recorded in a variety of regions. These trends are discussed in greater detail in the following section.

Insert Figure 5

Sector Variations, 1980-1986

The variation between the industrial sectors was much greater than that between regions. The net change over the seven years varied from a fall of 9,200 businesses in retailing through relatively small growth in agriculture and transport, to a rise of 62,100 businesses in 'other services' ('other services' covers a wide range of businesses including for example personal services such as hairdressing, entertainment businesses such as cinemas, business services such as contract cleaning) (Figure 6). Although retailing was the only sector to record a decline over the period as a whole, there were falls in individual years in the agriculture, construction and transport sectors.

Insert Figure 6

Table 5 gives details of these sector variations. The net increase of 62,100 businesses in 'other services' was made up of 194,800 registrations and 132,700 deregistrations. This represented a 49.3%

Figure 5

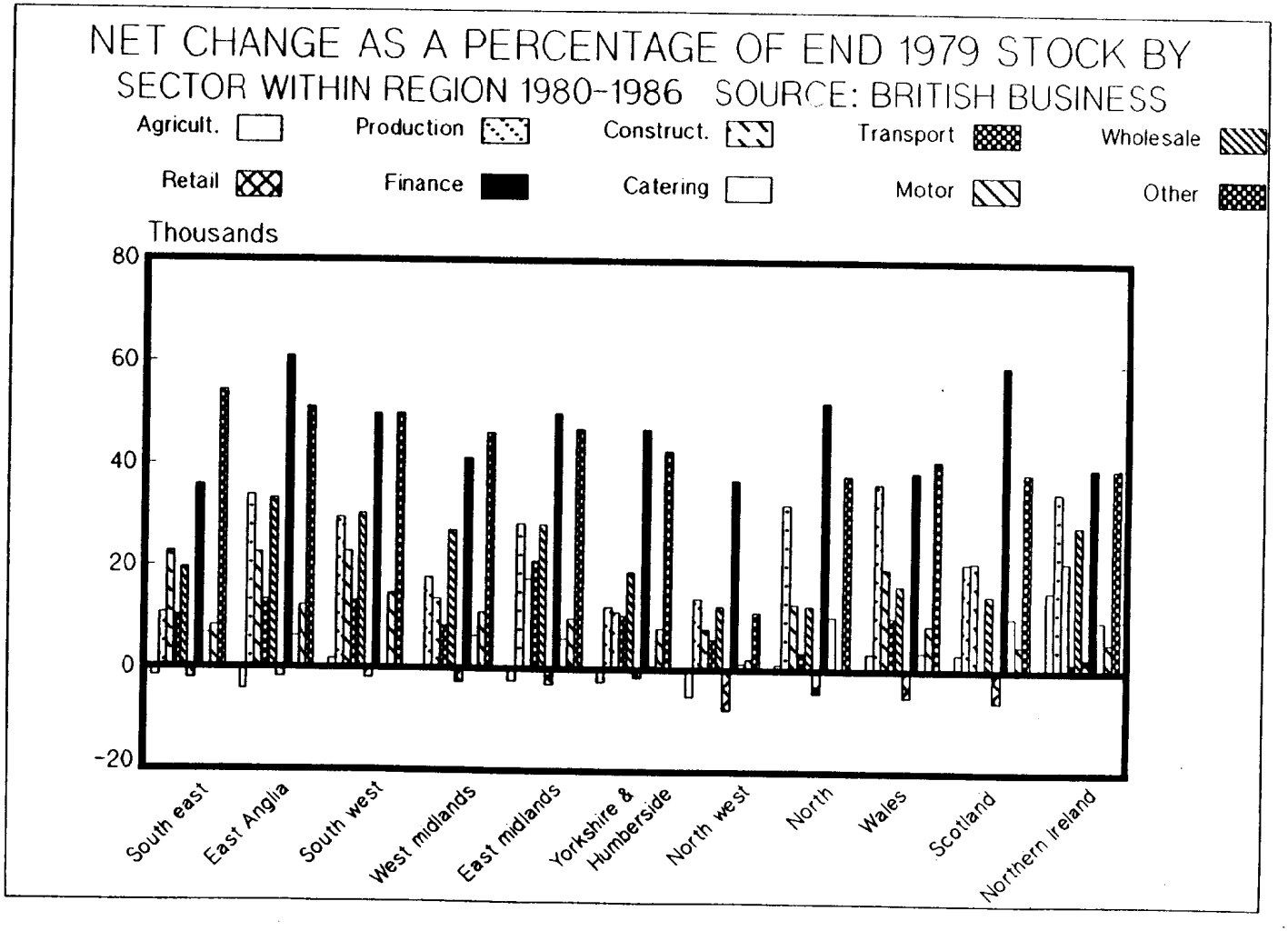
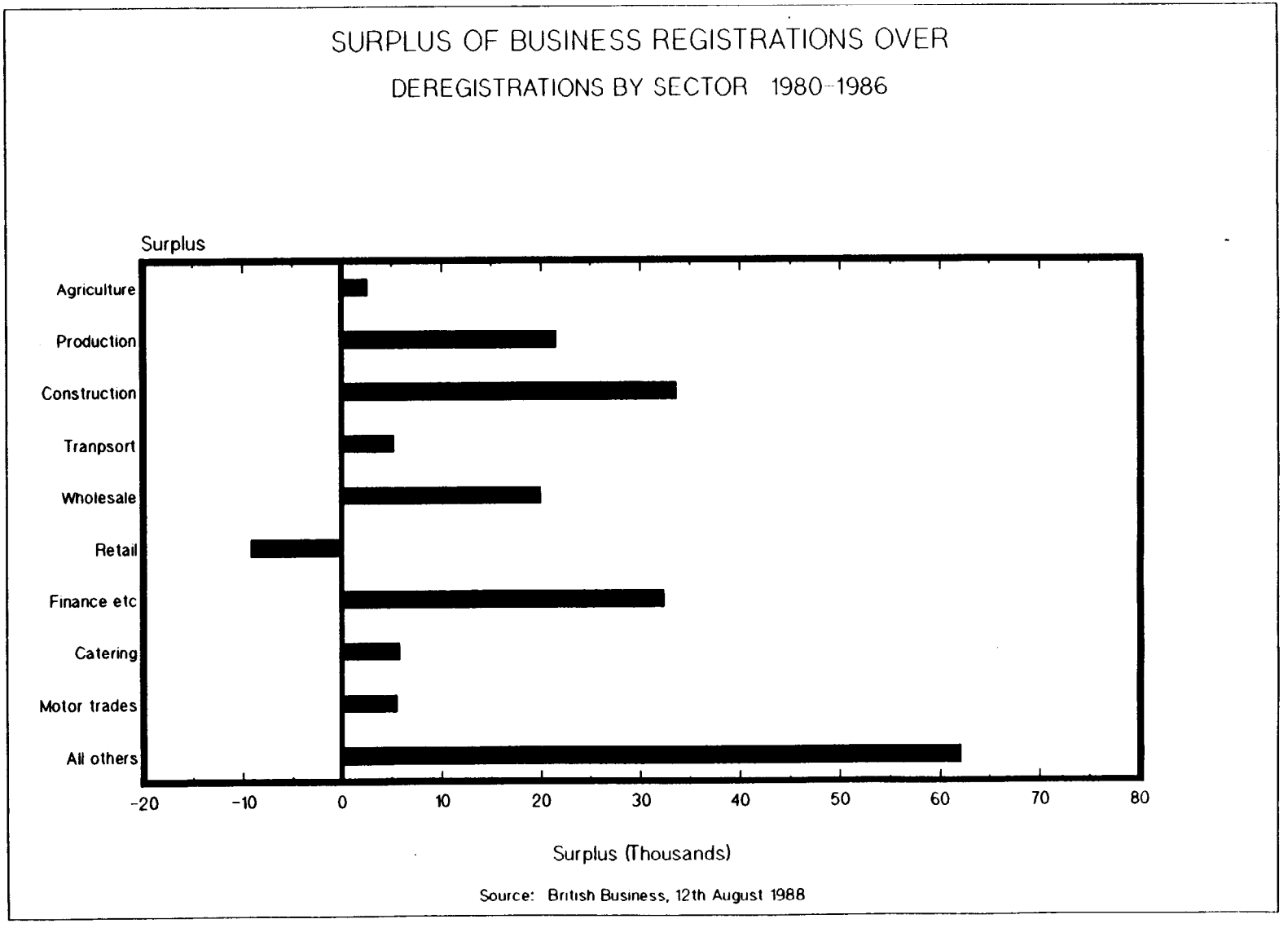

NET CHANGE AS A PERCENTAGE OF END 1979 STOCK BY SECTOR WITHIN REGION 1980-1986 SOURCE: BRITISH BUSINESS
Agricult.
Production
Construct.
Transport
Wholesale
Retail
Finance
Catering
Motor
Other
Thousands
80
60
40
20
0
-20
South east
East Anglia
South west
West midlands
East midlands
Yorkshire & Humberside
North west
North
Wales
Scotland
Northern Ireland

Figure 6


SURPLUS OF BUSINESS REGISTRATIONS OVER
DEREGISTRATIONS BY SECTOR 1980-1986
Surplus
Agriculture
Production
Construction
Tranpsort
Wholesale
Retail
Finance etc
Catering
Motor trades
All others
-20
-10
0
10
20
30
40
50
60
70
80
Surplus (Thousands)
Source: British Business, 12th August 1988

increase in the stock of businesses - the largest of any sector. This compares to the 3.4% net fall in the stock of businesses in the retail sector.

Table 5 Business Registrations, Deregistrations and Stocks by Industrial Sector: 1980-1986 (thousands)

Industrial sector	Stock at start of year	Registrations	Deregistrations	Net change	Net change as a % of stock	Registrations as a % of stock (1)	Deregistrations as a % of stock (2)	Stock at end of year
Agriculture	176.4	45.2	42.6	2.6	1.5	3.7	3.4	179.0
Production	121.2	122.8	101.3	21.5	17.8	14.5	11.9	142.7
Construction	180.9	179.3	145.7	33.6	18.5	14.2	11.5	214.5
Transport	55.8	53.2	48.0	5.2	9.3	13.6	12.3	61.0
Wholesale	95.7	107.9	88.0	19.9	20.7	16.1	13.1	115.6
Retail	268.8	235.1	244.3	-9.2	-3.4	12.5	90.9	259.7
Finance, etc	79.0	88.1	55.7	32.4	41.0	15.9	10.1	111.4
Catering	117.5	121.7	115.9	5.8	5.0	14.8	14.1	123.4
Motor trades	67.7	63.4	57.9	5.5	8.2	13.4	12.2	73.2
All others	125.9	194.8	132.7	62.1	49.3	22.1	15.1	187.9
United Kingdom	1,288.9	1,211	1,032	179	13.9	13.4	11.4	1,468

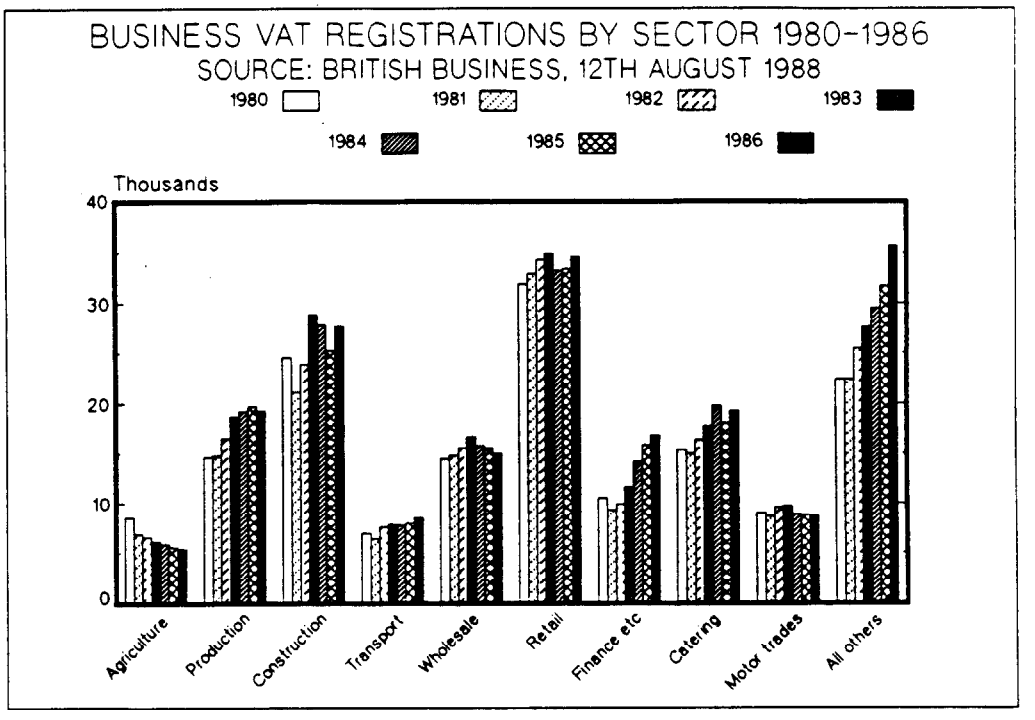
Notes: (1) (Number of registrations in Region i / Stock of units in Region i at the end of 1979) / Time period of analysis;
(2) (Number of deregistrations in Region i / Stock of units in Region i at the end of 1979) / Time period of analysis.

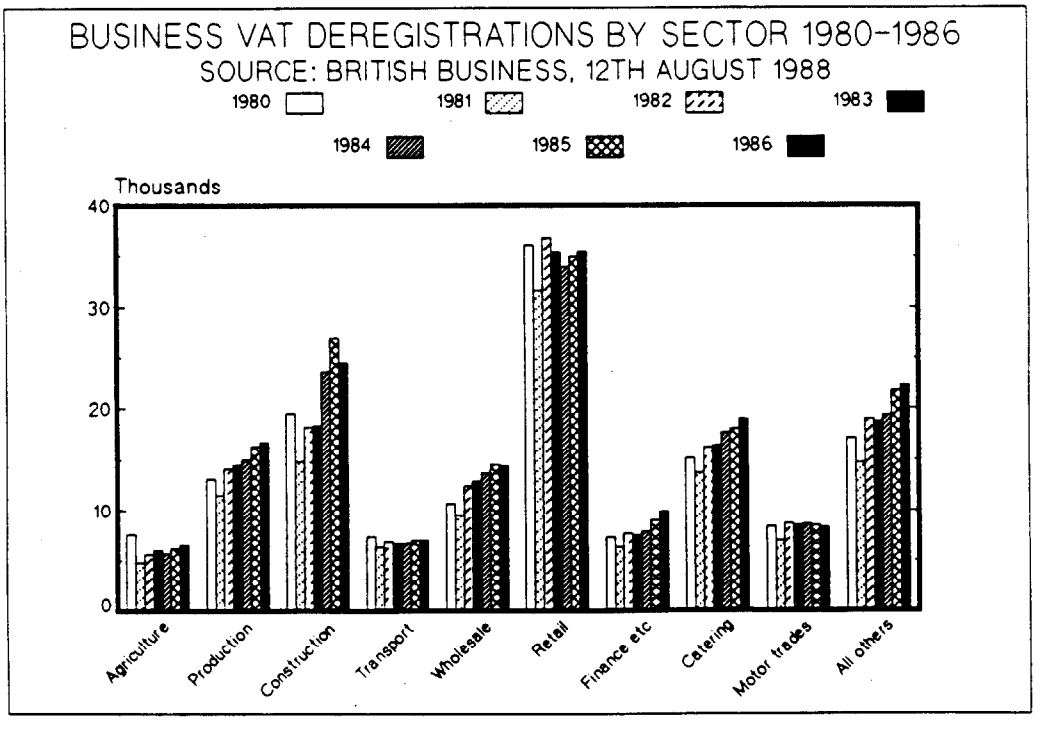
Source: British Business, August, 1988.

These falls are indicated when registrations and deregistrations over time are compared as in Figure 7a & 7b. Figure 7a also indicates the dramatic increase in VAT registrations in the United Kingdom since 1985 in 'other services' ('all others'), construction, catering, retail and finance, etc. In contrast, the level of deregistrations has generally increased in all sectors over time with the agriculture, transport and motor trades sectors being exceptions to this trend. In fact, in these sectors the level of deregistrations has remained fairly constant (Figure 7b). Although there has been no clear trend in the rate of increase in the number of businesses nationally, nor for any region, the rate of change in some industry sectors has varied significantly. Most noticeably, the rate of increase in transport was three times as great between 1984 and 1986 as between 1980 and 1983; while the number of businesses in agriculture declined between 1984 and 1986 but having risen between 1980 and 1983 (Figures 7a & 7b).

Insert Figure 7a & 7b

Figures 7a & 7b



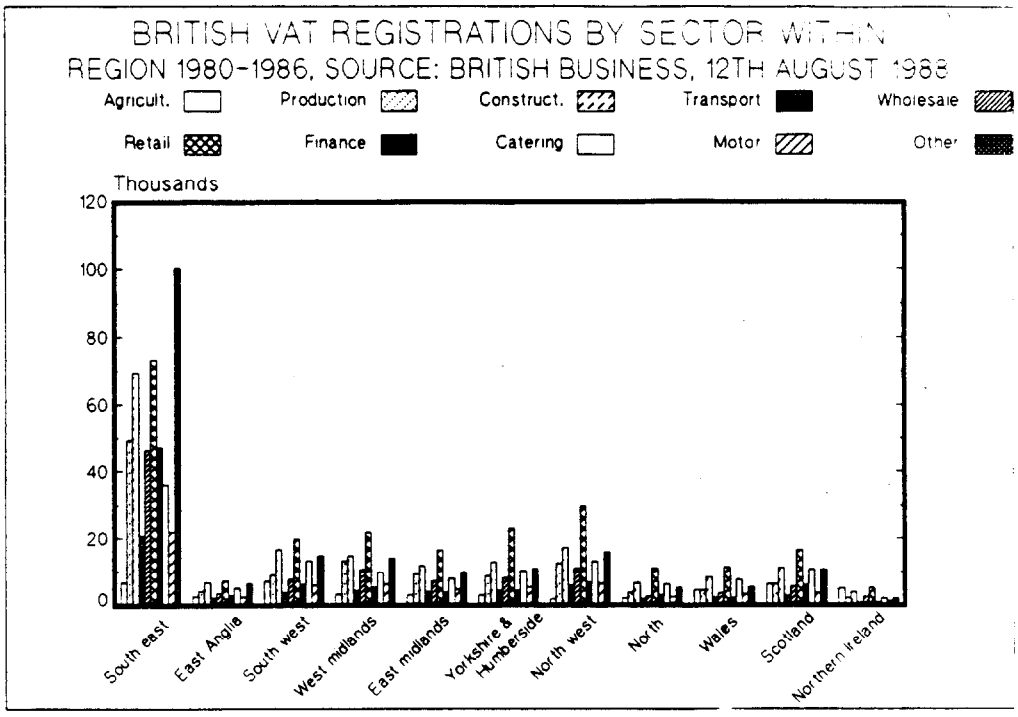


The pattern of VAT registrations and deregistrations by sector within region is graphically illustrated in Figures 8a and 8b. The tremendous volume of VAT registrations in 'other services', retail and construction over the 1980 to 1986 period in the South East alone is clearly illustrated. This growth reflects the growth of the City of London as a leading commercial centre in an increasingly global economy. The knock-on-effect has been a increased demand for housing and domestic consumable products in a region which has high relative levels of personal disposable income.

Insert Figure 8a & 8b

The over-representation of VAT registrations in particular sectors is clearly illustrated in Table 6. The 'location quotient' measures the extent to which different regions depart from the norm; for example the United Kingdom average. The location quotient indicates the degree of concentration, with higher values of the location quotient representing high concentrations, and values of 1 indicating equal distributions. From Table 6 the over-representation of registrations in the agricultural sector in Northern Ireland, Wales and Scotland is in marked contrast to the high location quotient values recorded in the finance and 'other services' sectors in the South East.

Figures 8a & 8b



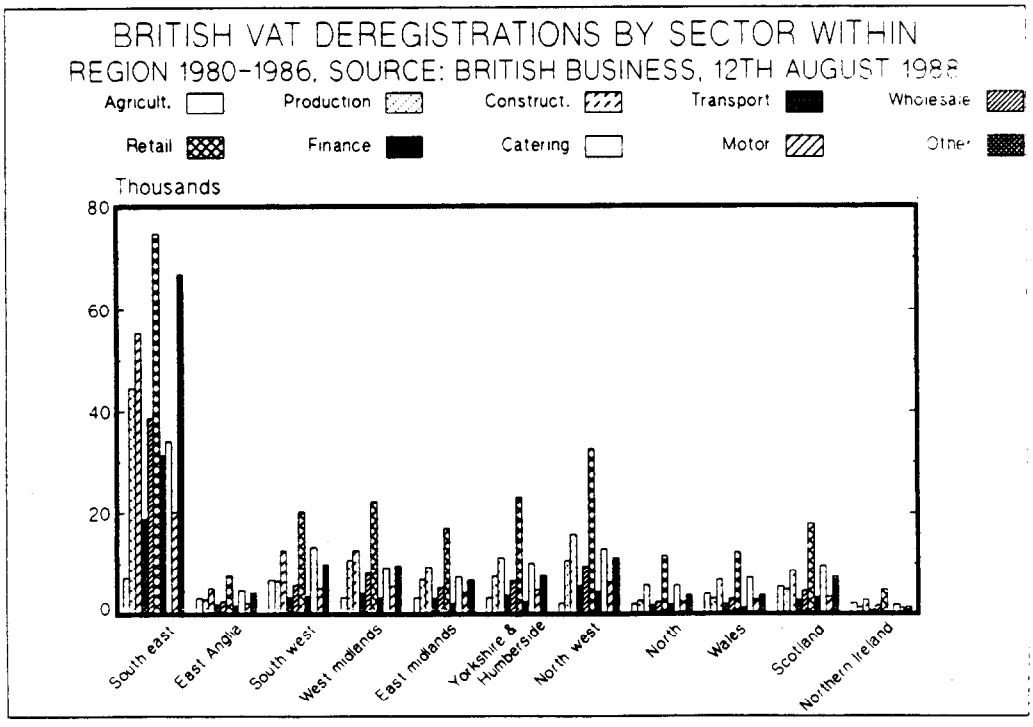


Table 6 **Regional Concentrations in VAT Registrations, 1980-1986 (Location Quotients)**

Region	Industrial sector									
	Agriculture	Production	Construction	Transport	Wholesale	Retail	Finance, etc	Catering	Motor trades	Other services
South East	0.39	1.04	1.00	1.00	1.10	0.80	1.37	0.77	0.89	1.32
East Anglia	1.59	0.95	1.04	1.15	0.90	0.87	0.94	1.14	1.09	0.93
South West	1.85	0.85	1.08	0.83	0.83	0.98	0.82	1.26	1.08	0.88
West Midlands	0.83	1.26	0.97	0.97	1.14	1.08	0.89	0.98	1.15	0.84
East Midlands	1.03	1.20	1.02	1.17	1.02	1.09	0.85	1.01	1.15	0.78
Yorkshire & Humberside	0.89	0.95	0.98	1.08	1.01	1.30	0.85	1.12	1.10	0.74
North West	0.40	1.02	0.97	1.12	1.02	1.28	0.78	1.09	1.02	0.82
North	1.28	0.82	1.00	0.97	0.88	1.27	0.92	1.38	1.03	0.70
Wales	2.34	0.83	1.08	0.95	0.77	1.12	0.58	1.42	1.13	0.63
Scotland	2.11	0.78	0.95	0.81	0.77	1.08	1.05	1.34	0.87	0.83
Northern Ireland	5.11	0.78	1.02	0.72	1.07	1.04	0.49	0.83	0.99	0.52

Note: Location Quotient = $\frac{(Xi/X)}{(Yi/Y)}$

where: Xi = number of VAT registrations in a given sector *i*, in a Region,
X = total number of VAT registrations in a Region,
Yi = United Kingdom number of VAT registrations in a given sector *i*,
Y = total United Kingdom number of VAT registrations

Not surprisingly, the South East has also recorded the largest numbers of deregistrations in the finance and 'other service' sectors (Table 7). It is also of interest to note the high level of deregistrations in retailing in the North West. The North West of England has in recent years suffered from high absolute and relative levels of unemployment and as a result of this and because of population decline there has been a decreased demand for retail products in small units at a time when the large chain stores have become increasingly dominant in the high street. As would be anticipated, there is an over-representation of deregistrations in the agriculture sector recorded in Northern Ireland, Wales, East Anglia and Scotland. These regions have been associated with a trend towards larger agricultural units in terms of size during a period of change relating to increasing EEC controls and smaller quotas which have made some smaller units less viable.

Table 7 **Regional Concentrations in VAT Deregistrations, 1980-1986 (Location Quotients)**

Region	Industrial sector									
	Agriculture	Production	Construction	Transport	Wholesale	Retail	Finance, etc	Catering	Motor trades	Other services
South East	0.44	1.16	1.00	1.04	1.16	0.81	1.46	0.77	0.92	1.33
East Anglia	2.10	0.83	0.99	1.14	0.82	0.90	0.83	1.17	1.10	0.93
South West	1.89	0.76	1.03	0.82	0.76	0.99	0.75	1.36	1.02	0.89
West Midlands	0.90	1.23	1.00	0.99	1.07	1.06	0.67	0.93	1.10	0.85
East Midlands	1.22	1.07	1.01	1.01	0.95	1.09	0.82	1.00	1.14	0.80
Yorkshire & Humberside	0.99	0.95	0.94	1.01	0.98	1.21	0.57	1.11	1.06	0.73
North West	0.48	0.97	1.01	1.08	1.00	1.24	0.73	1.03	1.01	0.79
North	1.22	0.89	1.02	0.97	0.71	1.23	0.89	1.26	1.08	0.72
Wales	2.12	0.87	1.04	0.89	0.77	1.13	0.53	1.40	1.09	0.83
Scotland	1.94	0.72	0.90	0.89	0.78	1.12	0.90	1.26	0.90	0.85
Northern Ireland	2.80	0.73	1.09	0.95	1.03	1.11	0.41	0.88	1.18	0.80

Note: Location Quotient = $\frac{(Xi/X)}{(Yi/Y)}$

where: Xi = number of VAT deregistrations in a given sector *i*, in a Region,
X = total number of VAT deregistrations in a Region,
Yi = United Kingdom number of VAT deregistrations in a given sector *i*,
Y = total United Kingdom number of VAT deregistrations

Business Stocks in 1987

Tables 8 and 9 summarise the information on the distribution of the stock of businesses between regions and industrial sectors in 1979 and 1986. In 1986 the stock of VAT registered units was 1.47 million with over 33.8% of units being located in the South East alone (Table 8) with a further 9.6% and 9.3% being located in the South West and the North West, respectively. Smaller proportions of VAT registrations were recorded in the peripheral regions of the United Kingdom such as Northern Ireland and the North. Table 9 shows that the three leading sectors in terms of the percentage of the total stock of units are retail (17.7%), 'other services' ('all other') (12.8%) and agriculture (12.2%). From Table 9 it is apparent that production only accounts for 9.7% of total VAT registered units.

Table 8 UK VAT Registrations Stock End-1979 and End-1986 by Region (thousands)

Region	Stock end-1979		Stock end-1986	
	No	%	No.	%
South East	417.7	32.4	496.8	33.8
East Anglia	51.8	4.0	59.6	4.1
South West	123.0	9.5	140.5	9.6
West Midlands	111.5	8.7	125.8	8.6
East Midlands	87.6	6.8	99.7	6.8
Yorkshire & Humberside	103.1	8.0	112.7	7.7
North West	127.7	9.9	136.6	9.3
North	53.2	4.1	58.2	4.0
Wales	70.6	5.5	77.4	5.3
Scotland	99.0	7.7	110.3	7.5
Northern Ireland	43.7	3.4	50.6	3.4
United Kingdom	1,286.9	100.0	1,468.2	100.1

Source: British Business, August, 1988.

Table 9 UK VAT Registrations Stock End-1979 and End-1986 by Industrial Sector (thousands)

Industrial sector	Stock end-1979		Stock end-1986	
	No	%	No.	%
Agriculture	176.4	13.7	179.0	12.2
Production	121.2	9.4	142.7	9.7
Construction	180.9	14.0	214.5	14.6
Transport	55.8	4.3	61.0	4.2
Wholesale	95.7	7.4	115.6	7.9
Retail	268.8	20.9	259.7	17.7
Finance, etc	79.0	6.1	111.4	7.6
Catering	117.5	9.1	123.4	8.4
Motor trades	67.7	5.3	73.2	5.0
All others	125.9	9.8	187.9	12.8
United Kingdom	1,286.9	100.0	1,468.4	100.1

Source: British Business, August, 1988.

Figure 9 shows the stock of registered businesses by sector within each region. It shows clearly the dominance of the South East economy in terms of the stock of VAT registered units particularly with regard to the following sectors: 'other services', construction, retail and finance. Conversely, the high level of VAT registered agricultural businesses is also apparent in Northern Ireland, Scotland and Wales.

Insert Figure 9

The latter points are reinforced when the pattern of location quotients for sectors in individual regions are referred to in Table 10

Table 10 Regional Concentrations in VAT Registered Stocks End-1986 (Location Quotients)

Region	Industrial sector									
	Agriculture	Production	Construction	Transport	Wholesale	Retail	Finance, etc	Catering	Motor trades	Other services
South East	0.32	1.05	1.05	0.98	1.15	0.84	1.57	0.83	0.92	1.49
East Anglia	1.55	0.88	1.08	1.09	0.85	0.88	0.80	0.98	1.04	0.85
South West	1.61	0.81	1.07	0.82	0.74	0.93	0.74	1.16	1.07	0.82
West Midlands	0.92	1.39	0.99	1.03	1.14	1.03	0.72	0.92	1.10	0.83
East Midlands	1.11	1.22	1.03	1.18	0.99	1.08	0.81	0.98	1.13	0.75
Yorkshire & Humberside	0.98	1.05	0.98	1.15	1.05	1.22	0.84	1.14	1.09	0.73
North West	0.50	1.12	0.98	1.15	1.15	1.32	0.84	1.12	1.08	0.85
North	1.34	0.78	0.92	1.17	0.88	1.25	0.77	1.35	1.00	0.88
Wales	2.13	0.88	0.88	0.98	0.71	1.06	0.51	1.26	1.04	0.55
Scotland	1.57	0.73	0.91	0.83	0.77	1.08	0.87	1.19	0.89	0.79
Northern Ireland	3.19	0.59	0.81	0.82	0.88	0.93	0.39	0.86	0.87	0.39

Note: Location Quotient = $\frac{(Xi / X)}{(Yi / Y)}$

where: Xi = number of VAT stock in a given sector *i*, in a Region,
X = total number of VAT stock in a Region,
Yi = United Kingdom number of VAT stock in a given sector *i*,
Y = total United Kingdom number of VAT stock

Table 11 shows the size distribution of number and percentage of VAT registered businesses in mid 1987. Adopting a criteria of turnover below £250,000, some 82% can be seen to be 'small'.

Figure 9

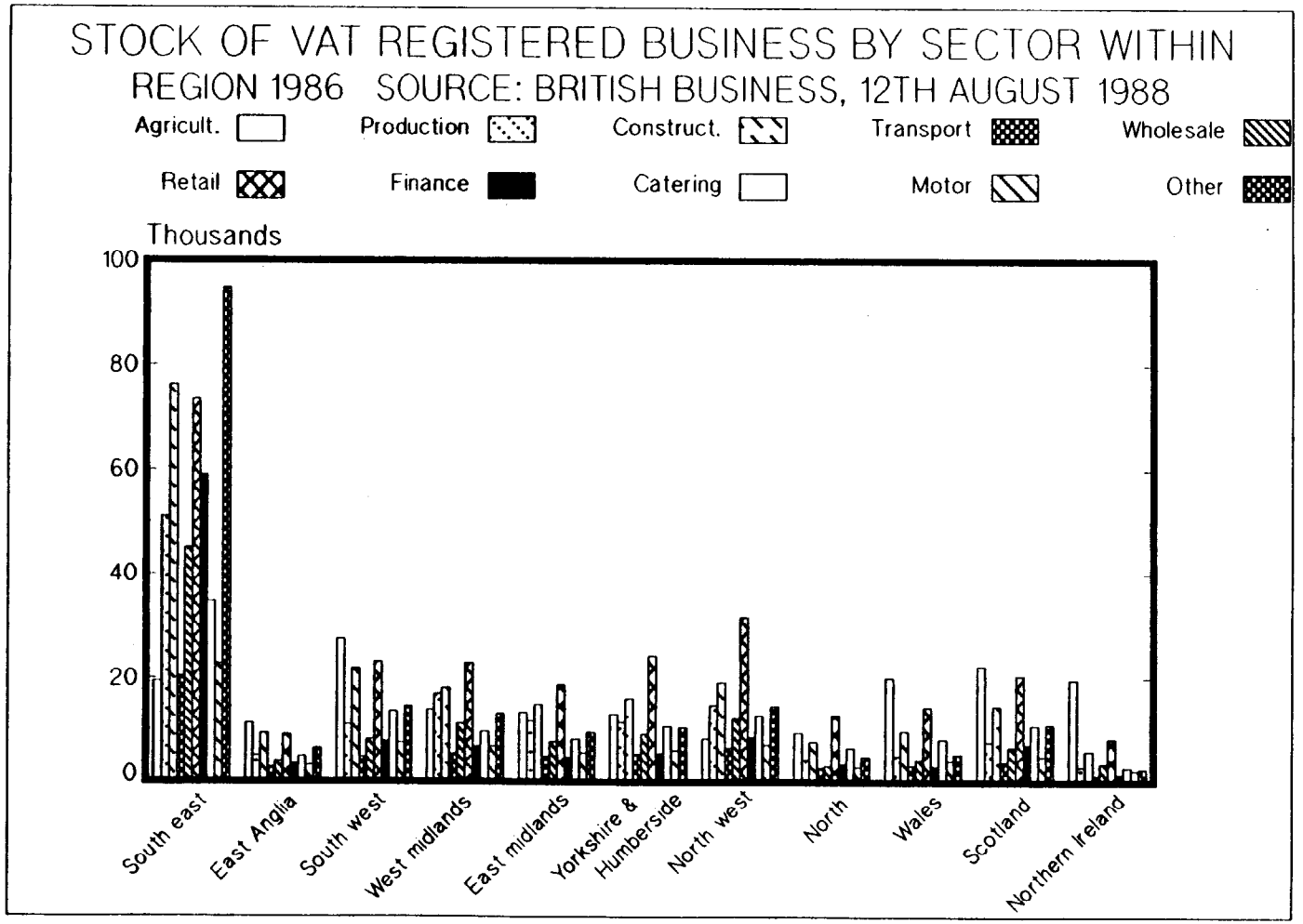

STOCK OF VAT REGISTERED BUSINESS BY SECTOR WITHIN REGION 1986 SOURCE: BRITISH BUSINESS, 12TH AUGUST 1988
Agricult.
Production
Construct.
Transport
Wholesale
Retail
Finance
Catering
Motor
Other
Thousands
100
80
60
40
20
0
South east
East Anglia
South west
West midlands
East midlands
Yorkshire & Humberside
North west
North
Wales
Scotland
Northern Ireland

Table 11 All VAT Registered Businesses - Analysis by Size of Turnover in 1986 - Number (percentage) of Legal Units in 1984

Standard Industrial	Turnover band (£'000)																	
	20-50		51-100		101-250		251-500		501-1,000		1,001-2,000		2,001-5,000		5,001-10,000		Over 10,000		Total	
Agriculture, forestry and fishing	49,183	(41)	32,894	(28)	25,402	(21)	7,573	(6)	2,602	(2)	813	(1)	329	(-)	75	(-)	44	(-)	118,733	(100)
Production	39,644	(28)	25,606	(18)	28,517	(20)	16,950	(12)	11,602	(8)	7,647	(5)	6,085	(4)	2,471	(2)	3,050	(2)	141,192	(100)
Mining and quarrying and public utilities	244	(18)	187	(14)	262	(19)	177	(13)	150	(11)	92	(7)	101	(7)	47	(3)	118	(9)	1,378	(100)
Manufacturing	39,400	(28)	25,419	(18)	28,255	(20)	16,413	(12)	11,452	(8)	7,555	(5)	5,984	(4)	2,424	(2)	2,932	(2)	139,814	(100)
Construction	88,452	(48)	36,158	(20)	29,864	(16)	13,617	(7)	7,613	(4)	3,736	(2)	2,081	(1)	656	(-)	588	(-)	182,765	(100)
Transport industries	26,420	(45)	10,062	(17)	9,067	(15)	5,246	(9)	3,470	(6)	2,021	(3)	1,305	(2)	453	(1)	545	(1)	58,589	(100)
Road transport and transport services	25,854	(46)	9,775	(17)	8,746	(16)	4,980	(9)	3,283	(6)	1,842	(3)	1,096	(2)	352	(1)	349	(1)	56,256	(100)
Other transport	566	(24)	287	(12)	321	(14)	266	(11)	207	(9)	179	(8)	210	(9)	101	(4)	196	(8)	2,333	(100)
Postal services and telecommunications	247	(42)	105	(18)	82	(14)	62	(11)	39	(7)	24	(4)	15	(3)	6	(1)	10	(2)	590	(100)
Wholesaling and dealing	24,280	(22)	17,665	(16)	22,590	(20)	15,624	(14)	12,463	(11)	8,577	(8)	6,881	(6)	2,362	(2)	2,209	(2)	112,431	(100)
Retailing	79,540	(32)	73,817	(30)	65,804	(26)	18,270	(7)	6,800	(3)	2,252	(1)	1,167	(-)	292	(-)	491	(-)	248,433	(100)
Finance, property and professional services	49,443	(50)	16,853	(17)	15,428	(15)	7,531	(8)	4,191	(4)	2,184	(2)	1,634	(2)	707	(1)	1,589	(2)	99,560	(100)
Catering	41,642	(34)	41,439	(34)	29,663	(24)	5,900	(5)	1,737	(1)	581	(-)	307	(-)	81	(-)	102	(-)	121,452	(100)
Motor trades	22,605	(32)	12,498	(18)	12,940	(18)	7,870	(11)	6,055	(9)	4,117	(6)	2,611	(4)	787	(1)	598	(1)	70,081	(100)
Business services and central offices	39,248	(52)	12,132	(16)	10,085	(13)	5,271	(7)	3,309	(4)	1,951	(3)	1,492	(2)	676	(1)	986	(1)	75,148	(100)
All other services	49,807	(55)	18,284	(20)	12,986	(14)	4,721	(5)	2,489	(3)	1,178	(1)	739	(1)	276	(-)	339	(-)	90,821	(100)
Total	510,509	(39)	297,313	(23)	262,446	(20)	108,275	(8)	62,370	(5)	35,081	(3)	24,426	(2)	8,844	(1)	10,551	(1)	1,319,795	(100)

Note: Excludes 243,683 units with turnover up to £19,500. Turnover relates mainly to a 12 month period ending in spring 1986.

Source: British Business, 18th September 1987.

Table 12 summarises the information on size distribution using the turnover criteria of £250,000. As can be seen, the proportion of small businesses is highest in catering at 92% and smallest in wholesaling and dealing at 58%. Production also has a smaller than average proportion of small businesses at 66%.

Table 12 Percentage of VAT Registered Businesses with Levels of Turnover Below £250,000

Standard industrial category	Percentage below £250,000 turnover
Agriculture, forestry and fishing	90
Production	66
Construction	84
Transport industries	77
Postal services and telecommunications	74
Wholesaling and dealing	58
Retailing	88
Finance, property and professional services	82
Catering	92
Motor trades	68
Business services and central offices	71
All other services	89
Total	82

3. FACTORS INFLUENCING REGISTRATIONS

At National Level

Since the publication in 1971 of the report of the Committee of Inquiry on Small Firms, better known as the Bolton Report (HMSO, 1971), successive governments in the United Kingdom have introduced a variety of measures designed to promote new firm formation and small firm growth (Beesley and Wilson, 1982). The election in 1979 of a Conservative Government pledged to create a thriving private enterprise economy has turned the steady stream of measures to assist the small firm sector into a torrent. Since the Governments re-election for a third term it has concentrated its efforts on 'repackaging' and publicising the plethora of small firms schemes available to take account of the criticism that there is only limited awareness amongst the small business sector of the assistance that is on offer (for example, as shown in a survey by the Economists Advisory Group, 1983) while the sheer number of different measures is confusing to the target clientele (Dickson, 1984). Small firms are now being singled out for special help and they have been made exempt from some of the more arduous requirements placed on them by various Government agencies. To further this end, the Government in January 1988 has condensed and simplified the sixty-four schemes under the remit of the Department of Trade and Industry into 'the Enterprise Initiative' covering investment, innovation, export and advice which is intended to be a more 'user friendly service'.

The measures introduced since 1979 by the Conservative Government, address four main constraints on small business activity (Mason and Harrison, 1986). First, the availability of finance for new and small firms, consistently identified as one of the most important limitations on their growth, has been tackled by the Loan Guarantee Scheme, while the fiscal incentives embodied in the Business Start-Up Scheme, subsequently extended and renamed the Business Expansion Scheme, have made it more attractive for individuals to invest in new and established small businesses. In addition the Enterprise Allowance Scheme was introduced to provide a payment in lieu of unemployment benefit to encourage more unemployed individuals to consider setting up their own businesses. Second, the provision of inexpensive or free business information and advice has been enhanced by an expansion of the activities of the Small Firms Service and through the reaction of local enterprise agencies whose establishment has been encouraged by the availability of tax relief on the contributions in cash and kind (e.g. seconded staff) from companies which support them. Third, legislative and administrative burdens on small firms have

been reduced by exempting them from certain obligations under various places of legislation (e.g. dismissal procedures under employment legislation and the provision of detailed financial information with the Registrar of Companies). Finally, tax rates have been lowered for both individuals (standard rate 25%, top rate 40%) and for companies (small companies 25%, larger companies 35%).

Already there has been considerable evaluation of these schemes conducted within and outside Government. Prominent examples include reviews of the Small Firms Counselling Service (Howdle, 1979, 1982; Research Associates Ltd, 1981), the Small Business Loan Guarantee Scheme (Department of Industry, 1982a; Robson Rhodes 1983a, 1983b, 1984a, 1984b; Harrison and Mason, 1986; Harrison and Mason, 1987; Mason and Harrison, 1986), the Small Workshops Scheme (Department of Industry, 1982b), the Small Engineering Firms Investment Scheme (Research Associates Ltd, 1984), the pilot version of the Enterprise Allowance Scheme (Department of Employment, 1984), the Business Expansion Scheme (Mason et al., 1988) and the New Enterprise Programme (Morris and Watkins, 1982; Dyson, 1982; Johnson and Thomas, 1983a, 1983b).

Subsequent sections will provide details from many of these studies. However, whilst many schemes have been evaluated in terms of cost / benefit analysis at the micro-economic level, it is almost impossible to disentangle the effect of the schemes at the macro-economic level. It is claimed that the measures introduced by the Conservative Government since 1979, taken together, have led to the development of a whole new 'enterprise culture' which has pushed up the rate of new business registration and contributed to the increase in the growth rate of the United Kingdom economy.

At Regional Level

Increasing numbers of local authorities have also sought ways in which they can aid and influence the economic prosperity of their immediate areas. As a result of their limited power and resources one of the most readily available audiences for any locally directed aid is the local small firms population. This trend has been most acute in the inner-city areas and in the less prosperous regions of the United Kingdom, for example, the Northern Region of England, Scotland and Wales. At a regional level the move towards supporting the local small firm population has drawn support from the failure of successive regional policy measures to ensure either a constant supply, or at least a supply of stable jobs for the assisted regions.

BANK FINANCE

Description: In the United Kingdom the importance of bank finance to small businesses is paramount (Burns and Dewhurst, 1986). The ratio of bank overdrafts to shareholders' funds is substantially higher for small businesses than for medium and large business (Burns, 1987). Nowadays small businesses still turn to their local branch manager not only for short-term funds but, increasingly, for medium- and long-term funds. The relationship that a proprietor or manager of a small business has with his local branch manager is therefore of crucial importance to him. When he wants external finance it is to his branch manager that he will almost certainly turn in the first place.

In the United Kingdom joint stock banks are part of the private sector and here we have:

1. Four main banks - the 'Big Four' (Barclays, Lloyds, Midland and National Westminster). Branches of these four cover the country.
2. A number of other smaller United Kingdom banks (for example, Coutts & Co., and certain other organisations which perform many of the functions of the main banks, for example, the 'Co-op' and Standard Chartered).
3. Foreign banks (typically local branches of American banks), consortium banks, building societies and so on.

Each of the 'Big Four' banks has some 2,000 or 3,000 local branches. Each bank manager has a budget given to him each year, and a loan limit which applies for every individual application. The individual loan limit varies considerably with the size of the branch. If the loan or overdraft application is above the branch manager's limit, he will refer it to his regional manager. Typically these managers will have limits of around £300,000 to £750,000. Above that amount the regional manager must 'push it up the line' to the next level of authority. Within his loan limits the power of the bank manager is absolute and for the first-time applicant, the attitude of his bank manager is crucial to the success of his business.

All managers will be concerned with business security based on the assets of the business, or personal guarantees from the loan applicant or his wife. He is also concerned with the prospects of the business, the appearance and attitude of the loan applicant, and the amounts the applicant is prepared to put in himself. The Wilson Committee (1979) noted that 'typical security ratios of net assets to borrowing were in the range 2:1 to 4:1'.

Banks typically make two charges for their services:

1. An Arrangement charge or Negotiation fee and (sometimes) an annual renewal fee.
2. An interest charge.

An arrangement charge or negotiation fee is usually made for short-term loans; less frequently, it is made when an overdraft facility is arranged. In either case it is a 'one-off' charge made at the time when the overdraft or loan is arranged. It is likely to be in the order of £100 to £300 for loans of, say, £5,000 to £20,000, but the exact charge varies considerably. The amount is at the discretion of the bank manager, and reflects his view of the quantity of work that the bank will be involved in when making the necessary arrangements.

Over the period of the loan the charge made by way of interest will be a much more substantial figure than the arrangements fee. The rates that banks give to depositors, and the rates that they charge for loans are tied to their own bank base lending rate. In this respect banks operate in a similar way to other financial institutions, such as HP finance houses, which also relate their lending and borrowing rates to their own base rate. The base rate is determined by a number of economic factors, such as the general money market rates and money supply, and, as well, pressure by the Government, mainly through the Bank of England. Although banks do, in theory, determine their own bank rates and the time of any change, in practice they usually move more or less in unison.

Overdrafts and short-term loans from joint stock banks have been for many years, and still remain, the main source of outside non-creditor finance for small businesses. The differences between the two are not very great. A short-term loan is a fixed commitment by the lender. This term commitment theoretically differentiates a short-term loan from an overdraft, which, technically, is repayable on demand by the bank. In practice, banks do not normally cancel an overdraft facility at short notice; indeed overdrafts frequently remain in existence over many years. In such circumstances it is hard to see that they retain any of the characteristics of short-term borrowing.

The other main differences between a bank overdraft and a short-term loan is that interest on the latter is either based on the agreed loan amount or on the balance outstanding after scheduled repayments. Interest for an overdraft is always only paid on the amount of money actually borrowed, and this is accumulated on a day-to-day basis. However, since overdraft rates are always expressed as so much (typically 2 to 3%) over bank base rate, and base rates do vary over time, overdraft interest charges

The move to support new and small firms in the less-prosperous regions also stems from the political and economic desire to develop indigenous potential rather than rely on the fortunes of a branch factory economy in decline (Cross, 1983). Moreover, locational and sectoral variations in registration rates and deregistration rates may in part be a result of differences in take-up rates of small business schemes and small business support mechanisms in general.

Whilst it is difficult to explain national levels of new business registrations, it is possible to identify some of the factors found to be associated with regional variations. Following the work of Whittington (1984) a range of factors (and 'surrogate' independent variables) hypothesised to be associated with business registration were explored and tested using correlation analysis. Table 12 lists the factors found in the research literature to be associated with new business formation and the 'surrogate' variables used. Some factors encourage whilst others inhibit individuals from business formation (Westhead, 1988). These variables were correlated against the numbers of VAT registrations in each standard region (1980-1986) per 1,000 employees in employment in the base year 1979. This measure was used because it reflects the process by which the population of industrial employees is the relevant indicator of the number of potential employees. A base measured simply in terms of VAT registered businesses fails to take into account the size of the existing industrial base. From Table 13 it can be inferred that there are marked regional differences in VAT registration rates in the United Kingdom. The highest registration rates were recorded in southern England in the South West, the South East and East Anglia in particular with rates above 62.24 per thousand. In contrast, the lowest rates were recorded in the following essentially economically deprived and peripheral regions: the North, Scotland and Northern Ireland.

Table 13 UK VAT Registrations, 1980-1986 Per Thousand of Total Employees in Employment, 1979 by Region

Region	Registrations, 1980-1986	Total employees in employment, 1979	Registration rate
South East	470.7	7,473.0	62.99
East Anglia	43.7	702.0	62.25
South West	104.4	1,598.0	65.33
West Midlands	103.2	2,241.0	46.05
East Midlands	77.8	1,555.0	50.03
Yorkshire and Humberside	90.3	2,011.0	44.90
North West	120.1	2,676.0	44.88
North	44.7	1,248.0	35.82
Wales	52.6	1,033.0	50.92
Scotland	78.9	2,102.0	37.54
Northern Ireland	25.2	658.0	38.30
United Kingdom	1,211.8	23,297.0	52.01

Source: British Business, August, 1988.

Table 14 shows the thirteen variables, related to six factors, that were found to be significantly associated with registrations. These variables were:

Table 14 Factors Identified by the New Firm Literature Which Are Associated With the Rate of New Business Formation

Factors		Surrogate variables	Explanation	Significant
1.	Size of 'incubator' firm	High percentage of total manufacturing employment in establishments employing 10 or fewer employees	High proportion of total manufacturing employment in small firms is conducive to new business formation	YES
2.	Occupational experience	High percentage of population in managerial and professional groups	Professional groups gain more appropriate experience and opportunities for new business formation than manual groups	YES
		Low percentage of population in manual groups		YES
3.	Turbulence	High rate of business closures	Business closures are a positive 'push' towards new business formation	YES
4.	Education	High percentage of employees with higher degrees	High educational attainment encourages new business formation	YES
5.	Access to capital	High house-owning population	High levels of prosperity encourage new business formation. It encourages demand and increases personal capital availability. House ownership provides a further collateral base	YES
		Low percentage of population in local authority housing		YES
		High gross weekly earnings		YES
		High disposable income		YES
		High rate of change in average male weekly earnings		YES
		High rate of change in average dwelling price		YES
		High rate of GDP per head		YES
6.	Market demand	High rate of population growth	Increasing demand and opportunity encourages new firm formation	YES

Further details of this analysis are given in Appendix 2. The results confirm the view that there is a regional bias in entrepreneurship in the United Kingdom that goes against the least prosperous regions (Storey, 1982; Whittington, 1984). These regions - the North, Scotland, Wales and Northern Ireland - will not receive the same support through national Government policies as the fortunate regions of the south of England.

4. FINANCE FOR SMALL FIRMS

The difficulty of obtaining finance is frequently cited as a barrier to small firms setting up and growing. In a survey of venture capital users, two out of three respondents rated both personal and external finance as a serious or moderate problem when establishing their new business and 41% saw it as a major obstacle to further growth. For small firms this problem can arise from their lack of size (lack of collateral) or their newness (lack of track record). As a result, the financial institutions, especially the high-street banks, regard loans to small firms as representing a higher risk than, say, making loans to medium or large firms. Efforts have made to educate those seeking funds and those investing funds on how to communicate. Many of the difficulties of raising finance are caused by the parties concerned not speaking the same language, yet they are both seeking the same end - somewhere to invest the bank's funds and funds to exploit a particular business opportunity. Research to date tends to suggest that this gap still exists despite continued government and banking involvement to reduce the gap, and at the present time much of the assistance programme for small firms is aimed at ensuring a flow of funds into new and existing small firms.

Survey evidence indicates that the majority of small firms rely primarily on personal savings for start up capital (Cross, 1981; Storey, 1982; Lloyd and Mason, 1984; Westhead, 1988). However, once established they tend to operate gearing ratios (debt to total funds) similar to or higher than large firms and a proportion of short term debt that is higher than large firms (Burns, 1987).

are more vulnerable than fixed interest rate loans to changes in government policy and general economic conditions.

BANK FINANCE

Scale: It has been estimated that the 'Big Four' banks had some £23.5 billion of loans outstanding to small firms in 1986/87 (Burns, 1987) (Table 15):

Table 15 'Big Four' Bank Loans to Small Firms, 1986/ 87

Bank	Bank loans £ billion
Barclays	8
Nat West	7
Lloyds	5
Midland	3.5
Total	23.5

This represents about £22,000 for each small business registered for VAT in the United Kingdom. The amount has grown between 8-10% over the previous year, well in excess of inflation. It also includes loans issued under the Governments Loan Guarantee Scheme (see next section).

BANK FINANCE

Evaluation: There has been much criticism of bank lending practises. A recent survey, which prompted responses from more than 5,400 small businesses in Great Britain and the United States, listed the following shortcomings (Bannock and Morgan, 1988):

- United Kingdom bank charges are being applied to a wider range of services and are increasing at a faster rate than appears justified.
- United Kingdom banks charge higher interest rates than the United States banks.
- United Kingdom banks demand higher levels of collateral than United States banks.
- The 'funding gap' in the United Kingdom is far wider than in the United States.

However, the situation is changing. There is a major and continuing programme of rationalisation of the delivery systems the 'Big Four' use for small firms. This has mainly taken the form of concentration of professional lending expertise in corporate style branches, but it has also taken the form of a more aggressive marketing effort including the emergence of new packaged lending products. Nat West's Business Development loans total over £1.73 billion and has seen growth of about 15% per annum since the current scheme was introduced in 1985.

Competition between the clearers is also increasing, with a borrowers' market for 'quality business' starting to emerge (Doran and Hoyle, 1986). Indeed, some surveys have indicated that the problem lies not with the bankers but with the quality of loan applications presented to them (Robson Rhodes, 1984c). Whilst competition might be increasing, there is little evidence that small firms are willing to change their banks. Seventy-three percent of small firms polled in a recent survey had not looked for a new bank in the previous three years (Bannock and Morgan, 1988).

Other Loan Schemes

British Coal Enterprise Limited was set up in August 1984 by the National Coal Board to provide new alternative job opportunities in areas traditionally associated with coal mining. Its main activity is to provide assistance in the form of loans to individuals, partnerships or companies who wish to start-up, expand or locate in the coalfields. There is no upper or lower limit to the funds the company will make available to individuals or companies who comply with the requirements of job creation, viability and location. Loans are given with interest at lower than commercial rates in the initial years and / or repayment holidays as appropriate. The loan normally would be for up to £5,000 per job created. In addition to direct financial assistance help can be given by the provision of premises or the provision of managed workspace - small workshops or work units available on easy-in, easy-out, low-cost basis with a central management unit supplying all the services normally regarded as overheads, inclusive in the cost of the lease.

Small- and medium-sized businesses are eligible for subsidised fixed interest loans from the European Investment Bank (EIB) and the European Coal and Steel Community (ECSC). EIB loans are about 2% cheaper than comparable borrowing from United Kingdom sources; ECSC loans are available in certain parts of the country on terms similar to EIB lending, but in addition carry a subsidy in the form of an interest rebate of up to 5% for the first five years of the loan. Local authorities now sponsor quite a range of loan schemes. Of these schemes, those offered by the development agencies have probably been the most widely used, often being cited as a reason for the relatively low take up of the Loan Guarantee Scheme in Scotland, Northern Ireland and Wales.

The Small Firm Loan Guarantee Scheme

Description: The Loan Guarantee Scheme (LGS) was introduced for an experimental three year period in England, Scotland and Wales in June 1981. Operation of the scheme by the Northern Ireland clearing banks only commenced on 1st April 1982. The current scheme will operate until 1989 under the following conditions:

- guaranteed loans may be for amounts up to £75,000 payable over periods of two to seven years by monthly or quarterly instalments. Capital repayments can be deferred for up to two years. The guarantees are not applicable to overdrafts;
- the Government guarantees 70% of all approved loans for which a premium of 2.5% is charged, the effect of which is to add 1.75% (i.e. 70% of 2.5%) to the interest charged by banks;
- no personal assets or personal guarantees will be taken as security to cover any part of a guaranteed loan. Any personal assets, including the applicant's home, must be already fully committed to secure conventional term loans or overdrafts before a loan guarantee will be considered. All available business assets will be required as security although the absence of these will not exclude consideration under this scheme;
- Proposals must be in respect of new or additional borrowing requirements for both capital spending and working capital where funds are not available from conventional sources.

Applicants may be made from sole traders, partnerships, co-operatives and limited companies either already trading or starting up in business. Most goods and services are covered by this scheme but there are a number of sectors excluded. The institutions participating in the scheme include all the clearing banks together with many other banks and financial institutions including Investors in Industry (3i). Government guarantees under LGS are not intended to replace existing security or to provide additional support for lendings which may be at risk. They are only available for new or additional lendings which are considered by the bank to be unacceptable because of the high gearing and lack of adequate security.

The current scheme is the third. Each scheme has seen slightly different conditions: and vetting and monitoring have generally been tightened-up (Table 16).

Table 16 International Venture Capital Markets, 1985

	1981 Scheme	1984 Scheme	1986 Scheme (current)
Guarantee	80%	70%	70%
Premium	3%	5%	2.5%

The Small Firm Loan Guarantee Scheme

Scale: The scale of each scheme has also varied greatly. Take-up has reflected the changing guarantee terms and more stringent vetting criteria imposed after the first scheme (Table 17).

Table 17 The Scale of the Loan Guarantee Scheme,1981 and 1984

	1981 Scheme	1984 Scheme
Number of loans	15,253	2,500
£ value of loans	£501.3 m	£33 m
Average value of loans	£32,900	£13,200

The Small Firm Loan Guarantee Scheme

Evaluation: The 1981 scheme created some 44,500 jobs at an average cost of £2,200 per job. Just over half the guarantees went to new businesses, and around 43% went to manufacturing firms.

Two of the most important criteria for evaluating the overall national impact of the LGS are, first, the additionality of the bank lending which is guaranteed, and, second, the viability of the business supported under the scheme. Both of these have been subject to comment by consultants appointed to review the 1981 scheme (Robson Rhodes, 1984a). Despite the Government's intentions it appears that only about half the loans were genuinely additional - that is, where in the absence of the scheme borrowers would not have been able to raise finance from elsewhere on any terms. This compounds the problem caused by the extreme financial precariousness of many of the firms benefiting under the scheme, which is reflected in high failure rates. By the time the consultants prepared their report up to one in three of guarantees issued had been drawn on and the failure rate for the first cohort of loan guarantees has now risen to 40%.

Harrison and Mason (1987) have shown that the proportion of guarantees issued in the South East / East Anglia has risen slightly from 37.1% in 1982/83 to 38.9% in 1983/84. However, there has been a progressive fall in the proportion of guarantees issued in the North West, the East and West Midlands and Wales. Nevertheless, there is no clear cut regional division in take-up rates from the LGS. They found that regions with more than their 'fair share' of scheme loan guarantees (in descending order) were the North West, Northern, South East and Yorkshire and Humberside regions. Take-up in the Midlands (East and West) and South West was only slightly lower than expected on the basis of their share of the national stock of businesses registered for VAT purposes in 1983. Scotland and Wales; however, obtained less than their 'fair share' of loans, while the very low take-up in Northern Ireland was, at least in part, a function of the administrative delay in introducing the scheme.

These variations have been tentatively attributed to a number of factors. First, it is possible that bank managers in different regions have promoted the scheme to varying degrees. The high relative take-up rate in the North West can plausibly be related, at least in part, to the fact that the banks in the region were reported to be more enthusiastic and responsive to the LGS than were their counterparts elsewhere and therefore marketed the scheme more actively to their new and existing small business clients (Robson Rhodes, 1984a). Second, the low level, in relative terms of LGS guarantees in Wales and Scotland may reflect, at least in part, the operation in these regions of the Welsh and Scottish

Development Agencies which have made available alternative sources of loan finance, often at very favourable interest rates. Finally, the low take-up rate of the LGS in Northern Ireland reflects the administrative delay in introducing the scheme (which may in turn reflect on the attitudes of the banks to the scheme in the early stages). In addition, loan and grant finance is also available through the region's small firms agency, the Local Enterprise Development Unit, and loans from this source do not incur the cost penalty inherent in the LGS.

Moreover, Mason and Harrison (1986) have indicated that the failure rates in the North West (which has the highest take-up of loans) and Wales (with the lowest take-up rate apart from Northern Ireland) are consistently higher than those recorded in other regions, while Scotland, Yorkshire and Humberside and, to a much lesser extent, the East and West Midlands, have experienced the lowest failure rates.

It has been suggested that the LGS has contributed to the weakening rather than the strengthening of the small business sector (Harrison and Mason, 1987). First, the provision of loan finance as quasi-equity leads to the problems of overgearing as the debt-equity ratio is increased. This, in turn, increases the exposure of the firm to high or rising nominal interest rates, leading to problems in servicing the debt during recession and eventually financial collapse. Second, and compounding this problem, LGS funds carry a premium which small business founders / managers who have access to and are willing to pledge collateral do not have to pay. This suggests that those firms relying on LGS funding will enter the market and begin trading with a cost disadvantage compared to those who have assets which can be offered as security.

Finally, a recent report by the National Audit Office (NAO) has suggested that the LGS may have made a contribution to job creation but question the LGS's in terms of value for money and effectiveness in nurturing businesses capable of independent life. In fact, the NAO has estimated that half the loans made under the LGS were not to those people the scheme was designed to help (Hosking, 1988).

Venture Capital

Description: The last decade has seen a mushrooming of institutional sources of equity capital for the new and small firms in the United Kingdom. The number of venture capital organisations has risen from 20 in 1979 to over 150 in 1987.

3 I dominates the institutional providers and is probably the largest organisation of its kind in the world. Founded in 1945, and jointly owned by the Bank of England and the clearing banks, 3 I has long term investments in some 4,800 unquoted companies. Alongside 3I there are the independent venture capital funds, some of which invest in the Business Expansion Scheme (BES) funds (see next section). Venture capital groups in the United Kingdom typically seek to develop a portfolio of equity investments in new businesses, established firms or management buyouts. Investments are normally in the £0.5 million to £2 million range and no more than 10 to 15% of the total resources of a venture capital fund would be committed to one firm. Larger investments are likely to be syndicated between a number of venture capital groups. Generally, venture capital organisations will expect their investments to produce a capital gain in about five to seven years, but by no means all will produce a return. It is accepted that two investments out of every ten will go into liquidation, six will survive but fail to develop and two will achieve rapid growth (Craig, 1984). However, the few successful firms will provide a sufficiently high return on the invested capital to more than offset the losses arising from those firms in the portfolio that either fail to grow or else to go into liquidation.

Most venture capital companies invest in a very small proportion of the applicants for funds which they receive and are reluctant to undertake the additional administrative costs (in relative terms) of making small investments in smaller and more risky enterprises which necessitate a greater involvement of management expertise provided by the venture capital institutions. In 1984, for example, venture capital organisations in the United Kingdom invested an average of £389,000 in each of 729 companies (Venture Economics, 1985).

Venture Capital

Scale: In 1985 venture capitalists invested some £687 million, including £147 million of BES funds (Table 18).

Table 18 Sums Invested by Venture Capital Organisations, 1985

Venture capitalist organisation	Sums invested (£ million)
3 I (year end 31.3.86, including loans)	260
Independent firms	280
Business Expansion Scheme	147
Funds	46
Loans	101
Total	687

The total pool of venture capital investments by United Kingdom funds now comes to over £3,000 million. It would seem that 1985 was something of a plateau for the independent funds as the capital they raised fell back from £247 million to £195 million in 1986.

Venture Capital

Evaluation: In terms of the pool of venture capital, the United Kingdom compares very favourably with other countries (Table 19).

Table 19 International Venture Capital Markets, 1985

Country	Total number of venture capital firms	Total venture capital pool £m	Venture capital pool per head of population (£'s)
USA	550	13,000	55
UK	126	3,000	54
France	45	500	9
Japan	70	600	5
West Germany	25	300	5
Denmark	14	80	5
Ireland	10	70	4

However, the industry is moving towards larger investments, particularly the independent funds. For 3i whilst 46% of investments are below £100,000, this represents only 8% of the investment by value (Table 20). For independent funds only 28% of investments were under £100,000 and this represents 3% of the investment by value. The BES stands out as providing 64% of its investments in amounts below £100,000 representing 10% by value.

Table 20 Proportion of Venture Capital Investments Below £100,000 and In Start-Ups

Amount invested per company	3i		Independent funds (**)		BES Funds & Direct	
	% by number	% by value	% by number	% by value	% by number	% by value
Up to £100,000	46	8	28	3	64	10
In start-ups	na	25 (*)	19	13	na	na

Notes: * Defined as under 3 years old.
** Include BES funds.

Sources: Venture Economics (May 1986); Inland Revenue Statistics, BES 1984/85; and 3i Annual Accounts.

Nevertheless, with an average size of financing of £564,000 in 1986, the United Kingdom average investment is half that of the United States.

Mason (1987) has shown that the geographical distribution of venture capital investments within the United Kingdom is characterised by marked inequalities between regions. The South East of England has been the major beneficiary: in 1985 Greater London accounted for 35% of venture capital investments by value and contained 23% of recipient companies; the remainder of the South East region claimed a further 25% of the funds invested and 24% of the venture capital-backed companies. The extent of this overconcentration of venture capital investments in the South East region can be guaged by the fact that it contained only 32% of the total stock of VAT-registered businesses in the United Kingdom business stock (Ganguly, 1984). In contrast, in Scotland, Wales and northern England which together contain one-third of the United Kingdom business stock (Ganguly, 1984) - attracted just 17% of venture capital investments in 1985. Investments by investors in industry (not all of which is 'venture' capital) is similarly concentrated in the South East, with 27% of loans and shares (by value) going to greater London and a further 24% to the rest of the region (Financial Times, December, 1986).

One explanation for these regional variations is that the lack of venture capital investments in the peripheral regions is a function of the paucity of small businesses with the potential for rapid growth (Financial Times, July, 1982). The alternative explanation is based on the fact that, like most United Kingdom financial institutions, venture capital funds largely operate from London. Of the 50 full members of the British Venture Capital Association (BVCA) in 1985, 70% are based in London and a further 8% operate from other parts of the South East region (Mason, 1987). It is equally plausible to interpret the concentration of venture capital funds in London and the concentration of venture capital investments in South East England as a result of the 'hands on' style of management adopted by such organisations. As a condition of investing, venture capital funds normally require that one of their executives joins the board of the investee company as a non-executive director. The need for frequent visits to monitor the performance of such companies that is deemed to be necessary makes geographical proximity between funds and client highly desirable and when allied to the shortage of experienced venture capital executives, encourages funds to restrict their investments to companies located within easy travelling distance of London. This consideration clearly militates against investments in the peripheral regions.

The Business Expansion Scheme

Description: The Business Expansion Scheme (BES) was introduced under the Finance Act in 1983 as a successor to the more restricted Business Start-Up Scheme which was established in 1981. It is aimed at overcoming the problems encountered by new and established small businesses in attracting venture capital on account of the lack of a track record and consequent higher risk. The objective of the scheme is to increase the flow of equity capital into small firms by offering substantial tax breaks to investors. Under the BES, private individuals can claim tax relief at their top rate on investments in new equity of unquoted companies up to a maximum investment of £40,000 per year. Such investments can be made in two ways.

First, individual tax payers can invest in 'direct issues' (minimum of £500 per company) - companies issuing shares directly to the public. Companies can either organise their own share issues with the help of an accountant or solicitor or can appoint a sponsor - usually a merchant bank, licensed securities dealer, member of FIMBRA, stockbroker or venture capital house - who prepares and issues the prospectus, organises publicity, receives applications and allocates shares. Sponsors charge a fee or commission which is related to the amount of capital raised and levy a management charge for work done during the following five years. Some sponsors may even take options over the shares.

Alternatively, individuals can invest through specialist 'BES investment funds' which pool investors money in order to invest in a portfolio of companies, thereby spreading the risk of failure and loss of the invested capital. In addition, representation of the fund on the board of investee companies can safeguard the interests of investors to ensure, as far as possible and thereby risking the loss of tax relief. Managers may also be able to offer skills to augment those of the original proprietors of the companies funded.

There are two types of BES funds. In 'approved funds' the managers must act as nominees for individuals in managing the funds on their behalf. Approval is given to fund managers by the Inland Revenue where they and their proposed fund meet the requirements of the legislation and also the Inland Revenue's extra-statutory requirements. In approved funds the £500 minimum investment per company per individual does not apply, although the Inland Revenue usually stipulates a minimum subscription amount of not less than £2,000 in respect of individual subscribers. Approved funds are 'closed', in the sense that the managers may not make investments until closing the fund to subscription from investors.

'Non-approved funds' have greater flexibility in that they can be open-ended and continue to take subscriptions whilst investing money already subscribed in qualifying companies. This means that early investors can be placed before later investors and should therefore be able to obtain their tax relief earlier than with an approved fund. However, the £500 minimum investment per company per individual applies. Unlike approved funds, investors can subscribe again whenever they wish, up to the £40,000 maximum for tax relief, and non-approved schemes may mix BES and non-BES money.

The Inland Revenue scrutinises the investments to ensure that they are within the rules of the scheme. In brief, the investor must be a UK resident and must not be 'closely connected' with the company in order to qualify for tax relief. Broadly, this means that an individual must not (together with any associate) own more than 30% of the company, taking into account the BES investment, and is neither an employee, partner nor a paid director in the company. The relief is granted for investments in new, genuinely additional and full-risk ordinary share capital and the investor must retain his shares for at least five years. Trades which do not qualify under the scheme include: dealings in land shares, or commodities; leasing and letting assets on hire; banking, finance and insurance and other financial services; and, since the 1984 Finance Act, farming. Qualifying companies must carry on their trade wholly or mainly in the United Kingdom (for a detailed outline of the BES legislation refer to Watkins and Knowlman, 1987). Three further changes to the scheme were announced in the March 1988 Budget. First, an attempt to improve the targetting of the scheme at small companies the Chancellor proposes to limit the amount of investment in a company in any twelve month period which can qualify for tax relief to £500,000, except for ship chartering for which a £5 million limit will apply. Second, in a further attempt to reduce the pressure on fund managers to make investments before the end of the tax year, tax relief for investors in approved BES funds will be given by reference to the closing date for investment in the fund rather than, as previously, the date that the fund invests in the company. At least 90% of the amount subscribed by the individual to the fund must be invested in eligible shares within six months of the closing date. Third, in order to support the Government's Housing Bill the BES is to be extended to investment in companies specialising in letting residential property on new style assured tenancy terms over a period of at least four years from the date it issues its BES shares.

The Business Expansion Scheme

Scale: Between 1983 and 1986, the scheme raised a total of £410 million (see previous section).

Evaluation: A government commissioned report by Peat Marwick on the BES in its first year of operation (1983-84) was published in 1986. This was generally very favourable, concluding that without BES:

- 94% of finance invested by individuals would not have gone to particular companies.
- 93% would not have been invested in United Kingdom unquoted companies.
- 73% would not have been invested in equities in general.

It went on to extrapolate that, without BES, 70% of the money invested would not have been raised by recipient companies at all. Further, in the year following the investment, BES would generate some £100 million of additional turnover and create 4,000 jobs.

However, the report suggested that the process of obtaining BES finance was by no means invariably a straightforward exercise, with 57% of firms in their survey reporting that it was a disruptive experience (22% claimed it was 'very disruptive'). The main sources of disruption experienced by companies which obtained finance through BES funds was mainly related to the pressure of time in producing information and in their general dealings with the fund. Indeed, it is interesting to note that 32% of firms which reported no real disruptions in their dealings with BES had sought out the funds themselves and had handled most of the preparation of the company profile or prospectus with little or no outside help. Peat Marwick found around half of their sample of recipient companies did not fully explore all possible sources of finance, either because they did not think that other sources would provide finance, the urgency of finding funds, their lack of awareness of alternatives or a belief that the BES was the best source.

A less tangible, but no less important benefit of finance raised through BES funds is access to the professional, marketing, planning and financial skills of fund managers. But some firms were unhappy with the lack of involvement by the fund after the investment had been made while others complained that the non-executive director appointed by the fund were either inexperienced in business or else ignorant of the firm's products or problems.

The Peat Marwick report suggested that a further advantage of raising finance through the BES is the base that it provides for companies to raise additional funds otherwise denied to them. But some BES recipient companies have encountered difficulties in second-round financing as a result of the legal restrictions of the scheme. The problem is that the non-BES potential financial backers may be unwilling to provide finance because of the need to observe BES rules so that original BES members do not lose their tax relief.

Recently, the character of the scheme has changed in a number of respects, notably the type of investments, the scale of investments and the types of recipient businesses with the following results (Mason et al., 1988). First, although the amount of finance raised by companies through the BES (£410 million in the three years, 1983-84 to 1985-86) is relatively significant in relation to other sources of venture capital finance, the take-up rate has been very low compared with other Government schemes to assist the small business sector.

Second, while the majority of companies have raised small amounts of finance through the scheme much of the finance invested has not contributed to a reduction in the size of the equity gap. In 1985-86, 70% by value of the finance invested through the scheme was in companies which each raised over £500,000. Moreover, the average size of investments under the scheme has increased from £147,000 in 1983-84 to £234,000 in 1985-86. These features of the scheme are largely a reflection of the increasing significance of prospectus issues, which are typically used by companies to raise amounts in excess of £500,000 (50% of all prospectus issues in 1983-84; 69% in 1986-87) and of a relative decline in fund investments, which predominantly make investments in the £50,000 to £500,000 range (77% in 1983-84; 79% in 1986-87). Nevertheless, the BES has made a more significant contribution to reducing the equity gap for businesses requiring less than £100,000 than the institutional venture capital industry. The reduction in the size of the equity gap has been largely due to informal direct investments.

Third, the scheme has not assisted significant numbers of high-risk businesses. Instead, the bulk of the finance raised through the scheme has been invested in service sector businesses, often asset-related, and predominantly in the wholesale, retail, real estate and leisure sectors. Although manufacturing companies have accounted for a fairly constant proportion of all BES investee companies over time (approximately 40%), the proportion of total finance invested in the manufacturing sector has declined from around one-third in 1983-84 to under one-quarter in 1985-86.

Fourth, the scheme does not appear to have led to a significant widening of share ownership. The proportion of higher rate taxpayers who invested through the scheme is estimated at only 2% in 1983-84. Moreover, most BES investors already invest in equities and the BES investment represents a very minor part of their investment portfolio.

Fifth, since 1983-84 the scheme has been associated with a significant increase in the average size of investments and an increase in the proportion of finance invested in non-manufacturing sectors, it is likely to have resulted in a decline in the additionality achieved by the scheme and led to an increase in the cost-per-job (which even in 1983-84 was higher than that for other small firm schemes). With the benefit of a longer time-period the Mason et al., (1988) report revealed high loss rates amongst fund investments made under the BES (over 50%) and, particularly in the early years of the BES (over one-quarter of investments made in 1983-84 and 22% of the capital invested in that year had been lost by late 1987). Overall, of the £175 million invested by funds and managed schemes in the seven years to April 1987, 17% had been lost by late 1987. This reinforces the view that the economic impact of the scheme is less favourable than that suggested by Peat Marwick.

Finally, the Mason et al., (1986) report highlights the significant regional inequalities in the impact of the scheme. The South East and East Anglia contain considerably more than their 'fair share' of BES investments relative to their shares of the total stock of UK businesses (51% of investments and 65% of the invested capital in the period 1983-84 to 1985-86 inclusive). All other regions contain less than their 'fair shares' of BES investments. All types of BES investment are disproportionately concentrated in the South East region; however, the over-concentration in the South-East (65% of companies; 71% of finance raised) is significantly greater than for fund investments (48% of investee companies; 54% of finance invested) and direct investments (46% of investments). Not surprisingly, BES investors are also concentrated in southern England. Nevertheless, the proportion of BES investments in the South East is much greater than its share of BES investors; conversely, in the rest of the country the proportion of investors is greater than its proportion of investments. Hence, a further adverse impact of the scheme on United Kingdom regional economic development has been to produce a north-south flow of risk capital.

With regard to the cost to business of using the BES investors are usually charged a fee for the work that is done on their behalf by the Funds. This is typically a percentage of the initial investment ranging up to 8% of the total. Some funds also make an annual charge to investors, typically 1% per year.

Some funds, however, charge investors nothing. Another source of income for the Funds is the interest earned on the investor's subscription prior to investment in a company. One fund also makes a charge against the realised profit when shares are sold (Watkins and Knowlman, 1987). Moreover, the cost to the Exchequer of the scheme in 1983-84 was in the order of £40 million (Mason and Harrison, 1986).

Capital Markets

Description: At the top end of the equity market in the United Kingdom we now have access for small businesses to the stock market through the *Unlisted Securities Market* (USM). The USM was created in November 1980 by the London Stock Exchange. Its purpose is to provide smaller, growing businesses with access to a capital market at lower cost than is involved in obtaining a full stock exchange listing and with less onerous entry requirements. In the USM only around 10% of the company's shares need to be made available to the public (not 25% as with a full listing) and substantial private companies wishing to raise share capital can arrange to place minority stakes with other institutions for fees of around 1 to 1.5% of the amount raised. Such institutions are unlikely to interfere in the day-to-day running of the company. Although there is no formal minimum size requirement for the USM, most companies must have a trading record of three years. Once listed, USM companies have to sign an undertaking, which contains some twenty provisions, virtually identical to the standard stock exchange listing agreement, most of which are designed to enforce a minimum standard of regular disclosure of the company's affairs. By June 1987 it had enabled some 565 member companies to raise over £1,100 million (over eighty of these companies subsequently graduated to a full listing on the London Stock Exchange). The cost of a USM listing is not likely to be much less than £100,000. Opinions differ, but most experts consider that pre-tax profits running at around £100,000 to half a million are generally a necessary pre-requirement.

Indeed, with over 65% of issues on the USM now involving administrative costs of over £100,000 to raise on average just over £2 million (Buckland and Davis, 1984), this source of equity capital is effectively barred to all but the very largest and most dynamic 'small' firms. It seems likely that, for the immediate future, the USM will often only serve as a means whereby proprietors can get their money out of their firms, rather than putting new money into them.

The expansion of the over-the-counter (OTC) market has provided a source of equity capital for small unlisted companies, particularly those at an early stage in their development. The OTC markets in unlisted shares operated by specialist institutions or merchant banks. These licensed dealers may deal directly in unquoted shares, others just act as agents bringing buyer and seller together. OTC shares are not governed by the rules of the Stock Exchange and they do not enjoy its protection.

Capital Markets

Scale: By June 1987 the USM had enabled 565 companies to raise over £1,100 million (Table 21). In the process it had created some 650 millionaires, an average of two a week since its inception.

Table 21 USM Listings

Year	Number of listings	Amount raised £'m
1980	23	12.4
1981	59	73.8
1982	63	74.3
1983	89	181.0
1984	100	179.4
1985	99	202.6
1986	94	300.0
1987 (6 months)	38	85.0

Evaluation: The success of the USM is only partly related to the new capital it raises. Its existence also creates an exit route through which entrepreneurs and earlier stage capital investors can realise their investment. This should make new firm creation and growth more attractive to both the entrepreneur and the venture capital investor.

5. GRANTS FOR SMALL FIRMS

There is now a plethora of cash grants to help and encourage businesses to set up and expand. Schemes to encourage new businesses to set up are largely confined to selected regions where unemployment is highest. There are many inner-urban schemes financed by local authorities. In addition there are national schemes which offer both automatic and discretionary cash grants.

Regional Grants

Description: Discretionary grants, called Regional Selective Assistance, are available towards the cost of projects, including new physical assets and essential related training costs, which create or preserve jobs. These are available in 'Development Areas' and 'Intermediate Areas', provided they meet the normal Regional Selective Assistance criteria, i.e., the project must be commercially viable, create or safeguard employment, demonstrate a need for assistance and offer a distinct regional or national benefit. The amount of grant will be negotiated as the minimum necessary to ensure the project goes ahead. An important consideration in any RSA is that a substantial amount of project costs must be met by private sector finance.

Companies in Development Areas with less than 25 employees may also be eligible for a Regional Enterprise Grant for Investment. The amount available towards the fixed asset cost of a project is 15% up to a maximum grant of £15,000. Only one application per business will be accepted by the Department of Trade and Industry and no applicant will receive more than £15,000 in total assistance. The grant will be selective and the applicant will be required to submit a business plan demonstrating the need for assistance and the viability of the project. The new investment grant will not be paid in addition to RSA.

Also, from April 1, 1988, the Support for Innovation scheme for companies with less than 25 employees has been replaced by a Regional Enterprise Grant for Innovation. This provides assistance towards the cost of developing new products and processes. Only one application per business will be accepted and the maximum grant is £25,000. In Scotland, this new innovation grant has replaced the old Better Technical Services scheme. Furthermore, Scotland, Wales and Northern Ireland have their own grant schemes administered through their development agencies.

Regional Grants

Scale: In the financial year 1986 / 87 £543.4 million was spent on RDG projects with a further £261.8 million being allocated to RSA measures.

Evaluation: Not surprisingly, the main beneficiaries of RDG and RSA grants have been the problem regions of Scotland, Wales, Northern , the North West and Northern Ireland.

The Enterprise Allowance Scheme

Description: The Enterprise Allowance Scheme (EAS) was set-up nationally on the 1st August 1983 to encourage unemployed people to set up their own business . Under the scheme a flat rate, taxable allowance of £40 per week for 52 weeks is paid to people qualifying under the scheme in order to supplement their business receipts while it is becoming established. In addition to this limited business advice is provided by the Department of Trade and Industry's Small Firms Service.

Entry into the scheme is strictly controlled by the Department of Employment. Only people unemployed or under a formal redundancy notice for at least 13 weeks can apply, and if jobless they must be in receipt of unemployment or supplementary benefit. In addition, the applicant must be willing to work full-time in the business, have at least £1,000 to invest in it (or a bank loan or overdraft for that amount), and be over 18 and under pensionable age. The business itself must be new, independent and employing less than 20 people in its first three months. Certain businesses (such as those involving gambling, pornography or politics) are not eligible.

The Enterprise Allowance Scheme

Scale: Over 329,000 people have qualified for EAS between the pilot launch in 1982 and end of March 1988. This has resulted in grants totalling approximately £1,300 being paid in 1987/88 106,300 people qualified for support.

The scheme is administered regionally, with regional 'quotas' for awards based upon regional 'need' - generally high rates of unemployment.

The Enterprise Allowance Scheme

Evaluation: Under the pilot scheme for EAS (in five areas in February 1982) a total of 3,331 people set-up in business. A study based on a 20% sample of participants in the pilot areas noted that 90% were male and over 35% of those in receipt of an allowance were under 35 years of age. One-quarter of the participants had been unemployed for over 12 months and, not surprisingly, the biggest single reason given for joining the scheme was the failure to find a job, although this accounted for under one-third of the total number of participants. Three-quarters of the businesses established were in the service sector - notably construction (especially repairs), retailing, and garage repairs, all activities where barriers to entry (skill and capital) are low - whereas only 13% of businesses were in manufacturing, despite the fact that over 40% of participants were previously employed in this sector. The job creation generated under the scheme was estimated at 50 additional employees per 100 businesses after nine months, but as 75% of businesses had no employees it is clear that a relatively small number of firms have generated a substantial proportion of the extra jobs (Department of Employment, 1984).

In addition, the survey estimated that the deadweight in the pilot scheme was around 100 businesses formed under the scheme was around 50%; in other words, for every 100 businesses formed under the scheme only around 50 did so only because the EAS was available. Moreover, deadweight businesses were on average larger in employment terms than non-deadweight ones. However, a follow-up survey of EAS participants after they had left the scheme concluded that the allowance had made a significant contribution to the survival of both types of firms during the vulnerable first year of trading. Indeed, 80% of businesses were still in existence six months after leaving the scheme. Overall, the pilot version of the scheme is estimated in its first year to have involved in a net cost to the Exchequer of £2,690 per person taken off the unemployment count. Moreover, under EAS there is no additional public expenditure after twelve months but if a firm continues to trade after this period there are continuing Exchequer savings from lower unemployment and higher taxation receipts, thereby reducing significantly the longer term net costs, perhaps to £650 per person removed from the unemployment register over two years (Department of Employment, 1984).

Take-up rates have varied between regions (Mason and Harrison, 1986). The North West has had the highest unemployment-weighted take-up rate when measured both in terms of the cumulative number of participants at November 1984, followed by the South West and Wales, another 'peripheral'

region. The Midlands (both East and West) and the southern area (East Anglia and the South East Standard Regions, excluding Greater London) also had take-up rates above the national average. However, the lowest take-up rates were recorded in certain peripheral regions, namely the North, Scotland, and Northern Ireland, but also in Greater London. One reason for this lack of a clear-cut distinction in the takeup rate of the EAS between the southern regions and the remainder of the country is that participation under the scheme is allocated according to regional quotas which reflect differences in 'need'. Hence the total number of places available has been divided amongst the regions on the basis of the numbers of long-term unemployed, although subsequently this has been modified to take account of the differing level of demand in each region.

Recently, the National Audit Office (NAO) has recommended that 'viability checks' be introduced to the EAS, which costs the Exchequer about £200 million a year (Hosking, 1988). At present there are no checks on the applicant's business proposal. Only activities clearly unsuitable for public funding such as gambling and pornography are ruled out. EAS ventures have tended to be concentrated in the service sector, where start-up costs are minimal. Out of the 329,000 people helped under EAS since 1982, 47,405 (14.4%) have dropped out. As the scheme has increased in popularity, the drop-out rate has risen. In 1987/88 an estimated 17,000 EAS participants out of a total of 106,300 dropped out (16%) during the twelve months they were on the scheme. Surveys suggest that of the survivors, one-quarter fail within six months of the £40 allowance ending. Only 57% of EAS businesses survive to celebrate their third birthdays. On the basis of this evidence, the NAO has suggested that 'losers' should be avoided and the Department of Employment should concentrate resources on entrepreneurs who would be 'winners'. The NAO also suggested that applicants should be encouraged to carry out market research to ensure that demand exists for the services they plan to offer

Small Engineering Firms Investment Scheme

Description: The Small Engineering Firms Investment Scheme (SEFIS) was established following the 1982 Budget to assist small firms in the engineering industry to undertake investment in certain types of advanced capital equipment, notably numerically controlled and computer controlled machine tools. The underlying objective was to strengthen the innovative capacity of small engineering firms by helping them to introduce new products and production techniques, and to secure improvements in their productivity and reliability. The scheme, which operated on a selective basis, offered a capital grant of one-third of cost of one project up to a maximum project cost of £200,000. Companies operating in Division 3 of the 1980 Standard Industrial Classification (Metal Goods, Engineering and Vehicle Industries) and employing not more than 200 full-time staff were eligible to apply under the scheme. Moreover, the scheme was unusual in having an implicit regional bias in the sense that companies receiving a SEFIS grant and located in an Assisted Area could also qualify for Regional Selective Assistance and European Community grants. In these cases the SEFIS grant was determined as one-third of the cost of the project net of Regional Selective Assistance.

Small Engineering Firms Investment Scheme

Scale: The Government allocated £30 million to the scheme (although it was initially intended to have a £20 million limit) but its popularity was such that this amount was used up in less than two months. A second version of the scheme - SEFIS II - was therefore introduced in the 1983 Budget with an allocation of £100 million. It was open to all small firms instead of being restricted to Division 3 of the SIC as previously, the maximum size was raised to 500 employees and all businesses, including subsidiaries of foreign firms, were eligible. However, the level of demand was much lower than for SEFIS I and the available funding had not been fully allocated by its closing date in September 1984, a situation which has been widely ascribed to the depressed condition of the UK engineering industry. Many business did not have sufficient orders to justify the extra financial commitment involved in a major high technology re-equipment programme.

Small Engineering Firms Investment Scheme

Evaluation: An evaluation of the original scheme by Research Associates Ltd (1984) concluded that SEFIS I had clearly met its original objective of stimulating investment by small engineering firms in advanced capital equipment. Moreover, the scheme has had a favourable aggregate impact on the firms that benefited, with the creation of 1,279 new jobs and the saving of 1,520 jobs, an increase in annual output of £77 million and in profits of £5 million. However, only about 66% of SEFIS I recipients made genuinely 'additional' investments in new machinery. When fully discounted for this additionality element, SEFIS I was estimated to have created 512 new jobs and saved 172 existing jobs amongst recipient firms and increased their annual profits by £2 million. But because 75% of SEFIS recipients were sub-contract engineering firms serving what is a finite market, it is highly probable that their extra business and jobs have been gained at the expense of competitors, thus resulting in a substantial displacement effect. Favourable indirect impacts of SEFIS I include 'imitation effects' whereby other small engineering firms have been encouraged to invest in advanced machinery in order to remain competitive, and 'knock on' effects on the customers of SEFIS firms in the form of faster delivery, improved quality and price reductions which might be expected to enhance their competiveness. In addition, United Kingdom manufactures supplied 59% of the machines purchased under SEFIS I, proving a welcome boost to the British machine tool industry.

Mason and Harrison (1986) have shown that a regional distribution of the firms in receipt of SEFIS I grants shows a marked concentration in the South East Region which contained 36% of the total, but because the average size of grant in the region was below the national figure, its share of total funding was somewhat lower at 32%. The West Midlands, in second place, contained 18% of SEFIS recipients and received a similar proportion of total funding. Mason and Harrison (1986) also indicate that Northern Ireland and the South West had received 'excessive' shares of the SEFIS grants. The South East region had more than its fair share of SEFIS recipients. At the other extreme, Wales, the North West, Yorkshire and Humberside and, to a lesser extent Scotland were under-represented in terms of both their proportions of SEFIS recipients and shares of SEFIS funds. The West Midlands, which the scheme was implicitly designed to help the most obtained less than its 'fair share' of SEFIS grants, a less favourable outcome than might have been anticipated.

6. ADVICE FOR SMALL FIRMS

The cornerstone of the United Kingdom advice network for small firms is the Enterprise Agency network which is coordinated nationally through Business in the Community. This network is locally based, attracting significant support for large private sector companies. Government financial support for the network is limited.

The Government has its own advice agency - The Small Firms Service - whose work is supplemented in rural areas by the Development Commission (until 1988 known as the Council for Small Firms in Rural Areas, CoSIRA). In addition, the Enterprise Initiative, launched in 1988, encourages small firms to use private consultants by offering subsidies for the consultancy project.

Enterprise Agencies

Description: There are over 268 Enterprise Agencies, locally based throughout the United Kingdom (in Scotland they are called Enterprise Trusts). Some have been in existence for a decade although most have only been set up in the last three or four years. They are usually run by a small staff of two or three people (the largest agency has 21 people).

Enterprise agencies are funded from a number of different sources. Government support through the Department of Trade and Industry has been increased since January 1988. However, it is intended that the bulk of the funds will continue to come from local authorities and large companies, so as to preserve the private and local element and prevent the establishment of a bureaucracy. Currently some measure of co-ordination for enterprise agencies is provided by its 'umbrella' organisation, Business in the Community (BIC). BIC is supported by some 300 corporate members who provide funds and secondees for the local agencies. In 1987, 245 secondees were deployed to local agencies and 30 to the BIC executive unit. However, some 70% of Enterprise Agency Directors are salaried. Under the Enterprise Agency Grant Scheme, Central Government made available some £2.5 million, to encourage increased private sector support, by providing matching funding within certain limits. The first year funding has also been completely taken up and over 80% of the total application amount was met. All Enterprise Agencies offer the basic service of free business counselling. However, more are offering a wider range of services, for which charges are often made. These are detailed in Table 22.

Table 22 Enterprise Agency Activity, 1987

Activity	% of agencies involved
Counselling	100
Training courses	79
Newsletters	66
Exhibitions	57
Asset loan / grant funds	56
Education links	54
Small business clubs	48
Youth enterprise	45
Managed workspace	44
Property register	42
Trade directories	28
Meet-the- buyer exhibitions	23
Business to business	20
Business competitions	20
Resource matching bureau	14

Enterprise Agencies

Scale: BIC was formed in 1981 when there were just 23 Enterprise Agencies. In 1987 there were 268 Enterprise Agencies (199 in England, 38 in Scotland, 19 in Northern Ireland and 14 in Wales). Excluding the Scottish Enterprise Trusts, they employ approximately 1,000 people, have over 270 secondees from BIC corporate members, and have an estimated annual running cost of £26 million.

Enterprise Agencies

Evaluation: BIC estimate that agencies are helping to create or save more than 70,000 jobs a year. A recent survey showed that firms assisted by agencies were twice as likely to survive as suggested by the VAT deregistration statistics (Business in the Community, 1987). However, such statistics involve an element of double counting since those firms coming to Enterprise Agencies for assistance are also likely to seek other forms of assistance for small firms.

The Small Firms Service

Description: The role of the Government's own *Small Firms Service* is to change and it is intended that the Small Firms Service will become a 'consultant' to the enterprise agencies, expending into more specialist areas such as marketing, new technology and patent advice and leaving day-to-day advice to the enterprise agencies. The Small Firms Service provides a comprehensive information and counselling service on a wide range of business matters, both to established firms and those considering starting one. The advice available includes taxation, sources of finance, government assistance schemes, local authority planning requirements and employment legislation. The service's business counsellors will help businessmen with the preparation of a business plan. Counsellors can analyse the needs of established businesses and bring to bear appropriate advice and experts in such fields as marketing, exporting, stock control and raising the finance needed for expansion. Moreover, the service operates through a national network of twelve Small Firms Centres backed up by over eighty Area Counselling Offices throughout Great Britain.

The Development Commission

Description: Enterprise agencies tend to be based in major urban areas. To redress this imbalance the *Council for Small Firms in Rural Areas* (CoSIRA) had established offices in each of the English counties. In April 1988 CoSIRA was merged with the Development Commission to form a new organisation with the aims of premises provision, aid to small business and community development. Each county has a representative backed by a voluntary committee which can call upon the Development Commission consultancy service run by over 100 officers. The Development Commission also organises training, provides professional consultancy, and local advice, runs workshops and offers extended loans. To help small businesses grow the Commission provides a wide range of financial help, export advice and training through its network of 32 Business Services centres throughout rural England. The Commission has also identified 27 priority Rural Development Areas (RDA's) in which small firms receive special help.

The Development Commission

Scale: The scale of assistance given by the Development Commission has grown markedly in recent years. In 1983 assistance was given to 15,061 businesses compared to 27,413 businesses in 1987. Moreover, the number of Commission workshop units has increased at similar rate from only 68 in 1981 / 82 to 329 in 1986 / 87. The Commission helps to create some 5,000 job opportunities each year in rural areas.

The Development Commission

Evaluation: Its schemes are cost-effective and use a relatively modest budget (£32 million in 1988 / 89) to unlock from other sources, not least the private sector (Rural Development Commission, 1988).

The "Enterprise Initiative'

Description: In a Government White Paper, published on 12 January 1988 changes in the policies and role of the Department of Trade and Industry (DTI) were announced under the umbrella of the 'Enterprise Initiative'. The objectives of the DTI are to encourage business to use its initiative and enterprise, so that it sees the opportunities and takes them. Linked with the objective of increasing prosperity the Department will assist this process throughout the economy and to champion the people who make it happen, rather than just individual sectors, industries or companies. Government is attempting to create a climate that stimulates enterprise and reduces red tape. The DTI suggests that business flourishes in a competitive and open economy and their aim is to secure this both at home and abroad. The growth in international trade will be promoted by the DTI and it will work towards a single market within the European Community. Furthermore, the DTI seeks to produce a more competitive market by encouraging competition and tackling restrictive practices, cartels and monopolies; secure a more efficient market by improving the provision of information to business about new methods and opportunities; create a large market by privatisation and deregulation; and increase confidence in the working of markets by achieving a fair level of protection for the individual consumer and investor. Related to the above points, the Government wishes to encourage the transfer of technologies and co-operative research, the spread of management education and the growth of links between schools and the world of work, Finally, the DTI's objective is to produce a climate which promotes enterprise and prosperity. In all the 'Enterprise Initiative' schemes the differing circumstances of the regions and of the inner cities to enable those who live there to help themselves. Therefore, the effect of the 'Enterprise Initiative' and other recent Government initiatives is to make financial assistance more and more discretionary. There is a special emphasis on small and medium-sized businesses and on companies carrying out capital projects in the sixty-one inner city area and the Assisted Areas.

By 1991 some £250 million should be committed to the DTI's 'Enterprise Initiative', which is aimed at all independent businesses, or groups, in most sectors of the economy throughout the United Kingdom which employ less than 500 people. Grants are available to subsidise business development consultancy in: design, marketing, quality, manufacturing, exports, business planning, financial / information systems and research and technology.

The DTI will provide assistance for a maximum of 15 consulting days, though assignments can be longer than this. The DTI will normally pay half the cost of the consultancy project, although in inner cities and Assisted Areas two-thirds of the cost will be borne by the DTI. Before help with any of these initiatives can be provided, the DTI (in Scotland the Scottish Development Agency (SDA) and the Highlands and Islands Development Board (HIDB), and in Wales the Welsh Office acting as agents for the DTI) investigate by visit from an 'enterprise counsellor' who will undertake a free business review. The enterprise counsellor will work with the company to identify the most appropriate sources of help required. To be approved for financial assistance, a consultancy project should be aimed at making a significant contribution towards the company's development, especially in management expertise. Enterprise counsellors are employed by the DTI on a consultancy basis and will spend up to two days visiting each potential recipient of advice under the Enterprise Initiative. Within one week of his visit, the enterprise counsellor has to make a formal report to the DTI (in Scotland the SDA / HIDB and in Wales the Welsh Office) presenting his recommendations. The DTI will pass the report to the relevant 'scheme contractor' who will then allocate an appropriate consultant to the company. All consultants have to be listed with scheme contractors to be able to provide consultancy advice through the Enterprise Initiative.

'Scheme contractors' are those organisations appointed by the DTI to co-ordinate the various initiatives and assign consultants to each project. The Institute of Marketing manages the marketing initiatives, the Design Council covers the design initiatives and the Production Engineering Research Association (PERA) covers both the quality and manufacturing initiatives, 3i Enterprise Support Limited has been appointed scheme contractor for both the business planning and financial / information systems initiatives.

In addition to allocating consultants, scheme contractors will also be required to monitor quality control of the individual assignments. Each local DTI office will employ 'enterprise advisers' and part of their role will be to ensure that applicants are indeed receiving the help that they require. It would appear that it will take a minimum of four to six weeks from the time of enquiry through the DTI to the consultant actually starting the work. It is the responsibility of the applicant and the consultant to decide upon the detailed terms of the reference, the timing of the assignment and the fees to be paid. The company will pay only the portion it is liable for and the consultant will seek to recover the balance of his fees from the appropriate scheme contractor. Scheme contractors will only pay once the work has been completed.

This is an added safeguard to the applicant to ensure that the consultants provide the services that is required from them.

Business Improvement Services consultancy support in England and Wales will still be available in all areas where funds have not been exhausted. BIS will not be paid in addition to consultancy advice under the new Enterprise Initiative. It is therefore in the best interests of both the applicant and the consultant to consider carefully which scheme would be more beneficial.

In Scotland, the Better Business Services (BBS) scheme, which allows access by businesses to professional advice at subsidised costs, used to be administered by the Industry Department for Scotland in the Strathclyde region, the HIDB for the Highlands regions and the SDA covering the remainder of Scotland. From the beginning of April, the HIDB continues to cover the Highland regions but the SDA has taken over administering BBS for the remainder of Scotland. The BBS scheme will be limited to companies of up to 50 employees requiring basic advice and counselling.

The "Enterprise Initiative'

Scale: Since the launch of the Enterprise Initiative on 13 January nearly 94,000 enquiries have been received for the Enterprise Initiative booklet (as at 24 June 1988) from firms and intermediaries. In addition 58,000 leaflets containing more detailed information on individual initiatives have been issued (as at 24 June 1988). The Department has spent some £1.47 million on these initiatives (end May 1988) and has a budget allocation of £74 million for the financial year 1988 / 89. By 1991, it is planned that some £250 million will be committed to the scheme over the three year period.

The "Enterprise Initiative'

Evaluation: It is too early to provide any evaluation. However, it has been suggested in the press that the take up of the scheme has not matched Government expectations.

Other Sources of Advice

BSC Industries Limited

BSC Industry Limited, a subsidiary of the British Steel Corporation, was formed in 1975 to help businesses start-up, expand or relocate in designated areas where steel industry jobs have been lost. There are nineteen 'BSC Industry Opportunity Areas' in the United Kingdom. BSC Industry can provide a wide range of assistance to job-creating businesses, including direct financial help in appropriate cases. The company also operates managed workshops sites where small units are available to start-up and developing businesses on easy-in, easy-out licence terms. Moreover, BSC Industry Limited works closely with the Enterprise Agencies operating in each of its areas.

Tourism

Specialist advice about the development, financing and marketing of tourism enterprises is available from the national tourist Boards, In addition, each of the tourist boards operates a scheme of selective financial assistance. Advice about promoting tourist attractions overseas can be obtained from the British Tourist Authority. Financial assistance may be available in the form of co-operative ventures.

Cooperative Development Agency

In recent years many people starting in business have recognised that running the business on a co-operative basis might suit their business needs and aspirations. The National Co-operative Development Agency provides information and advice about how to set up and manage a co-operative and offers a range of support services, such as training and a business registration service. The Agency also has close links with the network of local co-operative development agencies which also exist to promote and help co-operatives. In Scotland, information and advice is provided by the Scottish Co-operatives Development Committee. In Wales, the Wales Co-operative Centre provides a range of advice and free services on forming and running co-operatives.

Business and Technical Advisory Services

The Department of Trade and Industry operates its Business and Technical Advisory Services to help firms obtain expert advice on business problems and opportunities. Support is available in the form of two-thirds of the cost of consultancy for a minimum of eight and a maximum of fifteen days. All independent firms employing less than 500 people may apply. The main elements of the service are: advice and consultancy to improve productivity; advice and consultancy to help improve the quality of the businesses products and obtain quality assurance approval from recognised bodies; advice and consultancy on all aspects of product design; and advice and consultancy on marketing.

Grants up to 75% may also be available to small firms to help with the costs of feasibility studies by consultants, designed to exploit biotechnology, micro-electronics applications, advanced manufacturing technology (e.g. CAD / CAM, robotics, flexible manufacturing systems, computer-aided production management) for batch manufacturing. The upper limit of support is £2,500 per study, and all manufacturing firms may apply. In the case of studies involving the application of micro-electronics, firms in the service sector may also be eligible.

Regional Advice

A similar range of activities is offered by development agencies for small businesses situated in Scotland (through the Highlands and Islands Development Board (HIDB) and the Scottish Development Agency (SDA)), Wales (through Mid Wales Development (MWD) and the Welsh Development Agency (WDA)) and Northern Ireland (through the Local Economic Development Unit). Because these agencies are based in less prosperous areas of the United Kingdom, they are often able to offer cheap, extended loans or special grants to encourage the establishment and growth of small firms.

Exports

All United Kingdom companies, regardless of size, are eligible for export support. A wide range of assistance is available through the British Overseas Trade Board (BOTB). They can help with market advice, with special information about export opportunities and with practical and financial help in entering

new overseas markets. This includes support for exhibiting abroad, for overseas market research and for travelling to setting up sales facilities in markets abroad. Their Market Entry Guarantee Scheme can provide 50% of the cost of setting up sales facilities overseas. This is repayable by a levy on sales; if there are no sales, no repayment is required.

The Export Credits Guarantee Department (ECGD), based in nine regional offices, insures exporters against the risk of not being paid for their export sales. Certain conditions must be complied with and a fee is charged for the service. In addition, ECGD may be able to give a guarantee to exporters' banks under which finance can be obtained for export business, often at favourable rates of interest.

Employing People

Many small firms which could successfully expand are prevented from doing so because the owner of the business is worried about the problems associated with taking on employees. The Advisory, Conciliation and Arbitration Service (ACAS) offers a wealth of free advice on many of the aspects of employing people, such as: planning employment needs, hiring employees, contracts of employment, rules and procedures, controlling labour costs; communication with employees, consultation procedures and employee representation. On the occasions where things do go wrong, ACAS can help with impartial advice and conciliation services to those involved in Industrial Tribunal cases. ACAS can also provide conciliation and arbitration in trade disputes.

7. TRAINING FOR SMALL FIRMS

Nearly 300 institutions now offer courses in new and small business management and this represents at least a doubling of provision over the past two years. These courses cover a range of topics and a variety of styles of delivery. They are offered by educational institutions, private sector consultancies and enterprise agencies. The vast majority of these courses are funded by the Department of Employment (Training Commission), and most others are subsidised by local authorities or other organisations.

Department of Employment Courses

Description: Department of Employment courses usually offer not only free training but also subsistence allowance and sometimes a market research 'grant'. However, DE is moving towards a principle of only partial funding of courses for existing small firms and this has opened the door to non-subsidised course offerings by a number of organisations. DE started offering subsidised training to new and existing small firms only in 1977. Since then the volume of course places has mushroomed. Alongside this, recently the DE have begun to refocus their involvement towards existing small firms. The range of DE courses now offered is described in Table 23.

Table 23 Department of Employment Training Courses

Type of course	Programme	Year of commencement	1987 / 88 volume / cost (£ million)	Description
Business start-up	Firmstart (replaced New Enterprise Programme introduced in 1977)	1985	500 £2m	For businesses expected to employ over 12 people by end of second year. Twenty days free training over twenty-six weeks, free counselling, and market research grant (£500)
	Business Enterprise Programme (replaced Small Business Course (1980) and Self Employment Course (1981))	1987	86,000 £5m	Six free days training delivered in three modules over five weeks
	Business Enterprise Programme Seminar	1987		One day awareness seminar for self employment
Help to existing small firms involving secondment	Management Extension Programme	1982	2,000 £3.7m	Unemployed managers matched to small firms to develop growth projects. Managers receive three weeks free training and £38 per week allowance during the project. Seventy percent of managers subsequently find permanent employment
	Graduate Extension (or Gateway Programme)	1984	1,000 £2.6m	For graduates of higher education establishments. Based upon MEP, above
Existing small firms	Private Enterprise Programme	1987		Modular half day / one day courses on selected topics. Partly based upon written training material. Only part DE funded
	Growth Programme	1986	17,000 4.2m	Variety of extended part-time modular courses. No uniform model. Only part DE funded. Intended to be self-supporting in next few years
	The Small Business Programme	1989 launch		National distance learning programme developed by Cranfield / Open University under £800,000 contract with DE. Video, audio and workbook based. Modular. Self-supporting

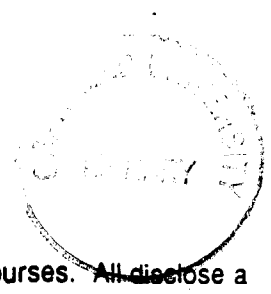
Department of Employment Courses

Scale: The volumes flowing through DE courses have increased dramatically since their inception in 1977. They are detailed in Table 24. The 1987 volume for start-up training represents approximately 28% of United Kingdom start ups. However, the volumes for existing small firms represent under 1% of the estimated stock of United Kingdom small firms.

Table 24 The Volume and Cost of Department of Employment Training Provision

Financial year	Start-up	Existing small	Total cost £ '000
1977 / 78	32	-	120
1978 / 79	64	-	250
1979 / 80	120	-	420
1980 / 81	330	-	850
1981 / 82	560	30	1,500
1982 / 83	1,377	123	2,910
1983 / 84	2,564	493	5,375
1984 / 85	6,444	1,426	9,017
1985 / 86	26,802	4,473	11,653
1986 / 87	53,917	13,121	17,966
1987 / 88	87,019	20,000	19,474

These increases in volume have been achieved by an ever-increasing investment in training - up to over £19 million in 1987/88. However, unit training costs have come down. This is partly because new courses tend to be modular and of shorter duration but also because older courses have seen cuts in their duration.



Department of Employment Courses

Evaluation: There are a large number of studies evaluating DE start-up training courses. All disclose a higher launch rate and employment generation rate for trained firms than is to be expected from national statistics (for example, Birley, 1985). In addition there are some cost / benefit analyses. One found that even if displacement effects were included a very pessimistic view regarding the appropriate discount rates was taken. The net present values were still sufficiently high, and by quite a significant margin, to conclude that start-up training was cost effective (Johnson and Thomas, 1983a). However, since most of the courses evaluated involve selection of participants it is almost impossible to conclude whether it is the course that is effective or the method of selection.

8. PREMISES FOR SMALL FIRMS

Most small businesses manage to find their own premises and the major sources of business accommodation are within the private sector. Local Authorities also help small businesses in a variety of industrial and commercial accommodation. In the Assisted Areas a wide range of industrial and commercial accommodation is available for rent or sale and premises can be built to specification, or altered to suit a small businesses needs. Some of the premises are less than 116 square metres (1,250 sq. ft.). Leases can be tailored to the needs of small businesses and rent-free periods are sometimes available (from agencies such as English Estates in England and in Scotland, Wales or Northern Ireland local Development Agencies).

In the twenty-five Enterprise Zones in the United Kingdom businesses in these zones are totally exempt from rates and almost free of planning controls. Businesses also get 100% tax relief on the cost of all new buildings. These benefits last for ten years from the date a zone became operational.

Also, all local authorities have been asked to cut planning delays and speed up decisions on applications for planning permissions for small firms. Planning permission is no longer required for businesses wishing to change from light industrial to warehouse use, or vice versa, except where hazardous substances are involved, for premises of 235 square. metres. (2,530 sq. ft.) or below. Moreover, planning applications are not normally needed for industrial or warehouse extensions of up to 25% of the original size of the building, subject to a maximum increase in floor area of 1,000 square metres (10,764 sq. ft.).

In the Assisted and rural areas of England and at other locations when requested by Government the English Industrial Estates Corporation takes strategic initiatives to help stimulate economic activity. With a continuous advance building programme in urban and rural areas, a wide range of properties is available on flexible lease or sale terms. English Estates can offer a full professional design and build service to cater for individual or specific property needs. Land for development is also available, some of which is within Enterprise Zones and Development Areas with many financial incentives. In urban areas English Estates provide a Business Support Service for small and medium sized businesses who are tenants or prospective tenants. Advice is freely given on all aspects of running a business including start-up, expansion, marketing, finance and grants. In rural areas a similar service is provided by the Rural Development Commission.

In Scotland the Highlands and Islands Development Board (HIDB) and the Scottish Development Agency (SDA), in Wales Mid Wales Development (MWD) and the Welsh Development Agency (WDA) and in Northern Ireland the Local Enterprise Development Unit all provide factory units ranging from 'nest units' to large factories. These factories may be rented, taken on a long lease or possibly purchased. Rental concessions may be available during the initial years of tenancy.

9. CONCLUSION

There has been a continued growth in the number of businesses registered in the United Kingdom, with the level of registration being higher than the level of deregistration resulting in a net increase in the stock of establishments. The majority of new additions are businesses trading in non-production activities predominantly in the South East of England. The reasons for this higher level of registration in the 'south' of England have been shown to be numerous but it does appear to be a result of a range of 'push' and 'pull' factors associated with various structural, social and locational variables.

In the United Kingdom there are a wide range of support mechanisms in order to assist the formation of small businesses as well as their development. The above mentioned support mechanisms have been introduced to overcome some of the problems and constraints associated with small enterprise development and survival. The plethora of measures detailed above cover issues such as finance, taxation, premises, information, training, employment, procurement, exports, education and legal and regulatory aspects of small firms assistance measures.

However, take-up rates are not uniform across a regional system in the United Kingdom and it is possible that additionality and displacement will also differ between regions. It is a consistent feature of the majority of schemes examined that the South East and East Anglia have more recipients and a greater share of the funds than is 'expected' on the basis of their proportion of eligible applicants in each scheme. In addition, three peripheral regions, namely Wales, Yorkshire and Humberside and Scotland, have fairly consistently displayed low take-up rates under the schemes examined here. Regional differences in entrepreneurial potential plus the associated differences in regional economic environments, notably the size and growth prospects of different regional markets, can help to explain this (Mason and Harrison, 1986). However, there are some other peripheral regions with take-up rates under particular schemes that are greater than 'expected' on the basis of their share of potential recipients, notably in the case of the Loan Guarantee Scheme, although there is no peripheral region that has consistently received more than its 'fair share' under each of the schemes examined. Indeed, some peripheral regions have experienced widely contrasting performances under different schemes.

The awareness amongst owner managers of government schemes of assistance, is generally low throughout the United Kingdom (Research Associates Ltd, 1984). However, it varies between regions. Often, specific schemes are vigorously promoted only in certain areas, either by Government agencies or

by interested private sector organisations such as the banks in the case of LGS, venture capital firms in the case of BES and machine tool suppliers in the case of SEFIS. For example, according to a survey of SEFIS recipients more owner-managers (29%) became aware of the scheme through machine tool suppliers than from any other source (Research Associates Ltd, 1984).

In some regions the use of certain schemes are also 'crowded out' by the activities of other organisations. For example, the more active involvement of Scottish banks in lending to small businesses than their English counterparts may have served to lessen the number of applicants under the LGS in Scotland (Hood, 1984). The under-representation of both Scotland and Wales in the LGS and BES may be related to the operation of the Scottish and Welsh Development Agencies which have made available alternative sources of loan and equity finance, often at very favourable rates. Similarly, the low take-up rate of the LGS in Northern Ireland is likely to reflect not only the administrative delay in introducing the scheme but also the alternative availability of finance through the region's small firms agency, the Local Enterprise Development Unit, which does not carry with it the cost penalty inherent in the LGS.

It could well be that the present support and assistance programme is only succeeding in extending the life of small firms which under free-market forces would fail. There is also the possibility that encouraging and allowing the 'success' of mediocre businesses might only succeed in crowding out, and possibly preventing the development of potentially successful business. The indiscriminate distribution of limited resources might at the end of the day only serve to undermine the vitality and reduce the overall quality of the small firm sector. Thus, just as the regional assistance programme which was rigorously applied during the 1960s and early 1970s has been shown to have in part undermined and further exacerbated the very problems which it was introduced to solve, the present small firms assistance programme and support mechanisms might have a similar effect on the small firm sector.

Appendix 1 Drawbacks of Using the VAT Database

Many firms are not registered for VAT, either because they have turnover below the threshold (currently £22,100) or because they trade only or mainly in exempt or zero-rated goods and services that are exempt from VAT. Although the number of such firms is not known, it is clearly large. Apart from the fact that many firms never enter the VAT system at all, a firm may well register some time after starting up depending, for example, on how long it takes for its turnover to build up to the threshold level. As detailed below, this threshold has been raised over the years. Although changes since 1981 have been set so as to balance the effect of inflationary increases in turnover, bringing some firms into scope. The database excludes group and divisional registrations and it is still possible for two or more VAT registrations to relate to the same 'enterprise group', where two firms are in fact under common ownership even though they are separately assessed for VAT (Table A).

Table A Changes in VAT Registration Threshold

From	To	Threshold (£)
April 1, 1973	September 30, 1977	5,000
October 1, 1977	April 11, 1978	7,500
April 12, 1978	March 26, 1980	10,000
March 27, 1980	March 10, 1981	13,500
March 11, 1981	March 9, 1982	15,000
March 10, 1982	March 15, 1983	17,000
March 16, 1983	March 13, 1984	18,000
March 14, 1984	March 19, 1985	18,700
March 20, 1985	March 18, 1986	19,500
March 19, 1986	March 16, 1987	20,500
March 17, 1987	March, 1988	21,300
	--------	22,100

A related but distinct, point is that a VAT registration or deregistration is not synonymous with the birth or death of a company. More importantly, there are a number of reasons why a firm may deregister without closing. One of four codes is assigned in the BSO database:

Trader goes out of business

Trader goes out of business, buyer already registered

Trader changes legal identity

Trader falls below exemption limit;

- is no longer taxable
- makes only zero-rated supplies and requests exemption; or
- accepts invitation to deregister.

Only the first code unequivocally relates to a closure and should be noted that closure is not necessarily synonymous with 'failure'. On the other hand, a firm may register for VAT in advance of starting to trade, and deregister after ceasing to trade. But these are thought to be less important factors.

Taken in combination, these factors suggest that the lifespan analyses obtained from VAT data will tend to lead to an understatement of the average lifespan of companies. There is a further difficulty in interpreting recent VAT data, in that registrations and deregistrations - particularly the latter - may take some time to be taken onto the database. Some deregistrations are not taken on until several years after they come into effect. For example, when a firm is found by the Customs and Excise to have ceased trading, and therefore removed from the register, the date associated with the deregistrations is the estimated date on which trading ceased, rather than the date on which the deregistration is processed. In consequence, the direct counts of the current number of VAT units, and of net growth for recent periods, are invariably overstated.

Appendix 2 Correlation Coefficients VAT Registration Rate (Y) and Selected Independent Variables (n= 11).

Independent variables	Pearson correlation coefficient (r)	Coefficient of of determination (r^2)	Significance of 'r' - t values
Percentage of total manufacturing employment in large establishments in heavy industries (SICs 5, 6 & 10), 1979	-0.51	0.26	
Percentage employment in manufacturing establishments with less than 11 employees, 1979	0.61	0.37	2.43 *
Percentage employment in manufacturing establishments with 500 or more employees, 1979	-0.34	0.12	
Percentage of persons being managers and professionals, 1979	0.67 *	0.45	2.85
Percentage of persons being manual workers, 1979	-0.63	0.40	2.57 *
Percentage of persons being self-employed, 1979	0.45	0.20	
Number of VAT deregistrations, 1980-1986 as a percentage of total employment stock, 1979	0.97	0.94	12.62 ***
Percentage school leavers going into employment without qualifications, 1979/80	-0.15	0.03	
Percentage of the workforce with a degree or equivalent, 1981	0.72	0.52	3.29 ***
Percentage of dwellings being owner-occupied, 1979	0.71	0.50	3.19 **
Percentage of dwellings rented from the local authority or new town, 1979	-0.83 ***	0.69	4.71
Average male weekly earnings, 1979	0.01	0.00	
Average weekly income per person, 1979-80	0.61	0.37	2.43 *
Personal disposable income per head, 1979	0.60	0.36	2.37 *
Average dwelling price, 1979	0.42	0.18	
Domestic rateable value, 1980	0.36	0.12	
Average domestic rates paid per hereditament, 1979/80	0.43	0.18	
GDP scaled per head, 1979	0.41	0.17	
Percentage rate of change in average male weekly earnings, 1979-1986	0.81 ***	0.66	4.37
Percentage rate of change in average disposable income per per head, 1979-1986	0.23	0.05	
Percentage rate of change in average dwelling price, 1979-1986	0.87	0.76	5.58 ***
Percentage rate of change in GDP per head, 1979-1984	0.75	0.56	3.59 **
Percentage total employment change, 1979-1986	0.51	0.26	
Percentage population change, 1981-1986	0.76	0.58	3.70 **
Percentage change in unemployment, 1979-1986	0.28	0.08	

Notes: * Significant at $p < 0.05$;
** Significant at $p < 0.01$;
*** Significant at $p < 0.001$.

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