HIGH GROWTH SMALL BUSINESS REPORT 2018

Rebalancing the economy: Unlocking the potential of the fastest growing smaller companies in the UK

Third Edition
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A brighter way

CONTENTS

Authorship and acknowledgements

This report has been produced by Cebr, an independent economics and business research consultancy established in 1992. The views expressed herein are those of the authors only and are based upon independent research by them.

The report does not necessarily reflect the views of Octopus Investments.

London, March 2018

EXECUTIVE SUMMARY

This is the third Octopus High Growth Small Business Report. The UK's high growth small businesses (HGSBs) have the power to drive the UK's economy, increase productivity, skills and employment. They make up less than 1% of UK companies, yet in 2016 they accounted for 3% of total UK jobs, creating an average of 3,000 new jobs every week.

Three out of five HGSBs are located outside London and the South East and are a vital part of the regional economy wherever they are found. Our findings highlight the need of HGSBs for skilled labour and high-quality infrastructure. No region of the UK can afford to be left behind, and in this report we have outlined the importance of HGSBs in helping to deliver the Government's aims and objectives, as set out in the Industrial Strategy.

KEY CONCLUSIONS OF THE REPORT:

- HGSBs make up only 1% of UK businesses, yet account for 3% of UK total jobs in 2016 (22,074 out of 5.6 million companies). HGSBs created an average of just over 3,030 new jobs every week – this represents about 20% of all jobs created.
- While making up only 3.6% of the UK's Gross Value Added (GVA), HGSBs have made a significant contribution to economic growth. Between 2015 and 2016, the UK's GVA grew by over £41 billion – 22% of this growth is estimated to have come from HGSBs.
- HGSBs can be found spread across all industrial sectors. The Professional, Scientific and Technical Activities sector accounted for 11% of HGSBs, supported almost 95,000 jobs (4% of the sector total) and contributed £7.4 billion to the overall sector's GVA in 2016 (6% of the sector total). Interestingly, fewer than one in ten HGSBs is in the technology sector.

Regional diversity

- Although London is the region with the largest concentration of HGSBs, nearly three in five HGSBs are located outside London and the South East, and more than 50% of HGSBs' GVA comes from other regions.
- We calculate that a 10% increase in the number of HGSBs in the North East would create more than 2,700 new jobs for the region.
- In Northern Ireland, the share of GVA growth from HGSBs reaches 51%. Yorkshire and The Humber, and the East of England also have impressive shares of GVA growth from HGSBs, 34% and 28% respectively.
- 74% of HGSBs surveyed feel more confident or have the same confidence level in the economic prospects over the next 12 months compared to last year.

Skills focus

- 60% of HGSBs surveyed consider finding talent/skills shortages to be an "important" or "very important" constraint on their business growth. Conversely, 8% of HGSBs consider it not to be at all important.
- 41% of HGSBs surveyed consider skills shortages to be the policy area where UK Government action could make the biggest difference for their businesses.
- 90% of HGSBs say that they face some form of skills shortages. This is even more remarkable when placed in the context of the UK average of just 17% of companies that say they have a skills gaps or skill shortages vacancies.
- 84% of HGSBs funded or arranged formal training for at least one member of staff over the past 12 months; this compares to the UK average of 66%.
- Across all regions, 61% of the HGSBs consider technical or practical knowledge related to the job to be a difficult skill to obtain when hiring staff.

Infrastructure

- One in three HGSBs considers digital infrastructure to be one of the biggest constraints on the growth of their business. 53% of HGSBs in London say poor transport links with other regions is a hindrance to their business and something that the Government could do more to alleviate.
- 69% of HGSBs consider the UK Government's Digital Communications infrastructure programme (as described in the Industrial Strategy Green Paper) to be "important" or "very important" to their business. Just 3% consider it not to be important at all.

22,074

Out of the 5.6 million companies that exist in the UK, only 22,074 of them are HGSBs. They can be found in every region of the UK.

20%

Between 2015 and 2016, HGSBs created 158,000 new jobs, representing 20% of employment growth in the UK.

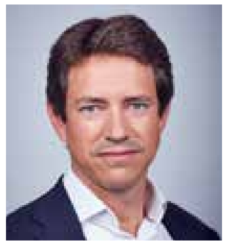
1 in 3

HGSBs considers digital infrastructure to be one of the biggest constraints on the growth of their business.

84%

of HGSBs funded or arranged formal training for at least one member of staff over the past 12 months.

FOREWORD



CHRIS HULATT, CO-FOUNDER OCTOPUS GROUP

High growth small businesses (HGSBs) are once again leading the way in employment, economic growth and productivity across all regions of the UK. Despite making up less than 1% of UK registered firms, they account for 3% of jobs and have been creating about 3,000 new jobs every week. In this, the third HGSB Report from Octopus, we show the enormous impact that these growing companies are having on the UK economy.

The Government's Industrial Strategy has highlighted the importance to UK plc of support for fast-growing businesses and its ambition to become one of the best places in the world not just to start, but also to scale a successful company. We are proud that our previous reports have got people championing HGSBs at both local and national level, and once again we are encouraging MPs to get out there and engage with the HGSBs in their own constituencies.

HGSBs may form only a numerically small segment of the new and small business sector, but they are disproportionately important. It is from among their ranks that the future market leaders will emerge, capable of competing globally and significantly adding to the country's future economic prosperity. Such firms need investment and support to help them grow and scale up over the longer term.

Our survey of some of the UK's most entrepreneurial companies has a particular focus on skills this year, with 90% of those we spoke to saying they face some form of skills shortage. HGSBs are also leading the way in tackling this, with 84% of them having funded or arranged formal training for staff over the past 12 months, against a national average of 66%. This year's report looks at some of the options open to the Government and other policy makers for tackling what is a growing issue for HGSBs, as Britain looks to a future outside the European Union.

Octopus is one of the most active investors in HGSBs in the UK and so we know the economic and social difference that these businesses make, wherever they are found. We are proud to once again highlight some of their great work in this report and call on everyone to get behind the high growth small businesses who are bringing jobs and prosperity to all parts of the country.

1

HIDDEN POTENTIAL: A SNAPSHOT OF HGSBs IN THE UK

We define high growth small businesses (HGSBs) as those with more than 20% annual average growth over a three-year period, and an annual turnover of between £1 million and £20 million.

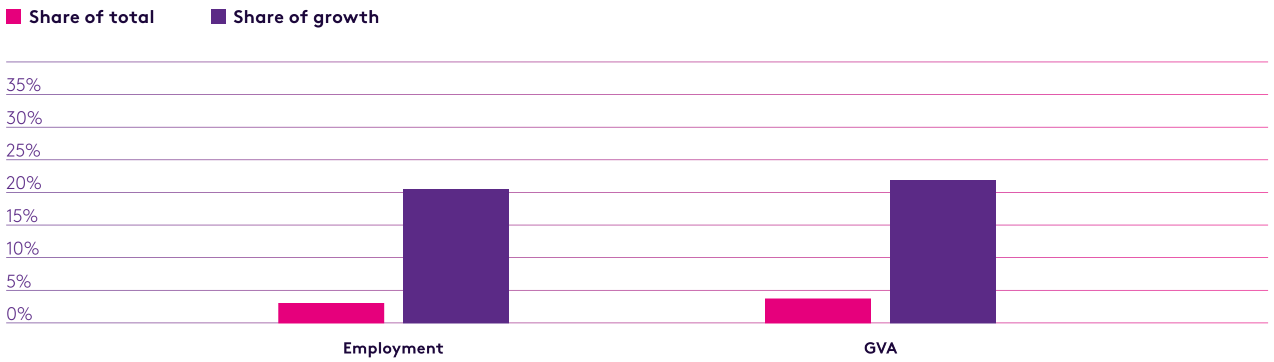
THEY ARE A SMALL GROUP...

As well as being small in size, HGSBs are few in number, representing a tiny proportion of all UK businesses. Out of 5.6 million companies in the UK, there were only 22,074 HGSBs in 2016, representing less than 1% of the business population.

...BUT THEY PUNCH WELL ABOVE THEIR WEIGHT

HGSBs make a disproportionately large contribution to our economic wellbeing, creating jobs and driving growth at an exceptional rate, as shown in Figure 1 below.

Figure 1: HGSBs' share of total UK employment and employment growth, and HGSBs' share of total GVA and GVA growth, 2016



Source: FAME, ONS, Cebr analysis

EMPLOYMENT

One in every five new jobs was created last year by an HGSB. Between 2015 and 2016, HGSBs created 158,000 new jobs, representing 20% of employment growth in that period. This amounts to just over 3,030 new jobs every week.

ECONOMIC GROWTH

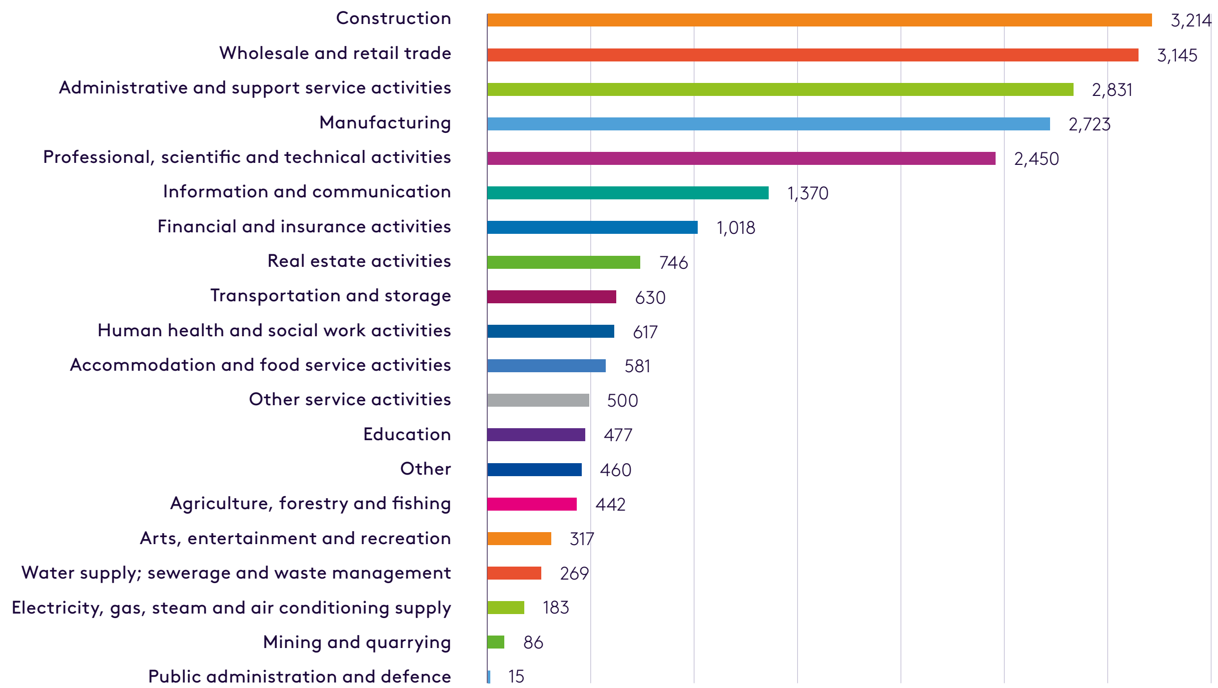
Despite making up only 3.6% of UK's GVA, HGSBs made a disproportionate contribution to economic growth. From 2015 to 2016, UK's GVA grew by over £41 billion – 22% of this growth is estimated to have come from HGSBs.

Gross value added (GVA) measures the contribution to the economy of each individual producer, industry or sector in the UK. It is used in national income accounts to measure productivity, or the value of goods and services produced by different sectors of the economy. It is calculated as the total value of goods and services produced, less the cost of all materials and other inputs used directly for that production.

HGSBS ARE GROWING IN EVERY BUSINESS SECTOR...

About 67% of HGSBs operate in the service sector. The largest single sector is Construction, with 15% of UK HGSBs, followed closely by Wholesale and Retail trade, which accounts for 14% of all UK HGSBs. Contrary to common perceptions, fewer than one in ten HGSBs is in the Technology sector.

Figure 2: Number of HGSBs in the UK by sector, 2016



Source: FAME, ONS, Cebr analysis

...AND BRINGING NEW BUSINESS TO EVERY REGION...

Significantly, HGSBs are found in every part of the UK. In the subsequent sections we explore this regional pattern.

...BUT THEY STILL STRUGGLE TO BE SEEN AND HEARD

The HGSBs segment comprises businesses spread across a broad range of industries, which do not make for a cohesive group. This, and their small size, help explain why they are easy for policymakers to miss within the wider SME (Small and Medium-sized Enterprise) population.

2

OPPORTUNITY EVERYWHERE: HGSBS AS GROWTH DRIVERS

HGSBs thrive wherever opportunity lies; every region of the UK has a high growth success story to shout about. While this is encouraging, there is a great deal more to be done if the UK is to unlock the full growth benefits HGSBs offer.

In the UK, we currently have businesses, people and places whose level of productivity is below what can be achieved, and it is this regional disparity which accounts for much of the UK's inequality. The latest ONS figures show that the US and France are nearly 30% cent more productive than the UK, while Germany outstrips the UK by 35%. HGSBs are more productive than other companies and can play a key role in seeing the UK address its lagging productivity levels.

HGSBS ARE MORE PRODUCTIVE THAN THE UK AVERAGE BUSINESS...

Britain's productivity problem is largely the result of the "long tail" of productivity, which was specifically highlighted as a key concern in the Government's recent Industrial Strategy. While the UK has some of the most productive businesses, people and places in the world it also has a "long tail" of underperformance. If the "long tail" of lower productivity is not dealt with, it will hold back UK growth, wages and living standards.

The Government can help to tackle this by promoting HGSBs in all regions. In 2016, excluding businesses operating in the financial and insurance sector[1],HGSBs' productivity (measured as GVA divided by the number of employees) was just under £65,000. This figure is significantly above the national average of just under £55,000. Our survey finds that in some sectors, such as retail, HGSBs have three times the average levels of productivity at £118,300 compared to all UK businesses.

...AND DRIVE PRODUCTIVITY IN EVERY REGION

The CBI's 2016 Unlocking Regional Growth Report observed that since the global financial crisis, only in London and the South East is GDP per head above its pre-crisis peak. As a result, the most productive area of the UK is now almost three times more productive than the least.[2] If each local area could improve at the same rate as the top-performing HGSBs in their respective region, the increased productivity would lead to more jobs, more exports and higher standards of living across the UK. HGSBs should, therefore, be an important consideration in all future local industrial strategies and City deals.

> "This report reinforces that scaling businesses are across all areas and sectors of the UK. They add value and generate jobs across local economies, as well as being highly productive enterprises. Increasing their numbers, and building up local capabilities to support them, is critical for improving UK productivity and national economic growth. This report provides further insights into their key needs across talent, infrastructure and finance. We hope that the recent announcements on the UK's Industrial Strategy, alongside the expanded role of the British Business Bank in relation to Patient Capital, lead to these issues being positively addressed by the public and private sectors working closely together."

Irene Graham
CEO of the ScaleUp Institute

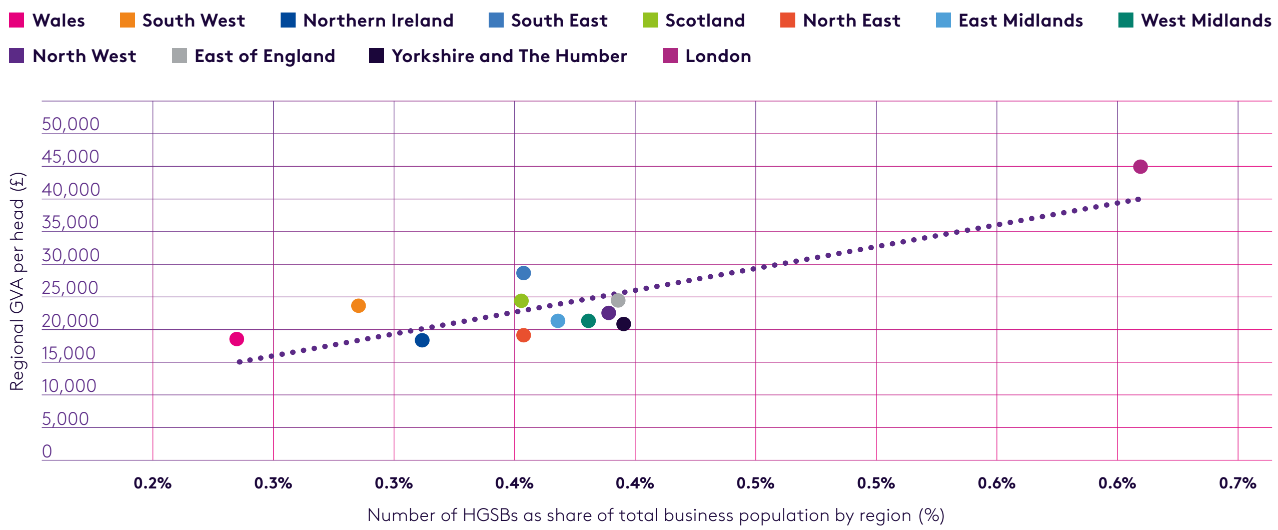
1. It is difficult to measure GVA for businesses in the financial and insurance sector, and typically requires the use of proxy measures. For the purposes of this productivity comparison, businesses operating in this sector have therefore been excluded. 2. CBI, 2016 Unlocking Regional Growth.

Figure 3: HGSBs' and total economy productivity by region (GVA per employee)

Source: FAME, ONS, Cebr analysis

Figure 4 below highlights the number of HGSBs as a share of all businesses in each region, plotted against the level of regional GVA in 2016. This supports the theory that there is a higher likelihood of finding HGSBs in areas performing more strongly economically.[3] It also underlines that the places where HGSBs are less common are often the areas that depend most on them, and are likely to benefit more from their growth.

Figure 4: Correlation between HGSBs' location and regional economic performance



Source: FAME, ONS, Cebr analysis

3. It is important to note that while there is evidence of correlation, it cannot be concluded that HGSBs are a cause of stronger regional performance. However, this correlation identifies the potential of HGSBs to drive regional growth. 4. The total number of HGSBs does not add up to the sum of across regions, because a very small number of HGSBs have been removed since their region was not able to be identified through the data available.

2.1 HGSBS ARE FLOURISHING RIGHT ACROSS THE UK

HGSBs are to be found in every part of the UK, and significantly, almost three in every five HGSBs are outside London and the South East. Figure 5 below shows the number of HGSBs located in each UK region.

Figure 5: Number of HGSBs per region[4]

Source: FAME, ONS, Cebr analysis

BUT SOME REGIONS ARE LAGGING BEHIND

Although HGSBs are succeeding in every region, some parts of the UK have relatively few. Wales, Northern Ireland and the North East have the lowest number of HGSBs, with fewer than 1,000 in each region. All three of these regions fall within the bottom five least productive regions by average GVA.

HGSBS IN LONDON AND THE SOUTH EAST ADD THE MOST TO UK ECONOMIC OUTPUT

In 2016, HGSBs in London and the South East had a combined GVA of £27 billion, which equates to 44% of the overall GVA contributed by all HGSBs across the UK.

Figure 6: HGSBs' GVA per region, £ billion

Source: FAME, Cebr analysis

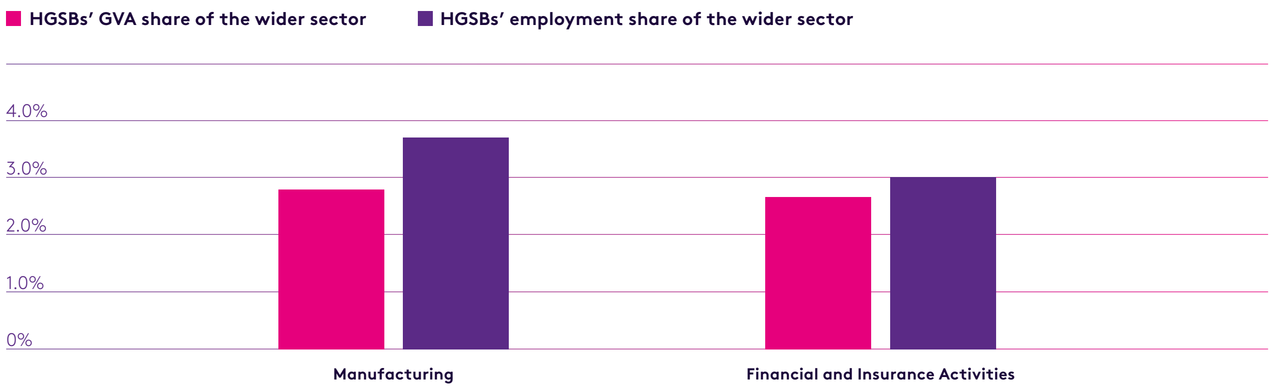
2.2 HGSBS CAN HELP BUILD THE UK'S INDUSTRIAL STRATEGY

The UK has a number of world-leading sectors that boast high productivity, competitive advantages at a global level, and have further growth potential. Sectors such as aerospace, automotive, the life sciences, the creative industries, digital, financial services as well as professional and business services have generated significant growth for the UK in recent years, and some of these have been earmarked for sector deals by the Government. HGSBs can help to accelerate their growth further and enlarge their geographical footprint.

HGSBS HAVE AN IMPORTANT IMPACT IN SECTORS SUCH AS MANUFACTURING AND FINANCIAL AND INSURANCE ACTIVITIES

In 2016, 12% of HGSBs were in the manufacturing sector and 5% in the financial and insurance sector. Combining the two, HGSBs contributed more than 124,000 jobs to the UK economy and are responsible for generating almost £8 billion in GVA.

Figure 7: HGSBs' contribution to GVA and employment in the Manufacturing and Financial sectors

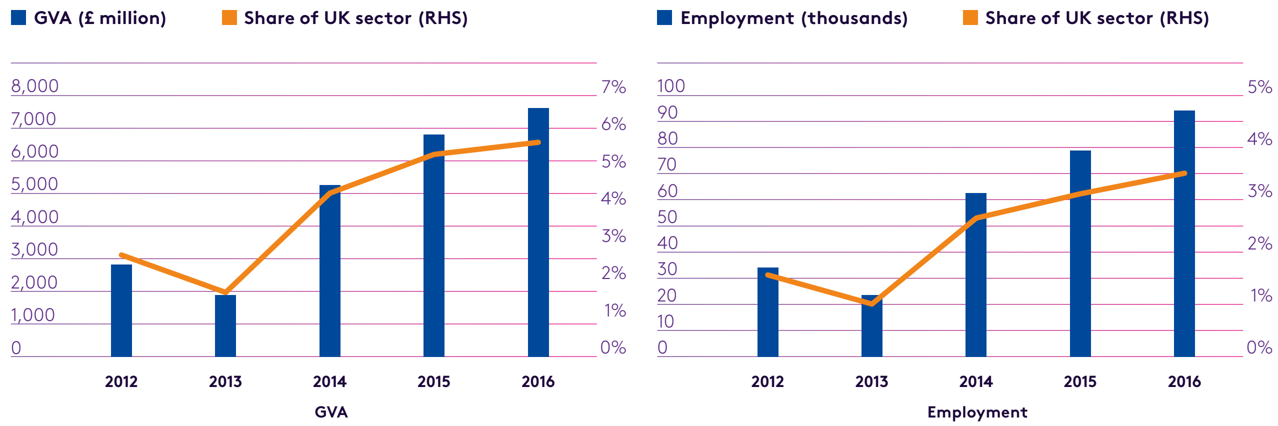


Source: FAME, ONS, Cebr analysis

HGSBS MAKE AN IMPORTANT CONTRIBUTION TO INNOVATION

Innovation is a key aspect of the professional, scientific and technical sector and 11% of HGSBs work within this area. HGSBs supported just under 95,000 jobs (3.5% of the sector total) and contributed £7.4 billion to the overall GVA of the sector in 2016 (5.8% of the sector total). HGSBs' GVA and employment figures in this sector also experienced considerable growth in recent years, as shown in Figure 8.

Figure 8: HGSBs' GVA and employment contribution to the UK Professional, Scientific and Technical Activities sector



Source: FAME, Cebr analysis

HGSBS ARE AN IMPORTANT DRIVER OF GROWTH ACROSS THE COUNTRY

HGSBs have the potential to play a far greater role in driving growth and increasing productivity in every corner of the UK. In Northern Ireland, the share of GVA net growth coming from HGSBs was 51%. Similarly, Yorkshire and The Humber, and the East of England also have very impressive shares of GVA net growth coming from HGSBs. The low share observed in Wales is somewhat driven by its corresponding low share of HGSBs in its business population.

The North East and North West of England both have a below-average share of HGSBs, yet their HGSBs still generated £7 billion in GVA in 2016 which equated to 11% of the total HGSBs contribution to the UK's GVA.

Figure 9: Share of GVA net growth coming from HGSBs by region

Source: FAME, ONS, Cebr analysis

For the UK to achieve higher levels of prosperity, and for the economy to work for everyone, all parts of the country must be firing on all cylinders. With the right investment and policy intervention, there is considerable potential for regions, cities and towns whose performance has been lagging, to close the gap on other areas. HGSBs are pivotal in accelerating this process.

3

THE HIGH GROWTH EFFECT: EMPLOYMENT AND SKILLS DEVELOPMENT

HGSBs create growth wherever they are found, but the impact is strongest in exactly the places that most need a boost. The Government recognises that more needs to be done to tackle regional inequality, and HGSBs offer a clear, strong and viable force for rebalancing the economy.

Research by the National Institute of Economic and Social Research in 2017[5] showed that productivity, measured by GVA per head, is 72% higher in London than the national average and is twice as high as in seven of the eleven other regions. In addition, skills shortfalls in some parts of the country contribute to imbalances in productivity in the UK, as shown in a recent CBI report[6] highlighting education and skills as the biggest determinants of regional variations in productivity. The Government's Industrial Strategy also highlighted how the UK's poor performance in basic and technical skills is key to its persistently lower levels of productivity, compared with other advanced economies.

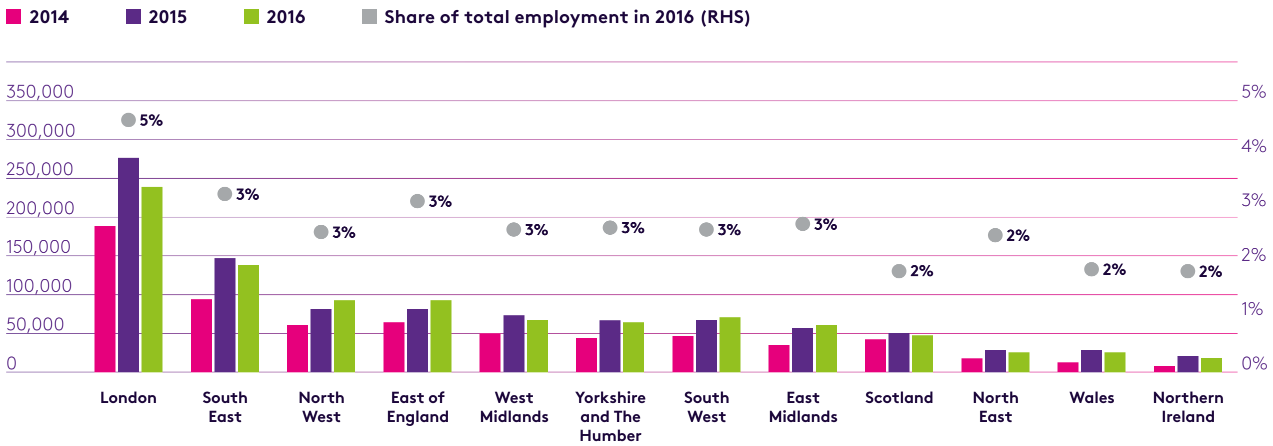
HGSBs have the power to drive employment growth and upskilling the UK's workforce, not just by creating jobs, but also by providing training to its employees. Our research shows that HGSBs have a disproportionate impact in weaker-performing areas of the UK outside London and the South East, and that HGSBs also invest more time and resources into training their workforce.

5. NIESR, (2017) 'Regional inequality in productivity in the UK: a closer look'. 6. CBI, (2016) 'Unlocking Regional Growth: Understanding the drivers of productivity across the UK's regions and nations'.

3.1 EMPLOYMENT

HGSBs make up only 1% of UK businesses, yet account for 3% of UK total jobs in 2016 and incredibly, one in every five new jobs was created last year by an HGSB. Between 2015 and 2016, HGSBs created 158,000 new jobs, representing 20% of employment growth in that period, amounting to just over 3,030 new jobs every week.

Figure 10: Number of people employed by HGSBs by region and share of total regional employment



Source: FAME, ONS, Cebr analysis

3.2 TRAINING

The Government's aim to drive productivity was central to the Industrial Strategy, and it identified 'people' or human capital as one of the five key pillars.

"We recognise that people, and the skills they have, are a key driver of productivity. Having the right skills increases people's earning power. Investing in our people across their lifetimes is fundamental to our shared success, from strong foundations for children and young people in schools and relevant, high-quality education and training in our further and higher education systems to career-long learning and enabling employers to invest in their workforce."[7]

While part of this is achieved via the formal routes of education, businesses raise skills levels by providing training to their employees, and HGSBs not only invest significantly above the national average in their workforce, they also face specific shortfalls.

Staffline Resourcing Plus
People Skills Jobs

The Staffline Group has two business divisions: Staffline Recruitment, market leaders in industrial temporary recruitment supplying up to 52,000 workers per day to more than 1,500 clients; and PeoplePlus, a leading provider of skills and apprenticeships which supports tens of thousands of people each year to transform their lives, get into work and progress their careers.

In the past five years, Staffline has seen significant and rapid growth, with an underlying operating profit compound annual growth rate of 29% and an increase in turnover of £591 million. Developing our people has been key to this success. Since becoming a listed company in 2004 we have continued to enjoy the support of Octopus Investments, our largest shareholder.

HGSBS ACROSS THE UK INVEST IN THEIR WORKFORCE

84% of HGSBs funded or arranged formal training for staff over the past 12 months, compared to a UK average of 66%.

Over the past 12 months, HGSBs spent, on average, £18,958 per business on training. 36% of HGSBs spent more than £10,000 on staff training/skills development over the past 12 months. This is well above the UK average investment in training, which is just under £8,000.

3.3 SKILLS SHORTAGES

SKILLS SHORTAGES ARE A UK-WIDE PROBLEM AND PRESENT IN EVERY REGION

It is widely recognised that the UK needs to tackle skills shortages, but our survey shows that an incredible 90% of HGSBs say that they face some form of skills shortages, and 61% of HGSBs consider it to be a policy area where there is a need for Government intervention. This is even more remarkable when placed in the context of the UK average of 17% of companies that consider they have skills gaps or vacancies due to skills shortages.

7. HM Government (2017). 'Industrial Strategy: Building a Britain fit for the future.' p.93.

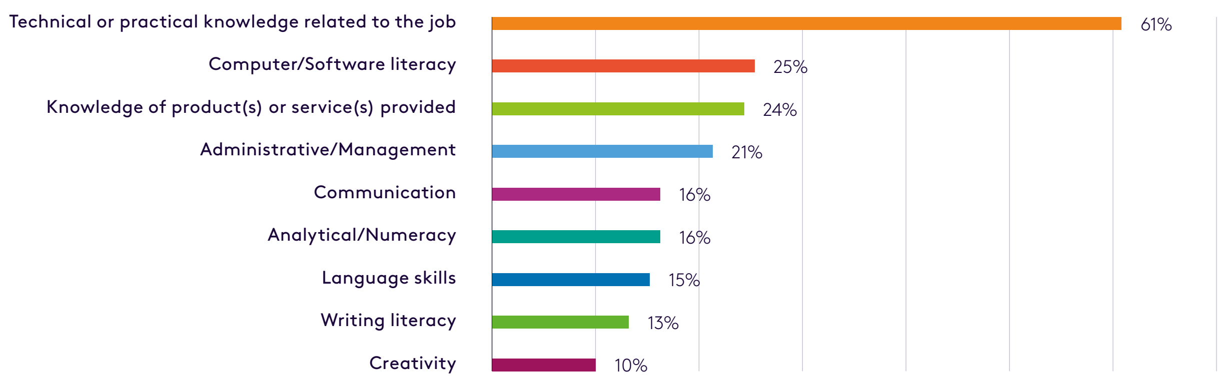
Figure 11: Share of HGSBs reporting any skills shortage(s) versus share of total companies in the region reporting any skills shortage(s) or vacancies

Source: ICM, UKCESS, Cebr analysis

KNOWLEDGE RELATED TO THE JOB IS A COMMON SKILL SHORTAGE

61% of HGSBs consider "Technical or practical knowledge related to the job" to be a difficult skill to obtain when hiring staff. This is universal across all regions in the UK, and also reaches non-HGSBs. The second most selected skill shortage is "Computer/Software literacy" (25% of HGSBs), with "Knowledge of product(s) or service(s)", coming in third, at 24%.

Figure 12: Share of HGSBs that find skill shortages to be common when hiring staff



Source: FAME, ONS, Cebr analysis

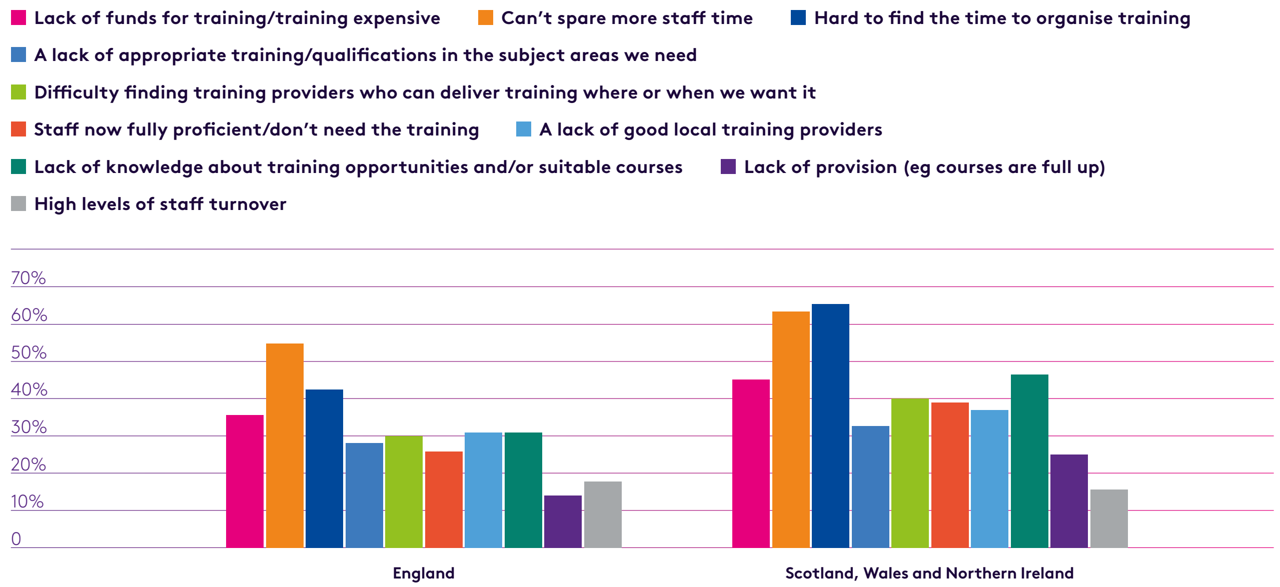
TIME AND FUNDING ARE THE MAIN BARRIERS TO PROVIDING MORE TRAINING

When asked about the barriers to providing more training, 55% of HGSBs state that they could not spare more time, 45% mention it was hard to find the time to organise training and 36% mentioned lack of funds for training or that training was expensive.

This reflects a general feeling across all companies and regions in the UK. According to the UK Commission for Employment and Skills (UKCESS)survey, these are the top three reasons constraining companies' provision of training.

An important difference, however, is that HGSBs in Scotland, Wales, and Northern Ireland seem to face relatively higher barriers to training than England.

Figure 13: HGSBs' barriers to provide more training by region



Source: ICM, Cebr analysis

GOVERNMENT ACTION IS NEEDED

The message is clear. While HGSBs are strongly contributing to the UK skills stock, they need more help to both attract those with the specific skills they need when recruiting, as well as train their existing workforce. 72% of HGSBs consider skills shortages to be a common challenge businesses face, and 39% of HGSBs consider developing a skilled workforce to be an area where the Government could provide more assistance.

4

UNLOCKING HGSBS' POTENTIAL: INFRASTRUCTURE

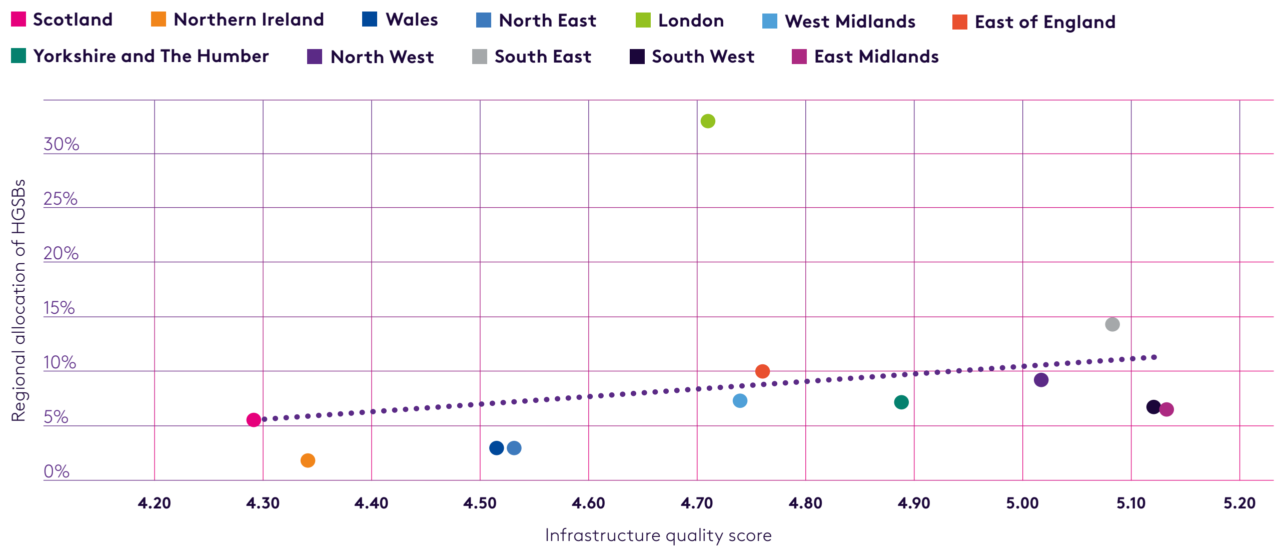
Wherever they spring up, high growth small businesses encourage energy and confidence in local economies. They bring new activity, commerce and employment; increase demand for services and infrastructure; set off new cycles of innovation and opportunity; and generate or attract other enterprises like them. However, infrastructure is an area where the UK fails to keep pace with its counterparts; with the areas of digital connectivity and transport concerning HGSBs the most, whichever region they are in.

4.1 INFRASTRUCTURE POLICY IN THE UK

The Government's Industrial Strategy acknowledges that investment in the UK's infrastructure is crucial in growing regional economies and creating the right environment for businesses to thrive. In pledging to increase the National Productivity Investment Fund to £31 billion and investing over £1 billion in digital infrastructure – to include the roll-out of full-fibre networks and 5G – the Government knows it has a critical role to play in supporting businesses to grow and prosper. Over the next five years, the Government plans to spend over £239 billion in infrastructure projects across the UK.

The quality of infrastructure – whether it be transport, communications, energy or water – varies by region, in the same way the number of HGSBs varies according to geographical location. Our research shows that HGSBs are concentrated in regions with the best infrastructure, and the regional growth of HGSBs can be fuelled by providing better infrastructure. The results of our survey of HGSBs suggests there is evidence to back these theories, with positive correlation between the regional infrastructure quality and the regional breakdown of HGSBs. If we exclude London, the positive correlation is even stronger.[8]

Figure 14: Correlation between HGSBs' location and regional economic performance



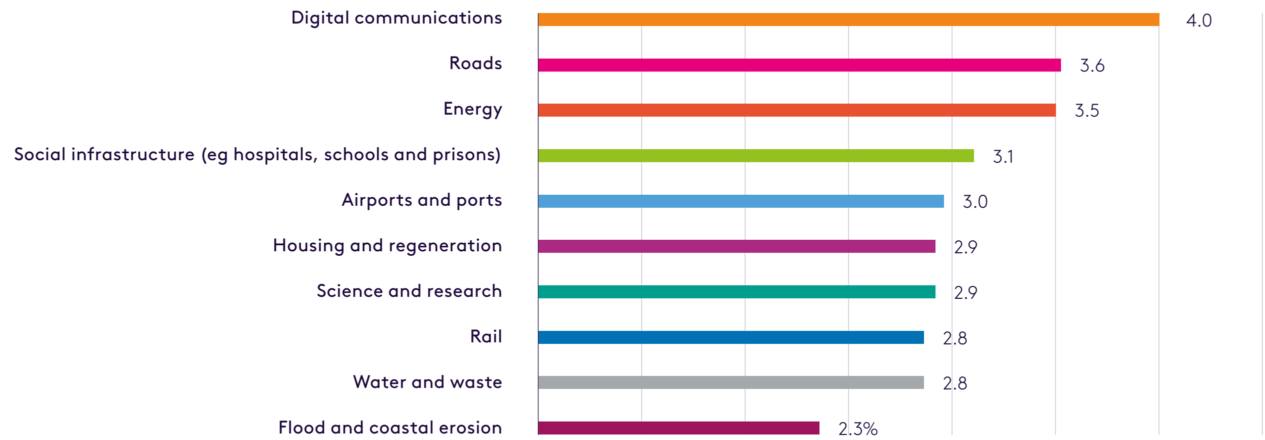
Source: FAME, Cebr analysis

HGSBS HAVE A CLEAR NEED FOR BETTER INFRASTRUCTURE AND RANK DIGITAL COMMUNICATIONS HIGHLY

Our survey asked businesses to rank which infrastructure programmes they would like to see more investment in. On average, HGSBs ranked digital communications as the most important Government infrastructure programme in relation to their business (4.0), followed by roads (3.6).

8. A likely reason for this outcome is that while most HGSBs are concentrated in London, the majority are located in Central London. The "London" region presented here includes local authority districts outside Central London with a lower infrastructure quality.

Figure 17: HGSBs' average rank of Government infrastructure programmes' importance to their business (where 1 is "Not important at all" to 5 is "Very important")



Source: FAME, ONS, Cebr analysis

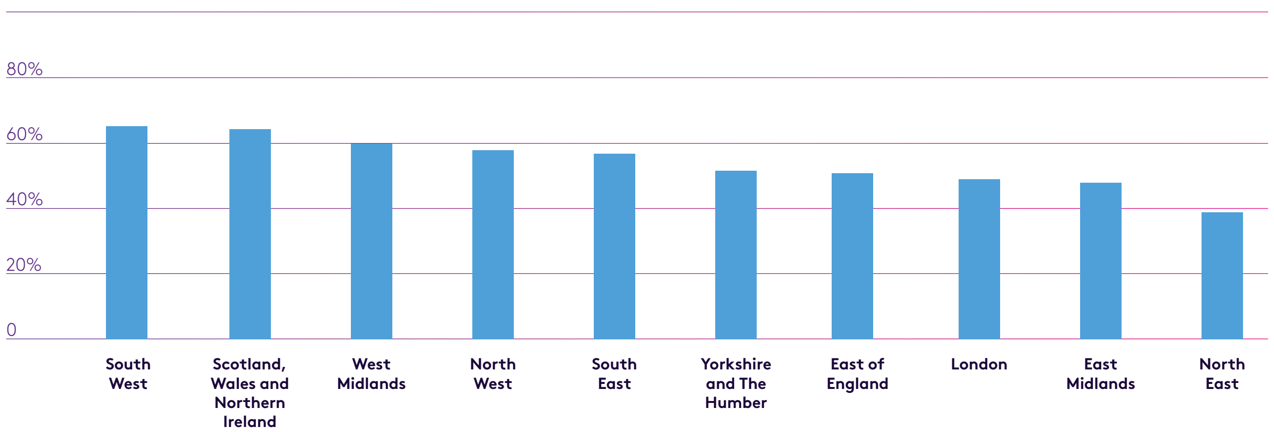
Poor digital and transport infrastructure – from slow broadband speeds to bottlenecks on key arterial roads – inhibits innovation, economic and social growth. Improving these can raise productivity by enabling towns and cities to achieve agglomeration effects, and thus support the rebalancing of the UK's economy.

4.2 HGSBS AND REGIONAL DEMAND FOR INFRASTRUCTURE

THE NORTH-SOUTH DIVIDE IS NOT AS EVIDENT IN TERMS OF HGSBS' DEMAND FOR DIGITAL INFRASTRUCTURE IMPROVEMENT...

The South West has the highest share of HGSBs that consider the quality of digital infrastructure as a "very important" or "important" constraint on growing their business, with the North East having the lowest share.

Figure 18: Share of HGSBs that consider digital infrastructure a "very important" or "important" constraint on the growth of their business



Source: ICM, Cebr analysis

The Government published its Digital Strategy in March 2017 consisting of seven strands, the first being "building world-class digital infrastructure for the UK".[9] Significantly, the Strategy signposted independent research that identified that increased broadband speeds alone could add £17 billion to UK output by 2024.

In the Autumn Budget 2017, DDCMS announced that as part of the Government's £740 million National Productivity Investment Fund (NPIF), a Local Full Fibre Networks (LFFN) Challenge Fund of £190 million would be available with the aim of helping "locally led projects across the UK leverage local and commercial investment in full fibre".[10]

A component of the LFFN programme is the Gigabit Voucher Scheme, which will provide vouchers worth up to £3,000 "to support the capital costs of getting new gigabit-capable connections for businesses". The scheme is currently being tested in four areas of the UK: Aberdeen and Aberdeenshire; Bristol, with Bath and North East Somerset; Coventry and Warwickshire (North Warwickshire, Nuneaton and Bedworth, Rugby, Stratford-on-Avon, Warwick); and West Yorkshire and York (Bradford, Calderdale, Kirklees, Leeds, Wakefield and York).

When comparing the areas identified by the Government with the areas in Figure 18, we can see that more often than not, the Government's support appears well targeted; at 65% of HGSBs in the South West, the region where HGSBs most needed digital infrastructure, which corresponds with the Government's own decision to trial the scheme in Bristol and Bath. Similarly, the West Midlands (or Coventry and Warwickshire in the Government's assessment) was the region with the third highest proportion of HGSBs which felt that digital infrastructure was important. However, Yorkshire and The Humber featured sixth (out of ten) on ranking the importance of digital infrastructure to HGSBs, with the North West and South East six and five percentage points higher respectively.

...BUT IT IS CLEAR IN TERMS OF HGSBS' DEMAND FOR BETTER TRANSPORT INFRASTRUCTURE

On average, in London only about one in three HGSBs considers transport infrastructure to be a "very important" or "important" constraint on their growth. In the North West, almost two in three HGSBs consider this to be the case.

Figure 19: Share of HGSBs that consider transport infrastructure a "very important" or "important" constraint on the growth of their business

Source: ICM, Cebr analysis

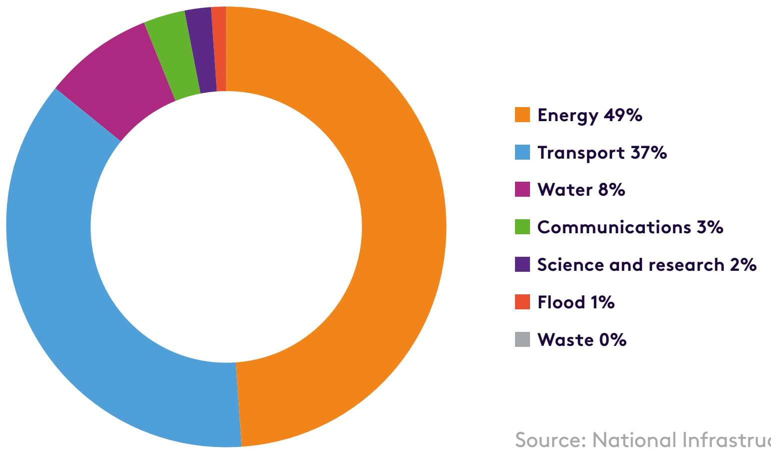
9. https://www.gov.uk/government/publications/uk-digital-strategy. 10. https://www.gov.uk/guidance/broadband-delivery-uk#contents

Overall, 55% of HGSBs surveyed consider poor transport links with other parts of the UK to be a common challenge facing businesses, with 43% saying the same about within-city transport links. With this view widespread across all regions of the UK, there is clearly work for the Government to do in order to address these issues, and a number of HGSBs would agree, with 42% of HGSBs considering infrastructure to be a policy area where there is still room for Government intervention.

4.3 THE NATIONAL INFRASTRUCTURE PIPELINE AND HGSBS

The National Infrastructure and Construction Pipeline (NICP) is a comprehensive forward-looking assessment of the planned investment in UK economic infrastructure across both the public and private sectors. Over the next four years, the UK Government plans to spend over £240 billion in infrastructure projects across the UK. The highest share will be allocated to the Energy sector (49%), followed by the Transport sector (37%).

Figure 20: NIP funding allocation across projects

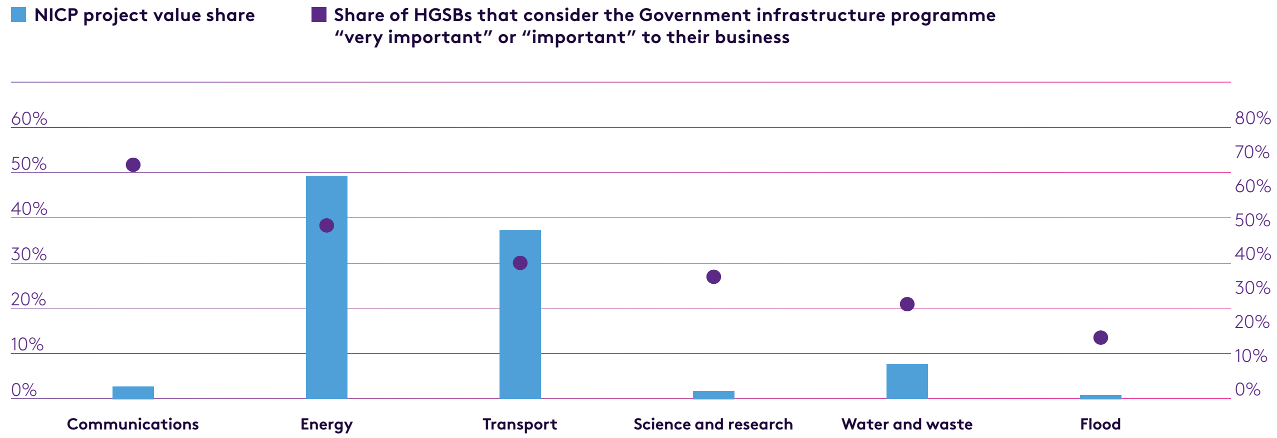


Source: National Infrastructure and Construction Pipeline, Cebr analysis

HGSBS HAVE DIFFERENT PRIORITIES FROM THE PLANNED NATIONAL INFRASTRUCTURE AND CONSTRUCTION PIPELINE

In our survey of HGSBs, business leaders backed the spending on transport and energy, but there was a clear divergence on the communications sector. 69% of HGSBs consider current communications infrastructure to be an important constraint on the growth of their business. However, it is important to recognise that while only 3% of total Government funds in the NICP is allocated to this sector, investment in digital infrastructure has shifted away from the public purse. Therefore the bare figures do not reflect overall investment, or the crucial role Government has in creating the right policy framework to encourage the further private investment needed to meet HGSBs' needs.

Figure 21: NICP funding allocation across sectors, and share of HGSBs that consider the given Government infrastructure programme "very important" or "important" to their business



Source: National Infrastructure and Construction Pipeline, ICM, Cebr analysis

NICP FUNDING DISCREPANCIES REMAIN AT A REGIONAL LEVEL

HGSBs are also concerned that London (11%) and the South East (4%) continue to get the majority of non-national infrastructure spend.

Figure 22: Allocation of NICP funding across regions over the next five years

Source: ICM, Cebr analysis

While these figures undoubtedly reflect London's role as the UK's financial and business hub, and the capital's numerous ongoing transport infrastructure projects, they will do nothing to assuage concerns about the "London-centric" nature of policymaking and funding decisions.

5

SUPPORTING BUSINESSES TO START AND GROW

The UK has one of the world's most successful markets for entrepreneurial small companies, with the UK ranked third in the world as the best place to start up a business according to the Organisation for Economic Co-operation and Development (OECD). However, as the Government's Industrial Strategy recognised, the UK is only in 13th position for scale-ups. Octopus was founded in 2000, and in the last 18 years has scaled up to become the largest venture capital investor in the UK, with £890 million of funds under management, representing a fifth of the UK market.

> "The Octopus High Growth Small Business report has established itself as one of the most important publications for entrepreneurship policy. Once again the report makes a strong case for supporting this dynamic and geographically dispersed collection of companies. Politicians and policymakers across the political spectrum should sit up and take note."
>
> Philip Salter, founder of The Entrepreneurs Network

THE OCTOPUS STORY

Scale-up funding provides the visibility that allows entrepreneurs to focus 100% on growing revenue, productivity and jobs, as opposed to focusing on survival and the next round of fundraising. We are proud of our track record in helping many successful start-ups navigate the scale-up process, some of which have become household names, such as Zoopla and Secret Escapes. Unconstrained by short time horizons and holding periods, we can support companies for the long term, helping them to grow. Thirty-three of our 39 AIM listed companies that we have invested in have been part of our portfolios for more than five years, 16 for more than ten years.

Secret Escapes is an online travel club and among the fastest growing holiday businesses in Europe. Members are offered options to purchase luxury holidays at significant discounts for a limited period, and these deals are guaranteed to be better than can be found elsewhere.

Octopus first invested in Secret Escapes in 2011, when the company had five members of staff. Since then, Secret Escapes has expanded internationally to countries across Europe, the US and the Far East, and now employs over 480 people. Yet it wasn't just financial backing that Octopus provided, and Secret Escapes was able to draw upon the network and expertise of the fund management team at Octopus, so that it could meet the challenges of growing and succeeding in a very competitive market.

> *What Octopus are doing with their support in helping us in Asia is actually operationally helping people explore possibilities and take first steps in probably the toughest market in the world. They are organising the meetings, sorting visa letters, doing the market research to find relevant targets – it's several steps on from anything we've seen on this front before. I can't stress enough that I think the difference is that there's a strong element of real work here, actual execution, not just firing off a couple of intro emails. You not only have people with all the contacts but those who will also roll their sleeves up and actually make things happen.*
>
> Alex Saint
> CEO and co-founder of Secret Escapes

Venture capital investors such as Octopus can provide management expertise, invest in tools, networks and resources to help companies scale and compete globally in new markets and geographies, providing a range of support in areas such as IT, operations, management and financial guidance.

£890 million

Largest venture capital investor in the UK, with £890 million of funds under management, representing 21% of the market

45%

overall growth in Octopus Ventures portfolio revenues

Supported over

450

smaller businesses

Octopus Ventures has

26

companies active in the US

£100 million

Octopus Ventures invested £100 million in the last year in 8 companies

£7.2 billion

funds under management

Invested in start-ups such as

Zoopla, Secret Escapes and Graze

before they became famous

Fluidly

Fluidly is a financial technology company that combines machine learning and AI with financial modelling, which transforms the way businesses manage their cash flows.

Octopus provided an initial round of seed funding, allowing the company to grow to 16 staff and kick-start its commercial activity. Along with funding, Octopus' expert team provided invaluable practical and strategic advice, as well as unique access to key industry stakeholders, including a trip to Silicon Valley to meet leading American tech entrepreneurs. With a rapidly expanding customer base, Fluidly is confident it can capitalise on its initial success, and has ambitious plans for major growth over the next few years.

As highlighted by the OECD figures, the challenge for UK entrepreneurs is in accessing the long-term finance required to scale up. This can be a particular problem for companies that outgrow the caps on VCT and EIS financing, as their companies grow to over £15 million or have already received £12 million in VCT/EIS money over their lifetime.

At this point, the companies are forced to bring in external funders, typically from the US, or even sell out their whole company to a big US corporate buyer which integrates the intellectual property into its core business. In the worst cases, we have seen businesses who have had to slow down their growth trajectory, reducing hiring and even laying off staff until they can secure further capital.

With many innovative, highly productive companies, it can often be a race to scale up quicker than the competition or become obsolete. The competition is often based in other countries with deeper pools of scale-up capital, putting our world-leading ideas and scientists at a competitive disadvantage.

If the UK were to make available deep pools of capital to support UK firms scaling up, our world-beating universities and entrepreneurs would be able to compete more effectively on the global stage. It would ensure that the FTSE 100 will still host world-leading companies in another 20 years when oil, traditional banking and telecoms will no longer be as relevant to the world we live in.

SUPPORTING THE AIM MARKET

So much more could be achieved with the right conditions. The Alternative Investment Market (AIM) has provided over £100 billion in growth capital to over 3,700 firms since it was established – more than any other stock market in the world – and is firmly recognised as one of the most attractive markets for a company to seek capital support once it reaches a sufficient scale.

HELPING COMPANIES TO EXPORT

We want to share what we learnt as a business. The Octopus Ventures team recently invested in an office in New York for the sole purpose of helping UK portfolio companies enter the US market, and navigate its complexities, as smoothly as possible. Arranging trips to Silicon Valley for UK entrepreneurs has shown them that there should be no limitations on their ambitions for their businesses.

In the US we are focused on helping the entrepreneurs we have backed in Europe to scope, enter and then scale in this market. This often involves both basic operational activities (incorporating a US company, discovering the optimal location to have a base) as well as more strategic decisions (determining who first to hire, which go-to-market strategies to leverage, when and how to fundraise). About 40% of our portfolio has a presence or operational reach in the US.

semafone
securing data · protecting reputations

Semafone provides secure voice transactions for call centres, allowing consumers to enter their payment card details and other personally identifiable information (PII) securely via their telephone keypad, while still engaged in a conversation with the call centre agent. Headquartered in the UK with US offices in Boston, Semafone works with more than 80 organisations in 14 countries on five continents.

Semafone wanted to establish a second support team location away from the UK, and reached out to Octopus' US team to help assess North America's viability, as part of a global review of possible support locations, which also included Asia and Australia.

Semafone chose Australia for its new support team location with greater confidence and expediency, as Octopus' support allowed the company to understand additional risks and challenges in the US before they were material, including talent leaching in certain parts of the country, cost inflation in target regions and recruiting costs, among others. Now, Semafone can deliver unparalleled customer support, 24x7, around the world and is well positioned for its continued global growth.

> *In our search for a new support team location, Octopus provided us with helpful information, answered our most difficult questions, and introduced us to a community of insightful connections to address our challenges. One CEO even offered us additional help setting up and renting office space. Semafone values the Octopus team's time and assistance – it was truly enjoyable to work with them on this project. Every communication was full of positivity, encouragement and cheerfulness, which is much appreciated.*

Christine Redmond
Customer Support & Services Manager, Semafone

Our US team invest significant time and effort understanding how the very best companies expand internationally. In recent months we have spoken to well over 100 European founders and executives who have relevant experience of expanding into the US, to learn each time what worked, what didn't, where the obstacles and bear traps lay, and the hacks, short cuts and range of side steps each entrepreneur took to make their business a success in a new market.

We're not closed or proprietorial about this knowledge either – we believe that we can all help each other and this is far from being a zero sum game – so we have established a European founders group to encourage collaboration between European executives in the US and regularly write about what we have learned and see as best practice.

In the US, we partner with other venture investors, advisers and groups with a mission similar to ours in the US to help entrepreneurs have access to world-class resources. Those range from exclusive conversations with industry leaders and corporates, advice from successful executives and expert service providers, events bringing entrepreneurs together and introductions to appropriate partners.

As this report demonstrates, HGSBs are fundamental to current economic growth, delivering 22% of GVA growth between 2015 and 2016. HGSBs deliver growth and jobs in all regions of the UK, but more can and must be done to ensure that these growing businesses receive the support and finance that they need to continue their journey to become great scale-ups. The businesses highlighted in this report, as well as the thousands of HGSBs all over the country, are thriving already, and with the right support and infrastructure they have the potential to bring employment and prosperity to every area of the UK. We're proud to back these companies and to give them a voice through this report, and ask that Government and other policymakers join with us to make this happen.

elvie

Elvie is a British femtech company, with a mission to build extraordinary products that improve the health and lives of women everywhere and at all stages of life. Its first product, Elvie Trainer, is an award-winning pelvic floor trainer backed by over 1,000 health professionals and stocked at major retailers such as John Lewis and Boots. Investment from Octopus has allowed it to take on ten more staff and develop a second product line for new mothers that is set to launch this year. Support from Octopus has also been vital to managing the firm's dizzying growth, as sales increased 100% year on year and it expanded to the US market, with the Elvie Trainer even included in the 2017 Oscars nominees' goody bag.

The combined backing from Octopus and AllBright (an organisation that supports and funds female entrepreneurs) was a huge mark of credibility for Elvie. Octopus is the leading consumer tech investor in the UK and we're proud to partner with such an experienced investor with strong expertise in taking British brands to the US.

Octopus has brought so much more than just capital to our business. Simon King and the team have become our trusted advisors, helping us with the team, strategic and operational decisions and avoiding common pitfalls of scaling up.

Andrea Zitna
CRO, Elvie

6
POLICY RECOMMENDATIONS

High growth small businesses (HGSBs) are pivotal to the Government's Industrial Strategy in addressing the long-term challenges facing the UK economy and achieving its aims of building on existing strengths and ensuring that every region meets its potential. The Government has committed to closing the gap between the most productive places, companies and industry and the least, and to making the UK one of the most competitive places in the world to start or to grow a business.

To encourage balanced growth around the country, the full potential of HGSBs needs to be unlocked. Against the backdrop of the UK's withdrawal from the European Union, it is important now more than ever for SMEs, the backbone of the UK economy, to flourish. We welcome the Government's enthusiasm and effort in supporting the UK's innovators and entrepreneurs as they contribute to our growing economy.

We call on the Government to ensure that the whole of the UK fully benefits from the economic growth and productivity of HGSBs, as it is crucial that no region is left behind.

1 ACCESS TO CAPITAL AND SUPPORT IS CRUCIAL IN ORDER FOR HGSBS TO SCALE UP

Although our funding environment for start-ups is among the best in the world, these growing businesses find it difficult to access the finance they need for the longer-term process of scaling up. This finance gap hinders the development of HGSBs and needs to be closed if they are to drive growth and productivity across the country. The Government has recognised this weakness in the UK's funding environment and commissioned the Patient Capital Review to explore ways to close the finance gap. The Autumn Budget contained a number of promising measures, but we think there is still more that can be done to channel large pools of existing capital to businesses looking to scale up.

WE RECOMMEND:

Allowing corporations to invest in VCTs in return for having 30% of the investment deducted from their corporation tax bill

There is significant potential to channel the excess cash held by corporations into innovative HGSBs seeking finance. £14 billion in excess capital is held by owner-managed UK corporates alone, and we recommend that the Government incentivises corporations to invest this excess cash in innovative HGSBs by extending the tax-advantaged Venture Capital Trust (VCT) scheme to corporations.

By allowing corporations to claim back 30% of the value of any investment in VCTs from their corporation tax bill, we believe it is reasonable to forecast that within three years there would be £1 billion additional inflow into VCTs. Such a change would unlock much-needed additional finance for HGSBs, which are significantly more productive than normal businesses.

Mandating public sector pension funds to allocate 1% of their assets to venture capital investment

Pension funds manage about £2 trillion of capital in the UK, but in comparison to other countries the UK has been poor at channelling these large pools of capital into the ambitious businesses that need it to scale up. Pension funds in the United States play a pivotal role in the development of high-growth businesses and have invested in some of the US' most successful companies. Even a small increase in the proportion pension funds invest in venture capital could unlock billions in extra cash and make a real difference to HGSBs across the UK.

The Government recognised this huge potential in its Patient Capital Review consultation, and set out a number of measures in the Autumn Budget designed to incentivise pension funds to increase investment in venture capital. While these were a welcome first step, we think that there is scope for the Government to be more ambitious and lead by example, mandating public sector funds to invest a small portion (1%) of their assets into venture capital.

Allow existing Stocks and Shares ISAs to invest equity in unlisted shares

There is £315 billion held in Stocks and Shares ISAs, and if just 1% of this capital were invested in small, unlisted companies, it would unlock £3.15 billion of extra investment for HGSBs. We therefore recommend permitting existing Stocks and Shares ISAs to invest into the shares of unlisted companies. As investors tend to retain assets in their ISA indefinitely, only removing money from their ISA as a last resort, such a reform would make it one of the most patient forms of capital.

The change would allow funds to be invested in earlier-stage smaller companies as well as in AIM and FTSE listed companies. The Government's decision to enable AIM shares to be held within an ISA wrapper has been a significant success story. Since the rules changed in 2013, Octopus has raised and deployed £500 million into AIM companies with a growth mandate, comprising both new ISA investments and the transfer of existing ISA portfolios that would previously have been invested in large FTSE listed companies or cash.

Currently investors can make loans from their ISAs to unlisted companies as a result of the Innovative Finance ISA, which often results in their taking equity-type risk (due to smaller early-stage companies being more poorly capitalised and having few assets) without having any potential to qualify for the incremental upsides attached to equity investments. We would expect the enabling of unquoted companies to be held in an ISA to be easily understood and therefore start to deliver benefits very quickly. It would also provide an additional source of financing for companies that have exceeded the VCT investment limits, and start to create an investment environment more akin to the US system.

The legislation required to achieve this would be straightforward to implement, and some of the existing anti-avoidance legislation employed for Self-Invested Personal Pensions (SIPPs) could be borrowed to prevent special-purpose vehicles from qualifying.

Reform the Advance Assurance process

At present, before investing, venture capital schemes must seek assurance from HM Revenue & Customs (HMRC) that their investment will qualify. According to rule changes announced in the 2017 Autumn Budget, this process should take a maximum of 15 days. However, a recent survey by the Venture Capital Trust Association showed that this process on average takes about 71 days, with some deals already waiting for over 20 weeks. This system is unsustainable, and businesses must have the access to capital or in some cases risk going out of business.

Currently all venture capital trusts must apply for advanced assurance when making an investment in a business, or risk the complete loss of status for making an inadvertent non-qualifying investment as a penalty. This penalty is intended to prevent abuse, but the unintended consequence has been that VCT funds are proceeding only with investments which have prior HMRC advance assurance approval. This places enormous pressure on HMRC inspectors and results in long approval processes which lengthen the time it takes for eligible companies to receive investment.

The current penalty for a breach whereby the whole fund is disqualified is disproportionate. We propose that the Government should increase resources to HMRC to deal with the backlog and should also amend the law to state that in the event of a breach on an individual company investment, the sanction could be the clawback of the VCT tax relief for that investment. Reducing the disproportionate breach penalty will lead to VCTs investing on the basis of professional opinion and dramatically reduce HMRC's advance assurance workload, saving scarce Governmental resources and speeding up the deployment of patient capital.

Assisting start-ups and SMEs to navigate the system of provision

In our last report, we suggested that the Government should use the Local Enterprise Partnership (LEP) network to ensure that HGSBs get the support they need. Since then, the Business, Energy and Industrial Strategy (BEIS) select committee has found[11] that SMEs remain largely unaware of the finance options available, or do not understand which ones are most appropriate for their needs.

The Government acknowledged this in its response to the Financing Growth in Innovative Firms consultation[12], recommending that a new commercial investment programme be developed through the British Business Bank to support developing clusters of business angels outside London. While this is welcome, the nature of devolution across the UK means that there is a patchwork quilt of support, where businesses remain unaware of the resources available for entrepreneurs. We welcome Government support of business angels, and recommend that Growth Hubs are better promoted to businesses and have a clear strategy for supporting HGSBs.

We also endorse the BEIS Select Committee's call for the Government to "add value by working with the major business groups and finance providers to make sure they have mentoring schemes or events specifically aimed at passing on the experience of successful business people on how to secure finance to grow a business."

11. BEIS Select Committee (2016), 'First Report of Session: Access to Finance'. 12. HM Govt (2017), 'Financing Growth in Innovative Firms Consultation Response'.

2 AS THE GOVERNMENT RIGHTLY IDENTIFIES IN ITS INDUSTRIAL STRATEGY, THE UK NEEDS TO ADDRESS ITS SKILLS SHORTAGES BOTH IN EXISTING JOBS, AND ALSO ENSURE THAT THE UK'S WORKFORCE IS TRAINED FOR THE JOBS OF TOMORROW

As some of the country's most innovative firms, it is unsurprising that 90% of HGSBs acknowledge that they face skills shortages, compared to a national average of about 18%. This disparity needs addressing in order for HGSBs to be fully equipped to scale up.

WE RECOMMEND:

Continuing to invest in digital skills to ensure the UK remains competitive

We welcome the Government's commitment to improving the UK's digital offer. The creation of a Minister for Digital and Creative Industries and the prominence of digital connectivity in the Industrial Strategy is testament to the emphasis Government is placing on the importance of digital infrastructure to a successful UK economy. Furthermore, the Government has demonstrated the importance of digital to the future of the UK in its Digital Strategy, published in 2017.

The Government recognises that a shortage of digital skills exist within the UK labour market, and that this poses a major risk to business growth and innovation.[12] It is imperative that this skills gap is filled, as this is not only detrimental to UK business, but also impacts the UK's attractiveness as a place to invest and do business.

Successive governments have been instrumental in encouraging the next generation to study STEM subjects, but too many leave the profession, resulting in a waste of talent in vital industries. Universities and businesses must now support the Government in its aim to close the skills gap by incentivising graduates to pursue STEM careers. This can be done by expanding schemes such as students undertaking a year in industry, having extensive networking opportunities and introducing mentoring schemes.

Taking a twin approach between technical disciplines and more traditional academic courses

Entrepreneurship should not be studied in isolation, as new businesses can be born from any discipline, and indeed often combine a variety of areas. The University of Bristol offers an Innovation programme which combines in-depth subject specialisms – in areas including history, computer science, management, physics and psychology – with entrepreneurial skills. Most crucially for HGSBs, the courses are heavily integrated into the local business environment, as students solve real-world challenges for local partners and are mentored by local stakeholders and business leaders.

The University of Huddersfield offers a BA in Enterprise Development, and is supported by visiting professors and entrepreneurs in residence. It also has the 3M Buckley Innovation Centre, home to over 100 start-ups, which facilitates access to finance for entrepreneurs and businesses; the centre combines the skills and expertise of University staff and partners to transfer knowledge between tenant companies.

We recommend that the Government should work with universities to encourage more interdisciplinary courses that combine teaching subject specialisms to a high standard, with the essential skills needed to succeed as an entrepreneur, or find innovative ways to combine entrepreneurship with teaching on site.

13. HM Govt (2016), 'Digital Skills for the Economy'.

Encouraging school career services to partner with HGSBs and ensuring teachers have the time to see how technology is changing the world of work

It is during secondary school that students make decisions that essentially begin their future careers; from their choice of GCSEs, the decision to attend university or not, or whether they wish to pursue a more technical qualification. 16 to 18-year-olds need a much more balanced education in order to be successful in the workplace.

It is at this stage in young people's lives that they need to be exposed to as many different options as possible in order to choose the right path for them. Ada, the National College for Digital Skills, puts the emphasis on a much more balanced education in order to teach a mix of tech, entrepreneurship and creative skills to all students. It works closely with businesses, taking the time to do outreach work with employers. This is enabled by recruiting more teachers than it needs, and fundraising to top up the money it receives from the Government to do so.

We recognise that not all schools and colleges will be able to do this, but we encourage the Government to work with the education sector to find ways in which school and college leaders can take the time to see how technology is changing the world of work. This could be by carving out a small amount of time each term enabling them to do outreach work, and taking the time out of the classroom in order to meet businesses, or by developing a specific course.

As technology develops, so must the skills required to be successful in the workplace. It is not enough to keep looking overseas for the talent required to work in start-ups and HGSBs. Schools and colleges must be supported to teach the necessary coding and other digital skills that will be necessary for the economy of the future.

Alongside the traditional career path of employment, we encourage the Government to ensure that entrepreneurship and the skills needed to set up and run your own business receive a much greater exposure in the career advice services within all schools. Careers advisers need to better understand the current world of work, how tech is changing it, and what this means for school leavers, so they can better advise on the options available for students.

Reforming the current Apprenticeship Levy to become a wider, more general Skills Levy

While we welcome the Government's commitment to increasing technical training with the implementation of the Apprenticeship Levy and the introduction of T Levels, there is still the opportunity to go further, particularly in more effectively utilising the funds from the Apprenticeship Levy. A key component of improving the success of the Apprenticeship Levy is allowing employers, particularly HGSBs, a longer timeframe to spend their Levy vouchers. It is also imperative that consideration is given to how the process of approving new skills standards across industries can be accelerated.

Expanding the current Apprenticeship Levy to evolve into a more flexible Skills Levy would allow the Levy to benefit a wider group of recipients and allow for the retraining and upskilling of the UK's workforce. Closing the skills gap is not solely dependent on creating more apprenticeships; it is also intrinsically linked to longer-term careers and throughout one's career, keeping pace with the skills demands of the UK's economy. The reform of the Apprenticeship Levy would need to incorporate a focus on the skills that are of strategic importance to the nation, particularly following the UK's departure from the EU.

Allowing larger companies to transfer their Apprenticeship Levy funds to smaller companies in their supply chain

This report has highlighted that 90% of HGSBs face skills shortages, compared to the national average of 17% for other businesses, and that one of the biggest barriers to providing more training was the cost of doing so. Larger companies, which are less likely than HGSBs to suffer from skills shortages and have more money available to pay for training, also benefit when staff in their supply chain are properly trained. Currently they can transfer only 10% of their Levy to smaller companies in their supply chain, but we believe that there should be no limit. The Government should consult on how the transfers should work and what controls would need to be put in place.

Investing in localised versions of the National Apprenticeship Service, and providing small amounts of funding for businesses to understand what training is available

Although the introduction of the Apprenticeship Levy was an important step in addressing the skills shortages in the UK economy, businesses are struggling to navigate the centralised, national database from which they access apprenticeships.

The report shows that, along with strains on time and funding, many HGSBs have difficulty finding training providers who can deliver the training that they need. This suggests a more localised system that is responsive to the specific needs of businesses in the region and linked closely to local college, universities and technical schools, would be much more effective at helping HGSBs get the skills they need to succeed.

There are already examples of how this might work, such as the Nottingham Jobs Hub, where specialist staff offer a tailored training needs analysis for small businesses, and then help to meet these needs through their partnerships with local universities and colleges. We commend this as a good model for a local apprenticeship service, that can complement the National Apprenticeship Service, by providing the local knowledge and stakeholder links that HGSBs direly need.

The Federation of Small Businesses in Wales has secured a £40 million package, offering small businesses up to £3,900 of funding towards an apprenticeship's salary in the first 12 months, and up to £500 per business for administration costs, such as identifying the most appropriate training or researching the options available. The FSB also found one in three small businesses said that a greater financial incentive would encourage them to employ an apprentice. Making HGSBs more aware of the support available, and offering small amounts of financial assistance, would go a significant way to improving access to training.

3 FOR HGSBS TO THRIVE IN THE 21ST CENTURY, THE CONNECTIVITY OF BUSINESSES MUST BE IMPROVED

While Government investment is vital to upgrading the UK's infrastructure as a whole, improving some aspects of the infrastructure network – such as digital communications – is no longer the sole responsibility of the Government and requires input from the private sector, local authorities and regional business networks, through the Super Connected Cities Programme, the Connection Voucher Scheme and launching a review into Telecoms Infrastructure.

WE RECOMMEND:

Increasing powers in City Deals to give Metro Mayors more power over digital infrastructure requirements

The creation of Metro Mayors is an exciting political innovation with the potential to transform these regions, as power is handed to local leaders with the drive and knowledge to affect real change. Many of these new mayors are attempting to meet the challenges of the 21st-century economy head on, spearheading initiatives to help their regions capitalise on technological change.

Andy Burnham in Manchester held the first-ever Greater Manchester Digital and Tech Summit, while West Midlands Mayor Andy Street has pledged to develop new spin-off start-up ventures from existing industries, such as an automotive start-up accelerator with Jaguar Land Rover.

However, this early promise will come to nothing if Mayors don't have the power to build the digital infrastructure they need to support a high-tech economy. Although there are a number of promising national initiatives, the devolution deals did not specifically address digital infrastructure, and we would urge the Government to develop tailored, regional plans, in partnership with Metro Mayors, that will enable them to upgrade digital infrastructure and realise their ambitious plans for the digital economy.

Accelerating and broadening current digital initiatives, particularly the Gigabit Voucher Scheme

Rapid improvement in digital connectivity is vital for the prosperity of HGSBs, and due credit should be given to the Department for Digital, Culture, Media and Sport, which has been at the forefront of driving this. However, the UK's digital infrastructure system currently lags behind those of other countries, and was acknowledged when the then Digital and Creative Industries Minister, Matt Hancock MP, referenced that "UK full fibre coverage is just 3%".[14]

The Government's Gigabit Voucher Scheme, which will provide vouchers worth up to £3,000 "to support the capital costs of getting new gigabit-capable connections for businesses" is currently being tested in four areas of the UK: Aberdeen and Aberdeenshire; Bristol, with Bath and North East Somerset; Coventry and Warwickshire (North Warwickshire, Nuneaton and Bedworth, Rugby, Stratford-on-Avon, Warwick); and West Yorkshire and York (Bradford, Calderdale, Kirklees, Leeds, Wakefield and York).[15]

We encourage the Government to expand this trial to areas which have identified digital infrastructure to be of the greatest importance, such as the North West, and target their investment accordingly. Following the trial, we also call on the Government to rapidly roll out this initiative across the entire UK, so every region can reap the rewards of digital connectivity.

14. Speech by Minister for Digital Matthew Hancock MP to Broadband Stakeholder Group 2017 Conference. 15. HM Government (2018), Broadband Delivery UK Strategy.

Increasing awareness of new digital technologies among business, local Government and public bodies, and informing small businesses about the benefits and availability of better digital connections

Businesses must be more aware of, and better prepared for, the speed of technological developments and the impact they have on companies, but they do not always have the time to do this. We recommend the Government considers partnering with bodies such as the Institution of Engineering and Technology, to educate training providers and local authorities so they are best placed to assist and provide advice to local businesses. The UK's businesses must be able to harness technology to drive efficiency, which in turn, increases productivity.

Encouraging the public sector to embrace new technology as an early adopter, such as using fibre over copper cables

Research commissioned by the Department for Digital, Culture, Media and Sport found the country gains £20 in net economic benefit for every £1 of public investment in digital infrastructure. Cutting-edge digital infrastructure requires full fibre networks that can operate at speeds 100 times faster than most current broadband links. However, replacing existing digital infrastructure is expensive, and can often see upgrades that claim to be "fibre broadband" but still involve copper cable.

This technology is known as "Fibre to the Cabinet", but it relies on a final leg of copper wire, from the cabinet into the premises. This slows data down and causes congestion. While these so-called "fibre" services are undoubtedly better than older technology, they cannot compare with the new era of gigabit speeds and are woefully inept at supporting the crucial uploading of data, leaving businesses unable to access the speeds they need. The Government should put more pressure on BT Openreach to accelerate its "Full Fibre" programme even further, beyond its unambitious target of reaching 3 million homes and businesses by 2020.

Large public-sector organisations, such as schools, hospitals and local councils, can ensure that investment in fibre infrastructure is commercially viable by agreeing to act as "anchor tenants" for full fibre broadband services. This provides certainty for private companies who build fibre infrastructure and ensures that other private companies in the area can then access this infrastructure once it has been built. The Government has said it would support projects that propose the use of public sector anchor tenancies as part of its Local Full Fibre Network Programme, but we feel the Government could be more proactive in exploring the use of anchor tenancies.

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For further information about the methodology and research data included in this report, please contact Beatriz Cruz at the Centre for Economics and Business Research (Cebr).

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