REGIONAL ACCESS TO FINANCE EXPERT GROUP FOR THE NORTH EAST

ACCESS TO FINANCE: DEMAND FOR FINANCIAL ENGINEERING TOOLS IN THE NORTH EAST OF ENGLAND

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1. EXECUTIVE SUMMARY

Deloitte & Touche has been commissioned to identify the financial needs of SMEs in the North East and to outline key recommendations to improve access to finance. As part of our study we have consulted with SMEs and intermediaries in the market place to understand the demand and supply side issues that currently affect the ability of SMEs to obtain finance.

This report has explored the issues facing new business start-ups (less than 36 months old) and growth businesses (more than 36 months old). A wide range of key problems have been identified in the region including:

- Low level of entrepreneurial development and business start-up rate;
- Higher level of business failure compared to other regions in the UK;
- Low SME base; and
- Relatively low levels of venture capital investment in all sectors.

The key issues identified as part of our study include:

- *Venture capital* - lack of choice and competition, lack of matched funding opportunities, insufficient knowledge about venture capital, high cost of transactions, few business start-up opportunities, lack of affordable management support to accompany venture capital investments;
- *Banks* - very risk averse, high security requirements, inflexible finance packages, start-up finance difficult to obtain, movement towards factoring;
- *Micro finance* - inability to obtain very small levels of finance for working capital requirements and growing reliance on credit cards, non payment to directors and personal loans;
- *Integrated packages* - few integrated support packages to provide funding with management support and advice;
- *Knowledge and awareness* - poor knowledge and awareness of finance options and financial issues;
- *Culture* - employee culture rather than entrepreneurial culture;
- *Public sector support* - confusion about public sector business support and key service providers;
- *Use of business support* - low use of business support due to cost, value for money and quality; and
- *Networking* - lack of networking opportunities.

We strongly recommend that an integrated approach is taken to address the key access to finance issues and improve SME performance. Demand and supply-side programmes should be developed to improve the ability of SMEs to recognise their financial needs, obtain finance and maximise their potential. The focus should be on developing a framework for long term sustainable business success in the North East.

The key recommendations are listed below and include a combination of short, medium and longer term initiatives to improve access to finance:

- Management support programme to accompany NERIF III finance to reduce inherent risk of the investment, maximise business potential and improve business survival rates;
- New business start-up integrated package (loans, venture capital, subsidised direct management support and mentoring) to meet the finance gap in the market for start-ups and help encourage entrepreneurial development;
- High growth business integrated package (loans, venture capital, mentoring) to identify and promote business growth;
- Micro loan fund to help small businesses meet their short and medium term working capital requirements;
- Network development for SMEs and key intermediaries to improve the efficiency of information flow in the region;
- Region wide business support/investment readiness programmes to develop the SME base, improve survival rates and reduce the risk of future investments; and
- Entrepreneurial development programmes to improve the communication and awareness of self-employment and business creation (in line with the Regional Enterprise Strategy and Regional Economic Strategy).

Several issues have also been highlighted that cannot be addressed at a regional level. We consider these issues to be important in improving overall SME access to finance and believe that the Regional Access to Finance Expert Group is best placed to raise these issues with national organisations to try to influence national policy. The key issues raised are:

- Inadequacy of the Small Firm Loan Guarantee Scheme eligibility criteria/limits;
- UK attitude towards entrepreneurialism compared to other countries;
- Confusion about business support services provide by Small Business Service and Business Links; and
- Risk averse nature of the banking sector and their continued reliance on tangible assets and trading records.

Overall, the evidence suggests that the North East is falling behind other regions in the UK in terms of new business development, survival rates, and venture capital investment. This will have long term implications for the competitiveness and economic growth of the region unless a long-term approach is adopted to help address the key financial and business support issues facing SMEs in the region today.

2. INTRODUCTION

This chapter outlines the project brief, background to access to finance in the UK and the structure of this report.

2.1 Foreword

Access to finance for small and medium enterprises (SMEs) has been a constant topic of academic research and policy for decades. Research has traditionally considered elements of both demand and supply-side issues affecting SMEs ability to access finance, although a supply-centred research methodology has prevailed.

This report provides the results of the Deloitte and Touche research into SME access to finance in the North East as commissioned by the Regional Access to Finance Expert Group. The report has a specific focus upon understanding the financial needs and requirements of SMEs and to identify the key access to finance issues that they face today, or anticipate facing in the future. Supply-side issues have also been explored to ensure that a well-balanced view of the financial market has been obtained.

Our report highlights the current regional access to finance position compared to the rest of the UK, the key access to finance issues facing SMEs, a series of recommendations taking into account the European Regional Development Fund (ERDF) Objective Two funding programme, higher level strategic issues that can be explored by the Expert Finance Group, and priorities for the region.

2.2 Background

Access to finance for SMEs is a recognised priority area at a regional, national and European level and is not unique to the North East of England. However each region has location-specific issues that impact upon the ability of SMEs to access finance and the regional operation of the finance and support structure.

Key strategic partners in the North East have recognised that the region is falling behind other UK regions in terms of SME performance and entrepreneurial development (regional performance issues are explored within Chapter 3). This is recognised in the Regional Economic Strategy (RES) and other key strategic documents, which indicate that improvements in SME access to finance are required if the region is to unlock its potential. The 2002 updated draft RES *'Realising Our Potential'* includes SME development and access to finance at the heart of two of its main objectives:

- Building a Knowledge Driven Economy (B1); and
- Establishing a New Entrepreneurial Culture (B2).

Therefore it is clear that SME access to finance issues, including entrepreneurial development, must be addressed if One NorthEast is to realise its vision.

A large proportion of the North East is designated as an Objective Two eligible area (or area of transition). The Single Programme Document (SPD) that informs the funding programme reflects the objectives of the RES and considers access to finance to be pivotal in achieving its three strategic components:

- To create a substantial volume of new jobs;
- To improve the number and performance of SMEs; and
- To tackle social and economic inclusion.

The SPD has four key priority areas and several measures within each priority. Two specific measures are directly relevant to SME access to finance:

- **Priority One – Establishing an Entrepreneurial Culture**
  Measure 1.2 – Providing Access to Finance for Entrepreneurs
  - Start-ups and entrepreneurs that have been operating for less than 36 months; and
- **Priority Two – SME Growth and Competitiveness**
  Measure 2.2 – Providing Access to Finance for SMEs
  - Existing SMEs that have been operating for more than 36 months and require finance for growth.

The above measures have been grouped as the '*Access to Finance Package*' and are operated by One NorthEast (ONE). ONE agreed to act as Regional Package Co-ordinators for priority areas within the Objective Two programme that require a strategic fit. An initial Package Delivery Plan (PDP), including the identification of the key forms of SME finance, was produced in 2001 to inform the delivery of this package. A copy of the PDP and the finance listing is available from the Government Office web-site: www.go-ne.gov.uk.

This report aims to identity the key issues affecting the effectiveness of SMEs at the start-up and growth stage and suggests areas for improvement and intervention if appropriate.

2.3 Terms of Reference

The key components of the project brief are:

- Identify, via direct SME consultation, the key types of financial support that SMEs require;
- Identify the key barriers affecting SME access to finance;
- Outline the types of SME financial support that has succeeded; and
- Recommend funding tools for SMEs that can be supported by European funding.

Deloitte & Touche will not produce a separate finance mapping analysis detailing finance options for small businesses. However ONE has commissioned a separate report to list all finance types available to businesses in the North East. Draft findings are expected to be available in the New Year. This separate study can be used as a quick reference guide for finance options.

Although the Programme Complement includes an '*Access to Finance*' and '*Business Support*' measure, our proposal stated that it is becoming increasingly difficult to separate the two areas as they are inextricably linked and impact upon SME development. Therefore we stated that we would refer to business support in addition to finance issues to:

- Ensure that recommendations were cohesive and had a firm focus on overall SME development;
- Maximise the effectiveness of specific financial measures; and
- Ensure a strategic fit with other regional initiatives including the RES and the Enterprise Strategy, '*Everybody's Business*'.

The Regional Access to Finance Expert Group will consider the findings of this study in addition to a Project Steering Group (see Appendix II and III for listing of members of both groups).

Full terms of reference are included in the tender documents produced by Government Office North East and are summarised in Deloitte & Touche's Project Initiation Document. Both are available on request.

2.4 Methodology

To complete the project brief requirements as outlined in section 2.3, we have used a wide range of research and strategic planning methods:

- **Desk Based Research**

  Review of current reports, studies and academic research to identify current business support and financial trends, performance indicators, key SME issues and sources of finance at a regional, national and European scale. Reference is made to relevant studies as relevant throughout this report.

- **SME Consultation Programme**

  The project brief stated that this research programme should be demand-led and should seek to consider the financial requirements of SMEs. Therefore two forms of consultation were performed:

  - ***In-depth interviews with 15 SMEs in the region to discuss:***
    - Current finance structure;
    - Future financial requirements;
    - Factors influencing finance decisions;
    - Barriers to accessing finance and success factors;
    - Knowledge and awareness of finance and business support;
    - Key financial and business issues now and in the future;
    - Use of business support services (and links to finance).

- ***SME questionnaire***
  - Database developed using One Source and VAT Registrations;
  - Issued to 500 SMEs;
  - Approximately 50 returns received (10% success rate on par with similar studies throughout the UK).

  The individual contact and business names of SMEs contacted, as part of the research programme will not be contained within this report for confidentiality purposes.

- **Intermediary Consultation Programme**

  Members of the wider business community (finance providers, business support providers, public sector organisations) were also consulted to provide a balanced overview of the key products and services available to SMEs and the key access to finance issues from a 'supply' perspective.

  A full list of consultees is provided in Appendix I and was discussed with the Project Steering Group.

  The number and list of consultees was agreed by the Project Steering Group at the outset of the project to include a variety of intermediaries. In addition, to the consultees agreed at the start of this assignment, we have also consulted with members of Deloitte & Touche corporate finance department.

- **Stakeholder Consultation**

  Regular meetings with the Project Steering Group have taken place during the research programme to share findings and obtain immediate feedback on emerging issues.

  See Appendix II for a list of the members of the Project Steering Group.

- **European Regional Packages Workshop**

  The North East of England European Partnership Regional Packages Partnership event took place on 6th August 2002 in Durham. As part of this event, an Access to Finance workshop was conducted by Government Office North East and One NorthEast to understand the key business support and financial issues for SMEs.

2.5 Report Structure

The remaining sections of the report include:

- Chapter 3 – reviews the relative performance of the North East compared to other regions in the UK to highlight some of the key issues facing the North East today. It considers business start-up and closure rates, levels of venture capital investment and survival rates.
- Chapter 4 – discusses the key access to finance issues affecting the North East using evidence obtained directly from SMEs and intermediaries.

- Chapter 5 – outlines a series of recommendations to address the key regional issues identified including next steps for the region.
- Appendix I – List of intermediary consultees.
- Appendix II – Members of the Project Steering Group.
- Appendix III – Members of Regional Finance Expert Group.
- Appendix IV – Regional business start-up and closure analysis.
- Appendix V – Listing of bottom ten postcodes for business start-ups and regional liquidation levels.
- Appendix VI – Questionnaire as distributed to SMEs.
- Appendix VII – Finance case study.

2.6 Key Features

The key features of the report include:

- We have considered issues that relate to new business start-ups (less than 36 months old) and growing businesses (more than 36 months old). This is consistent with the ERDF Single Programme Document. We have highlighted those issues that relate to a specific stage of the business life cycle. e.g. high growth business. Although unless otherwise stated, it can be assumed that an issue relates to all stages of the business life cycle;
- We have referred to SME issues as 'demand' or 'supply' issues. This assists in the communication of key issues and helps to differentiate between financial issues and wider business concerns;
- A universal definition of an SME does not exist with organisations using a variety of definitions. Therefore we have used the standard ERDF definitions unless otherwise stated;
- As part of the project brief, we have been asked to consider all of the access to finance concerns facing SMEs and their key needs. Therefore, although we have reported all key issues in this report we have not devised a recommendation to address each individual issue;
- Recommendations are stated as being short, medium or long term. We consider short term initiatives to be capable of implementation within six months, medium term initiatives capable of implementation between six and twelve months, and long term initiatives to be capable of implementation within eighteen months; and
- We have also included issues that are considered to be national policy issues in addition to specific regional issues. National issues have been summarised within Chapter 5.

2.7 Limitation

The analysis, opinions and recommendations contained in this report have been conscientiously and objectively produced on the basis of the information available to

Deloitte & Touche at the time. We can not be liable for the accuracy of data provided to us by third parties.

Their ultimate deliverability of our recommendations is subject to many factors beyond the control of Deloitte & Touche, including:

- The agreement of other partners and stakeholders within the SME finance network; and
- The market factors of demand and supply of finance to the SME sector.

Thus, whilst we cannot guarantee the achievability of the recommendations proposed, we do consider them sufficiently robust to determine the best way forward for the future development of access to finance for SMEs in the North East.

Our work was carried out to meet the specific requirements of the Regional Access to Finance Expert Group. As such it should not be relied upon by others to serve other purposes or meet other objectives.

3. PERFORMANCE OF THE NORTH EAST

This chapter discusses the recent business performance of the North East compared to other regions in the UK.

3.1 Introduction

This chapter explores some of the key social, economic and financial trends in the UK and the North East which may contribute towards current SME access to finance. Past and present relative performance is a key tool in understanding some of the issues that SMEs face today, and by reviewing entrepreneurial levels, venture capital investment trends and business start-up and failure rates, the North East can be placed into context within the UK as a whole.

Some of the key regional business statistics provide an interesting overview of the current position of the North East business activity. The North East economy has grown at a much slower rate than the rest of the UK and its GDP is well below the national average indicating a decrease in the relative economic importance of the North East. The region has the lowest SME stock base in the UK and has experienced one of the lowest levels of new business VAT registration levels in the UK demonstrating an inability to nurture an entrepreneurial culture.

In addition, the North East was the only region in the UK to experience a net decrease in the number of VAT registered businesses in 2001 highlighting potential weaknesses in the region’s ability to sustain new business development.

Some of the headline statistics as detailed below are further developed in Chapter 4 (key issues from market consultation) to help explain why the North East is statistically one of the most disadvantaged regions in terms of number of businesses, new business start-ups and survival.

3.2 VAT Data - Business Start-up Rates and Closures

VAT registrations and de-registrations are the best official guide to the pattern of business start-ups and closures. They are an indicator of the level of entrepreneurship and of the health of the business population. The latest Small Business Service (SBS) statistics for 2001 highlight several issues for the North East.

3.2.1 UK Position

- Total number of businesses has continued to increase year-on-year to a level of 1.68 million in 2001 (2000 – 1.66 million).
- In 2001 total registrations and de-registrations were slightly down on the previous year at 175,500 (2000 - 183,300) and 162,700 (2000 – 177,100) respectively.
- In 2001 there were 37 registrations for every 10,000 people aged over 16 in the UK (2000 – 39).
- London continues to attract the highest absolute levels of business start-ups, closures and has the greatest number of businesses.

3.2.2 North East

- **The North East has a relatively small business base**

  - The region has the lowest number of businesses in the UK, and it is decreasing (2001 - 41,900 and 2000 - 42,000).

  - This represents 2.5% of total businesses in the UK – the lowest in the UK.

- **The North East has a poor record of new business start-ups**

  - It has the lowest absolute number of business registrations and de-registrations in the UK.

  - Registrations in 2001 were 4,100 (2000 – 4,300).

  - De-registrations in 2001 and 2000 were 4,200.

- **The North East is lagging behind other UK regions in supporting businesses and developing an entrepreneurial culture**

  - The North East was the only region in the UK to suffer a net decrease in the number of businesses in 2001.

  - The North East has one of the lowest number of new business start-ups as a percentage of total businesses at 9.8% in 2001 (2000 – 10.2%). The UK average in 2001 was 10.8% (2000 – 11.4%).

  - The North East has the lowest number of new business start-ups per head of population. In 2001 there were 21 new business start-ups for every 10,000 people over 16 (2000 – 20). The UK average was 37 in 2001 (2000 - 39).

See Tables 4 & 5 in Appendix IV for further details of business start-ups and closures in the UK and a full regional analysis.

3.3 Bank of England Data - Business Start-ups and Closures

Business start-ups and closures are also monitored by national banks on a quarterly basis and feed into the quarterly Bank of England report on Small Businesses (this is not based solely on VAT registration data). The North East has one of the lowest levels of business start-ups in the UK and is has several of the least desirable postcodes in the UK for new business start-ups. For example, Sunderland is highlighted as a specific black-spot in the North East and is ranked lowest in the UK in terms of business start-ups per 1,000 of the working population. Appendix V Table 6 includes a full analysis.

The North East also has one of the highest number of liquidations and business bankruptcies in the UK as detailed in Appendix V Table 7. The North East has the third highest level in the UK for the half year to June 2002 (behind London and South East) indicating a disproportionate level of closures compared to the absolute business base and business start-ups.

3.4 Business Survival Rates

The SBS are also responsible for recording and monitoring business survival rates. Latest figures for 2000 indicate that in the UK, 61% of businesses survive for three years or more after start-up. However this compares to a North East average of 57%, with the South West and South East having the best survival rates in the English regions.

Therefore not only is there a low level of business start-ups in the UK, but those businesses that do start-up are more likely to fail within three years compared to other regions in the UK, further compounding the low business base in the North East.

3.5 Venture Capital Investment Levels

The British Venture Capital Association (BVCA) reports on annual investment levels in the UK and is considered to be the best indicator of venture capital activity. There are many widely used definitions of 'venture capital' however for the purposes of this report we are using the standard definition as used by the BVCA. Venture capital is considered to be the financing of unquoted companies ranging from small early stage companies to large management buy-out and buy-ins. In the USA, venture capital is referred to as investment in early stage and expanding companies only. Private equity is an increasingly used term in Europe, but some commentators use it to refer to management buy-outs/ins only.

Although it is important to examine the value of venture capital investment, it is particularly useful to consider the total number of investments as total investment levels can easily be distorted by large investment deals. Therefore throughout this analysis, we will refer to both the value of investments and the number of investments.

To analysis the current position of the North East venture capital market it is important to place the North East into a national context.

3.5.1 National Market

- **Fall in UK market size**
  - Value of investment has fallen substantially (2001 - £4,752m in 2001 and 2000 - £6,371m).
  - No of investments has increased (2001 - 1,307 in 2001 and 2000 – 1,182).
- **Little change to stage of investment – MBOs/MBIs dominate**
  - Number of investments:
    - Early Stage – 32%, Expansion Stage – 50% and MBOs/MBIs – 18%.
  - Value of investments:
    - Early Stage – 9%, Expansion Stage 34% and MBOs/MBIs – 57%.

- **Average investment size has fallen at all stages:**
  - Early Stage - £0.96m (£2000 – £1,719m).
  - Expansion Stage – £2,505m (2000 - £3,872m).
  - MBO/MBI Stage - £3,636 (2000 - £5,370m).
- **The hi-tech sector continues to attract high level of investment:**
  - One third of all investment was in the software and computer hardware sector (2001 - 379 investments and 2000 - 363).
  - This is followed by the pharmaceutical sector (2001 – 119 and 2000 - 98).

3.5.2 North East in a National Context

- **The North East venture capital market is very small compared to the rest of the UK and is declining:**
  - 33 investments out of a total 1,307 in 2001or 3% (2000 – 29 out of 1,182). In 1997, 47 investments were made in the North East.
  - Value of investments in 2001 was £33m out of £4,752m or less than 1% (2000 - £92m out of £6,371 or 1.4%).
- **The average deal size is lower than average:**
  - £1.15m in the North East (2000 - £3.17m).
  - £3.636m in the UK (£5.37m).
- **The North East has a lower than average value and number of Early Stage investments:**
  - 2% of total companies invested in the UK (9 companies in the North East).
  - 1% of value of investment (£2m in the North East).
  - The North East profile of companies receiving investment is broadly in line with the UK, albeit at a much lower scale. Early stage investment 27% (UK – 32%), expansion 61% (UK – 50%) and management buy-in/out 12% (UK - 18%).
- **The largest sector in the North East is Services followed by IT:**
  - 13 investments in services (out of 369 investments in the UK) with a total value of £14m. This is the lowest number of company investments in this sector in England. This highlights that although the North East is more successful in attracting investment in the service sector compared to any other sector, the region still has the lowest number of service company investments in England.

- 9 investments in IT (out of 438 investments in the UK) with a total value of £13m. This is the lowest investment number of company investments in this sector in England.

3.5.3 Local Market

- **Number of investments is decreasing year on year**
  - On average there have been 29 reported deals in each of the last three years – 25 in 2001.
  - *Source of all local market data is The Journal/PwC quarterly deals survey.*
- **Historically 3i has been the largest local investor**
  - Up to 1998, 3i's averaged 20 deals per annum.
  - Number of deals has reduced following closure of the 3i North East branch – 4 investments in 2001 (16% of total deals) compared to 17 deals in 1998 (40% of total deals).
- **Northern Enterprise Limited (NEL) is second largest investor (after unnamed sources)**
  - Unnamed sources are ranked first (includes all MBO/MBI).
  - NEL is main choice for start-up/expansion stage investment in the North East.On average the number of deals is approximately 10 from 1999-2001.
  - Very little venture capital investment by traditional banks in 2000 & 2001.

3.6 Implications for the North East

The evidence suggests that the North East has clearly fallen behind other regions in the UK as a business location for new start-ups and growth companies. The key issues raised so far are:

- Low rate of small business start-ups;
- Higher rate of business failure;
- Poor entrepreneurial culture;
- Below average levels of venture capital investment at all stages of investment, especially start-up stage;
- Declining local venture capital market with restricted choice and capped investment limits.

The specific issues raised by SMEs and intermediaries are discussed in Chapter 4 which outline some of the implications of the above issues and some of their causes.

4. KEY ISSUES

This chapter outlines the key access to finance issues facing SMEs today following the consultation programme and SME questionnaire.

4.1 Introduction

This section of the report outlines the key findings of the research based upon SME interviews, survey responses, intermediary interviews, and recent regional and national studies and surveys. This report seeks to differentiate between perception and reality to ensure that appropriate actions can be taken to address issues raised.

By way of an introduction, we have outlined the headline statistics and results from the SME survey analysis (see Appendix VI for a copy of the questionnaire) to highlight the current and future wider business needs of SMEs in the region. The issues raised as part of the questionnaire analysis are further explored within this chapter (section 4.3 and 4).

In considering SME access to finance issues, the terms ‘demand’ and ‘supply’ are well understood. Therefore for the purposes of this chapter the issues have been grouped as ‘demand-side’ or ‘supply-side’. We recognise that it is often difficult to consider demand and supply issues in isolation as they are inextricably linked. Therefore throughout this chapter, reference will be made to relevant associated demand and supply side factors as appropriate.

4.2 Questionnaire – Headline Results

4.2.1 Company Details

- 43% of respondents are start-up stage (less than 36 months old) and 57% are more than 36 months old (or did not state age).
- Good distribution of companies throughout the region.
- Good representation of a wide range of sectors including E-business, media, engineering, manufacturing, service sector, textiles, food and software and IT.
- 90% of people that completed their company details had a male Director/Chief Executive and more than 95% were of white origin.

4.2.2 Types of Finance

- The most commonly used forms of finance are:
  - Own money or family –77% of businesses;
  - Bank overdraft – 60% of businesses;
  - Credit cards –53% of businesses;
  - Short term loans/hire purchase/grants – each one used by 43% of businesses.

- 27% of business use overdrafts as a long-term form of finance.
- Venture capital finance has been used by less than 15% of businesses.
- Companies have used a wide range of finance with a large proportion (53%) using more than 5 forms of finance as part of a funding package. Only 19% of those companies were start-ups (less than 36 months old).
- Start-ups companies are more likely to have a simple finance structure with very few forms of finance used. 71% of companies who used less than 5 types of finance were start-ups.
- Start-ups are more reliant on internal sources of finance, credit cards, overdraft and loans.
- Established and growth companies are more likely to have complex financial arrangements – invoice discounting, factoring, venture capital, remortgages.

4.2.3 Funding in the Last Two Years

- Businesses have applied for overdrafts more than any other form of finance, with 83% of businesses being successful. 73% of overdrafts were less than £100,000.
- This is followed by grants and loans (success rates of 67% and 83% respectively). 80% of loans were less than £10,000.
- Few businesses tried to raise business angel finance or venture capital from a large institution.

4.2.4 Why is Finance Required?

- Businesses generally require finance for general working capital requirements (67% of businesses), followed by fixed asset purchase (43%) and product development (33%).

4.2.5 Who Makes the Financial Decisions?

- 58% of businesses stated that the owner makes all key financial decisions (followed by the finance director 17%). However 43% of owners who make the key decisions do not have a formal qualification (degree or finance qualification).

4.2.6 Use of Equity

- 31% of businesses have considered equity as form of finance for their business. However only 14% of all business have been successful, which appears to be higher than average, with key barriers noted to be:
    - lack of choice in the local market place;
    - lack of satisfactory exit route, especially for start-ups
    - lack of information about the equity process;

- lack of matched capital;
- equity was not appropriate for their business;
- internal lack of expertise to develop the business;
- business plans were not of a satisfactory standard;
- high costs of finance; and
- decision making process is too slow.

- The key barriers identified by the respondents suggest that there are demand and supply-side issues affecting the use of equity. These issues are further explored within Chapter 5.
- The average amount requested was £170,000 (variation £70-300,000).
- The survey results suggest that a higher than average number of businesses have used equity to finance their business. This suggests that respondents may be more financially aware than a typical business.

4.2.7 Availability of Business Information

- Businesses are generally not happy with the financial information available to them on grants, loans and equity:
  - 55% of businesses are not at all satisfied with information on equity, grants 43% and loans 35%;
  - 65% of businesses are quite satisfied or satisfied with available information on loans and 45% re equity information; and
  - New business start-ups are more likely to have the lowest level of satisfaction with financial information provision.

4.2.8 Financial Advice

- 54% of businesses use their bank as their main source of financial information, followed by professional advisors/accountants (20%) and Business Links (10%).
- In the last two years, businesses have contacted a wide range of organisations for support:
  - Banks 70%;
  - Business Links 53%;
  - Regional Development Agency (RDA) 20%; and
  - Professional Advisor 17%.
- Businesses are more likely to be satisfied with the advice they received from banks and professional advisors than Business Links and the RDA. The lowest level of satisfaction was recorded for the RDA.

- Business Links and the RDA are not perceived to be proactive and have the lowest level of satisfaction for response times.

- Advice is required for business planning (14%), applications (37%) and sources of finance (37%). A business is more likely to refer to an accountant for advice on business planning and wider sources of finance, and to banks for information on sources of finance.

4.2.9 Future Finance Needs

- 57% of businesses stated that they definitely intend to raise finance in the next two years, 17% did not and 27% were undecided.

- A wide range of finance is being considered for amounts between £5,000 and £1,000,000. Table 1 below highlights the financial requirements of businesses in the next two years.

Table 1: SME Finance Requirements in Next Two Years

Type of finance	Number	Value
Grants	7	Less than £5,000
Mortgage	5	Up to £300,000
Invoice Discounting/Factoring	4	Up to £500,000
Overdraft	4	Between £30-50,000
Equity from private investor	4	Between £30-200,000
Equity from institutions	3	Between £30,000 - £1,000,000
Loans	3	Between £30 - £100,000
Leasing/HP	2	Up to £150,000
Business Angel	1	£40,000
Credit Cards	1	Up to £15,000
Residential re-mortgage	1	£10,000

- 64% of businesses stated that they had access to enough information to inform their financial decisions as included in the table above.

- Grants are generally required for training purposes.

- Start-ups are more likely to require finance for working capital requirements.

- High-growth businesses (based upon turnover projections) are more likely to require venture capital.

- A shift towards factoring is evident. This is mainly due to the recent Brumark case resulting in changes to fixed and floating charges. This is expected to result in a shift away from the use of overdrafts and an increase in the use of factoring for small businesses.

- Businesses believe that there a wide range of obstacles that may affect their ability to raise finance in the next two years. Many of the points raised by SMEs are based upon their own experience of raising finance. Therefore, they are often perception based and not supported by the key intermediaries. The balance between the two is fully explored in section 4.3 and 4. The perceived key obstacles from the SME point of view include:

  - Limited sources of finance in the region;
  - Security required to obtain finance from banks;
  - Lack of track record for new business start-ups;
  - Requirement for detailed business plans beyond the expectations of the Director(s);
  - Insufficient time or knowledge to complete applications;
  - Perceived high risk of the business;
  - Business support agencies have a lack of specific business expertise to inform and guide a business through the finance process;
  - Inability to obtain matched funding;
  - Lack of understanding of larger SMEs by the public sector (larger SMEs refers to those businesses that are not based upon traditional industry and are considered to be high growth scientific based companies); and
  - Limited assets for security.

- Future finance is most likely to be required for working capital (25%), fixed asset purchases (25%), new product development (17%), market development (13%) and business acquisitions (6%).

4.2.10 Business Confidence

- 89% of businesses surveyed believed that their business activity would grow in the next 12 months with 11% expecting a downturn.

4.3 Demand-side Issues

4.3.1 Entrepreneurial Culture

The evidence suggests that the North East has a very poor entrepreneurial culture which has been said by many commentators to be due in part to its industrial legacy and traditionally high levels of employment in the manufacturing sector. This also reflects the UK's general attitude to entrepreneurs.

This manifests itself in low levels of business start-ups, low levels of high growth businesses, high levels of business failures and a reliance on large-scale manufacturing and engineering employers. This in turn results in a low level of role models for young people and a downward spiral of development.

However, the recent 2002 Entrepreneur of the Year awards included two North East based business people in the top 10. This indicates that the North East can create successful entrepreneurs and that the region has potential role models for other businesses.

Many finance providers in the region believe that the North East does not have difficulties in it's supply of finance but instead suffers from a low level of drive and determination amongst people in the region who do not want to own their own business. Therefore they would advocate that rather than introduce a range of supply side initiatives, steps should be taken to improve the entrepreneurial base and encourage all age ranges to consider the benefits of self-employment or owning their own business.

The evidence from this research strongly suggests that there are a series of supply and demand side issues that affect the SME base and access to finance in the region. The entrepreneurial culture is one of the key issues that is required to be addressed to improve the economic growth of the North East and develop a SME base that is proportionate to its population. This is also recognised as one of the key components of the Regional Economic Strategy.

4.3.2 Knowledge and Awareness

Interviews with intermediaries and SMEs, and the questionnaire analysis have highlighted that SMEs have a lack of understanding and awareness of:

- sources of business support available to them;
- 'trigger points' or critical events that suggest that external support or advice is required;
- range of finance available;
- advantages and disadvantages of various types of finance;
- how to decide what form of finance is best for them; and
- when is the best time to access finance.

This may result in a low level of business start-ups, low levels of business growth and/or business closure due to:

- inappropriate use of specific types of finance at key stages;
- failure to seek advice at critical stages (start-up, growth, cash flow problems); and
- inappropriate timing of finance injection.

Our research suggests that generally new business start-ups are most at risk. However high growth businesses and established businesses can also experience difficulties, especially if the business does not have access to financially qualified management. The main issues raised are:

- Confusion about the roles and services provided by support agencies in the region. Organisational changes in recent years have resulted in new organisations being created. SMEs do not understand the roles of Business Links, One NorthEast, Local Authorities or Small Business Service in assisting small businesses and require more clarity and improved sign-posting/referrals. As a result they are less likely to seek support at a time when they need it most;
- SMEs are not satisfied with the initial response rate and quality of relevant advice that they receive from public sector organisations and are reluctant to approach them again;
- SMEs have access to too much information (various web-sites, publications, newsletter) although they have an inability to identify what is most appropriate to them and how to use the finance to maximise the potential of the business;
- Reliance on traditional 'pecking order' of finance (own money, loans, overdrafts) due to insufficient time to research their finance options;
- Lack of financial awareness to recognise when external support is needed (banks, public and private sector support); and
- Poor timing in accessing finance. SMEs often raise finance internally (profits or friends and family) and spend this immediately on their business. This restricts their ability to raise further matched funding when they try to raise external finance from banks. Therefore knowledge and awareness is crucial in affecting financial decisions.

4.3.3 Business Support & Mentoring

The survey results highlighted that SMEs do consult Business Links (second most used source of advice) however they are more likely to contact them for advice on financial applications and to identify sources of finance for their business. They are more likely to be unhappy with the service that they received from Business Links with that provided by banks and professional advisors.

The key issues identified are:

- Confusion as to what is available and who to contact;
- Inconsistent and poor quality of service;
- Poor sign-posting;
- Lack of commercial and practical advice;
- Different products and services throughout the region;
- Lack of contacts throughout the region/ability to refer;

- Poor response rates and lack of proactive staff; and
- Poor value for money in addition to absolute cost.

Interviews and surveys revealed that in general SMEs are willing to pay for business support although they are likely to consider value for money in addition to total cost.

New business start-ups are less likely to use the services of a public or private sector support agency primarily due to cash flow shortages but also due to the plethora of agencies and confusion about what services are available.

The evidence suggests that small businesses are unlikely to pay for additional business support due to absolute cost considerations. Therefore attempts to improve the value for money of support services is unlikely to have a significant impact on small SMEs. Medium to large SMEs are more likely to take value for money into account.

Specific investment readiness issues, relating to venture capital, are discussed in section 4.4.1 below. However, business and managerial support in general has been outlined as a significant factor affecting the ability of SMEs to raise finance or use the most appropriate form of finance. Business support can be in many forms including:

- Assistance with business planning;
- Advice re funding options;
- Preparation of business plans;
- Marketing, strategic or product development advice; and
- Provision of business mentors or non-executive directors

SMEs consulted stated that they were willing and prepared to obtain external advice and support however an important barrier is how to obtain a good quality service. In other regions in the UK, initiatives targeted towards a specific business stage have been successful in encouraging businesses to seek advice and also in improving access to finance, especially when combined with specific finance provision.

4.3.4 Networking

Network associated issues have been raised by SMEs and intermediaries in the North East. There are currently very few opportunities to participate in region-wide networking to obtain information, develop markets and learn from recent mistakes or best practice.

- *Intermediaries* – interviews have suggested that there is currently insufficient communication and information sharing between the key finance and business support players in the region which may ultimately affect the quality of service provided to SMEs. For example, communication between banks and business links:
  - *Banks* - to communicate the current financial issues facing small businesses to ensure that Business Links are aware of

trends and problems, and referral of SMEs that can benefit from additional advice or support;

- *Business Links* – to update the banks on the services that they provide and alternative sources of finance.

- *SMEs* – interviews have indicated that informal and formal networks are a valuable source of information to benefit from best practice, share contacts, and improve general financial awareness. For example, regional start-up workshops have worked effectively to share knowledge, develop new markets amongst start-ups and share key regional contacts.

4.4 Supply-side Issues

4.4.1 Venture Capital

Several issues have been identified with regards to venture capital in the region which are discussed in turn:

- Choice and competition in the region;
- Equity gap in the North East;
- Knowledge and awareness – what is venture capital, when should it be used and when;
- Matched capital funding;
- Investment readiness of SMEs;
- Ongoing management and business support; and
- Cost of venture capital.

Choice and Competition in the Region

As outlined in Chapter 3, the North East venture capital market has declined in recent years and the exit of key players such as 3i has resulted in very few locally based venture capital providers. For a detailed analysis of the sources of finance for SMEs (equity, loans and grants) please refer to the separate financial mapping study commissioned by ONE, as discussed in Chapter 2.

Although several funds are available including the Regional Venture Capital Fund (RVCF), Capital North East and the North East Seed Capital Fund there is limited choice of venture capital provider. Northern Enterprise Limited (NEL) is the main player in the North East market and continues to be the only option for many SMEs in the region. In addition, the total amount of investment is capped, further restricting the value of total regional investments.

Competition is considered to be a necessary component of any regional financial structure and the lack of choice in the market place was the greatest concern amongst SMEs who had either used venture capital or considering using venture capital in the future. This is perceived to be a barrier to accessing venture capital by SMEs.

Interviews highlighted that new business start-ups are more likely to want to seek venture capital from a local source rather than a national source for many reasons including local contact, perception of increased understanding of the company, and response times. Therefore the lack of funding options may have an impact on business decisions to opt for venture capital finance.

Equity Gap in the North East

There is much debate about the size of the equity gap in the North East and the UK. The RVCF has an upper limit of £250,000 (although this can be extended to £500,000) and 3i typically invest upwards of £1 million although the closure of the North East branch has dramatically reduced their number of deals in the North East (see Chapter 3). Therefore, following discussion with finance providers, corporate financiers and SMEs in the region, the venture capital gap in the North East is today considered to be between £0.5 million and £2 million.

The survey analysis highlighted that the businesses that wanted to raise equity in the future required funding up to £1 million (starting at £30,000). Therefore, businesses in the North East are facing a future equity gap and the current limits of the RVCF are not sufficient to meet the gap in the market.

It is interesting to note that 3i are indirectly investing in deprived areas of North East via the new Bridges Community Development Venture Fund. This Fund can invest up to £2 million in a single business in a deprived area with high growth potential. As of September 2002 the Fund had not made any investments although it is expected to have a ten year life and have funds of £40 million. The Fund will expect to forge links with key partners in the region such as chartered accountancy practices, Business Links and venture capital providers although relationship development will be vital in attracting investment and levering additional finance.

There are also many eligibility criteria associated with this Fund, therefore this is not available to all businesses in the North East and is only available in specific locations.

Knowledge of Venture Capital

As discussed earlier, SMEs in general do not have an appropriate level of information and access to appropriate forms of advice to make informed financial decisions. This includes knowledge and awareness of general venture capital, the key benefits and disadvantages, how to access venture capital, requirements for applications and business plans, and when is the most appropriate time to use venture capital.

The North East has several venture capital funds each with a set of investment limits and eligibility criteria. Interviews highlighted that SMEs find it very difficult to understand what funds they can access and would prefer a smaller number of funds with more clarity about eligibility and investment limits.

It is vital that businesses have realistic expectations about venture capital and can meet the demands placed upon them by finance providers. For example, an equity provider will require an attractive exit route and this area is often not considered by small businesses.

Matched Capital Funding

Interviews with intermediaries raised the importance of matched capital requirements in attracting venture capital investment. They consider SMEs to be unable or unwilling to invest significant amounts in their business, which has a significant impact on the final decision to proceed with the investment.

However, SMEs do not always recognise the importance of having matched funding and will often invest their own finance first and then try to raise finance from a bank or venture capital provider, without having the resources to match any investment. SMEs are therefore considered to have insufficient knowledge about the expectations of investors and use of venture capital.

We have prepared a case study which considers the financial structure of five new business start-ups in the region (all less than 36 months old and considered to be average sized businesses). All businesses are seeking to raise additional forms of finance today and can therefore be considered to be growth businesses. These businesses have all raised significant levels of finance from private investors and own sources. However, they have not been able to access significant loan or venture capital finance in the region.

Appendix VII illustrates the combined funding structure of the five businesses (to preserve confidentiality of the businesses) with only 17% of total funding being provided by bank finance, nil from venture capital providers and 29% own finance. This highlights that businesses can provide match funding and can be successful in attracting private investors but traditional venture capital can be difficult to secure in the region.

Investment Readiness of SMEs

Poor investment readiness was stated as one of the main barriers affecting access to venture capital during interviews. This is both a regional and national issues and Entrust has been selected as one of six investment ready pilot schemes in the UK to improve SME performance in this area. Investment readiness is considered to reflect the business attitude to finance, quality of business documents and the general 'investability' of a project. i.e. does a business meet the requirements of a potential investor.

Investment readiness has demand and supply implications. A perceived lack of investment readiness may deter a business from applying for finance due to the expectation that they will be turned down. In addition, finance providers may restrict their investments if they are faced with a high number of inappropriate poorly produced plans that have an inherent high level of risk.

The survey responses suggest that SMEs face investment readiness issues as they do not appreciate the management input required in the venture capital process. For example, a selection of SMEs surveyed and interviewed stated that barriers to accessing venture capital included a lack of time to complete application forms and lack of internal expertise to develop the business.

In the region, investment readiness was considered to be a greater issue for new business start-ups. The key issues are:

- Lack of strategic focus;
- Poor business planning;
- Poor cashflow forecasts;
- Inappropriate management structure; and
- Reluctance to part with equity in their business.

This may reflect the low level of business support received at the start-up phase which may be attributable to the cash-flow position and financial difficulties faced by businesses during the first 3 years of business and also the confusion re support service provision.

However, value for money in business support services provided was highlighted as the key factor in determining the use of external support. This indicates that the quality of advice is crucial and also suggests that businesses are willing to seek external advice, and are willing to pay for such services.

Ongoing Management and Business Support

In addition to investment readiness, SMEs also strongly support the input of medium term managerial advice to accompany financial investments. The evidence from interviews would suggest that in the past venture capital investments have focused on production of the business plan, forecasting and the financial injection stage. However, very little practical support and guidance has been provided following finance injection. Businesses would prefer to have a more integrated approach and would like to see finance provision accompanied by managerial support and mentoring (the later being independent from the finance provider).

Businesses perceive the key benefits of this process to be risk reduction (beneficial to finance provider and to the company in helping to lever additional sources of finance) and independent advice (without fear of investor intervention as is perceived to be the case with non-executive directors).

Cost of Venture Capital

The administration costs associated with venture capital are often prohibitive to small scale investments. The legal, administration and due diligence costs of a large investment of say £2 million and a small investment of £100,000 are very similar. This acts as a significant barrier to small businesses that cannot afford the additional costs of venture capital.

Venture Capital Summary

Overall, the evidence suggests that in the future, small businesses in the North East will be trying to raise equity finance. However, there are several issues that cause concern to equity providers and SMEs alike that currently prevent the market from operating at its maximum strength such as imperfect information and investment readiness weaknesses which increases the level of inherent risk in a potential investment.

4.4.2 Bank Finance

The survey evidence clearly highlights the important role of banks to SMEs with a significant proportion of SMEs not only using banks as their first point of call for financial advice but also as their main source of finance (behind own funding).

Banks tend to have more contact with SMEs than any other external organisation and can have a significant impact upon their business. Therefore, the relationship between banks, other financial and business support organisations, and public sector organisations is therefore crucial in improving access to finance.

On the whole, SMEs rate the quality of the service that they receive from banks to be satisfactory, with one of the highest ratings of all service providers in our survey. During interviews, smaller SME were more likely to be dissatisfied with their bank than larger SMEs. This is primarily due to difficulties with loan and overdraft provision. Several issues have been raised as part of out research that have a significant impact upon the start-up, growth, and survival of banks in the region.

- **Key Issues:**

  Risk Averse Nature of Banks

  Banks are profit making organisations and will therefore not engage in high levels of risk. This is to be expected given that banks have a responsibility to maximise long term shareholder wealth above all other objectives. However, SMEs interviewed and surveyed considered banks to be too risk averse and reluctant to offer loans (at all levels).

  Therefore there is a perceived gap in the market for loan provision. This is turn is considered to have knock-on effects on the ability of SMEs to lever additional sources of finance and further compounds the difficulty for SMEs. This applies to all stages of a business (start-up, established and growth) however start-ups and very small businesses face more acute problems in accessing loan finance (see below).

  Financiers interviewed do not believe that the region faces a specific problem re loan provision and stated that applications are assessed individually and decisions will ultimately be based upon their internal risk assessment procedures. This represents an expectation gap between the needs of SMEs and the services provided by banks in the region.

  The finance structure for a sample of five recent start-ups in the region (Appendix VII) has been reviewed to identify the key sources of finances and identify emerging financial trends. Of the total finance raised of £2 million, only 17% related to bank finance (including the SFLGS). This indicates a relatively low level of bank finance and reliance upon alternative sources of finance. See Appendix VII for an analysis of the funding structure. The ability of SMEs to access finance from banks is likely to change in the future to reflect the Brumark case (as discussed above).

Quality of Service and Cost

As with Business Links, the quality of service provided by banks varies considerably and is often dependent upon individual bank managers. Of the SMEs interviewed, approximately half had changed banks since start-up due to unsatisfactory finance provision or high costs of services.

Security Requirements

SMEs interviewed and surveyed believe that banks require significant levels of security and often insist that individual homes be used as security. SMEs consider banks to be too inflexible with regards to security requirements and do not take individual circumstances into account. e.g. personal guarantees. New business start-ups or small businesses from disadvantaged areas face further difficulties in that they may not have a home that they can use as security and so cannot access finance (typical finance required for small businesses is less than £20,000). Again, given that the objective of most banks is to maximise shareholder wealth and generate profits, banks are more likely to finance established businesses as opposed to new business start-ups.

Traditionally banks have relied upon tangible assets for security and to assess business risk. New business start-ups and very small businesses tend to have an unattractive balance sheet and have faced barriers in accessing loan finance. This also applies to businesses in the service sector or software sector who have low level of tangible assets (perhaps due to a high level of intellectual property) and are immediately turned down for traditional loan finance.

Trading Record Requirements for Loan Finance

New start-ups in the region have faced difficulties in accessing loan finance due to a lack of trading history. SMEs believe that banks can be unsupportive of new businesses and inflexible in their risk assessment.

Inflexible Finance Options

The most important business issue affecting new business start-ups is cash flow with SMEs (interviewed and surveyed) highlighting cashflow or working capital requirements as their main reason for obtaining finance. However, SMEs do not consider the range of finance options to be most appropriate at the start-up and inflexible given cash flow requirements during the first three years. For example, repayment holidays and more flexible overdraft facilities were considered to be beneficial for start-ups.

In addition, SMEs expressed that they would like banks to either advise them or refer them to advisors that can make a difference to their business and assist in areas such as cash flow management, accountancy support and planning, especially at start-up stage. They consider that such support will ultimately improve their business and reduce the inherent risk of their business to the bank.

Banks Summary

Overall, SMEs are satisfied with the level of service that they receive from banks and continue to use banks for most of their financial needs and advice.

However, the research suggests that some SMEs face difficulties in obtaining loans to use for matched funding opportunities or for business start-ups – most noticeably new business start-ups and very small businesses.

Small businesses in general face more difficulties in accessing relatively small amounts of finance (less than £20,000) due to the low levels of security, low turnover and the often life style nature of the business.

SMEs would prefer banks to advise/refer them to appropriate and relevant business support services that would improve their business and ultimately reduce the risk of any loan finance to the bank.

4.4.3 Other Finance

The financial mapping study commissioned by ONE will highlight the range of other finance options available to SMEs in the North East. This section explores some of the issues identified as part of our research with regards to other forms of finance most commonly used by SMEs.

Regional Loan Funds

The North East had two regional loan funds, the North East Regional Investment Fund (NERIF) I and II which were both gap funders and operated successively. NERIF II has now closed. The majority of support was provided as loan finance. The average deal size of NERIF II was approximately £40,000 (upper limit was £100,000) compared to the upper limit for NERIF I of £250,000. Both Funds experienced a very high level of demand which ultimately resulted in the lower maximum limit for NERIF II

NERIF has been used by several SMEs consulted and is considered to be an essential part of the finance framework in the North East. Many SMEs also stated that there is now a gap in the market place given the closure of NERIF II. Although plans are underway to negotiate the next stage of NERIF III, the delay in implementation has resulted in a gap in the provision of loan finance for SMEs up to £100,000. This gap further restricts the ability of SMEs in the region to lever additional sources of finance.

NERIF I experienced several recent bad debts. The evidence from our research would strongly suggest that given the average investment of the Fund, additional business support (as outlined above) would be valuable to improving the performance of businesses and reducing the overall risk of the investment to the Fund.

The evidence indicates that SMEs in the North East have a demand for loan finance and plan to raise loan finance in the next two years. The difficulties that SMEs face in obtaining matched funding from banks would also suggest that growing importance of NERIF III in helping to stimulate further investment into the region for business start-up and growth.

Seed Capital

Spin-outs from the higher education sector traditionally rely on local sources of finance for new ventures. The main source of investment for such ventures in the region is the North East Seed Capital Fund, although the number of investments is comparatively low compared to other regions in the UK. The low number of spin-outs has implications for the long term SME base and regional economic growth. They are important sources of high growth businesses and create employment opportunities.

There are many difficulties in creating and generating successful spin-outs from the higher education sector including the ability of academics to run a business and become ‘technology translators’. This requires a significant investment in improving the investment readiness of new businesses to sustain a new business and encourage growth.

Credit Cards/Directors Pay

The survey results state that a high percentage of SMEs rely on credit cards as a source of finance. This mainly relates to very small businesses that cannot obtain finance from other sources and new business start-ups. This further raises concerns about the ability of such businesses to raise traditional micro finance in the North East.

Almost half of SMEs interviewed did not currently pay their directors a salary due to cash flow difficulties and an inability to obtain traditional forms of finance. Again, given the relatively low amounts involved, this indicates difficulties for SMEs in the North East to raise micro finance.

Grants

Our research suggests that businesses are becoming less dependent upon grants as a main source of finance. Over the next two years, more businesses are seeking to raise grant finance than any other form of finance (see table xx) although this is mainly for training purposes and not for start-up or growth purposes.

At the start-up stage, business grants are very important for new premises, staff training and IT support and can assist in providing the business with a ‘kick-start’. However, this is considered to be part of an integrated financial package and businesses do not expect to be funded by grants alone.

Although the information on grant finance is considered to be poor and SMEs would like better information on grants, grant finance was not specifically raised as a significant issue for SMEs.

The Small Firms Loan Guarantee Scheme (SFLGS)

The SFLGS was used by a wide range of businesses interviewed and was considered to be a valuable source of finance and enabled many businesses to start-up (it is last resort finance).

However, in the year to 31 March 2001, the North East received less than 3% of the UK total, highlighting its relatively low usage in the North East. The SFLGS is mainly used as part of a financial package (average loan size to year ending March 2002 was £59,660) and is an important source of finance to levering additional finance. However there are several issues associated with the loan scheme including:

- Varying participation by banks in the scheme (predominantly related to individual bank managers);
- SME perception that banks are reluctant to market the scheme;
- Complicated application process;
- Low value of total loans in the North East;
- Restrictive criteria for application – not applicable to all sectors; and
- Financial limits are too low and have not kept pace with business development.

Other Loans

The ONE financial mapping study will provide an analysis of the finance options available to SMEs in the North East. An important source of finance for new business start-ups is the Princes Trust that operates throughout the UK and, amongst other forms of support, can provide loan finance for up to £5,000. However, it is important to note that this finance is only provided for individuals between 16 and 30 years old and will provide finance for individuals who have been unable to obtain finance via conventional means. Therefore, although providers of micro finance exist in the North East that have been successful in developing new business start-ups and stimulating entrepreneurial development, the evidence suggests that micro finance provision remains insufficient to meet the needs of SMEs in the region.

4.5 Summary

A wide range of demand and supply side issues have been identified. SMEs and intermediaries in the region have strongly indicated that one of the most significant issues that they face is in ability to obtain an integrated service (in the public and private sector) that meets their key financial needs whilst addressing their key business issues or weaknesses. i.e. finance matched with appropriate business support to overcome inherent high risks associated with their business such as poor business planning, funding structure, strategy management or marketing.

Traditionally, initiatives have been developed that address a demand or a supply side issue, but they fail to take into account the impact of an integrated approach. The most successful initiatives have developed a financial package with business support to improve success rates and maximise investment returns.

5. THE WAY FORWARD

This section outlines our key access to finance recommendations for the short, medium and long term, and outlines the key next steps for the Regional Expert Finance Group.

5.1 Introduction

The evidence suggests that the North East faces a wide range of access to finance issues for new business start-ups and growing businesses. Perhaps one of the strongest messages to emerge from the study is the requirement for a greater degree of integration of initiatives to support SMEs to help them to start, grow and survive. In addition, it is important to recognise the need for programmes that will stimulate sustainable growth for SMEs in the North East and provide a framework for long term success.It is often easier and quicker to focus upon short term supply-side initiatives to try and achieve a 'quick fix' and demonstrate progress in improving access to finance. The evidence from this study indicates that longer-term integrated solutions are required that aim to:

- improve business performance and competitiveness;
- improve quality and quantity of new business start-ups;
- improve business survival; and
- maximise business growth.

5.2 Initiatives

5.2.1 Operation of NERIF III

As outlined in Chapter 4, SMEs in the region consider NERIF (North East Regional Investment Fund) to be a key component of the financial framework in the North East. The closure of NERIF II at the end of October 2001 has affected the ability of SMEs in the region to raise loan finance resulting in a noticeable gap in finance provision. There is considerable uncertainty amongst SMEs in the region as to the future operation of similar funds given the stop-start nature of the funding streams to date. SMEs interviewed and surveyed believe that loan finance will play a crucial role in their operational and expansion plans in the short and medium term.

As a priority, immediate steps should be taken to finalise the plans for NERIF III. We understand that several technical and operational difficulties have arisen which are in the process of being resolved, most importantly the increased level of bad debts in NERIF I which has implications for the NERIF III financial model. Steps to address this issue are discussed below.

We understand that an option being considered for NERIF III is a quasi equity model which has a loan fund with an option to convert into equity (quasi equity has a higher intervention rate). This delivers a financial model with an upside potential which may be more attractive to private investors. The flexibility of this model would address some of the key concerns of

SMEs in the region regarding the lack of choice and flexibility of finance in the region.

The ERDF implications of this financial model are currently being considered to ensure that all directives are complied and to determine the acceptable rate of intervention. The ERDF implications of associated management costs are also being reviewed to explore the option to make separate ERDF applications for the management cost and fund value. This has the benefit of maximising the total value of the fund. The North East and other regions in the UK have traditionally made one application for the fund value inclusive of management costs which has restricted the total value of loans. This would make a significant difference to the total loan fund in the region.

We suggest that steps may be taken to mitigate against the risk of bad debts by providing a support programme to accompany NERIF III. Support will obviously be subject to de minimis limits and maximum intervention rates. Other regions in the UK, such as Merseyside, Wales and South Yorkshire have introduced a management support programme with finance to try to improve the survival rates of new businesses and maximise the growth potential of existing businesses. See business support section below which includes examples of specific steps to help to achieve this and the ERDF implications.

This is short-term measure due to the requirement to address the current gap, however due to the expected life of fund, the impact will be medium term and will require ongoing assessment over the life of the Fund.

5.2.2 Integrated Support Package for New Business Start-ups and High Growth Businesses

The evidence suggests that new business start-ups face more difficulties in accessing finance than any other group of business. However, there are many layers of start-ups including life-style businesses, standard business start-up with some growth potential and high growth business start-ups. The evidences suggest that life-style and high growth business start-ups face the most acute difficulties. High growth established businesses also experience difficulty in raising finance predominantly due to the limited venture capital options in the North East and the lack of investment readiness of these businesses.

There are many factors that affect a businesses ability to obtain finance which have been discussed in Chapter 4, such as an inability to raise matched capital, lack of financial and business support information, requirement for personal guarantees, lack of trading history and assets, and poor investment readiness. Many of these factors increase the risk of any business to a potential finance provider.

Therefore it is important to have an integrated business support and financial package to address the barriers in the market place and provide a mechanism to minimise the risk associated with investing in the most disadvantaged new start-ups and high growth businesses.

An integrated package can include:

- A region-wide approach. e.g. North East High Business Growth Start-up Programme;
- Accessed by current Business Links throughout the region with sign-posting;
- Loan provision to meet identified financial gaps. e.g. for small businesses up to £20,000, high growth start-ups up to £250,000, mezzanine packages to suit funding structure of high growth businesses;
- Venture capital fund opportunities for high business growth start-ups and growth businesses;
- Subsidisation of venture capital costs (due diligence and legal) for high growth business start-ups to reflect the high absolute costs of venture capital transaction relative to small investments;
- Investment readiness programme for high growth business start-ups and growth businesses, and business support and mentoring for small businesses;
- New business start-up workshops/road shows to encourage new start-ups, share information and best practice.

Such an approach can be combined with regional entrepreneurial initiatives that are taking place as part of the Regional Enterprise Strategy to encourage new business development.

This is a long-term solution to address many of the key business start-up issues and can not be introduced in the short-term due to the degree of interaction required with a wide range of initiatives. This will require a large degree of central co-ordination however the overall expected benefits in terms of risk reduction, survival of businesses and improved level of new business start-ups will greatly contribute towards realising the regions vision contained within '*Realising Our Potential*'.

Other Objective One areas that have introduced such an integrated package have greater intervention rates than Objective Two areas. This would require a greater degree of private sector support which is currently an issue for the region, especially given the negotiations to secure NERIF III. The development of an integrated solution will require short and medium term discussion with the private sector to develop matched funding opportunities.

In providing training and addressing business support needs, various ERDF intervention rates will apply. New business start-ups are more likely to require generic assistance rather then sector specific help. e.g. business planning or accountancy. Therefore higher rates of intervention can be applied to maximise total eligible support to SMEs.

5.2.3 Micro Loan Provision for Small Businesses

The evidence suggests that small businesses today in the North East are facing difficulties in accessing relatively small amounts of flexible finance as evidenced by the high use of overdrafts, credit cards and non payment to directors.

Therefore a flexible regional micro loan fund would provide a short and medium term solution to help address some of the basic needs of SMEs. Flexible finance can incorporate holiday repayments, shorter-term loans (of say 6 months to meet working capital requirements).

Generic business support to accompany the loan fund would be valuable in providing advice on cash flow planning, business planning, and sources of information, training and applications. This would help in improving the survival rates of small businesses by helping to resolve basic financial issues that affect businesses ability to control cash flow. Risk reduction is an essential component of an integrated micro loan package and is required to attract private sector investment as match funding against ERDF finance.

This is relatively short and medium term solution to address current needs and should be monitored and evaluated regularly to determine the success and demand for the fund and the applicability of criteria and limits.

5.2.4 Multi-product Fund

A multi-product fund can be developed which incorporates several funding packages and business support initiatives under one umbrella structure. For example, the Merseyside Special Investment Fund has three separate pots of funding – Small Firms Fund, Mezzanine Fund and the Venture Fund. The Fund adopts a 'Money with Management' approach.

We consider a business life cycle multi-product package is best suited to the needs of the North East today given the access to finance issues facing small businesses, high growth business start-ups and high growth businesses.

However, this is a long-term strategy and cannot be implemented within a short time period. Therefore, prior to any multi-product fund being introduced, the current market conditions must be considered to ensure that the access to finance issues remain valid.

5.2.5 Business Support

SMEs traditionally rely on banks for business advice however this is mainly to obtain information about finance options. However SMEs also need good quality business advice and support that help them to make the right decisions and maximise the opportunities for their business.

Our research has indicated that SMEs are prepared to pay for support services if they provide value for money. Private sector service providers have been recognised as providing good value for money and have more extensive networks to access finance than public sector support.

However there are also economy of scale considerations and businesses will not pay a high absolute amount if they do not identify short-term tangible benefits to the business.

Taking into account our research findings our key recommendations are:

- Business Links should focus upon providing those services it is best placed to deliver. It should act as a sign-posting agent to other organisations to ensure that businesses receive the best quality advice.

  Typical comments include, '..*Business Links should stick to life style and small businesses and refer larger businesses with specific technical requirements to other organisations*'.

  Improved sign-posting is considered essential in helping SMEs understand the plethora of support agencies (public and private). For example, Business Links in other areas in the UK have developed a matrix of consultants/agencies including specific skills and services that they provide. This has led to improved sign-posting and the provision of advice by those individuals that are best placed to do so.

- Improved advertising and networking of Business Links

  A national marketing campaign is underway however SMEs remain confused about the services that they provide. Improved relationships with banks and other finance providers will also maximise referral opportunities.

- Business mentor/Non executive directors database

  SMEs in the region would like to have more access to business mentors and non-executive directors who can provide valuable advice and support to a business. They can also act as role models to the region or sector.

  It is often difficult to access a suitable person to act as mentor/non-executive director despite national measures to improve information provision. Therefore a more co-ordinated regional effort to develop a database would not only provide assistance to potentially improve survival rates, but can also be integrated with the wider regional entrepreneurial development programme to maximise private sector involvement.

The provision of an integrated business support package using public and private sector organisation can significantly reduce the risk of businesses and further stimulate the private sector finance market in the long term. However it is reliant upon cost subsidisation for the delivery of services as some SMEs will not be willing or able to pay. Soft aid is eligible for attractive intervention rates however it is reliant upon the beneficiary contributing towards the total cost of the service out of reserves of other financial sources.

Therefore, this service will generally be taken up by non-life styles businesses that want to expand or improve profitability. This will also maximise the contribution to the local economy.

Improving business support provision requires a long-term strategy although immediate steps can and should be taken to address some of the weaknesses. The key messages are integration and co-ordination. Business support and investment readiness should be considered to be vital steps towards business growth and improving access to appropriate finance.

5.2.6 SME Networking

Research at a national level suggests that networking is a crucial determining factor in achieving sustainable SME growth. Our consultation programme highlighted that past network events such as start-up business clubs have been very valuable in facilitating information sharing, best practice, developing markets, accessing finance and promoting an entrepreneurial or growth culture. However, SMEs do not believe that there are a sufficient number of good quality regional SME networking opportunities. Specifically, they require events that focus upon:

- Finance needs at key business stages for new start-ups and growth businesses; and
- Specific topics for established businesses such as training, cash flow management, applications for finance, and supply chain development.

Network development is an issue that can be tackled in the short term however it is an ongoing issue and should be part of a longer-term strategy.

5.2.7 Development of Regional Access to Finance Relationships

Communication between the key financial and business support providers can be strengthened to improve the overall quality of advice provided to SMEs in the region. Banks are most often used as a source of advice by SMEs and therefore are very influential in shaping the small business economic base.

As discussed above, private sector business support organisations are highly rated by SMEs in the region with one of the key differences being their ability to 'open doors' and introduce a wide range of finance providers. Public sector organisations should work alongside the private sector to extend their network base.

Such interaction of the public and private sector is crucial if a sustainable strong access to finance climate is to be developed for the North East.

This is a short-term measure that can be explored within the next six months however it is an issue that will require continuous effort by key players in the North East and a central co-ordination by a lead partner such as the small business service.

5.2.8 Entrepreneurial Development

A long term strategy is required to develop programmes to address the low level of entrepreneurial development in the region. We are aware that an entrepreneurial strategy (Everybody's Business) has been developed and that entrepreneurial development is one the most important issues being addressed as part of the Regional Economic Strategy.

Therefore, the programmes to address entrepreneurial development should also ensure that some of the issues raised within this report, including knowledge and awareness of finance, role model development and a robust business support network, are taken into account.

Short-term steps can be taken to address entrepreneurial development however a longer-term strategy is required to maximise success.

5.2.9 Summary

Several initiatives have been recommended to help to address some of the key issues facing SMEs in the North East today. Table 2 below summarises the short, medium and long term initiatives to provide a focus for action plan development. The table illustrates that steps can be taken in the short term to help address some of issues, however many of the recommendations require a long-term strategy.

Table 2: Implementation of Initiatives

	Short Term	Medium Term	Long Term
NERIF III Introduction			
NERIF III Business Support Package			
New Business Start-up Business Support Package			
High Growth Business Support Package			
Micro Loan Package			
Network Development			
Relationship Development			
Business Support Development			
Entrepreneurial Development Programmes			

It is important that a detailed action plan is developed to set out the steps required to address the key SME access to finance issues including the roles and responsibilities of key partners.

The timing of the introduction of these recommendations is an important consideration as future actions must take into account the current market dynamics and SME concerns. In Chapter 2, long term initiatives are considered to be capable of implementation after a period of 18 months. It is interesting to note that NERIF took approximately five years to implement and a delay on this scale would jeopardise the validity of these results and growth of the North East.

5.3 Next Steps

Several initiatives have been outlined above which address the key access to finance issues affecting SME development today. Some of the initiatives require ERDF support however several initiatives require greater co-ordination at a regional level to try to improve the interaction of the public and private sector.

The Regional Finance Expert Group is responsible for overseeing the access to finance regional strategy and agreeing the action plan to address the key issues. This is the next important stage for the Expert Group. In addition, the Expert Group can also play an important role in trying to influence national policy. The table below highlights the key issues that do not necessarily have a regional focus or can only be addressed at a national level. The Expert Group is considered to be best placed to consider these issues and influence key decision makers to address some of the key issues.

Table 3: National Access to Finance Issues

Key Area	Issues
Entrepreneurial Activity	Employee culture rather than entrepreneurial culture Few perceived benefits of owning a business
SFLGS	Perception of poor participation by banks Upper Limits are too low Not all sectors included
Innovation	Lack of business support for technical innovation
Banking Sector	Reliance on tangible assets as security Remain risk averse
Business Support	Message is not clear re roles, services and access - RDA, SBS & BL
Grant Regime	Too many separate 'pots of finance' Time consuming application process Cash flow implications of grant payments to new start-ups

6. APPENDIX I – LIST OF CONSULTEES (INTERMEDIARIES)

Dan Brophy	Business Link
Alistair Conn	Northern Venture Managers
Ray Crowe	GONE
Barrie Hensby	Northern Enterprise Limited
Garry Lumby	Yorkshire Bank
Robert Marris	Entrust
Neil Mundy	ONE
Martin Pallet	Yorkshire Bank

7. APPENDIX II – PROJECT STEERING GROUP MEMBERS

Ian Bolton	ONE
Karl Gardiner	ONE
Kay Goodinson	GONE
Mike Hawkins	ONE
Chris Hope	NEL
Robert Marris	Entrust
Paul McEldon	Business Innovation Centre
Neil McGuinness	GONE
Neil Mundy	ONE
Keith Raine	GONE
David Slater	GONE

8. APPENDIX III – FINANCE EXPERT GROUP MEMBERS

Neville Bearpark	Upton Nichol and Williams
Ian Bolton	ONE
Dan Brophy	Business Link Tyne and Wear
Sir David Chapman	Laing and Cruickshank
Joe Docherty	Tees Valley Urban Regeneration Company
Anthony Douglas	Business Innovation Group
Mark Ford	Barclays Bank
Karl Gardiner	ONE
Kay Goodinson	GONE
Mike Hawkins	GONE
Chris Hope	NEL
Robert Marris	Entrust
Neil McGuinness	GONE
Neil Mundy	ONE
David Park	Small Business Service
David Slater	GONE

9. APPENDIX IV – VAT BUSINESS INFORMATION

Table 4: Business VAT Registration Rates by Region

Region	2000 No. of Registrations ('000)	2000 Total Stock ('000)	2000 Registration Rate	2001 No. of Registrations ('000)	2001 Total Stock ('000)	2001 Registration Rate	2000-2001 Change in Stock
North East	**4.3**	**42**	**10.2%**	**4.1**	**41.9**	**9.8%**	**-0.1**
West Midlands	14.5	136.8	10.6%	14.2	137.8	10.3%	1
North West	18.5	161.8	11.4%	17.6	163.2	10.8%	1.4
East Midlands	12.0	111.1	10.8%	11.6	111.9	10.4%	0.8
Y & H	12.0	116.3	10.3%	11.7	116.5	10.0%	0.2
London	37.9	277.2	13.7%	34.9	280	12.5%	2.8
South East	29.2	257.4	11.3%	28.4	261.3	10.9%	3.9
South West	15.4	149.8	10.3%	14.5	150.6	9.6%	0.8
East of England	18.4	164.2	11.2%	17.4	165.2	10.5%	1
Wales	6.2	74.3	8.3%	6.0	74.40	8.1%	0.1
Scot	11.4	118.7	9.6%	11.5	119.50	9.6%	0.8
NI	3.4	54.9	6.2%	3.6	55.10	6.5%	0.2
Average UK	**183.2**	**1664.5**	**11.0%**	**175.5**	**1677.4**	**10.5%**	**12.9**

Table 5: Business VAT De-registration Rates by Region

Region	2000 No. of Deregistr'ns ('000)	2000 Total Stock ('000)	2000 Deregistr'n Rate	2001 No. of Deregistr'ns ('000)	2001 Total Stock ('000)	2001 Degistr'n Rate	2000-2001 Change in Stock
North East	**4.2**	**42**	**10.0%**	**4.2**	**41.9**	**10.0%**	**-0.1**
West Midlands	14.2	136.8	10.4%	13.2	137.8	9.6%	1
North West	17.7	161.8	10.9%	16.2	163.2	9.9%	1.4
East Midlands	11.9	111.1	10.7%	10.8	111.9	9.7%	0.8
Y & H	12.8	116.3	11.0%	11.5	116.5	9.9%	0.2
London	35.2	277.2	12.7%	32.2	280	11.5%	2.8
South East	27.3	257.4	10.6%	24.6	261.3	9.4%	3.9
South West	15.5	149.8	10.3%	13.7	150.6	9.1%	0.8
East of England	17.5	164.2	10.7%	16.4	165.2	9.9%	1
Wales	6.4	74.3	8.6%	5.9	74.40	7.9%	0.1
Scot	11.3	118.7	9.5%	10.7	119.50	9.0%	0.8
NI	3.1	54.9	5.6%	3.4	55.10	6.2%	0.2
Average UK	**177.1**	**1664.5**	**10.6%**	**162.8**	**1677.4**	**9.7%**	**12.9**

Source: Small Business Service 2002

10. APPENDIX V – BANK OF ENGLAND QUARTERLY BUSINESS STATISTICS

Table 6: Business Start-ups by Postcode area 2001

Bottom Ten Postcodes outside of London	
Postal Area	**New Business Starts***
Newcastle upon Tyne	**7**
Romford	7
Middlesborough	**7**
Warrington	7
Watford	7
Wakefield	7
Wigan	7
Durham	**6**
Liverpool	6
Sunderland	**4**
No 1 outside London - St Albans	**16**

* per 1,000 population aged 16-59 outside of London

Source: Bank of England Quarterly Report July 2002

Table 7: Liquidations and Business Bankruptcies by Region

Region	2001	Half Year 2002
North East	**4,724**	**2,731**
London	5,087	2,865
South East	7,075	3,943
South West	4,345	2,403
Eastern	1,992	950
East Midlands	2,408	1,137
West Midlands	2,322	1,873
North West	4,724	2,476
Wales	1,578	847
Scotland	4,519	2,593
Total	**40,532**	**21,818**

Source: Bank of England Quarterly Report July 2002

11. APPENDIX VI – QUESTIONNAIRE

ACCESS TO BUSINESS FINANCE

This questionnaire will take approximately 10 minutes to complete.

Please note this information is totally confidential and will not be released to any third parties.

PART A RAISING OF BUSINESS FINANCE

Q1: Have you ever considered applying for finance for your business but chose not to proceed with an application because you felt it would be rejected?

Yes θ

No θ

If yes, please give details
……
……
……

Q2: Please ✓ which of the following sources of finance you have used, tried to use or are aware of.

	Used	Aware of	Tried
Bank overdraft	θ	θ	θ
Bank short-term loan (up to 5 Yrs)	θ	θ	θ
Bank medium or long-term loan (more than 5 years)	θ	θ	θ
Credit card	θ	θ	θ
Leasing	θ	θ	θ
Hire purchase	θ	θ	θ
Commercial mortgage	θ	θ	θ
Invoice discounting/Factoring	θ	θ	θ
Equity finance from private investors	θ	θ	θ
Equity finance from institutional investors	θ	θ	θ
Business angel	θ	θ	θ
Residential re-mortgage for cash injection	θ	θ	θ
Business grants	θ	θ	θ
Own money/Family	θ	θ	θ
Alternative Investment Market	θ	θ	θ
Other sources, please specify....................................……...	θ	θ	θ

Q3: **a) Over the past two years, have you <u>tried</u> to raise these forms of finance?** **(Please circle Y / N)**
b) If you have, please indicate the amount you were trying to raise.
c) If you were ultimately <u>successful</u> in raising this finance, please tick.
d) If successful, how much did you actually succeed in raising? *(if different to b)*

Source of Finance	**a) Tried to Raise**	**b) Amount £ 000**	**c) Successful In Raising**	**d) Amount £ 000**
Bank overdraft (Including Renewed)	Y/N	…….	θ	…….
Bank short-term loan (up to 5 Yrs)	Y/N	…….	θ	…….
Bank medium or long-term loan (more than 5 years)	Y/N	…….	θ	…….
Credit card	Y/N	…….	θ	…….
Leasing	Y/N	…….	θ	…….
Hire purchase	Y/N	…….	θ	…….
Commercial mortgage	Y/N	…….	θ	…….
Invoice discounting/Factoring	Y/N	…….	θ	…….
Equity finance from private investors	Y/N	…….	θ	…….
Business angel	Y/N	…….	θ	…….
Equity finance from institutional investors	Y/N	…….	θ	…….
Residential re-mortgage for cash injection	Y/N	…….	θ	…….
Business grants	Y/N	…….	θ	…….
Alternative Investment Market	Y/N	…….	θ	…….
Other sources, please specify..............………….………....	Y/N	…….	θ	…….

Q4: **For what application(s) were the funds required? (✓)**

Working capital	θ
Fixed asset purchases	θ
Business acquisitions	θ
New product or service development	θ
Market development	θ
Funding losses	θ
Training programmes	θ
Restructuring/Reorganising the business	θ
Other reasons, please specify...….........	θ

Q5: **Who makes the key financial decisions inside your organisation/business?**

Owner	θ
Finance Director	θ
Internal Accountant	θ
Other 'Financially Aware' senior management	θ

Other, please specify........................……………………………........	θ
No-One	θ

Q6: Please indicate the level of business/financial qualifications they hold:

Qualifications Coding

Where: *1 = Professional Accountancy*
2 = Degree in Business Studies
3 = Other Business or Finance qualification
4 = Degree
5 = None of these

	Qualifications (1-5)
Owner	θ
Finance Director	θ
Internal Accountant	θ
Other 'Financially Aware' senior management	θ
Other, please specify..................……………………………...	θ

Q7: Have you ever considered raising equity finance ? (✓ or 5)

Yes θ

No θ

If no, would you like to know more about this option? Yes θ

No O

If yes:

(a) How did you find out about this form of finance?

……...………

………………..……………………………..………………………………………………………………………………………..

(b) How much did you wish to raise? £…………..

(c) Were you successful?

Yes θ

No θ

(d) Did you experience any problems?

….……..

….……..

….……..

…….

Q8: Do you use an overdraft as a long-term source of finance for your business? (✓)

Yes θ

No θ

If yes, have you considered alternative means of financing this debt?

……………………………………………………………………..………………………………………………………………...…

…….

Q9: How satisfied would you say you were overall with:

a) the application process for the finance?
b) information on loans, grants and equity?
c) identifying appropriate sources of finance available?

	a) Application Process	b) Information on: loans	grants	equity	c) Source of Finance
Not at All Satisfied	θ	θ	θ	θ	θ
Quite Satisfied	θ	θ	θ	θ	θ
Satisfied	θ	θ	θ	θ	θ
Highly Satisfied	θ	θ	θ	θ	θ

Q10: If you experienced specific problems above, please describe the main issues.

1 ……………………………………………………………………………………………………

……………………………………………………………………………………………………

2 ……………………………………………………………………………………………………

……………………………………………………………………………………………………

3 ……………………………………………………………………………………………………

……………………………………………………………………………………………………

Q11: If you were unsuccessful in raising finance, why do you feel that you did not succeed?

1 ……………………………………………………………………………………………………

……………………………………………………………………………………………………

2 ……………………………………………………………………………………………………

……………………………………………………………………………………………………

3 ……………………………………………………………………………………………………

……………………………………………………………………………………………………

Q12: Who is/are your main contact(s) for advice on sources of finance?

Source of Advice

Please rank from 1-3 with 1 being the first choice (if only one source use, rank 1 only)

Banks – please state which …………………………………………	θ
Professional Advisors – please indicate which	
1……………………………………………..	θ
2 …………………………………………….	θ
Internal management/owner	θ
Business Links	θ
Small Business Service	θ

Chamber of Commerce	θ
Regional Development Agency	θ
Trade association	θ
Venture capital firm	θ
Other, please specify	
1 ………..........…..………………...................	θ
2 …………………………………………...	θ

Q13: Please indicate which <u>External Agencies</u> you have contacted for financial advice about raising funds over the past 2 years.

Please indicate:

a) How satisfied you were with the way in your enquiry was handled?
b) How satisfied you were with the speed of response?
c) How satisfied you were with the quality of advice given?

Where: 1 = Not al All Satisfied, 2 = Quite Satisfied, 3 = Satisfied, 4 = Highly Satisfied

Source of Advice	**a) Contacted (Tick)**	**b) Enquiry (Rate 1-4)**	**c) Speed (Rate 1-4)**	**Advice (Rate 1-4)**
Banks - please indicate which.........................…..........……...	θ	θ	θ	θ
Professional Advisors – please indicate which ………………………………………………………..…….	θ	θ	θ	θ
Business Link	θ	θ	θ	θ
Small Business Service	θ	θ	θ	θ
Chamber of Commerce	θ	θ	θ	θ
Regional Development Agency	θ	θ	θ	θ
Trade Association	θ	θ	θ	θ
Other, please specify ....……………….................…….	θ	θ	θ	θ
None of These	θ			
Not Sure	θ			

Q14: Typically, in what area(s) was advice sought? (✓)

Financial and business planning	θ
Sources of finance	θ
Assistance with finance application	θ
Product development	θ
Asset purchase/sale	θ
Other, please specify ....……………………………….……	θ

PART B FUTURE INTENTIONS OF RAISING FINANCE

Q15: Do you intend to raise any finance in the next two years (2002, 2003 or 2004)? (✓)

Yes	θ
No	θ
Not Sure	θ

Q16: Please indicate which type(s) of finance you expect to raise, why have you opted for the specific type(s) of finance selected and if possible, please outline the anticipated funding level required. (✓)

	Attempt To Raise	**£000 Amount**
Bank overdraft	θ	……..
Bank short-term loan (up to 5 Yrs)	θ	……..
Bank medium or long-term loan (more than 5 years)	θ	……..
Credit card	θ	……..
Leasing/Hire purchase	θ	……..
Commercial mortgage	θ	……..
Invoice discounting	θ	……..
Equity finance from private investors	θ	……..
Equity finance from institutional investors	θ	……..
Business angel	θ	……..
Residential re-mortgage for cash injection	θ	……..
Business grants	θ	……..
Alternative Investment Market	θ	……..
Other sources, please specify............…………………….....................	θ	……..

Why did you choice the above finance types?

1 ....………………………………………..............…………………......…………………...............……........................

...................................……………………………………………………….............…..............................……………….........................

2 ....………………………………………………………..…….................…………………....

...................................………………………………………………………...……………….

3 ....……………………………………………………….........................……..……………….

...................................………………………………………………………...……………….

Q17: Do you feel that you have sufficient information to inform your decision?

Yes	θ
No	θ
Not Sure	θ

If no, what further information or support do you require?
………
………
………

……
……
……

Q18: What obstacles, if any, do you expect to come across in raising this finance?

1 ………
………

2 ………
………

3 ………
………

Q19: Who will you use as your key source of advice to raise additional finance?

Please specify
………

Q20: How will this finance be used? (✓)

Working capital	θ
Fixed asset purchases	θ
Business acquisitions	θ
New product or service development	θ
Market development	θ
Funding losses	θ
Training programmes	θ
Restructuring/Reorganising the business	θ
Other reasons, please specify………………………………………	θ

Q21: Do you expect your business activity over the next 12 months to: (✓)

Increase	θ
Decrease	θ
Remain static	θ

Q22: Do you feel that there are any significant gaps in the availability/type of business finance available to your business? (✓)

Yes	θ
No	θ

Q23: If yes, please give further details below:

1………

………
2 ……
……
3 ……
………

Q24: What changes would you like to see introduced affecting finance for small businesses at a local, regional and national scale?

1..
....
....
2 ....
....
....
3 ....
....
....

PART C CONTACT DETAILS

Please provide the following information for the Chief Executive/managing Partner/Proprietor of the business (3):

Q25: **Gender**

Male θ

Female θ

Q26: **Age:**

Under 25 θ

25-40 θ

41-50 θ

51-60 θ

Over 60 θ

Q27: **Years with the Business:** ………… yrs

Q28: **Ethnic group of the key decision makers (Optional):**

This information will be used for statistical purposes only to identify any ethnic specific financial issues.

White θ

Black – African θ

Black – Caribbean θ

Black – Other *(please specifiy)* θ …….…………………..……

Bangladeshi θ

Chinese θ

Pakistani θ

Other *(please specify)* θ ………………………….

Q29: **Has your company experienced any discrimination in accessing finance?**

Yes θ

No θ

If yes, please provide details below

……………………...…………………………………………………………………………………………………
……………...…….
……..….……
…………………………………………………………………………………...……………
…………………...……………………………………………………………………………………………………

……………………...…………………………………………………………………………………………………

………...……………

Please provide the following information relating to your business:

Q30: **Business Location (nearest Town/City):** …………………………………….

Q31: **Business Post Code:** …………………………………….

Q32: **Date of Establishment of Business:** …………………………………….

Is your Business: Less than 36 months old θ

More than 36 months old θ

Q33: **Was your business established as a result of:**

New start-up θ

Merger θ

Management buy-out θ

Spin-off θ

Other (please specify) θ …………………………….

Q34: **Turnover Levels:**

Turnover in last financial year: £…………….000 FY ……….

Turnover level two years ago: £…………….000 FY ……….

Q35: **Number of Employees:** ………………..

Q36: **Areas/Market where your business currently operates** *(please tick as many boxes as are relevant)*

Local	**Regional**	**National**	**International**
θ	θ	θ	θ

Q37: **Sector of Business** *(please give a short description and tick below)*

……………………..………………………………………………………………………………………………………

……….……..……………………………………………………………………………………………………

Manufacturing: (✓)	
Engineering and Electronics	θ
Energy	θ
Chemicals and Pharmaceuticals	θ
Textiles, clothing and footwear	θ
Food, drink and tobacco	θ
Timber and furniture	θ
Paper and printing	θ
Other Manufacturing	θ
Other	
Construction	θ
Transport	θ
Media (Publishing, film and TV)	θ
Leisure and entertainment	θ
Other creative industries	θ
Distribution and wholesale	θ

Retail	θ
Business Services	
Other services	θ
Not for profit	θ
Social Enterprise	θ

Would you be willing to discuss any of your responses with a consultant from Deloitte & Touche?

Yes θ *Please complete the contact details below*

No θ

Your contact details

Name: ……...……………………………………………………………………………………...…………

E-mail address: ....……………………………………………………………………………………...

Position: ....……………………………………………………………………………………...……

Business: ………..............……………………………………………………………………………...……

Address: ……..........……………………………………………………………………………………...……

……………………..................…………………………………………………………………………...……

Post Code: …..................…………

Telephone Number: …………………………

Deloitte & Touche may contact you from time to time to inform you of other services which may Be of interest to you. If you do not wish to receive this information, please tick this box θ.

Deloitte and Touche are notified with the Information Commissioner's Office. The information provided to Deloitte & Touche will be used solely for the purpose provided and all personal data will be processed in accordance with the requirements of the Data Protection Act 1998.

12. APPENDIX VII – FINANCE CASE STUDY

Table 8: Funding Structure of Five North East New Businesses

	£,000				
	Start-up	**First Round**	**Second**	**TOTAL**	**%**
Phase	**1**	**2**	**3**		
Sponsors Capital					
Initial Sponsors Capital	525				
Additional Sponsors Capital		33	21		
				579	29%
Private Investors					
From Private Individuals	450	325			
Additional Capital from Other Private Individuals			160		
				935	47%
Bank Finance					
Overdraft	55	34			
SFLGS		40	60		
Asset Finance	25		135		
				349	17%
Other Finance					
Loans (Non bank)		50	88		
				138	7%
TOTAL	**1,055**	**482**	**464**	**2,001**	100%

Five new business start-ups in the North East.

Trading between 6 and 36 months.

Now seeking finance between £2.5m - £3m.

Source: Deloitte & Touche