Myths surrounding growing a business

A focus group based study on behalf of the Small Business Service

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EXECUTIVE SUMMARY

This study was undertaken by Durham Business School on behalf of the Small Business Service from February to July 2006 and is intended to provide a better understanding of the perceptions of small business about growth. In total, 73 small businesses took part in 10 in-depth focus groups conducted throughout England. The sample was deliberately structured to include a range of both micro (under ten employees) and small businesses (between 10 and 50 employees). The aim was to capture the views of businesses with a track record of growth, and contrast them with newer and smaller businesses with successful operating experience, but relatively static levels of employment and/or turnover.

While extant research describes the barriers to growth faced by businesses, this study tries to distinguish between those barriers that *are* real and others which owner-managers *believe* to be real, but are, in fact, exaggerated or non-existent. It is proposed that owners of younger businesses are susceptible to these misperceptions or 'myths', and as a result are less inclined to grow their business. The experiences of such businesses are contrasted with those of more mature businesses with growth experience, to illustrate that some of these beliefs present a lower barrier than imagined, and the available range of solutions.

The report's key findings include:

- Most owners aimed for growth in efficiency (profit and margins), rather than in the standard indicators associated with becoming 'larger' (output, employment and assets). There is not universal agreement that 'business growth' equates to 'being bigger'.
- Many businesses distinguish the idea of being larger from the process of how to bring about change leading to growth. Non-growers are particularly susceptible to rejecting a strategy of growth because of negative views of the consequences of being larger. For these businesses, the questions of how to grow are never explored in great detail, simply because they do not want to deal with the anticipated consequences.
- Even for those who consider that being larger brings net benefits, the actual process of growth is believed to be inherently risky and associated with an exaggerated prospect of failure. Non-growers tend to think that maintaining their business at current levels is less likely to result in operating difficulties than a scenario involving growth.
- Non-growers are less likely to consider how risk can be quantified or minimised, by collecting data and calculating projections of their future profitability and cashflow.

Myths

The research identified 13 myths which tend to act as deterrents to growth. Most of these involve the overestimation of the problems inherent in the growth process. While these myths are the most prominent to emerge from the focus groups, further research is needed to determine the size of their influence on growth, the mechanisms by which they operate and are propagated and which individual businesses are most affected.

Myth #1 *Getting larger means business as usual, only more of it.*

Businesses assume that, if they grow larger, they would not need to alter their working practices or the products/services they supply. However, most larger businesses noted that this attitude would make growth more difficult, if not impossible, beyond a certain size.

Myth #2 *The management costs of a larger business are disproportionately greater, in particular the amount of my time that would be needed.*

Owners believe that an increase in size leads to a much larger increase in the resources that need to be devoted to management, both of day-to-day business operations and the frequent problems which businesses anticipate encountering when larger. The benefits of growth are not believed to compensate for this, and some businesses discount them almost completely, envisioning the consequences of growth in purely negative terms.

Myth #3 *Pursuing a growth strategy increases my chances of failure.*

Owners believe that failure is more likely in a situation of growth than of relative stability. They prefer to remain in a 'comfort zone' of perceived safety, at least partly due to their aversion to risk, which exaggerates or privileges the likelihood of failure.

Myth #4 *I would only be bothered to prepare a business plan to obtain finance, not to understand my growth potential nor plan for growth.*

Using information for strategic purposes, whether day-to-day micromanagement or longer-term planning, was not a priority for most businesses. The potential and ongoing value of business plans to a growing business is not fully appreciated by owners.

Myth #5 *I don't have enough working capital to accommodate growth, and there's no way for me to improve it.*

Owners often accept their level of working capital to be a given, rather than something that they have potential to improve. Many methods of improving cashflow – e.g. more effective ways of dealing with debt, extending overdraft limits – were generally not pursued, and often not even mentioned as possible options.

Myth #6 *I can't use a bank because they only sell me what they want to sell me.*

Owners made special reference to the inflexibility of banks to provide tailored solutions and respond to individual requests with discretion, rather than formulaic approval of loans on a scoring basis. Banks were seen as the principal institution to raise funds and few alternatives were considered.

Myth #7 *Internal finance is the only option, because external funders want too much control.*

Owners believed that all financial institutions placed constraints and conditions on lending that would involve the sacrifice of some control over the business. This was particularly true for those owners who expressed a view on equity capital, which was seen as offering too much of a stake in the business for too little investment. This myth again overemphasises the negative aspects of growing, rather than considering the benefits realised by growth made possible by investment.

Myth #8 I'm too small to try for work with the public sector.

Some owners believed that public sector contracts were more easily won by larger or more well-known businesses, leading them to avoid seeking public sector work. However, a significant proportion of local authority work actually does go to SMEs, in contrast to participants' perceptions.

Myth #9 Changing my HR practices wouldn't change the result, there are just too few suitable staff out there.

Owners used a narrow range of recruitment methods. This created an unnecessarily small pool from which to draw recruits, and exacerbated their inefficient selection practices, often leading to unsuitable candidates being chosen. Instead of blaming the subsequent poor performance and high turnover of new staff on internal deficiencies, owners tended to point the finger at the lack of candidates with the suitable skills and attitudes in the current tight labour market.

Myth #10 Growing means I'd have to become a manager, it's not what I'm good at and if I'm managing I'm not earning.

Owners often believed that their own value within the business lay in direct income generation (e.g. sales or production) and that indirect management activity took them away from this contact with customers and clients. They believed that as a business grew, management duties would absorb more of their time, which was not as good a use of their skills as more 'productive' activity.

Myth #11 My growth potential is limited by the market that I serve and I can't do anything about it.

Owners believed that their operating environment was limited by (a) their location in economically depressed areas; (b) operating in particular sectors; and/or (c) the saturation of their local market. Diversification and innovation had been adopted, to an extent, but owners largely failed to exercise such creative thinking and were resigned to accepting the status quo.

Myth #12 The costs of regulatory compliance would be too high if I grew any more.

Owners commonly exaggerated the effect on their costs of regulatory compliance if their business were to become larger. This typically stemmed from the belief that regulations required a greater or more extensive degree of compliance than they actually do.

Myth #13 The business support system is only useful at start-up, not during the growth process.

Owners were sceptical of the value of the business support system to mature businesses. There was a widespread perception that the network catered only for start-ups, and owners had limited knowledge of the range of help for growing businesses available from the Business Link brand.

Implications

These findings have a number of implications for possible policy development, particularly in terms of what might be done to support and promote growth, and how support and advice can most effectively be supplied to businesses. The key unifying feature of the myths is the lack of self-awareness, vision, strategic thinking and management capability among many small business owners. Therefore, policy implications principally relate to building the internal capacity, knowledge and skills of these business owners, to enable them to be more efficient and take a longer-term strategic view of the growth process. Although intervention is possible with (the minority of) firms that already engage with the business support infrastructure, other methods must be found to convey such information and rebut myths to those 'growth avoiders' who choose not to use the business support system because of misperceptions rather than bad experiences.

Our policy suggestions include:

- An information campaign, similar to Enterprise Week, could be delivered to dispel myths about growth, almost as a 'capacity-building' exercise. In order to effectively communicate with small businesses, the myths must be translated into terms which make sense to owners – i.e. framing them in terms of the actual impact they have, or could have, on business performance.
- The use of outside consultants to diagnose areas of weakness in businesses to raise awareness among owner-managers of their misperceptions, prompting learning and facilitating action to remedy failings. For example:
    - Identified weaknesses in HR processes could be remedied by a programme of education in good practice techniques.
    - Consultants can assess whether businesses are making the most of available sources of finance, and, in particular, recommend alternative sources better suited to funding a growth strategy.
- Leadership and management training would highlight weaknesses and address the ability of managers to systematically use information for planning purposes, and their capacity to implement change within their business.
- Specialisation into niche markets or diversification could be promoted for businesses facing competition or a declining market. Ideas can be garnered from networking and trade fairs.
- Businesses could also be encouraged to look further afield for new custom, either in terms of new clients in the local area or selling products and services in new geographical areas in the UK or abroad.
- The findings indicate that certain approaches of business support organisations could be used more widely. Informal mentoring was found to be a valuable resource for some businesses interested in growth and methods to extend it should be investigated.
- In terms of regulations, businesses should be made more aware of the costs of compliance and the actual content of relevant legislation and regulations. This needs to be presented in an accessible form, using plain English and directly applicable to their business situation. While the DTI's *No-Nonsense Guides* already aim to fulfil this function, some businesses may be unaware of their existence.

Several points from the preceding implications warrant highlighting. First, presenting evidence to small businesses needs to explicitly illustrate the feasibility and practicality of proposed recommendations for growth. Second, the support needs to *wanted* by small businesses, rather than 'forced' on them – thus, businesses need to trust the source of advice and support, and the services offered should be free and be regarded as of value to their business. These points imply that good sources of support for growth should initially be based around other (growing) small businesses, including avenues such as case studies and mentoring.

1 INTRODUCTION

1.1 Context of the research

This study was undertaken by Durham Business School, on behalf of the Small Business Service (SBS), between February and July 2006. The research team previously explored ideas and perceptions associated with starting a business (Allinson *et al.*, 2005), identifying those which are untrue or exaggerated – 'myths' which prevent some people from going into business. The current research builds upon that work, exploring the myths related to business growth.

The two pieces of work are related but take different starting points. The earlier report not only considered the perceptions of those involved in running a business ('Doers') and those considering doing so ('Thinkers'), but also of people who choose not to go into business at all ('Avoiders'). This facilitated consideration of the basic question, whether myths (such as pessimism about business failure) impede or limit the supply of entrepreneurs. The current report accepts the principle that myths produce sub-optimal outcomes and can directly affect the behaviour and decision-making of owners. However, while the owner's actions may influence the direction of the business, they are not solely responsible for variations in turnover, profit or other measures of business size. The demand for goods and services is not directly affected by the owners' misperceptions, and customers may actually confound the plans or expectations of businesses. Instead, it is assumed that myths modify or constrain decision-making, placing fundamental limits upon the extent of a business's potential and/or actual expansion, particularly planned or strategic growth. The fact that one business grows, while another in very similar circumstances does not, suggests that there are no absolute barriers to growth. Rather, there are a variety of obstacles to growth which, in many cases, are purely derived from misperceptions and inaccurate information held to be true by the owner-manager.

Many businesses do, indeed, anticipate growth - the Annual Small Business Survey 2004 reported that 53% of business owners stated that they intended to expand their workforce in the next 2-3 years, rising to 67% among businesses with employees. Furthermore, some 16% of businesses with employees reported that they had already experienced growth in the past twelve months; the same proportion anticipated growth in the coming year; and 11% reported both. Thus, it is clear that by no means all businesses dismiss the prospect of employment growth out of hand, and a substantial minority actually experience growth. However, this does not mean that this group of owners are not susceptible to myths at all – while their workforce may expand, their overall growth potential may be limited by other mistaken beliefs about the actual process of growth.

In this context, the 'myths' to be explored are (i) beliefs which are mistakenly held, based upon misperception(s) or untruths, i.e. factually incorrect, and (ii) those which result from an imperfect ability to process or judge information, i.e. with some basis in truth but where potentially soluble problems are held to be insurmountable obstacles, thereby acting as deterrents to action. This study has two main aims: (a) to identify those factors or issues which dissuade people from trying to grow their businesses, especially where the perceptions they hold are inaccurate; and (b) to identify whether the provision of information, designed to enhance understanding and knowledge, could systematically change risk and benefit judgments and lead to more growth-oriented behaviour among SMEs.

Previous focus group discussions related to starting and running a business seemed to indicate that training and intervention can build self-awareness and confidence, in turn facilitating a more realistic appraisal of, and positive approach towards, difficulties. Those classified as 'seriously thinking' about starting a business found that pre-start-up training courses enhanced their ability and willingness to appraise their current situation, plan for the future and seek appropriate advice and support. For most who had already established a business, experiential learning, gained from acting on the impulse to start, had put their fears into perspective, helped them to learn and understand more about the risks and returns involved, and significantly reduced areas of uncertainty. However, it is hypothesised that making the transition from being a 'start-up' to a 'growth SME' poses a new or distinctive set of challenges, which lead to a different assortment of misperceptions, myths and wrongly held beliefs, which are the focus of the current project.

1.2 Policy context

At the beginning of 2001, according to SBS estimates, there were 3.7m business enterprises in the UK, compared to 4.3m at the start of 2005 (DTI, 2006). However, the majority of this growth is accounted for by businesses without employees. The number of such businesses increased by 22.1% over the four year period 2001-2005, compared with just 9.1% for businesses with employees, so that the proportion of businesses with no employees has grown from 69.3% to 72.8%. However, these businesses also tend to have lower rates of growth in turnover - an average increase of 4.2% over the whole four-year period, compared with 12.2% for businesses with employees. Thus, while the number of businesses is increasing, there is the suggestion that many of the new businesses remain without employees.

It should be noted that not all of these businesses without employees *want* to grow – some may be operating at levels they are fully satisfied with. Alternatively, however, they may be apprehensive about growth because of beliefs in myths associated with employing staff. The fact that such a large – and *increasing* – proportion of enterprises choose not to hire any employees has potential consequences for future economic growth and labour market and training policies. Thus, the reasons which underlie decisions to grow (or not to grow) taken by owners of businesses without employees are crucial for the framing of advice and support policies, targeted at both start-up and established businesses, in order that misperceptions about growth be minimised.

Building the capability for SME growth is one of seven key themes for the Small Business Service, which together forming a strategic framework for a government-wide approach to helping small businesses. The current research addresses this theme directly, identifying myths which inhibit the ability of businesses to fulfil their potential. The research also touches upon four other SBS themes implicated in a full understanding of the topic: *Improving access to finance* – as external finance may be required in order to fund a planned programme of growth; *More enterprise in disadvantaged communities* – exploring the belief that businesses cannot grow in deprived areas; *Improving small businesses' experience of government services,* perceptions of government services and their accessibility; and *Developing better regulation and policy*, as part of the exploration of perceived barriers to growth.

2 LITERATURE REVIEW

2.1 Overview

While there is an expansive literature devoted to 'growth' (see Davidsson *et al.*, 2004 for a recent review), much of it concentrates on explicating 'stages' of growth (e.g. McMahon, 1998) or the managerial attributes required for a small business to grow. The 'stages' models are now almost universally seen as reductionist and flawed, with little practical utility. Often, the 'why' of growth is ignored, or taken for granted, with researchers instead looking at the path taken by those businesses which have already achieved growth, and analysing its more general applicability to small businesses (e.g. Upton & Felan, 2001)). This approach stems from the principle that growth is inherently desirable, and lessons can be formulated which enable small business owners to either overcome their own limitations (e.g. through training in organisational skills) or to circumvent external barriers. In most of these accounts, barriers to growth are based on the rational processing of accurate information and perceptions, rather than the result of systematic misperceptions or mistaken beliefs held by business owners. Relatively few papers take a 'before and after' approach, contrasting the beliefs of nascent businesses with those of growing businesses, informed by hindsight.

Studies which do address beliefs and perceptions more directly have a tendency to invent myths based on the researcher's assumptions, rather than on systematic research with small business owners. Phrases such as 'it is widely believed' or 'it is a commonly-held myth' recur, with no evidence of a basis for the subsequent statements; some articles (e.g. Linder & Cantrell, 2001) seem to use myths simply as straw man arguments, to be refuted in order to impart lessons for success, based on a particular management philosophy (which often *has* been researched with 'successful' – by their definition - small business owners).

There are also deficiencies in the literature regarding the conceptualisation of growth itself. Broadly speaking, the 'growth' variable is taken as a given, and refers to increases in employment and/or turnover, with little systematic research into how the SMEs themselves conceptualise growth, and would therefore assess and/or pursue it. For example, few studies examine profit margins explicitly, yet many focus group owners in the current study concentrated on this measure as their main 'growth aim'.

Others tend towards determinism, looking at the start-up features which are pre-conditions for later growth, particularly the sector, the personal characteristics of the owner-managers and their aspirations for growth, alongside a bundle of external factors (e.g. Delmar & Davidsson, 1999; Carter *et al.*, 2000), often within a simple regression model. This latter group of articles falls broadly into the 'picking winners' strand of small business literature, with a broad consensus that the multidimensional aspects of growth make predicting future growth paths difficult. In focusing upon the factors which make growth viable, this type of research by its very nature tends to exclude exploration of the reasons why some businesses choose *not* to seek growth in the first place.

2.2 Establishing a growth framework

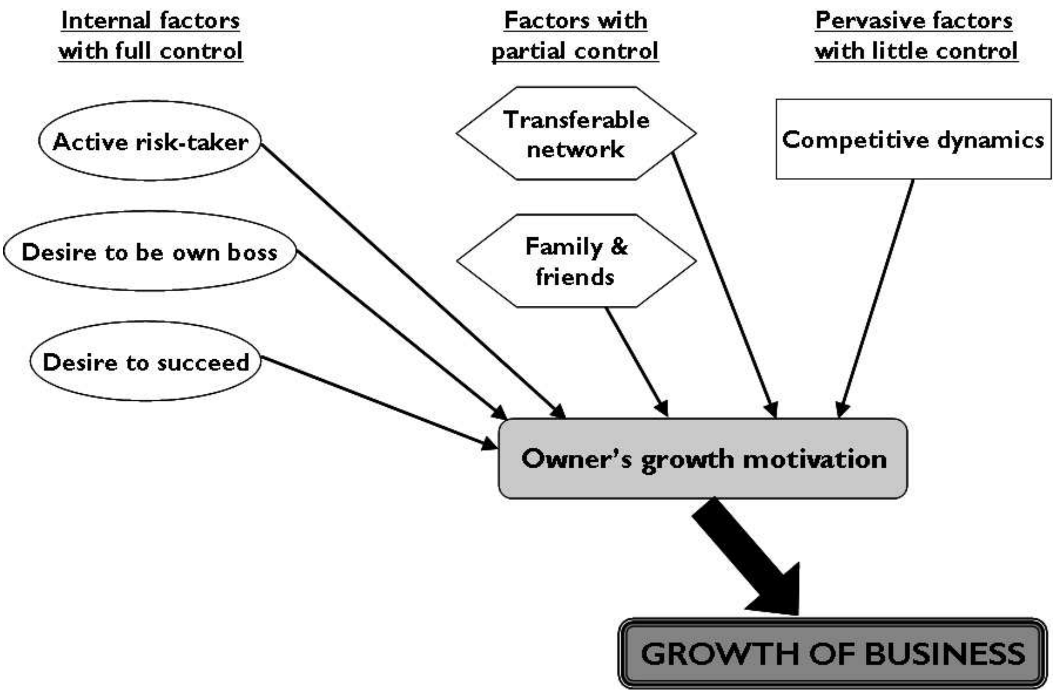
Perren (2000) proposes a loose framework of growth factors, intended to function as the foundation for Socratic questioning of micro-business owner-managers, designed to diagnose barriers to growth, but adaptable to the context of this research. The basis of the framework is that in the majority of cases, growth beyond the micro stage comes about through incremental adaptations to internal and external factors, rather than as the result of a well-defined plan or strategy. She conceptualises four 'interim' drivers of development: motivation and expertise in managing growth (both predominantly internal to the business and the individual owner/manager and dependent upon self-belief), demand (mostly external) and resource access (a mix of internal and external). The classification of these factors as internal or external is also related to an owner's ability to exert control. These drivers, and the ultimate reaction and growth path of the business, are influenced by a large number of independent factors, which must combine to produce a net positive influence, in order to allow the business to grow. These are:

- Factors requiring self-awareness, which the owner can fully control (innovation, risk-taking, desire to succeed or to be one's own boss)

- Pervasive or environmental factors, over which the owner has little control (economic and/or social context, sector, competition)

- Factors where the owner has some, but not complete control (investments from family/friends, employees, network, advice and support, their own transferable capital and skills)

An example of how these factors interact with one of the drivers, in this case motivation, fuelled by self belief, is shown below (adapted from Perren, 2000, p61):



This framework, and the factors and drivers therein, formed the basis for the analysis of misperceptions and mistaken beliefs within the focus groups. In our earlier research, related to myths inhibiting start-up, the importance of self-awareness factors became apparent, and, as illustrated in the above diagram, may influence perceptions (or misperceptions), for instance, about the degree of competition in an area lessening the motivation of the owner to grow, therefore influencing the actual growth of the business. Similarly, while the owner's personal network may be very supportive of his/her growth ambitions, it could be unable to provide or point towards a source of finance, leading to a belief that funding for growth is hard to obtain, again limiting the growth trajectory. The importance attached to this has implications for the type of advice and information needed to challenge misperceptions and the sources most trusted.

This interplay of factors, reflecting a relatively limited number of internal and external key drivers, provided the outline for the questions asked in the focus groups.

The exploration of these topic areas not only helped to identify growth myths, but also to indicate potential policy options for providing guidance to repudiate myths and minimize their effects. Within this, our findings provide specific details of the form and content of appropriate assistance.

2.3 Identifying the myths

Several articles do examine (mis)perceptions about growth, either implicitly or explicitly, fleshing out the general framework for the research outlined above and providing more focused topics around which to build discussions. This section principally concentrates on individual publications which indicate particular research directions, rather than attempting to construct a comprehensive overview of the somewhat disparate and piecemeal research on myths.

Morgan *et al.* (2002) examines the stages and progress of learning in small businesses, investigating the differences between growers (those that had reached over 20 employees and/or added employees between their birth in 1998/99 and 2001) and non-growers. It considers whether and where they seek knowledge that might challenge myths and how that knowledge is utilised. Owners of non-growth businesses were found to put far more emphasis on their own experience and ability than growing businesses, to involve staff to a lesser extent and were less likely to engage in in-house training, group meetings, one-to-one guidance and external courses. Thus, their own perceptions were unlikely to be challenged. Non-growers were also less likely to plan, reacting to situations rather than anticipating them, thereby weakening their growth potential.

NCE (2001) outlines myths about 'entrepreneurial growth companies' – start-ups that go on to grow significantly. While lacking in methodological detail, the myths presented, and their debunkings, seem reasonable and relevant to the current research, contrasting the start-up period with the later growth period. They also form a rough overview of the lines of enquiry described in the other articles mentioned. The relevant myths for investigation here (slightly reworked to emphasise the growth phase) are:

- *Growth is less risky* than start-up. Research shows that entrepreneurs risk relatively little at the start, compared to the risks that investment in growth requires. The managerial skills, drive and ambition required for growth are all at a higher level than those required for start-up.

- An *innovative product/service is more important* for start-up than growth. On the contrary, a new business can become established by simply doing the same thing as its competitors, only better, or with a slightly different emphasis. Long-term growth requires a more individual identity and a distinctive product or service.
- A *track record* in the sector is highly important to start-up. This is actually more important to growth, in order to both obtain the necessary funding and recruit the key personnel to sustain development.
- A *detailed business plan* is more important at start-up. Start-ups need to be responsive and adaptable to circumstances, and a cursory plan usually suffices. It is only when the business is larger that a more developed and consistent strategy is needed to build a coherent business.

In this framework, the role for policy is mainly related to education and training, both in entrepreneurial/management skills and in the technical areas required in high-growth sectors. There is also support for making finance more readily available, particularly informal borrowing and venture capital funds, as well as developing stock option schemes and the alternative investment market.

2.4 The perception of risk

Someone who fails in business incurs financial losses, and may also experience a strong sense of personal failure. The consideration of such risks figures strongly in decisions both to start and grow a business. In order to identify what motivates or inhibits entrepreneurial activity, it is essential to understand how individuals assess these risks, how they construct credible opportunities and the role of their perceptions in doing so - where less risk is perceived, an idea is likely to be evaluated favourably and considered worthy of follow-up.

Identifying and utilising information

In new or unpredictable situations related to business start-up or growth, information such as historical trends and past performance data may reduce levels of uncertainty. However, if entrepreneurs perceive a relatively low level of risk, they may react with overconfidence, failing to seek or take account of disconfirming evidence. Similarly, some do not consider past experience relevant, choosing to treat each situation or decision as unique, requiring a future orientation. Kahneman & Lovallo (1993) describe this as the 'planning fallacy'. Furthermore, if an entrepreneur dies choose to search for data, the subsequent processing of such information (as well as how it is framed) also affects outcomes. Opportunistic entrepreneurs are usually more growth-oriented, with a tendency to pursue more opportunities that arise. Cooper *et al.* (1998) found them to exhibit systematic cognitive biases, to overestimate their chances of success and to engage in less counterfactual thinking.

Retaining control

An 'opportunity' is defined by what the decision-maker deems desirable and feasible - i.e. within their control and competence. As Perren observes, the perception of control and the degree to which it can be exercised reveals cleavages. As there can be overconfidence in their ability to identify and interpret relevant information appropriately, so there can be an overestimation of their own skills to exert control over people and future events. The antithesis of this proposition also affects the pursuit of opportunities and the likelihood of business success - there can be a *lack* of confidence in the ability to identify and effectively process relevant information and an *under*estimation of the capacity for control. People's estimations of their own competencies to control and improve performance vary considerably, as does the level of trust in others for purposes of delegation (Langer, 1975) - both in turn affect growth capacity. This shifts the focus from those internal factors, over which the individual can have full control to the areas in which they can only have partial control. Entrepreneurs often perceive low levels of risk, believing they are able to influence future outcomes and take appropriate action to offset risk, although they do not go so far as to believe that they can control market conditions (Keh, Foo & Lim, 2002). This suggests that both entrepreneurs and more risk-averse individuals recognise their lack of capacity to control what Perren (2000) describes as 'pervasive' factors. This, in turn, indicates the potential for greater difference, inhibiting business growth at the level of personal or internal factors, or those over which they believe they have partial control.

Further empirical research on owner-managers' attitudes towards growth, and how their perceptions affect their behaviour, is reflected in a number of papers based on a ten-year longitudinal dataset of Swedish SMEs. Wiklund *et al.* (1997) note that, in apparent contradiction of straightforward economic theory, non-financial considerations were held to be more important than financial outcomes, in predicting the willingness of managers to adopt growth-oriented strategies (although the research does not track the *actual* outcomes of these strategies). The main question posed to owners, related to the possible consequences of their business doubling in size (for whatever reason). The most common response, across all sectors and sizebands, was concern for the well-being of employees, with many owners citing the 'atmosphere' of the business as crucial to its success. Other factors, such as concerns about their own workload, or a potential loss of quality or independence, were each rated as important by a number of individual managers, but no other factor achieved the same level of consensus as employee well-being. This prefigures some of the focus group evidence from the current study, although awareness of the potential for cultural specificity, in studies such as this Swedish one, needs to be maintained.

From our own research in relation to starting or operating a business (Allinson *et al.*, 2005), cleavages in perceptions were discernible amongst focus group participants, based on socio-economic group and past experience of the labour market. Participants drawn from the long-term unemployed (6 months or longer) and attending courses to facilitate the move into self-employment, conveyed a strong sense of appreciation of their circumstances, derived from their environment and past experiences. However, compared to participants from more prosperous areas, they also appeared to underestimate their own attributes and skills and to have less confidence in their business ideas. They exhibited greater levels of caution in response to common barriers, declared modest ambitions, and frequently appeared to lack self-assurance in approaching problems. This made them, potentially, much more vulnerable to 'myths'.

By contrast, participants from more prosperous areas tended to convey higher levels of *self-awareness* in relation to their own strengths and weaknesses, greater confidence in the marketability of their skills and ideas, and believe themselves capable of independent research; - in other words to believe they would be able to find the help they needed and that such help existed. This seemed indicative of a more positive approach towards problems – that they were soluble rather than insurmountable. Similar issues were assessed differently and potential difficulties were less likely to assume 'mythic' proportions.

2.5 Management capacity

Broadly, from Wiklund's (1997) research, larger businesses emerge as more willing to grow than small businesses, but there is no clear indication whether this is because small businesses overestimate the problems of growth, or because businesses which have already become large had a greater willingness to grow from the outset. The critical point, when businesses begin to properly confront and consider the realities of growth is, according to the authors, the introduction of professional managers. Where this capacity-related point lies, and how willing businesses are to recognise and take this step, were explored in more detail in the focus groups. This issue touches on both factors under the partial control of the owner-manager (e.g. the capacity to recruit appropriately) and personal control factors (e.g. the willingness to 'let go' or delegate). Using the same dataset, Wiklund & Shepherd (2003), also found that many small businesses are well-positioned on three out of the four of Perren's drivers (having the ability, resources and opportunity to grow), but lack the necessary motivation to take the opportunity. Whether such motivation is based on accurate forecasts of the consequences of growth, or misperceptions of these consequences or of their own ability, willingness and resources to grow, however, is not addressed.

Further comparison of the differing ways in which large and small businesses behave is illustrated in a quite particular way by Iversen (2004), through an examination of the success of patent applications in Norway. He found that greater proportions of applications from SMEs, compared to those from larger businesses, are withdrawn by the businesses or not granted. The implication is that SMEs find it more difficult to grow via capitalisation of non-tangible assets, due, potentially, to misperceptions – e.g. initial overestimation of the value of such assets; underestimation of the time or cost of pursuing a patent application; and/or overestimation of their understanding of the patent system. While growth via intellectual property (IP) was less relevant to businesses in our focus groups, a more general inference is plausible - that resources may be wasted pursuing fruitless growth opportunities, due to an inability to plan and cost such opportunities efficiently, and an over-estimation by owners of their own capabilities. Jones *et al.* (2003) look at a similar situation among SMEs in South Wales, examining barriers to expansion via e-commerce, and finding a lack of awareness amongst owners of the applicability to their own situation, and ignorance of both technology and costs. Only a minority used the Internet for sales, with most opting for a 'shop window' approach, suggesting that small businesses may be limited in their capacity to plan strategically; it implies a certain rigidity in thinking, in that small business owners also fail to recognise the relevance and potential of such technology, precluding any search for more detailed information on the topic. This, in turn, has implications for the way in which information may need to be delivered to small businesses, in that it should challenge ingrained thinking, be taken to its audience (as opposed to the audience seeking it out) and emphasise the specific, practical relevance to the business of the topic being promoted.

2.6 The effect of financial performance

Davidsson *et al.* (2004), in their more general literature survey of growth, look specifically at research on the relationship between profitability and growth (of turnover or employment), finding that most studies point to difficulties in growing from a position of low profitability – businesses which attempt this are likely to end up in a low profits-low growth equilibrium. This effectively debunks the apparently quite widespread belief that it is possible to grow out of a low profit situation, perhaps based on a belief that fixed costs will remain stable while turnover rises, allowing profitability to increase.

Torres & Anderson (1994) examine which aspects of previous financial performance can be used to predict growth in 'small' businesses – those with under 500 employees and under $5m annual turnover in 1980-82, by their definition, meaning these results are more applicable to the larger businesses in our research sample. They found that faster growing businesses were more highly leveraged, but also more profitable (in particular, in terms of the return on assets), which compensated for the higher level of debt – i.e. prior good performance fuels growth. Growing businesses tended to pursue an incremental investment strategy based on their profits, preserving liquidity, rather than a 'quick growth' strategy based on risky opportunities and aggressive leveraging. The authors also acknowledge that such a strategy is not suitable for all growth-oriented businesses (e.g. those based on innovation or first mover advantage, which require more rapid progress).

2.7 The impacts of regulation

According to the Better Regulation Task Force report on small businesses (BRTF, 1999), 'regulation impacts hardest on growing [small] businesses', as opposed to start-ups. The reasoning behind this is that, while start-ups often ignore regulations and avoid the attentions of enforcers; growing businesses will attract notice when they breach thresholds for exemption. The heavy burden of understanding the complexity of regulation, and the opportunity cost of dealing with it, usually falls on the owner-manager, potentially putting the business at a competitive disadvantage.

SBS (2005b) reviews the extant evidence on the extent and nature of the effects of regulation on small business performance. It finds a wide range of opinions on the subject, with some implication that the response of owner-managers is at least partly dependent on how the question is phrased or framed – for example, instances where 'regulation' is singled out as a burden, against instances where it forms part of a longer list of obstacles for an owner-manager to rate in order of importance. The language used frequently frames regulation in a negative light, presupposing that this is the case. Equally, the vague nature of the questions sometimes used means that businesses frequently simply treat them as an opportunity to complain about the government in general terms, rather than focus on the specific impacts of specific regulations, a tendency which we attempted to avoid in conducting the focus groups. Research on whether regulations actually inhibit growth in reality, or have any impact on decision-making, is scarce. Where an evidence base exists, the implications are that new regulations actually have minimal effects - for example, the introduction of the National Minimum Wage had very little impact on business behaviour or viability, with only those businesses *already* in trading difficulties being affected to any degree. Indeed, such regulation may actually spur improvements leading to growth – for instance, substituting higher quality labour in response to wage rises.

Evidence on threshold effects created by regulation is also somewhat scanty, although the implication from several recent studies (Blackburn & Hart, 2002; Atkinson & Hurstfield, 2004; NatWest, 2004) is that micro businesses not only encounter fewer problems with legislation than larger businesses, but actively choose to remain small, due to worries about red tape and the costs of compliance. However, few of the businesses surveyed could actually name specific regulations or legislation which would have an impact, preferring to speak in somewhat vague terms of more general issues with bureaucracy and compliance. Dean *et al.* (2000) point out that there is some truth in these beliefs – in a study of environmental regulations in the US, they found that smaller businesses are able to avoid the scrutiny from inspectors that is routine in larger businesses.

2.8 Human resource policies

Carroll *et al.* (1999) find that small businesses typically do not follow 'textbook' procedures for hiring staff, eschewing systematic processes in favour of informal methods, such as word-of-mouth recommendations or hiring 'known quantities'. While most of the 40 case study businesses utilised job descriptions, none used job analysis, and only a quarter explicitly questioned the need to fill the vacancy or performed job analysis. Preferred recruitment methods included recommendations from staff (all businesses) and other 'closed' methods, such as internal labour markets, rehiring former staff or registers of interested applicants. Jobcentres and the local press were also popular, having proven their worth as 'tried and tested' routes alongside more informal techniques. The common link between these methods is their relative simplicity, using existing channels and contracts, and avoiding specialist HR expertise. Most also typically reduce the risk and uncertainty of recruitment. The research supports a model of employment in small businesses which divides the workforce into core and transient components; the former can 'fit in', either socially or with the idiosyncratic working practices of the small business, while recruits in the latter group cannot, and would typically leave after a few days. Many managers seemed to be resigned to this state of affairs, and accepted high labour turnover as the norm. This state of affairs undermines the stability needed for growth, imposes recurrent costs of recruitment, training and management time, and does not necessarily lead to the 'best' recruit getting the job – closed methods, open only to select group of jobseekers, militate against efficiency in filling the post.

Kotey & Slade (2005) and Mazzarol (2003) attempt to answer the obvious follow-up question of the point at which it becomes worth the small business's while to establish formal HR policies, and how to do so. Based on a small number of in-depth case studies, Mazzarol finds that staff recruitment, retention and motivation represent a 'critical bottleneck' (p34) in the growth process, only overcome by the development of the owner-managers' skills and beliefs. Before formal HR implementation could be successful, they needed to develop competencies in leadership, coaching and management and to believe that they had an effective team to which they could delegate responsibility. The commitment to 'employee partnering' was crucial in overcoming the bottleneck and recruiting a stable and competent team to grow the business further. Kotey & Slade (2005) make similar points, noting the advantage to new businesses of a flexible and intuitive strategy aimed at aggressive search for and exploitation of opportunities and direct control by the owner, rather than dispersed responsibilities. As the business grows, the need for more systematic formal processes increases, but the owner needs to maintain a balance between formality, control and accountability on one hand, and flexibility to respond to changing circumstances on the other.

2.9 Does advice make a difference?

Ramsden & Bennett (2005) considered the impact and efficacy of advice given to businesses, finding that advice often acts as reassurance in the face of uncertainty, but does not consistently result in definitive positive outcomes for businesses, either hard or soft. In addition the size of businesses seems to be (largely) irrelevant to whether or not SMEs seek advice in the first place or the type of advice that they seek. In terms of the sources, public sector advice suppliers are reported as being of unpredictable quality, lacking professional skills, and applying over-bureaucratic eligibility criteria; all of which combine to limit both impact and satisfaction.

Robson & Bennett (2000) examined the relationship between SME growth and business advice and external collaboration and found that the main positive relationships were dominated by the private sector – lawyers, suppliers, friends and so on. They also established that obtaining external advice for strategy and recruitment were associated with raised performance; however, they could find little significant statistical evidence for a positive relationship between government-backed sources and business performance.

Contrary evidence comes from Bennett, Robson and Bratton (2001), in which some Business Link services are acknowledged as excellent, although conceding that others are poor. However, Ramsden and Bennett also note that Government services often suffer from negative brand and reputation effects and the opinions of businesses are often tainted by this impression. Indeed, many of the most vocal critics of Business Link are those who rarely or never use the service – the opinions, and performance of those who have actually received advice from government services tends to be more positive.

Roper and Hart (2005) tracked the performance of businesses over the period 1996-2000, comparing those assisted by Business Link at the start of the period (only), against those with similar characteristics which received no help, and found a significant boost to the former group. Employment in assisted businesses increased by 22.8 per cent and sales by 36.2 per cent, compared with increases of 12.2 per cent and 12.7 per cent, respectively, among non-assisted businesses. Managers of assisted businesses were also more likely to introduce new products, invest more heavily in their own business and share a greater proportion of the business's equity - all characteristics associated with growth. In addition NAO (2006) reports that customer satisfaction is consistently high, and has risen steadily, from 74 per cent satisfied in the 2000-01 survey to 90 per cent in 2004-05. It is clear, therefore, that the extremely negative opinions of some critics are not backed up by objective evidence from businesses who have actually made use of the service.

Business Link penetration of the small business sector *is* steadily increasing but there remains a majority of businesses which have had no contact with the service. NAO (2006) estimated the penetration rate to be 14.2 per cent in 2004-05, while SBS estimates (based on the Inter-Departmental Business Register) placed it at 27 per cent (excluding pre-starts) or 37 per cent (including pre-starts), with large inter-regional differences. It may well be that the issue for Business Link. in promoting growth among SMEs. is not necessarily improving its service *per se*, but rather to convince a greater proportion of small business owners that the services it provides are helpful and relevant to their businesses.

Indeed, the work of Bennett, Robson and Ramsden indicates that businesses which do use a wide range of business advice are drawn from the ranks of more rapidly growing businesses. This is also the conclusion of Wren & Storey (2002), who look at the impact of 'soft' advice on performance, while Johnson, Webber & Thomas (2004) find that firms planning growth are more likely to seek advice. Berry, Sweeting & Goto (2006) report similar results, and also conclude that accountants and network contacts are more frequently consulted than government-backed sources, drawing the inference that support agencies may indeed be more effective at promoting growth as gatekeepers to a network of advice, rather than as sources of advice in their own right.

Thus, it becomes clear that successful, rapidly-growing firms already acknowledge the need for and access a range of advice, and use that advice fairly effectively. However, there is also evidence that firms which have the potential to grow, but are not currently planning to do so, are not accessing advice which could prove useful in fulfilling their potential. There is a case, therefore, to be made for persuading them of the need to seek external advice and of the value of setting aside time to do so, possibly by the more effective recruitment of such firms into networks of advice and support, harnessing both public and private sources.

3 THE CURRENT RESEARCH

3.1 Aims of the study

The principle aim of this research was to uncover myths held by business owners about business growth. Such myths were defined as untruths or misunderstood facts, or real, but overstated, barriers to growth upon which decisions are based.

The basic process comprised:

a. An exploration of business owners' understanding of the concept of 'growth'; and how different measures of growth are configured (and interact with each other) within that understanding.
b. Identifying commonly-held beliefs about what growing a business entails, and how they go about it, particularly those beliefs which may discourage or divert growth ambitions.
c. Identifying areas where perceptions tend to be distorted in ways that may dampen or eliminate growth ambitions - for example, in relation to risks and rewards or regulatory burdens.
d. An evaluation of the identified beliefs and perceptions against available quantitative and qualitative evidence, to determine which are true and which are 'myths'.
e. A consideration of the policy implications arising from the research findings.

3.2 Methodology

The SBS brief for this project specified that it should be based around 10 focus group discussions with the owners of small businesses. The factors affecting actual growth decisions and experiences are complex and subtle, better explored and understood via a face-to-face, relatively open-ended process than by a large scale survey. As indicated in the literature survey, the framing of questions affects responses in particular areas quite markedly; a focus group methodology means this can be allowed for and more easily identified.

Each focus group session included two activities: a short questionnaire and a group discussion. The questionnaires provided background data on participants' businesses, an indication of their current growth trajectories and their future intentions towards growing their business. The subsequent discussions were facilitated using a semi-structured topic guide and open questions, with prompts as necessary. This approach allows for in-depth exploration of business practices, informed by owners' general appreciation of the principles of how to operate successfully and the degree to which growth is possible, desired or can be enabled in their business.

Conceptualising and identifying growth myths

It is important to distinguish straightforward good practice in business operation from plans aimed at growing a business. Good practice primarily provides a secure platform from which to grow, and unplanned growth can simply be a result of getting the basics right. In a sense, therefore, any ill-judged or misinformed decision-making in 'everyday' operation is relevant to our investigation, as it can hamper an otherwise well-planned growth strategy. In other words, some myths may simply be gaps in understanding caused by a deficiency of basic business management skills, which hold back both day-to-day operating performance and growth.

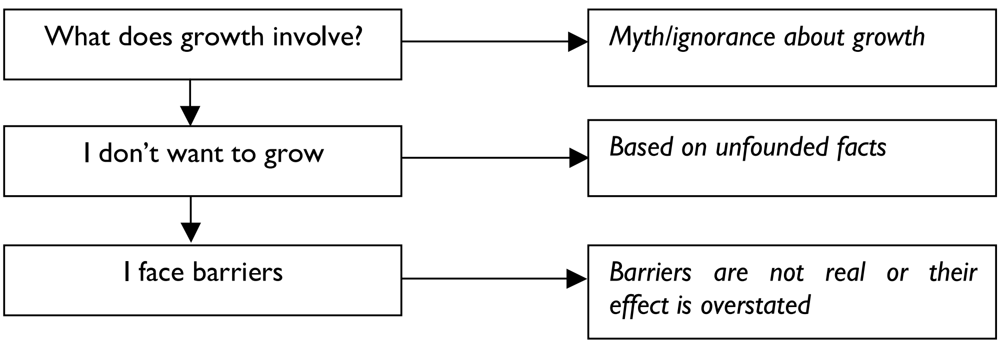
There are numerous other sources of myths, including: media scare stories, which inflate the barrier or risk involved, acting as a psychological deterrent to growth if these are believed; information picked up from other business owners, which may be exaggerated or not relevant to another business in a different sector or location; out-of-date information on, for example, business regulations or employment law which may have been superseded or repealed; and the erroneous application of good practice relating to nascent start-ups to more mature, growing businesses.

Some of the myths being tested have been derived from the literature (Section 2) and media-inspired 'folk theory', and were deliberately tested for in the group sessions. Other myths only emerged in the natural course of discussions with participants themselves. Thus, whilst not strictly following a 'grounded theory' approach, the adopted method embraces the ideas of a case-orientated perspective and induction from data, rather than deduction from theory.

Discussion framework

Each focus group discussion began with an exploration of participating owners' conceptualisations of and motivations towards growth, extending into how anticipated growth might impact on their business, i.e. what they were apprehensive about or how they thought growth would be achieved. This process reflected the framework adapted from Perren (2000), noted in Section 2, by examining a range of factors which fall into three broad categories: (i) 'self-awareness' factors, where the owner can retain a significant degree of control; (ii) those factors over which owners can exert partial control, such as the business's employees, financial assistance from family or friends etc.; and (iii) pervasive factors, such as the economic or social context, over which the owner can exercise little or no control.

The discussion also attempted to place these factors into the rough chronological order in which they affect decisions about growth. The diagram below illustrates the different points at which myths operate, from the first conceptions of the owner about what growth consists of, through to barriers encountered by a business actually planning or undergoing expansion.



Focus group discussions covered:

- Personal factors associated with the owner and their family situation. These include consideration of the anticipated personal benefits of growth (positive and negative) and whether these acted as a rationale for understanding growth motivations
- Risk and uncertainty. Owners were asked about their willingness to take risks (particularly financial), and whether risk-taking is necessary to grow businesses.
- The internal capacity to grow, including:
    - the ability of owners to 'let go' and delegate, including effective recruiting of staff
    - their attitude towards obtaining finance through various sources (e.g. banks and venture capitalists)
    - the use of 'systems' (stock control, customer records, debt-management etc.), both to release working capital into the business, and to facilitate expansion beyond the limits of the 'owner's head'
    - recruitment and retention, the skill levels of staff and employers' attitudes towards training.
    - market research, selling skills and attitudes towards customers, focusing on e-selling, finding new customers, sales experience and whether winning big contracts and selling principally to major customers offers security or is seen as a liability.
- Exogenous factors affecting growth:
    - market pressures
    - the local and national economic context
    - the effects of regulation, how they are perceived and the extent to which they are believed to limit or deter business growth
    - sources of advice and guidance, which would be the most trusted, and the required or desired content in terms of information. Participants were specifically asked about their knowledge of DTI and other public sector providers of information, advice and guidance.

3.3 The sample

The intention was to construct a sample that would capture the range of ways in which different small businesses regard the prospect of growth, why they might avoid it, their expansion plans and strategies and whether the provision of information and/or support would affect their attitudes and practices. The study focused on smaller businesses with under 50 employees. According to the ASBS, the desire for growth is least common among such businesses, particularly those without employees and those below the VAT threshold.

The achieved sample included participants with a variety of growth experiences and aspirations, across a range of business sizes, sectors and regions and of different ages. In total, the focus groups involved 73 participants, 68 of whom were self-employed or business owners; the remaining five were employees with some responsibility for growth strategies. Just over half of the sample businesses were limited companies (39), with a large number of sole proprietorships (23), and ten partnerships. The majority of businesses were start-ups (57), with the remainder split equally between acquisitions, inheritances and those businesses represented by an employee rather than the owner. The majority of businesses (85 per cent) were services businesses, and the male/female split of owners was roughly equal.

The key characteristics of the achieved sample are described in Tables 1-4. Around four-fifths of the sample were small businesses with fewer than 50 employees; most of the remainder had no employees. The median size of business was three employees. Just under a third of the businesses had a turnover below the current VAT threshold of £58,000, although the sample as a whole was skewed towards larger businesses – the median turnover was £125,000 and 14 per cent had sales of £1m or over. The mean age of participating businesses was 12 years, although the median was just 4½ years.

A small proportion of the achieved sample fell outside the specified sampling criteria - notably, two businesses had over 50 employees. When these are excluded, the remaining sample achieved for the study corresponds closely to the size, sector and other criteria specified.

Tables 1-4 show the broad make-up of each focus group, including data on recent performance in terms of employment and turnover change over the previous two years. Of the 45 owners who supplied employment data, more than half had experienced some growth, and only eight had downsized. A substantially greater proportion – 85 per cent of the 46 businesses which supplied data – had experienced an increase in sales turnover (i.e. in monetary terms, rather than an increase in output etc.). In aggregate, total employment among sampled businesses had risen by 36 per cent and turnover by 38 per cent, suggesting that the sample is somewhat biased towards growing businesses.

Table 1 Key characteristics of the focus groups

Group no.	Date conducted	Locality	No. of participants	Ratio of growing: static: shrinking (2004-06)[1]	
				Staff	Turnover
1	28 02 2006	Durham	8	2 : 1 : 1	5 : 0 : 0
2	28 02 2006	Durham	10	4 : 1 : 0	5 : 1 : 0
3	29 03 2006	York	4	3 : 1 : 0	3 : 1 : 0
4	04 04 2006	Harrow	7	4 : 1 : 1	2 : 0 : 1
5	12 06 2006	Stoke	8	2 : 1 : 0	1 : 1 : 0
6	13 06 2006	Watford	7	0 : 1 : 3	4 : 0 : 0
7	20 06 2006	Guildford	8	1 : 4 : 0	5 : 0 : 0
8	21 06 2006	Birmingham	7	4 : 0 : 1	5 : 0 : 1
9	03 07 2006	Sutton Coldfield	6	1 : 2 : 1	3 : 1 : 1
10	06 07 2006	Manchester	8	3 : 1 : 1	6 : 0 : 0
Total			**73**	**24 : 13 : 8**	**39 : 4 : 3**

[1] Businesses less than two years old are excluded

Table 2 Size characteristics (employees) of the overall achieved sample of businesses (n=68)

	Number of employees				
	0	1 - 2	3 - 10	11-49	>50
Number of businesses in category	10	20	27	9	2
Percentage of businesses in category	*15%*	*29%*	*40%*	*13%*	*3%*

Table 3 Size characteristics (sales turnover) of the overall achieved sample of businesses (n=57)

	Sales turnover			
	<58k	58-199k	200-500k	> 500k
Number of businesses in category	17	16	12	12
Percentage of businesses in category	*30%*	*28%*	*21%*	*21%*

Table 4 Age characteristics of the overall achieved sample of businesses (n=71)

	Years business has been operating			
	<2	2 – 5	6 - 10	> 10
Number of businesses in age category	12	24	11	24
Percentage of businesses in age category	*17%*	*34%*	*15%*	*34%*

3.4 The scope of the research

It should be emphasised that the research focused purely on identifying 'myths' held by business owners and associated with growing a business. The purpose of the research is thus *not* to contribute to the further understanding of the determinants of growth for micro and small businesses, but to explore the more novel concept of 'growth myths'. As qualitative research on a relatively small scale, it was never intended to provide quantitative evidence of the prevalence or incidence of myths, but rather to ascertain the range and nature of misperceptions among a broad sample of owners. Accordingly, the findings reported are basically descriptive. For the most part, the evidence (what the small business owners who participated in the research told us) has been collated and presented and, where appropriate and possible, we have outlined the reasoning behind participant's responses. Our analysis and comment are intended to contextualise these data within the narratives of the participants and, more broadly, within the established body of knowledge relating to the micro and small business sectors.

We believe the study presents findings indicative of the range of growth myths affecting the micro and small business sector. It is important to be clear, however, that there are limits to the generalisations that can be inferred from these data. Further research to establish general relevance and incidence would be appropriate if the issues described here are to provide a basis for specific policy formulations.

4 UNDERSTANDING GROWTH

The first category of myths relate to owner-managers' basic understanding of growth and their strategies, or lack thereof, for achieving it. This involved establishing a baseline – how many owners *wanted* to grow, and which aspects of performance, if any (sales, workforce size etc.) they conceptualised as 'growth objectives'. Myths were hypothesised to revolve around how owners felt about both their business *being* larger and the processes involved in *becoming* larger. In particular, we tried to examine how much control owners thought they had or could have over the process of growth, in terms of changing business practices and the costs of their own time, and how they felt about actively pursuing a growth strategy, as opposed to simply aiming to remain the same size.

4.1 Baseline position – the ambition for growth

The pre-discussion questionnaire asked participants for information about present sales and employment, and comparable figures from two years ago. They were also asked about their future growth intentions, and to define them in terms of significant growth, modest growth, no change or wish to downsize.

In their questionnaire responses, the majority of businesses, 67 in total (93 per cent) indicated a wish to grow, twenty-five (35 per cent) to grow significantly, and forty-two (58 per cent) sought modest growth (Table 5). Only two expressed a desire to downsize, whilst three anticipated no change. These results differ markedly from those of the SBS Annual Survey (2004), where 53 per cent of businesses declared an intention to grow in the next two to three years and 47 per cent did not, which may reflect some elements of sampling bias. However, the higher declared wish to grow may also have been affected by the addition of a *modest growth* category to our questionnaire (not an option in the SBS survey), picking up on latent aspirations.

Focus group discussions explored these responses further: while most expressed a wish to grow, a small number had no intention to act upon that wish. In Manchester, for example, each of the eight participants expressed the wish to grow their businesses, six modestly, two significantly. In the ensuing discussion however, two said they had no actual plans to achieve growth. Disparity of this proportion was fairly typical. As will be examined in more detail later, the anticipated implications of pursuing growth and/or of operating a larger business, may act as disincentives.

Table 5 Growth intentions declared on questionnaire, by current sales turnover (£) and size

	Average age/size			Aggregate growth 2004-06	
	Age (years)	Employees	Sales (£)	Employment	Turnover
Downsize	-	-	-	-	-
No change	-	-	-	-	-
Modest	9.1	4.1	160,000	+21%	+23%
Significant	14.6	10.6*	453,000*	+57%	+44%

* Excludes the two businesses with more than 50 employees

The SBS Annual Survey (2004) found that the age of a business was an indicator of growth ambitions. The percent of businesses wanting to grow was inversely proportional to the age of the business (Table 6). This accords with evidence in the literature review that rapid growth tends to occur in the first three years of operation – or not at all.

Table 6 Growth intentions by age of business

	< 3 Years	4-10 Years	>10 Years
Proportions answering 'yes, I would like to grow'	*85*	*74*	*59*

SBS Annual Survey (2004)

In the SBS Annual Survey, when asked about growth intentions in the next two to three years, 67 per cent of businesses *with* employees (and, therefore, most likely to have already experienced growth) expressed a desire to grow (Table 7).

Table 7 Growth intentions by number of employees/size

	All	Without Employees	With employees	Micro 1-9 emp	Small 10-49 emp	Medium 50-249 emp
Proportions answering 'yes, I would like to grow'	*53*	*48*	*67*	*65*	*74*	*81*

SBS Annual Survey (2004)

Table 8 Growth intentions by turnover

	< £58K	£58-249K	£250K-1.49M	£1.5M-2.8M	>£2.8M
Proportions answering 'yes, I would like to grow'	*61*	*66*	*70*	*78*	*83*

SBS Annual Survey (2004)

Non-growth businesses in our study were asked their reasons for choosing not to grow. Most did not cite reasons that were candidates for myths 'I am happy with the size we are' (49 per cent), 'I am looking to close the business or retire' (21 per cent). Some did provide reasons which represent potential myths: 'it is too complicated to take on staff'; 'regulations deter me'; 'it would cost too much/would need to get into debt'; 'too risky'; 'don't have the resources to grow e.g. space, people'; 'market wouldn't support growth e.g. industry declining'; these will be explored further in subsequent sections.

4.2 How is growth understood?

To identify which beliefs fuel or discourage the ambition for growth, it is essential to understand how growth is understood by small business owners. For our purposes, such understanding provides a framework for interpreting participants' responses and for isolating potential points for intervention.

Members of a Durham-based focus group distinguished between 'organic' and strategic growth. The former was conceived as occurring 'naturally', almost unintentionally, and to result from good practice – leading to word of mouth recommendations, larger orders and repeat business. Strategic growth needed to be planned for and seen as the result of review, audit and stocktaking processes. These categorisations allude to the 'how', with the notion of intentionality seen as essential:

> *It's all about the will to drive turnover up, not the need. You've got to push and drive up expectations about how the business will perform.* (Photographer, Durham 1)

Across the focus groups as a whole, growth was generally equated with profits and the 'bottom line', some emphasised the scale of the business (employees, turnover), whilst others focused on efficiency (profit-margins), some placing different emphases on the profit and loss statement (sale, costs, profits) and the balance sheet (assets and liabilities). These answers reflect the objectives of the business and begin to reveal how owners believe growth occurs.

How is growth achieved?

When businesses in the SBS Annual Survey (2004) were asked how they would achieve growth, the most popular response was to increase turnover, using the existing product/market mix:

- Just fewer than 80 per cent of businesses cited an increase in turnover, with little variation between those with no employees and medium-sized businesses.
- Extending or diversifying the range of products and services accounted for slightly under 40 per cent of responses, though with medium businesses almost half (48 per cent) chose this option.
- The least popular method was to move into new markets, a choice for 30 per cent of businesses, and most popular with medium businesses (43 per cent).

The SBS Annual Survey (2004) noted four anticipated impacts of growth in particular, the most common being taking on employees (55 per cent of businesses intending to grow). Businesses already employing staff were more likely to predict further workforce expansion (64 per cent), as well as the need to expand premises (37 per cent). Investment in capital equipment was anticipated by 45 per cent of all businesses intending to grow and 30 per cent thought they would need to seek external funding[2]. Three of these impacts represent issues which could be perceived as problems: the belief that recruitment is difficult or costly, or that skilled staff are in short supply; the view that suitable premises are unavailable could discourage the search; and the opinion that external finance is difficult to source or to qualify for could limit the search. Businesses choosing to grow demonstrate awareness of these issues but tend to see them as issues that may need to be addresses, while those choosing not to grow were more likely to perceive them as barriers *per se*.

Participants in our study were also asked about their priorities for growth. The questionnaire asked owners to rank their growth objectives (1=highest, 6=lowest), recording as many as were relevant.

Table 9 indicates that growing profit, profit margins and income were the main priorities of the businesses interviewed. Output, employment and assets were mentioned by the fewest respondents and scored as the lowest priorities. Only three participants mentioned other factors.

Table 9 Growth objectives (ranked 1= highest, 6 = lowest)

	Average score	No. ranked 1st	N
Profits	1.7	25	49
Margins	2.1	13	40
Income	2.5	8	40
Output	3.0	5	27
Employment	3.9	2	30
Assets	4.3	1	23

In total, rankings were available from 55 respondents[3] and profits included in all but five instances, ranked first by nearly half of the participants. The average number of priorities cited was three. There were seven responses referring to the sole growth measure of 'profit', with no other objectives; while six participants regarded 'margins' alone as a priority and two saw 'income' on its own as their priority. Fifteen participants gave all six of the measures a ranking, meaning that assets, output and employment tended to appear in longer lists of priorities, but typically with a middling ranking.

4.3 Business objectives at different stages/sizes/ ownerships

Business objectives were reported and ranked by participants and found to vary by size and age of business, and by strength of the ambition to grow. There was also some

[2] Businesses with no employees were more likely to anticipate seeking external funding (approximately one third of firms), but practically none expected to take on staff.
[3] An additional eight non-ranked answers were received

evidence of larger and older businesses adopting a greater number or range of measures of growth. Larger businesses also tended to relate certain factors more frequently - profits and sales, profits and age, and margins and employees, and to rate them more highly than smaller businesses. Overall, the objective rated least important by those seeking modest growth was an increase in assets. Profits were most important for both categories, but significant growth businesses placed a higher emphasis on margins, while income was a higher priority for modest growth businesses. Bigger differences emerge when comparing those reporting employment, output, assets or income as growth objectives (these were reported to a much greater extent by 'significant growers'). This may suggest that, while profit and margin growth are consistently sought, only significant growers have actually considered (or experienced) the additional impacts of their intentions.

In focus group discussions, solvency and the need to remain profitable were seen as key business objectives. This was not always allied to the related concept of profit margins, however, a distinction is made between the principle of profitability as a key objective and growth itself, with growth often viewed as an increase in scale (in terms of sales and staff). As with the desire to grow, discussions suggested slightly different perspectives from the questionnaires, in relation to growth objectives. There was some dispute about the importance of turnover and profit as goals. Members of one group (Durham 1) viewed personal fulfilment and the happiness of staff as their goals, from which a profitable and growing business would result. Such businesses did not suggest abandoning financial controls, but their focus was not directly on the bottom line. While these were the least mature and mainly micro-businesses, such evidence accords with Wiklund *et al.* (1997), referred to in the literature review, where many owners cited the 'atmosphere' of the business and employee well-being as crucial to success. Some participants also stressed that the ideas and skills they had to offer were what was important – the main drivers – and that the growth they wanted was to communicate these to the widest possible audience, rather than to pursue increased financial returns (though this may have derived from the nature of their businesses – personal growth trainer, motivational coach and innovation generation consultancy).

> *Testing out ideas and personal growth is why I do this – financial gain comes a long way down the list.* (Personal growth trainer, Durham)

4.4 Myths associated with the understanding of growth

Myth 1: Getting larger means business as usual, only more of it.

Groups were invited to consider the effects of a scale increase, by responding to a direct question: 'what would be the effect of doubling the size of your business?' Rather than changing how they do business, most focused on the negative aspects of their present size and assumed that these would be worse for larger businesses. Some appeared to lack the capacity necessary to explore alternatives and only considered duplication of their existing practice.

> *It would be a nightmare – I'd have to double the fleet and the drivers, it would be very expensive.* (Construction transport, Stoke)

Indeed, for many businesses the obvious route to expansion is through increased staffing and doing more of the same, with few benefits anticipated. The difficulties associated with staffing in particular were a pressing concern, in terms of costs, supervising difficult staff, and finding suitable recruits.

> *It's growth just for the sake of it – it all just goes in wages or tax.* (Real estate, Stoke)

There also appears to be a relatively widespread desire to stay small, to remain within a 'comfort zone' to avoid exposure to additional, higher costs. Although some owner-managers took a wider view of their businesses, many made repeated references to managing costs, with fewer references to increasing sales.

> *I'm just trying to keep costs down.* (Gym, Manchester)

For very small businesses, especially those with no employees, the issue of costs, or more particularly staying small to minimise costs, is a fundamental constraint on growth, which reflects the myth that being larger compromises profit margins. In most cases, low profitability was recognised as a fundamental constraint on growth, and some were in a low-profit position when they took part in the focus groups.

With the emphasis on the need to control size and costs in order to grow profits it is clear that some owners have a narrow perspective on how growth can be achieved. Yet different growth strategies do carry different implications, not every growth plan requires extra capacity (staff, premises etc) nor does it, necessarily, require a big idea – such as for a new product or new market. Growth may be attainable through changing the ways in which you do business.

> *I either get more people in – like a franchisee, they could pay me a cut, but I don't want the aggro – or I specialise, I get qualifications to do specialist training, like fleet training, contract work.* (Driving instructor, Sutton Coldfield)

The options for this driving instructor were to operate as a driving school and engage more staff to extend the hours of instruction, or undertake higher value work with different clients. If the driving school were to develop like a franchise, each driver would operate in a self-employed capacity, sharing the costs of a central function for bookings. A similar structure to this was operated by the owner of a hairdressing salon, providing premises and reception services for self-employed hairdressers, keeping her below the VAT threshold – i.e. limiting her costs. However, this also served to limit her flexibility, making the capacity for fundamental change more difficult, when she wished to go 'upmarket'.

The option of developing a higher value, niche market, may involve investment in training but can liberate the owner from administrative obligations to other people; whilst the former requires an increase in the volume of sales, but with a low profit-margin.

Some businesses were aware of the ways in which high street brands and supermarket chains behave strategically, innovating, analysing customer information to identify niches and provide additional services etc., but dismissed these as not directly transferable to their own operations.

> *I'm dealing directly with manufacturers, there's no room to negotiate with them, we just take what we're given.* (Medical aids, Manchester)

Owners tended to be resigned to being unable to duplicate such practices, rather than to consider some strategies or practices were within their grasp. Although a number of larger businesses had conducted the relatively simple exercise of re-focusing the business on the most profitable customers (i.e. not necessarily the biggest), very few smaller businesses cited this. Their sales and marketing practices appeared to take a scattergun, rather than a targeted, approach, offering the whole customer base 'more of the same', rather than strategically offering additional products and services to their best customers.

The main method of organising for growth can be a systematic review of present activity to refocus on those areas of the business responsible for income generation. A law business described how a holistic review of their activity had occurred, 'ditching' their broadcast approach of attending events and fairs, in preference of a focused targeted approach on selling to their existing core customers. The business had at the same time diversified into new areas, developing a web-service offering some basic low-cost generic legal solutions.

> *'We reviewed all our activity. We used to make presentations, go to conferences, but it didn't make us any money. Some of it was really just window dressing. Now we spend our time working in those areas that make us money'* (Law business, Durham)

A training company started in 1998 had undergone a similar process, moving from an event-driven approach to a relationship-based approach. Their sales were growing but had tended to plateau. They were using a management consultant to help them rethink their approach but found there was a capacity issue, in that staff were '*finding it hard and struggling to keep up'*

> *We know who our best customers are. This doesn't mean we ignore the small fish – they're the big fish of tomorrow. But we do try and make our sales efforts proportional.'*
> (Medical aids, Manchester)

They had started to analyse who their main customers were – what proportion of their business came from these customer and could they sell them more, rather than using resources to communicate far and wide with very little return – '*it's a fine line between spending enough time selling and telling*' (Law business, Durham2).

Overall, there appears to be some failure to recognise or apply relatively straightforward, transferable tools of analysis to better manage businesses, increase profitability and enable growth. However, micro and small businesses do not necessarily have the resources to adopt such tools in their entirety, and almost certainly not in one step. Brown (1999) notes that, while the use of quality processes in small businesses is far from homogeneous, one theme that distinguishes successful, growing businesses is their adoption of elements of quality frameworks in a relatively informal manner – what he refers to as 'quality without a label'. The managers of these businesses implement a philosophy of quality, based partly on their own experience and vision, and partly on more intangible aspects of formal systems – e.g. management commitment, open organisations and employee empowerment, rather than the 'hard' aspects of benchmarking, measurement and process improvement.

The implication is that growth *does* involve changing processes, albeit in an incremental way, learning from experience and cherry-picking elements of good practice from larger and/or more formally organised enterprises. This returns to the theme of management vision – those businesses where the owner lacks a strategic overview of the company and its future direction are unlikely to adopt the processes needed to realise an outcome of growth, preferring to continue doing business as they always have.

Myth 2: The management costs of a larger business are disproportionately greater, in particular the amount of my time that would be needed.

As well as growth requiring more or different skills and a willingness to look outside the business, there is an impact on the owner-manager's time and the capacity for direct control. The role of the entrepreneur necessarily changes, moving away from front-line activities such as selling and production, into a more managerial role, and the changing organisational structures create new roles for other individuals.

> *I call myself the UK Operations Director, I've got a Sales Director and a Finance Director, and they each head up their own teams.* (Manchester, 45 employees)

However, many respondents felt that the success of their businesses was dependent upon their personal touch, and that greater concentration on a managerial role would damage relationships with customers and/or suppliers, and therefore impact negatively on profits. The typical model was of the 'working owner', with a long-term future in this position. Only a small minority hoped to retreat from day-to-day business as it became larger. Some acknowledged a steady transition, whilst others resented the change and presented a bleak vision of work intruding into leisure, anticipating the situation worsening if the business grew.

> *I can see a need to go part-time on the management side and then gradually move towards full-time.* (Parcel delivery business, Sutton Coldfield)

For many this was also age or life-cycle related:

> *I just want to keep it ticking. I do what I do to pay the mortgage, I don't want any more hassle at my age.* (Gardening service, Watford)

Participants repeatedly stressed that their personal touch was vital to maintaining quality and retaining customers and that growing and growth would make unreasonable demands on them as individuals. This perception amongst owners that their own input in every part of the business is essential and that growth, because it will involve 'letting go', will ultimately be damaging, is probably misplaced. Morgan *et al.* (2002), in looking at the ways in which small businesses learn and seek support, found that owner/managers of non-growing businesses were more likely to have professional or vocationally-specific qualifications (as opposed to generic or business ones) than managers of growing businesses, and so were not necessarily best placed to deal with generic management tasks. Non-growers were also more likely to place greater emphasis upon their own experience and abilities than growing businesses, which were more liable to recognise the input and value of others, including staff and external sources.

Some participants did challenge this perception – asserting that there should be economies of scale in management costs, or that management responsibilities did not have to entirely rest with the owner. Amongst these contributions were some innovative approaches, which were based on the fact that hiring administrative assistance may be a more cost-effective solution than the owner working longer hours on routine tasks which could be outsourced:

> *We want to stick with what we're good at – IT… we also want more family time, so we're doing a skills swap with a firm of accountants. This way we both win.*
> (IT consultant, Harrow)

> *We just couldn't stretch ourselves any further but needed more admin help. In the end we've employed someone full-time and are sharing the costs with another business (my son's). It's really working out and it's given us more time.* (Blacksmith, York)

Myth 3: Pursuing a growth strategy increases my chances of failure.

The activities of commercial enterprises – such as commissioning advertising, cold calling and submitting tenders – carry uncertain outcomes and the prospect of failure: *'just by being in business you're taking a risk – it's not like drawing a guaranteed wage*' (blacksmith, York). However, such everyday business practices are qualitatively different to exceptional risk-taking, such as introducing new products without a track record, or the risks of using finance for bridging purposes or to provide capital.

> *'I know what amount of bad debt I take on, and I don't want any more. A risk for me is loaning to someone who is unlikely to pay me back, but I've got all that information in front of me, so I just go for the ones who will repay the loan'.*
> (Personal finance, Manchester)

For some participants, pursuing growth represented a step-change between what can be seen as the 'toe in the water' of going into business for yourself and the commitment to being a 'proper' business, with employees and a fully fledged marketing strategy. The risks associated with maintaining the status quo are limited and well understood by many owners, as opposed to the unknowns of pursuing growth:

> *Growth is scary – it's hard to evaluate the different options. I'm not sure how to assess the risk I'm exposing myself to.* (Media contact centre owner, Durham 1)

There appeared to be a degree of risk-aversion amongst owners, such that they were reluctant to consider jeopardising their present situation and this may have been related to a form of satisficing, in which owners are content with their current situation, and fear that any change will cause disruption which they cannot control.

Whilst it is true that the prospect of failure for larger businesses has greater implications (due to the greater number of employees for which they are 'responsible'), there is evidence that growing businesses can reap tangible business benefits, including improved survival rates. Phillips & Kirchhoff (1989) found that, in the US, 'survival rates more than double for firms that grow. Even a small amount of growth boosts the average survival rate to 66.3 per cent; that is two out of three growing firms survive.' They were also able to demonstrate that the timing of such growth was important 'the earlier in the life of the business that growth occurs, the higher the chance of survival.'

5 ENABLING GROWTH INTERNALLY

This section considers those factors that relate to the internal dynamics within the partial control of the owner-manager and relate to either i) better use of planning tools, or ii) a willingness to consider alternative solutions. In particular, we focus on two aspects – decisions over where, or whether, to obtain external finance; and the recruitment of staff, both in general and in terms of employees taking over some of the owner-manager's 'productive' activities, leaving the owner in a more managerial role.

Myth 4: I would only be bothered to prepare a business plan to obtain finance, not to understand my growth potential nor plan for growth.

The following discussion presumes that the use of appropriate management systems and structures within business increases the flow of information and enables businesses to make better decisions. Business plans are taken as the point of departure since they systematically refer to all aspects of the current business performance and outline a strategy for the future. The basis for the plan is the use of information collected by the business, and hence the viability of a business plan is contingent on businesses being able to produce and manipulate relevant information.

Many individuals starting businesses are more or less obliged to produce a business plan – by support agencies, banks etc – and often acknowledge the wisdom of doing so, at least retrospectively. In focus groups, a number of people recognised that systematic planning for growth is important – i.e. maintaining the business plan as a live document – yet many sheepishly admit failing to do so. They prioritise the day-to-day running of the business over longer term goals, more by default than by design, treating planning as a luxury rather than an essential ('*I know it would be good for me*'), yet never quite achieved. There is also a failure to acknowledge the distinction between a 'start-up plan and a growth plan' despite the information advantages that would be associated with a growth plan.

> *I find it difficult to keep the business plan up-to-date and relevant. I don't plan how much I'm going to take out of the business or what I need to earn. I just buy what I need and sort it out later with the accountant.* (Pub owner, Manchester)
>
> *In your first business plan you're just guessing what you're going to sell, but when you're up and running you can be more realistic, so if anything I guess a 'going for growth plan' is going to be more realistic.* (Consulting Engineers, Durham2)
>
> *I do have a business plan, but it's basically consigned to a shelf while we get on with running the business… I know I should be looking at it but never get around to it!* (Training company, Harrow)

Businesses have often decided upon remaining the same size, and, perhaps understandably, these businesses have decided not to produce any plan. However, there are some businesses that have ambitions to markedly alter their business, yet their vision is not matched by a detailed plan of how this will occur.

No I don't have a business plan, I have all my own finance, I don't want to borrow, so I don't need one. Staffing is my big issue – I'm not advertising, I have no real competition… this business represents my pension, I want to change its image completely – move upmarket, change the clientele and be able to charge more.

(Hairdressing business, Manchester)

As might be expected, those actively pursuing (and achieving) growth almost invariably do plan systematically. The owner of a medical aids business (which is growing significantly) prepares an annual business plan – setting goals, analysing the business etc. – while recognising that projections are often difficult for the innovative products he is trying to develop. Similarly a healthcare equipment business (also reporting significant growth) produces three- and five-year plans. It can be inferred from the 2005 Employer Skills Survey that smaller businesses are less likely to prepare a formal business plan: some 82 per cent of businesses with more than 25 employees reported doing so, compared with 51 per cent of businesses with fewer than 25 employees.

Yet the process of assembling and maintaining a business plan is a tool to manage uncertainty. The consequences of not doing so are that the owner may choose not to undertake changes leading to growth, despite being within a situation of manageable risk and profitability – because they may be unaware of this as they have not collected or analysed the available information, or may plan for growth in inappropriate and ineffective ways. It is also conceivable that owners susceptible to this myth may have uninformed positive optimism in an unprofitable and risky proposition, where a plan may have led them to reject or modify the idea so that it becomes viable. This myth is directly related to the *process* of growth and most typically dissuades expansion plans. The production of a business plan is a mechanism for objectively evaluating and managing owners' perception of risk, but acceptance of the myth serves to inhibit growth ambition. Indeed, planning may well be necessary simply in order to 'stay the same' – i.e. to maintain the same level of income – even in the many businesses which have no growth ambitions.

Business plans use information to take a strategic overview of a business at regular intervals. Information systems differ in that they relate to day-to-day micro-management of the business, yielding the most value when accurate information is used to inform activities. They may simply be regarded as methods to become more orderly, although even in this role they provide information to enable business growth. Information may also be used for strategic purposes to reposition the business so that it performs most effectively. Welbourne (2006) found that the timeliness of the collection of data by businesses, that is the speed at which it happens and is put to use, is positively related to success and growth. However, it is clear that many firms do not simply lack the will to engage in business planning, they also lack the basic capacity and skills to undertake strategic thinking and planning.

The business can be organised functionally or around its customers and their needs; to do the latter requires the collection and analysis of information. As noted earlier, examples of the use of information systems include the identification of the most profitable customers and the targeting of this audience; or attempts to cultivate relationships with new customers with similar profiles to high profit clients. While a small number of the sample had adopted such approaches, they were relatively untested – any success in selling goods/services with high profit margins was usually due to serendipity, rather than purposeful planning.

The effects of this myth are that decisions are made in the absence of clear information, meaning owners are operating from a state of ignorance. Thus, some owners may mistakenly reject business opportunities, believing that they lack the capacity to respond when they, in fact, would have been capable of fulfilling the order within the clients terms and timeframe. Combating these manifestations of this myth is a means of *enabling* growth within businesses. Morgan *et al.* (2002) found that growth businesses were more likely to undertake planning activities and seek professional help than non-growers. Growers were more likely to adopt a proactive stance, pre-empting problems, while non-growers are often reacting. While planning does not necessarily avert problems (or opportunities), it does provide the chance to anticipate and consider available options at a time chosen by the owner-manager. The study concluded that such businesses are more likely to stay in control of their own futures, whereas those which do not plan or consider options until their survival is threatened and the pressure is on.

Myth 5: I don't have enough working capital to accommodate growth, and there's no way for me to improve it.

As well as *investment* capital, businesses must have access to sufficient *working* capital to accommodate growth, to tide the business over until an investment begins to show a profit. They also should have an awareness of how large their day-to-day working capital need is going to be in the future, in order to plan effectively. In practical terms, this translates to a requirement for a predictable cashflow situation, with a minimum of unpredictable elements. Therefore, it is reasonable to argue that a prerequisite for growth is good debt management, such that bad debts and late payment are controlled as far as possible.

The preparedness, or reluctance and unpreparedness, of businesses to consider alternatives to existing practices permeates much of the discussion of myths. Contrasting approaches to bad debt are used here to illustrate differences between businesses in their pursuit of successful solutions. The majority of businesses appeared to adopt a reactive stance towards seeking payments from customers and had dismissed schemes to encourage early payment, such as discounts or factoring (where a business sells its invoices to a third party, at a discount, allowing it to raise loans against money owed to the business, effectively accelerating cashflow).

> *We've tried discounts, if you want to offer a discount then you put the prices up then offer a discount, and anyway I don't believe it makes any difference.*
>
> (Parcel delivery, Sutton Coldfield)

> *We've tried factoring – it just doesn't work, you're paying out a load of money for no gain.*
>
> (Automotive supply chain, Birmingham)

Many participants believed that very large businesses were the worst culprits for late payment, although large businesses had proved to be good clients in some instances. The experience of one participant was fairly typical:

> *We offered a discount for payment within ten days – the local authority didn't even try to get it to us in time, but still claimed the discount!*
>
> (Healthcare equipment, Manchester)

Whether or not a small business takes a large order often depends on whether they can afford it. For example, one business felt that they had to turn down a major order from Poland: given the low level of their working capital, the reluctance of their bank to extend further credit and the fact that they would not be paid for 60 days, the business lacked the requisite funds to meet the initial costs of production (buying raw materials etc.) without risking bankruptcy. A similar difficulty concerns late payment: an agreement to pay within 45 days, for example, often translates into payment actually arriving after 60 or even 90 days, potentially leaving some firms in financial difficulties, and restricting their capacity to fulfil orders at short notice. However, some businesses had managed to alleviate problems of late payment and bad debt using methods dismissed by other group members. Several simply advocated being more persistent in chasing up debts as a way to encourage prompter payment, although there was also acknowledgment that this could take up substantial amounts of time:

> *I don't believe the big companies are out to get you, sometimes its just a case of your invoice is stuck on someone's desk and they will be happy to pay you if they get a gentle reminder.* (Lighting products, Guildford)

> *I hate mithering for money – and I'm happy to* [outsource to a third party to] *chase it for me, it's not personal with them and they have the time to chase more frequently – I get payment on 70 per cent of all invoices within 48hrs and it doesn't ruin my relationships with clients.* (Building maintenance, Manchester)

Businesses which do not take such proactive measures to enforce debt recovery or improve cashflow in other ways are therefore also at a disadvantage in their ability to assess options for investment and growth. They are resigned to treating bad debt and late payment as a given, whereas it can more accurately be seen, in many cases, as a variable over which they can exert at least partial control, by implementing a more tenacious approach to debt collection, or methods such as outsourcing or factoring. The effects of this resigned attitude are exacerbated by both risk aversion and businesses' nervousness about their abilities to complete major contracts, process information effectively or enforce payment of debts.

This effect is not restricted solely to pursuing bad debts, but is also applicable when negotiating terms with suppliers and customers, or overdrafts with the bank. Owners susceptible to this myth are resigned to unfavourable relations with many external agents, without realising the prospect of improving these relationships in order to minimise cashflow difficulties.

It should also be noted that some businesses, mostly those where the main revenue expenditure is the labour costs of themselves or a small team, would require relatively little borrowing or reserves of working capital in order to grow incrementally. Such businesses would be less susceptible to the effects of this myth, whereas those with very tight margins (e.g. many of the manufacturers or small retailers in our focus groups) may be more susceptible to its effects, and those of the other financial myths.

Myth 6: I can't use a bank because they only sell me what they want to sell me.

The SBS 2004 Annual Survey found that 55 per cent of businesses looking to grow anticipated using entirely internal sources of funding, 24 per cent were likely to opt for a mix of internal and external, while only 15 per cent were likely to choose exclusively external sources. Not necessarily prone to the myth that borrowing is 'just plain bad', this group may be susceptible to myths related to the methods and sources for obtaining finance and the alternatives which exist. Those most affected by finance-related myths are those who choose not to grow, but both they and those who limit their finance and growth options, often do so because of a lack of knowledge about the range of options available and concerns about controlling the risks to their personal and business circumstances caused by borrowing - such as having to put their home up as security.

The Advisers' group confirmed the impression that business awareness of the range of financing options available is poor, reinforcing the notion that they may be inefficient at identifying and processing information which would alleviate their concerns: '*if someone needs a machine they think about buying it outright and getting a loan from the bank. They're unlikely to have done any research about the other options such as rental or even equity finance*'.

The awareness of financial options was generally limited to loans or re-mortgaging. A small minority used a wider range of sources for bridging finance, including credit cards. Despite punitive rates, the latter were seen as not requiring negotiation and the scheduling of repayments was within the owners' control. Overdrafts were also mentioned but often dismissed, on the basis that renegotiating payment terms or the extension of limits was very difficult.

A media contact centre (Durham 2) described trying to obtain bank finance via the Small Firms Loan Guarantee scheme. The loan was for £350,000, with the guarantee that the government would be liable for 80 per cent of this sum. Despite the comparatively low risk, the bank was unhappy about any further borrowing or overdraft extension. The repsondent's understanding of their response was that, while the bank did not regard her situation as financially untenable, they were unhappy because it did not comply with her original business plan.

> *My orderbook could guarantee a future income in excess of costs but there would be a cashflow issue before I'd get paid and it didn't fit the bank's template, so I had to let it go.* (Media contact centre, Durham 2)

There was general agreement in this group and others with the perception that banks were inflexible and bureaucratic and increasingly focused on short-term gain.

> *You used to be able to go along and talk to your bank manager but you just can't do that any more.* (Consulting engineer, Durham 2)

> *There aren't any bank managers these days, only salesmen without discretion or flexibility - they just want to sell you what they want to sell you and they don't want to take any risk.* (Language tuition, Guildford)

Although a small minority of participants countered this position, suggesting that they had good personal relationships with their bank (e.g. '*I get invited to all their corporate golfing days, and I have my managers mobile number*' [landlord, Stoke]), most felt that the comparatively weak relationship between bank managers and clients contributed towards difficulties in extending overdrafts.

These difficulties were further exacerbated by an unwillingness to seek information and compare offers from rival institutions, again reflecting owners' lack of capacity to obtain relevant information and use it to plan strategically. Overall, small businesses' attempts to raise finance from banks are characterised by a lack of accurate information and distorted perceptions of the range of options available to them. Furthermore, as the next section makes clear, these misperceptions apply not just to banks, but also to the full range of possible sources of finance.

Myth 7: Internal finance is the only option, because external funders want too much control.

The choice to limit finance to internal sources may lead to modest, suboptimal levels of investment, and, when large sums are required, remortgaging may not provide sufficient money. Such underinvestment can be avoided by supplementing internal resources with external finance and businesses should be more disposed to do so, especially when they are in a highly profitable enterprise. Torres & Anderson (1994) found that businesses growing more rapidly showed evidence of pursuing an incremental investment strategy, based on profits and preserving liquidity, rather than a quick growth strategy *per se*, which would be based more on risky opportunities and aggressive leveraging. They examined which aspects of previous financial performance can be helpful in predicting growth in small businesses. Faster growing businesses were more highly leveraged but also more profitable (particularly in terms of the return on assets), compensating for higher levels of debt - in other words, a track record of good performance fuels growth.

However, businesses had a negative attitude towards many external sources of finance. The use of equity finance was discussed with a dismissive attitude: '*they try to rip you off*' (plumbing supplies, Stoke-on-Trent); '*they want as big a stake as possible, while offering you as little money as possible*' (automotive supplies, Birmingham). Again this attitude appeared mainly derived from speculation and hearsay, rather than more objective sources. For example, one participant discussed a sleeping partner in his father's business as an arrangement which had not worked out, with the consequence that he was not prepared to sacrifice *any* control of his business. Handing over control of ownership in order to obtain finance was an important disincentive for owner-managers: '*it means you're working for someone else*' (instrument controls, Sutton Coldfield).

Attitudes to and involvement with external finance seemed to be related to the age and family circumstances of participants and their status as homeowners. Older business owners were averse to the risk of either putting their house up as security, because of the potential loss of an investment they had strived for. Another interpretation of this stance was a rational evaluation of the expectation that the net gains from expansion would not be long-lasting due to imminent retirement, and with lower gains the risk was less worthwhile.

Myth 8: I'm too small to try for work with the public sector.

Small businesses can be somewhat myopic or half-hearted in their attempts to source new clients. Due to ignorance, lack of time or application for research, or a preference for tried and trusted business practices and the familiar; they may overlook potentially lucrative new customers in favour of existing ones. Many SMEs do not appear to consider national or local government or other public sector organisations to be potential customers.

Despite initiatives attempting to make the public sector procurement process more accessible to small businesses, there was a general perception in focus groups that those letting contracts within local authorities and health care trusts often operated within a safety zone of 'known' businesses. At times, there was an inference that this was the result of lack of experience amongst gatekeepers, causing them to resort to known names and 'big players', even when smaller businesses were able to meet the criteria for tenders.

> *I meet all the criteria and I've got the capacity, but in the end they don't want to take a chance and let the contracts to the big guys.* (Medical aids, Manchester)

This was subsequently challenged in discussions: participating businesses were told that small businesses (with fewer than 50 employees) had been successful in securing 43 per cent of the estimated £50bn local authority budget in 2004 (Tyler, 2005). Even more encouraging was the finding of the Federation of Small Businesses, that 38 per cent of businesses with a turnover of less than £25,000 had a local authority as a customer (Mazliah, 2005). In general, participants were genuinely surprised by such figures; many had simply dismissed the local authority as a potential customer[4].

Amongst participants, some did mention a variety of positive experiences with public sector clients, primarily local authorities, the NHS and, in one example, NATO. The building maintenance business in Manchester relied on the local authority as its largest client to control risk, providing a regular work stream and, in a sector prone to seasonality, year-round work for staff. Those owners basing their views on experience, rather than perception had generally found public sector clients good in terms of guaranteeing payment, as a source of steady work and for presenting relatively low barriers to entry.

> *Working with the NHS is good – they will only place an order if they have the money to pay, so there's not much risk of bad debt, though cashflow can be an issue.*
> (Health equipment, Manchester)

> *I've got a contract with NATO. One night I took some top brass to the theatre. It was as simple as that. They were so happy with me I have a pass to get me onto any base.*
> (Taxi hire, Watford)

Myth 9: Changing my HR practices wouldn't change the result; there are just too few suitable staff out there.

The literature review found that staff recruitment, retention and motivation was a 'critical bottleneck' in the growth process, which is only likely overcome by the development of

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[4] Comparisons with central government are less favourable. . The figures for central government are 58 per cent of contracts awarded to SMEs, worth £1.04bn or 22 per cent of total pot (SBS, 2005)

the owner-managers' skills and beliefs (Mazzarol, 2003). In order for effective HR policies to be adopted, owner-managers need to develop competencies in leadership, coaching and management and to believe that they have an efficient team to whom they can delegate responsibility.

In focus groups, staffing was the most frequently mentioned impediment to growth, along with the difficulties in recruiting staff with satisfactory skills and attitudes. From their present position, owners anticipated a future scenario where staffing concerns remain the same proportionately, but where the impacts on resources would be greater because of larger staff numbers. They believed that skilled staff members are hard to find and that small businesses are unable to pay sufficiently high wages to attract and retain talented staff.

The literature review (see Section 2.7) makes reference to evidence that small businesses do not follow 'textbook' recruitment techniques, nor do they try to adopt HR expert approaches, preferring informal methods of recruitment, within a closed system (i.e. a limited pool) of contacts (Carroll *et al.*, 1999). This research further suggests that managers are resigned to a situation of core and transient workers; the former can 'fit in', either socially or with the idiosyncratic working practices of the small business, while recruits in the latter group cannot, and typically leave after a few days. This state of affairs was consistent with focus group findings and has the effect of undermining the stability needed for growth.

In addition, average salaries tend to increase proportionately with the size of the business (Brown & Medoff, 1989; Groshen, 1991; Oi & Idson, 1999). The lower wages paid by small businesses are often cited among the important reasons for differentials in both recruitment difficulties and retention, including by focus group participants:

> *Youngsters just don't care if they turn up or not – if they live with their parents and don't have any outgoings beyond going to the pub, they don't care about your business. I've had good ones, but they've all ended up going elsewhere where they can get more money.*
> (Parcel delivery, Sutton Coldfield)

While many focus group participants used the opportunity to criticise the attitudes of young people, others countered that the solution was to recruit older workers, rather than put the problem down to an actual skills shortage. Some focus group participants, especially from businesses that had grown beyond ten employees, presented evidence of their dependence upon and retention of core workers:

> *I've seen lads grow up with the company – I've seen them get wives and families*
> (Car valeting, Sutton Coldfield)

> *80 per cent of our staff have been with us for 20 years.* (Foundry, Birmingham)

The retention issue does appear to be a significant one and may well be symptomatic of business practices which breed success. Research into how businesses learn and their need for support (Morgan *et al.*, 2002) suggests that growers are much more likely to discuss business issues with employees and include them in decision-making processes than non-growers: 'they acknowledge their people, involve them and train them'.

Even when suitable staff can be found and are retained, several participants in each group believed that dismissing staff was very difficult: '*they've got the law behind them*'; '*employees* *have more rights than we have*'. This meant they were afraid of taking the next step towards growth, in case, if it failed, they would be unable to shed labour. Other participants countered that new recruits could be employed on a probationary basis, or that short-term contracts should be offered, at least in the early stages. Some participants were open about their ability to shed staff quickly when necessary:

> *We took four graduates on last September. It was well worth it, we're still feeling the benefits but by December they'd done their work and we had nothing on the books to keep them – so we got rid of them.* (Computer software, York)

In general, small businesses overstate the relative scale of recruitment difficulties – according to the 2005 National Employers Skills Survey, *internal* skills shortages are more prevalent. Only 7% of establishments report any hard-to-fill vacancies, which are caused by skill shortages in only around half of those cases (4% of businesses). In terms of the workforce as a whole, this is equivalent to 5 skills shortage vacancies per 1,000 employees. Although smaller businesses account for a proportionately higher share of vacancies and skills shortages than their share of employment, recruitment difficulties caused by skills shortages are, in reality, not as acute as many small businesses assume them to be.

This emphasis on recruitment problems obscures the larger problem of unsatisfactory workers within the business. This concern affects around 16% of businesses, with the proportion affected increasing with the size of the workforce. However, these internal skills gaps only cover around 6% of all employees, a relatively small number compared to the exaggerated beliefs of respondents. Moreover, the proportion of employers affected by a skills gap has been declining steadily since 2001.

Attitudes towards employment regulation also affect recruitment practices – these are covered in Section 6, which deals with beliefs surrounding regulation in general.

Myth 10: Growing means I'd have to become a manager, it's not what I'm good at and if I'm managing I'm not earning.

Not only did owner-managers in focus groups believe that the available supply of labour was poor, and that this factor beyond their control, but they also were reluctant to embrace the management role required to develop staff. Such reluctance stemmed from a belief that they were the most valuable member of the production team, as well as possibly lacking the requisite management skills – or the wish to acquire them. Many owners had technical backgrounds, adding value to the business through their own skills. Moving into management poses several dilemmas for such individuals:

- *Will any substitute for my labour be as productive or profitable as me?*
- *Will the time I spend managing be an opportunity cost, representing time I could have been 'earning?*
- *Do I have the necessary management skills?*
- *Is this what I went into business to do?*

Any combination of these objections may contribute to the decision not to grow and may also be the result of unfounded myths.

The right person, the one I'd want, would already be doing this for themselves.

(Estate agent, Stoke)

I would need to double the size of my business to warrant taking someone else on and I'd still regret the loss of personal service, being able to control the quality of what I provide.

(Fitness business, Manchester)

The effect of this myth is that growth is curtailed because of a belief that quality, productivity and performance are driven by the owner themselves and that their withdrawal into management means relinquishing control over these aspects and what makes the business what it is. This is truest for the smallest micro-businesses and corresponds with the myth about growth increasing the risk of failure.

6 EXTERNAL FACTORS

This section completes the analysis of focus group evidence. It deals with those myths and misperceptions related to factors over which owner-managers of small businesses perceive little or no opportunity for control – the state of markets, government policy, regulations and the nature of business support. We wished to test: (a) how far perceptions about markets were accurate – owners may believe that the nature of their geographical or sectoral market restricts their growth by its very nature, discouraging growth strategies; (b) perceptions of the level of regulatory interference - building on findings in Allinson *et al.* (2005) - that people are discouraged from starting a business by the perceived amount of red tape, it is reasonable to suggest that owners may believe that the larger a business, the greater the difficulty in dealing with regulations and bureaucracy; and (c) the opinions of owners on the utility of business support to a growing business (as opposed to a start-up).

Myth 11: My potential for growth is restricted by the market I serve and I can't do anything about it.

The economic context of the local area can hamper the growth of a business in two different ways:

- *Lack of demand* in, for example, an area with high levels of deprivation and disadvantage or a poor transport infrastructure, will cause difficulties both for growing a business which primarily serves that locality – e.g. small retail and personal services – and, possibly, in the recruitment and retention of skilled staff.
- *Overabundance of supply*. In, for instance, a more prosperous location, or one with good transport links, a small business may find that profits are driven down and skilled staff are in short supply, due to competition from numerous other businesses which are trying to capture (or have already captured) the local market.

Focus group participants operating in deprived and disadvantaged areas had a marked tendency to sweepingly extend the difficulties faced by *certain* business sectors to affect *all* businesses in the area, without necessarily taking account of differing market conditions. In Stoke-on-Trent, for example, participants found that much of their market, both to consumers and other businesses, came from the areas surrounding the six towns of the Potteries, though they would not consider the towns themselves to be a good place to set up a new business. Against this, KPMG/MMK (2004) found that Stoke was, in fact, the most cost-competitive place in the UK to set up a business, based on the costs of labour and facilities, and the existence of nearby affluent markets. In Birmingham, participants described how the pressures of competition can lead to growth difficulties – there are so many garages in the Black Country, for instance, that the price of tyres was thought to be significantly cheaper than in the surrounding area, despite rents etc. typically being at least the same as elsewhere, if not higher.

In both cases, a small business offering generic products or services to a local market was thought to face a struggle to earn sufficient profits to reinvest in growth. The advice offered to those businesses which *did* wish to attempt to grow was not to compete on price, but to find a niche and offer a high level of service to encourage customer satisfaction, repeat visits and word-of-mouth recommendations.

You have to think out of the box, and have lots of strings to your bow – charging for things that no-one else does. (Estate agent, Stoke)

People had heard of these new things – alloy wheel repairs, car sealants – and they kept asking: we needed to respond, stay one step ahead of the competition.
(Car valeter, Sutton Coldfield)

When I was arranging a wedding, one of her friends asked if I would do a charity party. It isn't something I'd done before, but I took the job on. (Wedding dresser, Watford)

Amongst those who had been in business for some time, there was broad consensus that competitive pressures had increased substantially. In particular, manufacturing businesses felt that they could no longer compete with foreign prices, and that growing a mass manufacturing business from scratch was no longer possible:

It's the 'China Syndrome'… it's tough to exist here, I've hardly got any customers left.
(Instrument manufacturer, Sutton Coldfield)

I don't have customers in Birmingham anymore… for anyone trying to make anything, being in Britain is a huge disadvantage. (Foundry owner, Birmingham)

I just can't compete on price with China, it's impossible, so I'm buying from them – making far less and becoming more of a salesman for their goods. (Blacksmith, York)

This is not a misperception – mass production is Britain is, indeed, steadily decreasing.[5] However, there was, again, a tendency to generalise the situation to cover all manufacturing, rather than mass production, with other non-manufacturing participants – based on the experience of their contacts or information from the media – largely agreeing with the pessimism about the production industries. In fact, among the manufacturers quoted two had successfully moved into niche areas of production (e.g. the foundry now concentrated on prototypes), enabling employment to remain relatively steady rather than decline. Thus, in contrast to the negative opinions of the groups, there may be scope for growth in certain (relatively small) manufacturing niches, notably high value-added products and services. Indeed, the number of micro manufacturing plants with ten or fewer employees has been steadily increasing, with a 52 per cent rise from 76,500 in 1987 to 116,400 in 2004, accompanied by a 12 per cent increase in employment numbers (Census of Employment/ABI).

Businesses with small high street outlets also reported feeling increasingly pressured by competition from larger retailers, even if not in direct competition - the closures of other businesses in town centres have knock-on effects on footfall, and therefore trade in the area generally. Even amongst younger participants or those in recently established businesses, there was still the perception that competition had intensified in the relatively recent past:

[5] According to the Annual Business Inquiry and its predecessors, the proportion of employees in England accounted for by manufacturing plants with 200 or more employees has declined from 12.0 per cent in 1987 to 4.5 per cent in 2004. Those plants' share of manufacturing employment has also declined, from 48.6 per cent to 37.8 per cent. The total number of large plants has nearly halved, falling from 4,000 to 2,200.

We find a new product, we get it out, but Tesco have already got it, and cheaper than us, we just can't compete. (Deli/bakery, Sutton Coldfield)

[In the 1960s,] *you could have a good run at setting up a business, coast along for three or four years, things weren't as cut-throat back then… today, if you're not successful straight away, you're finished.* (Instrument manufacturer, Sutton Coldfield)

Myth 12: If I grow, the costs of regulatory compliance will be too high.

According to BRTF (1999), 'regulation impacts hardest on growing [small] businesses', as opposed to start-ups. There was a wide range of responses to regulation and tax regimes from the small business owners in our sample. Many complained about the effects of regulation on their businesses, particularly those who had been owner-managers for some time. They contrasted recollections of more 'laissez-faire' governments in the past, with the 'over-regulation' or 'nanny state' of today, which was perceived as restricting growth. Others were more pragmatic, refusing to make heavy weather of compliance, believing it was 'do-able', as long as you were systematic and organised. Some were even positive, citing both Revenue and VAT inspections as having become less arduous and antagonistic over time. Some respondents were less concerned about inspections *per se* than by what they perceived to be the arbitrary, inflexible or uneven ways in which some officials apply regulations. This perception was fuelled by 'unpleasant' encounters with a variety of agencies, although many did concede that the situation had improved in recent years, particularly with HMRC officials, and more recently with VAT inspectors.

Many small businesses have somewhat nebulous conceptions of when and how they would actually be affected by regulatory thresholds. While they may have an idea about the levels at which various regulations begin to apply, they (a) often regard the thresholds as arbitrary; (b) tend to exaggerate the degree of compliance necessary when they reach thresholds; and (c) work on the basis of partial or out-of-date information, often derived from pejorative media reports or the misconceptions of other owners, instead of seeking up-to-date, accurate information from government or other reliable sources. In other words, the myth is *not* that the absolute costs of regulatory compliance will rise as the business becomes larger – this is likely to be true. The myth is, rather, that inaccurate information leads owners to believe that regulations are more stringent than they actually are, and, therefore, that the perceived costs of crossing a threshold are extremely high, thus encouraging businesses to remain small.

The Disability Discrimination Act for example, legislates for businesses to make 'reasonable adjustments' to enable access to provision for disabled people. Many small businesses assumed this meant that they had to make costly changes to their premises to achieve some vague but unattainable standard, rather than merely what was 'reasonable'. Similarly, one owner stated that when his business reached twenty employees, the law 'forced him' to take on a disabled worker whether he wanted one or not (plumbing supplies, Birmingham). Others assumed they would be 'forced' to increase the proportion of women and/or workers from minority ethnic backgrounds at a certain point. Many owners asserted that they had sound financial reasons for not employing disabled workers, for example, due to the perceived costs of accommodating disabilities, or '*women of childbearing age*', due to the costs of maternity leave.

The burden of understanding the complexity of regulation, and the opportunity cost of dealing with it, typically falls on the owner-manager, potentially putting the business at a competitive disadvantage, at least temporarily. As self-declared 'modest' start-ups, some believed you could risk ignoring regulations and avoid attention, while growing businesses may attract notice as they break through the various thresholds for exemptions. There was a feeling, not always articulated precisely, that the larger the business, the more regulations they must comply with, and the greater the time spent dealing with red tape. There did not seem to be a particular *fear* of crossing a threshold or of the consequences of being caught in breach (as BRTF (1999) states), but many simply assumed that they were '*too small to be worth* [the authorities'] *while to bother with*' (interior design, Birmingham), and that they would have to grow substantially before they needed to look at regulations in more detail. One business had even been explicitly informed by a VAT inspector that his business was

> *unlikely to receive any more visits as the inspectorate was more concerned about breaches by larger companies.* (Instrument manufacturing, Sutton Coldfield)

Some research supports this stance – for example, Dean *et al.* (2000), in a study of environmental regulations in the USA, find that smaller businesses are more likely to avoid scrutiny than larger ones.

Thus, there are perceived consequences attached to growing larger, which encourage businesses to restrict growth and remain small, in order to avoid threshold effects. Even businesses in sectors where inspections are more regular and non-compliance could have serious consequences (e.g. environmental health/catering establishments) there is a tendency to comply only with those rules deemed essential and to avoid others. There are clear misperceptions and exaggerations of the content of regulation and the costs of compliance, contributing towards an antipathy to growth. For example, in practice, the actual employment thresholds and the underlying legislation are, to an extent, irrelevant – some owner-managers demonstrated a high degree of ignorance, prejudice and misperception of these issues. Many appeared well aware that they were in breach of a number of laws and wished to stay small in order to escape scrutiny. Staying small was seen by some as enabling them to act in a discriminatory manner. This did not always appear to emanate from 'business reasons' but from racist or sexist attitudes which would not be tolerated in other circumstances; indeed, several seemed proud that they could flout laws with impunity because of the small size of their business.

This is backed up by evidence from the SBS 2003 Annual Survey of Small Businesses and by Blackburn & Hart (2002): both found that micro businesses were less likely to self-report difficulties with legislation than larger businesses. The latter attributes this finding to lower levels of awareness among micro businesses, and the lower level of need to actually engage with employment legislation. NatWest (2004) found that half of businesses either downsized or did not recruit more employees because of concerns over paperwork; Atkinson & Hurstfield (2004), in their analysis of the SBS Annual Survey, found that 7 per cent of businesses without employees would not recruit because of this concern. As in our focus groups, the problems revolved around general beliefs about 'red tape' and the indirect costs of 'compliance', rather than specific regulations or thresholds, reiterating that small businesses are not necessarily working to accurate information when planning recruitment.

In the focus groups, we made particular reference to the VAT threshold, to test whether there were any misperceptions attached to this specific, well-known threshold point. However, the beliefs of the majority of participants were, in fact, fairly accurate, and this financial threshold was not regarded in the same way as the regulatory thresholds outlined above. Businesses tended to treat VAT payments with resignation, something they had to do:

> *There's nothing to be concerned about, you just toe the line, it's not nice but as long as the books are OK, you're fine.*
>
> *It's straightforward, you have to do it, you set up a system and you just do it… if you're organised, you always know what you have to pay, it's not difficult.*

A minority saw the scrutiny involved as 'excessive'. While some small businesses would appreciate easier or more streamlined methods of payment, and many were unaware of schemes which already exist, the cashflow implications of VAT payments were not, in the majority of cases, perceived to be an impediment to growth, nor a reason for remaining below the threshold. Indeed, others claimed to have registered for VAT purely in order to gain credibility with clients (interior design, Harrow). It is reasonable to suggest, therefore, that myths about regulations relate mostly to employment thresholds, rather than financial ones.

Myth 13: The business support system is useful at start-up, but it can't help me to grow.

A common complaint among participants was that they felt the business support system was more focused on support for start-ups than established businesses. A number felt that, given their experience, they knew more about business in general, and the needs of their own business in particular, than any adviser they had encountered. While a minority had a more positive attitude towards advice received from government-backed sources, participants were broadly split into three groups: (a) those with no contact with Business Link and generally sceptical about its usefulness (the largest group); (b) those who had used a Business Link operator at start-up and found the advice useful, but thought it would be irrelevant to their business's current needs; and (c) those who were actively hostile towards Business Link, accusing the organisation of incompetence. In many cases, it was clear, these opinions were the product of prejudice and ignorance, rather than any actual experience of Business Link services, particularly recent experience, many owners were unaware of changes to the support system, and their views were based on the model prevailing a decade ago or even earlier.

These findings – of negative perceptions not rooted in actual experience - are consistent with those of other research (e.g. Allinson *et al.*, 2005) and appear to be fairly widespread, particularly the perceived greater ability and knowledge of owner-managers over advisers. Indeed, the SBS report on how small businesses learn (Morgan *et al.*, 2002) stresses that owners of non-growth businesses tend to put far more emphasis on their own experience and abilities, while growers recognise the value of input from others, and actively seek external advice and support.

Outside evidence on the reliability of public and private sector sources of advice is mixed. As noted in Section 2, advice obtained from the public sector (or publicly-funded providers) garners relatively low satisfaction ratings from some studies, but high ratings from others. The same distinction holds true for the correlation between contact with Business Link and improvements to actual growth variables, such as employment or sales growth. However, it is clear from the literature, and the focus groups, that a large part of the negativity towards Business Link and other publicly-funded advice and support derives from prejudice and misinformation among small business owners who have either never made use of the service, or used it some time ago and are unaware of changes to the system. Many owner-managers in this 'unassisted' section of the small business community (between 63 per cent and 86 per cent, depending on how it is measured) therefore lack trust in Business Link, regardless of its merits, which leads them to either (a) not use the service at all; or (b) give less weight to the recommendations provided than those derived from other sources.

This is, in many ways, an 'image problem', to be tackled by, say, an information campaign rather than wholesale changes to the services provided by Business Link. It is also clear that this image problem only applies to older businesses – on the whole, focus groups perceived Business Link as being very useful during the start-up and early life of small and micro businesses, to help owner-managers 'learn the ropes'. Once the business has been in operation for a few years, however, this perception tends to change among many, but by no means all, SME owner-managers, who regard themselves as not needing help and support *at all*. This myth therefore combines two separate misperceptions: (a) that owners of 'mature' businesses think that they do not require any outside help to manage their business effectively; and (b) that, even if they did require outside support, the private sector is always better than the public sector.

7 POLICY IMPLICATIONS

Broadly, the myths outlined above are united by the common theme of a deficiency of management capacity and vision. Many small and micro business owners find planning and strategy formation beyond their capabilities, preferring to operate to fairly short time horizons in many aspects of their business, from finance to customer management to recruitment and retention of staff. This is demonstrated by the disdain shown for formal business planning processes, and the relative reluctance to approach outside sources of support. The relationship of this lack of vision and strategy to the belief in myths is a vicious circle – owners' initial thoughts on planning are partly fuelled by myths, and the operation of the business and networking with other owners go on to create further myths, which then feed back into the planning process, and so on. This interrelationship of management capacity and misperceptions means that both these elements need to be tackled by policy interventions, since improvements in one aspect should lead to improvement in the other as well. This suggests that some form of training in leadership, management and planning would be required, to better equip small and, especially, micro business owners with the skills needed to systematically gather and process information and apply it to their own business.

To counter the effects of myths and misperceptions about growth, it is necessary first to identify these myths and then to consider *what* small businesses need by way of information, *who* is best placed to deliver that information, and the *means* by which it should be transmitted – how the intended target audience(s) can be reached most effectively. Overall, the potential receptivity of that audience also needs to be borne in mind; whatever information, advice or guidance is supplied may be met by a certain rigidity of thinking. Non-growers appear not to seek disconfirming evidence for their views, delivery, therefore, must engage challenge, and provide information directly relevant to particular situations. This suggests an information campaign targeted at this group is needed, delivered in such a way as to challenge understanding with both objective and subjective evidence directly relevant to their businesses – for example, that engagement with support agencies is both appreciated by clients, *and* leads to an improvement in turnover. The DTI *No-Nonsense Guides* already take a straightforward approach to communicate, for example, how to start a business, or the intricacies of government rules and regulations, and could be used as an exemplar for a similar approach here, based as it is around practical advice for businesses.

The way in which small businesses understand growth – and distinguish the process and effects of growing from actually being bigger – must also be taken account of, in order to ensure that this is reflected in the design and content of support. Such an approach might specifically address the following issues.

Business planning. Participants tended to shy away from detailed business plans once their business was up and running, despite the fact that both internal and external aspects of growth (as well as elements of day-to-day operation) would be facilitated by such a plan. The consensus was that owners did not have time to plan, and, since many had no great wish to expand their business, a plan was unnecessary. To move towards remedying this, first, it should be stressed during start-up that a business plan is *not* simply a means to obtain finance – rather, it is as much a vehicle for the owner to learn about the strengths and weaknesses of their business, to organise their strategic and operational thinking and feed back improvements into all aspects of the business. Second, businesses could benefit from an outside 'diagnostic' assessment of their operations, which would be seen as valuable (rather than a waste of their time, or 'meddling' in their business) and provide a rationale for outside involvement. This assessment could then feed back into an enhanced and refocused plan for the future, including the development of improved monitoring and information systems, in order to increase the capacity for the plan to be a constantly updated, 'live' document, of real use to the business.

Recruiting and retaining staff. While many small businesses have a solid 'core' workforce, the recruitment of new staff is often perceived as being difficult, to the extent that some businesses do not wish to grow, because they believe that there are insufficient suitable workers available to allow expansion. The evidence (from NESS and elsewhere) suggests that this is not valid for most businesses. It is clear that exaggerated negative opinions about the available pool of labour, especially younger workers, and militate against the motivation to expand. The solution (suggested by the literature) may be for small businesses to institute a more systematic human resources regime. This does not necessarily involve dedicated HR staff, but more simple measures, such as analysis of job roles and content, a wider search for recruits than simply appointing a 'known quantity', and questioning whether a vacancy needs to be filled or if resources could be better deployed in other areas of the business. However, owners inevitably see these processes as time-consuming and expensive, and may lack the requisite skills or strategic vision to enable them to change roles from hands-on worker to a more managerial position. Within the short-term time horizon that many small business owners work to (out of necessity or preference), it is true that more formal methods are expensive, but in the longer term this approach should pay dividends by reducing the costs of repeated recruitment and training rounds, through improved staff retention. The added stability, increased job suitability of staff and decreased, long-term costs of incremental recruiting should, therefore, act as an encouragement to growth or at least foster conditions more conducive to growth.

Small businesses' limited and partial view on potential sources of finance. The research raised important issues associated with the often limited and inaccurate views small businesses tend to have regarding potential sources of finance. Small businesses often prefer to use internal sources to fund expansion, limiting the extent to which they can grow. This is fuelled by opinions that loans are difficult to obtain and that banks, often the first port of call, are unhelpful in a variety of ways, and often too rigid in applying criteria or too busy pushing their own products. Alternative sources of finance, such as venture capital and business angels, are little-known, misunderstood or perceived to involve ceding a large degree of control. While it is true that finance may be difficult to obtain for a small proportion of businesses, those which are profitable and stable should be able to obtain funding for expansion if they wish. There is, therefore, a case for providing better information about finance to small businesses, either through a simple booklet or website outlining their choices (similar to that described above regarding regulation). A more active alternative would be offering the opportunity for businesses to be assessed by an outside specialist (e.g. a local accountant) for growth potential and eligibility for funding.

Pessimism surrounding manufacturing. While focus group participants generally demonstrated pessimism about the ability of manufacturing firms to grow at all, the more positive experiences of several respondents suggest potential strategies for facilitating growth within this sector. Small manufacturing businesses which are not growing or facing declining turnover and employment levels could be encouraged to diversify into different areas, seek new customers (through networking and trade fairs etc.) or to develop higher value-added products, rather than assuming that a slow decline is inevitable. Greater publicity about manufacturing success stories, rather than, for example, the domination of industrial news by large-scale plant closures, would aid in the realignment of perceptions about the 'inevitable' failure of British manufacturing.

Lack of growth in services due to competition. As with manufacturing, the issue of competition could be addressed through encouraging businesses to diversify or to identify a specific niche – for example, a food store finding its prices uncompetitive compared to the local supermarket could specialise in different products (ethnic foodstuffs, higher value-added products) or could move sideways into catering or takeaways. Similarly, several participants advocated a high level of customer focus and personal service as a facilitator of growth, allowing small outlets to distinguish themselves from 'faceless' larger stores, thereby encouraging both repeat business and positive word-of-mouth. This also suggests that it may be helpful to examine the ways in which small businesses learn and encourage the use of transferable techniques (such as Customer Relationship Management), particularly those often considered to be only applicable to big businesses.

The burden of regulation. The evidence suggests that small businesses, particularly micro businesses, exaggerate the effort and expense required to comply with certain regulations, contributing to a wish to remain small in order to escape the attention of inspectors and regulators. This implies either that the relevant agencies and organisations are not communicating the details of legislation correctly, particularly the ways in which it applies to small businesses, and/or that businesses ignore the information sent to them on this topic, regarding it as simply another piece of irrelevant 'junk mail'. A substantial proportion of businesses also lack the (often modest) capacity to deal practically and positively with regulation. It should be emphasised that many businesses are not particularly scared about the consequences of flouting legislation, or of growing to a size where they are forced to address compliance issues. Attitudes are based almost entirely on not wanting to incur unnecessary costs of compliance, best achieved in their opinion, by remaining small.

The general, more practical difficulties surrounding regulation are already being addressed, through the Better Regulation agenda, attempting to make the regulatory environment easier to navigate and understand. Therefore, efforts to tackle this myth may be more effective if they are aimed at the, admittedly, more nebulous area of challenging and modifying attitudes towards compliance, in particular the tendency of businesses (and the media) to overemphasise the negative consequences and exaggerate the costs associated with new regulations.

Evidence relating to changes in VAT and Inland Revenue practices in recent years suggests that a more open and approachable stance, combined with proactive supply of relevant information to small businesses, can reap considerable dividends in terms of goodwill and compliance among owners. A number of participants contrasted the 'bad old days' of inspections and heavy-handedness with the current situation, implying that the HMRC model could be rolled out to more government departments, as the basis for their dealings with small businesses.

Business support. Overall, the government-backed business support system, in particular Business Link, suffers from a negative image and a lack of trust among some SMEs. As well as limiting the support that growing businesses are willing to seek directly from such sources, there may also be 'guilt by association', such that any initiative badged 'funded by Business Link' for example, will be likely to encounter similar resistance. Different businesses and owners respond to different forms of advice and support in different ways; there are several, potential solutions to this difficulty, which need to be investigated and evaluated in more depth:

- Rebuild trust in Business Link and other government-backed sources of advice, through advertising and marketing initiatives, possibly working through more trusted intermediaries such as lawyers and accountants, and based largely upon a continuation of existing services.
- Aim more squarely at the businesses 'in the middle' – the bulk of the business base which is neither actively growing nor failing, but instead is satisfied with remaining more or less where they are. It is this group which is least likely to seek out business advice and support from government-backed sources, and which stands to benefit most from attempts to encourage growth.

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