

# **Micro-Business Task and Finish Group Report**

January 2012

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# Executive Summary

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The members of the Micro-Business Task and Finish Group have demonstrated a real commitment, passion and enthusiasm for the task in hand. We have recognised that the recommendations contained in this report are significant and bold which is quite rightly so as the micro-business sector is a vital, dynamic and integral part of the success of the Welsh economy and has the potential to be a driving force for economic recovery.

The importance of creating the right culture, environment and conditions, including connectivity and infrastructure, for micro-businesses to sustain and grow for the benefit of the Welsh economy is demonstrated by noting that micro-businesses (defined as employing less than 9) account for 193,010 or 94.5% of all businesses in Wales in 2011, they are responsible for 33.2% of private sector employment in Wales i.e. 331,400 jobs. Championing and cherishing micro-businesses as a vital part of the Welsh economy and communities is essential to develop a can-do culture in Wales.

It is evident from the work undertaken that the support mechanisms in place for micro-businesses in Wales historically have been complicated, difficult to access and often duplicated across providers of business support. Also, the business support infrastructure in Wales has faced many changes over recent years which make it difficult to plan and sustain an environment that creates the right conditions for micro-businesses to flourish. We therefore recommend that the Welsh Government should act on the advice provided in this document to produce policy to support a long term commitment to provide stability and focus.

Wales may be geographically spread with an urban economy in the city regions and a rural economy across Wales but it is a small community and therefore it is crucial for organisations within the public, private and third sector to work jointly on matters relating to micro-businesses. In identifying the importance of joint working we also believe that in order to strengthen the Welsh economy the role of the Welsh Government should be one of facilitation and enabling the private sector rather than a deliverer.

We believe that micro-businesses in Wales have immense potential to maintain, improve and increase the contribution that they can make to their communities, the economy and to the life of the Welsh nation.

We have identified five key priorities with recommendations to support the development of a Welsh Government micro-business policy and strategy. Our priorities and recommendations are:

## **Priority: Awareness and Access of Business Support Services for Micro-Business**

- Streamline and reduce the number of public sector deliverers of business support.

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- Proactively promotes access and awareness of business support services.
  - Create a single well recognised brand for access to business support (public/private).
  - Develop a network of 'One Stop Shops' for micro-businesses to receive direct/indirect support across Wales.
  - Expand and redirect the current Regional Centre Service to deliver a One Stop Shop concept for micro-businesses in Wales.

**Priority: Access to Finance**

- Facilitate accessible finance solutions of between £1,000 and £20,000 for micro-businesses that are simple and reflect the level of investment required.
- Support micro-businesses to access appropriate finance options.

**Priority: Mentoring and Coaching**

- Develop a pan-Wales mentoring and coaching scheme to support micro-businesses.

**Priority: Public Sector Procurement**

- Simplify public sector procurement processes and regulations.
- Introduce a Wales bill on Public Sector Procurement.
- Establish a Procurement Commission/Commissioner for Wales.
- Encourage local sourcing as part of public sector procurement.
- Encourage micro-business to consider consortia approaches to public sector procurement.
- Initiate smaller contracts to attract micro-business to tender.

**Priority: Regulatory Burden**

- Lobby for change in non-devolved matters – in addition to regulations that affect micro-businesses.
- Communicate where the responsibilities of regulatory burden sits.
- Simplify regulations within Welsh Government power (across all departments) to make it easier for micro-businesses to sustain and grow their business.
- Establish support for micro-businesses with regulations that impact on their business e.g. health and safety, taking on staff and planning.

The report also details other priorities to be considered.

We believe that there is potential for the growth of micro-businesses in Wales and by creating the right culture, environment and conditions this will put us at the forefront of development and economic growth.

**Robert Lloyd Griffiths**, Chair, Micro-Business Task and Finish Group

# Introduction

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The Micro-Business Report for Wales has been prepared by the Micro-Business Task and Finish Group (the Group), under the Chairmanship of Robert Lloyd Griffiths, Director Wales, Institute of Directors and its members:

- Allan Lloyd, Treasure, Mumbles
- David Russ, South Wales Chamber of Commerce
- Janet Jones, Federation of Small Business
- Jacque Williams, SCS Aftercare, St Fagan's
- Peter Denton, Williams Denton Cyf, Conwy
- Robert Chapman, Robert Chapman and Company, Cardiff
- Sue Balsom, Francis Balsom Associates (FBA) Aberystwyth

The purpose of the document is to provide the Minister with advice and recommendations on the development and implementation of a Micro-Business policy and strategy.

## *Task and Finish Group Mode of Working*

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In preparation of the report the Group has used their expertise and experience, which was supplemented and evidenced by best practice and evaluations including:

- Economic analysis
- A review of international good practice
- Literature review
- Gathering the views of micro-businesses
- Garnering the views of key stakeholders

## *Micro-Business Report Vision*

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The vision is to create the right culture, environment and conditions for micro-businesses in Wales to be sustainable and grow to benefit the Welsh economy through improved productivity, innovation and increased job creation.

# Policy Context

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## *UK Economic Context*

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Most recent economic data points to stagnant and weak economic performance, most tellingly in the labour market. The labour market is the most timely and comprehensive source of data describing the performance of the Welsh economy. Like the UK, employment declined in late 2011 and unemployment has increased.

UK economic forecasts included in HMT's Autumn Statement 2011 were prepared by the Office for Budget Responsibility (OBR). The central forecast for GDP growth has been revised down from 1.7 per cent to 0.9 per cent for 2011 mainly as a result of inflation squeezing household incomes and consumer spending.

Growth is expected to improve slightly in the second half of 2012. For full year 2012, GDP is expected to grow by 0.7 per cent. After 2012, UK growth is expected to accelerate, reaching 3 per cent in 2015. The OBR's forecast is predicated on the assumption that the Eurozone debt crisis is resolved in a way that leaves the Euro intact and debt put on a sustainable footing.

Other economic organisations have also recently revised downwards UK economic growth forecasts. The Organisation for Economic Co-operation and Development (OECD) expects the economy to slip back into recession briefly, starting in the current quarter. Growth is not expected to pick up speed until Autumn 2012. For the full year 2012, GDP growth is expected to be 0.5 per cent. Early in 2011 the OECD expected growth of 1.8 per cent. In November 2011, the Bank of England also cut its 2012 forecast for UK GDP growth substantially.

Downward revisions to UK growth have been accompanied by a less favourable forecast for the labour market. UK unemployment is expected to increase from the current rate of 8.3 per cent to 8.7 per cent in the fourth quarter of 2012, before declining to 6.2 per cent in 2016.

However it is important to note that it is possible for micro-businesses to make money and grow even in a poor economic climate.

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## *Wales Government Policy Context*

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As set out in the Programme for Government, Wales faces significant economic challenges in the coming years and jobs and the economy are the over-riding priorities. In line with the background set out above the main influences on the Welsh economy in the short to medium term are the state of the global economy and the monetary and fiscal policy set by the UK Government. A commitment has been made by the Welsh Government to help position businesses in Wales to face the challenging economic conditions ahead.

The Programme for Government priorities have been considered as part of the work undertaken by the Group and is noted where applicable under the Priorities section.

# Micro-Business Analysis

The information below provides an overview of the landscape of micro-businesses in Wales in 2011, with annex 1 detailing the breakdown of micro-business in Wales against each Local Authority and sector.

In 2011 there were 204,280 active enterprises in Wales with 193,010 of them employing less than 9 which represents 94.5 per cent of the total; relatively less than in the UK which is 95.7 per cent.

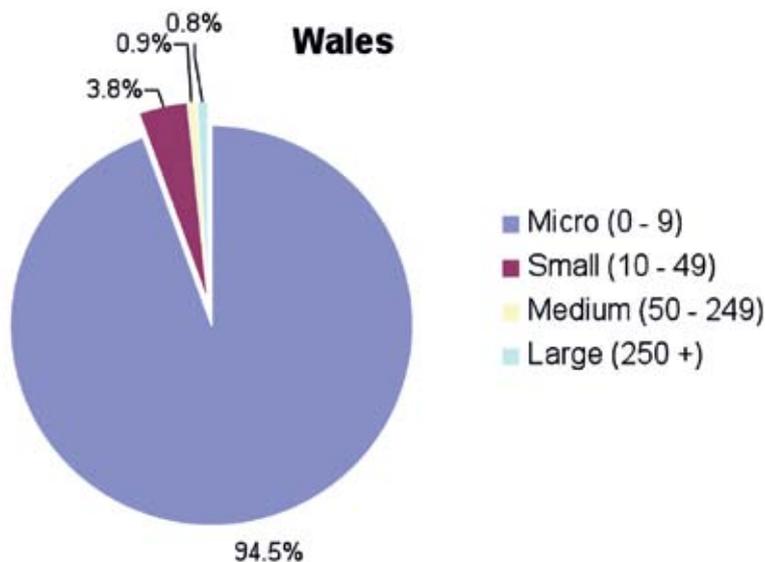


Fig 1 – Overview of active enterprises by size. Source: Welsh Government 2011.

The growth of micro-business in Wales from 2003 to 2006 has been similar to that of the UK, but since 2007 the growth of micro-businesses in Wales has fallen relative to the UK. Wales should aim to have the same growth as the UK.

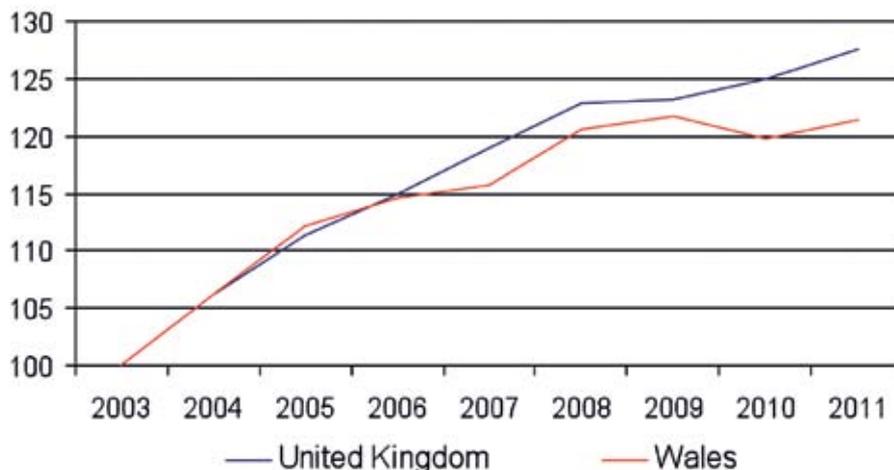


Fig 2 – Micro-Business from 2003-2006. Source: Welsh Government 2011. NB \*Due to improvements in the coverage of the IDBR, estimates increased between 2007 and 2008.

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Growing micro-businesses comes in two forms:

- More new businesses than cessations;
- Growth in existing businesses.

Start up businesses are important, however growth achieved in established businesses is often more sustainable so should be equally encouraged. Furthermore ensuring succession is vital to protecting and retaining jobs.

Even accounting for the trend highlighted in fig 2 in Wales, micro-businesses provide 33.2 per cent of private sector employment (331,400) – proportionately more than in the UK which provide 31.4 per cent of the private sector employment. This is a key aspect that Wales should aim to sustain.

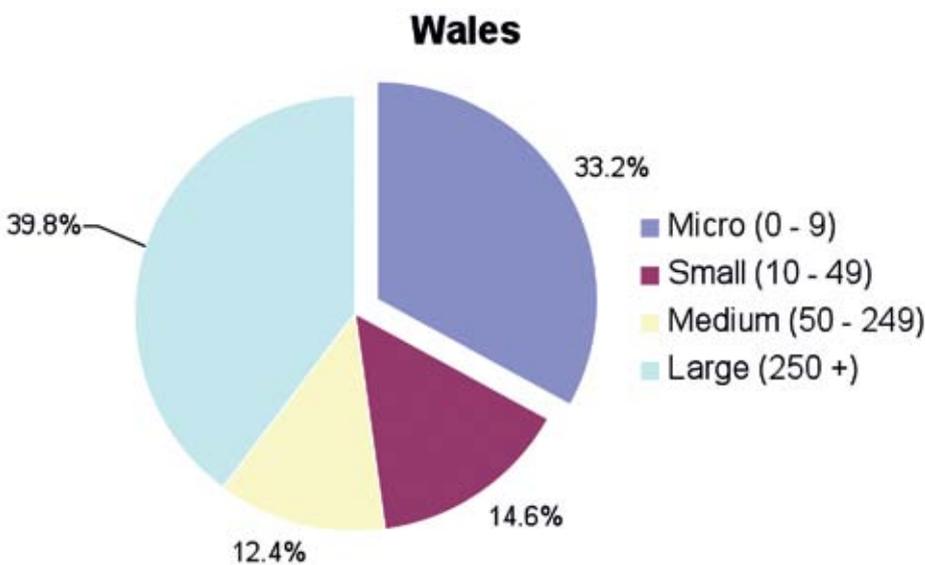


Fig 3 – Employment by business size. Source: Welsh Government 2011.

From 2003 to 2009, the growth of employment in micro-businesses in Wales has exceeded that in the UK. However from 2010, employment growth from micro-businesses in Wales fell by around 1 per cent, a decrease which was not observed in the UK.

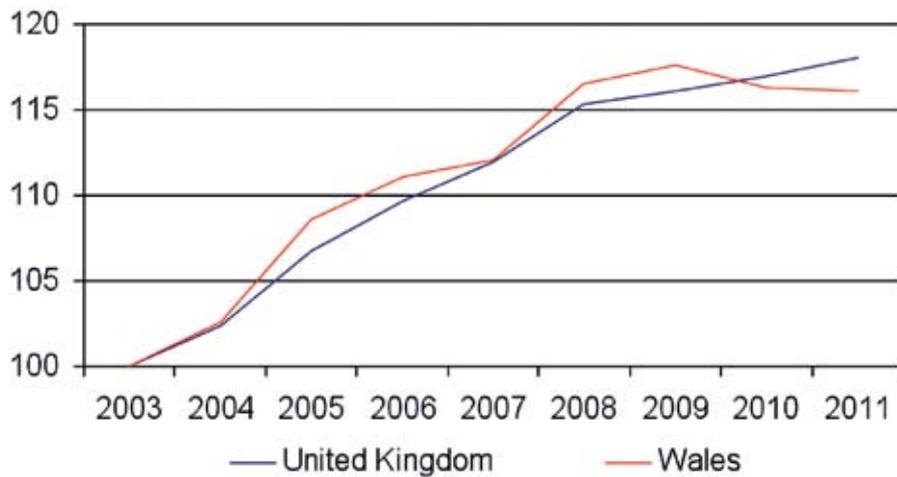


Fig 4 – Employment within Active Micro-businesses: Wales and UK – 2003 to 2011 [2003=100]. Source: Welsh Government 2011. NB \*Due to improvements in the coverage of the IDBR, estimates increased between 2007 and 2008.

In Wales, micro-businesses provide 16.8 per cent of turnover – proportionately less than the UK which is 18.4 per cent.

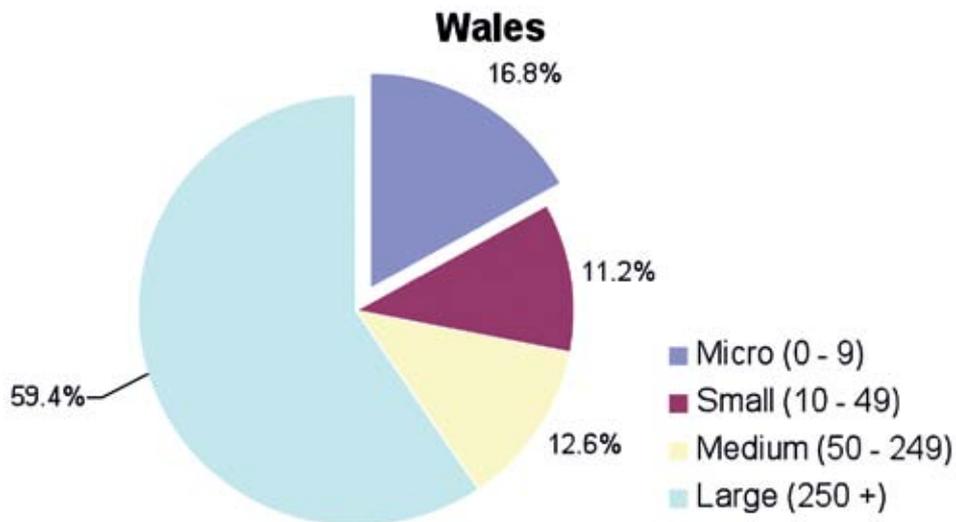


Fig 5 – Turnover by Business Size. Source: Welsh Government 2011.

# Guiding Principles

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The objective for the Welsh Government should be to provide the overarching framework to enable micro-businesses to be sustainable and grow in Wales. This framework should be delivered by effective and co-ordinated cross departmental and organisation work. The following principles and assumptions underpin the report:

1. A micro-business is classed as a enterprise which employs up to nine employees (and includes sole traders);
2. The framework for micro-business should be a long term commitment to provide stability and focused support. The Group recommends that the framework should be reviewed every five years;
3. Government's role should be one of facilitation and enabling rather than direct delivery, with the premise being that the private sector has the expertise and is often better placed to advise and guide micro-businesses;
4. Government should play a role in influencing and encouraging joint working in Wales on matters relating to micro-businesses;
5. Each micro-business is unique;
6. Support should be about quality and not quantity;
7. Support mechanisms for micro-business in Wales should be easily accessible, clear and simple and available to be accessed when needed;
8. The framework for micro-businesses should be delivered on a pan-Wales basis but taking into account the regional differences and uneven landscape of micro-businesses;
9. Setting clear measurable objectives and outcomes for policies that support micro-businesses is essential; and
10. Micro-businesses should be championed and cherished as a vital part of the Wales economy and communities.

# Priorities

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The Micro-Business Task and Finish Group recommend that the Welsh Government focuses on five primary priorities to sustain and grow micro-businesses in Wales.

The priorities are:

- Access and Awareness for Business Support Services;
- Access to Finance;
- Mentoring and Coaching;
- Public Sector Procurement; and
- Regulatory Burdens.

The priorities should be delivered under a simple effective brand that takes precedence over delivery providers, as all priorities are not distinct and do overlap.

## *Priority: Access and Awareness to Business Support Services*

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Currently there is significant confusion among businesses in Wales as to who offers business support, what is available and how to access relevant support. Historically there is also evidence of duplication (even competition) in how and where the public sector delivers support to businesses. This includes Welsh Government, Local Authorities, Third Sector and Academic Institutions as well as a host of EU funded initiatives and projects.

The Group also identified that in many instances public sector deliverers effectively duplicate and displace some business advisory services offered by the private sector where there is a wealth of knowledge and expertise available among Wales based professionals. Therefore it important that future provision helps facilitate local professional services within the private sector.

When micro-businesses responded to the question on where they would look for business support in the Business Omnibus Survey, October 2011 they cited a wide range of methods and organisation varying from the internet, Local Authorities and Welsh Government to accountants, banks and the Farmers Union of Wales.

The Small Business Survey 2010 noted that 28 per cent of SME employers agreed that government services are easily accessible and 47 per cent agreed that they would like government support but struggle to find out what is available.

Easily accessible, uncomplicated and rewarding business support mechanisms are key for micro-businesses and can include direct support and indirect support and an information gateway to external resources. There is also a preference among micro-businesses for bespoke face to face support. However the Group concluded that not all micro-businesses would need this level of support therefore there shouldn't be a universal offer to all, but a process/system of ensuring that micro-businesses understand the access points to the support if they ever require it.

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**One of the key areas identified as part of the international good practice review is that policies and mechanisms to support micro-businesses need to be well co-ordinated, simple to understand and accessible.**

Support agencies are often criticised for providing what government needs rather than what businesses want. A key success measure of support usually used by business support agencies is 'satisfaction' based on whether the services are coherent, good quality and accessible. However businesses base success measures on whether the service has met their expectations. This suggests that not enough effort is put into managing expectations – especially important for inexperienced micro-businesses. In taking forward any recommendations Government should focus on the expectations of the business, managing them and then evaluating the client's experiences.

**The Task and Finish Group recommends that the Welsh Government:**

- Streamlines and reduces the number of public sector deliverers of support for micro-business.
- Proactively promotes access and awareness of business support services for micro-businesses.
- Creates a single well recognised brand for access to Welsh Government assisted business support (public/private).
- Develops a network of 'One Stop Shops' for micro-businesses to receive direct/indirect support across Wales.
- Expands and redirects the current Regional Centre Service to deliver a One Stop Shop concept for micro-businesses in Wales.

***Priority: Access to Finance***

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Currently there is a wide ranging offer of different funding available to micro-businesses in Wales; however access to sources of funding can be difficult.

46 per cent of micro-businesses identified cash flow as one of the barriers to the success of their business in the Business Omnibus Survey, October 2011 and 25 per cent noted obtaining finance as a barrier.

The literature research notes that viable micro-businesses need viably-priced debt finance. What is needed is a means of freeing-up debt finance by de-risking through accessing industry expertise, and channelling it to improving the knowledge base of loan providers, and incentivising the informal market. Measures to address this might include:

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- Using sector experts as intermediaries between banks and businesses;
  - Supporting micro-business to prepare their case to access finance (also using mentors); and
  - Lobbying for tax reliefs on private loans to businesses.

Credit control intervention (cash flow) is a major issue for micro-businesses. Academic literature suggests that large businesses might supply more credit than they receive. Meanwhile, the Small Business Survey 2010 Wales report showed that 93 per cent of SMEs gave credit, while 74 per cent received credit. Late payment was of greatest concern for micro-businesses. Small businesses (particularly start-ups) may use credit to signal reputation and commitment (in the absence of a track record) creating financial vulnerability. This can make access to other forms of finance more difficult. In terms of market failure arising from business size, the important point is that the relative cost of managing debtors and creditors is highest for micro-businesses. The Small Business Survey identified cash flow was an obstacle for 41 per cent of Welsh firms in 2006/07 and for 49 per cent of firms in 2010.

Where otherwise strong businesses are hampered by this disadvantage, there may be a case for intervention.

**The Task and Finish Group recommends that the Welsh Government:**

- Facilitate accessible finance of between £1,000 and £20,000 for micro-businesses that are simple and reflect the level of investment required.
- Support micro businesses with application processes to access wider appropriate finance options.

### *Priority: Mentoring and Coaching*

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Facing difficult challenges, new situations and decisions can be a lonely situation for a micro-business owner, especially when they do not want to burden people close to them. Therefore at such times, a critical friend can be fundamental. The concept of mentoring and coaching for micro-businesses is important whereby they are matched with someone who has a similar background or faced similar challenges in order to receive guidance, discuss aspirations and assess options.

There has been interest in business mentoring in Wales for some years. Both free-to-mentee and paid-for programmes for existing businesses have historically been available. Currently some organisations offer mentoring support for businesses and start ups but there is no coordinated all Wales programme for micro-businesses as a whole.

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The Group felt strongly that if a micro-business is mentored and coached at the key critical stages of the business they are more likely to succeed, be more sustainable and future-proofed.

**The Task and Finish Group recommends that the Welsh Government:**

- Develop a pan-Wales Government assisted mentoring and coaching scheme to support micro-businesses.

### *Priority: Public Sector Procurement*

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Procurement has been a key issue for micro-businesses with many feeling that the regulations and processes surrounding procurement were mostly beneficial to larger businesses resulting in micro-businesses struggling to win key contracts.

In the Business Omnibus Survey, October 2011, 9 per cent of micro-businesses noted (unprompted) that support on winning more contracts/customers would be the most beneficial factor to their business with 49 per cent noting competition in the marketplace as the main barrier to the success of their business. Businesses benefit more from new contracts than grants.

Feed-back received by the Group included micro-businesses not being able to compete effectively for public sector contracts, not least the wide differences in public sector procurement processes and what is required in the procurement process. This represents an unacceptable waste of time, effort and money by both the businesses and public sector personnel involved.

Furthermore, the relatively large public sector in Wales means that the obstacles in public procurement represent both a greater opportunity loss and opportunity cost for micro-businesses. This means that procurement is a key issue for micro-businesses who too often do not get the opportunity to participate in lucrative contracts.

The Government of Wales Act uniquely includes a commitment to sustainability. To sustain micro-businesses in Wales there should be a determined, Welsh Government led policy of local sourcing by the public sector. Such a policy currently applies to Welsh food (see Local Sourcing Action Plan – ‘Food and Drink for Wales’ August 2011) but should also extend to other goods and services.

Whilst procurement processes must of course comply with EU and other regulation, too often these are crudely interpreted by inexperienced procurement staff. Other problems include local government and universities who use UK-wide sector consortia for their supplies, thus excluding local providers.

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Welsh Government should drive a 'Wales first' approach whereby sustainability is an essential criterion in all procurement decisions. Price is important but true 'value for money' addresses wider issues and frequently the price differential is minimal. Unless local sourcing by the public sector is championed, the Welsh Government faces the paradox of funding business support to prevent failure and unemployment in Wales, whilst at the same time exporting valuable contracts that benefit companies, the economy and staff elsewhere outside of Wales.

A requirement for all public bodies to include in their annual reporting the percentage amount of locally sourced procurement, in their region and Wales, could prove invaluable.

This priority supports the Welsh Government's Programme for Government action to implement recommendations from the Barriers to Procurement Opportunities report to ensure public procurement processes are straightforward and contract opportunities are open to all.

**The Task and Finish Group recommends that the Welsh Government:**

- Simplifies public sector procurement processes and regulations.
- Introduces a Wales bill on Public Sector Procurement.
- Establishes a Procurement Commission/Commissioner for Wales.
- Specifies local sourcing as part of public sector procurement.
- Encourages micro-businesses to consider consortia approaches to public sector procurement.
- Initiates smaller contracts to attract micro-business to tender.

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## *Priority: Regulatory Burden*

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Regulatory burden overwhelms micro-businesses. Some EU and UK regulations inhibit micro-business growth e.g. VAT, where the arbitrary nature of VAT registrations limit (at £73k per annum) is an inhibitor to micro-business growth.

The literature research identified that governments create a market failure with respect to small businesses in terms of compliance, and that they have a duty to mitigate the extra costs that result. It is accepted that it is unfair to expect micro-businesses to provide accurate accounts of the extra cost, and at the same time it is difficult for governments to reduce the bureaucratic burden. The EU Commission estimated that a large company spends €1 per employee compared to an average €10 for a small business. There is some justification for a range of business support mechanisms which may not directly relate to reducing red-tape but compensate for its costs.

The benefits of regulations are often neglected. Formal information and reporting systems afford efficiencies to businesses, and help to make them investor-ready.

European governments seem under increasing pressure to explore and implement policies which favour and assist micro-businesses through better regulation or de-regulation. Although this is arguably an area in which the Welsh Government has fewer direct policy or legislative levers, it is perhaps worth exploring some of the approaches that other governments have pursued, not least in the context of the new legislative powers the Welsh Government now has following the recent referendum.

In Iceland, businesses generally regard the burden of government regulation as comparatively low and the European Commission highlights Iceland as showing signs of good practice 'because practical aspects of requirements for SMEs are simplified, easily accessible and online'.

In the Business Omnibus Survey 46 per cent of micro-businesses identified regulations as one of the barrier to the success of their business, 48 per cent also identified taxation, VAT, PAYE, NI, maternity and paternity leave as a barrier to the success of their business.

Access to EU funding for the delivery of business support services should be made easier to enable and promote access to the funds among the private sector.

The Group note that there is a need to be clear on who is responsible for which regulations, Welsh Government or UK Government, and where the Welsh Government could make the biggest impact to support micro-businesses with regulatory burden. It is also critical that all government departments take on board the impact of regulations have on micro-businesses.

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**The Task and Finish Group recommends that the Welsh Government:**

- Lobbies for change in non-devolved matters – in addition to regulations that affect micro-businesses.
- Communicates where the responsibilities of regulatory burden lie.
- Simplifies regulations within Welsh Government powers (across all departments) to make it easier for micro-business to sustain and grow their business.
- Establishes advisory support for micro-businesses when regulations impact on their business e.g. changes to health and safety, employment, tax and planning law.

### *Other Factors Identified by the Group*

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Other important factors were considered by the group but were not able to be fully explored either due to time constraints, or because they were being addressed by other functions and groups within the Welsh Government.

### **Supporting Young People Not in Employment, Education or Training (NEETS)**

With the current unemployment rates among young people in Wales being high, the Group felt that a pre-apprenticeship support scheme targeted at young people not in employment, training or education (NEETS) – similar to the current schemes offered by The Prince's Trust Cymru – should be explored by the Welsh Government which will not only benefit young people but also micro-businesses in Wales. Consideration should also be given to extending this to the wider population. It was noted that the Welsh Jobs Fund is due to be launched in April 2012 which will partly address this priority.

### **Innovation Support**

Supporting micro-businesses to become more innovative as a means of improving productivity and job creation seems to be a fairly consistent and increasingly common theme within the economic development policies and programmes of governments.

International research and evaluation suggests however, that innovation support for micro-businesses needs to look beyond research and development in the context of products and processes. Also that investment should be focused on developing the capabilities of individuals involved in running small businesses for them to innovate and embrace new challenges.

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## **International Trade**

Supporting and encouraging micro-businesses to trade internationally is considered to be a vital service. It is felt that many micro-businesses will be making their first steps into this activity, and it can be a daunting process to go through that may discourage many from expanding their market and which may be a key requirement for growth for them. It is felt that the recommended network of One Stop Shop's across Wales could be utilised to deliver this service.

## **Business Rates**

It is recognised by the Group that the assistance available on business rates is making a difference for micro-businesses; however the assistance available is not always proactively promoted and shared with qualifying businesses. It was noted that a review of Business Rates policy has already been commissioned, and would endorse any outcomes which specifically benefits micro-businesses.

## **Communication Infrastructure**

Fast internet access is clearly identified in the literature research and elsewhere as a specific micro-business need, with rural and farm-based businesses perhaps needing to have specialised support. The literature does provide evidence that some micro-businesses show reluctance to adopt ICT because of lack of time and suspicion. However, the benefits of ICT adoption by business for growth are also well-evidenced and linked to increasing responsiveness to suppliers and customers, access to e-government, formalising financial and other management reporting. As well as internet connectivity and download speed issues, Wales also has significant 'not spots' for mobile phone signals and fares badly in terms of third and fourth generation networks. This is already a huge problem for rural micro-businesses and their plight will be exacerbated as 3G and 4G technologies rapidly develop and become the normal way to access information and conduct business.

## *Other Links*

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It has been identified that the role of Government is to deliver an overarching framework to enable micro-businesses to sustain and grow in Wales which should be delivered by effective and co-ordinated cross departmental and organisation work. This includes the need to identify what the key stages are to signpost micro-businesses to other appropriate support specifically when they achieve growth potential and aim to employ more than 9 employees.

# Criteria and Framework for Evaluation

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It is recommended that the Welsh Government should evaluate the impact of policy direction on micro-businesses by monitoring the following four indicators:

- Gross Value Added (GVA) per capita.
- Number of micro-businesses.
- Turnover and profitability of micro-businesses.
- Employment rate of micro-businesses.

Consideration should also be given to establishing a tracking survey on the attitudes and view of micro-businesses in Wales.

# Annex 1

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## *Number of Micro-Business in Wales by Local Authority – 2011*

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<b>Local Authority</b>	<b>Number of Enterprises</b>
Isle of Anglesey	4635
Gwynedd	12065
Conwy	7290
Denbighshire	6605
Flintshire	9280
Wrexham	7205
Powys	13960
Ceredigion	8625
Pembrokeshire	11650
Carmarthenshire	12545
Swansea	12720
Neath Port Talbot	5575
Bridgend	7625
The Vale of Glamorgan	7890
Cardiff	23660
Rhondda Cynon Taf	9165
Merthyr Tydfil	2560
Caerphilly	7575
Blaenau Gwent	2705
Torfaen	4260
Monmouthshire	7755
Newport	7935
<b>Total</b>	<b>193010</b>