



INSIGHT

THE CHANGING PROFILE OF THE SME



In 1971, the Bolton Report described the UK small firm sector as, “extremely large and remarkably heterogeneous”.¹ Fast forward to 2019 and it seems this description is still as relevant as it was nearly 50 years ago. However, the 1971 Report also described the SME sector as being “in jeopardy” and forecast a decline in the market. With nearly 5.7m SMEs currently operating in the UK², comprising 99.9% of all businesses, it seems fair to say this prediction has not been realised.



**5.7M SMEs OPERATING
IN THE UK**

However, the profile of the SME has changed significantly, as has the external environment it operates within. The 1970s was a world without internet; the UK was joining rather than leaving the EU, and the right to request flexible working was still thirty years in the future. The modern SME has had to adapt to such changes, which have inevitably brought opportunities, risks and challenges. Some of these are examined below.

BREXIT

With a revised date for the UK’s planned departure from the EU, it remains difficult to judge the potential impact on small and medium businesses. However, some SMEs are already reporting labour challenges due to difficulties in recruiting, combined with a growing skills shortage. This is being blamed, in part, on a lack of clarity around post-Brexit free movement rules and immigration controls, putting off workers from overseas.

¹ Bolton, J. (1971). *Report of the Committee of Inquiry on Small Firms*. London: HMSO.
² House of Commons Library (2018). *Business Statistics Briefing Paper*, 12 December 2018. [online] Available at: <https://researchbriefings.files.parliament.uk/documents/SN06152/SN06152.pdf>

In Autumn 2018, the Chartered Institute of Personnel and Development (CIPD) reported that 44% of employers had experienced greater difficulty in recruitment during 2018³, despite an enduring appetite for employing EU nationals. Certain trade sectors, such as engineering and construction appear to be most affected, with the Federation of Master Builders reporting many construction firms struggling to recruit bricklayers, carpenters and joiners.⁴ At this time of political uncertainty it's sensible for SMEs to review their workforce and assess their levels of dependency. Particularly business owners who rely heavily on EU workers need to familiarise themselves with their employees' status and rights and assess the potential impact of Brexit on their customers and suppliers.

However, Brexit could also hold opportunities for SMEs. Typically more agile and adaptable than larger corporates, smaller enterprises may find they can capitalise on the changing post-Brexit landscape through flexing their business models. This may take the form of adopting more rapid innovation, enabling them to bring products to market quicker than their larger counterparts.

THE RISE OF 'ARTISAN'

The description 'artisan' increasingly seems to adorn signage on coffee shops, cheese-mongers and bakeries, and is used to denote quality and exclusivity. Ethics seem to play a role in the rise of artisan, with many customers drawn to smaller businesses which promote niche products and the use of locally-sourced produce. As a result, UK coffee-chain sales have stalled and consumers have shown a willingness to spend more on a cup of coffee from independent outlets. Initiatives such as the annual 'Small Business Saturday' have also sprung up; this campaign aims to highlight small business success and encourages consumers to support small enterprises in their locality. In 2018, an estimated £812m was spent on such companies, compared to £748m the previous year.



Additionally, television programmes such as *The Great British Bake-Off* have been cited as a reason for the growing number of small cake-making businesses; in fact there was a reported 1,500% increase in the number of cake makers and decorators between 2012 and 2016.⁵

It's not just artisan food retailers which have seen an increase in sales but also craft and design retailers. These businesses often capitalise on online channels for selling products and are starting to match larger organisations in their use of cloud-based services and apps. This brings both advantages and risks as detailed in the next section.

3 Cipd.co.uk. (2018). *Labour Market Outlook*, Autumn 2018. [online] Available at: https://www.cipd.co.uk/Images/labour-market-outlook_2018-autumn-2018_tcm18-50460.pdf

4 Federation of Master Builders (2017). *State of the Trade Survey: Q1 2017*. [online] Available at: <https://www.fmb.org.uk/media/33387/state-of-trade-survey-q1.pdf>

5 Dellow, B. (2017). *Great British Bake Off inspires 20% surge in independent UK bakeries*. [online] Simplybusiness.co.uk. Available at: <https://www.simplybusiness.co.uk/knowledge/articles/2017/08/great-british-bake-off-inspires-20-per-cent-surge-in-independent-uk-bakeries/>



TECHNOLOGY

SMEs are becoming more digitally 'savvy' and many recognise the value of having a digital footprint in a world where the consumer is 'always on'. This ability to trade online and use an omnichannel approach has gone some way in levelling the playing field between smaller and larger businesses, allowing access to a global marketplace and enabling end-to-end trading. Technology can also assist with strengthening customer relationships and enhancing the customer journey, through such functionality as 'live chat', 'avatars' and interaction on social media platforms.

Additionally, the use of digital services has reduced the need for printing and paper storage, resulting in a lower dependency on physical premises, especially when combined with remote working options.

One challenge for SMEs can be having the financial ability to fund technology. Aside from not always possessing the cash reserves to match larger companies, SMEs also tend to evaluate their spend more closely. According to a YouGov report⁶ of 1,000 UK SMEs, 57% said price was the main barrier in adopting new technology.

A potential greater cost of technology can be the threat of cyber-attacks. In 2018, the National Cyber Security Centre (NCSC) ran a self-assessment campaign entitled "Would you be ready?" with the aim of raising awareness of this threat amongst SMEs, and providing guidance on how to mitigate the risks. This included recommending strong passwords, backing up data and educating employees on phishing and vishing attacks. Whilst businesses of all sizes are exposed to cyber-attacks, SMEs may not have the security platforms or IT resource to reduce the impact. They may also struggle to repair reputational damage without dedicated PR and legal teams.

However, with consumers increasingly choosing to purchase products and services online, technology will become a mandatory item on the shopping list for smaller businesses, in order to compete with larger equivalents.

LEGISLATION AND REGULATION

Aside from Brexit, there have been a number of market developments for SMEs to be aware of and which demand action. A significant new law affecting all businesses arrived in the form of the General Data Protection Regulation (GDPR) in May 2018. Despite it being hailed as one of the biggest changes to the regulatory landscape in years, a 2018 Allianz survey of 500 SMEs revealed that 49% were not fully aware of the implications of GDPR.⁷ With hefty fines – sometimes as much as 4% of annual turnover – this suggested a need for more education. Other implications of non-compliance include data breaches and reputational damage.

However, SMEs could also reap benefits from the new data privacy law. The need to cleanse databases will result in richer and more meaningful data. This in turn could build customer trust and promote positive relationships. Far from seeing GDPR as a burden, SMEs should view it as an opportunity to improve data management and strengthen cyber-security measures.

Another regulation which arrived in 2018 was the mandatory publishing of gender pay gap reports for any business with 250 employees or more. Whilst this meant that smaller enterprises were exempt from publishing this data, some argued that SMEs should undertake a gender pay review regardless, as part of best practice. Potentially an opportunity to blaze a trail in equality and diversity, SMEs could use this information to better understand drivers behind employee motivation, and use this information for recruiting and retaining staff.



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CULTURE AND WORKING PRACTICES

Achieving a work/life balance has never been so much in focus and the implications of not achieving this are serious. According to the Mental Health Foundation, work-related stress costs Britain 10.4 million working days per year.

SMEs have the advantage of really knowing and being able to engage with their employees, which can translate to creating a more appealing culture for the workforce. Whether this is through building modern, “trendy” workspaces or offering flexible and remote working options, SMEs are often well positioned to foster an environment of happy and motivated employees. Due to their agile nature, SMEs may offer a more dynamic and innovative working environment, unconstrained by the processes and protocols of large corporates.

On the flipside, modern SMEs often report struggles with retaining staff. This may be due to an inability to offer the same career progression opportunities or salary increases of a larger company. Competition for the best talent is fierce and puts pressure on SMEs to create incentives and reasons for their employees to stay put.

⁷ https://www.allianzbroker.co.uk/content/allianzbroker/en_gb/application/content/documents/news-and-insight/commercial/insurance-industry-supporting-smes-to-prosper/_jcr_content/documentProperties/currentDocument.res/supporting-smes-to-prosper_acom8021.pdf



THE SME OF THE FUTURE

Despite significant and ongoing change in the macro-environment, 77% of SMEs report that they feel confident about their future.⁸ Historically, SMEs have constantly proven themselves to be resilient and quick to adapt to market conditions. However, with the pace of change showing no signs of slowing, they will need to continue to evolve and embrace innovation and digitalisation. This may necessitate a preference and need for different employee roles, such as data scientists to predict risk or cyber security specialists.

Some predictions suggest that the number of SMEs will continue to grow, capitalising on their entrepreneurial nature to outperform their larger competitors. SMEs have long been a cornerstone of the UK economy, and evidence leads to the conclusion that they will remain so, for the foreseeable future.



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⁸ Collaborate UK 2018. <https://www.citysprint.co.uk>. [online] <https://cs-qa-media-01.azureedge.net/mediacontainer/medialibraries/citysprint/citysprint/downloads/collaborate-uk-2018-infographic.pdf>

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Registered in England number 84638
Registered office: 57 Ladymead, Guildford,
Surrey GU1 1DB, United Kingdom.

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