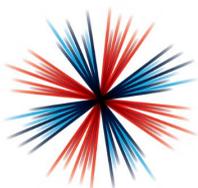




HM Government

BUSINESS PRODUCTIVITY REVIEW

November 2019



**INDUSTRIAL
STRATEGY**



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Any enquiries regarding this publication should be sent to us at: businessproductivityreview@beis.gov.uk

Contents

| | |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------|----|
| Foreword: Kelly Tolhurst, Minister for Small Business, Consumers and Corporate Responsibility, Department for Business, Energy and Industrial Strategy _____ | 4 |
| Foreword: Simon Clarke, Exchequer Secretary to the Treasury _____ | 6 |
| Executive Summary _____ | 7 |
| Business Productivity Review Actions _____ | 9 |
| Introduction _____ | 10 |
| Building our evidence base _____ | 14 |
| The Business Change Cycle _____ | 19 |
| Principles of policy development _____ | 21 |
| Realisation _____ | 22 |
| Assessment _____ | 25 |
| Navigation _____ | 27 |
| Embedding _____ | 30 |

Foreword: Kelly Tolhurst, Minister for Small Business, Consumers and Corporate Responsibility, Department for Business, Energy and Industrial Strategy

Our aim is to build a stronger, greener, future. We want to lead the world in tackling climate change, solve the Grand Challenges facing our society and make the UK the best place to work and grow a business. Fundamental to all these priorities is enabling the productivity of our businesses to flourish.



We are confident about our ability to deliver on these challenges because we are in a strong position. We have some of the world's leading businesses with globally competitive productivity and we are ranked as one of the best places in the world to start and grow a business. We also have businesses whose level of productivity is well below what can be achieved. The prize is great. The Bank of England estimates that if UK firms could move along the productivity distribution into the next quartile, then this would boost aggregate UK productivity by 13%, equating to a boost to UK GDP by around £270bn in today's prices.

By improving productivity while keeping employment high, we can earn more - raising living standards, providing funds to support our public services and improving the quality of life for all our citizens. As we exit the EU, businesses that take action to improve their productivity will increase their resilience to changing market conditions and be more globally competitive.

The Business Productivity Review was launched following the 2017 Industrial Strategy White Paper to consider what actions - by businesses, industry, and government would be most effective to help businesses to realise their productivity potential.

Through our call for evidence and extensive stakeholder engagement with leading academics, business representative groups, and business leaders, the review has identified best practice used by our leading businesses. Businesses that embrace leadership and management best practice and adopt tried-and-tested technologies are more profitable, productive and are better to work for. We need to get businesses across the country to adopt these actions and boost their own productivity.

The Business Productivity Review sets out ten key actions that will support businesses. These actions focus on evidence from What Works and tried and tested insights from the most productive businesses in the economy. They will be supported by £56m of new government investment, including funding to support business peer networks and to provide leadership training to our business leaders and the recently announced Productivity Institute.

The opportunity for businesses is there for the taking. We want to support and enable businesses, with access to the information and tools they need to make it happen. Government cannot solve these problems alone, and we will work closely with the private sector to drive real change.

A handwritten signature in cursive script that reads "kelly". The signature is written in black ink on a white background.

Kelly Tolhurst MP

Foreword: Simon Clarke, Exchequer Secretary to the Treasury

The UK has one of the most attractive business environments in the world and many businesses operating at the global frontier of productivity and innovation. A new business starts in the UK every 80¹ seconds and the UK is the top destination for European venture capital investment.



But we can do more to reach our goal of making the UK the best place to start and grow a business in the world. The Business Productivity Review examines how we can maximise the potential of all businesses and help the entire economy grow.

The review sets out how a focus on management, technology adoption, and the market for business advice can reap productivity benefits. We have responded to these findings with a £56m package of programmes announced at Budget 2018. The review's wider actions will continue to drive productivity progress and will closely involve private sector and industry partners. It is important that we continue to work collaboratively to develop joint programmes and solutions to productivity challenges.

The Business Productivity Review forms a crucial part of the Government's wider efforts to help boost UK productivity and I am committed to unlocking the productivity potential of people and places across the UK. That is why since 2010, the Government has delivered over half a trillion pounds in capital investment. This includes the biggest rail modernisation programme since the Victorian times and major projects like the Mersey Gateway bridge and Crossrail. This investment is alongside tax cuts to support business investment.

This review is timely. As the UK prepares to leave the EU, we want SMEs to be ready to take advantage of the opportunities that Brexit offers and continue to grow. We will continue to support businesses with the information and tools necessary to enable this growth.

A handwritten signature in black ink that reads "Simon Clarke". The signature is written in a cursive style and is positioned above a thin horizontal line.

SIMON CLARKE MP

¹ BEIS calculations based on BankSearch data

Executive Summary

The UK has some of the world's most productive businesses and has a strong business environment upon which we can build. For example: 1,075 businesses start every day in Britain² and we are ranked as one of the best places in the world to start and grow a business.³ Despite this, we have a longstanding productivity gap with our international competitors. Boosting the productivity of the UK's 5.9 million small and medium-sized businesses to match that of Germany could add up to £100 billion to our economy and improve the competitiveness of UK business.⁴ By making businesses aware of their potential they can seek simple measures to become more productive and grow.

The Business Productivity Review was one of the commitments set out in the Industrial Strategy White Paper. This review has been jointly undertaken by the Department for Business, Energy and Industrial Strategy and HM Treasury, and focuses on the decisions and actions taken by businesses that affect their own productivity.

We published a call for evidence on 23 May 2018 and received 146 written responses, providing views on our analysis of the role of leadership and management capability, technology adoption, and the private and public sector provision of business support in improving firm-level productivity. We have also met with over 3,000 business leaders and engaged with sector trade bodies and membership organisations that jointly represent over 500,000 businesses across the UK, including Scotland, Wales and Northern Ireland.

Responses to our call for evidence highlighted that the changes needed to improve the productivity of businesses and in turn realise growth are often cyclical and follow a number of key steps, each with their own challenges. We have taken a business-focused approach to understanding the issues holding back productivity and distilled the evidence, responses to our call for evidence, and what we heard from business into a single Business Change Cycle.

The four stages of the Business Change Cycle are:

- Realisation that a change is needed;
- Assessment of the costs of change and associated outcomes, quality and value of change, and of the business support available to help identify solutions;
- Navigation of the business support environment to find advice, or new services and products, to deliver the desired change;
- Embedding the change in the business to realise the benefits, which may require strong leadership and staff training.

This document discusses the Business Change Cycle in detail and sets out a series of corresponding policy principles which address each stage in the cycle and are the foundation for our policy recommendations. These principles have been developed from the evidence

² BEIS calculations based on BankSearch data

³ For example, the UK is ranked in the top 10 countries globally in the World Bank Ease of Doing Business Rankings 2019 and World Economic Forum's Competitiveness Index 2019

⁴ CBI (2017), From Ostrich to Magpie

presented to government through the call for evidence; direct conversations with business; international evidence; and considering what business support is proven to work.

To support realisation, we set out how a private and public sector can work together to build a movement, drive up demand and highlight opportunities for businesses to improve their productivity and potentially grow. Trusted networks and relationships are critical for the assessment stage, for businesses to find information and support. We reaffirm the importance of locally available business support for businesses to navigate the market, which must be complemented by national coordination of learning and identification of best practice. Finally, we discuss the importance of workplace skills to embed new products and processes. Together, these principles and associated policies will enable a business to successfully complete the Business Change Cycle.

This review and its underlying evidence base could provide a strong foundation for other policies including UK Shared Prosperity Fund, Local Industrial Strategies and Sector Deals, ensuring businesses have the potential to become more productive, grow and become international.

Budget 2018 announced a series of policies to increase firm-level productivity, including:

- £11m to create a Small Business Leadership Programme to provide small business leaders with leadership training, building on existing world class training programmes;
- £20m to strengthen the availability of local peer to peer networks;
- £25m through the Knowledge Transfer Partnerships to allow over 200 businesses to access the skills and talent to realise productivity growth opportunities.

We will work with the private sector to ensure businesses have access to clear advice and the tools they need to help them both understand and improve their productivity.

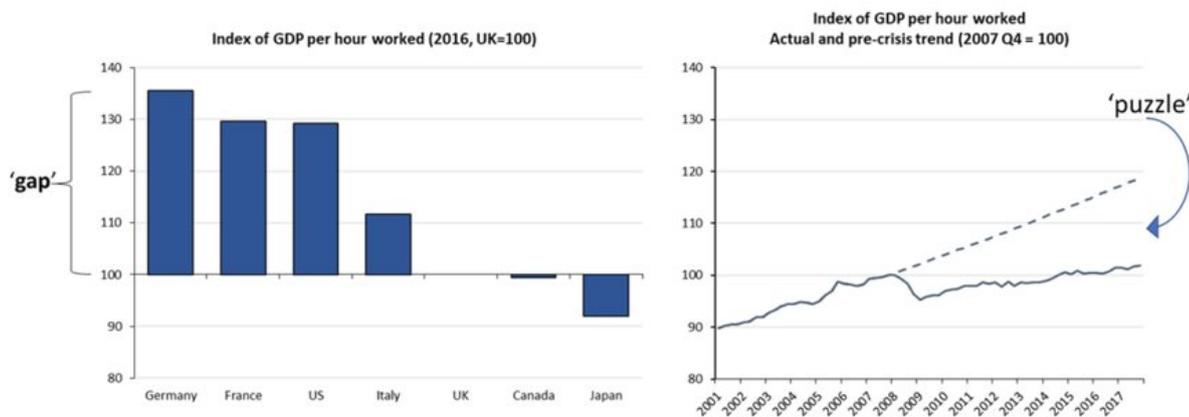
Business Productivity Review Actions

| | |
|----|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 | We are continuing to develop the evidence base on productivity through the recently announced Productivity Institute and through the BEIS Business Support Evaluation Framework. We will work closely with academics, the What Works Centre for Local Economic Growth, local support providers and the Enterprise Research Centre, to raise the standards of evaluation and disseminate best practice across the network of business support providers. |
| 2 | We will work closely with trusted intermediaries including accountants, trade bodies, sector councils, and Be the Business to propagate messaging and support to small businesses to improve business practices. |
| 3 | As part of Business Basics, we have commissioned the Behavioural Insights Team to run a series of trials on how best to communicate with small businesses to encourage them to take action to improve their productivity. |
| 4 | We will work with Be the Business to improve access to benchmarking tools drawing on ONS data promoting through key channels including local authorities, Local Enterprise Partnerships, sector councils and trade bodies. |
| 5 | We will work with trade bodies, membership organisations, sector councils and Be the Business to ensure small businesses have access to business mentors from the UK's leading and inspiring businesses to help them improve their productivity and grow. |
| 6 | The industry-led Professional and Business Services Council (co-chaired by a BEIS Minister and industry lead) will develop an action plan to increase SMEs use of professional business support services and make it easier for SMEs to find good quality support. |
| 7 | We have committed £20m to strengthen local Peer to Peer Networks focused on business improvement so that thousands of business leaders can share expertise on leadership, business development and technology adoption. |
| 8 | We will improve the customer experience for businesses accessing online government information and services addressing how businesses can grow domestically and internationally. |
| 9 | We have committed up to £11m to create a Small Business Leadership Programme to provide small business leaders with leadership training, building on existing world class training programmes; such as Be the Business' Productivity Through People, Lancaster University's LEAD and Goldman Sachs 10,000 Small Businesses Programme. |
| 10 | We are providing £25m through the Knowledge Transfer Partnerships to allow over 200 more businesses to access the skills and talent to improve their business performance and productivity by improving how well they are managed. |

Introduction

The UK has a longstanding productivity challenge; even before the financial crisis labour productivity was on average 13% higher in the rest of the G7 countries compared to the UK.^{5 6} This 'Productivity Gap' has since been exacerbated by the UK's unusually weak productivity growth since the financial crisis in 2007-2008 - referred to as the 'Productivity Puzzle', illustrated in Figure 1.

Figure 1: ONS (2018), International comparisons of UK productivity (ICP), final estimates: 2016



By improving productivity whilst simultaneously keeping employment high, we can boost our earning power - raising living standards, supporting our public services and improving the quality of life for all our citizens. By increasing collaboration and building the right skills, we can ensure everybody has an opportunity for high skilled work and high paying jobs.

Firm Level Productivity

The UK's overall productivity growth will, in large part, be determined by the performance of individual businesses. Whilst the UK has some of the most productive businesses in the world, we also have a large number of low productivity businesses.

⁵ This review focuses on 'labour productivity', which is usually defined as the amount of output e.g. Gross Value Added (GVA) per worker or per hour worked.

⁶ ONS International Comparisons of Productivity, Final Estimates 2016; pre-crisis taken to be '2007' Note: recent OECD analysis suggests the productivity gap with the UK and other G7 members may be moderately overstated, but still large relative to France, Germany and the USA.

Figure 2: The productivity distribution of UK businesses in 2015 (Source: ONS calculations using Annual Business Survey and Interdepartmental Business Register)



This review defines a low-productivity business as one with below the median productivity, which is £27,000 per worker in Figure 2. Through our call for evidence we tested whether there were many definitions of low productivity businesses commonly used but respondents did not identify any official or widely used alternatives.

There are large differences in productivity across sectors, for example average productivity in the pharmaceutical industry was £153 per hour in the second quarter of 2019, compared with £25 per hour in the retail industry. However, evidence from the Office for National Statistics (ONS) shows how low productivity businesses are found in all regions, sectors, and across all sizes of business. Indeed, there appears to be more variation across businesses within, rather than between, regions, sectors and sizes.⁷

To further our evidence base we have conducted new analysis into the characteristics of low-productivity businesses.

The untapped productivity potential amongst large parts of the UK business population further underpins the rationale for focusing specifically on firm-level factors in this review.

Our Approach

We want to build a stronger, greener future for our Country. Achieving net zero greenhouse gas emissions by 2050, solving the Grand Challenges facing our Society and making the UK the best place to work will require fundamental transformation in how our economy operates, and one that will drive stronger productivity growth.

⁷ ONS (2017), Understanding firms in the bottom 10% of the labour productivity distribution in Great Britain: “the laggards”, 2003 to 2015; ONS (2017), Labour productivity measures from the Annual Business Survey: 2006 to 2015, BEIS analysis of Annual Business Survey

Case Study: Be the Business

The government is providing up to £18.6m of funding to Be the Business to help SMEs better understand the simple changes they can make to raise their productivity levels by adopting best practice leadership and management techniques and making use of tried and tested technologies.

Be the Business is an independent charity chaired by Sir Charlie Mayfield and backed by some of the UK's leading businesses with the aim of building a movement of large and small businesses which want to improve their performance and share their experiences to help others do the same.

Be the Business provides inspiration, practical tools and free resources for businesses to identify opportunities for improvement and develop proven approaches to boost their productivity through expert analysis and advice from the business community.

Be the Business helps SMEs to improve and become more competitive through interactive digital benchmarking tools, place-based collaborative peer networks, bespoke mentoring with expert business leaders and structured executive leadership and management training.

www.bethebusiness.com

The Business Environment Foundation

We want the UK to be the best place to start and grow a business, supporting those already established here, and drawing in new investors from across the globe. We aim to create a business environment well equipped to meet the challenges and opportunities of new technologies and ways of doing business. In order to achieve that, our priorities include:

- Driving productivity improvements in businesses of all sizes all across the country by spreading the best practice, increasing collaboration, and building skills.
- Making finance available for innovative and high-potential businesses to thrive and grow.
- Helping businesses access international markets, by encouraging firms to export, and signposting the world-class support provided by the Department for International Trade.
- Continuing to develop our competition, legal and regulatory frameworks to ensure the UK remains a top world-class destination for businesses and investors.

British Business Bank

The British Business Bank (BBB) is a government-owned economic development bank that makes finance markets for smaller businesses work more effectively, allowing those businesses to prosper, grow and build UK economic activity.

BBB programmes are supporting more than £6.6bn of finance to over 89,000 smaller businesses (as at March 2019). These programmes are designed to bring benefits to businesses that are start-ups, businesses with high growth potential that are looking to scale up, and those looking to stay ahead in their market.

Case Study: Cornwall Hospitality Leaders Network (CHLN)

During 2018 and 2019, Be the Business has built a network in Cornwall made up of over 200 small and medium sized businesses within the hospitality sector, known as the Cornwall Hospitality Leaders Network (CHLN). Through this network, business leaders are coming together to share business ideas and solutions, both in person as part of masterclasses and networking events, and online via digital platforms.

Business improvement networks facilitate the sharing of best practice between firms that otherwise might not gain exposure to more efficient ways of working. To date, Be the Business' work has shown that many small and medium sized firms do not have an established or effective network of peers that they can talk with about how they manage and run their businesses, and how to become more productive.

In Cornwall, members of the hospitality network are identifying common challenges and Be the Business is helping them to mobilise around solving them. Using action learning sets, businesses are able to find common solutions to their business challenges through questioning in a structured and trusted environment with fellow hospitality business leaders and managers. This has given business leaders refreshed thinking and renewed confidence to go and develop their plans and chart a clear path to improved productivity.

Building our evidence base

We published a call for evidence⁸ in May 2018 which sought views on three specific factors that our existing evidence and analysis proved are linked to firm-level productivity:

1. Leadership and management
2. Technology diffusion and adoption
3. UK market for business support and advice

We also carried out an extensive engagement programme to raise awareness of our call for evidence and seek input from a wider audience, attending over 100 events across the UK, including visiting and meeting businesses in Scotland, Wales and Northern Ireland. This included conferences to present our thinking, hosting ministerial and regional meetings, attending workshops and meeting business owners. We engaged over 3,000 business leaders and met with sector trade bodies and membership organisations that jointly represent over 500,000 UK businesses.

Respondents broadly agreed with our interpretation of the evidence base, providing further insight and evidence to advance our understanding. Additional information was presented on the barriers SMEs face to improving their productivity and how they seek to overcome these barriers.

To further expand our evidence base we hosted an international workshop with the OECD and commissioned them to write a report⁹ on business support and productivity to improve our understanding from international evidence and best practice. This event was attended by UK and international academics and experts on business support, with participants from the UK, Portugal, Estonia, Denmark, France, Sweden, Norway and the Netherlands.

International best practice to improve SME productivity

Key findings from our joint workshop with the OECD include:

- Ambition is often crucial for businesses to realise improved growth and productivity performance; however, SME managers can often overestimate their own ability and company performance, reducing the likelihood they seek advice. It is important to raise both ambition and awareness of relative performance.
- Relatively basic practices such as implementing management best practice and making best use of technology are likely to have a big impact in businesses with low productivity.
- Good management is often the key enabler to driving up firm-level productivity and can be the stepping stone to businesses adopting other productivity improvements such as digital adoption and better working practices.

⁸https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/712342/Business_Productivity_Review_call_for_evidence_.pdf

⁹<http://www.oecd.org/cfe/leed/UK-BDS-Synthesis-Report-Final.pdf>

- Businesses often prefer to take advice from trusted sources and they look to their existing networks, such as their peers or their accountants, when taking advice. Businesses also usually take advice at trigger points, such as when faced with particular challenges requiring change, including both competitive pressures and opportunities.
- Businesses hold a lot of data and can make better use of it to understand their performance.
- International case studies also pointed to the importance of a nationally recognised brand for business support, operated by a single entity, to reduce fragmentation and ensuring a coherent and trusted public sector offer.

Looking to best practice

Through our call for evidence we tested two clear drivers of firm-level productivity: leadership and management practices and the diffusion and adoption of tried and tested technology.

Strong leadership and management practices include activity such as setting targets, analysing operations, and monitoring, managing and incentivising performance. These have been shown to be strongly correlated to firm-level productivity, with even small improvements in management practices being associated with up to a 5% increase in the growth rate of a business's productivity.^{10 11 12}

Despite this evidence, SMEs in the UK are less likely to use formal management practices and internationally we are ranked only 5th in the G7.^{13 14} Moreover, UK SMEs compare particularly unfavourably internationally on people management, which is the factor most correlated to productivity.¹⁵ Leadership and management practices therefore represent one of the greatest opportunities for firm-level productivity growth in the UK.

In regard to the adoption of tried and tested technologies, research commissioned from the Enterprise Research Centre (ERC) has shown that adoption of a range of basic technologies is associated with a productivity improvement of between 7% to 18%, depending on the technology.¹⁶ This is further backed by ONS analysis which shows the use of two or more business management technologies is associated with productivity gains of up to 25%.¹⁷

These technologies include accountancy software, customer relationship management systems (CRM), supply change management and enterprise resource planning software. Low uptake of these existing technologies has been suggested as one of the reasons for the UK's relatively poor productivity performance.

While the uptake of digital technologies has increased in recent years, as show in Figure 3, with web-based accounting software and cloud computing being used by more than 40% of

¹⁰ Bryson et al (2018), The impact of management practices on SME performance

¹¹ BIS (2012), Leadership and management in the UK. The key to sustainable growth

¹² Bryson et al (2018), The impact of management practices on SME performance

¹³ Bryson et al (2018), The impact of management practices on SME performance

¹⁴ BIS (2012), Leadership and management in the UK. The key to sustainable growth

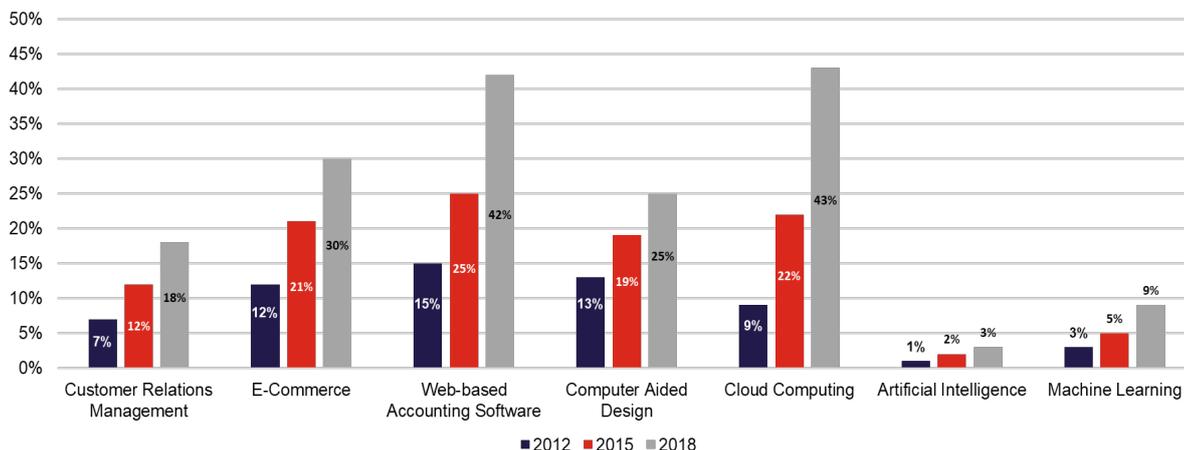
¹⁵ Bloom et al (2011), Management Practices across Firms and Countries

¹⁶ ERC (2018), Micro-Business Britain report

¹⁷ ONS (2018), Information and communication technology intensity and productivity

micro-businesses,¹⁸ ¹⁹ the proportion of UK businesses adopting these fairly basic technologies is significantly below the EU's best performers.²⁰ In 2017, the proportion of UK businesses with websites, internet trading capabilities, customer relationship management and enterprise resource planning systems were lower than the proportion of Danish businesses that had adopted them eight years earlier, in 2009.²¹

Figure 3: Percentage of micro-business adopters of digital technologies (Enterprise Research Centre- State of Small Business Britain Report (2018))



Case study: the OM Group

Damini Sharma launched the OM Group with her father in 2008 to provide health and safety services and training within the construction sector. In 2018 the business was hit hard when a number of its major clients closed following the collapse of Carillion. This prompted Damini to focus on improving productivity as she rebuilt the business and she took part in Be the Business' small business education programme 'Productivity though People' at Aston Business School.

The programme led Damini to embrace greater use of digital technology, in particular cloud technology when completing site evaluations. Being able to record evaluations in real time on tablets means employees no longer have to return to the office between client visits to update records. This use of relatively simple technology significantly reduced journey time for employees and means that the OM Group are able to make 50% more visits to client businesses each week. As a result, the business has been able to take a greater number of clients and improve levels of service at the same time.

¹⁸ CBI (2017), From Ostrich to Magpie; McKinsey (2015), 'Global growth: Can productivity save the day in an aging world?', <https://assets.mckinsey>

¹⁹ ERC (2018), Micro-business Britain Survey, www.enterpriseresearch.ac.uk/publications/state-small-business-britain-report-2018/

²⁰ OECD Science, Innovation and Technology Scoreboard, 2015

²¹ CBI (2017), From Ostrich to Magpie; McKinsey (2015), 'Global growth: Can productivity save the day in an aging world?'

The importance of existing technologies

Aside from the direct benefits to firm-level productivity set out above, the adoption of these existing technologies prepares a business for the later adoption of more sophisticated digital technologies.

Cloud computing and customer relationship management software can collect and better manage business and customer data. But it is this data that can give new insights that, in turn, support increasingly sophisticated data analytics, decision making algorithms or chat bots; and ultimately more sophisticated artificial intelligence (AI) applications with the potential to deliver greater returns.

Accenture has estimated AI and machine learning technologies could add £630bn to the UK economy by 2035.²² Our Industrial Strategy, AI & Data Sector Deal drew together a package of nearly £1bn of investment to drive these developments forward in the UK.

Case Study: Made Smarter

The Made Smarter Review,²³ led by Juergen Maier, CEO of Siemens UK, identified significant benefits to the UK manufacturing sector, and in particular for SMEs, from the development and adoption of industrial digital technology including AI, robotics, 3D printing and Industrial Internet of Things. The Made Smarter Review sets out that over ten years industrial digitalisation could boost UK manufacturing by £455bn, increasing sector growth up to 3% per year; create a net gain of 175,000 jobs whilst reducing CO2 emissions by 4.5%.

We have invested £20m for the Made Smarter North West Pilot that will provide technical and business support for manufacturing SMEs to adopt and exploit digital technologies to increase their productivity. Delivered through the 5 North West growth hubs, the pilot will engage with over 3,000 manufacturing SMEs and aims to increase regional GVA by p to £115m. It will provide up to 600 SMEs with intensive support that includes matched grant funding; leadership and management training and student placements.

We have also committed £147m for the Manufacturing Made Smarter Industrial Strategy Challenge Fund programme to develop innovative industrial digital solutions to manufacturing challenges, aiming to raise UK manufacturing total productivity by 30% and improve resource efficiency and waste reduction by 25%.

Ongoing robust analysis

In order to design, target and improve policies to best support business we need ongoing robust monitoring and evaluation of policy initiatives. This in turn allows us to identify what makes a business support programme successful, and what works less well than intended.

We have produced a new Business Support Evaluation Framework that sets out the expected quality standards for programme evaluations. This will help to ensure consistency and

²² Accenture 2018, Realising the economic and societal potential of responsible artificial intelligence in the UK

²³ Made Smarter Review 2017, <https://www.gov.uk/government/publications/made-smarter-review>

comparability of evidence across different schemes with similar aims, ultimately adding to the evidence base of what initiatives work, for whom and why.²⁴

Maintaining this robust analysis of public and private sector business support initiatives is integral to further developing our evidence base.

Action 1: We are continuing to develop the evidence base on productivity through the recently announced Productivity Institute and through the BEIS Business Support Evaluation Framework. We will work closely with academics, the What Works Centre for Local Economic Growth, local support providers and the Enterprise Research Centre, to raise the standards of evaluation and disseminate best practice across the network of business support providers.

We also continue to further develop our evidence base having committed £9m over four years from 2018 for the Business Basics programme to test and evaluate new and innovative ways to support small businesses to improve their productivity.

The review is influencing the external research agenda and spurring new avenues of work. Government is investing £43 million to support top researchers and analysts to explore how to improve UK productivity levels through a new ambitious Productivity Institute; undertaking research to understand the barriers such as productivity imbalances between sectors and regions, poor management practices and skills investment and what works to tackle them. The new Institute will support the Government's action to improve productivity, so small businesses particularly, can benefit from adopting new technologies and more efficient business practices that will boost their competitiveness. Additionally, the ESRC has £3.8 million of funding for five large scale projects on how management practices affect productivity in the UK.²⁵

We look forward to working with any external researchers looking at the topics raised in this review.

²⁴ <https://www.gov.uk/government/publications/business-support-evaluation-framework>

²⁵ ESRC, 18 January 2019; <https://esrc.ukri.org/news-events-and-publications/news/news-items/esrc-announces-3-8-million-for-successful-projects-to-investigate-management-practices-effect-on-productivity/>

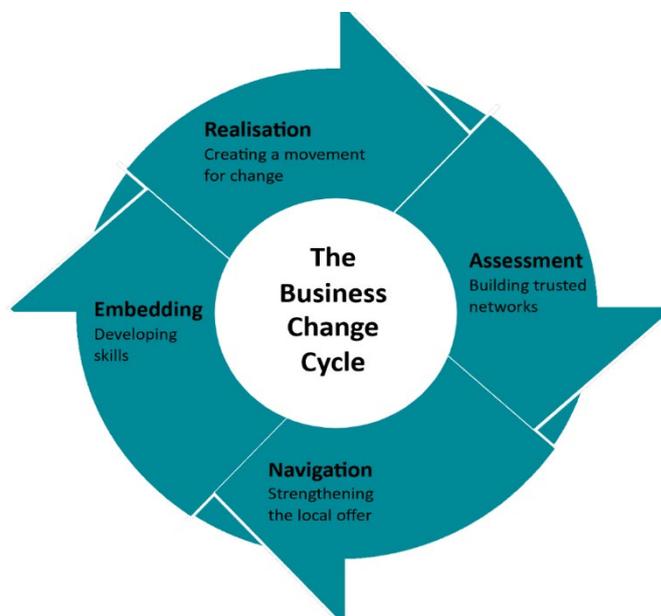
The Business Change Cycle

Businesses undergo change on a regular basis - from empowering a new member of staff or buying a new IT system to more complex restructuring.

Many of the changes made by business either require or could be better embedded with external advice. It is this constant evolution that drives improvements in business performance, increases productivity, and ultimately helps businesses become more profitable and grow.

We have taken a business-focused approach to understanding the issues holding back productivity and distilled the evidence, responses to our call for evidence, and what we heard from business into a single Business Change Cycle, set out in Figure 4.

Figure 4: The Business Change Cycle



The four stages of the Business Change Cycle are:

- **Realisation**: Enabling businesses to understand their performance, the opportunities to make changes to improve it and to drive up demand in the market. Before a business undertakes a change, it needs to acknowledge its current performance and identify an opportunity to enact a change and improve performance.
- **Assessment**: appraising the cost, quality and value of change, and the business support to help deliver it. Once a business has identified a change it wishes to make it needs to assess its options, including being able to appraise the costs and returns to the business of pursuing one option over another - in practice this means assessing which service, product, or business support advisor in which to invest.
- **Navigation**: identifying the product or advice from the business support market. Businesses will need to navigate the business support market for many of their more significant changes, where expertise is not held in house, or for new services or products they wish to incorporate into the business.

- **Embedding:** developing the skills of managers and employees to implement and embed the change. Change must be embedded in order to realise the benefits, often requiring direction and backing from business managers and the appropriate training of staff to give them the confidence and skills to embrace new processes.

This Business Change Cycle reflects almost all changes needed for a business to grow, adapt and remain competitive. However not all businesses face barriers at each stage.

We have set out four principles of policy development, one for each stage of the business change cycle. The following pages cover the stages in more depth, drawing on information presented through our call for evidence and the conversations we have had with businesses over the course of this review.

Principles of policy development

We heard many views on how businesses can and should address the challenges they face in making improvements to their performance. We have grouped these views into four principles that can help transform the approach taken by business at each step of the Business Change Cycle. These principles are supported by a series of actions that will be taken forward by Government and its partners. Many of which will assist businesses in overcoming multiple stages of the Business Change Cycle.

These principles provide the foundation of our policy recommendations:

- Realisation** —————▶ **Creating a movement for change**
- Assessment** —————▶ **Building trusted networks**
- Navigation** —————▶ **Strengthening the local offer**
- Embedding** —————▶ **Developing skills**

Creating a movement for change: business managers often require an external spark or stimulus to realise they need to make a change to stay competitive, or the awareness and motivation to realise they have the potential to improve. The increasing availability of digital tools is allowing business to measure their performance and benchmark against competitors, often identifying target areas within their business that are ripe for change.

Building trusted networks: businesses use different approaches to appraise their change options but will almost always turn to their trusted network for advice or affirmation they are making the right decision. Businesses use existing relationships with peers who may have been through a similar process, and intermediaries such as accountants and trade bodies to signpost them to the support that is right for them.

Strengthening the local offer: local businesses generally seek local support or support from trusted advisors such as their sector trade bodies. They are often unwilling and don't have time to travel significant distances for advice, so they need a strong and navigable local business support offer, provided by both the public and private sector. Once a business becomes familiar with its business support market it will build trust in its advisors and the advice, and likely return to the same advisors for future support.

Developing skills: business managers and employees need to have the appropriate training to be able to develop their skills in order to embed change. This can be generic leadership and management training or more basic skills such as digital for employees to effectively use a new system.

Realisation

Enabling businesses to understand their performance, the opportunities to make changes to improve it and drive up demand in the market place.

There are many factors that contribute to a business owner failing to enact change that could improve the productivity of their business, they may not be aware of opportunities, lack ambition or advantages held by competitors, with research showing four out of five businesses believing they are as productive or more productive than their peers.²⁶ With managers overestimating their own abilities,²⁷ ²⁸ many businesses simply do not progress past the first step in the Business Change Cycle.

There are many triggers for a business to realise opportunities to make a change to do something differently. These include: upskilling managers so they have greater awareness of opportunities open to them; using business performance metrics such as benchmarking tools; receiving ideas and inspiration from employees and sector leaders; new competitive pressures; and external campaigns, or publicly changing market trends.

Good management practices are essential to this process and have been found to be the key enabler for driving up firm-level productivity, and we set out in the Embedding chapter the actions being taken to drive up strong leadership practices.²⁹ ³⁰ ³¹ ³²

Responses to our call for evidence

- The Behavioural Insights Team highlighted four behavioural barriers that can prevent realisation of opportunities for change: fixed mindsets, present bias, the influence of information gaps, and scarce mental bandwidth. In turn, they highlighted four behavioural enablers that can assist in a business seeking change: growth mindsets, trigger events, ease, and networks.
- As well as overconfidence, respondents highlighted that a lack of time prevents business managers from creating time to seek to make improvements to their business, especially among SMEs which often need to prioritise day-to-day tasks over longer-term improvements. Some respondents believed there to be a strong relationship between businesses that placed lower emphasis on growth (what some called 'lifestyle businesses') and resistance to the adoption of technology.
- Most businesses do not recognise productivity as a term and therefore do not judge their business against it. As highlighted in the BEIS Committee 'Small Business and Productivity' report, there is a need to connect and engage with SMEs directly and

²⁶ Be the Business (2018), Overconfidence on productivity is hampering British performance

²⁷ Bloom et al (2007), What drives good management around the world

²⁸ Be the Business (2019), Raising UK competitiveness: Inside the mindsets of leaders of firms
<https://www.bethebusinessreport.com/>

²⁹ LSE Consulting (2016), The power of productivity

³⁰ ONS (2018), Management practices and productivity in British production and services industries

³¹ Bryson et al (2018), The impact of management practices on SME performance

³² IoD (2018), Lifting the Long Tail: The productivity challenge through the eyes of small business leaders
<https://www.iod.com/news-campaigns/news/articles/Lifting-the-Long-Tail>

through representative bodies to ensure they have a clear understanding of productivity and why it matters.³³

- Respondents also highlighted that many businesses lack awareness of new opportunities to adopt best practices, preferring 'tried and tested' methods over newer options. It was mentioned that this can be exacerbated when businesses are risk adverse to adopting something new, when the current model doesn't appear 'broken'.
- Whilst not within the scope of the review, respondents cited a lack of competitive pressure (regionally, or within industries) as holding back changes in work practices.

Policy Response: Creating a movement for change

Sparking business managers to realise how they could do something differently is the first step in helping them make a change, and this spark cannot and should not always be provided by government. This is why in 2017 government supported the launch of Be the Business,³⁴ an independent body set up to raise awareness of what simple steps businesses can take to address their productivity.

When business managers seek advice, they tend to do so from their trusted networks, comprising long standing professional relationships, their peers, their respective sector trade body or membership organisations. We should look to use these existing relationships to spread messaging, drive demand and help businesses access business support provision.

Action 2: We will work closely with trusted intermediaries including accountants, trade bodies, sector councils, and Be the Business to propagate messaging and support to small businesses to improve business practices.

We also know that many business managers do not think in terms of productivity when operating their business or measuring its performance, but consider metrics such as growth, employment, and profit gains instead. Business support providers, especially when publicly funded, use the language that is accessible to businesses and reflects how they operate.

Action 3: As part of Business Basics, we have commissioned the Behavioural Insights Team to run a series of trials on how best to communicate with small businesses to encourage them to take action to improve their productivity.

A business can better understand its performance relative to other businesses by undertaking simple benchmarking or carrying out data and skills audits in order to understand where they may wish to focus on making changes.³⁵ The ONS has an easy to use interactive tool that helps businesses to calculate their productivity and compare their performance to other businesses in the UK, but this website is not where businesses normally look for information on performance.³⁶ Be the Business has also developed a digital benchmarking tool linked to ONS

³³ BEIS Committee - Small businesses and productivity inquiry

³⁴ Be the Business, <https://www.bethebusiness.com/>

³⁵ Be the Business (2019), Raising UK competitiveness: Inside the mindsets of leaders of firms <https://www.bethebusinessreport.com/>

³⁶ ONS (2018), How productive is your business?

<https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/labourproductivity/articles/howproductiveisyourbusiness/2018-07-06>

and Companies House data to help businesses take the first step towards understanding their current productivity levels in relation to peers in their industry.

Action 4: We will work with Be the Business to improve access to benchmarking tools drawing on ONS data promoting through key channels including local authorities, Local Enterprise Partnerships, sector councils and Trade bodies.

The interactive tool also offers businesses tailored guidance, practical case studies and expert advice across five management areas, including leadership and strategy, people and teams or digital readiness. These diagnostic tools need to be easy to use and deliver value in order to become a trusted part of the business manager's toolkit. Government can also utilise the data it holds on businesses to assist businesses in realising they have potential to improve their businesses. Building on the successful trial using HMRC data to effectively target businesses with high growth potential, BEIS, in conjunction with HMRC and Behavioural Insights Team, is carrying out trials to identify low- to mid-productivity businesses and point them to interventions that can offer them support to improve.

Assessment

Appraising the cost and quality of business support to deliver a change, and the associated value to the business.

Businesses describe multiple factors that make it difficult to appraise the business support options available to them, including a lack of evidence to help them value making the investment, or that it will deliver the change they want to see.

Finding neutral and unbiased advice can prove challenging and can contribute to business managers lacking the confidence to commit to a decision. Businesses also recognise that considering and delivering change is a cost, with time and energy diverted from core business activities. Such barriers may prevent businesses from seeking external advice and productivity enhancing products and as such they stop trying to deliver the required change they realised was important.

Research shows that businesses seeking external advice are more likely to increase turnover, whereas businesses that have unmet demand for advice are more likely to experience a fall in turnover.³⁷ However, despite this information, recent evidence shows a downward trend in SME use of business support, falling from 49% in 2010 to 26% in 2018 that could point to wider factors, impacting on whether managers seek business support.³⁸

Responses to call for evidence

- Respondents highlighted that even when managers recognise the need for business support, the most common reasons for not seeking and using the support is insufficient information, doubts about the returns to investing in business support, relationship concerns, and credit constraints.
- Respondents also highlighted that many business managers are unable to determine the return on investment as business support is an 'experience good' that needs to be used before return can be calculated. Respondents proposed business case studies and success stories as a means to communicate the benefits to other businesses.

Policy Response: building trusted networks

With many business managers looking to their peers for trusted advice drawing on experience, we believe those business managers who have successfully overcome issues and grown a business, particularly within their sector, should lead by example and offer mentoring to other business managers.

³⁷ Longitudinal Small Business Survey, 2018 – panel report

³⁸ Longitudinal Small Business Survey, 2018 – SME employers

Action 5: We will work with trade bodies, membership organisations, sector councils and Be the Business to ensure small businesses have access to business mentors from the UK's leading and inspiring businesses to help them improve their productivity and grow.

Many respondents to our call for evidence also commented on the confusion faced when seeking support from the private sector as there are limited impartial means by which to compare and contrast the available business support. We heard that this can be exacerbated by a lack of trust in providers and technologies, that is often not helped by businesses' previous poor experience.

Action 6: The industry-led Professional and Business Services Council (co-chaired by a BEIS Minister and industry lead) will develop an action plan to increase SMEs use of professional business support services and make it easier for SMEs to find good quality support.

Navigation

Identifying the product or advice from the business support market.

Businesses describe a large, complex and ever-changing landscape of business support services, with competing voices in the public and private sector trying to market their solutions. Uncertainty surrounding the quality and suitability of advice further adds to the problem businesses face when trying to navigate the market.

While businesses look to trusted peers and professional networks for advice, they often leverage their networks and existing relationships with intermediaries to signpost and help them to navigate the business support market. Business managers learn from each other and share best practice, especially on a local level. Research has found that business networks can be an effective means for the diffusion of best practice and in turn for improving firm-level productivity.^{39 40 41}

Responses to call for evidence

- Numerous respondents echoed the complexity, fragmentation and size of the UK business support market and pointed out this complexity is found in both the public and private sector business support provision.
- Respondents trust public business support- but highlighted a confusion in being able to identify which business support was provided through the public sector, stating programmes need to have raised profile to ensure awareness of what is available to business. International best practice highlighted the importance of a nationally recognised brand for business support to reduce fragmentation and ensure a coherent and accessible public offer.
- Many respondents highlighted the sheer scale of the private sector offering can create inertia resulting from not being able to compare offers. Respondents also referenced the high volume of messaging promoting products and services that promise business growth and improvement, that can stall their decision-making and reduce their confidence in deciding which support is appropriate. This is coupled with many respondents reflecting on occasions where advice from the private sector was of lower quality than expected and did not deliver the results they needed. This can reduce trust and prevent business managers from seeking further business support.
- Many respondents highlighted the complexity and difficulty in using government's digital services, including both seeking advice on compliance and using systems required for compliance reporting.

³⁹ Fafchamps et al (2016), Networks and manufacturing firms in Africa

⁴⁰ Van Cauwenberge et al (2013), An evaluation of public spending: the effectiveness of a government-supported networking program in Flanders

⁴¹ J Cai, A Szeidl (2017), Interfirm relationships and business performance

- Business owners provided anecdotal views that they would not travel more than 30 minutes to find face to face business support and advice, preferring to seek support from their local area.

Policy Response: Strengthening the local offer

Places and a strong *Business Environment* are fundamental to the success of the UK economy. This is integral to delivering the right provisions to businesses across the UK and being unpacked further through our Local Industrial Strategies, that are building on well-evidenced and distinctive local strengths. Government has committed to the long-term future of Local Enterprise Partnerships (LEPs)⁴² that will help create stability and increased awareness of the local business support offer, particularly through the network of 38 Growth Hubs across England that they operate, enabling businesses to know where to turn for their local trusted advice

Case Study: PLATO Networking (Belgium)

The aim of the PLATO networking scheme in Belgium is to provide intensive guidance to SME managers by organising structured meetings between SME managers. These run over several sessions during the course of a year, under the supervision of highly qualified executives of large companies, acting as coaches.

The programme starts with a 2-day residential team building exercise to build trust between participants, followed by participants jointly agreeing the business issues and opportunities they wish to collectively focus and improve on over the course of the programme, resulting in it becoming highly tailored.

One study⁴³ found that participation in the scheme was associated with 2.5% higher labour productivity, another study⁴⁴ found that businesses participating in the network had 5% more assets and 7.4% higher value-added growth.

There is robust evidence that demonstrates the importance of business managers learning from peers, particularly in their local area. As mentioned in the chapter on assessment and building trust, peer networks are integral for trusted advice. They help businesses navigate multiple stages in the business change cycle, can be called on by businesses time and again, and through structured conversations they can be focused to support the specific issues faced by businesses.

Action 7: We have committed £20m to strengthen local Peer to Peer Networks focused on business improvement so that thousands of business leaders can share expertise on leadership, business development and technology adoption.

To address the concern that current sources of government information may not provide businesses with the information they require in the clearest and most efficient manner.

⁴²https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/728058/Strengthened_Local_Enterprise_Partnerships.pdf

⁴³ Van Cauwenberge et al (2013), An evaluation of public spending: the effectiveness of a government-supported networking program in Flanders.

⁴⁴ Schoonjans et al (2013), Knowledge networking and growth in service firms

Action 8: We will improve the customer experience for businesses accessing online government information and services addressing how businesses can grow domestically and internationally.

At present the vast majority of funding for local public business support is provided through European Structural and Investment Funding (ESIF), which many respondents pointed out is tied to seemingly unnecessary bureaucratic processes. The ESIF is being replaced by the UK Shared Prosperity Fund (UKSPF) and transition to UKSPF provides the opportunity to take stock of the targeting and focus of the local business support offer to ensure it best meets the local demand. The principles set out in this review will help inform our thinking about the role of business support in the UK Shared Prosperity Fund.

Embedding

Developing the skills of managers and employees to implement and embed the change.

Businesses highlighted leadership and management capability as a key factor in enabling positive change to be embedded within a business. This is supported by academic research that cites examples of 'better' management practices being adopted alongside the implementation of new IT systems achieving a much stronger productivity improvement (20 per cent) compared to when adopted with poor practices (2 per cent).⁴⁵

Within leadership and management capabilities, it is people management that is cited as particularly important for firms to realise productivity benefits from embedding changes. Research finds US multinationals obtain higher productivity from new IT systems than UK counterparts, a fact explained by higher levels of people management skills in US firms.⁴⁶ As mentioned under the best practice section, the UK compares particularly unfavourably on people management against G7 counterparts.⁴⁷

Responses to call for evidence

- Many respondents highlighted embedding change is often the stage that is most overlooked. If this stage of the cycle is not completed properly it is likely to hamper the benefit being sought through making the change, if not prove counterproductive. If unsuccessful it can prevent businesses from making further changes, knocking the business owner's confidence to be able to deliver successful change.
- Respondents echoed the academic evidence that leadership and management skills are central to ensuring change is embedded within a business. Respondents also highlighted that workers are regularly promoted to managerial positions with little or no leadership and management training, and the promotion can be a result of success in more junior roles and not indicators of management potential.
- Many respondents highlighted management skills can help overcome issues throughout the Business Change Cycle and, in particular, help businesses identify when to adopt new practices and technologies. However, respondents referenced a lack of awareness in SMEs of the benefits of investing time and money in embedding new leadership and management approaches or investing more broadly in training.
- Respondents noted that there is a wide range of leadership and management resources available through the private sector which could be better used by business leaders. However, there is likely to be issues with businesses trusting resources from unknown providers unless it is recommended by trusted sources.
- Respondents also stated it is the basic business and digital skills in the workforce that can impact the ability of a business to embed change.

⁴⁵ LSE Consultancy (2016), 'The power of productivity'

⁴⁶ Bloom et al (2012), 'Americans do IT better'

⁴⁷ Bloom et al (2014), 'Measuring and explaining management practices across firms and countries' <https://journals.aom.org/doi/pdf/10.5465/amp.2011.0077>

Policy Response: developing skills

We agree that there is a lack of trusted training provision available nationally targeted at SME business managers. Respondents stated training courses needed to have flexibility and be focused on the specific issues facing the SME managers, and not one-size-fits all.

Action 9: We have committed up to £11m to create a Small Business Leadership Programme to provide small business leaders with leadership training, building on existing world class training programmes; such as Be the Business' Productivity Through People, Lancaster University's LEAD and Goldman Sachs 10,000 Small Businesses Programme.

A limited number of strong initiatives were referenced, such as Lancaster University's LEAD, Be the Business' Productivity through People, the Goldman Sachs 10,000 Small Businesses Programme and the London Stock Exchange ELITE programme.

Case Study: Goldman Sachs 10,000 Small Businesses

The Goldman Sachs 10,000 Small Businesses leadership programme and the London Stock Exchange ELITE programme is an intensive programme delivered in partnership between Goldman Sachs and five leading universities and business schools. It comprises 100 hours of tuition over 12 one-day sessions, spread over four months, delivered through both face-to-face learning and online learning.

Participants use their own business as case studies, ensuring the training is tailored to the needs of their businesses. The 2016 ERC evaluation showed that participants grew faster than the control group of 'near misses' and found a strong boost to employment growth (17%) and turnover growth (19%), over and above what businesses would otherwise have experienced.⁴⁸

Some businesses face issues that require more bespoke skills that can be delivered through academic institutions, which facilitate the transfer of knowledge and technical and business skills into a business whilst stimulating new business relevant research in academia. Innovate UK's Knowledge Transfer Partnership programme⁴⁹ links businesses to experts and is proven to improve business performance by helping businesses become more competitive and productive.

Action 10: We are providing £25m through the Knowledge Transfer Partnerships to allow over 200 more businesses per year to access the skills and talent to improve their business performance and productivity by improving how well they are managed.

Through responses to our call for evidence and regular conversations with business managers, we heard SMEs find it increasingly difficult to recruit and retain individuals with the skills to function in the workplace. To address this concern we have announced that we will work

⁴⁸ Building Small Business Britain (2016 evaluation of the GS10KSB); Empowering entrepreneurs, accelerating growth (2014 evaluation of the GS10SB) <https://www.goldmansachs.com/citizenship/10000-small-businesses/UK/news-and-events/building-small-business-britain.html>

⁴⁹ Innovate UK Knowledge Transfer Partnership Programme, <http://ktp.innovateuk.org/>

closely with employers to give every worker the opportunity to upskill or retrain for the new economy. The National Retraining Scheme is the government's new programme to help adults retrain into better jobs and get ready for future changes to the economy, including those brought about by automation. By helping adults to retrain into better jobs, the scheme will also help to meet the needs of businesses for a multi-skilled workforce in the future. We are initially investing £100m to develop the National Retraining Scheme. This has allowed us to start delivering the first part of the scheme, Get Help to Retrain, whilst developing and testing a series of additional products that will make up the full service.

We will also be implementing state-of-the-art courses combining online learning with traditional classroom teaching to help people develop the key transferable skills for jobs of the future.

Our apprenticeship system supports apprenticeships across all sectors with a wide range of standards, including in leadership and management. As part of our reforms to apprenticeships, employers now lead the design of new standards - putting them in the driving seat to give apprentices the skills that businesses really need and creating higher quality training that will lead to a more skilled and productive economy.

Case Study: Lancaster University SME Leadership & Management Programme

Lancaster LEAD provided leadership development to over 1,700 SMEs across England and Wales, from 2004 to 2014. The intensive 10-month development programme brought together cohorts of 20-25 owner-managers who had ambitions to grow their businesses. Designed and delivered by Lancaster University Management School (LUMS), it involved an Integrated Learning Model (ILM) for SMEs, which included: coaching, masterclasses, Action Learning Sets, and shadowing exchanges.

An evaluation of LEAD showed that the programme boosted participants' leadership and confidence, and resulted in changes in management practices when returning to their organisations:

Three-quarters reported labour productivity improvements, by an average of £8,800 per year, through better use of existing employees and from organisational change.

90% of participants reported significant increases in profitability, employment or sales turnover.

The ILM was developed further under Productivity Through People, an industry-led initiative between LUMS, the Productivity Leadership Group, Be the Business and industry partners. The 12-month programme focuses on leadership, management and innovation skills and builds on key elements of the ILM, to include: site visits, case studies and mentoring by world-leading multinationals, including BAE Systems, Siemens and Rolls Royce.

The learning from Productivity through People is informing LUMS delivery of a leadership & management strand within the £20m **Made Smarter North West Adoption Pilot** (see *page 17 for more information on Made Smarter*).

We also have the Digital Skills Partnership that brings together government with private and charity sector partners to increase capability of individuals and organisations in a coordinated, collaborative way. One of its key aims is to increase motivation and digital capability among SMEs and charities, with the work overseen by a cross-sector Digital Enterprise delivery group.

Local Digital Skills Partnerships (Local DSPs) bring together regional businesses, large employers, charities, and public sector organisations to tackle local digital skills challenges and build thriving and inclusive local economies. 6 'trailblazer' Local DSPs have now been launched in the following Local Enterprise Partnership or Combined Authority regions: Lancashire, Heart of the South West, West Midlands Combined Authority, Cornwall & Isles of Scilly, Cheshire & Warrington and the South East.

Enabling a more diverse and inclusive digital workforce, that draws on the full range of talent in the UK, is also vital to address our digital skills shortages. To facilitate this, we have launched a £1m Digital Skills Innovation Fund to pilot or scale up innovative programmes that support people from underrepresented groups and disadvantaged backgrounds into digital roles.

A key theme that emerged throughout call for evidence responses and our stakeholder engagement is the importance of employee engagement, wellbeing and ensuring a diverse workforce, all of which are linked to business performance and are particularly pertinent during times of change.

Through the Business Basics Programme, government is funding several projects looking at building evidence about the role that activities aimed at improving engagement and wellbeing in SMEs can have on productivity.

This publication is available from: www.gov.uk/government/consultations/business-productivity-review-call-for-evidence

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