European Investment Bank

The EU bank

Using Financial Instruments for SMEs in England in the 2014-2020 Programming Period

A study in support of the ex-ante assessment for the deployment of EU resources

Annex Two – Area Overviews

East of England

January 2015

Disclaimer

Any disclosure of this report to a third party is subject to this disclaimer.

This report has been drafted by Regeneris Consulting Ltd at the instruction and under the supervision of the European Investment Bank (EIB) for use by the EIB and by the UK Government Department for Communities and Local Government (CLG). The contents and layout of this report are subject to copyright owned by CLG save to the extent that copyright has been legally licensed to the EIB or is used by the EIB and by Regeneris Consulting Ltd under licence.

Any views expressed herein reflect the current views of the author(s), and may not in any circumstance be regarded as stating an official position of the EIB or CLG. Opinions expressed herein may differ from views set out in other documents, including other research published by EIB or CLG.

The content of the report is based on market conditions prevailing, and on data and information obtained by the author(s) from various external sources and assumed to be accurate, correct and reliable, at the date of publication / submission, therefore changes affecting such matters after the time of submission may impact upon the content.

Nothing in this report constitutes investment, legal, or tax advice to the CLG (or to any other person), nor shall be relied upon as such advice. Specific professional advice should always be sought separately before taking any action based on this report.

The EIB cannot be held responsible for any loss or damage howsoever arising from the use of this report or of the information contained herein by any person other than EIB.

Version	**Date issued**	**Scope**
Version 2	2-02-15	Revised following comments of GDTs

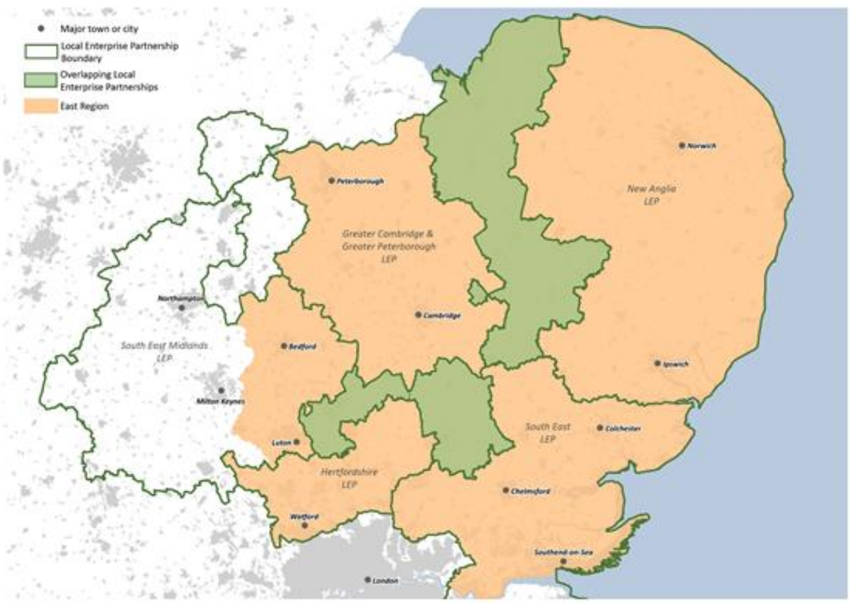
Area Overview: East of England

This section provides an overview of the SME finance market in the East of England, evidence on market failures and the implications for the overall scale and shape of market failures that could reasonably be addressed by future ERDF backed interventions for the 2014-20 programme period. **In order to interpret the overview it is necessary to read it alongside the assessment framework that is used**. These sections provide the theoretical basis for the market assessment framework used to assess the finance gap and the portion thereof that is accounted for by market failure. The assessment has been informed by an analysis of national and sub-national data and other evidence, as well as consultations with public sector organisations and the business and financial communities.

This section applies this assessment framework to the region and the overall conclusions and implications of this process are summarised at the end of the section. There are various limitations in the published data sets which are used to inform this assessment and various forms of uncertainty, all of which must be borne in mind in interpreting the assessment.

1.1 Economic Geography

Figure 0.1: The East of England Region



The East of England is home to 6 million residents, 2.6 million jobs and 226,900 businesses, 98% of which classify as micro or small[1]. Its total Gross Value Added in 2012 was £116.1 billion, equivalent to £19,700 per head of population, which compares to an England average of £21,900.

Strategic economic development policy in the region is led by three Local Enterprise Partnerships (LEPs):

- Greater Cambridgeshire and Peterborough: the economic areas around Peterborough and Cambridge covering 13 local authorities. (Note that part of this LEP stretches into Norfolk and overlaps with New Anglia)
- New Anglia: Norfolk and Suffolk counties
- South East: Essex, Southend, Thurrock, Kent, Medway and East Sussex counties totalling 32 local authorities. (Note that part of this LEP extends past the East of England region and into the South East.)

[1] Source: BIS Population Estimates. Note: This includes sole traders and businesses that are not registered for VAT or PAYE. This data is not available at a sub-regional level.

- Hertfordshire: Broxbourne, Dacorum, East Hertfordshire, Hertsmere, North Hertfordshire, St. Albans, Stevenage, Three Rivers, Watford and Welwyn Hatfield.

One of the peculiarities of the region is the anomalous position of the South East LEP in the nomenclature of English regions. The SE LEP straddles both the East of England region and the South East, which means that the analysis of SME finance needs, policy and economic profile is problematic. This is because the analysis is undertaken at regional level, including only part of SELEP's business population. Great care must be therefore taken in both interpretation and analysis to those issues relating to the East of England.

A related point is that Bedfordshire, very much part of the East of England region, is now part of the SEMLEP geography. Again, this makes an analysis of the policy context and statistical relationships harder to achieve. It also means that there are important legacy funding issues which are problematic to address.

The Greater Cambridgeshire and Peterborough LEP area contains 1.4 million residents (23% of the total population in the East of England), and 54,700 enterprises, of which 53,600 are SME employers.[2] It contributes £30 billion in annual GVA, with the main economic centres Cambridge and Peterborough where about a third of employment is concentrated.

There are 1.6 million residents in the New Anglia LEP area, with 56,600 businesses, of which 55,500 are SMEs. It is important to note that these figures for New Anglia overlap with those of Greater Cambridgeshire and Peterborough LEP. New Anglia contributes £27.5 billion per annum with a large proportion of employment concentrated in food, drink and agriculture activities and other growing priority sectors such as advanced manufacturing and logistics.

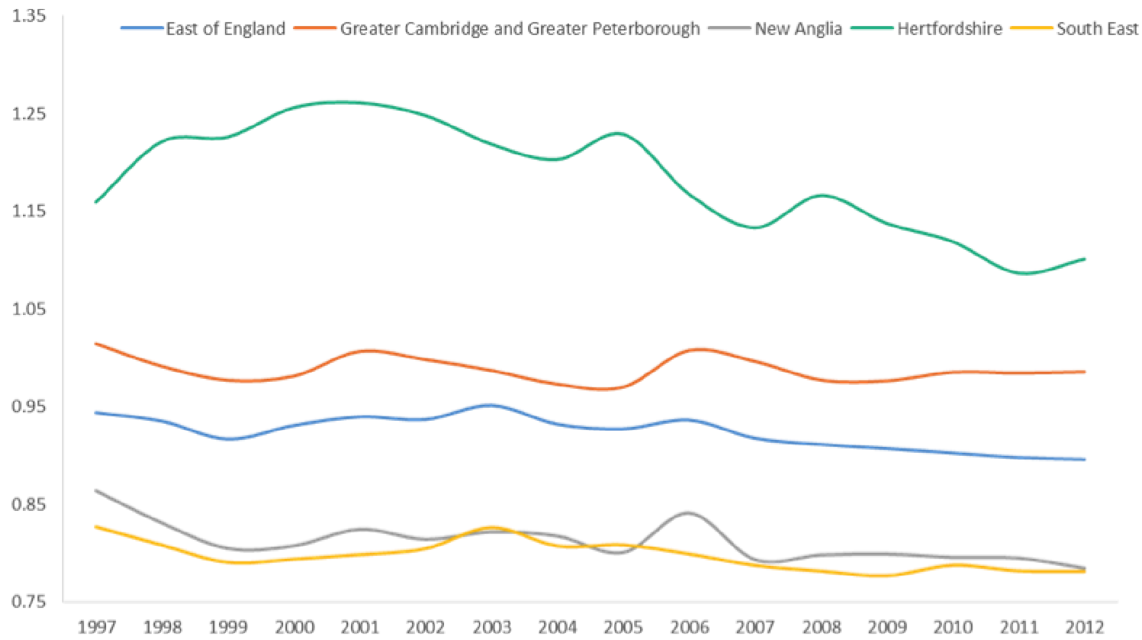
The South East LEP area contains 4.1 million residents, and 145,885 enterprises, of which 143,200 are SMEs. It is the second largest LEP in England (after London) and the largest LEP in the East of England. However, a portion of the LEP extends into the South East, straddling both regions. It contributes £63 billion in annual GVA, with significant variations across the three sub areas (Thames Gateway, Rural and Coastal). Overall, compared to the national average, the LEP has a higher proportion of jobs in construction, lower proportion of manufacturing, and is on par with England in terms of service oriented employment.

The population of Hertfordshire LEP is 1.14 million residents, with 48,800 businesses (47,800 of which are micro or small businesses). In 2012 the LEP area contributed a GVA of £27.3 billion to the national economy. The LEP area has sector strengths in life sciences, creative industries, engineering and business services.

Gross value added per head of the population in all LEP areas in the East of England has increased over the period 1997-2012. However, Hertfordshire and Greater Cambridgeshire and Greater Peterborough are the only LEPs in the region whose GVA per head consistently exceeds that of England. Since the recession, the GVA per head in the region has steadily fallen behind the national average, while New Anglia and South East LEP areas remain constant at about 78% of the national GVA per head.

[2] Source: ONS Business Counts. Note that this data source is the only one that can be used to understand the business base at a sub-regional level. It covers both enterprises and local units (which include multiple branches of the same enterprise). Regeneris Consulting have quoted the enterprise figures above. The data also only covers businesses with employees. For these reasons the SME figures quoted at LEP level differ from the regional figures from BIS Population Estimates cited above.

Figure 0.2: GVA per Head (England=100) - 1997-2012



Source: Office for National Statistics

1.2 Policy

Policy towards business support in the East of England is conditioned by the nature of the individual challenges faced by LEPs. In very general terms, the region is marked by a more rural agricultural and coastal fringe, co-existing with a sophisticated and increasingly divergent knowledge based and high technology core. This is centred on Cambridge and areas bordering the inner Home Counties. The policy context is also complicated by the proximity of higher growth areas in London and the South East, which provide access to an extremely wide market. Another point worth stressing is that a focus on the so-called 'knowledge economy' can rather deflect attention from the existing traditional manufacturing base which still thrives in the region.

A summary of the key priorities and actions identified by the LEPs, and associated investments, is set out below. There are a number of common themes within this, including the need to support existing growing businesses, support for start –ups and a focus on SME innovation. In addition there is stress on the need to support the growth of new sectors. As in other regions, this implies that there is a strategic context which would support the provision of finance in many segments of the market that is being considered. There is a particularly strong emphasis on the Low Carbon agenda, with a willingness from many public bodies to extend and strengthen current finance provision in this area.

Table 0.1: SME Competitiveness Priorities of East of England LEPs

Area	Actions identified
Greater Cambridgeshire and Greater Peterborough	Strong support for innovation – but predicated on a growth hub approach and the provision of world leading incubator space. Workshops and support is provided for SMEs relating to finance issues, but does not feature as a major policy issue in LEP strategy documents.
New Anglia	LEP Strategic economic plan focuses on five key industries (Advanced Manufacturing and Engineering, Agri-Tech, Energy, ICT Digital Culture, and Life Sciences.) The LEP has created a Business Growth Programme, to provide a framework for business support across the region. Includes commitments to six areas of activity: • Growth Hub • Business Start-Up support • Access to Finance • Encouraging Innovation • Access to markets • Rural
South East	There are four key LEP priorities: • Accelerating Growth and Innovation • Creating competitive locations • Building a 21st century workforce • Enabling Housing Growth
Hertfordshire	The LEP has key four objectives: • To encourage enterprise and business growth and build on our innovation assets. • To maintain and improve the skills and employment prospects of residents. • To identify and prioritise the strategic infrastructure required for economic growth • To secure greater investment from business and government in Hertfordshire by improved promotion and advocacy activity One of the key delivery mechanisms is a Business Hub approach.

Source: Strategic Economic Plans, European Structural Investment Frameworks

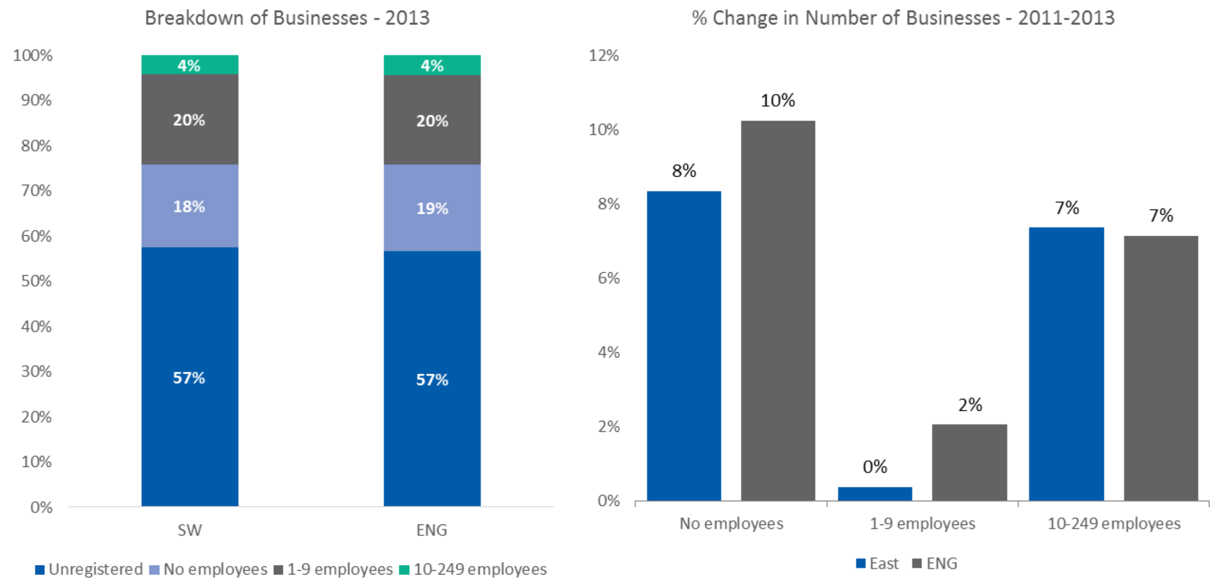
1.3 Business Demography Trends

1.3.1 Business stock

The region is home to 504,800 SMEs, of which 484,000 (96%) are micro businesses (less than 10 employees), 18,000 are small (10-49 employees) and 2,800 are medium sized firms (50-249 employees). Of the microbusiness stock, 289,200 are unregistered for VAT/PAYE and 95,600 are sole traders.

The structure of the region's business base is the same as the national level, with the greatest proportion of the SME base being unregistered businesses. Over the past few years, the East of England has seen an increase in the number of single person firms (8% increase), however this lags behind the national average (10% increase). There has been almost no change microbusinesses in the East compared to a 2% increase at the national level. However, the base of medium sized firms in the East has grown on par with England.

Figure 0.3: Composition (%) of SME Stock in 2013 and change 2011-2013



Source: BIS Business Population Estimates 2010-2013

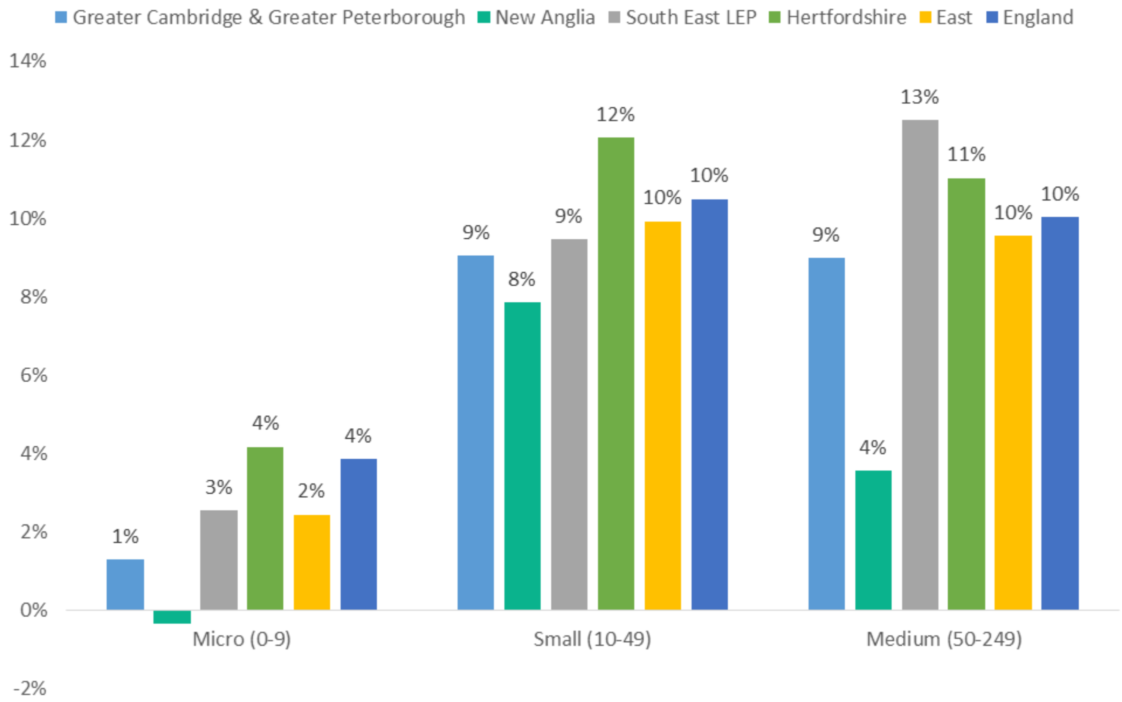
Within the region, the South East LEP area has the largest business base (135,600) followed by New Anglia (54,800), Greater Cambridge and Greater Peterborough (51,900) and Hertfordshire (48,800).[3] The composition of businesses by size band in each LEP area is similar, with each LEP area's business base comprising between 88-90% micro businesses. Across all areas, small businesses make up about 8-10% of the business base and 2% for large firms.

Hertfordshire and Greater Cambridgeshire and Greater Peterborough LEP areas both have business densities higher than the national average (35 per 1,000 residents). The highest is found in Greater Hertfordshire LEP (43 businesses per 1,000 residents), followed by Greater Cambridgeshire and Greater Peterborough with pockets of high business density located around Uttlesford, South and East Cambridgeshire, Rutland and North Hertfordshire. The South East LEP follows, with pockets of high density around Epping Forest, Maldon, Chelmsford and Brentwood.

Across the East of England, growth in the micro business base has been below the national level in all LEP areas with the exception of Hertfordshire LEP whose growth was in line with the national. Growth in the small business base has been variable compared to the national level, with New Anglia, SE LEP, Greater Cambridgeshire and Greater Peterborough lagging behind the rest of the region and Hertfordshire outperforming the national average. Growth in medium sized firms has been most variable across the region: growth in Hertfordshire and South East LEP areas exceed the national level (10%), while New Anglia's growth lags behind (4%).

[3] Source: ONS Business counts data

Figure 0.4: % Change in Number of Businesses 2011-2013



Source: ONS Business Counts

The largest proportion of the region's SME business base is in the professional, scientific and technical sector (17% equal to 38,300 businesses). The second largest sector in terms of the SME base is construction (14%) followed by information and communication (8%).

Given the size of the South East LEP area, the number of SMEs that it contributes to each sector's business base averages 55%. In other words, across the three LEPs, half of all SMEs in each sector are located in South East LEP. However, there are some sectors where New Anglia and Greater Cambridgeshire and Greater Peterborough SMEs have a higher representation. These include agriculture, where each LEP contributes roughly a third to the SME base, and public administration and defence, where New Anglia's SMEs make up 41% of the business base.

1.3.2 Business Starts

In 2012 around 25,300 new businesses formed in the region, surpassing many of the regions with the exception of the South East and London. When start-ups in the region are analysed in the context of the working age population (i.e. start-up rate), the East of England is slightly lower than the national rate. In 2012 East of England saw 68 start-ups per 10,000 working age adults, compared to a rate of 70 in England.

At the LEP level, the highest start-up rate is in Hertfordshire (87) and the South East LEP (70), however it is important to note that part of the SE LEP area falls in the South East region. Greater Cambridgeshire and Greater Peterborough LEP have a start-up rate of 63, with pockets of high performance in Cambridge, Rutland, South Cambridgeshire, North Hertfordshire and Uttlesford. New Anglia's start-up rate (52) is below the regional average and national average and has experienced a 4% decline in the number of annual business start-ups since 2009.

Table 0.2: Business Starts in East of England and its LEP Areas, 2009-12

	Business Starts				Business Starts per 10,000 WAP (2012)	
	2009	2012	Abs Change		Number	England=100
Greater Cambridgeshire and Greater Peterborough	5,300	5,500	200	4%	63	90
New Anglia	5,200	5,100	-200	-4%	52	74
South East	15,400	17,400	2,200	13%	70	100
Hertfordshire	5,700	6,300	600	10%	87	125
Total East of England	23,500	25,300	1,800	8%	68	98

Source: ONS Business Demography

1.3.3 High growth firms

Given the difficulties in defining and measuring high growth firms, there is little data available. However, the Business Growth Fund has commissioned research on high growth firms, using data from Experian UK's business database. It defines high growth firms as those that have revenues of between £2.5m and £100m, and have had 33% increase in turnover over three years, as well as 10% year-on-year growth for a minimum of two of these years. These are the kinds of firm that are likely to have a need for external finance to support this expansion.

The latest report found that 22.8% of businesses with a turnover of between £2.5 million and £100m in the region fall into this high growth category. This ranks the East of England 3rd out of the 9 English regions, with a proportion that has been steadily increasing since 2011. The region's performance in 2013 was the first year that it achieved a proportion greater than the England average.

Table 0.3: High Growth Firms as a % of all Businesses, 2011-13

	2011 Population of High Growth Firms	Regional Rank (2013)	2011	2012	2013
East of England	358	3rd	16.6%	19.9%	22.8%
England	4,044		16.9%	20.9%	22.0%

Source: BGF Growth Companies Barometer

1.3.4 Innovation activity

The East of England's innovation performance is slightly above the national average. About 46% of the businesses in the region are thought to be innovation active. While this is above the England average (45%), it is below that of other regions such as the South West (47%), East Midlands (49%) and North East (47%).[4]

R&D expenditure, in particular, that related to the private and university sectors is one driver of the spin-out and creation of companies and the demand for early stage risk finance.

Expenditure on research and development in the East of England has increased very moderately over the period 2001-2012. While overall R&D expenditure in England grew by 43% in this period, the East of England saw an increase of only 25%. The increased expenditure was seen in HERD (73% increase) and BERD (23% increase), with GERD actually decreasing by 27%. Nevertheless, the most recent data shows that in absolute terms, the region has the second highest R&D expenditure (£4,500 million in 2012), behind the South East (£6,000 million).

There have been 102 spinouts in the East of England since the year 2000, representing 11% of all spinouts in the UK. This is on par with the proportion of spinouts coming out of Yorkshire and the Humber and the North West. Almost all of the spinouts in the region have come from Cambridge University (82 spinouts). With the remainder coming from University of East Anglia, University of Essex and Cranfield University.

1.3.5 Enterprise indices

Alongside the data on start-up rates presented earlier, a number of indices provide an insight into the enterprise performance and conditions in the region.

The Global Entrepreneurship Monitor (GEM) provides frequent updates on the scale of early stage business activity, based on a survey of working age adults. Total Entrepreneurial Activity (TEA) measures the proportion of the working age population that is in the process of setting up a business or involved in a business which has been operational for less than 42 months (three and a half years). It is a commonly used indicator for assessing the extent of early stage commercial activity in an economy.

Using pooled data for 2008-13 at a regional level[5] suggest that the East of England had the second highest TEA rating of all the English regions, second only to London. It ranked above average across almost all other indicators with the exception being the proportion who intend to start up in the next three years.

---

[4] BIS (2010), UK Innovation Survey

[5] Pooling was necessary due to low sample sizes at a regional level.

Table 0.4: Measures of Entrepreneurial Activity, 2008-13

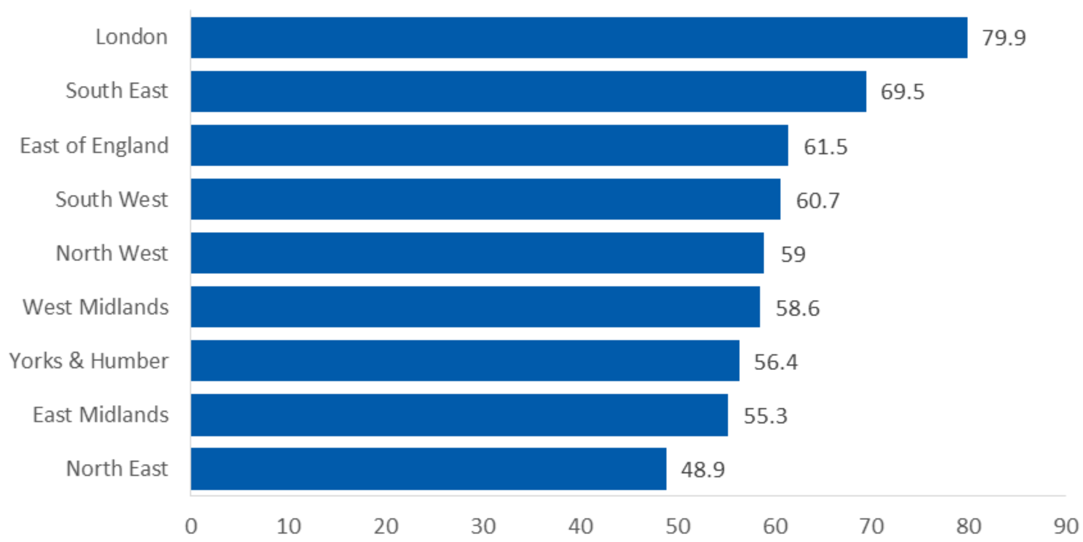
Highlighted cells shows above average results	TEA	% of Opportunity E'preneurs	Stages of Entrepreneurial Activity				High Growth Entrepreneurial Aspiration[6]	
			Intend to Start-up in Next 3 yrs	Nascent E'preneurs	New Firms	Est. Firms	All TEA	Est. Firms
London	8.2%	6.6%	8.2%	4.2%	3.8%	5.3%	22.8%	6.3%
East of England	7.6%	6.2%	4.4%	3.8%	3.7%	6.1%	16.0%	5.7%
South East	6.9%	5.5%	5.3%	3.1%	3.6%	7.6%	19.0%	4.2%
South West	6.9%	5.4%	4.6%	3.1%	3.4%	7.5%	9.6%	2.5%
Yorkshire & Humber	6.9%	4.8%	4.4%	2.9%	3.8%	6.2%	10.8%	3.5%
West Midlands	5.9%	4.2%	6.0%	2.7%	3.1%	5.6%	16.5%	5.1%
North West	5.9%	4.3%	4.0%	3.0%	2.8%	5.7%	14.4%	5.0%
North East	5.8%	4.6%	4.0%	2.8%	2.8%	4.2%	10.8%	3.6%
East Midlands	5.2%	3.8%	5.3%	2.5%	2.6%	5.9%	14.7%	2.0%

Source: Global Entrepreneurship Monitor 2008-2013, bespoke regional analysis.

The Santander Enterprise Index is an annual ranking of "the UK's regional entrepreneurial ecosystems." It uses a methodology developed by the Global Entrepreneurship and Development Institute (GEDI) to create an index for each of the UK regions, examining performance against 15 pillars of entrepreneurship. The index uses survey data on people's attitudes, abilities and aspirations with regard to enterprise and then weights these against objective measures of socio-economic infrastructure (broadband connectivity and transport links to other markets) which provide an enabling environment for enterprise.

The latest ranking for 2014 shows that the East of England is the third highest performing region, behind London and the South East. Cambridge is a local strength, ranking 1st with the highest enterprise score across all cities and towns in the UK.

Figure 0.5: Santander Enterprise Index Score - 2014



Source: Santander Enterprise Index 2014

6 % of firms looking to create 10 jobs and employment growth over 50% in the next five years.

1.4 Demand for and Take-up of External Finance

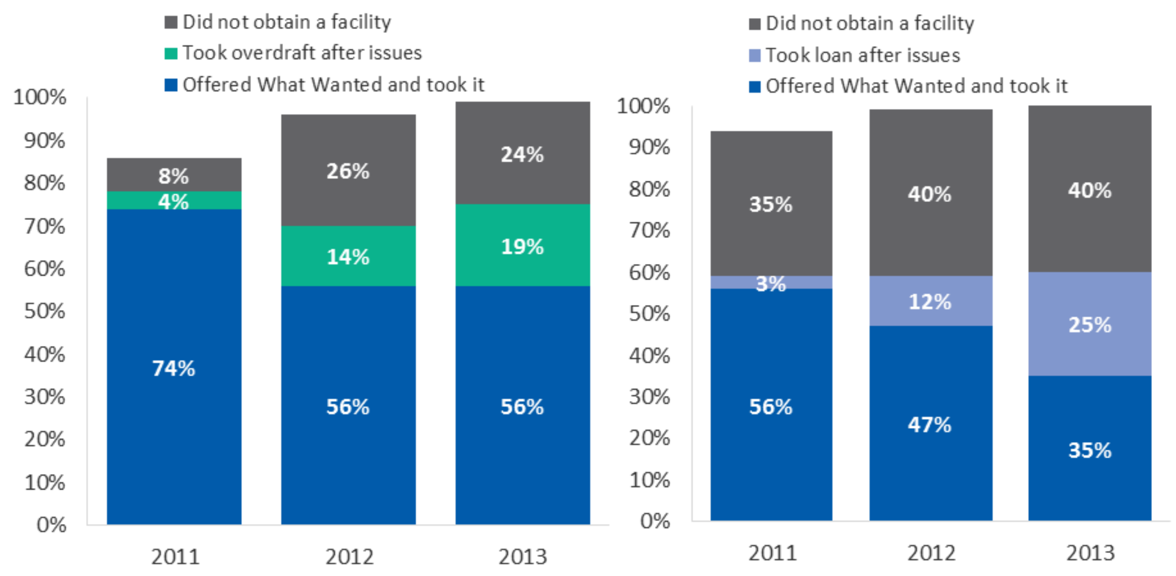
1.4.1 Survey evidence

As was set out in the main market assessment section of the report, the BIS Small Business Survey provides insights for the UK as a whole on the demand for different types of finance by region, but unfortunately it is not available regionally. The SME Finance Monitor – set up by the Business Finance Taskforce in 2010 - does provide some insight into the demand for finance from SMEs in the regions and the extent to which they are successful in obtaining the finance they are looking for. This only covers debt finance, so in looking at equity finance it is only possible to infer messages from the national SBS survey evidence. Also data is not available sub-regionally.

41% of SMEs surveyed in the East of England in 2013 had used finance of some sort[7] in the past five years. 50% had not used finance at all over this period. 34% had used either an overdraft, loan or credit card. 40% of all SMEs were classed as a "permanent non-borrower" (PNB), meaning that they have not used external finance in the last five years and have not attempted to borrow over the past 12 months, and have no inclination to borrow in the next three months. This PNB proportion has increased by 6 percentage points since 2011, which is the same percentage point increase experienced across England (6 percentage point increase since 2011).

Figure 0.6: Overdraft and Loan Applications in the East of England - 2011-2013

Overdrafts *Loans*



Source: SME Finance Monitor 2011-2013.

Notes:1) data for 2013 has small sample sizes and so should be treated with caution 2) the residual proportion is "took another form of financing"

[7] Bank overdraft, Credit cards, Bank loan/Commercial mortgage (these three form the core product category), Leasing or hire purchase, Loans/equity from directors, Loans/equity from family and friends, Invoice finance, Grants, Loans from other 3rd parties, Export/import finance.

8% of SMEs applied for a new overdraft or loan facility or sought to renew an existing facility. The proportion of SMEs successful in their application for overdrafts has decreased slightly since 2011 (from 78% to 75% in 2013), however the proportion of those successful in their application for loans has increased slightly (from 59% in 2011 to 60% in 2013). However, a greater proportion of SMEs have reported issues[8] in their application before approval. The latest data shows that for those firms that wanted to apply for a loan or overdraft facility over the last 12 months but didn't, 91% were discouraged either by the bank or indirectly because they didn't think they would be approved.

The regional data only covers debt finance, so in looking at equity finance it is only possible to assess at the national level. The only data provided in the BIS SBS is on the proportion of SMEs that were looking for equity investment. This highlights that only a small proportion actively seek out this type of finance, and that this has remained stable over time (standing at 2% in 2012, 2010 and 2008). Less than 1% were seeking mezzanine finance. This partly reflects the more niche nature of equity and mezzanine finance but also probably illustrates the lack of awareness amongst SMEs of this type of finance. The latest survey also shows an emerging awareness of alternative sources, including 1% who are aware of peer to peer/crowdfunding.

Unfortunately the survey evidence does not allow the separate review at the extent to which SMEs seeking this type of finance were successful in obtaining it.

1.4.2 Theoretical Unmet demand

Unfortunately, whilst the BIS SBS survey provides data that can be used to assess the extent of unmet demand from SMEs, this data is not available for the regions. However, the results of the UK level survey can be applied to the East of England's business base to provide indications of the number of SMEs different sizes that may be struggling to obtain the finance they are looking for, and hence the value of unmet demand.

The analysis indicates that, assuming the experience of SMEs in the region is similar to those in the UK as whole:

- In 2012 there were around 28,500 SMEs in the region looking for external finance, of which 21,800 were microbusinesses
- Of these, around 13,400 SMEs had difficulties of some sort in obtaining this finance
- 9,200 SMEs obtained none of the finance they were looking for, and 1,700 received some, but not all of what they were seeking (the national data indicates that the likelihood of successfully obtaining finance varies directly with business size).
- 6,300 SMEs had a need for finance did not apply, for the reason that they thought they would be rejected (there is no further detail available from the survey on why they thought they would be rejected).

[8] Issues is defined by BDRC as "something that needed further discussion before a loan or overdraft facility was agreed, typically the terms and conditions (security, fee or interest rate) or the amount initially offered by the bank"

Table 0.5: Illustrative Analysis of SMEs' Experience in Accessing Finance in the East of England, using Survey Data

	Total	Looking for finance	Had difficulties	Unable to obtain any finance	Obtained some, but not all finance	Discouraged from applying because thought would be rejected
Micros (1-9)	99,200	21,800	10,900	7,600	1,300	5,600
Small (10-49)	18,000	5,700	2,200	1,400	300	600
Medium (50-249)	2,800	1,000	300	150	50	50
All SMEs	**120,000**	**28,500**	**13,400**	**9,200**	**1,700**	**6,300**

Source: Regeneris Consulting calculations, using data from BIS Small Business Survey 2012 and BIS Business Population Estimates for 2013.
Note: Figure are rounded so may not sum to the totals.

It is possible to then use data on the amount of finance being sought by businesses of different sizes to generate **indicative estimates** on the scale of unmet demand over and above that being provided at the time by the private and public sectors. This analysis shows that total unmet demand in the region could be of the order of £1.7 billion in one year. It is not possible to determine from this type of analysis exactly how much of this is from SMEs that had viable business plans and propositions (i.e. those that, as a class of firms, could be supported in such a way that the financial and economic returns to the public sector from doing so would represent value for money, and hence constitutes a market failure).

However, Regeneris Consulting have set out below scenarios on the proportion of firms that might have been viable to illustrate the potential scale of market failure. For example, if 10% of these were viable, this would imply a finance gap of £5 million for microloans, £100m sought by micros seeking small loans, and a further c£80 million sought by small and medium sized SMEs. **It should be noted that this is, in effect, the gap over and above that what is already being addressed by public sector backed initiatives (including time limited ERDF backed schemes operating in the region).** The survey also implies that this unmet demand has grown over time, although this is, of course, based on national rather than regional data.

The survey does not provide data that allows Regeneris Consulting to split the unmet demand for larger amounts of finance between debt and equity finance. The SBS Survey reports that around 2% of SMEs overall are looking for equity finance. However, this does not necessarily accurately represent the extent to which equity finance might be suitable finance given the nature of their investment projects, as awareness of the benefits of this finance type amongst SMEs can be limited. Data presented by the British Business Bank suggests that around 4% of the value of finance to SMEs is in the form of equity.

Using SBS data which allows for the size of the SME and variations in the amount of finance sought by type of finance, around 8% of this overall unmet demand is likely to be accounted by equity finance (and 82% by debt finance and a further 10% by other forms of finance). This would imply a total unmet demand of around £150 million per annum for debt (if 10% of propositions were viable) and around £14 million per annum for equity (again if 10% of propositions are viable), in addition to that which is already being met by publicly backed initiatives.

Table 0.6: Illustrative Analysis of Unmet Demand (£millions) for Finance from SMEs in the East of England, using Survey Data 2012/13

	Micros (1-9)		Small (10-49)	Medium (50-249)	All SMEs
	Seeking microfinance up to £25k	Seeking larger amounts			
- those that obtained none of the finance they were looking for	£50	£920	£500	£270	£1,730
- those that obtained some, but not all, of the finance they were looking for*	£0	£40	£20	£30	£100
Total unmet demand	**£50**	£960	£520	£300	**£1,830**
Scenarios for % that are viable					
10%	**£5**	£100	£50	£30	**£180**
20%	**£10**	£190	£100	£60	**£370**
30%	**£16**	£290	£160	£90	**£550**
40%	**£21**	£380	£210	£120	**£730**

**Assumes that these firms obtained 75% of what they were looking for.*
Source: Regeneris Consulting calculations, using data from BIS Small Business Survey 2012 and BIS Business Population Estimates for 2013.
Note: Figures are rounded so may not sum to the totals.

In interpreting this analysis a number of caveats must be applied and limitations acknowledged:

- The data is based on a single survey of businesses undertaken in the UK in 2012. Since this is a sample survey the results are subject to sampling error. Regeneris Consulting have not been able to access any data from the 2014 survey as it will not be published until spring 2015. Finance market conditions in 2014 will be different from those in 2012.
- Regeneris Consulting do not know from the survey whether businesses in the East of England were more or less likely to be successful in obtaining finance than those in the UK as a whole consequently the difference between regions are explained by the differences in the size and the structure of the business base rather than the demand for finance.
- Although the survey reveals the proportion of SMEs that seek different types of external finance, it provides only very limited information on the unmet demand for these different types of finance.
- The analysis presented above only covers SMEs with at least one employee – it does not include sole traders or businesses unregistered for VAT/PAYE. Regeneris Consulting do not have any data on these businesses' experiences of seeking finance, but they account for 76% of all SMEs in the region. Including this could increase the finance gap, although the vast majority of these will have more modest finance requirements linked to growth plans.
- Similarly, this does not cover the experiences of early stage, pre-revenue businesses and then the demand for and unmet requirement for seed and start-up funding.

Whilst this analysis points to a very large level of theoretical unmet demand for finance, this calculation needs to be treated with considerable caution and should not be confused or conflated with a sensible investment range within which ERDF backed FIs should be operating, for different parts of the market i.e. the types of finance they require. There are very good reasons for this in particular:

- The calculation is based on national survey evidence, which does not provide a robust evidence base in its own right to draw sound conclusions about demand which goes unmet or is met by existing public sector backed schemes
- Experience suggests that much of this unmet demand does not arise due to market failure (as opposed to inadequate business plans), although the evidence about how much is unclear
- If the public sector chooses to use the available ERDF resources to provide finance to SMEs, it needs to do so on the basis of the absolute and comparative economic impacts and value for money it can secure (there are of course other competing demands for the scarce ERDF resources).

1.4.3 Evidence of demand from existing interventions

In addition to the theoretical exercise above, the experience from existing ERDF and other public sector backed interventions in the SME finance market can provide insight into the level of demand in various segments of the market, including that which is unmet. A more detailed discussion on the performance of these initiatives is provided in the analysis of the supply side. However, here it is worth noting the evidence on demand for the existing funds offered in the region.

The only major existing ERDF based financial instrument currently providing finance throughout the region is the Low Carbon Innovation Fund, which covers Norfolk, Suffolk, Cambridgeshire, Essex and Hertfordshire and the unitary areas of Bedford, Central Bedfordshire, Thurrock, Peterborough, Luton and Southend on Sea. The instrument targets SMEs contributing to the low carbon economy, and can invest in companies developing low carbon products or components. LCIF is a venture capital fund which makes early-stage investments as equity or convertible loans between £25k and £750k alongside co-investors. LCIF operates in a broad range of sectors and is now is now able to invest in the creative industries. Throughout its life, there has been a relatively strong deal flow, although it has benefitted from a strong marketing effort. Detailed performance data has not been provided for this fund, so this makes a full assessment of demand difficult to undertake. The latest data shows that up to June 2014 LCIF had invested £11.4m (39 investments in 24 SMEs) as part of £43.9m worth of investments. By the end of January 2015, 175 applications have been submitted, with 74 in progress and 38 successful investments completed.[9]

The fund benefits from an ERDF allocation of £20.5 million, then matched by over £30 million private sector investment; generating more than £50 million of investment in the East of England. LCIF can invest in a broad range of sectors and targets £3.5 million from the European Regional Development Fund to invest specifically in the creative industries sector.

There are a number of business grant and other support schemes in operation in some parts of the region. These include the following programmes: the East Regional Growth Loan Scheme, and the TIGER fund (Thames Gateway Innovation Growth and Enterprise) which only covers some limited parts of Essex. This is discussed in further detail below.

---

[9] SourceL LCIF Portfolio, 03/02/2015, https://www.lowcarbonfund.co.uk/LCIF/Portfolio.action

In addition to these sources, New Anglia LEP also commissioned the University of East Anglia in 2011 to examine the constraints on the provision of finance in Norfolk. Although now dated, it does provide a useful snapshot of some important sub-regional demand indicators. The report notes that Norfolk based businesses (at that time) believed that they will be turned down by High Street banks should they apply for finance. The survey also noted a longstanding aversion to equity type finance, largely explained by the traditional, family based nature of many businesses. These findings were corroborated during a number of consultations with financial intermediaries still active in East Anglia.

An overall summary of the demand indicators examined above is provided here.

Table 0.7: Summary of Key SME Finance Demand Indicators in the East of England

Microbusinesses and start-ups	• 484,000 microbusinesses in region (including 95,600 zero employees and 289,000 unregistered businesses) • Some growth in micro stock -> necessity entrepreneurs • Start-up rate 2% below UK avg but business starts growing • Strong performance in region on enterprise indices (GEM, Santander Enterprise Index) • Total theoretical unmet demand of £105 million per annum in addition to that which is served by existing interventions, £5m of which would be accounted for by microfinance
High growth early stage businesses	• Region has a good proportion of high growth firms • … and performs well on spin-outs • Almost all of the spinouts in the region have come from Cambridge University (82 spinouts). With the remainder coming from University of East Anglia, University of Essex and Cranfield University.
Established SMEs[10]	• 2,800 established SMEs (10-249 employees) • 23% of EE firms with t/o £2.5m-£100m defined as *high growth (Eng = 22%)* • Theoretical unmet demand of £80 million per annum assuming 10% of total unmet demand is viable, including small and larger loans and equity, which is in addition to that already being addressed by existing interventions

Source: Various

1.5 Supply of External Finance

The key trends in the supply of finance by market segment, are summarised below, using publicly available data. In the discussion of supply reference is made to the performance of the current available funds and other publicly backed instruments where this is available. This draws on the latest available performance data, and insights from the consultations with financial intermediaries and similar bodies. A summary table of the relevant sources of supply is provided at the end of this section.

[10] We would caveat that defining an established SME as one with 1 0 or more employees is one of several possible ways of defining established SMEs as distinct from microbusinesses and early stage ventures. Others could include using the age of the business. However, there is a lack of data available to do this.

1.5.1 Debt

As noted in the main market assessment, there has been an unprecedented shift in the landscape for bank debt for SMEs in the UK, with a vast reduction in the availability of credit following the financial crisis as banks have been rebuilding balance sheets. Although the precise dynamics vary from one bank to another, and some are more active in lending than others, to a large extent these trends are national (or indeed international) in scope, and hence affect SMEs in all of the English regions.

Nonetheless, it is worth briefly reviewing the available regional data. Sub-national data on bank debt was not available until the Business Finance Taskforce started to record lending to SMEs from Q3 2011. So whilst this data does not reveal anything about the period before this it does indicate the more recent trend.

The total value of overdrafts held by SMEs in the East of England fell between Q3 2011 and Q2 2014 from £2,401m to £962m (-60%), by a much larger proportion than in the UK as a whole (-20%). This reduction was felt by both medium and small businesses. The total stock of loans held by SMEs in the region actually increased by 2% to £6,846 million, compared to a 2% fall across the UK.

This headline data obscures the nuances of SMEs' experiences in the region. Evidence from consultations with banks and the professional advisory community confirm that businesses in the region suffered from the general tightening up of bank finance around the financial crisis, especially in particular sectors to which banks wished to reduce their exposure and for those whose businesses had a strong seasonal element. There is some survey evidence to support this from the SME Finance Monitor presented earlier. The data also obscures the reality that SMEs at the smaller end of the market, particularly microbusinesses, have been particularly affected by this readjustment

In addition to these publicly backed financial instruments, a number of grant schemes are available on a sub-regional basis. **Details of relevant schemes have only been provided by the South East LEP,** and most of the analysis provided by SELEP considers schemes available throughout the South East rather than the East of England. Given that SELEP straddles two English regions, it is therefore problematic to isolate the scope of monies available to East of England businesses. Table 6.8 shows those schemes currently available to businesses located in that part of SELEP that falls into the East of England region only (i.e. Essex). Those schemes available to businesses in other areas of the East of England are highlighted as appropriate. It should be noted that a number of the legacy schemes available in the East are currently funded but ERDF will expire over the next few six months (e.g. Low Carbon Freight Dividend, Low Carbon Keep Programme).

Table 0.8: Summary of ERDF and other funding available in Essex

Name of scheme	Funding Organisation	Geographical coverage	Eligibility	Type of finance	Size
East Regional Growth Loan Scheme	Former RDAs, funded by RGF.	Essex (EEDA Area), This scheme is also available in Essex, Suffolk, Norfolk, Cambridgeshire, Bedfordshire, Hertford	SMEs, viable, some sector exclusions.	Loans (50k to £200k	£6.5m
Foundation East	EEDA, RGF, etc.	Essex (EEDA Area), i.e. Bedfordshire, Cambridgeshire, Essex, Hertfordshire,	SMEs, open	Loans up to £100k	£1.5m

		Norfolk, Suffolk and neighbouring areas.			
Low Carbon Business	ERDF	Thames Gateway South Essex only. Expires 2014.	SMEs	Grant	£77k
Low Carbon Freight Dividend	ERDF	East of England – Essex, Thurrock & Southend (Haven Gateway) Expires 2015.	SMEs moving containers by road, 3 year programme.	Grant	2014: £1.3m
Low Carbon KEEP Programme	ERDF	Essex (in SELEP) plus Suffolk, Norfolk, Camb, Beds & Herts. Expires 2015.	Allows eligible SMEs to recoup 40% of the cost of buying capital items, **developing new products** that will help small businesses increase efficiency and reduce resource consumption. 97 businesses assisted, £6m provided to date.	Grant	£2.5m
Low Carbon Innovation Fund	ERDF	East of England Ceases investment 2015	SMEs contributing to the low carbon economy	Equity	£20m
TIGER	BIS – RGF	Dartford, Gravesham & Swale districts in Kent, Medway & Thurrock	SMEs with high growth & sustainable job creation potential. Sectors - manuf; low carbon tech; pharm & life sciences; ICT, software dev & info mangmt; media, creative & cultural inds; technology devt	Loan	£20m

Source: Access to Finance: Demand Assessment for the SE LEP Area, Center for Evaluation and Strategy Services (2014)

The UK Government has been active in trying to stimulate the flow of lending to SMEs in recent years. The main initiatives have included:

- Funding for Lending: As elsewhere the message from consultations appears to have been that Funding for Lending has not had any noticeable impact on the supply of debt to SMEs, and that lending has been focussed on mortgages.[11]
- Enterprise Finance Guarantee (EfG). The value of EfG-backed loans is the middle ranking of the English regions, behind London the SE, and the NW. The average value of loans backed by the scheme in the region is around £106k, showing that the scheme has been focussed on smaller amounts of debt, but at somewhat higher levels than what would constitute a microloan.
- The Business Finance Partnership and the British Business Bank Investment Programme provide funding to non-bank channels to invest in small and medium sized businesses.[12] To date, £73m has been invested in the region, which is equivalent to an annual average of £27 million. The average value of investment was £94k, below the English average. The overall funding secured across the EE equates to £221 per SME, which is below the England average of £500.
- The Start-up Loans initiative, set up in 2012 to help 18-30 year olds, has had some impact in the East of England. The latest statistics show that £73m in total has been allocated to 780 start-ups in the region.

Alternative sources of debt funding have had a role to play in getting debt out to SMEs in the region. The rise of debt-based alternative sources in the UK is well documented and set out in the main report. This may be playing a role in filling gaps at the lower end of the SME debt market, with the average size of loan raised in the UK being £73,000 in 2013 and 33% of borrowers believing they would be unlikely to get funds from elsewhere. There is no regional data on P2P business lending, but it has reportedly had some take up in the East of England. Consultations have reported that this is especially true in Cambridge and Cambridgeshire, where more sophisticated lending attitudes tend to characterise the more dynamic growth sectors.

There are a range of other sources of supply operating in the region. It is outside of the scope of this report to map these out in detail, but the key sources include:

- CDFIs: In the East of England, official data suggests that in 2013 **£1m** was invested by CDFIs in **372** businesses representing 4% of the national investment and 2% of the businesses. For example, Foundation East provides loans to business owners across the counties of Bedfordshire, Cambridgeshire, Essex, Hertfordshire, Norfolk, Suffolk and neighbouring areas, offering loans up to £100,000 to both start up and growing enterprises. In 2013; the organisations accounts showed that a total of £1.5m was lent, to 149 businesses (average of £10k)
- RGF backed schemes (see Table 6.8 above). For example, Finance East is working in partnership with the New Anglia Local Enterprise Partnership to deliver the New Anglia Growing Business Fund. Originally launched in April 2013, the Regional Growth Fund awarded the New Anglia Local Enterprise Partnership Growing Business Fund a total of £13.25m to provide grant funding to growth businesses across the whole of Norfolk and Suffolk. The Fund provides grants of up to 20% of the project cost, between £5,000 and £500,000, to businesses that have a shortfall in their investment plan and are able to create at least one job for every £10,000 provided by the Fund, with a minimum of one new role. Performance data is as yet preliminary, as the fund has only been in operation for less than a year. Finance East also operates the BIS supported East Regional Growth Fund Scheme, which has supported over 100 companies, agreeing more than £13m of loans and leveraging a further £27m of other finance into growth orientated SMEs

[11] Unfortunately the data on the scheme is not split between lending to businesses and lending to individuals, so it is not possible to verify this using performance data.

[12] The Business Finance Partnership ran until April 2013 and the Investment Programme has superseded it. The Investment Programme makes some money available to equity investors as well as lenders.

1.5.2 Early stage finance

As was noted in the main market assessment, the available data on the supply of early stage finance is limited in so far as much of the investment activity in this area is informal and therefore not wholly captured in published statistics. The available data from the BVCA shows that early stage investment in the East of England fluctuated significantly between 2007 and 2010: while £45 million was invested in 2007, this dropped to £20m in 2008 and £6m in 2009. After rising to £27 million invested in 2010, this figure has continued to fluctuate, dropping down to an average of £21 million in 2011 and 2013. .

A number of national initiatives have had some impact on the early stage funding landscape in the East of England. These include:

- The Angel Co-Fund. This £100m Fund was launched in November 2011 with a grant from the Regional Growth Fund. The aim has been to invest between £100k and £1 million in high potential businesses, and to leverage significant co-investment from business angels. It invests in both early and later stage businesses. The latest monitoring data indicates that a total of £8.8 million (including investment by co-investors to the ACF) has been invested in the East, in 7 companies. This represents 10% and 14% of the value of investment and number of companies in the UK, respectively. Regeneris Consulting do not have access to regional data on leverage but at the national level to date £3.80 has been levered in from business angel syndicates for every £1 invested by the ACF itself. At this stage it is clearly too early to judge the level of returns – the data available to us is at the national level, which states that one exit has been achieved at a 3 times return.
- Enterprise Capital Funds were originally set up in 2005 as a government-backed scheme with the aim of investing up to £2 million in early stage companies. ECFs operate as private companies that back private capital with Government-guaranteed leverage. The limit on the amount that ECFs could invest into any one fund was £25m, which has recently been increased to £50m. The ECFs are typically UK-wide Funds, although regional funds have been supported. For various reasons, two thirds of the value of investment made to date has gone to companies based in London, South East and East of England. There are two ECFs based in the East of England, including the first so-called super ECF – IQ Capital, which has the ability to invest up to £5m into individual companies. The latest monitoring data shows that 18 investments have been made in the East of England to date, with a value of £29 million (including co-investment).
- UK Innovation Investment Fund. This Fund provides capital for existing venture capital funds, with a total capital of £330 million (of which £150m has come from the UK Government and £180 million has come from the private sector). It is targeted at small businesses with growth potential and new ventures in the digital, life sciences, clean technology and advanced manufacturing sectors. Regional data is not available for this fund.
- Aspire Fund. No regional data is available.
- Tax incentives. Collectively tax incentives are the biggest intervention in the UK equity market by value. The Enterprise Investment Scheme (EIS) provides 30% tax relief for investors making an investment of up to £1m in any tax year. SEIS is a derivative of EIS, which aims to encourage seed investment in early stage companies. Investors receive tax relief of 50% on investments up to £100k and Capital Gains Tax exemption on any gains in SEIS shares. ONS data based on HMRC returns shows that a total of £135m has been invested through the EIS scheme, in 485 enterprises over 2009-2012, an annual average of around £45m. This is equivalent to £372 per SME employer, which compare to the English average of £650.There appears to be a general consensus from our consultations that these initiatives have had a strong impact in bringing forward investment from business angels and High Net Worth Individuals in the early stage arena.

Again, alternative funding sources have also played a role in this market, including equity based crowdfunding platforms. These are much smaller in scale than P2P platforms: the latest review of the UK market found that equity based crowdfunding amounted to £28 million nationally, representing very strong growth from the estimated £4m in 2012 (the average amount of money raised was £199,000). Consultations suggest that these routes have had little penetration in the East of England to date. Reward-based crowdfunding (where individuals donate to fund a project with the expectation of a non-financial reward in the event of its success) has also had little penetration in the region.

Whilst these platforms may play some role in early stage finance in the region, the view – supported by consultations across the country – is that they are very unlikely to serve all of the needs of early stage companies. Some of the consultees have made the point that mechanisms are well suited to project finance but much less well suited to building new, innovative businesses, given the need for a longer term commitment of funds through several rounds of funding and the potential for significant dilution for the initial investors. Further, given that these forms of financing are at an embryonic stage there remains potential for significant levels of write offs to come through from the investments made to date, which would impact on the reputation of the platforms.

1.5.3 Later stage growth finance

The BVCA also publishes data on later stage growth deals completed in the region (privately and publicly backed). According to this data the level of investment has steadily increased from 1998 when annual investment was £267 million to 2010 when it had risen to £739 million. While the overall trend has been positive, there were years of decline, particularly 2000, 2002 and 2004 when average annual investment was £152 million. After reaching a peak in 2010, annual investment figures in the East of England have been much lower over 2011-13, averaging £236 million per annum. The number of companies invested in each year has steadily declined since 2006 (98 companies) to 2010 (46 companies) and remaining steady thereafter. Given the role that business confidence plays in driving demand for this type of investment, these Funds faced a more challenging climate than the other Funds. Unlike businesses in their early stages of product and business development, established SMEs can easily postpone growth projects whist they wait for conditions to improve. The consultations suggest that this happened in the East (as it did in other regions), particularly around 2010 and 2011.

There are also several UK level initiatives in this space, from both the private and public sphere:

- **The Business Growth Fund (BGF)** was set up in July 2012 and is backed by a syndicate of banks with £2.5 billion of capital – it focuses on growth equity and mezzanine finance, offering £2m-£10m. It is designed to be an evergreen fund. Published data on the Fund's portfolio indicates that only three investments for a total of £16m has been made in the East of England to date (compared to an average investment of £5.6m in England). This chimes with the comments from stakeholders that the Fund is investing in larger propositions in the £2m-£8m range.
- **Enterprise Capital Funds is the British Business Bank scheme that** can also invest in later stage businesses (see above).

Based on the information supplied to Regeneris Consulting by LEPs, the Department for Communities and Local Government, and through consultations, there are no other ERDF or British Business Bank equity schemes operating in the region. This stands out in contrast to many other areas, although proximity to the London investment market, the sophisticated nature of investor relations in Cambridge, and a long standing history of equity aversion in the coastal and rural fringes goes some way to explaining this. Some private schemes are however available, including several Business Angel programmes run by the FSE Group.

An overall summary of the key sources of supply of finance to SMEs is provided below. It should be noted that there are significant overlaps between the sources (for example, EfG backed lending is a subset of total SME lending; some funding sources will have provided co-investment for others). Nonetheless, it gives a useful summary picture of the supply side in the region.

Table 0.9: Summary of Key Sources of SME Finance Supply in the East of England (England averages in brackets)

	Average annual value of Investment £m	Average value of investment made, £000s	Value per SME, £	% change in value 2011-13
Debt				
New loans to Small Businesses (BBA data)	£1,011	£83 (£82)	£8,426 (£7,300)	-16% (-12%)
New loans to Medium sized businesses (BBA data)	£1,033	£337 (£295)	£8,615 (£11,300)	33% (1.5%)
New overdrafts approved for Small Businesses (BBA data)	£309	£17,962 (£15,590)	£2,577 (£2,100)	-33% (-25%)
New overdrafts approved for Medium sized businesses (BBA data)	£218	£106 (£81)	£1,819 (£2,200)	-7%% (-5%)
Enterprise Finance Guarantee backed lending (Business Bank)	£36	£100 (£100)	£296 (336)	NA
Start-up Loans (Business Bank)	£2	£5 (£9)	£21 (£65)	NA
Business Finance Partnership & Investment Programme (Business Bank)	£27	£94 (£207)	£221 (£500)	NA
Equity				
Early stage equity investment (BVCA)	£28	£1,202 (£1,081)	£230 (£356)	132% (24%)
Expansion equity investment (BVCA)	£17	£1,310 (£4,830)	£141.71 (£584)	22% (62%)
Angel Co-Fund (Business Bank)	£3	£1,260 (£1,832)	£25 (£30)	NA
Enterprise Capital Funds (Business Bank)	£7	£1,610 (£1,335)	£31 (£27)	NA
Enterprise Investment Scheme (EIS) (HMRC data)	£45	£277 (£344)	£372 (£650)	14% (66%)
Business Growth Fund	£3	£5,400 (£5,617)	£41 (£77)	zero in 2011/12
Equity-based crowdfunding (NESTA)	£2.1	NA	£7.87 (£26)	(46%)
Other crowdfunding (reward-based, donation) (NESTA)	£1.7	NA	£14.7 (£35)	NA
LCIF	Est £4.5m based on 2 years of operation	Est £240k	NA	NA

Source: BBA, BVCA, NESTA, HMRC, BGF. Note: a detailed explanation of the sources and coverage of the data is provided in Appendix. Notes: [1] Based on five year average

1.6 Implications for Future Public Sector Backed Funds

This section brings together the results of the preceding analysis to draw out the high level implications for future public sector backed SME finance schemes during the 2014-20 programming period in the region. This is done with reference to the area based market assessment framework presented in the main report. **The final two steps of the assessment framework will be completed as part of the block two element of the ex-ante assessment**.

The assessment against the steps in the framework is provided in the table below.

<table>
<tr><th></th><th>Micro Loans</th><th>Early Stage VC</th><th>Debt for Growing,
Established SMEs</th><th>Expansion Equity for
Established SMEs</th></tr>
<tr><td>Step 1 - Demand and Supply Characteristics</td><td>• 484,000 microbusinesses in East of England (including 65,600 sole traders and 289,000 unregistered businesses)
• Good performance on enterprise indices; with start-up rates only slightly lower than the national average. Strong performance of Cambridgeshire and surrounding region.
• Unusually sharp reduction in overdraft provision by the major High Street banks.
• Range of schemes (CDFIs, local grant and loan schemes, start-up loans) operating in the region filling some of the gap at lower levels. Includes successful Foundation East partnership. However, many existing grant and sector loan programmes are due to end in the period up to 2015.</td><td>• Region has dynamic pockets of highly innovative research and production, and strong performance on enterprise indices
• But significant number of university spin outs based on Cambridge and other nationally recognised universities.
• EIS has had some impact on supply of co-investment, but less active than England average.</td><td>• 21,000 established SMEs in the region
• National reduction in bank lending has been felt in region – particularly in terms of overdraft provision to small businesses
• Reasonably strong take up of EfG in the region, close to the England average
• Other initiatives (BFP and Investment Programme) appear to have had less traction.
• P2P lending has had significant growth – impact on the region unclear and remains low in context of overall lending. Highly concentrated in certain sub-regions (Cambridge part of the Thames estuary).</td><td>• 21,000 established SMEs in the region
• 22.8% of businesses in region defined as high growth. East of England ranks 3rd of all English regions
• Demand for expansion equity hit by decline in business confidence but some signs of recovery
• Equity aversion remains a long term cultural issues amongst SME owners in the region, particularly in the rural and coastal fringes
• Few mainstream providers, generally focussing on fewer, larger deals (e.g. BGF age investment of £5.4m)</td></tr>
<tr><td>Step 2 – Unmet Demand</td><td>• Solid evidence pointing towards particular difficulties experienced by micro-businesses in obtaining finance
• Theoretical unmet demand of c.105m p.a. if only 10% of rejected firms had solid business plans (in addition to the gap being addressed by current public sector backed measures).</td><td>• Improved economic climate – leading to more start-ups.
• Current Lack of strong evidence of demand unmet from mainstream sources, but this may change given higher growth for knowledge based industries.
• Other sources potentially filling some, but not all of the gap.</td><td colspan="2">• National survey data suggests around 40% of small and 30% of medium sized businesses have problems accessing finance, and this has grown in recent years
• Not possible to split theoretical unmet demand calculation for debt vs. equity, but unmet demand for established SMEs as a whole amounts to c.£80m p.a. even if only 10% of rejected firms had solid business plans (in addition to the gap being addressed by current schemes)</td></tr>
<tr><td>Step 3 – Market Failure</td><td>• Only existing regional ERDF backed fund has solid demand profile, but assisted by strong marketing effort.
• Regional evidence base is compromised by statistical difficulties associated with ambiguous geographical position of schemes operating in SELEP area.
• Many current grant based schemes are due to end within the next 24 months.
• Strong consensus amongst consultees</td><td>• Little consensus amongst consultees of a structural long term equity gap at the early stage.
• Commitment to Herts based scheme to use public agencies to kick-start wider private sector provision</td><td>• Evidence on bank lending suggests amplification of pre-existing market failures in region.
• Existing structurally focused ERDF schemes (Low Carbon Freight, KEEP etc) due to expire.
• Also evidence from other initiatives (e.g. LCIF) of market failures in specific sectors.</td><td>• Demand hit by business confidence – also long term issues of equity aversion, especially in rural and coastal areas.</td></tr>
</table>

	of a structural long term funding gap at microfinance level.			
Step 4 – Persistence of Market Failure	• Consultations suggest banks likely to continue to focus on asset-backed, larger propositions in coming years • Market failure likely to continue for foreseeable future. • Evidence from Foundation East suggests continued reluctance of banks to lend.	• Evidence suggests mainstream players will continue to focus on larger, de-risked propositions • Little to suggest any changes in supply side provision outside of Cambridge and areas closer to London markets.	• Banks under continued pressure from regulation and increasing cost of capital – consultees view suggests unlikely to return significantly to SME market • P2P has grown but future path and sustainability unclear. Stronger performance in Cambridgeshire heartland, and in creative and high tech industries. • Economic recovery points towards increase in demand for debt and therefore potential increase in unmet demand.	• No sign of mainstream players moving away from fewer, larger deals, potentially leaving a gap at lower levels of equity/mezzanine. • Economic recovery suggests demand for expansion could pick up and therefore increase unmet demand and market failure • Caution required: equity aversion still an issue in region.
Step 5 – Specific Economic Development Priorities	• Support for new businesses through start-up programmes identified as a priority for LEPs throughout region • Interventions to develop enterprise culture (e.g. through education) are emphasised in LEP strategies • **Analysis to be further tested and reviewed as part of Block two work**	• All LEPs place emphasis on SME innovation and are putting in place a range of related interventions • **Analysis to be further tested and reviewed as part of Block two work**	• Supporting the growth of existing businesses highlighted as a priority by all LEPs • Range of associated business support actions are supported • **Analysis to be further tested and reviewed as part of Block two work**	
Step 6 – Delivery Capacity	A limited track record in the region of delivering publicly backed Funds. LCIF and other interventions have helped to develop an embryonic infrastructure, linkages and networks in the region, but this is heavily centred in certain sub-regions. CDFIs more active than national data suggests, therefore stronger delivery potential. **Analysis to be further tested and reviewed as part of Block two work as the potential investment strategy and delivery options are developed.**			