

Coventry & Warwickshire
Economic Assessment
TOPIC PAPER 2

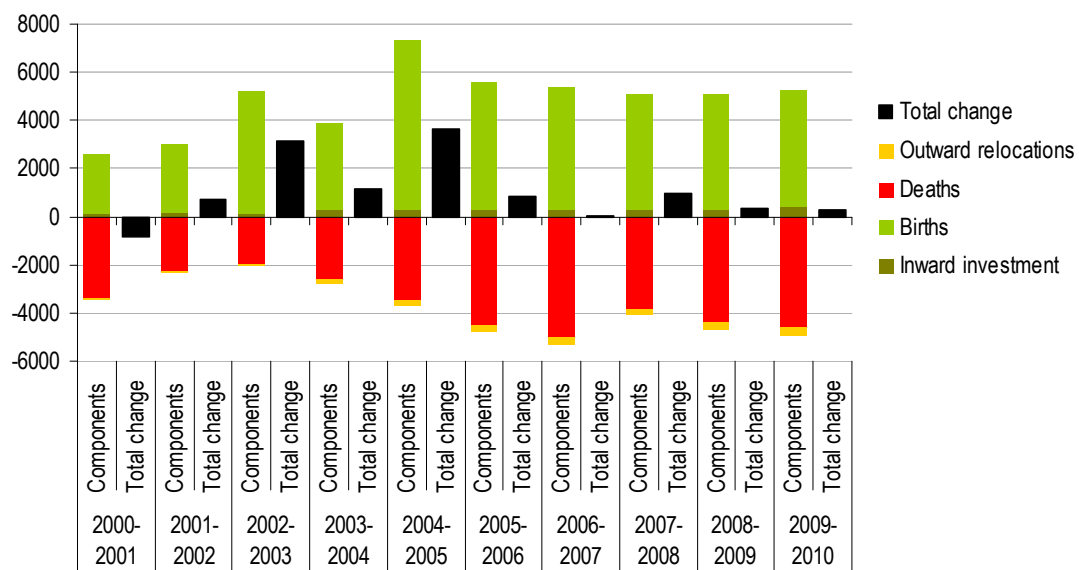
Enterprise & Business Growth in Coventry & Warwickshire

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New business starts are the overriding driver of growth of the sub-region's business base. 95% of all the new businesses within the sub-region over the last ten years have come from new business starts (as opposed to existing firms relocating to the area). The sub-region has also seen significant business churn (the rate of business replacement) – over the past 10 years, it is estimated that nearly 46,000 new businesses have started, and almost 36,000 businesses have closed. Business churn is generally regarded to be healthy for an economy, as new, more efficient and productive businesses replace older ones, increasing overall competitiveness. Figure 1 below highlights these changes, and also shows that net new business growth was strong in the early part of the decade but tailed off in later years despite new business formations remaining fairly constant.

Figure 1: Composition and change in year-on-year business growth



Source: BETA Model

There is significant variation in business start-up performance across the sub-region. The standard methodology for calculating relative enterprise performance is to look at the number of new starts per 10,000 population. On this measure, Nuneaton & Bedworth (40.7 starts per 10,000 population) and Coventry (47.0) perform quite poorly – the England average is 57.2. On the other hand, Stratford-on-Avon and Warwick Districts perform very well (with rates of 75.9 and 71.0 respectively) – making them some of the best performing areas in the country. The sub-region as a whole performs close to average, with a combined rate of 56.7 per 10,000 resident population.

However, population based statistics often favour rural areas (that generally have smaller numbers of residents) and ignore the possible agglomeration benefits from existing concentrations of businesses (areas that already have high numbers of existing businesses can help create more market opportunities for new business starts). Urban areas therefore often have higher birth rates of businesses (number of starts as a percentage of the existing business stock), while rural areas often perform better on population based measures. To overcome this, a Combined Enterprise Index can be calculated, which brings together both these elements and compares the overall performance with the England average (indexed at 100). Figure 2 below shows the combined index significantly improves Coventry's relative performance,

with rates now around the England average. The south of the sub-region still performs best of all, and the north the weakest – although they were close to the England average until the latest year of available data (indeed, all areas of the sub-region have seen a relative decline in performance compared to England in 2008).

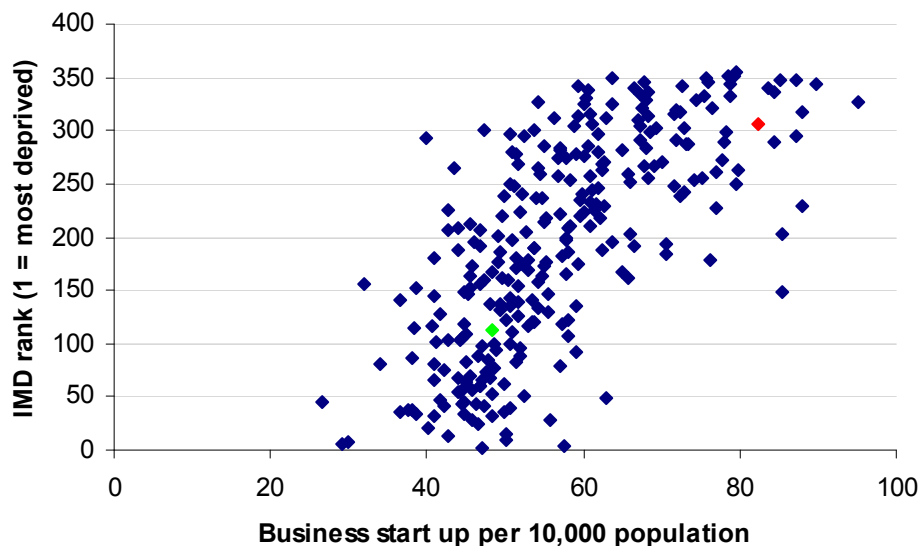
Figure 2: Combined Enterprise Index (2004-2008)



Source: ONS

Variation in new start-up rates is often also associated with deprivation levels, with local authority areas that have higher levels of deprivation often having lower business start-up rates – see Figure 3.

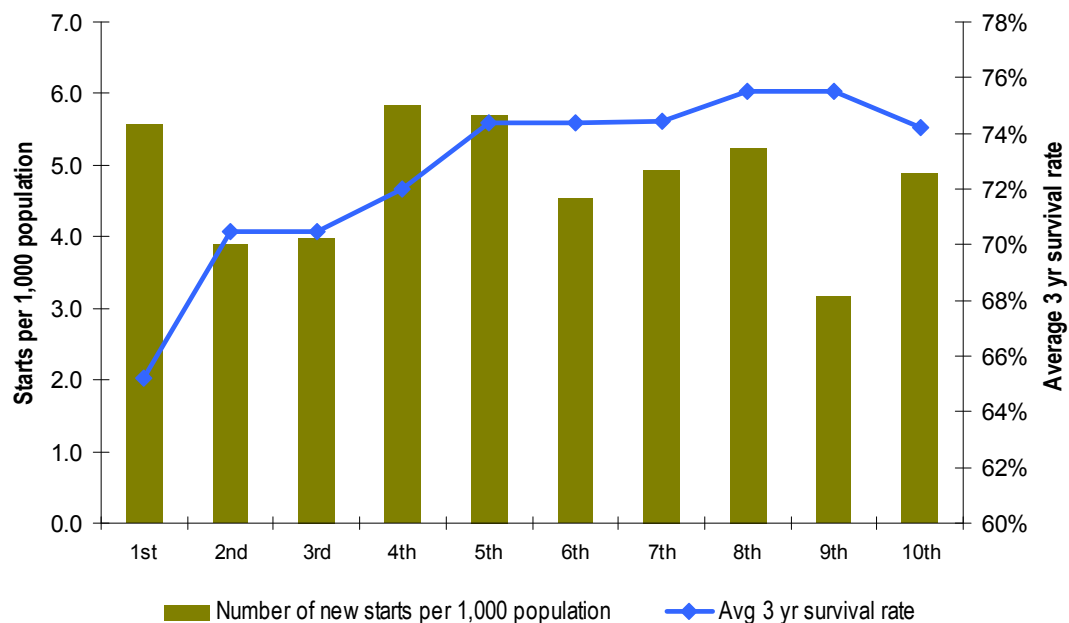
Figure 3: Business start up rates and levels of deprivation (UK)



Source: BERR/CLG

Figure 4 below therefore explores new start-up rates across the sub-region in wards grouped into deciles of deprivation (i.e. breaking the 123 wards in total in the sub-region into ten based on their relative levels of deprivation, with 1 being the most deprived). Perhaps surprisingly, this shows that the most deprived tenth of wards in the sub-region actually has one of the highest new start-up rates, and the most prosperous areas have some of the lowest. It should be noted, however, that the source for this data is the BETA model, which includes a much greater range of businesses than the “official” statistics from ONS that rely on information with respect to registration for VAT or PAYE (which is used for Figure 3 above). The BETA model includes smaller businesses that fall below these thresholds, and which are likely to be more predominant in more deprived areas. Figure 4 does, however, clearly show a strong level of enterprise within the more deprived parts of the sub-region which are often overlooked in the more standard data-sets. Of particular concern, however, is the survival rates of these businesses. The average 3-year survival rate is some 10% lower in the most deprived parts of the sub-region as compared to the least deprived wards. The steady increase of survival rates as deprivation levels improve is also interesting and perhaps worthy of further consideration and analysis of the key drivers and factors behind business failures.

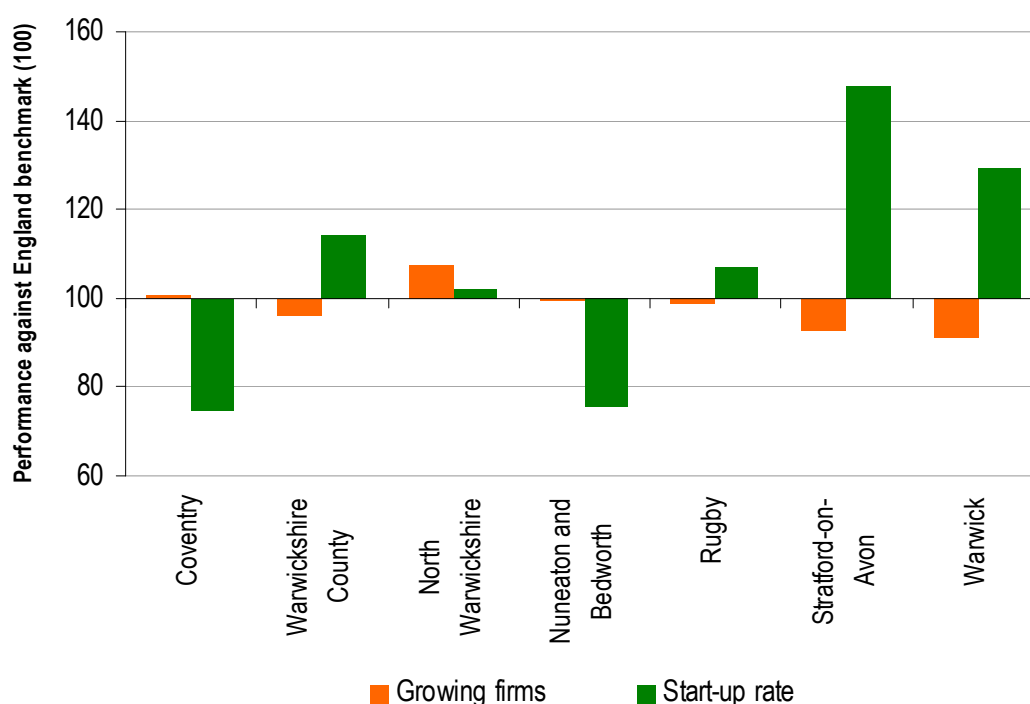
Figure 4: Start-ups and survival rates by decile of deprivation in wards in Coventry & Warwickshire



Source: BETA Model

While the sub-region has performed reasonably well in terms of new business starts – and the south of the sub-region particularly well – we have not seen such a good performance with respect to employment growth. Indeed, the difference between business starts and business growth (in terms of numbers employed) within the sub-region is quite apparent, as shown in Figure 5. While Stratford and Warwick Districts have well above average start-up rates, they both have below average rates of business growth, as is the case for the county overall. While Coventry underperforms with respect to new business-starts using ONS data, business growth is around average.

Figure 5: Average start-up and business growth rates, 1998-2008 (indexed to England (100))



Source: BERR

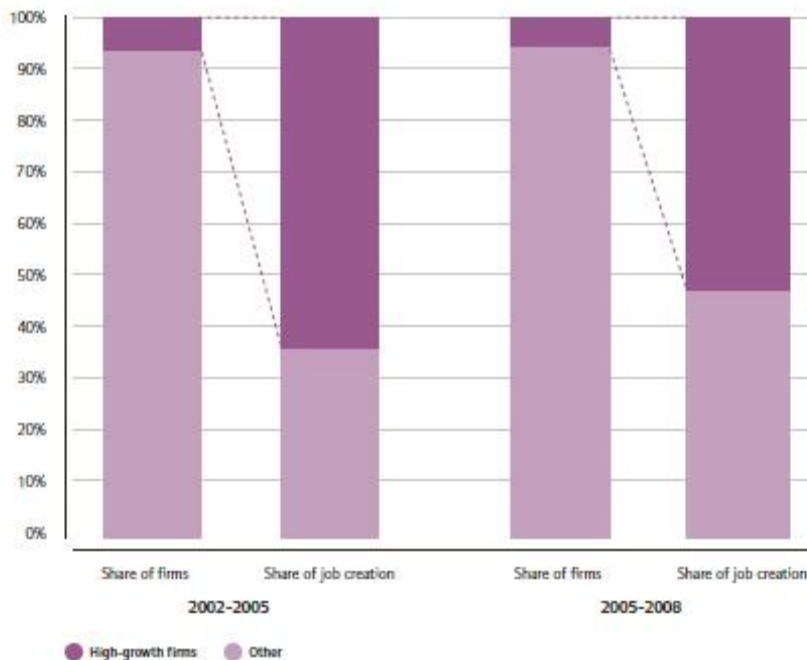
This analysis suggests that in those areas of the sub-region that appear to be doing well in terms of new business start-up activity also seem to be dominated by smaller, static businesses. This raises the distinct possibility of a profusion of so-called “lifestyle” businesses¹, although this hypothesis requires further additional research.

It should also be noted that national research has suggested that new business starts have a limited impact on employment growth in an economy². High-growth companies represent only 6% of all UK firms employing more than 10 people, but generated a majority of jobs (1.3 million out of the 2.4 million new jobs created in the period 2005-2008). The research found that the majority of companies only experience modest growth, and the number of businesses that decrease in size is similar to the number that increase their size. In contrast, the average high-growth company in the UK tripled its employment over a three-year period.

¹ “Lifestyle” businesses are generally businesses that are set up and run by their founders primarily with the aim of sustaining a particular level of income and no more; or to provide a foundation from which to enjoy a particular lifestyle. They can be found in all sectors of the economy.

² “The Vital 6 per cent”, NESTA, Oct 2009

Figure 1: The contribution of high-growth firms to job creation (10+ employees)



Source: ONS Business Structure Database.

Taken from the report "The vital 6 per cent", NESTA Oct 2009

Interestingly, the research finds that these high-growth companies are not confined to the so-called "high-tech" or "high-growth" sectors – they can occur in all sectors (even those in apparent decline) and are equally present in "low tech" as well as "high tech". High-growth businesses can also be found in all parts of the country, with no particular concentration in terms of share of the total business base (i.e. the South East has more high-growth businesses, but this is only in line with larger business base of that area). The research did, however, identify some key characteristics of high growth businesses:

- **Age is important** – the majority of high growth firms (70%) are at least five years old. However, young firms are more likely to be high-growth, with 11.2% of all young firms being high growth in 2002-05 compared to 5.4% of older firms; and 8.5% compared to 5.1% in 2005-08.
- **Size is important** – while 30% of high-growth firms were young (less than five years old), these were generally smaller and accounted for a relatively small amount of the total job growth generated by all high-growth businesses. Longer established, larger high growth firms are, therefore, more important in terms of net job creation than the so-called "gazellas" (fast growing new business starts). High growth companies employing more than 50 people in the base year were responsible for 73% of all high-growth business job growth in 2002-05 (68% in 2005-08)
- **Innovation drives growth** – innovative firms grow twice as fast (both in terms of employment and sales) than firms that fail to do so. The research used econometric analysis to show that innovation is actually driving business growth (and not just a contributory factor). This effect is also more marked the faster a company is growing. A high growth company that sees a 10% increase in shares of sales from new products adds almost 1.5% to its employment rate growth.

Policy Implications:

- There is a clear north/south divide in terms of business start-up rates, although when accounting for smaller businesses below the threshold for the “official” statistics there is evidence of strong entrepreneurialism in some of our more deprived areas.
- Businesses are far less likely survive when started in our more deprived areas, and may therefore require some particular focussed support (before and after start-up)
- Despite strong start-up rates in the south of the sub-region, there is below average levels of business growth (in terms of numbers employed). This may be through choice (“lifestyle businesses”), or through particular barriers. This needs to be explored in more detail.
- High-growth companies are likely to be larger and more established. Focussed support on companies with these characteristics (hitherto overlooked by most business support programmes) may therefore pay dividends.