



Success in
challenging
times:
Key lessons
for UK
SMEs

In welcoming this report I would like to express my gratitude to David Gray, Mark Saunders and Harshita Goregaokar for their tremendous efforts in producing such an expansive and rigorous piece of academic scholarship which also provides important, practical lessons for Small and Medium Sized Enterprises (SMEs), the Government and others.

SMEs are a vital part of the British economy. 99.9% of all enterprises in the UK are SMEs. These SMEs provide 59.1% of private sector jobs and are responsible for 48.7% of private sector turnover. The performance of SMEs has a major impact on the performance of the wider economy.

In the current economic downturn, growth is most likely to come from SMEs. It is therefore encouraging that 2011/12 saw the highest level of company start-ups since the last recession with over 450,000 new businesses registered. However, new businesses have a precarious existence and many do not survive their first year; only a minority will still be trading five years later.

For this reason, the following report which looks into the challenges facing UK SMEs could scarcely have come at a more appropriate time. Understanding the factors that determine the durability of SMEs will allow the development of best practice, and this vital information can then be communicated to entrepreneurs and SME owners.

The findings and recommendations contained in this report, such as the difficulty in obtaining loans or financing and the growing utilisation of social media to build brands and innovate, are extremely useful insights into the challenges faced by SMEs. It is my hope that this report will be used to inform both policy makers and SME owners and entrepreneurs so that the productivity of all British SMEs can be improved.

Sir Michael Snyder
Senior Partner
Kingston Smith LLP

11 October 2012



There are approximately 4.5 million businesses employing fewer than 250 people in the UK, providing a total of 13.7 million jobs, equating to half the private sector workforce in 2011. However, while such Small and Medium Enterprises (SMEs) are of importance, it is their *durability* that can be considered of greater significance. The precarious nature of SME existence has been well documented. Only about 65% of small businesses are still trading after the first three years of initial start-up. After five years, fewer than 45% of businesses will have survived. Put simply, small firms are more likely to die than larger firms. Indeed, other than size per se, the higher likelihood of death is what distinguishes small from large firms. However, multiple failures can be experienced as the springboard for later success (provided learning takes place). Much of the research into small firms has focused on their failure. The danger of this approach is that it identifies what has gone wrong, but may fail to discover what they need to get right. The approach of the current study, then, is to focus on the triggers that lead to SME success, as a way of highlighting more effective strategy decisions for firms themselves, and to inform better policy decisions for government. A return of over 1,000 survey questionnaires completed by SME owners/directors or senior managers, 20 in depth interviews and 13 focus groups, makes this one of the largest surveys ever into the strategic management of SMEs in the UK.

To request a copy of the full report, please email smesuccess@ks.co.uk.

Key findings

Finance

Successful SMEs are likely to use more than one source of finance to both start and sustain their business

- Most SMEs only use one source of finance to start the business, the main source being personal/family savings with a smaller proportion using a bank loan
- SMEs with a relatively large number of employees now are significantly more likely to have funded the starting of their business using:
 - Bank loan
 - Remortgaging personal property
 - Business Angels/Venture Capital finance/Grant
 - Leasing
 - Factoring and Invoice Discounting
- SMEs with a relatively small number of employees now are significantly more likely to have funded the starting of their business using:
 - Credit card
 - Personal/family savings
- The main sources of finance used by SMEs to fund their businesses now are:
 - Reinvesting profit (68%)
 - Personal/family savings (39%)
 - Bank loan (29%)
- SMEs seek routes to financing that avoid banks and traditional financial institutions
- The attitude of SMEs towards banks ranges from disappointment to contempt.

Cash flow and liquidity

Successful SMEs proactively monitor their cash flow and liquidity

- Alongside cash flow, SMEs with larger numbers of employees recognise the importance of the broad range of success factors (e.g. planning, sales, marketing, managing people, having a website, using social media)
- SMEs with larger numbers of employees consider that they are significantly more effective across the range of almost all success factors than smaller SMEs.

Social capital, social media and the web

Successful SMEs consider direct referrals and search engine optimisation as central to their success

- SMEs with smaller numbers of employees place greater importance on direct referrals
- SMEs with smaller numbers of employees put greater importance on the use of social media
- 94% of SMEs consider direct referrals important to their continuing success; 67% consider search engine optimisation important.

Innovation

Successful SMEs are willing to find new ways of doing things and encourage their employees to think and behave innovatively

- SMEs are significantly more likely to be innovative than competitively aggressive, proactive in the market or risk taking
- SMEs are significantly less likely to take risks than be proactive in the market, competitively aggressive or innovative
- SMEs with larger numbers of employees are significantly more likely to be proactive in the market.

Learning Orientation

Successful SMEs believe that learning gives them competitive advantage

- Newer SMEs are more committed to learning
- SMEs with less than 5 employees are significantly more likely to have a shared vision
- SMEs with less than 5 or more than 50 employees are significantly more likely to be open-minded
- SMEs with larger numbers of employees are more likely to learn from crises.

Advice and support

Successful SMEs are more willing to seek external advice

- Most SMEs seek external advice regarding their website (including search engine optimisation)
- SMEs with larger numbers of employees are more likely to purchase external advice on managing people and developing management skills.

Outsourcing and exporting

Successful SMEs have the flexibility to adapt to changing market conditions

- Half of SMEs outsource some of their activities, including: accountancy (payroll and bookkeeping), IT and web development, HR and marketing
- Outsourcing provides SMEs with the flexibility to respond to market conditions
- SMEs with larger numbers of employees view exporting as important to their continuing success.

Background

The Surrey Business School at the University of Surrey was commissioned by Kingston Smith LLP, a top 20 chartered accountancy firm, to conduct a research study into the ‘triggers for SME success’. This meant identifying the crossroads or critical incidents that businesses reached, how key decisions were taken at these vital timelines in business development and what triggers stimulated innovation and growth. The target audience for the project was current small and medium-sized businesses (SMEs) with fewer than 250 employees that have demonstrated business success. These were commercial businesses; they were neither lifestyle businesses nor were they organisations located in the voluntary sector. The study, conducted between May and September 2012, comprised a national survey with responses from over 1,000 businesses, the hosting of 13 focus groups across the UK, plus detailed qualitative interviews with 20 SME businesses as case studies.

Acknowledgements

We would like to thank Kingston Smith LLP for financing this research project and the many businesses and individuals who took part in the focus groups, interviews and responded to the survey. Special thanks go to Paul Samrah, Chris Lane and Annie Wilson of Kingston Smith who worked so constructively with us on the project. We would also like to thank the many organisations such as Chambers of Commerce that promoted the research survey amongst their membership. Lastly, we would like to thank Surrey Enterprise for their collaboration in making the project a success.



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Key finding 1

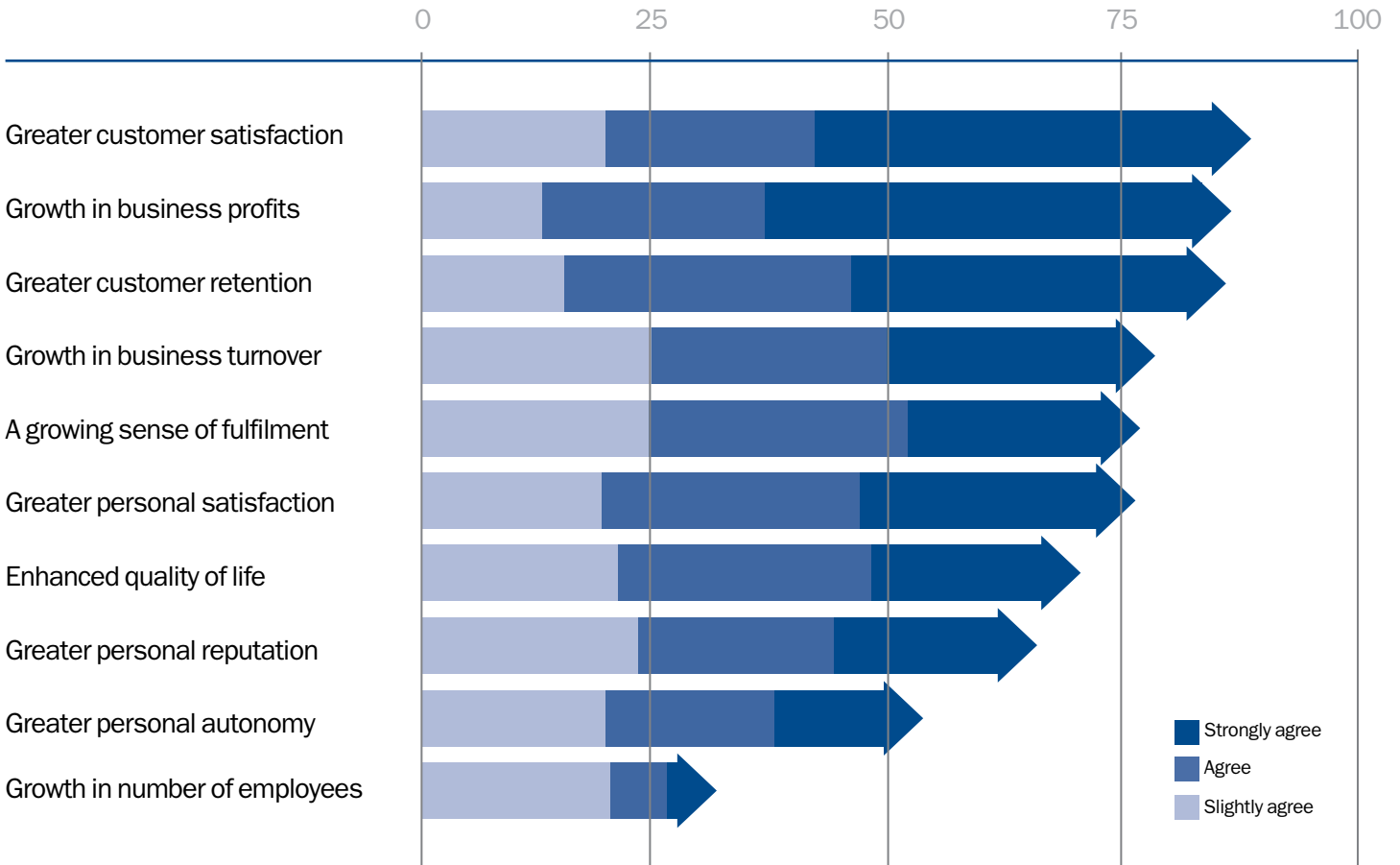
What does success mean to SMEs?

Before examining the actions and strategies adopted by SMEs for achieving success, we need to reflect for a moment on what they think of as 'success'.

Many SMEs acknowledged that they had been through a full business life cycle with its share of 'ups and downs'. Although it was good to have dreams about the business, the key to success for businesses was financial success, including maintaining cash flow. Success can mean not growing too fast, as this is a sure way of sucking cash too quickly out of the business. Success was based on repeatability of business to achieve recurring revenues and, for some, growth, maintaining cash flow and creating shareholder value. For others, however, success was also based upon non-financial measures such as a sense of fulfilment or challenge, or building a lifestyle business and work-life balance. Enhanced reputation and being seen as making a contribution to society were amongst the more altruistic goals. Whatever their idea of success, the means to achieve it were always evolving.

WHATEVER THEIR IDEA OF SUCCESS, THE MEANS TO ACHIEVE IT WERE ALWAYS EVOLVING

What year-on-year success means to SMEs (%)



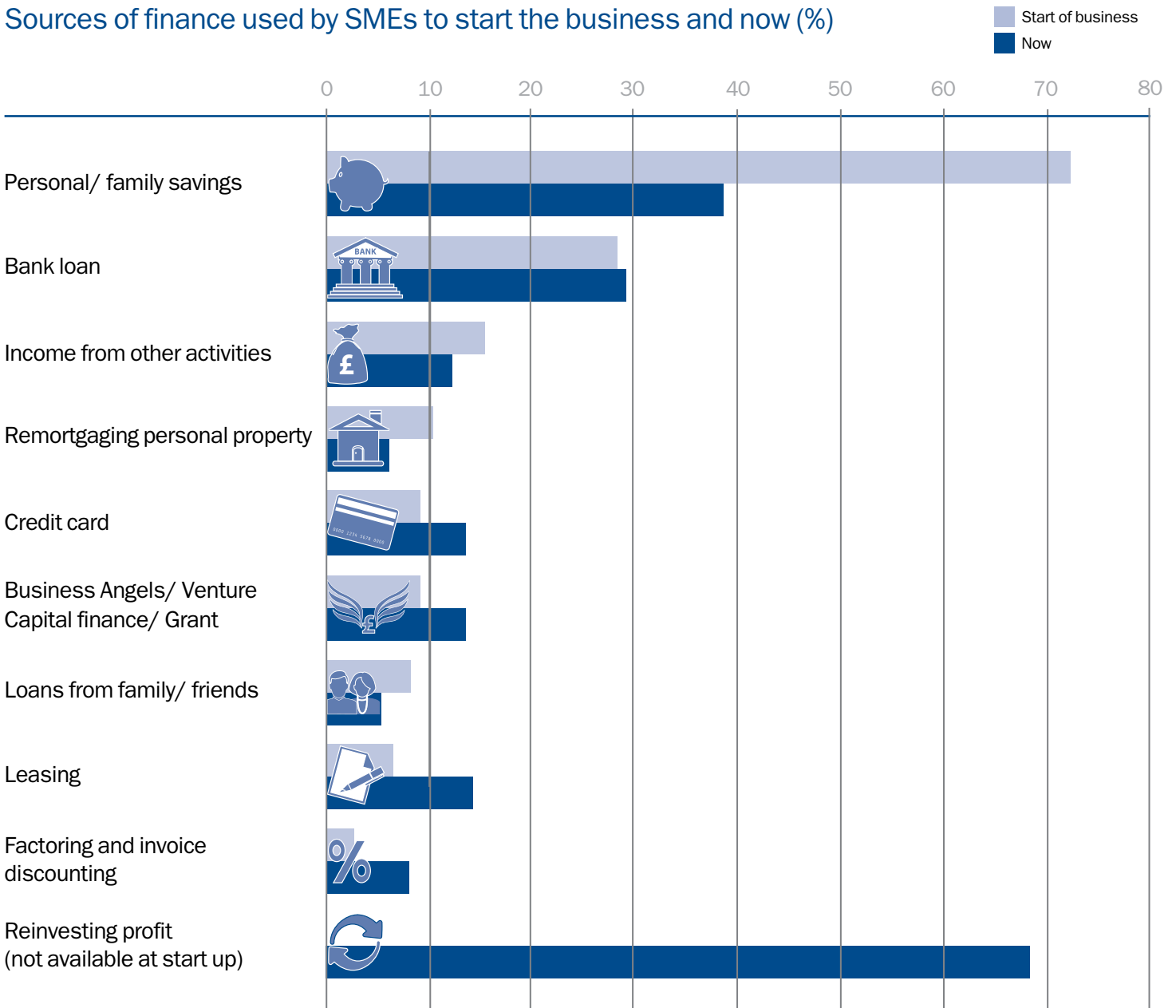
Key finding 2

Sources of finance

The attitude of SMEs towards banks ranges from disappointment to contempt. Not only do banks not provide the capital required, they seem to know very little about what businesses (particularly small businesses) need. As the data shows, finance is acquired via other means, including the use of credit cards. Some businesses have turned to discounting their invoices as a means of maintaining cash flow, whereby a discount is offered in return for prompt payment. Third party equity finance is sometimes utilised and sometimes new ventures are grown organically through the reinvestment of funds from an original, successful business. However, reinvested funds are often too restricted and they suck finance away from successful core activities.

NOT ONLY DO BANKS NOT PROVIDE THE CAPITAL REQUIRED, THEY SEEM TO KNOW VERY LITTLE ABOUT WHAT BUSINESSES (PARTICULARLY SMALL BUSINESSES) NEED.

Sources of finance used by SMEs to start the business and now (%)



Case study

The Organic Health Company Limited¹

The business has been trading for six years and makes pure and natural personal lubricants, free of skin irritants. The Organic Health Company Limited employs 10 people, including Anna and Heather, the two founders and directors. With growth last year up by 25% and a further 25% this year, 60% of sales are from exports which go to 66 countries. The UK Trade and Industry: Passport to Export programme was beneficial here. The company's success stems from the team's ability to innovate constantly to provide excellent customer service. The company strives to act ethically, creating products from the purest and safest ingredients. These are now assets in the current climate because customers favour good business ethics. This has resulted in high levels of customer loyalty, and a growing number of business awards. Most products the company sells in the UK are manufactured here: *"It's nice to confound people's expectations. We have supported the local economy."*

"IF WE COULD HAVE WON THAT INVESTMENT, OUR COMPANY WOULD BE A COMPLETELY DIFFERENT SIZE NOW"

One major limitation on expansion has been access to finance. In 2007 the company asked for a bank loan but was turned down. *"Bank managers speak with forked tongues."* As a result, the company has had to grow organically relying on its cash flow. Many new products in the pipeline have had to go onto the back burner, and the product line is restricted. *"If we could have won that investment, our company would be a completely different size now."* Another challenge has been the protection of their intellectual property, with competitors copying their products or infringing patents. The directors believe strongly that the UK is an innovative country, and that government should help small companies more in this area – for example by making it less expensive to defend patents through legal channels, or by helping new companies to understand intellectual property and help them to fast track their products through the Patent Office.

The Organic Health Company's top tip for new businesses: *"Go global. Anyone who doesn't see the world as one market is going to go out of business."*

¹Name of company and MDs changed and details of its technical operations omitted to protect confidentiality.



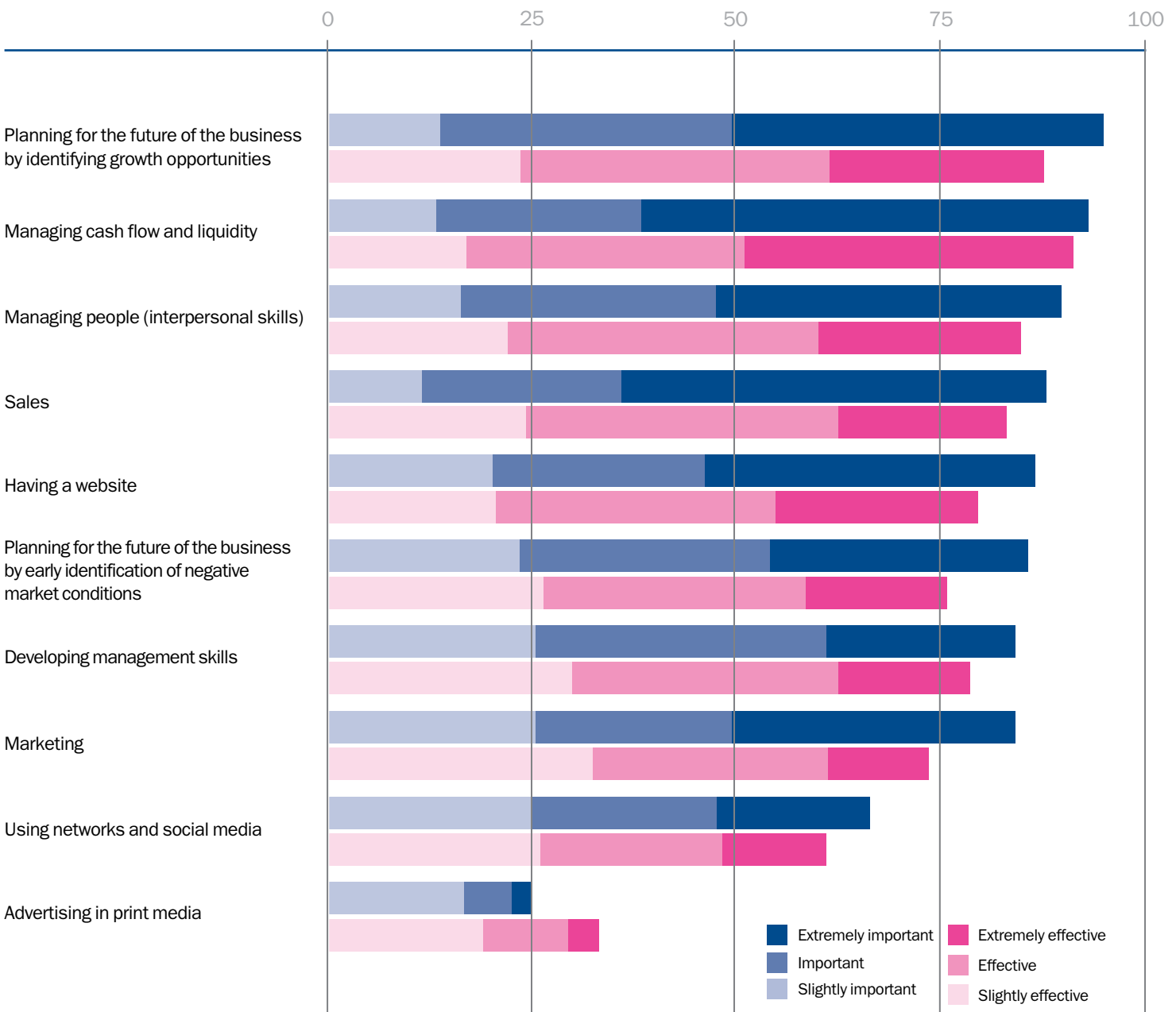
Key finding 3

Cash flow and liquidity

The key focus of SME finance is cash flow, in particular the need to learn about it. Monitor it and ignore it at your peril. Conversely, too much money is considered just as harmful, because SMEs are going to spend (and not always wisely) whatever they have got. Keeping a close eye on liquidity can mean using new technology to track liquidity on a regular basis. SMEs felt they needed to keep a close eye on their pipeline of orders, otherwise as one focus group participant commented “you just feel like somebody’s turned the engine off in the plane”.

They emphasised the need to look at people costs and look at unit costs and rein them in if necessary, otherwise “the plane doesn’t come to a nice, gradual descent – it crashes through the atmosphere quicker.” For businesses seeking growth, securing one large contract can put them into a new league of “big hitters”. It can transform the way the market perceives their business. However, they must also be able to contract when market conditions require it. This means being able to identify strains on financial liquidity at an early stage and take steps (for example, moving to smaller premises, laying off staff, especially contractors) in a timely fashion.

Importance of factors to continuing success and average SME effectiveness (%)



Case study

Kavanagh Communications Limited

Founded in 1996 by Anne Kavanagh, Kavanagh Communications Limited is a public relations company with a particular focus on retail, both in the UK and in global travel retail. It also helps clients with crisis communications, particularly where there is a need for damage limitation as a result of negative media scrutiny, assessing risk and running a proactive crisis communication strategy. The company, which employs 10 people, has an enviable client list, with 2011 being the company's most successful year to date.

2012, however, has proved to be very challenging. Two factors have been especially problematic. Firstly the banks have been very unhelpful, particularly in advising the company to embark on a base rate swap connected to the office property. Even the bank manager who sold the deal didn't understand the principles of the swap. The result has been considerable financial losses for the company, which it is still trying to resolve. Part of the resolution to the problem may come from the FSA's investigation into the issue, but the company cannot wait for this and has had to take urgent action by reducing fixed costs and head count. *"If I could get out of this today, I'd have a very different business tomorrow"*. The second problem relates to how larger companies, particularly corporates, indulge in negative tactics to delay payments. In many instances, payment terms have shifted from 60 to 90 or even 120 days, which puts particular pressure on SMEs' cash flow. They believe it is vital to understand the strategy for how larger businesses work because they are more sophisticated contractually and are adept at using *"every excuse in the book"* on procurement procedures. In one case it took nine months to get payment from a large business.

As a result, the company has taken decisive action, focusing its future growth strategy on greater global diversification on PR for the travel retail industry with customers in France, North America, South America, Scandinavia, Hong Kong and Singapore. Secondly, the company has decided that it no longer needs a costly UK base (and the drain it causes on overheads) because technology has moved on so much. The company is therefore transitioning from a traditional office setting to a smaller more flexible site and to greater virtual working where it's possible to maintain team contact through meetings in wifi enabled settings like hotels and cafes.

The company believes flexibility is the key to success in challenging times and that businesses must move with the times to stay ahead of the competition and to nurture the more enlightened customers who have a real partnership approach with SMEs. Social media is a tool that the company exploits and can be particularly powerful for SMEs dealing with the public (B2C), but for B2B the approach needs tailoring for business led social platforms: an effective social media strategy should always focus on who and where the customer is and tailor accordingly.

Kavanagh Communications' top tip for new businesses: *"Get right on top of payments coming in from customers. Make sure you get a purchase order, particularly from large, global businesses."*



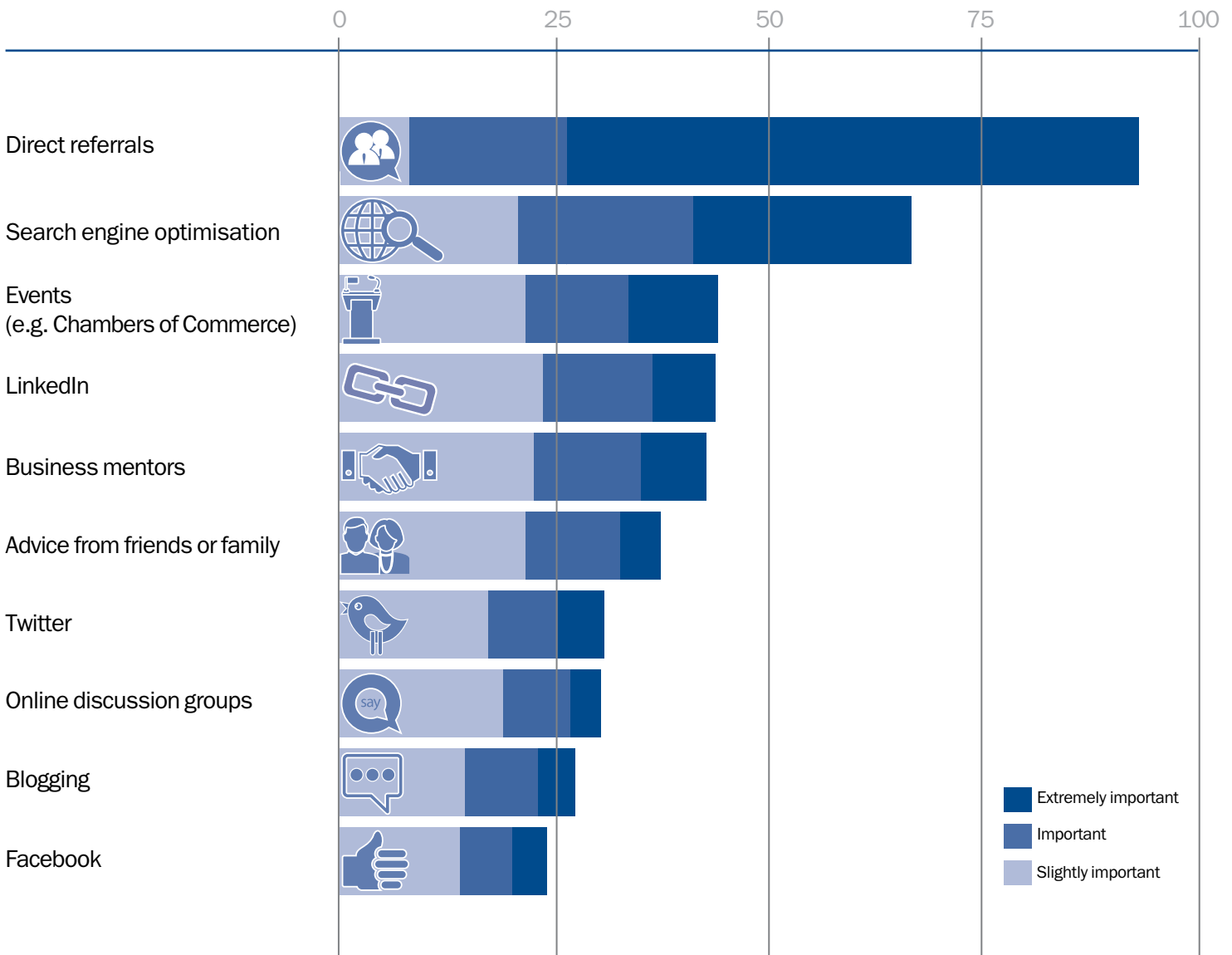
Key finding 4

Networking and social media

There is a strong engagement with web technology (some of it linked to social media). Hence participants talked about using LinkedIn to target customers. Some use Twitter as a form of viral marketing. Websites are used as interactive tools to connect to customers, gauge their needs and even talk to them in real time using Live Chat. Within this, a high quality website is considered important even for interacting with local customers. For more advanced users, the web is not used as a kind of electronic billboard, passively advertising product. It is used dynamically to analyse customer profiles, levels of interest, and buying intentions, or even train their customers to use a product. Websites are also used in recruitment, for example, looking at GitHub, a social coding environment to evaluate the quality of a potential employee's coding. But none of the entrepreneurs regard themselves as experts. They experiment and "feel" their way towards virtual solutions for their business – sometimes buying in external consultancy to develop social media campaigns.

The perception is that IT and social media are regarded as a "necessary evil", and there is no choice but to engage very proactively in this area. Respondents see themselves as connected to a number of communities which include their customers, associates and even former employees who are now independent contractors. It is all about direct contact, talking to the right people. Sometimes this means people who are outside the business (associates) offering feedback or advice, these people having done work for the business in the past. These were regarded as a "community of people" who might join in with a new business proposal. Unlike in the corporate world, participants argued they "feel a bit more loved" and appreciated in the SME environment.

Importance of networking and social media to SMEs (%)





The business began five years ago after MDs Josh Coleman and James Nash wrote a business plan for the entrepreneurship module of a university degree programme. The business plan got low marks compared to their other modules because the finance figures weren't accurate! Undaunted, they launched Bike Dock Solutions Limited, selling bike racks to both retail customers and to organisations and businesses. Other businesses have been launched with one inspiring the creation of another. For example, Bike Dock Solutions sells bike racks, but these need a shelter – cue the launch of Shelter Store for bikes. Shelter Store then led to the launch of Hudson Garden Rooms, supplying luxury garden offices made of wood. Bike Dock Solutions, Shelter Store and Hudson Garden Rooms all won contracts to supply products for the London 2012 Olympics.

From an initial investment of £10,000 by each of the two directors (and money borrowed from their parents), sales for Bike Dock Solutions reached £85,000 in the first year, followed by £400,000 in year two, £1.25m in year three and £2.5m in year four. Total sales for all companies exceed £4m. The company now employs 14 people with much of the manufacturing being done in the UK. There are good reasons for this: production could have been outsourced, for example, to China. But UK manufacturing achieves shorter lead times, which is important in a market where customers want tailored solutions.

SOCIAL MEDIA “MAKES US LOOK QUITE HUMAN”

Part of the company's success is down to its close interface with its customers. *“People are passionate about their cycling so we try to talk to them about it”*. The company uses both Facebook (it has almost 4,000 fans) and Twitter. The company produced a video to illustrate bike theft in a London street as part of a bike safety awareness campaign, which achieved over 34,000 YouTube views. Although social media brings in domestic customers, most of the sales come through businesses and organisations (e.g. schools and local authorities), but social media *“makes us look quite human”*. The company pays close attention to its website, and invested £10,000 recently on a Google pay per click marketing campaign, which saw sales triple. The company is always experimenting with search engine optimisation, to see what works and what doesn't. Bike Dock Solutions has been shortlisted for the National Business Awards in the small online business category.

One of the company's keys to success is not challenging competitors at their own game. The company competes for the same customers, but they do it in a different way. They ensure that lead times are good and allow people to track their deliveries via the website. Shelter Store is now trading in Dubai and the United Arab Emirates, and is tendering for bus shelters for the whole of Dubai. UKTI has helped Bike Dock Solutions start trading in Europe with its new Bike Safe website. In 2013, the company aims to start trading in the USA with Bike Dock Solutions.

Bike Dock Solutions' top tip for new businesses: *“It's not just about increasing sales. Keep an eye on suppliers and source new suppliers to refine costs, so if competitors get close to your prices you can drop them.”*

Key finding 5

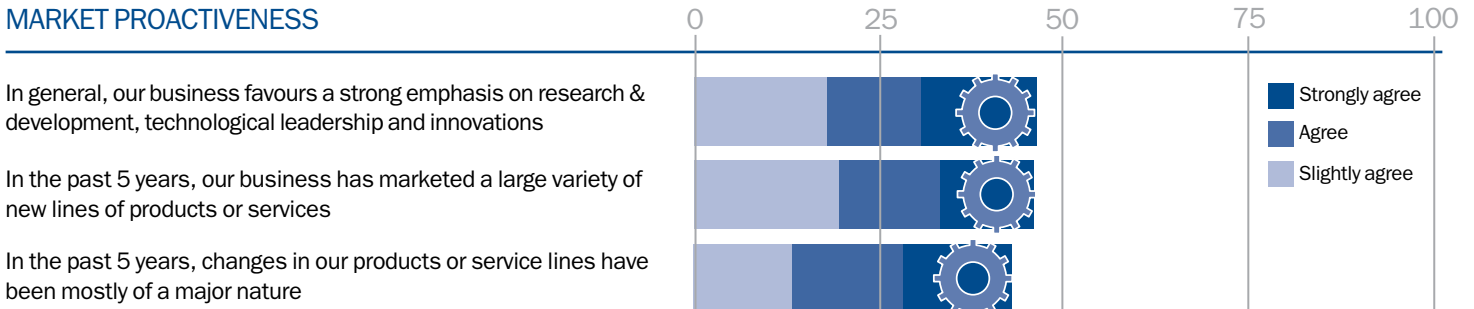
Entrepreneurial Orientation

Entrepreneurial Orientation (EO) is the process, practice, and decision-making that leads to new entrants to the market. In terms of Entrepreneurial Orientation, participants demonstrated high levels of commitment, proactiveness and “persistence in adversity”. For example, failure was viewed as just part of a learning process; you “learn from experiences”. When autonomy was mentioned it was always in a positive light, none of the entrepreneurs wanting to go back to the corporate or salaried world. “I am in control”, and “no one’s going to turn the lights out on me”.

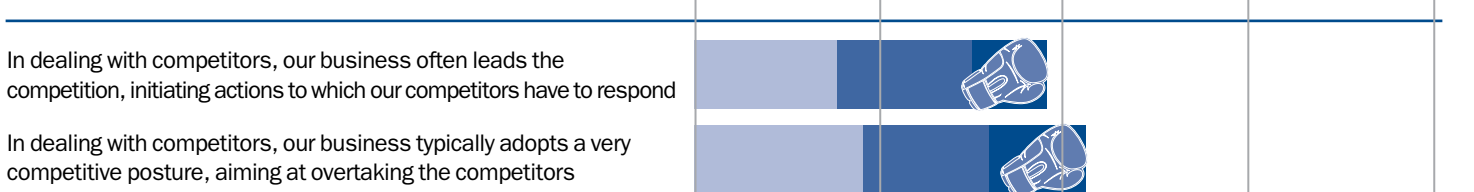
In terms of the corporate world (even though some have worked there), they often regarded themselves as unemployable. Entrepreneurial Orientation included being “open minded” or “open eared” at all times, being prepared to listen. It also meant showing drive and determination and being persistent – because success always took longer than expected. The downside of this entrepreneurial spirit is that excessive focus can result in being too blinkered and arrogant. Some felt they should have had the humility to step back and admit: “I was wrong”. The creative but reckless won’t survive. SMEs are often cautious about risk because they are usually investing their own money!

SME agreement with statements about Entrepreneurial Orientation (%)

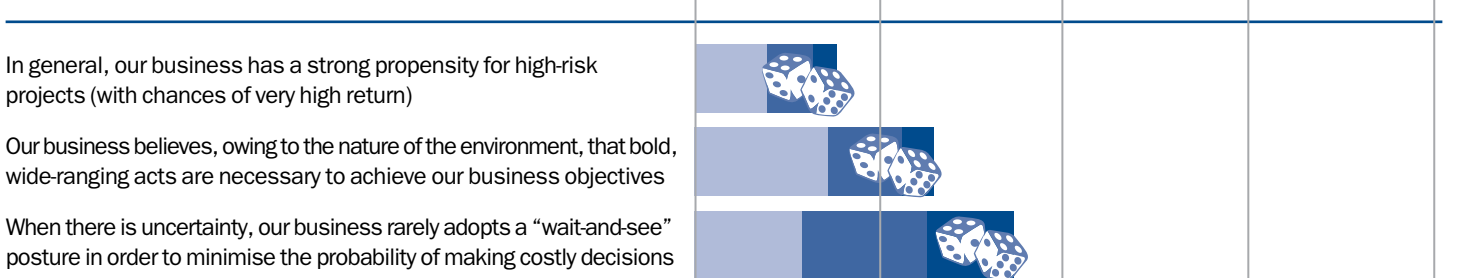
MARKET PROACTIVENESS



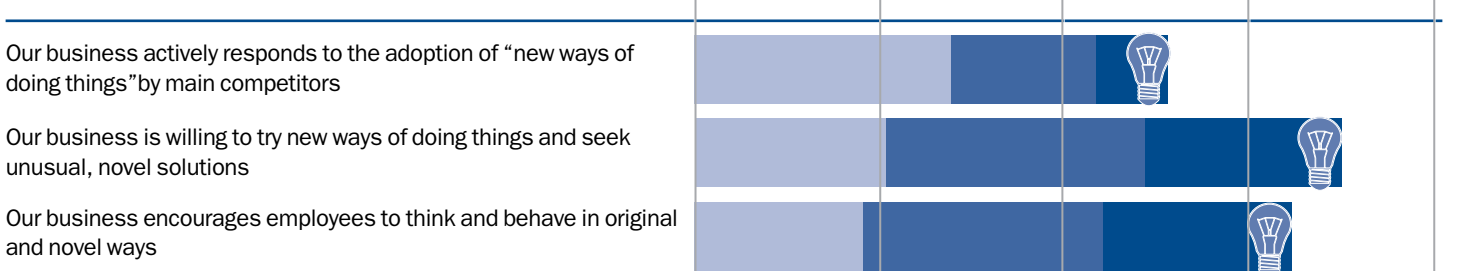
COMPETITIVE AGGRESSIVENESS



RISK TAKING



INNOVATIVENESS



Gen3 Systems Limited



Gen3 Systems Limited was founded in 2005, emerging from a previous company. Its name stems from the fact that three generations of the family are involved. Generation 1 began in heavy engineering during the late 1960s, with a major French manufacturer of cement plants, sugar refineries and more. Generation 2 subsequently moved into electronics, producing special varnishes used to protect electronic systems operating in difficult environments, mainly in the aerospace and defence industries. This business was sold in 2005, but the equipment manufacturing division was retained to become Gen3 Systems, with MD Graham Naisbitt.

The company is a manufacturer of specialist test equipment used to help predict reliability in electronics. There are 17 people working directly for the company with a further 250 people in Europe, Asia Pacific and North America working through distribution arrangements. Another business division, Gen3 Kinematics, manufactures specialist strength and conditioning equipment for athletes in a wide variety of sports, giving the family a diverse business operation.

Employing an “*inverse marketing technique*”, the business in its many guises has worked closely with customers to understand and resolve precise technical issues drawing on their diverse manufacturing capabilities. The company requires people with both experience and high level engineering skills.

The company has seen many challenging times. In 2008 the electronics industry “fell off a cliff”. For example, the semi-conductor business dropped 40% in September 2008 and for the next four months dropped a further 40% per month so that, by early 2009, it was at 20% of its 2008 level.

As this spread through the entire electronics industry, Gen3 had to halt its capital spend, cut costs dramatically, even resorting to a 20% salary cut across the entire company. “*We were hammered, as were so many other businesses*”, and needed to find new opportunities to survive.

They acquired a distribution company handling equipment complementary to that manufactured by Gen3. In 2010 another opportunity arose that provided diversification for Generation 3 into an entirely new industry, manufacturing sports training equipment. After only two years it is now showing a profit, selling mainly in the rugby world. Customers include top rugby clubs such as Exeter, Gloucester, Northampton, Worcester in England; Leinster, Munster and Ulster in Ireland; Toulon, Biarritz and Castres in France, and many more. The company supplied its equipment to Cycling GB and Rowing GB – both teams performed rather well in the London Olympics! It has also broken into UK universities, schools and colleges.

A key component of the company’s success is the retention of staff, who are paramount to the success of all businesses. Also, helping to write the International Standards relevant to their equipment/product was a thankless but necessary task, and one which opened doors to customers that would otherwise remain firmly shut. Gen3 employ external specialists, but all of this is funded internally and grown organically – “*because you can contain the risk*”. The business is family financed and free of any loans and commensurate pressure from banks and other financial institutions.

Gen3 Systems’ top tip for new businesses: “*In terms of marketing you need to be the best at what you do. A good website is essential, as is being at the top of search engine listings, and being active in social media.*”

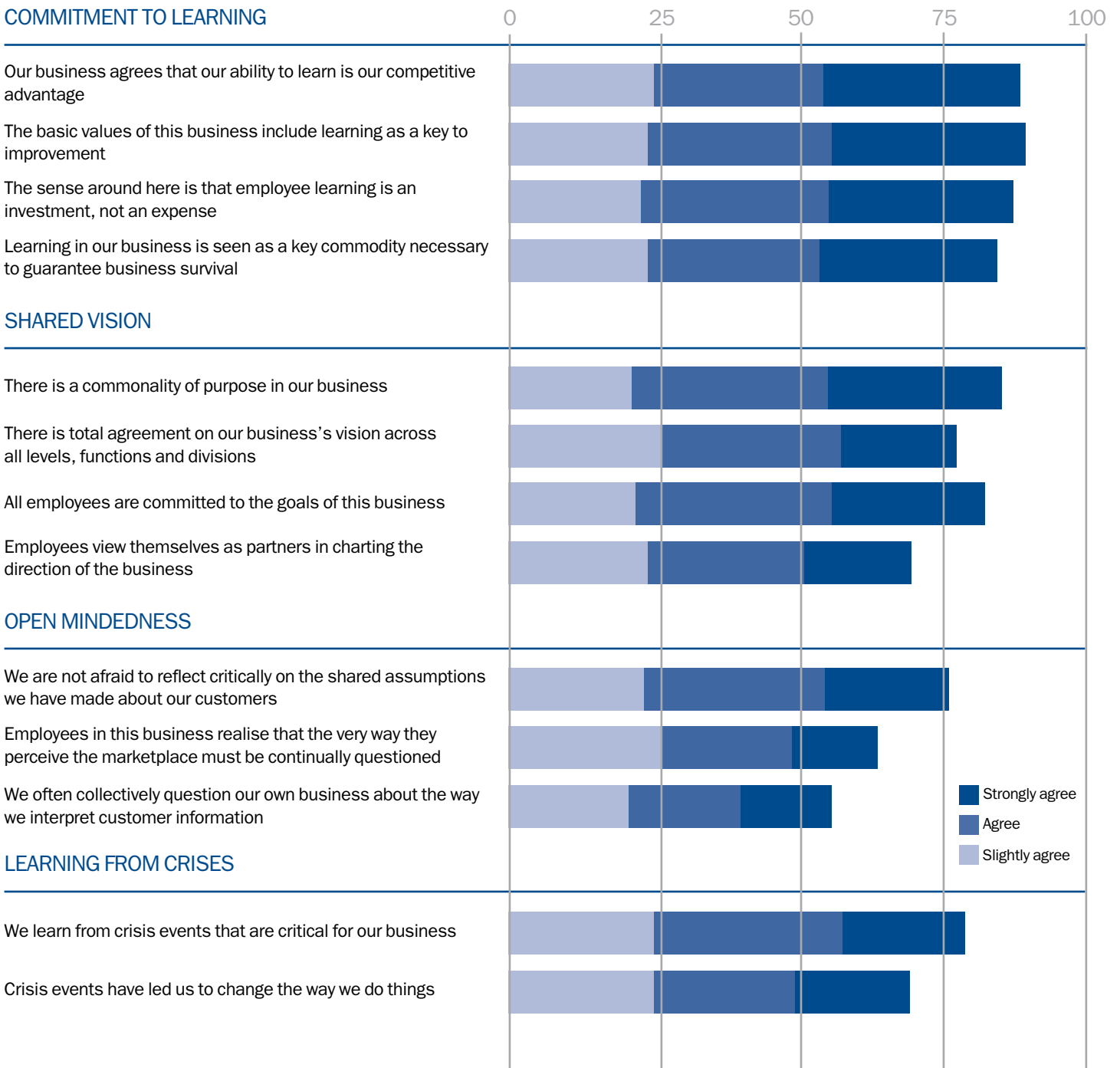
Key finding 6

Learning Orientation

SMEs value learning (whether formal through accredited programmes or informal – more usually the latter) and the majority were committed to personal development in one way or another. Sometimes this was as a result of a ‘critical incident’ such as a temper tantrum with staff that led to the entrepreneur undertaking counselling (and subsequently developing an interest in and learning about emotional intelligence). Some engaged with formal learning programmes, such as an MBA, but this was relatively uncommon. For most, making use of informal learning opportunities, such as the use of a mentor or coach was important.

Getting an external perspective from a range of groups whether it be peer groups, Managing Director groups (talking to fellow directors can be “*hugely powerful*”), breakfast seminars or casual conversations, helped in “*chewing over the business*”. “*You are cocooned and isolated as an SME*”. For example, if there is a dip in business, you can discuss this with competitors to find out if it’s a market trend, or a blunder you have made yourself. Whilst for informal learning like this there is never any great agenda, there is always a “*nugget*” that comes out, so the entrepreneur comes away thinking “*Yes, that’s something that I can work with.*” It is conversations that trigger ideas.

SME agreement with statements about Learning Orientation (%)



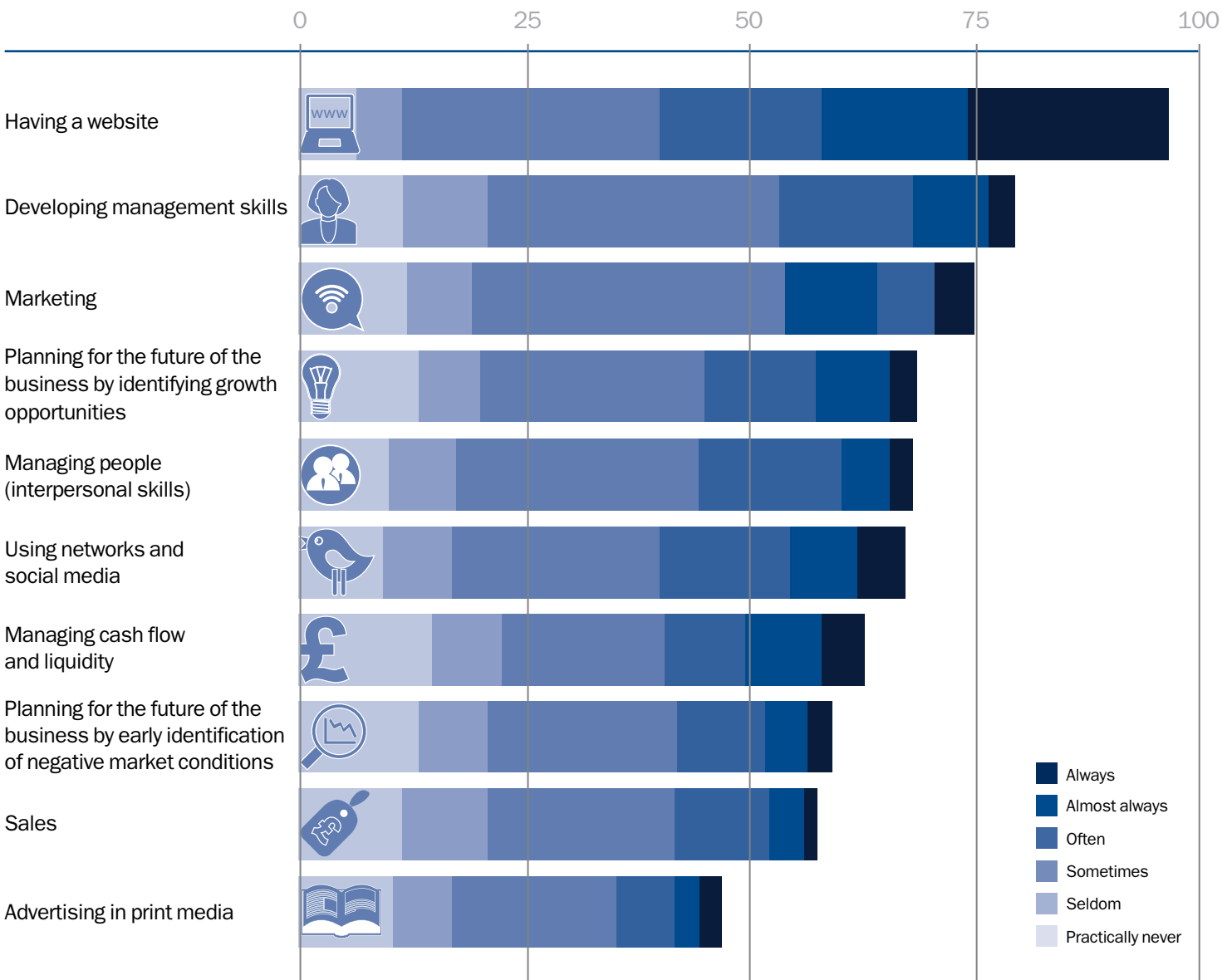
Key finding 7

Advice and support

Many SMEs purchase external advice, but tend to be highly selective as to what kind of advice they need, focusing primarily on the services of accountants, HR specialists, and IT consultants. The problem is that SMEs are outward (customer) facing, whereas external advice is usually sought to solve back office issues which SMEs regard as necessary but less rewarding. Both the issues themselves, and the external professional advice on offer, are usually fragmented.

Apart from finance and cash flow, the other key area where SMEs need advice is on website design and particularly search engine optimisation (SEO). However, few companies believe that the SEO advice they receive is effective - SEO consultants are giving different answers to the same question. Rather than pay for advice, some SMEs are turning to social media, live networks or informal management learning groups where they can discuss business problems with experienced fellow business owners.

Frequency of purchasing external advice / consultancy (%)



Key finding 8

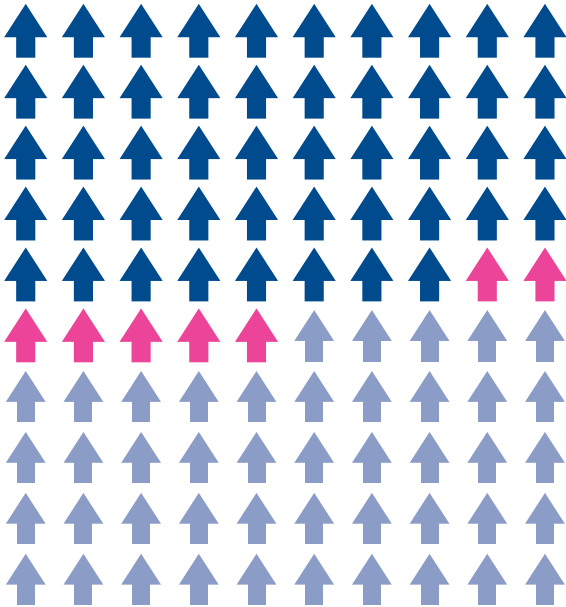
Outsourcing and exporting

Outsourcing is becoming increasingly important for SMEs as they strive to keep control of cash flow and as they attempt, in the light of this, to keep head count down. Typical areas include accountancy, human resources and payroll (often to agencies who are themselves SMEs), IT (particularly web design and search engine optimisation) and some legal advice. But one of the dangers of this strategy is employing people who don't necessarily identify with the business. Hence, it is essential to outsource to people who have the same ethic and work approach and appreciation of the brand that you are trying to build.

Outsourcing can be seen as engaging the services of the self-employed – itself a sign of a more entrepreneurial, flexible society. Moves into exporting sometimes develop iteratively, but at other times may result from a complete change in strategic direction. For example, experiencing a collapse in demand due to aggressive competition from overseas entrants to the UK market, a company launched their product into European and U.S. markets and is now exporting to 52 countries. Exporting might be one element of a company's move towards greater diversification.

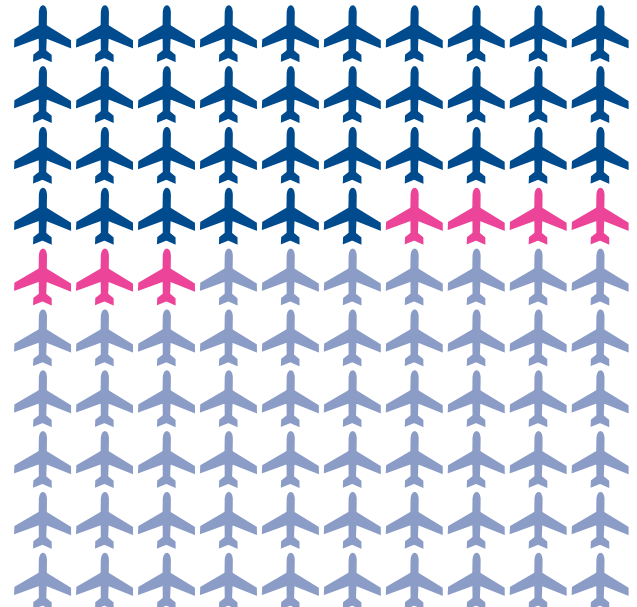
Current and future use of outsourcing and exporting outside the UK by SMEs

Outsourcing



- USE
- PLAN TO
- DO NOT PLAN TO

Exporting outside the UK



- USE
- PLAN TO
- DO NOT PLAN TO

Case study

Earlex Limited

Julian Baseley started Earlex Limited in 1988, manufacturing consumer steam wallpaper strippers, and has since moved into manufacturing wet and dry vacuum cleaners and paint sprayers. Earlex now employs around 180 people with offices in France, the USA and China. Turnover is around £25m, exporting to 52 countries. Earlex faced difficult times very soon after it started, firstly with direct competition from two corporate competitors. In 2004 competitors in China started to copy its products and sell directly to stores in the UK. Then there was the 2008 recession. This was not helped by the company's bank persuading it to hedge against the euro, pre-selling euros against their average sales. But the euro dropped by nearly 25%, causing the company considerable losses. The most challenging phase was 2003-4 where a competitor tried to buy up the company but was turned down. The competitor went to all Earlex's major customers and offered very low prices. Being attacked in its UK markets, Earlex went for exports, opening up in France, Spain, Italy and the USA.

The company has seven of its own design engineers, but also uses external design consultancies as well as the engineering department of a local university. In addition to technical consultants, they use accountants for advice on areas such as getting the right finance in place for business development and paying at the right level to attract and keep employees. HR consultants advise them on HR requirements for China, America and Europe. The manufacturing base is in Guildford. Although labour costs are high in the UK, there are quality and delivery issues overseas, particularly where there are fluctuations in demand due to seasonal variations. With UK manufacturing, customer orders can be serviced in 5 days. In places such as China there are also issues such as the infringement of patents that you do not get in the UK.

For sales and marketing the company makes extensive use of social media such as Facebook and YouTube, both in the UK and also for its French and US operation. Video is used for product demonstrations, and the company uses television screens in retail stores to sell products but also trains staff to demonstrate them to customers. This sells 10 to 15 times as many in a day as would normally be sold with the product just on a shelf. They feel it is important to use social media but not to be intrusive nor to use a 'hard' sell. Their main focus of selling to worldwide markets is met through attending trade exhibitions around the world, including countries such as China, Dubai, India, the USA and Germany. These exhibitions are for worldwide audiences and the company attends over 20 of these per year.

The trigger for Earlex's growth is innovation; making something different that people want to spend their money on. For example, the company makes paint sprayers and has now converted this idea into the spray tanning industry (fake sun tanning). Secondly it means going for world markets. Earlex's largest market is now the USA.

In the future the company believes its market is probably going to be Asia and South America rather than Europe and the USA. The time between product inception and launch is now down to about one year, whereas 20 years ago it probably took about 3 years. With new computer aided design systems they believe this could even come down to 6 months in the future. In addition, they feel that businesses will also have to show that they are more socially aware (including being environmentally clean) and that they are in the community, doing things for the community.

Earlex's top tip for new businesses: *"You have to be passionate about your products. Know your competitors and know your unique selling point. You need to be very, very well versed in your products."*



Key recommendations

SMEs

- Diversify sources of finance to include (but not be confined to) Venture Capital finance/Grant, Leasing, Factoring & Invoice Discounting and Crowd Funding²;
- Monitor cash flow and liquidity proactively (taking quick and decisive action when necessary), but also focus on planning, sales, marketing, managing people, website development, and using social media;
- Get 'close' to customers, establishing reputation and relationships to achieve retention and referrals. Work with customers to build the brand;
- Define the unique selling point of the business and put it on the front page of the website. Focus on search engine optimisation in website development;
- Connect with social media in ways that fit the business (especially for Business to Consumer businesses). Consider engaging external advice on ways to do this;

²The collective effort of individuals who pool financial resources, usually via the Internet, to support a new business initiative.

MONITOR CASH FLOW AND LIQUIDITY PROACTIVELY

- Encourage employees to think and behave in novel ways; monitor and respond rapidly to the actions of competitors; avoid high risk projects;
- Learn proactively from crises and difficulties; join and contribute to learning networks (for example business and professional associations, customer networks); engage the services of a coach or mentor. Share ideas through social networks and media;
- Take calculated risks but never ignore intuition. Respond to market conditions - learn to rein in the business as well as expand;
- Consider outsourcing some activities, especially in turbulent economic conditions.



Key recommendations (continued)

Policy makers

- Provide a flow of 'patient capital' through the establishment of a Business Bank aimed specifically at high-growth potential SMEs;
- Ensure that the market provides SMEs with choice for sources of finance. Use social media for disseminating information about sources of finance and engage SMEs in a debate about their financial needs;
- Demonstrate to SMEs through transparent policy initiatives that all businesses, irrespective of size, get equal treatment in fiscal and monetary policy initiatives;
- Make it easier and cheaper for SMEs to protect their patents and intellectual property.

Professional service providers

- Offer a holistic range of professional services encompassing accountancy, HR, law and IT, to integrate provision across 'back office' operations;
- Orientate services from the 'back end' (where possible and subject to regulatory frameworks) towards SME 'front end' perspectives (including customer orientation);
- Facilitate the management and leadership capabilities of SME owners to create synergy between their work and their values, confidence, and personal beliefs – the 'inner game'.

**ENSURE THAT THE MARKET PROVIDES
SMALL AND MEDIUM ENTERPRISES WITH
CHOICE FOR SOURCES OF FINANCE**



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