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Business as Unusual:

Creative industries, international trade and Brexit

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UK government statistics maintain that only 18 per cent of creative industries firms engage in international trade. The UK's *Industrial Strategy: Creative Industries Sector Deal* aims to increase UK creative industry exports by 50% within 5 years, arguing there is a "great deal of untapped potential in the sector." It also identifies small company size as a barrier to creative industry exports. Our research, however, challenges these assumptions. At least one creative industries hub is already deeply entwined in global trade. In Liverpool's creative and digital hub Baltic Creative, 69 per cent of tenants export. Furthermore, these exporters are highly dependent on their overseas income. Over one-third of exporters earn more than 50 per cent of their annual income from exports. Our research also finds that small company size was not a deterrent to international trade. Rather company owners report concerns about access to global markets after Brexit, which had already resulted in significant financial losses for some. Our study reveals that even the smallest micro-enterprises are exporting not by way of strained or concerted efforts, but simply because they are operating in an open, digital, global environment where international trade is integral to their business.

Keywords: Creative industries, design policy, international trade, Brexit, creative hubs

Introduction

Creative industries are growing at nearly twice the rate of the rest of the UK economy (Department for Business, Energy & Industrial Strategy, 28 November 2018). In 2015, they accounted for 6 per cent of UK jobs and an impressive 9.4 per cent of total services exports from the UK (Department for Business, Energy & Industrial Strategy, 26 July 2017).

Nevertheless, policy-makers are concerned that the creative industries are not sufficiently engaged in global markets. The government's 2018 *Creative Industries Sector Deal* aims to increase exports by 50 per cent before 2023 because the sector still offers a lot of "untapped potential" with many businesses not yet exporting at all (Department for Business, Energy & Industrial Strategy, 2018). The Department for Digital, Culture, Media & Sport (DCMS) maintains that only 18 per cent of creative industries firms are engaged in international trade (DCMS, 14 February 2018).

Creative firms are seen as having industry-specific barriers to international trade, in particular small company size (Department for Business, Energy & Industrial Strategy, 2018). The average creative company size is 3.3 full-time employees (FTE) and 34 per cent of creative sector workers are self-employed, which is more than double the UK average (Bazalgette, 2017). The *Creative Industries Sector Deal* states that micro-companies lack the “absorptive capacity” to undertake extra export duties such as identifying and assimilating useful information and using it to commercial ends (Department for Business, Energy & Industrial Strategy, 2018).

Our case study calls many of those assertions into question. In at least one creative industry hub – at Baltic Creative in Liverpool – even small one-man-bands are already deeply engaged in the global economy. Creative industry firms in this cluster are exporting at much higher rates and with more economic impact than official figures suggest. Small company size does not appear affect their ability to export. Are small, local creative industries more global than we think?

International Trade at Baltic Creative, Liverpool

Baltic Creative in Liverpool provides commercial space specifically designed for creative and digital industries, housing almost 100 SMEs (small and medium sized enterprises) and dozens of freelancers. In the UK, the creative industries comprise advertising, architecture, arts, crafts, design, film and TV, IT and software, museums, music and publishing – including both goods and services in these fields (Department for Business, Energy & Industrial Strategy, 2018).

In May 2018, we asked freelancers and company owners all based out of Baltic Creative to complete an online questionnaire about their international reach. This “International Trade Survey” consisted of 16 quantitative and qualitative questions. It was sent to 75 tenants, of which 59 responded. Each question in the online survey left room for a supplementary, open-ended reply. Many respondents used this space to clarify their responses. All of our statistics about company imports and exports are derived from this survey. In July 2018, we also conducted almost a dozen semi-structured, personal interviews.

In addition, we cross-referenced the 2018 International Trade Survey with data from Baltic Creative’s 2018 Business Owners Output Survey. Here, each year Baltic Creative’s tenants are asked to provide key figures including questions on annual turnover, annual growth and expected growth. In 2018, 71 company owners responded to this survey. We used this data to arrive at figures such as median company size, annual turnover, and per-employee GVA of both exporters and non-exporters. Combing responses from both surveys, we have data from 89 SMEs or freelancers.

Since the sample size of 89 is relatively small, we have used the median rather than the average when discussing the results. A very small number of firms at Baltic Creative have turnovers well in excess of £1m and employ over 50 workers, which would significantly distort the average of a small sample. By using the mean we have arrived a more accurate snapshot of the “average” firm based at Baltic Creative.

Although “international trade” should normally refer to both imports and exports, we will use the term synonymously with “exports” for two reasons. First of all, the documents that we are interrogating – the *Industrial Strategy* and the *Creative Industries Sector Deal* – almost exclusively refer to international trade in the form of exports. *The Industrial Strategy* mentions imports only once and the *Creative Industries Sector Deal* never mentions imports. Secondly, of our 59 respondents, only one firm imported a small amount without exporting. In all other cases, tenants who engaged in importing also exported. Conversely some exporters did not import. Further details will be discussed in our results, below.

Results

SMEs and freelancers based at Baltic Creative are highly engaged in international trade, with 69 per cent of tenants exporting. Of the 31 per cent who do not trade internationally, one-third would like to start exporting in the near future (Figure 1).

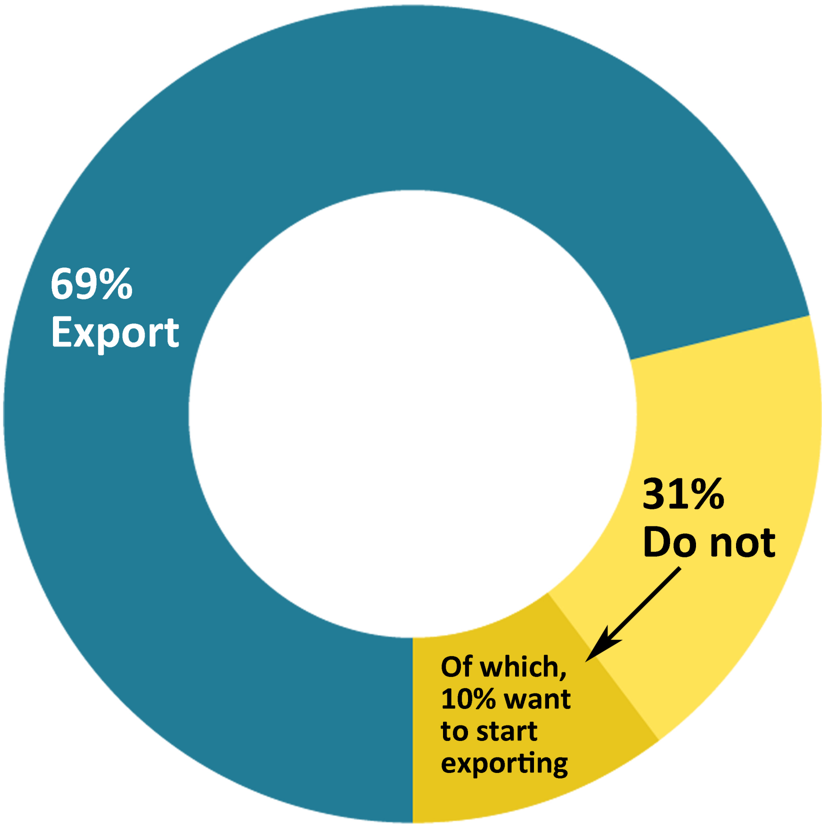

Figure 1 Proportion of Baltic Creative tenants that export

Isolating the exporting firms from the whole of Baltic Creative, henceforth "exporters," we find that most are trading in services with 70 per cent trading only in services, another 15 per cent trading in goods and services, and the final 15 per cent trading in goods only. Exporters reported that their primary concern around trade was Brexit. Europe is their main trade partner with 90 percent of companies exporting to the EU; 63 percent exporting to North America; and 51 percent trading with Asia.

Baltic Creative's exporters make a significant share of their income from overseas: 35 per cent of firms make over 50 per cent of their total income abroad, 37 per cent make between 10 and 50 per cent of their total income abroad, and 29 per cent make between one and 10 per cent of their total income abroad (Figure 2).

Figure 2 Baltic Creative's exporters rely heavily on their international income

Exporting is only half of the story. Exporters also import goods and services from abroad. While 21 per cent spent no money abroad, 38 per cent spent up to 10 per cent of their total expenditure abroad, 22 per cent spent between 10 and 25 per cent abroad, and the final 19 per cent spent over 25 per cent of their expenditure abroad. These last two groups of importers were hit by Sterling's sharp devaluation after the Brexit referendum in 2016. One business owner revealed that, because of sudden exchange rate fluctuations, his company lost £13,000 on the day of Brexit and more since then because of on-going international commitments.

Both exporters and non-exporters perceived the same major barriers to international trade: finding clients, access to knowledge and skills related to international trade, language and cultural issues. Interestingly, one would expect seasoned exporters to be less anxious, but instead exporters are more worried about customs procedures, delivery, tariffs and duties than non-exporters (Figure 3).

Figure 3 Perceived international trade barriers

Brexit then is a substantial concern for exporters at Baltic Creative because, at the time of writing, it is unclear whether tariffs and duties will be applied to goods and services entering the EU. Of all the companies we surveyed and interviewed, only two had managed to profit from Brexit. One business owner told us, "So far, Brexit has been good to us because the pound has weakened to the dollar and 65 per cent of our income is in US dollars. We've consciously spent more aggressively to acquire more US customers while the pound is weaker." The rest of the companies were either apprehensive about the effect of Brexit on their future business or had already faced significant losses since the June 2016 Brexit referendum.

Although 85 per cent of the surveyed companies trade in services and therefore do not face the prospect of direct taxes on goods, company owners (and European clients) still worry what the new trading environment will mean for permits, insurance and other compliance standards. As one photographer said, "I need a work visa for any shoots I do in the United States. I can't just enter on a tourist visa. My insurance would be void if I didn't get a work visa for the U.S. In Europe, I can just get up and go. I worry how Brexit will affect my work in Europe." His turnover is highly dependent on exports with 30 percent of his income coming from international work, of which 85 per cent is in Europe. Another SME owner admitted, "We are retrenching all international business and making teams redundant to increase productivity. Because of Brexit, we've lost 7 major contracts in the last 12 months, a risk we cannot afford to make again."

With 95 per cent of creative industry firms employing fewer than ten people (Frontier Economics, 2016), the *Creative Industries Sector Deal* identifies company size as a particular challenge to exports. Again, we have not found this to be true in our case study. Baltic Creative houses a selection of freelancers, micro-companies with under 10 employees, a few companies employing between 10 and 50 people, and only one firm employing more than 50 people. The mean company size of all tenants at Baltic Creative in 2018 was 2.5 full-time employees (FTE), with exporters slightly higher at 3.2 FTE. This is in line with, but slightly below, the national UK Creative company average size of 3.3 FTE (Bazalgette, 2017).

Discussion

The 2018 *Creative Industries Sector Deal*[1] contends that the micro-enterprises lack the "absorptive" capacity to increase exports. It does not, however, look deeply enough at the digital economy, which has – in less than two decades – dramatically reduced trade barriers for both large and small creative industries firms. According to the Centre for Economics and Business Research (Cebr), "We live in an era where the methods we currently use to trace trade flows are losing their relevance and ability to depict an accurate picture of trading realities," (Cebr, Creative Industries Council & Creative Industries Federation, 2018).

For an increasing number of creative industries firms, international business is not extra business: it's just business. One micro-enterprise owner told us, "We never set out to export. It's just the nature of the Internet to unlock that kind of potential without thinking you're starting a global business." This business creates YouTube content and over 75 per cent of its income is earned through overseas viewers and the associated advertising sales. The owner started the YouTube channel as a side project and now the firm employs 4 staff and 15 freelancers.

Another business owner told us, "In 2005…Google came up with this thing called Adsense. Overnight [my website] went from just [sitting on] the Internet somewhere to making more money than I made working full-time in the NHS." Using a website as their marketing tool, their company sold home-study DVDs. In 2013, they switched from selling DVDs to selling courses purely online, which only increased their international sales. The company currently makes 70 per cent of its annual income from exports and spends between 25 to 50 percent of its expenditure abroad. In 10 short years, the Internet transformed this micro-entrepreneur's career and business. The owner concluded, "If you are an online business and you are selling digital products, I think it's fairly standard that you are more of an exporter than…a domestic company because the cost of delivery is not there and the cost of fulfilment doesn't exist."

It's not only creative service providers that benefit from this borderless, digital global trading environment. Goods also have witnessed dramatic reductions in barriers to trade. "When we launch a product, we press release it [around the world]" another micro-enterprise owner told us. "As a result, it gets picked up by press and blogs in the US, UK and Europe. Our products are about film, music or literature…popular culture…that's why our customer base is so international." This micro-enterprise employs 4 full-time employees and earns between 50 and 75 per cent of income is from foreign sales.

The *Creative Industries Sector Deal* asserts that its priority for the creative sector is scaling-up: "helping the SMEs and entrepreneurs that overwhelmingly make up the sector to grow, in order to raise productivity," (Department for Business, Energy & Industrial Strategy, 2018). Interestingly, the two following examples of increased productivity resulted – not from scaling-up – but rather from clustering micro-enterprises into one shared location. One Baltic Creative company owner and exporter told us, "I recently hired a Google ads expert. I looked all over the Web to find somebody and there's plenty of companies or agencies that will do it…but in the end, I found a Google ads expert at Base Camp [a co-working space within Baltic Creative]. He is a real specialist and he sits next door. When you're in this online business everything is done by e-mail and it is a refreshing change to speak to somebody and express what you need in person instead of doing it backwards and forwards through e-mail…The first thing I do now is look to Base Camp." The company owner employs only 3 other people and earns between 50 and 75 per cent of its total income from exports. Rather than hiring a full-time employee to do the job, this micro-enterprise hired a neighbouring freelancer to increase exports. A second micro-enterprise owner told us, "We co-habit [our office] with another company, and they asked, "Why don't you claim for R&D tax credits? We do." The micro-enterprise owner had been unaware of the UK's Research & Development Tax Credit scheme. His unplanned, serendipitous conversation ended up saving his company thousands of pounds, which were then reinvested into the firm. Serendipity is an important benefit of clustering and it's countless opportunities for face-to-face contact (Storper and Venables, 2004).

[1]This includes the reports they reference: Peter Bazalgette's 2017 *Independent Review of the Creative Industries* and Frontier Economics' 2016 *Absorptive Capacity: Boosting Productivity in the Creative Industries*.

No interviewees saw a direct positive impact of clustering on their exports, but the benefits of clustering at Baltic Creative may be increasing their productivity, which would result in expanding their ability to export (Marrewijk). Clustering micro-enterprises may be a more economically viable and efficient way of helping SMEs "scale-up" – by expanding the network and knowledge base – without actually having to increase employee numbers.

Besides, scaling up does not always have advantages. At least one company owner cited worries about increased risks with scaling-up. Hiring more full-time staff required certainty of increased turnover. In an era of instability marked by Brexit, this micro-enterprise owner was unwilling presently to take that risk and preferred to hire freelancers on a case-by-case basis. Some economists point to clustering flops such as business parks where many similar firms share larger premises, but no interaction between tenants results (Wadha, 2011). This may be true, but clustering micro-SMEs and freelancers may produce different results from clustering larger companies. Businesses employing more than 10 people may indeed not require the serendipity and peer support that clusters offer because, as they grow, they hire specialised staff members and develop their own internal logic. But micro-enterprises and freelancers may benefit from the spill-over effects, networking and peer support that clusters such as Baltic Creative offer. Creative industries firms in 2007 were 15 per cent larger than in 2014 (Bazalgette, 2017) demonstrating a clear trend towards decreasing company size. Trying to force the industry in a direction that it is not naturally heading may be counter-productive. Instead, supporting creative clusters may be a more effective policy for increasing the productivity and exports of micro-SMEs and freelancers in the creative industries.

Our research is based on a small, geographically isolated sample of companies and cannot claim to represent a broader snapshot of creative industries in the UK. Indeed, economics research has found that the differences between individual firms are so astoundingly large, so-called "firm heterogeneity," that they call into question the viability of generalising from case studies (Marrewijk, 2017). We are indeed undertaking further research in four more creative industries hubs in England's North West to see if the trends extend to other digital and creative hubs. Moreover, we will revisit Baltic Creative in 2019 and 2020 to assess the impact of Brexit on tenants' international trade.

Key Insights

Our research suggests that official statistics may be understating the true value of exports to the creative industries. More refined and accurate data gives policy-makers better tools for designing effective strategies and efficiently allocating public funds.

The government's 2018 *Creative Industries Sector Deal* focuses efforts on helping creative industries firms to scale-up in order to increase exports. Our findings, however, show that small size is not hindering the exports of micro-companies based at Baltic Creative. Furthermore, these small companies are already highly dependent on their exports for total annual income.

Our findings are important because undervaluing current exports underestimates the possible negative effects of a significant break with the UK's hitherto successful international trading environment. If creative businesses are as financially reliant on exports as this study suggests, shocks such as a no-deal Brexit – or even the uncertainty caused by prolonged Brexit negotiations – are potentially far more wide-ranging on this set of businesses. A key factor in their export success has been the global, open, digital economy where international trade is integral to their business. The policy focus, then, should rather be on maintaining seamless – or at least consistent – access to global markets.

Should this prove to not be possible, gearing policy efforts towards providing affordable, not-for-profit creative industry hubs – and in underserved locations – may be a wiser allocation of public funds. Our preliminary research suggests that many creative industry firms do not want to scale-up, preferring to stay small and agile. Locating in a creative hub where they can temporarily employ the talent they need on a project-by-project basis, and possibly taking advantage of knowledge spill-over within the hub, may provide small creative firms safe harbour while they navigate the vagaries of Brexit.

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