



Is the start-up bubble about to burst?

There are said to be record numbers of start ups in the UK and the Government is encouraging more, with claims that it has never been easier to start a business. But starting in business is not the same as surviving in business, so is this really good news or a cause for concern? **BETTER BUSINESS** investigates.

According to the 2012 Business Population Estimates from the Department for Business, Innovation and Skills (BIS), the number of small businesses in the UK increased from 3.5 million to 4.8 million between the start of 2000 and the start of 2012. The recent *Growing Your Business* report published by BIS claims it has never been easier to start your own business, partly due to the help and support available from the Government.

It seems all you need is an idea and off you go – you can run the business from your back bedroom, use social media to generate leads and there are no expensive IT set-up costs as you can now buy a ready-made website and host it in the cloud. In fact, a recent poll carried out by PeoplePerHour found that the average cost of starting a micro business is just £312, significantly less than the average UK weekly wage of £442.

“Our members continue to see large numbers of people exploring the opportunity of starting their own business – this isn’t

unexpected during and coming out of recession as many think this might be their only option,” says Dawn Whiteley, Chief Executive of the National Enterprise Network.

But is this apparent increase in new start-up activity truly evidence of real new opportunities for start ups or will this increase in activity simply result in more start-up failures than ever before?



Dawn Whiteley, National Enterprise Network

The true level of start-up activity

It’s tricky to measure the actual number of new businesses, so the Government’s figures may not be very accurate. According to online accountants **Crunch**, this is especially the case with registered limited companies. Crunch’s Accountancy Training Manager **Laura Hughes** explains: *“Many new companies are formed as subsidiaries or ‘shell’ companies of existing organisations. These types of companies essentially contribute nothing to the wider economy, hence are not an accurate barometer of UK business activity.”* According to Crunch, a better representation of new business activity is the number of new PAYE schemes formed. The Government often quotes the figure of 451,700 newly registered limited companies in 2012/2013, but Crunch found that only 200,000 new company payroll schemes were registered in the same period. Hence it could be that, in reality, less than half the number

► page 20

► of new companies in the statistics are genuinely trading.

Not all businesses that start up register as limited companies or employ staff, and most micro businesses are launched and run by individuals who are registered as self employed. According to a report from the Royal Bank of Scotland (RBS), there are currently 4.2 million self-employed people in the UK, up from 3.8 million at the end of 2007 – the highest number on record. However, the report claims the rise in self employment is largely due to increased part-time self employment and that this will most likely continue.

“There are a growing number of people who start up a business while working so that they can test its viability and build up the capital required to leave their jobs,” says Dawn.

The ranks of the self employed may also soon be swelled by some of the one million people estimated by the Chartered Institute of Personnel and Development to be currently employed on flexible, zero-hours contracts where they are expected to be on call, but are not guaranteed any work from one week to the next. *“I’ve been working with some student entrepreneurs who are on zero-hours contracts, and running a business. These contracts often leave people with little choice but to look elsewhere for money to support themselves,”* says business coach and mentor **Ali Golds**.

Not ready for self employment

The RBS report also suggests that many people end up in self employment because of *“the push from unemployment rather than the pull of opportunity”*. Because these people, in effect, have been forced into it, they are often ill prepared for self employment.

Some people who have been made redundant are taken on by their previous employers as freelancers or contractors, which could land them in trouble with HM Revenue & Customs

Some people who have been made redundant are taken on by their previous employers as freelancers or contractors, which could land them in trouble with HM Revenue & Customs. *“According to HMRC rules, they may still be considered as employed, especially if their ex-employer determines how and when they do the work and if they have no other customers or clients,”* says **Graham Wilde**, Director of tax consultancy **TaxNetUK Limited**. *“The Revenue could cancel their self-employment status down the line and demand that the employer pays all relevant taxes for the period, but even if the freelancer had already paid self-employed tax, they may not be able to claim it back.”*

When they do try to get more new customers, some start ups offer their products and services at rates or prices lower than their established competitors. *“While this doesn’t impact too much on the latter in terms of driving down prices, many of these new businesses probably won’t be around for long,”* says **Julia Weldon**, a former business start up adviser. *“Many people prefer to choose goods and suppliers on the basis of quality and value, so they may be put off by cheap prices. Lower prices only appeal to customers looking for the cheapest deal and who will probably not be loyal. New start ups could be spending a lot of time and energy in marketing to get more new customers and not actually generating any orders, or only making a small profit that*

won’t even cover their overheads.”

Even if these low-priced orders do come in, especially all at once, the business may not have enough time or capacity to fulfil them. *“This will impact on the quality of service and hence repeat business,”* says Julia. *“Also, too many orders can lead to ‘overtrading’ where the business doesn’t have the cashflow capacity to purchase enough supplies to meet the orders; this is another common reason for start-up failure.”*

More reasons for failure

According to the RBS report, the one-year survival rate for a new business in 2012 was 82%, down from 86.7% in 2010 and 96.5% in 2007, and it is likely to be even lower at the moment.

“Many people don’t understand or underestimate the difficulties in starting a business,” says **Neil Davey**, Enterprise Coaching Programme adviser at **Working Links**. *“They may not have a viable idea or customer base, they may lack finance, skills and knowledge to run a business, but they go ahead regardless.”*

Lack of confidence or networking skills often cause problems, too. *“They aren’t sufficiently proactive in generating interest in their business and if it doesn’t take off quickly, they give up, not realising it can take many months or years to become established,”* says Julia. Others, even if they manage to drum up enough interest in their business at the launch, do not cope well if the interest wanes. *“When sales drop, and the marketing effort is not maintained or increased, they often feel it’s not working out and give up. Some give up because they find the business requires more of their time and energy than they can give – self employment is an all-consuming lifestyle that isn’t right for everyone.”*

The levels of self-employed income cannot be guaranteed, either. Some people do not adjust well to this uncertainty, especially now when, according to RBS, average self-employment income is more volatile and has fallen 5% below where it was in 2008. Add to this bills and debts that cannot be paid, and more people than





ever are being forced to file for personal insolvency. Individual insolvency rates released by the Government show a steeply upward path from 2004 until mid-2010, which is still elevated compared to the annual average seen over the last 25 years.

The choice of sector can work against start ups, too. According to the five-year data from the Office for National Statistics, the professional, scientific and technical sectors have the lowest rates of survival, followed by construction, hotel and catering, business administration and support services. The sectors boasting the highest survival rates over the same period are health and education. However, the authors of the RBS report note that the recent rises in self employment show no relation to the sectors that have the best business survival rates and say: "Therefore, newly self-employed businesses may find it harder going than in the past."

Will the bubble burst?

Poor access to finance has been stopping many start ups from thriving. "There's limited Government funding and, in general, the high-street banks remain reluctant to lend where there is no experience, track record and

security in place," says Dawn. In an attempt to encourage more start ups, the Government-backed Start Up Loans scheme has recently raised its application age limit to 30. "Many of our members are fully supportive of and actively involved in the delivery of Start Up Loans," says Dawn. "There has been some bad press for the scheme, but where the delivery is through any of our members, I have absolutely no doubt that all the right checks and balances will be put in place so that the client is only taking on the debt for an idea that has a good chance of success."

Small businesses have been turning to alternative lenders such as the peer-to-peer lending platform Funding Circle, which now also lends to sole traders. "However, too many funding streams have too complex an application process and this deters people from applying," says Neil Davey. "On the other hand, many of the clients we see on our programme are wary of taking on any form of debt even if funding is available."

Overall, more people are being encouraged and offered finance to start a business and enter the 'bubble', but will the 'bubble' just burst more quickly because of this? "I agree," says Ali Golds. "If more people borrow money without looking at the alternatives, we will see more failures. Setting

up a business needs to be taken seriously; the plethora of loans available makes me feel that it's being made to look much easier than it is and that scares me."

Neil's view is more positive: "I disagree that the bubble will burst more quickly as a result – as long as the appropriate steps are taken to support and train those people to ensure they understand the risks they are taking, and they possess the skills and knowledge to match a viable idea and take it to fruition." ■

INFOBANK

The National Enterprise Network

(www.nationalenterprisenetwork.org)
A membership body for not-for-profit organisations that provide independent and impartial advice, training and mentoring to new and emerging businesses. In 2011/2012, their members supported almost 69,000 clients considering starting a business.

Working Links (www.workinglinks.co.uk)

Their Enterprise Coaching Programme in Plymouth offers a holistic package of advice, guidance, information and business training, including tax and finance workshops, to those considering self employment.

Ali Golds

(www.aligolds.com, tel 07554 185909)
Ali works with student entrepreneurs, enterprise educators and other organisations across the country.

Graham Wilde

(www.taxnettuk.co.uk, tel 01202 237950)
Graham advises companies and individuals on all aspects of UK tax.

Many people...may not have a viable idea or customer base, they may lack finance, skills and knowledge to run a business, but they go ahead regardless