START-UP, SCALE-UP

Making Britain the best place to start and grow a business

Labour

THE PANEL

Tom Adeyoola is a technology entrepreneur passionate about disruptive technology for societal and climate good. He was CEO and founder of acquired apparel technology scale-up Metail (2008-2019). He is currently a co-founder of non-profit Extend Ventures, which aims to diversify access to finance for under-represented founders through data and research. He also serves as non-executive director for zero carbon monitoring consultancy Verco and environmental behavioural change start-up 'Do Nation'.
In addition, he is an active angel investor, chair of mindfulness app Spoke, governor of his former school St. Paul's, member of the London Mayor's Business Advisory Board and served on the board of the women's personal wellness scale-up Elvie (2013-2017).

Alex Depledge is CEO and co-founder of Resi.co.uk, the UK's largest home improvement platform. As of 2022, Resi has helped over 6,000 homeowners transform their properties and employs over 100 residential, financial, and coding experts. Recently named as one of the UK's 30 female founders to watch by the Financial Times, Alex has also earned herself an MBE for her services to the British tech industry. Her first start-up – founded with her long-standing business partner, Jules Coleman – Hassle.com, went on to become Europe's largest domestic cleaning marketplace and was sold for a reported £32 million. Alex also served on the Mayor of London's LEAP board between 2017-21 investing £500 million in sustainable growth for London.

Julie Devonshire is the Director of the Entrepreneurship Institute at King's College London supporting students, alumni and staff to learn entrepreneurial skills, acquire entrepreneurial experience and launch start-ups of their own. Over the last five years King's has supported more than 120 ventures that have collectively raised £55.5 million in investment and employ over 400 people. Julie is an ACCA Fellow and award-winning social entrepreneur, receiving an OBE in 2016 for her services to entrepreneurship, in the Queen's 90th Birthday Honours List.

Lord Jim O'Neill is a cross bench peer, and non-executive chairman of Northern Gritstone. He was Chief Economist, Goldman Sachs (2001-2013) and Chairman, Goldman Sachs Asset Management (2010-2013). From 2015, Jim served as a government minister having responsibility for championing the Northern Powerhouse and the focus on driving innovation to the North of England. Jim remains deputy chairman of the Northern Powerhouse Partnership. Jim is an alumnus of the University of Sheffield and is an Honorary Professor of Economics at the University of Manchester.

FOREWORD
FROM RACHEL REEVES

These are challenging economic times. But I know the spirit of enterprise, of creativity, of hard endeavour are as present in Britain today as they ever have been. I have seen that time and again as Shadow Chancellor, as I have had the opportunity to see the work of businesses and entrepreneurs all around the country.

We are at a post-Brexit crossroads. We can continue down the road of managed decline, falling behind our competitors, or we can draw on bold thinking to propel us forward. We can cling to the old ways; or we can apply ourselves with creativity, determination and common sense to shaping our future outside the European Union, while improving our trading relationships, including with our nearest neighbours. That calls for fresh thinking about regulation and planning, access to finance and strategic partnership with industry, so that we lead the way. That is why I am so pleased to welcome this radical plan to make Britain the high growth, start-up hub of the world.

Innovation is a great British strength. It defines our history, and it endures today in our entrepreneurs and businesses, in our world-leading universities, and in our people. These are immense resources. Fast-growing firms already contribute £1 trillion to our economy and employ 3.2 million people.

But I have heard time and again about the stubborn obstacles preventing many businesses from scaling up, and the opportunity to start and grow a business is still not shared widely enough. If we can remove those obstacles – if we can unlock that potential – that has implications not just for the entrepreneurs and founders of tomorrow, but for all of us. If the UK had the same level of venture capital investment as a % of GDP as the US, this would mean £16 billion more venture capital investment - nearly double the level currently. This would mean more innovation, higher economic growth, and better living standards.

The start-up review was tasked with giving us a road map to get there, to ask the difficult questions and present solutions: about incentives, access to capital, how to encourage more spin outs from our leading universities, and how to make the most of entrepreneurial potential across the whole country and from a more diverse range of founders.

The report is full of important ideas addressing exactly those questions: about the ambition and autonomy of the British Business Bank and unlocking patient capital; about how we can translate our world-leading university research into innovation and economic growth; and about building on our pre-existing system of tax reliefs for entrepreneurs and investors – Seed Enterprise Investment Scheme, the Enterprise Investment Scheme and R&D tax credits – to widen access and ensure those tax reliefs work to the greatest effect, spurring innovation and entrepreneurship. The ideas contained in this document will inform the development of our next manifesto.

I want to thank Alex, Jim, Julie and Tom – and the many others who took part in roundtable discussions and our call for evidence – for bringing their experience, commitment and insight to Labour's start-up review. This document, Start-Up, Scale-Up provides crucial insights towards achieving one of the guiding ambitions of the next Labour government: to make Britain the best place to start, and to grow, a business. And it sends a powerful message: that Labour is back in business.

Rachel Reeves,
Shadow Chancellor of the Exchequer

I am so pleased to welcome this radical plan to make Britain the high growth, start-up hub of the world.

EXECUTIVE SUMMARY

Labour has set out an ambition to make Britain the best place to start and grow a business. Shadow Chancellor, Rachel Reeves, asked us to undertake a review to this end – and this independent report to the Labour Party, 'Start-up, Scale-up', is the first step on that journey. It is the result of hundreds of submissions and conversations with entrepreneurs, investors, and others from across the ecosystem, and brings together their experiences and insights.

Our review has produced a number of policy recommendations that a future Labour government should consider. They include recommendations on mobilizing more institutional capital to finance growth, incentivising investment, supporting entrepreneurs from all backgrounds, and ensuring institutions serve the start-up and scale-up ecosystem as well as possible.

Key recommendations:

Unlocking institutional investment and patient capital: Britain should draw on the experience of the successful Tibi scheme in France, to build engagement and understanding between institutional investors and VCs. Labour should also review the opportunities for ISA investors to invest in high-growth firms, and ensure pension fund investments are as effective as possible, via fund consolidation and frameworks for institutional investors to invest alongside the British Business Bank (BBB).

Transforming the British Business Bank: Labour should ensure the BBB has the level of independence, remit, and aspiration it needs to succeed, as well as the ability to leverage external funds to amplify its work. And it should use its support to foster clusters around groups of universities to drive growth and investment across the whole of the UK.

Translating world-leading research into growth: A Labour government should publish, annually, a dashboard summarising each university's offer to spinouts, and metrics of each university's spinout success. It should also recommend that all universities offer a range of options for spinout founders to choose from, including an option where the university keeps a relatively small stake of equity.

Making public procurement work for start-ups: Labour should create a Procurement Council of Experts to review best practice and identify areas of improvement and should review the barriers to better pre-market engagement.

Incentivising investment and entrepreneurship: Labour should maintain and build on existing incentives, such as SEIS, EIS and the R&D tax credit system, to ensure investors and firms have the best possible incentives for growth.

Our review also summarises the responses to our call for evidence, and the insights gleaned from the eight roundtables that we held. These brought together diverse participants from the whole breadth of sectors and roles that comprise the start-up and scale-up ecosystem, and we are hugely grateful for their insight and expertise.

SECTION 1:
POLICY RECOMMENDATIONS

1. Unlocking institutional investment

Patient, long-term capital is crucial for the growth of innovative firms. One of the key sources of patient capital is institutional investors, and, in particular, pension funds. Compared with some of our international peers, the UK sees relatively little VC funding coming from pension funds. In the US, around 70% of VC funding comes from pension funds, but in the UK this figure is under 20%.[1]

- *A British 'Tibi' scheme to bring together institutional investors and VCs*
  In responses to the call for evidence, and in discussions with market participants, it was raised multiple times that there are barriers to institutional investment in high growth firms that are separate from regulatory barriers - in particular a lack of links between institutional investors and VCs. The BBB reforms set out below are one channel through which this could be tackled, but on top of this Labour should initiate a British 'Tibi' scheme. This would aim at improving engagement and understanding between institutional investors and VCs, using the convening power of government to do so.

  As with the French Tibi scheme, which as of June 21 had raised over €18 billion of institutional investment, this would be a scheme bringing together participating institutional investors with an accredited list of VC firms. The institutional investors would be asked to allocate a small proportion of their funds to the scheme, but would have full discretion over which VC funds to invest in from the list.

  As well as directly facilitating this investment, the scheme would enable increased engagement between institutional investors and VCs to foster better understanding of each other's needs. Labour should also, as part of the scheme, bring together accredited VCs and institutional investors to workshop innovative DC-centric fee arrangements – there is a strong incentive for VCs to engage with this given the ever-increasing size of DC schemes.

  British Patient Capital could be tasked with vetting VC applicant firms and drawing up the accredited list.

- *Reviewing opportunities for ISA investment in high-growth firms*
  Labour should explore ways to foster the provision of Long Term Asset Fund (LTAF) products for ISA investors who meet certain suitability criteria. This would allow a greater range of retail investors to invest in growing companies. In doing so, Labour should also assess how best to strike a balance between allowing ISA holders to invest in a greater range of assets and ensuring that this does not expose them to excessive risk.

  This would build on the 2013 change that allowed for ISAs to be invested in companies listed on AIM – a change that is estimated to have provided between £5 billion and £10 billion of patient capital for high-growth companies. There is more than £300 billion held in stocks and shares ISAs.

1 Beauhurst and British Business Bank. 2019. Small Business Equity Tracker. Available from: https://www.british-business-bank.co.uk/research/small-business-equity-tracker-2019/

- *Consolidating pension funds*
  A significant barrier to increasing DC pension fund investment in high-growth firms is the relatively small size of many UK DC funds. It is difficult for smaller pension funds to have the necessary governance and expertise in place for such investment, and their size means they have little bargaining power when it comes to negotiating performance fees. Labour should therefore require schemes below a certain size to consider, as part of their fiduciary duty, whether they are large enough to deliver fully in their members' interests. The government previously legislated to do this for schemes smaller than £100 million, but real change will require a significantly higher threshold.

  Labour should also review whether there are other policy levers that could be used to encourage DC pension fund consolidation – which could have significant benefits for pension holders as well as for wider economic growth through increasing the provision of patient capital.

- *The pension charge cap*
  This review sets out a number of measures aimed at bringing more pension fund investment into high-growth firms. The measures above are aimed at overcoming some of the non-regulatory barriers – a culture of conservatism in institutional investment, and the capacity requirements that managing such investments could entail. However, a number of responses, as well as participants at our roundtables, highlighted the current formulation of the pension charge cap as a barrier to greater investment.

  It seems likely though that further consolidation of DC pension funds would be required before changes to the charge cap might be worth serious consideration and assessment. Also, at present, a relatively small proportion of overall pension fund assets are covered by the charge cap. Labour should therefore keep the pension charge cap under review as the DC pension landscape develops.

2. Transforming the British Business Bank and making it truly independent

The British Business Bank (BBB) is a crucial pillar in the UK's policy support for start-ups and high growth firms. However, it has the potential to be even more effective – by giving it true operational independence, leveraging in more external funding, and more deliberately targeting its remit.

- *Giving the British Business Bank the true independence it needs to invest in growth* – At present, the BBB's business plan is annually reviewed and subject to approval by government, and its board has to consult the government regarding any changes it might make to its business plan. This makes it difficult for the BBB to pursue its objectives on a long-term basis – with its KPIs and strategy at risk of changing annually.

  Instead, a Labour government should extend this review period, which would in effect give the BBB greater operational independence to match the ambition government should have for it. This would allow the BBB to plan to a longer-time horizon and empower it to be more ambitious. This would also give further certainty to the entire funding ecosystem around start-ups, and build greater confidence to investment in the various asset classes involved.

- *Leveraging external funds:*
  Crowding in billions from pension scheme funds – DB pension funds have nearly £3 trillion in assets under management[2] – unlocking even a small proportion of this into BBB investments would be a substantial boost to the amount of additional financing available to BBB investment recipients. To do this a framework should be established for BBB investments so that external investors such as DB pension schemes and insurers will always be able to invest alongside it on comparable terms. This will help such funds from being restricted in allocating funds to VC and growth by the high informational barriers to entry, by allowing them to effectively piggy-back on the BBB's due diligence.

2 Office of National Statistics (ONS). 2022. Funded occupation pension schemes in the UK: July to September 2021. Available at: https://www.ons.gov.uk/economy/investmentspensionsandtrusts/bulletins/fundedoccupationalpensionschemesintheuk/july2021toseptember2021

Alongside this Labour should support work to broaden pension scheme coverage of the Long Term Asset Fund category and look at ways to support coordination of investments through these funds of DC pension funds with the BBB.

Unlocking more finance for SMEs – Labour should examine securitisation of ENABLE programmes to facilitate greater scale. This would enable more lending by challenger banks and small business lenders to SMEs to invest in their growth.

Powering up Regional Investment Funds – Local Government Pension Scheme (LGPS) funds have c. £340 billion of assets under management, of which £30 billion is already invested in alternative asset classes, such as VC.[3] In order to mobilise some of this capital into regional growth, Labour should convene BBB Regional Funds and the relevant regional pools of LGPS funds. And Labour should look at adjusting the terms of reference for LGPS funds so that while investment return would remain their priority, it would be clear that at the margin they could consider regional development as an investment factor, in a similar way to how broader ESG considerations are taken into account. This would increase the capital available for investment in their regions, for example through VC or into social enterprises, and give pension holders a stake in the growth of their regional economy.

- *Giving the BBB a remit fit for the future:*
  Translational funding for spinouts and supporting universities to work together – As part of achieving its regional KPI, Labour should instruct the BBB, through its Regional Funds, to offer match funding for Spinout Seed Funds. Each such fund would have to have been set up by a consortium of universities, on the basis that their resources and networks would also be pooled. These would provide translational funding to help bridge the gap between early-stage innovation resulting from university research and its commercialisation. They would also encourage universities to share resources and networks to reach a critical mass – so that self-sustaining clusters could develop to encourage innovation and growth in their local area.

  Targeting the deployment of finance to women and ethnic minority founders – Labour should also agree two additional KPIs with the BBB which set out an investment allocation target for the deployment of finance specifically supporting women and ethnic minority founders, and report regularly on the proportion of applications it considers that are from women and ethnic minority founders.

  Investing in Ethnic Diversity Code – Labour should build on the Investing in Women code set out in response to the Rose Review with a similar code for ethnic minority founders, reporting on progress against the code in addition to the measures outlined above.

  Deploying finance in every region of the UK – Labour should upgrade the BBB's KPI relating to deploying finance outside London by setting KPIs for finance deployed in each region, ensuring that the BBB will report and be held to account for its impact on financing available in every region individually.

  Fostering green investment – We welcome the BBB's new KPI of a target amount of investment aligned with net zero. Alongside this Labour should mandate that the BBB considers as an investment factor how it can help facilitate the emergence of a wider net zero investment landscape.

3. Translating our world-leading university research into economic growth.

One of the UK's undoubted strengths is its universities and the research undertaken in them. The 2021 Research Excellence Framework found that 84% of UK university research was either

3 Local Government Pension Scheme Advisory Board – England and Wales. 2022. Scheme Annual Report 2021. Available at: https://www.lgpsboard.org/index.php/schemedata/scheme-annual-report ‘world-leading’ or ‘internationally excellent’.[4] University spinouts, which commercialise this innovation, can directly drive up economic growth and productivity. But, by some measures, we lag behind countries like the US on generating and scaling spinouts. The recommendations below aim at bridging this gap, which would boost economic growth across the UK.

- *University Spinout Dashboard* – A Labour government should publish, annually, a dashboard summarising universities’ offer to spinouts, and their spinout data.

  This should include:
    - The average equity each university/Technology Transfer Office (TTO) have taken in spinouts over the past five years.
    - The average IP agreement made with each new spinout over the past five years, for both government-funded and non-government funded research.
    - The nature of support offered by the university to spinouts.
    - The number of spinouts founded at the university over the past five years.

  Universities should be required to provide this information annually.

  This would foster greater transparency, helping to address the information asymmetry that spinout founders face during negotiations. As explained below, spinout agreements can be an important factors in the future success of spinouts, particularly in their ability to raise funds in future. Requiring universities to publish both their realised agreement terms and metrics on the number of spinouts will also help to encourage them to attach greater priority to the commercialisation of research.

- *Founder-track agreements* – A Labour government should recommend all universities offer a range of options for spinout founders to choose from.

  In particular, universities should be asked to sign up to offering a ‘Founder-track’ option, one where the university takes a share of equity at or below 10%. Such an option could mean founders accepting a different level of support from the university, and Labour would need to consult with universities, founders, and investors, on the details of what the option should look like, with regards IP licensing, non-dilution protection, and the level of support that TTOs would offer alongside it.

  This would help address concerns that the higher equity stakes taken by UK universities are hampering UK spinout growth relative to other countries. But it would mean universities could continue to offer an alternative option where they would get a higher share of equity, and could decide what support to offer spinouts alongside that.

4. Making public procurement work for start-ups

Procurement can play an important part in supporting innovation, not least by helping start-ups and small businesses gain access to a market by being an anchor customer of their goods and services at an early stage. However, evidence suggests that the proportion of public sector procurement spending going to small businesses has decreased since 2016, from 25% to 21% in 2021,[5] and our discussions highlighted a range of obstacles.

- *Create a Procurement Council of Experts to review best practice and identify areas of improvement* – There are always constraints on procurement - the Cabinet Office cannot dictate every procurement and nor can the government always attract the best well-paid private sector leaders. But central government can do more to improve procurement across the public sector. Labour

4 Research Excellence Framework. 2022. New evidence highlights world-leading quality of university research. Available at: https://ref.ac.uk/guidance-and-criteria-on-submissions/news/new-evidence-highlights-world-leading-quality-of-uk-university-research/

5 British Chambers of Commerce and Tussell. 2022. SME Procurement Tracker. Available from: https://www.britishchambers.org.uk/media/get/British%20Chambers%20of%20Commerce%20&%20Tussell%20%20-%20SME%20PROCUREMENT%20TRACKER%202022%20-2.pdf

should set up a Procurement Council of Experts, made up of experienced leaders from the public, private, and third sector, including those from the co-operative and social enterprise sector, to review and advise on best practice. In particular, this would review and make recommendations on timing of procurements; forms of pre-market engagement; value for money; and standards. Labour should also explore how this council could, on a regular basis, assess the performance of government procurement, and at what level that could best be done. This could work in support of Labour's proposed Social Values Council.

- *Pre-market engagement*
  Labour should review the barriers to greater pre-market engagement in public sector procurement and assess the case for making pre-market engagement mandatory for all government buyers. This would complement Labour's existing policy around pre-market engagement with SMEs.

  Labour should also work to introduce greater engagement at different stages of a tender, including in tender design, to build openness to innovation into the service being defined. This will require greater use of novel market engagement strategies - roadshows, pitch days, and hack days.

5. Incentivising investment and entrepreneurship

Both the tax system and the accessibility of public equity markets have an important role to play in incentivising investment and entrepreneurship. As well as exploring where changes could be made for the better, Labour should commit to maintaining the parts of the system that work.

- *Commit to maintaining SEIS, EIS and VCTs* – Through the call for evidence for this review, and the various roundtables that we have held, it is clear that there is strong evidence as to the benefits of both the SEIS and the EIS schemes in stimulating investment and entrepreneurship. Labour should commit to maintaining the incentives provided by those schemes and should commit to continuing the EIS and VCT incentives beyond their 2025 sunset.
- *Review whether the scope and scale of EIS and SEIS are sufficient* – Labour should review the scope, scale, and design of both EIS and SEIS to ensure they are providing adequate incentives. This should include looking at whether the limits on how much companies can raise or the investor-side caps are too low, whether the qualifying period should be extended, and whether there are important innovative sectors that are excluded by the current rules.
- *Maintain and build on the R&D tax credit system* – Labour should ensure that the R&D tax credit system continues to adequately incentivise investment and innovation by high growth firms, including SMEs. Labour should also look at whether there are ways to make the process less burdensome for firms, balancing that with the need to tackle fraud.
- *Modernise the business rates system* – Labour should continue its work to reform and modernise the system of business rates to ensure that it incentivises entrepreneurship and does not place an undue burden on small businesses, particularly those that are pre-profit.
- *Review performance of UK public equity markets* – UK public equity markets continue to be an asset, but there have been some concerning trends in recent years. Given those trends, and recent changes following the Hill Review, a Labour government should undertake a progress review to assess whether further changes are required – in particular by monitoring where UK start-ups choose to list in coming years, to make sure regulation and the listings regimes are providing the best possible environment for UK firms to grow.

SECTION 2:
ACCESS TO PATIENT CAPITAL

Patient, long-term capital is crucial for the growth of innovative firms. Many such firms may not be profitable in the early stages, and will need longer time horizons around which to plan and invest in their growth. The shortage of such capital in the UK has long been recognised, and has become a particular focus as economic growth and, in particular, growth in productivity has been markedly lower over the last decade relative to previous decades. The gap is starkly illustrated by the fact that in 2021, venture capital invested £17.3 billion in the UK[6] versus $327 billion in the US.[7]

Responses to our call for evidence focused mainly on two particular gaps in terms of stage of funding, at pre-seed/seed stage, and at a later stage in between early-stage funding and public equity markets.

1. Pre-seed/seed

Respondents to the call for evidence, as well as participants in the roundtables, highlighted a gap at the pre-seed/seed stage (i.e. raising less than £1 million), especially outside of the London-Oxford-Cambridge triangle and for female and minority founders – as discussed further below.

The evidence supports this qualitative assessment - while the UK start-up ecosystem experienced a record high level of investment in the first half of 2021, 'seed' deals for less than £4m decreased to below 10% of all deals, less than half the proportion seen in 2012.[8] In two reports published in 2021 and 2022, market analytics firm Beauhurst outlined how both the absolute number of first round seed-stage equity deals, and the relative proportion of first round deals compared to second round seed-stage and beyond, have decreased in recent years.[9] And despite a slight recovery in 2021, the number of seed-stage equity deals remains down 18% from 2018.

Participants in roundtables also noted that there are limited debt funding options for growing companies. Historically lenders have relied on tangible asset security when lending to smaller companies. On top of the issues this can create (some of which are discussed further below), as the economic landscape shifts towards knowledge-led firms, it was pointed out that firms may have less in the way of tangible assets to secure loans. Roundtable participants pointed out that banks are highly reluctant to secure debt funding against IP.

2. 'The Valley of Death' – series B and subsequent rounds

Beyond the earliest stages, a second funding gap was raised by respondents – an equity funding gap between early-stage and the point at which businesses might be large enough for public equity markets. It was felt that there were insufficiently deep pools of VC capital, and this was highlighted as especially problematic in fields such as deep tech, where greater quantities of capital tend to be needed to reach profitability.

This is reflected in the UK's relative lack of success in scaling companies to the same level as some other countries. While two of the world's 15 most valuable privately held tech companies are from the UK (Revolut and checkout.com), no FTSE 100 top ten UK company has been built or scaled in the last 20 years, which is in stark contrast to the experience in the US.

6 British Venture Capital Association. 2022. Growing Great British Businesses. Available at: https://www.bvca.co.uk/Portals/0/Documents/Research/2022%20Reports/Growing-Great-British-Businesses-2022.pdf
7 Pitchbook. 2022. Pitchbook – NVCA Venture Monitor. Available at: https://pitchbook.com/news/reports/q4-2021-pitchbook-nvca-venture-monitor
8 Fulton, K. 2021. After raising 'astonishingly high' investment, UK tech scaleups must now consider their future impact. Tech Nation. Available from: https://technation.io/news/uk-tech-scaleups-must-decide-on-their-future-impact-after-astonishing-vc-growth-in-2021/
9 Beauhurst and SFC Capital. 2021. Seeding to Succeed: The Seed Stage of the Ecosystem. Available from: https://www.beauhurst.com/research/seeding-to-succeed/ and Beauhurst and SFC Capital. 2022. Seeding to Succeed: First-time Deals 2021 Trends. Available from: https://www.beauhurst.com/research/first-time-deals-2021/

Causes of these gaps
Responses highlighted in particular two prominent and closely connected causes of the later stage funding gap – the risk averse investment culture in the UK and the lack of institutional funding. A strong focus of responses explaining these causes was on the barriers to greater availability of pension fund capital. This lack of institutional funding is particularly brought out by the fact that when it comes to pension funds, which are one of the key sources globally of patient capital, international funds are sizable investors in VC compared to UK funds.

In the US, around 70% of VC funding comes from pension funds, but in the UK this figure is under 20%.[10] This points to a significant missed opportunity. DB pension fund assets are currently worth nearly £3 trillion, and DC fund assets are expected to double to £1 trillion by the end of this decade.

In addition, mobilising greater amounts of pension capital into high-growth firms could have significant benefits for UK pension holders too. Between 2015 and 2020 UK VC achieved 23% five-year annual net returns, compared to the FTSE 100 return of 6.2%. A 2019 report showed that the retirement savings for an average 22-year old could be increased by as much as 7-12% if their savings were exposed to venture capital, with the average 45-year old potentially seeing an increase of 6-7 per cent.[11]

A lot of consideration has been given to addressing some of these problems, and a common explanation among respondents was that there is a broad cultural conservatism in UK asset management. It was argued by roundtable participants that the UK's finance ecosystem is institutionally predisposed to a lower asset allocation to VC (as well as other forms of illiquid investment, such as infrastructure). Whilst clear there was no easy solution to this, several respondents felt that progress could be made by bringing together pension funds, insurance firms, and VC funds, to build an institutional ecosystem that would in time result in greater asset allocation to start ups.

With reference specifically to DC funds, respondents made clear that consolidation of those funds would help spur greater allocations to VC – the fragmented nature of the UK DC pension landscape makes it difficult for funds to have the necessary governance or expertise in place to justify investing in some alternative asset classes. By contrast, it was pointed out, the top 15 mega-funds dominating Australia's pensions sector have each amassed assets of around AU$100-200 billion (£56-112 billion). Greater scale has resulted in superfunds increasing their average allocation to infrastructure to 20%.

Regulatory barriers
Many respondents and roundtable participants also highlighted regulatory barriers. In particular, the charge cap on DC pension funds is widely seen as a barrier to UK DC funds investing in VC. It was felt that changing the rules around the cap could not only boost venture investment in Britain's fastest growing companies, but could also ensure that a wider group of people could reap the rewards from the growth of those businesses through their pensions. It was also recognised, however, that with the pension charge cap only currently applying to a relatively small fraction of UK pension assets, changes to the pension charge cap would not be a silver bullet.

Furthermore, it was highlighted that the current DC fund landscape, with multiple smaller funds, meant it was less likely that DC funds would have the relevant expertise to manage VC investments, even if the rules around the cap were changed to facilitate that.

Separately, there were some suggestions that qualified investors should be allowed to invest in unquoted companies through their ISAs, and that the existing barriers to investment in start-ups outside crowdfunding were prohibitive, but it was also noted that the FCA's Long-Term Asset Fund (LTAF) structure could provide a more diversified alternative.

In terms of debt provision to start ups, it was highlighted that alternate lenders to small and start-up businesses still struggled to access wholesale capital, and that improving this could in turn help drive SME lending growth.

10 Beauhurst and British Business Bank. 2019. *Small Business Equity Tracker*. Available from: https://www.british-business-bank.co.uk/research/small-business-equity-tracker-2019/
11 British Business Bank and Oliver Wyman. 2019. *The Future of Defined Contribution Pensions*. Available from: https://www.british-business-bank.co.uk/research/the-future-of-dc-pensions-enabling-access-to-venture-capital-and-growth-equity/

Beyond pension funds, Solvency II was highlighted as a barrier that limited the insurance industry from investing in VC, due to the high capital requirements associated with investment in unlisted equity. With the UK insurance industry holding assets in excess of £1 trillion, it is clear that reform here could unlock sizable investment. The panel understands Labour has been generally supportive of Solvency II reform and is examining the government's most recent proposals.

The role of the British Business Bank in the provision of patient capital and financing for start-ups

Respondents generally felt the British Business Bank (BBB) was a valuable institution, with one describing the BBB and its subsidiary British Patient Capital as 'crucial pillars in the UK's policy support for the UK's VC ecosystem'. However, it was also made clear that there is significant scope for its remit to be more ambitious. Some of the key observations around which there was a degree of consensus were:

- It was felt that the BBB, despite having operational independence, was too exposed to much political interference. Whether or not this was realised, the argument was that this created uncertainty around its future direction and the commitment it was able to represent, limiting the extent to which external investors could factor it into their decision-making – especially given the long time horizons in VC. Roundtable participants specifically described difficulties in engaging with the BBB and with making decisions based on BBB involvement because of worries that political interference would change its priorities.
- British Patient Capital (BPC), the arm of the BBB investing in UK VC, was typically well regarded by respondents, especially its regional focus. It was felt that The Northern Powerhouse investment Fund, Midlands Engine Investment Fund and similar entities show that crowding in other funding is possible. Some felt that there was a lack of flexibility and risk-taking, and some questioned whether BPC should be more focused on highly-innovative and disruptive businesses.
- Others highlighted the potential for the BBB to do more to crowd in pension fund investment alongside its own investment – with the resources of the BBB providing an extra layer of due diligence for funds making investments into asset classes they were less familiar with. For example, by allowing local authorities to deploy their pension funds alongside private capital and BBB funding, based on the successful model of the London Co-Investment Fund.

SECTION 3: **TAX AND INCENTIVES FOR START-UPS AND SCALE-UPS**

There is a strong economic rationale for providing tax incentives for investment in innovative firms and in R&D. Innovation and R&D can generate technological externalities, so that the social returns to such activities exceed the private returns – meaning the private market would tend to underinvest.

Unsurprisingly, therefore, the UK tax system has a number of schemes aimed at incentivising these activities. Respondents to our call for evidence made clear that there are elements of the UK's tax environment that are conducive to entrepreneurial risk-taking and growth, but that there remains considerable room for improvement. A key strength of the UK funding ecosystem is the availability of a range of fiscal incentives helping a variety of smaller, high-growth businesses. In this review we have focused on SEIS/EIS, and R&D tax credits. In future work Labour should review some of the other schemes in this space.

SEIS and EIS schemes
There was a particular focus on the SEIS and EIS schemes. These schemes are aimed at directly incentivising venture capital investments in small and medium-sized businesses and social enterprises in the early stages of growth.

- The Seed Enterprise Investment Scheme (SEIS) offers tax relief to investors when they invest in small and early-stage start-ups up to the value of £100,000.
- The Enterprise Investment Scheme (EIS) is designed to support entrepreneurs to grow their businesses by offering tax relief to individual investors who purchase new shares in firms that are up to seven years old. Under the scheme, businesses can raise up to £5 million a year, and a maximum of £12 million over the company's lifetime.

There was a clear consensus among respondents that these schemes significantly increase investment into start-ups. Some calculations suggest that the SEIS and the EIS have together facilitated nearly £27 billion of investment into 52,000 British start-ups since their inception.[12] And one respondent cited evidence that angel investors regard the EIS and SEIS schemes as vital to support their investment in high risk, growth focused businesses. 85% of angels surveyed said that the schemes enabled them to back earlier-stage, more risky businesses.[13]

International comparisons also support this. In 2017, the European Commission published a report comparing the effectiveness of tax incentives in fostering investment into SMEs and start-ups. It found that "the top three highest scoring tax incentives are, in descending order, the United Kingdom's Seed Enterprise Investment Scheme (SEIS), the United Kingdom's Enterprise Investment Scheme (EIS), and France's "Madelin" tax reductions scheme."[14]

However, there were a number of suggestions for improving both schemes that were made by multiple respondents. Some of these are summarised below.

- *Time horizon* – Many respondents highlighted problems caused by the April 2025 sunset clause around VCT/EIS schemes. While the government has now signalled an intention to extend these,

12 Enterprise Investment Scheme Association. 2022. Written evidence to the Treasury Committee's Tax Reliefs Inquiry. Available from: https://committees.parliament.uk/writtenevidence/111830/pdf/
13 UK Business Angels Association. 2022. The Climate for Angel Investing. Available at https://ukbaa.org.uk/policy-and-research/
14 European Commission. 2017. Effectiveness of tax incentives for venture capital and business angels to foster investment of SMEs and start-ups. Available from: https://taxation-customs.ec.europa.eu/system/files/2017-09/taxation_paper_69_vc-ba.pdf

as VCT/EIS all by design have timeframes longer than three years, the fact that this intention has only recently been signalled and has still not been fully confirmed is far from ideal – a number of respondents pointed to the importance of providing longer-term certainty to investors.

- *Age limits* – Both the EIS and SEIS impose age limits on the companies that are able to seek investment through the schemes. To use the SEIS, it must have been no more than two years since a company first carried out a qualifying trade. Similarly, a company can receive investment under EIS as long as it is within seven years of their first commercial sale (10 years for Knowledge Intensive Companies). These age limits obviously restrict the companies that are able to use the schemes but the impact of this is most significant outside of London and the South East. Evidence from the BVCA and others indicates that companies outside the South East take longer to develop and seek equity finance for significant growth. Government EIS stats continue to underline the disparity in take up of EIS across the regions with 65% of EIS investment being made in London and the South East. While the Government suggested it would extend these in the Autumn Growth Plan, this extension has not yet been clearly defined.
- *Per company limit* – A number of respondents noted that the £150,000 per company limit for SEIS was too low, noting that the limit had not increased since the scheme was introduced in 2012, despite the round sizes of early-stage investments increasing significantly since then. The government has, since our call for evidence closed, increased this to £250,000, but this remains below the level many respondents suggested would be appropriate.
- Some respondents highlighted that EIS relief was not applicable to investment in some regulated fintechs, which they felt was a regulatory oversight and undermined the future growth of one of the UK’s leading tech industries.

R&D tax credits
There was also strong support for the provision of R&D tax credits. One respondent cited econometric evidence by economists at the LSE showing that R&D tax credits have generated significant increases in patenting and R&D, as well as stimulating positive technology spillovers on other firms. That research also showed that the effects were particularly pronounced for smaller firms.

However, many respondents noted that many SMEs find it difficult and time consuming to access some tax incentives. One response noted that they had received numerous reports that R&D Tax Credits had become increasingly hard to access with payments often taking months to come through, resulting in some eligible businesses not applying.

Business rates
Some respondents also highlighted the current business rates regime as a barrier to investment. As business rates are based on the rateable value of relevant premises, and not revenue or profit, they are an immediate cost to early-stage businesses, for whom cashflow is often a top priority. It was also noted that business rates can act as a disincentive to invest in business property, as doing so can push up the rateable value of that property.

SECTION 4:
THE ROLE OF PROCUREMENT

It is clear from responses to the review that procurement can play an important part in supporting innovation. One of the main ways in which the Government can support start-ups and small businesses to gain access to a market is by being an anchor customer of their goods and services at an early stage.

However, evidence suggests that the proportion of public sector procurement spending going to small businesses has decreased since 2016, from 25% to 21% in 2021.[15] Evidence from Tussell for the Entrepreneurs Network also captured the variation across government departments. The Department for Culture, Media and Sport devotes 37% of its budget to small businesses, whilst the Department for Transport devotes just 2%.[16]

Respondents noted similar trends over recent years, including an increase in the proportion of government contracts going to the top 25 firms between 2013 and 2017, from 13 to 18%.[17]

Respondents noted a number of barriers to reversing some of these trends:

- A number of respondents felt that small businesses and start-ups do not get the same access to key decision-makers and contract opportunities as large multinational businesses and incumbents. It was noted that this can be compounded by the fact that large corporates have the resources to run extensive public affairs to build and maintain these relationships, whereas smaller firms are less likely to be able to dedicate consistent resource to these activities.
- Some respondents pointed to the lack of pre-/early market engagement by civil servants involved in procurement as a barrier. Because it resulted in civil servants having a less than full understanding of the full range of innovation in their area, this was seen as disadvantaging small innovative firms, as tenders were more likely to be written in such a way as to lock out the most innovative firms through narrow specifications.
- More broadly, it was highlighted that identifying, understanding, and bidding for government contracts takes resources that many start-ups and smaller businesses do not have. Therefore the more complex procurement processes are, the more disadvantaged such businesses are relative to larger incumbents.

The barriers identified above were also echoed in a survey of founders carried out by the Coalition for a Digital Economy. They found that 78% of founders did not know who to approach with a question about government procurement, whilst 54% of founders surveyed were not confident that civil servants had an understanding of digital trends and emerging technologies.

15 British Chambers of Commerce and Tussell. 2022. SME Procurement Tracker. Available from: https://www.britishchambers.org.uk/media/get/British%20Chambers%20of%20Commerce%20&%20Tussell%20%20-%20SME%20PROCUREMENT%20TRACKER%202022%20-2.pdf
16 Enterprise Nation and The Entrepreneurs Network. 2022. Access all areas: Government. Available from: https://static1.squarespace.com/static/58ed40453a04116f46e8d99b/t/62dacb0deb0e9d590ef044be/1658506012494/Access+all+areas+-+Government.pdf
17 Institute for Government. 2018. Government procurement. Available from: https://www.instituteforgovernment.org.uk/sites/default/files/publications/IfG_procurement_WEB_4.pdf

SECTION 5: **WOMEN AND ETHNIC MINORITY FOUNDERS**

The evidence is clear that both women and ethnic minority founders are being underinvested in relative to other founders:

- 0.24% of all venture funding between 2009 and 2019 went to Black founders, a figure that declined to 0.02% for Black female founders – a sum far lower than the population representation of 3.5% (18% in London).[18]
- At the same time, new businesses are almost three times as likely to be started by men as by women, and less than 5% of venture funding currently goes to female founders. By contrast, all-male teams accounted for 84% of total VC funding in 2020.[19]

It should be noted, however, that some types of business buck these trends. In particular, social enterprises – 47% of which are run by women and 12% of which are led by someone from an ethnic minority, twice as high as the rest of the population. Nevertheless, the broader statistics show that there is significant underinvestment in those people who fall into both of these brackets, which must be addressed both for its own sake, but also because it means we are not maximising the potential of the UK economy. The Rose Review of Female Entrepreneurship found that the UK has lower levels of female entrepreneurship and business ownership than many of our peers, and that if the UK were to achieve the same average share of women entrepreneurs as our 'best-in-class' peers, this could add £200 billion to UK GDP.[20] One respondent to our call for evidence calculated that if entrepreneurship among ethnic minority founders was increased to the average level, this could add a further £15-20 billion to UK GDP.

And it is worth being clear that the disproportionately low amount of VC funding going to women and founders from ethnic minorities is not simply because of a 'supply' or 'pipeline' problem. The success of numerous programmes aimed at ethnically diverse founders over the last two years makes this clear. For example, Google's Black Founders Fund programme backed 30 founders in 2021 with $2 million and 40 founders in 2022 with $4 million who have subsequently gone on to raise over $200 million, generating a significant number of jobs for the UK. Similarly, the latest Investing in Women Code report laid out that in 2021, 34% of VC deals made by code signatories were in companies with at least one female founder, compared to an industry average of 24%.

Related to this, participants at our roundtables highlighted the importance of data gathering – both with reference to women founders and to founders from ethnic minorities. It was pointed out that even measuring the scale of the problem creates momentum for change, as well as informing policy-makers and market participants about the types of issues to be addressed. One respondent highlighted that 'you cannot change what you don't measure'. A few respondents noted also that it was important not just to measure funding allocations to women and founders from ethnic minorities, but also to improve data on the numbers who applied or sought funding, and the numbers who were actually considered and interviewed by funders. This would make it easier to identify the exact nature of the barriers faced.

Founders from ethnic minorities
Participants at our roundtable looking into the barriers faced by founders from ethnic minorities

18 Extend Ventures. 2020. Diversity Beyond Gender. Available from: https://www.extend.vc/reports
19 The Alison Rose Review of Female Entrepreneurship. 2022. Progress Report. Available from: https://ukbaa.org.uk/wp-content/uploads/2022/03/Rose-Review_2022-Update-compressed.pdf
20 The Alison Rose Review of Female Entrepreneurship. 2019. The Alison Rose Review of Female Entrepreneurship. Available from: https://www.gov.uk/government/publications/the-alison-rose-review-of-female-entrepreneurship

talked in particular about the barrier of 'mirrortocracy' at the funding table – the idea that the lack of diversity at senior levels in funders biased investment decisions against founders from ethnic minorities. For example, one participant was clear that they felt they had only got funding from a VC because there was a black champion at that VC. Similarly, as described below, another founder had felt that she needed to hire a white male CEO to raise money.

Erika Brodnock is a co-founder and CEO of KAMI, which offers personalised employment support for families. She serves on the board of the APPG for entrepreneurship and is a co-founder of Extend Ventures.

Her journey in trying to fundraise for her previous start-up between 2012 and 2019 was so challenging that she reached the conclusion she would need to install a white male CEO to ever raise funding. Furthermore, from many conversations she has had, and the research generated through Extend Ventures, it has become clear to her that Black founders seeking investment face an uphill battle.

It was also highlighted by participants that the challenge of raising very early-stage funding is particularly relevant to ethnic minority founders. As noted above, there are limited debt funding options for very early-stage companies, meaning many founders obtain loans secured on their own home. As a result lower home ownership rates amongst some ethnic groups represent a significant barrier to many starting a business. Only 20% and 17% respectively of households in the Black African and Arab ethnic groups own their own home compared to 68% of White British households.[21] Participants highlighted that this was part of the explanation for why Black and mixed ethnic groups have consistently received a disproportionate number of government Start Up Loans.[22]

Some respondents suggested that there should be an Investing in Ethnic Diversity Code, similar to the Investing in Women Code – instituted in response to the 2019 Rose Review. The Investing in Women Code has seen organisations with investment power of nearly £1 trillion sign up, and respondents saw it as an important step in pushing funders to consider their allocation of capital to women founders and women-led teams as well as their broader practices.

Female founders

As with founders from ethnic minorities, respondents to our call for evidence and participants in our roundtable highlighted a mixture of broader structural factors and factors specific to the start-up landscape.

On the structural side, a prominent factor cited for many women was the affordability and availability of childcare. In 2019, the Rose Review found that women are twice as likely as men to mention family responsibilities as a barrier to starting a business. Some respondents to our call for evidence did note that entrepreneurship can offer greater flexibility around childcare, but in the main the shortage of affordable childcare options was seen as an obstacle to starting and growing a business. While out of scope of this review, the panel is encouraged to see that Labour has set out plans to modernise the childcare system.

Respondents argued that, similar to challenges faced by founders from ethnic minorities, one reason that women founders attract less venture funding is that they are less well represented at senior levels in funders. In support of this, one response noted that angel groups with a higher proportion of women were more likely to back all-female and mixed gender teams. Related to this, a number of respondents highlighted that women founders often had smaller relevant networks – one referring to the feeling that accessing funding relied on access to the 'old boys network'. This reinforces the findings of the Rose Review – that women were less likely than men 'to have access to sponsors, mentors, or professional support networks'.

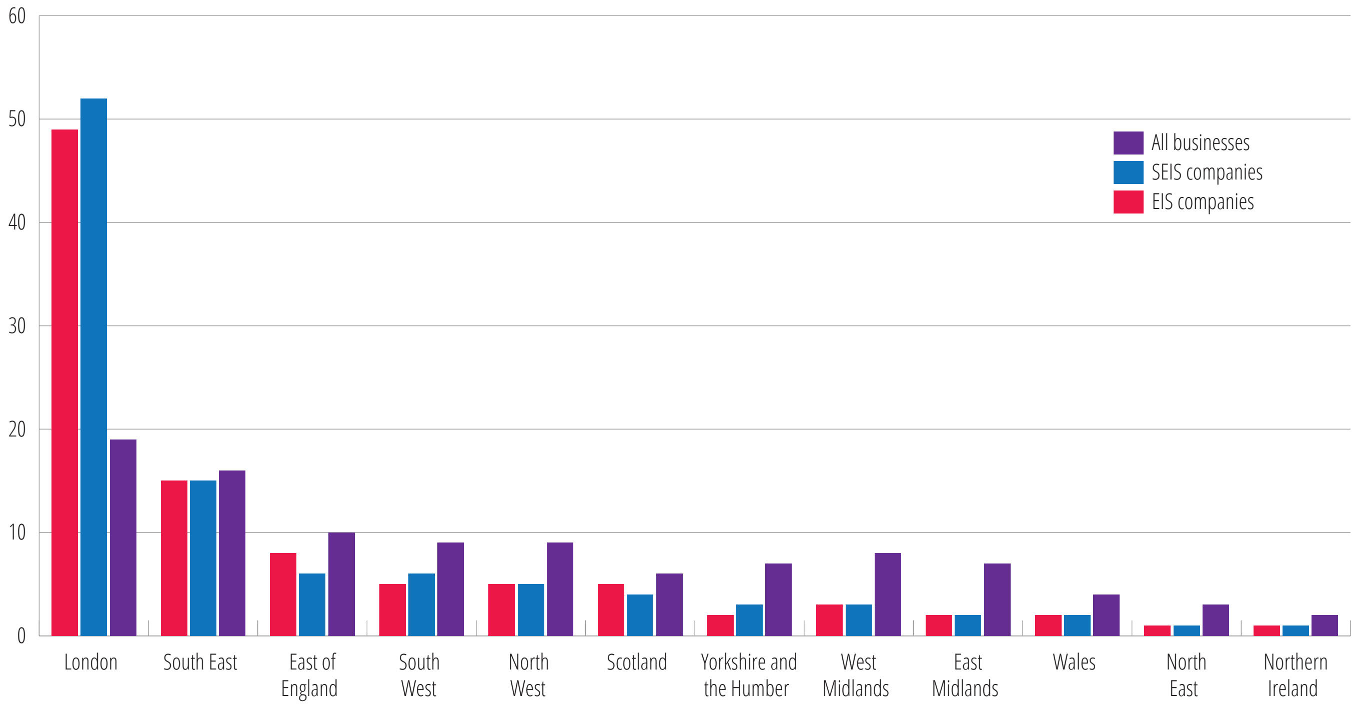
21 Ministry of Housing, Communities and Local Government. 2020. Home Ownership. Available from: https://www.ethnicity-facts-figures.service.gov.uk/housing/owning-and-renting/home-ownership/latest

22 Department for Business, Energy & Industrial Strategy. 2020. Receipt of Start Up Loans. Available from: https://www.ethnicity-facts-figures.service.gov.uk/workforce-and-business/business/access-to-start-up-loans/latest

SECTION 6: **GEOGRAPHIC DISTRIBUTION OF STARTUPS AND SCALE-UPS**

As highlighted by a significant number of respondents, start-ups are disproportionately concentrated in London. The chart below shows that London is the only region where there are more start-ups (as measured by firms benefitting from SEIS and EIS) than we would expect given the wider population of businesses. In the wider South East, the number of start-ups is roughly what we would expect. In every other region, there are fewer start-ups than expected. Such comparisons are imperfect – London is an exceptionally urban region. But the South East's relative strength demonstrates the wider pull of London on start-up activity.

Number of businesses by region (% total)



Sources: Enterprise Scheme Investment Association Written Evidence to Treasury Select Committee, BEIS: Business population estimates for the UK and regions 2021: statistical release (HTML)

Respondents put forward a number of factors to explain this, which are discussed below.

Finance

One of the most prominent factors was access to capital. Respondents highlighted significant difficulties in access to capital outside of London and the South East. This is borne out by the figures - 46% of VC and PE investment in 2021 went to London and the South-East, significantly out of proportion to its population size.[23]

23 British Venture Capital Association. 2022. BVCA Report on Investment Activity 2021. Available at: https://www.bvca.co.uk/Portals/0/Documents/Research/Industry%20Activity/BVCA-RIA-2021.pdf

Respondents pointed out that this was partly due to the simple fact that much of the financial sector is located in London. Recent BBB data shows that investors tend to invest in their local economies, with 82% of equity investment found to be invested within two hour's distance and 61% within one hour's distance. Roundtable participants made clear that the ability to travel, network and meet face-to-face still matters to investors and founders. Combined with the fact that, as of 2019, 80% of UK VC funds were based in the capital[24], it is clear that this presents a significant barrier to increasing the number of startups outside of London and the South East.

A respondent also highlighted that a more fragmented market outside of London can make it more intensive for VCs to identify start-ups, although some VC companies do have more staff working in some regions to overcome this barrier.

Respondents highlighted several proposals to overcome the barriers to finance faced by firms outside London and the South East. The most commonly discussed consideration was how to foster clusters of start-up activity, given some of the concerns highlighted above. A number of respondents and roundtable participants argued that where such clusters developed, this could lead to self-sustaining local or regional ecosystems, which, through having a critical mass of funders (including VCs and angels), mentors, and entrepreneurs and talent, could continue to support the founding and growing of start-ups. Specifically, a critical mass of well-selected and well-presented investment opportunities can make for a more attractive proposition to investors.

One key way of anchoring the development of such clusters is around universities. As discussed further below, UK university research across the country is one of our greatest strengths. And whilst the so-called 'golden triangle' accounts for a disproportionate number of university spinouts, there are important clusters developing in many parts of the UK – such as the Northern Gritstone alliance of Leeds, Manchester and Sheffield universities. Respondents noted that universities can play an important role as a finance hub for innovative firms and investors, even beyond their direct role in spawning start-ups. It was also noted that this role could be amplified where universities nearby to each other work together – sharing their networks and expertise.

Respondents also argued that public sources of funding, and the bodies that govern those, could do more to drive growth and investment in start-ups across all regions. For example, the BBB's various Nations and Regions Investment Funds were seen as a positive development, although they are not fully rolled out, but the program as a whole was also still regarded as overly centralised. One suggestion made by a number of respondents was that they could be tasked with working more closely with local institutions, such as local government pension funds. It was also suggested that the BBB's regional mandate could be strengthened by providing greater certainty of the BBB's long-term commitment to an area, which would help crowd in private investment and mobilise local players.

Infrastructure

Firms rely on physical and digital infrastructure to grow – reliable transport links both within and between clusters, sufficient nearby houses for employees, and access to digital infrastructure such as fast and reliable broadband. Respondents highlighted that the quality and reliability of key infrastructure is often poorer in regions outside London and the South East.

Infrastructure is beyond the scope of this review but we welcome Labour's commitment to improving infrastructure across the country, including building HS2 and Northern Powerhouse Rail in full.

Devolution

Clusters of innovative firms rely on a partnership between business and government. Several respondents noted the lack of regional government in the UK relative to comparable nations. Respondents suggested this can make it harder for policy makers to tap into the unique strengths of different communities, or identify and overcome local barriers to growth.

Again, devolution is out of scope of this review, but we note with interest the proposals that former prime minister Gordon Brown has made in his review on the future of the United Kingdom.

24 Beauhurst. 2019. Where are the UK's VCs located and where are they investing? Available at: https://www.beauhurst.com/blog/where-are-the-uks-vcs-located-and-where-are-they-investing/

SECTION 7: **UNIVERSITIES AND SPINOUTS**

As mentioned above, one of the UK's undoubted strengths is its universities and the research undertaken in them. The 2021 Research Excellence Framework found that 84% of UK university research was either 'world-leading' or 'internationally excellent'[25]. And university spinouts, which commercialise this innovation, can directly drive up economic growth and productivity, as well as doing so indirectly through the spillovers from innovation they create, by helping to seed new markets, and pushing forward the entrepreneurial dynamism of a local cluster or industry.

Unsurprisingly, given the quality of our universities, UK spinouts are already making a significant contribution to the UK economy. In 2020-21, firms that emerged from universities employed nearly 100,000 people and attracted more than £7 billion of external investment.[26] And the direction of travel is a positive one – 2021 was a record year for investment in UK spinouts of £2.5 billion, a 69% increase on the previous record set in 2020. The box below highlights one of the most successful spinouts from a UK university in recent years, Oxford Nanopore – an example of the potential that can be harnessed by commercialising university research.

Oxford Nanopore Technologies develops a range of portable DNA and RNA sequencing devices, with their most notable product used for COVID-19 testing. They employ over 800 people, mainly highly-skilled science and engineering graduates and collaborate extensively with universities and scientific bodies, in both fundamental and translational research.

Since spinning out from the University of Oxford in 2005, they have raised over £850 million in equity funding, have floated successfully on the London Stock Exchange in 2021 and Oxford Nanopore Technologies now sponsors fundamental research at a number of UK universities including the University of Oxford, the University of Cambridge, Imperial College, London, King's College, London, University of Nottingham, University of York, University of Southampton, University of Leicester and the Earlham Institute.

However, many respondents suggested that the potential existed in universities for the UK to be doing even better – some made the argument that a smaller proportion of UK spinouts become unicorns than in the United States. Even on a simple measure of the number of spinouts built on university research, our leading universities appear to be underperforming. Figures from Spinouts UK showed that the UK had produced 567 spinouts in the decade up to 2017. The University of Oxford, the best-performing university in that data, had produced 62 spinouts over those 10 years. This compared to 32 spinouts from Stanford in California in the single year preceding that. It is clear that significant progress has been made since then, but such figures indicate the likely scope for further improvement.

25 Research Excellence Framework. 2022. New evidence highlights world-leading quality of university research. Available at: https://ref.ac.uk/guidance-and-criteria-on-submissions/news/new-evidence-highlights-world-leading-quality-of-uk-university-research/

26 FE News Editor. 2022. Universities call on government to back world-leading UK research and innovation ahead of the Autumn Statement. Available from: https://www.fenews.co.uk/education/universities-call-on-government-to-back-world-leading-uk-research-and-innovation-ahead-of-autumn-statement/

How can we ensure even more successful commercialisation of UK university research?

A number of respondents had thought deeply about this question, given the innovative potential that could be realised. However, there were two topics that were most consistently brought up by respondents and roundtable participants, and these are discussed below. More broadly, a number of respondents felt that there was scope for universities to be more culturally and institutionally oriented towards the commercialisation of research – for example in being more flexible in the career path of academics wishing to lead spinouts.

Equity stakes and spin-out agreements
The most common point of discussion was the agreements that spinouts enter into with the universities at which they are founded. It was highlighted that a combination of risk averse university approaches, combined with the information asymmetry faced by founders during negotiations – as a result of the lack of data on spinout deals – was leading to a status quo where universities are taking equity stakes that are bigger than might be optimal. The argument consistently made was that if universities demand too large a stake in spinouts, this hampers spinouts subsequent ability to attract VC funding.

And data shows UK universities tend to take higher equity stakes than universities in other countries. According to Spinout.fyi, a database set up to counter the lack of information in this area, UK universities on average required 2.7 times more equity than European universities, and more than three times more than US universities.

On the other hand, the quantitative evidence on the relationship between university equity stake and subsequent success of a spinout is inconclusive.[27] And it is clear that UK universities' approach on this front is neither uniform nor static. Many universities offer a range of approaches – that take a higher equity stake where the university has provided or offered greater levels of support, and a lower stake where a lower level of support has been provided or offered. Furthermore, many universities 'have relatively recently reviewed their spinout-related policies and approaches or are about to do so'.[28]

Technology Transfer Offices (TTOs)
In responses to our call for evidence and in conversations at roundtables, there was also discussion about the role of TTOs in fostering the commercialisation of university research. One of the consistent comments respondents made was that there is significant variability in the way TTOs operate and their effectiveness. Some are able to add significant value, in smoothing the spinout process and bringing their networks and expertise to the table, whilst others can hinder the process and put off entrepreneurs and investors.

As a result, respondents had mixed views on the optimal role for TTOs. However, there was a clear consensus that TTO's would be more valuable if they were not simply siloed by institution. One route to improve the service they offer could therefore be to work on greater standardisation across TTOs – in terms of terms and conditions, and consistency of speed of response. Another suggestion was that facilitating greater coordination and collaboration between TTOs at different universities could have significant benefits. For example, if particular TTOs had expertise in particular technologies, collaboration could allow for greater specialisation and sharing of expertise. And if TTOs located near each other could share their networks, this might help build critical masses of investors and entrepreneurs to develop and promote clusters of innovation.

27 Ulrichsen, T.C. Roupakia, Z. and Kelleher, L. 2022. Busting myths and moving forward: the reality of UK university approaches to taking equity in spinouts (Executive Summary). Available from: 2022_UCI_University_spinout_equity_approaches_report_vExecSumm.pdf (cam.ac.uk)
28 Ulrichsen, T.C. Roupakia, Z. and Kelleher, L. 2022. Busting myths and moving forward: the reality of UK university approaches to taking equity in spinouts (Executive Summary). Available from: 2022_UCI_University_spinout_equity_approaches_report_vExecSumm.pdf (cam.ac.uk)

SECTION 8: **UK PUBLIC EQUITY MARKETS**

A consistent observation throughout responses to our call for evidence was that, despite a degree of underperformance in recent years, UK equity markets are among the deepest and most liquid in the world. There are currently over 1,100 companies listed on the London Stock Exchange's Main Market with a capitalisation of around £3 trillion. The role of AIM was also highlighted – since its inception in 1995, AIM has supported over 4,000 companies, which in turn have raised £48 billion at admission and followed this with further fundraising amounting to £84 billion. Over this period, the market has matured with both market cap and the size of admissions growing.

However, there are also some causes for concern that were highlighted by respondents. Between 2015 and 2020, London accounted for only 5% of IPOs globally, and the number of listed companies fell by c. 40% between 2008 and 2020.[29]

There was broad consensus around the benefits of firms being able to access public markets, which offer an important source of funds for businesses seeking capital. It was also highlighted that public markets can also offer an exit for earlier stage investors that are now seeking to redeploy their capital into other private market, growth opportunities. Listed shares also offer investment options for pension funds and retail investors to build up their financial resources for retirement and other long-term needs. These are important reasons to ensure that UK stock markets remain attractive.

Other respondents also highlighted that listing on public markets opens up a diverse and large variety of capital options for businesses.

With regards listing specifically in the UK, a number of respondents suggested that firms listing abroad would be more likely, over time, to move important parts of their business, including headquarters, abroad. For example, one company responding to our call for evidence mentioned that it was considering an IPO in a few years' time, and that if it did so AIM would be its likely market. It felt that if it listed in another country, its shareholders would be from other countries, and that over time its decision-making centre of gravity would leave the UK. On the other hand some respondents noted examples where this hasn't happened, arguing that it isn't always the case that firms listing abroad moved their economic activity abroad over time.

Nevertheless, it was agreed that where firms do move their decision making and centre of gravity abroad, in addition the direct economic impact, there can also be wider implications for UK economic growth – moving managerial and entrepreneurial talent abroad which has spillover effects.

Barriers to listing in UK markets

There was no clear consensus on whether the current listings regime could be significantly improved upon. On the one hand, some respondents felt that Lord Hill's UK Listings Review Report in 21 March, with most of its recommendations subsequently adopted by the FCA, had addressed issues around flexibility. In particular changes to the free float rules (with the minimum requirement reducing from

29 HM Treasury. 2020. UK Listings Review. Available from: https://www.gov.uk/government/publications/uk-listings-review

25% to 10%) and “dual-class” share structures being permitted were seen as positive developments. On the other, some respondents felt that this was insufficient, highlighting that the weighted votes will only apply in limited scenarios and that the dual-class shares will also be limited to five year terms, undermining the role they might play in setting the long term strategic direction.

There was also recognition that deep tech and life sciences companies were increasingly seeking NASDAQ rather than London listings. This, however, was felt to be the result of wider ecosystem factors, such as these industries requiring large sums of capital that AIM is not able to provide. London does not have a large enough community of investors willing to back pre-revenue life science and deep tech companies nor the analyst coverage to drive trading (which was highlighted as something that should be investigated further), resulting in poor liquidity and unfavourable fundraising conditions. There was a sense that UK fund managers prioritised dividend income from mature businesses rather than capital growth from earlier stage businesses.

Some felt that the mandatory issuing of new prospectuses when a company sought to raise significant incremental capital was a potential barrier. Others felt that a lack of experienced directors for high growth tech companies in the UK further inhibits tech firms from listing in the UK. Some respondents highlighted that UK listings carried less litigative risk than US listings, and that this should be better communicated.

SECTION 9: **CONCLUSION**

After an extensive call for evidence, and conversations with more than 120 roundtable participants, we are more sure than ever that the UK has a thriving pool of innovative talent. Already, British founders in every part of the UK are building start-ups that are bringing that innovative potential to bear – creating jobs, increasing productivity, and raising living standards. The UK has world-leading universities, and the research that takes place in them is second to none. And, with London being one of the financial centres of the world, we have the capital and financial infrastructure to back our start-ups and spinouts all the way.

However, we need to do more to ensure that this potential is fully realised. It is no secret that the UK can do better at unlocking institutional capital for investment in high-growth firms, and this review contains a set of recommendations aimed at doing so. Similarly, there can be no doubt that we are not currently making the most of the talents of founders and innovators outside of London, nor of women founders or those from ethnic minorities. Addressing these shortcomings is another focus of the recommendations set out in this review. Closely linked to this are the recommendations that aim at making more of our university research, because doing so can drive forward self-sustaining economic development across the whole of the UK.

We hope that the Labour Party takes forward these recommendations in full, and believe that doing so will help ensure that a future Labour government can achieve its stated mission to improve economic growth, increase productivity, and, ultimately, raise living standards in every part of the UK.

Labour

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