

Representation from Sage to HM Treasury Comprehensive Spending Review 2020

About Sage

Sage is a FTSE 100 tech company and the global market leader for software that provides small and medium businesses (SMEs) with the visibility, flexibility, and efficiency to manage finances, operations, and people. This technology includes integrated accounting, payroll and HR native cloud systems, as well as on-premise and connected cloud.

We are passionate supporters of the UK's small and medium sized business community. Our 2,500 Sage colleagues in the UK support over 1 million SMEs through our products, partners, and advice.

1) Introduction and context

This submission from Sage focuses on the following two key priorities outlined by the Government at the outset of their 2020 Comprehensive Spending Review:

- Strengthening the UK's economic recovery from COVID-19 by prioritising jobs and skills
- Levelling up economic opportunity across all nations and regions of the country by investing in infrastructure, innovation and people – thus closing the gap with our competitors by spreading opportunity, maximising productivity and improving the value add of each hour worked

Our contribution below focuses on the critical role that the adoption of technology by SMEs will play in determining whether Government is able to achieve both these objectives, which we agree are fundamental to the future success of the UK economy.

It outlines how through the Comprehensive Spending Review, the UK Government can act on a once in a generation opportunity to achieve a step change in the use of technology tools by SMEs. By acting now, HM Treasury can help to crack the UK's digital adoption challenge, that to date has seen the UK fall far behind international competitors when it comes to the productivity of UK businesses and the best practice use of tech tools.

At the time of writing this submission (September 2020) the UK economy remains in a precarious position and the effects of the COVID-19 pandemic are still being keenly felt. The UK economy saw encouraging signs of growth in June and July of 8.7% and 6.6%¹ respectively. However, many businesses still face very tough times ahead, with depleted capacity to invest in their recovery or to prepare for the realities of renewed disruption to business operations that lies ahead in the autumn and winter months.

The lessons of past economic crises show us it is the UK's SMEs who provide the economic growth and job creation to power Britain out of financial difficulty. To take the 2008 financial crisis as an example, from 2010 onwards the vast majority of job growth came from SMEs, who accounted for the creation of 73% of new private sector jobs². The UK Government will need to be laser focused on supporting these businesses and prioritise policies to enable their return to growth if the UK is going to rebound quickly from COVID difficulties.

In the background, the long-term challenges experienced by the UK economy are still present. Coming into the pandemic in March 2020, the UK's economy was still experiencing flatlining productivity growth and the UK Government had rightly identified a need to "level-up" economic

¹ <https://www.bbc.co.uk/news/business-54113948>

² Sage & Nesta, 2016, <http://stateofsmallbiz.com/>

prosperity across the UK's nations and regions. For an economy driven by SMEs, who prior to the pandemic accounted for over 99% of the number of businesses and 60% of private sector employment³, these long-term challenges will not be solved unless SMEs are empowered to invest in their capabilities to drive up outputs and performance.

Encouraging a step change in the use of digital technologies by SMEs has the potential to resolve both these challenges. This submission is based on insights from polling that Sage has undertaken with SMEs across the UK over the past 6 months, including a significant poll of UK SME leaders undertaken in September 2020. It identifies that financial incentives to invest in technology has the potential to drive an enterprise-led recovery, create jobs and establish an economy powered by more resilient and productive SMEs over the long-term.

Our comments below outline how vital technology has been to SMEs' response to the crisis so far. It shows that far from being tech-shy, a vast majority of business leaders are clear and confident about the benefits digital adoption can offer them, what they need technology to do for their business and that they do have the skills to adopt it. And importantly, why now offers a once in a generation opportunity to crack the long-term challenge of digital adoption in the UK economy.

Yet despite being cognizant of the benefits, lack of finance is holding SMEs back. Most feel they cannot afford to make the investment due to COVID-19. Through the CSR process, HM Treasury must send a strong and positive signal to help businesses invest in the digital solutions they need with confidence, through a tax incentive or digital voucher scheme that would increase investment in the essential tech tools to make the UK SMEs fit for the future.

2) The importance of tech adoption and COVID impacts

The UK Government has held a long-term ambition to see the UK's SMEs digitise at scale. While the COVID-19 pandemic has undoubtedly thrown serious and significant challenges to UK businesses, the effects of the past six months have created a galvanising moment for SMEs regarding their engagement and attitudes towards technology adoption.

The impacts of COVID-19 have caused a profound shift in the attitudes of SMEs towards technology adoption, which has created a once in a generation opportunity for Government and industry to lead a step change in the adoption of modern, productivity-enhancing technologies by UK businesses.

Coming into the crisis, millions of UK small and mid-sized businesses had failed to adopt digital tools. Just 20% of SMEs say their processes were fully digitised before the pandemic and just half of businesses said that investing in technology was a priority⁴.

Contrast this with during the pandemic, where 73% of businesses have already adopted new technology⁵. It is easy to see why this remarkable shift in approaches to adoption has been seen, with COVID-19 shining a light on the importance of tech adoption to SME resilience, with businesses embracing technology to shift to remote working, find alternative ways to serve customers under lockdown restrictions, identify new routes to market and adapt to changing customer demands.

³ UK Small Business Stats, Business Population Estimates for the UK and Regions in 2018, accessed from [FSB.org.uk](https://www.fsb.org.uk)

⁴ Polling for Sage, 500 decision makers in UK SMEs, fieldwork conducted 26/05/2020 to 27/05/2020

⁵ Polling for Sage, 1011 decision makers in UK SMEs, fieldwork conducted 01/09/20 to 04/09/20

Of the 73% of SMEs who have adopted new technology since the start of the pandemic, the following approaches have been seen:

- 21% have opted for 'quick tech' solutions to respond to immediate needs
- 19% say the tech they have invested in during the pandemic will help them improve processes in the long term
- Just 17% of those businesses had been planning to invest this technology before COVID hit
- 15% have used tech to support significant changes to their business model during the pandemic⁶

Given that just 17% of SMEs were planning to make this tech investment before the pandemic, the activities undertaken by SMEs in the past 6 months and their change in attitudes towards embracing new technology solutions undoubtedly represents a game-changing transformation.

However, this initial shift in engagement with technology by SMEs represents just the beginning of the levels of action SMEs need to take to ensure they are properly equipped to survive the difficult times ahead and raise productivity over the longer-term.

Over two-thirds of SMEs say that they would benefit from further investment in all digital areas⁷. The fact a significant majority of SMEs are now looking to invest more in digital tools represents perhaps a once in a generation opportunity to drive up levels of tech adoption in these businesses that Government cannot afford to let pass by.

This engagement is likely to be time-limited, so this moment must be acted upon to ensure that SMEs are fully equipped to embrace a digital future and put the UK on a path to "build back better".

The UK has long lagged our international competitors when it comes to business productivity. Driving up outputs from UK businesses is a fundamental challenge that needs to be cracked to both level up prosperity across the UK's regions and establish a truly world beating economy. The latest comparisons from the OECD confirm the UK's current lack of international competitiveness, with UK productivity falling well below both the G7 and EU averages⁸.

A lack of tech adoption by UK businesses to date has been a key driver of this problem. For example, the European Union's Digital Economy and Society Index has previously called out the UK for ranking 26th in the EU for use of ERP software, 27th for use of e-invoicing and last among EU countries for RFID⁹.

If Government can act now, the opportunity is there to lock-in the changing attitudes of SMEs towards tech and work with industry to turn this into actual adoption. There is a clear opportunity to create an economy fit for the long-term that is based on digitally enabled, high-growth SMEs, who utilise the latest technology innovations to attract talent, serve customers and adopt productive business models.

3) Benefits of tech adoption

⁶ ibid

⁷ ibid

⁸ <https://data.oecd.org/lprdy/gdp-per-hour-worked.htm>, using latest available data

⁹ Digital Economy and Society Index (DESI) 2018 Country Report United Kingdom, https://ec.europa.eu/information_society/newsroom/image/document/2018-20/uk-desi_2018-country-profile_eng_B4415D06-056C-DDB7-6B695AFEDFB5F952_52236.pdf

The benefits of SMEs adopting new technology go beyond just returning businesses to growth and restoring operations in the short-term. While this is extremely important in the current economic context, it must be acknowledged this will also offer significant long-term gains.

When Sage polled SMEs in September 2020 to get their views on the most significant benefits associated when using digital solutions, a reduced time spent on admin (36%) and increased productivity (36%) were picked out as the two most significant benefits. Overall, 63% of SMEs said that technology significantly improves their business performance¹⁰.

So it follows that the most likely technologies for businesses to be using are software to manage their finances and accounts, software to manage their workforce and people, software to prevent a cyber-attack and communications platforms to support remote working. These are being used regularly on average by 57% of businesses, but 72% say their business would benefit from more investment across all of these¹¹.

When it comes to the levels of investment SMEs feel they need to make to drive optimum business benefits by using tech, typically this is a relatively modest figure in relation to overheads such as wage costs. However, particularly during a period where COVID-19 impacts are greatly constraining business revenues and the ability to invest, for many businesses these amounts will still be viewed as significant.

Ideal levels of investment unsurprisingly vary by business size. When asked in our September 2020 polling to estimate what their business would need to spend on implementing new technology to best position themselves for the recovery from COVID-19, regardless of budget constraints, the median amount broken out by size of SME was as follows¹²:

- Businesses with 1 employee – £5000
- Businesses with 2 to 9 employees – £9000
- Businesses with 10 to 49 employees – £10,000
- Businesses with 50 to 99 employees – £15,000
- Businesses with 100 to 249 employees – £25,000

If SMEs were able to invest the full amount needed to optimise business benefits by using tech, they have identified the following significant benefits listed in the table below. It is important to note that while these benefits will have a positive long-term impact, these are stated if the SME were to make that investment today, in the current context of pandemic-related business impacts.

% who say these schemes would benefit would their business in the next 6 months	Average prediction of benefits
90% expect it would free up hours	17% of hours freed up each week
88% expect extra revenue	+15% increase in monthly revenue
61% expect to increase their workforce	Maintain or increase workforce by 12 people
85% expect increased profits	+14% increase in monthly profits
80% improved insights	79% would have improved insights
53% expect more access to markets	Access to 6 new markets

Source: Polling for Sage, 1011 decision makers in UK SMEs, fieldwork conducted 01/09/20 to 04/09/20

¹⁰ Polling for Sage, 1011 decision makers in UK SMEs, fieldwork conducted 01/09/20 to 04/09/20

¹¹ ibid

¹² ibid

When looking at the types of technologies that will drive these benefits for SMEs, we must acknowledge that these businesses have diverse needs. As such, we would recommend that any policy to incentivise tech adoption (see section 4 and 5) takes a broad-based approach of pushing SMEs to adopt technology that is new to their business. Contrary to perceptions, it is not simply tools such as video conferencing that SMEs are now keen to turn to as they look to put their businesses on a stronger digital footing.

Most SMEs think that they would benefit more from investment in all digital areas – with accountancy, communications and security being seen as most beneficial. To provide further detail on the range of technologies available to SMEs that will enhance their business performance and growth, the table below shows responses to our polling of SMEs when asked to identify technologies that would be beneficial for their business.

Q: How beneficial do you think it would be for your business' performance to invest more in technology in the following areas?	% response (somewhat /very /extremely)¹³
Accountancy software	75%
Communications platforms	74%
Cyber security	70%
Human resources / payroll software	69%
Digital marketing tools	67%
Customer relationship management systems	66%
Business planning / enterprise resource planning systems	66%
E-commerce platforms	65%
Managing the supply chain	64%
Advanced analytics or data capabilities	62%
Internet of Things devices	58%
Automated machinery	52%
Artificial Intelligence	49%

4) Why intervention is needed by Government to support tech adoption

Despite high awareness of the benefits and nearly three quarters of businesses turning to technology to help their business in the pandemic, 56% say that in reality the impact of the crisis has made investment in technology more difficult¹⁴.

In polling undertaken by Sage at the start of September 2020, COVID-19 (36%) and lack of finance (35%) were called out by SMEs as the two biggest barriers to adoption of new technologies¹⁵.

When asked to identify the three biggest barriers currently faced by their business to adopt new technology, SMEs gave the following responses:

¹³ ibid

¹⁴ ibid

¹⁵ ibid

Barrier to tech adoption	% selected ¹⁶
COVID-19 impacts have reduced our ability to invest in new technology	36%
Lack of finances to invest in new tech	35%
Lack the time needed to implement new tech or train staff	23%
The return on investment from adopting new tech is unclear or unconvincing	22%
The market is too complex to know which tools will be most effective	21%
Business lacks the digital skills required to adopt new tech	21%
Use of functioning legacy systems that are hard to integrate with new solutions	17%
None of the above	13%
We had a bad experience digitising in the past	9%

Interestingly, SMEs in our September 2020 poll did not typically cite that a lack of digital skills was preventing their business from adopting new tech tools. Additionally, in general the significant majority expressed confidence they are equipped to navigate and onboard new solutions:¹⁷.

- 75% of SMEs said they know how to effectively use the technology they have invested in, 62% have specialist IT staff
- 72% said they are aware of the technology options out there and how they could benefit their business
- 76% expressed that they are open to changing the way they work to adopt new tech tools in the future
- 71% said their business recognises technology will increase profitability
- 71% of SMEs are confident they have the knowledge to effectively implement accounting software, digital communications platforms, cyber security solutions, human resource and payroll software and digital marketing across their business.
- 77% say their business has access to a fast network and internet connection

While this is very encouraging, the financial constraints currently being felt cannot be ignored and, without action, this is set to be a significant limiting factor that prevents SMEs from making their desired investments in tech. The difficulty of today's business investment environment and other financial pressures mean that as things stand, SMEs currently only plan to invest 41% of the total amount they think they need to make in technology¹⁸.

Therefore, without action, there is a huge risk that the current unprecedented engagement from SMEs around tech adoption is not capitalised on, and tech adoption within the SME economy continues to tick along slowly. Government and tech providers need to consider these constraints now if we are to protect our businesses and enable them to weather the crisis in coming months.

As businesses prepare themselves for at least an autumn and winter of fresh disruption by COVID-19 and SMEs face unpredictable demand and operating conditions, HM Treasury needs to send a signal to businesses now that it recognises how vital technology is.

To achieve the step change in adoption needed, Government support should now be targeted towards alleviating these investment pressures. Through the CSR process, HM Treasury should look

¹⁶ ibid

¹⁷ ibid

¹⁸ ibid

to provide financial incentives to support SMEs to adopt the technologies needed to adapt their business in the short-term and ensure they have established the foundations for long-term growth.

5) Potential policy intervention from HM Treasury

Government offering financial incentives to enable tech adoption has been clearly expressed as a beneficial and useful policy by SMEs. We strongly believe that HM Treasury should look to introduce such measures as part of the Comprehensive Spending Review process.

89% of SMEs believe that if the Government introduced financial incentives to help their business adopt new technology, it would be beneficial for helping them improve their performance¹⁹.

The introduction of financial incentives to spur greater digital adoption was also expressed as a clear favourite by SMEs when compared against other potential measures from Government or industry to enable their implementation of new tech tools.

Q. Which of the following measures do you think would be the most effective in helping your business adopt new technology that will benefit your business? Please select the top three	% selected²⁰
Grants or tax incentives from Government to support new technology adoption	43%
Free trials to try new digital tools or technology	35%
Funding to support employee training in digital skills	30%
Independent advice on technology solutions	25%
More support from tech providers to onboard digital tools and train users	24%
Clearer explanations from technology providers of the benefits of new digital tools to your business	24%
Providing local digital skills programmes	22%
Signposting to training or peer to peer mentoring programmes	15%
Our business does not require support adopting new technology	7%

This should be of little surprise. Current financial incentives from HM Treasury appear significantly out of step with the behaviours and investments that will lead to productivity enhancements in today's economy. For example, Government provides incentives for manufacturing businesses to invest in plant and machinery, but does not incentivise manufacturing businesses to upgrade to modern, cloud-based CRM or supply chain management software that would lead to significant productivity gains.

Government also provides tax credits for the development of new innovative technologies through the R&D tax credit, but then does not incentivise the uptake of mainstream technologies, so the benefits to the wider economy fail to be realised. This might in part explain why the UK is established as a leading nation in terms of global tech innovation, yet often ranks very poorly when it comes to actual tech adoption within businesses (see section 1).

It is important to acknowledge that businesses are not necessarily expecting a handout from Government. Our research shows they are tending to favour measures that incentivise and support

¹⁹ ibid

²⁰ ibid

the right investment activity. When we tested potential solutions for a financial incentive, businesses offered the following opinions in order of most popular to least popular:

Intervention	Further info ²¹
Tax incentives	<ul style="list-style-type: none"> • 37% said tax incentives allowing a reduction of 200% of the value of the adoption of new technologies from their tax bill would be the most effective incentive for their business. • This scheme would allow SMEs to deduct 200% of both the upfront and subscription costs of adopting new technology, and could perhaps be applied for the first 3-5 years that the business uses that technology.
Digital vouchers	<ul style="list-style-type: none"> • 36% said digital vouchers for SMEs that reimburse two-thirds of the cost of adopting technology up to a cap of £5000 per business would be most effective. • This scheme could run in a similar way to the investment vouchers being provided by the Green Homes Grant scheme, which offers a similar incentive for investments in energy efficiency products and services.
Free digital skills training	<ul style="list-style-type: none"> • 16% of SMEs said a scheme where SMEs access free training for their employees to improve digital skills and knowledge of tech tools would be the most effective Government incentive. • This could be perhaps administered on a local level, led by LEPs in partnership with private sector skills providers or by other trusted partners.
Grant funding for tech investment	<ul style="list-style-type: none"> • 11% said digital adoption grants reimbursing SMEs up to £1000 of the costs of adopting new technology would be the most effective policy. • This policy could look to build on the precedent of grant funding being administered via LEPs to enable SMEs make investments in response to COVID-19, some which will already enable greater tech adoption depending on the criteria set by LEPs.

These present just some of the options available to HM Treasury to incentivise digital adoption and on average 1 in 2 SMEs said they would be likely to use a Government scheme that provides financial incentives for their adoption of tech²².

In brief, the above findings show that SMEs are currently indicating a preference towards part-funded options where Government nudges businesses in the right direction, rather than full grant funding or initiatives for training, which in isolation would not overcome the financial hurdles SMEs face. It also shows SMEs leaning towards support that helps them to adopt the financial tools themselves. Financial incentives to adopt technology itself are viewed as having the potential to be twice as effective as a scheme to access free digital training for staff.

It will be critical for any incentive to be delivered in a simple, frictionless manner to SMEs. The economic response to COVID-19 has shown that SMEs are hugely responsive to schemes that are easy to understand and straightforward to access. Timing is also vitally important, with SMEs needing this support now. Digital adoption among SMEs has been a challenge that Government has grappled with for several years, and it has arguably never been more important due to the critical role this can play in enabling more businesses to adapt to the current economic challenges.

Levels of business engagement with technology and a desire to adopt new digital tools has seen a significant transformation over the past months. If HM Treasury can act now through the

²¹ ibid

²² ibid

Comprehensive Spending Review, financial incentives for tech adoption have the potential to act as a crucial piece of the puzzle to galvanise businesses to lock in their engagement and adopt tools that will help build resiliency and raise business performance for the months and years ahead.