

# Covid-19 Impact on Innovative SMEs

This article provides an analysis of the impact of Covid-19 upon innovative SMEs and recommendations to support their recovery and growth.

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## Executive Summary

### Covid-19 Impact

- Covid-19 has had a substantial and negative impact upon most SME businesses
- The biggest impact has been a drop in demand for products and services resulting in significantly lost or reduced revenues
- Many SME product and service trials have been delayed or cancelled by clients
- Limited access to specialist R&D facilities and reduction in laboratory capacity (due to social distancing) has also caused delays to product development
- Early stage finance raises have stalled
- SMEs have responded primarily by cutting costs (including furlough, salary cuts, redundancies and reducing discretionary spend) to match anticipated revenues
- SMEs have sought alternative sources of revenue with 10% of SMEs identifying growth opportunities related to Covid-19
- SME leaders have been through difficult times and their personal resilience will have a profound effect upon business recovery.

### Recommendations

Most SMEs have stabilised and reduced their outgoings to match income. They are now focused on rebuilding their order books although this will be easier in some sectors than others. The following are key areas for support:

- Scenario planning and financial modelling to ensure that SMEs understand and are prepared for a range of different recovery pathways
- Advice to rebuild their business models to support sustainable growth in the short, medium and longer term
- Sales and marketing support to help SMEs develop new sales channels and acquire new customers
- Interventions that unblock early stage investment and give angels confidence to invest in new SMEs
- Greater incentives for large organisations (public and private sector) to restart development projects to trial and demonstrate new products and services.

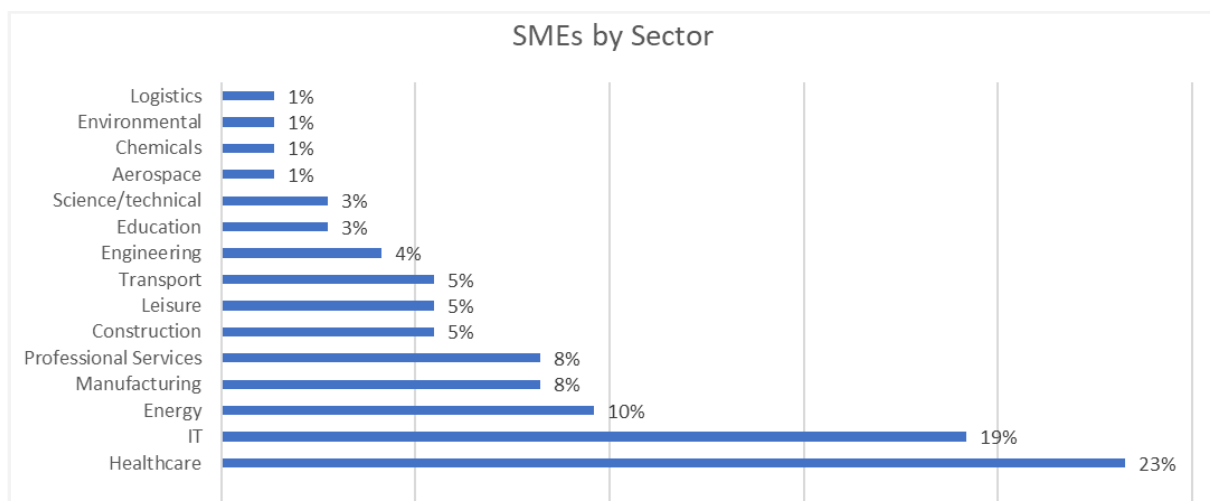
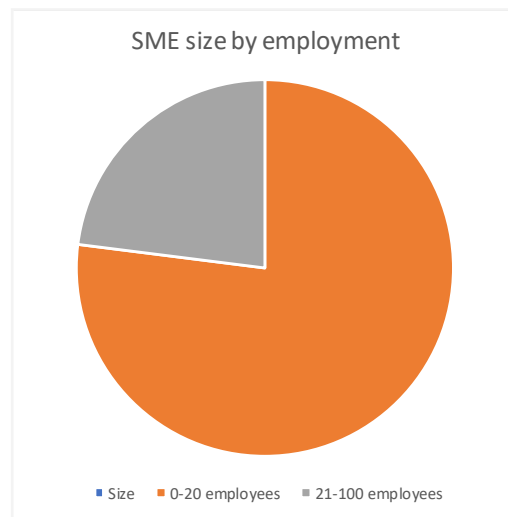
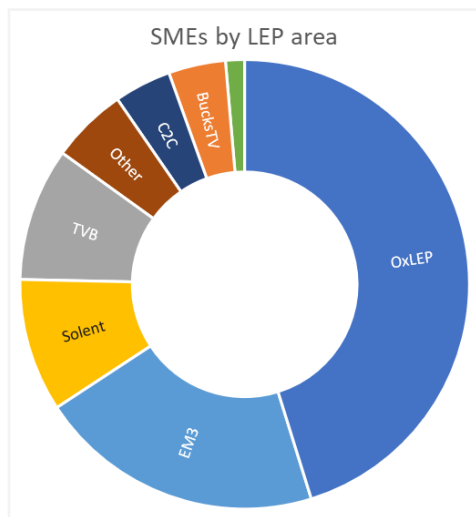
## Introduction

Oxford Innovation is currently working 1-1 with the leaders of >2,000 SMEs. We provide 1-1 business advice, operate 26 Innovation Centres and connect early stage investors to investable SMEs. We are actively supporting these SMEs to recover and rebuild from the impacts of the Covid-19 crisis.

This business intelligence report focuses on the impact of Covid-19 upon innovative SMEs. The analysis is based on conversations between our business advisers and the leaders of 73 SMEs in the South East of England over a 3-month period (14th April 2020 to 9th July 2020).

## The SMEs

The analysis is based on conversations with 73 SMEs in the South East. These SMEs are innovative: they are developing a new product, process or service, and the majority have received grant funding from Innovate UK or are likely to apply for Innovate UK support in future. They are typically small SMEs (0-20 employees), in knowledge-intensive sectors and sell to other businesses (they are not B2C). Twenty-one of the SMEs are equity backed and thirteen of the companies are not yet revenue generating. The makeup of this cohort of 73 SMEs is described below by location, employment size band and sector.



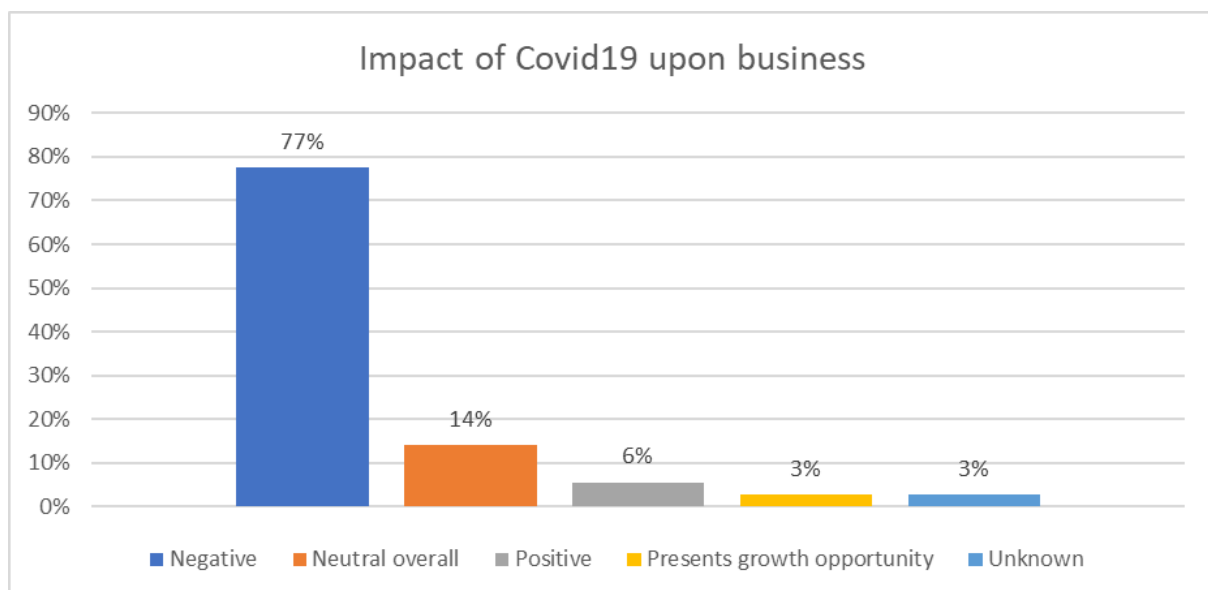
These 73 SMEs are:

- Already growing quickly or have the potential for fast growth
- Are typically developing products or services that are new-to-market innovations
- Are existing or future exporters.

This segment of the SME population will be crucial to the recovery of the UK economy.

## Impact of Covid-19

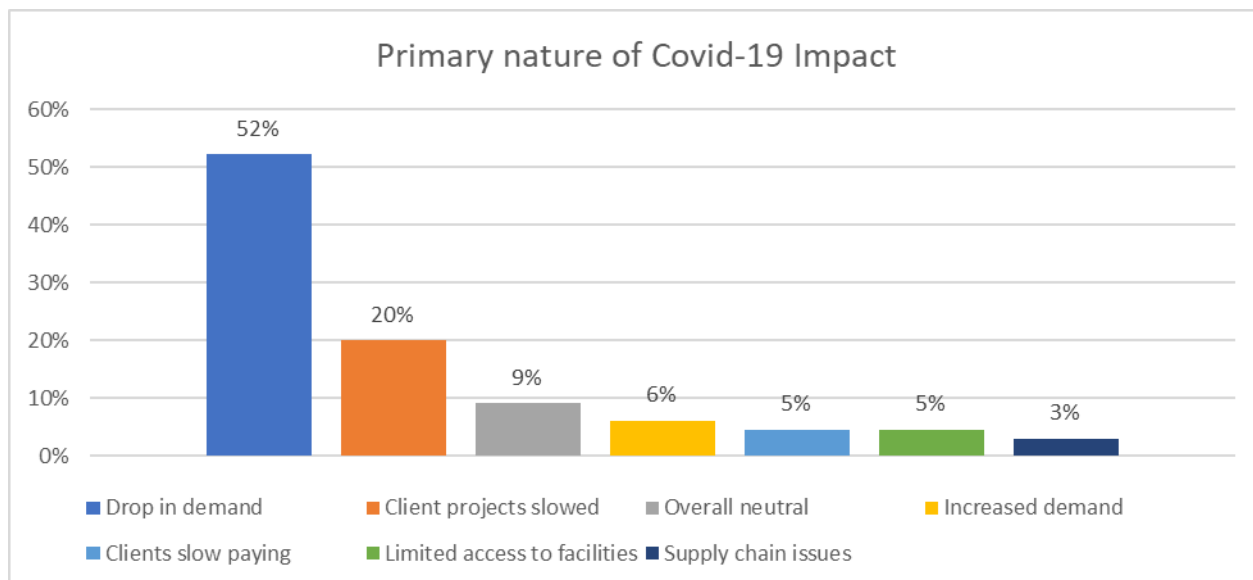
The majority of these SMEs have experienced negative impacts although one or two SMEs have spotted new market opportunities and repositioned their business to take advantage of these.



The biggest negative impact upon these SMEs has been a drop in the demand, and therefore drop in sales, for their products or services. In many cases these SMEs have experienced significant falls in revenue. These falls are not concentrated in one or two sectors. Examples include:

- Drop in monthly income from £100k to £25k (events/marketing company)
- Anticipated annual fall in revenue from £800k to £300k (energy company)
- Anticipated annual fall in revenue from £1.2m to £400k (science/technical company).

This drop in sales has been exacerbated by slow payment from customers, cancellation of orders and supplier delays.



SMEs are also dealing with reduced access to specialist R&D facilities and lower productivity as their labs operate at 50% capacity to comply with social distancing guidelines. Two companies have also delayed new product launches in the hope that trade shows/exhibitions will resume and overseas partnerships will be fully operational. Pre-revenue companies are typically actively involved in development projects and trials with large organisations where they are seeking to demonstrate their product or service, usually as a precursor to securing sales. If they cannot demonstrate their technology they will not be able to secure sales in future. In many cases, clients have cancelled or delayed projects. It is worth highlighting that public sector organisations, including the NHS, are amongst those large organisations that are delaying or cancelling development projects. Taken together, these factors are likely to result in innovative new products, services and processes taking significantly longer to get to market.

Those SMEs reporting increased demand (6%) had seen growth in their existing markets due to Covid-19 or spotted an opportunity to develop a new product meeting new Covid-19 related hygiene requirements.

## Equity-backed businesses

The sample includes 21 equity-backed SMEs of which 11 are not yet generating revenue. Three firms have seen product trials cancelled due to Covid-19, one has run out of cash and is considering selling its IP, and over half have cut their costs or scaled back a planned expansion to reduce their monthly cash burn. Only one company that has fairly recently raised funding reported no changes to their plans.

Fourteen SMEs were seeking to raise investment before Covid-19<sup>1</sup>. The majority say that funding raising activity has stalled: investors are currently very cautious, they are taking a long time to make investment decisions and/or they are withdrawing funding that was pledged earlier. One company cited their £4m funding round (on track to close in April 2020) eventually closed with only £750k as investors withdrew to focus on their existing investments.

<sup>1</sup> This is a mix of SMEs that already have investment and SMEs that are seeking their first round of investment.

Reduction of early stage capital will make it harder for fledging SMEs to scale and become revenue generating businesses. It is also likely to make existing companies more dependent upon grant income, which comes with its own constraints, and deter the formation of new scalable businesses.

## Business response

As might be expected for highly innovative businesses, 15% had spotted new market opportunities created by Covid-19 and responded by focusing their business to serve these new niches. Only three SMEs had responded by developing online sales but this is probably a reflection of the B2B nature of these SMEs and that, for most, social distancing measures have not shut down their sales channels.

Around one-third of these SMEs have made some use of the CJRS<sup>2</sup> scheme and around one-fifth have applied for Government backed loans. The most commonly sought form of Government backed financial support is grant funding, with half of businesses actively seeking out grants.

Finally, it is worth noting that these SME leaders have experienced a very stressful time and had to make difficult decisions involving people and finances. They are experiencing a much higher workload than normal, due to staff members being furloughed, and have had to implement large scale changes in their business to survive. They are still dealing with a very uncertain future and their personal resilience will be a crucial factor in the survival of their business.

## Recommendations

Most SMEs have stabilised and reduced their outgoings to match income. They are now focused on rebuilding their order books although this will be easier in some sectors than others. The following are key areas for support:

- Scenario planning and financial modelling to ensure that SMEs understand, and are prepared for, a range of different recovery pathways
- Advice to rebuild business models that support sustainable growth in the short, medium and longer term
- Sales and marketing support to help SMEs develop new sales channels and acquire new customers
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<sup>2</sup>Corona Virus Job Retention Scheme

**Below are the stories of three SMEs that illustrate the common issues faced by this group of innovative SMEs.**

### Transport company

Early stage company with six employees developing digital solutions for optimising the use of electric vehicles. The company has a live Innovate UK grant to optimise electric charging points in car parks.

Covid-19 has impacted the business in a number of ways:

- A 6-month delay in Innovate UK project caused by a manufacturing partner furloughing staff
- A number of public procurements cancelled
- A number of private customers halting their investments.

In response to reduced revenues, the company has applied and secured a bounce back loan of £50k which should help it survive until the next financial year. Currently the company is focusing on the grant funded activity and is looking to apply for further Innovate UK competitions.

### Biotech company

Early stage biotech company employing six staff that develops antibodies that fight inflammatory diseases. Typically, this type of technology takes ten years to go from concept to product: the company's most advanced product is roughly three years into the development cycle. They have secured a number of Innovate UK grants and also raised private investment.

Covid-19 has impacted the business in a number of ways:

- Laboratory capacity has been reduced by 50% due to the current guidance (which is slowing development)
- External subcontractor delays – one project has paused because the contractor has shut down completely, a second project has slowed significantly. This means that there are delays to the development of the technology.
- Delayed commitment from investors, with feedback they are focussing on shoring up their existing investments.

In response, the company has furloughed one staff member and is hoping to raise additional investment before the end of the year.

### Science/technical services company

Established company with 12 employees that develops innovative sensors, electrical engineering systems and software for monitoring large structures. They have received three Innovate UK grants.

Covid-19 has impacted the business in a number of ways:

- Delays in their clients/partners committing to the next phase of developmental projects and confirming orders for their existing products
- Pre-Covid-19, they were estimating £1.2m turnover for their 20/21 financial year but they are now expecting ca. £400k which would probably result in staff redundancies.

In response, the company is considering how to make best use of the furlough scheme and short-term actions to bring more cash into the business. Without improved cashflow they will be unable to undertake manufacturing products for overseas orders and undertake in-house new product development projects.



## OXFORD INNOVATION

Oxford Innovation has an outstanding track record for over 30 years of success in incubating and accelerating high growth SMEs through the provision of specialist coaching services, our network of Innovation centres, and a well established Investors network.



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