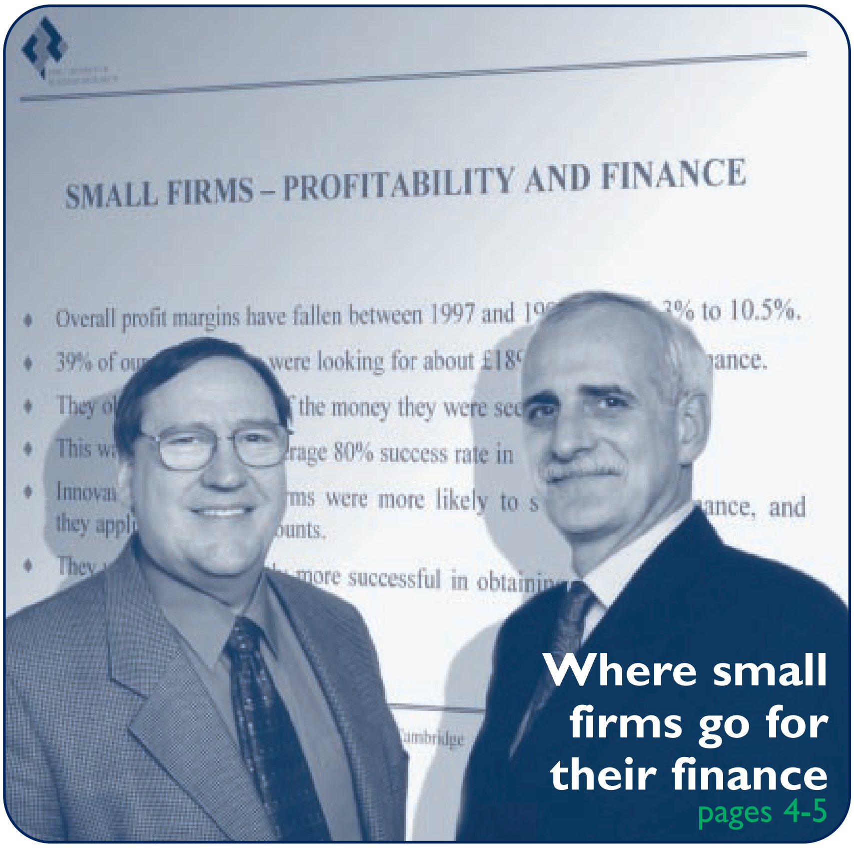
TOP FLOOR

News from the Centre for Business Research, University of Cambridge

Issue 1: Spring 2001

Brother, can you spare £100,000?



Where small firms go for their finance
pages 4-5

CBR

TOP FLOOR

News from the Centre for Business Research, University of Cambridge

Issue 1: Spring 2001

Editor's note

How an international task-force is tackling the crime of **money laundering;** what training can do to help **small firms;** and why bank managers want to improve businesses' **financial skills.** All this – and more – is in the first issue of TOP FLOOR.

TOP FLOOR is a new, free, quarterly newsletter from the Centre for Business Research (CBR) – a forum where staff from across the whole of Cambridge University can collaborate to produce rigorous and intelligent business research. Since it was set up six years ago, receiving core funding from the Economic and Social Research Council, the CBR has worked for, among others, the International Monetary Fund, the Bank of England and the European Commission.

Currently, the CBR is running a project for Employment Secretary David Blunkett which studies the impact of training on small firms' performance. This is vital research, given the well-documented skills shortages in the British workforce, and we report our first results on page four.

On this issue, as on any others featured in TOP FLOOR, the CBR welcomes feedback. Good social science research cannot take place in a vacuum; it is vital to us to test our findings through robust debate with the business community, with fellow academics and policy-makers. We look forward to receiving your responses, and to publishing some of them in future.

The next issue of TOP FLOOR will be out in April, previewing the Corporate Governance conference the CBR is hosting in May (see back page for more details). If you have colleagues who would like to receive that, or future, issues of this newsletter, please let us know.

Rachel Simpson, Editor, Top Floor.
Direct line: (01954) 780873.
E-mail: rachsimp@email.msn.com

E·S·R·C ECONOMIC & SOCIAL RESEARCH COUNCIL

Centre for Business Research
University of Cambridge
Austin Robinson Building
Sidgwick Avenue
Cambridge CB3 9DE

Tel: (01223) 335244
Website: www.cbr.cam.ac.uk

CBR News

Mentioned in dispatches

You may have seen the CBR's work featured in the press recently. In December, the Financial Times devoted a page to a new report by the CBR's Lilach Nachum and David Keeble on the phenomenon of business clusters, in particular the film industry cluster in London's Soho. In early February, our study "Governing Mutuals" – which called for a review of the legislation governing mutual societies – received widespread press attention. "Hopefully, this report… will be given due consideration by the government," said the Independent on Sunday. The Observer concurred: "Ministers should read it."

Moving on up

The CBR is going up in the world. Literally. After six years, our current location in the Department of Applied Economics has become very cramped. So we are delighted to be moving this summer to purpose-built offices on the TOP FLOOR of Cambridge University's business school – the Judge Institute of Management Studies. More details of this move in later issues.

Focus on communication

The excellence of our research was rewarded last year with funding for a second five-year term – at the highest level available – from the Economic and Social Research Council (ESRC). We are now grateful to Abbey National Treasury Services plc (ANTS), the Wholesale Banking division of the Abbey National Group, for sponsoring our communications programme and so helping us take our research to a wider audience. Their sponsorship has made this newsletter possible. It is also enabling us to relaunch our website, at www.cbr.cam.ac.uk Visitors to the site will notice changes in the coming months, and the fact that more of our Working Papers are becoming available online.

Hail and farewell…

… Dr Rahul Dhumale, who was working on Lord Eatwell's programme on international financial regulation. He has recently left the CBR, with our congratulations, to take up a post as Senior Economist with the Federal Reserve Bank of New York.

Taking the profit out of crime

New payment technologies, like smart cards and internet banking, may be good news for the consumer. But worryingly, they could also help boost the international crime of money laundering.

As Kern Alexander warns, in a new CBR report, there are already many ways for criminals to move their money around. The removal of barriers to the free movement of capital, and the sheer speed of computer generated financial transactions, have created new commercial opportunities, he says. Unfortunately, they also make the job of concealing criminal proceeds easier.

Tens of billions of dollars are laundered every year. And the amount is on the increase – particularly from non-drug crimes like insurance fraud, prostitution, arms smuggling and terrorism. (Nor are heads of state exempt from these crimes. At the moment, UK authorities are investigating the role allegedly played by British banks in handling $4 billion said to have been plundered by former Nigerian dictator, the late General Sani Abacha.)

Money laundering damages economies by corrupting officials and governments, skewing currency markets and destabilising financial institutions. And of course it makes crime profitable, encouraging criminal conduct to continue.

New laws

Kern Alexander is a Research Fellow in International Financial Law and Regulation at the CBR. His report tracks the way the international community has developed a network of anti-money laundering laws since 1980, when the Council of Europe first recommended that banks tighten up checks on customer identification.

Money, money, money – the battle against the launderers is far from over.

In 1990 the UN Drug Convention required member countries to criminalise all activities linked with drug-smuggling, including money laundering. The same year, the Basle Committee (of the world's leading banking authorities) drew up its own Statement of Principles on money laundering, encouraging banks to freeze suspect accounts, and to refuse to handle large transactions for unidentifiable customers.

Meanwhile, European Community leaders were growing concerned that drug-smuggling and money laundering could flourish in an integrated European financial system. So they drew up their own Directive, requiring all EU banks (and indeed credit card issuers, bureaux de changes and casinos) to report any suspicious transactions.

Task force

All these initiatives have been taken up and expanded by the Financial Action Task Force, set up by the Group of Seven nations in 1989. It is the only international body dedicated solely to fighting money laundering.

Its forty detailed recommendations for banks in member countries urge them to keep information on the beneficial owners of accounts available for the authorities to inspect. They must also examine ALL complex, large or unusual transactions, and all unusual patterns of transaction, in case they are suspect.

Such procedures, virtually non-existent ten years ago, are now in place in all but one of the FATF's 26 member countries. But its influence extends well beyond its membership. It harnessed enough international pressure in October 1996 to shame Turkey into finally enacting a law criminalising money laundering. And in 1999, FATF was instrumental in forcing Austria to introduce a law ending its anonymous passbook savings accounts.

These are positive steps forward by the international community. But Kern Alexander warns that the battle is not yet over. New money laundering problems resulting from new payment technologies like internet banking could yet jeopardise the gains that have been made.

"The Legalisation of the International Anti-Money Laundering Regime: the Role of the Financial Action Task Force" is published by the CBR as Working Paper 177.

BROTHER, CAN YOU

Where small businesses turn for their finance

Alan Hughes and Andy Cosh report.

In a series of surveys following the fortunes of small and medium-sized enterprises (SMEs) for over a decade, the CBR has built up a wealth of information. It has looked at how these small firms start up in the first place, and which of them survive. It has studied the North-South divide between them, and what distinguishes rural SMEs from those in cities. It has asked entrepreneurs about the problems holding back their growth, and recently studied the first effects on small businesses of introducing the minimum wage.

And each of the five biennial surveys that make up the 'British Enterprise' series has asked particularly about small firms' financial condition, and where they turn when they need external finance.

For small firms, raising significant sums for expansion or capital expenditure can be quite a challenge. In our most recent survey, "British Enterprise in Transition" (launched at our conference late last year), the average amount they were looking for was £100,000.

It is well documented that SMEs rely on internal funds for expansion. So any declines in their profitability are likely to mean increased pressure to seek external finance. And profits have been declining. Between 1997 and 1997, we saw small firms' margins drop overall from an average 11.3 per cent to 10.5 per cent. The only group of firms with improved margins were in the service sector.

How training helps create jobs

A CBR study for Employment Secretary David Blunkett has shown – for the first time – that carrying out training positively helps small firms create jobs. Unveiling the research at the Institute of Economic Affairs last month, David Blunkett said: "The CBR research shows that between 1987 and 1995, small and medium-sized enterprises offering sustained training to their employees fared better in terms of employment growth than those firms which did not train their employees."

He added: "The strong, positive impact of training on growth was closely associated with good human resources practices including quality circles, job rotation or performance-related pay. Importantly, this study demonstrates that the positive relationship between training and performance is not simply a matter of the more successful firms having the capacity to offer training; it concludes that training does provide a positive impetus to employment growth." The CBR is now undertaking further work for the Department for Education and Employment to study the impact of training on other company characteristics, including profitability and productivity, and we'll be reporting our findings in future issues.

"The Relationship between Training and Employment Growth in Small and Medium-Sized Enterprises", by A Cosh, A Hughes and M Weeks is published as CBR Working Paper 188.

SPARE £100,000?

Front cover shows Alan Hughes (left) and Andy Cosh presenting their research at the CBR conference "British Enterprise in Transition". Conference delegates (see images right) found it an enjoyable and stimulating day.

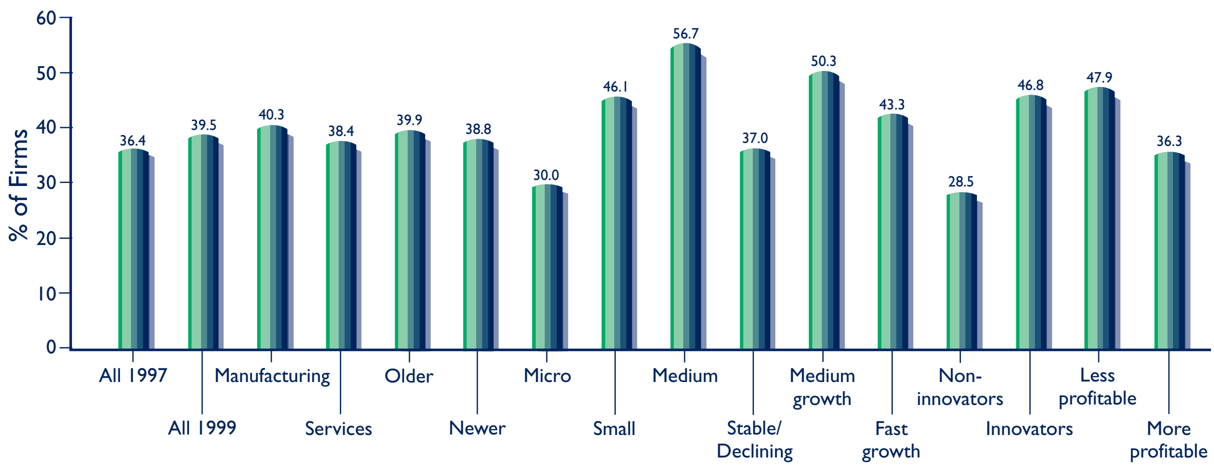
Which companies were looking for finance? Thirty-nine per cent of the sample firms in "British Enterprise in Transition" were together seeking about £189 million. On average, they obtained about 90 per cent of the money they applied for – an improvement on the 80 per cent success rate we measured in 1997. The improved success of raising finance benefited all types of firm.

And where did small firms go for external finance? The overwhelming answer was the banks. For the last few years, we have seen banks declining in importance as a direct source of funding, relative to HP/leasing finance. But in our latest survey, they bounced right back.

Of those small businesses looking for finance, 85 per cent went to their bank. The only other source approached by a significantly large number of firms was HP/leasing finance: 46 per cent of firms went to them. But all other sources of funding declined in the proportion of companies approaching them, compared to our 1997 survey. Venture capital firms, trade customers and private individuals were together approached by less than 10 per cent of our survey firms.

It therefore appears there has been a notable reduction in the diversity of SME funding.

"British Enterprise in Transition", sponsored by the ESRC, is available price £50 from the Publications Secretary, Centre for Business Research. Please make cheques payable to the University of Cambridge.



Percentage of firms seeking finance in the two years to 1999 (unless otherwise stated)

TAKE THE FLOOR... SIR JOHN BANHAM

Probably the first commandment to emerge from the first business school was the injunction not to "reinvent the wheel". Yet this is precisely what seems to be happening, both in business and in public life, time and again.

For instance, most UK taxpayers would expect that shortly after his or her appointment, the new Chairman of a Quango or government taskforce should receive a manual distilling the experience from similar ventures over, say, the last decade. It would tell him or her which were the most successful in terms of outcomes, and which the most disappointing; what steps the new Chairman should be sure to take, and which pitfalls should be avoided at all costs. After all the stakes are, or should be, high; and the value to be added by an effective Chairman should be considerable.

Providing answers

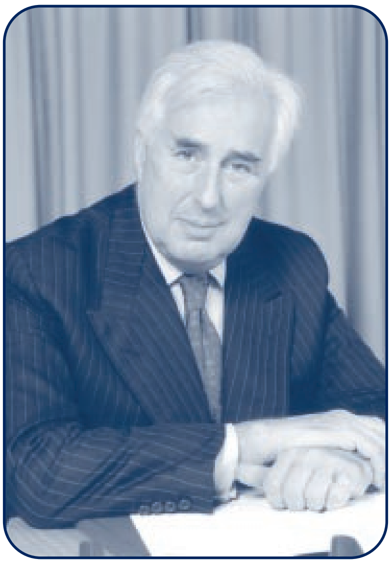
Sadly, the taxpayer's legitimate expectations are normally disappointed. Rather than useful lessons, a new Chairman is likely to receive either nothing at all from his new lords and masters, or voluminous "guidance" drafted by some civil servant who wants to fetter the new board's discretion - but is nowhere to be seen when it all ends in tears.

The same applies to the newly appointed Chairman or Chief Executive of a company. These are lonely jobs and there are very few disinterested but knowledgeable people with whom it is safe to share hopes, fears and questions. After all, the Chairman/Chief Executive is not paid (well) to have fears, but to provide answers which will lead to the company's shares outperforming the FTSE 100 index and market expectations alike.

The Cambridge Effect

TOP FLOOR could help fill this void. To be sure, the key programme themes of the Centre for Business Research (CBR) could not be more relevant in today's volatile - not to say temperamental - financial markets. They include Organisations and Technologies; Organisational Innovation and Change; Corporate Governance and Ownership; and Work and Workers. If through research in these important areas, the leaders of Britain's businesses are able to learn from the hard-won experiences of their peers, all those with a stake in the international competitiveness of the UK economy stand to benefit.

That would indeed be a worthwhile Cambridge Effect.



Sir John Banham is currently Chairman of Whitbread, Kingfisher and ECI Ventures. He was also director of McKinsey and Co before becoming the first Controller of the Audit Commission in 1983 and Director-General of the CBI in 1987. He was the first Chairman of the Local Government Commission for England from 1992-1995.

This page will be open in every issue for a guest contributor to air their views. The editor welcomes submissions.

THE GOLDEN KEY

Unlocking success in small firms

Small businesses in five areas of the country have been benefiting recently from a training programme called the Golden Key Package. Set up to help business managers improve their financial skills, it appears to have done just that.

In a study to discover how effective the course was, the Centre for Business Research found that the training has a small, but positive, impact on performance. Just under a fifth – 18.6 per cent – of firms taking the course thought it had helped them increase their turnover. And just over a fifth – 21.4 per cent – thought it had helped them increase their profits. Meanwhile, 8.4 per cent thought it had helped them create jobs.

Overall, the CBR discovered that after the training, managers made positive changes to the way they run their businesses. They introduced new financial management systems into the company; and made financial cost savings. And it increased their confidence in their own abilities. Over a third of managers thought that after the training they would be better able to cope, even in a recession.

Improving skills

The Golden Key Package was developed by the Small Business Initiative in Norfolk to help small firms improve their financial management skills. The training was introduced after research by Norfolk and Waveney TEC (Training and Enterprise Council) showed that lack of management skills was a factor in 80 per cent of business failures. The Package was first launched in Norfolk in 1994, and then rolled out to Suffolk, Southern Derbyshire, Hereford and Worcestershire and Tees Valley. It is aimed specifically at owner-managers of businesses with an annual turnover of less than £500,000 and with fewer than 25 employees.

By the time of the CBR survey, more than one thousand small business managers had undertaken the training – which is based on case-studies, dealing with relevant topics like pricing, cash flow management, and profit and loss accounts. The training is offered at a subsidised rate because it is sponsored by the high street banks. They also provide an incentive for firms to take part by cutting interest rates or account charges to these businesses.

Economic benefits

The results of the CBR survey, which was carried out for the British Bankers Association, are largely positive. A high number of the users are very satisfied with the training. And so are the bank small business managers who serve the firms that take this training. They suggest that it is associated with a favourable impact on performance risk and assessment.

Overall the CBR report recommends that this training should continue to be supported and promoted more widely, because it benefits all the parties involved: not just the firms who take the training, but also their banks, and the economy as a whole.

"Evaluation of the Golden Key Package component of the Small Business Initiative". A report prepared for the British Bankers Association by the CBR, and the consultants PACEC.

Out and about

- CBR staff have been in demand recently to speak at conferences and events. In September Simon Deakin and John Armour presented their report "Norms in private bankruptcy: the 'London Approach' to the resolution of financial distress" to both the European Association for Law and Economics and the Canadian Law and Economics Association.

- CBR director Alan Hughes went to Downing Street in October to speak at a Treasury seminar on Government Policy and Economic Growth. And in the build up to the recent "Opportunity For All" White Paper, he made invited contributions to seminars on Enterprise Policy chaired by Trade and Industry Secretary Stephen Byers and David Irwin, Head of the Small Business Service.

- Professor Hughes also visited Berlin in November with colleagues Andy Cosh and Paul Guest to present a paper on Managerial discretion and takeover performance at a Corporate Governance workshop. Meanwhile, Lilach Nachum has just returned to the CBR after spending January working as a consultant to the United Nations Conference on Trade and Development. Lilach has been advising on the geography of foreign direct investment for the UNCTAD division on technology, investment and enterprise development.

Robert Maxwell revisited...

With the DTI finally about to publish its official inquiry into the collapse of Robert Maxwell's business empire, the issue of corporate governance is firmly back in the spotlight. Indeed, it hasn't been far from it since the Maxwell scandal along with the collapses of Polly Peck and BCCI prompted the City to reform corporate governance via the Cadbury Report.

In the accepted model of governance, the shareholders of public companies own, while managers manage on their behalf. But this model is now changing significantly. The growth of pension-fund activism raises the question of whose interests, precisely, are being pursued in the name of good governance? Meanwhile, increasing attention is being turned to alternative forms of governance, including the way mutuals and co-operatives are run and the methods by which investors, customers and employees can exercise their collective voice.

All these issues will be debated at a conference this May run by the CBR, together with Cambridge University's Centre for Corporate and Commercial Law, and the European Centre for Corporate Governance at Bournemouth University. Topics will range from shareholder voting and executive pay, to the role of employees in corporate restructurings like the Rover rescue. Speakers will include Roberta Romano from Yale Law School, and CBR assistant director Simon Deakin.

CORPORATE GOVERNANCE

A one-day conference on "Reassessing Ownership and Control". Saturday 19th May 2001. Venue: The Faculty of Law, University of Cambridge. For details and a booking form please contact Simon Deakin, conference co-ordinator, Centre for Business Research, University of Cambridge **Tel:01223 335244 E-mail: sfd20@econ.cam.ac.uk**