BVCA Submission to the Business and Trade Committee inquiry on industrial policy

Industrial Policy: overview

The British Private Equity & Venture Capital Association (BVCA) is the voice of private capital in the UK. The BVCA connects institutional investors, fund managers, companies, advisers and service providers together, with our membership currently comprising over 600 businesses from across the private capital ecosystem. This includes over 250 General Partners, 100 Limited Partners and 200 Professional Services firms. Businesses backed by private equity and venture capital employ over 2.2 million people across the UK, and 90% of businesses invested in by BVCA members are small and medium-sized enterprises. The BVCA welcomes the opportunity to submit evidence to this important inquiry.

In an uncertain economic climate, it is more important than ever that we find ways to boost the UK's economic growth. Research by the BVCA has found that the total amount of capital invested into UK businesses by private equity (PE) and venture capital (VC) (private capital) in 2022 was £27.5bn, with 127 funds raising new capital[1].

UK businesses need to attract this capital. Despite such eye-catching figures, in practice UK businesses face significant challenges accessing the funding they need to grow, and often look overseas for expansion and growth capital. As a result, the UK is losing talent and intellectual property, which puts the brakes on economic growth.

The lack of certainty about industrial strategy can damage investor confidence and risks hindering the drive to increase investment in the UK. In January 2024, 71% of our members surveyed said that UK businesses that they invest in have experienced problems because of political and or policy uncertainty.[2] Almost half of those had decided not to invest in a UK business because of this uncertainty. The BVCA recommends that the Government produce a single source document, such as an Industrial Strategy, which sets out overarching sectoral policy frameworks and relevant timeframes. This would send a clear message to those considering making long-term investments and encourage them to invest in the UK, rather than in businesses based elsewhere.

The UK's strengths and competitive advantages

The UK has long been the hub of the world's financial markets, with a reputation as one of the best places in the world to start and grow a business. Our markets are internationally connected, the London Stock Exchange provides access to global capital and our workforce attracts leaders in their field from across the world. Financial services remain a key driver of the UK economy and we have a globally leading FinTech sector.

All of this makes the UK a centre for private capital and explains why so many of the world's biggest PE houses or newest VC firms want to base themselves here. In 2023, private capital investment supported 12,000 businesses across the UK accounting for 2.2m jobs and 6% of GDP in almost all sectors of the economy[3]. The BVCA wants to help ensure that the UK retains its place at the heart of the global financial ecosystem.

Private capital is a key investor in many of the Chancellor's five key growth strategies, and thus ensuring that the UK remains an attractive home for investors is vital for the growth of these sectors. UK businesses need to attract private capital. And yet, despite the UK having one of the largest pension sectors in the world, UK pension schemes, relative to global peers, currently invest very little in this asset class.

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[1] BVCA Report on Investment Activity 2022 https://www.bvca.co.uk/Research/BVCA-Publications/Details/BVCA-Report-on-Investment-Activity-2022

[2] As part of a programme of work undertaken with Public First, the BVCA carried out an online survey of senior investment professionals within the BVCA membership between 15th-22nd January 2024, receiving responses from over 60 senior decision makers in over 50 investment firms

[3] BVCA Report on Investment Activity 2022 https://www.bvca.co.uk/Research/BVCA-Publications/Details/BVCA-Report-on-Investment-Activity-2022

The private capital industry has continuously achieved stronger returns than the public markets. Investors in private capital have earned up to 41% more than an equivalent public equity investment since 2001[4]. This has informed the Chancellor's calculations that the Mansion House reforms could boost a typical pension by over £1000 per year. Currently, the vast majority of pension capital invested through UK private capital funds comes from overseas, meaning UK pension savers continue to miss out on the industry's strong returns. As well as enhancing retirement prospects for UK workers, increasing UK pensions' investment choices will also result in more funding for UK businesses.

Ensuring UK DC pension schemes can access these funds should result in better retirement outcomes for savers. The BVCA therefore welcomes the Chancellor Mansion House reforms and is leading the Investment Compact of over 100 Venture Capital firms committed to tackling this issue. But regulatory and Government action is needed to ensure that UK investors, particularly pension funds, invest in UK private capital. It is also important to reduce the cost to EU investors of investing their capital in UK funds to ensure that the UK maintains access to these funds.

To continue to attract private capital to the UK, the tax, legal and regulatory frameworks for private capital fund management must be considered, as they are often designed for different kinds of funds, whilst maintaining the high standards that the UK prides itself on. This means modernising fund structure options, capital requirements and reconsidering areas where we have gold plated EU laws and put UK firms at a competitive disadvantage compared to their EU counterparts. The UK should reduce unnecessary regulatory burdens, which will require legislative and regulatory changes, and speed up existing regulatory processes. Government should conduct a cross-cutting review of regulation of innovative technologies, focused on areas where regulatory capacity is holding back innovation and growth, and where legislation has not kept up with technological possibility.

The viability of investment is hampered by the length of time that it can take for businesses to get planning permission for facilities their businesses need, such as factories and labs. Planning delays on housing developments also impact workforce capacity, which limit businesses' ability to grow. One third of the members we surveyed told us that businesses that they'd invested in have experienced problems as a result of planning delays. This has a direct impact on the sectors that the Chancellor has named as his key growth sectors. The BVCA recommends changing planning laws to make it significantly quicker and easier to build both the facilities and the supporting infrastructure that enable investment and job creation in the UK.

Likewise, challenges accessing public infrastructure hamper moves to invest outside of London and the southeast in particular. Improved grid and public transport connections would help support key UK growth sectors. It is also vital that the UK remains a desirable place for people to work and that firms can bring people here. This means considering our personal taxation, regulatory pay rules and our visa schemes. The UK's pool of talent remains a huge draw for companies and individuals and we must protect this position.

We must make sure that the UK is the best place to both start and scale a business. That means protecting our world class universities, having investor support for spinouts, and improving our system for scale-ups. We welcomed the indefinite extension of the rules on full expensing in the Autumn Statement 2023, which encourages UK business to invest and grow. The Autumn Statement announcements on research and development (R&D) tax relief were also a positive step but the tax relief for R&D is still less generous than it was prior to April 2023, and this impacts on innovative SMEs in particular. The Government will need to go further in the amount of support provided if the UK is not to lose out to competitor jurisdictions. This includes generous rates, but also requires HMRC to be adequately resourced to avoid costly delays in processing R&D claims.

Net Zero

Achieving Net Zero is going to require large, long-term investments in both infrastructure and innovation. To find that amount of investment against a backdrop of ailing public finances is the reason why few governments will be able to tackle the climate crisis without the support of PE and VC. Furthermore, private capital funds

[4] BVCA Performance and Public Market Equivalent Report 2022 https://www.bvca.co.uk/Research/BVCA-Publications/Details/Performance-and-Public-Market-Equivalent-Report-2022

are well placed to drive the transition towards Net Zero in areas of the economy that public markets cannot reach, through investment in unlisted SMEs and start-ups working towards Net Zero breakthroughs.

Given that each year approximately 90% of the companies invested in by BVCA members are SMEs, and that SMEs represent 60-70% of industrial emissions, it is essential to support SMEs towards net zero via incentives to drive positive behaviours, clear voluntary reporting standards, and proportionate reporting requirements.[5],[6]

In the same way that a single source Industrial Strategy is a vital signal to businesses, a clear Net Zero blueprint with clear commitments and actions on public investment and policy including clear planning and fiscal arrangements, so that investors can be confident about the long-term investments they make.

Economic Security

The BVCA understands the need to assess the economic, and indeed national, security of the UK and has been involved in a number of Government workstreams and Committee hearings to date. We have continued to engage with the Government on this important topic and have provided feedback on the implementation of the National Security and Investment (NSI) Act based on views we have gathered from our members.

Specifically, the BVCA understands concerns in relation to national security screening. However, based on feedback from our members, we believe that the regime is not as effective as it could be, it is overly burdensome and does not strike the right balance between security and prosperity objectives. Although our overall impression is that the NSI Act is broadly meeting its objectives, a number of “teething” issues remain which are causing uncertainty and delay for investors. In our view there are specific areas where small improvements could help to address these issues. We have recently made representations on these issues to the Joint Committee on the National Security Strategy’s (JCNSS) inquiry into ‘The UK’s economic security’.

We have expressed our concerns that the overly burdensome nature of the regime as it stands risks making the UK a less competitive location for attracting investment, impacting negatively on innovation and growth. Compared with international peers, the number of transactions being caught is higher than the equivalent number in the US, a much larger market. The total was 866 in the full year to 31/3/23[7], which is almost double the number of the 440 filings lodged in the US[8].

There is a lack of flexibility or pragmatism around the nature of private capital investment. In some cases this is leading to unnecessary delays. For example, we know of members that have had to go through very time consuming processes for co-investment and top-up arrangements, despite the underlying firms and individual investors previously having being cleared. This is burdensome, while at the same time unnecessary, as the ownership has not changed.

We therefore continue to recommend that the Government take steps to address these issues and act on this feedback from businesses and investors. This should help improve the regime and make it more effective in achieving the Government’s goals whilst at the same time striking the right balance between security and prosperity objectives.

[5] World Economic Forum January 2023 Why big business must support SMEs for growth and net zero | World Economic Forum (weforum.org)

[6] BVCA Report on Investment Activity 2022 https://www.bvca.co.uk/Research/BVCA-Publications/Details/BVCA-Report-on-Investment-Activity-2022

[7] National Security and Investment Act 2021 annual report 2022-23 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1169054/National_Security_and_Investment_Act_2021_annual_report_2022-23__PDF_.pdf

[8] Treasury Releases CFIUS Annual Report for 2022 https://home.treasury.gov/news/press-releases/jy1663