State of the Nations research series

GROWTH FINANCE FOR THE CREATIVE INDUSTRIES

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with RSA

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- **Developing briefings and submissions** to respond to priority policy issues
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The themes and corresponding Research Leads are:

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GROWTH FINANCE FOR THE CREATIVE INDUSTRIES

State of the Nations research series

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Foreword

A consistent theme in UK government strategies on the creative industries, at least since the 2008 Creative Britain policy paper, is that creative industries firms seeking to grow struggle to raise finance. This problem appears especially marked in parts of the UK far away from London's deep financial markets, where the imperative for growth is even greater. Consistent with this, previous Creative PEC research has found that creative businesses in clusters outside London and the South East of England are more likely to report lack of access to external finance as a barrier to growth.

Yet, despite the great interest in creative industries growth finance shown by policymakers, the quantitative evidence base remains strikingly undeveloped. While reports are regularly available on the patterns of growth finance for, say, UK tech companies, reports on creative industries finance outside specialist areas like film and other project finance remain few and far between. This lack of evidence impedes not only the design of corrective policies but the development of creative industries financial markets themselves, as investors are naturally reluctant to invest in sectors where so little is known about growth finance supply and demand.

In this report, the Creative PEC takes a first step in trying to fill the evidence gap at both the national and sub-national levels. It will soon be accompanied by a second report presenting the findings of our own attempt to collect survey data on access to the finance in the creative industries, in partnership with Creative UK and the survey agency, BDRC. As ever we look forward to hearing your comments.

Professor Hasan Bakhshi,
Director, Creative PEC

Executive summary

The new UK government has committed to supporting the growth of the UK's creative industries. Ensuring that creative businesses with the desire to grow have access to sufficient capital to fund their growth is vital. In this report, we explore demand and supply for growth finance in the creative industries, considering where barriers may exist and highlighting the potential for novel investment products to support creative industries businesses.

Growth finance has multiple definitions. In one sense, any finance can be growth finance if a company uses it to grow. Our approach is to first consider creative organisations' demand for growth finance, and then focus on growth capital, as proxied by supply of venture capital (VC). VC, together with angel investment, is one of the most prominent forms of growth-oriented equity investment. We also consider investors' ability to exit their investments, because availability of profitable exit is an important part of the equity investment process. This approach is narrower than some definitions of growth finance – we adopt it because VC is a significant area for growth which has been poorly evidenced.

The report builds on a limited number of previous research studies exploring how creative industries businesses access finance. Creative businesses typically produce content and services that are intangible in nature and therefore more difficult to value. Previous research (e.g. Fraser and Lomax, 2011) has found that firms in some creative sub-sectors are more likely to be rejected for bank loans and other types of finance and are therefore more likely not to seek capital at all. Data from a Creative Industries Council (CIC) survey in 2017 (CIC, 2017) confirms that access to finance remains a pressing issue, with businesses often identifying it as a major barrier to growth (Siepel et al., 2020). Given the lack of recent creative industries research on this topic, the present report tries to paint a more up-to-date picture, using the frame of demand and supply for capital. It serves as a complement to forthcoming Creative PEC research with Creative UK, which will present the findings of a new survey of creative organisations' experiences accessing finance.

Demand for capital

The demand for capital in an industry is closely linked to its innovation activity. The vast majority of creative businesses engage in some form of innovation (Bird et al., 2020; Gkypali and Roper, 2018). Owners of creative businesses have multi-dimensional motivations and attitudes to growth, with the project-based nature of much creative work and the use of freelancers also giving business owners flexibility to expand and contract in line with demand (Sigurdardottir and Candi, 2019). This means that desire for growth may look different between the creative industries and other sectors.

One way to understand this is to consider how creative businesses identify opportunities for new investment. This report analyses data from the Department for Business and Trade's Business Finance and Investment Decision-making Survey of 1501 firms' investment decisions. The survey found that compared with firms in other sectors, creative industries firms are more likely to identify investment opportunities for R&D, particularly for new products, and less likely to identify potential capital investments in plant, facilities and property.

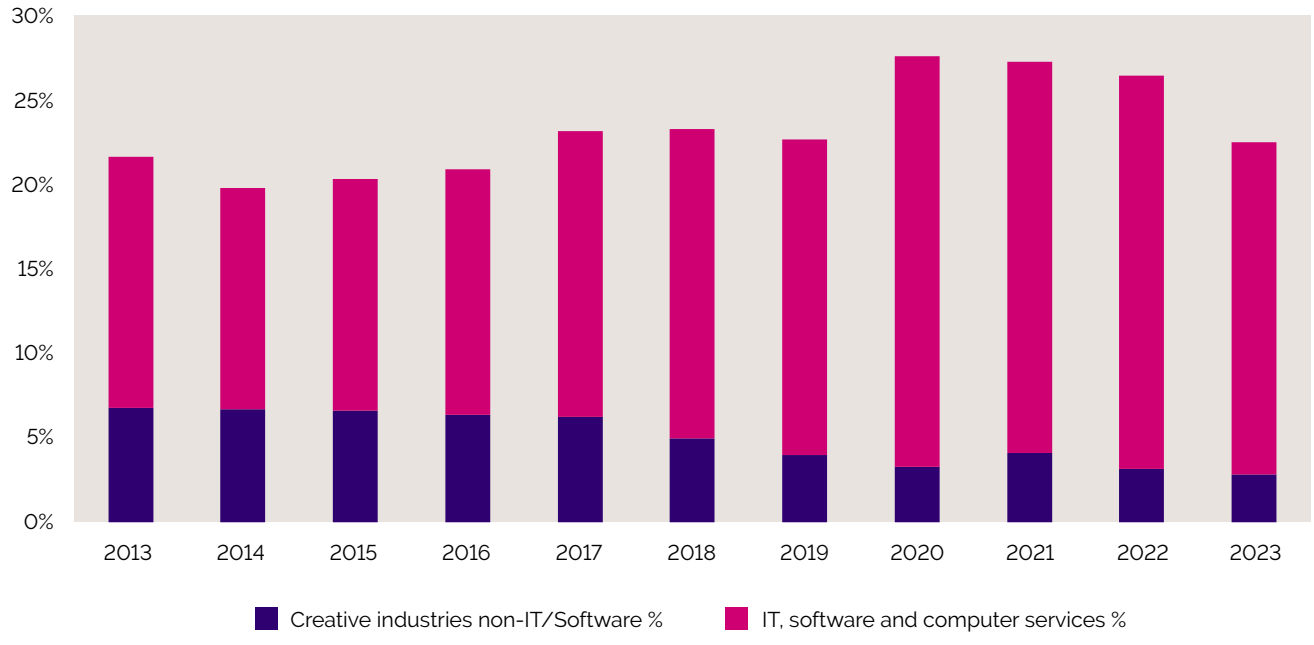
While many creative industries firms say they desire to grow (73% of firms in the CIC survey (CIC, 2017)) and can identify investment opportunities, they require support to become "investment ready". Investment readiness refers to a business's desire to grow, suitability for investment and ability to communicate with potential investors (Mason and Kwok, 2010). Supporting businesses to become investment ready involves a combination of business support and education about funders and what they require.

Another barrier associated with demand for capital relates to creative businesses' perceptions of investors and investors' understanding of the creative industries. If companies feel they are unlikely to be successful in seeking finance, for example, they may decide not to apply. This phenomenon, known as "discouragement", was identified in the creative industries in Fraser and Lomax (2011). This report presents new findings from an analysis of discouragement using the 2017 CIC survey data (CIC, 2017): one key factor associated with discouragement was the perception that financial institutions did not understand creative businesses.

Supply of capital

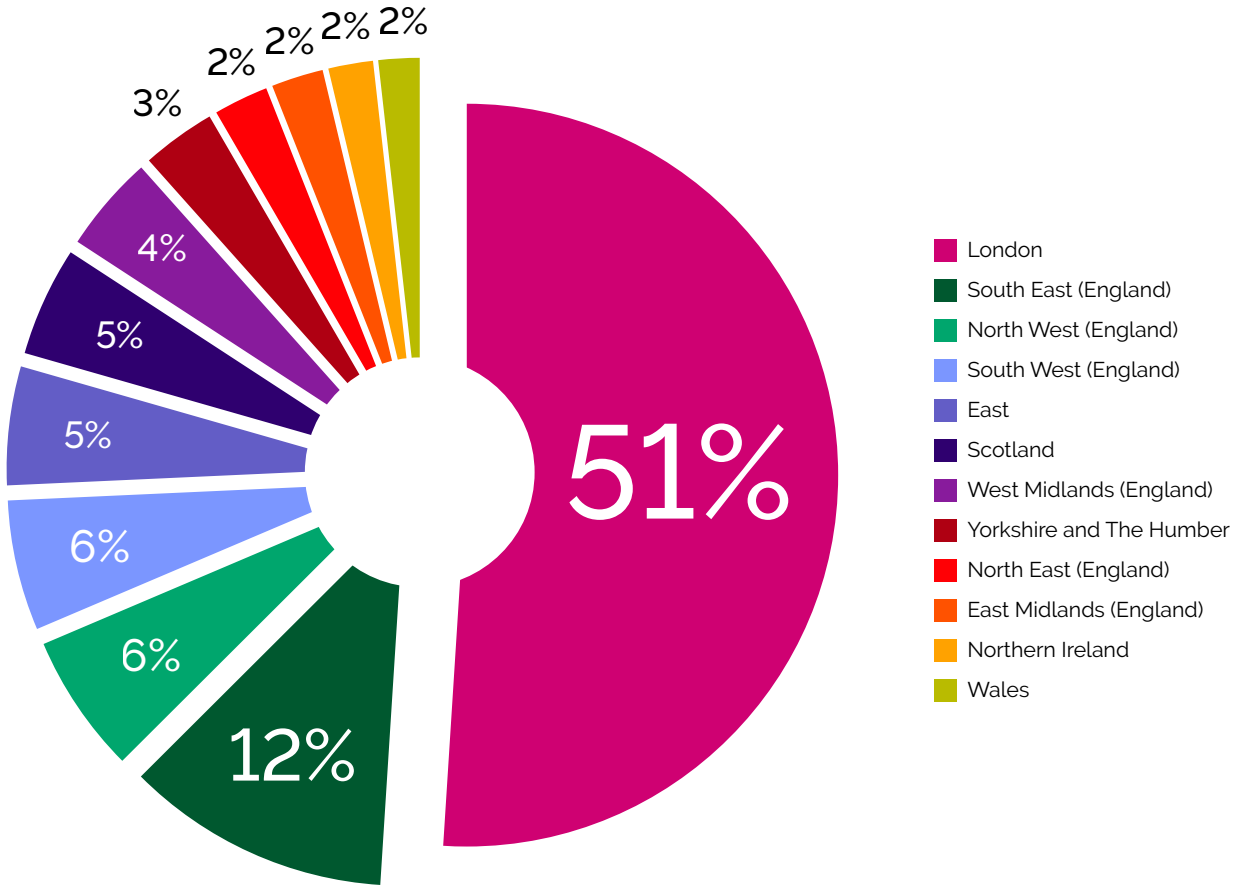
Although many forms of finance can be used for growth, the term growth finance is most widely associated with growth-oriented equity investments such as VC (investments by professional investors) and angel investments (investors who invest their own funds). Using data from the Dealroom platform, we analyse 4540 VC and angel investor deals in creative businesses, mostly from 2013 to 2023. We reveal that 85% of investments in the creative industries are made in IT, software and computer services, with 3% of investments each in advertising and marketing; design; and film, TV, video and radio. According to the Dealroom data, the overall share of (non-IT, software and computer services) investments in creative industries firms, out of all investments made across all sectors, dropped from 7% in 2013 to just 2.5% in 2023, as shown in the figure below.

Creative industries firms as percentage of all businesses receiving investment, 2013–2023



Geographically, this type of investment is heavily concentrated in London and the South East – 63% of all investments were made in these two regions, compared with 11% in the North of England (6% in the North West, 3% in Yorkshire and the Humber, and 2% in the North East), 5% in Scotland, and 2% in Wales and Northern Ireland, as shown in the figure below. These trends have persisted over time, despite regional efforts to narrow the gaps. We also find evidence that investment tends to be directed to creative clusters, with 92% of investments being made in the fifty-five creative clusters identified by the UK government's Department for Culture, Media and Sport (DCMS) (Frontier Economics, 2022) and 57% of all investments going to firms in creative microclusters (small creative clusters at the street, neighbourhood or town level) identified by the Creative PEC (Siepel et al., 2020). Only 5% of investments were made outside of creative clusters and microclusters.

Share of equity investments in the creative industries by region, 2013–2023



Ultimately, these sectoral and geographical inequalities are, at least to some degree, a reflection of wider trends in VC markets. And VC is but one form of growth finance – it is not suited to all firms. Nonetheless, the evidence suggests that further support for creative clusters to help businesses secure growth finance could help build robust, growing creative clusters that can address the UK's regional inequalities.

Exit

Exit opportunities are an important part of the equity investment lifecycle. The report therefore discusses the opportunities for investors to sell their shares or exit from equity investments. Investors typically exit investments by listing a company's shares on the stock market (an initial public offering, or IPO) or by selling the company to another business (an acquisition). There have been concerns, as discussed in the HM Treasury Patient Capital Review (HM Treasury, 2017), that short-term "impatient" capital, driven by investors' desires for quick exits, does not support the UK's long-term interests by creating large, independent UK businesses. In 2021, there were only four IPOs of creative industries businesses on London stock markets, but 130 mergers or acquisitions. Given that acquisition is evidently the dominant means by which investors can exit their investments profitably in the creative industries, the implications of such a high volume of sales of UK businesses bears further consideration.

Future research priorities

This report focuses on growth finance as proxied by equity investment, but also highlights that while VC is one important part of the funding ecosystem, opportunities abound for new and different financial instruments to better support creative industries businesses at the various life points in their development.

Investment is vital for creative businesses to grow, and the aim of building a high-productivity, growing economy necessitates that creative businesses can access appropriate finance to be able to realise their growth ambitions. While these investments may be VC or angel investments, they could equally take the form of new, innovative instruments in debt or equity that are better targeted to meet the specific needs of creative businesses. These include new, intellectual property-backed forms of finance, impact investing and community forms of finance. A broader range of finance options can address the limitations of VC and allow sector- and geography-specific solutions to help creative businesses grow. On this basis, there is a need for strengthening links and understanding between creative industries and providers of financial services.

One key element of building new financial instruments will be collecting better data capturing the flow of capital – public, private and philanthropic – into creative sectors: the lack of available sector- and investment-level data has previously been identified as a barrier to growth in the creative industries. Only by demonstrating in quantitative terms that creative businesses are solid investments, can new investors be attracted to the sector.

This call for more innovation in creative industries finance is timely, given the new UK government's shake-up of the funding infrastructure used to drive growth in the economy and the appetite of combined authorities and devolved nations for initiatives to support creative industries investment initiatives. Introducing new ways for investors' capital to flow to creative businesses may allow the UK to further unlock the growth potential of creative businesses.

Key findings and policy considerations

- **Creative industries firms are more likely to identify investment opportunities, particularly for R&D**, but are also likely to be dissuaded from seeking the capital they require, so need support to become "investment ready".

- **Our analysis suggests that while creative industries receive a substantial share of all early-stage investment**, most of these investments are in IT, software and computer services companies. However, the share of investments in non-IT, software and computer services creative industries firms has dropped from 7% in 2013 to 2.5% in 2023.

- **Investment in the creative industries remains heavily concentrated in London and the South East**, with 63% of investments going to businesses in those regions.

- **Creative businesses in creative clusters and microclusters are much more likely to receive VC investment**, with 95% of investments made in creative clusters and microclusters.

- **Creative businesses are far more likely to be acquired than to grow via an IPO** (listing on a stock market), with only four creative industries IPOs recorded in 2021 versus 130 acquisitions.

- **We therefore argue that there is a need for greater support to help businesses become 'investment ready'**, especially across sectors and regions where equity capital is not prevalent. There are a number of programmes in place that help business to become ready for investment, and these can be strengthened and extended to help drive demand for capital.

- **Exit opportunities are an important part of the equity investment life cycle**. The current low number of IPOs calls for further investigation into how stock market listings of creative businesses can be unlocked.

- **Closer links between creative industries and financial services providers can help to build a strong funding ecosystem for creative businesses**, ensuring that finance providers understand the nature of creative businesses and have access to data and knowledge to make informed decisions.

- **New, innovative financial products can provide alternative forms of growth finance** and can help creative businesses meet their growth needs.

1 Introduction

The sectors making up the creative industries play an increasingly large role in the UK economy (Department for Digital, Culture, Media and Sport [DCMS], 2024) and are vital in driving UK economic growth (DCMS and Creative Industries Council, 2023). In the current, challenging economic environment, where the new UK government seeks to support inclusive growth and address regional inequality, it is increasingly important to ensure creative businesses have access to the resources required to achieve their untapped growth potential. Among the barriers that creative industries businesses face, such as skills, trade and the economy, access to finance regularly rates highly (Siepel et al., 2020).

This report explores the issue of growth finance. Because most creative industries firms engage in some form of innovative activity (Gkypali and Roper, 2018), and innovation in creative sectors is not always visible to funders (Di Novo et al., 2022), innovation finance, growth finance and issues around general access to finance are closely interrelated.

It is important to clarify what we mean by growth finance. Any business can grow; there is no single profile for the characteristics of a firm that grows, and it is difficult to accurately predict which companies will grow (Coad et al., 2013, Coad et al., 2024). Moreover, not all businesses wish to grow – half of small firms express a desire to grow, and only 15% wish to grow by more than 20% in the next year (BVA BDRC, 2024). While keeping in mind the subset of businesses aiming for rapid growth, it is also essential to consider other businesses seeking growth. Our approach in this report is therefore to focus on demand for capital where companies wish to use (any) finance to help grow their business.

Any type of finance can be used to help a business grow, including debt (such as loans from a bank) and equity (including venture capital and private equity). While in our discussions of demand we look at any type of finance, for supply of capital we focus on growth capital, which is characterised by medium to high levels of risk (Rowlands, 2009). For our empirical examination of supply, we focus on early-stage equity investment, namely venture capital (VC). VC is not the only form of growth capital – other forms of equity include angel investment and (equity) crowdfunding, as well as debt and other investments (such as mezzanine finance, which we do not cover) – but because data on these other investment types is limited and VC is the dominant form of early-stage equity investment, it is our focus. We also reflect on the limitations of these forms of investment in the conclusion. Before we explore the issues of demand and supply in detail, we first explore the context for the creative industries and their relationship with finance and innovation.

1.1 Access to growth finance

As a category, the creative industries is broad, embracing – in line with the official definition – nine major sub-sectors and dozens of individual sectors. There is substantial diversity in the business models of sectors that comprise the creative industries, including companies providing creative services (such as advertising and architecture); producing and selling software (IT, software and computer services), producing content (screen sectors, publishing and music); selling physical items (crafts, galleries); selling experiences (performing arts, museums); and many other variations and combinations of these. It is vital to be aware of these distinctions because how a company grows depends substantially on its business model: a growing architecture firm's needs will be very different from the needs of an independent record label, and both are likely to differ from the needs of a company working with immersive experiences. For this reason, we must take care in analysing the creative industries as a category in the context of access to finance issues wherever possible, as the broader category may mask a deeper set of sub-sectoral or business model-level trends.

This need for sector-level specificity has been observed in several previous efforts to explore access to finance for creative industries businesses. A major 2011 study for the UK Department for Business, Innovation and Skills (DBIS) (Fraser and Lomax, 2011) found that creative sectors, including software, publishing, and film and TV, were more likely to be rejected for funding than similar non-creative industries businesses. Businesses in creative sectors were more likely to be "discouraged" (that is, not applying for capital because of a perception that the application would not be successful). But no such effect (either rejection or discouragement) was observed in advertising, architecture or music and performing arts. The report also identified that businesses in creative sectors were more likely to be affected by uncertainty about their prospects and lack of acceptable collateral. These results were striking, indicating that creative businesses face structural issues in accessing finance.

Building on this research, a survey conducted in 2017 for the CIC by BDRC Continental interviewed 575 creative businesses, aiming to better understand issues around growth and barriers to finance. The report found that, in line with the population of firms in general, many firms (approximately 40%) did not consider seeking finance because they did not need it (CIC, 2017). Approximately 53% of respondents had received funding from directors, friends and family. The report concluded that small and medium-sized enterprises in the creative industries had grown or had growth intentions, but companies with growth ambitions were generally younger, less likely to be profitable and less likely to have planned for growth. This indicated that there was potential for growth, but also a need for targeted support to help these businesses grow. Forthcoming research from the Creative PEC and Creative UK will present the results from a 2024 survey of creative organisations using similar questions to the 2017 survey, allowing us to understand how demand for capital has changed since this study.

There is also a geographical dimension to the availability of access to finance. The Creative PEC's Creative Radar data (Siepel et al., 2020) found that creative businesses inside microclusters but outside the largest creative clusters (as identified by DCMS in Frontier Economics, 2022) consistently reported higher growth ambitions but also access to finance as a barrier to their growth, indicating this as a possible cause of persistent regional inequalities in the creative industries (Siepel et al., 2023; Tether, 2019).

Given these inequalities, DCMS launched the Creative Scale Up (CSU) programme, a £4 million investment in three combined authorities (Greater Manchester Combined Authority, West Midlands Combined Authority and West of England Combined Authority) which supported 200 businesses to become ready for investment. The programme, which was a pilot, found that supporting businesses to become more investment ready helped to increase take-up of equity finance and supported growth. It also found that while investors were interested in better understanding investment opportunities within creative sectors, there was a need to support capacity-building activities to encourage investors to consider creative firms as viable investment targets. Research into investor attitudes by the UK Business Angels Association as part of the CSU project found that potential investors were not dissuaded from investing by risk but by lack of information on the sector (UKBAA, 2023).

The insights generated from the pilot led to the development of a programme, the DCMS Create Growth Programme, which is a £17 million investment (followed by another £11 million investment), in twelve regions across England.

1.2 Equity investment in the creative industries

An established body of academic literature highlights the challenges faced by innovative businesses in accessing finance, either equity or debt (Cowling et al., 2018; Lee et al., 2015). Because innovative, growing businesses may not have the collateral required to access debt finance, however, equity investment (where investors buy a share of the ownership of a company) may prove to be an alternative way of funding rapid growth. VC is among the most prominent types of equity investment for small firms. VC is a form of equity investment where a group of investors (venture capitalists) invest funds provided, usually, by institutional investors such as pension funds, into small growing businesses. VC was originally designed to provide innovative businesses (initially in computing and life sciences) with the capital that they needed to grow (Hsu and Kenney, 2005). From its start in Boston in the 1940s and growth in Silicon Valley in the late twentieth century, VC is now a major form of investment worldwide, including in the UK. In 2023, small UK firms received £8.8 billion in early-stage equity investment (British Business Bank, 2024).

Given VC's focus on innovative firms, the creative industries and its subsectors are, in principle, an interesting case because they tend to be highly innovative. Gkypali and Roper (2018), using UK Innovation Survey data, found that firms in the creative industries were more likely to engage in innovation than comparable firms in service sectors and just as likely to engage in R&D as manufacturing firms. These findings have been corroborated in other research: the Creative Radar survey (Siepel et al., 2020) found that 90% of respondents had undertaken some form of innovation (product, process, organisational or marketing) in the past three years, and 67% said that they had undertaken some R&D.[1] Similar findings emerged in the 2017 CIC survey, where 80% of respondents had engaged in innovative activities, compared with 46% of non-creative industries businesses in the SME Finance Monitor, to which the CIC study was benchmarked. In the 2017 CIC survey, 65% of businesses that had acquired new funding had used it to develop new products or services (CIC, 2017).

This innovativeness does not necessarily yield the benefits that might be expected. Di Novo et al. (2022), analysing the 2017 CIC survey, found that innovative activities do not appear to give funders a meaningful signal, either positive or negative, about the quality of the firm (CIC, 2017). This suggests that the sometimes highly symbolic and intangible nature of innovation in the sector could make it difficult for funders to ascertain whether an innovation is likely to be particularly valuable. Di Novo et al. also found that owners of innovative businesses are more likely to rely on injecting their funds into the business rather than seeking external capital. These findings indicate a substantial issue for creative industries firms, identified in Fraser and Lomax (2011) and elsewhere: while they are more likely to be innovative, the nature of the innovation is less observable to investors. And if innovation is less tangible to investors, this may prove to be a barrier to growth for innovative creative industries businesses.

This report therefore addresses these issues, considering the demand for growth capital and the supply of VC investment in recent years. In Chapter 2, it takes a broad view of demand for capital and growth, identifying some unique characteristics of creative industries businesses, as well as challenges around how companies interact with demand. In Chapter 3, it discusses recent trends in VC investment in the creative industries, identifying key factors associated with gaps in sectoral and regional investment. It also highlights structural issues around the nature of exit from VC investments that also have major implications for the UK creative industries. Finally, in Chapter 4, it builds on this analysis to identify some key frontiers for growth finance, highlighting the strengths and limitations of the current model.

2 Demand for capital

2.1 Contextualising access to finance

Effective markets for growth capital require both a supply of capital from funders and demand for capital from high-potential businesses. This report considers both.

In this chapter, we will explore demand for capital by innovative firms. Demand is challenging to observe as it is fundamentally counterfactual: we can observe supply based on the value and count of investments, but there is no equivalent data for demand (as we cannot track how many people considered applying but did not or were rejected by funders). Instead, we must rely on proxies – such as firms' responses to surveys – as indicators of demand. Given that innovation is widespread in the creative industries (as discussed in the introduction), our approach focuses on demand for finance to support growth in general, before looking at issues more specifically related to supply of growth capital in the next chapter.

In this section, we explore demand around four key dimensions: the level at which firms seek finance; the extent to which companies are investment ready; which opportunities are pursued by companies seeking capital; and some policy issues relating to demand.

2.2 Who seeks finance, and what finance do they seek?

While finance is crucial for many businesses, surveys show that most businesses do not seek capital in any given year. For example, SME Finance Monitor data consistently shows that approximately 85% of small and medium-sized enterprises (SMEs) did not apply for finance in the previous year (see BVA BDRC, 2024). This figure appears to be consistent for creative industries firms as well. Data from surveys of creative businesses, such as the Creative PEC's Creative Radar survey in 2020 and CreaTech survey in 2022 (Siepel et al., 2020, 2022), found that 75% and 78% of respondents, respectively, had not sought new capital in the previous year. Given limitations in sample size, these appear to not be statistically distinct from the 85% figure seen for the general population.

Most businesses have straightforward financial needs that can be addressed by common financial products such as overdrafts, business credit cards and loans. Because loans for larger amounts of capital typically are secured on collateral, businesses that are innovative or wish to grow rapidly may find that loans or other conventional debt instruments may not meet their needs. This is mainly because larger debt facilities typically need to be secured against collateral, and for innovative or high-growth firms, historically, the assets of these companies (being largely intangible or reliant on intellectual property) have not been accepted as collateral (see British Business Bank, 2018).

When most businesses in any sector desire funding, they are likely to seek conventional types of funding rather than equity investment. For example, in the 2023 SME Finance Monitor survey, 31% of all firms reported using core forms of finance (including business credit cards, overdrafts, commercial loans and commercial mortgages) and less than 1% reported using equity investment such as venture capital (VC). In the 2017 Creative Industries Council (CIC) survey, 44% of respondents reported using one or more of the core forms of finance (including business credit cards, overdrafts, loans and commercial mortgages). At the time, 7% of respondents had equity investment, with 8% having used it in the past. These figures – both for core finance and use of equity – are higher than the historical trend for the overall SME population, but sample sizes mean that there is likely no statistical difference between the creative industries and firms more broadly.

When businesses do apply for funding, the data suggests that success rates are generally similar to those of the overall population of businesses. In the Creative Radar 2020 data, 84% of respondents who had applied for loans had been successful, which is similar to the national figures (78% acceptance, albeit not directly comparable) from the SME Finance Monitor (BVA BDRC, 2024).

Demand for capital is closely linked to the desire to grow a business. The creative industries are unusual in that many creative business owners are intrinsically motivated not only by desire for profit but also by creativity and independence (Sigurdardottir and Candi, 2019), which may include preferring not to take investments that might dilute their equity (Fulghieri et al., 2020). On this basis, creative firms' attitudes towards growth are different, with businesses aiming to grow steadily over a long period (Creative Industries Federation, 2018) rather than aiming for high growth. Still, there is potentially more volatility in creative firms' growth prospects, particularly given the reliance on freelancers and project-based nature of many creative businesses' work (Sigurdardottir and Candi, 2019).

These figures show that the proportion of businesses willing to seek external investment does not always correspond with subsequent attempts to apply for finance. In the 2017 CIC survey analysis, only 34% of businesses were happy with how their business was funded, and 61% were happy to use external finance to grow the business. However, only 27% had applied for any new finance. This suggests that while there is an appetite for finance, businesses require support to access the capital they need. On this basis, one challenge appears to be supporting companies to become ready to receive investment.

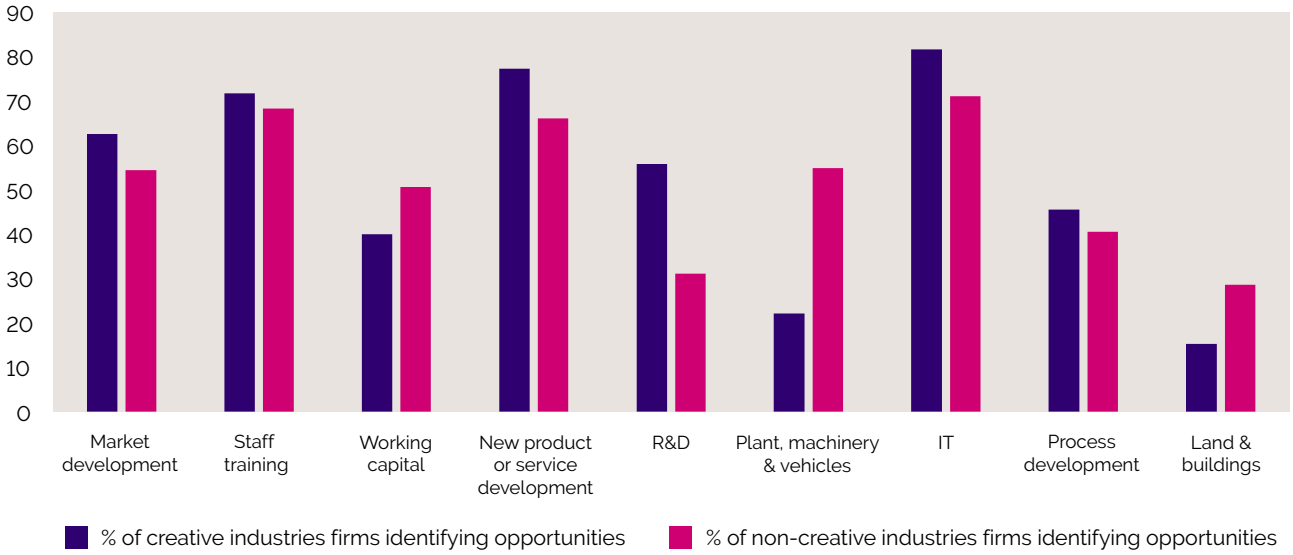
2.3 Investment opportunities and decisions

In research on the demand for growth capital, the acquisition of capital is often seen as the end point of the process, and there is comparatively little evidence on how companies invest external capital to support their growth. In the 2017 CIC survey, 65% of respondents who had received external funding said they had used the capital to develop new products or services, with 62% also citing finance as helping cash flow. Among the companies expecting to use extra finance, 76% anticipated raising funding to help develop new products or services, 65% anticipated taking on new staff, and 62% anticipated using capital to support marketing and business development.

The figures discussed above capture some ways in which finance may be invested, but also demonstrate the challenge of disentangling growth finance from finance used for cash flow. It is therefore helpful to examine how businesses identify specific opportunities for investment and how these might be financed. There is some evidence emerging in this direction, building on a unique UK survey conducted by the Department for Business, Energy and Industrial Strategy of 1501 firms about their investment and financial decision-making in 2018 (see Cowling et al., 2024). Respondents were asked whether they had identified any specific investment opportunities across a range of areas (market development, staff training, working capital, new product development, R&D, plant and machinery, process development, or land and building), and whether they had acted on any opportunities identified. The survey also asked about the types of finance that they had considered and used to act on these investments.

Given the importance of investment for innovation and growth, this data can be used to interrogate how creative industries businesses identify and act on investment opportunities, how they fund these, and the extent to which these are different from other sectors.[2] Figure 2.1 below shows the differences between types of investment opportunities identified by the creative industries versus other sectors.

Figure 2.1: Types of investment opportunities identified by creative industries versus non-creative industries firms

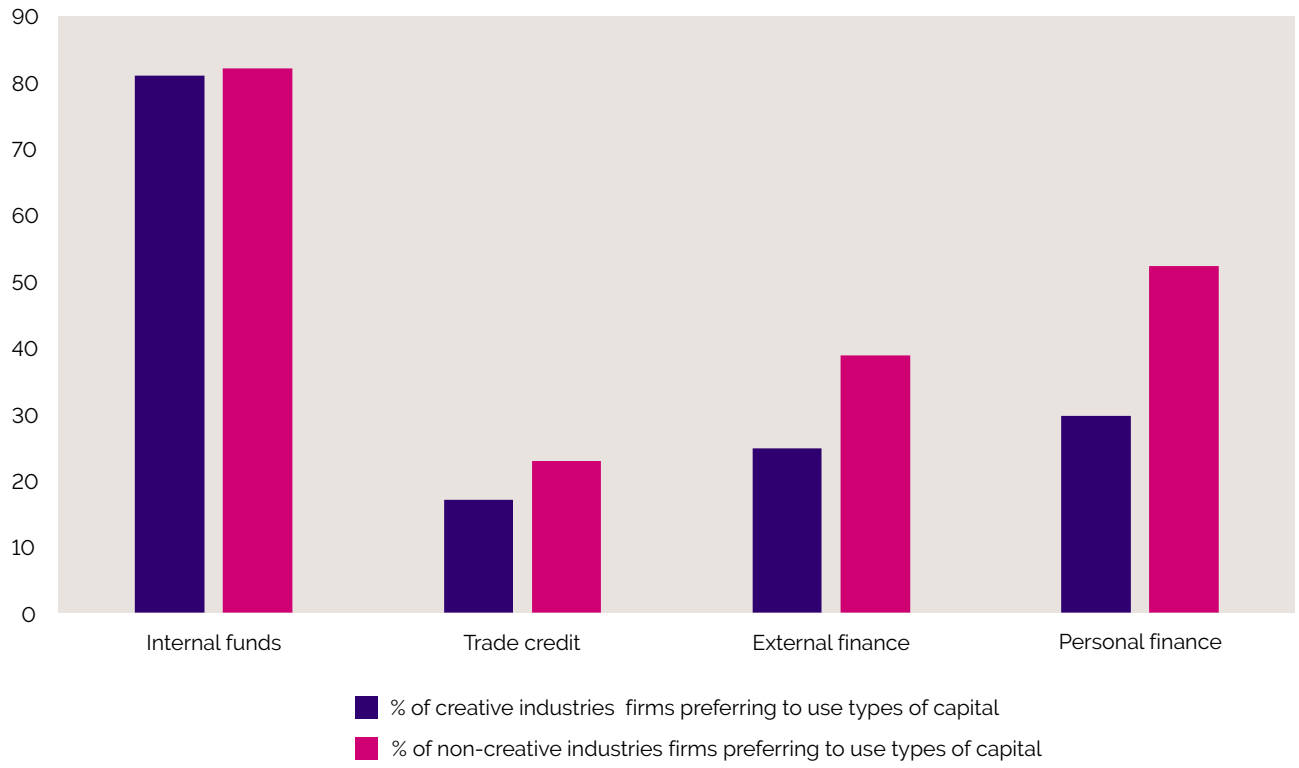


Source: Authors' elaboration from UK DBIS Investment Survey.

Figure 2.1 shows that compared with non-creative firms, creative industries firms are more likely to identify opportunities for investment across several areas – specifically R&D, new product development, and IT and software, all of which are statistically significant at least at the 10% level. Creative firms were less likely to identify investment opportunities for plant and machinery, land and buildings, and working capital, which were statistically significant.

The companies that had identified investment opportunities were asked about which types of capital they would ideally like to use to take advantage of these opportunities. The results, in Figure 2.2 below, show how creative and non-creative industries companies' idealised preferences for capital differ.

Figure 2.2: Companies' preferences on types of capital to use to fund investment opportunities



Source: Authors' elaboration from UK DBIS Investment Survey.

As would be predicted by conventional finance theories, businesses strongly prefer to use internal funds over external finance, but fewer creative industries firms in this survey preferred to use external or personal funds to take advantage of investment opportunities they had previously identified. This is interesting considering findings in previous research that innovative, creative firms were more likely to use personal funds (Di Novo et al., 2022), suggesting that this is not what creative business owners would prefer to do, but what they feel they must do.

Our econometric analysis of this data finds that creative industries firms were more likely to identify both R&D and new product/service development opportunities than other businesses in the sample. Creative firms were no more likely to seek equity or debt finance, but were significantly less likely to use equity or debt finance. Looking at the actual investments, creative businesses were significantly less likely to invest in new products and services, and the use of equity was strongly negatively associated with eventual execution of an identified investment opportunity. However, R&D was an exception to this trend: creative businesses were more likely to invest in R&D projects.

On balance, these findings suggest that while creative industries businesses are successful in identifying opportunities, they only tend to act on those relating to R&D. Given the nature and organisation of R&D in creative sectors (see Bakhshi, 2022; Siepel et al., 2022), it may be expected that the costs associated with R&D projects are comparatively lower than those for other sectors. However, the findings also suggest that valuable investment opportunities for new product or service development may be unrealised, at least partially due to problems in accessing equity growth capital.

2.4 Investment readiness

As discussed above, most businesses are happy to continue their activities without growing substantially or taking on the commitment and demands associated with external finance. Successfully acquiring capital – particularly growth – requires a desire to grow the business, an understanding of what equity investors are looking for, and the willingness to configure a business's governance and operations to meet investors' expectations. Businesses that meet these criteria may be identified as "investment ready". Investment readiness (Mason and Harrison, 2001; Mason and Kwok, 2010) is essential because, in the absence of sufficient demand, markets may fail to work effectively.[3]

Capturing investment readiness is challenging, but some factors that have been used to proxy investment readiness include (CIC, 2017):

- having a desire to chase further growth
- planning to expand the business
- having a formal, written business plan
- producing regular quarterly or monthly accounts and/or maintaining a risk register
- engaging in innovative activities
- exporting
- having a mentor
- having non-executive directors or trustees
- requesting professional advice before seeking external finance.

Companies may be assessed against how many criteria they meet as a proxy for investment readiness. In the 2017 CIC survey, 30% of respondents met eight or more of these criteria (CIC, 2017).

Investment readiness has emerged as a key issue, particularly in creative industries sectors. One of the key insights of the interim evaluation of the Creative Scale Up (CSU) programme (with the full evaluation due to be published shortly) was the importance of providing support for businesses in understanding what seeking investment entails and helping them to decide if equity investment is right for them. However, information and support do not always guarantee that investment barriers will be alleviated. For example, the evaluation of the Creative Industries Clusters Programme (Frontier Economics and BOP Consulting, 2024) found that while many participants in the programme said they benefited from new information about finance, the number of firms identifying finance as a barrier did not change after participating in the programme. This may potentially indicate an issue with the timeframe of the evaluation (that is, companies might have been asked the question but would eventually feel more comfortable seeking finance), but the challenge remains clear that efforts to improve investment readiness remains a key issue.

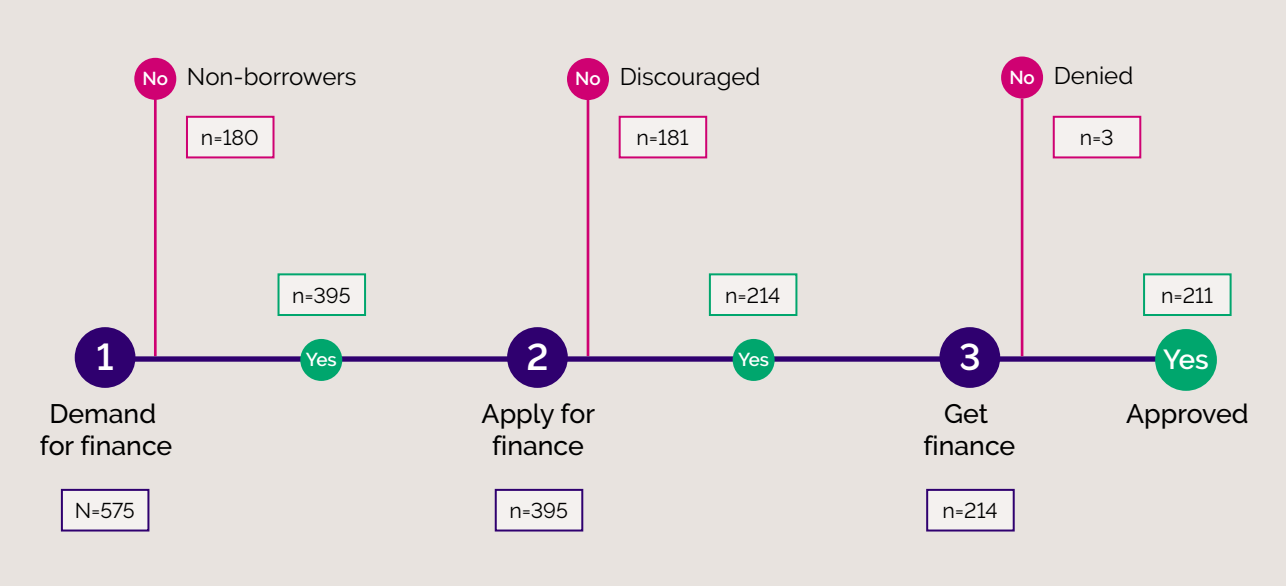
2.5 Discouragement and problems of information

Traditional economic models of supply and demand in finance assume that everyone who has demand will seek capital. This has been challenged by a body of literature that considers discouraged borrowers (or, more broadly, discouraged finance seekers) (Han et al., 2009; Kon and Storey, 2003) and recently "scarred" borrowers who self-exclude from the debt market after a negative experience (Cowling et al., 2021). These occur when businesses with a demand for capital decide not to apply for finance because they feel they would probably be rejected or, for scarred borrowers, due to a previous rejection. Awareness of this phenomenon is vital because financial institutions and investors can only assess the applications they receive, and businesses may assume that finance is too difficult to access. Therefore, the solution to discouragement is providing information to address knowledge imbalances. However, as identified in Cowling and Sclip (2023), discouragement can be a temporary phenomenon that many firms enter into and exit over time.

Discouragement is a legitimate concern in the creative industries. Fraser and Lomax (2011) found evidence of discouragement in software and content businesses (including film/TV, publishing and video games) and pointed to these sectors' reliance on intellectual property (IP) and project-based work as a reason why these companies were discouraged from seeking capital. The extent to which discouragement persists as an issue remains unclear. In the 2017 CIC survey, respondents were asked if they were not applying for capital because they feared rejection, and a limited number of respondents said "yes" (CIC, 2017).

The nature of discouragement in the creative industries may be explored in more detail, however, using a different methodology to identify it.[4] This methodology, based on a framework by Cowling et al. (2016) and highlighted in Figure 3.3, finds a substantial share of companies may meet the definition of discouragement.

Figure 2.3: Discouragement in the 2017 CIC survey



Source: Authors' elaboration based on CIC 2017 and Cowling et al. 2016.

The framework considers companies that have identified a need for finance, which in the 2017 data is 395 respondents, or 69%. Anyone who has identified a need for external finance but has not chosen to apply for finance is then considered to have been discouraged, in line with current academic literature (see Cowling et al., 2016). In this data, 181 respondents, or 31% of the entire sample and 46% of companies with demand, fit this category. Tables 2.1 and 2.2 give further details about the distribution of discouragement and demand.

Table 2.1: Percentage of companies identifying demand and discouragement by employment band

	Number of employees					
	All firms	1 employee	2–5 employees	6–10 employees	10–50 employees	51+ employees
Respondents with demand for capital	69%	53%	66%	79%	89%	91%
Respondents discouraged (of firms with demand)	67%	68%	49%	47%	24%	28%

Source: Authors' elaboration based on CIC 2017.

Table 2.2: Percentage of survey respondents identifying demand and discouragement, by age

	Age of company			
	<2 years	2–5 years	6–9 years	>9 years
Respondents with demand for capital	68%	63%	64%	74%
Respondents discouraged (% of firms with demand)	67%	63%	47%	28%

Source: Authors' elaboration based on CIC 2017.

Tables 2.1 and 2.2 show that while larger companies are more likely to require external capital, the smallest companies are more likely to be discouraged from seeking capital. A similar effect is identified for age: older companies are more likely to require capital, but the youngest companies are more likely to be discouraged from seeking it.

The econometric analysis shows that two of the main factors associated with discouragement are companies' perception that financial institutions do not understand their sector and, to a lesser extent, concern about losing control of the business.[5] Firms with 6–30 employees are most likely to perceive a misunderstanding of creative sectors, which suggests that it is not necessarily an issue of new or young firms being discouraged, but is a distinct phenomenon observed in (comparatively) larger firms that might otherwise be targeting growth capital.

Significantly, these issues around discouragement highlight the importance of addressing information asymmetries around finance. Demand-side interventions, like the Creative Scale UP and DCMS Create Growth Programmes, are trying to address these issues by helping companies become more familiar with the financial process.

This chapter has discussed some key issues around the demand for growth capital from businesses, particularly regarding the limited number of firms suitable for growth capital, the investment opportunities they identify, and issues around investment readiness and information. In the next chapter, we will discuss the trends in supply of growth capital.

Film and content finance

While most creative industries businesses operate in relatively conventional finance frameworks, some parts of the sector are distinct, such as content production. Content-based sectors have several unique features, at least compared with firms in other creative sectors: they are typically organised as projects, with the production of the content having high levels of upfront expense and the value of the IP produced being uncertain until it reaches the market. Moreover, the IP has long-term value, which means that once created, it may continue to generate revenue for years or decades to come.

The unusual nature of film finance has led to many unique approaches to it. Film financing is highly complex and involves many actors within the value chain operating in complex ways, as well as infrastructure such as studios and technology providers (see Franklin, 2024). For example, film productions commonly run through a special purpose vehicle (SPV, also known as a special-purpose entity). This is a firm that is created specifically for the purpose of producing and capturing value from a specific piece of IP. These SPV arrangements allow investors to invest in a specific film and to capture value from that film, while also offering them legal protections, because the SPV is a discrete legal entity.

The UK has long been a centre of this type of finance, and UK investors have a track record of investing in content through investment schemes such as the Enterprise Investment Scheme (and later the Seed Enterprise Investment Scheme) and Venture Capital Trusts, which provide tax breaks for angel investors and retail investors, respectively, by encouraging them to invest in particular businesses that are seen as strategically important. Such investments were widespread throughout the 2000s and early 2010s but were curtailed in the wake of the Patient Capital Review of 2016/2017, which limited the ability of film and other content producers to access these types of funding due to concerns about tax avoidance (Smith, 2024).

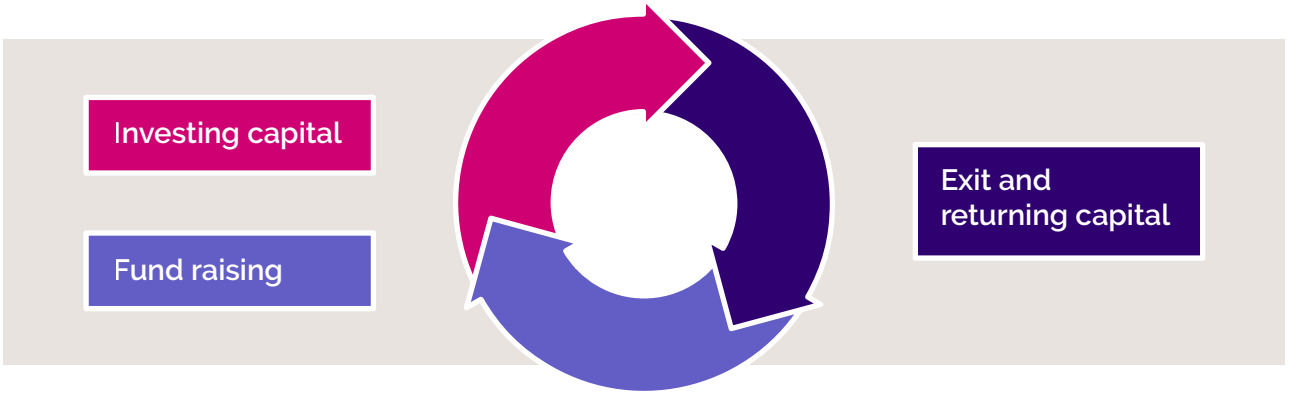
While the UK film and television sector has grown substantially in recent years, largely due to the influx of overseas-based productions being filmed in the UK, there are substantial concerns about the health of the UK independent film sector (Alma Economics, 2022; Keen, 2024). The data around film funding is highly complex and often ineffective in presenting cases for investment (Smith, 2024), and there is a need for better data on the film funding ecosystem. Given the complexities of film finance, we do not explicitly consider film and content finance within the remit of our report. Nevertheless, we highlight the huge importance of the sector and the need for more data and clearer insights into the sector.

3 Supply of equity investment

Equity investment can take many forms, from angel investors (individuals who invest their own money in businesses, often acting as mentors) to venture capital (VC) (professional investment groups who invest in growing businesses) to private equity funds (larger investors who typically buy out the ownership of a company),[6] and ultimately to the listing and trading of shares on a stock market. For this report, we focus on VC and angel investments as proxies for supply. This is a pragmatic decision, based both on the prominence of VC and angel investment as forms of investment, and on the availability of data. Likewise, investment from private equity funds is an important funding source for established firms but is typically less focused on growth-stage firms than VC.

The analytical perspective we will adopt is based on the notion of the "venture capital cycle", as discussed by the academics Paul Gompers and Josh Lerner (Gompers and Lerner, 2004). This idea is based on the dynamics of the VC sector: VC funds raise funding from institutional investors, invest that money in businesses with growth potential, support those businesses to grow and then exit those investments by selling their shares (hopefully generating large returns in the process) – returning money to the institutional investors, who then invest in future VC funds to keep the cycle continuing. Exit, in this context, typically refers to the portfolio company either acquired by another business or listed on a stock exchange, at which point the VC fund can return cash or shares to institutional investors.

Figure 3.1: The venture capital cycle



Source: Authors' elaboration based on Gompers and Lerner (2004).

This concept is important for several reasons: first, it highlights the cyclical nature of investments. If investors cannot make quality investments or the investments perform poorly, this can drive down returns and undermine institutional investor confidence in the sector. Consequently, this can make it more difficult for venture capitalists to raise funds and potentially dissuade them from investing in a given sector.[7] Equally, if there are high levels of demand for investment and strong returns, this can attract new investors seeking exit. While angel investors do not specifically follow this pattern (they are typically investing their own money, and hence do not need to engage in fundraising), the pressures – particularly around the need for exit – remain similar.

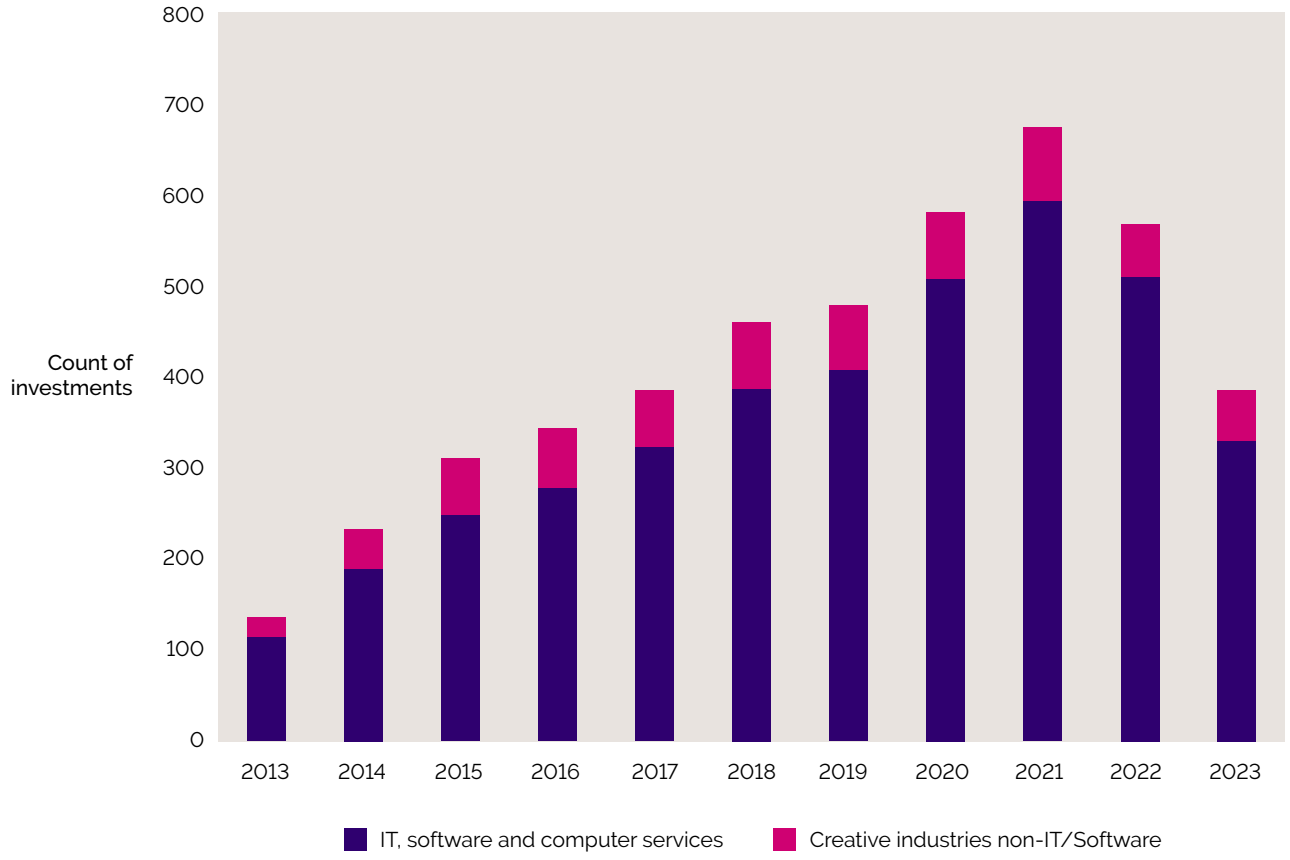
Our analysis is based on funding data from Dealroom, as provided by The Data City. The data captures 4505 unique investment rounds in 2519 companies from 2013–2023. The investments covered in our data include both VC and angel funding, but within the data provided the distinction is not always clear. Generally, the value of investments made by angel investors will be relatively smaller, while venture capitalists will look to invest substantially larger sums,[8] but this is not always the case. We discuss levels of investment and what can be inferred from these in Section 3.3. Our aim, therefore, is to capture investment trends for the creative industries overall and with regard to several crucial dimensions: sector, geography and deal size.

3.1 Investment trends

Analysing investment trends in the creative industries requires particular consideration of the differences between creative industries subsectors. This is because the IT, software and computer services subsector receives a disproportionate amount of investment – in 2023, businesses in this subsector received 85% of creative industries investment. This is neither unusual nor surprising, as software has been one of the sectors in which VC investors tend to specialise, but it does require consideration from the outset.

Looking at the overall number of investments received by creative industries firms in the data, as shown below in Figure 3.2, there is a general upward trend from 2013, a peak in 2021, followed by a slight decline in 2022 and a more substantial decline in 2023. This broadly tracks general investment trends across the UK for equity deals, although the 31% decline in the number of creative industries investments from 2022 to 2023 was higher than the 25% decline in deals across the whole of the UK (British Business Bank, 2024). The figures for IT, software and computer services show a 35% decline from 2022 to 2023, while for the rest of the creative industries the number of investments was very similar (57 in 2022 versus 56 in 2023), but these followed a 28% decline between 2021 and 2022.

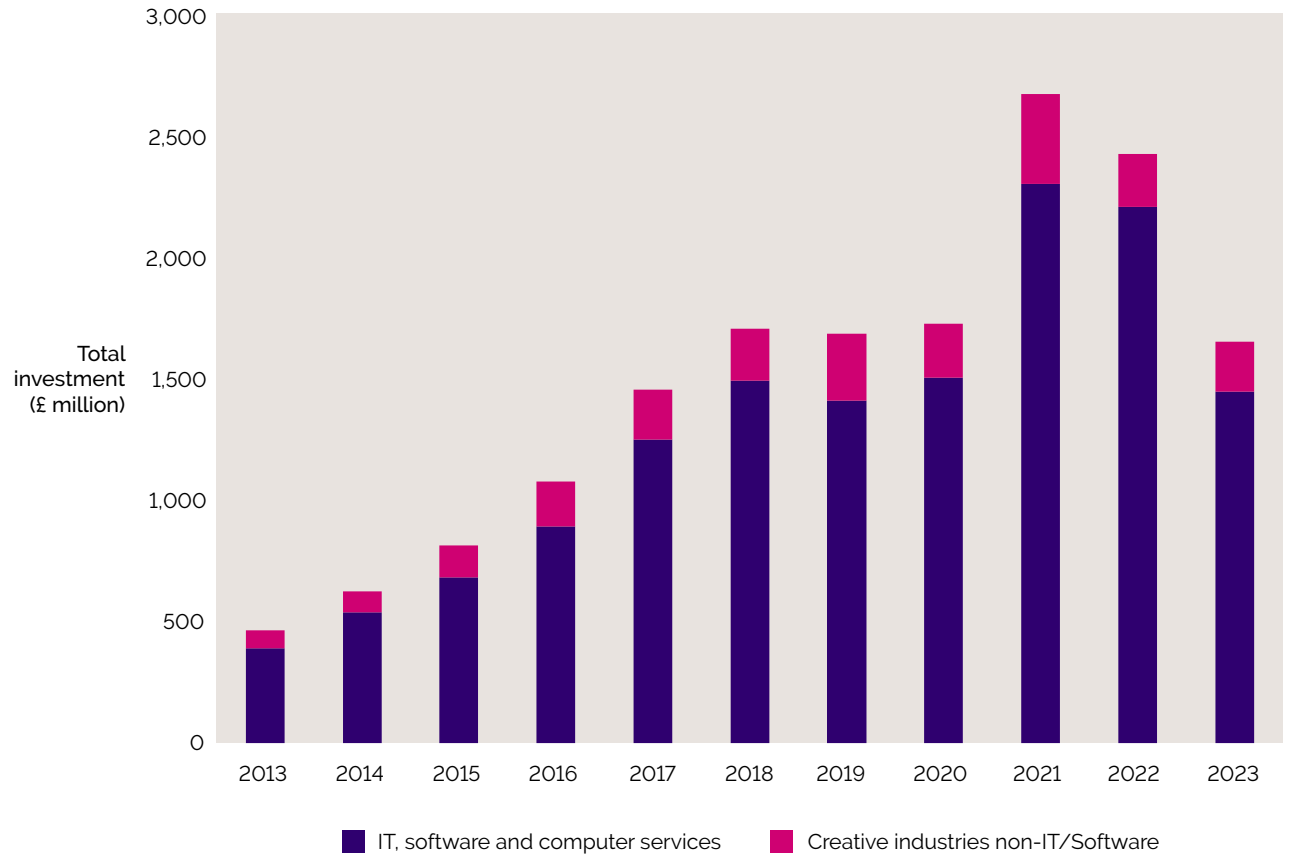
Figure 3.2: Count of creative industries firms receiving equity funding: IT, software and computer services versus non-IT, software and computer services, 2013–2023



Source: Authors' elaboration based on Dealroom data provided by The Data City.

The total value of investments over this period also follows a similar trend, as seen below in Figure 3.3. Deal value declined by 32% from 2022 to 2023 for creative industries, compared with a 48% decline across all sectors. For IT, software and computer services, the decline in total deal value was 34% from 2022 to 2023, compared with a 6% fall in the same period for creative non-IT, software and computer services. However, in the previous year from 2021 to 2022, non-IT, software and computer services had a decline in total deal value of 41%.

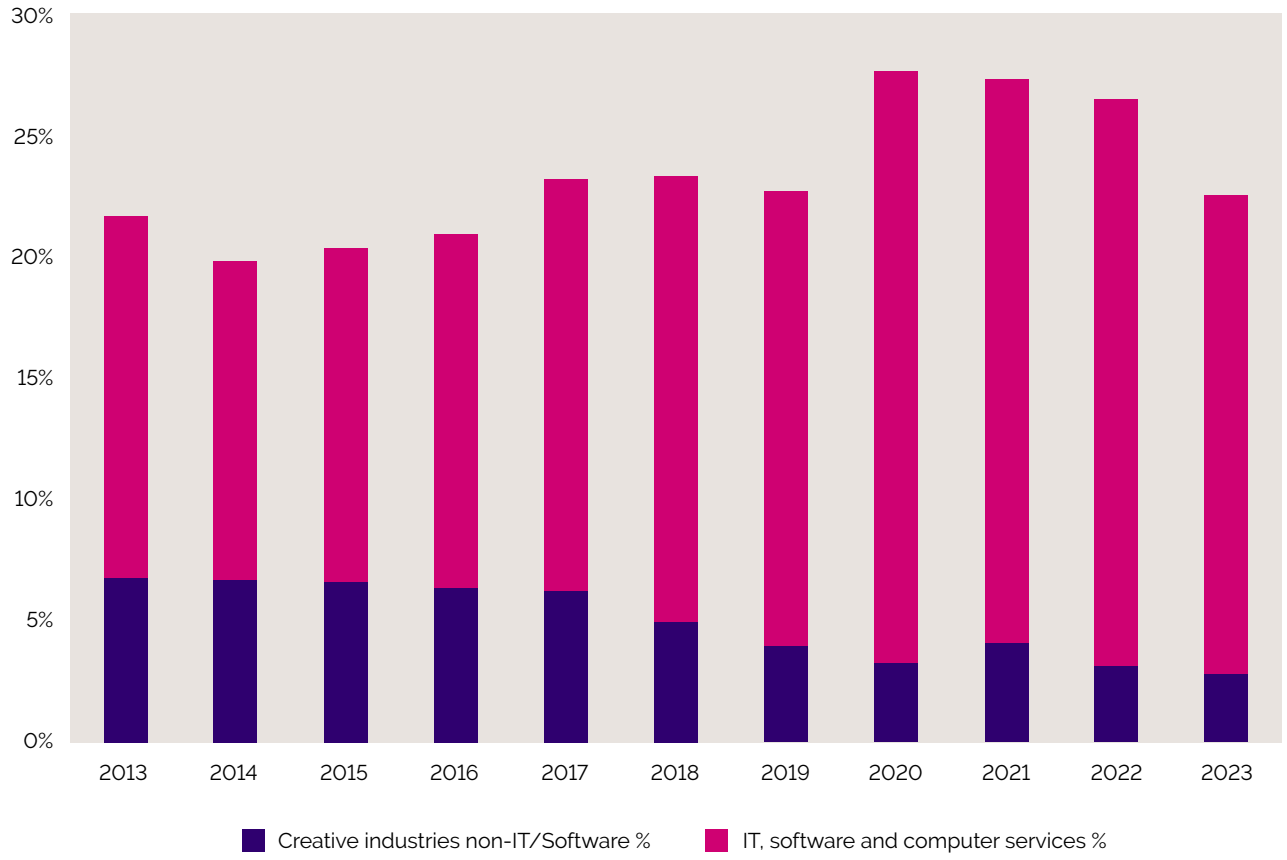
Figure 3.3: Total value of creative industries equity investments (nominal £ million): IT, software and computer services versus non-IT, software and computer services, 2013–2023



Source: Authors' elaboration based on Dealroom data provided by The Data City.

The amount of funding peaked in 2021 with £2.7 billion invested in growth capital in creative firms. Of this total, £2.3 billion was invested in IT, software and computer services and £370 million was invested in companies in other creative sectors. Overall, our data shows that creative industries businesses have raised a total of £16.5 billion over the period from 2013 to 2023, with £14.1 billion invested in IT, software and computer services and £2.2 billion in other creative sectors. This is substantial and represents a relatively consistent share of the overall UK growth-oriented equity market over this timeframe – as seen below in Figure 3.4, which shows the percentages that creative firms (split into IT, software and computer services, and other creative sectors) receiving investment make up of all firms receiving investment in the 2013 to 2023 period. Unfortunately, we do not have reliable figures for total non-creative industries VC investment spending by year so cannot include creative industries investment as a share of total funding.

Figure 3.4: Creative industries firms as percentage of all businesses receiving investment



Source: Authors' elaboration based on Dealroom data provided by The Data City.

The figure above also shows that the non-IT, software and computer services share of firms receiving investment has been steadily declining. In 2022, approximately 2.5% of all firms receiving investment were creative businesses outside the IT, software and computer services sector. This bears further consideration, as it implies that non-IT creative businesses are making up a progressively smaller share of investments.

3.2 Subsectoral analysis

As highlighted above, there is a sizeable disparity in funding between IT, software and computer services and other sectors. Table 3.1 below demonstrates this: between 2013 and 2023, 85% of firms in creative sectors that received investment were, indeed, in IT, software and computer services. The recent downturn in VC funding has also affected all sectors.

Table 3.1: Unique firms receiving investment by sector and year, 2013–2023

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Sector total	Sector total %
Advertising and marketing	9	11	16	20	13	20	11	18	18	6	11	153	3%
Architecture					1	2	1	3	5	1	3	16	<1%
Design and designer fashion	2	8	5	8	9	9	20	21	22	20	18	142	3%
Film, TV, video and radio	5	12	21	15	14	10	15	15	14	12	9	142	3%
IT, software and computer services	114	188	248	278	323	386	407	506	592	508	329	3879	85%
Music, performing and visual arts	3	4	10	11	15	12	11	9	12	12	10	109	2%
Publishing	2	8	9	11	10	19	12	7	9	6	5	98	2%
Year total	135	231	309	343	385	458	477	579	672	565	385	4,539	

Source: Authors' elaboration based on Dealroom data provided by The Data City.

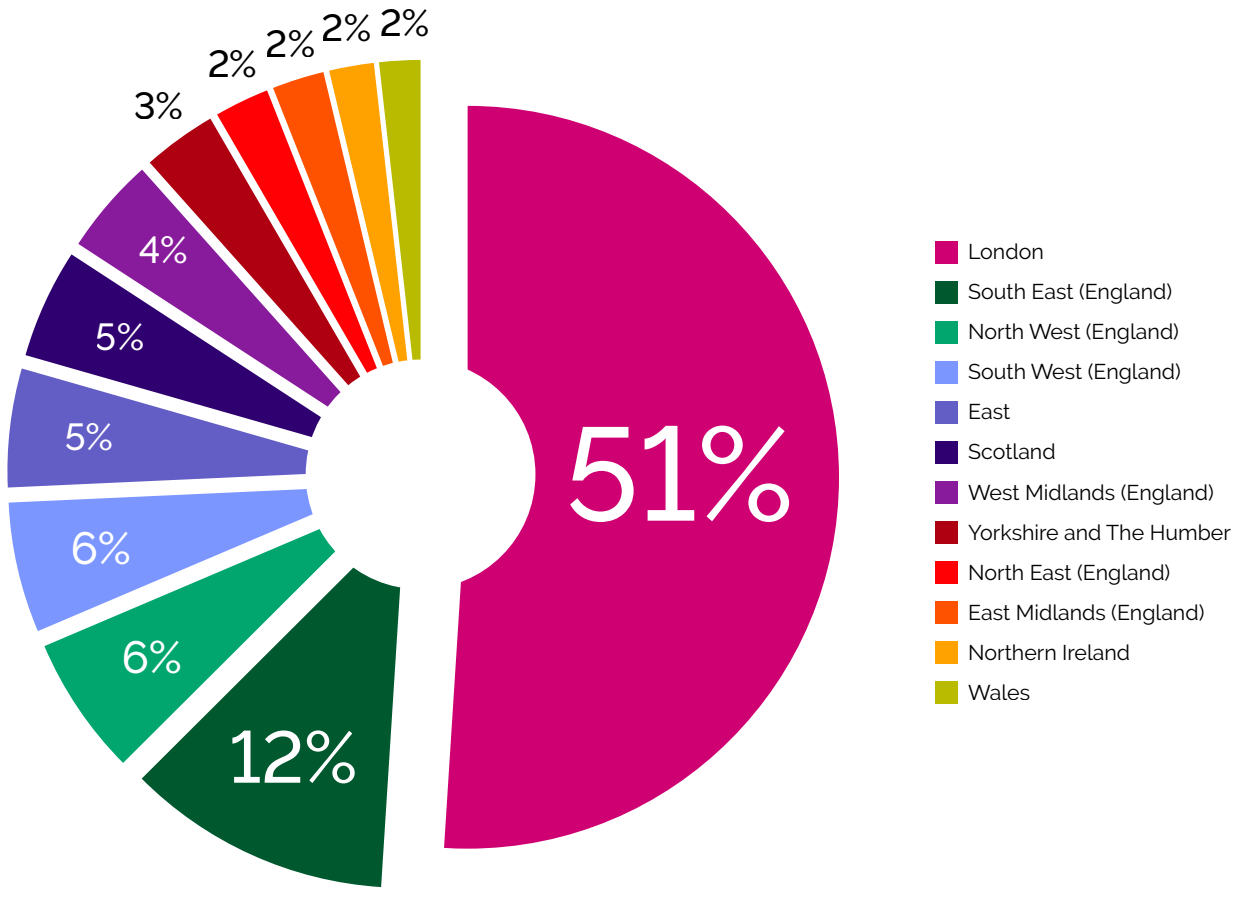
For most sectors, there was a steady increase in the number of investments, peaking around the 2019–2021 period and subsequently declining, though the numbers of investments are relatively modest so may not be indicative of overall trends.

3.3 Geographical analysis

Regional inequality is a major issue for the UK's economy, including the creative industries, with the highest levels of creative industry activity in London and the South East (Siepel et al., 2023; Tether, 2019). A similar phenomenon exists in VC, as VC investment in all sectors has long been concentrated within the Golden Triangle of London, Oxford and Cambridge. Given these parallel issues, improving access to growth capital to address regional inequalities has been a major policy priority for the creative industries. The Creative Scale Up and Create Growth Programmes aim to address this by increasing demand for capital outside London and the South East. In this section, we examine whether equity investment in the creative sectors mirrors regional concentrations in the creative industries and VC sectors more broadly.

Figure 3.4 shows the regional distribution of investments over the period from 2013 to 2023. The figures demonstrate that a disproportionate share of investments went to firms in London and the South East: 51% of VC investments went to London businesses and 12% went to the South East, meaning that 63% of investments in the sample were restricted to these two regions. By contrast, only 11% of investments went to the North of England (including 6% in the North West, 3% in Yorkshire and the Humber and 2% in the North East), 5% to Scotland, and 2% each to Wales and Northern Ireland.

Figure 3.5: VC investments in the creative industries by region, 2013–2023



Source: Authors' elaboration based on Dealroom data provided by The Data City.

These regional distributions are persistent over time (see the online supplementary materials for yearly figures by region) and do not show any evidence of narrowing – the combined share of investments from London and the South East remained over 60% across the ten-year period. These are also consistent with general investment trends, as shown below in Table 3.2, which shows that when compared with the overall VC and private equity market (as seen in data from British Business Bank, 2024), the regional distributions are nearly identical. What stands out is that the strengths in the South East are more in IT, software and computer services than in other creative sectors, and that creative industries investment is slightly lower in the East of England and Scotland compared with the market average.

Table 3.2: Regional distribution of investments versus total UK market, 2021–2023

Region	Creative industries total	Creative industries (IT/software)	Creative industries (non-IT, software and computer services)	Overall private equity/VC market (British Business Bank, 2024)
East	5%	5%	5%	7%
East Midlands (England)	2%	3%	4%	2%
London	53%	54%	54%	54%
North East (England)	2%	2%	2%	2%
North West (England)	6%	6%	5%	6%
Northern Ireland	2%	2%	1%	2%
Scotland	5%	4%	5%	7%
South East (England)	10%	11%	6%	9%
South West (England)	6%	5%	10%	5%
Wales	2%	2%	2%	2%
West Midlands (England)	4%	3%	2%	2%
Yorkshire and the Humber	3%	3%	4%	3%

Source: Authors' elaboration based on Dealroom data provided by The Data City and British Business Bank (2024).

Apart from London's dominance, we can see fewer creative industries investments in the other parts of the Golden Triangle: while 51% of investments in the sample went to London, only 3% of the investments in our sample went to Oxford and Cambridge, which is not a surprise as those cities tend to specialise in other high-tech sectors such as the life sciences.[9] Within the regional data, we see little evidence of sectoral specialisation in individual regions: the South West had 18% of investments in design firms, and both the North West and South West had particular success in attracting funding for advertising firms (8% each of the total number of investments).

Our analysis does suggest that funding is flowing towards creative clusters: Table 3.3 below shows the share of investments made within the fifty-five creative clusters identified by the Department for Digital, Culture, Media and Sport (DCMS) (Frontier Economics, 2022). In total, 92% of investments were made in these fifty-five clusters.

Table 3.3: Percentage of creative industries investments in DCMS creative clusters and microclusters

	Investments in DCMS creative clusters		Investments outside DCMS creative clusters	
		In microclusters		In microclusters
East	97%	48%	3%	-
East Midlands	24%	25%	76%	48%
London	100%	59%		
North East	80%	48%	20%	8%
North West	93%	75%	7%	74%
Northern Ireland	90%	-	10%	-
Scotland	91%	65%	9%	9%
South East	95%	49%	5%	40%
South West	80%	68%	20%	48%
Wales	60%	53%	40%	30%
West Midlands	52%	73%	48%	45%
Yorkshire and the Humber	73%	58%	27%	41%
Total	92%	58%	8%	42%

Note: we do not report a percentage value when the total number of investments received outside creative clusters was less than ten.

Source: Authors' elaboration based on Dealroom data provided by The Data City.

These percentages show that investment disproportionately goes to the most-established creative clusters, although this varies substantially by region – in the East Midlands (where Nottingham is not classed as a creative cluster by DCMS), the figure is only 24%, whereas in many other regions over 90% of investments occur in clusters. These results were expected, as VC investments tend to focus on particular clusters (Sorenson and Stuart, 2001). Looking into finer geographies, we see a similar effect for microclusters. Of all VC investments, 58% were made in businesses located in one of the 709 creative microclusters previously identified by the Creative PEC (Siepel et al., 2020). In Table 3.3, we see that the share of investments in microclusters by region indicates substantial regional variation. However, in line with the previous findings of the Creative Radar research, we do see that 42% of investments made outside of creative clusters were to businesses in microclusters. This suggests that microclusters have an important role – overall, only 4% of investments went to companies not in a creative cluster or microcluster.

3.4 Deal size

Growth capital investments can vary substantially in size. As companies grow, their initial, limited capital needs can become substantial. As we mention above, our data includes VC and angel investments – and examining the distribution of deal size can inform our understanding of the types of investment available to creative industries businesses. Table 3.4 below shows the percentage of deals in our sample by size.

Table 3.4: Percentage of investments by deal size

Investment size	Percentage of total investments
<£100k	9%
£100k–250k	15%
£250k–500k	13%
£500k–£1m	12%
£1m–5m	29%
£5m–10m	9%
£10m–50m	10%
£50m+	5%

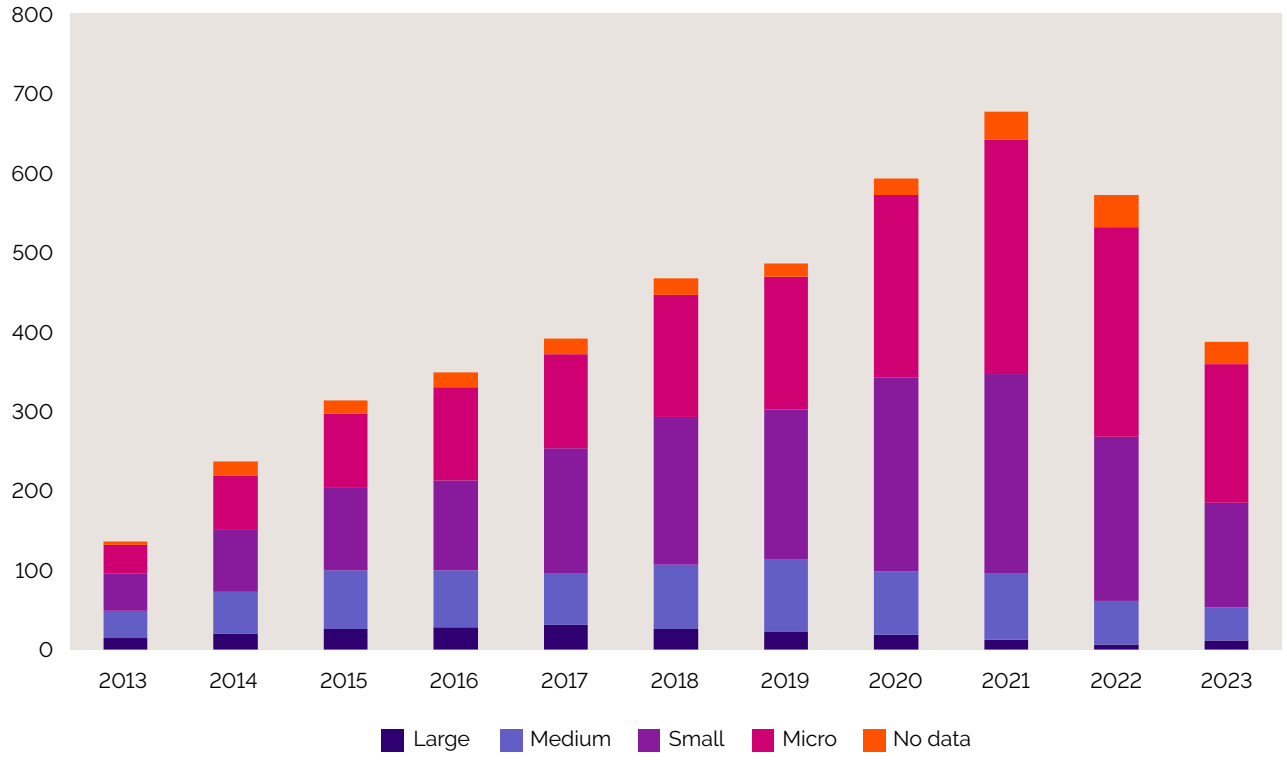
Source: Authors' elaboration based on Dealroom data provided by The Data City.

This table reveals some interesting insights. First, there is a relatively low proportion of investments in our sample at the smallest, pre-seed level (below £250k). This is unsurprising because these small deals are difficult to count and may not be found in many commercial databases. Even if we assume that these deals are undercounted (given that it is not unusual for early-stage businesses to fail), the similar share of investments in the £100,000–250,000, £250,000–500,000 and £500,000–£1 million bands, followed by a substantial share of investments over the £1 million level, is consistent with a potential "equity gap" (Wilson et al., 2018). An equity gap appears when certain values of deal are less common due to structural factors. In early-stage equity markets, this can occur when there are smaller-scale investors such as angel investors and large-scale investors such as venture capitalists, but there is a gap in funding where the deals are too large for angel investors but too small for venture capitalists. Our data does not comprehensively show that there is an equity gap, but this topic is worth further consideration.

Examining the size of companies when they received investment and the size of deals themselves can also be helpful. Few firms will progress to receive large investments, so the distribution can indicate the nature and scale of the funding "escalator" from small to large investments.

Our data includes information on firm size, classifying firms as micro (fewer than ten employees), small (10–25 employees), medium (25–100 employees) and large (100+ employees), as well as separating those for which there is no data. Figure 3.6 shows the relative composition of investments by size over the period from 2013 to 2023. It reveals that the number of large and medium-sized firms receiving VC investment remained relatively consistent, while much of the increase was in small and micro firms. This is significant because it indicates inflow of funds to smaller, emerging businesses.

Figure 3.6: Count of companies receiving VC by year and firm size



Source: Authors' elaboration based on Dealroom data provided by The Data City.

In conclusion, from our analysis of VC supply, we find that VC investments in the creative industries are heavily concentrated on IT, software and computer services, primarily in London and the South East of England. This should be viewed as a feature, not a glitch, of VC as a financial instrument. VC is well known for its high levels of both sector-level and geographical concentration. If the scope of VC investment is to be broadened beyond current concentrations, one key element will be to demonstrate that investments in sectors outside IT, software and computer services – and regions outside London and the South East – can generate viable returns. Capturing these returns will provide evidence to funders of the viability of further growth investment (UKBAA, 2023).

Markets for exit

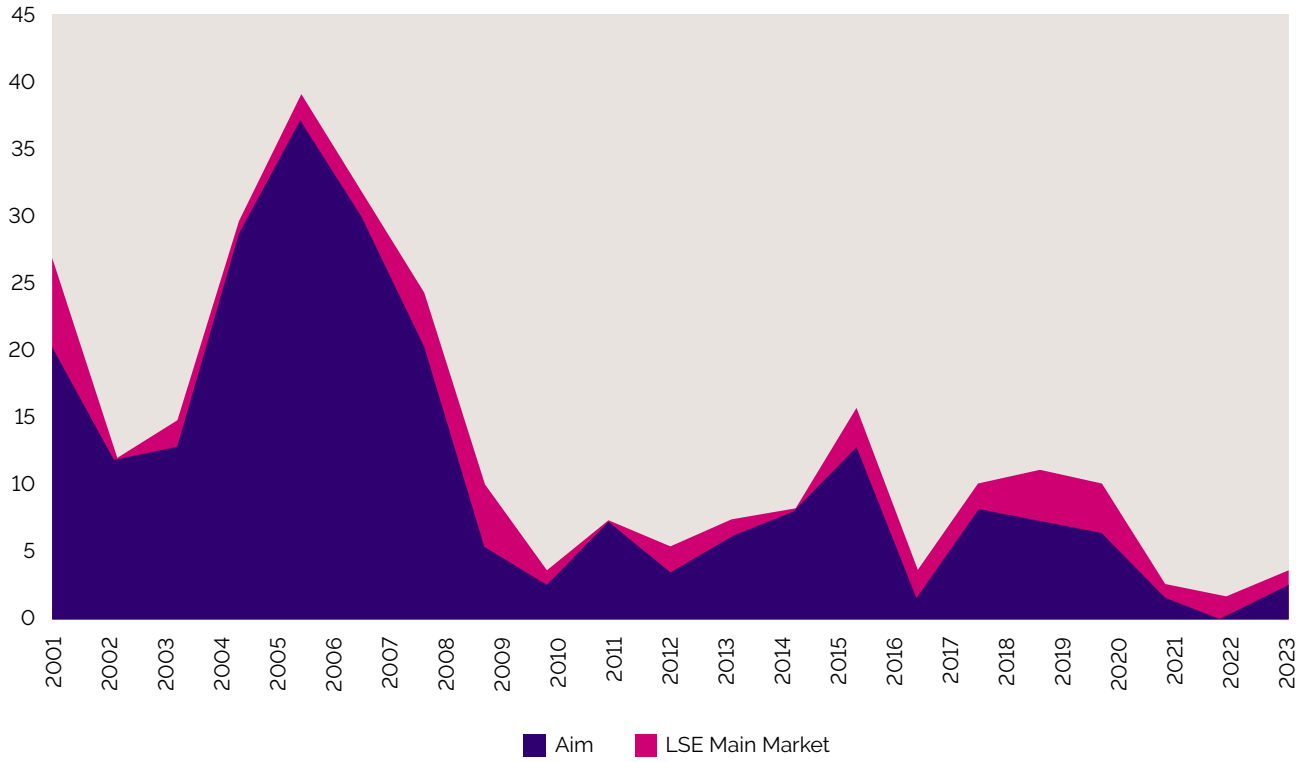
Markets for private investment, such as VC, only work when there is capacity for investors to realise returns from their investments. For this reason, the availability of exit opportunities is crucial for growth capital. Most VC investors prefer an optimal timeframe for exit of three to five years: for an investment to be successful, it must be able to realise gains and return them to investors (hopefully with a strong return) within that time.

For equity investors such as venture capitalists, typically, the most desirable means of exit are via initial public offering (IPO) on a stock market and acquisition (referred to as mergers and acquisitions, or M&A). In the UK, M&A deals are the most common form of exit but understanding exit via IPO is arguably a useful starting point.

3.5 IPOs in the UK

To best understand exit via IPO in the UK, it is useful to start with the case of the United States. The success of the US VC industry largely stems from the availability of hugely lucrative IPOs. US venture capitalists achieved large, lucrative, often overpriced IPOs on the NASDAQ market, demonstrating the business case for VC as an investment model (Gompers and Lerner, 2003; Lazonick, 2009). In the UK, the institutional and regulatory environment is very different. The UK has two major stock markets: the London Stock Exchange (LSE) for the UK's largest firms and the Alternative Investment Market (AIM) for smaller and growing companies. While the regulatory requirements for AIM are lower than those for LSE, they are stringent in a way that means new listings on AIM tends to be effective in allowing companies to access new funding rounds while not facilitating overvalued, highly lucrative IPOs, as seen with the NASDAQ market (Revest and Sapio, 2013). In practice, this means that VC-backed IPOs are relatively uncommon in the UK. Figure 3.7 below shows the number of creative industries IPOs in the UK from 2001 to 2021.

Figure 3.7: Count of creative industries IPOs on the AIM and LSE Main Markets, 2001–2021



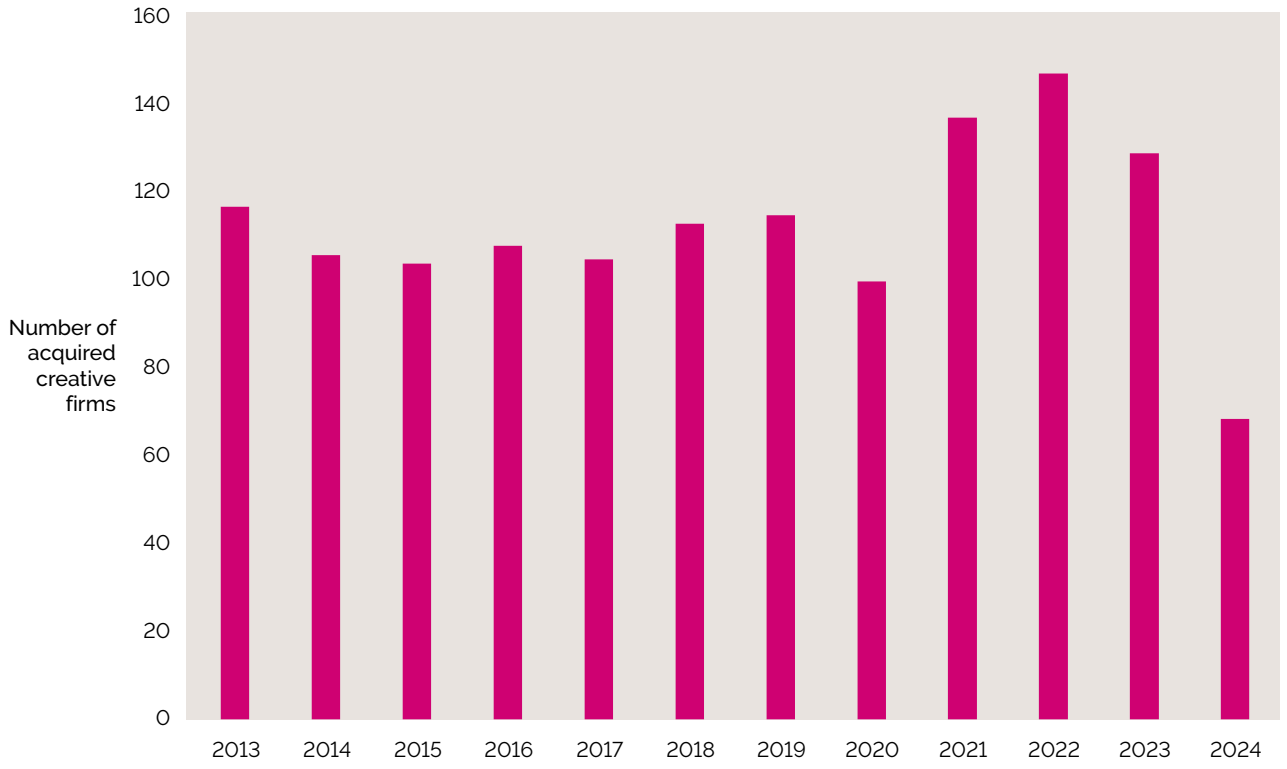
Source: Authors' elaboration based on LSE IPO data.

The figure shows that over the past ten years, the number of IPOs on AIM has been very low, with only a handful of creative industries businesses listing on the LSE Main Market.[10] This indicates the extent to which IPOs are not a feasible exit means. Moreover, the ability of VC-backed companies to exit on AIM or LSE remains limited; of the sixty-three IPOs by businesses in a DCMS creative industries SIC code from 2013 to 2024, only nine had received VC investment according to our data. All nine were in the IT, software and computer services sector.

Exit via M&A in the creative industries

The Creative PEC will explore M&A in much more detail in a future report, but our interest here is in how M&A relates to investment and exit. As IPOs do not provide a viable option for exit for venture capitalists and other growth capital investors, the only other plausible means of exit is via acquisition or M&A. This has been the case for decades but has significant implications for the structure and organisation of creative industries businesses in the UK. Figure 3.8 below shows the number of creative industries M&A deals from 2013 to 2024.

Figure 3.8: Number of creative industries firms acquired by year, 2013–2024



Source: Authors' elaboration based on Orbis M&A data.

The scale of this graph is notable in comparison to the IPO graph, with approximately 130 acquisitions in the UK in 2021 versus three AIM IPOs and one LSE IPO. Our analysis of Orbis data alongside the Dealroom data suggests that the share of acquisition deals backed by VC was modest – approximately 142 acquisitions of VC-backed firms occurred between 2010 and 2024, around 9% of all M&A deals in total. Of these M&A deals, 118, or 82%, were companies in the IT, software and computer services sector.

The evidence on exit is opaque and difficult to gather, and these figures represent best estimates with the available data. However, the implications are considerable: first, there is a substantial amount of M&A activity in the UK. This feeds into concerns previously raised about the tendency of UK businesses to sell to international companies and the long-term implications of this loss of ownership for the UK's potential businesses. For example, the video game sector has seen 118 transactions where a UK-incorporated video game studio has been acquired by overseas buyers since 1993 (Oxford Economics, 2022). Measuring the impact of these acquisitions is difficult but important (Oxford Economics, 2022). Future Creative PEC work will explore this in more detail.

The second implication relates to finance: equity investments such as VC require a means of exiting their investments and returning funds to their investors. M&A is the dominant means by which equity investors can achieve exit in the UK, but M&A can also serve to reinforce regional and other inequalities (Ioramashvili et al., 2024). It is therefore worth engaging in a discussion about whether other means of exit – such as IPO – or other forms of investment can provide returns to investors while also achieving the aim of longer-term patient capital set out in the HM Treasury Patient Capital Review (HM Treasury, 2017). Being able to demonstrate strong returns could help channel further growth capital into creative industries and other growing sectors.

4 Conclusion and future directions

This report explores the nature and availability of growth finance for companies in the creative industries. Given that most creative businesses engage in some form of innovation, the growth capital problem is also a broader access to finance problem. The paper explores three crucial elements of the innovation finance ecosystem: demand for growth capital, supply of growth capital and opportunities for exit.

4.1 Demand

Demand for capital is a vital and often underappreciated element of growth finance, particularly for the creative industries, which are characterised by large numbers of small and medium-sized firms. Creative firms are more likely than the general population of firms to expect to grow (CIC, 2017), but not all creative businesses want to grow (Sigurdardottir and Candi, 2018). The challenge, therefore, is how to unlock that desire for and anticipation of growth to best support growth and prosperity in creative firms across the UK.

Our research in this report shows that creative industries businesses are more likely to identify new investment opportunities but may struggle to access the finance required to take advantage of these opportunities. Several factors could explain this. One is discouragement, where businesses' perceptions that they will not be able to access finance deter them from applying (Cowling et al., 2016; Kon and Storey, 2004). We find that discouragement in creative firms is associated with perceptions that financial institutions are unfavourable to creative firms, as well as concerns about losing control of the business.

Another factor that can explain creative firms' difficulties in capitalising on investment opportunities is investment readiness, which refers to the attributes that make a firm a good candidate to receive growth finance (Mason and Harrison, 2001). Because businesses may not understand what is required for growth investment, support to achieve investment readiness can be invaluable. Recent policy interventions, such as the Department for Digital, Culture, Media and Sport (DCMS) Creative Scale Up (CSU) and DCMS Create Growth Programmes, have sought to help businesses boost their investment readiness by supporting them to better understand what investors want and how to configure their businesses to grow. These types of intervention can address both discouragement and investment readiness issues, thereby building demand for growth capital in companies that are ready to grow. This suggests that efforts to continue building capacity within creative ecosystems through strengthening creative organisations' investment readiness is a critical element of driving growth.

4.2 Supply

Our discussion of supply of growth capital focuses on growth-oriented equity investment, including venture capital (VC) and angel investment. Although many other forms of finance can be used for growth, these are among the most frequently used for small, rapidly growing businesses. Our analysis of investment in creative industries is consistent with academic research showing that VC investors tend to concentrate in specific sectors (Hsu and Kenney, 2005) and specific geographies (Ferrary and Granovetter, 2009; Sorenson and Stuart, 2001).

We find that most investment in creative industries is directed to businesses in the IT, software and computer services sector. Only 15% of VC investments from 2013 to 2023 were in creative subsectors outside of IT, software and computer services, and the relative share of other creative sectors in terms of total investments has declined in recent years.

VC also tends to be heavily geographically concentrated in specific regions and clusters (Florida and Mellander, 2016; Kenney, 2011). Our analysis finds that current geographical concentration of creative industries in London and the South East (Siepel et al., 2023; Tether, 2019) is also seen in VC investments, with 63% of VC investments in creative industries taking place in these regions. But from a perspective of tackling regional inequality, we also find that 95% of VC investments were made in creative clusters or creative microclusters. This suggests that efforts to support businesses in creative clusters and microclusters, such as the Arts and Humanities Council (AHRC) Creative Industries Clusters Programme, effectively support businesses in places that are likely to generate investable companies.

The heavy sectoral and geographical concentrations of investment in the creative industries are partially a feature of equity investment, as highlighted above. But specific factors may help to explain these gaps, and can be targeted through policy mechanisms.

One solution relates to investment readiness. Providing businesses with the knowledge to understand what equity investment means and what investors require can help owners make informed decisions. Given that creative businesses may have less desire for rapid growth or greater desire to avoid dilution of equity, building knowledge can address information asymmetries, which can characterise market failures. Equally, addressing the lack of sufficient data on returns in creative sectors (UKBAA, 2023) can help investors gain a better understanding about the returns and opportunities for investment in creative sectors, thus stimulating supply. Recent policy interventions, such as DCMS CSU and DCMS Create Growth Programmes, have attempted to address these gaps at a local and regional level. While evaluations are forthcoming, our analysis suggests that further strengthening of efforts to support investment readiness within the creative industries could help address the challenges identified in this report.

Building a robust supply of growth capital also means ensuring that there are sufficient successful exits from investments, as prior success can demonstrate the viability of a sector or region. Our analysis of opportunities for exit from investment shows that mergers and acquisitions (M&A) are far more common in the creative industries than initial public offerings (IPOs) on the stock market. The dominance of M&A as a means of exiting investments has other implications, including the reinforcement of regional inequalities (Ioramashvili et al., 2024). There is therefore a need to better understand the implications of M&A and IPO, and how exits can best be supported.

4.3 Building a successful system for financing growth in the creative industries

From the analysis in this report, we can see that while growth capital such as VC is vital for the creative industries, current configurations of growth capital reinforce inequalities and pose strategic challenges to the UK's position as a global leader in creative industries. In considering the future of growth capital, it is useful to look back in time.

The VC sector emerged in the late twentieth century in the United States and proved very effective at capitalising the vast numbers of technological innovations that were being produced, many of them by commercialising research that was originally commercially funded. But VC was, in fact, invented – and the form of VC that we know today is the result of decades of effort, development and evolution (Hsu and Kenney, 2005; Siepel, 2011). This speaks to the importance of innovation and evolution in finance; simply because VC is the dominant mode of growth capital does not mean that it is the only mode.

On this basis, the creative industries offer a rich setting for innovation. Notably, one of the only truly new asset classes to emerge in recent years was the music rights product pioneered by companies such as Hipgnosis and Concord Chorus. These companies made headlines by purchasing publishing rights to musical artists' back catalogues, with the aim of generating long-term returns through management of these rights. While views on the companies working in these markets vary, it is undeniable that they have introduced an innovative way of linking financial markets to artists. The creative industries, in all their diversity, offer other substantial opportunities for new innovations in finance. Moreover, VC, or indeed equity investment, need not be the only form of finance used by growing companies. Indeed, some new and innovative financial instruments are emerging already.

Intellectual property (IP)-backed finance: the HM Treasury Patient Capital Review in 2016/17 explored the challenges in accessing long-term patient capital for innovative and growing firms. Because of the challenges faced by companies that rely on IP, there has been substantial interest in strengthening IP-backed finance. Historically, IP-rich firms have turned to equity finance because banks perceived IP as too risky to accept as collateral. But a crucial 2018 study by the British Business Bank and UK Intellectual Property Office found that companies holding IP were less likely to default on loans, and losses to banks from defaulted firms were lower (British Business Bank, 2018). This finding was particularly important because it addressed the perceived bias by banks against IP-reliant companies. By demonstrating that IP-rich firms were, in fact, reliable, the study emphasised to funders that debt could potentially be a tool in the portfolio of growth capital, in addition to equity. In light of these findings, there is increasing interest in new and strengthened IP-backed finance (World Intellectual Property Organization, 2023), so that companies holding IP can access finance, with the IP being fairly treated as collateral or as the basis for equity investment. An increasing number of banks now offer IP-backed loans, and there is growing interest in this market.

Impact investing: impact investing refers to investments made with the aim of generating both financial and social returns. The impact investing sector is emerging and remains very broad, but there have been major developments in the area for the arts, cultural and creative sectors (Sanderson et al., 2023). The launch in 2024 of Figurative (previously Arts & Culture Finance) has highlighted the potential for new financial instruments – in Figurative's case, repayable finance offered to arts and cultural organisations. Impact investment generates positive returns, while allowing organisations to continue generating social impact, and points to the importance of repayable capital as an option for growth, rather than equity.

Community bonds: community bonds are an emergent trend in social finance that allow nonprofit groups to leverage supporters to pursue their mission by investing in a bond that serves the community. They are gaining popularity from an impact investing perspective but have interesting implications for creative sectors and communities that might struggle to attract conventional growth funding or other public investment.

Numerous other examples are available, with exciting opportunities for finance in creative sectors through these new instruments. One of the main challenges for designing financial instruments is how to attract new investors. Recent investments in the creative industries, such as the AHRC Creative Industries Clusters Programme, have been very successful in "crowding in"[11] external investors to support creative businesses (Frontier Economics and BOP Consulting, 2024). With the new government expressing interest in unlocking investment from the pensions sector into the UK, there are prominent opportunities for developing new financial instruments that will bring growth capital to the creative businesses and workers who can effectively use them. Creative UK's call for a "Bank of Creativity" represents one of many possible ways that these opportunities could be enacted.

It should also be noted that throughout this report, data availability and access were recurring issues. To our knowledge, this is the first report to explore VC investment trends in the creative industries, but there is much more that remains unknown. There is clear evidence that investors would be willing to invest in creative industries businesses if they had sufficient data on returns and exits. To date, at least to our knowledge, this data doesn't exist, putting creative businesses at a disadvantage relative to other sectors. Because the creative industries are identified by four-digit SIC codes, disaggregated data for the creative industries is difficult to access and is not widely published. Likewise, in some content sectors such as film, the absence of reliable financial data is a substantial problem (Franklin, 2024): filling these gaps may help to unlock further investment. There are multiple public sector investments in creative industries (DCMS CSU and Create Growth Programmes, and the Innovate UK Creative Catalyst scheme) where evaluations are forthcoming at a scheme level, but investment in data infrastructure to capture granular returns could produce tangible benefits in attracting new investors. The forthcoming research from Creative UK and the Creative PEC updating the 2017 CIC survey will help to give an updated perspective on demand, but deeper insights about flows of capital into creative industries (whether private, public or philanthropic) will help to drive better decisionmaking.

In conclusion, this report has explored the growth capital situation for the creative industries. It finds that there are meaningful issues in supply, demand and exit. All of these can be addressed – for instance, through support for demand (via supporting investor readiness) and supply (by combining targeted capital with adjusted funder attitudes), and increased openness on the part of investors, regulators and businesses for new financial instruments. The prize – a financial system that supports creative industries businesses to grow and reach their potential – is huge.

Glossary

Angel investment

Equity investments made by individuals using their own funds.

Debt capital

Investments where funds are provided to a business and repaid with interest but no equity changes hands. Debt holders have a legal priority in the event of company failure through bankruptcy or insolvency.

Discouragement

A phenomenon where businesses who would otherwise be able to access capital choose not to apply for it because they do not think their applications will be successful.

Equity capital

Investments where an investor purchases a share of the ownership of a company.

Growth capital

Investments designed to support companies to grow rapidly. Growth capital is typically associated with equity investment, such as venture capital, but may involve other forms of non-equity investment, such as venture debt.

Initial public offering (IPO)

Listing of shares on a stock market, thus allowing investors to sell their shares and exit the investment.

Private equity

Occasionally conflated with venture capital; for our purposes, this is considered to be investment where private investors purchase ownership of a mature firm, with the aim of growing the company.

Pre-seed and seed investment

Early-stage investments, made by venture capitalists or angel investors, in companies that are not sufficiently established to receive Series A funding.

Series A, B, C, D, etc

Funding rounds made by investors into growing companies. A company's first major funding round will be Series A, and a subsequent funding round would be Series B, and so forth. Funding rounds typically increase in size as the company grows.

Scarred borrowers

Firms that previously applied for debt but were rejected and subsequently self-exclude from the debt market.

Venture capital (VC)

Form of investment where professional investors raise funds from institutional investors, invest these funds in small, high-growth firms and support the firms to achieve profitable exit.

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Data availability statement

The following data sets were used in the production of this report:

DBT Investment Survey

Fig. 2.1, 2.2

The data behind the findings of this study is not publicly available. Queries about the data and the analysis presented here may be sent to the corresponding author, Dr Josh Siepel (j.siepel@sussex.ac.uk).

CIC Access to Finance Survey 2017

Fig. 2.3, Table 2.1, 2.2

The data behind the findings of this study is not publicly available. Queries about the data and the analysis presented here may be sent to the corresponding author, Dr Josh Siepel (j.siepel@sussex.ac.uk).

Creative Radar data

Chapter 2

The data behind the findings of this study is available on request from the corresponding author, Dr Josh Siepel (j.siepel@sussex.ac.uk). The participants of this study did not give written consent for their data to be shared publicly.

Dealroom investment data

Fig 3.2, 3.3, 3.4, 3.5, Table 3.1, 3,2, 3.3, 3.4, 3.5, 3.6

This data is commercially available and was accessed via The Data City platform (data accessed 12 May 2024). For more details see: https://thedatacity.com/

IPO data

Fig 3.7

This data is publicly available from the London Stock Exchange website (data accessed 4 July 2024): https://www.londonstockexchange.com/live-markets/market-data-dashboard/price-explorer

M&A data

Fig 3.8

This data is commercially available and was accessed through the ORBIS M&A data platform (data accessed 3 July 2024). For more details see: https://orbis.bvdinfo.com/

Endnotes

1. The Creative Radar survey sample frame included all creative businesses with employees, so it is difficult to compare these findings to the data in Gkypali and Roper (2018) because that analysis was based on the UK Innovation Survey, which excludes firms with fewer than ten employees.
2. This analysis is conducted by Marc Cowling, Huan Yang and Josh Siepel. Details about the research and methodology are presented in the Online Supplementary Materials.
3. The most notable example was the UK Regional Venture Capital Fund, a series of regional VC funds in the early 2000s. Nightingale et al (2009) discuss the poor performance of these funds, largely due to having too much money and chasing too few quality investments, resulting in poor quality portfolio firms and huge losses.
4. This analysis was done by Jorge Velez Ospina and Josh Siepel. Details of the methodology and analysis can be found in the Online Supplementary Materials.
5. Details of the analysis are available in the Online Supplementary Materials.
6. Definitions can be unclear but for our purposes we consider private equity funds to refer to investors who buy out ownership of a company; private equity tends to prefer larger, mature firms and so for our purposes we do not consider this type of investment as growth capital.
7. Such a phenomenon occurred in the mid-2000s in the biotechnology sector, where overhype and poor returns substantially dented investor confidence in biotech, depressing VC supply (see Hopkins et al., 2013; Owen and Hopkins, 2016).
8. Because contracting and oversight are fixed costs, venture capitalists are incentivised to make fewer, larger investments. This is one reason why there has been persistent concern about an equity gap for businesses between equity available from sources such as angel investors and funding available from venture capitalists (see Wilson et al., 2018).
9. See, for instance, efforts to unify the "Oxford-Cambridge Arc", which focused primarily on the benefits of technology firms: https://www.gov.uk/government/publications/oxford-cambridge-arc
10. The higher levels of creative industries IPOs on AIM in the mid-2000s could relate more to rules around the eligibility of firms on AIM at the time, which were tightened due to the late 2000s financial crisis.
11. "Crowding in" refers to situations where public funding is used to leverage private finance that would not be accessible otherwise. Examples include cases where public funding is used to help de-risk investments and attract private investors. It is the opposite of "crowding out", where public funds enter a financial market and provide a superior option for finance seekers, then driving private sector providers out from the market.

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