

Making a difference – The contribution of graduates to small business success

Report to the
Small Business Service

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summary

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Introduction

In February 2002, the Small Business Service (SBS) commissioned Leeds Metropolitan University (LMU) to conduct a review of the contribution of graduates to small business success. The project stems from a rising concern amongst policy makers that after years of experimentation in stimulating graduate demand in SMEs, there remains a lack of understanding about what impact this has on firms, and how the relationships involved actually work.

The focus has been on secondary research. This has sought to capitalize on the broad literature which has been developed since the mid 1990s on the activities of small and medium sized enterprises (SMEs) in the changing graduate labour market. The research has consequently centred on a stock-taking exercise, critically reviewing this extensive – if fragmented – evidence base, to draw together what is known about the impact new and recently qualified graduates have on these firms.

Our scope and objectives

The numbers of graduates leaving higher education and looking for productive work has expanded greatly in the last quarter of a century in particular, and policy makers have taken a number of initiatives to help build their ability to make earlier contributions to the organisations they join. These developments have coincided with what some commentators have seen as an erosion of the dominant role of larger firms in the graduate labour market, providing much greater scope for smaller firms to harness graduate skills and knowledge. Understanding the contribution that new graduates might play in enhancing SME performance is central to unlocking this potential, yet it remains a crucial gap in knowledge for policy makers.

This project has sought to start to fill this information gap. More specifically it aims to identify the characteristics and trends relating to the graduate labour market and the role of SMEs in this by:

- **Systematically reviewing existing literature relevant to the graduate labour market and SMEs;**
- **Synthesising the relevant literature and demonstrating the strengths and weaknesses of the current knowledge base; and**
- **Developing a conceptual model, which identifies key relationships between SMEs and the graduate labour market.**

The scope of the project has potentially been very broad. Its main focus has been SME relationships with the UK graduate labour market and in particular their experiences of the impact of recruitment, retention and utilisation of new graduates. By 'new' graduates we have sought to focus on new or recently qualifying first and higher degree graduates, whatever

their age or subject background. SMEs have been defined more pragmatically – since many of the studies we have looked at have adopted different approaches to definition. However, our main focus is on autonomous or semi-autonomous enterprises employing under 250 personnel.

The project is based on an analysis of a variety of secondary information. This has been drawn from published sources as diverse as academic literature, policy research and evaluation studies, consultancy reports and web-based material. This evidence base is very fragmented and to identify relevant material we have conducted:

- **A preliminary literature search to identify what publications were available relating to the topics of ‘graduates’ and/or ‘SMEs’ published, predominantly over the last five years.**
- **A supplementary review within this area, to isolate specific research and related contributions on graduate skills and graduate employment, recruitment, utilisation - in SMEs and more generally.**

A number of online databases were also searched, with a series of journals databases and conference proceedings from established small business conferences.

The searches showed a considerable body of literature which discussed graduate employment and skills, although only relatively recently have graduates within SMEs become a distinctive focus for researchers. Consequently, this SME ‘evidence’ base is still not rich. Much of the identified research and commentary is insubstantial and few studies focus specifically on evidence of graduate contributions within smaller firms. Using criteria agreed with SBS a total of 29 sources were selected as suitable for a more detailed review of graduate impact in such firms.

SMEs and the graduate labour market

Looking across this research, we propose that there is a distinctive SME graduate labour market operating in the UK. This is a constituent part of wider graduate supply and demand relationships in the economy, but shows characteristics which set it apart from the operation of larger firms. Unlike the rest of the graduate labour market it almost totally lacks transparency.

The SME graduate labour market is a neglected rather than a new phenomenon. It has probably been operating as a segment of the wider graduate labour market for over a quarter of a century - ever since recently qualifying graduates became a substantial feature of new labour supply to the economy. However, while research on graduate recruitment, development, utilisation and impact among larger firms has become a major theme of UK employment studies over this period, the role of SMEs in seeking and utilising new graduates has been consistently neglected.

What is known from more recent research suggests that SME recruiters are certainly not models in miniature of larger and more regular recruiters. We still do not know very much at all about the size or volatility of the SME graduate labour market, but it seems to have distinctive needs and very different processes.

Until recently these contrasts have been poorly understood – or prioritised – by careers advisor, placement and other services that effectively act as gatekeepers to wider graduate supply to the labour market. This seems to have held back demand from SMEs. There is also some evidence that this has created a legacy of suspicion and doubt between SMEs about the value of new graduates to their business circumstances, and among the graduates themselves about SME opportunities.

The apparent growth in the SME graduate labour market in the 1990s has come about despite these rigidities. This suggests an organic aspect to the growth, and may imply considerable scope for its further development. What else does the limited evidence tell us about graduates and SMEs? A number of cautious conclusions emerge from this review. In particular:

- There is no doubt that new graduates do find first destination employment in SMEs. However, for many of these the recruitment and selection processes of firms leave them under-utilised and with often weak prospects for continuing development. In some of these cases, they have been recruited **accidentally** into these firms with little or no reference to their qualifications – mainly into low skill jobs. Elsewhere it seems to reflect a largely immature market with distinctive processes for assessing and meeting graduate demand developed in very few smaller firms.
- The propensity for SMEs consciously to recruit new graduates seems to increase with the size of the firm. However, very little is known of sectoral characteristics and contrasts, or the selection consequences and impact of different occupational and technological contexts. The continuing lack of this evidence stems from limitations in the official data which have been long recognised. The otherwise rich annual data on graduates' first destinations has been a crucial tool in serving wider studies of the graduate labour market, but it remains virtually worthless for understanding the SME graduate labour market. What is known about SME graduate recruitment consequently comes from ad hoc research and some evaluation studies from programmes aimed at stimulating graduate recruitment in smaller firms.
- Some of this research has speculated that in many SMEs the graduate recruitment that does take place may reflect responses to new skill mixes across occupations. This seems to be particularly significant for intermediate (rather than higher level) jobs. Here, skill shortages for some auxiliary professional and intermediate level occupations are

seeing graduates recruited to substitute for the lack of external supply. These would not be seen in larger firms as 'graduate level' jobs but in SMEs there may be considerable opportunities for graduates to grow such entry level jobs into higher-level skill needs. Larger firms seem to segment graduate and non-graduate entry with the result that such opportunities for under-employed graduates are held back by rigidities in working practices.

- The limited evidence that is available suggests SMEs are often characterised by other barriers stemming mainly from management inexperience (and sometimes suspicions) of harnessing new graduate skills. Another barrier is the perceived capability gap among new graduates, with SMEs recruiting new graduates expecting higher levels of early post-entry contribution – applying similar standards as might be expected of other recruits. The widely reported difficulties of new graduate entrants rising to this challenge is a common cause of concern among SMEs recruiting new graduates. On this evidence it seems that the results of a decade of government investment in helping universities build work-readiness among under-graduates are not well received by SMEs.

This evidence is drawn almost wholly from ad hoc research studies. Over the 1990s, public policy has been showing an increasing interest in how graduate recruitment may provide an opportunity to build SME capabilities, stimulate latent demand for higher levels skills and improve performance, but this has not been matched by any initiatives to develop labour market intelligence which can guide and monitor such developments. There remains a total absence of sufficiently large-scale survey research on UK graduate demand in SMEs, and also the inability to define SMEs within the official first destination statistics covering all UK graduates. These are serious limitations to understand better how the SME graduate labour market works, and for mapping what would seem to be important differences between SMEs in their propensity to effectively use and develop graduate skills and knowledge.

Graduate contribution to SMEs

What does the research that is available tell us about how new graduates are contributing to the firms that recruit them? Most of the 29 studies selected for more detailed review have collated some organisational evidence – albeit through different approaches and intensity. This empirical base shows:

- Overall, the evidence on graduate contribution to SMEs is positive. This is despite the fact that the evidence is predominantly drawn from anecdotal and snap-shot assessments in SMEs after often short periods of graduate engagement. Few studies show graduates as being seen to fail in these firms, and on this evidence, the fears and assumed

risks that seem to hold back more SMEs from recruiting new graduates have little foundation.

- There are some common features of 'success' underpinning the contribution graduates make to SMEs, and the quality of brokerage between support agencies and SMEs in placing graduates within firms seems to be especially critical. To this can be added the thoroughness of the matching process between individuals and jobs, the specificity of managers in establishing pre-entry skill, aptitude and knowledge requirements, and also post-entry follow-up and support to graduate entrants and managers. Where these processes work well, new graduates can go beyond making a contribution through their own jobs and effectively act as catalysts and gatekeepers in firms for building wider value in graduate contribution.
- It is not clear if this generally positive contribution is conditioned by limited expectations by managers of what the new graduates can bring to the firm. Some graduate entry is to specific roles and requirements often requiring discrete skills, technical aptitudes and 'new' knowledge. It may only be in these, often highly mediated situations that new graduates act effectively as agents of technology or knowledge transfer into SMEs.
- One limitation to the contribution process – and success – is that many SMEs are still finding graduate entrants have serious skills gaps for their needs. Robust data on the capability gaps are limited, but the SMEs experience commonly stresses the importance of generic and transferable skills in new graduate entrants. Some studies have pointed to an observed lack of initiative, weak inter-personal skills, low levels of business awareness, and poor team working skills. The evidence does not tell us if this is accounted for mainly by supply factors – graduates commonly lacking these skills and qualities on recruitment, or a demand effect stemming from inappropriate matching of entrants to jobs, ill-framed or unrealistic expectations of managers.
- There is little evidence – outside of the TCS Scheme – of new graduates being recruited to SMEs consciously as agents of technological (or new knowledge) transfer. On this evidence, market forces alone seem to be insufficient to ensure that risk adverse SMEs will be calling on new graduates as knowledge based change agents. As the TCS evaluation evidence testifies, systematic and ongoing mediation will continue to be needed if more SMEs are to profit from this potential.
- Elsewhere, the potential to SMEs of new graduate entrants seems to be related to a more generalist value of bringing in young and intelligent minds into SMEs. This seems to be limited to firms where leadership and management culture means they more open to new ideas and ways of working. In some the contribution seems to be an indirect enabling effect – providing the time for senior managers to reflect on – and enhance – business performance.

Although generally encouraging, the quality of the evidence emerging from this review will disappoint those looking for clear evidence to encourage more SMEs to recruit new graduates. It is difficult to escape the conclusion that the studies reviewed here generate anything more than a shallow understanding of the relationship between graduate employment and SME business performance. There is very little quantification with which to measure the quality of the impact, and few studies set the experiences of SMEs against conditioning factors or provide for comparative or control group analysis. We also know very little about crucial contrasts within the SME constituency – even on such basic issues as sector and size of firms, and virtually nothing from these studies of the influence of management styles or organisational cultures.

The empirical evidence may be weak, but it does provide sufficient common ground to start to speculate on how SMEs relate to graduate recruit and utilisation, and how this might condition the contribution they make to the firm. A typology is proposed of six recruitment and organisational contexts which will embrace most SME contexts:

- SMEs where new graduate recruitment stems from an imposed **external requirement** or convention;
- Those where managers have **established capability building** (in higher level skills) as a strategic priority;
- Knowledge and other smaller businesses recruiting new graduates for specific **technology transfer** or related development activities;
- SMEs recruiting graduates below their skills levels as substitution for **intermediate level skills gaps**;
- **Experimental recruitment** of new graduates by SMEs – those awakening to the potential of the graduate labour market.;
- **Accidental recruitment** of new graduates – generally involving lower level jobs in SMEs.

These are stereotypes of what will be more customised process and requirements in individual firms. The typology is set out in more detail in Figure 1 in terms of the rationale likely to underpin graduate recruitment, and the illustrative sectors of activities likely to be involved.

More research evidence would enable this to be embellished and perhaps to make a distinction between sectors and occupations likely to be covered. What is clear is that these ‘types’ are unlikely to be mutually exclusive and graduate recruitment among more mature SMEs may respond to two or more types as a natural process in meeting its skilled labour needs.

Figure 1 A typology for SME engagement

Type of SME graduate recruitment	SME rationale	Conviction about value of new graduate recruitment	Typical sectors/activities
External requirement	Recruitment to professional level posts with accreditation normally from post graduate or related study.	High	Chartered accountants; Chartered/professional engineers; Legal specialists/lawyers; Personnel specialists; Veterinary surgeons; etc.
Established capability building	Recruitment of new graduates as strategic response to upskilling workforce – or parts of it.	High	Knowledge industries and others with or developing, high skills equilibrium as competitive strategy.
Technology transfer	Recruitment to new/emerging knowledge areas, or to specific development needs in high skills areas for business improvement.	High or moderate	ICT/database enhancement/ e-business development; Integration of novel technological processes; New product/service development outside existing SME skill mix; etc.
Substitution for intermediate level skills gaps	Inability to recruit, or weak competitiveness, for intermediate level skills needed by SME.	Moderate or low	Technician level posts; Auxiliary professional level vacancies; Intermediate level administrative/ customer service/ sales support; etc.
Experimental recruitment (awakening SMEs)	Novel or trial recruitment (or work placement) or new graduates. Cautious response to perceived high risk recruitment/ development.	Low or nil	Miscellaneous.
Accidental recruitment	No rationale – new graduates re-selected for jobs with no reference to their qualification level.	Nil	Recruitment mainly to lower level personal service and clerical jobs.

The typology includes accidental recruitment to cover situations where a new graduate is selected for a lower level vacancy with no reference to their qualification level. However, from a public policy perspective it is arguable if such recruitment should be included in any modelling of the SME graduate labour market, since what evidence does exist suggests that the circumstances of their recruitment mean graduates here will have little scope for growing these jobs into higher level activities or beyond a

minimal contribution to the firm. Effective public policy action to develop effective recruitment in the other five categories might also see accidental recruitment diminishing.

The typology focuses on SMEs engaged in, or awakening to, involvement in the labour market. It assumes – conversely – that for some SMEs, engagement will not be a rational response to their skill needs or market circumstances. In such companies it is questionable if graduates have much to contribute in terms of enhancing business performance.

Policy challenges and implications

Public policy has recognised the value of expanding SME demand for new graduates. This is against a background of rapidly rising graduate supply over the 1990s, higher levels of graduate under-employment, and changes which have seen demand for dedicated graduate entry to larger recruiters falling off as a proportion of graduate first destinations.

SMEs are consequently seen by policy makers as a crucial area for tapping latent demand to provide better early career and earnings opportunities for graduates. Failure to do so may see rising scepticism about the value of investment in a university education to individuals, and this becoming a serious barrier to governments ambitious targets for wider participation in higher education. Policy makers also see greater SME involvement as much more than soaking up any surplus graduate supply not wanted by larger firms. The policy rationale recognises that more new graduates, better utilised by SMEs, can make an important contribution to improved performance and competitiveness in these firms through improved adaptation, technology transfer and stimulating change management.

Government initiatives, consequently, have for some time been aiming to boost new graduate recruitment by SMEs. Some of these initiatives have been very long established such as the TCS Scheme, but public policy has also supported a plethora of short term funding streams stimulating graduate recruitment by smaller businesses. Challenge funding routes have become a particular feature of this in the second half of the 1990s. While, this has seen considerable support for experimentation by individual universities, local and sectoral collaborations – this review has shown this to have been poorly supported by information or intelligence on the evolving SME graduate labour market.

Beyond TCS, these publicly funded initiatives and constituent activities have produced plenty of mainly low-level evidence of SME involvement and attributed benefit, but little that is sufficiently broadly based or empirically sound. In short, these efforts may have produced some localised and mainly short-term experience, but we see little as having yet been learnt from this for national policy. This has been compounded by the scale and quality of project based research and evaluation stemming from most local and sectoral initiatives supported by publicly funded programmes funds in

this area. With the notable exception of TCS evaluations, cross-project programme evaluations have tended to emphasise contractual compliance and project processes – and have not added greatly to cross-project empirical evidence, and an understanding of good practice and success in SMEs.

It would seem that public policy goals of better engaging new graduates in SMEs are timely, and founded on solid **supply** possibilities, but have been poorly supported by foundation intelligence – and little robust evidence of subsequent project effectiveness. To this can be added the lack of sound **demand** evidence on SME needs and context, and lessons to be learnt about this for understanding impact. Other than for TCS, the considerable public investment in the last decade to encourage innovation and experimentation in boosting demand in the graduate labour market for SMEs, has provided only partial evidence that such interventions are well matched to SME needs, and contributing to business performance.

Towards a research agenda

If public policy has effectively been running blind on graduate contribution to SMEs, an important starting point for policy makers must be in remedying the lack of supply and demand evidence. The need for this is emphasised by government commitments more generally to evidence based policy development. Without a significant investment in large-scale primary research with SMEs, and longitudinal studies, these crucial evidence gaps seem set to continue to hold back any policy developments and effective innovations.

This review has shown that we cannot look to better use of current research or information sources to start to fill these gaps. Although such research provides a useful backcloth, more effort is needed among those responsible for official data and from researchers within the graduate labour market to generate the necessary evidence. There are two priorities in this:

- Information about the **SME graduate labour market**, its underpinning processes and diversity, and how it relates to wider changes taking place in the economy in graduate supply and demand; and
- Comparative evidence of the added-value and wider **contributions that new graduates make to SMEs** in different labour market and organisation circumstances, and encompassing different contexts (and expectations) of graduate entry to SMEs.

A number of specific actions are proposed in both areas. The intelligence and evidence that could be generated from such responses could go a long way to addressing what must be seen as two decades of neglect of the SME dimension within an increasingly complex and volatile graduate labour market. It will also provide better for the foundations on which any further policy initiatives to adjust the rising supply of graduates to changing

patterns of need – and the latent opportunities which are presented in some SMEs.

Overview

SMEs are clearly playing an increasingly important role in the graduate labour market. Belatedly they are attracting more interest from researchers, but as yet the evidence base on patterns of recruitment and deployment, let alone graduate contribution and impact within SMEs, is weak and too often insubstantive. Yet there is enough common ground in the various studies reviewed here to suggest that there is genuine value to both SME and graduate, and considerable scope to enhance this as strand on public policy in higher education and smaller business competitiveness.

Policy makers responding to this challenge are faced with a difficult choice. Do they pursue an **organic** approach and essentially leave developments to wider supply trends in the graduate labour market? This would anticipate more and more new graduates going to SMEs because of the lack of traditional graduate level employment – often choosing under-employment over unemployment. Or should policy makers look for an enabling approach within wider policies aimed at building SME capabilities and competitiveness. This would be based on an assumption that some further intervention is needed to help more constructive engagement – and more SMEs to capitalise on this potential.

Further use of public funds may be seen by some as of questionable value against a background of other pressures on the public purse and where graduates are finding their own way into SMEs – and bringing some value to those firms and themselves. This would be a narrow and short-term view which would not support other aspects of public policy in higher education very well. In particular, it would result in extensive under-employment of many of these individuals – an issue which may in turn have consequences for the wider graduate labour market, with potential undergraduates coming to question the value of the substantial investment now needed from individuals and their families to fund a first degree education. Policy makers will also recognise that the current processes also lead to what is probably sub-optimal value for SMEs – those who do recruit graduates but make ineffective use of them, and others who might undertake such recruitment if conditions were more favourable to their deployment in the firm.

If these are issues that policy makers wish to continue to be engaged with, they need much better information and intelligence to shape future policy responses. The research and development activity of the past six years has largely failed to provide this. A new impetus is needed for which we have proposed some specific developments. If this is not tackled much more effectively than in the past, policy makers will carry on ‘running blind’ in rising to the challenges presented in stimulating a stronger relationship between supply and demand in the SME graduate labour market.

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