Second OECD Conference of Ministers Responsible for Small and Medium-sized Enterprises (SMEs)



PROMOTING ENTREPRENEURSHIP AND INNOVATIVE SMEs IN A GLOBAL ECONOMY

TOWARDS A MORE RESPONSIBLE AND INCLUSIVE GLOBALISATION

EXECUTIVE SUMMARY
OF THE BACKGROUND REPORTS

OECD

Second OECD Conference of Ministers responsible for Small and Medium-sized Enterprises (SMEs)

Promoting Entrepreneurship and Innovative SMEs in a Global Economy

Towards a More Responsible and Inclusive Globalisation

Executive Summary of the Background Reports

Istanbul, Turkey
3-5 June 2004

OECD

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

Pursuant to Article 1 of the Convention signed in Paris on 14th December 1960, and which came into force on 30th September 1961, the Organisation for Economic Co-operation and Development (OECD) shall promote policies designed:

- to achieve the highest sustainable economic growth and employment and a rising standard of living in member countries, while maintaining financial stability, and thus to contribute to the development of the world economy;
- to contribute to sound economic expansion in member as well as non-member countries in the process of economic development; and
- to contribute to the expansion of world trade on a multilateral, non-discriminatory basis in accordance with international obligations.

The original member countries of the OECD are Austria, Belgium, Canada, Denmark, France, Germany, Greece, Iceland, Ireland, Italy, Luxembourg, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom and the United States. The following countries became members subsequently through accession at the dates indicated hereafter: Japan (28th April 1964), Finland (28th January 1969), Australia (7th June 1971), New Zealand (29th May 1973), Mexico (18th May 1994), the Czech Republic (21st December 1995), Hungary (7th May 1996), Poland (22nd November 1996), Korea (12th December 1996) and the Slovak Republic (14th December 2000). The Commission of the European Communities takes part in the work of the OECD (Article 13 of the OECD Convention).

Publié en français sous le titre :

Promouvoir l'entreprenariat et les PME innovantes dans une économie mondialisée

© OECD 2004

Permission to reproduce a portion of this work for non-commercial purposes or classroom use should be obtained through the Centre français d'exploitation du droit de copie (CFC), 20, rue des Grands-Augustins, 75006 Paris, France, tel. (33-1) 44 07 47 70, fax (33-1) 46 34 67 19, for every country except the United States. In the United States permission should be obtained through the Copyright Clearance Center, Customer Service, (508)750-8400, 222 Rosewood Drive, Danvers, MA 01923 USA, or CCC Online: *www.copyright.com*. All other applications for permission to reproduce or translate all or part of this book should be made to OECD Publications, 2, rue André-Pascal, 75775 Paris Cedex 16, France.

Table of Contents

Preface 5
Introduction 7
Entrepreneurship and SME Innovation 8
Tools for SME Innovation 17
SMEs in the Global Economy 25
Enhancing the Role of SMEs for Development 32
Evaluation of SME Policies and Programmes 37
Towards More Systematic Statistical Measurement of SME Behaviour 40

© OECD 2004

Preface

At the first OECD Conference for Ministers Responsible for SMEs, hosted by the Italian government in Bologna, Italy, in June 2000, Ministers from nearly 50 member and non-member economies adopted the "Bologna Charter for SME Policies". They envisaged the Bologna Conference as the start of a policy dialogue among OECD member countries and non-member economies and that it would be followed up by a continuous monitoring of progress with the implementation of the Bologna Charter. This dialogue and monitoring have become known as the "OECD Bologna Process". The second OECD Conference for Ministers Responsible for SMEs, hosted by the Turkish Ministry for Industry and Trade, envisaged by Ministers at Bologna, provides an occasion to assess the impact on SMEs of new developments relating to globalisation.

This report is an executive summary of background reports for the Istanbul Conference and sets out some policy messages and recommendations that have emerged from preparatory work in the OECD Working Party for SMEs and Entrepreneurship. The wide variation in stages of economic development, institutional arrangements and political context across the economies participating in the Bologna Process, now more than 80, means that not all parts of specific policies and programmes are appropriate for all participants. The messages and recommendations outlined below provide material from which governments may choose to draw in promoting innovative SMEs in the global economy. In broad terms, these policy messages and recommendations elaborate on the themes developed in the Bologna Charter. Ministers will consider these and other recommendations in their deliberations at the Istanbul conference.

This report is published on the responsibility of the Secretary-General of the OECD. Views expressed are those of the authors of the background reports which are summarized here and do not necessarily reflect those of the Organisation or its member governments. The full background reports are available in English and French on the Istanbul Ministerial Conference Web site, www.oecd-istanbul.sme2004.org, *and on the OECD Web site at* www.oecd.org/sti/smes.

© OECD 2004

Introduction

Ministers have the opportunity to assess priorities for SME policies…

The second OECD Conference for Ministers Responsible for SMEs brings together 30 OECD countries and more than 50 non-member economies at Ministerial level to exchange views on "Promoting Entrepreneurship and Innovative SMEs in a Global Economy". It offers Ministers the opportunity to take stock of the progress that has been achieved in implementing the Bologna Charter, adopted at the Bologna Conference in June 2000. They may also assess policy priorities for realizing the potential contribution that small and medium-sized enterprises (SMEs), especially innovative ones, can make to better economic performance, notably in terms of jobs and productivity.

… and to promote dynamic and innovative SMEs in a global context.

A major focus of the conference is on more dynamic SMEs. These develop new ideas, processes and technologies in innovative ways to prosper and grow if the business environment in which they operate permits this to happen. Some of the issues relate to policies that affect the whole economy and hence the general business environment in which SMEs must operate. Other issues relate to policies and programmes more specifically oriented to supporting enterprise creation, fostering entrepreneurship and facilitating the growth and prosperity of SMEs once established. Still others relate to mobilising human resources, in particular women, to realise their full economic potential.[1] A second major focus of the conference is the continuing process of international economic integration and ways to encourage

1. This work is an important part of the follow-up to the OECD Growth Project (*The New Economy: Beyond the Hype,* OECD, Paris, 2001) which underlines the need for micro-policy reforms to enhance innovation and productivity in knowledge-based economies. These relate in particular to the four main micro-drivers of growth: entrepreneurship, innovation and technology diffusion, information and communications technologies, and human capital.

© OECD 2004

SMEs, especially in developing economies, to take best advantage of this process.

This report summarises the background reports prepared for this conference.

The main messages emerging from the preparatory work for the conference incorporated in a series of background reports, are synthesised here. The first four sections below summarise the material relevant to the four main Ministerial workshops:

- Entrepreneurship and SME innovation.
- Tools for SME innovation.
- SMEs in the global economy.
- Enhancing the role of SMEs for development.

The final two sections summarise work relating to two sets of issues which cut across many of the other conference themes and which are fundamental to improving SME policy formulation and implementation:

- Evaluation of SME policies and programmes.
- Towards more systematic measurement of SME behaviour.

Key policy recommendations from the background reports are provided in boxes throughout the text.

Entrepreneurship and SME Innovation

Fostering entrepreneurship and firm creation

Entrepreneurship and firm creation generate jobs,…

The creation of new businesses and the contraction or exit of less productive firms are key elements in the dynamism of modern economies. New firms attract resources to new activities, and when they prosper and are able to grow rapidly, they generate significant numbers of new jobs. Empirical work at the OECD indicates that entry of new firms in most countries is similar to exit of existing firms, and perhaps surprisingly, there do not appear to be great differences in entry and exit rates across countries. On the other hand, young firms seem likely to grow more rapidly in some countries than in others. This points to the importance of ensuring that the business environment is conducive to rapid expansion of young, especially

© OECD 2004

innovative firms once they establish themselves. There is also considerable variation across industries. In particular, entry and exit rates have been exceptionally high in recent years in ICT-related service sectors and low in more mature industries.

… contribute to growth and productivity…

New firms must often have an innovative edge on their competition in order to survive, particularly in younger and high-technology industries where competitive pressure and firm churning are high. As such, they are often the source of new processes or products and contribute to productivity improvements in the economy as a whole. While in the short term cost reductions and increased competitive pressure can lead to job shakeouts, empirical work at the OECD indicates that the firm entry and exit that this entails facilitates the shift in resources from old and less productive uses to more productive ones. In the longer term, the resulting productivity increases are the basis for higher economic growth and rising living standards.

… and provide social benefits.

Governments have increasingly recognised the contribution that "social entrepreneurship" can make to reducing poverty and empowering disadvantaged groups. Many countries operate specialised entrepreneurship schemes to assist target population groups. Such schemes need to be designed carefully and adapted to be consistent with mainstream support programmes for these target populations.

Policies should ensure a business environment conducive to entrepreneurship and enterprise creation.

Creating a business environment conducive to entrepreneurship and enterprise creation in which innovative young firms have scope to expand rapidly once they have established themselves requires a broad range of mutually reinforcing and supportive policies. Many of these affect the economy as a whole but impinge importantly on potential entrepreneurs and SMEs. These include sound fiscal and monetary policies, which are essential to provide a basis for a stable macroeconomic environment. They also include structural policies that determine the overall economic framework in which the business sector operates, such as those affecting labour markets, tax design, competition, financial markets and bankruptcy laws. The

© OECD 2004

way these structural policies affect enterprise creation and small businesses should be taken into account in their formulation stages.

Regulatory and administrative burdens on small businesses should be kept low.

There is considerable evidence that regulatory and administrative burdens can impinge adversely on entrepreneurial activity. Legal entry barriers should obviously be avoided unless their benefits are very clear, since (according to a World Bank study[2]) they appear to be associated with less private investment, higher consumer prices and greater corruption. Employment regulation, which the World Bank finds is generally more flexible in advanced countries than in developing economies, limits management flexibility and leads to smaller firm size and less research and development as well as less investment in technology.

Barriers to exit may also discourage entry, since exit and entry rates tend empirically to be closely related. Since firm entry involves considerable risk, with survival chances that are difficult to assess, institutions that make exit very costly discourage entry. OECD work suggests, for example, that entry rates tend to be lower the longer creditors have claims on bankrupts' assets. Measures such as regulatory impact assessments and administrative simplification procedures can help to address some of these problems. However, the best approach to minimising regulatory and administrative burdens is to make this part of a broader regulatory quality agenda in which administrative simplification is an ongoing process whereby all regulations are continuously revised and simplified.

Education and training can promote an entrepreneurial culture.

Culture is increasingly acknowledged as a factor which can contribute to building an entrepreneurial society as it is an important determinant of career preferences and helps shape attitudes to risk-taking and reward. Developing an entrepreneurial culture and fostering entrepreneurial attitudes and values has moved high on government agendas. Education and training (including lifelong training) in entrepreneurship and creativity are the preferred

2. World Bank, *Doing Business in 2004: Understanding Regulation*, Washington, DC, 2003.

© OECD 2004

instruments for encouraging entrepreneurial behaviour in societies, and evidence suggests that such programmes can have an impact on entrepreneurial activity and enterprise performance. However, in spite of the numerous initiatives launched and implemented in recent years, a number of shortcomings and problems characterise this domain: entrepreneurship is not sufficiently integrated into educational curricula or integrated into national long-term economic strategy and planning; a lack of public resources has resulted in limited teaching and research capability in this field; there is a need to improve co-ordination among government agencies when designing and implementing initiatives; there is a need for a broader acceptance of the concept of education and training for entrepreneurship; and both more data and more evaluation and assessment of initiatives taken are needed.

The local dimension must be taken into account.

Entrepreneurship and SME policies also have an important local dimension. Indeed, facilitating increasing rates of enterprise creation is an almost universal concern for local authorities who seek to accelerate development or reverse decline in localities, whether disadvantaged or prosperous. Programmes aimed at reducing social distress and unemployment, including chronic unemployment, have been implemented in many countries. New enterprises can procure a range of benefits that contribute to local development, including: rises in employment and incomes; enhanced provision of services for consumers and businesses; and possibly, demonstration and motivational effects. Determinants of rates of enterprise creation at the local level include demographics, unemployment, wealth, the educational and occupational profile of the workforce, the prevalence of other small firms and infrastructure endowment.

Programmes and support policies should be systematically evaluated…

Governments often need to go beyond provision of the framework conditions that influence the business environment to address policy and market failures that dampen entrepreneurial activity and limit the scope for innovative small firms to grow. In practice, this requires programmes and support policies for small enterprises which may be complex and involve scarce resources. Many

© OECD 2004

of these programmes and policies are designed and implemented at the local level. To ensure that these programmes are cost effective and well targeted, it is important that they are systematically reviewed, assessed and evaluated. The issues that are involved are considered further below.

Key policy recommendations

- **Ensure stable macroeconomic and framework conditions to underpin the entrepreneurial business environment.** Policy design in areas such as competition, the regulatory framework, the tax system, labour markets, financial markets and bankruptcy laws should take account of the way these areas impinge on SMEs and innovation in knowledge-based economies.
- **Ensure the reduction and simplification of administrative regulations and costs which fall disproportionately on SMEs.** Take account of SME views during the regulatory process; require regulatory agencies to prepare Small Business Impact Statements; establish one-stop shops for regulatory information and transactions; and promote the use of e-government tools.
- **Promote an entrepreneurial society and entrepreneurial culture, in particular through education and training.** Integrate entrepreneurship at all levels of the formal education system and ensure access to information, skills and expertise relating to entrepreneurship via "lifelong learning" programmes for the adult population. Promote the diffusion of training programmes by stimulating the private market's supply of such services and providing hands-on focused courses.
- **Integrate the local development dimension into the promotion of entrepreneurship.** The roles of sub-national authorities in the promotion of entrepreneurship are of paramount importance and should be defined and co-ordinated with central governments, as appropriate for each country.
- **Ensure that programmes in support of SMEs and entrepreneurship are realistic in terms of cost and are designed to deliver measurable results**. An evaluation culture should be developed to ensure that programmes are systematically monitored and assessed for their performance in achieving objectives and for their cost-effectiveness.
- **Strengthen the factual and analytical basis for policymaking so that policy makers can take decisions in an informed manner based on empirical evidence.** A strengthened statistical base will permit cross-country comparative analysis and policy-relevant longitudinal studies. An internationally comparable set of indicators should be developed for monitoring the level of entrepreneurial activity and the entrepreneurial environment in each country.

© OECD 2004

… and based on evidence to the degree that this is possible.

It would be highly desirable if policy decisions could be made in an informed manner based on empirical evidence. Unfortunately, the factual and analytical base for such decisions is weak. Developing such a base will require strengthening the existing empirical foundation, in terms of data and statistics, to permit policy-relevant empirical analytical work to be carried out. The issues that are involved are considered further below.

Fostering women's entrepreneurship

Women's entrepreneurship is potentially an important source of growth…

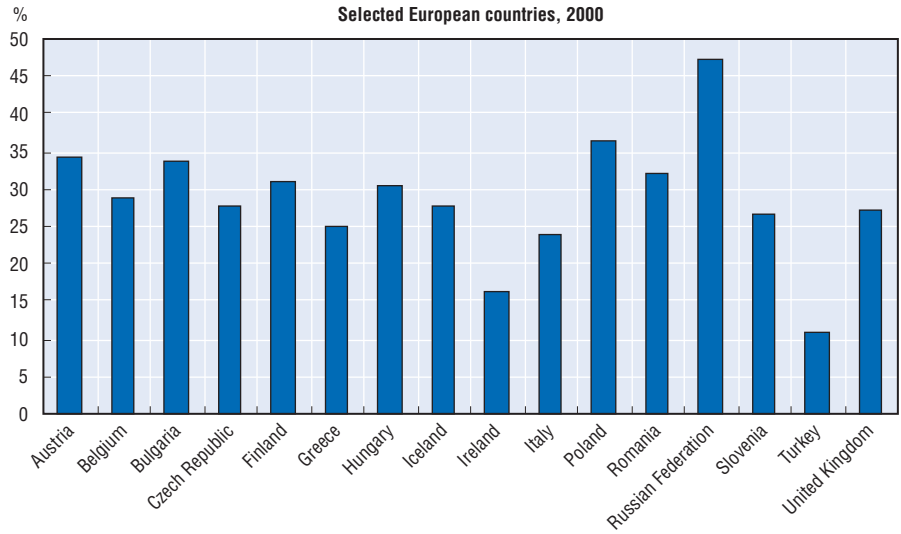
Women's entrepreneurship has increasingly become recognised as an important source of employment and potential growth. Indeed, data are very scarce, but estimates indicate that there are more than 10 million self-employed women in Europe (both European Union countries and others). In the United States 6.4 million self-employed women provide employment for 9.2 million people. Using the US ratio between number of employees and self-employment, it is estimated that the self-employed women in surveyed European countries might employ around 15 million persons. Indeed, self-employment represents one of the most important job options for women, especially for women in developing economies. Furthermore, as women behave differently from men, their entrepreneurship provides society with different, and often innovative, solutions to management and organisational problems as well as to the exploitation of new opportunities.

… but this source is largely untapped.

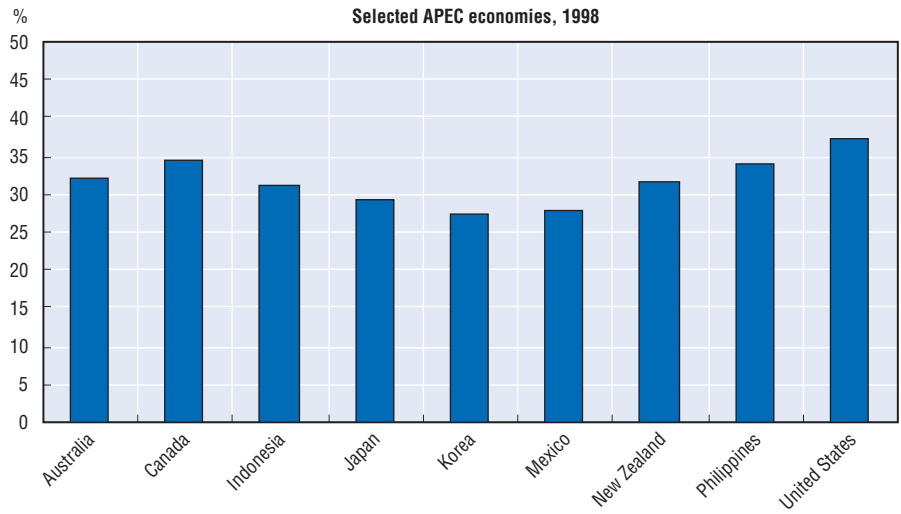
However, women still represent a clear minority of entrepreneurs nearly everywhere (Figure 1). Furthermore, they generally choose to start and manage firms in different industries than those chosen by men. These industries, primarily retail distribution, education and other service industries, are often perceived as contributing less to economic performance and growth than manufacturing and higher technology activities.Overall there appear to be market failures and impediments which operate to limit the extent to which women become entrepreneurs and their prospects for success.

© OECD 2004

Figure 1. **Female employers and own-account workers**
Percentage of total employers and own-account workers



Source: United Nations Economic Commission for Europe, Gender Statistic Database.



Source: B.J. Chun, *Women Entrepreneurs in SMEs in the APEC Region*, APEC, Singapore, 1999.

© OECD 2004

The empirical basis for informed policy design needs to be improved…

Reliable data and analysis relating to women's entrepreneurship are scarce and provide little empirical basis for policy design. Definitional issues complicate data collection, and some national systems prohibit statistics at the individual level, making gender-specific analyses impossible. Even in those few countries where such data are available, important information on development over time (panel data) and for the whole population are lacking. As regards analysis, longitudinal studies are needed to understand survival and growth among entrepreneurs (men and women), as well as time of entry and exit from business. They are especially important for women entrepreneurs, as the obstacles and challenges they face appear to change in the course of their involvement in the entrepreneurial process. More precisely, women face different obstacles at different stages in this process (*e.g.* opportunity identification, opportunity exploitation and fund-raising). Depending on the nature of those obstacles, only certain types of women will enter into business and succeed. Currently, the general picture is still based on cross-sectional samples, even if both the scope and the breadth of available data have improved during the last few years.

… and obstacles that need to be addressed can be identified.

The scope for women to realise their potential as entrepreneurs depends on both the status and role of women in society and the forces operating within society which influence entrepreneurship. These relate to the political context, institutional framework, family policies, market forces and the suitability of particular individuals, in terms of temperament and qualifications to assume entrepreneurial roles. Specific obstacles to greater entrepreneurship by women include inappropriate educational background, lack of role models, the gendering of entrepreneurship, weak social status, competing demands on time – notably associated with family responsibilities – and limited access to finance.

Progress can be made by removing obstacles to female participation in the labour force,…

An important area where progress can be made is in removing obstacles to female participation in the labour force. Family-friendly policies, notably as regards child care, parental leave arrangements and other child-related financial support, can have a positive effect on women's employment generally and entrepreneurial activities more

© OECD 2004

specifically. Such policies are part of the wider package of economic and social arrangements in any economy and there is no simple relationship between such policies and observed behaviour across countries. Economies in transition and the Nordic countries, for example, have some of the best provisions for working women but do not stand out as having high levels of female entrepreneurship. However, family-friendly policies allow more flexibility to manage time in order to combine family commitments and career.

… incorporating a women's dimension in SME programmes at the design stage,…

Policies and programmes are too often "menstreamed", failing to take account of the specific needs of women entrepreneurs and the obstacles to their entrepreneurial activity and success. To ensure that policies and programmes to support SMEs and entrepreneurship contribute more effectively to encouraging more equal opportunity between men and women, these should incorporate a women's dimension at the design stage. As with all assistance and support policies and programmes, these should be evaluated regularly to identify ways to improve the effectiveness, both in terms of impact and participation of target beneficiaries, of those that should be retained.

… and ensuring that women entrepreneurs themselves are heard.

The most effective way to ensure that a woman's dimension is incorporated into policies and programmes is to include it at the formulation stage. There are various ways to do this, such as making consultations with associations representing women entrepreneurs part of the process. Another approach, which has had considerable success in the United States, and is likely to be tried soon in Canada, is the creation of a government office of business ownership, which would itself have programme responsibilities for providing information and support to women entrepreneurs.

Support for women's entrepreneurship should not be confined to government policies and programmes. Women entrepreneurs and associations representing them have much to teach each other. Networks should be encouraged both within economies and internationally to support the diffusion of knowledge and experience within the private sector to facilitate entrepreneurial endeavours by women.

© OECD 2004

Key policy recommendations

- **Increase the ability of women to participate in the labour force by ensuring the availability of affordable child care and equal treatment in the workplace**. More generally, improving the position of women in society and promoting entrepreneurship generally will have benefits in terms of women's entrepreneurship.
- **Listen to the voice of women entrepreneurs.** The creation of government offices for women's business ownership is one way to facilitate this. Such offices could have programme responsibilities such as providing women's business centres, organising information seminars and meetings and/or providing web-based information to those wanting to start and grow a business.
- **Incorporate a women's entrepreneurial dimension in the formulation of all SME-related policies**. This can be done by ensuring that the impact on women's entrepreneurship is taken into account at the design stage.
- **Promote the development of women entrepreneur networks.** These are major sources of knowledge about women's entrepreneurship and valuable tools for its development and promotion. Co-operation and partnerships between national and international networks can facilitate entrepreneurial endeavours by women in a global economy.
- **Periodically evaluate the impact of any SME-related policies on the success of women-owned businesses and the extent to which such businesses take advantage of them.** The objective should be to identify ways to improve the effectiveness of those that should be retained. Good practices that are identified in this way should be disseminated and shared internationally.
- **Improve the factual and analytical underpinnings of our understanding of the role of women entrepreneurs in the economy.** This requires strengthening the statistical basis for carrying out gender-related cross-country comparative analyses and longitudinal studies of the impact of important developments and policies, especially over time.

Tools for SME Innovation

Financing for innovative SMEs

Access to risk capital is a major obstacle to SME expansion.

High administrative costs and uncertainties about future performance often make financing SMEs unattractive to potential funding sources in the private sector. These problems are amplified for innovative SMEs seeking to expand, making it difficult to write contracts that are mutually agreeable to investors and SMEs looking for risk

© OECD 2004

capital. First, the returns to innovative activities are highly uncertain and often skewed. Second, entrepreneurs may possess more information about the nature and characteristics of their products and processes than potential investors. Third, innovative activities are usually intangible so that it is difficult to assess their monetary value before they become commercially successful. This has led to a proliferation of government programmes to close perceived financing gaps faced by innovative SMEs.

The main problems relate to skills and expertise,…

Addressing these problems requires finding ways to fuse entrepreneurship and finance. This involves ensuring the availability of entrepreneurial, technical and managerial expertise to the providers of finance and engaging investors actively in the development of the firm. This requires a class of intermediaries capable of assessing the quality of applicants, undertaking due diligence and monitoring prospects and performance, and providing management assistance to SMEs. The desirability of close contacts between suppliers of funds and those requiring finance also points to the importance of regional and local initiatives, support of business angel networks and business incubators.

… and not to a lack of funds.

This has important policy implications. First, it means that simply providing money to innovative SMEs is unlikely to be successful. There is likely to be a significant amount of waste and low returns while entrepreneurs will probably continue to complain that they cannot raise finance. Second, the features commonly associated with well-developed financial markets, namely efficient stock markets and banking systems, while necessary, may not be sufficient. Third, the traditional tools of government policy, such as taxation, subsidies, regulation and the creation of new government institutions are unlikely to be appropriate.

Public financial support should focus on early stages and leveraging private financing.

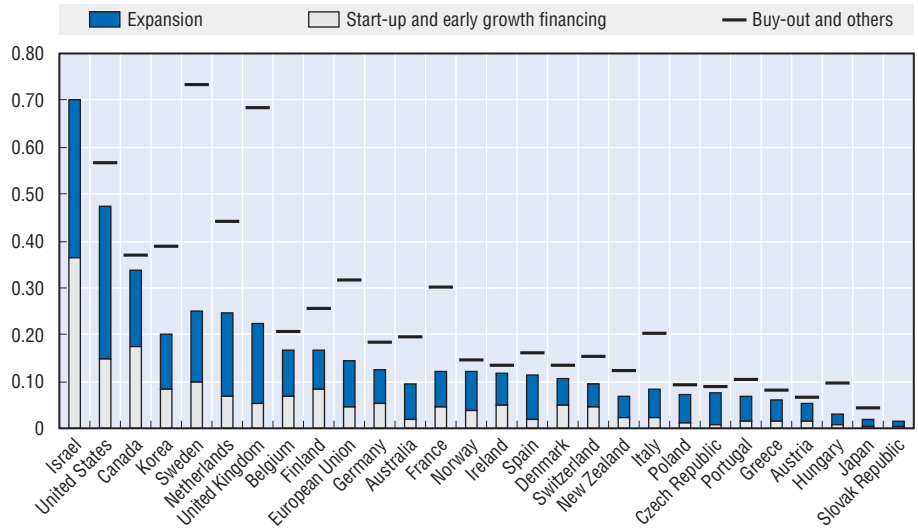
Modest public support may be warranted where private financial markets capable of providing risk capital to SMEs seeking to expand are not yet established. For example, even the well-developed venture capital market in the United States has benefited from federal funding for many years. Where such support is provided, it should be targeted at the early stages of SME development, where difficulties

© OECD 2004

accessing finance are most acute (Figure 2). It should also be managed by the private sector and structured to leverage private sources of financing. The experience of several countries with small business investment companies may offer useful guidance.

Figure 2. **Venture capital investment, 1999-2002**

Percentage of GDP



Note: 1998-2001 for Australia, Japan, Korea and New Zealand. The definition of private equity/venture capital tends to vary by country.

Source: OECD Venture Capital Database, 2003.

International capital markets have a role to play.

The need for proximity and close interaction between investors and entrepreneurs at early stages of firm development should not lead to neglect of the contribution international capital markets can make. Where capital markets are not well-developed, especially in developing countries, accessing finance and tapping expertise internationally can minimise the need to create new institutions.

Regulations should be designed to minimise negative impacts on provision of risk finance.

Regulations and supervisor arrangements designed to safeguard the soundness of financial systems can affect the provision of risk finance to SMEs. Such regulations should be subject to cost-benefit assessments before they are implemented and their impact should be monitored subsequently. In this regard the impact of the forthcoming

© OECD 2004

Basle II agreement on innovative SMEs and on SMEs in general in developing countries should be the object of further research and should be kept under review. Where current regulations restrict institutional investors from providing risk capital or limit international investment in venture capital they should be reviewed with a view to easing or eliminating them.

Key policy recommendations

- **Concentrate policies for promoting availability of risk capital to innovative SMEs mainly on early stages of the financing of the firm.** Public sector funds could be used to leverage private sector financing in order to reduce the financing gap. Where countries believe that such support is warranted, they could draw on the experience of several countries with small business investment companies.
- **Recognise the need for proximity between suppliers of funds and those who require finance, particularly for small-scale investment.** Regional and local equity initiatives (*e.g.* regional funds) are therefore appropriate for such types of investment. Such equity programmes should be created in parallel with the development and support of regional and local business angel networks as well as business incubators.
- **Increase the managerial and technical expertise of intermediaries whose role is to evaluate and monitor companies.** This requires the development of a class of intermediaries who focus on reducing the asymmetry of information between entrepreneurs and providers of finance through *a)* assessing the quality of applicants; *b)* undertaking due diligence; *c)* exercising corporate governance and monitoring; and *d)* assisting SMEs as they use the funds.
- **Facilitate international transfer of institutional infrastructure and expertise.** Consideration should be given to ways in which countries with less well developed capital markets can draw on the expertise of countries with well developed stock markets. Access to liquid international stock markets and an investment community that has expertise in venture capital-backed initial public offerings avoids the need to create new institutions.
- **Subject new regulations which could adversely affect the provision of risk finance to cost-benefit tests of their likely effect before implementation and monitor their subsequent impact.** Current regulations that create restrictions on institutional investors to invest in risk capital or barriers to flows of foreign venture capital funds should be reviewed with a view to reducing, easing or eliminating them.
- **Encourage, in conjunction with business and accounting bodies, small business to recognise, measure, and report intangible assets** (ICT skills, organisation, software and networks, intellectual property rights) so that new and small firm assets can be managed more effectively and more reliably valued by capital markets and investors.

© OECD 2004

Recognition and measurement of intangible assets should be improved.

Finally, intangible assets such as intellectual property are important elements of the growth potential of innovative start-ups and SMEs, especially those that are technology-oriented. Better methods of recognising, measuring and reporting these assets can facilitate more accurate evaluation by financial markets of SMEs, particularly those potentially in the early stages of growth, and improve their prospects for raising necessary risk capital.

Networks, partnerships, clusters and intellectual property rights

SMEs must draw on external sources of information, knowledge and technology.

Even more than larger firms, SMEs need to access external sources of information, knowledge, know-how and technology in order to build their own innovative capability and to reach their markets. They can only partly secure such access through markets for goods, services, intellectual property rights and human resources. They must also participate in networks, particularly those that nurture the tacit knowledge and other non-tradable competences that are critical for pursuing innovation-based competitive strategies.

Networks linking innovative firms should be encouraged.

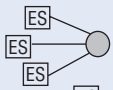
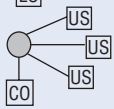
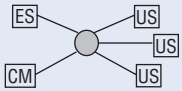
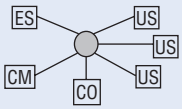
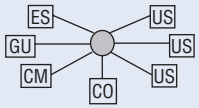
Different types of SMEs have different needs and the appropriate networking strategy will vary accordingly (Figure 3). However, all must be connected to the most prolific sources of new knowledge and expertise, either directly or through multi-layered innovation networks that link the most research-intensive and/or innovative firms to others at regional, national and global levels.

Public-private partnerships are one good approach,…

One of the best ways to do this is through public-private partnerships for research and innovation. These set a framework for the public and the private sectors to co-operate and join forces in areas where they have mutual or complementary interests but cannot act as efficiently alone. Traditional in building physical infrastructures, they are increasingly popular in research and development and innovation policy. This is because they are unique policy tools for filling certain gaps in innovation systems (*e.g.* the lack of interaction between science and industry), or for increasing the efficiency of government policy in addressing other market failures that affect innovation processes (*e.g.* sharing the cost and risk of pre-competitive research).

© OECD 2004

Figure 3. **Types of innovative networks**

Type of network (Survey of 8 European countries[1])	% share
Weak or no network linkages	12.9
Equipment supplier (ES) dominated networks 	14.4
Marketing-oriented networks: users (US) and competitors (CO) 	16.0
Marketing-oriented networks: equipment and component (CM) suppliers and users 	15.8
Marketing-oriented networks: equipment and component suppliers, users and competitors 	21.9
Complete innovation networks, including government laboratory and university (GU) 	19.1

1. Belgium, Denmark, France, Germany, Ireland, Italy, Netherlands, Norway.

Source: OECD, *Managing National Innovation Systems*, 1998.

… and geographically concentrated clusters of innovative firms are another.

Another promising approach is to encourage geographically concentrated clusters of such firms. Clusters are localised innovation systems where increasing private and social returns on public and private investment result from physical or cultural proximity that encourages human networks and facilitates flows of tacit knowledge. They also result from close co-operation between firms and government in building tangible and intangible infrastructures for innovation and in coping with market failures. The "art of cluster-based policy making" is not well understood, but five case studies carried out by the OECD suggest that stress should be placed on working through partnerships and networks to achieve outcomes that the market by itself will not. Such networking and partnership initiatives should also have an international dimension, and national, regional and local initiatives should be integrated. In addition, further examination of best practices and countries' experiences is suggested in such areas as the role of universities and knowledge-intensive services in cluster

© OECD 2004

development, the regional attractors of knowledge-intensive foreign direct investment, and the governance structures and means of evaluating cluster initiatives.

SMEs must understand and take advantage of the intellectual property rights system.

Intellectual property rights have emerged as key tools for managing innovation and resolving some of the "market failures" regarding the appropriability and tradability of knowledge faced by innovating firms, especially in high-technology sectors. It is, therefore, increasingly important for entrepreneurs, inventors, researchers, SMEs and business consultants to have a good understanding of the intellectual property system, including its strategic use by large firms, in order to manage all the processes involved in building and using a firm's intellectual assets effectively. This is especially true for new technology-based firms that are not only more numerous than in the past (especially in areas such as nanotechnology, biotechnology, software and new materials) but also play an increasingly important role as innovation agents.

Not all SMEs need to enter the "patenting or licensing game" but all must be aware of the opportunities and constraints created by the intellectual property system. Evidence from a number of OECD countries show that many firms lack basic awareness and competence in this field. Obstacles include limited knowledge of the system, high costs and lack of adequate legal, business and technical support for developing a successful intellectual property strategy as part of SMEs' business strategy. Greater effort is required by all institutions operating in the national innovation system to ensure that intellectual property is adequately incorporated into the broader framework of support for entrepreneurs and SMEs. Important issues include registration of rights, their commercial exploitation, the use of patent databases, the valuation of intellectual property assets and enforcement. Of particular importance is the development of cost-effective ways of resolving disputes.

© OECD 2004

Key policy recommendations

- **Improve SMEs access to information about networking opportunities.** This will require co-operation among all stakeholders – including SME associations, public agencies and intermediary organisations – to correct deficiencies in existing sources of information. Strengthen international linkages between national and regional hubs of relevant information flows.
- **Increase the participation of SMEs in research networks and technology markets.** This includes greater SME involvement in existing (regional, national and global) public-private partnerships that connect science to innovation.
- **Support the emergence and maintenance of innovative clusters.** Help local actors implement the cluster strategies primarily through schemes to stimulate collaboration between public and private research institutions, improve the availability of market information and strengthen co-operation among firms, for instance in the fields of market intelligence, design and branding, and technological and human resource development.
- **Identify and promote best practice policies which support company innovation through cluster development.** Encourage exchange of experiences at national and international levels, especially regarding the governance structures and evaluation of cluster initiatives.
- **Enhance SME awareness and knowledge of all elements of the intellectual property system.** These include patents, trademarks, industrial designs, utility models, trade secrets, copyright and related rights, plant varieties and non-original databases. Strengthen the teaching of intellectual property rights at universities and training institutions for entrepreneurs, engineers, scientists, designers and business managers.
- **Strengthen the integration of intellectual property issues in programmes and policy initiatives aimed at fostering innovation in SMEs.** This will require greater interaction between intellectual property offices, SME support institutions, business associations, national, regional and local governments.
- **Facilitate the use of the intellectual property system by promoting the development of cost-effective mechanisms for application and for the resolution of intellectual property disputes.** These include opposition procedures, arbitration and mediation. Consider the development of the market for intellectual property insurance as a tool for reducing the costs of litigation for SMEs, identify existing barriers to this development and determine the scope and form of government intervention to remove them.

© OECD 2004

SMEs in the Global Economy

Facilitating SMEs' access to global markets

Globalisation offers SMEs opportunities…

The globalisation of business has increasingly drawn SMEs into global value chains through different types of cross-border activities. Many entrepreneurs are recognising the opportunities that this process offers and gaining access to global markets has become a strategic instrument for their further development. Access to global markets for small businesses can offer a host of business opportunities, such as larger and new niche markets; possibilities to exploit scale and technological advantages; upgrading of technological capability; ways of spreading risk; lowering and sharing costs, including R&D costs; and in many cases, improving access to finance. Gaining access to global markets can help prospective high-growth firms realise their potential and is often an essential strategic move for SMEs with large investments in intellectual property.

… and poses challenges.

But globalisation can also pose challenges and threats which SMEs, from a resource viewpoint, are less well-equipped than larger firms to confront. These challenges can expose them to heightened international competition from foreign firms, and may result in the loss of traditional markets to lower-priced competition from overseas. Challenges and threats may concern the following: standards and international compatibility issues; intellectual property protection; political risks; corruption; and rule of law issues.

SMEs' participation in global markets lags behind that of larger firms.

While data are scarce, the broad picture for many OECD and some non-member economies is that of a low, although increasing, level of activity by SMEs in international markets.

- A study conducted for Asia-Pacific Economic Co-operation (APEC) economies suggests that SMEs account for less than 30% of total exports in the region.[3]

3. C. Hall, *Profile of SMEs and SME Issues in APEC, 1990-2000*, World Scientific Publishing, Singapore, 2002.

© OECD 2004

- In Europe, exporting activity rises with firm size. The share of medium-sized enterprises engaged in exporting is more than twice that of micro-enterprises.[4]
- US experience suggests that exporting SMEs often confine their efforts to one market.
- A 2001 survey of European enterprises showed that around one-third of SMEs report an increasing number of international business contacts, ranging from 30% for micro-enterprises to 50% for medium-sized enterprises.[5]
- Few SMEs invest abroad. A recent survey showed that only 3% of SMEs in Europe have subsidiaries, branches or joint ventures in other countries.[6]

Governments should reduce barriers to access to global markets,…

Governments have a role to play in lowering the barriers faced by entrepreneurs who wish to globalise their activities. By playing this role they would benefit entrepreneurs whose businesses have high growth and export potential and those able to develop and exploit niche markets and expand their businesses on international markets. Most obviously, they can seek to ease trade barriers through international negotiations. Governments can also promote inward foreign direct investment which can serve as a vehicle for SMEs to access international markets indirectly by joining the supply chains of multinational enterprises. Indeed, foreign direct investment is often an efficient way to diffuse technology and better business methods to SMEs and enhance their international competitiveness.

… especially non-tariff barriers.

Although the evidence on these impediments is mostly fragmentary and anecdotal, it would seem that many of the impediments are *not* at the borders. Rather, they are non-tariff barriers and often relate to the need for smaller firms to deal with two or more sets of regulatory requirements once they go beyond a single market.

More generally, the success and growth of international SMEs will be enhanced by a more internationalised infrastructure that is geared to the smooth growth of firms

4. Observatory of European SMEs, *EIM Business and Policy Research*, Luxembourg, 2002.
5. *Ibid.*
6. *Ibid.*

© OECD 2004

Key policy recommendations

- **Seek, through the WTO Round and other channels, to ease trade barriers.** Progress in this regard will facilitate efforts by SMEs to access international markets.
- **Promote the role that foreign direct investment can play as a vehicle for SMEs to access international markets.** In particular, the inclusion of local SMEs in the supply chains of multinational enterprises, and their resultant (indirect) involvement in exporting activity can lead to significant diffusion of technology and more efficient business models, thereby raising the international competitiveness of SMEs.
- **Encourage the smooth, cross-border growth of SMEs by reducing the need for internationally active SMEs to comply with multiple sets of rules or requirements.** Important areas in this regard include standards, intellectual property rights, financial market regulations and other regulatory domains.
- **Facilitate access to the information SMEs need to operate internationally.** Particularly important is information relating to tax, regulatory frameworks and requirements, advisory and support services for SMEs and dispute resolution procedures.
- **Enhance incentives for new public-private partnership initiatives that would help SMEs reach global markets for innovative products and access foreign sources of advanced technologies and knowledge.** This involves broadening the scope for foreign participation in national programmes and linking national networks of SMEs with similar needs and complementary capabilities.

across borders. This applies especially to access to information as regards tax, regulatory frameworks and requirements, advisory services, markets and regulation, and dispute resolution processes. This will require active collaboration among governments, international agencies and the private sector to address issues, and to develop products and services geared to high-growth nascent and existing entrepreneurs.

Promoting e-business adoption by SMEs

E-business offers great potential benefits to SMEs,…

Information and communications technologies (ICTs) offer a wide range of benefits in terms of efficiency and market access. At the inter-firm level, they reduce the costs and increase the speed and reliability of transactions, especially over long distances. They can also make management of supply chains more efficient. Electronic

© OECD 2004

business-to-business interaction and real-time communication can reduce information asymmetries between buyers and sellers and build closer relationships among trading partners. In the business-to-consumer context the Internet provides an effective tool for communication, often providing customers with better service and allowing their needs to be monitored more accurately, facilitating new product development. A home page with a direct link to a business e-mail account provides an easy contact point and eases problems of communicating across different time zones.

… but they have been slower than large firms to take advantage of them.

As with all new technologies, small businesses have been slower to adopt information technology than large ones (Figure 4). In many cases this reflects the lack of applicability in sectors where SMEs are heavily represented, or lack of incentive to change business models unless returns are clear. But SMEs also face generic barriers to adoption, including trust, transaction security and concerns about intellectual property rights as well as challenges in areas of management skills and technological capabilities. The issues for governments are to move beyond policies that encourage basic connectivity and to foster business environments that facilitate e-business and the use of more complex applications of information technology. Governments should target programmes to overcome market failures to the extent that they are needed in particular areas (*e.g.* skill formation, specialised information).

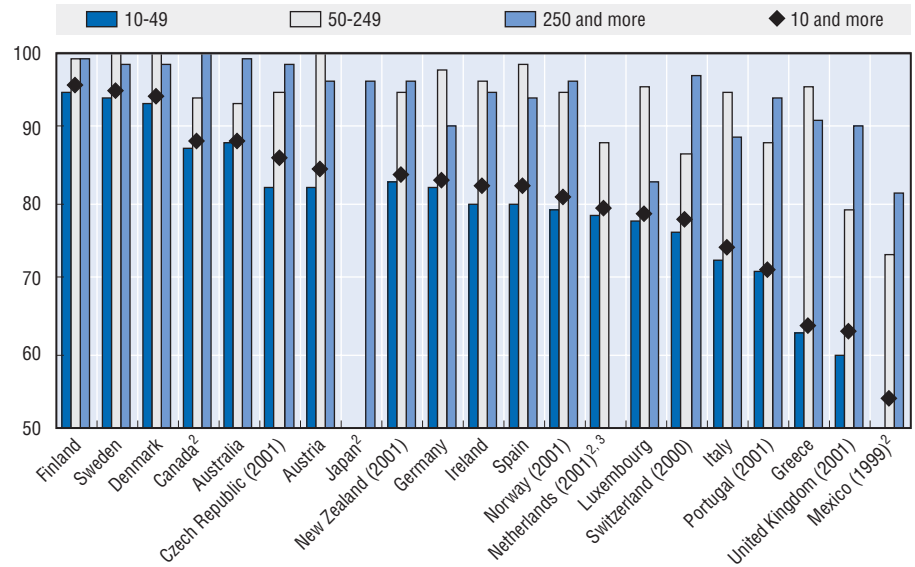
Liberalisation and competition in network infrastructure should continue and be strengthened,…

Rollout and use of quality infrastructure at affordable prices are crucial. Broadband in particular is a key to realising the potential benefits to SMEs of information and communications technology. It facilitates innovation and promotes efficiency, network effects and positive externalities. The development of broadband infrastructure, efficient and innovative supply arrangements, and effective use of broadband services require policies that: promote effective competition and continued liberalisation in infrastructure, network services and applications across different technological platforms; encourage investment in new technological infrastructure, content and applications; and ensure neutrality across competing and developing

© OECD 2004

Figure 4. **Internet penetration by size class, 2001 or latest available year**

Percentage of businesses using the Internet[1]



1. In European countries, only enterprises in the business sector, but excluding NACE activity E (electricity, gas and water supply), NACE activity F (construction) and NACE activity J (financial intermediation), are included. The source for these data is the Eurostat Community Survey on enterprise use of ICT. In Australia, all employing businesses are included, with the exception of businesses in general government, agriculture, forestry and fishing, government administration and defence, education, private households employing staff and religious organisations. Canada includes the industrial sector. Japan excludes agriculture, forestry, fisheries and mining. New Zealand excludes electricity, gas and water supply, and only includes enterprises with NZD 30 000 or more in turnover. Switzerland includes the industry, construction and service sectors.
2. For Canada, 50-299 employees instead of 50-249 and 300 or more instead of 250 or more. For Japan, businesses with 100 or more employees. For the Netherlands, 50-199 employees instead of 50-249. For Switzerland, 5-49 employees instead of 10-49 and 5 or more employees instead of 10 or more. For Mexico, Businesses with 21 or more employees, 21-100 employees instead of 10-49, 101-250 instead of 50-249, 151-1000 instead of 250 or more.
3. Internet and other computer-mediated networks.

Source: OECD, ICT database and Eurostat, Community Survey on ICT usage in enterprises 2002, May 2003.

technologies to encourage interoperability and innovation and to expand choice. Public financial assistance to expand coverage for under-served groups and remote areas could complement private investment where appropriate, provided it does not pre-empt private sector initiative or inhibit competition.

© OECD 2004

… and digital content, including increased use of e-government services, should be stimulated.

Digital products, information services and interaction with government in areas such as procurement, regulatory compliance and tax offer SMEs important potential efficiency gains and marketing opportunities. While the potential contribution of e-government is significant, the private sector must play the key role in providing content. This makes balanced regulation with regard to intellectual property rights crucial. Particularly important for innovative small firms are satisfactory protection of ICT innovations and digital products and holding the cost of intellectual property protection to reasonable levels. The rapid growth of software and business method patenting also increases small business costs and the likelihood of infringement. Regulatory frameworks that balance the interests of suppliers and users are needed to protect and manage intellectual property and digital rights without disadvantaging innovative e-business and content distribution models.

Trust, security, privacy and consumer protection are essential,…

Regulatory and self-regulatory efforts to bolster trust, security, privacy and consumer protection can enable SMES to take full advantage of e-business. A culture of security to enhance trust in the use of ICT, effective enforcement of privacy and consumer protection, and efforts to combat cyber-crime and spam are essential. Strengthened cross-border co-operation among all stakeholders is necessary to reach these goals. Of particular relevance for small firms are low-cost on-line dispute resolution mechanisms among firms and between firms and consumers.

… as are skilled human resources.

Lack of information and communications technology skills and e-business skills are widespread impediments to effective use of e-business processes once adoption decisions are made. Whereas large enterprises can afford specialised staff, SMEs must often rely on the qualifications and training of their general workforce. Governments have a major role to play in providing basic ICT familiarity during compulsory schooling, but teaching ICT skills needs to be integrated into the curriculum. Governments also have an important role, in conjunction with education institutions, business and individuals, in providing the framework to encourage ICT skill formation at higher levels, in vocational training and in ongoing lifelong learning.

© OECD 2004

Key policy recommendations

- **Move beyond policies for basic connectivity and ICT readiness to facilitate more widespread uptake and use of complex ICT applications and e-business uptake by small firms.** Target programmes where there are demonstrated market failures (*e.g.* R&D incentives, frameworks for standards, skill formation, information and demonstrations on best practice and benefits from adoption and use of ICT), taking into account that commercial considerations and returns drive business adoption of new technologies.
- **Encourage rollout of affordable quality broadband networks to underpin the competitiveness and growth of SMEs.** Continue to liberalise network infrastructure and promote broadband competition and liberalisation in network services and applications. Where the needs exist, and without pre-empting private initiative or inhibiting competition, complement private investment with public financial assistance to expand coverage for under-served groups and remote areas.
- **Strengthen the infrastructure for trust, security (including spam and viruses), privacy and consumer protection.** Intellectual property protection of ICT innovations and digital products is necessary to build the confidence among SMEs that is essential if such firms are to take full advantage of the potential of domestic and cross-border on-line activities.
- **Expand, in conjunction with business and consumer groups, SMEs' use of low-cost on-line dispute resolution mechanisms.** Strengthen cross-border co-operation between stakeholders and the development of rules with cross-border application.
- **Develop and distribute digital content, including by expanding the commercial use of information about the public sector, education and health care.** E–government services to enterprises should be used as a tool to improve efficiency of government interactions and operations with SMEs.
- **Reduce ICT skill impediments to the growth of SMEs.** Strengthen government and private roles to improve basic ICT skills and developing frameworks to encourage higher level ICT and e-business skill formation (including marketing, organisational, security, trust and management skills in addition to ICT skills) in conjunction with education institutions, business and individuals.

© OECD 2004

Enhancing the Role of SMEs for Development

Transition and developing economies need to strengthen their capacity to take advantage of trade and investment opportunities.

Recent assessments of growth recognise an understanding that an important influence on the rate at which countries grow is their ability to integrate with the global economy through trade and investment. Enterprises in transition and developing economies face major challenges in strengthening their human and institutional capacities to take advantage of opportunities in these areas. While governments make trade and investment policies, it is enterprises that trade and invest. Therefore, supply-side bottlenecks in the trade and investment areas and the way in which governments, development partners and the private sector itself address these constraints have direct implications for the economic growth potential of transition and developing countries.

SMEs have an important role in contributing to development and poverty reduction.

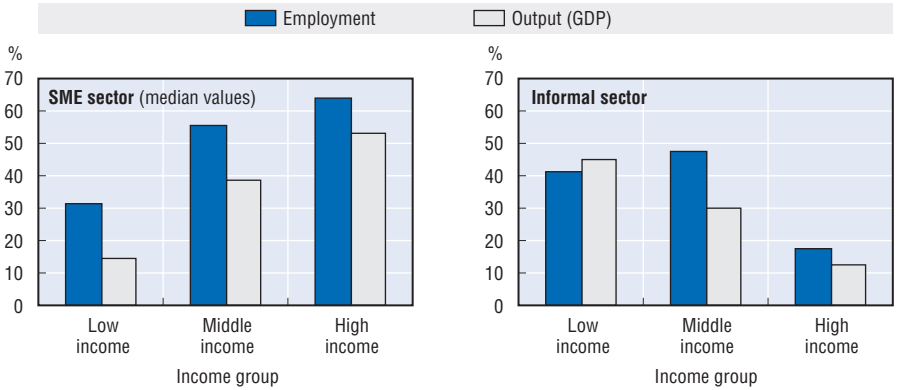
Most enterprises in transition and developing countries are SMEs. These firms typically account for more than 90% of all firms outside the agricultural sector, constitute a major source of employment and generate significant domestic and export earnings. In the poorest countries they nevertheless make up a relatively small part of the economy, contributing less to employment and output than the informal sector (Figure 5). An important policy priority in low-income countries is to facilitate the creation of SMEs in order to bring the poor into the formal sector, where they participate in markets and can engage in higher value-added business activities.

Policies toward SMEs should be integrated into broader national development strategies.

SME development requires a cross-cutting strategy that touches upon many areas: the ability of governments to implement sound macroeconomic policies and structural policies that contribute to healthy business environments conducive to enterprise creation and growth; the ability of SMEs to implement competitive operating practices and business strategies; and capable public and private institutions. Implementing such a strategy requires, in particular, simplified legal and regulatory frameworks, good governance, abundant and accessible finance, suitable infrastructure, supportive education, and sufficiently healthy and flexibly skilled labour. SME development strategy must be integrated into the broader national

© OECD 2004

Figure 5. **Contributions to employment and output**



Source: M. Ayyagari, T. Beck and A. Demirgüc-Kunt, "Small and Medium Enterprises across the Globe", World Bank Policy Research Working Paper 3127, Washington, DC, August 2003, pp. 27-28.

development and poverty reduction strategy of transition and developing countries.

- Dialogue and partnerships between the stakeholders (public sector, private sector and civil society) foster ownership of these strategies, make them easier to implement (by better addressing SME needs), and make them politically credible and sustainable.
- Access and integration into local, national, and global markets require substantial investments in sustainable development of institutional and physical infrastructure and service delivery to SMEs in all areas, including those that are rural or remote. Continued dialogue and partnerships between stakeholders about implementation and review of supportive measures, particularly, those related to capacity building in private sector service providers, yields improved outcomes.
- Enhancing women's ability to participate in SME development should be taken into account at every level, as women account for an important share of private sector activity and contribute strongly to poverty reduction. In all SME development strategies and programmes, gender issues need to be taken into account and specific, targeted initiatives need to be directed at critical obstacles.

© OECD 2004

Trade and investment capacities of SMEs must be strengthened.

SMEs must be able to respond quickly and efficiently to international market signals to take advantage of trade and investment opportunities and reap the benefits of the international trading system. This means they need to be competitive and productive. Effective business support systems are needed to enhance the competitiveness and productivity of SMEs, as well as to build their trade and investment capacity. Business support agencies (including financial institutions) must be customer-oriented and have a demonstrated ability to deal with the SME sector. Specific steps are desirable to:

- Increase the capacity of financial institutions to construct profitable SME lending programmes, while prioritising the development of innovative solutions to collateral issues. These include the acceptance of more flexible forms of collateral, particularly for SMEs with few fixed assets; the use of group guarantees and loan guarantee schemes for SMEs; more emphasis on cash flow than balance sheets in assessment of borrowing capacity; easy and effective loan application assessment methodologies.
- Strengthen the business support system, through an intermediary role, by building capacity in business services, both public and private (*e.g.* provision of market, product and process information, accounting, market analyses and research, legal advice, transport, express delivery and advertising).
- Develop a national strategy for export development and promotion, led by the appropriate ministry, but which involves participation by all key stakeholders. The overall objective should be to increase the volume and value of exports and the number of exporting companies. The strategy should seek to address the needs of firms at different stages of export market development. It should also seek to integrate export support and promotion into a well developed and effective business support system.

The benefits of foreign direct investment to local SMEs should be maximised.

The potential benefits of foreign direct investment to host economies include sources of external capital, technology and knowledge transfer, job generation, skills enhancement and enterprise development through linkages and spillover effects. These include backward linkages with suppliers, forward linkages with customers, linkages with

© OECD 2004

competitors who set new standards and necessitate greater efficiency, and linkages with technology partners. A programme to strengthen linkages between foreign direct investors and local SMEs would include:

- Improving the flow of information about potential local suppliers to potential purchasers in multi-national enterprises and about supply opportunities to potential suppliers through the development of a national Web site and/or business directories, supplemented by "meet-the-buyer" events.
- Targeting suppliers on the basis of proven abilities and commitment to future improvements,
- Working closely with multi-national enterprises by inviting them to help potential suppliers to *a)* understand their supply requirements, *b)* identify areas in which they have good opportunities to supply, and *c)* draw attention to weaknesses they must overcome in order to succeed. Such an intermediary role helps to build mutual understanding and trust between multi-national enterprises and potential suppliers.
- Helping SMEs that have the potential to supply multi-national enterprises to identify their needs and then to access the public and private support services they need.
- Offering some form of monetary incentive to multi-national enterprises and local SMEs to participate in the linkage programme. This could include contributing to the salary costs of engineers and managers in multi-national enterprises which devoted time to supplier upgrading (Singapore); cash grants to promising suppliers to help with initial investment costs (Ireland); and subsidized training and consultancy necessary for enhancing supplier capability (Chinese Taipei).
- Developing capacity building programmes that include supply chain and cluster initiatives which recognize the potential for developing tiers of suppliers to maximize trickle down effects, including to micro-enterprises as lower-tier suppliers.

© OECD 2004

Governments in advanced economies should promote policy coherence and greater effectiveness of development assistance.

Finally, overall policy coherence is essential for the successful implementation of SME development strategies. Development partners need to recognize that better attention to local conditions is necessary for trade and investment capacity building in transition and developing economies. These have to go hand in hand with market access and improved policy co-ordination among donors.

Key policy recommendations

- **Embed strategies toward the private sector and SMEs in countries' broader national development and poverty reduction programmes.** Encourage and help SME associations to participate effectively in national dialogues that help set the strategic frameworks for development, so that the contribution and the policy and support needs of SMEs are fully recognised as central to growth, employment and poverty reduction.
- **Strengthen SME capacities to improve their competitiveness in domestic, regional and global markets.** Encourage and support private sector associations and enterprises able to provide information on markets and standards, advice on strategies, and access to technology and innovation coupled with appropriate financing packages. Promote tools, such as value chain analysis, which enable entrepreneurs to see what problems and challenges they need to address within and beyond their own borders and what kind of partners they need to help them.
- **Promote policy coherence at regional, national and international level.** Work to support whole of government approaches so that trade and investment policies and standard setting are aligned with development co-operation objectives and policies. Support completion of the Doha Round of multilateral trade negotiations, including a reduction of barriers to trade in manufacturing and agricultural sectors with major benefits and opportunities for developing countries.
- **Maximise the spillover of management skills and knowledge from multi-national enterprises to local SMEs.** Spillovers of knowledge and management skills to local firms are one of most critical benefits of foreign direct investment for host countries. Support policy frameworks and multi-national enterprise behaviour that facilitate such spillovers and better document real-world cases to increase public understanding of the contribution of foreign direct investment in progression of development.

© OECD 2004

Evaluation of SME Policies and Programmes

Systematic evaluation is an essential element of a well-designed SME policy framework.

A recurrent theme in the work summarised here is the need for systematic assessment and review of SME policies and programmes. Regular evaluation is essential to identify ways of improving those programmes that should be retained and to provide a basis for reallocating funds where they should not. SME policies and programmes can involve considerable sums of public money (Table 1 shows estimates for the United Kingdom, where the necessary calculations have been made), and evaluation contributes to ensuring that they are cost-effective. In practice, the commitment of policy makers to evaluation and the extent to which it is undertaken systematically vary both among countries and among programmes within the same country.

Table 1. **United Kingdom support for small businesses, 2001**
In millions of GBP

Expenditure		**5 342**
of which		
Small Business Service budget	349	
Other expenditure by Department of Trade and Industry and its agencies	275	
British Trade and Industry	44	
Department of Culture, Media and Sport and agencies	332	
Department of Education and Skills and agencies	138	
Regional Development Agencies	274	
Department of Work and Pensions	71	
Local authorities	300	
Tax agencies (support services)	81	
Department for Environment, Food and Rural Affairs		
(grants, advice, in-kind support)	3 120	
Department of Transport, Local Government and Regions and agencies	107	
EC and EIB	246	
Favourable tax treatment (R&D tax credit; 10p Corporation Tax; 20p Small Company Corporation Tax Rate; Venture Capital Trusts; Enterprise Investment Scheme)		**2 590**
Total		**7 932**
(as a per cent of GDP)		(0.8)

Source: "Cross Cutting Review of Government Services for Small Businesses", Department of Trade and Industry, September 2002, URN 02/1324.

© OECD 2004

SME policy makers should develop an "evaluation culture".

Making programme evaluation central to the policy process begins at the design stage. When legislation is being framed, clear objectives should be set to provide a basis for future evaluation. A budget for evaluation should be provided and any necessary data collection should begin as soon as is feasible. It is also advantageous to formulate an evaluation methodology. Addressing these issues should not be left until after programmes are implemented.

All programmes should be evaluated.

Ensuring that evaluation is given a higher priority means that all, rather than merely some, programmes should be assessed. There is room for debate about the extent to which all programmes should be assessed with the same level of sophistication. It is clear that methods incorporating a high level of sophistication are desirable, since these are likely to produce more accurate estimates with less risk of over-estimating policy impact. Furthermore, a consistent high level of sophistication across programmes enables valid comparisons to be undertaken between one programme and another. The argument against this is that it is inappropriate, and not cost-effective, to have similar evaluation budgets for programmes of widely differing scales. And clearly, poorer and less developed countries will face limits as to what they can do.

Assessment teams should be independent but informed.

A judgement has to be made about whether programmes should be evaluated by the departments responsible for delivering them, by other organs of government or by external organisations. There are arguments which favour choosing evaluators from each of these groups. The departments responsible for delivering the programme clearly have unique inside knowledge and understanding, which will not be available to any outsiders. They may also be more likely to engage the support of those delivering the programme. At least for major evaluations, their involvement is vital. On the other hand there is the risk that this closeness may impair their "independence" and subject the evaluation to "capture" or political influence.

An alternative is for such evaluations to be conducted by a specialist part of government, independent of the programme delivery department. The advantage here is that they will have greater specialist evaluation skills, and be seen to be more independent than the department

© OECD 2004

delivering the programme. Their detailed knowledge of the programme will be less, however, and so they will rely more heavily upon the co-operation of the programme deliverers.

A third option is to engage specialist "outsiders" such as consultants or academics. Both these groups have the advantage of being less clearly subject to "capture" and being likely to be specialists within their subject. The central disadvantage of the use of outsiders is that if evaluation is viewed as one element in the process of policy improvement, then this has to lead to discussion. However, there is a risk that the discussion may engage those responsible for the programme less when it is led by outsiders, who may be viewed as less well informed, than when it follows from an evaluation conducted by those responsible for the programme.

Evaluation should lead to policy modifications.

Evaluation should not generally be the "end of the line" but should often lead to policy modifications. These modifications may be either changes in the objectives of the programme or changes in the way the programme is implemented or delivered. For example programmes may be extended to include businesses in sectors that were previously excluded; changes in the terms and conditions of the programme or changes in the desired outcomes.

The process by which any programme changes are implemented is likely to vary depending on the scale and profile of the programme, and according to political processes. Nevertheless, the key purpose of conducting evaluations is to influence policy. In some countries, particularly for high profile programmes, it may be valuable for information stemming from the evaluation to enter the public domain. This is more likely to occur where "outsiders" have conducted the evaluation.

© OECD 2004

Key policy recommendations

- **Apply the C.O.T.E. framework to SME policy:**
  - **C**larity and **C**oherence of SME policies require a clear rationale for policy intervention and statement of purpose. The various parts of government interacting with SMEs to facilitate their development should ensure that their efforts are consistent and co-ordinated.
  - **O**bjectives of SME policies should be clearly specified. Examples would include the creation of new firms, the growth of existing firms or promoting enterprise among target groups in the population.
  - **T**argets should be specified in measurable ways to facilitate evaluation of the extent to which objectives should have been achieved.
  - **E**valuation of policy, which must be based on clear policy targets, should be the most important test of its effectiveness.
- **Develop an "evaluation culture" by making evaluation of programmes central to the policy process.** Evaluation should not be simply undertaken as a historical accounting exercise but should be used to inform current policy, the objectives and targets of which may be modified in the light of the results of evaluation.
- **Integrate the methodology of, and budget for, evaluation of programmes as part of the legislative process.** These should not be delayed until after the programme has been implemented.
- **Ensure that all, rather than merely some selected, programmes are subject to evaluation.**
- **Major evaluations should be undertaken with independent but informed assessors.** Nevertheless, the involvement of the programme teams, both policy makers and deliverers, is vital.
- **Evaluate all programmes using the most sophisticated techniques that are feasible taking into account the need to be cost-effective.** In practice, more approximate approaches will be necessary in assessing smaller programmes.

Towards More Systematic Statistical Measurement of SME Behaviour

The empirical basis for SME policy formulation is poor.

A second recurrent theme in the preparatory work for the Istanbul Conference has been the poor empirical basis for informed policy making in the area of SMEs and entrepreneurship. Deficiencies are apparent at two levels:

- The underlying statistical base which provides the factual foundations for analysis is poor, especially in terms of international comparability; and as a consequence,

© OECD 2004

- Available high-quality empirical analysis, notably cross-country comparative studies and longitudinal studies which allow analysis of the important economic forces or policies over time, is limited.

Key policy recommendations

- **Promote international convergence of statistical concepts and processes.** Common target definitions should be encouraged across countries, data formats and procedures, notably as regards statistical observation units and size classes. the OECD should continue to act as a forum that promotes best practices in statistical data collection, processing and dissemination.
- **Foster greater international comparability of statistics.** This requires the OECD to strengthen its inventory of business statistics and prepare recommendations to improve their quality and international comparability. Non-member economies should be involved in this work where possible.
- **Develop an integrated business statistical register.** This requires that countries introduce a single identification number for enterprises, so that data from different sources can be matched. It also requires that policy makers address those barriers, often legal, that prevent national statistical authorities to have access to administrative data, such as tax offices and chambers of commerce.
- **Promote data linking to make better use of existing data and reduce respondent burden on SMEs.** Databases with linked data can strengthen the information base for policy-relevant research, but require that statistical authorities arrange access while ensuring the confidentiality of information provided by individual firms.
- **Carry out policy-relevant empirical analyses to underpin evidence-based policy making.** Cross-country comparative analysis and longitudinal studies which allow the analysis of firm behaviour over time, provide insights about the impact of policies on enterprise performance and growth as well as differences across OECD countries.

Basic conceptual problems and cost considerations are at the root of the problem.

There are a number of reasons for this state of affairs but two stand out:

- SME statistics are really just a subset, organised by size classification, of structural business statistics. This statistical system has fundamental problems of definition, notably as regards the basic statistical unit to be counted, measured or monitored. These problems hinder collection efforts and have impeded international agreement on basic concepts and methodology.

© OECD 2004

- It is desirable to contain costs at statistical agencies and to reduce, rather than increase, the respondent burden on businesses, especially SMEs.

Given these basic problems, it is perhaps unsurprising that detailed subsets of such data and analysis of them, for example women's entrepreneurship, barely exist.

But there is scope for improvement.

As part of the preparation for the Istanbul Conference, representatives of national statistical agencies have discussed these problems and identified ways to improve the situation. Some actions, notably the development of integrated business statistical registers, the introduction of single identification numbers for enterprises and their use to link data more efficiently, and greater use of administrative sources of data (*e.g.* tax, chamber of commerce), can only be taken in capitals and in several cases involve issues (*e.g.* confidentiality, structure of business registers) that require legal, technical and organisational initiatives supported by policy authorities. Other actions can usefully be taken at the international level. These include drawing up an inventory of existing practices which will make the deficiencies more transparent, and working to agree on target definitions and classifications which would facilitate international comparisons as national practices converged around them. None of this will happen quickly and movement from resolving these problems to collection of useful data comparable on a cross-country basis will take even longer. But the proposals summarised in the "Key policy recommendations" box offer a good start.

© OECD 2004

OECD PUBLICATIONS, 2, rue André-Pascal, 75775 PARIS CEDEX 16
PRINTED IN FRANCE
(00 2004 2 A 1 P) – No. 82677 2004