

OECD Studies on SMEs and Entrepreneurship

Strengthening SMEs and Entrepreneurship for Productivity and Inclusive Growth

OECD 2018 MINISTERIAL CONFERENCE ON SMES



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Foreword

On 22-23 February 2018, the OECD organised the third OECD SME Ministerial Conference on “*Strengthening SMEs and Entrepreneurship for Productivity and Inclusive Growth*”, hosted by the Mexican Ministry of Economy in Mexico City, Mexico. The event gathered over 300 participants, including Ministers, Vice Ministers, senior policy makers and high-level representatives from 55 OECD Member and Non-Member countries, the European Union and 12 international organisations. The conference was chaired by Ildefonso Guajardo Villarreal, Minister of Economy of Mexico. The Vice Chairs were Marie-Gabrielle Ineichen-Fleisch, State Secretary for Economic Affairs, Education and Research of Switzerland, Stuart Nash, Minister for Small Business of New Zealand, and Hasan Ali Çelik, Vice-Minister of Science, Industry and Technology of Turkey.

Against the background of low growth and rising inequality, the event offered a platform for a high-level Ministerial dialogue on how governments can provide SMEs with the right conditions to enhance their contributions to productivity, growth and social inclusion. Discussions drew on latest OECD findings and body of analysis on these issues. Ministers recognised the major role of SMEs in delivering more inclusive growth, and the importance of enabling SMEs to seize the benefits of ongoing transformations, such as globalisation and digitalisation. They discussed opportunities, challenges and effective policy approaches to enable SMEs to scale up, access a diversified set of financing instruments, and increase their participation in a globally integrated economy. They shared views and experiences on approaches to improve the business environment for SMEs through effective regulation, facilitate SME business transfer to address the challenges arising from an ageing population of entrepreneurs, develop entrepreneurship competencies, promote innovation in established SMEs, strengthen social inclusion through inclusive entrepreneurship, and improve the monitoring and evaluation of SME and entrepreneurship policies.

Issues related to digital transformation were pervasive in the discussions, testifying to the profound impact of digital technologies. The importance of stakeholder engagement, including direct engagement with SMEs and potential entrepreneurs, was highlighted throughout the Conference.

Fourteen years after the last OECD Ministerial Conference on SMEs in Istanbul in 2004, the 2018 Ministerial Conference represents a new milestone in the OECD Bologna Process on SME and Entrepreneurship Policies, which was launched in 2000 at the first OECD SME Ministerial Conference in Bologna, Italy, as a dynamic political mechanism to foster the entrepreneurship agenda and SME competitiveness at the global level. The *OECD Bologna Charter* provides OECD and non-OECD countries a frame of reference for improving the efficiency of policies directed at fostering entrepreneurship and catalysing the development and competitiveness of SMEs at the local, national and international levels. The *Istanbul Ministerial Declaration on Fostering the Growth of Innovative and Internationally Competitive SMEs* advanced this agenda to enhance entrepreneurship and SME innovation as drivers of growth in a global economy.

The Ministerial Conference in Mexico City delivered the *Declaration on Strengthening SMEs and Entrepreneurship for Productivity and Inclusive Growth*, along with the *Chair's Summary* of the Conference. The Declaration, which was adopted by 55 countries, including all OECD Members and 20 non-OECD Members, as well as the European Union, underlines the need for whole-of-government approaches and evidence-based policies to foster SME development and growth. It recognises the central role the OECD plays in analysis, policy dialogue, exchange of good practices and tailored policy support to governments. The *Chair's Summary* provides a substantive account of the Ministerial discussions on all the themes addressed at the Conference.

The Ministerial Conference provided an opportunity for high-level exchange on the policy priorities of governments and informed the discussions of the Programme of Work and Budget of the OECD Working Party on SMEs and Entrepreneurship for 2019-20. This forward-looking work programme centres on key issues such as SME digitalisation; SME productivity; participation in global value chains (GVCs); SME financing; business transfer; monitoring and evaluation of SME policies; and the development of an OECD Strategy for SMEs.

The OECD will continue to advance the SME and entrepreneurship agenda, by strengthening knowledge, fostering policy dialogue and further intensifying its efforts to support countries in developing better SME and entrepreneurship policies.

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Table of contents

Foreword	3
Acknowledgements	5
Executive Summary	11
1. Key Issues	15
SMEs are key to strengthening productivity, delivering more inclusive growth and adapting to the major transformations of our time	16
SMEs are very heterogeneous in their characteristics and performance.....	18
SME productivity performance varies across firms, and the persistent gap with large firms affects growth potential and income distribution	19
Enabling SMEs to scale up and innovate can have a considerable economic and social impact	20
Digitalisation offers new opportunities for SMEs to participate in the global economy, innovate and grow	22
Better access to global markets and knowledge networks can strengthen SMEs' contributions.....	24
The new industrial revolution, changing nature of work and demographic trends present new opportunities and challenges for SMEs	26
A sound business environment is essential for SME competitiveness and growth	26
Financing in the appropriate forms is important to enable small businesses to start up, develop and grow	28
Entrepreneurship competencies and management and workforce skills also drive business innovation and growth	29
Monitoring and evaluation of SME policies are needed to deliver strong outcomes	30
A holistic, cross-cutting perspective on SMEs is needed to seize the potential for SME growth in a rapidly evolving context.....	30
References.....	31
2. Enabling SMEs to Scale Up.....	35
The scaling up of SMEs is key to boost productivity and achieve inclusive growth.....	36
Productivity growth is faster when businesses can grow... and shrink	37
SMEs can experience high-growth at different stages of their life cycle, generating benefits for the economy	37
... but high growth is a transitory stage in the life of firms	37
Start-ups that scale up provide a key contribution to job creation... ..	38
... but post-entry growth of start-ups varies widely across countries.....	40
Medium-sized enterprises that scale up are key drivers of competitiveness	41
SMEs can achieve scale through different mechanisms, including external growth	42
Digitalisation is a powerful engine to scale up, enabling new modes of growth.....	42
Participation in global markets and GVCs can also spur growth.....	43
Policy can play a role in enabling SMEs to scale up	43
A coordinated policy approach is needed to devise mutually reinforcing policies for SME scale-up	48
Notes	49
References.....	49

3. Enhancing SME access to diversified financing instruments	53
Access to finance is key to the creation, growth and productivity of SMEs	54
Longstanding challenges in accessing bank finance limit SME growth in many countries	54
The recovery in SME lending following the crisis has been uneven	54
Overall, SMEs remain too dependent on straight debt	57
There are opportunities for SMEs to tap into a wide range of alternative financing instruments	58
The digital transformation offers new opportunities to improve SME access to finance	62
The G20/OECD High Level Principles on SME Financing provide a comprehensive framework for policy makers	63
Governments have been stepping up efforts to foster a diversified financial offer for SMEs	64
Notes	69
References.....	69
4. Fostering greater SME participation in a globally integrated economy	73
Better access to global markets is key to strengthening SME contributions to economic development and social well-being.....	74
Changes in the global trading environment offer new opportunities for SMEs	76
A range of internal and external factors influence SMEs' ability to participate in global markets ..	80
SMEs are adapting their internationalisation strategies for the 21 st century	82
Policies can enable SMEs to integrate into global markets	84
Creating a supportive domestic and international operating environment for SMEs takes a whole- of-government approach	86
Notes	87
References.....	87
5. Improving the business environment for SMEs through effective regulation	91
Why does it matter?	92
What are current trends and challenges?.....	92
What are key areas for policy to consider?	96
Notes	97
Further Reading	98
6. Business transfer as an engine for SME growth.....	99
Why does it matter?	100
What are current trends and challenges?.....	101
What are key areas for policy to consider?	102
Notes	104
Further Reading	105
7. Developing entrepreneurship competencies.....	107
Why does it matter?	108
What are current trends and challenges?.....	108
What are key areas for policy to consider?	111
Notes	112
Further Reading	112
8. Promoting innovation in established SMEs	113
Why does it matter?	114
What are current trends and challenges?.....	114
What are key areas for policy to consider?	117

Further reading.....	119
9. Strengthening social inclusion through inclusive entrepreneurship.....	121
Why is it important?	122
What are current trends and challenges?.....	122
What are key areas for policy to consider?	124
Further Reading	126
10. Monitoring and evaluation of SME and entrepreneurship programmes.....	127
Why is it important?	128
What are current trends and challenges?.....	128
What are the key areas for policy to consider?	130
Notes	131
Further Reading	131
Annex A. Conference Programme	133
Agenda at a glance	134
Annex B. Declaration on Strengthening SMEs and Entrepreneurs for Productivity and Inclusive Growth	143
Annex C. Chair's Summary	147
Enabling SMEs to scale up	148
Enhancing SME access to diversified financing instruments	150
Fostering greater SME participation in a globally integrated economy	151
Improving the business environment for SMEs through effective regulation	152
Business transfer as an engine for SME growth	153
Developing Entrepreneurial Competencies	154
Promoting innovation in established SMEs.....	154
Strengthening social inclusion through inclusive entrepreneurship.....	155
Monitoring and Evaluation of SME and Entrepreneurship Policies and Programmes	156
The way forward.....	158

Tables

Table 3.1. Suitability of alternative financing instruments for different firm profiles and stages.....	59
Table 7.1. The entrepreneurship competencies identified in the EntreComp entrepreneurship competency framework	110
Table 10.1. Six Steps: Methods for assessing the impact of SME policy	130

Figures

Figure 1.1. SMEs provide the main source of business employment.....	17
Figure 1.2. Once in business, women entrepreneurs feel as confident as men about the future	18
Figure 1.3. There are large differences in the SME contribution to employment and value added across countries, particularly in manufacturing.....	19
Figure 1.4. The productivity gap between large firms and smaller SMEs has widened since the global crisis.....	20
Figure 1.5. Young firms are a key driver of job creation	21
Figure 1.6. SMEs lag behind in the adoption of more sophisticated digital technologies.....	24

Figure 1.7. Compared to their contributions to national economies, SMEs are under-represented in global trade	25
Figure 1.8. SME performance is strongly influenced by the business environment	27
Figure 1.9. The gap in credit costs between SMEs and large enterprises has widened.....	28
Figure 2.1. The productivity gap between large firms and smaller SMEs has widened in some OECD countries since the global crisis	36
Figure 2.2. Young firms are a key driver of job creation	39
Figure 2.3. Few micro start-ups grow, but these contribute disproportionately to job	40
Figure 2.4. Post-entry growth varies across countries.....	41
Figure 3.1. SME loan rejection rates vary greatly across countries	55
Figure 3.2. The recovery in SME lending has been uneven.....	55
Figure 3.3. The gap in credit costs between SMEs and large enterprises has widened.....	56
Figure 3.4. Women believe they are less likely than men to have access to finance to start or grow a business	57
Figure 3.5. SMEs continue to rely heavily on traditional debt instruments	58
Figure 3.6. Leasing and hire purchases are on the rise.....	60
Figure 3.7. Factoring volumes are expanding, especially in emerging economies	61
Figure 3.8. Venture capital investments differ widely across countries, but only account for a very small share of SME financing	61
Figure 4.1. Where export propensity by SMEs is higher, wage gaps vis-à-vis large firms are smaller	74
Figure 4.2. Compared to their contributions to national economies, SMEs are under-represented in global trade.....	75
Figure 4.3. The gap in exporting activity in the industrial sector is particularly large.....	75
Figure 4.4. SMEs account for a larger share of value added in international trade when indirect exports are taken into account	78
Figure 4.5. Indirect export contributions to value added are particularly relevant among independent SMEs.....	78
Figure 4.6. The number and complexity of cross-border data transfer restrictions are rising.....	84
Figure 5.1. Barriers to entrepreneurship, 2008 and 2013	93
Figure 5.2. Trend in adoption of Regulatory Impact Analysis (RIA) across OECD countries	94
Figure 5.3. Barriers to firm restructuring	95
Figure 7.1. Fear of failure, 2006, 2010 and 2014	108
Figure 7.2. Perceived capabilities for entrepreneurship, 2006, 2010 and 2014.....	109
Figure 8.1. Use of enterprise resource planning, 2015	114
Figure 8.2. Innovation types by firm size, 2010-12.....	115
Figure 9.1. Self-employment rate, 2016.....	123
Figure 9.2. Proportion of self-employed with employees, 2016	123
Figure 9.3. Barriers to business creation in the European Union, 2012	124

Boxes

Box 3.1. The G20/OECD High Level Principles on SME Financing	64
Box 3.2. Policies to improve the credit information infrastructure	67
Box 6.1. Gift and inheritance tax preferences in selected OECD countries.....	104
Box 8.1. Upgrading managerial skills through ICT in SMEs: A review of government programmes	116

Executive Summary

SMEs are key players in national economies around the world. Representing 99% of all businesses, generating about 60% of employment and between 50% and 60% of value added in the OECD area, they can play a major role in delivering growth that is more inclusive and whose benefits are shared more broadly. This is particularly relevant at a time when many countries face the challenges of low growth and productivity, along with rising or persistently high inequality. As important drivers of innovation, SMEs are also instrumental to ensure that economies and societies adapt to major transformations, such as digitalisation, globalisation, ageing and environmental pressures. To enhance the contributions of SMEs, policy should work to address the inefficiencies and barriers that may be holding back entrepreneurship and the development of small businesses, and ease SMEs' access to resources that are strategic in a global and digitalised economy, such as financing, skills and innovation networks.

SMEs create jobs across different geographic areas and sectors, employing broad segments of the labour force. In addition, entrepreneurial opportunities represent an important vector for economic and social participation and upward mobility, by allowing disadvantaged groups, including young people, women, seniors, migrants, ethnic minorities and the disabled, to participate in the economy. These populations typically face specific barriers to business creation. Increasing entrepreneurship among these groups and improving the quality of their business start-ups can increase participation in the labour market and boost productivity.

At the same time, SMEs are a dynamic population, which is very diverse in terms of age, size, business model, performance, and the profile and aspirations of entrepreneurs. Their composition varies widely across countries and sectors, which is reflected in their diverse contributions to innovation, productivity, quality job creation and growth. This diversity has implications for how policies are crafted and requires a deeper understanding of the SME population, based on more comprehensive data.

SMEs that grow can have a considerable impact on employment creation, innovation, and the competitiveness of national and sub-national economies, as well as contribute to raising wage and income levels. Firms with different characteristics and sectors of activity can experience growth at various moments in their life cycle. At the same time, sustained growth is usually a transitory phase in the life of a firm, influenced by many factors, including entrepreneurs' skills and ambitions. In this context, governments are increasingly focusing on the growth journey of SMEs to enable conditions for post-entry growth, growth of small firms into mid-size ones and the scaling up of mid-size companies, and seeking to better target and tailor their SME and entrepreneurship policies.

Some SMEs are at the productivity frontier and amongst the most innovative firms, jumpstarting new industries. These firms can exploit technological or commercial opportunities that have been overlooked by larger companies, and enable the commercialisation of knowledge generated by research organisations. Start-ups are a key

source of radical and disruptive innovations, especially in sectors such as software, nanotechnology, biotechnology and clean technologies, including through increased competitive pressure they put on incumbent firms. More broadly, SMEs are often an essential channel for the diffusion and adaptation of innovations to different contexts. The contribution of SMEs to innovation has increased in recent decades. Enterprise innovation is often the outcome of collaborative efforts in which businesses interact and exchange knowledge and information with other partners as part of broader innovation systems. This shift towards an ‘open innovation’ paradigm, also in part facilitated by the digital transition, has reduced the need for innovation-related capital investments and eased participation in innovative activities by SMEs. It however requires SMEs to strengthen their capacity to tap into and participate in innovation networks, and policies can play an important role in this regard.

Access to the appropriate forms of finance is a key condition to enable small businesses to start up, develop and grow. Although SMEs’ access to bank lending has largely recovered since the financial crisis, market failures and structural challenges remain, including information asymmetries, high transaction costs in servicing SMEs, and lack of financial skills and knowledge among small business owners. Policies that help broaden the range of financing instruments available to SMEs and entrepreneurs can increase SMEs’ resilience to changing conditions in credit markets and improve their contribution to economic growth. The *G20/OECD High-Level Principles on SME Financing* advocate a holistic policy approach to addressing SME financing gaps, with a need to take into account both demand-side (e.g. lack of financial skills, disadvantageous tax treatment) and supply-side barriers (e.g. opacity of the SME market).

In addition, a sound business environment and a well-functioning entrepreneurial “eco-system” for business, including at the local level, is essential for countries and regions to spur SME development. Start-ups and SMEs are typically more dependent than large companies on their business environment. Due to internal constraints, they are more vulnerable to market failures, policy inefficiencies and inconsistencies, which may result from the interaction of regulatory and policy approaches across different areas. Appropriate institutional and regulatory settings, as well as enabling conditions to access markets and resources, are therefore indispensable to incentivise risk-taking and experimentation by entrepreneurs and ensure that business growth potential can be realised. A transparent regulatory environment, efficient bankruptcy regulation and judicial systems are essential to support the growth of start-ups and SMEs, especially in innovative, high-risk sectors, as well as to foster participation of SMEs in a globalised and digital economy, and further policy efforts are needed in these areas.

Stronger participation by SMEs in global markets creates opportunities to scale up and enhance productivity, by accelerating innovation, facilitating spill-overs of technology and managerial know-how, and broadening and deepening the skillset. International exposure, whether through imports, exports or foreign direct investment (FDI), frequently goes hand in hand with higher productivity and wages. However, in both OECD and non-OECD countries, few SMEs export directly and for those that do, exports typically represent a lower share of trade turnover relative to larger firms. However, SMEs’ indirect contribution to exports in OECD countries, as suppliers to larger domestic firms or multinational companies (MNCs), can represent more than half of total exports in value added terms. Enabling SMEs to become active in GVCs calls for whole-of-government approaches which address the constraints that SMEs face in internationalising, including access to information, skills, technology and finance, as well as trade facilitation and connectivity.

Digitalisation offers new opportunities for SMEs to participate in the global economy, innovate and grow, allowing SMEs to improve market intelligence and access global markets and knowledge networks at relatively low cost. They can also facilitate the emergence of different forms of growth, including “born global” small businesses or firms that achieve scale without an important mass of employees or other tangible assets. Furthermore, Big Data and data analytics provide new opportunities for SMEs to enhance their competitiveness, enabling product and service innovation, improved production processes within the firm, as well as a better understanding of clients and partners’ needs, and the overall business environment. The use of digital technologies can also facilitate SME access to skills and talent, through better job recruitment sites, outsourcing and online task hiring, as well as connection with knowledge partners. Furthermore, technology can facilitate access to a range of financing instruments, with innovative solutions to address information asymmetries and collateral shortages. However, to date, a large number of SMEs have not been able to reap the benefits of the technological transition. While, in most countries, the digital adoption divide with large firms is narrow for simple connectivity and web presence, the gap broadens when considering participation in e-commerce and the adoption of more sophisticated applications. Closing these gaps calls for policies to support the development of appropriate skills and complementary investments in organisational change and innovation.

Demographic change also brings about specific challenges for SMEs, such as skills shortages and business transfer needs. Across OECD countries every year, a significant number of economically sound SMEs disappear from the market as a result of problematic business transfers, with implications for economic growth, employment, innovation and social inclusion. While business transfer is essential for the continuity of firm activity and value creation, it may also represent an opportunity for new entrepreneurs to start a business and for SMEs to rethink their vision and business model, innovate by bringing in up-to-date knowledge, techniques and business methods, and thereby seize new opportunities. A stronger evidence base on business transfer is needed, as is raising awareness of the importance of early succession planning and acquisition opportunities for new entrepreneurs; fostering the development of business transfer markets; taking account of tax consequences on sale or disposal of SMEs; and ensuring an appropriate financing offer to facilitate transfer.

Successful entrepreneurship and business growth also require an expanded skillset to channel the complexities of today’s economies: from commercial (e.g. marketing and serving of new offers), to project management (e.g. logistics, organisations of events), financial (e.g. capital and cash flow management) and strategic thinking skills (e.g. building internal leadership, coordinating sets of actions to fulfil new strategic objectives). This might be particularly challenging for smaller firms and entrepreneurs, and policies that enable SMEs to develop, attract and retain qualified skills, both within and across borders, as well as to upgrade managerial capacities and practices, are therefore essential to boost growth. Workforce skills are also important, especially in small businesses, where a larger proportion of workers than in large companies are involved in the implementation of business innovation on the ‘shop floor’.

Available evidence suggests that there is substantial direct public expenditure on SME and entrepreneurship programmes. In addition, many other policy measures, which target SMEs have important indirect public finance implications through foregone tax revenue. Monitoring and evaluation is therefore essential to assess the economic efficiency of SME and entrepreneurship policies, and inform their design by identifying those programmes and policy features, which lead to desirable outcomes.

The main outcomes of the Ministerial Conference are embodied in the *Declaration on Strengthening SMEs and Entrepreneurship for Productivity and Inclusive Growth*. It highlights the multidimensional contributions of SMEs and entrepreneurs to inclusive growth, and the need for an enabling and evidence-based policy environment and supportive SME infrastructure to offer opportunities for diverse firms and a level playing field for all enterprises. The Declaration calls on governments to enhance SME participation in the national and global economy and enable SMEs to make the most of the digital transition. It underlines the importance of access to appropriate forms of finance; entrepreneurial opportunities for all segments of the population; entrepreneurship education and training and upskilling of entrepreneurs and workers; and multi-stakeholder dialogue on effective policies. The Declaration also encourages the OECD to consider a number of areas moving forward, including:

- supporting a better understanding of the heterogeneity of SMEs and entrepreneurs, the drivers of business creation and growth and policy implications across countries;
- deepening understanding of the combined effects of structural reforms on the SME business environment and of the role and impact of targeted policies;
- pursuing analysis on entrepreneurship that contributes to social inclusion;
- analysing key levers for enhancing SME contributions to sustainable and inclusive growth; and
- continuing to promote the sharing of best practices and the development of evidence.

This publication contains the documentation of the third OECD SME Ministerial Conference on “*Strengthening SMEs and Entrepreneurship for Productivity and Inclusive Growth*”, which was hosted by the Mexican Ministry of Economy in Mexico City on 22-23 February 2018.

1. Key Issues

Summary

- Many countries are facing low productivity growth, weak trade and investment, and rising or persistently high inequality. In addition, major trends, including the new industrial revolution, the changing nature of work and demographic changes, call for innovative policy solutions.
- SMEs are key to strengthening productivity, delivering more inclusive growth and adapting to megatrends. SMEs that grow have a considerable positive impact on employment creation, innovation, productivity growth and competitiveness. SMEs can scale up and innovate at different stages of their life cycle. Fostering innovation in established SMEs can enhance aggregate productivity and narrow wage gaps.
- The population of SMEs is very diverse in terms of age, size, business model and the profile and aspirations of entrepreneurs. They vary in their characteristics and performance, including across sectors, regions and countries. These differences have implications for how policies are designed and targeted.
- Digital technologies enable SMEs to improve market intelligence and access distant markets and knowledge networks at relatively low cost, and stronger participation in international activity can boost SME growth. However, SMEs are lagging behind in the digital transition and are disproportionately affected by trade barriers, deficient intellectual property protection, and quality of infrastructure and institutions.
- A conducive business environment, including institutional and regulatory settings, is essential to incentivise risk-taking and experimentation by entrepreneurs, and foster business growth potential. Despite wide-ranging reforms in many countries, the complexity of regulation, high compliance costs and inefficient insolvency regimes remain a major obstacle to entrepreneurial activity.
- Micro firms, young, innovative and high-growth SMEs, and certain categories of entrepreneurs, including women business owners, face persistent challenges in accessing finance in the appropriate forms and volumes. The G20/OECD High Level Principles on SME Financing highlight that broadening the range of financing instruments requires comprehensive approaches to address both demand- and supply-side barriers.
- Access to entrepreneurship competencies, management and workforce skills, technology, innovation, and networks, is also critical to enable SME growth.
- A cross-cutting approach to SME policy can enhance SME contributions to inclusive growth, as can strengthening the monitoring and evaluation of policies.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

SMEs are key to strengthening productivity, delivering more inclusive growth and adapting to the major transformations of our time

In many countries, governments are facing the challenges of low productivity growth, weak trade and investment, and rising or persistently high inequality of income, wealth and well-being. These challenges were exacerbated by the 2007-08 global crisis, but they also reflect structural conditions (OECD, 2016a, 2017a).

In addition, governments are seeking innovative solutions to seize opportunities and mitigate risks that emerge from major transformations in economy and society, such as increased globalisation, digitalisation, the new industrial revolution, the changing nature of work, demographic changes, and the circular economy and the transition to a low-carbon economy. These mega-trends have far-reaching consequences for productivity and income distribution, and for the role that policy can play to enhance inclusive growth.

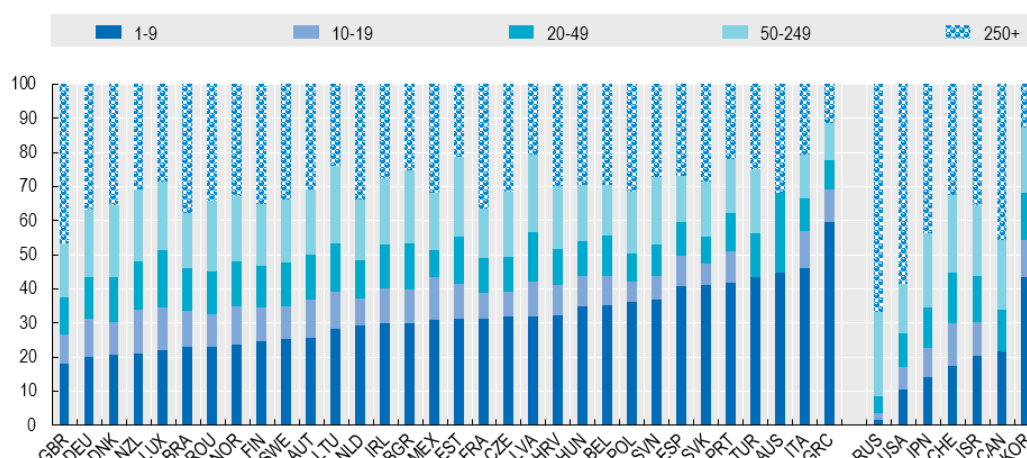
Small and medium-sized firms (SMEs) are central to the collective goal of increasing productive potential, reducing inequality and ensuring that the benefits from increased globalisation and technological progress are shared, as documented in OECD work on the productivity-inclusiveness nexus (OECD, 2016a). Furthermore, SMEs can help countries adapt to other major transformations in the global environment, seizing new opportunities and contributing to mitigate risks.

SMEs are the main source of jobs in the business sector

In the OECD area, SMEs represent almost the totality of the business population, account for about 70% of total employment and generate between 50% and 60% of value added, on average (OECD, 2017b). SMEs contribute to more than one third of GDP in emerging and developing economies and account for 34% and 52% of formal employment respectively. In recent decades, employment in SMEs has steadily increased at the global level. Over 2003-16, across 132 countries, the number of total full-time employees in SMEs has nearly doubled, from 79 million to 156 million (ILO, 2017).

Figure 1.1. SMEs provide the main source of business employment

Percentage of all persons employed, total business economy, 2014 or latest available year



Note: For Canada, Switzerland, Israel, Japan, Korea, the United States and the Russian Federation, data do not include non-employers. Data for Korea and Mexico are based on establishments. Data for the United Kingdom exclude an estimate of 2.6 million small unregistered businesses. For Australia, Canada and Turkey the size class 1-9 refers to 1-19.

Source: OECD (2017b).

Innovation is often driven and diffused by new and established SMEs

Some SMEs are at the productivity frontier and amongst the most innovative firms, jump-starting entire new industries. These firms can exploit technological or commercial opportunities that have been neglected by larger companies and enable the commercialisation of knowledge generated by research organisations (Baumol, 2002; OECD, 2010a). Start-ups are a key source of radical and disruptive innovations, especially in sectors such as software, nanotechnology, biotechnology and clean technologies, including through increased competitive pressure they put on incumbent firms. More broadly, SMEs are often an essential channel for the diffusion and adaptation of innovations to different contexts.

SMEs are central to efforts to ensure growth is more inclusive

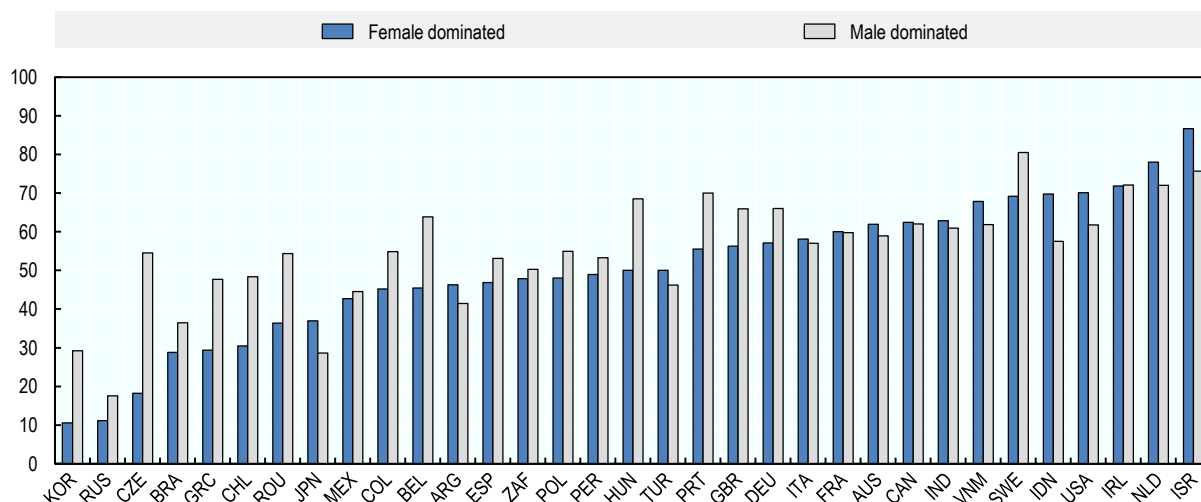
SMEs typically create job opportunities across geographic areas and sectors, employing broad segments of the labour force, including low-skilled workers, and providing opportunities for skills development. As such, SMEs that generate value added and quality jobs represent an important channel for inclusion and poverty reduction, especially but not exclusively in emerging and low-income economies. Small businesses also contribute to inclusion by serving locations, populations and markets that do not have enough scale to attract larger firms.

In addition, entrepreneurial opportunities represent an important vector for economic and social participation and upward mobility, by allowing disadvantaged or marginalised groups, including young people, women, seniors, migrants, ethnic minorities and the disabled, to participate in the economy. OECD work on inclusive entrepreneurship shows that while these social groups are heterogeneous, their members typically face specific barriers to business creation (OECD/EU, 2015). Increasing entrepreneurship among these groups, as well as improving the quality of their business start-ups, represents an

opportunity to increase participation in the labour market and boost productivity. For instance, while most countries in the OECD area show gender gaps in the perception of barriers to setting up a business, recent evidence suggests that, in most countries, despite these gaps, women feel as confident as men about their business and its future once it is up and running (Figure 1.2).

Figure 1.2. Once in business, women entrepreneurs feel as confident as men about the future

Positive evaluation of current business status, percentage of survey respondents (average 2016 - 2017)



Source: OECD (2017b), based on the Future of Business Survey, conducted by Facebook in collaboration with the OECD and the World Bank.

SMEs are very heterogeneous in their characteristics and performance

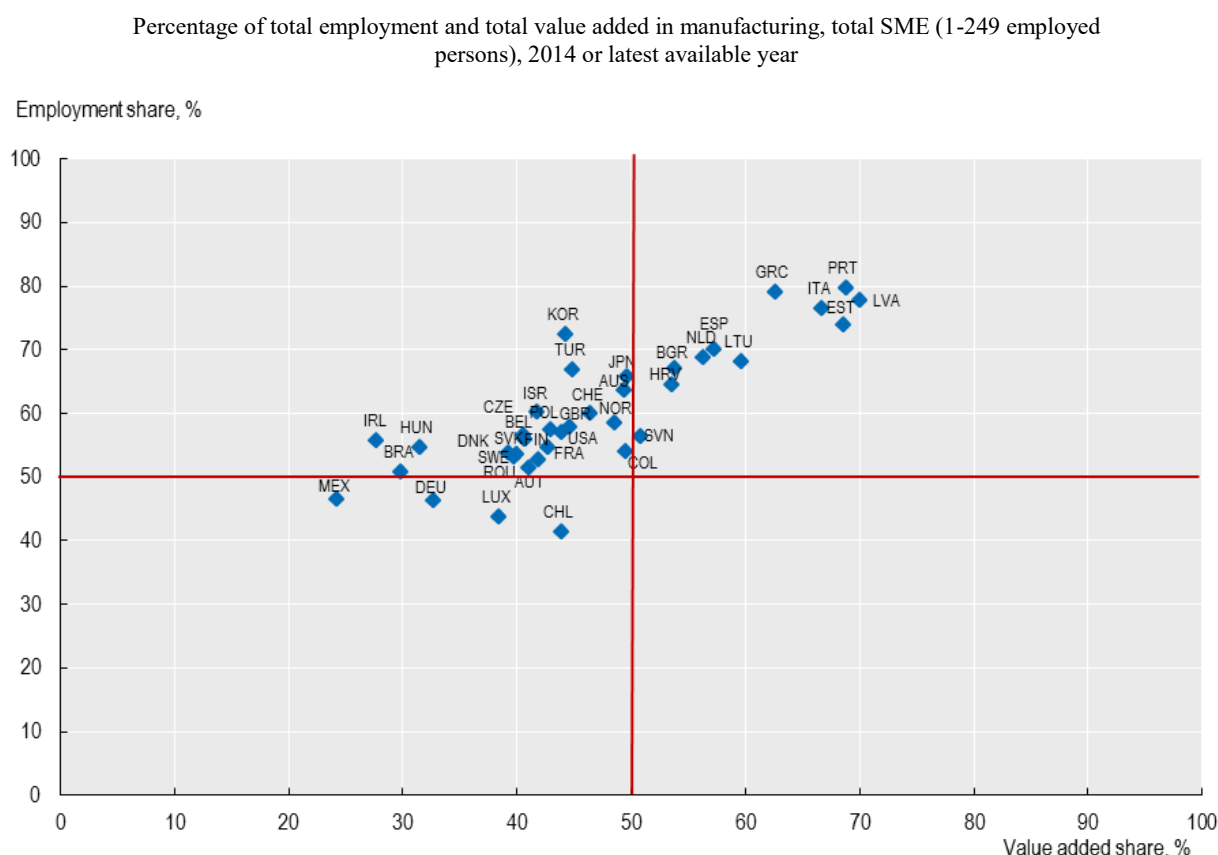
SMEs are a dynamic and evolving population, which is very diverse in terms of age, size, business model, performance, and the profile and aspirations of entrepreneurs. Their composition varies widely across countries and sectors (Figure 1.3), with implications for their contributions to innovation, productivity, quality job creation and growth. They also have implications for how policies are designed and targeted.

SMEs and young firms that experience rapid growth can have a considerable impact on employment creation and productivity growth, including through innovation, heavy investments in human capital, new demand for advanced products and services, knowledge spill-overs that other enterprises can harness, and impact on local entrepreneurial ecosystems.

Established medium-sized enterprises that innovate and scale up are the driving force behind growth in many OECD economies, often ensuring the coordination, upgrading and participation in supply chains of smaller suppliers (e.g. Coltorti and Venanzi, 2017). There are also many small enterprises in mid or low-tech sectors which are embedded in competitive local production systems, and which generate incremental innovation and contribute to employment, social inclusion and territorial cohesion.

At the same time, many SMEs do not extend their reach beyond small local markets. These firms, which produce limited innovation, and whose owners do not have strong growth aspirations, often remain small throughout their life cycle.

Figure 1.3. There are large differences in the SME contribution to employment and value added across countries, particularly in manufacturing



Notes: For Australia, SMEs refer to < 200 persons employed; for Japan and Korea, SMEs refer to < 300 persons employed; for Japan, the United States and Switzerland, data do not include non-employers. Data for the United Kingdom exclude an estimate of 2.6 million small unregistered businesses. For Chile, only enterprises with more than 10 employees are covered.

Source: OECD (2017b).

SME productivity performance varies across firms, and the persistent gap with large firms affects growth potential and income distribution

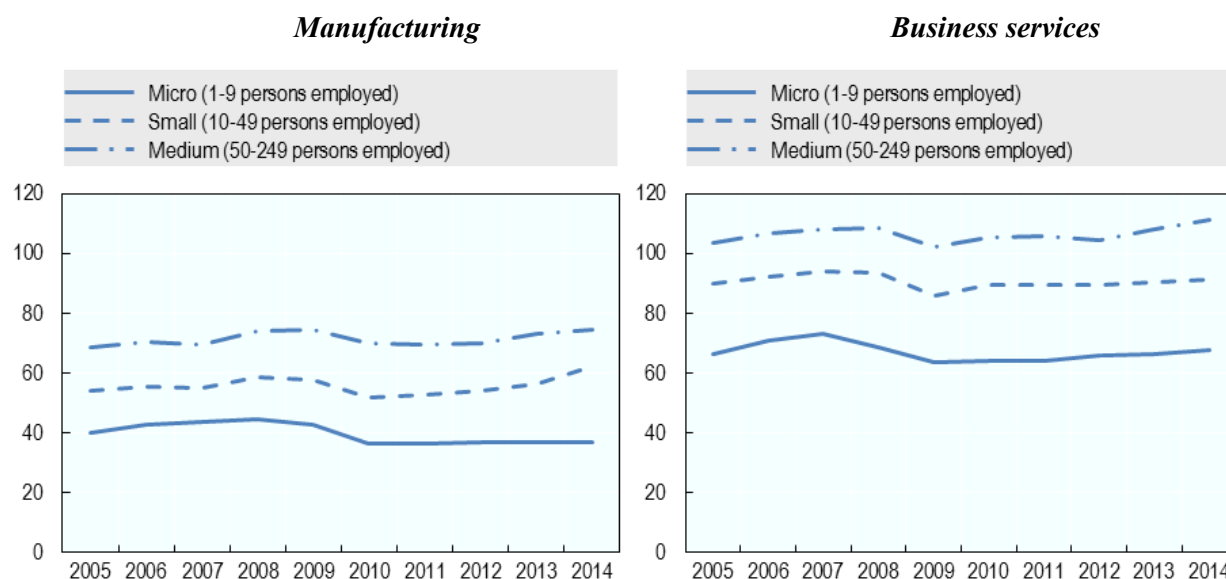
Across countries, there is in general a persistent productivity gap between SMEs and large firms. To the extent that large firms can exploit increasing returns to scale, productivity typically increases with firm size, although some variability across sectors and countries is observed. In particular, in the services sector, medium-sized firms outperform large firms in some countries, exhibiting competitive advantages in niche, high-brand or high intellectual property content activities, as well as the intensive use of affordable ICT (OECD, 2017b).

OECD work on productivity shows that, in some countries, the gap in productivity between SMEs and large firms increased in aftermath of the 2007-08 global crisis. While for small and medium-sized enterprises there has been a reversal in this trend during the recovery,

the larger gap has become persistent for micro-firms, especially in manufacturing, where production tends to be more capital-intensive (Figure 1.4). This gap is also an important driver of the observed rise in inequality, including wage inequality, in many countries (OECD, 2016b and 2017c).

Figure 1.4. The productivity gap between large firms and smaller SMEs has widened since the global crisis

Value added at factor cost per person employed, current US dollars, current PPPs
Large firms (250 persons employed or more = 100)



Note: Data cover Austria, Czech Republic, Estonia, Germany, Hungary, Italy, Latvia, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, and United Kingdom. Data for manufacturing (10-33 of ISIC rev.4) and business services, excluding financial services (45-82 less K of ISIC rev.4).

Source: Source: OECD Structural Business Statistics (database), November 2017.

In many emerging and developing economies, the productivity gap between large firms and SMEs – and the resulting income gaps – are especially large, due in particular to a disproportionate concentration of employment in micro and small firms, often informal ones, with relatively little employment in medium-sized firms.

Enabling SMEs to scale up and innovate can have a considerable economic and social impact

In many countries, enabling SMEs to seize growth opportunities over time is a policy priority to address low productivity growth and widening wage and income gaps. SMEs that grow, in terms of employees, turnover profitability or market share, can have a considerable impact on employment creation, innovation, and the competitiveness of national and sub-national economies, as well as contribute to raising wage and income levels.

All kinds of firms, with different characteristics and across many sectors, can experience growth at various moments in their life cycle. Growth can be spurred to satisfy a major increase in demand, strengthen competitive position, or seize new opportunities in markets,

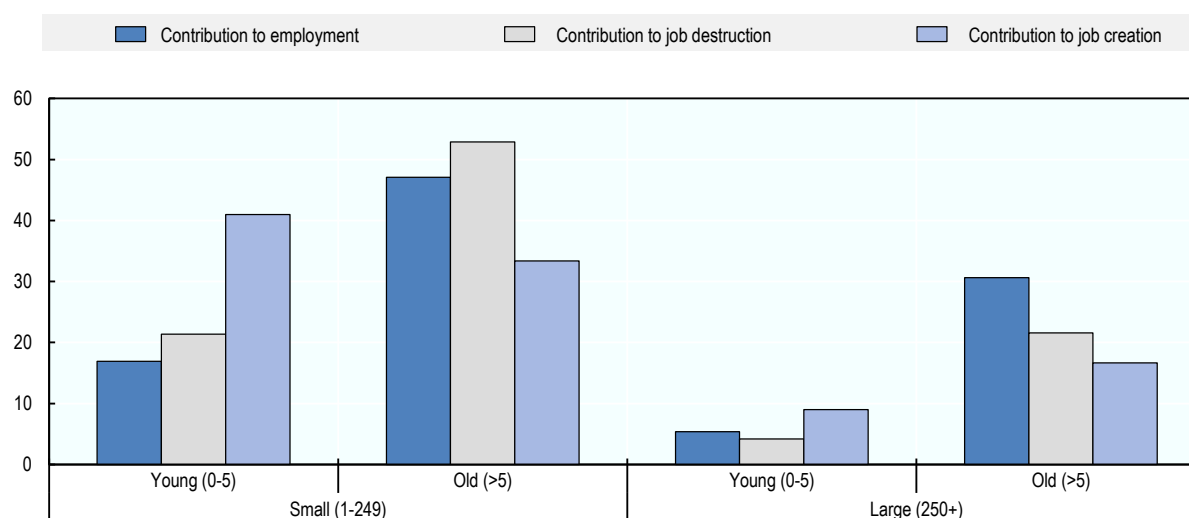
and can take different forms, including organic (i.e. internally generated) and non-organic growth (i.e. through mergers and acquisitions, joint-ventures or alliances). At the same time, OECD studies illustrate that sustained growth is a transitory phase in the life of the firm, influenced by many factors, including entrepreneurs' skills and ambitions (OECD, 2010b).

Young and high-growth SMEs create jobs and bring a range of benefits to the economy...

OECD work shows that the share of young SMEs in total job creation is about twice as large as their share in total job destruction or in total employment. However, the majority of new enterprises fail in the first years of activity and post-entry growth varies widely across countries. Surviving start-ups scale up faster in high-risk sectors, such as telecommunications, scientific research and development and IT services. Older SMEs and older large firms continue to account for the bulk of employment across countries, but create fewer jobs than they destroy (Figure 1.5) (Calvino et al., 2016).

Figure 1.5. Young firms are a key driver of job creation

Employment, job destruction and job creation by firm age and size



Note: Data cover eighteen countries and firms in manufacturing, construction and non-financial business services. Data refer to the 2001-11 for most countries. Owing to methodological differences, figures may deviate from officially published national statistics

Source: Criscuolo, Gal, and Menon (2014) based on the OECD DynEmp Express database.

High-growth firms (HGFs), i.e. firms that grow rapidly over a short period of time, typically represent a small share of total businesses, but account for a larger share of employment. For example, in Israel HGFs represented 4% of firms but accounted for 10% of employment when considering established companies with more than 10 employees, in 2015 (OECD, 2017b).

While there may be a short-term trade-off between rapid employment growth and productivity growth, evidence suggests that, in the long run, HGFs have higher productivity growth than other firms, since they are more innovative and invest heavily in human capital (Du and Temouri, 2014; OECD, forthcoming). Furthermore, fast-growing firms provide an

indirect contribution to aggregate productivity growth by contesting markets and forcing other firms to invest and upgrade, sparking new demand for advanced products and services, generating knowledge spill-overs which other nascent or existing enterprises can harness, and strengthening the local entrepreneurial culture by acting as role models for future and nascent entrepreneurs (OECD 2010b).

Scaling up and innovation are at the reach of many SMEs

Increasingly, governments are focusing on the growth journey of SMEs, that is, on enabling conditions for post-entry growth, growth of small firms into mid-size ones and the scaling up of mid-size companies, as a lever to boost aggregate productivity growth and competitiveness by ensuring coordination and upgrading of smaller suppliers.

The contribution of SMEs to innovation has increased in recent decades due to changes in the way innovation takes place in the economy. Enterprise innovation is often the outcome of collaborative efforts in which businesses interact and exchange knowledge and information with other partners as part of broader innovation systems. This shift towards an ‘open innovation’ paradigm, also facilitated by the digital transition, has reduced the need for innovation-related capital investments, making business innovation more accessible to SMEs (OECD, 2017c and 2010a).

In light of such developments, the importance of an open, competitive and pro-growth environment and of innovation systems that are conducive to knowledge flows and effective commercialisation of research has increased. Globalisation has also increased the importance of cross-border collaboration in innovation, but SMEs often find it difficult to identify and connect to appropriate knowledge partners and networks at the local, national and global levels.

Supporting innovation in established SMEs holds the potential to contribute to inclusive growth by enhancing productivity growth of small businesses and reducing wage gaps between SMEs and large companies. OECD studies show that while conducive framework conditions are essential to small business innovation, managerial skills and formal management practices play a key role for leveraging internal strategic resources towards in-house innovation and collaboration with external partners. Similarly, the effective adoption of ICT and Industry 4.0, which involves the use of automation and digitalisation in manufacturing, requires strong managerial skills in SMEs. In this regard, evidence suggests that targeted programmes that combine ICT solutions with management training and advisory services can be especially effective (OECD, 2017c).

Digitalisation offers new opportunities for SMEs to participate in the global economy, innovate and grow

Digital technologies allow SMEs to improve market intelligence and access global markets and knowledge networks at relatively low cost. The digital transition facilitates the emergence of “born global” small businesses and provides new opportunities for SMEs to enhance their competitiveness in local and global markets, through product or service innovation and improved production processes. Furthermore, Big Data and data analytics provide a wide range of opportunities for SMEs, enabling a better understanding of the processes within the firm, the needs of their clients and partners, and the overall business environment.

In addition, the digital transition opens a range of new opportunities for scaling up, and different forms of business growth are emerging, with some companies able to achieve a

substantial scale without an important mass of employees or other tangible assets. “Lean start-ups” are emerging that leverage the Internet to lower fixed costs and outsource many aspects of the business to stay agile and responsive to the market (OECD, 2017d).

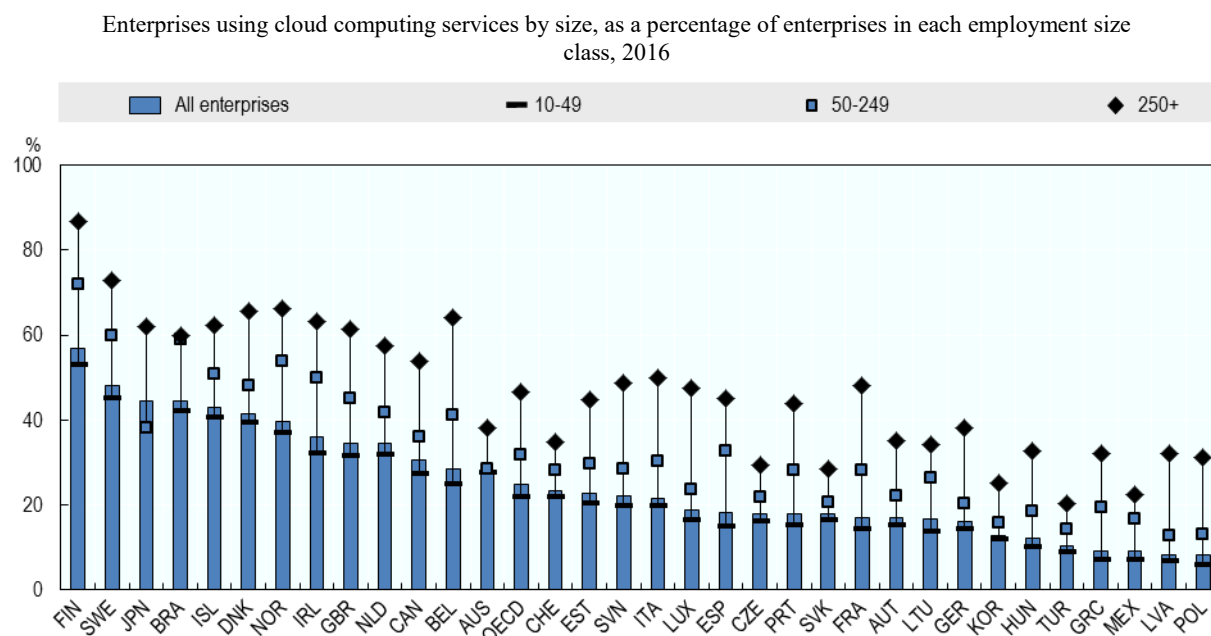
The use of digital technologies can also ease SMEs’ access to skills and talent, through better job recruitment sites, outsourcing and online task hiring, as well as connection with knowledge partners (OECD, 2017d). It can also facilitate access to a range of financing instruments. Mobile banking and online payments have had an important impact on traditional SME financing and digitalisation has allowed new financial services to emerge, with innovative solutions to address information asymmetries and collateral shortages.

... but SMEs are lagging behind in the digital transition

To date, a large number of SMEs have not been able to reap the benefits of the technological transition also due to limited adoption of digital technologies. While, in most countries, the divide with large firms is narrow for simple connectivity and web presence, the gap broadens when considering participation in e-commerce and, especially, more sophisticated applications. For instance, across OECD countries, enterprise resource planning (ERP) software applications to manage business information flows are popular among large firms (78% adoption rate in 2016) but less used by SMEs (less than 28%). In many countries, a large adoption gap is also observed for cloud computing, i.e. the renting of computer power from an external provider, which can allow smaller firms to use Big Data, while overcoming some of the barriers associated with the high fixed costs of ICT investment (Figure 1.6).

As the OECD Going Digital project underlines, the adoption lag of SMEs is mainly due to lack of investment in complementary knowledge-based assets, such as R&D, human resources, organisational changes and process innovation, and this lag has implications for their capacity to turn technological change into innovation and productivity growth. Furthermore, SMEs face specific challenges in managing digital security and privacy risks, mainly due to lack of awareness, resources and expertise to assess and manage risk effectively (OECD, 2017e).

Policy can play a role in ensuring that SMEs reap the benefits of increased digitalisation. While affordable and widespread coverage of digital networks is essential, targeted policies can help diffuse digital technologies to SMEs and enable their effective use, while addressing related risks. This can be done through the development of appropriate skills and complementary investments in organisational change and innovation. Also, ensuring sound competition in digital markets is key to enable new firms to challenge incumbents, efficient firms to grow, and inefficient ones to exit (OECD, 2017e).

Figure 1.6. SMEs lag behind in the adoption of more sophisticated digital technologies

Note: Cloud computing refers to ICT services used over the Internet as a set of computing resources to access software, computing power, storage capacity and so on. Data refer to manufacturing and non-financial market services enterprises with ten or more persons employed, unless otherwise stated. Size classes are defined as: small (10-49 persons employed), medium (50-249) and large (250 and more). OECD data are based on a simple average of the available countries.

Source: OECD (2017e).

Better access to global markets and knowledge networks can strengthen SMEs' contributions

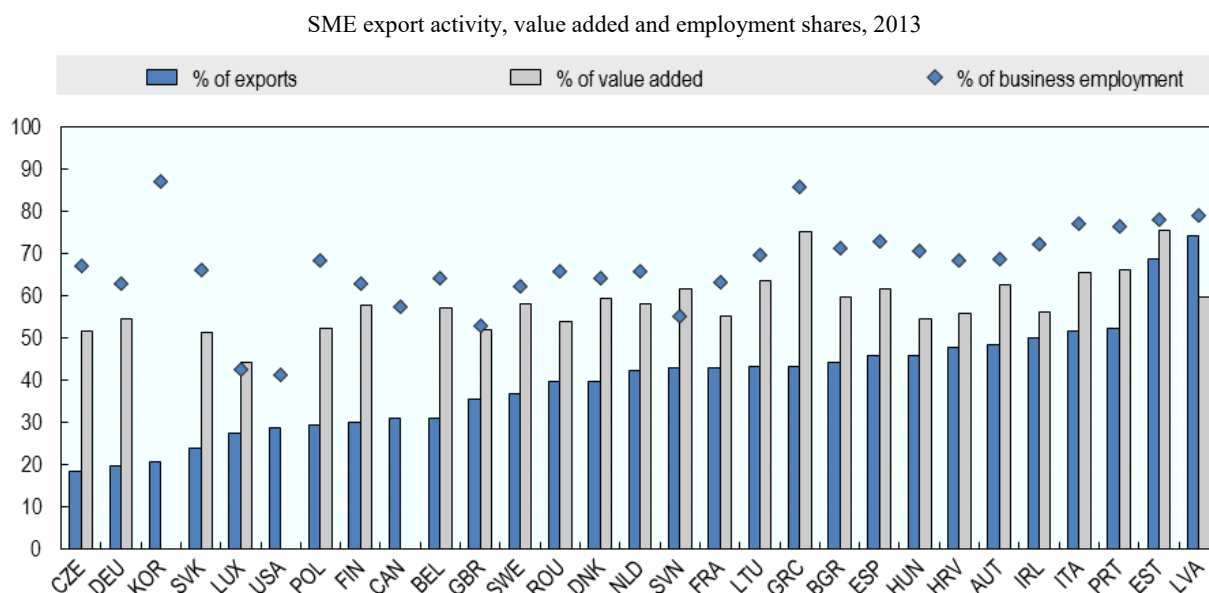
The structural shift in the international division of labour associated with the rise in global value chains (GVCs) offers SMEs new opportunities to participate in global markets, specialising in specific segments of production. SMEs can integrate the global economy in different ways, as exporters, suppliers to large firms that export, and importers of competitively priced and higher quality foreign inputs, capital goods and technologies.

Stronger participation by SMEs in global markets creates opportunities to scale up and enhance productivity, accelerating innovation, facilitating spill-overs of technology and managerial know-how, broadening and deepening the skillset. International exposure, whether through imports, exports or foreign direct investment (FDI), goes frequently hand in hand with higher productivity and wages. For instance, in countries where SMEs have a relatively high share of exports, differences in average salaries between SMEs and larger firms are smaller.

Greater flexibility and capacity to customise and differentiate products can give SMEs a competitive advantage in global markets relative to larger firms, as they are able to respond rapidly to changing market conditions and increasingly shorter product life cycles. “Born global” firms and highly innovative SMEs are often fully integrated into global markets (“micro multinationals”), dominating some niches or serving as key partners of larger multinationals in developing new products or serving new markets.

On the other hand, across OECD and non-OECD countries, few SMEs export directly and for those that do, exports typically represent a lower share of trade turnover (relative to larger firms) and generally target neighbouring countries (OECD, 2016b). At the same time, when considering SMEs' indirect contribution to exports, as suppliers to larger domestic firms or multinational companies (MNCs) that export, SMEs in OECD countries can represent more than half of total exports in value added terms (Figure 1.7).

Figure 1.7. Compared to their contributions to national economies, SMEs are under-represented in global trade



Source: OECD Structural and Demographic Business Statistics and Trade by Enterprise Characteristics databases.

Benefits from GVC participation, including in terms of productivity growth, depend on the position of the firm within global production networks and the nature of inter-firm linkages. Firms and industries positioned at the centre of complex production networks have access to a greater variety of foreign inputs, and potentially a broader range of technologies, compared to those at the periphery. Smaller firms display faster productivity growth in those sectors that have become more central to global production, than those on the periphery, and also in sectors with stronger linkages to more productive foreign buyers/suppliers (Criscuolo and Timmis, forthcoming).

Closer global integration also has implications for firms that operate in local markets, through increased competition, which can have disruptive effects on local economies and requires enhanced market knowledge and competitiveness by small businesses.

... but SMEs are more affected by trade restrictions than larger firms

GVCs and digitalisation amplify the importance of goods and services trade policies. Trade and investment openness, trade facilitation, intellectual property protection, and infrastructure and institutional quality, are all key to SME engagement in global markets. However, while some trade costs have fallen significantly in recent years, due also to the expansion of digital platforms, others remain. Reform of slow or cumbersome border procedures can cut costs of trading by 12%-18%, depending on a country's level of development (OECD, 2015a). OECD analysis shows that opening up services markets

would primarily benefit SMEs. For instance, for cross-border exports of services, an average level of services trade-restrictiveness represents the equivalent of an additional 14% tariff for SMEs relative to large firms (OECD, 2017f).

The increasingly complex trading environment requires greater international cooperation to identify global solutions to global challenges, from traditional standards to new regulatory issues in the digital age. It also calls for a focus on domestic whole-of-government approaches, which address the constraints that SMEs face in internationalising, including access to information, skills, technology and finance, as well as trade facilitation and connectivity.

The new industrial revolution, changing nature of work and demographic trends present new opportunities and challenges for SMEs

The new industrial revolution and the changing nature of work, with greater demand for high-skilled and non-routine jobs, generate new opportunities for innovative entrepreneurs and are leading to the emergence of new business models. However, these shifts also pose challenges to SMEs that cannot offer attractive wages and job conditions.

Furthermore, in some markets, the expansion of platform-based transactions between professionals and consumers (e.g. the “gig economy”) is increasing competition by self-employed and may have implications for how firms operate and grow, with the potential to reduce firms’ shares and firm-based employment (OECD, 2016c and 2017d).

Another key trend shaping the economy is an increasing concern with achieving environmental sustainability. SMEs are central to this effort, in light of their large aggregate environmental footprint. The transition to a low-carbon and circular economy may pose specific challenges for SMEs to adopt more sustainable practices while maintaining or strengthening competitiveness in local and global markets, but it also opens new opportunities to small entrepreneurs, with respect to their role in supplying green goods and services and developing new sustainable business models (OECD, 2013a).

In addition, small businesses can represent an effective tool to address societal needs through the market, as in the case of social enterprises which fill gaps in general-interest service delivery (EU/OECD, 2016). Likewise, ageing populations in many countries are enabling the expansion of small businesses that address the needs of the senior population, through new technologies, products and services, and creating the conditions for greater engagement by seniors in entrepreneurial activities.

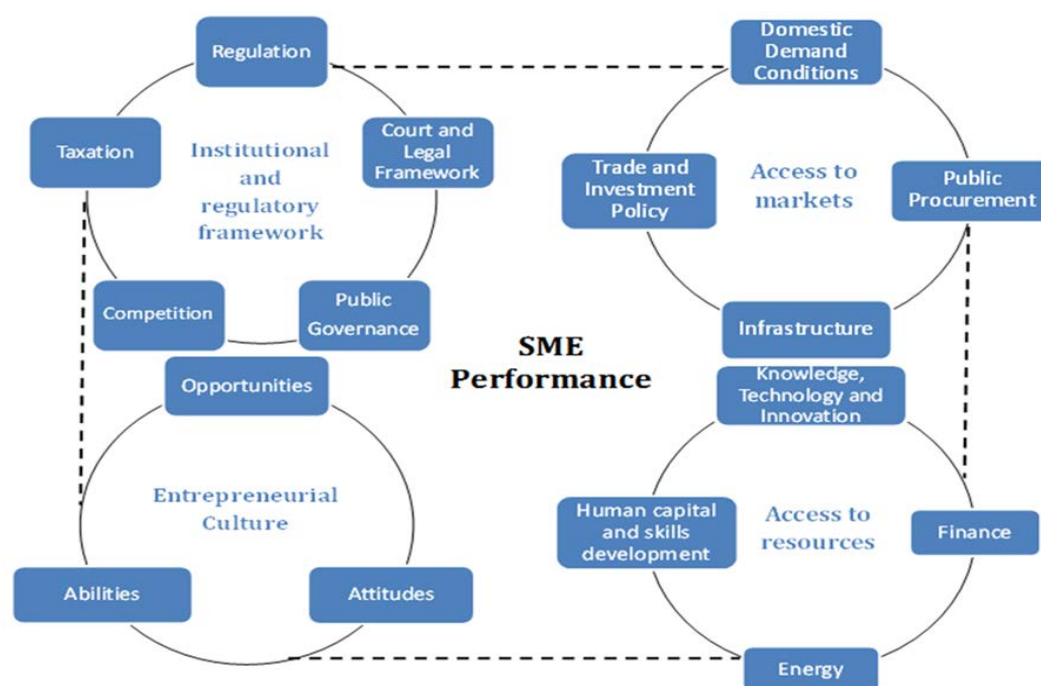
At the same time, demographic change brings about specific challenges for SMEs, such as skills shortages and business transfer needs. Across OECD countries, every year, a significant number of economically sound SMEs disappear from the market as a result of problematic business transfers, with implications for economic growth, employment, innovation and social inclusion. While business transfer is essential to the continuity of firm activity and value creation, it may also represent an opportunity for new entrepreneurs to start a business and for SMEs to rethink their vision and business model, innovate by bringing up-to-date knowledge, techniques and methods to a business, and seize new opportunities (Brigham et al., 2007).

A sound business environment is essential for SME competitiveness and growth

A sound business environment and a well-functioning entrepreneurial “eco-system” for business, including at the local level, is essential for countries and regions to foster

participation of SMEs in a globalised and digital economy. Such a framework including institutional and regulatory settings, and conditions to access markets and resources, is indispensable to incentivise risk-taking and experimentation by entrepreneurs and ensure that business growth potential can be realised. An entrepreneurial culture is also important to offer attractive opportunities for entrepreneurship and develop the abilities and attitudes among the population which are necessary to seize them (Figure 1.8).

Figure 1.8. SME performance is strongly influenced by the business environment



Source: OECD (2017g).

Start-ups and SMEs are typically more dependent than large companies on their business ecosystem and, due to their internal constraints, are more vulnerable to market failures, policy inefficiencies and inconsistencies, which may arise in different areas of policy, or result from the interaction of regulatory and policy approaches across different areas. In particular, OECD studies illustrate that a transparent regulatory environment, efficient bankruptcy regulation and judicial system are essential to support the growth of start-ups and SMEs, especially in innovative, high-risk sectors (Calvino et al., 2016).

Public sector transparency and integrity and competitive neutrality are also essential for a level playing field for businesses of all sizes. Opacity and corruption in the public sector, while detrimental to all businesses, pose particular problems for SMEs, and market entry and growth of new and small businesses encounter limitations when state-owned enterprises (SOEs) benefit from an unfair edge in domestic and cross-border activities (OECD, 2012, 2017h).

The OECD report *Small, Medium, Strong: Trends in SME performance and business conditions*, the first instalment in a project to monitor SME performance and benchmark the effectiveness of policies in creating the appropriate conditions for SMEs to flourish and grow, documents developments in the SME business environment (OECD, 2017g). In recent years, in many countries, important progress has been made to reduce the

administrative burdens on start-ups, lower legal barriers to entry, and reduce the costs for regulatory compliance in different areas. Policy efforts to simplify regulations and administrative procedures for businesses, and SMEs in particular, are widespread and include the use of ICT, as well as improved availability and provision of information. Regulatory policy bodies responsible for regulatory oversight have been established in many countries to ensure that regulation serves whole-of-government policy. Regulatory impact assessments (RIA) have become a common practice in most OECD members, including in most cases SME impact assessments, although in some countries only for major regulations or selected regulatory instances. However, in several areas, such as license and permit systems, insolvency regimes and taxation, the complexity of regulatory procedures remains a major obstacle to entrepreneurial activity and business growth.

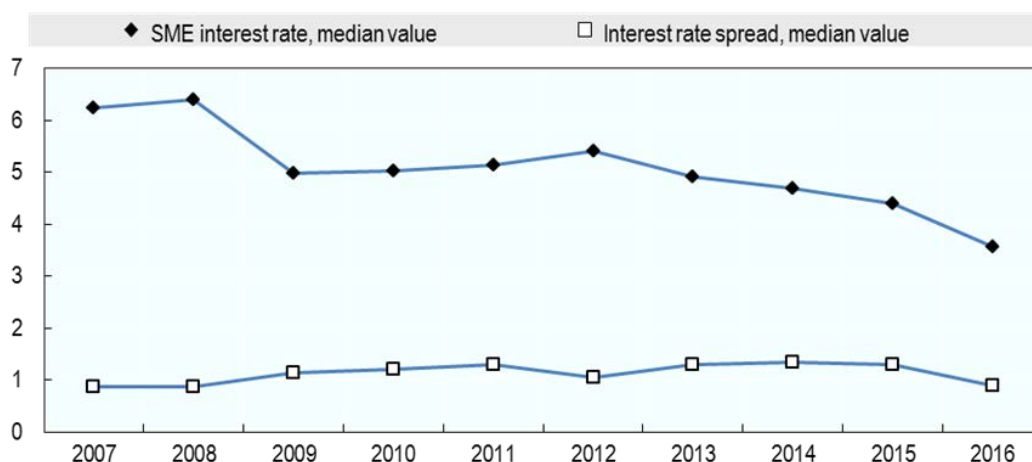
Financing in the appropriate forms is important to enable small businesses to start up, develop and grow

Access to finance is a critical prerequisite for the development of dynamic and productive SMEs in the context of an increasingly globalised and digital world. However, longstanding challenges in access to finance limit SME growth in many countries.

Although SMEs' access to bank lending largely recovered after the financial crisis, market failures and structural challenges remain, including information asymmetries, high transaction costs in servicing SMEs, and lack of financial skills and knowledge among small business owners. In addition, the financial crisis illustrated the vulnerability of many SMEs to changes in the credit cycle and more rigorous prudential rules have led banks to modify their business model and adopt more stringent credit selection criteria. As a result, and even though interest rates have declined considerably across a large number of countries, and survey data illustrate more accommodating credit conditions, the spread in the average interest rates charged to SMEs and to large firms has widened compared to the pre-crisis period (Figure 1.9).

Figure 1.9. The gap in credit costs between SMEs and large enterprises has widened

Average interest rate charged to SMEs and average spread between interest rates charged to SMEs and large enterprises, median values



Source: OECD (2018).

Implementing the G20/OECD High Level Principles on SME Financing can enable SMEs to access finance in the appropriate forms and volumes

Debt finance presents heightened barriers for firms with a higher risk-return profile, such as new, innovative and growth-oriented enterprises, whose business model may rely on intangibles and whose profit patterns are often difficult to forecast (OECD, 2015c). Alternative financing instruments, including asset-based finance, alternative forms of debt, hybrid tools and equity instruments, offer opportunities to mitigate the SME financing gap and to serve the diverse needs of the SME population. In this regard, policies that help broaden the range of financing instruments available to SMEs and entrepreneurs can increase SMEs' resilience to changing conditions in credit markets and improve their contribution to economic growth. Indeed, evidence shows that, industries that are more dependent on external finance grow relatively faster in countries with more developed financial markets and finance improves post-entry performance of firms, even when controlling for the size of entrants (Bravo-Biosca et al., 2016; Rajan and Zingales, 1998).

The OECD Scoreboard on Financing SMEs and entrepreneurs shows that, in recent years, an increasing range of financing options has become available to small businesses and governments have been stepping up efforts to foster a diversified financial offer for SMEs, including new policy initiatives, scaling up existing measures and policy experimentation. In addition, the advent of Fintech (combining technology and innovative business models in financial services) has gained considerable momentum and could have sizeable effects on SME financing, offering unprecedented solutions to deal with the main barriers that SMEs face in financial markets: information asymmetries and collateral shortage (OECD, 2016d).

The G20/OECD High-Level Principles on SME Financing advocate a holistic approach to addressing SME financing gaps, recognising that the availability and access to alternative sources of finance are held back by a number of demand-side (e.g. lack of financial skills, disadvantageous tax treatment) and supply-side barriers (e.g. opacity of the SME market; G20/OECD, 2015). As a consequence, financial instruments for SMEs often operate in thin, illiquid markets, with a low number of market participants, which, in turn drives down demand from SMEs and discourages potential suppliers of finance (OECD, 2016d; Nassr and Wehinger, 2015).

Entrepreneurship competencies and management and workforce skills also drive business innovation and growth

Evidence suggests that changes in entrepreneurial behaviour have significant consequences on levels of growth and innovation (OECD, 2010a). Successful entrepreneurship and business growth require an expanded skillset to channel the complexities of today's economies: from commercial (e.g. marketing and serving of new offers), to project management (e.g. logistics, organisations of events), financial (e.g. capital and cash flow management) and strategic thinking skills (e.g. building internal leadership, coordinating sets of actions to fulfil new strategic objectives). This might be particularly challenging for smaller firms and entrepreneurs, and policies that enable SMEs to develop, attract and retain qualified skills, both within and across borders, as well as to upgrade managerial capacities and practices, are therefore essential to boost growth (OECD, 2013b).

In particular, evidence points to a strong link between better managerial skills and formal management practices (e.g. HRM, standards and certifications, accounting) on the one hand and productivity growth on the other (OECD, 2017c). Workforce skills are also important,

especially in small businesses where a larger proportion of workers than in large companies are involved in the implementation of business innovation on the ‘shop floor’. In this respect, there is evidence that SMEs that provide employees with opportunities to develop problem-solving skills are more likely than others to succeed in developing new products or processes (OECD, 2015b).

A perceived lack of capabilities remains one of the most frequently cited barriers for people to start a business and is in particular a challenge for youth (18-30 years old). OECD work on youth entrepreneurship shows that across all OECD countries, more than half of youth surveyed in the period 2012-16, reported a lack of entrepreneurship knowledge and skills (OECD/EU, 2017).

Globally, efforts to build entrepreneurship competencies through education have increased greatly over time. Schools, vocational and higher education institutions are increasingly enriching their study programmes with dedicated entrepreneurship education courses, and problem-based teaching and assessment methods have proven particularly successful.

Public policy should consider a progressive approach to entrepreneurship education over the student’s lifetime, as well as specialised entrepreneurship education training and support for teachers, and strengthened business start-up support in vocational and higher education institutions, including linkages between education institutions and existing business support organisations.

Monitoring and evaluation of SME policies are needed to deliver strong outcomes

There is substantial direct public expenditure on SME and entrepreneurship programmes. In addition, many other policy measures which target SMEs have important indirect public finance implications through foregone tax revenue. Monitoring and evaluation is therefore essential to assess the economic efficiency of SME and entrepreneurship policies, and inform their design by identifying those programmes and policy features which lead to desirable outcomes.

Key challenges include increasing the application of rigorous evaluation techniques; better specifying policy objectives, targets and indicators; making better use of data, including existing national administrative data sets for purposes such as tax and social security; and seizing the potential of Big Data. It is also important to make better use of evaluation in the policy cycle; evaluate systematically across the portfolio of SME and entrepreneurship interventions; and assess the impacts on SMEs and entrepreneurship of policies in areas where business development is not the primary objective.

Continued efforts by governments are needed to strengthen evaluation culture in the field of SME and entrepreneurship, building on recent policy developments in the SME and entrepreneurship policy environment and advances in monitoring and evaluation data availability and techniques. The OECD Framework for the Evaluation of SME and Entrepreneurship Programmes and Policies (OECD, 2007) provides a guiding tool for monitoring and evaluation.

A holistic, cross-cutting perspective on SMEs is needed to seize the potential for SME growth in a rapidly evolving context

The SME policy space is complex. It comprises framework conditions; broad policies that impact SMEs; and specific targeted policies. These areas often cut across the boundaries of ministries and government agencies, as well as across levels of government. Moreover,

since SMEs are often embedded in local eco-systems, it is important to consider factors affecting framework conditions at the local level, and how policies developed at national level are tailored to local conditions, as well as how they coordinate with policies that are shaped at the regional or territorial level (OECD, 2016e).

While many governments increasingly recognise the need for a comprehensive perspective when developing SMEs policies and have taken steps in this direction, the synergies, trade-offs and complementarities within and across policy areas, as well as the implications for different types of SMEs, are often not well considered, due also to limited evidence and insufficient understanding of the interdependency of policies.

A better understanding is needed of the combined effects of structural reforms on the SME business environment, as well as on the role and impact of policies targeted to SMEs. Efforts in this direction should consider the potential synergies and trade-offs across diverse policy areas, including distortionary effects that may be introduced by some policy actions; recognise the heterogeneity of the SME population; and acknowledge the multidimensional contributions SMEs make to the economy and society. They should also recognise that countries have different priorities for different populations of firms, depending on the specific national contexts and circumstances.

Over the past two decades, the OECD has been at the forefront of international SME policy dialogue and efforts to provide an evidence base for more effective SME policies in both OECD and non-member countries. Governments can leverage its unique expertise in developing, collecting and understanding business statistics across Members and non-Members, and build on the strong foundation of policy analysis developed across OECD Committees, in areas such as SME finance, innovation, taxation, regulation, digitalisation, employment, skills, trade, internationalisation and GVCs, environment, and others. The OECD can also make use of its extensive networks, including with stakeholders from the private sector and financial institutions and its recent experience in developing cross-cutting policy strategies in other areas to serve governments in their efforts to enable SMEs and entrepreneurs to contribute more fully to productivity and inclusive growth.

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2. Enabling SMEs to Scale Up

Summary

- Enabling SMEs to scale up can help countries address low productivity growth and widening income gaps, since SMEs that grow have a considerable impact on competition, innovation, employment and wages.
- SMEs, with different characteristics and across many sectors, can scale up at different stages of their life cycle, to seize new opportunities in markets and strengthen competitive position. High growth represents a transitory stage in the life of firms. Many factors influence high growth, and entrepreneurs' skills and ambitions are critical.
- Start-ups that scale up represent only a tiny fraction of all start-ups, but are a key source of innovation and job creation. However, post-entry growth varies widely across countries, and surviving start-ups scale up faster in high-risk sectors, such as telecommunications, scientific research and development and IT services.
- Medium-sized enterprises that scale up are a driving force of competitiveness and often contribute to increase aggregate productivity by ensuring coordination and upgrading of smaller suppliers.
- Participation in global value chains (GVCs) allows SMEs to scale up and increase productivity, especially in sectors that are at the centre of global production networks.
- The digital transition triggers new and different forms of business growth, with some companies able to achieve a substantial scale without an important mass of employees or other tangible assets. However, digitalisation also increases the need for skills upgrading and investment in complementary assets.
- A coordinated policy approach is needed to support the scaling up of SMEs and start-ups. Institutional and regulatory settings are crucial, as well as policies to ease SMEs access to markets and strategic resources for scaling up, including growth capital, workers and management skills, as well as knowledge and technology. Strengthening partnerships between SMEs, large firms, investors, Universities and research centres, including at the local level, can spur SME growth.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

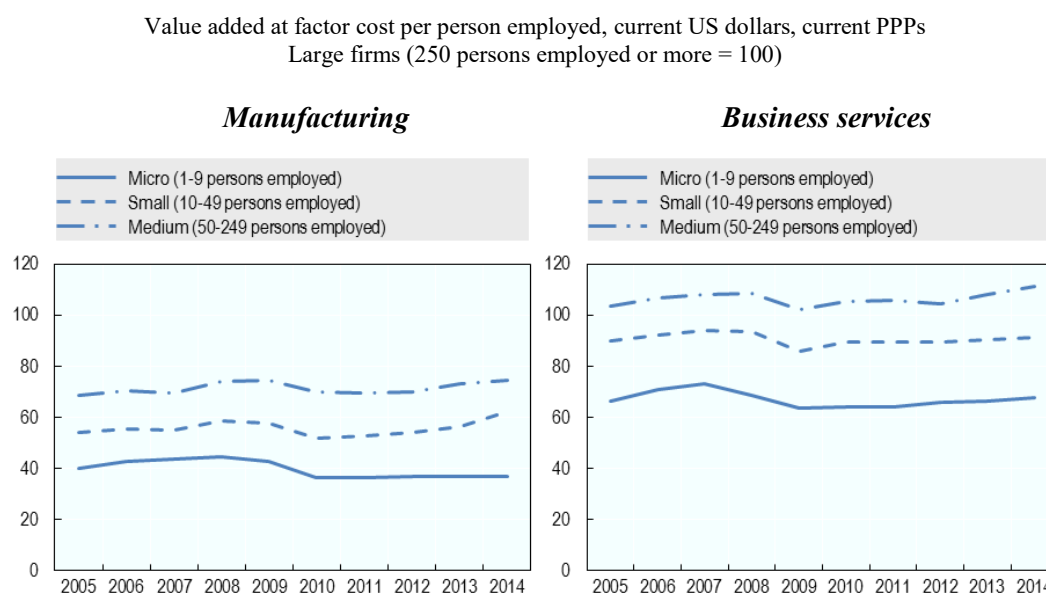
The scaling up of SMEs is key to boost productivity and achieve inclusive growth

The dynamics of SMEs and entrepreneurship is a key underpinning for productivity enhancement and inclusive growth. SMEs that grow, in terms of employees, turnover profitability or market share, can have a considerable impact on employment creation, innovation, productivity growth and the competitiveness of national and sub-national economies, as well as contribute to raising wage and income levels. Scaling up may be sought following the start-up phase, but also at other moments in the life of a firm, for example to satisfy a major increase in demand, strengthen a competitive position, or seize new opportunities in markets.

In many countries, enabling SMEs to seize growth opportunities over time is a policy priority to address low productivity growth and widening wage and income gaps. Across countries, there is in general a persistent productivity gap between SMEs and large firms. To the extent that large firms can exploit increasing returns to scale, productivity typically increases with firm size, although some variability across sectors and countries is observed. In particular, in the services sector, medium-sized firms outperform large firms in some countries, exhibiting competitive advantages in niche, high-brand or high intellectual property content activities, as well as the intensive use of affordable ICT.

In some OECD countries, the gap in productivity between SMEs and large firms increased in aftermath of the crisis. While for small and medium-sized enterprises there has been a reversal in this trend during the recovery, the larger gap has become persistent for micro-firms, especially in manufacturing (Figure 2.1).

Figure 2.1. The productivity gap between large firms and smaller SMEs has widened in some OECD countries since the global crisis



Note: Data cover Austria, Czech Republic, Estonia, Germany, Hungary, Italy, Latvia, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, and United Kingdom. Data for manufacturing (10-33 of ISIC rev.4) and business services, excluding financial services (45-82 less K of ISIC rev.4).

Source: OECD Structural Business Statistics (database), November 2017.

Productivity growth is faster when businesses can grow... and shrink

Across countries, the distribution of business growth exhibits large similarities, with most firms experiencing modest or zero growth, and a relatively small share of firms that are expanding or contracting. However, evidence shows that productivity grows faster in competitive environments, where the share of firms that expand and shrink is higher.

A dynamic distribution of firm growth is linked to innovation, as it reflects a business environment where firms experiment with new projects, scale them up when successful, and are able to back track and shrink when unsuccessful (Bravo-Biosca, 2010). Furthermore, expanding SMEs contribute to innovation and higher productivity indirectly, by contesting markets and forcing other firms to invest and upgrade (OECD, 2010a).

SMEs can experience high-growth at different stages of their life cycle, generating benefits for the economy

High-growth firms (HGFs) are firms that grow rapidly over a short period of time¹. They typically represent a small share of total businesses, but account for a larger share of employment. For example, when considering established companies with more than 10 employees, in 2015 in Israel HGFs represented 4% of firms but accounted for 10% of employment (OECD, 2017b).

While there may be a short-term trade-off between rapid employment growth and productivity growth, evidence suggests that, in the long run, HGFs have higher productivity growth than other firms, since they are more innovative and invest heavily in human capital (Du and Temouri, 2014; OECD, forthcoming). Furthermore, HGFs provide an indirect contribution to productivity growth by sparking new demand for advanced products and services, generating knowledge spill-overs which other nascent or existing enterprises can harness, and strengthening the local entrepreneurial culture by acting as role models for future and nascent entrepreneurs (OECD, forthcoming; OECD 2010a).

... but high growth is a transitory stage in the life of firms

Evidence suggests that "high growth" represents a transitory phase in the life of firms, which may have different characteristics and operate in many sectors (OECD, 2010a). In fact, there is no consistent pattern across countries as to which sectors host the largest share of high-growth enterprises. For example, in France and Sweden the rate of high-growth enterprises is higher in the services than in the industry sector, while in Hungary and Latvia the opposite is true. However, countries with a comparatively large share of HGFs in one activity tend to have a large share of HGFs in other activities, too, suggesting that the drivers of high growth are strongly influenced by the underlying business environment (OECD, 2017b).

While HGFs are more common in regions with high population density and skilled human capital (i.e. large urban areas), especially in the services industry, they can also sprout in peripheral regions, where their impact on net job creation and social inclusion can be significant (OECD, forthcoming).

Evidence suggests that established firms account for the largest share of HGFs. For instance, in 2014 in Canada and in 2015 in New Zealand respectively, 82% and 87% of HGFs were more than 5 years old (OECD, 2017b). However, within a given size class,

young firms (less than 5 years) appear more likely to be high-growth firms than their older counterparts (Bravo-Biosca, 2010).

HGFs tend to be innovative, but are not necessarily found in high-tech sectors; in some countries, for instance, they appear to be overrepresented in the business-to-business services segment. Very few high-growth firms are university spin-offs, while a larger share are corporate spinouts, suggesting the importance of knowledge channels and close interaction with customers and other entrepreneurs to seize growth opportunities (OECD, forthcoming).

Growing fast can also put considerable pressure on managerial, financial and technical resources, and growing firms may need to address new risks that scaling up can bring. In particular, difficulties in supporting the leadership capabilities of SMEs, such as through an expansion of the leadership team around the founder, have been identified as a key barrier to growth (OECD, 2010a; Goldman Sachs, 2015).

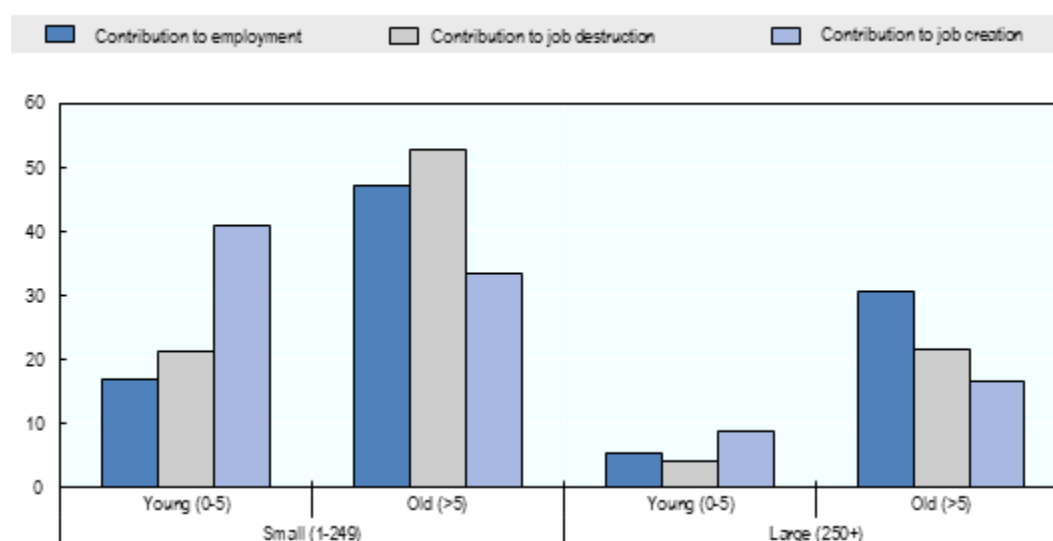
Furthermore, while high growth is the result of a mix of factors, growth ambitions, skills and personal experience of the entrepreneur, such as international experience and links to knowledge networks, are critical (Richbell et al., 2006; Moen et al., 2016). In fact, most entrepreneurs do not wish to grow, especially in employment, even under favourable macroeconomic conditions. A survey among UK SMEs, for example, indicates that only about 15% of firms have substantive growth ambitions (TBR, 2016). The entrepreneurial eco-system is important for nurturing the growth ambitions of SMEs, and policies can have an impact on aspirations of current and potential entrepreneurs, through entrepreneurship education and training, support to peer-to-peer networks and collaboration between entrepreneurs and knowledge centres, and promotion of role models. Still, a better understanding of what types of measures might be most effective in different contexts is needed.

Start-ups that scale up provide a key contribution to job creation...

Start-ups are a key source of radical and disruptive innovations and young firms contribute disproportionately to net job creation: the share of young SMEs in total job creation is about twice as large as their share in total job destruction or in total employment. The same is true for young large firms, although there are relatively few such firms. Older SMEs and older large firms continue to account for the bulk of employment across countries, but create fewer jobs than they destroy (Figure 2.2).

Figure 2.2. Young firms are a key driver of job creation

Employment, job destruction and job creation by firm age and size

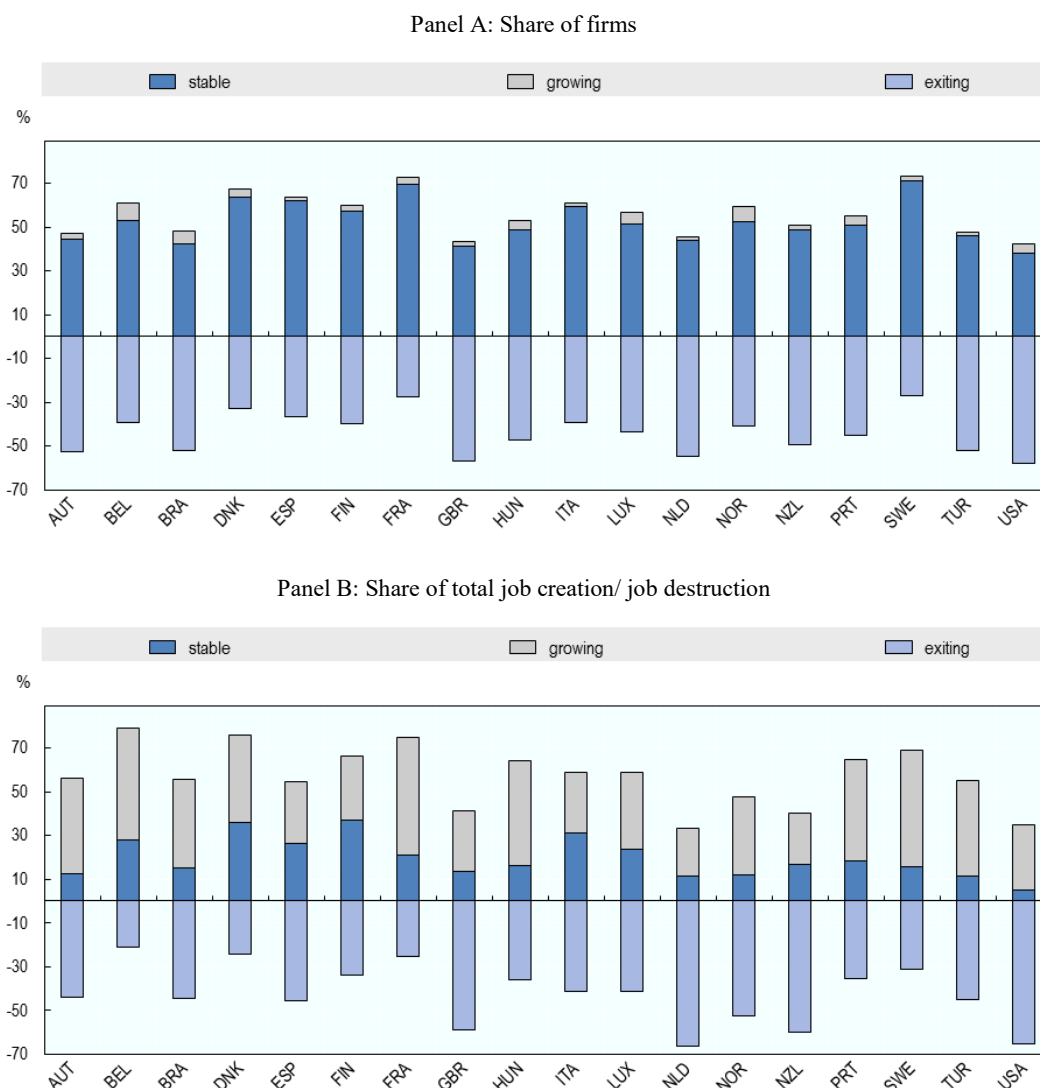


Note: Data cover eighteen countries and firms in manufacturing, construction and non-financial business services, and refer to the 2001-11 period for most countries. Owing to methodological differences, figures may deviate from officially published national statistics.

Source: Criscuolo et al. (2014) based on the OECD DynEmp Express database.

Start-ups that grow represent only a tiny fraction of all start-ups. However, it is the rapid scaling up of a small number of very successful start-ups that drives the large overall job creation by young firms. For instance, only 4% of micro-start-ups grow on average, but they contribute disproportionately to new jobs in this segment: between 22% (the Netherlands) and 53% (France) (Figure 2.3).

In contrast, most start-ups either fail in the first years of activity or remain very small. For instance, Figure 3 shows that out of 100 micro start-ups entering the market in a given year, after five years 26 to 58 are not active, 36 to 71 have still less than 10 employees, and only 1 to 8 have 10 employees or more. The large number of failing young firms is due to the distinctive “up-or-out” dynamics of start-ups, where high average growth rates co-exist with low survival rates. This happens to a much larger extent for young firms than for older incumbents (Bartelsman et al., 2013; Criscuolo et al., 2017).

Figure 2.3. Few micro start-ups grow, but these contribute disproportionately to job

Note: Figures report the average for different time periods $t = 2001, 2004$ and 2007 , conditional on the availability of data. Panel A represents the share (in terms of number of units) of micro (0-9 employees) entrants at time t by their size class at time $t + 5$. Panel B represents the net contribution to aggregate flows (defined as net job creation by the group over the sum of the net job variations by all groups in absolute values) for micro (0-9 employees) entrants at time t by size class at time $t + 5$. Size classes are aggregated as follows: stable (0-9 employees), growing (10 or more employees) and exiting units. Owing to methodological differences, figures may deviate from officially published national statistics.

Source: Criscuolo et al. (2017) based on the OECD DynEmp v.2 database.

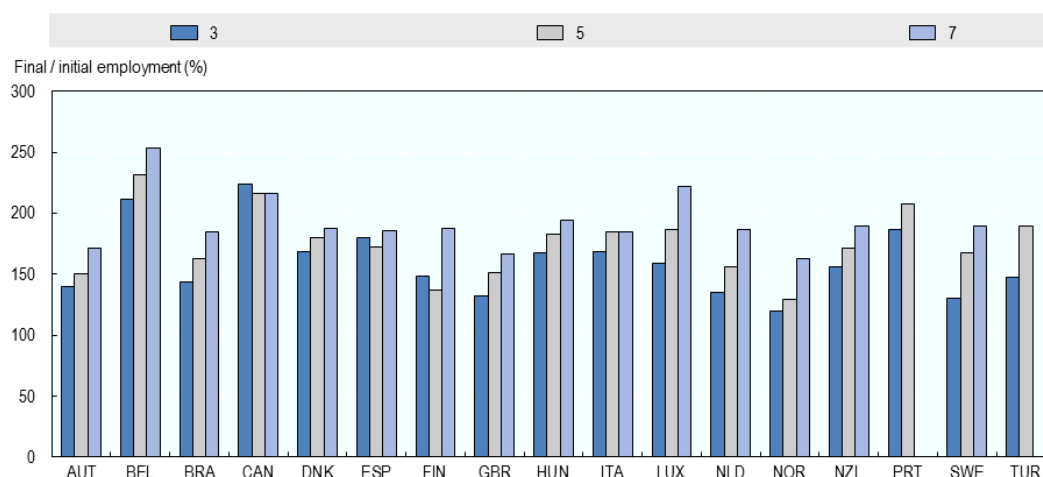
... but post-entry growth of start-ups varies widely across countries

There are sizeable differences across countries in the extent to which younger firms are able to scale up. Rapid expansion of successful young firms seems to be more of a feature of the United States than of other OECD economies (Calvino et al., 2016). The cross-country differences depend on the industrial structure and country size, but are likely to be also affected by institutional and policy settings. Figure 2.4 shows that although for all countries most of the growth of new entrants occurs in the first 2-3 years of activity, there

are significant differences across countries in the extent to which start-ups continue to grow in the following years. For instance, in countries like Belgium and Sweden, start-ups continue to grow also after five and seven years following entry, while in other countries – like Italy and Denmark – the trend is much flatter after the third year.

Figure 2.4. Post-entry growth varies across countries

Country average of final over initial employment for initial years 2001 and 2004, surviving entrants at 3, 5, and 7 years, in percent



Note: The graph shows the ratio between employment at time $t + j$ and employment at time t of surviving entrants. Figures report the average for different time periods $t = 2001$ and 2004 , conditional on their availability. Sectors covered are: manufacturing, construction, and non-financial business services. Each of the time lags $j = 3, 5, 7$ is reported separately. Owing to methodological differences, figures may deviate from officially published national statistics.

Source: Calvino et al. (2016) based on the OECD DynEmp v.2 database.

Medium-sized enterprises that scale up are key drivers of competitiveness

Established medium-sized enterprises that innovate and scale up are the driving force behind growth in many OECD economies, often ensuring the coordination, upgrading and participation in supply chains of smaller firms. For instance, in Italy, more than 60% of manufacturing medium-sized firms are located in industrial districts and play a crucial role in driving local supply chains of specialised small producers, typically focusing on market niches which are created or dominated through product differentiation and continuous innovation (Coltorti and Venanzi, 2017).

In Germany, medium-sized enterprises (50-249 persons employed) represent 2.25% of the business population, but account for about 20% of jobs and value added (OECD, 2017b). Studies find that independent German companies in the range of 50-749 employees are more productive and efficient than their larger counterparts (Holz, 2013).

Increasingly, governments are focusing on enabling conditions for the scaling up of mid-size companies, and the growth of small firms into mid-size ones, as a lever to boost productivity growth and competitiveness. For instance, in France, since 2008, this attention has translated into an official statistical recognition, through the creation of a new category of observation and policy target, the ETI (Entreprises de Taille Intermediaire), including firms with 250-5 000 employees and turnover between EUR 50 million and 1.5 billion.

SMEs can achieve scale through different mechanisms, including external growth

The growth journey of SMEs can take different pace and forms, including organic (i.e. internally generated) and non-organic growth (i.e. through mergers and acquisitions, joint-ventures or alliances).

There are multiple driving forces that can push a SME into domestic and international strategic alliances, such as the increasing rate of technological change, globalisation of markets, and increased customers' demand for quality and timeliness (Hoffman and Viswanathan, 1997). Alliances enable small firms to access critical resources, complementary assets and markets, particularly international markets that typically require a larger scale. Moreover, alliances can strengthen trust-based relations in business networks. At the same time, forming and managing alliances can be costly and challenging for a small business, also due to power disparities and asymmetries among the partners (Das, 2015).

Mergers and acquisitions (M&As) represent another non-negligible channel to achieve external growth for SMEs. Over 1996-2007, across Europe and the US, M&As by SMEs accounted for 20% of total deals involving firms from the same country. Furthermore, evidence shows that acquiring SMEs tend to rely more intensively than large firms on M&As to grow rather than to limit competition, i.e. acquiring SMEs largely seek synergies with the target firm in order to seize growth opportunities and increase the value of the firm (Weitzel and McCarthy, 2011).

Digitalisation is a powerful engine to scale up, enabling new modes of growth

The digital economy opens a range of new opportunities for scaling up, reducing costs, and enabling the creation of new business models that can challenge existing ones in radically novel ways (Goldfarb and Tucker, 2017). SMEs can draw many potential benefits from digital technologies, such as better access to skills, talent or markets, better collaboration and communication, or greater access to novel technologies and applications. Recent evidence shows that the use of digital tools enables access to international market also for micro enterprises (OECD, 2017b). However, compared to large firms, SMEs' uptake of ICT is lower and they face higher barriers to the adoption of several digital technologies in their operational activities (OECD, 2017c).

Competition in the digital economy appears to be affected by network externalities (among other factors), where the value of a product or a service to its users increases with the number of users. This may lead to the emergence of winner-take-most dynamics, the implications of which deserve particular attention (Autor et al.; Andrews et al., 2016).

These changes in the nature of competition can also be associated with the emergence of different forms of business growth, with some companies able to achieve a substantial scale via the use of digital technologies without an important mass of employees or other tangible assets.

To realise the full potential of the digital transformation, including to scale up, firms need to upgrade the skills of workers and management and to invest in complementary knowledge-based capital, such as research and development (R&D), data, and new organisational processes.

Participation in global markets and GVCs can also spur growth

While domestic demand remains central to most SMEs, global value chains (GVCs) present particular opportunities for SME growth, as they allow firms to specialise in specific activities within production networks, rather than compete along the entire line of activities, and can spur complementary investments in technology, process innovation or organisational change (Lileeva and Treffer, 2010; Caliendo and Rossi-Hansberg, 2012). GVC participation may also increase productivity, for example through increased foreign competition and access to new varieties of inputs and knowledge spillovers from foreign frontier firms (Amiti and Konings, 2007; Saia et al., 2015).

However, while trade and investment liberalisation and the digital transformation have contributed to an increased cross-border fragmentation, trade costs and restrictions remain which affect SMEs disproportionately. Also, the impact of GVCs on SME upscaling and growth is dependent upon the position in the global production network, the quality of infrastructures, the policy environment and access to strategic resources. For example, GVC participation typically requires additional capital to finance exports and address the working capital needs that may arise from the delays between production and payment from foreign customers (WTO, 2016). To fully leverage new sources of knowledge, including through FDI linkages, firms need to be able to upscale and make complementary investments in skills, management organisation and processes (Brynjolfsson and Hitt, 2000). Accordingly, policies that impede labour market flexibility may weaken the linkages between SMEs' position within GVCs and their growth (Criscuolo and Timmis, 2018).

Policy can play a role in enabling SMEs to scale up

Policy can support SME scale-up, by fostering a dynamic business environment that facilitates entrepreneurship and enables firms of all sizes to reach their full potential, including through better integration in global markets and value chains. This includes adopting a broader, more inclusive approach to productivity growth that considers how to expand the productive assets of an economy and provide an environment, in which all firms have a chance to seize growth opportunities, including in lagging regions.

Targeted policies can ease access to and effective use of strategic resources by growth-oriented entrepreneurs and SMEs, including finance, skills, technology and knowledge. These policies must take place against the backdrop of sound framework conditions, including the institutional and regulatory framework, in order to incentivise risk-taking and experimentation by entrepreneurs, and ensure that business growth potential can be realised.

Improved access to finance is needed to boost SME scale-up

Difficulties in accessing finance are widely recognised as one of the major obstacles for starting and growing a business (OECD, 2006, 2015a). Lack of finance prevents SMEs from investing in innovative projects, improving their productivity, and seizing opportunities in expanding or new markets.

In credit markets, adverse selection and moral hazard are exacerbated in the case of young, innovative businesses without loan history or collateral to secure a loan. Due to their higher risk profile, fast-growing companies also typically suffer from higher loan rejection rates than averagely performing firms (OECD, 2015a). At the same time, traditional debt may be ill-suited for new, innovative and fast-growing companies, which have a higher risk-

return profile. The “financing gap” affecting these businesses is in fact often a “growth capital gap”. Financing constraints can be especially severe in the case of start-ups or small businesses whose business model relies on intangibles which are highly firm-specific and difficult to use as collateral in traditional debt relations. Capital gaps also exist for companies seeking to undergo important transitions in their activities, such as ownership and control changes, or entry into new markets, including international ones.

Evidence shows that industries that are more dependent on external finance grow relatively faster in countries with more developed financial markets, i.e. where firms can access a range of alternative financing instruments. Appropriate access to finance also improves post-entry performance of firms, even when controlling for the size of entrants². Yet, in many countries, there are few alternatives to traditional debt for most enterprises (OECD, 2015b).

The G20/OECD High-Level Principles on SME Financing call for strengthening bank lending, while broadening the range of instruments available to SMEs and entrepreneurs at different stages of their life cycle, including asset-based finance, hybrid instruments (e.g. mezzanine finance) and equity finance (OECD, 2015c). In recent years, governments have been stepping up efforts to address SMEs’ growth capital gaps. For instance, in the EU, in the framework of the Programme for the Competitiveness of Enterprises and Small and Medium-sized Enterprises (COSME), the Equity Facility for Growth supports SME growth, research and innovation through investment in venture capital and mezzanine finance funds. Austria’s federal development and financing bank for the promotion and financing of companies (aws) offers guarantees of mezzanine investments in SMEs aimed at modernisation, expansion or acquisition of other companies. In Italy, in 2012 regulation was introduced for new debt security instruments (“mini-bonds”), which under certain conditions can be issued by unlisted SMEs.

Strong entrepreneurial and management skills and access to talent are necessary for SME growth...

High growth is a disruptive process that alters the organisational dynamics and management practices of an enterprise, and new leadership and management skills are often needed to cope with this process (OECD, 2010a). SME founders usually have specific expertise, while growth often requires an expanded skillset to channel the emerging complexities: from commercial (e.g. marketing and serving of new offers), to project management (e.g. logistics, organisations of events), financial (e.g. capital and cash flow management) and strategic thinking skills (e.g. building internal leadership, coordinating sets of actions to fulfil new strategic objectives). Smaller firms may face a particular challenge in this regard, as their limited human resources are focused on day-to-day running of the business (Hellman and Kavadia, 2016).

Upskilling of existing staff, including management, is key for SMEs to undertake growth-oriented strategies. However, there is evidence that SME training efforts are on average significantly weaker per employee than in larger firms (OECD, 2013a). Also, SMEs appear to be relatively behind in the use of company-level learning strategies, i.e. the use of managerial practices and methods that promote workers’ learning and autonomy (OECD, 2015d).

Moreover, it is often very difficult for SMEs both to find and to retain skilled and high-qualified personnel in order to sustain growth. In Canada, a recent survey among SMEs shows that 55% of all SMEs and 80% of mid-sized businesses identify this as a major hindrance to growth (BDC, 2016). In the UK, around 20% of SMEs report that finding

people with the right skills is a barrier to business growth (BIS, 2013a), a share that rises to 50% when considering high-growth firms (Coutu, 2014). Leaders of scale-up companies indicate that access to talent is their most pressing problem to address customer orders.

In this regard, policies that support skills development in SMEs and enable small businesses to attract and retain qualified personnel, both within and across the border, are essential to boost growth. For instance, in Ireland, the National Training Fund (NTF) supports training networks (“Skillnets”) formed by private sector businesses in the same sector and/or region that have come together to carry out training-related activities that may not be possible on their own. In 2015, SPRING Singapore launched the Human Capital Movement, which helps SMEs to attract and retain talent, through the sharing of best practices with experienced Human Resource Directors, human capital advocates, learning forums, workshops, career fairs and student events aimed at highlighting good career opportunities in SMEs. To address gaps in the skill set of high-growth firms, in 2015, the Business Development Bank of Canada (BDC) created a new division, BDC Advantage, devoted exclusively to providing high-impact firms with advice, formal management training, peer to peer networking and referrals to outside consulting (OECD, 2017d).

Furthermore, labour mobility can be important, since growth-oriented firms face inherent uncertainty about their future prospects. Evidence shows that stricter employment protection legislation leads to slower firm growth in sectors which are more labour-intensive, more innovative, or characterised by greater uncertainty. It increases the share of firms that neither grow nor shrink, but it also reduces growth among the best performing firms, and contraction among the underperforming ones (Bravo-Biosca et al., 2016; Calvino et al., 2016).

...as are access to knowledge and the ability to innovate

To seize market opportunities and grow, SMEs need to be able to access state-of-the-art knowledge and implement it in their operations through innovation. Importantly, innovation does not only involve research and development (R&D) activities, but also the introduction of new products, services, processes and business models. Policies aiming to support SME growth through innovation should thus go beyond traditional R&D policies and also focus on other modes of innovation. For example, they can provide advice and training to start-up entrepreneurs, who have strong technological knowledge, but lack market and commercial expertise, and they can promote corporate and university spinoffs with initiatives for proof-of-concept, pre-competitive research and seed funding (OECD, 2010b). For instance, in Germany, the EXIST-Transfer of Research programme provides support to research teams at universities or research institutes to develop proof for the technological feasibility of their product idea and to prepare business start-up.

Furthermore, SME innovation is often the outcome of collaborative efforts in which businesses interact and exchange knowledge and information with other partners, as part of broader innovation systems. In this regard, facilitating knowledge flows and promoting partnerships among SMEs and between SMEs and large firms, investors, Universities and research centres, including at the local level, can enhance SME growth prospects. Soft innovation infrastructures, in the form of science parks and business incubators, may create opportunities for innovation partnerships and collaborative research, promote skilled labour mobility, and facilitate the commercialisation of university research. In knowledge-intensive sectors, which are characterised by strong spatial clustering, policies can stimulate knowledge flows, for example, through programmes that facilitate informal interactions among entrepreneurs and by encouraging universities to get involved in “third

mission” activities, such as knowledge exchange, technology transfer and cooperation with private enterprises (OECD, 2010b). As a case in point, in 2015, the Catapult network was launched in the United Kingdom, consisting of world-lead centres focused on a specific area of technology and expertise with great potential, which connect nascent entrepreneurs and businesses of all sizes with academia and research institutions.

Foreign direct investment represents another relevant vector for knowledge and innovation that can benefit SME growth. Policies should foster a business environment that is conducive to inflows of foreign direct investment and promote links between foreign subsidiaries and domestic firms in the form of supplier-buyer relationships, joint ventures and joint technology development and training. Strengthening skills is especially important to enable SMEs meet requirements of multinational enterprises, absorb new technologies, and develop relationships that foster the diffusion of knowledge (OECD, 2017e).

The management of intangible assets (IA) is critical for turning SMEs’ innovation potential into market value, competitiveness and growth. However, SMEs are lagging behind larger firms in recognising, exploiting and protecting their intellectual property. To better enable SMEs to leverage their intangibles, policies should target both internal obstacles, such as lack of knowledge and strategic perspective, and the hurdles that affect the accessibility of the IP system for SMEs, such as administrative burdens and complex and costly litigation and enforcement mechanisms (OECD, 2011a). National guidelines on IA management and reporting exist in several OECD countries. For instance, in France, in 2011, the *Observatoire de l’Immateriel*, supported by the Ministry of Finance, released a methodology for the valuation of intangibles to complement existing business financial reporting, with the aim to improve firms’ communication on their IA and internal metrics (OECD, 2013b).

Framework policies are critical to unleashing the growth potential of young firms and SMEs, especially in high-risk sectors

Targeted policies for SME growth can only be effective against the backdrop of sound framework conditions. SMEs are typically more dependent than large companies on their business ecosystem and, due to their internal constraints, are more vulnerable to market failures, policy inefficiencies and inconsistencies, which may arise in different areas or result from the interaction of regulatory and policy approaches across different areas.

Start-ups are particularly exposed to the policy environment and local and national framework conditions, due in part to credit constraints and weaker resilience relative to incumbents. The effect of policies on the growth of young firms is especially pronounced in high-risk sectors, such as telecommunications, scientific research and development and IT services (Calvino et al., 2016). Regulations may also be tailored to the prevailing technology adopted by incumbents, rather than to the innovative technology used by start-ups. Even if this is not the case, entrants may be less familiar with the policy environment, which may increase their adjustment costs.

Institutional and regulatory settings are crucial to ensure that businesses of all sizes compete on a level playing field. An effective and transparent regulatory environment is key to business growth, and an increasing number of countries are adopting regulatory impact analysis (RIA) to assess the effects of proposed and existing regulations on businesses, including on SMEs. Also, regulatory policy bodies, with responsibility for regulatory oversight, have been established in many countries to ensure that regulation serves whole-of-government policy. An example of a central oversight body is the Regulatory Reform Committee (RRC) in Korea, set up in 1998 to provide strategic

perspective to regulatory reforms, to monitor the improvement efforts of relevant agencies and ensure coherence between their actions (OECD, 2011b).

Public sector transparency and integrity and competitive neutrality are also essential for a level playing field, including between public and private firms. Opacity and corruption in the public sector, which are detrimental to all businesses, pose particular problems for SMEs; and market entry and growth by new and small businesses can be limited when state-owned enterprises (SOEs) benefit from an unfair edge in domestic and cross-border activities, such as through financial support that lowers the cost of capital, tax concessions, preferential treatment in public procurement, regulatory privileges that support monopoly advantages and legal immunities (OECD, 2012, 2017f).

Effective contract enforcement and civil justice system support firm growth

Bankruptcy laws that ensure strong guarantees for investors without posing an excessive burden on entrepreneurs in case of failure matter for business investment and growth. Improving the efficiency of corporate bankruptcy procedures can foster labour productivity and value-added growth, notably in sectors that are most dependent on external finance, and be positively associated with GDP investment share (de Serres et al., 2006; Succurro, 2012). Entrepreneur-friendly personal bankruptcy regulations seem also to be positively associated with entrepreneurship development (Lee et al., 2011; Klapper et al., 2006). To this end, several OECD countries have reformed their bankruptcy regulation to allow for automatic discharge, i.e. discharge takes place at the payment of the quota agreed upon in the enterprise insolvency proceeding, with no need for an additional court decision (OECD, 2017g).

The efficiency of the court and legal system is particularly important for SMEs, which typically need to divert a higher share of resources than large firms to resolving disputes (OECD, 2017g). Efficient judicial systems are intrinsically related to larger average firm size (Kumar et al., 1999; Giacomelli and Menon, forthcoming); and tend to improve the predictability of business relationships. Where courts are weak, on the other hand, firms are unwilling to interact with a new contractual partner, which particularly disadvantages entrants and limits their growth (Johnson et al., 2002). Weak contract enforcement is also associated with low relationship-specific investments which can further constrain start-ups' post-entry growth prospects (Nunn, 2007). In many OECD countries, governments have taken steps to enhance efficiency in courts. In Australia, for example, an electronic case and court management system is in place, whereby ICT is used to automate and support case management and ease transfer of information through the judicial system.

Potential disincentives to scaling up should be considered when devising size-contingent policies

Levelling the playing field, i.e. addressing competitive disadvantages for SMEs that stem from market failures, coordination failures and policy inefficiencies, is a common objective of SME policy. However, the role and effectiveness of framework and targeted policies, as well as potential trade-offs or distortionary effects of policy interventions are the object of conceptual debate and empirical assessment. In particular, policies that target firms below or above a certain size threshold may create disincentives for scaling up. For instance, in the case of regulatory simplification for SMEs, efficient firms may choose to remain small to avoid the additional regulatory burden related to crossing a certain threshold.

A coordinated policy approach is needed to devise mutually reinforcing policies for SME scale-up

The policies and frameworks which influence SME scale-up are interconnected and often cut across the boundaries of different ministries, government agencies, levels of government and administration. Furthermore, supporting business growth requires a long-term perspective and coherence over time, since the impact of policies on firm growth performance are mainly visible in the mid- to long run. In this sense, a whole-of-government perspective is needed, taking into account policy synergies and trade-offs across different domains.

In recent years, a number of scale-up strategies have been launched, which recognise the need to consider SME growth opportunities over time and craft coherent and mutually reinforcing policies across different domains. These approaches typically reflect that SME growth requires efforts on a number of fronts, including institutional and regulatory frameworks, conditions to access local and international markets, and timely access to resources that are essential to seize growth opportunities, including finance, skills, knowledge and technology.

An important example of such an approach is the European Commission's *Start-Up and Scale-Up Initiative*, launched in November 2016, which aims to address key challenges to business growth by articulating initiatives in a coherent way. In a similar vein, in 2013, the UK government launched the initiative "Small business: GREAT Ambition", which encompasses all the government's efforts to make it easier for small businesses to grow (BIS, 2013b).

Furthermore, several governments are taking initiatives to strengthen and consolidate services that are offered to scale-up firms, including by fostering synergies among the different players which provide growth-facilitating services or products. For example, in 2016, in Denmark five regional authorities and the Ministry of Business and Growth launched "Scale-up Denmark", a project to establish multiple "scale-up hubs" specialised in different sectors, with the aim to offer a full set of services to growth-oriented entrepreneurs and small businesses³.

SMEs are often embedded in local eco-systems, which represent their primary source of knowledge, skills, finance, business opportunities and networks. In this regard, it is important to consider factors affecting framework conditions at the local level, and how scale-up policies developed at the national level are tailored to local conditions and link with policies designed and implemented at the local level. Local authorities often play a key role in the development of a conducive business environment, including through partnership with the business community, research organisations and investors, and multi-level governance is an important dimension of any coordinated policy approach to SME growth.

Notes

¹ The OECD-Eurostat Manual on Business Demography Statistics (2007) defines high-growth enterprises as “enterprises with an average annualised growth greater than 20% a year, over a 3-year period, and with 10 or more employees at the beginning of the observation period”. Growth is measured by turnover or employment, with the turnover definition giving higher numbers than the employment definition. Gazelles are the subset of high-growth enterprises which are up to five years old. In the European Union, the Commission implementing regulation (EU) No 439/2014 has lowered the recommended growth threshold to “greater than 10% per annum, over a three year period”.

² See Bravo-Biosca et al.(2016), Rajan and Zingales (1998), Aghion et al. (2007); and Klapper et al. (2006), among others.

³ <https://scale-updenmark.com/>

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3. Enhancing SME access to diversified financing instruments

Summary

- Across all stages of their life cycle, SMEs require access to appropriate sources of financing for their creation, survival and growth.
- Although SME access to bank finance largely recovered after the financial crisis, market failures and structural challenges remain, including information asymmetries, high transaction costs in servicing SMEs, and lack of financial skills and knowledge among small business owners.
- There is a need to broaden the range of financing instruments available to SMEs and entrepreneurs, in order to address diverse financing needs in varying circumstances, increase SMEs' resilience to changing conditions in credit markets and improve their contribution to economic growth.
- Alternative financing instruments offer opportunities to meet SME financing needs. However, their potential remains underdeveloped in most countries due to demand- and supply-side barriers. Capital market instruments for SMEs often operate in thin, illiquid financial markets, with a low number of participants and limited exit options for investors.
- The digital transformation holds potential to improve SME access to finance, offering unprecedented solutions to address barriers related to asymmetric information and collateral shortage. At the same time, it requires regulatory frameworks to support novel developments, while ensuring financial stability, consumer and investor protection.
- Governments have been stepping up efforts to foster a diversified financial offer for SMEs, following the two-pronged policy approach advocated by the G20/OECD High-Level Principles on SME Financing, which call for strengthening SME access to credit, while also supporting the diversification of their financing sources.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Access to finance is key to the creation, growth and productivity of SMEs

Financing for SMEs in the appropriate forms is important at all stages of the business life cycle, in order to enable these firms to start up, develop and grow, and make contributions to employment, growth and social inclusion.

Access to finance improves post-entry performance of start-ups and industries which are more dependent on external finance grow relatively faster in countries with more developed financial markets, thanks to enhanced information sharing and risk management, and a better allocation of resources to profitable investment projects (Rajan and Zingales, 1998; Giovannini et al., 2013). On the other hand, financing constraints that prevent firms from investing in innovative projects, seizing growth opportunities, or undertaking restructuring in case of distress negatively affect productivity, employment, innovation and income gaps.

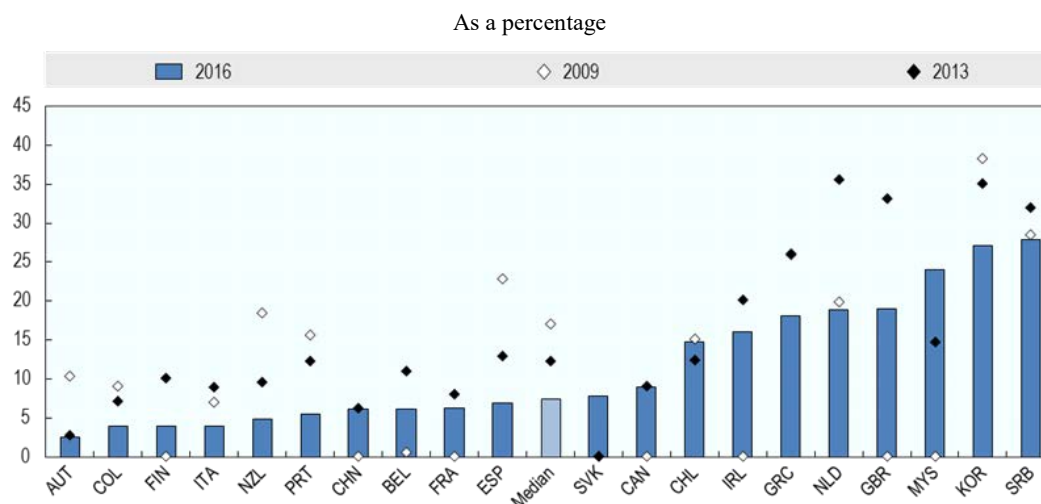
Longstanding challenges in accessing bank finance limit SME growth in many countries

Bank lending is the most common source of external finance for many SMEs and entrepreneurs, which are often heavily reliant on straight debt to fulfil their start-up, cash flow and investment needs (OECD, 2016a). SMEs, however, typically find themselves at a disadvantage with respect to large firms in accessing debt finance¹. Asymmetric information and agency problems, including high transaction costs, and SMEs' opacity limit access to credit by small businesses and start-ups, in particular, which are often under-collateralised, have limited credit history and, and may lack the expertise and skills needed to produce sophisticated financial statements (OECD, 2013). Access to debt finance is also more difficult for firms with a higher risk-return profile, such as innovative and growth-oriented enterprises, whose business model may rely on intangibles and whose profit patterns are often difficult to forecast (OECD, 2015).

In middle- and low-income countries, funding gaps are often even more pronounced and among the main barriers to small business formalisation. Moreover, while a large share of SMEs do not have access to formal credit, long-term credit to sustain investment and innovation is even scarcer, which severely limits growth opportunities (IFC, 2013).

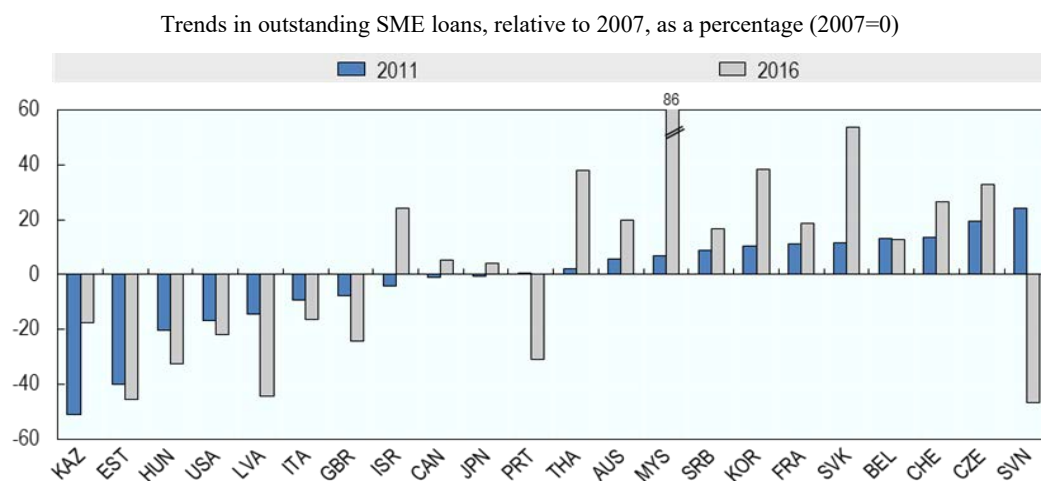
The recovery in SME lending following the crisis has been uneven

In many countries, the 2008-09 global economic and financial crisis exacerbated the financial constraints experienced by SMEs and resources dried up for the most dynamic enterprises. While in 2009, for instance, only 5.2% of loan applications were rejected among large firms, that share was double for small firms and even three times as large among micro businesses (European Commission, 2009). Although recent trends provide an indication of loosening credit conditions, large cross-country differences persist in the share of SMEs that experience full or partial rejection of their credit demand, which, in 2016, ranged from around 27% in Serbia and Korea, to 2.5% in Austria (Figure 3.1). In 2017, large firms continued to face a better financial situation and much lower bank loan rejection rates (1% vs. 6%) compared to SMEs (European Commission, 2017).

Figure 3.1. SME loan rejection rates vary greatly across countries

Source: OECD (2018).

The financial crisis illustrated the vulnerability of many SMEs to changes in the credit cycle. During the uneven recovery, often marked by GDP contraction or slow growth in many countries, credit to SMEs followed a similar pattern or contracted even more sharply, with the exception of some emerging economies, where business loans expanded at a sustained rate (Figure 3.2).

Figure 3.2. The recovery in SME lending has been uneven

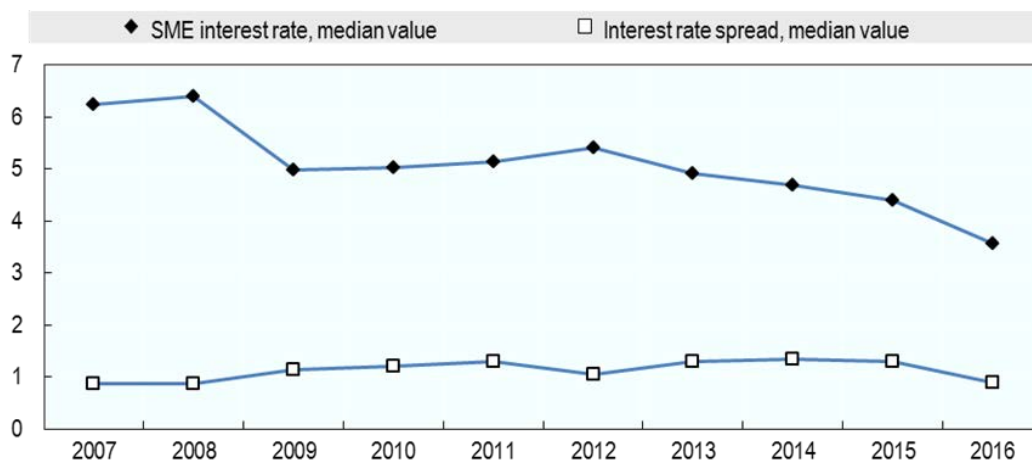
Source: OECD (2018)

In recent years, SMEs have found it easier to access credit and the economic environment in which they operate has generally improved, as evidenced by lower bankruptcy rates and shorter payment delays. However, this has not systematically led to more credit flowing to SMEs, in part due to weak credit demand and uneven investment opportunities (OECD, 2018a). Also, more rigorous prudential rules have led banks to modify their business model and adopt more stringent credit selection criteria.

In addition, declining interest rates have benefited large enterprises more than small ones, pointing to a persistently higher credit risk for SMEs. In fact, across a large number of countries, the spread in the average interest rates charged to SMEs and to large firms has widened compared to the pre-crisis period (Figure 3.3). In 2008, the median interest rate charged to SMEs was 15.5% higher than the rate charged to large enterprises, whereas in 2016, that percentage had more than doubled, standing at 32.7%.

Figure 3.3. The gap in credit costs between SMEs and large enterprises has widened

Average interest rate charged to SMEs and average spread between interest rates charged to SMEs and large enterprises, median values



Source: OECD (2018)

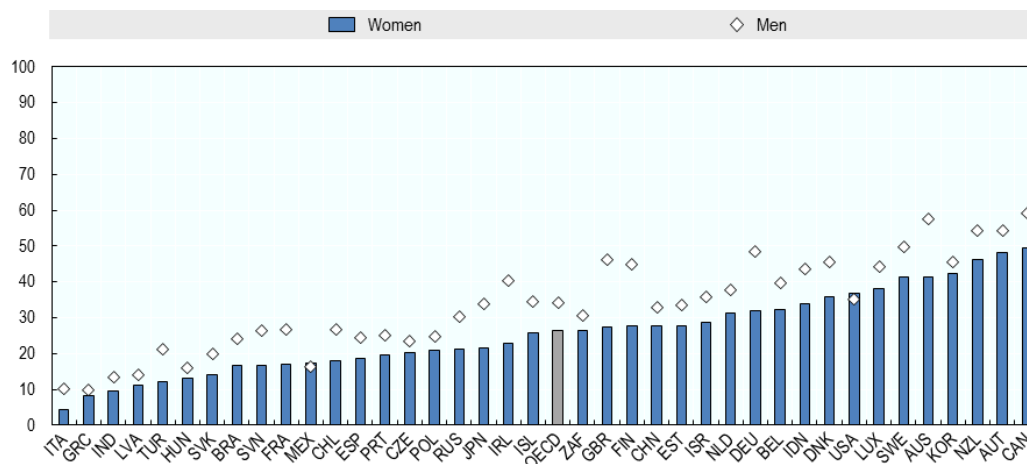
Certain categories of firms and entrepreneurs face higher barriers to accessing bank finance...

While credit has become more easily available for some SMEs, other segments of the SME population still face substantial difficulties in accessing debt finance. Transaction costs are particularly high in relative terms for micro-enterprises, start-ups, young SMEs, innovative firms and businesses located in remote and/or rural areas, potentially excluding them from any sources of formal external financing.

At the same time, these firms' financing needs tend to be high compared to their turnover and assets, and they usually lack assets that are easy to collateralise. Moreover, evidence suggests that financial institutions have become more risk-averse compared to the pre-crisis period, and that the financing constraints of these firms may have become more structurally entrenched (OECD, 2017a). In addition, certain categories of entrepreneurs, such as women, migrants or youth, often face additional obstacles to accessing financing in the appropriate volumes or forms. For instance, in many countries, women are much less confident than men that they can obtain the financing they need to start or grow a business (Figure 3.4).

Figure 3.4. Women believe they are less likely than men to have access to finance to start or grow a business

Proportion of individuals who answered “yes” to the question “Do you have access to the money you would need if you wanted to start or grow a business?” by gender, 2013



Source: OECD (2016), *Entrepreneurship at a Glance 2016*, OECD Publishing, Paris

...as do many SMEs in emerging economies, in part because of high levels of informality

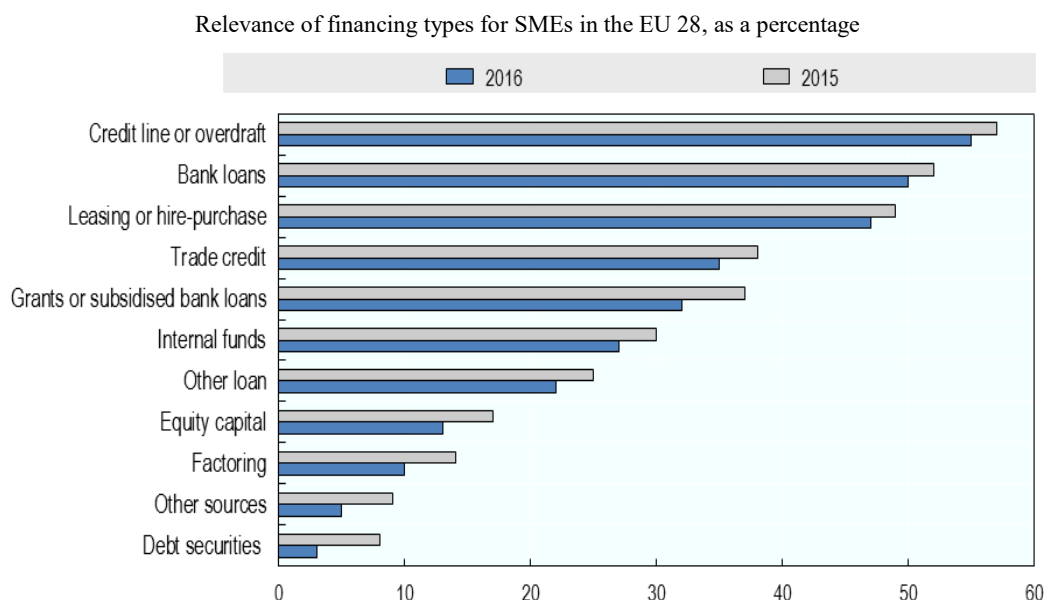
Small firms operating in developing countries are more likely to be credit-constrained and pay significantly higher interest rates than their counterparts in high-income countries. Firm-level data indicate that, while there are many barriers to SMEs' growth in emerging and developing markets, insufficient access to financing is particularly constraining and represents the most robust barrier to firm expansion within the business environment (Dinh et al., 2010).

In part, that is because as many as 80% of firms in developing countries are estimated to be active in the informal sector, employing around 60% of the labour force. These enterprises are often fully or partially excluded from formal financial sector. Their reliance on internal revenues and informal, often very expensive, sources of external financing inhibits their growth potential and is associated with increased firm illegality.

Overall, SMEs remain too dependent on straight debt ...

Many SMEs around the world remain heavily reliant on straight debt and are undercapitalised, which makes them more vulnerable to economic downturns and dependent on the health of the credit market. For instance, across eight continental European countries in 2014, bank loans constituted 23% of small and 20% of medium-sized firms' balance sheets, compared with only 11% for large firms (Deutsche Bank, 2014).

A more balanced capital structure may increase the likelihood of attracting bank credit at good conditions, and is associated with higher growth in employment and turnover (Brogi and Lagasio, 2016). However, only 13% of SMEs surveyed between October 2016 and March 2017 in the EU 28 considered equity financing as relevant for their business, i.e. had used it in the past or were considering doing so, a share significantly smaller than for most other sources of finance at their disposal (Figure 3.5).

Figure 3.5. SMEs continue to rely heavily on traditional debt instruments

Source: European Commission, 2015a and 2017

... in a context of less credit as the “new normal”

Notwithstanding recent improvements, trends point to a business environment in which less credit is becoming the “new normal”, also as a result of financial reforms, which affect SMEs and entrepreneurs disproportionately, with banks continuously modifying their business models in response to more rigorous prudential rules (OECD, 2015).

Against this backdrop, the long-standing need to strengthen SME capital structures and decrease their dependence on borrowing has become more urgent. While bank financing will continue to be crucial for SMEs, a more diversified set of financing options can contribute to reducing systemic risk, increasing the resilience of the real economy to large shocks, and enable SMEs to continue to play their role in investment, growth, innovation and employment.

There are opportunities for SMEs to tap into a wide range of alternative financing instruments

In recent years, an increasing range of financing options has become available to SMEs, although some of these are still at an early stage of development or, in their current form, only accessible to a small share of SMEs.

While debt finance offers moderate returns for lenders and is therefore appropriate for low-to-moderate risk profiles, i.e. firms that are characterised by stable cash flow, modest growth, tested business models, and access to collateral or guarantees, alternative financing instruments alter this traditional risk sharing mechanism. These instruments consist of multiple and competing sources of finance for SMEs, including asset-based finance, alternative forms of debt, hybrid tools and equity instruments and not all are suitable and of interest for all enterprises, depending on their risk-return profile, stage in the business life cycle, size, scale, management structure and financial skills (Table 3.1).

Table 3.1. Suitability of alternative financing instruments for different firm profiles and stages

Type of financing instrument		Profile and stage of firm
Low risk / return	- Asset-Based Finance - Asset-based lending - Factoring - Purchase order finance - Warehouse receipts - Leasing	- Start-ups - Firms with limited credit history and lack of collateral - Fast growing and cash-strapped firms - Firms with solid base of customers but high investments in intangibles - High-risk and informationally non-transparent firms - Firms changing their capital assets frequently - Producers and traders of commodities
	- Alternative Debt - Corporate bonds - Securitised debt - Covered bonds - Venture debt - Private placements - Crowdfunding (debt)	- Large to mid-size firms with stable earnings and relatively low cash flow volatility - Firms responding to reporting requirements linked to issuance - Firms undertaking investment or seizing growth opportunities - Firms that do not wish dilution of ownership and control - Smaller companies with limited visibility in public markets (<i>private placements</i>) - Firms lacking collateral or credit history (<i>debt crowdfunding</i>)
Medium risk / return	"Hybrid" Instruments - Subordinated loans/ bonds - Silent participations - Participating loans - Profit participation rights - Convertible bonds - Bonds with warrants - Mezzanine finance	- Young high-growth firms seeking cheaper expansion capital than VC and less dilution of control - Established firms with emerging growth opportunities - Firms undergoing transition and restructuring - Firms seeking to strengthen capital structure - Firms with well-established and stable earning power and market position
	Equity Instruments	
High risk/ return	Private equity	Business angel investments - Firms in their seed and early investment stage - Innovative ventures requiring investment and business-building skills
		Crowdfunding (equity)
		Venture capital - Firms in their seed, early and late investment stage - High-growth-potential firms, with capacity for high returns in a short time frame
	Public equity	Other private equity - Mature businesses undertaking restructuring or ownership change - Distressed businesses with potential for rescue
		Specialised platforms for public listing of SMEs - Young, innovative and high-risk small firms - Firms with highly structured governance and management systems, and extensive disclosure

Source: Adapted from OECD (2015).

Finance instruments that pose fewer risks to investors can flourish more readily and even in the absence of comprehensive, transparent, and standardised credit data, especially when backed by collateral or guarantees by the enterprise. Accessing asset-based finance, in particular, depends on the liquidation value of the underlying asset, rather than on the creditworthiness of the business. Survey data also show that these instruments are more widely known and used by entrepreneurs compared to riskier finance instruments (OECD, 2015).

Equity finance holds particular promise for firms with a high risk-return profile, such as new and innovative SMEs. Seed and early stage equity finance can boost firm creation and growth, while other equity instruments, such as specialised platforms for SME public listing, can provide financial resources to growth-oriented SMEs. Business angel investment may also play a significant role, although it is difficult to estimate their weight in SME financing due to data issues (OECD, 2015).

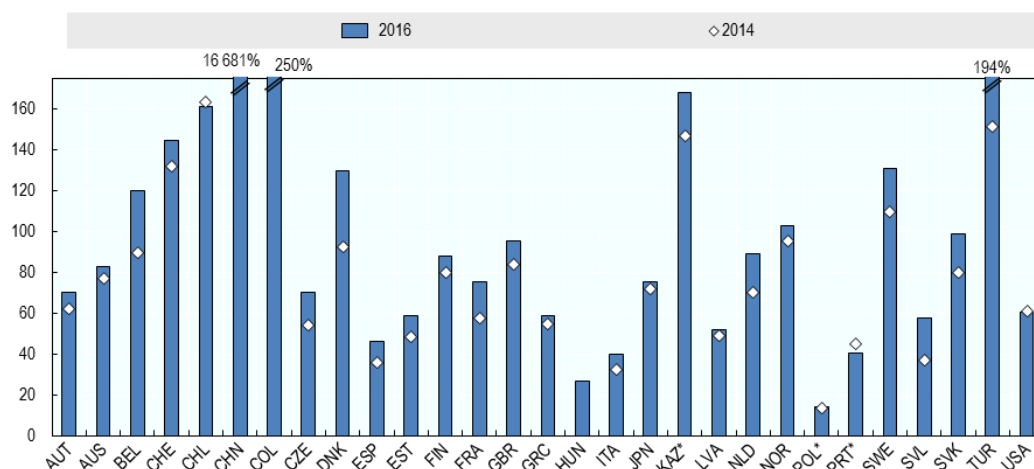
The private capital market, through a full range of debt and equity instruments, offers advantages for small firms with a higher risk profile seeking flexible form and conditions. Finance through capital markets often complements rather than replaces bank financing; banks typically provide short-term working capital, and may work with investors in order to steer companies toward a mix of financial products that suits their needs. This pattern of financing might become more prevalent in the future, with banks operating at the short-term low-risk part of the market, while investors focus on higher-risk high-reward and low liquidity operations (OECD, 2017b).

...but the development and use of alternative financing instruments by SMEs is highly uneven

Asset-based finance is widely used by SMEs across OECD countries, and increasingly in emerging economies, to meet their working capital needs, support domestic and international trade, and, in some cases, for investment purposes. In Europe especially, the prevalence of these instruments for SMEs is about on par with conventional bank lending. Moreover, asset-based finance has grown steadily over the last decade, in spite of repercussions of the global financial crisis on the supply side.

Figure 3.6. Leasing and hire purchases are on the rise

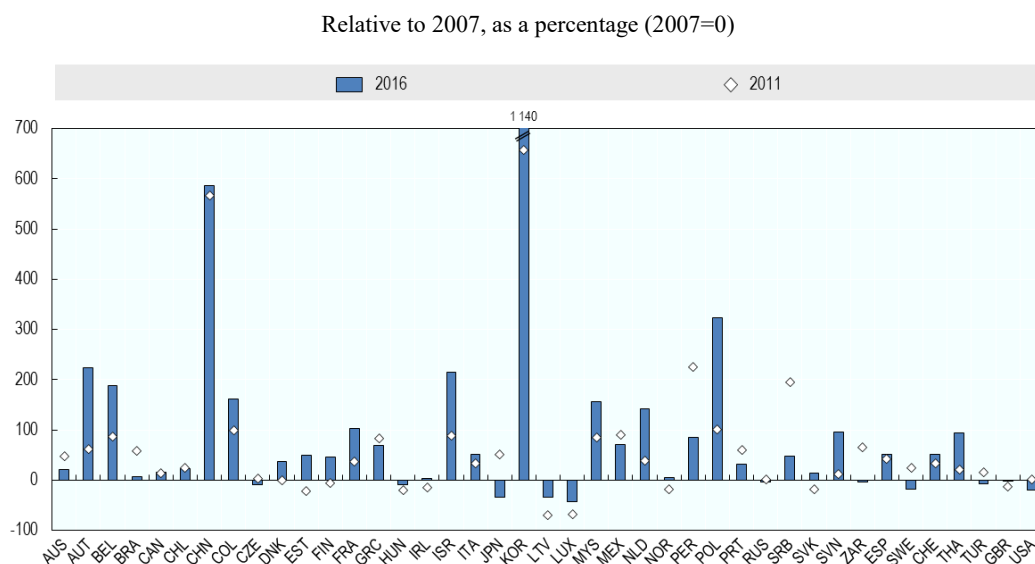
Yearly new production in leasing and hire purchases, relative to 2007 (2007=0), as a percentage



Note: For Hungary, China and Colombia, 2014 data is not available. Data is indexed to 2009 for Poland and Portugal and to 2010 for Kazakhstan. For Portugal, most recent observation refers to 2015.

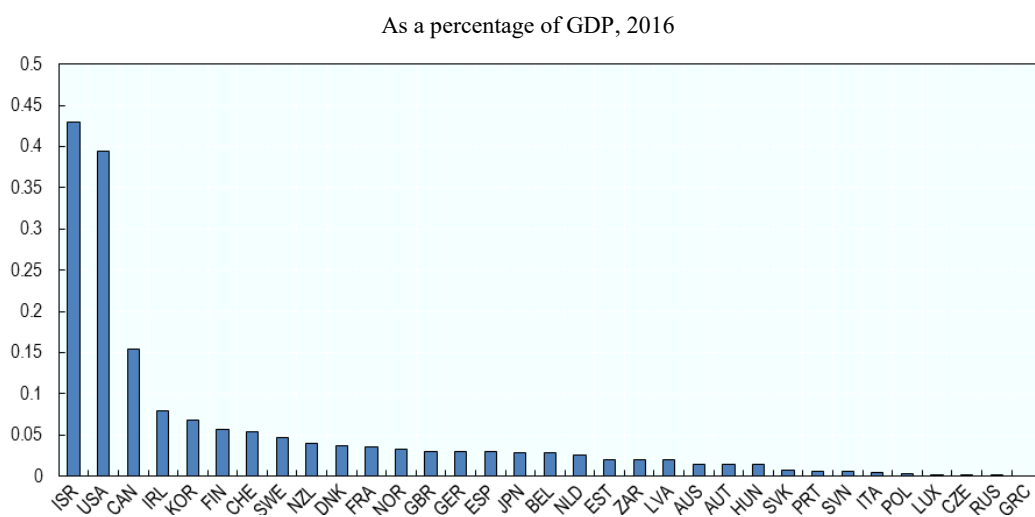
Source: Leaseurope (2017) and OECD (2018).

Factoring has become a more widely used and accepted alternative to liquidity-strapped SMEs in many countries, with volumes expanding significantly over the last decade, especially in emerging economies – although here often from a low base (Figure 3.7).

Figure 3.7. Factoring volumes are expanding, especially in emerging economies

Source: Factors Chain International (2017)

In contrast, venture and growth capital investments account for a very small share of SME financing, less than 0.03% of GDP in most OECD countries. However, the degree of development of capital market finance for SMEs differs widely among countries. Relative to the size of the economy, in Canada, Israel and the United States, venture capital investments are a multiple of activities in the Euro area. Even within continental Europe, large differences persist, with venture capital funding much more widely used in Finland, Sweden, and especially Switzerland, than in Central and Southern European countries (Figure 3.8).

Figure 3.8. Venture capital investments differ widely across countries, but only account for a very small share of SME financing

Source: OECD (2017c)

Despite the relatively modest amounts of money involved, venture capital activities are believed to have a disproportionate economic impact. In the United States, for example, public companies with venture capital backing employ four million people, account for one-fifth of market capitalisation, and 44% of the research and development spending of public companies (Gornall and Strebulaev, 2015).

The capital market is particularly well suited to firms embarking on riskier endeavours, i.e. start-ups, fast-growing ventures, but also established firms undergoing a major transition, such as a change in ownership, accelerated growth or transformation into a firm with a stronger market position. Private equity, for instance, is a widely recognised vehicle for financing potential high growth SMEs, which depend on equity finance to realise their growth ambitions. Empirical evidence shows a positive and strong relationship between capital market financing and firm growth in a wide array of countries, especially for small firms (Didier et al., 2015). However, access to equity finance remains difficult in many countries, especially for fast-growing firms, with adverse implications for economic growth and inclusiveness.

...and remain underdeveloped due to a number of demand- and supply-side barriers markets

The availability and access to alternative sources of finance is held back by a combination of demand and supply-side barriers. On the demand side, many entrepreneurs and business owners lack financial knowledge, strategic vision, resources and sometimes even the willingness or awareness to successfully attract finance other than straight debt. The lack of appetite by SMEs for alternative financial instruments, equity in particular, can also be attributed to their tax treatment vis-à-vis straight debt. On the supply side, potential investors are held back by the overall opacity of SME finance markets, a lack of exit options and regulatory impediments. As a consequence, financial instruments for SMEs often operate in thin, illiquid markets, with a low number of participants, which, in turn drives down demand from SMEs and discourages potential suppliers of finance (OECD, 2017d; Nassr and Wehinger, 2016).

The digital transformation offers new opportunities to improve SME access to finance

The advent of Fintech (combining technology and innovative business models in financial services) has gained considerable momentum in recent years, with global investments rising at exponential rates. It holds the potential to revolutionise SME financing, as it can offer unprecedented solutions to deal effectively with the main barriers that SMEs face in financial markets: information asymmetries and collateral shortage (OECD, 2017d).

On the one hand, digital technologies, such as online and mobile banking and payment solutions, have had an important impact on traditional SME financing. They allow financiers to considerably lower transaction costs when reaching out to unserved and underserved segments of the SME population. They introduce accounting technology to help manage SME financial statements, as well as alternative credit scoring mechanisms using non-traditional sources of information, such as payment history, usage and payment of utilities, online activities and mobile history. These make lenders able to address information asymmetries in a cost-effective manner and enable higher approval rates with a relatively low default rate.

While traditional banks are investing in updating their business practices, many new-born Fintech companies are entering the market addressing an increasing demand for fully digital, remotely accessible and cheap financial services. Giant online merchants (e.g. Amazon, Alibaba) have also started to offer financing options for their clients, leveraging the wealth of information on their trading history and business behaviour. These developments are particularly relevant for emerging economies and small businesses that currently find it hard to access the formal financial sector, such as micro-enterprises, informal ventures and firms operating in rural and/or remote areas (OECD, 2017d). While new financing opportunities for entrepreneurs open up, the entry of large tech companies into the SME finance market might be disruptive for traditional players, and the overall implications of these changes need to be better understood.

Digitalisation has also allowed some innovative and inherently digital financial services to be offered to SMEs. Peer-to-peer lending and equity crowdfunding provide alternative sources of financing and have experienced rapid growth in many parts of the world, as they enable investment projects that are too small or too risky for traditional banks to address (World Economic Forum, 2015). They still represent a very minor share of financing for businesses; however, they are rapidly expanding from the starting non-profit and small scale entertainment niche, to for-profit activities and businesses (OECD, 2017a).

A major push in this direction is due to the development of Blockchain (i.e. Distributed Ledger) technology, which addresses information asymmetries and collateral shortage in an innovative way and is applicable to any digital asset transaction performed online. “Smart contracts” based on this technology can immediately execute transactions when certain agreed upon conditions are met, bypassing the need of any middle-man or the risk (and cost) of enforcement. Originally developed for the Bitcoin digital currency, the technology has turned out to be a multipurpose tool that could have a large impact on SMEs access to finance. Traditional financial players recognise the opportunity offered by this new technology and are moving accordingly. For instance, in Europe, the Digital Trade Chain Consortium was created in 2017, gathering major commercial banks, to build a new cloud-based platform based on blockchain technology, directed at SME clients. A similar project is being considered that would serve Japan and other countries in Asia (IBM, 2017).

The G20/OECD High Level Principles on SME Financing provide a comprehensive framework for policy makers

Recognising that financing needs and constraints vary widely across the SME population and along the life-cycle of firms, the G20/OECD High-level Principles on SME Financing advocate a holistic approach to address existing demand- and supply-side obstacles to SME financing, calling for strengthening SME access to credit, while also supporting the diversification of their financing sources (Box 3.1). The OECD is working to identify effective approaches for the implementation of the Principles, in order to support governments in designing appropriate policy measures that are suited to their national contexts and specific challenges of their SME population.

Box 3.1. The G20/OECD High Level Principles on SME Financing

1. Identify SME financing needs and gaps and improve the evidence base.
2. Strengthen SME access to traditional bank financing.
3. Enable SMEs to access diverse non-traditional financing instruments and channels.
4. Promote financial inclusion for SMEs and ease access to formal financial services, including for informal firms.
5. Design regulation that supports a range of financing instruments for SMEs, while ensuring financial stability and investor protection.
6. Improve transparency in SME finance markets.
7. Enhance SME financial skills and strategic vision.
8. Adopt principles of risk sharing for publicly supported SME finance instruments.
9. Encourage timely payments in commercial transactions and public procurement.
10. Design public programmes for SME finance which ensure additionality, cost effectiveness and user-friendliness.
11. Monitor and evaluate public programmes to enhance SME finance.

Source: G20/OECD (2015)

Governments have been stepping up efforts to foster a diversified financial offer for SMEs

A range of government policies to foster SME access to finance have been introduced since the financial crisis, including new policy initiatives, scaling up existing measures and policy experimentation.

Credit guarantee schemes remain the most widely adopted policy instrument in OECD countries, and their design is continuously being revised to keep up with evolving needs. Export guarantees and measures to support trade credit, direct lending schemes, interest rate subsidies, as well as the provision of business advice and consultancy to SMEs looking for external finance constitute some other commonly used policy instruments.

At the same time, governments increasingly provide support for equity-type instruments, with initiatives that often target start-ups, innovative and fast-growing small businesses. This is the case, for instance, of regulatory reforms aimed at enabling crowdfunding activities. In some jurisdictions, public support for improving access to finance for (innovative) start-ups is being complemented by a comprehensive bundle of policy measures to address other challenges these firms face, such as a high regulatory burden, weak managerial skills, access to skilled labour, innovation and internationalisation.

For instance, in the framework of the Investment Plan for Europe (Juncker Plan), the European Fund for Strategic Investment (EFSI) was created in 2015, implemented and co-sponsored by the EIB Group, to address the paucity of alternative sources of finance for SMEs and mid-caps, by mobilising private capital, such as through guarantees and equity investments. Given its success, the SME window of the EFSI was scaled up in 2016. Furthermore, to improve the quality of investment projects, a European Investment

Advisory Hub (EIAH) was launched, which acts as a single access point to tailored advisory and technical assistance services for European project promoters.

There is also an emerging trend towards tailoring SME financing policy approaches to local and regional circumstances. For example, in France, the *Banque de France* has created a network of regional correspondents, around 100 advisors, which provide advice on emerging financial problems to very small local firms. In the United Kingdom, in 2017, the British Business Bank launched its first regionally-focused fund, the Northern Powerhouse Investment Fund (NPIF), in collaboration with ten Local Enterprise Partnerships (LEPs), to provide commercially-focused finance to help SMEs start up and grow (British Business Bank, 2016). In China, the national SME development fund, which was established in 2015, set up its first regional subsidiary fund in Shenzhen City in 2016. In 2017, a national programme of innovative demonstration cities for small micro-enterprises started, with the aim to fund directly innovative SMEs and entrepreneurship at the city level, or to improve the urban environment for SME innovation and entrepreneurship (OECD, forthcoming).

Efforts by governments to enable SMEs to fully reap the benefits of a more diversified financial offer should focus on several areas (OECD, 2015).

Improving SME skills and strategic vision for their financing needs

SME skills and strategic vision are key ingredients in any effort to broaden the range of financing instruments. Targeted financial education programmes are not only a matter of increasing knowledge about individual instruments. They can also help entrepreneurs to develop a long-term strategic approach to business financing, enhance understanding of the economic and financial landscape of relevance to their business, identify and approach providers of finance and investors, understand and manage financial risk for different instruments.

Complementing financial support for SMEs with non-financial elements, such as counselling and mentoring, can enhance SME financial skills and planning. In this regard, the providers of SME-targeted programmes, including governments, public financial institutions, multilateral development banks (MDBs) and relevant non-for profit institutions, can play a key role to foster SME financial capabilities. For example, in many of its programmes, the Business Development Bank of Canada (BDC) complements financial support with consulting services, and independent research indicates that this combined approach leads to a significant performance improvement by beneficiaries (OECD, 2017d).

While many countries have a national strategy in place to foster financial literacy, only few have a specific focus on SMEs, even though financial literacy needs of entrepreneurs go much beyond those of the general population (OECD/INFE, 2015). In Portugal, for example, financial education needs of SMEs are addressed in a comprehensive manner under the “National Plan for Financial Education.”

It is also necessary to improve the quality of start-ups’ business plans and SME investment projects, especially for the development of the riskier segment of the market. In many countries, a major impediment to the development of equity finance for young and small businesses is the lack of “investor-ready” companies. Furthermore, SMEs are generally ill-equipped to deal with investor due diligence requirements. In Italy, for instance, the ELITE programme, launched by the London Stock Exchange Group, helps growth-oriented SMEs to access the capital market by offering training, tutoring, and direct access to the financial community. A partnership with the Italian government started in 2017 to increase

participation in the programme by innovative start-ups and SMEs from Southern Italian regions.

Designing effective regulation that balances financial stability and the opening of new financing channels for SMEs, including through digitalisation

The regulatory framework is a key enabler for the development of instruments that imply a greater risk for investors than traditional debt finance. In particular, efficient insolvency procedures and strong right enforcement mechanisms can increase the confidence of a broad range of investors in SME markets.

Designing and implementing effective regulation, which balances financial stability, investors' protection and the opening of new financing channels for SMEs, represents a crucial challenge for policy makers and regulatory authorities. This is especially the case given the rapid evolution in the market, resulting from technological changes as well as the engineering of products that, in a low interest environment, respond to the appetite for high yields by financiers. In addition, new financing models, such as crowdfunding, are emerging that may engage relatively inexperienced investors.

While promising, the development of digital tools also poses challenges for policy makers, regulators and supervisory authorities. First, it is key to stay abreast of the rapidly evolving trends and developments in dialogue with traditional and new private sector partners. Second, the regulatory and supervisory framework needs to be accommodative of novel developments, while guaranteeing consumer protection, data protection and privacy restrictions and financial stability. In the European Union, for instance, the Directive PSD2 provides a legal framework promoting the use of innovative and disruptive solutions for banking and payment services (European Commission, 2015b).

Expanding access to financial services at a very rapid pace with lower controls might create a risk for systemic financial stability and of over-indebtedness for SMEs, which might be addressed by fostering financial literacy and awareness (Weidmann, 2017). Raising awareness about digital risks and enhancing digital skills is essential, also because continuous remote access implies that cyber risks extend to the personal devices (e.g. smartphones, personal computers) of borrowers, to which is to be added the possibility of larger attacks with data breach on the clouds. For instance, in response to this challenge, the French data protection agency, ANSSI and its German counterpart, BSI, jointly published a standard to be used to certify trustworthy providers of Cloud services with the Franco-German label: European Secure Cloud (ANSSI, 2017).

As financial and technological developments increasingly span the globe, close international cooperation can help to identify good practices and harmonise approaches.

Developing information infrastructures to reflect more accurately the level of risk associated with SME financing and encourage investors' participation

Information infrastructures for credit risk assessment, such as credit bureaus, registries or data warehouses with loan-level granularity, can reduce the perceived riskiness investors fear when approaching SME finance and help them identify investment opportunities (Box 3.2). More reliable information about risk may also help reduce higher financing costs typically associated with SMEs.

Box 3.2. Policies to improve the credit information infrastructure

One of the main difficulties faced by SMEs in accessing financial markets is related to information deficiencies that prevent investors from reliably assessing the risks and potential benefits from investing in them. The development of a credit risk assessment infrastructure plays a crucial role in overcoming existing information asymmetries and improving transparency in SME finance markets:

- Japan established its **Credit Risk Database (CRD)** in 2001, led by the Japanese Ministry of Economy, Trade and Industry and the Small and Medium Enterprise Agency (SMEA). The CRD provides credit risk scoring, data sampling, statistical information and related services. It therefore not only facilitates SMEs' direct access to the banking sector, but also smooths access to the debt market by enabling the securitisation of claims.
- In France, the **Euro-Secured Notes Initiative (ESNI)** aims to overcome information asymmetries that limit the development of a well-functioning securitisation market for SME assets by making use of the *Banque de France*'s credit assessment of non-financial companies, as well as the internal ratings from banks. The ESNI was set up in March 2014 as a Special Purpose Vehicle by private banking groups and with support from the *Banque de France*. The securities, regulatory and banking supervisory authority ensures that the scheme complies with existing regulation.

Source: OECD (2017d).

In some countries, policies seek to address the information gap between SMEs and potential investors by facilitating their direct interaction, with different degrees of public engagement, from awareness campaigns to brokerage and match-making. In the business angel market, for instance, public action has largely aimed at improving information flows and networking opportunities between financiers and entrepreneurs. In some cases, however, the facilitation efforts have not produced the desired results, due to the lack of maturity of local markets, i.e. little scale or lack of investor-ready companies. This highlights the need for a policy mix that takes into account existing limitations on both the supply and the demand sides (OECD, 2016b).

Many obstacles also persist to unlock SME financing through intangible assets², which make up an increasing part of SMEs' value, especially of innovative ones. Recent initiatives have mainly focused on helping the market determine which company-owned intangible assets have realisable value, with most of the activity concentrated in Asia, such as the provision of subsidised IP evaluation reports in Japan. In China, the State Intellectual Property Office acts as a central registry of pledges and evaluation regimes, complemented by a set-up of measures to stimulate IP financing techniques, such as state-backed compensation schemes to cover bad debts, a guarantee coverage of up to 100% under certain conditions, lender incentives (dependent on the relative number of IP-backed loans), interest rate subsidies for IP-backed loans, and dedicated funds. The Korean Development Bank has initiated loans for purchasing, commercialising and collateralising IP, and its credit guarantee institution offers underwriting for an IP valuation for lending or securitisation (OECD, 2017e).

Leveraging private resources and develop appropriate risk-sharing mechanisms with the private sector

Policy can play a role in leveraging private resources and competencies and develop appropriate risk-sharing and mitigating mechanisms, such as through co-investment or guarantee schemes and private-public equity funds. Governments can contribute to raise awareness and improve knowledge by different financial providers about investment opportunities in SMEs, by raising the profile of the public debate about SME finance market development and investors' advantages from diversification in the SME asset class; by improving visibility of successful transactions and platforms for alternative instruments; and by facilitating information sharing between investors and SMEs.

Direct investments by governments through funds, matching or co-investment funds and funds-of-funds have been identified as an effective means of addressing supply-side gaps in the availability of start-up and early stage capital since they can increase the scale of SME markets, enhance networks and catalyse private investments that would not have materialised in the absence of public support. Israel's Yozma programme, the Danish Growth Capital Fund or the Turkish Growth and Innovation Fund – all based on co-investments between the private and public sector - are prominent examples in this respect. Governmental VC schemes also seem more successful when operating alongside private investors, rather than through direct public investments. Indeed, in recent years in many OECD countries the focus of support instruments has shifted from government equity funds investing directly to more indirect models such as co-investments funds and fund-of-funds (European Investment Fund, 2015).

Improving the evidence base

In most OECD countries, there is an established framework to collect quantitative data on SME access to finance, including by conducting demand and supply-side surveys. By providing a framework for data collection and information on policy initiatives, the annual *OECD Scoreboard on Financing SMEs and Entrepreneurs* serves as the international reference for monitoring developments and trends in SME and entrepreneurship finance and financing conditions, thus improving cross-country analysis and comparability and supporting the formulation and evaluation of policies in this domain.

However, national data collection efforts usually focus on traditional bank finance, while the evidence about SME access to alternative financing tools remains patchy. Moreover, while quantitative data on SME finance are often broken down by the size of the enterprise, more granular data by other relevant parameters such as the business age, location, sector, export status and innovativeness are available only in a minority of countries. Similarly, only few countries gather detailed data broken down by key characteristics of principal business owner, such as age, educational attainment, business experience or gender (OECD, 2018b).

The lack of hard data, especially on non-debt financing instruments, represents an important limitation for the design, implementation and evaluation of policies in this area. This limitation is particularly critical when seeking to take account of SME heterogeneity and the varying nature of finance gaps in the process of policy design. Better micro data and micro level analysis, along with a stronger culture of evaluation are therefore essential to improve understanding about the different needs of SMEs and effectiveness of policy interventions, as well as the potential and challenges of new business models emerging in the financial sector.

Notes

¹ Traditional debt includes instruments such as bank loans, overdrafts, credit lines and the use of credit cards.

² Intangible assets are defined as identifiable non-monetary assets without physical substance, such as patents, copyrights, brand equity, software of computerised databases.

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4. Fostering greater SME participation in a globally integrated economy

Summary

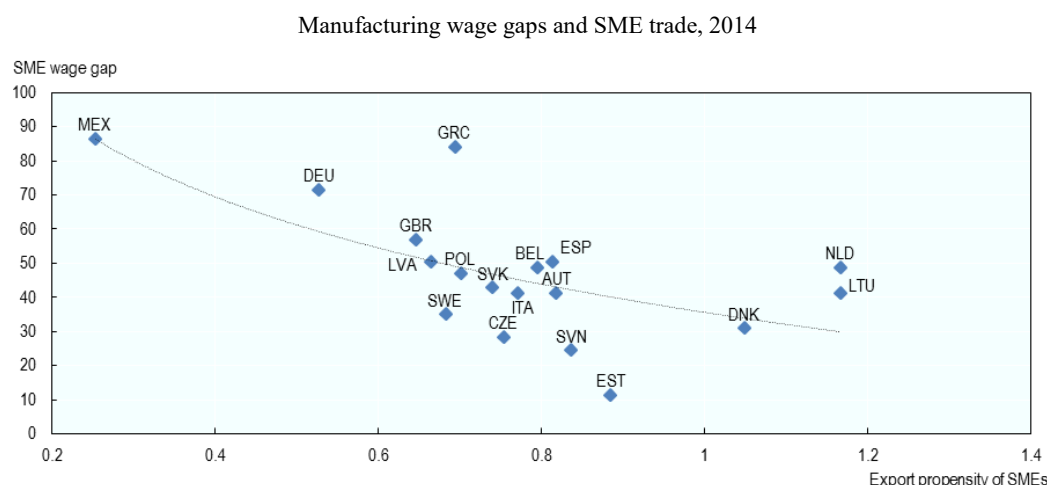
- Stronger participation by SMEs in global markets creates opportunities to scale up, accelerate innovation, facilitate spill-overs of technology and managerial know-how, broaden and deepen the skillset, and enhance productivity.
- Global value chains (GVCs) offer new opportunities for SMEs to integrate the global economy, as exporters, suppliers to large firms that export, and importers of competitively priced foreign inputs and technologies. However, benefits from GVC participation depend on the nature of inter-firm linkages and position in global production networks.
- The digital transformation is reducing trade costs, increasing SME involvement in trade and spawning a new breed of born-global enterprises. Nevertheless, trade costs and restrictions remain which impact SMEs disproportionately. Moreover, the increased number and complexity of digital “border control” may condition the benefits that SMEs gain from digital trade.
- The increasingly complex trading environment requires greater international cooperation to identify global solutions to global challenges, from traditional standards to new regulatory issues in the digital age. It also calls for domestic whole-of-government approaches to address SME constraints in internationalising, including access to information, skills, technology and finance, as well as trade facilitation and connectivity.

Better access to global markets is key to strengthening SME contributions to economic development and social well-being

Stronger participation by SMEs in global markets creates opportunities to scale up and enhance productivity, by accelerating innovation, facilitating spill-overs of technology and managerial know-how, and by broadening and deepening the skillset. International exposure, whether through imports, exports, or foreign direct investment (FDI), goes frequently hand in hand with higher productivity, and can be an important driver of employment growth (Wagner, 2012).

In addition, there are growing concerns that the benefits from globalisation have not spread evenly within economies, possibly exacerbating long-standing wage gaps between large and smaller firms. Average compensation per worker across OECD economies is significantly lower the smaller the firm, with remuneration levels, even in medium-sized firms, around 20% lower than in large firms. This reflects in large part correspondingly lower productivity, but the extent of direct exports by SMEs also appears to play a role. In countries, where SMEs have a relatively high share of exports, for example, differences in average salaries between SMEs and larger firms are smaller (Figure 4.1).

Figure 4.1. Where export propensity by SMEs is higher, wage gaps vis-à-vis large firms are smaller



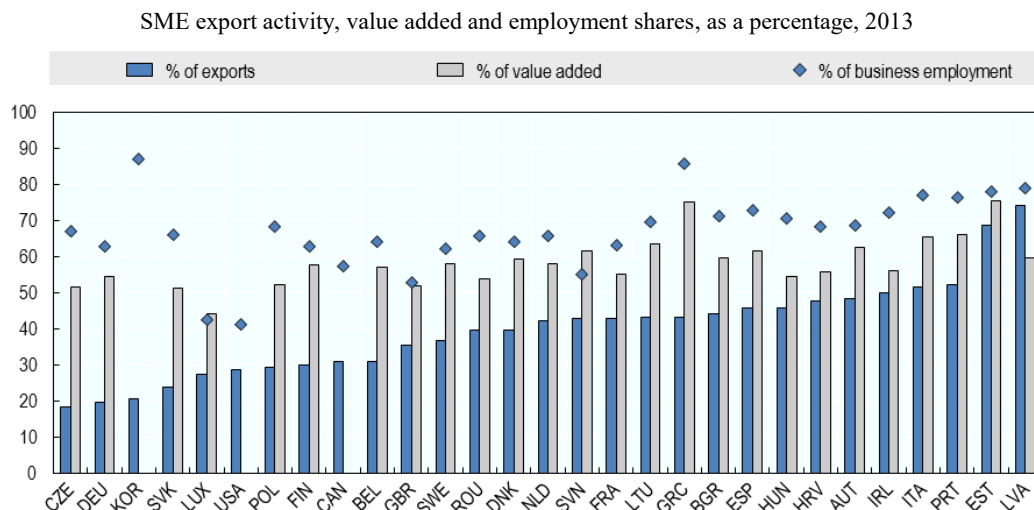
Note: SME wage gaps are measured as the difference between average salaries per employee in large firms and SMEs as a ratio of average salaries in SMEs. Export propensity of SMEs is measured as the share of exports by SMEs divided by the share of output by SMEs.

Source: Based on OECD Structural and Demographic Business Statistics and Trade by Enterprise Characteristics databases.

SMEs tend to be under-represented in international trade

Relative to their share of overall activity and employment, SMEs account for only a small proportion of exports (OECD-WB, 2015). In most OECD economies, for example, SMEs account for upwards of 95% of all firms, around two-thirds of total employment and over half of business sector value-added, but their contribution to overall exports is significantly lower – between 20% to 40% for most OECD economies (Figure 4.2).

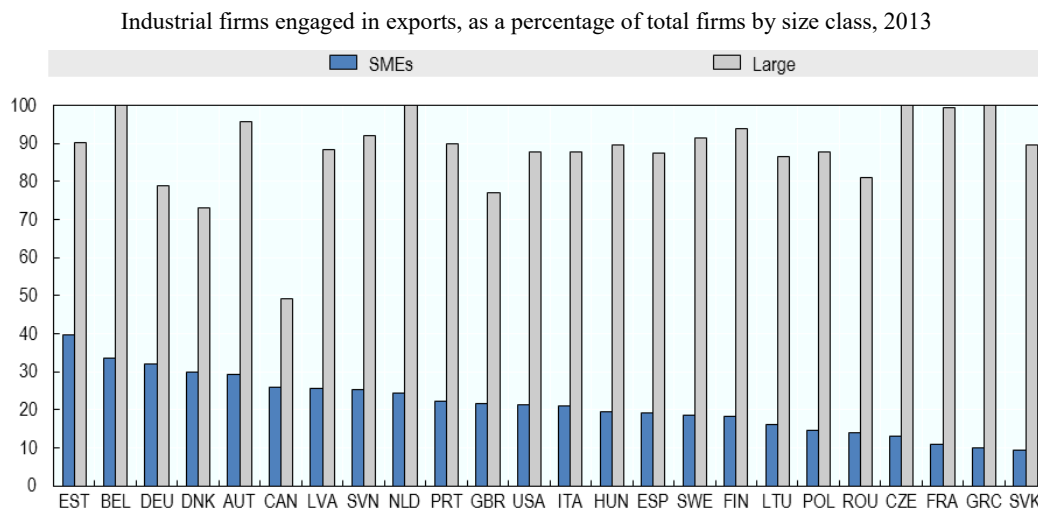
Figure 4.2. Compared to their contributions to national economies, SMEs are under-represented in global trade



Source: OECD Structural and Demographic Business Statistics and Trade by Enterprise Characteristics databases.

The relatively low contribution of SMEs to overall exports partly reflects their lower contribution to mining and manufacturing (industry), where economies of scale play a role. However, even within the industrial sector, the share of SMEs that export is significantly lower than the corresponding share in large firms. In most economies, more than 90% of large industrial firms export, compared to 10%-25% of SMEs (Figure 4.3).

Figure 4.3. The gap in exporting activity in the industrial sector is particularly large



Source: Trade by Enterprise Characteristics database.

Engaging in international markets can be expensive and usually only the most productive firms can afford to do so (Melitz, 2003; Bernard et al., 2007). Lacking economies of scale, trading costs represent a higher share of SMEs' exports – meaning that they are disproportionately affected by tariff and non-tariff barriers to trade (WTO, 2016a). In turn,

SMEs also face considerable challenges in accessing finance for new investment, information, skills and technology, all of which reduce their international competitiveness and their ability to face trade costs. The *Facebook-OECD-World Bank Future of Business Survey* corroborates these findings. In 2017, asked to cite barriers to trade, SMEs with a digital presence named the following factors: finding business partners (63%); market access limitations (41%); different regulations in other countries (38%); customs regulations (35%); language and/or cultural gap (33%); securing export finance (31%); poor online payment alternatives to sell online (29%); large geographical distance from home country (26%); and poor internet connection to sell online (18%).

In many countries, women entrepreneurs face heightened challenges to participate in international markets. Businesses run by women are less likely to be involved in international trade, whether as exporters or importers, than male-run enterprises. In addition, among exporters, women-led businesses tend to be more focused on individual consumers and less engaged in business-to-business trade than male-run enterprises, which reflects, in part, gender differences in the sectors of activity (OECD, 2017a).

Changes in the global trading environment offer new opportunities for SMEs

Recent changes in the global trading landscape, such as the rise of global value chains (GVCs) and the digital transformation, offer new opportunities for SMEs to integrate into the global economy. Greater flexibility and capacity to customise and differentiate products can give SMEs a competitive advantage in global markets relative to larger firms, as they are able to respond rapidly to changing market conditions and increasingly shorter product life cycles.

Some niche international markets are dominated by SMEs, and innovative small enterprises are often key partners of larger multinationals in developing new products or serving new markets. For example, in Germany small- and mid-size companies hold between 70% and 90% of global market shares in some specialised manufacturing segments, and account for the bulk of the German international trade surplus. In 2015, across twelve OECD countries, the share of SME merchandise export in textile, apparel and wood manufacturing represented respectively 66%, 64% and 61% of the total (OECD, 2016a).

At the same time, SMEs comprise a very heterogeneous group of firms and opportunities to internationalise will depend on the activities undertaken, as well as on whether SMEs operate in tradable or non-tradable sectors.

....through GVCs...

GVCs allow SMEs to specialise in specific segments of production, rather than having to master all processes required to produce finished goods and thus integrate into segments of global production chains. In turn this can be a pathway towards economic development through productivity growth, exporting more sophisticated products, and a less concentrated export basket (Kowalski et al., 2015).

This integration can occur on the ‘output’ side, through direct cross-border exports and also indirectly, through upstream supplies to larger firms, which provides a vehicle to overcome trade related costs and challenges. But SMEs can also benefit on the ‘input’ side, through access to cheaper inputs and capital goods as well as through better sourcing or use of foreign technologies, products or knowhow (Lopez-Gonzalez, 2017).

Outward FDIs can also allow SMEs to access international markets and integrate in GVCs, often indirectly, as upstream suppliers to exporters (OECD-WB, 2015). In fact, survey evidence indicates that proximity to global enterprises, as suppliers, is one of the main drivers of outward FDIs by small businesses, although this form of internationalisation is relatively uncommon among SMEs: in a 2009 survey of European SMEs, only 2% indicated direct investment abroad (European Commission, 2010). In this regard, empirical evidence suggests that public measures to support outward FDIs by SMEs are effective in enhancing firm performance in terms of domestic turnover and productivity growth, especially for smaller and younger firms (Bannò et al., 2014).

... as exporters...

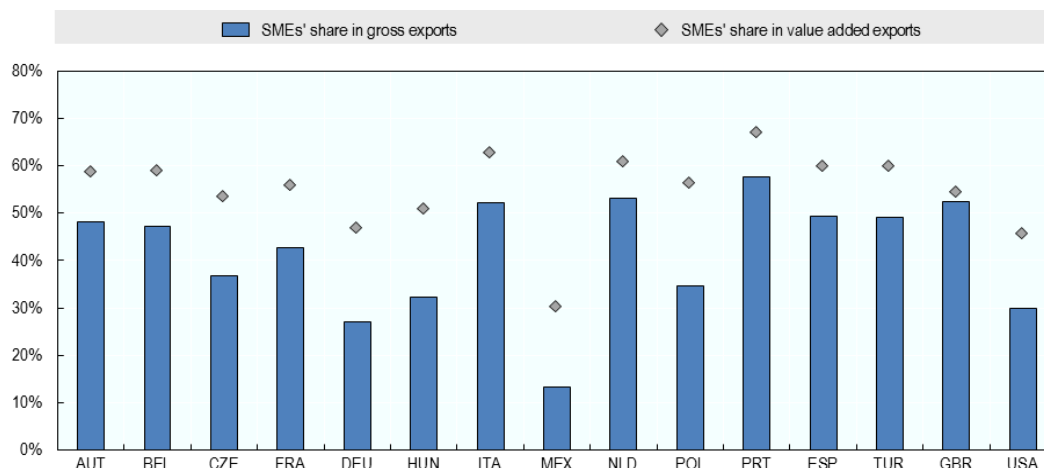
Direct participation in GVCs takes place when SMEs export intermediate goods and services for further processing. Evidence for Southeast Asian countries shows that selling inputs is particularly important: manufacturing SMEs in these countries have a higher tendency than larger firms to export goods and services that are sold directly into GVCs. In Thailand, for example, 16% of the value added in the exports of manufacturing SMEs is sold directly to firms abroad for further processing, versus only 6% for larger manufacturing firms. Opportunities for SMEs operating in service sectors might be even bigger. In Viet Nam, the share of exports by SME used by other countries to produce exports jumps from 5% (manufacturing only) to 26% when service firms are included (Lopez-Gonzalez, 2017).

... as suppliers to larger firms that export

Another way for SMEs to benefit from GVCs is through indirect exports, or by supplying intermediate goods and services to typically larger firms – domestic or foreign-owned – which then export. Recent evidence suggests that, in OECD countries, looking only at direct exports by SMEs under-represents the actual engagement of small firms in a country's gross exports (Figure 4.4). In Mexico, for example, SMEs account for less than 15% of gross exports, but for 30% of the total value added in the country's exports. In other terms, when the role of SMEs as suppliers of inputs to larger direct exporters is taken into account, the importance of SMEs as exporters doubles.

Figure 4.4. SMEs account for a larger share of value added in international trade when indirect exports are taken into account

Direct and indirect exporting activity of SMEs in OECD countries, as a percentage of gross exports, 2009

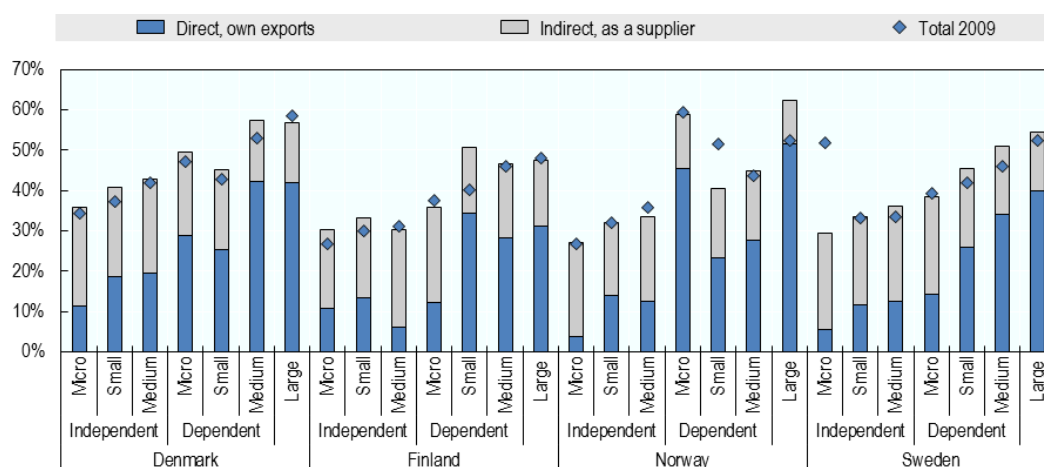


Source: OECD Trade by Enterprise Characteristics (TEC), Structural and Demographic Business Statistics (SDBS) and Inter-country Input-Output Trade in Value Added (ICIO/TiVA) Databases.

The significance of indirect channels is especially important for independent SMEs (i.e. those not owned by a larger domestic firm or foreign firm). For example, while only 3% of total value added generated by independent micro SMEs in Sweden is exported directly, an additional 18% of their value added is indirectly embodied in exports (Figure 4.5).

Figure 4.5. Indirect export contributions to value added are particularly relevant among independent SMEs

Direct and indirect exporting activity of SMEs in Nordic countries, as a percentage of total value-added, 2013



Source: Nordic countries in Global Value Chains (2016), OECD-Statistics Denmark.

Indirect exports by SMEs are particularly large in sectors where GVCs are important and where scale matters. In the transport equipment sector, for example, SMEs account for over 40% of total US value-added exported, with nearly all of that contribution reflecting upstream component and services suppliers to the transport equipment industry. This

indirect mode of internationalisation provides SMEs access to foreign markets and new sources of growth, but without incurring trade-related costs.

SMEs can strengthen and upgrade supply linkages by establishing specific contractual arrangements with Multinational Enterprises (MNEs), such as supply/manufacturing agreements, licensing, R&D agreements, technology transfer and quality support, as well as by receiving inward FDI. The existence of industry clusters at the local level represents an important location factor for many MNEs.

... and as importers of competitively priced foreign inputs and technologies

Imports matter for export competitiveness and SMEs may also benefit from GVCs on the input, or buying, side (Lopez-Gonzalez, 2016 and 2017). Firms which use more imported goods and services are more productive, and are better able to face the costs of exporting (Bas and Strauss-Kahn, 2014 and 2015).

SMEs, including non-exporters, can increase their productivity by drawing on cheaper and more sophisticated imports; by exploiting new technologies embodied in new and cheaper capital products; as well as through improved access to new technologies from engagement with internationally-oriented firms, including through linkages arising from foreign investment. All of these channels can also help to target specialisation in parts of the value-chain, where SMEs have comparative advantages and can in turn foster upgrading.

Existing potential remains untapped, however. In Nordic economies, for example, SMEs consistently source a lower share of foreign goods and services to produce exports than larger firms. In addition, the evidence highlights that dependent SMEs also have higher integration from an input (import) perspective than independent SMEs, and so are able to leverage on those links to overcome import trade barriers. This underscores the importance of policies that address constraints not only to exporting, but also to importing for small firms.

... but these gains may vary by position as well participation in GVCs

The benefits from GVC participation depend not only on the degree of integration or participation, but also on the position within global production networks and on the characteristics of other participants in the value chain. Firms and industries positioned at the centre of complex production networks have access to a greater variety of foreign inputs, and potentially a broader range of technologies, compared to those at the periphery. Smaller firms display faster productivity growth in those sectors that have become more central to global production, than those on the periphery, and also in sectors with stronger linkages to more productive foreign buyers/suppliers (Criscuolo and Timmis, forthcoming).

In addition, certain risks may arise for SMEs that participate in GVCs, due to their typically weaker bargaining power vis-à-vis larger firms. In this respect, due diligence requirements and their implementation matter for creating a level playing field. The OECD Guidelines for Multinational Enterprises, which cover also relationships with sub-contractors and suppliers, represent an important reference¹.

A range of internal and external factors influence SMEs' ability to participate in global markets

While the global fragmentation and specialization of economic activities provide a number of economic opportunities for SMEs, challenges for tapping into these remain due to a number of internal and external factors.

Internal factors

Innovation

SMEs that innovate are more likely to engage in global markets than non-innovative firms. Process and organisational innovation, for example, can increase firm productivity by reducing production costs and allowing SMEs to achieve the minimum level of efficiency required to cover the fixed costs of exporting. Through product innovation, marketing innovation and innovative branding strategies, SMEs differentiate their products from those of their competitors, which enables them to gain market shares in global markets.

Technology adoption

The use of emerging technologies can enhance firm productivity, making it easier for them to access foreign markets and compete. However, new technologies tend to require considerable upfront costs, as well as a reorganisation of the firm to adopt and effectively implement them, making the investment often too expensive for SMEs and larger firms more likely to adopt advanced technologies, including digital ones. Small firms are, for instance, less likely to adopt a range of hardware and software technologies, including servers, Enterprise Resource Planning (ERPs), database management systems, and innovation software (DeStefano et al., 2017).

In addition, unlike large firms, SMEs have considerably less knowledge-based capital and accumulated technology, making it harder for them to adopt emerging technologies (Gibbs and Kraemer 2004). In fact, certain technologies may actually favour large multinational firms, as advances in information and communication technology enable large multinationals to coordinate and profit from complex and fragmented production networks (OECD-WB, 2015).

Management and human capital

SMEs, particularly in emerging markets, generally have weaker managerial skills and less efficient organisational practices than large firms, which can be a barrier to effective participation in global markets. Poor management skills are usually correlated with low levels of productivity, an inefficient use of the workforce, higher frequencies of wastage and damaging of tools, machinery, materials and inputs, and overall ineffective use of the manufacturing floor (Bloom et al., 2012; Iacovone and Qasim, 2013). In this regard, management can be considered as a type of technology which, if used effectively, can enhance the competitiveness of a firm (Bloom et al, 2012; Bloom et al, 2013), and significantly raise their productivity (Andrews and Criscuolo, 2013). Workers with higher levels of human capital are more adaptable to technological change, making it easier for firms to adopt and reorganise around emerging technologies (Bartel and Lichtenberg, 1987; Bresnahan et al, 2002). However, developing or acquiring the right mix of skills, ideas and talents is a challenge for SMEs, especially in markets where the required skills are scarce or expensive. Worker skills in SMEs are also an important factor in their relation with

MNEs and link with Foreign Direct Investments (FDIs). However, evidence shows that workers in smaller firms tend to have lower cognitive skills (including literacy, numeracy and problem solving skills) than those in larger firms, putting SMEs at a higher risk of not meeting the skills requirements of multinationals. Relationships between MNEs and affiliates (or local suppliers) – and their respective bargaining powers – may also influence the diffusion of knowledge and technology, and thereby firms’ ability to gain a larger share of the value generated within GVCs. Having the skills capacity to absorb new technologies can help SMEs to develop the types of relationships that foster the diffusion of knowledge (OECD, 2017b).

External factors

Access to finance

Many of the internal factors of SME participation in GVCs are dependent upon finance. For example, both product and process innovation require considerable up-front investments that may not be at reach of many SMEs. Moreover, emerging technologies tend to be expensive and therefore require considerable investment. Financial barriers are found to hamper R&D and investment (Hall, 2002; Lerner and Hall, 2010) and to substantially hinder technological investment, which is the main reason for the gap in productivity and innovation between domestic and foreign-owned firms (Gorodnichenko and Schnitzer, 2013).

Specific challenges limit access to finance by SMEs. These are largely related to the greater difficulties that lenders encounter in assessing and monitoring SMEs relative to large firms, leading to higher transactional and informational costs. This is especially the case for traditional bank lending, which represents the main source of external finance for SMEs. However, increasingly complex and interconnected financial markets offer opportunities to serve the needs of SMEs that seek to integrate global markets (OECD, 2015a). In particular, trade finance instruments (e.g. factoring, letters of credit, guarantees, export credit and credit insurance) have become increasingly important to mitigate risk related to cross-border transactions. Supply chain finance has gained particular importance, also as a result of the increased complexity of supply chains and progress in digital technologies. However, globally, over half of trade finance requests by SMEs are rejected, against 7% for MNEs. Gaps are highest in countries that are experiencing rapid growth in trade opportunities, as global production patterns evolve (WTO, 2016b).

Access to information

SME engagement in international activities may be hindered by limited information and understanding about target foreign markets. This limits the ability to customise products to the diverse needs of consumers and to meet product requirements and standards under local regulatory environments.

In comparison to larger firms, SMEs also lack established contacts with suppliers and business partners abroad. While advances in telecommunication technology may help to alleviate some of the knowledge gap, foreign contacts are essential for overcoming information barriers particularly for SMEs.

Bottlenecks in infrastructure and distance

In addition, a number of more general barriers affect the integration of small businesses into GVCs. The geographic location of a firm, for instance, is an important determinant for

joining GVCs (Kowalski et. al. 2015). While the geographical distance between trading partners matters, the ability of firms to access foreign markets and participate in GVCs is greatly affected by the quality of physical infrastructure, such as roads, ports, and airports, as well as the efficiency of the procedures followed in the operation of those facilities (Bernhofen et al., 2016). In particular, in Low-Income Developing Countries (LIDCs), the ability of firms and industries to engage in trade is determined much more by the quality of their port facilities (sea and air), than by the types of preferential access that they might enjoy in major industrialised markets (OECD-WB, 2015).

Telecommunications infrastructure is another important component which supports the value chains of physical goods and enables the creation and trade of digital services, which account for a growing share of total international trade. Access to such infrastructure can therefore be important for SMEs that seek to participate in global markets.

Logistics infrastructure reduces the time, cost, and uncertainty involved in importing and exporting for all types of firms. However, improving the overall efficiency of a country's logistics infrastructure is more important for small businesses than for large firms, since costs of trade are fixed regardless of the size or revenue of the firm.

Intellectual property

Intellectual property rights (IPRs) are useful tools for SMEs to protect their innovations and intellectual property, particularly if the product is easily replicated by others. Moreover, IPRs can increase the perceived value of the firm, which can be leveraged to access external sources of finance, as well as attract knowledge and commercial partners.

SMEs encounter a unique set of challenges using IPRs when operating internationally. These relate mainly to cost, in particular legal overheads; multiple filings, regulatory and technical differences across countries, which often meet with expertise deficiencies; and the robustness of local IP enforcement. Streamlining procedures and reducing application costs and time, particularly in industries where innovation occurs at a rapid rate, and improving litigation and enforcement mechanisms are important to SMEs looking to operate in GVCs and international markets. Likewise, improving cross-border IP information, coordination and enforcement, including access to protection mechanisms provided by international treaties, can ease SME participation in GVCs and export markets (OECD, 2011). In this regard, the European Union has created the European IPR Helpdesk, which provides free-of-charge, first-line support on IP matters to beneficiaries of EU-funded research projects and SMEs engaged in transnational partnership agreements.

SMEs are adapting their internationalisation strategies for the 21st century

The digital transformation is changing what and how we trade (Lopez-Gonzalez and Jouanjean, 2017) and SMEs are both facing new challenges and adopting new internationalisation strategies.

Digital platforms reduce trade costs and increase SME involvement in trade

Access to digital technologies have considerably lowered the barriers of entry into global markets, enabling SMEs to internationalise at a fraction of the cost, and making it easier to participate in international production networks, find customers abroad and make international payments. Many crucial ICTs needed to sell goods abroad can be accessed cheaply, as long as a firm has access to the internet. For example, online platforms reduce the cost and speed of finding buyers of their products and services, and sellers of

intermediate inputs at home and abroad, thus connecting supply and demand globally. Many of these digital platforms offer services that facilitate payments and provide warehousing and logistics services, all of which further reduce trade-related costs. Taken together, this has contributed to a greater participation of SMEs in trade, as well as a rising number of small packages crossing international borders (Lopez-Gonzalez and Jouanjean, 2017).

However, while some trade costs fall, others remain. Goods still incur considerable to-the-border, at-the-border and behind-the-border costs, underscoring the need for continued efforts to streamline trade facilitation. Reform of slow or cumbersome border procedures can cut costs of trading by 12%-18%, depending on a country's level of development (OECD, 2015b). Trade costs faced by SMEs also depend on the applied *de minimis* thresholds, that is, the value threshold, under which no tariffs or taxes are collected. Above this threshold, not only will a tariff have to be paid, but packages might also be delayed at the border for inspection, increasing delivery time.

Some countries do not have a *de minimis* provision, so their customs inspect and collect duties, if applicable, on all arriving packages. But among those that do, there is a wide variation in thresholds. This matters for SMEs for two reasons. First, because low *de minimis* thresholds can lead to higher trade costs through longer clearance times and tariffs – which disproportionately affect low or small value trade flows. And, second, because different *de minimis* thresholds make it difficult to estimate costs when selling products to different markets.

... but services restrictions hit SMEs harder than larger firms

The digital transformation is also giving rise to new 'information industries', such as big-data analytics, cyber security solutions or at-a-distance quantum computing, and presents new opportunities for SMEs. However, services restrictions may mean that these opportunities remain untapped, especially by small firms.

For cross-border exports of services by SMEs, an average level of services trade-restrictiveness represents the equivalent of an additional 12% tariff relative to large firms. Establishing an affiliate abroad involves an even wider range of sunk and fixed costs. For a medium-sized firm of EUR 5 million in turnover, selling specialised services through foreign affiliates, the average level of services trade-restrictiveness can be equivalent to an additional 19% tariff compared to large firms.

Opening up services markets would primarily benefit SMEs. Not just through greater market access, but also by reducing the costs of service inputs which are essential for the international operations of SMEs.

... and 21st century trade requires digital connectivity

Firms are increasingly relying on digital solutions, not just in the production stages and the delivery of goods and services but also as a means of connecting different, and geographically dispersed, customers or suppliers, including as part of GVCs. Digitalisation also allows firms to draw on data from users to better respond to consumer preferences, better target services, as well as to connect and customise production processes.

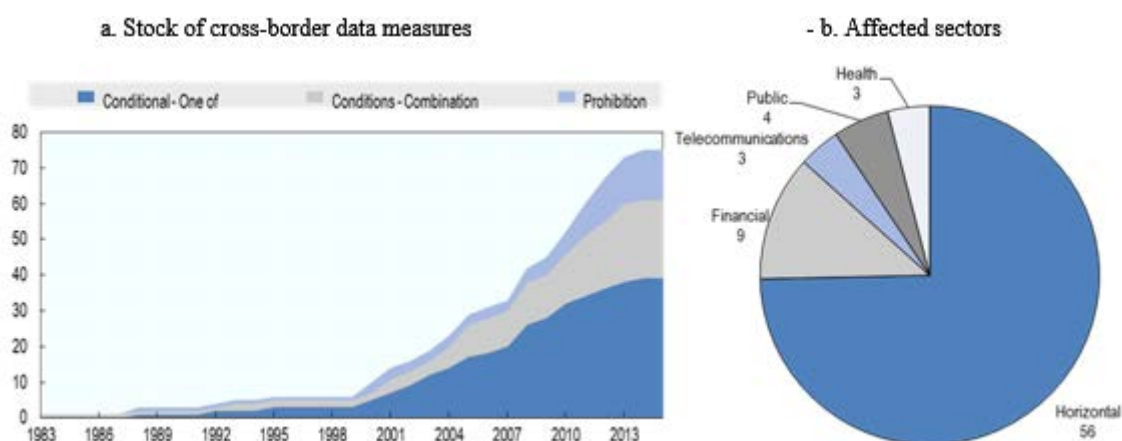
SMEs seeking to engage in digital trade require cheap and reliable access to digital networks. This means good physical infrastructure and appropriate regulatory frameworks. Here, restrictions on trade telecommunications services can inflate costs of access to digital

networks, disproportionately affecting SMEs' ability to benefit from the new opportunities offered by digital trade.

The digital trade environment has spawned a new breed of 'micro-multinationals' that are 'born global' (Lund and Manyika, 2016). Access to online inputs contribute to SME competitiveness and help SMEs operate across distant markets to overcome trading costs. For example, cloud computing helps SMEs access IT services with little upfront investment and scale up their IT functions in response to changes in demand. Better and faster access to critical knowledge and information can also help SMEs overcome informational disadvantages, notably with respect to larger firms, and compete on a more even footing. The Internet and international data transfers help SMEs better connect, improve their ability to secure and fulfil global contracts and access global supply chains. As a result, SMEs are increasingly becoming lead firms within GVCs and connecting with other SMEs (including micro companies) as providers of inputs.

However, the ubiquitous exchange of data has led to the emergence of 'data localisation' measures seeking to address concerns ranging from security and protection of individual privacy, to regulatory and audit reach. These introduce digital 'border controls' through restrictions on cross-border data transfers and/or local storage requirements. They are growing in number and complexity (Figure 4.6) and may condition the benefits that SMEs draw from engaging in digital trade. Finding balance between meeting key public policy objectives in a way that preserves the benefits of an open internet will be key.

Figure 4.6. The number and complexity of cross-border data transfer restrictions are rising



Note: Cross-border data flow restrictions are differentiated between "One of" (at least one of a set of conditions must be met) "Combination" (a combination of restrictions must be met).

Source: OECD (2016b).

Policies can enable SMEs to integrate into global markets

Policy plays a key role in overcoming the barriers to SME integration into global markets. The complex web of global production highlights that a broad range of policies can matter, from services trade to efficient domestic markets.

Global value chains amplify the importance of both goods and services trade policies. Modern production networks rely on two-way flows of imports and exports of goods and services. These intermediate inputs often cross borders multiple times, each time

accumulating additional trade costs, and these trade costs disproportionately affect SMEs, given their lower revenue base. Although tariffs for many goods are low in advanced economies, substantial barriers to trade in services remain. OECD work on Service Trade Restrictiveness Indicators reveals restrictions on foreign ownership, restrictions on the movement of people (e.g. quotas, stay duration limits) and barriers to competition even amongst advanced economies (OECD, 2017c).

Competitive domestic markets foster GVC participation, but there is scope for further services liberalisation. Lifting product market regulations encourages innovation and growth of the most efficient SMEs through increased competition, enhancing their GVC participation. In addition, by providing easier and cheaper access to inputs, reductions in red tape can also lead to gains in downstream firms using these inputs (Abe, 2013). Reducing barriers to entrepreneurship in services sectors, such as telecommunications, transport and logistics, and professional services, are particularly important for broader GVC participation.

The diversity of regulatory standards can be a major barrier for SME integration into GVCs. Technical barriers to trade cover 30% of international trade and more than 60% of agricultural products are affected by sanitary and phytosanitary measures (Nicita and Gourdon, 2013). However, standards are far from harmonised across countries and complying with each final destination market's regulations and standards can require firms to make costly investments in adapting production processes, specific packaging and labelling or undertake multiple certification processes for the same product (OECD, 2013). Mutual recognition and convergence of regulatory standards would reduce the burden of compliance for small-scale exporters in particular (OECD-WB, 2015).

GVC participation often requires investment in product and process innovation to upgrade technology and working capital to finance exports. However, access to finance is a particular challenge for SMEs and calls for policies that address credit market imperfections and support the broadening of financing instruments available to SMEs, in line with the G20/OECD High-level Principles on SME Financing. This includes export credit guarantees and measures to develop supply chain finance (OECD-WB, 2015; BIAC et al., 2016). For instance, in Mexico, the Production Chains Programme, launched by NAFIN, the state-owned development bank, allows small suppliers to use their receivables from large buyers to access working capital financing; provides financial training an assistance to SMEs; and eases the interaction of large buyers, SMEs and financial institutions through an electronic platform (OECD, 2015a).

The complexity of customs procedures and quality of transport infrastructure affect the cost of accessing export markets and importing intermediates. This raises compliance costs and causes delays, the latter requiring firms to hold larger inventories and working capital, which is a particular hurdle for SMEs. Promoting policies that streamline border procedures, simplify trade documents and automate border processes is likely to help (OECD, 2015b). There is no one-size-fits-all institutional arrangement for countries to implement logistics-related reforms. However, a collective framework that includes the private sector is important for consistent implementation. Canada, China, Finland, Germany, Malaysia, and Morocco have all introduced councils or similar coordination mechanisms for this purpose (OECD-WB, 2015).

Public support can help overcome information barriers related to business opportunities, foreign product standards, trade procedures and how to contact potential buyers/suppliers, for example, through providing information on rules and regulations, disseminating market information, international trade fairs or identifying foreign business partners (European

Commission, 2010). In addition, spillovers can occur from nearby firms within the same industry and exporting to the same market and hiring workers with experience of that export market (Choquette and Meinen, 2015). However, many SMEs are not aware of the support available, even amongst those SMEs that are internationally active (European Commission, 2010). This is despite evidence suggesting export promotion agencies (which often provide a range of these information services) have a larger impact on exports of SMEs than larger firms (Cruz, 2014). For instance, in Korea, the Export Capacity Enhancing Project, implemented by the Small and Medium Business Administration (SMBA), offers SMEs a broad range of services, such as education, global market information supply, marketing, market research, strategy consulting and global brand development. (Kyung-ho, 2017).

Upgrading technology and scaling-up production requires skills and organisational capital. In this regard, supporting investment in skills is critical, such as through policies that combine high-quality initial education with vocational education and lifelong learning opportunities, as well as initiatives that support SMEs in attracting talent and appropriate skills to undertake international activity (OECD-WB, 2015). In Portugal, for instance, the “INOV Contacto” programme matches young graduates with companies that seek high-potential human resources aiming for an international career.

Programmes that support internal capabilities through training and skills development can also form a key element of the internationalisation process of SMEs (OECD, 2008). A comprehensive approach to improve SME expertise and strategic capabilities for navigating international markets can be found in programmes that combine training with coaching by a consultant or export adviser. This is the case of Denmark’s Vitus programme, launched in 2010, which targets SMEs with a particularly high international growth potential, offering counselling and one-year intensive coaching for developing and executing an export strategy. On the other hand, policies that impede labour market flexibility and limit immigration might restrict the ability of SMEs to hire the skilled workers needed to reorganise and scale-up production.

Policies that support investment in local innovation, such as through intellectual property protection, R&D fiscal incentives and university-industry collaborations, can play a role in developing SMEs’ capacity to absorb new technologies. Policies that encourage stronger links between firms and research, educational and training institutions can facilitate the knowledge transfers required for upgrading in GVCs. In addition, policies that promote partnerships between SMEs and foreign firms can help to develop or transfer technology, products, processes or management practices (OECD, 2008). For instance, in Turkey, in 2017, following the decision by the Ministry of Economy to provide support to the membership of e-commerce websites, the Turkish Exporters’ Assembly signed an agreement with the e-commerce platforms Alibaba and Kompass, which is expected to foster SMEs participation in global e-commerce markets and create opportunities for new entrants.

Creating a supportive domestic and international operating environment for SMEs takes a whole-of-government approach

The increasingly complex trading environment requires a greater focus on domestic whole-of-the-government approaches. Many of the constraints that SMEs face in internationalising relate to access to information, skills, technology or finance, underscoring the importance of continued action to address them. In terms of trade policy, reducing the costs of importing, through continued liberalisation of goods and services and sustained support for trade facilitation and connectivity, will particularly help SMEs to

better exploit new opportunities. Improved export competitiveness can be achieved through broader policy measures that recognise the important upstream role played by SMEs. Policies should thus be adapted to reflect the holistic view of production, especially in sectors which require scale.

Programmes that provide greater information to SMEs on new opportunities and help promote linkages and partnerships with larger firms, domestically and internationally, can enable SMEs to better exploit their comparative advantage in the production of intermediate goods and services.

Promoting digital connectivity, by increasing the quality of digital infrastructure and decreasing the cost of access, will empower smaller firms to take full advantage of the digital trade revolution. In this regard, it will also be critical for policy-makers to explore ways to meet key public policy objectives in a way that is least trade distorting and preserves the benefits of a free and open internet. This means engaging in greater international dialogue, involving different stakeholders, including firms of all sizes and civil society.

Greater international efforts are needed in this area. As the global economy becomes more interconnected and globalised the opportunity costs of not engaging in further international cooperation rise. From traditional standards to new regulatory issues in the digital age, global challenges require global solutions to provide an international operating environment where SMEs can flourish.

Notes

¹ <http://mneguidelines.oecd.org>

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5. Improving the business environment for SMEs through effective regulation

Summary

- Regulatory conditions are among the most important factors affecting SMEs and entrepreneurship. SMEs usually face bigger challenges than large firms in screening the regulatory environment and dealing with norms.
- In recent years, important progress has been made to reduce the administrative burdens on start-ups, lower legal barriers to entry, and reduce the costs for regulatory compliance in different areas. However, the complexity of regulatory procedures, covering a wide range of areas such as license and permit systems, insolvency and tax, among others, remains a major obstacle to entrepreneurial activity.
- To enhance regulatory conditions for SMEs, there is no one-size-fit-all model. Key elements for SMEs include: simplification of regulations and administrative procedures, regulatory impact assessment, reforms to tax administration and bankruptcy procedures, including to promote a second chance for honest entrepreneurs, improved availability and provision of information, and use of digital technologies to reduce administrative burdens and facilitate collaborative relationships with businesses and citizens

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Why does it matter?

An effective and transparent regulatory environment is key for entrepreneurship and SME development at all stages of the business life cycle, including entry, investment and expansion, transfer and exit. Reducing the regulatory burden on SMEs can facilitate their participation in the formal economy, help improve their productivity and competitiveness, and enhance their participation in and benefits from a globally integrated economy.

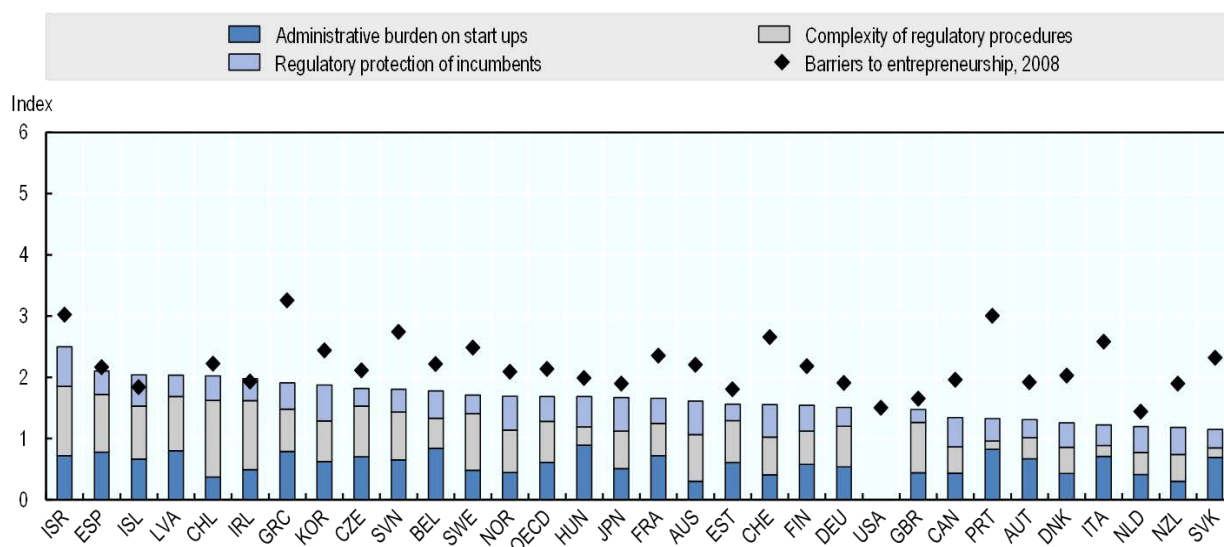
What are current trends and challenges?

SMEs are typically less efficient than large firms in screening the regulatory environment and dealing with norms. The proportion of resources they divert to administrative functions is usually greater than for large firms (OECD, 2017). For instance, about 12% of surveyed European SMEs cite regulation as their most pressing problem compared to 16% in 2016 (EU SAFE survey 2017). For SMEs that participate in global markets and value chains (GVCs), regulatory divergence across countries can impose an additional layer of difficulty. Asked about barriers to trade, 38% of SMEs with a digital presence cite different regulations in other countries as the main challenge to export in 2017 (Future of Business Survey, 2017).

Across most OECD countries, regulatory barriers to entrepreneurship have been declining over time (Figure 5.1). Over the last decade, reforms have focused on reducing the administrative burdens on start-ups, lowering legal barriers to entry, and decreasing the costs for regulatory compliance in different areas (e.g. environment, labour legislation, product standards and certification). For instance, in the OECD area over 2008-13, the number of days required to start a business fell from 14 to 6, and the cost from 5% to 2% of income per capita (median values). In Portugal, a reform was introduced in 2005 which reduced the time to incorporate a company from several months to as little as one hour; and the fees from EUR 2 000 to less than EUR 400. In Chile, since 2013, a virtual one-stop shop allows the creation of a firm in one day, with a single-step, minimal red-tape and at zero cost. In addition, a clear trend towards reducing the stringency of employment protection was observed over 2008-13, mostly focused on individual and collective dismissal of permanent workers.

Figure 5.1. Barriers to entrepreneurship, 2008 and 2013

Scores from 0 (least restrictive) to 6 (most restrictive)



Note: For the United States, the 2013 observation is not available.

Source: OECD (2017), based on OECD Product Market Regulation Statistics (database).

However, the complexity of regulatory procedures remains a major obstacle to entrepreneurial activity. While important progress has been made in the communication and simplification of rules and procedures, challenges persist related to tangled license and permit systems. Countries are taking steps to address the complexity of license systems. For example, in Israel¹, a business license reform was enacted in 2012 to harmonise license requirements across the country and make it more difficult for municipalities to add extra local requirements on top of national ones (OECD, 2016). In December 2017, a new government resolution grouped businesses into different environmental risk categories and made significant reductions in license specifications for low risk businesses.

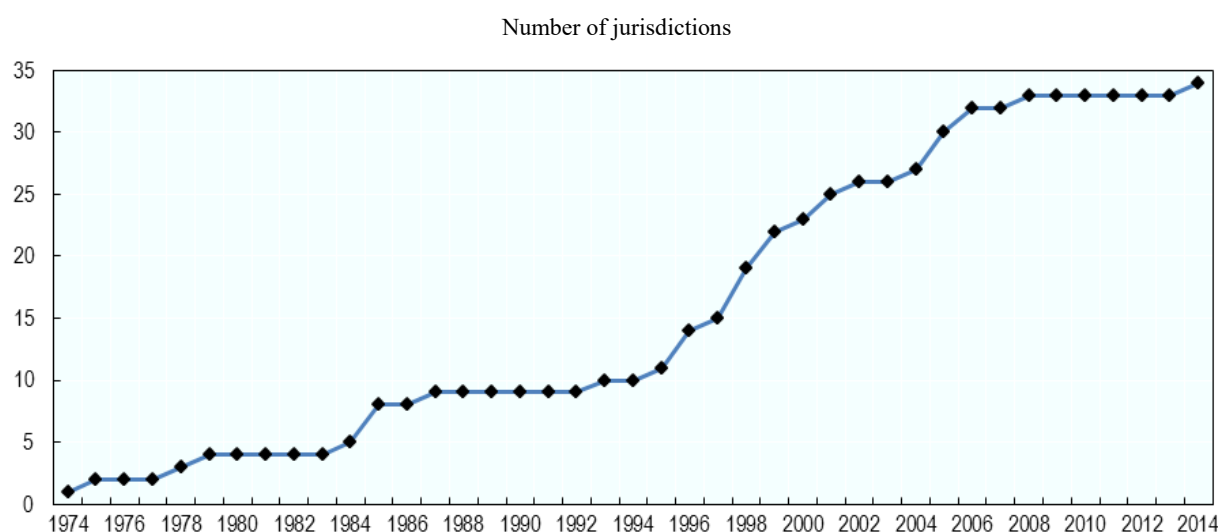
To tackle remaining challenges, recent efforts have aimed primarily to cut red tape for businesses and to improve transparency and cost-efficiency of administrative regulations. In Denmark, for instance, the Business Forum for Simpler Rules was launched in 2012, based on a comply-or-explain principle, to identify business regulations that firms perceive as the most burdensome and propose simplification. In Denmark and Sweden, consultation with the private sector is encouraged through the Burden Hunt Programmes, which engage civil servants in developing smart regulation that can reduce red tape. In the UK, over 2011-13, the Red Tape Challenge website promoted open discussion on how the aims of existing regulation can be fulfilled in the least burdensome way possible. Comments were used by the British government to design a package of 3 000 reforms to cut red tape.

In addition, dedicated institutions have been set up to help SMEs and entrepreneurs to better navigate the regulatory environment, including through the provision of e-government services, and to liaise with official bodies, such as through the creation of digital “one-stop shops,” i.e. single entry points for government services. In this context, the use of digital technologies holds the potential to further streamline procedures for SMEs in particular. In the Slovak Republic, for instance, the introduction of a “silence is consent” procedure and the creation in 2013 of a single contact point to handle notifications and

licenses via the Internet have simplified the process of opening and operating a business. In 2017, Switzerland launched an e-Government platform dedicated exclusively to companies (EasyGov.swiss), which offers a customer-centric integrated approach to business to government interactions, overcoming silos between agencies and federal levels.

Regulatory impact analyses (RIA)² have also become a common practice in most OECD members (Figure 5.2), including in most cases SME impact assessments, although in some countries only for major regulations or selected regulatory instances. In Mexico, for instance, the RIA process provides important public consultation opportunities, as well as safeguards to ensure that adequate account is taken of comments received from stakeholders, including extensive periods of consultation on the draft RIA (OECD, 2015a).

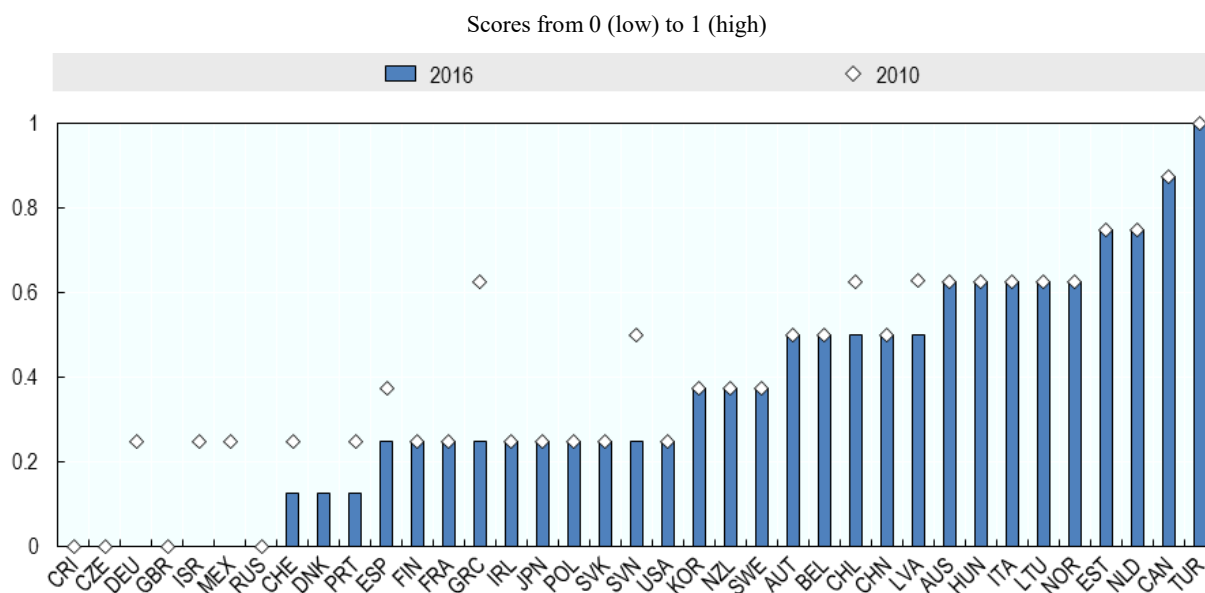
Figure 5.2. Trend in adoption of Regulatory Impact Analysis (RIA) across OECD countries



Source: OECD (2015), Regulatory Policy Outlook.

Inefficient insolvency regimes limit business dynamism, restructuring of viable firms and access to external finance by SMEs. In some countries, in the case of unincorporated micro and small firms, the treatment of individual defaulters is very severe, leaving full personal liability for many years beyond liquidation of the business. Lengthy and complicated processes can significantly affect the capital and reputation of small entrepreneurs, drastically decreasing the chance of starting a business again. The fear of social stigma, legal consequences and inability to pay off debts is stronger in some regions, such as Europe, partly because of much longer debt discharge periods (i.e. the time between liquidation and formal cancellation of debt).

Reforms have been particularly slow in this area, with efforts focusing mainly on prevention and streamlining (e.g. through pre-insolvency regimes), particularly in Europe, although early-warning systems and special insolvency procedures for SMEs are only available in about one-third of OECD countries (Adalet et al., 2017). Over 2010-16, barriers to firm restructuring remained stable or declined only marginally in most countries. In particular, the time to discharge – and thus the personal costs associated with entrepreneurial failure – remains high in many OECD countries (Figure 5.3).

Figure 5.3. Barriers to firm restructuring

Source: Adalet et al. (2017). Calculations based on the OECD questionnaire on insolvency regimes.

High costs and complexity of tax compliance fall disproportionately on small and young firms.

Given the substantial fixed cost of compliance with tax regulatory requirements (e.g. record keeping, filing and payment processes), small businesses are at a disadvantage with respect to large enterprises. For young firms, which also tend to be small, high compliance costs and complexity of tax regimes can exacerbate the resource and cash-flow constraints often experienced in the early stages of business development, and may act as a deterrent to formalisation. In some cases, tax compliance costs for small firms may even exceed their tax cash payments. In recent years, policy approaches have focused on reducing compliance complexity for SMEs, reflecting a more systemic perspective on the SME business environment and activities. Greater emphasis is being placed on ensuring compliance from the outset, making tax compliance a by-product of the steps a business follows to transact. For instance, in Chile, an Electronic Invoicing System allows business taxpayers to issue and receive invoices that are immediately available to the revenue body, and provides, free of charge a simplified and complete accounting system. However, despite widespread reforms in recent years, tax compliance remains a challenge for SMEs. While electronic filing and changes in the payment system have generally reduced the number of payments required by businesses, time to comply has remained stable in most countries (OECD, 2015b, 2017).

While lack of transparency and corruption in the public sector are detrimental to all businesses, they pose particular problems to SMEs, which often lack the capacity to cope with an opaque public sector, design and implement anti-corruption strategies and lobby for their needs in the absence of an established framework for participation in public decision making. Most OECD countries have accelerated the implementation of Open Government Data (OGD), to increase transparency, ease access to information and create opportunities for citizens, businesses and civil society organisations to reuse the data in new ways. For instance, in the United States, a dedicated portal provides public users with access to federal regulatory content and a tool for commenting and influencing the

regulatory process. In addition, several OECD countries have adopted principles of transparency for lobbying activities (OECD, 2017).

What are key areas for policy to consider?

Cross-country evidence suggests that different types of regulatory burdens may have greater importance for SMEs than for large firms, with their impact depending on the general macroeconomic framework, institutional legacy and structure, as well as the sectoral make-up of the economy. At the same time, size-contingent policies that seek to ease the regulatory burden on SMEs with employees below a certain threshold can also produce adverse effects by discouraging these firms to grow (OECD, 2015).

As the complexity of economies increases and new societal needs emerge, regulations need to evolve while limiting burdens and pursuing cost efficiency. However, there is no "one size fits all" model for regulatory reform, and policy responses need to be context-specific, while following established good practice principles for regulatory reform, as outlined in the **2012 Recommendation of the OECD Council on Regulatory Policy and Governance**. Key areas for policy consideration include:

- **Improving the efficiency of bankruptcy procedures and fostering a second chance for honest entrepreneurs:** This can include reduction in the time for discharge, which decreases the administrative burden imposed on entrepreneurs in the course of bankruptcy procedures. In several countries discharge is automatic and does not require an additional court decision.
- **Facilitating tax compliance:** Process simplifications, particularly through targeted use of technology, can be a powerful tool to enhance compliance and to reduce its costs. Certain tax preferences may help support SME creation and growth. However, such measures should be carefully targeted to ensure that they meet their policy objectives in a cost-effective way and do not create further distortions or complexities.
- **Cutting red tape for businesses:** Consultation with the private sector and continuous dialogue with citizens can support civil servants in developing smart regulation that reduces red tape. An increasingly popular instrument for controlling the administrative burden on business is the One-for-One rule (or one-in-one-out rule), which stipulates that regulators must remove a regulation each time they introduce a new one that imposes an administrative burden on business. At the same time, policy needs to consider potential trade-offs and strike a balance between regulatory exemptions or simplifications and compliance to norms across different areas, such as, for example, labour protection.
- **Strengthening public sector integrity and transparency, and conducting regulatory impact analysis (RIA) to enhance the effectiveness of regulation and assess its implications for SMEs:** Regulatory frameworks can support regulators in analysing the specific impact of legislation on SMEs, and in considering flexible regulatory options that reduce costs for small businesses. At the EU level, the SME Test helps implement the "Think Small Principle", by analysing possible effects of EU legislative proposals on SMEs, including through: i) consultation of SME stakeholders; ii) identification of affected businesses; iii) measurement of the impact on SMEs (cost-benefit analysis); and iv) assessment of alternative mechanisms and mitigating measures. For major regulation, focus groups and panels can be used to produce full tests of regulatory impacts on SMEs.

A regulatory policy body, close to the centre of government and responsible for regulatory oversight, can ensure that regulation serves whole-of-government policy, although the specific institutional solution should be adapted to each system of governance.

Notes

¹ The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

² Regulatory Impact Analysis (RIA) is a systemic approach to critically assessing the positive and negative effects of proposed and existing regulations and non-regulatory alternatives through a range of methods. In many OECD countries, it has increasingly become an important element of an evidence-based approach to policy making.

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6. Business transfer as an engine for SME growth

Summary

- Many economically sound SMEs exit the market as a result of problematic business transfers, with negative effects for the growth and innovative potential of economies. In the coming years, with the ageing of entrepreneurs, the volume of business transfers is expected to become increasingly significant in many OECD countries.
- Successful business transfer of viable SMEs at different stages of their life cycle is crucial to retain employment, preserve the value of assets and ensure continuity in production processes and business relations. Furthermore, business transfer can represent an opportunity to rethink a firm's strategic vision and business model, innovate and seize new opportunities, as well as for new entrepreneurs to enter the market.
- Business transfers can be a complex matter due to the number of parties typically included in the process, the need for business valuation, and the variety of regulations that apply. Financial and administrative requirements typically add to the regulatory and management challenges.
- In recent years, governments have taken action to improve the conditions for business transfer, such as through gift and inheritance tax preferences, special financial facilities, and the development of platforms for business transfer.
- There is a need to improve the evidence base on business transfer trends; raise entrepreneurs' awareness of the importance of early succession planning and acquisition opportunities for new entrepreneurs; support the development of business transfer markets; tackle administrative burdens and regulatory complexities; consider tax consequences on sale or disposal of SMEs; and ensure an appropriate financing offer to ease transfer.

Why does it matter?

Business transfer¹ represents a critical stage in the life of many small businesses, which the ageing of the population of entrepreneurs has brought to the fore in many OECD countries. In Japan, for instance, more than 300 000 SME incumbents will attain the age of 70 within the next five years according to recent figures by the Ministry of Economy, Trade and Industry. In Italy, about 9% of entrepreneurs are over 70. In Austria, 27% of all SMEs in the industrial economy, accounting for 30% of employment, are expected to be handed over in the period from 2014 to 2023 (Ziniel et al., 2014). In Canada, approximately 50% to 60% of business owners will retire over 2017-27. In Switzerland, as of 2013, 22% of SME incumbents intended to pass ownership over in the next five years and 25% were seeking to hand the leadership position over (Christen et al., 2013). Furthermore, in former socialist economies in Central and Eastern Europe, the first generation of entrepreneurs is nearing retirement, leading to a significant proportion of the business stock having to be transferred in the coming years.

Against this backdrop, a significant number of economically sound SMEs disappear from the market as a result of problematic transfers, with implications for economic growth, employment, innovation and social inclusion. In the European Union, for instance, around 450 000 SMEs change ownership annually, affecting more than 2 million employees, but up to one-third of these transfers may not be successful, thus endangering around 150 000 enterprises and 600 000 jobs (European Commission, 2013). In Japan, about one fifth of micro firms consider that it is unavoidable to discontinue the business in one's own generation, and approximately 70% of those managers who think that business closure is unavoidable have come to this conclusion without actually considering the possibility of business transfer (Government of Japan, 2014). The challenge is exacerbated in rural areas, since urbanisation trends make it more difficult for business owners to find eligible successors.

While the retirement of the business owner is one of the main reasons for the business transfer, other drivers include the pursuance of other career opportunities by the entrepreneur, the sale of the business to set up a new enterprise, or unforeseen events. In all cases, closures of economically viable SMEs as a consequence of problematic business transfers can induce job losses, domino effects on local enterprises and suppliers, and the loss of specialised knowledge. Failed transfer processes also negatively affect the individual entrepreneur and his/her family, such as through the forfeiture of family assets. Furthermore, unresolved transfer arrangements can harm ongoing and future business prospects, such as by unsettling business partners, customers and suppliers. For instance, pending transfer planning may induce customers to refrain from business deals, due to uncertainty over the firm capacity to guarantee supply in the long-term. Also, financial institutions may be induced to downgrade creditworthiness (Schlepphorst, 2016).

Successful business transfer of economically sound SMEs is crucial to retain employment, ensure continuity in production processes and business relations, and preserve the value of tangible and intangible assets. Furthermore, business transfer can provide an opportunity to rethink the strategic vision and business model of the enterprise, and to introduce innovations and new management practices. Business transfer may also represent an opportunity for new entrepreneurs to take over a business (Brigham et al., 2007).

What are current trends and challenges?

One of the major challenges for SME business owners is the identification of a capable and willing transferee, as well as an appropriate form of transfer, which may include mergers and acquisitions (M&As) (i.e. sales to other enterprises), initial public offerings (IPOs), transfer of ownership to foundations, and the succession to family members. For example, more than half of Canadian SMEs view the identification of a successor as a major obstacle in planning the business transfer (Canadian Federation of Independent Business, 2012). In Switzerland, the number of potential successors per SME executive director is expected to drop from 4.3 in 2016 to 3.4 by 2030 (Andric et al., 2016).

In the case of family businesses, entrepreneurs often strive to keep the business ownership within the family. In Switzerland, for example, more than 40% of the current incumbents took the business over from a family member (Christen et al., 2013). In the Netherlands, 73% of those family businesses that have undergone a business transfer report a family relation between the former and the new business owner (Flören et al., 2010). However, non-family transfers have increased in recent years, and will likely gain further importance in the future in many OECD countries, due to the decreasing number of family descendants; the wider access to education by youth, leading to more career options outside the family firm; and greater involvement by descendants of business owners in succession decisions.

Business transfer can also take the form of transfer to individuals who are employed in the company, such as employees (i.e. Employee-Buy Outs - EBOs) and executives (i.e. Management-Buy Outs - MBOs), whose knowledge of the company and the business owner generally facilitates sales negotiations. However, the lack of a second executive in most smaller enterprises makes MBOs relatively rare. Also, the short “cognitive” distance between these insiders and the established business model can prove detrimental if strategic realignments are necessary. In contrast, individuals who are external to the business can often make such changes more easily, such as in the case of acquisition by a private and non-self-employed person (i.e. Management-Buy-In - MBI), although a longer familiarisation period for the new owner to understand existing structures and procedures is typically required.

In the context of increasing globalisation and saturated domestic markets, young firms and SMEs are increasingly the target of mergers and acquisitions (M&As) by other companies, including for growth purposes, the broadening of a company’s product range or the strengthening of technological competencies (Hussinger, 2010). In the case of small family businesses, however, the sale to strategic investors may be resisted, including because of a fear of the loss of (local) jobs.

Initial Public Offerings (IPOs) (i.e. the issue of shares to raise capital from a wider group of investors) can be a transfer option, but it is rarely considered a feasible option for SMEs, and family businesses in particular, including businesses with high growth potential, largely due to disclosure requirements and costs, but also for the dilution of ownership and the loss of managerial discretion that going public entails.

Transferring a business can be a complex task, which demands adequate planning and competencies. The complexity arises from the number of parties that are typically included in the process, often with differing expectations, the involvement of advisors and financial institutions, as well as the variety of regulations that apply, such as contract arrangements and tax law, including on gift and inheritance, and the incumbents’ pension schemes. In addition, the valuation of the enterprise typically represents a critical and complex stage in the transfer process.

The absence or delay in transfer planning further challenges the transferability of enterprises. The transfer process is in most cases a unique event in the transferors' and transferees' life, for which they have no or only little experience. Furthermore, owners of SMEs often begin to deal with their own withdrawal relatively late. For instance, a survey conducted by the Family Firm Institute in 2017 illustrates that while 79% of family-owned businesses plan to transmit the management within the family, only 16 % of these firms have prepared a consolidated family succession plan. Proper preparation is all the more necessary if the business operates across different countries, since different local operating conditions and business relations increase the amount of "managerial know-how" that must be acquired and mastered by the new owner.

The takeover of established businesses often requires financial capital. Smaller businesses typically rely on personal resources from the owner (beyond the company's equity) when a transfer or selling takes place. An additional financial weakening can occur when other family members need to be paid out (OECD, 2017). Approximately every second Canadian SME owner, for instance, ranks obtaining the necessary financing for a takeover among the top barriers of transfer planning (Canadian Federation of Independent Business, 2012). Even if the necessary amounts are usually not very large on average, transferees can experience difficulties in raising finance. Almost 43% of German transferees, for example, invest up to EUR 10 000 and almost 33% up to EUR 25 000 in a business transfer (Ullrich and Werner, 2013).

In addition, administrative obligations can pose a challenge. In some countries, businesses are legally required to inform employees of the transfer. In Germany, for instance, the business owner has to inform each employee in writing about the business transfer, including the exact timing of the (intended) transfer, the reason for transfer, legal, economic and social consequences for the employee, as well as the intended measures that may affect the employee (e.g. protection against unfair dismissal, further training measures that result from changes in production). In 2014, similar legislation was adopted in France.

To sum up, failures in business transfer are driven by a combination of factors. However, in the absence of current and representative statistical data on business transfers, due also to different definitions and data collection frameworks across countries, the mortality or survival rates of businesses before and during transitions remain largely unknown.

What are key areas for policy to consider?

Many countries have recognised the importance of business transfers for SMEs and taken action to improve the conditions for business transfer. For instance, at the European level, in 1994, the European Commission issued Recommendations on the transfer of small and medium-sized enterprises. Business transfer issues are also specifically addressed by the EU Small Business Act and easing business transfer is indicated as a priority in the Entrepreneurship 2020 Action Plan (European Commission, 1994, 2012).

A variety of strategies and instruments are being developed to ease SME transfer conditions. These include awareness raising, special financial facilities designed to finance transfers, legal transformation (notably the possibility to create public limited companies facilitating the selling of a firm), as well as transparent markets for business transfers. Key areas for policy makers to consider include:

- **Improving the evidence base:** Despite considerable progress in research on business transfers in recent years, better evidence is needed to monitor business transfer processes across countries, sectors, firm typologies and entrepreneurs'

characteristics, assess the main causes of transfer failure and main impediments to cross-border transfer, and identify the levers for successful transmission in different contexts, including the growth performance of transferred firms and the impact on jobs. A better understanding is also needed of the implications of various tax issues for SME business transfer.

- **Increasing awareness of the importance and complexity of business transfer planning, including for expected and unexpected transfers:** National awareness campaigns have proven useful to inform (upcoming) entrepreneurs through brochures, seminars, innovative digital tools such as webinars and social media, as well as through personal consultations. Regionally located tax, financial and legal experts, as well as chambers of commerce and business development agencies, are well placed to provide necessary information. In this regard, appropriate training of the professionals involved can contribute to improve knowledge. In addition, incumbents of all ages need to be made aware of the importance of planning for business transfers in case of emergencies. Useful tools include “emergency kits”, which can facilitate smooth transitions in case of sudden events, comprising, for example, copies of important documents such as testament, business agreements, life insurances and essential passwords for accessing business systems.
- **Increasing the number of (potential) transferees:** Raising awareness by potential new founders regarding the possible takeover of established companies, as well as promoting entrepreneurship among all segments of the population, including among disadvantaged groups such as women, youth, ethnic minorities or migrants, can contribute to addressing “transfer gaps”. Online marketplaces for business exchanges have been set-up in recent years, including by the private sector. For instance, in Europe, an association on SME transfer was created in 2010, Transeo, which gathers public and private operators in the SME transfer market, with the aim to promote collaboration and exchange of information and good practices.
- **Ensuring appropriate financing conditions:** In some countries, development banks or public financial institutions provide a range of mezzanine or subordinated loans to enterprises that change ownership. Specific loan programmes, including micro-credits for young, first time entrepreneurs taking over a business are also used to ease the financial burden associated with a business transfer. For instance, “take off loans” to young entrepreneurs are offered by Finland’s public development institution, Finnvera, and by the French *Réseau Entreprendre*, a private association running a regional network with the participation of public partners. Although it currently accounts only for a limited number of operations by SMEs, venture capital can also serve transfer purposes and, in Denmark, a dedicated matching online site supports buyers that seek additional equity from venture capital firms (OECD, 2017). Disseminating information about available instruments, including a clear description of eligibility conditions, along with contact details, can help increase the use of existing programmes.
- **Considering tax consequences on sale or disposal of SMEs.** Several OECD countries have introduced preferences targeted at SMEs under gift and inheritance taxes, with the aim to address adverse tax consequences, including on retirements savings or intergenerational transfer of assets, and ease business transfer (Box 6.1). At the same time, the introduction of preferences on the disposal of SME assets should be considered against the revenue and efficiency costs of doing so, including

the risk of creating further distortions, such as discrimination against transfers of private wealth relative to transition of business ownership (OECD, 2015).

Box 6.1. Gift and inheritance tax preferences in selected OECD countries

Germany provides an exemption from gift and inheritance taxes if the successor continues to hold the business and keeps the wage bill steady. This requirement is relaxed for SMEs so that they only need to continue to hold the business.

Hungary exempts the inheritor or donee of the SME's assets from stamp duties or gift taxes, depending on the number of employees and net sales revenue.

Italy allows transfers of firms or shares to the spouse or descendant to be exempt for inheritance tax if the activity is carried on (or for shares, if control is retained) for five years.

In **Japan**, there are various measures to ease the transition of the business, including reducing the taxable value of sites for business under the inheritance tax by 80%, up to a limit of 400m², deferment of inheritance tax payments and gift tax on unlisted shares.

The Netherlands provides a provisional exemption for inheritance taxes of businesses that are continued for at least five years. This exemption applies at 100% up to a going concern value of EUR 1 045 611 (in 2014) and at 83% for values above this amount.

With respect to closely-held businesses, the **United States** allows estate tax to be paid over a 10 year period if the value of the business exceeds 35% of the estate and the owner had an interest of at least 20% in the business. Only the tax relating to the interest in the business may be deferred. The United States also allows a special use valuation for real property used as a farm or in another trade or business, allowing them to be valued for estate tax purposes at actual use rather than highest and best use. This can decrease the value of the asset by up to a maximum of USD 750 000, which is adjusted for inflation since 1997.

Belgium also provides preferences under gift taxes, although these are levied at the regional level.

Source: OECD (2015), Taxation of SMEs in OECD and G20 Countries, OECD Tax Policy Studies, No. 23, OECD Publishing, Paris.

Notes

¹ Business transfers are commonly understood as the transfer of ownership of a company to one or more legal entities or natural persons.

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7. Developing entrepreneurship competencies

Summary

- Entrepreneurship competencies combine creativity, a sense of initiative, problem-solving, the ability to marshal resources, and financial and technological knowledge. These competencies enable entrepreneurs and entrepreneurial employees to provoke and adapt to change. They can be developed through entrepreneurship education and training that focus on promoting an entrepreneurial mindset and behaviours.
- Schools, vocational and higher education institutions are increasingly developing these competencies in students by enriching their study programmes with dedicated entrepreneurship education courses, either as self-standing modules or embedded into curricula. Problem-based teaching and assessment methods are particularly successful.
- Key priorities for public policy include introducing a progressive approach to entrepreneurship education over the student's lifetime; specialised entrepreneurship education training and support for teachers; and strengthened business start-up support in vocational and higher education institutions, including linkages between education institutions and existing business support organisations.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Why does it matter?

Entrepreneurial employees are among the major enablers of SME innovation. They are critical to the capacity of SMEs to provoke and adapt to change, alongside entrepreneurs themselves, who fulfil a three-fold role as creators, organisers and market-makers (Schoonhoven and Romanelli, 2002). There is an underlying set of entrepreneurship competencies that allows individuals to identify, create and act upon opportunities in order to create value, by marshalling resources, demonstrating self-efficacy and confidence in ability to achieve, and persisting in the face of obstacles (OECD, 2014). The formal education system can make an important contribution to the development of these entrepreneurial competencies.

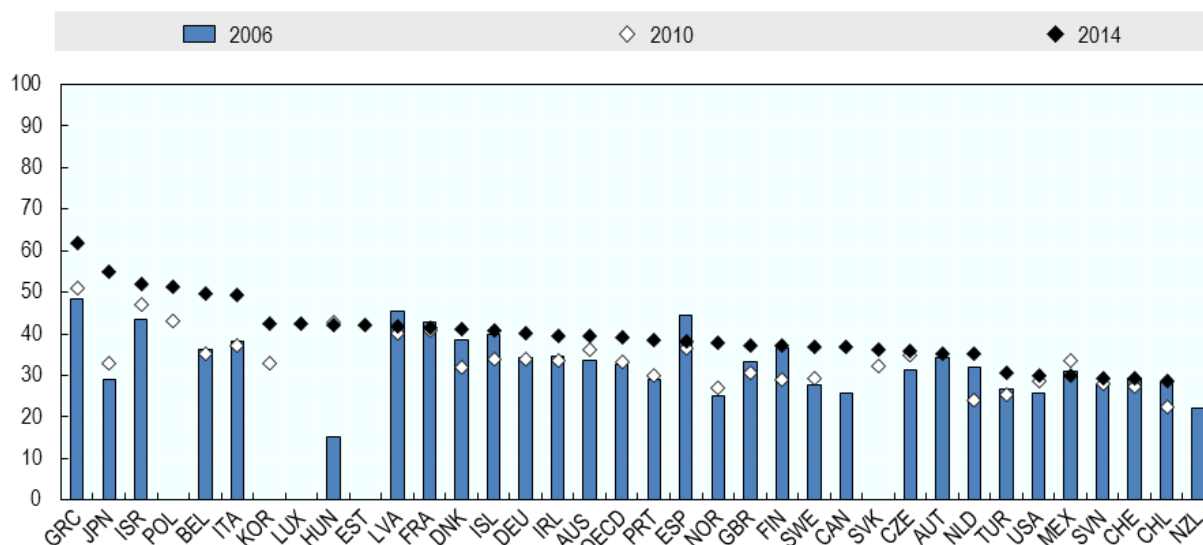
What are current trends and challenges?

A perceived lack of capabilities remains one of the most frequently cited barriers for people to start a business. This is in particular a challenge for the youth (18-30 years old), who have to rely more on education to gain relevant knowledge and skills. Across all OECD countries, more than half of the youth surveyed in the period 2012-16 reported a lack of entrepreneurship knowledge and skills (OECD/European Union 2017a).

One of the aims of developing competencies for entrepreneurship is to reduce the fear of failure through a combination of measures focused on awareness-raising, as well as providing knowledge and know-how that allow individuals to demonstrate resilience and persistence in the face of obstacles. This continues to be an important area for intervention, since in most OECD countries, fear of failure as an impediment for starting a business has been rising (Figure 7.1).

Figure 7.1. Fear of failure, 2006, 2010 and 2014

Percentage of 18-64 year-old population, who indicates that fear of failure would prevent them from setting up a business



Note: New Zealand refer to 2005 instead of 2006; Austria, Israel¹, Portugal and Switzerland refer to 2007 instead of 2006; Czech Republic, Poland and Slovak Republic refer to 2011 instead of 2010; Czech Republic, Israel, Korea, Latvia and Turkey refer to 2013 instead of 2014..

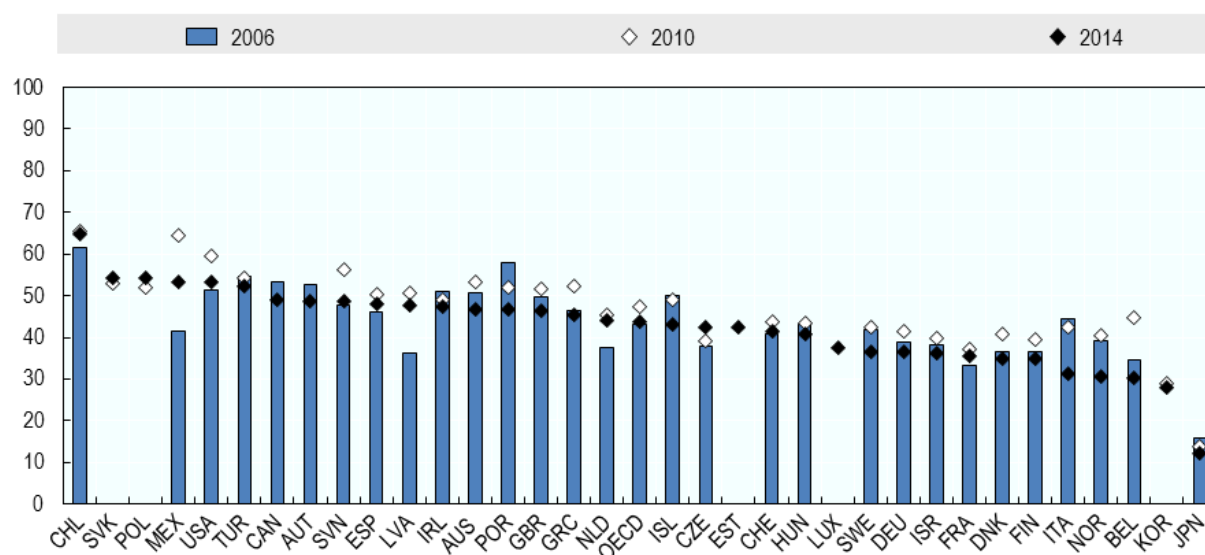
Source: OECD (2017b), based on data from the Global Entrepreneurship Monitor.

Globally, efforts to build entrepreneurship competencies through education have increased significantly over time. In many OECD countries, schools, vocational education and training institutions and higher education institutions are enriching their study programmes with dedicated courses on how to start a business, either as self-standing modules or embedded into curricula. As part of lifelong learning, these courses also target individuals already working in firms, including SMEs. In Europe, 27 out of 38 countries participating in Eurydice (the European Union's network to enhance co-operation in lifelong learning) dedicate public funding to entrepreneurship education (Eurydice, 2016). Developing countries are also becoming more active in this area. In several African states, the United Nations Industrial Development Organization (UNIDO) collaborates with governments through the Entrepreneurship Curriculum Programme to introduce entrepreneurship education into secondary education and vocational education and training (UNIDO, 2017).

A common aim is to nurture an entrepreneurial culture and to stimulate innovation. Emphasis is placed on helping people to consider the desirability and feasibility of starting a business or acting entrepreneurially as an employee - and to develop the ability to cope with failure. Recent survey results show that progress requires long-term endeavours. The share of people reporting possessing the knowledge and skills to start a business has not grown significantly over the period 2006-14 (Figure 7.2).

Figure 7.2. Perceived capabilities for entrepreneurship, 2006, 2010 and 2014

Percentage of 18-64 year-old population, who believes they have the required skills and knowledge to start a business



Note: New Zealand refer to 2005 instead of 2006; Austria, Israel, Portugal and Switzerland refer to 2007 instead of 2006; Czech Republic, Poland and Slovak Republic refer to 2011 instead of 2010; Czech Republic, Israel, Korea, Latvia and Turkey refer to 2013 instead of 2014.

Source: OECD (2017b), based on data from the Global Entrepreneurship Monitor.

Competencies for entrepreneurship need to be developed over the full course of education, with the extent of business start-up orientation being increased in later years (OECD, 2014). Several countries (e.g. US, Ireland, Denmark) have opted for a progressive approach in which early intervention is followed up by evenly distributed interventions throughout secondary and tertiary education. However, in many countries there is a lack of entrepreneurship education activities in lower levels of education (GEM, 2017). When

early intervention does not take place, however, it will be challenging to develop certain entrepreneurship competencies at later stages (Cunha and Heckman, 2010).

There is an increasing move to codify entrepreneurship competencies in order to help design and deliver appropriate education responses. Entrecomp, for example, is a competence framework used in European Union countries (see Table 7.1). For each of the competencies, the framework sets out a set of defined learning outcomes and a description of different levels of achievement. The aim is to encourage the use of the framework for curricula design and teacher training (European Commission, 2016).

Table 7.1. The entrepreneurship competencies identified in the EntreComp entrepreneurship competency framework

Ideas and opportunities	Resources	Translation into action
Spotting opportunities	Self-awareness and self-efficacy	Initiative taking
Creativity	Motivation and perseverance	Planning and management
Envisioning	Mobilising resources	Coping with uncertainty, ambiguity and risk
Valuing ideas	Financial and economic literacy	Working with others
Ethical and sustainable thinking	Mobilising others	Learning through experience

Source: European Commission (2016), *EntreComp: The Entrepreneurship Competence Framework*, Publication Office of the European Union.

A common approach in entrepreneurship education is problem-based learning (OECD, 2014b), the success of which depends on the overall learning environment. Findings from the OECD's Programme for International Student Assessment (PISA) show that the teaching and learning methods used in some countries are more effective at developing problem solving skills than others, and even countries which are very good at teaching reading, mathematics and science literacy can be weaker in developing students' problem-solving abilities (OECD, 2017a).

Traineeships, study visits and "job shadowing" can potentially represent very conducive learning environments for problem-based learning and the development of entrepreneurship competencies. Large firms and multinational companies are good at making use of engagement opportunities through well-structured programmes. SMEs, instead, often face collaboration barriers related to size and a lack of structured contacts with educational institutions (OECD, 2015a).

In addition, teachers play a fundamental role in building entrepreneurship competencies. Effective teaching requires adequate preparation time from teachers, tailored education material and guidelines that facilitate the collaboration with external partners (OECD, 2015b). In many countries, teacher networks have been formed to provide peer support for this (e.g. US Network for Teaching Entrepreneurship, NFTE), whereas public policy has so far played a less active role.

So far, most efforts to promote entrepreneurship competencies have been undertaken in higher education institutions, where incubation facilities, mentoring and support to access financing are growing quickly, partly in response to an increasing demand from students and young scientists, as well as opportunities to commercialise research (OECD/European Union, 2017b). At this level, there has been an increase in best practice exchange among stakeholders across different institutions. For example, HEInnovate, a joint initiative of the European Commission and the OECD, is a guiding framework to establish effective approaches to support entrepreneurship and innovation through higher education. Part of

this is an on-line development platform (www.heinnovate.eu) that supports higher education institutions to design and implement graduate start-up support actions, as well as entrepreneurship education and knowledge exchange mechanisms more generally. The framework also provides guidance on how to create effective linkages between HEIs and SMEs. However, there has been less activity and exchange at upper secondary and vocational levels of education.

What are key areas for policy to consider?

Formal education can play an important role in developing entrepreneurship competencies. However, a cultural shift is likely to take a generation, if not more. For governments, this means a long-term commitment to supporting entrepreneurship through education. Key areas for policy consideration are:

- **Developing a progressive approach to promoting entrepreneurship competencies that builds up with the stage of education.** Efforts to develop entrepreneurship competencies through formal education will be most effective if organised in a progressive way that covers all levels of education, starting early on with laying out the foundations of an entrepreneurial mind-set and building on this with targeted and specific activities the closer learners get to choose their career paths.
- **Supporting teachers.** Teachers need to be supported in their new roles of promoting entrepreneurship competencies. Continuous professional development, temporary mobility programmes to gain work experience in industry and civil society, the involvement of teachers in new curricula design, and sharing monitoring and evaluation information on the success of different entrepreneurship education approaches are promising ways of support.
- **Closing gaps in start-up support.** Activities to develop entrepreneurship competencies should be paired with business start-up supports for students who are motivated and able to start a business in the near future, starting at upper secondary level and continuing through vocational and higher education. Close connections between education institutions and support offered by local business support organisations such as business incubation, finance and mentoring are important to achieve this objective. Students in higher education should be supported to combine studies and their start-up efforts, for example by receiving a special status similar to sport champions.
- **Policy co-ordination.** Providing a sustainable answer to the question of how to effectively develop entrepreneurship competencies brings together different policy portfolios. The aim should be to carefully balance different objectives - education, employability, innovation - to prepare learners to succeed in an unknown future. A cross-portfolio approach is needed that involves collaborations across different ministries, facilitates co-ordination and tailoring of activities across different levels of education, and allocates financial resources in a balanced and mutually-supportive manner.

Notes

¹ The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

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8. Promoting innovation in established SMEs

Summary

- Innovation is a key determinant of productivity and long-term growth. Supporting innovation in established SMEs can foster inclusive growth by reducing productivity gaps and wage gaps between SMEs and large companies.
- SMEs are, on average, less innovative than large enterprises. However, some small enterprises are highly innovative and can reach productivity levels above those of large companies. Companies which develop and use their internal strategic resources effectively (e.g. managerial and workforce skills, ICT, R&D, etc.), and collaborate with external partners in the innovation system, have better innovation performance.
- Governments can support innovation in SMEs by fostering a sound business environment, helping SMEs to develop and use their internal strategic resources effectively, and building an innovation system that is effective in the commercialisation of research and inclusive of a large range of SMEs.

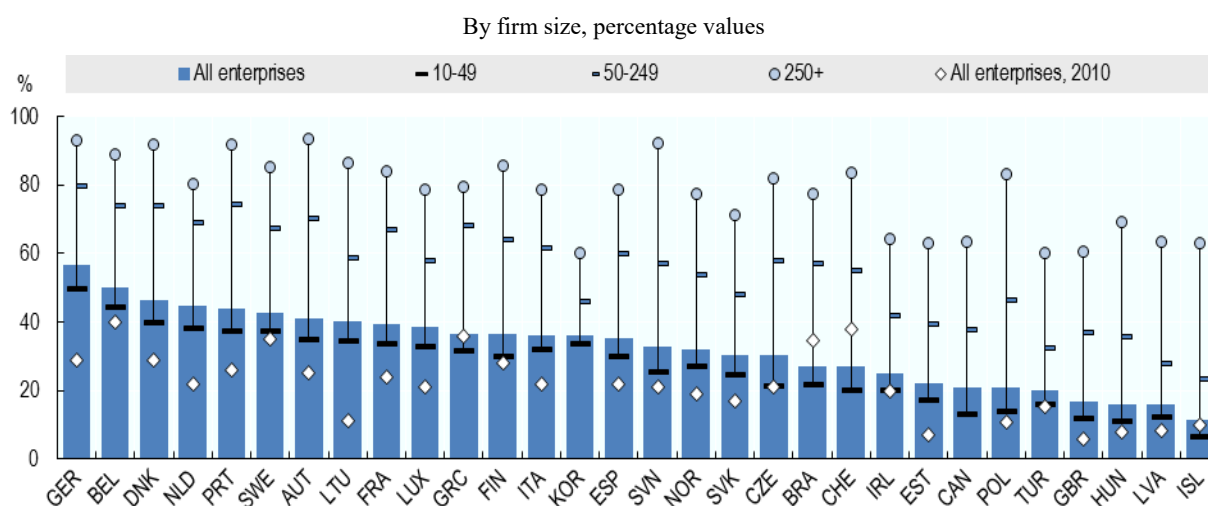
Why does it matter?

Innovation is a key driver of productivity and long-term growth and can help solve social challenges at the lowest possible cost (OECD, 2015a). Innovation in small and medium-sized enterprises (SMEs) is at the core of inclusive growth strategies: more innovative SMEs are more productive SMEs that can pay better wages and offer better working conditions to their workers, thus helping reduce inequalities. Furthermore, recent developments in markets and technologies offer new opportunities for SMEs to innovate and grow. Digitalisation accelerates the diffusion of knowledge and is enabling the emergence of new business models, which may enable firms to scale very quickly, often with few employees, tangible assets or a geographic footprint (OECD, 2017c).

What are current trends and challenges?

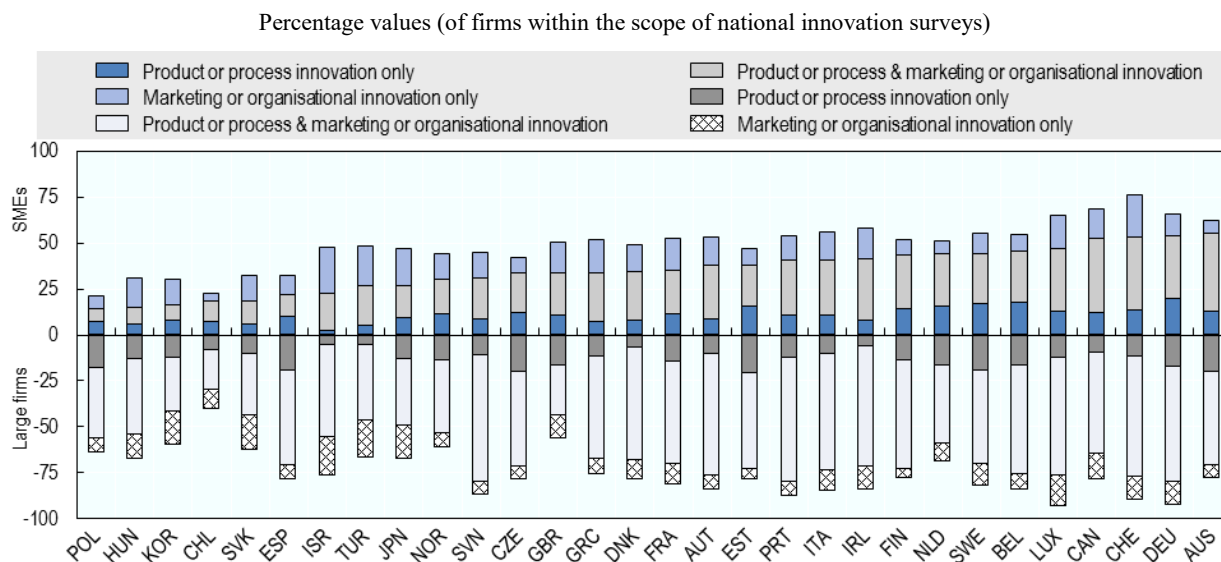
SMEs are, on average, less innovative than large companies. For example, across OECD countries, the median value in the national SME share of business R&D is 35%. Moreover, small firms (10-49 employees) are approximately only half as likely as large firms to have a business website allowing for online ordering and only one-third as likely as large firms to be using Enterprise Resource Planning (ERP), a software platform that integrates core business processes in real-time (Figure 8.1).

Figure 8.1. Use of enterprise resource planning, 2015



Source: OECD ICT Database.

However, aggregate figures conceal an extremely heterogeneous reality (OECD, 2017a). Survey data show that a significant proportion of SMEs engage in all forms of innovation, especially in higher-income countries (Figure 8.2), and that even the smallest employer enterprises (i.e. less than 10 workers) can reach productivity levels above the large-company average (OECD, 2017b).

Figure 8.2. Innovation types by firm size, 2010-12

Source: OECD (2015), OECD Science, Technology and Industry Scoreboard 2015, OECD Publishing.

The contribution of SMEs to innovation has increased in recent decades thanks to changes in the way innovation takes place in the economy (OECD, 2017d). Enterprise innovation is no longer limited to corporate R&D labs, and is often the outcome of collaborative efforts in which businesses interact and exchange knowledge and information with other partners as part of broader innovation systems. This shift towards an ‘open innovation’ paradigm has reduced the need for innovation-related capital investments, making business innovation more accessible to SMEs (OECD, 2010a). Furthermore, especially in science-driven sectors (e.g. biotech and nanotech), small businesses are often the source of radical innovations, thanks to their flexibility and to their ability of working outside of dominant knowledge paradigms; for example, SMEs account for about 20% of patents in biotechnology-related fields in Europe (OECD, 2017d). SMEs also constitute the bulk of high-growth firms, which are quintessentially “innovative” enterprises able to grow fast over a short period of time thanks to disruptive changes in their ‘business as usual’ practices (OECD 2010b; OECD, forthcoming).

Differences in SME performance and growth orientation result from how internal strategic resources are leveraged to invest in in-house innovation and to collaborate with external partners. Evidence points to a strong link between better managerial skills and formal management practices (e.g. HRM, standards and certifications, accounting, etc.) on the one hand and productivity growth on the other (OECD, 2017b). By way of example, process innovation often involves cost-reduction strategies, whose success depends on the capabilities of the company management. Similarly, the adoption of Industry 4.0, which involves the use of automation and digitalisation in manufacturing, requires strong managerial skills in SMEs.

Many governments have supported the upgrading of managerial skills in SMEs, both in low-tech and high-tech industries. Canada’s Operational Efficiency Programme, for example, strengthens operational efficiency in manufacturing SMEs by enabling participating companies to benchmark and monitor their operational performance against the industry average. The objective is to eliminate causes of waste in the production process

and to make the business process more productive. Mexico has delivered a large-scale six-hour management training course for micro business owners in traditional sectors (e.g. retail trade). As part of this programme, low-skilled entrepreneurs receive an electronic tablet which embeds the management training software programme and enables customer electronic payments.

Workforce skills are also important, especially in small businesses where a larger proportion of workers than in large companies are involved in the implementation of business innovation on the ‘shop floor’. In this respect, there is evidence that SMEs that provide employees with opportunities to develop problem-solving skills and to make use of their knowledge are more likely than others to succeed in developing new products or processes (OECD, 2015b). Governments in OECD countries support workforce training in SMEs through policies which encourage the formation of business training groups. Examples include Germany’s Inter-company Vocational Training Centres, Australia’s Group Training Organizations, and Korea’s Training Consortia. This approach has important benefits both for the government and for small businesses: governments can reach a larger number of companies through a single policy intervention, while small businesses gain access to better trainers at lower costs and learn from their peers in the same training group.

The adoption and effective use of ICT hardware and software is a form of business innovation, but also a prerequisite and further driver of other forms of business innovation. Certain management software (e.g. customer relationship management or enterprise resource planning) can support the professionalisation of small business management, but may require upstream improvements in managerial skills through training and consulting (see Box 8.1). Some digital technologies are more relevant than others for SMEs. For example, cloud computing can enable businesses to rent computing infrastructure and software services from a third party provider without upfront investment in ICT capital (OECD, 2017c; OECD 2014). It can also alleviate the need for on-site IT staff, and can enable SMEs to make use of other relevant digital technologies such as data analytics, i.e. the use of raw “big data” for business purposes after adequate cleaning and processing. Policies which support investment in ICT should take into consideration the level of development, technology needs and managerial skills of the targeted companies.

Box 8.1. Upgrading managerial skills through ICT in SMEs: A review of government programmes

A recent OECD comparative analysis of government programmes aimed at improving managerial skills in small enterprises, mostly from traditional sectors of the economy (e.g. retail trade and low-tech manufacturing), finds that combining management training and consulting with support in ICT use is a common approach to boosting innovation in small low-tech enterprises. This combined offer tends to improve the performance of participating companies through, among others, a better understanding of local markets, benchmarking their performance against the local industry average and sourcing inputs at lower cost. However, similar programmes need to have simple rules and low per-recipient costs if they want to reach low-skilled entrepreneurs. Moreover, drawing on private-sector trainers and advisors in the implementation phase helps these programmes have a stronger impact.

Source: OECD (2016), “Increasing Productivity in Small Traditional Enterprises: Programmes for Upgrading Managerial Skills and Practices”, CFE/SME(2016)6

The large majority of SMEs do not have an IPR strategy in place, nor do they integrate IPRs into their overall business strategy or model, which is mostly the result of lack of knowledge and expertise in SMEs. Obstacles to the use of IPR become particularly acute when SMEs operate internationally and may involve legal overheads, multiple filings, regulatory and technical differences across countries, and the robustness of local IP enforcement (OECD, 2011). Supporting the development of managerial skills is also important to spread the use of IPRs in SMEs.

SMEs are also often unaware of the close link between business innovation and business survival and growth, or may not be cognisant of how to engage in innovation; for example, small enterprise owners are often unaware of the extent to which digitalisation can improve their business (OECD, 2017e).

Small businesses may also be discouraged to innovate if large (international) players have dominant market positions, which may well be the case in an economy where technology leaders increasingly capture most market shares due to “winner-takes-all” dynamics (OECD, 2015c).

Globalisation has increased the importance of cross-border collaboration in innovation, but SMEs find it difficult to identify and connect to appropriate knowledge partners and networks at the local, national and global levels (OECD, 2013).

Finally, government innovation policy may not be suited to the way SMEs innovate. For example, R&D tax credits, one of the most common forms of innovation policy, often unintentionally favour large firms because R&D activity is highly concentrated in a few, mostly large, firms, and because of their administrative complexity. Some OECD countries have put in place special provisions to spur SMEs to use R&D tax credits, such as enhanced investment tax credit rates (e.g. Australia, Canada, Japan, Korea, Norway, Poland and United Kingdom). Other innovation policies, such as pre-commercialisation public procurement, may not take account of the collaborative approach to innovation that is typical of SMEs.

What are key areas for policy to consider?

Governments can foster innovation in established SMEs, in co-operation with the other main stakeholders of the national innovation ecosystem, by providing a business environment that is conducive to growth; and supporting the development of strategic assets and resources at the firm level (skills, ICT, access to finance, etc.).

- **Upgrading workforce skills in SMEs.** Improving workforce skills supports both the generation of new in-house innovation and the absorption of new knowledge sourced through collaborations with external partners.
- **Helping SMEs adopt ICT and adapt to the digital revolution.** It is important not only to support SMEs in adopting and effectively using ICT hardware and software which can professionalise business management, but also open up SMEs to the new opportunities of the ongoing digital revolution (e.g. cloud computing, data analytics, etc.).
- **Ensuring that R&D policy is inclusive of SMEs.** R&D grants are typically more likely than tax credits to reach SMEs, as they can directly be targeted at small enterprises or at activities in which small enterprises are more likely to be involved (e.g. collaborative innovation). Governments can also design existing R&D tax

credit programmes so that they better serve the needs of SMEs, including through enhanced investment tax credit rates for SMEs and simpler operational rules.

- **Fostering IP use among SMEs.** It is also important to encourage the use of IP by SMEs by raising awareness about the different types of IPRs, increasing IPR-related skills in SMEs through education and training, and making the overall IP system friendlier to SMEs by streamlining procedures, adequately structuring fees and costs, and improving litigation and enforcement mechanisms (OECD, 2011).
- **Developing an effective and inclusive national innovation system.** National governments have an important role to play in building national innovation systems that are effective in knowledge commercialisation and inclusive of SMEs of different sizes and from different sectors. This primarily involves strengthening collaborations and knowledge flows among the main players of the innovation system (e.g. enterprises, business service providers, universities, government organisations, financiers) through policies such as technology extension services, industry-university collaborative research, business accelerators, and business clusters (OECD, 2010a).

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9. Strengthening social inclusion through inclusive entrepreneurship

Summary

- Some social groups are under-represented or disadvantaged in entrepreneurship, for example women, youth, older people, migrants and the unemployed. Increasing entrepreneurship among these groups, as well as improving the quality of their business start-ups, represents an opportunity to increase participation in the labour market and boost economic growth.
- While these social groups are heterogeneous, their members typically face greater barriers to business creation than the mainstream population. Challenges include a lack of entrepreneurship skills, difficulty in accessing finance for business start-up, difficulties navigating the regulatory framework, a fear of failure and a lack of confidence.
- Inclusive entrepreneurship policies seek to give everyone an opportunity to be successful in business creation and self-employment, regardless of their background or personal characteristics.
- Governments can do more to support entrepreneurship for disadvantaged groups with a range of tailored instruments that improve access to finance, strengthen entrepreneurship skills, and help build entrepreneurial networks. Key success factors include effective outreach to the target populations, as well as ensuring that the support provided addresses the unique challenges faced.

Why is it important?

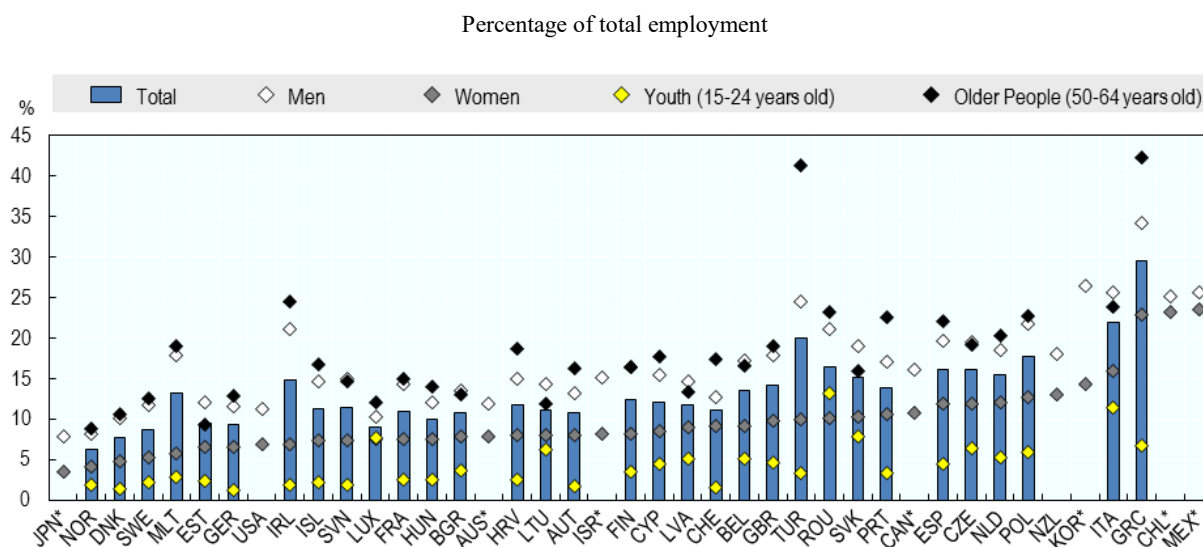
Inclusive entrepreneurship is an important vehicle for achieving inclusive growth. Business creation by under-represented and disadvantaged groups helps create jobs and fight social and financial exclusion, while stimulating economic growth across the economy. However, while entrepreneurship plays an important role in stimulating innovation and driving job creation, only a relatively small part of the population is involved in starting a business, and not all people have the same opportunities to create and run a business. The objective of inclusive entrepreneurship policies is to ensure that all people have an opportunity to start up and operate in business or self-employment, regardless of their personal characteristics and background.

Supporting the creation of sustainable businesses by members of target group populations is expected to increase labour market participation and attachment, thus providing individuals with an opportunity to earn income and improve their standard of living. Furthermore, entrepreneurship offers an opportunity for individuals to be more active members of society, increasing their self-confidence and building their local community. Lastly, the employability of individuals within the target populations is also expected to improve. While not everybody who receives entrepreneurship training or support will start a business, individuals participating in entrepreneurship training programmes, interacting with a coach or mentor, or receiving assistance in developing a business plan, will acquire skills and experience that make them more employable.

These outcomes can benefit economies, as unemployed and inactive people move into work, either through self-employment or wage employment. This can also lead to more business start-ups that have the potential to create jobs for others, and improve growth prospects by utilising under- or unutilised human capital.

What are current trends and challenges?

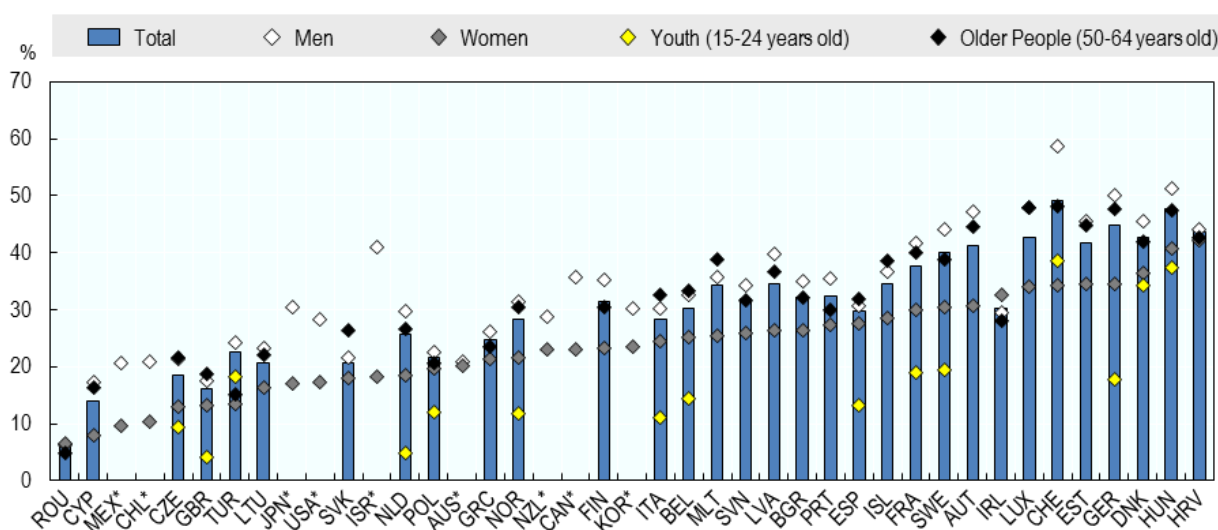
Youth and women are less likely to be self-employed than the mainstream population. In 2016, men were nearly twice as likely as women to be self-employed across OECD countries, although there are some countries such as Mexico and Chile, where the gender gap in the self-employment rate is very small (Figure 9.1). Youth are also under-represented in self-employment. Fewer than 5% of working youth (15-24 years old) were self-employed in nearly all OECD countries in 2016, which was approximately one-third of the proportion of the adult population. Moreover, few unemployed people return to work through self-employment. In most countries, approximately 2% of unemployed people report that they intend to return to work by becoming self-employed. However, nearly 3% return to work by starting a business, suggesting that many cannot find any other employment opportunity. Other social target groups such as seniors and migrants are not under-represented in self-employment, but often face more and greater barriers to entrepreneurship (and in the labour market more generally).

Figure 9.1. Self-employment rate, 2016

Note: *denotes data from 2015.

Source: Eurostat (2017), Labour Force Survey, available at: <http://ec.europa.eu/eurostat/web/lfs/data/database>; OECD (2016), "Indicators of gender equality in entrepreneurship", OECD Gender Portal, available at: www.oecd.org/gender/data/.

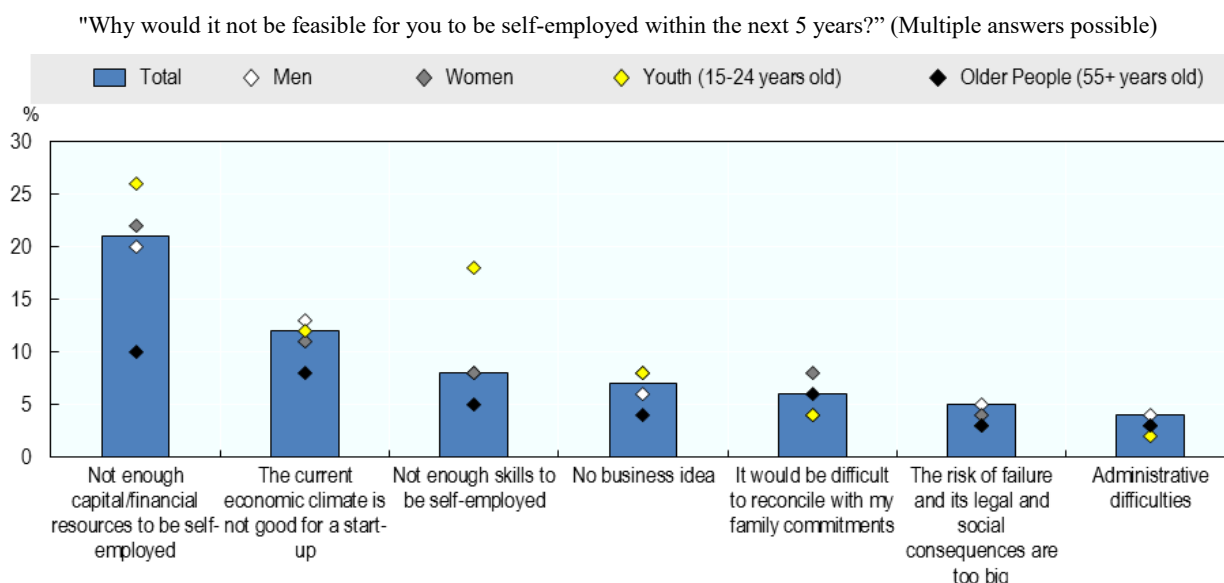
Furthermore, businesses started by people from these social target groups appear to be smaller. Self-employed women and youth were less likely than the average to have employees in nearly all countries in 2016 (Figure 9.2). Approximately 30% of self-employed men in OECD countries had employees, while only about 20% of self-employed women did. Self-employed youth were even less likely to have employees – fewer than 10% did in 2016. The picture is mixed for the self-employed over 50 years old, who were less likely to have employees than the average in approximately half of OECD countries.

Figure 9.2. Proportion of self-employed with employees, 2016

Note: * denotes data from 2015

Entrepreneurs from under-represented and disadvantaged groups are more likely to report barriers to business creation than the general population. One of the most frequently cited barriers to business creation is access to finance, which was cited by 26% of youth and 22% of women in 2012 (Figure 9.3). Youth were also twice as likely as adults to cite a lack of entrepreneurship skills as a barrier. Older people appear to face different barriers, since they tend to have more experience in the labour market, and are more likely to have relevant professional networks and savings that can be used for business creation. Significant barriers to entrepreneurship for senior entrepreneurs include a lack of awareness, age discrimination, declining health, financial disincentives, as well as the opportunity cost of time (i.e. they may prefer leisure activities over the value future income, since the timeframe for reaping the benefits may be relatively short). The barriers typically faced by the unemployed include a lack of finance and skills, but also small or outdated professional networks and high opportunity costs since the income earned in self-employment may be less than the unemployment benefits received. Immigrants face different barriers, including a lack of knowledge about the regulatory and institutional environment, low levels of social capital and language skills.

Figure 9.3. Barriers to business creation in the European Union, 2012



Source: European Commission (2012), "Entrepreneurship in the EU and Beyond", Flash Eurobarometer, No. 354.

What are key areas for policy to consider?

Policy makers can do more to support inclusive entrepreneurship by addressing market, institutional and behavioural failures, that tend to fall heavily on disadvantaged and under-represented groups such as the unemployed, youth, women and migrants. This includes building a culture that is supportive of entrepreneurship in diverse social groups; increasing awareness about the opportunities, benefits and practices of entrepreneurship; as well as increasing motivations to pursue these activities. Moreover, inclusive entrepreneurship policies should not only seek to increase the number of start-ups among under-represented and disadvantaged groups, but also seek to improve the quality of these start-ups so that they have a greater chance of becoming sustainable. In this respect, it is also important that the businesses created be sustainable and minimise the displacement of other activity.

Therefore, inclusive entrepreneurship policies and programmes need to be designed to encourage creativity and innovation, and be targeted at those entrepreneurs with distinctive business ideas with the potential to become sustainable businesses.

Key policy approaches used to promote and support inclusive entrepreneurship include entrepreneurship training, coaching and mentoring, facilitating access to finance and building entrepreneurial networks. To be effective, support measures need to be tailored to the unique challenges faced by the different social target groups, and targeted outreach efforts are needed to reach potential entrepreneurs. For example, Going for Growth in Ireland provides coaching and mentoring to growth-oriented women entrepreneurs, as well as helping them build their networks. It is also important for policy makers to consider bundling support measures into packages, since many of the barriers and challenges are inter-related, and to utilise appropriate delivery mechanisms. This approach is taken by the BBZ programme in the Netherlands, which provides entrepreneurship training, coaching and mentoring, and an allowance to support people receiving social welfare assistance in business creation. Support measures are often more effective when specialist agencies or specialist branches of mainstream agencies are used, but client density must be sufficiently high to achieve cost efficiency. Key actions policy makers may consider include:

- **Deepening the understanding of the challenges that different social target groups face in entrepreneurship**, and of the effectiveness of different policy approaches used to address these challenges. This calls for improving data collection and efforts to assess the impact of inclusive entrepreneurship policies and programmes.
- **Addressing barriers in the process of acquiring entrepreneurship skills** by offering entrepreneurship training courses that exploit the potential of online technologies, and provide complementary support such as finance, coaching and mentoring.
- **Improving access to finance** in conditions of high risk and little collateral by providing financial information and advice to entrepreneurs, supporting the matching of investors and entrepreneurs, offering loan guarantees, and participating in the emergence of microfinance institutions and crowd funding platforms focused on disadvantaged and under-represented groups.
- **Providing flexibility in how social security entitlements are paid**, allowing for lump sum payments to support business creation and providing allowances or continuing to pay unemployment benefits for a fixed period of time to people who start up from unemployment.
- **Offering business development support** to upgrade the quality of businesses started by people from under-represented and disadvantaged groups, including by encouraging business projects in markets where there is excess or growing demand and by developing business management expertise.
- **Building the entrepreneurial networks** of growth-oriented entrepreneurs from outside the mainstream population to help fill gaps in their access to entrepreneurship skills and finance.

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10. Monitoring and evaluation of SME and entrepreneurship programmes

Summary

- Monitoring and evaluation is needed to assess the economic efficiency of SME and entrepreneurship policy actions. They should also inform the design and mix of SME and entrepreneurship policies by identifying those features which lead to desirable outcomes. Evaluation is fundamental to public accountability.
- Reliable methods for the evaluation of SME and entrepreneurship policies using appropriate counterfactuals have been established and demonstrated. However, such methods, which can address the heterogeneous impacts of policies on different types of SMEs, are not widely used.
- Key challenges include increasing the application of rigorous evaluation techniques; better specifying policy objectives, targets and indicators; making better use of data, including existing national administrative data sets for purposes such as tax and social security; and seizing the potential of Big Data.
- It is important to make better use of evaluation in the policy cycle; evaluate systematically across the portfolio of SME and entrepreneurship interventions; and assess the impacts on SMEs and entrepreneurship of policies in areas where business development is not the primary objective.

Why is it important?

A core justification for SME and entrepreneurship policy is the presence of coordination failures and information asymmetries, which may limit SMEs' ability to contribute to economic and industrial development, innovation, job creation and social cohesion. SME and entrepreneurship support can come in various forms, including advice, training, and enhanced access to finance and can help both, the individual SME owner as well as the rest of society through positive spill-over benefits in terms of job and wealth creation, as well as economic growth.

There is consequently substantial direct public expenditure on SME and entrepreneurship programmes and many other policy measures, which target SMEs, have important indirect public finance implications through foregone tax revenue. It is the responsibility of policy makers to use monitoring and evaluation¹ to provide accountability, and to ensure that expenditure is in line with programme objectives and has the intended effects. Monitoring and evaluation is also needed to refine and redirect programme interventions, hence improving performance and "value for money". Applied systematically across different types of policy interventions, it can help to ensure that policy, in aggregate, is coherent and that the policy mix is appropriate.

What are current trends and challenges?

There have been a number of recent advances in policy evaluation techniques, many of which are likely to be particularly valuable in the evaluation of SME and entrepreneurship programmes and policies. There have also been some important advances in data collection for SME and entrepreneurship policy development. SME and entrepreneurship programme monitoring is now widely established internationally, and monitoring frameworks for SME and entrepreneurship strategies are largely in place. For example, through the yearly SME Performance Review, the European Commission monitors and assesses countries' progress in implementing the European [Small Business Act](#) (SBA). SBA country fact sheets focus on key performance indicators and national policy developments related to the SBA's 10 policy dimensions (European Commission, 2017). Estonia has developed an SME policy monitoring and evaluation system for its SME strategy 2014-2020, which includes a full quantitative evaluation every two years with the support of foreign experts under the responsibility of the Ministry of Economic Affairs and Communication. However, progress has been less significant in governments' use of these advances to make the most rigorous assessments of policy effectiveness, and to use the results for continuous policy improvement. In short, the creation of an evaluation culture has yet to be widely established and significant challenges remain.

SME and entrepreneurship policies are frequently implemented without clear objectives. The objectives of the intervention are best framed in terms of the market or institutional failure the intervention seeks to address or the social benefit sought. Targets or key performance indicators can then be established against which the outcomes (intended and unintended) of the policy action can be monitored. In particular, more attention is needed to better understand the mechanisms through which policy will lead to benefits and to consider the potential unintended consequences that the policy may have (positive or negative). Appropriate data need to be collected and analysed, reflecting this understanding of potential consequences.

There is also room to improve the data collection systems and national statistical information available for SME and entrepreneurship policy monitoring and evaluation.

Data should be available at appropriate time intervals and levels of disaggregation, and refer to an outcome indicator that is relevant for the foreseeable future. In some cases dedicated data collection exercises may be required, but in most cases the evaluator can rely upon existing data sources.

Rich and relevant data often exist within different parts of the administration, but remain unexploited for SME and entrepreneurship policy evaluation, e.g. in tax records or the unemployment registry (OECD, 2017b). Other sources of data outside public administration can be helpful. For example, in the SME space, the use of bank client data for evaluation is another promising area, e.g. as exploited in Coad et al (2013).

Legal barriers, a lack of incentives to make the data available or a lack of incentives to utilise the data for assessments can prevent their use. To address this challenge, some OECD countries have made major steps in recent years to broaden access to confidential data and to link data from different sources, such as Denmark, Norway and Sweden. France is making administrative data available through remote access to authorised researchers (see also OECD, 2017).

Looking ahead, “big data” collected with digital technologies holds promise for improving evaluation. Recently-developed methodological tools to analyse big data could become an important resource in the area of SME and entrepreneurship policies.

A further challenge is to ensure that account is taken of the interactions between the outcomes of different SME and entrepreneurship policies and programmes. Only in this way can informed judgements be made about potential adjustments to the policy mix; i.e. identifying programmes that merit expansion and programmes that merit contraction or abrogation. However, SME and entrepreneurship programmes are highly diverse. Some are expected to have an impact in the very short term (e.g. export facilitation), while others are unlikely to have an observable impact in less than a decade (e.g. innovation).

The impacts on SMEs and entrepreneurship of policies targeted at other areas need to be evaluated, too. Ministries of economy and industry commonly have the formal responsibility for leading and co-ordinating SME and entrepreneurship policies across government. However, expenditures in other ministries such as those responsible for finance, education, employment and infrastructure, strongly influence entrepreneurship and SME activity. These include policies in the areas of taxation, social security, business regulation, immigration, competition etc.

The impact of their policies on SME and entrepreneurship activity needs to be assessed, for example through using monitoring and evaluation evidence to support Regulatory Impact Assessments and the SME Test, and by creating cross-cutting groups within government to undertake evaluation and reflect on evidence from evaluations on the impact of these policies on entrepreneurship and SME development.

There has been an increase in the use of the most reliable and rigorous evaluation techniques, including for SME and entrepreneurship policy. New econometric techniques can correct for selection bias which can plague the evaluation of many of the types of support measures, e.g. through propensity score matching². There has also been increased use of Randomised Control Trials (RCT), whereby a group of eligible recipients and their performance is compared over time with those eligible recipients who were randomly excluded in order to establish a counterfactual. A number of recent exemplar RCT evaluations have been undertaken in the area of SME and entrepreneurship policy, for example on management and workforce training in SMEs in the United Kingdom (Georgiadis and Pitelis, 2016); the subsidised entry of the unemployed into new business

creation in Germany (Caliendo, M., Künn, S., & Weißenberger, M. 2016); and entrepreneurship training in the United States (Fairlie et al, 2015), etc.

However, high-quality evaluations remain relatively rare in the field of SME and entrepreneurship policy. For example, the US Government Accountability Office report for 2012 reviewed 53 entrepreneurship programmes across four different agencies with a budget of USD 2.6 billion. It reported that for 39 of the 53 programmes, the four agencies had either never conducted a performance evaluation or had conducted only one in the past decade (GAO, 2012). In addition, the UK National Audit Office concluded that none of the UK government evaluations in the field of business support provided convincing evidence of policy impacts (NAO, 2006).

Effective monitoring and evaluation requires a commitment to evaluation as an integral part of the policy-making process. Often evaluations are undertaken as individual exercises and not embedded in the policy cycle. A monitoring and evaluation culture should permeate all stages of policy design, implementation, and reform. This could be built for example through targeted training and partnership with independent evaluation agencies and academic institutions. The use of monitoring and evaluation evidence also requires space for policy experimentation and acceptance of failure.

What are the key areas for policy to consider?

The methodologies and data available for SME and entrepreneurship policy evaluation have improved dramatically over the last decade. However, widespread and systematic evaluation continues to be lacking. There are several examples of best practice evaluation, but little evidence of a comprehensive evaluation culture in this policy space. The OECD Framework for the Evaluation of SME and Entrepreneurship Policies and Programmes has established a six-step approach to monitoring and evaluation, where Step I (analysis of take-up) is the simplest methodology and step VI (methods which take into account selection bias) is the most complex methodology (Table 10.1) (OECD, 2007).

Table 10.1. Six Steps: Methods for assessing the impact of SME policy

Monitoring	
STEP I	Take up of schemes
STEP II	Recipients Opinions
STEP III	Recipients' views of the difference made by the Assistance
Impact Assessment and Evaluation (note that these are not necessarily sequential)	
STEP IV	Comparison of the Performance of 'Assisted' with 'Typical' firms
STEP V	Comparison with 'Match' firms
STEP VI	Taking account of selection bias

Source: Based on OECD, 2007, OECD Framework for the Evaluation of SME and Entrepreneurship Policies and Programmes.

In addition, the following elements are important:³

- **Clear policy objectives:** in practice many policies have only vague objectives, which makes evaluation difficult, particularly in cases where there are multiple objectives.
- **A complete overview of the full policy mix:** it is important to have a clear understanding of the policy levers implemented and the potential interactions of the

potential outcomes of different policies, as some instruments may be complementary on the one hand or reciprocally offsetting on the other hand.

- **Good data:** poor data quality is sometimes the main reason why studies fail to find any statistically significant effect of evaluated policies. More and better measures can not only widen the scope of the evaluation, but also improve its precision.
- **Widening the focus beyond outcome:** There are several other variables for policy makers to consider that could play an important role in explaining its effectiveness. These include the eligibility criteria, the targeted sample, the spatial unit of reference (e.g., regions or municipalities), how agents are informed about the policy, etc.
- **A commitment to evaluation as an integral part of the policy-making process:** A monitoring and evaluation culture should permeate all stages of policy design, implementation, and reform.

The OECD Framework for the Evaluation of SME and Entrepreneurship Programmes and Policies (OECD, 2007) provides a guiding tool for monitoring and evaluation of SME and entrepreneurship policies and programmes.

Notes

¹ It is important to distinguish between monitoring and evaluation. Monitoring programmes involves the direct collection of data from policy-makers and/or the recipients of the policy to give a qualitative view of the programme outcomes. It may also involve the collection of data from third-party sources, including business registries and administrative data. In contrast, evaluation is based on linking such outcomes with the specific characteristics of the policy or programme, taking into account the role of other factors which may influence monitored outcomes.

² Examples can be found across the fields of pre-start business advice (Pons Rotger et al, 2012), business assistance programmes (Yusuf, 2012), high-growth firm support (Autio and Ranniko, 2015), subsidised entry of the unemployed into new business creation (Caliendo and Kritikos, 2010; Caliendo, Künn and Weissenberger, 2016), business coaching (Loersch, 2014), etc. Machine Learning techniques can also be useful to predict what policy interventions may be needed, for example in assessing which SMEs suffer credit constraints.

³ See OECD (2017) for a discussion in the context of regional policy evaluation.

Further Reading

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Annex A. Conference Programme

Related events preceding the OECD Ministerial Conference on “Strengthening SMEs and Entrepreneurship for Productivity and Inclusive Growth”

OECD-inadem workshop on building business linkages that boost sme productivity

The workshop “Building business linkages that boost SME productivity” is the third of a series of workshops on the topic of SME productivity organised by the OECD in collaboration with Mexico’s National Institute of the Entrepreneur (INADEM). The first workshop in the series looked into the importance of upgrading managerial skills and management practices to enhance SME productivity (Puerto Vallarta, Mexico, 3-4 November 2016), while the second dealt with the link between workforce skills and SME productivity (Puerto Vallarta, Mexico, 15-16 May 2017). This third workshop will focus on business linkages and how strengthening SME supply chain linkages and other types of inter-firm collaboration can boost SME productivity.

Women entrepreneurs: seizing the benefits of digitalisation and globalisation

This event will be an interactive workshop that includes an expert panel discussion and a policy hack. An international expert panel will explore the challenges faced by women entrepreneurs through a moderated discussion, with time allotted for questions and discussion with the audience. Key issues to be covered include digitalisation, access to finance and internationalisation. The policy hack will bring together participants in small groups to identify a tangible solution to specific policy challenges. Each group will identify one person who will “pitch” their solution to expert judges and other participants in 3 minutes. The expert judges will then select the top 3 ideas.

For more information on these events, please visit: oe.cd/2df

Agenda at a glance

Wednesday, 21 February				
19:00	Welcome reception at the Soumaya Museum			
Thursday, 22 February 2018				
07:30-9:00	Registration			
9:00-11:30	Side event with SME stakeholders and Ministers (or their representatives)			
11:30-12:30	Opening Ceremony and Introductory Remarks			
	- Mr Angel Gurría, Secretary General, OECD - Mr Ildefonso Guajardo Villarreal, Minister of Economy, Mexico			
12:30-14:00	Lunch			
14:00-15:30	Plenary 1: Enabling SMEs to scale up			
15:30-16:00	Family Photo Ministers and Heads of Delegations		Coffee break	
16:00-17:30 Parallel Sessions	Improving the business environment for SMEs through effective regulation	Business transfer as an engine for SME growth	Developing entrepreneurial competencies	
19:00	Gala Dinner			
Friday, 23 February 2018				
9:00-10:30	Plenary 2: Enhancing SME access to diversified financing instruments			
10:30-11:00	Coffee break			
11:00-12:30 Parallel Sessions	Promoting innovation in established SMEs	Strengthening social inclusion through inclusive entrepreneurship	Monitoring and evaluation of SME and entrepreneurship programmes	
12:30-14:00	Lunch			
14:00-15:30	Plenary 3: Fostering greater SME participation in a globally integrated economy			
15:30-16:30	Statements by Vice Chairs			
	- Ms. Marie-Gabrielle Ineichen-Fleisch, State Secretary at the Federal Department of Economic Affairs, Education and Research (EAER), Switzerland - H.E. Dr. Faruk Özlü, Minister of Science, Industry and Technology, Turkey - Hon Stuart Nash, Minister for Small Business, New Zealand			
	Statement by OECD			
	Mr. Angel Gurría, Secretary General, OECD			
16:30-17:00	Statement by Mexico and presentation of the Ministerial outcome document			
	Mr. Ildefonso Guajardo Villarreal, Minister of Economy, Mexico			
16:30-17:00	Press Conference to present the Ministerial outcome document			

Day 1: Thursday, 22 February 2018

Pre-Ministerial Event	
9.00-11:30	Side event with SME stakeholders and Ministers (or their representatives) Master of Ceremony: Mr. Roberto Martinez <i>Head of the OECD Mexico Centre</i> The event will consist of two separate panel sessions of one hour each, bringing together representatives from government and the private sector to address the following topics: Session 1: The importance of SMEs for globalisation, growth and inclusiveness Moderator: Ms. Lamia Kamal-Chaoui <i>Director, OECD Centre for Entrepreneurship, SMEs, Regions and Cities</i> Panellists will discuss the opportunities international trade creates to accelerate innovation, facilitate spill overs of technology and managerial know-how, broaden and deepen skillsets, and enhance the productivity of SMEs. To date, participation in global markets and value chains remains uneven across the SME population, with only a few “born global” firms and highly innovative SMEs that are fully integrated into global markets. Additional challenges arise from the fact that SMEs are less able to face the costs of engaging in international trade, due to their limited resources and management capacities. Panellists • Mr. Kris Peeters, Deputy Prime Minister and Minister of Employment, Economy and Consumer Affairs, Belgium • Ms. Geannina Dinarte, Minister of Economy, Industry and Commerce, Costa Rica • Ms. Cathy Feingold, Director of the AFL-CIO, representing The Trade Union Advisory Committee (TUAC) to the OECD • Mr. Alban Maggiar, Vice President, European Association of Craft, Small and Medium-sized Enterprises (UEAPME) Session 2: The future of SMEs in the digital economy Moderator: Mr. Andrew W. Wyckoff <i>Director, OECD Directorate for Science, Technology and Innovation</i> Panellists will discuss the opportunities and challenges of the digital economy for SMEs. Digitalisation can offer greater access to markets, talent and finance, the ability to better communicate and collaborate, as well as help reduce red tape. At the same time, there is a significant difference between large and small firms in how they take advantage of the ongoing digital transformation. SMEs face several barriers to adopting digital technologies in their operational activities. In particular, they often lack resources to acquire the necessary complementary knowledge-based assets, such as organisational and human capital, including the upskilling of workers. Panellists • Mr. Pat Breen, Minister of State for Trade, Employment, Business, EU Digital Single Market and Data Protection, Ireland • Mr. Mariano Mayer, Secretary of Entrepreneurs and SMEs, Ministry of Production, Argentina • Ms. Jackie King, COO of the Canadian Chamber of Commerce • Ms. Victoria Grand, Director of Policy Programs, Facebook

Ministerial Conference	
11:30-12:30	Opening Ceremony Master of Ceremony: Mr. Roberto Martínez <i>Head of the OECD Mexico Centre</i> Opening remarks • Mr. Angel Gurría, Secretary-General, OECD • Mr. Ildefonso Guajardo Villarreal, Minister of Economy, Mexico (Chair of the Ministerial Conference) Report back from the session with stakeholders and Ministers • Mr. Kris Peeters, Deputy Prime Minister and Minister of Employment, Economy and Consumer Affairs, Belgium (for Session 1) • Mr. Mariano Mayer, Secretary of Entrepreneurs and SMEs, Ministry of Production, Argentina (for Session 2)
12:30-14:00	<i>Lunch</i>
14:00-15:30	Plenary 1: Enabling SMEs to scale up Chair: Ms. Marie-Gabrielle Ineichen-Fleisch <i>State Secretary, Federal Department of Economic Affairs, Education and Research (EAER), Switzerland</i> SMEs can experience sustained growth at different stages of their life cycle and across many sectors. Start-ups that scale up are a key source of innovation and account for a disproportionate share of job creation. Medium-sized enterprises that grow are a driving force of competitiveness in many countries. Growth-oriented small firms can achieve scale through different mechanisms, including strategic and inter-firm linkages. Digitalisation and participation in global markets and value chains are powerful engines to scale up, enabling new modes of growth. Questions for discussion • <i>What policy approaches have proven effective in stimulating the scaling up of start-ups and SMEs? Which barriers to SME growth call for further attention?</i> • <i>How can digital technologies be harnessed to enable SMEs to scale up? How can policy address the barriers to adoption and use by SMEs of digital technologies?</i> • <i>How can policy take into account different growth aspirations by entrepreneurs and help them manage the challenges of high growth?</i> Lead speakers: • Mr. Peter Kažimír, Minister of Finance, Slovak Republic • Mr. Pat Breen, Minister of State for Trade, Employment, Business, EU Digital Single Market and Data Protection, Ireland • Mr. Sugyu Choi, Vice Minister of SMEs and Start-ups, Korea • Dr. Armgard Wippler, Deputy Director-General for SME Policy, Ministry for Economic Affairs and Energy, Germany
15:30-16:00	<i>Coffee break Family Photo with Ministers and Heads of Delegations</i>

16:00-17:30

Parallel Sessions

Improving the business environment for SMEs through effective regulation**Chair: Mr. Álvaro Santos Pereira***Acting Chief Economist of the OECD*

Regulatory conditions are among the most important factors affecting SMEs and entrepreneurship. SMEs usually face bigger challenges than large firms in screening the regulatory environment and dealing with norms. In recent years, important progress has been made to reduce the administrative burdens on start-ups, lower legal barriers to entry and reduce the costs of regulatory compliance in different areas. However, the complexity of regulatory procedures, covering areas such as license and permit systems, insolvency and tax, among others, remains a major obstacle to entrepreneurial activity.

Questions for discussion

- *Have government efforts to develop a business environment that offers a level playing field for SME and entrepreneurship development been effective? How can remaining obstacles be overcome?*
- *When developing regulatory policies, how should governments take into account characteristics of SMEs such as size, age or sector?*
- *How can governments achieve regulatory simplification for SMEs, while preserving the incentives for these businesses to grow? Have regulatory simplification efforts been effective in boosting investments by SMEs?*

Lead speakers:

- **Mr. Kris Peeters**, Deputy Prime Minister and Minister of Employment, Economy and Consumer Affairs, Belgium
- **Mr. Timur Suleimenov**, Minister of National Economy, Kazakhstan
- **Mr. Mariano Mayer**, Secretary of Entrepreneurs and SMEs, Ministry of Production, Argentina
- **Mr. Viljar Lubi**, Deputy Secretary General for Economic Development, Ministry of Economy, Estonia

Business transfer as an engine for SME growth**Chair: Mr. Greg Medcraft***Director, OECD Directorate for Financial and Enterprise Affairs*

Many economically sound SMEs exit the market as a result of problematic business transfers, with negative effects for the growth and innovative potential of economies. In the coming years, with the ageing of entrepreneurs, the volume of business transfers is expected increase in many OECD countries. Successful business transfer of viable SMEs at different stages of their life cycle is crucial to retain employment, preserve the value of assets and ensure continuity in production processes and business relations. Furthermore, business transfer can represent an opportunity to rethink a firm's strategic vision and business model and to innovate and seize new opportunities. It can also enable new entrepreneurs to enter the market.

Questions for discussion

- *What can governments do to create conducive framework conditions for business transfer?*
- *Which targeted measures may be most effective to address the transfer challenges of small businesses?*
- *What are the main knowledge gaps with regard to business transfer conditions and trends?*

	Lead speakers: • Mr. Daisaku Hiraki, Parliamentary Vice-Minister of Economy, Trade and Industry, Japan • Ms. Kristin Schreiber, Director for SME Policy and the COSME Programme, European Commission • Mr. Sanu de Lima, Deputy Director for Corporate Governance Reform, Department for Business, Energy and Industrial Strategy (BEIS), United Kingdom Developing entrepreneurial competencies Chair: Ms. Mari Kiviniemi <i>Deputy Secretary-General, OECD</i> Entrepreneurship competencies combine creativity, a sense of initiative, problem-solving, the ability to marshal resources, and financial and technological knowledge. They can be developed through entrepreneurship education and training that focus on promoting an entrepreneurial mindset and behaviours. Schools and vocational and higher education institutions are increasingly developing these competencies in students by enriching their study programmes with dedicated entrepreneurship education courses, either as self-standing modules or embedded into curricula. Problem-based teaching and assessment methods have proven particularly successful. Questions for discussion • <i>How can government approaches to promoting entrepreneurship competencies be enhanced? How can collaboration be achieved across relevant government ministries?</i> • <i>What are current trends and gaps in developing entrepreneurship competencies from early levels of education to university? How can links between entrepreneurship education and start-up support be strengthened?</i> • <i>How can the impact of entrepreneurship education and different entrepreneurship education approaches on business start-up and SME innovation performance be assessed? How can entrepreneurial culture and entrepreneurship attitudes be measured?</i> Lead speakers: • Mr. Youcef Yousfi, Minister of Industry and Mining, Algeria • Ms. Eva Štravs Podlogar, State Secretary at the Ministry of Economic Development and Technology, Slovenia • Mr. Daniel Arango, Vice Minister of Business Development, Ministry of Trade, Industry and Tourism, Colombia • Mr. Peter Cully, Senior official, Department of Jobs and Small Business, Australia
19:00	Gala Dinner (Location: Museo Casa de la Bola)

Day 2: Friday, 23 February 2018

09:00-10:30	Plenary 2: Enhancing SME access to diversified financing instruments <i>* The session will start with a reporting back from the parallel sessions on the afternoon of Day 1 by the Chairs (10 minutes).</i> Chair: H.E. Mr. Faruk Özlü <i>Minister of Science, Industry and Technology, Turkey (Vice Chair of the Ministerial Conference)</i> Across all stages of their life cycle, SMEs require access to appropriate financing sources. While bank lending continues to be the main external source of finance for SMEs, it may be ill-suited to certain segments of the business population, such as new, innovative and fast-growing firms. At the same time, the uptake of alternative financing instruments remains uneven, pointing to persistent market failures and longstanding challenges on both the demand and supply sides. There is a need to broaden the range of financing instruments available to SMEs and entrepreneurs, in line with the G20/OECD High Level Principles on SME Financing. Questions for discussion • <i>Are recent policy approaches to address SME financing challenges on the supply and demand sides meeting their objectives? What elements call for further attention?</i> • <i>Which policy measures have proven most successful to stimulate the uptake of alternative financing instruments by small businesses? What role should policy play in channelling a broader range of financial resources, including private savings, towards SMEs?</i> • <i>How can policy help maximise the potential of the digital transformation to strengthen SME access to finance and financial inclusion?</i> Lead speakers: • Ms. Lienneke Maria Schol Calle, Minister of Production, Peru • Mr. Daisaku Hiraki, Parliamentary Vice-Minister of Economy, Trade and Industry, Japan • Mr. Stefano Firpo, Director General for Industrial Policy, Competition and SMEs and SME Envoy, Ministry of Economic Development, Italy
10:30-11:00	Coffee break

11:00-12:30 <i>Parallel Sessions</i>	Promoting innovation in established SMEs Chair: Mr. Mario Pezzini <i>Director, OECD Development Centre</i> Supporting innovation in established SMEs can foster inclusive growth by reducing productivity gaps and wage gaps between SMEs and large companies. SMEs are, on average, less innovative than large enterprises. However, some small enterprises are highly innovative and can reach productivity levels above those of large companies. Companies which develop and use their internal strategic resources effectively (e.g. managerial and workforce skills, ICT, R&D, etc.), and collaborate with external partners in the innovation system, have better innovation performance. Questions for discussion ● <i>What are the key policy mechanisms that have proven successful to encourage innovation in SMEs? What new approaches are needed?</i> ● <i>How can such policies be addressed to SMEs with differences in terms of industry, size, age, and growth performance?</i> ● <i>How can policy help SMEs to harness the most recent advances in digital technologies?</i> Lead speakers: ● Mr. Zhang Feng, Chief Engineer, Ministry of Industry and Information Technology, People's Republic of China ● Mr. Balázs Rákossy, State Secretary for EU Funds, Ministry for National Economy, Hungary ● Ms. Ana Lehmann, Secretary of State for Industry, Ministry of Economy, Portugal ● Mr. Raimonds Aleksejenko, Deputy State Secretary, Ministry of Economics, Latvia
	Strengthening social inclusion through inclusive entrepreneurship Chair: Ms Gabriela Ramos <i>OECD Chief of Staff and Sherpa to the G20</i> Some groups are under-represented or disadvantaged in entrepreneurship, e.g. women, youth, older people, migrants and the unemployed. Increasing entrepreneurship among them, as well as improving the quality of their business start-ups, represents an opportunity to increase participation in the labour market and boost growth. While these social groups are heterogeneous, their members typically face greater barriers to business creation. Challenges include a lack of entrepreneurship skills, difficulty in accessing finance and navigating the regulatory framework, fear of failure and lack of confidence. Questions for discussion ● <i>What are the specific entrepreneurship support needs of people from under-represented and disadvantaged groups in entrepreneurship, and how can policy address these needs?</i> ● <i>How can inclusive entrepreneurship measures leverage digital platforms and tools to reach target clients that are often hard to reach?</i> ● <i>How do programmes balance tailoring support for the unique needs of socially excluded groups against the economies of scale gained through mainstream delivery?</i>

Lead speakers:

- **Ms. Geannina Dinarte**, Minister of Economy, Industry and Commerce, Costa Rica
- **Mr. Paul Thompson**, Associate Deputy Minister, Ministry of Innovation, Science and Economic Development, Canada
- **Ms. Paula Marinela Pirvanescu**, Deputy Minister for Investments, Ministry for Business Environment, Commerce and Entrepreneurship, Romania
- **Ms. Edith Vries**, Director-General, Department of Small Business Development, South Africa

Monitoring and evaluation of SME and entrepreneurship programmes**Chair: Ms. Martine Durand**

Chief Statistician and Director of the OECD Statistics Directorate

Monitoring and evaluation are fundamental to public accountability and for assessing the economic efficiency of SME and entrepreneurship policies. They should also inform the design and mix of SME and entrepreneurship policies by identifying those features, which lead to desirable outcomes. Reliable methods for the evaluation of SME and entrepreneurship policies, using appropriate counterfactuals, have been established and demonstrated. However, such methods, which can address the heterogeneous policy impact on different types of SMEs, are not widely used. Key challenges include increasing the application of rigorous evaluation techniques; better specifying policy objectives, targets and indicators; making better use of data, including existing national administrative data sets; as well as seizing the potential of Big Data.

Questions for discussion

1. *How can a stronger culture of monitoring and evaluation be established for SME and entrepreneurship policy?*
2. *How can governments ensure that evaluation outcomes are reflected in policy design?*
3. *Which new data sources can be exploited for SME and entrepreneurship policy monitoring and evaluation, and what is needed to enable their use?*

Lead speakers:

- **Mr. Mario Buisán**, Deputy Vice-Minister for Industry and SMEs, Ministry of Economy, Industry and Competitiveness, Spain
- **Ms. Dato' Hafsah Hashim**, CEO, SME Corporation Malaysia
- **Mr. José Fernando Ramos de Figueiredo**, Special Honorary Chairman, European Association of Guarantee Institutions (AECM)

12:30-14:00

Lunch

14:00-15:30	Plenary 3: Fostering greater SME participation in a globally integrated economy Chair: Hon Stuart Nash, Minister for Small Business, New Zealand While SMEs tend to be under-represented in international trade, changes in the global environment, such as the rise in global value chains and digitalisation, offer new opportunities for SMEs to participate in global markets and scale up, innovate, broaden and deepen their skill-set, and enhance productivity. These trends increase the importance of whole-of-government approaches to lift longstanding and new barriers that SMEs face in internationalising, including connectivity, access to information, skills, technology and finance. Questions for discussion • <i>What policy approaches have proven successful to strengthen SMEs' participation in international trade? What new approaches are needed?</i> • <i>Which types of firms prove to be most successful in integrating global value chains, and how can policy enable the integration of other SMEs? What aspects of open markets matter most for SME participation in global value chains?</i> • <i>How can policy help SMEs harness the potential of digital technologies for international activity?</i> Lead speakers • Ms. Marie-Gabrielle Ineichen-Fleisch, State Secretary, Federal Department of Economic Affairs, Education and Research (EAER), Switzerland (Vice Chair of the Ministerial Conference) • Mr. José Ricardo Veiga, Secretary of Micro and Small Enterprises, Ministry of Industry, Foreign Trade and Services, Brazil • Mr. Mario Buisán, Deputy Vice-Minister for Industry and SMEs, Ministry of Economy, Industry and Competitiveness, Spain • Mr. Scott Ticknor, Acting Special Representative for Commercial and Business Affairs, Department of State, United States
15:30-16:30	Closing Session Statements by Vice Chairs • Ms. Marie-Gabrielle Ineichen-Fleisch, State Secretary, Federal Department of Economic Affairs, Education and Research (EAER), Switzerland • H.E. Mr Faruk Özlü, Vice-Minister, Science, Industry and Technology, Turkey • Hon Stuart Nash, Minister for Small Business, New Zealand Statement by OECD • Mr. Angel Gurría, Secretary-General, OECD Statement by Mexico and presentation of the Ministerial outcome document • Mr. Ildefonso Guajardo Villarreal, Minister of Economy, Mexico
16:30-17:00	<i>Press Conference to present Ministerial outcome document</i>

Annex B. Declaration on Strengthening SMEs and Entrepreneurs for Productivity and Inclusive Growth

WE, THE MINISTERS AND REPRESENTATIVES of Algeria, Argentina, Australia, Austria, Belgium, Belize, Brazil, Bulgaria, Canada, Chile, Colombia, Costa Rica, the Czech Republic, Denmark, Egypt, El Salvador, Estonia, Finland, France, Germany, Greece, Guatemala, Hungary, Iceland, Ireland, Israel, Italy, Japan, Kazakhstan, Korea, Latvia, Lithuania, Luxembourg, Malaysia, Mexico, the Netherlands, New Zealand, Norway, Panama, Peru, Poland, Portugal, Romania, Singapore, the Slovak Republic, Slovenia, South Africa, Spain, Sweden, Switzerland, Turkey, the United Kingdom, the United States, Uruguay, Viet Nam and the European Union, in the context of the OECD Ministerial Conference to discuss strengthening SMEs and entrepreneurship for productivity and inclusive growth which took place on 22-23 February 2018 in Mexico City, Mexico:

In many countries, governments are seeking opportunities to enhance productivity growth, foster quality job creation, strengthen trade and investment, and reduce inequalities.

We consider the need to deepen our understanding of the underlying causes of current economic challenges, as well as create the conditions that enable the benefits of globalisation, open markets and technological progress to be enhanced and shared more broadly across the economy and society.

Small and medium-sized enterprises (SMEs) are a major component of the world economy, accounting for more than half of formal employment globally and contributing on average between 50% and 60% of national GDP in OECD Member countries.

SMEs and start-ups provide an important stimulus to employment and productivity growth. They can play an important role for meeting specific market needs including in regions and sectors where scale may be limited or of lesser relevance, and can help foster competition in established sectors. SMEs, including those that scale up and innovate, benefit the economy, stimulating markets, making available new and innovative products and services – delivering benefits to consumers and wider society, and contributing to productivity growth and job creation. SMEs are often strongly linked to their local economies, contributing to social cohesion and integrating diverse populations into the economy.

The population of SMEs is very diverse in terms of age, size, business model, performance, and the profile and aspirations of entrepreneurs. These differences, including across sectors, regions and countries, affect their contributions to innovation, productivity, quality job creation and growth. Firm heterogeneity also has important implications for the design of policies across countries and for different types of SMEs..

While not all SMEs aspire to grow, many continue to face challenges related to their size; limited resources (such as skills and finance); or industry and market conditions, including within supply chains and with larger enterprises, which may impact the firm's ability to fulfil its growth potential, scale up, and take advantage of regional and global value chains.

Strengthening SMEs and entrepreneurship, including women- and youth-owned businesses, is important for achieving more inclusive societies and growth; particularly at a time when digitalisation, the next production revolution, demographic trends and, last but not least, in some cases, the circular economy and the transition to a low-carbon economy are changing the opportunities and challenges for firms to start up and grow.

An enabling and evidence-based policy environment and supportive SME infrastructure are needed to offer opportunities for diverse firms and a level playing field for all enterprises. Such conditions are critical to enable SMEs and entrepreneurs to thrive, scale up and contribute to an open, digitalised and inclusive economy. This includes an effective regulatory environment, effective contract enforcement and civil justice systems, and transparency and integrity in the public sector.

The field of SME and entrepreneurship policy is complex. We recognise the usefulness of a coordinated and integrated approach that fosters synergies across different ministries and government agencies and different levels of government, while ensuring consultation with stakeholders, including representatives of the business and financial sectors, trade unions, and education and research institutions.

WE RECALL the outcome of the first OECD Ministerial Conference on SMEs on "Enhancing the Competitiveness of SMEs in the Global Economy: Strategies and Policies", held in Bologna, Italy, in 2000; as well as the outcome of the second OECD Ministerial Conference on SMEs in Istanbul, Turkey in 2004, focusing on the need to enhance SME competitiveness worldwide.

WE NOTE that the "Bologna Charter on SME Policies" provides a frame of reference for the design of SME policies to contribute to economic growth and social development, in OECD Member countries and around the world. We note that the "Istanbul Ministerial Declaration on Fostering the Growth of Innovative and Internationally Competitive SMEs" advanced the agenda to enhance entrepreneurship and SME innovation as drivers of growth in a global economy.

WE WELCOME the third OECD Ministerial Conference on SMEs, convened by the OECD and hosted and chaired by Mexico in Mexico City on 22-23 February 2018, which marks an important moment for sharing good practices across countries and in informing a forward-looking, global policy agenda on SMEs and entrepreneurship.

WE WILL ENDEAVOUR TO PURSUE EFFORTS in the following areas, taking into account SME heterogeneity and relevant policy considerations, as well as our national context and circumstances:

- continuing the development, implementation and evaluation of effective policies for SMEs, which enable SMEs to increase their contributions to sustainable and inclusive growth, with due attention to creating a business environment that promotes competition, integrity in the public sector, quality employment and decent work, healthy firm dynamics and the formalisation of businesses;
- enhancing SME participation in the national and global economy, including through transparent policies and trade facilitative procedures, that enable SMEs to: seize the opportunities offered by regional, national and global value chains and by public procurement; innovate; scale up; broaden and deepen their skill-set; and increase their productivity;

- enabling SMEs to make the most of the digital transition by fostering conditions for SME adoption and diffusion of innovative and digital technologies, investment in complementary knowledge-based assets and digital security;
- creating the right conditions, including through effective and innovative policies or regulation, that enable businesses to start, grow and thrive in established and emerging sectors, including through collaborative practices;
- enabling access to appropriate forms of finance by SMEs and entrepreneurs, including by implementing the G20/OECD High Level Principles on SME Financing, to address diverse financing needs in varying circumstances;
- considering the importance of local and regional ecosystems, networks and clusters for strengthening SME integration in value chains and increasing economic competitiveness, including by fostering greater cooperation among actors in the SME support network, such as incubators, accelerators, small business development centres, export assistance centres, and others as appropriate;
- promoting inclusive growth by enhancing entrepreneurial opportunities for all segments of the population, and better understanding and addressing the unique challenges faced by women and other underrepresented entrepreneurs, such as youth, seniors or certain ethnic groups;
- promoting entrepreneurship education to build the competencies needed for successful start-up and growth of enterprises, and strengthening training and upskilling of entrepreneurs and workers to participate in a digital, creative and knowledge-based economy, while fostering SME dynamism and the right conditions to attract and retain talent;
- continuing multi-stakeholder dialogue on effective policies to support development, growth and competitiveness of SMEs in a global and digitalised economy;
- improving our understanding of the drivers of SME productivity and growth and how policies can ensure that SMEs and entrepreneurship strengthen their contributions to quality job creation and inclusive growth.

WE ENCOURAGE the OECD to consider, without prejudice to its future Programme of Work and Budget, the following areas moving forward:

- supporting a better understanding of the heterogeneity of SMEs and entrepreneurs, including contributions to the economy and society; the drivers of business creation and growth; and the implications for policy across different countries;
- deepening understanding, including through firm-level analysis, of the combined effects of structural reforms on the SME business environment, of the role and impact of targeted SME policies, such as those focusing on business dynamics, SME growth, access to finance, innovation, employment creation, entrepreneurship competencies, management skills and workforce training;
- fostering entrepreneurship that contributes to social inclusion, including by pursuing analysis on entrepreneurship by women and other underrepresented groups;
- analysing key levers for enhancing SME contributions to sustainable and inclusive growth, including policies that help SMEs scale up, innovate, and take advantage of new opportunities such as those presented by the digital economy, regional and global value chains, and the transition to a low-carbon economy; and that takes account of firm heterogeneity and specific national contexts;

- continuing to promote the sharing of best practices and the development of evidence-based policy advice to support governments in planning, developing, monitoring and evaluating SME and entrepreneurship policy approaches, including across different levels of government.

Annex C. Chair's Summary

On 22-23 February 2018, the OECD convened a Ministerial Conference on “Strengthening SMEs and Entrepreneurship for Productivity and Inclusive Growth”, hosted by Mexico and under the guidance of the Chair, Minister Ildefonso Guajardo Villarreal (Mexico) and the Vice-Chairs, Minister Stuart Nash (New Zealand), State Secretary Marie-Gabrielle Ineichen-Fleisch (Switzerland) and Vice-Minister Hasan Ali Çelik (Turkey).

The meeting took place at a time when governments are seeking innovative solutions to address low productivity growth, concerns about international trade and rising or persistently high inequality. Small and medium-sized enterprise (SME) and entrepreneurship policies have a crucial role to play in delivering these solutions and in enabling SMEs and entrepreneurs to seize opportunities and mitigate risks that emerge from major shifts in the economy and society, such as increased globalisation, digitalisation, the new industrial revolution, the changing nature of work, demographic changes, the circular economy and the transition to a low-carbon economy.

The Ministerial Conference was the third Ministerial Conference held in the context of the OECD Bologna Process on SME and Entrepreneurship Policies, a dynamic political mechanism involving more than 80 economies around the world at different levels of development, and a large number of international organisations, institutions and non-governmental organizations (NGOs). It seeks to strengthen dialogue and co-operation to foster the entrepreneurship agenda and SME competitiveness at the global level, and encourages increasing co-operation in this area. The Bologna Process was launched at the first OECD Ministerial Conference on SMEs, held in Bologna, Italy, in June 2000, which produced the Bologna Charter on SME Policies. The second Ministerial Conference on SMEs was held in Istanbul, Turkey, in June 2004, and led to the Istanbul Ministerial Declaration on Fostering the Growth of Innovative and Internationally Competitive SMEs.

The Ministerial Declaration on Strengthening SMEs and Entrepreneurship for Productivity and Inclusive Growth was adopted at the Mexico City Conference by 55 countries, including all OECD Members and 20 non-Members, as well as the European Union.

The Conference brought together Ministers, Vice-Ministers, State Secretaries, senior government officials, and high-level representatives from international organisations and associations from 68 Delegations, including 33 OECD Members, 22 non-Members, the European Union, and 12 other organisations and stakeholders.

In the opening session of the Conference, the Secretary-General of the OECD, Mr Angel Gurría, highlighted the role of SMEs and entrepreneurship in economies and societies as a source of employment, added value, innovation, and social inclusion. He underlined the considerable economic and social benefits that can be achieved by enabling SMEs to scale up and innovate and of broadening entrepreneurial opportunities to all social groups. He pointed to the large heterogeneity of the SME population and the widening productivity gap between smaller SMEs and larger firms. He stressed the new opportunities for SMEs

and entrepreneurship brought about by digitalisation and globalisation, but noted that more efforts were needed to ensure that more small businesses can benefit from them.

He highlighted the crucial role of institutional and regulatory settings for SMEs. He indicated that the OECD is prepared to support governments to enable SMEs to overcome longstanding and emerging challenges, harness the digital revolution and play a greater role in the global economy.

The Chair of the Conference, Minister Ildefonso Guajardo, recalled the profound changes in the economic model since the last SME Ministerial Conference in 2004, and stressed the need to continue to find the right foundations to support market openness and entrepreneurship. He shared that in Mexico, SMEs and entrepreneurship are a high policy priority, leading to the creation of the National Entrepreneur's Institute (INADEM) in 2013, which has been supporting all aspects of entrepreneurship and SME development, including financing, skills, business development services, innovation and many others. He underlined the importance of stakeholder engagement in policy development for SMEs and entrepreneurship. He invited the OECD to deepen its analysis and dialogue on SMEs, and issued a call to the OECD to increase the visibility and impact of its work on SMEs.

Minister Kris Peeters (Belgium) and Secretary of State Mariano Mayer (Argentina) reported back from a side event with SME stakeholders and Ministers (or their representatives) that examined the views of businesses and social partners on the role of SME and entrepreneurship policy in the context of globalisation, digitalisation, technological change, and the changing nature of work. Stakeholders and participants stressed the importance of regulatory settings for SMEs, highlighting the potential of digital information portals and the need to consult entrepreneurs on the impacts of proposed new legislation. They also underlined the need to reflect the SME perspective in international trade negotiations. They agreed that governments should do more to foster linkages between SMEs and large firms to include SMEs in social dialogue and industrial relations systems. Participants called for governments to engage SME and entrepreneurs in policy making and supported the commitment of the OECD to pursue the dialogue with SME and entrepreneurs associations.

Participants agreed that digitalisation should be understood as a process and stressed the valuable contribution of the OECD to support countries in developing a comprehensive approach. They highlighted priority areas for policy action and public-private dialogue to foster SMEs' transition to the digital economy, including: developing appropriate regulatory frameworks; improving connectivity, cybersecurity and privacy; addressing SME financing needs; strengthening skills and facilitating upskilling and reskilling; fostering leadership capabilities in SMEs; developing partnerships with platforms and key industry players; using public procurement to foster SME innovation; reducing the administrative burden to foster entrepreneurship; addressing concerns of SMEs that feel threatened by change; and including workers in the digital transformation.

Enabling SMEs to scale up

SMEs that grow have a considerable impact on competition, innovation, employment and wages. Ministers and heads of delegations underlined that SMEs can scale up at different stages of their life cycle. Many factors influence high growth, and entrepreneurs' skills and ambitions are critical. It was noted that not all SMEs seek to grow.

Ministers and heads of delegation recognised that the capacity of start-ups and SMEs to scale up is influenced by institutional and policy settings including the regulatory environment, framework policies and targeted policies.

Key drivers for SME scale-up were discussed, including framework conditions and access to strategic resources, such as finance, skills, IT diffusion, technology and knowledge networking. Participants recognised that there are several different ways to achieve scale-up. The digital economy is opening a range of new opportunities for scaling up, including the emergence of new business models. Participants underlined that internationalisation, participation in global value chains (GVCs) and linkages with foreign direct investments can also help trigger SME scale up through access to international markets and technology transfer. Facilitating business transfers and mergers and acquisitions can also support SME scale-up.

Participants discussed various policy instruments to enable SMEs to scale. Governments are stepping up efforts to facilitate access to appropriate forms of finance for SMEs and start-ups to scale up by investing in innovations and new markets, including venture capital and private equity. Financing along the whole life cycle of firms was considered to be extremely important.

Initiatives are underway to upskill existing SME workforces and supporting SMEs to hire and retain skilled and high-qualified personnel, including training programmes combining classroom training with hands-on in-company training. Tailored business development services, including advice, consultancy and mentoring for entrepreneurs and SME managers, and business incubators and accelerators, are being developed across countries.

Governments are also seeking to facilitate access to state-of-the-art knowledge for SMEs through knowledge partnerships with research organisations, universities and other businesses. Participants highlighted that strategic use of public procurement can help SMEs innovate and scale-up. They also noted the importance of fostering mutually beneficial partnerships between SMEs and large firms along supply chains, and addressing unfair treatment of SMEs.

Ministers and heads of delegation agreed that an effective and transparent regulatory environment is critical for business growth, along with effective contract enforcement, intellectual property protection and civil justice systems. They discussed the importance of an SME Test for all proposed new legislation, to identify the potential impact on SMEs and entrepreneurship, and the use of regulatory sand boxes. It was also noted that size thresholds for regulatory compliance or policy incentives should not act as obstacles to scaling up. Participants highlighted that policy support should be tailored to the heterogeneity of the SME population.

Ministers and heads of delegation underlined that the OECD can play a crucial role in providing policy recommendations to improve the SMEs business environment, to enable growth-oriented SMEs to seize new opportunities, to promote competitiveness, productivity gains, open and fair international trade, cuts in red tape and pro-business reforms, and to help SMEs that are lagging behind, enabling adaptation, transformation, restructuring and orderly exit from the market.

Ministers and heads of delegation called for an integrated, whole-of-government approach to foster scale-up of SMEs, involving all key stakeholders, including direct engagement with SMEs and potential entrepreneurs. Several participants asked the OECD to support the development of such a strategic approach.

Several participants underlined the role the OECD can play in facilitating knowledge exchange across countries to support the sharing of good practices, and helping governments design and implement mutually reinforcing policies for enabling SMEs to scale up. They welcomed OECD tailored support to governments in reviewing and assessing SME and entrepreneurship policies and supporting the development of SME strategies.

Enhancing SME access to diversified financing instruments

Ministers and heads of delegation underlined that access to appropriate forms of finance is key to the creation, growth and productivity of SMEs and crucial to achieve Sustainable Development Goals across countries. They noted that certain categories of SMEs continue to face difficulties in obtaining financing in the appropriate forms and volumes. They also noted that while SME lending has been stagnating or contracting in some countries, SMEs are increasingly turning to alternative financing instruments. They agreed that more efforts are needed to diversify SME financing sources and address financing gaps for specific types of firms.

Ministers and heads of delegation acknowledged that the digital economy is opening a range of new opportunities for SME financing – known as Fintech - such as in the form of new financial services, the broadening of the investor base, and the use of alternative data to enhance credit risk assessment and achieve greater financial inclusion. SMEs need finance more than ever before. Preparing for the Next Production Revolution requires large scale investments in new machinery, IT, competences and know-how, which is unfeasible for cash-strapped small companies if financial markets cannot be accessed. On top of that in a more and more knowledge based economy, in which data, algorithms, skills and know-how are becoming key factors of success, funding can no more be provided simply on the basis of tangible assets and physical collateral, but more attention should be paid to intangibles. At the same time, participants highlighted the importance of appropriate regulatory frameworks to support these developments.

Participants discussed policy instruments and experiences to enhance SME access to diversified financing instruments. They noted the importance of enhancing credit guarantee schemes, to address diverse financing needs by SMEs, including for investment and export-related activity, and ensure additionality. Participants highlighted measures to strengthen credit risk information infrastructures, including through the use of Big Data and Fintech, to reflect more accurately the level of risk associated with SME financing. It was also noted that facilitating SME cooperative initiatives can help them achieve scale and strengthen access to credit.

Governments are increasingly using public procurement to foster SME development, and participants noted that aligning purchasing policies across government, ensuring timely payments and combining public purchases with advisory services and training of entrepreneurs can increase the effectiveness of these strategies.

Ministers and heads of delegation shared experiences to support the development of factoring finance, corporate debt markets for SMEs, crowdfunding and peer-to-peer lending, venture capital funds for early stage start-up support, SME listings and private equity investments, mobilising private capital for growth and leveraging private competencies. They noted that schemes should ensure appropriate risk-sharing with financial institutions and entrepreneurs. They also noted the potential of block chain to

enhance SME financing, and the importance for governments to stay abreast of developments in technologies and finance markets.

Ministers and heads of delegation agreed on the need to address financing needs along the entire life cycle of the SMEs, tackling both demand and supply-side barriers. In particular, they noted importance of identifying effective policies to sustain financing for growth and innovation, as well as SMEs' transition to a low carbon economy and investment in green technologies. They also underlined the need to address regional imbalances and support financing for underrepresented groups, including youth and women entrepreneurs.

Participants asked for the OECD's support to improve the evidence base, deepen understanding of SME financing needs and share good practices. They highlighted importance of implementing G20/OECD High-level Principles on SME Financing. They underlined also the need to engage more with SMEs and other stakeholders.

Fostering greater SME participation in a globally integrated economy

Ministers and heads of delegation recognised that changes in the global environment, such as the rise in GVCs and digitalisation, offer new opportunities for SMEs to participate in the global economy, with positive implications for SME innovation, scale-up and productivity. However, it was noted that participation in global markets is uneven across the SME population, and benefits from GVC integration depend on the nature of inter-firm linkages and position in global production networks. Participants also highlighted that, while digitalisation facilitates SMEs to access global markets and the emergence of “born-global” enterprises, many SMEs are lagging behind in the digital transition.

Ministers and heads of delegation discussed key barriers to SME participation in global markets, including limited information and understanding about foreign markets and GVC requirements and standards, lack of skills and efficient organisational practices, financing constraints, weak infrastructures and logistics services.

Ministers and heads of delegation recognised that although tariffs have been reduced substantially in recent decades, trade barriers remain, which impact SMEs disproportionately. They also acknowledged that the increased number and complexity of cross-border data transfer restrictions may condition the benefits that SMEs gain from digital trade. They underlined the importance of considering SME-related issues in international trade dialogue.

Policy instruments to enhance SME participation in the global economy were discussed, and good practices and novel policy approaches were shared. Participants stressed the importance of fostering competitive domestic markets and lifting product market regulations, especially in services, to encourage innovation and growth of the most efficient SMEs and enhance their participation in GVCs. Governments are streamlining and automating border procedures and simplifying requirements, in order to reduce the administrative burdens for trading that typically affect SMEs disproportionately. Governments are also taking action to address information barriers for SMEs about business opportunities, foreign partners, standards, regulations and trade procedures.

Ministers and heads of delegation discussed policies to enhance SME access to appropriate forms of finance, such as credit and supply chain finance, support SME investment in skills, access to skilled workers and development of strategic capabilities to navigate international markets, and foster SME innovation, including through R&D fiscal incentives, research partnerships and intellectual asset management. Governments are also placing priority on

improving digital connectivity and fostering participation by new firms and SMEs in global e-commerce markets.

Ministers and heads of delegation also focused on policies to foster SME linkages with larger firms, taking into account new developments in GVCs, including as a consequence of digitalisation.

Ministers and heads of delegation underlined that the increasingly complex global environment calls for domestic whole-of government approaches to address constraints to SME internationalisation. Also, greater international cooperation is needed to address global challenges, from traditional standards to new regulatory issues in the digital age.

Ministers and heads of delegation highlighted the OECD role in documenting SME participation in the global economy, fostering an exchange of knowledge and good practices, and understanding the policy implications of ongoing transformations.

Improving the business environment for SMEs through effective regulation

Ministers and heads of delegation recognised that an effective and transparent regulatory environment is essential for levelling the playing field for businesses of all sizes, fostering SME investment and innovation, promoting entrepreneurship, lowering informality and reducing corruption.

Ministers and heads of delegation acknowledged the disproportionate impact of regulatory complexities add burdens on SMEs' capacity to invest, innovate and compete, including in global markets. They stressed the importance of efficient contract enforcement, transparency and integrity in the public sector, since opacity and corruption, which are detrimental to all businesses, pose particular problems to SMEs.

Ministers and heads of delegation acknowledged the need to use digitalisation to improve regulatory conditions and reducing administrative burdens, as well as delivering better administrative services to businesses, including through closer collaboration with the private sector. They also noted the importance of the regulatory framework for access to finance by SMEs.

Participants discussed policy approaches to improve regulatory conditions for SMEs, such as cutting red tape for businesses, or through the One-for-One rule, and the "once only" principle, as well as facilitating regulatory and tax compliance through simplification, targeted use of technologies and improved communication, including one stop shops and online submission of information. It was noted that exemptions and simplification measures should be carefully designed, to avoid creating additional complexities or distortions, which may limit SME growth.

Participants discussed the implementation of SME tests in regulatory impact analysis and sand box approaches to facilitate experimentations. Participants acknowledged that there is no "one size fits all" model for regulatory reform, and policy responses need to be context-specific. They underlined the need for policy coherence and coordination, stability and predictability across Ministries, as well as stakeholder coordination. The risk of threshold effects as a result of size-contingent policies was noted.

Ministers and heads of delegation underlined that the OECD can help support a level playing field for SMEs, including through the identification and diffusion of good practice principles for regulatory reforms. Some asked the OECD to support countries in developing

coherent approaches and better data to improve regulatory conditions for SMEs in the context of developing an OECD strategy for SMEs.

Business transfer as an engine for SME growth

Ministers and heads of delegation recognised that enabling the successful transfer of economically sound SMEs is crucial to retain employment, preserve assets value and continuity in production processes and business relations. It was noted that more employment can be retained thanks to successful transfer than what is created by new firms. Participants also highlighted that business transfer can represent an opportunity to innovate business models and managerial practices and for new entrepreneurs to enter the market. Participants underlined that policy makers should focus on take-ups, as well as on start-ups.

In light of the ageing of entrepreneurs, Ministers and heads of delegation highlighted the urgent need to address key business transfer challenges that are causing the closure of many viable SMEs. These include regulatory complexity and administrative burdens, lack of adequate planning and competencies in SMEs, limited access to advisory services, difficulties in the identification of potential transferees and appropriate forms of transfer, resistance to dilute ownership and managerial discretion in family businesses, and financial constraints to takeover.

Participants discussed policy instruments to create sound conditions for SME transfer and enhance entrepreneurial opportunities. They agreed on the importance of developing a conducive regulatory, administrative and fiscal environment. In particular, they discussed approaches to reduce administrative burdens, and address adverse tax consequences on sale or disposal of SMEs, such as through exemptions from gift and inheritance taxes and the loosening of pre-existing tight conditions to benefit from these exemptions.

Ministers and heads of delegation noted that increasing entrepreneurs' awareness and enabling advanced planning for expected and unexpected business transfer is crucial. This also includes supporting access to networks of professional advisers involved in business transfer, developing guidelines and toolkits and providing targeted services to entrepreneurs.

Ministers and heads of delegation shared views and experiences on how governments can strengthen match-making and the development of business transfer markets. They discussed measures to raise awareness about SME takeover opportunities, and foster on-line market places for business exchanges, including across borders, ensuring quality standards and transparency. It was noted that family businesses face specific challenges for successful transfer, and how mentoring and coaching approaches can facilitate smooth succession. Governments are also taking action to enhance access to appropriate forms of finance by firms undertaking ownership change and by potential transferees, including credit guarantees and equity instruments.

Ministers and heads of delegation underlined the importance of a seamless policy approach to business transfer, addressing needs at the pre-transfer, mid transfer and post-transfer stages. They also noted importance of ensuring coherence across policy areas that have implications for business transfer.

Ministers and heads of delegation encouraged the OECD to improve evidence about SME business transfer forms and trends, distinguishing different types of SME, to increase knowledge about the causes of business transfer failures and policy levers for successful

transmission. In light of their relevance across countries and their specific features and challenges, they called on the OECD to undertake work on family businesses.

Developing Entrepreneurial Competencies

Ministers and heads of delegation recognised the importance of entrepreneurial competencies for enabling successful business creation and enabling employees to contribute to SME innovation. They also noted the social and ethical aspects and impacts of entrepreneurial competencies.

Ministers and heads of delegation highlighted the breadth and soft nature of entrepreneurial competencies, which combine a range of attributes, including creativity, a sense of initiative and responsibility, problem-solving, team work, negotiation, the capability to manage resources, and financial and technological knowledge.

They emphasised the critical role of the formal education system for the development of entrepreneurial competencies, and that entrepreneurship education is needed across the primary, secondary, and tertiary education levels. They also highlighted the importance of entrepreneurship training outside of the school system.

Despite recent efforts to increase support for building entrepreneurial competencies, participants emphasised that more students, employees and entrepreneurs should be offered appropriate entrepreneurship education and training. They underlined that teaching for entrepreneurial competencies should be practical rather than theoretical, including practical entrepreneurship projects and work-integrated learning experiences in SMEs. They shared knowledge on recent approaches.

In assessing the impacts of entrepreneurship education and training, participants noted that the full impacts may only become evident in the longer term and that the benefits can be broad, encompassing self-development, community development and business development.

Ministers and heads of delegation discussed various policy instruments to support entrepreneurial competencies, in particular through providing training, networks and support materials for teachers of entrepreneurship; and offering start-up support for students who are motivated and able to start a business in the near future such as access to finance, mentoring, and incubation.

Ministers and heads of delegation emphasised the importance of taking an integrated policy approach, involving all the ministries with relevant tools and interests, co-ordinating across different levels of education, and building links between entrepreneurship education and start-up support. They recognised the important role of the OECD in facilitating policy analysis, knowledge exchange, peer learning and capacity building among countries in this area.

Promoting innovation in established SMEs

Ministers and heads of delegation underlined that innovation in established SMEs is a key driver of inclusive growth, by reducing productivity gaps and wage gaps between SMEs and large companies. However, they also noted that there is strong heterogeneity in the SME innovation performance.

Ministers and heads of delegation underlined the shift towards an ‘open innovation’ paradigm in which innovation is the outcome of inter-firm collaboration and industry-

university collaboration. They agreed this shift is making innovation more accessible to SMEs. Participants also remarked that government spending in R&D and innovation is on the rise in many countries, but national targets are not being yet met in many cases. Some participants noted that business innovation should be mostly private-sector driven.

Ministers and heads of delegation emphasised the importance of creating national and local innovation systems which are inclusive of SMEs, such as through the establishment of innovation centres and centres of excellence which promote collaborative research between SMEs and research organisations and transfer applied knowledge to SMEs. They pointed out the importance of clusters as a hotbed of innovation, noting the importance of engaging different industries, to enable convergence to create innovative products and services.

Ministers and heads of delegation emphasised the importance of the institutional and regulatory settings to promote innovation in SMEs, ensuring a coordinated and comprehensive approach. They pointed to the importance of regulations which favour SME innovation, including a flexible labour market furthering the allocation of resources to the most productive sectors and firms.

Ministers and heads of delegation emphasised the role of skills for innovation in SMEs. Building a strong education sector which generates a talented labour force, upgrading managerial and workforce skills in SMEs, and raising awareness in SME about innovation, were all priorities mentioned by participants. Participants also stressed the urgency for SMEs to go digital and the role of policies to enhance digital skills, digital infrastructure and access to markets. It was noted that funding initiatives, such as innovation vouchers, have the merit of supporting innovation in SMEs and also creating a market for innovation services.

Discussion showed that approaches differ across countries, with some adopting a sectoral approach to supporting business innovation, and others developing horizontal strategies, with due consideration to avoid the risk of “picking winners”.

Strengthening social inclusion through inclusive entrepreneurship

Ministers and heads of delegation recognised the importance of enhancing entrepreneurial opportunities for under-represented and disadvantaged groups, including women, youth, seniors, the unemployed, migrants, indigenous people, people with disabilities, and people in peripheral and rural areas. Tapping into entrepreneurial talent that flourishes in different parts of society holds the potential to both help empower different groups and spur growth. They stressed that inclusive entrepreneurship is critical for achieving global agendas such as the Sustainable Development Goals.

Ministers and heads of delegation highlighted a number of significant barriers that hinder under-represented and disadvantaged groups from creating successful and sustainable business. Amongst others, these obstacles include the lack of entrepreneurship skills; difficulties in accessing start-up financing; difficulties in navigating the regulatory environment; administrative burdens for business creation and development; limited access to small entrepreneurship networks; fear of failure and lack of confidence; and negative social attitudes. These barriers tend to be larger in scale or different in nature for under-represented and disadvantaged social groups in entrepreneurship.

Ministers and heads of delegation shared knowledge on policy instruments to foster inclusive entrepreneurship, including dedicated and tailored programmes for specific social groups in the areas of entrepreneurship training, coaching and mentoring programmes, and

microcredit and loan guarantee programmes. In addition to dedicated programmes for target social groups, it is also important to increase the outreach of mainstream entrepreneurship support programmes to under-reached parts of the population, including through training for business development service providers to effectively work with people from these target groups and collaborations between business development service providers and relevant community organisations with access to target populations.

Ministers and heads of delegation also stressed the importance of tailoring microcredit and loan guarantee programmes for women, young people, and immigrants. It was also underlined that public financial institutions have a key role to play to foster access to equity, such as by favouring greater gender diversity in boards. Clusters and public procurement were also identified as key levers to better integrate vulnerable groups, when used strategically.

Increasing attention is also being placed on building entrepreneurship networks for women, youth, immigrants and unemployed entrepreneurs and other social groups and ensuring that these networks are well-connected with professional business supports.

The discussion identified a number of key success factors for inclusive entrepreneurship policy. These include effective outreach to target clients; understanding the challenges faced by the target entrepreneurs; and the use of an integrated package of supports combining training, mentoring, financing and networking. Ministers and heads of delegation noted that interventions typically have the greatest impact when they encourage innovation and the exploitation of markets with excess demand.

Ministers and heads of delegation underlined the importance of the territorial dimension of inclusive entrepreneurship to ensure that actions targeting vulnerable groups take account of local specificities and communities.

Ministers and heads of delegation agreed on the importance of joint work across Ministries and government agencies, in order to ensure that inclusive entrepreneurship policies and programmes are coherent with labour market and education policies. They underlined that OECD can facilitate knowledge exchange between countries to support the transfer of good practices in inclusive entrepreneurship policies.

Ministers and heads of delegation also underlined the need to address informality, which is more common among disadvantaged groups, and negatively affects productivity, access to social services and financial inclusion. They also stressed that the underlying causes of exclusion should be addressed. They called on the OECD to undertake work on policies to enhance formalisation.

Monitoring and Evaluation of SME and Entrepreneurship Policies and Programmes

Ministers and heads of delegation and participants underlined the importance of evidence-based policy making. They agreed that impact assessment and evaluation are extremely important, as they contribute to the accountability of programs and policies. They are necessary to understand which policies work and which do not, and to demonstrate to taxpayers that public resources are being used effectively. They referred to the crucial roles of ex ante evaluations and appraisals to guide decisions about which sorts of new policies to introduce, as well as timely mid-term evaluations and robust final impact evaluations.

However, Ministers and heads of delegation also identified a number of barriers to improving evaluation practice. These barriers included obtaining data from other

government agencies, the adequate timing for obtaining the data, lack of knowledge about high quality evaluation practices and methods, a fear of negative reactions to poor evaluation results, and a lack of systematised and comprehensive approach to SME and entrepreneurship policy evaluation. They also recognised that the evaluation process is often complex, not only for the difficulties often faced in the ex-post data collection from beneficiaries, but also for the high cost that sometimes the whole process entails.

They stressed that more efforts are needed to spread a culture of evaluation in SME and entrepreneurship policy. They highlighted how the culture of evaluation can be supported in various ways that include establishing relevant administrative structures for evaluation, establishing clear measurable objectives at the outset of programmes, developing appropriate key performance indicators, evaluating against established objectives and indicators and sharing and publishing the results. They pointed to the need to create spaces for policy experimentation and evaluation, recognising that evaluations will provide negative as well as positive results.

They underlined that impact evaluation must move away from simply providing statistics of programme expenditures and activities to analysis of causal effects and counterfactual analysis. Several participants pointed to how recent advances in evaluation techniques can be brought to bear on the impact evaluation of SME and entrepreneurship policies and programmes, including control group studies and experimental studies. Several countries presented evaluations they have undertaken using robust counterfactual and control group based evaluation approaches and detailed and independent data. However, they noted that the use of these techniques and data sources is still underdeveloped in SME and entrepreneurship policy evaluation.

Ministers and heads of delegation also recognised substantial recent increases in the availability of data within government administrations, including social security data and tax data, and also the wider availability of Big Data and Open Data. Use of these data can shed more light on policy impacts on SMEs, entrepreneurs and the economy and helping provide more timely evaluation results. However, they recognised that deliberate strategies are needed to exploit these data for SME and entrepreneurship policy evaluation. Several participants also referred to the importance of developing qualitative data and wider studies to complement quantitative impact evaluation approaches.

They stressed the need for a whole-of-government approach to SME and entrepreneurship policy evaluation. Evaluations should be undertaken in a systematic and holistic manner across the domain of SME and entrepreneurship policy, including all the various programmes, agencies and ministries involved. Participants and participants also stressed that the evaluation approach should also take account of how mainstream sectoral policies – immigration, skills, transport, health, culture, education policies etc. – impact on SMEs and entrepreneurship.

Ministers and heads of delegation underlined the role of the OECD in facilitating knowledge exchange among countries on evolving practices and approaches to SME and entrepreneurship policy evaluation and support the sharing of good practices. Participants called on the OECD to update its 2007 Framework for the Evaluation of SME and Entrepreneurship Policies and Programmes to reflect recent changes in policy measures, data availability and evaluation techniques. It was also proposed that the OECD work directly with countries to evaluate their programmes, particularly with regards to impact evaluation.

The way forward

During the discussions over the two days of the Ministerial Conference, participants highlighted the importance governments attach to SMEs and entrepreneurs, and the necessity to enable them to contribute more fully to productivity and inclusive growth. They underlined the need for evidence-based policies to foster SME development and growth and recognised the central role the OECD plays in analysis, policy dialogue, exchange of best practices and tailored policy support to governments in the area of SMEs and entrepreneurship. Several participants called on the OECD to step up its work on SMEs, to support governments by developing a holistic, integrated approach to SME policy making.

Several participants also called on the OECD, through its Working Party on SMEs and Entrepreneurship, to elevate the visibility and impact of its work on SMEs for the benefit of all countries. To this end, they asked the OECD to undertake an assessment which provides recommendations for achieving these objectives. They also asked the OECD to organise other high-level events on specific dimensions of SME policy, as well as another Ministerial meeting in 2020 or in the near future, in order to continue the fruitful dialogue and information sharing that took place in Mexico City.

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

The OECD is a unique forum where governments work together to address the economic, social and environmental challenges of globalisation. The OECD is also at the forefront of efforts to understand and to help governments respond to new developments and concerns, such as corporate governance, the information economy and the challenges of an ageing population. The Organisation provides a setting where governments can compare policy experiences, seek answers to common problems, identify good practice and work to co-ordinate domestic and international policies.

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