

Potential Creation for SMEs

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Abstract

This article gives an overview of which policy areas are essential parts of a government overall strategy to enlarge SMEs' potential. The article also provides insights into the relative importance of each of these policy areas. Article conclusions are based on a cross-country comparison of indicators measuring performance and business environment for SMEs.

This study is to suggest a specific set of indicators, to provide with a quick overview of which policy areas are crucial. Potential creation for SMEs is measured via entrepreneurship performance and top performers are identified. The relative importance of the policy areas affecting SMEs' potential is determined by linking indicators of performance with the indicators of the business environment.

Key words: SME, SMEs' potential, entrepreneur, entrepreneurship.

JEL Classification: JEL B21, B50, L26

1 Introduction

Entrepreneurial approach shows a cohesive and pervasive policy approach that spans all aspects of society. Policy to create potential for SMEs is pervasive and includes a broad spectrum of agencies, organizations and institutions. It comes from a shift of identification of contemporary economy from managed economy to entrepreneurial economy. Potential of SMEs ensures small firm can compete in the marketplace and they are not prejudiced because of their small size, relative to large firms. It allows create a dynamic economy, which ensures that people can start new ventures and subsequently develop these venture to become high-growth firms. To promote potential for SMEs, governments should support and increase a country's ability to compete on knowledge, new ideas, and the ability to adapt and find new solutions to problems.

Contemporary entrepreneurship antecedents – historical background:

In order to accomplish certain objectives we highlight main concepts in the evolutionary path of entrepreneurship over the years. We try to construct a comprehensive view of entrepreneurial characteristics and processes. We find necessary to search for better understanding of the overall

entrepreneurship landscape, in terms of historical and conceptual mile stones developed over time, as follows:

First introduced the concept of entrepreneur Richard Cantillon (1680 - 1734). Entrepreneur comes from “*Entreprendre*” = ability to take charge. *He gives the simplest and perhaps the most encompassing characterization ever offered.* Cantillonian entrepreneur took charge of the situation at hand and did whatever necessary to achieve his objectives.

Jean Baptist Say (1767 - 1832) pointed to the critical role of resources and commanding (i.e., “marshalling”) them to help materialize the entrepreneurial project. He emphasized the ability of Entrepreneur to command resources for responding to unfulfilled opportunities.

An “economic good” had to have a direct “causal connection” to the needs of analytical consumers in the market place. Carl Menger called them “economizers” imputing a value (i.e., consumer’s expected price) to that good for satisfying their needs. Entrepreneur recognized the logical process underlying consumer’s decision-making processes in favour of higher valued products. He distinguished between „economic goods“ and all others. The entrepreneur would in turn determine whether or not to respond to the opportunity at the imputed value with a lower price.

In modern management terminology, this is equivalent to conducting a feasibility study (and a business plan) for responding to such pending demand, which would serve to firm up (or abandon) commitments to deliver the „economic goods” at, or below, that expected price.

Entrepreneur according to Menger saw the economic opportunity in terms of *exchange of „economic good” of unequal value in order to generate mutual value* for both the entrepreneur supplying the goods and the ever „analyzing consumer” demanding them. Unfortunately, the Mengerian concept of “exchange” of “economic goods” of unequal value was lost for a long time.

Entrepreneurs have the ability to take integrated action in the enterprise as a whole. Ely and Hess envisioned a *four-factor model of the firm* (i.e., *capital, labour, enterprise and the entrepreneur*) with the entrepreneur as an integral part of the firm. This conception resonates very well with the proposed grounded framework outlined earlier. Unfortunately, in the classical Theory of the Firm, the *explicit role of the entrepreneurs* was lost and is still missing in the modern theory of international firms (e.g., Multinational Enterprises).

While the enterprise has gained more prominence, the role of entrepreneurs has diminished. Ely and Hess saw entrepreneurship’s horizon expanding far beyond the industrial revolution in England. They re-confirmed Cantillon’s early vision of internationalization of entrepreneurship. Entrepreneur is nested in the enterprise and both are embedded in a resourceful environment, while transacting in the market, as intimately interactive and adaptive entities.

This vision and the four-factor model of Ely and Hess remained hidden to the economic science for nearly a century. A re-formulated version of this four-model factor serves as the fundamental basis for formulation of the grounded entrepreneurship framework.

Entrepreneurs “*create*” opportunity by using “*innovative combinations*”. Schumpeter’s entrepreneurs had non-conformable attitude, they used novel combinations pro-actively to respond to unfulfilled opportunity. This opportunity should eventually lead to “*creative destruction*” of passive industry practices. Entrepreneur was not required to invent. But he would have to possess the ability to take the necessary invention to the market place and commercialize them successfully. Such entrepreneurs had the special ability. They could recognize the temporally-unstable nature of market equilibrium in the absence of what Menger had called “economic good”. Entrepreneurs were capable of launching products and processes of extremely higher value than the prevailing products for exchanges of “unequal value”. Of course, they kept thriving to create higher-value “economic products” and like this disrupt the temporal “equilibrium” of lower-valued products.

Entrepreneurs according to Hayek followed principle of entrepreneurial discovery and action. Entrepreneurs recognize the prevalence of information asymmetry. It comes due to unequal distribution of information. Information has got two critical aspects: access and comprehension. On access information is costing and not immediately available. Entrepreneur needs to distinguish between worthless data and valuable information.

This specialization leads to deeper comprehension of new information. However, access does not necessarily mean comprehension. Hayek’s entrepreneurs would follow a “discovery procedure”, they search opportunities and keep discovering what to bring for exchange to the market place in order to satisfy consumers demands.

Albert Shapero characterized entrepreneurs as identifying “credible opportunities”. They depend on two critical antecedents: i.e., perception of “desirability” and “feasibility” from both personal and social viewpoints. Ability to recognize and analyze immediately is the most important.

Logical steps according to Shapero are as follows: 1. analysis of the “credibility of the opportunity” before acting on it, 2. considering the impact of the market factors influential in their potential action 3. ultimate decision influenced by “intention to act”.

Peter Drucker brings to a science a phenomena of entrepreneur - manager. He can foresee market trends. Managers are forced to see, or develop a vision to foresee, to be aware of lager size and diversity of international markets. New entrepreneur has to look into the international market horizons for trends and opportunities. Small firms are consistently internationalizing.

“Creative destruction” (according to Schumpeter) would organize and re-organize the industry structure and nature of work in the industry. Shapero’s entrepreneurs act upon opportunities. They possess the fertile minds with acute cognitive and analytical capabilities.

2 Body of Paper

Small enterprise is not a single event, but a process that transforms an innovative idea of an entrepreneurs into a growing firm. Most SMEs are result of failure, while others survive at, or near, the break-even point. Very small minority of SMEs turn into high-growth enterprises. [9]

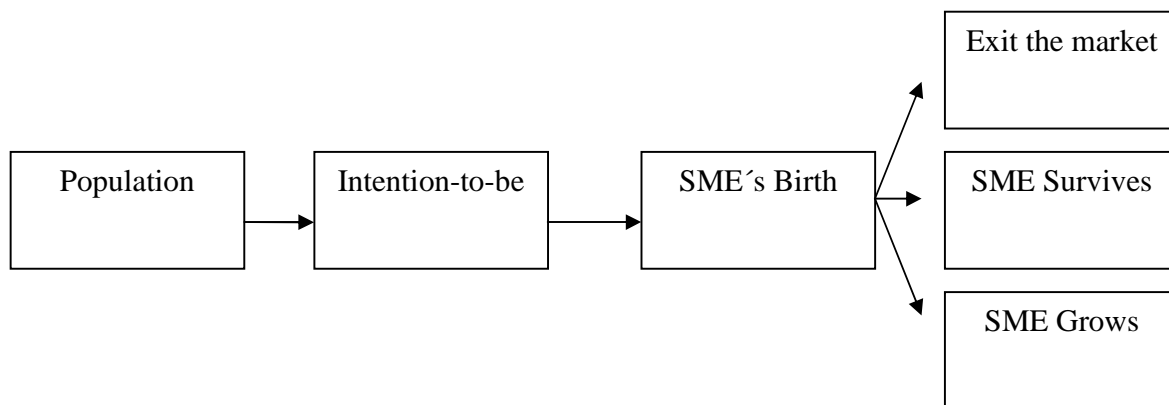


Figure 2.1 SME's survival

Source: Own, Kaufman [9]

Potential creation for SMEs should be designed to meet a set of policy objectives. Consequently the basis of Potential creation for SMEs must reflect policy objectives. Three main objectives are defined:

1. Job creation
2. Economic growth
3. Regional development.

Conclusive analyses shows a direct link between these three aspects of entrepreneurial process.

<u>Entry of SMEs</u>	<u>New high growth SMEs</u>
SMEs' entry rates, average 2000-7 (new firms as % existing firms)	Share of young SMEs with more than 60 % growth rates in turnover
Entrepreneurial activity (TEA) average 2000-7	Share of young SMEs with more than 60 % rates in employment

Figure 2.2 Entry indicators of SMEs

Source: Own

Only a few comparable data exist, which can be used to measure SMEs' potential and performance as it is defined in this article. Four indicators are used in this analysis (Figure 2.2). These data will be defined as performance indicators, as they measure the outcome of SME's activity. Some alternative measures of SME's performance exist, but these will not be included in this analysis as their link for our purposes is less clear.

Top performing countries:

High growth firm is defined as a firm which share of growth rate (in either employment or turnover) is higher than 60 % in three year period. The 60 % threshold is commonly used, but is not based on any hard evidence. Both turnover and employment are used as measures of high growth because of the differences on growth patterns across sectors.

European Union harmonized SME's definition and their data on entry of firms. EU's Eurobarometer publishes Observatory of European SMEs.

The current Observatory of SME Survey was carried out in the 27 Member States of the European Union (only 25 were already members at the time of the fieldwork), as well as in Norway, Iceland and Turkey under the framework of the Flash Eurobarometer survey series. It included 11 000 small and medium enterprises (with 250- persons employed) in its sample.

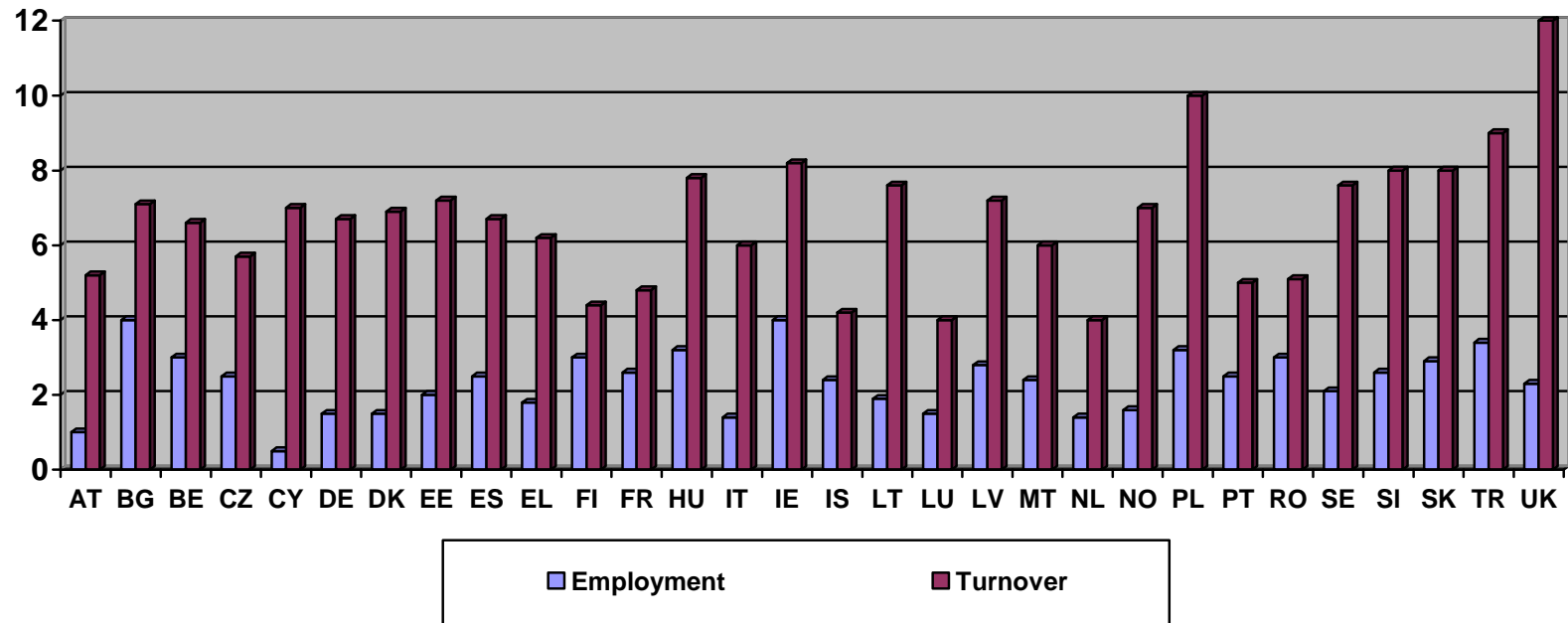


Figure 2.3 In % - Share of SMEs with more than 60 % growth rates
 Source: Calculation based on Observatory of European SMEs [10]

The Figure 2.3 shows that the ranking countries stands up to changes in the 60 per cent threshold. The ranking is also robust to corrections for differences in the industry structure across countries. From this analysis, the United Kingdom and Poland are performing better than other countries studied speaking about turnover the better performing are Ireland, Bulgaria and Belgium. The growth data of Bulgaria are biased because of a lack of data in certain years.

Policies must always be designed to match the set of macroeconomic policy objectives. Entrepreneurship is consequently defined as the entry and creation of high-performance firms, as our following analyses shows direct links between these two parts of the entrepreneurial process and productivity growth.

Analysis was based on cross-country analysis by benchmarking their business environment to that of the top-performing countries. This will give an overview of those parts of their business that need to be improved.

A lot of definitions in the literature describe the factors affecting entrepreneurship. The differences between various studies are often semantic. The firm is created by combination of three factors:

1. Opportunities
2. Skilled labour
3. Capital

Combination of these does not necessarily create or increase SMEs potential. If costs outweigh potential benefits, then opportunity should not be pursued. Opportunities are needed for SME's potential growth. All in all, the regulation and legal environment must affect skills, opportunities and capital along with an appropriate incentive structure and motivation. Role of motivation support is essential for future SME's potential.

Despite the obvious limitations of the approach presented in this chapter, no real alternative exists for increasing the SME's potential advising stakeholders on what to do about SMEs and entrepreneurship in their country.

3 Conclusions

The incremental attitude suggests that the rest of the economy remains unchanged, but new instruments are introduced to spur entrepreneurs. The most important result is not just a few entrepreneurial start-ups, but rather an entire economic approach. We can see new public policy direction that not only spans many, if not most, institutions, but also leaves no branch of the economy untouched.

Concluding we stress that policy to create a sufficient potential for SME may actually be less about specific new instruments or agencies and more about how traditional policies and agencies need to be redirected. It requires the shift from their traditional role in the managed economy to a very different orientation in the "entrepreneurial economy". Rather than focus on the addition of

potential creation for SMEs via arsenal of public instruments, the debate should perhaps focus instead on the changing role of public policy in the “entrepreneurial economy”. Public attitude towards taxes, finance, labour markets, education, research, international trade, social and health security becomes dramatically different as the “entrepreneurial economy” replaces the “managed economy”.

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