HOW TO BE A STAND OUT SME

A Performance Study of the EU SME Sector for the Period 2008 - 2013

MAZARS

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FOREWORD

There is no doubt that SMEs are and will always be the backbone of every economy in Europe. There are over 20 million SMEs in Europe and they have contributed to the generation of substantial income, employment, outputs, innovation and new technologies. The SME sector has over the last number of years experienced the most severe economic crisis in living memory. Some SMEs have emerged from this downturn more resilient and stronger than ever before. Others, however, were forced to downsize or close down as a result of the downturn.

This study was prepared to provide analysis, insights, learnings and guidance to SMEs no matter where in the world they are operating. The study highlights the similarities and differences of SME performance in Germany, Sweden, Netherlands, Portugal, Spain, France, Ireland and the UK. It explores what it takes to achieve levels of superior performance, to compete in the marketplace and effectively "stand out from the crowd".

The Mazars SME Practice Group has had a deep involvement with the international SME sector for many years. During this time the Mazars SME Practice Group has been dedicated to truly understanding the challenges facing SMEs and developing tools and mechanisms to help SMEs perform to their best. Our practice has helped many SMEs worldwide deal with a myriad of challenges so that they become the stand out SME. We would be very happy to help you too. We use a tool called The Mazars Quick Score which is an online assessment tool that helps SMEs to understand their business performance against four fundamental drivers of business success. To complete the online assessment to see if your business is a stand out SME, please visit www.mazars.ie

We would like to thank the many people who helped to produce this study. In particular we would like to thank our SME clients who gave us valuable information and acted as a great resource for this study. In producing this study we have relied heavily on extensive EU and national level research. A full listing of the references used in this study is outlined in Section 8.

We hope you find this study useful and informative.

Phil Verity & Joe Carr

1. EXECUTIVE SUMMARY

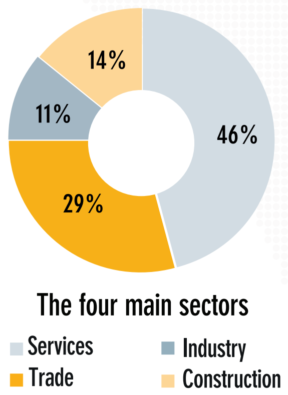
1.1 KEY FACTS - A CROWDED AND COMPETITIVE MARKETPLACE

- **Hard to be seen**

As an SME it is hard to be seen and stand out. A European SME is one of almost 21 million.

- **The ten employee barrier**

Very few SMEs grow beyond the micro stage. Across the EU-27 approximately 92% of companies have fewer than 10 employees. This is a universal story across individual countries. The German market however, is unique for a number of reasons, not least the size profile of companies, with a significantly higher share of larger companies than its European counterparts.



The four main sectors

- **The top of companies, 1% have secured a commanding position**

1% of the total enterprise population within the non-financial business economy (including both SMEs and large enterprises) of the EU 27 generates 60% of total private sector value added.

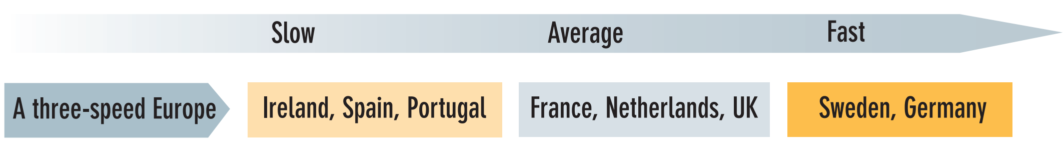
- **The four main sectors**

The sectors within which SMEs operate in four main groups: services, industry, trade and construction.

- **A three-speed Europe following the crisis**

Since the downturn SMEs have effectively operated in a three-speed Europe with German and Swedish SMEs benefitting from much more favourable economic environments. The strength of national economies and the quality of domestic demand was certainly a key influencer of SME performance over the last few years.

SME Economy Speed of Recovery at Country Level



- **Country competitiveness is key**

A globally competitive position can be achieved regardless of the broader socio-economic model adopted by the country. For example, the tax and public policies of Germany, the US and Sweden are very different yet they rank 4th, 5th and 6th respectively on global competitiveness ranking.

1.2 LEARNING FROM THE BEST - SIX SUCCESS FACTORS TO STAND OUT FROM THE CROWD

This study has identified six success factors to help SMEs reach the bar of superior performance and stand out from the crowd.

- **Maintain a sharp focus on the market**

Where and how you position your company in the wider market should never be regarded as fixed, it is always changing. It requires constant market information and the time and attention of management to identify the important underlying messages or signals from all the noise of the market and act accordingly at the right speed.

- **Bring more to the party**

The traditional model of the shop, wholesaler, service, trade or profession with very little value added in terms of brand difference, technology and know-how is simply not sufficient. For companies to compete and succeed they must bring more to the party and add better value to their customers with technology becoming a key enabler in this process.

- **Build resilience and operate with financial discipline**

The creation of safety buffers through higher profitability and retained earnings for the tough times, together with a prudent attitude to borrowing, are key features of stand out SMEs.

- **Right size your organisation**

While biggest is not always best, our analysis suggests that size does matter and having the right critical mass for the specific competitive and performance challenges of each business is absolutely crucial. In some companies it will not be possible to maintain market position without being significantly bigger. SMEs should be open to mergers, alliances and joint ventures.

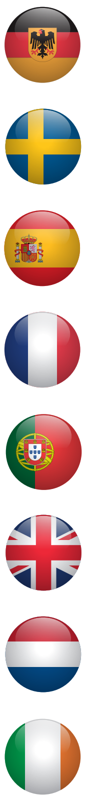
- **Increase your international outlook and extend your geographic footprint**

While it will not be possible for all SMEs to export, the burden of growth and recovery within most national economies currently falls on too few SMEs. Those that do not extend their businesses beyond local or regional markets must be aware of, and accept the higher risk threshold, of focusing solely on the local market and being at the mercy of domestic demand.

- **Manage for today and lead for tomorrow**

In our experience the quality of the management team is the most important determinant of the success or failure of business in the SME segment. Irrespective of country, sector or size the management team in each business needs to remain focused for both the short and longer term on the four fundamental drivers of stand out performance. They are:

  - Market position, customer offering and selling
  - Operations and customer service
  - Finance, business performance and risk management
  - Leading and managing people and teams

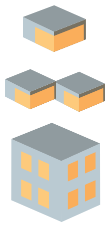


8 countries included in the study

2. BACKGROUND

2.1 NUMBER AND SIZE OF ENTERPRISES

The small and medium sized enterprise (SME) segment of the non-financial business economy in Europe comprises over 20 million enterprises. SMEs are defined as micro, small and medium enterprises with up to 250 employees. The main factors determining whether a company is an SME and whether it is a micro, small or medium SME are number of employees and either turnover or balance sheet total.



	Employees	AND	Turnover	OR	Balance Sheet Total
Micro	< 10		< € 2 m		< € 2 m
Small	< 50		< € 10 m		< € 10 m
Medium	< 250		< € 50 m		< € 43 m

While this study focuses primarily on the SME segment, reference is also made to large enterprises. Large enterprises refer to the balance of the private sector enterprise population or non SMEs, namely those employing greater than 250 people.

	Employees	AND	Turnover	OR	Balance Sheet Total
Large	> 250		> € 50 m		€ 43 m

2.2 COUNTRIES INCLUDED IN THE STUDY

The countries selected for review include Germany (DE), Sweden (SE), Netherlands (NL), Portugal (PT), Spain (ES), France (FR), Ireland (IE) and the UK (UK). These countries were selected as their national economies and relative SME performance are sufficiently diverse to support useful comparison but are also broadly representative of the European economy. These eight countries, hereafter referred to as the EU-8, represent just over half (53%) of the total SME population across the EU-27, just under 60% of total employment and account for 70% of the total value added generated within the EU-27. In other words, within the EU-8 there were 10.9 million SMEs employing 51.6 million people and generating value added of €2.4 trillion.

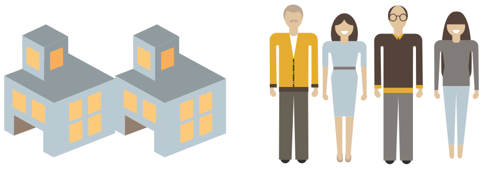
2.3 METHODOLOGY

The methodology adopted for this study included consolidating data and information from a number of EU and national level reports and databases. This desk based exercise was supplemented with interviews with Mazars' experts across the countries selected for review. A full listing of the references used in this study are set out in Section 8.

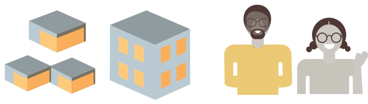
3. KEY FACTS - A CROWDED AND COMPETITIVE MARKETPLACE

3.1 A EUROPEAN SME IS ONE OF OVER 20 MILLION ENTERPRISES

In 2013 the total non-financial business economy comprised nearly 21 million enterprises which can be subdivided into two categories:



Large enterprises or those employing
> 250 people
(approximately 44 thousand in total)



SMEs or those employing
< 250 people
(approximately 20.6 million in total)

THE SME SEGMENT

The SME segment represents 99.8% of the total population of enterprises in Europe. This segment employs 87 million workers and generates €3.4 trillion in value added to the economy. Thus the SME segment employs two thirds of the total workforce and generates approximately 58% of total gross value added[1] within the non-financial business economy.

Source: Eurostat (2013) The Structural Business Statistics Database.

This total enterprise population, including both SMEs (20.6 million) and large enterprises (approximately 44 thousand), is broken down in further detail for each of the individual countries in Table 1.

Table 1: Number of Enterprises by Size Class

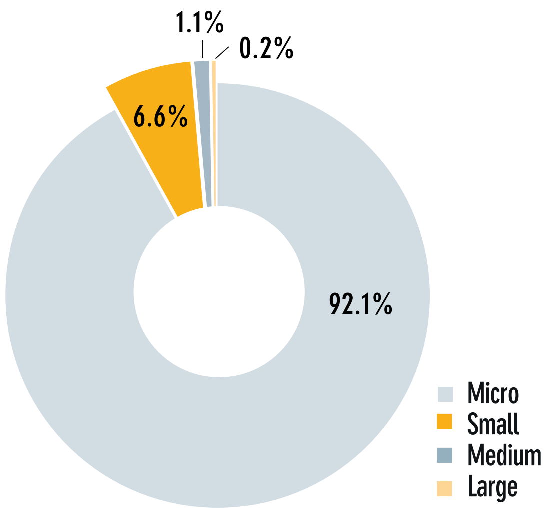
	DE	ES	FR	IE	NL	PT	SE	UK	EU-8	EU-27
Micro	1 809 659	2 106 499	2 368 958	125 474	627 609	757 093	638 361	1 453 811	9 887 464	19 025 518
Small	334 803	121 119	128 306	14 577	45 007	36 026	29 112	141 442	850 392	1 362 643
Medium	57 252	15 502	20 462	2 566	8 431	5 361	4 928	25 135	139 636	225 952
Total SME	2 201 715	2 243 120	2 517 725	142 618	681 047	798 480	672 401	1 620 388	10 877 493	20 614 113
Large	11 023	2 736	4 526	458	1 523	763	1 035	5 870	27 933	44 021
Total Population	2 212 738	2 245 856	2 522 251	143 075	682 570	799 243	673 436	1 626 258	10 905 426	20 658 134

Source: Eurostat (2013) The Structural Business Statistics Database

THE MICRO SME SEGMENT

The Micro SME segment, those employing less than 10 people, dominate the landscape across the EU-27. Very few SMEs grow beyond the micro stage. Across the EU-27 approximately 92% of companies have fewer than 10 employees. This is a universal story across individual countries. The German market however, is unique for a number of reasons, not least its size profile, with a significantly lower share of micro companies than its European counterparts.

1 Gross value added is the revenue of an entity or country less the direct costs associated with production without an allowance for depreciation or fixed costs.

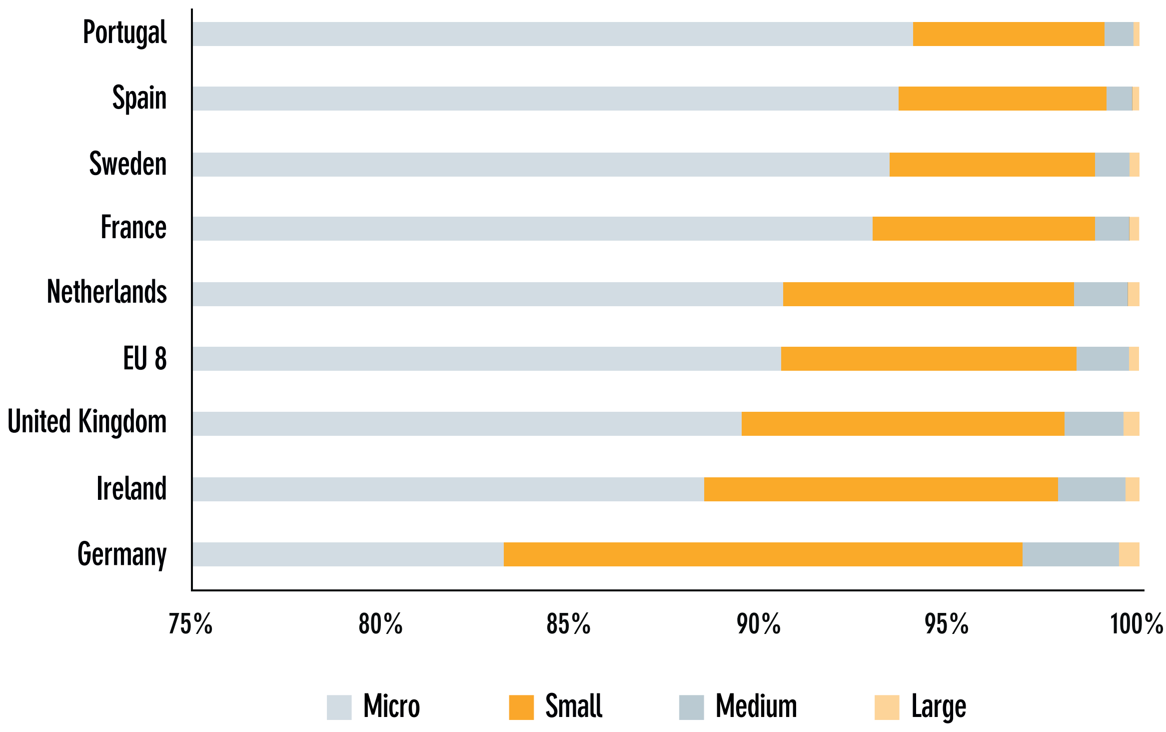


Source: Eurostat (2013) The Structural Business Statistics Database

Figure 1: SME Enterprises Split by Size

This pattern of the dominance of micro SMEs within the SME population is broadly similar across the EU-27 and the eight countries selected for review. However, Germany's "Mittelstand" model of SME companies stands out with over twice as many small and medium sized enterprises (17.8%) in comparison to the EU-27 average (7.7%) or conversely a much smaller share of micro businesses at approximately 10% lower than the average across the other 7 countries reviewed. While Germany is a definite outlier, the Irish and UK SME segments also have a slightly lower proportion of micro SMEs.

Figure 2: SME Enterprises Split by Size within Each Country



Source: Eurostat (2013) The Structural Business Statistics Database

3.2 SME - CONTRIBUTION TO EMPLOYMENT AND GROSS VALUE ADDED

The SME contribution to total employment varies from a share of 52% in the UK to 79% in Portugal. The SME segment is significantly more important in terms of employment in Spain (75%), Portugal (79%) and Ireland (70%). While the SME sector also contributes significantly more to gross value added in both Spain (65%) and Portugal (69%), the contribution of SMEs to gross value added is much lower in Ireland at only 50%.

	Ireland	Spain	Portugal
SME Employment	70%	75%	79%
Gross Value Added	50%	65%	69%

The high reliance on the SME segment in Spain and Portugal for employment may be a concern for the following reasons:

- **The continued downward trend in domestic demand** within both countries.
- **A continued downward trend in employment within the SME segment** (likely to further impact domestic demand).
- **A downward or stagnant trend in gross value added** within the SME segment.
- Portugal and Spain are **below the EU-27 in terms of involvement in value added activities**.
- Portugal and Spain are also **below the EU-27 average across all three value added indicators** of share of high tech manufacturing, share of high and medium to high tech manufacturing and share of knowledge-intensive services.

The SME segment appears less important to the overall gross value added terms in those economies where there is a higher share of large enterprises. The SME contribution to gross value added varies from a share of 50-54% in Ireland, the UK and Germany to a share of 60-70% in the Netherlands, Spain and Portugal. The lower contribution to gross value added by Irish SMEs has been put down to lower labour productivity as many Irish SMEs are small non-exporters reliant on the domestic economy. This has been very weak since 2008 and the Irish government's focus on attracting foreign direct investment has resulted in a greater contribution of larger firms to overall gross value.

Table 2: Percentage Share of SME Contribution

	DE	ES	FR	IE	NL	PT	SE	UK	EU-8	EU-27
Enterprises	99.5%	99.9%	99.8%	99.7%	99.8%	99.9%	99.8%	99.6%	99.7%	99.8%
Employment	62.3%	74.8%	63.6%	69.9%	66.5%	79.2%	64.9%	52.3%	63.1%	66.6%
GVA	54.2%	64.8%	58.2%	50.3%	63.8%	68.6%	57.7%	49.8%	56.2%	57.8%

Source: Eurostat (2013) The Structural Business Statistics Database

Table 3: Absolute Share of SME Contribution

	DE	ES	FR	IE	NL	PT	SE	UK	EU-8	EU-27
Enterprises (million)	2.20	2.24	2.52	0.14	0.68	0.80	0.67	1.62	10.88	20.61
Employment (million)	16.43	8.00	9.33	0.76	3.56	2.36	1.97	9.30	51.70	87.09
GVA (billion)	765	285	505	39	191	49	108	460	2,402	3,430

Source: Eurostat (2013) The Structural Business Statistics Database

Table 3 shows the population and contribution to employment and gross value added in absolute terms. The population ranges from approximately 140,000 enterprises in Ireland to over 2 million in Germany, Spain and France.

Large Enterprises – Contribution to Gross Value Added

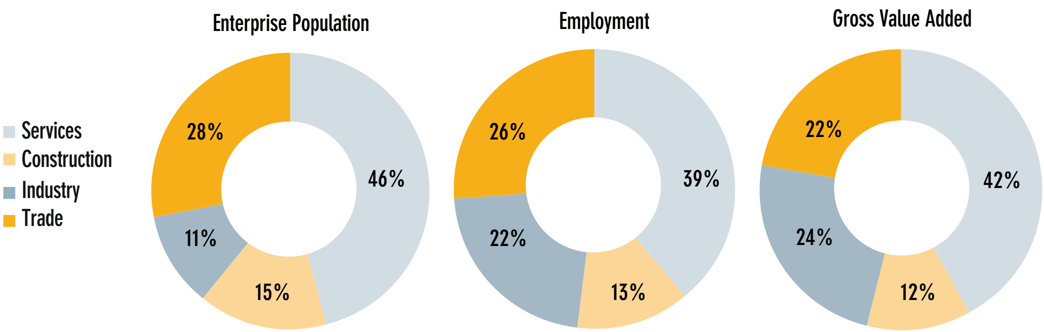
Approximately 1% of the total number of enterprises generates 60% of total value added. Only 44 thousand large enterprises (0.2% of the total enterprise population) generate approximately 42% of total private sector value added. While the overall population of large companies is very low across all countries this small share of companies represents a significant contribution to value added. When medium SMEs are added to the mix, this total population of 270 thousand enterprises (or just over 1% of the total enterprise population) generates 60% of total value added.

Germany, the UK and Ireland have a higher share of large enterprises than their European counterparts. Their contribution to value added is particularly stark, with this small share of organisations generating almost half of total value added. In Germany 45.8% of the gross value added is generated by large enterprises (0.5% of the total population). In the UK just over half of the value added (50.2%) is generated by large enterprises (0.36% of total enterprises) and just under half of gross value added (49.7%) in Ireland is generated by large enterprises (0.32% of total enterprises). This significant contribution of larger companies to gross value added equally holds true for those countries with a lower percentage of large companies.

3.3 INDUSTRY SECTORS

A significant number of SMEs (45.9%) across the EU-27 are involved in the services sector. These service-oriented SMEs employ 39.1% of all employees and contribute 41.5% to total gross value added within the SME segment. The charts in Figure 3 depict the sector split across the EU-27 in terms of population, employment and gross value added. They highlight, for example, that while a significantly lower proportion of enterprises are involved in industry they provide a significantly higher relative contribution to employment and to gross value added.

Figure 3: SME Contribution by Broad Sector



Source: Eurostat (2013) The Structural Business Statistics Database

While the services and trade sectors appear to provide less of a return to gross value added in relation to the size of their active proportion in the sector, construction provides a more consistent contribution of 12-15% across all indicators – numbers active in the sector, persons employed and gross value added.

Across the EU-27 while 11% of enterprises are involved in the industry sector, these enterprises represent double that contribution to employment (22%) and to gross value added (24%). This is likely to be due to the higher preponderance of larger SMEs within the industry sector. Thus a higher share of enterprise involvement in industry sectors, mainly manufacturing, should in theory provide a larger return in terms of employment and gross value added to the national economy.

A more in-depth analysis of the sectoral profile shows that there are some significant variations in terms of sectoral spread when viewed on a country by country basis. Spain, and to a slightly lesser extent, Portugal, has a significantly higher share of enterprises represented in trade than the other countries in the EU-8.

Table 4: Sectoral Split of SME Segment – Number of Enterprises

	DE	ES	FR	IE	NL	PT	SE	UK	EU-27
Industry	9.8%	8.3%	10.1%	3.1%	7.3%	9.3%	9.1%	7.7%	10.8%
Trade	26.8%	32.3%	24.1%	26.0%	26.5%	29.9%	19.6%	21.4%	28.5%
Services	52.1%	48.9%	45.0%	53.0%	48.8%	49.2%	57.0%	55.6%	45.9%
Construction	11.2%	10.4%	20.8%	17.9%	17.4%	11.6%	14.2%	15.3%	14.8%

Source: Eurostat (2013) The Structural Business Statistics Database

Table 5: Sectoral Split of SME Segment – Number of Employees

	DE	ES	FR	IE	NL	PT	SE	UK	EU-27
Industry	22.2%	17.0%	20.5%	12.4%	14.4%	24.9%	20.1%	16.4%	22.3%
Trade	25.9%	28.7%	24.0%	32.1%	28.5%	27.0%	23.1%	21.9%	25.9%
Services	41.8%	42.1%	40.1%	49.5%	45.6%	33.4%	42.7%	50.5%	39.1%
Construction	10.1%	12.2%	15.4%	6.0%	11.5%	14.7%	14.1%	11.2%	12.7%

Source: Eurostat (2013) The Structural Business Statistics Database

Table 6: Sectoral Split of SME Segment – Gross Value Added

	DE	ES	FR	IE	NL	PT	SE	UK	EU-27
Industry	25.5%	23.5%	19.4%	22.2%	19.8%	27.5%	22.0%	18.7%	24.3%
Trade	23.3%	23.9%	21.8%	28.5%	26.3%	25.5%	20.2%	18.5%	22.5%
Services	42.7%	39.2%	44.9%	44.2%	42.2%	34.4%	46.3%	49.8%	41.5%
Construction	8.4%	13.5%	13.9%	5.1%	11.7%	12.6%	11.6%	12.9%	11.7%

Source: Eurostat (2013) The Structural Business Statistics Database

The gross value added contribution of the sectors demonstrates the importance of individual sectors to the respective economies.

- Industry contributes more to gross value added in percentage terms in Portugal and Germany than the EU average. The gross value added contribution of Irish firms is, however, near the average despite the small proportion of firms active in industry.

- Trade is of significantly more importance in Ireland than in other European countries at approximately 6% greater than the EU average contribution to gross value added.
- The services industry is of particular importance to both the UK and Sweden in terms of contribution to gross value added. The gross value added for the UK is approximately 8% higher than the EU-27 average and the gross value added for Sweden is approximately 5% higher.
- Construction – comparing the relative contributions of the construction sector also suggests some cross country disparities that may require further analysis. While at an overall EU-27 level the contribution to population, employment and value added is in the region of 12-15% across all indicators, however, within individual countries there are stark differences. Only in Spain and Portugal is the contribution of the construction sector greater in employment and gross value added terms than the contribution in population terms (number of enterprises) which may suggest productivity issues in other countries. In Ireland, while construction represents approximately 18% of the total population of enterprises, it contributes only 6% in terms of employment and 5% in gross value added, which is significantly below most other countries and the EU-27 average of approximately 10-11%.

A more granular analysis of the sectors shows that a significant proportion of SMEs across all countries are involved in three sectors, which are heavily reliant on domestic demand. The percentage of SMEs represented in construction, wholesale and retail and accommodation and food services is approximately 50% in terms of both population and employment across the EU-27. This is of particular concern in those countries where domestic demand has been low and is likely to remain so in the short to medium term. Sweden appears somewhat of an outlier in this regard with approximately 10% less participation by Swedish SMEs in these sectors relative to their European counterparts.

Table 7: Percentage Share of SME Contribution within Domestic Sectors

	IE	FR	DE	SE	NL	UK	PT	ES	EU-27
Number	54%	55%	49%	38%	50%	45%	51%	55%	50%
Employment	56%	49%	47%	44%	49%	45%	52%	53%	48%
Gross Value Added	41%	41%	35%	35%	41%	35%	44%	44%	38%

Source: Eurostat (2013) The Structural Business Statistics Database

3.4 QUALITY OF THE COMPETITION

SME performance diverged significantly across countries. While all countries and SMEs were impacted by the global financial crisis and ensuing downturn, SMEs within individual countries felt the effects in significantly different degrees. SMEs in certain countries have been impacted more severely, with significant and enduring results. An analysis of performance data highlights the strong relative performance of German and Swedish SMEs vis-à-vis their other European counterparts. It is clear that while some improvements are now emerging at a national level in terms of GDP, the SME segments within particular countries still have a long way to travel to reach the pre-crisis situation.

	Weak	Average	Strong
SME Performance	Ireland, Spain, Portugal, UK	France, Netherlands	Sweden, Germany

While the GDP outlook is now projected to improve from 2014 onwards in all countries with an upturn in the global economy, albeit to different levels, this overall metric masks to some extent the impact on the SME segment, particularly in countries such as Ireland where a significant amount of gross value added is generated by larger companies.

Germany and Sweden are the only two countries that have fully recovered and in fact exceeded their 2008 levels in terms of population, numbers employed and value added generated. Spain and Ireland were the most heavily hit in terms of decreases in numbers of enterprise, numbers employed and gross value added. Table 8 depicts the trends in the number of SMEs between 2008 and 2013. Table 9 depicts the number of people employed in SMEs and Table 10 depicts the gross value added in SMEs over the period 2008 to 2013, using 2008 as the base year for analysis.

Table 8: Trend in the Number of Enterprises (Index: 2008=100)

	2008	2009	2010	2011	2012	2013
France	100	94	108	113	107	108
Germany	100	108	110	114	115	118
Ireland	100	101	91	84	84	86
Netherlands	100	107	135	114	114	118
Portugal	100	95	110	108	104	103
Spain	100	96	94	92	85	85
Sweden	100	102	106	108	109	116
UK	100	96	95	95	97	94

Source: Eurostat (2013) The Structural Business Statistics Database

Ireland, Spain and the UK have not yet returned to their 2008 levels in terms of number of enterprises. While Germany, Sweden and the Netherlands have significantly exceeded levels reached in 2008. Growth in the Netherlands has not progressed in the same steady fashion as in Germany and Sweden. The Netherlands reached a significant post-crisis peak in 2010 before falling back significantly in 2011. Since 2013 it is now beginning to recover again. While five of the eight countries have returned to their 2008 levels in terms of the number of enterprises, this has not translated into the same levels of employment or gross value added in most countries.

Table 9: Trend in the Numbers Employed (Index: 2008=100)

	2008	2009	2010	2011	2012	2013
France	100	112	116	110	110	113
Germany	100	109	112	116	117	117
Ireland	100	88	83	83	83	84
Netherlands	100	97	98	98	97	98
Portugal	100	95	99	96	92	90
Spain	100	91	88	84	79	78
Sweden	100	94	98	102	99	103
UK	100	104	99	98	99	98

Source: Eurostat (2013) The Structural Business Statistics Database

Only Germany, Sweden and France have recovered to, or exceeded, 2008 levels in terms of total numbers employed by SMEs. Ireland and Spain have been particularly heavily hit with drops of greater than 15% on 2008 levels. Portugal is also seeing a more delayed but still significant decline in recent years.

Table 10: Trends in Gross Value Added (Index: 2008=100)

	2008	2009	2010	2011	2012	2013
France	100	92	98	97	97	98
Germany	100	102	103	112	112	115
Ireland	100	88	77	77	77	78
Netherlands	100	102	97	100	100	101
Portugal	100	95	100	97	94	93
Spain	100	85	82	80	76	76
Sweden	100	87	102	98	99	105
UK	100	83	89	95	91	89

Source: Eurostat (2013) The Structural Business Statistics Database

Germany, Sweden and the Netherlands are the only countries where gross value added has now exceeded 2008 levels. Only in Germany and Sweden did this gross value added coincide with increases in both enterprise numbers and employment levels beyond 2008 levels.

The most recent ECB SAFE survey (August to October 2013) also reflects this divergent pattern of SME performance cross-nationally. The European Commission (EC) and the European Central Bank (ECB) established the Survey on the Access to Finance of Small and Medium-sized Enterprises in the European Union (SAFE), which is now conducted across 37 countries.

The ECB SAFE survey results further highlight the relatively strong position of German and Swedish SMEs, reporting significantly higher net percentage increases in turnover (+26% in both countries) and in profit margins (Germany +6%, Sweden +11%).

3.5 A THREE-SPEED EUROPE

The strength of national economies and the quality of domestic demand has obviously been a key determinant of SME performance. Some countries had strong and sustainable national economies and solid buffers on entering the crisis, while others were in relative terms very exposed. The strength of the national economy and the ability of national governments to take countermeasures were of particular importance for SMEs, who in general are more heavily reliant on national domestic demand.

In some countries such as Ireland, Portugal and Spain, the ability of governments to intervene and allow automatic stabilisers to kick in and preserve domestic demand was significantly curtailed by weak public finances, rising government debt levels resulting from the transfer of excessive private debt levels to government balance sheets and the ensuing austerity measures. This resulted in many SMEs entering the crisis and effectively operating through it from a very weak starting point. Countries with a large share of non-exporting enterprises within the SME segment, in particular, were significantly impacted by the sharp decrease in domestic demand following the crisis and the enduring nature of this fall off. Over the last number of years SMEs have thus effectively operated in a three-speed Europe, with much stronger environments for German and Swedish SMEs.

A three-speed Europe	Slow	Average	Fast
	Ireland, Spain, Portugal	France, Netherlands, UK	Sweden, Germany

An analysis of cross country trends in GDP since 2008, with forward projections to 2014 and 2015, shows one aspect of the impact of the financial economy at national economy level.

Figure 4: Cumulative Real GDP Growth Rate (2008 – 2013) and Projections (2014-2015) (Index 2008=100)

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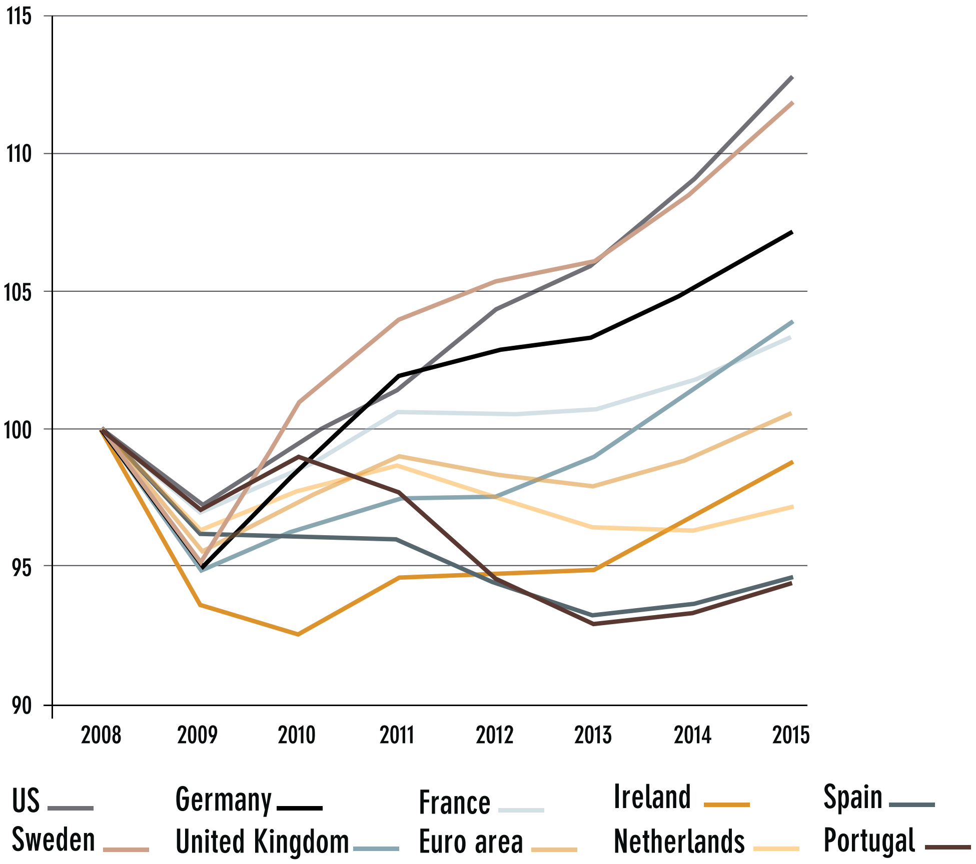


Source: OECD 2009

Most countries experienced a v-shaped dip in 2008 and 2009 with recovery from 2010 onwards, albeit that the extent of recovery varied significantly. This v-shaped dip and recovery did not occur in Ireland and Spain where the impact of the crisis was longer and more enduring.

While Portugal did experience a v-shaped recovery the impact of the crisis was somewhat delayed with a significant second drop in GDP growth from late 2009/early 2010. The Netherlands also experienced a delayed impact following initial recovery. While the Netherlands was on a recovery trajectory following an immediate v-shaped dip, performance deteriorated again in 2011 and has not yet recovered to pre-crisis levels.

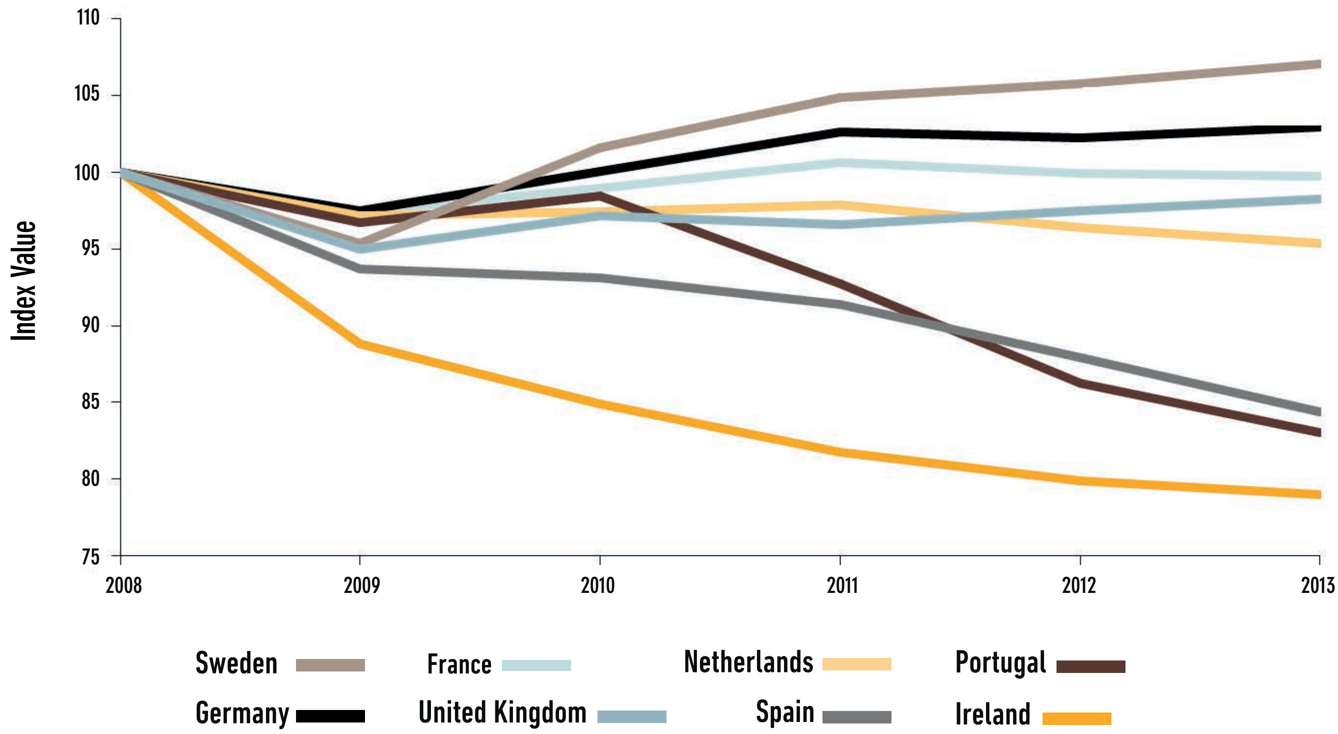
After an immediate post crisis dip Sweden, Germany, and France (as well as the US) recovered from 2010 onwards, albeit that the recovery in France plateaued at low levels for a longer period. The crisis had a more prolonged impact in the UK which has now recovered and exceeded 2008 levels, with strong growth projections into 2014 and 2015. Ireland, Spain and Portugal remained below 2008 levels in 2013. While the impact was severe and prolonged in Ireland, Spain and Portugal, Ireland has, in recent years shown some small but steady progress in contrast to a continued downward trend in Spain and Portugal. The outlook for Ireland is more positive with some forecasts suggesting that 2008 levels may be reached from 2016 onwards. However, Portugal and Spain would appear to have further and longer to travel to reach 2008 levels.

While GDP performance across most of the countries has resulted in a more recent upward trend, which is projected to improve with the upturn in the global economic environment, this has, in many cases, been fuelled by export oriented growth. However, many SMEs are active in sectors which are not export-oriented. Even where they are exporting, many SMEs are only active to a small extent and thus are wholly or mainly dependent on domestic demand which, as shown in Figure 5, remains subdued or significantly below pre-crisis levels.

Domestic demand is particularly important for the SME segment due to the large share of indigenous non-exporting SMEs in some countries. While the quality of domestic demand was only marginally impacted in some countries for a short time immediately post crisis, and either plateaued at similar pre-crisis levels (the Netherlands and the UK) or recovered to improved levels (France, Sweden and Germany), the situation in Ireland, Spain and Portugal resulted in a significant decrease in domestic demand which was sustained and remains significantly below 2008 levels. Spain, Portugal and Ireland still remain in excess of 15% below 2008 levels of demand as at the end of 2013, with Ireland and Spain experiencing early and enduring demand drop off and Portugal more latterly since 2010.

Other countries were not impacted to the same extent. In Sweden and France in particular, automatic stabilisers played their role in negating the impact on domestic demand. However, in France, some of these initiatives would now appear to be impacting competitiveness and slowing down recovery.

Figure 5: Trends in Domestic Demand (Index: 2008=100)



Source: Eurostat (2013) Annual National Accounts

3.6 COUNTRY COMPETITIVENESS IS KEY

Global competitiveness rankings are an important benchmark of national SME performance. National competitiveness is a major factor in ensuring sustained growth. Thus the relative performance of individual countries across a range of indicators provides a significant backdrop to any cross country analysis. The Global Competitiveness Report assesses the national competitiveness position of 148 economies and is the most comprehensive analysis of its type. Outlined below is a summary of the movement in the competitiveness of the EU-8 since 2011/12, with Germany and Sweden leading the field.

	PT	ES	IE	FR	UK	NL	SE	DE
2011/2012	45	36	29	18	10	7	3	6
2012/2013	49	36	27	21	8	5	4	6
2013/2014	51	35	28	23	10	8	6	4
Direction of travel	↓	↔	↔	↓	↔	↔	↓	↑

Source: World Economic Forum (2013) The Global Competitiveness Report 2013-2014

4. LEARNING FROM THE BEST SMES

HOW TO STAND OUT FROM THE CROWD

LEARNING FROM THE BEST SMES - HOW TO STAND OUT FROM THE CROWD

Success in business is about a few things going right and other things not going wrong. It is certainly not a black art. Most business issues can be controlled to an extent albeit some will involve an element of luck and timing. However with better positioning, management and a resilient balance sheet luck becomes far less important.

SMEs in some countries were hit by a double blow – on one side they were faced with a weak national economy and very poor domestic demand, and on the other side they were hit with weak balance sheets and unsustainable funding structures on entering the crisis. In early 2014, with a more positive global outlook, improvements are now emerging at a national level in terms of GDP. However, the SME segments within particular countries still have a long way to go to reach the pre-crisis situation. While some of this success is due in no small part to the national economy and quality of domestic demand – which are outside the control of individual SMEs - a number of other dimensions will require enhanced focus at individual SME level and at national policy level.

This study has identified six key success factors to support SMEs reach the bar of superior performance and stand out from the crowd

- ✔ Maintain a sharp focus
- ✔ Bring more to the party
- ✔ Build resilience and financial discipline
- ✔ Right size your organisation
- ✔ Increase your international outlook and extend your geographic footprint
- ✔ Manage for today and lead for tomorrow

4.1 MAINTAIN A SHARP FOCUS

It is increasingly important that SMEs are very clear on their target position within the sector in which they decide to operate and have a very strong understanding of the dynamics and changes within that sector. Certainly the recent experiences of many SMEs involved in sectors such as construction and retail serve as stark lessons in terms of positioning, understanding and predicting market trends and risk management.

The best SMEs internationally have proved that such focus is key. Hermann Simon, author of "Hidden Champions: Aufbruch nach Globalia" describes this sharp focus as one of the key ingredients of the German "Hidden Champions", mid-sized market leaders in their respective world markets. These companies define their markets narrowly, know their markets and the market dynamics intimately and work deep into the value chain. They are pragmatic in terms of balancing focus and depth with their scale. While they outsource they adopt an anti-outsourcing approach to their core competencies to ensure total quality control and focus on being the best or world class. While not every SME will be looking to be an international player or indeed leader, even local and regional players need to understand how they add value and differentiate themselves within markets. A local retailer for example can differentiate itself by selling local produce or in the words of one commentator "Don't keep making hamburgers when a McDonald's comes to town. Sell something else"[2].

2 Sun, L Impact of Globalisation on Small Business http://www.businessdictionary.com/article/583/impact-of-globalization-on-small-businesses/

Learnings

For some there will have to be hard choices in terms of sector and market position, particularly those that have not taken a long term and strategic approach to markets and market position. Across the EU-27, half of SMEs in terms of both number and employment are involved in three sectors which are heavily reliant on domestic demand - construction, wholesale and retail, and accommodation and food services. Due to the significant proportion of SMEs operating in these traditional sectors and in particular those countries where domestic demand remains low or has stagnated, many SMEs are operating in a very competitive space where organic growth will be difficult and hard choices will have to be made. These choices may include:

Repositioning the Product or Service Offering

SMEs may seek to reposition their product or service offering to other target customers, for example, budget versus high end.

Consolidation with Others

Organisations may benefit from economies of scale and purchasing power through consolidation with others at a regional or national level. As a very broad rule of thumb larger organisations are more successful in securing finance. Therefore, consolidation for size and growth may in itself be a medium to long term strategy for supporting improved access to credit.

Alignment with National and Regional Strategies and Initiatives

There are gains to be leveraged from participation in industry or sectoral clusters. For example, accommodation and food service operators need to ensure they are aligned with tourism strategies and initiatives to enhance visitor numbers, durations of stay and levels of spend.

Small Does Not Necessarily Mean Simple

92% of SMEs across the EU-27 are micro SMEs. An important area of focus should be to ensure that best practices in terms of business models, operational efficiency, technology and management practice become part of the DNA of this important cohort of SMEs.

Agility Reaps Rewards

While SMEs are often seen to be at a disadvantage in terms of scale and structure in comparison to larger firms that generally have more access to capital, larger teams of specialists, economies of scale and more ability to take risks within larger and diversified portfolios, there are also benefits for SMEs in terms of agility. Often SMEs are able to react quicker to fast changing market and customer requirements, are closer to their customers, develop stronger personal relationships with their clients and make decisions quicker than larger firms.

4.2 BRING MORE TO THE PARTY

In some countries the SME model of operation is still very traditional. It is based on a simple shop, service, trade or profession with very little value added through brand, technology and unique know how. For economies to compete and succeed a larger portion of SMEs will need to bring more value to what they do.

The most recent Innovation Scoreboard (2013) reports that innovation performance has improved across Europe despite the long term economic crisis. However, it points out that gaps in relative performance are nonetheless widening across Member States, with front runners, the innovation leaders, significantly improving their performance while others show more limited or little progress. Germany and Sweden again lead the field here with Spain and Portugal lagging behind on innovation.

Innovation Cluster	Position of 8 countries	Other countries in Europe
Innovation leaders (Above EU average)	Germany, Sweden	Denmark, Finland
Innovation followers (Close to EU average)	Netherlands, UK, Ireland, France	Luxemburg, Austria, Slovenia, Cyprus and Estonia
Moderate Innovators (Below EU average)	Spain, Portugal	Italy, Czech Republic, Greece, Slovakia, Hungary, Malta and Lithuania
Modest Innovators (Well below EU average)	N/A	Poland, Latvia, Romania and Bulgaria

The SME Performance Review (ECorys, 2012) suggests that one of the reasons that SMEs in certain countries have recovered to their 2008 levels of gross value added and employment was due to their strong position in high tech and medium tech manufacturing and having strong knowledge-intensive services.

Table 11: Share of High Tech and Medium to High Tech Manufacturing and Knowledge-Intensive Services

	SME Population (Total Number)	High Tech Manufacturing (% of Total)	High and Medium to High-Tech Manufacturing (HMHTM) (% of Total)	Knowledge-Intensive Services (KIS) (% of Total)	Total Share HMHTM and KIS
Netherlands	626 066	0,3	1,3	30,9	32,2
UK	1 648 933	0,4	1,5	29,1	30,6
Sweden	555 160	0,3	1,6	25,7	27,3
Ireland	154 484	0,1	0,4	23,4	23,8
Germany	2 086 667	0,4	1,6	21,3	22,9
EU-27	20 703 172	0,2	1,2	20,9	22,1
Portugal	749 827	0,1	0,6	20,1	20,7
Spain	2 470 979	0,1	0,7	18	18,7
France	23 777 297	0,2	0,7	16	16,7

Source: eCorys 2012

As Table 11 suggests France, Portugal and Spain are below the EU-27 average across all three indicators – share of high tech manufacturing, high and medium to high tech manufacturing and knowledge-intensive services. Germany, Sweden and the UK are leaders in high-tech and medium to high-tech manufacturing, with the Netherlands performing close to the average across the EU-27. The Netherlands leads with the highest proportion of knowledge-intensive services followed by the UK. While Germany has a strong competitive advantage in high tech manufacturing, its share of knowledge-intensive services places it further down the rankings but still marginally above the EU average.

Learnings

The SME Performance Review, as well as the analysis within this report, strongly suggests that innovation has become critical if not the most important thing for business sustainability and growth. On the one side competition is increasing through greater globalisation and the growing application of smart strategies by leading SMEs. On the other side there is a much more discerning and demanding consumer base, both across the B2B and B2C segments. More SMEs need to focus on these smart strategies which will increasingly become the minimum performance benchmark. This will require innovation in products, innovation in business models, innovation in process for speed and cost efficiencies, and innovation through technology - placing technology at the heart of the business to ensure a competitive advantage.

Increasing and sustaining employment and gross value added particularly in those countries that have not yet reached pre-crisis levels will require SMEs to become more competitive through enhanced innovation. In some cases and particularly in smaller markets, this may require consolidations and mergers of existing SMEs, significant repositioning within markets or enhanced policy focus and support to ensure that smaller SMEs can avail of innovation opportunities, including the specific SME measures under the Horizon 2020 framework.

4.3 BUILD RESILIENCE AND FINANCIAL DISCIPLINE

The attitude of the private sector to bank borrowing from one country to the next was remarkably different. SMEs in some countries would appear to have been naturally cautious; some were open and neutral; while others took on borrowing with what appears in hindsight to be reckless abandon.

The national psyche would appear to have been, to some extent, influenced by previous experience. In Sweden, for example, the previous national crisis in the 1990s has resulted in what has been described by our experts as a very cautious and reasoned approach to taking on debt. Thus Swedish SMEs were already better positioned on entering the crisis. Dutch SMEs were also considered to be cautious; while access to finance has more recently become a significant issue this appears to be due to a lack of supply, with little sign that Dutch SMEs were overleveraged on entering the crisis. Similarly, German SMEs had also progressively improved their equity ratios over a number of years leading up to the crisis.

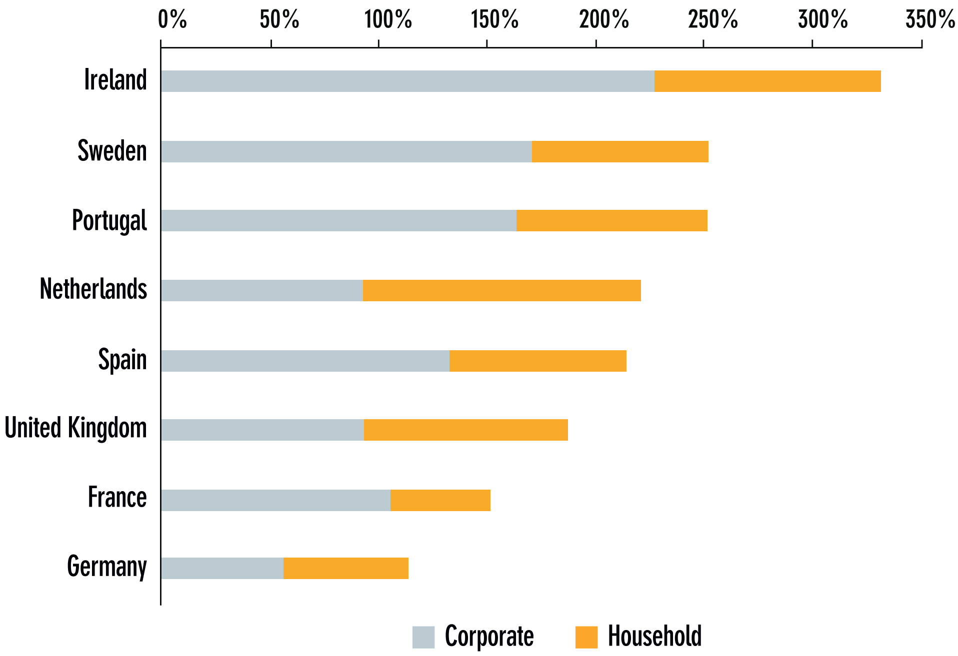
During the boom and with strong turnover and profit generation some SMEs had built up strong financial reserves, which strengthened their positions for more difficult times. SMEs with strong buffers were able to withstand early losses at the peak of the financial crisis and were in a stronger position to invest in repositioning and leveraging new opportunities during the crisis where necessary. They were able to utilise retained earnings to subsidise short term losses due to declines in revenue and increasing bad debts and were also able to fund increases in debt payment cycles due to later payments by customers. Overall there were strong patterns at country level with German and Swedish SMEs in a relatively stronger position.

	Weak	Average	Strong
SME Resilience/balance sheet strength	Ireland, Spain, Portugal,	UK, France, Netherlands	Sweden, Germany

There is little comparable cross-country data on SME borrowing levels and balance sheet strength. While survey data does provide some comparative information on SME financial strengths and needs, the absence of balance sheet data from reporting SMEs limits the analysis somewhat.

Equally, while non-financial corporation debt levels are sometimes used to suggest excessive private sector borrowing, this does not present an appropriate picture of SME borrowing at a national level. This can be distorted by the debt of large multi-national corporations which has been said to explain the high debt levels in Sweden and, indeed, in Ireland. However, it is important to note that overall corporate debt (non-financial corporations) as a percentage of GDP was lowest in Germany, which suggests that at least here there was little systemic risk either at overall level or within the SME population. Sweden appears an outlier with corporate debt levels similar to Ireland, Portugal and Spain. A recent OECD analysis has however suggested that this is not as large a problem as in other countries for a number of reasons. Firstly, this debt can be attributed to the large number of multi-national companies operating in Sweden but with a debt not directly linked to the Swedish economy. Secondly, the debt to asset and debt to equity ratios within the corporate sector are below the EU average and have been respectively stable and decreasing over the last ten years.

Figure 6: Outstanding Debt



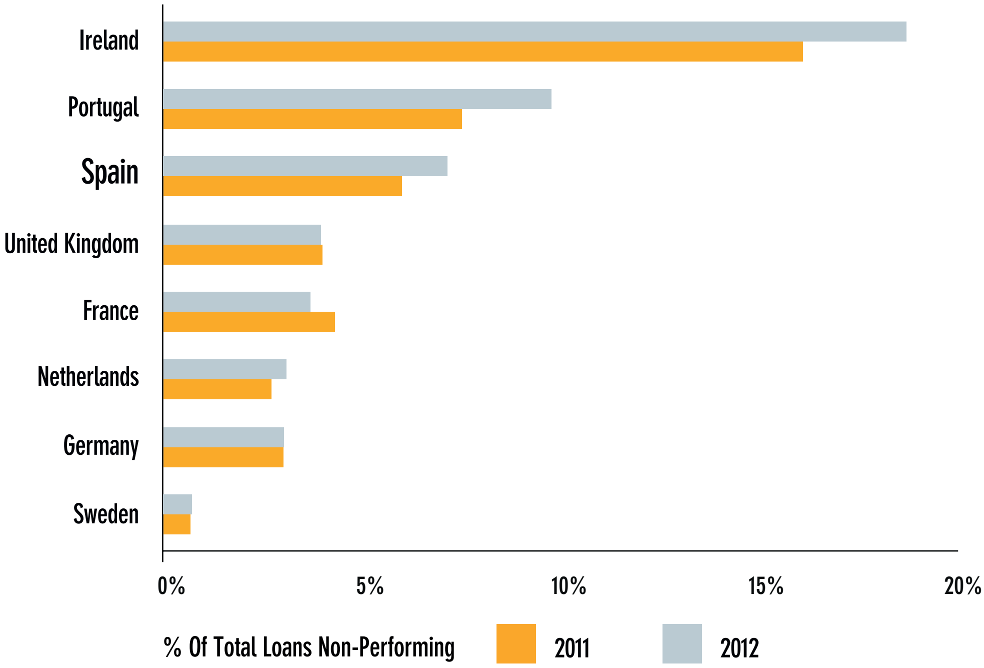
Source: Eurostat

In a European Commission Working Paper "Exploring the steady-state relationship between credit and GDP for a small open economy" (EC, 2013), the authors note the emergence of a "twin club" development across Europe. They note that while Irish credit growth increased markedly over the past 10 years, some other European countries also experienced significant increases. This constituted what they called a twin club being Ireland, Spain, Portugal, the UK and the Netherlands which experienced significant increases in credit growth, while in other countries the growth in credit was at much lower levels.

For those countries with high levels of financial debt the ratio of private sector corporate credit to GDP was around 200% by 2010, following a period of sustained growth in the ratio, mainly from about 2003 onwards. While the other countries including Germany and France also experienced growth, it was at much lower levels - a ratio of approximately 100% by 2010.

A useful proxy of balance sheet strength of non-financial corporations is the level of non-performing loans. This picture highlights the extent of ancillary and in some cases reckless borrowing in certain countries. The crisis and the ensuing economic downturn have resulted in a significant increase in the number of non-performing loans in some countries. While this data has to be approached with some level of caution due to the different assessments and approaches adopted by banks within individual countries, it does present patterns which would be consistent with anecdotal and expert analysis of the situation. Ireland, Portugal and Spain show cause for concern in relation to non-performance. Repairing bank balance sheets will remain critical to support increased lending and support economic growth for certain countries.

Figure 7: Non-Performing Loans



Source: World Bank

However, while much of the debate now centres on the question of access to funds for SMEs, there is also a deeper issue. Leading up to the crisis the source of funds would not appear to have been an issue with a high level of credit availability and private borrowing for both households and corporates. This rise in private debt was not generated by sound economic fundamentals but rather fuelled by excessive credit growth. The problem in hindsight, therefore, rests not with the availability of funds but with the application of those funds. In certain countries and in particular Ireland, Spain and Portugal the corporate sector applied a lot of resources that in hindsight were based on inadequate thinking, foresight and risk management.

Financial discipline and a focus on investing in the core business is a hallmark of success particularly for the SME segment in countries such as Germany and Sweden. SMEs in many other countries were distracted by ancillary or non-core business investments, in particular property. While the impact of this has been widely debated in terms of the residual debt overhang post crisis, the time spent on ancillary speculative investments pre-crisis and the management of the post-crisis debt has in many cases been a costly if not critical distraction from developing and managing the core business. Many SMEs, in particular those in Spain, Ireland and Portugal, are likely to have lost years of focused and proactive developmental investment in their core business.

It is also clear that in many countries a significant portion of SMEs scaled up significantly before the crisis to service high levels of domestic demand, stimulated by the boom, the ready availability of credit and low interest rates. This is a particular issue in Spain, Portugal and Ireland where many SMEs are now servicing debt associated with an over-scaled capital base, in the context of very significant drops in domestic demand.

Working capital management is a key aspect of financial resilience and sustainability at any time, but particularly during a prolonged downturn such as this. Some indicators, particularly from survey evidence, suggests that working capital is a more significant issue in some countries than in others. Evidence from the Bach database suggests that measured as a percentage of turnover the weight of working capital requirements is relatively small in Germany and France and much higher in Spain and Portugal.

Significant variations in the use of short term financing also suggests disparity in terms of working capital management practices. Irish SMEs are significantly more reliant on bank overdrafts, credit lines or credit card overdrafts. Sixty per cent of Irish SMEs used this method of financing in the last six months, significantly higher than the EU-28 average of 39%. On the other hand there was a relatively low use of overdrafts by Swedish SMEs, indeed 80% had never used this source of financing as it was not considered suitable for their business.

	IE	NL	UK	FR	EU-28	PT	DE	ES	SE
Used bank overdraft, credit line or credit card overdraft in the past 6 months	60%	47%	45%	42%	39%	36%	36%	34%	7%

Source: European Commission SAFE Survey

Irish SMEs and UK SMEs are significantly more reliant on trade credit than their European peers. In particular usage levels of trade creditors in Sweden, France and Germany were significantly lower than in Ireland and the UK.

	IE	UK	ES	EU-28	PT	NL	SE	FR	DE
Used trade credit in the past 6 months	64%	60%	42%	32%	30%	29%	21%	17%	15%

Source: European Commission SAFE Survey

As overdrafts and trade credit are essentially short term funding sources, this pattern of high reliance does suggest some sign of financial fragility. It is interesting to note that German and Swedish SMEs are strong on both indicators and well below the EU-28 average in both cases. Portugal appears an outlier as it is strong on both indicators (marginally below the EU-28 average), although Portuguese SMEs show signs of financial fragility on many of the other indicators.

While the above suggests that SMEs, particularly those in certain countries may need to ensure an enhanced focus on improving working capital management, some of it is also systemic at a country level. Late payments can cause significant financial problems for small businesses and create an extended need for financing, particularly working capital financing. Average payment delays vary significantly across Europe. The following table outlines the average payment days across the eight countries reviewed.

	SE	DE	NL	UK	FR	IE	PT	ES
Average payment days	35	35	43	44	57	66	90	97

Source: Intrum Justitia (2012) European Payment Index 2012

Learnings

In many countries some of the important aspects of the company's affairs, for example financial discipline, a resilient balance sheet, a sustainable funding plan and tight working capital management, were in many cases never formally managed or monitored prior to the crisis. Such lessons emerging from the recent crisis must not only be learned but also hardcoded into practice for future generations.

The access to finance debate, which is very prominent for the SME segment, must also however focus on the lessons learned from the financial crisis to ensure SMEs have adequate funds for their business in the long-term. SMEs should ensure that their working capital policies and procedures are rigorous, including having clear guidelines on how to accept or reject new customers, price negotiation and credit terms in an effort to reduce the prospect of excessive bad debts and cashflow difficulties.

Furthermore, it may also be useful to do business in overseas territories where settlement patterns are better than the local market.

4.4 RIGHT SIZE YOUR COMPANY

The analysis would certainly suggest that the size of a company does in fact matter. We have seen that approximately 1% of total enterprises (large corporates employing greater than 250 people and medium sized SMEs employing 50 to 249 people) generate approximately 60% of value added.

Germany and the UK have approximately twice as many large enterprises in percentage terms within their overall population as the EU average and approximately four times higher than in Spain and Portugal. While the overall population of large enterprises (non-SMEs) is very small across the EU-27 and the Mazars EU-8, small differences at this level can have multiple and significant influences on the SME sector within a country, in particular with large enterprises playing a significant role as direct or indirect customers for SMEs within the domestic market. Larger firms are more likely to be exporting, exporting to a greater extent and across more geographic markets.

The higher proportion of SMEs active in the industry sector might, to some extent, explain the larger size of German SMEs. However, the profile of the German SME enterprise fabric has also been put down to a number of characteristics which may be critical to superior performance. These include the adoption of a long term view to business positioning and planning, high innovation, a strong focus on niche products that link in to global supply chains, and strong national positioning as a global player. However, while size may be a product of these success factors it may also now be an important influencing success factor itself: for example, success in internationalisation has been strongly correlated to increased size.

Learnings

While size does matter, it is not necessarily true that bigger is always better. Rather than simply big being better, the more useful lesson is to "right-size" your organisation. If a company is staying small it needs to ensure it maintains a niche focus and that it is deeply rooted in supply chains and the wider ecosystem to ensure the benefits of critical mass can be leveraged. This may involve outsourcing non-core activities and developing strong partnerships with others as an alternative to internal organic growth. SMEs must ensure that they are linked to important sectoral clusters and ecosystems to enhance value chains and remain abreast of sectoral innovations and best practice.

At a national level, the SME sector may need to be treated to some extent as a numbers game. Certainly you need as many SMEs as possible to move beyond the 'hand to mouth stage' to a level of sustainability. If a significant portion of SMEs are forward looking, developing and entering foreign markets this will build scale within the SME sector. The profile of the SME sector should increasingly become a national level policy focus including analysis of the impact of changes in the pyramid structure (micro, small and medium) on macroeconomic performance, including contribution to gross value added and GDP. A high level comparison of SME numbers at national level suggests that the different population profiles of the SME sectors within individual countries may need further attention to guide policies and choices.

Each country should strive to produce a few new truly international companies every decade. Germany, for example, has a strong track record in growing truly international mid-sized companies. It has a high number of "hidden champions", mid-sized market leaders in their respective world markets and companies that are truly international. Germany has 1,307 hidden champions - international mid-sized companies that are leaders in their fields. These hidden champions are thought to account for approximately 25% of German exports and have experienced annual growth rates of about 10% in the last decade. They have adapted to changes in global markets including the stagnant economies of Europe and the US by becoming truly global. While a decade ago the German Hidden Champion's revenue came from Europe and the USA, approximately 75% is now coming from Europe, Eastern Europe and Asia.

4.5 INCREASE INTERNATIONAL OUTLOOK AND EXTEND THE GEOGRAPHIC FOOTPRINT

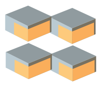
While there is limited useful comparative data on SME export performance, the evidence does tell us that in general far too few SMEs export and where they do export, they do not export to any great extent. There is a general consensus across the published literature that certainly the German 'Mittelstand' appears to stand out in terms of export participation and the extent of that participation in value terms. Many of the barriers to internationalisation for SMEs, identified at an overall level and repeated within national studies suggest that these are not only barriers to exporting but rather barriers associated with the fundamentals of the business – market position, innovation and a strategic approach to management.

Most commentators and national studies on exports accept that more SMEs need to export. However, for many this will increasingly become a necessity as opposed to a choice, especially in countries where domestic demand has been low and is projected to remain stagnant in the short to medium term.

There is limited useful comparative data on SME export performance across countries. At an overall economic level, while exports as a percentage of GDP growth provide some indication of trend level performance over time by country, they mask significant differences in terms of the enterprise fabric with small open economies, such as Ireland and Luxembourg that are influenced significantly by the high proportion of large multi-nationals. Larger economies such as the UK, Germany and France show much lower percentages of export growth.

In 2009 the European Commission conducted a study to map the level of internationalisation of European SMEs which analysed all activities that put SMEs into a meaningful business relationship with a foreign partner: exports, imports, foreign direct investment, international subcontracting and international technical co-operation. The survey involved 9,480 SMEs in 33 European countries. It found that across the EU-27 one in four SMEs export or had exported at some point during the last 3 years, with international activities mostly geared towards other countries inside the EU and only about 13% of EU SMEs active in markets outside the EU.

The European Commission study also found that:



	Internationally active SMEs	NON Internationally active SMEs
EMPLOYMENT GROWTH	+ 7%	+ 1%
INTRODUCE NEW PRODUCTS OR SERVICES	+ 26%	+ 8%

ONLY 16% of SMEs are aware of public support programmes for internationalisation

Most SMEs started international activities by importing: SMEs that both import and export started with importing twice as often (39%) than exporting (18%).

A more recent report within the UK by The Select Committee on Small and Medium Sized Enterprises (2012) noted that only one in five UK SMEs export, fewer than the EU average of one in four. The study suggested however that this was broadly similar to larger economies such as Germany and France and was likely to be due to the fact that SMEs in smaller countries are more likely to have local or regional sales which cross land borders due to the smaller geographic scope.

However, the number of enterprises exporting can also mask significant differences in the level of exports by SMEs. The French Study (Trésor Economics 2009) also highlights this issue. While a significant proportion of France's export population were independent SMEs, their share of exports was extremely small with a very small number of large firms representing approximately 70% of export revenues. Many of the independent firms were found to have short and small forays into the international markets often limited by their small size, limited innovative capacity, a tendency to target a limited number of often neighbouring countries and often not retaining or building on market share in new geographies. The study again differentiated the German SME segment which it described as larger, more innovative, with bigger and more regular exporters with exports accounting for a larger share of revenues.

The success of the German experience has been put down to a number of factors:

- **The dominance of industry,** a highly export oriented sector, in the German SME population.
- The presence of a number of **large industrial enterprises** within the German SME population.
- The lead enjoyed by German firms, and especially German SMEs, in terms of **innovation**.
- The lower level of micros and consequently **higher number of larger SMEs**.
- A strong and **growing track record in emerging markets**.
- **A highly ambitious and competitive national psyche** as evidenced in the high presence of truly international companies – Germany has approximately half of the total number of hidden champions – international mid-sized companies that are leaders in their field.

Learnings

While many studies reiterate the challenges and barriers to internationalisation faced by SMEs, it is arguable that many of these barriers are not barriers to internationalisation per se but in fact barriers to successful performance (See Table 12 below Internationalisation Barriers Ranked by SMEs). By addressing the fundamentals of performance including understanding and defining your markets appropriately and taking management time to develop strategies to support follow through on these issues, internationalisation becomes a natural consequence as opposed to an objective in its own right.

With the German economy and in particular the German SME segment, the 'Mittelstand' standing out as a leading performer there are certainly lessons for other countries and their SME segments.

OECD research on internationalisation (OECD 2009) identified ten top barriers to internationalisation for SMEs, barriers which appear to be repeated across many national surveys and reports on internationalisation.

Table 12: Internationalisation Barriers Ranked by SMEs

Rank - Weighted Factor	Barrier to Internationalisation	Rank - Weighted Factor	Barrier to Internationalisation
1	Shortage of working capital to finance exports	6	Lack of managerial time to deal with internationalisation
2	Identifying foreign business opportunities	7	Inadequate quantity of and/or untrained personnel for internationalisation
3	Limited information to locate/analyse markets	8	Difficulty in matching competitors' prices
4	Inability to contact potential overseas customers	9	Lack of home government assistance/incentives
5	Obtaining reliable foreign representation	10	Excessive transportation costs

Many of the barriers to internationalisation identified above cross over significantly with the six key success factors outlined in this report. Many of them are not solely barriers to internationalisation but indeed challenges to successful performance. The companies that address these fundamentals to achieve superior performance are more likely to naturally turn down the path of internationalisation, as a consequence of improved performance, as much as through an objective in its own right. While some businesses will choose not to expand across national boundaries this should be as a result of a considered decision rather than due to a lack of time to work on the business. SMEs need to be more innovative if they are to succeed in competing internationally. This requires not only innovation in terms of product but also innovation in terms of business models and processes. Leveraging innovation and technology, should put more SMEs in a position to address barrier 8 (difficulty in matching competitors' prices) and barrier 10 (excessive transportation costs). For example, difficulties in matching competitors' prices will increasingly, in a global environment, require cost savings through innovation efficiencies or removing price from the equation through innovation in product and service.

As highlighted earlier in this report, the overwhelming majority of SMEs are micro SMEs employing fewer than 10 people. While some of these are small companies with a niche focus, that are linked into global supply chains, the vast majority are non-exporting SMEs that are dependent not only on domestic demand within the national economy, but also domestic demand at much more local levels. For those that choose to stay local they must ensure that they in some way stand out to be seen. This could be through leveraging local benefits such as the supply and retailing of local produce. SMEs that are involved in a simple, shop or trade service, dependent on the local economy, are likely to remain small and are at risk from unpredictable demand and the threat of new competition.

While many of these businesses may remain sustainable and successful they are subject to high sustainability threats and the risk appetite of these businesses should generally remain low. For example, many local businesses in Ireland, Spain and Portugal over-invested in the local domestic economy and ran risks far beyond their natural thresholds. In most cases they were neither leaders nor innovators in their fields but rather provided simple and repeatable products, services and business models which made them very exposed to the downturn in their domestic markets. For such businesses extension of geographic footprint may involve simple strategies such as:

- Consolidation with other providers, regionally and nationally, to achieve critical mass and economies of scale.
- Strategic partnerships with other local product and service providers where complementary benefits and relationships can be leveraged to mutual benefit e.g. cross-selling, sharing of marketing campaigns.
- Introducing best practices to extend customer reach through working with industry representative groups and national development authorities/organisations.

However, more SMEs, particularly those within national economies where domestic demand is stagnant, must extend their footprints to ensure sustainability and improve competitiveness. The extension of geographic remit, however, for most small businesses, will be far from opening overseas offices but rather rooted in better deployment of technology to enhance international marketing and sales, linking in to industry clusters including state support for growth and internationalisation.

In most countries the burden of growth and recovery through increased exports and internationalisation falls on too few SMEs. It is clear that many more SMEs will have to work through the identified barriers to internationalisation or they might find international competition coming to them instead.

4.6 MANAGE FOR TODAY AND LEAD FOR TOMORROW

In our experience the ambition, focus and simple hard work displayed on a day-to-day basis by the owners and managers of a business is probably the single most important determinant of long term success or failure. Regardless of the location, size or sector all managers have to harness **four fundamental drivers of performance in order to succeed.**

FOUR FUNDAMENTAL DRIVERS OF PERFORMANCE:

1. Market position, customer offering and selling
2. Operations and customer service
3. Finance, business performance and risk management
4. Leading and managing people and teams

While it would never be appropriate to appraise the management style and focus of any one company on the basis of its location alone, the particular business culture, history and norms of the various countries included in this survey also appear to influence the overall performance of the SME segment in their respective national markets.

Certainly many commentators have discussed the beneficial aspects of the Germanic model and style of management. Various commentators including our industry experts have suggested that a hallmark of success for German SMEs has been the core business focus and a long term approach to planning. While this long term approach to planning has been put down by some to the high proportion of family businesses amongst German SMEs - 'the Mittelstand' - broader research on national cultures (Hofstede's Dimensions of National Culture) has also pointed out that long term orientation is a unique characteristic of German National Culture. Whether Generation Y (those born after 1970) will continue to manage within this tradition when they take control is a very important question to consider and address.

Hermann Simon, author of "Hidden Champions: Aufbruch nach Globalia" puts the success of these German hidden champions down to a number of core aspects of planning and management style, which are useful and may have broader application for a larger number of SMEs

Strong ambition
setting themselves extremely ambitious goals regarding market leadership and growth

Strong leadership
authoritarian on one side with no discussion on the principles and values, but strong participation and flexibility in the operational details

Qualified loyal employees
a high percentage of university graduates among the workforces but also very low staff turnover rates evidencing a focus on retention of top talent and their know-how

Product quality
competitive advantage is not integrated in the product but in the advice, systems integration and ease of use, advantages that reside in high quality staff expertise and intellectual capital which increases the barriers to entry

Value driven strategies
strategies are value driven not price driven with many of the companies charging a premium on market average showing that quality is still an important factor where value is differentiated

Closeness to customer and competitive advantages
a natural advantage of smaller and mid-sized companies. They are particularly close to their customers particularly top customers who have continuous high demands.

Focus and depth
they define their markets narrowly, work deep into the value chain, adopt an anti-outsourcing approach to their core competencies to ensure total quality control and focus on being the best or world class

Globalisation
because they are niche – deep rather than broad in the market they have to go global

Innovation
the effectiveness of innovation and R&D activities, which focuses on the integration of technology and customer needs beats that of large corporations by a factor of five. At the same time their patent costs are much lower than that of large companies as they dedicated a few experts to find new solutions rather than adopting a big budget approach

Learnings

In the mid to long term sustainable performance can only be achieved when the management team devotes sufficient attention and resources of the company to all of the fundamental challenges of today as well as the thinking, planning, investments and changes required to lead the business to a better future. This is a very difficult but crucial balancing act.

In discussions with our industry experts some of the following characteristics of management style of countries in the EU-8 were considered more conducive to sustained long term performance:

- **Long term orientation** - a long term approach to business planning.
- **Risk based planning** - a cautious risk based approach to opportunities.
- **Competitive focus** - a strong desire to be the best and compete at a high level internationally.
- **Core business focus** - strong clarity on market position and focus on quality of product offering.
- **Financial discipline** - financial management strongly integrated with business planning and risk management, a considered, non-speculative approach combined with strong control over fundamentals including tight working capital management.

5. IDENTIFYING PRIORITIES AND STAND OUT ACTION PLAN

5. IDENTIFYING PRIORITIES AND STAND OUT ACTION PLAN THE MAZARS QUICK SCORE

We have developed a tool called **The Mazars Quick Score**, which helps SMEs to analyse their business by a range of different success factors including:

✔ **Business:** reputation and market position.

✔ **Strategy, product and service people:** strategic management, culture and communication, change management, HR.

✔ **Finance:** operational performance, risk management, cashflows.

✔ **Future:** innovative thinking with a vision for the future, future leadership.

This tool is used to help SMEs understand where the business currently is under each of these success factors and where the business needs to be in order to be a “Stand Out SME”.

The Mazars Quick Score process helps SMEs by providing them with:

- Relevant, independent and easy to use observations about their business.
- Invaluable insight into particular areas of the business.
- Priority areas where attention may be required.
- Comfort for the management team by offering an independent confirmation of the business's existing strengths.

This tool, in conjunction with advice from our SME Practice Group, helps SMEs to identify the priorities for their business. Our SME Practice Group can help SMEs to put a strategic action plan in place to help them become a Stand-out SME.

To assess whether your business is a stand out SME or to find out how you can become one, visit our website (www.mazars.ie) and complete The Mazars Quick Score today.

Please also feel free to contact any member of our SME Practice Group, outlined in Section 7 of this report.

6. HOW MAZARS CAN HELP SMES

6. HOW MAZARS CAN HELP SMES

OUTSOURCING AND ACCOUNTING

- Accounting and Financial Support
- Business Process Outsourcing
- Outsourcing of Accounting Function
- Consolidation and Reporting
- Credit and Working Capital Management
- Company Secretarial
- Financial Management Outsourcing

AUDIT

- Audit
- Pension Audit
- Grant Audit
- Internal Audit
- Consolidation and Financial Reporting
- Technical Accounting Advice
- Regulatory Assurance

MAZARS

VALUE ADDED SERVICES

CONSULTING AND ADVISORY

- Strategy and Business Planning
- Business Process Improvement
- Decision Support and Financial modelling
- Human Resource and Organisational Development
- Governance, Risk and Internal Controls

TAX

- Corporate Tax
- International Tax
- Private Clients
- Employer / Employee Tax
- VAT
- Succession Planning
- R&D Tax
- Restructuring and Acquisitions

FINANCIAL ADVISORY SERVICES

- Corporate Finance
- Business Valuations
- Business Turnaround
- Forensic Investigatory
- Debt Restructuring
- Insolvency
- Cost Reduction
- Mergers & Acquisitions
- Due Diligence

7. TALK TO US

For further information, please contact your local Mazars office (www.mazars.com) or any of the SME Practice Group contacts below.

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