

IOE European Meeting RIGA

10-11 September 2009

1. What has the crisis taught us about SMEs and their issues?

What the crisis has most clearly done is to highlight a number of continuing hazards which affect the SME sector.

First, that the cost of and access to finance is a major and ongoing concern for SMEs across most economies

- IOE surveys confirm this. In 2008 when we asked members what was the largest non-wage cost that impacted on business competitiveness the cost of financial services ranked highest (above a host of other things like energy costs, municipal charges; insurance, and transport). In Africa and Asia it was listed as the leading reason for the growth in the informal economy. In our 2009 survey high capital costs again came through as a major obstacle to enterprise startup and development – everywhere.
- From an SME perspective the kinds of issues that are thrown up are...
 - ✓ *Are there sufficient policy and regulatory incentives to encourage financial institutions to lend to SMEs?*
 - ✓ *Are financial products adapted to the needs of SMEs?*
 - ✓ *Is there support targeted to SMEs such as advisory services and programmes to assist them in preparing bankable loan proposals?*
 - ✓ *Is the information about financial services well disseminated to SMEs?*
 - ✓ *Is competition in the banking sector promoted so as to improve access to finance at an affordable cost.*
 - ✓ *Are there SME credit bureaus to compile the credit ratings of SMEs.*

Clearly the answers to these questions in many economies is (or was) probably a negative one. Without access to finance, enterprise growth is retarded as is development. As EOs this is therefore a massive issue for us.

The second major issue that has been highlighted is the regulatory and cost burden that is placed on SMEs.

- As governments scrambled to respond to the crisis, a range of emergency measures were introduced in order to keep smaller business solvent. These range from cutting pay roll taxes and social insurance contributions, to regulatory changes that eased costs (monetary and time). This has helped keep many small firms in business, but it also illustrates just how heavy compliance with legislation can be for SMEs in many jurisdictions. It raises the question, if so many costs can be removed so easily; why were they there in first place. *It provides EO's with important signposts and direction for their ongoing advocacy efforts, during and after the crisis.*
- The revealing picture is that regulatory and costs burden for SMEs are often extremely onerous – and not just in terms of dollar amounts. The time factor is often underestimated and the need for external expertise to comply with legislation.
- This raises a number of questions:
 - ✓ *Why are taxes levied on companies regardless of whether they make a profit or not?*
 - ✓ *What is the justification for payroll taxes which bear no relationship to profitability or capacity to pay?*
 - ✓ *Why are there not deductions for SMEs to invest in equipment and facilities?*
 - ✓ *Why is the red tape and bureaucracy burden still so high?*
 - ✓ *Why are there still not in many economies regular regulatory reviews?*
 - ✓ *Why do patent fees and trademarks cost so much?*
 - ✓ *Why are regulatory bodies not more accountable and more safeguards against inappropriate regulation in place?*

Third and more generally, that we live in a global economy, meaning that our collective fortunes are linked – too the good and to the bad.

- As consumer demand collapsed; so has trade and with it SMEs dependent on that consumer demand in areas such as the EU and US. Export orientated SMEs in particular have been hammered.
- What has become clear is that because SMEs lack the capacity to analyse the economic effects a policy change or an economic incident can generate on the overall global economy; not to mention the impact on their business, they are blind to any on-coming calamities.
- Subsequently they are unable to adjust internal management to suit the need of the new or approaching situation (whereas larger firms can be both better prepared for a crisis; can adapt better; and take a longer term perspective).

2. What does this mean for EOs and their policy agenda?

For a start, it underlines the Importance of speaking and being seen to speak for SMEs

- SMEs have been the real victims of this crisis. Considering their importance to all economies EOs need to be seen to be ‘batting’ for SMEs. That means they may need to say uncomfortable things about financial systems and services. They certainly need to be very vocal in talking about the regulatory and compliance burden on SMEs and proposing alternatives.
- Public opinion is angry with the current situation. Certainly very angry with financial institutions and what they pay themselves. But that has not translated into necessarily a general anti-business feeling. There have been too many examples of companies going out of business and people consequently losing their jobs. The public have also seen that this is a holistic crisis impacting on everybody, business included. This is the position we need to emphasis as EOs
- Let me give you what I thought was a useful and concise articulation of this view. This is the ACCI’s approach which framed its position on the crisis in this regard at the start of this year.

“Businesses and employers in the real economy here in Australia – my constituents – neither caused this, nor contributed to it. They together with our community at large are on the receiving end.

By all means learn the lessons, but responsible policy makers do not embark on collective regulatory punishment of those businesses which also suffered loss because of the governance and conduct failures of others.”

Second, it means that we need to ensure that our advocacy priorities clearly address the needs of SMEs. These include.....

- Advocating for financial systems that can help the SME sector grow; Promoting competition in the banking sector to improve access to finance at an affordable cost; establishing credit bureaus to help SMEs access credit; developing with the banking sector codes of conduct on SME lending....
- Actively examine reductions in administrative, compliance, taxation and labour regulatory regimes for SMEs. Eliminate unnecessary red tape and bureaucracy. Make it easier to start and stay in business. Let me give you a quote from one of the respondents to our global survey this year: *“The law in my country assumes that all businesses are multinationals and have their resources and means”*. This crisis has demonstrated that the law needs to assume the exact opposite.
- Advocating particular support for “Innovation-oriented” SMEs as this type of activity is usually highly pro-cyclical. It is a key pillar in ensuring future growth.
- Promoting market competition and support open trade

In the first truly global financial crisis of the modern globalization era, the need for representative organisations of business to affect positive policy change on all issues affecting business, large and small, has been reinforced.

Third, by providing market information; economic analysis; and identifying trends

- Clearly SMEs need analysis of current business cycles and broader economic trends. They need this in a digestible fashion that they can understand, relate to and take actions to adapt in their business if necessary.

They also need someone looking down the track predicating what will happen next? Take the following examples:

- One emerging change from the crisis, predicated by some early analysis, may be a shift away from global to more regional supply chains (changes also being driven by the climatic change debate and possible regulatory changes in this domain). This has major implications for the SME sector.
- It is likely that a more consolidated financial system will emerge from the crisis; competition may be weaker leading to higher costs of credit and other financial services. There may well be an increase in the real cost of capital. Enterprises, particularly small ones will need to prepare for this reality.
- What about the trade environment. As we have seen SMEs have been devastated by the drop in global trade. The incremental pushes towards protectionism are happening in spite of what governments publicly protest. The chances of a global trade deal – Doha – seem distant. Meanwhile many countries are pushing on with bilateral trade deals - that usually represent a poorer deal for the weaker negotiator and usually have much more limited impact than professed.

The crisis has underlined how little SMEs know about wider economic trends and the impact that they can have on their business. EOs can help...

Fourth, EO as a platform for dialogue with the banking sector

- EOs can provide a space for the banking sector to liaise directly with SMEs to hear and consider their concerns and perspectives. They can facilitate regular banking- small business forums and so forth.

Lastly, using the crisis as an opportunity

The crisis presents an opportunity to push for reforms in the operating environment for business. Such has been the speed of the crisis; governments are responding and are open to regulatory and other policy changes. EO's need to capitalise on this situation.

3. How has the IOE responded?

- At a technical level the IOE has prepared a number of publications and policy briefs relevant to SME issues - all available on our website.
- We have prepared a specific publication on this theme for this meeting – which will be updated on the basis of this conversation.
- We additionally are working with the ILO on a number of SME publications – a number of these are already done.
- Lastly we envisage rolling out in the immediate period major national SME advocacy events with EOs. These will be national events focused on developing SME advocacy charters. The intention is to pilot 5 of these before the end of the year across all regions. On the basis of this pilot phase will develop a programme for 2010.
- At a policy level within the ILO we are seeing a shift since the sustainable enterprises debate in 2007. We are continuing to push the ILO to step up its efforts in SME development – in particular in terms of the policy environment for small growing enterprises – not the mama and papa outfits, but the small dynamic enterprises that really can be engines for growth, innovation and jobs in economies. There are reasons to be encouraged.
- Politically positioning “enterprise development efforts” in ‘SME’ language is politically useful in the ILO context
- The Global Jobs Pact is additionally a useful opportunity. The GJP contains very useful language on the importance of the SME sector and also on the regulatory environment for that sector to grow.