

Operational Fit or Misfit? Targeting Small Business Support Programmes

Per-Anders Havnes and Erik Arntsen

Abstract

Relatively few small enterprises engage in systematic development projects in spite of the efforts of governments to stimulate through small enterprise support programmes. Part of the explanation can be that these programmes are based on managerial and operational systems that are found in large enterprises but not shared by small enterprises. Anecdotal evidence suggests that there are differences between large and small enterprises regarding the parameters of development processes. Further research is necessary to verify such differences and their practical implications. Such knowledge would be conducive to improve the fit between the small business support programmes and the managerial procedures of small enterprises.

Introduction

In the early years of his carrier one of the authors found himself in a managerial position in a small enterprise after having studied, researched and taught management. On one occasion when particularly difficult problems arose he searched among the management theories and methods he knew for an instrument to solve the problems, but nothing could be used and he had to rely on common sense. After the first frustration of the inadequacy of his academic training had subsided, he realised that the information required for the analytic methods of management was not available in small enterprises. The analytic methods, like most of the management theories, were developed from studies of large enterprises. They are more complex, have more formalised control systems, have scale advantages in all aspects of information systems, have specialised personnel, and so on. Which means that although many of the managerial principles are similar the managerial methods, the precision of control systems and the approach to management are quite different in large and small enterprises.

Even now, several decades later very few are aware of and appreciate the differences between managing a small and a large enterprise. One consequence is that support programmes targeted at the small business sector often are attuned to a managerial reality that is not found in the target group. This can be one of the reasons that, in most countries, only a very small proportion of small enterprises respond to support programmes.

In spite of their economic importance and their dispersion small enterprises have not been systematically researched until the past few decades. One consequence is that the different aspects of business management theories and procedures have been developed with insight gained through study of large enterprises. The small business perspective is therefore not fully recognised and appreciated by the academia or by the policy makers. The assumption that small enterprises are miniaturised large enterprises, or even infant large enterprises, seems to have influenced the design of policies and support programmes to this day.

The purpose of this paper is to draw attention to the fit or the misfit between small business support programmes and the managerial reality of small enterprises by means of personal experience and anecdotal evidence and to discuss the ensuing consequences for programmes in support of the small business sector.

The small business sector

Governments in all countries see the small business sector as fundamental for their economic development. There are many good reasons for the significance of small enterprises – first of all the fact that small business is the normal format for conducting business since small business constitutes more than 95 % of the business population in all countries.

*European SMEs are a key to deliver stronger growth and more and better jobs – the two main objectives of the new Lisbon partnership for Growth and Jobs. They make up a large part of Europe’s economy: there are some 23 million SMEs in the EU, providing around 75 million jobs and accounting for 99% of all enterprises. They are also a key part of European industry, as they contribute up to 80% of employment in some industrial sectors, such as textile, construction or furniture.*¹

The sector of small and medium sized enterprises (SME) is defined quite precisely for statistical reasons². However, enterprises that statistically belong to the SME sector will often be regarded as being large in small communities. Here we will be less stringent and precise, and address the phenomenon small businesses in general terms. We will recognize small enterprises by one or more of the following characteristics:

- Few employees and simple organisation
- Low formalisation in management systems and decision procedures
- Independently owned, not belonging to group of enterprises
- Limited resources
- More focus on general than specialised competence
- Operate in small or niche markets

Small enterprises require limited resources and markets for establishment and operation. They find their room in niches and local markets of densely populated areas, and they can operate economically in areas with low population density. Small enterprises are flexible and adaptable in turbulent business environments, but at the same time exhibit less volatility in employment than large enterprises in turbulent times³. It is also generally assumed that the flexibility of small enterprises constitutes a more favourable setting for innovation than the rigid and formal systems of large enterprises.

The small business sector can be delimited by parameters that can be defined with a high degree of precision. Nevertheless, the sector is better characterised by variety than by similarity when it comes to what they do to make money; how they organise their value creation, as well as their roles and positions in the value chain towards a final product and the end user. The heterogeneity of the small business sector is also due to the fact that one or a few persons often make strategic choices, and therefore individual preferences and priorities have stronger influence than in large enterprises.

Many small enterprises compensate for their shortages and limitations when it comes to capabilities and capacity by adequate organisation of resources and co-operation in value creation networks. In a turbulent business environment this approach is quite efficient. Changing partners is far easier, swifter and more expedient than restructuring the facilities and the organisation of a large enterprise. Thus the limitations in resources and in capabilities contribute to large variety and adaptability of small enterprises. Consequently it is very difficult to design policies and support measures that are relevant and applicable to a majority of small firms. Dedicated and targeted policies and support measures are required.

There is now a multitude of international and national support programmes for small enterprises. Systematic evaluations demonstrate that many of these programmes only reach a very small minority of this large target group^{4,5}. Could the reason be that these enterprises really do not need assistance

¹ Information page European Commission, Enterprise and Industry, July 2006, http://ec.europa.eu/enterprise/entrepreneurship/index_en.htm

² Micro enterprises: 0 – 9 employees; small enterprises: 10 – 49 employees; medium-sized enterprises: 50 – 249 enterprises; not part of a group; equity less than 43 million €; annual turnover less than 50 million €; European Commission. With this definition 99 % of the enterprises in EU are SMEs.

³ European Commission, SMEs in Europe 2003, Observatory of European SMEs: Report 2003/No. 7. Report submitted to the Enterprise Directorate General by KPMG Special Services, EIM Business & Policy Research, and ENSR; Brussels, 2004

⁴ European Commission Enterprise Directorate-General (2002) Report submitted by Sheikh, Sonja, Ingrid Pecher, Nadia Steiber, and Eva Heckl (2002) Support services for micro, small and sole proprietor’s businesses. Brussels

⁵ Jakobsen, Stig-Erik and Erik Døving (2006) *Følgeevaluering av Forskningsbasert kompetansemegling. [Interim Evaluation of Brokering of Research Based Competence]* SNF Report 08/06. Institute for Research in Economics and Business Administration, Bergen.

and support? Is the reason that the support programmes do not fit with the way these enterprises operate? Or is the reason that the enterprises of the target group are not aware of the opportunities they are missing? An affirmative answer to any of these questions indicates that more knowledge is needed about management of small enterprises.

Rationale of Support Programmes

Small business support programmes use many different approaches or instruments. The programmes may provide or facilitate training, financing, networking, internationalisation, product development, regional development and so on – or a combination of several of these. Any support programme is based on a given set of premises that constitutes a rationale of the programme. One part of this rationale is a set of objectives, see the list below. A support programme is seldom so focused that it shall serve only one purpose. The problem is that multiple objectives very easily create internal goal conflicts in the programmes – especially when the programmes have several supporting institutions.

Another part of the rationale is the instruments that are assumed to be conducive to reach these objectives. Choosing appropriate instruments will depend on the problems that need attention to reach the objectives and how the recipients of support presumably will respond to the instruments.

The most common objectives for support programmes for the small business sector is to:

- a) Compensate for market failures that limits the operation or development of small enterprises
- b) Compensate for inherent disadvantage due to scale for small enterprises
- c) Stimulate to changes or transformation in the strategic development of small enterprises
- d) Stimulate or facilitate start-up of new enterprises.

Frequently several of these objectives are combined in the same programme.

The intention of the policy and programme makers is always to stimulate the small enterprises to adopt another direction of development than they would without the stimulus or support of the programme. The programme is then seen as the only or main cause to these changes, as illustrated by figure 1.

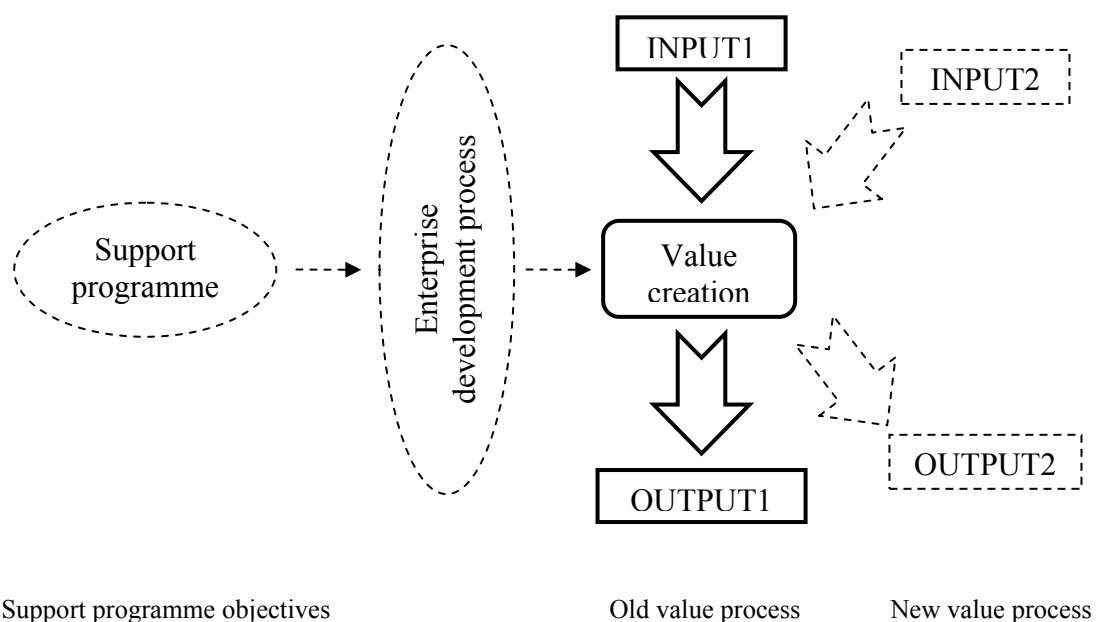


Figure 1 Implicitly assumed impact of support programmes

It is assumed that the introduction of the support programme will cause the firm to change its operational mode from using INPUT1 and producing OUTPUT1 to using INPUT2 and producing OUTPUT2. This transformation will require that the value creation process of the firm also change. It also requires that the support programme instruments have sufficiently strong impact to be registered over the continuous impulses from the dynamic business environment and the momentum of ongoing activities in the enterprise.

However, the intended changes in strategy and behaviour will not occur unless the design of the support programme is compatible with the priorities and objectives of the decision makers in the firms. One short example will illustrate this: A policy objective of increasing employment in small enterprises will never succeed if most small business managers try to cut costs by increasing mechanisation and reducing employment.

There are three main flaws in the relationships depicted in figure 1:

1. That the mechanisms of enterprise development processes are assumed to be identical in small and large enterprises,
2. The impact of the manager’s and/or the owner’s perception and volition is not included in the model,
3. The influence of the business environment is not included in the model.

The development processes for small businesses that are implicitly assumed by the authors of small business support programmes are therefore incomplete. When the three missing factors are included, a more complete depiction of the factors and the relationships may be as set out in figure 2:

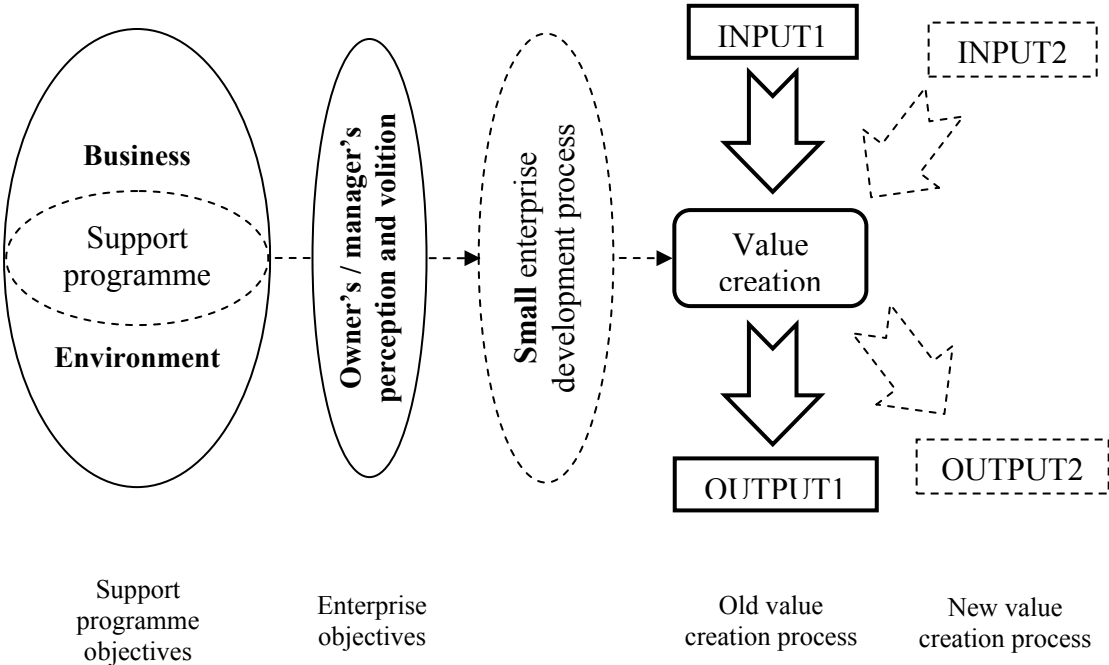


Figure 2 Proposed real impact of support programmes

All support programmes are part of a business environment that has some general elements and some that are specific to each firm. The information flow from the business environment to the enterprise will be intercepted by the observer’s perception. In figure 2 the manager and the owner personify the observer of the signals from the business environment. The perception of which information is relevant to the enterprise will in depend on their goals for the firm as well as their personal goals. Volition and perception are important factors when interpreting behaviour on individual enterprise level. Each firm will follow a line of activities that in part is decided by the interaction of the business environment and the volition, which contributes to the high variation in the characteristics of small enterprises. The ensuing development process will be different in small and large firms. There will, however, also be large variation in development processes found in small firms.

What is the apparent rationale of the policy makers and support programme designers, and what appear to be their assumptions about the rationale of the decision makers in small enterprises? This is never explicitly stated in any of the support programmes and will of course vary much. The issue has not been subject to empirical research so there is no authoritative source of information in this issue. In

lieu of facts, we will allow ourselves some reflections based on common features of some support programmes. The sequence of the discussion does not reflect any assumption of the priorities or significance of the discussed features.

Economic man – optimising utility

Most programmes seem to assume that a business manager will strive to optimise profit. A manager with a short time horizon will try to optimize operational activities, while a manager with long time horizon will try to optimise strategic development; and all intermediary categories will also be found.

This assumption reflects the prescribed methods in most the textbooks on business economy and business management. The goal is to seek the best solution to any problem or the best alternative for any decision. Finding the best solution will in economic terms mean optimising the monetary value of utility in all decisions. The economic man is able to analyse the outcome of all decisions, recognise the best outcome and be at liberty to select the best alternative. This implies that the decision maker(s) have access to sufficient information to identify the different alternatives and sufficient data, analytic capacity and time to calculate their outcomes. Moreover, the priorities must be sufficiently clear to range the alternatives.

The reality in the small business sector is far from the situation of the economic man. First of all, the scale of operations and the number of transactions makes it very costly to aggregate detailed information on operations and markets. The administration of small enterprises is very limited – almost frugal – with little capacity and capability for analyses in excess of operational requirements. Most small business managers are painfully aware that they do not possess sufficient information, time or the analytic capacity to find the best solution.

The parameters of any optimisation change rapidly in the real and consequently the best solution is highly transient. The optimal solution today may therefore be an inferior solution tomorrow. Finally, owners and managers of small enterprises often give high priority to non-economic value dimensions, such as security, predictability, social responsibility, and so on. Many of these evaluation parameters are so ambiguous and contextual that it is not possible to establish a precise and permanent ranking of the alternatives.

As a consequence most small business managers will therefore strive to find a satisfactory, sufficient or good solution that they believe is robust. That means that the outcome is not expected to vary too much if some of the data or assumptions of the analysis turn out to be transient, inaccurate or wrong.

Public information channels and mastering lingo bureaucracy

Discussions with representatives of the support services have left the impression that they assume that once a programme is published, it is also known and correctly understood by its target group. There are two misconceptions in this assumption.

The basic misconception is that the general public is tuned in to the governmental information channels. The real situation is that the small business manager has an overflow of information with little or no assistance to distinguish between essential and non-essential information. Market information is most important and crucial for a small business. The information from the public sector is usually of a character that it does not require immediate action and will therefore easily be overlooked by the small business manager.

The recent development in communication technology has increased the managers' capability to search for specific information, but the capacity of the inbound information channels to the enterprises has increased even more to a level where one person cannot keep track of everything. Since most small enterprises have little capacity to filter information or to extract and digest the essential information, there is no way that the small business manager can keep track of all public information on support programmes, no matter how relevant they might be to the enterprise. Much information is therefore missed, other is not recognised as being relevant or even important. The small business manager will very often depend on being advised on important information by colleagues or professional advisors such as accountants.

Some public agencies now use professional communications advisors when preparing information on new support programmes. In spite of this, programmes are often presented with words and concepts that are more familiar and appropriate for the large bureaucracies than for small enterprises. The words “innovation”, “strategic planning” or “market development” may not be part of the vocabulary in small enterprises even though the enterprise may be highly innovative and the functions of strategic planning or market development may be performed at high standards. Differences in semantics or the use of concepts may decide whether or not a small business manager perceives a support programme as relevant to the enterprise. Without this initial recognition of relevance there will be no further steps in the process that ends up with one more enterprise taking advantage of the programme.

A general aspect of communication between the public sector and small enterprises is that the beneficiaries of support programmes need to present a plan or an application prior to acceptance, and cost and progress reports during and after completion of the programme. In spite of the attempts to reduce red tape, it is becoming increasingly important to present proposals and reports in a correct format and with the correct terminology. It has become a lucrative line of business to assist small firms when making proposals, business plans, financial statements, and so on.

Development orientation

Most of the management literature asserts that it is normal for firms to develop by growing, extending their markets, improving their managerial control system, mastering more complex technology, and so on. Most small business support programmes seem to incorporate the same assumption on the normal development pattern for their target group. At any given moment, however, only a minority of the small enterprises will report that they have been developing or have intentions to develop in any of these aspects in the near future. This does not mean that these firms maintain a static position over long time. It is merely a statement that change processes have other forms than intentional and planned activities.

There are many examples that small firms develop in other directions than growing and extending. Frequently, enterprises will withdraw from specific markets, discontinue product lines or reduce employment in planned and controlled processes. Such development traits may be permanent or temporarily. Likewise, closure of a firm cannot be interpreted as a failure if this is a free choice by the decision maker(s) to obtain a higher utility than continuation of the enterprise would entail.

Development will therefore take many forms in small enterprises. Growth and retraction, changing market focus, renewing technology and products, and new competence are all examples of development – and so is simplification and focusing in products and production lines. Common to all development is that the firm’s competitive position changes. Such changes will always take place as the outcome of a process, which implies costs and uncertainty.

All business ventures pass through different phases. The initial phases are highly creative with new combinations of ideas, knowledge, and resources. Then follows a phase where all creative elements are refined and given a practical form. In this phase creativity is gradually replaced by proficiency. However, both of these phases are investment periods where the new venture incurs costs but no income. These costs can only be recovered in an ensuing value creation phase where products or services are generated and subsequently sold. In this value creation phase focus is on proficiency and efficiency, which means that few changes in the parameters of the value creation process. As long as there is positive outcome prolongation of the value creation phase will increase the payback period for the investments that were made in the initial creative phase.

This interchange between periods with focus on high creativity and periods with focus high efficiency becomes very obvious and is imperative to small enterprises that have few parallel business ventures at different life cycles stages. The individual development project may often be large in relation to the total turnover or the total assets of a small enterprise. A failure on a project like this may therefore be critical to a small enterprise, and assessment and avoidance of unnecessary risks may be vital to a sustainable development of the enterprise. It might seem that many small enterprises follow a risk adverse strategy, while it just avoiding risks that can be detrimental to the firm and its long-term survival.

Formalised reporting system

All public programmes will require that the participants provide specified information at all stages, from application to final report. Quite often this is information that is not used in the firms' own economic control and needs to be assembled only to comply with the requirements of the programme. This may concern the detail with which costs and income can be attributed to specific activities or products, the detail of progress plans, the specifics of marketing plans and market budgets, and so on. Managers of small firms can control such issues with far less detailed and formalised records and reports than managers of large and more complex firms. Overly detailed and formalised reporting systems are therefore an unnecessary cost and steal from the precious administrative capacity of the enterprise. Most small enterprises try to keep their reporting systems simple and to the minimum requirements.

Lean organisations – organisational slack

Development processes require that there is slack in the organisation. Persons and resources that are essential to the process cannot be fully utilised for daily operations.

Small and large enterprises organisations alike strive for efficiency by cutting away elements that are not necessary for their value creation. However, a small enterprise manager who attends a project meeting may represent 20% of the managerial capacity with no substitute in his or her special field. A manager coming from a large organisation may represent less than 1% of the managerial capacity and only one of several persons that is capable of performing her or his tasks.

The fact that the planning horizon is short and dominated by operational requirements makes it difficult to make schedules and set aside sufficiently large periods of time for development processes in small enterprises. Although there will always be slack in all organisations, this slack has to be available at certain and predictable points in time and in sufficiently large blocks if it shall be useful for development purposes.

This is another reason that incremental changes are so commonly found in small enterprises.

Dynamics of Small Business

Talking to the hairdresser while having a haircut, one of the authors asked her how much and how often changes occurred in her business. The answer was: "When you are here each day you do not notice any changes, but people who have been on leave of absence for some months always need to learn much about new products and new methods." This answer epitomises the change processes that we find in most small enterprises. Their business environments change continuously, and most small enterprises adapt to these changes without being conscious of any internal development process. However, new demands from their customers induce adjustments of products and product portfolio with ensuing changes in raw materials and work procedures. The individual enterprise may or may not take active part in the development processes of new products or procedures. Nevertheless, the dynamics of small business repeatedly puts the personnel in a learning situation.

The dynamics of small business means that the individual enterprises change somehow. The norm of all textbooks in the management field is that a firm should grow, expand its markets, develop new and better technologies, improve managerial control systems, and so on. Most small enterprises give preference to stability over change.

The prescribed planning processes for the development are supposed to have a strategic and long-term time horizon. Most small firms have operational focus and short-term planning horizon.

The most auspicious change mode is radical innovation where the innovation marks a decisive and significant break with previous products and processes. The governmental support programmes often favour radical innovation at the expense of incremental innovation where the changes mostly are modifications of previous products and processes. However, as discussed above, small enterprises will for many reasons favour incremental innovations. This can be attributed to several factors where small and large enterprises differ and government support programmes are mostly in accord with the large enterprises, as summarised in table 1.

Table 1 Summary of development parameters in SME, LSE and government programmes

Development parameter	Small enterprises	Large enterprises	Government
Dominant dynamic mode	Stable	Growth	Growth
Dominant change mode	Incremental	Incremental + radical	Radical
Control system	Low detail, informal	High detail, formal	High detail, formal
Planning horizon	Short, operational	Long, strategic	Long, strategic
Competence	General	Specialised	Targeted programmes = specialised
Information channels	Few, selected	Multiple	Multiple
Intelligence capacity	Specialised, limited	Differentiated, large	Rapidly changing programmes
Organisational slack	Limited	Medium	High
Risk concentration	Few ventures	Many ventures	Very many ventures

Need for further research

Table 1 represents a set of propositions on differences in structure and intention between small and large enterprises that mostly are based on anecdotal evidence and personal experience. Each of these propositions can be investigated independently as the first step.

This paper proposes that the accumulated effect of these differences is so significant that the development processes in small and large enterprises take different forms. Furthermore, that the governmental support programmes for small enterprises is based on the development processes observed in large firms. Hence, the support programmes do not reach out to more than a minority of the small enterprises. Both of these propositions are quite difficult to investigate since the variation within the group of small enterprises probably will be larger than the difference between the “averages” for small and large enterprises.

In light of this it is reasonable to propose a concerted research effort to document and analyse the managerial processes of small enterprises. The results from this research would be that government support programmes can be designed better to reach the intended beneficiaries of the programmes. The research would also give background for reconsidering the management literature for the small enterprise segment.

References

- European Commission Enterprise Directorate-General (2002) Report submitted Österreichisches Institut für Gewerbe- und Handelsforschung, edited by Sheikh, Sonja, Ingrid Pecher, Nadia Steiber, and Eva Heckl (2002) *Support services for micro, small and sole proprietor's businesses*. Brussels
- European Commission, Enterprise and Industry, Information page July 2006, http://ec.europa.eu/enterprise/entrepreneurship/index_en.htm
- European Commission, SMEs in Europe 2003, Observatory of European SMEs: Report 2003/No. 7. Report submitted to the Enterprise Directorate General by KPMG Special Services, EIM Business & Policy Research, and ENSR; Brussels, 2004
- Jakobsen, Stig-Erik. and Erik Døving (2006) *Følgeevaluering av Forskningsbasert kompetansmegling. [Interim Evaluation of Brokering of Research Based Competence]* SNF Report 08/06. Institute for Research in Economics and Business Administration, Bergen.