

Supporting the internationalisation of SMEs

Final Report of the Expert Group





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Final Report of the Expert Group

on

Supporting the internationalisation of SMEs

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SUPPORTING THE INTERNATIONALISATION OF SMES

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1. EXECUTIVE SUMMARY

Globalisation has brought a shift to the economic environment of the European SME. The progressively disappearing barriers and borders are exposing all companies both to new markets and to international competition. Consequently SMEs that do not consider internationalisation are unknowingly self imposing a severe restriction on their potential for long term survival.

Internationalisation is not to be considered as a separate part of the company or as a strategy to be enacted only in times of reduced local demand, but fully integrated into the SME as a core part of the company's long term strategy. This is reinforced by the fact that internationalisation has been proven to be one of the key engines for competitiveness and growth.

Despite the advantages of embracing globalisation and the risks of not doing so **many European SMEs still remain focused on their national markets**: only 8% of EU27 SMEs export and only 12% of the inputs of an average SME are purchased abroad. The main reported reasons are a **lack of financial resources** but most of all **lack of skills or skilled human capital to tackle internationalisation**.

In order to have more internationalised SMEs Government support remains vital. Many SMEs would not consider internationalisation if it were not because of support. This "additionality" effect fully justifies governmental intervention.

Effective Government policies should consider operating on two fronts:

- For present SMEs. Raise awareness of the need to internationalise and prepare a set of policies that will help companies overcome barriers to internationalise. For long term effect, these will have to be based on the acquisition of new capacities rather than on the provision of grants or subsidies.
- For future SMEs. Promote an environment conducive to more and better equipped international entrepreneurs via language education and the promotion of entrepreneurship in the academic curricula.

Developing a successful strategy to support current SMEs to internationalise:

- Adapt to the local reality which calls for the participation of all direct stakeholders in developing both policies and programmes: national and regional governments, business associations, business support associations and banks: it will facilitate implementation, create synergies and guarantee the best possible match to the local economy.
- Each country should consider internationalisation as part of the policies to enhance competitiveness. As countries progress through the value added ladder this will lead to merging internationalisation and innovation under one single umbrella. Inside Europe this is already starting to happen in Ireland, Finland and Norway, just to mention some examples.
- The main effort should be directed towards having more internationalised companies rather than focusing on those companies with the largest potential.

- In order to be able to support the largest number of SMEs, programmes and policies must focus on the main barriers to SME internationalisation: lack of financial resources, lack of skills and lack of information.
- The most effective means of support to an SME is individualised support. Effective long term support must be based on the creation of capacities inside the SME.
- Without disregard for extra-European markets, for the vast majority of European SMEs the internal market is the main market/partner. It is also sufficient for the launch of their international operations. In most cases the internal market creates the possibility for small and micro SMEs to grow to the stage where they can successfully compete beyond the EU borders. As such, for most SMEs the EU can act as a launch pad for a more successful engagement in international markets.

2. INTRODUCTION: GLOBALISATION AND THE SME

Globalisation: the free movement of goods, services, capital, people, information and knowledge leading to a more integrated global economy.

Globalisation is not new. Certainly the pace is rapid and has quickened in recent years but the process of greater international economic integration has been underway for decades: the volume of good currently being traded across the world is 15 times greater than in 1950 and its share in global GDP has tripled.

In the last 20 years more open economic policies and trade liberalisation worldwide and technical advances, notably in transport and communication have combined to lower costs and accelerate globalisation. Global trade in products and services has been growing at an average 6% since 1990, faster than global GDP.

The most notable elements of the current wave of globalisation are:

- An unprecedented lowering of trade barriers worldwide.
- Vastly improved logistics and communications systems available to all companies.
- The information technology revolution which has opened the way for greater technology and knowledge exchanges and the advent of new types of economic transactions such as e-commerce.

This means that trade can be conducted cheaper, faster, easier and over larger distances and the advent of previously non tradable services. It has also incorporated lesser accessible markets and the large emerging global players of Brazil, China, India and Russia.

But globalisation is not only trade. It also involves foreign direct investment including offshoring and relocation and an increase in all forms of technology transfer. FDI flows have grown from less than 5% of global GDP in 1980 to over 15% in the late 1990's.

As a consequence of all this companies not only have greater possibilities in accessing more markets and suppliers but also of determining the organisation, management and location of most aspects of their own operations.

Globalisation has effectively “shrunk” the world. Through globalisation national borders are constantly losing their significance as limitations for human interaction in general and economic collaboration in particular. This means that for all economic actors their natural spheres of activity are expanding from national into multinational or even global.

On a global scale the benefits of this greater economic integration and expanded trade relations have been praised and demonstrated ever since Ricardo and Smith. The European Union is a point at hand: it is estimated that 20% of the gains in living standards in the EU over the last 50 years can be attributed to the EU's growing integration with the world economy. And a full 63% of European Union citizens are in favour of globalisation¹.

¹ Source: Flash Eurobarometer 151b « Globalisation ». European Commission 2003

But what is good in this macroeconomic scenario is also good for SMEs? And more importantly, how are European SMEs to transform this to their advantage?

For an SME globalisation means that the natural or “local” environment is being constantly transformed and growing, which brings greater opportunities in the form of larger markets and new suppliers but also threats in the form of greater competition and shorter product life cycles. Yet many SMEs remain passive despite the fact that this shift to an increased complexity and faster pace of events can only be expected not just to remain but possibly accelerate in the future.

This greater integration and reduced barriers mean that international competition starts at home. Even businesses that focus primarily, or even exclusively, on the domestic market have to be competitive internationally in order to secure long-term survival and growth².

This new, ever changing scenario that is globalisation will require and reward inventiveness, agility and flexibility: the very qualities that are commonly used to define SMEs. Embracing these qualities means that competitive SMEs will not only be in a position to tackle globalisation but embrace it and profit from it.

Therefore, a pro-active attitude to global competition and markets is increasingly becoming not a choice but a matter of necessity. Each company must adopt internationalisation as part of the strategic search for the company’s competitiveness and not as a reaction to times of reduced national demand. On the positive side, critical challenges to succeed in international operations are fundamentally identical to those of the home market³.

For this, continuous technological, managerial and operational innovation inside the SME will be one of the key tools for their sustainability and growth.

Internationalisation is an engine for SME competitiveness

Internationalised companies have shown to have better capacity to innovate and grow. The 2002 OECD study High-Growth SMEs and Employment demonstrates that exporting is a precursor of strong growth. The link between exports and enhanced productivity/competitiveness is clearly established by numerous studies⁴ and specifically, firms with international sales have higher sales growth than firms that sell only domestically⁵.

² Karagozoglu, N., and M. Lindell (1998). “Internationalization and Small and Medium-Sized Technology-Based Firms: An Exploratory Study,” *Journal of Small Business Management* 36(1), 44–59.

³ Winch, G. and Bianchi, C. “Drivers and dynamic processes for SMEs going global” *Journal of small business enterprise development*, Vol.13, no.1, pp73-78

⁴ As an example: Establishment level empirical study of links between exporting, innovation and productivity-CIS4” Richard Harris and Q Cher Li, September 2006

⁵ Internationalisation of High-Tech Start-Ups and Fast Growth - Evidence for UK and Germany, Burgel, O.; Fier, A.; Licht, G. and Murray G.C.; ZEW discussion paper No. 00-35, 2000

In Norway, the 1995-2005 evaluation of the IRDC programme shows that the projects with an international customer have a much higher success rate than those with a Norwegian one.

But the benefits of internationalisation do not refer exclusively to exports. Exporting, as the traditional way to internationalise, is still very important, but importing not only is a source of improved performance, via the acquisition of new technology and abilities but importers tend to be keener/faster exporters⁶.

Other forms of internationalisation such as foreign direct investment (relocation or outsourcing), technology transfers, participation in international value chains, and other forms of inter SME co-operation are gaining ground. In all cases the quest for greater competitive advantage is even more direct: access to other markets is only one motivation usually shared or outweighed by access to technology or cheaper or more readily inputs.

⁶ On the direct impact of imports on increased productivity and growth “Imports of services and economic growth: a dynamic panel approach”, Xiaoying, L., Greenaway, D. and Hine, R.C., SETI project, May 2003. “Small and medium enterprises internationalization and the influence of importing on exporting” Holmlund, M.; Kock, S. and Vanyuhin, V., International small business journal 2007, Vol. 25, pp.459 Also “Born Globals internationalization in the creative industries”, a paper by Professor Staffan Gullander remarks the crucial causations effects between inward and outward activities.

3. KEYS TO INTERNATIONALISATION

3.1 The drivers to internationalisation

The attitudes that lead to internationalisation stem from the same source as start-ups, innovation and entrepreneurship: developing lines of growth. In the case of SMEs the reasons that move companies to internationalise are closely related to the personal and professional experiences of the owner/manager and the evolution and “attitudes” of the SME⁷.

Extensive literature supports that **international orientation of decision makers** is a key determinant of the nature and extent of internationalisation. A survey of successful internationalised UK SMEs identified the international commitment of the founders, entrepreneurial firm behaviour and pro-activity in foreign markets as key predictors of performance⁸. The firm age and the CEO age are the main predictors for becoming an internationally committed company.⁹

This international orientation is a consequence of the professional experience of the owner/manager and the industry/sector to which the SME belong. In both cases again the level of international exposure plays a key role. This central role of the entrepreneur and his personal networks is even more important in the case of “born globals”.¹⁰

As we can see from the previous paragraph, exposure to internationalisation, either because the sector is particularly exposed or because of the personal and professional experience of the owner/manager, are the main drivers to internationalisation. This somehow makes internationalisation a “closed loop” where previous experience is the best guarantee to “future appetite”: internationalisation breeds internationalisation.¹¹

This already indicates what should be the first and earliest intervention in order to foster internationalisation. An international orientation by the SME decision makers is necessary and the first phase of policy support mechanisms might focus on developing the international orientation and formal entrepreneurial training of key decision makers in SMEs¹².

⁷ Amongst others Welch, L.S. and Luostarinen, R. “Internationalization: evolution of a concept” Journal of general management, Vol.14, No.2, pp 34-35

⁸ Micromultinational research project, Report for Scottish Enterprise, Glasgow May 2003

⁹ “International activities in small firms: examining factors influencing the internationalization and export growth of small firms” Andersson, S.; Gabrielsson, J. and Wictor, I.; Canadian journal of administrative sciences, Mar 2004; 21,1

¹⁰ “The entrepreneur in the born global firm in Australia and Sweden” Andersson, S, and Evangelista, F. Journal of small business and enterprise development, Vol.13, no.4, 2006

¹¹ “The internationalization of small and medium sized firms: the role of organizational learning effort and entrepreneurial orientation” De Clercq, D., Sapienza, H.J. and Crijns, H., Vlerick Leuven Gent Working paper series 2003/19

¹² For example Luthans, F., Stajkovic, A. and Ibrayeva E. (2000) “Environmental and psychological challenges facing entrepreneurial development in transitional economies”, Journal of world business, Vol.35, No.1

Raising more international SMEs will require raising more international entrepreneurs. This calls for early interventions preferably in the educational system, to actively promote greater exposure to the international environment and demonstrate the benefits of an international orientation.

On the short term this calls for policies on continuous education for SMEs, particularly in the area of language acquisition¹³. But more importantly Government policies could consider the relevance of this driver in order to boost the pool of future international entrepreneurs¹⁴ by promoting greater awareness and exposure to foreign cultures, supporting early language acquisition and fostering the acquisition of entrepreneurial attitudes and internationalisation. A relevant example could be:

Empresa Joven Europea – EJE (Asturias-Spain¹⁵)

The programme has been included in the secondary education curriculum as an optional subject and is aimed at students aged 12-16 years. Throughout a full academic course, students start up and manage import-export companies involved in real trade activities with student companies abroad. Students will communicate via video-conference and e-mail with partner companies abroad, place and dispatch orders and sell imported goods at the local trade fair. Eventually, profits are distributed among the partners of the company and a portion of profits goes to an NGO or any other community project.

Besides fostering the entrepreneurial skills of pupils, the programme considers new technologies as an integral part of the teaching-learning process. Also, positive attitudes are promoted toward foreign language learning as an instrument of communication between partner mini-companies located in different countries.

The other drivers to internationalisation are access to know-how and technology, increased efficiency and economies of scale, increased competence by entering difficult markets, exploiting the advantage of leading edge technology which are closely related to innovation. This will be further analysed under policies.

3.2 Main barriers to the internationalisation of SMEs

Successful policies to increase the number of internationalised SMEs must start by understanding which are the main problems faced by SMEs when considering the possibility to start operating with a foreign partner. According to the OECD¹⁶ the main barriers to greater internationalisation as reported from SMEs are:

1. Shortage of working capital to finance exports;
2. Identifying foreign business opportunities;
3. Limited information to locate/analyse markets;

¹³ A 2007 study focusing on language skills of SMEs in Norway based on more than 600 interviews found that almost 40% had lost valuable contracts due to bad language skills.

¹⁴ A strong proponent is to be found in “Why are some Spanish manufacturing firms internationalizing rapidly? The role of business and institutional international networks”, Belso-Martínez, J.A., Entrepreneurship and regional development, 18 May 2006, 207-226

¹⁵ Extracted from Mini-companies in secondary education. Best procedure project: final report of the expert group, European Commission, Directorate-General for Enterprise and Industry, September 2005

¹⁶ Final background report of the OECD-APEC joint project on "Removing barriers to SME access to international markets" OECD-APEC Global Conference, 6-8 November 2006, Athens, Greece

4. Inability to contact potential overseas customers;
5. Obtaining reliable foreign representation;
6. Lack of managerial time to deal with internationalisation;
7. Inadequate quantity of and/or untrained personnel for internationalisation;

These problems are consistently repeated along other surveys¹⁷ and could be grouped in the three SME's main areas of concern:

- 1. Insufficient managerial time and/or skills required for internationalisation**
- 2. Lack of financial resources**
- 3. Lack of knowledge of foreign markets, mostly consequence of the previous two**

A successful and sustainable internationalisation will require an internationalisation strategy and the acquisition of a series of capacities, abilities and resources prior or at the first steps of internationalisation. This is probably the explanation for the **proven relation between competitiveness and internationalisation**¹⁸. Interestingly this relationship between internationalisation and productivity at firm level is valid both for exports and for imports. This latter being consistent with knowledge and technology acquisition through imports of intermediates and capital goods.

Empirical research has associated successful small firms with greater skills in **organizational learning**¹⁹ and **strategy development**²⁰. Numerous studies have shown that companies with a structured market strategy are more active exporters than firms lacking formal planning²¹. Sadler-Smith et al.²² identified a positive relationship between organizational capabilities and small business performance

Regardless of the specific name being used, **organizational capabilities are consistently found to be important in explaining sustainable growth** within the small business development literature²³.

¹⁷ Just to mention one: UNECE (BSEC workshop, Kiev 1997) states that the main internal barriers for SME exports are: lack of information, lack of capital and insufficient management skills, including lack of languages.

¹⁸ A list of relevant literature can be found in "SMEs, FDI and financial constraints" by De Maeseneire, W. and Claeys, T.

¹⁹ Chaston, I., B. Badger, T. Mangles, and E. Sadler-Smith (2001). "Organizational Learning Style, Competencies, and Learning Systems in Small, UK Manufacturing Firms," *International Journal of Operations and Production Management* 21(11), 1417–1432.

²⁰ Julien, P. A., and C. Ramangalahy (2003). "Competitive Strategy and Performance of Exporting SMEs: An Empirical Investigation of the Impact of Their Export Information Search and Competencies," *Entrepreneurship Theory and Practice* 27(3), 227.

²¹ Diamantopoulos and Inglis 1988; Burton and Schlegelmilch 1987; Denis and Depelteau 1985; Cavusgil 1984; Cavusgil and Nevin 1981

²² Sadler-Smith, E., Y. Hampson, I. Chaston, and B. Badger (2003). "Managerial Behavior, Entrepreneurial Style, and Small Firm Performance," *Journal of Small Business Management* 41(1), 41–67

²³ The 2 previously cited and Dickson, P., W. Schneier, P. Lawrence, and R. Hytry (1995). "Managing Design in Small High-Growth Companies," *The Journal of Product Innovation Management* 12(5), 406–415

Other studies, comparing exporting and non-exporting firms discovered that companies with formal market planning were more likely to be active exporters, while firms lacking formal market planning failed to enter foreign markets. Also, the more systematic the selection of foreign target markets the higher the export performance will be for SMEs.²⁴

This underlines the importance of support in the area of managerial competences for those SMEs considering internationalisation. It also starts to hint one of the main SME problems in terms of internationalisation readiness: the severe SME lack of international strategy. This situation is closely related to size²⁵: on average the smaller the SME the more management building capabilities required. Small SMEs tend to have lesser structured management procedures and a tendency to making opportunistic rather than systematic strategic decisions.

There is certainly concern that SMEs have usually resorted to using support services in a rather haphazard and ad hoc manner, reflecting the particular needs perceived at any given point in time by the key decision makers themselves rather than using such support services as part of a strategic approach to internationalisation.

A structured management system is fundamental for a successful internationalisation and may be one of the key elements that hinder further SME internationalisation.²⁶ This already point out to one of the main areas of support.

The lack of financial resources to tackle internationalisation is another key impediment for many SMEs and has been consistently reported in surveys as one of the main areas where support is required. Policies or programmes that fail to incorporate the financial dimension of internationalisation will not be providing support that not only is demanded but required from SMEs willing to internationalise. Programmes dealing with this issue are mentioned in chapter 5.3.

Programmes to support SMEs in their lack of knowledge of foreign markets are also discussed in chapter 5.3.

²⁴ The Role of Systematic International Market Selection on Small Firms' Export Performance Brouthers and Nakos (Jsbm 2005)

²⁵ Kristos Kalantaridis "Internationalisation, Strategic Behaviour and the Small firm: a comparative investigation"

²⁶ "Strategic orientation, management characteristics and performance: a study of Spanish SMEs" Aragón Sánchez, A. and Sánchez Marín, G.; Journal of small business management 2005, 43 (3), pp287-308 and also "the role of management characteristics in the internationalisation of SMEs. Evidence from the UK retail sector" Hutchinson, K., Quinn, B. and Alexander, N.; Journal of small business and enterprise development, Vol.13, No.4, 2006, pp513-534

4. LEVEL OF INTERNATIONALISATION OF EUROPEAN SMEs

Internationalisation: Business activities responding to the opportunities and challenges that globalisation brings.

SMEs represent 99% of SME across Europe and similar figures around the world. Yet their level of internationalisation and weight in world trade is substantially below that number. According to the Observatory of European SMEs²⁷ only 8% of total EU27 SMEs are involved in exports, only 12% of the inputs of an average SME are purchased abroad and 5% of SMEs in the EU receive some income from foreign business partnerships, either from subsidiaries or joint ventures abroad. These results are not dissimilar to those of the 2003 Observatory of European SMEs which stated that 63% of SMEs are active only in their home country²⁸.

This picture broadly coincides with the evidence gathered from Member States²⁹. In Romania SMEs represent 99.6% of total companies but only 90% of exporters and a very modest 27.5% of total exports. In Finland 82 % of SMEs don't see any need to increase international activities and the international market is significant to only 4 % of SMEs.

On a positive note, numerical evidence reported at national level does support some progress in internationalisation, particularly from new Member States³⁰, even though starting from a very low base. In the Czech Republic SME imports have more than doubled from 417 to 998 billion crowns and exports have nearly trebled from 263 to 744 billion crowns in the period from 1997 to 2005. As expected, a large percentage of this growth can be explained by the incorporation of those countries into the EU.

Internationalisation by SME size

Not all SMEs present the same internationalisation profile. The latest data confirm that internationalisation is related to company size. As an example, the chart shows the import intensity of EU companies by size.

Percentage of inputs purchased abroad (% , EU27)

Size class	EU27 SMEs	11,7
	1-9 persons employed	11,5
	10-49 persons employed	13,3
	50-249 persons employed	15,8
	250+ persons employed	17,6

²⁷ Flash Eurobarometer 196- Observatory of European SMEs, European Commission

²⁸ Some controversy exists on the actual number: a paper by KPMG based on survey conducted in 2007 on 840 SMEs indicates that 53% of SMEs are already internationalised. The 2002 Observatory of European SMEs 2002 /No. 1 "Highlights from the 2001 Survey " states that 20% of the SMEs are engaged in exports.

²⁹ IfM Bonn citing the Federal Statistical office indicates that only 10.9% of German SMEs were exporters in 2002 (SMEs in Germany. Facts and Figures 2004, IfM materialen no.161, IfM Bonn 2004)

³⁰ Bulgaria, Czech, Estonia, Cyprus, Latvia, Lithuania, Hungary, Malta, Poland, Romania, Slovenia and Slovakia

This tendency is also reflected when plotting other internationalisation aspects like exports or external foreign direct investment: the larger the size of the SME, the more internationalised. This relation between size and internationalisation is universal across all EU 27 countries. For example, in the case of Finnish SME exporters by size

Company size	% of exporters
1-9 employees	17
10-49	30
50-249	54
SME Total	20

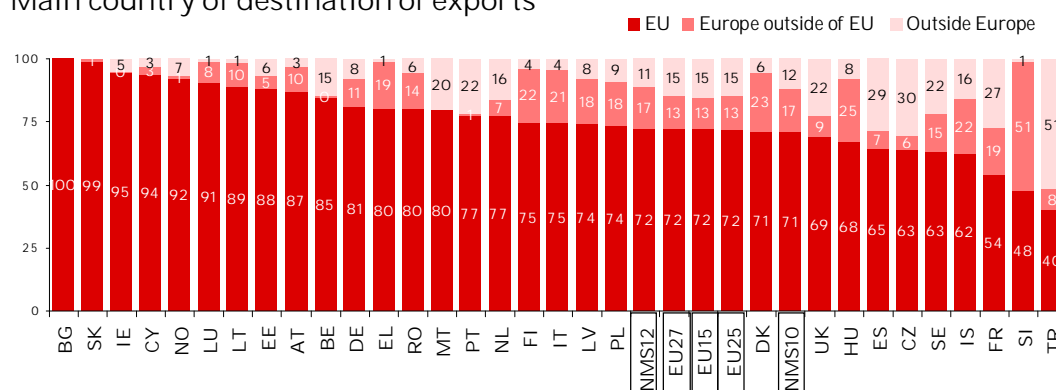
This fundamental relation between size and internationalisation is one of the most relevant and will be studied in greater detail later.

Internationalisation by trade partner countries

For any European country the internal market remains the key partner any internationalisation activity. In terms of trade the EU represents 2/3 of total trade for the average Member State.

The importance of the internal market as the key partner is even more accentuated in the case of SMEs. The table below shows the relative importance of the internal market for European SMEs.

Main country of destination of exports



For all countries bar Slovenia and Turkey trade is primarily focused on the EU. This also reflects that SMEs tend to interact more with countries across the border rather than distant ones. This predominance of the EU as the key market remains universal and constant across all SME sizes.

Prime destination of exports (% of exporters, EU27)	EU country	Europe, outside EU	Outside Europe
EU27 SME	72	13	15
1-9 persons employed	73	14	13
10-49 persons employed	71	9	20
50-249 persons employed	73	11	16

Sectoral differences

Considering only trade flows the importance of the EU as the key partner for SMEs is also reflected across all sectors of activity.

Prime destination of exports	(% of exporters, EU27)	EU country	Europe, outside EU	Outside Europe
D. Manufacturing		73	12	15
F. Construction		72	17	10
G. Wholesale and retail		66	14	20
H. Hotels and restaurants		97	0	2
I. Transport, storage and communication		83	9	7
J. Financial intermediation		85	11	3
K. Real estate, renting and business activities		77	13	10
N. Health and social work		92	8	0
O. Other community, social and personal service		83	16	0

As the previous chart corroborates services are even more dependent (in terms of trade) on the EU market than products.

Trends

The study “EU Industry structure and the single market” indicates a particularly relevant increase in intra-industry trade which has grown faster than total trade, particularly inside the EU. Trade in intermediates is growing and domestic production increasingly relies on foreign inputs. This seems to indicate very clearly that further integration both at a global level (globalisation) and most particularly at an European level (full consolidation of the internal market) have been gaining momentum in the last number of years.

The data on FDI and capital flows³¹ underline the previous statement and indicate strongly that even for SMEs internationalisation is growing beyond just foreign trade. Again, for European SMEs the destinations of foreign business partnerships are more likely to

³¹ Intra-EU FDI flows (inflows+outflows) account for 80% of total EU FDI flows in 2004-2005. North America represents half of the remaining 20% both for inflows and outflows. Source: European foreign direct investment yearbook 2007, Eurostat.

remain in Europe: 77% of the locations of all joint ventures and foreign subsidiaries mentioned are in the territory of the EU.

Key facts on the internationalisation of European SMEs

The level of internationalisation of European SMEs is low.

Level of internationalisation is closely related to company size. There seems to be plenty of scope for growth in the number of internationalised SMEs, particularly the smallest (micro and small) companies.

Even though trade beyond EU has gained weight in the last 10 years as a percentage of both imports and exports, **for the average European SMEs Europe remains the main and key trade partner**³² across all sectors and company sizes and even more so in the case of services.

SMEs themselves are showing that **internationalisation is growing well beyond just exports** and moving into more developed levels of co-operation.

³² The evaluation of the Dutch PSB programme, based on a survey of actual users (Dutch SMEs) reported that “there is no reason to emphasise distant markets”

5. POLICIES TO SUPPORT THE INTERNATIONALISATION OF SMEs

5.1 The importance and rationale of public support

Internationalisation of SMEs in the form of export promotion has been a prominent element in European Government policies for a long time: the first Internationalisation Agency³³ was founded in Finland in 1919 and nowadays all European Governments devote a considerable amount of resources to the issue. Italy, for example has a Ministry for International Trade.

Programmes to support SME internationalisation have traditionally been focused on promoting greater exports and usually developed independently from other policies. In fact, approximately 70% of all of them are focused exclusively on supporting exports. For these programmes it is estimated that 1 € of support produces a 40 € return in terms of increased exports³⁴ which proves their **high value in terms of return for investment**.

Yet the most potent argument in favour of governmental support lies on the fact that SMEs play a key role in the stability and potential of any national economy. As most SMEs face resource limitations, they need to be supported to acquire the capabilities needed to compete successfully in the international market.

Traditionally Government support has been based on the “level field” concept: as **SME lack the expertise and resources of multinational enterprises (MNE) they need support to create a “level field” of competition**.

Lately a third approach is emerging. It is based on the fact that **SMEs are likely to benefit disproportionately from the pro-competitive effects of internationalisation**³⁵: internationalisation provides the SME with both growth and increased competitiveness, and is thus a fundamental engine for its long term sustainability.

Studies³⁶ have shown that **government support measures based on building capacities and supported by consultants produce a high level of “additionality”**: an important number of SMEs in these programmes wouldn’t have internationalised without the Government support.

³³ Other common names are Trade Promotion Agency (TPO) and Export Promotion Agency (EPA)

³⁴ The World Bank estimates that \$1 of export promotion produces a \$300 increase in exports for the median Export Promotion Agency. Source: Daniel Lederman, Marcelo Olarreaga, Lucy Payton, Trade note 30, International trade department, The World Bank Group, 30 September 2006

³⁵ “The decision to enter and exit foreign markets: evidence from UK SMEs”, Requena-Silvente, F., Small business economics (2005) 25, pp 237-253

³⁶ “An evaluation of public support measures for private external consultancies to SMEs in the Walloon region of Belgium”, Lambrecht, J. and Pirnay, f., Entrepreneurship and regional development, Vol.17, No.2, pp89-108

5.2 Policies to promote greater SME internationalisation

One of the central concerns of Governments and support organisations must be the low numbers of SMEs involved in internationalisation which may be curtailing their future growth and competitiveness. In order to maximise the effectiveness of government funds devoted to supporting internationalisation of SMEs policies should consider:

- **A successful policy for internationalisation must consider the barriers that impede or restrain the internationalisation of SMEs and the drivers** that move companies to internationalise. The former is essential to produce results in the short and medium term. The second creates the basis for a long term policy on internationalisation.
- For increased effectiveness **each country will have to build its own set of policies based on “on the ground” experience** and focused around the actual SMEs they are trying to support. Increased and regular co-ordination between the Central Government, the support agencies and sectoral, local and regional actors should be improved as the best way to guarantee best use of available resources. **A fluid, integrative and consultative process between all the stakeholders (Government, support agencies and SMEs) is possibly the best key for successful policy development.** In the case of Romania the business community was involved both in the creation (in 2004) and currently the management of the National export Council, the body charged with developing national export policy.³⁷ Both UBIFRANCE and EVD in the Netherlands have representatives of the private sector in the board of directors.
- In the dilemma between concentrating support on a short number of winners (usually companies that have already started their internationalisation process) or providing support to the larger number of non or minimally internationalised companies **the greater effort must be placed in increasing the number of internationalised SMEs.** Evidence from studies³⁸ supports this second approach as the most efficient in the long term. This also supports the fact that there is a performance advantage in rapid internationalisation. That is, the earlier a company internationalises the faster it seems to grow.³⁹
- **Internationalisation is a moving target.** The level of internationalisation of the SME is related to its size and resources. The problems and the corresponding support measures required will have to change as the company evolves and grows⁴⁰.

³⁷ “Linking business communities to export markets”, Costin Lianu, General Director, Ministry for SMEs Trade, Tourism and Liberal Professions, Co-ordinator of National Export Strategy. International Trade Forum-issue 2/2007

³⁸ De Clercq, D., Sapienza, H. and Crijns, H. “The internationalization of small and medium firms” Small business economics 24: 409-419, 2005 shows that internationalisation is one of the main engines for further internationalisation.

³⁹ “Defining international entrepreneurship and modelling the speed of internationalisation” Oviatt, B.M. and McDougall, P.P., Entrepreneurship theory and practice, September 2005

⁴⁰ Experts and studies coincide in signalling the stage of internationalisation of the SME as the most important variable in the internationalisation of SMEs. “SME exporting challenges in transitional and developed economies” Neupert, K.E., Baughn, C.C. and Dao, T.T.L., Journal of small business and enterprise development Vol.13, no.4, pp 535-545

- **Micro and Small companies present a vast internationalisation potential.** In terms of export potential a recent Dutch research has found that the export-participation ratio of 1 person SMEs is 6.9% and 9.9% for 2-9 person firms. This contrasts with the average for the Dutch SMEs which is 9.5%. Also, in recent years an impressive increase has been reported in the 1 person firm category.
- One of the main reasons for non utilisation of support is **that enterprises lack awareness.** In general smallest SMEs do not have the desirable knowledge about the support measures⁴¹ due to the lack of resources devoted to internationalisation. **This calls for a simplified information and access points.** Yet the common situation is of numerous and often un co-ordinated support institutions providing what some SMEs describe as a “Promotion Jungle”. In terms of actual support in Germany only 34% of micro SMEs (up to 10 employees) participate in promotion programmes in contrast to 54% for medium sized companies (50 to 250 employees) and 70% for companies of over 500 employees⁴².

The Finnish KiVi-project provides a concept and a platform for organising events where information on internationalisation services and instruments is distributed. Each seminar is organised locally and ideally all local actors join in at the planning stage in order to include all relevant experiences about the needs and preferences of local enterprises.

- Effective support to SMEs must consider the variables that influence the process of internationalisation: available financial and human resources, company size and stage of internationalisation, sector, geographical location, target markets, etc. All this strongly supports an approach based on **individualised support to each SME** and the implicit recognition that internationalisation goes well beyond the international department of the company.

From policies for internationalisation to policies for competitiveness

As stated in previous chapters there is a strong relation between all competitiveness policies. Just as with internationalisation, the main support to promote more innovation intensive start-ups⁴³ should focus on the promotion of management skills, supporting the creation of trans-national networks, bridging the financial gap and the need for government support.

In the case of high tech firms usually characterised by intense competition and shorter windows of opportunity, early internationalisation is fundamental to increase their economic success⁴⁴.

⁴¹ This is also supported by “SME perspectives on business support services” Boter, H. and Lundström, A., Journal of Small business and enterprise development, Vol.12, no.2, 2005, pp 244-258. In a survey of 1000 Swedish micro and small enterprises (of up to 49 employees) there was a clear direct relation between size a number of contacts with support organisations.

⁴² Barriers to SME Access to Promotion of Foreign Trade and Investment Dr. Christian Hauser, Institute for SME Research Bonn, Germany

⁴³ Main recommendations of the OMC-SMEs expert group on the design of measures to promote growth of young research intensive SMEs, European Commission 2006.

⁴⁴ Internationalisation of High-Tech Start-Ups and Fast Growth - Evidence for UK and Germany, Burgel, O.; Fier, A.; Licht, G. and Murray G.C.; ZEW discussion paper No. 00-35, 2000

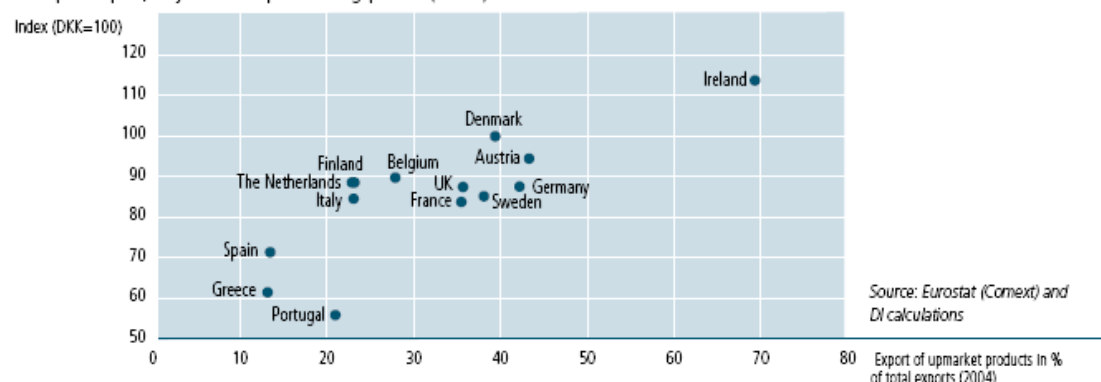
In addition to sharing common drivers, SME innovation and internationalisation are inversely related to the size of the company and share the same main barriers: lack of financial resources and lack of management skills. Another area of potential synergies between innovation and internationalisation is in the management of support programmes to “born globals”. These are companies usually associated with a new technological development, that internationalise extensively shortly after inception and in a very short period of time.

Building on this and on the proven relationship between technology, knowledge, productivity and exports⁴⁵ a trend is starting to appear fundamentally in the most advanced countries towards **integrating policies for competitiveness and growth**. Internationalisation is starting to be merged with the other (particularly innovation) policies and they are starting to be seen as part of the same issue: policies to enhance sustainable long term competitiveness.

The graph⁴⁶ shows that there is a direct relationship between wealth and export of high value added production.

Wealth through upmarket product exports

GDP per capita, adjusted for purchasing power (2004)



In fact **as sectors and progressively countries move up the value chain the rationale for the integration of internationalisation and innovation** into a single set of competitiveness policies **becomes more evident**.

Enterprise Ireland integrates all competitiveness and growth policies under one umbrella: innovation, IP, internationalisation management training and human resources audits.

Finland is launching the growth company service concept merging the services of 4 business support agencies into a service that identifies potential growth companies, analysis, action plan and follow up based on a single account manager and specialist.

⁴⁵ “Exports and economic performance”, Aart Kray and “Lessons from empirical research on international technology diffusion through trade and foreign direct investment”, B. Hoekman and B. Smarzynska Javorcik, both in “Global integration and Technology transfer” edited by B. Hoekman and B. Smarzynska Javorcik (2006). Also “Review of the Literature: the role of international trade and investment in business growth and development” Harris, R. and Cher Li, Q., September 2005, UKTI, DTIref:UKTILITREV 05/01

⁴⁶ Extracted from « Global benchmark report 2006. Ready for globalisation ? », p.77, Dansk Industri

In Norway innovation, internationalisation and regional development are contemplated in the same perspective.

But it is critically important to remember that innovation is a lot more than research. It comprises:

- Technological innovation
- Innovation in operations and management

In relation to SME competitiveness, for the vast majority of companies there is a large potential for innovation in operations and management, including the acquisition of IT and quality systems and capabilities.

To further highlight this point it is important to remember that “marketing” entrepreneurs will go international before “technical” entrepreneurs and that innovation at plant level is not a guarantee *per se* of improved or increased performance⁴⁷.

In this sense, greater use of the possibilities offered by IT and support for greater use of e-commerce and CRM systems (just to mention two examples) point one way forward and can be the most relevant innovation strategy for small companies, crafts and services. In this area the Spanish programme PIPENET sets a good example of workable support.

The Spanish programme PIPE NET run by the Spanish Institute for Foreign Trade with the financial backing of the European Commission provides a strategic plan to the companies structured through meetings with the company carried out by a consultancy service. The plan includes two research projects: the first refers to the situation of new technologies in the targeted countries and the second to companies of reference within the Internet sector. It also contemplates the needs of the company concerning technologies, budget and personnel.

PIPENET optimises new technologies, information and communication (TIC) for participating SMEs by using personalized consultancy services and the most appropriate technology tools.

During the first year after the delivery of the final documentation, the consultancy service is at the disposition of the SME to offer technical assistance in relation to the plan.

As part of SME innovation standardisation plays a key role in fostering the competitiveness and growth of SMEs. This has also been identified as one important element for SME greater involvement in global value chains⁴⁸.

The Polish scheme to support businesses’ internationalization via product certificates was introduced after exporting companies showed that product certificates can constitute a genuine barrier in entering a new market.

Turkey is supporting and promoting quality development in SMEs as a key for increased export performance.

⁴⁷ Adegbesan and Ricart, IESE working paper no 668, Jan. 2007

⁴⁸ “Enhancing the role of SMEs in global value chains: final synthesis report”, OECD, 25 May 2007

5.3 Programmes

Programmes are the set of activities that implement policies. They are the tangible support to SMEs. In as much as all support programmes are valid, this chapter will focus on the set of critical programmes to support internationalisation.

a) Individualised support

Individualised support is based on the analysis of the individual SME, the identification of the areas where support is needed and the provision of it based on the specific resources and capabilities of each individual SME.

These programmes usually start by screening the “internationalisation readiness” and are usually followed by long term consultancy support to help companies build the management capabilities required for internationalisation. These programmes are usually complemented by a series of measures to provide for the other areas of commonly required support: information and sometimes support on finances for internationalisation, access to information, networks, etc.

Individualised support programmes are both holistic in their view of the company and tackle the individual barriers to internationalisation of each SME. They are in fact a “programme of programmes” whose focal point is to establish a sustainable internationalisation strategy for the individual SME⁴⁹.

Individualised support programmes provide a large component of additionality. Participating SMEs in the Dutch programme PSB (Starters in foreign markets) which is based on the principle of guided support report that 1/6 would have not exported to the target market without PSB and 1/2 of all are still exporting regularly after their participation in PSB. 44% of participating companies started exporting earlier thanks to PSB.

In the case of the UK almost 10,000 SMEs have passed through or are on the programme Passport to export since November 2001. The results for April/June 2007 indicate an estimated benefit of £244,000 per SME and a satisfaction level of 87%.

In the case of the Spanish programme PIPE. 4.994 companies have benefited from it since 1998. On average, exports increased by 71.1%, total revenues by 24.8% and personnel by 13.5% in the participating companies.

It is important to remember that internationalisation is about enhanced competitiveness and the analysis must contemplate all forms of potential internationalisation.

The Swedish programme “Move or Stay & Improve” aims to give SMEs deeper information on more variables than just labour cost in other countries in order to create more secure decisions in international business. It is a computerized tool where the SMEs

⁴⁹ Supporting this holistic and individualised support “Profiling the capabilities of SMEs to compete internationally”, Grimes, A.; Doole, I. and Kitchen P., journal of small business and enterprise development, Vol.14, No.1,2007

own result report and balance sheet are the basic documents. Figures for 18 different factors are filled in to compare the situation in 10 different countries. In the calculation it is possible to see how the company's revenue will change if they move the business to different countries. The tool is currently being developed to simulate different improvement activities if the company chooses to stay at home and to see what effect these activities should bring to the company's revenue.

This tool makes companies work with their productivity instead of moving production. This strengthens the European dimension because the companies are encouraged to think about many ways of cooperation with European companies instead of Asian production.

In principle FDI tends not to be one of the main lines of internationalisation at least in the initial stages. For example only 2% of Dutch SMEs invested abroad in the period 2002-2004. Yet these numbers can only be expected to grow in particular with the full implementation of the Services Directive by 2009. This is an area where programmes must be able to grow.

Particularly since the main external barriers for SME FDI are existing laws and regulations and lack of support and/or advice, elements that could be successfully tackled by support.

b) Financial support

One of the main barriers to SME internationalisation is the lack of financial resources⁵⁰ as access to sufficient and affordable finance is a fundamental pre-requisite for internationalisation. Government programmes must focus on the provision of expertise (usually associated with individualised programmes) on the available financial support mechanisms.

For trade related finance existing mechanisms (trade credit insurance, guarantees, factoring, etc.) the level of information and availability is good across most European countries.

The Dutch internationalisation agency has created a web file in the site www.internationaalondernemen.nl which presents the products of the private financial sector, the state, the EU and multilateral institutions including products like export-credit-insurance, international credit rating, factoring, venture capital, payment habits, leasing and checklists, which can be very useful for cross border finance. Products are grouped together and presented in a simple and user friendly way. The site also provides terms and price comparisons for the products

Yet there is a documented⁵¹ and considerable lack of support for further stages of internationalisation like cross border investments particularly for the comparatively small amount commonly demanded by an SME: 46% of Dutch SMEs with FDI invested less than €100,000 abroad and a further 35% invested an amount between €100,000 and €1,000,000⁵².

⁵⁰ Also Bell, J. "A comparative study of the export problems of small computer software exporters in Finland, Ireland and Norway" International business review, Vol.6, No.6, pp.585-604

⁵¹ "SMEs, FDI and financial constraints" by De Maeseneire, W. and Claeys, T.

⁵² Source: OECD

Lack of finance for growth companies.

For an SME financial preferences lean towards internally generated funds, then external debt and equity being the last option⁵³. This highlights the importance of access to debt for growth project such as internationalisation.

Royalty scheme from Malta offers SMEs the possibility of pledging a piece of the future sales against an advance provided by the investor avoiding the need to sell an equity stake. The measure provides access to finance for projects that are considered to risky for support through loans. Activities covered include SMEs undergoing a market penetration strategy based on internationalisation but also development of new products/processes, innovative knowledge-based start-ups.

A pan-European venture capital market is non existent valid step forward would be to mutual recognition of venture capital funds and their management companies⁵⁴

An additional possibility would be to consider a widening of the JEREMIE scheme to include the intra European dimension of internationalisation. Also the EIB could also play a part in supporting SME investments in co-operation with national institutions

c) Networks

Networks expand the capacity of the individual SME to internationalise and remain one of the vital components of support to internationalise. Networks can be of two different types: support networks and co-operation networks.

Support networks tend to be managed by the government (Commercial offices abroad) or big business associations. They play a key role as a support measure for any type of internationalisation as they provide access to information that is directly usable by the SME. In this role they cover one of the areas of greater demand and need from SMEs

The German AHK-network with its 120 Offices of German Chambers, Delegates and Representatives of Commerce Abroad (AHK) in 80 countries on every continent offers information services and consultation for SMEs on external markets worldwide. AHKs mediate about 100,000 business contacts per year. The services include information on import and export regulations, customs duties, investment conditions abroad, currency regulations, market opportunities and marketing strategies for German companies. They also provide advice and help to establish international business contacts. Basic information is free of charge but detailed analysis and specific individual consulting have to be paid.

Co-operation networks are focused on promoting direct co-operation between companies. Studies indicate that co-operative approaches, alliances and networks involving SMEs will intensify in the future.

⁵³ Nummela, N., Loane, S. and Bell, J. "Change in SME internationalisation: an Irish perspective" Journal of small business and enterprise development, Vol.13, No.4, 2006.

⁵⁴ "Expert group report on removing obstacles to cross-border investments by venture capital funds", European Commission DG Enterprise and Industry, 2007.

Eight out of ten co-operating SMEs report that co-operation strengthens their competitive position with little variation between countries. Also companies that co-operate reported higher growth than non co-operating companies.⁵⁵ Networks constitute a way to get access to key resources, notably knowledge and as such an important route to growth⁵⁶. A particular case of this type of networks is supply chains which promote enhanced competitiveness through a process of learning by doing.

Unsurprisingly, the characteristics that favour entry and success into a co-operation arrangement closely mirror those of internationalisation⁵⁷

ECONET Platform: Business cooperation for Austrian, Slovak and Czech SMEs within the triangle Vienna - Bratislava - Brno www.advantageaustria.org

The aim of the programme is to improve the situation of SMEs in the border regions by providing or increasing the levels of information, consulting, training measures, cross-border networking and co-operation between SMEs to foster innovation and competitiveness through intensive business co-operation. The programme features Business Clubs, Business cooperation meetings in all participating countries, seminars, consulting for SMEs and business studies.

As one of the most relevant support networks in Europe the European Commission's Enterprise Europe network could play an important role in linking businesses together in particular in the area of long term SME co-operation.

Both types of networks are important. The relative importance of one or the other will be closely linked to the activity of the SME. For classic sectors which tend to internationalise through stages support networks are vital. For new fast moving sectors, for "born globals" development networks provide better support.

d) Sectoral programmes

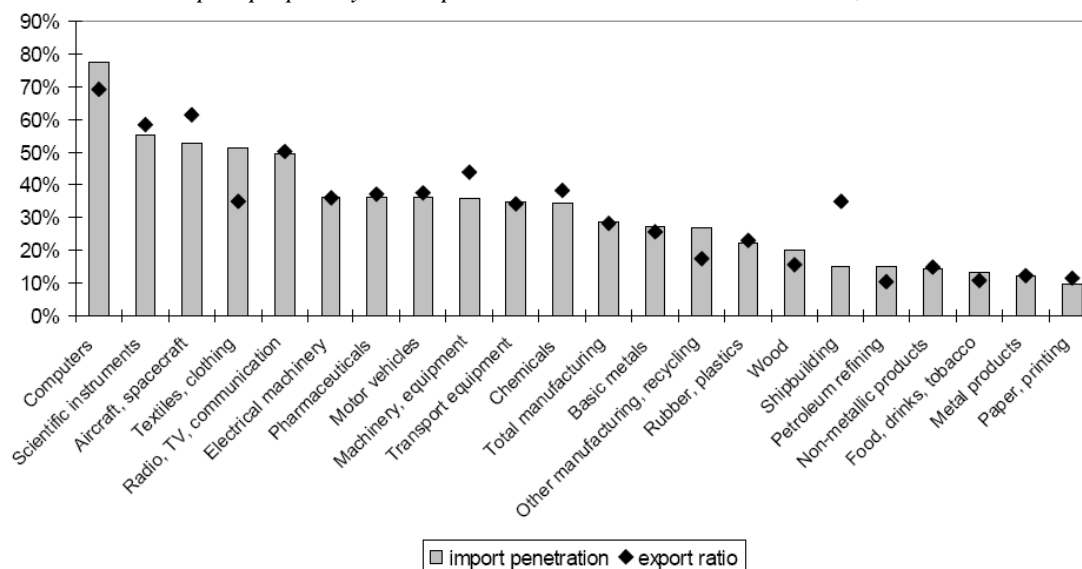
Sector does play an important part in "exposure" to foreign markets as **not all industries are equally affected by globalisation**. High and medium-high technology industries are on average generally more internationalised than less technology-intensive industries. In this respect no fundamental difference exists between product sectors and service sectors.

⁵⁵ Observatory of European SMEs. 2003/5 SMEs and co-operation, European Commission 2004

⁵⁶ High growth SMEs versus non high-growth SMEs: a discriminating analysis, Moreno, A.M. and Casillas, J.C., Entrepreneurship and regional development, Vol.19, No.1, January 2007

⁵⁷ Promoting the co-operation between SMEs in Europe: The Technofocus experience, a study by Javier Merino, Public University of Navarre, lists 8: prior experience in co-operation, prior experience in international trade, financial situation of the firm, spirit and capacity for innovation, level of education, age of entrepreneurs, presence of a leader and willingness to take risks

Import propensity and export ratio in selected OECD countries, 2003



Note: 1. The export ratio measures the share of production that is exported (i.e. X/Y); the import propensity shows to what degree domestic demand is satisfied by imports M (i.e. $M/(Y-X+M)$).

2. OECD includes Austria, Canada, Denmark, Finland, France, Germany, Italy, Japan, Korea, Netherlands, Norway, Portugal, Spain, Sweden, United Kingdom, and the United States.

Source: OECD (2005a).

This is already important for small, high income countries which tend to have more industries in high value sectors. Ireland has increased its share of exports of computer services more than 22 times and the income from those exports by a factor of 27.

In particular, companies in the high technology sectors must be specialised and niche-oriented order to compete. In this case or where significant sector specific challenges emerge a recommendation could be to set up a tailor made programme for this.

This could be particularly relevant for technological sectors. An example is the programme “Gateway to California” operated by the Business Innovation Centre of La Fucina in Milan:

Objective: to introduce small innovative ICT and Biotechnology companies in Silicon Valley. This was challenging because Italian companies were not famous in these sectors and area and small Italian companies tend to work only locally.

The programme selected 20 best practices from more than 200 companies based on Swot analyses and partner search with Californian experts. This was followed by the organisation of a week of one to one meetings for the final 10 selected companies with big and medium US companies, universities and research centres, venture capital companies and public and institutional actors

Both strategy and outcome were different from other programmes as companies had a more global perspective looking not only for new markets but also for know how, technology, finance, partners, suppliers etc.

In relation to sectoral programmes an interesting example emerges from Sweden where imports are considered the edge for the competitiveness or even survivability of certain sectors, for example the textile and music industries⁵⁸. This not only illustrates the link between import and greater propensity to export but the importance of keeping competitiveness as the driving goal of the internationalisation policies.

e) Successful programmes

The main recommendations are:

- National level is the most adequate for the development of policies and programmes (rather than regional or local). But it is fundamental that implementation is close to the SMEs which requires full collaboration with regional and local actors. This also provides the ability to identify and the flexibility to develop and adapt programmes.
- Co-ordination of all actors is paramount to avoid repetition of programmes and waste: too many programmes focused on the same topic or support. This should also help prevent a “support jungle” and ease SME access into support programmes.
- Programmes must focus on the main issues for SME internationalisation and reduce the risks and barriers associated with internationalisation (reduced resources and lesser access to information).
- Programmes must target management and focus on capacity building for which training and consulting are fundamental. Programmes must help create or consolidate a long term internationalisation strategy for the SME rather than short term progress.
- Internationalisation is for all SME, regardless of size. But for programmes to be effective, scanning of companies and “negative screening” must be introduced. An example would be a system like Norway’s “Ready, Willing and Able” in their *Regional Programme to promote the export and internationalisation of SMEs*⁵⁹
- Tailoring support to the individual SME and sufficient network support must play a central role in governmental programmes. Internationalisation is a moving target which will vary not only with the evolution of markets but with the evolution of SMEs themselves. Programmes must consider the stage of internationalisation of the SME and dispose of tools to cover different aspects of the internationalisation of SMEs.
- The focus must be supporting long term co-operation between companies rather than trade development: search of partners rather than customers.
- Evaluation of programmes is a valuable tool to analyse the effectiveness of support and also to identify those areas where further support is required. User surveys seem to be the most adequate instrument for this.

⁵⁸ This case is highlighted by “Born global: internationalization in the creative industries” by Professor Staffan Gullander, Stockholm University, School of business

⁵⁹ More information available in “Supporting the internationalisation of SMEs. Good practice selection”, European Commission, chapter 3, practice 1.

- The EU could play a valuable role in three main areas. First, widening JEREMIE or a similar scheme to include the intra European dimension of internationalisation could be a valuable contribution. Another option would be considering a possible role for the EIB in supporting SME investments in co-operation with national institutions. Finally promoting greater businesses links in particular in the area of long term SME to SME co-operation through European Commission's Enterprise Europe network could also prove to be a valuable source of support.

5.4 The role of Internationalisation agencies

Internationalisation agencies (IAs), also known as export promotion agencies or trade promotion agencies are the bodies charged with implementing the programmes to support SMEs. In 2002 a benchmarking study undertaken for OSEC business network⁶⁰ reviewed IAs in 8 western countries and concluded that the IAs were still needed. Also the number of customers that seeks assistance validates the need of IAs.

Preferably IAs will have a sufficient level of capillarity. The ability to deliver support locally or regionally is best as it permits to individualise services. Also SMEs prefer a local or regional contact point 4 times more than a national or 8 times more than a European level.⁶¹

Ideally IAs should be based on the one-stop-shop principle to facilitate greater and easier access to SMEs, particularly for the smallest ones.

Brandenburg Economic Development Board has combined 5 different tasks - inward investment, technology promotion, foreign trade promotion, start-up promotion and energy saving consultancy. Some German regions have already followed this example, such as Berlin, Schleswig-Holstein or Baden-Württemberg as synergies can be won. The basic advantage is that this model permits to develop a deep and broad knowledge of the region's economy and companies. For the companies it is also easier, as they can easily identify where to go to if they need support. Functions cooperate closely, permitting a comprehensive and synergistic support to the SME.

⁶⁰ Reynolds, A. (2002), Benchmarking Study of Trade Promotion Structures Undertaken for Osec

⁶¹ "Support services for micro, small and sole proprietor's businesses" European Commission, DG Enterprise, April 2002, Vienna and own elaboration.

6. THE THREE DIMENSIONS OF INTERNATIONALISATION: CROSS-BORDER, INTRA-EU AND OUTSIDE THE EU

When considering internationalisation, the geographical dimension is not the most relevant issue. An SME will search for those countries where it can maximise its competitive advantage be it in terms of increased exports, better suppliers or cost or market advantage if considering investment abroad.

The European dimension

Intra-EU trade represents approximately 30% of total world trade. Yet the internal market remains under-explored for European SMEs: the single market counts for less than 1% of revenues. In addition **just one in four EU15 companies engage in trade of products or services with new Member States**. And they are mostly large firms and companies in the industry sector.

Less than one in two firms confirms that they regularly sell products or services to other Member States in the EU as a whole.

The EU still is a less integrated trade area than the USA: the ratio of intra US states exports to GDP is around 70% higher than the ratio of intra EU-15 exports to GDP. Even though internal trade among members of the EU is relatively well integrated and has evolved to more elaborated forms (higher intra-industry trade, and higher FDI inflows as a % of GDP) the border effect still remains substantial. For example, trade inside the EU is a third what it could be if relative income and distance from market were the only determinants of trade⁶².

This demonstrates **the potential to further boost intra-EU trade**. But the trade boosting effect of the internal market is not limited to the promotion of intra-EU trade. Integration boosts the dynamism and competitiveness of EU businesses. The development of the single market has delivered an increase of 2% or 225 billion euro (2006 figures) to EU GDP.

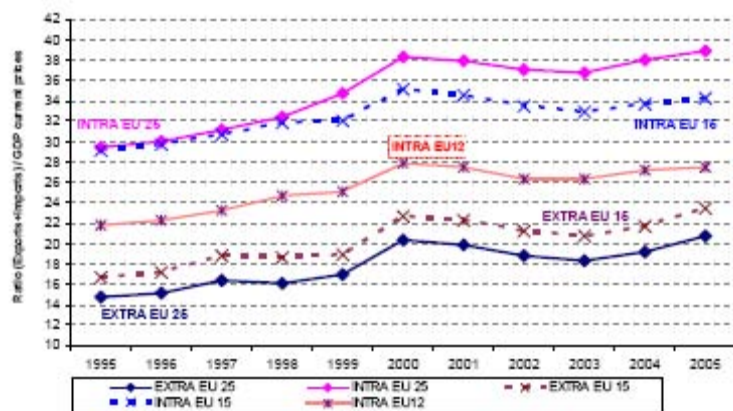
A study has found that 2004 enlargement has spurred the regional internationalisation and strengthened the intra-union competitiveness compared to external regions such as Russia or China⁶³.

The internal market has helped the EU to improve its export performance: foreign trade has increased from 6.9 to 12.3% of EU GDP from 1992 to 1995. It has also improved productivity, up to 2% in some sectors.

The following graph confirms the increasing openness of the EU economy as the share of extra EU trade to GDP has grown.

⁶² OECD economic surveys: European Union, 2007

⁶³ Hilmeresson, M. and Sandberg, S. "EU enlargement effects on international trade in the Baltic sea region" presented at the 9th Vaasa conference of international business, Vaasa - Finland



Source: Eurostat

The internal market as a tool for growth

The internal market has the potential to be a main engine for SME growth. It can allow SMEs to gain size and competitiveness which in turn will allow them to face international competition better, both at home and abroad.

In this respect two groups could particularly profit:

1. Companies in the **services sectors** which account for 70% of employment and value added but only 20% of intra-EU trade.
2. Micro and small companies, particularly in the crafts sector. For these direct SME co-operation is a natural match. Sectoral matchmaking events could be one of the most relevant measures. Clustering can also be a very instrumental in supporting the internationalisation of crafts, as in the case of example vertical (or horizontal) integration inside a protected denomination of origin (PDO), just to mention one example.⁶⁴

This would call for action in two areas that seems to concentrate the main problems:

- **Information support:** sometimes the main problem surrounding a border is regulatory requirements. This could be particularly relevant to small services providers. Information and support to deal with regulations across the border does facilitate cross-border internationalisation. A good example of support is set by the Austria Service by the Chamber of crafts of Munich⁶⁵.
- **Technical barriers:** despite the fundamental principle of free movement of goods, many companies still face **technical barriers** when exporting to another Member State as the authorities require goods coming from other Member States to be adapted to their national technical rules. Cases presented at the EICs prove that this issue ranks 1st

⁶⁴ Bertolini, P. and Giovanetti, E present an example in "Industrial districts and internationalization: the case of the agri-food industry in Modena, Italy", Entrepreneurship & regional development, 18 July 2006, 279-304

⁶⁵ Selected as a 2007 good practice for the Berlin European Charter of Small Enterprises Conference http://ec.europa.eu/enterprise/enterprise_policy/charter/2007_charter_docs/gp2007en.pdf

in the SME complaint list⁶⁶. This is particularly relevant in the case of services. **If mutual recognition were used, bilateral trade in commercial services would increase by 30 to 60%** The Commission has tabled a proposal for a regulation which will require national authorities who deny market access to duly justify their decision⁶⁷.

The main problem throughout Europe is the existence of different regulations: fiscal, complaint resolution, regulations in consumer transactions... which affect all companies but particularly services and retail. Greater uniformisation would provide a boost to trade.

In principle a lot is to be expected from the future advent of the Services Directive to come into force at the end of 2009. Exports of services, which have been growing at an average 3.8% in real terms for the last 25 years, will certainly experience an increase. But the most fundamental shift will probably be the substantial increase in SME cross-border investment as more companies settle throughout the other Member States.

⁶⁶ Euro Info Centre Network & IPM feedback mechanism – Overview of activities July 2003-December 2004

⁶⁷ Commission proposal COM(2007) 36 final
http://ec.europa.eu/enterprise/regulation/goods/mutrec_en.htm

7. CONCLUSIONS AND RECOMMENDATIONS

It is difficult to separate internationalisation from the context in which it is a natural element: competitiveness and growth. This calls for **a more integrative “holistic” approach in all the areas related to supporting the internationalisation of SMEs**: in the development of policies, programmes and in the delivery of support. It will also require policies to upgrade the human resource base of the economy. Addressing this through education and training policies will require a growing focus on life-long learning.

Policies to support internationalisation should start by considering the drivers and the barriers for SME internationalisation.

A long term policy outlook should consider policies based on the main driver to internationalisation: positive attitudes toward entrepreneurship and international activities, which calls for interventions in the educational system.

More immediate **support should be based on supporting SMEs in the areas of reported need**: lack of managerial resources and skills for internationalisation, lack of sufficient financial resources and availability of usable information.

Government support for the internationalisation of SMEs remains vital. **SMEs are likely to benefit disproportionately from the pro-competitive effects of internationalisation and government support produce a high level of “additionality”**: an important number of SMEs wouldn't have internationalised without the Government support.

Countries are not competitive, companies are. As it has been shown internationalisation cannot be separated from a company's competitive position. And each company will have its own set of individual variables and barriers for competitiveness. Consequently, **the most effective way to guarantee a successful long term internationalisation is to provide individualised support for each company**, beyond supporting the merely “international” part of the company.

Successful support will have to be based on building capabilities inside the SME where access to training and consulting should play a central role. This will require scoring, filtering and analysing companies prior to providing any support and adapting the mix of (usually) standardised support programmes to create a company specific support plan.

All key stakeholders must be involved in the development of policies and programmes: regional and national bodies, internationalisation agencies, business representatives and banks. This is conducive to developing support that is required by the SMEs, avoid overlapping of programmes and maximise allocation of resources.

Development of policies is probably better co-ordinated at national level. But for maximum results implementation must be at local or regional level.

In order to enhance competitiveness and growth, **programmes must support internationalisation, not only exports**. The main internationalisation programmes must permit the participation of the widest number of SMEs possible.

Programmes must be demand driven and adaptable. They must incorporate feedback from SMEs in order to evolve as SME needs shift.

A strong emphasis must be placed in **supporting and promoting networks** at all possible levels.

Internal size is conducive to greater competitiveness in the international arena. In this respect the potential of the internal market is far from fully exploited as the internal market could act as a breeding ground for international companies that may become global players. **Support of direct SME co-operation, matchmaking, promotion of intra-European value chains and co-operation between SMEs-MNEs** could be conducive for greater competitiveness and growth

An important effort must be placed in **raising SME awareness of the need to internationalise**. Ideally this should be coupled with an easy access to support based on the one stop shop principle.

Internationalisation agencies have to become customer led and customer centred and offer comprehensive support. This also opens the door for service integration which is conducive to additional synergies. Some examples:

Malta Enterprise has merged the three agencies in charge of trade promotion, investment promotion and support to SMEs acting effectively as a one stop shop both for foreign and local companies

Enterprise Ireland is the result of merging the industrial development agency and the trade development agency.

The Dutch EVD agency for internationalisation is becoming part of the Enterprise Europe network and merging with promotion of foreign investment will also include foreign based offices.

8. PROJECT DESCRIPTION AND PARTICIPATING EXPERTS

This report is part of the project “Supporting the internationalisation of SMEs” by the European Commission’s Enterprise and Industry Directorate General. The goal of the project was to **understand the forces that facilitate and prevent the internationalisation** of SMEs and **identify existing policies that encourage and support SMEs** and provide **recommendations on how public policies can support SMEs** efforts to achieve international growth.

The present report is based on the oral and written contributions of the group of experts listed below. In addition to this report, the group also identified and selected a series of good practices in promoting internationalisation of SMEs published in a separate brochure.

The project spanned from November 2006 to December 2007. The group met four times.

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