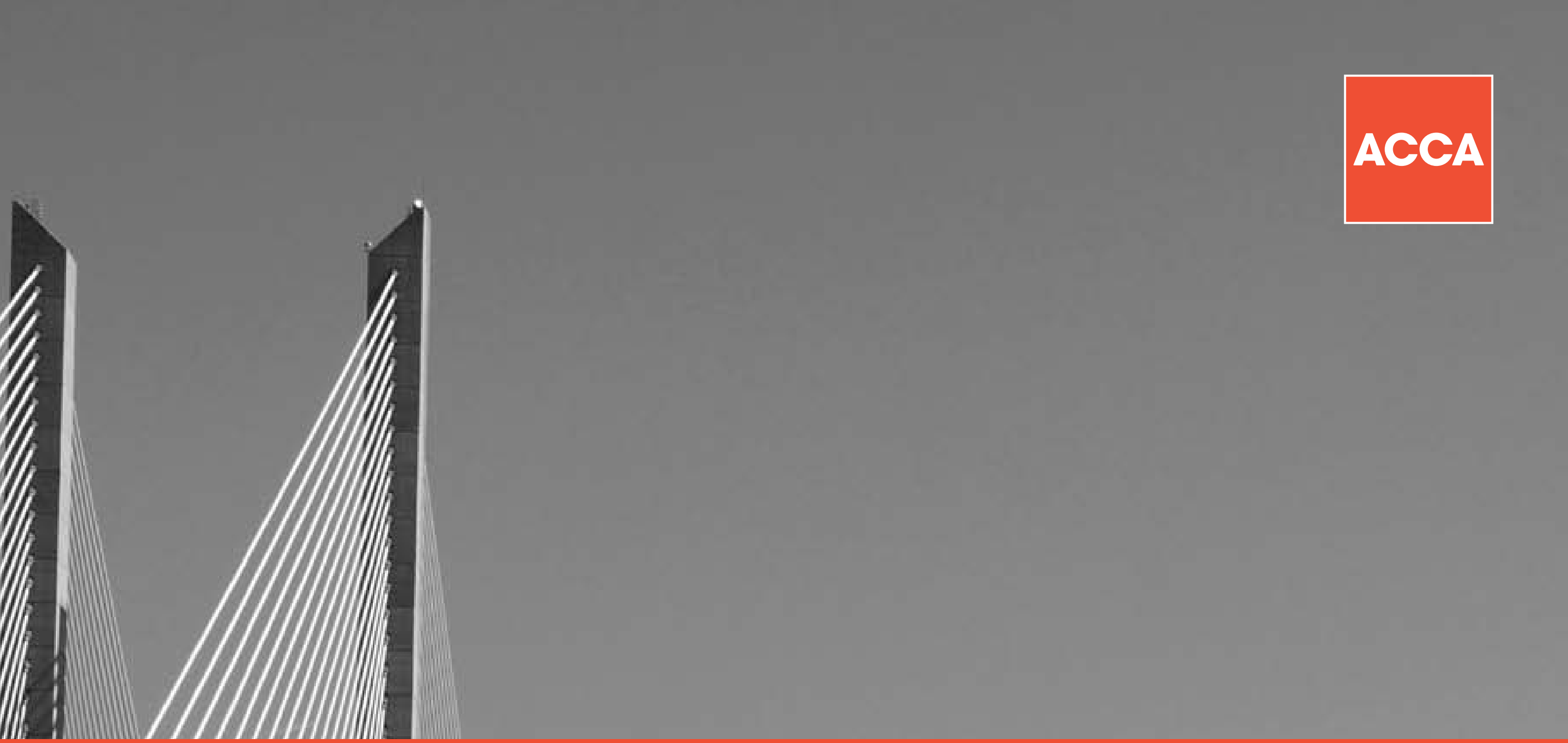

Tapping into SME international potential

About ACCA

ACCA (the Association of Chartered Certified Accountants) is the global body for professional accountants. We aim to offer business-relevant, first-choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accountancy, finance and management.

Founded in 1904, ACCA has consistently held unique core values: opportunity, diversity, innovation, integrity and accountability. We believe that accountants bring value to economies in all stages of development. We aim to develop capacity in the profession and encourage the adoption of consistent global standards. Our values are aligned to the needs of employers in all sectors and we ensure that, through our qualifications, we prepare accountants for business. We work to open up the profession to people of all backgrounds and remove artificial barriers to entry, ensuring that our qualifications and their delivery meet the diverse needs of trainee professionals and their employers.

We support our 162,000 members and 426,000 students in 170 countries, helping them to develop successful careers in accounting and business, with the skills needed by employers. We work through a network of over 89 offices and centres and more than 8,500 Approved Employers worldwide, who provide high standards of employee learning and development.

ABOUT ACCA'S GLOBAL FORUMS

To further its work, ACCA developed an innovative programme of global forums which brings together respected thinkers from the wider profession and academia around the world.

www.accaglobal.com/globalforums

About the ACCA Global Forum for SMEs
The ACCA Global Forum for SMEs provides a unique platform for promoting the role of SMEs in the global economy. Representing over 15 countries and a wide range of professional backgrounds – from finance institutions, academics and professional advisers to entrepreneurs themselves – the Forum represents the sector's needs at a global level and facilitates the sharing of best practice.

This paper presents a number of recommendations for increasing SME presence in international trade. Aimed at policy makers and broader business support stakeholders, the paper identifies critical success factors that hinder cross-border trade for SMEs, as well as areas in need of further development that remain under-exploited by policy makers and business owners alike.

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Tapping into SME international potential

Globalisation of business is often seen as synonymous with the rise of gigantic multinational corporations, and hence SMEs are thought to have only a marginal role to play in this process. In fact, the proportion of SMEs (even the smallest ones) engaged in international activity is much greater than is often assumed (European Commission 2010) and, with the rise of e-commerce and increasing globalisation of markets, it is thought to have been growing rapidly.

Reported levels of internationalisation vary substantially between countries. In 2006, the OECD estimated SMEs' contribution at around 30% of exports and 10% of foreign direct investment (FDI) (OECD 2006). SMEs' contribution to the total value of exports varies from 8% in Australia (Ergas and Orr 2007), 19% in Malaysia (NSDC 2007) and 25% in Pakistan (SMEDA 2007) to 30% in the US (USITC 2010), 40% in India (MSME 2010) and 68% in China (Hall 2007). More than two-thirds of Singapore's SMEs (69%) are internationally active (Fernandez 2010), against 44% of European SMEs, which in turn are more likely to be internationalised than those in the US or Japan (European Commission 2010). Although the different SME definitions employed in these countries have much to do with these variations, there are other, more systematic differences that bear upon the extent of SMEs' international activity.

International activity comes with many benefits for SMEs. There is evidence that those SMEs that have greater levels of internationalisation tend to report higher turnover growth. European SMEs that export grow more than twice as fast as those that do not, while 'internationally active' SMEs are three times more likely to introduce products or services that are new to their sector than those that are entirely domestic in orientation; SMEs that are internationally active show higher employment growth (European Commission 2010). Internationally active businesses are also more likely to be, or to grow into, larger firms (Di Giovanni et al. 2010). Even in fairly large economies, SMEs typically have no option but to export if they wish to grow substantially (Blackburn et al. 2008). Finally, international firms can improve their productivity after exporting (OECD 2013).

Yet, for all its benefits and close correlation with growth and higher productivity, SME internationalisation is a difficult proposition. Would-be international enterprises need to stay abreast of market and public policy developments in one or more foreign markets, and navigate the bureaucracy of foreign countries in addition to their own domestic rules, often with little local knowledge or resources. They need to adopt new working practices and quality standards, and overcome barriers in language and business culture as well as limitations in the skills and outlook of their own management and staff. They need to make provision for late payment and enforce claims against customers in unfamiliar legal systems; they also need to provide for exchange rate volatility, usually without access to efficient hedging products or the option of structural hedging. Internationalisation is further complicated by the need to establish and maintain partnerships with larger organisations, which, in addition to their often different business practices and culture, can also be the senior partner in unequal relationships.

All the above factors create genuine market failures that governments have an important role in addressing and the ACCA Global Forum for SMEs identifies some critical factors that create these persistent market failures, as well as some areas for further development that are yet to be fully exploited by policymakers and business owners alike. The Forum believes that the issues outlined here are common to many countries and business owners around the world and hence point towards significant potential for collaboration and sharing of best practice.

THE INTERNATIONALISATION AGENDA IS WIDER THAN EXPORTING ALONE

The internationalisation of SMEs not only takes the form of export activity, but also involves importing, foreign direct investment, international subcontracting and international technical cooperation. Once all of the above activities are taken into account, ACCA's research shows that internationalisation of high growth firms is present in 50% of firms across all the major economies (ACCA 2012). Despite this, government policies are often overtly focused on exporting, overlooking the benefits of other forms of internationalisation. For example, not only do firms that import perform better than non-importing firms, they are also around one-third more likely to go on to export (European Commission 2010). Importing also has a direct benefit for performance: although all SMEs that are internationally active show higher employment growth than firms that operate purely domestically, non-importing SMEs increased their work force by only one-quarter of the increase seen among those that import (2% versus 8% in the year). Importing therefore is not only an important first step to internationalisation more generally, but also carries direct performance gains by sourcing important efficiency gains in its own right. Policies directed at SME internationalisation need to reflect this more explicitly, and make sure that this is appropriately reflected in governments' business support frameworks.

INDIRECT EXPORTS

Through the supply chain, indirect exporters form a significant springboard to international activity for many SMEs. For this reason, the relationship between large and small firms remains crucial and is an often-forgotten dimension in government policy. Through participation in global value chains, both SMEs' awareness of opportunities in international markets and their understanding of the potential advantages and possibilities increase (OECD 2007).

Although much of the SME participation in global value chains would not technically register as export activity, it provides access to new business practices; skills, technological advances, standards and information, which all come with greater exposure to international business. As a result, SMEs' internal capacity is increased and thereby their ability to engage in international markets.

Better understanding of how global supply chains improve SMEs' capacity and even lead to more direct involvement in international markets by SMEs should inform government policy aimed at increasing SME internationalisation. While indirect exports may not be a new source of international activity, the capacity building within SMEs that it may result in can provide an important springboard to more direct international export opportunities. These dynamics need to be better understood, and encouraged by governments, international institutions and business associations.

GOVERNMENT SUPPORT

Enabling innovative firms to move beyond borders is one of the key areas in which governments have a direct role in improving the competitiveness of SMEs. Innovative small firms may often find that domestic markets are too limited for their niche or highly technical product or service, and being able to access markets across borders enables them to commercialise their innovations and grow as a result. Governments should work towards removing barriers to cross-border trade to enable small firms to access international markets. Initiatives by the European Union, the Caribbean Community, the Association of Southeast Asian Nations, and the Southern African Development Community already exist and have promising potential to broaden markets for the SME sector. These should be used as a policy vehicle to enable small businesses to take their products and services to wider markets.

Moreover, government efforts need to be coordinated at an international level. One of the key constraints in greater SME participation in global markets is the inability to absorb the demands of multiple business environments. For that reason, any efforts towards greater internationalisation of infrastructures relating to standards, intellectual property rights, financial markets, dispute resolutions and regulation more generally will greatly enhance global trade, and most importantly SME participation within it.

REGULATION STARTS AT HOME

Governments that are looking to encourage SME international activities still need to focus their efforts on the domestic business environment. Although complexities in dealing with foreign legal systems and regulations are often cited as a major challenge by business owners and policymakers alike, the regulatory environment in the home market still affects businesses' ability to engage in international trade. In fact, much of the cost of exporting is already accumulated before the product or service leaves the domestic market. Tariffs and other domestic trade barriers in the home country are cited by up to one-third of SMEs across Europe as a barrier to international trade and this finding is even more pronounced among those SMEs wishing to export beyond the European market (European Commission 2010). Coordination of the various aspects of the domestic enterprise agenda across government departments should therefore always seek to reflect the needs of internationally active SMEs.

BETTER USE OF ADVISERS

Advisers are especially important in addressing SME internal barriers to internationalisation – from management capacity and organisational structure to ensuring that the right finances are in place to support the SME's international ambitions. Ensuring that SMEs have access to the right external advice can help business owners ensure that their strategy reflects important internal resource limitations, and it provides a stronger footing for moving beyond borders. SME advisers themselves need to develop better skills to advise SMEs on international trade. These advisers range from branch managers in high street banks, who need to have better knowledge of specialist export finance products, to accountants, who need to strive to develop better international networks.

SMEs find it especially difficult to form international relationships with foreign business partners and potential customers. ACCA provides a vital global network, into which SMEs can tap via their own ACCA-trained finance directors and managers or their professional advisers in ACCA-accredited firms. For example, ACCA already has an active and fast-growing *LinkedIn* member network, which is used for regional discussions and for making international connections among individual members. ACCA recognises social media as a unique enabler for international connections and will seek to make social media platforms more efficient for such engagement in the future.

EXPORT FINANCE

Research shows that the banks' specialist export products are heavily under-used by SMEs – or perhaps ill-suited for SMEs in the first place. Only a very small minority of SMEs claim to use export finance (BDRC 2013). As a rule, banks are not always good at cascading information on such niche products to all managers and branches, so it is possible that they are responsible for some of the low uptake. Business owners themselves therefore tend to finance their export activity through general finance, which does not address the various risks associated with international business such as fluctuating foreign currencies, longer lead times, and greater uncertainties over dispute resolution. The uptake of more specialist products that are offered by government institutions is equally low (Edinburgh Group 2013). For this reason, governments and finance institutions need to ensure that the export finance offered is relevant to and affordable by small businesses, and along with business advisers, seek to increase awareness of their availability and benefits.

STAYING CLOSE TO HOME VERSUS ACCESSING FAST-GROWTH MARKETS

It is acknowledged that SME international activity tends to start close to the home market and that this pattern becomes firmly established, with small businesses rarely seeking to export to markets beyond their own continent (Edinburgh Group 2013). The continuing economic turbulence that started with the financial crisis in 2008 resulted in little or no economic growth in many developed economies, raising some fundamental questions around the opportunities that remain untapped in developing and frontier economies further afield. For example, except for imports from China, business with other BRIC countries is underdeveloped in the EU, making up only about 7–10% of the export market (European Commission 2010). Policymakers and SME owners alike perceive high-growth markets to have higher entry barriers (OECD 2013).

At the same time, ACCA's research report, High Growth SMEs: Understanding the Leaders of the Recovery (ACCA 2012), shows that the fastest-growing businesses across the leading economies build domestically first, before becoming international. Hence the path to fast-growth seems to lie in encouraging nascent entrepreneurs to grow strong in domestic markets first, and then to look for international markets for accelerated growth.

This natural tendency in SMEs to remain close to a home market, or grow domestically first, must be appropriately reflected in government policy and the perceived and actual higher cost of entering markets further afield must be fully addressed. A more targeted approach for business support provision to SMEs entering 'high-growth markets' is therefore justified, ensuring the widest possible access for business owners rather than a 'picking winners' approach.

NETWORKS AND CLUSTERING

Owing to the inherently limited resources and management capacity within SMEs, networks (defined as a group of firms using combined resources to cooperate on joint projects – OECD 2000) and clusters (defined as an agglomeration of firms in a related line of business – OECD 2000) represent excellent opportunities for small businesses to launch their international ambitions on a stronger footing. By combining expert knowledge, skills and resources, and pooling efforts on product development, market research and overseas contacts, SMEs are able to access a variety of benefits that would not be available if they operated in isolation. Further still, the economies of scale and opportunities that are opened up through clusters and networks not only allow small firms to compete on a par with larger businesses, but also overcome many of the inherent market failures that are closely tied to the size of firms, which no amount of policy intervention could hope to address fully.

While most economies have some programmes in place to develop clusters and networks within specific industries or sectors, the effectiveness of such programmes is patchy and there is still significant scope for international learning to ensure that best practice is shared and more widely adopted; this is especially the case for bridging the success rate between developed and developing economies (UNIDO, undated). Furthermore, the potential for development of cross-regional and cross-border clusters remains underexploited but contains significant potential for allowing SMEs to derive maximum benefits from increasing momentum towards regional economic integration across the world.

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