

Growth Dynamics and Development Problems of Small and Medium Enterprises

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Small and medium enterprises (SMEs) have a great significance for developed market economies and represent the basis of their economic development. They make around 99% of the total number of enterprises within these countries and employ more than two-thirds of the available workforce. This paper analyses the growth and survival of SMEs and the problems of their development. In the end of the paper, the marketing orientation as a foundation for steady growth and development of SMEs is emphasized, as well as the need for implanting the marketing concept into cultural norms of these enterprises.

1. Introduction

There are many categorizations by which small and medium enterprises (SMEs) can be defined. These categorizations can be quantitative, as well as qualitative.

Nevertheless, the main criterion for the size categorization of an enterprise is quantitative and is focused on the number of employees. According to this categorization, there are: (1) micro enterprises (1-9 employees), (2) small enterprises (10-49 employees), medium enterprises (50-249 employees) and large enterprises (250 or more employees).

SMEs, which represent the first three categories listed, i.e. up to 249 employees, are the main force of the development of market economies. They usually make a large majority of the total number of companies, which makes them the fundamental driver of entrepreneurship and the whole economy.

This is the main reason why it is necessary to understand more comprehensively the manner in which they operate, as well as their growth dynamics and development problems. In-depth knowledge on these issues will greatly increase the chances of long-term growth and development of SMEs, and therefore the whole economic system in which they operate.

2. The importance of SMEs in a market economy

SMEs are a very important economic segment of each country and their primary role is similar throughout the world. Although not a large number of employees are working in small or medium enterprises, a large number of these enterprises causes that the majority of workforce within each country is working in an enterprise of this size. This means that SMEs do contribute

significantly to the total employment rate. In addition to this role, their other role can be seen through their entrepreneurial activities and contribution to raising the overall level of competitiveness. This is accomplished by their massiveness, as well as their increased offer of competitive products and services [16].

SMEs are also very important in international context because their main characteristics, such as flexibility and networking ability, are enabling them to be a strong competitive threat to a number of large multinational and transnational corporations in various aspects of their operations. Because of their size, SMEs are usually more adaptable and better prepared for the changes in their environment. Their proximity to markets enable them to obtain information regarding their environment in a much more simple manner, which allows them to respond more promptly in comparison with their larger counterparts and make all the necessary changes in their organization and processes in a timely manner [24].

SMEs are one of the driving forces of economic development in already developed market economies. They stimulate initiative, inventiveness and entrepreneurship, while their characteristics enable them to be much more flexible than large companies, which is one of the main preconditions for adaptability to changes in the environment. These are only some of the reasons why a large number of SMEs exist in all developed countries, thus indicating their extreme importance.

In the year 2005, within the EU-27, almost 20 millions of enterprises were active within the nonfinancial sector, out of which 99.8% were SMEs. Their share in employment was 67.1% of available workplaces at

that moment, while their value added amounted to 57.6% of the total value added. In 2005, SMEs within EU-27 employed 4.3 persons on average. This average had significant variations between the member countries, e.g. the highest average of 12 employees per SME was in Slovakia, while the lowest average of 3 employees per SME was in Czech Republic (data from 2004) and Greece [22]. Some of these indicators are illustrated in Table 1.

	Σ	SMEs	Micro 1-9	Small 10-49	Middle 50-249	Large >249
Number of enterprises (in millions)	19.65	19.60	18.04	1.35	0.21	0.04
Share in percents (%)	100.0	99.8	91.8	6.9	1.1	0.2
Number of employees (in millions)	126.7	85.0	37.5	26.1	21.3	41.7
Share in percents (%)	100.0	67.1	29.6	20.6	16.8	32.9
Value added (in billions of euro)	5360	3090	1120	1011	954	2270
Share in percents (%)	100.0	57.6	20.9	18.9	17.8	42.4
Workforce productivity (1000 euros per employee)	42.3	36.4	29.9	38.7	44.8	54.4
Share in percents (%)	100.0	86.1	70.7	91.5	105.9	128.6

Table 1. Enterprise key indicators according to their size within the nonfinancial business sector in EU-27 in 2005 [22]

It ought to be noted that the number of SMEs within the EU-27 in 2007 increased to a lesser extent and now amounts to 20,409,000 which is an impressive percentage when compared to 43,000 large enterprises [1].

Based on these facts, one can easily comprehend the great importance of SMEs for the EU economy, primarily due to their share in the total number of enterprises. This is why SMEs in the EU are usually called “the backbone of economic development“.

The importance of SMEs for the overall economy of Serbia is also high. The SMEs sector is becoming an increasingly important segment of the economy during the structural reforms implementation, specifically its function of reviving the overall economic growth, job creation and poverty reduction. SMEs are therefore very important for the success of the transition process in Serbia, although the fact is that the economic results of the transition are far from expected.

The SME sector in Serbia is the most profitable segment of the economy. In 2006, SMEs (including entrepreneurs) accounted for 99.7% of the total number of en-

terprises, 63% of the total employment, while at the same time provided over 40% of total exports and 60% of total imports of the non-financial sector. Viewed from the prism of these data, it is clear that SMEs are the most profitable segment of the Serbian economy [13].

In 2007, SMEs (excluding entrepreneurs) accounted for 99.29% of the total number of employees. These data clearly emphasize the great importance of SMEs for the Serbian economy. Table 2 shows some Serbian enterprise key indicators according to their size.

	Total	Micro 1-9	Small 10-49	Middle 50-249	Large >249
Number of enterprises	84,109	71,065	9,874	2,572	598
Number of employees	1,097,913	146,307	203,091	271,543	476,972
Income (in millions of RSD)	5,079,482	886,631	1,213,891	1,013,667	1,965,293
Gross value added (in millions of RSD)	1,062,559	120,500	200,105	226,341	515,611

Table 2: Enterprise key indicators according to their size within Serbia in 2007 [13]

The importance of SMEs clearly indicates the need for studying their growth and development as the basic dimensions of their long-term survival. Before doing so, it is most important to comprehend that the growth is a quantitative and development is a qualitative category. Knowledge on the dynamics of these categories will greatly facilitate the process of their control, which will contribute to the reduction of the rate of their deterioration.

3. The growth and survival of SMEs

Growth and survival are the main problems faced by SMEs. The nature of small dimensions of these enterprises implies the need for growth as a basic condition for their survival and further development.

Simon and Bonini [23] have studied 500 largest companies in the U.S. in the period 1954-1956 and concluded that there was no difference in growth rates between companies of different sizes. Evans [5, 6] has, however, come to a completely opposite conclusion. He has found that the growth rate negatively correlated with the size of enterprise, i.e. small companies grow faster than larger ones. This conclusion has been also obtained by Hall [8], who observed only manufacturing firms.

The survival of companies is also a topic that has obtained a particular interest by scholars in recent years. The results of the research into manufacturing companies have shown that the survival rate of newly established companies is higher than the rate of their deterioration [3]. A similar conclusion came from Phillips and Kirchhoff [19], who have found that the survival rate increases along with the size of an enterprise and its age. They have also found that this rate differs between different industries, as well as between different sizes of firms.

Headd and Kirchhoff [9] conducted a study in the U.S. in the period 1992-2002 and came to many conclusions that are of great importance for understanding the growth dynamics and survival of SMEs. We highlight a few of them:

1. The number of SMEs in which the increase in employees is recorded is similar to the number of SMEs in which the decrease in employees is evident.
2. One cannot speak of the regularities from the empirical point of view according to which SMEs are rapidly growing in their first years of existence, after which the decline of this rate takes place.
3. The survival rates of SMEs are similar in different time periods.
4. Significant correlation between industries that have a high rate of growth and SMEs within these industries that also have a high rate of growth has not been discovered.
5. Industries with a large number of fast growing SMEs also have a large number of SMEs that are shrinking rapidly.

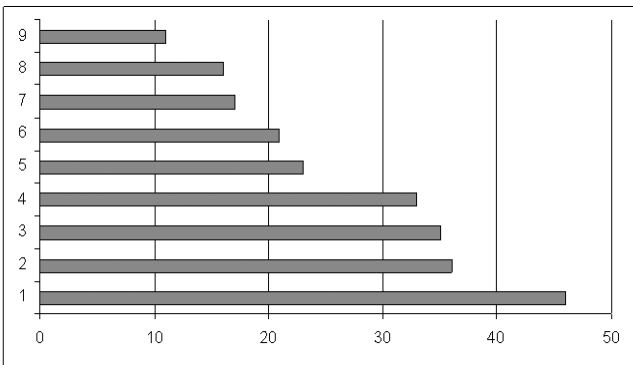
All these facts reflect the growth and survival of SMEs. Nevertheless, in addition to the growth dimension, it is very important to take a closer look on the development dimension of SMEs, i.e. the problems faced by SMEs during their development.

4. Development problems of SMEs

The problems faced by SMEs during their functioning and development are numerous. Due to their specific nature, they are far more sensitive to the occurrence of acute crisis situations than their larger counterparts. Thus, the need to emphasize some of the common problems they face is desirable. When problems are known, as well as their causes, the decision-making process regarding management actions that will contribute to avoiding or solving the issue at stake, is far easier.

It has been concluded in many studies that the two primary causes of SMEs bankruptcy are the lack of adequate managerial skills and lack of financial resources [26]. These are two main problems faced by SMEs in all market economies, which among other things supports the fact that SMEs need external support, i.e. outsourcing, primarily in the form of information and knowledge related to various aspects of the firm's operations (management, finances, marketing, production, etc). In other words, in contemporary conditions, SMEs are often not capable of developing and acting independently in the market. They ought to have their own core competencies they must continue to develop and thus become competitively superior in their respective business. They also need to establish different forms of cooperation with other individuals, companies and institutions in order to achieve the set objectives.

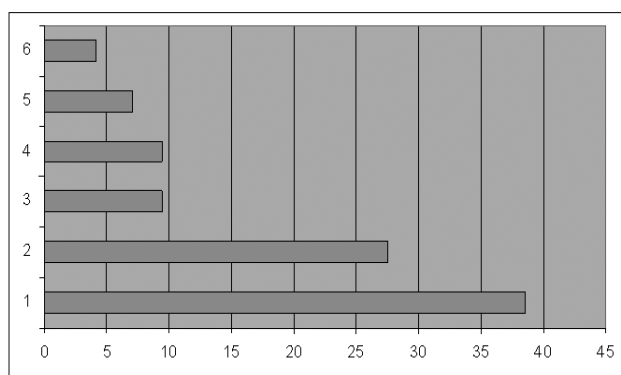
However, the survey that was conducted during November and December 2006 in the EU-27 on a sample of 16,339 SMEs revealed different results [25]. This research has indicated that limited purchasing power (46% of the sample), inadequate legislation (36% of the sample), lack of workforce (35% of the sample), and high labour costs (33% of the sample), are the most common problems that SMEs face. In the fifth place, inadequate infrastructure has been revealed (23% of the sample), while the lack of financial resources (21% of the sample) has been found in the sixth place, which is totally atypical when it comes to development problems of SMEs. The problem list continued with new technologies implementation (17% of the sample), new forms of organizing implementation (16% of the sample), and finally the lack of adequate managers (11% of the sample).



Legend:
 1 – population purchasing power; 2 – inadequate legislation; 3 – lack of workforce; 4 – high labor costs; 5 – inadequate infrastructure; 6 – lack of financial resources; 7 – new technologies implementation; 8 – new forms of organizing implementation; 9 – lack of adequate managers.

Figure 1. Development problems of SMEs within EU-27 in 2006

On the other hand, research studies conducted in this country show that the lack of financial resources is one of the main problems of SMEs development; e.g. research conducted by the Agency for SMEs and Entrepreneurship Development in 2006 in order to determine the major problems of SMEs and entrepreneurs in Serbia [4]. The study included 1,404 respondents who provide employment to a total of 14,485 people, which makes 13 employees per firm on average. The results have shown that the biggest problems for respondents are: lack of financial resources (38.5%), legislation (27.5%), lack of market information (9.4%), lack of skilled labour (9.4%), non-compliance with the standards (7.1%), lack of information on technologies (4.1%).



Legend:
1 – lack of financial resources; 2 – legislation; 3 – lack of market information; 4 – lack of skilled labour; 5 – non-compliance with the standards; 6 – lack of information on technologies

Figure 2. *Development problems of SMEs within Serbia in 2006 [4]*

Based on the presented results, we conclude that the problems faced by SMEs are numerous, but mostly generic, i.e. these problems are inherent in the very nature of SMEs.

Nevertheless, in addition to the above mentioned problems that represent the specific hindrance in SMEs development, the evident lack of marketing orientation is also a factor that contributes to the growth and development slowdown. All companies, regardless of their size, need to adopt the marketing concept as a basis of their growth and development.

5. Marketing orientation as a basis of growth and development of SMEs

Marketing orientation is a powerful source of sustainable competitive advantage for the following reasons: it is difficult to imitate all of its specifics, the firm focuses on finding opportunities for growth, and reduces the time delay between identifying and exploiting the growth opportunities [15]. Implementation of the marketing orientation in the firm and its fostering require leaders to pre-

viously institutionalize the values and behaviours that are inextricably linked to marketing orientation [14]. In other words, marketing orientation must be deeply embedded in the organizational culture in order to come to life in practice. In this regard, many authors advocate marketing orientation as a set of values and beliefs that are deeply incorporated in the culture of an organization. These values and beliefs direct the behavior of all organization members [18, 27], i.e. they are part of the permanent orientation of a firm towards creating and delivering superior values to its customers [17]. Relying on the concept of organizational culture [20, 21], numerous scholars have observed the marketing orientation as a critical aspect of culture within the company [10, 7].

Marketing orientation enables organizations to develop skills that will help them define their internal processes and link them with the environment. This will allow for them to become more competitive due to the establishment of connections with their customers, distributors and suppliers [2]. These organizations fully understand the importance of using information on customers and competitors when forming their own strategies. Thus, they are able to create a better offer and deliver more value to their target markets than their competitors [11]. Considering that the market orientation is a distinctive type of resource within the organization, it enables the organization to develop a specific competitive advantage [14], which is hard to imitate, causing it to become sustainable competitive advantage [12].

Based on aforementioned, it is quite clear that marketing orientation is the basis of growth and development of all enterprises, especially SMEs, which are far more sensitive to the market changes because of their size. Therefore, the pressure toward firms to implement marketing concept in all their processes actually originates from the increased level of competition in the market.

Conclusion

It is clear today more than ever that it is virtually impossible to achieve long-term economic position internationally without strong SMEs. Their outstanding entrepreneurial role makes them a solid basis for the development of a country's overall economy, through attracting foreign direct investments, employment reduction, increase in GDP and exports, as well as many other things.

The importance of SMEs is primarily reflected in their percentage of the total population of firms; e.g. in the EU over 99% of all enterprises are SMEs. Between 2002 and 2007, their number increased by 2 million, while the number of large companies rose by only

2,000. About two-thirds of all employees work in SMEs. Their contribution to employment growth during the period 2002-2007 amounted to 84% [1].

Based on these facts, the motivation, as well as interest in researching issues regarding the growth and development, as basic dimensions of SMEs functioning, ought to be clear. Without healthy SMEs, the economy of any country cannot achieve long-term development and secure itself a stable position in the world that is increasingly changing.

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