



Small and Medium-size Enterprises in 2010

Report of the SME Observatory

The SME Observatory's 2010 report has been drawn up within the same framework and following the principles adopted when it was first published in 2005.

This report draws on contributions from Observatory members involved in public support for SMEs. It highlights quantitative and qualitative changes in SMEs and their environment, while providing a basis for international comparisons, as well as information on the tools and concepts used to measure and describe the multiple facets of businesses in this category — over three million in all — that together represent the essential foundation for the future of the French economy.

The report has four main parts:

A **“General trends”** section analyses SME demographics (INSEE), the economic behaviour of these companies (OSEO) and their financial position (Banque de France). This section also includes a detailed presentation of the new category of intermediate-size companies (*entreprises de taille intermédiaire* or *ETI*) introduced in recent French legislation (DGCIS, the Competitiveness, Industry and Services Division of the French Ministry of Finance).

Under the heading **“Key themes”**, the report brings together the most recent data on employment (OSEO), innovation (*Ministère de l'Enseignement supérieur et de la Recherche*, DGCIS and OSEO), exports (*Direction Générale des Douanes*), public procurement (*Observatoire économique de l'achat public*) and payment terms (Altarex and Banque de France).

The **“Current Issues”** section focuses this year on German SMEs, analyzing the reasons for their competitive strength, in particular qualitative factors (CIRAC, *Centre d'information et de recherche sur l'Allemagne contemporaine*) and how they finance innovation (KfW Bankengruppe).

The 2010 report ends with a review of action taken by French authorities to support the development of SMEs (Caisse des Dépôts, OSEO and Médiation du crédit) and a summary of the main legislative and regulatory measures that concern them.

H I G H L I G H T S

The period under review raised hopes of recovery, encouraged by the most recent data. We have outlined key developments below.

BUSINESS START-UPS IN 2009: NEW REGIME FOR “AUTO-ENTREPRENEURS” SETS THE PACE

Business start-ups in 2009 showed a rise of over 75% to total 580,200, mainly as a result of the 320,000 launched under the *“auto-entrepreneur”* status for independent workers, which came into force on January 1, 2009. These were in nearly all sectors. Excluding *auto-entrepreneurs*, business start-ups declined by more than 20% from the previous year, although there is no way of determining how much of this is due to substitution effects.

At the same time, there was a sharp drop in business start-ups initiated by companies as opposed to personal businesses. The latter surged 152% during the year, with three-quarters under the *auto-entrepreneur* regime. Reflecting this, the proportion of new businesses without creation of payroll employment rose from 87% in 2008 to over 94% in 2009.

At January 1, 2009, there were 3,100,000 businesses in the competitive non-farm sector, of which 99% counted fewer than 50 employees.

RISE IN 2009 BANKRUPTCIES FOCUSED ON SMEs

The 14% surge in bankruptcies from 2008 to 2009 mainly concerned SMEs with more than ten employees, with the number of procedures for companies going into administration or liquidation up more than 40% on a year.

But this was followed by encouraging signs of a significant decline in failures in the first half of 2010, lending support to hopes of recovery.

TIMID REBOUND IN BUSINESS PACE

SME managers surveyed in May 2010 pointed to still weak improvement, and predicted sales growth averaging only 1% for all sectors taken together. There were modest upturns for capital goods, wholesaling and business services — sectors that bore the full brunt of recession at the end of 2008 and the beginning of 2009.

The cash positions of micro-enterprises (fewer than 10 employees) were particularly tight in spring 2010 and there were fears of continued strains over the near term. Investments were expected to show a modest downturn overall, but pick up a little in industry following a sharp contraction in 2009.

Views of prospects for 2011 are much more optimistic, with SMEs in industry, wholesaling, services and tourism looking forward to significant increases in sales. The expected rebound should yield full benefits for businesses taking the lead in exports and innovation, since they are the best placed to take advantage of accelerating world trade.

SME FINANCIAL STRUCTURES WITHSTAND THE DOWNTURN

The slump that set in at the end of 2008 carried over to the 2009 accounts of SMEs, which suffered from declines in sales, margins and reserves. Businesses involved in exports and manufacturing were hardest hit.

Investments showed a worrying decline of over 15% in 2009, raising questions about businesses' faith in the future. The already structu-

rally low investment rate among SMEs tumbled to its lowest in over ten years.

On the brighter side, SME balance sheet structures have held up, with equity bases reinforced despite lower profits. Debt ratios are on the decline and it mainly relates to short-term borrowings, which are closely correlated with business volumes. Short-term financing needs for inventories and trade credit are under better control.

EMPLOYMENT CONTRACTS SHARPLY IN 2009

Overall, businesses shed more than 320,000 jobs in 2009. In a departure from previous trends, SMEs of all sizes cut their workforces, although this was more limited among those employing fewer than 10 people and more aggressive among larger companies.

Business leaders surveyed on job prospects for the current year in May 2010 were more optimistic than they had been six months earlier, when they hit their lowest since 1993. Businesses with 10 to 49 employees took a slightly brighter view than others; employment is steadying in export sectors and innovative businesses have held on to staff.

Against this backdrop, 2010 appears as a turning point for employment in SMEs, standing between the downturn in 2009 and the expected rebound in 2011.

INNOVATION FOR BUSINESSES IN ALL CATEGORIES

Extending the scope of the study to intermediate-size businesses (ETI, counting 250 to 5,000 employees) and using more varied indicators have made it easier to identify the features that set innovative businesses apart.

- Businesses concerned tend to be relatively recent — 56% were founded less than ten years ago — and are generally on the smaller side within each category considered (micro-enterprise, SME and intermediate-size business). They are nonetheless open to international markets.

- The sector breakdown is stable, with innovative businesses in operation for three years or more mostly in industry (42%), whereas those in operation for less than three years are more likely to be in the information and communication sectors (24%) or in specialized scientific or technical activities (30%).
- Recourse to public support for innovation is on the rise, with growing numbers of SMEs benefiting from research tax credits or joining competitiveness clusters.

DECLINE IN THE NUMBER OF SME EXPORTERS STEEPENS IN 2009

In 2009, SMEs active on export markets suffered more than others and their numbers fell 5.3% compared with a 3.6% decrease in exporting firms in general. Their sales plummeted 16% after steadying in 2008.

These trends reflect a sharp fall in the number of SMEs making their first export sales, with the decline reaching 13% in 2009 after 5% in 2008.

SMEs are more focused on European markets than others, and thus suffered more from the poor conditions prevailing there in 2009. A decline of 17% in sales to the European Union accounted for over two-thirds of the fall in SME sales.

PAYMENT TERMS GRADUALLY IMPROVING IN FRANCE AND EUROPE

The trend to faster trade payments has broadened and quickened in France as a result of the Modernization of Business Act (*Loi de Modernisation des Entreprises*) that came into force in January 2009. Big companies have started to shorten terms for supplier payments which were down 5 days on average from 2007 to 2009, whereas they had previously been the only category to raise them over the longer term with an increase of 3 days from 1990 to 2007.

At the end of the first half of 2010, there was further confirmation that France's larger businesses are less inclined to meet payment

deadlines than smaller businesses. While 35% compliance rate falls by nearly two-thirds to 12% for those with over 250 employees. Micro-enterprises are the most virtuous, with 39% paying on time.

At the end of June 2010, figures showed that over four out of ten European businesses pay on time — the best result in four years. German and Dutch firms are the main contributors to improvement, while their French counterparts lag.

PUBLIC PROCUREMENT: SMEs WIN MORE CONTRACTS THAN LARGER SUPPLIERS, BUT BOOK LOWER AMOUNTS

SMEs win 60% of public procurement contracts, but only 30% of the total amounts involved. The proportion by number of contracts is higher at local government level, standing at 63% compared with 49% for central government procurement. The gap is even wider in terms of amounts, with SMEs accounting for 40% of the total at local government level and only 21% in the case of central government orders.

Individual contract values are also distinguishing features, with the proportion of SMEs declining as these rise. The lower representation of SMEs is particularly marked for the largest contracts, those exceeding €1 million.

PUBLIC SUPPORT FOR SMEs TENDS TO THE LONGER TERM

Action under the government support plan, and then the economic stimulus of 2009, initially focused on the short-term cash squeeze resulting from slumps in business volumes.

By the end of 2009, 16,000 businesses had benefited from OSEO assistance, with guarantees for bank loans totalling over €3.5 billion. At the same time, Credit Mediation structures dealt effectively with applications totalling over 22,000 in the period from November 2008 on. The success rate was high, with nearly two out of three businesses gaining access to financing at the conclusion of the mediation process.

The measures adopted have, by stages, tended to tackle more fundamental financial issues and consolidate financial structures not only in sectors still struggling but also in those showing signs of recovery.

In autumn 2009, OSEO contributed to this trend, responding to government requests with the launch of the *Contrat de Développement Participatif* (subordinated loan), a new financing option designed to reinforce the capital bases of businesses with up to 5,000 employees. In the same vein, Credit Mediation has taken advantage of the greater trust it has established between businesses and their partners to address longer-term financial needs in the cases it deals with.

Another important initiative was taken by *CDC Entreprises* with the launch of funds dedicated to businesses in difficulty (among them *Fonds de Développement et Consolidation des Entreprises* (FDCE) and OC+ convertible bond funds) to support development projects with genuine potential. These funds play a countercyclical role in a situation marked by the sharp contraction in investment-capital flows observed in 2009.

Now, as 2010 draws to a close, public action is placing less emphasis on alleviating cash strains, although this remains an important concern, and more on support for recovery and financing for innovation and investment. The resources dedicated to these purposes, focused on investment in the future, should enable businesses to come out of the slump with renewed vigour.

GERMAN SMEs: COMPETITIVENESS FOUNDED ON HUMAN AND SOCIAL VALUES

The German economy is staging a rapid recovery, driven in particular by SMEs and its own openness to the world, which entails greater exposure to international risk but also explains the impressive resilience of German businesses.

Nearly all German businesses are SMEs, which account for 99.7% of the national total of 3.5 million. But this is a category with wide variations: what Germans call the *Mittelstand* is defined above all by qualitative features relating to governance, community roots and a culture of partnership that favour outstanding responsiveness to demand on world markets.

Over the past ten years, the total number of businesses has held steady, but there are now more at the top end, with annual sales exceeding €50 million. Changes in the economic context since the 1990s have brought a wave of business concentration, leading seven out of ten SMEs to make acquisitions or merge over the past ten years. This trend is particularly marked in the industrial sectors most reliant on exports and thus most exposed to global competition.

Very outward looking, with 25% involved in international business, German SMEs invest massively and are major contributors to innovation. Their competitiveness, particularly in manufacturing, is founded on a set of values that reflect Germany's social model and a longstanding culture of innovation focused on human factors.

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