



Towards a European Small Business Act for innovative growth companies

Opening 1500 billion € worth of annual public procurement to European SMEs

I. The barriers to SME growth in Europe

European SMEs are smaller and more numerous than American ones.

	Europe	United States
Average staff	6	19
Share of micro-companies in employment	34%	11%

The growth of European SMEs is blocked by a glass ceiling preventing them to become global players. Since 1980, American SMEs have generated 7 times more new global players than their European counterparts.

	Europe	United States
New companies (created after 1980) among world top 1000 (capitalization 1998)	9	64

European large companies are therefore much fewer than the American ones. There are twice as many large companies per inhabitants in the USA than in Europe.

	Europe (15)	United States
Population 2003 (in millions)	380	291
Number of companies with turnover > 100 M€	2006	3176

The glass ceiling has a negative impact on the dynamism of the whole European economy.

The Lisbon Agenda for R&D

The glass ceiling also impacts the European R&D capabilities.

In March 2000 the Lisbon European Council set the goal of becoming by 2010 "the most competitive and dynamic knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion".

Two years later the Barcelona European Council, reviewing progress towards the Lisbon goal, agreed that investment in European research and development (R&D) must be increased with the aim of approaching 3 % of GDP by 2010. It also called for an increase of the level of business funding to two-thirds of total R&D investment.



Even though European large companies invest more in R&D than their American counterparts, as is shown by the geographical origin of the world top 500 enterprises in terms of R&D expenditure, they are not numerous enough to reach this objective.

	Europe	United States
R&D expenditure per company	651 M€	646 M€
Number of companies	132	208

While the EU has large companies that are outstanding performers in the R&D arena, it lacks a critical mass of medium-sized fast-growing companies that are strong on research and innovation.

European Commission

The 2004 EU industrial R&D investment scoreboard

What Europe needs to accomplish the Lisbon Agenda is the emergence of new large companies. The condition to do so is for innovative SMEs to be able to break the glass ceiling.

Negative Discrimination

The glass ceiling stems from negative discrimination. The rules of competition favour already established enterprises against newcomers, regardless of the quality of their offer. In some cases, contracts which could have been executed as well as or better by innovative SMEs, were not awarded to them because of biases based on their size and age (lack of visibility, lack of information on the needs of large clients, oversized contracts, competition with prime contractors, real and perceived risks, reluctance to change, etc.).

Large Japanese companies and the Japanese government reduce risk by buying from large companies with which they have long and tight relationships. When purchasing decisions are based on personal relationships and reputation instead of on product quality, start-ups cannot compete.

The Japanese entrepreneur / making the desert bloom

Edward A. Feigenbaum, Stanford University, 2002

The Government's philosophy is that there should be a level playing field for business seeking to bid for contracts. At present, public sector structures and practices too often mean that small businesses are disadvantaged through lack of knowledge of available opportunities or assessment and selection systems that unfairly disadvantage them. As a result the public sector too often misses out on gaining access to best value, efficient and innovative suppliers of goods and services.

Small Business Service

Access to Public Procurement for Small & Medium Enterprises

Progress Report, March 2005

Regulating competition is necessary in order to foster the emergence of new large companies in the economic structure.

Such a policy does not necessitate any further public funding. It would also provide added value to large companies since working with the best SMEs reinforces open innovation and thereby productivity. By creating a virtuous circle, this policy would enable innovative SMEs to raise more capital, thus allowing the emergence of new global players among European innovative SMEs.



II. How to implement such a policy?

The American Small Business Act

In 2003, a total of 95 billion dollars in public procurement contracts was awarded to American SMEs, through the framework of the U.S. Small Business Act (SBAAct). Excerpt from the Small Business Act founding article II (1953):

The essence of the American economic system of private enterprise is free competition. Only through full and free competition can free markets, free entry into business be assured. The preservation and expansion of such competition is basic to the economic well-being of this Nation. Such well-being cannot be realized unless the actual and potential capacity of small business is encouraged and developed. It is the declared policy of the Congress that the Government should aid, counsel, assist, and protect, insofar as is possible, the interests of small-business concerns in order to preserve free competitive enterprise and to insure that a fair proportion of the total purchases and contracts or subcontracts for property and services for the Government be placed with small-business enterprises.

This policy is put in practice according to the following rules:

- 23% of direct contracts and 40% of subcontracts are targeted for SMEs. Each Agency has to measure and communicate its annual results to the Administrator of the SBA and the President of the United States.
- Several programmes are implemented to reach these objectives:
 - All small contracts (< 100 K\$) are reserved for SMEs,
 - Subcontracting plans must be negotiated for all large contracts (> 1 M\$), where the prime contractors commit to allocating a share of subcontracts to SMEs,
 - Contracts to which at least 2 SMEs can make a credible offer are set aside for SMEs,
 - SBIR programme: 2,5 % of external R&D budgets from main Agencies are awarded to SMEs through a fast and light procedure¹.
- An SME is an independent company with less than 500 employees.

A Small Business Act for Europe

All over Europe, governments sharing the objective of curbing negative discrimination in order to foster the emergence of new global players should be allowed to set SME targets in public procurement of innovative products or services.

European governments do not have the right to give European SMEs a preferred supplier status due to the unbalance of the WTO GPA negotiated in 1995, while the United States have obtained a derogatory status allowing them to exclude American SMEs from the frame of this agreement.

Both the EU and national governments need to act now to ensure that European SMEs get equal rights in the new 10-year World Trade Organisation treaty. The WTO calendar opens a window of renegotiation of the Procurement Agreement in 2005. Once this first objective has been reached, a sectorial European Directive on the access of SMEs to public procurement of innovative products and services will have to be implemented, allowing the setting up of SME targets.

¹ this programme only accounts for a small share of the R&D contracts awarded to American SMEs.



A first step: the SME Pact

The SME Pact is a pilot action implemented in France since 2005. Focused on SMEs with a strong growth potential, it is a voluntary commitment made by large public or private entities.

As a support measure, large companies and large public bodies are provided with schemes allowing them to work with the best innovative SMEs. A set of indicators is established in order to monitor the share of SMEs in procurement of innovative products or services.

From the large entities' standpoint, the SME Pact comes down to being able to reconcile two opposing constraints : reducing acquisition costs and globalizing demand while ensuring open innovation.

Conclusion

A European Small Business Act allowing SME targets in public procurement of innovative products and services should be able to generate 100 billion euros of supplementary contracts for innovative European SMEs on a yearly total of 1500 billion euros of public procurement. By facilitating the access of innovative SMEs to markets in the whole European Union, a European Small Business Act would foster the emergence of the 1000 new large companies necessary to meet the Lisbon Agenda and take up the challenges of globalization.