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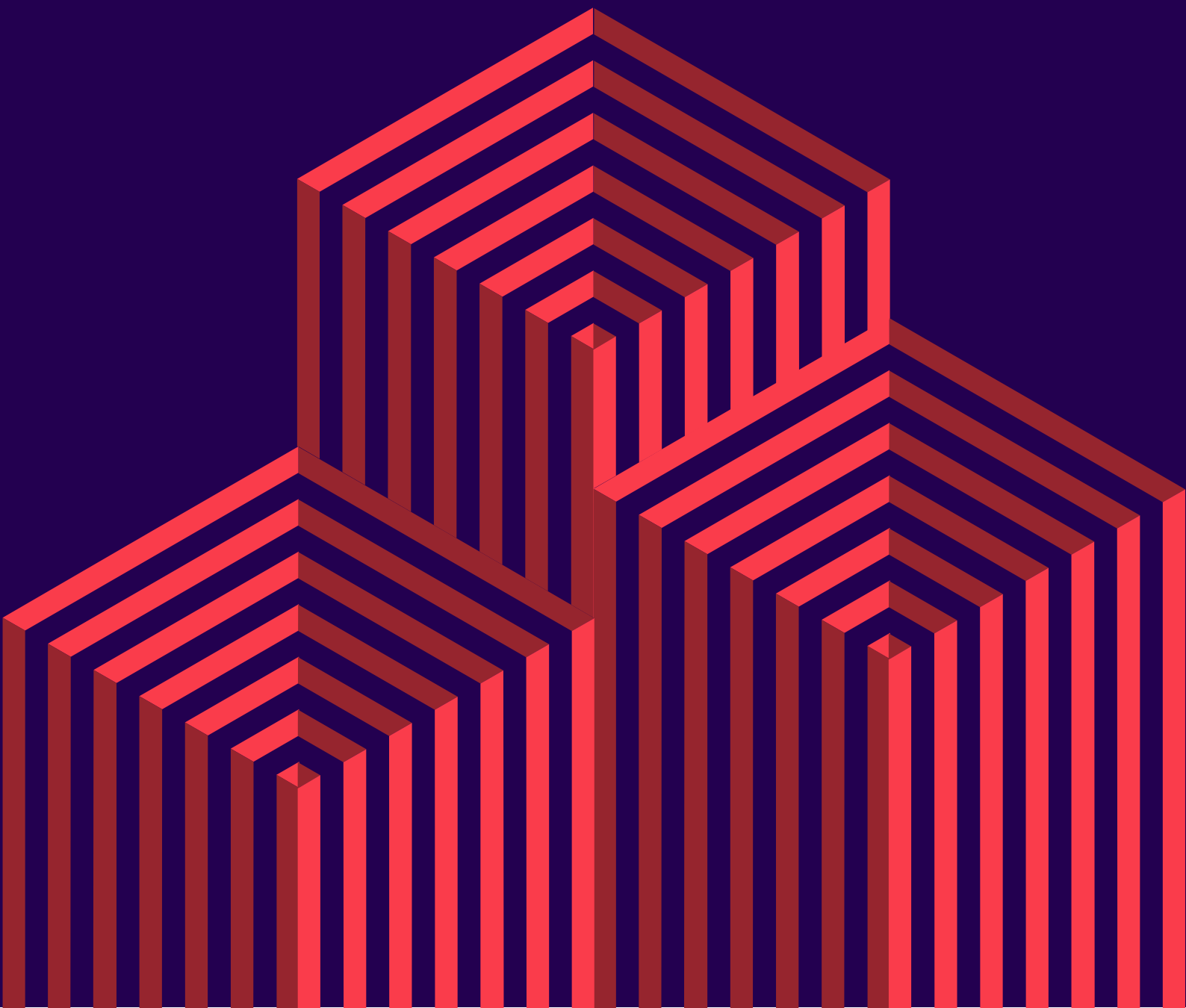
Internal and external factors for SME success

What EBMOs should know to promote more competitive enterprises



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November 2021

Bureau for Employers' Activities (ACT/EMP)

International Labour Office

First published (2021)

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English edition

Internationl Labour Organization– Geneva: ILO, 2021.

ISBN 978-92-2-035604-3 (print)
ISBN 978-92-2-035605-0 (web PDF)

Produced by the Publications Production Unit (PRODOC) of the ILO.
Graphic and typographic design, printing, electronic publishing and distribution.

The ILO endeavours to use paper sourced from forests managed
in an environmentally sustainable and socially responsible manner.
Code: CMD- REP

▶ Preface

Small and medium-sized enterprises (SMEs) are the backbone of the world economy. They create the bulk of employment worldwide and are the main source of income for the billions of people who work in them. To a greater or lesser degree, they are the base of the business pyramid of countries and rest on fundamental values that contribute to social cohesion and the development of the communities in which they carry out their activities.

Although we think that we are all referring to the same thing when we talk about SMEs, this could not be further than the truth. In fact we are talking about a vast universe in which heterogeneity is the rule, with differing levels of complexity. Whether for reasons related to the geographical location, the quality of the business environment, the characteristics of the sector to which they belong, the structure of the company, or the intrinsic qualities of the entrepreneur, each one seeks its particular way of dealing with their particular context to survive, grow, develop and become sustainable.

In analysing the statistics concerning business mobility – it is clear that the vast majority of SMEs do not succeed in growing. A very high percentage of them enter the market and leave it quickly because they do not reach the minimum efficient production scale and they fail to consolidate. The speed at which SMEs are born and disappear throughout the world is astonishing.

But for the benefit of society, this process of continuous change makes a few of those that enter the market become companies that could be classified as successful, regardless of how entrepreneurial success is defined. It could be due to the year-on-year growth in sales, the increase in hired human resources, the profitability obtained to invested assets or sales, or dozens of possible definitions. What is it that makes them different? How do they go about taking that leap, surviving, and becoming competitive? Is the type of sector in which they are working or the characteristics of the entrepreneur more important? Is it easier to succeed in services than in agriculture?

Through the research in this publication, we have carried out an in depth bibliographic review in order for us to discover what some of the main reasons are for SME success. Knowing this has important implications for the design of public policies in favour of entrepreneurship, the creation of decent jobs, the quality of employment, the economic growth of countries, and, ultimately, their economic and social development.

The pandemic revealed that many SMEs were not prepared to face such a crisis. However, global crises have always existed and will unfortunately exist in the future. The key for resilience will be knowing what the main internal characteristics

of successful SMEs are – looking at their resource base, business strategies, management practices and entrepreneurial actions – and also looking at external factors to their success which are associated with the overall business environment.

Given these multiple factors, it is not easy to design and implement public policy that aims to promote the creation of business development services or public policies in favour of SME development. Nevertheless, it is clear that fostering the resurgence of a sustainable business sector requires a consistent and comprehensive approach.

This report aims to contribute to this reflection and action and we hope it will provide assistance to those Employer and Business membership organisations who wish to engage in policy advocacy in this area. We are of course at the disposal of our constituents to deepen this reflection and action so that we have more sustainable companies, capable of creating more and better jobs to improve the quality of life for all.

Deborah France-Massin

Director
Bureau for Employers' Activities
International Labour Office

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▶ Acknowledgements

This report, prepared by the ILO Bureau for Employers' Activities (ACT/EMP), has benefited from the participation of several experts and specialists who have collaborated in different phases of its development. First, we would like to thank researchers Jorge Paolino and Andrés Jung for their meticulous work in reviewing the literature and designing a strategy so that the report reflects a comprehensive approach to the topic. We thank them for their professionalism and dedication.

Our thanks also go to Roberto Villamil, ACT/EMP Senior Specialist, co-author of the report and responsible for the research process. Also to José Luis Viveros-Añorve and Magdalena Bober, ACT/EMP Specialists, who in addition to providing valuable technical inputs throughout the process of preparing the report, which they also co-authored, provided a thorough review of the report and made substantive contributions. We would also like to thank Paolo Salvai, ACT/EMP Specialist, for reviewing the report and providing valuable comments to evaluate some chapters and suggest concrete directions for future areas of research.

Finally, we would like to give special thanks and recognition to our colleagues from the ILO's SME Unit, Dragan Radic, Mario Berrios, Marlene de la Chaux, and Michael Elkin, who have kindly reviewed the report and provided detailed and valuable technical comments to improve it.

Introduction

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Small and medium-sized enterprises (SMEs) are highly heterogeneous economic units with diverse levels of complexity. They account for a high percentage of the total number of enterprises and create the bulk of employment worldwide. The ILO (2019) finds that small economic units create, on average, 70% of jobs globally. In the OECD, SMEs account for 99% of all businesses and generate between 50% and 60% of gross value-added. Almost one-third of workers are employed in micro firms (fewer than 10 employees), and two-thirds work in an SME. In emerging countries, these figures are frequently higher considering micro and SMEs in the formal and informal economy. In Latin America and the Caribbean (LAC), considering the formal economy, 88.4% are micro firms and 11.5% SMEs, while employment participation shows that 27% work in micro firms and 34% in SMEs (Correa et al., 2020). Additionally, SMEs are key drivers of job creation and usually contribute to the identity and social cohesion of local communities (OECD, 2019).

However, the levels of enterprise mobility in this segment of companies are very high. A large majority of SMEs enter and exit the market rapidly because they fail to consolidate. But a small number of them do. What makes them different? Why do they manage to reach an efficient scale of production and be competitive? How important are the entrepreneur's characteristics?

The objective of this study is to identify the main internal and external factors that contribute to the possibilities of success of an SME. Although the factors of business success may vary by firm size and economic sector, particularly given the heterogeneity of small-scale economic units and the diverse quality of the business environment across regions, the adopted approach is focused on key drivers identified by evidence-based studies. Hence, the main identified factors include those linked to the characteristics of the entrepreneur, the structure of the company, the sector of activity, and the general business environment in which a formal business venture develops.

Following the analysis of the results achieved, it also attempts to identify some trends that Employers and Business Management Organisations (EBMOs) should take into account in designing support services or policy proposals that promote entrepreneurship based on the factors identified in the research. This is an area where there are major challenges and which will certainly require further research.

1.1. What is a Small and Medium-sized Enterprise?

Although there is vast literature related to SMEs, there is no universal classification of SMEs, because of the characteristics of the different economies. As a general criterion, the diverse definitions aim at classifying firms into relatively homogeneous groups that face similar situations, either of problems or opportunities.

This way, the definition of SMEs varies depending on countries or organizations. The most common denominator for a definition is the number of employees, although turnover and assets criteria are also used. Many governments (particularly middle-income and high-income economies, the OECD, the European Union (UE), and the International Monetary Fund (IMF), define an SME as an enterprise employing up to 249 persons, considering micro (1-9 employees), small (10-49 employees) and medium (50-249 employees) enterprises. Lower-income economies more frequently use 50 or 100 employees as a threshold for defining an SME. Thresholds for turnover and assets are usually different for high and low income, or big and small, economies.

Some detailed definitions by international organizations may set a standard frequently used:

The **World Bank** considers three parameters to define the firm size: employees, assets, and annual sales. Enterprises must meet at least 2 of the following 3 characteristics:

a. Micro enterprises are those that employ fewer than 10 persons and/or that has assets under USD 100.000 and/or annual sales under USD 100.000

b. Small enterprises are those that employ fewer than 50 persons and/or that has

assets under USD 3 million and/or annual sales under USD 3 million

c. Medium-size enterprises are those that employ fewer than 300 persons and/or that has assets under USD 15 million and/or annual sales under USD 15 million

The **European Union** definition of SME considers staff headcount and annual turnover or annual balance sheet total to classify enterprises.

a. Micro enterprises are those that employ fewer than 10 persons and that have an annual turnover or annual balance sheet smaller than Eur 2 million.

b. Small enterprises are those that employ fewer than 50 persons and that have an annual turnover or annual balance sheet smaller than Eur 10 million.

c. Medium-sized enterprises are those that employ fewer than 250 persons and that have an annual turnover smaller than Eur 50 million or an annual balance sheet smaller than Eur 43 million.

This definition also considers the ownership, partnership, and linkages with other enterprises.

Inter-American Development Bank has a different definition of SMEs according to the countries and activity sector considered.

1.2. Most common ways of measuring SMEs performance

There are different approaches to measuring firm performance, and its 'success'. The main variables typically identified by empirical studies to measure firm performance are employment, turnover, profits (before taxes)[1], and productivity (Siepel and Dejardin, 2020). Other indicators include total assets, market shares, total capital ratio[2], return on equity, return on capital employed, cost-to-income ratio , market valuation, or stock price for those publicly traded, which is an exceptionally rare occurrence. Once selected or identified the variable to measure performance, the question is how to consider the outcome as 'successful'. The most used metric is growth (relative, absolute, or as a complex index). Furthermore, it is important not only to focus on one specific way of measuring performance (success) but also to consider the relationship or sequence between different variables.

Employment. The number of employees is a standard metric for a firm's size. Employment growth, for a given period, is commonly used by scholars and policy makers to understand business development and job creation (e.g., Davidsson et al., 2007; Coad, 2009; Wiklund et al., 2009; Siepel and Dejardin, 2020). Perhaps employment growth is not the first variable an entrepreneur or manager would consider evaluating business success, but it is a key indicator of medium and long-term business development and of great value for analysis.

Turnover. This variable refers to firm sales and is used to consider growth as a measure of a firm's performance (Siepel and Dejardin, 2020). Coad (2009) argues that sales are an indicator of output, but not of performance (i.e., value-added). Anyhow, it is a relevant variable to consider, as the literature on firm growth suggests that turnover growth and employment growth are mutually dependant, although in a different sequence for most firms and high-growth firms (Coad et al., 2017).

Profits. Although there are different ways of measuring profits and data is not usually easily available for empirical analysis, profits are an important measure of firm performance. Undoubtedly it is a key indicator for the entrepreneur or manager of a firm (Siepel and Dejardin, 2020).

Productivity. Productivity is an important indicator of performance at micro, sectorial and macro levels since it is a measure of efficiency in the use of production factors. Although the most comprehensive way of looking at productivity is through the total factor productivity (TFP), partial metrics such as capital productivity

1 Known as P/L before tax (profit or loss before tax).
2 To assess the operating expenses of an organization vis-à-vis its income.

or, most frequently, labour productivity are usually used in empirical analysis. Gross value-added per working hour and firm real sales per worker or working hour are frequent proxies of labour productivity (ILO-ACT/EMP, 2020).

Small-scale economic units typically face challenges to reach a minimum efficient scale and achieve sustained increases in productivity. A productivity ecosystem tailored to SME development would help small-scale economic units escape from the low-productivity-low revenue trap. Through efficiency gains, increased productivity may enable SMEs to save and invest in, for instance, workers' skills development and machinery and equipment, which would, in turn, enable capital accumulation. This process would eventually facilitate access to credit and encourage further investment in production process upgrading, diversification and output growth.

Firm survival. Although perhaps it is not usually considered as a measure of firm success, the survival of a firm is somehow an indicator of its ability to continue with the business. As reported by Coad et al. (2017), the distribution of growth rates is 'tent-shaped' with zero as a central value. Not every firm has growth as a performance goal, and sometimes success for a small entrepreneur may translate as the possibility of sustained competition in the market. A general finding in the literature is that most firms start small, live small, and die small (Zhou and de Wit, 2009). Entry and exit of new firms are a usual phenomenon in market dynamics, and entry rates are highly correlated with exit rates.

The main bulk of new entrants are imitative ventures that frequently exit a short time later with a 'revolving door' effect. Only some new ventures survive, as others exit the formal economy due to a variety of reasons. In developing economies, where the informality is relatively high, becoming informal is also a kind of survival. Only a few new ventures grow and become innovative businesses that nurture a process of 'creative destruction', displacing less efficient incumbent firms. Most new firms, enter service sectors oriented to local markets (mainly in low value-added activities as retail trade and other non-financial services) and do not have growth aspirations (Parker, 2009). These small ventures, many of them non-employee firms and sometimes informal businesses (particularly in developing countries), are important for employment, but they do not increase global productivity in the economy. It is reasonable to expect that high levels of entrepreneurship based on informal self-employment would correlate with slow economic growth and lagging development (Acs, 2006).

These are usually (but not always) variables considered in the literature to measure firm performance. Except for survival, in general, the way to evaluate 'success' is the growth of the selected performance variable in a certain timeframe.

The different metrics used to measure success focus on partial aspects of the performance and evolution of a firm. It is important to understand the relationship between them. Coad (2009) reports previous analysis finding that growth of a firm's employment is associated with the growth of sales and labour productivity, and that there is a kind of 'positive feedback loop' between them, in other words, a virtuous circle of productivity growth and employment growth.

Small firms struggle to reach the industry minimum efficient scale (MES), and to achieve it, increases in employment should be associated with higher productivity (Coad, 2009). Sales growth and productivity growth contribute to the subsequent growth of profits, increasing the capacity of saving, investing, and creating decent jobs, and generating the conditions for escaping a low-productivity trap. Furthermore, SMEs tend to rely on labour-intensive technologies, relative to larger firms (Yang and Chen, 2007), and require adequate business strategies and management practices in the use of their resources and capabilities to be productive.

A particular group of dynamic firms important as job creators are the so-called High-Growth

Firms (HGF) or 'Gazelles' [3]. These can be found across all sectors experiencing above-average growth. Although representing a minority, this small number of high-growth firms, frequently young and small size ventures, are particularly important for net job creation and the economic wealth of a region (Henrekson and Johansson, 2010; see also an extended discussion in Moreno and Coad, 2015). Half of the employment generated in the United Kingdom between 2002 and 2008 was created by 6% of the highest growth businesses, which were found in every region of the UK and very different sectors (NESTA, 2009).

1.3. Structure of the document

The document is organized as follows. After this introduction, in chapter 2 the study presents a review of the academic literature related to the main factors for SME success. In chapter 3, the analysis is focused on the main challenges faced by SMEs, given the main drivers of global and business trends, accelerated by the deep crisis brought about by the COVID-19 pandemic. Chapter 4 will present selected cases of supporting actions to foster SME performance, and in chapter 5 the main conclusions and recommendations are presented.

3 According to the OCDE definition, these are high growth young firms (i.e., less than 5 years old), with at least 10 employees at inception and an average employment growth rate exceeding 20% p.a. over a 3-year period.

SMEs success factors: Literature review

- 2.1. Which are the main success factors considered in the literature?
- 2.2. How success factors may interact in a comprehensive approach
- 2.3. Selected success factors to foster SME's performance.

2

2.1. Which are the main success factors considered in the literature?

Empirical studies usually consider success as growth in some of the variables that measure performance at the firm level. They analyse the evolution, persistence, and different determinants associated with firm growth.

Although there is a prolific strand in literature studies based on the relationship of firm growth based on size and age, following a path that was pioneered nearly a century ago by Gibrat (1931), further research has taken a broader approach, studying different factors that explain the performance (i.e., growth) of new and small firms. Firm growth is a complex process, in which several factors play their part. As stressed by Nelson and Winter (1982) in another reference study, growth is an organizational outcome resulting from the combination of firm-specific resources, capabilities, and routines, and these firm-level actions occur in specific industrial and regional or national contexts, which in turn may also affect firm performance. This highlights the relevance of the quality of the business environment in which enterprises operate and compete.

The factors associated with firm-level growth are usually classified into three main groups: individual (associated to the entrepreneur), organizational (the firm and its own strategies and characteristics), and environmental (the industrial and regional/national environment in which firms develop their activity) (Schutjens and Wever, 2000; Peña, 2004; Nichter and Goldmark, 2009; Zhou and de Wit, 2009). Based on the comprehensive survey by Zhou and de Wit (2009), this section presents a brief analysis of a variety of determinants of firm growth found in the literature.

Individual Determinants

The decisions made by an entrepreneur have an obvious incidence in the performance and growth of a firm. As stressed by Zhou and de Wit (2009), the main characteristics that mould the decisions of the entrepreneur are personality traits, growth motivation, individual competencies, and personal background:

- Entrepreneurial **personality traits** refer to the need for achievement, risk-taking propensity, locus of control, self-efficacy, and extraversion.
- The 'tent shaped' distribution of firm growth rates shows that the main bulk of firms do not grow or grow in a small interval around zero (Coad et al., 2017), either because of barriers to grow or lack of willingness of the entrepreneur. What the literature shows is that the **growth motivation** of the entrepreneur is an important factor for the actual growth of the new venture (Delmar, 1996). Although firms usually start small and grow to a certain size, struggling to reach a minimum efficient scale (MES), they are sometimes successful but other times they are not. Frequently, firms reach a survival but suboptimal scale and continue their business even though they have not reached the MES. Once a sustainable size is reached, the entrepreneur may decide to continue growing or maintain that level.
- The knowledge, skills, and/or abilities required to develop a business are the **individual competencies** of the entrepreneur (general or specific competencies).
- The **personal background** of the entrepreneur includes general aspects such as gender, age, level of education, and years of experience. Several studies show that male and younger entrepreneurs are more likely to engage in firm growth (e.g., Brush et al., 2006; Wagner, 2007; Levesque and Minniti, 2006; Kautonen et al., 2014). Entrepreneurial experience, managerial skills, and education level have a positive impact on the firm´s performance, particularly when accompanied by growth motivation (Wiklund and Shepherd, 2003).

Organizational Determinants

There is a large strand of literature studying organizational factors behind firm success, such as employment or turnover growth, profits, or growth in assets, being a key determinant of how evolves its productivity. As referred to by Zhou and de Wit (2009), relying upon the evolutionary vision of the firm ... "firm growth can

be determined by the degree of effectiveness and capability with which firm-specific resources such as labour, capital, and knowledge are acquired, organized, and transformed into sellable products and services through organizational routines, practices, and structure."

The main organizational determinants can be seen as part of three main groups: firm attributes, firm resources and structure, and firm strategies.

- **Firm attributes.** One of the more prolific strands in literature studies the relationship of firm growth with size and age, which are the classical firm attributes. The debate on the relationship between firm age and size and firm growth had its origin in Gibrat's law (Gibrat, 1931; Audretsch et al., 2004), which states that the growth rate of a firm is independent of its initial size and that there is no difference between firms in the probability of a given growth rate during a specific time interval within the same industry. However, the main bulk of empirical studies show that younger firms show higher growth rates than older firms, and this is consistent through countries and industries (e.g., Yasuda, 2005). By the same token, empirical studies show as a stylized fact that smaller firms grow faster, arguing their need to achieve a minimum efficient size (e.g., Audretsch et al., 2004) to be competitive[4].

- **Firm resources and structure.** Based on a resource-based view (RBV), financial resources and human capital are the most important resources for small business growth (Zhou and de Wit, 2009; Wiklund et al., 2009). Financial resources allow for strategic flexibility since they can be transformed into other types of resources. Human capital stands for knowledge, skills, and experience. Human capital, embodied in the employees working for the firm, is perhaps the most important resource for SMEs. It is also important how these human resources are organized (firm's structure), and to what extent an SME can reconfigure, reallocate, and recombine its resources to achieve its goals (dynamic capabilities) (Eisenhardt and Martin, 2000; Teece et al., 1997). Structure and dynamic capabilities that nurture strategy are the key components of a successful firm (Nelson, 1991).

- **Intrapreneurship.** The organizational structure and strategy may favour the entrepreneurial activities of their personnel, which is a way to foster the entrepreneurial orientation of the firm. Broadly speaking, intrapreneurship is 'entrepreneurship within an existing organization' and an intrapreneur is a person who plays an entrepreneurial role in an organization (Bager et al., 2010). This intrapreneurial experience by an individual working in a firm is defined as "a human capital attribute of employees who have a leading role in the development and implementation of re-generation activities within an organization under a proactive, innovative, and risk-oriented focus" (Guerrero and Peña-Legazkue, 2013). Regarding the effect on the organization, Bager et al. (2010) report two distinct traditions: Those who narrowly focus on the formation of new business units within existing firms, and those who apply a broader view encompassing many types of innovation and organisational renewal activities within the firm (a more comprehensive approach).

- **Firm strategies and management practices.** Firm strategies and management practices that are based on their resources and dynamic capabilities, are a key determinant of growth (Zhou and de Wit, 2009). Wiklund et al. (2009) stress on the influence of entrepreneurial orientation on firm growth. Entrepreneurial orientation involves the willingness to innovate, to take risks to try out new and uncertain products, services, and markets, and to be more proactive than competitors towards new marketplace opportunities. Market orientation may be also an important determinant of growth. Firms with market orientation, can track and respond to the customer's needs and preferences.

  Moreover, basic business management practices, such as formal accounting methods, are associated with improvements in productivity and profitability (Bloom et al., 2010; de la Rosa et al., 2017). Yet, small-scale economic

4 Some studies find that Gibrat's law only holds for firms above a certain size threshold, that is big firms (e.g., more than 400 employees) (Bigsten and Gebreeyesus, 2007).

units, particularly the family-owned ones, face challenges to separate returns to the business from household income, making harder for the entrepreneur or business manager to retain profits for business investment purposes.

Environmental Determinants

The influence of location on firm growth is stressed by several studies (e.g., Wiklund et al., 2009; Ipinnaiye et al., 2017; Jung et al., 2013; Hoogstra and van Dijk, 2004; Nichter and Goldmark, 2009). As reported by Zhou and de Wit (2009), the sectorial and regional environment in which the firm operates varies along several dimensions and has an influence on firm growth (favouring growth or being a barrier to its development). An adequate infrastructure is a key element for SME development, particularly dealing with technological needs that may favour innovation-oriented activities.

Market structure and intensity of competition favours or hinders new firm entry, and sometimes are barriers to entry. When the competition dynamics is dominated by SMEs, the MES is lower, and entry is easier. Institutional and financial barriers for small businesses growth are commonly addressed in the literature. Institutional barriers are mainly discussed with the focus on firms' interaction with government, including quality of institutions and governance, regulations, rule of law, taxation, and government support, among others.

SMEs frequently face unfavourable tax systems, discriminatory regulations, and complicated laws. Financial barriers typically refer to difficulties to access to financial resources. Financial institutions usually are more cautious providing loans to SMEs because of information asymmetries, asking for higher collaterals and charging higher interest rates (Zhou and de Wit, 2009).

Macroeconomic and sectorial growth and other variables reflecting the business cycle, may clearly have a positive influence on firm performance and particularly on new-firms start-ups (Audretsch, 1995). Location factors also matter and have been discussed extensively in the literature (e.g., van Oort and Stam, 2005, Jung and Camacho, 2012). Entry and growth patterns are influenced by the spatial concentration of economic activity. These externalities associated to the spatial concentration have been discussed in two different streams: a) as the potential economic effects of agglomeration of similar activities where specialization is the key driver; and b) as the potential economic effects of concentration of different activities over the same location where diversity is the key driver.

These agglomeration economies (based either on specialization or diversity) could generate knowledge spillovers, better labour supply and lower costs for firms in a specific region. These issues relate to the literature on industrial districts and clusters as favourable environments for new venture creation, firm growth, and competitiveness enhancement. There are other locational factors influencing entry and growth, such as income levels, human capital, and labour availability, all in all, and particularly for SMEs, the environmental factors are important to favour or hinder the possibility of developing firm strategies.

2.2. How success factors may interact in a comprehensive approach

Several studies intend to consider success factors in an integrated manner, using a diversity of approaches but always trying to articulate the interaction between the different groups of factors. This study presents three different and specific integrated approaches to the analysis of firm success factors.

An integrative model of small business growth

The first is the case of Wiklund et al. (2009), who build a model for small business growth (employees, sales, and growth relative to competitors) based on five theoretical perspectives:

1. ***Entrepreneurial orientation.*** This is a key component and refers to the firm's strategic orientation, capturing specific entrepreneurial aspects of decision-making styles, methods,

and practices. It involves willingness to innovate, rejuvenate market offerings, take risks to try out new and uncertain products, services, and markets, and be more proactive than competitors toward new marketplace opportunities. As Wiklund et al. (2009) argue... "There is reason to believe that Entrepreneurial Orientation as an overarching construct can have worldwide positive performance implications."

2. ***The environment.*** Firms develop their business activity in specific contexts that may favour or hinder their possibilities of success. Some of the main aspects that conform with those contexts include infrastructures, institutions, market structure, general economic conditions, adequate supply of workers, policies, and regulations, to name a few. In this case, Wiklund et al (2009) refers to studies that assess some dimensions of the environmental influence of location, industry, and market on firm performance, such as market structure and the degree of scale economies (e.g., Audretsch, 1995), industry growth rate (e.g., Audretsch and Mahmood, 1994), and market maturity (e.g., Baldwin and Gellatly, 2003). Additionally, researchers have suggested that it may be advantageous to describe the environment of small businesses by dimensions reflecting subjective perceptions of small business owners. Dynamic environments are characterized by instability and continuous change. Hostile environments create threats to the firm, either through increased rivalry or decreased demand for the firm's products, reducing growth opportunities. Heterogeneity captures the complexity of an environment, making it relatively easier for small firms to find and develop market niches.

3. ***Strategic fit.*** The effectiveness of any strategic orientation depends on the nature of the environment of the firm. The strategy, based on the characteristics of the firm, needs to achieve a fit with the environment in which it operates.

4. ***Resources.*** Based on the resource perspective of small business growth, Wiklund et al. (2009) stress three distinct theoretical constructs to achieve better performance: a) Small firms have limited access to financial capital, which limits their growth (e.g., Reid, 2003; Lopez-Gracia and Aybar-Arias, 2000); b) better human capital of entrepreneurs running their businesses should achieve higher performance in executing relevant tasks, as follows from the theory of human capital, c) entrepreneurial network resources are a positive influence for small business growth. Access to financial resources favours strategic flexibility, giving firms a variety of options to reach competitive advantage. This idea refers to the concept of dynamic capabilities defined as "the firm's ability to integrate, build, and reconfigure internal and external competences to address rapidly changing environments" (Teece et al. 1997).

5. ***Growth attitude.*** In most economic literature, growth attitude is taken for granted, if people act in ways to maximize their profits. In the entrepreneurship literature, the role of small business managers' attitudes, specifically growth aspiration, is associated with actual business growth. Scholars argue that the growth attitudes of small business managers set limits to the growth a business will achieve. In fact, not every entrepreneur has growth ambitions for his business.

These five perspectives are not necessarily independent of each other, and they may lead to conflicting hypotheses about growth under certain circumstances. Wiklund et al. (2009) argue that to integrate the different perspectives is required to view the strategic orientation—basically the entrepreneurial orientation—of the small business as a central construct mediating the impact of resources, environment, and attitude on firm growth. They also stress that is likely that the entrepreneurial orientation-growth relationship itself is dependent on these constructs, specifically the environment of the small business. This is highlighted by the strategic fit perspective, which states that the strategic posture of the firm must match environmental conditions.

Drivers of SME performance: a holistic and multivariate approach

Ipinnaiye et al. (2017) develop and test a holistic multivariate modelling approach that integrates three sets of determinants in explaining SME

performance: firm characteristics, firm strategy, and macroeconomic conditions. They consider as performance variables turnover, employment, and productivity growth. Turnover and employment growth measure the firm's actual performance and potential productive capacity, respectively (Bottazzi et al., 2008), while productivity growth assesses its efficiency of resource use in producing a given level of output.

Heterogeneity in the performance of firms, even within the same narrowly defined industries, is well noted in the literature (Caves 1998). Based on the evolutionary and resource-based views of the firm, these performance differences have been attributed to variations in the resources and capabilities embedded in the firm, the strategic choices made in exploiting these resources and capabilities, as well as responses to changes in the business environment (e.g., Nelson and Winter 1982; Nelson, 1991). Macroeconomic conditions may have an indirect effect on firm performance through the strategies adopted by the firm, and the specific impact of macroeconomic variables on firm growth may also be subject to firm characteristics.

The main findings of the study by Ipinnaiye et al. (2017), focused on three different performance measures, adding complementary emphasis to the analysis.

- As expected, findings on ***firm characteristics*** show an inverse size/growth relationship, the larger the firm, the lower the business growth. The effect of the initial level of productivity varied with the firm performance measure used. They find a negative effect for this determinant on turnover growth, suggesting a convergence effect. Hence, firms entering the industry with low productivity levels need to increase output quickly to reach the industry MES to avoid failure.

  By contrast, the positive labour productivity coefficient in the employment growth model provides evidence that firms with higher initial levels of productivity grow faster than less productive firms, consistent with Jovanovic's (1982) model of passive learning, which posits that firms only gain knowledge of their true efficiency after entry into a given industry, and they adjust their sizes accordingly.

- Regarding ***industry characteristics***, a positive industry growth variable indicates that firms located in fast-growing industries showed faster employment and turnover growth, implying a low competition effect and the availability of more opportunities in these industries (Delmar and Wennberg, 2010). These opportunities may be more accessible in markets characterized by product differentiation. Firms in industries with relative high concentration show lower growth rates, although its significance is not uniform throughout the period.

- Results on ***firm strategy*** variables, show that trade drives manufacturing turnover growth, with two-way traders benefiting from exporting and importing concurrently. Related to employment, although, firms engaged in importing and two-way trade experienced decreased employment growth. There are mixed results between the firm performances measures used in relation to the effects of the R&D variables. As expected, turnover growth was, on average, positively associated with the firm's R&D investment decision, but turnover and employment growth declined with R&D intensity, although with a low incidence. Training had a positive effect on employment and turnover performance.

- As ***external determinants*** of employment and turnover growth, Ippinaye et al. (2017) found some expected but also some contra-intuitive results. They found a significant positive relation between aggregate unemployment and SME growth for the 1991–2007 sample period. This unexpected result may be related to the specific situation of the Irish economy during that period, and to the fact that the sample includes manufacturing micro firms (fewer than 10 employees not excluding self-employed) while unemployment rates reflect the situation for the whole economy. Inflation was associated with lower employment growth but was positively associated with turnover growth.

  Lower real interest rates will likely stimulate consumption and investment spending through borrowing, with higher aggregate demand leading to growth in firms' turnover. In line with a priori expectations, a decline in national competitiveness (measured by the variation in

the real effective exchange rate) was associated with a decrease in employment and turnover growth. Concerning domestic credit growth, their results support the hypothesis that the availability of credit promotes turnover growth in manufacturing SMEs.

The overarching insight emerging from this research is that SME growth is driven by a combination of firm characteristics, firm strategy, and macro and industry economic conditions. More specifically, they find evidence in support of smaller firms as important sources of employment and turnover growth, consistent with the literature on Gibrat's law.

This finding was robust across all model specifications and growth periods. The firm's starting quality in terms of its initial size and initial level of productivity is critical to its subsequent performance. In terms of strategy, evidence shows that two-way traders have better turnover and productivity performance than firms that export or import only. The policy implication of this finding is that initiatives which support SMEs in sourcing international suppliers may be as important as policies aimed at facilitating their entry into global export markets.

Similarly, the firm's decision to invest in R&D has a positive effect on turnover and productivity growth. Ippinaye et al. (2017) argue that the decline of employment and turnover growth with R&D intensity may be related to high risks associated with large investments in R&D that do not yield commercial success.

The finding that training investment boosts SME growth also provides support for further analysis regarding the design of relevant training programs for SMEs. This research also highlights a potential role for policies aimed at creating favourable macroeconomic conditions, as well as export-oriented policies that promote balanced and sustainable economic growth. All of these are necessary to stimulate SME growth.

The lack of data relating to other measures of firm performance such as profitability and total factor productivity is a limitation of the analysis.

A system dynamics approach for assessing SMEs' competitiveness and its effect on performance.

Lafuente et al. (2020a), drawing on the resource-based view of the firm (RBV) and the configuration theory, evaluate the effect of competitiveness and the configuration of the competitiveness system on SME performance.

Research rooted in the RBV is extensive and has mostly evaluated two fundamental assertions of this theory: (a) that some resources and capabilities have the potential to enable businesses to implement value-creating strategies and (b) that such resources and capabilities can be a source of competitive advantage when they possess attributes that make their imitation costly. RBV theorists propose that the associations resulting from connecting resources and capabilities (i.e., competencies) contribute to enhancing business competitiveness and subsequent performance (Prahalad and Hamel, 1990; Wernerfelt, 1984).

The concept of competitiveness at the firm level is understood as the ability of a company to compete in a competitive environment, to grow, and to be profitable (Dvouletý and Blažková, 2020). Building on RBV theory postulates Lafuente et al. (2020b) define competitiveness "as the mutually dependent bundle of resources and capabilities that allow the creation or development of valuable competencies". They stress that competitiveness is a multidimensional construct linked to resources and capabilities, and that competitiveness is positively correlated with performance. They argue that perhaps because of the difficulties of measuring competitiveness, most empirical studies have sought to evaluate the individual contribution of different resources or capabilities to performance.

Previous work by Lafuente et al. (2020b) calculates a complex firm-level competitiveness index, which is based on ten competitiveness pillars: technology, human capital, products, domestic market, networks, international markets, online presence, marketing, decision making, and strategy. Instead of studying the individual contribution of competitive factors, they evaluate

how different strategic configurations impact employment growth.

Lafuente et al. (2020a) conclude that the view that SMEs' competitiveness only differs in resource availability, and that all that SMEs need to do for improving their competitiveness level is to replicate strategies observed in other (more competitive) peers, is overly simplistic. Firms are a bundle of interconnected resources and capabilities, and accurate competitiveness analyses should also consider the competitive strengths and weaknesses that conform the business' configuration of competencies. Technology and knowledge, for example, are highly interconnected resources in services such as financial or knowledge-based consultancy firms, but the relevance of this connection may not be the same in other businesses. SMEs' competitiveness depends not only on its resources and capabilities, but also on the way they interconnect to configure competencies.

This approach considers the heterogeneity of the different businesses and offers an interesting framework to the design of firm strategies and public policies oriented to foster SMEs' competitiveness, since it offers a comprehensive firm skills and resources interacting with context conditions such as access to human and financial capital, technology, and markets.

2.3. Selected success factors to foster SME's performance.

Economic development is associated with a higher level of productivity and income. Productivity refers to efficiency with which people, firms and economies use resources to produce goods and services. It is important in... "generating economic growth, increasing firms' profits and growth, lowering consumers' prices, raising workers' wages and improving the standard of living for the overall population" ILO-ACT/EMP (2020).

This productivity-enhancing and productive diversification process, rely on the generation of dynamic capabilities at the firm level (Hausmann and Rodrik, 2003). In this respect, SMEs play a fundamental role in being the backbone of economic systems. This way, the level of productivity and income of a given economy, is ultimately dependent on the productivity and value-added by its firms, and particularly SMEs.

The importance of SMEs for most countries, and the necessity of upgrading the factors behind SMEs success, is clearly stressed by the World Bank (2019):

"A key focus of most countries is to stimulate growth in their small and medium enterprises (SMEs). There are various influences on SME competitiveness. These include improving capabilities, including knowledge and information to increase their productivity and ability to compete; improving their ability to access and compete in new markets and find customers through supply chains, global value chains, government procurement and other channels; improving access to finance to fund operations and investment for growth; and a conducive business environment, including the availability of infrastructure (hard and soft) and effective regulations. SME upgrading involves increasing an SME's ability to make higher-quality products, to make them more efficiently, or to move into higher-value activities, new markets, or a combination of some or all of these. Thus, upgrading involves innovating to increase value-added."

▶ **(World Bank, 2019, pág.2)**

The literature review identifies several personal, organizational (firm-level), and environmental factors important for achieving increased productivity and sound firm growth. Firm-level factors are key aspects associated with venture growth (e.g., Schutjens and Wever, 2000; Peña, 2004; Nichter and Goldmark, 2009; Wiklund et al., 2009; Zhou and de Wit, 2009), and from the perspective of the EBMOs, they seem to be an adequate focus for promotion services. The individual determinants are almost a given (although perhaps the growth aspiration is an aspect to work upon). The environmental determinants cover policy issues and may be considered in an agenda for dialogue with authorities. The organizational or firm-level determinants offer a wide field to work on different factors in SMEs performance. In fact, the above paragraph of the World Bank (2019), highlights some of the factors that are consistently mentioned throughout the literature as organizational determinants of firm success.

This perspective is consistent with the role EBMOs may play in fostering not only productivity but also better working conditions at the firm level. Building on Churchill and Lewis (1983), it may be argued that SMEs go through different stages during their growth process. Initially, most firms struggle to survive and do not have either financial capacity or, perhaps, managerial skills to carry out improvements in working conditions (for instance, higher wages or improvements in occupational health and safety).

At this survival stage, the main challenge for an SME is to improve technical efficiency to reach a minimum efficient scale, increase earnings, and escape from the productivity trap. However, once companies reach stages of success and take-off, they are able to operate at (or above) a minimum efficient scale, increase value added and invest in improving working conditions. Better working conditions contribute further to higher productivity, thus fostering a process of endogenous growth, which should be enhanced by a conducive business environment.

Authors	Organizational Determinants of firm success	Main concepts	Focus on action to increase productivity and achieve a better performance
Wiklund et al. (2009)	Entrepreneurial orientation	• Willingness to innovate. • Take risks to try new and uncertain products, services, and markets. • Proactive towards new marketplace opportunities	• Innovation (product, process, organization) • Internationalization
	Strategic fit	• Strategy and management, based on firm characteristics, fits the environment	• Prospective analysis of environment for capabilities-based strategy
	Resources	• Access to financial capital • Better human capital • Entrepreneurial network resources	• Financial resources • Training • Networking
Ipinnaiye et al. (2017)	Firm strategy	• International trade: importing and exporting firms benefit from turnover. Exports for employment. • Investment in R&D positive on turnover • Training positive on turnover and employment	• Internationalization • R&D and innovation • Training
Lafuente et al. (2020)	Firm strategy	• Resources and capabilities source of value-creating strategies and competitive advantage.	• Firm capabilities-based strategies
	Firm Competitiveness index	• technology, human capital, products, domestic market, networks, international markets, online presence, marketing, decision making, and strategy	• Technology/ digitalization • Innovation • Networking • Internationalization • Firm capability-based strategies

Based on the three holistic approaches reviewed (Wiklund et al., 2009; Ipinnaiye et al., 2017; and Lafuente et al., 2020a), the table presents a synthesis of the concepts involved and some central issues to focus promotion activities oriented to increase productivity and achieve better performance for SMEs. Through a synthesis and reorganization of the main determinants, four areas for action may be identified by SMEs to reach higher productivity and improve their performance: strategy and management, innovation, digitalization, and internationalization.

Strategy and management practices

The reported studies stress the need for strategic decisions, rooted in the dynamic capabilities of the firms, to increase productivity and reach better performance in the current global situation characterized by uncertain economic and social prospects. In this context, it is particularly important an adequate strategic fit with the competitive environment of the firm, and adequate management practices to align the internal resources, structure, and organization of the firm with the strategic decisions.

Teece et al. (1997) emphasize the key aspects of dynamic capabilities: "The term 'dynamic' refers to the capacity to renew competences to achieve congruence with the changing business environment; certain innovative responses are required when time-to-market and timing are critical, the rate of technological change is rapid, and the nature of future competition and markets difficult to determine. The term 'capabilities' emphasizes the key role of strategic management in appropriately adapting, integrating, and reconfiguring internal and external organizational skills, resources, and functional competences to match the requirements of a changing environment."

The need for adequate strategic decisions that fit with the changing business environment, goes hand in hand with good management practices to reach higher productivity, growth, and profits. The importance of management practices is crucial. Bloom et al. (2017) show that better management quality improved firm productivity and performance in both non-experimental and experimental settings, for a large sample of firms from 34 countries.

Forth and Bryson (2018) report a growing body of evidence showing that firms which engage in more extensive use of data collection and analysis, target setting and performance-focused human resource practices (such as training and incentive pay) are more productive – and have higher levels of productivity growth – than firms with fewer of these formal management practices. In their own empirical analysis, they find that, although SMEs are less likely to use formal management practices than larger firms, more extensive use of formal management practices helps SMEs to grow and increases their productivity (Forth and Bryson, 2018).

One of the main aspects to consider for an adequate strategic fit is the market structure and the type and intensity of competition confronted by a new venture or an established SME. Competition and management practices show a positive feedback. Firms in sectors facing greater competition are more likely to have better management practices, with an effect on better performance (Bloom et al., 2017). Regarding market structure, the most common types are oligopolies and markets of monopolistic competition. Economists have produced several models of oligopolistic markets, where few firms with a relevant market-share compete (and sometimes also collude).

The central element in this case is the strategic interdependence, whose main feature is the consideration of how firms respond to each other's choices. This is not the case in a market where monopolistic competition prevails, and this is the most attractive market structure for SMEs. In a context of monopolistic competition, firms may exploit diverse market segments innovating with slightly differentiated products and various cost structures. Regarding new firms, the different economic value assigned to knowledge by the entrepreneur, induces disruptive actions introducing new products (or radically new processes) in the market.

This is associated with a dynamic of creative destruction and is favoured by markets where differentiation prevails as Audretshc already stated in 1995. Reasoning in terms of existing

SMEs, the key issue is how the firm creates value for the consumer, that is what the combination of product attributes and prices that match consumer preferences is. This bundle of price and attributes, in the presence of monopolistic competition and differentiation, opens opportunities for the coexistence of firms of different MES in the same market (Besanko et al., 2013). A typical example is the beer industry, where small local breweries share the market with large capital-intensive companies, with different products, technologies, and cost structures.

However, considering the market structure and competition intensity, firms that are willing to increase productivity and improve their performance through better strategy and management practices, need to focus on some key areas for action such as innovation, digitalization, and internationalization. Innovation is a must to produce more efficiently new and better goods and services, digitalization is needed specially for SMEs, to reduce costs and reach the customers more efficiently, and internationalization is necessary to grow either as direct or indirect access to foreign markets (through integration in value chains), in those sectors open to trade. Effective action requires not only knowledge and skills to design and implement strategic decisions, but also necessary access financial resources to facilitate adequate strategic flexibility.

Innovation

Through new products and processes innovation firms reach out better to new markets. This firm-level innovation paves the way for the diversification of countries' productive structure, adding to their export portfolio more sophisticated products and services and making faster growth (Hausmann et al., 2007) viable. This productive and export diversification is possible when entrepreneurs explore their capacities to innovate as a mechanism of "self-discovery" (Hausmann and Rodrik, 2003). As reported by Barrere et al. (2021), the basic rationale is that innovating firms are the main agents of economic change, introducing more sophisticated products and processes and being the drivers of competitiveness and long-term growth at a country level (Hausmann and Rodrik, 2003).

Innovation is generally defined as the search for the discovery, development, improvement, adoption, and commercialization of new processes, new products and new organizational structures and procedures (Dosi, 1988; Stam and Wennberg, 2009). The process of innovation is a complex one, and involves the creation of knowledge (discovery, research, development) and the transformation of that knowledge into value usually through the markets.

Governments intervene in the process to solve market and systemic failures, and sometimes more proactively to favour innovative activities. They have an important role in the generation of an adequate innovation environment and in the provision of public complementary goods, investing in the first stages of the innovation process, where fundamental research is the main activity and risks are higher (Mazzucato, 2018, Chapter 7). But innovation involves the transformation of knowledge into economic value or of new ideas into economic and social solutions (Navarro et al, 2016), and this is mainly a role played by market firms. It may be radical or incremental and may intend to introduce new products and processes just for the firm, the local market or for the world.

Innovation is difficult to measure. In general, data refers primarily to inputs, such as research and development (R&D), staff or financial resources, or intermediate outputs, such as patents. Information on outputs such as sales of new products or share of turnover from new products comes from surveys as the Community Innovation Surveys in Europe or innovation surveys in other countries (Siepel and Dejardin, 2020)[5].

As reported by Wiklund et al. (2009), there is a strong direct effect of entrepreneurial orientation on firm growth. Entrepreneurial orientation is a construct including innovation, and attitudes associated with innovation as proactivity and disposition to adopt risk-taking actions. In fact, the innovation process involves uncertainty, risk-taking, experimenting, and testing. Empirical evidence on the effect of innovation on firm

5 These surveys are based on standards, for example those from the Oslo Manual or the Bogotá Manual.

growth is not unanimous, although it is well accepted as a positive influence. Coad (2009) reports that empirical evidence is not conclusive, particularly for growth measured by sales. Calvo (2006) studied the case of small, young, and innovating firms, and found that both process and product innovation are strongly and positively related to small firm survival and employment growth.

Innovations include R&D activities but are not limited to them. Non-technological innovations might be relatively more important than technological innovations, particularly for low-tech firms (Stam and Wennberg, 2009). R&D builds knowledge within the firm and improves its ability to understand and absorb knowledge from outside the firm (Cohen and Levhintal, 1989). The generation of absorptive capacity at the firm level is a key issue to promote business innovation (particularly entrepreneurial innovation) in developing countries, specially associated with linkages to international firms and markets (González-Pernía et al., 2015).

Innovation creates value but doing so requires reaching the market. Speed to market with distinctive new products and services can be a critical advantage for SMEs. Moreover, technology is disrupting the very process of innovation, so it is less dependent on capital investments and more dependent on talent and flexibility. There is also a growing trend towards open approaches to innovation. All in all, these tendencies benefit innovation activities by SMEs (Oxford Economics, 2017).

Digitalization

Economic literature has progressively recognized the link between information and communication technologies (ICTs) diffusion and productivity growth acceleration, both at the macro and at the firm level. At the firm level, as stressed by the extant literature reported by Grazzi and Jung (2019), ICT adoption can improve business performance speeding up communication and information processing, decreasing internal coordination costs, facilitating decision making, promoting firm restructuring, making internal processes more flexible and rational, and reducing capital requirements by improving equipment utilization and reducing inventory.

Moreover, through better communication with suppliers, clients, knowledge providers, and competitors, firms may increase their innovation capacity (Grazzi and Jung, 2019). These ideas are extensively discussed in the case of small businesses in studies by the International Labour Organization (ILO, 2021b) and are at the heart of the 'smart use of ICT' promoted by the European Union and the strategy for the digital transformation proposed by CAF in Latin America, to bolster the productivity and innovation capacity of SMEs (European Commission, 2015; Deloitte, 2020).

Already in 2017, Oxford Economics stressed that effective use of technology was increasingly important for SMEs, as more and more industries digitalize. Technology was becoming more affordable, cloud-based technologies allowed SMEs to invest incrementally in IT (without the risks of big investments), and it was possible to use partners to access new technologies. Then, according to the survey by Oxford Economics and American Express (2017), almost 60% of SMEs considered technology a priority to improve decision making, including data analytics, enterprise systems, and workforce productivity. Just over half of SMEs found improving operational efficiency a priority through the Internet of Things, process automation, and robotics. Since then, this tendency has been accelerating even before the dramatic changes were brought about by the COVID-19 pandemic.

In fact, digitalization opens new opportunities for young firms and SMEs to innovate and transform their business models and work practices. This transformation of the world of work (ILO, 2021a) and its potential implications for overall productivity and inclusive growth are large across the economy, including those sectors traditionally dominated by small firms (OECD, 2019).

As stressed by Katz et al. (2020) broadband connectivity usually translates into productivity improvements by facilitating the adoption of more efficient business processes (e.g., marketing, inventory optimization, and

streamlining of supply chains); in accelerated innovation by introducing new consumer applications and services (e.g., new forms of commerce and financial intermediation); and in more efficient functional deployment of enterprises by maximizing their reach to labour pools, access to raw materials, and consumers (e.g., outsourcing of services, virtual call centres). Several aspects stressed by OECD (2019) reveal these possibilities:

- Digital business platforms ease access to markets, strategic resources, and networks, by reducing associated costs (e.g., by pooling resources, by reducing information asymmetries, by connecting demand and supply).
- These business platforms reduce structural disadvantages faced by SMEs in achieving economies of scale, allowing them to reach scale without mass (e.g., accessing skills through online job recruitment sites, platforms for outsourcing and online task hiring, and interfaces connecting SMEs with knowledge partners).
- Big data analytics allow greater customization and product differentiation. Through mobile apps, sensors, artificial intelligence, 3D printing, drones, etc., SMEs may leverage shorter distances and time to markets, which in turn are likely to benefit smaller and more responsive businesses.
- Supply chains and wholesale businesses will need to adapt. Through the Internet of things, there is a way forward for real-time inventory and the development of integrated business intelligence systems.
- Digitalization also supports open sourcing and open innovation, with new opportunities for SMEs. Large firms may contribute to the transformation of business ecosystems through business accelerators and innovation labs that provide start-ups and innovative SMEs with access to resources and markets.

Although those promising avenues open for SMEs, they lag in digitalization (ILO, 2021b). These firms face more difficulties in undertaking complementary investments in skills and organizational changes that are needed to adopt and benefit from technology. According to OECD (2019), in 2018, across the OECD, large firms were twice as likely to purchase cloud computing services as small firms, and the gap was 3 to 1 in Mexico and Spain, almost 4 to 1 in France, and almost 5 to 1 in Poland. Firms tend to purchase more cloud computing services when they have access to enhanced broadband infrastructure and tend to adopt more complementary digital technologies (i.e., business intelligence software), when they also use cloud computing.

Unfortunately, gaps in high-speed broadband penetration rates between small and large firms have increased in recent years in all countries, revealing that both public investment and an adequate context for private investment in physical and digital infrastructure is required (Katz et al., 2020; Jung, 2020). In fact, regulatory frameworks must be adapted to address competition challenges from the increasing convergence of networks and services in the digital economy. A stable, predictable framework fosters long-term investment in broadband infrastructure and digital innovation. At the same time, innovation-friendly regulation is needed to facilitate new industries and digitally intensive firms (OECD et al, 2020). The SME lag in connecting to high-speed broadband or in using key digital technologies can jeopardize their participation in the next production revolution (OECD, 2019).

SMEs face also other obstacles. They are less prepared to face cyber security threats, which is a weakness to participate in complex and hyper-connected systems. SMEs are also less likely to have the skills for managing their digital transformation, and still too few of them engage their employees in ICT training (ILO, 2021b). Few small firms provide ICT training to their employees, less than 25% in most countries, and little progress has been made in recent years (OECD, 2019).

Internationalization

Internationalization is also a characteristic of the entrepreneurial orientation of a firm. It requires the proactive search for new markets,

introducing new or adapted products, with the uncertainty and risk associated with that strategy (Wiklund et al., 2009).

It is widely accepted that exporting has a positive effect on performance and growth (Coad and Tamvada, 2012; Jung et al., 2013) in those sectors open to trade. Lu and Beamish (2006) find that exporting has a positive impact on the growth of small and medium-sized firms (SME), measured by sales and assets growth. Empirical evidence consistently shows that exporting firms are more productive than non-exporters (e.g., Clerides et al., 1998; World Bank, 2019). Findings of other studies (e.g., Lu and Beamish, 2001; Federico et al., 2009), also conclude that exporting is an effective growth strategy for SMEs. However, the reason why such patterns are observed, and the direction of causality, are debated (World Bank, 2019).

The contribution of exporting to firm growth through sales seems straightforward. Higher sales provide the possibility of a higher production volume and expansion in production capacities to meet the market demands (Jung et al., 2013). Then, the larger volumes of sales and production made possible through exports enable firms to achieve economies of scale and increase labour productivity and management efficiency. These effects on firm competitive capabilities may be influenced also by economies of scope associated with product diversification.

There is an opportunity for smaller businesses with significant scope to compete in specialized segments of value chains and to scale up activities abroad while capitalizing on robust growth in emerging markets. This way SMEs may access foreign technology and knowledge and increase productivity and wages (OECD, 2019).

Firm innovation and export behaviour are generally seen as interrelated. Innovative firms are more likely to be exporters, while exporters are more likely to be innovators (World Bank, 2019). Anyway, it is unclear whether efficient firms self-select into export markets or if they experience faster growth once they begin to export (e.g., Bigsten et al., 2004; Eliasson et al., 2010; Coad and Tamvada, 2012). This is not a minor issue. As expressed by Barrere et al. (2021):

"Given the fact that a diversified and sophisticated structure of exports is important for long-run growth and that innovation is the key driver to reach productivity, complexity and diversification, the question is how firms may both innovate and access export markets. Attending to the product-cycle and technology gap theories, the sequence of the process turns out to be an important question. This is particularly the case of small and medium-sized enterprises (SMEs) from developing countries that confront restrictions in financial and human resources that limit their strategic choices, particularly to build the absorptive capacity needed to innovate and internationalize. In fact, given their limited resources, SMEs are forced to focus either on innovation or export activity (Neves et al., 2016). The main issue they face may be set out as an option between is innovation necessary to be more efficient and, in this way, access export markets or is the participation in export markets the way firms access new knowledge that enables further innovation. These two approaches, non-mutually exclusive, have been referred to in the literature as the self-selection hypothesis and the learning by exporting hypothesis."

When introducing the destination markets of firms located in a developing economy as part of the analysis, Barrere et al. (2021) find interesting results. When firms located in a developing economy export to another developing country, they find that innovation (either based in R&D or external knowledge) may – and perhaps should – be part of an export strategy. When the export market is a developed economy, they find that SMEs, are not able to cope with both strategies simultaneously or in a short period (Hauser et al., 2013), concluding that they may need more time and resources to overcome the technology gap and access the foreign market.

Whatever the sequence and the difficulties to be surmounted, SMEs may turn to exports as a focus to growth. A survey by Oxford Economics and American Express (2017), found that to boost export sales SMEs are investing in digital platforms, developing marketing intelligence in overseas markets, and partnering with established multinationals. Digitalization can create effective mechanisms to reduce size disadvantages in international trade and multinationals (MNEs) can play an important role in SME technology upgrading (OECD, 2019). The recent concentration of FDI in the acquisition of digital assets, especially in non-digital sectors, is likely to reinforce the importance of MNE-SME linkages for the SME digital transformation (OECD, 2019). To a lesser extent, SMEs are also setting up local branches and working with local agents to expand internationally, though these can require significant investment and local knowledge.

Future challenges for SMEs

- 3.1. Main drivers behind global megatrends
- 3.2. Emerging technologies as key drivers of disruptive change
- 3.3. COVID-19 crisis and firm response: Technological change and productivity
- 3.4. Specific issues about SMEs

3

3.1. Main drivers behind global megatrends

The global context is changing dramatically since the irruption of the pandemic in early 2020. But in fact, it was already changing at an unprecedented pace before the irruption of the pandemic, generating a completely new landscape for firms (SMEs and big companies alike), governments and individuals. There is a certain consensus about some features of the future the world was facing, where some drivers were mentioned once and again. Some examples may shed some light on this shared outlook.

In 2015, McKinsey and Co. published a document (Dobbs et al., 2015) identifying and characterizing "four global forces breaking all the trends": urbanization, accelerated technological change, aging population, and global networks. They argue that because of the interaction of these forces, change was happening ten times faster and at 300 times the scale compared with the Industrial Revolution, meaning an impact 3000 times greater.

In 2019, Euromonitor International called attention to five socio-economic drivers shaping consumer megatrends, stressing changes in behaviour, the emphasis placed on experience over possessions, and in healthy and ethical living: shifting economic power, technology, population change, environmental shifts, and pressures, and changing values (Euromonitor International, 2019). Ernst & Young, at the outbreak of the pandemic in 2020, identified four primary forces that were "the root causes of disruption": technology, globalization, demographics, and environment (Ernst & Young, 2020). The main driving forces of the future trends have not been recently discovered.

In 2019 the International Labour Organization and the International Organisation of Employers called the attention on similar trends: "Five global trends are shaping the way businesses across the world operate. Technological innovation, global economic integration, demographic and generational shifts, climate change and sustainability, and a global shortage of skilled labour are impacting businesses regardless of size, sector and location, with major implications for the Employer and Business Membership Organizations (EBMOs) that serve and represent them." (ILO/IOE, 2019, page xiii).

A brief synthesis of these driving forces will shed some light on the general environment where firms in general, and SMEs in particular, will compete and, hopefully, develop successfully in the future, even after the Covid-19 pandemic is over. This driving forces are relevant because they influence the evolution and prospects of social and economic activities.

- **A shift of economic activity:** Global economic growth is showing a huge shift to emerging markets. By 2030, the Chinese economy is expected to be 1.8 times larger than that of the USA (Euromonitor International, 2019). Additionally, economic activity within emerging markets will shift to cities. Dobbs et al. (2015) stressed that by 2000, 95% of the world's largest international companies (for example Airbus, IBM, Nestlé, Shell, and The Coca-Cola Company) were headquartered in developed economies, but by 2025, many of the world's large companies (defined as those with revenue of $1 billion or more) would be headquartered in emerging markets. At the same time, they noted that the population grew steadily in cities: the global urban population has been rising by an average of 65 million people annually during the three previous decades.
- **Technological changes:** A driving disruptive force is an acceleration in the scope, scale, and economic impact of technology. The role of technology as a disruptor is not new, but today is highly present in everyday life and changes at an unprecedented speed. We are now in a new revolution, powered by human augmentation technologies as artificial intelligence, autonomous vehicles, robots, augmented and virtual reality, and more (Ernst & Young, 2020). Dobbs et al. (2015) show the scope, impact and speed of change with some notorious examples: "It took more than 50 years after the telephone was invented until half of American homes had one. It took radio 38 years to attract 50 million listeners. But Facebook attracted 6 million users in its first year and that number multiplied 100 times over the next five years. China's mobile text- and voice-messaging service WeChat has 300 million users, more than the entire adult population of the United

States. Accelerated adoption invites accelerated innovation.

In 2009, two years after the iPhone's launch, developers had created around 150,000 applications. By 2014, that number had hit 1.2 million, and users had downloaded more than 75 billion total apps, more than ten for every person on the planet". The impact of connectivity and processing power is expanded with the extended availability of data and information. Data is a key asset driving the digital economy (ILO, 2021a). This has a high disruption impact that has profound consequences for the future. For developing countries, this trend is an opportunity, but it may widen the technological and productivity gap between and within countries and economic sectors.

- **Demographic changes.** The human population is getting older. This has been observed in developed economies for some time (for example, Japan, Russia with declining populations), and now the demographic deficit is spreading to China and Latin America. "For the first time in human history, aging could mean that the planet's population will plateau in most of the world. Thirty years ago, only a small share of the global population lived in the few countries with fertility rates substantially below those needed to replace each generation—2.1 children per woman. But by 2013, about 60% of the world's population lived in countries with fertility rates below the replacement rate. This is a sea change" (Dobbs et al., 2015).

  This aging of the population is not uniform across countries, and different generations have different influences across countries and regions. "The Gen Z[6] future is not evenly distributed. Generational change is occurring between countries, not just within them. The populations of the world's leading economies are growing elderly, while developing-market societies have growing numbers of youths. India stands out with a population that includes 375 million people — 27% of the total — in Gen Z. At the other extreme is Japan, where Gen Zers make up just 14% of the population" (Ernst & Young, 2020). Changes due to urbanization (61% of world's population living in urban areas by 2030), ageing (995 million aged 65 and over by 2030), and net migration (explaining more than half of population growth in Western Europe, Australasia, and North America to 2030), will reshape lifestyles and purchasing decisions (Euromonitor International, 2019).

- **Globalization:** The world has been going through a long wave of increased connectivity through trade, capital movements, people, and information (data and communication). Although this is a disruptive force that has changed the way economies and societies relate, there are some changes under way. "Trade and finance have long been part of the globalization story but, in recent decades, there's been a significant shift. Instead of a series of lines connecting major trading hubs in Europe and North America, the global trading system has expanded into a complex, intricate, sprawling web" (Dobbs et al., 2015). In fact, it seems that regionalization will characterize the future of globalization.

  Asia is becoming the world's largest trading region, with China and India increasing its weight and their companies moving up the value chain. Additionally, populism and nationalism spurred across several countries and regions and are likely here to feed a trend toward protectionism (Ernst & Young, 2020). Migration flows have been problematic for several regions. Although these are some forces shifting these strong previous trends towards globalization, "the links forged by technology have marched on uninterrupted and with increasing speed, ushering in a dynamic new phase of globalization, creating unmatched opportunities, and fomenting unexpected volatility" (Dobbs et al., 2015). But technology may also enable a more regionalized future, through more localized supply chains (Ernst & Young, 2020).

- **Environmental impacts:** After a long period of rapid but linear warming and change, the world enters a new phase marked by exponential climate impacts, volatility, and disruption (Ernst & Young, 2020). Changes can be found in conditions of temperature,

6 Population with ages between 10 and 24 years

air, oceans, and ice, and are happening much faster than previously thought. Climate change will be the catalyst and driver of profound economic and social disruptions. As stressed by Ernst & Young (2020), "business leaders must look at climate risk in a new way. Exponential climate impacts threaten more than supply chains and physical infrastructure — they endanger growth by exacerbating systems-level disruption to customers, investors, employees, and communities". SMEs adaptation and structural change towards a low-carbon economy will be an important challenge, particularly in countries with a large informal economy.

These radical changes are happening simultaneously and feeding each other. More than six years ago, Dobbs et al. (2015) argued that this "means that our world is changing radically from the one in which many of us grew up, prospered, and formed the intuitions that are so vital to our decision making. Our intuition has been formed by a set of experiences and ideas about how things worked during a time when changes were incremental and somewhat predictable... But that's not how things are working now—and it's not how they are likely to work in the future".

3.2. Emerging technologies as key drivers of disruptive change

Anyway, it may be argued that the main disruptor among these driving forces is the fast and radical technological change. In 2019, Dell Technologies and the Institute for the Future (IFTF), explored how emerging technologies would reshape human lives (and obviously business and societies) over the next decade. The introductory statement of their report is quite impressive:

"The gap between human and machine is shrinking. The difference between bits and atoms is blurring. A new era of human-machine alliances is on the horizon. Over the next decade, everything around us will become more intelligent, communicative, and connected. New kinds of networks, devices, interfaces, and artificial intelligences will help us augment, enhance, and optimize our lives. From autonomous vehicles to smart homes to digital cities we will not just live with our machines, but rather become more immersed and work in partnership with these machines and devices. We will evolve our abilities to program our lives for stability and resilience, to surpass our own limitations, to become augmented individuals. Over the next decade, the most powerful and successful relationships between people and computers will be those that are symbiotic and make use of their respective complementary strengths. Along the way, we will also undoubtedly grapple with negative unintended consequences, from possible threats to privacy and security to environmental degradation to new kinds of digital addiction. However, the only way to ensure that tomorrow's technology enables a smarter, better life for everyone, and reaches its true potential to drive human progress is to think systematically about what the future may hold and then make better decisions in the present".

▶ **(IFTF and Dell Technologies, 2019; page 3).**

The impact of processing power and connectivity is multiplied by the data revolution, which places unprecedented amounts of information in the hands of consumers and businesses alike, and the proliferation of technology-enabled business models as Alibaba, Airbnb, Amazon, Uber, and the like (Dobbs et al., 2015). These digital labour

platforms (online web-based and location-based platforms) are transforming business models and labour processes[7] (ILO, 2021a). Over these lines IFTF and Dell Technologies (2019) stressed the role to be played by some technologies that would drive a new wave of changes in the years to come[8]:

Internet of Things (IoT): will change the way we live and also reveal much about our homes, cities, and more.

Mobile Edge Computing: based on low-latency, high-bandwidth wireless networks, computing power will increase, bringing artificial intelligence to myriad connected devices.

5G and beyond: By 2030, 5G will move into maturity and 6G standards will continue the evolution of mobility networking, paving the way for smart cities along with a more intelligent industrial infrastructure.

Artificial Intelligence: Artificial intelligence is now rapidly expanding in capabilities and application areas. Machine learning based on big data is employed in everything from chatbots to self-driving cars.

Augmented reality: The virtual and real will blend in deeply immersive experiences that bring us closer together, no matter where we may be.

The rapid development of these technologies defies businesses and government agencies to take advantage of the full potential of Industry 4.0, with its ability to transform economies, jobs, and society through the introduction of new technologies and processes. "Definitions for Industry 4.0 abound, but the change it portends at its core is the marriage of physical and digital technologies such as analytics, artificial intelligence, cognitive technologies, and the internet of things (IoT). This marriage of the physical with the digital allows for the creation of a digital enterprise that is not only interconnected but also capable of more holistic, informed decision making" (Deloitte, 2018).

How can firms cope with these new and changing scenarios? Redefining their strategy based on their core capabilities, adjusting their structure to that strategy, and seeking differentiation to gain competitiveness (Nelson, 1991), targeting the markets in their new and emerging conditions with efficiency and productivity. Sustained productivity growth is a key component of any successful firm strategy since it enables companies to be profitable (by expanding output and/or minimizing production costs) and feed a virtuous loop. Firms can then reinvest such higher profits to continue increasing their efficiency and profitability in the medium term (ILO-ACT/EMP, 2020).

In the current context, this process implies a strong challenge for SMEs located in developing economies, especially because frequently it will require the adoption of new technologies. Introducing new digital technologies favours feedback loops that generate opportunities for new products and services, better ways to serve customers, new types of jobs, and new business models (Deloitte, 2018), with impact on industries, businesses, and society. These changes open new opportunities for young firms and SMEs if they acquire the capacity to use and combine emerging digital technologies to transform their business models and work practices. Potential implications for overall productivity and inclusive growth are large across all business sectors, including those traditionally dominated by small firms (OECD, 2019).

Particularly in developing countries, policies should be oriented towards favouring technology adoption and skills development, and supporting productivity growth that is the way SMEs may reach economic viability and growth potential. The attraction of FDI, being a way to ease

7 On online web-based platforms, tasks or work assignments are performed online or remotely by workers. These tasks may include carrying out translation, legal, financial, and patent services, design, and software development on freelance and contest-based platforms; solving complex programming or data analytics problems within a designated time on competitive programming platforms; or completing short-term tasks, such as annotating images, moderating content, or transcribing a video on microtask platforms. The tasks on location- based platforms are carried out in person in specified physical locations by workers, and include taxi, delivery, and home services (such as a plumber or electrician), domestic work and care provision (ILO, 2021)

8 On a similar vein, see for example "Banco Interamericano de Desarrollo, Disrupción exponencial en la economía digital, III Cumbre Empresarial de las Américas, Lima, Perú, 2018"

technology diffusion, is a key component of economic policies in developing economies, but it should be accompanied by internal efforts to develop absorptive capacity to be fruitful in terms of innovative entrepreneurship and SME development (González-Pernía et al. 2015). This context of change was already challenging for business in general (and SMEs in particular), even before the disruption of the COVID-19 pandemic.

3.3. COVID-19 crisis and firm response: Technological change and productivity

The COVID-19 crisis and beyond

The COVID-19 pandemic has caused health and economic crises that have disrupted economies and societies worldwide. It will have long-term effects, and its final outcomes remain relatively uncertain (OECD, 2021). One of the distinctive features of this crisis from an economic standpoint is that it has affected both supply (companies faced reduced labour supply, could not offer their services or produce, and could not obtain supplies) and demand (consumers suffered fear of contagion or were not able to access stores; uncertainty and lost income lead to a drop in demand), needing both aspects to be addressed (Ketels and Clinch, 2020; OECD, 2020).

In 2020, in most countries GDP dropped, jobs were lost, and unemployment soared. With different emphasis according to the global strategy adopted by each country, businesses were forced to close for long periods and in some cases, they permanently shut down. Consumption and investment were reduced because of lower-income and greater uncertainty. Governments stepped up expenses, subsidies, tax exemptions, and introduced some level of flexibility in payments and credits, to facilitate a transition to a better economic situation post-pandemic.

Evidence on the COVID-19 crisis impacts on SMEs from business surveys indicates severe disruptions and concerns among small businesses (OECD, 2020). An OECD report updated to July 2020, presents the outcome of 41 SME surveys identified world-wide on the impact of COVID-19 on SMEs. All in all, more than half of SMEs faced severe losses in revenues, and up to 50% feared to be out of business without further support in the short run. On average, businesses reduced their employees by 40% and three-quarters of respondents indicate they have two months or less in cash in reserve.

Estimates by the Small Business and Entrepreneurship Council of the United States, showed that 9.4 million small businesses (almost 30% of the total) closed between January and December 2020, some permanently. By mid-April 2020, the SMEs closed were 44%. Similarly, according to a survey among SMEs in 132 countries by the International Trade Centre (ITC), two-thirds of micro and small firms reported that the crisis had strongly affected their business operations, and one-fifth faced the risk of shutting down permanently (ITC, 2020).

Based on surveys taken in several of countries, McKinsey (2020) indicates that between 25% and 36% of small businesses could close permanently due to the disruption in the first four months of the pandemic. In Latin America and the Caribbean, the crisis severely impacted productive structures, resulting in the closure of more than 2.7 million firms, and the labour market, as the number of jobless persons has escalated to 44.1 million (ECLAC, 2021). The ILO estimated the impact of COVID-19 to result in a rise in global unemployment of between 5.3 million and 24.7 million, signalling that 'sustaining business operations will be jeopardize Small and Medium Enterprises (SMEs)' (ILO, 2020)

Confronted with this crisis, with a dramatic drop in demand and a disruption of production conditions, firms were pushed to change, adapt, and innovate or to turn informal or even to close. Firms that had managed to remain in (formal) business, took measures to reorganize, digitalize, and invest in other technologies. McKinsey Global Institute (2021) stresses that sector reviews show real productivity[9] potential gains from

9 Labour productivity, measured as gross value added divided by total hours worked, expressing the average value created for each hour devoted to the production of goods and services.

actions taken, although "early firm-level evidence suggests that advances have been relatively concentrated in leading sectors and in so-called superstar firms.

If this concentration is confirmed and persists, any acceleration in productivity growth could fall short of potential. The gap between superstars and a long tail of lagging or zombie companies could widen, and income inequality or unemployment could increase. The technology gap in favour of big companies from leading sectors, especially in developing economies, would give place to a productivity gap. Actions should be taken to foster technology adoption and productivity enhancement by SMEs.

Covid-19 pandemic implied a test for industrial digitalization. Companies maintaining operations, across sectors, must reorganize yet protect their employees. Did Industry 4.0 technologies help firms to manage the challenge? Imagine a firm of professional services going overnight to online work from home, or a restaurant relying on delivery sales and internet and social networks marketing, for example. Those SMEs that had previously had some experience with digital technologies were in a better position to respond to the crisis through these tools.

It is reasonable to expect that some of those firms needed to re-evaluate the progress of any digital transformation and decide which further action to take. Those SMEs which had not explored the use of digital technologies had a longer way to go, not only investing and mastering new technologies but re-thinking their business model in the middle of the crisis. It could be argued that previous experience with Industry 4.0 technologies helped firms in general -and SMEs in particular- to react to the crisis of the COVID-19 pandemic.

The pandemic has reinforced the value of industry 4.0, but it has also exposed the technological gap between frontier firms and smaller ones with lower productivity and the limitations of today's implementations (ILO, 2021b). Moreover, many businesses faced challenges to adopt new technologies, such as running short of cash for technology investments, while the crisis put more pressure on talent. The crisis affects sectors in very different ways: some face a prolonged period of low demand, others face an additionally drop in prices and cost pressures, other as medical products need to cope with high and volatile demand in some products and below average in others. Supply chains disruptions in some cases pose the need to work on resilience and flexibility, not limited to costs and efficiency (Agrawal et al., 2021).

What to expect in post-pandemic times

The post-pandemic evolution of productivity will likely depend on two drivers: the strategies and decisions of enterprises and the economic conditions in which these enterprises operate. The strategic decisions of firms -particularly SMEs- required during the pandemic and will require afterwards policies oriented to re-build productive capacity and foster investment in technologies and changes in business models.

The fiscal efforts made by governments during the pandemic will limit possible support programs, so public and private sectors should be creative and bold. Robust aggregate demand is a necessary component to favour higher productivity at the firm level impacts in a widespread increase in productivity (McKinsey Global Institute, 2021), but that demand needs to encounter an adequate supply capacity. In a context of growth in consumption, investment, exports, and public demand, and reduced uncertainty, firms should be prone to innovate and invest in higher capacity and new technology, but they will need enabling support.

This is the appropriate setting for economy-wide productivity growth, which is the favourable environment for actions oriented to reach productivity gains in SMEs. This post-pandemic era will show some distinctive features, as stressed by Sneader and Singhal (2021):

- ***A consumer rebound.*** As consumer confidence returns, demand will grow but with differences across sectors. Some services that have suffered the most, with restrictions to their businesses and deep drops in demand, are expected to bounce back with more strength (for example, restaurants, entertainment, tourism). How fast and deep confidence will recover is an open question, and probably

will be different for each country. Spending will only recover as fast as the rate at which people feel confident about becoming mobile again (Sneader and Singhal, 2021). The rollout of COVID-19 vaccines undoubtedly will affect the speed of recovery, and probably this will determine which developing economies will lag.

- ***A special case: travel.*** Leisure travel is discretionary while business travel is less so. Leisure travel will recover hand in hand with confidence about mobility. But will business travel recover to pre-pandemic levels? Almost certainly not as much as before. Video calls and collaboration tools that enable remote working, for example, could replace some onsite meetings and conferences. Sneader and Singhal (2021) argue that regional and domestic business travel will likely rebound first, and then extend to other destinations. All in all, however, they report that executives in the field think that global economic growth will generate new demand, but it may never recover to the 2019 level.[10] Structural changes in business travel will be part of the new norm.

- ***A time for innovators and entrepreneurs.*** COVID-19 crisis has been devastating for small businesses. As reported before, there has been a worldwide disruption in economic activity with severe losses in SMEs revenues and with temporary and permanent closures (or exit into informality), both in developed and developing countries. However, it seems to be a positive signal at least based in data of some developed economies. Sneader and Singhal (2021) report in the case of the US, in the third quarter of 2020, there were more than 1.5 million new-business applications (two times the figure for the same period in 2019). Although many of those businesses are non-employee establishments, it is worthy to note that "high-propensity business applications" (those likeliest to turn into businesses with payrolls) had also risen strongly (more than 50% compared with 2019). They also report that in the European Union, perhaps because of a recovery strategy centred on protecting jobs, the surge in new ventures was more moderate. Anyway, they report strong new business formation in the third and/or fourth quarters of 2020 in France, Germany, the UK, and Japan, among others. In the UK, for example, new businesses registered in the third quarter of 2020 rose 30% compared with 2019 (largest increase since 2012). It is to be seen how this trends may be sustained and how the prospects in developing countries continue.

- ***Digitally enabled productivity gains.*** Although it was already a trend under course, the COVID-19 crisis brought an acceleration in the growth of digitalization: from online customer service to remote working, to supply chain reinvention, to the use of artificial intelligence (AI) and machine learning, or to improve operations (Ketels and Clinch, 2020). Even healthcare has changed substantially with the development of telehealth and biopharma. As stressed by Sneader and Singhal (2021): "There's no going back. The great acceleration in the use of technology, digitalization, and new forms of working is going to be sustained."

Post-pandemic, business trends, and firm response

COVID-19 crisis has pushed companies to reconfigure their operations and innovate, opening an opportunity for radical transformation. To do so, and enter a path of sustainable productivity growth, firms need to redefine their strategy based on their core capabilities, adjusting their structure to that strategy, and seeking differentiation to gain competitiveness (Nelson, 1991). Technology adoption, skills development, and digital infrastructure are necessary to sustain these SMEs decisions.

Public policy has a clear role in this respect, to ensure that digital technologies generate economy-wide productivity growth. The diffusion and impact of digital technologies on productivity,

10 Sneader and Singhal (2021) report that in 2018, business-travel spending reached $1.4 trillion, which was more than 20% of the total spending in the hospitality and travel sector and represent a disproportionate share of profits.

particularly in developing countries, are not automatic and depend on indispensable elements, including proper access to and diffusion of digital technologies, healthy business dynamism, SMEs' engagement in digital transformation, and adequate competition in the digital economy (OECD et al. 2020).

Joining the digital economy could enhance SME development [ILO, 2021b]. Digital channels become the primary access to customers, automated processes become a primary driver of productivity (and the basis of flexible, transparent, and stable supply chains), and agile ways of working are a prerequisite to meeting seemingly daily changes to customer behaviour (Blackburn et al., 2020). Nonetheless, how digitalization will feed long-term productivity growth has yet to be evaluated.

There are at least two important features to highlight from this process. First, the necessity to introduce changes to respond to the crisis and support firms to install or adapt new technologies under pressure. This will require complementing the effort with a more holistic approach (for instance, capability building and institutionalization of current advances). Second, the speed at which technology and digitalization are spreading across the economy and society in general is an indication of a fast impact on productivity. The transition from digitalization innovations as 'cool new things' to productivity drivers will speed up in relation to the impact of new technologies in the past (Sneader and Singhal, 2021). Structural productive conditions and aggregate demand are necessary enablers for this to happen.

Some expected business trends that firms need to confront in this post-pandemic era, are a consequence of the changes in course, accelerated by the COVID-19 crisis:

- ***Changes in shopping behaviour are here to stay.*** Shopping behaviour has changed for good. The Economist Intelligence Unit estimates that online retail sales in the 60 biggest economies will be likely to account for nearly 20% of total retail sales by 2025, up from 10% in 2019, even affecting sectors that have traditionally been less reliant on digital sales, such as automotive (EIU, 2020). Sneader and Singhal (2021), based on McKinsey surveys, argue that two-thirds of consumers have tried new kinds of shopping and more than 65% intend to continue to do so. Moreover, they abound about the pace of change:

"Specifically, the shift to online retail is real, and much of it will stick. In the United States, the penetration of e-commerce was forecast in 2019 to reach 24% by 2024; by July 2020, it had hit 33% of total retail sales. To put it another way, the first half of 2020 saw an increase in e-commerce equivalent to that of the previous ten years. In Latin America, where the payments and delivery infrastructure are not as strong, e-commerce use doubled from 5 to 10%. In Europe, overall digital adoption is almost universal (95%), compared with 81% at the start of the pandemic. In normal times, getting to that level would have taken two to three years. Strikingly, the biggest increases came in countries that had previously been relatively cautious about shopping online. Germany, Romania, and Switzerland, for example, had the three lowest online penetration rates prior to the COVID-19 crisis; since then, usage increased 28, 25, and 18%age points, respectively—more than in any other markets."

▶ **(Sneader y Singhal 2021)**

This change in the behaviour of consumers poses a big challenge to firms and brands that want to sell directly to consumers and at the same time have become an opportunity for SMEs. They should be prepared, developing new skills, capabilities, business, and pricing models

- ***Supply chains require more sophisticated management.*** The COVID-19 pandemic revealed vulnerabilities in the long, complicated supply chains of many companies. Sneader and Singhal (2021) report that three issues were found to be relevant to how supply chains worked.

  First, disruptions are not unusual. They are predictable features of doing business that must be managed like any other. Second, cost differences among developed and many developing countries are narrowing. In manufacturing, companies that adopt Industry 4.0 principles (meaning the application of data, analytics, human-machine interaction, advanced robotics, and 3-D printing) can offset half of the labour-cost differential between China and the United States. And third, most businesses do not have a good idea of what is going on lower down in their supply chains, where sub-tiers may play small but critical roles.

  These findings require more sophisticated risk management. With the development of artificial intelligence and data analytics, companies can learn more about audit, and connect with their entire value chains, managing better risks and costs. Security and resiliency, and not so much cost optimization, have turned out to be most important in supply chain management.

- ***The future of work is already here.*** The future of work has been an issue for some time. A large strand of studies analysed how digitalization, remote work, automation, and the like would affect the way people worked. Moreover, studies projected how many existing jobs would be lost or new jobs would be created. Workforce development was a priority even before the pandemic. The idea was in the air but not proceeding very far or fast. But the pandemic changed that, and again, accelerated the trends.

  Tens of millions of people transitioned fast to working from home in a wide range of industries (even in healthcare, where telehealth visits increased exponentially). Companies such as Zoom, Okta and Slack, and TikTok developed fast and changed the way teams operate. Remote working will have far-reaching implications, with effects on everything from customer management to recruitment. In manufacturing, companies are automating production and stepping up digitalization of supply chain management and product design (EIU, 2020). The McKinsey Global Institute (MGI) estimates that more than 20% of the global workforce (most of them in high-skilled jobs in sectors such as finance, insurance, and IT) could work effectively away from the office. This is a "once-in-several-generations change" (Sneader and Singhal, 2021).

  There are two important challenges related to the transition to working away from the office. One is to decide the role of the office itself, which is the traditional centre for creating culture and a sense of belonging. The other challenge has to do with adapting the workforce to the requirements of automation, digitalization, and other technologies. It is a challenge across the board, even in sectors not associated with remote work (Sneader and Singhal, 2021; ILO, 2021a).

- ***The biopharma revolution takes hold.*** The COVID-19 pandemic triggered an accelerated process of merging biology with technology. The sequencing of the COVID-19 genome and the development of the vaccines are the most visible features. But the implications are by far much wider. "Urgency has created momentum, but the larger story is how a wide and diverse range of capabilities—among them, bioengineering, genetic sequencing, computing, data analytics, automation, machine learning, and artificial intelligence (AI)—have come together" (Sneader and Singhal, 2021). This technological convergence also impacts activities like agriculture, energy, materials, among others, signalling the amplitude of its widespread potential.

Some other issues that firms should consider in this post-pandemic time are changes in the structure of industries and the adaptation towards a low-carbon economy. The COVID-19 crisis had a very divergent sectorial impact. Some industries suffered badly because of the drop of demand or restrictions and problems organizing production at the firm level. Other industries flourished because of high demand and the possibilities of transforming their process online. Probably, these

disparities will tend to balance back with new normality in place.

What probably will show lasting consequences are the structural differences within industries. Resilient businesses will come out stronger while others will be severely weakened. With respect to business adaptation to climate change, enterprises need to consider and incorporate in their decision-making processes climate risks, which implies the development of an enterprise risk management strategy to strengthen business resilience and be better equipped to cope with global risks, black swan events and climate change.

How can firms cope with this fast shift to use industry 4.0 technologies? Given the contextual situation and how the firms seem to be prepared for digitalization, Agrawal et al. (2021) suggest a course for action:

"Against this background, a laser-focused approach to Industry 4.0 transformations seems the most realistic choice for most companies. Over the coming months, few organizations will have either the time or resources to support a scattergun approach to digital experimentation. Most will be better served by building a strategic roadmap for their Industry 4.0 ambitions, picking a handful of digital use cases that target their top one or two strategic objectives, and pursuing a rapid, agile process to refine, roll out, and aggressively scale these technologies."

In this scenario of accelerated changes in business trends, and in the context of recovery from the COVID-19 pandemic crisis, firms will have to make strategic decisions that go far beyond their usual business. The main goal of firms, whatever its size, should be to reach a productivity level to be competitive in the new business conditions. Every firm will need to define the best combination of strategy, structure, and capabilities (Nelson, 1991) to be successful in the new market conditions. McKinsey Global Institute (2021), based on its surveys and bottom-up analysis, looked at drivers that could result in productivity growth in the current context of pandemic crisis and beyond. Their main findings shed some light on the possible emphasis of firm strategy in the near future:

- **Innovation and business models.** The pressures of the crisis forced many businesses not only to be more efficient (reducing costs) but also transform their products, commercialization, and operating models. Resiliency (the ability to absorb a shock and recover swiftly) will be a key asset to the survival and long-term prosperity of the firms. But looking into the post-pandemic era, firms not only need to be reactive but re-think their business models and embrace innovation as part of their core capabilities.

  In a recent survey to executives and firm managers by McKinsey Digital (2021)[11], 64 percent of the respondents say their companies need to change their business models to build new digital capabilities to be economically viable through 2023. This should be a global approach for firms, integrating Industry 4.0 technologies, operational efficiency, and the required human capital. This way strategies may be sustained in the long run and potentially drive faster productivity growth.

- **Digitalization, automation, and a shift to online channels.** During the crisis, some firms accelerated the pace of digitalization and adoption of other technologies, struggling to be more efficient and agile. Remote working became the norm. These changes will transform business over the long term and could raise productivity (either by reducing costs or boosting output per worker) but are yet concentrated in some firms. In regions where relatively few companies use digitalization in their everyday operations and productivity disparities are considerable according to

11 The online survey was in the field from January 19 to January 29, 2021, and garnered responses from 1,140 C-level executives, senior managers, and business-unit, department, or division heads representing the full range of regions, industries, company sizes, and functional specialties.

the size of the firms. In Latin America and Caribbean, the digital transformation brings an opportunity but also a risk of reinforcing disparities.

Therefore, this situation should be incorporated in policy agendas and organizational strategies, because greater digitalization is a feature of the post-pandemic economy. As well as for SMEs, firms will have to adopt technologies to process large amounts of information to improve decision processes, introduce changes in sale and delivery of goods and services or in interactions with suppliers, and redefine business models (OECD et al. 2020; ILO, 2021b)).

This process of adapting to Industry 4.0 in the post-COVID-19 world, will not be uniform across firms and industries. Some firms may accelerate previous plans to introduce digital technologies in their day-to-day business, while others may put in pause any effort in this regard, because of productive or financial difficulties. Perhaps the main bulk of SMEs will adopt a more cautious approach selectively implementing digital technologies to meet specific and focused objectives (Agrawal et al., 2021)

- **Operational efficiency.** The reaction of many firms to the crisis brought about by the pandemic shows the capacity to rapidly transform the organization when needed. This flexibility and capacity to be agile in change and transformation confronted to new scenarios is an organizational asset. These are key capabilities in uncertain times, especially for SMEs, and may make the difference to fasten productivity growth.

- **Investment in human and physical capital.** These are two key elements to drive productivity growth, and a post-crisis period will require appropriate funding schemes. McKinsey Global Institute (2021) reports that 72% of respondents to a KPMG survey ranked re training in new skills as one of the most important paths to shaping the workforce, yet only 33% said it was easy to implement "There are no easy fixes to talent and organization challenges, however. Companies will need the right people and the right processes in place to support their Industry 4.0 ambitions" (Agrawal et al., 2021). Firms in the post-COVID-19 economic environment will require people with some critical skills such as in data science and IoT engineering.

The different components of firm strategy make sense if considered in an articulate manner. To reach a successful productivity outcome, they must be integrated into a comprehensive approach, which for each firm will have different weights for each component. This will require a learning process to find the best strategic fit. Research indicates that people and organizations learn more quickly because of network effects. An environment of competition and cooperation seems to be the best way forward to profit from the network effects (Blackburn et al., 2020). Although in the short term, the effect of the pandemic could hamper productivity growth, comprehensive action by firms may enhance productivity if those actions spread in a context of recovery of productive capacity and growth of aggregate demand.

3.4. Specific issues about SMEs

In this context of business trends and pandemic crisis that pushes firms to transform and adopt new technologies to ensure business continuity and become more productive, SMEs face specific challenges. They need to survive but also to transform themselves to face the 'new normal' post-pandemic world. How SMEs adapt to the new reality will have significant implications on employment, productivity, and economic growth.

Moreover, SMEs will play a vital role to sustain the economic recovery. In this respect, two main factors can be brought out. First, as individuals face loss of income and uncertainty, the reduction in consumption will have an impact on SMEs through different channels such as a fall in demand and backward and forward linkages among them and with large enterprises. Second, the crisis is likely to call into question regional economic development plans, to build forward a more powerful and sustainable economy. In such a transition, supporting SMEs in adapting towards

a sustainable economy will be key to minimize labour market disruptions.

Specific challenges faced by SMEs

Some factors increase the difficulties faced by SMEs to take actions in the crisis and during the post-pandemic recovery (OECD, 2021; Albaz et al., 2020; ILO 2020, ILO 2021), as they need to reach higher levels of productivity and build stronger firms, with business models capable of coping with future shocks:

- ***Reduced demand and liquidity challenges.*** Smaller firms are typically more financially fragile and have smaller cash buffers than their larger counterparts (OECD, 2021). The pandemic brought a sudden and dramatic decline in demand that confronted SMEs with liquidity problems and difficulties to surmount them. As reported by Albaz et al. (2020): "According to 15 surveys in Organisation for Economic Co-operation and Development (OECD) countries, more than half of SMEs already face severe losses in revenues, with many having only a few months of reserves. In Portugal, 37% of SMEs reported a more than 50% drop in production. At the start of the outbreak, two-thirds of SMEs in China reported having enough cash to cover fixed costs for no more than two months. In the United States, an average small business has only 27 days of cash flow".
- ***Weakness to manage supply chains difficulties.*** SMEs have weaker supply chain capabilities than their larger counterparts, particularly they have smaller management teams to react when difficulties surge (OECD, 2021). The irruption of the pandemic showed two main problems in this regard (Albaz et al., 2021): a) the disruption of these supply chains, leaving many SMEs facing higher costs or without the materials needed to maintain operations; b) measures adopted to slow the disease from spreading during the pandemic disrupted SME production processes, and these firms do not have factory floors designed for physical distancing, causing difficulties to reconfigure operations.
- ***Lag in use of digital tools.*** Smaller companies lag in terms of the uptake of digital tools and technologies which can help to build resilience in the current pandemic crisis. Digitalization brings opportunities for gains in productivity by SMEs, but they face barriers that hamper the possibilities of achieving a real digital transformation (ILO, 2021b). Although surveys show that the pandemic has increased the use of digital technologies by SMEs, there are differences between countries and firm sizes. The uptake of digital technologies by SMEs is roughly half of that by larger firms (OECD, 2021).
- ***Labour shortages*** with adequate skills and the need to reach ***new employment arrangements***, related to changes in business models and adoption of digital technologies (e.g., telework) are an important challenge for SMEs.
- ***SMEs overrepresentation in hardest-hit sectors.*** SMEs are overrepresented in the sectors most affected by the crisis, in particular wholesale and retail trade, air transport, accommodation and food services, real estate, professional services, and other personal services (OECD, 2021). Whereas in the business economy at large, SMEs account for over 50% of employment across OECD countries. In these sectors the share of SMEs in employment is on average 75% (OECD, 2020). These sectors will take longer to recover due to long-term demand and supply disruptions, including retail, hospitality, food service, entertainment services, and construction (Albaz et al., 2020).

Issues for an SME post-pandemic policy agenda

As stressed by OECD et al (2020) for LAC countries, the outcomes of the waves of contagions, mobility restrictions and moderate policy support may well become the destruction of some capital (i.e., firm bankruptcies) and high unemployment and informality. Given the fact that low productivity has long been a hindrance to potential growth, policy efforts should be directed to facilitate mobility and efficient reallocation of resources to more productive firms and sectors.

There is much to advance in this regard to promote SMEs building back and upgrading competitiveness in the 'new normal' situation: building infrastructure, particularly for digital diffusion; fostering skills development; promoting

competition, innovation, technological adoption and entrepreneurship; supporting SMEs' efforts to adapt to a low-carbon economy; simplifying regulations and tax systems to encourage firm expansion and formalisation; and improving state capacities to provide better goods and services to citizens (OECD et al., 2020). The International Labour Organization has been promoting an enabling environment approach that is a combination of conditions which may favour an enterprise's capacity to start up, grow and create decent jobs (ILO/EESE, 2021).

It is worthy of attention to highlight some of the issues and policy areas that will require governments and support organizations in the post-crisis times and that should be part of a structural agenda for SMEs in the 'new normal' (OECD, 2021; Albaz et al., 2020).

The first necessary condition to favour SMEs recovery and further development in the post-pandemic era is the fluent access to financial instruments. Particularly important are the ***liquidity support*** measures adopted by governments during the pandemic or to be adopted in the transition to a 'new normal' situation. Financial resources are necessary not only to fund the recovery of pre-crisis level of activity but also to facilitate the strategic flexibility needed to adapt to the new reality. These include access to venture capitals and credit guarantee schemes (OECD, 2019).

Ease SME access to support. SMEs need comprehensive support, and this calls for a single and integrated point of contact for SMEs that could work as a 'SME nerve centre' (Albaz et al., 2020). This would facilitate increased SMEs' participation and a more suitable design of support programs. SMEs need fast and easy access to services. Additionally, that 'SME nerve centre' can monitor the impact of programs establishing a feedback loop.

Focus on building competitiveness for the 'new normal'. The speed of recovery will depend on the ability of SMEs to return to sustainable operations post crisis and to the redefinition of their business models. Some initiatives should be highly placed in an SME policy agenda (OECD, 2021; Albaz et al., 2020):

Productivity-enhancement programs will be essential for the survival of SMEs and their ability to compete internationally. While many SMEs have fought through the crisis by, for instance, introducing rapid e-commerce solutions, they need more innovation and digitalization to further enhance their economics and assure their survival and further competitiveness. Support for digitalization, innovation, technology development, and up skilling and re training of the workforce are key issues for SMEs to reach a sufficient MES and escape the productivity trap in the new reality (ILO, 2021b).

- ***Public procurement*** may be a key instrument for sustainable SME development, given its share of total demand (for example, 30% in OECD countries and more than 50% in developing countries). It would be important to ease restrictions and administrative burdens to foster SME participation in public procurement.
- ***Support technological adoption and digitalization*** by SMEs, including skills development in a context of rapid change, as a challenge to be addressed by public/ private collaboration.
- The pandemic has disrupted ***supply chains and international trade***, and SMEs will need support and resources to rebuild the broken connections and access new markets.
- Support high-performing and innovative ***companies with scale-up potential***. These firms account for 2 to 3% of SMEs in most countries but generate more than 60% of economic and employment growth (Albaz et al., 2020).
- Promote ***entrepreneurship*** aimed at enhancing business creation (Kusinikova, 2020), particularly innovative ventures, in priority industries, increasing the number of high-quality jobs, easing business formation and registration, and improving the socioeconomic resilience and competitiveness of SMEs. The promotion of accelerators and incubators may be very helpful in this context (OECD, 2019).
- Policies oriented to ***promote clusters and industrial districts***, may favour externalities and spillovers, strengthening networking, interdisciplinary and research capacity through more industry-science, cross-sectorial and international interactions (OECD, 2019).

Selected cases of supporting actions

- Federal Ministry for Economic Affairs and Industry (BMWi), Germany
- SPRI, Basque Country, Spain
- Confederation of British Industry (CBI), United Kingdom
- National Business Association of Colombia (ANDI), Colombia
- Singapore National Employers Federation (SNEF), Singapore
- Federation of Egyptian Industries, Egypt

4

The business environment varies largely across regions and countries. Most developed economies have more competitive business environments, where public and private institutions offer a vast range of services. Usually, in developing countries companies face a diversity of business barriers and both, financial and non-financial services, especially for SMEs, are not sufficiently developed. This situation accentuates the importance of upgrading financial and non-financial business services to SMEs. As stressed by Abdulaziz et al. (2020), "with the right support, small and medium-size enterprises could significantly boost economic growth." Financial access in favourable conditions is required for the development of small businesses, and it is a necessary condition for the advancement of non-financial services for SMEs, especially in a systemic approach (for instance, the case of the German KfW is an example of best practices in this regard).

During the Covid-19 pandemic unprecedented coordination efforts of public and private institutions to cope with the difficult situation took place in many countries. In the case of Employers and Business Members Organizations (EBMOs), there was an active interaction with public authorities and policy makers about appropriate ways of mitigating the effect of the pandemic on private companies, preserving business activities and safeguarding jobs. (ILO-ACT/EMP, 2021).

The problems faced by SMEs and the response to the pandemic by public and private organizations brought out the necessity of a systemic approach and intense networking. There are several examples worldwide of this kind of approach to non-financial support services to SMEs coordinated by private and public organizations.

A traditional and comprehensive approach is the systemic support to SME that is part of the German strategy for SMEs. The German economy has a wide and strong basis of SMEs, which excel in international presence being world class firms. The so called Mittelstand is usually referred to as the main economic engine of Germany. The German government leads these efforts and consults with different stakeholders the implementation of the SME support strategy with the objective of helping SMEs overcome the challenges of the fast-changing conditions. It has established a Committee of State Secretaries for the SME Sector.

"With the SME Strategy, our aim is to support SMEs in overcoming the economic challenges in a changing world, and in maintaining and consolidating their strong position in the face of national and international competition now and in the years ahead. The Strategy is to help ensure that the SME sector remains resilient even during weak economic periods and continues to be the mainstay of the economy it has always been. It contains measures that will take effect on the short term, but also actions that will help safeguard the competitiveness of the SME sector over the longer term. Our focus here is primarily on creating a clear, consistent, and stable framework, complemented by suitable forms of assistance. After all, one of the fundamental principles of the Social Market Economy is that the state should define the framework but interfere in the market as little as possible. This will give businesses the flexibility, freedom and certainty they need to be equipped to face the challenges of the future and develop their innovative talent to the full."

▶ **(Federal Ministry for Economic Affairs and Energy- BMWi, 2019).**

The German case is paradigmatic, because it is part of a more global economic strategy, it is systemic, participative, centered in SMEs and sustained through time. Some of the key points of the German SME Strategy, under the leadership of the Federal Ministry for Economic **Affairs and Industry (BMWi)** are presented in the next box.

Organization/ Country

Federal Ministry for Economic Affairs and Industry (BMWi), Germany

Public/ private

Public leadership, with private participation

General areas of intervention

- Improving the policy environment
- Improving Germany's tax policy
- Continuing to reduce bureaucracy
- Labour market
- Developing and building strong, efficient infrastructures
- Financing for the SME sector
- Strengthening entrepreneurship
- Attracting, training and skilling specialised workers

Supporting SMEs in the areas of innovation and digitization

- Transfer Initiative
- Tax credit for research and development
- Mittelstand 4.0 Centres of Excellence
- "Digital Agency"
- IT security
- Investment grant programme
- AI technologies
- Data economy and the competitive framework

Developing new markets in Germany and abroad

- Industrial Strategy in Germany and Europe
- A level playing field
- Promotion of foreign trade
- Business networks

Another interesting case of public leadership in developing non-financial services for SMEs with a comprehensive approach and private participation, but at a regional level, is that of the Basque region in Spain. In this case, the SME strategy is organized with multiple public agencies and private organizations coordinating efforts to support SMEs. In 2021, the **SPRI**, under the Department of Economic Development, Sustainability and Environment, offers a bundle of support measures for SMEs, including 68 support programs related to different topics and business areas.

Organization/ Country

SPRI, Basque Country, Spain

Public/ private

Public, with private participation

General purpose

"We work for companies just like yours, who are looking to specialise, digitalise, improve their international position, or for more affordable pavilions and offices. We have resources to face any challenge and a global vision that leads the way. Here you have expert help and the guarantee that we will turn your company around."

General areas of intervention

- Entrepreneurship
- Innovation
- Digitalization
- Cyber security
- Cluster policy
- Infrastructures
- Internationalization
- Basque industry
- R&D
- Funding

Specific support programs for SMEs in the following areas:

- Technology R&D
- Innovation
- Digital Transformation (AI, ultra-fast boardband for business, entrepreneurial 5G, Industry 4.0, cyber security, etc.)
- Entrepreneurship
- Industrial Development
- Internationalization
- Energy transition
- Rural areas, primary sector, food, bioeconomy
- Funding

The case of the **Confederation of British Industry (CBI)** of the United Kingdom is different in its scope and approach. This private organization, that claims to represent 190.000 businesses of all sizes, stresses its dialogue with government on issues regarding a better business environment, and offers services to its members.

Organization/ Country

Confederation of British Industry (CBI), United Kingdom

Public/ private

EBMO (Private employer organization)

Mission focus

- **Campaigning** (Using the power of a united voice)
- **Collaborating** (Bringing business and government together)
- **Sharing** (Bringing together business leaders enabling them to think big, share best practice and challenge the status quo)
- **Empowering** (Empowering business with intelligence to make informed decisions and to lay the foundations for success)

Areas of action and/or of non-financial services for firms (SMEs)

- People and skills
- Infrastructure and energy
- Innovation and digital
- Tax and regulations
- International trade
- Regional growth
- Brexit & EU negotiations

Examples of action guidelines

- Business intelligence to make informed decisions
- Inspiration, ideas and thought leadership
- Connections, networks, and access
- Experts to help your business campaign successfully

CBI helps create the conditions that enable businesses to devise new ideas and invest in R&D, and gives a voice to business on international issues, crucial in post-Brexit

The **National Business Association of Colombia (ANDI)** is a private non-profit Business Organization with more than 1.200 members that represents around 50% of Colombia's GDP. As representative of the private sector's interests, ANDI assumes the representation of its members, including SMEs, before national and international institutions, dealing with economic, legal, social, environmental, and business issues.

Organization/ Country

National Business Association of Colombia (ANDI), Colombia

Public/ private

EBMO (Private employer organization)

Mission focus

Andi Strategy 2025 is oriented to promote economic, social, and environmental development of Colombia, within a participatory democracy, strengthening free enterprise and business competitiveness.

ANDI will actively lead, from the business sector, the economic reactivation of the country, with proposals that generate quality employment and accelerate growth

Areas of action and/or of non-financial services for firms (SMEs)

- Innovation and Entrepreneurship
- Economic Development and Competitiveness
- Digital Transformation
- International Affairs

Examples of action guidelines

- Innovation Management
- Accelerate Innovation Portfolio
- Innovation Financing
- Perform analysis and surveys
- Generate public policies proposals
- Promote digital improve members´ productivity
- International agreements
- Promote good business practices

The **Singapore National Employers Federation (SNEF)** is the national Employers Organization, representing the interests of all sectors of the economy with more than 3.400 members (80% SME). It is an independent, autonomous non-profit organization funded by membership fees and revenue from consultancy, training, research and other activities. Its mission is to advance tripartism and enhance labour market flexibility to enable employers to implement responsible employment practices.

Organization/ Country

Singapore National Employers Federation (SNEF), Singapore

Public/ private

EBMO (Private employer organization)

Mission focus

To advance tripartism and enhance labour market flexibility to enable employers to implement responsible employment practices.

- Areas of action and/or of non-financial services for firms (SMEs)
- Represent the key interests of employers in national tripartite committees, forums and national-level reviews
- Provide expert consultancy and advice to corporate members by experienced consultants on the proper application of local labour laws, policies and tripartite guidelines
- Update corporate members on the latest important developments in labour, manpower and employment issues through briefings, industrial group meetings and other platforms
- Enable employers to develop sustainable and competitive workforces through training programmes, organised by our Training Institute, and productivity programmes
- Facilitate employers' efforts to build an inclusive workforce and progressive workplaces through programmes focusing on Workplace Health, WorkPro, Fair Employment and Work-Life Balance
- Provide leading-edge and timely research and information on local HR and employment trends e.g. on local salary trends, to enable corporate members to maintain their competitiveness

The **Federation of Egyptian Industries (FEI)** is formed by 19 industrial chambers, representing over 102,000 industrial enterprises. FEI defends and supports Egyptian industries, advocates the common interests of its members, including SMEs, and defends their positions towards governmental and legislative bodies, as well as other local and international associations.

Organization/ Country

Federation of Egyptian Industries, Egypt

Public/ private

EBMO (Private employer organization)

Mission focus

Create a strong and stable industrial society that is globally competitive being the main catalyst for development and prosperity in Egypt.

Areas of action and/or of non-financial services for firms (SMEs)

- Economic Studies & Research
- Technical Consultations & Labour Training
- Assist senior management set plans & business development
- International Trade Point

FEI's committee on SMEs that:

- Highlight FEI's vision of the current situation and future perspective for SME industries
- Study the scope of services including available financing services to SMEs and projects implemented through international entities
- Stimulate the relationship between FEI and the Social Fund for Development [SFD], reviewing available programs initiated by SFD to assist SMEs to direct some of these programs to the industrial SMEs

These illustrative cases show how some different organizations, public and private, form a diversity of regions and countries that face the challenge of promoting SMEs' higher productivity and better performance. As can be seen, each case presents specific features. It seems that when the public sector intervenes, it is possible to organize a more holistic approach to face SMEs' problems and challenges from a diversity of perspectives.

However, even in the cases where public agencies have a leading role, one way or the other private organizations participate at some point. This public/ private partnership seems to be a necessary and important feature to be successful. Another key aspect is networking, either between organizations or among SMEs. Last, but not least, the specific ways to organize non-financial support services to foster SMEs' productivity and performance are idiosyncratic and should be 'tailor made' considering the characteristics of each sector, region or country.

Conclusions and recommendations

5

The first objective of this study is to identify key internal and external factors that contribute to SMEs´ success. To this end, an extensive literature review was conducted. Once those success factors were identified, the study addresses the main challenges SMEs face concerning global business trends and emerging risks and structural changes accelerated by the COVID-19 pandemic. An indirect objective of the study is to identify criteria or guidelines for potential services that EBMOs could create or promote to support SMEs and issues for a policy agenda to promote sustainable enterprise development and nurture EBMOs' dialog with government agencies and other organizations. As it is mentioned at the beginning of this document, this is an area where there are major challenges and which will certainly require further research.

The next diagram illustrates the general systemic approach followed in the study. There is a large strand of literature that classifies the factors associated with firm-level performance into three main groups: individual (associated to the entrepreneur), organizational (the firm and its own strategies and characteristics), and environmental (the industrial and regional/national environment in which firms develop their activity).

The individual level includes factors such as entrepreneurial culture, personality traits, knowledge and experience of the entrepreneurs and their growth aspirations. These are part of the global institutional framework of a region or nation and subject to short and long-term changes.

The organizational or firm level factors include a vast array of issues that are important to improve performance. In this case, based upon the empirical literature and considering the business trends in course, four were considered crucial aspects: strategy and management practices, innovation, digitalization, and internationalization, when applicable, and more related to the concept of internationalizing the company's activities than to simply exporting.

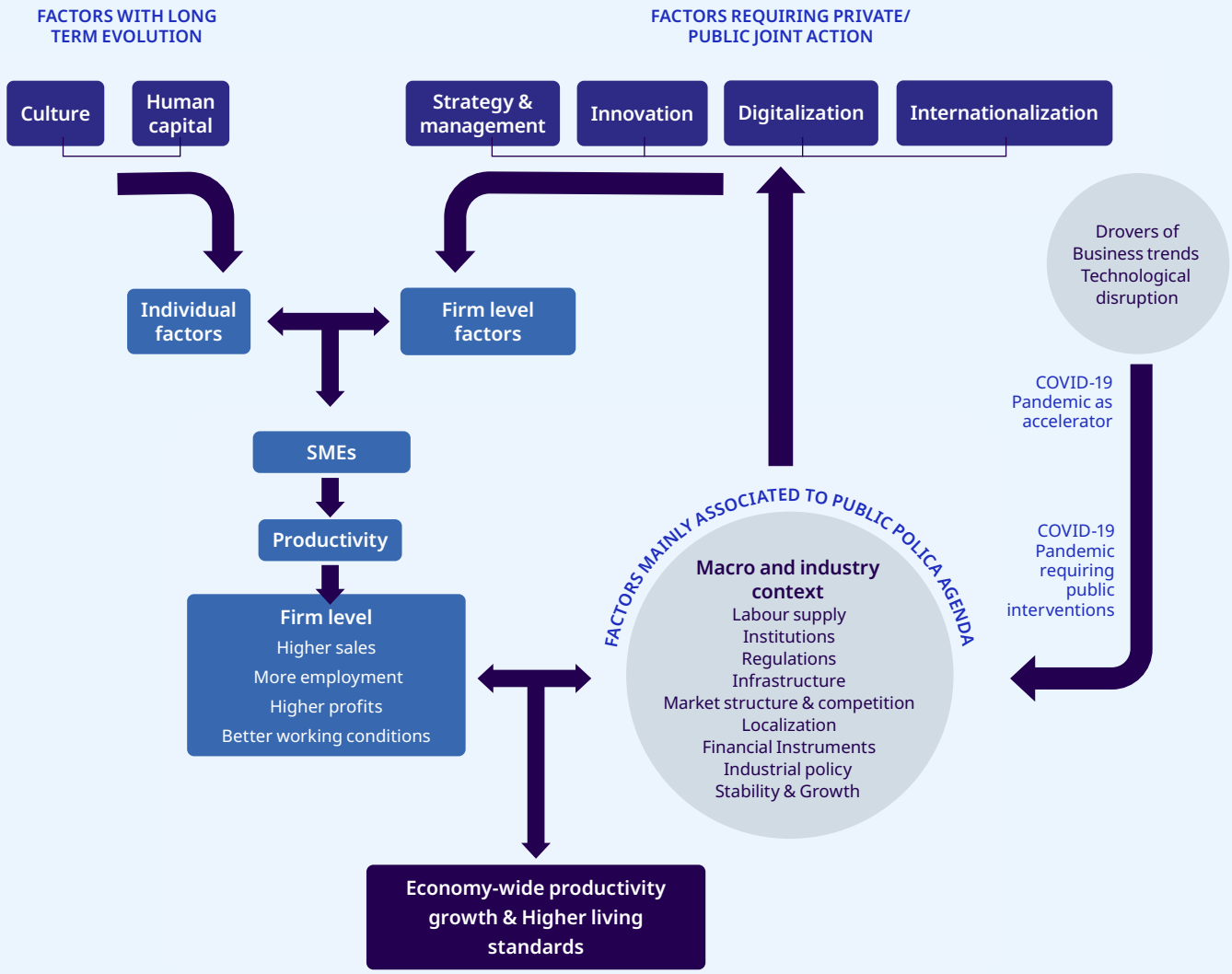
All these individual and organizational level factors are immersed in global and business trends that pose an important challenge to firms' (in this case SMEs', but not only) strategy and management decision making. These trends, and especially the fast and far-reaching technological change, have been accelerated by the need to respond to the COVID-19 pandemic crisis, putting extra pressure on SME management.

The decisions and actions by SMEs regarding these four organizational factors, responding to the fast-changing trends, will be crucial for their success. Private organizations, mainly EBMOs, and public agencies should work hand in hand to foster the recovery of SMEs after the COVID-19 crisis and their best possible adaptation to the 'new normal' reality. A systemic view and private/public partnerships are required features for a successful approach, which in each specific case should be adapted to the political, institutional, and economic conditions of regions or nations.

Notwithstanding the importance of the individual and firm level factors, the SMEs´ performance depends also on the economic conditions in which their business develops. Given the systemic nature of the business activity, these economic conditions influence the way SMEs manage the key organizational factors. At the same time, these economic conditions suffer the influence of the current macro and business trends in course.

SMEs managing their firm level factors immersed in a complex economic, social, and technological environment, need to reach adequate levels of productivity to achieve higher sales, employment, and profits. This way, they can generate better working conditions, which, in turn, favour increasing productivity, and better salaries.

This firm level performance that depends not only on the individual and organizational factors, but also on the economic conditions in which the business develops, may have an economy-wide impact on productivity and income levels if the individual businesses are embedded in a favourable macro and industry context. It works as a virtuous feedback loop.



The analysis of the situation from a systemic approach offers a comprehensive view of the main factors of success and their interaction. One of the main consequences that follows is that the support actions for SMEs should be built into a global strategy including individual, organizational, and environmental factors, considering the macro and business trends faced by the SMEs (new and established ventures).

If this is the case, the different agencies, public authorities, and actors involved in SME promotion, should work in a flexible network. EBMOs, other private organizations (including those SME specific associations), public agencies, policymakers, universities, and research centres, incubators and accelerators, and even big companies that usually structure complex supply chains, may be

important players in a comprehensive approach to SME promotion.

This kind of ***systemic and networked approach*** requires a specific conformation in each specific region or country, because of the different local conditions such as culture, politic organization, institutions, governance practices, private sector strengths, academic and business relations. Some countries have a long tradition and strong institutional base promoting SMEs from a systemic approach (e.g., Germany and its Mittelstand), others perhaps have strong support organizations in some specific areas (e.g., countries with innovation promotion agencies).

Some countries have strong sectorial and general private sector organizations. In some countries the academic institutions are used to working close to businesses, but this is not a general rule. Some countries have comprehensive competitive strategies or productive development policies, but this is not a general case throughout countries and regions; yet they share common criteria and guidelines, and use different tailor made EBMOs' strategies to boost SMEs.

In most of the developing world, EBMOs tend to be focused on advocating for the legitimate interests of their members. This is not surprising, considering that the business environment varies by country and tends to have inefficiencies that hinder business performance. But they have also been creating support services for business development, especially in areas related to training or trade. Some have gone further and are now also providing advice on issues such as corporate social responsibility, environmentally responsible production, quality culture, dissemination of knowledge and information with a certain degree of processing, etc.

These services, while necessary, tend to make a limited contribution to business growth and development. They are part of a set of services that assume that both the entrepreneur and the structure of the company are adequate to compete and become sustainable in the market. However, this is seldom the real case. Otherwise, results would be different and there would be a growing number of enterprises getting affiliated to EBMOs that would not be confronted with challenges to survive, reach a minimum competitive scale and become a source of greater added value and employment.

If in 'normal times' the decision-making process of an SME should begin with a careful strategy resource based and on its capabilities, smartly fitted to the economic environment, in the current context of the pandemic crisis, rapid change and uncertainty is of the upmost importance.

The fast technological change and the uncertainty about the future that may require rethinking business models, only make strategy and strategic fit more necessary for SMEs. However, the design of an adequate strategy is useless if it is not transformed into action through efficient management practices. This should be the first step in a supporting programme designed to strengthen the dynamic capabilities of SMEs, aimed at achieving higher productivity levels and better performance. This is where EBMOs could focus to support SMEs´ development.

This strategic decisions and better management practices should lead to actions in different areas. This study has identified three specific areas that, in the current global situation and considering the macro and business trends in course, are crucial for SMEs strategies: innovation, digitalization and, when applicable, internationalization. This does not mean that other areas of business action or traditional services offered by EBMOs, and public agencies are not important, but the previous analysis shows the need to focus on those three areas to process the transformations needed to face the challenges that lie ahead.

The implementation of strategies and management processes, innovation actions, digitalization investments, retraining employees in new skills access to international markets (directly or through participation in supply chains), require at least: a) advice and non-financial support, through consultancy or business services provided by EBMOs or other organizations; and b) financial resources to pay for those services and for the investments needed to put the strategy into action.

In both cases, there are various possibilities that will depend on the characteristics of the region or country and industry. Non-financial support services may be organized based on networks including different actors such as EBMOs, sectorial

chambers, universities, public agencies, private organizations, consultancy firms or individual professionals (Kusinikova, 2020). It will depend on the relative strengths and availability of resources in each case. Funding usually requires public support, because SMEs are not able to pay the full cost of business services, and adequate financial schemes to pay for investments.

Any funding scheme for advice or investment, should require the participation of the SME assuming part of the financial burden. The funding sources will depend on the institutional and economic environment: public funds, international organizations, venture capitals, business angels, financial institutions, and capital markets. Again, solutions in each case should be 'tailor made'.

Although networking is an essential part of any successful SMEs' support program, it may or may not require a formal institutional organization. What is necessary is to articulate actions between different organizations as part of a shared comprehensive strategy. EBMOs may play this role, alone or jointly with other organizations (private, public or academics).

Regarding **innovation** activities in SMEs, a required feature of support and promotion programs should be strengthening their 'absorptive capacity'. In most cases, SMEs will not be disruptive innovators (although some may be), but they should at least be able to receive and adapt knowledge from sources such as research centres, big companies, and multinationals (taking advantage from foreign direct investment). This requires developing some R&D capacity by the SMEs to 'tinker' and adapt available technologies and products, upgrading the skills of their human capital.

This kind of support at the firm level will be successful if complemented by a favourable context for innovation, including a proactive attitude of the public sector, policies oriented to solving market and institutional failures, appropriate financial instruments to partially fund and make the necessary investments feasible. It is worth highlighting that innovative environments should be accompanied by public policies to foster science and technology. They usually generate more basic knowledge and reduce risks taken by firms in their market-oriented innovations. The same can be said for policies to promote foreign direct investments.

EBMOs can advocate for the implementation of such public policies. The more conducive the environment in which SMEs are born, especially from a technological point of view, the more likely they are to survive, and the higher their rate of innovation above sectorial average. It has also been shown that small firms which are able to produce goods with higher technological content are more likely to survive, even when competing against larger firms in the same sector, than those focused only on basic goods and services. Moreover, they can also offer services to encourage technology transfer to help SMEs improve their processes, products and services. In doing so, they can contribute to fostering the creation and consolidation of new enterprises in economic activities with higher value added.

Digitalization is a necessary SME response to current macro and business trends, which have been accelerated by the COVID-19 pandemic. This response calls for rethinking previous business models, introducing digitalization as part of a coherent strategy, and adapting management practices to the new situation (ILO, 2021b). Adapting to online selling or introducing widespread telework requires decisions that go far beyond the use of appropriate digital devices. In addition to investments in equipment, the firm's organization should be consistent with those strategic decisions while employees need to acquire the necessary skills to work in this new environment and with the new devices.

SMEs will need support to process these changes and reskill their workforce. As in the case of innovation, public intervention is important to encourage and enable SME adaptation to a digital economy. Appropriate regulation to encourage private sector investment in infrastructure and ICT services, public investment, and skills development programmes for labour reskilling and strengthening formation in software development and ICT, are possible public actions to promote the required transformation of

SMEs. In this area there are large opportunities for public/private coordination and partnership.

EBMOs can play a leading role to support and accelerate the digitalization of SMEs by providing tailor-made services. It is important to help them streamline the changes that will inexorably occur and that have been accelerated by the pandemic. They give advice on how to digitalize and modernize processes, in any functional area, including information management and data analysis, general administration and human resources, management, production and logistics processes, marketing, commercialization and all kinds of relationships with suppliers, customers and other stakeholders.

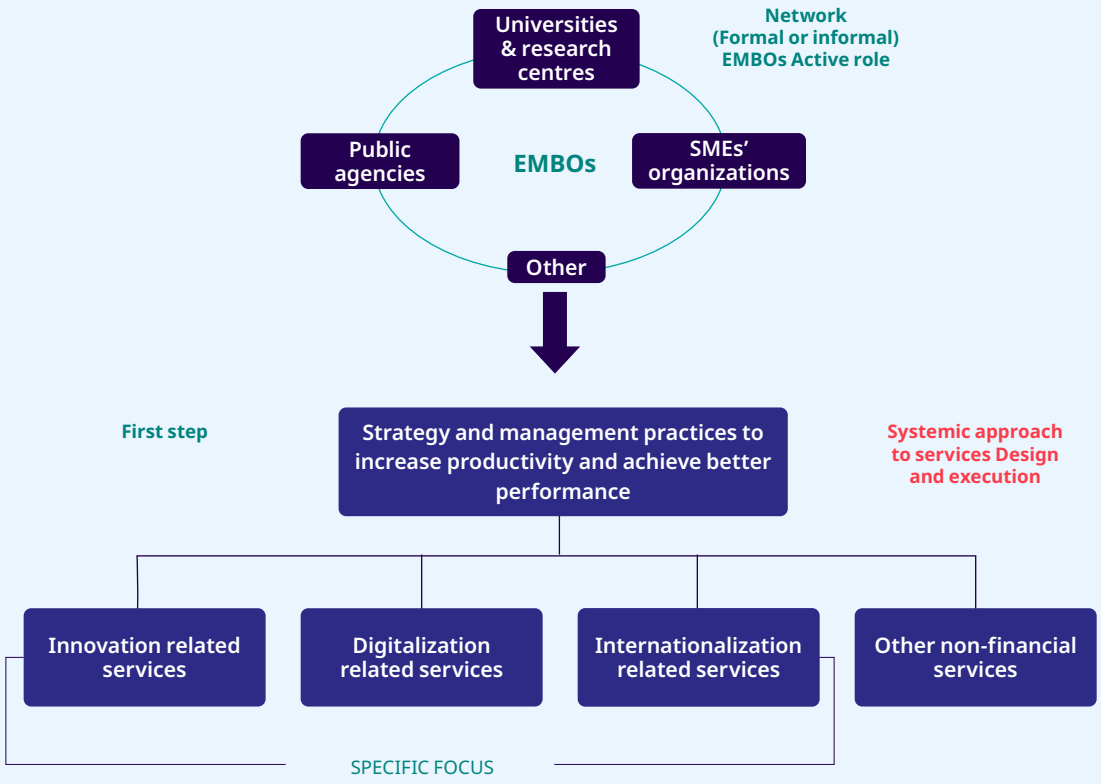
Not every SME may expand its business through internationalization. There are non-traded services whose potential market is domestic. But in the case of businesses open to foreign trade, internationalization – particularly exports- may be a necessary component of a growth strategy. There is considerable empirical evidence showing that companies that export and belong to more internationalised sectors are more likely to succeed.

SMEs with activities open to trade, may directly access new markets, or participate in supply chains with global presence, expanding their opportunities to achieve higher levels of productivity and increasing sales, employment, and profits. In an interdependent relation with their innovation and digitalization strategies, these SMEs need support in areas such as market intelligence, logistic assistance, and quality and regulatory requirements in destination markets.

This is a role EBMOs may play jointly with public agencies that promote exports and foreign investments in countries and regions. Extensive literature discusses two different -non mutually exclusive- paths relating innovation and internationalization: a) firms that through innovation and better management practices increase their productivity, increasing competitiveness to access international markets; and b) firms that through export activity, learn from requirements of the international markets and through this knowledge innovate and reach higher productivity levels, in a feedback process with their export strategy. One way or the other, innovation, productivity and exports seem to be parts of the same framework.

However, most SMEs might not be able to cope with both strategies simultaneously or in a short period (whether innovating to access export markets or transforming knowledge from exports into innovation). For SMEs, lack of financial, managerial, or human resources is a limitation difficult to surmount. One way or the other, an open economy and a favourable environment for trade and innovation is important to foster international activities of SMEs, especially in small developing countries.

These general proposals, with services to SMEs delivered through a network of institutions (formal or informal) based on a systemic approach, where EBMOs play an important role, may be illustrated in the following diagram:



Obviously, the provision of non-financial services is not the only role played by EBMOs. These business organizations play an important role in their dialogue with policy makers advocating for policy-oriented reforms, regulatory agencies, and other public institutions to foster more favourable economic and market environments for the development of SMEs. The environmental success factors are an important part of the story. However, these proposals may be a general guide helping EBMOs, together with other actors, to promote higher productivity and better performance of SMEs through firm level success factors that are crucial not only in the current 'new normal' times but also to move forward and become better in the post-COVID-19 economic recovery.

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International Labour Organization
Bureau for Employers' Activities
4 route des Morillons
1211 Geneva 22
Switzerland
www.ilo.org

ISBN: 978-92-2-035605-0