

WORLD ENTREPRENEURSHIP FORUM
2008 EDITION

ENTREPRENEURSHIP AND SME POLICY

D.J. Storey

Warwick Business School

WHY IS THIS TOPIC IMPORTANT?

- The only government in the world that has fully identified the scale of taxpayer funds devoted to “supporting” small firms and entrepreneurship is the UK.
- It calculates that each year around £8 billion is spent. This is approximately the same sum as spent on the Police and more than is spent on Universities.
- The scale of this expenditure is disguised because it is spent by a wide range of government departments, regional organisations and non government agencies –the vast majority of whom spend only modest sums and rarely identify the “end beneficiary”
- Although data are not available for other countries it is very likely that, in relative terms, their expenditure is similar to that of the UK
- The public and taxpayers in every country have a right to know whether this money is being spent effectively.
- This paper sets out the case for such expenditure and shows how the public could become better informed about the effectiveness of this expenditure.
- Specifically it sets out an Evaluation methodology that has been endorsed by OECD.

KEY POINTS

1. Entrepreneurship is viewed as an ingredient to wealth creation and social justice
2. Governments believe they have a role to play in stimulating entrepreneurship
3. Different governments pursue very different policies to promote entrepreneurship
4. Drawing upon work for OECD, together with separate work with a number of member countries, this paper argues that although there are a massive diversity of policies in operation, there is little reliable evidence about their effectiveness.
5. This is primarily because of the reluctance of government to ensure policies are carefully evaluated
6. Despite these knowledge imperfections the personal assessment of the author is that, in general, “macro” policies are more effective than “micro” policies in promoting entrepreneurship.

7. "Macro" policies include: demand management; immigration policy; competition policy; tax and benefit regimes; regulation.
8. "Micro" policies include: training, information, advice and management programmes for SME owners or potential owners; cultural change programmes such as enterprise education; access to finance programmes
9. These very broad conclusions do, of course, vary somewhat depending upon the specific circumstances of the country and the specific nature of the policy.

ISSUES TO DISCUSS

1. How can entrepreneurship policy evaluation be moved up the policy agenda?
2. Why is it that, in comparison with for example labour market programmes, the quality of evaluation of entrepreneurship programmes is so weak?
3. Is there agreement that the key influences on Entrepreneurship are "macro" factors?
4. Is there agreement that evidence of impact of "micro" policy instruments is weak?

1. Introduction

Van Praag and Versloot (2007) identify four economic benefits of entrepreneurship: job generation; innovation; productivity and growth; and the potential for entrepreneurship to increase the 'utility' of individuals by increasing, for example, their satisfaction or income. Governments, however, can exert either a positive or a negative influence on the extent to which in practice these benefits materialise. This paper examines the influence of government on entrepreneurship generally, and particularly upon small and medium sized enterprises (SMEs). Government influence is referred to as Entrepreneurship and SME Policy –or SME policy for short.

The paper begins by asking why, if enterprising individuals and firms provide these economic benefits, does government play any role? There are two “standard” answers to this question. The first is that if markets were perfect, and buyers fully informed, then there is no economic case for public policy and hence for government. However this is not the case with respect to SMEs and it is the alleged presence of “market failure” that justifies intervention. Second, it is argued that a wide range of government policies – for example - security, immigration, taxation, welfare policy, education and macro-economics – all exert either a positive or a negative influence on SMEs and entrepreneurs. As key political constituents, the owners of (small) businesses are likely to take into account the impact of government policies on their enterprise in choosing where to cast their vote. Governments therefore have to be concerned with this electorally substantial political “constituency”.

However a third, but relatively infrequently discussed, factor also influences the extent to which governments can enable SMEs and entrepreneurs to deliver the economic benefits identified by Van Praag and Versloot. This is the extent to which governments deliver their policy in a cost effective manner. The economics literature is clear that the identification of a market failure is a necessary but not a sufficient condition for government intervention. Intervention is justified only when the effect of that intervention leads to a net welfare improvement. In simple terms government intervention is more likely to be justifiable when it is cost effectively delivered.

This paper reviews Entrepreneurship and SME policies in developed (OECD) countries according to three dimensions. It begins by reviewing the justifications for the policies. It then turns to the policies and highlights the diversity of policy instruments currently in operation which seek to enhance “enterprise”. Finally it reviews the evidence on the effectiveness of such policies in facilitating the economic benefits identified by Van Praag and Versloot (2007b)

2. SME and Entrepreneurship policy: Characteristics and Choices in OECD countries.

This section begins with a review of the market failure-based rationale for SME and entrepreneurship policies. It then moves on to provide a review of the menu of policy choices open to policy makers in this area. Finally it sets out current best practice in this area as articulated by OECD (2007a, 2007b).

2.1: The concept of Market Failure

We noted above that public policies to promote SMEs are normally justified on grounds of market failure¹. By this we mean that taxpayer’s funds are used to provide welfare-improving services that would not otherwise be provided, or be inadequately provided, by private organisations. A necessary, but not sufficient, condition for government intervention is evidence of market failure, four forms of which are relevant to SME policy: The first three relate to imperfect information, and the fourth reflects a divergence between social and private returns:

1. Individuals do not realise (are ignorant of) the private benefits of starting a business. This is frequently used to justify ‘entrepreneurship policies’ such as the raising of enterprise awareness amongst young people.
2. Owners of small firms do not fully appreciate the private benefits to their business of taking certain courses of action. This information imperfection is

¹ For a review see Storey (2003)

used to justify public subsidies to promote SMEs to undertake workforce or management training or obtaining external advice from specialists or consultants or used to fund visits by SMEs to overseas trade fairs.

3. Financial institutions are unable to accurately assess the risk of lending to small firms so denying some (good) small firms access to funds and constraining their growth. To respond to this problem governments in many countries have introduced Loan Guarantee Schemes in which the state agrees to reimburse defaults on bank loans made to SMEs with viable business plans but lacking the collateral that banks would expect to be available if they were making fully commercial loans.
4. Finally, a range of SME policies reflect the divergence between private and social benefits. The best examples relate to policies to promote innovation in small firms. Here it is argued that, without subsidies, there would be a socially sub-optimal formation and growth of technology-based firms. The potential presence of positive externalities is used to justify policies to promote Science Parks or public funding of seed equity programmes focussed on technology-based small firms

Public policy to support SMEs is then justified on the grounds that the market fails on one or more of the four grounds identified above. Policy interventions therefore seek to rectify this market failure.

The presence of market failure is, however, a necessary but not a sufficient condition for government intervention. Alternatively expressed, a market failure may be identified but this does not automatically imply that governments are expected to address the failure. So, whilst a market failure may be identified, different views may be taken about whether government intervention would lead to an improvement. The concept of market failure therefore offers little guidance on the appropriate scale of any intervention.

The “market failure test” therefore requires intervention to address and overcome one or more of the above four “failures”. Publicly funded programmes to address market failures can have a temporary life for two reasons. First, the market failure is temporary because it is addressed in full by the programme. An example is a programme aimed at demonstrating to SME owners the benefits of workforce or management training. If such

benefits become clear to SME owners as a result of undergoing the training then they would be expected to fund such training themselves. The information imperfection is overcome and the programme has a temporary life. Second, over time, the market may become better informed, for reasons unrelated to the programme. An example might be a government-backed loan guarantee programme. Here the programme might be justified at one point in time when, as with Market Failure 3 above, financial institutions were unable to accurately assess risk. However, perhaps as a result of expertise acquired by participating in the programme, or because of greater competition in the finance market-place, or because of improvements in the processing and analysing information on their customers, financial institutions may improve their ability to accurately assess lending risk. Hence an effective and market-failure addressing programme at one point in time may become less justified when circumstances change.

2.2 Key Policy Choices

Those responsible for formulating Entrepreneurship and SME policy are faced with a number of choices. This section examines two key policy choices and demonstrates that the choices made by policy makers often differ radically between OECD countries.

The first choice is over the emphasis placed on Entrepreneurship, as opposed to SME, Policy. A second choice is whether to focus on lowering “barriers” or “offering support”. The nature of these choices and the decisions reached in OECD countries is discussed in turn.

We noted earlier the important distinction between SME and Entrepreneurship policy in which the former applies to existing enterprises whereas the latter relates to policies seeking to enhance the creation of such enterprises². The distinction is shown in Table 1 which takes examples or elements of both.

Table 1: Features of SME and Entrepreneurship Policy

² For a recent review see .Audretsch, et al. (2007).

SME POLICY	ENTREPRENEURSHIP POLICY
Reducing red-tape and paperwork burden	Reducing red-tape and paperwork burden
Access to capital/financing	Access to micro loans and seed funds
Provision of information services	Provision of information about start-up
Export and marketing services	Highlighting entrepreneurs as role models
Provision of training and consultancy	Entrepreneurship education
Technology transfer	Facilitating networking services

Source: Lundstrom and Stevenson (2005)

Despite seeking to draw a distinction between SME and Entrepreneurship policies there are several elements that appear to be common to both policies. For example, both SME policy and Entrepreneurship policy is concerned to minimise bureaucratic and paper-work “burdens”. However a distinction between the policies remains valid because the precise nature of these “burdens” does vary sharply between start-ups and established businesses. For example, the relevant measure of “bureaucratic burdens” for an individual considering starting a business may be the length of time this takes, the number of procedures required and the costs of completing these procedures. In contrast, the bureaucratic burdens upon an existing SME will include the cost of complying with, for example, health and safety or workforce legislation.

What is now clearly documented is that the scale of “burdens” on both those considering starting a new business and those operating existing businesses does vary widely from one country to another. The World Bank 2006 “**Ease of Doing Business Survey**” reports that to start a “standard business” in Mexico City requires 9 procedures, requires 58 days and requires costs which are the equivalent of 16% of income per capita. This contrasts with, for example, Canada where 2 procedures are required to start the “standard business”, taking 3 days and at a cost of less than 1% of income per capita.

The World Bank 2006 also documents bureaucratic burdens for established firms. One illustrative “burden” is the cost of firing workers. Here a “standard” worker and “standard” firm are compared according to eight indicators such as whether either a Union or the Labour Ministry has to be informed prior to firing workers or whether training has to be provided prior to dismissal. Based on these eight indicators a country score is generated. Again there are wide variations between countries with hiring and firing being easiest in countries such as US, UK and Denmark and most difficult in for example Portugal, Greece and Spain..

The differences between two developed countries- France and the United States- are clearly shown in Table 2 below. Using data from ***Ease of Doing Business Survey 2006*** the final row of the table shows that, whilst overall the United States is the third “easiest” place in the world to do business, France is in forty fourth place. Second it shows that this difference primarily reflects the greater rigidities in employing labour in France, where France has scores of 80 and 66, compares with US scores of zero and 3.

Finally the numbers in parenthesis reflect the position of the two countries in 2000 according to the number of procedures and time taken to start a “standard” business. This shows that France has changed radically during the last six years. In 2000 it took 53 days to start a business in France and now it takes six, bringing it much closer to the US. French policy makers have therefore seen this as a crucial area for policy change.

Table 2: Ease of Doing Business: France and USA

	France	USA
Number of procedures	7 (15)	5 (4)
Time in days	8 (53)	5 (4)
Cost (% of income per capita)	1.2	0.5
Rigidity of Hours Index	80	0

Rigidity of employment Index	66	3
OVERALL	44	3

NOTES: 1999 position in parenthesis

Sources: 1999 position taken from Djankov et al 2002; 2006 positions taken from World Bank (2006)

A second key policy choice is the extent to which governments emphasise policies that focus upon providing direct assistance, compared with those that focus upon seeking to lower the 'burdens' or impediments to business creation or to small firm expansion. Dennis (2005) shows this choice as a 2x2 matrix which makes a distinction between the provision of assistance and the lowering of impediments. This is reproduced as Figure 1.

It shows policy makers have four options. Most EU countries have, by OECD standards, comparatively high what Dennis calls impediments³ to starting a business, as illustrated by the World Bank 2006 survey. On the other hand EU countries also commit considerable sums of public money to assisting SMEs, which Dennis regards as seeking to compensate for the impediments. For this reason, this box is labelled 'compensating'. These countries also seem to place relatively more emphasis on SME rather than Entrepreneurship policy. The EU countries are therefore concentrated in the bottom left area of Figure 1.

Figure 1: A Typology of Public Policy toward Small Business

³ The term 'impediments' is used as it is the one used by Dennis (2005). However the term clearly has negative connotations, implying perhaps that individuals are prevented from starting a business without good reason. Governments in countries that have high 'impediments', however, justify these policies on the grounds that this provides protection for the consumer. For example all countries impose 'impediments' preventing the unqualified establishing a business as a doctor or surgeon, whereas only some countries have similar restrictions on those wishing to start a business as an electrician or a driving instructor. The justification for 'impediments' to entry into the medical profession is presumably based on potential damage to the consumer's life. However errors or incompetence on the part of the electrician or the driving instructor can also clearly endanger human life, yet the extent to which these individuals are 'impeded' from starting a business varies considerably from one country to another, depending upon the extent to which emphasis is placed on the desire to protect the consumer.

Low Direct assistance	LIMITING [Developing Countries]	COMPETING [USA]
	COMPENSATING [EU]	NURTURING [US Minority]
High Direct assistance	High Impediments	Low Impediments

Source: Dennis (2005)

A very different approach is adopted in the USA. Here the direct assistance is argued to be low⁴ but so, as we have seen, are the barriers to starting and operating a business. Competition enhancement is seen as the focus of US small business policy and so this box is labelled ‘competing’ and it is shown in the upper right box of Figure 1.

The US however, does have some exceptions to this - its programmes to promote the interests of technology-based firms, and in the promotion of minorities. Here again the barriers are low but there is a high level of direct assistance provided. This is shown in the box labelled ‘nurturing’. OECD countries which could also be viewed as reflecting this policy choice could include Canada and perhaps New Zealand. This is shown in the lower right box.

Finally there are many countries where the barriers to starting a business are high by international standards, but where public assistance is low. This is referred to as Limiting and is very characteristic of less developed countries. It is shown as the top left box.

Clearly then there is diversity in policy approaches and philosophy in Entrepreneurship and SME policy. Given that all governments are seeking to achieve the economic and

⁴ Data are difficult to obtain on this topic for the US. Our current “best guess” is that on a per capita basis enterprise policy spend is about 17,000 USDs annually in the UK and 10,000 USDs in the United States [Greene and Storey (2008)]. Whilst it makes the point that the US expenditure is much less than the UK, it calls into question whether the US can be considered as a “low” direct assistance economy.

social gains identified by van Praag and Versloot (2007b) such a diversity of approaches may appear curious.

2.3 Policy Delivery

Policy effectiveness, however, is determined not only by the policy choices discussed above but also by policy delivery. It is to this latter issue that we now turn.

There are several grounds for favouring simplicity and consistency in SME policy delivery. The first is that SMEs are of a simple organisational form, at least in comparison with larger enterprises. Hence SME policy instruments should not be complex if they are to be understood and implemented by smaller firms. The second is that SME owners, since they have a business to run, regard themselves as having little time with which to engage with government. They do not have the resources, unlike many large enterprises, to employ specialist individuals for this purpose, so policies that are subject to frequent change are likely to be ignored by SME owners. A third reason is that, in general, the owner of an SME considers him or herself to be of a practical disposition focussed upon customers rather than governments. For all these reasons it might be expected that SME policy would be simple, easily understandable and cost effectively delivered.

The evidence from OECD countries suggests that, if anything, the reverse is the case. SME policy is remarkably complex, delivered in a variety of very different ways for not very obvious reasons and subject to considerable changes over short periods of time. It seems reasonable to ask why this is the case. Several explanations have been proposed.

The first is that, although SMEs are simple in organisational form, they are both numerous and diverse. There is no "typical SME". Diversity occurs because of sectoral differences, because of regional differences, because a very young firm faces different challenges from that of a long established firm that may be no larger. A fast growing firm has different challenges from that of a slow grower. The failing firm differs from one with strong financial underpinnings. And, it is this diversity that presents challenges to the policy makers since there is a tendency for policies to be developed for each "group".

Frequently this means a myriad of policies co-exist, supposedly tailored to meet the needs of each group,

A second explanation is that many departments of government see SMEs as “their responsibility”, by which it is meant that they feel the need to formulate policies to assist them. The Education department sees enterprise education and perhaps innovation as their responsibility; the devolved governments claim to understand what “their” SMEs want better than central government; the Finance ministry recognises that the taxation regime is a key influence upon business creation, survival and growth. The Employment Ministry sees itself as having responsibility for skills and training whether these are delivered by large or small firms but, in most countries, it is the large firm “agenda” that dominates.

The effect of these influences is that a bewildering array of policies exists in many countries, the effect of which is frequently to have the reverse effect that is desired. Because each policy is “tailored” to specific groups of SMEs the eligibility criteria have to be tightly specified. The effect of this is to exclude businesses, for what the business owner regards as purely bureaucratic reasons. This, in turn, leads to resentment on the part of owners who very quickly communicate that sentiment to other business owners. So, whilst policy makers seek to increase the willingness of SME owners to participate in public programmes their often well-meaning efforts to “tailor” policies generally has the opposite effect.

All countries with SME policies face this problem of delivery, but respond to it in very different ways. For example SME advisory services in Sweden are provided by public servants in a publicly owned organisation, ALMI . To give it its full name, ALMI Företagspartner AB, is owned by the state and is the parent company of a group of 21 subsidiaries, which are 51 per cent owned by the parent company. Other owners are county councils, regional authorities and municipal cooperative bodies.

The disadvantages of having small business advisory services provided by public servants are twofold. The first is that the credibility of these services with the SME customers may be lower if advice is provided by public servants on the grounds that such individuals may be less well informed than consultants who are themselves in

business. The second is that the provision of state- funded and delivered advice “crowds out” private suppliers who, in the absence of the state subsidy, would be more suitable suppliers. Nevertheless it is the case that, despite these theoretical disadvantages, the services provided by ALMI are well regarded by Swedish smaller firms.

The Swedish example makes it clear that successful SME policies can be delivered in a variety of ways, by organisations having widely differing governance structures. It highlights the importance of judging policy not on ideological grounds but on grounds of demonstrable effectiveness. A framework for reaching that judgement is now set out.

2.4: The COTE Framework:

One of the ten background reports prepared for the 2nd OECD Conference of Ministers for Small and Medium Sized Enterprises , Istanbul ,Turkey June 2004 set out the COTE Framework.

- In COTE the letter “C” stands for both policy clarity and policy coherence. “Clarity” in this context means that the policy is fully understood by those delivering it and those expected to benefit from it. “Coherence” refers to the need for all parts of government to work together in the interests of delivering a unified and mutually reinforcing SME policy, even when these are delivered by different departments or agencies. SME policies are unlikely to be coherent when they are delivered by many organisations without the requirement to justify its expenditure alongside that of other organisations seeking to deliver services to SMEs.
- “O” refers to the specification of “Objectives” of policy. Examples of such objectives could be the creation of new firms, the growth of existing firms, or promoting enterprise amongst target groups in the population.
- “T” refers to the specification of measurable “targets” that reflect these objectives. Hence, if the objective were to create more new firms, then an example of a target would be “to increase the number of new firms by X% by 2010”.

- “E” refers to “Evaluation”. Policy can only be considered to be effective if it passes the challenges of high level evaluation, but Evaluation can only be undertaken when clear policy targets exist.

Applying the COTE Framework would mean that all SME and Entrepreneurship policies and programmes would have clear objectives and targets. An objective is a statement of the expected impact of the policy. For example, an objective of an incubation programme might be to increase the number of new businesses started in specified areas of technology. A target converts that objective into a specified number. An example would be that the target is to provide incubation facilities for 100 or 500 new businesses per year.

A second important distinction is between input-based and output-based targets. SME Training programmes provide examples of each. An example of an input-based target is: “we will provide X hours of training for Y SMEs”. In contrast, an output-based target is “The Y SMEs for which training is provided will show Z% increase in sales in the following year”. Output based targets are much preferred to input based targets on the grounds that they focus the attention of the policy deliverer on changing the performance of the SME rather than simply delivering the service. They are however much less frequently used, perhaps because policy makers do not wish to be held responsible for decisions made by SME owners over which they have no influence.

2.5: The key role of Evaluation⁵

Evaluation refers to a process that seeks to determine as systematically and objectively as possible the relevance, efficiency and effect of an activity in terms of its objectives, including the analysis, implementation and administrative management of such activity’

This definition emphasises that Evaluation has an integral role to play in the policy *process*. Evaluation cannot be left ‘at the end of the line’ to be undertaken once policy has been in operation for many years. To do so would be to consign it to the role of economic history. Instead, it has to be a key element of initial policy formulation. When policy is being formulated objectives and targets have to be specified in such a form as

⁵ This section draws heavily upon OECD (2007b)

to make them amenable to evaluation. This provides the clarity of thought which underlies all successful policy.

It also means that all organisations and individuals responsible for policy delivery have to be aware that evaluation is to take place. Once the evaluation has been undertaken, and sometimes as it is taking place, it should be used as the basis for dialogue with policy makers, with the objective of delivering better policy. The outcome of the evaluation can then become an input into a debate on the appropriate ways for governments and SMEs to interact.

There are several reasons for undertaking evaluations. The most important is that substantial sums of tax payers' money are used for administering and delivering SME and Entrepreneurship policy⁶. So, given the sums involved, governments have a responsibility to the tax-payer to demonstrate that the monies are spent in a manner likely to achieve the aims of the policy. Part of this role is normally played by public auditors whose task is to ensure expenditure is incurred where the legislators intended. A very different role is played by evaluators. Their task is to assess whether the tax payer obtained value for money from the policy. In short, did the policy work and what lessons can be learnt for improvement? Evaluations are most effective when their results enter the public domain. This emphasises not only the importance of undertaking evaluations, but also that their findings are disseminated. Evaluation therefore provides the informed basis for debate on policy impact.

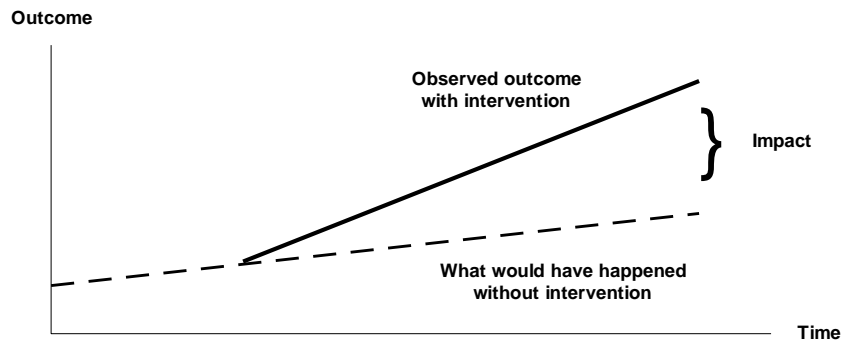
Evaluation uses a number of criteria⁷, but at its core is the concept of Additionality. This is defined as the true impact of the scheme/programme. Whilst it is not always easy to quantify, it is likely to be reflected in a measure such as additional output, employment, sales or export activity that can attributed to the existence of the programme. In other words it is activity that would not have taken place without the programme, and is attributable to the firm participating in the programme. This is shown diagrammatically in Figure 2 below taken from Oldsman (2002).

⁶ Greene and Storey (2008) point to UK government estimates that policy costs are approximately £8 billion

⁷ These and The OECD SME Working Party identified seven headings under which policies can be assessed. are: Rationale, Additionality, Appropriateness, Superiority, Systemic Efficiency, Own Efficiency and Adaptive Efficiency [OECD, 2000].

It shows, for any given outcome, that policy impact can be considered as the difference between the observed outcome with the intervention, and what would have happened without the intervention. The Figure shows these two outcomes diverging after the time when the policy is implemented.

Figure 2: The Impact of an Intervention



Source: Oldsman (2002)

Whilst this is, in principle, a simple concept, identification of the programme impact ‘as systematically and objectively as possible’ can be challenging. This is because programme impact cannot be easily observed for a number of reasons. The first is that it is not always clear what changes might have occurred in the firms as a result of participation; in other words the Outcome measures are unclear. Some programmes might be expected to lead to a greater likelihood of firm formation or survival, others to growth in sales, profits or employment, others to a greater likelihood of innovating or selling into overseas markets. Other programmes might be expected to enhance all these characteristics and in other cases it is unclear what firm characteristics are expected to show improvement. Evaluation therefore requires a decision on appropriate Outcome measures.

A second problem is that participation in the programme may precede any improvement in firm performance. Using the example of Figure 2, the point at which the lines diverge will not necessarily be immediately after the programme is delivered. Some programmes

will have their impact possibly years before others. For example, a programme in which SMEs are subsidised to participate in an international Trade Fair so as to encourage them to internationalise⁸, might be expected to have an impact upon sales within months. In contrast, a programme to fund Research and Development in SMEs would be expected to have little impact for several years. A programme to develop enterprise education might have no impact for two decades.

A third problem is the myriad of influences upon the performance of an SME, other than that of programme participation. These include the skill of the owner, the sector and location of the business, macro-economic conditions and the role of chance. In principle, only when account is fully taken of these 'exogenous' factors can the impact of the programme be estimated.

One helpful way of categorising evaluation frameworks in the SME and Entrepreneurship policy area is the 'Six Steps to Heaven' framework'. This is shown in Table 2 below, and has previously been used for reviewing SME Policy in Mexico⁹. The Mexican programmes that have been evaluated are shown in the right hand column of the Table. Note there are no examples of Step VI evaluations having been undertaken.

The 'Six Steps' procedure recognises that there is a gradation of sophistication in assessment procedures. The six steps show this gradation, with Step I being the least sophisticated procedure and Step VI being the most sophisticated. Here sophistication is intended to reflect the confidence the policy maker can have in being able to attribute changes in businesses supported under the programme - often called the 'treatment group' - to participation in the programme. Alternatively expressed, it may be considered as the confidence the policy maker has that all other influences are held constant.

⁸ 'Access to International Markets', a presentation by the Delegation of Greece, OECD Working Party on Small and Medium-Sized Enterprises, Athens, 26-28 April 1998

⁹ Tan and Lopez-Acevedo (2007). It derives originally from Storey (1999).

Table 2: Six Steps to Heaven: Methods for Assessing the Impact of SME Policy

Step	Action	Example
Monitoring		
Step I	Take up of Programme	PAIDEC 2000
Step II	Recipients opinions	PAT 2000
Step III	Recipients views of the impact of Programme	COMPITE 2003
Evaluation		
Step IV	Comparison of Assisted Firms with “typical” firms	
Step V	Comparison with Matched firms	CIMO 2002
Step VI	Selection bias taken into account	

Table 2 also shows that a distinction is made between Monitoring and Evaluation. The difference between Monitoring and Evaluation is that the former relies exclusively upon the views of the recipients of the policy. Evaluation however seeks, by some means, to contrast these views or actions with those of non-recipients in order to present the “counter factual”. The difference between actual changes and the “counter factual” is viewed as the impact of the policy – or its ‘additionality’. In terms of Figure 2 Monitoring is the continuous line, and it is only the inclusion of the control group that enables the dotted line to be identified and hence the correct impact of policy to be evaluated. Steps I to III are therefore not considered as Evaluation, but instead are referred to as Monitoring.

A full review of Steps I to IV are provided in Tan and Lopez-Acevedo (2007), but for current purposes it is sufficient to note that, despite the frequency with which Steps I to III are used, these approaches either do not attempt to make a comparison with a ‘control group’, or do so in a clearly inadequate manner. It is not until Step V that an attempt is made to compare ‘treatment’ with ‘non-treatment’ firms, where the latter do not differ in terms of observable factors such as ownership, size, sector and geography. This is normally undertaken through a matching process. Once the matching is complete

then differences in the performance of the two groups is attributed to participation in the programme.

Whilst the Step V approach reflects a real attempt to address the issue of the counter-factual, it cannot now be considered as 'best practice'. This is because the results are ambiguous because observed differences in the performance of treated and non-treated firms may reflect the presence of 'un-observables'- and cannot therefore be exclusively attributed to the policy. The most obvious 'un-observable' is the dynamism or motivation of the SME owner, with this leading to various forms of selection bias in the estimation techniques.

Two examples of selection bias are self- selection and committee selection. Self selection bias may occur where, for example, programmes seek to provide support for rapidly growing businesses. Here those businesses where the owners are seeking growth may be more likely to apply to become participants in the programme than those with only modest or with no growth ambitions. The problem arises where this is only partly reflected in 'observable' factors, since the latter under-estimate how the firm would have performed even if the programme had not existed. The 'counter-factual' dotted line in Figure 2 is specified too low, and the programme impact is consequently over estimated. One clear example of this is where applicant firms, although apparently no different from non-applicant firms in terms of the "controls"¹⁰, in fact have more motivated owners¹¹. These differences in owner motivation- which is very difficult to observe- mean these firms would be expected to perform better than the 'matches', even if there had been no programme. It is therefore unreasonable to attribute all differences in performance between the programme firms and the matches to programme participation. Failure to take account of selection, however, leads to precisely this error.

A second example is committee selection. This refers to programmes where only a proportion of applicants are successful. Here a committee or similar group makes a judgement, with the 'better' firms/applicants obtaining the funding. If the committee is effective it will eliminate those firms likely to perform poorly, so that the programme participants are clearly non-randomly drawn from applicants. As before, even if the

¹⁰ Here typical 'controls' might be business sector, location, age and ownership.

¹¹ This is because the focus of assistance programmes is clear in the way in which they are promoted. Thus programmes seeking to attract growing businesses are unlikely to have as high a proportion of 'life-stylers' as in the SME population as a whole.

programme did not exist, the selected firms would be expected to have outperformed the other firms. Hence observed differences in performance between programme participants and matched firms cannot be attributed solely to programme participation

There are now a number of statistical and other techniques that address the issue of selection bias with these being closely associated with James Heckman. [Heckman and Robb (1985); Heckman and Vytlačil (2001)].

Another, probably more reliable, approach is through the use of randomised trials. Here, in order to assess the issue of both self and (possibly) committee- selection, all eligible applicants for a programme are placed in a lottery. Funding is provided to those that “win” and their performance is then compared over time with the “losers”. The difference between the performances of the two groups is defined to be the impact of the programme.

Sadly, randomised trials for SME programmes are extremely rare anywhere in the world. This is primarily because policy makers are uncomfortable with allocating public support through a lottery. The general view is that all eligible businesses merit access to support, and to exclude some in order to conduct an evaluation is indefensible. However, in practice access to public programmes is restricted by having specific “eligibility criteria” which means such programmes are rationed by law rather than through a lottery. On these grounds the reluctance of policy makers to undertake randomised trials, whilst being understandable, has little underlying logic.

3. So what seems to work and where is the jury still out?

Given the highly imperfect information available to policy makers seeking to enhance entrepreneurship or enterprise in their economy, what guidance can researchers provide?

To address this question a valuable distinction can be made between “macro” and “micro” policies. Macro policies are government-wide policies that impact upon SMEs and entrepreneurship but do not have this group as their prime target. Micro policies are those that are focussed upon SMEs and/ or entrepreneurship and are normally delivered by the arm of government responsible for smaller enterprises.

Table 3 below identifies seven “Macro” policy areas and summarises briefly and interprets the findings of the OECD (2007b) review of policy impact in these areas. It broad conclusion is that for each of the seven policy areas there is some evidence of them influencing entrepreneurship. In general the evidence upon which these statements are based are large scale outcome-based surveys often using official data.

Table 3: Macro Policies: Influences on Entrepreneurship

POLICY AREA	COMMENT
Control of Inflation/ Low interest rates/ Economic certainty	Entrepreneurship is lower when interest rates are high and self employment rates are enhanced by stability
Low tax regime	Tax impact is complex. Low marginal tax rates increases self-employment effort. However low rates also reduce the tax benefits of self employment over being an employee. It therefore discourages individuals to shift
Immigration policy	In-migrants from another country are often [but not always] highly enterprising individuals. Policies to either encourage or restrict immigration therefore can impact powerfully upon enterprise
Welfare payments	In most developed countries the unemployed are more likely to enter self employment than the employed. The evidence is that countries with more generous and long-lasting benefit regimes have fewer unemployed individuals “pushed” into self employment
Competition policy	Competition amongst financial institutions is critical to providing access to finance for SMEs. Where competition is imperfect financial institutions can make “easy” money by lending to government or

	large firms, without having to incur the costs and risks of the SME market.
Business Regulation	As noted in this paper there is clear evidence that the difficulty of starting and operating a business varies considerably between countries. Whilst it is less clear that regulation influences the overall scale of entrepreneurship in a country it is clear that it influences the scale that is recorded in official data.
Policy Delivery	It appears that the same policy can be effective in one country and yet ineffective in another. It also appears that the same policy in the same country can vary in effectiveness over time. Our view is therefore that economic circumstances and policy delivery influence overall effectiveness

We now turn to micro policies to promote entrepreneurship. We noted above in Table 3 that evidence pointed towards policy effectiveness varying both between countries and according to economic circumstances even within the same country.

To illustrate the absence of a “one size fits all” approach to policy, Table 4 takes five “micro” policy examples from the very different countries of UK and Mexico. For each policy it reviews whether, using the Six Steps framework, there is evidence of policy effectiveness and, by implication, whether such policies should be extended in scale. In making the latter judgement account has to be taken both of the circumstances of the country as well as policy impact *per se*. The evidence base for these judgements is primarily OECD (2007a,b)

The first micro policy area is that of management and workforce training. In the UK the evaluations undertaken point to very different outcomes. Broadly those using evaluation approaches Steps I to IV point to evidence of impact, whereas those using Steps V and VI do not. For this reason the UK impact is classified as Mixed. In Mexico there are no evaluations of this policy area.

Seeking to increase R&D in SMEs is a major focus of policy in many countries. In part this is because of the role that new enterprises, particularly those in the high-tech sector, can play in developing major new innovations. Many countries have sought to implement programmes similar to the Small business Innovation Research Program (SBIR) that spent, for example, 1.1 billion USDs in 1999 in awards to small businesses in the high tech sector. The fact that the US is a technology leader and that the US government is a massive spender in this area seems to have persuaded other governments that they should have similar programmes, even though the evidence that the SBIR program provides significant additionality has been questioned. In the context of a country like the UK, with its strong science-base, such funding can *a priori*, be more easily justified in comparison with the US than is the case for Mexico.

A third policy area is increasing Entrepreneurial capabilities. This includes policies to train business owners. Here the evidence of policy effectiveness depends heavily upon the evaluation approach used. Using the Six Steps approach, Steps I to III point to effectiveness, whereas Steps VI and particularly Step VI approaches find little evidence of effectiveness.

Policies intended to create an enterprise culture have a similar, but perhaps even weaker record. The central problem here is that “cultural change” is, at best, a lengthy process. Changes in education in schools are unlikely to result in more or different businesses being established for at least one decade and probably more than two. The use of control groups, as required in Steps V and VI, would therefore be unlikely to produce useable results for perhaps up to twenty years. Evaluation therefore continues to rely on self-report data of the form used in Steps I to III.

Improving access to finance is a key policy area in almost every developed country for understandable reasons. This is because an, in principle, case that small firms suffer from market failure because of both their higher risk and imperfect information about their operations. Governments have therefore felt justified in “intervening” in providing public funding in both the loan and the equity market. Loan intervention is generally in the form of guarantees, whilst equity intervention is in public funding for funds providing small-scale equity. Evidence of the impact of loan guarantee programmes does point to some additionality. However, as the banking system becomes both more sophisticated and more competitive, it becomes more able to accurately assess risk and information

imperfections are reduced. So, in a country such as the UK, the case for public intervention is less than for example Mexico where the banking system is both less competitive and less sophisticated.

Table 4: Micro Policies to promote Entrepreneurship: Is there a case for further policy development UK and Mexico?

SME and ENTREPRENEURSHIP POLICY AREAS	UK	Mexico
Subsidising increased management and workforce training in SMEs	Mixed	?
Increasing R & D in SMEs	Yes	Some
Enhancing Entrepreneurial Capabilities	Some	Some
Creating an Enterprise Culture	?	?
Improving Access to Finance	No	Yes

The overall case therefore is that whilst there is evidence that the “macro” policies influence the scale and nature of entrepreneurship in a country, the evidence on “micro” policies is more mixed and clearly depends on the circumstances of the country.

4. Conclusion

Two key entrepreneurship themes are woven together in this paper. The first is that entrepreneurship can have key social and economic benefits and, for that reason, the subject is of interest to governments. The second is that governments recognise they can influence the scale and nature of entrepreneurship in an economy. Where there is

much less consensus is about what, if anything, governments can do to ensure that these benefits are delivered. What is clear is that there are considerable financial implications for taxpayers, business owners and the rest of society. Failure to create an entrepreneurial environment may impose a substantial economic penalty in terms of economic growth forgone. However the funding of small business/ entrepreneurship where this has been quantified is substantial. In the UK, for example, annual funding is similar to expenditure on the police or Universities. These are therefore key economic and social decisions.

The paper argues that a necessary but not sufficient condition for this scale of expenditure is evidence of market failure. It is necessary to demonstrate that, without such expenditure, the key social and economic benefits associated with entrepreneurship would either not materialise or do so on a much smaller scale.

Government involvement means key choices have to be made. The first is the extent to which policy should focus upon lowering business barriers, defined as making it easy for individuals to start and run a business. Even amongst wealthy countries there is currently a wide variation in, for example, these barriers. A second choice relates to the extent to which public funds should be directed towards the “support” of new and small firms- where this support is in the form of, for example, the provision of subsidised business advice, or access to finance. A third choice is the extent to which other key policy decisions in areas such as taxation, welfare payments, immigration, education take into account their implications for new and small firms.

The paper is not prescriptive about what constitutes appropriate choices. It recognises these will vary according the circumstances and traditions of that country. However it does argue that, following OECD (2007b) it is in the interest of businesses, taxpayers and society more widely for policies to be both clearly formulated, articulated and evaluated.

Whilst best OECD practice is in evidence in some countries, the overall picture is one of diversity. Particularly noteworthy is the absence of a tradition of evaluation in SME/ Entrepreneurship policy. Some policies never appear to get evaluated and, where assessment takes place, it is too frequently undertaken using only the most primitive of tools.

The paper therefore sets out an approach to evaluation that seeks to focus the attention of policy makers in this area with the intention of ensuring that policy is formulated and delivered in the interests of taxpayers, businesses and society more widely.

REFERENCES

Audretsch, D.B., Grillo, I and Thurik, A.R (2007), "*Handbook of Research on Entrepreneurship Policy*", Edward Elgar, Cheltenham.

Capelleras, J_L., Mole, K.F. Greene, F.J. and Storey, D.J. (2008), "Do more heavily regulated economies have poorer performing new ventures? Evidence from Britain and Spain", *Journal of International Business Studies*, Vol. 39, No 4, pp.

Cooper, R.S. (2003), "Purpose and Performance of the Small Business Innovation Research Programme", *Small Business Economics*, Vol. 20, No 2, March, pp. 137-151

Dennis, W.J. (2005) "Creating and sustaining a viable small business sector" Paper presented at the School of Continuing Education, University of Oklahoma, 27th October

Djankoff, S., La Porta, R, Lopez-de-Silanes, F., Schleifer, A.,(2002), "The Regulation of Entry", *Quarterly Journal of Economics*, Vol. 117, No1, pp.1-37

Department of Trade and Industry, (2007) "*Simplifying Business Support: A Consultation*", London, June

Graham, T (2004), "*Review of the Small Firms Loan Guarantee*", H.M. Treasury, London

Greene, F.J. and Storey, D.J. (2008), "Enterprise Policy: A UK-US comparison", CSME, Warwick Business School, Coventry.

Heckman, J.J. and Robb, R., (1985), "Alternative Methods for Evaluating the Impact of Interventions", *Journal of Econometrics*, Vol. 30, pp 239-267

Heckman, J.J and Vytlacil, E (2001) "Policy-Relevant Treatment Effects"
The American Economic Review, Vol. 91, No. 2, pp. 107-111

Jovanovic, B (2001) "New Technology and the Small Firm", *Small Business Economics*,
Vol.16, no 1, pp53-55

Lundstrom, A and Stevenson, L.A, (2005), "*Entrepreneurship Policy: Theory and Practice*", ISEN International studies in Entrepreneurship, Springer, New York

OECD (1997), "*Best Practice Policies for Small and Medium-Sized Enterprises*", 1996
Edition, Paris

OECD (1998) 'Access to International Markets', A presentation by the Delegation of
Greece, OECD Working Party on Small and Medium-Sized Enterprises, Athens, 26-28
April 1998

OECD (2007a), "*SMEs in Mexico: Issues and Policies*", Paris

OECD (2007b), "*Framework for the Evaluation of SME and Entrepreneurship Policies
and Programmes*", Paris

Oldsman E and Hallberg, K (2002), "*Framework for Evaluating the Impact of small
enterprise initiatives*", Nexus Associates Inc.

Papaconstantinou, G and Polt, W (1997), "Policy Evaluation in Innovation and
Technology: An Overview" in "*OECD Proceedings Policy evaluation in Innovation and
Technology: Towards Best Practices*", Paris, pp. 9-14

Storey, D.J. (1999), "Six Steps to Heaven: Evaluating the Impact of Public Policies to
support Small Businesses in Developed Economies", in D.L. Sexton and H. Landstrom
(eds.), "*Handbook of Entrepreneurship*", Blackwells, Oxford, pp. 176-194

Storey, D.J. (2003), "Entrepreneurship, Small and Medium Sized Enterprises and Public Policies", in Z.J.Acs and D.B. Audretsch (eds.), "Handbook of Entrepreneurship Research", Kluwer, Dordrecht, pp. 473-511

Tan, H and Lopez-Acevedo, G (2007), "Evaluating Mexico's Small and Medium Enterprise Programs", World Bank, Washington, DC

van Praag, C.M. and Versloot, P.H. (2007) 'What is the value of Entrepreneurship? A Review of Recent Research', *Small Business Economics*, Vol.29, no. 4, pp.351-382

World Bank (2006) "Ease of Doing Business Survey" Washington DC

Wren, C and Storey, D.J. (2002), "Evaluating the effect of soft business support upon small firm performance", *Oxford Economic Papers*, Vol. 54, pp.334-365