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Working Party on Small and Medium-Sized Enterprises and Entrepreneurship

**FOSTERING ENTREPRENEURSHIP AND FIRM CREATION AS A DRIVER OF GROWTH IN A
GLOBAL ECONOMY**

The OECD BOLOGNA PROCESS

**2nd OECD Ministerial Conference on SMEs on "Promoting Entrepreneurship and Innovative SMEs in a
Global Economy -- Towards a more Responsible and Inclusive Globalisation" jointly organised by the
OECD and the Turkish Ministry of Industry and Trade, ISTANBUL, Turkey, 3-5 June 2004**

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FOREWORD

At the first OECD Conference of Ministers responsible for SMEs, hosted by the Italian government in Bologna, Italy, in June 2000, Ministers from nearly 50 member and non-member economies adopted the “Bologna Charter for SME Policies”. They envisaged the Bologna Conference as the start of a policy dialogue among OECD member countries and non-member economies and that it would be followed up by continuous monitoring of progress with the implementation of the Bologna Charter. This dialogue and monitoring have become known as the “OECD Bologna Process”. The second OECD Conference of Ministers responsible for SMEs, hosted by the Turkish Ministry for Industry and Trade (Istanbul, 3-5 June 2004) provides an occasion to assess the impact on SMEs of new developments relating to globalisation.

This report is one of ten background reports prepared for the Istanbul Ministerial Conference, the theme of each report being linked to a specific Workshop of the Ministerial Conference. Several earlier versions of the report were reviewed by the OECD Working Party on SMEs and Entrepreneurship whose comments have been incorporated into the final version. Non-member economies participating in the OECD Bologna Process have also had an opportunity to provide comments. The final report sets out some policy messages and recommendations that have emerged from the preparatory work undertaken in the Working Party on SMEs and Entrepreneurship. The wide variation in stages of economic development, institutional arrangements and political context across the economies participating in the Bologna Process, now more than 80, means that not all parts of specific policies and programmes are appropriate for all participants. The messages and recommendations outlined below provide material from which governments may choose to draw for in promoting innovative SMEs in the global economy. In broad terms, these policy messages and recommendations elaborate on the themes developed in the Bologna Charter. Ministers will consider these and other recommendations in their deliberations at the Istanbul Conference.

This report and its annex were prepared by the SME Unit of the OECD Secretariat (Marie-Florence Estimé and Marian Murphy) with contributions by Peter Ladegaard (Directorate for Public Governance and Territorial Development) (Annex A) and Zhang Gang (Science and Technology Policy Division) (Annex B). Dr. Chris Hall, Macquarie University, Sydney, Australia, served as external consultant and also contributed Annex C.

This report is issued on the responsibility of the Secretary-General of the OECD. Views expressed are those of the authors and do not necessarily reflect those of the Organisation or its member governments.

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SME Unit website : <http://www.oecd.org/sti/smes>

Conference website: <http://www.oecd-istanbul.sme2004.org>

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Fostering Entrepreneurship and Firm Creation as a Driver of Growth in a Global Economy¹

EXECUTIVE SUMMARY

Entrepreneurship is considered key to economic performance, in particular with respect to innovative change, playing an important structural and dynamic role in all economies. Encouraging entrepreneurship is increasingly recognised by governments as an effective means of: i) creating jobs; ii) increasing productivity and competitiveness; and iii) alleviating poverty and achieving societal goals, in particular by helping specific population groups to help themselves.

There is no universally accepted definition of entrepreneurship, and the concept of “entrepreneurship” may be applied broadly or in a narrow sense. The vocation of this report is neither to address the definitional issues nor to cover the broad span of entrepreneurial activity in the economy. Rather the report focuses on a segment of the entrepreneurship spectrum – *the pre-start-up, start-up, and to an extent, the early-post start-up phases of entrepreneurial activity*. The report also emphasises the need to take account of the various types of entrepreneurs, having regard to their propensity for risk and uncertainty, and with regard to entrepreneurial behaviour motivated by necessity or opportunity. In addition the report argues for the need for policymakers to take into account the ‘package’ of business environment factors, and the need for policy to be adapted to specific contexts, trade-offs being inevitable and there being no ‘one-size-fits-all’ formula.

Facilitating the building of a more entrepreneurial society is a priority shared by most governments. The emergence of a larger pool of entrepreneurs in national economies presupposes the existence of a conducive entrepreneurial business environment, dependent on the provision of a stable macroeconomic environment and appropriate general framework conditions. These framework conditions affect the business climate in a variety of ways, including through regulatory and administrative burdens; labour market legislation; the legal framework; competition policy etc. While regulatory and legal frameworks can carry intrinsic benefits for enterprises they may also act as barriers to firm entry. Recent OECD research has shown that excessively stringent product and labour market legislation can have a negative impact on both firm entry and productivity. Measures such as Regulatory Impact Assessments and administrative simplification procedures are being developed to address these issues. Likewise, employment protection legislation, if unduly restrictive, can discourage the hiring of personnel and jeopardise enterprise expansion when growth opportunities arise. Similarly, excessively stringent bankruptcy legislation can deter firm entry, make exit from the market very costly for unprofitable firms, and deprive “unsuccessful” entrepreneurs of a second chance.

Culture is increasingly acknowledged as a factor for contributing to building an entrepreneurial society in so far as it is an important determinant of career preferences and helps shape attitudes to risk-taking and reward. Cultivating an entrepreneurial culture and creativity and fostering entrepreneurial attitudes and values has moved high on government agendas. Education and training (including lifelong training) in entrepreneurship is the preferred instrument for fostering entrepreneurial behaviour in societies,

¹ Separate reports have been prepared on related topics: “Women’s Entrepreneurship: Issues and Policies”; “Facilitating Access to International Markets for SMEs”; and “Financing Innovative SMEs in a Global Economy”

and evidence suggests that such programmes can have an impact on entrepreneurial activity and enterprise performance and profitability. However, in spite of the numerous initiatives launched and implemented in recent years, a number of shortcomings and problems characterise this domain: entrepreneurship is not sufficiently integrated into educational curricula nor integrated into national long term economic strategy and planning; a lack of public resources has resulted in limited teaching and research capability in this field; there is a need to improve coordination among government agencies for the design and implementation of initiatives; there is a need for a broader acceptance of the concept of education and training for entrepreneurship; and a need for more data and evaluation and assessment of initiatives taken.

Entrepreneurship and SME policies have also an important local dimension, and indeed, facilitating increasing rates of enterprise creation is an almost universal concern for local authorities for accelerating development or reversing decline in localities, applying to both disadvantaged and prosperous localities. Numerous programmes with the aims of reducing unemployment, including chronic unemployment, and social distress have been implemented in many countries. New enterprises can procure a range of benefits that contribute to local development, among which: employment and incomes growth; enhanced provision of services for consumers and businesses, and possibly, demonstration and motivational effects. Determinants of rates of enterprise creation at the local level include demographics, unemployment, wealth, the educational and occupational profile of the workforce, the prevalence of other small firms, infrastructure endowment etc. However, recent OECD research finds a set of related constraints that can impede entrepreneurship, especially in deprived localities (OECD, 2003a).

Key policy recommendations

- **Ensure stable macroeconomic and framework conditions to underpin the entrepreneurial business environment.** Policy design in areas such as competition, the regulatory framework, the tax system, labour markets, financial markets and bankruptcy laws should take account of the way these areas impinge on SMEs and innovation in knowledge-based economies.
- **Ensure the reduction and simplification of administrative regulations and costs which fall disproportionately on SMEs.** Take account of SME views during the regulatory process; require regulatory agencies to prepare Small Business Impact Statements; establish one-stop shops for regulatory information and transactions; and promote the use of e-government tools.
- **Promote an entrepreneurial society and entrepreneurial culture, in particular through education and training.** Integrate entrepreneurship at all levels of the formal education system and ensure access to information, skills and expertise relating to entrepreneurship via "lifelong learning" programmes for the adult population. Promote the diffusion of training programmes by stimulating the private market's supply of such services and providing hands-on focused courses.
- **Integrate the local development dimension into the promotion of entrepreneurship.** The roles of sub-national authorities in the promotion of entrepreneurship are of paramount importance and should be defined and co-ordinated with central governments, as appropriate for each country.
- **Ensure that programmes in support of SMEs and entrepreneurship are realistic in terms of cost and are designed to deliver measurable results.** An evaluation culture should be developed to ensure that programmes are systematically monitored and assessed for their performance in achieving objectives and for their cost-effectiveness.
- **Strengthen the factual and analytical basis for policymaking so that policy makers can take decisions in an informed manner based on empirical evidence.** A strengthened statistical basis will permit cross-country comparative analysis and policy-relevant longitudinal studies. An internationally comparable set of indicators should be developed for monitoring the level of entrepreneurial activity and the entrepreneurial environment in each country.

In order to facilitate greater dynamism in the creation and expansion of businesses, governments need to go beyond these efforts by designing programmes and support policies in order to increase the likelihood of a high degree of entrepreneurial activity. Clearly specifying objectives and targets of policy is essential for conducting programme evaluation². Given the complexity of designing programmes and support policies well, and the need to ensure that scarce resources are used cost-effectively, it is important to ensure that they are systematically reviewed, assessed and evaluated. It is essential to incorporate the evaluation dimension into the design stage of support policies and programmes.

But, to design programmes and support policies in a cost-effective way, governments need a good empirical understanding of the linkages between, *inter alia*, entrepreneurial environment factors, entrepreneurial activity, social factors and the entrepreneurial contribution to outcomes. Currently, many major gaps exist in the current empirical knowledge and there is a need to strengthen the factual and analytical basis for policymaking so that policy makers, having a better understanding of the processes and the trade offs, can make decisions in an informed manner based on empirical evidence. At minimum, this will require strengthening the present empirical base in terms of data and statistics³.

² The evaluation of policies and programmes was designated as a cross-cutting theme of the Istanbul Ministerial Conference and a separate background report was prepared on this theme. The report strongly emphasises the need to clearly specify policy and programme objectives and targets in order to undertake meaningful evaluations.

³ A separate background report “Towards a More Systematic Statistical Measurement of SME Behaviour” addresses these issues.

Fostering Entrepreneurship and Firm Creation as a Driver of Growth in a Global Economy

INTRODUCTION

Entrepreneurship is increasingly considered key to economic performance, not just in the OECD area, but also world-wide, playing an important structural and dynamic role in all economies. Governments are therefore seeking to maximise the contribution of entrepreneurship to achieving key policy outcomes. Indeed, Ministers participating in the Bologna Conference on SMEs in June 2000 *recognised* in the Bologna Charter on SME Policies that entrepreneurship and a dynamic SME sector are important for net job creation, for increased competitiveness, for restructuring and revitalising economies, and for combating poverty. It is in this context then that one of the themes of the 2004 Istanbul SME Ministerial Meeting Programme has been designated to be “*Fostering entrepreneurship and firm creation as a driver of growth in a global economy*”.

Defining entrepreneurship: facing the challenges

There is no universally accepted definition of entrepreneurship. The concept of “entrepreneurship” is elusive, difficult to define, measure and therefore, promote. The concept of “entrepreneurship” may be applied broadly or in a narrow, focused way depending on the context. “Enterprise” and “entrepreneurship” can have a range of meanings in different contexts (Bridge, *et al.*, 2003), denoting a mindset or type of behaviour (entrepreneurial behaviour) in the broadest sense or equated with a small business undertaking in the narrow sense. Entrepreneurship has typically been referred to as an action, process, or activity, in which innovation plays a significant role. Substantial entrepreneurial behaviour can occur among existing entrepreneurs and existing firms, including longer established firms, and the systematisation of innovation and commercialisation within existing firms. The recent Green Paper on Entrepreneurship in Europe by the European Commission (2003b, p.6) defines it as follows: “Entrepreneurship is the mindset and process to create and develop economic activity by building risk-taking, creativity and/or innovation with sound management, within a new or an existing organisation”. Despite the definitional differences, it is commonly agreed that entrepreneurship is a driving force behind SMEs.

A number of major research projects are underway or have been undertaken recently on the topic of entrepreneurship, all of them appearing to adopt a different definition or approach. The *Entrepreneurship Policy for the Future* research project led by Lundström and Stevenson (2001, 2002) defines entrepreneurship policy as “*aimed at the pre-start, the start-up and post start-up phases of the entrepreneurial process; designed and delivered to address the areas of motivation, opportunity and skill; and with the primary objective of encouraging more people in the population to consider entrepreneurship as an option, to move into the nascent stage of taking the steps to get started and then to proceed into the infancy and early stages of a business*”. The Finnish Government’s recent “Entrepreneurship Project” used measures corresponding to the different stages of the enterprise lifecycle and concluded a need for governments to move away from traditional SME policy towards a more comprehensive enterprise/entrepreneurship policy. The Danish Government recently launched the “Entrepreneurship Index Survey”, involving a number of other countries, and designed to develop tools for monitoring the entrepreneurial business environment.

The OECD too has addressed the issue of entrepreneurship from a number of angles: e.g. from the local economic development perspective, emphasising the role of entrepreneurship and self-employment for local economic development (OECD, 1998a, 2003a); and in the context of the Growth Study and its follow-up, the role of entrepreneurship in the present time of innovative change is highlighted, in this particular case, the focus of entrepreneurship being on the creation and expansion of firms.

The present report does not pretend to solve definitional problems or to embark on an exhaustive examination of what would constitute entrepreneurship policy. Rather, it aims at identifying ways that governments (of OECD member and non member economies) may, in the context of globalisation, advance the growth agenda through policies that foster firm creation and the rapid growth of start-ups and existing SMEs.

The approach taken in this report considers entrepreneurship policy as directed more towards individuals (isolated or in teams) and considers SME policy as concerning firms *per se*, and geared to creating and growing these businesses. The scope of the report is on entrepreneurship policy and its articulation with SME policy, and how policy objectives and intended policy outcomes can be achieved.

The accumulated body of work on entrepreneurship and SMEs to date indicates the existence of a rationale for both entrepreneurship policy and for an SME policy. Entrepreneurship policy cannot substitute for SME policy and needs to be seen in the wider context of SME policy, as without sound entrepreneurship policies, there cannot be strong SMEs. Neither can SME policy substitute for entrepreneurship policy. The two policies are complementary and should be carried out together, as part of the same continuum – *from the would-be or aspiring entrepreneurs to the large firms*.

In this context, women's entrepreneurship is also attracting increased attention from policy makers and researchers and is recognised as an important untapped source of economic growth, although a reliable and detailed picture of the economic impact of women's entrepreneurship is still lacking. Recent efforts initiated by the OECD in 1997 and 2000 were preliminary responses to this lack of knowledge (OECD 1998b, 2001c). A separate background report on the topic of women's entrepreneurship is being prepared for the Istanbul Ministerial Conference.

Against this backdrop, this background report is structured as follows:

- Under the heading “*Entrepreneurship Matters: the contribution of entrepreneurs to achieving policy outcomes*”, evidence is presented on the structural and dynamic economic role that entrepreneurship plays, showing how entrepreneurial activity contributes to achieving policy objectives, in terms of its contribution to economic growth.
- The next section proposes an analytical framework to assist policymakers to shape a conducive *Entrepreneurial Business Environment (EBE)*, through an appropriate *Entrepreneurial Policy Environment (EPE)*. The framework uses these two pillars, the *EBE and EPE*, and distinguishes between entrepreneur types (*aspiring, lifestyle, growth-oriented and heroes*) based on risk/uncertainty criteria and the necessity *versus* opportunity factor. This framework has policy implications depending on the prevailing entrepreneur types and the actual policy context. The role of regulatory and administrative burdens, the role of education and training, as well as local factors, for fostering the creation and development of enterprises are reviewed.
- The final section presents some concluding remarks, addressing the implications for entrepreneurship policy.

The intention being to produce a concise report, more detailed empirical evidence, and supporting material and documentation are treated in a number of Annexes to the report.

ENTREPRENEURSHIP MATTERS: THE CONTRIBUTION OF ENTREPRENEURS TO ACHIEVING POLICY OUTCOMES

The creation of new businesses and the decline or market exit of less productive firms are regarded key to business dynamism and economic growth. Young firms are thought to help shift resources to new markets, to be especially innovative and to play an important role as job creators. Available evidence suggests that entrepreneurship *can contribute significantly* to achieving key policy objectives. Entrepreneurship is an effective means of achieving certain policy objectives, but not all, and at least in the short term, there are trade offs which have to be recognised. Entrepreneurs are the driving force behind SMEs, and SMEs play an important *structural and dynamic* role in all economies. The main areas where increased levels of entrepreneurial activity *can* contribute significantly to specific policy outcomes are:

- i) *Job creation.*
- ii) *Economic growth, productivity improvement, and innovation.*
- iii) *Poverty alleviation and social opportunities.*

Job creation, and unemployment reduction

Entrepreneurial activity can create jobs as entrepreneurs pursue opportunities, profits, and personal ambition and self fulfilment. It should also be stressed that entrepreneurial activity contributes to maintaining and securing jobs in addition to the generation of new jobs. Because job creation is a policy priority for almost all OECD member and non member economies, the ability of entrepreneurial activity to create jobs is thus of major interest to most governments. Jobs are created when firms start up or grow while the net balance of creation and destruction leads to net job creation. There are two main avenues by which this occurs:

- ❖ *An excess of jobs created by firm start ups over jobs lost by firm exits.* In any given period, a proportion of firms exits and a proportion enters the economy. On balance, if the number of jobs created by entry exceeds the number of jobs created by exit, then it is likely that there will be net job creation occurring. This process is affected by cyclical patterns in the economy. In addition, when unemployment increases, some people start up ventures as an alternative to unemployment.
- ❖ *The growth of existing firms.* Growth of existing firms seems to be a major source of net job creation, but it is typically concentrated in a relatively small group of firms, characterised by rapid growth. OECD research (OECD, 2002a) shows that the growth trajectories of these high growth firms are often unpredictable, so at an individual firm level "picking winners" is never likely to be an effective policy. However, many SME managers do not wish to expand, or lack resources and capability to do so, or are deterred by government policies which create artificial barriers to expansion. There are opportunities for governments to facilitate job growth by encouraging or making it easier for growth oriented entrepreneurs to expand.

Overall there is fairly clear evidence from many economies that SMEs are a major contributor to job creation, but that this differs by size and type of SME, and by economy (Schreyer (1996), OECD, 1997, 2000, 2002a). Whether this net job creation comes from a small proportion of high-growth firms or

from the more general process of start up is an empirical question and depends on the business environment and the time period. In Europe, for example, from about 1990 to 2001 micro enterprises were the only significant contributors to net job creation, and made a positive contribution only from about 1997 onwards⁴. Evidence from Australia in the 1990s suggests that SMEs contributed between 63% and 78% of net employment growth⁵.

OECD studies of business demographics (Bartelsman *et al* 2002.; Brandt, 2004a, 2004b) have shown that significant numbers of firms enter the market every year. At the same time, an approximately equal number of firm exits, as entrants drive incumbents firms out of the market. In many cases, the newcomers do not survive for long themselves. This general pattern combining high rates of entry and exit occurring simultaneously can be found across all economic sectors, including narrowly defined sectors. Overall, the cross-country variation of entry and exit rates, i.e. the number of new or exiting enterprises in relation to all active firms, is rather modest and Scarpetta *et al* (2002). find a similar degree of firm churning in Europe and in the United States. However the latter study does find distinguishing features of firms' behaviour in the United States market compared with the EU situation to be: i) the smaller (relatively to industry average) size of entering firms in the US; ii) the lower labour productivity level of entrants relative to the industry incumbent; and iii) the much stronger (employment) expansion of successful US entrants in the initial years which enable them to reach a higher average size. Overall, the studies find considerable cross-industry variation, entry and exit rates having been exceptionally high in recent years in young ICT related services sectors, but much lower in more mature industries.

Exploring the industry dimension of the data reveals that firm entry rates are significantly correlated with output and employment growth across services sectors, while this relationship is much less clear-cut in manufacturing. Brandt (2004b), in order to gain further insights into this issue, explores how EUROSTAT firm entry data along with OECD economic performance indicators are related to economic performance. A central finding is that firm entry rates tend to be higher in industries with higher output and employment growth. The relationship between entry rates and performance measures is much stronger in services industries than in manufacturing and there are indications that it takes time for firm creation to unfold its impact on economic performance. Indeed, Van Steel and Storey (2002) find that firm entry has its strongest impact on employment creation after four to seven years.

New firms may have a positive impact on output and employment growth via productivity in the younger services sectors, while their role for productivity and thus output and employment would be less important in more mature sectors (it should be noted that productivity effects are addressed in the next section). At the same time, output and employment growth can be expected to be higher in younger industries because both new firms enter and incumbents expand in an attempt to seize unexploited business and technological opportunities. Moreover, the competitive pressure due to firm turnover should be expected to be stronger in younger industries, simply because firm churning is higher.

Growth, productivity and innovation

The recent emphasis on entrepreneurship also reflects new key insights into the relationship between entrepreneurship and productivity, innovation and growth. An OECD study (OECD 2001d) finds a positive relationship between the level of entrepreneurship (as measured by start-up rates) and economic growth for OECD economies, as shown in Figure 1. A recent report by the Inter-American Development Bank (2002)⁶ confirmed the capacity of entrepreneurs to create employment in the regions subject of the

⁴ European Commission/Observatory of European SMEs (2002a).

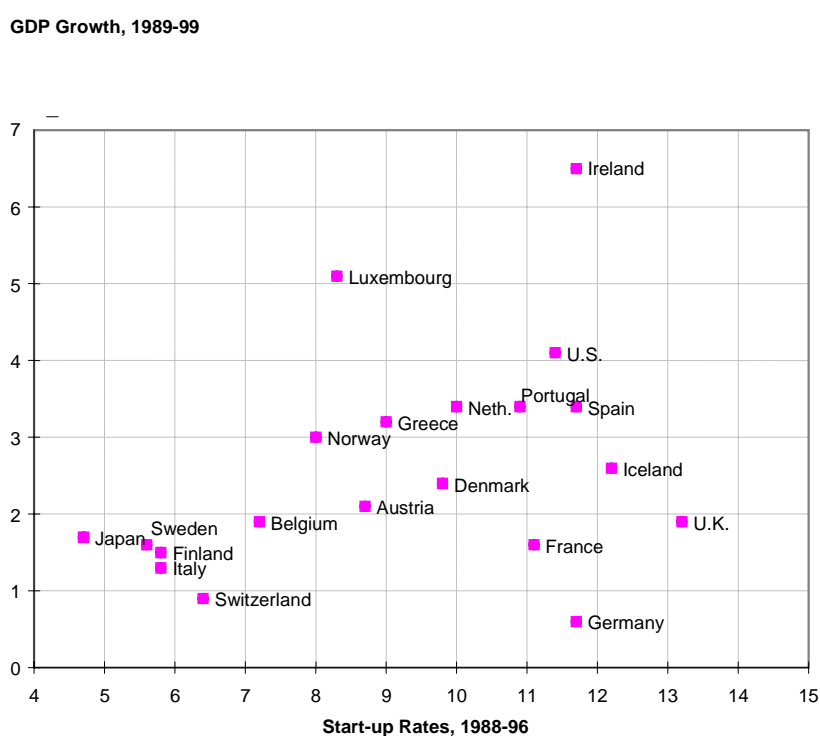
⁵ Hall (2002).

⁶ IADB (2002).

study, Latin America and East Asia, the expansion being particularly robust in East Asia. As part of the OECD Growth Project, the micro-economic linkages to productivity growth between 1989 and 1994 were examined, finding for seven of the ten OECD countries analysed that the start up of new firms has a positive and significant impact on the overall productivity of firms. The contribution from firm dynamic processes was most notable in high tech industries where new firms tend to play an important role.

Using more recent data for nine European countries and examining more closely the relationship between firm entry and economic performance, Brandt (2004b) found that firm entry has a significantly positive impact on labour and total factor productivity growth, although the impact is generally higher and more robust when the analysis is confined to services industries. The finding that the positive relationship between firm entry and productivity is stronger and more robust in services is an indication that in these industries the innovative activity performed in new firms and the competitive pressure exercised through this has a particularly pervasive effect, while large-scale research and development based on specialised personnel and laboratories dominate as drivers of productivity in the generally more mature manufacturing industries. The findings suggest that countries' policies and institutions might be particularly important for the youngest and most dynamic industries (Brandt, 2004b). In addition, a study by the Local Economic and Employment Development (LEED) Programme of the OECD (2003a) points to a link between entrepreneurship and growth existing at the local and regional levels. In general, findings also suggest that the effect of new firms on productivity takes time to unfold.

Figure 1. GDP Growth and Start-up Rates



Note: GDP growth rates: 1995-99 for Austria, 1990-99 for Germany.

Source: OECD and the European Observatory for SMEs, Fifth Annual Report.

Improvements in productivity are often considered to "destroy" jobs, in that they reduce costs, improve efficiency, and increase competitiveness, thus enabling firms to compete and grow. However, improvements in productivity also release workers for other, often more productive and valuable uses. In

the longer term, the bulk of economic growth comes from doing things more efficiently rather than from increasing inputs *per se*. A part of this productivity improvement is "unexplained" and Baumol (2002, pp. 58-59) has argued that entrepreneurship capital may account for a significant amount of the growth left unexplained in traditional production function models. A recent literature has emerged suggesting that such entrepreneurship capital may be a missing link in explaining variations in economic performance (Acs and Audretsch, 2003).

Further to this theoretical proposition, an OECD study (Scarpetta *et al.*, 2002) has shown that firm entry and exit help increase aggregate productivity growth by shifting resources from old and less productive firms to new and more productive ones. Likewise, a Canadian study shows that because new firms tend to be much more productive than exiting firms, net entry contributes significantly to aggregate productivity growth. Entering cohorts become more productive on average over time both as a result of selection and of learning, as competition forces the less productive firms to leave the market, while surviving young firms improve their productivity (Baldwin and Gu, 2003).

Poverty alleviation and social opportunities

Over the last two decades, there has been a shift toward encouraging greater "social entrepreneurship" as a means of poverty alleviation, increasing employment opportunities and empowerment of disadvantaged or under-represented groups. Awareness of the potential which entrepreneurship may offer for promoting social inclusion is growing worldwide. The European *EQUAL* Community initiative on "Making Entrepreneurship Accessible to All" has, *inter alia*, recently sought to mobilise stakeholder opinion and collect comments, in the wake of the European Commission's Green Paper on Entrepreneurship, and in preparation for the Spring 2004 Action Plan, so as to ensure effective integration and coordination between start-up policies and employment and social inclusion policies. This is being done so as to more effectively address the needs of the concerned disadvantaged groups experiencing obstacles to entrepreneurship. The *Equal Initiative* finds that the tools on which service or finance providers rely to assess business start-ups and their needs do not reflect the present diversity of potential entrepreneurs as they are based on traditional profiles and criteria prevalent in the past. The comments collected call for "valuing diversity" and argue that beyond the regular statistical collection, data should be systematically collected on start-ups taking into account gender, ethnic origin, age, the existence of disabilities etc. It is considered to be a priority to promote positive role models of entrepreneurship among disadvantaged social groups, "shifting away from a sense of powerlessness experienced by many disadvantaged groups".

Much of this emphasis placed by governments is focused on assisting target groups to start up micro enterprises, usually by means of the provision of low cost micro finance. These policies implemented in many non-member economies have been shown to be remarkably effective by some criteria, and are well illustrated by the success of the Grameen Bank⁷. Micro enterprises are important in their own right, for two closely interrelated reasons:

- In the longer term, they can provide a seed bed for entrepreneurship, and for the corporate growth and economic renewal needed to maintain international competitiveness. Almost all

7. The Grameen Bank Project originated in 1976 in Bangladesh, to examine the possibility of designing a credit delivery system to provide banking services targeted at the rural poor, to eliminate exploitation of the poor by money lenders, and create opportunities for self-employment for the unemployed. In 1993, by which time the Grameen Bank Project had extended its operations to several districts, became an independent bank. The Grameen Bank is now owned by the rural population which it serves.

SMEs start as a micro enterprise, in that they start as a concept developed by a single person or a few people⁸.

- In the immediate term, they can provide an alternative to unemployment, and they can provide a means of alleviating poverty and social disparities. Most micro enterprises are non-employing, but they create a job (even if it is only part time) for the entrepreneur.

Entrepreneurship can offer greater social mobility to disadvantaged population groups in all economies. Significant country and regional variations in entrepreneurial activity by population groups are found. A recent Inter-American Development Bank report which examined entrepreneurship in emerging economies in Latin America and East Asia found that nearly half of the dynamic ventures⁹ in East Asia were founded by people from the lower and middle classes, while in Latin America only about one-quarter came from these population strata, suggesting that the contribution of entrepreneurship to social mobility, and to the creation of wealth, is lower in Latin America than in East Asia. One of the report's conclusions recommends that a policy aimed at promoting entrepreneurial capacity should focus on increasing the number of entrepreneurs and broadening the range of social origins of entrepreneurs who can access the means necessary to create new businesses. It is this latter aspect of poverty alleviation and providing a social and economic alternative to chronic unemployment that is of importance to entrepreneurship policy objectives, in OECD economies and especially in non-OECD developing economies.

Recent OECD (2003a) research finds that most countries operate specialised entrepreneurship schemes to assist target firms and population groups. These include programmes designed for ethnic minorities, youth, women and social enterprises. There is clearly also a local dimension with regard to this issue and recent growth in entrepreneurial activity in some of these target population groups is often closely linked to local communities.

With regard to *ethnic minorities*, many of these populations reside in geographically concentrated communities. Difficulties encountered by members of ethnic minorities to access employment on the one hand, and to access financing in support of their self-employment, are recognised. Nevertheless, the share of certain minority populations that engage in entrepreneurship is often relatively high with respect to the national average. Various competing theories have sought to explain this. On the one hand, it is held that minorities can face obstacles in obtaining waged and salaried employment (including for reasons of skills). On the other hand, a set of broadly positive influences might "pull" ethnic minorities into entrepreneurship. These could include supportive ethnic business networks etc. A recent OECD study (2003a) suggests that programmes could be selectively adapted when targeting ethnic minority groups, while policy should tackle discrimination and other barriers. The study points out potential drawbacks to developing separate programmes for ethnic minority entrepreneurs, and instead recommends appropriate adaptation and specialisation within mainstream support programmes for these target populations. Policymakers, including at the level of local authorities, need to pay attention to the lack of knowledge among immigrants concerning the practical steps to starting a business, and in this regard, a frequently encountered problem is the low usage of mainstream advisory and support services among minority groups.

High rates of unemployment prevail among young people especially in deprived communities. This phenomenon combined with the associated social problems, have spurred action for encouraging

8. This seems not only true for developing non-member economies, but also true for the OECD economies, as Brandt (2004a) finds that start ups in six OECD countries are normally smaller in size than existing firms.

9. Dynamic ventures are defined, in the IADB report, to be ventures able to expand their workforce between 15 and 300 employees within the first ten years of business. It was decided to focus the analysis of the survey results primarily on dynamic or successful ventures because they appear to offer the most relevant lessons for fostering entrepreneurship.

youth entrepreneurship. Large numbers of young people aspire to self employment, but their lack of human capital and relevant experience makes entrepreneurship a viable option for very few among them. Indeed, young aspiring entrepreneurs generally face a number of obstacles that are more severe than for other groups. In addition, the age of the entrepreneur is found to be an important determinant of enterprise survival. For instance, Scott (1995) found that persons over thirty-five years of age entering self employment usually have greater survival chances. And in France, an INSEE study conducted in 2000 found that a new entrepreneur, if aged fifty or older, stood a 66% chance that the new enterprise would survive for three years. By contrast, this probability falls to 50% if the entrepreneur is younger than twenty-five. More particularly, as a remedy for unemployment amongst disadvantaged youth the promotion of entrepreneurship on its own is not expected to be very effective, and a coherent programme package needs to take account of the particular set of difficulties confronted by the specific target population group. As in the case of programmes for ethnic minorities, the OECD study considers that establishing separate schemes for youth could be inefficient and existing programmes should rather be adapted and advertised in a variety of specific ways (OECD, 2003a). In particular, training and mentoring networks could play a critical role to help compensate for the lack of prior business experience.

Many OECD governments are aiming to support enterprise in disadvantaged areas and amongst disadvantaged and underrepresented groups through various programmes and support projects and schemes. An example is the United Kingdom's Phoenix Fund which provides support for projects involving specialist business support organisations in disadvantaged communities.

CREATING AN ENTREPRENEURIAL BUSINESS ENVIRONMENT CONDUCTIVE TO ENTERPRISE CREATION

“The key to successful enterprise policy is true horizontal cooperation within which various ministers and ministries work together. It means appointed officials of various ministries are responsible for ensuring that legislation is drafted to promote entrepreneurship and that the impact of various policy measures on entrepreneurship is taken into account”¹⁰.

Policies affecting the overall business environment

Because of the importance of entrepreneurship to economic growth and competitiveness, governments of OECD countries, and non-OECD economies alike, pay increasing attention to how to design policies to promote entrepreneurship. However, this remains a challenge for most national governments since creating an entrepreneurial business environment conducive to enterprise creation and rapid growth of innovative firms comprises a number of building blocks covering a wide range of policy domains. First and foremost, start-ups will best be encouraged and able to prosper in a stable macroeconomic environment based on sound fiscal and monetary policies. In addition, the range of structural policies that define the broad framework conditions governing business activity generally, should be designed to impinge at least neutrally, if not favourably, on SMEs and entrepreneurial behaviour. This involves, among other things, ensuring appropriate competition policies, open capital markets, a competitive taxation regime, flexible labour markets, access to global markets, and access to government procurement opportunities.

An important element of the general policy framework is its implications for risk, and in particular, the risk-reward trade-offs facing potential entrepreneurs. The propensity to bear risk is relative, and relative to aspects such as the level of education and training. This has important implications, because the relativities can be altered by policy, for example, by creating more flexible labour markets and discouraging the certainty that goes with lifetime tenure and corporate support. For example, throughout much of Europe, there is an observed tendency to try to limit the expansion of the welfare state, and in China the "iron rice bowl" (which guaranteed workers state services, such as housing and health, from cradle to grave) has been broken. Similarly, reducing the penalties associated with bankruptcy, or changing the tax treatment of capital gains, changes the risk borne by entrepreneurs relative to that faced by those on fixed wages and salaries.

Programmes and Support Policies

However, governments need to go beyond the provision of the necessary framework conditions with respect to the goal of achieving the highest *likelihood* of entrepreneurial activity. In particular

¹⁰ Message delivered to the Budapest Workshop on Entrepreneurship in September 2003, by the Finnish Delegation, reporting on the lessons learned from the Finnish Entrepreneurship Project.

governments need to address policy and market failures which can serve to dampen entrepreneurial activity. In practice, this requires programmes and other policies of assistance or support for SMEs and entrepreneurial behaviour. To design such programmes and support policies in a cost-effective way, governments need a good empirical understanding of the linkages between:

- Entrepreneurial Environmental Factors (*i.e.* Rule of Law, education – especially entrepreneurship education, culture, property rights, finance availability etc.).
- Entrepreneurial Environment Package (*i.e.* the package of factors at a given time and place, which is partly a result of history, but which can be significantly impacted by policy initiatives, and is increasingly affected by the pressures of globalisation).
- Entrepreneurial Types present in a particular location (*i.e.* lifestyle entrepreneurs, growth-oriented, heroes, etc).
- Entrepreneurial Activity (as reflected in “interested would-be” entrepreneurial intentions, start-up rates, exit rates, etc.).
- Entrepreneurial contribution to outcomes (*e.g.* to net job creation, innovation, GDP growth, etc.).
- The impact of policy, especially entrepreneurship policy and SME policy on all of the above.

At present the basis for such understanding is weak in nearly all countries. To develop it will require strengthening the existing empirical information base, in terms of data and statistics, so as to permit policy-relevant longitudinal studies and cross country comparative analysis with the aim of developing an internationally comparable set of indicators for monitoring the level of entrepreneurial activity and the entrepreneurial environment in each country¹¹.

Designing such programmes and support policies in a cost-effective way also requires clarity in terms of their objectives and target beneficiaries. In this regard, it is important to recognise that not all entrepreneurs are the same, and *are thus unlikely to respond to policy initiatives in the same way*. For this reason it is useful to suppose a few broad categories of entrepreneurs (and would-be or aspiring entrepreneurs) on the broad basis of their propensity to bear risk and uncertainty. While any classification is of course artificial and does not meet the complexity of reality, it may nevertheless be helpful to distinguish four main types of entrepreneur who may respond differently to any particular programme or policy:

1. Aspiring or would-be entrepreneurs

Considered to be the largest group, they would have a higher propensity for risk and uncertainty than the general public, although only a small proportion would actually take steps to start a business. However, the group would represent a large latent pool of potential entrepreneurs even if most of them do not have sufficient risk and uncertainty propensity to set up a business, except when environmental factors force them to (such as losing their job in a downturn).

¹¹ A separate background report “Towards a More Systematic Statistical Measurement of SME Behaviour” has been prepared which addresses these issues.

2. *Lifestyle entrepreneurs*

Lifestyle entrepreneurs would have a relatively low propensity for risk and uncertainty, and would generally not be interested in growing their business beyond a relatively small manageable size. Most reproduce someone else's ideas and apply them in a different place with small "entrepreneurial" modifications (*e.g.* restaurants, boutiques, small hotels etc.). These lifestyle businesses could constitute the vast bulk of all enterprises, women entrepreneurs probably having a higher proportionate representation in this group.

3. *Growth oriented entrepreneurs*

This group would have a higher propensity to take risk, its members seeking to grow their venture. Their share in the entrepreneur population would differ across economies, and vary with structural and cyclical conditions. Many of them would be professional managers, often working for, or seeking to sell out (*i.e.* capitalise out) to, a larger firm. They mostly operate on the basis of fairly well known risks, even if those risks are quite high. They tread new paths, but have good navigation equipment to help them.

4. *"Heroes"*

Heroes would be a small subset of the growth oriented entrepreneurs. They step into the unknown, where they don't know what the risks are, because no one has really tried it before. They are usually strongly growth oriented, having a high propensity to bear risk and uncertainty.

Given the complexity of designing programmes and support policies well, and the need to ensure that scarce resources are used cost-effectively, it is important to ensure that they are systematically reviewed, assessed and evaluated. The separate background report on evaluation sets out the main issues that must be addressed to achieve this, arguing that evaluation should be incorporated into programmes and support policies at the design stage¹².

Reducing regulatory and administrative barriers

Regulatory and administrative burdens have been identified as barriers to entrepreneurial activity in recent studies by the OECD (Scarpetta (2002), Brandt (2004b,)) and the World Bank (2003). Likewise, a joint report by the OECD and the EBRD concerning the South East Europe Region¹³ states that barriers to business entry, in terms of procedures, delays, costs and capital requirements remain unnecessarily high in this region. Similarly, a report on entrepreneurship in East Asia and Latin America by the Inter-American Development Bank (2002) finds that red tape and compliance costs hinder the creation of new ventures.

However, policymakers have been tackling this issue in recent times and continue to seek more effective and more coordinated ways to address this issue. In a recent joint initiative¹⁴, the Irish, Dutch, Luxembourg and UK presidencies of the European Union decided to jointly prioritise regulatory reform over the course of 2004 and 2005, and have called for an increasing awareness of the importance of a well-designed regulatory framework for strong economic performance. Included in this joint initiative is a

¹² "Evaluation of SME Policies and Programmes", a background report prepared for the 2nd OECD Conference of Ministers responsible for SMEs.

¹³ OECD-EBRD (2003).

¹⁴ Joint Initiative on Regulatory Reform: An initiative of the Irish, Dutch, Luxembourg and UK Presidencies of the European Union, 26 January 2004.

proposal that the Commission be asked to consider the possibility of developing a common method to measure the administrative burden on companies, due to European legislation.

There is abundant evidence that regulatory and administrative burdens can negatively affect entrepreneurial activity. Scarpetta *et al.*, (2002) show that excessively stringent product and labour market regulations have a negative impact on both firm entry and productivity and conclude that legal *barriers to entry* should be avoided unless their benefits are certain to outweigh the cost that consists in hindering the potential of young firms to help shift resources to new and productive uses, innovate and adopt new technologies. A recent World Bank study (2003) finds that cumbersome entry regulation is associated with less private investment, higher consumer prices, greater administrative corruption, and a larger informal economy. The Inter-American Development Bank (2002) found that in some Latin American countries, red tape and compliance costs were identified by entrepreneurs as a hindrance to the creation of new ventures. These studies and the findings of another major OECD survey-based study (discussed below) recommend that regulatory and administrative procedures should be simplified, transparent, faster to carry out, and should cost less so as to avoid impinging on firm entry.

Barriers to exit may also discourage firms from entering the market much in the way as entry barriers would. Business demography studies invariably find that firm entry is highly experimental involving a lot of exit at the same time, as new enterprises drive a large number of incumbents out of the market and often do not survive for long themselves. To exploit the potential of those young firms that will turn out to be successful and innovative, the experimentation process associated with firm entry should be hindered as little as possible. Since entering firms know little about their survival chances, institutions that make firm exit excessively costly, risk discouraging firms from entering the market in the first place. Brandt (2004b) finds that entry rates tend to be lower the longer creditors have claims on bankrupts' assets.

Likewise, *employment regulation* (employment protection legislation) governing the individual employment contract has implications for firm entry and exit. Employment regulation is found to be generally more flexible in developed countries (World Bank, 2003). Nordic-origin countries regulate employment relations the least in conditions of employment but tend to regulate more in relation to dismissals. The so-called "English-origin countries" have the lightest regulation. Across regions, East Asian economies regulate the least and Latin American countries the most. For example, in 1999 the cost of firing a full time worker was equivalent to 93 days of wages in Latin America, twice the OECD average of 45 days.

Strict employment regulation has many undesirable side effects. According to the World Bank study, strict employment regulation limits job creation reduces the flexibility of the workforce, constrains R&D investment and investment in technology, and leads to smaller firm size, leaving economies of scale unexploited in manufacturing and in some services. All of these effects contrive to dampen productivity growth. A reduction in productivity is also concluded by Scarpetta (2002) who finds that employment protection legislation seems to hinder productivity, especially when these costs are not offset by lower wages and/or internal training thereby inducing sub-optimal adjustments of the workforce to technology changes and less incentive to innovate. In addition, the World Bank study finds that employment regulation is especially a burden on businesses in many developing countries, limiting the opportunities for disadvantaged groups to come out of poverty, and excessive regulation being associated with higher unemployment, especially so for youth and women.

Strict regulation also affects innovation and technology adoption according to the Scarpetta study which finds that a firm's likelihood to innovate and adopt new technologies seems to depend on the joint configurations of: i) product market regulations that influence competition amongst incumbents and the entry of new firms; and ii) labour market arrangements affecting the extent to which firms use either the external or internal labour market to adapt the production process to evolving technologies.

The World Bank study also addresses another issue which is not addressed in this paper - the need for entrepreneurs to be able to enforce contracts, and reviews the types of reform of contract enforcement which have proven to be successful.

Table 1: Frequency of entry procedures across countries

| Purpose of procedure | Percent of countries |
|-----------------------------|-----------------------------|
| Tax registration | 93 |
| Labour registration | 87 |
| Administrative registration | 76 |
| Bank deposit | 68 |
| Notarisation | 63 |
| Health benefits | 62 |
| Notice in newspaper | 36 |
| Company seal | 38 |
| Court registration | 32 |
| Chamber of commerce | 27 |
| Statistical Office | 17 |
| Environment | 12 |

Source: World Bank (2003)

Further, recent empirical findings of OECD research (OECD, 2003b, 2003c and Annex A) covering almost 8 000 businesses showed that administrative compliance costs represent around 4% of Business Sector GDP in the countries surveyed, and the survey confirmed the well-known inverse relationship between the compliance cost per employee and the size of the company indicating that regulatory costs have an increasingly disproportionate impact on smaller companies. This is due to numerous interrelated factors and particularly, economies of scale and scope when managing a firm. The data suggest that a threshold exists at around 20 employees after which the cost per employee stabilises. The findings also draw attention to the role of exit barriers.

As mentioned above, recent work by OECD's Working Party for Regulatory Management and Reform highlights the administrative compliance costs imposed on businesses. Such burdens fall disproportionately on SMEs. In response, governments have launched a variety of programmes to simplify administrative regulations in general, often to reduce burdens for SME's in particular. Examples of these tools and practices include small business impact statements, consultation mechanisms, sunset clauses, time-limits, plain-language drafting, compliance assistance, "tiering" of regulations, targeted compliance cost surveys, one-stop shops, and special guidance material to SMEs. Special agencies and organisational units have also been created to oversee and advocate such programmes.

Experiences from OECD countries and the findings of the World Bank study suggest that strategies to reduce administrative burdens – with a particular focus on SMEs – could include considerations of the initiatives listed below:

- Institutionalise SME concerns by establishing permanent or ad hoc governments units mandated to represent SME views in the regulatory process.

- Employ requirements for regulatory agencies to prepare Small Business Impact Statements during the regulatory process.
- Consult small business on proposals with an effect on small businesses prior to formulating policy and producing Regulatory Impact Assessments (RIAs).
- Scale and calibrate administrative regulations when deemed necessary.
- Consider setting specific time-limits for administrative decision-making.
- Ensure plain-language drafting and specific compliance guidance for SMEs.
- Establish a central registry of administrative procedures and licences and initiate a comprehensive review (using RIAs) to determine how to reduce burdens.
- Build a system for measuring administrative burdens.
- Establish one-stop shops for regulatory information and transactions.
- Ensure that IT is widely available for SMEs to take advantage of e-government tools.

Box 1. Which countries regulate business entry the most?

Extract from *“Doing Business in 2004”*, a publication of the World Bank (2003)

“When the countries are divided into groups according to their income per capita, the high income countries have the smallest number of procedures, with a median of 7. They are followed by the upper-middle income group with a median of 10 procedures. Lower-middle income countries have the highest number of procedures, around 12 while the poorest countries have a median of 11. The time required to register a company is the shortest in the richest countries, at less than one month. Although the registration process takes around the same amount of time – 50 days – in upper middle and lower middle income countries, it is significantly higher in poorer countries, where the median number of days is 63. In contrast, the cost of starting a business accounts for less than 10% of income per capita in the high income group, and 120 % in low-income countries.

Regional differences are also significant. Latin American governments regulate business entry the most in terms of procedures and time; they are followed by African and Middle Eastern governments. OECD governments regulate the least. The cost of registration is extremely high in African countries – at around 190% of per capita income. Similarly, the minimum capital requirements – with a median of more than 700% of per capita income – are much higher in the Middle East and North Africa than in any other region.

Strong patterns emerge by legal origin. Nordic countries have the smallest number of procedures- a median of 5, the shortest time, at 21 days, and the lowest cost, at less than 1% of per capita income. Countries in the French civil laws tradition take the longest time and have the most procedures and highest cost*. Countries in the German tradition have the largest capital requirement, more than 100% of income per capita, whereas the median capital requirement for English-origin countries is zero.”

* It is noteworthy that legislation was passed in France in 2004 involving simplification of the regulatory and administrative burden affecting firm creation.

Needless to say, special initiatives to reduce burdens and support regulatory compliance of SMEs should be balanced against other concerns. When establishing tools and institutional arrangements dedicated to support SME interests, risks of capture by special interests increase. “Positive discrimination” of SMEs may also have dynamic drawbacks by providing SMEs with incentives not to grow beyond thresholds qualifying for special support or to break up strategically as soon as the threshold is passed.

Experience shows that administrative simplification and SME-facilitating initiatives can help mobilise support for reform by promising and achieving highly visible results within a short period of time.

However, administrative simplification policies might divert attention away from deeper and more fundamental regulatory quality programmes. The best basis for developing and prioritising administrative simplification is most likely to occur where these efforts are integrated into a broader regulatory quality agenda. Administrative simplification policies should be an on-going process in which both old and new regulations are continuously revised and simplified.

Building an entrepreneurial society: the role of education and training

Culture is an important determinant of career preferences and helps shape attitudes to risk-taking and reward. Significant differences in entrepreneurial attitudes can exist among countries, and there is evidence that cultural characteristics have an impact on entrepreneurial activity, as recent research by the European Commission has found. A whole range of cultural factors can affect an individual's willingness to start or grow a business. Some of these factors, such as "fear of failure" may be deep-rooted, and others such as the attitude to enterprise, can be instilled in people from an early age. There is awareness that the image of entrepreneurs as positive role models has never been as strong in Europe as in the United States. In a recent study highlighting the particular case of Spain, it was pointed out that a lack of a supportive attitude on the part of Spanish society had been one of the obstacles for starting up a business in Spain although a gradual welcome change in attitudes was underway towards a greater acceptance of entrepreneurs¹⁵. In Japan, it may frequently be claimed that starting up in business goes against the grain of the Japanese character¹⁶. However, this is shown to be far from the reality (see Annex B) where many Japanese are shown to be interested in starting a business. Governments have a role to play, via the educational system, in fostering entrepreneurial attitudes and behaviour. Appropriate training policies (providing business management skills) are also necessary to help entrepreneurs and would-be entrepreneurs, including the unemployed, to adapt to the changing business environment, enable them to adopt new technologies, seize business opportunities, and meet the challenges of the global economy. The key role of lifelong learning in meeting these challenges is gaining recognition.

In acknowledgement of the economic and social contribution of entrepreneurship, cultivating an entrepreneurial culture and fostering entrepreneurship values and spirit for building an entrepreneurial society have moved high on government agendas. However, because fostering entrepreneurship, as a social-economic institution, is very different from what is required in designing and implementing other economic policies, governments are faced with a new challenge here. A feature of the Finnish Government's *Entrepreneurship Project* was their involvement and cooperation in this project of a large number of concerned ministries – 9 ministries, as well as the Association of Finnish Local and Regional Authorities.

For encouraging the enterprise spirit it is acknowledged that a cultural aspect needs to be taken into account, and for which education and training in entrepreneurship can make a significant contribution. In European countries, entrepreneurship is gaining wide recognition as a basic skill to be encouraged and developed throughout the educational and training systems, and through lifelong learning. The European Commission's *Best Project*, as an effort to identify the best initiatives across Europe that aim to promote the teaching of entrepreneurship in the education systems at all levels, illustrates this interest. One task of the *Best Project* expert group was to agree on a common definition of "entrepreneurship teaching". There was a general recognition that the concept would embody two distinct elements: i) a broader concept of education for entrepreneurial attitudes and skills which involves developing certain personal qualities and is not directly focused on the creation of new businesses; and ii) a more specific concept of training on how

¹⁵ Unpublished paper presented by the Spanish Delegation to the OECD Budapest "Workshop on Entrepreneurship: Strategic Issues and Policies", 8-10 September 2003.

¹⁶ Japan Small Business Research Institute & Ministry of Economy, Trade and Industry (2003).

to create a business. Likewise, the Japanese Government is actively promoting the goal of a more entrepreneurial society via various educational and training initiatives.

Box 2. Examples of Education and Training Policies in support of Entrepreneurship in European Countries

In **Spain**, educational authorities, in a reform of the educational system, are seeking to imbue pupils of all ages with the skills and capacities that go with fostering of the entrepreneurial spirit. The 2002-3 reform aims to integrate, as a spinal column, throughout all stages of education, the qualities inherent to the entrepreneurial spirit, as appropriate to the different age groups. This reform applies to the entire national territory. In addition, certain of the autonomous communities are preparing additional optional subjects. For example, the Asturias have introduced the "Young European Company" and the region Castilla y Leon is also planning to introduce this option into the curriculum for the school year 2005-6. With regard to vocational training, co-operation agreements have been established with the business community in order to guarantee better training and provide greater possibilities of employment. Beyond the formal education dimension, the objective is that the working population will continue to receive training in the enterprises in which they work and the recent legislation favours continuous training in SMEs and for the self-employed.

In the **Netherlands**, the creation of a special Commission on "Entrepreneurship and education" (from primary to university level) aims to promote pilot projects and to collect good examples that can easily be copied by other educational institutions. Financial support is provided by the Ministry of Economic Affairs for the development of learning methods and materials, and for other activities (such as seminars, teachers training etc.) The idea is that central government should not impose, but facilitate).

Although the United States has a longer history in, and more widely diffused education in entrepreneurship, than European or Asian countries, it took 30 years for the field of entrepreneurship to gain legitimacy in the academic community. Fifteen years ago, entrepreneurship courses could only be found in a handful of schools in the United States, whereas currently, more than 1 500 colleges and universities offer some form of entrepreneurship training – a trend that started in the early 1990s and continues to flourish. Interest in entrepreneurship education has now spread to non-business disciplines, applying to students in engineering, life sciences and the liberal arts.

Education and training in entrepreneurship can have two types of effects. Firstly, they can have considerable impact on the performance of entrepreneurs, helping them to augment their firm's survival chances, and to a lesser extent, increase profitability. A Kauffman Center study (Charney and Libecap, 2000) finds that education in entrepreneurship increases the likelihood of start-ups, and self-employment, and enhances the economic reward and self-satisfaction of entrepreneurial individuals. The second effect, although difficult to measure, concerns the longer term impacts that education in entrepreneurship may have on the entrepreneurial spirit and on entrepreneurial attitudes. In particular, compared to other business school alumni, entrepreneurship graduates:

- Are three times more likely to start new businesses.
- Are three times more likely to be self-employed.
- Have annual incomes that are 27% higher and own 62% more assets.
- Are more satisfied with their jobs.

The Kauffman study also found that on average, small firms employing entrepreneurship graduates had greater sales and employment growth than those that employ non-entrepreneurship graduates. In addition, entrepreneurship graduates also seem to gravitate toward high technology companies. The study found that entrepreneurship graduates either founded or worked for high-technology firms in greater numbers than other business school alumni. Additionally, they are more involved in new product development and research and development activities, and work with products having shorter life spans.

In spite of the recent growth in attention given by national governments and by international fora, to the key role of education and training in entrepreneurship, and the numerous initiatives and programmes

that have been launched in almost every country (see Annex B for more detail), entrepreneurship education and training are nevertheless characterised by a number of problems and shortcomings, which policymakers might address. These shortcomings include:

- Fostering entrepreneurship through training and education is not sufficiently integrated into long term economic strategy and planning;
- Entrepreneurship is neither integrated into the curriculum nor part of a coherent framework, resulting in a narrow impact on limited numbers of students;
- Lack of public funding for entrepreneurship as an academic discipline has resulted in a limited teaching and research capability, and consequently, limitations for expanding entrepreneurship education;
- There is a need to improve co-ordination among government agencies in designing and implementing policies for promoting entrepreneurship through co-coordinated actions;
- There is still a low degree of acceptance (by policymakers, practitioners, and academics, alike) of the broader concept of education for entrepreneurial attitude and spirit as opposed to education and training for entrepreneurial skills (business skills for SMEs);
- Indicators and quantitative measures, and programme evaluations are still very limited.

In light of the above, government attention to issues of education and training for entrepreneurship could focus on:

- i) the integration of entrepreneurial subjects throughout formal educational systems, in a coherent and systematic way, for teaching entrepreneurial skills, and for fostering an entrepreneurial society;
- ii) the promotion of various forms of public and private partnership, from internship arrangements to private financing, between public educational and research institutions and the private sector, especially SMEs;
- iii) increases in public funding for teacher training, and for the development of curricula and programmes for entrepreneurship;
- iv) improved co-ordination between different government bodies involved in promoting entrepreneurship;
- v) the development of indicators, and programme evaluation.

Fostering the creation and development of enterprises: the local dimension

Entrepreneurship and SME policies have an important local dimension. Indeed, facilitating increasing rates of enterprise creation is now an almost universal concern for local authorities for accelerating development in disadvantaged localities. Countless programmes have been implemented with the aim of reducing joblessness, providing a social and economic alternative to chronic unemployment, and raising standards of living in distressed localities (OECD, 2003a). Fostering entrepreneurship is also of course considered to be a valuable economic development instrument for more prosperous localities. The creation of new firms can procure a range of benefits affecting local economic development, including: employment and incomes growth, with indirect employment effects operating over time; increases in tax revenue, although of uncertain and possibly small magnitude; enhanced provision of services for local consumers and businesses, with consequent increases in local income retention; and difficult-to-quantify but possibly important demonstration and motivational effects.

Rates of enterprise creation can differ markedly across regions within OECD countries (OECD, 2003a). Rapidly growing regions usually have high rates of enterprise start-up. At the local level there appears to be a broad association between incomes and entrepreneurship, although this relationship is not straightforward. Areas of significant deprivation can also experience high rates of firm creation. Determinants of rates of enterprise creation across regions include demographics, unemployment, wealth, the educational and occupational profile of the workforce, the prevalence of small firms, the extent of owner-occupied housing, infrastructure endowment, and a region's history. A set of related constraints can impede entrepreneurship in deprived localities. These obstacles may influence both the extent and form of entrepreneurial activity and also affect their chances of survival.

Among the impediments to entrepreneurship to be found in differing combinations in deprived communities are the following: limited social and business networks; low levels of effective demand in the local economy; constraints in access to finance; a lack of work experience and skills and a lack of role models; cultural obstacles, including linguistic barriers and a lack of affinity with mainstream institutions; the phenomenon of sectoral clustering; problems of transition from reliance on benefits; and inappropriate government regulation. While these obstacles are not exclusive to deprived localities, their prevalence, the likelihood that they will occur simultaneously, and their severity, are often greater in poorer communities.

In the context of the local dimension, mention should be made of the role that *enterprise clusters* can play for the promotion of entrepreneurship. Clustering is a reality in most countries and cluster development initiatives have been adopted by developed and developing economies alike, and applied to wealthy and lagging regions. According to one estimate for the United States, there were some 380 clusters (in the mid-nineties) operating across a broad spectrum in service and manufacturing and together they accounted for 57% of the nation's workforce and produced 61% of the country's output (see Rosenfeld, 1996). Aside from the recognised benefits in terms of productivity, innovativeness and competitive performance of firms, clustering can also lead to high rates of enterprise start-up¹⁷. There is often a high degree of vertical mobility in the local labour market, with workers frequently aspiring to become owners of SMEs themselves. The inter-firm specialisation that clusters can permit may lead to a low degree of vertical integration among firms, lowering barriers to entry and creating a fertile environment for enterprise creation.

There are a number of key policy considerations for local and regional governments for the promotion of entrepreneurship and business development. Among the initiatives finding favour with local and regional policy makers are: business advisory schemes, business incubation facilities and services; training, education and awareness programmes, angel networks, micro-finance programmes, and fiscal incentives, some of which may be considered in a context of clustering. The available research findings with respect to entrepreneurship promotion at the local and regional levels provide a number of conclusions, among which the following figure prominently:

- i) Support for the unemployed to enter self-employment can be cost-effective if targeted to the appropriate section of unemployed.
- ii) The promotion of entrepreneurship cannot be considered to be a solution to social exclusion for large numbers of individuals, affected by multiple forms of distress.
- iii) Pro-entrepreneurship policies require extended time horizons, and are unlikely to yield major benefits in the short run.

¹⁷ Note that a separate background report "Networks, Partnerships and Clusters: Opportunities and Challenges for Innovative SMEs in a Global Economy" has been prepared.

- iv) Competition generated by start-up firms can result in displacement effects (loss of output and/or employment among existing enterprises), in those types of businesses prevalent in poor localities.
- v) Mainstream support services should be adapted to the requirements of target groups.
- vi) Access to training services and new communications technologies is important.
- vii) There is a need for proper evaluation and monitoring of programmes.

CONCLUDING REMARKS

The empirical evidence outlined above and in Annex A and the framework discussed in the last section and also in Annex C can be brought together to examine the implications for entrepreneurship policy. Governments can use entrepreneurship policy to achieve any one of three main policy objectives: job creation; poverty alleviation; and competitiveness.

To achieve these objectives, governments have three basic strategies:

- Increase the size and/or quality of the pool of nascent or aspiring entrepreneurs as a means of increasing net start ups.
- Encourage the entrepreneurial expansion of existing SMEs or the spinning off of new ventures.
- Smoothen the exit of entrepreneurs and SMEs that are really not sustainable or competitive.

There are many different ways in which these three basic strategies can be implemented. For example, the pool of potential and aspiring entrepreneurs can be increased via immigration, entrepreneurship courses in schools, tax and regulatory changes and simplification etc. Similarly, smoothing the exit of unsustainable uncompetitive SMEs may be addressed by local readjustment assistance packages, retraining, changing attitudes to failure, reforming bankruptcy laws, and so on.

However, underlying the way that all policy options can be implemented is to change the business environment to be more conducive to entrepreneurial activity. Different policy outcomes may require different entrepreneurial business environments (EBE), recognising the existence of different types of entrepreneurs in terms of their experience and propensity to deal with risk and uncertainty. An EBE suited ideally to "heroes" is not likely to be the same as an EBE ideally suited to micro lifestyle businesses.

Thus there are some potential trade offs between the main policy outcomes where entrepreneurship policy can have an effect. For example, job creation and poverty alleviation may require a trade off with improved competitiveness and productivity, and the trade-off decision (which types of EBEs should be given priority) is essentially one of political compromise. To make that decision in an informed manner, various stakeholders to the decision need a framework and empirical evidence of what the implications are.

For example, the EBE which best facilitates *job creation* may be one which best facilitates high growth start up and expansion from small, to medium or large, *or* which best facilitates lifestyle start up and expansion, *or* which best facilitates micro start up and expansion. Any one of these three business environments will help to create jobs, and a government seeking to use the entrepreneurial engine to create jobs can approach the problem in different ways – *there is no one ideal way to do this, because it will depend on circumstances and government priorities*. All of this comes down to compromises, and to make the appropriate decisions, political leaders and government officials need a clearer idea of the trade offs and circumstances in which they operate *vis à vis* the entrepreneurial engine.

A number of implications that can be drawn are that:

- **Governments seeking to pursue job creation, improved growth and competitiveness, and poverty alleviation as part of broader social and economic objectives need to give entrepreneurship policy a high priority.** Entrepreneurs have the potential to make a significant contribution directly to these three main policy outcomes. Entrepreneurial activity strongly correlates with these target outcomes, but there are trade offs between them that need to be taken into account.
- **There is no ideal "Entrepreneurial Business Environment" applicable at all times and in all places which is optimal for all types of entrepreneurs.** There is no "one size fits all" in entrepreneurship policy. Different countries will have different priorities. To develop appropriate policy strategies and initiatives policy makers need to make decisions which are essentially political compromises. Trade-offs will be based on a range of considerations, which includes their objectives, the profile of existing (and desired) entrepreneurs in their economy, and the business environment. To make that decision in an informed manner, various stakeholders to the decision need a framework and empirical evidence of what the implications are.
- **The most effective Entrepreneurial Policy seeks to create a conducive "Entrepreneurial Business Environment" or EBE.** The entrepreneurial business environment (EBE) most suited to one policy outcome will not necessarily be that most suited to other policy outcomes, as explained above. This is primarily because there are different types of entrepreneurs, in terms of their experience and propensity to deal with risk and uncertainty. An EBE suited ideally to "heroes" is not likely to be the same as an EBE ideally suited to micro lifestyle businesses. A government's entrepreneurial policy needs to not only reflect and be adapted to its desired policy objectives and the trade offs between them, but also to the profile of prevailing entrepreneurs.
- **There is no necessary direct relationship between individual factors in the business environment, and the level of entrepreneurial activity.** Policy which seeks to address the factor "finance" in isolation may not lead to any discernible increase or improvement in entrepreneurial activity. It is not so much the individual environmental factors that affect the entrepreneur, but the package or profile of factors. A package of factors, shaped by policy, is only as strong as its weakest link. Increasing an individual factor, such as the level and availability of finance, will not necessarily lead to any increase in entrepreneurial activity if other factors (such as education, regulation or corruption) are constraints. Neither will increasing the amount of entrepreneurship education, or reducing regulations, *per se*, increase the level of entrepreneurial activity, if finance is a constraint. Some factors are thus step functions rather than just correlates. It is the whole package, or portfolio, or profile of environmental factors that is important to the level of entrepreneurial activity. These packages tend to be time and place specific, and specific to specific types of entrepreneur (lifestyle, growth oriented etc.). The implication is that governments will get a higher return from limited resources by taking steps to identify the "weakest links" in the packages of EBE factors.
- **Governments need to have much better capability for monitoring their Entrepreneur Profile, Entrepreneur Activity, and Entrepreneurial Business Environment.** This is because these weak links are relative to various types of entrepreneurs, relative to policy

priorities and relative to competing EBEs provided by other governments in the global economy. Using the COTE framework for policy formulation (a framework covering a number of policy aspects and dimensions, notably clarity and coherence, objectives, targets etc.) as proposed in the companion background report on evaluation, can assist government efforts in this respect.

- **Much of the infrastructure which underlies the EBE is provided by the private sector.** It includes financial markets and services, telecommunications, educational and advisory services, incubators and hatcheries, technology research, dispute resolution means, markets for tangible and intangible property rights etc. There is a need for public-private collaboration to ensure that firms in the private sector are not unnecessarily impeded, and where appropriate, are encouraged to develop suitable products and services geared to the needs of entrepreneurial start up and growth. This suggests that governments develop models of private sector collaboration and consortia appropriate to their country.

- **At a national and local level there is an increasing need for all governments to review their own strategies for encouraging entrepreneurship, relative to the strategies adopted in other locations.** At an international strategic level, there is a need to adopt a strategic approach to coordinating entrepreneurship policy so as to provide a better international entrepreneurial business environment. This could, for example, require the identification of a list of indicators of a conducive EBE in the most advanced “entrepreneurial” economies. That is the definition of a “holy grail” profile for all developed economies may be sought. In doing this maximum targets are set, even though they may be very difficult or impossible for some governments to achieve in a politically realistic timeframe. In a global economy this approach has some merit, because it sets a target or a “lighthouse” to guide policy in the strategic sense over the longer term.

ANNEX A

REDUCING REGULATORY AND ADMINISTRATIVE BURDENS

Introduction

This annex presents an overview of recent, SME-relevant findings of work carried out under the auspices of OECD's Working Party for Regulatory Management and Reform. It focuses on administrative compliance costs incurred by companies when complying with regulations, and the strategies employed by governments to reduce these costs.¹⁸

Administrative regulations are important tools to support public policies in many areas such as taxation, safety and environmental protection. Administrative regulations can create benefits for enterprises by setting market frameworks in which commercial transactions can take place in a pro-competitive and low cost environment. There is a risk, however, that administrative regulations can impede innovation or create unnecessary barriers to trade, investment and economic efficiency, and even threaten the legitimacy of the regulation. The cumulative effect of many regulations and formalities from multiple institutions and layers of government slows down business responsiveness, diverts resources away from productive investments, hampers entry into markets, reduces innovation and job creation, and generally discourages entrepreneurship.

These problems are particularly severe for SMEs. They have less managerial depth, lower turnover to absorb increases in fixed costs and fewer financial resources. In a competitive environment, SMEs rely more on developing the key capabilities that drive long-term success – the ability to innovate, to maximise operating efficiency and to adapt to change over time.

Section 2 introduces a set of empirical findings illustrating SMEs' views on administrative burdens and regulations. Section 3 reviews organisational approaches and simplification tools used in OECD countries to reduce administrative burdens for business in general and SMEs in particular. South East Europe being the case in point, Section 4 explores how non-OECD countries can benefit from these experiences. Section 5 introduces a set of tentative policy implications, which may feed into the ongoing considerations of a set of principles for SME policies in preparation of the 2004 Istanbul Ministerial SME Conference.

¹⁸

Administrative compliance costs include all the time and resources spent by owners, managers, staff or hired experts to understand regulations, collect, plan, process, report and retain data, and fill in forms required by governments. They include the administration of taxes, but not the actual amount of money paid as tax. It does not include the non-administrative compliance costs, for instance capital costs incurred by business such as the investment and equipment needed to comply. It focuses on existing companies and it therefore does not capture the administrative compliance costs associated with starting a business, which involves a host of additional requirements.

SMEs' views on administrative regulations and costs

An OECD survey published in 2001 covering almost 8 000 businesses provides insight into SMEs' views on administrative regulations and costs.¹⁹ The survey showed that administrative compliance costs represent around 4% of Business Sector GDP in the countries surveyed. Box A.1 below illustrates how some of these costs are distributed among companies and policy areas. The survey confirmed the inverse relationship between the compliance cost per employee and the size of the company indicating that regulatory costs have an increasingly disproportionate impact on smaller companies (Figure A.1). This is a well-described phenomenon due to numerous interrelated factors and particularly due to economies of scale and scope when managing a firm. The data suggest that a threshold exists at around 20 employees after which the cost per employee stabilised. This is further illustrated by the number of requests made to government authorities. Businesses participating in the survey informed that they asked for an average of eight authorisations or decisions per year. However, when adjusted for the number of employees, small SMEs make approximately four times the number of requests per employee than medium-sized SMEs and eight times more than large SMEs, *cf.* Figure A.2).

The survey showed some differences in administrative compliance costs between sectors, *cf.* Figure A.3. Professional services (business service companies) and services with environmental impact (such as transport and public infrastructure companies) have higher annual costs per employee than the manufacturing sector. The majority of the administrative compliance costs is spent on complying with tax and employment regulations, while the amount spent complying with environmental regulations was lower (though these costs are growing rapidly, *cf.* Figure A.4).

The survey also examined SMEs views on their contact with government agencies (Box A.2). Overall, SMEs are more critical of the quality of tax and employment regulations than of the quality of environmental regulations (Figure A.5). SMEs criticise tax and employment regulations because they are not flexible enough to be implemented efficiently by companies, do not achieve their objectives as simply as possible, are not easy to understand, and because changes are not predictable. In addition, SMEs were asked to assess the quality of administration when seeking information (Figure A.6), and when seeking decisions or permissions from government officials (Figure A.7). Although not evaluated on the same criteria, the general picture is that SMEs are more critical of their contacts with government offices to obtain decisions than they are of their contacts to obtain information. Specifically, they are critical of the lack of consistency and predictability of decisions (over time and among similar companies), and of the accountability of the administrator in charge. Surprisingly, the slowness of government decision-making and the lack of definitive answers from officials are not considered so unfavourably.

¹⁹ OECD (2001b) The publication *Businesses' Views on Red Tape* builds on a multi-country business survey implemented between April 1998 and March 1999 covering almost 8 000 SMEs in 11 countries: Australia, Austria, Belgium, Finland, Iceland, Mexico, New Zealand, Norway, Portugal, Spain and Sweden. Three standardised questionnaires were prepared by the OECD on tax, employment and environmental protection regulations. Each survey measured enterprises' perceptions of the quality of the regulations and formalities, perceptions of the quality of the regulatory administration, and estimates of the administrative costs of complying with the regulations and formalities.

Box A.1: SMEs' administrative compliance costs

Figure A.1. Annual administrative costs per employee

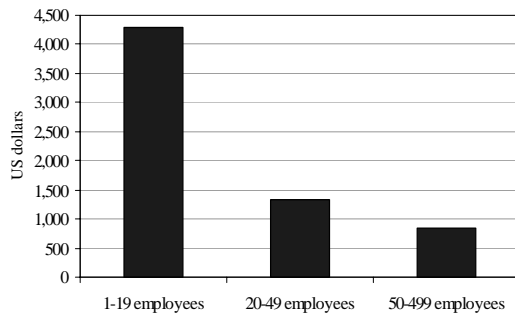


Figure A. 2. Annual number of requests for permissions per employee

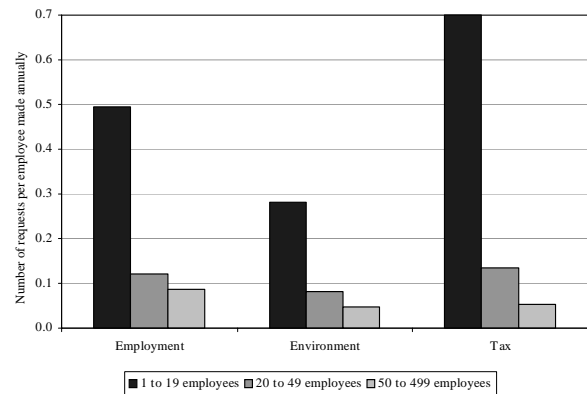


Figure A.3. Annual administrative costs per employee by economic sector

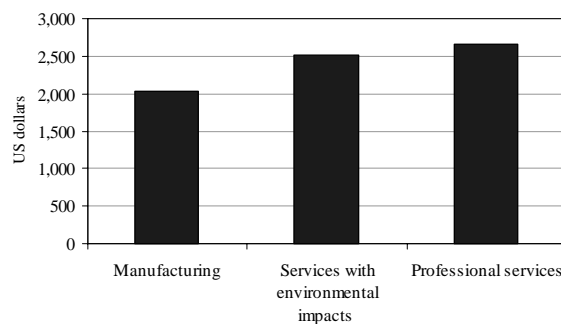
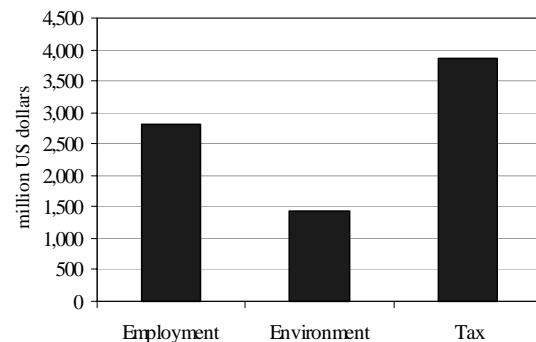


Figure A.4. Aggregate annual administrative costs



Source: OECD (2001), Businesses' Views on Red Tape.

The majority of companies (around 60%) reported that administrative compliance costs increased over the period 1998-1999. The main reason identified by companies for increases in tax and employment administrative compliance costs is the increase in the complexity of existing regulations. For environmental regulations, the introduction of new regulations and an increase in regulatory compliance, as well as increasing complexity, are seen as important drivers of increased compliance costs. It is interesting to note that the external provision of regulatory compliance services to businesses (*e.g.* accountants, lawyers, etc.) has become an economic activity in its own right. Whilst such activity may stimulate growth and create jobs, there may be more productive ways in which companies' resources could be invested.

Box A.2: SMEs views on their contact with government agencies
 (% of respondents disagreeing or strongly disagreeing)

Figure A. 5 Quality of regulations

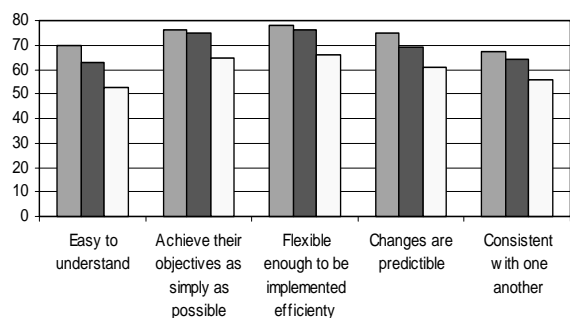


Figure A. 6. Effectiveness of information on regulations

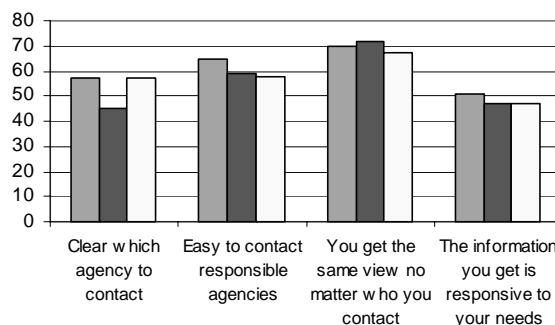


Figure A.7. Obtaining decisions or permissions

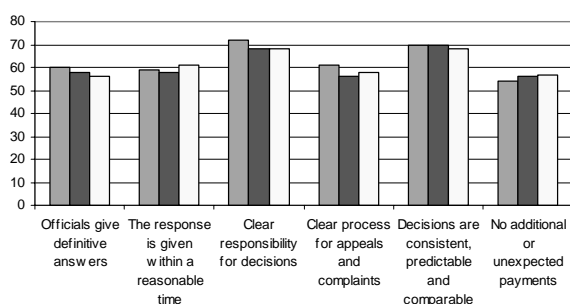
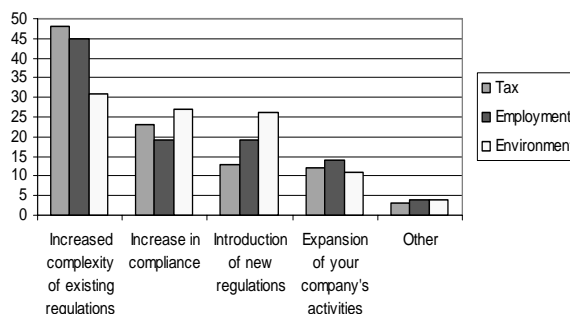


Figure A.8. Reasons for increased compliance costs



Source: OECD (2001), Businesses' Views on Red Tape.

Government responses: Tools and strategies to reduce administrative burdens

Governments are increasingly aware of the risk that administrative regulations may slow down business responsiveness and discourage entrepreneurship. In response to these challenges, steps are being taken to improve the quality of regulations and reduce compliance costs – sometimes including particular strategies targeting the regulatory environment facing SMEs (OECD, 2003c).

Organisational approaches: Institutionalising concerns for regulatory effects on SME

There is considerable variety in the organisational models countries use to pursue administrative simplification policies. This variety reflects the different political and administrative structures – and the underlying political cultures – as well as different conceptions of the nature of the administrative

simplification task. In general, organisational approaches used to advance administrative simplification policies can be classified in four different categories:

- “Single Purpose Entities” where the promotion of specific sub-elements of administrative simplification policies – *i.e.* plain language or burden reduction for special groups (*e.g.* SMEs) – are designated to an agency or unit with this task as its sole objective.
- “Administrative Simplification Agencies” where a special government agency has the promotion of administrative simplification policies as its sole or primary objective.
- “Regulatory Reform Agencies” where the promotion of administrative simplification policies is designated to agencies responsible for broader regulatory quality management issues.
- “External Committees” refers to committees established by the government and composes a majority of non-governmental representatives such as academia and business organisation with the purpose of co-ordinating, promoting, proposing or implementing administrative simplifications.

In many OECD countries, “Single Purpose Entities” have been established to assist SMEs in complying with administrative regulations. Examples of such entities are discussed next, in particular permanent government units and ad-hoc committees.

Permanent government units safeguarding SME concerns in the regulatory process

In the United Kingdom, the Small Business Service (SBS) was established in 2000 to provide a voice for small firms within the government, and to simplify and improve the quality and coherence of support to small firms. SBS has a strong institutionalised position in the regulatory process, for example the right to have its views recorded in Regulatory Impact Analysis (RIA) in a wording of its own choice. As another example, the US Small Business Administration (SBA) was established in 1953 to provide special assistance to small businesses in receiving government grants and loans. Since then, the SBA has engaged in numerous activities intended to simplify small business compliance with regulatory requirements.

Ad-hoc Committees

The key advantage of the use of a short-term taskforce is that it can provide a high profile and focused response to a political priority. A standing taskforce model highlights the government’s commitment to administrative simplification and it provides a focus for attracting reform ideas. It may also act to educate the bureaucracy on private sector concerns and alternative approaches to regulation and on methods of implementing reform initiatives in complex or politically difficult areas. Finally, it assists in educating private sector bodies on the difficulties and issues involved in implementing administrative simplification measures. This can create a broader understanding of the nature and dynamics of government reform processes. However, the ad hoc nature of a body can pose difficulties in ensuring implementation and follow-up.

In 1996, Australia established a Small Business Deregulation Taskforce as a vehicle for a one-off reform. Its six members were drawn from the business sector, supported by a senior officer, and were mainly from small business background. The Taskforce was given specific terms of reference on its establishment, with its task being to design a programme to substantially reduce the regulatory and administrative burdens on business.

Ex-ante approaches: Improving the quality of new regulations

In addition to the above mentioned institutional approaches, some countries have taken a more procedurally oriented path to ensure that new and amended regulatory requirements are, from the outset, sensitive to small business compliance issues.

Regulatory Impact Analysis with special obligations to consider effects on SMEs

Use of Regulatory Impact Analyses (RIAs) is now widespread among OECD countries. RIA is a decision tool to systematically and consistently examine selected potential effects of government's regulatory activities, and a way of communicating the information to decision-makers. In this way, RIA can also constitute a systematic mean of ensuring that consideration is given to administrative burden issues during the regulatory development process. RIAs can also be targeted towards specific subgroups, for example, to require agencies to prepare special impact statements for proposed regulations that affect small businesses. "Small Business Impact Statements" are often required to contain, among other things, a description of regulatory alternatives that can accomplish the stated objectives while minimising any significant economic impacts of the proposed rule on small businesses.

In the United Kingdom, new regulations are subject to a RIA, which includes a Small Business Litmus Test to ensure that the burden on smaller enterprises will not be disproportionate. In the United States, many States are adopting "regulatory flexibility" laws for small businesses. State laws similar to the federal Regulatory Flexibility Act require regulators to determine the impact of proposed rules on small business or periodically consider the impact of existing rules.

Australian Government agencies are required to prepare Regulation Impact Statements, which include an assessment of the impact of each option on small business compliance costs and the paper work burden. This requirement applies to all reviews of existing legislation, proposed new or amended legislation as well as treaties involving regulation that will impact directly or indirectly on business. Where new policy proposals will have an impact on small business, Australian government agencies are also required to consult with the Office of Small Business. State and local governments have their own regulatory impact assessment processes.

Consultation mechanisms

Another approach, which can be adopted in conjunction with the impact statements and the institutional approach mentioned above, is to require specific consultative approaches to be undertaken in order to ensure adequate representation of the views of small business. Consultations have the benefit of verifying government estimates of the size of the burdens involved, as well as providing a forum for alternative proposals to be discussed, thus helping to ensure that regulatory costs are the minimum necessary to achieve regulatory objectives.

The United Kingdom Regulation and Small Business Policy Directorate has established customer consultation mechanisms that seek evidence for regulatory burdens and priorities for their reform, in partnership with small businesses and their representatives, the Better Regulation Task Force, the Regulatory Impact Unit at the Cabinet Office, and regulatory departments and agencies. The Directorate also works closely with a network of Local Business Partnerships, which complements the advisory role of Business Links by providing a forum for discussion on a range of regulatory and enforcement issues.

Special regulatory provisions for SMEs: Scaling and calibrating administrative regulations

Another example of meeting compliance needs of small businesses is through "tiering" of regulations. "Tiering" can be described as the design of regulations to alleviate disproportionate burdens,

ensure that the regulatory solution fits the problem, and make more efficient use of its limited enforcement resources. Even when it is possible to set an appropriate tier, a possible disadvantage is that tiered regulations may provide a disincentive for a firm to grow and, consequently, subject itself to a more stringent standard. The United Kingdom “Think Small First” initiative introduced some flexible exemptions to certain legislative provisions for small businesses, for example providing that (a) companies below five employees were exempted from the stakeholder pension, (b) union recognition was deemed not necessary for companies below 20 employees, and (c) certain accounting standards were made applicable only to firms with more than 50 employees. In the United States, the EPA has tiered 50 different regulations based either on firm size or the amount of pollution released.

Positive discrimination of SMEs

Given the special case of SMEs, the question is to what extent high-quality design of administrative regulations should be more responsive to small business needs. At a theoretical level, the concept of adopting more sophisticated approaches to regulatory design that take better account of both the compliance capacities of different groups and the relative risks posed by them seems to be clearly consistent with principles of regulatory quality, as identified by the OECD. Here, careful implementation is required, as the benefits conferred on SMEs could be outweighed by the costs to society. In addition, concerns have been voiced that some mechanisms, such as “tiering”, may offend against important principles such as the equitable application of the law to all parties. “Positive discrimination” of SMEs may also have dynamic drawbacks by providing SMEs with incentives not to grow beyond thresholds qualifying for special support or to break up strategically as soon as the threshold is passed. However, it is clear that the political will to continue and expand these programmes is strong, while a substantial body of experience with their implementation is beginning to accumulate.

Other tools

Administrative burdens are determined only partially by business and citizens’ direct costs related to collecting required information, filling out forms and dealing with administrators. Costs are also incurred by time delays and uncertainty in the provision of either information or answers to requests. OECD countries therefore apply a range of other ex ante tools to improve the regulatory environment for businesses, e.g. sunseting of regulation, setting time-limits and plain-language drafting. Korea is one of the few countries that use *sunseting* systematically.²⁰ Where regulations “have no clear reason to continuously exist”, their maximum duration is not “in principle” supposed to exceed five years. This is supplemented by a requirement that the duration of regulations should be the minimum needed to achieve their objectives. Where agencies believe that regulations should be extended beyond this time, they must ask the Regulatory Reform Committee to review them, along with RIA and self-assessments as applied to new regulations, at least one year prior to their expiry. However, sunseting may tend to reduce compliance towards the end of the lifespan, and rigorous sunseting runs a real risk of overwhelming RIA review resources.

Setting *time limits* on governments’ case-handling time often leads to reduced administrative costs for businesses. It also has important accountability implications by putting a stronger onus on the authorities to provide businesses with a definite and binding time limit. The use of “silence is consent” or “silence is denial” rules in many cases provides an effective assurance to applicants that they will obtain a timely resolution to their request.

²⁰

While sunseting has traditionally been used to define an ex ante desirable duration period for a given regulation to ensure that regulations are up to date and meet certain standards, sunseting can also be used in an ex post sense to review the existing stock of regulations.

Many OECD countries have undertaken programmes to improve the clarity of their formalities and forms by using *plain language* in all new rule-making documents. Instruction and training sessions have been held on how to make information requirements readable. The advice covers such things as format, headings, paragraphing, use of tables and illustrations, and use of active verbs.

Ex post approaches: Simplifying and communicating existing regulations

Working in an ex post sense means simplifying and communicating existing regulations, providing special assistance and guidance to help SMEs meet their compliance requirements for administrative regulations, and amending the administrative requirements themselves to make them less stringent for small businesses.

Compliance assistance to SMEs

Compliance can be significantly enhanced by preparing comprehensive guidelines and a well defined process to respond to small business inquiries on compliance with administrative regulation requirements. In the United States, legislation requiring specific attention given to the compliance needs of small businesses has been in place since the passage of the Regulatory Flexibility Act in 1980. The Act was strengthened in 1996 with the passage of the Small Business Regulatory Enforcement Fairness Act, which introduced legislated requirements for agencies to take specific actions to assist small businesses in meeting their compliance obligations. These include the production of regulatory compliance guides and other guidance materials, as well as additional consultation requirements.

In support of their requirements to issue guidance on all new legislation impacting on business, the United Kingdom SBS has provided extensive best practice advice to regulators on how to produce guidance which meets the needs of small firms, including the pamphlet *How to Get the Message across – Guidance on Legislation that Affects Small Businesses*.

Another approach to reduce effective compliance burdens through regulatory redesign is to ensure that there is an adequate *notice period* before new legal and regulatory measures come into effect. By providing businesses with a longer period to reach compliance, they are given the opportunity to consider the most cost-effective means of reaching it and to obtain expert advice where necessary. In 2000, the United Kingdom Small Business Service published the *Guidelines on Implementation Periods – Timing of the Issue of Guidance to Business on Compliance with New Legislation*. These guidelines recommended that business should be provided with at least a 12-week preparation period before a regulation comes into force (“implementation periods”). In addition, they recommend that these preparation periods should be further extended in more complex cases, while the time frame should be reduced to below 12 weeks only in exceptional cases.

Measuring administrative burdens

Cutting red tape is firmly on the political agenda in most OECD countries. Despite the high profile, however, governments seldom have a detailed understanding either of the total administrative burdens imposed on businesses, citizens and government itself or of the cost-efficiency of many of the administrative simplification tools applied. Measuring the size of existing burdens can be an important approach to foster political support for the development of a policy on burden reduction. It can also form the basis for evaluating policy initiatives needed to improve and sustain long-lasting government efforts. Many OECD countries have employed survey-based methods, either to measure compliance costs directly or to measure satisfaction with the forms and/or processes used in administrative procedures.

In the Netherlands, the MISTRAL methodology has been developed to measure administrative burdens in three stages: (a) and in-depth analysis during which all “data transfers” between a business and

the authority (*e.g.* a request for a license) are isolated and defined; (b) the time involved in each “data transfer” and the level of the person performing it (professional qualification and hourly wage-rates) are then determined; and (c) the data are computed to produce cost estimates. MISTRAL has been used to quantify administrative compliance costs of different laws and regulations, including evaluation of the information requirements of labour law, annual accounts, corporation tax, wage tax and social premiums, legislation concerning working conditions, and environmental legislation. Burdens are quantified in time as well as in monetary terms.

In 1996, the Australian Small Business Deregulation Taskforce commissioned a national survey of the paperwork burden on small business to guide the preparations of an integrated burden reduction programme. The survey results allowed the calculation of estimates of the total time spent on average by small businesses on administration and compliance activities (estimated at 16 hours per work). In addition, the distribution of the burden between broad regulatory areas was also examined.

Drastic reductions in the time to register a company and online registration have been accomplished in Spain. The “*Nueva Empresa*” (New Enterprise) project launched by the Spanish Directorate-General for SME Policy, includes a legal status for a new type of limited liability company, specifically adapted to very small enterprises. Available since 1 June 2003, it ensures that personal and business assets remain separate. The project includes simplified administrative procedures, a simplified bookkeeping system, as well as an advantageous financial and tax framework. In addition, advice and services will be provided to entrepreneurs through the Information Centre and Business Creation Network (CIRCE), comprising of a network of Advisory and Procedure Initiation Points (PAIT).

An electronic document, the Single Electronic Document (DUE), includes all of the elements for setting up companies under the New Enterprise status. DUE allows for new businesses to be created in 48 hours and considerably reduces the number of forms to be filled in. Businesses can currently be created electronically, by accessing CIRCE’s Electronic Processing System¹⁰⁵, in the pilot autonomous regions of Madrid, Murcia and Valencia. It is foreseen to extend the CIRCE network to the other autonomous regions by signing collaboration agreements with various organisations (Development Agencies, Business Associations, Chambers of Commerce, etc.).

According to information from Spain, the average time taken between the first visit to the PAIT and completion of the electronic process, including prior advice and actual processing, has been 8.53 days (including weekends and public holidays) and the processing time from the appointment with the Notary to registration in the Trade Register has been 57.6 hours (excluding weekends and public holidays). Furthermore, through the personal, non-electronic procedure available since 2 June 2003, 1 181 company name reservation certificates had been issued with 534 companies registering by 23 October 2003. The average time taken between the issue of the company name certificate and the registration of the company in the Provincial Trade Register is 15 days, compared with the 30 to 60 days in the past. According to this information, the Spanish target to reduce start-up time by 50% to 42 days by 2006 seems to have been well exceeded already.

In Belgium, a survey of enterprises’ views of administrative regulations and administrative burdens showed that for the year 2000, enterprises estimated that they were facing government imposed administrative burdens at a size equal to 2.6% of GDP. The survey also showed that nearly 70% of the burdens were borne by small enterprises. The survey invited enterprises to give their views on how governments should prioritise administrative simplification policies. In order of priorities, the answers were: to improve the quality of regulations, to make public services more user-friendly, to develop IT mechanisms and to introduce one-stop shops.

Reviews of existing regulations

Even high quality regulation becomes less effective and appropriate over time, as the economy and society change, and policy learning continues. Perhaps the least developed element of the regulatory policy agenda in OECD countries is the practical and systematic updating of existing regulation to ensure that they continue to meet their intended objectives efficiently and effectively. Regulatory rigidities are enormously costly, increasing the risk of policy failure and slowing technical and organisational innovation. A selection of the many strategies that have been developed and applied include scrap and build, generalised reviews and automatic review mechanisms.

A *scrap and build* review means dissolving and then rebuilding the entire regulatory structure and framework in a selected area. It is a costly and time-consuming review tool. In practice it has proven relatively effective; benefits appear fast, affected parties have time to adapt, vested interests have less opportunity to block change, and reform enjoys higher political profile and commitment. Producing an integrated package of reforms also facilitates prioritisation of reviews for specific sectors and takes into account the interactions of multiple regulations. In *generalised reviews* regulatory bodies review the entire body of their regulations against general criteria such as need and efficiency. Such reviews have often absorbed the energies of governments and delivered only minor results. Generalised reviews have tended to be weakened by exemptions, by lack of priority setting, fragmentation, and by the lack of depth and rigor in the review. *Automatic review processes* are systematic reviews of existing regulations, in which regulations are grouped according to their age, and progressively reviewed against currently used regulatory quality criteria, thus gradually bringing the stock of regulations into conformity with those standards. In this process, unlike sunseting, a rule will continue unless action is taken to eliminate it.

In general, review activity in OECD countries remains too infrequent and too limited. Few reviews are systematically undertaken and have almost invariably been episodic in nature, rather than being integrated into the longer-term policy agenda. In the absence of such standardised approaches, substantial discretion is left with the regulatory agency conducting the review, inconsistencies necessarily result, and quality control cannot be exercised at the whole of government level. In addition, the absence of clear ex ante criteria for the review can potentially lead to regulatory capture.

IT-driven mechanisms: Facilitating access, communication and participation for SMEs

Administrative simplification is increasingly driven by IT mechanisms. IT mechanisms are not only the most important “physical” enabler of burden reduction; they can also facilitate process re-engineering. Bringing together the full range of information requirements, licences and permits required in relation to a given business tend to highlight areas of overlap and/or duplication and point out redundancies. However, the increased use and importance of IT in government-business relations may increase the “digital divide” with some businesses finding it difficult or impossible to access government services provided electronically.

One-stop shops

An important positive assistance to small businesses is the service provided by Web-portals and one-stop shops set up especially to cover the particular needs of small businesses. One-stop shops have the potential to deliver substantial savings in time and costs for users by providing seamless, integrated and easily accessible points of contact. Notwithstanding the fast growth of Internet-based one-stop shops, physical one-stop shops possess qualities, such as providing opportunities for personal advice and face-to-face dialogue, which Web-based one-stop shops cannot offer. In the United States, for example, the SBA created the US Business Advisor, which is a one-stop shop for access to Federal Government information, services and transactions.

Other IT-driven mechanisms

The Internet has also facilitated specific mechanisms for giving advice to small businesses. Interactive, electronic tools can give tailored, understandable advice about how to be in compliance with regulatory requirements. In the United States, for example, the Department of Labor (DOL) has developed 18 “E-law Advisors”, Web-based expert systems that the public can query through menus and routine questions to better understand and comply with the DOL regulations. In the United Kingdom, the SBS is developing an Electronic Regulation Service as part of its National Information and Advice Centre. This service includes online authoritative regulatory guidance, and a new service will guide SMEs to regulatory information tailored to their circumstances. In Turkey, KOSGEB (the Small and Medium Industry Organisation) has been very active in improving information networks such as the Small and Medium Enterprises Common Information Network Project (KOBINET), Internet Contact Points, and a single data base with information on SMEs, shared between all public entities.

Sharing experiences: Administrative simplification in South East European countries

The move from a planned economy to a market economy necessitates a massive reform programme supported at the highest political level. Also, the prospects for EU accession means that most South East European (SEE) countries are in the process of adopting a significant amount of new regulations and amendments over a short period of time. The recently published *Review of Regulatory Governance in South East Europe* (OECD, 2003b) finds that state institutions do not always function effectively, implementation and enforcement of legislation is weak, and a lack of transparency has led to widespread corruption in most of the countries.

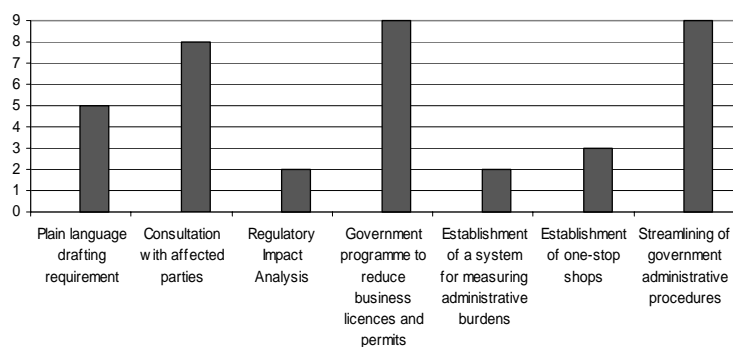
The Review identifies 10 principles of good regulatory governance designed to assist the establishment of a transparent, efficient and accountable regulatory regime supportive of a dynamic business environment. In particular, SEE governments are encouraged to continue their efforts to reduce the regulatory burden and make the rules governing privatisation and business operation more stable, predictable and transparent. Administrative burdens, and in particular business licenses and permits, are among the most important barriers to entrepreneurship and market entry in the region. By allowing non-compliance and grey regulation they nourish unfair competition within the economy and maintain barriers to market access. Rapid and resolute abolition of this type of regulation can bring swift economic gains and build a constituency among stakeholders for further reform.

Administrative simplification policies in South East European countries

Figure A.9 in Box A.3 depicts a selection of institutions and regulatory reform tools applied in the region. Consultation requirements are the most common element although the nature, quality and depth of the procedures differ across the region. However, fewer resources are being invested in improving the quality of the draft proposal before it is sent for consultation (plain language drafting and RIA). All of the countries examined in this report have now initiated programmes focussed on reducing business license and permit requirements, which in most cases has led to the streamlining of government administrative procedures and reallocation of power between government departments and/or levels of governments.

Box A.3: Figure A. 9. Administrative simplification policies in South East Europe

During the transition period, economic reforms often leaped ahead of institution building. SEE countries encounter significant difficulties and risks when trying to design and implement good governance: fragmented political structures, lack of technical expertise, unclear and complicated regulatory procedures, and weak horizontal co-operation and co-ordination (OECD, 2003c).



Even if many of the simplification programmes contain targets for administrative burden reduction, only two of the nine countries have established a system for measuring administrative burdens. In three cases, a result of the administrative simplification initiatives has been the establishment of one-stop shops aimed at assisting business in complying with licenses and permit requirements. In Bulgaria, a pilot one-stop shop project was under preparation and the first resulting offices are expected to open in 2003 in Sofia and Russe. In Moldova, the Chamber of Licensing in Chisinau was established in 2001 as a one-stop shop for issuing licenses. All State Departments, with previous authority in the field of licenses, now forward all data regarding licenses given to economic agents, licensing regulations, and so on to the Chamber. The Chamber must answer applications for licenses in a maximum period of 15 working days from when all documents are presented.

In 2001, Romania established one-stop shops for traders' registration and licensing, obtaining notices, authorisation and/or agreements necessary for traders' activities, and solved problems related to the complicated application procedures, by simplifying registration and licensing procedures, and by reducing the registration time limit, taxes and fees. All information regarding the incorporation and operating of licenses for tradesmen is supplied by the Assistance Office of the Single Access Point and by the Bucharest Business Development Department. The latter supplies various information concerning notices, authorisations, licenses, agreements and special arrangements.

Leap-frogging: Avoiding 1st generation problems encountered by OECD countries

In the transition of SEE countries to a market economy framework, where private investment levels lag behind those of developed countries and the private sector is stagnating, the necessity to create an enabling environment for SMEs and private investment is of urgent priority. Reform of the business and investment environment leading to the creation of a dynamic entrepreneurial culture is crucial to drive the process of change in industrial structures. SEE governments are increasingly recognising that SMEs are a vital source of new jobs, exports and economic development. Several of the countries in the region are currently adopting national SME strategies, establishing organisational units targeting SME needs, and adopting reform tools and mechanisms specifically directed towards SMEs.

Although administrative simplification policies receive significant political attention and support in the region, the implementation of important reforms is still in the initial phase. Governments in the region confront many of the problems that faced OECD countries less than a decade ago, such as ineffective communication and consultation with SMEs, overlapping SME activities and poor internal co-ordination, a complex and burdensome legislative framework characterised by unpredictable and short-sighted changes, regional differences and solutions, a low degree of SME organisation, inexistent systems for measuring administrative burdens, and low degree of trust in the government. It is likely that SEE countries can benefit from past experience thereby avoiding some of the 1st generation problems encountered by OECD countries.

Conclusions: Some tentative policy implications

Recent work by OECD's Working Party for Regulatory Management and Reform highlights the administrative compliance costs imposed on businesses. Such burdens fall disproportionately on SMEs. In response, governments have launched a variety of programmes to simplify administrative regulations in general, often to reduce burdens for SMEs in particular. Examples of these tools and practices include small business impact statements, consultation mechanisms, sunset clauses, time-limits, plain-language drafting, compliance assistance, "tiering" of regulations, targeted compliance cost surveys, one-stop shops, and special guidance material to SMEs. Special agencies and organisational units have also been created to oversee and advocate such programmes.

Experiences from OECD countries suggest that strategies to reduce administrative burdens – with a particular focus on SMEs – could include considerations of the 10 initiatives listed below:

- Institutionalise SME concerns by establishing permanent or ad hoc governments units mandated to represent SME views in the regulatory process.
- Employ requirements for regulatory agencies to prepare Small Business Impact Statements during the regulatory process.
- Consult small business on proposals having an effect on small businesses prior to formulating policy and producing RIAs.
- Scale and calibrate administrative regulations when deemed necessary.
- Consider setting specific time-limits for administrative decision-making.
- Ensure plain-language drafting and specific compliance guidance for SMEs.
- Establish a central registry of administrative procedures and licences and initiate a comprehensive review (using RIAs) to determine how to reduce burdens.
- Build a system for measuring administrative burdens.
- Establish one-stop shops for regulatory information and transactions.
- Ensure that IT is widely available for SMEs to take advantage of e-government tools.

Needless to say, special initiatives to reduce burdens and support regulatory compliance of SMEs should be balanced against other concerns. When establishing tools and institutional arrangements dedicated to support SME interests, risks of capture by special interests increase. "Positive discrimination"

of SMEs may also have dynamic drawbacks by providing SMEs with incentives not to grow beyond thresholds qualifying for special support or to break up strategically as soon as the threshold is passed.

Experience shows that administrative simplification and SME-facilitating initiatives can help mobilise support for reform by promising and achieving highly visible results within a short period of time. However, administrative simplification policies might divert attention away from deeper and more fundamental regulatory quality programmes. The best basis for developing and prioritising administrative simplification is most likely to occur where these efforts are integrated into a broader regulatory quality agenda. Administrative simplification policies should be an on-going process in which both old and new regulations are continuously revised and simplified.

ANNEX B

EDUCATION AND TRAINING IN ENTREPRENEURSHIP: COUNTRY EXPERIENCES

Overview and Policy Issues

As entrepreneurship is being increasingly recognised as a crucial factor for economic growth and international competitiveness in a global economy, cultivating an entrepreneurship culture and fostering entrepreneurship values and spirit with a view to building an entrepreneurial society have become important issues on government agendas. However, because fostering entrepreneurship as a socio-economic institution is very different from what is required in designing and implementing other economic policies, governments are faced with a new challenge in this respect.

Education and training have been recognised in this context as the single most important means for achieving the objective of fostering entrepreneurship in societies²¹. Education and training in entrepreneurship can have two types of effects. First, they can have considerable impact on the performance of entrepreneurs, especially with regard to assisting entrepreneurs increase their firm's chances of survival, and to a lesser extent, to help make the resulting business more profitable. A Kauffman Center study (Charney and Libecap, 2000) finds that education in entrepreneurship increases the chances for start-ups and self-employment and enhances the economic reward and satisfaction of entrepreneurial individuals. Second, although extremely difficult to measure, education in entrepreneurship is also supposed to have some longer term impacts on the degree of entrepreneurial spirit and attitudes which are fundamental for an entrepreneurial population and society.

Although national governments as well as international fora, such as the EU, the APEC, and the OECD, are giving increasing emphasis to the importance of education and training in entrepreneurship, and many initiatives have been launched in practically all countries, entrepreneurship education and training are still characterised by a number of problems and shortcomings that need to be addressed urgently. These include:

- Entrepreneurship is not integrated into the curriculum, nor is it part of a coherent framework, but is more likely to be taught as a separate subject, or treated as an extra-curricular activity, resulting in a narrow impact on limited numbers of students.
- A lack of public resources for the academic discipline of entrepreneurship has resulted in limited teaching and research capability on this and related subjects, creating a major bottleneck in expanding education in entrepreneurial subjects at all levels of formal education and vocational training, as well as leading to an underdeveloped academic infrastructure in these subjects.

²¹ Another means which is far less common is the use of entrepreneurship campaigns.

- A need to improve co-ordination among government agencies in designing and implementing policies for promoting entrepreneurship through co-coordinated actions, and among different government programmes and initiatives.
- Fostering entrepreneurship through training and education is not yet well integrated as part of national long term economic strategy and planning;
- A low degree of acceptance (among all stakeholders) of the broader concept of education for entrepreneurial attitude and spirit as opposed to education and training for entrepreneurial skills (business skills for SMEs).
- Development of indicators and quantitative data, and evaluation of measures undertaken, are still very limited and undertaken only occasionally.

In light of the above, issues in the area of education and training in entrepreneurship that require special government attention may include:

- Integration of entrepreneurial subjects in the formal education systems, in a coherent and systematic way, not only for the purpose of teaching entrepreneurial skills, but also for fostering an entrepreneurial population, throughout all levels of education, and an entrepreneurial society more broadly.
- Promoting various forms of public and private partnership, from internship arrangements to private financing, between public educational and research institutions and the private sector, especially SMEs.
- Increasing public funding devoted to education and research in entrepreneurship, especially for improving capacity in teacher training, and for developing curricula and programmes in entrepreneurship.
- Improving co-ordination between different government bodies involved in promoting entrepreneurship through education and training and through other initiatives.
- Developing indicators, compiling quantitative data and evaluating the measures undertaken.

Empirical evidence on the impact of education

Education in entrepreneurship can have considerable impact on the performance of entrepreneurs. Although empirical evidence on the impact of education and training is still very limited and preliminary, it demonstrates that education and training in entrepreneurship can help entrepreneurs increase their firm's chance of survival, and to a lesser extent, it can help make the resulting business more profitable. According to a Kauffman Center study, compared to other business school alumni, entrepreneurship graduates:

- Are three times more likely to start new businesses.
- Are three times more likely to be self-employed.
- Have annual incomes that are 27% higher and own 62% more assets.
- Are more satisfied with their jobs.

The study also found a variance between the growth rates of entrepreneurship graduates' firms and other alumni's firms, regardless of whether the graduates were employees or owners. On average, small firms employing entrepreneurship graduates had greater sales and employment growth than those that employ non-entrepreneurship graduates.

Entrepreneurship graduates also seem to gravitate toward high technology companies. The study found that entrepreneurship graduates either founded or worked for high-technology firms in greater numbers than other business school alumni. Additionally, they are more involved in new product development and research and development activities, and work with products having shorter life spans.

European Union Initiatives

The *European Charter for Small Enterprises*, adopted by the General Affairs Council, 13 June 2000, and welcomed by the *Feira European Council*, 19-20 June 2000, commits the EU to teach business and entrepreneurship at all school levels and to develop training schemes for managers. A number of initiatives have been taken since, including the adoption in 2001 by the European Council of three strategic goals (and 13 associated concrete objectives) to be attained by 2010 with a view to organising education and training systems around quality, access, and openness to the world. In spite of efforts made by all countries, there have been indications²² recently that "the reforms undertaken are not up to the challenges and their current pace will not enable the Union to attain the objectives set". In particular, it is reported that the level of take-up by Europeans of lifelong learning is low and the levels of failure at school and of social exclusion remain too high". The European Union lags the United States and Japan in terms of investment in human resources and in relation to the level of private sector investment in higher education and continued training. The report concludes that if all the necessary steps are not taken now, the gap between the European Union and its main competitors will become even wider.

Box B.1: Findings of the Expert Group on the "Best Procedure": European Commission (2002)

- There is a policy commitment in almost all countries – to varying degrees – for promoting the teaching of entrepreneurship in the educational system.
- The development of indicators and collection of quantitative data in this field are very limited.
- The evaluation of measures undertaken is mostly done on a limited or occasional basis.
- Initiatives for promoting an entrepreneurial spirit are still rare at primary school level, although a number of good practices can be found; this type of teaching is more frequent in secondary schools.
- Vocational training systems (at secondary level) in most countries are not sufficiently oriented towards self-employment and entrepreneurship.
- Entrepreneurship training at university level is directed mostly at business and economics students.
- Schemes based on "learning by doing" (whereby students can create and run mini-businesses) are widely used in many countries for the development of entrepreneurial skills, especially at secondary level.
- The current provision of specific training for teachers of entrepreneurship is insufficient and represents a major obstacle to introducing the concept into classrooms.
- Links between schools and business, aimed at promoting entrepreneurship are widely developed in most countries (frequently local, independent efforts by individuals, educational institutions & organisations).
- There is a lack of private funding for entrepreneur programmes in Europe.

²²

[(Communication 11.11.2003 from the Commission -- "Education and Training 2010" The success of the Lisbon Strategy hinges on urgent reforms" (draft joint interim report on the implementation of the detailed work programme on the follow-up of education and training systems in Europe)]

The Final report of the Expert Group on the “Best Procedure” (a project within the framework of the Multi-annual Programme for Enterprise and Entrepreneurship, 2001-2005) acknowledges that, with regard to encouraging the enterprise spirit, a cultural aspect needs to be taken into account, for which education may offer an important contribution. The report recognises that the image of entrepreneurs as positive role models has never been as strong in Europe as in the United States, although some positive change is observed, in particular a growing awareness in Europe that initiatives should be developed in order to promote an enterprise culture. A list of the report’s findings are contained in Box B.1. Among the report’s main conclusions were the following: many of the numerous activities currently being developed at all levels of education are neither integrated into the curriculum nor part of a coherent framework; initiatives are often isolated, frequently driven by external actors, and entrepreneurship is likely to be taught as a separate subject or seen as an extra curricular activity. As a result, most students do not yet have the possibility of taking part in entrepreneurship courses and programmes. There is a need to prepare education systems for challenge by: creating a solid framework for entrepreneurship teaching; training more teachers for this topic; an ensuring that these programmes are generally available to students.

Box B.2: The Case of Spain

A recent study²³ highlighting the case of Spain pointed to a certain lack of a supportive attitude on the part of Spanish society constituting one of the obstacles for starting up a business in Spain. However a gradual change in attitudes, especially on the part of the younger generation, towards a greater acceptance of entrepreneurs was reported. In particular, there is a decline in the tendency to view entrepreneurs suspiciously when successful, or to see them as speculators when they fail.

Recent educational reforms in Spain have sought to imbue pupils of all ages with the skills and capacities required for entrepreneurial activity, the intention being that school-leavers will have benefited from a package of training allowing them to confront the social and professional reality awaiting them. Reforms apply to the national territory, and in addition, the autonomous communities implement optional complementary programmes. For example, the Asturias started the “Young European Company” and the region Castilla y Leon is preparing a curriculum for incorporating this option for the school year 2005-6. Concerning vocational training, co-operation agreements have been signed with the business community to guarantee better training and improved employment opportunities. The reform requires better teacher training for this subject and to this end a number of actions have been undertaken, such as the development of a teaching handbook and educational materials, as well as promotional campaigns. It is expected that a comprehensive evaluation of this reform cannot be known until a whole generation has completed its training.

Beyond the formal education dimension, it is also the intention the working population, whatever its educational level, will continue to receive training. To this end, the administration and the social partners have been working together with good results since 1993 to provide continuous vocational training, and legislation was passed covering the tripartite nature of continuous vocational training and making the system simpler, less bureaucratic, and accessible to a greater number of enterprises. In particular, the legislation favours continuous training in SMEs and for the self-employed through measures that facilitate and popularise the access of these groups to training.

APEC Initiatives

The APEC 2003 SME Ministerial meeting emphasised that culture is an important determinant of an entrepreneurial spirit. As significant variations of entrepreneurial attitudes exist across the APEC economies, policy-makers have a major role to play to foster entrepreneurial activities through education and training. Ministers called upon opinion leaders and civil society to publicly highlight entrepreneurship as a valuable way of life that enriches the community as a whole.

²³ Unpublished paper presented by the Spanish Delegation to the OECD Budapest “Workshop on Entrepreneurship, 8-10 September 2003.

Entrepreneurial activities require both *business opportunity* and *entrepreneurial capacity*. Entrepreneurial education and training should focus on:

- Identifying and enabling individuals and especially would-be entrepreneurs so that they may comprehend changes in their national and global economies and to identify business opportunities; and
- Assisting individuals and would-be entrepreneurs in developing the skills necessary to pursue business opportunities.

In response to interest for learning more about fostering entrepreneurship, supporting a dynamic SME sector, and creating jobs, APEC SME Ministers endorsed the second “US Voluntary Visitors Program for APEC SME Government Officials” to be implemented in June 2004. Ministers also welcomed the involvement of participating officials in sharing best practices for fostering entrepreneurship learned in their home markets. They looked forward to a report on the outcomes of this programme at the 2004 APEC SME Ministerial in Santiago. Ministers also welcomed the information shared on the US Small Business Administration’s Small Business Development Center Program, as it provides a model for co-operative public-private sector delivery of counselling, training and technical assistance in all aspects of business management for current or potential small business owners.

United States

Although the United States has a longer history in, and more widely spread, education in entrepreneurship, than other countries, it took 30 year for the field of entrepreneurship to gain legitimacy in the academic community. Fifteen years ago, entrepreneurship courses could only be found in a handful of schools in the United States. Today, more than 1 500 colleges and universities offer some form of entrepreneurship training – a trend that started in the early 1990s and continues to flourish. Interest in entrepreneurship education has spread to non-business disciplines, where students in engineering, life sciences and liberal arts show interest in becoming entrepreneurs. Furthermore, in the United States, training of the entrepreneurial spirit is more common as part of compulsory education (primary and secondary schools), and there are initiatives to encourage young people to set up entrepreneurial projects while in college and at university.

At the present time, education in entrepreneurship is mostly provided by schools in two main types of courses. The first type introduces the student to the principles of entrepreneurship (or small business). This includes forms of organisation, entrepreneurial behaviour, start-up strategies, and the application of marketing, accounting, and finance to the start-up. The second type of course usually focuses on creating a business plan, often with advice from practitioners from outside the business school.

Other types of courses include entrepreneurial finance (*e.g.* venture capital, angel investors, crafting deals, etc.), family business (*e.g.* succession, protecting the estate, working with relatives, etc.), high-technology business (*e.g.* intellectual property protection, prototyping, technology transfer), as well as courses in franchising, managing the mature business, and corporate entrepreneurship (*i.e.* intrapreneurship).

Japan

In present day Japan, launching a new business can be regarded as something special, in contrast with the situation prevailing in the United States. There are those who say that this is because starting up in business goes against the grain of the Japanese character. In reality, there are many Japanese who are

interested in starting their own business²⁴. Indeed the numbers of would-be entrepreneurs are increasing. Asked why they established their own business, the most common reply was “to have a free hand in work” (44%), and to achieve self-fulfillment (40%). Regarding their reasons for their choice of field of business, 60% of entrepreneurs said “to use own specialist skill and knowledge” and 46% said to “make use of contacts formed before setting up the business. Japan’s government, as other OECD governments, attaches a high priority for support of entrepreneurship, start-ups and business development. In particular, Japan’s government ensures support for the development of business management skills for would-be entrepreneurs and for the enhancement of human resource development for assisting business innovation.

Among the measures undertaken are: the organisation of a national start-up and venture forum in order to raise awareness in the general population of entrepreneurship, start-ups and business ventures. To help create conditions conducive to producing large numbers of entrepreneurs, experienced entrepreneurs and experts will be assembled for a nationwide awareness raising campaign. Start-up classes, startup courses and start up seminars are envisaged and the Central Federation of Societies of Commerce and Industry and the Japan Chamber of Commerce and Industry will greatly expand the number of locations where start-up classes can be taken. Prefectural support centres for SMEs will organise start-up seminars to help people acquire basic knowledge about start-ups. Jasmec will organise practical business seminars for start-ups and business ventures. With regard to new start-up support training, Jasmec will provide training for people planning to establish new start-ups to equip them with the requisite knowledge etc.

Selected National Experiences in Entrepreneurial Education

The United States and the United Kingdom have introduced various kinds of entrepreneurship training in primary and secondary schools since the late 1970s. Despite the long history of entrepreneurship training no single model can be identified as a benchmark and it is still not clear how entrepreneurship should best be introduced. Should young people learn how to start their own business or should they be taught willingness to change or other personal characteristics associated with entrepreneurs?

Canada, the United Kingdom and the United States have chosen the *first* approach. Children are taught self-employment as an alternative career and about the positive effects of entrepreneurship. With regard to the Canadian experiences: in the four Atlantic Provinces in Canada, for example, all students are exposed to entrepreneurship training. All such programmes have been evaluated and subsequently improved (Lundström and Stevenson, 2002). They emphasise a “learning by doing” style of teaching, where students create ideas, write business plans and run their own mini-firms. The Kauffman Centre for Entrepreneurship in the United States can also be mentioned as a source for education materials concerning the important role of entrepreneurs for the United States economy and practical tools for creating a business plan.

Finland has chosen the *second* approach, aims at developing an attitude of ‘intrapreneurship’ involving flexibility, initiative, creativeness, capability of taking risks and self initiative. Introducing entrepreneurship in schools is viewed as a means to encourage the entrepreneurial spirit. One result of the Entrepreneurship Project in Finland was a new curriculum (from 2004) which requires primary schools to incorporate entrepreneurship and provides guidelines on its implementation. No other country appears to have gone so far with regard to entrepreneurship in primary school curricula.

Entrepreneurship education at the university level is particularly advanced in the United States. Stanford University has records of entrepreneurship education in the 1930s. Several studies show large positive effects of these programmes. The entrepreneurial model of Stanford is viewed by many as the main driver of Silicon Valley. Firms with Stanford alumni or faculty founders for example generate more

²⁴ Japan Small Business Research Institute (2002, and 2003).

than 60% of Silicon Valley revenues. The Stanford model can be used as an inspiration for how entrepreneurship can be learned at the university level (Box 3). In addition to creating entrepreneurs, other positive effects from the Stanford entrepreneurship education model resulted, as shown by the Kauffman Foundation (Charney and Libecap, 2000). Compared to other business school alumni, entrepreneurship graduates are three times more likely to start new businesses, they have annual incomes that are 27% higher and own 62% more assets and are more satisfied with their jobs.

Box B.3: The Stanford model for entrepreneurship

Stanford University has a very close relationship with businesses. The engineering school is, for example, endowed with a Yahoo! Professor and a William Gates Computer Science Building. These formal relationships are important, but the informal relationships might be even more important. People go back and forth from academia to industry. Many faculty members have part-time jobs in industry and many industry people have part-time faculty appointments. Stanford also emphasises entrepreneurship skills in their courses. For example, in the High-Tech Entrepreneurship course, students discuss case studies of high-tech start-ups often with the founder/manager of the firm present in the class. In the industrial engineering class, students take three months of classes, three months of internship, and then three more months of classes.

However, the main force driving Stanford's unending production of start-ups is that so many people have started companies in the past that it seems normal for students to take what they have learned and make a company out of it.

Source: <http://corporate.stanford.edu/innovations/index.html>

Overall, effective policies used in these countries for integrating entrepreneurship in education can be summarised as:

- Use hands-on teaching methods in schools to introduce children to entrepreneurship (Canada).
- Teach personal characteristics of entrepreneurs in schools (Finland).
- Focus on integrating entrepreneurship at the university level (the United States).

Campaigns to promote entrepreneurship

Many countries have had campaigns in various forms for the promotion of entrepreneurship. These campaigns can serve as a source of inspiration but the actual campaign effects are difficult to evaluate. In Finland, for example, attempts at evaluating campaign results show very mixed results. Nevertheless, three rather obvious conditions for a good campaign can be drawn from the different countries' experience. These are *visible*, *empowered* and *regional* (Table B. 1).

- Changing attitudes/spirit requires a very *visible* campaign. Involving the Prime Minister or President is one way to insure a high profile in the press. Giving out rewards is another method. The United States President for example has his Small Business Person of the Year Award. Some countries have had alliances with the media, and successful entrepreneurs are presented on television programmes. Canada, for example, runs public-sponsored television shows on entrepreneurs to influence attitudes (*Venture* is one such weekly programme that has been running for several years. The positive effects these televised events in Canada have been documented by Lundström and Stevenson (2001). In the United States, several magazines are devoted to entrepreneurs.

- Those behind the campaign need to be *empowered* by the government to make the necessary changes when it involves different ministries. In many cases, campaigns are anchored in the Ministry of Industry, which makes it very difficult to make changes that are in the responsibility of other ministries, for example, administrative burdens associated with taxation. In the case of Finland, although many ministries were involved in the Entrepreneurship Project, the project did not succeed in generating policy changes or the introduction of new schemes by the various ministries, because of lack of a central authority. The United Kingdom has offered a solution to this problem by giving the UK Small Business Service direct access to the Prime Minister.
- Since business start-up rates vary substantially across regions within a country, successful campaigns should focus on regional aspects of entrepreneurship. The campaign design should be tailored to deal with the regional specific issues. The United Kingdom has dealt with the regional aspects by putting on road shows. In Finland, public authorities meet entrepreneurs and would-be entrepreneurs once a month in connection with regional Entrepreneurship Fora. The themes of each regional forum are tailored according to the specific interest of the region in question, and the topical project. The evaluation of the Entrepreneurship Project showed that the Fora have been well received by the firms and that they do well in addressing the specific needs of the different regions.

It is difficult to ascertain whether campaigns have a significant effect on the level of the entrepreneurial spirit. However, some data suggest that the United Kingdom Government's commitment to improve the conditions for entrepreneurs might have played a role in changing the entrepreneurial spirit there. To what extent were the observed positive changes in the entrepreneurial environment in the United Kingdom a direct result of the government's visible policy campaign, and did previous eight years of high growth make people more willing to take risks? This remains an open question.

Overall, effective policies used in these countries for entrepreneurship campaigns can be summarised as follows:

- Entrepreneurship campaigns should have be highly visible (the United States and the United Kingdom).
- Entrepreneurship campaigns should be empowered to introduce the necessary changes (the United Kingdom).
- Entrepreneurship campaigns should be tailored to the different needs of the regions (Finland)

Table B. 1 How are Entrepreneurship campaigns organised in different countries?

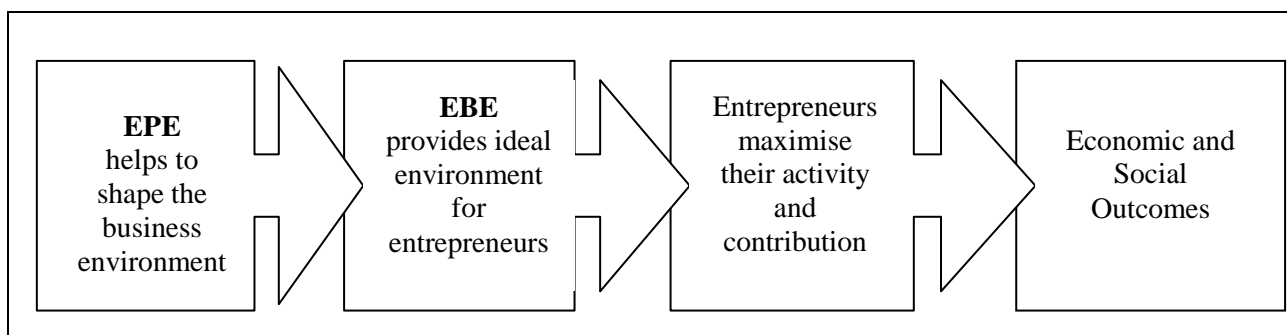
| | United Kingdom | Finland | United States |
|---|--|--|---|
| Name of the campaign | Think Small First | Entrepreneurship Project | Several campaigns but most visible is Small Business Week |
| Link to information about the campaign | Www.sbs.gov.uk/press/news30.asp | Www.ktm.fi/eng/1/yhanke/yhanke.htm | Http://smallbusinesssuccess.sba.gov/ |
| When was the campaign launched? | 2000 | 2000 | 1953 |
| Visibility: Who launched the campaign (e.g. the prime minister)? Does the campaign involve a prize for something like "Entrepreneur of the year"? Does the Prime Minister/President mention the importance of entrepreneurship in his/her new year speech or opening of parliament? | The Prime Minister No No | The Minister of Trade and Industry Yes No | President Yes Yes |
| Empowerment: Is promoting entrepreneurship mentioned in the budget address? Does the campaign have access to the Prime Minister/President Number of ministers involved (share of the total)? | Yes Yes The Small Business Service can work across all ministries | No No Nine ministries and the Association of Finnish Local and Regional Authorities | Yes The SMA has close links to the President and the Congress |
| Regional: Does the campaign have a regional aspect? | No | Yes | Yes |

ANNEX C

A SUGGESTED ANALYTICAL FRAMEWORK FOR POLICY

To start with, it may be conjectured that an “ideal” Entrepreneurial Business Environment (**EBE**) exists, shaped by government policy initiatives, and optimal in terms of encouraging entrepreneurship. In the simple framework illustrated in Figure C1 there is an ideal Entrepreneurial Business Environment, which, it can be argued, may be used to devise a suitable set of government policies and policy initiatives to move to that ideal position commensurate with a given set of desired economic and social outcomes. The Entrepreneurial Policy Environment (**EPE**) describes that package of policies and initiatives. The choice of an appropriate EPE is determined by the desired outcomes, and by knowledge of the current EBE and its shortcomings, so there are “feedback loops” from the outcomes, the entrepreneurial activity, and from the EBE which help to shape the EPE.

Figure C.1 Basic Policy Framework



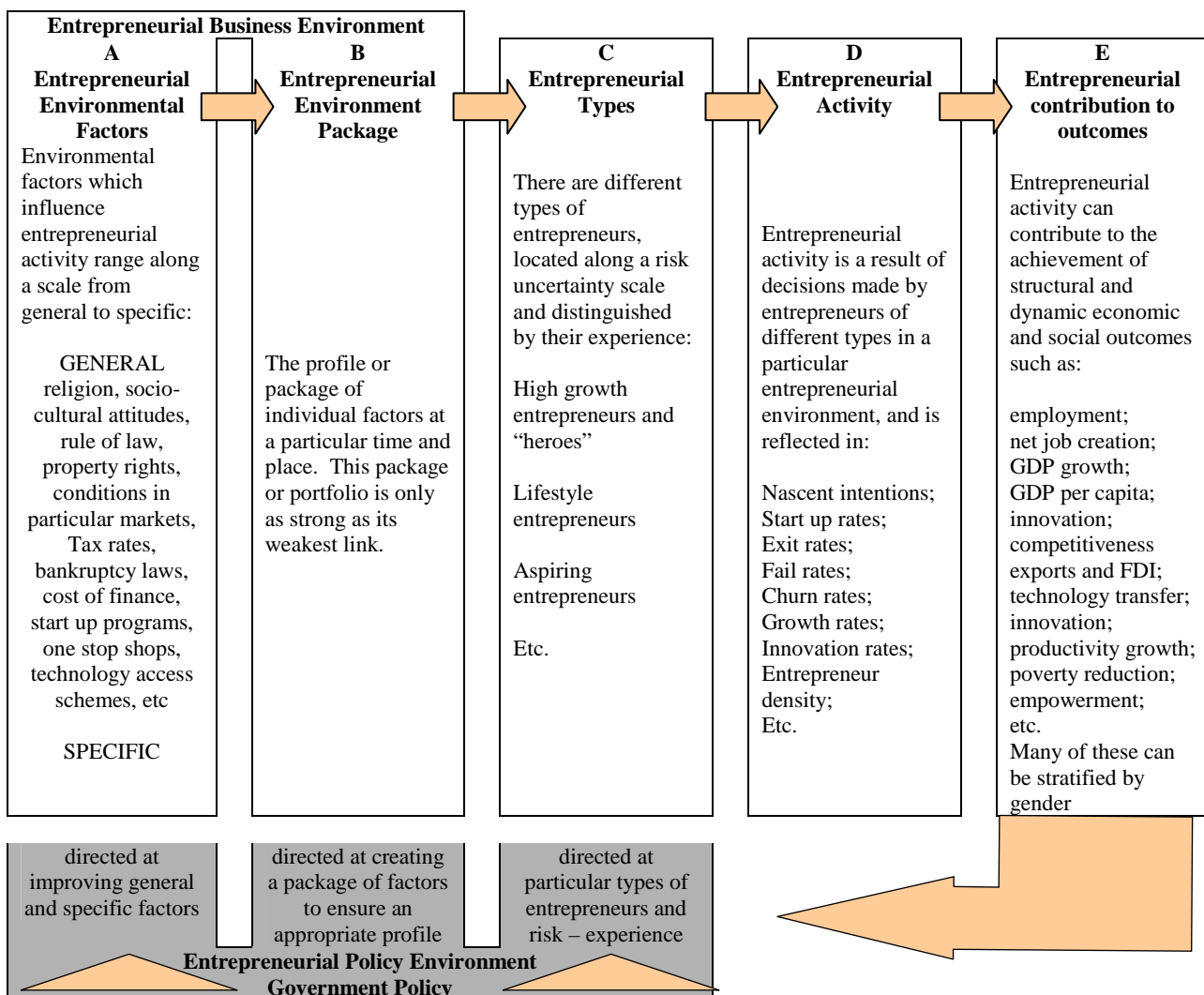
However there is unlikely to be a general set of laws or principles which can be applied in all economies, in all societies, at all times, to define an “ideal” business environment which is optimally conducive to entrepreneurship. There are several reasons for this, among which the following three may be cited:

- First, there are differences in the priorities given to different economic social and economic outcomes. In the context of the OECD, and the countries participating in the Bologna Process there is a diverse range of political and social priorities. A government which places very high priorities on poverty alleviation and reduction of regional inequalities may seek to use the “entrepreneurial engine” as an effective policy tool. A government which places very high priorities on international competitiveness and innovation may also seek to use the “entrepreneurial engine” to facilitate productivity improvement, growth and innovation. However, the EBE best suited to micro enterprise entrepreneurship in a transitional economy is likely to differ somewhat from the EBE best suited to “heroes” and growth entrepreneurs in an advanced economy.
- Second, there is the difference in entrepreneurs' propensity to take risk and uncertainty, and their experience. An EBE which suits experienced “heroes” is likely to be unstable,

unpredictable, and full of exciting, risky opportunities. This is quite different from the ideal EBE for timid aspiring entrepreneurs about to invest their whole life pension savings in small lifestyle businesses. If governments want a nation of shopkeepers, then they can create a single homogeneous EBE suited to them, but which will not be likely to provide adequate job creation or international competitiveness in a fast changing global world.

- Third, there are differences between existing business environments, the historical and cultural differences, and the stage of development. Simply moving from an existing business environment to another can be a difficult process. In Akimatsu's "flying geese" model, Europe took something like 600 years to move from a business environment of feudal agriculture to a post industrial knowledge based society. The United States took about 300 years, Japan about 60 years, and China is seeking to achieve the same in 20 years or so. Much of this development has been based on the efforts of entrepreneurs, and it is easier for the following geese because they can ride the slipstream of the leaders, and learn from their experiences. The EBE which is ideal at one point in time for a given culture and society, may not be the most appropriate to another, even at a similar stage of development.

Figure C. 2. Enhanced Policy Framework



Source: OECD Secretariat.

How may governments be assisted for devising policies to shape a better EBE? A possible framework for doing this is suggested in Figure C.2.

The main features of Figure C.2 are as follows:

- **First, starting with the far right hand column E**, it is the prerogative of governments and societies to determine their policy objectives and desired outcomes. Entrepreneurship is an effective means to some ends, but not to all. Entrepreneurs and SMEs play an important structural and dynamic role in almost all economies, and as shown in the previous section, they have the potential to address many of the major policy issues facing governments today. The relative importance of these policy issues and outcomes, and the trade offs between them are matters for governments to assess in the light of the best available evidence.
- **Second, moving to the far left hand column A**, there are many factors affecting the level of entrepreneurship, some of which may impede entrepreneurship, and others which may facilitate it. These may be visualised across a scale which ranges from very general to quite specific. At a very general level are factors such as historical, religious, and cultural factors. At specific levels may be, for example, individual motivation and education, subsidies and training packages for particular skills in particular industries, and the specific pattern of relations between firms and other players in a market (such as population ecology, clusters, networks, etc.). These factors may be changed by the influence of government policy, but changing more general factors usually takes longer and has more far reaching consequences than changing very specific ones.
- **Third, at column B**, it is not so much the individual environmental factors that affect the entrepreneur, but the package or profile of factors, shaped by policy and which is only as strong as its weakest link. These packages also tend to be time and place specific. Strengthening an individual factor, such as the level and availability of finance, will not necessarily lead to any increase in entrepreneurial activity if other factors (such as education or corruption) are constraints. Entrepreneurial activity may be more sensitive to changes in some environmental factors than others. A factor which impedes one entrepreneur, may assist another.
- **Fourth, moving to column C**, there are different types of entrepreneurs, and they will be affected differently by different “packages” of the business and policy environment, depending on their propensity to accept risk and uncertainty, and their experience.
- **Fifth, taking the bottom boxes, the Entrepreneurial Policy Environment is shaped by government policies**. These can be aimed at general or specific factors in the EBE. They can also be aimed at the weak links, and ensuring a suitable package or portfolio of factors. Finally they can be aimed at specific types of entrepreneurs, and the risk-uncertainty-reward-experience mix. The government policy shaping the EPE needs to be seen in the broader prioritisation issues addressed in the right hand column, and in the feedback loop, which comes from that column.
- **Sixth, in column D, entrepreneurial activity is manifest in a number of different ways**, and the level and trend of this activity can be monitored by a variety of indicators. This activity is a means to an end; it has an impact on the outcomes desired by a government or society.

This framework provides a basis for understanding how governments might create a more conducive Entrepreneurial Business Environment. This environment has two main aspects, a list of factors which influence entrepreneurship, and the “package” or “portfolio” or “profile” of those factors.

At a strategic level, we might identify a list of key factors and seek to achieve the levels of those factors achieved in the most advanced “entrepreneurial” economies. That is, we can seek to define an ideal profile for column A to which we aspire. In doing so we are setting maximum targets, even though they may be very difficult or impossible for some governments to achieve in a politically realistic timeframe. In a global economy this approach has some merit, it sets a target or a “lighthouse” to guide policy in the strategic sense over the longer term.

At a more pragmatic level, a government might seek to identify “weak links” in the package or profile of entrepreneurial environment factors. By devoting resources to improving the weakest links, government policy is likely to have the greatest measurable effect in the short term. If the factor that most impedes potential entrepreneurs is, for example, a lack of seed finance, or the lack of effective laws banning discrimination against women borrowers, then fixing that weak link will lead to immediate benefits. That is, provided that there is not another weak link, such as lack of managerial skill, or high costs of accessing market information. The difficulty with this approach is that it is a little like fixing a leaking bucket; once one leak is fixed, you have to move on to the next. Consequently it is necessary to have a strategic overview in order to establish priorities.

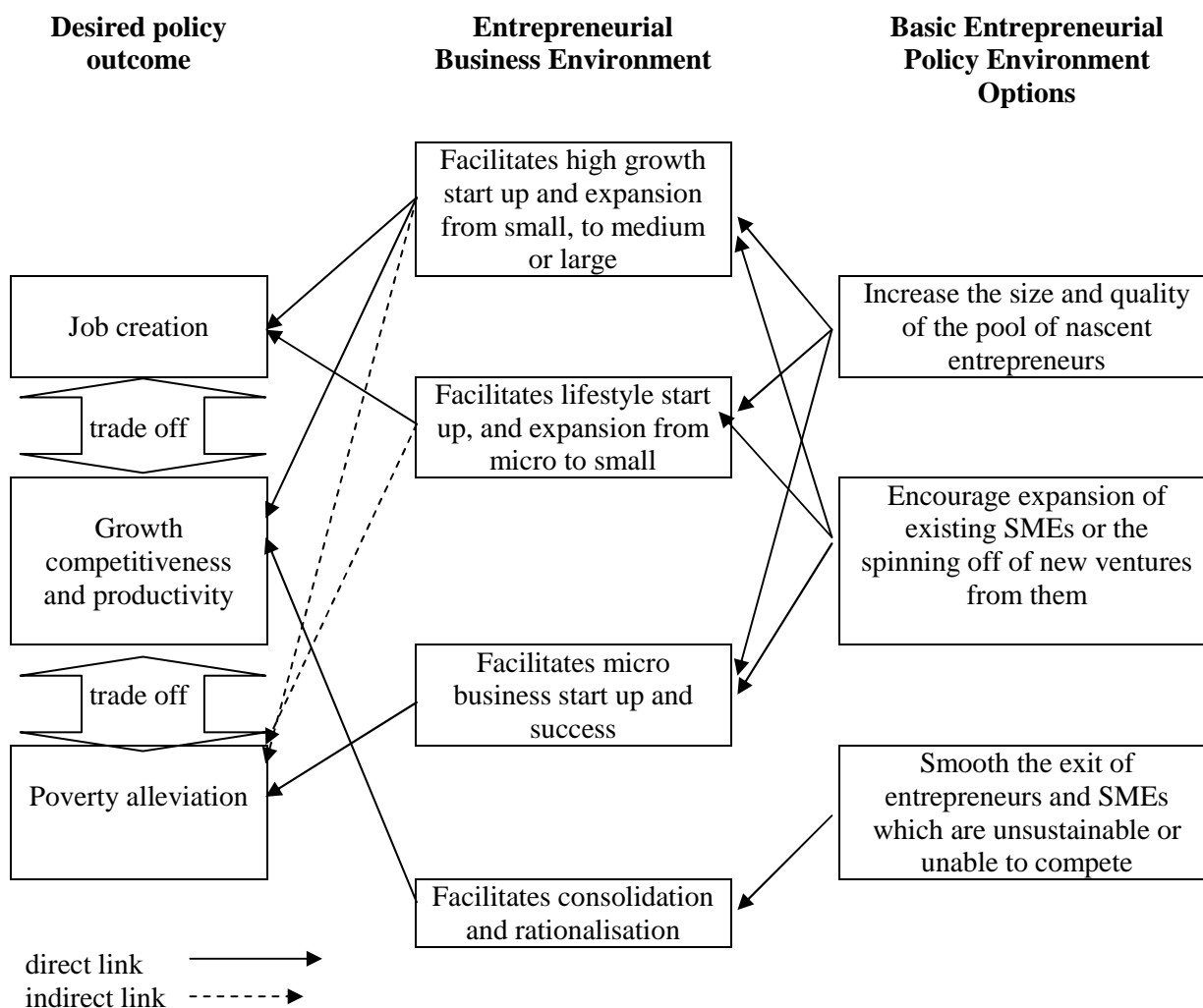
The framework thus leads us to an important conclusion. A conducive EBE can be best defined in relation to the types of entrepreneurs, and relative to the policy outcomes desired. An EBE which best suits small lifestyle entrepreneurs, or which is designed to maximise the participation of women in micro enterprise entrepreneurship, will not necessarily be the EBE best suited to heroes or growth oriented entrepreneurs. The former are likely to thrive in a stable predictable environment, the latter in a more turbulent opportunistic environment. The contributions they make to outcomes will differ too. It is unlikely that small lifestyle entrepreneurs will make as large a contribution to productivity and competitiveness as “heroes” might well do. Both “lifestylers” and heroes can contribute to job creation, but in different ways. The former mostly do it by an aggregation of a large number of net start ups, but the business environment most conducive to net start ups is not necessarily the same as that most suited to the rapid growth and experimentation of a small number of high growth SMEs.

This poses another important question: “can EBEs which are particularly conducive to one type of entrepreneur, and to given desired outcomes, be also compatible with the EBEs best suited to other types and other outcomes?” This means that the issue of developing conducive EBEs is quite complex, and like many policy issues, depends on making political decisions about priorities and trade offs. To make these decisions, policy makers need to have a better understanding of the processes and the trade offs, and it is that empirical issue that is dealt with in Part II of the background report.

Figure C.3 then brings together the main relations between *Outcomes*, *Business Environment* and *Policy Options* in a highly reduced and simplified form. Thus, for example, to achieve job creation as an outcome, a government may seek to increase the size or quality of the pool of aspiring entrepreneurs, and/or it may choose to encourage expansion of existing firms. The relative emphasis and the way it does this will depend on the circumstances it faces and the resources it has available. It may seek to create a business environment best suited to high growth firms in which case it may also achieve gains in productivity and competitiveness, but losses in the short term at least in poverty alleviation goals. In the longer term, and especially in an increasingly global world, improved competitiveness is probably essential to “the rising tide” effect that is indirectly addressing poverty by raising the level of incomes and wealth in the community. However this effect is likely to be long term and indirect, hence the dotted line and the trade off made clear in Figure C.2. The government may choose instead a more direct approach to job

creation and poverty alleviation (if the latter is a key priority) by encouraging the start up of large number of micro enterprises. It may do this by creating incentives for financial institutions to provide micro finance.

Figure C. 3. The Role of Factors Affecting Entrepreneurial Activity



This section sets out the available and relevant empirical evidence of relationships between:

- Entrepreneurial activity and outcomes (*i.e.* between columns D and E in the policy framework set out in Figure C.2.).
- Entrepreneurial factors and entrepreneurial activity (*i.e.* between column A and column D in Figure C.2.).
- Entrepreneurial policy and entrepreneurial activity (*i.e.* between the EPE, and column D in Figure C.2.).

As discussed in Section II of the main report, there is reasonably good evidence of direct relationships between the level of entrepreneurial activity (start-ups, exits, firm expansion etc.) and outcomes (job creation, growth).

The relationship between *entrepreneurial factors* (such as culture, immigration, psychological attitudes, availability of finance, education levels etc.) and *entrepreneurial activity* is more problematic and the results are more equivocal. This is because to establish a relationship between, for example, increased availability of finance, and the level of entrepreneurial activity it is necessary to take account of two intervening elements; the *package* of factors, and the *type* of entrepreneur (Columns B and C in Figure C.2). It is thus necessary to control for: i) the lags involved (it can take years before some factors have much effect on levels of entrepreneurship); ii) other factors which can interact and so cancel or reinforce each other; iii) different types of entrepreneurs (aspiring, heroes etc.) which are affected differently by different factors; iv) the *package* of factors, and whether there are any "weak links". Few studies control for all these effects, and so the results are equivocal or not reliable.

The relationship between policy initiatives which target the EPE (Entrepreneurial Policy Environment) and EBE (Entrepreneurial Business Environment) and the level of *entrepreneurial activity* is similarly fraught with difficulties. Policy evaluation work is still in its infancy. There is very little evaluative work that systematically controls for all the aspects identified in the previous paragraph. However there is some evidence emerging from the experience of the OECD's Working Party on SMEs and Entrepreneurship in applying the Framework for the Assessment of Programme and Policy Evaluation.

Entrepreneurial activity and outcomes

The relationship between entrepreneurial activity and outcomes is covered in Part II of the main background report. This shows that there is a reasonably consistent correlation between entrepreneurial activity (start up rates, turbulence, etc.) and outcomes such as employment growth, productivity increases, levels of innovation, etc.

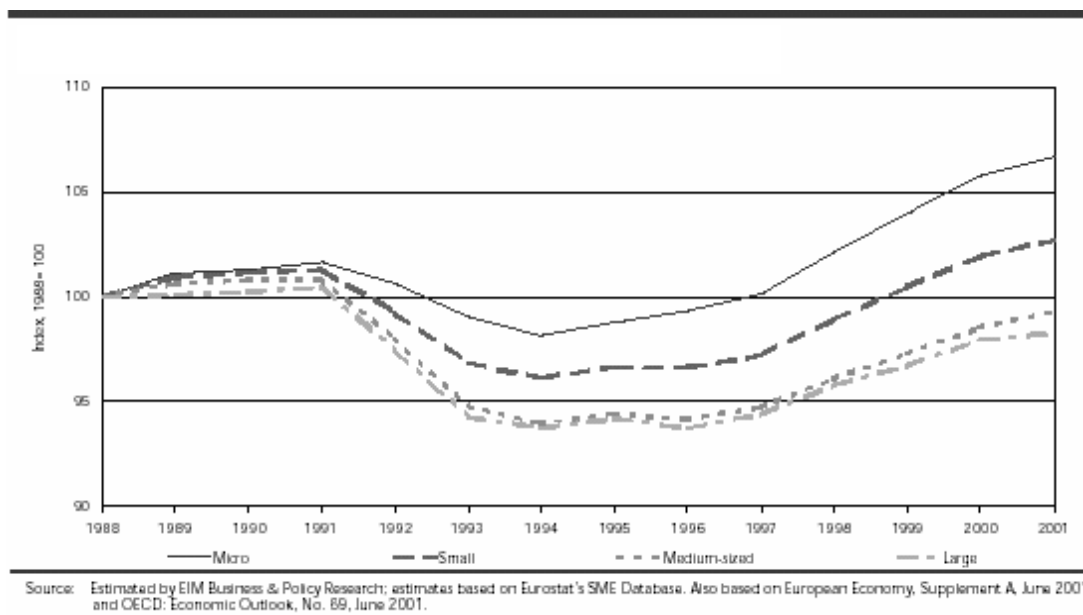
Figure C.4 shows the contribution of SMEs, and especially micro start ups to overall growth in 19 European countries over the last decade.

Environmental factors and entrepreneurial activity

The literature on the effect of environmental (including psychological) factors on entrepreneurial activity is substantial, and somewhat frustrating, in that it provides very little by way of consistent policy guidelines, and very rarely finds consistent relationships between environmental factors and the level of entrepreneurial activity, or the final outcomes of that activity. This is really not very surprising, because the literature usually seeks to find direct correlates between a set of independent variables (the entrepreneurial environment) and dependent variables (the level of entrepreneurial activity) without regard to the two intervening variables (identified in Figure C.2) *that is, the package or profile, and the particular type of entrepreneur*. Consequently there is no a priori reason to expect that an improvement in a particular factor will automatically be positively correlated with entrepreneurial activity unless the correlations are very carefully specified. For example, increasing access to public equity finance (for example by setting up low cost over the counter stock markets) will not of itself increase the level of lifestyle entrepreneurship if it is not a critical variable in the package for most lifestyle entrepreneurs. It may have a small effect on high growth entrepreneurs, but these are only a small proportion of entrepreneurs. Even then, it is only likely to have a significant correlation with levels of high growth entrepreneurship activity, if access to finance is a "weak link", and all other relevant factors (such as management capability, investment readiness, access to skilled technologists, etc.) are not also acting as constraints.

The literature and research can be reviewed at two levels; attempts at holistic approaches, and more specific approaches to the role of particular factors or sets of factors.

Figure C. 4. Employment growth by size class, Europe-19, 1988-2001



Holistic approaches

There are almost no systematic attempts at empiricism at a holistic level. That is, there have been remarkably few attempts to put together a comprehensive picture of the empirical relation between *all* likely environmental factors and the entrepreneurial activities. Similarly, even in studies which focus on the influence of specific factors, there is very little by way of attempts to control for the factors not included specifically in the study.

Specific approaches

Most studies focus on the effect of specific factors, or clusters of factors. Numerous environmental factors have been posited to have an impact on the level of entrepreneurial activity. For example, the availability of finance facilitates entrepreneurial activity, but in its absence impedes it. In other cases it may facilitate some and impede others. For example, the removal or reduction of government corruption may facilitate some entrepreneurs, and discourage others.

Table C. 1. Examples of specific factors affecting entrepreneurship

| Factor cluster | <i>Examples, evidence</i> |
|-------------------------------|---|
| CULTURE | Attitudes to wealth, elders, youth, experimentation, risk, work, professions, achievers, success etc. Family, extended family, collective ownership vs. individual Treatment of women, castes, classes, minorities, etc. Religion and ethical attitudes to business |
| INFRASTRUCTURE | Tangible, intangible, telecommunications, transport, distribution, health, public safety, law and courts, education system, etc. |
| SOCIAL | Demographic profile (e.g. ageing population reduces entrepreneurship and start up rates) Immigration and migration patterns Caste and class rigidities Social homogeneity |
| ECONOMIC | Growth opportunities, domestically and across borders Cyclical opportunities and threats (unemployment may lead to entrepreneurship) Taxation treatment of capital gains, start up expenses, intangible asset expenditure, stock options, etc. |
| LEGAL AND REGULATORY | Administrative burden imposed on smaller firms and start ups Regulatory barriers (licenses, etc.) Property rights (tangible, intangible) can be protected and marketed Right to incorporate, and costs of incorporation Costs of defending or enforcing agreements or rights Penalties imposed for "failure", treatment of bankrupts Specific regulations and laws relating to specific markets or activities |
| INFORMATION | Access to information about opportunities, technology, partners, laws and regulations etc. Freedom of press and ability to advertise or disseminate information (e.g. about new products) Accessibility of information in different languages |
| FINANCE | Discrimination in finance (e.g. age, gender, class discrimination) Sophistication and development of markets (e.g. microfinance, start up and seed finance, angles, equity, religion [e.g. Muslim finance], Venture Capital, second board and OTC markets, mezzanine, etc.) Continuity in finance markets (i.e. are the gaps in the markets, or can an entrepreneur expand smoothly from seed to IPO) Competition in financial markets (e.g. competitive finance markets reduce the margin above cost of finance to lenders, and increase range of services) Ability to use property rights as security (enables entrepreneurs to secure finance) |
| TECHNOLOGY | Access to large firms or universities and research labs for technology transfer Access to supply chains Access to incubators and technology support |
| EDUCATION and HUMAN RESOURCES | Levels of literacy, numeracy Computer and ICT literacy -- Specific education in entrepreneurship at school, university - Access to training programs, mentoring, advice, nanyangs |
| MARKET STRUCTURES | Monopolistic behaviour, predatory pricing by large firms Networks, clusters Flexibility in labour markets Industry or market specific incentives and subsidies |
| INDIVIDUAL | Individual personality and motivation traits e.g. locus of control, risk taking, innovativeness Individual experience and knowledge |

Entrepreneurship policy and entrepreneurial activity

Evidence of the relationship between entrepreneurial policy and the level of entrepreneurial activity is difficult to interpret for technical reasons, and the decision by the OECD's SME Working Party

on SMEs and Entrepreneurship to promote the evaluation of policy initiatives more rigorously will require a more systematic framework, and more information on contributing factors. Systematic evaluation of policies and programmes will improve decision makers' understanding of the impact of programmes and build governments' capacity to draft policies that are conducive to business performance and economic growth²⁵. There are many different policy initiatives that have been explored by governments, and anecdotal evidence suggests that some of these are more effective than others in achieving desired policy outcomes. Examples are:

- *Entrepreneurial campaigns* can be particularly successful if they are linked to actual changes in the business environment and improvements in the climate for start-ups, such as a reduction in administrative burdens or streamlining of procedures for beginning a business. Many campaigns are anchored in the Ministry of Industry, which makes it difficult to implement reforms in areas such as taxation or business registration. Finland tried to overcome this problem by involving a number of ministries in the Entrepreneurship Project, while the United Kingdom Think Small First campaign was run by the Small Business Service which could recommend reforms in the practices of other Ministries (OECD, 2002b).
- *Another policy instrument to promote entrepreneurial culture is to highlight entrepreneurial accomplishments* (Lundström and Stevenson, 2002). Many countries have introduced campaigns and prizes to promote entrepreneurship. In order to be effective, country experience shows that these campaigns should be visible, empowered, and regionally based. Changing attitudes towards entrepreneurship requires a very visible campaign. Involving high-level officials is one way to ensure a high profile in the press. The award of prizes is another approach. In the United States, for example, there is a *Small Business Person of the Year Award* presented by the President. The Canadian government sponsors a weekly television show, *Venture*, about entrepreneurs (OECD, 2002b).
- Because start-up rates and entrepreneurial attitudes vary substantially from region to region, campaigns should be tailored to particular locales (OECD, 2002b). The United Kingdom used regional “road shows” in its campaign, and Finland has held monthly regional Entrepreneurship Fora whose themes vary according to regional interests and issues. But whether start-up rates are due to government campaigns or higher GDP growth rates is difficult to determine. Effective approaches to entrepreneurial promotional campaigns used in these countries include the following (OECD, 2002b): Making entrepreneurship campaigns visible through use of high-level officials and media (Canada, US); Linking entrepreneurship campaigns to real improvements in conditions for start-ups (Finland, the United Kingdom); and tailoring entrepreneurship campaigns to regional needs and conditions (Finland).

25. A separate background report *Evaluation of SME Policies and Programmes* has been prepared for the 2nd OECD Conference of Ministers Responsible for SMEs.

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