Nurturing Small and Medium Sized Enterprises in Europe

In Entrepreneurship in Hospitality and Tourism, Goodfellow Publishers,

Editors: Levent Altinay, Maureen Brookes

Mark Anthony Camilleri*

Department of Corporate Communication, University of Malta

*Resident Academic Lecturer, Department of Corporate Communication, University of Malta, MALTA Email: mark.a.camilleri@um.edu.mt **Tel.** +356 2340 3742

Introduction

Tourism is one of the world's major industries responsible for economic growth, foreign exchange earnings, employment opportunities and regional balances in individual countries and across regions. This industry generates over 5% of the European Union (EU) gross domestic product and has strong linkages with other economic sectors. In fact, tourism triggers infrastructural developments that are related to the industry such as airports, seaports, parks, roads and rails. Within the EU alone, the tourism sector consists of about 1.8 million businesses. Most of these tourism businesses are small and medium sized enterprises (SMEs) that employ 5.2% of the total European workforce that translates to approximately 9.7 million jobs, with a significant proportion of young people (EU, 2010). This chapter considers relevant academic literature that differentiates SMEs from their larger counterparts. It maintains that small businesses are often constrained by their size and limited resources. Arguably, the accessibility to finance is one of the most critical factors for the SMEs' inception and growth. These entities are often viewed by financial institutions as relatively risky when compared to enterprises from other industries.

Therefore, this chapter contends that tourism SMEs may easily find themselves in an 'equity gap' where it may prove very difficult to raise capital for further investment. Consequently, national governments and other regulatory stakeholders are increasingly stepping in to support micro and small enterprises in many contexts. In this light, the European Union (EU) has reaffirmed its commitment for SMEs. As a matter of fact, the EU has drafted the 'Small Business Act' in 2008 and refined it again in 2011. The EU's commitment is quite evident from their frequent calls for research and training schemes in the subject areas of “SMEs” and “tourism”; where grants are frequently issued under ‘Marie Curie’ and ‘Cordis FP7’ programmes. Therefore, this chapter identifies specific policies and initiatives that are aimed at fostering a climate for job creation and competitiveness for SMEs in Europe. By the end of the chapter you should be able to:

- Define small and medium sized enterprises in the European Union context;
- Distinguish the differences between small and medium sized enterprises and large firms;
- Learn about the European Union measures that are currently supporting the financing needs of small and medium sized enterprises;
- Be knowledgeable of crowd-funding as an alternative form of financing.

SMEs in Tourism

The European Union (EU) has set its own criteria for small and medium sized enterprises (SMEs), as illustrated in Text Box 1.

Text Box 1: EU Definition of Small and Medium Sized Enterprises

Company category	Employees	Turnover (€)	Balance Sheet (€)
Medium	< 250	≤ € 50 m	≤ € 43 m
Small	< 50	≤ € 10 m	≤ € 10 m
Micro	< 10	≤ € 2 m	≤ € 2 m

(Source: EU, 2003/361/EC; EU, 2015a)

These ceilings apply to the figures that represent individual firms. According to the above criteria, most businesses in Europe can be classified as SMEs. Over 99 % of enterprises employ fewer than 250 individuals (EU, 2015a). The terminology of what constitutes small or medium sized organisations in tourism may vary in the literature (Storey, 1994; IC, 2011). For instance, in Canada small enterprises are defined as companies that have 99 employees or less, whereas the medium sized enterprises are defined as companies that have between 100 and 499 employees. The size of the enterprise is usually measured in terms of their staff count, sales turnover and / or profitability. Generally, SMEs may be regarded at sectorial level. Where in some industries the firms may be considered small, in others they are simply not recognised as SMEs. There are many parameters which have often been used in the past to identify SMEs. In the past academic literature, many authors have used multi-dimensional concepts of SMEs. For example, Storey (1994) maintained that there are issues about uncertainty, evolution and growth, entrepreneurial leadership and informality which are important differentiating factors. However, the broad parameters which often categorise SMEs may not always be derived from the size perspective. Arguably, an organisation employing five people and another employing 100 can both be classified as SMEs. Yet, both companies can behave significantly different in their approaches and practices. The small and medium sized firm may not always be a 'smaller' version of the larger firm. The numerous theories relating to SMEs must consider all the distinctive variables which distinguish them from their larger counterparts. The most common and easiest criterion to define SMEs and to differentiate them from the larger firms is by using different thresholds, as illustrated in the Text Box above.

Characteristics of Tourism SMEs

SMEs have a desire for independence, freedom from intervention and bureaucracy. The smaller businesses tend to exhibit less formal structures as they have looser control systems, less documentation on transactions and fewer procedural hurdles (Morris *et al.*, 2002). It may appear that there is better communication in such firms since the owner or manager is closer to the workforce. Therefore, the owner-manager of the smaller firm may be better placed to lead the organisation and to make the best decisions in the interest of all employees (Storey, 1994). For these reasons, SMEs may offer interesting work prospects as there can be closer social relationships between management and employees. This informal style of management may also translate to better communications with other stakeholders.

Moreover, SMEs can offer more varied duties and responsibilities, as employees may participate in different kinds of work in a stable workplace. The familiar environment is usually characterised by infrequent industrial disputes. The absence of trade unionism is particularly conspicuous among the smaller businesses. An empirical study among small and medium sized Chinese firms revealed that there are relatively fewer SME firms experiencing unionisation (Zheng et al., 2009). In SMEs there may be fewer strikes since the collective element needed for strike action is absent and the potential conflict may be expressed through more individualistic means of protest such as absenteeism and labour turnover (Carraher, 2011). Some of the characteristics of SMEs as opposed to their larger counterparts are clearly laid out in Text Box 2.

Text Box 2: Characteristics of Different Firms

Strategic orientation	SMEs	Large firms
Consolidated	Independence	Group
		Joint ventures
		Alliances
	Internally financed	Externally financed
	Cash limited	
	Multi-tasking	Diversified
	Flexibility	Rigidity
	Economies of scope	Economies of scale
	Owner-management	External management

Strategic orientation	SMEs	Large firms
Emerging	Competitiveness-keeper	Competitiveness-maker
	Informality	Formalised
	Invisible to the media	Visible to media and NGOs
	Largely local	National
		Multinational
		Global
	Relational	Transactional
	Personal Relationship	Structured relationship
	Trust	Branded
	Openness	

(Source: Russo and Perrini, 2010)

On the other hand, some empirical studies have demonstrated that tourism SMEs can offer poorer economic rewards, employment terms and physical working conditions, and a lower level of job security when compared to the larger enterprises (Davidson *et al.*, 2006). Other findings reveal that the quality of the job environment is much poorer within smaller firms than it is within larger businesses (Nadiri and Tanova, 2010). Moreover, it may appear that SME owner-managers often “lack the necessary skills, expertise or resources to function efficiently and effectively” (Ritchie and Crouch, 2003:141). As firms grow, they start employing more individuals to act as managers or supervisors (Kusluvan *et al.*, 2010). Within large organisations, there is a clear distinction between ownership and management, as described in the agency theory (Ramon Rodrigues, 2002). Moreover, the employees of the bigger enterprises often enjoy superior employment packages and better perquisites than those employees working in small businesses. Small firms frequently lack the required resources; comprising both the financial capital and human competencies (Altinay et al., 2013). The very size of small businesses often creates a special condition, which is referred to as `resource poverty'. This factor distinguishes SMEs from the larger corporations (Morrison and Teixeira, 2004; Getz and Carlsen, 2005).

Financing of SMEs

Small firms tend to find themselves in an equity gap, where sometimes it can prove quite hard to acquire capital finance for further investment. Although banks are key providers of finance for many enterprises through the provision of loans; unsecured bank finance is very limited. Therefore, the SMEs' growth into viable investment opportunities may be severely restricted. Cashflow-based lending is relatively rare and growing businesses rarely have unused security at their disposal. Tourism SMEs are very reliant on personal savings to finance their business (IC, 2011). The main source of financing during the start-up phase is usually through personal savings, with more SMEs in tourism industries using this source (EU, 2014). SMEs in tourism industries are significantly more likely to make use of lease financing and significantly less likely to use retained earnings (IC, 2011). Moreover, SMEs in tourism industries are almost twice as likely as SMEs in non-tourism industries to use informal financing (loans from friends and family) to financing their ongoing operations

(IC, 2011). This issue could be an indication that tourism SMEs may encounter more difficulty in obtaining credit from financial institutions than SMEs in non-tourism industries. As a result they will inevitably need to turn to alternative means of financing their business (i.e., either through personal savings and / or informal financing). Despite the changing debt market, one of the main reasons why small businesses fail to acquire debt finance is due to their inability to provide adequate and sufficient collateral. Even small businesses with high growth potential can experience difficulties in raising relatively modest amounts of risk capital. Moreover, certain external forces and potential threats in the business environment can impact harder on the small businesses than on the larger corporations. Changes in government regulations, tax laws, labour legislation and interest rates may potentially affect a greater percentage of expenses for the smaller businesses than they do for their larger counterparts.

Throughout the years, the EU has dedicated several funds to help enterprises. Recently, the EU's Enterprise and Industry Division has reiterated the importance of improving access to finance for SMEs. On the 2nd May 2013, the European Commission / European Investment Bank (EIB) joint report maintained that their support for SMEs has reached €13 billion in 2012. In addition, the Commission funded guarantees that have helped 220,000 small businesses across Europe as it mobilised loans that were worth more than €13 billion. This interesting development led to numerous funding schemes as well as to the new generation of financial instruments that support SMEs' financing needs. In addition to these financial resources that were made available to SMEs there was a €10 billion injection in the European Investment Bank's (EIB) capital. Moreover, the EU Commission has also launched a new single online portal on all financial instruments (for SMEs) as well as an information guide to promote SMEs' stock listings. It has committed itself to boost its support for SMEs through various financing programmes, as illustrated in Text Box 3.

Text Box 3: EU Measures that support SMEs

EU programme for the Competitiveness of Enterprises and Small and Medium Sized Enterprises (COSME)	Guarantees for loans up to EUR 150 000 to small and medium sized enterprises.
Competitiveness and Innovation Framework Programme (CIP)	Supports innovation activities (including eco-innovation).
InnovFin Programme (Horizon 2020)	Loans and guarantees to innovative businesses. Financing of research & development projects. Equity (early and start-up phase).
The SME instrument	Funding and coaching support to innovative SMEs.
Creative Europe	Loans to small and medium sized enterprises in the cultural and creative sectors.

Programme for Employment and Social Innovation (EaSI)	Microloans up to EUR 25, 000 to micro-enterprises and to vulnerable persons who wish to set up or develop a micro-company. Equity up to EUR 500 000 to social enterprises.

(Adapted from EU, 2015b; Welcome Europe, 2014) <<End of boxed text>>

Evidently, Europe is responding to the contentious issues facing SMEs by providing a mix of flexible, financial instruments under programmes such as the Competitiveness and Innovation Framework Programme (CIP), Progress Microfinance, the Risk Sharing Instrument (FP7), EIB loans and Structural Funds. For example, lately the EU allocated a budget of €2.3bn specifically to bolster the "Competitiveness of Enterprises and Small and Medium sized Enterprises" (COSME) for the period between 2014 to 2020. This initiative has been designed to support European SMEs in four key areas: developing entrepreneurship; helping SMEs access finance; supporting SMEs who wish to internationalise their business; and reducing the legislative and regulatory burden on SMEs. Almost 220,000 SMEs had already benefited of the Commission's Competitiveness and Innovation Framework Programme (CIP) as it helped them through the provision of collateral for their loans. EU (2013a) envisaged that for every euro that was dedicated to loan guarantees, it has in turn stimulated 30 euros in bank loans. CIP has helped to mobilise over €13 billion of loans and €2.3 billion of venture capital for SMEs across

Europe (EU, 2014). An example of a project that has been co-funded by the Eco-Innovation initiative under the auspices of the EU's CIP is featured below.

A CIP-funded project

"MOVE-IT" was supported by the EU's CIP funding. This project was made up of various organisations, namely; Stockholm Environment Institute from Tallinn (Estonia), KATE (Germany), Eco-Counseling Enterprise (Belgium), Groupe One (Belgium), TIME Foundation (Bulgaria), Aeoliki Ltd (Cyprus) and Menschels Vitalresort (Germany) (EU, 2015c). MOVE-IT developed and tested eco-innovative coaching and learning models that helped many tourism SMEs to acquire an Eco-Management Audit Scheme (EMAS) certifications and Eco-labels. It provided service packages for its clients, "by linking cultural, economic, ecological and social aspects" (EU, 2015c).

Some of the outcomes of MOVE-IT included the provision of coaching on environmental sustainability; vocational training for regional development agents and consultants; an online platform for communication, e-learning and coaching at European level (that was available in six languages); the preparation of cluster management guides that explained how to make an excellent tourist destination in terms of local governance and environmental performance; and the development of web-based tools and green software that facilitated integrated management systems.

The European Commission launched a consultation programme (between the 3rd October to 31st December 2013) to explore the costs and benefits of ‘crowdfunding’ as an alternative form of finance (EU, 2013b). Contributions were sought from competent authorities, crowdfunding platforms, entrepreneurs and individuals who launched crowdfunding campaigns. This new form of financing entails the collection of funds through small contributions from many parties in order to raise capital for a particular project or venture. This latter source of financing has the potential to bridge the equity gap many start-ups face. It is hoped that this recent initiative stimulates entrepreneurship amid different regulatory, supervisory, fiscal and social structures of the European Union. Apparently, the EU is delving through extant national legal frameworks to understand better how businesses can raise their capital through such open forms of financing. Whilst some crowdfunding campaigns are local in nature, there may be others who are already benefiting from easier access to financing within the single European market. In a similar vein, the United States’ Securities and Exchange Commission (SEC) is also considering crowdfunding. Crowdfunding was incorporated in “Jumpstart Our Business Startups Act” (Stemler, 2014). It is very likely that the proposal for crowdfunding will bring a major shift in how small U.S. companies can raise their money in the private securities market.

Alternative sources of finance which are already secured via the internet include monetary contributions in exchange for rewards, product pre-ordering, lending and / or investment. Arguably, these plans can be successful only if the regulatory costs are kept as low as possible. Otherwise, small enterprises may not be intrigued by such financing propositions. From the outset, it may appear that crowdfunding is still not so popular among tourism SMEs. However, there are start-ups that have taken advantage of such financing programmes. A case in point is Outski Inc., as this innovative start-up is still raising its capital requirements through public fundraising (see Text Box 5). Probably, one of the main causes of concern about crowdfunding will be the reporting requirements for small companies to file their annual financial statements. The most experienced entrepreneurs and their intermediaries will have no difficulty in meeting crowdfunding rules and regulations, but first-time entrepreneurs may require further support. At present, the smaller businesses earning revenues (and profits) below a certain threshold are not legally obliged to provide audited financial statements. Moreover, small enterprises may not always hold historical financials. This means that financial services authorities will find it quite daunting to determine how small companies are truthful and fair in their financial reporting. According to the US proposals, the businesses that will opt for crowdfunding as a source of financing will have to audit their annual accounts (Stemler, 2013). In a similar vein, the European enterprises would have to meet certain regulations to acquire this 'new' source of finance. It is hoped that facilitative, soft-law measures on crowdfunding will lead to fruitful legislative and regulatory actions across many contexts. Through crowdfunding, more capital will be unlocked for start-ups, investments and projects. This additional capital finance will also help to spur the economic growth of SMEs.

Crowdfunding for etourism

Outski Inc., an information communications technology (ICT) enterprise that is based in Tucson, Arizona - has already raised more than $629,000 of its seed financing requirements through crowdsourcing (Crowdfunder, 2015). This start-up enables its users to plan and save for their future vacations by setting aside a portion of the employees' pay-cheques for their future vacations. Therefore, Outski offers B2B solutions that are related to employee incentives and benefit packages with an integrated vacation savings account.

Employees can search and book flights and hotels through Outski's site. There is also a social element to this site, where vacation plans can be shared with family and friends. Outski's site (or app) allows people to discuss vacation ideas and share links and reviews. What differentiates Outski from other travel sites is that its users can set up savings accounts and can plan for their future trips. They can also add funds to their account through their own credit and / or savings accounts or through PayPal. Users can send and request money from each other and have the ability to withdraw funds at any time. Their money is accessible through an Outski Visa or Discover Travel Savings Card, which has a PIN and works like any other debit or credit card. Outski has partnered with 14 different companies and all of those companies are integrated into its website. Most of the partnerships deal with financial elements of the site, but there are also companies like Expedia and Amazon. In 2014, the company has launched its beta web product with over 1,000 users and has also developed an iOS app for iphones.

Conclusion

No longer are smaller businesses considered as reactive and peripheral forces in terms of innovation, employment and productivity. This chapter has provided a definition of SMEs in the European context. Afterwards, it shed light on how these enterprises possess certain characteristics that set them apart from big businesses. SMEs are often constrained by their organisational size and their limited, scarce resources. Very often these entities may find themselves in an “equity gap” as they may find it difficult to access finance to start up or even grow their business. Therefore, this chapter has featured some relevant EU practitioner-oriented policies and instruments that are helping European SMEs to raise capital for further investment. It is hoped that this chapter informs readers on how small and medium sized enterprises can access finance through EU institutions. Indeed, the wider European political initiatives that bring economic growth, jobs and competitiveness may not be realised without the contribution of all SMEs, including those in the tourism sector.

References

Altinay, L, Brookes, M. and Aktas, G. (2013) ‘Selecting Franchise Partners: Franchisee Perspectives, Processes and Criteria’, *Tourism Management*, **37**, 176-185.

Carraher, S. M. (2011) ‘Turnover prediction using attitudes towards benefits, pay, and pay satisfaction among employees and entrepreneurs in Estonia, Latvia, and Lithuania’, *Baltic Journal of Management*, **6** (1), 25-52.

Crowdfunder (2015) ‘Travel and Tourism’ Retrieved on 18th January from https://www.crowdfunder.com/crowdfunding/travel-and-tourism.

Davidson, M., Guilding, C. andTimo, N. (2006) ‘Employment, flexibility and labour market practices of domestic and MNC chain luxury hotels in Australia: Where has accountability gone?’, *International Journal of Hospitality Management*, **25** (2), 193-210.

EU (2003). ‘Structure, performance and competitiveness of European tourism and its enterprises’ http://ec.europa.eu/enterprise/sectors/tourism/files/studies/structure_performance_competitiveness/pwc_en.pdf.

EU (2003/361/EC) ‘SME definition’, Retrieved on 18th Janaury 2015 from http://eurlex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2003:124:0036:0041:EN:PDF.

EU (2010) ‘Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions - Europe, the world's No 1 tourist destination – a new political framework for tourism in Europe’, Retrieved on 18th December 2014 from http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52010DC0352.

EU (2013a) European Commission Enterprise and Industry: Improving access to finance for SMEs: key to economic recovery- IP/13/387 Retrieved on 18th January 2015 from http://europa.eu/rapid/press-release_IP-13-387_en.htm.

EU (2013b) ‘European Commission Enterprise and Industry: Public consultation: Crowdfunding in Europe ? Exploring the added value of potential EU action’ Retrieved on 18th January 2015 from http://ec.europa.eu/internal_market/finances/crowdfunding/.

EU (2014) 'CIP success stories (on Youtube)', Retrieved on 12th January from http://ec.europa.eu/cip/successstories/index_en.htm.

EU (2015a) 'What is an SME?', Retrieved on 13th February, 2015 from http://ec.europa.eu/enterprise/policies/sme/facts-figures-analysis/sme-definition/index_en.htm.

EU (2015b) 'Access to Finance', Retrieved on 12th January 2015 from http://europa.eu/youreurope/business/funding-grants/access-to-finance/index_en.htm.

EU (2015c) 'Environmental Compliance Assistance Programme for SMEs: Small, Clean and Competitive', Retrieved on 28th January 2015 from http://ec.europa.eu/environment/sme/cases/moveit_en.htm.

Getz, D. and Carlsen, J. (2005) 'Family business in tourism: state of the art', *Annals of Tourism Research*, **32**(1), 237-258.

Hall, C.M. (ed.) (2007) ‘Pro-poor Tourism’. Channel View, Clevedon, New Zealand.

IC (2011) ‘Industry Canada: Small Business Financing Profiles: Small and Medium Sized Enterprises in Tourism Industries, Small Business Branch, Industry Canada’, Retrieved on 10th January 2015 from https://www.ic.gc.ca/eic/site/061.nsf/eng/02245.html.

Kusluvan, S., Kusluvan, Z., Ilhan, I., and Buyruk, L. (2010) ‘The human dimension a review of human resources management issues in the tourism and hospitality industry’, *Cornell Hospitality Quarterly*, **51** (2), 171-214.

Morris, M. H., Schindehutte, M., Walton, J., and Allen, J. (2002) ‘The ethical context of entrepreneurship: Proposing and testing a developmental framework’, *Journal of Business Ethics*, **40** (4), 331-361.

Morrison, A. and Teixeira, R. (2004) ‘Small business performance: a tourism sector focus’, *Journal of Small Business and Enterprise Development*, **11** (2), 166-173.

Nadiri, H. and Tanova, C. (2010) ‘An investigation of the role of justice in turnover intentions, job satisfaction, and organizational citizenship behavior in hospitality industry’, *International Journal of Hospitality Management*, **29** (1), 33-41.

Ramón Rodríguez, A. (2002) ‘Determining factors in entry choice for international expansion. The case of the Spanish hotel industry’, *Tourism Management*, **23** (6), 597-607.

Ritchie, J. B. and Crouch, G. I. (2003) ‘The competitive destination: A sustainable tourism perspective’, Cabi Publishers, Wallingford, UK.

Russo, A. and Perrini, F. (2010) ‘Investigating stakeholder theory and social capital: CSR in large firms and SMEs’, *Journal of Business Ethics*, **91** (2), 207-221.

Stemler, A.R. (2013) ‘The JOBS Act and crowdfunding: Harnessing the power—and money—of the masses’, *Business Horizons*, **56** (3), 271-275.

Storey, D.J. (1994) ‘Understanding the Small Business Sector’, Routledge, London.

Welcome Europe (2014) ‘European Funds for the Tourism Sector’, Retrieved on the 6th January 2015 fromhttp://www.welcomeurope.com/fact-of-the-day/european-funds-tourism-sector-211+111.html.

Zheng, C., O'Neill, G., and Morrison, M. (2009) ‘Enhancing Chinese SME performance through innovative HR practices’, *Personnel Review*, **38** (2), 175-194.