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VIII Encuentro Cotec Europa

SMEs Growth to Improve Innovation Abilites

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Topics covered in the presentation

1. The corporate universes of Italy, Portugal and Spain: an over-representation of micro and small enterprises
2. The imperatives of job creation and economic growth
3. The importance of Fast-Growing Companies
4. Fast-Growing Companies, Fast-Declining Companies and Bankrupt Companies or the return to the “creative destruction” metaphor and the confirmation of considerable differences between the European and the United States development models
5. Creative destruction and increase of productivity
6. Brief reference to the results achieved by Italy, Portugal and Spain regarding the works already performed on Fast-Growing Companies
7. Implications of the relevance given to Fast-Growing Companies, namely in terms of Public Policies





The corporate universes of Italy, Portugal and Spain

The totality of companies of the EU 27 is distributed as follows in terms of Employment, Gross Value Added and Productivity:

EU 27 companies	% Employment	% GVA	Productivity	Productivity (%)
Micro	29.6	20.9	29.9	70.7
Small	20.6	18.9	38.7	91.5
Medium	16.8	17.8	44.8	105.9
Large	32.9	42.4	54.4	128.6
TOTAL	100.0	100.0	42.3	100.0

Source: SBS Eurostat, 2005





The corporate universes of Italy, Portugal and Spain

The totality of Italian, Portuguese and Spanish manufacturing industry companies is distributed as follows in terms of Employment and Productivity:

Italy (Manuf)	Weigth Employment	Productivity	Productivity (%)
Micro	26.2	23.6	55.6
Small	33.3	39.1	92.3
Medium	17.2	52.9	124.7
Large	23.3	60.5	142.7
TOTAL	100.0	42.4	100.0

Portugal (Manuf)	Weigth Employment	Productivity	Productivity (%)
Micro	20.4	11.7	47.1
Small	31.1	18.8	75.6
Medium	19.1	25.7	103.5
Large	29.4	39.8	160.3
TOTAL	100.0	24.8	100.0

Spain (Manuf)	Weigth Employment	Productivity	Productivity (%)
Micro	21.5	26.9	57.2
Small	32.8	40.9	87.1
Medium	20.2	49.8	105.9
Large	25.5	69.5	147.8
TOTAL	100.0	47.0	100.0





The imperatives of job creation and economic growth

The necessity of job creation and economic growth in our three economies:

- since 2003, the World Economy grew at the most higher rates ever, with rates ascending to 5%/year, up to 2007;
- a growth rate of 5.3% was again reached in 2010 – but, even that year, the United States grew only 3%, and the Euro area grew just 1.9%;
- considering 2012, and just the so-called developed countries, OECD is supposed to grow 1.6%, reaching 2.4% in the United States, with a contraction of -0.1% in the Euro area. In Italy, Portugal and Spain, GDP will decrease -1.7% , -3.2% and -1.6%, respectively;
- unemployment rates will reach in 2012, and pursuant to the OECD forecasts (which may be surpassed), 9.4% in Italy, 15.4% in Portugal and 24.5% in Spain;
- the growth rate of the so-called potential GDP is currently of 1.7% for all OECD countries, having dropped to 2% in the United States and to 1.2% in the Euro Area. The value expected for Spain is also of 1.2%, whereas Italy and Portugal reach only 0.3%.





The importance of Fast-Growing Companies

Which are the companies that can contribute the most to solve our problem?

- SMEs?
- Start-ups?
- High-tech?
- Innovative?

Or, just in a more empirical and prosaic view:

- Fast-Growing Companies?





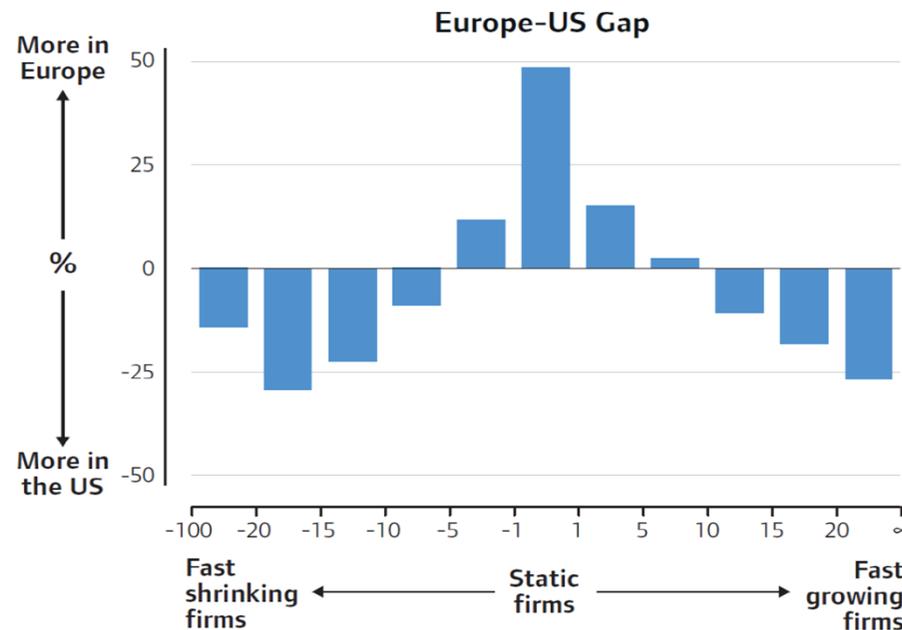
The importance of Fast-Growing Companies

The conclusions of the work developed by NESTA are beyond any doubt:

- «the research makes a powerful case that a small number of high-growth businesses are responsible for the lion's share of job creation and prosperity, and that innovation is instrumental in the success of these businesses.»;
- from 3% to 6% of Fast-Growing Companies are responsible for between 35% and 50% of the jobs created by all companies that survive;
- «this has significant implications for the direction of economic policy. It shows that enabling innovation is good for growth. Just as importantly, it shows that focusing attention on growing businesses and promoting excellence, far from being an elitist policy, gives rise to widespread job creation and prosperity.»;
- «we hope that this research will be a powerful contribution to the debate on how to foster economic growth.».



The importance of Fast-Growing Companies, Fast-Declining Companies and Bankrupt Companies or the return to the “creative destruction” metaphor



It's difficult to have a large number of Fast-Growing Companies without having also a large number of Fast-Declining Companies or Bankrupt Companies.





Creative destruction and increase of productivity

The conclusions of these works provides new insights on how creative destruction (or, more precisely, resource reallocation) may help to explain some of the productivity differences across countries:

- «aggregate productivity grows both when firms improve their internal practices as well as when resources are reallocated towards those firms (or plants) that have successfully developed superior practices»;
- «a more dynamic growth distribution, in which most firms expand or contract and only a few remain stable, is likely to accelerate both these processes»;
- «on the contrary, an economy without experimentation results instead in a much higher share of stable firms, and lower productivity growth».





Brief reference to the results achieved by Italy, Portugal and Spain regarding the works already performed on Fast-Growing Companies

If applied to our three countries, the conclusions of these works show that:

- Italy and Portugal appear among the countries with the lowest percentages of “fast-growing companies” (only 2% and 4%, respectively in the manufacturing industry and services, in Italy, for companies with more than 10 employees, with results for Portugal being only marginally above in both cases);
- Spain appears in a better position with a percentage of “fast-growing companies” reaching 3% in the manufacturing industry and close to 5% in services, but still in the “lower range” of the studied countries;
- to provide us with means of comparison, “fast-growing companies” reached 6% and over 4.5% in the United States, respectively for the manufacturing industry and services;
- these percentages are largely exceeded in some fast growing countries.





Implications of the relevance given to Fast-Growing Companies, namely in terms of Public Policies

- 1. A cultural change**
- 2. Infrastructure requirements**
- 3. Innovation in the companies**
- 4. Importance of intangible investment and creation of intangible assets, mainly in the companies**
- 5. The State as catalyst of innovation**
- 6. The decisive role of venture capital**





A cultural change

It is, first and foremost, a cultural change. In the place previously occupied by other policies (start-ups, technological companies, SMEs, companies in a problematic economic situation, priority regarding preservation of jobs, etc.) now appear the “fast-growing companies”:

- which are not just start-ups, although start-ups usually grow faster;
- which are not just technological companies and can appear in any activity sector;
- which are not mandatorily SMEs, although most of them are.





Infrastructure requirements

- educational basis of the human capital available: educational system, particularly higher education, which is expected to provide training, on a graduate level, to a high percentage of the active population, with predominance of the science and engineering areas;
- there is also the effort required from the State in terms of R&D: despite the known importance of the weight of corporate R&D in GDP (more than the weight of all R&D costs in GDP), it seems difficult to create an environment where corporate R&D has a higher impact on GDP without the State simultaneously achieving minimum critical values of R&D costs;
- however, it must be noted that not all R&D public effort must fall in direct public costs. In some countries with a better innovation performance (Canada, Japan, Holland, Korea), the largest part of R&D public costs is comprised of tax incentives regarding corporate R&D.





Innovation in the companies

What is required from the Fast-Growing Companies:

- formulation of goals in terms of sale of new products and services or, at least, sale of already existing products and services but with significant improvements;
- integration of innovative people, namely new employees with higher education degrees particularly in the science and engineering areas;
- investment in innovation, namely R&D;
- investment in other intangible assets, like branding;
- proper management of all aspects related to intellectual property, particularly patents.





Importance of intangible investment and creation of intangible assets, mainly in the companies

The importance of intangible investment which can result in the creation of intangible assets, refers to:

- **costs with more conventional R&D activities, including acquisition of design and industrial property;**
- **costs with software development and acquisition of software and databases;**
- **costs often considered as investment costs and related to the acquisition of “economical and management skills”, such as training, organizational development, branding and marketing.**





The State as catalyst of innovation

The State must play an important role as “catalyst” of innovation, which would include:

- direct support to companies, namely corporate investment in R&D;
- creation of a favourable environment and conditions for entrepreneurialism and creation of new companies, with particular focus on technologically based start-ups;
- respect for the effective competition regulations, giving particular attention to violations that can limit the challenge of companies with high market shares by small and medium size companies regarding their competitors;
- protection and imposition of a respectful environment regarding the different ways of intellectual property;
- imposition of standards and accreditation requirements, either for products or the exercise of certain activities;
- leading a public procurement policy regarding the acquisition of innovative goods and services, with particular focus on the acquisition of products still under development, in a pre-competition stage.





The decisive role of venture capital

It is not possible to make companies grow without providing them with a permanent capital – which sometimes forces to changes in the shareholder base and in management skills or in the organizations' top.

Therefore the importance of venture capital in all its expressions:

- seed;
- start-ups;
- early development;
- expansion;
- we refer both to the contribution of capital and to management skills, sometimes very specialized.

The problem of small countries, not big enough to justify a continuous presence of venture capital operators...





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Thank you.

**Daniel Bessa, COTEC Portugal's CEO
VIII COTEC Europe Meeting
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