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## **Growing Regional SMEs – Some Policy Lessons from Northern Metropolitan Melbourne**

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### **Abstract**

Growth in the small and medium-sized enterprise sector has been a significant focus for policy makers both in the developed and developing world. The inhomogeneity of the sme sector presents challenges to the policymakers and those who seek to assist in the growth process for the sector. This paper reports on a study of fifteen companies in Northern Metropolitan Melbourne. Business profile benchmarking was used to identify strengths, weaknesses and potential barriers to growth for each company. A business growth plan was then developed based on the strengths identified. The firms were then assisted in the initial stages of implementation of the business growth plan. Of the fifteen companies which agreed to participate, all proceeded to benchmarking using the Benchmark Index, and twelve proceeded to the growth plan and implementation phases. This paper reports on the outcomes for the twelve companies. The process of benchmarking, action planning and implementation of the action plans raised a number of policy level issues that require further investigation, since they may lie at the heart of any growth strategy for the sector.



## **Introduction**

The development and growth of the small and medium-sized enterprise (sme) sector has been a feature on the policy landscapes of many administrations for some time. The demanding task is to develop approaches which will meet the genuine needs and wants of the owner managers in a wide range of industry sectors, geographic locations and personal motivations. Hart et al. (2000) report on the impact of the work of the Local Enterprise Development Unit in Northern Ireland. A change of policy in that organization resulted in a different approach to the provision of financial assistance to small firms. The support agency had provided support for a wide variety of firms and the research partitioned the firms into 'growth' and 'established' firms. The authors concluded that the policy change to focus on 'growth' firms had appeared to be successful. Summon (1998) reported on the UK government's support through the 'Business Links' and a review of a number of studies of the impact on the sme sector of the Business Links approach to sme support. O'Gorman (2001) reports on research into the sustainability of growth in sme sector firms and explores the debate between the 'strategic choice of entrepreneurs' explanation of sme growth and the 'industry structure' explanation. Sparkes and Thomas (2001) investigated the importance of the internet developments to the Welsh agri-food sector and concluded that, because of peripheral location on the 'Celtic fringe', the development and growth of the industry will depend on the ability to take up the marketing opportunities presented by internet technologies. Choeke and Armstrong (2000) reported on the initial results of a study aimed at investigating the reasons for 'organisational growth' and 'business success' in the sme sector. The authors' conclusions include suggestions that this research may point to the need to revisit the policy agenda and refocus the nature of advice and assistance initiatives to take account of the influence of 'organisational culture' on sme growth and development. Vickers and North (2000) examine the role of a particular intervention, 'regional technology initiatives' on sme sector firms in the English regions. The initial ideals involved long term strategic partnerships for innovation and technology transfer. However, the reality was that many smes really wanted short-term problem solving assistance rather than to avail themselves of long term innovation and technology transfer opportunities. The various views and perceptions relating to the research reported here indicate that there are many different interpretations that the readers and users of the research might reasonably draw about sme growth and development. Gibb (2000) argues that there has been a growth of ignorance, which paralleled the growth in the volume of research and publication around entrepreneurship, enterprise and small and medium enterprise growth and development. This research reports on a set of case studies which seeks to illustrate interventions, which address the specific requirements of individual owner managers who have indicated that they wish to achieve 'growth' in their sme company. The paper concludes with an evaluation of the interventions.

## **Research programme**

The research programme sought to establish whether international business profile benchmarking could be used to identify business growth opportunities for firms in the Australian SME environment. The programme consisted of a pilot study of 15 companies in Northern Metropolitan Melbourne. The process involved identifying companies which were geared for growth. Owner managers were then asked to provide financial and management data which was required to carry out the business profile benchmarking process. The data was validated by site visits and interviews. The data was then used as input to the 'Benchmark Index' (Pilcher (1988)) and a report was generated which benchmarked the firms across around eighty different measures of performance. The report was presented to senior staff of the firms and its meaning was explained and contextualised for the particular company in its industry sector.



## **The Benchmarking Index**

The input data requirements for the generation of the company's profile consists of several elements which have been derived from, for example, *Management Today's* Best Factory Awards. These are Financial Revenue and Costs, and Financial Capital which form the financial data set and a Management Data set. Each of these areas has a number of elements for which data is required. Each element is accompanied in the data capture instrument by an explanatory definition. For manufacturing firms, there is an additional module which addresses competitiveness issues in manufacturing operations, including component and assembly set-up times. Other modules are available for other industry sectors and other functional areas. Dalrymple (1999) and Pilcher (1998) provide more detailed background to the instrument.

## **The Report**

The output of the comparisons is contained in a report which provides a graphical comparison and a table showing best in class, worst in class, lower and upper quartiles and the average for the each of several measures in the following categories: *Profitability, Financial Management, Productivity, Investment, Growth, Customer Service, Innovation, Supplier Management, People Management and People Satisfaction*. A manufacturing-specific module was also used in this project.

## **Reporting Back**

Individual meetings were held with the participant owner managers and the report was presented and explained to participant. The relative position in each category was discussed and the implications for business growth for individual measures and categories were explored. At this stage, the first exploration of what the company perceptions of 'growth' were began. This is an essential step in enabling the owner manager to understand the implications of the various 'growth' paths might be.

After the owner managers had been given time to digest the report and its contents, a seminar was held to enable a group of companies to get together and be instructed on how they might use the information contained in the report to trace back to the operational activities of the company. This also enabled the interpretation of the direction which growth may eventually take.

## **The Business Planning Process**

Following the feedback and seminar elements of the program, each company participated in an in-company business development planning process. The benchmarking report was used for guidance to enable the company personnel and an experienced facilitator to identify where the company presented as having strengths when compared with an international peer group. The question of 'growth' was also explored to establish whether the growth which was being sought was in market share in a particular market, turnover, profit, new markets, new products, etc., since the implications of each of these may well have very different implications for the eventual business planning activity and the actions which flow from that.

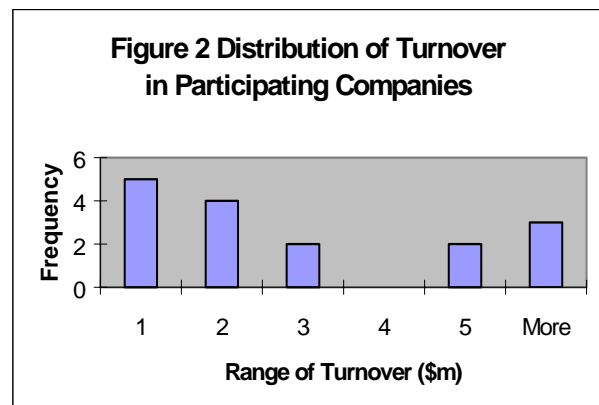
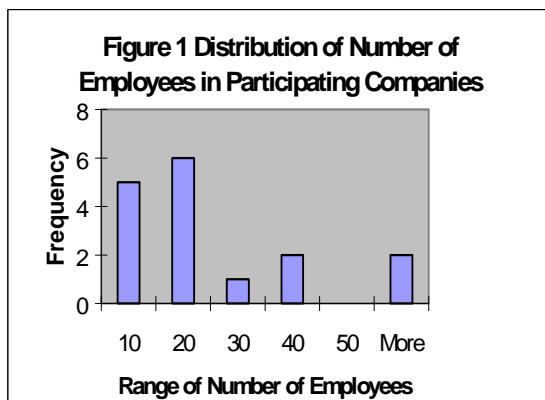
The next phase in the process is drawn from the manufacturing strategy literature. It involves the identification of 'what wins orders in the marketplace' for a particular company's product. These deliberations coupled with



the information derived from the business profile benchmarking report were the basis of the business planning and consequent action planning.

## Results

The participating companies ranged in size from 2 to 250 employees. Eleven companies (69%) had less than 20 employees and only two companies had more than 50 employees. The distribution of number of employees is shown in Figure 1. Only three participants had a turnover of \$5million or more per annum. The distribution of turnover is shown in Figure 2.



All participating companies underwent the benchmarking exercise to develop an international business profile. Three of the larger companies attended the workshops on tools and techniques but developed growth plans in-house. One small company is in the process of being sold and no growth plan was developed. The remaining twelve participants attended workshops and were assisted in developing a growth strategy and plan, and also had help in taking the first step in the plan.

## Model for achieving growth

The approach, through a combination of workshops and “one on one” mentoring, was to: -

- provide participants with an understanding of the tools and techniques for systematically seeking opportunities for growth,
- carry out a gap analysis on what needed to be done to achieve growth, and
- develop strategies and plans for growth.

## Company results

All fifteen companies participated in the business profile benchmarking process. Three of the larger firms attended the workshops to interpret the reports and then used the reports as a basis for their own internal business growth activities. These larger companies had established, experienced and capable management teams. The management teams of the smaller companies often consisted of the owner manager and perhaps a small group of people with management or supervisory responsibilities. The managers of these twelve companies participated in the full program.



## Outcomes from Case Studies

### *Market opportunities*

Finding realistic market opportunities for growth was not a problem. Opportunities per company varied from 3 to 17 with an average of 8. Sources of opportunity by category were: -

Existing Markets/Existing Products	25%
Existing Markets/New Products	31%
New Markets/Existing Products	33%
New Markets/New Products	11%

### *Growth targets*

A short-term target was set based on the level of turnover to be achieved in two years, on an annualised basis. i.e. if the target is \$4.8 million p.a., in two years time monthly sales will have reached \$400,000.

Short-term targets ranged from an 18% increase in turnover from the value used in the business profile to 100% increase, with an average increase of 44%. Companies will monitor their progress on achieving their short term targets. Long-term growth targets were from a minimum increase in turnover of 50% to +100%.

### *Major constraints on growth*

The major constraints on growth were: -

<b>Constraint</b>	<b>Number of companies to which the constraint applied</b>
Lack of a method to accurately predict costs and margins in a period of growth	5
Lack of Market and/or Sales resource time, and/or - appropriate promotional material	4
Price competition	3
Lack of capacity	3
Funding growth	2
Difficulty in finding appropriate skilled people	2

The major issue was a lack of an appropriate accounting system that would give management the information needed to manage and control growth. Participants indicated that conventional monthly profit and loss statements were not giving them the information they needed to manage and control their company, particularly when growth is underway. The move from the well-known and well understood equilibrium position through a



growth phase was causing uncertainty. Whilst participants understood in principle the variation in unit cost with volume none of them had a system that measured and monitored that variation.

The first step for five participating companies was to develop a standard cost/price system that measured contribution to non-manufacturing overhead and profit, and a variance reporting system that provided information on the effect of price and volume, and manufacturing efficiencies, on profitability.

The second problem area was lack of marketing and sales resource. For most participating smes the proprietor was the marketing and sales person for the company and difficulties were seen in creating the time necessary to carry out the additional business development activities associated with growth. Potential solutions were: -

- Initially concentrating on growth within existing markets as the additional marketing and sales effort is marginal, until turnover and profitability is increased to a level to justify employing additional sales support.
- Delegating some authority to employees to free up time.

The other issue regarding marketing and selling resources is the generally poor level of supporting promotional material. Material that was available concentrated on promoting the technical features of the product sold, not the benefits and value to the customer. It is interesting to note that only 1 in 4 companies saw price competition from competitors as a barrier.

### **Policy Implications**

The developing and developed economies of the world have focused on the small and medium-sized enterprise sector as a potential source of economic growth, jobs and additional contribution to GDP. Most approaches seek to increase the business birth rate, improve the business survival rate or encourage the growth of existing businesses. In many cases, the thrust of the interventions lies in the increasing use of new, often cutting edge, technology to make businesses more up to date in their approach to business operations. Two of the most recent cases are the move to encourage small and medium-sized businesses to join the 'e-business' trend and the encouragement of sme sector companies to enter export markets.

The tentative implications from this study are that business survival and business growth present a different set of challenges to those being addressed by the thrust of some current policy. The issues raised include:

1. Many companies participating in this study found some difficulty in assembling the data to participate in the business profile benchmarking phase of the research. Many companies required assistance to complete the data collection instrument.
2. A number of companies were unable to cost products and their associated service packages to an appropriate level of accuracy. In most cases, the current mix of products and services produced an end of year profit, but the inability to cost the individual components of that mix means that growth which involves something other than a scale up of 'more of the same' may result in increased turnover and reduced profit, since cost and price need to be related in a way that price exceeds cost!
3. Many sme firms are actively engaged in more than one business activity. For example, a cool store business may be involved in manufacture and installation as well as service and repair of their own and other manufacturer's product. This exacerbates the problems referred to in 2. above.
4. The focus of such marketing materials that were in use was on technical specification of the product or product and service package, rather than focusing on customer related benefits.



If these issues are more widespread and prevalent in the sme sector companies generally, then the policy implications are likely to be to focus on much more fundamental management capability and capacity building, rather than moving along the technology adoption and exporting trend lines. Companies which do not have the basic data capture facility and which are unable to accurately identify costs of all elements of their product and service packages are unlikely to prosper in an e-business environment. They are also unlikely to contribute significantly to export revenues in a sustainable way.

### **Conclusions**

The International Business Profile Benchmarking instrument which was initiated in the UK as the BenchmarkIndex and has been developed into a diagnostic instrument for European small and medium-sized firms was successfully piloted in Australia (Dalrymple (2000)). The use of the instrument to identify areas for investment in quality improvement activity was established. Further, in a group of companies, its use was demonstrated to provide a catalyst for change in those firms and significant improvements in operational performance were demonstrated by those participants which were given intensive assistance to implement action plans for process improvement.

This research program has taken the use of the instrument into a new domain by coupling its use to the manufacturing strategy literature and linking the strengths of the company to the answer to the question “What wins orders in the marketplace for your product?” This program has made a significant contribution to the sme sector participants by providing guidance for rational business growth and development planning. The firms were assisted to avoid the gamble often involved in the choice of which part of the business to expand and develop. If sme companies can be assisted to make better business growth decisions, many more will be able to participate successfully and profitably in the e-business and exporting environments.

### **Acknowledgement**

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