Competitiveness Survey of Small Enterprises in Hungary

Dr. György Kadoesca
Budapest Tech, kadocsa.gyorgy@kgk.bmf.hu

Abstract: Our assumptions made on the basis of an incomplete evaluation of the completed questionnaires that have been returned reflect our very first impressions. During the survey, businesses considered developments in the business environment as definitely favourable. In addition to reporting increasing uncertainty, they deemed Hungary’s political climate, domestic markets and social changes as having marked effects. One and a half years after Hungary’s accession to the European Union, SMEs cannot perceive major impacts of accession, or blame the prevailing political situation for all changes. Small businesses do not capitalize on the opportunities offered by the European Union, and do not make efforts to apply for EU grants and funds, or attempt to penetrate new markets.

Keywords: competitiveness research environment, economic policy factors, effects of EU enlargement, environmental factors and responses, micro economic factors of competitiveness of SME

1 SME Competitiveness Research Environment

Several institutions conduct SME researches in Hungary and the neighbouring countries: universities, colleges, research and development institutions. Below we shall only look at one segment of the research to evaluate the factors of competitiveness of Hungarian SMEs, more specifically family businesses leading to conclusions on the competitiveness of SMEs through their review.

The Competitiveness Research Centre attached to Budapest Corvinus University Corporate Economics Department has analysed competitiveness of Hungarian companies since 1995. Its latest report published in 2004 contained the following chapters, analysing the main factors competitiveness [1]:

- Environment of corporate operation
- Corporate strategies, strategic management
- Organisation and operation
- Impacts of the EU accession
The majority of the companies involved in the research are medium-sized and large companies, and the share of small companies is only 5%. Consequently, the conclusions apply mainly to large companies, therefore, the description below does not relate to them.

The situation of SMEs is regularly analysed by the Small Enterprise Development Institute and, after it was integrated into the Ministry of Economy and Transport, the ministry, in an annual report. The structure and methodology of the reports is consistent, looking at the factors affecting the situation and development of SMEs according to the following criteria [2]:

- Ownership structure
- Participation in networks
- Capital investments
- Revenues and export
- Profitability
- Productivity, efficiency
- Financing

The questionnaire-based survey of the Ministry of Economy and Transport conducted in 2003 contained the following key conclusions:

Approximately, two thirds of SMEs consider that the economy of the country stagnates or slightly improves, they mainly sell in the retail market, have moderate development, for which they rely almost exclusively on their own resources.

16-20% of SMEs are in the initial or declining phase of their lifecycle; they consider their situation bad and have a pessimistic future vision too.

15% of SMEs are in the phase of growth or maturity with a good position and optimistic future vision. The analysed factors of competitiveness are positive, and these enterprises use bank loans for their development project too.

In summary, in terms of status analysis, the research conducted on approximately 2000 enterprises has brought more unfavourable conclusions compared to the previous surveys. Despite many valuable conclusions, the report does not provide any closer guidelines for research in terms of definition or influencing factors.

Professor Mugler, who has been devoting his literary and public life activities to the research and development of the SME sector for many years, has defined the two main directions of research in his first book as follows [3]:

- Definition of the concept of entrepreneur and analysis of his impacts on economic development.
• Distinction of SME strategic potential, primarily in the different phases of the lifecycle.

Consequently, he analyses in detail the issues of strategic planning, marketing, controlling, and resource management as well as the SME basis. In fact, he considers these aspects the key areas of the viability and development of SMEs.

In his second book, Professor Mugler [4]: analyses the key factors of development, breaking them down into external environmental factors and internal (resource) factors. Looking at typical changes, he is trying to identify the specific driving forces of development for SMEs in the different phases of the lifecycle of an enterprise using various development theory models.

Professor Belak approaches the developing abilities of SMEs from the management side. He also divides the influencing factors into external and internal factors, structuring development potential as follows [5]:

• Political, strategic and operational opportunities.
• Coincidence of development potentials, i.e., availability of resources required for the opportunity within the enterprise.

In terms of the opportunities and problems of development of Slovenian enterprises, he reaches the same conclusions as apply to the most reform countries in the 1990s. He lists the following main influencing factors of SME competitiveness, which at that time typically hindered development:

• Harmony between competition opportunities and operational performing ability,
• Social, economic and partner relations,
• Crisis and change management experiences (lack of them),
• Future vision (‘survival’ enterprises),
• Harmony between organisational and personal potential.

Assistant Professor Mojca Duh analyses the role and importance of organisation and personal relations on the example of Slovenian enterprises [6], which typically determined the developing capability and competitiveness of the large number of SMEs.

MER Evrocenter [7], edited by Professor Belak, published the results of many years of activities and co-operation of the MER research group, as the book repeatedly refers to the role and impact of synergy effects within and between enterprises operating in the new and old EU Member States, as a new element of competitiveness. This is how the possibility of SME involvement in networks, associations and clusters has been brought into the picture as an instrument to boost competitiveness.
Professor Lubica Lesakova describes a practically similar situation in her presentation analysing the situation and future opportunities of SMEs in Slovakia [8]. The number of employees, market share, export figures are used to illustrate the economic role of SMEs, while the main factors of competitiveness are summarised as follows:

- To implement an effective management scheme
- To possess skilled personnel and management staff
- To apply for innovation, modern and efficient technologies
- To achieve high quality of their products and services
- To put more effort into networking, subcontracting and developing clusters

In the last few years, attention has moved towards family businesses (FB) in the Central and Eastern European countries, co-operated with MER Net. In this context, in 2003 the following objectives were set as a target for research [9]:

- The situation of FB in cooperative countries and their importance for the development of international economies
- The state of existing research and consulting databases including data about FB
- Particularities of external and internal factors influencing the development and operation of FB

The above short and fragmented summary illustrates the research environment in which Budapest Tech SME research team has been working for more than ten years now.

2 Sampling and the Method of Survey

The sample of businesses used in the survey comprised independent legal entities employing no less than 10 and no more than 49 persons, and having net annual sales revenues not exceeding a HUF amount equivalent to EUR 7 million, or a balance sheet total not exceeding a HUF amount equivalent to EUR 5 million.

When launching the survey, we selected the businesses for the purposes of the questionnaire from the database *Magyar cégek 2005* by Dun & Bradstreet Hungária Kft with a view to the number of people employed, the business activity and representativeness, based on the 2004 data of the Central Statistical Office.

At the start of the survey, a database consisting of 300 companies was set up, and a questionnaire was forwarded to the majority of the businesses in attachment to electronic messages, and the minority received it by post or in person.
The questionnaire is 20 pages long, and endeavours to cover all fields of corporate operation. The questionnaire was compiled partly on the basis of a questionnaire elaborated by the Centre of Research in Competitiveness at the Corvinus University of Budapest, adapted to the small businesses.

Representativeness of the database was examined in the light of certain characteristic features which can be compared with the available economic statistical data:

- Distribution by staff numbers
- Core businesses of the companies
- Regional distribution of businesses

The questionnaires were sent to companies active in three characteristic sectors including a large number of businesses. The selected sectors included: manufacturing, trade and repairs, real property agency and business services.

3 Findings of the Survey

3.1 Macro Economic Factors of Competitiveness

Reasons for Uncertainty in Corporate Operation

In Hungary, the most important reason for uncertainty is the political factor, followed by domestic markets and social changes. Foreign markets, technical and technological development and foreign suppliers can be regarded as relatively stable environmental segments.

Effect of the Individual Kinds of Taxes on Competitiveness

In connection with the individual kinds of taxes and rates, we asked the respondents about their effects on competitiveness. Most businesses consider social security contribution (50%), corporate business tax (43.75%) and personal income tax (43.75%) as the predominant factors. The majority consider the simplified business tax (62.5%) and customs duties (50%) as having no impact on competitiveness. 43.75 per cent of the businesses considered local business tax as having medium impact.

Major Effects of Macro-Economic Factors on Corporate Operation

Small businesses consider the domestic political situation (68.75%), the domestic economic environment (62.5%) and the activity of the government (62.5%) as the key factors affecting their business activities. Changes due to accession to the European Union (37.5%) were evaluated as a favourable macro-economic factor by most of the companies.
Effects of the Macro-Economic Environment on Businesses

Certain significant economic factors of the macro-economic environment were also evaluated separately from the point of view of corporate operation. The findings show that reliable monetary policy (50%) is the only one of the listed factors that was regarded as a definitely supporting factor. The second most favourable factor was accession to the EU (37.5%). The factor considered by the respondents as the third most favourable was an upward shift in the HUF exchange rate band (31.25%).

All respondents considered rise in two of the unfavourable factors – inflation (100%) and VAT (100%) – as detrimental to their businesses. The third such factor included general government deficit (62.5%). Postponement in the adoption of the euro (56.25%) and the specific level of the statutory minimum wage (50%) were seen as neutral factors.

Trends in Domestic Markets in the Past Three Years

The majority of businesses thought that their turnover had been growing in the domestic market.

Competitors

The majority of companies know their competitors and are aware of their financial standing. The majority of the competitors (62.5%) have 4-5 major competitors. We requested the companies to compare their own performance on the basis of 45 considerations with their most powerful competitor, and indicate the fields they wished to improve.

In what follows, our survey tackles the best, the worst and the five areas most in need of development. The majority of businesses are of the opinion that their contacts with the consumers are the most successful field, followed by flexible reaction to the changes in consumer needs. Next come accuracy in supply and product quality.

The weakest points in comparison to competitors are profitability, market share, and presence in export markets, technological standards and incentives to innovative sales. The fields they wish to develop do not necessarily coincide with fields in which these businesses fall behind their competitors. Among the fields to be developed, cost-efficiency was indicated by most of the respondents, followed by technological standards, quality of goods, market share and level of profitability.

Fundamental Goal of the Company

37.5 per cent of the businesses considered the provision of the best possible service to consumers as their fundamental goal. 25 per cent of the respondents envisaged the realisation of the highest possible profit as their fundamental objective.
Taking the most money out of the company was seen as the primary goal by 18.75 per cent. Only 6.25 per cent of the respondents considered employee satisfaction as a fundamental goal.

**Significance of Factors Affecting Operation**

The respondent businesses considered good relationship with their customers as the most powerful factor affecting their operation (92.2%). The second most important factor included financial resources (81.3%). Further significant factors included acquisitions (76.6%) and good relations with the suppliers (73.4%).

Accession to the EU (26.6%) and foreign market competition (45.3%) were factors considered to have the least effect on their operation. The 26.6 per cent assigned to accession to the EU is so much the more strange as in an earlier issue, this factor was considered as one of the most important elements.

**Response to Environmental Changes**

In the interviewed businesses’ opinion, the most frequent response to environmental changes is the timely realization of changes and preparation in anticipation for them in good time. This was indicated by 31.25 per cent of the businesses. 18.75 per cent of the businesses claimed that they had recognized changes but could not adjust because they failed to find appropriate solutions.

12.5 per cent of the participants in the survey realized environmental changes late. This means that 43.5 per cent of the businesses reacted on environmental changes extremely well, however, if subsequent reaction is also considered appropriate, 68.75 per cent of the businesses may be deemed to have good adaptability. This favourable picture is made slightly more subtle by the fact that in the course of completion of the questionnaire, the businesses evaluated themselves.

### 3.2 Micro Economic Factors of Competitiveness

**Corporate Strategies**

Only 12.5% of the businesses have written strategic plans and most of them do not follow any market strategy at all (56, 25%). 6.25% of those with a corporate strategy withdraw, 12.5 % have a defensive strategy and 6.25% follow an aggressive strategy. None of the companies in the survey has a focusing strategy to follow.

**Market Strategies**

In connection with the implementation of a market strategy the respondents evaluated three main objectives. For the majority, the most acceptable objective was moderate growth (62.5%). This is followed by the retention of market share (25%), whereas aggressive growth was valued only by a smaller group (12.5%).
Business Plan

Most of the businesses included in the survey do not make business plans, 18.75% of them do not make a business plan at all (1). 25 per cent make plans in their heads but they do not discuss those with their colleagues (2). Sometimes plans are put down on paper, but in 25% of the businesses it is not harmonized with anybody (3). 6.25% of the businesses prepare production, purchasing, labour, cost, performance and liquidity plans on a regular basis (4). Businesses make an analysis of the regularly prepared plans and explore the reasons of the deviation from the plan (5) in 6.25% of the enterprises. After detecting the reasons for deviating from the plan’s data they implement the necessary measures (6) in 12.5% of the businesses.

Capacity Utilization

31.25% of the businesses included in the survey utilize the capacity only to a small extent, 56.25% of them think they utilize it properly, and 12.5% have insufficient capacity.

Capital Investments

Most businesses in the survey (75%) had an investment project exceeding HUF 5 million in the last three years. The invested funds were used for buying a new business facility, an office, machinery and vehicles. In 81.25% of these investments, loan was used at least in part for funding. Borrowing is not seen as a serious problem for most of the small businesses (61.25%), however, because of the high interest rates and insecure future they do not prefer long term loans. 61.25% of the businesses have investment plans for the next 3 years with a value over HUF 5 million.

Tender Applications

12.5% of the businesses in the survey participated at some or another kind of tenders and had been granted support. Their applications were successful in all the cases and the allocated funds had been used.

Business Lines, New Products and Services

31.25% of the businesses pursue a homogenous activity. 37.5% of the businesses are engaged in two different business lines, 18.75% of them in three lines, and 12.5% in more than three lines.

62.5% of the businesses launched a new product in 2006. New production technology was introduced at 25% of those asked in 2006. According to the answers given by the businesses, with 75% of them the parameters of products and services do not change frequently.
Environmental Projects

None of the businesses surveyed have an environment centred management system. In the last 5 years 43.75% of the businesses have implemented projects with the purpose of environmental protection (e.g. building a sewerage system)

The environmental performance of the businesses questioned depends primarily on the regulations of the authorities. The second most important factor is the environmental legislation of the European Union. The third most important factor is the visible problems of environment. The most important driving engines of environmental investments are official expectations coming from various places. Improvement of the company’s image and the market pressure of competitors impose the smallest motivating force on the businesses

Employees

62.5 of the businesses recruit new employees by the help of advertisements. 25% try to find new work force via friends. 12.5% of the businesses have already used the services of employment offices.

We asked the persons filling in the questionnaire to rank the 6 features below according to their relevance in selecting the new employees. The ranking according to the survey: the practice and experience of the employee, the qualification of the employee, sympathy, age, how does he/she fit into the current staff, references.

According to the employers, it is relatively difficult to find the necessary experts in the labour market. 56.25% of the managers of the businesses in the survey studied in vocational secondary schools or grammar schools. 31.25% of them graduated from a college/university. 12.5% of them have qualified as skilled workers.

Areas in Need of Developing the Improvement of Efficiency

In order to improve the efficiency of the business activity customers think that there is still a lot to be done in the transformation of cost management, trading /marketing and sales. So as to reach good management more than just the average changes will have to be introduced in the field of production, technical development, finances, top management and payroll management. Organisation development, information management and accounting are those areas where company experts feel the least necessity for changes.

Supplier Performance

The performance of supply on time is 84 per cent. In other words, corporate managers experienced some or another kind of delay in 16 per cent of the cases. Problems related to supply quality arose in 18.75 per cent of the cases. In terms of volume, 90 per cent of the performances are correct, i.e. problems are found with the volume of freight on every tenth occasion. Invoices accuracy is 89 per cent.
Thus problems are encountered in connection with invoices in 11 per cent of the cases.

84 per cent of the freight was found to be undamaged. This means that 16 of 100 cargos arrive at their destinations in a damaged condition. In 56.25 per cent of the cases more than four suppliers were used, 31.25 per cent of the businesses worked with four suppliers, and 12.5 per cent had less than four suppliers.

Payment Discipline

68.75 per cent of the respondent businesses claimed that they had never or very rarely have paid their suppliers late. However, 12.5 per cent of them pay regularly or frequently late. A survey of the payment discipline from the seller’s perspective reveals that 31.25 per cent of their customers are regularly late with payment, while 37.5 per cent answered that their partners performed on time and late payment was rare. Default penalty interest continues to be the most frequently applied sanction for late payment. The second most frequently used sanction is that new orders are performed only after the debt has been paid. Customers who pay late may subsequently purchase goods only for cash from every fourth business. Only 12.5 per cent of the businesses use the possibility offered in legal sanctions. The customer is no more provided service and option is applied only in extreme cases.

3.3 The Way to Improve the Competitiveness of SE

The primary aim of the government’s financial assistance for the furthering of the development of small and medium enterprises is to create such economic conditions that ensure the improvement of competitiveness and the offsetting of competitive disadvantages. The following list includes some of the methods by which the government assists SE development in keeping with EU principles [10]:

- The potential assets of the government for the improvement of competitiveness
- Creating a system of sources of cheap loans: banking interest rate subsidies
- Loans encouraging investment
- Loans enhancing operational efficiency
- Tendering systems
- Financial assistance from the EU
- Financial assistance that encourages the economy
- Export subsidies
- Ensuring a domestic outlet background
Conclusions

Our assumptions made on the basis of an incomplete evaluation of the completed questionnaires that have been returned reflect our very first impressions. Stressing the above, we wish to point out the following statements and correlations.

Small businesses active in manufacturing predominate in the sample. Rural businesses are underrepresented in the sample. During the survey, businesses considered developments in the business environment as definitely favourable. In addition to reporting increasing uncertainty, they deemed Hungary’s political climate, domestic markets and social changes as having marked effects.

One and a half years after Hungary’s accession to the European Union, SMEs cannot perceive major impacts of accession, or blame the prevailing political situation for all changes. Small businesses do not capitalize on the opportunities offered by the European Union, and do not make efforts to apply for EU grants and funds, or attempt to penetrate new markets. In my opinion, this is due to the lack of information. In our opinion, the companies participating in our survey are not aware of the opportunities available for them.

Among the economic policy factors, a reliable monetary policy has the most benevolent impact on the operation of businesses. Inflation and VAT-regulation are considered to have the most unfavourable effects.

References
