

Chapter 31

Innovations and Financing of SMEs, Part II: Case Study of German SMEs in 2010

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ABSTRACT

Financing is one of the most critical boundaries for the establishment and growth of a Small and Medium-sized Enterprise: SME (Moore, 1993). This chapter describes traditional and non-traditional financing opportunities for SMEs in Germany by focusing on its applicability. The disclosure of financial business information and giving a say to an equity financier is a difficult topic for owners of Small and Medium-sized Enterprises (SMEs), because these companies are often run as a ‘one-man-show’ (by a single manager) and this person identifies itself with the company. The request for external funds is in that perspective still regarded as a disability of a business to be self-financed. A comparison of the organisational structure of a SME and that of a Large Scale Enterprise (LSE) reveals the structural weaknesses in terms of research and development (R&D) activities. While LSE have an extra department, budget and procedures to develop product and process innovations similarly to a knowledge push, in SMEs, innovations are often originated from customers—similarly to a need pull process (Tidd & Bessant, 2009). Furthermore, CEOs and customer contribute to a great extend to innovations in SMEs (BDI, 2010). The results of an online-based survey presented in the BDI-Mittelstandspanel 2010, show that less than 13% of innovations are originated by external scientists, R&D organisations and consultants. This proves that external R&D sources (to compensate missing internal resources and structures) are rarely employed; impeding or slowing down the development of innovations.

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INTRODUCTION

There are various financing options available to Small and Medium-sized Enterprises (SMEs) that can be classified generally in traditional and non-traditional financing as introduced in the previous chapter. Due to a rather conservative attitude towards dependence on shareholders, non-traditional financing options (e.g. private equity) are not very common within SMEs (especially in Europe); aggravating the amelioration of the company's financial structure and therefore creditworthiness. In order to get a rather holistic view, a case study based on a survey presents the structural development and economic situation of SMEs- and its financiers in Germany.

German Banks offer SMEs rather medium or long-term bank loans than project related loans. Therefore, the control and monitoring of banks over the efficient use of borrowed money is low compared to project financing. Looking at finance as an 'Organisation's Creative Area' (OCA), non-traditional financing can be more suitable to develop core competencies and promote product innovations. Sometimes they are even the only financial source available when it comes to high-risk project financing. In order to support SMEs and generate a high profit, Private Investors are more likely to take part in project related (e.g. for a product innovation) financing. The level of control and monitoring, in order to ensure that a product or service innovation is turned into money, is high. By the financial and managerial support, Private Investors especially promote the 'knowledge push' innovation model. Due to lack of resources, the 'knowledge push' innovation model is rarely used compared to the 'need pull' innovation model in which the innovation is originated from customers.

BACKGROUND

The financing sector in Germany is highly competitive with the three types of banks (private banks, banks governed by public law and cooperative banks) trying to maintain and gain market share and the non-traditional financiers (private equity and debt financiers). Therefore, the credit conditions have been favourable in Germany during the last decades. CEOs of SMEs tend to have a conservative attitude concerning additional shareholders and financial independence. Therefore, medium- and long-term bank financing has been in Europe (especially in Germany and France) a major financing option for SMEs. However, with respect to the financial crisis of 2008/2009, the credit conditions (especially risk premium) changed, impeding the availability of loans. While financiers accuse SMEs for having a weak financial structure, SMEs representatives accuse the financiers (especially banks) for the so called 'credit crunch' with unacceptable credit conditions.

SME-FINANCING AND INNOVATIONS

Financial Resources and Innovation Boundaries of SMEs

The BDI¹ announced in its latest report (BDI, 2010), based on an online survey, the developments and weaknesses of German SMEs in 2009 and expectations for 2010. These weaknesses include innovative boundaries, based on fundamental problems of the organisational structures and resources. Therefore, finance can also be regarded as an 'Organisation's Creative Area' (OCA) that helps develop core competencies especially with the support of Private Investors, controlling and monitoring the realisation of product and service innovations.

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