

# Research of Competitiveness Factors of SME

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*Abstract: An SME is able to cope with the global challenge if it realizes reliable, balanced and high-standard operation in its business. There are some management and organizational methods increasing the competitiveness of SME. Controlling as a management tool and management function as well as a factor affecting competitiveness came more into focus. Outsourcing of activities not belonging to the main profile of the enterprise seems natural for most SME-s. Family business as the driving motor of the business can bear bigger loads than SME of similar sizes but not organized around a family.*

*Keywords: competitiveness factors, management methods, family business speciality*

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## 1 Introduction

The challenge of the 21<sup>st</sup> century for SME-s is global competitiveness. This means that customers need to be provided with constant and reliable products and services of a recognized quality, while the market environment is characterized by global competition.

An SME is able to cope with the global challenge if it realizes reliable, balanced and high-standard operation in its business.

The Institute for Organisation and Management of the Budapest Tech where an SME research and development team is operating – in co-operation with other research institutes in Hungary and abroad – puts great emphasis on investigating the role of controlling in increasing the competitiveness of businesses.

One of the surveys of BT SME research group, currently in progress, analyses competitiveness, focusing on EU membership and a new competitive environment created by globalisation.

The operational and organisational conditions of competitiveness are manifold and involve each specialist area as well as management and direction itself.

SME research was started in 1994 at the Budapest Tech (BT). In 1993 at a summer university forum held at the University of Economics (WU) in Vienna and at a consequent international conference attention of the participants from reform countries was drawn to the increasing importance of the SME-s in developed European countries. At the same time an international research program called MER ('Management, Entwicklung, Razvoj') was launched at the Maribor University in Slovenia, namely under the guidance of Prof. Dr. Janko Belak and with the effective cooperation of Prof. Dr. Josef Mugler from Vienna. In addition to Austria, Switzerland, and Germany almost all of the reform countries were represented in the program. On behalf of the Bánki Donát Polytechnic, the legal predecessor of BT, a still existing Organization and Management Institute (SZVI) was the one to take part from the beginning in the researches and the MER cooperation.

At the beginning of the 90's our experiences gained in the neighbouring countries and domestically confirmed our view that great emphasis needs to be placed on SME research and development. Therefore SZVI included enterprises, and within this SME research in its program of education development and research [3].

The SZVI research program features the following activities and results [4]:

- Establishment and introduction into education of a new subject

- Literature review

- SME counselling

- Surveys done about SME-s

In the framework of the SME research conducted at Budapest Tech we launched a survey of SME in 2002-2003, focusing on the main characteristics of family businesses (FB), as well as their position and prospects in Hungary. Based on the theory and technical literature available in 2002, in 2003 we analysed 200, and in 2004 further 200 businesses in practice, the majority of which were family businesses. This report summarises the research results of the last three years.

The former theoretical and research projects contained in publications confirmed also, by the analysis of approximately 800 family businesses, our intention to continue researching the position of the family businesses analysing their development options.

The survey described below did not target at agriculture, or family farms operating in agriculture; it covered the other sectors of the economy.

## 2 Research Method

There were several methods applied during the SME researches and developments. Our selection from among the possible methods was greatly influenced by the fact that we had no or only rather scarce external financial resources available to us. The test sample was determined and picked also accordingly. In this respect, however, there was a favourable condition serving us: both the number of students and their circle of acquaintances cover the whole country. Accordingly, the enterprises selected and inspected by them cover – at least in a geographical sense – the whole country.

We have used our resources so far to apply the following research methods [6]:

- Interviews and studies by students

- Personal experiences gained by counsellors

- Quick test disclosing the application of organisation and management methods

There were also several surveys were conducted in the subject of SME-s. While education was running, students were included in the program by receiving interim practical tasks in connection with the theme of SME-s. Such were for instance:

- Launch of SME-s

- Business planning for SME-s

- Investigation of SME life lines

- Investigation of family businesses

Since almost 400 students were studying ‘Business Set-Up’ in the past years, thus the number of SME case studies were available to us to carry out research thereon.

Approximately 100 SME-s have completed the questionnaire (quick test) sufficiently for the research too.

We involved students in their last year, participating in the enterprise management course, to visit SME-s, acquaintance or local community relations or at random selection.

The students conducting the survey came from almost all parts of the country, from small and large settlements. Thus, in our opinion, the enterprises found and analysed by them represent the Hungarian average well among the SME-s.

A case study was prepared on each business on the basis the criteria indicated above. The institute’s research group later analysed this case study. The analysis was made with the method of individual interpretation and evaluation, with occasional supplementary information, and not with a mathematical statistical method. Thus the most important factor in evaluating phenomena and tendencies behind figures was finding the stress, and highlighting the essential information.

SME counselling began in 1994 when the German RKW (Rationalisierungskuratorium der Deutschen Wirtschaft) came to Hungary. Three members of the present research group of our Institute took part jointly in RKW's programs, and we carried out SME counselling all over the country for years. Considerable experiences were gained with such counselling and related at different domestic and international forums.

This report provides a synthesis of the results obtained with various research methods to date. Of the factors of competitiveness, we would like to highlight controlling, as we analyse its implementation opportunities in the SME sector, primarily among small enterprises.

### 3 Analised Factors Influencing the Competitiveness

The factors influencing competitiveness of SME-s can be divided into two groups, into external and internal factors.

External factors:	Internal factors:
Employment	Marketing
Productivity	Innovation
Capital supply opportunities	Productivity
Globalisation	Knowledge-based development
EU	Capital supply
Business relations	Management, organisation, structure
Alliances	Cost-efficiency
Networks	Compliance

Table 1  
Influencing factors of competitiveness

Measuring competitiveness is the most difficult task. A few values, indicators, or characteristic features that can be quantified and accessible, or are not quantifiable or accessible at all, or are difficult to quantify or access, have to be identified at corporate level. These measuring points are the following:

- Revenues, Export, Profit, Market share, Productivity,
- Technical standard, Corporate value, good-will, Image,
- Customer satisfaction, 'Value' of the product, service

The structure, aspects and factors of the analysis of globalisation and competitiveness outlined in this study represent an initial phase of a longer research programme, focusing clearly of SME-s and specifically small enterprises.

## 4 Competitiveness of SME in Hungary

On the basis of the surveys, SME-s compete in the following areas:

- Retail trade,
- Repair, assembly and personal services for the population,
- Real estate brokerage, real estate trade,
- Restaurants, catering,
- Intellectual property (consultation, software development),
- Travel arrangements, holidays,
- Agricultural farmer activities (plant cultivation, animal breeding).

The composition of enterprises participating in the surveys more or less reflects the composition according to activity.

According to Hungarian statistics, most of the SME-s are operating in the commercial and service sectors.

It is an important factor that currently we do not analyse agricultural SME-s.

### 4.1 Experiences of Application of Certain Management and Organisation Methods

Without trying to be fully comprehensive, we analysed the following areas:

- Planning,
- Marketing,
- Quality assurance,
- Organisational methods,
- Controlling.

Planning was analysed at strategic and business (annual) planning levels. We concluded that of the surveyed SME-s 37% had a written strategic plan and 46% had written business plan.

In terms of the strategic plan, this proportion is acceptable, but the written form of the business plan shows a very low figure. Among the analysed SME-s, strategic thinking was not missing, but they did not consider that it was important to put it into a written form. A bigger insufficiency is the lack of registration of short-term business planning. It cannot always be explained with the uncertainty of planning, much more with the lack of professional business planning skills and underestimating of the importance of planning.

The presence of planning in some separately analysed enterprises confirmed our belief that a written strategy and business plan are both very useful for an enterprise, irrespective of which SME segment it operates.

In terms of marketing, 40% of the enterprises have an individual or organisation who and which fulfil the marketing function. Of the remaining 60%, 18% plan to create and operate a marketing group or organisation in the near future.

This proportion also indicates that SME-s consider marketing, i.e. management of market activities, very important. However, in terms of their future plans, the 18% enhancement indicates rather reserved development ideas.

The focus on marketing activities is explained with the direct use of market activities, aimed primarily at advertising activities and sales incentives.

In the area of quality management, very few enterprises, only 15%, have an ISO certified quality assurance system.

On the other hand, the future image is promising: of the other 85%, more than one-third, i.e. in total 30% plan to introduce an ISO quality assurance system in the future. The introduction of a quality management system is mainly motivated by their intentions to become a supplier or act as a supplier, it is more rarely considered part of a separate market image.

In terms of the application of various organisation methods, we have limited information. The analyses covered only a few special methods selected at random.

Although the BPR method is not completely unknown among SME-s, only a small proportion (approximately 10%) have applied it, or are willing to reorganise their business processes.

Regular and continuous development of operation is an ordinary and right method for the majority of enterprises (approximately two-thirds). The Kaizen method with similar contents as a definition is almost completely unknown though.

Outsourcing of activities not belonging to the main profile of the enterprise seems natural for most SME-s. However, this does not mean that outsourcing is a fully comprehensive deliberate activity. It rather means that entrepreneurs manage their external resource requirements on the basis of the principles of needs and there is no plan for how to outsource their activities. The controlling function is present in 20% of the analysed enterprises, but it does not mean that 20% of the enterprises have created a controller's function, or a controlling organisation. Of the remaining 80%, only 11% plan to establish the controlling function in their enterprise in the near future.

## 4.2 Outsourcing

Outsourcing of activities not belonging to the core activities is the result of natural distribution of work among SME-s. It is a general practice that an SME does not conduct the following activities in its own organisation but uses them as an external service:

- Legal representation, Legal consultation,
- Accounting, Tax consultation, Business and financial consultation,
- Market research, survey, Training, further training,
- Compilation of loan applications and other applications.

Outsourcing of these activities is not a deliberate activity, but a kind of feature of SME-s. They cannot economically create and operate capacities that would be specialised for such activities within their organisation.

Naturally, various resources are also outsourced in the material processes, which represent 'real' outsourcing in this context, but for the purpose of this survey, these relations are not very important.

The quality and reliability of activities outsourced for competitiveness are very important. Let us just imagine new environmental conditions involving global competition, such as

- A tender for raising funds,
- International law, accounting and tax regulations,
- New capital investment and loan opportunities,
- Joining supplier systems.

The outsourced activities are also different from each other that they contain some regular and irregular occasional activities. For example, accounting is typically an outsourced continuous activity, while taking loans or legal representation take place occasionally.

A key factor of the competitiveness of the Hungarian SME sector is cost-efficiency and productivity. The controlling system has already proved to be useful in the development of cost-efficiency in the entire world, and it has become a widely used useful and indispensable tool of the management of large companies.

There is also a theoretical possibility to outsource the controlling function, but according to our experiences to date, SME-s do not use this opportunity very often. Regular consultation, relating, for example, to accounting and business consultation services, would be ideal to encourage the manager of an enterprise to use controlling tools. Another possible solution is the adoption of a complex enterprise system, containing also the right management methods and tools. Such

a system is a franchise system, for example. Below, we shall review the controlling and franchise situation and their mutual opportunities in terms of improving the competitiveness of SME-s.

### **4.3 Controlling in SME-s**

One of the factors of competitiveness is cost-efficiency, which is required for real processes, as well as planning and controlling of costs.

Controlling as management tools fulfils the following main functions [2]:

- Planning,
- Measurement,
- Comparison,
- Evaluation.

These functions form a regularly repeated closed system, considered a sub-system of management, and discussed as a management function on its own in the technical literature.

In the controlling system, cost controlling is very important, which is suitable to increase cost-efficiency and thus, competitiveness.

Empirical studies and theoretical and literary researches have proved that controlling contains planning, coordination and control functions. Empirical signs indicate that it also plays a role in management. Development from an economic operation model to the management model indicates that controlling, an integrating management function, develops towards a new model.

On the basis of the results of empirical researches, the theoretical approach can be assumed. Thus controlling is:

- strictly and mainly practice-based,
- dominated by profit-orientation concerning its objectives,
- has an economic operation approach,
- its theoretical basis originates from economic operation, too,
- and its main functions are coordination and an information system.

As it was indicated above, the controlling function is present in 20% of the analysed enterprises. However, it does not mean that these enterprises have created a separate controller's position, or controlling organisation.

A closer study of individual cases has indicated that the manager of an enterprise requires regular generation and availability of information relating to the controlling area. Most often the information is generated by the accountant or



business consultant of the enterprise, and the controlling report, i.e. the inclusion of the information in a system and its interpretation – is also prepared with external assistance. It happens very rarely that the entrepreneur's own administration prepares the information and the controlling report is prepared by a competent expert – controller – or the manager himself.

Controlling is a professionally demanding function, involving an expenditure, the yield of which is not always seen directly by the entrepreneur. This explains that of the 80% of SME-s without a controlling function, only 11% plans to implement a controlling function in their enterprise within the near future.

At the same time, the personal interviews have also revealed that the managers of such enterprises consider themselves rather cost-sensitive and economic persons, who do everything to increase cost-efficiency.

Such a low level of the presence of the controlling function among the SME-s, can be explained best with the fact that the qualifications of the managers of the analysed enterprises (a sample of 400 companies) show a rather varying picture. 30% of the managers have diploma, 42% have a secondary qualification.

Assuming that each SME manager with a diploma knows exactly what controlling is and intends to apply it too, the proportion of existing and planned controlling functions is close to 30%. Although attempts for cost-efficiency can be expected from managers with secondary or lower qualifications and it can actually be observed, but the solution, i.e. application of a controlling system or function does not even occur to them without the relevant knowledge or information.

Thus, the presence of a need does not point to controlling, but to an economic system that somehow contains both the controlling function and system.

#### **4.4 Appearance of Franchise and its Potential Role in Increasing Competitiveness**

Franchise is widely used in the entire world, and it has been introduced to Hungary recently, too. Franchise is a type of enterprise based on close cooperation, in the framework of which the franchiser, i.e. the owner of the system provides a complex system, established on professional and trading considerations, and successfully tested in the market environment, with a full scope of training, use of a brand name and continuous control and assistance to the franchisee, who operates the system in his own enterprise at his own profit and risk, according to the requirements of the franchiser, on the agreed area and for the agreed period, in exchange for a fee [7].

However, there are several definitions of the franchise concept. In America, the business aspects are highlighted most, but there are other ideas, too, that underline support and assistance in terms of franchise. The German literature looks at franchise mainly in terms of organisation.

A business franchise can be characterised best by saying that in this framework the franchiser does not only provide the use of a product service or trade market to the franchisee, but also makes available the strategic, marketing, quality control, accounting and other business information required for the successful operation of the whole enterprise to the franchisee.

The majority of the franchise system operating in Hungary are in the trade and service sectors, which is the sector containing most SME-s. Disclosed elements of the franchise contracts also indicate that in many cases the low amount of start-up capital clearly encourages SME-s to use already tested franchise ideas in their enterprise instead of implementing their own individual ideas.

In order to increase competitiveness, cost efficiency and be successful, the franchise contract should be extended to the management functions as widely as possible. This means the expansion of rights and obligations of the franchiser in this context.

Primarily, planning, accounting, control and feedback functions require a lot of attention, as these are the weak points of the Hungarian SME-s.

A controlling system required and practiced by a franchiser could also help franchisees, having little information in the area of controlling to use a modern and effective tool for such purposes. This solution could also mean the extension of controlling, i.e. controlling outsourcing.

## **5. Competitiveness Speciality of FB in Hungary**

In accordance with the Hungarian technical literature, the FB criteria are the following [1]:

- At least two people of the family participate in the business
- either in the owner's position, and/or
- with an involvement in the management of the business, and/or
- with an involvement in the daily operation of the business.

It was possible to evaluate in total 378 SME-s, of which 322 SME-s satisfied the criteria of FB. This ratio corresponds to 85.2%.

The quantified results of the analysis are contained in Table 2 [5].

The figures indicate the following phenomena:

Most FB-s were founded in the first half of the 1990s, and these days they mostly operate as unlimited partnerships or limited liability companies (83%), in almost equal proportions. Almost all enterprises were established for an indefinite period

(98%) and, since with a few exceptions they are still active, it indicates more thorough preparations. We have found FB-s among the businesses that operated well, and have survived several generations too.

Points of views		FB	%
Date of FB establishment	before 1990	43	13
	1990-95	139	43
	1996-2001	122	38
	2002-	18	6
Scope of activities	service	147	45
	trade	108	34
	industrial prod. and sale	67	21
Origin of the FB property	own	108	34
	family	207	64
	external resources	7	2
Owners of FB	family	570	92
	external	50	8
Managers of FB	family	634	92
	external	57	8
Employees	family	370	21
	external	1411	79
FB viability	stable	193	60
	uses credit to develop	48	15
	unstable	81	25
Technical level	out of date	212	66
	adequate	80	25
	up-to-date	30	9
Owner's motivations	committed, purposeful	162	50
	wishes to change	160	50
Owner's qualification	degree	80	25
	secondary qualification	180	55
Imagined future for the family	civil life (middle layer)	100	30
	welfare, prosperity	222	70

Table 2  
Results of the analysis of FB

The origin of assets illustrates well the role of family business and economic organisations consisting of two or more members in the market. Nearly 70% of the analysed FB-s had assets originating from the family and several family members. Business were started from family capital, establishing business relations between brothers and sisters, parents and more distant relatives, in this order of frequency. Having analysed the scope of activity, we concluded that most

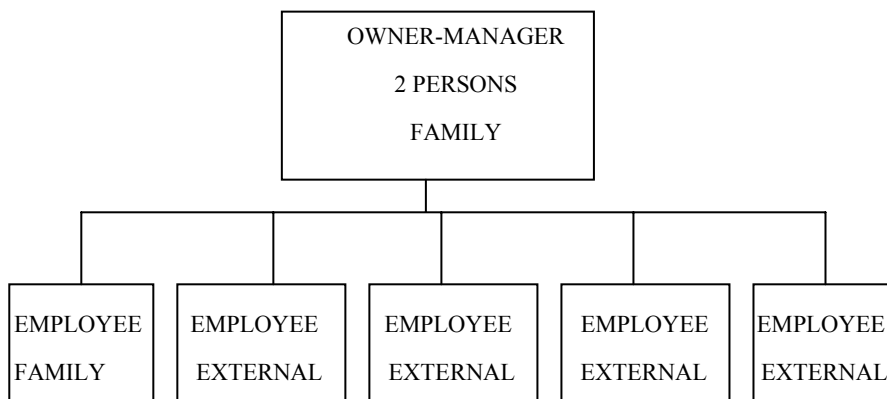
FB-s operated in services, followed by trade and the industrial sector. Almost all FB-s are managed by a family member or family members who is/are owners in the business.

There are very few external individuals among the owners, representing only 8%. The composition of management is similar.

There is not a lot of different in the number of employees of the FB-s between sectors. The fewest employees work in FB-s engaged in services. Each FB has economic staff management and employs the minimum number of staff required for their activities. According to the origin of employees, 21% have family relations and 79% are external employees.

Looking at the number of FB-s and number of managers and employees, the average FB structure can be seen on Picture 1.

Approximately 25% of owner-managers have a degree, 55% have secondary qualifications, and experts with a lot of practice are present only in FB-s established long time ago as managers.



Picture 1

Structure of average Hungarian FB

The majority of FB participants (approximately 80%) are aged between 30-55 years. In these businesses the issue of succession occurs less frequently than in other FB-s established a long time ago, in which the owner is over 60 years of age or more. In this category, the owners would prefer to maintain the business within the company. In fact, family businesses where succession has occurred as an issue succession within the company would be preferred.

Tendering is more frequently applied for selecting the management in recently founded FB-s, influenced by external owners, too. This step may also change the future of FB-s compared to FB-s where management remains in the hands of the family.

Approximately two thirds of the analysed businesses consider their economic position stable and outlooks positive. At the same time, only 50% of the owners are fully committed to their own business, the other half would like to make fundamental changes and intend to change the current operation and directions of the FB.

In approximately two thirds of the FB-s, the technical standards, the applied instruments and procedures are out of date and obsolete, they are adequate in approximately 25%, and only 8-10% of FB-s could be considered up-to-date.

Concerning economic stability and development, only 15% of FB-s use loans for development, 60% seem stable and 25% consider the position of their business unstable. 50% of the businesses cover their investment needs from their own families.

The future vision of the family and business also involves a link to primarily financial welfare and wealth. This is the specific objective for 70%, and only 30% said that their intention was to provide a good life for their families. At the same time, it is perhaps not surprising that the interviewees were reluctant to talk about the financial position of their businesses or families.

Concerning experiences, we should note that we have studied a few businesses that have covered the same path as known in the experience of Western countries as an FB tuning into a multinational enterprise sooner or later, or already operating as an international business. Studies of clearly successful exemplary businesses are analysed further, and we intend to use the research results in future research activities as well as education.

## **Conclusions**

Certain management and organisation methods are successfully applied at SME-s.

The presence of planning in some separately analysed enterprises confirmed our belief that a written strategy and business plan are both very useful for an enterprise, irrespective of which SME segment it operates. The focus on marketing activities is explained with the direct use of market activities, aimed primarily at advertising activities and sales incentives. The introduction of a quality management system is mainly motivated by their intentions to become a supplier or act as a supplier, it is more rarely considered part of a separate market image.

Outsourcing of activities not belonging to the main profile of the enterprise seems natural for most SME-s. However, this does not mean that outsourcing is a fully comprehensive deliberate activity. It rather means that entrepreneurs manage their external resource requirements on the basis of the principles of needs and there is no plan for how to outsource their activities.

A closer study of individual cases has indicated that the manager of an enterprise requires regular generation and availability of information relating to the

controlling area. Most often the information is generated by the accountant or business consultant of the enterprise, and the controlling report, i.e. the inclusion of the information in a system and its interpretation, is also prepared with external assistance.

Family business are typically small and medium enterprises. Our statements relating to certain features of family businesses could be summarized as follows.

The scope of activities of family businesses, in accordance with the SME sector's nature, includes mainly services, trade, and to a smaller degree production and sales activities.

Their capital adequacy, terms of and possibilities for receiving credit are very unfortunate, their technical level is lower than the average, and is not modern. Capital restrictions present serious difficulties to the development of family business and the increase of their compatibility, especially under the current economic conditions - considering stagnation, or a slow growth. With respect of the system of regulations and available supports, only agricultural family businesses enjoy slightly better conditions.

It can be seen from the survey of human resources of family businesses that despite any unfortunate external conditions, family relationships and personal resources have rendered recently many family businesses into successful enterprises. This shows that the family as the driving motor of the business can bear bigger loads than SME of similar sizes but not organized around a family. This is the most important lesson of our researches so far.

If our further studies confirm this phenomena then distinguished legal and financial treatment of family businesses may rightfully demanded of both the society and the economic management.

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