

Market Failure or State Failure: a re-assessment of the case for SME policy

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'Our review of small business policy instruments indicates that, with a few exceptions, results are unimpressive - and even for the exceptions, they are fairly marginal in their effects. There is no reason to suppose that if most subsidy and assistance programmes were abolished altogether, it would make a significant difference to the shape and prosperity of the SME sector anywhere' (Bannock, 2005; 133)

Principal Topic Researchers, policy makers, support agencies and SME groups have a tendency to assume that there exists a strong case for the provision of government support for the SME sector. Most policy debates revolve around how to promote and/or support SMEs, rather than whether to provide such support as opposed to spending public resources elsewhere. This paper is intended to remind all groups concerned with SMEs that there is a need to constantly revisit and refresh the fundamental arguments for SME policies. Prompted by the challenge laid down by Graham Bannock (see quote above), a leading commentator on SME policy issues and a successful entrepreneur in his own right, the paper will assess critically the arguments for the provision of government support for SMEs, with a primary focus upon the 'market failure' approach which dominates the thinking of many governments.

The aims are to outline a theoretical framework within which SME policy can be understood, analysed and evaluated, and to examine the extent to which policies on selected issues can be justified on the grounds of 'market failure'. The paper will build on previous work by the author and others on the justifications for SME policy and the evaluation of policy interventions to support SMEs.

Methodology/Key Propositions

This will be a synthesis paper, involving a review of the relevant economics and public policy literature, policy approaches of governments and international organisations and evidence on the impact of SME policies in relation to a range of issues such as job generation, business start-ups, support for existing businesses, minority entrepreneurship and employee training in SMEs.

Results and Implications

The paper will suggest that the 'market failure' approach provides a plausible explanation for many of the policy initiatives pursued in many countries in recent years. However, the framework does not provide an adequate justification for all interventions and does not always explain why one policy option is chosen over another.

In order to appreciate more fully the reasons why governments make specific choices about public policy towards SMEs, it is necessary to consider equity as well as economic efficiency arguments; to utilise wider range of explanatory frameworks (for example the public choice model) and to take into account the role of small business lobby groups and the symbolic role played by entrepreneurs and SMEs within the free market system.

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