

# **A Trade Strategy for Europe 2020**

## **Focus on the Role of the Local and Regional Authorities and SMEs**

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# Table of Contents

- Executive Summary ..... 1**
- 1. Introduction ..... 3**
  - 1.1 Context..... 3
  - 1.2 Purpose and scope of the briefing note ..... 3
  - 1.3 Tasks ..... 3
- 2. A review of trade policy and forecast of future developments ..... 6**
  - 2.1 Current EU trade policy..... 6
  - 2.2 Factors informing the Global Europe policy ..... 6
  - 2.3 Global Europe. Competing with the world: The Agenda ..... 8
  - 2.4 Global Europe Two Years on..... 12
  - 2.5 EU trade and development policy ..... 15
  - 2.6 A new trade policy for Europe 2020: ..... 17
- 3. Policy Measures for SME Support ..... 21**
  - 3.1 Drivers of internationalisation..... 21
  - 3.2 Barriers to internationalisation ..... 22
  - 3.3 Policy implications ..... 24
- 4. Recommendations for LRAs on areas of interest within trade policy .. 29**
  - 4.1 An open, competitive EU market..... 29
  - 4.2 Opening markets abroad: the WTO, FTAs and bilateral agreements . 31
  - 4.3 Enforcing existing agreements ..... 31
  - 4.4 Adapting to the environment of international standards ..... 31
  - 4.5 IPR..... 32
  - 4.6 High-level strategic dialogue..... 32
  - 4.7 China..... 32
  - 4.8 MAS..... 33
  - 4.9 Public procurement..... 33
  - 4.10 NTBs..... 33
  - 4.11 Revise GSP ..... 33
  - 4.12 Trade defence instruments..... 34
  - 4.13 FDI – protect and access..... 34
- 5. Bibliography..... 36**

# Glossary

<b>Term</b>	<b>Explanation</b>
ACP	African, Caribbean and Pacific Group of States
Cotonou	Treaty between the EU and the ACP Group
EPA	Economic Partnership Agreement
FDI	Foreign direct investment
FTA	Free trade agreement
GSP	General System of Preferences: a formal system of exemption from the more general rules of the WTO
IPR	Intellectual property rights
LATAM	Latin American
Med	Mediterranean
MTS	Multilateral trading system
NTB	Non tariff barriers
WTO	World Trade Organisation

# Executive Summary

- *This briefing note addresses the question of what the role of local and regional authorities (LRAs) could be, especially vis à vis SMEs, in the trade strategy for Europe 2020.*
- *The note first considers current EU trade policy, as set out in 2006 in “Global Europe, competing with the world”, in support of the renewed Lisbon Strategy of 2005.*
- *It looks at the drivers underlying the Global Europe approach, its agenda, the development angle, and presents a note on a report that considers the EU’s position two years on in 2008 – and no doubt will inform the current review of trade policy (see below).*
- *The drivers of Global Europe are the continued globalisation of trade, the increasing competitive pressure being experienced and the need to respond to that in a way that will enhance EU competitiveness. This requires an internal response: competitive markets, openness and social justice; and an external response: opening markets abroad and a sharper focus on barriers to trade.*
- *The Global Europe agenda is one of trade creation, building on the multilateral trading system but also using free trade agreements and bilateral agreements where considered appropriate, to obtain access to key, fast growing markets.*
- *There is more focus on IPR protection and enforcement and the transatlantic dimension. Due to its importance, China has a special position. The Market Access Strategy is renewed, there is a focus on public procurement and a review of trade defence instruments.*
- *A new trade policy communication for Europe 2020 is to be published in the Autumn of 2010. However, it looks at this stage as if it will build on the Global Europe approach with an additional focus on some less conventional areas such as international standards.*
- *Next, policy measures for SME support are reviewed. Research findings as regards drivers of internationalisation are presented, followed by the barriers to internationalisation, and then policy measures for SME support are set out.*

- *The research suggests that key predictors of SME internationalisation tend to be the personal and professional experience of owners/ managers, firm age and the sector of activity.*
- *A wide range of barriers is identified, but these can be summarised as being constraints on managerial time and skills and a lack of knowledge of foreign markets.*
- *Policy to support SMEs increasingly takes a holistic, evolutionary view of the firm, bearing in mind the firm life cycle. While the lack of awareness of internationalisation opportunities requires a particular focus, preparing the firm for internationalisation is now seen as a competitiveness increasing initiative: it needs planning, systems, skills and increased capabilities to present a sound platform for positive action.*
- *The importance of local development of support, on a targeted individual firm basis is seen, increasingly, as a key factor in success. Access to local networks is also seen as a contributing factor to success.*
- *A wide range of support measures is available for EU SMEs.*
- *On the basis of the thrust of trade policy on the one hand, and the areas identified as useful intervention policies for internationalising SMEs on the other it is possible to identify policy areas where LRAs could play a useful role.*
- *These areas are:*
  - *Support of open markets in the EU*
  - *Building on the opening up of foreign markets*
  - *Supporting enforcement of existing agreements*
  - *Adapting to international standards*
  - *IPR protection*
  - *High-level strategic dialogue*
  - *China*
  - *Market Access Strategy*
  - *Public procurement*
  - *Non-tariff barriers*
  - *Revision of the GSP*
  - *Trade defence instruments*
  - *Foreign direct investment*

# 1. Introduction

## 1.1 Context

With the entry into force of the Treaty of Lisbon, the competences of the Committee of the Regions were extended to include, among other areas, trade policy.

This new competency needs to be looked into in order to determine specific issues on which the Committee of the Region might need to form an opinion, in particular the SME dimension in trade policy and the possible new role and competencies of local and regional authorities in this field.

## 1.2 Purpose and scope of the briefing note

The purpose of this briefing note is to:

- provide an overview of developments in the area of trade policy and identify industries that may have impact on local and regional authorities;
- investigate the policy measures provided to support SMEs;
- identify trade policy areas of particular interest for *policy measures* to be taken by local and regional authorities.

The findings of the report should serve as background to support the rapporteur drafting an opinion as well as forming a basis for possible further investigation of policy measures. It will provide a factual insight into trade policy and suggest possible future scenarios for CoR involvement in this policy.

## 1.3 Tasks

1. To present an EU trade policy review to determine the starting point and areas of interest from the local and regional perspective
2. Identify SME policy measures applicable to trade policy, particularly those that foresee an active role for LRAs
3. Draw conclusions for the support of LRA involvement in trade policy.



## **2. A review of trade policy and forecast of future developments**

This section sets out the main features of current of EU trade policy and where it is heading.

### **2.1 Current EU trade policy**

The basis for current EU trade policy was set out in the 2006 Communication “Global Europe. Competing with the world”<sup>1</sup>, conceived as a tool to support the renewed Lisbon Strategy of 2005.

Trade policy aims to support the EU internal and external agenda. Internally, the aim is to open markets, develop high quality, efficiently enforced, international rules, and secure the social cohesion needed to help EU companies compete globally.

Externally, the aim is to create opportunities in a global economy. The priority is an ambitious, balanced, just, multilateral system, based on liberalising trade and opening markets in which to compete and grow.

In a global world, the EU’s economic strength at home is based on its competitiveness in the world. Trade policy should focus on competitive sectors and keeping markets open (in the EU and abroad), both in large established markets and in fast growing geographical areas.

### **2.2 Factors informing the Global Europe policy**

At the time of the 2006 Communication, it was considered necessary to develop a new trade policy for the EU due to the rapidly changing global economic order, as driven by the increased economic and financial integration resulting from trade and capital flows, the ICT revolution and falling transportation costs that had created opportunities for growth and development but that had also put pressure on natural resources, climate change, traditional industries, and livelihoods and life styles.

The corporate response to these changes was to apply advanced technology and invest capital in the educated labour pools in developing countries, the

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<sup>1</sup> EC, External Trade (2006), Global Europe. Competing with the world. A contribution to the EU’s Growth and Jobs Strategy (COM (2006) 567).

globalisation of supply chains, the outsourcing of high value added activities to low cost areas and obtain multiple sources for products.

Changes in global trade had been driven by tariff reductions, and the key to future trade competitiveness was seen as knowledge, innovation, intellectual property, services, and efficient resource use.

In this context a new trade policy approach to drive competitiveness was required, based on correct internal policies (reflecting external competitive challenges), maintaining openness to trade and investment, ensuring open markets abroad and application of fair rules in other markets, especially with future trading partners. To achieve this, transparent, effective rules were needed. In this way a direct link between trade and competitiveness was established.

Within the EU, this required:

- competitive markets: a single market that creates globally competitive companies due to transparency, a predictable, stable environment, that can reap economies of scale and allow the best allocation of resources, innovation, while opposing anti-competitive State aids, and applying high quality rules and standards.
- openness, to create jobs and growth by exposing the domestic economy to competition, to spur renewal and innovation, to access new technologies, and to increase the incentive for new industries. Protectionism is rejected because it raises prices, limits choice and diverts resources away from the more productive parts of the economy, especially if as a result others retaliate. Some temporary, targeted restrictions on anti-competitive measures could however be supported.
- social justice and cohesion to deal with the potentially disruptive effects of structural change associated with globalisation, especially in some sectors and regions, to help the workforce adapt, and also ensure that benefits of globalisation would be passed to all citizens of the EU. There would also be a promotion of EU values around the world, as regards for example the rule of law, social and environmental standards and cultural diversity.

Abroad, core principles informing the strategy are a progressive opening of markets coupled with a rejection of protectionism at home. Key elements of the approach are: stronger engagement with major emerging economies and regions (especially Brazil, India and China) and a sharper focus on barriers to trade.

- Non-tariff barriers (NTBs): As tariff barriers have fallen, regulations and procedures have become more important, and often less visible, more complex and sensitive. Such measures should be less discriminatory and more transparent. The most frequent NTBs encountered are: burdensome customs procedures; discriminatory tax rules and practices; technical regulations; standards; conformity assessments; sanitary and phytosanitary measures; restrictions on access to raw materials; poor IPR protection; services and FDI; restrictive or non-transparent public procurement; abuse of trade defence mechanisms; and, unfair use of state aids or subsidies. They are often hard to address, complex, require a high level of resources and are not fully covered in the WTO. Instruments to deal with such measures could be: mutual recognition agreements, international standardisation, regulatory dialogues, and technical assistance to third countries. These require new ways of working with the Commission and others.
- Access to resources. EU products and exports have a high import content. Restrictions on EU firms' access to energy, metals and scrap, primary raw material and agricultural markets, hides and skins need to be addressed. Energy is especially important as the EU increases dependency on external sources, and develops an internal energy market. As regards climate change there are major implications for economic growth and trade related to increased energy efficiency, use of renewables and rational use of resources.
- New areas of growth. This includes opening of markets and stronger rules on IPR in new areas of importance (especially for innovative companies), services (a cornerstone of the EU economy), investment (e.g. for globalisation of supply chains), public procurement (an untapped area) and competition (especially State aids).

## **2.3 Global Europe. Competing with the world: The agenda**

Based on the context as outlined in 2.2. above, the key points on the Global Europe, competing with the world agenda were as follows:

Internally, in the context of the renewed Lisbon strategy, this required a coherent agenda to adapt the EU economy to the new global environment, including a fundamental review of the Single Market (in terms of international competition, to support diversification, innovation and specialisation) and trade policy factors in the new global competitive challenge.

EU citizens would expect to share in the benefits of globalisation, and should be helped to adapt. So there were new cohesion policy programmes and an EU Globalisation Adjustment Fund to promote change and modernise.

From an external point of view the Global Europe agenda would include:

- As regards the WTO, there was a need for a strong MTS, and increased multilateralism (see box on the Doha Round below).
- Expansion of and increase in the use of free trade agreements (FTAs), as a stepping-stone towards the WTO. Selection of FTA areas would be driven by economic factors such as: market potential, level of protectionism, and impacts and risks as regards present trade partners.
- Strengthened sustainable development through regulatory convergence, IPR protection, good governance, making rules of origin simpler and more modern, and monitoring progress.
- IPR protection and enforcement should be a more important element in future bilateral agreements. This would involve China, Russia, Turkey, ASEAN, Korea, Mercosur, Chile and the Ukraine.
- Transatlantic trade and competitiveness.
- China presented a major challenge to the EU's capacity to gain from globalisation, and a comprehensive China strategy was to be developed (see box below).
- Renewal of the market access strategy originally launched in 1996 to open third country markets and help enforce multilateral and bilateral trade agreements.
- Public procurement. Almost all EU trade partners had restrictive public procurement practices against EU suppliers. A proposal would be presented to target these practices and obtain a level playing field.
- A review of trade defence instruments in the MTS to ensure that the benefits of openness were not undermined by unfair practices.

The main thrust of policy was to increase EU competitiveness in the global economy and thereby to increase the contribution of trade policy to growth and jobs in the EU. The primary tool for this would be a multilateral trading system.

To implement the Global Europe market access strategy required stronger partnership between Member States. The report on the public consultation on the market access strategy suggested more emphasis on “on the ground” support in

third countries<sup>2</sup>. EU market access strategy should be more assertive, effective and dynamic to tackle trade and investment barriers. It was suggested that a trade barriers network between Member States be set up and that the market access advisory committee be reinforced. Other aspects were: a one-stop shop to improve information flows ; publication of annual trade barrier reports; more active participation by EU businesses; and, more attention paid to the needs of SMEs. Prioritisation should reflect impacts – especially important were the main EU trading partners and the BRICs. Also particularly important were the non-tariff barriers (regulatory and IPR). Bilateral agreements were suggested, not to compete with the WTO, but because issues were very complex and the WTO could not really deal with these yet. The Trade Barriers Regulation should be simplified so that SMEs could use it more easily. The Market Access Database could also be improved by adding more information on tariff barriers, services, IPR, investment and emerging markets. Its updating could be improved, especially as regarded trade barrier complaints. Also, special attention should be given to SME needs.

In May 2010, it was reported, that almost 280 restrictive trade barriers had been put in place by major EU trading partners over the previous 18 months, while hardly any had been removed, despite G20 commitments.

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<sup>2</sup> EC, Directorate General for Trade (2007), Report on the Public consultation on the EU Market Access Strategy, Brussels, 28 February, 2007.

## The EU and China

*China is considered the single most important challenge for EU trade policy. It is the world's third largest economy, the biggest exporter and increasingly important politically.*

The EU supported China's accession to the WTO in 2001 and obtained improved access to China's market, reduced tariff and non-tariff barriers. The view is that China is making progress in its commitments but issues remain, for example in commitments to WTO obligations, IPR protection, discriminatory industrial policies, and access to raw materials.

EU trade policy vis a vis China was set out in the Communication "Partnership and Competition Agreement" (PCA) in 2006. The approach accepts that there is tough competition with China and pushes a fair trade policy. On-going negotiations on the PCA started in 2007, to upgrade the bilateral trade and investment relations and upgrade the 1985 EU China Trade and Economic Co-operation Agreement.

<b>EU China Trade and Investment (€bn, 2009)</b>			
EU exports to China (goods)	81.7	EU imports from China (goods)	214.7
EU exports to China (services)	18.0	EU Imports from China (services)	13.0
EU FDI in China	5.3	Chinese FDI in Europe	0.3

High-level discussions deal with matters such as: trade, investment and competition, SMEs, customs co-operation, sustainable development, energy, food (safety and trade), consumer protection, healthcare, innovation and IPR, geographical indications, technical and information society, and transport.

<http://ec.europa.eu/trade/creating-opportunities/bilateral-relations/countries/china/global-europe/>

## 2.4 Global Europe two years on

Two years after launching the "Global Europe" policy, the performance of the EU in global markets (excluding intra-EU trade) over the preceding ten years was assessed, with a view to evaluating EU competitiveness. The findings are reproduced here because they also provide a context for the development of the post-EU 2020 Trade Policy set out below.

## **Global Europe two years on\***

- 1 The EU has maintained its share in world markets at some 19.5% since the mid nineties despite major changes in the shares of others in the market.
- 2 The EU trade balance in manufactured goods is in surplus, helping offset a rising energy import bill.
- 3 Developing country exports have continued to grow, especially from China, that has overtaken the US as the world's major exporter.
- 4 The strong EU performance is the result of upgrading the quality of its products and its ability to sell at a premium price due to quality, branding and related services.
- 5 The EU has become the principal exporter of high tech products, although this presents underperformance in terms of overall market size.
- 6 The EU has lost significant market share in some fast growing markets, especially in Asia.
- 7 Some two-thirds of extra-EU imports are incorporated as inputs into production.
- 8 The EU is the leading services exporter in the world and its share is growing.
- 9 The EU is the world's biggest foreign investor and the principal host of inward foreign direct investment.
- 10 The EU has a higher ratio of inward and outward investment to GDP than the US and most developed countries.

*The review found that there were significant variations between Member State sources of imports and destinations of exports and FDI, as well as the sector composition of exports and imports.*

*Local and regional organisations have a key role to play in understanding the strengths and weaknesses of particular places and identifying opportunities and intervention areas for trade policies.*

The implications of the performance review were that:

- The EU should continue to focus on high quality products and services to sell at premium prices. It cannot compete in low range market segments. For this the EU needs to continue upgrading skills and competitive performance.
- Innovation is a key component in success, but the EU is losing ground in high-tech products – this requires action on R&D and innovation, and IPR protection.
- There is poor performance in some dynamic markets, justifying the negotiation of trade agreements

EC, Directorate General for Trade (2008), Global Europe. EU performance in the global economy, Brussels.

\* 2008 – full reference

## 2.5 EU trade and development policy

The EU is the principal trading partner for many of the poorest countries of the world. Some 40% of EU imports are from developing countries. The EU has a wide range of policies in support of external development. These include the Europe Agreements of the 1990s, the Barcelona Process of 1995, the EuroMed Bilateral Association agreements, European Neighbourhood policy and agreements with the ACP, Cotonou, Latin American, Middle Eastern and Asian states.

The main instruments are preferential trade agreements, technical assistance and grant funding. There is an export help desk for developing countries to help them export to Europe, to provide information on GSP tariffs, document requirements, rules of origin, etc. The Centre for Development Enterprise supports implementation of private sector strategies in ACP countries through non-financial services. Pro Invest promotes investment and trade flows in ACP countries. The European Development Fund is the main instrument for aid and development cooperation in ACP and overseas countries and territories.

The objectives of these instruments are to enable developing countries to use trade more effectively to promote growth, development and poverty reduction; to facilitate access to international markets for beneficiaries; help countries implement and adjust to trade reform; assist in regional integration; and, assist in the implementation of trade agreements. To reach the Millennium Development Goals developing countries do not just need access to markets but also help in removing supply side constraints and infrastructure bottlenecks. This can be supported by means of trade-related assistance.

EU trade preferences for developing countries include:

- GSP: the generalised system of preferences whereby industrialised countries can apply for a waiver for this non-reciprocal preferential tariff with developing countries
- Everything but Arms: a GSP scheme that eliminates duties and quotas for 50 of the least developed countries, including bananas, sugar and rice.
- GSP Plus: to support sustainable development and good government in developing countries.
- The Cotonou Convention, which, as the successor to Lomé, provides a framework for cooperation for 78 developing countries and the EU.

- EU South Africa – a bilateral Trade and Development Cooperation Agreement.
- Association Agreements: bilateral agreements with LATAM and Med partners that could lead to FTAs.

EU ACP Economic Partnership Agreements have also been concluded with ACP countries, providing a broad agreement to build regional markets and diversify ACP economies before the gradual opening of trade and exports to the EU, representing a move away from tariff protection that is seen as a disincentive to reform. This includes financial and technical assistance to improve basic physical infrastructure etc.

### **The Doha Round**

The Doha Round was launched at Qatar in November 2001. This was intended to take the WTO into a new era with a broader agenda than trade rounds of the past and aimed at addressing the needs of developing economies. There would be a focus on reforming agricultural subsidies, improving access to global markets, ensuring new liberalisation in the global economy and support for sustainable development needs. Main EU priorities were:

- To raise trade flows by cutting tariffs in the industrial goods sector.
- Reform of farm subsidy programmes – in terms of the 2003 CAP Reform.
- Market access for trade in services.
- Agree a package of measures to support development.
- Agree a new set of rules to govern use of trade defence instruments so that they are not abused and protect geographical indication.

The discussions broke down due to disagreements on how to deal with matters in the agricultural sector.

<http://ec.europa.eu/trade/creating-opportunities/eu-and-wto/doha/>

## 2.6 A new trade policy for Europe 2020:

Europe 2020<sup>3</sup> is a key statement of the EU's strategy for responding to the on-going economic and financial crisis. It sets out five clear targets for the EU and proposes seven flagship initiatives to address them. Trade policy, as set out in "A Trade Strategy for EU 2020"<sup>4</sup>, is seen as a significant tool to support the achievement of these targets and help the transformation of the EU into a smart, sustainable and inclusive economy.

The aim of future trade strategy would be to ensure EU external competitiveness in the face of rapid change in the post crisis global economy. The new EU trade strategy would anchor EU trade strategy for the next five years. During the crisis EU trade flows contracted significantly. Trade is seen as contributing significantly to a strong recovery and growth, and the other objectives of EU 2020.

Objectives of trade policy would include:

- Multilateral and bilateral trade negotiations and better enforcement of existing agreements.
- Trade opening initiatives: for example for sectors of the future – e.g. green products and technologies, high tech products and services and international standardisation in growth areas.
- Proposals for high-level strategic dialogue with key partners.
- A regulatory framework within the EU that takes account of what other major economies do to minimise the cost of trading between different regulatory regimes – develop international standards accordingly.
- In view of the emphasis of Europe 2020 on smart and sustainable growth, high tech initiatives and green technologies – develop trade policies to contribute by facilitating trade in these sectors so as to create larger markets, reduce costs, and stimulate more innovation.
- Action in the field of promoting EU values such as the rule of law and sustainability.

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<sup>3</sup> European Commission, Communication from the Commission, Europe 2020 A strategy for smart, sustainable and inclusive growth, (COM(2010) 2020, 3.3.2010).

<sup>4</sup> EC (2010), A Trade Strategy for 2020 (Roadmap).

- Also there should be greater focus on ensuring that partners have implemented what has been negotiated and working harder on IPR enforcement, obtaining more leverage in government procurement (reciprocally), and disciplining the use of State aids in third countries.

In parallel with this there is the development of an industrial policy and internal market policy, all of which should be logically consistent.

Some initiatives cut across several policy areas, appropriate links with other departments would be developed.

On 22 June 2010 the EU Commissioner for Trade announced that an EU Trade Policy Communication was being planned to dovetail with EU 2020<sup>5</sup>. The following elements would be included:

- concluding the Doha Round;
- concluding ongoing bilateral negotiations, with differentiation in the agreements concluded, based on the level of development of partner countries;
- including broader issues, beyond the traditional tariff agenda, in future negotiations;
- re-energising the Transatlantic Economic Council;
- re-energising the High Level Economic and Trade Dialogue with China;
- promoting greener production and trade by putting in place the right regulatory environment and international standards;
- continuing negotiations with the ACP to tailor agreements to ACP needs, avoiding a one-size fits all approach;
- revising the GSP scheme to target preferences more towards those countries that need them most;
- examining how the EU's new powers in foreign direct investment can be used to expand opportunities for EU companies and better protect EU investments in third countries.

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<sup>5</sup> De Gucht, K., (2010b), 'Speaking Points: Future Trade Policy', European Parliament, Committee on International Trade, Brussels, 22.10.2010.

The aim is that the Community would adopt these towards the end of October 2010



### 3. Policy measures for SME support

Europe's economy is particularly dependent on the performance of its small and medium-sized enterprises and they are expected to play an important part in increasing Europe's global trade. However, by far the majority of EU SMEs currently depend largely on domestic markets. When asked for a recent report, about 25% in total responded that they export, or have exported, in the preceding three years, mainly within the EU and only about 13% are active in markets outside the EU; some 29% import, 7% are involved in technological co-operation with foreign firms, and a similar percentage is involved in international sub-contracting, while 2% have made foreign direct investments<sup>6</sup>.

A great deal of research has taken place in the area of the internationalisation of SMEs over the past decades with a view to understanding the process better and developing measures that can support greater internationalisation of SMEs. This section will summarise the major findings of research – as appropriate to this project. In the next section, areas of overlap with trade policy and SME policy where LRA can profitably intervene will be presented.

#### 3.1 Drivers of internationalisation

As some 99% of all firms, there are of course very many SMEs, and there will be differences among them that are very important to bear in mind as far as internationalisation as part of trade policy is concerned. Categorisation of SMEs can be in terms of: new or established exporters, “born global” firms, early and late starters, “the international among others” and “the lonely international”<sup>7</sup>.

An Expert Group on SME internationalisation, convened by DG ENTR reported (2007)<sup>8</sup> that internationalisation in SMEs is closely related to:

- The personal and professional experience of the owner/ manager, the industry to which the firm belongs, the evolution of the firm and attitudes of those in it – particularly in the “born global” firm.

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<sup>6</sup> EC, Enterprise and Industry Directorate-General, (2010a), Internationalisation of European SMEs, Final Report, EC, Brussels., p5.

<sup>7</sup> Johanson and Matson article Johanson, J. and L.-G. Mattsson, 1988, "Internationalization in Industrial Systems - A Network Approach", in Hood and Vahlne, eds., *Strategies in Global Competition*, New York: Croom Helm. Johanson, J. and Vahlne, J.-E., 1977., "The Internationalization Process of the Firm - A Model of Knowledge Development and Increasing Foreign Market Commitments", *Journal of International Business*, 8, Spring/Summer, pp. 23-32, Department of Business, Innovation and Skills (DBIS), (2010), Internationalisation of Innovative and High Growth SMEs, BIS Economics Paper no 5, DBIS, UK.

<sup>8</sup> EC Enterprise and Industry Directorate-General, (2007), Final Report of the Expert Group on Supporting the Internationalisation of SMEs, EC, Brussels, p.

- International orientation in terms of the commitment of the founders – this was an integral factor in the firm’s behaviour and its propensity to proactively target foreign markets (a “key predictor”).
- Firm age and the age of the CEO - these are the main predictors for becoming an internationally involved company.

An OECD report<sup>9</sup> found that SMEs had a need to grow and obtain knowledge, and often appreciated the potential of international pathways and associated opportunities to this end. Other drivers for internationalisation identified included: networks, supply chain linkages, social ties, immigrant links, improved global trade infrastructure, sector and region of origin factors. Importantly, the 2010 report on the internationalisation of SMEs found that most first internationalised through importing<sup>10</sup>.

### **3.2 Barriers to internationalisation**

There appears to be a good degree of agreement as regards the barriers to the internationalisation of SMEs. The OECD (2008) points out that barriers are dynamic and contingent<sup>11</sup>. They relate to the size of the firm, learning experience and knowledge, the business environment and lack of capabilities.

The OECD (2009) Report on Barriers to Internationalisation<sup>12</sup> identifies key barriers as:

- shortage of working capital to finance exports;
- identification of foreign business opportunities;
- limited information available to locate and analyse markets;
- Inability to contact potential overseas customers;
- problems securing reliable overseas presentation;
- lack of managerial time to deal with internationalisation;
- inadequate personnel for internationalisation.

In essence, this boils down to managerial time and skill constraints and lack of financial resources, which result in a lack of knowledge of foreign markets.

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<sup>9</sup> OECD (2009b), “Top Barriers and Drivers to SME Internationalisation”, Report by the OECD Working Party on SMEs and Entrepreneurship, OECD, p. x.

<sup>10</sup> EC, Enterprise and Industry Directorate-General, (2010a), Internationalisation of European SMEs, Final Report, EC, Brussels.

<sup>11</sup> OECD, (2008c), Removing Barriers to SME Access to International Markets, OECD, Paris, p.8.

<sup>12</sup> OECD (2009b), p.10.

Research for the EU 2010 report found that while one needs to distinguish between those already exporting and those not yet doing so, perceived barriers to internationalisation are the same<sup>13</sup>. These are:

- internal – the price of their products and high costs of internationalisation (e.g. obtaining information, going on missions, participating in trade fairs);
- external – the lack of capital and of adequate information, inadequate public support, and costs of and difficulties associated with export documentation – which means there is more intra-EU than extra EU trade;

Barriers are greater for smaller SMEs, in particular as regards obtaining appropriate staff (staff are often specialised so there is probably a cost/ scale of operation issue). Larger SMEs have more difficulties with laws and regulations, smaller ones in obtaining capital. Otherwise problems experienced by small and larger SMEs are similar.

Research by the Department for Business, Innovation and Skills in the UK on the internationalisation of innovative and high growth SMEs found that “born global” companies use various modes to internationalise: including networks and serendipity, but are more likely to use independent analysis with market selection<sup>14</sup>.

Barriers are experienced in:

- access to networks and contacts;
- unfamiliar business environments – including different languages and cultures;
- procedural barriers – product standards and legal/ regulatory matters;
- understanding the competitive environment – identifying opportunities and risks;
- confidence and management times and resources to investigate and pursue opportunities overseas.

Culture was seen the biggest impediment to entry. Barriers change over time until the firm becomes an “insider”. There are more barriers in fast growing markets.

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<sup>13</sup> EC, Enterprise and Industry Directorate-General, (2010a), Internationalisation of European SMEs, Final Report, EC, Brussels, p.7.

<sup>14</sup> Department of Business, Innovation and Skills (DBIS), (2010), Internationalisation of Innovative and High Growth SMEs, BIS Economics Paper no 5, DBIS, UK , p.70.

The current global crisis has also had an additional impact on the financing of SMEs and entrepreneurship by tightening the “usual” SME financing gap, as in the downturn a worsening situation is expected and as a result there is more pressure on early payment, less financing available and the cost of capital is increasing<sup>15</sup>. Bank attitudes are further influenced by the poor prospects of SMEs and the need to rebuild their balance sheets.

### **3.3 Policy implications**

According to the Expert Group Report (2007)<sup>16</sup> there are good reasons for policy to remain focused on national markets: lack of skills and lack of finance, both contributing to lack of knowledge of foreign markets. To be effective, policy should be conducted on two fronts:

- For existing SMEs: to raise awareness of the need to internationalise, to prepare policies to overcome barriers, and in the long term to acquire new capabilities, rather than depend on short-term grants or subsidies.
- For future SMEs: to create an environment conducive to more and better equipped international entrepreneurs through language education and the provision of entrepreneurship in academic channels.

Smaller firms tend to be harder to support, and make more haphazard use of support services.

Principles to guide support policies are:

- A structured management system in the firm is fundamental.
- Policies must include financial measures.
- Policies must address the lack of knowledge of internationalisation in SMEs.

There are many elements to a successful policy to support internationalisation.

These include the following matters<sup>17</sup>:

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<sup>15</sup> OECD, (2009a), The Impact of the Global Crisis on SME and Entrepreneurship Financing and Policy Responses, OECD, Paris p.

<sup>16</sup> EC Enterprise and Industry Directorate-General, (2007), Final Report of the Expert Group on Supporting the Internationalisation of SMEs, EC, Brussels p.4.

<sup>17</sup> EC Enterprise and Industry Directorate-General, (2007), Final Report of the Expert Group on Supporting the Internationalisation of SMEs, EC, Brussels; EC, Enterprise and Industry Directorate-General, (2010a), Internationalisation of European SMEs, Final Report, EC, Brussels.

There is a low usage of support due to a lack of awareness of support measures. Awareness and use of public support programmes needs to be promoted more vigorously. Financial support programmes are used mainly by larger, non-financial by smaller SMEs. Simplified points of access to support are needed (e.g. through the European Enterprise network).

Plans developed at national level should be elaborated in terms of local realities through direct participation of stakeholders in development of policies and programmes. Coordination at different levels is necessary for best resource use – there should be a fluid, integrated, consultative process between various stakeholders. To be effective support must be targeted towards the variables that matter most: financial and human resources, company size and stage of development, sector, geographical location, targeted marketing. There is an increasing tendency to take a sub-national approach to promote regional and sector-specific SME internationalisation.

Not all sectors are equally internationalised or globalised or in the same way. There is therefore a need for tailor-made programmes.

The first phase of intervention strategies should be to develop an international orientation and provide entrepreneurial training for the key decision makers: more exposure to international markets is needed. There is also a need for continuous education, especially language acquisition, greater awareness of and exposure to foreign cultures and fostering of entrepreneurial attitudes. These capabilities should be developed before the first steps in internationalising are taken. This includes a more formalised approach to and systematic selection of foreign markets – in short the development of an internationalisation strategy.

As regards financial support, available mechanisms must be identified that can support the company over time. Finance for working capital, trade finance, is good, but it needs to include funding for later stages (including FDI). There is also a lack of finance for growth companies (a need to build a pan-EU venture capital market, possibly with specialist “internationalisation” funds, or widening the application of Jeremie support on discussion with the EIB).

Internationalisation should be seen as a contributor to competitiveness, merging internationalisation with innovation as a move up the value added ladder. Supporting innovation spurs internationalisation, so support programmes should be combined. Promotion of management skills in innovation intensive start-ups, also includes support with and accessing of international networks, finance and government support. For a high-tech firm there is often a short window of opportunity, so early internationalisation is fundamental. So there are common drivers for internationalisation and innovation support, that can be blended into

“competitiveness” support, as has happened in countries such as Finland and Norway that developed a “growth company” service, promoting greater use of IT e-commerce and CRM systems as important systems for companies, as well as product standardisation and certification so that there is more ready access to global value chains.

There is a need to concentrate on increasing the number of internationalised companies, rather than on those with the largest potential. Focus on micro and small enterprises that present a vast pool of potential. There should be easier access to support measures for micro-firms (they benefit most but are least aware).

To support a maximum number of SMEs, focus should be on the main barriers to remove. Internationalisation involves much more than exports, but most support still focuses on that, usually in the form of providing information, analysis and access to fairs and trade shows. There is little focus on removing international trade barriers and improving the domestic business environment (e.g. though tax and R&D support). Trade barriers can be influenced by: international negotiations, legal proceedings and trade advocacy. The timing and costs required vary in each situation.

Individualised support is the most effective— creating capabilities within the SME. The challenges of internationalisation differ as the firm evolves and grows; the problems vary and the support required changes. Focus should be on individualised support, based on analysis of individual SMEs, identifying specific areas of support provision in terms of specific resources and capabilities. Firms should be screened for readiness and provided with consultancy support to build long-term capabilities. This implies a holistic approach to the company, including general programmes as well as those targeting internationalisation (including imports, FDI, etc.).

Networks expand the capacity of companies to internationalise, for example by using government offices and business associations. It is important to promote direct cooperation between companies.

The EU internal market is a good launch area for the international operations of most EU SMEs. There should be more cooperation between Member States in collecting market information, and coordination to reduce duplication.

There should also be a focus on supporting imports as well as exports, and on fostering e-commerce.

Focus should be on long term cooperation between partners, rather than short-term customer focused trade development. Organised private sector-led support is increasingly seen as important (e.g. Chambers of Commerce)<sup>18</sup>.

Programmes should be evaluated– user surveys seem most useful.

DG Enterprise has developed a useful publication “Best Practice projects”<sup>19</sup> setting out some examples of internationalisation support programmes under the headings of: raising awareness of the benefits and support programmes; providing high value information; human resource development programmes; supporting the financial needs of internationalisation; promotion of networks; supporting internationalisation of services; using internationalisation to enhance competitiveness; individualised support – need or event specific; border zones and cross-border cooperation.

A wide range of support measures is available for European SMEs<sup>20</sup>. There are four major types within which specific programmes exist:

- Themes: Competitiveness and Innovation Programme (Enterprise and Innovation, ICT Policy Support), the 7<sup>th</sup> Framework Programme, Eureka, Erasmus, Leonardo da Vinci, and Culture.
- Structural funds: ERDF<sup>21</sup>, ESF, Rural Development, Jeremie, Jasmine.
- Financial Instruments: CIP framework, EIF and EIB.
- Support for internationalisation (often provided through intermediaries): AL-Invest (Latin America), PRO-INVEST (ACP), EU Gateway (Japan and Korea), EU Japan Industrial Cooperation Programmes.
- Executive Training Programme (Japan, Korea).

Information about these is available through the Enterprise Europe Network.

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<sup>18</sup> OECD (2009b), “Top Barriers and Drivers to SME Internationalisation”, Report by the OECD Working Party on SMEs and Entrepreneurship, OECD, p

<sup>19</sup> EC, Enterprise and Industry Directorate-General, (2008b), Supporting the Internationalisation of SMEs, Good Practice Selection, EC, Brussels

<sup>20</sup> EC, Enterprise and Industry Directorate-General, (2008a), European Union Support Programmes for SMEs, EC, Brussels

<sup>21</sup> For example, a £6 million pound project has been recently launched in the West Midlands to provide SME's with funding and advice on how to develop their companies internationally and sell to new overseas markets. West Midlands (SME) Internationalisation is an ERDF funded project which can provide grants to eligible SME's, to support a range of internationalisation activities including developing an international trade strategy, skills development and attending overseas trade fairs and exhibitions.

The box below sets out how SMEs can become involved in global value chains.

### **Enhancing the role of SMEs in global value chains\***

A study to identify how SMEs could increase participation in global value chains identified the following challenges and policy conclusions:

- Awareness and understanding of structure and dynamics of global value chains is insufficient, and varies between sectors.
- The majority of SMEs cannot identify their competitive strengths within value chains, nor understand why it is important.
- SMEs are affected mainly by inadequate availability of managerial and financial resources, and inability to upgrade and protect in-house technology and innovate.
- Compliance with strict quality standards to participate in global value chains is difficult and costly.
- SMEs want frameworks that assist in managing intellectual assets and IPR protection;
- To move up the global value chain generally requires carrying out larger and or more complex tasks. SMEs often lack the managerial capability to do so.

Policy conclusions – participation in global value chains could be stimulated by:

- raising awareness of the potential of participating;
- supplier financing;
- promoting technological upgrading;
- protecting IPR;
- facilitating compliance procedures;
- promoting skills development;
- attracting FDI;
- promoting the development of clusters;
- promoting the development of domestic industries and service networks in developing countries.

\* Source: OECD (2008), pp.10-11

## **4. Recommendations for LRAs on areas of interest within trade policy**

In general, public sector support of internationalisation of SMEs is considered to contribute substantial additionality. Also, there is considered to be a great deal of scope for additional internationalisation from the vast pool of micro-, small and medium-sized enterprises that exists in the EU. Given the opportunity in question, there is a strong argument for the role of additional intervention in favour of trade policy-linked support for the internationalisation of SMEs.

The review of Trade Policy and SME internationalisation set out in sections 2 and 3 suggests that there are several areas of policy interest for LRAs in current and future trade policy, especially as regards the internationalisation of SMEs.

In principle, the driving force of trade policy, to increase the competitiveness of EU industry by keeping markets with the EU open, and opening markets to EU industry abroad, is one that LRAs would certainly underwrite, especially if backed by measures to support EU adaptation to global change through measures such as the cohesion funds and the Globalisation Adjustment Fund.

The presentation in section 3 also suggests that there is not likely to be a great deal of change in the items on the agenda for the Europe 2020 Trade Policy as compared with the Global Europe approach, although there might be a shift in emphasis towards more targeted market access initiatives and combating more obtuse trade barriers.

In this section, areas of interest for LRAs as regards support for the internationalisation of SMEs will be presented in terms of the key preoccupations of trade policy.

### **4.1 An open, competitive EU market**

As has been shown above, SMEs often start internationalising through imports. The need to access raw materials and intermediate goods and services is key for the EU's SMEs and a spur to further internationalisation. This could mean, from the point of view of LRAs, providing support to incoming trade missions from within the EU as well as from outside, and ensuring that the EU does not apply discriminatory barriers to incoming trade that could lead to retaliation elsewhere.

## **4.2 Opening markets abroad: the WTO, FTAs and bilateral agreements**

A major thrust of trade policy is to open new, fast growing markets, for EU firms, especially where it has been seen that the EU has not been performing well compared with its competitors. LRAs can contribute to this by increasing awareness of opportunities in those markets among local and regional SMEs, and at the same time increasing awareness of the support available to access and develop those markets. This can include skills development programmes as well as making information available on access to finance, identification of gaps in the provision of finance, and information on and access to other networks, including the European Enterprise Network.

There is an identified need for regional and local elaboration and delivery of SME internationalisation programmes involving local and regional stakeholders. This would also include identification of gaps in support.

There is also a sectoral dimension to this in that EU trade policy focuses more on high tech and green markets. These are areas that LRAs could help target and develop through their regional and local networks.

As regards intra-EU markets, the roll out and awareness of programmes such as Erasmus for Young Entrepreneurs can be supported to increase the predisposition among EU SMEs to internationalise and at the same to develop skills required to internationalise successfully.

## **4.3 Enforcing existing agreements**

EU trade policy is setting out to ensure that where agreements have been entered into in return for certain commitments, those commitments are adhered to. LRAs can involve themselves in their SME communities in this respect by acting as sounding boards for SME grievances on this score and reporting back to the appropriate bodies, and also making SMEs more aware of this form of support for their internationalisation initiatives.

## **4.4 Adapting to the environment of international standards**

Preparing products and services for certification and standardisation in international markets has often been a daunting and costly process for SMEs. If EU standards were closer to, or the same as, or accepted by international bodies, it would make it easier for SMEs to export. This is a complex area, and probably

requires sector-based intervention, working through national standards bodies, but LRAs can become involved in this area by keeping local and regional firms in the sectors where changes are being considered aware of developments and ensuring that their voice is heard at national level.

## **4.5 IPR**

Protection of IPR and enforcement of agreements on the protection of IPR is a key and increasingly important matter in trade policy, especially in view of the fact that the high tech sector is one where the EU has a very strong export performance. It is a major issue for SMEs entering export markets. In particular there has been a lot of emphasis on abuse of IPR and failure to enforce IPR protection, which discourages SMEs from putting in the effort to make their goods and services known in third markets. LRAs could contribute here by making local and regional SMEs more aware of the various support measures available through the EU, such as for example the IPR China Helpdesk.

## **4.6 High-level strategic dialogue**

In view of initiatives on FTAs, on bilateral agreements, and the Transatlantic dialogue, it will be important to keep up to date on developments as regards those *demarches*. While it would be inappropriate for every LRA in the EU to be individually involved, there is a case for higher-level monitoring and reporting back to individual LRAs of developments and opportunities that have emerged or are emerging from the high-level strategic dialogues being conducted. As in the case of China (see box above), these affect a very wide range of issues, and could have a major impact on SMEs.

## **4.7 China**

China remains the single most important challenge for EU trade policy. The impact of China on the EU underlies the need to stay engaged with and follow the high-level strategic dialogue on China. In the meantime, some LRAs, such as the East Midlands Regional Development Agency in the UK, have developed highly proactive approaches for engaging with China, as for example through the East Midlands China Business Bureau, and recently also an economic partnership agreement has been signed between Derbyshire and Nottinghamshire Chamber of Commerce (DNCC) and representatives from the Yangquan region of China.

There could be value in developing a network among LRAs to share knowledge and best practice on how to deal with China, and other possible strategic partners or issues.

## **4.8 MAS**

Market access strategy is at the core of EU trade policy, and is covered by many areas dealt with above and below. However, SMEs are not always aware of the existence of the Market Access Database (MAD), nor do they use it, so this could be publicised by LRA action. It may also be possible for LRAs to obtain feedback on the use and usefulness of the MAD for SMEs in the region, and possibly drive or support its development in that respect.

## **4.9 Public procurement**

This is an area that came to fore in Global Europe, and is set to continue in the future. It does provide some significant opportunities for SMEs, but also potentially some major challenges. Public sector procurement contracts can have quite onerous conditions, presenting high risks, and make major demands on the SME. Research has also indicated that SMEs tend not to be familiar with notions of global value chains and their position in it. In this area there is, therefore, as in preceding points, substantial scope for individualised training and mentoring of SMEs.

## **4.10 NTBs**

Dealing with non-tariff barriers is gaining increased attention in EU trade policy as they are increasingly important, especially with higher tech companies, and will continue to be so in the future. LRAs could play a role here by ensuring that local and regional exporters and would-be exporters are aware of the mechanisms available to deal with and report on such barriers, maybe acting as a collection point for feedback and identifying which are most important in their region (e.g. in terms of sectors or destinations of exports or sources of imports) so as to drive advocacy for addressing those barriers.

## **4.11 Revise GSP**

Revision of the GSP will probably have most relevance as regards developing countries, but should also provide some opportunities for SMEs in some areas, as will Trade Related Assistance. LRAs should therefore monitor developments and make firms aware of emerging opportunities.

It may be that firms from particular cultural *milieux* are better placed than others for accessing such opportunities, but that should not act as a barrier to new firms wishing to explore and enter those markets.

## **4.12 Trade defence instruments**

LRAs could play a role in tracking abuse of trade defence instruments by foreign governments that impact their regions and providing feedback to EU trade policy managers.

## **4.13 FDI – protect and access**

Foreign direct investment is an increasingly important adjunct of internationalisation, especially in the field of services. Internationalisation in the services sector, and in high-tech sectors is almost synonymous with undertaking foreign direct investment in those markets. Therefore, to ensure exports it is necessary to ensure that FDI in those markets can take place, especially if the EU market is open to such countries in those service sectors. While this could effectively be treated as a form of NTB, FDI is sufficiently important to be treated as a separate matter.



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