



The Dynamics of Small Business - An AIB Perspective

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A significant percentage of Ireland's population earns its living working in small business. During the last decade in particular, economic planners, national governments and financial institutions have identified the importance of the small business sector in the Irish economy.

During the late 1980's and early 1990's, financial institutions designed and delivered various support packages to small business. This case study looks at the response by AIB Bank to the need for increased support to small business from the banking sector.

Ireland, in common with the rest of Europe, experienced profound unemployment problems during the 1970s. An economic recession, the rapid development of lower cost production facilities in countries on the Pacific Rim, and the privatisation and consequent downsizing of many large state enterprises, contributed to the crisis. In Ireland this situation was keenly felt because of the relative weakness of the indigenous industrial base.

In both Ireland and Europe, Government attention began to focus on small business. These were enterprises that seemed to offer real prospects of job creation in economies that were reeling from the social unrest brought about by increasing unemployment.

By the early 1990s, the small business debate had taken on an increasingly urgent tone and became a top priority on Ireland's political, social and economic agenda.

Around this time, people with small businesses had started to join and support 'lobby groups' - groups with particular interests which they wanted to promote. They include the Small Firms Association (SFA), the Irish Small and Medium Enterprise Association (ISME), Chambers of Commerce, trade associations and other interest groups. The growing linkages between business, represented by their lobby groups and the banks, attracted the interest of politicians who could see that the promotion of small business was crucial to the economy.

In 1993 the Irish Government established a *Task Force on Small Business* to find out what needed to be done to help small businesses to start up and develop. The Task Force reported in 1994 and, for the first time, a set of facts emerged that

suggested appropriate supports and development actions. Among the principal findings of the *Task Force* were the following:

- 98% of Ireland's estimated 160,000 non-farm businesses have an annual turnover of less than £3 million, and employ fewer than 50 people.
- 90% of small businesses employ fewer than 10 people.
- Small business accounts for around half of all employment in the private sector.
- Since 1970, domestic and international trends have illustrated that small business became a net creator of jobs, while large business became a net shedder of jobs.
- The level of enterprise in Ireland is comparable to other countries - Irish business start-up numbers compare favourably with the European average.
- Irish business failure is above the European average - e.g. 56% of grant aided businesses set up in 1983 had failed by 1994.
- Low profits meant that it was difficult for Irish companies to obtain ongoing finance.
- There are serious skill shortages in management and marketing in small businesses in Ireland.

These findings showed how important small businesses are to the Irish economy. However, they also highlighted certain problems that anyone starting up a new business has to overcome.

The Task Force findings uncovered two major areas of concern for small businesses:

- limited financial resources, which was a fact of life for many small businesses
- weak business management and marketing skills.

How did AIB respond to the findings of the Task Force?

Even before the Task Force Report was published, the Bank had begun to appreciate the importance of supporting and developing small businesses. AIB had commissioned its own market research and in light of these findings, had created the AIB Enterprise Development Bureau, which was dedicated to looking after the financial needs of small businesses during their start-up and infancy stages.

AIB Bank had several broad objectives, such as increasing the confidence and goodwill of the customers, the government, the media, regional and local business and lobby groups. These objectives could be achieved through a specific action plan, which was drawn up on the basis of AIB's own market research and the Task Force recommendations.

AIB Bank's response was unique to them but it was driven by a recognition of market needs. The Bank formulated a mission to establish AIB Bank as a *pro-enterprise bank*. It developed an action plan that was created to provide support by:

- providing low cost funding
- providing start-up equity
- bridging the skills-management gap
- increasing its 'approachability'
- providing transparency on rates and charges removing the need to use the family home as security for business loans.

low cost funding

The provision of low cost funding was addressed in a number of ways. In 1993, AIB Bank launched its £10 million *Enterprise Fund* to provide loan finance for start-up companies, especially sole traders and very small businesses dealing

in regional or domestic markets. The *Enterprise Fund* was made available to entrepreneurs without the need for personal guarantees or the need for the family home to be used as security. The fund was subsequently increased to £40 million. To date, £33 million has been advanced to over 240 projects nationwide. This fund has helped create or sustain over 3,800 jobs. Although some businesses have ceased to trade, the majority of companies who have used the fund have survived and demand for the fund has increased to the extent that its size will be increased to £60 million in the near future.

AIB Bank also developed the *Business Credit Line* to provide a low-cost source of working capital funds, especially suited to businesses who have a seasonal or short term need for capital. The finance is made available at a discount of 2% on the standard business overdraft rates. AIB also secured IR£90 million in long term loans from the European Investment Bank which was made available to the business community in Ireland through loans with fixed or variable interest rate options for terms of up to 15 years.

The Bank participated in the EU/Government-sponsored scheme *Access to Finance*. Under this £208m project, small businesses were offered an interest rate of 6.5% fixed for 7 years. AIB contributed £79 million to this fund, and along with other participating banks and the Government, absorbed the cost of the interest-rate subsidy.

start-up equity

To address the need for a long-term funding source, the Bank created a special-purpose £12 million *Equity Fund* to provide early stage venture capital to progressive Irish companies. The fund works in an entirely unique way by combining AIB funding, EU funding and funding from an industrial partner. The minimum investment by the fund will be £50,000 and the maximum £1 million. The Fund will be promoted to encourage potential companies to submit their investment plans and will make its first investments in late 1997.

bridging the skills-management gap

AIB devised and conducted an innovative training programme for all bank personnel involved in lending to business. This was one of the biggest training courses undertaken by the private sector in Ireland. The training programme, known as *Credit Professionalism*, aimed to ensure that the banker had the specialised knowledge which is required to understand the business person's perspective and their business cycles.

Since a shortage of management skills is often the cause of the downfall of many small businesses, the Bank launched a workshop programme for small business people called *Essentials for Success*. This programme of workshops and lectures was designed to cater directly to the needs and concerns of small business. Since 1993 over 5,000 people have attended the workshops nationally and the Programme is entering its fifth year of operation.

AIB, in collaboration with Forbairt, sponsored the creation of a *Start-up-Panel* of mentors who were available to support small business people in an expert, advisory capacity.

In addition, AIB Bank designed business documentation to guide and assist business owners when submitting business plans and applications for credit facilities. The Bank also sponsored the highly acclaimed series of TV business programmes, "Start Me Up", aimed at providing advice and opinion on key business issues for early stage companies.



Increased approachability

AIB's small business strategy is based on *localised lending*. Local branches are now fully able to service the local community. Branch managers have a local knowledge which often means that they are the best people to evaluate a loan application, and this has been fully recognised by AIB - in fact, 90% of the needs of small business can and are being met by local branch management.

In order to establish general points of reference, and to regularise and standardise the relationship of the bank with its customers, the AIB Bank introduced a *Code of Practice for Business Customers*, outlining the mutual responsibilities of Bank and customer and the principles of good banking practices. AIB is the only Irish Bank to have a fully operational Code of Practice for business customers.

The Bank has also encouraged staff to participate more actively in local business organisations including Chambers of Commerce and County Enterprise Boards. This local involvement has helped AIB to appreciate the issues and challenges facing its customers. As part of its aim to become more locally based, AIB advertising strategy has taken a more regional and community-based focus through a more extensive use of local press and radio.

transparency on interest rates and fees

A number of steps were taken to pre-notify business customers of fees and charges and to ensure that there was more transparency around interest rates, charges and fees.

Since 1992, the Bank's fees and charges for business customers have not been increased. This was made possible because of increased efficiencies in new technology and economies of scale



introduced throughout the Bank's procedures. Fees and charges for business customers in Ireland represent a discount of about 50% on similar charges in the UK - providing a competitive advantage for Irish businesses.

Thirdly, technology was used to greater effect through services such as Electronic Business Banking, Paypath and Direct Debit.

The Results

AIB initiatives since the mid 90s were designed to re-position the Bank in the small business sector and in the public arena. More businesses have chosen AIB as their financial partner than any other bank. AIB lends more money to Irish business than any other Irish bank. However, the Bank knows that if it is to keep this business, it must keep working to expand its range of products and services.

The sustained growth in the Irish economy continues, the small business sector has played a crucial role in this economic upturn. There have also been cultural changes in Irish society. Attitudes to small business, to self-employment, and to the new breed of entrepreneur have become more positive and supportive. Profit and business success have become respectable things to strive for. Business ownership is regarded as a desirable occupation and the attitude to business failure is changing, with an appreciation that failure offers a valuable source of feedback, and that people who have tried and failed before are least likely to make the same mistakes again.

The Way Forward

AIB has responded to the identified needs of the marketplace and developed a programme for future support for the small business sector:

- AIB must understand the needs of every customer, whatever their business.
- The Bank must learn to give practical advice as well as coming up with innovative ideas for complex problems.
- AIB aims to establish and maintain close relationships with its business customers so that it can identify problems as they develop and exploit opportunities as they unfold.
- The Bank must expand its product range in order to keep its existing customers and win new ones.
- The Bank must maintain complete transparency in its dealings with customers.



- The Bank must continue its staff development programme to meet future financial challenges such as the Single European Currency.

AIB's future initiatives for the business sector will depend on customer needs. The Bank is committed to maintaining leadership in the market through its product development and business initiatives. Substantial progress has been made - AIB will continue to support and participate in the life of the small business community and is poised to maintain a future position as 'first choice' financial partner for small and medium business.

The definition of a small business

There is no universally accepted definition of a small business. For the purposes of a working definition however, there is broad agreement in Ireland that the small business sector includes enterprises that employ under 50 people and have annual turnover (sales) of less than £3 million. Enterprises that employ between 50 and 250 people are considered medium sized, and businesses employing in excess of 250 people are categorised as large. Small business activity is cross-sectoral and can include manufacturing, construction, or service suppliers. Many large enterprises that are household names such as Jefferson Smurfit, Marks and Spencer and Fyffes started life as small family enterprises.



The current position of small business in the Irish Economy

There are approximately 160,000 small businesses in Ireland. The Central Statistics Office estimates that in 1996, small business accounted for 28% of employment in the manufacturing sector; 75% of employment in the retail sector and 57% of employment in the wholesale sector. By any objective measurement, small business is a crucial component of the Irish economy.

TASKS AND ACTIVITIES

- 1** Discuss what you believe to be the defining characteristics of an entrepreneur.
 - ii How does your definition distinguish the entrepreneur from any other businessperson?
 - iii Can you identify a potential entrepreneur in your class?
 - iv Is there general agreement about who you have identified as a potential entrepreneur?
- 2** Reflect upon and discuss your own career ambitions in the light of what you know about the characteristics of entrepreneurs.
- 3** Why do banks exist?
 - ii To whom are banks accountable?
 - iii Should banks have social obligations and responsibilities?
 - iv What are their obligations and why do they have them?
- 4** Obtain the latest annual reports of the main Irish banks as a class resource. Draw up a table comparing the Interest Income, Profit before Tax, Profit after Tax, Net Assets and Shareholders Funds. Assess the claim sometimes made that banks earn too much profit.
- 5** Obtain a copy of the *Financial Times* on 1st day of January and arrange to purchase it subsequently on the 1st February, 1st March and 1st April (or any other consecutive 4 month period). Divide the class into ten groups each representing one of the industrial sectors listed in the *FT London Share Service* pages. At the outset (Jan. 1), each group should select five shares of their choice from that sector - representing their portfolio. At each subsequent date, the group should monitor the increase/decrease in price and at the end calculate a return for the portfolio.
- 6** Define working capital in an enterprise. What is the working capital cycle of an enterprise? For the companies that you selected in Question 5 measure the working capital cycle of each enterprise.
- 7** The branch type organisational structure is common in certain industries banking, insurance and retailing among others. What general problems does the branch type structure pose for organisations? Are there additional problems posed by this form of organisation for banks? In relation to banks specifically, consider each of the problems you identify and develop solutions for dealing with these.
- 8** Sketch in broad outline the *bank of the future* - pick 2020 as the year.
- 9** Assign students into groups of 5 to prepare a business plan for a small enterprise. The plan will be presented to the loan committee of a financial institution. Your enterprise may be some activity that you would like to pursue when you leave school or alternatively a more limited activity spanning (say) a three month Summer vacation. Your business plan should identify and evaluate the potential market, and explore the technology and finance needed to establish your business.



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