Panel Discussion: What is the Future for Small Business?

The final session of the Conference was a panel discussion about the panellists’ experiences in the small business sector and how they saw the future for small businesses. The panellists were drawn from a wide cross-section of the small business sector, including representatives from the not-for-profit sector, the entrepreneurial sector and an industry body. The discussion was chaired by Michael Schaper, Deputy Chairman of the Australian Competition and Consumer Commission and Adjunct Professor at the Curtin Business School. The panellists were:

- Michael Henderson – Founder and Chairman of MEDSCI International Healthcare and Adjunct Professor with the Faculty of Medicine, Dentistry and Health Sciences at the University of Western Australia
- Bruce Jeffreys – Co-founder of GoGet CarShare and Dresden Optics
- Kate Carnell – Chief Executive Officer (CEO) of the Australian Chamber of Commerce and Industry.

Each panellist provided their views after which the Chair invited comments and questions from all participants.

1. Michael Henderson

I am not an economist, nor a banker and I am not here with an academic hat on. Instead, what I want to do today is to look at a couple of grassroots examples of social and corporate entrepreneurship, from my perspective as an entrepreneur. I want to use these examples to illustrate the way that innovative technologies have changed, and will continue to change, the landscape for small and medium-sized enterprises (SMEs) and not-for-profit organisations. This matters because these enterprises can promote social outcomes like remote access to health care and can deliver cost savings for the health sector. The future of SMEs and the not-for-profit sector depends on ensuring that we continue to provide the technology platforms that permit these enterprises to achieve these outcomes and deliver these savings.

I have had a very personal experience with the way technology can and has transformed health care. Three years ago I was hit in the face by a tow rope while I was in a remote town north of Perth, Western Australia. The impact threw me into the air and I ended up with a critical injury of my eye, a broken nose, a broken cheek and a broken eye socket. I was taken to an after-hours medical centre, which was staffed by a nurse who was completely distraught about how to manage me and my injury. I was lucky that on my smart phone I could call a Professor of Ophthalmology, who was on holidays in Sydney at the time. We converted to a Skype call and – with intervention from the ophthalmologist – we were able to save my eye. Without that Skype call, I would have most likely lost my eye within the next five to ten minutes.
This experience really reinforced my view that everyone should be treated the same and have equal access to medical care via technology that is capable of delivering valuable social outcomes. Ultimately, I wanted to use technology to improve conventional medical support by potentially having up to six specialists over the shoulder of a paramedic, nurse or GP and to deliver specialist, acute advice that would not otherwise have been available to a paramedic, nurse or GP in a remote site. This support program has grown exponentially and is now providing acute point-of-injury and triage support for major resource companies – both onshore and offshore – and the program is now being backed by a major international emergency response group.

SMEs can be found in both the for-profit and not-for-profit sectors, and the future growth of both types can benefit from new technologies. For example, another not-for-profit SME delivering ‘multiplier’ social outcomes is the International Skills and Training Institute in Health (ISTIH), which I co-founded with Professor Bruce Robinson in 2005. The idea with ISTIH is to build healthcare capacity by having a volunteer doctor travel overseas to train and ‘upskill’ local doctors as trainers themselves. These doctors can, using the same training platform, pass this knowledge on to others. It is like dropping a pebble into a pond. These ripples mean that you have the expertise in place when the next tsunami or natural disaster strikes, to save the lives of people that would otherwise die in the first 6 to 12 hours if those services had not been developed.

One of the most interesting examples of a small not-for-profit using technology to transform health care is Silver Chain Group headquartered in Western Australia. They have now grown to be a significant national interest on the back of this technology. What they have been able to do is provide a unique and cost-effective model for managing patients. They are able to deliver services to groups of patients for say $60 million or less, when delivering services that would have previously cost state governments $80 million or more. The really interesting thing about this small not-for-profit is the technology that the organisation has developed. This technology is now being considered for sale to one of the major telecommunications companies and is not only going to change the way medicine is delivered nationally and internationally, it will also promote that social outcome of equal access to medicine that I discussed earlier.

All these SMEs are using technology in new ways to deliver social outcomes. The future of innovative SMEs really hinges on leveraging technology in innovative ways. So the real question that these observations and examples raise for me – and I put this out there as a grassroots individual, not an economist or policymaker – is: how do we provide SMEs and the not-for-profit sector with the skills and technology they need?

We need to be smart and think about this question in terms of an overarching and holistic funding model and not focus at the micro level in terms of an individual SME. We need to think about the best ways to fund and bring together organisations like the Commonwealth Scientific and Industrial Research Organisation (CSIRO) and National ICT Australia (NICTA) to provide technological infrastructure for SMEs. We need to ensure that these efforts are focused and not spread randomly across disparate federal government organisations. We need to make sure that these institutions can provide tools for SMEs and the not-for-profit sector, particularly because both these types of enterprises can provide significant cost savings for the burgeoning federal health budget and promote valuable social outcomes. With the government funding constraints that are in play at the moment, we need to think laterally about these issues. The future of these sectors depends on addressing the question I raised above.
2. Bruce Jeffreys

For me, there are really two major changes that are shaping the future for small businesses. But I want to first detail the two businesses I am involved in and then link these businesses to the changes that I see.

I founded GoGet with Nic Lowe in 2003. It seemed like an easy idea: why not share unused cars rather than everyone owning a car? It was a classic small business: no capital; two people who did not really know what they were doing; and everything was built from the ground up. The only exception is that we were not based in a garage because we were in inner-city Sydney – all we had was a laundry. We started with three cars; we built a booking system; and then we put these cars online for people to become members and use them by the hour.

We had 12 customers initially. The cars were hardly used, which really underscores just how underutilised this very expensive fixed asset really is. It took us about three years to get to 20 to 30 cars, and then another couple of years to get to a couple of hundred. From there, it really took off. After 12 years, we now have 60 000 members and we are about to hit the 2 000 car mark.

It did not seem like what we were doing was that new because people had been sharing cars forever. But we formalised it, so it really was a whole new business model. As a result, we ran into a lot of barriers along the way. Financing was a problem; so were regulations and insurance. With everything we touched, we fell into a grey area. For instance, the then Road and Transit Authority did not know how to deal with us – they could not figure out if the cars were business or private. But we had extremely enthusiastic members who loved the service and who powered our growth through word of mouth.

The second business I am involved with is Dresden Optics, which I co-founded about a year ago. Dresden Optics is about challenging the manufacturing model for retail optics. The current optics industry – like many consumer goods industries – has an extremely long and complicated supply chain. We are launching a retail store with injection-moulding manufacturing instore. The idea is you can bring in plastics – like the lids of drink bottles – and mould them into glasses frames. It is about responsive manufacturing.

We are trying to reinvent the model for optometry with Dresden because the conventional optics industry delivery model is quite outmoded and extremely expensive. We want to break the model of having to make a booking and an appointment, and only doing so when you have a problem. We are offering free self-service eye testing that will then go – via the cloud – to ophthalmologists and optometrists. We want to screen the whole population and pick up things that are not currently an issue – including non-eye-related health issues like diabetes. This is possible because the costs for the equipment have fallen through the floor. The equipment that scans eyes used to cost $250 000; it now costs just $10 000. But the whole Medicare model is built on those old cost-of-equipment assumptions. What we are trying to do with Dresden really dovetails with what Michael was talking about with Silver Chain. We are using technology to change the way health services are delivered.

Those are the businesses I am involved in and where I have come from. I will turn now to what I think is changing in the small business sector and how that is going to shape the way future
small businesses may look. These changes are behind the success of GoGet and behind what we are trying to do with Dresden.

The first change is the internet and the fragmentation of the economy and systems. What we are doing with GoGet could not exist without the internet. We were fortunate with our timing when we started. The internet has allowed us to connect this decentralised micro-fleet of vehicles to everyone’s smart phone. You can pull up our website on your phone and have a car within walking distance that is ready to go, right now. It is an amazing convenience. With Dresden, the internet and this fragmentation have driven the commodification of manufacturing; small-scale manufacturing equipment is now really quite cheap to buy. We could not have the responsive-manufacturing model that we are building with Dresden without that. This fragmentation, driven by the internet, creates so many opportunities for small businesses to step into niches.

The other major factor is that values are changing – especially in younger people. When we started GoGet it was a bit of a ‘green’ thing to do; now it is just common sense. Environmental values are intrinsic now. There has been a big shift in values. With Dresden, what we are picking up on – and hopefully what will resonate with consumers – is that consumers feel cut out from the way that big businesses deliver products. Consumers feel very alienated. We are trying to tap into this grassroots movement that wants to know where products have been made, what’s in them and how they work. The small-scale manufacturing that we’re doing – in store – really taps into that shift in values.

And so I think small businesses have a huge opportunity now and into the future. Consumers want to feel connected to what they are buying; big businesses cannot provide that. With the internet and the fragmentation it creates, it is possible for small businesses to find their market, find their niche.

I will finish with what I think is the biggest barrier that small businesses in Australia face. It is extremely exciting starting businesses in Australia; it is incredible how easy it is to do. But the biggest barrier I face is my staff thinking of why they cannot do something. They have a very risk-averse mindset. Risk is viewed negatively; it is viewed as recklessness. But the advantage of small businesses is that they can take risks. The future of small businesses – and entrepreneurs in particular – depends on finding people who can move beyond just thinking about the risks to thinking about the benefits and only then thinking about what risks need to be taken.

3. Kate Carnell

I thought I would start by going backwards for all the economists that are here today. Back in the 1770s, Scottish economist and philosopher Adam Smith was talking about division of labour and specialisation. What are we talking about here today? We are talking about specialisation – that small businesses in Australia can do smaller and smaller bits of a supply chain, do it really well and do it in a global free market. And before anyone in this room was born, Austrian-American economist Joseph Schumpeter was talking about creative destruction.

Maybe nothing is new in the universe.

I am from the Australian Chamber of Commerce and Industry (ACCI) and I bought my first small business – a pharmacy that I ran for 20 years – when I was 25. I have seen small business change
over the years, but the main issues have not. At ACCI, our members – and we represent more than 300 000 SMEs in Australia – tell us that their biggest issues are access to market, access to people and access to capital.

These same issues go all the way back to Smith and Schumpeter. What is exciting for the future of small business is how technology is changing the responses to these issues. Smith and Schumpeter did not have the internet.

Let’s talk about access to market. Technology has really changed how quickly businesses can take products to market and get take-up. It took 75 years for the telephone to get to half of the population; it took the smart phone less than 10. This increased pace means that businesses need to be more flexible, more nimble and more capable of changing quickly. This puts small businesses in a really good place.

In terms of the way small businesses are getting their products to market, there are three waves that describe how businesses look now and how they will look in the future.

The first wave is those businesses that are using technology as an add-on to their core business. Technology – the internet in particular – grows their market, but the underlying business has not changed. I will give you an example – although this one is partly second wave too – based on a dress shop called Birdsnest, a fashion retail outlet on the main street of Cooma. Birdsnest is a family-owned and operated business, and it was going broke. The family took the business online and they are now employing 100 staff. What they have done is personalise their service; Birdsnest helps you solve your fashion and style problems.

The second wave is businesses that are starting up with a tailored service, a service that is really about individuals. I will use a company called Shoes of Prey as an example. It is an Australian company that lets women design their own shoes. They can specify what heels they want, what colour and what add-ons – they design and order their own personalised shoes. And Shoes of Prey has a 365-day warranty where the shoes can be returned for a refund or sent back to be redesigned or fixed. It was winner of the Online Sales category in the 2014 Premier’s NSW Export Awards. It is a company that does not sell shoes; it works with customers to grow a product.

The third wave of businesses is very much about products and services we did not even know we needed and new solutions that no one had thought of. GoGet is a great example: I need to be able to travel, but now I need not have a car. Fifteen years ago, no one in Australia had thought of that.

So, in terms of access to market, there is a whole range of new and novel approaches.

Access to people is the next area that technology is changing. Once upon a time you would put an advertisement in the newspaper; that is not done very much now. After that, it all moved onto internet sites – you would put an advertisement on somewhere like Seek. Now you can go to somewhere like Freelancer, to use an Australian example. Freelancer’s approach is ‘if you’ve got a skill, we can get you a job’, not the other way around. With Freelancer, I can go online and find someone to do just about any job. A friend of mine’s Executive Assistant (EA) is in the Philippines – her EA is on the phone, on the internet, and she can manage her diary out of the Philippines just as well as anybody else. She is the only person I know who has an EA with a PhD. The internet is really expanding the capacity to find people for roles.
Another example is DesignCrowd. We used it recently for some graphic design work we needed done for a subsidiary company. We logged on to DesignCrowd, specified what we wanted and the price we were willing to pay; they asked a couple of questions and sent us back some ideas. After paying $250, we had a logo and some business cards. It turned out that the person who did the work for us was from a little town in Ohio.

Access to capital is the last area that I want to talk about. Our members tell us that their biggest problem is access to capital. Access to traditional finance is becoming harder and harder for young people – the people that are setting up innovative businesses and growing them – because so few young people own houses which they can use as security for a loan. Housing affordability is a real problem.

But the internet is changing access to capital for small businesses through crowdfunding and peer-to-peer lending. A great example of the success of crowdfunding is a product called Flow Hive. It is a new beehive design – developed by a father and son out of Tamworth – where you don’t have to pull apart the beehive to get the honey out. They needed $70,000 to take it to the next phase in order to manufacture their product. They went on to Indiegogo and, as of this morning, had raised over $6 million, a lot of which is from the United States. What you can do on that site is buy a beehive, or bits of a beehive, or just send money to support them. This is what the future of financing looks like for a lot of people. And you would be aware that the Federal Minister for Small Business – the Honourable Bruce Billson MP – has indicated that he is planning to launch a crowdfunding platform later this year, and he has been out consulting in the market.

I think the banks are starting to realise that the train has left the station with respect to crowdfunding. At ACCI, we have a line-up of banks asking what they can do for small business. They see that things have changed. But I think they still cannot get around their risk issues.

Research suggests that it might not be the age of the business that matters, but the digitalisation (Deloitte Access Economics 2013). It has found that the 16 per cent of small businesses that are highly digitalised are four times more likely to be employing. The internet and technology are changing all aspects of the economy, and that is a huge opportunity for small business. There are new and radically different answers to the issues that small businesses face – access to market, access to people and access to capital – because of the internet and technology.

The world has changed.

Reference


4. General Discussion

Discussion focused on the public policy implications of the panellists’ remarks, particularly with respect to support and financing for small businesses.

A participant began the discussion by noting that all the panellists’ remarks had focused on the importance of the internet in connecting businesses with customers. In this light, the participant
asked the panellists’ views on the value of government-provided infrastructure – using the National Broadband Network (NBN) as an example – versus government subsidies such as the research and development tax credit.

Kate Carnell responded that small business subsidies tend not to work very well. ACCI’s members rarely say that what they need is more government support. Rather, they have problems with forms and red tape. As long as you have sensible policies – for example, sensible tax treatment of acquisitions and depreciation – what really matters is infrastructure: whether that be roads, ports or the internet. What matters for businesses is getting their product to market. If the infrastructure is not in place to do that, subsidies are no use. Michael Henderson stated the question was a bit like asking, ‘I have water and I have a glass, which would you prefer?’. Rather, the biggest value proposition is the entrepreneurial interaction with existing infrastructure – where someone looks entirely differently at something that everyone has access to. Professor Henderson opined that the more important question is how the government can inspire and capture the benefits of those innovations that lead to both national and international value.

Relatedly, a participant queried the panellists’ opinions on the importance of fibre-to-the-home or fibre-to-the-node for the NBN. The panellists agreed that it really depended on the application; most small businesses did not need the high speed provided by fibre-to-the-home. What was critical for small businesses was robust and reliable internet access. In addition, emerging new technologies – that were potentially more cost-effective – made it difficult to definitively state that one particular model was best.

Discussion turned to funding for small businesses. One participant noted that European regulators have been looking at crowdfunding platforms and have run into two competing considerations. On one hand, heterogeneity of regulation across the many regulatory regimes in Europe has meant that overseas platforms cannot operate in Europe and European platforms cannot even operate across all of Europe. On the other hand, regulators have to consider investor protection in the event of business failure. Balancing these two considerations is proving challenging. Ms Carnell noted that regulation of crowdfunding and peer-to-peer lending was likely to happen shortly in Australia. She stated that it would have to be a light-touch regime. Consumer and investor education about the risks is important, but overregulation will kill crowdfunding.

Continuing on the theme of crowdfunding, a participant noted that it is an adjunct to traditional bank funding, rather than an alternative (as it is often presented). Crowdfunding has a huge advantage because it can be used pre-production, before a firm has revenue. No bank can provide that sort of funding, because firms at that point cannot service the interest on a bank loan. The participant noted that the crowdfunding success stories – including the example discussed by the panellists – did not raise money to commercialise a product. Rather, they used crowdfunding to pre-book sales. The participant opined that there would be some interesting challenges emerging in the future around prepayment exposure – once a firm reaches its funding goal and charges everyone’s credit cards, the risk is back on the banks.

Another participant picked up on the same point and noted that the pre-sales model of crowdfunding solves a problem that banks cannot. Even if a bank is interested in a firm, the bank cannot know whether the firm’s products will succeed in the market. With the pre-sales model, lots of firms can put their products up on the sites unsuccessfully. However, unlike with a traditional
bank loan or equity investment, no one has committed to these unsuccessful firms and nobody loses any money. The participant opined that this was why pre-sales models have proven to be the most popular among crowdfunding platforms.

A participant stated that there was a disconnect in the regulatory dialogue about banks and small business lending. On one hand, the dialogue focuses on the importance of stable risk-averse banks, but on the other hand chides banks for not taking risks and lending to small businesses. Ms Carnell agreed that the Australian banks face difficulties in balancing the risks of small business lending. However, she noted that there was a problem going forward because so few young people – the people growing innovative businesses – own houses, which they could use as security for a loan. She noted that this was, by far, the biggest issue that ACCI hears from its members. A number of participants agreed, but noted that collateral is not the only factor that affects small business lending. Banks do lend to small businesses on an unsecured basis; however, the loans tend to be much smaller and more expensive.

Bruce Jeffreys noted that he had only been able to finance the cars used to start GoGet by using a house as collateral. On the topic of access to bank finance, he opined there was a dissonance between bank advertising and what small businesses experience. He stated that it would often be better for banks to always refuse to lend, so that small businesses could go and find alternative funding straightaway. Rather, it had been his experience that banks often took too long to say ‘no’ and spent too much time on time-consuming processes, such as interviews with branch managers. Small businesses are vulnerable because they are burning through their money; if it takes six months instead of a week to get refused a loan, it makes a big difference. In response, Professor Henderson partly disagreed. He stated that, in the areas and sectors that they operate in, the banks do a good job. However, he agreed that in other areas – particularly entrepreneurial SMEs – there was an opportunity to move those financing options that are seen as risky by regulators out of banks and into other processes for funding SMEs.

On the topic of the venture capital industry, a participant noted the puzzling finding that venture capital investments – at least in the United States – have been extraordinarily unprofitable. The participant cited a report by the Kauffman Foundation that showed that limited partners had consistently underperformed the market (Mulcahy, Weeks and Bradley 2012). The participant noted that this fact raised questions about crowdfunding and peer-to-peer lending. Mr Jeffreys agreed and stated that, in his view, the US venture capital model is very flawed. He noted that GoGet did not use venture capital funding; rather, it was grown by working for free and growing it organically. He stated that the venture capital model is flawed because it is a ‘star model’; it is built on the idea of the ‘crash-through’ entrepreneur who has a great idea. This model is at odds with reality; building a business is far less glamorous. The entrepreneur is on their own, dealing with the day-to-day tasks. However, too many young people automatically look to venture capital for funding. Mr Jeffreys noted that this was a concern because it set too many businesses up for failure unless they were a ‘superstar’. Professor Henderson agreed that the US venture capital model is very aggressive. However, he thought that the model was beginning to shrink back in Australia and was being replaced by a more relationship-based model, which was proving to be more manageable and a more effective model for SMEs.
The final comments for the discussion focused on the role of innovation. A participant noted that a paper earlier in the conference had shown that most firm-level innovations are firms using ideas obtained from other firms, rather than truly new innovations (Palangkaraya, Spurling and Webster this volume). By contrast, the panellists’ examples were mostly new innovations, which suggests that those types of innovations were the most important from a social perspective. However, firms cannot necessarily capture all the benefit of those types of innovations because other firms take the ideas, and in many cases those ideas won’t be patentable. The participant wondered whether enough was done to promote these types of innovations. Professor Henderson agreed that it was critical that there was support in place, whether at the federal, state or industry body level. He noted that Silver Chain Group illustrates how important SMEs can be in developing valuable intellectual property; the technology that Silver Chain Group has developed and patented is being considered for sale to a major telecommunications company. Ensuring there is support for SMEs is particularly important, because many do not have the luxury of being able to secure their intellectual property.

Reference

Mulcahy D, B Weeks and HS Bradley (2012), “‘We Have Met the Enemy … and He is Us’: Lessons from Twenty Years of the Kauffman Foundation’s Investments in Venture Capital Funds and the Triumph of Hope over Experience’, Report, Ewing Marion Kauffman Foundation, May.