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## Critical Business Environment Factors for SMEs in the UK Chemical Distribution Industry: A Qualitative Perspective

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### Abstract:

The UK chemical distribution industry is a significant and well-established, yet fragmented and subject to strong consolidation, part of the chemical industry and a major contributor to the UK economy and employment. However, it remains largely unexplored, with limited research in the factors contributing to SMEs success. This paper, which is part of a larger-scale study, addresses a well-established gap in the UK chemical distribution industry and provides a qualitative perspective of the *business environment* factors critical to the success of small and medium-sized distributors. This research is based on the opinions of owners and very senior managers (Managing Directors, Directors, CEOs and CFO's), an approach extensively used by other researchers. A total of 180 SMEs fulfilling the criteria of this study are identified with 118 owners/managers participating, generating a very satisfactory response rate of 65.5%. The paper informs key stakeholders and policy makers with a view to improve strategy formulation and decision-making process in supporting chemical distribution SMEs.

**Keywords:** Business Environment; Critical Success Factors; SMEs; UK Chemical Distribution Industry; Qualitative Study.

### 1. Introduction

Small and medium-sized enterprises (SMEs) are the focus of political, business and management research with their benefits firmly established (Amoros et al., 2013; Dobbs & Hamilton, 2007; Halabi & Lussier, 2014). These are integral to contemporary economic and social regeneration (Unger et al., 2011), essential for the establishment of a solid industrial base (Smallbone et al., 2010), key driver for innovation and R&D (European Union, 2015) and above all significant contributors to employment generation (Lussier & Halabi, 2010; McLarty et al., 2012; Simpson, Padmore, & Newman, 2012). Despite their well-established importance, there is still no universally accepted definition for SMEs with significant variations in different countries (Smallbone et al., 2010; Unger et al., 2011), no single agreed-upon definition of success (Beaver, 2002; Rogoff et al., 2004), no universally accepted model to incorporate all aspects of small business success (Chawla et al., 2010; Lampadarios et al., in press) and with knowledge being more fragmented than cumulative (Dobbs & Hamilton, 2007). Most importantly, SMEs tend to exhibit high failure rates and poor performance levels (Arasti, et al., 2012; Franco & Haase, 2010; Gray et al., 2012; Ropega, 2011) with their success and/or survival receiving an ever-increasing attention from academia and practitioners alike. Business literature features a wide range of success factors through a number of conceptual frameworks that attempt to capture aspects of SMEs success. However, their importance appears to be relative and varies with the business environment, that is the industry and country SMEs operate in; meaning that while one success factor may be of great importance in one industry or country, it may not necessarily be of equal importance in another (Benzing et al., 2009; Kader, et al., 2009; Krasniqi et al., 2008; Lin, 2006; Simpson et al., 2012). This inevitably creates a need for more empirical studies to investigate the critical success factors in each individual industry and in a specific country setting.

An industry where small businesses have a particularly strong presence is the European and especially the UK chemical distribution (BCG, 2013; Chemagility, 2012; Disticonsult, 2013; European Association of Chemical Distributors

[FECC], 2013). However, very little is known about SMEs in the specific industry, their *modus operandi* and any factors contributing to their success and/or failure (Chemical Business Association [CBA], 2015; FECC, 2015). In fact, due to the wide variety of functions performed by these companies and confusion with other types of trading in the industry, there is still no universally agreed definition of a chemical distributor (Chemagility, 2012). More importantly, there has been no academic study on the success of small and medium-sized chemical distributors in the UK and even on a European level, very little research exists (Hornke, 2012); mainly attempts being made by industry consultants such as Districonsult and the Boston Consulting Group (BCG). Also, there appears to be no official statistical and/or financial data available on the companies operating in the industry (Chemagility, 2015). With the UK chemical distribution being an important yet understudied industry with very little known about small businesses and their success, a clear research gap is established.

This paper is part of a study conducted by Lampadarios (2015, 2016). The primary aim of that study was to identify and investigate the factors critical to SMEs success within a specific industry and geographical context; the UK chemical distribution industry. The success factors were categorised in entrepreneurial (relating to the individual), enterprise (relating to the firm) and business environment (external). Furthermore, in order to develop a more comprehensive view of the industry and provide a richer, deeper view into the research topic, qualitative data on the individual success factors was also collected. However, due to the large amount of data and as it would not have been possible to disseminate them all together, these were presented separately. To that end, this paper reports and discusses the qualitative aspect of the business environment success factors for small and medium-sized chemical distributors in the UK.

## 2. UK Chemical Distribution Industry

Chemical distributors are a fragmented network, positioned between chemical producers and their customers, adding value through an extensive range of services to both customers and suppliers such as managing complexity, accessing markets, providing financing and support etc. (Chemagility, 2008; FECC, 2011). Even though chemical distribution is a well-established practice in the UK, it is severely understudied both on an academic and business level with the majority of information originating from the study of the European chemical distribution industry (Districonsult, 2013; Jung, et al., 2014; Hornke, 2013; Mortelmans & Reniers, 2012). Similarly, there are limited statistical data available on the industry and information such as turnover, sales and margin growth, performance and future trends are drawn from industry reports (for instance Chemagility).

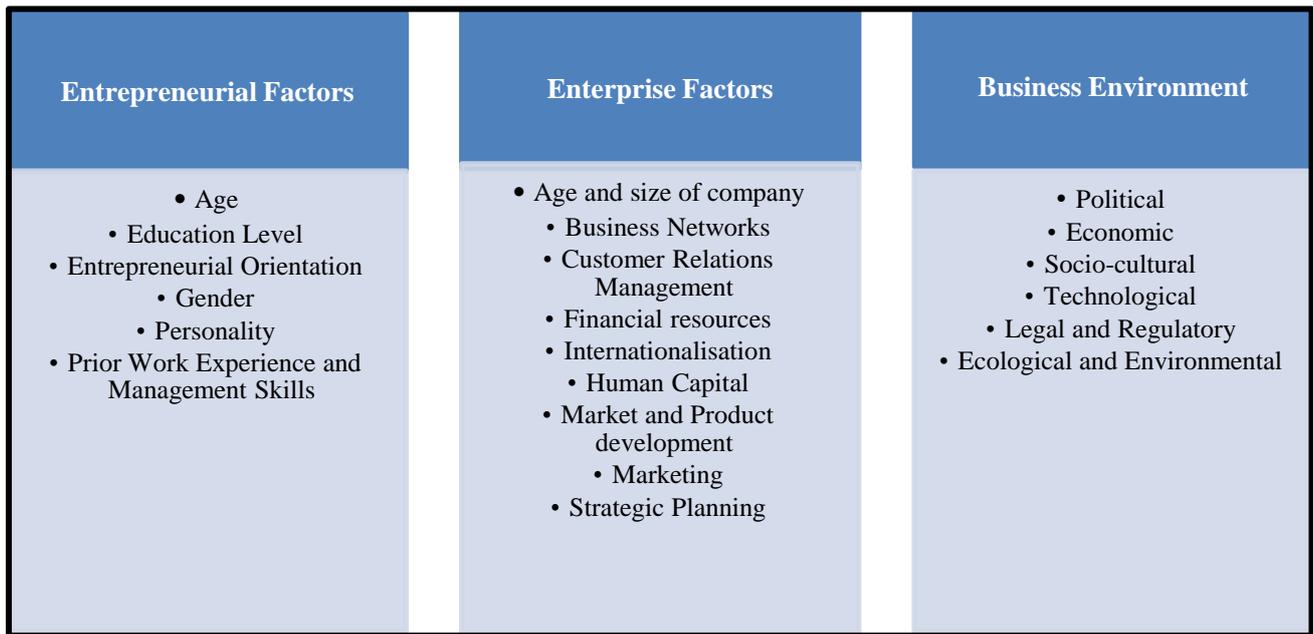
The UK chemical distribution industry is a growing, well-established, significant part of the chemical industry (Chemagility, 2008) and remains a significant contributor to the economy and employment (European Chemical Industry Council [CEFIC], 2012; FECC, 2013; Hornke, 2013). According to the latest data available from Chemagility (2015), in 2014 the UK chemical distribution market was worth GBP 4.42bn (EUR 5.44bn), employing circa 6,800 employees and representing 10% of the total European chemical distribution market worth EUR 52bn. With the total number of chemical distributors in the UK being 280 and with over 75% of them being small or micro-sized enterprises (210 companies if subsidiaries of larger international groups are excluded), it is evident that SMEs have a very strong presence in the specific industry. Despite major challenges due to increasing compliance costs, reduced margins, global competition and uncertainty, the UK distribution market achieved a 6% annual growth rate between 2005 and 2010, a 5% growth between 2011 (GBP 4.1bn) and 2014 (GBP 4.5bn) and is anticipated to grow further to GBP 5.6bn by 2020 at a rate of 3.6%, which is higher than expected the GDP growth (Chemagility, 2015).

However, the industry, like the rest of Europe has also experienced significant industry consolidation resulting in the overall reduction of the number of companies present and increasing even more the pressure on the survival of SMEs (Chemagility, 2012; Key Note, 2011; Kronimuns et al., 2009; Plimsoll, 2013). It is worth noting that in 2014 large enterprises and multinationals held 67% of the total UK chemical distribution market value, leaving a smaller share of 23% (GBP 1.47bn) to all other small businesses (Chemagility, 2015).

## 3. SMEs Success Factors Framework

Generally, there is no universally agreed framework for carrying out research in the area of SMEs success (Chawla et al., 2010; Dobbs and Hamilton, 2007; Halabi and Lussier, 2014; Simpson et al., 2012). The most recently informed and highly consolidated framework is that of Lampadarios et al. (2015). This is based on the extant literature, including entrepreneurship and not only SMEs specific studies while incorporating factors contributory to all aspects of small business success (growth and non-growth) and failure. The basis of this framework is a number of influential studies and established models in the areas of SMEs and entrepreneurship (e.g. Lussier, 1995; Chawla et al., 2010; Ropega, 2011; Rogoff et al., 2004; Simpson et al., 2012; Global Entrepreneurial Monitor (GEM) and Vienna Entrepreneurial studies (VES) initiatives) which then expanded to include the plethora of studies that had been conducted in varied industries and geographies from the mid-1990s until 2014. This is shown in diagrammatic form in Figure 1.

Figure 1: Conceptual Framework (Adopted by Lampadarios et al. , 2015)



This framework categorises the variables of small business success into three broad categories: factors relating to the individual (personal or entrepreneurial), factors relating to the firm (enterprise) and factors relating to the external business environment. This is an approach widely used in studies investigating small business growth and success factors (Andersson and Tell, 2009; Caca, 2010; Kader et al., 2009; Karpak and Topcu, 2011; Krasniqi et al., 2008; Ogundele, 2007; Simpson et al., 2012; Smallbone and Wyr, 2000).

The entrepreneurial (personal) factors include those variables which are considered specifically related to the owners/managers of SMEs and consist of their personality traits, characteristics and features, acquired skills, experience and background dimensions. For instance, the age and gender of owner/manager, education, motivation, personality traits and characteristics and any prior work experience and management skills. The enterprise factors are any factors relating to the business itself; that is the structural characteristics, policies and strategies of the firm. These are the age and size of company, business networks, customer relations management capabilities, financial and human resources, internationalisation, market and product development, marketing and strategic planning. The business environment factors include any external determinants reflecting the political, legal, economic, sociocultural, technological and ecological elements. This is in line with the PESTLE analysis framework comprising of political, economic, socio-cultural, technological, legal and regulatory, ecological and environmental factors.

#### 4. Methodology

To achieve the aim of the study, a survey strategy was utilised and self-administered questionnaires -incorporating open questions- were used to collect the views of owners/managers. As the collection of data -qualitative in nature- was based on pre-determined themes (success factors) the use of more sophisticated methods of analysis (for instance quantitative content, thematic) was not deemed necessary and thus this research drew upon the basic principles of qualitative content analysis. This is a well-established, flexible and straightforward qualitative data analysis method (Finfgeld-Connett, 2014; Krippenforff, 2013; Polit and Beck, 2012; Vaismoradi et al., 2013) that represents a systematic and objective means of describing and quantifying phenomena (Bloor and Wood, 2006; Gbrich, 2007; Pope et al., 2006; Powers and Knapp, 2006; Schreier, 2012). In line with content analysis, during this study data were collected, collated under the pre-determined categories, reduced, summarised and finally reported.

All participating companies were SMEs as defined by the European Union, that is enterprises employing fewer than 250 people and with an annual turnover not exceeding EUR 50m (European Union, 2003); located in the UK; not part of a another organization or belonging to a larger corporation and without any manufacturing activity and capability.

Due to the fact that there had been no official statistical data on the total number of SMEs operating in the UK chemical distribution industry, a combination of industry reports (Plimsoll, Chemagility, Key Note), business associations (the British Association of Chemical Specialties, the Chemical Business Association, the European Association of Chemical Distributors, the National Association of Chemical Distributors, the North East Process Industry cluster), internet sources (the Chemagility Online Database of Chemical Distributors and ICIS magazine, were utilised to produce a comprehensive list and thus determine the target population for this study. Each of the identified SMEs was individually

checked at a later stage to ensure they fulfilled the criteria of the study. However, lack of official statistical data on the target population means that allowances should be made for omissions due to human error and for the fact that the total number of SMEs operating in this industry may have changed since the time of the study.

The total number of SMEs in the UK chemical distribution industry satisfying the criteria was 180. No sampling technique has been used but instead a census was conducted. Owners and very senior managers (CEOs, Managing Directors-MDs and Directors) of SMEs in the UK chemical distribution industry were the key informants, an approach extensively used by other researchers (for instance Keskin, 2006; Lee and Cheung, 2004; O'Cass and Weerawardena, 2009; Ojala, 2009; Revell, 2007; Wilson et al., 2012). A total of 118 SMEs responded positively by returning the questionnaire, in a usable and valid form for statistical analysis, generating an overall response rate of 65.5%. Thus, it can be argued that the findings of this study offer a reliable representation of SMEs operating in the UK chemical distribution industry.

## 5. Findings

Based on Lampadarijos' (2015 and 2016) study, Legal and Regulatory, Ecological and Environmental and the Economic environment are identified as the most important business environment success factors for SMEs in the UK chemical distribution industry and are thus considered critical. These factors and their importance are investigated further through the collection of qualitative data from the participating owners/managers, providing a richer, deeper view into the research topic.

A very interesting finding of this study is the fact that the vast majority of owners/managers consider Legal and Regulatory and Ecological and Environmental factors very closely related and interlinked with each other in the context of the UK chemical distribution industry. In more detail, 68 out of the 71 respondents who identify the above factors as the most important ones, express the opinion that both should be viewed as one factor, under regulatory compliance: '*...industry views both as one factor with same effect on the business...*' (R115); '*...we have always treated those two factors as one...*' (R19); '*...the effect on the business is very similar...*' (R48); '*...regulatory compliance covers both areas...*' (R56). In fact, owners/managers further comment that it has been very common practise for Ecological and Environmental requirements to be 'translated' into Legal and Regulatory requirements in this industry. The main reason behind their argument is the fact that ecological and environmental factors create and drive the need for regulation, which is subsequently expressed through legal and regulatory factors.

In justification, it has long been established in the business literature that the use, production, transportation and safe disposal of chemicals has an adverse impact on both human health and the environment (European Chemical Agency, 2014; Keynote, 2013; Jerrentrup, 2009). As a result, the chemical and subsequently the chemical distribution industry have been traditionally heavily regulated with this trend having intensified in the recent years where a number of initiatives aim at developing industry-wide support for best-practice standards i.e. REACH, Biocide directive etc. (CEFIC, 2013; European Chemical Agency, 2014; Hillier, 2013). As such, it has never been uncommon practise for Ecological and Environmental requirements to develop into Legal and Regulatory requirements. On the basis that owners/managers consider these two factors as one prerequisite for success, this study reports and further analyses them both under the 'Regulatory compliance' umbrella.

### 5.1 Regulatory Compliance

Regarding the effect of the business environment on the success of small firms, many respondents (20 in total, 17% of population) express the opinion that smaller SMEs are quite unaffected by the environment they operate in. In more detail, smaller companies are considered to be less affected by their environment as they can adapt quickly to new situations and thrive in all conditions depending on their offering thus increasing their chance for survival: '*...small companies can always adjust...*' (R9) and '*...if something changes in the market, we can change quickly too...*' (R14). This is unlike larger companies that need more time to react and are less flexible to any change in their environment. However, owners/managers unanimously agree (70 out of the 71 respondents who considered regulatory compliance the most important success factor) that the only elements that cannot be disregarded or avoided in the business environment are the regulatory requirements: '*...no way you can avoid ...*' (R49); '*...compliance is not an option, it has to be done...*' (R59); '*...extremely difficult to work around regulations...*' (R18); '*...there will always be a good business idea that would work regardless of the business environment but regulations cannot be avoided...*' (R33).

Regulatory compliance is considered by far the most critical factor in the success of SMEs in the UK chemical distribution industry. Owners/managers express very strong views regarding the importance of this factor: '*...simply said...if you want to sell products you have to have it...*' (R80); '*...if your product is not registered or not compliant, you can't sell it...*' (R31); '*...regulatory compliance has to be at the core of your strategy...*' (R4) and its effect on small businesses: '*...regulations and especially REACH will put a lot of strain on our business...*' (R59); '*...REACH affects all aspects or business...*' (R84); '*... (REACH) will definitely strain and drain your resources...*' (R99); '*...it will affect products, planning, financial and human resources...*' (R101). In fact, regulatory requirements and especially REACH

and the biocides directive, are seen to impact upon all the other identified critical success factors such as Market and Product development (MPD), Customer Relations Management, Human Capital, Strategic planning and financial resources. This finding further supports the view that REACH is the most burdensome piece of EU legislation for SMEs (Flavell-While, 2012) and has a significant impact on chemical distributors (ECHA, 2014; Pistolese, 2011).

Many owners/managers (45 in total, 38%) comment that REACH reduces the number of chemical products available to them and effectively restricts the market making it more difficult for smaller companies to compete: *'...we will have less approved products to trade...'* (R90); *'...REACH will dictate our product portfolio'* (R77); *'...we will be limited in our choice of products...'* (R12). As a result, chemical distributors would have to adjust their product offering and re-evaluate the markets they refer to: *'...need to consider whether to stay in a market or pull out...'* (R118); *'...are the potential sales worth the overall cost?'* (R3). Similarly, that affects the supply chain by restricting new suppliers entering the European market or eventually pulling out of Europe altogether due to registration costs. In the views of the respondents (with 40 of them concurring), all the above inevitably creates oligopolistic market conditions in the least and instigates further consolidation amongst distributors as: *'...there won't be enough suppliers left...'* (R80); *'...the suppliers that will be left will control the price...'* (R30); *'...suppliers will need to recover their registration costs one way or another...'* (R103); *'...many SMES will not be able to compete, cope with costs or source products...'* (R92); *'...many small businesses will be forced to exit'....* (R21).

At the same time, many respondents (55 in total, 47%) also report a strain on customer and technical services as increasingly more customers turned for advice on regulatory compliance, request technical data, send questionnaires to complete and *'...expect us to cover all their regulatory requirements...'* (R61). This does only not increase the workload but also the complexity of the business and creates the need for more expertise: *'...we have reached the point where we need external advice...'* (R102); *'...my technical manager is snowed under...'* (R22); *'...I am getting more and more involved into technical requests...'* (R67); *'...costs have increased for the same business...'* (R75); *'...we will have to employ a technical manager now...'* (R63); *'...business requires a deeper understand now...'* (R10). A number of owners/managers (60 in total, 51%) argue that the above mentioned communication is very demanding and time consuming -as previously identified by Pelkmans et al. (2013)- and concur that registering chemicals products under REACH *'...comes at a high cost to a small business...'* (R104).

Respondents (28% of population) highlight that the incurring costs for regulatory compliance are not only direct financial ones but also indirect such as time, expertise required, potential external advice, training etc.: *'...regardless of being direct or indirect, costs will take out a large part of our profits and turnover...'* (R116). They further argue that this inevitably leads to price increases as companies try to recover these costs: *'...there is no option; we can't just absorb the cost; we will have to recover at least some of them...'* (R81); *'larger companies have more resources and can cope better with the upfront cost, we will have to increase prices immediately...'* (R115). This finding further supports business literature on the European chemical industry where regulatory compliance has been established as having a significant cost impact on SMEs (BCG, 2013; Bishop and Walker, 2010; ECHA, 2014; Flavell-While, 2012; Pistolese, 2011). There is also a special mention to the 2018 deadline for registering chemicals for smaller usages as this has a more profound effect on smaller chemical distributors *'...REACH could push you out of business...'* (R56); *'...2018 will have a devastating effect on small businesses...'* (R28); *'...we are bracing for 2018...'* (R86). The majority of owners/managers (56% in total) accept the fact that, inevitably, all chemical distributors including micro and small businesses have to fully implement the measures necessary to comply with regulations otherwise they will not be able to operate in these markets - as already identified by a number of authors (Burns, 2010; Chemagility, 2008; Frost, 2013).

Last but certainly not least, the perceived added value of REACH for SMEs in the UK chemical distribution industry is found to be limited. The majority of respondents (68 in total, 58% of population) consider regulatory compliance a necessity, not a competitive advantage or a means of differentiation and consider the chemical and the chemical distribution market overregulated. In fact, many owners/managers (39 in total, 33%) believe that REACH impedes on SMEs growth and success, leading to a competitive disadvantage for their companies: *'...with so much regulation, you have no time to sell!'* (R53); *'...the cost will become unbearable...'* (R25); *'...simply too much regulation...'* (R13, R96). Respondents also argue that overregulation has a dampening effect on entrepreneurial activity, as in new business venture creation and innovation: *'...it will be difficult to start a new business with such high regulation costs...'* (R72); *'...entrepreneurs will be discouraged by the heavy regulatory burden...'* (R32); *'...many SMEs will be discouraged to enter markets...'* (R102); *'...new projects will have to incorporate the cost of registering now; innovation will decrease...'* (R79).

In the first instance, it seems that there are very few recommendations that this study can offer in the area of regulatory compliance, in light of the fact that it is a fundamental requirement for any company (SME or not) to operate in the chemical and chemical distribution industry. Owners/managers need to accept the fact that if they do not register their products and adhere to environmental and legal regulations, they will not be able to sell their products and will eventually need to exit or be pushed out of the market. The findings of this study strongly support the necessity and inevitability of compliance for operation in this industry and suggest that keeping a low profile or adopting a *'just say yes'* approach is

pointless. On that basis, recommendations are given instead on how to manage and facilitate the compliance process to minimise the impact on SMEs.

## 5.2 Economic Environment

Owners/managers highlight the many aspects of the economic environment and stress its effect on SMEs in the UK chemical distribution industry: '*...the economic environment significantly affects our business; unfortunately it is something you cannot control...*' (R5); '*...chemical production and consumption are tied to the economy...*' (R29). There is an overall agreement (45 respondents, 38%) that the economic environment has a significant impact on small businesses, affecting short and long term planning and thus it need to be taken under careful consideration.

Generally, respondents recognise the fact that chemical consumption is closely related to GDP and economic growth and therefore interest rates, inflation and unemployment affect consumers and investors' confidence (with 40 owners/managers agreeing to the matter). Low confidence means that consumers do not spend and investors are less likely to take risks and invest, both of which has an adverse effect on SMEs: '*...it is simple...if people don't buy consumer products, chemical consumption would drop and we would sell less...*' (R43); '*...investors and private equity funds won't come anywhere near you, if they don't get a quick return on their investment...*' (R107); '*...the buying and borrowing power of smaller businesses is restricted...*' (R36); '*...if the market is doing well, we have better chances to be successful...*' (R8). This further supports contemporary research suggesting that periods of high demand conditions increase the chances for small business to survive and grow (Dobbs and Hamilton, 2007).

Owners/managers (38 in total, 32%) identify access to finance (funding) as the single, most important aspect of the economic environment; a factor that could potentially be very restricting to growth: '*...cash is king...*' (R52); '*...a business needs the financial strength to invest when required and to remain solvent during difficult times...*' (R39); '*...finance is the lifeblood of any business...*' (R29); '*...it is the bedrock of a good business...*' (R88); '*...business without cash is like running an engine on fumes...*' (R110).

Several respondents (28 in total, 24%) further comment that especially during recession periods, the UK banking sector is reluctant to lend money to SMEs because of high risk: '*...small businesses were always considered high risk as they have few assets...*' (R51); '*...banks are not very supportive in times of recession...*' (R62); '*...even companies with good financial ratings find it difficult to secure more funds...*' (R114). With many financial institutions restricting funds and private investors similarly holding back, that eventually hinders economic recovery: '*...as it has happened many times in the past...*' (R51). A good working relationship with the lenders is also considered paramount: '*...need to work closely with your bank...*' (R54); '*...have to keep your investor and lenders happy and informed...*' (R46) as it potentially increases their confidence in your business and '*...help secure financial backing for future opportunities...*' (R117).

A large number of respondents (42 out of the 45 that identified the economic environment as the most important factor, 36% of population) stress out the fact that all businesses, independent of their size and market conditions, need funding at some point in their life whether it is to start up, grow or cope with cash flow shortages. Regarding starting up, owners/managers agree that the vast majority of small businesses in the chemical distribution industry require financing at the start up stage with 35 agreeing on the matter. In the words of R108: '*...unless you are 100% self-financed, which is very rare, how else would you start?*'. Funding also affects the capacity and confidence for future growth, expansion and investment into the business. Respondents express very strong views regarding the effect of available finance on small businesses: '*...it is the fuel to growth...*' (R64); '*...poor cash flow will kill a growing business...*' (R6); '*...if you can't finance your business then it will never take off...*' (R16); '*...funding is required in times of growth...*' (R50); '*...very difficult to be cash rich these days...*' (R18); '*...many companies rely on outside finance to grow...*' (R38).

Similarly, even if a business has sufficient funding, it still needs to be able to deal with and manage unforeseen cash flow shortages. Several respondents (25 in total, 21%) highlight the fact that the chemical and chemical distribution industry is largely handled on credit terms and there is always a discrepancy between the supplier and customer payment terms; for instance, suppliers normally require payment in 30 days while customers normally require 60-90 days. In the words of R98: '*...In the chemical distribution industry, suppliers dictate short payment terms (30 days in Europe, upfront payment for China and the Far east) while customers demand long payment terms; we (distributors) are unfortunately in the mide...*'. Managing payment terms and balancing cash flow under these conditions creates a further need for finance services and flexible borrowing options: '*...need to manage payment terms correctly to survive...*' (R41); '*...make sure you don't run out of cash...*' (R118).

Several owners/managers (22 in total, 19%) also comment on the fact that small businesses need to avoid and manage bad debts as these have a detrimental effect on their growth. During times of recession, an increase in bad debts is not uncommon and thus expected. Respondents recognise that losses due to bad debts put a considerable strain on SMEs and in extreme cases push them into bankruptcy. In fact, many cases of small businesses going out of business following bankruptcy of their largest customer are reported. At this point, there is another distinction between larger and smaller SMEs. Owners/managers are of the opinion that such losses are more easily absorbed by larger SMEs unlike their smaller counterparts where '*...the loss would hurt us a lot*' (R44). On the other hand, smaller SMEs could, at some point,

be self-financed and become less dependent on external finance; for instance working through a bank overdraft: *'...we have been running our business on a bank overdraft with no issues for the last 10 years'* (R27). Larger SMEs find it more difficult to achieve that and hence they have to rely more on external finance, especially in times of growth and expansion: *'...there is no way we could run our business on an overdraft, we would be over it every month!'* (R66).

On a more positive note, several respondents (15 in total, 13%) argue that many opportunities for growth (and start-ups) are found in times of recession and that *'...it is not all doom and gloom...'* (R57); *'...there are always opportunities around...'* (R76). If a small business could *'...identify a niche market or service...'* (R42), *'...offer a unique and competitive product...'* (R87) that could *'...add value and produce a cost saving...'* (R49) then it would be successful. In fact, a number of owners/managers (11 in total, 9%) argue that many SMEs have been successful for that reason; despite the difficult economic environment they are able to offer savings while providing a better service. Recession is considered a good time to offer new, value-adding, cost-saving, innovative products as buyers are more open to products that give their company a competitive advantage. Respondents comment that this is exactly the way they manage to get access to larger organisations where, in times of recession, buyers are interested in discussing about savings and value-adding products: *'...before costs really became an issue, we were not important enough to the large multinationals; now that has changed...'* (R37). Furthermore, some owners/managers (10 in total, 8%) suggest that recession provides good opportunities for acquisitions as cash rich companies have a distinctive advantage over small companies affected by the economic downturn.

## 6. Discussion and Concluding Remarks

This study establishes Regulatory Compliance and the Economic Environment as the most important business environment (external) success factors for SMEs in the UK chemical distribution industry. The above findings are discussed, several conclusions are drawn and a number of recommendations are made.

### 6.1 Regulatory Compliance

Despite the fact that SMEs, unlike their larger counterparts, are considered to be more flexible, adaptable and thus less being able to cope with the business environment more effectively, this study concludes that regulatory compliance cannot be avoided. Inevitably, all SMEs operating in the UK and European chemical distribution industry have to fully implement the measures necessary to comply with regulations otherwise face the real risk of being excluded from the market. A compliance strategy needs to be developed and implemented while a long-term, flexible outlook on regulatory requirements, especially on REACH and competition law, has to be maintained. Keeping a low profile or adopting a *'just say yes'* approach would be meaningless.

Regulations, particularly REACH, impact greatly upon all other business success factors. Owners/managers have to carefully manage their already limited resources and weigh potential benefits against investment. Strict financial control is essential to manage the incurring costs (direct or indirect) to the business. An investment in human resources, so as to achieve the level of expertise and regulatory competence required, is necessary and highly advisable. Utilising external consultants is deemed more appropriate in the initial stages of the registration process - where more expertise is required - but in the long term permanent employees are needed to manage the process. Similarly, SMEs need to develop and adjust their product portfolio based on regulatory requirements while strengthening relationships with existing and new suppliers.

Throughout the compliance process and as part of their strategy, owners/managers are strongly advised to utilise any sources of support available to them, for instance the European Chemicals Agency (ECHA), the European Commission and the Chamber of Commerce among others. In fact, this study raises serious concerns of whether SMEs are able to cope with the regulatory requirements without the support of the government and industry organisations due to a well-established lack of resources. On that basis, the government and relevant associations carry the responsibly and ought to reach out to SMEs to offer more support and access to resources and training in order to support small business activity.

The findings of this research strongly suggest that REACH is becoming overly burdensome, with that having a potential dampening effect on existing small business activity, entrepreneurial (start-up) activity and innovation. In fact, this study has reached the conclusion that the perceived added value of REACH for SMEs in the UK chemical distribution industry is limited and viewed it more as a necessity rather than a competitive advantage or unique selling point for small businesses. This finding directly contradicts the European Chemicals Agency's (ECHA) philosophy that REACH has been adopted not only to protect human health and the environment but also to foster innovation and enhance the competitiveness of the European chemicals industry. This study uncovers a serious divergence between the theoretical (intended by the policy makers) and actual (as viewed by owners/managers) effects this regulation has on small businesses that needs to be addressed immediately to ensure a successful implementation. Unfortunately, the overall stated objective to foster innovation and increase the competitiveness of the European chemical industry has remained rhetoric. Therefore, policy makers need to reinstate the intended benefits and intensify efforts to 'sell the idea' to small businesses. Communication about REACH, especially on its intended goals and benefits (health and environmental)

needs to be improved. Failure to do so would severely affect the competitiveness of the European chemical and chemical distribution industry alongside small business and entrepreneurial activity in this industry.

This study, in line with business literature (BCG, 2013; Chemagility, 2008; Hornke, 2012), concludes that REACH has already impacted negatively on SMEs with this effect expected to intensify in the coming years. In more detail, it is seen as a significant contributing factor in increasing the entry barriers for this market thus impeding entrepreneurial activity and new business venture creation. As per Porter's five forces (in Wetherly and Otter, 2014) the presence of strong regulations, high initial capital requirements, difficult access to distribution, a requirement for economies of scale and a presence of large manufacturers make entry even more difficult. SMEs would struggle in the future to enter the European and consequently the UK chemical distribution industry. REACH has also reduced the number of suppliers and chemical products due to high registration costs and long returns on investments, thus creating oligopolistic market conditions and intensifying the already strong consolidation trends amongst distributors. Increasing regulations have further imposed a significant strain on human resources through an increase in the complexity and workload of the business and the need for more expertise, customer and technical services to satisfy requirements and on financial resources through direct (registration costs) and indirect costs (i.e. time, expertise required, potential external advice, training etc.). This, in turn, has led to price increases as companies eventually try to recover these costs and pass them on to consumers. Last, the heavy regulatory burden and high costs of producing and managing new products, has impacted negatively upon innovation and R&D activity.

## 6.2 Economic Environment

This research concludes that the economic environment has a significant impact on small businesses in the UK chemical distribution industry, affecting short and long term planning and thus it needs to be taken under careful consideration. Even though it can be argued that the economy is beyond the control of any business, SMEs still need to cope and adapt to economic conditions, be flexible in their planning and maintain a proactive outlook allowing for change. Owners/managers and prospective entrepreneurs are urged to consider the economic environment carefully before investing or committing to business ventures in this industry. This study identifies a clear need to engage in financial planning, control and forecasting and incorporate economic conditions and variables into the business strategy. Concurrently, it also reveals a distinct lack of the financial skills and know-how necessary to perform these tasks on behalf of the owners/managers. This gap in skills and knowledge needs to be addressed either through the provision of training or the use of external advice. In other words, chemical distribution SMEs have to invest in internal training courses or external consultancy and further utilise any available support from the government and any industry associations.

Access to finance is identified as the single, most important aspect of the economic environment, as it could potentially be very restricting to SMEs growth. The fact that all small businesses in this industry, independent of their size and market conditions, need funding at some point in their life (whether it was to start up, grow or cope with cash flow shortages) is established. The importance of access to funding becomes paramount when, especially during recession periods, financial institutions are reluctant to lend money to SMEs - because of their high risk and low collateral - and private investors similarly restrict access to funds further affecting small business growth. This research concludes that it is imperative for owners/managers and entrepreneurs to secure multiple sources of finance and fully utilise all available options in the market(s) they operate in. In detail, chemical distribution SMEs are urged to look for more perfect capital markets where more financing channels and better access to capital and credit schemes are available, especially when exporting. Similarly, it is important that owners/managers and prospective entrepreneurs seek markets where government policies (i.e. availability of grants, loan guarantees, subsidised interest rates) and support (i.e. the Chamber of Commerce and UKTI (UK Trade and Investment etc.) are available for small businesses. Of course, once funding is secured, there is a still need to monitor cash flow and liquidity proactively, focus on planning and maintain a close and trustful relationship with investors and lenders.

Regarding sources of finance, the findings suggest that a distinction between SMEs in the specific industry is made based on their size. Smaller SMEs, mainly micro businesses, tend to be more flexible in their finance options and use personal funds, credit cards and loans from family. In fact, they could, at some point and with proper financial planning and control, become self-financed and thus minimally dependent on external finance. On the other hand, their larger counterparts find it extremely difficult to achieve financial independence and have to rely on external finance (financial institutions and private investors), especially in times of growth and expansion.

However, even if a business has sufficient funding, it still needs to be able to deal with and manage unforeseen cash flow shortages. The findings reveal that the chemical and chemical distribution industry is largely handled on credit terms and a discrepancy between the supplier and customer payment terms is not out of the ordinary. Managing payment terms and balancing cash flow under these conditions creates a further need for finance services and flexible borrowing options. Similarly, during times of recession, an increase in bad debts is not uncommon and small business need to be prepared. This research recognises that losses due to bad debts create cash flow shortages, put a considerable strain on SMEs and, in extreme cases, push them into bankruptcy. The latter scenario mostly applies to micro businesses depending heavily

on very few customers. At this point, this study makes a further distinction between smaller and larger chemical distribution SMEs, with the first being more vulnerable and the latter being able to cope with bad debts more efficiently due to their size and funding options. Therefore, cash flow and credit terms management alongside building up a contingency fund for difficult times become crucial.

On a more positive note, this study recognises the fact that many opportunities for growth and business start-ups can be found in times of economic downturn in the UK chemical distribution industry. In fact, recession is considered a good time to offer new, value-adding, cost saving, innovative products as end customers are more open to products that give their company a competitive advantage. Larger distributors tend to offer a package of products which may not necessarily be competitive on all its individual components but offers an ease of handling and managing and is more convenient. However, during recession, buyers tend to be more focused on reducing costs than convenience and thus give the opportunity to smaller businesses, which can only offer a number of products, to quote for the business. Similarly, buyers may be more open to new ideas and products that offer innovation and a differentiation for the competition. At this point, small chemical distributors have the opportunity to adjust their product portfolio, offer a more personal service and exploit their lower overhead costs and margin expectations in order to gain more business.

Last, recession provides good opportunities for acquisitions as cash-rich companies have a distinctive advantage over small companies affected by the unfavourable economic conditions. Small companies experiencing financial difficulties are not uncommon during an economic downturn. These can become lucrative acquisition targets for other small or larger SMEs looking to grow and having the means to pay for it. However, larger SMEs might find themselves in a more advantageous position due to the breadth of finance options they have.

## 7. Implications

This paper addresses a well-established gap in the UK chemical distribution industry and provides a qualitative perspective of the business environment factors critical to the success of small and medium-sized distributors. Based on the findings, there are several implications to various stakeholders in the industry.

SMEs owners/managers can utilise the findings of this study to strategize, run their businesses more efficiently and effectively - by concentrating their efforts and resources to the areas that really make a difference in their business -, plan and prepare for the future - including challenges in their planning process and addressing any issues in the very early stage -, improve their decision-making process and uncover and address training requirements such as strategic and financial planning skills, lack of technical and regulatory expertise, recruitment etc.

The Government, policy makers and financial institutions may utilise the findings of this study to develop and implement policies directed at SMEs in the specific industry; improve and develop the necessary support infrastructure; extend the nature and the range of advice and offer training and education for SME owners, managers and employees.

Non-Government, industry specific organisations such as the European Federation of chemical distributors (FECC), the Chemical Business Association (CBA) and the British Association of Chemical Specialties (BACS), also benefit from this research as it increases their understanding of the industry, especially from a small business perspective. It also provides the knowledge for these associations to approach and recruit new members, especially SMEs that have always been difficult to approach or the ones that did not see a value in joining before.

Last, chemical manufacturers and suppliers are able to get a deeper, more complete understanding of the market and SMEs operating in it. Therefore, they would be in a position to evaluate, formulate and implement their distribution channel strategy in a more efficient and effective way.

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