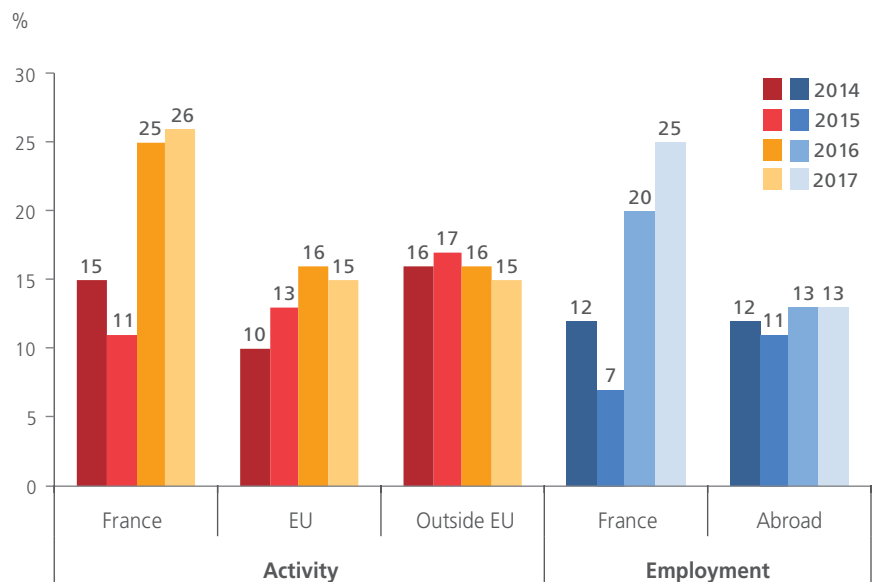


Outlook for France's intermediate-sized enterprises hits a five-year high in 2017

The business outlook for France's intermediate-sized enterprises (ETIs) has continued to improve in 2017. For the second year running, ETIs are more optimistic regarding sales growth in France than sales growth abroad. On the whole, they reported better results in 2016 and greater expectations for 2017 than the previous year, in terms of business activity, employment, order books, investment, and cash position. The 2016 indicators for industrial ETIs seem to show an upswing, after a mixed performance in 2015. The only area remaining negative is export sales, but forecasts are encouraging for 2017. To fund investments, ETIs are increasingly replacing internally generated funds by bank credit, but lending growth is expected to slow in 2017. The overwhelming majority of ETIs report continued easy access to lending, even if one-fourth regard collateral requirements as a significant barrier to borrowing from banks.

Chart 1: Change in balance of opinion on expected activity and employment, by location



Sources: 2014-2017 DGE-Bpifrance ETI surveys.

The survey was conducted early in 2017 by the Direction Générale des Entreprises (Directorate General for Enterprises: DGE) and Bpifrance (Box 1). It found that the business outlook for ETIs had reached a five-year high, with 50% of ETIs expecting sales growth in 2017 and 11% expecting a decline. These figures yield a balance of opinion on expectations of +39 points, up 4 points from 2016, when the balance posted a 7 points improvement on 2015. Expectations, however, are less optimistic than in 2011, when the balance was 10 points higher.

Business outlook has continued to improve in 2017

The balance of opinion on expected business activity for 2017 increased for ETIs with more than 500 employees (+50 after +47 in 2016) and for those with fewer than 500 employees (+27 following +25 in 2016). But the balance was unchanged for ETIs with fewer than 250 employees (+18 in 2017, or the same as

in 2016 and 2015). The least internationalized ETIs stand out in terms of the improvement in their opinion on expected business activity (+5 points from 2016 to 2017) –in contrast to the most internationalized ETIs¹ (-1 point)– even if the balance of opinion on the level of activity remains lower for companies with a low international presence (+37 versus +49). The balance of opinion on expected activity improved strongly among service-sector ETIs (+54 points after +44 in 2016); the service sector is thus the most optimistic category of ETIs for 2017.

ETI remain optimistic about business activity in France in 2017

For the second year in a row, ETIs are more optimistic about sales growth in France than sales growth abroad (Chart 1): the balance

¹ i.e. firms in which one-fourth of employees are located outside France.

of opinion on expected activity in France in 2017 comes to +26 (versus +25 in 2016), compared with only +15 for sales growth abroad (as against +16 in 2016). ETIs in industry are far more optimistic regarding the trend in their activity abroad, particularly outside the European Union (+32 outside the EU, +24 in the EU, and +18 in France), unlike ETIs in commerce and services.

The outlook for business abroad by the most internationalized ETIs has fallen since 2016 (balance of opinion of +37 for 2017 versus +50 in 2016 with the EU, and +43 versus +55 outside the EU), although it remains higher than for the other ETIs.

In 2017, 16% of ETIs plan to create subsidiaries or acquire stakes abroad, versus 15% in 2016. Planned expansion in other EU countries is higher (9% versus 7% in 2016), but still below the level of 2015 (10%).

Outlook for hiring continues to improve in France, and has stabilized abroad

The balance of opinion on ETI hiring expectations in France rose from +20 in 2016 to +25 for 2017. The upswing is especially strong in industry (+23 for 2017 after +8 for 2016), and in companies with more than 500 employees (+31 after +20). Smaller ETIs (under 500 employees), on the other hand, are somewhat less optimistic for 2017 (+18 after +20).

Prospects for hiring abroad have stabilized at +13. They have fallen for the most internationalized (+39 after +47), innovative ETIs² (+19 after +23), and ETIs in industry, but have risen for ETIs with more than 500 employees, ETIs with a low degree of internationalization, and low-innovation ETIs.

Uptrend in orders in 2016 expected to continue in 2017

After declining in 2015, ETI order books were replenished in 2016: 20% of ETIs consider they were high versus 11% reporting they were low (14% versus 18% in 2015). A slightly higher proportion of the least internationalized ETIs consider their order books were high in 2016 than the most internationalized ETIs (21% versus 19%). Similarly, the proportion of ETIs with more than 500 employees reporting high order books was greater than those with fewer than 500 employees (23% versus 17%), but ETIs with fewer than 250 employees report a level close to that of ETIs with more than 500 employees (22%). In terms of sectors, ETIs in services reported an improvement in their situation, which was already favorable in 2015, while the balance of opinion of ETIs in industry returned to positive ground, as 23% reported high order books in 2016 versus 12% who reported low order books (compared with 16% and 21% in 2015). Commerce-sector firms again had a negative balance of opinion.

This general upswing should continue in 2017 because the balance of opinion on expected orders stands at +21, up from +14 for 2016. ETIs with more than 500 employees (+29), industrial ETIs (+28), ETIs with the greatest international presence (+28), and the most innovative ETIs (+28) are particularly optimistic. The only ETIs with a negative balance are those with fewer than 250 employees (-1).

² A business is considered «innovative» if it has taken at least one of the following five steps during the previous 3 years: (a) funded research and development expenditure (in-house or externally) or recruited R&D personnel; (b) acquired an operating license for a process or technology; (c) filed a patent, trademark, design or utility model; (d) developed a new or significantly improved product or process (service provision) on behalf of a third party; (e) marketed a new product, asset or service (other than simply reselling new products bought from other companies and excluding aesthetic changes or changes to the packaging of products already in existence), or has used a new production, marketing or organizational process (or method). Furthermore, no similar product or process should already have been marketed or used by competitors.

Table 1: Percentage of ETIs citing major barriers to growth in 2017 (followed by 2016 figure)

%

	All ETIs	Industry, construction	Commerce, transportation, tourism	Services
Lower margins	51 (53)	53 (54)	50 (53)	48 (53)
Lack of equity capital	16 (14)	10 (14)	17 (14)	22 (13)
Excessive debt	13 (12)	12 (15)	13 (14)	14 (6)
Tighter credit terms	14 (13)	15 (15)	14 (11)	13 (13)

Sources: 2016 and 2017 DGE-Bpifrance ETI surveys.

ETI export performance in 2016 again below expectations

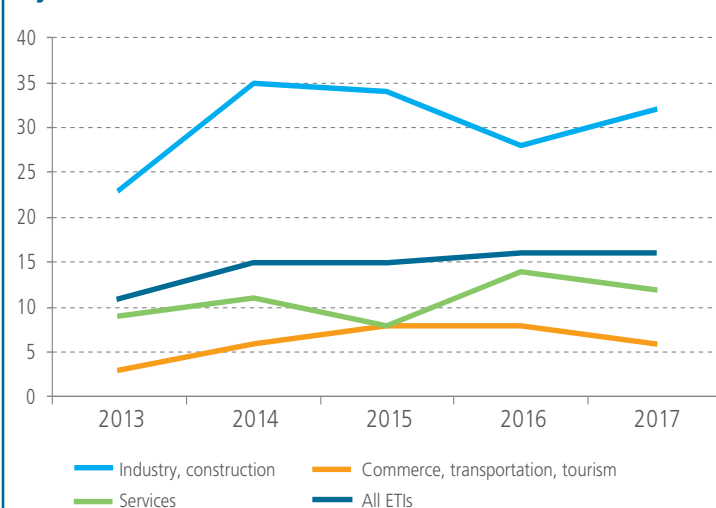
Actual export performance by ETIs in 2016, however, was negative, as only 12% reported higher-than-expected exports in 2016 versus 22% reporting the opposite (compared with 16% and 23% respectively in 2015). Only service-sector ETIs appear to be satisfied with their international activity: 18% stating that they exceeded their export objectives, whereas only 15% regarded their 2016 exports as below their objectives.

The balance of opinion on expected exports in 2017 is the same as in 2016, with a 16-point difference between the percentage of ETIs expecting higher exports in 2017 and the percentage expecting lower exports (Chart 2). The most optimistic ETIs are those with the greatest international presence (+43), followed by industrial ETIs (+32), innovative ETIs (+27), and ETIs with more than 500 employees (+20). The only categories with a low balance of expectations are low-innovation ETIs and commerce-sector ETIs (+1 and +6 respectively).

The opinion of ETIs regarding the reduction of margins as a barrier to growth continues to improve

Fifty-one percent of ETIs viewed the reduction in margins as a major or insurmountable barrier to growth in 2016, down from 53% a year before (Table 1). The decrease was sharpest for the least innovative ETIs (from 53% to 46%), ETIs with under 500 employees, and service-sector ETIs (from 53% to 48%). ETI in construction remain the most sensitive to the reduction in margins, although the proportion regarding this as a major or insurmountable barrier has fallen (from 68% to 64%).

Chart 2: Change in balance of opinion on expected exports, by business sector



Sources: 2013-2017 DGE-Bpifrance ETI surveys.

The 2016 investment upswing confirmed in 2017

The balance of opinion between ETI managers reporting higher internal-growth investment during the year (tangible and intangible investment) and those reporting a fall widened from +22 in 2015 to +32 in 2016. The increase occurred in all categories except service-sector ETIs, where the balance narrowed slightly after a major increase in 2015 (+33 after +34). The service sector, however, remains one of the ETI categories with the highest balance of opinion on the investment trend, alongside ETIs with more than 500 employees (+34), innovative ETIs (+33), and industrial ETIs (+31).

The 2017 outlook for internal-growth investment is unchanged from 2016 (Chart 3). The categories with the highest intention to invest in 2017 are ETIs with more than 500 employees, innovative ETIs, internationalized ETIs, and service-sector ETIs (balance of +28 for each of these categories).

Upbeat forecasts for external-growth investments in 2017

Concerning external-growth investments, intentions to acquire equity stakes or set up subsidiaries are higher in 2017 than in 2016: 41% of ETI managers plan to acquire an interest in another company and 28% plan to create a subsidiary in 2017, versus 36% and 24% respectively a year before. The increase is pronounced for industrial ETIs (up from 32% to 43% for acquiring an equity stake, and from 25% to 32% for creating a subsidiary).

Funding by debt and bank financing stabilized in 2016

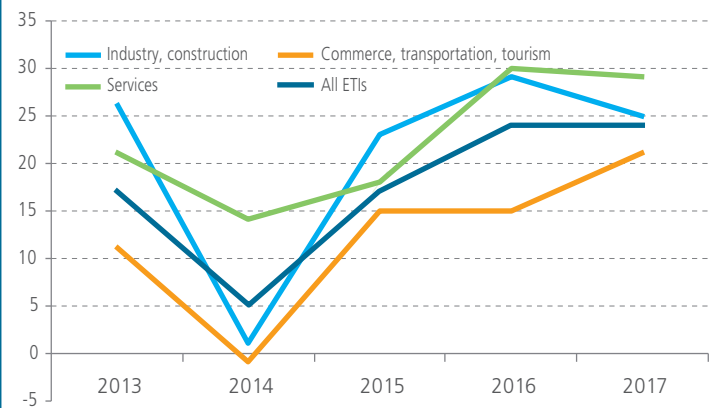
Debt and bank financing as a percentage of financing for internal- and external-growth investment remained stable between 2015 and 2016, as ETIs used credit to fund half the amount of their investments. ETIs in the commerce, transportation, and tourism sectors, as well as ETIs with low international presence, made the greatest use of this method of financing. Equity injections continue to account for a very modest –albeit increasing– portion (3% versus 2% in 2015). The share of self-financing continued to fall in 2016, when 44% of ETI investment was self-financed, down from 48% in 2015 and 53% in 2014. But self-financing is still the leading source of funding for ETIs with fewer than 250 employees (59%), the most internationalized ETIs (57%), and service-sector ETIs (50%).

Use of self-financing expected to fall again in 2017

In 2017, the balance of opinion on expected investment funding indicates that the trend of greater reliance on credit and a fall in self-financing should continue, albeit to a lesser degree than in previous years (-6 for self-financing versus -10 in 2016 and -11 in 2015; +11 for bank loans after +14 in 2016 and 2015). The decline in self-financing should be greatest for those ETIs that continue to fund the largest share of their investments this way (balance of -12 for service-sector ETIs and -11 for ETIs with fewer than 250 employees). Unsurprisingly, these are the categories of ETIs with the greatest intention to use bank financing (balance of +21 for ETIs with fewer than 250 employees, and +17 for service-sector ETIs). The need for equity capital should again decline in 2017 (balance of -1) except for ETIs with fewer than 250 employees (+5).

This slower growth in the use of credit occurs in a context where one in seven ETIs views tighter access to credit as a major or an insurmountable barrier, and where one in eight ETIs reports that it is being restricted by excessive debt. These proportions are roughly the same as a year before. The percentage of ETI that consider the lack of equity capital to be a barrier to borrowing rose from 14% to 16%.

Chart 3: Change in balance of opinion on expected tangible and intangible investment, by business sector



Sources: 2013-2017 DGE-Bpifrance ETI surveys.

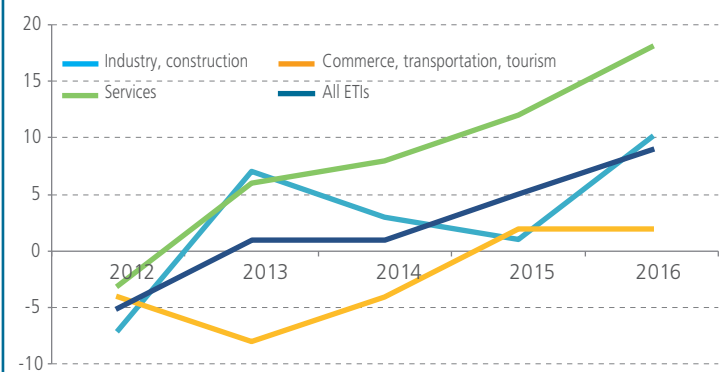
Eight out of ten ETIs report no difficulty in access to lending

In 2016, eight out of ten ETIs report they had no major difficulty in accessing credit for general business requirements or for investment. However, they identified factors that limit their recourse to bank financing. Collateral remains the main barrier, representing an important or insurmountable constraint on short-term and long-term loans for 18% and 24% of ETIs respectively. Despite continuing low interest rates, the level of rates is seen as a major or insurmountable barrier to borrowing for general business purposes by 6% of ETIs, and a barrier to credit for investment by 8% (up from 2% in 2015).

Cash positions expected to keep improving in 2017

The positive trend in the balance of opinion of ETIs concerning their cash position first recorded in 2015 persisted in 2016 (Chart 4). This is the case for a large majority of ETIs. The steepest increases were for ETIs with a strong international presence (up from +2 to +18), and industrial ETIs (up from +3 to +10). As in 2015, the smallest ETIs (fewer than 250 employees) reported better cash positions in 2016 than ETIs with more than 500 employees (+18 versus +10). On the other hand, they do not expect their cash positions to improve in 2017, unlike ETIs with more than 500 employees (+2 versus +14). The other categories of ETIs with high values for the balance of opinion on expected cash positions are those with a strong international presence (up from +7 in 2015 to +23 in 2016), and innovative firms (up from +3 to +13 respectively).

Chart 4: Change in balance of opinion on cash position, by business sector



Sources: 2013-2017 DGE-Bpifrance ETI surveys.

Box 1: Source, methodology, and definitions

Business climate survey of ETIs

This study sets out the results of the business climate survey conducted in March and April 2017 by the Directorate-General for Enterprises (Direction Générale des Entreprises: DGE) and Bpifrance of French «national» intermediate-sized enterprises (Entreprises de Taille Intermédiaire: ETIs), i.e., those intermediate-sized enterprises whose parent company is located in France. A total 670 questionnaires were received, of which 518 were analyzed after eliminating those that were either incomplete or outside the scope of ETIs. The sample was adjusted by post-stratification on the basis of three criteria: size, business sector, and region. The analysis examined the consolidated accounts, if any—or, failing that, company data for the respondent firm.

Intermediate-sized enterprises (ETIs)

The category of intermediate-sized enterprises was introduced into French law by the Economic Modernization Act of August 2008. These are firms that are not included in the category of small and medium-sized enterprises

(SMEs; in French, petites et moyennes entreprises or PME, i.e., firms with fewer than 250 employees and annual sales not exceeding €50 million or total assets not exceeding €43 million), but with:

- fewer than 5,000 employees;
- annual sales not exceeding €1.5 billion or total assets not exceeding €2 billion.

They accordingly rank between SMEs and large enterprises.

Balance of opinion

Balance-of-opinion indicators are standard in business climate surveys to track sentiment regarding key parameters for companies, including economic and labor factors (such as activity, employment, exports, and investment) and financial factors (such as cash position and access to lending). They express the difference between the percentages of opposing opinions:

- Trend indicators = $[(\% \text{ «up»}) - (\% \text{ «down»})] \times 100$

- Level indicators = $[(\% \text{ «good/easy»}) - (\% \text{ «bad/difficult»})] \times 100$

Box 2: “Patrimonial” ETIs are less optimistic regarding the trend in their activity in 2017

- Who owns a company’s capital can have an impact on the company’s plans and operations. The high proportion of “patrimonial” firms (entreprises patrimoniales) –and, more specifically, family firms– among French national ETIs warrants an investigation of their growth and trajectories relative to other ETIs. Patrimonial firms are defined as firms whose capital is majority-held by one or more natural persons identified by name. If there are family ties among the majority owners of a patrimonial firm, it is designated as a «family firm.» For the purposes of this study, a patrimonial firm owned by a single person is considered to be a family firm.
- In 2016, 64% of French national ETIs were classified as patrimonial ETIs, and 45% were classified as family ETIs.
- Patrimonial ETIs are more likely to have affiliates abroad, as 34% have foreign subsidiaries compared with 27% for non-patrimonial ETIs. But non-patrimonial ETIs have a greater percentage of employees abroad (21% versus 17%) and generate a larger share of annual sales abroad (16% versus 15%). Nineteen percent of direct and indirect employees of family ETIs are located abroad, compared with 11% for patrimonial non-family ETIs.
- Non-patrimonial ETIs are more optimistic than patrimonial ETIs regarding the trend in their activity in 2017 (balance of +41 versus +38). Family ETIs are slightly more optimistic than non-family ETIs (+40 versus +36). The balance of opinion among family ETIs on the trend in their activity abroad in 2017, expressing the difference between those expecting positive growth and those expecting negative growth, is +16 in the EU and +18 outside the EU, versus +14 and +11 respectively for patrimonial non-family ETIs, and +17 and +12 for non-patrimonial ETIs. Regarding the trend in activity in France, the balance of opinion of patrimonial non-family ETIs is +36, compared with +24 for family ETIs and non-patrimonial ETIs. For hiring in 2017, patrimonial non-family ETIs are the most likely to hire in France and abroad, whereas non-patrimonial ETIs are the least likely to hire.
- For 2017, a greater proportion of patrimonial ETIs plan internal-growth investments than the other ETIs (+28 versus +18). They also tend to focus more on external-growth operations, as 46% envisage equity investments compared with 32% for non-patrimonial ETIs, and 30% (compared with 24%) plan to create new subsidiaries.
- Patrimonial ETIs have a greater tendency to fund their investments with bank financing; this method was used by 59% of family ETIs in 2016, 49% of other patrimonial ETIs, and only 39% of non-patrimonial ETIs. The use of bank financing should increase further in 2017: 28% of patrimonial non-family ETIs plan to make greater use of bank financing, as do 25% of family ETIs and 18% of non-patrimonial ETIs. Regarding barriers to growth, patrimonial non-family ETIs have the greatest tendency to cite narrower margins (57%), lack of equity capital (20%), and tightening credit terms (18%). Family ETIs have the greatest tendency to cite excessive debt (15%).

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Find out more:

See «La conjoncture des ETI: enquête annuelle 2017» (in French), Bpifrance, June 2017. This publication provides a detailed analysis of the survey conducted jointly by DGE and Bpifrance.

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