

The Policy Environment for the Development of SMEs



Pacific Economic Cooperation Council
Chinese Taipei Pacific Economic Cooperation Committee

Preface

Over the past decade, small and medium enterprises (SMEs) have attracted considerable attention for their wide-ranging contributions to the economy. At the same time, the world has witnessed a significant change in the global business climate. The world wide trend of globalization creates new challenges to policy makers. What is the appropriate SME policy that promotes economic development the best? Will the usual practice of SME policy work in the knowledge base surroundings? What kind of policy transformation needed in the new environment? And, will SME sector develop to fulfill our expectations?

In response to the growing awareness of the importance of SMEs and SME policies, the CTPECC proposed a task force under PECC international project, "The Policy Environment for the Development of SMEs" to gather information on SMEs, highlight obstacles to SMEs development in Asia-Pacific economies and feasible solutions and sound policies to help interested economies promote SMEs.

The present report is the final product of the PECC project, and the report committee has invited a number of experts to contribute to the PECC project. The report consists of several policy papers, and the focus is on SME development across industries of specific economies.

The report begins with an Australian perspective of SME policy development, with a focus on global scale (Chapter 1), contributed by Professor Patrice Braun. In Chapter 2, Professor Andrina Lever discussed the current challenges and opportunities of Canadian SMEs. Professors Luis Riveros and Mario Morales listed the disappointment and challenges of Chilean SME policies in Chapter 3. Institutions and policies backdrop of SMEs in Colombia were discussed by Professors Angelica Acosta and Catalina Rojas

in Chapter 4. In Chapter 5, Professors Teruhiko Yoshimura and Rika Kato highlighted the policy environment for promoting SMEs in Japan. Professor Joo-Young Kim displayed and analyzed Korean SMEs innovation policies in Chapter 6. Professors Coral Ingle and Claire Massey discussed the New Zealand policy environment for the development of SMEs in Chapter 7. Professor Tan Wee Liang described SME development in Singapore with a focus on entrepreneurial infrastructure in Chapter 8. In Chapter 9, Professor Wen-Heng Chao analyzed the changing face of Chinese Taipei's SME sector. In Chapter 10, Professors Sam Do and Thach Pham outlined the policies on developing SMEs in Vietnam. Finally, an executive summary that reviews, analyzes, and draws inferences of the contributing studies, written by Professor Ming-Wen Hu, constitutes the last portion of this report.

A handwritten signature in black ink, reading "David S. Hong". The signature is fluid and cursive, with the first name "David" and last name "Hong" clearly legible, and "S." as a middle initial.

Dr. David HONG
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The Policy Environment for the Development of SMEs

SME Policy Development in a Global Economy

An Australian Perspective

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Introduction

Small and medium enterprises (SMEs) have long been recognised as important to the economy in terms of their considerable contribution to GDP and employment creation and, as such, have been a priority agenda item for APEC since the 1993 Leaders' meeting in Seattle (Hall, 1995). During the last decade, the rise of information and communication technologies (ICT) and the related rise of service sector industries have significantly altered the course of industry and SME policy from a protectionist approach to a culture favourable to entrepreneurship. In particular, policy makers have been looking at what actions should be taken to encourage entrepreneurship and innovation by SMEs in an increasingly connected and global business environment (Audretsch and Thurik, 2001).

This paper commences with a summary of SME initiatives currently in place in Australia, highlighting programs, issues and barriers pertaining to the development of SMEs. It then explores public-private partnership options to assist SME promotion and growth. The paper concludes with policy implications and suggestions towards the sharing of best practice for SME development in the Asia-Pacific region.

Australian SMEs

The SME business sector in Australia accounts for 95 per cent of all business and employs 3.3 million Australians, or 47 per cent of the non-agricultural private sector workforce, in industries across all parts of the Australian economy. At the last census in 2002, there were approximately 1.2 million small businesses in Australia, accounting for around 15 per cent of gross domestic product (GDP). The Australian Bureau of Statistics (ABS) defines small businesses as firms with fewer than 20 employees; medium businesses employ 20 to 199 people (ABS, 2002).

The small business sector is very diverse, with a high representation in the property, business services, construction and retail trade sectors. Around 67 per cent of all small businesses are home-based (ABS, 2005). Australian SMEs are becoming increasingly export focused; approximately 41 per cent of all goods exporters are small businesses (ABS, 2004). The 2006 Sensis Business Index shows that SMEs believe the economy to be strong and future economic expectations remain positive.

The World Bank report *Doing Business in 2006* describes Australia as a country that is easy to do business in and is friendly to small business. The ease of doing business refers to governments creating a regulatory environment that is conducive to the operation of business (World Bank, 2006). A new business in Australia can typically be established in less than two days, with just two steps compared with an OECD average of six steps and 25 days. Some 110,000 new SMEs were started in the last 10 years (ABS, 2006), which is not to imply they all survived and thrived. In a comparison of entrepreneurial activity across 30 countries, Australia's small businesses ranked as the eighth most entrepreneurial. Australia's high self-employment and entrepreneurship rates are attributed to the large percentage of immigrants who enter Australia and start a business (Hindle & Rushworth, 2003).

Australian SME Policy

The Australian Government recognises that the economic health of Australia

depends, in large part, on the growth generated by those entrepreneurial Australians who operate their own small businesses. Small business is generally regarded as having the dynamic entrepreneurial culture that leads to innovation and employment growth. Small businesses are also seen as organisationally more flexible and therefore more able to provide rapid response to changing customer demands (OECD, 2001). While there is evidence of constant turbulence in the SME sector, with firms downsizing, new firms being formed, and existing firms expanding, these dynamic entrepreneurial processes, once perceived as a negative influence, are now seen as critical to innovation and growth (Stevenson & Lundstrom, 2001).

In 2004, the Australian Government released its *Committed to Small Business* statement, bringing together a range of initiatives aimed specifically at enhancing the operating environment for small business (Commonwealth of Australia, 2004). Underpinning the Government's encouragement of entrepreneurship and innovation is a program of legislative reform and funding to drive continuous improvement in the workplace, flexibility in the labour market, skills development, and reduction in taxation, regulation and compliance cost for business. The 2006 Federal Budget delivered \$435 million in business tax cuts over four years through a range of measures aimed at reducing the complexities of doing business for SMEs. Cuts to business taxes are designed to reduce business costs, relieve the burden of red tape, and assist business to sustain high rates of productivity (Commonwealth of Australia, 2006). On the other side of the financial coin, new measures have been put in place to increase the supply of venture capital to start-up companies and small enterprises seeking capital injections. Recent studies have shown the important role new high growth firms can play in job creation and economic development (Yencken et al, 2006), so SMEs with a technology focus and high growth potential are especially targeted as the key beneficiaries from increased access to capital.

While SME initiatives are developed across more than one agency, AusIndustry (www.ausindustry.gov.au), which is part of the Department of Industry, Tourism and Resources (DITR), is the main industry support agency. AusIndustry's goals as the central point for business assistance and information are to support R&D, commercialisation and innovation. Under the theme *Grow Your Small Business*, AusIndustry provides a range of products

designed to assist small business to become innovative and internationally competitive (<http://www.ausindustry.gov.au/index.cfm>). Initiatives cover a variety of SME development and growth stages, examples of which are discussed below.

The *Innovation Investment Fund* is a venture capital scheme first introduced by DITR in 1998. Through this program, the government co-invests in early-stage equity companies together with private venture capital funds. The aim of the scheme is to encourage research and development (R & D) and growth of new Australian technology-based firms through the supply of venture capital. Approximately 75 firms have received funding through the program. The program is currently being evaluated, but can generally be considered successful in terms adequate return on investment for all parties concerned. While the program was designed to supply venture capital to early-stage firms, due to investor risk aversion in practice most participating firms have been in later stages of development. For the continuation of the program, a successor scheme (the Pre-Seed Fund) has been redesigned to support earlier stage development to a greater degree (Yencken et al, 2006).

As part of *Backing Australia's Ability* (<http://backingaus.innovation.gov.au>), an initiative that supports research, innovation and skills development, the *Commercialising Emerging Technologies* (COMET) program was introduced in November 1999 to aid the commercialisation of innovation products, processes and services. COMET targets all industry sectors and provides support to early-growth stage companies, spin-off companies and individuals in the areas of commercialisation and business development activities. The program has been shown to increase the motivation of participating firms and COMET has been extended until June 2011, with a further \$100 million in funding (Autio et al, 2007).

The *Commercial Ready Program*, introduced in 2004, provides competitive merit-based grants to SMEs for commercialisation activities, for R&D with high commercial potential, and for proof-of-concept activities. The program supports both R & D in new ventures as well as applied research leading to new innovations by established SMEs. The aims of the program are to support Australian businesses in the technology sector to develop innovative products, processes and to encourage collaboration between industry and research

institutions. Grants require matching contributions by receiving firms which limits the program to firms that already have significant financial resources. In 2005-06, 600 firms were supported through the program, which is considered particularly useful to SMEs in the expansion stage, e.g. to assist in the funding of product customisation activities for new markets. The fund contributes to an increased growth motivation for established SMEs by facilitating the continued development of new products and product lines (Yencken et al, 2006).

Foreign owned businesses in Australia contribute a disproportionate share of R &D and innovation and until very recently businesses which held their intellectual property overseas did not qualify for R & D tax concessions. With the aim to make Australia a more attractive place for innovation, from July 2007 onwards SMEs and large firms which boost their long-term investment in Australian innovation will be rewarded with a subsidy on additional R & D conducted in Australia (Commonwealth, 2007).

With the main role for small business considered to be job creation and making a contribution to (regional) economic development, continuity of business experience and enterprise, as well as entrepreneurial capacity building are actively encouraged through business development programs. The *Small Business Entrepreneurship Program* and the *Building Entrepreneurship in Small Business* support a new culture of entrepreneurship by providing grants focusing on the ongoing improvement of Australia's small business operating skills with grants being made available for incubation, training and mentoring and succession planning. Funding themes within these programs include women entrepreneurs, young entrepreneurs and the development of skills in the use of information and communication technologies (ICT) to conduct electronic business transactions with clients and suppliers.

The drive for improved efficiency and a reduction in the cost of doing business is also being actively pursued through information technology tools such as the *Business Cost Calculator* and the *VANguard initiatives*. Both are designed to reduce the cost of compliance for business in terms of time and money. The Calculator can be used to estimate/calculate an approximation of regulation costs and their impact on small business. The Calculator can also be

used to compare the compliance cost based on location or industry and identify strategies to reduce the compliance burden. In keeping with the theme to simplify compliance for small business, the *VANguard initiative* takes a whole-of-government approach to electronic validation, authentication and reduction of red tape to complete transactions with government agencies (Commonwealth of Australia, 2006).

In addition to the aforementioned technology developments, a *New to Business* initiative for aspiring entrepreneurs has been rolled out. A web-based checklist delivered through www.business.gov.au, provides entrepreneurs with a one-stop-shop start-up resource, combining information from all three tiers of government relevant to starting a business. Small business is further assisted by being exempted from unfair dismissal laws allowing for more flexibility in its workforce, business investment and growth. New export opportunities for small business are also being created through the negotiation of foreign trade agreements aimed at reducing transaction costs involved in cross border trading.

To help SMEs start and run a successful business, SMEs also have access to state-level support in the State or Territory they reside. Programs and resources vary from state to state and range from finance to support for the development of a business plan, to training and assistance to attend overseas trade fairs. The State of Victoria's *Building Innovative Businesses Program*, for example, provides participating SMEs with intensive management assistance, internationally focused market support and access to private sector equity (Yencken et al, 2006).

SME Development Issues

Australia has a wide-ranging set of SME initiatives in place, with a number of them enjoying iterative lifecycles as a result of the same political party having been in office for more than a decade. While Australia may have a comprehensive set of SME policies related to the resources and support SMEs need in different phases of development, a number of SME development issues remain. As Yencken et al (2006) observe, Australia may have a

reasonable record in public funding of research and development, but policy makers still tend to view innovation as a pipeline. When funding is provided for product research and SME development on one end of the pipe, new technologies, commercial applications, SME growth and job creation are expected flow out on the other end. Policy measures have a limited lifecycle and are adjusted continually to address perceived gaps, but anticipated outcomes of many of the SME policies may well be too high (Autio et al, 2007).

Current Australia's SME policies have an emphasis on new technology and a focus on businesses with a strong potential for high growth. There are a number of phases of business that need to be negotiated between opportunity, start-up and expansion that lead to successful high-growth. These steps are arguably the most difficult for any firm and are strongly influenced by the capability, behaviour and motivation of the entrepreneur in terms of translating technology-driven business ideas into reality in the marketplace. Yet, these situational conditions tend to fall outside the scope of entrepreneurship support policies (Autio et al, 2007).

While the contribution to job creation by high-growth SMEs is extremely important, in reality only a small percentage of entrepreneurial ventures achieve rapid growth and contribute to high quality innovation and job growth. As a recent article on the employment opportunities presented by SMEs in Australia suggests, the country should not solely rely on SMEs to create job opportunities since the majority of them are not interested in hiring people (Schaper, 2006).

Another development issue pertains to the fact that SMEs are a heterogeneous group. The contemporary make-up of small business shows that over 30 per cent are operated by 'baby boomers' who may be exiting their business over the next decade and less than 10 per cent are run by those under 30 years (Commonwealth of Australia, 2006). SMEs also operate in different industry and local contexts. As such, there is little benefit in treating SMEs as a homogeneous group without regard to gender, education and demographic make-up, the industry sector they operate in, or the local context within which they are embedded. Location is considered an important context for entrepreneurship, but all locations do not equally contribute to

entrepreneurship. The ability of entrepreneurs to induce entrepreneurial activities in their region also depends on their education, experiences, skills and motivations (Kotey, 2006). Deregulatory measures designed to cut red tape and support SMEs in a generic fashion may result in the creation of a low quality and low wage employment environment for SMEs with little future (Parker, 2000). Van Stel and Storey (2004) caution against policies that promote short-term self-employment by individuals with low levels of human capital and subsidising of less efficient firms to prevent them from leaving the market when competition intensifies.

That is not to say that SME capacity building, especially on the micro firm level, is not required. As a 2003 Senate Report on *Small Business Employment* by the Employment, Workplace Relations and Education References Committee observed, "despite being highly skilled and capable in many areas, many proprietors lack the business management skills they need to compete effectively in today's more competitive, deregulated environment. The lack of these skills is a major cause of under-performance, business failure and untapped potential in the small business sector" (Commonwealth of Australia, 2003, pp.xix-xx). This is not a new finding, nor one confined to Australia. Over the past 25 years the need to improve the business management skills of small business owners has consistently been identified in small business studies and reports undertaken by Australia, APEC and the OECD. Australian government officials at all levels have, to varying degrees, acknowledged the needs of small business and rolled out small business development initiatives. Worthwhile as many of these programs may have been, "most initiatives fall short of providing the level, quality and type of business development support that would allow small business to reach its full potential" (Commonwealth of Australia, 2003).

Barriers to small business capacity building are in part related to the Australian culture which attaches a high value to self-reliance, resulting in atomistic behaviour by Australian SMEs and a pervasive culture of 'going it alone' (Braun, 2004). As a result, many SMEs lack awareness and understanding of the benefits of training, resulting in widespread indifference to training. Since SMEs are often time- and resource-poor, the cost of training, including time loss from the job, is frequently seen as a disincentive. Training provision is often not sufficiently flexible, while the diversity of small

business and the preferences of owner/managers make even the best of training programs a difficult undertaking (Kearns, 2002).

These barriers extend to the area of information and communication technology (ICT) adoption by small business, an essential tool for any small business wishing to participate in today's global business environment. Many Australian SMEs have yet to comprehend the value of integrating ICT into their business processes, lacking the strategic e-business planning, skills and knowledge required to operate in the digital economy (Braun & Van Beveren, 2005; Braun, 2004). Government interventions designed to overcome ICT adoption barriers have not markedly increased the uptake of e-business by Australian SMEs (Braun & Harman, 2004), with women-led SMEs trailing their male counterparts in the integration of e-business practices (Sensis, 2006). SMEs that continue to remain unskilled and unintegrated in the digital economy may eventually experience a reduction of market opportunities.

Other issues that impact on Australian SMEs operating in a global business environment relate to compliance with international tax laws, rules and regulations relating to cross-border trading, e-business, e-payment, intellectual property rights (IPR) and international financial reporting standards (IFRS). Results of a survey indicate that most SMEs are not ready for international financial standards such as IFRS (Heathcote, 2005) and cross border trading. The latter is based on cooperation by regulatory authorities across jurisdictions and a clear delineation of authority and responsibility. Such delineation is typically not yet present and SMEs hence need help with the rapidly changing international regulatory environment. The Australian Government has established eight so-called Export Hubs in key locations that offer local businesses a one-stop shop for trade and industry assistance. However, governmental export agencies whose mission it is to increase Australia's export volume, particularly those of SMEs, appear to fall short in serving a valuable purpose, with only 45 per cent of SME exporters seeking any advice or assistance when they start exporting (Kerin, 2006).

Aforementioned issues highlight the challenges of designing and implementing effective public policy to support Australian SMEs, particularly in areas where the prevalent SME culture tends to favour a *laissez-faire* approach. One area where Australia has been making significant progress is in

the public-private partnership arena. The aforementioned *Innovation Investment Fund* is one example of a successful public-private partnership program.

Public-Private Partnerships

With the rise of the knowledge economy, public-private partnership (PPP) models have moved well beyond shared investment in key public infrastructure towards a framework for innovation through knowledge sharing. The importance of knowledge sharing is reflected in the 2006 adoption of the Hanoi Declaration on Strengthening SME Competitiveness for Trade and Investment, in which Ministers agreed to become proactive in sharing experiences, research and best practice in the areas of SME competitiveness for trade and investment (APEC, 2006).

The development of joint initiatives between the public and private sectors for SME development is of considerable interest to Australia as SMEs play a strategic role in fostering the Australian innovation process and are a significant source of national wealth creation. Building partnerships, skills and infrastructure that enable SMEs to experience the full benefits of R & D and produce commercially viable outcomes that attract global interest are seen as necessary to compete in the global business environment. The sourcing and supporting of entrepreneurship and innovation through public-private partnerships also reflects the policy shift from a protectionist approach to a culture favourable to entrepreneurship. As such, deregulation measures, venture capital, encouraging R & D and new firm start-ups are all designed to enable SME creation and commercialisation of knowledge (Stevenson & Lundstrom, 2001). As Audretsch and Thurik (2001, p.32) point out "entrepreneurship generates growth because it serves as a vehicle for innovation and change, and therefore as a conduit for knowledge spillovers".

Australia's *Cooperative Research Centres* (CRC) Program was established in 1990 to improve the effectiveness of Australia's research and development efforts. CRCs are funded for seven years and promote long-term strategic links and collaboration between industry, universities and government

research institutions. CRCs link researchers with industry to focus R & D efforts on progress towards utilisation and commercialisation. The close interaction between researchers and the users of the research is a key feature of the program. Another feature is the industry contribution to CRC education programs to produce industry-ready graduates (Yencken et al, 2006). At present the CRC Program has a network of 56 active CRCs, mostly made up of small companies formed through a collaboration of businesses and universities, but can also include government agencies and other research organisations. Each CRC falls into one of six broadly defined sectors: environment, agriculture, information and communication technology, mining, medical science and technology and manufacturing. Some six hundred SMEs currently are or have been involved with CRCs and the return and impact of the work by CRCs on the Australian economy is estimated at A\$2.7 billion (Innovation Australia, 2007). The CRC Program has become a global role model for collaboration between business, academia and government, aiming to turn scientific innovations into successful new products and services.

In addition to supporting R & D through partnerships, market-based approaches that have a focus on creating a market environment conducive to SME development are also actively pursued. For example, to maximise opportunities for Victorian SMEs, the *Victorian Industry Participation Policy* (www.diird.vic.gov.au/VIPP) seeks to increase opportunities for participation by SMEs in major government procurement contracts, projects and infrastructure. The program aims to boost SME employment and business growth and to expose SMEs to new technologies, new processes and best practice. One of the primary issues to heed in rolling out market-based programs is the difference in capacity between public and SME partners, whereby capacity building of SMEs needs to be ongoing and responsive to the growth and inevitable changes SMEs face by participating in these types of partnerships.

Public-private dialogue and partnerships promote better diagnosis of the investment climate and related policy design; make policy easier to implement; create more transparency; and promote trust. While PPPs assist in creating an enabling environment for SME development, they should not be considered a panacea. There will be instances where PPPs may be ineffective, especially when the interests of SMEs are being under-represented in the

partnership. Dialogue to develop specific goals, strategies, and priorities for the partnership will lessen these problems. Considering implementation of PPP initiatives in phases - a discovery phase, a high impact phase, and a sustainability/transfer phase - can also be a useful strategy (Herzberg & Wright, 2006).

Enabling Environment for SME Development

International experience has shown that subsidies alone have limited effectiveness in promoting SME development and a clear understanding of the role of government in creating enabling environments for SME development is essential. Typically, the role of government has been to get the enabling environment right for business by removing obstacles to private sector activity - including those resulting from inappropriate legislation, institutional deficiencies and market failures. Increasingly important components to consider within the enabling environment are the local context and asset base, including access to infrastructure and institutional support; industry structures and networks; research and training.

ICT and the digital economy have created a level playing field and policy initiatives would do well to move away from creating generic enabling environments without regard to gender, demographic make-up, firm size (micro versus SME), the industry sector SMEs operate in, and the local context within which they are embedded. For example, women are increasingly important in terms of their contribution to GDP (Braun, 2007; Daly, 2007). However, women-led SMEs face different obstacles from men, such as access to finance and juggling family care and business when venturing into business (Centre for Women's Business Research, 2003). SME strategies should hence take into account the full range of factors that influence the creation of new firms and the growth of existing firms and include not only the regulatory apparatus, but also the legal system and the taxation system. SMEs will benefit most from policy that is integrated and coordinated, in the sense that SME development programs are considered within the overall policy environment and are complementary across agencies. In addition, promoting transparency and SME awareness of laws, rules and

regulations, especially in rapidly changing areas such as e-business, cross-border trading and intellectual property rights, will assist SMEs to act local but think global.

Perhaps the most important step governments can take in getting the enabling environment right is to embrace a public-private partnership approach for policy innovation. The advent of ICT provides policy makers with a useful platform for sustained dialogue on the local level. An inclusive approach to policy creation will lead to informed policy initiatives that are tailored to SME needs. A shared approach also promotes trust, which in turn will assist in the identification of industry opportunities and increased uptake of development programs by SMEs.

Knowledge Sharing across APEC Economies

This paper has highlighted policies, programs, issues and barriers surrounding the development of SMEs in Australia. It discussed Australia's public-private partnership approaches to assist SME promotion and growth. The paper has also explored the role of government in creating enabling environments for SME development.

Australia is not alone in its quest to enhance SME performance and find solutions that will boost SME growth and innovation. With each economy now globally engaged and the integration between economies increasing daily, it is imperative to build knowledge sharing partnerships both within and across our borders, especially in the areas of SME research, technology and product innovation. Recognising that both the business climate and enabling environment impact on SME development and growth, it is also vital to share the processes and observations of particular policy reforms that have led to an improved business climate. The sharing of policy design, implementation, monitoring and evaluation processes will assist in building an evidence-based regional charter for good practice in SME development.

There is no doubt that the sharing of knowledge across economies will contribute to increased understanding of how to best support entrepreneurship,

SMEs and related economic development in the Asia-Pacific region. ICT-based technologies and the Internet can effectively assist economies to collaborate and share their research, knowledge, technology and policy experiences. Much like generic SME policy, generic knowledge sharing would be ineffective in terms of creating good practice for SME development across the region. Research and knowledge sharing require a best practice framework and infrastructure accessible to all those generating and sharing the knowledge base. This would enable targeted and equitable content contribution and distribution. It would also be conducive to the formation of communities of practice in special interest areas such as R & D, innovation, specific industry sectors or regional areas and other social, cultural, political and economic dimensions that influence entrepreneurship and SME development. Encouraging dialogue across interests would promote a culture of cross-fertilisation and transparency. In time, such a knowledge base could become a valuable resource for collaboration and an effective tool to generate policy guidelines towards best practice in SME development across the Asia-Pacific region.

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SME Development and Policy in Canada

A Review of Challenges and Opportunities for Small Business 2007

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Introduction

This paper shall present an overview of sme's and current sme policies in Canada, provide details on some interesting issues that are of concern to Canada, highlight specific challenges for Canadian sme's, explore the potential for public-private cooperation, and offer recommendations for opportunities for small business development moving forward.

Overview of Canada's Small and Medium Sized Business Sector²

- Small business establishments represent 97% of all Canadian businesses (based on 2.4 million businesses)
 - o The majority of those businesses has no payroll employees and is typically unincorporated (56.2%)
 - o 24.8% have fewer than five employees
 - o 16.7% have between five and 49 employees

- o 2.2% have between 50 and 499 employees
- o 0.1% have more than 500 employees
- The SME sector is Canada's major employer with 56% working for an employer with less than 500 workers. (based on 13.3 million employees)
- Among all businesses eligible for the Scientific Research and Experimental Development tax credit, enterprises with fewer than 500 employees invest more in R & D as a percentage of their revenue.
- The majority of Canadian businesses that export are small: companies with up to 100 employees represent 85% of total exporters; businesses with fewer than 50 employees make up 72% of all exporting Canadian businesses and are responsible for close to a quarter of the total value of exports.
- Over 40% of Canadians indicate that starting a company or being self employed would be their most rewarding career path.
- The number of self employed Canadians increased 30% from 1990 to 2004 and even when there was a dip in growth it remains the prevailing growth force in the Canadian labour market.
- Close to 55% of entrepreneurs chose being self-employed for reasons such as having independence and being able to balance work and family.

Clearly these statistics from the Canadian Federation of Independent Business show an overwhelming tendency towards small business development and growth in Canada and thus it is vital for the government to create an environment which encourages, enhances and allows small business to thrive and become the most competitive in the world.

Current SME Development Policies in Canada

Perhaps a unique characteristic of sme policy in Canada is that it is not necessarily completely developed by one Federal department but rather it is segmented and being developed at several levels: federal (primarily through Industry Canada but other Federal government departments develop policy which can have a significant effect on small business development); regional (such as programs funded through Industry Canada but for implementation in a specific region of Canada); provincial; by sector and with respect to specific groups of peoples, i.e., Aboriginal peoples, women, youth and those with disabilities.

Industry Canada is the primary Federal government department set up to oversee policy development for Canadian industry in general and sme's but also includes technology, tourism, statistics Canada, and a variety of regional programs. "The department's mission is to work with Canadians to build a growing competitive, knowledge-based economy. Industry Canada hopes to improve conditions for investment, enhance Canada's innovation performance, help make Canada the most connected nation in the world, increase Canada's share of global trade, and build a fair, efficient and competitive marketplace."³ Through Strategis, the official portal for Industry Canada, the department provides business and consumer information to all Canadians without the constraints of time and geography. The site has allowed Industry Canada to shift from a paper-based information culture to a more efficient electronic one. Before Strategis, the department produced over 5,000 information products on paper. In addition to providing information to all who can access Strategis, the site makes use of new technologies to offer interactive applications such as customizable benchmarking tools, cost calculators, and online business planning. Many of Industry Canada's services (such as filing an application for patent or incorporating a company) can now be completed online.⁴

Policy has been developed over the years with different initiatives being announced by successive governments with an emphasis for 'Government online' to urge sme's and all businesses to access all government information and filings online and thus making a commitment to use technology even in micro businesses through websites such as Strategis.⁵

The last overall federal government policy statement that was issued in 1994 stated the government would:

- ensure that the business environment is conducive to SME growth (i.e. ensure that the tax system does not inhibit growth and job creation, reduce regulatory burden, deliver services effectively and efficiently;
- target limited government resources to promote competitiveness and growth (i.e. fewer subsidies, more strategic information and advice).

Since then, much of the sme development and assistance policy has been developed with specific agendas in mind or by specific departments. For example, Heritage Canada has specific programs in place to assist arts, culture and the protection of Canadian content in broadcasting that often assists small businesses in Canada which are involved in arts, productions, publishing, exporting and protecting intellectual property and preserving Canadian identity.

The Department of Foreign Affairs and International Trade has internal departments which develop policy to assist Canadian small businesses within organizations such as the OECD and APEC and holds the mandate for the Canadian Trade Commissioner Service which promotes Canadian businesses overseas through the trade commissioner services, sector specialists and electronically through the virtual trade commissioner.

Recently Indian and Northern Affairs Canada has absorbed the Aboriginal Business Canada program from Industry Canada and is responsible for small business development policy and programs with specific reference to Aboriginal and native peoples in Canada. In addition, there are regional programs funded through Industry Canada but with a specific emphasis on western Canada (the Western Enterprise Development Initiative) or Atlantic Canada (Atlantic Canada Opportunities Agency) which were originally created to equalize opportunities for businesses across Canada and specifically in regions with high unemployment or cyclical economies.

In addition to Federal level policy, Canada is composed of 10 provinces and three territories and each has developed their own sme policies, regulations

and economic development departments within their own jurisdiction. Opportunities and challenges for business can vary dramatically for a variety of reasons, but essentially Canada is geographically one of the largest countries in the world, with a relatively small population (approx. 31 million people) with most people concentrated within easy travel to the United States. This leaves vast areas of Canada sparsely populated with economic and small business challenges of their own. Governments and provinces vie for business across the Canada.

Focus of small business policy

Recently in Canada, there has been a surge of interest in 'getting regulation' right with several initiatives being announced. As has been cited by the World Bank review on business climates⁶, and recently at the APEC 'Private Sector Development' symposiums, actually incorporating and starting a business in Canada is a relatively easy, fast and inexpensive procedure and Canada ranks as number two in the world for this and overall among the top five (at number 4) countries in the world for ease of doing business in general. Where Canada's rating does drop dramatically is in the area of regulations and licensing. With so many jurisdictions in Canada, licensing and mutual recognition of qualifications becomes a bureaucratic nightmare. In addition, the Federal government continues to try to drive forward with its Paperwork Burden Reduction Initiative, simplifying taxation for small business and financing.

Budget 2007

Many of the federal government policies of Canada are revealed when the Minister of Finance releases the current federal government budget. This year this was released on March 30, 2007 and it reveals what the current priorities are as well as includes overall comments as to the current health and focus of the Canadian economy.⁷ Many of these will affect the emphasis on business. The key messages and themes for this year included:

- Canada today is strong and has a plan for a better tomorrow
- Budget 2007 will achieve this (the plan for tomorrow) by:
 - o Taking historic action to restore the fiscal imbalance and investing in things that are important to Canadian such as a modern health care system, the environment and infrastructure such as roads, bridges and public transport
 - o Delivering on Advantage Canada,⁸ the government's long-term economic plan for Canada
 - o Further reducing the tax burden in Canada to make things easier for working families with initiatives such as the tax back guarantee and working families tax plan
 - o Cracking down on corporate tax avoiders
 - o Investing in social priorities
 - o Implementing tax benefits for sme's such as
 - ◆ Increasing lifetime capital gains exemptions
 - ◆ Allowing capital investment write-off in machinery and equipment purchased between March 19, 2007 and 2009 using a special 50 % straight line rate
 - ◆ Increasing the capital cost allowance for buildings used in manufacturing and processing and also for computers
 - ◆ Eliminating interest deductibility for foreign active business income
 - ◆ Updating the Canada-US Tax treaty to facilitate cross-border investment and commerce
 - ◆ **Reducing the federal paper burden on small business by 20% by**

November 2008

- ◆ **Reducing the tax compliance burden on small business by decreasing the frequency of their tax remittance and filing requirements**
- ◆ Providing incentives for provinces to eliminate provincial capital taxes which will provide benefits to business
- ◆ Incentives to harmonize provincial and federal GST taxes
- ◆ Strengthening capital markets and creating a single capital market regulator
- ◆ Reviewing Canadian Competition policy⁹
- ◆ Investigating elimination of barriers to trade, investment and labour mobility between provinces
- ◆ Launching the Global Commerce Strategy¹⁰
- ◆ strengthening the regulatory system
- ◆ spending on infrastructure

Issues of concern to Canada

Three areas that have been of concern to small business in Canada and the government in general are in the areas of **taxation**, **the paper burden** and the always contentious area of **access to finance**.

Taxation continues to present a major concern to small business in Canada, particularly when put into the context of being competitive with Canada's largest trading partner, the United States. If Canadian small businesses are to be truly competitive with their neighbours to the south, then they must have

competitive support and taxation policies. "Taxation is the most fundamental way in which small business interacts with the government. Governments must reform their tax systems to facilitate the creation of wealth by small business."¹¹ **Taxes that are not based on profits represent approximately 70 percent of all direct taxes paid by corporations. (Department of Finance).** Because Canada's tax system includes federal, provincial and municipal jurisdictions, the Canadian tax system imposes a disproportionate burden on small businesses. This burden has impaired the competitiveness of sme's and their ability to create wealth and jobs. On its Strategis website, Industry Canada lists the **first principles of small business taxation** as:

- tax systems at all levels must support the creation and growth of viable small businesses
- tax measures should not result in disincentives to hire
- Canada's tax systems must reduce their dependence on all forms of profit-insensitive taxes
- Tax systems must be simplified to reduce the compliance costs borne by small business and free up productive capacity
- Tax systems must encourage the retention of profits to finance the internal growth of small businesses
- The federal, provincial and municipal governments must coordinate and simplify their tax systems to ensure that the total tax burden on small businesses is fair and reasonable
- Potential reductions in tax returns must be balanced by reductions in government spending¹²

The government of Canada's own department responsible for small business policy recommends that the federal government must reduce the burden of profit-insensitive taxes (such as payroll taxes, unemployment insurance, etc.) on small businesses by lowering premiums on unemployment insurance and the Canada Pension Plan. Small businesses in Canada also have concerns

about the complexity of tax administration and compliance at both the federal and provincial levels and recognize that this places an unnecessary burden on SMEs because of their size and lack of internal expertise. Concerns include: harmonization, coordination and simplification, penalties and dispute handling, clarity and consistency and services to taxpayers.

The second area of concern is that of the **paper burden** to small business. The government of Canada has been working with key stakeholders such as the CFIB, Chambers of Commerce, and Conference Board of Canada to **reduce the paper burden** and hence reduce the costs of regulatory compliance costs. "Paperwork" or "red tape" consists of the time and resources spent by business owners, managers, staff or hired experts to understand and comply with government rules and regulations relating to operating a business. From the firm's perspective, complying with regulation includes planning, collecting, processing and reporting of information, completing forms and retaining data required by governments. The "burden" represents the administrative costs incurred above and beyond the normal day-to-day costs associated with running a business.

This initiative has a focus on small business as articulated on their website because:

"Small businesses make an important contribution to the Canadian economy. Small businesses - establishments with fewer than 100 employees - accounted for 99 percent of all registered businesses in Canada, according to Statistics Canada's *Business Register*, as at June 2003. Nearly 60 percent of employers - about half of all Canadian firms - had fewer than five employees.

Doing business in Canada means that a business must deal with the cumulative requirements imposed by three government jurisdictions - federal, provincial/territorial and municipal. Research suggests that complying with regulatory requirements results in a disproportionate cost on small businesses compared with larger firms. Results of an Organisation for Economic Co-operation and Development (OECD) study of 11 countries - *'Businesses' Views on Red Tape: Administrative and Regulatory*

Burdens on Small and Medium-sized Enterprises' - indicated that paperwork burden per employee in the smallest companies was found to be more than five times higher than for larger firms, with small firms in the service sector facing the greatest burden. Micro-businesses - establishments with fewer than five employees - face particular challenges relating to economies of scale."¹³

Small businesses recognize that regulation can provide a stable and predictable business environment. However, they also believe that the burden of compliance at times outweighs the benefits of regulation. Excessive compliance costs can be a determining factor in a small business remaining viable and productive, or in investment capital leaving Canada for a more streamlined business and regulatory environment elsewhere.

This has been an ongoing initiative of the government which recognizes the undue burden that this places on small business.¹⁴ Statistics Canada undertakes a triennial survey focusing on small business and the challenges they face in complying with information obligations stemming from government regulations. The Paperwork Burden Reduction Initiative (PBRI) involves measuring the costs and impact of regulatory compliance on small business and pursuing opportunities to reduce, rationalize and simplify regulatory requirements across federal departments and agencies. It was launched in February 2005 in response to the Government of Canada's 2004 Budget commitment to create a working group of government officials and small business representatives to measure the impact of regulatory compliance on businesses and to make measurable reductions in paperwork burden.

The PBRI has three key components:

- An Advisory Committee on Paperwork Burden Reduction (ACPBR)
- The Survey of Regulatory Compliance Costs
- Annual progress reports to the Minister of Industry

The Paperwork Burden Reduction Initiative builds on the recommendations of the External Advisory Committee on Smart Regulation (EACSR) presented in

Smart Regulation: A Regulatory Strategy for Canada, released in September 2004. Specifically, the EACSR advocated that further work be done on issues relating to compliance and enforcement, including harnessing the potential of e-government as a vehicle for single-window access to government regulatory programs.

The PBRI contributes to the Government of Canada's Smart Regulations Strategy as it:

- Addresses the regulatory burden imposed by federal departments and agencies;
- Encourages better coordination across federal government to reduce regulatory burden and manage unintended duplication of regulatory requirements;
- Examines the cumulative impact of regulations; and
- Establishes baseline data on the cost of compliance facing small businesses.¹⁵

The paperwork burden associated with government regulation and reporting requirements has historically been a top priority concern for owners of small and medium-sized enterprises (Sme's) in Canada. The Canadian Federation of Independent Business (CFIB) has undertaken a comprehensive survey to quantify the cost of regulation and paperwork burden on business, identify the most burdensome reporting requirements from all levels of government, address the opportunity costs of complying with excessive paperwork, and seek SME input into finding meaningful ways of reducing regulatory and paperwork burden. The CFIB has released a report on its findings, entitled *Rated R: Prosperity Restricted by Red Tape*.¹⁶

The third area of continual interest to Canadian small businesses is **access to finance, both debt and equity**. With this in mind, the Business Development Bank of Canada (BDC) is a crown corporation mandated by the Minister of Industry Canada to be a 'complimentary lender' and to provide funding to small businesses that are unable to secure funding from traditional sources.

Far from being a lender of 'last resort', BDC has emerged as a 'partner' with small business and has been the source of many innovative programs developed to specifically address the financing needs for Canadian small businesses. The bank works closely through its network of consultants to identify that the growth needs of the business are met in the most advantageous ways.

BDC offers a range of products and services including financial services, consulting services, subordinated finance and venture capital. BDC provides services across Canada in both official languages through its 94 branches. In addition, the Bank maintains a user-friendly, interactive website at www.bdc.ca which supplies continuously updated information and links to information for and about small business. The Bank has also established a virtual branch online at www.connex.bdc.ca where clients can apply for further financing as well as maintain up to the moment information on their account.

In addition to term loans, BDC has created three special financing programs focused on sme's: co-vision to support start-ups and small businesses under \$150,000; productivity plus which supports the productivity improvements in sme's; and innovation which provides working capital solutions to support growth projects for sme's. The BDC also has a popular consulting service which provides expert advice at a reasonable rate on the four core topics of: transition, business planning and management, operational efficiency and innovation.

In addition to providing financial services and consulting, BDC is also a provider of subordinated financing and venture capital. BDC Venture Capital has been involved in venture capital since 1975 and has to date invested in more than 400 companies involved in the areas of life sciences, telecommunications, information technology and advance technologies. In addition, the Bank set aside a special \$25 million fund to specifically invest in women controlled companies and that money was fully invested within 18 months, proving that there is a demand for venture capital for women controlled businesses and that women's businesses do indeed qualify for venture capital.

Challenges Specific to Canadian SME's

In addition to the three ongoing challenges for sme's listed above, Canadian sme's may face some other challenges that are unique to Canada and Canadian culture. These challenges face sme's in the manufacturing sector, young entrepreneurs, women entrepreneurs and new Canadians. All face challenges but at the same time offer incredible opportunities to Canada.

Manufacturing Sector

Canada's manufacturing sector has been badly hit in recent years by the combination of competition from lower labour costs in other parts of the world as well as a shortage of skilled labour in Canada and the higher value of the Canadian dollar. In a report to the Standing Committee on Industry, Science and Technology¹⁷, the Canadian Federation of Independent Business provided a good overview of the state of manufacturing in Canada as well as what the future may hold. A higher percentage of companies in the manufacturing sector predict that they shall need to increase both their full time and part time employees in the 12 months following the report. 62% of the respondents in their survey indicated that the higher Canadian dollar is hurting their business. The major business factors which are affecting their businesses include: energy prices, other input prices, rising insurance premiums and interest rates with labour availability, competition and market wages also causing concerns.

A significant percentage of the businesses surveyed (with the exception of those in the service sectors) indicated that if fuel prices stayed at high levels or increased, either their businesses would not survive or they would have to make significant changes in investment, employment or prices to cope. Consistent with the previous section of this paper, small business priorities overwhelmingly focused on their total tax burden and government regulations and paper burden. Another area of real concern is a shortage of labour (this is discussed later in this paper). With respect to the sme productivity priorities, the following were of the greatest concern: reducing taxes, easing burdensome regulations, and making government fees and penalties more equitable. As a

recommendation to government, the report finally recommended what would help businesses comply better with regulations and they cited the following:

- Simplify existing regulations
- Reduce the total number of regulations
- Make owners aware of new regulations
- Improve government customer service

Young Entrepreneurs

An area for great growth and opportunity lies with young entrepreneurs. Canada is a young country with an ambitious well-educated population from diverse backgrounds. Toronto, alone, is considered one of the most multi-ethnic cities in the world. In the next few years, many of these young people will enter into business rather than into the traditional job market. No exact figures exist on the number of potential young entrepreneurs but in a recent internal study conducted by the Canadian Youth Business Foundation (CYBF) it was noted that there are approximately 7.5 million youth between the ages of 18 and 34, 8% of the total adult population are engaged in entrepreneurial activities and 20% of youth would consider starting their own business. This represents a huge potential in economic contribution by youth.¹⁸ However, oddly enough, no organization offers a comprehensive picture of the future for youth entrepreneurship and there are no real national programs that exist to support young entrepreneurs. There are some programs such as Junior Achievement, ACE and Shad but all are underfunded. CYBF provides mentoring and startup loans up to the amount of \$15,000 but due to their own funding challenges can only reach a very small percentage of this potentially huge and prosperous market. It is obvious that more work needs to be done to nurture and support young people to pursue their entrepreneurial dreams and also make an economic contribution to the country while also creating jobs.

While substantial funding has been provided for these youth entrepreneurship development programs much more needs to be done to instill in today's youth a culture of entrepreneurship, a 'can-do' and 'can succeed' attitude that can allow Canada to successfully move ahead - it is by nurturing today's youth and allowing them to pursue their dreams that the economic future of country shall be secure. This culture needs to begin at the primary and secondary school levels where business skills need to be taught along side other basic skills. While Canada is a country rich in natural resources it must continue to mentor and grow other business sectors, particularly in the knowledge and technology sectors where so many young people are thriving today. Investing in young entrepreneurs is not just about allowing a young person to pursue his or her dream, but it is also about the economic future and advantages of the country. Too many policy advisors are too narrowly focused or do not have the long term vision required to develop and implement policy that will enhance the future entrepreneurs and small businesses.

Women Entrepreneurs

'Forget China, India and the internet: economic growth is driven by women.'¹⁹ '...there is a business case for expanding women's economic opportunities: it is smart economics.'²⁰ 'Womenomics: les femmes font rouler l'economie du Quebec.'²¹ Women entrepreneurs and women-owned businesses have been on the rise since the 1970's with the demographics today being very different from the 1950's and 1960's when many women stayed at home or worked part time. Women entering the workforce and also starting businesses has had a most dramatic effect on the economy of Canada, but it is still difficult to attract the attention of policy makers that due to the dual role that women must play (i.e. mothers, homemakers and now senior caregivers, as well as competitive business owners) that there need to be good policies (such as day care, retirement benefits, financing opportunities) in place to ensure that women are able to take advantage of their best business opportunities. Women are playing an increasingly important role in the economic growth of Canada and globally. Women owned businesses are the fastest growing sector in Canada and 40% of these businesses alone are based in the province of Ontario.²² Even with those figures, Ontario is third after British Columbia and

Alberta - an odd discrepancy given that Ontario is the powerhouse behind the Canadian economy.

In November, 2002, former Prime Minister of Canada, the Right Honourable Jean Chretien, announced Canada's Innovation Agenda which included creating the first ever Parliamentary Task Force on Women Entrepreneurs. In launching the task force, Prime Minister Chretien declared that 'our success depends on our ability to marshal the skills and ingenuity of all of our people. As an important source of talent and creativity, women entrepreneurs have much to contribute. However...women entrepreneurs face unique challenges, particularly in accessing capital and expertise required to grow new businesses.'²³ Under the Chairmanship of the Honourable Sarmite Bulte, P.C., the task force traveled across the country and held town hall meetings, consultations and online discussions with over two thousand women entrepreneurs, followed by government officials at all levels of government. The result was a report with specific recommendations and a clear vision and path for going forward that was presented to the Prime Minister in November 2003.

Recommendations were categorized under the following sections:

1. coordinating support for women entrepreneurs
2. advocacy: a voice for women entrepreneurs
3. access to capital
4. access to employment benefits and social safety net programs
5. access to mentoring programs and networking opportunities
6. access to business skills training
7. access to information - 'one-stop shopping': a hub for women entrepreneurs
8. access to government procurement

9. focusing on the service sector
10. promoting Canadian women entrepreneurs nationally and internationally
11. encouraging and training women entrepreneurs to be export ready
12. lack of research

Prime Minister Chretien accepted the report and immediately announced 10 initiatives. However, shortly thereafter there was a change in government and many of the other recommendations were never implemented. **The true value of this report though, lies in the blue print that it set out to support and develop women's businesses in Canada and that while it focused on women, the report laid out a blue print, that if followed, could promote the development of all small businesses across the country.**

Other emerging issues that may be unique to Canada

Four other issues are emerging that could present problems to Canada if they are ignored or could create real opportunities for Canada if savvy government policies are put in place now. One of the major concerns of business today and this affects SME's more, due to their vulnerability in economic and demographic changes is a **lack of people in the workforce and lack of talent**. Canada's immigration process has slowed down considerably with the average wait time to immigrate to Canada taking at least two years if not longer. If special work issues are involved or people are willing to go where there is a shortage of labour, this application time may be fast tracked but time is of the essence for small businesses. This is creating a situation where some small businesses in Canada are opening warehouses and offices in the U.S. where labour may or may not be cheaper but at least is accessible - this is particularly true with new complications in getting goods and people across what used to be the most open border in the world: that between the U.S. and Canada. Immigration and border transit has been changed dramatically since the events of 9/11.

A shortage of labour is now of major concern across Canada and in areas such as the oil patch and the four provinces of western Canada, more than 60% of small business cites this as a major concern.²⁴ Long term vacancy rates have sky rocketed between 2004 and 2005.

The flip side to the labour shortage is the opportunities that **immigrants and 'new Canadians'** are bringing to Canada. According to Statistics Canada, immigrants will account for all net growth in the labour market in coming years.²⁵ The opportunities for young immigrant entrepreneurs track this growth as well. These immigrants are being concentrated in a handful of urban centres and most growth will come from the Chinese, Spanish and Punjabi communities. With good policy development this could create a wellspring of sme's for Canada.

Another area of concern is the **aging baby boomers** and the number of entrepreneurs that are planning to exit their businesses within the next 10 years. The CFIB²⁶ puts this figure at more than 70% of the businesses it surveyed. The ramifications of this are so serious that BDC has now put into place a new program to assist in transition. Other major banks are also beginning to look at this market. Not only will these business people be leaving the workforce, it could have a dramatic effect on loss of jobs or on balance sheets if employees try to raise financing to purchase an otherwise debt-free company. In addition, new businesses (hence the vital contribution of youth, women and new Canadians) need to be encouraged to replace those exiting. Another reason for forward thinking and good policy that needs to be in place in anticipation of this happening. The flip side of this conundrum is that according to the Canadian Imperial Bank of Commerce (CIBC), the fastest growing portion of the new entrepreneurial landscape in Canada are so-called '**seniorpreneurs**' or those Canadians over the age of 55 who, for a number of reasons now make up one in four self-employed individuals in Canada and a large portion of that are women. The majority of these older entrepreneurs are termed as 'lifestylers' and do not have growth or longevity plans for their businesses.

Finally, another unique characteristic of Canada is the **remote communities**. Canada is a vast land mass with a relatively small population as mentioned earlier. This means that there are many small communities struggling to

survive in remote areas where even the weather can be isolating. Regional economic development programs must be maintained in order for these communities to survive.

Public – private cooperation

Private-public cooperation is actively encouraged in Canada and indeed some of the most rewarding outcomes are as a result of private-public cooperation. Canada has a tradition of holding public consultations on issues regarding new public policy. In addition, most of the government departments have private sector consulting or advisory boards which assist the government in developing policy. The Minister Responsible for International Trade appoints an SME Advisory Board which meets twice a year with the Minister and conducts work intersessionally on issues of importance that will assist Canadian sme's to be more active in exporting. It is also an opportunity for business to inform the government first hand as to the greatest challenges that they face. Most recently the Advisory Board was able to advise the Minister of Canada's new Global Commerce Strategy to enhance the competitiveness of Canadian business internationally.

Task forces such as those on young entrepreneurs, women entrepreneurs, paper burden reduction, sectoral advisory groups, the Vancouver Olympics and all regional development programs have private sector advisors. Recommendations have also been made to create better and more transparent government procurement procedures so that small business can have better access to government contracts for supplies and services - a critical area for small business since the government is the single largest purchaser of goods and services in Canada. Most recently, Accenture has released a report with guidelines on 'Keys to Successful Public Sector Shared Services Implementations: Focus on Governance' to address these opportunities.

Recommendations going forward

Canada is a country with great potential which needs to take a 'holistic approach' to its new, young, aging and diverse population. Traditionally Canada has been a resource based economy but it needs to have a long term vision for encouraging the growth of sme's in a variety of sectors including technology and the myriad of opportunities which exist in the service sector - the fastest growing sector in the world. Some of the most successful economies are those which have no resources and therefore have to rely on developing the talent of their people. Canada should be looking at this as well.

Canada would be wise to create a small business agency to coordinate all policy impacting on sme's and to be an advocate within the government for sme's. Rather than adding another layer of government and reporting, this agency would be seen as the hub for all sme issues. In conjunction to this, it would be most advantageous to create a high level advisory council reporting directly to the Prime Minister on the advancement of sme's.

Programmes need to be supported which encourage more young people to become entrepreneurs. The government must address the differential impact of taxation and paper burden on sme's in general but on women in particular. A national day care policy needs to be implemented which allows women to either have access to cost effective day care, or allows women to deduct the cost of child care and elder care as a business expense in order to allow women to spend time creating jobs for others in their role as entrepreneurs. Programmes which encourage seniorpreneurs to continue to add to economic development need to be implemented so that all members of society continue to make productive contributions and are not deemed to be 'users' of the system. The different levels of income need to be taken into account so that women and young entrepreneurs can set aside a larger portion of their income for retirement. Due to its geographic makeup, with remote communities and communities that may be isolated due to adverse or severe weather at times of the year, Canada is an ideal environment to develop and promote technology to provide more markets for the service sector.

Governments do recognize the importance of supporting sme's in general. However, small business is risky and governments are not in the risk business, and not all sme's are created equally therefore policy cannot be one size fits all. The challenge is to develop an environment which supports small business and creativity; one that looks to the future and has a vision of where the opportunities lie and puts into place a plan that will achieve that vision. Too often, policy is dictated by politics and is short sighted with lessons learned too late.

Resources

- Business Development Bank of Canada (BDC) (www.bdc.ca) assists small businesses both by providing loans and equity financing to small business and by providing management services such as advice on how to operate a successful small business. The online branch can be located at www.connex.bdc.ca.
- The Canada Business Web site at www.canadabusiness.gc.ca provides a comprehensive directory of information on the private sector and federal, provincial and municipal government services, business information guides, programs and regulations. The site contains information to assist small- and medium-sized enterprises (Sme's) seeking start-up financing.
- Sustainable Development Technology Canada finances and supports the development and demonstration of clean technologies, including those related to energy efficiency. Their website at www.sdte.ca provides details on eligible projects and how to apply.
- The National Research Council's Industrial Research Assistance Program (NRC-IRAP) provides financial support in addition to a range of both technical and business oriented advisory services to growth-oriented small businesses enterprises. For further information or to contact an Industrial Technology Advisor, it is possible to call, toll-free, 1-877-994-4727.
- Industry Canada has developed the Sources of Financing Web site, at

www.strategis.ic.gc.ca/sources, which enables Sme's to interactively access objective information on appropriate forms of public and private sector sources of debt and equity financing. This information is provided through a searchable database that generates a comprehensive customized report on relevant sources of financing.

■ Also available is the Steps to Growth Capital web site at www.growth.ic.gc.ca. This site provides a step-by-step guide to entrepreneurs seeking growth capital.

■ Canadian Federation of Independent Business (www.cfib.ca) is a membership based lobby group which acts in the best interests of small business while producing research and participating in many private public sector dialogues.

Notes

1. Mrs. Lever is the founder and President of Lever Enterprises, Canada. She represented small business at all APEC SME WG and MM since 1996. For nine years (1998-2006) she was the Prime Minister of Canada's representative on the APEC Business Advisory Council where she chaired the Capacity Building and SME Working Groups. She has also acts as an advisor to the Minister of International Trade and to other Canadian and international government for a with respect to SME policy.
2. Canadian Federation of Independent Business (CFIB), Small Business Profile, December 2005.
3. www.strategis.gc.ca Website for Industry Canada programs.
4. www.strategis.gc.ca
5. See appendix for links to other primary websites.
6. Doing Business in 2006, Creating Jobs, a copublication of the World Bank and International Finance Corporation.
7. For full details of Budget 2007, go to <http://www.d-room.com/active/sme.nsf/id/HHUA-6ZSTXP?Open&Login>
8. "*Advantage Canada* is a plan that will help Canadians to build a strong economy. Government has an important role to play in creating the right conditions for

Canadians - and Canadian businesses and organizations - to thrive. This plan will create new opportunities and choices for Canadians" (<http://www.fin.gc.ca/ec2006/plan/ecpame.html>)

9. See <http://csgb.ubc.ca/ccpp/articles.html>
10. Currently under development with the Department of Foreign Affairs and International Trade.
11. Strategis, www.ic.c/epic/site/sbrp-rppe.nsf/en/rd0054le.html
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Disappointment and Challenges

Policies Addressing the Micro, Small and Medium Size Enterprises in Chile

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Introduction

In recent years, the Chilean economy has been featured by its high growth and manifest macroeconomic stability. Economic reforms carried out during the 1970s and 1980s, have transformed the economy from an inward-oriented development strategy into an open economy based on international trade and financial flows. Likewise, Chile moved from policies which implied a relatively high state intervention across markets to a more deregulated and competitive system in which resources are basically allocated on the basis of free markets.

In spite of the significant progress observed by the Chilean economy in terms of its growth and stability, there are still pending problems regarding the Chilean social dimension. As a result of the application of an ample policy package aimed at tackling the social situation, a dramatic decrease in the percentage of poverty from 40% to about 20% of the population happened in the 1990s. However, the country is still characterized by a deficient income distribution, a situation which displays an important political effect affecting the sustainability of the economic development. In fact, Chile has remained during the 1990s and 2000 among the 12 more unequal countries in the world regarding the distribution of total incomes, dramatically contrasting to its place among the 10 more stable and dynamic economies in the world. This is contradictory with the overall economic progress that has been praised all over the world

A key factor in explaining the poor income distribution of Chile in comparison with its noticeable success in macroeconomic achievements connects with the insufficient development of the Micro, Small and Medium Enterprise (MISME). On the one hand, this is a crucial sector in order to increase the competitiveness of the Chilean economy regarding the need of further diversifying exports, increasing the labor productivity and stimulating innovation and entrepreneurship. Reaching greater economies of scale through a better coordination and association of MISMEs is a potentially important instrument for Chile to continue in its economic strategy of trade openness. On the other hand, the development of the MISME can imply a significant improving in the prevailing income distribution, given that it is more labor intensive and able to better reflect on labor earnings the actual productive results.

The Chilean economy has done much in terms of setting macroeconomic policies which afforded good aggregate results and made the country world famous to their respect. However, the policies addressing the development of MISMEs are still wanting and need to be improved in the continuation to what has been called "the second stage of economic development", which implies a necessary change from exports intensive in natural resources to those more intensive in local value added. In this context, policies addressing the development of the MISME are an indispensable ingredient.

The Chilean Economic Results

Economic results between 1987 and 1995 were brilliant from the view point of GDP growth, exports, investment rates and low inflation. If in the 1950-1971 period the economic growth averaged 4.2% p.a., in the 1987-1995 period growth reached more than 7% p.a. in average; by the same token, yearly inflation decreased from an average of 26% to 7% p.a. whereas investment, expressed as a percentage of the GDP, increased from 17% to 26% in the aforementioned periods. The per capita income grew at 2.0% p.a. in 1950-1971, while in the 1987-1995 period the growth of this variable was 5.3 % p.a. Altogether with these important achievements, the open unemployment rate remained around 6% of the labor force in the two periods which we are

comparing. Hence, the period 1987-1995 is considered a golden period of the Chilean economy, resulting from the productive potential awakened by economic reforms carried during the 1970s and 1980s, which were kept in their essential components by the democratic governments in the 1990s.

The economic reforms of the Chilean economy followed the lines of the structural adjustment programs encouraged by international financial institutions under the so called "Washington Consensus". These programs aimed at reducing the extreme weaknesses of developing economies, trying to open them to international trade and at reducing the economic size of the state. Along those lines, a dramatic reduction in tariffs was carried out in Chile in 1974-1978 to produce an important opening of the economy to foreign trade. This took place along with a significant stabilization program aimed at attaining lower inflation rates, one of which decisive instruments was a tight monetary policy altogether with a notorious drop in fiscal expenditures. A significant reduction in the economic size of the State and the degree of government intervention across the economy were also key companions of the macroeconomic program. After the dramatic financial crisis in the early 1980s, largely due to an overvaluation of the Chilean peso due to a nominally fixed exchange rate, the government continued implementing a deep economic reform program. This included the privatization of most public firms, the continuation of a tight fiscal and monetary policy and the adoption of an export-promoting strategy.

As mentioned above, the notable achievements of the Chilean economy in macroeconomic terms diverge quite remarkable with the observed situation reached in the social dimension. Unemployment rate has remained relatively high in recent years, in spite of a GDP growth above of 4% p.a., this being an important factor underlying the persistence of an unsatisfactory income distribution. In fact, the difference in the average income of the 20% poorer compared to the 20% richer amounts to 17 times, whereas it is only 9 in the USA and 10 in Korea. Although the country has done a lot in terms of reducing the extent of absolute poverty, which currently remains a little below 20% of the population after having reached as much as 40% in the 1980s, the gaps between different income groups are still very significant, and becomes a decisive political factor that may hinder the continuation of the economic strategy. As many see the economic model as the final responsible for these

observed social results, the effect of a deteriorated income distribution may attain a significant detrimental effect on aggregate economic achievements.

This situation of the income distribution in Chile is largely due to the role played by several structural factors connected with the distribution of education and human capital among the population, as well as to the different productive specialization that characterizes different regions inside the country. Nonetheless, a key factor regarding the poor record reached with regard to the income distribution in Chile connects with the labor productivity and the distribution of the human capital across different segments of the labor force. In fact, the discussion about failures in education quality and the absence of an adequate system of public education as well as in connection with the low expenditure in research and development (R&D) have been pointed out in discussing the poor progress of the country regarding its competitiveness (World Development Forum, *World Competitiveness Index*, 2007).

At the same time, another crucial factor in explaining the deteriorated income distribution observed in Chile concerns the structure of the productive activity. In fact, although many policies have allowed large firms an adequate environment for their development and subsequent success in terms of production and exports, these policies do not apply to smaller firms. Although the MISME is the primary labor source in the economy, and it is present in all productive branches and regions of the country, policies addressing its development have been inadequate and insufficient. The high degree of financial exposure, the lack of collaboration to obtain resources for the investment, high cost to initiate and develop business due to red tape, the absence of instruments to provide smaller firms with opportunities for labor training, etc. are all crucial detrimental factors which have been insufficiently tackled by the economic policy. Politicians and government authorities have manifested concerns about the macroeconomic dimension and the need for supporting MISMEs development, but little has been done to attend the necessary microdimension in establishing a more friendly environment regarding the development of the smaller firms.

The Concept of MISME

Traditionally Chile has not adopted a formal, well established definition of the micro, small and medium enterprise. Lately, however, data from the Internal Revenue Service (IRS) has allowed a definition based upon the value of total sales (Table 1). According to these criteria and as a proportion of the total private employment³, the occupation provided by the MISME reaches a 81.1%; in comparison, this sector represents only a 21.7% of the total sales in the economy, according to IRS figures in 2003⁴. In other words, if productivity is defined as sales per employee, it is clear that, at a national, aggregate level, large firms are 36 times more productive than MISMEs. If this index is calculated only for the medium size firms, the productivity gap with large firms is equal to 3, whereas it is equal to 6 in the case of small firms.

Given the high proportion of the employment provided by MISMEs, it is clear that the sector must constitute a concern for the public policy. The adequacy of a policy aimed at promoting the MISME can be questioned on the ground that is a low productivity sector, as reflected by the amount of sales per employee. However, the ratio formed by sales and employment cannot be considered as an indicator of labor productivity, given that the efficiency of the sales dimension in any enterprise is associated with general management aspects, such as those related to expenditures in marketing, transportation and installations, rather than to merely production. At the same time, the high labor intensity of the MISME sector implies that policies aimed at achieving its development can introduce a significant equitable impact, particularly in the area of labor force training.

In any case, the MISME has been declining its relative importance in sales between, for instance, 1999 and 2003⁵. Similarly, the importance of exports associated with the MISME in relation to total exports has dropped from 5.3% to 3.9% between 1999 and 2003. Therefore, and as a result of an inadequate policy environment, the participation of MISMEs is quite high in employment but quite low and decreasing in terms of sales and exports⁶. The current political debate in Chile concerns with this significant difference, and the need for different policies aimed at stimulating the MISMEs to reach higher sales and exports, as well as better productivity standards.

Problems Regarding the Development of the MISME in the Chilean Economy

Nine fundamental problems can be identified with regard to the situation of the MISME in Chile. These problems act as a significant impediment for achieving its more prominent productive development.

- (1) The public policy does not recognizes MISMEs as a different economic unit as opposed to large enterprises. As a consequence, economic policies do not discriminate by size of the productive unit and are defined only in connection with large private firms. Governments need to give recognition to existing differences and problems for both large and smaller productive firms, thereby introducing different policies in the context of targeting economic results;
- (2) MISMEs are characterized by a rather disadvantaged access to markets, as they face a more difficult situation than larger firms regarding the conditions of financial intermediation and the access to services such as insurance, transport and commercialization services;
- (3) As providers of intermediate production for large enterprises, MISMEs are subject to a discriminatory treatment particularly in terms of payment delays, thereby implying that large firms transfer part of their financial liabilities to smaller firms, which are therefore paying for part of their commercial risks;
- (4) MISMEs constitutes an interesting political market which is widely exploited in electoral periods. However, there usually are no further commitments to their problems once a government is elected, thereby creating the sensation of a customary political exploitation. Moreover, leaders of MISMEs are not even considered as valid counterparts when discussing policy decisions at aggregate levels, at least not as compared to the prevailing situation with leaders of larger firms;
- (5) MISMEs are characterized by an ample heterogeneity regarding factors such as economic size, entrepreneurship capabilities, industrial branch to which they pertain, regional adscription, links to relevant output markets,

etc. Therefore, this causes weaknesses as public policies can hardly be targeted to all possible existing situations. In fact, the design of specific policy measures aimed at stimulating smaller firms are defined in such general terms that they cannot attain any significance in terms of potential impact. Another dimension of this heterogeneity problem connects with the enforcement of policies regarding taxation, environmental impact, intellectual property, labor policies and so on, which usually do not differentiate by firm size in terms of its application;

- (6) A serious constraint for the MISME sector is its faulty access to credit and to the financial sector in general. Lack of credit, particularly for working capital, is a serious factor inhibiting the development of the MISME sector due to the lack of enough collateral and absence of credit lines able to properly reflect higher risks with acceptable interest rates and periods of return;
- (7) There is an inadequate statistical definition of the MISME sector (ANNEX A). The use of definitions based on sales implies that there is a significant volatility in the statistics since the number of firms pertaining to alternative groups varies significantly from year to year. In turn, this is an inconvenient factor with regard to policy design and evaluation;
- (8) There are too many definitions of instruments for the promotion of the MISME, which are located at different levels in various public sector institutions. At the same time, the MISME entrepreneur usually does not have the time or the professionalism to complete so many forms and evaluate alternative offers which respond to alternative opportunities. In addition, there is insufficient emphasis in this sector of the economy, as demonstrated by the fact that between 1990 and 2004 public resources for industrial promotion has increased 2.5 times and that only 39.8% of these resources are allocated to MISMEs, thereby demonstrating the bias of the public policy towards larger firms.
- (9) MISMEs are particularly disadvantaged in accessing instruments of human capital formation, such as formal training and specialized education, as well as in counting with applied research that may increase their productive efficiency and capacity of innovation. All the corresponding

policy instruments in place in the country are based in the reality of larger firms, and therefore they openly discriminate against the needs of the MISME.

The problems so described make virtually impossible to attain a significant development of the MISME, particularly in the export industry. Chilean politicians recognize in their public speech that the continuation of the country's development strategy necessarily implies a shift from a natural resource-based industry to an export strategy concentrated in industries that include more value added in the local production. The international experience, particularly the Asian one, indicates that export diversification should be associated with a potent growth of the MISME, with policies that allow their development, their coordination and integration to gain economic efficiency. As said above, this would also allow Chile to obtain better distributive results as an expansion of the MISME may also promote an increase in the labor productivity. To attain a significant development of the MISME in Chile a political decision is essential. In this context, the government must aim at better policies to address the fundamental failures that characterize the situation of the MISME in the financial, training and general policy design.

The Public Policy Environment

The policy design has not been aimed at stimulating the development of the MISME, since in its general inception economic policies have fundamentally targeted the large firms as their basic objective. This is in fact responding to the actual importance of large firms in terms of production and exports, since they concentrate around 90% of the economic activity measured according to these parameters. However, these policies do not account for the importance of the MISME with regard to employment, as well as to the possibilities of increasing the labor productivity in the economy and attaining a development strategy based upon the productive increase of the MISME.

It is not, however, the case that Chilean governments have done nothing in terms of policies and institutions regarding the MISME. The problem is the

dispersion of policies and institutions in charge of the MISME inside the government, at the same time that overall resources have not been enough to deal with the magnitude of observed problems.⁷ In the past five years, for example, the government has created more than one hundred programs in support of the MISME which have operated through no less than fifteen distinct government offices in different Ministries. In addition, the amount of resources has not been enough considering the important target constituted by so numerous enterprises characterized by a large diversity from different viewpoints. As mentioned before, the MISME is characterized by substantial heterogeneity regarding the industrial branches to which they pertain, regional adscription and specific situation regarding their financial situation, as well as the particular condition regarding human capital needs and the peculiar impact of regulatory policies. On the contrary, the large enterprise is more homogenous and characterized by a high degree of concentration, making it easy to target alternative policies and evaluate their result.

The general economic policy cannot provide a propitious environment for the MISME, as policies regarding taxation, general business regulations, labor, environment, etc., cannot discriminate according the size of economic units. This has resulted in a quite unequal situation for the existing competition between the MISME and the larger firms, and has not provided adequate protection to the former when there prevails a vertical integration which is prone to abusing smaller firms. Policies that have stimulated the international insertion of the country, for example, have openly favored larger firms, since, differently than the MISME; they accomplish the several financial requirements and have the organizational capabilities to attain an active and permanent participation in foreign trade.

The example of the retail sector can be used to illustrate with regard to some of the issues mentioned above. This sector represents in Chile about 42% of the total entrepreneurial initiatives. However, measured through the Gini coefficient⁸ the degree of concentration in large firms, as opposed to MISMEs, is extremely high: going from 0.835 in 1998 to 0.842 in 2004. This degree of concentration of retailing in larger firms is not in principle beneficial to consumers, and it is the result of general economic policies that have either propitiated concentration or disregarded the importance of it. To a large extent this situation is due to the access of large enterprises to lower input prices,

which allow them to drive MISMEs out-of-the-market, and subsequently increase the final price to consumers. This situation has not been prone to promoting a more transparent competition, raising the need for more sophisticated rules on regulatory policies than those actually prevailing.

The economic policy has not been able to successfully introduce a positive discrimination to attain a further development of the MISME sector. The past government administration and the present one have attempted to create alternative policy packages aimed at encouraging the development of this sector, but they have not been successfully implemented. Three examples can be quoted to illustrate the lack of an adequate policy design in the aim of encouraging the MISMEs development.

The first example was the project that in 2006 attempted to solve the existing problem of tax liabilities of the MISME sector, including the negotiation of periods of payment and the reduction in interests and charges against the debt amount. Since there were more than 360.000 tax payers in arrears pertaining to the MISME sector, a situation that exerted negative consequences regarding their prospects to obtain access to the financial sector, it was expected that a large number of them could have used this alternative. However, only 10% of the total numbers of those entrepreneurs in tax arrears were actually able to take the package. The reason was simple: the government proposal implied the immediate payment of 30% of the total debt in arrears, whereas the remaining 70% had to be paid in 11 payments. Given the financial reality of MISMEs the offer was simply unaffordable for this productive sector, making the announcement of the package a failure with regard to its actual achievement⁹.

A second example was the announcement made by the government in August 2006 in order to modify the timing for enterprises to pay their sale taxes. Firms in Chile have to make two tax payments that may significantly affect their cash flow: the 10th day of the month they have to pay the payroll tax, and the 12th day they have to do the same with the value added tax (19% of their sales) plus a provisional payment of about 1% to 3% of their total sales as a credit on their annual tax payment. The government proposal consisted in postponing those payments to the 20th day of the month, in order to alleviate the cash flow situation of the MISME, and granting more time for them to get

enough resources. However, such a good idea did not work out since an eligibility requisite was that all payments should be made using internet, thereby also implying that enterprises had to have a checking account in the banking system and being able to emit electronic documentation on their sales. Given that this is not the reality of the vast majority of micro and small enterprises, from an universe of about 690,000 MISMEs, less than 2,000 were able to access to the proposed benefit. In fact, more than 50% of MISMEs do not have any checking account given their prevailing liabilities with the financial sector, and 99% of them did not yet have any access to electronic technology to process and produce electronic sale receipts¹⁰.

A third example of inadequate policy design was the proposal made by the government in 2001 in order to have a law for the promotion of the MISME. Six years later it can be said that this has not been at all carried out in spite of the commitment publicly made by the government. However, a new announcement made by the Minister of Finances in April 2007, has once again proposed the idea of developing an ample legal framework for the MISMEs.

The problem with the policy design regarding the importance of the MISME sector in the economy has suffered from two inconveniences. First, the lack of a real political commitment of the authority with the evolution and contribution of the sector to the economic activity and employment. Second, the improvisation of policy measures which are more oriented to gain a superficial support by the public, but not to achieve any effectiveness in terms of the real impact in the economic activity, employment and the income distribution. In general, the idea of firm which largely prevails in the inception of the economic policy corresponds to that of large firms, which is at the same time the sector able to put more economic and political pressures on governments.

Public - Private Collaboration and the MISME Development

Although disadvantaged by the general inception of the economic policy, the MISME in Chile has proved its capacity to compete in an environment of transparency and fair rules. Their open competition with large enterprises,

however, is affected by financial disadvantages, specially because they are exposed to a situation in which the larger firms can delay payments and create cash-flow complications to the smaller ones. This is the case when the MISME is a provider of intermediate products for larger firms. Other times the open competition in product markets is affected by the size of the MISME, because they cannot compete with the marketing expenses of large firms. The bargaining power of the MISME vis-à-vis the large firm is undoubtedly weak, and it is the reason for their visibly lower capacity to compete. However, it is possible to assert that, under more transparent conditions, particularly regarding information, the MISME can compete very much better with its larger counterparts.

The Chilean government has implemented an on-line system where firms are invited to furnish with their offers of goods and services, in the frame of specific demands raised by the public sectors. This *Portal Chile Compra* is a system adopted by the government to facilitate the management of public resources allocated to buying goods and services from private suppliers, at the same time than offering a transparent system for an open competition on the part of private firms. In this system, which is not featured by asymmetric information or other common market distortions, the MISME reaches a 38.8% of the total sales made by the government¹¹, a proportion that is strikingly higher than the 21% of participation they reach in "open" markets. This is a clear indication that the higher the transparency of the market, and the lesser the asymmetry of information, the higher the possibilities of success of the MISME.

The situation of the MISME is strongly related to the existence of market mechanisms that negatively discriminate against smaller firms, given their economic size and lack of capital. This is the reason the public policy concern gravitates around the idea of adopting policy measures that may give more opportunities to MISMEs. In this aim, the authority has called upon public-private task forces or committees to address proposals in this context and acquiring a better knowledge of the industrial organization issues surrounding the participation of the MISME in the market. The usual problem in adopting a policy view on regulations that may improve the competitiveness of the MISME in the context of better market rules, is the prevailing view that raises concerns only to the relationship between the state and the firms, this being

conceived in the frame of large-formal firms. This view disregards the existence of the MISME, a disadvantaged sector with regard to general economic policies.

That prevailing view has affected the quality of policy decisions with regard to their potential effect in term of the MISME. Whenever a discussion takes place in decision-making instances, with regard to providing assistance to the productive sector, the issue of declining fiscal revenues or possible harm to the large firms comes about. By the same token, policy measures aimed at helping the MISME with regard to taxation or labor issues are generally rejected with the support of labor unions which also only see the large enterprise as the beneficiary, since they do not use to differentiate firms by sizes.

The crucial issue concerns the need of targeting policy measures to the MISME in order to improve their financial stance and their actual possibilities of competing in the market by means of more transparent rules. However, the targeting of MISMEs is very difficult to achieve given the prevailing view on private firms as one homogeneous situation, in which there would not prevail disadvantages that can be seen as negative economic externalities.

This simplistic view of the relationship between the state and the private firms has dominated the policy scenario relevant to the MISME. If a differentiation is made between the MISME and the large firms, a great benefit can be attained for the former in terms of taxation, financial and other measures aimed at alleviating the disadvantages for them to operate in distorted and not fully transparent markets. As mentioned above, the nine issues that characterize the weaknesses of the MISME shall be tackled though appropriate policy measures that need to clearly identify the sector and its problems¹².

Policies to Achieve MISME's Adequate Development

A key endogenous variable to consider in the aim of attaining an improvement of the MISME connects with its own management. This in turn connects with

the possibilities of gaining access to adequately trained human capital characterized by both technical competences and due knowledge of relevant markets. In many respects the current situation in Chile reflects a notable deficit in this matter derived from the prevalence of relatively low salaries of the managerial staff in the medium size enterprises, and the inexistence of any professional management in micro and small firms. In general, the low attractiveness of professional jobs in the MISME is entailed to the high volatility that characterizes this sector regarding its development in terms of expansion and survival conditions. Altogether with these structural problems, the MISME has a very low access to formal training systems, particularly those eligible for public subsidies.

Regarding the exogenous factors that affect the development of the MISME in Chile, the lack of adequate access to formal training is of paramount importance. For the MISME the opportunity cost of its employed labor is higher than that corresponding to the case of the large firms, particularly because there is insufficient possibilities of substituting job positions from the inside of the firm. In addition, the prevailing rules to access public subsidies for the formal training¹³ establish a clear discrimination against the MISME given that the subsidy is provided through a credit that operates in a year time frame, which is a negative factor affecting the MISME's cash flows.

Another key exogenous factor affecting the development of the MISME connects with the relationship between this sector and that of large firms. As mentioned above, the latter usually employs some unfair practices in competing against smaller firms. In the case when both the MISME and the large firms operate in the same market as suppliers, the large firms carries price policies aimed at installing entry barriers which normally hinder the possibilities of fair competition and usually attain to expel the MISME from the market. In the case when the MISME operates as a suppliers of inputs or parts to the large firms, it is usually the case that payment delays and arbitrary rules regarding delivery conditions may simply drive out the MISME from the market. Undoubtedly, there is large room for improving or creating a more appropriate legal body regulating this unfair competition practices.

The situation of the MISME is raising an active political debate in Chile as it is being more and more clear that the low development opportunities that public policies offer to the MISME seriously threaten the possibilities to sustain aggregate economic growth in a long term context, as well as to achieving an improvement in the income distribution. This is the reason why the current government administration has been raising the need for discussing a new legal framework to assist the MISME, emphasizing the basic conditions to attain its sustainable development. In this context, there is a need for discussing some urgent policy measures which are not necessarily aimed at modifying structural prevailing conditions affecting the MISME, but only aimed at correcting some specific problems. Basically these measures connect with the large financial debt of the MISME, which is virtually obliterating its development potential and drastically restricting available cash flows. New terms regarding financial charges, especially those connected with risk assessment and periods of payments should be included in a legal definition that must also include the eligibility conditions to access government subsidies. This new legal arrangement should also establish similar measures regarding the high indebtedness of the MISME sector with the tax system and the social security.

At the same time, the public policy must deal with some of the structural problems affecting the MISME. To this respect, it is envisaged that the new MISME's legal body (*Estatuto*) should be the key to establishing the difference in economic size as a fundamental variable guiding the public policy. If economic size is recognized in the law as a relevant policy variable, it will provide ground to prepare new regulations to avoid unfair competition based on firm sizes, and it will allow better conditions for the development of the MISME. The new legal framework for the MISME (*Estatuto*) shall be based upon the idea of securing market transparency, a key structural ingredient to achieve the development of smaller firms. Asymmetric information and the practice of unfair competition by large firms are two basic elements that the *Estatuto* should address upfront. A fair-play system should stem from the *Estatuto* to avoid those practices that, by reducing the access of the MISME to markets, are key in deterring its development. The government must use its regulatory capabilities to enact a new legal framework in this regard. Similarly, the government can use its own economic size to install competitive practices by which only the good management and the

competitive advantages of firms should be accounted as the only factor able to explain market success.

There are three aspects in which the Estatuto shall be carefully designed to attain an adequate competitive environment to favor the MISME's development.

- (a) Access to the financial markets in better conditions regarding interest rates and time frame. The high risk normally associated with the MISME and the lack of sufficient collateral are structural weaknesses that can be effectively mitigated through state subsidies and the operation of Chile's State Banks and other government institutions which can be mandated to deal with MISMEs. This subsidy is consistent with the idea of positive externalities that in terms of economic activity, employment and the income distribution, can be entailed to the development of the MISME.
- (b) Access to training through similar instruments than those that allocate resources to large firms, but without affecting the cash flow as it now happens in the case of the MISME.
- (c) Access to technology and innovation by measures to allow engagement of consortiums of MISMEs in different production fields with research centers. This would allow the MISME access to fresh knowledge and technologies, thus also allowing research institutions to tackle problems that specifically affect this sector of the economy. This would also allow research institutions to be better in touch with national priorities in terms of applied research.

An appropriate definition of the MISME

The appropriate definition of the MISME is a key element regarding regulatory aspects as well as in adopting alternative economic policies. The segmentation at the inside of the MISME is also a fundamental aspect to consider given the need of targeting alternative policy instruments to different categories of firms. Until now there has not been any official definition of micro, small and

medium size firms, a subject on which there have prevailed many alternative criteria based upon different grouping of firms. These definitions have originated in academic purposes, as well as on entrepreneurial views, considering either sales, employment or taxation as clear-cut definitions.

The need of an official formal definition is paramount to any policy effort aimed at attending the needs of the sector. An incorrect definition may leave some larger firms classified as small or medium - if only sales is, for instance, the variable used to measure economic size. This would allow some large firms to access benefits designed for the smaller ones. By the same token, by only considering employment as clear-cut definition of size, a significant volatility could be introduced in the statistics, thus causing serious problems to properly target policy measures. The most usual definition of micro, small and medium size firms, as opposed to large firms, is based upon the amount of sales, which is a variable that may introduce significant distortions.

Currently there is not any official definition or policy action that effectively takes into account the needs of the MISME sector, because legally it does not exist. At the same time, policies addressing MISME issues are ineffective in absence of an appropriate statistical definition. The new legal body sought by the government (*Estatuto*) constitutes an effort to carry out policy initiatives to support the development of the MISME, but they would do little in absence of adequate definitions of the sector.

To avoid the volatility and the misleading use of the statistics that segment firms by size we propose a methodology to define an index number. This will allow distinguishing between micro, small, medium and large firms based upon the agreement on specific value brackets. This classification takes into account three variables which are usually available from sources such as tax information:

- (a) Sales (S_t): Annual sales (period t) of the firm measured in Chilean pesos (\$);
- (b) Employment (L_t): employment in different job positions used by the firm in period t, a variable which should not be included in simple linear terms given its high variability across firms according to efficiency levels and the organization of the firm;

- (c) Assets (A_t) corresponding to the declaration of the firm on accumulated investment net of depreciation.

It seems that a proper way to include the employment variable in determining the index number is by considering it relative to the amount of sales. What it is important for policy purposes is the labor intensity that characterizes the productive behavior of smaller firms, and this can be adequately proxied by the value of sales by employee. Thus, the polinomy we propose to build up the index number (I_t) is the following:

$$I_t = a_1 S_t + a_2 (L_t / S_t) + a_3 A_t$$

$$\text{With } a_1 + a_2 + a_3 = 1$$

Instability can still be a problem with this definition. Think, for instance, in the case of a small firm that has been classified as such for several periods, and that in a particular year, given the selling of a large amount of output, it is classified as "large". This could also happen the other way around, introducing problems which may affect the effectiveness of alternative policies. Therefore, we propose the calculation of the index described above by a moving average over three years.

Concluding Remarks

Chile has been a very successful in its aggregate economic results. In general, the macroeconomic policy has been quite satisfactory regarding the attainment of higher growth and investment, a fair degree of economic openness and low inflation rates. However, there are still problems regarding the income distribution and a need for microeconomic policies aimed at attending issues arising from the different size of economic units. Only by making this distinction it would be possible to provide better conditions for the MISME development, an objective which is important in attaining higher employment creation and better distributive results. At the same time, the development of the MISME is paramount to attain a higher productive efficiency and to consolidate the progress of the economy towards a diversification of its export

base, including a higher value added.

The economic policy has not been able to introduce a better environment for the development of the smaller firms, although the government has attempted to provide adequate incentives towards that direction. In general, the economic policy has been considered in terms of the large firms and their problems, but not necessarily with the smaller productive units. The Chilean government is attempting to enact a new law to provide the MISME with a more appropriate policy environment, and thereby simulate its development. In this new initiative, which has been waited for a long time in the country, it will be necessary to account for the main disadvantages that the current situation presents to the MISME, and introduce the definitional criteria regarding the size of the firm allowing to improve the targeting of alternative policies.

Table 1: Classification of Firms by Amount of Sales and Employment

Size	Annual Sales (US\$ Dollars)	Number firms (According to sales)	Number of Employees	Number firms (According to Employment)
Micro	35 to 83,000	570.544	1 to 9	647.529
Small	83,000 to 865,500	105.524	10 to 49	39,329
Medium	865,000 to 3,462,000	14.577	50 to 199	6,964
Large	3,462,000 and more	6.868	200 and more	3,691
Total		697.513		697.513

Table 2: Number of Firms, Employment and Sales

Size	Number of Firms (IRS Criterion)	Number of Firms (%)	Employment*	Employment %	Sales IRS Criterion (million US\$ Dollars)	Sales %
Micro	570,544	81.8	2,276,032	49.1	8.6	3.4
Small	105,524	15.1	822,745	17.8	24.14	9.5
Medium	14,577	2.1	600,787	13.0	22.2	8.8
Large	6,868	1.0	933,858	20.2	198.72	78.3
Total	697,513	100.0	4,633,422	100.0	253.66	100.0

* Data obtained from the Socioeconomic Survey (CASEN) 2003.

Table 3: Expenditure in Productive Promotionⁱ

Year	Total	MISME	%	SM	%
1990	158 ⁱⁱ	10	6,3	2	1,3
1991	218	17	7,8	5	2,3
1992	299	30	10,0	7	2,3
1993	426	31	7,3	10	2,3
1994	528	43	8,1	13	2,5
1995	537	18	3,4	13	2,4
1996	598	63	10,5	25	4,2
1997	639	80	12,5	23	3,6
1998	660	84	12,7	32	4,8
1999	673	115	17,1	44	6,5
2000	687	125	18,2	47	6,8
2000/1999	4.3	12.5	21.5		

ⁱ The data corresponds to the total expenditure in productive promotion by the MISME and the Small and Medium Enterprises (SM). It also reproduces the expenditures in export promotion and training.

ⁱⁱ Million of US\$ Dollar 1998.

Source: Ministry of Economic Affairs 2001.

Year	Total	Export	%	Training	%
1990	158	49	31,0	31	19,6
1991	218	89	40,8	44	20,2
1992	299	137	45,8	52	17,4
1993	426	224	52,5	66	15,5
1994	528	269	50,9	76	14,4
1995	537	274	51,0	77	14,3
1996	598	300	50,2	78	13,0
1997	639	297	46,5	74	11,6
1998	660	298	45,1	93	14,1
1999	673	254	37,7	108	16,0
2000	687	282	41,0	101	14,7
2000/1999	4.3	5.7		3.3	

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Notes

1. Full Professor of Economics, PhD University of California-Berkeley; former President of the University of Chile and Professor (Invited) Autonomous University of Barcelona.
2. Industrial Engineer, Professor of Management, M.A. in Business Accounting; Chairman of the Department of Accounting and Management - School of Economics and Business - University of Chile.
3. The Total Private Employment is equal to the total employment in the economy discounting that provided by public (government) services and the Army Forces.
4. To this respect, see Table 2 in the Appendix.
5. The MISMEs sales relative to the total flow of sales in the economy, according to IRS data, declined from 26.9% to 21.7% between 1999 and 2003.
6. In addition, if 27.5% of the large firms that existed in 1996 had disappeared by 2002, this proportion was 84.8% in the case of micro enterprises, and 58.6% and 41.6% in the cases of small and medium enterprises respectively.
7. After increasing political pressures derived from the rejection in the Parliament of a Project aimed at providing more resource to large firms. The government has proposed a new financial package for the MISME amounting to US\$750 millions, which however is less than 0.5% of the GDP.
8. The Gini Coefficient adopt values between zero and one, been closer to one as higher may be the degree of concentration.
9. A new project (2007) has reinstalled this idea, with some modifications regarding a larger amount of taxes in arrears and a lower downpayment.
10. As it could be expected, the large enterprise has made plenty use of this benefit originally thought for the MISME sector.
11. Data obtained from the Portal Chile Compra (www.chiulecompra.cl) for the year 2006.
12. The Director of the Chile's IRS has declared that 90% of corporate taxes are paid by the 1.8% of the private firms, clearly large firms. That is, only 10% of taxes which reflect corporate profits, are associated to the MISME. With little fiscal effort, the MISME could reinvest profits, this having a significant impact on employment and the economic activity.
13. In Chile this subsidy is managed by the National Training and Employment Service (SENCE).

The SMEs in Colombia

Institutions and Policies

By Angelica Marcela Acosta and Catalina Jimenez Rojas

*Colombia Association for Micro,
Small and Medium Enterprises - ACOPI*

ACOPI - Colombian Association for Micro, Small and Medium Enterprises

It is the gremial organization of Colombia that groups together the formal micro companies and the small and medium companies of the various productive sectors. It is an organization without profit motive, founded in August 27, 1951. Its Mission is to foment the development of the small and medium companies as well as the micro companies for the progress of the country, within the rules of the social and ecological economics of market. ACOPI has functions of representing the interests of the sector before the various national and international instances and has assumed the role to lead the process of sustainable and competitive development of the micro, small and medium enterprises (MIPYME) through associative programs of initiatives for the productive linking, formation and training, technical assistance, commercial, institutional relationships at national and international level.

ACOPI has led in Colombia and it has advanced with the support of the Inter-American Development Bank, the government authorities in the Departments, the Konrad Adenauer Foundation and national institutions, initiatives tending to fortify enterprise collective processes with methodologies that respond to the local and sector necessities as well as at the level of associative experience and conformation of networks on which already it counts on an important number of affiliated and not affiliated companies. ACOPI groups ten

thousands affiliated at a national level, in enterprise, associative, registered and institutional categories. It counts on 15 regional offices at national level (Structured Services Portfolio).

The strengthening of MIPYME segment in Colombia, fundamental mission of ACOPI, demands the design of policies, strategies and actions that reflect and approach the relation of the minor size enterprises with their closer surroundings, the locality. This involves connecting the segment enterprises to productive initiatives that influence the areas that affect it more, the poverty in all their social and economic expressions, the unconventional work, the minimum access to the knowledge, the absence of real productive linkings, the lack of professional training and technical assistance, the absence of scale economies, by means of actions that strengthen the attributes of the small and medium enterprises as they are: a modern production without ecological deterioration, effective answers in employment terms, capital distribution, good social balance, adaptability to the technological change, methodical answer to the necessities and demands of the international markets, profits distribution, efficiency, versatility, harmony production scales with sizes and characteristics of the markets, diversification of the exportable offer, enterprise associability, and factor for the regional linking.

ACOPI supports the National Government and the national gremial Board in the policies formulation for the strengthening of the MIPYME in Colombia as well as to stimulate the segment companies to fulfill the millennium goals. ACOPI works with the multilateral cooperation institutions, with national institutions in the improvement and implementation of strategies and projects that favor the development, the diversification of the supply, the access to new markets and the improvement of the environmental and social conditions in the productive activity of the minor size enterprises.

Principal ACOPI's Activities

The ACOPI's gremial activities have two big functions: The first one is to take the representation of the partners in front of the public opinion, the private organizations, the governmental authorities and the international

organizations. The second one is to develop services for benefit of its members. ACOPI, as a social and economical entity of national character has assumed the role of leading the process of sustainable and competitive development of the Small and Medium Enterprises, not only by means of the formulation of offers of public politics, but as direct Executor of many programs directed to achieve such a development and to the projection of the sector in the orders nationally and internationally.

ACOPI is an institution that offers services of training, technical assistance, information, organization, commercial, institutional relations and project administration.

ACOPI in an international context

In the international field, ACOPI supports its leadership and realize efforts for extending its relations and influence. The Association exercises the presidency of the Latin-American Federation of Median and Small Enterprise CLAMPI. Likewise, ACOPI had the opportunity to preside at the Afro - Asian Conference of SMES and the Council of Government of the World Assembly of Organizations of the Small and Medium Enterprises (WASMES) re-elected to the union in the World Vice-presidency of the associations and institutions of the sector.

ACOPI supports activity in the SLAMP - Latin-American Symposium of Mike, Small and Medium Company-, as well as in the Andean Federation of the Small and Medium Industry CONANPYMI, the Latin-American Organization of Small enterprise - OLAMP - and in the Economic Council of the Pacific Basin, so that this gremial association has given to the Colombian SMEs a high level of representation in the international area.

In order to qualify the Colombian SMEs from international successful cases, ACOPI organizes annually different sectoral and cross-sectoral to different countries. In the last years, the missions had been organized to Spain, Italy, Germany, in Europe; Singapore, Malaysia, Taiwan, Hong Kong in Asia; Chile, Venezuela, Peru in South America; Cuba and Dominican Republic in the

Caribbean, etc. Nowadays, it leads, in alliance with other institutions, the program EUROSMEs - PROLIDER.

ACOPI was gathering and leading Andean integration of SMEs in the Negotiation of the Andean Free Trade Agreement (AFTA) between these countries and the United States of America.

On the other hand, in August of 2006, in the Third Round of Negotiations Colombia - Countries of the Triangle North of Central America (Honduras, El Salvador and Guatemala), the presidents of the national federations of SMEs, belonging to the Latin-American Federation-CLAMPI, led by ACOPI, presented a set of offers to the Negotiating Chiefs of every country, whose content includes five offers for the effective incorporation of the small and medium enterprises, and the utilization of the opportunities of the Agreement of Free Trade in mention. Some of the offers are: an agenda of horizontal cooperation, political public and instruments, institutional managerial strengthening, integration of the SME of the region, and an effective incorporation of the small and medium enterprises in the Agreement.

The Small and Medium Enterprises in Colombia: Engine of the Economy

A. CLASSIFICATION AND STATUS OF SME.

The definition of the SMES companies is a great help to know the magnitude of every segment of companies, and, therefore, its impact in the productive activity, and to take measurements best focused of promotion of the production. Nevertheless, "there is not a definition of SME universally recognized and, probably it is not chance. According to the International Labour Organization -ILO-, there is no definition that can assemble all the aspects of what is a small or medium enterprise, the differences between companies, sectors or countries with different degree of development ".

The countries apply diverse criteria to define the size of the companies of to sanely to its number of workers, of its economic activity, volume of sales, the

share capital, the brute value of the production of assets, also the degree of utilization of the capital, the character of the structure of property (familiar or not relative), the degree of formalization, the technological used level, the organizational structure and the typology of the management of the company among others. For the previous thing, the classification of companies under the name of SME, will depend on every country and its own legislation, on conformity with its economic national environment and its needs.

Nevertheless, the definitions are based with more frequency on the employment, the Sales / income and the assets. Besides, some countries have many differences in the definition, depending on if the economic unit is manufacturing, commercial or on services. Even, there are countries in which the definitions change according to the institution that establishes them and, therefore, every institution applies its own one to formulate its political ones of promotion"¹.

DEFINITIONS OF SME

Category	Country	Category of industry	Criteria
Developed economies	Australia	Manufacturing	<100 employees
		services	<20 employees
	Germany	SME	<500 employees
	France	SME	10-499 employees
	Japan	Manufacturing	<200 employees
	Canada	Manufacturing	<200 employees
	USA	Very small	<20 employees
		Small	20-99 employees
		Medium	100-499 employees
	China	SME	Depends on product group. Usually 100 employees; Investment ceiling US\$8 million
Developing economies	Indonesia	SME	<100 employees
	Malaysia	SMEs	<175 full time workers.
			Investment US\$1 million
	Thailand	Labor intensive	<200 employees
		Capital intensive	<100 employees
	India	SME	Up to Rs10.00 million in plant and machinery

Source: Advanced manufacturing technology implementation. Evidence from Indian small and medium enterprises (SMEs), in: <http://www.emeraldinsight.com>

In Colombia, according to the Law 590 of 2000, which promotes the development of the SMES, "its understanding for micro, small and medium enterprises are any unit of economic exploitation, realized by natural or juridical person, in managerial, farming, industrial, commercial activities or of services, rural or urban". Equally, the law defines three big categories according to workers' number and the size of the assets that it possesses, since it appears later:

THE SMEs IN COLOMBIA

Size	Amount Workers	Total Assets
Micro	1 to 10	Up to US92.750
Small	11 to 50	Between US92.750 and US927.500
Medium	51 to 200	Between US927.500 and US5.563.640

1 US = 2200 COP

Like it can be observed in the previous picture, the criteria of classification used for the SMEs in Colombia, are the number of workers and the total assets. In case of appears a combination of parameters of Total Assets and of number of workers, different from the definite ones, the determinant element is that of the total assets. This managerial stratification, it allows "to support statistical references that serve to define trends and the behavior of the economic sectors and to evaluate the productive impact of each one on the GDP, which allows directing the efforts of promotion and development towards the strengthening of the most vulnerable sectors and the backing of the most productive"².

In Colombia the segment MIPYME "it develops in all the economic sectors, assuming different roles in the economic concert: supplier of goods and services for other companies, and producer of goods and final services"³. The micro, small and medium enterprises, conceived as a set of important links in the regional economies of the country, constitute a nucleus of growth and potential development of great importance, which needs support and strengthening with participation of all the possible actors (public, private, ONG, unions, international entities, etc.). In this environment, "the political ones on SMES must cause a development adapted to the like revitalizing market of the competitiveness and the managerial, like that growth it is a question of local markets, the national market or the international market."

The Colombian SMEs become the economic sector, with the biggest strategic potential to grow and develop in the Colombian economy, because already represents around 96% of the total of the enterprises and more of the 35% of the GNP, generating almost the 65% of the labor.

Micro, small and medium enterprises, according to information of the Presidency of the Republic, "They represent 96% of the business of the country and 33% of the working population. Its participation in the industrial employment ascends to 60% and in the value added of the industry to 48 %. In the trade, they represent 95% of the employment and 74 % of the production. "Nevertheless, according to the numbers of CONFECAMARAS (Colombian Association of Chambers of Trade), SMES in sales only contribute 33%, whereas the big companies that in quantity are 2%, they contribute 67% of the sales. Of the previous thing, it is possible to deduce that though SMEs only generate the third part of the sales, which can be equivalent to the same proportion of the GDP, they are the big generating ones of employment, in reason to which the big companies you have best levels of technology, which gives them major productivity.

But, only 13% of the SMEs are exporting firms, other 6% has intended it and the 81% remaining never have exported. From the other side, increasing global competition means that all enterprises, regardless of size, must adopt multinational perspectives. The circumstances - as a result of the globalization - that face up the Colombian SMEs are not propitious and has seriously affected their grow. Their future is very uncertain, because of the arrival of imports products and a consistent increase of the competition for a weak internal demand each time more demanding and selective.

As a fact, those productive units - that grew in a context characterized by a minimum inter-connection with the rest of the world, and mainly basing their growth in the dynamism of the local market, "closed" by the imports substitution model, that was adopted by the government at the end of the '60s and where the exports alternative was and still is, only an exception or an accidental business, depending only of the "ups and downs" of the local market and -some times- depending on the revaluations of the Colombian money. Now days they confront an unexpected scenario where they must face a strongest competition from all over the world.

This difficult situation has led to the disappearance of thousands of SMEs and a minimum growth for the survivors, because the unfavorable condition of the local demand in the last years (unemployment of 15%, and less than US\$ 2.400 income per capita). This situation has been acting as a motivation "motor" to some SMEs to explore the foreign markets (mainly our partners in the Andean Pact), with a relative but a significant success. In spite of the numerous groups of manufacturing companies, the value of their individual exports is not big enough and their permanence in the future is very questionable.

According to information of CONFECAMARAS, in 2001 there were 43.242 small enterprises and 8.041 median enterprises. According to the DANE, Administrative National Department of Statistics, in its first National Survey of Micro establishments of trade, services and industry, realized in the last trimester of 2001, in the year 2000 in Colombia there were 967.315 micro establishments, of which 58% was in the trade, 30% in services and 12.5% in the industry.

During that period, the micro-establishments generated 1.094.755 employments, what would be equivalent to 1.1 employments for establishment. The employment relationship for establishment is of 1.8 percent in the sector trade, 2.8 percent by the industry and 2.5 percent in the services. The survey also points out that in the 2000 they existed around 7.600 industrial establishments with more than 10 workers and 120.785 micro-enterprises.

In the trade, the establishments with more than 20 workers they totaled 3.832, they occupied 215.818 people and they carried out sales for 40.2 trillion pesos. The micro-business with not more than 10 workers they were 558.000, they generated 556.775 employments and they registered sales of 8 trillion pesos.

MICRO ENTERPRISES AND EMPLOYMENT

Sector	Number of Establishments	Total Workers
Commerce	557.759	630.267
Services	288.771	381.328
Industry	120.785	156.653
TOTAL	967.315	1,168.248

SOURCE: DANE

On the other hand, the SME is oriented mainly to the domestic markets. However, in accordance with The Colombian Association for Micro, Small and Medium Enterprises, ACOPI, 6% of the production is exported and 94% goes to the domestic market; in the year 2004, the exports were of 900 million dollars. The main destinations of the exports are the countries of the Andean community and the United States.

On the other hand, the Colombian magazine DINERO affirms in this respect that "...the exports of the companies inscribed in Expopyme, which is a program flag of the government for the exporter companies, they increased 256% from 1999, until 171 million dollars. The number of companies grew 156% when adding more than 800..." Regarding the main problems that it faces the sector to export their products, the same one articulates affirms that "studies of Proexport (an organization of the Colombian government) identify these aspects among the main obstacles of the SME to export. 71% of the companies consider the knowledge of the market as obstacle, 77% the adaptation of the product and 85% the access to channels".

The industrial sectors with more significant presence of the SMEs are allowances, makings, graphic arts, Metalmechanic, wooden furniture, leather and footwear, all them highly concerned. As a result of the processes of economic opening, the market of the products of the SMES confronts a strong competition of legally cared products, others of smuggling and some that, although legally cared, enter to the market under conditions of disloyal competition or of "artificial competitiveness" on the part of other countries.

In front of narrow and highly concerned internal markets, the SMEs are in front of more difficult conditions to attack processes of technological development that are economically viable in function of the size of their markets.

This way, there are several reasons that justify the formulation of a public politics to promote the development of the SMEs in Colombia. On one hand, they represent, like it was said previously, the biggest percentage in the total number of establishments and they contribute a high portion of the employment and of the added value of the economy. Not alone that, the government's intervention is also necessary due to the structural inadequacies

in the markets of factors and to the structure industrial Colombian characterized by big companies in an end and micro-enterprises and informal sector in the other one. It is clear also that to promote the development of the SMEs contributes to increase the competitiveness of the economy in general, and even more, if we speak of the segment that is the motor of the economy of the country.

B. SME INSTITUTIONS IN COLOMBIA

The law 590 of 2000 established rules for the regulation, promotion and development of the small and medium enterprises, as well as for the micro-enterprises. It is the call SMEs Law. For parliamentary initiative this law was modified by the law 905 of 2004 that "establishes a group of instruments to facilitate the access to the productive resources of the small producers.

However, it is the law 590 the one that marks the starting point for the support of the SMEs, since it looked for to endow to this managerial segment of the strategic and institutional inputs to overcome their structural difficulties, being the Politics' of State law mark for the promotion of the development of the SMEs. Their main achievements are:

- It strengthens the paper of the State as revitalizing of processes for the development of the private initiatives.
- An effort in the integration of the politics' different instruments, looking for to promote the integral development of the micro-enterprise.
- Efforts to channel the resources efficiently and to give them transparency. In this address it was created the Colombian Fund of Modernization and Technological Development of the SMEs - Fomipyme (in Spanish) - and the bottom to Undertake.
- It looked for a rationality of the resources and the institutional efforts when incorporating to other government and not government entities dedicated to the same objectives.
- It strengthens the development of the administration of the State from the

local things; this is, from the municipalities.

- It makes the National System of SMEs, defining their composition and functions.

The introduction of changes in the institutional mark made by the Law 590 sandal mainly three areas: their composition, the instances of decision and politics' instruments. Regarding their composition, it gives origin to agreement spaces among public and private entities: It created the National System of SMEs, conformed in turn by the superior advice of small and medium company, the superior advice of micro - enterprise and the regional advice, for the Ministry of Trade, Industry and Tourism, Ministry of Social Protection, Ministry of Agriculture, National Department of Planning, Colciencias, Bancoldex, National Fund of Guarantees and FINAGRO.

The law also believes the Superior Council of the Small and Medium Company, and it defined its functions: to contribute to the definition, formulation and execution of political public general, traverse, sectorial and regional of managerial promotion of the small and medium companies, - SMEs -, to analyze the economic, political and social environment; their impact on the sector and envelope the capacity of these to energize the competition in the markets of goods and services, to contribute to the definition, formulation and execution of programs of promotion of the SMEs, with emphasis in those referred to the access to the markets of goods and services, formation of human capital, modernization and development technological and bigger access to the institutional financial markets.

They are also part of their functions to contribute to the coordination of the different programs of promotion of the SMEs that are carried out inside the mark of the development plans and government's politicians, to propose political and mechanisms of invigoration of the competition in the markets, to incline for the periodic evaluation of the politicians and public programs of promotion of the SMEs, by means of impact indicators and to propose the necessary correctives, to foment the conformation and operation of Regional Councils of Small and Medium Company, as well as the formulation of political regional of development for this companies, to foment the conformation and operation of Departmental Councils for the Productive

Development, for the competitiveness and stimulating chains of value at subregional and sectorial levels inside the mark of the National Plan of Development.

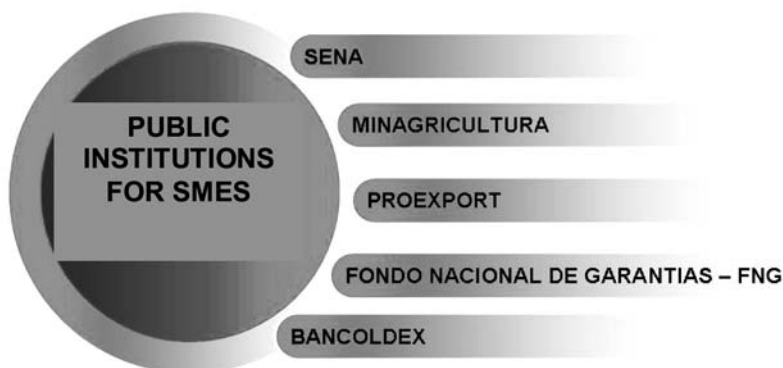
The superior advice of the SMEs should also propitiate the conformation of Regional Council for the development of the Micro, small and medium companies and for the promotion of projects and managerial investments, to stimulate the development of the managerial organizations, the associativeness and the strategic alliances among the public and private entities of support to this sector and to promote the agreement, with Mayors and Governors, of integral plans of support to the Small and Medium Company, mainly.

It is important to highlight like besides officeholders, this law grants in its composition recognition to the union participation, pointing out expressly which unions and it designates its presidents like members. This way, they are members of the Superior Council of Small and Medium Company: The minister, or vice minister in their defect, of Trade, Industry and Tourism, Agriculture, working and Social Security or in their defect the General Director of the SENA, that of Environment, the Director of the *DNP, a representative of the Universities, the National President of the Colombian Association of the Micro, Small and Medium Enterprises - ACOPI -, the National President of the Federation of Merchants - FENALCO -, the President of the Colombian Confederation of Chambers of Trade - CONFECAMARAS, in representative of the dedicated *ONG'S to the technological research and development of the small and medium companies, one representative of the Regional Councils of Micro, small and Medium Company, designated by the same Councils, a representative of the mayors of those municipalities in which is in operation a plan of integral development of the small and medium companies, designated by the Colombian Federation of Municipalities

Regarding the instances of decision, the definition functions, formulation and execution of politicians are centralized in the Ministry, entity that makes the Technical Secretary of the Superior Councils. The Superior and regional Councils contribute, support, offer, advise, foment, propitiate, promote and articulate. The specialized dependences of attention guarantee the materiality of the stocks, and they surrender annual reports. They also make part of this

new structure directed to the SMES specialized dependences of attention to micro enterprises in each one of the public entities that conform the Superior, more other Councils six, in *IFI, *FNG, SENA, *Colciencias, *Bancoldex, *Proexport.

Public Institutions for SMEs



Regarding the policy instruments, the most important in the law is the creation of the Colombian Fund of Modernization and Technological Development of the Micro, Small and Medium Enterprises - *FOMIPYME - with a contribution of 10 million dollars per annum during 10 years. Their object is the financing of the projects, programs, technological development and the creation of instruments for its development and promotion. Additionally it was created The Fund of Investments of the Risk capital of the Micro, Small and Medium Enterprises "EMPRENDER". The Managerial Unique Registration is also among the instruments contributed by this law, to reduce steps before the State.

Other instruments are the explicit preference in favor of the small and medium companies in the state purchases, on the base that equality of price conditions, quality and supply capacity exist in the offer of such goods and services; also the command of making pursuit and evaluation, besides the orientation.

Additionally, the SME Law establishes tax incentives for the creation of small and medium enterprises, so that the State authorizes to the territorial entities to

establish special taxes (periods of exclusion, inferior rates, etc.), established parafiscal incentives for the creation of SMES, reduced the contributions (SENA, *ICBF and compensatory Funds) during the first three years of operation of these company, created the environment so that the financial entities and the NGO, specialized in micro enterprise credit, direct their resources to this segment.

On the other hand, the Banking Supervision Office "Superbancaria" establishes the micro-credit modality. In this mark the promotion of the organization of local and national fairs also settled down to energize markets in benefit of the SMEs, of tributary stimuli to the creation of companies, and in general, the promotion to the access to financial markets.

An important Private Institution for the SMES in Colombia is the "CINSET" Corporación para la Investigación Socioeconómica y Tecnológica de Colombia. CINSET is an organization without profit motive in mind, founded in 1987, executes projects in environmental, social, economic and technological areas for the promotion of micro, small and medium enterprises, fundamental element of the economic activity. Its purpose is to promote sustainable human development within the criteria of Social and Ecological Economics emphasizing in micro, small and medium enterprises (MIPYME). Besides, CINSET works as a research, training and technical support center, specialized in holistic promotion of MIPYME, the sustainable development and the models of local and regional development within a prospect of the Social and Ecological Market Economics. Offers national and international consulting services, conforms inter-institutional alliances and develops projects with governmental, private and multilateral sponsors.

CINSET's principal action outlines are:

- Identification and consolidation of mini-supply chains all around the country regions. Guidelines formulation of competitiveness and productivity policies for mini-supply chains at a regional level.
- Identification of regional and sector opportunities for enterprises creation and development of business plans. Training and sensitizing of the marginal, reinserted and displaced population on business opportunities.

- Design of associative strategies, oriented to generate collective developments to increase MIPYME productivity.
- Execution of Cleaner Production Programs (PML), guidelines formulation to national policies, environmental management, contamination prevention, minimization and assessment of wastes, improvement of productivity and competitiveness, addressed to manufacture, agro-industry and services MIPYME.
- Development of socio-economics studies and Action Plans in specific regions and for the various entities of the country.
- Support to enterprises on professional risks topics, implementation of the basic assisted health care program.

This way, the institutional politics of support to the SMEs leads to an institutional synergy, of resources, norms and procedures, in order to strengthen, to develop and to articulate the sector of the micro, small and medium enterprises in Colombia.

Finally, it is important to settle down in a punctual way the entities that make part of the National System of Support and Promotion of the SMEs, which help to the managerial sector in a different way and in many occasions in a combined way:

Financial Private Entities

- Banks
- Financial NGO
- Cooperative
- Compensatory Funds

Non-Financial Private Entities

- Gremial Organizations: ACOPI, FENALCO, sectorial Unions
- NOGS of support to the micro enterprise. Carvajal Foundation, Compartir Foundation, Micro enterprises of Antioquia.

- Investigation Centers and NGO of support to the SME
- Chambers of Commerce
- Centers of Managerial Development
- Universities
- CINSET
- Entities of the Solidary Sector

Financial Public Entities

- BANCOLDEX
- FINAGRO
- Financial entities, trustees and of *leasing
- Covenants of title: National Fund of Covenants of title, *FAG

Non-Financial Public Entities

- Vice-ministry of Managerial Development
- SMES Direction.
- Competitiveness and Productivity Direction
- Vice-ministry of Foreign commerce
- Business Dealings Direction
- Net of Technological Development Centers
- SENA
- Proexport
- Colciencias

Private Entities

- *ACOPI
- *ACICAM
- *CORFOMEX
- *CONAMIC
- Corporation for the Development of the Micro-enterprises -CDM
- *FEDESMERALDAS
- *FUNDES
- *ICONTEC
- *BANCOLDEX

- Incubators of Companies
- Centers of Regional Technological-Productive Development

Implementation and results of the principal public policies directed at the sector of SMEs.

The public policy directed to the strengthening and development of the micro, small and medium company in Colombia, is based on the determination of this segment, the strengthening of her entrepreneurship: productive, of management, technological and innovative, and finally the internationalization of the managerial Colombian sector.

This policy consists mainly of two components: The first has a financial component and the second has not a financial component. The last one seeks to help, to promote and to strengthen the SMEs across programs, projects and actions directed to improve their position on the market.

Their principal pillars of work are: programs in marketing, governmental contracts, subcontracting, mini - productive chains, national program for the design industry, access to internal and external market, Suppliers' development, management in technological parks, FOMIPYME, Capital fund of risk, and the Innovation prize.

The **Program of Commercialization** seeks to generate spaces of marketing for the micro-businessmen of massive products by means of associative options to optimize elements of management, production and marketing to recover space in domestic and international markets.

This implementation had been done in diverse regions of the country; this program had achieved to receive 2,400 SMEs until 2005, the subscription of agreements with big surfaces markets and the accomplishment of 8 business rounds. Hereby, the Department across this program has achieved to generate 20 regional projects of marketing.

On the other hand, **The Program of State Buys** is important as part of the Policy of Support to SMEs in order for the State to facilitate offer spaces of this managerial segment and it receives benefit with its products and services. The government wants to develop SMEs competitiveness and productivity principally in some sectors like metal mechanic, electrically, electronic and industrial services, facilitating to them the access to Buys States because they can improve their position in the domestic and international markets, integrating public and private sector.

The actions of this program, for example, during the year 2004 was the implementation this program in 5 State Entities, where they benefited more than 150 SMEs. Also, an agreement was formalized with ECOPETROL and SENA for access licitation formation and buys state processes as establish of contracts with SMEs of the whole country. These actions gave continuity to the Indumil development program of Suppliers as well it granted besides active participation in the project Cluster of the energetic sector CIDET-MEDELLIN, and it developed the project BID-FOMIN-Fomipyme⁴ with ACOPI.

The Subcontracting Program deigns for SMEs has as objective to promote links between the offer and the demand of goods, services, productive process and technology of the productive chains. Among their aims also it wants to generate strategic and technological alliances of mutual benefit between big companies and SMES in order to improve their productivity and competitiveness, to offer business opportunities for the production of parts, pieces, components, Intermediate subsets, services and technology and to spread information about the demand, the regional and national offer, across the Colombian Net of Centers of Subcontracting.

Between their principal actions are to realize more than 50 Suppliers' Lounges and Fairs, the subcontracting with 20 big companies in order to benefit 400 SMES. Likewise, it subscribes and developes an agreement with the SENA for the support and managerial strengthening. Also it has been established and agreement with COLCIENCIAS where this entity gives some programs support of suppliers' development⁵.

On the other hand, with the intention of reaching the goals established by the current Government in the National Plan of Development 1998 - 2002, PROEXPORT AND ACOPI agreed to realize the Program **EXPOPYME**.

EXPOPYME is a program directed to promoting Colombian PYMES' adjustment to the requirements of the world economy (globalization, competitiveness and opening on the outside). It is a result of conciliation between the gremial organization, the public and private sector and the academy.

The results of this promotion policy of exports have been visible. In 1999 the medians and small enterprises linked to Expopyme exported 48.9 million dollars, in the 2000 these exports increased in 37% until 67.1 millions. But the best achievement is that the tendency continues and in the first semester of 2001, 319 companies of the Program they have exported 46.2 million dollars.

In the period included between January and September 2001, more than the half of the not traditional exports were realized by companies attended by Proexport, due to destinations in this period the 7.486 millions of weight for investment for this entity. Expopyme has linked 1.680 small and medium companies, of which 1.070 designed his plan of exportation. 417 of the evaluated companies invoiced 49 million dollars in 1999, number that ascended to 46 millions in the first semester of 2001. For 2002, Proexport linked 250 small and medium companies; the coverage of the program was extended to 1.930 industrial establishments⁶.

The Program of Development of Productive Mini-chains principally aims to consolidate and project the economics regional activities, which answer to a natural vocation, generating a positive impact on the growth and inversely on the poverty, across strategies of association and solidarity, constructing the conditions of social equity and economic stability, generating mutual benefits to the productions groups.

Between the principal actions is the accompaniment of almost 50 mini-chains across workshops of methodological induction, diagnosis and proposition of solutions. Likewise, it has achieved the promotion and development of marketing activities and the support to 40 new mini-chains⁷.

PROJECTS OF PRODUCTIVE MINICHAINS ADVANCED IN THE COSTA ATLANTICA REGION

Departments	Socio-productive Mini-chains	Number of Benefits
Atlántico	Handcrafted and productive fishing	31 Micro - companies
Bolivary Sucre	Tejidosy Hamacas	300 craftsmen
Cesar	Lacteal	400 producers
Cesary Magdalena	Palm Esterea	100 Craftswomen
Córdobay Sucre	Caña Flecha	409 Indigenous craftsmen
Guajira	Chinchorros	200 Indigenous craftsmen
San Andrésy Providencia	Inputs and services to the Tourism Industry	16 micro - companies

The National Program of Design for Industry is a tool designed by the State because it wants to integrate PYMES to the new schemes of innovation and development, implementing integral strategies of Design in his productive networks and marketing. Some of these activities are the promotion and execution of the design projects, this Program has 200 SMEs beneficiaries, of the Metal mechanic sector, Textile - Confection, Leather - Footwear and Furniture - Wood.

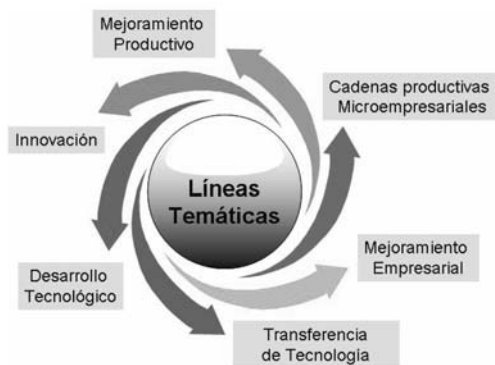
Also, The Department searches for ways to stimulate the new creations of SMEs across the motivation and recognition of his companies. For this reason, the Department created the **Prize to the Technological and Managerial Innovation INNOVA**, this figure born to foment innovative culture and technological development. It wants recognize the talent, the hardworking investigations and managerial innovative attitudes of the PYMES.

The Strategic Orientation of this program is constituted basically by the benefits that receive the winning companies, established in the decree 1780 of 2003: it gives support to receive national and international technical assistance, International specializing training, supports for the national and international participation in events of innovation and strategic commercial management.

For the development of this program exists an active inter-institutional participation, across Sponsoring Members, as the National Federation of Coffee growers, Associate Members like ACOPI, The Externado de Colombia University, The National University and the Chamber of Trade and Institutional Members (ANDI, ACICAM, Quality Corporation, etc.), all of these organizations are under direction of the Department of Trade and FOMIPYME. With this structure, the Program search to unite efforts to support the formation of human talent, the automation and standardization of processes and the access to technological specializing services.

The results obtained with the Prize INNOVA indicate for 2004 a whole of 222 postulated companies, 18 of these enterprises were the winners; in 2005, 117 companies were postulated and in 2006, 224 companies are postulated.

However, In spite of the development of these programs like contribution to the growth of the MIPYME in Colombia, the "**Colombian Fund of Modernization and Technological Development of the Micro, Small and Medium Companies - FOMIPYME**" is the principal instrument of policy of the law MIPYME. It has \$20 billion per year and these resources come from the National budget and its objective is the funding of projects, programs and activities for the technological development of the PYMES.



The items that are financed in the projects promoted by FOMIPYME are: training, advising and technical assistance, national and international experts, internships, technological missions and participation in events of national and

international training, specializing studies, design and development of specializing software, of equipments of production, of new products and of processes that include technological innovation, participation in fairs and in commercial national and international events, patents, license and records, normalization and certification.

In 2004, after four years of vigor of the Law, the Government realized fiscal contributions for approximately \$26,190,477 millions that have activated the Fund, which is controlled and directed by the Department of the Foreign Trade, Industry and Tourism. According to information of the Department of Trade, Industry and Tourism, exposed in 2004, it had executed to the date resources for \$7.620 in SMEs of direct and indirect exporters. Also FOMIPYME developed the Inter-institutional Agreement between the Department and the SENA to increase the co-financing projects of innovation and technological development⁸.

	Approved Offers	Resources Approved
SME	40	1.114
Micro	280	47.326
Total Approved Cofinancing	320	58.470

On the other hand, it is important to emphasize that besides the policy of promotion, the laws 590 of 2000 and 905 of 2004 establish benefits for creation of micro, small and medium companies. These allow a reduction in the parafiscal contributions for the first three years counted from the date of operation if these companies do the requirements of constitution and installation. About this form, the SMEs that assemble the requirements of this law and want to take their benefits, these must report in writing to the Box and present photocopy of the brief presented to the DIAN for the installation of the company.

This review of the principal institutional instruments of the public policy directed to the sector MIPYME from the Law 590, it allows emphasizing an active role of the State in the support of the activities directed to the sector in

the orientation and joint between the actors of the sector.

Nevertheless, with the expedition of the Law 590, the participation of the not governmental organizations in the design and monitoring of programs and policies specifics is relatively limited. The not governmental institutions don't have a lot of influence in policies. It is reflected in small influence in different social actors on the decisions of the SMEs' policies, in all their levels of action and depending on collective interests.

Additional, the MIPYME law or 905 law of 2004, they don't generate mechanisms to endorse or to foment the development of the micro-companies in Colombia. In fact, this law increases instances, offices, steps and reports from the creation of the advices for the micro-company. On the other hand, from the 590 law of 2000, it has been reduced legitimacy to the traditionally organizations were coming resting to the micro-companies with programs of training.

Example of this is Corpomixta's case, which was the instance from 1994 until 1998 created as the program of technological services for the micro-company, it is entrusted of evaluating the projects that micro-companies present to compete for the resources of the Fund for the Modernization and Technological Development of the Micro, Small and Medium Companies, Fomipyme. Initially, this corporation had in its account 60 billion of pesos to operate and finally it remained without budget.

The 590 law of 2000 and the 905 law of 2004 constitute a setback in the development of regulation of the public legitimacy SME and in the relations between the State and the civil Colombian society in his to gesticulate in favor of the development of this wide and strategic sector shaped by the micro - companies, the small and the medium companies.

Hereby, to solve these deficiencies, it is not enough promulgate another law, though it is private initiative. It is important to restructure the legal frame where the principal actors of the sectorial dynamics can include their consensus, and that allows to establish the basic agreements of an interinstitutional scheme of work between the public and private sector for the PYMES development. This coordination and conciliation will be able to join

efforts and to use the resources efficiently. Also, it will be able to extend the coverage and quality of the existing programs⁹.

The component of financial support of the Public Policy orientated to the Colombian SMEs search to increase the credit resources collocation and the capitalization development. The Colombian Government has been searching the consecution about this objective across the subscription of agreements between the Commercial Banking and the Department of Trade, Industry and Tourism and between Banks and NGOs. Likewise Bancoldex has designed strategies and policies that facilitate to the sector SME access to extending credits as the National found of Guarantees, which offers automatic guarantee for micro-companies in alliance with the territorial entities and financial institutions.

In this way, the Agreement signed with the Commercial Banking for 2004 had been achieved the disbursement of 388.954 credits that are equivalent to 858.845 million pesos¹⁰:

AGREEMENT BANKING - DEPARTMENT OF CIT			
	First Year (September 2002 - August 2003)	Second Year (September 2003 - March 2004)	Total
Disbursements (Million of Pesos)	\$489.090	\$369.755	\$858.845
Number of Credits	189.660	199.295	388.954

Likewise, the balance of this policy for 2004 shows that it was achieved a total disbursement of 763.657 million pesos across direct credits to micro companies and an amount of 105.188 million pesos for credit concept across NGOs. Finally, Bancoldex increased significantly his participation as credit supplier for the sector:

Additional, like complement of this politics of State, the banking of the country has overturned towards the SMEs. According to the results of Asobancaria's survey in October, 2005, 90% of the banks have a specializing SMEs` area. 5 Years ago only 40% of banks had it, this is a result of a process

that it has began since 2001, when the banks started separating the segment SME of the corporate segment. From 2002, the bank has started to separate the credit analyze to the corporative SME segment¹¹, with flexibilisation for the sector. For this reason, the bank sector has developed products and services directed to the SMEs.

However, one barrier that continues preventing the growth and develops of the managerial sector of the small and medium Colombian companies is the difficulty of financing their needs, principally the work capital. Besides, the country has lacked traditionally culture of risk capital because the difficulties to finance business in improvement and growth. Also, the government does not have organisms that concentrate the development of innovative projects wish give to the PYMES the risk capital and technical assistance that they need for their growth.

Institutional Infrastructure in Favour the SMEs: It is a Sufficient Tool for the Sector ?

THE INTERNAL SMEs AGENDA¹²: AN OFFER OF ECONOMIC TERRITORIAL AND SECTORIAL DEVELOPMENT.

The managerial policies are not born of the governmental initiative. It is a fundamental role of the economic and social actors incorporate alternatives and offers that give solutions to their needs. Hereby, the Colombian Association of the Micro, Small and Medium Companies close to the Consejo Gremial Nacional has been constituted in an actor who tries to highlight the interest of the private managerial sector, contributing initiatives for the strengthening of the MIPYME in Colombia.

The last year, the Private Sector Colombia agglutinated in the Consejo Gremial Nacional extended CGN-CAT gave to the Government and the public opinion a compendium of offers called "Intern Agenda SME". This was a result of the private preoccupation with Free Trade Agreement. The document tries to adopt some public policies decisions and programs that wish to be include in the Internal Agenda.

For the production of this offers compendium, the gremial institutions that integrate the Consejo Gremial Nacional Extended CGN-CAT had participated and dialogued about the document. The coordination was realized by ACOPI, Dr. Luis Gustavo Florez, coordinator the Intern Agenda of CGN - CAT, has been done the control of these meetings.

The document has 10 strategies for the improvement the SME competitive prospectus. These have topics related to the effective internationalization of the sector, the productivity elevation and the answers of the internal market needs; it integrates Regional bets for the productive diversification of the SME, these offers are agree with the DNP methodology.

It is appropriated to indicate that the document concentrates the propositions for the competitive improvement from the perspective SME and it does not try to be a document of Industrial and Productive Policy because it tries to incorporate topics like institutional reform, frame regulatory, fiscal policies, monetary and exchange, sciences strategy, innovation and technology, Pluri - Regional associations, infrastructure endowment and general policies about human talent and labour development.

The formulations of strategies need financial support of the general resources that integrate the financial component of the Internal Agenda, managerial contributions, resources of the international cooperation and the revenues assigned to the sector across instruments as FOMIPYME, the FNG, BANCOLDEX and PROEXPORT.

10 Strategies to Strengthen the PYMES

1. *Strengthening of the PYME* for the best exercise of the Exterior Trade. It is a strategy that tries to strengthen the Exterior Trade System existing in Colombia, the creation of special services of managerial sector advising and formation of new negotiators in all areas.
2. *Construction of statistical information for the segment SME.* With this strategy it proposes the construction of statistical information about the

sector because the country has not a system of information about this managerial group. It is not certainty the number of SMEs that it operates in Colombia. Also, the number of SMEs that it agglutinates in the locally and regionally orders. In addition, the financial and countable information of the sector is limited and offers high degree of imprecision. Likewise, across this strategy it wants to strengthen and to give continuity to the SME Observatory, the DANE work, ACOPI and the EAN University.

3. Development of a policy activates in favour of the segment SME, across the unions, Buys State and programs of suppliers' development. The strategy proposes suppliers' development and industrial desegregation of projects, in big projects of investment on the Costa Atlantica, Antioquia and Valle del Cauca, emphatically in energetically sectors, systems of road communication and public transport. Also it is important the strengthening of platforms specializing in remanufacture in Colombia, the SME segment across the Buys State.
4. Programs for the technologic development and innovation, restructuring and transfer of technology to the SME segment. Between actions to propose in this strategy are the implementation of Assistance Nuclei Sectorial Technique - NATS -, wish agglutinated National and International Services offer.
This strategy is organized and qualified to give assistance to the SMEs for sectors and regions; Identification of the technological condition of the SME in the principal segments and incentives for technology investment. The principal formulation that is done in this point is the creation of an institutional scene to achieve the Strategic Plan of Science, Technology and Innovation. This articulates national systems of innovation and vocational training.
5. Competition promotion and control of restrictive practices. It wants to create a Monitoring Unite about restrictive practices and behaviours intra and inter sectorial.
6. Managerial formation in exterior trade.
7. Exporting initiation in the segment SME - diversification of the exportable

offer, and entrepreneurs' development.

8. Credit access, financial deepening and innovation in credit instruments for the SME.

9. Sustainable development in SME.

10. Social responsibility and the SME commitment with the goals of the millennium.

The Regional goals that the Internal Agenda proposes are: the Santanderes integration with the Venezuelan economy, the South West integration with the Andean Pacific Ocean, the South West integration with the Pacific Basin, the managerial integration in Cartagena, the joint of Mamonal's region with the Forest and the SME, regional Development integrated with the SMEs' unions.

The development of minichains between the Littoral and the North Colombian Region, the productive Integration of the agro-manufacturer SME in the Cundiboyacense region, the SME suppliers' development for the Mining industry in Cundinamarca, Strengthening of the ecotourism, the sequences and the mini productive chains between Risaralda, Caldas and Quindio.

Additional there appears the associative managerial development in this Region, the development and joint of the MISME in the Piedemonte Llanero; the identification of new mini productive chains, the development of supplier groups for the petroleum sector in this region, Associative Local development in the SME antioquena; qualification of the exportable offer in Antioquia, and finally the integration, and new models of relacionamiento between.

This private initiative tries to contribute to the National government and the National Department of Planning with the Internal Agenda construction, this initiative constitutes an exercise that reflects the commitment of the principal social and economic actors of the country with the processes of economic incorporation, the increasing introduction of an economic democratic order and with social and environmental responsibilities, across strategies focused to the SMEs.

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The Policy Environment for Promoting SMEs in Japan

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Introduction: The Context of SME Development in Japan

In Japan, the significance of small and medium enterprises (SMEs) is widely recognized. SMEs have been performing multi-layered functions for the Japanese economy. First, SMEs contribute heavily to economic activities and growth of a country. Second, SMEs create many employment and income generating opportunities in society. Table 1 shows that SMEs in Japan contribute to over 99 per cent of all business and more than 70 per cent of all employees. In particular, smaller-scale enterprises have provided job opportunities especially for women and elderly who have been excluded from economic activities. Thus, SMEs play a major role in the creation of employment opportunities in Japan. Additionally, SMEs exceed large enterprises in annual value added as a foundation of Japanese industry.

Table 1: Situations of SMEs in Japan

	SMEs	Large-scale Enterprises	Total
Number of Enterprises (private, non-primary industry, 2004)	4,326,342 (99.7%)	11,793 (0.3%)	4,338,135 (100%)
Number of Employees (private, non-primary industry, 2004)	28,086,554 (71.0%)	11,466,209 (29.0%)	39,552,763 (100%)
Value of Shipments (manufacturing industry, 2004)	144,056 (billion) (50.7%)	140,115 (billion) (49.3%)	284,171 (billion) (100%)
Equipment Investments (manufacturing industry, 2004)	3,834 (billion) (37.1%)	6,503 (billion) (62.9%)	10,337 (billion) (100%)
Added Value (manufacturing industry, 2004)	57, 513 (billion) (56.6%)	44,163 (billion) (43.4%)	101,677 (billion) (100%)

Sources: White Paper on SMEs in Japan.

Third, SMEs and venture enterprises are considered as a source of dynamism for economic activities in Japan. SMEs have been creating value in Japan. Fourth, SMEs are key actors in local economic development. It can be easily understood that SMEs form the foundations of the Japanese economy and that substantial (re)vitalization of the Japanese economy is impossible without the (re)vitalization of SMEs. SMEs are expected to become the main actor not only in the local economy but also in the local society.

The business environment for SMEs has been changing dramatically during the past five decades. Government policy to support SMEs has also been forced to change. A summary of SME development policy is presented here, after considering how the policy has changed. Supportive programmes for SMEs undertaken by the local government are also discussed in the case of Nagoya City, where its evolving economy is given attention.

Definition of SMEs

There are several discussions on definition of SMEs. In Japan, SMEs are defined under the SME Basic Law. According to the 1999 SME Basic Law, the definition is based on quantitative considerations such as capital size and the number of employees (see Table 2). Much attention has been given to the

growing number of innovative and entrepreneurial venture enterprises, which pioneer and create new markets in Japan. In most cases, the venture enterprise is an SME and has a high potential for growth in Japan.

Table 2: Definition of SMEs

Industries	Capital Size (in million)	Number of Employees
Manufacturing and Others	300 or less	300 or less
Wholesale	100 or less	100 or less
Retail	50 or less	50 or less
Services	50 or less	100 or less

History of the Policy Environment for Promoting SMEs in Japan

SMEs were gradually recognized as a very important actor in the Japanese economy from the time Japan entered its rapid economic growth period in the 1960s. However, there were great differences in productivity and salary levels of employees between SMEs and large enterprises at that time. Modernization led to SMEs being left behind in adjusting to the new economic environment. The SME Basic Law was enacted in July 1963 as a basic legal framework to solve the problems which SMEs were facing. Supportive policies based on the trends and the surrounding environment for promoting SMEs were improved as part of national policy. The main objective of supportive policies at that time was to help SMEs as vulnerable entities, with programmes such as modernizing equipment, financing, ensuring management efficiency and training among others. Since then, programmes which support SME have been implemented according to the economic and social changes in the environment surrounding SMEs', such as, diversification of people's needs, rapid technical innovation, and development of tertiary industries. The programme included development of new products by design and technical innovation, aggressive promotion of trade and foreign investment, and so on.

Another important supportive policy was encouraging SMEs to organize themselves to facilitate economies of scale. The SMEs Cooperatives Act was enacted in 1949. Since then, cooperatives SMEs have been encouraged to take

advantage of opportunities in economic activities. In short, the establishment of cooperatives was promoted through government initiatives. Many cooperatives were established nationwide. The government intended to support SMEs indirectly through cooperatives enabling mutual aid among members. Local industries as well as traditional industries have also been promoted and supported through a group of local SMEs. In 1963, there were 23,851 business cooperatives in Japan. The number of cooperatives has increased during the following decades. They expanded their activities based on members' mutual cooperation. Their activities included joint purchase of resources, joint sales of products, provision of loans, welfare programmes, etc. The establishment of joint rules and advocacy activities were also vigorously implemented to improve SMEs' social status.

Systematization of SMEs through initiatives of large enterprises also took place during Japan's period of rapid economic growth. A pyramid structure of businesses was formed in the manufacturing process, especially in the manufacturing industries such as automobiles, machine tools, and textiles. The subcontractors formed the bottom of the pyramid with a large enterprise at the top. More than 60 per cent of SMEs in manufacturing industries were subcontractors in the 1980s, securing their positions by maintaining good relations with parent enterprise. However, in reality, subcontracting SMEs have been affected when parent enterprises faced difficulties, such as during oil crises, depressions and overseas expansion caused by a weakening Japanese yen. This structure has declined gradually as Japan became a mature economy undergoing rapid technical innovation. The number of business cooperatives steadily decreased since attaining a peak of 46,802 associations recorded in 1983. The system encouraging mutual assistance among SME as well as the system of subcontracting for parent enterprises had to change. SMEs are now expected to tackle the challenges of new business development and reorganization using their creativity and mobility, rather than pursuing economies of scale.

In the 1990s, there emerged recognition of SMEs as not just vulnerable entities in a dual structure composed of large and small enterprises, but also, as playing an important role in innovation, as the source of the Japanese economy's vitality and dynamism. In December 1999, the SME Basic Law underwent its first radical overhaul in 36 years, expanding the range of SMEs

eligible for support measures and enhancing support for start-ups and SMEs engaging in business innovation. The policy of SME systematization was also changed to include the idea of partnerships to promote the sharing of business resources, by organizing cooperatives not only among SMEs in the same industries but also among SMEs in different industries as well as with voluntary groups. In general, the policy framework supporting has shifted from uniform support through cooperatives to intensive encouragement of individual and constructive SMEs. SMEs can be empowered to develop of new technology through exchange programmes with different businesses and partnerships among industry, academia, and government. The substantial amendment of the SME Basic Law was a turning point that transformed SMEs into driving forces of the economy, instead of being an object of protection. However, the policy changes were meant to concentrate limited resources (in particular, budget) on SMEs while leaning out the smaller and weaker entities which form the majority of the industry at the same time. But this has resulted in widening the disparities among enterprises.

Next, we will examine the overseas expansion by SMEs. Since the beginning of the 1990s, the collapse of the bubble economy and the ensuing prolonged slump forced Japanese enterprises to further cut costs, accelerating the transfer of production operations overseas among large enterprises in particular. This changing business environment confronted some SMEs with the perilous decline of business within Japan, forcing them to decide for themselves whether to expand overseas. This process is still ongoing. Large enterprises are developing end-to-end production systems in East Asia that allow everything from development to parts procurement and production of consumer goods to be performed locally. They have increased the production of parts and materials sourced from within the host country or region in order to cut procurement costs. Due also to the growth of local manufactures of finished products, demand is growing for parts and machinery throughout East Asia. As a result of these changes, the establishment of operations in East Asia has become a necessary part of the growth strategies of SMEs as well. Private trading enterprises and financial institutions, as well as governmental organizations such as the Japan External Trade Organization (JETRO) and the Organization for SMEs and Regional Innovation, Japan (SMRJ) provide many supportive programmes for SMEs to expand overseas investment and trade.

In reality, there has also emerged a new recognition of the growing number of SMEs. In the 1970s, the main issue surrounding SMEs was that there were too many very small enterprises. However, the main issue today is the declining number of new business of start-ups since 1990s. According to the SME white paper, approximately 170,000 enterprises per year were established from 2001 to 2004, but approximately 290,000 enterprises per year were unable to continue operating. As a result, supporting programmes for new business start-ups were provided aggressively not only by the government but also by private companies. To assist those intending to start a new business in acquiring the necessary practical abilities, numerous classes and seminars were held, and incubation facilities have been increased rapidly. Public financing measures have also been maintained by many local governments. There are many business consultants and NPOs providing supportive programmes for new business start-ups. It can be said that supporting business start-ups itself has become new industry.

In 2002, legislation, including the Law for Facilitating the Creation of New Businesses, was amended under the Law for the Support of SME Challenges to allow exemptions from the minimum capital requirements for corporations (dubbed the "One Yen Start-up System") in order to provide support for start-ups and new SME business ventures. The Law on Supporting Business Innovation by SMEs was revised in 2005 in order to establish the Law for Facilitating New Business Activities of SMEs, and support for "new partnerships" undertaken by business in different fields as a means of effectively combining their respective business resources was initiated. Meeting challenges to the new business through SME partnerships, and supportive measures for their efforts, are very important for revitalization of the local economy. The measures to revitalize the SME sector carried out in 2006 by the Ministry of Economy, Trade and Industry (METI) were in the following five areas comprising the "pillars" of the recovery; 1) supporting manufacturing SMEs in high technology areas, which in turn supports the growth of the manufacturing industry in Japan; 2) securing and developing human resources for SMEs; 3) helping SMEs tackle the challenges of new business development and reorganization; 4) facilitating SME financing; and 5) revitalizing shopping districts and city centres. As Japan enters the era of mass retirement of workers who have contributed to rapid economic growth, METI is encouraging the development of developing human resources for the

next generation and local revitalization. The Regional Resources Utilization and Enterprise Development Programme was established in 2007. METI started to support the development of new products and services fully utilizing local technology and local resources. It is a policy to support the development of local economies, in collaboration with the local government and local SMEs.

With economic globalization, SMEs have been forced to expand their business regardless of their location to survive the competition. However, since traditional business activities utilizing local resources within the locality have been decreasing, the business environment for local economies such as shopping districts has increasingly become more difficult. In addition, social problems affecting the local environment, such as the progressive aging of the population, the collapse of local communities, bullying and abuse of children are taking place. Corporate Social Responsibility (CSR) is also expected to be practiced by every enterprise. In this context, SMEs have come to better appreciate the importance of regenerating the society. For instance, systems combining work and parenting such as in providing maternal leave benefits have not been established in smaller enterprises. However, since smaller enterprises tend to overcome the hurdles by responding flexibly to changing working conditions such as through arranging working hours according to an employee's individual circumstances, the turnover rates for women with children is lower in SME than in large enterprises. There are studies showing that long-term impact on promotion declines as enterprise size decreases (Fujitsu Research Institute, Business Survey Regarding Small Business Support for Balancing Work and Family 2005).

Currently, some SMEs with the same objectives are cooperating and taking the initiative to enhance their competitiveness and attractiveness through local branding. A "local" or "regional" branding strategy is considered as a potential marketing alternative to develop a niche market and achieve global/local competitiveness. Local/regional branding strategies promote excellent products and goods that make the most of each region's distinctiveness through an agreed branding or trademark approach. This strategy strengthens the competitiveness of regional industry by increasing the value of products and enterprises and local/regional brand formation. The brand could relate to the locality or region overall, or be specific to particular product categories,

niches, or modes. The concept of a regional brand involves branding special products or services in the region as well as branding the image of the region, its culture, and history. Thus, the establishment of local/regional brands requires three perspectives: a local/regional perspective, a products perspective, and consumer perspective. Products cannot become competitive without a high value added. Products cannot remain sustainable without gaining the preference and confidence of consumers. Products should reflect ownership of, pride in, and solidarity with the local/regional culture. Products can be marketable with the flavour and vitality of the local/regional characteristics. Good practices can be observed all over the Japan, where local artisans and local owners of SMEs have collaborated and succeeded in the development and sales of new brands. They are making good use of national and local government support programmes, with SMEs initiating and promoting projects. Good practices include the Yamagata Carozzeria Project which has succeeded in creating new products making good use of local traditional technology with the support of well known designs industry from the region, the Textile Bishu Brand that was created through the collaboration among textile SMEs facing crises in the Owari region, the Arimatsu Brand of new fashion created by the traditional tie dyeing craftsmen, among others. In addition to local branding, the significance of design is also to be emphasized all around the world. The design itself triggers the expansion of market channels or development of niche markets.

Furthermore, community business has increasingly become the focus of attention as an important factor in local economic development. Community business includes business activities aimed at addressing individual, various, and numerous problems which are increasing in the community against the background of the collapse of local society, which are difficult for the government as well as profit-oriented enterprises to address. Community business not only provides working opportunities to vulnerable people such as women and the elderly but it also promotes the revitalization of the local economy, since it promotes business based on social relationships and social capital. However since community businesses operate very small scale, the government has not understood their importance. Community businesses need to prove that they can contribute to the local industry. Japan has a long history of supporting SMEs (supportive measures for SMEs have been an important policy area for elected representatives). Non-Profit Organizations (NPOs) are

increasing as providers of community business, but NPOs are unable to use supportive measures for SMEs in practice. The establishment of effective supportive measures is required for further promotion of community businesses. Local governments have started to examine how they can support community business as in place of the national government, because community businesses are closely connected to local revitalization which is one of the major issues for local governments. Thus, community businesses represent a potential area for SMEs' contributions to the local economy. In fact, according to "the 2004 White Paper on SMEs in Japan," "community businesses are entities mainly formed by local residents in order to respond closely to local problems that cannot be solved within the conventional framework of public administration (the public sector) and private-sector commercial activities. In addition to the goal of contributing to society, a strong emphasis in community businesses is on their continuation as businesses, setting them apart from volunteer organizations." Their main characteristics are that: "(1) the main actors are local residents; (2) they do not have profit maximization as their objective; (3) they provide goods and services to meet the needs of residents and problems of the community; (4) they provide places of work for local residents; (5) they are continuous businesses or entities; and (6) they are independent from local government both financially and in terms of personnel." In reality, locally residents, local-based organizations and SMEs are very active in the area of community business. From this perspective, community business is expected to provide employment opportunities as well as to revitalize the local economy.

Additionally, to enhance the competitiveness of SMEs, the division of labour and advantages of specialization through formation of clusters and linkages among enterprises including SMEs, will be important. Clusters originally means bunches of grapes and is used to mean a group or a gathering. In this context, METI has been promoting the Industrial Cluster Programme since FY2001. The basic idea of the programme is to develop a business environment that facilitates of innovations in respective regions. This programme is a project through which regional SMEs (world-class SMEs) and new venture enterprises take advantage of resources to form industrial concentration (industrial clusters) in the information and communication technology, bio-technology, nano-technology, environment technology, and manufacturing sectors, aiming to strengthen the competitiveness of Japanese

industry. In forming industrial clusters, innovation is the key. Innovation is particularly expected to exert a significant impact on the economy and society through the marketing of competitive products and commodities based on new technologies and ideas.

Legal and Regulatory Framework for Promoting SMEs

As described earlier, in Japan there are several fundamental laws on SME promotion, as well as a relevant policy framework and several supportive policy measures. In addition, governmental institutions were also established.

The SME Agency under the METI is the body that mainly deal with SME-related issues in Japan. The task of the SME Agency is to provide strong support to dynamic and active SMEs with pioneering spirit because they are the driving force behind economic (re)vitalization and job creation. To this end, the Agency will integrate and upgrade existing laws and regulations, and support new partnerships among SMEs, backing them in their efforts to start up new businesses or open up new markets. At the same time, the Agency will continue to upgrade the financial safety net and provide necessary (re)vitalization support to enable SMEs to secure their own space where they can play active roles.

In terms of legal framework, the first SME Basic Law was enacted in 1963 and subsequently revised in 1973, 1983 and 1999. This 1999 amendment relates to the shift of its basic policies from "rectifying disadvantages" to "promoting diverse and vigorous growth and development of independent SMEs." It is recognized that SMEs are not weak entities, but represent a driving force behind a dynamic Japanese economy. According to the 1999 SME Basic Law, the policy concept is to develop and support the growth of a wide range of independent SMEs to promote greater economic vitality. SMEs are highly expected to create new business, to promote market competition, to increase attractive job opportunities, and to revitalize regional and local economy.

Table 3: Comparisons of the SME Basic Law

	The Previous SME Basic Law	1999 SME Basic Law
SME	- A weak entity	- The driving force behind a dynamic economy
Policy Concept	- Rectify the gap between LE and SMEs in terms of productivity	- Develop and support the growth of a wide range of independent SMEs to promote greater economic vitality
Policy Goal	- Promote fewer but larger SMEs - Promote collaboration among SMEs	- Promote self-help efforts of independent SMEs - Promote business innovation
Policy System	- Upgrade structure of SMEs (improving productivity) - Address disadvantages (improving trading conditions) - Finance and taxation (common policy tools)	- Support self-help efforts for business innovation and start-ups (support for ambitions enterprises) - Strengthen management base (enhancement of management Resources) - Facilitate appropriate response of enterprises to abrupt environmental change - Finance and taxation (common measures)

Source: Website of SME Agency.

Table 4: Major SME-related Laws

Name of Law	Originally enacted
Small Business Credit Insurance Law [Act No.264]	1950
Small Business Finance Corporation Law [Act No.138]	1953
SME Financial Assistance Law [Act No.115]	1956
SMEs Association Organization Law [Act No.185]	1957
Law Regarding Mutual Relief for Worker Retirement in SMEs [Act No.160]	1959
SME Basic Law [Act No.154]	1963
SME Support Law [Act No.147]	1963
SME Investment and Promotion Company Law [Act No.101]	1963
Law on Ensuring Government Procurement and Contracts for SMEs [Act No.97]	1966
Law on the Promotion of Subcontracting SMEs [Act No.145]	1970

Table 4: Major SME-related Laws

Name of Law	Originally enacted
Small and Medium Retail Business Promotion Law [Act No.101]	1973
Law for Facilitating New Businesses of SMEs [Act No.18]	1999
Law on Organization for SMEs and Regional Innovation, Japan [Act No.147]	2002
Law concerning the Enhancement of the Fundamental Technologies for SME Creativity (SME Technological Advancement Law) [Act No. 33]	2006

There are two different approaches in promoting SMEs. One approach is to protect the socially disadvantaged SMEs, while the other approach is to encourage SMEs with growth potential leading to national and local economic development. In this context, the policy framework for promoting SMEs is aimed at a) supporting self-help efforts and promoting new business start-ups and business innovation (supporting ambitious enterprises); b) strengthening the management base of SMEs (enhancing management resources); and c) facilitating smooth adaptation to economic and social changes (providing a necessary safety net).

Based on the information on SME policies , supportive policy measures can be summarized as follows.¹

1. FACILITATION OF FUNDING AND ENHANCEMENT OF EQUITY CAPITAL

Difficulty in procuring funds is one of the managerial issues for SMEs, which in most cases private financial institutions find unattractive as loan recipients. As a result, there were not enough funding sources for SMEs. Thus, financial institutions that can provide a stable supply of fixed long-term and low-interest funds to SMEs regardless of fluctuations in the economy were needed in the form of governmental financial institutions. In response to this situation, the State strengthened the functions of governmental financial institutions. To meet above-mentioned needs, financing supports has been provided by the Japan Finance Corporation for Small and Medium Enterprise (JASME), the National Life Finance Corporation (NLFC), the Shoko Chukin Bank and others. In accordance with policy needs at different times, these SME financial institutions also have a role in areas where market mechanisms do not apply,

extending special loans with advantageous conditions such as reduced interest rates and flexible demand for collateral and guarantee.

In addition to this, the credit guarantee system aims to offset the insufficiency of credit and security for SMEs and facilitate funding. The State has developed credit enhancement mechanisms, directed private financial institutions to lend to SMEs, and taken any other necessary measures. System to supplement credit is provided by JASME and Credit Guarantee Corporations (CGCs). Enhancement of capital is undertaken by the Small and Medium Business Investment & Consultation Co. Ltd. (Tokyo, Nagoya, Osaka).

2. SUPPORT FOR BUSINESS START-UPS

The Japanese economy has been increasingly characterized by a diversification of consumer needs, intensification of price competition, and internationalization under a globalizing economy, accompanied by a reverse phenomenon with regard to the ratio of start-ups to business closures, provoking serious concern about stagnation of the country's economic dynamism and vitality.

In such circumstances, active support for start-ups and launching venture businesses are critically required in order to counteract stagnation, revitalize the economy, and create opportunities for employment. It is also expected that SMEs will lead the entire Japanese economy toward economic revitalization through business innovation and managerial improvement.

In this light, to facilitate a smooth start-up and business operations for SMEs starting up businesses, those at the initial stage of business opening, and those that are actively engaged in creative business activities such as the development of new products or services, the State has been providing comprehensive support with respect to funding, human resources, management know-how, information, technology development, etc., according to the level of their development. In addition, the State has been enhancing SME's capacity through training programmes on business start-ups.

In reality, there are several supporting measures: those based on "the Temporary Law concerning Measures for the Promotion of the Creative

Business Activities of SMEs", those based on "the Law for Facilitating the Creation of New Business", support through financing and taxation, support through funding and advise on start-ups, fostering entrepreneurship through organizing meeting and events, strategic utilization of retirees, and support for creative technical development by SMEs.

3. SUPPORT FOR BUSINESS INNOVATION

Business innovation has become important in responding to the diversification of consumer needs, intensification of price competition, advances in Information Technology (IT), and economic globalization. Innovation is aimed at substantive managerial improvement through the development and manufacture of new products, the development and provision of new services, the introduction of new methods and techniques of production and sales, the introduction of new methods and techniques of providing services, and the formulation and implementation of other new business activities. The State broadly supports business innovation in SMEs of all categories that are taking on the challenge of contemporary management issues. For instance, support under "the Law on Supporting Business Innovation of SMEs" and matching human resources for business innovation are provided.

4. STRENGTHENING OF THE MANAGEMENT BASE

Improving the business environment and management system for SMEs is becoming a crucial issue. The State provides SMEs with appropriate advice on solutions to their managerial issues and the smooth acquisition of management resources, attentively responding to their widely diverse needs. The State also takes appropriate measures to contribute to the securing of business resources necessary for reinforcing the business infrastructure of SMEs such as improvement of business methods and development of technologies. In this respect, the SME Agency has utilized three types of SME Support Centres: SME/Venture Business Support Centres, Prefectural SME Support Centres, and Regional SME Support Centres. Additionally, it has appointed private citizens as consultants for overall SME management. The State also encourages exchanges and tie-ups among SMEs, as well as SME business cooperatives in order to facilitate SMEs' complementation of each other's business resources. The State is also promoting industrial agglomeration under

"the Law on Temporary Measures concerning the Activation of Specific SMEs."

5. SUPPORT FOR TECHNOLOGY DEVELOPMENT

In spite of their own views and preferences, SMEs often have difficulties in obtaining by themselves all of the necessary management resources such as technology, funds, and information, and are limited in their approach to human resource development.

In order to overcome such difficulties and limitation and to promote the development of independent and creative SMEs, the State has been providing various types of support, which are as follows: a) active support for the self-help efforts of motivated SMEs in technical innovation; b) reinforcement of production technologies and technical development infrastructure, and promotion of smooth access to and use of management resources such as human resources, technologies, funds and information, which are insufficient in SMEs, and related support measures; c) enhancement of the potential of academia, industry, and government through promotion of collaboration, mutual exchange and education for production technologies and innovation; and d) holding of training workshops and seminars and improvement of the common infrastructure of SMEs to actively use IT and promote business innovation to cope with the IT revolution, which has been rapidly advancing.

6. NECESSARY INFRASTRUCTURE DEVELOPMENT

Finally, for SME promotion, physical infrastructure such as facilities for water supply, electricity, roads, and ports is required. Currently, Information and Communication Technology (ICT) infrastructure is also indispensable for further development. Furthermore, to ensure competitiveness, intellectual property infrastructure for supporting business is a must.

Supporting Programmes for SMEs by Local Government - The Case of Nagoya City

Both the national and local governments have provided various supporting programmes and systems for SMEs. For instance, in Nagoya, the city government established in 1907 a special section of the Commerce and Industry Division, providing supportive measures for SMEs. A cooperative association with various cooperatives in the city as members was established as an initiative of the city government in 1947. An association for shopping districts was also established in 1950. Various programmes to subsidize these cooperatives as well as many kinds of financing programmes for SMEs have been provided. These subsidy programmes have been criticized for wasting a lot of money, but they have been sustained until the present, with their contents having been changed according to the changes of their social roles.

Nagoya is located in the central part of Japan with 2.1 million inhabitants. Greater Nagoya (area within one hour from Nagoya) is an important manufacturing center for the automobile (Toyota is one of its leading company), machine tool, aircraft and aircraft tool industries with a population of more than 11 million. Nagoya is often mentioned in many newspapers and magazines as the most dynamic area in Japan. The GDP of Greater Nagoya has exceeded the GDP of Taiwan. Aichi prefecture, of which Nagoya is the capital ranked first among Japan's cities of shipment of manufactured goods for 28 consecutive years.

SMEs, representing 99 per cent of business establishments in Nagoya, are playing a very important role in the local economy as well as in local society. Various institutions promoting SMEs, including the SMEs Promotion Centre, have been providing many programmes and services for financing, advising, organizing trade fairs, providing information, and assisting SMEs with product development. In addition to municipal support, there are many other supporting programmes provided by the national and prefectural governments as well as by economic organizations such as the Chamber of Commerce and Industry in Nagoya. Overlapping programmes in support of SMEs have the potential to be reorganized effectively through good partnerships among institutions.

The ratio of business closures to start-ups in Nagoya is higher than the Japanese average. To remedy this situation, the city government has put emphasis on supporting programmes to promote the establishment of new business, as well as to attract investment from outside city. SMEs are considered not only as recipients of support, but also as catalysts for the revitalization of local society. Innovative measures are also being carried out such as supporting programmes for start-ups to create new business development in cooperation with the locally revitalizing Machi-zukuri activities.

In Industry Revitalization Plan was established in March 2005 to turn the success of the EXPO Aichi 2005 into a drive to revitalize local industries as well and to further attract enterprises and industries as an international business city. The goal of this plan is to be developed an international business city to support the manufacturing heartland by promoting the establishment of industrial facilities as well as by supporting existing industries with step-up projects for ambitious SMEs. The six focus area are: 1) Manufacturing Technology, developing new products in which advanced technologies are integrated, such as automobiles, airplanes, robots, etc.; 2) Environment & Energy, developing environmentally friendly material such as photo catalysts, fuel cells, biodegradable plastics, etc.; 3) Medical, Welfare & Health, producing nursing care/health equipment through collaboration of the medical and technology industries; 4) Information Technology, application of ITS technology, digital content, information service, etc.; 5) Design & Fashion, industrial design, interior, fashion, etc.; and 6) Business Support Services, Consultancy, recruitment agencies, accountants firms, advertising agencies, etc. The following are major supporting programmes for SMEs provided by the Nagoya city government.

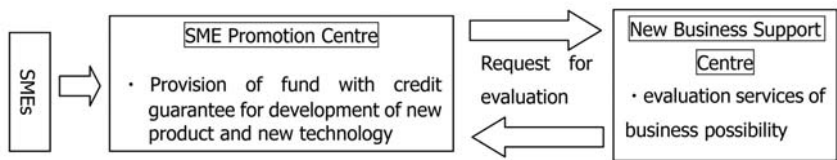
1. STABILIZATION OF BUSINESS AND FINANCING

The Nagoya SME Promotion Centre provides various services for SMEs such as business advisory services provided by lawyers and certified public accountants, as well as specialists in business training, information services and others. The Nagoya City Credit Guarantee Corporation and the Nagoya City Small Business Finance Corporation, organizations which are funded by the city government, also provide various funds and credit guarantees for

SMEs to enable them to access loans from banks without mortgages. Nagoya is a unique city hosting an institution, the Nagoya City Small Business Finance Corporation, which provides funds directly to very small enterprises (5 employees or less for the service industry, 20 or less for the manufacturing industry). The financing programmes include general funds for business operation, funds for the manufacturing industry, and funds for business start-ups , or among others. In providing credit guarantees, the national insurance programme is used, but the budget for financing is huge, accounting for approximately 50 per cent of the budget for industry promotion.

2. HELPING SMEs FACE THE CHALLENGES OF NEW BUSINESS DEVELOPMENT

The Nagoya New Business Support Centre, established within the Nagoya Urban Industries Promotion Corporation, a city government funded institution, provides various services such as advisory services for new business development and business start-ups, feasibility studies, business matching, forums for student ventures, business plan seminars etc. for SMEs. The New Business Support Centre cooperates with institutionalized financing for the challenge of new business in the fields of environment, medical and information technology.



3. PROMOTION OF COLLABORATION AMONG INDUSTRY, ACADEMIA, AND GOVERNMENT

The aim of collaboration is to create new industries. Joint research and forums to exchange opinions with participation of enterprises, universities and research institutes have been organized in the fields of manufacturing technology, environment, medical, welfare & health, and information technology. The "Wooden Biological Mass Electric Power Generation Project", which converts organic waste into high temperature gas, was

developed through the collaborative project and was introduced as a new business at the Aichi EXPO. Exchange programmes such as exhibitions and forums have also been organized to introduce new technology and new products developed by universities and SMEs, with the cooperation of the Aichi prefectural government and the Nagoya Chamber of Commerce and Industry.

4. ORGANIZING INDUSTRIAL EXHIBITIONS

Trade fairs and exhibitions which have multiplier effects on the economy, have been organized or hosted by the international exhibition halls, owned by the city government and business opportunities are provided for SMEs. These include the exhibition of mechatronics equipment, welfare and health equipment and services, and new technology, materials and products of photo catalyst. "Messe Nagoya", the exhibition of environmentally friendly technologies has also been organized with the collaboration of the Chamber of Commerce and Industry.

5. SUPPORTING PROGRAMMES FOR THE EXPANSION OF OVERSEAS INVESTMENT AND TRADE, AND CITY GOVERNMENT PROMOTION OF URBAN INDUSTRIES AND FOREIGN INVESTMENT

An advisory office has been established in Shanghai, China, to support SMEs which are planning to setup offices or factories, as well as to expand the trade in and with China. SMEs which have a head office in Nagoya, can take services such as legal and taxation advice and, business information on China among others. City promotion programmes to encourage investment in Nagoya have been actively undertaken through a set of measures that include provision of subsidies to companies' buildings, factory or research institutes, and setting up office among others. Subsidies for foreign companies setting up offices and factories in Nagoya are also provided.

6. PROMOTION OF DESIGN APPLICATION

Nagoya is proud of its rich tradition in design, having been declared as the "Design City" in 1989. The International Design Centre, Nagoya (idcN) was established and funded by the city, prefecture and the business community.

The idcN has been developed as a center where SMEs can deepen their understanding of design and to make good use of design not only to meet present needs, but also for the development of business strategy. The programme for SMEs includes design consulting, and providing designers to give for advice on new product development, among others.

7. PROMOTION OF THE FUSHIMI CHOJAMACHI VENTURE TOWN CONCEPT

This is a very unique project supporting start-ups of businesses with the collaboration of the local community. The Fushimi-Chojamachi area is located in the centre of downtown between the Nagoya station and the Sakae, shopping areas. This area was developed as one of the big three textile wholesale districts in Japan after World War II. However, since many wholesale businesses have gone bankrupt or closed due to the changes in the production and distribution systems for textile, the district has lost its dynamism and many buildings and shops had to be closed. There was a sense of crisis among local people and wholesalers who feared that the district might become a night entertainment district. Local people started a revitalization project on their own initiative. The city government believed that synergies can be achieved through collaboration with the local population, and so launched the venture town concept as part of the city industry revitalization plan in 2005, aimed at the integration of urban industries such as design, fashion, and digital content within this area. To support the efforts of the local population, the city provides subsidies to repair old vacant buildings and provide small offices for ventures and subsidies for rent among others. At present, approximately 20 ventures (small companies) have started their business in two model buildings which have been opened under this project. 2-3 buildings per year will be repaired and provided for ventures until 2010.

8. DEVELOPING BUSINESS FOR VENTURES BY OPERATING INCUBATION FACILITIES FOR START-UPS

At present, the city operates seven incubation facilities to support ventures in cooperation with associated institutions. The programme, which is provided for tenant companies includes subsidy for rent and advisory services by managers, among others. Each facility has a target business area for tenant

ventures. The target areas include computing software and system development, medical, biotechnology, health, and welfare, and design related SMEs etc. In particular, one unique and original undertaking by the city is the operation of incubation facilities using a former elementary school building which was closed due to depopulation. This facility provides offices for small entities which are willing to start community businesses. A NPO is selected as a manager to provide daily services for tenants. The city also supports the revitalization project for the shopping district by providing opportunities and subsidies for ventures of community businesses to set up offices using vacant spaces in the shopping district.

9) SUPPORTING MANUFACTURING SMEs THAT POSSESS HIGH LEVELS OF TECHNOLOGY, RESEARCH & DEVELOPMENT, AND DEVELOPING HUMAN RESOURCES FOR SMEs

The Nagoya Science Park has been developed to promote research and development in leading industries of the next generation, based on Nagoya's traditional manufacturing industries. Facilities are provided for ventures starting new businesses in cooperation with universities and research institutes. A site for research and development facilities has also been provided. Business structures bridging new technology to local industries, have been organized here. The Nagoya Municipal Industrial Research Institute provides technical support to SMEs in manufacturing industries. The programme includes technical consulting services by institute staff assigned to SMEs, various tests of quality and performance of materials, rent facilities and equipments and commissioned research for SMEs and so on. The institute is also engaged in the development of new technology such as manufacturing technique lightening of automobile parts, and development of new materials such as biodegradable plastics. The city provides subsidies for SMEs to undertake for cooperative research and development of new products in high-technology industries, and subsidies to obtain patents.

10.DEVELOPING HUMAN RESOURCES FOR INDUSTRIES, NAGOYA MONO-ZUKURI (MANUFACTURING) COLLAGE

The mass retirement of baby-boomers has started. Fearing a shortage of workforce as well as of technological expertise and skills, the city supported

OJT (On the Job Training) and in-house programmes to transfer technical expertise and skills to SMEs. Securing and developing human resources for next-generation SMEs in manufacturing industries, supporting programmes such as technical practice at the industrial high school have been provided. The city also encourages students to become interested in the manufacturing sector, and local manufacturing SMEs providing internship programmes for high school and university students. Retired skilled workers are also employed as trainers. At present, 70 retired skilled workers are registered as technical advisers and are providing professional training in the field of plating and plastic. They also organize management training for managers, including those of next-generation of SMEs.

Possibilities of One Village One Product Movement

In promoting SMEs, one of the interesting and integrated policy packages is the "One Village One Product (OVOP)." The OVOP movement was advocated by the then governor of Oita prefecture, Morihiko Hiramatsu, in 1979 as a local revitalization movement when the Japanese economy remained sluggish after the oil crisis that hit the nation in 1973. Around that time people were becoming aware of the negative effects of the period of high economic growth - such as environmental pollution, widening regional disparities, depopulation of rural areas, and the problems of an aging society- and began to seek endogenous forms of regional development. In those days, the Oita prefecture's economy was struggling for a number of reasons: (1) The prefecture was financially dependent on the national government to a great extent and more businesses were moving in while fewer businesses were moving out; (2) The prefecture's economic structure was not well balanced, with only a small number of manufacturers; (3) The prefecture's average level of income was lower than the national average and there were large disparities in revenues among its municipalities; and (4) Lastly, the prefecture had many depopulated areas. Then the oil crisis occurred. Even after exogenous development projects seemed to have reached their limit, local people clung to their dependence on support from external authorities. Thus, the major challenges for Oita Prefecture were: (1) halting the depopulation trend and revitalizing the sluggish economies of rural areas, which resulted from the

concentration of the population in cities; (2) creating new businesses for the revitalization of rural areas by taking advantage of local features; and (3) changing the mentality of local people to relinquish their overdependence on authorities and motivate them to develop a greater sense of self-reliance.

Under these circumstances, Governor Hiramatsu put forward the idea of OVOP, aimed at invigorating Oita, which was suffering from depopulation problems. The OVOP concept required people to take up one product that reflected their pride in their community. Although this movement was a kind of spiritual campaign, it was also intended to revitalize local industries. Mr. Hiramatsu intended that through continuous efforts to develop products that people took pride in and that reflected potential local wisdom and local resources, communities would inspired to achieve a form of self-reliant community development without dependence on central government subsidies or ready - made business solutions from corporations outside the prefecture. Considering that the OVOP concept required people to develop independent ways of thinking, it could be heavily emphasized that its ultimate goal was to foster human resources.

After more than 25 years' experiences and achievements, currently and internationally, OVOP is widely recognized as one of the most responsive strategies of poverty alleviation and local revitalization in developing countries. Japan has recently announced a comprehensive development package, the "Development Initiative for Trade," with a view to promoting the development of developing economies and helping benefit form the multilateral trading system. As part of this initiative, the Government of Japan supports initiating the OVOP movement in developing economies, in particular, those in Asia and Africa.

Conclusions

SMEs from the foundations are considered as a source of Japan's economic dynamism. SMEs have been playing very significant roles in the vitality of the Japanese economy and in social stabilization. The State and local governments have been setting up necessary supporting measures and related institutions

for promoting SME development. Even though major challenges remain for SMEs to adapt to dynamic changes and transformations in the economic and social environment, it should be recognized that with the globalization of the economy, SME promotion utilizing local resources and social networks without heavily depending on national government is very important to achieve long-term sustainable local economic developments.

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SME Innovation Policies in Korea

By Joo-Yong Kim¹

Introduction

GLOBAL ENVIRONMENT SURROUNDING SMEs

The transition to New Economy and knowledge-based economy in the 1990s and early 21st century created an atmosphere that entrepreneurs and SMEs became crucial engines of economic growth. It was conjectured that such trends were brought about various changes in global business environment. These changes include technological changes, increased globalization, employment flexibility, consumer diversity, deregulation, privatization and entrepreneurial activities.

In the past, Korean SMEs have steadily grown as sub-contractors of large enterprises due to their relatively low wages, interrelationship with large companies and market protection. The changes in the global business environment, however, enforced these factors to be complemented and replaced with a new paradigm of SME policies. The merit of low wages is nowadays threatened domestically by the high-cost economic structure. In addition, the Korean SMEs should compete against the emerging Chinese economy and other countries' economy with much lower labor cost. Large enterprises have pursued their viability through global outsourcing, and thus Korean SMEs cannot sustain their business any longer by resorting to the interrelationship with large enterprises only. Free trade agreements in the global economy never allow the Korean economy to be indifferent to its trend and, therefore, the Korean government cannot protect domestic markets for the advantage of SMEs. The recent rapid change in technologies

hardly lets Korean SMEs acquire, innovate and accumulate their own technology capability and capacity. All in all, the Korean SMEs are highly likely to be confronted with severe competition domestically and globally.

The difficulties with which Korean SMEs have been confronted are not easy to overcome. The difficulties may make worse the inherent deficiencies of SMEs. New Acquisition of innovated technologies by SMEs themselves becomes more risky and lengthy. Public and private financing for SMEs may be blocked on account of uncertain market and insufficient collateral. The productivity gap of SMEs may be more widened compared to large enterprises. Accordingly, recruiting skilled and talented workforce remains much harder for SMEs.

Nevertheless, the importance of SMEs cannot be overemphasized to the Korean economy and the level playing field presents challenges and new opportunities to Korean SMEs in competing on the global stage. Recognizing this kind of new paradigm for SMEs, the Korean government has set its policy priority towards SMEs. It has put the SME policy goal on establishing vibrant and creative SMEs as the driving force for economic growth engine and job creation. In other words, the government plays a key role in providing an appropriate environment for SMEs to meet the challenges and make use of the new opportunities.

SME DEFINITION

Korean SMEs were defined when the 'Small and Medium Enterprises Act' was enacted and promulgated in 1966. Following the enactment, the scope of SMEs was changed through 10 revisions. According to the SME Act, SMEs in the area of manufacturing are considered as companies which have less than 300 employees or its capital worth under KRW 8 billion (Refer to the Table 1).

Table 1: Definition of SMEs in Korea (as of Year 2002)

Sector	Scope	
	employees	Capital or sales (KRW Won)
Manufacturing	less than 300	capital worth KRW 8 billion or less
Mining, construction, transportation	less than 300	capital worth KRW 3 billion or less
Large general retail stores		
hotel, computer-related business	less than 300	sales worth KRW 30 billion or less
Seed and seeding production		
Fishing		
Electric, gas and waterworks	less than 200	sales worth KRW 20 billion or less
Assorted services such as tour, warehouse, telecommunication, engineering, medical, film, etc.		
Wholesales, product intermediation, science service, sewage, etc.	less than 100	sales worth KRW 10 billion or less

As of 2004, the number of SMEs in Korea is approximately about 3 million, including 84,000 medium enterprises (with 50~300 employees), 230,000 small enterprises (with 10~50 employees) and 2.68 million micro-enterprises (with less than 10 employees). As the main component of the Korean economy, SMEs represent 99.8% of the entire enterprises (3 million SMEs), and 86.5% of total employment (10.41 million employees). In the process of overcoming the financial crisis from late 1998 to 2004, the number of employees working for large enterprises decreased by 900,000 due to business restructuring, while SMEs created new jobs of approximately 275,000 (Refer to the Table 2). This shows that SMEs have a major role in terms of job creation.

Table 2: Status of SMEs by Year (Unit: Thousands, %)

Classification		1998	2000	2002	2003	2004
Number of businesses	Total	2,629	2,864	2,953	3,004	3,003
	SMEs	2,607	2,854	2,948	2,999	2,999
	Ratio	99.2	99.7	99.8	99.8	99.8
Number of employees	Total	10,177	11,530	11,975	12,041	12,036
	Large	2,519	1,853	1,590	1,567	1,621
	SMEs	7,659	9,677	10,385	10,474	10,415
	Ratio	75.3	83.9	86.7	87.0	86.5

Source: Annual Report on the Business Statistics, Korea National Statistical Office.

Major SME Innovation Policies

Traditional SME policies typically refer to the policies implemented by a ministry or government agency charged with the mandate to promote SMEs. It takes the existing SMEs as exogenous and develops instruments to promote their viability. The Small Business Act of 1953 in USA explicitly mandated the role of the Small Business Administration as "aid, counsel, assist and protect [...] the interests of small business concerns." The SME policy framework in Korea began with governmental efforts to protect SMEs from dominance of large enterprises (Refer to Figure 1). Korea created traditional SME polices in the early 1960s and protected SMEs from large enterprises during the industrial period in the 1970s and 1980s. The turning point was the inauguration of WTO in 1995. Korea shifted its policy focus to autonomy, opening and competition since then.

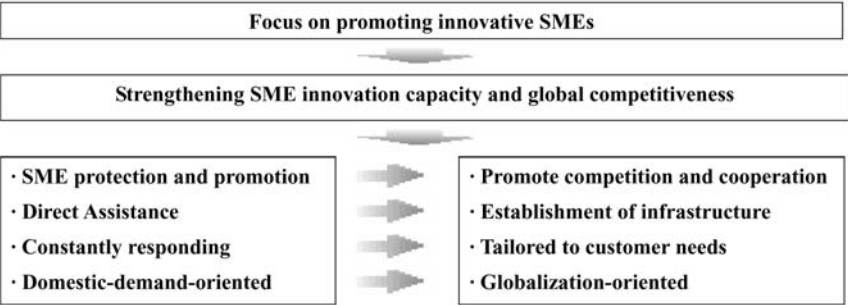
It is well recognized that productivity increases with technological innovation rather than labor and capital investment. It was witnessed with the advent of New Economy, which was influenced by Information and Communication Technology innovation. Innovation has become a new economic growth engine. The business environment is being shifted to an innovation-led economic structure. As such, it is prevalent that a new strategy needs to be established and implemented to ensure that the SME sector should enhance its competitiveness. Against this backdrop, there is an increasing demand to shift the focus of SME policies from the protectionist policy to the policy of increasing SME competitiveness by promoting competition and enhancing technological and management innovation capacity. The Korean government reflected the trend on its SME policy since 2003 as seen in Figure 1.

Figure 1: Transition of SME Policies in Korea

1960s: Created SME Policies · Established a legal framework for assisting and fostering SMEs · Small and Medium Enterprise Association Act('61), Private Contract with SME Associations('65), Basic Act on Small and Medium Enterprises ('66)
1970s - 1980s : Protected and fostering SMEs · Fostered SMEs as a player of supplying parts to the heavy chemical industries · SME-Exclusive Industry('75), Interrelated SMEs to Large Companies('80) · Created Credit Guarantee Fund('76), Small Business Corporation('79), Technology Credit Guarantee fund('89)
1990's: Pursued structural improvement of SMEs · Shifted policy focus to autonomy, opening and competition with the inauguration of WTO (Jan.'95.) · Announced removal of SME-Exclusive Industry('94), Reduced Private Contract with SME Associations('95), Enacted the Act on Structural Improvement and Management Stabilization of Small and Medium Business('95), Established Small and Medium Business Administration(SMBA)('96)
Financial Crisis - 2002: Fostered venture businesses and promoted start-ups · Emphasized venture policy as a growth engine such as IT and NT and established measures to complement weak areas such as Small and Women's business · Opened KOSDAQ('96), Special Act on Venture Business('97), Small Business Act('97), Women's Business Act('99)
2003 -: Strengthen Self-Sustaining and Innovation Capacities · Implemented the strategy to secure SME competitiveness suitable for the innovation-driven era · Comprehensive plan to enhance SME competitiveness('04.7), Plan to vitalize venture businesses('04.12), 12 tasks for policy innovation('05.1), Comprehensive plan for self-employment('05.5), Revision of financing policy('05.6)

In an effort to meet the demand, the Korean government changed its SME policy to the direction with strengthening competitive edge of SMEs, an effort to foster SMEs as economic growth base. The government was therefore able to establish a strategy that is more conducive to the innovation-led economic structure (Refer to Figure 2).

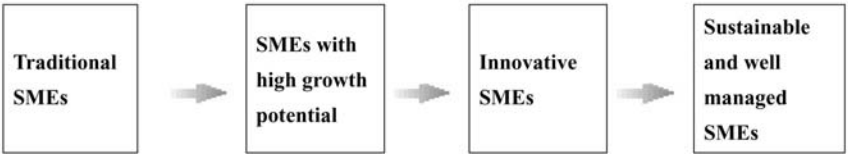
Figure 2: SME Innovation Policy Direction



Source: Innovative SME Advisory Committee (2006)

The government's SME development roadmap was designed to create an environment where all businesses including small firms and micro-enterprises are able to grow into innovative SMEs and the government seeks to make a shift in policy paradigm from the protectionist policy to the policy of promoting free competition and cooperation (Refer to Figure 3). The government continues to customize SME policies to meet the objectives differentiated in accordance with the demands and characteristics of SMEs. Focusing on indirect SME assistance such as establishing infrastructure and offering service and information rather than providing direct SME assistance, the government aims to lay the foundation for an innovative-friendly environment where SMEs can grow into innovative SMEs.

Figure 3: SME Development Roadmap



Source: SMBA(2006)

SME Innovation Policies

Innovative SMEs are defined to be SMEs equipped with R&D (which enables new product and process innovation) and commercialization capabilities. They are estimated to represent about 30,000, which is about 10% of the 330,000 total small and medium manufacturing enterprises in Korea. The government has systematically supported the innovative SMEs by promoting technology-based start-ups, innovating technology and marketing, and others.

1. TECHNOLOGY POLICY

The government implements various policies with focus on the following areas: fostering innovative SMEs that will lead technology innovation of SMEs; reinforcing networking of industry, academia and research institutes; promoting commercialization of developed technology; and encouraging public institutions to use their technological budget for SMEs.

SME Technology Innovation Program

Korea has executed the SME Technology Innovation Program to promote technological innovation of SMEs which have inherited R&D, to accumulate R&D capacity and enhance technological competitiveness by supporting the development of new products and processes. The government supports the program in a year project for general task or in three-year project for strategic tasks. The central government supports 50% and local governments 25% of the costs. When the SME technology innovation program is finished with success, the government receives back 30% of its contribution as technology fee for five years in installments. The program was initiated in 1997. Table 3 shows the result of the program per year since 1997.

Table 3: SME Technology Innovation Program by Year

(Unit: Billion Won, each)

	1997-99	2000	2001	2002	2003	2004	2005	Sum
Budget	107.2	60.0	86.1	99.3	110.1	130.6	142.2	735.5
SMEs	2,147	996	1,301	1,532	1,654	1,883	1,912	11,425

Industry-University-Research Institute Consortium Program

The Korean government supports local SMEs that have lack of innovation capacity to enhance their technology innovation and resolve technical problems by encouraging them to use excellent equipment and manpower of universities or research institutes. For the program of the Industry-University-Research Institute Consortium, the central government provides 50% and local governments 25% of the costs for technology development for up to one year. The industry-university-research consortium program started in 1993. The program resulted in 5,026 patent applications, 13,600 cases of prototyping, and 10,446 cases of process improvement during 1993-2004. Table 4 shows the result of the Industry-University-Research Institute Consortium program by year since 1993.

Table 4: Industry-University-Research Institute Consortium by Year

(Unit: Million Won, each)

Year	1993-99	2000	2001	2002	2003	2004	2005	2006	Sum
Grant	49,265	21,000	35,000	38,102	34,120	39,120	42,100	42,600	301,307
Consortium	433	146	182	197	206	218	222	135	1,739
SME	6,997	1,870	2,554	2,787	2,757	2,876	2,788	2,276	24,905
Task	6,286	1,795	2,327	2,611	2,593	2,743	2,690	2,276	23,321
Performance									
Patent	1,257	654	731	787	761	836	-	-	5,026
Prototype	3,692	1,160	2,029	2,184	2,284	2,251	-	-	13,600
Process	2,611	739	1,536	1,648	1,806	2,106	-	-	10,446

New Technology Purchasing Assurance Program

To commercialize technologies newly developed by SMEs, government agencies, public institutions including Korea Electric Power Corporation, Korea Gas Corporation, and Korea Railroad Corporation, and private large businesses commissioned SMEs to develop new technologies with the assurance that they will purchase the new technological products. The government supports financing for the technological development, while public institutions purchase the products for a certain period of time. The program started in 2003 by supporting 49 projects for one government agency. As of 2006, the government supported 120 projects for 45 demanders

including government agencies, public institutions and private large businesses.

Korean Small Business Innovation Research (KOSBIR) Program

In an effort to offer government-wide support for SME technology innovation activities, the government conducted the Korea Small Business Innovation Research (KOSBIR) program since 1998. In the KOSBIR, 16 agencies including 10 government agencies with massive R&D budgets and 6 government investment institutions are recommended to provide more than 5% of their R&D budget to SMEs. Since 2000, when the 13.2% of the national R&D budget was supported for SME technology development, the proportion has continuously increased up to 20.6% in 2005. The continuous increase is interpreted that the 16 participating agencies allocated more R&D budget for SME technology development and improved their institutional process to support SMEs in response to the promotion policy of innovative SMEs.

2. FINANCING POLICY

The government provides direct and indirect financing support for SMEs to ensure that innovative SMEs do not fail as a result of financing difficulties. For direct financing from the market, the government promotes the venture capital market. As for indirect financing, the government provides a credit guarantee service for SMEs ineligible for bank loans due to a lack of collateral.

Venture Investment Fund

To ensure the continuation of venture investments from the market, the government created \$500 million worth of venture investment funds in June 2006 by setting up 102 venture capital firms and 366 venture capital partnerships (Refer to Table 5 and 6). To build a foundation for the stable growth of venture capital, the government also formed the Fund of Funds to promote the establishment of investment funds for SMEs and venture businesses. Until 2009, the investment resources worth 1 trillion won will be created. So far, 385 billion won have been created, including 170 billion won

in 2005 and 215 billion won in 2006. In 2005 the Korea Venture Investment Corp was designated as the institution for operating the fund of funds.

Table 5: Status of Venture Capital Firms by Year

(Unit: ea, billion KRW)

Year	2000	2001	2002	2003	2004	2005	June, 2006
Firms	147	145	128	117	105	102	102
Fund	2,139	2,219	1,965	1,865	1,653	1,537	1,518

Table 6: Status of Venture Capital Partnerships by Year

(Unit: ea, billion KRW)

Year	2000	2001	2002	2003	2004	2005	June, 2006
Partnerships	326	396	412	430	424	400	366
Fund	2,406	3,051	3,270	3,579	3,817	3,936	3,734

Debt Equity Financing

Debt equity financing is provided for SMEs in order to enhance their access to finance by resolving market failures and to foster innovative SMEs. In July 2004, the government set up a comprehensive measure to strengthen competitiveness of SMEs to expand the provision of start-up fund, long-term facilities fund, and the fund for developed technologies to market. In 2005, measures of debt equity financing focused on innovative SMEs, seeking customer convenience through simplifying procedures, producing more results and strengthening post mortem.

The debt equity fund amounted to 3 trillion won in 2004, 3.16 trillion won in 2005, and 2.75 trillion won in 2006. A one-stop service of the debt equity financing, which does not require visiting loan guarantee institutions, has made the loan process quicker than before.

Credit Guarantee Program

Credit guarantees are provided to SMEs which have difficulty in financing by easing capital shortage and supporting business stability. The purpose of the

credit guarantee service is as follows: first, the service evaluates the level of technology, its commercialization and marketability; second, it offers financial assistance; and third, it intends to foster and develop SMEs with excellent technology and promote technical financing.

The credit guarantee funds are managed by the Korea SME Credit Guarantee Fund and the Korea Technology Guarantee Fund created in 1976 and 1989, respectively. Meanwhile, the Regional Credit Guarantee Foundation was established in 1999 and is being operated in 16 cities and provinces nationwide.

Certification of Innovative SMEs

There are three types of innovative SMEs in Korea. First, it is adventurous and challenging venture business. The venture business is expected to bring high profit and high risk as venture capital investments increase. The second type of SMEs is Innovation business (Inno-biz), which offers high growth potential and is capable to secure technology competitiveness through technology innovation. The third type of SMEs is management innovation-driven SME, which currently carries out management innovation-related activities or has made innovative achievement after implementing management innovation activities within the past three years.

Once a business is certified as innovative SMEs (either a venture business or inno-biz business), the government provides them with diverse benefits such as the standard reduction of issued capital, higher priority and additional scores for a patent, and special benefit when listed on the stock market. In addition, employees in a certified venture business can have tax benefits when they receive stock option. In particular, technology innovative SMEs (inno-biz companies) can take part in various technology development support programs on preferential basis.

3. BUSINESS INCUBATOR POLICY

The government has supported a program for establishing and operating Business Incubators (BIs) at universities and research institutes. The program beneficiary would be entrepreneurs of technology-based start-up firms and

potential SME starters. The program has provided SMEs with business spaces for 2 to 3 years in BIs, management, technology, or marketing counseling services, and bridging financing.

In 1998, the government began to fund some costs for establishing BI centers at university, national and public research institutions. The government grants are provided for operational costs of BIs and the expansion of their facilities. If an incubator achieves poor performance, it would be excluded in the list of beneficiaries for the next financial season. In 1999, the government increased the number of BIs to create more jobs and resolve unemployment. As of June 2006, there are 268 BI centers, which accommodate 4,287 companies, and 4,255 companies graduated from BI centers.

4. MANAGEMENT INNOVATION POLICY

So far, the government has been promoting innovative SMEs by focusing on their technological capability. Traditional SMEs may have a deficiency in high technology, but they have contributed to the Korean economy in terms of job creation and tax payment. The competitiveness of an enterprise can be also brought forth by innovating non-technological areas such as marketing and organizational efficiency as well as technological innovation. Traditional SMEs can build up and enhance their competitiveness by means of management innovation.

SME Consulting Service Program

The SME consulting service program started in 1999. In 2005, the government developed the Coupon-based SME Consulting Service program, a radical change from the previous one by introducing the voucher system and digitalizing the application processes in the website. This Coupon-based Consulting Service program is the outsourcing strategy to counsel SMEs to resolve bottleneck inherited in the organization by major management innovation activities.

The Coupon-based Consulting Service program has a special feature in not only transforming the conventional consulting program but also contributing to fostering the consulting industry. Moreover, the government has

implemented a code of ethics for prohibiting moral hazards, training programs for capacity building of consultants, and consulting evaluation. The government conducts a survey on consulting companies and a survey on the satisfaction of SMEs as policy consumers.

Customized Policy Information System

Korea has a customized policy information system or SPi-1357 system that combines online portal site and a call center for troubleshooting. The portal site (www.spi.go.kr) is the gateway to provide policy information in real time in 9 areas such as finance, manpower and technology by integrating 7,200 kinds of information held by 232 SME support agencies. An offline comprehensive counseling system is also provided for SMEs through the toll-free number of 1357. The specialists in each area answer questions, and counsel the bottleneck of business for SMEs. Through the integration with the public purchasing network, the SPi system is not only a guide to starters and potential founders but also reduce an unnecessary excessive competition within each sector and area.

5. MARKETING POLICY

Procurement of Government

The government requires public institutions to purchase SMEs' technological products that have been approved for performance by the government, thereby promoting technology development in SMEs and public purchasing of SME products. In July 2005, the government introduced a system of performance recognition and insurance of technological products developed by SMEs. It also established a basis for purchase personnel in public institutions to be exempt from liability.

The government adopted the Technological Product Purchase Target System to public institutions. The proportion of purchased technological products made by SMEs stood at 5% in 2006, but will be increased to 10% in 2010. To secure the effectiveness of the system, the accomplishment level is reflected in evaluating public institutions. The purchase amount has increased 400 billion won in 2003 to 1.1 trillion won in 2006.

Export Promotion

In the program of supporting overseas private service center, 153 private consulting companies in major economies were designated as overseas service centers to help SMEs advance into foreign markets. They are responsible for conducting market surveys on export and foreign investment, identifying partners, and providing consulting for projects such as establishment of a local legal entity. During 2001- 2005, the number of companies that received support recorded 752, achieving export sales worth \$12.78 million.

The trade missions are dispatched to overseas niche markets in order to find product markets for SMEs and promote their exports. Since 1998, trade missions have been sent for cooperatives of each industrial sector.

The large and small firms' joint entry into overseas market program, which began in 2006, aims to enhance export competitiveness of SMEs. The purpose of the program is to help small companies advance into overseas markets by using experiences and human networks of a large firm with high brand recognition at home and abroad. The government provides indirect costs for individual firms, while large firms cover the overhead costs incurred. Direct costs are borne by individual companies such as airfare and lodging costs.

6. HRD POLICY

Recruiting

Through the promotion of SME R&D manpower recruiting project, the government assists with the establishment of university-industry cooperation offices and research institutes attached to business so as to enable SMEs to utilize ample workforce and physical R&D resources of a university. In 2005, 164 university-industry cooperation offices were installed and 44 university-industry collaborated research institutes attached to SMEs were established.

In particular, the Industrial Technician Selection program was designed to relieve SME labor shortage problems. The program selects some of those who have obligation to do military service and instead sends them as

industrial technicians to SMEs for production or manufacturing.

Training

The SME Manpower Structure Upgrading Program aims to enhance productivity of SMEs and resolve their manpower shortages by training employees at SME cooperatives in each sector through educational courses. Since 2005, this program involves the Federation of Small and Medium Business, which is in charge of general supervision, and its cooperatives. They conduct the program after reflecting the needs of its member SMEs. In 2005, 20 cooperatives participated in 205 educational courses with the presence of 6,908 workers from 3,338 SMEs.

Status and Issues

The government has set the SME development direction by transforming past SME support practices of protection and direct support policies into a new environment, which can provide a venue for self-managed system, free competition and cooperation. Under the premise that "Cultivating innovative SMEs is the key to a new environment," the government is forecasting that SMEs will play a pivotal role in the Korean economy with its major emphasis on a policy of cultivating, certifying and supporting innovative SMEs. As we have seen from the previous chapter, the government has continued to develop a variety of programs, often newly drawing up a plan suitable for a new environment. This chapter presents policy programs' review of current trends and various issues.

1. TECHNOLOGY POLICY

General and strategic tasks of the SME technology innovation program are supported by the government for one year and three years respectively. Given the government-sponsored tasks are one-time program only, it is easy to witness that a lack of continuity in commercializing developed technologies has made the technologies gradually disappeared in the market. According to a study report, 10 to 100 times of development fees are required for successful

technology commercialization and average six years are taken for transferred technology to be successfully commercialized.

As such, the government needs to upgrade the SME technology innovation program in line with business and market developments. There is a tendency among advanced economies that industrial sectors with high risks are specially defined as market failure and the governmental support for them is increasing. SBIR in the USA supports labor costs of venture companies and even executes pilot projects by itself to reduce the risks that may be taken by private sectors. The technology policies would need to place an emphasis on core technologies having high potential in commercialization and support them long enough to make success in the market.

2. FINANCING POLICY

Although the government is shifting from debt financing to equity financing, the debt financing in Korea still occupies the majority of its financing policy. The debt financing is mostly used in facility investment and operations rather than in technology development. The dependency of debt financing on the government may cause SMEs in trouble, because it would be difficult for them to concentrate on technology development due to a so-called "pay-back pressure." Even those technology-based start-ups would have rare chances to have debt-financing because of no previous record of performance.

The government has adopted the fundamentality of competition and cooperation. However, the government intervention is inevitable in high-risk technology innovation because of market failure. Particularly fostering innovative SMEs requires equity financing from the high-risk and high-return venture capital. The governmental should make efforts to build an environment conducive to SME innovation by promoting direct equity financing for the early staged start-ups.

3. BUSINESS INCUBATOR POLICY

Since most of tenants at the initial stage show lack of marketing, equity and investment capabilities, continued restructuring is a must for BIs producing less satisfactory performance. In addition, integrating BIs spread in many

geographical areas into one and specializing them by industrial sector need to be considered for better BI performance. The followings are programs which can assist tenants to be successful in building their venture businesses: the programs include supporting mutual technology development fund, uniting brand names into one, providing a joint market and establishing technology innovation network as well as conducting management training programs targeting for business managers. Moreover, the government is able to enhance the efficiency of BI programs by pushing for introducing a private licensing system for BI managers and providing a specialized training tailored to managers' capacity building.

There are three ways for the government to achieve BI competitiveness: first, it should be committed to draw further interests in venture capital investment by specializing BIs; second, it should focus on actively supporting model incubators; third, it should secure the foundation for quality innovative incubators by liquidating insolvent BIs. As for venture capital, evaluation and management system for BIs should be enhanced to have active interactions with venture capitals and additional incentives should be given for quality BIs.

4. MANAGEMENT INNOVATION POLICY

Current SME Consulting Service Program is providing one-time service with its government focus on management advice in the areas of operation management. The government needs to offer a policy to promote actual SME innovation by combining consulting service with technology, marketing and e-Business. It is also recommended that a multi-level approach which can provide diagnosis, action plan, and execution helps SMEs fully conduct their own projects independently. BUNT(Business Development using New Technology Program) by the multi-discipline team of Norway, COMET (Commercializing Emerging Technology) of Australia and IRAP (Industrial Research Assistant Program) of Canada can be ideal programs for benchmarking.

5. MARKETING POLICY

Government-initiated marketing programs are offering marketing opportunities to SMEs rather than actually strengthening SME marketing

capacity. The government procurement policy initiates and promotes the sales of the newly developed products by SMEs. To prolong the sales, the government may consider a support policy for marketing service companies. The marketing service companies will be majoring in product planning and distribution, while innovative SMEs will be developing and manufacturing products.

6. HUMAN RESOURCE DEVELOPMENT POLICY

The inflow of high skilled people into SMEs is critical for SMEs to become successful and sustainable. Most SMEs cannot afford to hire high-skilled people nor equip themselves with self-owned training facility, while universities are already equipped with not only facility for training but also skilled trainers and lecturers. The government can induce region-based collaboration between SMEs and universities by providing policy programs of technology development and training. Particularly university students would have chances to work in SMEs and be familiar with an SME environment before graduating from universities. The earlier experiences would lead them to continue their jobs in SMEs.

Public/Private Cooperation in Promoting SMEs

As discussed in the previous chapters, the government has driven the public sector towards supporting SME innovation. One of the representative programs is Industry-University-Research Institute Consortium Program. In the sense that this program promotes technological development through cooperation between Central government, local governments, local universities, local research institutes and local SMEs, it is well evaluated as ideal structure for the regional industrial and SME developments. However, it has been indicated that the government grant is too small with less than 10 million won to make technological development, the manpower of the universities and institutes lacks in field experiences, and the SMEs anticipate outcomes in a hasty manner.

It should be noted that the program involves diverse stakeholders and each one's interest is also different. To produce better performance out of the program, cooperation structure must be sound and effective for the intended synergy effect. In addition, the program needs to set up a prearranged plan with consensus among program participants and to build regional human networks with stakeholders before the participants make a proposal for the program. It also requires refinement and improvement of the consortium structure by linking other regional innovation programs such as Techno Parks, TLO (Technology Licensing Office), TIC (Technology Innovation Center), BI (Business Incubator), and RRC (Regional Research Center).

In details, the current regional innovation programs should be reorganized according to regions, industrial sectors, and hosting organizations. At the same time, the Industry-University-Research Institute Consortium Program should be reorganized to be integrated into the regional innovation programs. Meanwhile, large companies need to be involved in the regional innovation programs so that they can further purchase SME developed products. More structured support programs need to be designed and built along the development lifecycle.

Some other programs for public and private cooperation may include New Technology Purchasing Assurance program, KOSBIR program, Fund of Funds, and Technological Product Purchase Target system. The New Technology Purchasing Assurance Program involves government agencies, public institutions and private large businesses for SMEs to be solely engaged in the technology development without the concerns of marketing. The KOSBIR program recommends 16 government agencies to allocate some portion of their annual R&D budget to the SME technology development. The Fund of Funds using public finds complements private venture capital markets by stabilizing the venture investment environment. The Technological Product Purchase Target system institutionalized the obligatory purchase of SMEs' technological products by public institutions for promoting technology development in SMEs.

These public and private cooperation activities indicate that the government has a strong commitment to promote innovative SMEs by resolving inherent deficiencies of SMEs like technology development, marketing development

and financing. Well-designed cooperation programs will not inhibit the free competition paradigm but foster the policy paradigm of concentration on innovative SMEs.

Conclusion

We have briefly reviewed overall background of SME innovation policies in Korea. This paper describes SME innovation policy development in chronological order. Then it explains major policies on technology, financing, business incubator, management innovation, marketing and HRD, followed by various issues on those policies. Finally, we look at public and private cooperation in promoting SMEs in the last chapter.

In 2005, a comprehensive plan for developing SMEs into innovative SMEs was rebuilt and introduced, and it has been carried out since 2006. The Korean government has focused on the institutional establishment of a SME-friendly environment to enhance SME competitiveness. With the development of e-business, the government has built an online system which provides a tool for submitting applications and conducting ex-post monitoring. Korea has also established and operating the SPi-1357 system on <http://www.spi.go.kr/>, with the aim to deliver integrated information about government support policies and programs to SMEs which have less capability of collecting information.

Moreover, the government has introduced certification systems of innovative SMEs and provides benefits for certified innovative SMEs when they participate in governmental programs. There are certification systems that are being implemented: Venture business certification was introduced in a bid to overcome the 1997 financial crisis, while technology innovation certification and management innovation certification were created in 2001 and 2006 respectively. It shows that the government would focus on setting a qualitative goal and creating an environment for innovative SMEs, rather than counting the target number for a quantitative goal in promoting innovative SMEs.

Starting 2000, the Korean SME policy focus has been shifted to strengthen competitiveness and build innovative capacity from protectionist policy. Given that local governments have a relatively short history and SME policies are less developed, it is advised that the local governments in Korea closely work with the central government to strengthen the SME innovation.

In conclusion, Korea has worked hard to create best practices just suitable for Korea and it has experienced trials and errors to successfully launch them. Its strenuous efforts finally pay off and it has produced various favorable results by benchmarking, adapting and improving cases of other economies. Now, it wants to share its past experience with other member economies. The Korea-made best practices can be well referenced by other economies as long as they recognize and understand the history behind them. Otherwise, those economies may repeat the same mistakes Korea made. Therefore, it is strongly suggested that economies at the PECC level need to build a framework of best practices to effectively share it in the Asia Pacific region.

Notes

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The New Zealand Policy Environment for the Development of SMEs

By Claire Massey and Coral Ingley

Preface

This report has been written as a contribution to the PECC project, "The Policy Environment for the Development of SMEs", coordinated by Dr. David Hong, Director General of CTPECC and President of the Taiwan Institute of Economic Research.

The project seeks to identify obstacles to SMEs development in Asia-Pacific economies and to develop feasible solutions and sound policies to help interested economies promote SMEs. The product of this project will be a report consisting of several policy papers, and the focus will be on SME development across industries for specific economies.

This report addresses the issues in New Zealand. It has been prepared by Professor Claire Massey, Director of the New Zealand Centre for SME Research at Massey University and Associate Professor Coral Ingley, Senior Lecturer at the Auckland University of Technology. Research assistance was provided by Tanya Jurado from the New Zealand Centre for SME Research.

While various individuals were consulted in the process of writing the report, the views expressed and the conclusions drawn are those of the authors alone.

Introduction

New Zealand is a small developed nation located in the South Pacific that is inhabited by just over 4 million people. The New Zealand economy has sizeable industry and service sectors and a significant primary sector. The economy is currently enjoying low unemployment, and some economic growth. Areas of concern for the government as far as small and medium enterprises (SMEs) are concerned revolve around New Zealand's low productivity rates compared to other OECD countries and low volumes of exports. New Zealand has a good overall infrastructure, a sophisticated banking system and a developed transport system.

The globalisation of the economy has affected the way all New Zealand businesses operate, and no less so SMEs. Whereas once access to overseas markets would have been limited, information and communication technologies, such as the internet, have made it more viable to access other markets. However competition is also greater than ever before and New Zealand businesses must also overcome the challenge of distance and size in order to expand their markets overseas.

These new pressures of competition have had an impact on what areas of industry are thriving. They have also influenced recent governments in their approach to policy formulation in relation to economic growth. The overall approach that is guiding current government policy is broadly indicated in the term "economic transformation". The key objective is to increase business performance through policies that are aimed primarily at globalisation and increased productivity. This is the framework under which government policy towards SMEs in New Zealand is formulated today.

This report outlines this approach, detailing the specific policies and programmes-against a background of the New Zealand economy.

SMEs in New Zealand

As a young economy, early New Zealand firms were typically small or medium in size until relatively recently. However along with much of the rest of the world, New Zealand became more aware of the significance of the SME sector following the landmark report of the Great Britain Committee of Inquiry on Small Firms (1971). The government responded by establishing the Small Business Agency (SBA) in 1976, an agency designed to help small firms grow.

DEFINING A SMALL FIRM

One of the first tasks of the SBA was to define a small business in New Zealand. This definition was contained in legislation, which stated a small business was one employing fewer than 50 FTEs in the manufacturing sector, fewer than 25 people in the wholesale and retail sectors and fewer than 10 people in the service sector (Bollard, 1988). At the time the term "small and medium enterprise" was not as commonly used as it is today, and no definition was provided for an SME. With the closure of the SBA in 1987 the definition of a small firm fell into disuse and since this time New Zealand has lacked an 'official' definition of a small firm.

The closure of the SBA took place against the background of the economic reforms that were taking place during the 1980s in New Zealand. This followed the election of a Labour government in 1984, a government that was committed to deregulating the economy - in all sectors. This period of deregulation had a major impact on many of the sectors that make up the business infrastructure - such as banking, telecommunications and transport. However the commitment to creating an "even playing field" for all business did directly lead to the disestablishment of the SBA - an event that meant that small firms temporarily fell off the government's agenda.

It was not until the 1990s that small firms were again explicitly included in government policy statements such as the Budget (where the term SME was introduced for the first time) and another attempt at a definition was made. This was led by the government department with primary responsibility for economic development; the Ministry of Economic Development (MED).

Then known as the Ministry of Commerce, in 1999 MED published the first issue of its annual publication SMEs in New Zealand: Structure and dynamics (Ministry of Commerce, 1999). This described a small firm in New Zealand as one which employs fewer than 10 full time equivalent employees (FTEs) and an SME as one which employs fewer than 20 FTEs; it also described a large firm as one with more than 100 FTEs. While not an official definition, this definition is widely used by the Ministry in its publications. It should be noted however that in some of its own research other definitions are used. For example the Business Practices and Performance Survey (published as Firm Foundations in 2002 by Knuckey, Johnston, Campbell-Hunt, Carlaw, Corbett and Massey) defines an SME as a firm with more than 6 and fewer than 50 FTEs. The MED definition is regarded by some as being problematic as it provides no categorisation for firms with more than 20 and fewer than 100 FTEs. Nor is it easy to align with other international definitions. In response to these perceived shortcomings, academic researchers have provided an alternative definition. Cameron and Massey (1999) offer a categorization that is consistent with the international definitions in use in other parts of the world and draws upon the characteristics of an SME that were identified by the committees of inquiry in the United Kingdom and Australia. This definition also makes allowance for the fact that large firms in New Zealand are smaller than large firms in other countries, such as the United States and many European countries. Cameron and Massey's definition for New Zealand firms is as follows:

- a micro-enterprise employs fewer than 5 FTEs,
- a small firm employs between 6 and 49 FTEs,
- a medium firm employs between 50 and 99 FTEs,
- a large firm employs more than 100 FTEs.

A STATISTICAL OVERVIEW

The most recent New Zealand statistics available show that in February 2006 the business frame (the term given to the central database of New Zealand firms) was comprised of approximately 346,091 'economically significant enterprises' (Statistics New Zealand, 2007)¹. In addition there are around 65,000 enterprises engaged in agricultural production (farms) but these figures are calculated by a separate survey of agricultural production and are therefore

usually excluded from official statistics. This total (of around 400,000 enterprises) represents the New Zealand business population, but it is important to remember that there are two important omissions from these statistics. Firstly, it is not known with any degree of accuracy how many 'economically insignificant' enterprises exist. These enterprises are difficult to identify, partly because of the lack of an accepted definition of 'insignificance', but in general, these are businesses that are so small in terms of sales that are not considered to be worth counting. Secondly, the underground, or black market, economy is also omitted, and it is unknown how many enterprises this diverse sector may include.

It is common for statistics on SMEs to be presented in terms of the number of individuals each enterprise employs (usually in terms of full-time equivalent employees - or FTEs). Table 1 shows the 2006 total of economically significant enterprises by their different size groups, using FTEs as the unit of data collection and the Cameron and Massey definition of the different size categories. This figure excludes enterprises which are engaged in agricultural production.

Table 1 illustrates that approximately 86% of 'private sector' firms, (i.e. all enterprises once central and local government, incorporated trusts and societies and cooperatives are excluded) employ between 0 and 5 employees. It also shows that 99.4% of all New Zealand firms can be categorized as SMEs. These figures again exclude enterprises engaged in agricultural production.

Table 1: SMEs in New Zealand (2006)

Category	Number of employed	Enterprises		Number employed	
Micro	0-5	300,571	86.8%	189,810	10.8%
Small	6 to 49	41,277	11.9%	573,550	32.5%
Medium	50 to 99	2,309	0.7%	158,830	9.0%
Total SMEs	344,157	99.4%	922,190	52.2%	
Large	100+	1,934	0.6%	843,250	47.8%
Total	Total	346,091	100.0%	1,765,440	100.0%

Source: Statistics New Zealand, 2007.

Table 1 shows that most New Zealand enterprises can be classified as micro, small or medium sized, with a mere 1,934 large enterprises employing more than one hundred people. However, although this large firm category is the smallest number in terms of enterprise units, it is by far the largest employer. These data make it clear that the SME sector dominates the New Zealand economy in terms of numbers of enterprises, as it accounts for 99.4% of the entire business population.

These SMEs also employed 52% of the total work force (without taking into account the ownermanagers who are not considered as employees). A significant proportion of this group comprises sole traders and micro-enterprises. As a consequence, many are small, closely held firms that, while sharing some of the features of large firms, will be dissimilar in their legal structure, market scope and management practices.

These statistics have been drawn from the annual update of the New Zealand "business frame" - a database that includes all economically significant firms in New Zealand (with the exceptions noted above). Another perspective on the significance of the SME sector is to examine the statistics on the individuals who work in these firms, such as those collected by the Census (undertaken every 5 years) and the Household Labour Force Survey. This shows that around 81% of the employed New Zealand labour force are paid employees while 19% are selfemployed or are an employer.

These statistics also allow us to examine the characteristics of the self-employed in more detail.

Between 1996 and 2006 the number of self-employed women employed has risen from 28.4% to 32.8% of all self-employed. In 2006 men accounted for 68% of all employers (including selfemployed) and women accounted for 32% (HSLF, 2006). Further, between 2001 and 2006 the proportions of men and women in paid employment have remained consistent but there has been a 21% increase in absolute numbers for both genders.

According to the 2001 Census, the largest group of self-employed were European (90.5% of the total number of self-employed) followed by Asian (5.6%) and Maori (5.47%). Pacific Islanders only made up 1.8% of the total.

However, between 1991 and 2001 the percentage of European self-employed has decreased by 3%, while there has been some growth amongst all other ethnic groups, especially amongst Asian where the number of self-employed grew by 80.6% (from 3.1% to 5.6%) (Census, 2001). The latest official statistics from the 2006 Census for this category are not yet available but the pattern is unlikely to have changed.

BUSINESS PRACTICES IN NEW ZEALAND SMEs

The statistics paint a picture of the New Zealand SME sector as one which is dominated by micro-enterprises and where the category of self-employed individuals with no employees (as opposed to those individuals whose enterprises do employ staff) is in the majority. This has significance for the way in which the owners and/or owner managers operate their firms. A fundamental point of difference between the management practices of SMEs and that of large firms is the level of informality in relation to management and organisation. For example, in small firms it is typical for there to be a high degree of informality, as the owner-manager establishes systems that are appropriate for the type of firm - without reference to the practices of other firms. This approach to the development of systems that are situation specific is a particular feature of new firms, which tend to develop unstructured, reactive, flexible responses to situations that are often being encountered the first time. This lack of formalisation can be an advantage - as it can be a strength that can assist the firm to be innovative. As the firm gets larger, the degree of formalisation in terms of practices and processes changes - with most successful firms developing more structured and/or formal practices.

This can be seen as an increase in the capability of the firm - and "firm capability" has been an interest of the New Zealand government for some time. In 2000 the New Zealand Ministry of Economic Development established a project in an attempt to increase its understanding of the business practices of New Zealand firms: the survey of Business Practice and Performance. Underlying the study was the idea that excellent business practice (in terms of six core areas) leads to a high level of results for the firms (as measured by outcomes such as competitiveness and innovation).

The project used a model of business practice that was adopted by the Australian Manufacturing Council for their 1994 study and this model was based on a review of international best practice models, including the Baldrige National Quality Award Criteria for Performance Excellence (CPE), the European Foundation for Quality Management Excellence and the Canadian Framework for Business Excellence.

The survey instrument was refined for the second survey which was carried out in 1997 and revised again before being used for the third time in New Zealand in 2001. Statistics New Zealand was responsible for administering the survey using a mandatory mail questionnaire, (the Business Practices Survey) to the target population for the questionnaire (all private sector firms operating in New Zealand).

All industry groupings and all firm sizes were represented. For the purposes of this study, 'small' firms were defined as those with 6-19.5 FTEs, 'medium' firms were those with 20-49.5 FTEs and 'large' firms were those with more than 50 FTEs. The questionnaire was sent to 3,378 enterprises, (813 large, 1,116 medium and 1,449 small). Responses were received from 2,756 enterprises (679 large, 921 medium and 1,156 small). The firms that responded were located in agriculture, manufacturing and service sectors and were spread across the whole country. The survey examined business practice in terms of six key elements: leadership and planning; customer focus; information and benchmarking; employee practices; quality and supplier focus and innovation and technology.

Results from the survey were published as Firm Foundations in 2002 (Knuckey et al, 2002). Key findings were that while a good number of New Zealand firms have built a firm foundation of effective practices, several key areas were highlighted as needing further attention. Areas of particular concern were strategic planning; environmental management; staff performance management; supplier relationships and research and development activity.

This survey provided important new knowledge on the way in which New Zealand managers operate, and some key questions from the survey are now integrated into the annual Business Operations Survey administered by Statistics New Zealand.

The New Zealand Infrastructure

At a national level, New Zealand's infrastructure is in reasonable condition as ascertained by a recent stocktake (PricewaterhouseCoopers, 2004). Subject to an ongoing appropriate level of investment, the current infrastructure should not pose a barrier to the government's growth and sustainable development objectives. However, there are significant local and sector-specific issues, which may have significant impacts, both locally and nationally. Of particular note are:

- Land transport, particularly roads in the major cities and deferred maintenance of the rail network;
- Water and wastewater:
- Security of potable water supply in drought-prone areas,
- Water supply and wastewater treatment in smaller communities with large tourism-driven seasonal fluctuations in population; and
- Competing demands for water supply (particularly agricultural and commercial/industrial).
- Fuel for future electricity generation and certainty of supply in dry periods.

These concerns are detailed below:

Energy: Electricity

- The condition of the existing generation plant does not inhibit its ability to operate at acceptable levels of reliability.
- Some transmission constraints exist.
- New generation capacity is clearly required in the near future, but uncertainty in a number of areas is inhibiting investment:

- Kyoto Treaty and carbon taxes (which will affect the relative costs of fuel supplies),
- Regulation and the role of the Electricity Commission,
- Coordination of generation and transmission investment.
- The changing mix of generating fuel also creates uncertainty (compounded by the potential impact of carbon taxes).
- Given the preponderance of hydro generation, the overall level of emissions from electricity generation is relatively low, but is highly sensitive to the choice of fuel supply at a few key assets.
- Market-based risk management tools offer opportunities to improve demand management.
- There is a consensus that changes to household and workplace practices could reduce electricity demand. It is an open question as to whether education and persuasion are likely to be able to influence such practices.

Energy: Gas

- Processing and transmission infrastructure assets are relatively new assets. Their condition does not inhibit their ability to operate at acceptable levels of reliability.
- Sources of natural gas supplies remain an issue.
- There is concern as to whether current exploration and discovery levels will be sufficient to ensure gas supplies are secure.
- Without secure gas supplies, thermal generation capacity in New Zealand will need to rely on coal or imported LNG.
- Major discoveries outside the Taranaki region would require substantial infrastructure investment (processing and transmission), affecting the

economics of exploration and commercialisation, or major new gas consumers to be located nearby (e.g. electricity generation).

- Consumption of gas in the home is generally the most efficient use of fossil-fuels energy (particularly compared to conversion to electricity). A number of commentators have indicated that there appears to be little expansion in domestic gas usage, although the reasons for this are unclear.

Water Supply

- The quality and security of supply of residential reticulated water is generally at a level necessary to meet demand (although there are exceptions).
- There has been substantial investment in treatment plants over the last 10 years.
- There are issues with competing demands for water (particularly between agricultural and industrial users);
- The current mechanisms for water allocation, via the Resource Management Act (RMA)², have limited ability to prioritise competing water uses; although the creation of integrated water management plans can assist with allocation processes (essentially by preempting a large part of the debate over the priority of use).
- Water allocation processes, undertaken at local or regional levels do not contain incentives to balance local and national benefits and costs in the allocation of local water rights.
- Few market mechanisms are in use in the water sector: there is no charging for water abstraction and charges to end-users are most often via the rating system. There is very little residential water metering.
- In the absence of pricing signals, demand management is confined to rationing or regulation (e.g. the Building Act requiring use of water-efficient systems). Lack of pricing signals also has implications for

determining the optimal level of investment (within the requirements of health regulations).

- Small communities servicing comparatively large tourism activities may be faced with the need for, but not have the rating base to support, necessary investment in processing plant and systems (or such investment may consume a disproportionate amount of a rating base, diverting expenditure from other activities). These issues are likely to become more acute with the projected growth in tourism.

Wastewater

- As for water supply, the condition and capacity of wastewater assets is generally at a level to meet demand. There has been substantial investment in treatment plant over the last 10 years.
- The RMA provides considerable flexibility for treatment processes that are appropriate to given regions.
- However, there are no national benchmarks on the level of discharges into the environment, which makes an assessment of the environmental impact of wastewater treatment difficult across the country.
- There is anecdotal evidence that some wastewater treatment systems are in breach of their RMA consents.
- As for water supply, tourism activities heavily influence effluent output in some small communities that may lack the rating base to make the necessary investments.

Transport: Road

- Transit NZ's measures of road condition indicate that, overall, the condition of roading infrastructure is generally good, although there are exceptions.
- Congestion affects the Auckland region to the greatest extent. There are some issues of congestion in other parts of the country.

- The structure of road use charges is such that there are few pricing signals that affect driver behaviour and, likewise, investment decisions cannot be based on pricing signals sent by road users.
- Use of the roads gives rise to a number of environmental and other impacts including noise, emissions, contaminated water run-off, accidents, congestion etc). A study is underway to estimate the costs associated with these impacts and the extent to which they are factored into existing charges for using the road network.
- Governance arrangements, particularly in Auckland, have been raised as an issue in terms of the responsiveness of planning and investment to growing road and other land transport issues.
- Funding of roads projects is essentially on a pay-as-you-go basis.
- This inevitably constrains the volume of investment within a given period, particularly when facing investment "humps".
- Without some other source of revenue (e.g. tolls) or funding (e.g. Crown contributions), borrowing allows optimised scheduling of projects. Within a fixed budget and time horizon, borrowing to fund more current investment inevitably constrains future investment. However, it would be assumed that the decision to bring forward investment would be based on cost: benefit analysis that concluded in its favour, as indicated in the previous section of this report.
- There is a growing acknowledgement of the need for integrated planning and transport management, particularly in urban areas, so as to mitigate the potential for increasing traffic volumes.

Transport: Rail

- The rail network is suffering from low and declining levels of asset replacement. This has implications for the quality and reliability of services.

- Despite increasing productivity in the mid-1990s, the rail business has not been able to recover its cost of capital.
- The quantity of freight carried on rail is increasing.
- Parts of the rail network, usually tunnels, are not capable of taking the longer or higher containers that are increasingly used internationally.
- The proposed government investment in the railway network is expected to reduce the level of deferred maintenance. Two particular issues arise for policy in this area:
 - The basis of allocation of investment to specific lines; and
 - The access charges regime for use of the network.
- The historical layout of the rail network does not favour commuter services, particularly in Auckland.
- The negative externalities from rail are generally lower than negative externalities from road. This needs to be balanced against the lack of door-to-door flexibility of rail compared to road transport.
- The Alternative to Roothing framework for funding rail investment focuses on benefits to road users, rather than wider national benefits.

Transport: Ports

- Generally, there is excess capacity in the sector, and there has been significant investment undertaken over the last ten years (particularly to accommodate the containerisation of trade, but also driven by growth in dairy and forestry industries).
- Assets are generally maintained to meet commercial demands and previous issues of under-maintenance have generally been remedied over the last 10 years.

- Many ports do face constraints on their operations or ability to expand:
- The availability of land affects most ports to some extent.
- As trade grows, transport links are increasingly important, with consequential difficulties arising from the location of most ports on central urban waterfronts. To some extent this can be ameliorated through management of deliveries and the development of inland ports.
- Internationally (particularly in the container trade), there is a steady trend towards fewer, larger vessels, making fewer calls at fewer ports. Many ports face constraints (in berths, or channel draft or width) in being able to accommodate these larger vessels.
- In the long term, this could imply that international (particularly inter-continental) trade will consolidate increasingly on fewer ports, although this is uncertain and there is a range of views on the matter. If such hubbing did occur at a few ports, the impact on other ports will be site-specific, depending on the relative economics of coastal shipping, road and rail transport.

Transport: Airports

- Over the last 10 years, the number of international airports has increased from three (Auckland, Wellington and Christchurch) to seven (adding Dunedin, Hamilton, Palmerston North and Queenstown). Other airports also have plans to offer facilities capable of supporting services. Only Auckland and Christchurch are currently used for intercontinental services (excluding trans-Tasman travel as intercontinental).
- Of the airports included in the study, Auckland and Wellington face the greatest constraints on aircraft movements. Auckland has far greater capacity to expand capacity, with land for a second runway.
- The ability of the sector to accommodate growth in passenger capacity depends in large part on the airlines:

- Being able to schedule international/intercontinental services outside of busy periods (not a simple task, as New Zealand is generally a schedule-taker);
- Increasing plane sizes on domestic routes. The trend has been to use smaller planes and more frequent flights. Overall using larger planes could increase seating capacity on some routes.
- There is considerable ongoing investment in the sector, with terminal expansion planned at Auckland, Hamilton, Christchurch and Dunedin. Other smaller regional airports would benefit from terminal expansion and runway extensions.
- Most new terminal developments are specifically designed for (relatively) simple modular expansion.
- Terminal expansion can be expected to trail passenger numbers (airports and airlines want the greatest possible utilisation of current assets before further investment is undertaken).
- New Zealand has an array of smaller regional airports that play a key access role. Maintenance investment in these will be a continuing requirement.
- Airports must operate within noise constraints set out district plans. Some (e.g. Wellington) operate under a curfew. Airports report that they can continue to operate within current plans for the foreseeable future, but tightening of controls (particularly the imposition of curfews) would cause significant problems.
- The air traffic control system (oceanic and domestic) has considerable capacity (including high levels of redundancy in the system). The system is also generally scalable to allow operation of a larger number of airtracks if needed.

Telecommunications

- Telecommunications has a number of characteristics that are different from the rest of the sectors, not least as these systems tend to be far more flexible

and scalable than other infrastructure. This is not to underestimate the complexities of upgrading and managing a telecommunications network: it is just that by comparison, it is likely to be subject to fewer external constraints than, say, building a new power station or motorway.

- New Zealand avoided the excesses of the recent telecommunications boom and its consequent losses. A corollary is that New Zealand does not have the vast quantities of unlit or barely used fibre that are reported elsewhere in the world (particularly the US).
- Uptake of advanced services (broadband), particularly by households, is low by international standards. This would appear to be attributable to pricing structures and relatively low-cost dial-up internet access, rather than the availability of infrastructure.
- Competition in infrastructure provision appears to be increasing, with the roll-out of wireless services in particular. This has been assisted by Project Probe. It is too early to say whether this increase in competition will prove sustainable.
- Regulation can be expected to continue to play an important role in the sector, both in relation to interconnect, but also the potential unbundling of the local loop ("LLU").
- The issue of LLU is highly contentious, not just with Telecom New Zealand ("TCNZ"), but also with those companies that are investing in wireless networks that bypass TCNZ's local loop.
- Mobile services cover approximately 97% of households, plus central business districts, major business areas and major transport corridors. Third Generation Mobile (broadband for mobiles) has been introduced but the two operators (Vodafone and TCNZ) were unwilling to disclose details of roll-out plans.

Summary of infrastructure issues

Each of the infrastructure sectors raises particular issues. Some themes can be drawn out that often cross sector boundaries. Some issues tend to be apparent

in publicly owned and managed infrastructure. The government's ability to affect or influence infrastructure varies across sectors due to the difference in ownership and varying control over funding regimes: central government (State Highways; State-owned Enterprises in the energy sector; participation in some airports; likely to now extend to the rail network), regional or local government (local roads, water and waste-water infrastructure, ports and airports) and the private sector (telecommunications, energy, some ports and airports). Substantial policy efforts are underway in many sectors.

Problems in SME development

Government economic development policy in New Zealand has changed radically in the past 30 years, with small and medium enterprises taking on more and more a more central role in the formulation of this policy. As a consequence SMEs are now seen as an important vehicle for New Zealand's continued economic prosperity. However, many consider that for SMEs to contribute to the economy in a genuine way there needs to be a greater understanding of the barriers to development faced by SMEs. These barriers are primarily linked to the special characteristics of SMEs, in particular to the fact that most SMEs in New Zealand are owner operated, with characteristics that set them apart from bigger firms. These include less time, difficulties in accessing expert advice, and fewer resources. These characteristics create a situation where development - both for the individual owner manager and for those charged with development at the level of the economy - is challenging. This section lists a range of issues that are frequently cited as being barriers to SME development in New Zealand. Where relevant this section also discusses the various government responses to these issues - the government's response to the sector overall is addressed in the next section.

ISSUE 1: COMPLIANCE

One of the most common complaints of SME owner managers revolves around the difficulties they have meeting the various government regulations and requirements. These complaints (which are regularly voiced through a range of business surveys and/or in reports from the Small Business Advisory

Group) revolve largely around time constraints and a perceived excess of "red tape".

This view is challenged by some empirical evidence, such as the OECD study (OECD, 2001), which compared the cost of compliance in eleven different countries. This study made a distinction between "administrative compliance costs" (filling in forms etc), "capital costs" (capital investments needed for compliance purposes), and "indirect or efficiency costs" which arise when regulations reduce productivity and innovativeness. The study excluded firms with no employees and suggested that in New Zealand the direct cost of compliance is low by comparison with other OECD countries. This provided important information to the government agencies that are charged with reducing the negative impact of compliance in New Zealand and a number of government initiatives have been established to address these issues directly.

The Ministerial Panel on Business Compliance Costs was established in December 2000 to provide advice to the government on ways to reduce unnecessary or over-burdensome compliance costs to business arising from central and local government regulation. The Panel identified a number of concerns that are held by New Zealand firms, and the various reports that were produced as a result of the Panel's work provided the platform for further work by the Regulatory and Competition Policy Branch of the Ministry of Economic Development (MED). More recently the government has shifted its focus from reducing compliance requirements to focussing on the quality of its interaction with businesses. To this end it set up a Quality Regulation Review which seeks to make it easier for businesses to comply with these requirements. Recently the government announced a Regulatory Impact Analysis which will look at the impact of legislation on the ability to do business. The work of this review is heading into its final stages and should be completed by July 2007.

ISSUE 2: MANAGEMENT CAPABILITY

It is clear that most SME owner managers operate their business, especially in the early stages, almost on a survival basis. As a consequence, the New Zealand government has the development of "management capability" as a key tool in the development of effective firms - particularly those that are

small or medium in size. One theme of this work has been to adapt best practice programmes developed in the context of big business to SMEs (e.g. the Criteria for Performance Excellence - more commonly known as the Baldrige criteria). Given the unique nature of SMEs these are usually not adequate or practical for SME owner managers to use. Another theme has been to study the supply of, (and demand for) "management capability building" initiatives compared to "business capability building" initiatives.

This research found that whilst business capability building initiatives are widely available, the provision of management capability building is not as prevalent (Massey, Gawith, Perry, Ruth, & Wilson, 2005, p.73). More importantly, in direct conflict with current government's focus on growth through internationalisation, this study found that what SMEs value as management and business capability does not align itself with growth and internationalisation. Furthermore the ability for owner managers of SMEs to participate in any of the capability building initiatives that the government offers are hindered by lack of time and/or by lack of resources. This study on capability in New Zealand concluded that unless confronted by economic forces such as increased competition, there is no real incentive for owner managers to engage in capability building.

Government attempts to address this problem include the Enterprise Development Grants Capability Building (EDG-CB). This initiative allocates funds to projects to improve capability, profitability and international competitiveness. It not only addresses the issue of management capability but also business capability. Evaluations of these grants have shown that the best results were achieved through the provision of direct advice (through mentoring, expert assistance or training). Furthermore, firms that undertook activities associated with the development of management capabilities, as opposed to business capabilities, reported better results. This reinforces the need for a focus on owner-manager initiatives when it comes to SME policy development.

ISSUE 3: ACCESS TO FINANCE

Access to finance is one of the problems facing SMEs in New Zealand which appears to be more of a perceived problem than an actual one. As with the

issue of compliance noted above, the government has devoted considerable time to researching this issue and has consistently found that in fact this problem is more perceived than real. One of the first studies done on this by the Ministry of Economic Development was done more than 10 years ago (Austin, Fox & Hamilton, 1996). This has developed into a yearly business survey of Business Operations carried out by Statistics New Zealand. The latest of these surveys found that a third of SMEs sought debt financing and 90% of these were successful (MED, 2007).

ISSUE 4: PRODUCTIVITY

The government's overwhelming focus for business development is on increasing New Zealand's role in the global economy and in radically shifting the way New Zealanders traditionally do business. New Zealand's low productivity rate, as compared to other OECD countries, is considered a key problem which needs to be addressed through a series of measures. These include stronger international links, better workforce skills, enhanced management and leadership capability, innovative workplace cultures and greater business and infrastructure investment, more effective business collaboration and networks, and a supportive economic and social environment (MED, 2006b). The government's focus on these issues, in particular the forging of closer international links and the development of innovative workplaces could mean that many SMEs are excluded from the process of growth.

For the government an increase encouraging productivity appears to go hand in hand with encouraging the growth of globally competitive firms. This policy of growing globally competitive firms operates on two levels: to improve the general business environment for all firms in New Zealand and to focus on those firms that have potential to become global. In actual fact the government is pursuing the latter approach more actively, focussing on high growth firms which in many cases are in industries which are likely to access global markets. It also assumes that SMEs should grow and reach the point of internationalisation at some point, which is not always the case (depending on the industry and the owner-manager).

Innovation has been identified as another key to New Zealand's growth by the government policy makers. Innovation implies the need for firms to re-invent themselves continually - both from a production and a marketing point of view. Innovation needs to be supported through the cutting back on regulations that make this harder for businesses to do. And innovation is also very closely linked to research and development and close collaboration between researchers and firms. Currently there is very little collaboration between the vast majority of SMEs and researchers.

ISSUE 5: ENERGY, TRANSPORT AND COMMUNICATIONS

The provision of local infrastructure, including telecommunications, is critical to economic development and has been identified by the Small Business Advisory Group (SBAG) as being key to economic growth. Being connected by broadband is a key element of this provision. Fast, reliable and effective communication is increasingly important for business growth, particularly outside the main cities and towns. However, New Zealand SMEs perceive the New Zealand infrastructure to be wanting, in particular when it comes to broadband. The government is trying to address this problem by implementing a five year plan to improve New Zealand's performance in the information and communications technology as compared to other OECD countries. To this end it has launched the Digital Strategy, to "enhance the contribution ICT makes to New Zealand's overall business productivity" (www.digitalstrategy.govt.nz).

A range of initiatives in the government's recent telecommunications package include unbundling the local loop and encouraging investment in alternative infrastructure such as fibre, wireless and satellite networks. The aim is to provide faster, cheaper broadband for New Zealanders and their business ventures.

The government has also established the Broadband Challenge, a \$24 million contestable fund intended to provide seed funding to encourage building very high speed (1Gbps) urban fibre networks. Funding is also available to provide for lower speed networks in remote and underserved areas and is intended to stimulate interest from communities and local authorities to build open access networks. The Digital Strategy secretariat is also working with Local

Government New Zealand to take open access conduit and fibre requirements into account when developing District Plans.

Developing the SME Sector

During the protectionist era of the 1970s assistance to SMEs in New Zealand was developed in the context of the prevailing economic orthodoxy - that growth was both desirable and achievable³. During this period overall goals were established for the economy that focused to a large extent on expanding the manufacturing sector and expanding the range of exports. To achieve these goals, New Zealand governments in the two decades before 1984 chose to guide the economy by using a mix of policy instruments, with a focus on import and export licensing, price and wage controls, subsidies, taxation and controls on the financial sector.

CENTRAL GOVERNMENT INITIATIVES

This approach to intervention was the government's belief that the full potential of the small business sector could not be achieved in the face of big business and overseas competition without the intervening hand of government. The main vehicle for assistance was the Small Business Agency (SBA), established in 1978.

When the Fourth Labour Government was elected in 1984, a significantly different approach was taken to the economy in general and SME assistance in particular. The new government undertook a massive reform programme, through deregulation, corporatisation, and privatisation. By 1996 thirty-two State Owned Enterprises (SOEs) had been privatised and sold. As a result of the massive redundancies that ensued, there was pressure on the government to strengthen its assistance to SMEs. Instead of increasing support to SMEs, however, the government proceeded to dismantle the framework of programmes that had been in place to support growth in regions that were seen as disadvantaged. 'Small business' was henceforth discarded as a term for government assistance.

The 1987 stock market crash coincided with rising unemployment, partly as a consequence of the restructuring process, and partly as a reaction to international economic trends. The period 1989/90 saw a focus on developing a range of new measures that provided assistance to SMEs through the mechanisms of community-based initiatives. However, 'small business' was not the focus; rather it was 'employment creation' through the establishment of SMEs.

Assistance to SMEs was further boosted in the year leading up to the 1990 election. Here the view prevailed that as large business and government departments were shedding labour, only small businesses offered jobs. SMEs were an attractive policy target, due to an assumed modest requirement for resources, and the ease with which programmes focusing on small firms could be implemented. There was a feeling that small amounts of assistance could be given (in the context of employment creation rather than SME support) without detracting from the overall policy approach of non-intervention.

However by 1996 the government reintroduced the term SME into policy statements, specifying SMEs as a particular target group. A review of enterprise assistance signalled the government's new priorities, to expand the role that local communities were already playing in economic development. To this end the BIZ programme was established in the late 1990s to build management capability amongst SME owners and managers (in this context SMEs were defined as firms employing fewer than 20 employees). The primary focus for the programme was to be the assessment of business needs and the delivery of training and seminars, one-on-one mentoring, and networking. To deliver the programme, the Ministry of Economic Development (MED) contracted appropriate agencies to offer a range of training programmes and information services, and the 46 organisations appointed to deliver management capability services included a range of non-governmental organisations.

A referral service (known as BIZinfo) was also established, provided by a national consortium through a free telephone service, a website and 34 local BIZinfo 'shops'. BIZinfo's initial focus was on developing a database of 2,500 training courses and other services (provided by some 900 organisations).

While the BIZ programme was being introduced to strengthen the capacity of existing SMEs, the government was also addressing the broader issue of enterprise and entrepreneurship, at a more conceptual level. After consulting with communities and business groups throughout the country, the Bright Future policy document was released (Ministry of Commerce, 1999). Focusing on five 'steps ahead' ("lifting our skills and our intellectual base; better focusing the Government's efforts in research and development; improving access to capital; removing the red tape stifling innovation; promoting success; and supporting creative and innovative New Zealanders"), the policy document presents quite a different set of objectives from that of the existing business development policy (which focuses on SMEs).

This important policy position resulted in the establishment of the Growth and Innovation Advisory Board (GIAB) in 2002, which developed the Growth and Innovation Framework (GIF). The various documents released by GIAB describe a set of strategies for encouraging those responsible to running New Zealand firms to become more innovative - with the assumption that this will help the firms grow.

The government's efforts to continue a more conceptual debate about these issues continued with the GIAB encouraging "a national conversation between groups and individuals about what growth and innovation mean" (GIAB, 2004, p.1). To this aim it commissioned a research into New Zealanders' attitude to growth (UMR, 2004). Interestingly, the research identified that economic growth was not a motivator for many young New Zealanders due in part to the massive economic reforms New Zealand underwent in the late 1980s and early 1990s. Therefore the concept of growth needs to be made meaningful to New Zealanders in general and SMEs in particular for businesses to grow successfully. Innovation, however, was found to be an attribute that New Zealanders could identify as part of a national trait, linked to resourcefulness and practicality.

THE ROLE OF LOCAL GOVERNMENT

New Zealand also operates a system of local government with 86 local authorities. Of the 86 councils in New Zealand 12 are regional councils and 74 are territorial local authorities. The role of regional councils is predominately

planning and regulation of the environment and catchment management issues. Some of the major metropolitan regional councils have functions of urban transport, bulk water and in some cases bulk disposal of sewage. Regional councils are funded from regional land taxes (rates) based on property values, with little or no financial support from central government.

Territorial local authorities are also locally funded through land taxes, provide local services and are locally accountable to their communities. Their functions are wide ranging and include infrastructure management, recreation services, planning, and local regulation such as dog control, building control and local bylaw enforcement. In the past the functions that local authorities have undertaken have been subject to the constraints of legislation but they are now able to undertake any functions provided they have the support of the local community (Local Government New Zealand, 2007).

With reference to infrastructure, that is roading, water, wastewater, storm water and solid waste services (refuse), an exception to the local funding of local government functions that are funded locally is roading, where approximately half the funds are received from central government. The central government income for roading comes from commercial road user charges (based on truck weight and distance travelled) and from a petrol excise tax of approximately 12%.

Roading infrastructure

As approximately 50% of local government roading maintenance and construction funds are from central government, the funds are tagged by requiring that all physical works be publicly tendered. This change took place in the early 1990s where there was previously a mix of local government direct service provision and private sector provision, to now being a 100% private sector provision. The experience has been that significant reductions in cost have been achieved and since that time there has been a trend towards larger contracts (network maintenance) and longer term contracts. The extent of competition in the private sector has been of concern and the experience is that there are now only four major companies bidding for these larger contracts in New Zealand. There are, however, some concerns that competitive pressures may not be sufficiently strong.

Transit New Zealand - the government owned roading agency, maintains approximately 12% of the nation's roading network by length - the main roads and state highways. They have recently developed a procurement policy where a third of the contracts with the private sector will be for a 10 year period. These contracts are called performance specified maintenance contracts - they are not prescriptive and the contractual outcomes are very broad. To date Transit New Zealand's experience has been that significant further savings over conventional shorter term contracts have been achieved - of up to around 30%. These contracts also include the professional engineering services of project management, design and supervision.

The use of formal public/private sector partnerships in roading has been reasonably limited to date in New Zealand. The Land Transport Management Act 2003 (Transit New Zealand: Ararau Aotearoa. (2005) provided legislation to allow for public/private partnerships for roads. These provisions require partnership agreements to be for a specified term, the assets at all times will be operated under public supervision and all assets will become publicly owned at the end of the agreement. It is expected that these types of arrangements in New Zealand will be on the main roads, will be few in number, and will be associated with the introduction of toll roads. (Currently there are no toll roads in New Zealand, although there have been three instances of these being constructed in the last 40 years).

Water utilities and services

With regard to the infrastructural services of water, wastewater and storm water, this is solely provided by local government in New Zealand. Up until 15 years ago these services were provided directly by local authorities' staff but with the growing trend toward outsourcing, it is estimated that up to 50% of the maintenance of these services is now contracted out. Traditionally major new capital work has been outsourced to the private sector, typically in oneoff project contracts. However in recent years there has been a trend to adopt some of the international models - design build operate (DBO), build own operate transfer (BOOT), and design finance build operate transfer (DFBOT), particularly for wastewater treatment plants. Some of the terms of these contracts have been typically for 25 years.

Only one small urban local authority has entered into a concession/franchise arrangement for the maintenance of its water, wastewater and storm water network. The term for this contract was 30 years with the right of renewal for a further 20 years, and was reasonably controversial in New Zealand. As a result legislation⁴ prohibits contracts for the management of whole systems for water, wastewater and storm water for any longer than 15 years. This would not prevent 25 year public/private partnerships for components of the system such as a wastewater treatment plant.

National and urban rail networks

Longer term public/private partnerships allow the provision of urban rail systems where the land and the physical infrastructure remains in public ownership but maintenance of the infrastructure and the rolling stock is the subject of a long term concession/franchise. Toll NZ has exclusive rights until 2070 for freight, long distance passenger operations and metro passenger services in Wellington. Urban rail is provided by Connex New Zealand in Auckland under contract to the Auckland Regional Transport Authority. Toll NZ freight and passenger rights are subject to 'use it or lose it' provisions. New operators will be able to operate long-distance passenger services on routes not serviced by Toll NZ from July 2007. Other operators can exercise their existing rights on the network and can be granted rights to line segments where Toll NZ is unable to meet its 'use it or lose it' obligations or does not take up its right to operate over new sections of the network.

2006 & BEYOND: A FOCUS ON "ECONOMIC TRANSFORMATION"

In 2006 the government launched the economic transformation agenda as a key priority for the government over the next decade. This policy seeks to address the issues that have arisen due to the globalisation of the economy, and New Zealand's position in the world as economies around the world become more and more competitive and interconnected. In the government's view internationalisation is particularly important for New Zealand given its small size and has based this emphasis on growing the economy on the premise that "export intensity will play a role in increasing our productivity levels" (MED, 2006b, p.11). The focus of this economic transformation agenda lies heavily on two key aspects, innovation and internationalisation.

Because New Zealand does not rate highly against other OECD countries in terms of productivity, the government also wants to address this issue.

The economic transformation agenda revolves around five themes:

- to grow globally competitive firms,
- to develop a world class infrastructure,
- to promote innovative and productive workplaces,
- to make Auckland an international and competitive city and
- to encourage environmental sustainability.

Within this framework, the government has several policies in place that address SMEs, in particular to encourage their internationalisation and to foster innovation. For example, to encourage New Zealand businesses to engage in the global economy, 2007 was branded as "Export Year" with a focus of encouraging SMEs to export as well as "increasing New Zealand's long term export performance" (www.exportyear.co.nz).

The government has also recently announced a new regional development policy with the creation of the Enterprising Partnerships Fund. This fund seeks to encourage regional projects that are commercially driven and to generate economic benefits to the region through partnerships between business, industry, local governments and education, training and research organisations. The overall aim is to develop and implement regional strategies that will improve the business environment with a sharp focus on increasing the numbers of internationally competitive firms.

Along with these new initiatives the government has continued to support existing business assistance programmes which focus mostly on building business and management capability. These are designed to address market failures and have four key objectives: to improve access to finance, increase internationalisation, increase innovation and support new business and provision of information (MED, 2006b). The assistance is delivered through

the Biz portal in partnership with other government agencies, economic development agencies and chambers of commerce.

Addressing the needs of capability development have also resulted in the formation of the Business Capability Partnership (BCP) which is a private-public partnership aimed at enhancing business and management capability in New Zealand. This body seeks to enable enterprises to improve their management and business capability and, as a result, boost their business success. For BCP business capability has a direct impact on business success and many New Zealand enterprises have scope to improve their capability. Because in some instances the market of services that are available to enhance business capability is cluttered and confusing, and there is also a high degree of variability of quality, appropriateness and accessibility, New Zealand enterprises would benefit from: clear signposting of services available; filling gaps in delivery, and; greater shared knowledge of the drivers of business success.

Other initiatives that impact on SMEs include the Workplace Productivity Project run by the Workplace Productivity Working Group (WPWG) of the Department of Labour which seeks to improve productivity through collaboration between government, industry, firms and unions. Another project to facilitate SME business practices revolves around concerns from owner managers that they spend too much time complying with different government regulations. One of the latest surveys on this issue appears to confirm that SME owner operators find that complying with tax and employment related issues the most demanding on their time. (BusinessNZ-KPMG, 2006).

Undoubtedly today New Zealand society has evolved to the point where people's expectations about what work means have an impact on what choices they make. As found in the above mentioned study, growth on its own is not always a motivator for some New Zealanders, and this certainly appears to be the case with the owners and managers of many SMEs. Instead, other issues such as work-life balance and being 'your own boss' may motivate SME owner managers more, especially if they are micro-enterprises. Given the fact that micro-enterprises make up such a considerable part of the New Zealand economy, for government policy to be effectively implemented their unique nature needs to be taken into account.

PUBLIC-PRIVATE PARTNERSHIPS

A particular focus of the PECC project is on identifying feasible solutions to the complex topic of SME development. One of these approaches may be the establishment of public-private cooperative efforts. This section provides some examples of this type of effort in New Zealand - known generally as "public-private partnerships" (PPPs).

Typical examples of infrastructure concession agreements where a government agency awards a long-term contract to a private party to design, build and operate a facility that provides services either to the public or to the government agency, include toll roads, prisons, water treatment plants, military training facilities. There have been very few PPPs of this kind undertaken in New Zealand and there have been no substantial PPPs entered into by a central government agency. New Zealand no longer has a Ministry of Works and design and construction is almost always contracted out to the private sector.

While operation and maintenance is often carried out by the public sector, this is not always the case. For example, Transit New Zealand (the agency responsible for building and maintaining state highways) contracts out all maintenance of state highways as well as design and construction. Another example is the Auckland Central Remand prison, the operation of which was contracted out in 2000. However, in this instance the management contract was not renewed in 2005 as a result of the Corrections Act 2004.

A further example is the Auckland Indoor Arena, an entertainment and sporting events centre entered into by the Auckland City Council in May 2004. The main reason for choosing a PPP approach in this instance was that the Council does not understand, and has no experience in operating, a major events venue. The private sector partner, who agreed to build, own, operate and maintain the Arena for 40 years, has the experience and skills to run this kind of business and is responsible for operations and carries the risk. At the expiry of the contract, ownership of the building and the operating systems will be transferred to the Council.

Local Authority Trading Enterprises and joint ventures

A further variation of public/private partnerships is joint ventures that local authorities are able to establish. These are known as Local Authority Trading Enterprises (LATEs), where they have 50% or more of the shareholding. There are a number of cases where local authorities have established these partnerships to undertaking road and other maintenance contracts. Some have used this mechanism as a stage in divesting themselves of the function and have subsequently sold off their shareholding as a viable commercial entity.

Asset management planning and policy

One of the important ways that has been developed to ensure the integrity of infrastructure assets in New Zealand is through asset management planning. This has been driven through financial reporting requirements and asset valuation. Asset management plans are now in widespread use and are becoming increasingly sophisticated.

There are no specific policies, rules, or tender documents for awarding contracts to SMEs at the level of Land Transport NZ; although some may have this effect they are not structured for this purpose. Transit NZ does however have an informal policy of allowing contracts under NZ\$100,000 for consultants and \$200,000 for physical works to be awarded to SMEs or other new entrants without going to open tender where it is believed that this will allow them to prove themselves or develop their category ratings in order to be able to tender for larger projects. In this area risk is moved to the private sector by requiring bonds to be provided for large projects (i.e. a lending institution assesses the ability of a company to undertake the project and provides the bond accordingly).

Emerging developments

The experience with public/private partnerships in New Zealand has evolved from traditional full public sector provision, to both mandatory and voluntary outsourcing for shorter term contracts and this is now evolving into longer term contractual arrangements. Also emerging is the development of conventional public/private partnerships such as DBO, and BOOT and

DFBOT. Joint ventures, particularly for the maintenance of infrastructure, have also been common. While there has been some disquiet over these trends, the legislative framework provides ample scope for continuation of these changes and seems generally to follow international trends in procurement.

Estimating, quantitatively, value for money delivered by these projects is subject to much debate, especially since they are in the early stages of their contracts and there is little empirical data available for analyzing the costs and benefits. It is believed, however, that PPPs will need to be adopted eventually with major capital works initiatives for expanding and/or developing key infrastructure, such as major roading projects and telecommunication networks.

This approach continues to be controversial and has been resisted by both the government and the general population, where the public perception has been that some but not all of these projects have succeeded (IPENZ, 2002) and it is unlikely that the present government will engage in major PPP initiatives. According to a 2006 Treasury policy paper (Katz, 2006), the main arguments against this approach from New Zealand's perspective are that there are other ways of obtaining private sector finance without having to enter into a PPP (and financing of such projects is not at present an issue for New Zealand); that most of the advantages of private sector construction and management can also be obtained from conventional procurement methods (under which the project is financed by the government and construction and operation is contracted out separately); that the advantages of PPPs must be weighed against the contractual complexities and rigidities they entail and which are avoided by the periodic competitive re-tendering that is possible under conventional procurement. The Treasury paper concludes that PPPs are worthwhile only if all of three conditions are met. These are that the public agency is able to specify outcomes in service level terms, thereby leaving scope for the PPP consortium to innovate and optimize; that the public agency is able to specify outcomes in a way that performance outcomes can be measured objectively and rewards and sanctions can be applied; and that the public agency's desired outcomes are likely to be durable, given the length of the contract.

The IPENZ report (2002) on the potential application of PPPs in New Zealand also highlights the small population and low population density as further reasons that fully private-sector funded PPP projects are unlikely to be as economically attractive as they are in some other countries. However, partial funding (where private sector operators compete by tendering for the lowest government subsidy or capital injection) may widen the scope.

Concluding comments

Since the 1970s, when the significance of the SME sector began to be widely recognised, a reasonably substantial literature has developed on how to create an environment that encourages development (for example Haskins & Gibb, 1987; Neck & Nelson, 1987; Van de Ven, 1993). However, given the wide variance in the way business and/or economic development is approached (in response to widely different circumstances) it has not yet been possible to develop a blueprint for best practice enterprise assistance. Those that have attempted to do so have established little common ground or have become bogged down in arguments of detail (for example see the debate between Bryson, Churchward, & Daniels, 1997 and Hutchinson, Foley, & Oztel, 1996 on the development of a typology of delivery agencies).

The result is that there is no single recipe for successful SME development that takes into consideration the differing contextual factors in each country. The situation is exacerbated by the difficulty of effectively evaluating the impact of policy, and the relative infrequency with which this occurs. Alan Gibb argues that the lack of robust evaluation research is just one of a number of factors that has led to the field of SME development being built upon "ignorance, mythical concepts, myths, assumptions, rituals and confusions" (Gibb, 2000, p13). The existence of 'fads and fashions' of policy making, and the absence of adequate analysis of the way in which the different policies have evolved have led to programme design that ignores country-specific factors. This in turn encourages fragmentation, policy and programmes that are incongruent and where the genuine learning from the experience of other countries is replaced by the indiscriminate adoption of ideas that do not necessarily fit.

This can only be avoided if policymakers (and in the broadest sense of the term this includes politicians, academics and other economic commentators as well as those working within government agencies) make a genuine effort to understand the history of policy development in their own country and attempt to assess the impact of these policies. Only when this fundamental understanding is in place can those involved correctly assess the value of the lessons learned by their counterparts in other countries.

In relation to this last comment, this paper offers a review of the New Zealand situation, and aims to make a contribution to the debate that is currently occurring on how best to encourage economic growth.

In summary, this demonstrates that over the last twenty years a substantial shift in the ideology of SME development has taken place in New Zealand. Central government is now focused on transforming the whole economy, through the means of SMEs, and there are a number of examples of initiatives where government leadership is being provided to other parties from the private and voluntary sectors.

The legacy for the SMEs of today is an economy that has, over the years, both debated and experimented with different approaches to business development. Although there has been a general non-interventionist approach by governments since 1984, the governmental response has changed over the years, and assistance for SMEs remains - and in fact has increased over the last decade. However, this assistance no longer comes directly from government, which has remained consistent to the non-interventionist philosophy established by successive governments. The key assumption of this philosophy is that a liberal economy ensures an optimum number of firms through the operation of the market. New firms are created by normal competitive market forces in industries where opportunities for profit exist, and others disappear from industries where demand has declined. If there are business opportunities that favour SMEs, in the absence of artificial barriers these will be exploited without any necessity for significant government intervention. Under this philosophy, lame ducks are not supported, and businesses must survive on their own merits.

The consequence of this way of thinking in relation to economic development is the tendency for the government to move to a more indirect approach. Instead of actively assisting firms on an individual basis, there is a focus on minimising barriers to SME progress by ensuring the economy is open and competitive. This is part of the wide-ranging programme of reform that has focused on restructuring the economy to eliminate inefficiency and promote competition.

As government has moved to a less hands-on role in business and/or economic development, an opportunity has been created for other parties to take over this role - in partnership activities. While to date there are few examples of long standing public private partnerships that have been specifically established to encourage the development of SMEs, the Workplace Productivity Working Group and the Business Capability Partnership are encouraging signs that this approach is being considered.

In the context of this project, this may be the key lesson from New Zealand.

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Notes

1. Economically significant enterprises is a term used in New Zealand to describe an enterprise which meets at least one of the following criteria: Has greater than \$30,000 annual GST (goods and services tax) expenses or sales; has more than two full-time equivalent paid employees; is part of a group of enterprises; is a new GST registration that is compulsory, special or forced (this means the business is expected to exceed the \$30,000 boundary).
2. The Resource Management Act 1991 (RMA) is the main piece of legislation that sets out how the environment is to be managed.
3. This section draws substantially upon Massey, C., & Jurado, T. (2005). The support infrastructure for New Zealand firms. In C. Massey (ed), *Entrepreneurship & small business management in New Zealand* (pp.17-36). Auckland, New Zealand: Pearson Education New Zealand Ltd.
4. For example the Local Government Act 2002.

SME Development in Singapore

Of Entrepreneurship Infrastructure and SME Strategies

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Introduction

Local enterprises in the form of small and medium-sized Enterprises (SMEs) need to be fostered in any economy. They form the little acorns from which large enterprises and future multinationals grow. There is a need for a vibrant SME sector. Much research has shown these enterprises account for job creation, innovation and entrepreneurship in many economies.

Yet they face constraints for their growth depending on the prevailing industrial and market conditions. To develop vibrant local enterprises, there is a need for relevant and appropriate policies to address the needs of SMEs. SME policies put in place in economies do much to help them in their development. Yet the policy offerings whether by way of incentives, assistance, regulations, law, information, are shaped by the state of development the SMEs are in, the desired economic development outcomes in particular the development intentions for SMEs, the environment conditions among other factors.

In this paper we examine the environment of SME policies in Singapore and how these policies have developed. This paper begins with a discussion of the SME policies in general introducing the concepts of entrepreneurship infrastructure and SME strategies. It then proceeds to argue that underlying all SME policy offerings is the role of entrepreneurship infrastructures and what they provide. It then proceeds to discuss the entrepreneurship infrastructural provisions in Singapore over time in the third section.

SME Policies

Size and SME Policies SMEs have been variedly defined in the many economies. Most economies use employment size or size of capital as a means of defining SMEs for policy purposes. However, there is no universal definition. A recent compilation of definitions by the APEC Secretariat is shown in Table 1.

Table 1: Summary of Main Definitions of SMEs in selected APEC Economies

Country	Definition of SME	measure
Australia	Manufacturing - less than 100 employees Services - less than 20 employees	Employment
Canada	Manufacturing less than 500 employees Services less than 50 employees	Employment
PRC	Varies with industry, usually less than 100 employees	Employment
Indonesia	Less than 100 employees	Employment
Japan	Less than 300 employees, or ¥10 million assets Wholesaling - less than 50 employees, ¥30 million assets Retailing - less than 50 employees, ¥10 million assets	Employment/ assets
Korea	Manufacturing - less than 300 employees employment Services - less than 20 employees	
Malaysia	Varies. Less than RM 2.5 million and less than 75 employees. Definitions are for SMI. Different for Bumiputera enterprises	shareholders funds employees
Philippines	Less than 200 employees, P 40 million	Assets Employment
Singapore	Manufacturing - less than \$12 million fixed assets Services - less than 100 employees	fixed assets employment
Chinese Taipei	Manufacturing - less than NT\$ 40m paid up capital and less than total assets of NT\$120m. In business, transport, and other services - sales of less than NT\$ 40m.	paid up capital assets and sales
Thailand	Less than 200 employees for labor intensive Less than 100m Baht for capital intensive	Employment Capital
USA	Less than 500 employees	Employment

Source: Hall, C. 2002.

For the purposes of this paper, the definition of SME is less important than an understanding of the policies. Hence we shall not delve into the discussion on the merits of the definitions suffice to note that the criteria employed are indirect manifestations of the underlying policy. An economy that chooses to support growing enterprises might not provide any assistance to the smaller enterprises. By defining SMEs to be a certain size, an economy would exclude smaller enterprises.

Entrepreneurship vs SME Policies. Lundstrom & Stevenson (2005) draw a distinction between SME policies and entrepreneurship policies. The first are policies addressing SMEs in general. Entrepreneurship policies, on the other hand, may impact selected SMEs at the startup phase, but seek to develop venture creation and/or entrepreneurial spirit in the economy. Entrepreneurship policies unlike SME policies that specifically target enterprises, could address the general climate towards entrepreneurship. As such, entrepreneurship policies could address children in schools, the education system, the media and the role models that are depicted on national television for example that could inspire individuals to start businesses. There is undoubtedly some overlap between these two types of public policy.

Lundström & Stevenson (2005) differentiated between the two categories nonetheless and Table 2 below reproduces their comparative table. In Singapore, policies addressing entrepreneurship have been dealt with as part of SME policies.

Table 2: Characteristics of SME Policy and Entrepreneurship Policy: A Comparison

Characteristics	Traditional SME Policy	Newer Entrepreneurship Policy
Outcome	Firm growth, productivity growth.	Growth in entrepreneurial activity (i.e., in number of business owners and firms).
General goal	Create a "favourable business climate" (e.g., tax regime; marketplace frameworks; reduced red tape).	Create a 'favourable entrepreneurial climate and culture' (e.g., few barriers to entry, promotion of entrepreneurship in society).
Specific objective	To help individual firms modernize, expand or improve competitiveness.	To encourage more people to start their own businesses and provide opportunities for them to learn about the entrepreneurial process and develop the necessary skills.

Table 2: Characteristics of SME Policy and Entrepreneurship Policy: A Comparison

Characteristics	Traditional SME Policy	Newer Entrepreneurship Policy
Focus	On firms rather than individuals.	On individuals rather than firms.
Stage of business cycle	Primary focus is on support after the business has actually started.	Support is offered in the nascent stages as well as during the critical first years of start-up.
Client groups and targeting	Existing firms. (Often) targets high growth sectors or high growth firms (i.e., "picking winners" approach).	Nascent and new entrepreneurs. Targets the general population and (often) segments within it (e.g., women, youth). Generally no sector targeting.
Policy priorities	Reduce red tape and paper burden for existing SMEs	Reduce procedural, regulatory and taxation barriers to business entry.
	Improve access to financing	Facilitate access to micro-loans, seed capital and other start-up financing.
	Improve SME access to information (provide business, economic market, government regulatory and programme information).	Improve access to start-up information and advice, entrepreneurial know-how.
	Facilitate SME's access to domestic and international markets (e.g. tariff reductions, export subsidies).	Facilitate networking activities and exchanges to promote peer-learning, partnering and dialogue.
	Improve the competitiveness of small firms (e.g. management skills, strategic consulting).	Increase opportunities for people to learn the entrepreneurial process and skills for starting a business (e.g., education, training); enhance the quality of start-up support services.
	Foster R&D and technology adoption among SMEs (e.g., technology transfer).	Create awareness of entrepreneurship as a viable option (e.g. profile role models, influence public attitudes).
Primary policy levers	Use of financial/fiscal incentives to lever specific SME activities (e.g. R&D investment, exporting).	Greater use of non-financial levers (except in the case of start-up and seed financing).
Time period for results	More immediate (aims for results over a three-to-four year cycle).	More long-term (process perspective requires time).

Source: Lundstrom & Stevenson (2005).

Some areas of overlap could exist in training as nascent entrepreneurs and SME owners may require training in management and business processes. Both categories of individuals may require professional assistance from lawyers and accountants. They would need information about industry sectors and country market information should they seek to export or establish new ventures abroad. As such for the purposes of this paper, we adopt the same approach as adopted by the Singapore policy makers not differentiating between the two types of policies.

Entrepreneurship Infrastructure: the means. If one were to take a step back from the specific policies captured within SME and entrepreneurship policies, it would be possible to see that the measures constitute what my colleagues and I have called "entrepreneurship infrastructures" (Tan, Young and Tan, 2000). While industrial infrastructure represents the place-specific notion of the facilities and services underpinning all of the industry and populations residing within a given location (Vaughn, 1983; Porter, 1990), entrepreneurial infrastructure, represents a sub-set of the more general industrial infrastructure concept. Entrepreneurial infrastructure represents the facilities and services present in an economy which encourage the birth of new ventures and the growth and development of SMEs.

The idea of entrepreneurship infrastructure had been considered by other researchers. Entrepreneurial infrastructures include: (a) the development of resource endowments for basic knowledge, (b) financing mechanisms, (c) competent labor, and (d) an institutional governance structure which legitimizes, regulates, and standardizes the activities of industry members (Van de Ven (1993). Another explicit reference to the "new venture infrastructure" concept was made by McMullan and Long (1990). McMullan and Long (1990) considered the components of a "new venture infrastructure" to be entrepreneurship education, incubators, and venture capital. They considered these components of the infrastructure to be complementary and mutually supportive of each other.

Entrepreneurial infrastructures provide support to potential new business owners, owners of small growing businesses, and existing small and medium-sized businesses in the form of: (1) assistance with tasks which the business owner or small firm must accomplish, (2) resources - physical or monetary, (3)

information, and (4) knowledge. Such infrastructures are important for community economic growth and development because communities can influence the level of entrepreneurship activity within their domains by influencing elements within the entrepreneurial infrastructure (Bull and Winter, 1991).

Assistance with Tasks: Conceptually, one can consider the tasks which the business owner performs within the operating domain of the business as internal tasks. Such internal tasks would include planning, directing, and organizing various functional activities of an enterprise. Likewise, one could consider tasks performed by others, in various functional areas, within the boundary of the enterprise as internal tasks. Using these perspectives pertaining to internal task processes, the decisions of individual entrepreneurs or representatives of businesses to seek assistance in performing their tasks, from entities outside the business, can be viewed as decisions to form boundaries with external individuals or organizations (Mackenzie, 1986).

Required Resources: physical or monetary In order to function effectively, business owners and small firms require facilitative resources. For instance, with regard to business creation, potential business owners require adequate physical accommodations and capital. To the extent that physical facilities and installations exist and are able to accommodate aspiring business owners (e.g., incubators) and growth-oriented businesses (e.g., industrial parks) or, that capital sources are adequate (e.g., venture capital firms), the infrastructure support network is effective.

Required Information: Growing SMEs require information in order to effectively carry out their work. For instance, information is needed regarding the environment. Such helpful information, which can assist business owners in making effective decisions, would include economic, market, legal, technological data, and other environmentally related data. This information and data could be made available from facilities established within the entrepreneurial infrastructure.

Required Knowledge: SMEs will be ultimately successful only if the business owner or firm has attained a level of knowledge which is adequate for accomplishing the tasks with which they are faced. Such knowledge,

which is stored in the business owner's long-term memory, can be acquired by experience through trial-and-error while operating the business (Reuber and Fischer, 1993). However, entrepreneurial knowledge can also be acquired through formal training in the concepts and skill areas which can be directly applied within the business venture (e.g. Barnes and Jones, 1995; Gosh and Block, 1993). When facilities exist to encourage the transfer of such knowledge, these facilitates are said to be components of the entrepreneurial infrastructure.

To illustrate the concept of entrepreneurship infrastructure Table 3 below maps some of the elements present in Singapore's entrepreneurship infrastructure at present. There are a host of government assistance programs in Singapore that address the needs of SMEs. They can be found at the new website created for the purpose: EnterprriseOne (www.enterpriseone.gov.sg).

Table 3: Illustration of Singapore's Current Entrepreneurship Infrastructure

Assistance with tasks	Required Resources	Information	Knowledge
Management consultants whose charges are reimbursable under the <i>Local Enterprise Technical Assistance Scheme</i> .	SMEs can seek financing from the financial institutions under the <i>Local Enterprise Financing Scheme</i> where the loans are guaranteed by the government.	The National Library Board is planning to provide an information search service for SMEs funded by the government SME agency.	Executive programs designed to equip SME CEOs and offered at the three local universities: National University of Singapore, Nanyang Technological University and Singapore Management University.
Enterprise Development Centers have been funded and established in the past two years at industry associations to assist their SME members.	<i>Loan Insurance Scheme (LIS)</i> SMEs can secure loans by getting them insured against default. The government will subsidize 50% of the insurance premium.	Information is available through the SME First Stop Hotline. The SME First Stop links the enquirer to the relevant agency and information sources.	<i>Short courses</i> organized by various consulting firms, professional bodies and commercial schools that SMEs can avail themselves to.

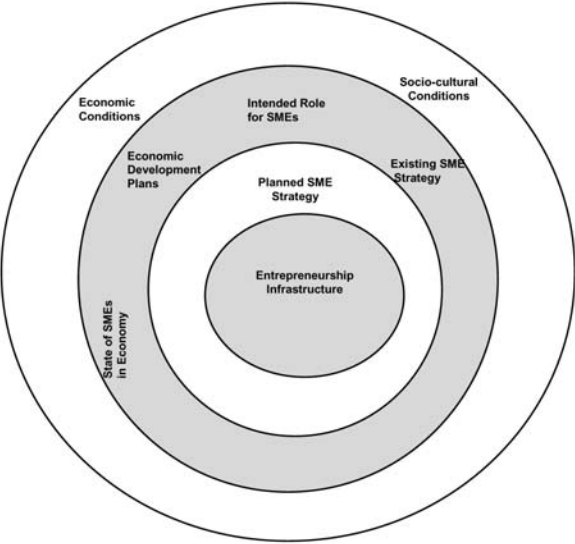
SME Strategy. Entrepreneurship infrastructures are the means for SME policies. In truth the SME policies are contingent on the strategies that the policymakers have decided upon for the SMEs. If SMEs are not the primary focus of economic development attention, the level of incentives offered to them, the amount of public finance allocated and the types of programs developed, would differ. The Taiwanese government, for example, placed an emphasis on the development of SMEs and technology diffusion to its SMEs, hence the priority in policies and the presence of the SMEA, which has a higher profile and role than other economies. In recent years, other economies have followed with the establishment of the appointment of a minister for entrepreneurship as in Malaysia. Singapore appointed its first minister-in-charge-of-entrepreneurship in 2003.

While we have used the term SME policies, at this point we introduce the term SME strategy because the word "strategy" connotes direction and purpose. Further, it allows us to discuss measures at different levels of strategies and capable of addressing different groups in fashion the term is used in corporations to speak of corporate strategy as opposed to business strategy, and strategies on for different functional areas such as marketing and human resource, or globalization. SME strategies can be broad based or narrow in their reach. Just as in corporate strategy where the strategies could be for the whole corporation, for specific business sectors, for specific units, SME policies could address all SMEs (broad) or SMEs in specific sectors (narrow). An education programme to train up managers with skills SMEs would be a broad SME strategy. Raising the productivity of SMEs in general through incentives, training for the development of work improvement teams, a national campaign to raise awareness of productivity among SMEs, etc. is another example of a broad strategies at the enterprise level as opposed to affecting their environmental factors such as regulations, labor force, wage levels, etc..

Plans to introduce new technologies and to expose the SME owners in the furniture manufacturing sector to best practice is an example of narrow-based strategy at the sector level. Establishing a retail promotion centre to help retailers improve their store looks, lighting, processes and service is another example of a sector strategy.

The choice of strategy and accompanying entrepreneurship infrastructure is a result of various factors. These considerations need to be borne in mind when evaluating the SME policies of any economy as the policies are contingent upon local conditions. An attempt to depict these factors is shown in Figure 1 below.

Figure 1: Factors Shaping SME Strategy



The general economic conditions would have an impact on the economic development plans. Here attention has to be paid to the international trends that are likely to impact the economy and the SMEs. As the emphasis is on strategy, there is a need to take the long term view and look far out into the future. The SME strategy would apply for a period of time into the future. In addition to the economic conditions which includes the stage of economic development in the economy, the socio-cultural conditions play a role in shaping the SME strategy. In a society where entrepreneurship and innovation are highly regarded different approaches to SME development would be required as opposed to economies where the socio-cultural preferences is for employment or where there is great shame and fear attached to failure. If

business failure is frowned on and if there is shame associated with it, the effort to develop SMEs would differ. For one thing, there would be less new startups under these conditions.

The prevailing conditions in an economy would shape its economic developments plans. These plans would take into account the role for SMEs, shaping the existing SME policies. Those factors together with the state of the SMEs influence the SME strategy planned and the resultant entrepreneurship infrastructure.

The way in which the factors are considered can be seen in the process for the development of SME strategies in Singapore. We outline the strategies in the next section and they have taken the form of two SME masters plans (1989 and 2000). The process undertaken in Singapore involves an understanding the profile of SMEs in Singapore at the time that the master plans are being developed. The committees responsible then conceived of the role SMEs would play in the future and in the economic setting in Singapore and internationally. Hence, the master plans that were produced invariably spoke of the future, global trends and the anticipated role for the SMEs.

Bearing in mind that a myriad of factors influence the SME strategies, it goes without saying that the SME strategies being adopted or introduced at any point in time would be subject to the existing state of SMEs in the economy. The strategies need to be appropriate for the SMEs and future SMEs to be developed. Hence, in evaluating SME strategies, it is necessary to consider these factors and to be mindful of the conditions on the ground.

Singapore's SME Strategies¹

An overview of Singapore's SME strategies since 1965 is provided in Table 4. Singapore became a nation with its independence in 1965. Prior to independence, there were no SME policies of note. The development of the Singapore government's policies towards the Small and Medium-Sized Enterprises (SMEs) today can be traced back to Singapore's independence since the mid 1960s. In the 1960s, Singapore's position as a regional entrepôt was threatened from the rapid developments of the competing ports of her

neighbors. The then government thus decided to leapfrog the industrialization process by focusing on a production-based economy. Dr Goh Keng Swee was the architect of this plan. Foreign direct investments were harnessed by inviting foreign multi-national corporations (MNCs) to make huge capital investments locally through the building of factories to support manufacturing activities. With the constraints - of the largely untrained small population of 1.6 million and the lack of natural resources - faced by Singapore, all government policies were crafted to support the export manufacturing activities of the foreign MNCs anchored locally to allow them to flourish. The successful gearing up of the workforce met the labor requirements of the MNCs but there were no government policies expressly addressing the development of SMEs.

The watershed year for SME policies was 1987, with the publication of the economic report that addressed new directions for the Singapore economy after the recession in 1985. In review the economic directions for Singapore is it sought recovery from the economic recession in 1985, the Economic Committee noted the contribution of SMEs to the Singapore economy. At that time, SMEs although constituting 90% of the total number of establishments, lagged behind their foreign counterparts in productivity, management skills, marketing and technology.

Singapore economic development had seen it develop as an international manufacturing base. However, looking ahead into the 1990s the Committee saw the need for Singapore's inclusion of other activities to become a major mode for global business. There was a need to extend beyond manufacturing to encompass the full spectrum of business activities - from research and development to design and product development, production, marketing, distribution, finance and international business management. SME development became important as they constructed a key component of the strategy to develop Singapore's services and manufacturing as the twin engines of growth.

Following the Economic Committee's report, the Economic Development Board (EDB) of Singapore initiated a multi-agency effort to draft a master plan for SME development. Six government agencies² - the National Computer Board (NCB), National Productivity Board (NPB), Singapore Institute of Standards and Industrial Research (SISIR), Singapore Tourist

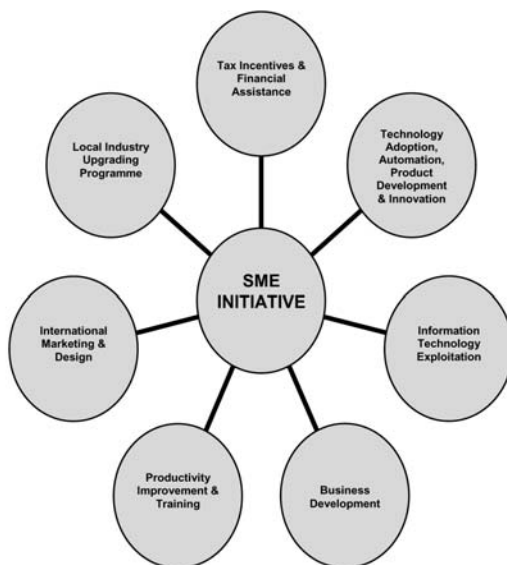
Promotion Board (STPB) and the Trade Development Board (TDB) came together under the umbrella of the SME Committee to examine the issues and brainstorm on ways to develop a vibrant and resilient local business sector. The resultant master plan had 5 strategic thrusts mentioned in Table 4 below.

Table 4: Overview of Singapore SME Strategies

Years	SME Strategies	Remarks
Before independence	British colonial rule - no discernible SME strategies.	Not apparent.
1965 - 1985	Industrialization with SMEs being subsumed under the focus on attracting multinational corporations.	SMEs acted and served as suppliers to MNCs (Doh, 1993).
1986	<i>Singapore Economy: New Directions</i> published - role of SMEs and entrepreneurship highlighted for need of new policies.	EDB establishes the Small Business Unit to address the small business sector.
1989	First <i>SME Master Plan</i> published with	The SME Master Plan has five underlying strategic thrusts for SME growth: ● Technology adoption, application and innovation; ● Business planning and finance ● Human resource management ● Productivity improvement and training; and ● International marketing and business collaboration.
1996	Merger of the relevant parts of the Economic Development Board (EDB) with the National Productivity Board to form a statutory board, the Productivity and Standards Board (PSB) responsible for among other things, SMEs.	The SME First Stop was launched. Programs such as SME Enterprise Development Growth and Expansion Programme were launched.
2001	Publication of <i>SME 21</i> the second SME Master Plan.	Three strategic goals 1 - Grooming Innovative High-Growth SMEs 2 - Developing Productive SME Sectors 3 - Creating a Knowledge-Based, Pro-enterprise Environment
2002	PSB renamed as Standards Productivity Innovation and Growth (SPRING).	

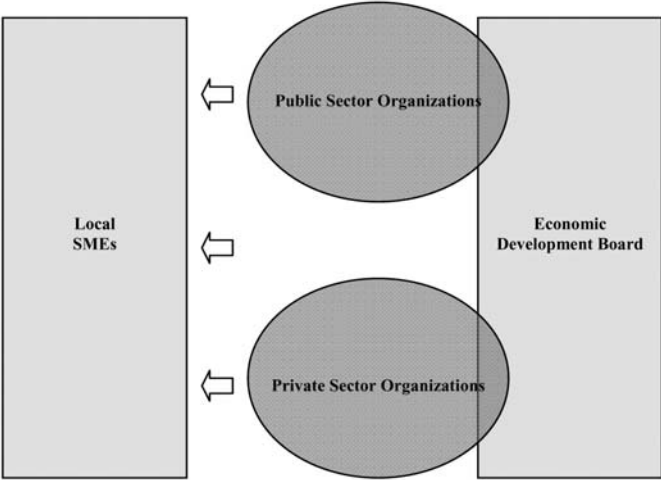
The key feature of the SME Master Plan was the formation of a multi-agency network. Each of the agencies in the public sector circle is responsible for one particular aspect of the SMEs' needs. Private sector organizations were also involved. Public sector organizations then included the National Computer Board, the predecessors of SPRING (Singapore Productivity and Standards Board), the International Enterprise (Singapore) and the Singapore Tourism Board. The private sector organizations included participating financial institutions, venture capital funds, consulting firms, chambers of commerce and private associations. The network helped administer the self help package under the SME initiative (see Figure 2).

Figure 2: SME Initiative under the SME Master Plan (1989)



This multi-agency network (see Figure 3) saw the growth and the introduction of enterprise centers in local tertiary institutions such as the Nanyang Technological University Entrepreneurship Development Centre (ENDEC; from 1989 to 1999), Entrepreneurship Centre at the National University of Singapore and NITEC at the Ngee Ann Polytechnic.

Figure 3: The Multi-Agency Network in the 1988 SME Master Plan



The next milestone in Singapore SME strategies was the transfer of responsibility for SMEs from the EDB, creating the Productivity and Standards Board (PSB). The PSB was formed from the amalgamation of the National Productivity Board with the Singapore Institute of Standards and Industrial Research and selected units responsible for SMEs and incentives. The PSB had a unit that was responsible for providing assistance to SME and an incentives unit that looked after financial programs for SMEs under which qualifying SMEs could obtain reimbursement for selected services or acquisitions of equipment. The PSB established the SME First Stop Centre in 1996 to provide broad-based assistance to SMEs. The productivity training arm of the PSB, took on additional responsibilities in training SMEs. One notable programme was developed by the author and adopted by the PSB in conjunction with ENDEC and a financial institution, Heller Asia called Enterprise Development Growth and Expansion (EDGE). This programme was collaboration between a university entrepreneurship centre (ENDEC), Heller Asia Capital who financed the development of the programme and the PSB. The programme was designed to address the challenges SMEs faced at various stages of growth.

The achievements under the entrepreneurship infrastructure created under the 1988 SME Master Plan were considerable. The key achievements that were highlighted in the SME Master Plan 1989 are reproduced in Appendix 1.

The next landmark development in SME strategy was unveiled in 2000 at the beginning of a new millennium and the advent of the knowledge based economy. A new SME committee had been formed to develop a ten year strategic plan to create vibrant and resilient SMEs that will enhance Singapore's competitiveness and economic growth.

The committee noted that the SMEs faced structural weaknesses which lead to their poor productivity performance (PSB, 2000). These include:

- Weak entrepreneurial culture
- Insufficient management know-how and professionalism
- Shortage of professional and technical manpower
- Insufficient use of technology
- Outmoded, unproductive methods of operation
- Limited ability to tap economies of scale
- Small domestic market

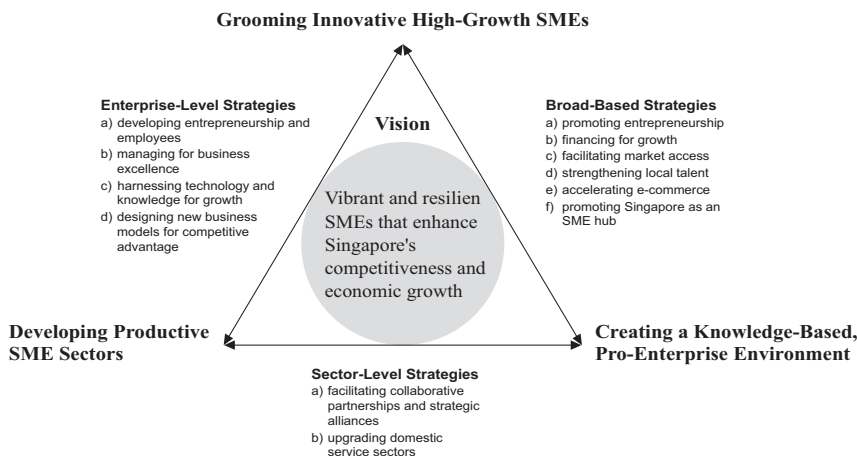
To assist Singapore SMEs to overcome these challenges and face the knowledge-based economy, the committee's report entitled SME21 outlined three strategic goals shown in Table 4. They also detailed a three project approach to achieve the three goals.

- Enterprise level - addressing the firm's capabilities.
- Sector level - addressing the needs of earmarked industries and fostering alliances and collaborations within sectors.

- Broad-based strategies - addressing the needs of the SMEs in general in the areas of financing, market access and technology, seeking to promote Singapore as a SME hub.

The goals and strategies are shown in Figure 4 taken from the SME 21 Master plan.

Figure 4: SME Strategies and Strategic Goals under SME 21



There have been extrusions to Singapore entrepreneurship infrastructure as a result of the SME21 Master Plan. Programs supporting the goals and strategies as outlined in SME21 are found in Appendix 2.

A concrete result of this integrated, multi-agency approach is the recent launch of EnterpriseOne, which stands for "One Network for Enterprises" in 2006. The portal at www.business.gov.sg is a Government-wide initiative managed by SPRING in partnership with business chambers and industry associations. It enhances SMEs' access to business information, Government e-services from more than 30 agencies, and advisory and consultative services³.

Key Observations

It is clear from the foregoing that the Singapore SME policies have been driven by its economic policies - these have varied over time in Singapore's brief national history of 41 years from 1965. In the early days of industrialization and up till the first recession in 1985, the SMEs did not receive special attention. The attention was on the attraction and facilitation of the foreign investors and multinationals that Singapore was attracting. SME policy then was indirect addressing the development of manufacturing capabilities to act as subcontractors to the multinationals (Doh, 1993). The watershed year was 1986 with the publication of the *Singapore Economy: New Directions Report* (1986).

With the realization of the contribution of SMEs to job creation and entrepreneurship in the review of Singapore's economic new directions after the 1985 recession, there have been SME policies since that have been forward looking. Singapore's entrepreneurship infrastructure covers the generic aspects of the business environment for the SMEs. It also has focused areas of interest by way of industry sector and capacity building in the enterprises. The policy makers are to be commended for their actions once there was a realization on the integral role that the SMEs played in Singapore's economy and economic plans. As the SMEs strategies are crafted with Singapore's economic plans in mind, the emphasis has been on developing SMEs that are able to create value or add value. Programmes are initiated to enable them to develop new technology. Other programmes seek to provide the technical expertise so that they can deliver products and services internationally. Yet others address their ability to meet the needs of their MNC partners.

With the enlightened view on the role of SMEs, there have been various strategic plans for SME development with the level of policy increasing over time. The entrepreneurship infrastructural offerings present today are vast compared to those prior to 1986. In this section, we draw some lessons from the Singapore experience.

Multi-agency approach: As SMEs permeate all levels of the economy (depth) and a variety of sectors (breadth), the multi-agency approach adopted in

Singapore is most apt. SMEs can access the centers in Singapore's tertiary institutions for assistance with tasks that they may have the relevant expertise. At the same time, where the SMEs require management consultancy services, they could access the consulting firms and apply for grants from SPRING. As members of a trade association, the SMEs could also approach their association for information.

A clear benefit of this approach is the decentralization of effort that enables localization of effort as the agencies have specialized functions, the depth of knowledge and information, and the guidance and assistance that is made available can be tailored to the specific needs of the SMEs.

Entrepreneurship Infrastructure Coordination: Adopting a multi-agency approach has implications on coordination. In this regard, the policy level coordination has taken place in Singapore through the various committees over the years. In designing the new economic directions, a high level committee involving ministers, government officials, academics and industrial representatives produced their report. This approach soon became pattern in the committees that produced the two SME master plans(1989, 2000). While policy level coordination would have ensured that the direction for policy offerings were suitably provided for by designated agencies, there is also a need for coordination in implementation of policies. Here there have been informal and formal meeting between the bureaucrats of the various agencies that have helped eliminate duplication and redundancy in effort, and provided SMEs with the transitions and collaboration when they require assistance from more than one agency. Such an instance of a SME requiring assisting from more than one agency at the same time is no inconceivable. SMEs participating in one of Singapore's many business study missions would be involved in a multi-agency endeavour. Similarly, when SMEs participate in a consortia to invest overseas in a government initiated venture, for instance the development of a port overseas.

Public-Private partnership: While the private sector has featured as a party in the multi-agency network for SMEs, in the recent three years beginning in 2006 that the role of the private sector has been increased. From 2006, the government has established the Local Enterprise and Association Development Programme (LEAD) so that the associations will be able to offer relevant services to their

members. The rationale behind this move is for the parties closest to the SMEs to recommend pertinent measures. A number of industry associations have established enterprise development centres under the LEAD programme. This measure is laudable but much remains in the hands of the industry associations. The involvement of the private sector is an excellent one subject to the industry associations having the right attitudes towards its members. It, however, has limitations if the industry associations seek to be entrepreneurial and seek profit despite having received grants from the government.

Private sector involvement in SME policy initiatives has positive outcomes apart from implementation benefits. Feedback on the relevant SME needs is best gleaned from the private sectors. The view from the policymakers' armchairs needs to be balanced and complemented by the inputs from the ground. An example of this is the recent move to have a different set of accounting standards for the SMEs. It had long been contended by the SMEs that the requirement for them to comply with the same accounting standards as the big boys was onerous and illogical. These calls fell on deaf ears but the endorsement and similar calls from the accounting professionals and university academics has seen an examination and development of standards more pertinent to smaller enterprises is currently underway.

Other SMEs not within identified sectors and those smaller. As Singapore has identified certain sectors for development and has goals for high technology and high growth SMEs, one may be wondering what about the other SMEs who are smaller or not in the selected sectors. Here one could imagine criticisms for the policy makers for apparently neglecting the others whom we could group under the category of the smaller guys - micro-enterprises, home-based entrepreneurs and the equivalent of the American garage-based startups. It must be conceded that the SMEs policies and infrastructural offerings, that are directed as selected industry sectors, appear to focus on growth enterprises or targeted industries that the policy makers are seeking to grow in Singapore. However, the reader must bear in mind the model presented earlier in Figure 1. Singapore's SME strategies have been shaped by the dualistic nature of Singapore's economy - the presence of MNCs and larger successful enterprises and the need for vibrant local enterprises. The strategies have been crafted to enable the SMEs to contribute to Singapore's economy and competitiveness.

While it would be tempting to assert that the other enterprises who are not geared for growth are neglected, that is far from the case. Entrepreneurs and enterprises that are intended to substitute for income from jobs lost receive assistance from another government agency, the Workforce Development Agency. Other startups and aspiring entrepreneurs embarking on second careers after retiring from the various arms of government such as the armed forces, receive assistance and advice from in-house departments and offices that are far too numerous to detail in this overview piece. The authors has thus chosen to focus on the express SME strategies in Singapore.

Implementation Issues. While we have dealt with SME policies in this paper, we have not discussed the other aspects of SME policies that matter to the users. This paper looked at the supply side, so to speak, of SME policies: the policy makers, their agenda, aims and the form that the policies have taken in Singapore.

The presence of the elements of an entrepreneurship infrastructure in an economy does not mean much if the intended users or participants - the SMEs - are engaged. The participation of SMEs in the infrastructure is needed, without which the policy intent remains an intention that has no fruits. Whether SMEs would participate in a programme is contingent on a number of factors. The SME has to realize it has a need. No enterprise seeks out unwanted activities as it has customers and business targets to meet. The challenge for policy makers is convincing the business owners that any scheme or programme is of value to them and that they need it. The former (convincing them) is not as critical as the second (getting them to act). It is possible to preach to the SMEs of the potential value of any government schemes. Yet we are familiar with our personal experience in other settings where we might personally agree with the value of government initiatives intellectually or on some other basis without acting on them. SMEs are no different, if they are informed of new initiatives, but cannot identify the relevance to them or their businesses, the policy efforts are wasted. Policy makers need to conceive not just policy pronouncements and implementation but also the means through the relevance of the measures is brought home to the potential users.

In this regard, the Singapore policymakers have to be commended for the advances they have made over the years. In the early days after the first SME

master plan, they were encountered feedback lack of publicity of the government schemes, red tape and bureaucracy. They have since addressed these through the mass media. The means have taken the form of advertisements, media coverage through the publications of the government agencies such as *Enterprise Today* (a bi-monthly and free magazine published by SPRING Singapore) and previously the *Productivity Digest*. They have also had seminars, conferences and road shows that have brought greater awareness to the SMEs and general public. The inaugural SPRING Enterprise Conference, for instance was held in April 2007. The policy makers used the conference and the surrounding media coverage to launch SPRING Singapore's new \$20 million Management Development Programme (MDP). The MDP aims to equip SME leaders - the CEOs and key managers - with appropriate knowledge and general management expertise to give them an edge in today's globalised economy. The programme expects to send some 1,000 SME leaders and managers back to business school over the next five years. Initially, SPRING will partner three local universities - Nanyang Technological University of Singapore (NTU), National University of Singapore (NUS) and Singapore Management University (SMU) - to provide customized postgraduate and executive development courses that focus on the business management needs of SMEs. The first course will start with the launch of the NUS and NTU postgraduate Executive MBA programmes in July 2007 with executive development programmes being launched in the later half of 2007.

The involvement of the other stakeholders, particularly the SMEs and industry associations, is relevant. Here policy-makers have taken a leaf from the nonprofit sector in motivating the volunteers, which encompasses most stakeholders. In the nonprofit sector volunteers need to be mustered, encouraged, trained and recognized. Lessons could be drawn from there. The SME peers and other stakeholders can help introduce the relevant schemes to the SME business owners. Hence, the policy-makers in Singapore have introduced over the past few years, the Action Community of Entrepreneurs (ACE) with its monthly events, activities and informational fairs. The government, together with the private sector formed the Action Community for Entrepreneurship (ACE) in 2003. This unique private-public sector effort aims to foster a business friendly environment and promote entrepreneurship in Singapore. Another example of the involvement of the stakeholders has

been mentioned earlier. Industry associations have applied under the LEAD programme to obtain grants to establish new initiatives for their industries. The Association for Small and Medium Enterprises and the Singapore Manufacturers' Federation, for example, have established Enterprise Development Centres where their members can obtain assistance and consulting services pertinent to their special needs.

Conclusion

Singapore's policy makers have been proactive in their stance and policies towards SMEs. They have adopted both an environmental approach creating elements of an entrepreneurship infrastructure that meets the needs of all and sundry, and also having strategies that focus on selected industry sectors. One could call this approach a balanced one, not neglecting the general body of SMEs while at the same time identifying the industry sectors that need assistance and the others that need to be developed. They must be commended for dovetailing their SME policies into the general economic development plans - noting the role of SMEs in innovations, new creations as well as meeting the needs of larger corporations as suppliers and service providers. The proactive stance taken has developed over time and with the increasing visualization of the role to be played by entrepreneurs, innovators and SMEs in the country.

Gazing into the crystal ball, the future of SME policies in Singapore is likely to see an element of crossvergence. Convergence has been used to refer to the coming together of ideas. The term crossvergence is used to refer to situations where the ideas migrate across domains; when two areas meet with both leaving the point changed. The idea of SMEs being confined to the for-profit arena will be a thing of the past, SMEs will need to be developed and encouraged in the nonprofit sector. In the non profit sector these enterprises are called social enterprises. They usually take the form of either enterprises with dual objectives (social and business agenda) or purely business enterprises that plough back the surplus to fund activities meeting social needs. The former name two goals, they attempt to meet two sets of agenda business and social. An example would be a food and beverage outlet where the

employees are also disadvantaged. The later is a business enterprise that could be operated by a charity with the aim of funding a social arm of the organization. What is interesting about these enterprises is they are in essence SMEs but in the social sector. The move has began but has not been conceived as the transference of ideas between the two areas with the vehicles, the SMEs being the same. At the same time, SMEs will meet the social agenda and like their larger cousins begin to measure up to social expectations and introduce socially responsible business practices and policies.

What next, one might ask. There is an air of expectation as a chief architect of Singapore's economic development, particularly, industry and cluster development, Phillip Yeo, has been appointed the new Chairman of the statutory board responsible for SMEs, Singapore Productivity Innovation and Growth (SPRING) on 1 April 2007. New initiatives have been announced in time with his appointment and yet more new initiatives are expected. His new appointment together with the fact that the SME21 plan is now 6 years old in times of rapid change, might portend new changes ahead. The rationalization SPRING's role as the *de facto* statutory board for SMEs may also be another reason for speculating on the development a new SME master plan. The inaugural SPRING Enterprise Conference also signaled change as the former mission and tagline for the statutory board, productivity, was absent. Instead, Mr. Lee Yi Shyan, the Minister of State for Trade and Industry and Minister-in-charge-of-entrepreneurship, who opened the conference on 5 April 2007, spoke of the mission of SPRING as the champion of SMEs.

In conclusion, it must be noted that this paper has sought to give a summary of the SME policy environment in Singapore. It is far from comprehensive as there is much detail about the various programmes that the reader needs to obtain from the various sources. It is hoped that this paper provides a flavour of the SME strategies developing in Singapore.

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Notes

1. It would not be possible to provide all the details to Singapore's SME strategies and entrepreneurship infrastructure, readers are directed to the main website where the information on the infrastructural offerings can be found at: www.enterpriseone.gov.sg.
2. These agencies have since been reconstituted as new statutory boards. For example, the TDB is now under International Enterprise (Singapore), STPB is now Singapore Tourism Board, and NCB has now been subsumed by the Infocomm Development Authority of Singapore.
3. Speech by Mr Lim Hng Kiang, Minister for Trade and Industry during the Committee of Supply Debate on Monday, 6 March 2006.

Appendix 1: Some Key Achievements under the SME Master Plan 1989

Thrust	Key Achievements
Technology Adoption, Application and Innovation	To raise the R&D capabilities of local enterprises, the National Science & Technology Board (NSTB) has developed the NSTB Plan 2000. More than \$4 billion will be committed over five years to strengthen the indigenous technology capability for private R&D. To defray the cost of innovation expenditure by local companies, the Innovation Development Scheme (IDS) was developed and implemented by the Economic Development Board (EDB) and five other government agencies. In 1997, about 230 innovations were approved. To encourage greater IT usage, the Infocomm Development Authority of Singapore (IDA) intensified efforts to promote computerization through the Local Enterprise Computerization Programme (LECP). In 1997 alone, 340 LECP applications were approved. IDA has committed \$4 million to train 1,300 IT professionals from over 500 companies through the Critical IT Resource Programme.
Business Planning and Finance	To encourage local enterprises to adopt a long-term strategic business focus, the Singapore Productivity Standards Board (now SPRING Singapore) enhanced the level of support under the Local Enterprise Technical Assistance Scheme (LETAS) for the Strategic Business Planning (SBP) programme. As at June 1999, 9,190 applications amounting to \$189 million had been committed since the inception of LETAS in 1986. To help SMEs gain better access to finance, the number of participating financial institutions under the Local Enterprise Finance Scheme (LEFS) has been increased to 28. LEFS was enhanced to enable more SMEs to gain easier access to financing. In the FY 1998 Budget, the government increased the loan-line of LEFS from \$760 million to \$1.1 billion. This was further increased to \$2 billion. As at June 1999, a total of 22,630 LEFS loan applications amounting to more than \$5.9 billion had been approved since its inception in 1976. To support acquisition of technology and investment in high-technology SMEs, government venture funds like the EDB Ventures (EDBV) Pte Ltd, EDB Ventures 2 (EDBV2) Pte Ltd and Singapore Bio-Innovations Pte Ltd (SBI) were created to provide equity funds to start-ups and high-growth SMEs. Since the start of the EDB Venture Capital Programme in 1985, a total of \$148

Appendix 1: Some Key Achievements under the SME Master Plan 1989

Thrust	Key Achievements
	million has been committed in 81 projects under EDBV and EDBV2. SBI was founded in 1990 and has since committed a total of \$43 million in 34 projects.
Productivity Improvement, Human Resource Management and Training	To make it easier for SMEs to access government assistance, SPRING Singapore set up the SME First-Stop Centre in 1996 to provide broad based assistance to SMEs. To date, more than 20,000 cases have been assisted. To help SMEs improve operations management, the Productivity Management and Project Team (PROMPT) Scheme was introduced in 1989. Assistance in productivity improvement was extended to SMEs in six industries. To encourage SMEs to embark on training, PSB's Institute for Productivity Training (IPT) has tailored courses for SMEs. For example, the Enterprise Development Growth and Expansion (EDGE) programme equips SME entrepreneurs with management skills to develop, grow and expand their business. IPT has trained about 10,100 SME participants over the last three years. As at June 1999, a total of 735,500 SME training places, amounting to \$186 million, had been approved by the Skills Development Fund (SDF). The approved SME training places grew by 8.7% p.a. from 1992 to 1998. The number of first-time SME applicants also grew by 3.4% to 3,200 in 1998.
International Marketing and Business Collaboration	To help SMEs gain access to international markets, PSB and the Trade Development Board (TDB) intensified their business-matching missions. More than 900 SMEs have participated in 31 business matching missions conducted by PSB since 1996. To promote business collaborations among SMEs in the domestic service sectors, PSB and TDB facilitated the formation of franchising and economic groupings. As at 1998, a total of 60 franchises and eight economic groupings have been formed in 39 trades, with 712 participating SME members. Through franchising, eight out of 10 businesses achieved better sales and seven out of 10 saw increased in profit. To help local companies set up operations overseas, the Regionalization Training Scheme (RTS), administered by EDB, has facilitated the training of 2,400 key foreign personnel. To provide equity funds for local companies venturing overseas, the Regional Investment Company (RIC), under EDB, was formed in 1996. In 1997 alone, it invested \$13.7 million in 5 projects to help local companies with good growth potential

Appendix 1: Some Key Achievements under the SME Master Plan 1989

Thrust	Key Achievements
	expand in the region. To date, it has invested \$36 million in 14 projects. To help SMEs gain access to funds to invest in machines and equipment in their overseas manufacturing plant, the Regionalization Finance Scheme (RFS) has provided \$104 million worth of loans to 87 SMEs since 1993.

Source: SME 21 (2000).

Appendix 2: Programs Supporting the Three-Pronged Approach in Singapore's SME Strategies for SME Development under SME 21

Enterprise-Level Strategies	Programs
Developing Entrepreneurs and Employees	SME Mentoring Programme to help SMEs map out strategic directions. SME Circles (EntreNet) to provide SMEs with learning partners. Entrepreneurship Education to equip entrepreneurs with management and leadership skills. SME Virtual University to provide IT and e-business courses to SMEs through the Internet.
Managing for Business Excellence	Business Excellence Framework to help SMEs manage their organizations professionally. National Best Practice Centre to help SMEs learn from and apply best practices. A pool of professional managers to help transform SMEs into professionally-run organizations. Assistance for SMEs to set up effective value and cost management systems.
Harnessing Technology and Knowledge for Growth	SME Business Support Centers to offer a wide array of integrated business support services and advice to SMEs. Technology Network (TechNet) Programme to facilitate connections between aspiring technopreneurs, innovative SMEs, researchers and experts and venture capitalists. Technology Incubator Programme to provide SMEs with access to management assistance, finance, and business and technical support services.

Appendix 2: Programs Supporting the Three-Pronged Approach in Singapore's SME Strategies for SME Development under SME 21

Enterprise-Level Strategies	Programs
Designing New Business Models for Competitive Advantage	Strategic Business Planning self-help package to enable SMEs to develop their own strategic business plan. Innovative Business Concept Award to spur SMEs to continuously develop new business concepts.
Sector-Level Strategies	Programs
Facilitating Collaborative Partnerships and Strategic Alliances	Franchising and economic groupings as strategic tools to help domestic businesses become regional and global players. Shared services to help SMEs better manage their costs and resources, and focus on core activities. Business fusion groups for SMEs to share knowledge, experience and ideas, and leverage on each other's capabilities.
Upgrading Domestic Service Sectors	Industry Upgrading Programme to raise the productivity of tradable and non-tradable sectors. Upgrading assistance programs to help domestic businesses overcome the disadvantage of size, build up capabilities to grow, leverage on the Internet to do business and be internationally competitive. A comprehensive range of measures to restructure, revitalize and upgrade the retail sector. A wide range of programs to upgrade the construction sector.
Broad-Based Strategies	Programs
Promoting Entrepreneurship	An "SME March" with month-long activities to convey the message that SMEs need to forge ahead and change their mindset. Media programs to raise the profile of SMEs in Singapore. Awards for local enterprises enhanced to ensure their relevance and attractiveness to SMEs; and more competitions to encourage SMEs to develop new business ideas and models. Local SMEs promoted as preferred business partners to foreign companies.
Financing for Growth	Business Angel Network to promote equity financing for innovative and high-growth firms. Business-to-Business Working Capital Matching Service to help SMEs in need of working capital to purchase raw materials or to fulfill a contract. SME schemes reviewed constantly to ensure their relevance and effectiveness in the knowledge-based economy.

Appendix 2: Programs Supporting the Three-Pronged Approach in Singapore's SME Strategies for SME Development under SME 21

Broad-Based Strategies	Programs
	Economic Value Added promoted as a tool for measuring the effectiveness of capital usage.
Facilitating Market Access	Business.Connect programme more widely promoted and enhanced. Singapore Connect publicised widely to more SMEs; and linkages with databases of other countries, as well as local and foreign industry associations and chambers, accelerated. Importance of branding promoted to SMEs; and a unique Singapore brand image developed for SMEs to leverage on as they explore new markets overseas.
Strengthening Local Talent	More SME Scholarships developed to groom local talent. Effective systems put in place to facilitate life long learning and skills development in organizations. Foreign talent tapped through various measures and programs.
Accelerating E-commerce (EC)	Promising e-commerce SMEs identified and developed as role models. Adoption of business-to-business portals by SMEs encouraged and accelerated. One-stop SME portal for foreign and local SMEs created to access the required information and services easily. E-commerce infrastructure in Singapore developed.
Promoting Singapore as an SME Hub	Economic twinning programs with other countries identified and pursued to establish areas for SME collaboration. Concerted marketing effort to encourage SMEs to use Singapore as the conduit and venue for international transactions. Chambers of commerce and industry associations as information and networking platform providers for foreign SMEs to meet up with their local counterparts. A package of fiscal measures to attract foreign SMEs to locate in Singapore. SME community created to attract foreign SMEs to start their operations here. Financing for collaborations between foreign and local SMEs to take place.

Source: SME 21 (2000).

Appendix 3: Some of Singapore's Government Initiatives to promote entrepreneurship & SMEs

Financing initiatives for businesses in Singapore

Schemes	Target Group	Validity Period	Eligibility Conditions	Funding
Micro Loan Programme (MLP)	Small local enterprises or micro enterprises.		10 or less than employees.	• A maximum loan of \$50,000 with fixed interest rate to help businesses augment their working capital needs like start-up costs or operational costs. • The programme is administered by participating financial intuitions and managed by SPRING.
Local Enterprise Financing Scheme (LEFS) — managed by SPRING	Local enterprises planning to upgrade, strengthen and expand their operations.			• Companies can apply to 17 participating financial institufor loans of up to \$15 million at fixed interest rate to help them modernize and automate their plant and equipment, expanding manufacturing capacity and finance projects.
Loan Insurance Scheme (LIS)	SMEs			• A portion of the loans will be insured against default risks. The insurance premiums will be co-shared between the government (through (IE) Singapore and SPRING) and the enterprises. • Participating financial institutions will also have the flexibility of using their own funds to package attractive loan facilities for the enterprises, based on their risk profile.

Appendix 3: Some of Singapore's Government Initiatives to promote entrepreneurship & SMEs

Financing initiatives for businesses in Singapore

Schemes	Target Group	Validity Period	Eligibility Conditions	Funding
SME Loan Securitisation Programme	Under-served SMEs, such as start-ups without established track records and SMEs that lack collateral.	Q105 onwards.		• This will leverage on the bond markets to reduce the credit risks for lending banks. • It is anticipated that the securitisation issue will be in the size of at least \$300m. • DBS is the appointed programme manager
Regionalisation Finance Scheme	Singapore-based enterprises setting up operations overseas.		Funding can be used for purchase of fixed assets, like buildings and machineries, as well as, construction of factories or buildings.	• Fixed interest rate financing scheme managed by IE Singapore.

Appendix 3: Some of Singapore's Government Initiatives to promote entrepreneurship & SMEs

Initiatives to facilitate SMEs and Start Ups in Singapore

Initiatives	Assistance / Services provided
SME One-Stop	• Consists of a self-help web-portal, supported by a call centre and a walk-in service centre. The proposed portal will create a single point of online access for SMEs in their search for information related to government. The objectives of the One-Stop Service are to improve the service delivery to SMEs so as to reduce their incidences of being passed from pillar to post when they approach government agencies. • To better develop this service, SPRING had conducted a study with a group of 300-400 SMEs to better cater to the needs and concerns of SMEs. • This service is expected to roll out in FY 05.
Online Business Licensing	• To reduce the burden and hassle that businesses face in obtaining business licences, the Online Business Licensing portal was launched in Jan 04. • Through OBLS, businesses can now apply online for 69 licences across 19 Government agencies. • The portal can be accessed via www.business.gov.sg.
Local Enterprise and Association Development Programme (LEAD)	• Industry associations can now get a grant to take the lead in envisioning and shaping their industry.
Local Enterprise Technical Assistance Scheme (LETAS)	• Get a grant to hire external experts to improve your management and operations.
SME Management Action for Results (SMART) Initiative	• Get a grant to develop business systems and processes for business excellence.
Technology Innovation Programme (TIP) - Experts	• Get a grant to hire technical experts from leading local and overseas R&D institutions.
Technology Innovation Programme (TIP) - Projects	• Get a grant for technology innovation projects that lead to new products or processes for your business.

Appendix 3: Some of Singapore's Government Initiatives to promote entrepreneurship & SMEs

Summary of tax incentives for businesses in Singapore

Schemes	Target Group	Validity Period	Eligibility Conditions	Incentives
Tax Exemption for New Companies	New companies	Any of the first 3 consecutive Years of Assessment (YA) falling within YA 2005 to YA 2009.	• Incorporated in Singapore. • A tax resident of Singapore for that YA. • No more than 20. shareholders throughout the basis period relating to that YA. • All. shareholders are individuals throughout the basis period relating to that YA.	Full tax exemption on the first \$100,000 of normal chargeable income.
Enterprise Investment Incentive Scheme (EII) - administered by SPRING	Investors in non-technology start-ups <i>(to mitigate risks of private equity investments)</i>			• A start-up can issue certificates to its investors for investments of up to \$3m. • Investors with these certificates will then be able to deduct any investment loss from their taxable income.
Enterprise Investment Incentive Scheme (Technopreneur) - administered by EDB	Investors in technology start-ups <i>(to mitigate risks of private equity investments)</i>			• A start-up can issue certificates to its investors for investments of up to \$3m. • Investors with these certificates will then be able to deduct any investment loss from their taxable income.

Appendix 3: Some of Singapore's Government Initiatives to promote entrepreneurship & SMEs

Summary of investment-related programs in Singapore

Schemes	Target Group	Validity Period	Eligibility Conditions	Funding
Start-up Enterprise Development Scheme (SEEDS)	Young and innovative companies with high potential and the ability to scale up their business.			Every dollar raised by a start-up from third party investors up to a maximum of \$300,000 is matched by EDB (technology) or SPRING (non-technology).
Growth Financing Programme	Singapore-based companies that have the potential to become global competitive enterprises.		The minimum investment from third party investors is \$500,000.	Every \$2 raised by growth company from third-party investors will be matched \$1 from EDB, subject to a maximum of \$1 million.
Entrepreneurial Talent Development Fund (ETDF)	Institutes of Higher Learning (IHLs)	ETDF is a \$25 million dollar grant deployed to the IHLs under the purview of the MOE, over five years, starting July 2004.	The IHLs can utilize the grant to invest in potential companies which are set up by students, alumni and staff, up to a maximum of \$50,000 per company.	Matching funding by the students and IHL concerned is provided by SPRING.

Source: Spring Singapore. The tax and financing incentives lists are not exhaustive of all schemes offered to promote and support entrepreneurship and SMEs.

The Changing Face of Chinese Taipei's SME Sector

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Introduction

Small and Medium Enterprises (SMEs) have been the driving force to Chinese Taipei's economic development; especially in the 1970s and early 1980s, SMEs enjoyed a strong position in Chinese Taipei's production outputs, numbers of enterprises, numbers of employees and export value. During that period, the growth of the SME sector was mainly driven by the dynamic growth of enterprises in the manufacturing industry. Under the contribution of manufacturing SMEs, Chinese Taipei's economic development demonstrated a special pattern of flexibility¹.

In the later 1980s, however, Chinese Taipei faced a series of challenges that had never happened before; including appreciation of NT dollars, soar of land and labor costs, decline of export competitiveness, and outflow of SMEs to other foreign production bases. From then on, the position of SMEs in Chinese Taipei's economy has experienced gradual changes. Large enterprises have been grasping their important share in Chinese Taipei's economy and the importance of the manufacturing industry has been gradually declining. The changing environment brought up the changes in the SMEs' share of export value, number of people in the SME sector, R&D tendency of SMEs, SMEs' adoption of e-commerce etc. and SMEs have been losing their primacy.

The topic of the change of Chinese Taipei's SMEs is really worth studying. As a driving force of economic growth they have used to be, SMEs' changing characteristics reflects the changing pattern of Chinese Taipei's economic development. In addition, the number of SMEs still accounts for around 98% of all Chinese Taipei's enterprises, and the number of people in the SME sector still occupies around 75% of Chinese Taipei's working force. Therefore, SMEs still have significant meaning in terms of economic and societal development in Chinese Taipei. Among existing studies and research, however, only very few pieces have addressed the changes such as the decrease of the SMEs' share of export value, but there lack comprehensive and systematic studies on the whole picture of the changes. In order to compensate this insufficiency, this study tries to systematically investigate the changes and examine the government policy to cope with the changes.

Changing Definitions of SMEs

Table 1 below shows how the definition of SMEs in Chinese Taipei has changed over the years. One significant change is the increase in the maximum capitalization, total assets and annual sales revenue that an enterprise may have and still be classed as an SME. In the past, a firm in the manufacturing, mining or quarrying sectors had to have capitalization of less than NT\$5 million to be considered an SME; today, the threshold has been changed to NT\$80 million. This relaxation in the qualifications for SME status was partly a deliberate effort on the part of the government to ensure that as many enterprises as possible could enjoy the benefits of SME status, but it also reflects the general trend for business enterprises in Chinese Taipei to get larger. With average capitalization, total assets and annual sales revenue all tending to rise, if the government had kept the size qualification for SME status at the same level, the number of enterprises eligible for SME status would have grown steadily smaller.

At the same time, with the increase of labor and land costs, the average operating costs per enterprise have risen too. It now costs more to set up a new business and keep it operating than it did in the past. Today, an enterprise with capitalization of NT\$80 million can expect to encounter the similar

problems (in terms of securing financing, limited manpower resources, market access, operational constraints etc.) that would have affected an enterprise with capitalization of NT\$5 million in the past. The changing of the capitalization threshold to NT\$80 million was thus very much a necessary measure on the government's part.

As regards the number of employees that an enterprise may have and still be classed as an SME, this has not displayed the same simple upward progression that the capitalization requirement has. For enterprises in the manufacturing industry and in the mining and quarrying industries, SMEs were defined in 1967 as those enterprises with less than 100 employees. This figure was increased to 300 in 1979, but then reduced to 200 in 1995. For enterprises in the agriculture, forestry and fisheries sector, in the public utilities industry and in the service sector, the maximum number of employees that an enterprise can have and still be classed as an SME has generally been kept at 50.

Table 1: Changes in the Definition of SMEs in Chinese Taipei

Manufacturing, Mining and Quarrying			
	Capitalization	Total Assets	No. of Employees
1967	Under NT\$5 million		Under 100 employees
1973	Under NT\$5 million	Under NT\$20 million	Electronics, garment and footwear manufacturing industries: Under 300 employees Food industry: Under 200 employees Other industries: Under 100 employees
1977	Manufacturing: Under NT\$20 million Mining and quarrying: Under NT\$20 million	Under NT\$60 million	Manufacturing: Under 300 employees Mining and quarrying: Under 500 employees
1979	Manufacturing: Under NT\$20 million Mining and quarrying: Under NT\$40 million	Manufacturing: Under NT\$60 million	Manufacturing: Under 300 employees
1982	Manufacturing: Under NT\$40 million Mining and quarrying: Under NT\$40 million	Manufacturing: Under NT\$120 million	

Table 1: Changes in the Definition of SMEs in Chinese Taipei

Manufacturing, Mining and Quarrying		
	Capitalization	Total Assets No. of Employees
1991	Manufacturing and construction: Under NT\$40 million Mining and quarrying: Under NT\$40 million	Manufacturing and construction: Under NT\$120 million
1995	Under NT\$60 million	Under 200 employees
2000	Under NT\$80 million	Under 200 employees
2005	Under NT\$80 million	Under 200 employees
Agriculture, Forestry and Fisheries, Public Utilities, and Service Sector		
	Annual Sales Revenue	No. of Employees
1967	Under NT\$5 million	Under 50 employees
1973	Under NT\$5 million	Under 100 employees
1977	Under NT\$20 million	Under 50 employees
1979	Under NT\$20 million	Under 50 employees
1982	Under NT\$40 million	
1991	Under NT\$40 million	
1995	Under NT\$80 million	Under 50 employees
2000	Under NT\$100 million	Under 50 employees
2005	Under NT\$100 million	Under 50 employees

Source: Small and Medium Enterprise Administration, Ministry of Economic Affairs, *White Paper on Small and Medium Enterprises in Taiwan*.

Key Trends in the Development of Chinese Taipei's SME Sector

Since late 1980s, the development of SMEs in Chinese Taipei has advanced to a different direction with respect to competitive advantage, industrial structure, and the position in the economy. This section will explore relevant indicators and statistics to demonstrate the changes of the SME sector of Chinese Taipei. The data of this study are mainly from White Paper on Small and Medium Enterprises in Taiwan, which contains the most completed information about SMEs. However, because the data in the White Paper still have its limitation on scope and time, this study will also refer to other sources to complement the insufficiency of the White Paper.

1. THE NUMBER OF SMEs IN CHINESE TAIPEI

The number of SMEs in Chinese Taipei has grown steadily over the years. Over the period 1982 - 2005, the total number of SMEs in Chinese Taipei rose by 74.7%, from 701,839 in 1982 to 1,226,095 in 2005, representing an average annual growth rate of 2.47%. During the period 1996 - 2005, the average annual growth rate was 2.15%, down from 3.3% in 1986 - 1995; however, the rate of increase has recently started to pick up again, climbing to 4.17% in 2005.

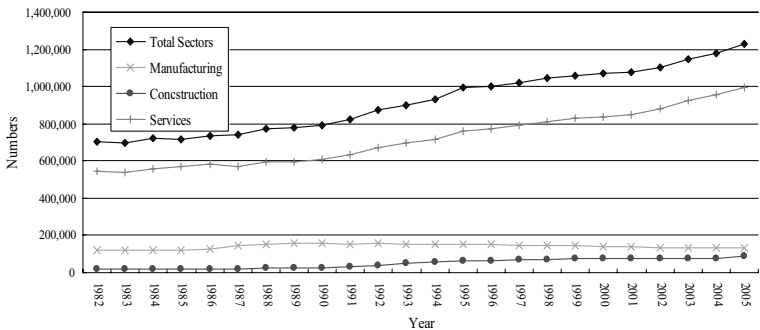
While the trend for the number of SMEs in Chinese Taipei to increase has remained unchanged, the structure of the SME sector has altered considerably over the years. We select some key sectors to demonstrate the change in terms of industries. Figure 1 shows the changes in the number of SMEs in key industries. As can be seen from this figure, the increase in SME numbers in recent years has been heavily concentrated in the service sector. The number of SMEs in the manufacturing sector has actually been falling since 1992, and the number of SMEs in the construction industry has increased only very slightly. The number of SMEs in the service sector began to grow rapidly in 1991; since that year, the SME growth rate for the service sector has been consistently higher than the growth rate for Chinese Taipei's industry as a whole. Broadly speaking, since 1991 - 1992, the service sector has accounted for more or less all of the annual increase in the number of SMEs in Chinese Taipei. In 2004, for example, the number of total SMEs in Chinese Taipei grew by 29,786, while the number of SMEs in the service sector increased by 30,620.

As regards SMEs' share of the total number of enterprises in Chinese Taipei, 1995 was a watershed year in this respect. SMEs' share of all enterprises had fallen steadily from 98.67% in 1982 to 96.26% in 1994. However, in 1995 SMEs' share of the total number of enterprises in Chinese Taipei began to rise again. The main reason for this increase was the government's revision of the definition of SMEs; the adoption of the new definition caused the number of SMEs to increase by 6.3% compared to the previous year. Since then, SMEs' share of all enterprises has remained at around the 98% level.

In the manufacturing sector, SMEs' share of all manufacturing enterprises has been falling steadily, while large enterprises' share has risen. In the service

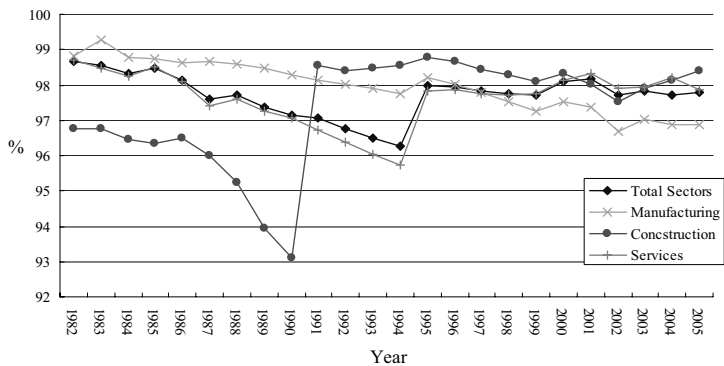
sector, the last few years have not seen any significant increase in SMEs' share of the total number of enterprises in the service sector in spite of its significant increase in the absolute terms, reflecting the fact that the number of large enterprises in the service sector has been growing at a similar rate to the number of SMEs.

Figure 1: The Number of SMEs in Chinese Taipei



Source: Small and Medium Enterprise Administration, Ministry of Economic Affairs, *White Paper on Small and Medium Enterprises in Taiwan*.

Figure 2: SMEs' Share of the Total Number of Enterprises

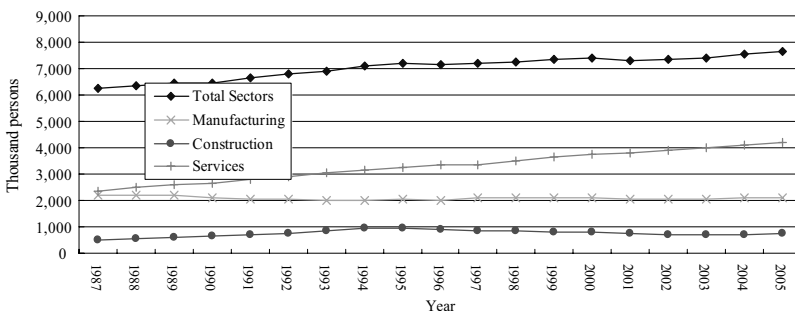


Source: Small and Medium Enterprise Administration, Ministry of Economic Affairs, *White Paper on Small and Medium Enterprises in Taiwan*.

2. THE NUMBER OF PERSONS EMPLOYED BY SMEs

The number of people working in the SME sector has grown slowly but steadily since 1987. In 1987, there were 6,271 thousand people working in SMEs in Chinese Taipei; by 2005, this figure had risen by 21.96% to 7,648 thousand. There was a slight, temporary decline in the number of people working in the SME sector in 1995 - 1996. As regards the situation in individual sectors of the economy, the service sector has seen the largest increase in the number of people working in SMEs. In 1987, there were 1,487 thousand people working in service sector's SMEs in Chinese Taipei; by 2005, this figure had increased by 79.78% to 2,329 thousand. Here again, one can see the shift in the center of gravity of the SME sector towards the service industries. The number of people working in SMEs in the manufacturing sector has for many years remained steady at around 2 million to 2.1 million people, while the number of people working in SMEs in the construction industry rose initially before falling. In 2005, the number of people who worked in the SME sector as a whole increased by 95 thousand; the service sector accounted for 89.47% of this increase, with 85 thousand additional people working in service sector's SMEs. As of 2005, 54.63% of all people working in SMEs were working in the service sector.

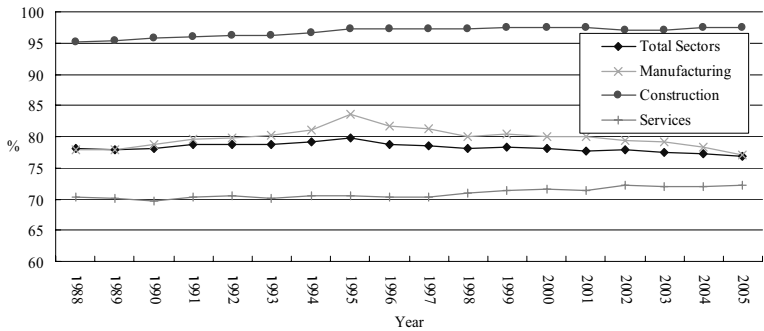
Figure 3: The Number of People Working in SMEs



Source: Small and Medium Enterprise Administration, Ministry of Economic Affairs, *White Paper on Small and Medium Enterprises in Taiwan*.

While the number of people working in SMEs has increased in absolute terms, the SME sector's share of total employment in Chinese Taipei has been falling. SMEs' share of the total number of working force in Chinese Taipei peaked at 79.75% in 1995 following the introduction of the revised definition of SMEs. Since then, it has fallen steadily, declining to 76.93% by 2005. Although the number of people working in SMEs has been rising, the number of people working in large enterprises has been growing even faster, reflecting the growing importance of large enterprises within the economy as a whole. The decline in SMEs' share of working force has been especially pronounced in the manufacturing sector. It decreased from 83.5% in 1995 to 77% in 2005. By contrast, SMEs' share in the service sector has risen, with an increase from 70.52% to 72.28% over the same period. The trend for enterprises to get larger has thus been more evident in the manufacturing sector than it has in the service sector.

Figure 4: SMEs' Share of Total Working Force



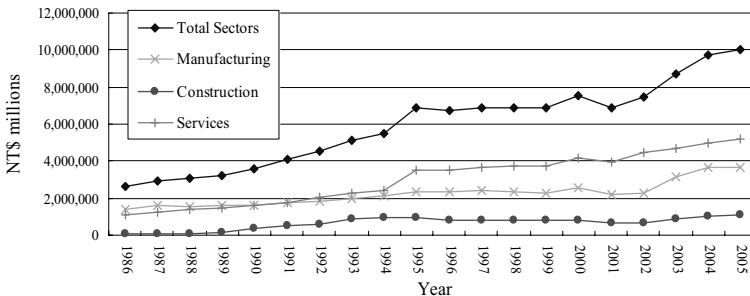
Source: Small and Medium Enterprise Administration, Ministry of Economic Affairs, *White Paper on Small and Medium Enterprises in Taiwan*.

3. SME SALES PERFORMANCE

The growing dominance of the economy by large enterprises is very obvious when one examines sales performance. Figure 5 shows the changes in SME sales performance since 1986. It can be seen that, over the period from 1986 to 2005, total annual sales for the SME sector as a whole grew by 282%.

However, growth was not continuous during the whole of this period; in particular, the sales performance of the SME sector as a whole remained more or less flat over the period from 1995 to 2001. In terms of industries, the service sector had the highest sales growth rate over the period 1986 - 2005. Combined sales for all service sector SMEs rose by 356% during this period, compared to 164% for the manufacturing sector and 136% for the construction industry. One point worth noting is that even though the whole period witnessed a faster growth in the total annual sales in service sector, the growth rate of the manufacturing sector in the last three years has been higher than the corresponding growth rate for the service sector. The average sales per manufacturing sector SME have risen by 18.19% in the last three years, compared to an increase of just 4.87% in the service sector.

Figure 5: SME Sales Performance

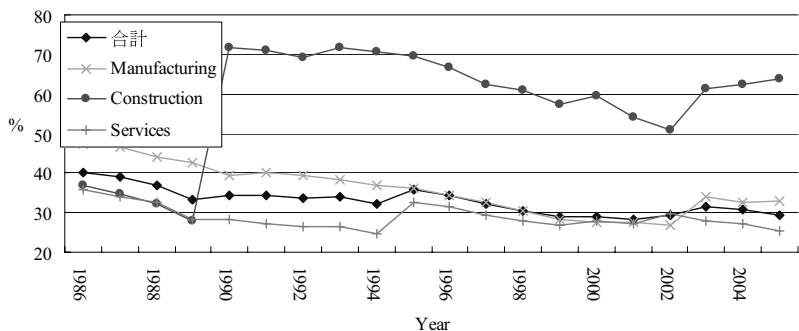


Source: Small and Medium Enterprise Administration, Ministry of Economic Affairs, *White Paper on Small and Medium Enterprises in Taiwan*.

SMEs' share of total annual sales for all enterprises has been falling steadily, from 40.28% in 1986 to 29.46% in 2005, while large enterprises' share has risen, reflecting the growing importance of large enterprises within the Chinese Taipei's economy. In the manufacturing sector, SMEs' share of total annual sales fell by 30.69% from 47.37% of total sales in 1986 to 32.83% in 2005; if the comparison is made between 1986 and 2002, then the decline is even more pronounced, at 43.14%. In the service sector, SMEs' share fell by 27.21% over the period 1986 - 2005. The fact that the decline in SMEs' share was less pronounced in the service sector reflects that fact that the trend towards larger enterprises has been less evident in this sector than it has in the

manufacturing sector. The construction industry is the only sector in which SMEs' share of total annual sales revenue has not fallen. In the construction industry, SMEs' share of total annual sales has risen by 72.1%; however, because the construction industry's annual sales are relatively low compared to the manufacturing sector and the service sector, this increase has had little impact on the economy as a whole.

Figure 6: SMEs' Share of Total Annual Sales Revenue



Source: Small and Medium Enterprise Administration, Ministry of Economic Affairs, *White Paper on Small and Medium Enterprises in Taiwan*.

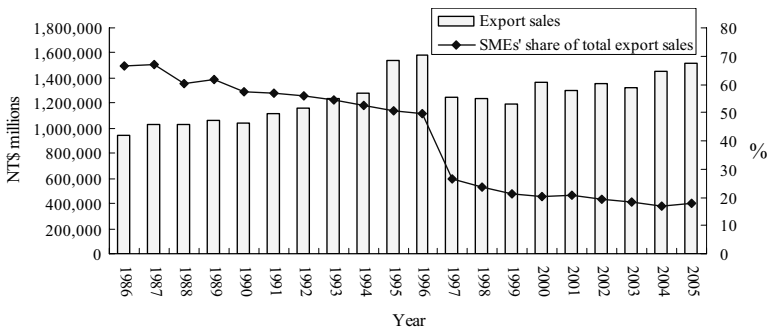
4. SMEs' EXPORT SALES AND EXPORT PATTERNS

In the 1980s and the early 1990s, SMEs accounted for the largest share of Chinese Taipei's exports; Chinese Taipei's large enterprises were mainly oriented towards the domestic market. This difference in market orientation between SMEs and large enterprises has been viewed as one of the most significant characteristics of Chinese Taipei's economic development. Chou Tien-cheng describes the Chinese Taipei's economy as having a "dichotomous structure".² Recently, however, this situation has been changing. Large enterprises are expanding into overseas markets, and SMEs' dominance of the export business is much less marked than it was.

Figure 7 shows the annual export sales of Chinese Taipei's SMEs and their share of total export sales for all enterprises. In 1986, SMEs accounted for

66.37% of Chinese Taipei's exports. Since then, although SME exports have continued to increase in absolute terms, SMEs' share of total exports for all enterprises has fallen steadily. By 2005, SMEs' share had dropped to 17.6%. It should be noted that the adoption of new calculation methods in 1997 caused both SME export value and SMEs' share of total export for all enterprises to fall dramatically. Nevertheless, even without this additional factor, the general trend would still have been downwards. A similar decline can be seen in SMEs' share of the total number of enterprises, their share of employment, and their share of total annual sales revenue. In every case, these figures reflect the trend towards dominance of the economy by large enterprises.

Figure 7: SMEs' Annual Export Sales and Their Share of Total Exports for All Enterprises



Source: Small and Medium Enterprise Administration, Ministry of Economic Affairs, *White Paper on Small and Medium Enterprises in Taiwan*.

While the decline in SMEs' share of Chinese Taipei's annual exports is partly attributable to the growing importance of large enterprises within the economy, examination of changes in production and sales models in Chinese Taipei's industry suggests another important reason. In the past, Chinese Taipei's exports were mostly relatively simple products; processing accounted for a large share of export-oriented production. With products of this kind, SMEs were often able to handle exportation themselves; alternatively, they could work through trading companies. Today, industrial production in

Chinese Taipei generally involves a complex division of labor. A single product often includes components and materials supplied by a number of different SMEs, which are then assembled and exported by a large enterprise. The SMEs and the large enterprise form what is sometimes known as a "central-satellite system".

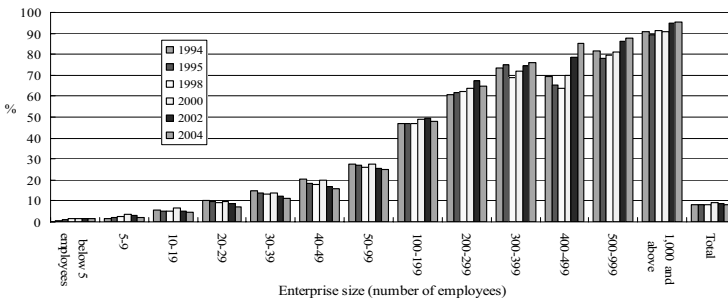
Many of the SMEs that in the past exported their own products no longer exist; others have been drawn into center-satellite systems, where their products merely constitute part of the product of a larger enterprise, so that exportation takes place indirectly via the large enterprise. Under these circumstances, Chinese Taipei's export statistics - which are concerned only with direct exports - cannot show the full contribution made by SMEs to Chinese Taipei's export performance.

Data on indirect exports is very difficult to obtain, but some existing data and research that have been undertaken in this field still makes it possible to develop a rough picture of the shift from direct exports to indirect exports in the SME sector. The 2003 edition of the *White Paper on Small and Medium Enterprises in Taiwan* contained some rough preliminary estimates for two categories of indirect exportation: exportation via large enterprises, and exportation via trading companies.³ Using data for 1999 and 2001 - the only two years for which data was available - the White Paper found that SME exports via trading companies had fallen from NT\$702.7 billion in 1999 to NT\$671.9 billion in 2001. By contrast, SME exports via other large manufacturers had increased from NT\$968.9 billion in 1999 to NT\$1,664.1 billion in 2001. Exports via other manufacturers had thus come to dwarf exports via trading companies, and were still growing. By way of comparison, Chinese Taipei's SMEs' direct exports totaled NT\$1,197.8 billion in 1999 and NT\$1,300.3 billion in 2001. Exports via other manufacturers in 2001 thus exceeded SMEs' direct exports in that year. While direct exports increased by NT\$102.5 billion between 1999 and 2001, indirect exports via other manufacturers increased by NT\$695.2 billion over the same period. Although it is difficult to say for certain on the basis of data for just two years, it does appear that Chinese Taipei's SME sector may be shifting away from direct export towards indirect export via other manufacturers.

5. R&D ACTIVITY IN THE SME SECTOR

In the last few years, not only has the percentage of Chinese Taipei's SMEs that undertake R&D activity fallen, the amount spent on R&D has also been in decline. As can be seen from Figure 8, for SMEs of almost every size within the 10 - 99 employees range, the percentage that engage in R&D activity has been falling in recent years. In 1994, 5.67% of SMEs with 10 - 19 employees undertook R&D activity; by 2004 this figure had fallen to 5.17%. Over the same period, the percentage of SMEs undertaking R&D fell from 10.37% to 8.8% for SMEs with 20 - 29 employees, from 14.72% to 12.31% for SMEs with 30 - 39 employees, from 20.17% to 17.05% for SMEs with 40 - 49 employees, and from 27.37% to 25.59% for SMEs with 50 - 99 employees. In the case of SMEs with less than 10 employees, while the percentage of SMEs in this group that engaged in R&D had been rising prior to 2000, since 2000 it has been falling. By contrast, the percentage of medium-sized enterprises with 100 - 199 employees that undertake R&D has risen slightly, from 46.88% in 1994 to 47.78% in 2004, and there has been a significant increase in the percentage of large enterprises (those with 200 or more employees) undertaking R&D activity.

**Figure 8: The Percentage of Enterprises Engaging in R&D Activity-
by enterprise size (number of employees)**

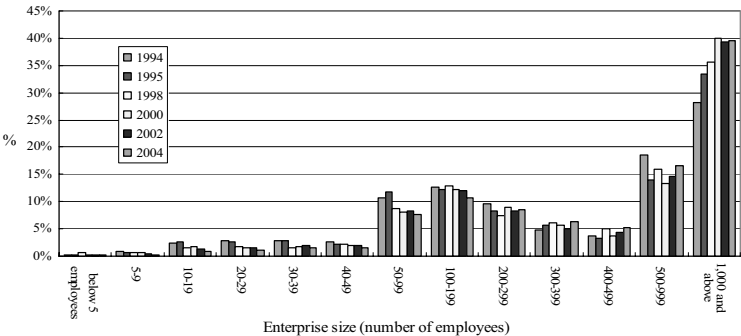


Source: Ministry of Economic Affairs, *Report on Annual Survey of Industries*.

A similar picture emerges when one examines the percentage of total R&D spending by enterprises. In 2004, large enterprises with 200 or more employees accounted for 76.27% of all R&D spending by Chinese Taipei's

industry as a whole; SMEs with less than 200 employees accounted for 23.73%. As can be seen from Figure 9, the share of total R&D expenditure held by SMEs has been in decline, falling from 35.15% in 1994 to 23.73% in 2004. The decline has been most evident in the case of small enterprises with 5 -9 employees (-72.88%), and least evident in the case of enterprises with 100 - 199 employees (-15.73%). Broadly speaking, the smaller the size of the enterprise, the greater the decline in R&D spending has been.

Figure 9: The Percentage of Total R&D Spending Held by Individual Enterprise Size Classes



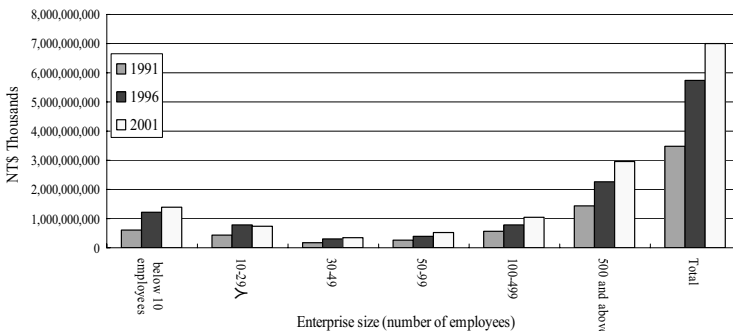
Source: Ministry of Economic Affairs, *Report on Annual Survey of Industries*.

6. SME VALUE ADDED LABOR PRODUCTIVITY

As shown by Figure 10, the amount of value added created by SMEs increased over the period 1991 - 2001. Enterprises with fewer than 10 employees posted the fastest increase in value added, at 130%, while those with 10 - 29 employees had the smallest increase, at just 67.76%. The increase in value added for large enterprises with 500 or more employees over this period was 105.25%, a figure that was surpassed only by enterprises with fewer than 10 employees. Large enterprises with 500 or more employees accounted for 42.09% of total value added created by all enterprises in 2001, while enterprises with less than 100 employees accounted for 42.7%. Given that SMEs accounted for only 28.38% of total sales for all enterprises in Chinese Taipei in 2001, their contribution to value added creation is very impressive.

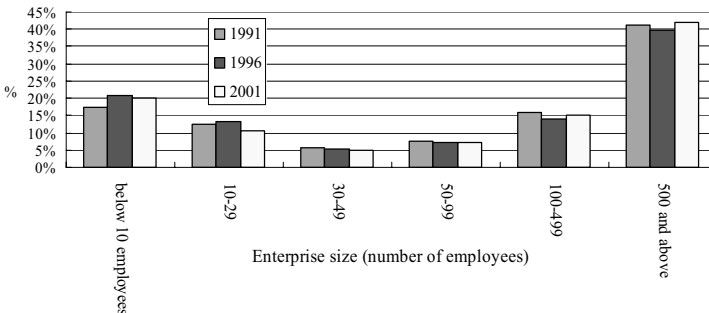
It can be seen from Figure 11 that, within the small enterprise segment, the share of total value added held by enterprises with less than 10 employees increased over the period 1991-2001, whereas for all other small enterprise size classes, the share of value added held fell during this period. Enterprises with less than 10 employees and large enterprises with 500 or more employees were thus the only two size classes to see their share of value added increase between 1999 and 2001.

Figure 10: Value Added Creation by Enterprises of Different Size



Source: Directorate General of Budget, Accounting and Statistics, *Industry Commerce and Service Census*.

Figure 11: The Shares of Total Value Added Held by Enterprises of Different Sizes



Source: Directorate General of Budget, Accounting and Statistics, *Industry Commerce and Service Census*.

Owing to the limitations of the available data, the ratios between value added and the number of employees have been used to estimate labor productivity for enterprises in each size class. According to the results of these estimates, in 2001, each employee in those enterprises with less than 10 employees was creating an average of NT\$681,810 of value added per year; for employees in large enterprises with 500 or more employees, the figure was NT\$1,641,140. Labor productivity in large enterprises with 500 or more employees was thus 2.5 times as high as that in small enterprises with less than 10 employees.

In terms of the growth rate of labor productivity, enterprises in the 50 - 99 employee class have seen the most rapid increase in labor productivity, followed by those in the 100 - 499 employee class and enterprises with less than 10 employees. However, labor productivity growth for enterprises with 500 or more employees has been disappointing. It can thus be seen that, although SMEs' labor productivity is still lower than that of large enterprises, labor productivity in SMEs is improving more rapidly than it is in large enterprises.

Table 2: Labor productivity of enterprises by Size

Units: NT\$ thousands; %

	1991	1996		2001		Average	
	Value added /no. of employees	GDP/no. of employees	Growth rate (1991-1996)	Value added /no. of employees	Growth rate (1996-2001)	Value added /no. of employees (average for all three years)	Growth rate (1991-2001)
Less than 10 employees	377.09	582.91	54.58%	681.81	16.97%	547.27	80.81%
10-29 employees	400.58	601.74	50.22%	676.98	12.50%	559.77	69.00%
30-49 employees	415.87	611.95	47.15%	686.17	12.13%	571.33	65.00%
50-99 employees	460.97	693.29	50.40%	869.98	25.49%	674.74	88.73%
100-499 employees	599.11	929.27	55.11%	1096.57	18.00%	874.99	83.03%

Table 2: Labor productivity of enterprises by Size

Units: NT\$ thousands; %

	1991	1996		2001		Average	
	Value added /no. of employees	GDP/no. of employees	Growth rate (1991– 1996)	Value added /no. of employees	Growth rate (1996– 2001)	Value added /no. of employees (average for all three years)	Growth rate (1991– 2001)
500 or more employees	1196.89	1720.50	43.75%	2006.03	16.60%	1641.14	67.60%
All enterprises	595.13	871.42	46.43%	1050.07	20.50%	838.87	76.44%

Source: Directorate General of Budget, Accounting and Statistics, *Industry Commerce and Service Census*.

7. E-COMMERCE ADOPTION IN THE SME SECTOR

The last few years have seen a significant increase in both computerization and e-commerce adoption in Chinese Taipei's SME sector. However, as can be seen from Table 2, SMEs in the manufacturing sector continue to lag behind large enterprises in terms of both computerization and e-commerce adoption. As of 2005, 96.09% of large enterprises in the manufacturing sector were using computers, whereas 71.20% of SMEs were doing so. As for e-commerce, 53.69% of large enterprises were using e-commerce in 2005, compared to 47.66% of SMEs; the gap between large enterprises and SMEs in this respect was thus only 7 percentage points. Although both computerization and e-commerce adoption are less advanced in the SME sector than they are among large enterprises, SMEs are catching up fast. This is particularly true for small enterprises with less than 100 employees. Whereas in 2001 only 35.59% of small enterprises with less than 100 employees were using e-commerce, by 2005 this figure had jumped to 47.66%; over the same period, the percentage of large enterprises that were using e-commerce increased only from 45.61% to 53.69%. The situation with regard to computerization is similar.

Overall, while Chinese Taipei's SMEs currently still have lower levels of computerization and e-commerce adoption than large enterprises, their growth

rates in this respect are higher. Despite SMEs' smaller resources and manpower, the fact the SME sector has managed to achieve almost the same level of e-commerce adoption as large enterprises suggests that there is strong demand for e-commerce among SMEs.

Table 3: Computerization and E-Commerce Adoption among Chinese Taipei's Enterprises

Unit: %

	Computerization			E-Commerce Adoption		
	2001	2003	2005	2001	2003	2005
200 or more employees	93.06	93.98	96.09	45.61	54.67	53.69
100-199 employees	91.67	89.51	87.99	37.88	45.52	50.42
Less than 100 employees	63.64	67.98	71.20	35.59	45.24	47.66

Source: Ministry of Economic Affairs, *Survey Report on the Operation of the Manufacturing Industry*.

8. THE ESTABLISHMENT OF NEW ENTERPRISE

Over the last few years, the number of new SMEs established in Chinese Taipei each year fell in the first place and then increased again. During the period 1998 - 2002, the number of new SMEs established each year declined steadily, but in 2003 it began to pick up again. The establishment of new enterprises is an important indicator of the health of an economy's entrepreneurship; the decline in SME start-ups prior to 2003 was thus a serious warning sign for Chinese Taipei. It remains to be seen whether the improvement since 2003 was only a temporary phenomenon. Judging by industries, we found that service firms still accounted for largest portion of newly established enterprises and the number of them also experienced fast growth. From 1998 to 2005, the number of startups in the service increased from 86,396 to 107,868, while the startups in the manufacturing sector decreased from 6,521 to 5,723.

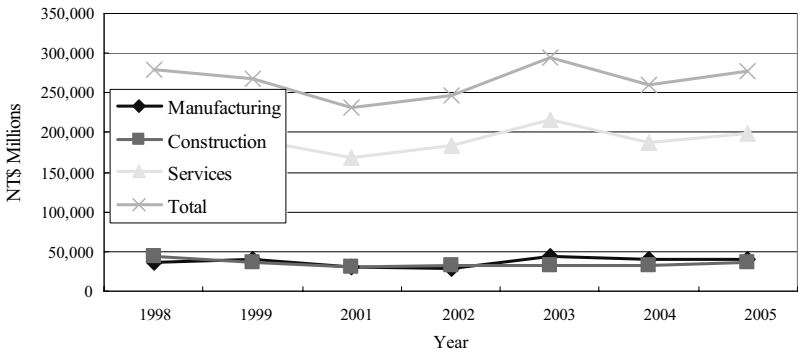
Figure 12: The Number of New SMEs Established in Chinese Taipei Each Year



Small and Medium Enterprise Administration, Ministry of Economic Affairs, White Paper on Small and Medium Enterprises in Taiwan.

With regard to annual sales, startups' performance lags behind their achievement in the increase of the number of firms. Between 1998 and 2005, the number of startups increased by 20.67%, but the annual sales decreased by 0.51%, demonstrating a tendency on the shrinking of scale of startups during recent years. The ratios between annual sales and the number of startups can prove this observation. In 1998, the average annual sale of each startup is NT\$ 2.69 million, but it decreased to NT\$ 2.22 million by 2005. Compared to overall SME sector, the performance of startups is obviously surpassed by average SMEs on annual sales. An average each SME' annual sale is NT\$ 8.16 million in 2005, while an average startup's annual sale is only NT\$ 2.22 million. The shrinking size of startups during recent years is attributable to a large number of startups rushing in the service sector. Average annual sale of each startup in the service sector was NTD 2.27 million in 1998, but it quickly decreased to NTD 1.85 million in 2005, while during the same period, average annual sale of each startup in the manufacturing sector increased from NT\$ 5.61 to NT\$ 6.93 million.

Figure 13: Total Annual Sales of All Newly-established SMEs



Small and Medium Enterprise Administration, Ministry of Economic Affairs, White Paper on Small and Medium Enterprises in Taiwan.

On the basis of the statistical data presented above, the following trends can be identified as having affected the development of Chinese Taipei's SME sector in the last few years.

1.SMEs' Share of Economic Activity in Chinese Taipei Has Been Falling Steadily

It can be seen from the data presented above that SMEs' share of several key aspects of economic activity - including employment, annual sales, exports, R&D spending and value added creation - has been falling, while large enterprises' share has risen. In the case of annual sales, SMEs' share of the total fell from 40.28% in 1986 to 29.46% in 2005. The decline in SMEs' shares of export sales and R&D spending was almost as pronounced, while the decline in SMEs' shares of employment and value added creation was more modest. The increase in the importance of large enterprises has been particularly marked in the manufacturing sector.

2.The Service Industries Now Constitute the Core Element in Chinese Taipei's SME Sector, and the Number of Service Sector SMEs has Grown Rapidly

Whether viewed in terms of the number of enterprises, the number of working force, or annual sales, the center of gravity of the Chinese Taipei's SME sector has been shifting towards the service industries. In the last few years, it is the service sector that has seen the most rapid increase in the number of SMEs. Most newly established SMEs have been in service industries; the number of SMEs in the manufacturing sector has in fact been falling since 1992. The service sector has also been the source of most SME job creation. This change is related to the tendency of the development of Chinese Taipei's industrial structure towards the service sector. By contrast, there is higher threshold for the survival of manufacturing SMEs; the higher limitation is not only placed on the capital requirements but on technology level.⁴

3.There Has Been a Significant Improvement in SME Labor Productivity

Regardless much of the data for Chinese Taipei's SME sector make depressing reading, SMEs in Chinese Taipei have achieved an impressive increase in labor productivity. Although labor productivity in SMEs is still inferior to that in large enterprises, SMEs' productivity has been growing faster than that of large enterprises. SMEs' share of the market may have contracted, but they have become more efficient.

4.SME Spending on R&D Has Fallen, and the Percentage of SMEs that Undertake R&D Has Declined

Although SMEs' labor productivity has improved significantly, this is not the result of increased spending on R&D. Both the amounts that SMEs spend on R&D and the percentage of SMEs that undertake R&D activity have fallen; the smaller the size of the enterprise, the more evident the decline. This trend reflects not only the SMEs' ignorance of the importance of R&D, but also the fact that a growing percentage of Chinese Taipei's SMEs are in the service sector; most service sector enterprises (small retailers for example) have neither the capability nor the motivation to undertake R&D.

5.Integration into Value Chains Has Gradually Become the Main Business Model for SMEs in the Manufacturing Sector

With indirect exports via other manufacturers gradually replacing direct exports by the SME itself, for SMEs in the manufacturing sector at least, integration into value chains (or center-satellite system) has become the main production/sales business model. As a result, SMEs today need to acquire new skills and capabilities; while they may no longer need to be able to develop customers for themselves, they do need to be able to collaborate efficiently with the other companies in the value chain.

6.The Percentage of SMEs Making Use of E-Commerce Has Risen

The percentage of SMEs that have computerized their operations and the percentage that have adopted e-commerce have both risen dramatically. The e-commerce adoption rate is now almost as high among SMEs as it is among large enterprises. Under cost pressure, SMEs still devote resource to e-commerce, indicating that they clearly have strong demand for e-commerce. The spread of e-commerce in the SME sector is also related to the integration of SMEs into larger supply chains, and to the growth of online shopping.

7.After Falling for Several Years, the Number of New SMEs Established Each Year Has Started to Rise Again

New business establishment is one of the most important indicators of the strength of a economy's entrepreneurship. It can be seen from the data presented above that, after falling during the period 1998 - 2002, the number of new SMEs established in Chinese Taipei each year started to rise again in 2003 - 2005, reflecting a strengthening of entrepreneurial activity. However, the increase can be attributable to the large scale increase of small service startups.

Policy to Cope with the Changes

1. CHANGES IN THE GOVERNMENT'S SME POLICY

Up until the 1990s, the Chinese Taipei government's policy with respect to the development of the SME sector was dominated by the concept of "guidance"; there was little in the way of policy measures to achieve structural improvement in the overall business environment. "Guidance" generally involved recruiting experts to provide consulting services, visiting SMEs to provide on-site support, organizing training courses for SME employees, etc. For the most part, guidance content was limited to traditional business skills, such as finance, business administration, etc. Guidance measures like these could help only a limited number of SMEs (mainly those who actively requested assistance); they had limited impact on the vast majority of SMEs in Chinese Taipei. Very few attempts were made to achieve an across-the-board improvement of the business environment; the most significant of these was the establishment of the SME Credit Guarantee Fund, which made it easier for SMEs to secure financing.

From 2000 onwards, the government's SME policy began to change. Although SME policy continued to emphasize "guidance", there was an increased emphasis on improving the business environment for SMEs. Measures were introduced to simplify the administrative procedures and reduce the transition cost for establishing a new enterprise. The government has also worked to provide a better environment for e-commerce, and has leveraged information and communications technology (ICT) to make it easier for SMEs to access the information they need. The last few years have seen the launch of several integrated ICT platforms, whereby different plans in the same area are integrated using the Internet, making it possible to provide better and more comprehensive services for SMEs.

The biggest single change in the Chinese Taipei's government SME policy since 2000 is that almost all new policy measures have taken the emergence of the knowledge economy into account. Many of the tools that business enterprises require in the era of the knowledge economy are things that individual SMEs cannot develop on their own. Active government assistance is needed to support the development of e-commerce, industrial clusters, and

stronger intellectual property right protection. The following sections will examine the policies adopted by the Chinese Taipei in response to a changing business environment, and those adopted in response to the changing nature of the SME sector itself.

2. POLICY MEASURES ADOPTED IN RESPONSE TO A CHANGING BUSINESS ENVIRONMENT

(1) Business Start-up and Incubation Policy

Business start-up and the entrepreneurship are two of the most important factors in the worldwide striving for innovation and sustainable development. The decline in the number of new SMEs established each year that Chinese Taipei experienced in 1998 - 2002 constituted a clear warning that Chinese Taipei needed to do more to cultivate business start-ups, and pointed up the need to create a business environment conducive to the establishment and development of new firms. Recognizing the importance of this issue (while also responding to the global trend towards encouraging entrepreneurial activity), the Chinese Taipei's government began to provide active support for new business start-up. Government policy in this area covered two key aspects: stimulating new business establishment, and start-up incubation.

The government has introduced a series of new policy measures to promote the establishment of new business enterprises, including the provision of information and consulting services, the establishment of "entrepreneur academies" and business start-up guidance centers (the Entrepreneurship Lab), and awards for innovative new business ventures. The first Entrepreneurship Lab was set up in 2005. They provide one-to-one on-site guidance, diagnostic services, technology matching, in-depth guidance programs, etc. In addition, the Realization of Entrepreneurial Dreams website serves as a portal site integrating the various plans and policy measures outlined above, and provides a wide range of information for entrepreneurs.

Chinese Taipei's Company Law was revised in 2001, greatly simplifying the process of new business establishment and eliminating unnecessary legal and regulatory restrictions. For example, a registration system replaced the old business licensing system; in the vast majority of industries, all that is

necessary to establish a new enterprise is to register it with the relevant government authorities. The minimum number of shareholders that a company is required to possess has also been reduced; in the case of a limited corporation, a company can now be established with just one shareholder. The administrative procedures relating to company establishment have also been simplified.

As regards the government's incubator policy, the basic purpose of a business incubator is to meet the needs of different types of start-up with regard to space, equipment, technology, expert manpower support, business services, information etc. Business incubators can help start-ups to develop new products and new technologies, thereby contributing to the goal of industrial upgrading and transformation. Over 80% of the business incubators in Chinese Taipei are located in universities, which are able to provide a comprehensive range of services - including technology, marketing, accounting and management services - at low cost. Those incubators are also in a good position to commercialize the results of academic research. Besides serving as a hotbed for start-up establishment, incubators can thus also contribute to the furthering of collaboration between universities and industry; they can also play an important role in industrial cluster development.

(2) Promoting Computerization and E-Commerce Adoption in the SME Sector

Since 2001, the Chinese Taipei's government has introduced a series of policy measures intended to promote e-enablement in the SME sector, including both guidance measures and plans for improving the overall ICT application environment. The key items in this comprehensive set of measures are as follows:

- a. Helping SMEs to make effective use of business-related ICT applications:
The government has provided industries support for the development of B2B e-commerce system and oriented towards the needs of SMEs. It has also set up an e-enablement service team, implemented measures to cultivate e-business talent, and set up electronic marketplaces.
- b. Promoting broadband Internet access in the SME sector: The government has encouraged SMEs to adopt broadband Internet access, which is the

foundation for successful e-enablement. A service team has been established to provide consulting services and help SMEs to deploy new broadband services.

c.Promoting online learning: Important measures adopted by the government in this area include the establishment of online learning platforms, the creation of online learning content, curriculum design and the production of online training materials.

d.Online integration of government services for SMEs: A website has been established to integrate all SME-related policy measures and projects, to make it as easy as possible for SMEs to access the information they need. This site provides a wide range of services, business matching functions and databases for the use of SMEs.

Given that a large number of SMEs demand for e-enablement service, the success or failure of the government's policies in this area will depend on how effectively the measures can be made available to all SMEs. In order to reach as many SMEs as possible, the policies should be implemented in close collaboration with local government authorities.

One major gap in the government's policy package is the need to reduce the cost of adopting e-commerce, including both broadband Internet access costs and the cost of deploying e-commerce. These costs can constitute a major burden for SMEs. While it is always possible for SMEs to rent space for website establishment or to set up an online store in an existing electronic marketplace at a lower cost, these options may not be ideally suited to the needs of individual SMEs. From SMEs' point of view, lowering costs are a very fundamental step to make e-commerce feasible for their adoption.

3. INDUSTRIAL CLUSTER POLICY

It can be seen from the statistical analysis presented above that integration into a supply chain has become the mainstream business model for SMEs in Chinese Taipei. Industrial clusters are one of the most important mechanisms for the formation and strengthening of value chains, so the Chinese Taipei's government has introduced a series of policy measures to promote industrial

cluster formation. Although not all of these measures are designed specifically for SMEs, SMEs can still benefit from them. The government has for many years been providing support for the establishment of center-satellite systems; these measures can help SMEs enter a supply chain. In the case of industrial parks and science parks, the presence of large enterprises in these parks can encourage large numbers of SMEs to locate themselves there, which therefore is more possible to become members of supply chains. In recent years, the emphasis in Chinese Taipei's industrial park and science park policy has shifted towards a focus on integration, building links with the local economy, strengthening private-sector participation, and encouraging cross-industry interactions. An industrial cluster is no longer just a collection of companies in the same industry; it will often also include research facilities, venture capital providers, business incubators, technology services providers and other types of service industry enterprises. The promotion of industrial cluster development can thus help to create new business opportunities for SMEs in the knowledge- and technology-intensive service industries and in other branches of the service sector.

Chinese Taipei's policy also includes measures to promote the development of industrial clusters in some specific areas and industries. For example, where 12 or more related enterprises are located in the same district, government supports are available for joint manufacturing, joint R&D, collaborative design, joint purchasing, joint marketing, joint distribution, etc. The goal here is to strengthen the integration of business capabilities between enterprises.⁵ The government has also been helping particular industries (such as the car parts industry) to integrate their B2B e-commerce activities, leveraging e-commerce to strengthen the industry value chain.

4. PROVIDING SUPPORT FOR R&D ACTIVITY IN THE SME SECTOR

Failure to invest in R&D is one of the major threats to the long-term development of Chinese Taipei's SMEs. As can be seen from the data presented in this report, the government's efforts have not so far been very successful in improving the R&D environment or getting SMEs to spend more on R&D. One of the key elements in the government's SME R&D policy is the Small Business Innovation Research (SBIR) project, implementation of which began in 1999. The SBIR project aims to encourage SMEs in Chinese

Taipei to step up the development of innovative technology and new product R&D. SMEs submit R&D proposals; if the proposal is approved, the SME will receive up to NT\$10 million in funding from the government, or up to NT\$50 million in the case of R&D alliances. As a quota were established in SBIR program, the SBIR project may help a limited number of SMEs that have already possessed first-rate R&D capabilities to develop innovative new products and technologies, but it is unlikely to provide a significant boost to R&D activity in the SME sector as a whole.

Another measure adopted by the government to encourage R&D activity in the SME sector is the promotion of collaboration between universities and industry. By and large, SMEs lack R&D resources and have only limited R&D capabilities. In theory, promoting collaboration between SMEs and universities should go some way towards compensating for these deficiencies, thereby helping SMEs to raise their overall technology level. In reality, however, SMEs' lack of resources and information makes it difficult for them to build collaborative relationships with the academic sector. For example, SMEs are usually not in a position to pay for technology transfer, lack the capabilities needed for collaborative R&D, do not have access to information about opportunities for collaboration with universities, and may not even be aware of the training courses and other resources that universities have to offer. In 2002, the National Science Council introduced a Plan for the Upgrading of Industrial Technology and Manpower Cultivation that targeted the SME sector. The objective was to leverage the R&D capabilities of universities and colleges to help SMEs undertake collaborative R&D. The amount of funding per project was set at NT\$400 - 500 thousands; SMEs would be required to pay 25% of the R&D costs themselves. Like the SBIR project, this plan will benefit only a small percentage of SMEs, and the funding provided will be even more limited.

Evaluation and Conclusion

Comparison of the major trends affecting the SME sector in Chinese Taipei with the government's SME policy points up two issues that have not really been addressed by the government: the gradual decline in SMEs' share of

overall economic activity, and the shift in the center of gravity of Chinese Taipei's SME sector towards the service industries with a significant increase in the number of service industry SMEs. While the decline in SMEs' share of economic activity may simply reflect a natural trend resulting from the changing pattern of economic development in Chinese Taipei, before concluding that there is no cause for concern, we need to clarify whether the decline is due to a worsening in the overall business environment for SMEs. This is a complex issue that is beyond the scope of this report; the government might want to consider undertaking systematic research in this area.

Another issue that the government has done little to address is the growing importance of the service industries within Chinese Taipei's SME sector. Leaving aside the question of whether this trend is a good or bad thing for the Chinese Taipei's economy as a whole, given that government SME policy is intended to provide service and support for SME development, there is clear need for the government to formulate a set of policies that will ensure the provision of this service and support for SMEs in the service sector.

Another important trend that the government has addressed, but where the results achieved so far appear to be rather limited, is the decline in SMEs' R&D spending and the fall in the percentage of SMEs that engage in R&D activity. It can be seen from the data presented in this report that these trends are worsening; the measures adopted by the government to tackle the problem have had little effect. The SBIR plan has much to recommend it, and will certainly help some SMEs that have already possessed significant R&D capabilities to undertake cutting-edge innovation; however, it will do little to boost R&D spending among the great mass of Chinese Taipei's SMEs. The government will therefore need to formulate additional measures that can provide an across-the-board boost to R&D activity in the SME sector as a whole.

Notes

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Policies for Developing Small and Medium Enterprises in Vietnam

By Sam Do and Thach Pham

I. The SMEs Development Policies of Vietnamese Government

1. A HISTORICAL PERSPECTIVE

In recent years, Small and Medium Enterprises (SMEs) have contributed considerably Vietnam's economy. In 2005, there were 109,738 SMEs, which account for 96.81 percent of all enterprises in Vietnam. SMEs employed 2528623 employees, representing 40.5 percent of the total number people employed by enterprises in Vietnam. In the same year, SMEs contributed 54476 billion VND, comprising 34.33 percent of tax and fees paid by enterprises in Vietnam¹.

However, SMEs in Vietnam have experienced difficulties in their development. The centrally planned economy has been in force in North Vietnam since 1954 and in the South of Vietnam since 1975. The Government has mobilized all the resources to develop heavy industry. Private ownership in Vietnam's economy has been eliminated. There was no room for private sector development. State-owned Enterprises (SOEs) and Cooperatives have played a decisive role in the national economy.

Domestic economic difficulties, the decline of assistance from the Soviet Union and East European countries, and changes in international relations forced Vietnam Government to transform its economy. At its Sixth Party Congress in 1986, the Vietnamese Communist Party launched the country's Economic Renovation (Doi Moi), marking the starting point of its reform and

open-door era. Since 1987, foreign investors have been welcome in Vietnam through the National Parliament's approval of the Law on Foreign Investment. The household-contract system implemented in 1988 under Decree No.10 has deregulated the economy in rural areas. In 1991, the private sector in Vietnam was legally recognized through the Law on Private Enterprises and the Law on Companies. Following that, the amended Constitution in 1992 allowed a "multi-sector economy in accordance with the market, based on state management and socialist orientations". The development of domestic enterprises has been promoted through the Law on Encouraging Domestic Investment adopted in 1994. In 1998, policies to speed up the equalization of SOEs were proposed. An agenda for improving economic management policies and streamlining administrative procedures to facilitate the development of SMEs was put forward by the Ministry of Planning and Investment (MPI) in 1999.

However, the business environment for the development of SMEs, mainly in the private sector, had been unfavorable. In fact, the Government still gave preferential treatment to SOEs over private sector entities. Government policies, regulations and laws on SMEs and the private sector were unstable. SMEs deal with great obstacles in mobilizing capital from financial and banking systems, and limited access to land. Moreover, SMEs face the hurdle of poor infrastructure, including inadequate access to water, electricity and the slow development of new facilities that hamper business activities.

Since 2000, the business environment for the development of SMEs has improved dramatically. The New Enterprise Law promulgated in June 1999 that took in January 2000 reduces administrative procedures for enterprises. More importantly, in November 23, 2001, for the first time since 1986, the Vietnamese Government promulgated "Supporting Policies for SME development" with Decree No 90/2001/ND-CP establishing an official framework for government support in the development of SMEs in Vietnam. Especially, at the fifth session in 2002, the Central Committee IX issued Resolution 14-NQ/TW dated March 18 to confirm Vietnamese Communist Party's efforts to continue to reform economic mechanisms and policies in order to encourage and to facilitate the development of the private sector.

2. CURRENT POLICIES

According to Government Decree No 90/2001/ND-CP, dated 23 November 2001, SMEs in Viet Nam are defined as "independent production and business establishments, which are registered as business according to the current legal provisions, each with registered capital not exceeding VND 10 billion or with an annual employment labor not exceeding 300 people. These two criteria on capital and labor may be applied in a flexible manner based on the basis of the concrete socio-economic situation of each branch or locality. (Article 3- Decree No90). Under Decree No90, SMEs include enterprises set up and operating under the Enterprise Law and the State Enterprise Law, cooperatives set up and operating under the Cooperative Law, and business households registered under Government Decree No. 02/2000/ND-CP of the Government of February 3, 2000 on business registration (Article 4 Decree No90).

Under Decree No90, the Vietnamese Government has identified developing small and medium-sized enterprises (SMEs) as an important task in its strategy for socio- economic development and acceleration of national industrialization and modernization. The view of the State on SMEs is clearly expressed through the State's encouragement and provision of favorable conditions for SMEs to bring into play their activeness and creativeness, raise their managerial capability, develop science, technologies and human resources, expand their cooperative ties with enterprises of other forms and increase their profits as well as competitiveness in the market; develop production and business, create jobs and improve the laborers' lives (Article 1- Decree No90).

The Vietnamese Government's supporting policies consist of investment encouragement, establishment of the credit guarantee fund for SMEs, assisting SMEs to enhance their competitiveness by providing opportunities for SMEs to access information on markets and prices and assist them to expand markets and sell their products, export promotion, on information, consultancy and human resource training.

According to Decree No 90, SMEs are placed under comprehensive management. This Decree established a Department for SME Development under the MPI for the first time to assist the ministry in performing the

function of State management over SME development promotion. Moreover, the Decree also set up the SME Development Promotion Council chaired by the Minister of the MPI, which is responsible for advising the Prime Minister on mechanisms and policies to encourage the development of SMEs.

The members of the SME Development Promotion Council come from various ministries. There are representatives from MPI, the Ministry of Industry, the Ministry of Finance, the Ministry of Agriculture and Rural Development, the Ministry of Construction, the Ministry of Communications and Transport, the Ministry of Trade, Ministry of Science, Technology and Environment, the Ministry of Transport, the Ministry of Education and Training, the Ministry of Labor, War Invalids and Social Affairs, and the Ministry of Justice. The SME Development Promotion Council also includes representatives of the People's Committees of Hanoi, Ho Chi Minh City, Hai Phong and Danang, the most dynamic economic cities in Vietnam. Business associations such as the Viet Nam Chamber of Commerce and Industry, the Central Council of the Union of Vietnamese Cooperatives and a number of enterprise associations also have representatives in this Council. In particular, this Council's membership also includes some a number of economic, scientific, technological and training experts. In fact, it took quite a long time to activate this new mechanism. After only fourteen months, Decree No 90 was issued and the SME Council was officially established on January 17, 2003 under Decision No.12/2003/QĐ-TTg by the Prime Minister. Two months later, on 24 March, 2003, the President of the SME Council promulgated the Regulation of Activities of SME Council under Decision 185/QĐ/BKH to stipulate the functions, tasks, mandate, operational mechanism, and working relations of the SME Council in detail.

Under Decree No 90, the SME Technical Support Centers under the Department for SME Development) were set up to provide support to both authorized organizations of the government and SMEs. These Centers advise the Department for SME Development and consult on technological and technical matters, renovation of equipment, guidance for technical management and maintenance of equipment, creating conditions for SMEs to acquire new technologies and equipment. On May 12, 2003, the Minister of MPI issued Decision No 290/QĐ-BKH to officially establish the SME Technical Support Centers in Hanoi, Danang and Ho Chi Minh City.

The SME Technical Support Centers have the following mandates (Article 2 Decree No90):

- (1) Providing technical assistance and advice to SMEs on investment for technology, application of new techniques application, innovation, and improvement of product quality;
- (2) Organizing training and courses on technical and technological management by the request of SMEs;
- (3) Promoting the cooperation and linkages among SMEs and large companies;
- (4) Acting as focal point in providing and disseminating information on techniques and technology for SMEs;
- (5) Developing a database of consultants on techniques and technology to meet the demands of SMEs;
- (6) Engaging and collaborating in research of technology application, technology transfer, assisting SMEs in accessing new technology (including the secondary technology and new products);
- (7) Carrying out other duties as assigned by the General Director of ASMED and the Manager of the Department of Personnel and Organization.

Establishing Credit Guarantee Funds for SMEs

Access to funds is a challenge the development of SMEs. Therefore, to meet the demand of SMEs for capital, and follow in Decision No 90, the Vietnamese Government set up Credit Guarantee Funds for SMEs. On December 20, 2001, the Vietnamese Prime Minister signed Decision No 193/2001/QĐ-TTg on issuing Regulation on the Setting up, Organization and Operation of Credit Guarantee Funds (CGFs) for SMEs. CGFs were set up and managed by the People's Committees of the provinces and centrally-run cities in order to provide credit guarantee to SMEs (Article 1).

CGFs are non-profit financial institutions ensuring the recovery of capital and self-payment of expenses. They have the status of charter capital, balance sheet and their own seal and may open accounts at the State Treasury and domestic commercial banks. CGFs are exempt from tax payment and State budget remittances in activities providing credit guarantee to SMEs (Article 2). On June 25, 2004, the Vietnamese Prime Minister issued Decision No 115/2004/QĐ-TTg on Amending and Supplementing the Regulation on the Setting up, Organization and Operation of Credit Guarantee Funds for SMEs, which was promulgated together with the Prime Minister's Decision No 193/2001/QĐ-TTg of December 20, 2001 with a change in sources of CGFs operational capital.

Box 1: Sources of CGFs's operational capital (Decision No 193/2001/QĐ-TTg)

1. Starting capital, including:
 - a. Capital allocated from the budget of a province or a centrally-run city.
 - b. Capital contributed by credit institutions;
 - c. Capital contributed by enterprises;
 - d. Capital contributed by production and/or business associations, organizations representing and supporting SMEs.
2. Lawful aid capital (including ODA capital) provided by organizations and individuals inside and outside the country for the purpose of developing SMEs, cooperatives as well as agricultural, forestry and fishery development programs.
3. Capital supplemented from the results of operation of CGFs as prescribed.

CGFs are set up when they meet the following conditions: (1) Having sufficient starting capital of at least VND 30 billion; (2) Having a list of the members of the Management Council, Control Board and Executive Board with full civil act capacity and professional qualifications suitable to the operation requirements of the CGF; (3) Having a draft charter and organizational and operational plan of the CGF, which accord with the provisions of this Regulation and other legal provisions.

The CGF's Management Council has the following tasks and powers: (1) To submit to the president of the People's Committee of the province or centrally-run city for ratification, supplement and/or amendment the CGF's charter and operational mechanism; (2) To adopt the CGF's operational orientation, financial plan and final account settlement reports; (3) To perform tasks and exercise powers as provided for in the charter of the CGF; (4) To supervise and inspect the CGF's activities according to its charter and the decisions of the Management Council; (5) To decide on the appointment, dismissal, commendation, reward and discipline of members of the Control Board; (6) To examine reports of the Control Board and settle complaints as prescribed. To be entitled to use the CGF's seal to perform the Council's tasks and exercise its powers (Article 10)

A CGF shall provide grant credit guarantees to the following types of : (1) Enterprises of all economic sectors, which are classified as SMEs according to law provisions; (2) Cooperatives and unions of cooperatives; (3) Individual business households as prescribed by the Government's Decree No. 02/2000/ND-CP of February 3, 2000 on business registration; (4) Farm owners, peasants' and fishermen's households' that carry out projects on aquaculture, offshore fishing, planting of industrial trees or husbandry... (Article 14)

Box 2: Conditions for being granted credit guarantee

- (1) Having feasible investment projects and production and/or business plans, being capable of repaying loan capital;
- (2) The total value of the CGF's properties mortgaged or pledged at credit institutions is equal to at least 30% of the loan value as prescribed by law;
- (3) Owing no tax debts or overdue debts to credit institutions or other economic organizations.

Credit guarantee levels are stipulated in this Regulation. According to the Regulation, a CGF shall provide credit guarantees equal to no more than 80% of the difference between the loan value and the value of the customer's

properties mortgaged or pledged to credit institution(s). The credit guarantee level for a customer shall not exceed 15% of the capital of the CGF's owner.

On September 29, 2004, the Minister of Finance issued Circular No. 93/2004/TT-BTC, providing guidance on the regulations on setting up, organization and operation of credit guarantee funds for small - and medium - sized enterprises. According to this Circular, the conditions for setting up a credit guarantee fund include:

- Having a scheme on setting up of a credit guarantee fund already approved by the president of a provincial/municipal People's Committee. The scheme contents must prove the credit guarantee demands of small- and medium-sized enterprises operating in the locality, and a feasible plan for the organization and operation of the credit guarantee fund for the first three years.
- Having sufficient starting capital of at least VND 30 billion allocated by the provincial/municipal budget and/or contributed by organizations and individuals at home and abroad.
- Having a list of members of the management council, the control board and the executive board, who have the professional qualification, university degrees and at least 5 years' experience of working in the economic or financial sector.
- Having a draft charter compliant with the provisions of Article 6 of the Regulation on setting up, organization and operation of credit guarantee funds, promulgated together with the Prime Minister's Decision No. 193/2001/QĐ-TTg and other legal provisions.

Within 6 months after the presidents of the provincial/municipal People's Committees have issued decisions on their establishment, the concerned credit guarantee funds are required to commence their operations. At least 30 days before commencing its operation, the credit guarantee fund must publish in a newspaper or announce through the mass media its office address for three consecutive issues its setting-up decision, operational contents and scope, and its clients.

On February 20, 2006, the Governor of the State Bank of Vietnam issued Circular 01/2006 on capital contributions to Credit Guarantee Funds for SMEs. This Circular provides instructions on the contribution of capital to set up the Credit Guarantee Fund for SMEs by credit organizations which are, as follows:

- a) The amount of capital contribution from a credit organization to a credit guarantee fund can not exceed 11% of the starting capital of the credit guarantee fund
- b) The total amount of capital contribution to the credit guarantee fund and other commercial investment can not exceed 40% of the starting capital and reserve fund of the credit organization
- c) A representative must be appointed the preparatory committee to set up the Credit Guarantee Fund upon request of the provincial/municipal People's Committee
- d) The Management Council of the Credit Guarantee Fund should include representatives reflecting the capital contribution by the credit organization as per the Decision of the Chairman of the provincial/municipal People's Committee.
- e) The credit organization should cooperate with the credit guarantee fund to develop the guarantee process and procedures. Cooperate with the credit guarantee fund to inspect and monitor the process of using loans and debt payment of the debtors, ensuring the safety of the capital

Trade Promotion Programs

The Vietnamese Government has designed trade promotions programs to provide business information to SMEs. On September 27, 2002, the Minister of Finance issued a Circular on Guidelines for Expenditures in Support of Trade and Export Promotion Activities. According to this Circular, the State shall annually put aside a budgetary amount based on export turnover to

support trade and export promotion activities under national key programs (trade promotion programs). It aims to:

- Create conditions for enterprises to access export markets.
- Improve the competitiveness of export products.
- Raise export-marketing knowledge and skills.
- Diversify exports, reform the commodity structure and expand export markets.
- Propagate Vietnamese exports.

On the basis of the State's export orientation for each period, the Ministry of Trade shall assume the prime responsibility for synthesizing the news of various ministries and agencies, and evaluating and proposing key national trade promotion programs, clearly stating their content, implementation duration, managing agencies and funding estimates, for submission to the Prime Minister for approval.

Based on the financial capacity of local units, the presidents of the provincial/municipal People's Committees can set up local trade promotion funds or export support funds for spending on export promotion, including trade promotion activities prescribed in the Circular mentioned above. The provincial/municipal Trade Services shall assume the prime responsibility for formulating key local trade promotion programs for submission to the provincial/municipal People's Committees for approval. The principles governing such support are as follows:

- Funding for the implementation of key trade promotion programs shall be contributed by participating enterprises and partly supported by the State via the program-managing agencies.
- The agencies assigned to manage the programs shall ensure that funding is used economically and efficiently, and take responsibility for the spending contents strictly according to current regimes.

Box 3: Contents of key trade promotion activities eligible for support cover

- 1.1. Gathering trade information, conducting export promotion and setting up data centers in support of enterprises;
- 1.2. Providing export advisory services;
- 1.3. Organizing training courses in order to raise export capacity and skills of enterprises;
- 1.4. Organizing export fairs and exhibitions;
- 1.5. Surveying and seeking export markets;
- 1.6. Promoting for national trademarks and typical export products;
- 1.7. Providing initial expenses for building infrastructure for trade promotion: building bonded warehouses, trade promotion centers and exhibiting export products at home and abroad;
- 1.8. Conducting research on the application and development of e-commerce related to exports;
- 1.9. Other trade promotion activities identified by the Prime Minister.
- 2.0 Entities qualified for support are enterprises from all economic sectors covered by key trade promotion programs.

Support levels

- To support 50% of expenses for activities stated at points 1.1 to 1.5
- To support 70% of expenses for the remaining activities. Special cases shall be decided by the Prime Minister or the presidents of the provincial/ municipal People's Committees (for local Unit).

Entities receiving support include trade associations, trade promotion agencies under various ministries and agencies, and eligible enterprises designated to act as agencies managing national key trade promotion programs approved by the Prime Minister (for programs supported by the central budget) or the presidents of the provincial/municipal People's Committees (for programs supported by local units' budgets). Enterprises providing trade promotion services shall not be entitled to support.

Capital used for support is provided by the State. Annually, the State puts aside a budgetary amount equal to 0.25% of the total national export turnover

of the previous year (excluding crude oil turnover) and transfers such amount into the Export Support Fund to form the support source for national key trade promotion programs. In cases where such amounts are not paid out, the remainder is deducted into from amount to be spent in the subsequent year. The provincial/municipal People's Committees shall use the capacity of their local units and the demand for export promotion spending as a basis for deciding the appropriate levels of deduction for the local trade promotion funds or export support funds.

In January 2003 Ministry of Trade Decision No. 104/2003/QĐ-BTM on the Regulation on Formulation and Management of National Key Trade Promotion Programs was promulgated. Key national trade-promotion programs are trade-promotion programs which are approved by the Prime Minister as proposed by the Ministry of Trade's proposal, aiming to develop exports and raise the competitiveness of Vietnamese commodities, focusing on key commodities and key markets. Annually, the Ministry of Trade shall announce the list of key commodities and key markets. (Article 1)

The programs' requirements are as follows: (1) The program should to boost export growth and raise the competitiveness of Vietnamese commodities; in line with the national export development goals for each period, and prioritizing key commodities and key markets as announced annually, (2) It should be compatible with the contents of key trade-promotion activities under the guideline of Section 1, Part II of the Ministry of Finance's Circular No. 86/2002/TT-BTC dated September 27, 2002. (3) It should be feasible and rational in terms of implementation mode; pace and timelines; human resource, financial and material requirements as well as technical foundations. (4) For some activities as mentioned below, apart from these requirements, the program must also satisfy the following:

a) Organizing or participating in overseas trade fairs and/or exhibitions:

- Multi-branch fairs and exhibitions must have 20 standard pavilions (3mx3m) or include the participation of at least 18 enterprises.
- Specialized fairs and exhibitions must have 10 standard pavilions or involve the participation of at least 8 enterprises.

b) Organizing or participating in domestic fairs and/or exhibitions:

- Fairs and exhibitions in Hanoi and Ho Chi Minh City must have 350 standard pavilions or involve the participation of at least 300 enterprises.
- Fairs and exhibitions in other localities must have 250 standard pavilions or involve the participation of at least 200 enterprises; particularly, fairs and exhibitions in localities bordering on neighboring countries must have 120 standard pavilions or involve the participation of at least 90 enterprises.

c) Organizing or participating in delegations for market surveys or commercial transactions in foreign countries:

- Multi-branch delegations must be composed of at least 18 enterprises.
- Specialized delegations must be composed of at least 8 enterprises.

d) Training and/or fostering courses for strengthening export capacity and enterprise skills must be attended by at least 50 trainees (Article 4).

On November 3, 2005, the Prime Minister promulgated Decision No.279/2005/QĐ-TTg on the Regulation on the Elaboration and Implementation of the 2006-2010 National Trade Promotion Program. It aims to enhance trade promotion activities, develop export markets; create initial conditions for building material foundations in service of trade promotion activities; contribute to capacity-building for business community; link trade promotion activities with investment and tourism promotion for the period 2006-2010.

Box 4: The Program's contents (trade promotion schemes) eligible for supports

1. Trade information and export promotion, including the organization of visits to Vietnam by representatives of foreign mass media agencies to write about Vietnam's exports.
2. Hiring domestic and foreign experts to advise on the development of export and the design of models and products to raise the quality of goods and services.
3. Organizing domestic and overseas training to improve export capacity and business skills. For overseas training courses, government support shall be concentrated on specialized training courses to develop new products lasting no more than 3 months.
4. Organizing, participating in trade fairs and/or exhibitions
 - a) Organizing or participating in overseas trade fairs and/or exhibitions
 - For multi-branch fairs and/or exhibitions, each must have at least 15 standard commodity pavillions (3m x 3m) or involve at least 12 enterprises;
 - For specialized fairs and/or exhibitions, each must have at least 7 standard commodity pavilions or involve at least 5 enterprises;
 - b) Organizing domestic fairs and/or exhibitions of export goods
 - For fairs and/or exhibitions in centrally-run cities, each must have at least 200 standard commodity pavilions or involve at least 150 enterprises;
 - For fairs and/or exhibitions in other localities, each must have at least 150 standard commodity pavilions or involve at least 120 enterprises. Particularly for fairs and/or exhibitions in localities bordering on neighboring countries, each must have at least 100 standard commodity pavilions or involve at least 80 enterprises.
5. Organizing delegations for market survey or commercial transactions in foreign countries
 - a) For multi-branch delegations, each must involve at least 15 enterprises;
 - b) For specialized delegations, each must involve at least 7 enterprises.
6. Organizing general promotion activities (combining trade with investment and tourism) to boost Vietnamese exports of goods and services and to attract foreign investment and tourists to Vietnam.

7. Introducing into overseas markets specific brands of goods or services that have been awarded export prizes by the Prime Minister under annual national branding programs and promoting their penetration of such markets.
8. Building trade promotion infrastructure at home and abroad: a) To set up overseas trade promotion centers; b) To set up domestic trade promotion centers;
9. Formulating and applying an electronic business process; applying branch standards on electronic data exchange.
10. Other trade promotion activities as decided by the Prime Minister.

Human Resource Development Programs

Along with establishing Credit Guarantee Funds and implementing Trade Promotion Programs, the Vietnamese Government also carries out human resource development programs to improve the quality of SMEs' human resources. On August 10, 2004, The Prime Minister issued Decision No 143/2004/QĐ-TTg on the Human Resource Development Program to assist SMEs. It is part of the overall policies and assistance programmes undertaken by the State for the benefit of SMEs as specified by Decree No. 90/2001/ND-CP dated November 23rd, 2001 by the Government in support of SME development. The Vietnamese Government realizes that at present SMEs' capacities are limited, and that training for SMEs' management personnel is still inadequate. Meanwhile, the demand of businessmen and SMEs for training managers has increased continuously, so that the state's assistance in training management human resources for SMEs has become very necessary.

The programs objective combines both overall and specific objectives. The overall objectives of this program include promoting and facilitating SMEs' competitiveness, contributing more and more to national socio - economic development; developing in terms of quantity and quality the system for assistance and provision of business development services, especially consultancy and human resources training to assist the growth and sustained development of SMEs. Specific objectives consist of providing the necessary knowledge to businessmen, SME managers, and people intending to establish

enterprises; overcoming the inadequacy of knowledge, skill and information; the gradual enhancement of management capacity, and the development of techniques, technology and human resources to meet the growing demand of SMEs; and assisting SME managers with the knowledge and skills to formulate their business and production strategies, expand the domestic and overseas markets and to integrate themselves into the global economy.

The scope of this programme covers: a) SMEs and businessmen: Training on enterprise administration for owners and managers, including training on business management, business planning, marketing administration, accounting and financial administration, human resource management, technical-technological management; marketing consultancy; training on business start-ups. b) Business assistance service providers: Training and enhancing the quality of assistance service providers for SMEs in special area to ensure quantity, quality of lecturers to implement the Programme. This Programme lasts 5 years from 2004 to 2008.

Box 5: Training human resource programme content

1. Training human resource for SMEs:
 - a) Training on business start up provides necessary information on the law and policies of the Party and the State, regulations on the establishment and operation of enterprises; knowledge and skills to formulate business and production plans and strategies. This part includes short courses lasting 5 days.
 - b) Training in business administration includes short courses lasting 7 days with the following content:
 - Increasing the capacity of SMEs to formulate plans and manage business and production activities through courses on general business management.
 - Strengthening the personnel management capacity of SMEs through courses on human resources management.
 - Strengthening the marketing capacity of SMEs through courses on marketing administration.
 - Assisting SMEs in formulating marketing plans and developing their

marketing skills, and ability to effectively participate in fairs and exhibits through courses on planning and marketing.

- Strengthening accounting and financial management skills of SMEs through courses on accounting and financial administration.
- Strengthening the SMEs' management capacity related to techniques, technology, intellectual property and quality standards through courses on technique and technology management.

2. Enhancing the quality of business services providers:

In order to intensify skills of general business services providers, various training activities are offered under the Programme, which contains as following:

- Training in general consultancy and marketing skills for consultants and lecturers and encouraging them to upgrade their professional standards.
- After participating in general consultancy training courses, business services providers are trained intensively in business start-ups, general business administration, marketing administration, accounting and financial administration, business planning, technique and technology administration, and human resources administration.

This part of the training includes short courses lasting about 14 days.

3. Programme implementation plan:

It is anticipated that in 5 years, the Programme shall be implemented as follows:

- Developing basic training materials.
- Carrying out 18 training courses for 540 lecturers.
- Carrying out 3,589 various training courses for SMEs and individuals as well as, organizations intending to establish business for about 107,670 people.

Decision No 143 specifies in detail the rate of progress of programme implementation. The Programme will be implemented in two periods. The first period is from 2004 to 2005, which focuses on building the foundations of the programme, such as through research, surveys of specific demand for training by SMEs, and planning the implementation of the programme; selecting and cooperating with organizations currently conducting human resources training, regardless of economic sector, organizational model and

location to effectively implement the programme, meeting the demand from SMEs in industrial sector; organizing seminars to discuss with domestic and overseas organizations that have experience in training and capacity-building for SME owners and managers in order to draw lessons in implementing the programme; preparing textbooks and necessary documents to improve the management mechanism for implementing the programme through pilot training courses. The second period is from 2006 to 2008, during which training courses are offered. Programme expenditure amounts to VND 119.4 billion (USD 75 million).

On November 24, 2004, the Minister of MPI issued Decision No. 1347/2004/QĐ-BKH on Guidelines for the Implementation of the SME Human Resource Development Program. The Human Resource Training Support Program for SMEs for the period 2004-2008 is a state target program specifically for SMEs, which is organized, implemented and managed under current regulations (Article 1). The purpose of the program is to provide essential knowledge for businesspersons, managers of SMEs and those who intend to set up their own enterprises; to overcome shortcomings in terms of knowledge, skills and information; to create favorable conditions for enterprises to progressively enhance their managerial capability and technological and human resource development for faster growth; and to help equip SME managers with knowledge and skills in formulating business strategy and undertaking internal and external market expansion in response to international economic integration (Article 2). The beneficiaries of the training are businesspersons, SME owners and managers and trainers (Article 3). The topics of training cover : (1) business start-up; (2) business management for SME managers, including general business management, human resource management, marketing management, market expansion, marketing planning and skills, financial and accounting management and technological management; (3) improving service quality for providers of training services, such as general consultancy, training skill and service marketing, and specialized training for different components of the program.

The program gives priority to trainees who are businesspersons, and SME owners and managers in the following sectors: labor-intensive and potential labor-intensive SMEs; SMEs undertaking business and production in government-encouraged sectors; SMEs with great export potential for

products and services; SMEs that are able to absorb laborers and disabled workers; SMEs that have not yet participated in the program; and are female entrepreneurs.

Trainers from service providers who need capacity building and training fulfill the following requirements: possess a bachelor's degree or a professional certificate for training consultancy or business consultancy if legally required; having lectured on or possess qualifications in a specific area and needing to acquire higher skills and competence to be able to participate in the program; committed to implement at least 3 training courses for the program after undergoing training; and not having been the subject of the legal action or meted administrative punishment in the area of consultancy and/or training that he/she is providing.

Priorities will be given to trainers who belong to training service providers, business associations, sectoral associations especially for sectors and areas that the government is encouraging; and those who have already attended a training [-for-trainer] course in the program but have been identified as needing be retrained.

After 4 years of implementing the Enterprise Law, Encouraging SME Development Law and other relevant laws and regulations, the development of SMEs has achieved considerable progress. These policies have facilitated the growth of SMEs nationwide, promoted innovation and entrepreneurship, contributed to growth and economic restructuring and helped address social issues.

However, serious obstacles for the development of SMEs remain. The Vietnamese Prime Minister, in his Directive No 27/2003/CT-TTg on Continuing to Step up Implementing Enterprise Law, Encouraging SME Development dated December 11, 2003, admits that "the right to freely engage in business under State regulations has not been fully ensured; policies on assisting SMEs have been implemented slowly; management of state-owned enterprises is still inadequate; there are still cases where legal document issuance doesn't correspond to business and production requirements; procedures to access markets are still irrational and involve high costs and delays prolonged time, especially in branches with conditional

businesses; plans for branch development still require repeated amendments, which poses obstacles to new business and investment expansion; occasional resort of some enterprises to illegal activities in order to circumvent extraordinarily strict and complicated regulations; agencies, officials and civil servants, and arbitrary imposition of inconvenient administrative procedures by particular, which have caused enterprises to miss opportunities and suffer costs. On the part of enterprises, knowledge of the law attitudes of a number of owners and managers leave much to be desired; some enterprises do business dishonestly, and violate legal regulations deliberately; internal management is weak and not transparent; SMEs have no linkages, cooperation efficiency and competitiveness are low; business associations are not clear about their proper roles, and are not sufficiently supportive of their members development."

To continue to strengthen and support the development of SMEs, on October 7, 2005, the Prime Minister issued Directive No. 40/2005/CT-TTg regarding the Resolution of the SME Council on the SME Development Plan for 2006-2010. The Prime Minister directed ministers, heads of ministerial level agencies, heads of government agencies, chairmen of People's Committees of provinces and centrally governed cities to ensure the effective implementation of measures and tasks with the goal of creating a favorable business environment and support for enterprises. Ministries, agencies, and provincial governments are expected to act on their own initiatives and submit proposals to the government, and the Prime Minister for the promulgation of guiding legal documents within their competence, and in the meantime, provide the necessary conditions for the implementation of Enterprise Law and Investment Law after they have been approved by the National Assembly.

Recently, on October 23, 2006, the Prime Minister issued Decision No. 236/2006/QĐ-TTg on the Approval of the SME Development Plan for 2006-2010. This Decision confirms the commitment views of the Vietnamese Government to SME Development. Under this Decision, the guiding principles for SME development are set out, as follows: (1) implement consistently the policy of building a multi-sectoral economy. Economic sectors that do business in compliance with legal regulations are all important constituent parts of a socialist oriented market economy with a vision of long term development, cooperation and healthy competition; (2) Create a sound

policy, legal and institutional environment that ensures fair and healthy competition for SMEs and service providers from all economic sectors so as to mobilize all internal and external resources for development investment; (3) Develop SMEs in an active but sustainable way, enhancing quality and quantity to achieve economic efficiency and the goal of contributing to employment generation, poverty reduction, ensuring social safety and security. SME development objectives are also to be integrated into national goals and to specific socio-economic goals of every region and locality, encouraging agricultural industries and traditional sectors with a focus on SME development in mountainous areas and regions confronted with socio-economic difficulties. SMEs owned by ethnic minorities, women and the disabled...should be prioritized and supported with priority given to SMEs (4) Gradually shift from direct support to indirect support in enhancing the capacity of SMEs; (5) Link business activities with environmental protection and ensuring social security and safety (6) Raise awareness of governments at all levels about the role played by SMEs in socio-economic development².

II. Challenges for the development of SMEs in Vietnam

The results of surveys conducted by the General Statistics Office of Vietnam in 2004, 2005 and 2006 revealed that 96.81 percent of total enterprises were SMEs in 2005. Enterprises with less than 10 employees accounted for 51.30 percent. Enterprises having between 10 and 200 employees made up 44.07 percent. Enterprises with 200 to 300 employees accounted for 1.43 percent. By size of capital, enterprises with less than 1 billion VND accounted for 41.80 percent. Enterprises with 1 and 5 billion VND composed 37.03 percent. Enterprises with 5 to 10 billion VND account for 8.18 percent.³

In process of development SMEs, in Vietnam face many challenges as shown in a survey conducted by the Agency of SME Development, MPI in 2005. The sample of the survey was 63,000 enterprises in 30 provinces and cities in the North of Vietnam, in various industries.

High need on capital, market and training

The results of the survey show that the enterprises' capital size is relatively small. Nearly 50 percent of enterprises have capital amounting to less than 1 billion VND (62,000 USD). Nearly 75 percent of enterprises have less than 2 billion VND (124,000 USD). 90 percent of enterprises have less than 5 billion VND (310,000 USD). Due to their small scale of production, their competitiveness is low. Technological innovation is urgently needed, but is really difficult to carry out due to SME's budget constraints.⁴

Access to capital is the most important challenge facing the development of SMEs. 66.95 percent of enterprises always face difficulties in finding the needed capital. In terms of accessing government funds, only 32.38 percent of enterprises have been able to access these; most of them are SOEs and equitized enterprises. 35.24 percent of enterprises are able to access these funds with difficulty, and 32.38 percent of enterprise are completed unable to access these funds. Meanwhile, accessing other funds is also difficult. Only 48.65 percent of enterprises are able to access these other funds, and 20.9 percent of enterprises are unable.⁵

SMEs also face other challenges. 50.62 percent of enterprises cope with obstacles to market expansion, 41.7 percent of enterprises face hindrances with respect to land, and production sites, 25.22 percent face difficulties with the high cost of production, 24.23 percent lack support through preferential tax. 19.4 percent face difficulties due to lack of information, and 17.56 percent have difficulties with human resources training.⁶

Moreover, participating in Trade Promotion Programs of the government is also difficult. Only 5.2 percent of enterprises have participated in such programs. 23.12 percent find it difficult to participate, and 71.67 percent have never participated.

Training needs in various fields are acute. 33.64 percent of enterprises need training in finance, and accounting, 31.62 percent in corporate governance, 24.14 percent in marketing, 20.17 percent in formulating business plans, and business strategy, 12.89 percent in developing new products, 12.89 percent in negotiating skills and contracts, 11.62 percent in human resources

management, and 10.85 percent in the application of IT.⁷

Inadequate management and technology

According to the survey, 55.63 percent of entrepreneurs have middle-level education, while 43.3 have junior-level and high-school education or below. The entrepreneurs who hold PhD account for only 0.66 percent; those who hold Master's degrees 2.33 percent, and those with university education 37.82%. One interesting characteristic is that most entrepreneurs, including those who hold university and advanced degrees often are not trained in economics and corporate governance. It does impact on the effectiveness of business plans, business strategy and the management of Vietnamese enterprises.

In terms of technology, only 8 percent of enterprises have advanced technology, most of whom are Foreign Direct Investment Enterprises. Although 60 percent of enterprises use computers, only 11.55 percent of enterprises use LAN networks, and only 2.16 percent of enterprises have their own websites.⁸

These results show dire situation with regard to the potential of enterprises in North Vietnam to participate in E-commerce and exploit business information which; does not meet the expectations of the Government with respect to the development of e-commerce.

This survey also shows a paradox: while the level of technology is low, the need of enterprises for training in technology is also very low, and only 5.65 percent of enterprises surveyed expressed a need to be trained in technology. It means that Vietnamese enterprises in general and enterprises in the North in particular do not appreciate technology, regardless of it being the decisive factor for the success of enterprises in the market.

The survey shows one difference between Vietnamese enterprises and foreign enterprises. While foreign enterprises care much about technology and technical progress, and market supply and demand, Vietnamese enterprises

only care about information on business mechanism and policies on enterprises.⁹

III. Solutions for the Development of SMEs in Vietnam

After Vietnam's accession to the World Trade Organization at the end of 2006, the pressure on SMEs has increased. They have to struggle to enhance their competitiveness as soon as possible with the highest effectiveness in order to deal with international competition. Strengthening CGFs, and technological innovation are essential for SMEs. However, in the short-term, SMEs need more support with information on markets, marketing their products and intellectual property rights.

In recent years, government agencies and international organizations have undertaken great efforts to support SMEs. The Vietnamese Government has implemented several policies to encourage the development of SMEs. Governments at the local level also actively facilitate the development of SMEs. For example, Ho Chi Minh City established an Investment and Trade Promotion Center to provide business information for SMEs, and to offer training courses for SMEs on corporate governance. Seniors officials of the Vietnamese Government also regularly meet with SMEs to explore the problems that SMEs face and how to solve them. The Norwegian Agency for Development Cooperation (NORAD) and the United Nations Industrial Development Organization (UNIDO) recently agreed to provide a technical aid, which cost 626,000 USD, to improve the business environment in Vietnam from July 2006 to March 2007.¹⁰

There are many policies issued to promote the development of SMEs, but SMEs still lack channels to obtain information about these policies. From this perspective, the role of business associations is very important.

Business associations can represent the interests of SMEs in many industries vis-à-vis the Government. They can also provide essential information for SMEs. After Vietnam joined the WTO, enterprises benefited from adoption of WTO requirements with respect to the transparency of the legal system,

providing an enabling business environment, tariff-reduction commitments, and market access both in Vietnam and in other WTO members. With SMEs lacking capabilities to obtain the needed information on the WTO, business associations can help them take advantage of opportunities in international trade.

Moreover, business associations can help SMEs to resolve international trade disputes. The role of business association has been very clearly demonstrated in recent trade disputes involving Vietnam enterprises during the past few years. Such as in anti-dumping cases related to cat-fish, gas-lighters, bicycles, and leather shoes.

However, there are few business associations today in Vietnam that are able to play well their roles efficiently. Many business associations have been established because it is fashionable to do so, but most of them have unclear roles.

In conclusion, since 2000 the Vietnamese Government has undertaken great efforts in formulating policies on SME development. These policies have encouraged the development of SMEs in Vietnam. However, SMEs in Vietnam still face many difficulties. Business associations can play an important role in promoting SMEs.

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Overview of SME Policies in Selective Economies

Overview of SME Policies in Selective Economies

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Multiple Facets of the SME Sector

It is now commonly agreed that a healthy industrial structure requires enterprises of all sizes play complementary roles in an economy, SMEs as well as their larger counterparts (Marshall, 1890). Much attention has been paid to the development of SME sector as well as the corresponding policies. A number of experts were invited to contribute to the PECC project, "The Policy Environment for the Development of SMEs". This analysis is drawn from a review of the contributing studies of SMEs in ten PECC member economies, consisting of Australia, Canada, Chile, Columbia, Japan, Korea, New Zealand, Singapore, Chinese Taipei, and Vietnam.

One major lesson drawn from the studies of the task force is that there is heterogeneity inherent in the SME sector. It is also well noticed that the roles SMEs played in economies with varies degree of economic development may be different. Even within the same economy, the SME sector itself demonstrates transformations throughout the economic development process, and SMEs may play different roles in different regions of the economy at the same time. But still, there is a general consensus that a sound SME sector is conducive to economic development. We see SME policies design or redesign in these economies to fulfill the ultimate goal of boosting the socio- economic growth.

Under the versatile facets of SMEs, however, there are some important common characteristics shared by all SMEs in essence. Before we ardently adjust the policy, we have to put these features of SMEs into consideration. It is obvious that most host economies initiated their SME policies based on more than one of the prominent features of SMEs, they are job generation, competitiveness, resilience, networking, and entrepreneurship.

JOB GENERATION

The existence of SMEs provides more employment possibilities. For example, SMEs offer employment opportunities in the rural area where no large firm exists. Since small businesses tend to use more labor-intensive technique in production than their larger counterparts, they do absorb a larger amount of labor relative to turnover size.

SMEs also help providing jobs where there is certain discrimination in large firms, or where discouraged workers find their prospects of promotion blocked in large firms. Barriers to employment can be resolved in SMEs as discouraged workers become self-employed. We notice women entrepreneurs are encouraged in many economies when the chance of being hired is low. Further, the probability that an owner of an SME is a former employee of an SME is greater than their being a former employee of a large firm. The fact that small companies breed other small companies creates a virtuous cycle help to relief the unemployment problem of an economy.

COMPETITIVENESS

It is common knowledge that SME sector has higher entry and exit rate than large firms do. The successful small firms 'graduate' into large firms. Those who fail will soon be replaced by their better peers. Thus SMEs remain the most competitive sector in a Darwinian sense (Hu, 2003a). Given the intensity of competition, it is natural that the failure rate among SMEs should be high. Fortunately, the entry rate is also high for SMEs in contrast to large firms, so that there are always enough newcomers to replace those that fail. SMEs, as the 'competitive fringe', are among the most vibrant actors in the marketplace. This helps to create a healthy industrial environment for an economy's continuous thrive, as Alfred Marshall (1890) put it in his forest

allegory:

...We may read a lesson from the young trees of the forest as they struggle upwards through the benumbing shade of their older rivals. Many succumb on the way, and a few only survive; those few become stronger with every year, they get a larger share of light and air with every increase of their height, ...Though the taller ones have a better access to light and air than their rivals, they gradually lose vitality; and one after another they give place to others, ... And as with the growth of trees, so was it with the growth of business as a general rule...

There are many real life cases of such healthy industrial environment, for example, the empirical evidence provided by Aw and Roberts (2003) suggests that in contrast to Korea, Chinese Taipei as an economy with abundant SMEs provides strong competitive pressures that lead to market selection based on productivity differences. With the competitiveness stimulated by a well-performed SME sector, the looser market structure decreases the share of producer surplus and pushes the economy further closer to welfare maximization (Scherer and Ross, 1990).

RESILIENCE

Apart from the labor-intensive SMEs' well-noticed contribution in the labor markets, and their provision of competitive mechanism in the economy, SMEs are also considered outperforming their larger counterparts in dealing with the business downturn due to the flexibility rooted in SME sector, as they provide the resilience needed in the turmoil. The SME sector as a whole is often considered more flexible than the larger firm sector. They can respond quickly to outside change. Stigler (1939) long ago pointed the smallness that enables a firm to respond quickly to outside changes could be more important than scale efficiency. Therefore, in the test of a changing environment, small businesses prove to be the fittest form of an organization (Hu, 2003b).

There are many indications or sources of the resilience inherent in SME sector. For example, Van Dijk (1995, p.21) defines 'flexibility' in an industrial context as "the ability to shift promptly from one process and/or product configuration to another and to adjust quantities of output rapidly up or down

over the short run." One possible display of such 'flexibility' is firm's ability to change its factor intensity rapidly when the relative factor price is changing. The labor-intensive SMEs do usually elbow easier than their capital-intensive larger counterparts to change their factor intensity in a wage-increasing environment.

SMEs have often been categorized as production units quick to respond with outside change. This specialty is what we generally call 'adaptability', reflecting another source of flexibility. In the study of organizational behavior, adaptability concerns the organization-environment interface, and the achievement of fit between the organization and its ecological niche (Stoica and Schindehutte, 1999). The terms including adaptability, flexibility, and responsiveness have been used to describe the ways firms adjust themselves to the changing environment. Empirical evidences based on experiences across many economies demonstrate small firms are more flexible than large firms (Mills and Schumann, 1985; Acs, Audretsch and Carlsson, 1991; Das, Chappell and Shughart, 1993; Schive and Hu, 2001). According to Aiginger, Mueller, and Weiss (1998), in the field of industrial organization, scholars of the nineties had held the consensus that small firms were more flexible in adapting to an exogenous shock.

NETWORKING

The concept of network is not a modern invention. Marshall (1890) long before pointed out, that "the advantages of production at a large scale can be as well attained by the aggregation of a large number of small masters into the district as by the erection of a few large works". There are different names designated to such relationship. It reflects a network of firms of all sizes cooperated in many forms (vertically or horizontally) in the economy (Chang and Hu, 1999). It can be built on an abstract relationship. For example, Lovett, Simmons and Kali (1999) identify certain kind of Guanxi-type network that rooted from ancient Chinese traditions that are based on personal relationships (a specialty for SMEs). The scholars preach the advantages of such Guanxi networks: that they transmit information more effectively, they are more flexible, and they adapt more quickly to changing circumstances, and reduce transaction costs.

There are also substantial network relationships. For example, the subcontract system connects small firms with their larger counterparts. In the core-satellite system, SMEs and the center firms interact in a form of vertical disintegration. People also call the relationship found in Japanese 'supplier-group system' (Howard, 1990). Japanese SMEs are thus subordinate firms of large firms in the core-satellite system. According to Kim (2007), Korean SMEs have also acted as sub-contractors of large enterprises. It is also well recorded that there is a well-developed subcontract system in Chinese Taipei (Hu and Schive, 1996). Although it seemed that in such relationship, the well-being of SMEs depends on their subcontractors, SMEs may still act independently. In Chinese Taipei, subcontract system that develops by backward and/or forward integration among related firms builds a healthy self-governing SME sector.

Strategic alliances formed by firms of same interest constitute a different kind of network. Since in most industrialized economies there is competition policy that bans collusion among large firms, strategic alliances are usually accepted among SMEs as a mean to overcome their scale limitation when the advantage of mass production or financial economies of scale appeared. This is important when innovation is a major policy concern, the R&D strategic alliances can be formed to beat barriers of scale economies found in many innovative activities. Many successful experiences are found under certain public-private supporting systems that help link SMEs and innovative institution to form strategic alliances. The public-private cooperation itself is also a network.

When we add in the geographic substance, the relationship further materializes as industrial district, agglomeration or cluster. The traditional concept of 'industrial districts' later has been defined as "productive systems characterized by a large number of firms that are involved at various stages and in various ways, in the production of a homogeneous product".¹ Porter (1998) later defines clusters as critical masses - in one place - of unusual competitive success in particular fields. In their survey article, Fan and Scott (2003) explore the issue of industrial agglomeration and its relationship to economic development and growth in the less-developed countries of East Asia. They provide evidence of a positive relationship between agglomeration and economic performance.

When we further add in technology as an ingredient, the clusters or industrial districts transform into the concept of high-tech 'Science Park'. The Silicon Valley of the U.S. can be seen as a successful example that aimed particularly at manufacturing high-technology products. Similar high-tech clusters are found in many member economies as well. Science Park takes the advantage of network density producing a perfect environment allowing R&D or knowledge spillovers among neighboring firms (Audretsch, 2003; Meagher and Rogers, 2004; Fosfuri and Ronde, 2004). Howard (1990) takes Silicon Valley as a successful example of the network relationship, preaches that government should provide regional institutions as glue of the SME network. The public-private cooperation is thus given new meanings in the profile.

ENTREPRENEURSHIP

Entrepreneurship and small businesses are often considered to be overlapped concepts (Thurik and Wennekers, 2004). There are many definitions of an entrepreneur, and even more of the concept of entrepreneurship. Entrepreneurship can range from merely the creation of new enterprises (Low, 2001) to the eagerness to deploy resources in the pursuit of an opportunity that is independent of the origin or ownership of such resources (Johannisson, 1998). In highlighting personal characteristics, Hebert and Link (1989) have defined the entrepreneur as someone who specializes in taking responsibility for and making judgmental decisions that affect the location, the form and the use of goods, resources or institutions.

There is typically one entrepreneur in each firm, despite the size of the firm. In other words, no matter how large the capital scale a firm employs, what really count is the way people handle the capital. In almost all economies, there are more than ninety out of one hundred enterprises that belong to SMEs, and in places like Japan and Chinese Taipei, the corresponding figure of the number of SMEs out of one hundred enterprise amounts to ninety-five (Hu and Schive, 1998). Therefore, most of the entrepreneurship resource in the economies is found in the SME sector. Small businesses are vehicles for entrepreneurship.

The enterprising behavior inherited in the SME sector helps shaping the foundation of a wealthy nation in a stable environment. This is what Adam

Smith (1776) has described with his doctrine of invisible hand, where:

"Every individual endeavors to employ his capital so that its produce may be of greatest value. He generally neither intends to promote the public interest, nor knows how much he is promoting it. He intends only his own security, only his own gain. And he is in this led by an invisible hand to promote an end which was no part of his intention. By pursuing his own interest he frequently promotes that of society more effectually than when he really intends to promote it."

In a survey article, Wennekers and Thurik (1999) review the East Asian miracle as a historical evidence that links entrepreneurship and economic growth. In a more modernized context, as an economy transformation into a knowledge-based one, entrepreneurship draws special attentions in the world. The economy is put in a more dynamite, versatile setting under such regime. Since one feature of the knowledge-based economy is a high degree of people starting new firms to pursue, explore or carry out new ideas, Audretsch and Thurik (2000) thus synthesize knowledge-based economy with entrepreneurial economy. They point out that the developed economies are undergoing a fundamental shift away from a managed economy and toward an entrepreneurial economy. They further emphasize the innovative role of entrepreneurs, granting entrepreneurship a key to successive creation of knowledge that leads the economy to further development. Acs, Carlsson, and Karlsson (1999, p.12) also consider that "small firms and entrepreneurship are both necessary for long-run macroeconomic prosperity" in the new century.

SME Policies of the Selective Economies

This section aims to review the SMEs development and the relating policy of the selective economies. Brief comments are also made in summarizing each contributing studies.

AUSTRALIA

Australian SMEs enjoy a friendly environment, and have already play

important role in the global market. The entrepreneurship resources that have been brought in by immigrants are well noticed. Low transaction cost allows Australian entrants to set up a business in two days (Braun, 2007). The self-reliance culture found in the economy may be good for independence and individually orientation that many considered to fit in the entrepreneurial profile (Beugelsdijk and Noorderhaven, 2005). However, for established SMEs, the pervasive culture of 'going it alone' may hinder the future development.

Australian SME policy aims to create an enabling environment for SME development. After the release of Committed to Small Business statement in 2004, several programs are initiated, such as tax cut, providing venture capital, and supporting R&D. The main focuses of these programs are on the information and communication (IC) industries. Australian SME policies are designed to boost innovation, improve efficiency, and increase international competitiveness. Programs built upon public-private partnerships have proved to be successful. The Cooperative Research Centres (CRC) Program established in 1990 is said to become a global role model for collaboration between business, academia and governments. Furthermore, innovation, technological development, and job creation will be the focus for future SME policy design in Australian.

CANADA

Canadians have noticed the increasing importance of SMEs, and yet, most policies or programs are not designed specifically for SMEs. The last policy statement addressing SMEs on the federal scale was dated 1994. Since then, only specific agendas consider mainly the mature SMEs with designated purpose. Most recently, three major concerns that relating to SME development are found in Budget 2007, they are taxation, the paper burden, and the access to finance (Lever, 2007).

Canadians notice that a disproportionate cost burden of red tape (paperwork burden) put upon SMEs compared with larger firms. The Paperwork Burden Reduction Initiative (PBRI) launched in 2005 was designed in great detail to reduce, rationalize and simplify regulatory requirements by the government. These and other emphasis help create a climate conducive to doing business,

and thriving entrepreneurship. The special financing programs combine with innovation supports and consulting service, as well as venture capital produce a righteous environment for start-ups and small businesses.

Several beneficial factors boost the future prospect of entrepreneurship in Canada. The culture of independence and family value creates a fairly high self-employment rate. New Canadians (immigrants) also bring in entrepreneurial energy. The aging baby boomer becomes a source of entrepreneurship (seniorpreneurs) is also a novel idea for mature economies. One important policy prospect is to build supportive system to allow the potential entrepreneurial resources (women, young, and new Canadian) easy access to education, training program that help nurture, successful entrepreneurs.

However, being a resource based economy in the past signifies special challenges for Canada to further develop the manufacturing and service sectors, which can go hand in hand with the flourishing SME sector. One important learning idea for policy maker is to recognize that small, new firms, as well as large, mature firms are all important for creating a healthy production system (Marshall, 1890; Acs et al., 1999). Furthermore, the high exit and entry rate of SMEs may signify a risky sector, and it also demonstrates a high competitive business environment that adapts quickly in the knowledge based environment.

CHILE

The lack of an adequate SME promoting policy design is noticed in Chile. Therefore, there is long way to go for Chilean micro, small and medium enterprises (MISMEs). The under development of MISMEs may hamper the achievement of some economic goals. For example, one of the major challenges for Chile is the deficient income distribution, as this is coupled with the insufficient development of the SME partly due to decades of policy biased against SME. The political culture makes situation even worse for not being able to recognize the importance of MISMEs (Riveros and Morales, 2007).

This is one of the major obstacles for Chilean MISMEs. It is evidenced SMEs perform better when competing in a less distorted on-line system. Experience

drew from other economies also indicates a less biased industrial policy may be the best that SMEs can expect (Hu and Schive, 1998). A business environment with more transparency, and less discrimination is just the medicine for the Chilean SMEs to rise from the rural beginnings.

It is also important to recognize MISMEs represent various business entities. For the purpose of boosting regional development, MISMEs may act as job-creators. There are also entrepreneurial MISMEs that are suitable for enhancing export competitiveness of the economy. For these SMEs, the future policy prospect may focus on three general aspects: helping MISMEs to have fair access to financing, training, technology and innovation.

Furthermore, for an economy used to export intensive in natural resources, like Chile, to distribute economic activities among firms of different sizes is important to maintain international competitiveness. Under the circumstance, a sub-contract system bridges large firms and SMEs may be an answer.

COLOMBIA

Colombians notice the structural inadequacies of economic activities dominated by large firms. Therefore, a well structured Law 590 and the Law 905 were promulgated in 2000 and 2004, respectively. These Laws that aim at SMEs promotion and development have created a friendly climate for SMEs in Colombia. Although the Colombian SME sector is still far from a modernized sector when measured in the degree of internationalization, the consensus that SMEs are engine of the economy helps form a beneficial environment for SME development (Acosta and Rojas, 2007).

The Law 590, Law 905 and the other rules, programs and strategies in the consecutive years cover all major concerns of SME development that are found in other economies. Colombian government also notices the importance of institutional synergy in supporting SMEs. Colombia also sets up a prize to encourage elite SMEs in technological and managerial innovation (Prize INNOVA). Similar devises can be found in other member economies, for example, there is an annual prize for best-performed SME owners in Chinese Taipei. For small business owners, it is glamorous to be named as role models to their peers. This provides a motivation that triggers

SMEs' continuous pursuing for success.

Apart from the usual practice, there is special interest in the cross border integration of SMEs. The policy intends to build network relationships with neighboring economies and the Pacific Basin. These and other measures that focus on issues about globalization, competitiveness of SMEs demonstrate integration into world economy and are Colombian policy goals. Although these projects have been carried out for a short period of time, some successful results have been noticed. For example, the sharp increase in the number of exporters and the figures of export sales are recorded under the Proexport program.

JAPAN

Japan is always known for having a large SME sector. The SME Basic Law was enacted as early as 1963. However, under the hierarchical business structure of the economy, Japanese SMEs used to play passive, supportive roles to large firms. They were thus considered the vulnerable entities. The 1999 SME Basic Law amendment finally changed the perspective. It was only recently, SMEs in Japan were recognized as an important player in the economy.

The major SME-related Laws since 1999 cover both protective and supportive approaches for SME development, the former targets disadvantaged SMEs, and the latter targets ambitious enterprises. Still, many of the political resources are concentrated on the elite SMEs (world-class SMEs), for example, creating local branding, formation of cluster, and other supportive measures. The Nagoya City experience (with Industry Revitalization Plan launched 2005) and the One Village One Product Movement (advocated since 1979) are both brilliant designs with fruitful results. Policies that target on the development of SMEs in remote and rural areas are also introduced in Japan (Yoshimura and Kato, 2007).

Even though the current SME-related Laws have changed perspective about Japanese SMEs, most policy measures are put in the regional horizon. It is true that SMEs can boost local economic development. Still, the potential of SMEs being an important international market player, and the entrepreneurial

resource largely endowed in SME sector are worth to be explored.

KOREA

Korean SME policy is experiencing a change from traditional protectionist to an enabling one. SME act was first promulgated in 1966. However, under the backdrop of hostile industrial policy toward SMEs in the postwar era, it is well received that the distorted policy design restricted the development of Korean SME sector and hindered the foundation of Korean economy toward later prosperity (Chon, 1996). This may also explain the inherent deficiencies of traditional Korean SMEs in comparison to some other economies.

The inauguration of World Trade Organization (WTO) in 1995 marked the obvious shift of the policy focus, SMEs have since aimed to transform into an innovative entities equipped with competitiveness needed in the global arena. A system of policy measures is structured to create a very sophisticated SME policy paradigm in modern Korea. The certification of innovative SMEs is one example that demonstrates the ambition of Korean government in adjusting her SME policy to create an elite SME sector (Kim, 2007).

SME sector includes firms with high degree of heterogeneity. Some successful SMEs graduate into to large firms. However, a majority of SMEs that comprise the foundation of the entire SME sector may never become innovators. Therefore, it is impractical to expect every SME can grow into innovative one. There are ample of examples that SMEs can be a born global firm as well as a born innovative firm, for these firms, no transformation is needed. It is the entrepreneurial talent that needs to be explored. Apart from being the innovators, SMEs play many different roles in the economy. The overall performance of the SME sector and the effectiveness of the SME policy still need to be carefully evaluated in Korea.

NEW ZEALAND

New Zealand established the Small Business Agency (SBA) in 1976 to help small firms grow. Recent statistics show that the SME sector dominates the New Zealand economy (Massey and Ingley, 2007). The fast growth self-employed rate of Asian New Zealanders is also reported in the statistics.

In order to transform from an economy that depends largely on agricultural sector towards a knowledge-based one, New Zealand has experienced a policy changed toward liberalization and deregulation since 1980s (Hamilton and Dana, 2003). Under the non-interventionist philosophy, since 1986, the SME policy in New Zealand minimizes government intervention, allows SMEs to compete on their own. The policy emphasis instead is now on providing fair environment and suitable infrastructure.

In view of the globalization of the economy, New Zealand government launched the economic transformation agenda in 2006. A more aggressive policy measure is set up to boost productivity, export, innovation, and internationalization. As an economy with abundant resources, the true challenge for the policy designer may be the special national trait of lacking the motivation for growth. Since self-employed entrepreneurs are often ambitious, they may be immune from such national trait. SMEs thus become the ideal means for New Zealand government to reach designated policy goal.

SINGAPORE

It was not until 1986 that the contribution of SME sector to Singapore economy was finally recognized. Since then, the job creation and entrepreneurial sourcing functions of SME sector are both appreciated by Singapore. Here after, we find policies designed specifically for SMEs.

There are two SME master plans in Singapore, published in 1989 and 2001. In 1989, the first master plan issued to focus on the general issue about strategies for SME growth. After a decade, the policy was evaluated, and then made adjustment accordingly. In 2000, poor productivity performances of SMEs were reported. Several obstacles were noted, for example, weak entrepreneurial culture, and hassle of red tape and bureaucracy. In 2001, the second SMEs master plan was published to groom innovative high-growth SMEs, develop productive SME sector, and to create a knowledge-based, pro-enterprise environment (Liang, 2007).

Some special Singaporean experiences may provide lesson for other economies. For example, in contrast to traditional infrastructure, the entrepreneurship infrastructure building has been paid with special attention in

Singapore. It has been noticed in Singapore that there are many SMEs that are not aware of the policy measures or have no initiative to resort to public help. Singapore also calls for setting up a SME agency with higher political profile and role to gather resources and fulfill policy goals.

CHINESE TAIPEI

It has been well received that Chinese Taipei's economy has grown largely as a result of international business in which SMEs have been heavily involved (Fuller, 2003). Although the Rule for Promotion of SMEs was promulgated in 1967, and there were many subsequent measures aimed at promoting SMEs, no definite evidence to prove the effectiveness of these policies (Hu and Schive, 1998). Ronnas et al. (1998) have conducted an in-depth analysis of the Asian experience of small business and have acknowledged that Chinese Taipei is a classical success story, in which the government has played anything but a passive role.

Since 2000, Chinese Taipei has made an obvious change in her SME policy. Apart from providing guidance for SMEs, SME policy gradually shifted to a much active role in improving the business environment for SMEs (Chao, 2007). The policy change has been partly triggered by the requirement of the emerging knowledge based economy. Since then, many mature and sophisticated policy layouts have been designed to upgrade the SME sector in Chinese Taipei.

SME sector is a heterogeneous production sector. In order to achieve the desire goal of the policy measure, it is important to learn first the intrinsic characteristics or essence of the targeted SMEs. SMEs in Chinese Taipei have long participated actively in the international arena. Their adaptabilities to the fast changing global market decide their future.

VIETNAM

Modern Vietnamese private sector was relatively young in comparison to other economies, as it was formed in 1991. Vietnamese SME sector had developed in a hostile environment until 2000, when the New Enterprise Law took effect. Soon after, in 2003, SME Development Promotion Council was

organized. The job-creation and export potential of SMEs are exploited under the SME-related policy (Do and Pham, 2007).

Although there are still obstacles, Vietnamese SME sector is experiencing a speedy development. Drawing inference from the SME developing experience of other economies, the urgent challenge for Vietnam may well be the creation of a stable macroeconomic environment combined with an open and freer market in terms of low entry barriers and transaction costs (Hu and Schive, 1998). For example, free information is an important segment of market mechanism, as well as infrastructure in knowledge based economy. In a survey, information access is shown to be important for Vietnamese enterprises.

The accession to WTO in 2006 marked a new phase for Vietnamese economic development. New focus was added in the SME policy. Vietnamese SME sector has to be able to mature quickly, so as to enhance managerial and innovative ability as well as competitiveness to help with fulfilling its designated socio- economic goals.

The SME Policy Outlook

After reviewing the findings of each study, in this section, we will compare and draw inferences from the member economies' experiences. The various policy objectives, institutional backdrop, and the dual nature of entrepreneurship will be our main focus.

VARIOUS POLICY OBJECTIVES

The economies that participate in the project demonstrate the policy environment for the development of SMEs, are with varied degree of economic development. For example, we have well-advanced economies such as Canada, Japan, Australia, New Zealand and Singapore at one end, newly-developed economies of Korea and Chinese Taipei in the middle, and Columbia, Chile, and Vietnam as shining new stars at the other end.

Since the economic status varies, we find that each economy has policy design or concern differently in planning their SME policies. Basically, the most urgent problem facing rural economies is unemployment, so that job generation is the policy concern. While for developing economies, how to catch up with mature economies, adaptation to globalized environment, and industrial upgrade are the policy objectives. For those well-developed economies, maintaining their competitiveness, creating a vibrant environment to nurture entrepreneurship, and building a sound knowledge based economy are more of their concern.

Of course, each economy also faces its distinct problem and special policy interest. These considerations form the background for each participating economy when designing their SME policies. We can roughly categorize three SME policy objectives in these studies. First, we find that in Canada, Australia, New Zealand, and Chinese Taipei, the major focus of the SME policy is to stimulate R&D ability, innovation, and entrepreneurship. Then, there are also economies that address the issue about job creation, for example, Vietnam, Colombia, Singapore, Korea, and Chile. Finally, Colombia, Singapore, Korea, and Japan put their policy efforts on sub-contractor system. Japanese SME experience in the area of regional development proved to be a successful example of an ingenious policy design.

Many policies aim at clearing hurdle for SMEs. If we concentrate on the obstacles that SMEs confront, each economy shares some common experiences. The major concerns of SME sector include sources of funding, managerial ability, quality of human capital (employee training), and so on. These are emphasized in almost all economies' studies.

There are also problems confronting policy makers which are unique to certain economies. For example, reducing bureaucratic red tape that hinders enterprising behavior is emphasized as the highlighted policy for Canada, New Zealand and Singapore. Although Chinese Taipei has long been famous for her SME environment, an amendment in the Corporate Law to facilitate SMEs (improving business environment) was launched only recently, in 2000. On the other hand, an Australian new comer can set up a firm within two days and this creates an ideal example for other economies to follow.

Apart from the differences in economic status, the inherent endowments of these economies are different too. For example, Australia, Canada, Chile, and New Zealand all have abundant natural resources that have long born impacts on their economic focuses, and also entailed different policy angles.

INSTITUTIONAL BACKDROP

It is emphasized that economic development requires not only physical and human capital formation, but also institutional support (Assane and Grammy, 2003). Due to the institutional and cultural differences, different economies may conceive SMEs differently. These perceptions affect the design as well as the successfulness of SME policies. Take the time when the first SME-related policy published in each economy for example, back in 1960s, Japan, Chinese Taipei, Korea, Columbia all had their first SME policy launched. New Zealand set up Small Business Agency (SBA) in 1976. Other economies have their policy focus on SMEs in much later date. Even though the starting points are different, the late developers can often learn from early experiences, their policy contents may be equally sophisticated.

The policy concern often reflects or interacts with the underlining culture or other institutional frameworks. Take Chinese Taipei for example, the Rule for Promotion of SMEs was first promulgated in 1967. In 1997, under the growing consensus about the achievement made by SME sector, the SME Protection Clause was put in the Amendment of Constitution. The result demonstrates a general consensus, which help creates a culture of identification as well as a friendly environment for SMEs in Chinese Taipei. This is also a valuable asset promising the SMEs' further prosperity in the island.

Culture and other institutional factors that affect SMEs as well as policy are also depicted in other economies. It is noticed that in northern Vietnam, a relatively conservative cultural surrounding may make it a challenge for building a knowledge based economy in comparison to southern Vietnam. In Korea and Chile, SME used to symbolize backwardness and a sector lacking competitiveness, this invites difficulty for policy aim to promote SMEs. It is also noted that Chilean passive culture may demand a stronger policy initiative to make it possible for a more autonomous SME sector. Singapore

admits a weak entrepreneurship culture, which is not a proper environment to nurture entrepreneurship as well as SMEs. For practice oriented New Zealanders, innovation is not a well received concept. Furthermore, it is said that economies with abundance resources that are not used to the idea of pursuing growth by innovation instead of resources, may build a culture that is fruitless for entrepreneurial development. This may also explain why New Zealanders lack the motivation for growth.

On the other hand, many economies enjoy the imported entrepreneurial resources that are brought in by new immigrants. Both Canada and New Zealand notice the high self-employment rate of the new nationals. In a globalized world, speedy movement of human capital via immigration may help to change culture disadvantage, so as to develop entrepreneurship.

Nowadays, not just immigrants, SMEs as a production entity also move across border. For example, SMEs in Chinese Taipei are known for their capabilities of diversifying their activities abroad through export (Aw and Batra, 1998; Schive and Hu, 2001). When enterprises need to adjust their organization to adapt to a changing environment, two strategies they often adopt are diversification and/or foreign direct investment (FDI). In Chinese Taipei, it was SMEs rather than large firms that were the first to embrace such choices back in the mid-1980s (Schive, 1995). Since many SMEs in the island have resorted to outward FDI, the recent decline in SMEs' share may require a broader examination to read the true message. People should also note that there might be concurring trends in macro-economy and SMEs' performance. Therefore, the worry with the latest decline of SMEs' share in Chinese Taipei may be pre-matured. This is also a lesson worth noticing when making policy judgment in a growing globalized world.

THE DUAL NATURE OF ENTREPRENEURS

So far, we have been looking at SME sector as a whole, however, not all families of SMEs are performing alike; there is alienation within the SME sector. For example, there are micro-enterprises as well as larger SMEs. We can find SMEs in traditional sectors as well as in high-tech industries. Some SMEs confine their operations domestically while others engage in global activities. These are all typical SMEs that can be found in almost any given

economy. It is dangerous to treat all SMEs alike when making policy decisions. We find several economies set up different strategic measures targeting specific SMEs for achieving diverse policy goals.

By the same token, not all entrepreneurs are the same. Furthermore, the role of entrepreneurial activity differs empirically across the stages of economic development (Sternberg and Wennekers, 2005). In the new economic era that features speedy advancement in technology, entrepreneurship has become one important element of production. The two well-received features of entrepreneurship are new entry or start-ups, and innovators or newness. The latter clearly is closer to the entrepreneurship concept raised by Schumpeter that relates technological progress to continuous prosperity of an economy. Many define entrepreneurs with such quality of 'real' entrepreneurs.

The self-employed population may include a majority of managerial business owners, a group which is generally excluded from the category of Schumpeterian 'real entrepreneurs' (Wennekers and Thurik, 1999), largely because during a business downturn, discouraged members of the population who have become newly unemployed may suddenly find themselves forced to be their own bosses. In fact, it is well documented that individuals may be pushed into own-account status by the lack of work opportunities (Earle and Sakova, 2000).

In such a case, it is the business downturn itself that causes the increase in self-employment, with such reluctant self-employed people actually exhibiting very little entrepreneurial potential. Therefore, some mixed signals are expected when using the self-employment rate or the new entry as proxies for entrepreneurship capital in any empirical studies.

Indeed, the Global Entrepreneurship Monitor (GEM) research found clearly that there are two main reasons why people set up their own businesses: opportunity and necessity (Sternberg and Wennekers, 2005). The former motivation demonstrates the well received Schumpeterian 'real entrepreneurs' concept. It is this kind of self-employed behavior that stimulates innovation. While the latter, when people become self-employed out of necessity, they perform little entrepreneurial function.

Under the backdrop, an important lesson to learn is that when SME policy targets on boosting innovative entrepreneurship, it may work better via instrument, such as incubating system, venture capital, R&D related funding, public-private cooperation, and so on. The policy aims at assisting entry may only fulfill the goal of maintaining a competitive market environment. And the special programs that help facilitating self-employment are essential when the social-economic goals are kept in mind, such as a low unemployment rate, an undistorted income distribution, and in the interest of taking care of the disadvantage group.

Conclusion

SMEs provide jobs, act as competitors, inject resilience, constitute network, incubate entrepreneurship and fuel technological change. This analysis has shown these main features of SMEs, as they are the cornerstones that help us understand SMEs, and provide blueprint in designing SME policy.

Multi- facet SMEs help fulfill social-economic goals. The contributing studies to this analysis have offered an opportunity for us to learn experiences of SMEs and SME policy development of different economies. If we trace the path of policy adjustment in each economy, we realize that the fast changing global environment is the main force behind the policy redesign. The time when an economy joins WTO often marks the turning point when the economy starts to establish or enlarge its knowledge based or entrepreneurial sector. When exposed under the international markets, the competition pressure inevitably forces an economy to mature. However, most economies comprise knowledge based and resource based traditional sector at the same time. SMEs and entrepreneurship incubated within can be the engine or fuel in both sectors. Therefore, policy makers should bear in mind to properly split policy resources among both sectors. Apart from policy transformation, parallel policies that promote both traditional and entrepreneurial sectors should also be considered.

Furthermore, regional economic integration is another trend that affects global economic environment. Regional integration contributes to cross border

cooperation, experience and knowledge sharing, and growth. The current project is an example of collaboration. When the research results are put together, we find common ideas as well as dissimilar experiences. It is hoped that from the mutual learning process, coherence will be formed. This would enhance our knowledge and policy performance. For example, there exists the suggestion to generate policy guidelines towards best practice in SME development across the Asia-Pacific region. It is hoped that the efforts will realize the pursuit of welfare and growth for economies.

Similarly, the European expert group for SME policy research organized by European Commission had held their first meeting in June 2007. One of the main objectives of the European expert group of SME policy research is to bridge the gap between SME research and policy-making. This is thus also an example of the public-private collaboration or networking in a larger scale. Economies should consider making current project a regular association to provide analogous function. It is important that through the public-private cooperation, a platform is established to facilitate the communication among government, industry, and research institute.

Finally, there are controversies about whether experiences in one economy can be effectively transferred to other economies. It is believed that cultural and institutional factors make many differences regarding the transferability of successful experience. The economies' studies provide interweaving evidences about culture and institutional background. It is important to learn experiences from other economies with similar culture or institutional backdrop when making policy decision. It is also important to understand the policy goals and the policy takers. Further, different institutional frameworks, traditions and legal frameworks have been developed around the world. Therefore, before engaging in any redesign or adjustment of the existing SME policies, it would be prudent for policy makers to clearly understand the underlining development of their SMEs, the institutional and culture background, and fellow economies' experiences. Under the circumstances, with carefully chosen and evaluated policies, a healthy and trusty SME sector that helps achieve social-economic goals may be expected.

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Notes

1. This definition was made in 1995, by the International Institute of Labour Studies in Geneva.



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