Chapter 2 – Literature Review

2.1 Concepts of Small and Medium Enterprises

Small and Medium Enterprises (SMEs) have long played an important role in the economic development of many countries (Beck et al., 2005). There have been changes in rivalries in the global market and economy drove SMEs to adapt themselves to the new management paradigm where cost reduction becomes an important strategy. Companies that are capable of utilizing strategy, knowledge and shift their businesses into a new market will survive (Glenn, 2009). The study of Young and Molina (2003) has shown that one way for SMEs to survive in today's unsteady business environment is to form strategic alliances or merge with other similar or complementary business companies. When compared with larger businesses, SMEs' contribution to output tends to be lower per firm because they tend to be more labour intensive than larger firms and concentrated in service sectors. They therefore typically achieve lower levels of productivity, though they do contribute significantly to employment (Wymenga et al. 2011).

SMEs can in fact become the engines that sustain growth for long-term development in developing countries. When growth becomes stronger, SMEs gradually assume a key role in industrial development and restructuring. They can satisfy the increasing local demand for services, which allows increasing specialisation, and furthermore support larger enterprises with services and inputs (Fjose et al. 2010).

2.2 SMEs and Employment

As noted, SMEs tend to be more labour intensive and at a macro level, therefore, provide a substantial contribution to employment. A World Bank survey of 47,745 businesses across 99 countries revealed that firms with between 5 and 250 employees accounted for 67% of the total permanent, full-time employment (Ayyagari et al. 2011). SMEs were also creating more jobs than large enterprises. Between 2002 and 2010, on average, 85% of total employment growth was attributable to SMEs (de Kok et al. 2011).

Myanmar's transition to a market-based economy is accompanied by rapid development of the private manufacturing sector, which has large potential for improving economic growth. The overall success of the sector, however, should not be taken for granted. Future advances will greatly depend on the policy and business environment in which manufacturing activities take place. It is, therefore, important to better understand the business environment and help inform policies conducive to sustainable economic growth.

The Central Statistical Organisation (CSO) of the Ministry of Planning and Finance of Myanmar, the United Nations University World Institute for Development Economics Research (UNU-WIDER), and the University of Copenhagen, supported financially by Denmark, have initiated the project 'Towards Inclusive Development in Myanmar'. The project aims to strengthen evidence-based policy-making and analysis through a rigorous 'Myanmar Micro, Small, and Medium Enterprise Survey' of private manufacturing enterprises.

Manufacturing activity in Myanmar follows the topographical circumstances of the country. Most of economic activity is concentrated in the central lowland strip down to the coast in the south. The foundation of the sector is the food industry, accompanied by textiles and apparel in the centre, wood in the north, and non-metallic mineral products in the south. These sectors, however, have limited growth potential as they are generally the least innovative and rely on low levels of technology.

Enterprises appear to be taking advantage of agglomeration benefits in the form of industrial zones and clusters, but the infrastructure conditions could be improved. Not all firms have access to electricity and public water and 80 per cent, respectively, are without access), and only 5 per cent of firms have access to the internet.

The regulatory environment is complex and dispersed among several institutions, which results in noncompliance in different areas of enterprise activity. While the rate of formalization defined as obtaining a licence or registration with any government authority is high (81 per cent), the rate of registration with the Directorate of Investment and Company Administration, expected to be the only institution responsible for the registration of enterprises, is very low (3.5 per cent). The adherence to tax regulation appears to be weak, as only one-third of enterprises pay the corporate income tax. A comparison of wage and productivity levels of informal firms indicates their lower performance compared to formal firms.

Technology-wise, enterprises in Myanmar tend to rely on hand tools and old, second-hand machinery. Fewer than 20 per cent of the enterprises have acquired technology through imports. This suggests that financial constraints are high and that direct contact with the producers of technology is limited, which may negatively affect productivity through limited knowledge transfer. Enterprises tend to specialize in producing a single product. The innovation rates are low, both in terms of introducing new products (3 per cent) and improving the existing ones (12 per cent). Certification based on international standards, which could facilitate market access, is very low as well, the exception being a handful of larger firms.

2.3 Myanmar and SMEs

SMEs in Myanmar account for 50-95 percent of employment, and contribute 30-53 percent of the country's GDP. According to the Small and Medium-Sized Enterprises (SME) Development Bill (SME Bill), which was launched in January 2014, "small enterprises" are defined as those with K50 to K500 million in capital, or with 30-300 employees. “Medium-size” firms are defined as those with K50 million to K 1 billion in capital, or with 60-600 employees. As a result, 99.4 percent of business in Myanmar are approximately classified as SMEs, and there are now 50,694 SMEs altogether in the regions and states on Union territory.

In Myanmar, SMEs are considered important to the national economy. They create a lot of job opportunities for the population and contribute to employment and income generation, resource utilization, and promotion of investment. For this reason, the Myanmar government is trying to give special attention to the development of SMEs and provide support for existing SMEs to become larger industries. SMEs cannot be ignored, as they make up 99 percent of Myanmar’s firms.

2.4 Myanmar SMEs Development

Myanmar’s business environment is undergoing a lot of rapid changes. However, SMEs in Myanmar face many challenges during the period of political and economic transition. New trends have to be taken into account continuously, such as growing demand and customers’ expectations on flawless products and services. Moreover, SMEs are facing increasing global competition, the emergence of new technologies and impact on integrated supply chain and production systems among ASEAN member states. In Myanmar, challenges to SMEs are varied and complex, depending on the sector and level of development. Common challenges include financial access, human resource development, R&D in technology, management, and marketing.

In conclusion, the development of SMEs is important for the country’s economic development, as they are major contributors to the economy and job creation. However, SMEs are confronted with numerous challenges, including insufficient financial support, electric power supply and credit guarantee. Given that SMEs form the backbone of the country’s economy, economists have called on the government to improve the banking sector, and encourage banks to provide more loans to SMEs at a reasonable interest rate.

2,.5 Myanmar Government Prioritizes the Development of SMEs

The Myanmar government is making efforts to transform the political, economic and social environment to be in line with global changes, and to promote sustainable economic growth. This includes promoting small and medium-sized enterprises (SMEs), which play a pivotal role in the economic development of both developing and developed countries.

Myanmar has a vision to develop SMEs, based on the policy to create regionally innovative and competitive SMEs across all sectors, to stimulate income generation, and contribute to socio-economic development. Various studies estimate that SMEs in Myanmar account for 50-95 percent of employment, and contribute 30-53 percent of the country's GDP. According to the Small and Medium-Sized Enterprises (SME) Development Bill (SME Bill), which was launched in January 2014, "small enterprises" are defined as those with K50 to K500 million in capital, or with 30-300 employees. "Medium-size" firms are defined as those with K50 million to K 1 billion in capital, or with 60-600 employees. As a result, 99.4 percent of business in Myanmar are approximately classified as SMEs, and there are now 50,694 SMEs altogether in the regions and states on Union territory. In Myanmar, SMEs are considered important to the national economy. They create a lot of job opportunities for the population and contribute to employment and income generation, resource utilization, and promotion of investment. For this reason, the Myanmar government has given special attention to the development of SMEs, support for existing SMEs to become larger industries, and creating a conducive business environment for SMEs. The SME Development Central Committee's Joint Chairperson, State Counsellor Daw Aung San Suu Kyi, stated at one committee meeting that SMEs cannot be ignored, as they make up 99 percent of Myanmar's economic force. With regard to SMEs, the government has prioritized human resource development, support for technical development and innovation, capital funding, better infrastructure, gaining a foothold in the marketplace, reasonable taxes and regulations, and the creation of suitable businesses. A new policy to promote the development of SMEs includes tax relief and tax exemptions, since SMEs in Myanmar suffer from arduous tax and monetary policies. They also suffer from lack of access to capital and protection of intellectual property, as well as high interest rates, and lack of close relations with Myanmar banks. However, on 1 August 2017, the State Counsellor met with the Chair of 22 Myanmar banks in Nay Pyi Taw, and urged them to cooperate with the government in promoting Myanmar's economic growth. SMEs and businessmen hope that this meeting will benefit SMEs and the business sector.

Financial Support for SMEs: The Myanmar government provides only non-financial assistance to business enterprises, due to limitations on the government budget. However, thanks to the Financial Support for SMEs policy, the Myanmar Economic Bank (MEB), Myanmar Investment & Commercial Bank (MICB) and Myanmar Industrial Development Bank (MIDB) have provided loans to SMEs since 2004. The state-owned Myanmar Agriculture Development Bank has also provided loans to farmers throughout the country. At the same time, banks are trying to reduce the interest rate on loans in order to contribute to national economic development. They have proposed that interest rates be reduced from 17 percent to 15 percent. Banks and the Ministry of Agriculture are also working together to provide financial support towards the development of rural areas and rural livelihoods. For example, state-owned Myanmar Agriculture Development Bank has provided small loans to farmers, the fishery sector and rubber plantations. In addition, the Japan International Cooperation Agency (JICA) will provide a K 15 billion loan through the government to develop SMEs in 2017 at a low interest rate. The loan is granted through the Myanmar Economic Bank (MEB), and SMEs and businessmen who apply for the loan are required to submit their current business situation and future program of their businesses to the SMEs Development Department. Nevertheless, despite the increasing provision of loans, the lack of financial access and high tax rates still restrict the development of SMEs in Myanmar.

SMEs Development

Myanmar's business environment is undergoing a lot of rapid changes. However, SMEs in Myanmar face many challenges during the period of political and economic transition. New trends have to be taken into account continuously, such as growing demand and customers' expectations on flawless products and services. Moreover, SMEs are facing increasing global competition, the emergence of new technologies and impact on integrated supply chain and production systems among ASEAN member states.

2.6 Export Barriers

Recent economic slowdown of economy along with major demographic changes have become a thorn to Thai companies. Although SMEs provide a large chunk of employment to local people, the whole focus has been on Multinational companies. Whereas the SMEs are hit hard by the challenges posed by the aforesaid changes in economy and demography. One of the best way to overcome this hurdle is to look at other economies and going beyond boundaries. Internationalization among small and medium-sized enterprises (SMEs) is a topic of a grown importance, owing to the observed growth effects of globalization, and the demonstrated capacity of SMEs to drive economic development at national, regional, and global levels.

Slangen (2014) had noted that research on SMEs internationalization and relevant strategies are still inconclusive, and a need for further research. Pan and Tse (2000) have emphasized that there are a number of entry mode choices available to firms to enter foreign markets. Prominent among those are export (both direct and indirect), contractual agreements, such a licensing and franchising, joint ventures, acquisitions and wholly owned greenfield investment. The choice of entry is an important strategic decision with substantial bearing on a firm's commitment to resources, risks faced from the host market (Hill et al., 1990), and level of control (Anderson and Gatington, 1986). Moreover, Lu and Beamish (2001) mentioned that by changing the entry mode after initial entry could have a serious negative impact on performance.

Due to differences in institutional settings, export barriers for developed countries could be very different from export barriers in emerging countries. Building on institutional theory developed by North (1990), Scott (1995) and Peng et al. (2008) it was stated that strategic choices, such as export decision, is not just driven by industry conditions and firm capabilities, but also by formal and informal institutional constraints faced by the managers. Formal and informal institutions play a vital role in internationalization decisions as they affect transaction and coordination costs that engage in internationalization (Arslan and Larimo, 2011). Institutional factors affect export propensity and performance, and therefore omitting such factors could seriously limit our understanding about exporting (Gao et al., 2010). Hessels and Parker (2013) maintained that due to smaller size, SMEs are vulnerable to institutional barriers, and emphasized careful considerations of such obstacles to maintain expected growth. Laufs and Schwens (2014) pointed out that foreign market entry mode is likely to be dependent on home country institutional factors. However, linking home country factors with the entry mode decision of SMEs is very rare in cases of emerging markets. For example, in a recent comprehensive survey, Laufs and Schwens (2014) stated that most studies in this area focus on developed markets, and there is a scarcity of detailed analysis for the impact of home country factors on SME entry mode decisions.

2.7 Economic Barriers

Economic Barriers North (1990) defined ‘institution’ as humanly devised constraints that structure political, economic and social interactions. There are formal institutions that include government system, legal procedures etc. and informal institutions that include social and cultural components. Political and legal institutional constraints are part of formal institutions and work as economic barriers for SME internationalization. Politics is the combination of efforts by government, and other bodies and groups, to give future direction to the country - considering the value and interest that people hold - in addition to maintaining governmental and state affairs (Daunton, 2011). Generally, government develops the rules and procedures for day-to-day life through a political and legal framework. Business is considered as the integral part of this daily life, therefore, cannot be conducted against the tide of the political and legal system (Sethi et al., 2012).

How might a political and legal framework influence the business environment? Firstly, the political and legal system of each country directly influences the business environment by amending (or introducing) policies, regulations and laws. Secondly, government determines a fiscal and monetary policy that directly influences the way of doing business. Finally, political stability has a huge and contributing impact on the way business is conducted.

Political forces might assist the internationalization of firms, such as, removing international trade barricades and embargoes, or by setting up export processing zones (EPZ) where the firms can produce and trade under favorable condition. Similarly, certain political and legal factors might become barriers to entering foreign markets, such as, political instability, legal procedural barriers, corruptions and inadequate legal supports (Bhatti and Awais, 2012).

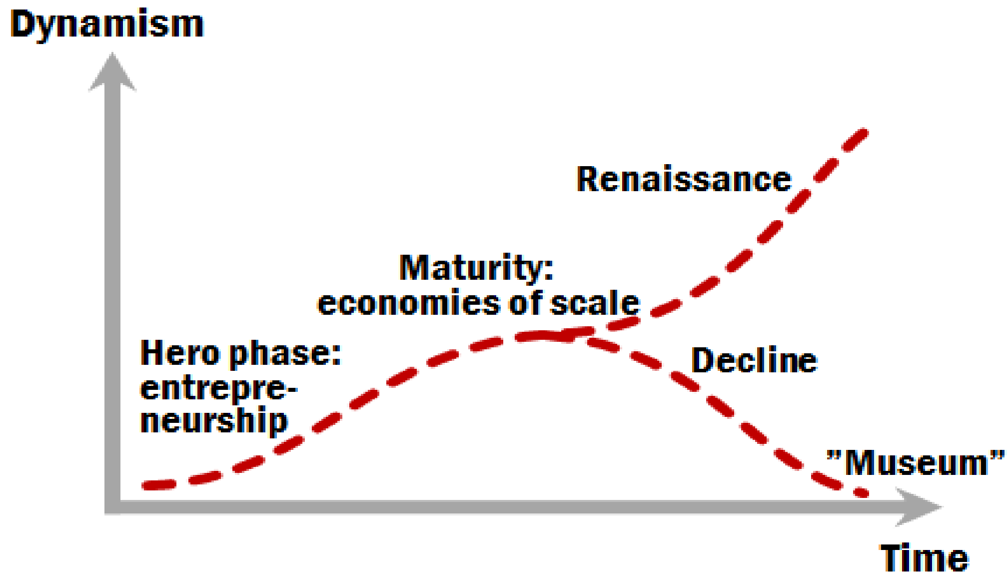
Therefore, the decision to go for international trade expansion should only be taken after understanding the nature of political and legal environment of the target country.

2.8 Social Barriers

The social and cultural environment, which form part of informal institutional dimensions as suggested by North (1990), include the attitudes, tastes, beliefs, behaviors, lifestyle and relationships among the population. Business activities objectively meet the demands of the people, whereas, the demands of the people are based on social needs, functional requirements and cultural aspects. In cases of international business activities, the role of the social and cultural environment is more predominant. By crossing the national boundary through the internationalization process, firms involve themselves with a different culture and society (Gomes et al., 2011, p.238). Although most theories raised these cultural aspects as dominant factor for internationalization (Ellis, 2011), the Uppsala model shed light on the term 'psychic distance'. According to Johanson and Vahlne (1977), psychic distance is "the sum of factors preventing the flow of information from and to the market." Furthermore, they have given such examples as, language, education, culture, political factors, business practices and industrial development as related distances. For Uppsala's model of internationalization, culture is the part of psychic distance. Previous studies collectively identify social and cultural factors as barriers of internationalization including socio-cultural traits, verbal and nonverbal language differences, habits, and attitudinal components of foreign customers and clients (OECD, 2006). Similarly, Barkema and Vermeulen (1997) reported cultural distance as one of the most influential barriers of internationalization. Rothaermel et al. (2006) similarly identified a strong connection between cultural dimension and internationalization.

2.9 SME Cluster life cycle

Every business they start small and then they grow, and SME cluster follows the same trend. SME Cluster life cycle is similar to the development of the industry life cycle in many aspects. As a rule, the stage is described by the age and the growth of the cluster in analogy to the industry life cycle (Enright 2003, Dalum et al. 2005, Maggioni 2002).Audretsch and Feldman (1996) and Pouder and St. John (1996) pointed out that the development of clustered and non-clustered firms differ during different stages of industry development. Clustered firms show better performance at the beginning of the life cycle while they are outperformed by non-clustered firms at the end.



Source: The Green Book (Orjan Solvell: 2003)

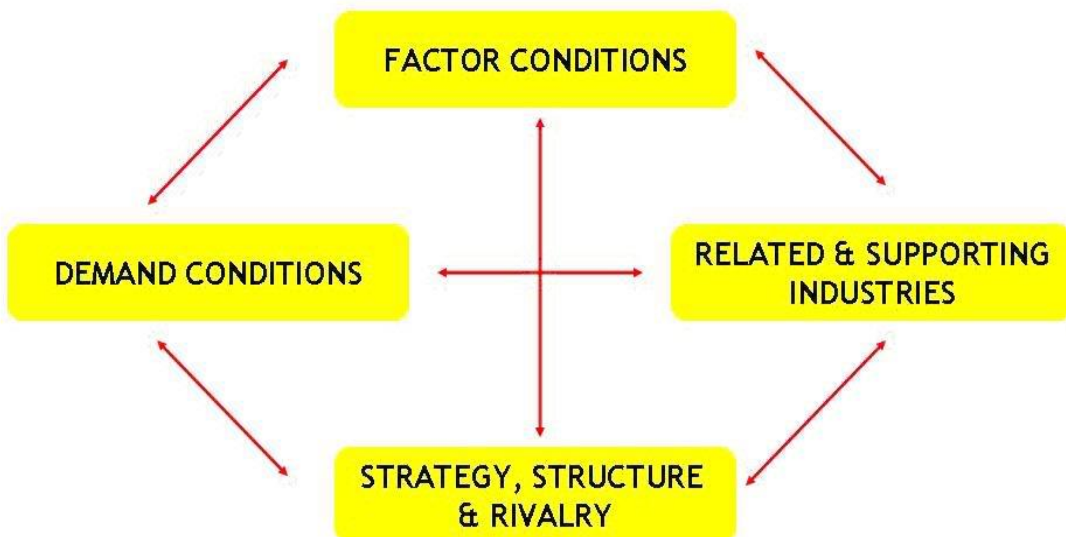
Figure 2.2 Cluster Life Cycle

Green book Solvell, Lindvist, Ketel (2003, 52), Cluster failure is strongly related to lack of consensus, and absence of formulative visions and quantitative target for the clusters. Kerstin

Press (2006) has stated that the euphoria about successful clusters however neglects that historically, many thriving clusters did deteriorate into old industrial areas.

2.10 Porter's Diamond Model

Porter did a four-year research on competitiveness in focusing on10 nations during early 90's, the studies had shown many remarkable examples of the niche industries with the right valuable proposition to specific target market demands from the aggregation of a large number of firms where by their own individual, they would not be able to stand up for the competition. The condition explained by Porter's Diamond model in which represents a relationship and the interaction of the strategy at the national level and the firm level into four driving factors as the "cluster".



Source: Porter (2012)

Figure 2.3 Diamond Model

Porter's diamond model suggests that there are inherent reasons why some nations, and industries within nations, are more competitive than others on a global scale. The argument is that the national home base of an organization provides organizations with specific factors, which will potentially create competitive advantages on a global scale. Porter's model includes 4 determinants of national advantage, which are shortly described below:

a. Factor Conditions

Factor conditions include those factors that can be exploited by companies in a given nation. Factor conditions can be seen as advantageous factors found within a country that are subsequently build upon by companies to more advanced factors of competition. Factors not normally seen as advantageous, such as workforce shortage, can also be seen as a factor potentially strengthening competitiveness, because this factor may heighten companies' focus on automation and zero defects.

Some examples of factor conditions are highly skilled workforce, linguistic abilities of workforce, rich amount of raw materials, workforce shortage.

b. Demand conditions

If the local market for a product is larger and more demanding at home than in foreign markets, local firms potentially put more emphasis on improvements than foreign companies. This will potentially increase the global competitiveness of local exporting companies. A more demanding home market can thus be seen as a driver of growth, innovation and quality improvements. For instance, Japanese consumers have historically been more demanding of electrical and electronic equipment than western consumers. This has partly founded the success of Japanese manufacturers within this sector.

c. Related and Supporting Industries

When local supporting industries and suppliers are competitive, home country companies will potentially get more cost efficient and receive more innovative parts and products. This will potentially lead to greater competitiveness for national firms. For instance, the Italian shoe industry benefits from a highly competent pool of related businesses and industries, which has strengthened the competitiveness of the Italian shoe industry world-wide.

d. Firm Strategy, Structure, and Rivalry

The structure and management systems of firms in different countries can potentially affect competitiveness. German firms are oftentimes very hierarchical, which has resulted in advantages within industries such as engineering. In comparison, Danish firms are oftentimes flatter and more organic, which leads to advantages within industries such as biochemistry and design.

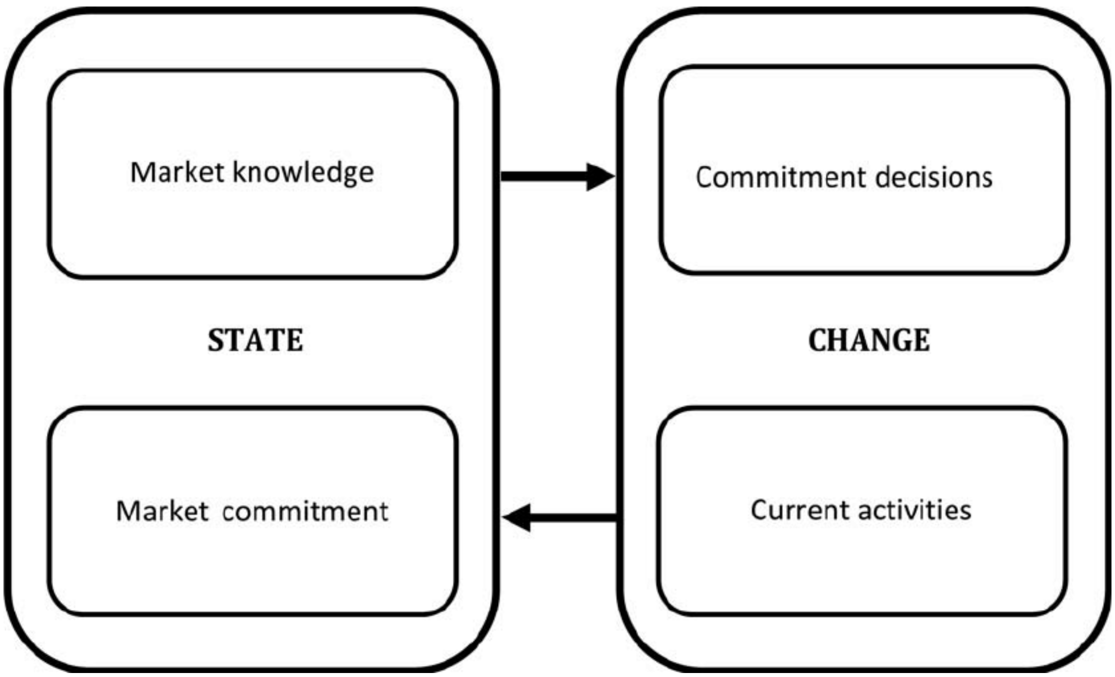
Likewise, if rivalry in the domestic market is very fierce, companies may build up capabilities that can act as competitive advantages on a global scale. Home markets with less rivalry may therefore be counterproductive, and act as a barrier in the generating of global competitive advantages such as innovation and development.

By using Porter's diamond, business leaders may analyze which competitive factors may reside in their company's home country, and which of these factors may be exploited to gain global competitive advantages. Business leaders can also use the Porter's diamond model during a phase of internationalization, in which leaders may use the model to analyze whether or not the home market factors support the process of internationalization, and whether or not the conditions found in the home country are able to create competitive advantages on a global scale.

Finally, business leaders may use this model to asses in which counties to invest and to assess which countries are most likely to be able to sustain growth and development.

2.11 The Uppsala model

Uppsala model is a theory that explains how firms gradually intensify their activities in foreign markets.[1] The key features of Uppsala model are the following: firms first gain experience from the domestic market before they move to foreign markets; firms start their foreign operations from culturally and/or geographically close countries and move gradually to culturally and geographically more distant countries; firms start their foreign operations by using traditional exports and gradually move to using more intensive and demanding operation modes (sales subsidiaries etc.) both at the company and target country level.



Source: Journal of Global Marketing (2012)

Fig 2.4: Uppsala Model

2.12 SME and Competitiveness

Competitiveness is a well-known term in Business and few understand it well. The agony of the competitiveness is that everything matters from production process to infrastructures, from environment to education as well as employee health. Porter (1990) noted that competitiveness can be sustained only through relentless effort to upgrade the standard in the economic regions.

Porter further explained that competitiveness is a never-ending process dealing with lots of different sectors all combined to shape the productivity of a region.

Competitive advantage involves managing the entire value system in compassing the value chains of the firm, suppliers, channels and buyers. The importance of the value system to competitive advantage is manifested by the prevalence of clustering (Porter: 1990). Competitiveness is about the way how production and exchange of goods and services can be made more advanced. Firms' sophistication lies at the heart of competitiveness because the firm is at the level at which wealth is created and competition occurs. However, firms' productivity is inextricable interknit with the environment in which they operate. This is what makes the improvement of competitiveness dependent on the government and other societal institutions (World Bank: 2009).

2.14 Pillars of Competitiveness

There are 12 Pillars of Competitiveness (2009 -2010, World Economic Forum) which has been identified and effects the competitiveness of a region. In line with the well-known economic theory of stages of development, the GCI assumes that, in the first stage, the economy is factor-driven and countries compete based on their factor endowments: primarily unskilled labor and natural resources. Companies compete on the basis of price and sell basic products or commodities, with their low productivity reflected in low wages. Maintaining competitiveness at this stage of development hinges primarily on:

- (pillar 1) well-functioning public and private institutions
- (pillar 2) well-developed infrastructure
- (pillar 3) a stable macroeconomic environment
- (pillar 4) a healthy workforce that has received at least a basic education.

As a country becomes more competitive, productivity will increase and wages will rise with advancing development. Countries will then move into the efficiency-driven stage of development, when they must begin to develop more efficient production processes and increase product quality because wages have risen and they cannot increase prices. At this point, competitiveness is increasingly driven by

- (pillar 5) higher education and training
- (pillar 6) efficient goods markets
- (pillar 7) well-functioning labor markets
- (pillar 8) developed financial markets
- (pillar 9) the ability to harness the benefits of existing technologies
- (pillar 10) a large domestic or foreign market.

Finally, as countries move into the innovation-driven stage, wages will have risen by so much that they are able to sustain those higher wages and the associated standard of living only if their businesses are able to compete with new and unique products. At this stage, companies must compete by producing new and

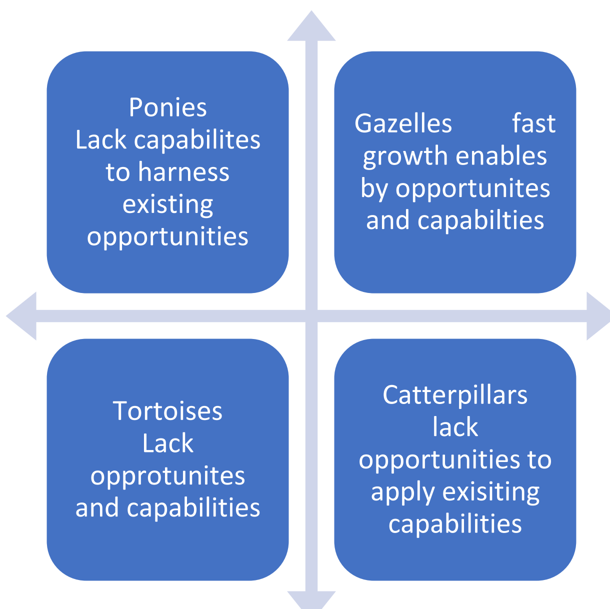
- (pillar 11) different goods using the most sophisticated production processes
- (pillar 12) and through innovation

The GCI takes the stages of development into account by attributing higher relative weights to those pillars that are more relevant for an economy given its particular stage of development. That is, although all 12 pillars matter to a certain extent for all countries, the relative importance of each one depends on a country's particular stage of development. To implement this concept, the pillars are organized into three sub-indexes, each critical to a particular stage of development.

The basic requirements sub index groups those pillars most critical for countries in the factor-driven stage. The efficiency enhancer's sub index includes those pillars critical for countries in the efficiency-driven stage. And the innovation and sophistication factors sub index includes the pillars critical to countries in the innovation-driven stage.

2.15 Typology of SME Growth

Why do some SMEs expand rapidly, while others stagnate? What factors account for the wide variation observed in SME growth trajectories? Clearly, opportunities for profitable business activities shape the ability of an entrepreneur to expand his or her firm. Yet, profitable business opportunities are a necessary but insufficient condition for firm growth (Mead, interview, 2004). To take advantage of business opportunities, entrepreneurs must also possess appropriate capabilities, such as skills, resources, or technology.



Source: (USAID, 2005)

Figure 2.4: Typology of SME Growth

As we can see from the above figure 2.4 provides an overview of how opportunities and capabilities can interact to shape the trajectories of SME growth. This typology presents four "ideal types" of SME growth profiles— distinctions are blurrier in reality, so a particular SMES may not clearly fall into one category. Most prominently, SMEs that demonstrate high, sustained growth rates are frequently termed "gazelles." These highly performing firms typically share two fundamental characteristics—they have profitable business opportunities and appropriate capabilities to harness these opportunities. Only a minority of firms become "gazelles," which drive overall growth in the SME sector.

Some SMEs may face potentially lucrative business opportunities, but be unable to take full advantage of them due to inadequate capabilities. Although these "ponies" may expand quickly for short durations while trying to harness these opportunities, they often lack endurance as they do not have requisite capabilities for sustained growth. For instance, some small honey producers in Brazil initially experienced strong demand for their organic honey in open marketplaces, and hoped to sustain growth by marketing to supermarkets. However, inadequate capabilities inhibited them from achieving this goal because inappropriate technology prevented them from satisfying the formal packaging requirements of supermarkets (Nichter, 2004).